



Feasibility Study Report on
Alternative Service Delivery
Mechanisms for the
Pine Forest Resort

August 2011

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Executive Summary

The Witzenberg Local Municipality has appointed Grant Thornton to conduct a feasibility study on alternative service delivery mechanisms for the Pine Forest Resort (Bid 08/2/8/47) and the study has been conducted according to the Municipal Service Delivery and PPP Guidelines Toolkit: Municipal PPPs for Private Sector Commercial use of Municipal Property.

The agreed deliverables include:

- Needs Analysis, which includes:
 - Demonstrating that the project aligns with the municipality's strategic objectives
 - Identifying and analysing the available budget
 - Demonstrating the municipality's commitment and capacity
 - Specifying the outputs
 - Defining the project.
- Project Due Diligence, which includes:
 - A demand assessment
 - A financial cost assessment
 - A legal review based on available information
 - A review of site enablement issues
 - A BEE and Socio-Economic assessment
- Solutions Options Analysis & Output Specification and Value Assessment, which includes:
 - Developing options on the most appropriate commercial activities to be undertaken.
 - Benchmarking of 2 previous PPP options that have succeeded/failed
 - Evaluating and assessing each option
 - Summarising the evaluation and assessment of all options considered
 - Recommending the preferred option
 - Preparing a preliminary output specification that:
 - Describes the services to be delivered
 - Specifies the outputs required to deliver the service
 - Specifies minimum standards
 - Assesses whether the output specification can meet Witzenberg Municipality's ongoing needs
 - Specifies key performance indicators and measurements
 - Recommending the preferred alternative service delivery option

Needs Analysis

The needs analysis found that the project aligns with the strategic objectives of the Witzenberg Municipality as indicated in the IDP and other strategic documents. The SDF for Witzenberg Municipality clearly states that the Pine Forest Resort should be redeveloped and managed in a sustainable manner as a resort and tourism node.

Budget projections indicate that the Pine Forest Resort will incur a loss of R1.8 million in the 2011/12 financial year, R2.2 million in the 2012/13 financial year and R2.6 million in the 2013/14 financial year if it continues to be managed as it is currently managed.

If the resort were to be managed by a private party, these costs will be saved by the municipality as the municipality would not be required to make regular payments to the private party. The assessment of the internal capacity and resources of the municipality has shown that the

municipality would need to incur additional costs to ensure that a competent person is employed by the municipality to manage the contract with the private party on the municipality's behalf.

The project outputs have been identified as:

- Redevelopment of the Pine Forest Resort;
- Upgrading of the facilities of the Pine Forest Resort;
- Contribution by the Pine Forest Resort to the broad based black economic empowerment targets of the Witzenberg Municipality; and
- The management of the Pine Forest Resort in a sustainable manner.

The BEE and social development target of the proposed PPP project should be as set out in the BEE Scorecard for the Tourism Industry.

Due Diligence

The demand assessment for the Pine Forest Resort found that:

- The entrance fee of R55 per person at Pine Forest Resort is slightly higher than the average entrance fee for comparable resorts
- The maximum number of day visitors at the Pine Forest Resort is limited to 100 people per day which provides a maximum of 36 500 per annum. This is below the average visitor number of 55 000 people per annum for the survey sample
- Pine Forest Resort has 97 self catering units and 21 camping sites. The number of self catering units are in line with the size of the resorts in the survey sample, but the number of camping sites could be increased
- The 2011/12 rates for the self catering units range from R289 per 2 or 3 bed unit in the low season to R928 for a 6 bed unit in the high season. The prices are comparable with the rates being charged by the survey sample
- Rates for the camping sites at Pine Forest Resort range from R92 per site for 6 people in the low season to R228 per site for 6 in the high season. The camping prices compare favourably with the rates being charged by the survey sample
- The chalet occupancy of the Pine Forest Resort is low when compared to the survey sample, while the market of Pine Forest is similar to these resorts;
- The leisure activities at Pine Forest Resort include swimming pools, mini-golf, rowing boats, hiking trails and trampoline. The recreation centre includes squash, badminton, table tennis, snooker and darts. These leisure activities are consistent with the activities offered at the resorts in the survey sample
- The hall at the Pine Forest Resort is underutilised and could be utilised as a conference facility in order to expand the market that is currently being targeted. The hall can accommodate at least 300 people in cinema style

Based on our market assessment it is the opinion of the Transaction Advisor that:

- A private party would be able to realise the market demand for the facilities and experiences offered by the Pine Forest Resort
- The Pine Forest Resort would need to be renovated in order for the demand to be realised
- A conference facility could be established at the Pine Forest Resort in order to increase the utilisation of the resort
- A restaurant could be established at the Pine Forest Resort in order to cater to conference delegates, day visitors and overnight visitors

The financial assessment found that the Pine Forest Resort could achieve a net profit from the second year of operation, while achieving a positive net cashflow from the first year of operation if capital of R6.8 million is spent to upgrade the resort and if the resort is managed in accordance with business principles i.e market related rates are charged, sufficient marketing is being done, regular maintenance are conducted and costs are being maintained.

The legal review found that the Witzenberg Municipality do own the land upon which the Pine Forest Resort is located and the land is zoned for use as a resort. No land claims have been registered but 280 stands are currently being leased to individuals on a yearly basis. These leases would need to be terminated if the resort were to be managed by a private party.

No constraints are foreseen in reintegrating the current staff of the Pine Forest Resort into the Witzenberg Municipality.

Site enablement issues that would need to be addressed are:

- Felling of trees that has become old and unstable;
- Fire prevention measures;
- A geotechnical study to confirm that no issues of concern exist in regards to the soil and geology; and
- Replacement of water pipes (which is currently underway)

Options Analysis & Output Specification

An analysis of the potential land use for the Pine Forest site indicated that the current use as a resort would have the most advantages and least disadvantages for the Witzenberg Municipality.

The output specification identified the following services that need to be delivered:

- A quality tourism experience to overnight and day visitors to the Pine Forest Resort;
- A quality management service of the Pine Forest Resort;

In order to deliver these services the key performance indicators and measurements have been identified as:

- Upgrading of the Pine Forest Resort to achieve either a 2-star or 3-star grading by the Grading Council of South Africa;
- Achieving similar occupancies and room rates as comparable resorts;
- Contributing to the income of the Witzenberg Municipality through the payment of a concession fee.

An evaluation of the preferred use of municipal property indicated that that a PPP mechanism would be most suited due to:

- The operation and management of a resort not being a core function of a municipality or an organ of state;
- The PMFA and MFMA that the municipality or organ of state operates under makes procurement services difficult for a resort operation which needs to procure goods and services on a timeous basis;
- A private sector entity could provide the tourism and business expertise and experience required in order to return the resort to economic, environmental and financial sustainability.

Value Assessment

A valuation conducted by the Witzenberg Municipality indicates that the Pine Forest Resort is valued at R20 272 000.

Financial scenarios indicate that the Pine Forest Resort would still be financially viable even with a 15% decrease in the rates charged for the chalets and campsites or a 15 percentage point decrease in the occupancies for the chalets and campsites.

In regards to the concession payment due to the Witzenberg Municipality, the scenarios has indicated that the key factors that would impact on the amount paid are those factors that impact on the gross operating revenue such as occupancies and rates.

The project would thus be affordable to the Witzenberg Municipality as in addition to the concession payment received, the Witzenberg Municipality will save the projected lossess of the Pine Forest Resort under the management of the municipality i.e R1.8 million in the 2011/12 financial year, R2.2 million in the 2012/13 financial year and R2.6 million in the 2013/14 financial year.

The risk analysis indicates that the identified risk can be effectively allocated and mitigated.

Based on the solutions option analysis and output specification as well as the value assessment, it is recommended that the Pine Forest Resort be operated and managed by a private party through a concession agreement with the Witzenberg Municipality.

The key reasons for this service delivery mechanism recommendation are:

- The Pine Forest Resort is currently being operated at a loss by the Witzenberg Municipality;
- The operation of a resort is not a core function of a municipality;
- The concessioning of the Pine Forest Resort will ensure that the Witzenberg Municipality not incur the losses of the Pine Forest Resort and in addition receive a concession payment;
- The private party could manage the Pine Forest Resort in order to achieve the municipality's strategic objectives namely, maximising the benefits that the Pine Forest Resort holds for the Witzenberg Municipality, including the upgrading, development and better management of the resort in order to generate additional revenue for the municipality; and
- Appropriate risk transfer will occur from the Witzenberg Municipality to the private party.

Introduction

A. Background

The Witzenberg Local Municipality (“**the Municipality**”) has appointed Grant Thornton to conduct a feasibility study on alternative service delivery mechanisms for the Pine Forest Resort (Bid 08/2/8/47).

The Pine Forest Resort is situated in Ceres and includes accommodation, conference facilities, swimming pools and recreational facilities such as mini golf, trampolines, etc.

The management of the resort is currently not achieving its true potential and the Municipality does not have the financial and human resources to achieve this true potential. Accordingly the Municipality wishes to investigate alternative service delivery mechanisms in accordance with the Municipal Finance Management Act, 2003 (MFMA), the Municipal Systems Act (MSA) and the Municipal Service Delivery and PPP Guidelines.

The Terms of Reference indicated that the investigation should include:

- An explanation of the strategic and operational benefits of the proposed alternative service delivery mechanisms for the municipality in terms of its strategic objectives and other government policies;
- A description, in specific terms, of the municipal property concerned, how this property has been used, if at all, before feasibility study, and the ways that a private party may legally use the property;
- A demonstration of the financial obligations the proposed alternative service delivery mechanisms will impose on the municipality and the affordability of the alternative service delivery mechanisms for the municipality;
- Setting out the proposed allocation of financial, technical and operational risks between the municipalities and possible private parties;
- Demonstrating the anticipated value-for-money to be achieved by the municipality through the proposed alternative service delivery mechanisms;
- An explanation of the capacity of the municipality to procure, implement, manage, enforce, monitor and report on the proposed alternative service delivery mechanisms.

B. Methodology

The feasibility study on alternative service delivery mechanisms for the Pine Forest Resort has been conducted according to the Municipal Service Delivery and PPP Guidelines Toolkit: Municipal PPPs for Private Sector Commercial use of Municipal Property.

The workplan and deliverables are in accordance with the agreed workplan dated 5 April 2011 attached as **Annexure A**.

The methodology of the relevant sections and deliverables of the study is indicated below.

C. Requirement of a Needs Analysis

According to the Municipal Service Delivery and PPP Guidelines Toolkit: Municipal PPPs for Private Sector Commercial use of Municipal Property the requirements of a needs analysis are:

- Part 1: Demonstrate that the project aligns with the municipality's strategic objectives
- Part 2: Identify and analyse the available budget
- Part 3: Demonstrate the municipality's commitment and capacity
- Part 4: Specify the outputs
- Part 5: Define the project

D. Requirement of a Project Due Diligence

The Municipal Service Delivery and PPP Guidelines Toolkit: Municipal PPPs for Private Sector Commercial use of Municipal Property states that:

“The pre-feasibility will have investigated the municipality's authority under the MFMA to enter into a PPP and the legal issues around ownership of the property. A further thorough investigation must be conducted for this due diligence part of the feasibility study.”

The agreed workplan specifies that the project due diligence will include:

- A demand assessment including very high level tourism and day tripper market research
- A financial cost assessment including projections on the revenue and costs based on the demand assessment
- A legal review based on available information regarding ownership, land use rights, land claims, lease agreements, use of rights of the institution and regulatory matters that may impact on the private party's ability to deliver as expected
- A review of site enablement issues such as environmental matters, geotechnical matters, heritage matters, municipal integrated development plans and infrastructure requirements
- A BEE and Socio-Economic assessment

E. Requirement of a Solutions Option Analysis & Output Specification and Value Assessment

The Municipal Service Delivery and PPP Guidelines Toolkit: Municipal PPPs for Private Sector Commercial use of Municipal Property indicates that the requirements for a value assessment are:

- Part One: Valuation of the entire property
- Part Two: Compiling a business model
- Part Three: Demonstrate affordability
- Part Four: Initial value-for-money test

The agreed workplan specifies that the solutions option analysis & output specification will include:

- Develop Options on the most appropriate commercial activities to be undertaken.
- Examine and report on commercialization activities of 2 previous PPP options that have succeeded/failed (benchmarking)
- Evaluate and assess each option
- Summarise the evaluation and assessment of all options considered
- Recommend the preferred option
- Prepare a preliminary output specification that:
 - Describes the services to be delivered
 - Specifies the outputs required to deliver the service

- Specifies minimum standards
- Assesses whether the output specification can meet Witzenberg Municipality's ongoing needs
- Specifies key performance indicators and measurements
- Recommend preferred alternative service delivery option

The agreed workplan specifies that the value assessment will include:

- Valuation of the entire property to be provided by the municipality
- Prepare a business model with relevant scenarios
- Demonstrate Affordability
- Value for Money Test
- Develop a risk matrix for all project risks:
 - Identify risks
 - Assess the impact of the identified risks
 - Identify strategies to mitigating risks
 - Allocate risks
 - Develop a single risk matrix
- Recommend the alternative service delivery mechanism choice

F. Terminology

The following abbreviations and terminology have been used in this report.

DWAF	Department of Water Affairs and Forestry
EIA	Environmental Impact Assessment
GRAP	General Recognised Accounting Practice
IDP	Integrated Development Plan
IRR	Internal Rate of Return
IT	Information Technology
MFMA	Municipal Finance Management Act
MSA	Municipal Systems Act
PMFA	Provincial Management Finance Act
PPE	Property, Plant & Equipment
PPP	Public Private Partnership
SDF	Spatial Development Framework
TA	Transaction Advisor
The Municipality	Witzenberg Local Municipality
TWK	Theewaterskloof Municipality

Part 1: Needs Analysis: Witzenberg Municipality's Strategic Objectives

1.1 Introduction

The requirement for Part 1 is to demonstrate that the project aligns with the Witzenberg municipality's strategic objectives. Accordingly the vision, mission and strategic objectives of the municipality were sources from various policy and strategic documents and the project was measured for alignment with these strategic objectives.

Not each and every objective from each and every document has been reproduced in our report but a summary of the relevant objectives for the purposes of this study has been provided. Where available the vision and objectives specific to Ceres are specified.

The documents that have been reviewed include:

- Witzenberg Integrated Development Plan (IDP) 2007/2011;
- Witzenberg Public Land Audit, June 2009
- Witzenberg Spatial Development Framework (SDF), January 2006;
- Witzenberg Draft Annual Report V2, 2009/10;
- Witzenberg Local Economic Development (LED) Strategy, March 2005;
- Witzenberg Asset Management Policy, July 2010;
- Witzenberg Budget 2011/2012 – 2013/2014.

1.2 Vision, Mission & Objectives

The Witzenberg Municipality was founded in 2000 and is classified as a Category B municipality. The vision of the municipality as per the Draft Annual Report V2 2009/10 and the IDP 2007/2011 are:

“A united, integrated, prosperous municipality progressively free of poverty and dependency”

The mission of the municipality as per the Draft Annual Report V2 2009/10 and the IDP 2007/2011 are:

“To build a sustainable and environmentally sound Witzenberg that through efficient and effective utilisation of its current resources, establishes a platform for the progressive overcoming of poverty, underdevelopment and provides the basis for a prosperous life for all its citizens”

The goals that have been identified as critical to realise the vision are (as per the IDP 2007/2011):

- Goal 1: To create integrated, sustainable, linked and productive human settlements.
- Goal 2: To build our financial sustainability.
- Goal 3: To deepen and entrench good governance practices, including better communication and public involvement.
- Goal 4: To grow the local economy in order to increase opportunities for participation and equity.

- Goal 5: To foster and strengthen strategic partnerships to make meaningful advances in the areas of health, safety and security, education and training, and poverty alleviation

The strategic thrusts that have been identified to support the goals are (as per the IDP 2007/2011):

- Build human and institutional capacity
- Promote broad based economic growth and empowerment
- Develop smart partnerships
- Focus on vulnerable groups
- Build sustainability

The SDF for Witzenberg Municipality dated January 2006 state within its recommendation for Ceres that:

“Dennebos en omgewing moet herontwikkel en oorgedra word aan regs persoon vir volhoubare bestuur as oord en toerisme-nodus”

The Asset Management Policy for the Witzenberg Municipality dated 1 July 2010 have been reviewed for the purposes of this report as the Asset Management Plan have not yet been obtained from the Witzenberg Municipality.

The Asset Management Policy state that:

“The overall responsibility of asset management lies with the Municipal Manager.

However, the day to day handling of assets should be the responsibility of all officials in terms of delegated authority reduced in writing.”

The land asset register shows that the Pine Forest Resort is located on Erf 1002 and 1003 in Ceres and that the erven are owned by the Witzenberg Municipality (see **Annexure E**). The erven have been jointly valued at R20 272 000 (see **Annexure B**).

1.3 Compliance with the Witzenberg Municipality's Strategic Objectives

The appointment of a service provider to conduct a feasibility study on alternative service delivery mechanisms for the Pine Forest Resort stems from the fact that the management of the resort is currently not achieving its true potential and the Municipality does not have the financial and human resources to achieve this true potential.

The SDF for the Witzenberg Municipality of 2006 also clearly identified the Pine Forest Resort for redevelopment and transfer to an entity that can manage it as a resort and tourism node.

The project is thus deemed to be aligned with the Witzenberg Municipality's strategic objectives.

Part 2: Needs Analysis: Budget

2.1 Introduction

The Municipal Service Delivery and PPP Guidelines Toolkit: Municipal PPPs for Private Sector Commercial use of Municipal Property specifies that within Part 2 the total cost to the municipality of the procurement of the proposed PPP project should be drawn up. Costs already budgeted should be identified as well as any additional costs that may be incurred by the municipality.

Costs may include:

- additional resources to procure and manage the PPP;
- providing infrastructure to the property, which may include utilities;
- maintaining the infrastructure over the term of the PPP agreement;
- zoning or town planning activities that may be required;
- overseeing the property, in recognition of the fact that ownership of the property remains with a municipality over the term of the PPP agreement and afterwards;
- over the term of the PPP agreement to ensure that the private party only conducts agreed upon activities;
- near the end of the PPP agreement to ensure that the property is returned to the municipality in the appropriate condition;
- receiving and accounting for all payments by the private party to the municipality; and
- determining, assessing and collecting any penalties that may be imposed on the private party for breaches of the PPP agreement.

2.1 The Budget

The costs that have already been budgeted for the project are:

- National Treasury has provided a budget of R500 000 for the conducting of the feasibility study
- Cost for the service provider to conduct the feasibility study on alternative service delivery mechanisms for the Pine Forest Resort: R290 700 including VAT and disbursements
- The costs for the operation of the Pine Forrest Resort are shown in the table below. The table clearly indicates that if the Pine Forrest Resort continues to be managed as it is currently managed, the loss will be R1.8 million in the 2011/12 financial year, R2.2 million in the 2012/13 financial year and R2.6 million in the 2013/14 financial year.

Cost centers	Actual	Actual	Current Year (Forecast)	Budget Year	Budget Year +1	Budget Year +2
	2008/2009	2009/2010	2010/2011	2011/2012	2012/2013	2013/2014
REVENUE						
Pine forest: Administration	3 539 712.05	3 734 811.24	4 179 356.00	3 727 080.00	3 842 880.00	3 963 200.00
Pine forest: Security services	0.00	0.00	0.00	0.00	0.00	0.00
Pine forest: Semi permanent units	1 178 511.11	1 451 728.89	1 419 283.00	1 513 372.00	1 602 680.00	1 665 530.00
Pine forest: Cleaning services	0.00	0.00	0.00	0.00	0.00	0.00
Pine forest: Swimming pools	0.00	0.00	0.00	0.00	0.00	0.00
EXPENDITURE						
Pine forest: Administration	-2 761 967.11	-3 028 994.94	-3 587 805.00	-3 892 715.00	-4 221 000.00	-4 544 758.00
Pine forest: Security services	-1 108 534.26	-870 104.89	-1 702 041.00	-1 234 607.00	-1 311 770.00	-1 370 540.00
Pine forest: Semi permanent units	-58 971.42	-50 348.26	-50 374.00	-74 246.00	-78 650.00	-81 800.00
Pine forest: Cleaning services	-1 025 557.69	-1 122 738.18	-1 082 396.00	-1 576 808.00	-1 726 460.00	-1 889 480.00
Pine forest: Swimming pools	-229 494.75	-266 930.10	-300 232.00	-312 022.00	-329 464.00	-351 109.00
SURPLUS/DEFICIT	-466 302.07	-152 576.24	-1 124 209.00	-1 849 946.00	-2 221 784.00	-2 608 957.00

It is projected that the project will result in a user pay PPP i.e. the Municipality would not be required to make regular payments to a private party and therefore no additional budget is proposed.

The ongoing management of the project will be the responsibility of Mr Raymond Esau, Director Finances and Chief Financial Officer. Currently the Municipality is considering the appointment of a Contract and Performance Manager on a post level of 10 and an estimated cost to company of R150 000 a year. These costs have not yet been budgeted for in the municipal budget.

The Transactional Advisor advises that the Contract and Performance Manager would need to be of a higher post level in order to ensure that a suitably qualified person is employed. The ideal candidate would need to have at least 5 to 10 year experience in the management of resorts in order to have the required managerial and tourism and hospitality knowledge to manage the private party on behalf of the municipality. The position requires insight to the daily operation of the resort to ensure that it is effectively managed by the private party.

Part 3: Needs Analysis: Municipal Commitment and Capacity

3.1 Introduction

In this section the current internal capacity and resources of the municipality to manage the PPP agreement is critically assessed.

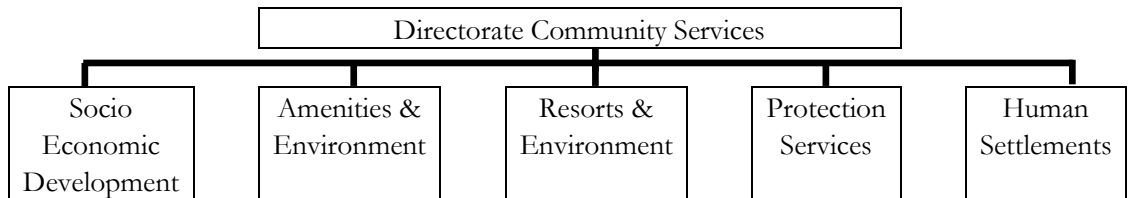
3.2 Staff and Skills Levels

A steering committee has been appointed to oversee the feasibility study on alternative service delivery mechanisms for the Pine Forest Resort. The steering committee consist of representatives of the Witzenberg Municipality and National Treasury:

A summary of the personnel numbers of the Witzenberg Municipality were obtained from the Budget: 2001/2012 – 2013/2014 and is attached as **Annexure C**. The summary indicates that in 2009/10 the Municipality had:

- 5 Municipal Manager and Senior Managers
- 22 Other Managers
- 380 Technicians

The Pine Forest Resort falls under the Community Services Directorate and is currently managed by an Acting Resort Manager. The Community Services Directorate is headed by a directors and the structure is shown below.



The Resort sub-directorate is not only responsible for Pine Forest but also for Kliprivier Park Resort in Tulbagh and all municipal swimming pools. The sub-directorate is headed by a Manager, but this post is vacant and one of two Senior Clerks in the sub-directorate is acting as the Manager.

Section	Staffing	Key Functions/ Processes	Service Levels
Management	1x Manager (vacant) 2x Senior Clerks (one acting as Manager)	Management of function including financial administration	Management of both resorts and all swimming pools

Section	Staffing	Key Functions/ Processes	Service Levels
Pine Forest (Ceres)	2x Senior Clerks (one acting as Manager)	Terrain Maintenance	97 Chalets
	3x Clerks	Building Maintenance	21 Caravan Sites
	Swimming Pools	Reception, resort bookings, financial administration, receipt of fees	350 Permanent sites
	3x Caretakers (1 each per swimming pool)	Swimming pool maintenance	2 halls
	Cleaning		
	2x Leading hands	Access control for resorts and swimming pools (outsourced)	
	14x Workers		
	5x Clean Green Seasonal Workers		
	Terrain Maintenance		
	1x Tractor Driver		
	4x Workers		
	3x Seasonal Workers		
	Building Maintenance		
	4x Workers		

A number of issues plague the resort i.e. trees poses safety hazard, but cannot be felled due to specialised skills and equipment required. Pumps at all swimming pools antiquated and sand filters not replaced in years. Marketing of resorts are not effective and facilities, i.e. boats, trampolines, etc are broken due to insufficient control and supervision. Insurance not utilised to replace damaged facilities.

Although the maintenance of the amenities is their task, teams do not have sufficient skills and certain tasks need to be performed by other sub-directorates. In such instances no quotes are asked and it is perceived that work done by said sub-directorates are then more expensive, but of a lesser quality than what is available in the market. Staff not qualified according to maintenance needs, i.e. pool operators cannot read or write and give incorrect readings, to the detriment of the pools, input from senior staff is not obtained during the appointment of

swimming pools staff. Staff not sufficiently skilled to perform maintenance tasks therefore facilities poorly maintained, leading to unhappy users and a poor reflection on the municipality.

The entire resort structure and operations is therefore dysfunctional and not fully operational. A number of internal audit reports and Auditor General reports have made reference to the poor functioning and operations of resorts and Pine Forest in particular. The resort is currently being managed by Senior Clerk and no real resort management experience and skill currently exists. The capacity to manage and operate the resort optimally is therefore in doubt and clearly needs external intervention.

It is believed that there is sufficient staff at an appropriate skill level to manage the feasibility study on alternative service delivery mechanisms for the Pine Forest Resort.

It is unclear whether there are sufficient skills for the post-procurement phase, in particular, contract management and tourism and hospitality specific general management skills. These skills are required to ensure that the Municipality effectively engage with and manage a private partner to ensure their contractual agreements are met. As indicated in Part 2, it is recommended that the Municipality employs a capable Contract and Performance Manager in order to fulfil the contract management function.

3.3 Stakeholder Analysis

The key stakeholders in the project have been identified as follows:

- Residents on the Pine Forest Resort site
- Organised labour
- The local community and community organisations
- The private sector and Chamber of Commerce
- Government
 - National Department of:
 - Treasury
 - Tourism
 - Provincial Department of:
 - Economic Development and Tourism
 - Treasury
 - Cape Winelands District Municipality
- Cape Town Routes Unlimited
- Environmental Groups

The transactional advisor will be responsible to contact any stakeholders for specific information while the Witzenberg Municipality will conduct any broad and public participation. Accordingly a public participation plan is not addressed in this report.

Part 4: Needs Analysis: Output Specification

4.1 Introduction

In this section the outputs of the proposed PPP project in relation to the requirements of the municipality is described. This will form the basis against which the various options will be assessed and against which the selected option will be tested. The output specification will also serve as the specification for the PPP agreement.

4.2 Output Specification

The project can be described as the utilisation of the Pine Forest Resort in order to achieve its true potential.

The project objectives can be described as maximising the benefits that the Pine Forest Resort holds for the Witzenberg Municipality. This includes the upgrading, development and better management of the resort in order to generate additional revenue for the municipality.

The project outcomes can be described as transforming the Pine Forest Resort into a first class tourists destination with overnight and day visitor facilities.

The project outputs can be described as:

- Redevelopment of the Pine Forest Resort;
- Upgrading of the facilities of the Pine Forest Resort;
- Contribution by the Pine Forest Resort to the broad based black economic empowerment targets of the Witzenberg Municipality; and
- The management of the Pine Forest Resort in a sustainable manner.

The BEE and social development target of the proposed PPP project should be as set out in the BEE Scorecard for the Tourism Industry.

The 7 key areas of focused empowerment and transformation as set out in the Tourism Sector BEE Scorecard are:

- Ownership;
- Strategic Representation;
- Employment Equity;
- Skills Development;
- Preferential Procurement;
- Enterprise Development; and
- Social Development and Industry Specific Factors.

A summary of the Tourism Sector BEE scorecard is provided in **Table 4.1**.

Table 4.1: Tourism Sector BEE Scorecard

Indicator	Weight	Sub-Weight	Measurement	Target
Ownership	20%	20%	% Of direct shareholdings by black people	30%
Strategic Representation	12%	3%	Black people as a % of Board of Directors	50%
		3%	Black women as a % of Board of Directors	25%
		3%	Black people as a % of executive management	50%
		3%	Black women as a % of executive management	25%
Employment Equity	12%	2%	Black people as a % of management	50%
		2%	Black women as a % of management	25%
		2%	Black people as a % of supervisors, junior and skilled staff	65%
		2%	Black women as a % of supervisors, junior and skilled staff	35%
		2%	Black people as a % of total staff	75%
		2%	Black women as a % of total staff	40%
Skills Development	18%	4.5%	% Of payroll spend on skills development	3%
		4.5%	% Of skills development spend on black employees	75%
		4.5%	Number of learnerships as a % of total employees	2%
		4.5%	Number of black learners as a % of learnerships	80%
Preferential Procurement	18%	18%	% Of total procurement spend on BEE compliant companies	50%
Enterprise Development	10%	10%	The sum of the % of post-tax profits and employee time spent on enterprise development	1%
			Enhanced revenue and/or cost savings and/or initiatives facilitated for black owned SMMEs as a % of revenue	1%
Social Development and Industry Specific	10%	6%	% Of post-tax profits or employee time spent on social development	1%
		1%	% Of new recruits with no prior work experience	10%
		3%	Status of TOMSA levy collector	Yes

Source: Tourism BEE Charter 2005

Part 5: Needs Analysis: Defining of the Project

5.1 Introduction

According to the Municipal Service Delivery and PPP Guidelines Toolkit: Municipal PPPs for Private Sector Commercial use of Municipal Property, this part should define the scope of the proposed PPP project, including the project area and the anticipated development responsibilities of both the municipality and the private party.

5.2 Project Scope

The description and indication of outputs provided in Part 4 already provides a good indication of the general scope of the proposed PPP. The proposed PPP could potentially comprise a variety of different facilities/services and it is impossible to specify at this stage (without a detailed feasibility assessment) which facilities/services to include or exclude.

What can be defined is the project outputs namely:

- A comprehensive project proposal;
- Agreed most effective use of the site;
- Modelling of financial alternatives;
- Management agreement; and
- Potential revenue and savings.

Part 6: Due Diligence: Demand Assessment

6.1 Introduction

The demand assessment is not part of the Municipal Service Delivery and PPP Guidelines Toolkit: Municipal PPPs for Private Sector Commercial use of Municipal Property. It has been included in the due diligence report in order to address the requirement that the feasibility study on alternative service delivery mechanisms for the Pine Forest Resort should include:

*“A description, in specific terms, of the municipal property concerned, how this property has been used, if at all, before feasibility study, **and the ways that a private party may legally use the property.**”*

The financial assessment that is included in the next part will build on the market assessment in order to inform:

“A demonstration of the financial obligations the proposed alternative service delivery mechanisms will impose on the municipality and the affordability of the alternative service delivery mechanisms for the municipality.”

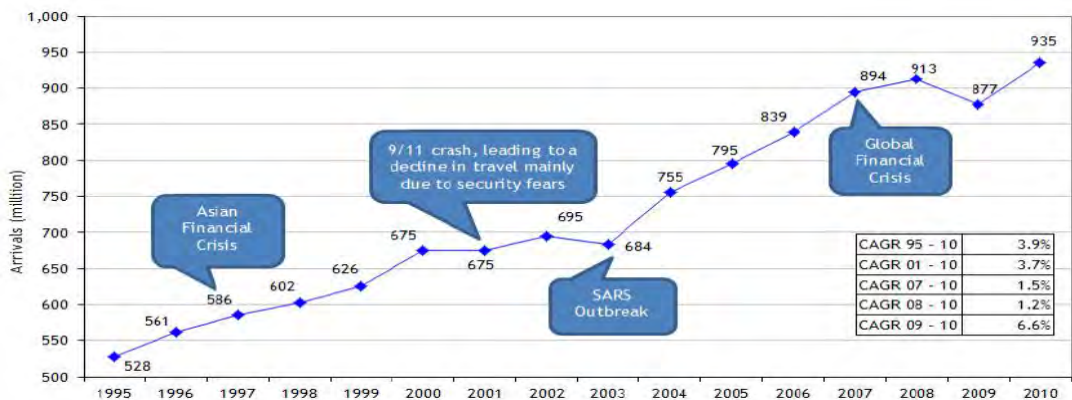
The market assessment includes an analysis of the tourism industry as the demand for the Pine Forest will emanate from the tourism industry. The tourism industry includes both foreign and domestic visitors that stay overnight, as well as day visitors which may emanate from local residents and visitors from the region.

6.2 Foreign Tourism

6.2.1 Global Tourism Context

Global tourist arrivals **declined by 4,3% in 2009** following a peak at 922 million in 2008 (average growth of 4,4% per annum from around 278 million in 1980¹). In January 2010, the World Tourism Organisation (“UNWTO”) forecasted growth rates of 3-4% in international arrivals in 2010.

Figure 6.1: Global inbound tourism: international tourist arrivals (millions)



Source: UNWTO

¹ UNWTO World Tourism Barometer, January 2010 & SAT 2009 Annual Tourism Report

In January 2011, the UNWTO released its latest tourism barometer which shows that International tourism recovered strongly in **2010**. International tourist arrivals were up by almost **7% to 935 million**, following the 4% decline in 2009 (**Figure 6.1**). Despite persistent economic uncertainty and natural disasters, international tourism demand held up well in 2010.

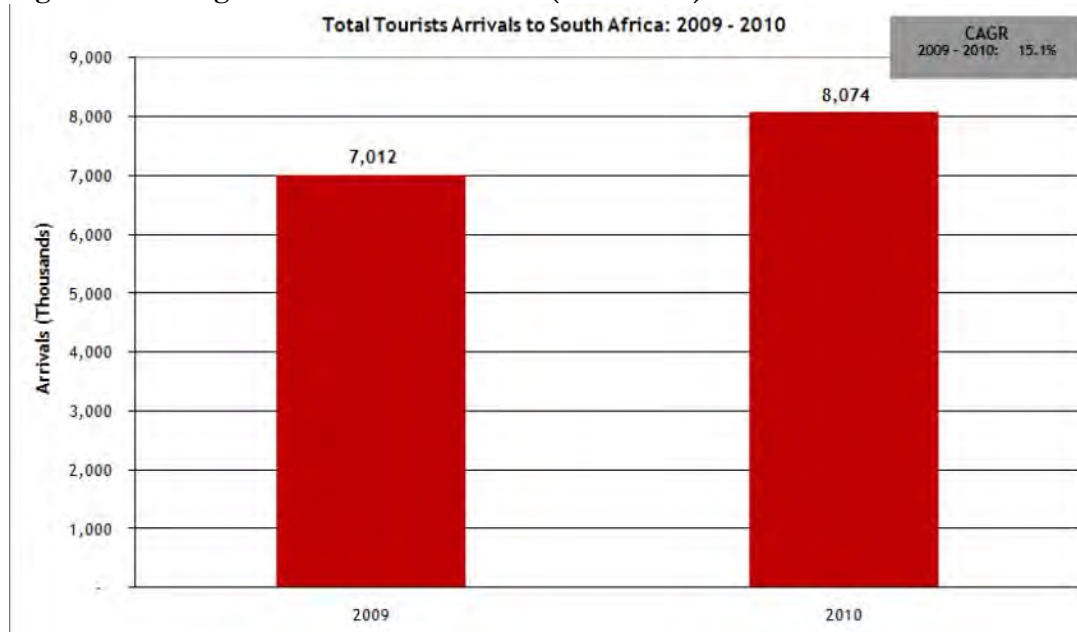
Following a year of global recovery in 2010, growth is expected to continue for the tourism sector in 2011 but at a slower pace. The UNWTO has forecasted international tourist arrivals to grow at between 4% and 5% in 2011, a rate slightly above the long-term average.

6.2.2 Foreign Tourism in South Africa

Total tourist arrivals to South Africa (“SA”) have been on an **upward trend since 2006**, although the incremental increases in tourist arrivals have been declining over time. In 2009 and 2010, SA was one of the few countries to experience a growth in international tourist arrivals when global movements declined. In **2010 tourist arrivals to SA reached 8.1 million** – a 15.1% increase over 2009 (**Figure 1.2**). Arrivals to SA were boosted by the FIFA Soccer World Cup.

A large portion of arrivals are African land arrivals to the country and many are cross-border traders and shoppers and therefore do not make use of recognised tourism products and services. Of the total 8.1 million arrivals to SA in 2010, the number overseas and African air arrival tourists was 2.6 million comprising of **2,3 million overseas arrivals** and **340 000 African air arrivals**.

Figure 6.2: Foreign Arrivals to South Africa (in Millions)



Source: SAT Annual Report 2010

Purpose of Visit

Overall, the main purpose of visit for foreign tourists to SA was **leisure at 57.1%** while visiting for **business purposes** accounted for **30.8%** of trips².

² SAT 2010 Annual Tourism Report

Length of Stay

According to the 2010 SAT Annual Report, the **average length of stay** of foreign tourists to SA in 2010 increased slightly to **8.5 nights** from 8.3 nights in 2009. The average length of stay of **foreign holiday tourists** to SA in 2010 was **10.9 nights**, down from 11.4 nights the previous year. **These changes reflect the global trend towards shorter holidays.**

Bednights

In 2010, foreign tourists spent a total of **66 852 503 bednights** in SA, up 19.8% on 2009 with the majority of the bednights being spent in Gauteng and Western Cape.

Activities Undertaken

In 2010, shopping was the most popular activity undertaken by foreign tourists to SA, followed by nightlife. Holiday tourists engaged in visiting natural attractions, wildlife cultural, historical and heritage and beaches.

Table 6.1: Activities undertaken by Foreign Tourists to SA in 2010

Activities by purpose of visit - 2010									
	Holiday	Shopping - Personal	Shopping - Business	Business traveller	Business tourist	Medical	VFR	Religion	Other
Shopping	97.4%	99.9%	97.8%	89.7%	92.0%	94.2%	98.1%	97.3%	96.3%
Nightlife	91.8%	83.7%	65.8%	83.1%	79.4%	72.3%	79.5%	83.7%	87.9%
Social	33.3%	16.7%	9.0%	12.2%	17.5%	32.6%	90.5%	59.4%	22.1%
Visiting natural attractions	57.3%	0.9%		15.4%	15.6%	1.4%	18.3%		22.7%
Cultural, historical and heritage	42.3%	2.0%		9.5%	12.6%	3.3%	23.1%		18.5%
Business	1.4%		1.9%	83.5%	81.3%		0.9%		3.3%
Beach	38.3%	1.2%	1.5%	9.1%	7.7%	1.8%	14.5%		17.0%
Wildlife	46.4%			9.5%	6.4%		8.7%		13.8%
Theme parks	25.4%	2.3%	0.7%	7.2%	7.6%		12.6%		11.0%
Trading	0.9%	3.6%	66.8%	1.9%			0.6%		
Visited a Casino	13.1%	1.7%		6.8%	4.5%		5.9%		3.2%
Medical	1.6%			0.5%		91.6%	2.0%		1.4%
Sporting spectator	16.3%			3.0%			2.6%		6.1%
Adventure	10.5%			1.2%	1.5%		2.6%		7.5%
Education/training/study	0.5%			0.6%	2.2%		0.4%		45.5%

Source: SAT Annual Report, 2010

Average Spend per Tourist

The average spend per tourist per day were R1 080 in 2010, which is slightly higher than the average spend per day of R1 060 in 2009. The average spend per day of key source markets are:

- UK – R670
- Germany – R540
- USA – R710
- Angola – R1 420
- Lesotho – R960
- Mozambique – R2 480
- Swaziland – R7 380

It should be kept in mind that the tourist arrivals from Africa are visiting mainly for shopping purposes with a shorter length of stay and accordingly their spend per day is higher.

6.2.3 Foreign Tourism to the Western Cape

In 2010, the Western Cape received **1 501 620 foreign tourists** (up 14% on 2009) and was the **second most visited province**. Western Cape's share of the total foreign visitors to South Africa in 2010 was 18.6% which is similar to the 2009 level.

Source Markets

Europe is the biggest source region for foreign visitors to the Western Cape, while Africa and the Middle East are the smallest. In terms of the top ten source countries, Cape Town Routes Unlimited (“CTRU”) reported that the United Kingdom (“UK”) at 18.3% of total arrivals was the number one source country of foreign tourists to the Western Cape in 2010, followed by Germany (9.6%) the United States of America (“USA”) (at 9.2%) and the Netherlands (at 4.5%). Namibia (8.1%), Zimbabwe (4.6%) and Mozambique (4.5%) were the only African Countries included in this list of top ten source countries.

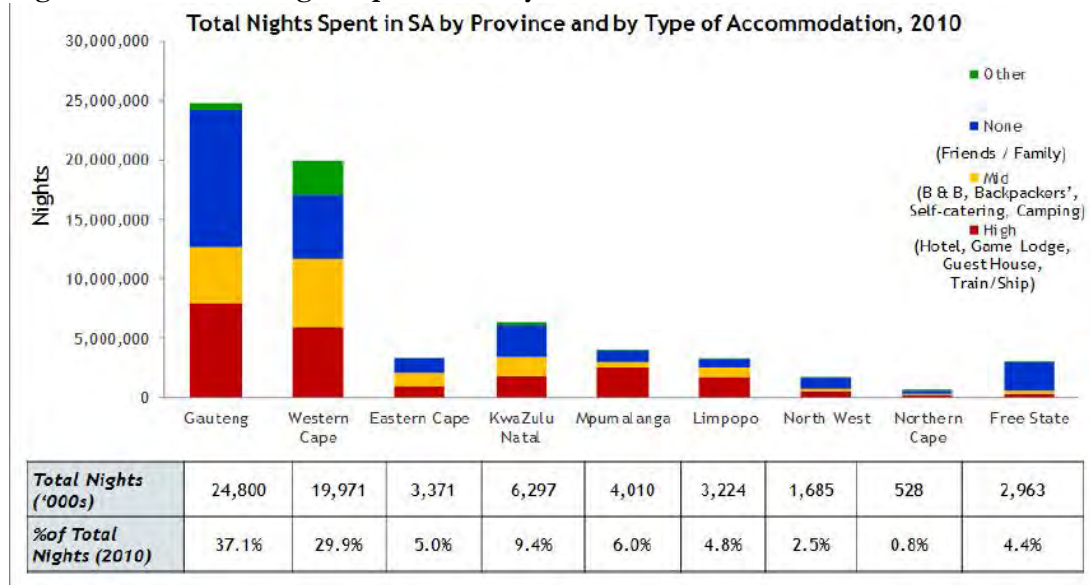
According to previous studies, the main reasons why foreign tourists visit the Western Cape are (listed in order of importance):

- Leisure/ Holiday;
- VFR;
- Business;
- Education;
- Events;
- Conferences; and
- Other reasons such religious or medical purposes.

Bednights

In 2010, a total of **19.97 million foreign bednights** (up 27.3% on 2009) were spent in the **Western Cape Province**, 29.8% of the total foreign bednights spent in SA during 2010.

Figure 6.3: Total Bednights Spent in SA by Province



Source: SAT Annual Report 2010

Most of the bednights were spent in High-end accommodation (hotels, game lodges and guest houses) followed by the Mid-end accommodation which includes self catering establishments and camping sites.

Attractions

11 of the top 20 attractions visited by foreign air arrivals in SA are located within the Western Cape.

Table 6.2: Attractions visited by air arrivals in SA

ATTRactions OR LANDMARKS VISITED BY AIR TOURISTS IN SA : 2009 - 2010		
Top 20 attractions or land marks	2009	2010
V&A Waterfront	920,899	1,024,021
Cape Town Central City	770,249	921,722
Table Mountain Cableway	658,252	767,410
Cape Point	660,074	736,031
The Winelands	591,843	639,056
Beaches	554,234	597,194
Western Cape - Flea/craft markets	408,844	496,970
Sandton Square / Sandton City	324,188	418,623
The Garden Route	342,281	350,515
Nature conservatories	301,811	333,438
Kruger Park via Skukuza, Numbi, Malelane, Crocodile Bride	279,840	273,422
Durban beach front	226,772	265,997
Gauteng - Flea/craft markets	158,175	250,585
Whale watching	247,731	235,792
Robben Island	210,153	228,214
Tour of Soweto	155,705	213,781
Ostrich farms	200,788	206,988
Eastern Cape - Game reserves	168,237	162,059
Cape Town township tours	148,305	158,372
Pretoria's attractions	135,403	157,740

Note: these represent only tourists who have arrived by air
Source: SA Tourism Departure Surveys

Source: *SAT Annual Report, 2010*

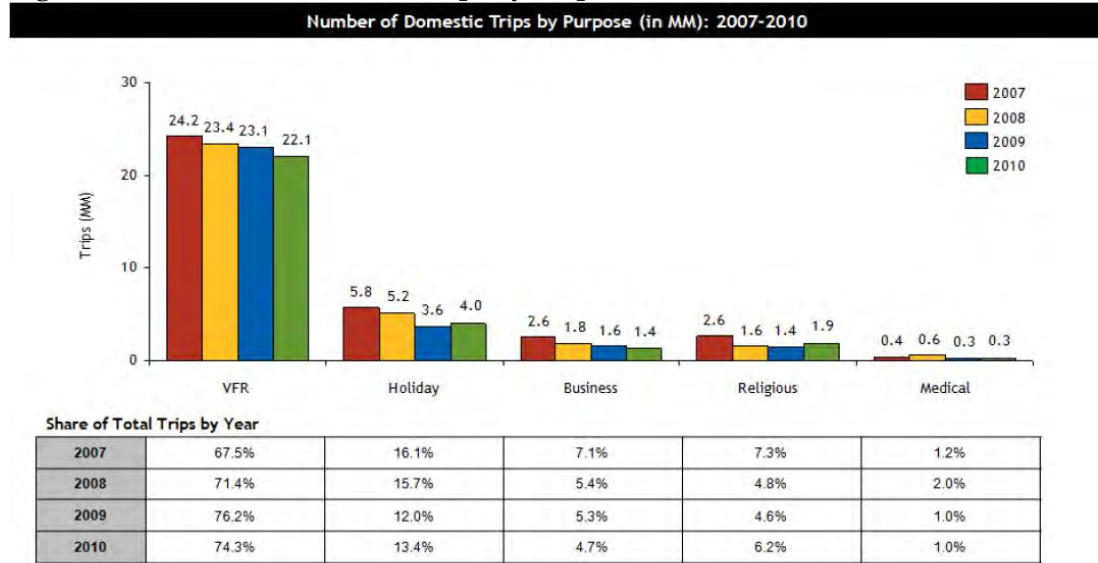
6.3 Domestic Tourism

6.3.1. Domestic Tourism in South Africa

The number of overnight trips taken in South Africa has been declining in recent years with a total of **29.7 million overnight trips** taken in 2010, which is down from the 30.3 million trips taken in 2009, 32.9 million in 2008 and 35.9 million in 2007.

The majority of domestic overnight trips are taken to visit friends and family (“**VFR**”), followed by holiday trips (see **Figure 6.4**).

Figure 6.4: Number of Domestic Trips by Purpose of Visit



Note: Share of trips does not add to 100% because of category "Other" that is not shown on the graph; Holiday includes sports (spectator) and shopping (personal); Business includes business (professional), business (MICE), shopping (resale) and sports (participant)
Source: SAT Domestic Surveys for 2007-2010

Source: SAT Annual Report, 2010

Length of Stay

The average length of **domestic overnight trips in 2010 was 4,4 nights**, which is slightly up from 4.2 nights in 2009.

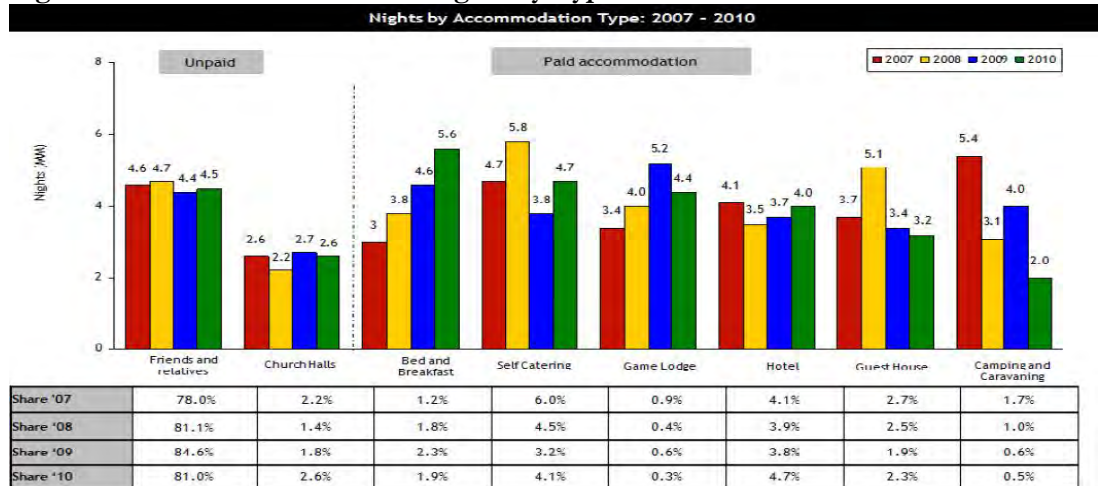
Bednights

In 2010, **130.8 Million domestic bednights** were spent in SA, up from the 128.4 million spent in 2009.

Types of Accommodation Utilised

Staying with friends and family was the most popular type of accommodation utilised in 2010 by domestic overnight travellers. **4.1%** of Domestic nights were spent at **self catering establishments** while **0.5%** trips were spent at **campsites and caravan parks**.

Figure 6.5: Number of Domestic Nights by Type of Accommodation



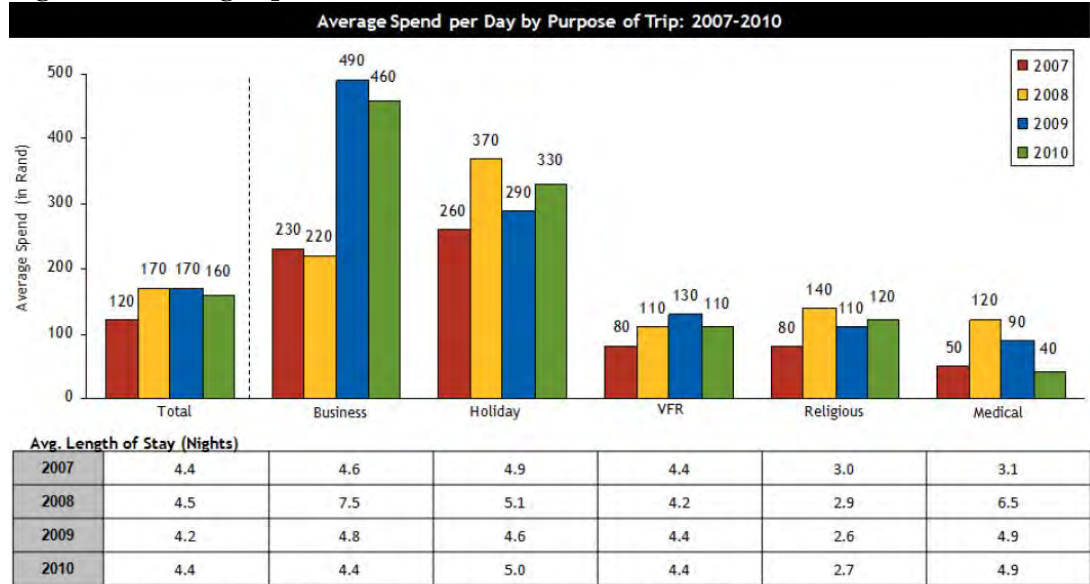
Source: SAT Domestic Surveys for 2007-2010

Source: SAT Annual Report, 2010

Average Spend

The average spend of domestic tourists declined slightly to R160 per day in 2010, from R170 per day in 2009. As to be expected business tourists are the highest spenders, followed by holiday tourists, who spent an average of R330 per day in 2010.

Figure 6.6: Average Spend of Domestic Tourists

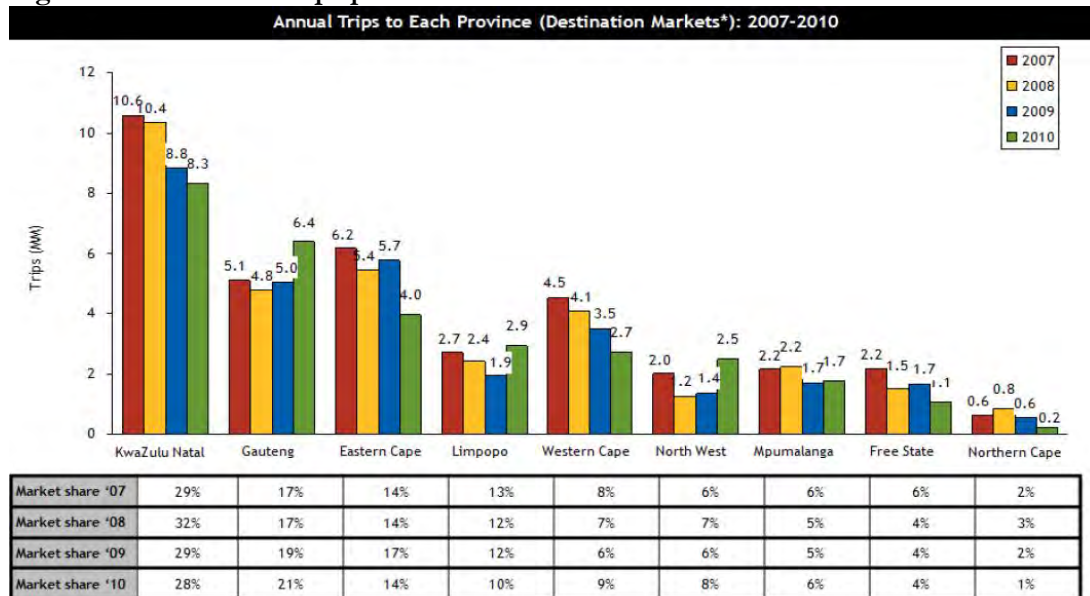


Source: SAT Annual Report, 2010

6.3.1. Domestic Tourism in the Western Cape

The Western Cape received **2.7 million domestic trips in 2010**, which were down from 3.5 million in 2009, 4.1 million in 2008 and 4.5 million in 2007.

Figure 6.7: Domestic Trips per Province



Source: SAT Domestic Tourism Report, Provincial Scorecard 2007-2009

Source Markets

The Western Cape's main domestic source market is residents of the Western Cape with **29% of domestic trips being undertaken by residents of the Western Cape to destinations within the Western Cape** in 2010. Eastern Cape and Gauteng are the other important source markets of domestic tourism to the Western Cape.

Bednights

25.7 million domestic bednights were spent in the Western Cape during 2009. This is a 2.6% decrease from the total annual bednights spent in the Western Cape during 2008.

Types of Accommodation Utilised

Staying with family and friends were the most popular accommodation type utilised by domestic overnight tourists in the Western Cape during 2009. **Self catering establishments were the second most utilised type of accommodation** (receiving 12 400 trips). Camping and caravan parks received only 5 800 trips during 2009.

6.4 Overview of Tourism in the Cape Winelands District

A 2006 study by CTRU found that around 65% to 75% of all **international visitors** to the Western Cape visit the Cape Winelands District, within which Ceres is located. This translates to around 976 000 to 1.1 million foreign tourists.

CTRU also estimates that around 28% to 35% of all **domestic visitors** to the Western Cape visit the Cape Winelands District, which translates to 756 000 to 945 000 domestic tourists.

A survey by CTRU in the fourth quarter of 2010 found that the foreign visitors to the Cape Winelands district originated from Germany (13.2%), the UK (12.5%) and the Netherlands (8.2%). Foreign visitors to Ceres had a similar profile.

Domestic tourists to the Cape Winelands District originated from within the Western Cape (20.6%), followed by Gauteng (8.8%) and KwaZulu-Natal (2.6%). The domestic visitor profile was similar for Ceres.

The most common size of a travel group to the Cape Winelands District were two (61.2%) for both foreign and domestic tourists.

The average length of stay in the Cape Winelands District was four nights with the most common being one night for all tourists. Foreign tourists stayed an average of 3.5 nights in Ceres, while domestic visitors stayed two nights.

The main purpose of visit for all tourists to Ceres was holiday (83.7%), followed by business (7.8%).

6.5 Market Survey

In order to inform our market assessment we conducted primary research amongst the following resorts:

- ATKV Goudini Spa – Rawsonville
- ATKV Hartenbos – Mossel Bay

- Aventura Resort Plettenberg – Plettenberg Bay
- Berg Rivier Resort – Paarl
- Elephant Leisure Resort – Citrusdal
- Kleinplaas Holiday Resort – Oudtshoorn
- Montagu Springs Resort – Montagu
- Na Smit Holiday Resort – Oudtshoorn
- Sanddrif Holiday Resort – Cederberg
- Blue Bay Lodge – Saldanha

In addition a report titled “An evaluation of city owned resorts” which Grant Thornton compiled for the City of Cape Town, were evaluated. The report details the facilities, markets and performance for the following resorts owned by the City of Cape Town:

- Silverstroom
- Soetwater
- Millers Point
- Fish Hoek
- Zandvlei
- Blue Waters
- Monwabisi
- Macassar
- Voortrekker Park
- Harmony Park
- Hendon Park
- Kogel Bay
- Kuilsrivier

The information obtained during the market survey state that:

- Entranced fees range from R25 per person to R50 per person with an additional fee being charged per car ranging from R10 per car to R50 per car. Most resorts charge R25 per person
- The average number of visitors per annum range from 6 000 to 200 000 people per annum. The average number of visitors per annum is 55 000
- The majority of guests to the resorts are domestic visitors (around 95%)
- The majority of the domestic visitors originate from Cape Town (around 80%)
- Between 60% and 100% of the visitors to the resorts are overnight visitors
- The majority (around 90%) of both the overnight and day visitors are families
- The average length of stay for the overnight visitors are 2 nights
- Accommodation facilities at the resorts include self-catering units and camping sites
- The highest number of self catering units at a resort are 237 and the highest number of camp sites are 579
- Rates for self-catering units range from R120 per 2-bed unit in the low season to R2 140 per 8 bed unit in the high season
- Rates for camping range from R100 per site for 6 people in the low season to R490 per site for 6 people in the high season
- Discounts of around 10% are offered to tour operators

- Average annual occupancies for the self-catering unit range between 50% and 68% per annum with the mean occupancy being around 55%. Double occupancies are around 100% meaning that there are at least two people occupying the same unit
- Average annual occupancies for the camping sites are around 30% per annum
- The resorts are most busy over weekends and during the April and December school holiday period, while June, July and August are the least busy
- The length of stay are decreasing from a traditional 14 days to 7 days
- Pensioners and couples without children tend to camp for longer period outside the busy season
- The main source of utilisation is holiday visitors (around 80%), followed by business & conferencing (around 10%) and other purposes such as school groups and sport tours (around 10%)
- Only three of the resorts surveyed had a restaurant facility and the average seating capacity is around 100 people. The utilisation of the restaurant by day visitors range from 10% to 90%, while the utilisation by overnight visitors range between 30% and 60%. The average spend for breakfast is around R80, with lunch being around R100 and dinner around R150
- Only one of the resorts had a bar facility, with around 20% of day visitors and around 60% of overnight visitors utilising the facility. The average spend in the bar was around R100
- Only one of the resorts had a small supermarket which was being utilised by guests
- Three of the resorts had a kiosk selling snacks and food, with around 80% of day visitors and overnight visitors utilising the kiosk. The average spend is around R75
- Seven of the resorts had conference or meeting facilities, with the largest facility being 9 rooms and a maximum capacity of 800 people and the smallest being 1 room that can accommodate 44 people
- Utilisation of the conference facilities ranged from 1 event a week to around 5 a week with the average number of delegates ranging between 20 and 40 people
- Full day conference packages range from R195 per person per day to R395 per person per day
- Leisure activities include hiking, swimming, mini-golf, tennis, volleyball, pool table, games room, trampolines, bird watching and fishing. The utilisation of these activities are high
- All the resorts included a swimming pool
- None of the resorts included a spa

6.6 The Pine Forest Resort

An analysis of the operating performance of the Pine Forest Resort for the period 1 July 2010 to 30 June 2011 indicated that:

- The chalets at the resort operated on a 23.5% annual occupancy;
- The camping sites at the resort operated on a 19.2% occupancy;
- The achieved room rate for the chalets were R446;
- The achieved site rate for the camp sites were R154;
- Discounts of up to 47% were given on rack rates;
- The utilisation of the conference venue were 14.3%;
- The average venue hire was R179;
- 94% of the guests are domestic and 6% foreign; and
- The average length of stay at the resort is 2.5 days.

6.7 Relevance for this study

The following conclusions can be drawn from the primary research and the analysis of the current operating performance of the Pine Forest Resort:

- The entrance fee of R55 per person at Pine Forest Resort is slightly higher than the average entrance fee for comparable resorts
- The maximum number of day visitors at the Pine Forest Resort is limited to 100 people per day which provides a maximum of 36 500 per annum. This is below the average visitor number of 55 000 people per annum for the survey sample
- Pine Forest Resort has 97 self catering units and 21 camping sites. The number of self catering units are in line with the size of the resorts in the survey sample, but the number of camping sites could be increased
- The 2011/12 rates for the self catering units range from R289 per 2 or 3 bed unit in the low season to R928 for a 6 bed unit in the high season. The prices are comparable with the rates being charged by the survey sample
- Rates for the camping sites at Pine Forest Resort range from R92 per site for 6 people in the low season to R228 per site for 6 in the high season. The camping prices compare favourably with the rates being charged by the survey sample
- The chalet occupancy of the Pine Forest Resort is low when compared to the survey sample, while the market of Pine Forest is similar to these resorts;
- The leisure activities at Pine Forest Resort include swimming pools, mini-golf, rowing boats, hiking trails and trampoline. The recreation centre includes squash, badminton, table tennis, snooker and darts. These leisure activities are consistent with the activities offered at the resorts in the survey sample
- The hall at the Pine Forest Resort is underutilised and could be utilised as a conference facility in order to expand the market that is currently being targeted. The hall can accommodate at least 300 people in cinema style

6.8 Recommendations

Based on our market assessment it is the opinion of the Transaction Advisor that:

- A private party would be able to realise the market demand for the facilities and experiences offered by the Pine Forest Resort
- The Pine Forest Resort would need to be renovated in order for the demand to be realised
- A conference facility could be established at the Pine Forest Resort in order to increase the utilisation of the resort
- A restaurant could be established at the Pine Forest Resort in order to cater to conference delegates, day visitors and overnight visitors

Part 7: Due Diligence: Financial Assessment

Due to the sensitivity of the information, the financial assessment has been excluded from this document.

Part 8: Due Diligence: Legal Review

8.1 Introduction

In this section a legal review is conducted based on available information regarding ownership, land use rights, land claims, lease agreements, use of rights of the municipality and regulatory matters that may impact on the private party's ability to deliver as expected.

8.2 Ownership

The Pine Forest Resort is located on Erf 1002 and 1003 in Ceres. A search of the deeds registry has indicated that both Erf 1002 and 1003 are owned by Witzenberg Municipality (see **Annexure E**).

8.3 Land Use Rights

The land is currently being used as a resort and is zoned accordingly. It is not envisaged that the land use would change.

8.4 Land Claims

There are no land claims registered on Erf 1002 and 1003 in Ceres.

8.5 Lease Agreements

There are currently 280 stands within the Pine Forest Resort which are being leased to individuals on a yearly basis (92 timber cabins and 188 stands with tents & caravans). If the Pine Forest Resort is to be operated by a private party, they may want to terminate the leases and redevelop the timber cabin stands.

Accordingly the lease agreements (see **Annexure F**) were analysed in order to investigate the procedure and implications of the termination of the lease agreements.

Clauses 2.1 and 3 are material to the proposed termination of the lease agreement.

Clause 2.1 states that:

"The period of lease is 12 (twelve) months and will commence on the first day of July of each year and continue until 30 June of the ensuing year"

Despite the continued renewal of the lease, even for several successive years, the lease is effective for a period of 12 months only. Each renewal after the 30th June each year constitutes a new lease agreement, even if it is automatically renewed in the absence of a notice.

Clause 3 states that:

“Unless 3 (three) months written notice, by any of the parties hereto, of intention to cancel this agreement is given prior to the termination hereof, it shall be automatically renewed for a further period of 12 (twelve) months on the same terms and conditions and similarly at the end of each renewal period this agreement shall be automatically renewed for a period of 12 (twelve) months, unless 3 (three) written months notice of a contrary intention is given.”

Termination may occur on three months notice. In terms of the above provisions, notice must therefore be given by the 31st March each year, should the Municipality (or the Lessee) intend cancelling the agreement.

While there is no contractual obligation which obliges the Municipality to provide reasons for the termination of the lease agreement, the Municipality must act reasonably in the circumstances. This is because of the obligations placed on organs of state by the Promotion of Administrative Justice Act 3 of 2000. Any administrative action (such as the decision to terminate the lease) by an organ of state (which includes a Municipality) which affects the right of any person falls to be determined by the aforementioned Act.

“Procedurally fair administrative action affecting any person

3. (1) *Administrative action which materially and adversely affects the rights or legitimate expectations of any person must be procedurally fair.*

(2) (a) *A fair administrative procedure depends on the circumstances of each case.*

(b) *In order to give effect to the right to procedurally fair administrative action, an administrator, subject to subsection (4), must give a person referred to in subsection (1) -*

(a) *adequate notice of the nature and purpose of the proposed administrative action;*

(b) *a reasonable opportunity to make representations;*

(c) *a clear statement of the administrative action;*

(d) *adequate notice of any right of review or internal appeal, where applicable; and*

(e) *adequate notice of the right to request reasons in terms of section 5.”*

The above provisions should guide the municipality in respect of its extra-contractual obligations to give notice to the lessees before it may terminate the lease. The three months' notice to terminate may however be adequate in the circumstances, but depends on the facts position at play. If the lease has been in existence for several years, the notice period may be more onerous, i.e. longer than three months. The municipality should also assess to what extent the lessees are adversely affected from a financial perspective.

It is suggested that the Municipality give the contractually required 3 months' notice period, but simultaneously send a notice to lessee/s which accords with the above requirements. It is suggested that the notice to the lessees reads as follows;

“RE: NOTICE TO TERMINATE LEASE: SEMI-PERMANENT CARAVAN STANDS

Notice is hereby given that the Municipality intends to terminate all Semi-Permanent Caravan Stand Leases with effect from (date). We recognise that the aforesaid leases have been effective since (date) and that you may be adversely affected by the proposed termination. It is however the intention of the Municipality to (alternative use/engage in Public Private Partnerships etc) and that this is in the broader interest of the municipality.

In the circumstances, you are afforded an opportunity to make representations to the Municipality within one month of the date of notice hereof, in respect of the proposed termination. All representations must be submitted to the Municipal Offices at (address) for the attention of (name of responsible official/ Municipal Manager)

We note that the Municipality has already given the mandatory 3 months notice of termination of the aforementioned leases as is required in the lease agreement between itself and the respective leases. Such notice is however subject to the above representations being properly considered by the municipality during such period but does not affect the date of termination should the municipality nevertheless decide to terminate the lease agreements”

Note that the full prescripts of the Promotion of Administrative Justice Act and its regulations must be followed carefully. Quoted hereunder are the other provisions of the Act and Regulations for ease of reference.

Section 4 of PAJA provides that in cases where an administrative action materially and adversely affects the rights of the public, an administrator, in order to give effect to the right to procedurally fair administrative action, must decide whether –

- “
- (a) to hold a public inquiry in terms of subsection (2);
 - (b) to follow a notice and comment procedure in terms of subsection (3);
 - (c) to follow the procedures in both subsections (2) and (3);
 - (d) where the administrator is empowered by any empowering provision to follow a procedure which is fair but different, to follow that procedure; or
 - (e) to follow another appropriate procedure which gives effect to section 3.”

The effect of Section 4 is that the Department has to choose which one of the aforementioned administrative procedures to follow. If the Municipality follows a notice and comment procedure, it must³ –

- “
- (a) take appropriate steps to communicate the administrative action to those likely to be materially and adversely affected by it and call for comments from them;
 - (b) consider any comments received;
 - (c) decide whether or not to take the administrative action, with or without changes;
- and

³ Section 4 (3) of PAJA

(d) comply with the procedures to be followed in connection with notice and comment procedures, as prescribed.”

It is evident from the aforementioned, that regulations regarding the notice and comment procedure must be followed. Regulations⁴ published in 2002 make it mandatory to follow the prescripts thereof. The applicable sections of the aforementioned regulation read as follows:

“18. *Publication -*

1. *Information concerning the proposed administrative action must be published by way of notice –*

(a) if the administrative action affects the rights of the public throughout the Republic, in the Government Gazette and a newspaper which is distributed, or in newspapers which collectively are distributed, throughout the Republic; or

(b) if the administrative action affects the rights of the public in a particular province only, in the Provincial Gazette of that province and a newspaper which is distributed, or in newspapers which collectively are distributed, throughout that province; or

(c) if the administrative action affects the rights of the public in a specific area only, in a newspaper which is distributed in that specific area.

2. *A notice published in terms of subregulation (1) must include*

(a) an invitation to members of the public to submit comments in connection with the proposed administrative action to the administrator concerned on or before a date specified in the notice, which date may not be earlier than 30 days from date of publication of the notice;

(b) a caution that comments received after the closing date may be disregarded;

(c) the name and official title of the person to whom any comments must be sent or delivered; and

(d) the –

(i) work, postal and street address and, if available, also an electronic mail address;

(ii) work telephone number; and

(iii) fax number, if any, of the person contemplated in paragraph c.

3. *A notice published in terms of subregulation (1) must -*

(a) contain sufficient information about the proposed administrative action to enable members of the public to submit meaningful comments; and

⁴ Published in GN 1022 on 31 July 2002

- (b) *when appropriate, specify a place or places where, and the hours within which, further information concerning the proposed administrative action will be available for public scrutiny.*
4. *A notice published in terms of subregulation (1)(a) and (b) in a newspaper may, notwithstanding the provisions of subregulations (2) and (3), only contain -*
- (a) *a concise statement of the proposed administrative action;*
- (b) *the name, official title, contact telephone number and physical address of the person from whom further information on the proposed administrative action and the administrative procedure can be obtained; and*
- (c) *a note that a more detailed notice concerning the proposed administrative action appears in the Government Gazette or Provincial Gazette, as the case may be.*
5. *If a notice published in terms of subregulation (1) specifies a place or places where further information about the proposed administrative action will be available for public scrutiny, access to that information must be allowed from the date on which the notice is published until the closing date for comment, with the exclusion of Saturdays, Sundays and public holidays.*
6. *In order to ensure that a proposed administrative action is brought to the attention of the public, an administrator may, in addition, publicise the information referred to in subregulations (1) to (5) by way of communications through the printed or electronic media, including by way of press releases, press conferences, the Internet, radio or television broadcasts, posters or leaflets.*
19. *Language -*
1. *A notice published in terms of regulation 18(1) must be in at least two of the official languages.*
2. *A notice published in terms of regulation 18(1)(b) or (c) must take account of language preferences and usage in the province or area concerned.*
3. *Written comments may be in any official language.”*

8.6 Other Regulatory Matters

The use rights of the Witzenberg Municipality i.e. the use of the Pine Forest Resort which is municipal property by another entity, including a private party in a possible PPP has been reviewed. Taking the precedent of other PPP's it is the opinion of the Transaction Advisor that the Pine Forest Resort could be utilised by a private party through a PPP process.

Other regulatory matters that may impact on the private party's ability to deliver as expected include tax legislation, labour legislation, environmental & heritage legislation, foreign exchange legislation, legislation governing the use of certain financial instruments, competitive legislation and sector regulations such as potable and wastewater treatment standards, solid waste transportation and disposal standards.

The only other regulatory matter that may impact on the private party's ability to deliver as expected is labour legislation. The tourism industry is subject to the Hospitality Sectoral Determination No 14 of 2007 which prescribes a minimum wage for employees. The private party would need to adhere to this legislation.

The private party would also need to be cognisant of the current staff compliment at the Pine Forest Resort. Negotiations with staff would need to be initiated to gauge whether the staff would prefer to remain in the employment of the Witzenberg Municipality or whether they would want to be absorbed in the structure of the private party.

The Witzenberg Municipality has indicated that the current staff compliment at the Pine Forest Resort could remain in the employment of the Witzenberg Municipality and they could be redeployed to other positions within the municipality. The budget allocation for their salaries has already been made by the Witzenberg Municipality.

Part 9: Due Diligence: Site Enablement Issues

9.1 Introduction

In this section a review of the site enablement issues are conducted based on available information regarding environmental matters, geotechnical matters, heritage matters, municipal integrated development plans and infrastructure requirements.

9.2 Environmental

It is not envisaged that an environmental impact assessment would need to be conducted as the Pine Forest Resort would continue with its current use as a leisure resort.

An environmental issue that has been raised is the state of the trees on the Pine Forest Resort. The trees have become old and some have toppled over causing damage to property. The trees are estimated to topple over at a rate of one to two every six months.

The felling of these trees is problematic as specialist equipment does need to be procured from Cape Town and brought to Ceres at great cost. The Witzenberg Municipality has advised the tenants of the timber cabin stands to secure additional insurance for potential damage from the trees that topple over.

Other environmental issues include the danger of fires on the site (given the number of Pine Trees) and the maintenance of firebreaks with surrounding properties.

The occasional problem with baboons has also been raised.

9.3 Geotechnical

Geotechnical issues relates to the soil and geology of the Pine Forest Resort. There no known issues in regards to the soil and geology that would prevent a PPP transaction. It is advisable though to conduct a geotechnical analysis of the site in order to confirm this.

9.4 Heritage

The Pine Forest Resort is not classified under the National Heritage Resources Act or the Heritage Resources Authority. Accordingly it is not foreseen that it would be required to notify the Heritage Resources Authority of the proposed development.

9.5 Municipal IDPs

It has been shown in the Needs Analysis Report that the development of the Pine Forest Resort is aligned with the Witzenberg Municipal IDP.

9.6 Infrastructure Requirements

The issues raised in regards to the infrastructure requirements for the Pine Forest Resort are:

- **Water:** The water pipes are old and some have burst. A detailed inspection of the water pipe infrastructure is required before the Pine Forest Resort can be incorporated in a PPP transaction. The upgrading of the pipes is currently underway;

- **Sewer:** The state of the water pipes and its impact on the sewer pipes need to be clarified and a detailed inspection of the water and sewer pipe infrastructure is required before the Pine Forest Resort can be incorporated in a PPP transaction
- **Electricity:** The electricity supply is sufficient for the requirements of the Pine Forest Resort
- **Telecommunications:** The telecommunications provision is sufficient for the Pine Forest Resort

The maintenance plan for the period 2010 to 2011 indicates the extent of the general repairs and maintenance that would need to be conducted (see **Annexure G**).

Part 10: Due Diligence: BEE & Socio Economic Assessment

10.1 Introduction

Part 5 includes a BEE and Socio-Economic Assessment including identifying sectoral BEE conditions, black enterprise strength in the sector and the local area, the ability of communities to take advantage of possible benefits and BEE constraints for the sector as well as socio-economic factors for the project location.

10.2 The Tourism Sector BEE Scorecard

The BEE and social development target of the proposed PPP project should be as set out in the BEE Scorecard for the Tourism Industry.

The 7 key areas of focused empowerment and transformation as set out in the Tourism Sector BEE Scorecard are:

- Ownership;
- Strategic Representation;
- Employment Equity;
- Skills Development;
- Preferential Procurement;
- Enterprise Development; and
- Social Development and Industry Specific Factors.

A summary of the Tourism Sector BEE scorecard is provided in **Table 10.1**.

Table 10.1: Tourism Sector BEE Scorecard

Indicator	Weight	Sub-Weight	Measurement	Target
Ownership	20%	20%	% Of direct shareholdings by black people	30%
Strategic Representation	12%	3%	Black people as a % of Board of Directors	50%
		3%	Black women as a % of Board of Directors	25%
		3%	Black people as a % of executive management	50%
		3%	Black women as a % of executive management	25%
Employment Equity	12%	2%	Black people as a % of management	50%
		2%	Black women as a % of management	25%
		2%	Black people as a % of supervisors, junior and skilled staff	65%
		2%	Black women as a % of supervisors, junior and skilled staff	35%
		2%	Black people as a % of total staff	75%
		2%	Black women as a % of total staff	40%
Skills Development	18%	4.5%	% Of payroll spend on skills development	3%
		4.5%	% Of skills development spend on black employees	75%
		4.5%	Number of learnerships as a % of total employees	2%
		4.5%	Number of black learners as a % of learnerships	80%
Preferential Procurement	18%	18%	% Of total procurement spend on BEE compliant companies	50%
Enterprise Development	10%	10%	The sum of the % of post-tax profits and employee time spent on enterprise development	1%
			Enhanced revenue and/or cost savings and/or initiatives facilitated for black owned SMMEs as a % of revenue	1%
Social Development and	10%	6%	% Of post-tax profits or employee time spent on social	1%

Indicator	Weight	Sub-Weight	Measurement	Target
Industry Specific			development	
		1%	% Of new recruits with no prior work experience	10%
		3%	Status of TOMSA levy collector	Yes

Source: Tourism BEE Charter 2005

10.3 Witzenberg BEE Conditions

The state of the tourism industry in the Western Cape and the Witzenberg Municipality is based on indicative evidence as there is limited research available for comparison. We believe that transformation of the tourism industry in the Western Cape and the Witzenberg Municipality would be more or less similar to that of the South African Tourism Industry given the Western Cape’s share of the foreign and domestic tourism market.

Discussions with tourism stakeholders during the compilation of a provincial tourism study indicated that transformation seem slow to some stakeholders and that others believe that good progress has been made. We believe that more information regarding transformation should be disseminated to the tourism industry in order to dispel the perception that transformation is only about the transfer of ownership. As the majority of tourism enterprises are SMME’s they find it difficult to support transformation because they believe that they would have to transfer ownership of their business. The fact that transformation could also occur through strategic representation, employment equity, skills development, preferential procurement and enterprise development should be explained.

The Witzenberg Municipality has indicated that they will utilise their own preferential scoring as per the procurement policy of the municipality, when awarding the tender for a private party.

10.4 Witzenberg Socio-Economic Conditions Pertinent to this Transaction

The Witzenberg IDP 2007/2011 indicated the high poverty level of the Witzenberg population. The study also indicated the lack of diversity in the economy of the Witzenberg Municipality.

The redevelopment of the Pine Forest Resort will address the challenges of poverty by providing employment to mainly unskilled and semi-skilled people as around 50% of employment opportunities created by a tourism resort is for unskilled or semi-skilled people.

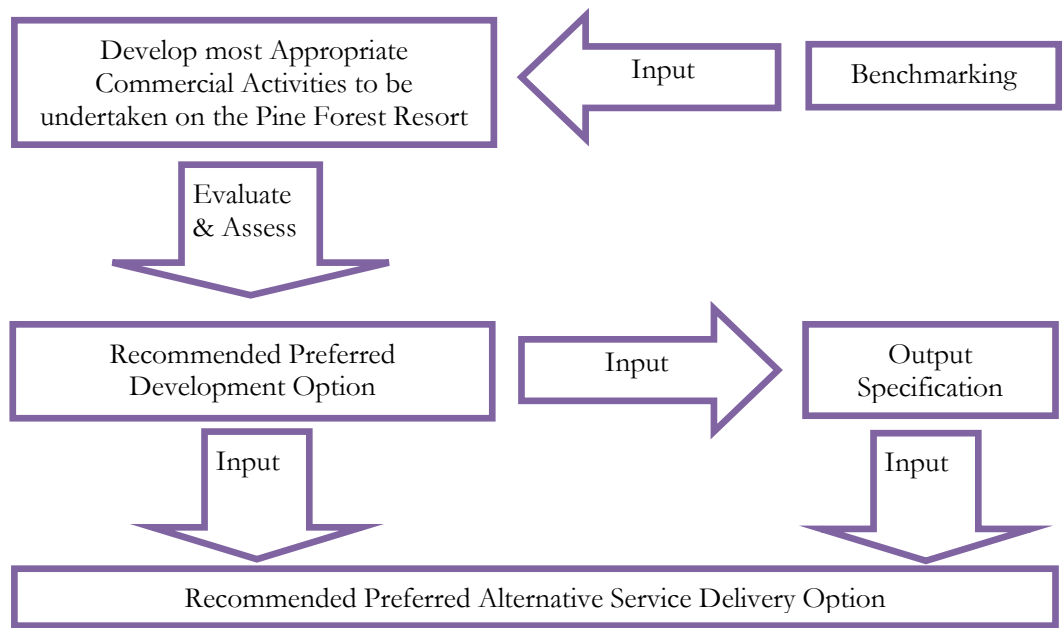
The tourism resort will also bring diversity to the economy of the Witzenberg Municipality. The resort will focus on the services industry rather than the agricultural industry but could utilise the products of the agricultural industry to provide this service i.e. utilising food produced in the area to feed tourists to the resort.

Part 11: Options Analysis & Output Specification

11.1 Introduction

In this section the most appropriate commercial activities to be undertaken on the Pine Forest Resort site is developed and assessed. Based on the preferred development option, the outputs are specified. The preferred alternative service delivery option is then specified in order to deliver the specified outputs.

Our approach to this section is shown in the diagram below.



11.2 Commercial Activity Options Analysis

The potential commercial activities that could be conducted on the Pine Forest Resort site could be broad and varied. In order to filter the number of potential commercial activities to realistic potential activities we have developed a matrix to assess the potential land use for the Pine Forest Resort site.

Table 1.1: Assessment of the Land Use of the Pine Forest Site

Leisure	
Advantages <ul style="list-style-type: none"> • Current use of the site – facilities are already suited for the type of land use • No rezoning required 	Disadvantages <ul style="list-style-type: none"> • Continuous maintenance costs
Residential	
Advantages <ul style="list-style-type: none"> • Provision of additional housing to address housing backlog 	Disadvantages <ul style="list-style-type: none"> • Rezoning required • Additional infrastructure required on site • Additional pressure on water, electricity and

	sewerage resources of the municipality • Competition with existing residential developments
Retail	
Advantages • Provision of retail facilities	Disadvantages • Rezoning required • Additional infrastructure required on site • Additional pressure on water, electricity and sewerage resources of the municipality • Competition with existing retail developments • Lack of demand for retail space
Commercial	
Advantages • Provision of commercial facilities	Disadvantages • Rezoning required • Additional infrastructure required on site • Additional pressure on water, electricity and sewerage resources of the municipality • Competition with existing commercial developments • Lack of demand for commercial space
Industrial	
Advantages • Provision of industrial facilities	Disadvantages • Rezoning required • Additional infrastructure required on site • Additional pressure on water, electricity and sewerage resources of the municipality • Competition with existing industrial developments • Lack of demand for industrial developments

Based on the above assessment it is recommended that the current use of the Pine Forest Resort be retained as it would not require rezoning, additional infrastructure or place additional pressure on the service infrastructure of the municipality.

11.3 Benchmarking

The following two case studies have been assessed in order to benchmark the type of business to be conducted on the Pine Forest Resort site.

11.3.1. City of Cape Town – Oatlands Resort

The Oatlands Resort is an existing resort owned by the City of Cape Town and **located** in Main Road at Froggy Pond in Simon's Town. Attractions in the area include Boulders Beach and the Simon's Town harbour.

The accommodation facilities at the resort consist of 8 Round Houses (Rondavels) each with a double bed, 10 A-style chalets able to sleep 6 people and 7 B-style chalets able to sleep 4 people. The resort also includes 48 electrified caravan sites.

Other facilities include 3 conference rooms able to accommodate 25, 45 and 100 people respectively, an English style pub utilised for meals served to the conference groups, a swimming pool, trampoline, swings & see saws and a laundrette.

The resort has previously been graded as a 2-star facility but the grading process has not been done since 2008. The accommodation facilities at the resort are currently being upgraded but the majority of the accommodation facilities are still in need of general refurbishment particularly in regards to repainting and the replacement of furnisher.

The resort is currently being leased by a private operator from the City of Cape Town and has a staff compliment of 13 people with a small onsite management team.

The management of the Oatlands Resort indicated that their **market** is predominately conference delegates. They indicated that as much of 70% of the utilisation of the accommodation facilities consist of conference delegates, with 30% consisting of visitors during Easter and December holidays.

The management has indicated that they achieve high room occupancies through this market with average annual occupancies being around 80%. Busy months are February, December, September and January with less busy months being June, July, October and November.

Indications are that as much as 98% of the conference delegates attending an event at Oatlands Resort require overnight accommodation. The majority of these conferences are being held over the weekend with Thursday and Friday being included in many of the events.

The management of Oatlands Resort has indicated that they would like to expand the conference facilities at the resort in order to capitalise on the conference market, along with an expansion in the number of rooms.

It should also be noted that the management indicated that they provided a variety of discounts to conference delegates in order to secure the event. The market is thus budget driven with management rather filling rooms at lower prices than have empty accommodation.

The **financial analysis** of Oatlands Resort shows that the policy of the resort to provide large discounts to secure business, has a significant impact on the financial returns that the resort is able to achieve.

The financial analysis has also shown that the resort will be able to pay the City of Cape Town a higher lease payment if it achieves market related rates. Also, the City of Cape Town could negotiate a management contract and be able to pay the operator a fee that is on par with variable payments as a percentage of total gross revenue of management, as well as higher than market related levels of marketing and repair & maintenance overheads if it is able to achieve market related rates.

The debate now arises as to whether a strategy to drive occupancies at the expense of rates is preferable to driving higher rates at lesser occupancies. The argument is also made that business at a lower rate is better than no business at all.

It is argued that a golden midway may be found with the current operation continuing as is, while a higher share of marketing is being spend to attract a higher paying level of clientele. This marketing drive should be coupled with a higher spend on repairs and maintenance in order to upgrade the resort to a high level 2-star facility.

Given that the main marketing tool of the resort is word of mouth, the improved facilities should lead to an improved image of the resort in the market and ultimately increased utilisation.

It was recommend that a management type contract be negotiated and that the payment from the City of Cape Town be linked to gross revenue and GOP in combination with an agreed budget for marketing and repairs and maintenance. This will ensure that the payments from the City of Cape Town incorporate fluctuations in the tourism industry as well as ensuring that the required marketing and repairs and maintenance are conducted to capture the target market.

The variable payment could consist of a basic fee of 5% of total gross revenue as well as an additional fee of 10% of gross operating profit.

The marketing spend could be at least 10% of total gross revenue with the repairs and maintenance budget being determined by the repairs and maintenance required, but at least 10% of total gross revenue.

Lessons for the Pine Forest Resort

- A resort owned by a municipality could be leased to a private party, but the lease needs to be managed in order to ensure that the resort is not being mismanaged;
- Higher returns could be achieved by a private party but the relationship between the municipality and the private party should be structured correctly to ensure that the municipality have insight to the business strategy of the private party;
- Sufficient budget should be allocated in order to ensure that the facilities are maintained;
- The contract between the municipality and the private party should be structured in such a way that both parties carry appropriate risk, but also share in appropriate reward.

11.3.2. Eikenhof Dam Resort – Grabouw

The Eikenhof Dam Resort was a proposed development of a sustainable, environmentally friendly resort on an upper 3-star, lower 4-star level at the Eikenhof Dam in Grabouw. The resort was proposed to include the following:

- 150 room
- 100 time share chalets (2 bedroom/6 sleeper)
- 4 corporate lodges (sleeps 10 people)
- Conference facility (250 pax)
- Wedding chapel (100 to 150 pax)
- Spa (5 treatment rooms)
- Restaurant (150 pax)
- Bar with wine cellar for wine tastings
- Indoor sports court (basket ball, volley ball, etc) and gym
- Swimming pools – 1 kids pool, 1 adult pool and a water slide
- Youth Centre with 70 bed youth hostel
- Parking & back of house facilities
- Walkways/jogging path
- A number of Jungle gyms and play pits around the area
- Games room with pool tables, darts, table soccer, ping pong and video games
- Non motorized water sport i.e. recreational canoeing and sailing
- Hiking – may need MTO cooperation
- Mountain biking – may need MTO cooperation
- Bird watching
- Wine tasting
- Apple tasting, cooking, processing, etc
- Star gazing
- Beach volley ball court
- Trampolines
- One multi purpose sports field – soccer, rugby, hockey, etc
- Mini golf – Putt Putt
- Electronic clay pigeon shooting
- Archery/slingshot shooting
- Paintball
- Pottery and painting classes
- General child minding facilities

In 2008 the project cost was estimated at R477 million including escalation and VAT, but excluding the cost of bringing bulk services to the site. Around R88 million of this cost was projected escalation costs due to the time required for the transfer of land, EIA, rezoning and procurement of a developer.

The proposed resort was projected to achieve net profit from the 5th year of operation, while achieving a positive net cashflow from the 3rd year of operation. The development was

projected to achieve an ungeared, pre-tax Internal Rate of Return (“**IRR**”) over 20 years of 9,8%.

It was projected that the Theewaterskloof (“**TWK**”) Municipality would receive a concession payment of around R9,6 million per annum.

The risk analysis indicated that the main risks to the municipality include:

- Land not transferred to TWK Municipality or taking many years;
- The required planning and EIA approvals are not granted;
- Unavailability of bulk services;
- Unavailability of the required sustainability technology; and
- The construction not being up to standard.

All other risks are transferred to the developer.

The fatal flaw analysis indicated that:

- The transfer of the land from DWAF may not occur
- The quality of the dam’s water could be jeopardised
- The EIA process may not provide the required approvals
- Bringing bulk services to the site would be expensive
- The development will operate at low margins

It was recommended that the transaction does not continue to the procurement phase, given the time period involved to transfer the land and conduct the EIA.

Lessons for the Pine Forest Resort

- Long timeframes in order to complete the transaction adds significantly to the development cost due to escalation of construction materials;
- It needs to be ensured that the municipality owns the relevant land prior to conducting a planning exercise;
- Significant returns for the municipality could be realised by engaging a private party to develop a resort.

11.4 Output specification

This section aims to describe the commercial use of municipal property to be delivered and to specify the outputs required to deliver this commercial use. It also aims to specify minimum standards and to assess whether the output specification can meet Witzenberg Municipality’s objectives. Finally it aims to specify key performance indicators and measurements.

As indicated in the Needs Analysis Report, the project can be described as the utilisation of the Pine Forest Resort in order to achieve its true potential. In order to achieve this goal the following services needs to be delivered:

- A quality tourism experience to overnight and day visitors to the Pine Forest Resort;

- A quality management service of the Pine Forest Resort;

The project outputs needed to deliver the commercial use of municipal property can be described as:

- A redeveloped Pine Forest Resort;
- Upgraded facilities of the Pine Forest Resort;
- Additional revenue generated for the municipality;
- Contribution by the Pine Forest Resort to the broad based black economic empowerment targets of the Witzenberg Municipality; and
- The management of the Pine Forest Resort in a sustainable manner.

The Witzenberg Municipality's objectives can be best described as maximising the benefits that the Pine Forest Resort holds for the Witzenberg Municipality. This includes the upgrading, development and better management of the resort in order to generate additional revenue for the municipality.

The output specification should be able to meet the objectives of the municipality.

The key performance indicators and measurements are:

- Upgrading of the Pine Forest Resort to achieve either a 2-star or 3-star grading by the Grading Council of South Africa;
- Achieving similar occupancies and room rates as comparable resorts;
- Contributing to the income of the Witzenberg Municipality through the payment of a concession fee.

11.5 Preferred Use of Municipal Property Option

An evaluation matrix has been compiled in order to recommend the preferred use of municipal property option. The potential service delivery options are:

- An Internal mechanism:
 - A department or other administrative unit within its administration
 - Any business unit devised by the municipality, provided it operates within the municipality's administration and under the control of the council in accordance with operational and performance criteria determined by the council
 - Any other component of its administration
- An External mechanism, by entering into an agreement with:
 - A municipal entity
 - Another municipality
 - An organ of state such as a licensed service provider registered or recognised in terms of national legislation
 - Any other institution, entity or person legally competent to operate a business activity

	Internal Mechanism		External Mechanism			
	Department or Administrative Unit	Municipal Business Unit	Municipal Entity	Another Municipality	Organ of State – Licensed Service Provider	Private Party
Advantages	<ul style="list-style-type: none"> Strengthening of the in-house capacity 	<ul style="list-style-type: none"> Can provide a one-point service Can align the income & expenditure nature of the resort Can allow for a more devolved decision making process 	<ul style="list-style-type: none"> Ring-fenced entity with total responsibility for service delivery 	<ul style="list-style-type: none"> Established service delivery organisation 	<ul style="list-style-type: none"> Technical and managerial skills 	<ul style="list-style-type: none"> Tourism & leisure sector expertise Ability to raise its own funds Ability to take on risk
Disadvantages	<ul style="list-style-type: none"> Lack of tourism & leisure sector expertise Lack of in-house capacity Lack of fund raising ability Management of a resort is not a core function 	<ul style="list-style-type: none"> Lack of tourism & leisure sector expertise Possible duplication of certain functions Limited capacity Lack of fundraising 	<ul style="list-style-type: none"> Lack of tourism & leisure sector expertise Limited ability to raise on funding Possible issues on staff and asset transfer 	<ul style="list-style-type: none"> Lack of tourism & leisure sector expertise Lack of capacity Lack of fundraising ability 	<ul style="list-style-type: none"> Lack of tourism & leisure sector expertise Lack of fundraising ability 	<ul style="list-style-type: none"> Requires robust contract management by the municipality
Risk Transfer	<ul style="list-style-type: none"> No risk transfer 	<ul style="list-style-type: none"> No risk transfer 	<ul style="list-style-type: none"> Ultimate risk stays with the municipality via the municipal entity 	<ul style="list-style-type: none"> Some risk can be transferred but financial risk cannot 	<ul style="list-style-type: none"> Some risk can be transferred but financial risk cannot 	<ul style="list-style-type: none"> Significant technical, operational and financial risk can be transferred
Direct & Indirect Costs	<ul style="list-style-type: none"> Operating cost incorporated in municipal budget Financial losses borne by the municipality 	<ul style="list-style-type: none"> Operating cost incorporated in municipal budget Financial losses borne by the municipality 	<ul style="list-style-type: none"> Ultimate costs and financial losses incorporated in municipal budget via municipal entity 	<ul style="list-style-type: none"> Operating cost incorporated in other municipality's budget Financial losses borne by the other municipality 	<ul style="list-style-type: none"> Operating cost incorporated in organ of state's budget Financial losses borne by the organ of state 	<ul style="list-style-type: none"> Operating cost incorporated in private party's budget Financial losses borne by the private party
Financial Impacts	<ul style="list-style-type: none"> Capital & operating cost borne by the municipality 	<ul style="list-style-type: none"> Capital & operating cost borne by the municipality 	<ul style="list-style-type: none"> Capital & operating cost borne by the municipality via the municipal entity 	<ul style="list-style-type: none"> Capital & operating cost borne by the other municipality 	<ul style="list-style-type: none"> Capital & operating cost borne by the organ of state 	<ul style="list-style-type: none"> Capital & operating cost borne by the private party
Funding & Affordability	<ul style="list-style-type: none"> Lack of fund raising ability 	<ul style="list-style-type: none"> Lack of fundraising 	<ul style="list-style-type: none"> Limited ability to raise own funding 	<ul style="list-style-type: none"> Lack of fundraising ability 	<ul style="list-style-type: none"> Lack of fundraising ability 	<ul style="list-style-type: none"> Self fund raising ability

	Internal Mechanism		External Mechanism			
	Department or Administrative Unit	Municipal Business Unit	Municipal Entity	Another Municipality	Organ of State – Licensed Service Provider	Private Party
Resources & Organisational	<ul style="list-style-type: none"> Lack of tourism & leisure sector expertise Lack of in-house capacity Management of a resort is not a core function 	<ul style="list-style-type: none"> Lack of tourism & leisure sector expertise Possible duplication of certain functions Limited capacity 	<ul style="list-style-type: none"> Lack of tourism & leisure sector expertise Possible issues on staff and asset transfer 	<ul style="list-style-type: none"> Lack of tourism & leisure sector expertise Lack of capacity 	<ul style="list-style-type: none"> Lack of tourism & leisure sector expertise 	<ul style="list-style-type: none"> Specific resort management and tourism expertise
Qualitative Factors	<ul style="list-style-type: none"> Risk of continued non performance of resort 	<ul style="list-style-type: none"> Risk of continued non performance of resort 	<ul style="list-style-type: none"> Risk of continued non performance of resort 	<ul style="list-style-type: none"> Risk of continued non performance of resort 	<ul style="list-style-type: none"> Risk of continued non performance of resort 	<ul style="list-style-type: none"> Employment creation Skills development
BEE & other socio-economic aspects	<ul style="list-style-type: none"> No additional BEE achieved 	<ul style="list-style-type: none"> No additional BEE achieved 	<ul style="list-style-type: none"> No additional BEE achieved 	<ul style="list-style-type: none"> No additional BEE achieved 	<ul style="list-style-type: none"> No additional BEE achieved 	<ul style="list-style-type: none"> Could be required to meet BEE targets
Delivery arrangements	<ul style="list-style-type: none"> Not a core service function 	<ul style="list-style-type: none"> Not a core service function 	<ul style="list-style-type: none"> Not a core service function 	<ul style="list-style-type: none"> Not a core service function 	<ul style="list-style-type: none"> Not a core service function 	<ul style="list-style-type: none"> Conducted in accordance with best practice
Transitional management issues	<ul style="list-style-type: none"> No transitional Issues 	<ul style="list-style-type: none"> Limited transitional Issues 	<ul style="list-style-type: none"> Transition of staff would need to be managed 	<ul style="list-style-type: none"> Transition of staff would need to be managed 	<ul style="list-style-type: none"> Transition of staff would need to be managed 	<ul style="list-style-type: none"> Transition of staff would need to be managed
Legislation & regulations	<ul style="list-style-type: none"> Municipal procurement regulations apply 	<ul style="list-style-type: none"> Municipal procurement regulations apply 	<ul style="list-style-type: none"> Municipal procurement regulations apply 	<ul style="list-style-type: none"> Municipal procurement regulations apply 	<ul style="list-style-type: none"> Public Sector procurement regulations apply 	<ul style="list-style-type: none"> Subject to terms & conditions of PPP contract

	Internal Mechanism		External Mechanism			
	Department or Administrative Unit	Municipal Business Unit	Municipal Entity	Another Municipality	Organ of State – Licensed Service Provider	Private Party
Capability & Appetite	<ul style="list-style-type: none"> • Lack of tourism & leisure sector expertise • Lack of in-house capacity • Management of a resort is not a core function 	<ul style="list-style-type: none"> • Lack of tourism & leisure sector expertise • Possible duplication of certain functions • Limited capacity 	<ul style="list-style-type: none"> • Lack of tourism & leisure sector expertise • Possible issues on staff and asset transfer 	<ul style="list-style-type: none"> • Lack of tourism & leisure sector expertise • Lack of capacity 	<ul style="list-style-type: none"> • Lack of tourism & leisure sector expertise 	<ul style="list-style-type: none"> • Specific resort management and tourism expertise

The analysis above indicates the various elements that were considered in the recommendation of the preferred use of municipal property option. The analysis points to the PPP mechanism due to:

- The operation and management of a resort is not a core function of a municipality or an organ of state;
- The PMFA and MFMA that the municipality or organ of state operates under makes procurement services difficult for a resort operation which needs to procure goods and services on a timeous basis;
- A private sector entity could provide the expertise and experience required in order to return the resort to economic, environmental and financial sustainability.

Part 12: Value Assessment

12.1 Introduction

The value assessment enables the Witzenberg Municipality to determine the best procurement option choice for the Pine Forest Resort. The three tests prescribed by both the MFMA and MSA are:

- Is it affordable?
- Does it appropriately transfer risk from the municipality to the private party?
- Does it provide value for money?

The analysis below provides input to answering these questions.

12.2 Valuation

The Witzenberg Municipality has conducted a valuation of Erf 1002 & 1003 upon which the Pine Forest Resort is located. The valuation indicates that the property is valued at R20 272 000 (see **Annexure B**).

12.3 Business Model

The Municipal Service Delivery and PPP Guidelines Toolkit: Municipal PPPs for Private Sector Commercial use of Municipal Property requires that a business model be compiled to indicate:

- The best and worst case private party scenarios in terms of the total revenue to be generated by the private party's commercial activities on the municipal property over the term of the PPP agreement;
- The best and worst case municipality scenarios in terms of the total costs to be incurred by the municipality in procuring and managing the PPP over the term of the PPP agreement;
- A range of concession fee payments mechanism options to reflect total turnover and concession fees accruing to the municipality. These options should reflect the values of concession fees after the valuation of the entire property;
- The best and worst case BEE procurement scenarios.

A base case business model and financial analysis were developed for the Pine Forest Resort during the compilation of the Due Diligence Report. This base case business model is utilised in order to analyse the various required scenarios.

In regards to the best and worst case BEE procurement scenarios, the Witzenberg Municipality's preferential scoring will be utilised to adjudicate the tender to secure a private party operator for the Pine Forest Resort. The best case scenario would be to obtain a level 1 BEE contributor, with the worst case scenario being obtaining a level 7 BEE contributor.

12.4 Affordability

The Municipal Service Delivery and PPP Guidelines Toolkit: Municipal PPPs for Private Sector Commercial use of Municipal Property requires that in order to demonstrate affordability, the

viability of the concession model for both the municipality and private party should be determined.

As indicated in the Needs Analysis Report, the Witzenberg Municipality estimates that the Pine Forrest Resort will make a loss of R1.8 million in the 2011/12 financial year, R2.2 million in the 2012/13 financial year and R2.6 million in the 2013/14 financial year if it continues to be managed in the same way as it is currently managed.

In addition to the concession payment received, the Witzenberg Municipality will save R1.8 million in the 2011/12 financial year, R2.2 million in the 2012/13 financial year and R2.6 million in the 2013/14 financial year.

12.5 Value for Money Test

The Municipal Service Delivery and PPP Guidelines Toolkit: Municipal PPPs for Private Sector Commercial use of Municipal Property requires that benefits of the current use of the property be compared with the revenue and strategic benefits that can be expected from the proposed PPP project.

As demonstrated in the Needs Analysis Report, the Pine Forest Resort is expected to make a loss of R1.8 million in the 2011/12 financial year, R2.2 million in the 2012/13 financial year and R2.6 million in the 2013/14 financial year if it continues to be managed in the same way as it is currently managed.

In contract, the Pine Forest Resort is projected to achieve a net profit from the second year of operation, with a positive cashflow from the first year of operation.

The Municipal Service Delivery and PPP Guidelines Toolkit: Municipal PPPs for Private Sector Commercial use of Municipal Property also indicates that value for money is demonstrated by the extent to which the proposed PPP project will meet the municipality's strategic objectives for the use of the property.

The Needs Analysis Report clearly indicates that the proposed PPP project is aligned with the Witzenberg Municipality's strategic objectives and that the SDF for the Witzenberg Municipality of 2006 clearly identified the Pine Forest Resort for redevelopment and transfer to an entity that can manage it as a resort and tourism node.

The Needs Analysis Report also indicates that project objectives can be described as maximising the benefits that the Pine Forest Resort holds for the Witzenberg Municipality. This includes the upgrading, development and better management of the resort in order to generate additional revenue for the municipality.

These objectives can be realised with the appointment of a private party to manage the Pine Forest Resort.

12.6 Risk Matrix

Value for money also incorporates the transfer of risk and the risk matrix below identifies the relevant risks to the redevelopment and management of the Pine Forest Resort by a private party.

The allocation of the identified risks shows that there is appropriate transfer of risk from the municipality to the private party.

Table 12.13: Risk Matrix of the Re-Development of the Pine Forest Resort

Category	General Description	Mitigation	Risk	Allocation
Regulatory	<ul style="list-style-type: none"> The possibility that the various legislative consents and/or compliance with legislation from government authorities will not be obtained or, if obtained, are delayed or can only be implemented at a greater cost than originally projected. 	<ol style="list-style-type: none"> 1) Early and proper motivation of reasons for regulatory applications 2) Continued follow up with relevant authorities 	Low	Shared municipality & private party
Environmental Risk	<ul style="list-style-type: none"> Compliance with conservation management legislation Degradation of natural environment due to construction or operations 	<ol style="list-style-type: none"> 1) Manage visitor numbers to ensure conservation principles are adhered to 2) Implement environmental management plan (EMP) to effectively monitor possible environmental damage 	Low	Private party
Utilities	<ul style="list-style-type: none"> Municipality unable to supply electricity, water and waste disposal services to levels required Shortages in supply of electricity and water 	<ol style="list-style-type: none"> 1) Enter early discussions with utility companies to ensure adequacy of supplies 2) Back-up power generators 3) Rain water catchment tanks 4) Recycling of waste water 5) Ensure policies are in place to reduce water and electricity consumption 	Medium	Shared municipality & private party
Design	<ul style="list-style-type: none"> Design development, including adjustments to comply with regulatory compliance stipulations and operator requirements leads to increasing time and cost budgets 	<ol style="list-style-type: none"> 1) Early finalisation of the operator 2) Clear design brief and criteria 3) Finalisation of design pre upgrading so as to avoid costly changes to design during upgrading 	Low	Shared municipality & private party
Market, Demand or Volume Risk	<ul style="list-style-type: none"> Decline in the domestic tourism within and to the Western Cape Decline in the number of “self-catering based tourists” Quality of the experience less than expectations resulting in poor ‘word of mouth’ 	<ol style="list-style-type: none"> 1) Private party to ensure proper marketing strategies for the redeveloped Pine Forest Resort 	Medium	Private party
Completion Risks	<ul style="list-style-type: none"> Delays in planning and redevelopment periods 	<ol style="list-style-type: none"> 1) Appointment of experienced project management and professional team 2) Appointment of competent contractors with appropriate performance benefits and penalties 	Medium	Private party
Cost Overrun Risk	<ul style="list-style-type: none"> Budget overruns due to scope changes and/or delays 	<ol style="list-style-type: none"> 1) Appointment of experienced quantity surveyors and cost engineers 2) Strict criteria for scope management 	Medium	Private party
Exchange Rate Risk	<ul style="list-style-type: none"> Weakening of the Rand during upgrading period may increase the cost of imported materials for the project Strengthening of the Rand during operations may deter foreign tourist markets coming to SA, or reduce their period of time as guests 	<ol style="list-style-type: none"> 1) Forward purchase higher value imported materials 2) Alternative markets marketing campaigns 3) Selling of discounted bed-nights to tourism wholesalers and retailers for package tours 	Medium	Private party

Category	General Description	Mitigation	Risk	Allocation
Force Majeure Risk	<ul style="list-style-type: none"> Unforeseen acts that may result in delays and increased costs during upgrading and reduced visitor numbers during operations 	1) Adequate insurances during upgrading and operating periods for items of force majeure	Low	Private party
Inflation Risk	<ul style="list-style-type: none"> The possibility that the actual rate will be higher than projected 	<ol style="list-style-type: none"> During the upgrading period endeavour to minimise inflation clauses within the contracts During operations minimise forward sales beyond 12 months, or alternatively include an inflation clause within the sales agreements 	Medium	Private party
Insolvency Risk	<ul style="list-style-type: none"> In the event of the operating entity going insolvent 	<ol style="list-style-type: none"> Formation of a 'ring-fenced' legal entity for operations, separate from the fixed assets holding entity Limitations on debts and funding commitments of the operating entity 	Low	Shared municipality & private party
Interest Rate Risk	<ul style="list-style-type: none"> In the event of interest rates rising during the period of loan repayment 	<ol style="list-style-type: none"> Maximise portion of loan repayment at fixed interest rate Hedging Instruments 	Low	Private party
Latent Defect Risk	<ul style="list-style-type: none"> Period after upgrading that professional team and contractors remain responsible for maintaining and repairing latent defects 	<ol style="list-style-type: none"> Ensure that all professional team appointments include adequate professional indemnity cover, including period beyond completion of upgrading Ensure contractors have adequate contractors all-risks insurance and that adequate retentions are withheld post construction until all work has been signed-off by the professional team Beyond the period of 1 and 2 above, adequate insurances should be taken out to cover the fixed assets 	Low	Private party
Maintenance Risk	<ul style="list-style-type: none"> Ongoing maintenance after the construction maintenance period can prove costly to operational budgets 	<ol style="list-style-type: none"> Design and budgeting criteria to be set that ensures proper analysis of 'capital cost versus maintenance costs' of construction methods and materials, including furniture and fittings Penalty regime and performance monitoring Special insurance and special security in the form of final maintenance bonds 	Low	Private party
Operating Risk	<p>Any factors impacting on the operating requirements of the project, including:</p> <ul style="list-style-type: none"> Skilled staff could not be sourced from the local community pushing up salary costs Operating expenses exceeds budgets as a result of incompetent staff 	<ol style="list-style-type: none"> Due diligence of permanent staff members to be performed prior to appointment Monitoring of staff performance Right to terminate contracts for non-performance Skills development of the community to be undertaken to allow for permanent staff appointments from within the community 	Low	Private party
Political Risk	<ul style="list-style-type: none"> Political instability within the area of the project will deter visitor numbers Political will for the project must exist and without political interference in the project 	1) Early presentations and skills development of the local politicians as to the nature and advantages of the project	Low	Private party

Category	General Description	Mitigation	Risk	Allocation
Resource or Input Risk	<ul style="list-style-type: none">• The possibility of a shortage in the raw natural materials required for the construction phase• The possibility of a shortage in the inputs/resources required for the operation of the project	1)Ensure that sufficient supply contract with reliable suppliers are in place	Low	Private party

12.7 Service Delivery Mechanism

Based on the solutions option analysis and output specification as well as the value assessment, it is recommended that the Pine Forest Resort be operated and managed by a private party through a concession agreement with the Witzenberg Municipality.

The key reasons for this service delivery mechanism recommendation are:

- The Pine Forest Resort is currently being operated at a loss by the Witzenberg Municipality;
- The operation of a resort is not a core function of a municipality;
- The concessioning of the Pine Forest Resort will ensure that the Witzenberg Municipality not incur the losses of the Pine Forest Resort and in addition receive a concession payment;
- The private party could manage the Pine Forest Resort in order to achieve the municipality's strategic objectives namely, maximising the benefits that the Pine Forest Resort holds for the Witzenberg Municipality, including the upgrading, development and better management of the resort in order to generate additional revenue for the municipality; and
- Appropriate risk transfer will occur from the Witzenberg Municipality to the private party.