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Statement on the Financial Adjustment Company (FINSAC)

INTRODUCTION

FINSAC's primary objectives are to resolve the problems currently being faced by the financial sector. These objectives may be summarized as follows:

1. Address issues concerning liquidity and solvency of banking and insurance institutions.
2. Address the weakness in financial management that has been partly responsible for the difficulties in the sector.
3. Over the long term, improve the efficiency of the sector in mobilizing and allocating financial resources in the economy, and enhance the viability and profitability by restructuring the sector as well as conglomerates and firms within it.
4. Establish an incentive framework favouring better management and increased vigilance by shareholders.
5. Create a desirable environment for investors to re-capitalize the institutions while keeping to a minimum the public sector's role in capitalizing to a minimum of short duration.
6. Strengthen the supervision of the sector with specific focus on conglomerates.
7. Avoid and minimize the extent to which the public sector protection of depositors, policyholders and pension schemes is seen as relieving managers of the need for prudence and depositors of the responsibility for being selective in the placement of their funds.

FINSAC's Terms of Reference

In pursuit of these objectives, the Government of Jamaica has established the Financial Sector Adjustment Company (FINSAC) with the following terms of reference:

1. FINSAC serves as the vehicle through which realignment and restructuring of the financial sector will take place.
2. FINSAC serves as the executive arm of the Ministry of Finance and Planning in which Government strategy will be planned and through which the interventions of various agencies (specifically the Bank of Jamaica (BOJ) and the Superintendent of Insurance) will be coordinated.
3. Through FINSAC, the Government will provide financial assistance to the sector and therefore will have the responsibility

of the accountability for the spending of such resources provided to it directly or guaranteed by the Government.

4. Through FINSAC, the Government will provide guidance and technical assistance to the financial sector. It may mobilize and deploy external technical and managerial support for the restructuring of intervened institutions.
5. FINSAC will sponsor and/or undertake diagnostic studies of the overall health of the financial sector with specific focus on the institutions which require assistance.
6. FINSAC will assist institutions in developing work-out plans, where necessary, to return them to viability. Such plans will form the basis for the conditions which FINSAC will attach to financial assistance. FINSAC will monitor the implementation of such plans on a continuing basis and will evaluate their effectiveness in achieving their specified objectives. It will inform and coordinate the inputs of Government's members of boards of intervened institutions on issues considered essential to the viability of the financial sector.
7. Based on the experience gained in its work, FINSAC will advise the Government on the prudential regulation of the sector and on the renewal, suspension and revocation of operating charters of individual institutions within the sector.

Financing of FINSAC

Basically, FINSAC is being financed by the Government through borrowing in the domestic market. Funds are being raised through the sale of long-term Registered Stock, with coupon rate tied to the rate on Treasury Bills. The stocks are being placed in small amounts as FINSAC requirements are not at all up-front and the total cannot be known with certainty at the outset. This approach has the merit of avoiding the shock of a large placement on the market at one time. So far, J\$1.5 billion has been raised and transferred to the account of FINSAC in the Bank of Jamaica.

While this is the approach to the long-term financing, it is necessary for FINSAC to have substantial interim financing, specifically for the purpose of reversing the overdraft positions of certain banks in the Bank of Jamaica. This is being provided through a Government guaranteed loan from BOJ to FINSAC out of certain sterilized Government deposits in BOJ.

Financing of FINSAC's housekeeping budget so far has been by advances provided by the Agricultural Credit Bank (ACB). Of the \$56 million provided by the Ministry of Finance so far, the ACB has reimbursed \$36 million (covering advances for about four months before FINSAC until the end of March 1997); approximately \$20 million remains unspent. In the future, FINSAC's budget will be financed out of the margin between its borrowing and lending.

Exit Strategy for FINSAC

FINSAC is expected to have a life of about seven (7) years. Support is provided to solvent companies on the basis of rehabilitation plans to be implemented in five years. FINSAC expects to be fully repaid by the end of the fifth (5th) year, assuming successful work-outs of the existing

problems. Interventions leading to the temporary acquisition of institutions will be short-lived. All the necessary interventions are likely to take place within the first year of FINSAC's existence. Components which can be restored to viability will be rehabilitated and returned to private ownership within a year, while other components will be liquidated or sold for merger with other institutions as soon as possible.

Given the experience of other countries, liquidations and the sale of assets as well as the collection of debts can often be a lengthy process. The usual approach has been to set up facilities for handling these aspects outside of the vehicle for rehabilitation. For example, real estate investment trusts have been used as a holding arrangement for the management and disposal of real estate; paper assets have been put in unit trusts and the units marketed; and non-performing loans have been sold to a central debt-collection agency. FINSAC will evaluate the option of setting up a real estate investment trust and other asset disposal approaches. This can be with the assistance of the Urban Development Corporation (UDC). These liquidation arrangements are likely to outlive FINSAC.

After the initial period of interventions and assistance activities, the role of FINSAC will be narrowed to primarily supervision and monitoring of work-out plans of institutions that have been financially assisted by FINSAC and the management of the investment' portfolio arising out of assistance activities. Supervision and monitoring should end in six (6) years as the work-out plans are completed. Interventions are unlikely to give rise to such a portfolio since intervened institutions will be rehabilitated and resold and the proceeds used to retire portions of FINSAC's debt to Government. By year seven (7), FINSAC's only responsibility is expected to be the collection of repayments from assisted institutions.

**Excerpt from the Budget Presentation by
the Minister of Finance and Planning
27 March 1997**

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