ANNUAL REPORT FOR THE YEAR ENDED 30 JUNE 2009

A. FINANCIAL STABILITY

INTRODUCTION

The year has seen the credit crunch loom large, and increasing signs of a faltering economy – factors that will also have had an impact on the municipalities cash flow and collection rates.

Against this backdrop we've performed well. We have sustained a solid cash flow, collection rates are reasonable, 100% of the capital budget was spent and capital expenditure was fully funded.
We have achieved a credit rating of A1 for the short term and AA- for the long term.

In the current year the annual financial statements were prepared in full compliance with the GRAP accounting framework. The basis of accounting is consistent with prior years with the exception that no exemptions were issued by National Treasury for the current year.

1. FINANCIAL RATIOS BASED ON KEY PERFORMANCE INDICATORS

	R'000	2009	2008
Debt Coverage		**19.21**	**19.52**
Total operating revenue	17 033 579		
Grants and Subsidies	3 868 780		
Debt service payments (i.e. interest + redemption) due within the financial year	685 484		
Outstanding service debtors to revenue		**38.52**	**36.64**
Total outstanding service debtors	3 946 940		
Annual revenue actually received for services	10 246 036		
Cost Coverage		**3.47**	**6.91**
All available cash at year end	7 225		
Investments	2 969 122		
Monthly fixed operating expenditure	858 018		

The debt coverage and Outstanding service debtors to revenue indicators have remained fairly constant in relation to the prior years performance.

The decrease in cost coverage is due to the R1.8 billion rands decrease in investments and 22% increase in monthly fixed operating expenditure.
The decrease in investments is as a result of the utilisation of cash from investments utilized to fund capital expenditure as opposed to increasing external borrowings.
The main reason for the increase in monthly fixed operating expenditure is due to a 35% increase in the electricity bulk purchases cost which is a direct result of the substantial tariff increases by Eskom.

2. CREDIT RATING 2009/10

Global Credit Rating Co. (GCR) recently reviewed the credit ratings for Ethekwini Municipality, following a detailed analysis of the Municipality's 2008/09 financial statements and medium term expenditure budgets. GCR confirms that the ratings have been accorded as follows :

- **Long term :** The rating has been maintained in the "double A band", but lowered by one notch to AA - (double A minus), from AA (double A) previously. The rating is defined as having a very high credit quality.
- **Short term rating :** The rating has been lowered by one notch, to A1 (single A one), from A1 + (single A one plus) previously. The rating is defined as having a very high certainty of timely payment.

Rating Definitions:

Investment grade

AA + Very high credit quality. Protection factors are very strong.
AA Adverse changes in business, economic or financial conditions would
AA - increase investment risk, although not significantly.

High Grade

A1 Very high certainty of timely payment. Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

However, the downgrades are a worldwide phenomenon, affecting the financial sector as well. Five of South Africa's largest banks (ABSA, First Rand, Investec, Nedbank and Standard) had their bank financial strength ratings downgraded by Moody's Investors Services.

The Executive Vice President of Global Credit Rating Company, Marc Joffe writes :

" Notwithstanding the one notch reduction in both the long and short term ratings, however, the credit ratings are still considered very strong (as per the rating definitions), and in our opinion the municipality continues to exhibit a very high ability to honour its debt and interest repayments. Furthermore, the ratings must be viewed in light of the financial and economic challenges faced globally and the resultant spate of rating downgrades worldwide, from which the South African Local Government sector has not been immune."

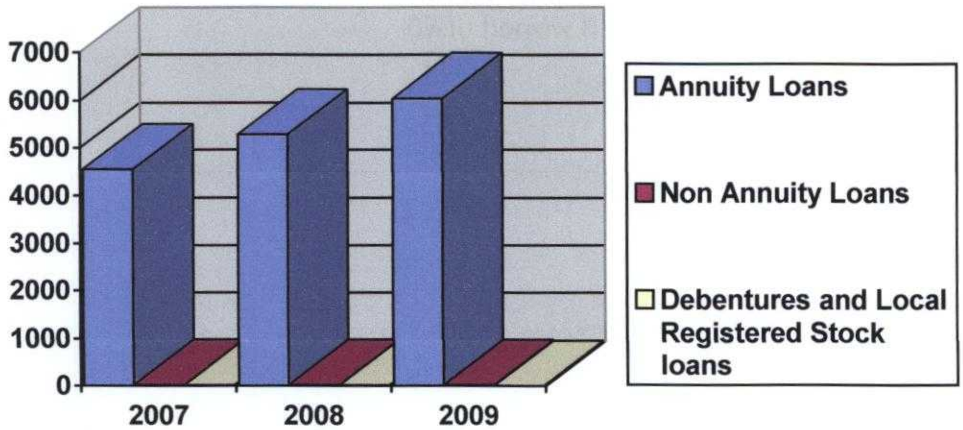
3. BORROWINGS

The Municipality entered into a loan agreement with the Development Bank of Southern Africa in November 2007 to borrow R2.9 billion at a fixed interest rate of 8.3% unsecured over 20 years.

The Municipality has made a draw down of R1, 050billion (2008:R950m) from this facility for the financial year ending 30 June 2009.
A further draw down of R300m was made on the 1st of July 2009.
It is anticipated that a final draw down of R 600 million will be made on the 30th of September 2009.

These funds will be utilised solely for the financing of Capital Expenditure.

Figure 1:ACTUAL BORROWINGS 2006/07 – 2008/09



4. PRICING OF SERVICES

In order to remain financially viable and sustainable, the municipality must generate sufficient resources. As limited scope exists to generate alternative revenue, it is necessary to increase rates and tariffs annually. The determining of tariffs is the responsibility of Council, as per the provision of the Local Government Municipal Systems Act.
Affordability was an important factor when considering the rates and tariff increases. Consideration was also given to the alignment between the resources of the municipality, level of service and customer expectations.

Rates:

The levying of rates in terms of the Municipal Property Rates Act has had an impact on the rates individual property owners were charged with effect from 1July 2008. Properties were assessed based on the market value (which had substantial gains in value); however, the gains in terms of rates revenue were limited owing to the increase in various rebates to the different classes of ratepayers. The cent in the rand (randage) was adjusted downward to compensate for the higher values. In addition, the impact on the indigent, pensioners, disability grantees and lower and middle-income ratepayers was considered to ensure a limited impact.

Service Charges:

The electricity tariffs increased by 27.25 %, which was much higher than that of previous years mainly due to the above average increase by Eskom as approved by the National Electricity Regulator.
These above average increases are expected to continue in the medium term.

The 9.9% increase in water tariffs are as a result of (amongst other factors), bulk purchase tariff increase from Umgeni Water, the water loss intervention programme, the increase in maintenance of ageing infrastructure and the roll out of infrastructure to new areas / developments.

Social Package:

Furthermore, the cost of the basic social package of R 1.107.2m in order to provide a social welfare to residents who cannot afford to pay also contributed to the need to increase tariffs. The cost of the social package was funded from the equitable share allocated to Council by National Treasury in terms of the Division of Revenue Act.

General:

The following service delivery challenges also influenced the levels of tariffs and service charges for the municipality i.e. the developmental challenge to address the service delivery backlogs in the rural areas of the municipality The declining local economy will be insufficient to absorb the unemployed and this will have a service delivery impact and harm the ability of the municipality to sustain its revenue base to finance extended services.

The other general contributory factors for the increase in levels of rates and service charges were:

Salary increase of 8.75% with effect from 1July 2008
Provision for the filling of Critical Vacancies
Rollout of infrastructure and the provision of basic services
Increased maintenance of network and structures

5. OUTSTANDING CONSUMER DEBTORS

INTERVENTION MEASURES PLANNED FOR 2009/10

GOVERNMENT DEBT

Over the years Ethekwini Municipality has developed a good relationship with the Provincial and National Government. There have been notable successes in recovering outstanding debts, however there is still a number of unresolved issues. One of the most pertinent issues is the debt accumulated over a number of years on hostels. Discussions will continue to resolve the impasse. By the end of the financial year other long outstanding debts will be resolved e.g. outstanding rates on schools.

COUNCIL PROPERTIES

Council properties are not rateable as per the rates policy, except properties owned by trading services.

ARREST A DEBT

The process of sending redline, final demand letters and summons is being automated so that more customers are targeted. The main intention of the Municipality is to contain debt on customers so that it doesn't become too large to manage.

MAJOR DEBTORS

Customers that fall under this category are those that own more than 50 properties. These customers are able to pay provided they get correct accounts, and their queries are resolved on time. More emphasis will be put in to resolve all outstanding queries so that these accounts are always up to date.

DISCONNECTIONS/10 DAY CHECK

There is a focus on ensuring that disconnection of services for non-payment of accounts is done immediately and effectively. There will be an immediate follow up on those customers that have been disconnected and have not made any arrangements to pay debts.

TOP DEBTS

Top debtors are those customers that owe the municipality large amounts. The Credit Control section focuses on these debtors in terms of the 80/20 principles.

LEGAL PROCESS

MPRA repealed Section 105 of DEP whereby all customers that were in arrears were taken to court at the same time and judgement was taken on all of them. This process was effective because it targeted a number of customers at the same time. The Municipality could not continue with this process, as the legislation is no longer applicable. Council is required to take individual owners to court to recover outstanding funds, which is an onerous process. Senior Counsel has been engaged to assist in the preparation of documents to attempt to revive Section 105.

REASONS FOR REDUCTION IN COLLECTION RATE

a) IMPLEMENTATION OF MUNICIPAL PROPERTY RATES ACT (MPRA)

The implementation of MPRA had a substantial negative impact in the collection rates of our debtors. The Municipality had to value properties on market value for the first time. Body Corporates that were sectionalized were rated individually for the first time.

OBJECTIONS

The implementation of the Act resulted in approximately 55 000 ratepayers objecting to the increased value of their properties. These customers were given a concession to pay their rates based on what they believed was the correct value. Those customers with consolidated accounts were not disconnected for a number of months.

SECTIONAL TITLES

Rating the sectional title properties added approximately 120 000 properties to the valuation roll.

b) RECESSION and NATIONAL CREDIT ACT

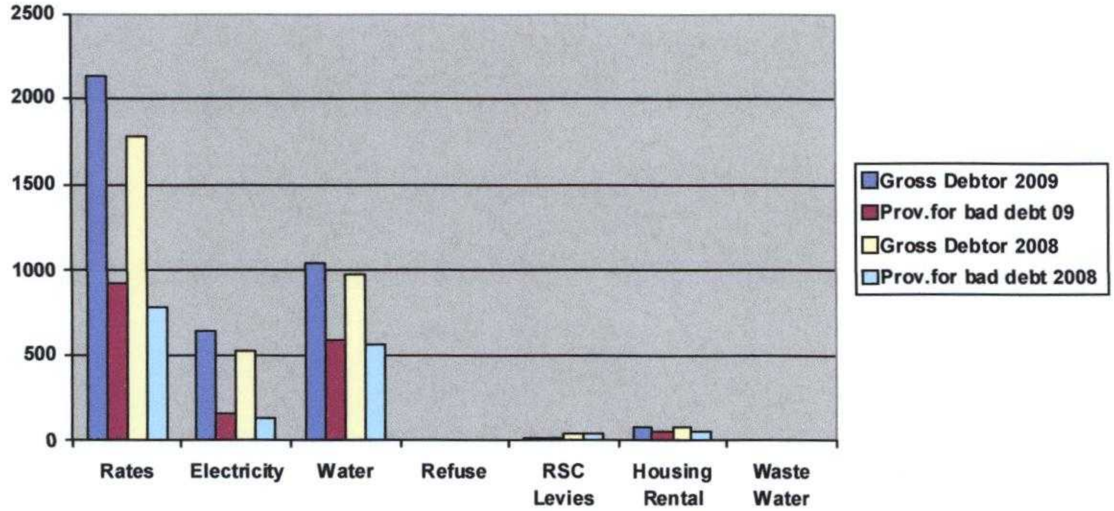
The recession had a negative impact on the collection of outstanding debts. Customers could not afford to pay outstanding amounts. Certain consumers were granted extended terms to pay.

These customers could not raise loans to pay outstanding Municipal accounts because of the National Credit Act. The banks requirements for granting loans became stringent and that had a huge impact in recovering outstanding amounts.

OUTSTANDING CONSUMER DEBTORS PER CLASS

	Rates	Electricity	Water	Refuse	RSC Levies	Housing Rental	Waste Water
2009: Debtor	2,125,553	644,746	1,040,110	10,665	24,738	89,781	11,347
Prov.for bad Debt	923,057	157,649	587,056		24,738	61,469	
2008: Debtor	1,779,294	517,844	978,257	8,842	41,160	79,178	9,583
Prov.for bad Debt	788,172	140,000	562,313		41,160	56,787	

Figure 2:OUTSTANDING CONSUMER DEBTORS



REVENUE
Income from grants and subsidies contribute to 23 % of total revenue recognised for the year.

GRANTS AND SUBSIDIES:
Revenue from grants and subsidies comprise a number of different types of grants. Grants can be unconditional or conditional.
Conditions associated with grants prescribe the specific content and process of spending required by municipalities to access the grant.
Unconditional grants can logically only take the form of cash transfers.

Conditional grants can be in the form of cash or in kind, i.e.,
Goods and services that are supplied to municipalities by the transferring authority.

Figure 3: PROPORTION OF GRANTS OVER THE PAST 3 YEARS

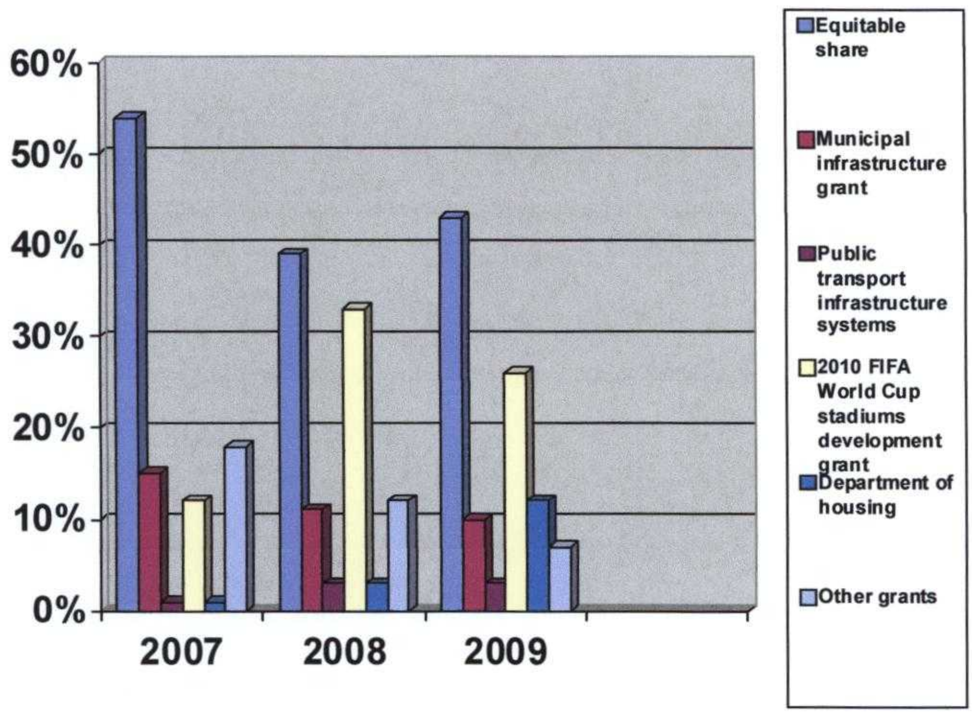
GRANT	2006/07	2007/08	2008/09	GRANT USED FOR
Equitable share	54%	39%	43%	The provision of infrastructure development and job creation in INK as an urban regeneration programme
Municipal infrastructure grant	15%	11%	10%	The construction of roads and sewerage infrastructure
Public transport infrastructure systems	1%	3%	3%	Traffic and pedestrian planning as well as the Remant Alton Bus Operating Subsidy.
2010 FIFA World Cup stadiums development grant	12%	33%	26%	The construction of the stadium and infrastructure in preparation for the 2010 World Cup.
Department of housing	1%	3%	12%	To administrate hostels in KwaZulu-Natal
Other grants	18%	12%	7%	To fund various Council projects.

Equitable share

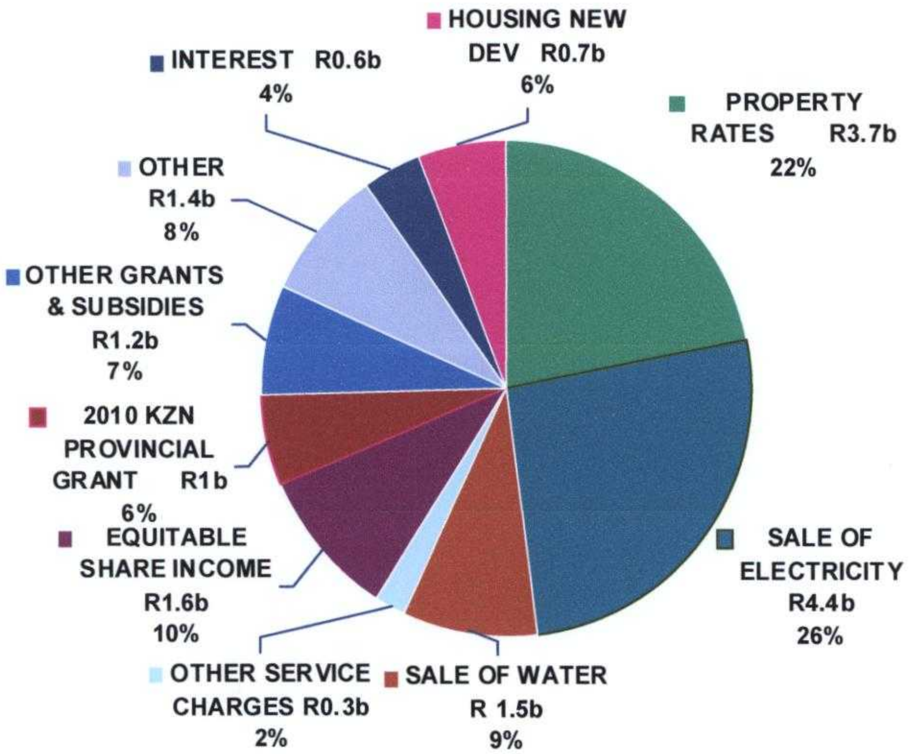
The rapid growth in local government's equitable share is largely due to increases in the allocations for indigent households. The growth in equitable shares is intended to assist in meeting the capital and operating costs of providing basic services to poor households.

The main purpose of the equitable share is to provide free basic services to poor households, but it also supports the specific project expenditures of the municipality.

Figure 4: PROPORTION OF GRANTS OVER THE PAST 3 YEARS

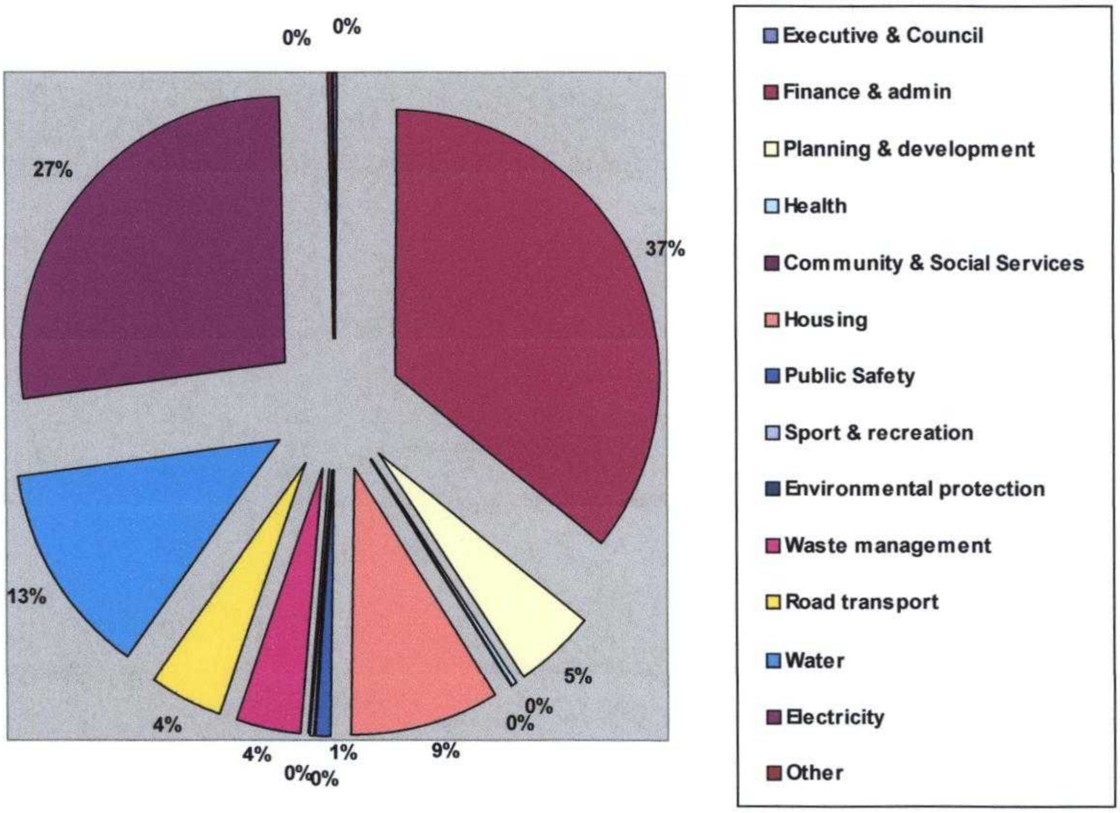


Revenue generated in the current year is derived from the following sources:



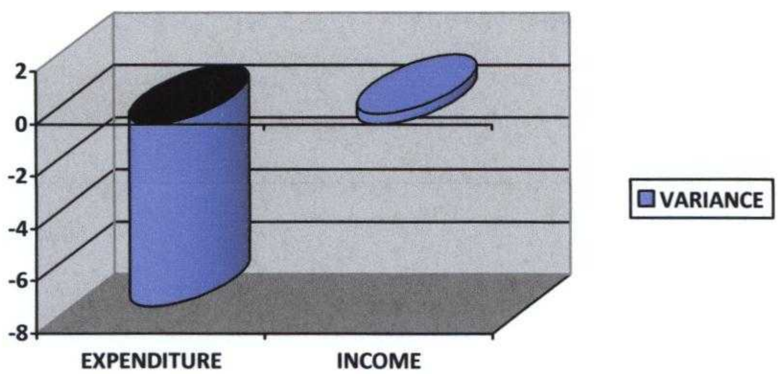
As per the above the main sources of income is income from property rates and the sale of electricity.
23% of total revenue is derived from grants, subsidies and public contributions.
60% of total revenue is derived from property rates and service charges.

The figure below reflects show the revenue by source category for the current year.



DESCRIPTION	PREVIOUS FINANCIAL YEAR	CURRENT YEAR 2009 YEAR OF ANNUAL REPORT		% VARIANCE
Rthousands	AUDITED OUTCOME	ADJUSTED BUDGET	AUDITED OUTCOME	ADJUSTED BUDGET VS OUTCOME
FINANCIAL PERFORMANCE				
Property rates	3,828,799	4,245,778	3,918,685	-8
Service charges	5,490,368	6,923,826	6,327,351	-9
Investments revenue	444,770	318,668	539,200	69
Transfers recognised-operational	1,393,525	1,711,774	1,593,796	-7
Other own revenue	2,075,502	1,564,879	2,379,563	52

TOTAL REVENUE (EXCLUDING CAPITAL TRANSFERS AND CONTRIBUTIONS	**13,232,964**	**14,764,925**	**14,758,595**	**-0.04**
Employee costs	3,235,690	3,995,899	4,089,007	2
Remuneration of councillors	59,033	66,800	69,671	4
Depreciation and asset impairment	794,334	1,221,872	1,060,723	-13
Finance charges	606,604	655,013	685,484	5
Materials and bulk purchases	2,915,858	3,690,812	3,649,336	-1
Transfers and grants	115,828	142,418	93,254	-35
Other expenditure	3,510,307	5,774,775	4,841,898	-16
TOTAL EXPENDITURE	**11,237,654**	**15,547,589**	**14,489,373**	**-7**
SURPLUS / (DEFICIT)	**1,995,310**	**-782,664**	**269,222**	
Transfers recognised-capital	1,997,809	2,760,287	2,274,984	-18
SURPLUS / (DEFICIT) AFTER CAPITAL TRANSFERS & CONTRIBUTIONS	**3,993,119**	**1,977,623**	**2,544,206**	29
Share of surplus / (deficit) of associate	63,794	0	19,601	0
SURPLUS / (DEFICIT) FOR THE YEAR	**4,056,913**	**1,977,623**	**2,563,807**	30



EXPENDITURE:

EXPENDITURE PER CAPITA

	2006/07	2007/08	2008/09
POPULATION	3 320 108	3 341 780	3 341 780
TOTAL OPERATING EXPENDITURE	10 874 374	11 228 636	14 385 300
PER CAPITA SPENDING	3.275	3.360	4.304

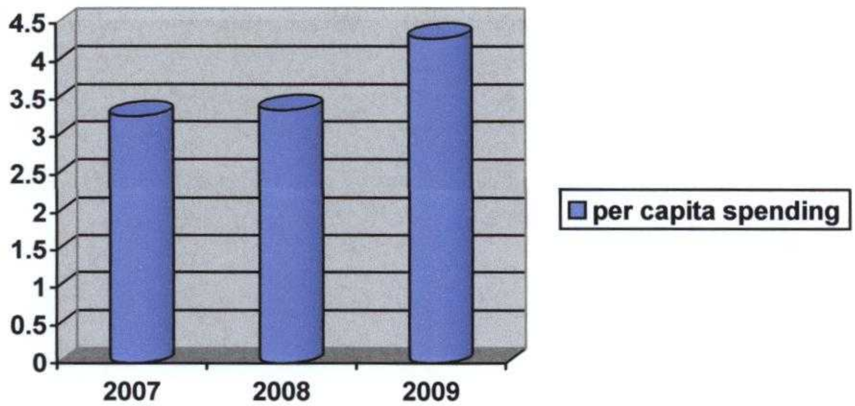


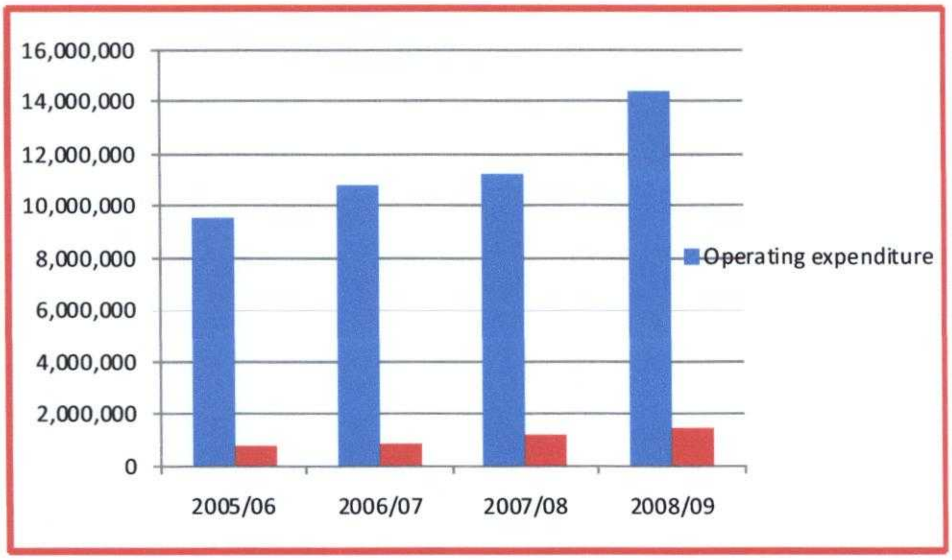
Figure 5.MUNICIPAL CAPITA PER SPENDING

OPERATING

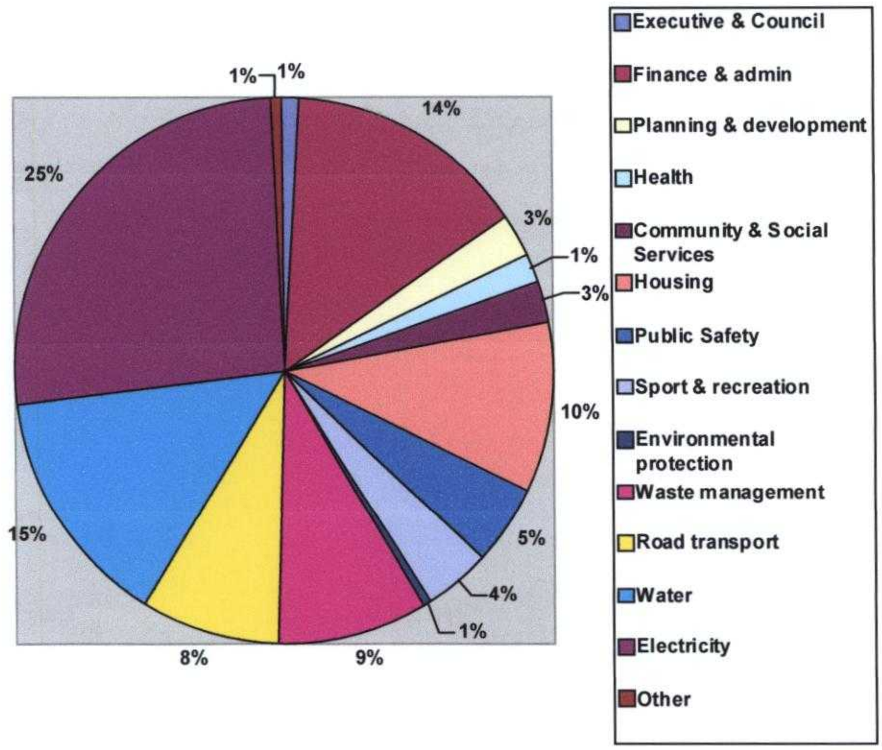
EXPENDITURE

REPAIR AND MAINTENANCE OPERATING EXPENDITURE

ITEM	2005/06	2006/07	2007/08	2008/09
Operating expenditure	9,600,733	10,874,374	11,237,654	14,489,373
Repairs and maintenance	830,240	879,222	1,218,338	1,494,375
% of OPEX	8.64%	8.08%	10.8%	10.3%



VOTE DESCRIPTION	CURRENT YEAR 2008/09					
Rthousands	ACTUAL	ORIGINAL BUDGET	ADJUSTED BUDGET	VARIANCE ON BUDGET	ORIGINAL VARIANCE	% ADJUSTED VARIANCE
EXPENDITURE BY VOTE						
Executive & Council	200,146	167,031	214,586	-14,440	20	-7
Finance & admin	2,444,134	2,693,014	1,925,267	518,867	-9	27
Planning & development	417,283	635,183	512,609	-95,326	-34	-19
Health	241,195	285,044	249,329	-8,134	-15	-3
Community & Social Services	422,576	492,813	468,938	-46,362	-14	-10
Housing	1,644,893	424,193	1,596,795	48,098	288	3
Public Safety	740,758	624,090	750,233	-9,475	19	-1
Sport & recreation	620,309	624,333	662,914	-42,605	-1	-6
Environmental protection	92,791	10,220	89,583	3,208	808	4
Waste management	1,473,032	1,248,740	1,475,083	-2,051	18	0
Road transport	1,323,101	1,276,999	1,409,888	-86,787	4	-6
Water	2,247,023	2,421,443	2,501,091	-254,068	-7	-10
Electricity	4,176,532	4,442,045	4,641,042	-464,510	-6	-10
Other	87,169	79,562	98,800	-11,631	10	-12
TOTAL EXPENDITURE BY VOTE	**16,130,942**	**15,424,710**	**16,596,158**	**-465,216**		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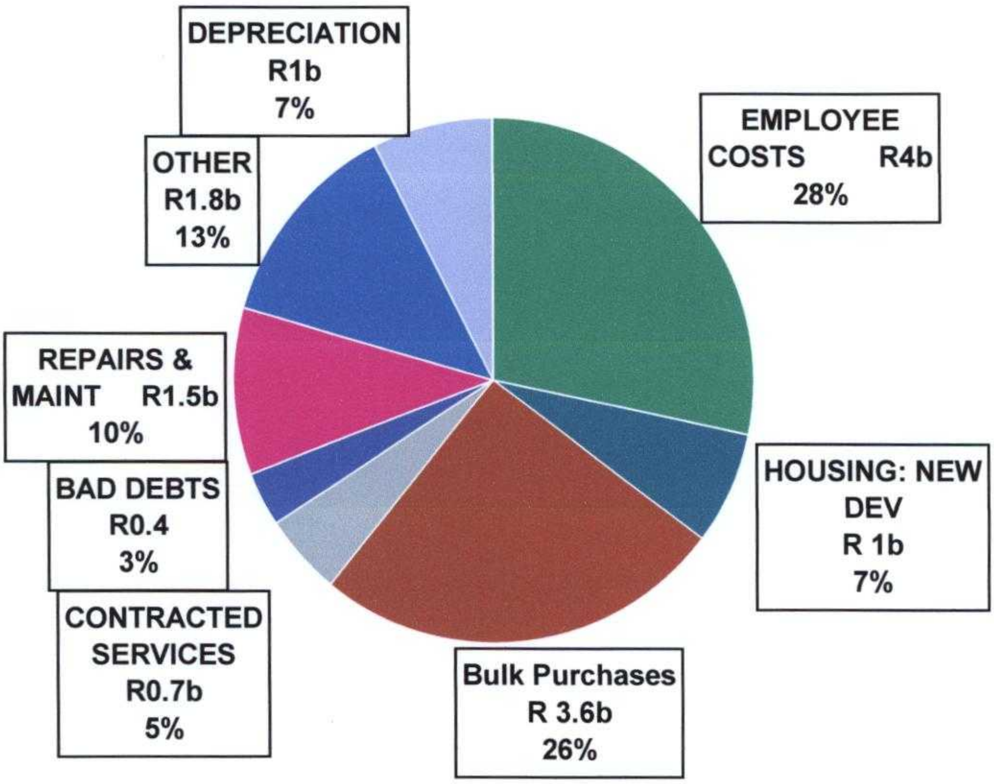
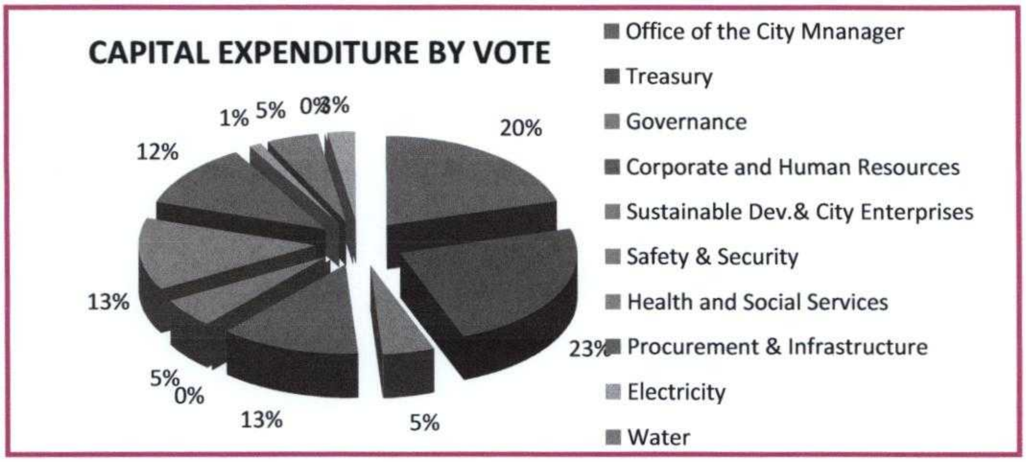
Executive & Council
Finance & admin
Planning & development
Health
Community & Social Services
Housing
Public Safety
Sport & recreation
Environmental protection
Waste management
Road transport
Water
Electricity
Other

TEMPLATE 6.13 : EXPENDITURE BY TYPE

DESCRIPTION	CURRENT YEAR 2008/09		
	ACTUAL	ORIGINAL BUDGET	BUDGET DEVIATION
Employee related costs	4,089,007	4,116,858	-27,851
Remuneration of councillors	69,671	48,510	21,161
Debt impairment	475,891	323,711	152,180
Depreciation & asset impairment	1,060,723	1,167,417	-106,694
Finance charges	685,484	641,636	43,848
Materials and Bulk purchases	3,649,336	3,776,963	-127,627
Contracted services	741,991	717,939	24,052
Transfers and grants	93,254	169,589	-76,335
Other expenditure	3,621,060	4,461,946	-840,886
Loss on disposal of PPE	2,956	140	2,816
TOTAL EXPENDITURE	**14,489,373**	**15,424,709**	



VOTE DESCRIPTION	CURRENT YEAR 2008/09		
SINGLE-YEAR EXPENDITURE TO BE APPROPRIATED	ORIGINAL BUDGET	AUDITED FULL YEAR TOTAL	% VARIANCE
Office of the City Manager	2,039,373	1,183,483	42%
Treasury	94,665	582,460	-515%
Governance	20,703	17,771	14%
Corporate and Human Resources	5,013	9,029	-80%
Sustainable Dev.& City Enterprises	173,118	180,274	-4%
Safety & Security	22,480	27,737	-23%
Health and Social Services	55,320	102,590	-85%
Procurement & Infrastructure	848,419	1,450,490	-71%
Electricity	586,348	561,854	4%
Water	1,040,680	1,402,304	-35%
Housing	299,968	302,721	-1%
Markets	7,600	6,959	8%
Airport			
CAPITAL SINGLE-YEAR EXPENDITURE SUB-TOTAL	**5,193,687**	**5,827,672**	
TOTAL CAPITAL EXPENDITURE-VOTE			



D.OTHER FINANCIAL MATTERS

BACKLOGS TO MUNICIPAL SPENDING ON SERVICE DELIVERY INFRASTRUCTURE

In recent years there has been immense pressure placed on local government to deliver on housing and basic services. Vast strides have been made by the municipality in addressing the service delivery backlogs.

A comprehensive Infrastructure Plan (CIP) was submitted to CoGTA in compliance with the Division of Revenue Act in respect of housing, water, sanitation, roads and electricity provision.

Housing delivery and service provision in urban areas as well as basic service provision programs in rural areas were assessed in an integrated manner with a view to verifying the nature and the extent of the eThekwini backlogs. All projects were captured on a geographic information system resulting in multi sector backlog data set with a high degree of accuracy. (Refer table below for backlog summary).

The backlogs are huge and in certain instances will take up to 70 years to eliminate at the present rate of spending. The current urbanisation trends and migration patterns may even push the backlogs eradication target date even further.

	Backlogs	**Cost (Rmillion) 2008 prices**	**Legislated/National target date**	**Target date at current funding**
Housing	195 000	21 000	2014	2040
Water (ground tank)	73614	1014	2008	2015
Sanitation (urine diversion toilet)	37841	341	2010	2013
Electricity (house connection)	10500	106	2012	2022
Roads (all rural municipal roads)	2430 km	7290	2012	2174