

EXECUTIVE COUNCIL

PUBLIC

Title: FIMCo Guarantee

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Responsible Director: Managing Director, FIDC

Report Author: Managing Director, FIDC

Portfolio Holder: MLA Mark Pollard

Reason for paper: This paper is submitted to Executive Council:

To meet a statutory requirement.¹

Publication: No - due to commercial sensitivities, as highlighted in grey. However, if it is deemed that it should be made published then the redactions should be implemented.

Under Executive Council Standing Order 23(2), Executive Council must have regard to the categories of exempt information in Schedule 3 to the Committees (Public Access) Ordinance when determining if information should be withheld. The categories which are potentially relevant to this paper are:

Clause 9 - Information about others' financial and business affairs.

Previous papers: 07/16 – FIMCo Guarantee
23/17 – FIMCo Guarantee

List of Documents: Appendix A: REDACTED
Appendix B REDACTED

¹ In order to provide the necessary context to facilitate informed decision-making, this report draws heavily on papers previously prepared for Executive Council and in particular 07/16 – FIMCo Guarantee 23/17 – FIMCo Guarantee

1. Recommendations

Honourable Members are recommended to:

- a) Approve the Falkland Islands Development Corporation providing a guarantee to Standard Chartered Bank for FIMCo's overdraft facility, at a reduced level of **REDACTED** for a period of 12 months from 1st April 2018 – 31st March 2019;
- b) Approve a request be forwarded to the Secretary of State for Foreign and Commonwealth Affairs to consent to the Falkland Islands Development Corporation continuing to provide a corporate guarantee for the overdraft facility;
- c) Note the work that is taking place to improve FIMCo's commercial and financial position.

2. Additional Budgetary Implications

2.1 None.

3. Executive Summary

- 3.1 The Falkland Islands Meat Company (FIMCo) is an EU-accredited export meat plant processing local mutton, lamb and beef. As the only abattoir on the Islands, it's a vital service to the Falkland Islands' economy, providing an outlet for mature sheep, primarily raised for wool, and an alternative income stream for meat producers to combat the vagaries of the wool price cycle.
- 3.2 FIMCo is an important enabler of economic diversification in the agricultural sector and whilst it operates as a Private Limited Company, strategic decisions are made with the long term development of the Islands agricultural economy in mind.
- 3.3 The Falkland Islands Government (FIG) have provided an operating subvention to FIMCo, since its inception in 2003. FIMCo is wholly owned by Falkland Islands Development Corporation (FIDC), which in turn is a body corporate and not part of FIG or the Crown.
- 3.4 In addition to the annual subvention payment from FIG, and with no reserves to finance its working capital requirement, FIMCo has access to an overdraft facility provided by Standard Chartered Bank (SCB). The overdraft is guaranteed by FIMCo's shareholder and subject to annual renewal.
- 3.5 In 2017, FIMCo Directors were minded to increase the overdraft limit from **REDACTED** to **REDACTED**, to ensure the company had adequate working capital available to the business. It was recognised at the time that this increased overdraft limit could only be an interim solution and FIMCo needed to urgently review its operating model to ensure it performed within its financial means.
- 3.6 In support of this aim, and as majority shareholder, FIDC commissioned a review of FIMCo's model of operation and Business Plan. This work was completed in June 2017

and generated an independent and informed assessment of the challenges and opportunities facing the meat processing plant at Sand Bay.

- 3.7 The FIMCo Board subsequently agreed to implement changes to the operation, and a cultural shift in the abattoir's approach to business, in order to become a more commercially viable operation.
- 3.8 As a result of the changes that have already been made, FIMCo's commercial position is much improved, and whilst there is still a need for an overdraft to cover timing delays between costs leaving the Company bank account and sales revenue being paid to the Company, **REDACTED**.
- 3.9 FIMCo is therefore seeking to renew the overdraft facility **REDACTED** by the end of March 2018. This will provide access to funding that may be needed to ensure the company is able to make business decisions that are not adversely affected by cash flow, with the long term aspiration of building and retaining reserves it needs to operate year on year.

4. Background

- 4.1 The Falkland Islands Meat Company (FIMCo) was established to support the strategic diversification of Falkland Islands agriculture and to provide additional revenue opportunities for farmers. Along with the sector's traditional focus on the export of wool, the operation of FIMCo has resulted in new market opportunities for the production of mutton and lamb, as well as import substitution of beef in the domestic market. By providing a facility for the slaughter and processing of animals, FIMCo ensures that farmers have more than one potential stream of revenue from their livestock.
- 4.2 Since its inception, FIMCo has required government subventions to operate, **REDACTED**. These are provided based on the strategic importance of the sector and FIMCo's role in the development of the Islands' meat industry. While agriculture accounts for only 2.1% of GDP, it employs 10% of the workforce and is vital to the continued viability of Camp.

Table 1 **REDACTED**

- 4.3 FIMCo has always relied on FIG to provide a subvention to cover annual losses, and there has only been a single year in which a subvention was not drawn.
- 4.4 Since that time, losses have increased significantly, as have the subvention and overdraft requirements. Cognisant of this worsening situation and the risk to the long term future of the operation, the FIMCo Board asked their shareholder FIDC to undertake a strategic review of FIMCo.
- 4.5 FIDC commissioned specialist consultants to conduct an independent review on the current operation at the meat processing facility, covering a range of performance factors, including throughput, staffing and productivity.
- 4.6 Whilst not the focus of this paper, that review has now been completed with the Consultants recommending the following priority areas are considered;
- Export marketing and sales strategy- review the current approach of ‘selling complexity’ with all the associated costs of production;
 - Procurement – working more closely with producers to facilitate better planning on staffing requirements and daily throughput
 - Costs – review and improve the overall efficiency of the plant, and, in line with a more commercially focused sales and marketing strategy, remodel the operation to reduce overall costs.
- 4.7 The review process also highlighted the need to appoint an experienced Business Improvement Manager to provide the organisation with the expertise and capacity to research and design a new business model for FIMCo. That person has now been recruited and arrived in the Islands in early February 2018.
- 4.8 Whilst work has started on implementing the recommendations from the review, FIMCo still has a significant working capital requirement, which in itself contributes to the company’s current loss-making position.
- 4.9 Cash flow challenges have always existed for FIMCo due to its short and intensive export season, distance to markets and timing delays between costs leaving the company bank account and sales revenue being paid to the company.
- 4.10 In 2016/17, when considering FIMCo’s overdraft requirement, Directors faced a ‘perfect storm’ of market and operational challenges including;
- FIG’s decision to cap the annual subvention payment **REDACTED** – regardless of any worsening market position;
 - A considerable amount of working capital tied up in unsold stock;
 - All the costs associated with maintaining a high level of stock and the potential for this stock to become worthless over time;

- The end of a phase of oil exploration which would see local sales significantly reduced and the loss of around **REDACTED** from incinerator income.
- 4.11 Against that backdrop, forecast losses for 2016/17 financial year were estimated to be in the region of **REDACTED**, and in the worst- case scenario as high as **REDACTED**. Given the potential impact this would have on the Company’s bank balance, Directors thought it prudent to increase the overdraft limit to **REDACTED**, to ensure there would be adequate working capital available to the business.
- 4.12 Securing access to these funds provided an interim solution to FIMCo’s cash flow challenges and provided the time and space to consider the strategic decisions required to improve the company’s commercial position.
- 4.13 FIMCo is currently in a much stronger position and a number of pressing issues have been addressed:
- The volume of stock has been considerably reduced;
 - **REDACTED**
 - Sales prices have been significantly increased.
- 4.14 Whilst there is still a lot more to do, these changes have already had a positive impact on the company’s financial position **REDACTED**
- 4.15 **REDACTED**. Subject to securing the corporate guarantee required by Standard Chartered Bank, **REDACTED**.

5. Options and Reasons for Recommending Relevant Option

- 5.1 Option 1: Do not provide a guarantee for FIMCo’s overdraft facility with Standard Chartered Bank once it expires at the end of March 2018. This option is **NOT RECOMMENDED** as it would likely result in default by FIMCo on any current overdraft with the Bank and would likely lead to the ultimate bankruptcy of the company. This would eliminate an important source of income for farmers and set back the gains that have been made in diversifying the agricultural sector. In addition, if FIMCo defaults on its loans, FIDC will be liable to repay SCB or assume the debt itself, which could mean an increase in its subvention request to FIG.
- 5.2 Option 2: FIDC extends its guarantee for an additional year **REDACTED** from 1st April 2018 – 31st March 2019. This option is **RECOMMENDED** as it will permit FIMCo to cover cash flow shortfalls due to timing delays and also provide sufficient working capital to operate whilst the company continues to design and implement a robust and sustainable model of operation for the meat processing plant.
- 5.3 The arrangement with SCB has been reviewed on several occasions to ensure it is an efficient and effective means of funding the abattoir’s working capital requirement. Alternative funding options were considered again last year (Executive Council paper no 23/17) **REDACTED**.
- 5.4 Having revisited these options in the context of the proposals set out within this paper, the overdraft with SCB is still considered to be the most cost effective and practical

method of financing FIMCo's working capital requirements and to allow for changes to be implemented before the next overdraft review.

6. Resource Implications

6.1 Financial Implications

SCB has not yet confirmed the facility fee and interest rates which will be met by FIMCo. **REDACTED**

6.2 Human Resource Implications

None for the purposes of this paper.

6.3 Other Resource Implications

None for the purposes of this paper.

7. Legal Implications

7.1 The Finance and Audit Ordinance requires the consent of the Secretary of State for the granting of any guarantees by FIG. The Foreign and Commonwealth Office view is that when considering FIG's contingent liabilities account must also be taken for the actual and contingent liabilities for which FIG is legally responsible, which includes corporations such as FIDC and any companies wholly owned by FIG and or its statutory corporations.

8. Environmental & Sustainability Implications

8.1 None for the purposes of this paper.

9. Significant Risks

9.1 There are no direct, immediate financial implications from Executive Council granting approval. The corporate guarantee, if approved, will be recognised as a contingent liability for FIDC, which is in turn a contingent liability for FIG. Should FIMCo default on its loan, FIG could be required to reimburse FIDC for any payments due to SCB.

9.2 There is a clear need for the company to renew the overdraft by the 31st of March 2018. Based on current projections, the overdraft limit can be reduced and still provide sufficient working capital for the business.

9.3 It should be noted, FIMCo's working capital requirement is at its highest during the first half of May-the point at which the export season's costs have been incurred and the customers haven't yet paid the company. As customers are buying several containers of product at a time, payments are in the hundreds of thousands of pounds and not made until the meat is delivered. Any shipping delays therefore have a very significant impact on the company's bank balance and the overdraft facility helps mitigate this risk.

9.4 If it's not possible to renew the overdraft facility, there is a risk that the company will not have sufficient funds to be able to continue trading, with the resulting losses likely

to exceed the proposed overdraft limit. If FIMCo is dissolved, there will be immediate detrimental impacts on the farming community, as they will have no options for selling livestock currently designated as being raised for meat. In addition, ongoing efforts to diversify agricultural exports will be delayed or halted.

- 9.5 There is a risk that the proposed overdraft will not provide sufficient working capital and that FIG will have to provide additional financial support.

10. Consultation

- 10.1 The FIDC Board held a meeting on the 25th January 2018, and considered the renewal of this guarantee, having approved the recommendation to approve a reduced guarantee, as set out in FIDC Board paper number 728/18, the Board are seeking support from Executive Council and the Secretary of State, to consider FIDC continuing to provide a corporate guarantee for the overdraft facility.

- 10.2 A copy of this paper has been shared with MLA Mark Pollard and MLA Stacey Bragger prior to submission to Executive Council.

11. Communication

- 11.1 Subject to the approval of Executive Council, FIDC's Managing Director will liaise with Government House regarding the request to the Secretary of State for Foreign and Commonwealth Affairs.

- 11.2 Once all the necessary approvals have been secured, FIDC's Managing Director will ensure that both the overdraft and corporate guarantee documents are signed by Members of the FIMCo and FIDC Board before the 31st March 2018.

Schedule of suggested deletions to enable publication of paper:

As highlighted