AUDITOR GENERAL'S DEPARTMENT
PERFORMANCE AUDIT REPORT

DEVELOPMENT BANK OF JAMAICA LIMITED (DBJ)

The Auditor General is appointed by the Governor General and is required by the Constitution, Financial Administration and Audit Act, other sundry acts and letters of engagement, to conduct audits at least once per year of the accounts, financial transactions, operations and financial statements of central government ministries and departments, local government agencies, statutory bodies and government companies.

The Department is headed by the Auditor General, Pamela Monroe Ellis, who submits her reports to the Speaker of the House of Representatives in accordance with Section 122 of the Constitution of Jamaica and Section 29 of the Financial and Administration and Audit Act.

This report was prepared by the Auditor General's Department of Jamaica for presentation to the House of Representatives.

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Vision

Our vision is aimed at promoting a better country through effective audit scrutiny of Government operations.

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QUOTED:-

December 8, 2015

The Honourable Speaker
House of Representatives
Gordon House
81 Duke Street
Kingston
Jamaica

Dear Sir,

In accordance with the provision of Section 29 of the Financial Administration and Audit (FAA) Act, I have the honour to submit my report on the findings and recommendations of the Performance Audit on the Development Bank of Jamaica (DBJ) for tabling in the House of Representatives.

Yours faithfully,

Pamela Monroe Ellis (Mrs.)
Auditor General

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Summary

The Development Bank of Jamaica (DBJ) is a self-financing entity, which obtains loans from local and international multinational organizations for on-lending to finance investment projects. DBJ was created to foster economic growth and development of strategic sectors of the Jamaican economy. The Bank's aim is to facilitate the growth and development of all viable enterprises in the productive sectors, which include agriculture and agro-processing, manufacturing, information technology, mining and quarrying, energy, services and tourism. Within the last six years, 2009-10 to 2014-15, DBJ disbursed JMD$17.96 billion and US$79 million in loans to finance investments projects.

The performance audit was conducted to determine if DBJ is fulfilling its mandate to foster economic growth and development in the Jamaican economy. The Key findings are outlined in paragraphs 1 to 4.

Key Findings

1. **DBJ placed emphasis on providing financing through financial institutions to small and medium-sized enterprises (SMEs) and direct loan financing in order to stimulate production and employment creation. Since inception in April 2000, DBJ has not assessed the extent to which it is achieving its intended outcome of facilitating economic development.** DBJ determined economic benefit through its review and assessment of each loan application to evaluate the proposed project's ability to create jobs, generate foreign exchange, stimulate foreign investments and utilize local produce. However, in the absence of robust post evaluation of the economic performance of the projects, we were challenged to determine whether DBJ is truly fulfilling its mandate and the extent to which the country is benefitting economically from loans granted by DBJ, which amounted to $17.96 billion over the period 2009-10 to 2014-15. DBJ's Annual Reports covering the 6 year period 2009-10 to 2014-15 indicated that, on aggregate, 20,134 potential jobs would have been created from loans disbursed **(Table 2)**. However, except for actual the job creation data for the ICT/BPO[1] sector, which revealed that only 19 per cent of the targeted job creation for this sector had been achieved to date **(Table 3)**, DBJ has not assessed the economic impact, including actual number of jobs created from loans disbursed to finance development projects.

2. DBJ's attempt to measure the impact of its loans by the engagement of a consultant in February 2015, did not obtain the anticipated value as the consultancy agreement was modified to exclude the impact assessment deliverable. It is our view that this crucial exercise should be built into DBJ's governance and business process and not be relegated to a one-off activity. The outcome of post evaluations can also assist the DBJ to refine and strengthen its pre-evaluation process but more importantly, it will

[1] Information Communication Technology/Business Process Outsourcing (ICT/BPO)

provide critical information to determine successful strategies or lack thereof and allow for early intervention.

3. **DBJ also provides financing to SMEs through various financial institutions. However, DBJ did not monitor the financial institutions to satisfy itself that the loans disbursed met the stipulated criteria. We noted that DBJ was required to monitor these institutions based on the signed general agreements with AFI's[2]; DBJ did not enforce this requirement.** In August 2015, DBJ amended the Letter of Commitment and Disbursement Letter to include the requirement for AFIs to provide evidence of disbursement within 30 days and has expanded the loan progress report to track receipt of the submissions. For example, over the six year period (2009-10 to 2014-15), DBJ provided $2.42 billion in loans to a Cooperative for on-lending to finance projects in the agricultural sector. However, DBJ did not monitor the Cooperative's loan disbursement to ensure that the loans provided to the Cooperative were only on-lent to borrowers for agricultural activities. In November 2015, DBJ noted that post disbursement monitoring would be included in a monitoring and evaluation framework that will be developed in the first quarter of the 2016 calendar year.

4. As at March 2015, DBJ's loan stock represented 68 per of its total assets. Loan interest was the largest contributor to total income, representing 43 per cent. The composition of DBJ's assets and level of income indicates that its financial resources are aligned to its mandate of providing loan financing. However, DBJ's non-performing loans (NPL) grew from $1.1 billion as at March 2010 to $2.5 billion as at March 2012 **(Figure 2)**. The NPL subsequently declined to $897.8 million as at March 2015, mainly due to write-offs, instead of recovery of outstanding loans, which suggests that DBJ may have difficulty recovering non- performing loan amounts from delinquent borrowers.

Recommendation

DBJ should develop a monitoring strategy to periodically assess the impact of its loan disbursements on economic growth and development in Jamaica. The strategy should include a follow-up mechanism to determine the extent to which the proposed economic benefits of the projects were actually realized. DBJ should also ensure that AFIs, MFIs[3] and the Cooperative are properly monitored to provide greater assurance that loans provided to these institutions are on-lent to borrowers in the respective sectors of the economy for the interned purpose.

[2] Approved Financial Institutions

[3] Micro-Financing Institutions

Part One

Introduction

Why was DBJ created?

1.1 The Development Bank of Jamaica Limited is registered under the Company's Act of Jamaica and is wholly owned by the Government of Jamaica. It was created in April 2000, from the merger of the Agricultural Credit Bank of Jamaica Limited and the National Development Bank of Jamaica Limited. The operations, assets and liabilities of the National Investment Bank of Jamaica (NIBJ) were later amalgamated with the DBJ on September 1, 2006.

DBJ's Mandate

1.2 DBJ was created to foster economic growth and development of strategic sectors of the Jamaican economy. The Bank's aim is to facilitate the growth and development of all viable enterprises in the productive sectors, which include agriculture and agro-processing, manufacturing, information technology, mining and quarrying, energy, services and tourism.

DBJ seeks to fulfil its mandate by providing financial capital to viable investments projects through:

1. Alliances with Approved Financial Institutions (AFI) and other financiers Medium and long-term financing solutions to small and medium-sized enterprises,
2. Direct lending for large projects in strategic areas.
3. Management and privatization of national assets and investments
4. Facilitating capacity development to address demand side issues relating to access to financing.

How is DBJ funded?

1.3 DBJ sources loan funding from local sources such as the Capital Development Fund (CDF), National Insurance Fund (NIF), PetroCaribe and various international financial institutions such as the Caribbean Development Bank, Inter-American Development Bank (IDB), China Development Bank, European Investment Bank and the World Bank (through the MoF&P). DBJ on-lends funding received from these institutions. The Bank also generates income through re-flows from loan repayments.

The audit scope and methodology

1.4 The performance audit was conducted to assess DBJ's loan disbursement activities to determine the extent to which DBJ is contributing to Jamaica's economic growth and development. Our audit was planned and conducted in accordance with the Government Auditing Standards, which are applicable to Performance Audit and issued by the International Organization of Supreme Audit Institutions (INTOSAI). Our assessment is based on the review of internal and external documents, interviews with senior management and staff, observations and analysis of information provided by DBJ.

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Part Two

Monitoring Arrangements

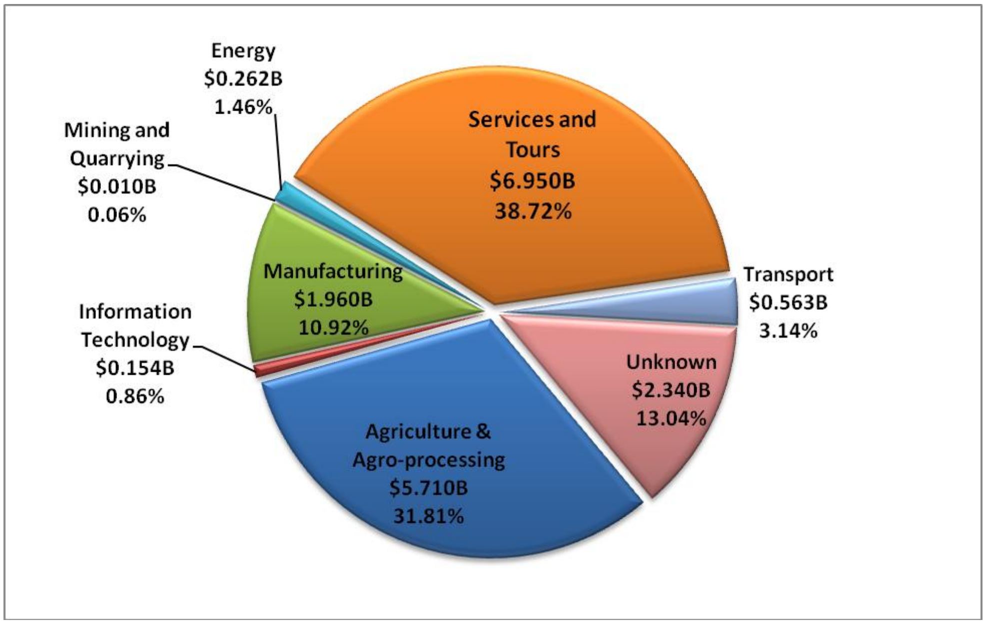
2.1 Vision 2030 National Development Plan has recognised that that the capabilities of micro, small and medium sized enterprises (MSMEs) should be developed to assist in achieving the national outcome of an enabling business environment in Jamaica. To attain this objective, DBJ is charged with expanding credit facilities for MSMEs in order to foster economic growth and development in the Jamaican economy. DBJ's strategic goal is to provide funding for development projects to the productive sectors, at affordable interest rates. These sectors include agriculture, agro-processing, manufacturing, information technology, mining and quarrying, energy, services and tourism. In seeking to achieve this strategic goal, DBJ sourced funding directly from local[4] and international financial institutions under specific line of credit facilities. DBJ also received funding from the Government of Jamaica (GOJ) through the Ministry of Finance and the Public Service (MoF&P) to provide financing for specific projects that would spur economic growth and development. DBJ on-lends these funds to existing and start-up businesses in the respective sectors to finance development projects. Financing for large development projects are provided through DBJ's direct loan facility; while, financing to small and medium-sized enterprises (SMEs) are provided mainly through Approved Financial Institutions (AFIs) and Micro-Financing Institutions (MFIs). AFIs include commercial merchant banks and cooperative enterprise; while MFIs include credit unions and small micro-financing institutions.

2.2 DBJ requires that borrowers demonstrate that proposed projects would be able create a net economic benefit to the country, through any combination of the general development criteria outlined in DBJ's loan policy. These general criteria include the project's ability to create jobs, generate foreign exchange, stimulate foreign investments and utilize local produce. This is to ensure that loan financing is provided to projects that will stimulate economic development. DBJ assesses each loan application to ensure that the projects meet the general criteria, as well as to determine the project's financial viability and its ability to repay the loan.

2.3 **Figure 1** shows that over the last six years, 2009-10 to 2014-15, DBJ disbursed $17.96 billion in loans. Of this amount, $6.95 billion (38.7 per cent) was provided to businesses in the service sector and $5.71 billion (31.8 per cent) to the agricultural sector. The manufacturing sector accounted for $1.96 billion (10.9 per cent); while, $2.34 billion (13 per cent) was not linked to any specific sector. The remaining $0.99 billion (5.6 per cent) was provided to finance development projects in the information technology, mining and quarrying, energy and transport sectors.

[4] National Investment Fund (NIF) and Petro Caribe.

Figure 1 Loans disbursed to targeted sectors April 2009 to March 2015



Source: AuGD compilation of Information provided by DBJ

2.4 Realizing that small and medium-sized enterprises (SMEs) are the main drivers of economic growth, DBJ placed emphasis on providing financing to these enterprises in order to stimulate production and employment creation. Of the $17.96 billion disbursed in loans, between 2009-10 and 2014-15, DBJ provided $10.9 billion (61 per cent) to SMEs through AFIs, $2.84 billion (16 per cent) through MFIs and $2.42 billion (13 per cent) was provided to the agricultural sector through a cooperative enterprise. The disbursements to SMEs through AFIs, MFIs and a Cooperative represented a combined total of $16 billion (90 per cent) of the total loan disbursements **(Table 1)**.

Table 1 Loans disbursed between 2009-10 and 2014-15

Loan Type	%	Total $'000	2014-15 $'000	2013-14 $'000	2012-13 $'000	2011-12 $'000	2010-11 $'000	2009-10 $'000
AFI	*61%*	*10,910,393*	*2,730,570*	*3,062,485*	*1,324,651*	*1,350,896*	*648,769*	*1,793,022*
MFI	16%	2,842,598	860,379	570,863	574,896	491,483	168,130	176,847
Cooperative	13%	2,424,710	220,388	478,138	443,418	419,512	345,273	517,981
Total	**90%**	**16,177,701**	**3,811,337**	**4,111,486**	**2,342,965**	**2,261,891**	**1,162,172**	**2,487,850**
Direct	10%	1,786,096	159,282	521,016	45,105	216,553	404,211	439,929
Total	**100%**	**17,963,797**	**3,970,619**	**4,632,502**	**2,388,070**	**2,478,444**	**1,566,383**	**2,927,779**

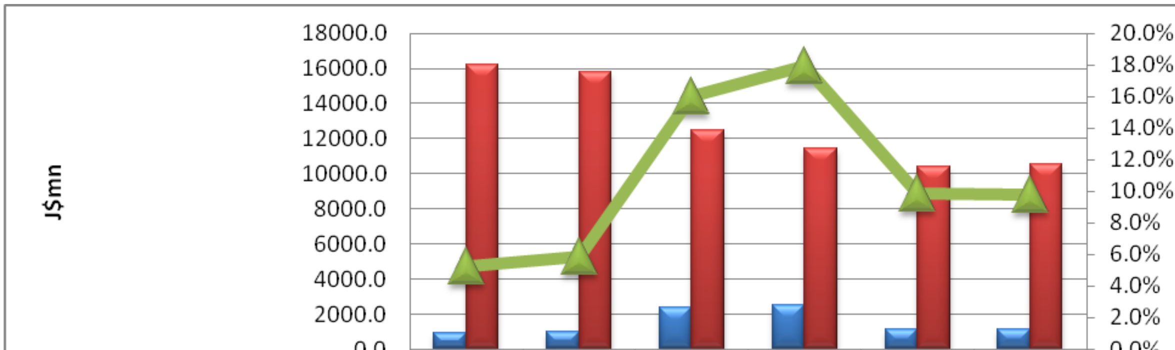
Source: AuGD compilation of Information provided by DBJ

2.5 DBJ also provided US$79 million in loans to the targeted sectors over the period. AFI's received US23.95 million and direct lending of US$55.52 million. While this level of loan disbursement to SMEs demonstrates DBJ's continued focus on driving economic development through SMEs, DBJ was not effectively monitoring these institutions to satisfy itself that the loans disbursed by the financial institutions met the stipulated criteria.

2.6 There was no requirement for the AFI, MFI and DBJ to monitor the implementation of the project to ensure that funds are used for the intended purpose and to ensure ongoing monitoring of projects to ensure sustainability. As a result, we found that DBJ did not satisfy itself that the projects undertaken met the desired outcome to increase economic growth. DBJ could have benefitted from a post disbursement monitoring of the projects to determine their outcome and identify lessons learnt to better inform their pre-assessment procedures.

2.7 As at March 2015, DBJ's loan stock represented 68 per of its total assets. Loan interest was the largest contributor to total income, representing 43 per cent. The composition of DBJ's assets and level of income indicates that its financial resources are aligned to its mandate of providing loan financing. However, DBJ's non-performing loans (NPL) grew from $1.1 billion as at March 2010 to $2.5 billion as at March 2012 **(Figure 2)**. The NPL subsequently declined to $897.8 million as at March 2015, mainly due to write-offs, instead of recovery of outstanding loans, which suggests that DBJ may have difficulty recovering non- performing loan amounts from delinquent borrowers.

Figure 2 Six-year analysis of non-performing loans



	2014/15	2013/14	2012/13	2011/12	2010/11	2009/10
Non-Performing Loans	897.8	977.8	2374.6	2499.4	1133.6	1145.3
Performing Loans	16186.3	15789.3	12459.0	11460.0	10400.6	10539.2
Percentage of Loan Portfolio (RHS)	5.3%	5.8%	16.0%	17.9%	9.8%	9.8%

Source: AuGD analysis of data provided by DBJ

Approved Financial Institutions (AFIs)

2.8 DBJ signed a general agreement with AFIs and MFIs to allow these institutions to apply to DBJ for funds for on-lending to customers. We observed that AFIs processed and approved customers' loan applications and submitted the applications to DBJ for final approval and fund disbursements. The general agreements specified that AFIs should disburse all funds received from DBJ within 30 days and provide DBJ with evidence of such disbursements to the respective customer. However, DBJ did not ensure that AFIs complied with this requirement.

2.9 We reviewed 46 loans totalling $2.7 billion approved by DBJ to determine whether the AFIs disbursed the approved amounts to the respective customers. However, we were unable to determine how DBJ satisfied itself that the funds were in fact on-lent to the customers as the required reports were not submitted by the AFI's. DBJ responded that while the agreement specified this requirement, it was not included in the Letter of Commitment signed with the AFIs; and as such, the AFIs were not aware of the requirement.

2.10 In August 2015, DBJ amended the Letter of Commitment and the Disbursement Letter to include the requirement for AFIs to provide evidence of disbursement within 30 days and has expanded the loan progress report to track receipt of the submissions.

2.11 We also observed that DBJ disbursed funds to MFIs on the basis of obtaining a schedule of customers for whom loans were approved by the MFIs. However, DBJ did not include in the MFI's general agreement, a similar requirement for the MFIs to provide evidence of funds disbursement to the respective customer. We found that DBJ made contacts with 323 (or 6.7 per cent) of the 4,764 applicants with loan amounts totalling $405.2 million who obtained loans through MFIs to confirm that they were in receipt of the loan proceeds.

DBJ not assessing the impact of loans on job creation

2.12 DBJ placed emphasis on providing financing through financial institutions to small and medium-sized enterprises (SMEs) and direct loan financing in order to stimulate production and employment creation. Since inception in April 2000, DBJ has not assessed the extent to which it is achieving its intended outcome of facilitating economic development. DBJ determines economic benefit through its review and assessment of each loan application to evaluate the proposed projects' ability to create jobs, generate foreign exchange, stimulate foreign investments and utilize local produce. However, in the absence of robust post evaluation of the economic performance of the projects we are challenged to determine whether DBJ is truly fulfilling its mandate and the extent to which the country is benefitting economically from loans granted by DBJ.

2.13 One of the major targets outlined in DBJ's three-year Corporate Plan and Budget 2012-13 to 2014-15 is to facilitate job creation, through loans disbursed for investment projects. Although DBJ recognized that job creation is a key benchmark for measuring economic growth, DBJ did not make it a priority to assess the actual number of jobs created from loans disbursed to finance investment projects.

2.14 Each year, DBJ reported in its Annual Report the number of jobs proposed to be created across various sectors as a result of loans disbursed to finance development projects. As shown in **Table 2**, between 2009-10 and 2014-15, DBJ reported that 20,134 potential jobs would be created. However, except for the ICT/BPO[5] sector, DBJ did not conduct an assessment to verify the full extent to which the 20,134 jobs were actually realized to determine its contribution to job creation in the Jamaican economy.

[5] Information Communication Technology/Business Process Outsourcing (ICT/BPO)

Table 2 Potential jobs from new investments 2009-2015

Sectors	2014-15	2013-14	2012-13	2011-12	2010-11	2009-10
Agriculture	82	263	737	1,829	96	859
Agro-processing	120	0	32		63	0
Manufacturing	190	143	15	23	57	84
Mining & Quarry	0	14	0	2	0	6
Service & Transport	465	3,876	154	229	481	39
ICT/BPO	2,518	0	6,185	0	0	0
Tourism	264	140	148	16	154	139
Govt. Entities	0	0	0	0	11	660
Govt. Programme	0	0	0	0	0	22
MFI	0	0	0	0	0	18
Total	**3,639**	**4,436**	**7,271**	**2,099**	**862**	**1,827**

* A total of **20,134** jobs were proposed to be created between 2009-10 and 2014-15.

Source: DBJ's Annual Reports 2009-10 to 2014-15

2.15 DBJ disbursed US$21.8 million, between October 2014 and June 2015, to development projects in the ICT/BPO sector, which proposed to create approximately 10,324 jobs. However, a post assessment review conducted by DBJ revealed that, as at June 2015, 1,950 (19 per cent) were actually realized **(Table 3)**. DBJ reported that *"of the eight projects listed, only three were completed and could accommodate BPO employees, while the others were either still in the construction phase or had been recently approved and not yet started construction."*

Table 3 DBJ job creation data for ICT/BPO Sector as at June 30, 2015

Company/ Project	Amount Disbursed $	Date of Last Disbursement	Projected No. of Employees	Actual No. of Employees
Company 1	5,793,503.00	11-Dec-14	1,344	850
Company 2	471,650.80	6-May-15	0	-
Company 3	1,091,209.22	23-Jun-15	1,500	-
Company 4	3,644,488.00	30-Mar-15	2,000	-
Company 5	1,655,014.36	5-Jun-15	0	-
Company 6	3,644,092.00	21-Oct-14	1,000	-
Company 7	2,874,788.00	28-May-15	1,480	-
Company 8	2,649,188.00	01-Mar-13	3,000	1,100
TOTAL	**21,823,933.38**		**10,324**	**1,950**

Source: Data provided by DBJ

2.16 On October 3, 2014, DBJ's management approved the engagement of a consultant to determine the impact of its loan and capacity building programmes on job creation. The assessment was to be undertaken over a five-month period ending May 2015. The specific objectives were to conduct an audit of gross direct jobs created through DBJ's financing and an economic impact survey of DBJ's loans and grant recipients to determine the impact of DBJ loans and capacity development intervention on SMEs. The Consultant was expected to produce, among other things, an inception and a final report highlighting the research findings. The details of the deliverables and timelines are outlined in **Table 4**, which shows that only the inception report was completed before the contract period ended.

2.17 We noted from a Memorandum dated April 24, 2015, that there were challenges with the deliverables, which include incomplete capturing of information, delayed response in providing updates, missing deadlines and incomplete data quality checks. The Consultant was paid a deposit of $3,487,500 in March 2015, representing 50 per cent of the Contract Price. The Consultant reported that almost 47 per cent of the 220 respondents reported 465 new jobs were created after obtaining funding from DBJ. In April 2015, DBJ re-scoped the consultancy agreement to exclude the impact assessment owing to challenges such as obtaining relevant data and locating borrowers. Consequently, DBJ terminated the consultancy agreement on June 26, 2015. Further, DBJ was unable to indicate whether value for money was received for the deposit paid, as the requisite site visits to the companies, verification of jobs and the overall impact on firms visited were not presented.

Table 4 DBJ's impact assessment consultancy deliverables

Deadline	Deliverables	Status
February 9, 2015	• Deliverable 1 - Inception Report	• Completed (Report dated February 6, 2015)
February 13, 2015	• Report on Deliverable 2 – Updated Ma-ster-list of approvals. • Microsoft Excel File with updated information	• Not completed • Completed July 2015
March 6, 2015	• Report on the number of establishment visited by geographic region and details on the name of MSME and large companies visited, date of visit and name of researcher. • Report on highlights of deliverable 3 (Verification of jobs)	• Not completed • Completed August 2015
March 6-13, 2015	• Submission of Deliverable 3-Final Report and PowerPoint Presentation to the Senior Management and Board of Directors.	• Draft completed
April 6, 2015	• Report on highlights of Deliverable 4 (DBJ's impact on firms). • Submission of Final Report Deliverable 4 and PowerPoint Presentation to the Senior Management and Board of Directors.	• Not completed • Not completed

Source: Consultancy Contract