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CAPACITY
BUILDING FUND

TODAY MORE THAN EVER THE NEED EXISTS FOR A LONG TERM FINANCIAL MODEL (LTFM) THAT UNDERPINS LONG TERM FINANCIAL PLANNING IN MUNICIPALITIES

Presented To:
CIGFARO Conference
6 July 2022

LONG –TERM FINANCIAL PLANNING:

1. **Contextual Perspective**
   - MFMA Circular 112

2. **The Objective**
   - Financial Sustainability & Resilience

3. **What Is Needed To Navigate Into The Future**
   - Long-Term Financial Plan/Strategy (LTFP/S)
   - Long-Term Financial Model (LTFM)

4. **Benefit To The Municipality If LTFP Is Executed Successfully**

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MFMA Circular 112 (December 2021)

- National Treasury is supporting municipalities to **develop and implement** **long-term financial models and strategies**.
- This **reform** seeks to develop more **sustainable, and integrated infrastructure development programmes over the longer term**, informed by **strategic plans**, and **financed in the most effective and efficient manner**.
- The municipality's long-term financial strategy, informed by a long-term financial model, must articulate a **sustainable, efficient and effective borrowing strategy and practices** for the municipality and provide a **clear statement of intent for lenders and other stakeholders**.
- Although some municipalities have long-term financial models (LTFM), they are not always **integrated with municipal plans**, or **based on actual cash flow analysis** and **investment programmes**, or able to consider **alternative financial scenarios and outcomes in relation to the ability to borrow and the structuring of market transactions**.

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MFMA CIRCULAR 112 (DECEMBER 2021)

- Municipalities need to develop LTFM that **support decisions on investment selection** and **assesses the financial impact of policy choices**, by **forecasting future financial performance** and the **impact of infrastructure projects on borrowing capacity**.
- The LTFM needs to inform the municipality's long-term financial strategy.

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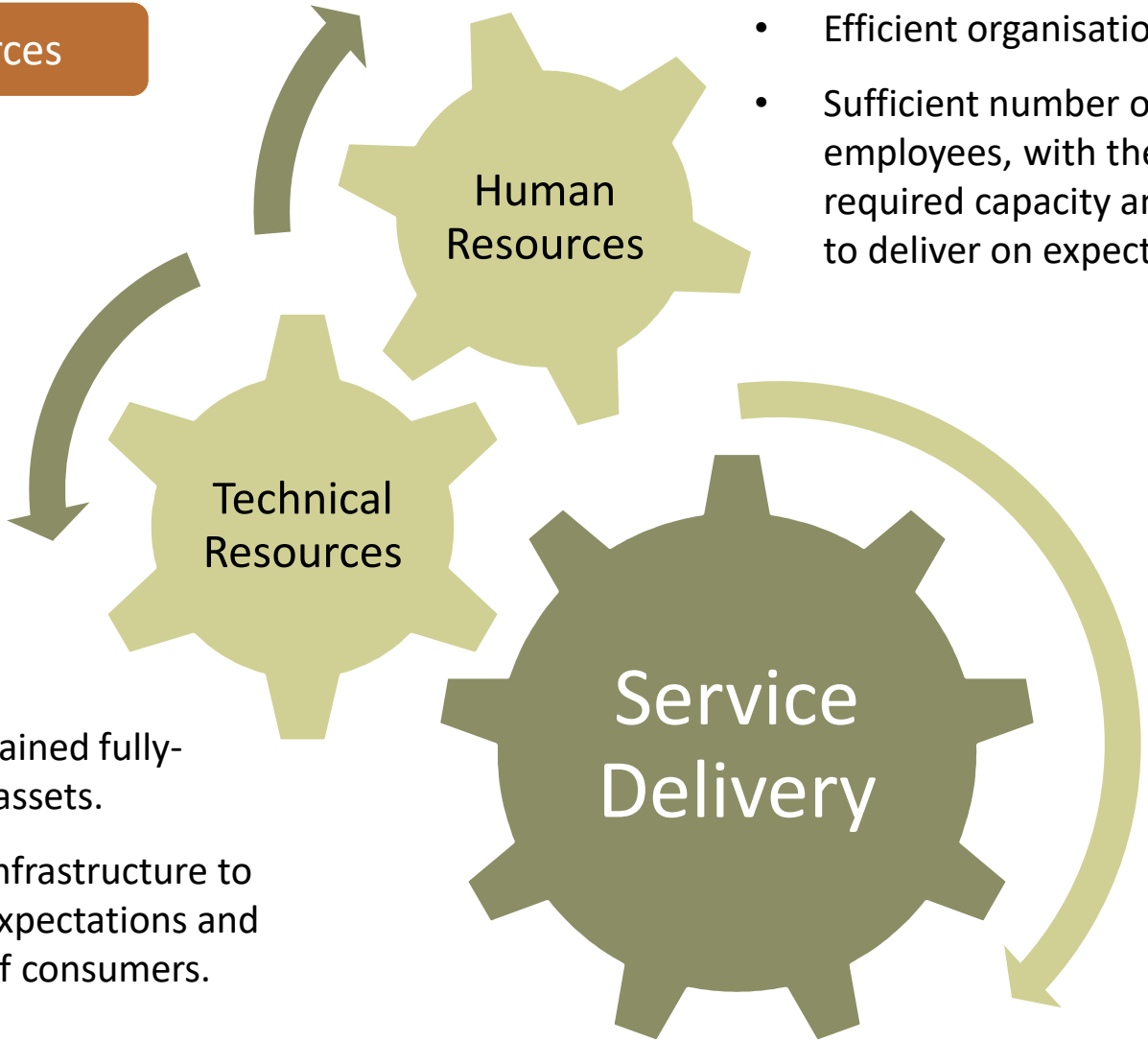
THE OBJECTIVE: SERVICE DELIVERY

Financial Resources



- Efficient organisation.
- Sufficient number of employees, with the required capacity and skill to deliver on expectations.

- Well-maintained fully-functional assets.
- Sufficient infrastructure to meet the expectations and demands of consumers.

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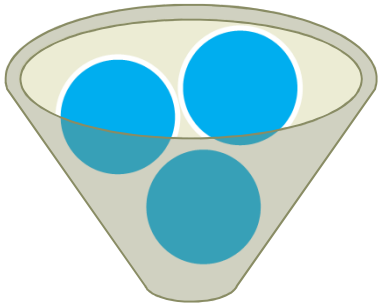
Objective: Financial Sustainability

1 **Future Uncertainties**

Demand



2 Financial Capacity

LTFM → LTFP/S

Financial Sustainability and Financial Resilience

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Objective:
Financial Sustainability But Also Financial Resilience

Financial Sustainability

SUFFICIENT

Financial Resources

=

Operating Profitability + Cash Generation + Optimal Cash Utilisation = Financial Sustainability

Financial Resilience = Financial Sustainability + Uncertainties (Unforeseen Events)

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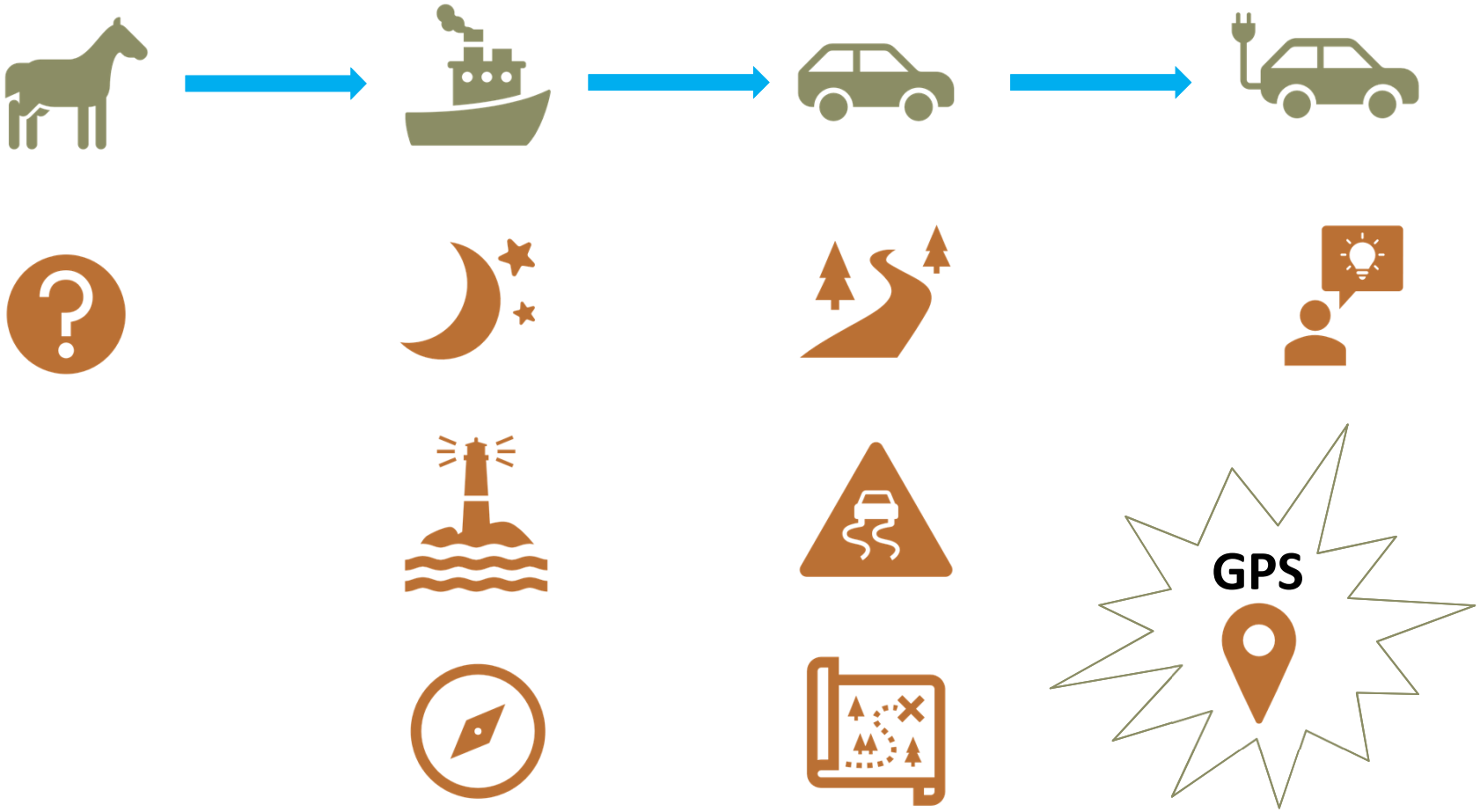
The History of Navigation



What Financial Navigation System is your Municipality using?

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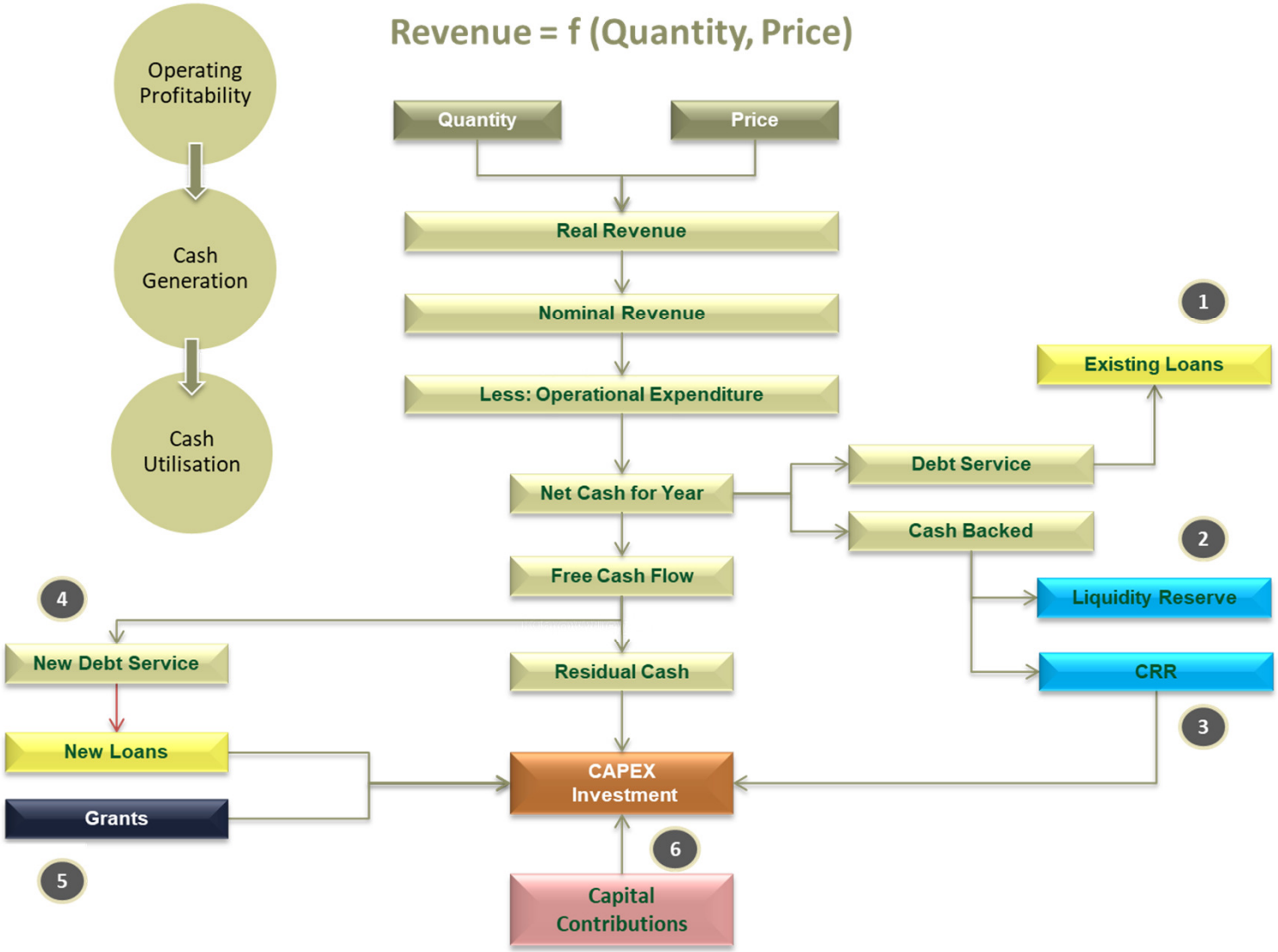
THEORY BEHIND MUNICIPAL LONG-TERM FINANCIAL PLANNING



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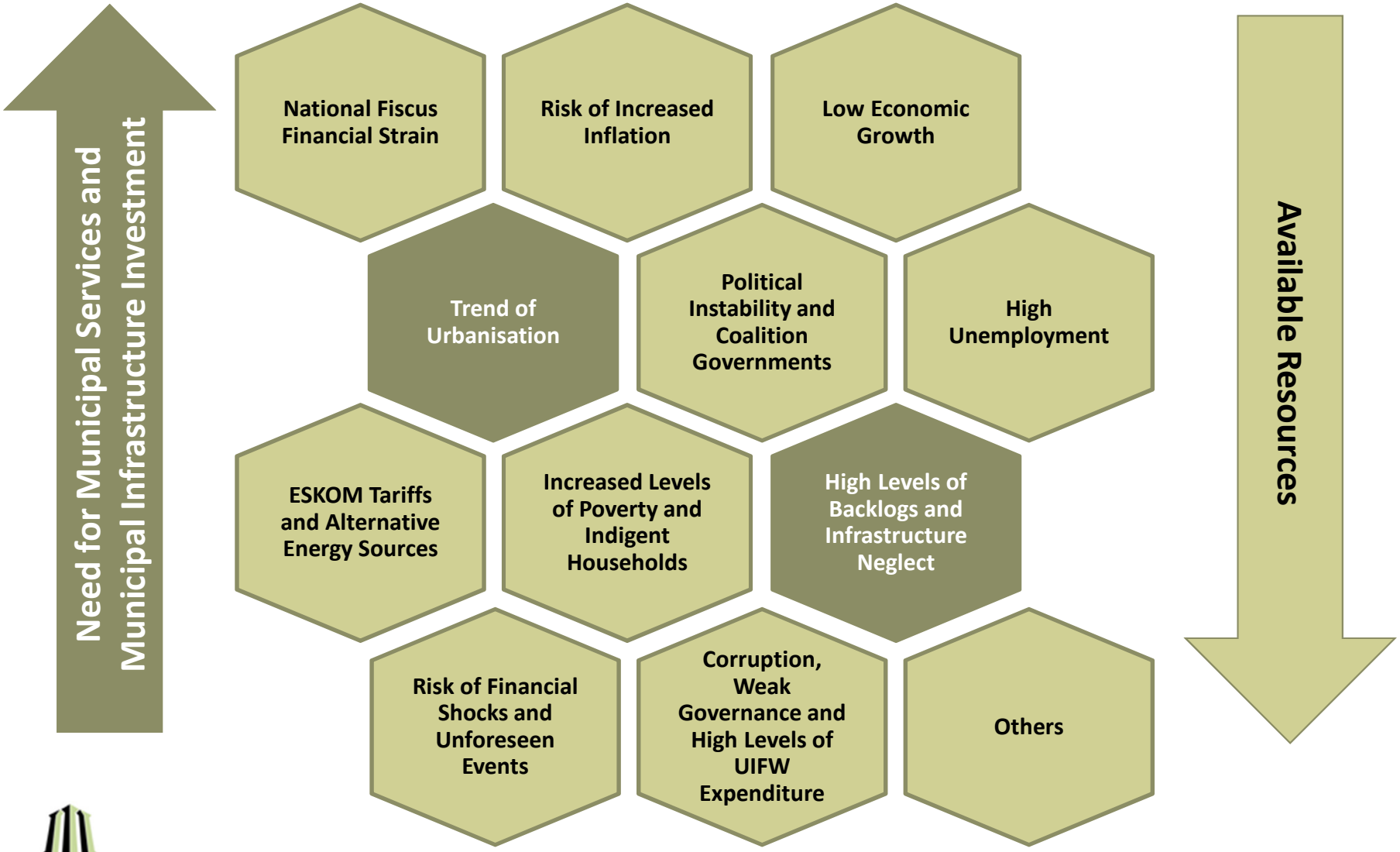
MUNICIPAL ENVIRONMENT - UNCERTAINTIES



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A LTFM as Tool Is Needed To Underpin a LTFP

Essential Characteristics of a LTFM

1 Intellectually Robust and Sophisticated

A Long-Term Financial Model should:

- be technically sound and acknowledge inter-financial relationships;
- incorporate demographic and economic indicators;
- accommodate specific user assumptions and inputs to develop its forecasts;
- be able to quantify and respond to the financial impact of external events; and
- support sensitivity and scenario-analysis.

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ESSENTIAL CHARACTERISTICS OF A LTFM

2 User Friendly and Understandable

A Long-Term Financial Model should:

- not be reliant on specialised user skills;
- clearly communicate the input assumptions required from the user;
- clearly present its outcomes in various formats (graphs and tables);
- be supported by a user manual; and
- be institutionalised with sufficient user training and ongoing support.

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ESSENTIAL CHARACTERISTICS OF A LTFM

3 Objective, Factual and Reliable

A Long-Term Financial Model should:

- incorporate data from reputable sources;
- minimise the risk of user error or intentional user manipulation; and
- present objective outcomes solely reliant on the integrity of the model.

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ESSENTIAL CHARACTERISTICS OF A LTFM

4 Regularly Updated, Quality Maintained, and Adaptable

A Long-Term Financial Model should:

- be supported by a team of professionals;
- be regularly updated and improved to remain relevant; and
- be adaptable to individual municipality's needs.

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ESSENTIAL CHARACTERISTICS OF A LTFM

5 Efficient and Affordable

A Long-Term Financial Model should:

- be efficient in developing a base case and performing sensitivity analysis and scenario testing; and
- create economies of scale to remain affordable to individual municipalities.

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ESSENTIAL CHARACTERISTICS OF A LTFM

1. Intellectually Robust and Sophisticated
2. User Friendly and Understandable
3. Objective, Factual and Reliable
4. Regularly Updated, Quality Maintained, and Adaptable
5. Efficient and Affordable

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Benefits of a Successful Long Term Financial Model (LTFM) & Long Term Financial Plan/Strategy (LTFP/S)

Benefits and Uses of the LTFM

- Assists the municipality in assessing the financial impact of various ***Policy Choices***:
  - Rates & tariff increases
  - Financial impact of catalytic infrastructure/investment programmes
  - Liquidity Policy, Borrowing Policy, Credit Control etc.
- Assists the municipality in assessing the financial impact of ***Changes in the Environment***
  - Population- & economic growth forecasts
  - Growth in indigent households
  - Collection rates, etc.
- Assists the municipality in assessing the financial impact of various ***Alternative Capital Investments***
- Provides an ***Affordability Envelope*** for a Capital Expenditure Framework
- Assists the municipality in devising a ***Capital Funding Mix*** and ***Borrowing Strategy***
- The outcome of the LTFM should ***inform the MTREF***
- The impact of various policy choices on ***Household Bills*** can be illustrated

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Benefits of a Successful Long Term Financial Model (LTFM) & Long Term Financial Plan/Strategy (LTFP/S)

Benefits and Uses of the LTFP/S

- Provides long-term financial certainty and enables integrated long-term planning and implementation
- Provides clarity on what is affordable and informs expectations
- Provides ***Comfort to Lenders*** that the municipality has applied a long term view of financial sustainability that assist with creditworthiness
- Will prove useful in building local partnerships with stakeholders
- Lastly, it bridges the cycle of short-term political tenure

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Thank you

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