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Anxious to keep all eyes on the Cup

In spite of racial tensions and the murder of a white supremacist, investors appear calm, reports **Richard Lapper**

Game changer: projects linked to the World Cup have helped bolster the economy but the encouraging picture has been overshadowed by political complications Reuters

Traffic to the east of Johannesburg has been more than usually congested of late, as stunned motorists stop their cars to gawp at the sight of a sleek silver and blue bullet-nosed train accelerating across newly built viaducts.

The $2.5bn Gautrain – on test runs ahead of its official opening in June – is the most expensive and emblematic of South Africa's football World Cup projects, proof that, in defiance of sceptics at home and abroad, the country will be ready to stage the biggest sporting event in African history.

"The enthusiasm this project has generated is incredible," says Dave Barry, vice-president of the Gautrain project and an executive at Bombardier, the Canadian company that supplied the trains and track. "It is a game-changer for South Africa. It proves what can be done."

The railway, which will not be fully operational until next year, when the line between Pretoria, the capital, and Johannesburg, the country's commercial hub, is completed, is one of a number of transport, stadium and other infrastructure projects linked to the tournament.

Six new football stadiums have been built at a cost of more than $1bn. Visitors will arrive at new or upgraded airports in Cape Town and Durban. Training camps and hotels are being erected, roads improved and, in Johannesburg at least, some supporters will arrive at games on the articulated buses of the city's new rapid transit system.

Economists may debate the longer-term benefits of this spending, but they agree that the construction effort has helped shelter the economy from the impact of the global downturn of 2008 and 2009 and eased the depth of the country's recession.

Last year, although traditional markets for manufactured goods and raw materials shrank, the economy declined by less than 2 per cent and recovery has already begun. The building work – 20,000 South Africans were employed on the stadiums alone – is one of the reasons. "It provided an important cushion," says Jeff Gable, head of research at Absa Capital, in Johannesburg.

South Africa has been helped by another factor. Expansion in China, India and other emerging markets has maintained demand for precious metals, such as platinum, and raw materials, such as coal and iron ore, keeping prices high and offsetting falling European and US demand.

In 2009, China became the country's biggest trading partner, leapfrogging the US, Germany, Japan and the UK. "South Africa is increasingly hitched to a part of the world that is growing strongly and wants what it produces. That's a big plus," says Mr Gable.

What is more, domestic spending has recovered from last year's contraction faster than most analysts expected. That seems set to reinforce the confidence of foreign investors excited by the potential growth of the domestic market.

Heineken, the Dutch brewer, and Diageo, of the UK, its partner in a local joint-venture, for example, this year opened a €310m brewery south of Johannesburg, arguing that the South African market ranked in importance for them alongside such emerging giants as Brazil, Russia, India, China, Mexico and Vietnam.

This rather attractive picture, however, has been recently overshadowed by political complications. For some time, investors have been unsettled by the threats of mine and land nationalisation coming from the radical firebrands of the governing African National Congress' Youth League.

However much President Jacob Zuma and his ministers may insist that mine nationalisation is not government policy, Julius Malema, the unruly 29-year-old president of the league, has continued to press on the issue and has threatened to campaign to shift the party's stance at its next congress in 2012.

In the past two months, Mr Malema has become increasingly belligerent in other areas, making common cause during a recent visit to Zimbabwe, with President Robert Mugabe, and reviving an aggressive apartheid-era resistance song, "Shoot the Boer". For Afrikaners, this posture, combined with the brutal murder of Eugene Terre'Blanche, a white supremacist leader, has crystallised concerns about violent crime in rural areas, prompting exaggerated talk among some sections of the international media of a "race war". This has heightened anxieties about race relations, which in South Africa's still highly unequal society are never far below the surface.

Travel agents fear visitor numbers could be affected and, already, hopes that the country could attract more than 450,000 people during the tournament are being seen as optimistic. By mid-April, prices for hotel nights in cities such as Port Elizabeth and Durban while the World Cup is on were being offered at sharply discounted rates, a clear indication of lower-than-expected demand.

And yet there are still grounds for optimism about South Africa's immediate prospects. For one thing, worried by the damage to its "brand" and the country's image overseas, the ANC has moved to rein in Mr Malema. This month, after much prevarication, Mr Zuma warned him that recent conduct and statements of his organisation had been "totally alien to the culture of the ANC" and that his indiscipline would not be tolerated.

By breaking his silence, Mr Zuma has reassured some critics. "It [Mr Zuma's warning] was very clear and to the point. Malema is now on the back foot," says Iraj Abedian, chief executive of Pan African Capital Holdings, who argues that South Africa's broader "socio-economic landscape is sophisticated enough to manage these kinds of controversy".

There are further signs that Mr Zuma is givting priority to the quest for stability. Despite continued pressure for change from his leftwing allies in the Communist party and the Congress of South African Trades Unions (Cosatu), his government has continued to pursue roughly the same macro-economic policies as his predecessors.

Pravin Gordhan, who replaced Trevor Manuel as finance minister shortly after Mr Zuma was elected last year, has loosened fiscal policy, but by less than critics would like. Interest rates have been reduced too, but the central bank remains committed to an inflation targeting policy.

Although they control two economic ministries – economic planning and trade and industry – leftwingers are growing impatient. Indeed, in one recent speech, Zwelinzima Vavi, Cosatu's Communist leader, accused the government of "ignoring policy directions it does not like and only implementing the ones that the markets [and] capital are happy with. "We are angry that the Treasury remains infected by the highly organised but conservative bureaucrats who have been driving neo-liberal and conservative policies for the past 16 years."

Markets do seem to be comfortable. Despite the negative publicity surrounding Mr Malema and the death of Mr Terre'Blanche, investors do not seem to be too worried. Attracted by relatively high local interest rates, depressed returns elsewhere and the promise of more rapid growth, money continues to flow in.

In the second week of April, when the new race controversy was at its height, foreign investors poured R1bn into South African bonds and equities, bringing total purchases for the year to R30bn, an amount that means the country is on course this year to exceed the record level of inflows of R101bn achieved in 2007."It might have seemed pretty scary at times, but people are calm," says Mr Gable. "Financial players within and without are undeterred."

Inside this issue

Efforts to contain Malema, a thorn in the side of the ANC

Politics

The youth leader's outbursts are badly timed, writes **Richard Lapper**

If he had wanted to upset preparations for the football World Cup, which takes place in June, Julius Malema could not have chosen a better time to do it.

The 29-year-old leader of the African National Congress' Youth League has long been a thorn in the side of liberal South African society. But in recent weeks, as the country prepares to welcome thousands of foreign visitors, he has seemed to be out of control.

For some time, Mr Malema has unsettled investors with his constant threats to nationalise mines and land or embarrassed party leaders by defending the right of black politicians to become rich or threatening journalists who have investigated his high living and business interests.

But in the past two months, his bellicosity has reached new heights.

At the beginning of April he trampled over President Jacob Zuma's efforts to bring about a rapprochement between the warring government factions in Zimbabwe, by siding publicly with President Robert Mugabe and praising his controversial and violent land reform policy.

He has defied a court order preventing the singing of an old anti-apartheid resistance song "Shoot the Boer", stoking racial tensions and in the process cementing his position as a hate figure among white Afrikaners.

And then, with that controversy already causing alarm in the wake of the murder of the white supremacist Eugene Terre'Blanche, Mr Malema further upset international opinion by insulting and then expelling a British journalist from a televised press conference.

Malema (left) seems out of control, just ahead of football World Cup

Ten days ago, these incidents earned Mr Malema and the Youth League a public rebuke from an apparently incensed Mr Zuma, who called a press conference to warn the youth league that its recent conduct and statements had been "totally alien to the culture of the ANC".

With his talk of "party discipline", "drawing a line" and "consequences for anyone who crossed that line", it may have seemed that, true to ANC form, Mr Zuma was being mild and bureaucratic, particularly since Mr Malema was not even mentioned by name.

But analysts insist that, by ANC standards, the party is being unusually tough. For example, writing

Continued on Page 3

Exchange held back by apartheid-era regulations

The JSE

Richard Lapper reports on a system slow to change

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From banking to beer and from mining to mobile phones, South African companies have begun to establish a solid presence on the rest of the continent, giving weight to government aspirations to occupy a place at the table of the Brics, the big emerging markets whose rise has begun to transform the shape of the world economy.

So it is at first glance a surprise to find that the Johannesburg Stock Exchange – far and away the largest and most liquid stock market in the region – has not been able to establish more of a continental role.

Last year saw the launch of the JSE's Africa Board, a facility designed to encourage African companies to list on the market. However, it has got off to a slow start, with only two companies, a Namibian financial services group and a Botswanian tourism concern, taking advantage so far.

AltX, a junior market that might seem designed to appeal to the start-ups exploiting Africa's huge mining potential, is still being out-gunned by its better established rivals in Toronto and Sydney.

Delve a little deeper, however, and it becomes clearer why Johannesburg is lagging behind. For a start, exchange controls, a legacy of the apartheid era, though modified, remain in force.

In addition, it was only in the middle of this decade that government rules were modified in order to allow foreign listings.

As Mick Davis, chief executive of Xstrata, an international mining group, put it in a recent presentation to the Wits Business School, if South Africa wants to attract foreign resource companies to the JSE it will have to allow the free flow of funds in and out.

Although the exchange control system had matured, no South African government had managed to shed exchange control completely and it "had to happen".

Regulations also prevent foreign companies from being included in the JSE's market indices. That matters because funds that track the index are obliged to invest in the share of listed companies included within it.

Although companies such as Anglo American, the international miner which moved its primary listing to London but retained a listing in Johannesburg, are included in the index, newer entrants are not.

"South Africa has the potential to become the centre of mining finance for the continent... But the restrictions that prevent foreign companies from enjoying full-indexation on the JSE, coupled with ongoing exchange controls, make this vision almost impossible to achieve," said Mr Davis.

Perhaps not surprisingly, Russell Loubser, the chief executive of the JSE, was relatively cautious about the JSE's ability to play a broader international role when he was interviewed by the Financial Times this year.

He is confident that the Africa Board will grow, predicting that six or seven companies from nearby Zimbabwe, Zambia and bigger west and east African

> If South Africa wants to attract foreign companies to the JSE it will have to allow the free flow of funds

economies will take advantage before the end of the year.

But alliances with rival exchanges in Africa or further afield are not especially attractive, not least because of the unevenness in the levels of technological development. The JSE has a long-standing trading platform link with the neighbouring Namibia exchange and is examining examining technical co-operation with its counterpart in Egypt, but discussions with other markets have borne little fruit.

"We have been trying to work with African exchanges the entire 13 years that I have been here. But, without credible technology, there is a limit to how much you can co-operate." In addition, he reckons that few other African exchanges have devoted the same level of attention to service as the JSE.

On the other hand, Mr Loubser believes that sharp improvements in the JSE's business organisation and in particular its settlement system mean the market is well positioned to progress.

Thirteen years ago, one out of two trades failed; now – according to Mr Loubser – there has not been a failed trade for nine years and the World Economic Forum Global Competitiveness Report rates South Africa's securities regulation as the second best in the world.

"Our settlement procedures were regularly classified as the worst place in the world. Every now and then we used to beat Bangladesh and we were the second worst place and we used to rejoice," says the JSE's 50-year-old chief executive.

Indeed, the exchange has withstood the recent downturn in with a fair degree of success. Last year, when some listed markets struggled, the JSE reported in March that revenues rose 8 per cent and the exchange successfully integrated its local fixed interest market, the Bond Exchange of South Africa.

Trading liquidity – the value of all shares traded each year – now stands at about 50 per cent of the market's capitalisation, having grown fourfold since 1997.

"All our analysts were predicting that our volumes were going to disappear. I had to remind them of a critical factor. We are coming off a low base and this exchange is not remotely overheated," he says.

Change in the landscape as links grow with the Brics

Banking

Richard Lapper on increased interest in African returns

Clifford Sacks, the former head of Merrill Lynch, is not surprised that his new employer, the powerful Russian investment bank, Renaissance, has chosen to co-ordinate much of its push into Africa from Johannesburg.

"There has been a change in the landscape here," says Mr Sacks, who joined the bank, half-owned by Mikhail Prokhorov, the Russian oligarch, this year.

With local investors increasingly interested in the rapid growth and wide margins offered by African markets, customers are easy to find.

"If you get on to a plane from Johannesburg to anywhere in the rest of Africa and you look around, you will see more and more South African fund managers on those seats," says Mr Sacks.

What is more, a bank such as Renaissance is finding it relatively easy to recruit the specialist talents – from financial engineers to IT experts – that it needs.

"It has always been a struggle to pull talent down here but in the past 12 to 18 months we have seen a lot of skills returning," he says.

Renaissance's interest is mirrored in the banking sector more widely. There are growing trade and investment links between South Africa, the bigger emerging markets such as

> The continent is beginning to influence strategic thinking in financial institutions

China, India, Brazil and Russia, and the rest of the African continent influencing strategic thinking at financial institutions that have traditionally been more focused on Europe and the US. Three of South Africa's four big banks – Standard, FirstRand and Nedbank (owned by the London listed Old Mutual) – have announced new strategic orientations, with FirstRand making a particularly sharp change in course last year.

So far though, the pace of advance has been relatively slow. Standard Bank has made the most decisive moves. The sale in October 2007 of 20 per cent of its equity to the Industrial and Commercial Bank of China for $5.7bn, still stands out as the biggest single Chinese investment on the continent.

Standard followed that up by acquiring a third of Troika, the Russian investment bank, early last year. FirstRand's pursuit of Asian opportunities has so far involved a "strategic alliance" with China Construction Bank Group, while Nedbank in December 2008 agreed a similar co-operation deal with Ecobank, an institution whose footprint extends across west, central and east Africa.

Analysts suggest developments have not been quicker for three main reasons. First, although local banks avoided the worst of the credit crunch on international markets in 2008 and 2009, they have not been unscathed.

When South Africa's economy contracted last year, more than 900,000 jobs were lost, leaving many home- and car-owners unable to pay loans. The banks have seen a rise in nonperforming loans and credit growth has been modest.

At the end of January, outstanding loans were 1 per cent down on the same month last year.

"The credit crunch has slowed things," says Athol Williams, a consultant at Bain & Co in Johannesburg. "You can visibly see the banks pulling in."

Second, bank supervisors have been cautious about giving permission for local banks to acquire stakes elsewhere, refusing, for example, to allow at least one South African bank to purchase a target in Nigeria.

Jeff Gable, head of research at Absa Bank in Johannesburg, says the financial crisis has served to reinforce the prudent stance of regulators.

"Before the crisis, financial groups wanted to grow by acquiring. The Reserve Bank was very cautious about it. It said 'no' to a lot of things. And they are feeling pretty good about that right now," he says.

Goolam Ballim, chief economist at Standard Bank agrees: "It has been easier to say 'no' than allow a bank to acquire in Nigeria."

Third, there is some indication that banks have struggled to come up with ways to translate Africa's longer-term potential into short-term profits.

The market for corporate mergers and acquisitions being chased by Renaissance and Standard is highly competitive, and bankers complain that, in spite of rapid growth in consumer banking, it is still hard to make money in retail markets.

Here, a lot may depend on the ability of banks to extend services to low-income sectors through the use of mobile technology and agency arrangements.

No bank has succeeded, although several are developing strategies.

But anyone who does find a successful formula at home might well be able to deploy it elsewhere in black Africa, where analysts argue conditions are similar.

"Low-income banking at home can be a platform for advance in Africa," says Mr Williams at Bain.

Retail therapy? Banks that finds a sales formula in the townships may deploy it elsewhere

Campaign to recruit those excluded from the formal financial system

Almost every weekday, Deborah Gumede, a social worker, brings an pensioner, an invalid or a single mother to the corner of the social security offices in Umlazi to meet the young salesmen of Standard Bank.

The bank has a stall in a corner of the run-down office, where it opens accounts for social security recipients by mobile phone. Ms Gumede, is convinced it is a good idea. "It is the easiest thing for them," she says, explaining that her clients, who are paid a few hundred rand a month, are often robbed when they receive their money in cash.

Welfare claimants are not the only type of customer that Standard Bank is recruiting in Umlazi, a black township of 700,000 people, next to the city of Durban. Over the past 15 months, Vusi Mtolo, who runs its community banking unit in Umlazi, and his staff have been signing up 700 new customers a week as Standard rolls out its mobile phone technology and extends services to a sector of the population which has been largely excluded from the formal financial system. About 40 per cent of the adult population lack access to bank accounts.

Widespread poverty means typical transactions are too small to make it worthwhile for banks to open branches, while savings products such as life assurance or unit trusts were too expensive for black families struggling to make ends meet. However, over the past few years things have changed.

As the economy grows, living standards have improved. Townships such as Umlazi now boast shopping malls and their residents have begun to buy cell phones and subscriptions for satellite TV. At the same time, the government has encouraged "financial inclusion" as part of its efforts to spread wealth. Since 2004, banks have been obliged to offer no-frills *Mzansi* accounts to the poor.

Two small banks – Capitec and African Bank – have put pressure on the big groups by developing a successful low-cost model for poorer areas. "You go into their branches and there are plastic chairs and melamine tables. The products are simple and basic," says Athol Williams, a consultant with Bain & Co in Johannesburg. Wizzit, a start-up pioneered by Brian Richardson, a former Barclays banker, has also made headway in poor areas, with its slick marketing and innovative technology bringing phone banking to tens of thousands of poorer South Africans.

In the past few months, South Africa's bigger banks are beginning to reassess the commercial potential of the country's black communities. "The banks talked about these markets before but, until five years ago, they mainly paid lip service. Now they are waking up to the masive economic opportunity," says Mr Williams.

For example, NedBank announced plans to team up with Vodacom, the local subsidiary of the UK's Vodafone, to launch a mobile phone banking service along the lines of the hugely successful M-Pesa, a Kenyan mobile bank.

Regulatory approval has still to be negotiated, however, and analysts say that Standard is more advanced. According to Coenraad Jonker, director of community banking at Standard, the bank has been working on a comprehensive approach to branchless banking using mobile technology for three years and recently decided to scale up its operations by targeting 4m-5m potential customers before the end of this year.

Standard's technology allows its sales people to sign up customers using a mobile phone (identity details are digitally photographed and checked for compliance). Standard has signed up small grocers' shops and tavern owners to act as agents, where customers can withdraw and deposit cash in the same way as they would by going to a bank branch.

For Standard, though, it is important to tempt customers into other products such as mortgage loans and insurance. Savings products are also on the cards although, in low-income areas, these are likely to be quite different from those in the mainstream market.

"We have found that people typically save in tins, one tin for the funeral money, another for the school fees and another for the rent," says Mr Jonker. An ideal product would allow people to do that. One of the things we have learned is that it is a bad idea to sit behind your desk and design products. You have to engage with your customers and get to know them well."

Richard Lapper


Athol Williams: big opportunities

Big push to make sure the power stays on

Energy crisis

William MacNamara looks at efforts by industries to prevent steep price rises threatening their competitiveness

Power-less: generation capacity has hardly budged since late 2007 when a crisis revealed the extent of the grid's inadequacy and its potential to undermine South African and regional growth Reuters

Some dry valleys an hour's drive north of Johannesburg contain most of the world's platinum and chromite reserves. Smelters and ore piles belonging to various mining companies dot the landscape.

One of them, International Ferro Metals, a London-listed ferrochrome producer (the material that makes stainless steel), is building a power cogeneration facility. Toward the end of this year, it will start trapping emissions from the plant and recycling them into energy, adding extra power that is equivalent to 10 per cent of the company's use.

This is one way that South African businesses have found to mitigate rising power prices. The increases are both a threat to the competitiveness of some industries and the source of much-needed stability for the country's long-term power supplies.

IFM is one of many South African companies that smelt metals and alloys, generally an energy-intensive process. All industries will see average electricity prices double over the next three years, after a series of increases since 2008.

David Kovarsky, the chief executive of IFM, says the timing of the cogeneration plant is fortunate, but owes as much to luck as planning. It was approved before the electricity crisis that started in January 2008.

In that month, the country's sophisticated but ageing power infrastructure finally burned through its reserve margin, a danger that had been predicted for years.

No power plants had been built for more than 20 years, but the economy had grown steadily since the end of white rule in 1994, increasing power demand. Early in 2008, the power supply sputtered and seized up like a car that had not been oiled, repaired, or replaced by its owner since 1990. Blackouts gripped the country. Most of the mining industry ground to a halt for five days.

Very low power prices were part of the problem, as they starved Eskom, the state-owned utility, of money it needed to expand. The policy remedy means that average power prices will rise by about 25 per cent a year for three years, starting in the tariff year that began in April 2010. The price rises will be disproportionately shouldered by heavy industrial users, who consume most of Eskom's power.

Last year, business leaders helped persuade the energy regulator not to accept Eskom's proposal to raise tariffs by 45 per cent a year. The increase was knocked down to 35 per cent before being settled at 25 per cent.

Now, executives such as Mr Kovarsky of IFM, view the price rises pragmatically, often mentioning that the country has seen far worse trials. They emphasise the need to find cost savings in other areas, be less wasteful with the power allotted and innovate to create extra power.

"Heavy industries require a base level of power to provide much of the country's foreign exchange," says David Brown, chief executive of Impala Platinum, the world's second-biggest platinum producer.

"There is a certain paradox in penalising the companies that provide that wealth with the biggest price hikes. But at the same time we recognise that we had cheap power for a very long time. Clearly measures had to be taken. Whichever way they were taken, there were ways to cushion the blow."

In February and March, several platinum and ferrochrome producers agreed ore treatment deals that should achieve lower extraction costs, mitigating the increased power costs.

IFM paired with Anglo American's platinum division, and Xstrata's ferrochrome division linked with Lonmin, the platinum producer – though Xstrata has this month put on hold a R5bn plan to expand its ferrochrome business in Johannesburg because of the power shortages.

The similar deals give the companies access to the chromite or platinum that has been mined but not used by the other company. The two metals occur in the same place in those dry valleys. But one is usually discarded to get to the other.

Creative thinking and a stoical attitude, however, cannot remove the pressure power prices will be placing on heavy industry. The threat is not to the industries' survival but to their competitiveness when combined with other factors.

South Africa is a leading supplier of platinum group metals, gold, coal, chrome, and iron ore, and diamonds.

> South Africa's power prices were the world's lowest until 2008, giving a basic competitive advantage to industries such as aluminium and ferrochrome

These industries already faced rising labour costs, a strong rand that erodes export earnings and rising production costs as the mines go deeper and materials get more expensive.

On top of that, power prices will now double by 2013. Meanwhile, the industries continue to compete internationally, with every saved dollar per tonne providing an edge.

"Energy is the make-or-break issue," says a worker at IFM's furnace, adding: "I would not invest any money in ferrochrome today in this country." Another worker said the same about gold.

The pessimism was pertinent in March, when the benchmark ferrochrome price was $1.03 a pound, compared with IFM's break-even price of about $1.10 a pound – depending on the exchange rate – according to Mr Kovarsky. Since then, the benchmark price has risen to $1.36 a pound.

"I don't remember a time when cost pressures have been so severe," Mr Kovarsky said last month, noting the strong rand coupled with rising coke prices and rising power prices.

South Africa's power prices were the world's lowest until 2008, giving a basic competitive advantage for industries such as aluminium and ferrochrome.

Mr Kovarsky calculates the compound increases will add 10 cents a pound to production costs. "That takes us up to around the level of the Indian producers," he says.

"What lets me sleep at night is that whatever cost pressures there are should be passed on to consumers."

Like the platinum producers, he also takes comfort in the fact that the vast majority of his industry's ore is located in South Africa. For some business leaders, the deepest fear is uncertainty over what comes next, after power prices top out in 2013.

"The increases over the three-year period had to be taken," says one corporate executive. "But I just don't have the sense that after three years we will be back to 'normal' increases."

"Normal" in that sense would mean flat power prices year-on-year or even declining prices in real terms. To many South Africans, including the construction workers building IFM's cogeneration plant, those days seem long gone.

Eskom Components of the country's long-term energy policy start to come into focus

Electricity-intensive billboards in Johannesburg are counting down the days until the 2010 World Cup. International investors may be more interested in a countdown to 2013, when the country's chronic power shortage may finally ease.

Power generation capacity has hardly budged since late 2007, when a crisis revealed the extent of the power grid's inadequacy and its potential to undermine not only South Africa's economic growth, but the neighbouring economies that rely on imported electricity from Eskom, the state-owned utility.

The government responded with a power-plant building programme, and its five-year price tag is now R461bn.

But the first big new power station, Medupi, will not come on stream until late 2012 or early 2013.

The country is in a waiting game. It is bound by time considerations on one side and money considerations on the other.

Within these limits, the government has worked out a complex calculus. It must raise enough money to ensure the new stations come on time and at capacity, or it risks damping economic growth. Either it raises the money by increasing power prices or by relying on the capital markets; both options carry economic and fiscal dangers.

The game became a little less tense on April 8, when the World Bank approved a $3.75bn loan that will finance the building of Medupi, which will add 4,800 megawatts of coal-fired power, on more attractive terms than available in the debt markets.

In February, the government worked out a compromise agreement on power price rises that are high enough to stabilise Eskom's finances but low enough to be accepted by households, business leaders and ministers worried about inflation and job losses.

Power prices will rise on average 25 per cent for each April-April tariff year, starting this month until April 2013. This means that customers will pay about R66 cents per kilowatt hour in 2013, up from 42 cents today and 18 cents in 2007. Large industrial users will be exposed to annual increases higher than 25 per cent. Households – especially poorer ones – will face more moderate increases.

The World Bank loan and price rises will help Eskom sort out the power situation, but billions of dollars are still needed. An annual increase of 45 per cent would have paid for the R461bn capital expenditure programme, says Mpho Makwana, Eskom chief executive, leaving the shortfall at less than $7bn.

The second proposal – a 35 per cent rise – would leave it with a $21bn gap. "In the 25 per cent [scenario]," Mr Makwana told the Financial Times in March before the World Bank loan's approval, "it's even bigger numbers".

This month, Eskom appointed JP Morgan to help evaluate 50 financing proposals to help it raise funds on the bond markets, according to Reuters.

Some mothballed stations have reopened since the crisis, boosting capacity marginally in years to come.

Meanwhile, independent power producers are expected to come in over the next three years, doubling their capacity from 517MW to 1,400MW by 2013, according to the energy regulator. But these stopgap measures do not compare with the roll-out of Medupi and Kusile, another new coal-fired station.

Eskom is looking for an equity partner to share the development of Kusile.

"It takes four years to build a coal-fired power station if you don't cut corners, and it takes seven years to build a nuclear power station," Mr Makwana said during the March state visit to London of President Jacob Zuma. "Nothing is going to mushroom tomorrow. Nobody is going to say: 'here is power'.

"Every day you have 40,500MW coming on stream," he added, "and you have demand of 36,000 or 37,000MW, and you've got 3,000MW that you hold on to, because of the load reserve margin. So if anything goes wrong with one power station, you've got a problem. If there are adverse weather conditions you have a problem, as we saw in December and January."

It is sometimes a joke and sometimes a sober observation, but many South Africans comment that the global economic slowdown is the best thing that could happen to the country. The electricity grid simply could not sustain the pre-crisis industrial boom, without steep power rationing.

The reserve margin will remain thin – about 16 per cent of capacity – until 2013 when it will expand to 24 per cent.

The components of the country's long-term energy policy are coming into focus since the passage of the 25 per cent annual price rises.

The debate now centres on whether and how to build nuclear power stations. Middle-class residents in Johannesburg complain about the rising bills, but they will still enjoy relatively low-priced electricity, even in 2013.

The more serious worry is how Eskom finances the single biggest project budget in the country's history.

William MacNamara

Efforts to contain youth league leader

Continued from Page 1

in the web newspaper The Daily Maverick, Stephen Grootes, a local political journalist, said: "If you read the fine print, it may appear no real action is being taken. But pass it through the ANC thesaurus, and Zuma is as pissed off as he can possibly be."

But how easy will it be for Mr Zuma and the leadership to bring Mr Malema to heel? Until recently, he has been an important ally of the president. In the long power struggle between Mr Zuma and former President Thabo Mbeki, Mr Malema mobilised effectively on the current president's behalf.

"Zuma used the Youth League to get rid of Thabo," says Moeletsi Mbeki, a political analyst. "That is why he [Zuma] has been so reluctant to say anything".

In last year's election campaign, he proved his worth as a speaker among black university students and helped mobilise the vote for Mr Zuma. His simplistic radicalism goes down well with a social group frustrated by limited job opportunities and a growing wealth gap.

What is more, Mr Malema is well placed to play a role in factional fighting that has been growing in recent months. The broad alliance backing Mr Zuma has been creaking at the seams, with leftwingers attacking the government's economic policy as too cautious and lambasting its tolerance of corruption.

Zwelinzima Vavi, the leader of the leftwing Congress of South African Trades Unions, has blasted the influence of what he describes as a "small right-wing tendency led by materialistic and 'tenderpreneurs' within the ANC leadership", an allusion to the party leaders who have benefited personally from black economic empowerment policies or the practice by ANC officials to award state contracts to political allies and other associates.

> 'Pass it through the ANC thesaurus, and Zuma is as pissed off as he can possibly be'

If the battle between the government and the left were to intensify, Mr Malema and the Youth League could be useful allies for Mr Zuma. Mr Malema is already close to a number of powerful ANC business figures targeted by Mr Vavi, and the Youth League has challenged the influence of the Communist party.

Last year, Mr Malema clashed with the party over its opposition to his proposed mine nationalisation and referred disparagingly to Jeremy Cronin, the its deputy general secretary, as a "white messiah".

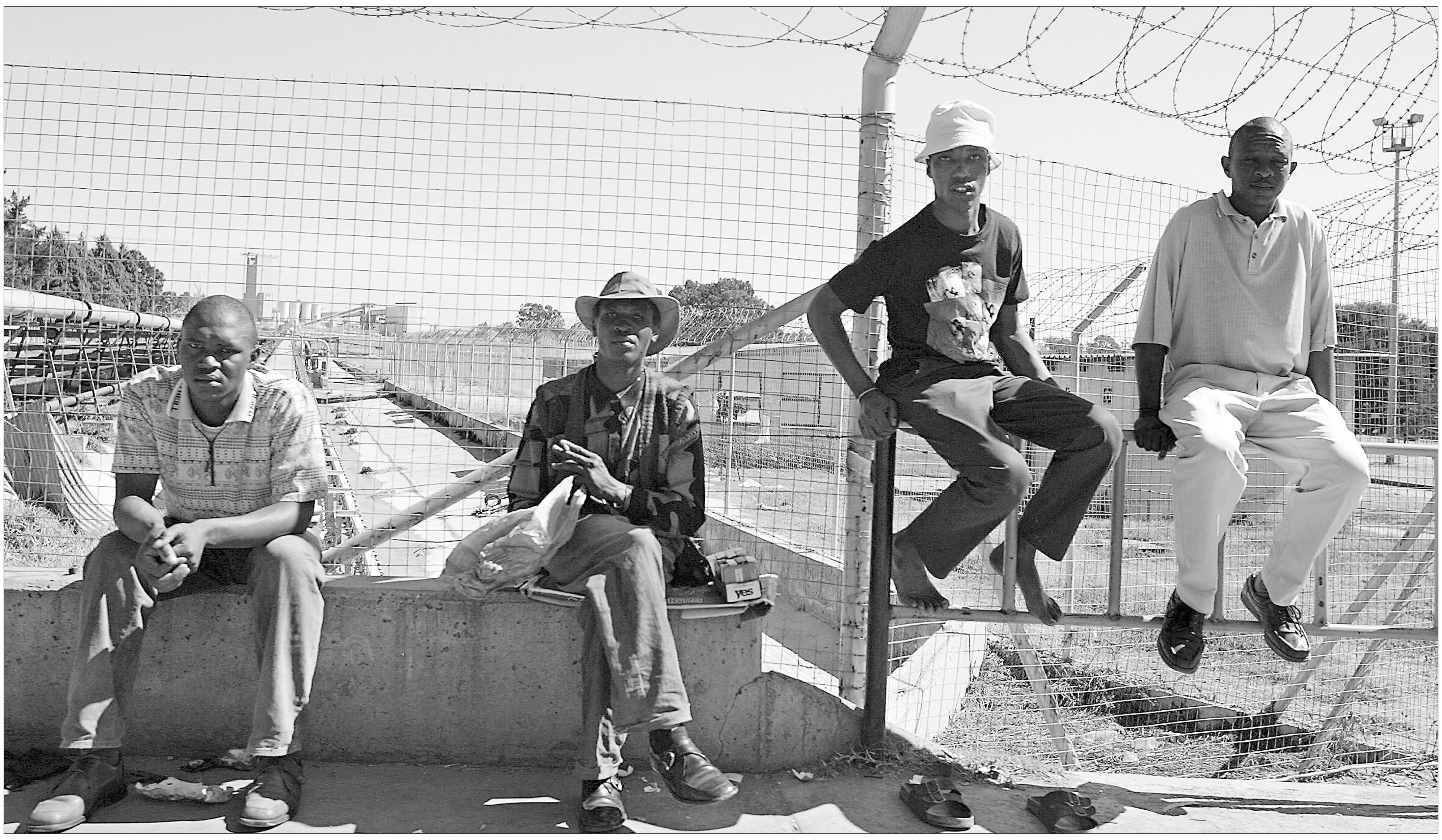
The Youth League says it wants to replace Gwede Mantashe, the ANC general secretary and a leading Communist, with Fikile Mbalula, the deputy police minister.

Party elders may well clip their unruly young protégé's wings when they deliberate on his recent indiscpline over the next few weeks, but it would be unwise to write him off just yet.

Fierce debate over transfer of power

BEE and mining

William MacNamara reports on the detail of legislation designed to transform society



Wrong side of the fence: missed targets in levels of black empowerment have meant that 83.7 per cent of the mining industry's senior management is still white Getty

International investors often wrongly see black economic empowerment, or BEE, as a discrete programme in South Africa, not unlike education reform or initiatives to contain the spread of HIV.

However, it is the basic socio-economic project of a country where 20 years ago the majority of its citizens were systematically excluded from commerce, education and property ownership. Just as the 1964 Civil Rights Act in the US stood for wider efforts to promote socio-economic equality, BEE legislation is the face of a grand, messy design that aims to tranform an entire society.

Its purpose is to transfer an equitable share of the country's resources to the non-white majority. And like most ambitious projects in their early days, the devil is in the detail. This can be seen in the debates surrounding the "mining charter" review.

In 2004, the mining and banking sectors were chosen to test "broad-based" BEE enforcement mechanisms. The mining charter passed that year, stipulates a variety of targets. The most important is that a minimum 26 per cent of the industry – at the equity or asset level – be owned by blacks by 2014. At the charter's five-year mark in 2009, 15 per cent ownership was required. A review and report was envisaged for 2009 to gauge progress and maybe introduce changes.

The 2009 report is still not published, but a leaked draft that was circulated in the media this month suggests the industry is behind on almost all the main measures of empowerment. Only 9 per cent of the industry was black-owned by 2009, the report allegedly states.

Frans Baleni, general secretary of the National Union of Mineworkers, says 84 per cent of the mining workforce is black while 83.7 per cent of its senior management is still white.

A March 31 deadline to agree changes to the charter has been pushed back for three months, as mining ministry and industry leaders work out compromises. According to people involved in the talks, the 26-per-cent-by-2014 rule will not change.

But a fierce debate surrounds other empowerment measures, such as what percentage of management should be black by a certain date, how much equity employees should own, how "preferential procurement" should work and how "community upliftment" should be achieved.

No industry executive interviewed on mining charter review disagreed with BEE. But the issue is loaded, and it tended to draw broader comments.

Paul Stuiver, chief executive of Pretoria Portland Cement, southern Africa's biggest cement maker, says: "10 years ago, 99 per cent of middle and upper management were white males Now, it is socially diverse, racially diverse, gender diverse. None of this would have happened if it had not been forced."

But, he adds: "The 26 per cent target is high, and trying to do it too quickly creates problems. You can't 'fast-track' enough people into 75 per cent of management roles.

"You can't 'fast-track' experience. People go wrong when they think there is a substitute for experience."

> 'You can't fast-track enough people into 75 per cent of management roles. You can't fast-track experience'

PPC has met the 15 per cent ownership target by 2009, he says. But its application for new order mining rights, the reward for meeting BEE guidelines, is still being processed along with many others awaiting an outcome three months into the new year.

Several executives suggested that the problem was not the spirit of BEE, but the approach based on minute targets and ownership levels. "Personally I'd like to see more of a sliding scale instead of a 'yes or no' approach," says one executive who asked not to be identified.

"You need to encourage people to move along the transformation curve and see it as a journey instead of a box-ticking exercise, and with different targets allowed in different time-frames.

"There should be bonus points for overachievement. They should set minimum standards and real incentives to exceed them."

The focus on ownership levels meant deeper problems facing the mining industry were being ignored. The unions, he says, have become empowered to push through high real wage increases, regardless of cuts to metals production during the downturn.

"The real problem here is that productivity and wage increases are moving in opposite directions, and that is the biggest weakness in terms of this country's competitiveness. Unfortunately, this session [of the five-year review] will not address these broader questions.

For other mining industry leaders, the lack of resolution over the new mining charter creates its own problems. "Clarity in the rules of the game is what investors need, so they can model with certainty what happens in this country," says Nick Holland, chief executive of Gold Fields.

"Uncertainty is the worst possible factor."

Mr Holland says the same concept applied as Julius Malema, the ANC Youth League leader, continued to make internationally publicised calls to nationalise the mining industry, thereby achieving empowerment that far surpassed the BEE approach.

Mr Malema got air time, and the ANC's open-forum approach to issues meant it was not immediately rejected.

"South African equities already factor in the bad news and worse, so when things are less bad than expected, they tend to improve," Mr Holland says. There is a "zero per cent chance" of nationalisation, "because the government can achieve its social objectives without it".

Those social objectives are now being debated – in an ANC spirit of open discussion – between the government and the mining industry. They hope to work out a solution on the new mining charter by June.

In addition to the broad issues, there are practical debates about BEE financing. Many deals were structured as equity transfers financed by the parent company and loaned to the BEE partner, which then repays it through dividend streams. But the age of ready credit is over, making them harder to facilitate.

The extent of change to date is impressive to some but inadequate to the government. After all, to leaders representing the black majority, the concerns of the mining companies may look like so many whinges next to the overall good.

Becalmed but ready for action once the BEE deal-flow ends

Venture capital

Margaret O'Connor considers constraints on a new wave of entrepreneurs

South Africa-born astronaut, entrepreneur, and philanthropist Mark Shuttleworth's recent decision to bow out of venture capital (VC) financing for early-stage companies marks the shrinking of an already tiny universe.

Foreign VCs are unlikely to fill the vacuum, despite growing recognition of the talent and technology incubated in Africa's biggest economy.

The government's Innovation Fund and the Industrial Development Corporation offer a lifeline for start-ups, but have made little progress in unlocking the individual and institutional money required to create a thriving eco-system for entrepreneurs.

Over the past decade, risk-averse South African institutional investors have channelled their money into private equity funds that have bankrolled black economic empowerment.

This profitable deal-flow is expected to continue for at least another two or three years.

By 2013, an improved telecoms network should catalyse another cycle of expansion in VC financing, such as the one the country experienced during the dotcom boom. In the meantime, companies founded in the past two years are optimistic about the cheap, quality assets they can acquire during the lean years.

The international operators plan to invest about R350m each to facilitate the overseas expansion of companies with proprietary technology, despite foreign exchange controls and regulations aimed at preventing the flight of intellectual property (IP).

Locally funded venture groups say they are also focused on opportunities beyond South Africa's borders.

Mobile phone applications offer a significant near-term opportunity. The country's 48m people own more than 42m mobile phones. A similar concentration of mobile phone ownership and usage holds true in neighbouring countries.

But expansion into the US is the more familiar route for South African start-ups. Typical of that migration is the path of Global Vision, part of the portfolio of Hasso Plattner Ventures Africa (HPVA).

Jon Jacobson, the chief executive, worked on Wall Street for five years after graduating from the University of Cape Town with an engineering degree.

The sale of his New York apartment funded his development of a beta version of his proprietary marketing automation software for customer relationship management.

Having earned revenues of R27m in South Africa last year, Global Vision expects to wedge open doors at US digital agencies that are interested in the kind of measurable solutions for mobile and online campaigns that his company has developed.

One of the main incentives for South African entrepreneurs to sell their businesses offshore is the relatively low price/earnings ratios offered by conservative local institutions. "Why would I accept a p/e ratio of five or six when I can get twice that in the US," asks Mr Jacobson.

Government interference is another factor driving entrepreneurs overseas.

> Investors have channelled money into private equity funds that have bankrolled black economic empowerment

The recently formed department of technology and innovation plans to attach strings to government funding for university research.

Efforts to commercialise intellectual property developed at local research institutes will be supervised by a newly created body whose mandate remains a work-in-progress.

"We need a satin-clad lasso to make government initiatives move in the right direction," says JP Fourie, head of the South African Venture Capital Association.

One benefit of the government's interest in fostering a bigger knowledge-based economy is the creation of training and mentoring programmes designed to help entrepreneurs learn how to conduct market research, manage business growth and speak the language of business.

While the intention is excellent, few participants have mastered the process. VCs fear that government trainers have a hard time grasping the nuance of complex topics and fail to convey the sense of urgency entrepreneurs need to keep ahead of fast-evolving markets.

David Frankel, the founder of South Africa's first private internet hosting company, and more recently, a Boston-based investment company called the Founder Collective, is part of the tribe of seasoned entrepreneurs who are trying to bridge the gap between the South African start-up scene and the expectations of international customers and investors.

Mr Frankel laments the lack of intuitive business know-how at South Africa's top technology and business school programmes. "It's just not in the water," he says.

He helped create Endeavor, a non-profit group devoted to helping high-impact entrepreneurs from emerging markets such as South Africa connect with world-class strategic advisers and each other.

This type of "mentor capitalism" is starting to create role models that inspire new ways of working together.