

November 28, 2023

**Directorate for Financial Markets**

**Re:** Comments on change to the interest rate cap to 20%

To whom it may concern,

In connection with the announcement of the decrease in the interest rate cap from 21% to 20% using the effective interest rate methodology, please accept this communication as our perspective of the effects of this new decree on Island Finance Bonaire N.V.'s (hence "IFB" or "Island Finance") business operations.

As you know, IFB is a consumer finance company dedicated to the granting of unsecured consumer loans in the Bonaire market. Primarily, IFB serves the low to middle income population segment who generally do not have access to credit through traditional lenders such as banks.

IFB often serves as a "bridge" to consumers by offering them initial access to credit and allowing them to establish credit history to later graduate to bank loans. In fact, this year to date, more than 160 customers have already paid off their IFB loan using funds received from that of a competitor. This represents a business loss of more than \$300,000 USD. As such, IFB is a promoter of financial inclusion, a key enabler to reducing poverty and boosting prosperity, as established by the World Bank.

**Lending and the creation of a social gap and dangers**

Island Finance fulfills a social role by providing credit to individuals who may not initially qualify for financing with local banks because they are considered higher risk. Said customers do not provide collateral to guarantee loans. Island Finance, on the other hand, is willing to accept this risk, which is normally offset by our pricing structure.

In addition, there is the risk that a major social gap might be created and/or exacerbated by the unavailability of funding to people who are not capable of complying with established bank requirements. This restriction of credit creates a more robust, informal market for lenders. These individuals take advantage of the needs of this population for short-term financing and charge exorbitant amounts of interest on very short-term loans (usually not more than one month in term). Moreover, these entities or persons do not comply with reporting regulations, thus impairing the financial sector of the island.

Regulated financing to this socioeconomic population level in Bonaire is primarily used to address basic needs such as the acquisition of major household appliances, resolving medical bills or auto-repairs. Those who earn enough to qualify are able to easily obtain financing from banks. However, a significant portion of Bonaire's population does not qualify for bank loans without collateral. Island Finance plays an important role in the market by providing credit to individuals who, generally speaking, would not qualify for financing at local banks because they do not possess or cannot offer collateral. These individuals are, in general, considered of higher financial risk. Currently, Island Finance is willing to accept this risk and fulfill the needs of the market and society.

Another important factor that must be taken into consideration is the lack of overdraft facilities available to the general public. A similar situation occurs with regard to the use of credit cards. The inability to access short-term financing options such as revolving credit can place the population in a precarious situation. Proscribing access to financing options may force a significant portion of the population of Bonaire to resort

to informal or unregulated sources of credit, such as loan sharks, which could have other social consequences.

At Island Finance, we strongly believe in our business model and the way in which we evaluate the creditworthiness of our clients. This can be seen by the fact that we have served the island for more than 35 years. An important factor with respect to the higher risk level of the credit provided by Island Finance is the fact that we are lending to borrowers who may not have a current account relationship. Local banks use the current account relationship to offset some of the counterparty risk. Our business model is predicated on a risk-based approach well-founded on the credit profiles and payment behavior of our customers. When granting credit to its customers, IFB's credit analysis focuses on customer's ability to repay, payment history, and payment flexibility and elasticity (apart from complying with the current Credit Worthiness Test).

Our loan product is predicated on the use of simple, non-compounding interest bearing methodology. We feel our customers benefit from this non-compounding interest methodology as the result is a less expensive loan. Please recall we lend under the following conditions:

- No administrative or borrowing fees.
- No late fees.
- No pre-payment penalties.
- Non compounding interest calculation method.

### **Cost of funds**

As you know, 'credit institutions' such as Island Finance have different business models and funding structures than those of banks. We are primarily funded through market debt, credit lines and equity and do not accept deposits. Thus, the cost of our cost of funds is significantly higher than banks and other financial institutions as we do not use deposits as a source of funding. Loans provided by Island Finance Bonaire are unsecured which means that in case of default, the company does not have collateral on which they can utilize to recover the money disbursed to customers.

The revenues of Island Finance Bonaire compared to local banks vary significantly. Local banks have a significant source of secondary income by means of commissions, trading and investment income. Based on the limitations of Island Finance Bonaire being able to attract funds, the company must resort to other funding alternatives in order to provide financing, particularly to a sector in the community in which regular bank financing is virtually not possible.

The fact that Island Finance customers have a higher risk profile and the company's more expensive funding structure, mandates the company to charge higher interest rates. Island Finance's position is that a further interest rate cap such as this one discriminates against entities that have alternative funding structures such as ours.

In IFB's market space of lower incomes, customers are more likely to default in meeting loan repayment schedules. Delinquencies arise from job losses, unforeseen events such as illness and from the reality that customers have little or no savings on which to draw. Delinquencies represent both loss of income to the institution and imply cost of recoveries. Intense collection efforts correlate to higher operational costs IFB invests heavily in loan collections. Delinquent customers are systematically pursued with success.

### **Pricing of loans in this business**

As is to be expected pricing in this business will be very challenging as it depends on the cost of funds, the various type of risks that loan rates must cover and administrative costs. Pricing must take into consideration cost of funds, operational costs, risk assessment of customers and their ability to repay, and loan loss provisioning (reserves) of our loans to comply with regulatory requirements and mitigated loss risk.

If this cap is further reduced, we are considering stopping loan originations. Additionally, we must commence a process of terminating valued, long tenured employees who have families to support due to insufficient business volume caused by rate caps. The Act and Decree as construed in relation to lending has negatively affected the operations of the company, and ultimately its continuity.

### **Conclusion**

Island Finance has been performing a social function in the local community by providing legal / regulated credit facilities to a portion of the local population for more than 35 years. The experience Island Finance has gained during the course of the years has allowed us to develop a credit policy that mitigates our exposure and protects clients from over-extension of credit. As an entity embedded in the market, we have acquired the necessary skills to evaluate the creditworthiness of the people living in Bonaire. As a socially responsible company, we truly understand the implications the new regulations could have for the population and economy of Bonaire.

We have taken several efficiency measures in our business over the last several years, having ultimately reached the limit of business viability and profitability. A further decrease in the interest rate cap will inevitably impair the business and our ability to remain an alternative source of credit for consumers in the Bonaire market.

Ultimately, continuing to restrict the market via regulations, particularly, the interest rate cap and the effect of the current inflation rate and global interest rate environment may cause the exiting of credit providers from the market causing a lack of availability of regulated credit products and competition. Inflation, as discussed in our prior letter, is also negatively impacting the consumers and IFB operations. Even with the subsidy on fixed usage tariff for electricity implemented in November 2022, prices continue to increase for food and other consumer inelastic products.

Island Finance Bonaire would support a reasonable cap on interest rates in order to avoid the abuses of short-term lenders. However, the current Credit Worthiness Test and unreasonable interest rate caps have adversely impacted both legitimate, responsible, lenders, such as us, who have served the Bonaire community for decades and the denial of access to credit to the neediest.

We would welcome the possibility to discuss in detail all the earlier-mentioned explanations. We are currently commissioning an economic study that we will share during the month of December 2023.

Regards,

A handwritten signature in black ink, appearing to read "Joel M. Eliza Rivera".

Joel M. Eliza Rivera  
Legal Counsel  
Island Finance Bonaire N.V.