CITY OF CAPE TOWN
ISIXEKO SASEKAPA
STAD KAAPSTAD

ANNEXURE D

CITY OF CAPE TOWN – 2021/22 BUDGET (JANUARY 2022)

2021/22 MTREF AMENDED CHAPTER REQUIRED TO BE INCLUDED IN THE IDP

Overview of budget assumptions applied to the 2021/22 MTREF

Introduction

The Local Government Municipal Systems Act, Chapter 5, Section 26, prescribes the core components of the Integrated Development Plan (IDP). Section 26 (h) requires the inclusion of a financial plan, which should include a budget projection for at least the next three years. This financial plan aims to determine the financial affordability and -sustainability levels of the City over the medium term.

Part 2 of the MBRR (Budget-related policies) requires the Accounting Officer to ensure that budget- related policies are prepared and submitted to Council. One of these policies relates to the long-term financial plan, which aims to ensure that all long-term financial planning is based on a structured and consistent methodology, thereby ensuring long-term financial affordability and sustainability.

A municipality's financial plan integrates the financial relationships of various revenue and expenditure streams to give effect to the IDP. It provides guidance for the development of current budgets and assesses financial impacts on outer years' budgets by incorporating capital expenditure outcomes, operating expenditure trends, optimal asset management plans and the consequential impact on rates, tariffs and other service charges. The City has developed a financial model, namely the Long Term Financial Plan (LTFP), which aims to determine the appropriate mix of financial parameters and assumptions within which the City should operate to facilitate affordable and sustainable budgets for at least 10 years into the future. In addition, it identifies the consequential financial impact of planned capital projects on the City's operating budget.

The LTFP model is reviewed annually to determine the most affordable level at which the City can operate optimally taking the following into account:

- Fiscal overview;
- Economic climate;
- Demographic trends;
- National- and Provincial influences;
- IDP and other legislative imperatives; and
- Internal governance, community consultation and service delivery trends.

The key budget assumptions of the 2021/22 MTREF include a discussion of the sources of information used to develop assumptions for revenue and expenditure, which drive the 3-year MTREF of the City under the following headings:

- Impact of the COVID-19 pandemic;
- Financial Strategic Approach;
- Financial Modelling and Key Planning Drivers;
- Economic outlook/external factors (including demographics);
- National and Provincial influences;
- Expenditure analysis – a three-year preview;
- Revenue analysis – a three-year preview; and
- Local Government Equitable Share and Fuel Levy.

Based on latest mid-year budget and performance assessment, this annexure was updated with changes affected in the 2021/22 January adjustments budget where applicable.

1.1 Impact of the COVID-19 pandemic

The national lockdown declared on 23 March 2020, whereby all citizens' (except essential services) were ordered to stay home for a period of 21 days commencing at midnight on 26 March 2020, would forever be considered as the start of the devastating effect on an already vulnerable economy. As the country eased in and out of restrictions levels, in riding the first and then second wave of the COVID-19 pandemic, municipalities had to adapt to the impact of the economy on its operations and the impact of the affordability levels of its consumers.

The 2020/21 approved budget included an amended, viable financial plan (from the initial March 2020 tabled budget) over the short- to medium term, taking the variables and impacts emanating from the COVID-19 pandemic into account. To recap, changes in the approved 2020/21 budget included the provision of additional operating expenditure of R903 million, increased debt impairment provision (R1 499 million due to expected lower collection rate, reduction in revenue of R1 427 million and a reduction in operating expenditure of R1 703 million) as a result of programmes/projects envisaged not to go ahead but also reprioritisation of budgetary allocations to cover the additional requirements.

The 2020/21 budget was thus prepared with much uncertainty on how the COVID-19 pandemic would affect consumers' payment behaviour but the City has managed to maintain a high average collection ratio despite the devastating effects COVID 19 had on the economy. The collection rate outcome for the first five months of the 2020/21 financial year remained strong showing higher outcomes when compared to the budgeted collection rates. The 2020/21 budgeted collection rates for all trading services were therefore revised upwards in the adjustments budget following the mid-year review and assessment process. This upward prediction - although not at pre-COVID-19 levels and due to debt management actions resuming - followed through to the 2021/22 financial year.

The impact of the pandemic was as expected one of the determinants in the LTFP and 2021/22 MTREF and the assumption that the impact of the pandemic will be felt till the end of this financial year (2020/21) and possibly beyond based on restriction levels of possible future waves.

This impact is not necessarily by way of additional expenditure as most of the additional expenditure was provided for in the previous and current (2020/21) financial years with only R408 million carried over from the 2020/21 financial year for ongoing COVID-19 related expenditure.

In addition, an amount of R683 million reduced from directorates' budget in 2020/21 was reinstated in the 2021/22 financial year. This was part of the savings identified in the 2020/21 of R1.5 billion to cover the COVID-19 related expenditure.

Economic context

The preparation of the drafting of the LTFP and subsequent MTREF commenced with a macro environmental scan of the economy as one of its determinants. The factors taken into consideration included the CPI, interest rates, exchange rates, service growth and GDP, which is briefly discussed below. The 3rd quarter of 2020 showed an improvement in GDP with limited economic rebound, however, renewed restrictions in December 2020 as South Africa experienced its second wave of heightened infections might impact this rebound. The City's LTFP and the 2021/22 MTREF was drafted against this backdrop.

However, national government is optimistic for the current calendar year projecting real economic growth of 3.3 per cent in 2021, which is expected to moderate to 1.9 per cent in 2022 and 2023.

The currency similarly has been under severe pressure since the outset of the pandemic and South Africa in a hard lockdown with the first week in April 2020 reflecting the weakest rate at R19.26 to the US dollar. This coupled with the Moody's ratings agency downgrading the country to junk status.

Inflation for 2020, as reported by Stats South Africa with its December 2020 results, was the lowest in 16 years and the second lowest in 51 years. The average annual inflation rate for 2020 was 3.3% - the lowest since 2004 (1.4%) and the second lowest since 1969 at 3%. Annual inflation ended in December 2020 at 3,1%, slightly lower than November 2020's reading of 3,2%. 2020 also saw the inflation rate dropping below the 3% band (Reserve Bank 3%-6%) in May and June of 2020 at 2.1% and 2.2% respectively. The inflation rate in the MTREF will be discussed further in the document.

According to the Monetary Policy Committee's (MPC) January 2021 statement, the current economic and financial conditions are expected to remain volatile for the foreseeable future. Against this backdrop, the MPC decided to keep rates unchanged at 3.5% in January 2021 and projects an increase of 25 basis points in the second and third quarter of 2021. The MPC projected the year-end rate to be 4.1% for 2021, 4.9% for 2022 and 4.9% for 2023.

National influences on municipalities due to COVID-19

As national government reshuffled its finances to provide for much needed COVID-19 related requirements for social, infrastructure and local provisions, it was to be expected that this would impact on future grant allocations to municipalities. During the pandemic, additional allocations were made and the City received additional Local Government Equitable Share (LGES) as well as the approval of conversion of unspent grants to cover COVID-19 related expenditure. National government, as part of its fiscal consolidation policies aimed at reducing government deficits and debt accumulation, reduced the LGES and Fuel levy transfers to municipalities over the 2021/22 MTREF. These transfers were much lower than what was projected for the City when compared to the 2020/21 indicative allocations. This reduction in revenue received from national government was one of the major impediments in getting the City's 2021/22 MTREF to a balanced position.

The City's COVID-19 pandemic recovery plan

The City's recovery plan and focused work has been drafted on the premise that assumes that South Africa, Cape Town and the City will not simply return to normal once the pandemic has run its course. The plan would therefore enable the City to adapt and serve residents in the best way possible in a post-pandemic crisis context.

This recovery programme consisted of three phases. This in order to accommodate the emerging impacts of COVID-19 and unknowns around the duration and extent of the pandemic:

- Phase 1 - Stabilisation to run until June 2021: This refers to navigating and managing possible increases and multiple peaks of COVID-19 infections. The focus is on organisational stability (functional and financial); least disruption to service delivery, focus on efficiency (doing same/more with less), and focus on effectiveness (focusing on what matters). Investment in core services and in non-negotiable modernisation, including capital projects which support the economy, is to be defended.
- Phase 2 - Adaption - July 2021 to June 2022: The focus of this phase is to build on the efficiencies that have been gained through the stabilisation phase and making organisational/service adjustments that are not possible to implement in the 2020/21 financial year.
- Phase 3 - Rebuild/Recovery - July 2022 to June 2027: This phase covers the post COVID-19 period and new term of office IDP period and will focus on how to relieve the sustained economic and social impacts of the pandemic.

From a financial viewpoint, the three phases highlighted action to be taken in prioritising financial stability in the Stabilisation phase (until June 2021); prioritising financial sustainability in the Adaptation stage and maintaining financial sustainability in the Rebuild/Recovery Stage.

The above processes and actions were part of the LTFP deliberations when drafting the 2020/21 MTREF and taking it into the 2021/22 budget process.

1.2 Financial Strategic Approach

The 2021/22 LTFP and MTREF was prepared with the intention of keeping revenue parameters as low as possible to assist already struggling communities and businesses. In doing so, serious considerations in reducing expenditure was made but at the same time not compromising on service delivery.

The key focus areas over the coming year as provided during the Strategic Review phase of the Strategic Management Framework (SMF) process are:

- Pandemic response;
- Prioritize essential services;
- Prioritize financial sustainability;
- Enable economic recovery;
- Respond to land and housing crisis;
- Prioritize safety;
- Respond to health and social impacts; and
- Organizational stabilization and adaptation and building resilience.

The Strategic brief further iterated that in response to the severe shock which has reverberated through Cape Town's social and economic systems in the form of the COVID-19 pandemic, and the cascading stresses on systems of municipal financing and governance – the City must make the hard choices around how to deliver on the outcomes of the IDP within the boundaries of a severely constrained budget.

At the SMF Operational Review directorates had to present and finalise cost cutting proposals and present progress on the planning/implementation of the strategy brief. They were further required to include additional operational asks only if it was an emergency, critical additional expenditure related to COVID-19 or focus areas that emerge from the strategic brief, with a motivation showing that the costs cannot be covered within the existing budget.

LTFP rationale and financial strategies implemented

The strategies included in the 2021/22 MTREF include the following:

- The depreciation strategy, which commenced in the 2020/21 financial year, continued for this MTREF in an effort to utilise available cash and reduce tariffs.
  - This strategy sees the City using its surplus cash flow to negate the recovery of a depreciation charge of R500 million per annum over seven years. This is done in order to offset revenue increases, due to loans not taken up previously. Subsequent to the tabled budget this amount was increased to R523 million for 2021/22 to fund a portion of the cost relating to the unlawful occupation of land initiative; and
  - This attributed to the Budgeted Financial Performance showing a bottom-line deficit although the City's budget is fully funded as reflected in the Budgeted Cash Flow statement.
- Various cost savings initiatives were also implemented to achieve a budget that is realistic, sustainable and credible. Still ensuring the continuation of services and keeping revenue increases at low levels.

1.3 Financial Modelling and Key Planning Drivers

The principles applied to the MTREF in determining and maintaining a sustainable financial plan included:

- A base reduction on various expenditure categories of R72.5 million across all directorates in response to performance outcome of the 2019/20 financial year as well as a 5% reduction across all directorates on contracted services amounting to R149.1 million. This reduction however excluded contracted services linked to repairs and maintenance and externally-funded projects.
- Staff and vacancies:
  - A vacancy reduction of R311.3 million;
  - The zero percent cost of living increase proposed in the approved budget was adjusted to 3.5% in the 2021/22 January adjustments budget, in accordance with the SALGBC agreement approved in September 2021;
  - No performance increases for TASK grades 14 and above;
  - Budgeting at 95% of employee costs; and
  - A differentiated percentage budget approach on vacancies.

- No increases on overtime provision except for labour intensive directorates where inflationary increases were applied.

- Repairs and maintenance growth based on the previous year's actual expenditure, service delivery needs and efficiencies identified.
- Differentiated expenditure parameters include a combination of no growth (other expenditure), reduction to the base (other materials) and reduction of 50% of the current year budget; no growth going forward for bursaries and ABE and training programmes (Training).
- A 100% capital expenditure implementation rate.
- Credible and realistic collection rates based on current and projected trends considering the impact of the pandemic.
- National- and Provincial allocations as per the 2021 Division of Revenue Act (DoRA) and 2021 Provincial Gazette (Provincial Gazette Extraordinary 8400).

The following were included in the MTREF:

- A reduction of R500.4 million - additional expenditure included in the 2020/21 for COVID-19 related expenditure – but no longer required in 2021/22 financial year;
- Of the savings identified in the 2020/21 financial year to cover COVID-19 related expenditure R683 million were reinstated in the 2021/22 MTREF;
- In response to the SMF Operational Review process, initial additional asks by Rate-funded services were R1.2 billion. However, an amount of R226.9 million was allocated as additional impacting the rates revenue parameter. The balance of the requests was absorbed by a combination of:
  - Reviewing original submitted requirements;
  - Providing once-off allocations in the January 2021 adjustments budget; and
  - Reinstated COVID-19 related expenditure savings identified in 2021/22.
- The City's portion of the Law Enforcement Advancement Program (LEAP), which was originally budgeted at R146 million for 2021/22, was adjusted downward by R80.3 million in the 2021/22 January adjustments budget; and
- The City experienced a surge in unlawful land occupations as a consequence of the COVID-19 pandemic. A provision of R170.8 million for 2021/22 was allocated across various services to combat this surge. This cost is budgeted to be funded from previous years' USDG VAT claw-back surpluses and the increase to the depreciation strategy amount.

On account of the timing of the adjustments budget, following the municipal elections and prior to the approval of a new IDP, it has not been possible for the adjustments budget to be fully realigned to reflect the electoral manifesto, however, the inclusion of the following immediately implementable initiatives has been facilitated:

- Extending allocations to the City's Clean-up Campaign;

- Additional budget for repairs and maintenance for Human Settlements and in the urban environment;
- Additional Safety and Security budget;
- Further support for Safe Spaces;
- Additional resources to ensure title-deed transfers;
- Repairing irrigation at Strandfontein Sports Complex and fast-tracking of planning for the Strandfontein Pavilion;
- Repairs to the Muizenberg huts; and
- Vaccination programme support.

Demographic trends

The population of Cape Town in 2020 was estimated at 4 604 986, growing by 2.0% from 2019 to 2020 (Mid-year Population Estimates, Statistics South Africa, 2020). This makes Cape Town one of the larger metropolitan municipalities in South Africa and the main urban centre in the Western Cape.

In the context of the current COVID-19 pandemic facing the City and Cape Town, it is complex and not yet possible to fully consider what the shorter- and longer term impacts on demographic trends may be. However, at a high-level, it is still expected that the broad trends will be similar and Cape Town's population is expected to continue to grow as has been the past trend.

It is projected that the population will grow to around 5.1 million in 2030 (City of Cape Town, 2018). Moreover, the number of households in Cape Town in 2020 was estimated at 1.4 million, an increase of 10.5% since 2016 (City of Cape Town 2020, using Mid-year estimates). The average household size is estimated to have declined from 3.3 persons in 2015 to 3.2 persons in 2020 (City of Cape Town, 2020).

These trends of a steadily increasing population growth (albeit at a declining growth rate) and an increasing number of households, form some of the informants to City planning and service delivery for the residents of Cape Town. These trends will continue to be monitored, and refined as needed to inform COVID-19 recovery responses and planning.

National and Provincial influences

a) National Treasury MFMA Circular No. 107, issued on 4 December 2020

The purpose of this annual budget circular is to guide municipalities with the compilation of the 2021/22 MTREF.

The objectives of the circular are to, inter alia, demonstrate how municipalities should undertake annual budget preparation in accordance with the budget- and financial reform agenda and associated "game changers".

Key focus areas stemming from this circular included:

- Macro-economic forecasts to be considered when preparing the 2021/22 MTREF municipal budgets;
- 2021 Local Government Elections and the budget process – managing of four significant risks;
- Version 6.5 of the mSCOA chart released with the circular to be utilised for the preparation of the 2021/22 MTREF;
- Municipalities to budget for water as inventory in the 2021/22 MTREF;
- Municipalities to set cost reflective tariffs to ensure that recovery of the full cost of rendering the service;
- Transfers to local government to be reduced for the local government equitable share, general fuel levy and direct conditional grants over the 2021 MTEF period;
- All municipalities should be aware that section 8 of the Municipal Property Rates Act on the determination of categories of rateable properties has been revised through the Local Government Municipal Property Rates Amendment Act, 2014;

- Municipalities to maintain tariff increases at levels that reflect an appropriate balance between the affordability to poorer households and other customers while ensuring the financial sustainability of the municipality;
- Municipalities are advised to use the tariff increases previously (March 2019) approved by the National Energy Regulator of South Africa (NERSA);
- Accounting officers reminded of their responsibility in terms of section 62(1)(a) of the MFMA to use the resources of the municipality effectively, efficiently and economically;
- In the absence of any information in this regard from the South African Local Government Bargaining Council (SALGBC), municipalities are advised to take into account their financial sustainability when considering salary increases; and
- Municipalities need to be proactive in exercising credit control measures to ensure that arrear debt is collected.

b) National Treasury MFMA Circular No. 108, issued on 8 March 2021

This budget circular is a follow-up to Circular 107 issued in December 2020. It guides municipalities with preparation of the 2021/22 MTREF. This circular is linked to the MBRR and the mSCOA and strives to support municipalities' budget preparation processes so that the minimum requirements are achieved. The key focus of this circular is the grant allocations per the 2021 Budget Review and the 2021 Division of Revenue Bill.

The circular also covers the following:

- An update on the South African Economy and inflation targets;
- Key Focus Areas for The 2021/22 Budget Process – changes to Local Government Allocations:
  - 2021 Local Government Elections and The Budget Process - Transitional Processes - Development and Adoption of IDPs during the 2021 Election Year and Hand-over reports for the newly elected councils.;
- mSCOA – guidance on transferring of opening balances, surplus or deficit journals and rollovers and repayment of unspent grants;
- Municipalities to maintain tariff increases at levels that reflect an appropriate balance between the affordability to poorer households and other customers while ensuring the municipality's financial sustainability;
- An update on Eskom's Bulk Tariff Increases and municipalities expected to mitigate the negative impact of the expected 16 to 20 per cent increase by improving efficiencies on both the revenue collections and the spending side;
- Funding choices and management Issues – includes guidance on the process to be followed with regard to the payment of danger allowance to employees – frontline staff rendering services to communities during the pandemic;
- Mayor's discretionary funds and similar discretionary budget allocations – municipalities must refer to section 12 of the MFMA in relation to setting up a relief, charitable, trust or other funds and must refrain from setting up sub-votes or allocations to "Mayoral Discretionary Funds", "Special Projects", "Special Events" or similar discretionary type funds;
- Conditional grant transfers to municipalities – setting out the criteria for the rollover of conditional grants and process and rollover requests against the COVID-19 funding allocated through the Equitable Share; and
- Information on the MBRR reporting and the budget process and submissions for the 2021/22 MTREF also included.

c) Provincial Treasury Municipal Circular 20/2020 issued 18th December 2020

In addition to reiterating the key aspects included in the MFMA Circular 107, this circular also highlighted:

- Economic and Fiscal environment of the Western Cape;
- Budgetary response to the Western Cape Recovery Plan; and
- Key dates of the 2021/22 Integrated Planning and Budgeting Process.

d) Provincial Treasury Municipal Circular 5/2021 issued 17th March 2021

This circular reiterated the key aspects raised in the MFMA Circular 108. In addition, it provided municipalities with a briefing on the Strategic Integrated Municipal Engagement (SIME) process scheduled for April/May 2021 after tabling of the budget.

1.4 Expenditure analysis – a three-year preview

a) General inflation outlook and its impact on municipal activities

National Treasury CPI projection is 3.9% for 2021/22, 4.2% for 2022/23 and 4.4% for 2023/24.

The City's CPI projection is within the South African Reserve Bank's (SARB) inflation target range of between 3% and 6% and in line with National Treasury guidance. CPI applied by the City for the 2021/22 MTREF is 3.10%, 4.60% and 4.50% over the respective three years. The City utilised BER's CPI projections at a point in time during the planning process and applies the projections in municipal financial years. To compensate for the higher CPI in 2020/21, the City applied a lower CPI for 2021/22.

The inflation rate had little impact to the City's expenditure budget as the City continued with the differentiated approach to give effect to a form of zero-based expenditure budget. Inflation was therefore not the primary driver of expenditure. CPI was considered in determining the miscellaneous tariffs.

b) Contracted Services, Overtime and Operational Cost

The pandemic presented significant constraints to the City's expenditure budget. The negative impact the pandemic had on the City's revenue budget limited the funds available for expenditure. In preparing the 2021/22 MTREF various cost saving initiatives were implemented to drive cost down whilst still ensuring the continuation of municipal services.

Similar to previous years the outcome of the 2019/20 budget performance was used as a basis to identify areas where savings were possible. Interventions adopted included budget reductions, reprioritisation of budgets and a differentiated approach to various expenditure categories. The differentiated approach consisted of a combination of zero-based and different percentage increases based on the nature of expenditure, the nature of the service departments (e.g. labour intensive in the case of overtime) and previous performance. The approach included a combination of no growth (other expenditure), reduction to the base (other materials) and reduction of 50% on the training budget. In addition, contracted services were reduced by 5%, excluding grant funded and contracted services related to repairs and maintenance work.

The Municipal Cost Containment Regulations and the City's Cost Containment Policy embedded in the City's operations also continued to assist in driving cost down and ensuring that value for money is achieved and resources of the municipality are used effectively, efficiently and economically.

c) Interest rates for investment of funds

Investments are made in terms of the City's Cash Management and Investment Policy, which aims to secure sound and sustainable management of the City's surplus cash and investments. The MPC cut the repo rate by 300 basis point (3%) in the previous financial year to aid South Africa's recover from the COVID-19 pandemic. Even though the repo rate was increased in November 2021 by 25 basis points (0.25%), the lower cumulative repo rate results in lower investment rates being offered by commercial banks, which in turn contributes to the City's reduced investment income budget.

Given the above, investment interest rates for 2021/22 is 4.02% and 4.48% for the outer years of the MTREF.

d) Collection rate for Property Rates and Service charges

NT Circular 107 reiterates the guidance provided in NT MFMA Circulars 93 and 98 as it relates to municipal collection rates. The guidance provided advises municipalities to comply with Section 18 of the MFMA and ensure that they fund their 2021/22 MTREF budgets from realistically anticipated revenues to be collected. Subsequently, municipalities are cautioned against assuming collection rates that are unrealistic and unattainable.

Performance outcomes of the first five months of 2021/22 showed improved collection rates when compared to the budgeted collection rates. This necessitated a review of the budgeted collection rates in line with performance. Collection rates were therefore revised as follows in the January 2021 adjustments budget.

Table 1 Collection Rates

Services	Original Budget 2021/22	January Adjustment Budget 2021/22	Budget Year +1 2022/23	Budget Year +2 2023/24
Rates	95.14%	95.14%	95.59%	96.04%
Electricity	98.50%	99.00%	98.50%	98.50%
Water	87.00%	91.00%	89.00%	92.00%
Sanitation	87.00%	93.00%	89.00%	92.00%
Refuse	85.00%	90.00%	85.00%	85.00%

The Rates collection rate is projected at 95.1% for 2021/22, which shows an improvement to the budgeted collection rate of 2020/21. The higher projected collection rate is based on current trends and continued debt management initiatives.

The collection rates for Tariff-funded services' were all adjusted upwards in the 2021/22 January adjustments budget as result of, amongst other, continuous rollout of electricity prepaid meters, revenue protection initiatives, increased debt management action and moving out of the COVID-19 environment.

e) Salary increases

The 2020/21 financial year was the last year of the 3-year Salary and Wage Collective Agreement. In the absence of a renewed agreement during the budget process, National Treasury, in its circulars 107 and 108, advised municipalities to take into account their financial sustainability when considering salary increases especially given the current economic condition exacerbated by the COVID-19 pandemic. Municipalities were urged to consider projecting increases to wages that would reflect their affordability and even to exercise the option for exemption for any negotiated increase above the level of their affordability.

Due to the constraints on the City's expenditure budget certain interventions including no provision for a cost of living increase in the 2021/22 financial year has been made. However, in the event that the Salary and Wage Collective Agreement concludes an increase for 2021/22, the City will be necessitated to implement a budgetary intervention to the salary budget of a permanent nature. In the absence of an agreement, the outer year's salary increases were based on the latest calendar year BER CPI projections.

Subsequent to the above, the SALGBC agreement was finalised mid-September 2021. The City applied for exemption citing financial affordability and sustainability as motivation, but it was not successful. In accordance with the provisions of this agreement, the salary increase was changed from 0% to 3.5% for 2021/22, including, amongst other, a non-pensionable once off lump sum payment.

To further reduce costs, no provision for performance- and other notch increases were made for T-grade level 14 and above. A provision of 2% was made for incremental allowances for T-grade level 13 and below.

In addition, the City continued with the method of budgeting for salaries at 95% as introduced in the 2018/19 financial year. The 2021/22 MTREF also saw the continuation of partial budgeting for vacancies, due to previous years' outcomes showing a recurring underperformance. This approach was adopted as the turnaround time of vacancies has attributed significantly to the underperformance on the salaries budget. Furthermore, a reduction in vacancies were also implemented in the 2021/22 financial year to further drive down cost.

f) Ensuring maintenance of existing assets

NT MFMA Circular 107 advised municipalities to refer to annual budget circulars of previous years for guidance on budget preparation not covered in this circular. In this regard, NT MFMA Circular 55 states that municipal councils, mayors and municipal managers are urged to ensure that allocations to repairs and maintenance, and the renewal of existing infrastructure are prioritised.

To ensure investment in repairs and maintenance, the differentiated approach introduced in previous years was applied to repairs and maintenance expenditure for the 2021/22 MTREF. This approach considered previous years' performance, service delivery needs, efficiencies and the nature of the function that individual services provide. The following varying parameters were applied:

- CPI increase to services where the nature of business is primarily to provide repairs and maintenance, and where the condition of the assets must be secured, and for services, which although their main function is not providing repairs and maintenance but the nature of business and facilities requires a proper maintenance provision; and
- No increase for support services.

Even though this approach was followed, the pandemic prevented the full service of repairs and maintenance to continue. This resulted in a reduction of the repairs and maintenance base in the 2020/21 financial year. It is expected that this trend will continue in the 2021/22 financial year.

NT MFMA Circulars 55 and 70 set the ratio of operational repairs and maintenance to asset value (write down value of the municipality's property, plant and equipment (PPE)) at 8%. The ratio outcome for 2021/22 improved from 7.2% in the approved budget to 8.2% in the 2021/22 January adjustments budget. This improvement is because of increased investment in repairs and maintenance and reduced PPE cost.

g) Operational financing for capital depreciation

Calculation of depreciation on new capital expenditure is based on variables such as asset class and lifespan, depending on the nature of the asset. An annual capital expenditure implementation rate of 100% was assumed. Depreciation of existing assets is calculated based on simulated SAP data that reflect actual values per annum. Assets under construction (AUC) are calculated based on asset class lifespan and projected capitalisation dates.

h) Credit rating outlook and borrowing

The City needs a credit rating to demonstrate its ability to meet its short- and long-term financial obligations. Potential lenders also use it to assess the City's credit risk, which in turn affects the pricing of any subsequent loans taken. Factors used to evaluate the creditworthiness of municipalities include the economy, debt, finances, politics, management and institutional framework.

Moody’s Investors Service completed their annual review of the City in April 2021 and released its credit opinion in this regard on 10 June 2021 in which it affirmed the City’s global scale and national scale ratings of Ba2 and Aaa.za, respectively, with a negative outlook.

Subsequent to the above, on 16 July 2021, Moody’s implemented rating actions on five South African Regional and Local Governments entities, which included the City. This downgrade by Moody’s was as a result of an analysis performed on the local government “sector” as a whole, with reasoning provided that there appears to be “rising liquidity pressure as a result of material shortfalls in revenue collection, that Moody's expects to last, in the context of very weak growth. South African Regional and Local Governments are likely to draw down on cash buffers, with different starting positions, eroding their capacity to absorb future shocks”. Although the City’s reporting indicated a resilient collection ratio and strong cash position at the time, the City, as an individual entity, was still directly impacted by this “sector” review and downgrade. As a result of this assessment, the City’s long-term global scale and national scale ratings were automatically downgraded to Ba3 and Aa3.za (highest possible national scale rating relative to the global scale rating), respectively, and placed on review for downgrade as an individual entity. Flowing from the local government “sector” downgrade indicated above, Moody’s formalised the City’s downgraded ratings by issuing an individual credit opinion on 29 July 2021.

On 26 November 2021, Moody’s Investors Service confirmed the City’s global scale rating, national scale rating as well as its negative outlook. This confirmation was issued after Moody’s concluded the above-mentioned review.

The City’s national scale rating is currently Aa3.za/P-1.za, which reflects the City’s credit profile of strong financial performance supported by prudent financial management, a large and diverse economic profile and predictable sources of revenue from property taxes and service charges. The City has consistently generated robust operating surplus and strong liquidity compared with that of its peers in South Africa. Although the City’s debt is expected to rise gradually over the medium term, it will remain lower than most of its peers in the country. The City’s credit profile is constrained by the capital spending pressure arising from infrastructure backlogs and population growth. It is further constrained by the structurally weak economic environment; worsened by the ongoing coronavirus restrictions; which is expected to moderate the city's operating performance.

The City’s known ratings over the last period were as follows:

Table 2 Credit rating outlook

Category	Currency	Current Rating 26 November 2021 Update following review conclusion	Previous Rating 29 July 2021 Downgrade after sector review	Previous Rating 10 June 2021 Update following the City’s annual review	Previous Rating 1 December 2020 Update following downgrade of Sovereign
Outlook	-	Negative	Rating(s) under review	Negative	Negative
NSR Issuer Rating	Rand	Aa3.za	Aa3.za	Aaa.za	Aaa.za
NSR ST Issuer Rating	Rand	P-1.za	P-1.za	P-1.za	P-1.za
NSR Senior Unsecured	Rand	Aa3.za	Aa3.za	Aaa.za	Aaa.za

- Stable Outlook – reflects that a credit rating assigned to an issuer is unlikely to change;
- Negative Outlook - reflects that a credit rating assigned to an issuer may be lowered;
- Rating under Review - a review indicates that a rating is under consideration for a change in the near term;
- NSR Issuer Rating – Aaa.za - Issuers or issues rated Aaa.za demonstrate the strongest creditworthiness relative to other domestic issuers;
- NSR ST Issuer Rating – P-1.za – Issuers (or supporting institutions) rated Prime-1 have the strongest ability to repay short-term senior unsecured debt obligations relative to other domestic issuers; and
- NSR Senior Unsecured – Aaa.za - Issuers or issues rated Aaa.za demonstrate the strongest creditworthiness relative to other domestic issuers.

The City’s borrowing is done in terms of Chapter 6 of the MFMA as well as the City’s Borrowing Policy, in terms of which a long-term loan will only be entered into if it’s affordable and sustainable. The City’s loan requirements are determined by the capital investment requirement (excl. Transfers Recognised: Capital) and the projected cash position. The City primarily borrows against future revenue generating assets.

The below table reflects the borrowing and interest rate over the MTREF.

R Thousand	Budget Year 2021/22	Budget Year +1 2022/23	Budget Year +2 2023/24
Borrowing	1 200 000	4 500 000	7 000 000
Borrowing Interest Rate (%)	11%	11%	11%

1.5 Revenue analysis – a three-year preview

Growth and Revenue parameters remained unchanged with the 2021/22 January adjustments budget.

a) Growth

Property Rates

No growth is projected for Property Rates for 2021/22 and 2022/23. A slight growth of 0.1% is projected for 2023/24. This is due to the expected impact of the pandemic on valuations.

Electricity

No growth in sales revenue is projected for 2021/22, followed by a shrinkage of 1.5% over the two outer years of the MTREF. The conservative approach is mainly due to the effects of the pandemic as well as a sustained declining demand on electricity sales.

Water and Sanitation

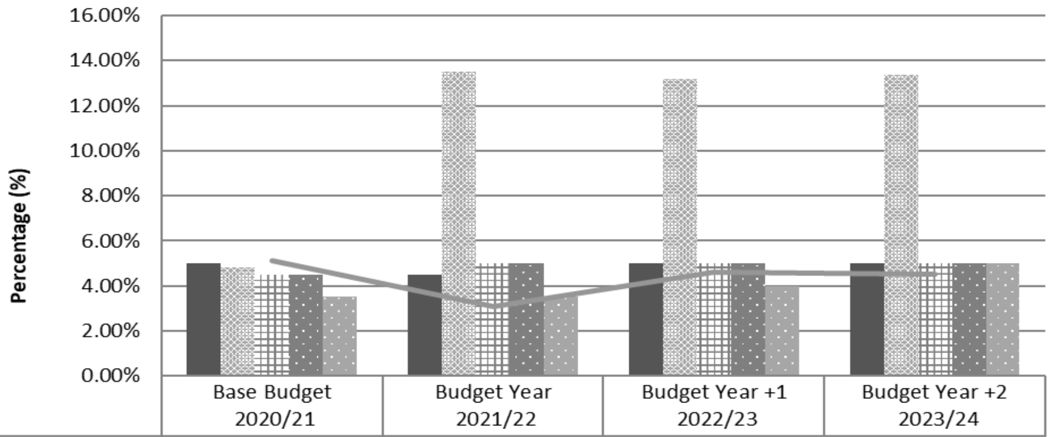
A growth of 4% is projected for water and 3% for sanitation for both the 2021/22 and 2022/23 financial years. A 2% growth is projected for both Water and Sanitation in 2023/24. The projected growth is evident in the current trends and can mainly be attributed to the expected increase in consumption as the City experiences the “bounce-back” after the drought flowing from the withdrawal of the restrictions and restriction tariffs.

Refuse

Average revenue growth over the last 3 years showed a consistent 2% growth for Refuse revenue. Based on this a 2% growth factor was applied over the 2021/22 MTREF. Waste disposal, however, showed no increase over the last 3 years therefore no growth is projected for Disposal over the MTREF period.

b) Major tariffs and charges: Rates and Trading services

National Treasury, in NT MFMA Circular 107, encourages municipalities to maintain tariff increases at levels that reflect an appropriate balance between the affordability to poorer households and other customers while ensuring the financial sustainability of the municipality. The Consumer Price Index (CPI) inflation is forecasted to be within the lower limit of the 3% to 6% target band; therefore, municipalities are required to ***justify all increases in excess of the projected inflation target for 2021/22*** in their budget narratives and pay careful attention to tariff increases across all consumer groups.



	Base Budget 2020/21	Budget Year 2021/22	Budget Year +1 2022/23	Budget Year +2 2023/24
Property Rates	5.00%	4.50%	5.00%	5.00%
Electricity	4.83%	13.48%	13.18%	13.36%
Water	4.50%	5.00%	5.00%	5.00%
Sanitation	4.50%	5.00%	5.00%	5.00%
Refuse	3.50%	3.50%	4.00%	5.00%
City's CPI projection	5.10%	3.10%	4.60%	4.50%

Figure 1 Revenue parameters for the MTREF period

Property Rates

The revenue parameter for Property Rates over the 2021/22 financial year is at level below the upper limit of the inflation target range. This lower increase was achieved by implementing various cost saving initiatives to counter the reduction in supplementary revenue sources such as the Fuel levy, LGES and investment income. The increase of 4.5% for 2021/22 will allow for the continuation of providing Rates-funded services, further investment in initiatives such as COVID-19 pandemic related requirements, servicing of new informal settlements, ongoing investment in repairs and maintenance and various safety and security operations.

Electricity

On 16 February 2021 NERSA was ordered by the High Court of South Arica to add R10 billion to Eskom's allowable revenue to be recovered in the 2021/22 financial year. This also follows the approval of Eskom's Regulatory Clearing Account (RCA) applications for year 2 (2014/15), year 3 (2015/16) and year 4 (2016/17) of the third Multi-Year Price Determination (MYPD3) period and Eskom's supplementary tariff application for the 2018/19 financial year of R4 749 million and R1 288 million respectively, be recovered in the 2021/22 financial year. A municipal guideline increase of 14.59% was approved by NERSA according to the Guideline on municipal electricity price increases for 2021/22 dated 15th May 2021.

The nature of business for the Electricity service is the purchasing and redistribution of electricity, where bulk purchases averages 65% of the services budget. The Electricity revenue increase is therefore mainly as a result of the Eskom approved average increase of 17.8% on bulk purchases.

The full impact of this increase was however not carried over to the consumer. In an effort to lower revenue increases, the Electricity department implemented cost saving measures on various expenditure types, such as reducing the staff budget, but also improved on the collection of debt. Based on the above, the electricity average revenue increases are 13.48%, 13.18% and 13.36%, respectively over the 2021/22 MTREF.

Water and Sanitation

NT MFMA Circular 99 stated that "*Municipalities should take strategic action to ensure effective water management and resilience to drought, including the security of water supply, environmental degradation,* *and pollution of resources to achieve economic growth, development and socio – economic priorities in an equitable and sustainable manner."*

The average revenue increase applied over the 2021/22 MTREF period for water and sanitation is 5% annually. To ensure the lowest revenue increase was achieved, expenditure was reduced while still ensuring that the strategic imperatives of the service could continue. The revenue increase makes provision for, amongst other, the following:

- To ensure sustainable and resilient provision of water, budgetary provision for the New Water Plan was made, which includes initiatives to further invest in the underground extraction of water from aquifers;
- Water demand management to limit the abuse and loss of water;
- Upgrades and extensions to the wastewater treatment plants;
- Continued investment in asset replacement programs to ensure proper asset management;
- Ongoing investment in repairs and maintenance program and maintaining required compliance standards;
- Supplying water and sanitation at appropriate compliance, capacity, skills, service delivery and responsiveness levels; and
- COVID-19 pandemic requirements which has been incorporated into permanent aspects of the service levels.

Refuse

Guidance on budgeting for Solid Waste matters was provided in NT MFMA Circular 99 stating that "*Investments in waste collections and treatment infrastructure should be made in tandem with industrial and urban developments to minimise pollution to our land and waters*". In this regard, the following revenue increases are projected for Solid Waste Management over the 2021/22 MTREF.
Solid Waste consists of three services of which two are tariff-funded and one funded by Property Rates. The tariff funded services consists of Refuse and Disposal.

Refuse service charges is the revenue received for the removal of waste from residential and non-residential properties. The Refuse average increase is 3.50% for 2021/22 and averages 4.50% over the two outer years. The average increase will fund, inter alia, the upgrading of drop-off facilities to accommodate the expansion of the service, continuous implementation of waste minimisation initiatives, upgrading of depots, maintenance programs and the typical day-to-day service operations.

Disposal service charges is the revenue received for the disposal of waste from residential and non-residential properties. The Disposal average increase for 2021/22 is 4.41% whereas the increases for the two outer years are 8.94% and 8.91% respectively. These increases are required for the continued operational requirement of the service, the development of landfill infrastructure, development and upgrading of transfer stations, plant replacement, additional Material Recovery Facilities and Landfill Gas generation to beneficiation at all landfill sites.

Housing rental (Council rental properties)

The monthly rental charge for housing rental properties is based on a rate per square meter applied to the size of the unit being rented, coupled with a set of premiums/deductions based on the location, maintenance level, facilities et al of the specific property for which the rent is charged.

Through addressing the economic challenges faced by many poorer communities residing in, particularly, the City's rental stock, the average total monthly rental charge percentage increase associated with the City's rental properties has been retained at an affordable level and is based on an annual increase of 3.13% (where the unit has a separate water meter) or 3.49% (for those units which include water in the rental charge) for 2021/22.

The projected rental charge increase is lower than CPI, due to rental units operating on a City-subsidised basis.

Tenants who are occupying rental properties since 2007 receive a subsidy of 20% of the rental charge, this being the final portion of the phase-out program, which was not fully implemented by the City to facilitate affordability of long standing tenants. This key initiative, reflected within the City's Credit Control and Debt Collection Policy, supports affordable rentals to many poor communities and the City's initiatives in terms of its housing debt collection drives whilst supporting the City's housing debtor book that it does not unduly increase due to, potentially, unreachable charges.

The proposed 2021/22 housing rental charge is in line with previous annual rental increases and is again aimed at ensuring affordability for the City's poorer communities. The rental rate (per square meter per month) is R11.62 (where the unit has a separate water meter) or a rental charge (including water charge where applicable) of R19.70 per square meter per month.

The City's housing premiums and deductions charge structure addressing the variations in the City's diverse rental properties remains as follows:

- Discounts on account
  - Outside toilet (R20 per month)
  - External Water (R30 per month)
  - No ceiling (R15 per month)
- Premiums on account
  - Saleable unit (R4,50 per month)
  - Well maintained (R5 per month)
  - Local environment (R3,50 per month)
  - Well located (R5 per month)
  - Hot water cylinder (R4 per month)

A surcharge for tenants earning a monthly income above the rental income threshold (R3 500) is charged at a stepped rate of 8% for those earning R3 501 – R7 500 and 10% for those earning R7 501 – R10 000. Tenants who earn more than R10 000 per month will pay a surcharge of 25% of the amount above R10 000. A two (2) year lease agreement will be signed, which will not be renewed if the income remains more than R10 000.

Capital funding

The capital budget was prepared considering very strict assessment criteria to ensure affordability and the ability to implement the capital budget. In this regard the Project Readiness Assessment (PRA) tool were used. The PRA tool took into consideration matters such as the procurement and implementation readiness, technical, financial feasibility and strategic alignment. The capital budget was adjusted in the 2021/22 January adjustments budget to the following for the 2021/22 MTREF.

Table 3 Capital Budget over MTREF

Funded by: **R Thousand**	**Budget Year 2021/22**	**Budget Year+1 2022/23**	**Budget Year +2 2023/24**
Transfers recognised - capital	1 792 589	2 964 846	2 855 179
Borrowing	1 200 000	4 500 000	7 000 000
Internally generated funds	3 102 526	1 569 035	1 766 299

Total	6 095 115	9 033 880	11 621 478

1.6 2021 Division of Revenue Act (DoRA) and Fuel Levy

Equitable Share

In terms of Section 227 of the Constitution, local government is entitled to an equitable share of nationally raised revenue to enable it to provide basic services and perform its allocated functions. The local government equitable share is an unconditional transfer, which supplements the revenue that municipalities can raise themselves (including revenue raised through property rates and service charges).

NT MFMA Circular 107 indicated that the local government equitable share formula has been updated to account for projected household growth, inflation and estimated increases in bulk water and electricity costs over the MTEF period. Furthermore, according to the 2021 National Budget review document to implement government strategy of fiscal consolidations, equitable share decreases by 1% over the next three years. The equitable share allocation to the City is therefore much lower than the indicative allocations reflected in the 2020 DoRA. The 2021 DoRA provides for the following allocations, which have been included in the City's MTREF:

- 2021/22 – R3 215 million
- 2022/23 – R3 455 million
- 2023/24 – R3 506 million

Sharing of the Fuel Levy

The general Fuel Levy is legislated by the Taxation Laws Amendment Act (Act 17 of 2009), which provides that each metropolitan's share should be announced in the government gazette.

The General Fuel Levy allocation letter, as received from National Treasury for the 2021/22 MTREF, stated that the 2019 (latest) fuel volume sales were used to determine the 2021/22 sharing of the general fuel levy allocations. Due to the COVID-19 pandemic and a constrained fiscal environment, the local government sphere is subjected to budget reductions for the next MTEF period. These reductions will also have an impact on the sharing of the general fuel levy allocations with all the metropolitan municipalities. Based on the data and the phasing-in approach the sharing of the general fuel levy allocations was provided for metropolitan municipalities.

In addition, the allocation letter further advises municipalities that the allocations for the two outer years of the 2021 MTEF are provisional and that actual allocations will be based on fuel sales.

The following amounts allocated to the City, as per the 2021/22 allocation letter, was included in the City's MTREF:

- 2021/22 – R2 609 million
- 2022/23 – R2 713 million
- 2023/24 – R2 706 million

1.7 Major parameters

The following table summarises the major parameters applied to the 2021/22 MTREF operating budget as per the 2021/22 January adjustments budget:

Table 4 Summary of parameters applied to Operating Budget

	Budget Year 2021/22	Budget Year +1 2022/23	Budget Year +2 2023/24
CPI	**3.10%**	**4.60%**	**4.50%**
COLLECTION RATES			
Rates	95.14%	95.59%	96.04%
Electricity	99.00%	98.50%	98.50%
Water	91.00%	89.00%	92.00%
Sanitation	93.00%	89.00%	92.00%
Refuse	90.00%	85.00%	85.00%
REVENUE PARAMETERS			
Rates	4.50%	5.00%	5.00%
Electricity	13.48%	13.18%	13.36%
Water	5.00%	5.00%	5.00%
Sanitation	5.00%	5.00%	5.00%
Refuse	3.50%	4.00%	5.00%
Disposal	4.41%	8.94%	8.91%
GROWTH PARAMETERS			
Rates	0.00%	0.00%	0.10%
Electricity	0.00%	-1.50%	-1.50%
Water	4.00%	4.00%	2.00%
Sanitation	3.00%	3.00%	2.00%
Refuse	2.00%	2.00%	2.00%
EXPENDITURE PARAMETERS			
Salary increase			
Salary increase (SALGBC Agreement)	3.50%	4.40%	4.60%
Increment provision	2.00%	2.00%	2.00%
Operational cost	Differentiated	Differentiated	Differentiated
Repairs & Maintenance	Differentiated	Differentiated	Differentiated
Interest Rates			
Interest paid	11.00%	11.00%	11.00%
Interest on investment	4.02%	4.48%	4.48%
OTHER			
Capital Borrowing expenditure	R1.200bn	R4.500bn	R7.000bn
Equitable Share Allocation	R3.215bn	R3.455bn	R3.506bn
Fuel levy	R2.609bn	R2.713bn	R2.706bn