

Impact of the proposed increase in electricity tariffs on the agricultural sector – Presentation to NERSA

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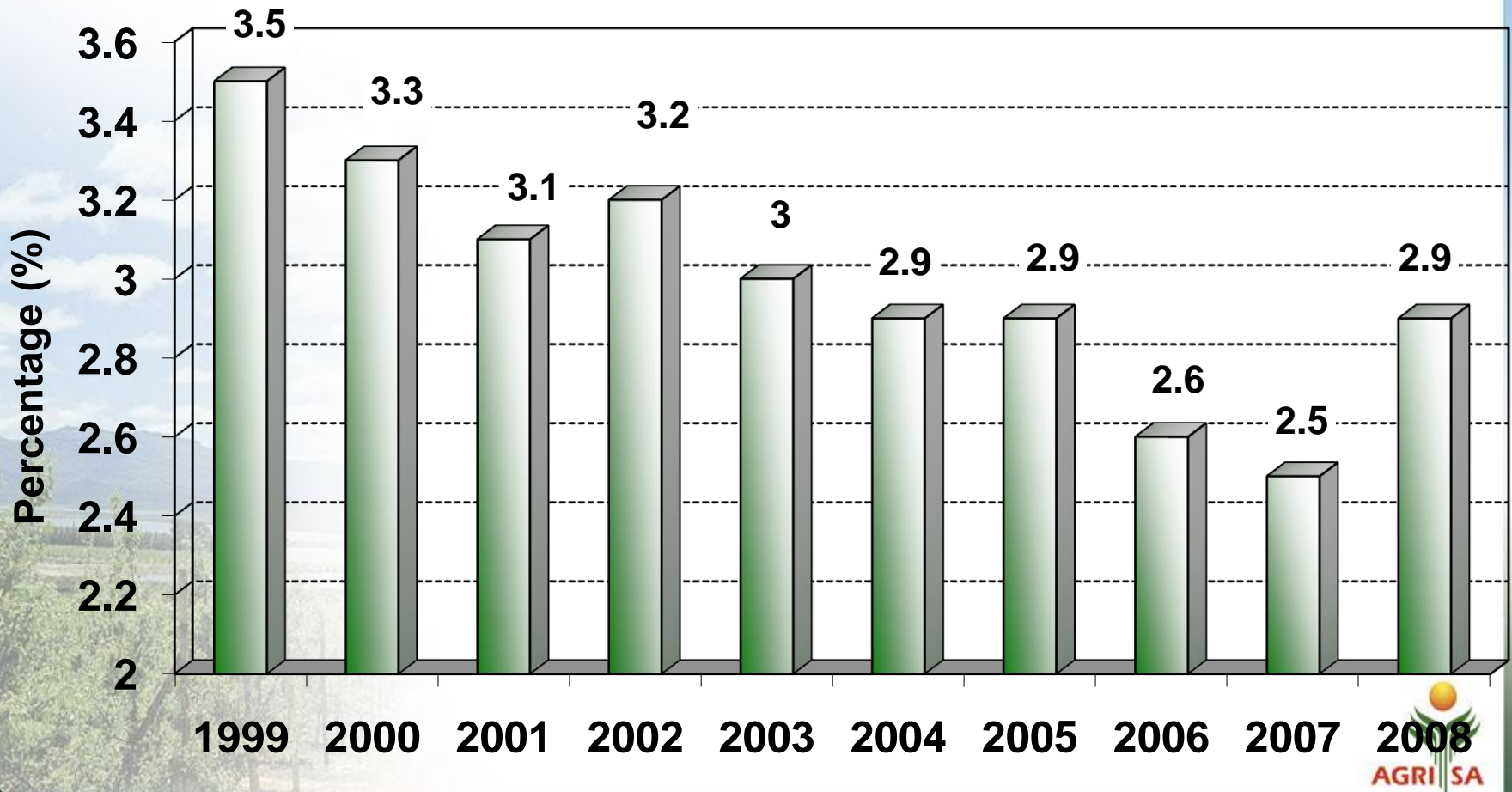


Agri SA

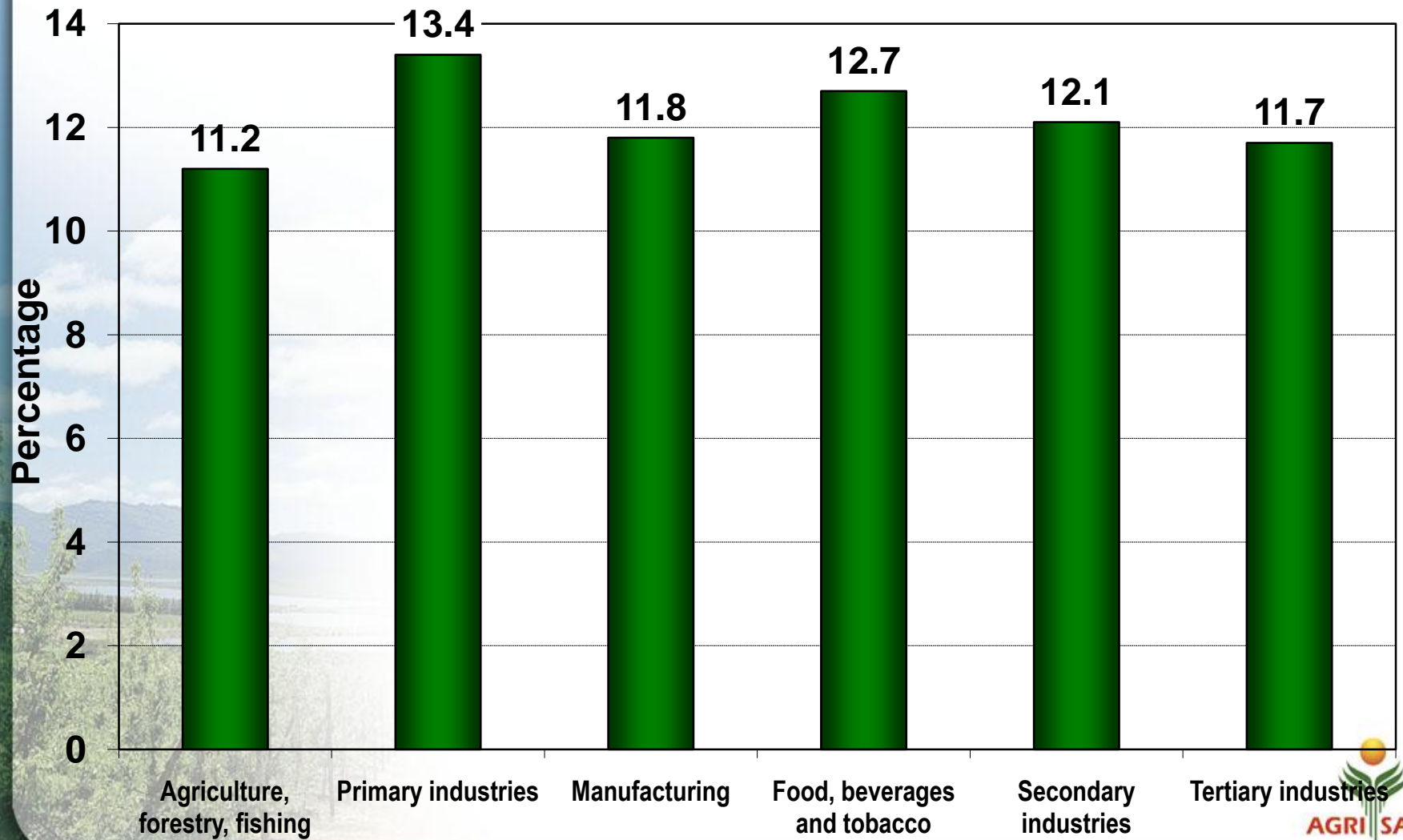
- Agri South Africa is a federal organisation, which promotes on behalf of its members, the sustainable profitability and stability of commercial agricultural producers and agribusinesses through its involvement and input on national and international level
- Represent commercial and emerging farmers through:
 - *9 provincial unions*
 - *26 commodity organisations*

Contribution of agriculture to the gross domestic product in SA, 1999 to 2008

(At constant 2000 prices)



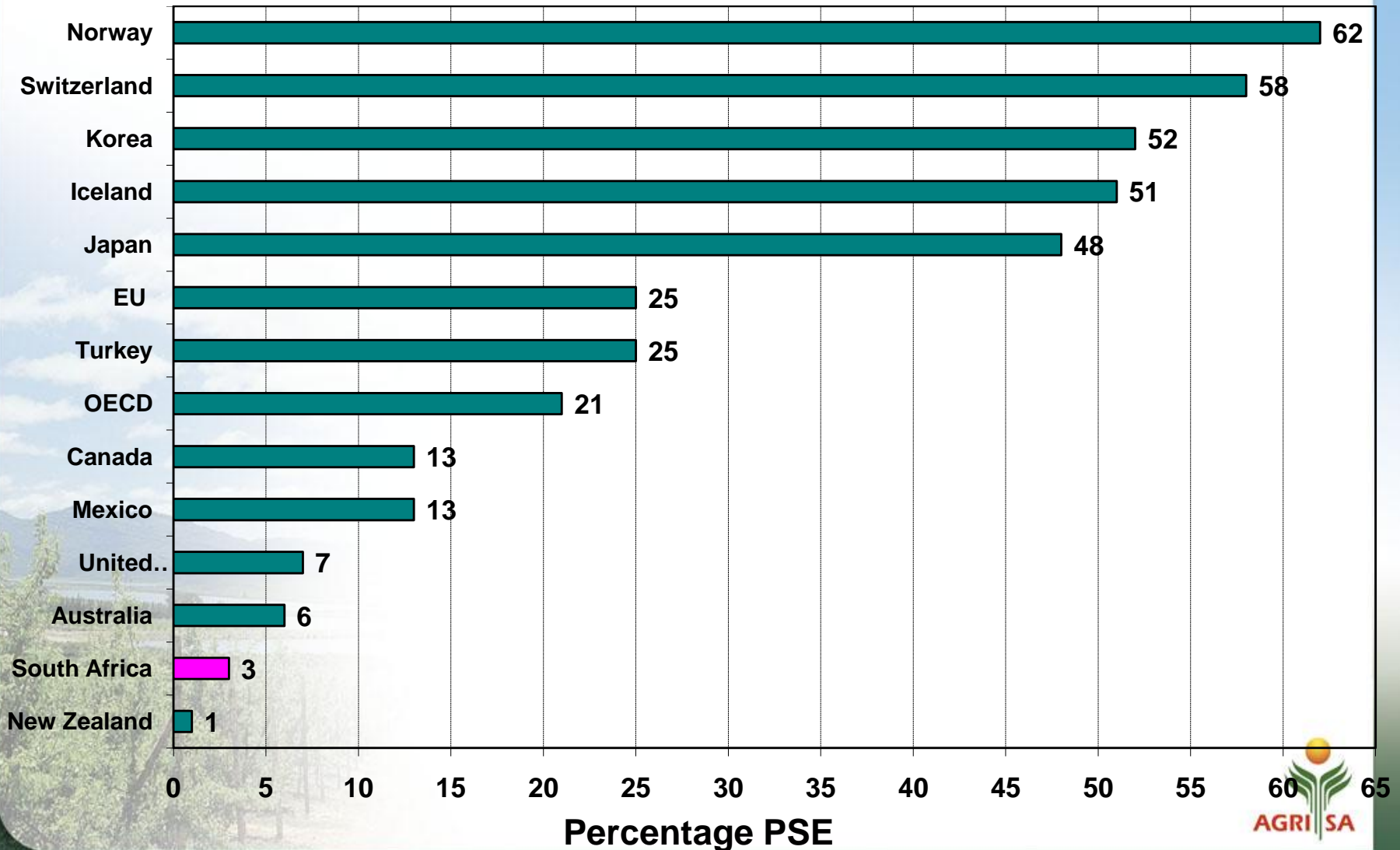
Value added per sector, 2001 – 2008 (Percentage growth)



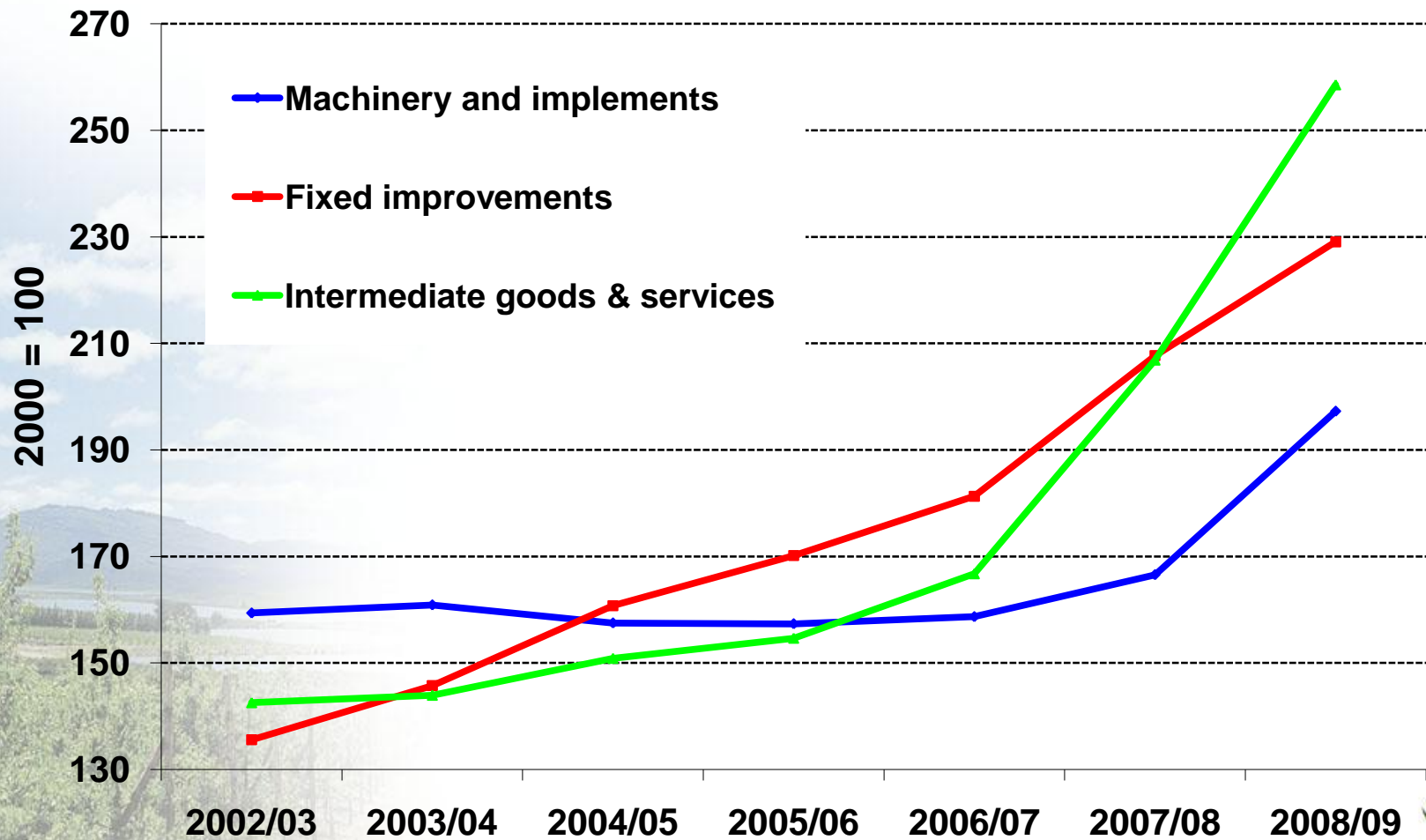
The Producer Support Estimate (PSE) is an indicator of the annual monetary value of gross transfers from consumers and taxpayers to support agricultural producers, measured at farm gate level, arising from policy measures, regardless of their nature, objectives or impacts on farm production or income.



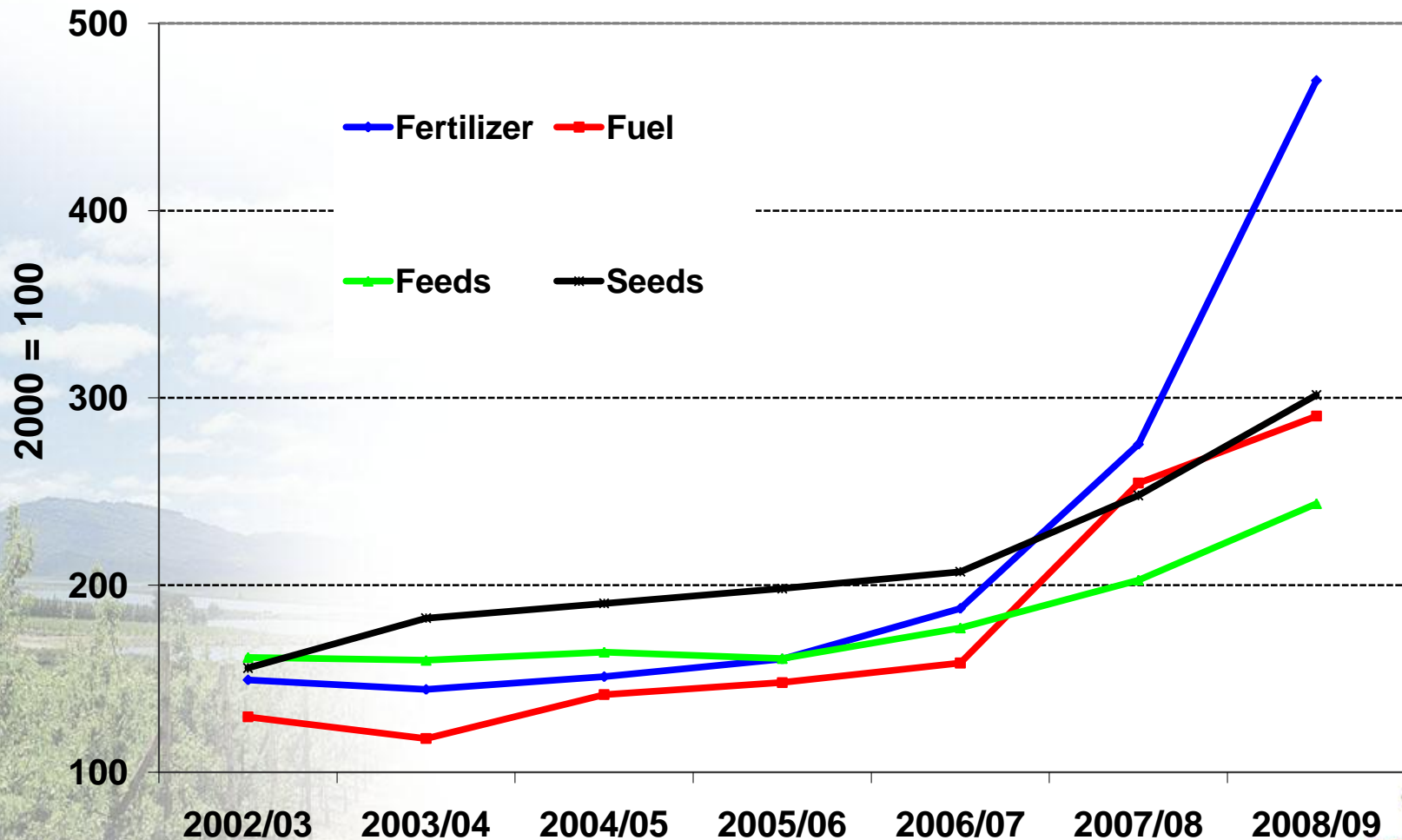
Estimates of support to agriculture in selected non-OECD and OECD countries (2008)



Price index of farming requisites (2002/03 – 2008/09)



Price index of farming requisites (2002/03 – 2008/09)



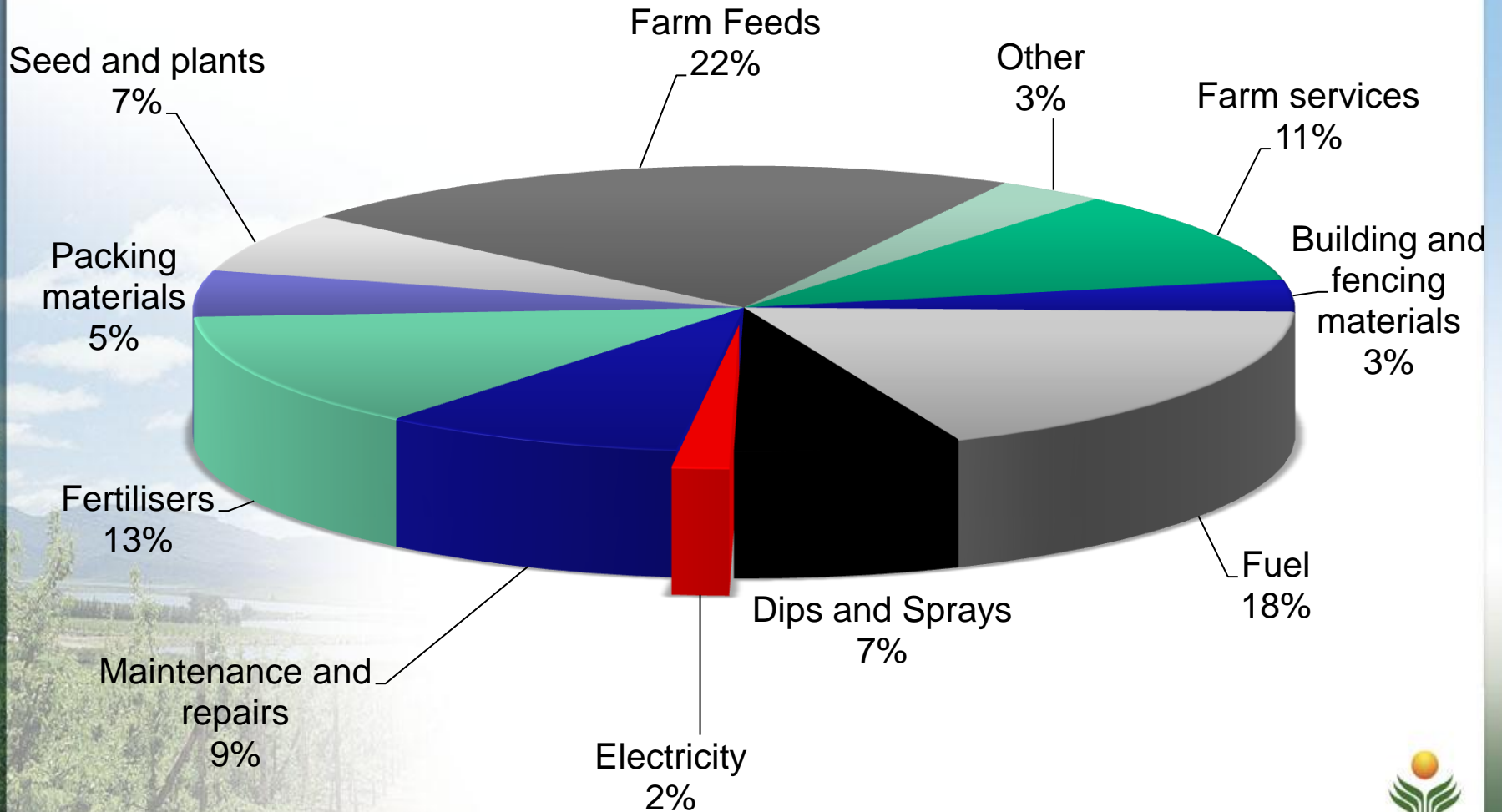
Expenditure on intermediary goods and services, interest, labour and investment in vehicles, machinery and implements

	2007/08 R'million	2008/09 R'million	% Change
Farming services	6336.6	7500.9	18.4
Fuel	8387.2	12705.1	51.5
Dips and sprays	3591.4	4641.5	29.2
Electricity	1011.7	1163.5	15.0
Maintenance and repairs	5212.9	6213.5	19.2
Fertilisers	7691.5	9163.9	19.1
Seed and plant material	3855.7	4781.1	24.0
Farm feed	14111.6	15263.1	8.2
Total: Intermediary goods and services	57485.7	69862.2	21.5
Labour costs	11119.8	11564.6	4.0
Interest	4364.1	5018.8	15.0
Gross Investment: Vehicles, machinery, implements	6242.3	7788.7	24.8

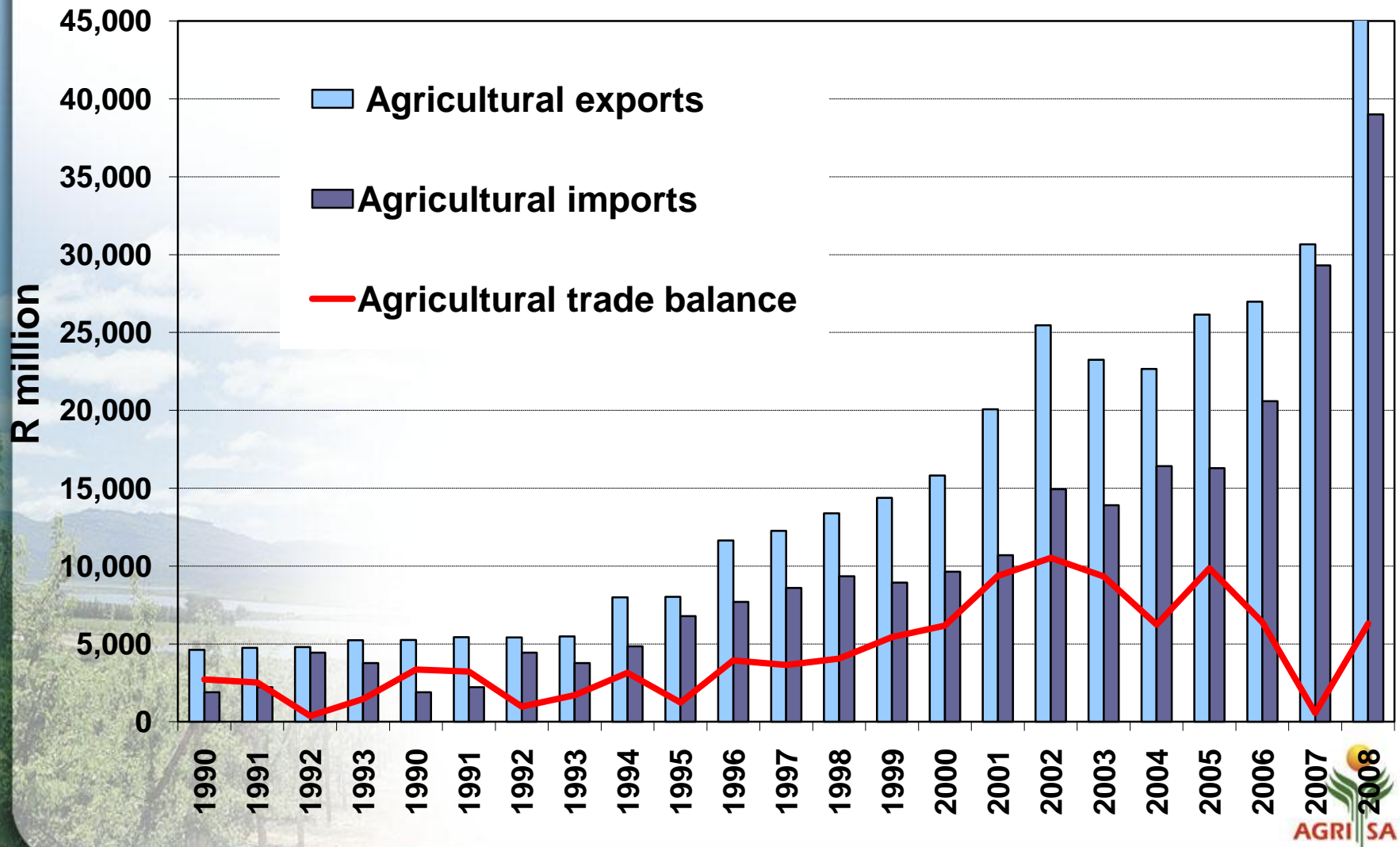


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Expenditure on intermediate goods and services (2008/09)

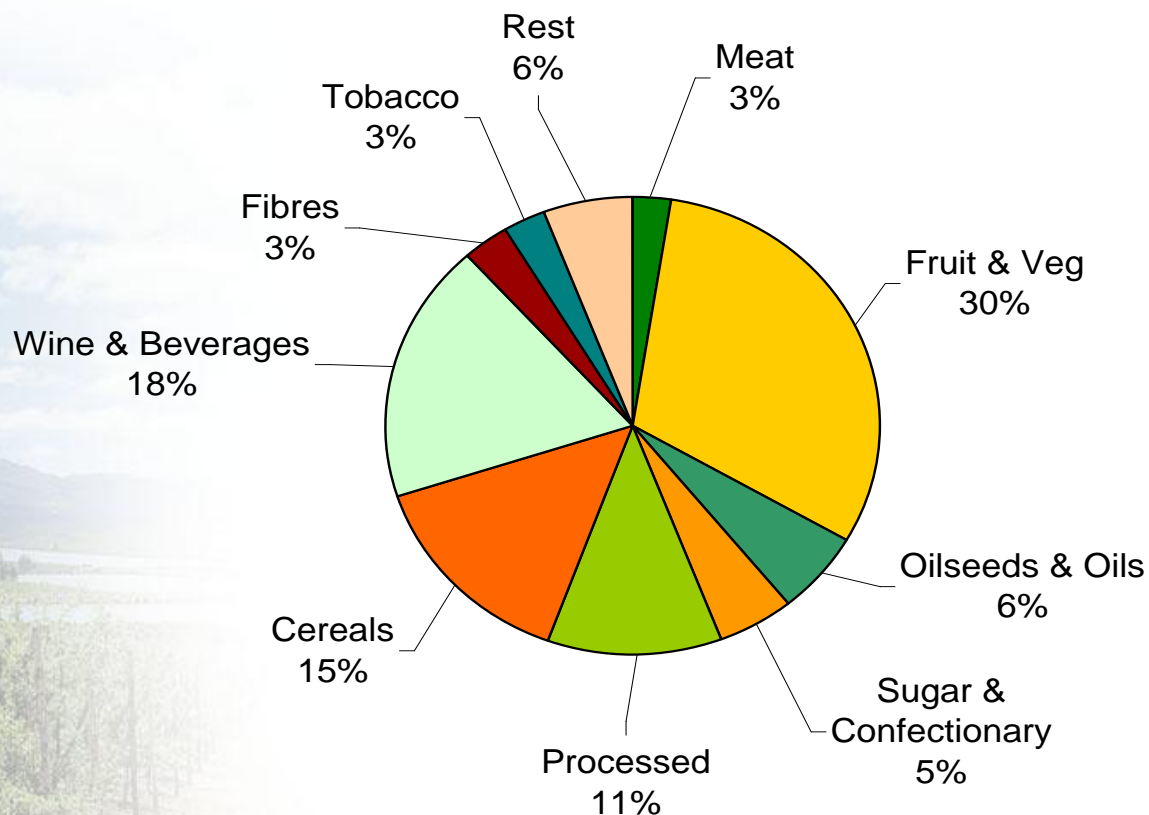


South African Agricultural exports and imports, 1990-2008



Change in structure of product exports

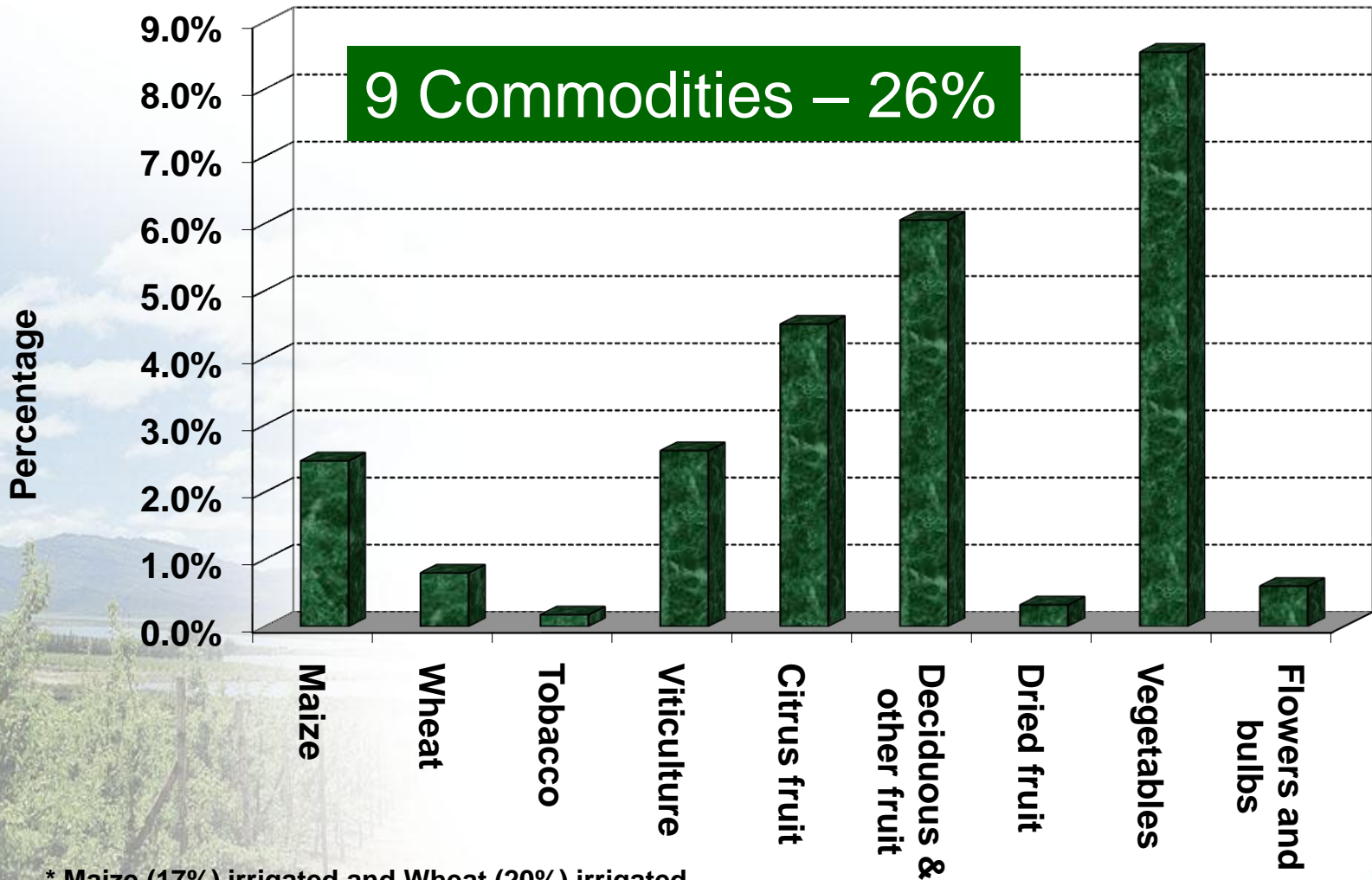
EXPORT COMPOSITION OF AGRICULTURAL PRODUCTS, 2008



Electricity in Agriculture

- Agriculture use <5% of national electricity

Value of Commodities under irrigation as percentage of total gross income of agriculture

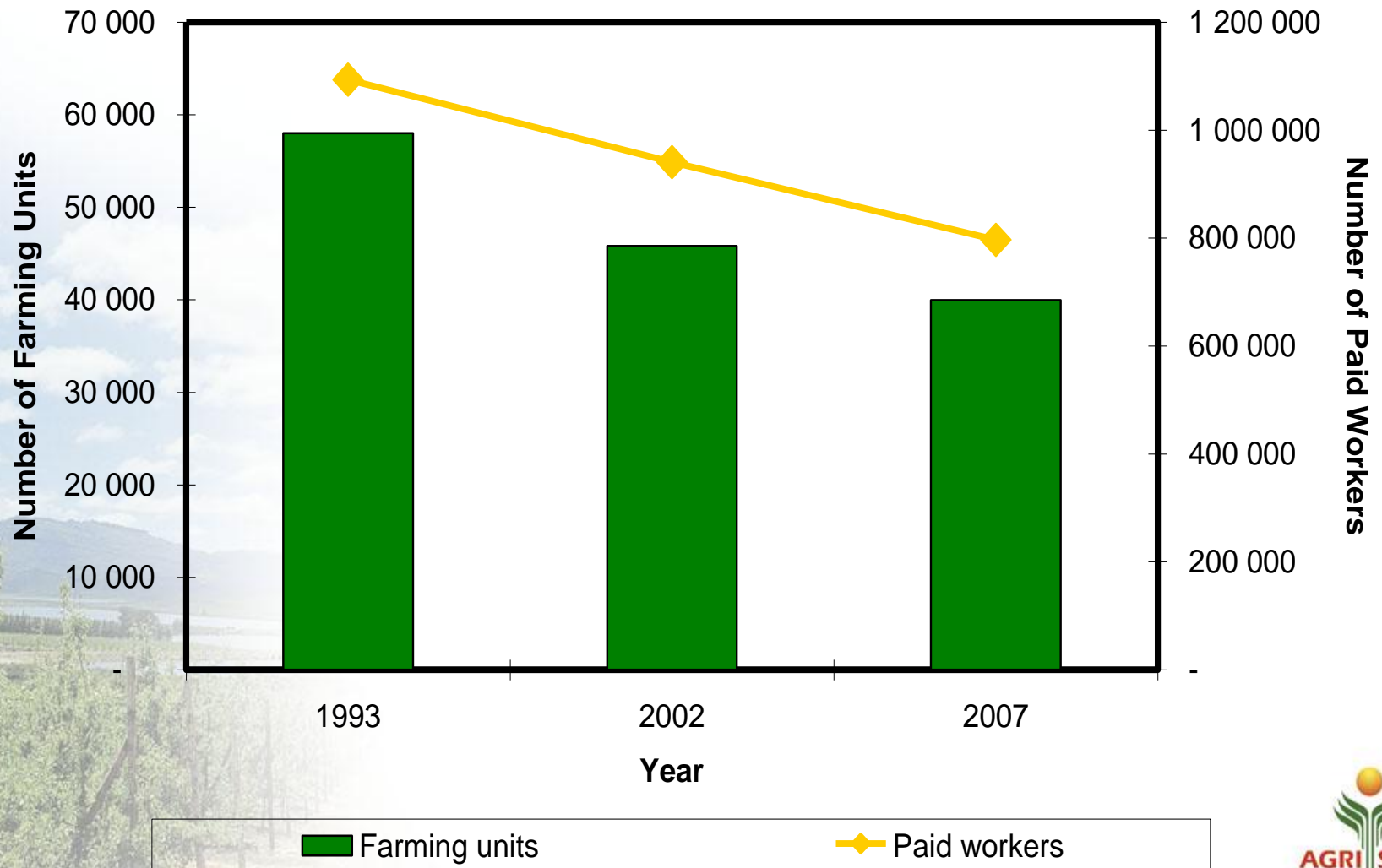


* Maize (17%) irrigated and Wheat (20%) irrigated



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FARMING UNITS AND EMPLOYMENT IN SA AGRICULTURE - 1993, 2002 & 2007



Impact on some important irrigation industries

- Deciduous fruit
- Maize
- Wheat
- Dairy
- Wine industry

Sources

- Agri SA Provincial Affiliates
- Milk Producers' Organisation
- Hortgro
- Grain SA
- Wine Cellars South Africa

Context

- Input prices will rise in 2010 (10%+)
- Administered prices (e.g. minimum wages) will probably increase in real terms
- Water tariffs will increase up to 50% in some cases
- Exchange rates remain strong
- International commodity prices low

Deciduous fruit*

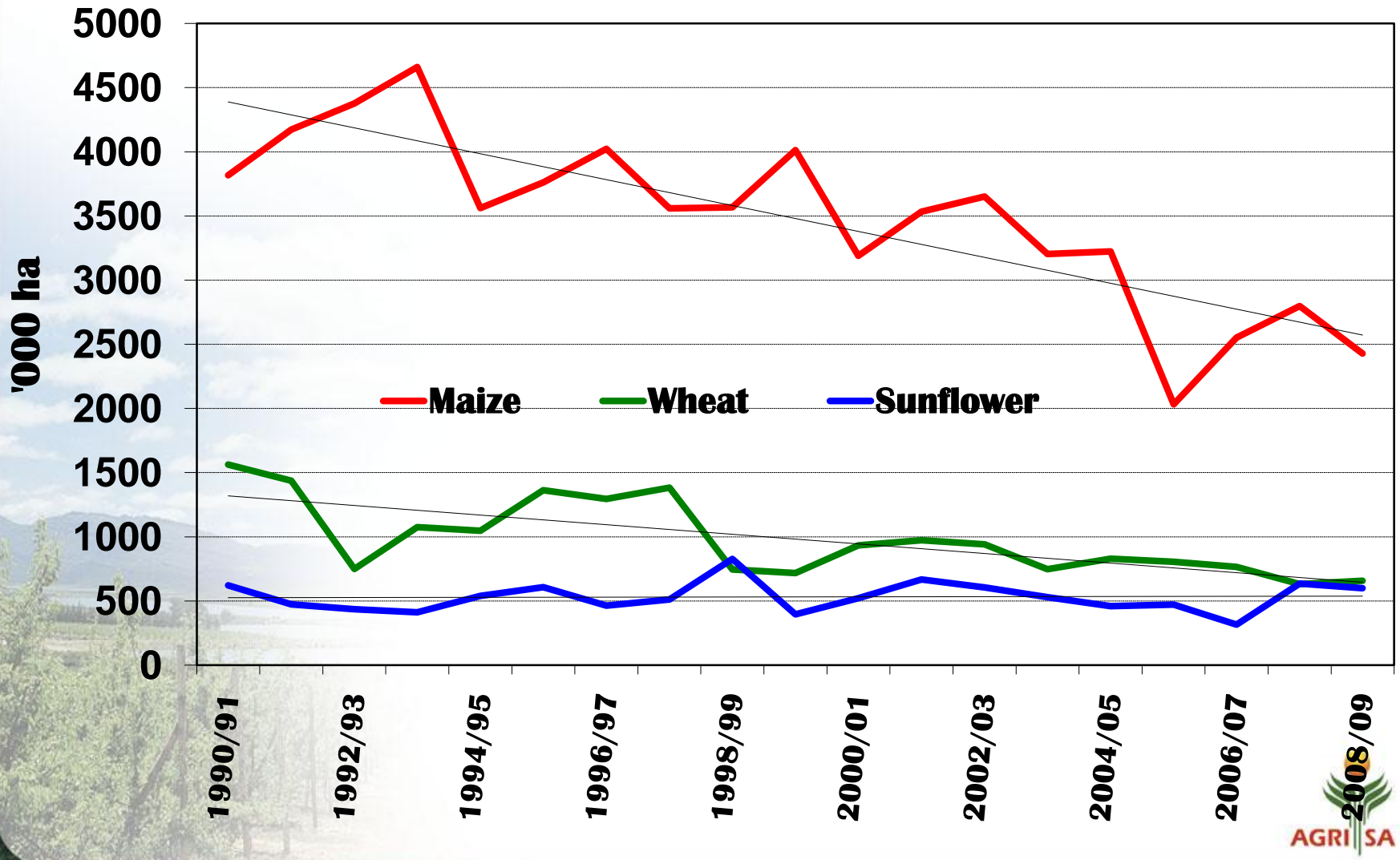
Fruit	Current profit	Year 1	Year 2	Year 3
	R/ha	35%	35%	35%
Dried grapes	7 316.58	5 215.52	4 480.15	3 487.40
% Change in profit	-	-28.72	-38.77	-52.34
Apples	29 162.23	27 672.06	27 150.50	26 446.39
% Change in profit	-	-5.11	-6.90	-9.31
Pears	11 724.68	10 572.06	10 168.64	9 624.03
% Change in profit	-	-9.83	-13.27	-17.92
Peaches & Nectarines	11 465.72	10 082.58	9 598.48	8 944.94
% Change in profit	-	-12.06	-16.29	-21.99

* Only expected increases in electricity tariffs taken into account. Prices of other inputs assumed constant.

Deciduous fruit

- Substantial losses in profits
- Employment:
 - *Current = 100 798 direct permanent jobs*
 - *Increasing tariffs can lead to substantial job losses*
- Long term sustainability under pressure
- Earnings of foreign exchange can be negatively affected

AREA PLANTED, 1990/91 TO 2008/09



Wheat

	Income	Variable Input Costs	Gross Margin	Net Profit	Change
	R/ha				%
Current	15 639.00	10 819.78	4 819.22	1 848.24	-
Year 1	15 639.00	11 232.88	4 406.12	1 435.14	-22.35
Year 2	15 639.00	11 831.87	3 807.13	836.15	-54.76
Year 3	15 639.00	12 700.41	2 938.59	-32.36	-101.75

- Yield = 6.5t/ha
- Other input costs constant (highly unlikely)

Maize

	Income	Variable Input Costs	Gross Margin	Net Profit	Change
	R/ha				%
Current	12 979.50	12 428.13	551.37	-1 434.97	-
Year 1	12 979.50	12 988.13	-8.63	-1 994.97	-39.03
Year 2	12 979.50	13 744.13	-764.63	-2 750.97	-91.71
Year 3	12 979.50	14 764.73	-1784.23	-3 770.57	-162.76

- Yield = 10t/ha
- Other input costs constant (highly unlikely)

Grain

- Grain is most important sector in agriculture
- Severe negative impact on profitability
- Employment = 108 000 jobs
 - *Could lead to job losses*

Dairy

	Current	Year 1	Year 2	Year 3
	R/litre			
Estimated direct electricity cost	0.25	0.34	0.46	0.62
Indirect impact	-	0.01	0.01	0.01
Total cost increase	-	0.10	0.22	0.38
Average net farm income	0.20	0.20	0.20	0.20
Net farm income after price increase		0.10	-0.02	-0.18

Dairy

- Employment
 - *Direct = 35 000 jobs (210 000 dependants)*
 - *Indirect = 67 000 up- and downstream*
- Economic contribution
 - *GDP multiplier = 1.30 (If sales of milk increase by R 1.00, total GDP will increase by R 1.3004)*
- Tariff increase will jeopardize milk production in most areas
- Impact negatively on growth in secondary industry

Wine Industry

	2009	2010	2011	2012
Average expenses per cellar				
Electricity	559,638.10	755,511.44	1,019,940.44	1,376,919.59
Other expenses	18,792,256.98	19,919,792.40	21,114,979.94	22,381,878.74
Total expenses (excluding paid for wine/grapes)	19,351,895.08	20,675,303.83	22,134,920.38	23,758,798.33
Percentage of total expenses	3%	4%	5%	6%
Average electricity cost per ton				
Average tons pressed per cellar	16 360			
R/ton	34	46	62	84
Cumulative decrease in income (R) per ton	-	12	28	50

Summary: Electricity tariff increases

- Electricity costs in the sector will increase from the current level of R1,16 billion to R2,85 billion over the next 3 years – an effective increase of approximately R1,7 billion or 146%.
- Can the sector recover such cost increases by commodity price adjustments? No, farmers are price takers!
- Evenly spread across the sector the particular tariff hikes will have a more tolerable impact but the incidence will mostly be on 25-30% of agricultural production i.e. irrigation.
- Calculations presented today and by our affiliates at previous public hearings emphasize the devastating impact the tariff hikes will have on certain sub-sectors of agriculture.

Summary: Electricity tariff increases (cont.)

- A hopefully worst case scenario, but certainly not an unrealistic one, will entail a drastic decrease in production under irrigation and the agricultural sector turning from a net exporter to a net importer of agricultural products. National self-sufficiency of food in South Africa will be undermined if not terminated.
- Food prices on retail level will most certainly, due to the likely production limiting impact in primary agriculture and the cost increase in the food chain, show drastic increases.
- The extensive part of agricultural production is for obvious reasons also the most volatile part of agriculture. If irrigation i.e. the stable part of the sector is jeopardised, total production and prices will obviously also become more volatile.

Summary: Electricity tariff increases (cont.)

- Due to, amongst other economic reasons, the sector experienced serious labour shedding in recent times (from 940 820 in 2002 to 796 806 in 2007). The sector is still disproportionately labour intensive, which indicates that further decreases in labour utilization because of electricity tariff hikes is a real possibility.
- In our response to the MYPD questionnaire we proposed a combination of equity, guaranteed debt and funding involvement through loans at zero interest by the Reserve Bank. We expressed reservations about the need for a real return on capital given the current crisis, as well as on items like road maintenance costs to be included in OPEX.

Summary: Electricity tariff increases (cont.)

- The fact that the agricultural sector is a relatively small consumer of electricity implies that a more lenient approach towards the sector will have a relatively small overall impact on Eskom's financial position. Consideration of the PCP program seems to have acknowledged this peculiar nature of agriculture. We trust that further options to deal with the sector, especially to mitigate high financial demands on the sector, will be seriously considered by NERSA.

Thank you

