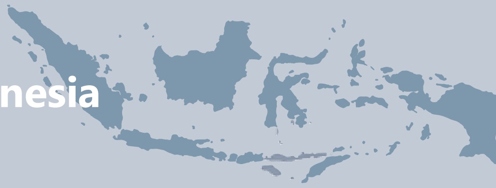
Temporary Capital Placement
PT Bank Century (2008)



Background and context

PT Bank Century (Bank Century) was established on 28 December 2004 following the merger of PT Bank CIC International, PT Bank Pikko and PT Bank Danpac. In 2008, Bank Century held total assets of IDR15.02 trillion ($1.28 billion) and a network of 56 offices focusing on retail, consumer and SME banking. In comparison, during the same period, the total assets of Indonesia's largest bank, PT Bank Mandiri, stood at IDR318.7 trillion ($25 billion).

The resolution of Bank Century happened in the midst of the GFC, with policy measures in place to maintain public confidence in Indonesian banks. This included raising of the deposit insurance limit substantially from IDR100 million to IDR2 billion (about $180,000) in October 2008. Subsequently, on 21 November 2008, the central bank – Bank Indonesia (BI) – deemed Bank Century to be a failed systemic bank, paving the way for its takeover by the Indonesia Deposit Insurance Corporation (IDIC). IDIC is directly accountable to the President of Indonesia.

IDIC then restructured and rebranded Bank Century as PT Bank Mutiara (Bank Mutiara) and sold it to a Japanese finance company, J Trust Co. Ltd (J Trust) in November 2014 for IDR4.4 trillion ($360 million) at 3.5 times price-to- book value. As at October 2014, Bank Mutiara had registered losses of IDR163.1 billion ($13.4 billion).

Resolution actions

Temporary Capital Placement (TCP)

On 21 November 2008, an FSSC meeting – led by the Minister of Finance and attended by members of the FSSC, namely the Governor of BI, the Chairman of IDIC, and several other related parties – discussed Bank Century's problems and measures that needed to be taken.

There were three key considerations. Firstly, the threat of contagion to, as well as runs in other banks, if Bank Century were to be declared insolvent. According to BI (then Indonesia's banking supervisor), 23 other mid-sized banks were at risk with liquidity problems having experienced bank runs. The concern was then a broader spread of vulnerabilities from the financial sector to other industries and the impact on jobs. Moreover, there were financial and economic uncertainties from the GFC during that period.

> ***In an emergency situation - market psychology wise - any failing bank would trigger a bank run ... the contagion would travel from bank to bank, from the financial sector to industries, which eventually would hurt jobs***
>
> Boediono, former Governor of Bank Indonesia

Second was the financial condition of Bank Century and the costs of saving it. At the time of the decision, Bank Century's CAR was -3.53%, equivalent to additional capital requirements of IDR632 billion ($51 million). However, three days later, Bank Century's actual CAR was discovered to be -35.92%, after accounting for non-performing securities and fictitious assets.

Third was the strain that the bailout costs would put on the deposit insurance fund (Fund). Decision makers deemed the first estimate of capital requirements to be reasonable in terms of impact to the Fund. The critical factor was whether the deposit insurance scheme could support depositors, and prevent the loss of confidence and severe bank runs such as those that had taken place during the AFC in 1997 to 1998. In 2008, the Fund size was IDR14 trillion ($1.1 billion) compared with total covered public deposits of up to 1,000 trillion ($78.4 billion).

During the resolution process performed by IDIC (from November 2008 to November 2014), IDIC made five TCPs in Bank Century / Bank Mutiara amounting to IDR8.011 trillion ($658 billion).

Resolution of Bank Century – Timeline of Key Events

28 Dec 2004
Bank Century established (merger of Bank CIC-Pikko-Danpac) and remained under intensive supervision by Bank Indonesia.

Dec 2004-Oct 2008
Bank Century took actions to resolve problematic assets and liquidity problems, including additional capital injection by shareholders through a rights issue.

5 Nov 2008
BI determined Bank Century as a "Bank under Special Supervision" due to its liquidity and solvency problems.

20 Nov 2008
BI saw Bank Century as systemically important and proposed their conclusions to the Financial System Stability Committee (FSSC) for further discussion.

21 Nov 2008
FSSC determined Bank Century as a failed bank with systemic impact and handed over Bank Century to IDIC. Bank Century was then resolved by IDIC via temporary capital placement.

2008-09; 2013
IDIC temporary capital placement in 2008-09: IDR6.76 trillion ($556 million) into Bank Century and 2013: IDR1.25 trillion ($102 million) into Bank Mutiara.

2011-2013
The process for sale of Bank Mutiara's shares was carried out openly by IDIC. However, there were no potential investors that met the requirements.

Apr 2014
IDIC starts public bidding process for Bank Mutiara.

Mar-Nov 2014
IDIC continued with its transparent sale process until Bank Mutiara was sold to J Trust with a value of IDR4.41 trillion ($360 million) (3.5x book value) in November 2014. Subsequently, renamed as PT Bank J Trust Indonesia (Bank J Trust) in March 2015.

2014-2017
J Trust Group injected capital of about IDR3 trillion ($221 million) in phases into Bank J Trust.

Mar 2020
Improvement of Bank J Trust's financial performance: CAR at 13.11%, total assets of IDR19.5 trillion ($123 million), Registered profit of IDR9 billion ($0.6 million), gross NPL ratio of 2.63% (2014: about 14%).

> ***The sale of Bank Mutiara's shares to a Japanese investor, J Trust, was done openly and transparently ... IDIC has handled the failed bank according to the law***
>
> Indonesia Deposit Insurance Corporation

In April 2014, pursuant to IDIC's auction of Bank Mutiara, 11 potential buyers from China, Indonesia, Japan, Malaysia and Singapore submitted letters of interest. Those short-listed then submitted preliminary bids and were given access to IDIC's data room to facilitate the due diligence processes. Buyers were attracted to Bank Mutiara due to exemption from the 40% cap on foreign ownership of local banks in Indonesia, and the prospect of tapping into a profitable market with strong growth potential. In November 2014, after approval from the Financial Services Authority or Otoritas Jasa Keuangan (OJK), J Trust was announced as the successful bidder. On 30 March 2015, Bank Mutiara was rebranded as Bank J Trust.

From a legal perspective, the IDIC was required to complete the sale of Bank Mutiara within a five-year period. This was required to be conducted at a minimum amount equal to the total of IDIC's TCP (known as the Optimum Return). However, where the Optimum Return could not be realised within five years, the law permits a sale, in the sixth year, at the most optimal market price.[61]

Bank Mutiara was sold to J Trust for IDR4.4 trillion ($360 million) at 3.5 times price-to-book value. Most analysts saw the sale price as being a premium, given the weak financial condition of Bank Mutiara. Pursuant to the acquisition, from 2014 to 2017, the capital position of Bank J Trust was strengthened through phased injections amounting to a total of IDR3 trillion ($221 million). According to results in the first quarter of 2020, Bank J Trust's financial performance has improved: CAR stood at 13.11% with gross NPL ratio of 2.63%.

Key takeaways

Arriving at a decision on the idiosyncratic or systemic nature and impact of a FI is highly challenging. In Bank Century's case, this was made more complex by four inter-related factors. First, the prevailing GFC environment with low level of public confidence in the financial sector and economic uncertainties. Second, the speed and urgency of decisions as contagion risked sparking more bank runs. Third, the mid-sized characteristic of Bank Century made it harder to establish adverse impact on the overall financial system and economy. Fourth, the structure of the Indonesian financial system with a large number of banks and the developmental stage of market- based finance.

A decision on the optimal resolution method is heavily reliant on accurate data concerning the financial condition of the institution. This is critical to enable decision makers to ascertain the costs of resolution and the amount of resources required to tackle the root problem.

Resolution via nationalisation provides immediate stability to the financial system, but can take up considerable amount of resources and time. Bank Mutiara required two large capital injections and was divested to J Trust after six years of being managed by the IDIC.

Coordination and cooperation amongst financial safety net players is a crucial and key success factor in resolving problem banks to safeguard financial system stability. Sound governance – including clear and transparent processes and strong legal foundations – are important pillars for effective bank resolution. These are important to support decision making by policy makers, and in light of scrutiny by lawmakers and other stakeholders of the selected resolution scheme and actions such as capital injections and sale of the distressed bank to interested parties.

[61] In 2014, the Constitutional Court issued a decision stating that IDIC may sell the shares of the rescued failed banks with the price below the TCP value, provided that it does not cause the state loss as long as it is carried out openly and transparently