



# **TRADING SERVICES REFORM IN SOUTH AFRICA'S MAJOR CITIES**

# **PROGRAMME OVERVIEW**

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## PROGRAMME OVERVIEW

National government is implementing a performance-based grant to incentivize a turnaround in the performance of water and sanitation, electricity, and solid waste services in South Africa's eight metropolitan cities<sup>1</sup>. The reforms are led by National Treasury working together with the relevant national government departments – Department of Cooperative Governance and Traditional Affairs (local government), Department of Electricity and Energy (electricity), Department of Water and Sanitation, and Department of the Forestry, Fisheries and Environment (solid waste management), and the Department of Human Settlements. All eight metropolitan governments are participating in this Trading Services Reform Programme.

The programme responds to the long-term decline in the reliability of these trading services which undermines the livelihoods and quality of life of more than 4 in every 10 South Africans and constrains economic growth and job creation. South Africa's metro areas are the engine of economic growth and prosperity, accounting for over two-thirds of its economic activity.

The end of load shedding provided clear evidence of a breakthrough in the turnaround in Eskom's performance. In a similar way, the success of this reform initiative will be evident when households and businesses in South Africa's major cities experience reliable electricity, water and solid waste services. The scale of the reform is significant. The 24 trading service businesses serve over 24 million people, employ appropriately 60 000 people and have an annual revenue of approximately R150 billion. Reform progress will be monitored through published data that will show a turnaround in the financial health of the institutions providing the service, substantially increased investments into the service and progressive improvements in key service performance and outcome indicators.

## WHY ARE THE REFORMS IMPORTANT?

**Reliable electricity, water, sanitation and waste management services are an essential foundation for investment and jobs in cities, to support livelihoods and enable quality of life.**

However, these services are in long-term decline due to under-investment in maintenance, rehabilitation and expansion, and inefficient operations. Services are increasingly unreliable, compromising quality of life, jobs, investment, the environment and economic growth. A 1% constraint to economic growth costs the nation more than 1.5 trillion Rand over 6 years. For this reason, the reform programme has been included in the 7th Administration's Medium Term Development Plan endorsed by Cabinet and is one of Operation Vulindlela's priority programmes to unlock constraints to economic growth.

## WHAT WILL THE REFORMS ACHIEVE?

The immediate reform objective is to turnaround the decline in service reliability and quality through the turnaround in the performance of the institutions providing the service, leading to improving cash revenues, increasing maintenance and investment, improving efficiencies and improving services.

The outcome of successful reforms will be safe, reliable, accessible and financially sustainable service provision for all residents, business and institutions in South Africa's major cities.

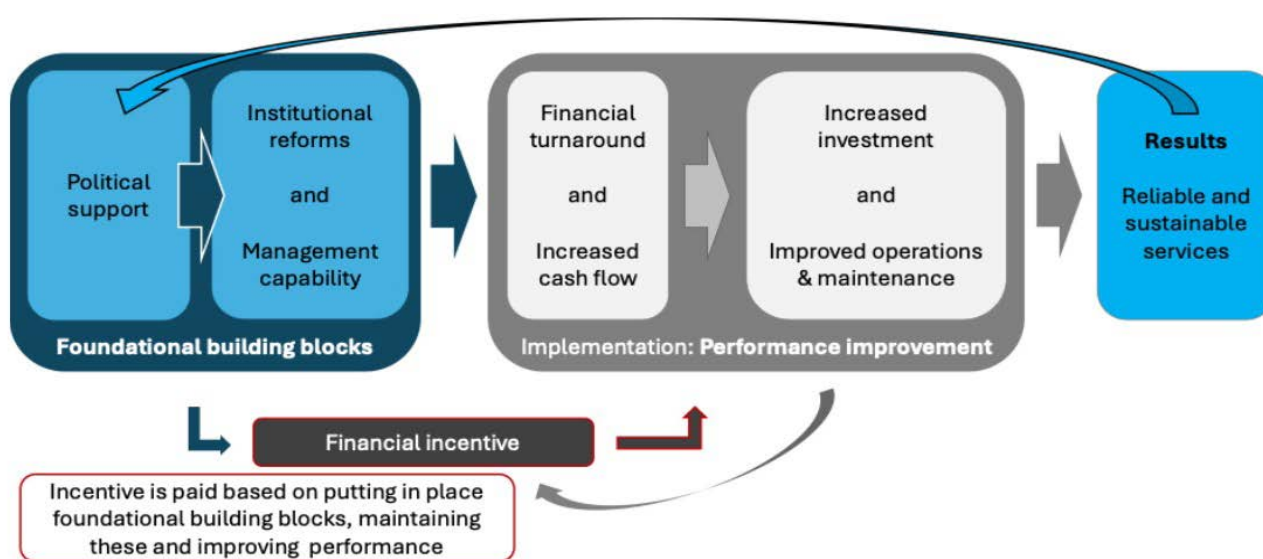
The reform objective and intended outcomes are both practical and achievable. South Africa has the collective resources and capability to provide safe, reliable and accessible trading services for all residents, businesses and institutions in its major cities.

<sup>1</sup> MTBPS, October 2024.

## HOW WILL THE TRADING SERVICES BE REFORMED?

National government is implementing a new financial incentive for metropolitan municipalities to turnaround the performance of their trading services. Metropolitan governments will be able to access this significant incentive if they establish three foundational conditions – political support to improve their trading services, key institutional reforms and establishment of management capability with accountability. The incentive will be paid out based on actual performance, that is, the extent to which the metropolitan governments establish, maintain and build on these foundations to achieve improved service outcomes through a financial turnaround with increased cash flows, increased levels of investment, and improved operations and maintenance. The incentive therefore serves a dual purpose. The incentive both rewards improved performance as well as provides a direct contribution to increased investment that can lead to improved performance. The incentive is designed to promote a virtuous cycle of improving performance and service outcomes, supported by improving cash flows and higher levels of investment. The incentive design and reform sequencing are shown in Figure 1.

**Figure 1: Incentive design and reform sequencing**



There are three key reforms that the incentive seeks to promote. Municipalities must manage the service using a business-like approach with delegated management authority and accountability for performance. Effective management capability must be established. A financial turnaround in the performance of the business must be achieved to support improved outcomes.

Delegated management authority with accountability is important because the trading services are multi-billion Rand operations dependent on tariff revenue. Effective management of these services requires that they be managed using a business-like approach that integrates the revenue value chain and customer relations with operations and investments. The manager responsible for each trading service, together with his/her management team therefore needs to have the managerial responsibility as well as the necessary autonomy to manage the service effectively, including control over the performance of essential support services. This means that the service must be structured



either as a business unit with a single point of accountability, or as a separate entity, and operate within a protective and supporting governance environment that allows management to succeed. A corporate structure in the form of a public utility company has several advantages but is not a requirement to access the incentive grant<sup>2</sup>.

Management capability is important because the trading services are large-scale, complex operations that require professional infrastructure management and engineering skills to be managed effectively in a challenging economic and social environment. Within municipalities, there are significant gaps in the management and technical capabilities needed to successfully turnaround and manage the performance of these businesses. The programme will offer technical assistance to the metros to assist them to establish the necessary management capability through recruitment, training and management contracts.

A financial turnaround in the performance of the business is important because without this the service will be under-resourced and service quality and reliability will continue to decline. Government grants, although significant in quantity, are insufficient to meet the investment needs of these services. Therefore, it is necessary for the service itself to support higher levels of investment through direct cash contributions and access to loan finance. This means that the business unit or entity providing the service needs to generate positive cash flows from its operations.

Political support at the municipal level is essential for success and must be obtained at the outset and maintained throughout the life of the programme (Figure 1). Political support for the programme has already been demonstrated through Council approval of trading service improvement strategies, institutional road maps and business and investment plans for all three services in all eight metros.

## **WHEN WILL THE REFORMS YIELD RESULTS?**

As has been the case for Eskom, years of under-investment in maintenance and rehabilitation of infrastructure cannot be fixed overnight. The timeframe to make substantive improvements in the quality, reliability and sustainability of these services is expected to be at least three years. Nevertheless, with the right interventions it is possible to change the trajectory of performance in some areas within a much shorter period, showing improvements in key performance areas such as billing and cash flow, thus making more resources available for maintenance and investment.

The intention is for the foundational building blocks to be put in place within a period of one year. In parallel with this there will be a strong focus on improving revenues, cash generation and efficiencies, which are essential for making more resources available for operations, maintenance and investment. A significant increase in capital investment is anticipated within a three-year period and substantial improvements in service outcomes will become evident in a three- to five-year period.

## **WHERE CAN I FIND OUT MORE?**

Further information is available at [https://lg.treasury.gov.za/ibi\\_apps/portal/Municipal\\_Trading\\_Service\\_Reform](https://lg.treasury.gov.za/ibi_apps/portal/Municipal_Trading_Service_Reform)

<sup>2</sup> A corporate structure can create a clearer separation between the ownership and management roles, can introduce independent oversight by a skilled and experienced board, can create greater financial transparency through a separately audited set of financial statements, and can create clearer accountabilities for performance through a dedicated management team with a clear mandate and performance agreement with the Board.