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Cabinet

28

9 December 2015

7 MINISTER OF ENERGY**7.1 RECOMMENDATIONS ON THE NUCLEAR NEW BUILD PROGRAMME (NNBP) FINANCIAL IMPLICATIONS: PROPOSED FUNDING MODEL, RISKS IDENTIFICATION AND MITIGATION STRATEGIES**

(Cabinet memorandum 13 of 2015 dated 8 December 2015, file number E/2/5/9/3, Ministry of Energy. Refer to item 6.1 of the minutes dated 10 June 2015)

7.1.1 The discussion was attended by Messrs T Zulu, Director-General, Z Mbambo, Deputy Director-General from the Department of Energy and L Fuzile, Director-General of the National Treasury.

7.1.2 The Cabinet –

- (a) **requested** that the last sentence of the first paragraph under paragraph 9 be deleted;
- (b) **approved** that the Department of Energy issue the Request for Proposal (RPF) for a Nuclear New Build Programme (NNBP) of 9600 MW of nuclear power;
- (c) **approved** that the final funding model be informed by the response of the market to the RFP and thereafter be submitted to Cabinet for final consideration; and
- (d) **requested** that, where relevant, the exchange rates referred to in the memorandum, be adjusted to current values.

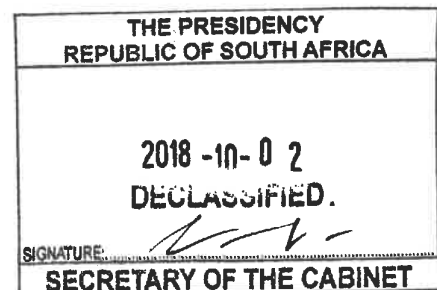
7.2 APPOINTMENT OF CANDIDATES TO SERVE AS MEMBERS OF THE CENTRAL ENERGY FUND ('CEF')

(Cabinet memorandum 12A of 2015 dated 7 December 2015, file number CEF/ba/2015, Ministry of Energy. Refer to item 3.4.4 of the minutes dated 4 November 2015 as well as item 3.3.6 of the minutes dated 19 February 2014)

The **Cabinet approved** the appointment of the following Members to the Central Energy Fund (CEF) Board for a period of 3 years with effect from 10 December 2015 to 9 December 2018, subject to the verification of qualifications and the relevant security clearance:

- (a) Dr X Mkwana (Chairperson);
- (b) Ms M Molope;
- (c) Ms L Mtunzi; and
- (d) Mr M Moagi.

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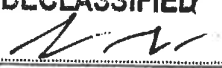
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MINISTRY OF ENERGY

Private Bag X19, Arcadia, 0007

CABINET MEMORANDUM NO: 13 of 2015
DATE : 08 December 2015
FILE NUMBER : E/2/5/9/3

<p align="center">THE PRESIDENCY REPUBLIC OF SOUTH AFRICA</p> <p align="center">2018 -10- 0 2 DECLASSIFIED</p> <p>SIGNATURE: </p> <p align="center">SECRETARY OF THE CABINET</p>
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1 SUBJECT

***Recommendations on the Nuclear New Build Programme (NNBP)
Financial Implications: Proposed Funding Model and Risks
Identification and Mitigation Strategies.***

2 PURPOSE

- 2.1 To report to Cabinet on the progress achieved by the Department of Energy and the National Treasury in developing a proposal and recommendations regarding the Financial Implications; Proposed Funding Model and Risks and Mitigation Strategies , and the Contributions by Countries as contained in the Intergovernmental Agreements

3 SUMMARY

- 3.1 During its seating of the 10th June 2015, Cabinet approved that the Minister of Energy must in consultation with Minister of Finance and Energy Security Cabinet Subcommittee, as matter of urgency submit a memorandum dealing with: (i) The Financial Implications, (ii) The Proposed Funding Model (iii) The Risks and Mitigation Strategies (iv) The contributions by countries as contained in Intergovernmental Agreements.
- 3.2 Several engagements have been held between the Department of Energy and National Treasury in order to consider and discuss matters related to the Cabinet approved Strategic Hybrid Procurement Process, financing and commercial proposals made by vendor countries during three nuclear vendor parade workshops concluded in March 2015 as well as Independent studies for the Cost of nuclear power, Owner Operator Financing structure, Assessment of Financing Options,

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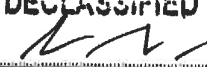
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Economic Impact of Localization for Nuclear New Build Programme commissioned by the Department of Energy.

- 3.3 The two Departments have developed recommendations covering the Nuclear New Build Programme Financial Implications; proposed Funding Model, and Risk Identification and Mitigation, for the consideration of Cabinet.

4 STRATEGIC FOCUS OF THE MEMORANDUM

- 4.1 South Africa's vision for nuclear power is based on the Nuclear Energy Policy of 2008 that provides a framework within which; prospecting, milling, mining, the use of nuclear materials and the development and utilisation of nuclear energy for peaceful purposes is to take place. Some of the key government objectives for the nuclear new build programme include: (a) Attainment of global leadership and self-sufficiency in the nuclear energy sector in the long term; (b) Contribution to the country's national programme of social and economic transformation, growth and development; and (c) Improvement of the quality of human life and to support the advancement of science and technology.
- 4.2 In March 2011, Cabinet approved a 20 year Integrated Resource Plan (IRP2010-30), Government's electricity plan that is currently being implemented, providing for an energy mix that allocates a nuclear capacity of 23% (9600MW) by 2030. In accordance with this plan it is intended that the first unit will be commissioned by 2023.
- 4.3 The National Development Plan (NDP), approved in 2012 enjoins us to conduct thorough investigations on various aspects of the Nuclear New Build Programme (NNBP) before a procurement decision is taken. In line with this policy prescript Government undertook detailed studies on various aspects of the nuclear fuel cycle value chain, including amongst other, costs, financing, funding model, skills development, and economic impact of localisation.
- 4.4 Guided by the relevant policy framework mentioned above, Government has undertaken various activities which have placed the country in a position where the procurement phase of the NNBP is now ready to proceed.
- 4.5 During its seating of the 10th June 2015, Cabinet was presented with four memoranda which covered; (i) the Inter-Governmental Framework Agreements, (ii) the pre-procurement phase, (iii) the proposed Nuclear New Build Procurement Process and (iv) State of Readiness to Implement Nuclear New Build Programme.
- 4.6 Prior to opening the procurement phase of the NNBP, Cabinet instructed that the Department of Energy look into financing matters jointly with National Treasury. This Cabinet memorandum provides feedback following engagements between the two Departments.

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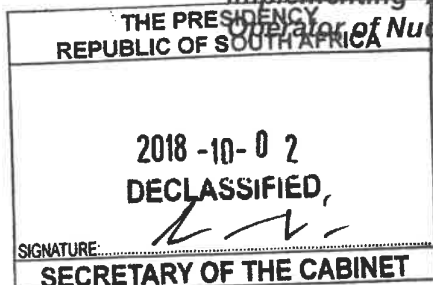
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- 4.7 Several meeting engagements have been held between the two Departments in order to engage on matters that relate to; (a) the Cabinet approved Strategic Hybrid Procurement Process, (b) financing and commercial offerings by vendor countries during three nuclear vendor parade workshops concluded in March 2015, (c) the financial implications of the NNBP, (d) the proposed funding model for the NNBP, (e) the risks identification and mitigation for the NNBP and (f) independent studies commissioned by the Department of Energy.

5 DISCUSSION

- 5.1 During its seating of the 10th June 2015, Cabinet instructed the Department of Energy (DoE) in consultation with National Treasury (NT) to develop a recommendation in the form of a Cabinet Memorandum dealing with (i) the Financial Implications, (ii) the proposed Funding Model (iii) Risks and mitigation strategies (iv) the contributions by countries as contained in the Intergovernmental Agreements.
- 5.2 A Joint Task Team, headed by Directors General of the DoE and NT and made up of members of the two Departments was established and its first meeting took place on 24 July 2015. To date, a total of eight engagements were held: 24 July, 7, 12, 20, 25, 28 August, 3 and 8 September 2015. Representatives from Nuclear SOE's (Eskom, NECSA and National Nuclear Regulator) were also called upon for support.
- 5.3 During these meetings, the two Departments considered the following: (a) the Cabinet approved Strategic Hybrid Procurement Process, (b) financing and commercial offerings by vendor countries during three nuclear vendor parade workshops concluded in March 2015, (c) the financial implications of the NNBP, (d) the proposed funding model for the NNBP, (e) the risks identification and mitigation for the NNBP and (f) independent studies commissioned by the Department of Energy amongst others.
- 5.4 The two Departments propose the following recommendations to Cabinet:
- 5.4.1 Funding Model in order to manage the economic impact as a result of implementing the NNBP, a model that takes into account multiple country objectives is attached as **Annexure A**.
- 5.5 South Africa is the member of the BRICS grouping of nations. It is important to note that the Department has put the Nuclear New Build Programme funding application to the BRICS Bank as a possible source of funding this infrastructure programme. This is expected to mitigate the funding impact on the fiscus.
- 5.6 Regarding structures relevant for the implementation of the NNBP the following is also noted:
- 5.6.1 Cabinet has made the following decisions: The **Procuring and Implementing Agency** for the NNBP is the DoE while the **Owner** of **Nuclear Power Plants** is Eskom.



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- 5.6.2 The DoE is in the process of establishing and operationalising the Programme Management Office (PMO) under which the procurement process for the NNBP would be undertaken. The PMO is the relevant structure for overseeing that the NNBP is implemented in line with the approved strategies of the Energy Security Cabinet Subcommittee.
- 5.6.3 Capacity building within DoE and its nuclear entities is required to implement the NNBP. A Medium Term Expenditure Framework (MTEF) process to secure funds has been started and is on-going. Initial funding estimates for the structures to deliver on the expected NNBP objectives under the MTEF period is **R6 bn**.

6 IMPLEMENTATION PLAN

The PMO will, amongst other things, produce a programme implementation plan that will cover the following:

Procurement:

The following procurement governance committees will be put in place and operationalised:

Bid Specification, Bid Evaluation, Bid Adjudication, and, finalisation of the feasibility study on the procurement specification and implementation of the NNBP.

Siting:

Conclude the site readiness activities. Obtain site related permis. Securing pieces of land. Transmission integration.

Long lead items:

Identify and procure long lead items.

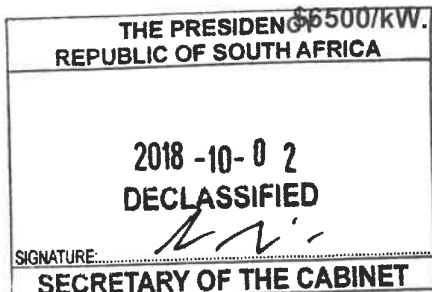
7 ORGANISATIONAL AND PERSONNEL IMPLICATIONS

The Department of Energy has established and is operationalising the PMO in response to initially undertaking the NNBP procurement process. Any resultant personnel movements between SOE's both in the short and medium term will be managed within existing legislation while mitigating any associated risks.

8 FINANCIAL IMPLICATIONS

Initially for the MTEF period, an amount of **R6 bn** is envisaged in order to effect organisational readiness for the Department of Energy and its nuclear related entities to be well capacitated to manage the NNBP implementation (operational cost).

The experience in Asia shows a nuclear power overnight cost of as low as **\$2500/kW**, whilst the IRP-2010-30 estimates an upper limit of **\$6500/kW**. Utilising these numbers, the total cost for the **9600 MW**

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programme ranges between **R240 bn (\$2500/kW)** and **R624 bn (\$6500/kW)**.

National Treasury has modelled two scenarios that take firstly an aspirational figure of **\$5000/kW** which translates into **R480 bn** for the **9600 MW** and secondly the upper limit of **\$7500/kW** which translates into **R720 bn**.

The **9600 MW** fleet can be constructed in a phased manner, constructing two units at a time, while still maintaining the envisaged programme benefits (such as self-sufficiency, socio-economic benefit, advancement of research and development, mining and beneficiation of strategic mineral like uranium, manufacturing, etc.). The cost of constructing two units in a phased manner, with a capacity of **2400 MW** at a time will range between **R60 bn (\$2500/kW)** to **R156 bn (\$6500/kW)**.

The above scenarios are summarised in the table below.

	Experience-based Overnight Cost		National Treasury Modelled scenarios Overnight Cost Assumptions		
Programme size	\$2500/kW	\$6500/kW	\$2500/kW	\$5000/kW	\$7500/kW
9600 MW	R240 bn	R624 bn	R240bn	R480 bn	R720 bn
2400 MW	R60 bn	R156 bn	R60bn	R120 bn	R180 bn
* Assumed exchange rate is one dollar to 10 rands.					
** Overnight cost – the cost without any interest charges and other impacts.					

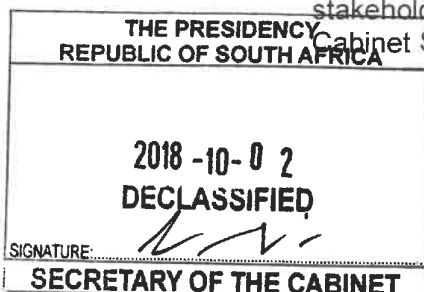
Except for a few outliers, world experience in nuclear new build programmes is within \$2500/kW to \$6500/kW. It is the intention to keep the overnight costs of the South African nuclear new build programme within this range.

9 COMMUNICATION IMPLICATIONS

The worst case programme cost scenario should not be part of our communication strategy. Prices should not be communicated prior to the procurement process being complete in order to enable Government to achieve better pricing during this period. If any communication has to be done around the costs of the programme, it is better to talk about the low end of the range, whilst referencing where that price is applicable.

The NNBP has a dedicated long term nuclear communications and stakeholder engagement strategy under review in the Energy Security Cabinet Subcommittee structures. The strategy covers a broad range of

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communication tools to reach South Africans from all levels and ensure that the message about demystifying nuclear energy and benefits of implementing the NNBP is disseminated equitably.

10 CONSTITUTIONAL IMPLICATIONS

None.

11 IMPLICATIONS FOR VULNERABLE GROUPS

The involvement of South African companies and institutions in Nuclear New Build Programme will create industry and directly present jobs and business opportunities for designated groups and other previously disadvantaged groups.

12 SECURITY IMPLICATIONS

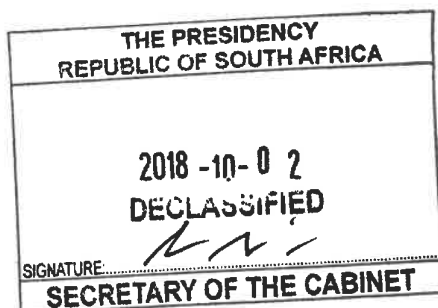
Due to commercial sensitive and intellectual property concerns, especially before the conclusion of the procurement process, relevant steps are taken to safeguard information related to the NNBP.

13 DEPARTMENTS AND PARTIES CONSULTED, RESPONSES AND COMMENTS

- 13.1 The NNBP implementation is still being conducted with the participation and consultation of various Government Departments and State Owned Companies. Department of Energy has consulted with National Treasury, NECSA, Eskom and National Nuclear Regulator.

14 RECOMMENDATIONS

- 14.1 It is recommended that:
- 14.2 The Cabinet approves that Department of Energy should issue the Request for Proposal (RPF) for Nuclear New Build Programme of 9600MW of nuclear power.
- 14.3 The final funding model will be informed by the response of the market to the RFP and be submitted to Cabinet thereafter for final approval and implementation.

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15 OFFICIAL RESPONSIBLE FOR THE MEMORANDUM

I declare that the memorandum adheres to the Guidelines dated November 2012 provided by the Cabinet Secretariat for the drafting of memoranda. The requirements in relation to electronic presentations were noted.

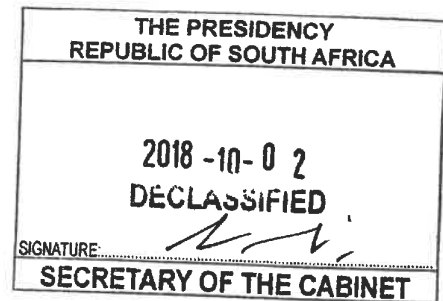
Name: Mr Zizamele Mbambo
 Designation: Deputy Director General: Nuclear
 Telephone: 012 406 7664
 Cellular: 079 529 5646
 E-mail: Zizamele.mbambo@energy.gov.za

16 HEAD OF DEPARTMENTS

Mr Thabane Zulu
 Director-General: Energy

Signature.....


Date... 08/12/2015



17 AUTHORISATION FOR PROCESSING THE MEMORANDUM

Ms Tina Joemat-Pettersson, MP
 Minister of Energy


Signature.....


Date... 08/12/2015


Is there a need for an electronic presentation to be done in addition to the memorandum? Yes

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2018/10/02



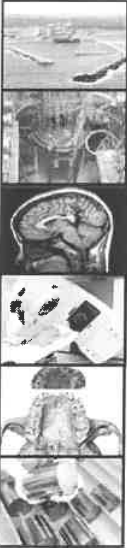
Presented by
Ministry of Energy
&
Energy Security Cabinet
Subcommittee
to
CABINET
9 December 2015
Union Building, Pretoria



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Cabinet Decision

- During the seating of 10 June 2015, Cabinet
- **approved** that the Minister of Energy must, in consultation with the Minister of Finance and the Energy Security Cabinet Sub-Committee , as a matter of urgency submit a memorandum dealing with –
 - i. the financial implications;
 - ii. the proposed funding model;
 - iii. the risks and mitigation strategies; and
 - iv. the contributions by countries as contained in the Inter-Governmental Agreements.
- **approved** that South Africa should proceed with the procurement of the 9.6GW of nuclear power plants to realise its self-sufficiency policy objective



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OPENING REMARKS AND OBJECTIVES


1. To appraise Cabinet on the work and progress made by the Department of Energy and National Treasury with regards to Funding Model of Nuclear New Build Programme in response to Cabinet directive
2. To appraise Cabinet about benefit of nuclear to provide long term electricity solution as presented in the Cabinet endorsed Integrated Resource Plan 2010-2030.
3. To seek Cabinet approval of the Funding Model recommendation and to allow the Department of Energy to issue the Request for Proposal (RFP)



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AFRICAN COUNTRIES PLANNING TO EMBARK ON NUCLEAR NEW BUILD

Summary of Anticipated Nuclear Units

Name of Country	MWe (nuclear)	Year
Algeria	1200	2022
	2400	2027
Egypt	900-1650	2020-2026
Ghana	400-1000	2020-2025
Kenya	4000	2020-2030
Nigeria	1000-4000	2020-2030
Morocco	2000	2020
Sudan	4000	2030




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SOUTH AFRICA NUCLEAR LEADERSHIP ROLE AND SUPPORT TO THE AFRICAN CONTINENT


24 IAEA Fellows (including 7 women) from 9 African countries are receiving training in South African Institutions.

Countries: Namibia, Nigeria, Lesotho, Botswana, Zimbabwe, Uganda, Tanzania, Zambia and Ghana

Fields of Study: Primarily Nuclear Medicine but also Medical Imaging, Clinical Oncology, Radiation Oncology, and Plant Breeding & Genetic


Institutions: Wits University, UCT, Steve Biko Academic Hospital, Medunsa, Stellenbosch University, Agricultural Research Council, Tygerburg Hospital, CPUT, and Groote Schuur Hospital

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The 2030 Shortfall

Total expected demand by 2030	61 200 MW*
Current Nominal Capacity	43 500 MW
Current Eskom generation capacity	42 000 MW
Imports from Cahora Bassa	1 500 MW
Add:	17 880 MW
Current new build – Medupi/Kusile/Ingula	10 932 MW
Other new build	315 MW
Renewable Energy Independent Power (REIPP)	5 243 MW
Co-generation	1 390 MW
Less:	(26 100 MW)
Breakdowns (current 2015 levels)	(11 300 MW)
Projected decommissioned plants by 2030	(14 800 MW)
Total projected capacity by 2030:	35 280 MW
(43 500 - 17 880 - 26 100)	
Total projected shortfall using these assumptions:	25 920 MW

*Note: Per 2013 Update Base Case total projected installed nominal capacity will be 61 350 MW (See Table 2) with expected peak demand 60 509 MW (comparable to 61 200 MW).

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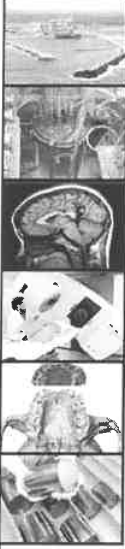
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NUCLEAR ARGUMENTS

AGAINST

- There are three main arguments against nuclear:
- Safety – Disasters at Three Mile Island, Chernobyl and Fukushima but less than 60 deaths in total (all at Chernobyl). At Fukushima, no one died but 20 000 died in the tsunami/earthquake.
- Nuclear Waste – but it does not just get dumped anywhere. The safety protocols are rigorous
 - A 1 000 MW nuclear power station produces about 27 tons of high-level waste per year, a 1 000 MW coal-fired power station will produce about 850 000 tons of ash in the same time. Nuclear waste is stored deep underground, while ash and other harmful gas from burning fossil fuel remains in the environment.
- Construction cost – A new nuclear build is more expensive than other forms of generation.


While Renewable Energy is becoming an increasingly vital part of the power mix it won't be able to address South Africa's baseload needs (without access to meaningful hydro).



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NUCLEAR ARGUMENTS continued

FOR

- The four main benefits of nuclear power would be:
- Environmental considerations – to limit global temperature increases to just 2°C by the end of the century, a halving of energy-related emissions is needed by 2050 and South Africa's baseload options are essentially coal or nuclear
- Reliability – nuclear power stations tend to run very reliably with strict adherence to maintenance programmes and monitoring procedures
- Ability to operate independently of fresh water – (unlike South African coal-fired power stations)
 - Medupi upon completion would require around 17 billion litres of fresh water per year to be consumed almost entirely (less than 10% of this amount would be recycled) compared to Koeberg which saves 22 billion litres of fresh water per year because it uses sea water.
- Low operating cost over the lifetime of the plant – In the second half of its life the cost of producing nuclear power is lowest compared to other forms of electricity. Koeberg is Eskom's most efficient and most profitable power station operating today.
 - 2014 Operating cost: Coal - R192/MWh, Nuclear - R34/MWh, and Open Cycle Gas Turbine - R2886/MWh (nearly R10billion per year spent on diesel). Koeberg currently cross-subsidises coal generation.



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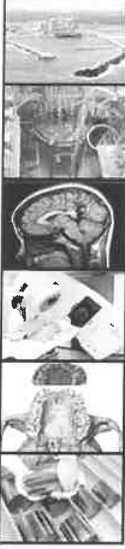
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Economic Investment - increased economic activity

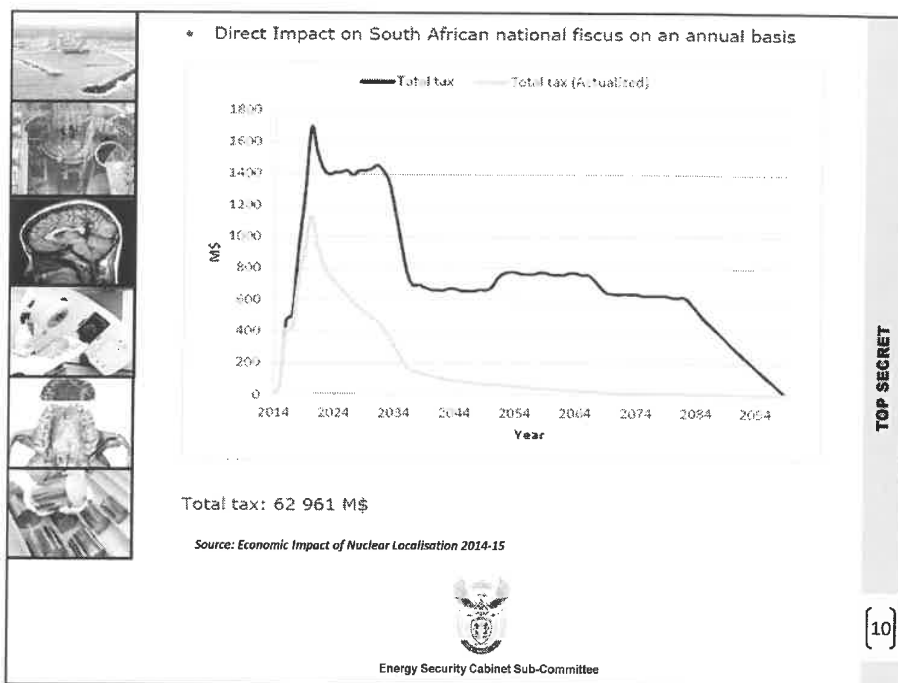
- Contribute positively to GDP **R40 billion** per annum during construction, and **R5 billion** during operation phase.
- Contribute positively to Fiscus – net positive return even with incentives
- Indirect effect on economy from low cost, reliable baseload electricity of nuclear is logically positive but cannot be easily assessed.
- *Dr Dawie Serfontein from UNW has estimated that nuclear new build programme is a R650-billion investment that will generate R54-billion profit each year for 60 years in a row. Thus our R650-billion investment is going to produce a total return of R3.2-trillion for South Africa*

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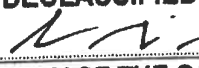
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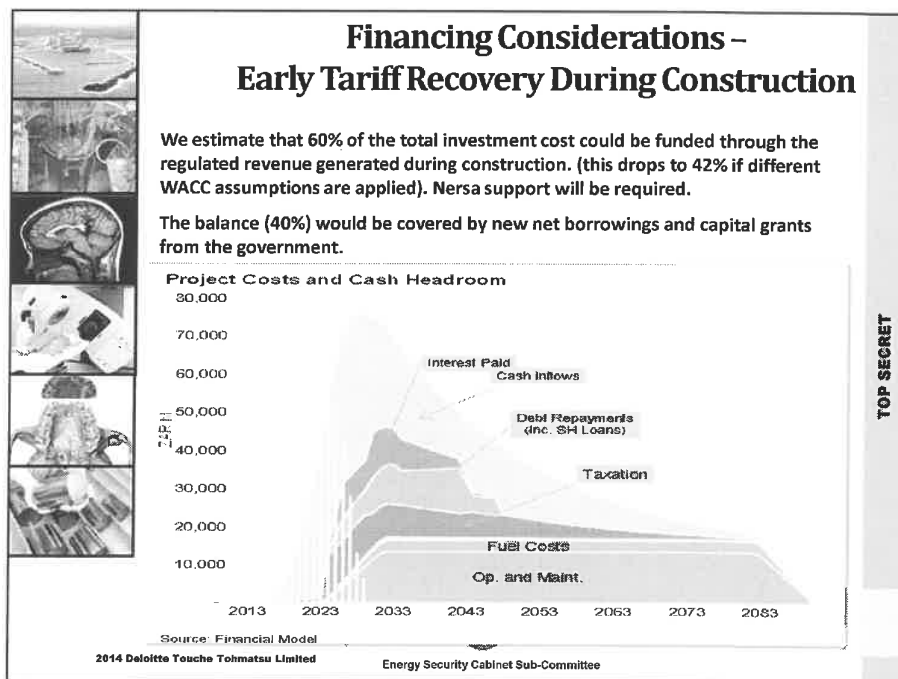
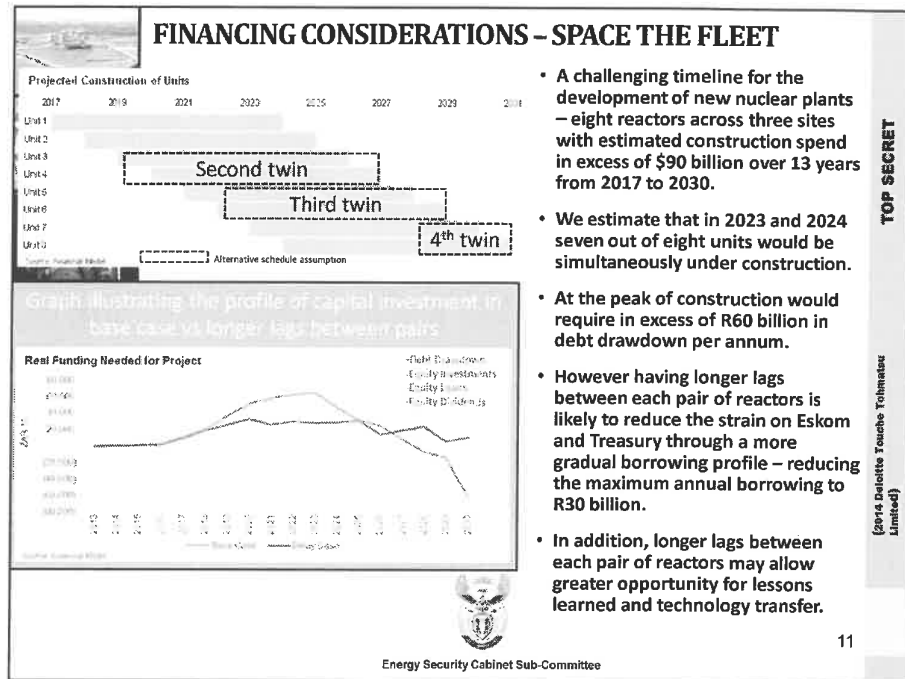
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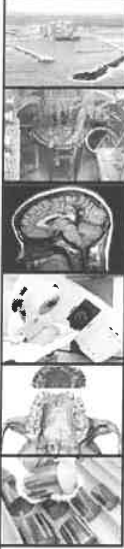
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FUNDING MODEL - SCOPE

The following elements of the funding model and their attendant risks need to be engaged holistically in designing the financial programme supporting the investment:

- Investment cost of the build programme
- Impact on the electricity tariff path
- Costs of developmental and ancillary objectives
- Financing structures, contracting models and procurement processes
- Macroeconomic impacts
- Fiscal context and consequences


The constitutional, legal and regulatory framework will interact with and influence the funding model. This has not been fully addressed in the preliminary report.



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FUNDING MODEL – Financing Sources & Instruments

- The use of different financing structures (corporate finance / project finance) does not have a significant direct impact on the costs. However, it may have important implications for how risk is managed and mitigated to ensure that incentives are aligned to an efficient outcome. Government therefore should be open to considering different structures.
- Export Credit Agency (ECA) financing is likely to be the most cost-effective source to make up the bulk of the debt financing.
- Reliance on ECA financing will limit the extent of localisation as vendor countries seek to support their own exports. As the level of localisation increases, debt financing will increasingly need to be obtained from other sources, including the capital markets, commercial banks and multilaterals.
- Most of the debt financing will be foreign denominated, resulting in an exposure to a depreciation in the exchange rate. Where appropriate local financing should be encouraged.
- Local currency debt, hedging, insurance or other instruments to fully mitigate financial risks may not be available or the costs may be prohibitively high; reinforcing the need for government to limit the size of the initial commitment to retain flexibility to manage this risk.



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FUNDING MODEL – Fiscal Scenarios

- Full 9.6 GW programme and a smaller initial commitment of 2.4GW modelled
- Scenarios were then constructed in which the cost of the programme (\$/kW) and long run rate of economic growth are varied.
- The intention of the scenarios is to given an indication of the range of possible outcomes.

SCENARIO	COST	ECONOMIC GROWTH
A Low cost, Moderate growth	The cost of the programme is very low (\$5000/kW)	Economic growth returns to its long run average, between 3 and 4 per cent per annum
B Low cost Low growth	The cost of the programme is very low (\$5000/kW)	Economic growth remains at current Reserve Bank estimates of potential output growth (2-3 per cent) over the life of the programme.
C Cost overrun Moderate growth	Cost overruns are 50% resulting in a \$7500/kW cost	Economic growth returns to its long run average, between 3 and 4 per cent per annum
D Cost over run, Low growth	Cost overruns are 50% resulting in a \$7500/kW cost	Economic growth remains at current Reserve Bank estimates of potential output growth (2-3 per cent) over the life of the programme.

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FUNDING MODEL – Fiscal Scenarios

Full 9.6 GW programme and a smaller initial commitment of 2.4GW modelled.
 Profile of Fiscal Commitments (debt, nuclear debt, guarantees as % of GDP)
 9 600 MW programme 2 400 MW programme (Phase 1)
 Overnight cost of USD5000/kW

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FUNDING MODEL


- Initially for the MTEF period, an amount of **R6 bn** is envisaged in order to effect organisational readiness for the Department of Energy and its nuclear related entities to be well capacitated to manage the NNBP implementation (operational costs)
- The experience in Asia shows a nuclear build cost of as low as **\$2500/kW**, whilst the **IRP-2010-30** estimates an upper limit of **\$6500/kW**.
- Utilising these numbers, the total cost for the 9600 MW programme ranges between **R240 bn (\$2500/kW)** and **R624 bn (\$6500/kW)**.
- National Treasury has modelled two scenarios that take firstly an aspirational figure of **\$5000/kW** which translates into **R480 bn** for the 9600 MW and secondly the upper limit of **\$7500/kW** which translates into **R720 bn**.



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FUNDING MODEL

- The 9600 MW fleet can be constructed in a **Phased Approach**, constructing two units at a time, while still maintaining the envisaged programme benefits (such as self-sufficiency, socio-economic benefit, advancement of research and development, mining and beneficiation of strategic mineral like uranium, manufacturing, etc.).
- The cost of constructing first two units in a **Phased Approach**, with a capacity of **2400 MW** as **Phase 1** will range between **R60 bn (\$2500/kW)** to **R156 bn (\$6500/kW)**.
- The construction of **phase 2** (next two units) will be **subject to supplier performance to meet specified contract conditions agreed upon during procurement negotiations**.
- It is important for South Africa to implement to full programme to benefit from the economies of scale (**with an expected 30% reduction on cost**).
- It is important to note that the actual price can only be determined by starting the procurement process and testing the market.
- The above scenarios are summarised in the next slide:




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FUNDING MODEL					
Programme size	Experience-based Overnight Cost		National Treasury Modelled scenarios Overnight Cost		
	\$2500/kW	\$6500/kW	\$2500/kW	\$5000/kW	\$7500/kW
9 600 MW (Full Programme)	R240 bn	R624 bn	R240 bn	R480 bn	R720 bn
2 400 MW (Phase 1)	R60 bn	R156 bn	R60 bn	R120 bn	R180 bn


* Assumed exchange rate is one US dollar to 10 rands
 ** Overnight cost – the cost without any interest charges and other impacts.

Except for a few outliers, world experience in nuclear new build programmes is within \$2500/kW to \$6500/kW. It is essential to keep the overnight costs of the South African nuclear new build programme within this range.

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FUNDING MODEL - SUMMARY	
	<ul style="list-style-type: none"> The elements of the funding model that were considered in this report with National Treasury, include: <ul style="list-style-type: none"> A ring-fenced special-purpose vehicle financing structure the project (i.e. a project finance, not corporate finance approach) Equity amounting to 30% of the project cost is provided by government, financed by issuing bonds The remaining 70% is financed as far as possible by ECA-backed debt Government guarantees all debt issued by the SPV Debt is repaid through tariff with increases taking place on commissioning so that all financing can be repaid over a 20 year period, following which tariffs reduce to cover operational costs only.


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Strategic Decisions Impacting on Funding Model


- The modelling of fiscal implications was done in terms of the funding model summarised on the previous slide. However, a number of strategic decision points would affect the parameters of the model substantially.
- Each of these needs to be considered in further detail:
 - **Tariff path:** raising tariffs early would reduce fiscal costs by shifting some of the burden to electricity consumers.
 - **Phased or once-off commitment:** Should government commit in advance to the full 9.6GW, or make commitments in a phased manner?

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Strategic Decisions Impacting on Funding Model

- **Corporate or project finance:** Should the project be financed on the balance sheet of Eskom or another large state entity, or is the ring-fenced SPV approach preferred?
- **Equity partner:** Should government go-it-alone as an equity contributor or should an equity partner, prepared to share in the financial reward and risk of the project, be included?
- **Localisation and ECA-backed finance:** Vendor financing is cheaper and on easier terms, but limits the extent of localisation since vendors seek to promote their exports.
- **Affordability limits:** What limits should trigger a rethink of affordability and what range of variables should be included in "stop-go" decision making (e.g. exchange rate, economic growth, interest rate, construction cost, lead times, localisation performance...)

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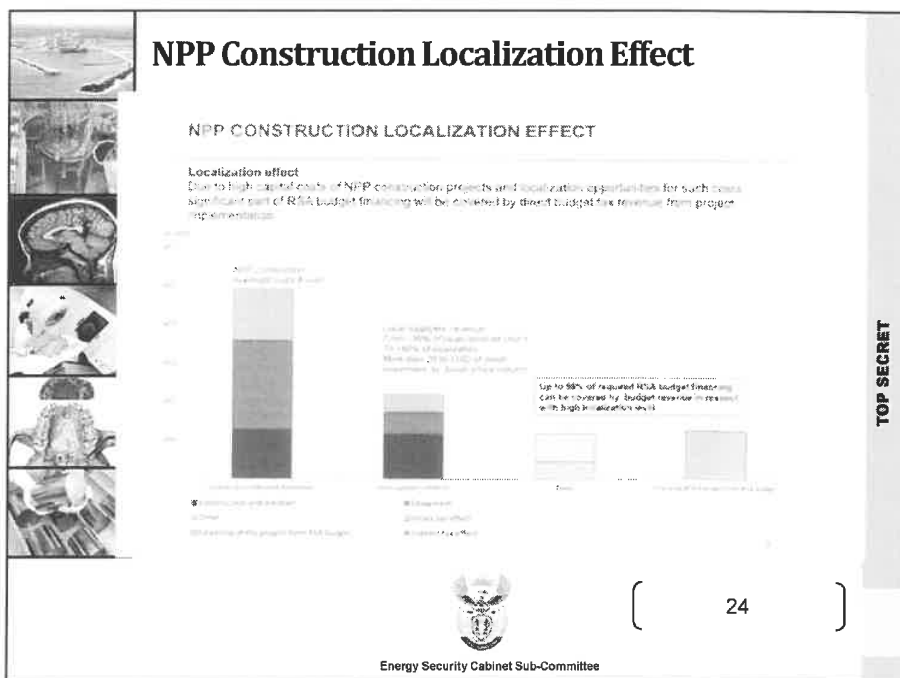
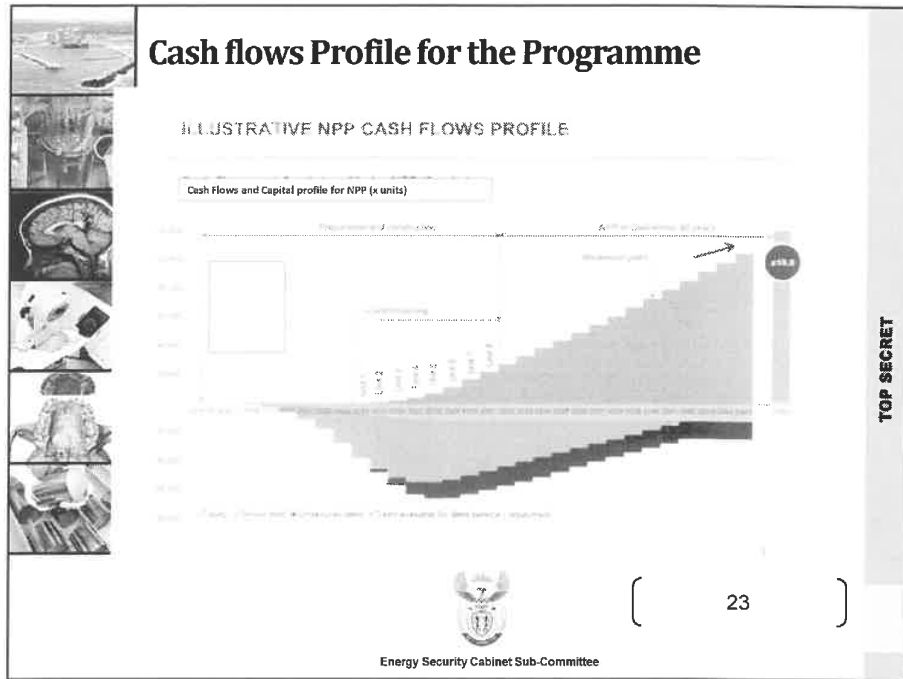
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Cabinet

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31 August 2016

5 MINISTER OF FINANCE**5.1 BRIEFING ON THE FINANCIAL AND FISCAL COMMISSION (FFC)**

(No document)

5.1.1 The **Minister of Finance** made the Cabinet aware of concerns with regard to integrity matters related to certain individuals.

5.1.2 The **Cabinet noted** that the Minister of Finance would be providing a detailed briefing on the above matter in due course.

5.2 CREDIT RATING AGENCIES(No document. Refer to [item 5.1](#) of the minutes dated 8 June 2016)

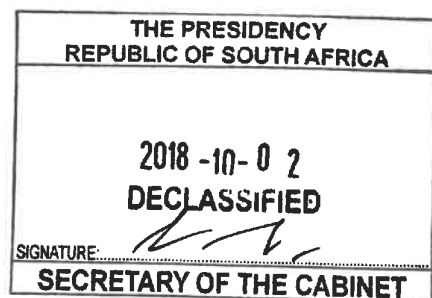
5.2.1 The **Minister of Finance** reminded the Cabinet that the credit rating agencies would be returning to South Africa to review and assign the relevant credit rating during September, November and December 2016.

5.2.2 The **Cabinet noted** the briefing by the Minister of Finance.

5.3 APPOINTMENT AND RE-APPOINTMENT OF DIRECTORS TO THE BOARD OF SOUTH AFRICAN AIRWAYS SOC LIMITED (SAA)(Cabinet [memorandum 5](#) of 2016, dated 24 August 2016, file number M2/1/35, Ministry of Finance. Refer to [item 8.1](#) of the minutes dated 22 October 2014)The **Cabinet -**

(a) **approved** the appointment of a permanent Board comprising of the following twelve non-executive directors to the Board of South African Airways (SAA) for a period of three years from 1 September 2016 to 31 August 2019, subject to annual review:

- (i) Ms D Myeni;
- (ii) Ms T Ramano;
- (iii) Ms BS Tshabalala;
- (iv) Ms T Mgoduso;
- (v) Ms N Moola;
- (vi) Mr AH Moosa;
- (vii) Ms G Sepamla;
- (viii) Mr S Buthelezi;



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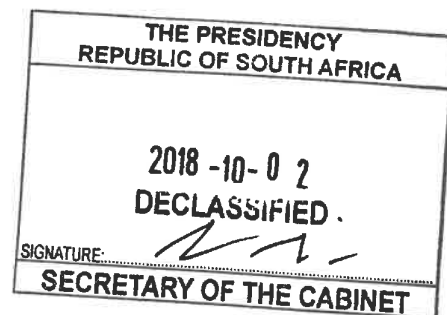
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31 August 2016

- (ix) Mr PH Maluleka;
- (x) Mr M Malunga;
- (xi) Dr M Mbatha; and
- (xii) Mr P Tshisevhe;
- (b) **approved** that Ms D Myeni be re-appointed as Chairperson of the board for a period of 1 year with a view to ensuring continuity and a seamless transition for the newly appointed board and Deputy Chairperson;
- (c) **approved** that Ms T Ramano be appointed as the Deputy Chairperson of the board for a period of three years from 1 September 2016 to 31 August 2019 subject to annual review; and
- (d) **noted** that the new board would be tasked to work on measures to be implemented with a view to placing SAA in a stronger position in terms of governance and improving the likelihood of possible financial recovery and **approved** that Cabinet be briefed in due course.



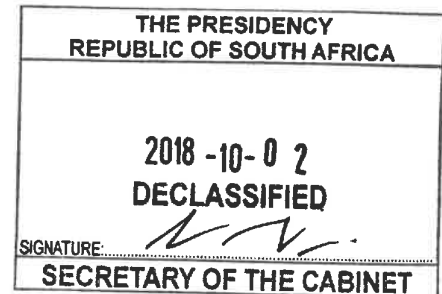
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MINISTRY OF FINANCE



CABINET MEMORANDUM NO : 5 of 2016
DATE : 24 August 2016
FILE NUMBER : M2/1/35

1. SUBJECT

Appointment and re-appointment of Directors to the Board of South African Airways SOC Limited (SAA) as part of the strategic package for the successful turnaround of the airline

2. PURPOSE

2.1 To request Cabinet to consider and approve the following interventions required for the successful turnaround of SAA:

- 2.1.1 Appointment of twelve non-executive directors (Ms Bajabulile Swazi Tshabalala, Ms Thandeka Mgoduso, Mr Stavros Nicolaou, Ms Nazmeera Moola, Mr Akhter Hoosen Moosa, Ms Gugu Sepamla, Mr Siphile Buthelezi, Mr Peter Holmes Maluleka, Mr Mzimkulu Malunga, Dr Martha Mbatha, Ms Tryphosa Ramano and Mr Peter Tshisevhe) to the Board of SAA for a period of three years from 01 September 2016 to 31 August 2019, subject to annual review.
- 2.1.2 Appointment of the current Chairperson of the Board (Ms Duduzile Myeni) as non-executive director and Chairperson of the Board of SAA for a period of two years from 01 September 2016 to 30 September 2018, subject to annual review.
- 2.1.3 Appointment of one of the non- executive directors (Ms Tryphosa Ramano) as the Deputy Chairperson of the Board for a period of three years from 01 September 2016 to 31 August 2019, subject to annual review.
- 2.1.4 A package of further measures to be implemented to place SAA in a stronger position in terms of governance and improve the likelihood of possible financial recovery.

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3. SUMMARY

- 3.1 The financial health of the state owned company (SOC) portfolio has been highlighted as one of the major risks to South Africa's ability to deliver on its fiscal targets and hence for the sovereign credit rating over the medium term. To continue to operate, the airline is dependent on support from government and has requested a further R4.756 billion government guarantee. It would not be prudent for government to support the airline, without first mitigating the fiscal risk.
- 3.2 As a first step, it is proposed that the current Chairperson of the Board and an additional twelve new non-executive directors be re-appointed/appointed respectively, subject to annual review. The Board appointment is done in terms of Section 13.1 of the Memorandum of Incorporation (MOI) which states that the Board shall consist of minimum of five directors and maximum of fifteen directors, who are to be appointed by the Minister in consultation with Cabinet. Furthermore, the MOI states that the shareholder should ensure that the Board comprises of Executive Directors (EDs) and Non-Executive Directors (NEDs) and with no less than two EDs, being the Chief Executive Officer (CEO) and Chief Financial Officer (CFO).
- 3.3 Once appointed the Board will be tasked with implementing the following package of actions: appointing the CEO, CFO and other key executives; strengthening SAA's strategy to accelerate the turnaround of the airline and ensure alignment with the other state owned airlines; ensuring SAA secures funding to meet its liquidity requirements; putting in place the Air Traffic Liability guarantee; and considering providing additional government support to the airline.

4. STRATEGIC FOCUS OF THE MEMORANDUM

The aim is to strengthen SAA and government's airline businesses so that they can make a more meaningful and impactful contribution towards connecting South Africa to the continent and the continent to the world without posing any risk to the already pressurised public purse.

5. DISCUSSION

- 5.1 SAA has made some progress toward a turnaround. During the 2014/15 financial year the company implemented the 90-day Action Plan, to deliver R1.1 billion of savings. SAA's management accounts indicate that the airline has realised a provisional net loss of R1.8 billion for 2015/16 (about R400 million worse than budget) but considerably lower than in 2014/15. However, the 2016 Corporate Plan projects that the airline will only achieve a net profit in 2020/21 rather than in 2019/20 as projected in the 2015 Corporate Plan.

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The airline has applied for additional guarantees amounting to R4.756 billion to enable the it to sign off on its 2014/15 annual financial statements (AFS) and continue operating as a going concern.

- 5.2 It would not be prudent for government to support the airline, without first mitigating the fiscal risk. In fact, granting SAA another guarantee before the package set out in this Cabinet Memorandum is implemented would not only pose a serious fiscal risk, but would impair the reputation of government and risk a "contagion" effect on all guarantees which total over R400 billion.
- 5.3 A package of actions is required which include (1) appointing a full-strength Board; (2) appointing the Chief Executive Officer (CEO), Chief Financial Officer (CFO) and other key executives; (3) strengthening SAA's strategy to accelerate the turnaround of the airline and ensure alignment with the other state owned airlines; (4) ensuring SAA secures funding to meet its liquidity requirements; (5) putting in place the Air Traffic Liability guarantee; and (6) considering providing additional government support to the airline.
- 5.4 **Appointment of the full-strength Board:** SAA's Board appointment is done in terms of Clause 13.1 of the Memorandum of Incorporation (MOI) which states that the Board shall consist of a minimum of five directors and maximum of fifteen directors, who are to be appointed by the Minister in consultation with Cabinet. Furthermore, the MOI states that the shareholder should ensure that the Board comprises Executive Directors (EDs) and Non-Executive Directors (NEDs) with no less than two EDs, being the CEO and CFO (**Annexure A**).
- 5.5 The appointment of the three existing NEDs that make up the interim Board, Ms D.C Myeni, Ms Y Kwinana and Dr J.E Tambi, is subject to annual review. At the Annual General Meeting (AGM) held on 30 January 2015, it was decided that the review of the appointment of the existing interim Board members and appointment of a full-strength Board be dealt with outside the AGM process. This was necessary to provide the new shareholder department (National Treasury) time to do a proper assessment of the Board requirements, e.g. Board size and skills required to steer the organisation's turnaround. Thus, the term of the Board was extended until such time as a new Board was appointed.
- 5.6 The skills within the current Board include Auditing, Finance and Aviation. With regard to other aspects of Board composition diversity, the current NEDs are 100 per cent black and 60 per cent females.
- 5.7 To ensure continuity whilst strengthening the current, under-capacitated Board, it is recommended that the current Chairperson of the Board and an

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additional twelve new Board members be re-appointed/appointed respectively subject to annual review.

- 5.8 Skills identified to strengthen the SAA's Board include Finance, Risk Management, Treasury, Investment, Project Management, Business Strategy, Marketing and Business Management, Legal, Banking, Stakeholder Management, Communications and Social Development
- 5.9 Therefore, the appointment of Ms Bajabulile Swazi Tshabalala, Ms Thandeka Mgoduso, Mr Stavros Nicolaou, Ms Nazmeera Moola, Mr Akhter Hoosen Moosa, Ms Gugu Sepamla, Mr Siphile Buthelezi, Mr Peter Holmes Maluleka, Mr Mzimkulu Malunga, Dr Martha Mbatha, Ms Tryphosa Ramano and Mr Peter Tshisevhe on the SAA Board for a period of three years, from 01 September 2016 to 2016 to 31 August 2019, subject to annual review is proposed. Curricula Vitae (CVs) of the proposed new appointments /re-appointments of candidates are attached as **Annexure B**.
- 5.10 The appointment of the current Chairperson of the Board (Ms Duduzile Myeni) as the NED and Chairperson of the Board of SAA will be for a period of two years from 01 September 2016 to 31 August 2018 subject to annual review. Clause 13.4.1 of the MOI stipulates that a NED shall not hold office for more than three consecutive terms (of three years each). Ms Duduzile Myeni was originally appointed to the SAA Board on 1 October 2009, therefore her nine years ends on 30 September 2018. It is therefore recommended that she be re-appointed for a period of two years from 01 September 2016 to 30 September 2018.
- 5.11 Clause 13.2.1 of the MOI stipulates that the Minister shall appoint the Deputy Chairperson. Taking into account that the Chairperson's term will be ending in two years' time, a succession plan is important to ensure continuity. It is against this background that Ms Tryphosa Ramano is recommended to be the Deputy Chairperson of the Board.
- 5.12 In effecting these appointments, the Board will comprise of thirteen directors (**Annexure C**). In compliance with Principle 2.18 of King III on Corporate Governance, the Board will comprise a majority of non-executive directors of whom 53 per cent will be females. In terms of race, the Board will comprise 77 per cent Black, 15 per cent Indian and 8 per cent White representation.
- 5.13 **Appointment of the CEO, CFO and other key executives:** The existing Board has shortlisted three candidates for appointment as CEO. However, a good rapport between the Board and CEO is essential for ensuring alignment in driving implementation of SAA's strategy. Moreover, there have been a number of changes that have taken place at the airline since the candidates were identified, including the appointment of candidates to serve at other

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companies. Therefore, the newly appointed Board should be provided with the opportunity to re-open the process, review candidates for the CEO appointment and submit recommendations to the Minister of Finance. A new CEO should take the lead in appointing the other executives, in consultation with the Board and Minister, to ensure that accountability lines are clear.

- 5.14 **Strengthen the strategy and ensure alignment with other state owned airlines:** The newly appointed Board will be required to strengthen the strategy to accelerate the turnaround of the airline and to ensure its robustness in the context of increasing competition and volatile movements in fuel and exchange rates. This requires more aggressive cost containment. Refinement of the network and fleet plan based on a sound business case demonstrating the profitability of the proposed changes and ensuring alignment with the other state owned airlines is required. The airline's strategy needs to better differentiate the airline, enabling it to continue to compete effectively, inter alia through addressing the customer value proposition. National Treasury will be working with the Department of Public Enterprises to give consideration to the realignment of government's shareholding in the airlines and the possible introduction of a strategic equity partner.
- 5.15 **Secure funding to meet the airline's liquidity requirements:** The Board will need to take immediate action to raise the finance required for the airline to meet its liquidity requirements during 2016/17, including the repayment of R4.5 billion of debt maturing between the end of September 2016 and January 2017.
- 5.16 Lenders are reducing their unguaranteed facilities with SAA and appetite to lend to SAA, even with the support of the government guarantees, is drying up. A range of stakeholders have raised concerns relating to the governance and financial position of SAA. The appointment of a capable, full-strength Board and experienced executives implementing a robust strategy are vital to enable the airline to raise the funding it requires to operate.
- 5.17 **Putting in place the Air Traffic Liability (ATL) Guarantee:** SAA applied for an ATL guarantee on 16 August 2016. This consumer protection guarantee is a precondition for the issuance of a domestic and international air traffic license. Without the licence, SAA will be unable to operate. The new guarantee requirement of R541 million for the 12 month period up until 30 September 2017 can be accommodated within existing guarantee facilities.
- 5.18 Additional requirements for the new Board to deliver on SAA's mandate as set out in its founding legislation and MOI will be captured in the Shareholder Compact, the key elements of which are summarised under **Annexure D**.

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- 5.19 **Providing additional support to the airline:** SAA has applied for R4.756 billion in additional guarantees. Without the guarantees, the Board cannot sign off the 2014/15 Annual Financial Statements (AFS) as a going concern: the company is technically insolvent and would not be able to demonstrate that it is able to meet its liquidity requirements over the next 12 months. Instead the company would have to be placed into business rescue.
- 5.20 The financial health of the state owned company (SOC) portfolio has been highlighted as one of the major risks to South Africa's ability to deliver on its fiscal targets and hence for the sovereign credit rating over the medium term. It would not have been prudent for government to issue further guarantees to SAA without first taking steps to mitigate the fiscal risk, starting with appointing a full-strength Board.
- 5.21 Having appointed a full-strength Board tasked with executing the proposed measures, government can legitimately provide guarantee support to the airline. This will allow for SAA's 2014/15 AFS to be finalised and tabled in Parliament, as well as being made available to other stakeholders. Once demonstrable progress has been made with implementing the proposed measures, government could consider a range of other possible measures to support SAA's turnaround strategy which could include equity (from government and/or strategic equity partner) as may be deemed appropriate.

6. IMPLEMENTATION PLAN


The appointment of new members to make up a full-strength Board will be effective from 01 September 2016 to 31 October 2019, subject to an annual review. The reappointment of the Chairperson, Ms Duduzile Myeni, will be effective from 01 September 2016 to 30 September 2018. For continuity, Ms Tryphosa Ramano will be appointed as the Deputy Chairperson. The Board will be responsible for reviewing candidates for the appointment of the CEO and re-submitting recommendations to the Minister. The Board must take immediate steps to extend, roll over and refinance the debt that will mature from the end of September 2016 and review and strengthen SAA's strategy to accelerate the turnaround of the airline.

7. ORGANISATIONAL AND PERSONNEL IMPLICATIONS

None for Government.

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8. FINANCIAL IMPLICATIONS

- 8.1 With regards to the non-executive directors, there is no financial implication for government: remuneration of directors from outside the public service will be paid by SAA. No remuneration will be paid to members of the public service.
- 8.2 Having appointed the full-strength Board tasked with executing the proposed measures, government can legitimately provide guarantee support of R4.756 billion to the airline.
- 8.3 Should SAA default on existing guarantees and short term facilities then Government would have to settle the R14.4 billion in guaranteed debt. The breach of the expenditure ceiling would likely trigger a sovereign downgrade.

9. COMMUNICATION IMPLICATIONS

Upon approval of the appointment of the permanent Board of Directors, the Chairperson of the Board and the appointed Board members will be informed of their appointments.

10. CONSTITUTIONAL IMPLICATIONS

None.

11. IMPLICATIONS FOR VULNERABLE GROUPS

None.

12. SECURITY IMPLICATIONS

None

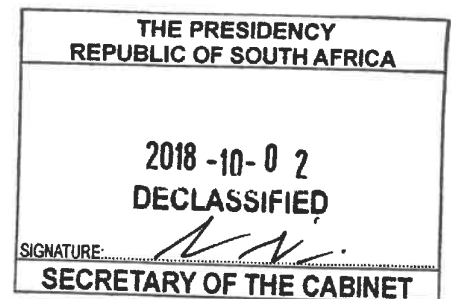
13. RESPONSES AND COMMENTS FROM DEPARTMENTS AND PARTIES CONSULTED AND CONSIDERATION BY THE RELEVANT DIRECTORS-GENERAL CLUSTER

None

14. RECOMMENDATIONS

- 14.1 It is recommended that Cabinet approves the following interventions required for the successful turnaround of SAA:

- 14.1.1 Appointment of a permanent Board comprising of twelve (Ms Bajabulile Swazi Tshabalala, Ms Thandeka Mgoduso, Mr Stavros Nicolaou, Ms



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Nazmeera Moola, Mr Akhter Hoosen Moosa, Ms Gugu Sepamla, Mr Siphile Buthelezi, Mr Peter Holmes Maluleka, Mr Mzimkulu Malunga, Dr Martha Mbatha, Ms Tryphosa Ramano and Mr Peter Tshisevhe) non-executive directors to the Board of SAA for a period of three years from 01 September 2016 to 31 August 2019, subject to annual review.

14.1.2 Appointment of the Chairperson of the Board (Ms Duduzile Myeni) as the non-executive director to the Board of SAA for a period of two years from 01 September 2016 to 30 September 2018, subject to annual review.

14.1.3 Appointment of one of the non-executive directors (Ms Tryphosa Ramano) as the Deputy Chairperson of the Board for a period of three years from 01 September 2016 to 31 August 2019, subject to annual review.

14.1.4 A package of the following further measures to be implemented to place SAA in a stronger position in terms of governance and improve the likelihood of possible financial recovery:

14.1.4.1 Board to review and resubmit recommendations for the appointment of the Chief Executive Officer (CEO). The CEO will in turn be responsible for the appointment of the other executives.

14.1.4.2 Board to review and strengthen SAA's strategy to ensure alignment with that of the other state airlines and that a turnaround is delivered by 2019/20.

14.1.4.3 Board to take immediate steps to secure funding to meet the airline's liquidity requirements including extending, rolling over or refinancing the R4.5 billion in debt maturing between September 2016 and January 2017.

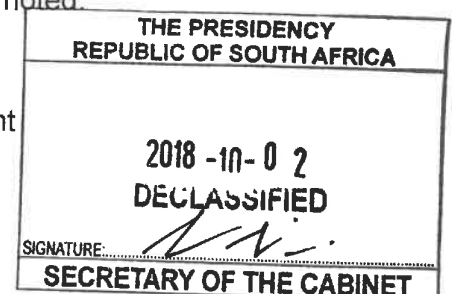
14.1.4.4 Subject to the above steps being taken, government to consider a range of other possible measures to support SAA's turnaround strategy which could include a guarantee, equity (from government and/or strategic equity partner) as may be deemed appropriate.

15. OFFICIAL RESPONSIBLE FOR THE MEMORANDUM

I declare that the memorandum adheres to the Guidelines dated July 2015 provided by the Cabinet Secretariat for the drafting of memoranda. The requirements in relation to electronic presentations were noted.

Mr Anthony Julies
Deputy Director-General: Asset and Liability Management

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National Treasury
012 315 5415
anthony.julies@treasury.gov.za

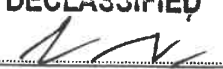
16. HEAD OF DEPARTMENT

Mr Lungisa Fuzile
Director-General: National Treasury
Tel: 012 315 5151

17. AUTHORISATION FOR PROCESSING THE MEMORANDUM**MINISTER**

PRAVIN GORDHAN, MP
MINISTER OF FINANCE

Is there a need for an electronic presentation to be done in addition to the memorandum? **No**

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