



MEDIA STATEMENT

Eskom reports first-half profit of R9.3 billion

Tuesday, 25 November 2014: Eskom today reported a profit of R9.3 billion for the six months that ended on 30 September 2014. This is down 24% from R12.2 billion for the same period the previous year.

While Eskom reported a profit of R9.3bn in the first half of its financial year, these profits are expected to decline to R0.5 billion for the full financial year. This is because, traditionally revenue in the winter is much higher than during the summer due to time-of-use tariffs to key industrial customers and there is less maintenance performed on Eskom power plants – which contributes to the profitability of the first half of the year, while tariffs are lower in summer and maintenance activities increase, resulting in higher costs.

Group revenue in the first half of the 2014/15 financial year increased by 5.4% to R81.9 billion (2013: R77.7 billion). This reflects the impact of the 8% tariff increase offset by a contraction in demand for electricity. Revenue growth has been offset by escalating primary energy costs due to increased purchases from independent power producers (IPPs) to help balance the demand and supply of electricity, increases in coal costs, and the continued use of open-cycle gas turbines (OCGTs).

Eskom Chief Executive Tshediso Matona said: “We will work to achieve financial and operational sustainability in a balanced manner, through internal efficiencies, the migration to cost-reflective tariffs through regulatory tariff processes, deferrals, or scope changes on projects, and government support.”

Eskom’s financial health has deteriorated over the past few years as a result of substantial cost increases, lower sales, and the lack of cost-reflective tariffs at a time when it has to invest heavily in building new capacity and power lines for the country. In addition, compliance with the new atmospheric emission legislation will result in significantly increased financial obligations.

Eskom started an internal financial efficiency drive called the Business Productivity Programme (BPP) last year to cut costs and extract efficiencies within the organisation. Total cash savings of R9.8 billion are targeted for the 2014/15 financial year. But efficiencies alone will not resolve the company’s financial difficulties.

Eskom Finance Director, Tsholofelo Molefe, said: “We are working with an Inter-ministerial Committee comprised of the Ministers of Public Enterprises, Minister of Energy and the Minister of Finance to find sustainable solutions, and these efforts have yielded initial results, with the National Treasury announcing a support package for Eskom last month.



This package will support liquidity in the short-term, but in the long-term it remains absolutely imperative that the tariffs must reflect the cost to supply electricity.”

“While electricity revenue increased 5.9% to R81.9 billion in the period under review, sales volumes declined by 1.4% following the widespread mining industry strikes and the closure of the Bayside aluminium smelter. We made a fair value gain of R1.6 billion on embedded derivatives in the period under review after the Bayside aluminium smelter had been closed,” said Ms Molefe.

Revenue per kilowatt-hour sold increased to 74 cents, compared to 69 cents in the same period in the previous year, while operating costs rose to 62 cents from 55 cents.

The R200 billion funding plan for the remainder of the Third Multi-year Price Determination (MYPD3) from 1 April 2014 to 31 March 2018 is progressing well, with 32.8% of funding secured (R66 billion).

On 13 September 2014, Cabinet approved a financial package in a bid to support Eskom’s liquidity and its financial sustainability and to ensure that the energy security of the country is maintained in an effort to aid GDP growth. On 22 October 2014, the Minister of Finance, Mr Nhlanhla Nene, announced that equity funding of at least R20 billion would be provided to Eskom. The package is seen as a first, yet robust, step on the road to ultimate financial sustainability.

Following the downgrade of the sovereign by Moody’s Investors Service, Eskom was also downgraded to Ba1 with a stable outlook on 7 November 2014. However, Standard & Poor’s (S&P) removed the negative CreditWatch placed on Eskom, while affirming with a negative outlook the BBB- rating on 11 November 2014, and Fitch Ratings affirmed Eskom’s credit rating of BBB+ with negative outlook on 28 October 2014. Both Fitch and S&P have indicated that the government support package has had a stabilising impact and will support Eskom’s liquidity and credit metrics.

“Any further downgrade would seriously impede Eskom’s ability to raise external funding or significantly increase the cost at which Eskom is able to borrow,” Ms Molefe said.

Total municipal arrear debt increased to R4 billion (March 2014: R2.6 billion). The continuing increase in arrear debt poses significant cash flow concerns. Following an intervention by the Minister of Public Enterprises, Ms Lynne Brown and the Minister of Cooperative Governance and Traditional Affairs, Mr Pravin Gordhan Eskom suspended bulk electricity disconnections to the three Free State municipalities, which would have happened on 3 October 2014.

The ministers have requested a period of time to find a solution to the problem. We support the ministers’ call to engage further on the matter, as it has serious bearing on



Eskom's financial sustainability and liquidity. As part of this process, we are engaging with the Premier of the Free State and the affected municipalities in the hope that they can come up with workable payment plans.

In keeping with the principle of zero harm to the environment, Eskom continues to pursue a range of actions to limit the environmental footprint of its existing fleet, although a significant reduction in carbon dioxide emissions will only be feasible with a diversification of the energy mix, or into a new-generation fleet.

Eskom's power system continues to be significantly constrained. Notwithstanding that, apart from three load shedding events over three evening peaks in June 2014, electricity demand was met during the six months to 30 September 2014. Demand was adequately met during the day, and although evening peaks were tight, sufficient generation capacity and emergency reserves were available to meet the demand.

"This was achieved through alternative supply side options and the utilisation of the open-cycle gas turbine (OCGT) stations. However, it must be noted that Eskom is no longer able to keep the light on at all costs as this has dire consequences on the health of the plant," said Mr Matona.

The nature of the capacity challenge changes from the evening peak in winter to a constraint throughout the day during summer. Eskom embarks on load shedding as a last resort to prevent a longer, more damaging shutdown of the entire system, which would negatively impact the economy.

Summer is a maintenance season, and coupled with the recent Majuba incident, load shedding cannot be ruled out as a controlled way of protecting the national grid from a total collapse or blackout.

Eskom Chairman, Zola Tsotsi, said: "We have said, for some time, that electricity supply will be tight until our capacity expansion programme is substantially completed. Our large new power station projects, Medupi, Kusile, and Ingula, have reached a series of important technical milestones. Our wind power plant, Sere, has performed beyond expectation and started feeding power into the grid in October 2014 ahead of the scheduled December date."

"We have seen several renewable projects from IPPs connected to the grid and delivering power. We anticipate that the supply from IPPs will grow steadily, assisting in managing the tight system. South Africans have played a significant role in helping to manage the electricity situation, and we continue to ask every electricity consumer to use power sparingly," he said.



Steady progress is being made in relation to the Medupi Unit 6, first synchronisation, with all efforts being made to meet the target date of 24 December 2014. However some commissioning risks still remain, which may delay synchronisation by several days beyond this date. The risks are receiving management's full attention. Full commercial operation of the unit is expected approximately six months later. Additional resources were mobilised to Unit 6 by both the boiler and control and instrumentation (C&I) contractors to mitigate any resource-driven delays. Additional shifts were introduced 24 hours a day, seven days a week, in order to accelerate progress on site. Eskom continues to work with contractors to resolve any issues that could affect the schedule.

The commissioning of the next unit, Unit 5, was initially forecast to occur within six months of bringing Unit 6 online. Eskom has indicated that this was no longer possible due to the challenges experienced at Unit 5, as resources were redeployed from Unit 5 to Unit 6 in an attempt to recover the schedule at Unit 6. The expected completion date of Unit 5 and the rest of the units will be communicated during March 2015.

The Kusile Project is making good progress after resolving significant quality issues with the boiler, the business rescue of a major subcontractor working on the flue gas desulphurisation (FGD) plant, and obtaining permits for the coal stockyard and ash dam through a protracted process as a result of revised legislation. The 4 800 MW plant is on track for the synchronisation of the first unit in December 2015.

Eskom and contractors have established a stringent tracking process and recovery plans in order to recover the schedule. Furthermore, a commercial strategy has been defined to increase contractors' resources and improve their performance.

Eskom is building additional power stations and major power lines to meet South Africa's rising demand for electricity and also to diversify its energy mix. Ultimately, the capacity expansion programme, which commenced in 2005 and is expected to be completed by 2020/21, will increase generation capacity by 17 384 MW, transmission lines by 9 756 km, and substation capacity by 42 470 MVA.

Since inception in 2005, the capacity expansion programme has resulted in 6 137 MW of additional generation capacity, 5 659 km of transmission lines and 27 655 MVA of substation capacity. The programme has cost R251 billion to date (excluding capitalised borrowing costs), and the total cost of the programme to completion is currently estimated at R348 billion (excluding capitalised borrowing costs).

At Ingula, since the tragic accident on 31 October 2013, progress has been significantly impacted resulting in limited progress for a period of almost 12 months. The section 54 work stoppage was lifted completely in September 2014, allowing underground works to resume. The projected forecast date for synchronisation of the first unit is November 2015, with the remaining three units following at approximately two-monthly intervals after that.



Eskom acknowledges the role that independent power producers (IPPs) must play in the South African electricity market and remains committed to facilitating their entry into the market. Total capacity of 4 280 MW has been contracted with IPPs as at 30 September 2014.

The investigation on the Duvha unit 3 over pressurization incident which took place on 30 March 2014 has been concluded. The combination of several issues created the build-up of the over pressurization incident. We have a mitigation strategy in place and there will be significant learning to ensure that a similar incident does not occur in future.

At approximately 12:30 on Saturday 1 November 2014, operating staff at Majuba Power Station noticed a crack in the main coal silo. The area was evacuated and at 13:12, the silo collapsed. No injuries were reported. As a result of the collapse, the supply of coal to the boilers of a number of units was interrupted, and output at the station was reduced to just over 600MW. Load shedding was implemented on Sunday 2 November 2014 to preserve coal at Majuba Power Station and water at the pumped-storage plant, in order to meet demand during the following week and to prevent the power system suffering a total blackout. An investigation into the incident is underway, and is expected to take around three to six months to finalise. Following this incident, Eskom has undertaken an investigation of all coal silos at its power station to ensure that they are structurally sound.

“Eskom’s mandate is to provide electricity and to help stimulate the South African economy, thereby improving the quality of life of the people of this country and the region. To achieve that, what we have to focus on right now is the sustainability of our finances, operations, and completion our capacity expansion programme,” said Mr Matona.

The executive team will work with the Chief Executive over the next few months during which time they will finalise Eskom’s strategy and objectives for the medium to long-term, taking into account current constraints and opportunities.

“I will, before the end of this financial year, present to the Eskom Board of Directors a top structure, including an Executive Committee that will be smaller and more agile. The structure will be designed such that it focuses on operational effectiveness, efficiency, our core business and key priorities that are aligned with shareholder expectations,” said Mr Matona.

ENDS