CHAPTER 5

MONETARY MANAGEMENT AND FINANCIAL MARKET DEVELOPMENT

Monetary Policy and Monetary Management

The eighth and ninth issues of Bangladesh's Bank half-yearly Monetary Policy Statement (MPS) outlined the monetary policy outlook for the first and second half of FY2009-10 respectively. Both the MPSs were designed to support the target of achieving the highest sustainable output growth, while containing inflation at moderate levels. Against the backdrop of recessionary global environment, Bangladesh Bank pursued easy credit condition during FY2009-10 with special emphasis on the sectors like agriculture and small and medium-scale enterprises (SMEs). In addition, downward stickiness of lending interest rates and service charges of financial services of banks are being addressed more directly rather than advisory measures. The intention of Bangladesh Bank's guidance is to enhance the inclusiveness of financial services to all segments of population with a view to engage them into the productive economic activities.

Aiming to provide adequate liquidity during global recession, Bangladesh Bank refrained from mopping up excess reserves at the beginning of FY2009-10. Despite adequate supply of money and credit, demand for credit did not increase during this period. As a result, liquidity increased in the money market and the call money rate plummeted below 1 percent. Under the circumstances, Bangladesh Bank started operating 30-day Bangladesh Bank Bills from August, 2009 and resumed its' reverse-repo operation in October, 2009 with a lower interest rate that led to gradual reduction of excess reserves of the scheduled banks. However, a large portion of the excess liquidity was absorbed to provide credit to the private sector and import payments as the economic activities boosted up in the middle of the fiscal year. Moreover, the inter-bank call money rates exceeded 4 percent. In spite of substantial decline in the excess reserves, inflation continued to show upward trend and exceeded the earlier projected level of 6.5 percent for FY2009-10. In order to contain such inflationary pressure by restraining expansion of monetary base, Bangladesh Bank raised Cash Reserve Requirements (CRR) and Statutory Liquidity Ratio (SLR) by 0.5 percentages point which were effective from 15 May 2010.

Money and Credit Situation

Broad money (M2) recorded an increase of Tk. 66,531.4 crore or 22.44 percent during FY2009-10 in comparison with the increase of TK. 47,704.9 crore or 19.17 percent during FY2008-09. Componentwise analysis of broad money shows that the currency outside the banks rose by 28.04 percent. However, the deposit also increased by 21.66 percent of which the demand deposits soared by 37.7 percent and time deposits grew by 19.55 percent. The stock of broad money stood at Tk.3,63,031.2 crore at the end of

FY2009-10 compared to Tk.2,96,499.8 crore at the end of FY2008-09. Table 5.1 shows the composition of money supply, credit and their movements over time.

Table 5.1: Composition of Broad Money (M2) and its Trend over Time

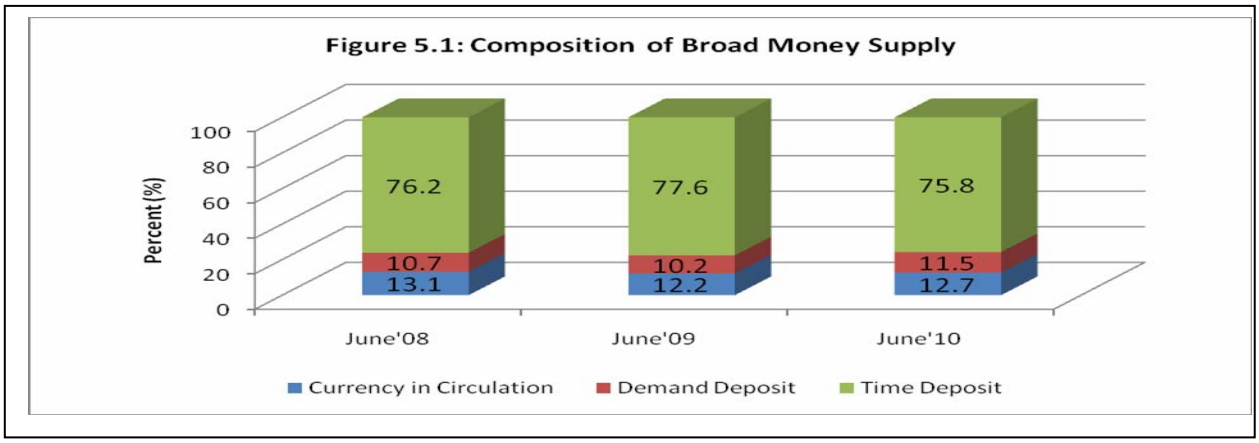
(Tk. in crore)

Particulars	June 2008[R]	June 2009[R]	June 2010	Change	
				July -June 2009-10	July-June 2008-09
1	2	3	4	5=4-3	6=3-2
1. Broad Money (M2) Supply (a+b+c)	**248794.90**	**296499.80**	**363031.20**	**66531.40 (+22.44)**	**47704.90 (+19.17)**
a) Currency notes and coins with the public	32689.90	36049.20	46157.10	10107.90 (+28.04)	3359.30 (+10.28)
b) Demand deposit[1]	26624.50	30377.70	41831.20	11453.50 (+37.70)	3753.20 (+14.10)
c) Time deposit	189480.50	230072.90	275042.80	44969.90 (+19.55)	40592.40 (+21.42)
2. Source to change the Broad Money (M2) (a+b)	**248794.90**	**296499.80**	**363031.20**	**66531.40 (+22.44)**	**47704.90 (+19.17)**
a) Net foreign assets of the banking system	37317.90	47459.40	67066.90	19607.50 (+41.31)	10141.50 (+27.18)
b) Net domestic assets of the banking system ((1)+(2))	211477.00	249040.40	295964.30	46923.90 (+18.84)	37563.40 (+17.76)
(1) Total domestic credit of the banking system[2] (i+ii+iii)	248677.20	288552.40	340176.00	51623.60 (+17.89)	39875.20 (+16.03)
i) Government sector (net)[2]	46909.10	58185.20	54392.30	-3792.90 (-6.52)	11276.10 (+24.04)
ii) Public sector (other)[2]	11632.40	12439.70	15023.00	2583.30 (+20.77)	807.30 (+6.94)
iii) Private sector[2]	190135.70	217927.50	270760.70	52833.20 (+24.24)	27791.80 (+14.62)
(2) Other assets (net)	-37200.20	-39512.00	-44211.70	-4699.70 (-11.89)	-2311.80 (-6.21)

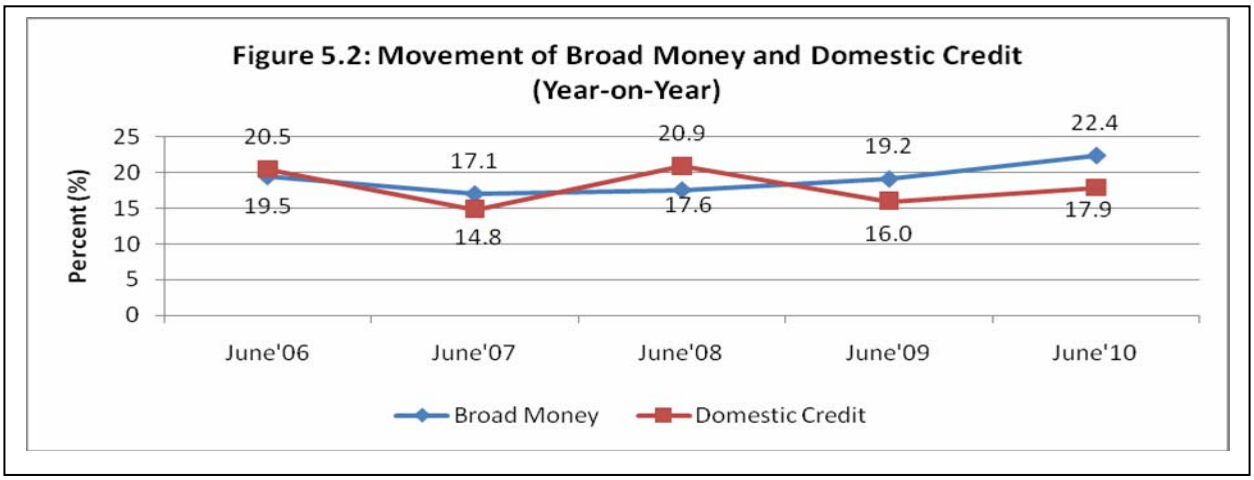
Source: Bangladesh Bank

Note: Figures in parentheses indicate percentage changes over end June of the previous year, R= Revised
1/ including accrued interest. 2/ including deposits of other financial institutions and government agencies

Figure 5.1 depicts the component of broad money supply. It reveals from the figure that, recently currency in circulation and demand deposit increased, while the time deposit decreased.



During FY2009-10, domestic credit of the banking system recorded an increase of Tk. 51,623.6 crore (including accrued interest) or 17.89 percent in comparison with the increase of Tk. 39,875.2 crore or 16.03 percent during FY2008-09. The rise in domestic credit during FY2009-10 was due to significant rise of private sector credit Tk. 52,833.2 crore or 24.24 percent compared to the increase of 27,791.8 crore or 14.62 percent in FY2008-09. Besides, net credit to the government sector decreased by Tk. 3,792.9 crore or 6.52 percent, from Tk. 58,185.2 crore at the end of June 2009. However, credit to the other public sector grew by Tk. 2,583.3 crore or 20.77 percent compared to the increase of 6.94 percent in the previous fiscal year. Figure 5.2 shows the movement of broad money and domestic credit over last five years.



In FY2009-10, the private sector credit increased mainly due to mandatory lending and refinancing to the agriculture sector, lending to SMEs and other priority sectors including the trade sector. On the other hand, net outstanding Government borrowing from the banking system declined due to high growth of revenue and the higher level of financing from the non-bank sources. Particularly net sale of national savings certificates increased remarkably because of the higher interest rate compared to the interest rates for deposit in the banking system.

Reserve Money

In recent years, reserve money (RM) has been used as an operational target to adjust liquidity with the overall monetary projection. At the same time, the auctions of weekly Bangladesh Bank Bills were used to influence the level of RM, while repo and reverse repo instruments were used for fine-tuning for liquidity management.

In FY 2009-10, reserve money of Bangladesh Bank increased by Tk.11,120.2 crore or 16.03 percent from Tk.69,390.1 crore at the end of June 2009 to Tk.80,510.3 crore at the end of June 2010 . The growth of reserve money was mainly attributable to the increase in net foreign assets (NFA) of Bangladesh Bank by 41.52 percent. However, net domestic assets (NDA) of Bangladesh Bank decreased by 26.13 percent during the period. The consistent growth of remittances and the decline of import payments mainly contributed to the rise of net foreign assets. In contrast , Bangladesh Bank's claims on government sector

(net), deposit money of the scheduled banks (DMBs) and other public sectors declined by 22.91 percent, 14.53 percent and 1.87 percent respectively which caused a plunge in the net domestic assets. Money multiplier of M2 increased from 4.273 at the end of June 2009 to 4.509 at the end of June 2010. During the same period, M2/deposit ratio increased from 0.138 to 0.146 and reserve/deposit ratio declined from 0.128 to 0.108. Table 5.2 shows the composition of reserve money and its changes over time.

Table 5.2: Reserve Money: Composition and its Changes over Time

(Tk. in crore)

Particulars	June 2008[R]	June 2009 [R]	June 2010	Change	
				July-June 2009-10	Jul -June 2008-09
1	2	3	4	5=4-3	6=3-2
1. Reserve money (a+b+c)	52789.60	69390.10	80510.30	11120.20 (+16.03)	16600.50 (+31.45)
a) Currency issued	35648.50	39448.70	50465.40	11016.70 (+27.93)	3800.20 (+10.66)
b) Balances of scheduled banks with BB	17034.20	29800.20	29835.50	35.30 (+0.12)	12766.00 (+74.94)
c) Reserves of other financial institutions with the BB	106.90	141.20	209.40	68.20 (+48.30)	34.30 (+32.09)
2. Sources of change in Reserve Money (a+b)	52789.60	69390.10	80510.30	11120.20 (+16.03)	16600.50 (+31.45)
a) Net foreign assets of BB	32835.80	43244.90	61198.10	17953.20 (+41.52)	10409.10 (+31.70)
b) Net domestic assets of BB (i+ii)	19953.80	26145.20	19312.20	-6833.00 (-26.13)	6191.40 (+31.03)
i. Domestic credit (a+b+c+d)	35927.20	38632.40	31492.90	-7139.50 (-18.48)	2705.20 (+7.53)
a) Government sector (net)	25997.30	28955.50	22320.60	-6634.90 (-22.91)	2958.20 (+11.38)
b) Public sector (other)	898.90	808.10	793.00	-15.10 (-1.87)	-90.80 (-10.10)
c) BB's claims on DMBs	7334.20	6846.70	5852.00	-994.70 (-14.53)	-487.50 (-6.65)
d) BB's claims on non-bank depository corporations	1696.80	2022.10	2527.30	505.20 (+24.98)	325.30 (+19.17)
ii. Other assets (net)	15973.40	12487.20	12180.70	306.50 (+2.45)	3486.20 (+21.83)

Source: Bangladesh Bank

Note: Figures in parentheses indicate percentage changes over end June of the previous year. R= Revised.

Financial Market Management

Financial market in Bangladesh essentially consists of banks and non-bank financial institutions and capital market which include state owned commercial banks (SCBs), private commercial banks (PCBs), foreign commercial banks (FCBs), government owned specialized banks, non-banking financial institutions (NFIs), Investment Corporation of Bangladesh (ICB), House Building Finance Corporation

(HBFC), Dhaka Stock Exchange (DSE), and Chittagong Stock Exchange (CSE). Besides, a total of 44 general insurance companies (1 state-owned) and 18 life insurance companies (1 state-owned) are operating in the country.

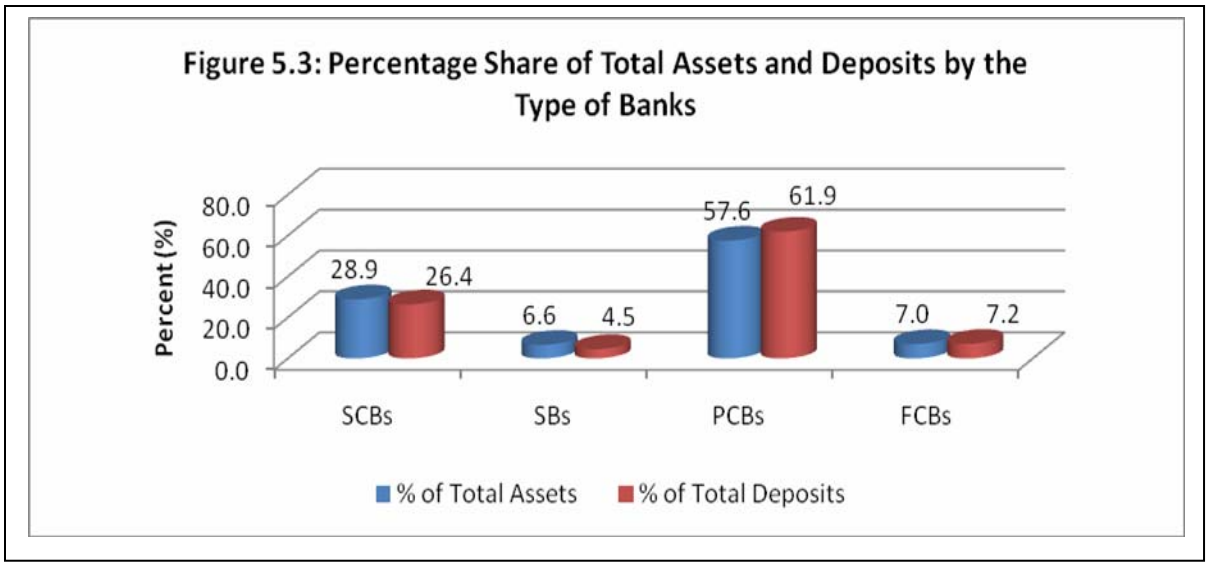
Banking sector

As of June, 2010 47 scheduled banks which include 4 state-owned commercial banks, 30 private commercial banks, 9 foreign-owned commercial banks, 4 government-owned specialized banks, are operating in Bangladesh through their 7,246 branches . Among those branches as many as 3,394 belong to state-owned commercial banks, 2,427 branches to local private banks, 59 branches to foreign banks and 1,366 branches to specialized banks. Moreover, there are 1 National Co-operative Bank, 1 Ansar VDP Bank, 1 Karmasangsthan Bank and 1 Grameen Bank which are operating as the non-scheduled banks. In Bangladesh, 4,169 branches of the scheduled banks are operating in the rural area. The structure of banking system and individual bank's share (in percent) of total deposits and assets are shown in Table 5.3 and figure 5.3 respectively at the end of June, 2010.

Table 5.3: Structure of the Banking System in Bangladesh (up to June 2010)

Type of Banks	No. of Banks	No. of Bank Branches	% of Total Asset	% of Total Deposit
SCBs	4	3394	28.85	26.42
SBs	4	1366	6.60	4.53
PCBs	30	2427	57.55	61.90
FCBs	9	59	7.00	7.15
Total	47	7246	100.00	100.00

Source: Bangladesh Bank.

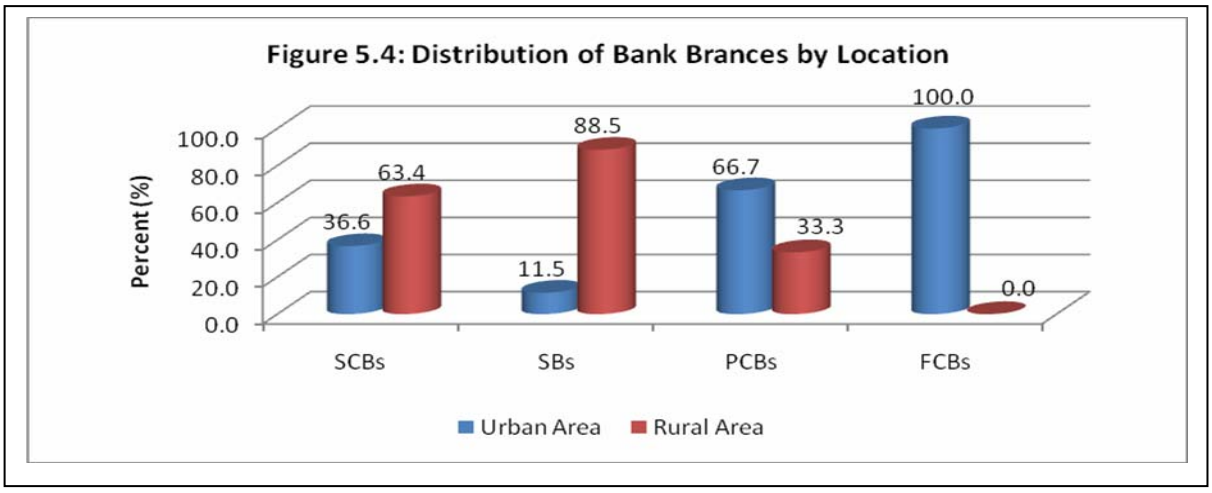


Although private and foreign banks are better in terms of capital adequacy, qualities of assets, income-expenditure ratio etc., they offer only limited access. On the contrary, there is much more access of mass people to the state-owned commercial banks and specialized banks because of wider distribution of their branch network. As of June, 2010 while there was no branch of the foreign banks in the rural areas, only 33.3 percent of the total branches of the local private banks were located in rural areas. On the other hand, 63.41 percent and 88.51 percent of the total branches of state-owned commercial banks and specialized banks are located in the rural areas respectively. Regional distribution of the branches of the banks (in percentage) and their categories (up to June 2010) are shown in Table 5.4 and Graph 5.4 respectively.

Table 5.4: Distribution of Bank Branches in Different Regions

Type of Banks	No. of Banks	No. of Bank Branches			As % of the Total Branches		
		Urban	Rural	Total	Urban	Rural	Total
SCBs	4	1242	2151	3394	36.59	63.41	100
SBs	4	157	1209	1366	11.49	88.51	100
PCBs	30	1619	808	2427	66.70	33.30	100
FCBs	9	59	0	59	100.00	0.00	100
Total	47	3077	4169	7246	42.46	57.54	100

Source: Bangladesh Bank.



To achieve greater efficiency, stability and transparency in the financial sector, the ongoing reform continued through FY2009-10 and the financial indicators remained at satisfactory levels during this period. Due to the expansion of economic activities, bank credit increased by 23.16 percent at the end of June, 2010 in comparison with the same at the end of June, 2009. As a result, excess liquidity in banking sector decreased to 10.81 percent in June 2010 from 13.14 percent in June 2009.

Despite little increase in loans and advances in the year 2009 compared to 2008, there had been no adverse impact on the income and profitability. Therefore, Return on Asset (ROA) increased from 1.16 percent in December, 2008 to 1.37 percent in December, 2009 (considering profit after provision and tax).

To comply with international best practices and to make the bank's capital more resilient as well as to build the banking industry more risk sensitive, shock absorbent and stable, Bangladesh Bank commenced implementation of Basel-II capital adequacy framework from January 2010 as regulatory requirement for banks. Before unveiling the program there had been a test run period of one year with four trial-reporting in 2009. It is noteworthy that from 1996 to 2009, the banks inside Bangladesh maintained capital on the basis of risk weighted asset in line with Basel-I wherein only credit risk was taken into account. However, under Basel-II, credit risk as well as the market and the operational risks are being considered for calculating Minimum Capital Requirement (MCR). Moreover, necessary action has been taken to ensure public disclosure of information about bank's capital structure through market disclosure. It is also to be noted that the minimum capital requirement of a bank is a certain percentage of risk weighted assets as fixed by Bangladesh Bank from time to time or Tk. 200 crore, whichever is higher. Bangladesh Bank has fixed up minimum required Capital Adequacy Ratio (CAR) and Minimum Capital Requirement (MCR) for banks at 8 percent up to June 2010, 9 percent up to June 2011 and 10 percent from July 2011 and onward. It is pertinent that banks will have to have paid up capital and reserves (at least Tk. 200.00 crore as paid up capital) of at least Tk. 400 crore by 11 August 2011. The CAR of the banking industry under Basel-II was 7.98 percent in March 2010 compared to 8 percent in December 2009. However, under the Base-I, the CAR of the banking industry was 11.7 percent in December 2009.

Non-bank Financial Institutions

Some non-bank financial institutions (NBFIs) along with banking sectors made significant contribution to the financing of certain important sectors of the economy such as industry, commerce, housing, transportation and information technology. There are 29 licensed non-bank financial institutions in the country until 30 June 2010. At present, 97 branches including 29 head offices of NBFIs are operating in Dhaka city and different areas of the country. Total paid up capital and reserve of these institutions stood at Tk.3081.19 crore as on 30 June, 2010, in which paid up capital was Tk.1,465.97 crore. Total assets and deposits of NBFIs stood at Tk.22,187.75 crore and Tk.7,897.38 crore respectively as on 30 June, 2010. Their investment in different shares and securities stood at Tk.1,538.5 crore at the end of June, 2010. NBFIs also participate in the call money market. They can borrow from this market up to 15 percent of their net assets. Total loan and lease of the NBFIs stood at Tk.16,350.21 crore at the end of June, 2010 and the rate of classified loan of the financial institutions stood at 6.93 percent as on 30 June, 2010.

Interest Rate Movement

Due to excess liquidity in the banking system during the last quarter of FY2008-09 and the first quarter of FY2009-10, the Bangladesh Bank resumed reverse repo auction since October 2009. Eventually, the rate on repo (1-2 Day tenure) plunged into 4.5 percent in November, 2009 from 8.5 percent in September, 2009 and remained unchanged at 4.5 percent up to June, 2010. On the other hand, the rate on reverse repo (1-2 Day tenure) declined to 2.5 percent in October, 2009 from 6.5 percent in March, 2009 and also remained unchanged at 2.5 percent up to June 2010. In line with the trend of liquidity, the inter-bank bank

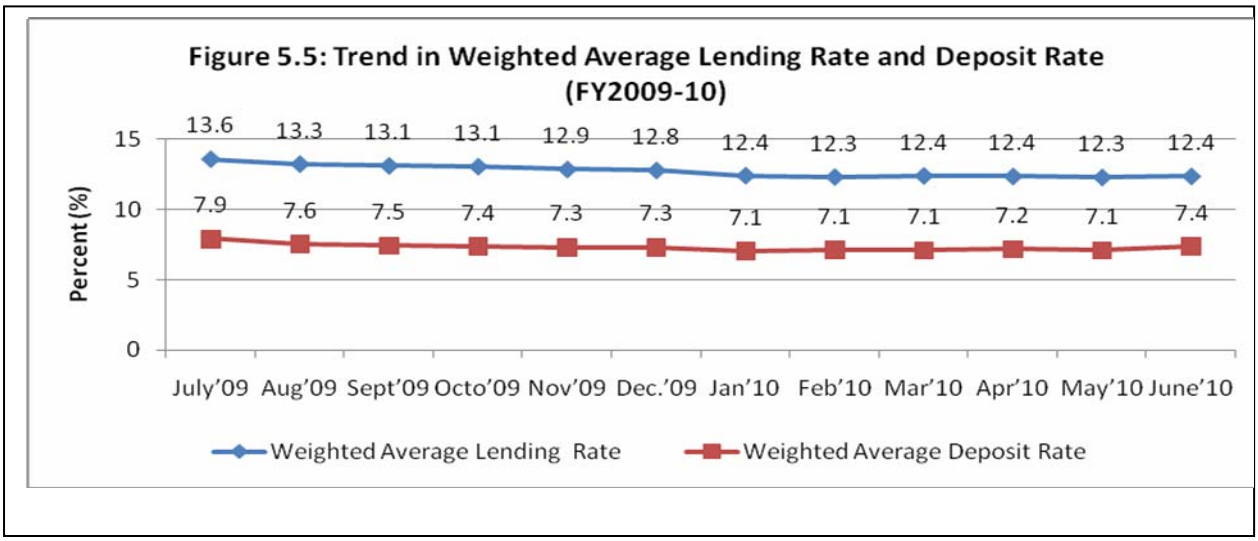
weighted average call money rate increased to 6.46 percent in June, 2010 from 1.08 percent in July, 2009, with some irregular fluctuations within this period. The weighted average yield on 91-Day treasury bills increased from 1.86 percent in July 2009 to 2.42 percent in June 2010, while the average yield on Bangladesh Bank bills increased from 0.96 percent in August 2009 to 2.54 percent in June 2010. The weighted average yield on 182-Day treasury bills, 364-Day treasury bills and the long-term Bangladesh Government Treasury Bonds (5-Year, 10-Year, 15-Year and 20-Year BGTB) were broadly stable during the fiscal year particularly from October, 2009 (Table 5.5)

Table 5.5: Interest Rate Movement during FY2009-10

Month	Treasury Bill			B.B Bills	BGTB				Repo	Rev. Repo	Call Rate	Lending Rate*	Deposit Rate *
	91-Day	182-Day	364-Day	30-Day	5-Year	10-Year	15-Year	20-Year	1-2 Day	1-2 Day			
July'09	1.86	3.75	5.01	--	8.20	9.42	9.93	8.97	--	--	1.08	13.61	7.93
Aug'09	--	--	--	0.96	7.47	8.55	8.59	8.59	--	--	0.72	13.26	7.57
Sept'09	2.05	3.50	4.33	1.00	7.49	8.43	8.80	--	8.50	--	4.39	13.13	7.45
Oct'09	2.14	3.51	4.57	1.04	7.80	8.75	8.69	9.10	--	2.50	2.82	13.07	7.39
Nov'09	2.30	--	4.60	2.50	7.80	--	--	--	4.50	2.50	4.43	12.87	7.33
Dec.'09	2.30	3.54	4.61	2.48	7.80	8.75	8.69	9.10	4.50	2.50	5.05	12.80	7.33
Jan'10	2.34	3.55	4.61	2.50	7.80	--	8.74	--	4.50	2.50	4.83	12.43	7.06
Feb'10	--	3.56	4.62	--	7.82	8.75	8.74	9.11	4.50	2.50	4.51	12.33	7.14
Mar'10	--	3.54	4.63	2.53	7.85	8.76	8.75	9.15	4.50	2.50	3.51	12.41	7.13
Apr'10	2.34	3.42	4.15	2.55	7.85	8.77	8.77	9.17	4.50	2.50	4.36	12.37	7.20
May'10	2.37	3.52	4.20	2.55	--	8.77	8.80	9.19	4.50	2.50	5.18	12.30	7.13
June'10	2.42	3.51	4.24	2.54	7.87	8.78	8.80	9.15	4.50	2.50	6.46	12.37	7.40

Source: Bangladesh Bank, * Weighted average rate

The weighted average rate of interest on commercial lending decreased to 12.37 percent in June 2010, from 13.61 percent in July 2009 and the deposit rate decreased to 7.4 percent from 7.93 percent over the same period. Thus the interest rate spread narrowed to 4.97 percent in June 2010 from 5.68 percent in July 2009 (Figure 5.5).



Rationalising the Rate of Interest/Charges

The government is encouraging banks and non-bank financial institutions to disburse more credit into the productive sectors of the economy to accelerate economic growth and poverty reduction by rationalising interest rates on loans. Currently, banks are free to determine interests on deposits and advances independently except for the advances on export sector. The interest rate for the advances on the export sector was fixed at 7 percent from January 10, 2004. Bangladesh Bank has been closely monitoring the rationalisation of banks' interest rate spread between credit and deposit rates, and has fixed the charge/fees for the services related to credit/deposit for different sectors. It has also been publishing interest rate statements of different banks in their journal and websites on a monthly basis to create competitive environment for fixing interest rates.

Considering the necessity of reducing interest rates to face the current inflationary pressure and global economic situation, the maximum rate of interest on agriculture sector, term loan for large and medium scale industries and working capital loan, housing, and trade financing including financing to NBFIs (Non-Bank Financial Institutions) by banks had been fixed at 13 percent per annum from April 19, 2009. Moreover, to ensure adequate supply of essential commodities and to keep their price within a reasonable limit during Ramadan, the maximum rate of interest on import financing of edible oil (crude and refined), chickpeas, lentils, beans, onions, spices, dates, fruits and sugar (refined and raw sugar/raw cane sugar) had been fixed at 12 percent. However, where the maximum rate of interest was fixed by the central bank, other banks shall report their own maximum limit. Banks are allowed to set different rate of interest that may vary up to a maximum of 3 percent considering comparative risk elements involving borrowers belonging to the same lending category.

To protect the interest of depositors/investors/customers, Bangladesh Bank has rationalized the charges of some services. Considering the interest of the small depositors, no charge can be imposed by the banks in the name of account maintenance fee for average deposit balance up to Tk. 5,000 and maximum Tk. 100 may be imposed as account maintenance fee on six month basis for average deposit balance up to Tk. 25,000 Besides, banks have to display the complete schedule of charges in suitable and visible places inside their offices for their customers' information and upload the same in their respective websites.

Financing in Agriculture, Industry and SMEs

In recognition of the role of agriculture and rural sector in the overall socio-economic development of the country, emphasis has been given on agriculture and rural credit disbursement through banks and non-bank financial institutions in the current fiscal year. Bangladesh Bank is actively engaged in ensuring supply of necessary credit for agricultural activities along with encouraging more involvement of public, private and foreign banks by providing refinance to the government specialized banks. New guidelines along with simplifying agricultural credit disbursement procedures have been issued recently for all operating scheduled banks of the country including private and foreign banks in order to channel more agricultural credit to marginal level. Commercial and agricultural banks are continuing micro credit

operations for alleviation of poverty besides financing the agriculture sector. The target of agricultural credit disbursement through BKB, RAKUB, SCBs, PCBs, FCBs, BRDB and BSBL in FY2009-10 was set at Tk. 11,512.3 crore of which a total Tk.11,116.88 crore was disbursed i.e. 96.57 percent of the target.

Rapid industrialization is critical to attaining the expected momentum of economic development of agro-based developing countries. Due to continuation of industrial credit and other assistance offered by banks and financial institutions to encourage the expansion of large industries and medium and small industries in the past, the amount of industrial credit disbursement by the government has increased over time. During FY2009-10, the amount of industrial credit disbursement and recovery stood at Tk.85,047.61 crore and Tk.64,214.45 crore respectively. During this period, the disbursement of industrial term loans stood at Tk. 25,875.66 crore, which is 29.56 percent higher than that of the pervious fiscal year.

Currently, special emphasis is being given on channeling of credit supply from banking system to the small and medium enterprises bearing in mind the large potentialities of employment generation. Total SME loans increased by Tk 8,266.66 crore or by 17.01 percent, to Tk. 56,720.18 crore at the end of June 2010 as compared to Tk. 48,473.52 crore at the end of June 2009.

Financial Sector Management and Policy Reforms

An efficient financial sector is a prerequisite for economic development. Keeping this in view, the government has taken a number of initiatives to reform this sector. Some of the ongoing and new reforms are discussed below:

Reforms in the Banking Sector

Bangladesh Bank

- The Bangladesh Bank is implementing the Central Bank Strengthening Project (CBSP) with the financial assistance of the International Development Agency (IDA). The project started in 2003 and expected to be completed by 2011. The main objective of the project is to transform Bangladesh Bank into a modern and dynamic central bank capable of playing appropriate regulatory and supervisory role in the monetary and banking sector. The main components of the project are:
    - Strengthening the Legal Framework
    - Reorganization and Modernization
    - Capacity Building

  Some of the works that have been done (up to June 2010) under the project include the followings.
    - Review of the existing laws (Bangladesh Bank Order, Bank Company Act, Financial Institution Act) has been completed and the Bangladesh Bank authority has already examined the consistency of draft BBO, BCA and FIA

- Functional, reorganization of the Bank has been accomplished through abolishing and merging a number of departments of the Bank. Besides, functions of some departments have been reorganized.
- LAN/WAN infrastructure is in place and connectivity has been established between head office and branch offices.
- A modern Performance Management System (PMS), Recognition and Award Policy, Training Need Assessment (TNA) and a new Training Policy and Procedure have already been formulated and are being followed now.
- A Policy Analysis Unit (PAU) has been established to enhance the quality of research work of the Bangladesh Bank.
- Policies on licensing, good governance, policies on accounting (disclosure), loan classification and provisioning, capital adequacy, liquidity risk management and credit risk management have been formulated and adopted to reinforce prudent regulations and to strengthen supervision activities of Bangladesh Bank.
- Bangladesh Bank has adopted International Accounting Standards (IAS) as its accounting framework and International Standards on Auditing (ISA) for auditing standard from fiscal year 2003.

Reforms in State Owned Commercial Banks

- The Government has already corporatized 3 SCBs (*Sonali* Bank Ltd., *Janata* Bank Ltd. and *Agrani* Bank Ltd.) to enhance efficiency of the banking sector. Meanwhile, *Rupali* Bank Limited has submitted a 'Recapitalization and Progressive 3 Years Transitional Plan'. It is in the process of finalization. Furthermore, the overall progress of these four banks are monitored and reviewed under the Memorandum of Understanding (MOU) signed by the respective banks. Besides, preparation of MOU for Bangladesh *Krishi* Bank and *Rajshahi Krishi Unnayan* Bank for the FY2010-11 is in progress.

Legal Reforms

- To expedite the settlement of disputes regarding loan recovery of financial institutions, the Money Loan Court Act, 2003 *(Artha Rin Adalat Ain, 2003)* has been made effective. In order to strengthen the process of recovering defaulted loans, banks, under this Act are now empowered to sell the collaterals without prior approval of the court. Effective application of this Act has started yielding encouraging results. As of June 2010, 1,10,247 cases were filed, of which 73,976 cases were settled accruing the recovery of Tk. 5,635.39 crore against the claim of Tk. 34,261.67 crore.

Money and Financial Market Reforms

In order to reform and build up a banking system of international standards and to strengthen, fortify and reinforce the overall banking system of the country, several initiatives have been taken in recent years. Some of initiatives of FY2009-10 are discussed below:

- To comply with international best practices and to make the bank's capital more resilient as well as to build the banking industry more risk sensitive, shock absorbent and stable, the Bangladesh

Bank commenced implementation of Basel-II capital adequacy framework from January 2010 as regulatory requirement for banks

- In order to strengthen the capital base of the banks as required by Basel-II accord, guidelines for risk based capital adequacy for the banks have been issued and as per the guidelines, commercial banks will calculate their Minimum Capital Requirement (MCR) against Credit Risk, Market Risk and Operational Risk
- Apart from these three risks, banks will determine their adequate capital against comprehensive risk under their Supervisory Review Process (SRP)
- In addition to guarantee of adequate capital through SRP, necessary action has been taken to ensure public disclosure of information about banks' capital structure through market disclosure.
- As per Basel II criteria, stress testing at half-yearly intervals was also made mandatory for the banks for regular self-assessment of their vulnerabilities and necessary guidelines were issued for the purposes
- The MCR of a bank has been defined as certain percentage of risk weighted assets as fixed by Bangladesh Bank from time to time or Tk. 200 crore, whichever is higher
- Bangladesh Bank has fixed up minimum required Capital Adequacy Ratio (CAR) and Minimum Capital Requirement (MCR) at 8 percent or more for January 2010 to June 2010, 9 percent or more for July 2010 to June 2011 and 10 percent or more for July 2011 and onwards
- Banks will now have to have paid up capital and reserves (at least Tk. 200 crore as paid up capital) of at least Tk.400 crore by 11 August 2011
- Banks can issue subordinated debt as hybrid capital instrument for inclusion in Regulatory Capital
- Banks having subsidiaries i.e. merchant bank, securities brokerage have been instructed to make the financial statement consolidated/solo basis for the purpose of calculating CAR. If it is prepared on solo basis, the deduction for such investment will be 50 percent from Tire-1 capital and 50 percent from Tire-2 capital. The asset representing the investments in subsidiary companies whose capital had been deducted from that of the parent company would not be included in total assets for the purpose of computing the CAR
- Guidelines on Supervisory Review Evaluation Process (SREP) have been issued with a view to evaluating bank's SREP. As per the principles of pillar 2 of Basel-II, every bank will formulate its' own SREP in order to link capital adequacy with the level of risk management
- In order to bring discipline in the capital market, oversight on capital market activities by the banks was tightened; restrictions were imposed on bank in case of lending for land purchase and land acquisition by banks
- Bangladesh Foreign Exchange Dealers Association (BAFEDA) has taken decision to publish the Dhaka Inter-bank Offered Rate (DIBOR) i.e. the average interest rate among banks in the Dhaka inter-bank market with the help of Bangladesh Bank.

Reforms in Insurance Sector

Considering the expansion of trade and commerce in the country and reducing risk related problems in people's life, a new law titled "Insurance Act 2010' has been enacted to update the provisions of 'Insurance Act 1938'. Besides this, the' Insurance Development and Regulatory Authority Act 2010' has been enacted in Parliament, with a view to:

- Synchronize the activities of the existing Insurance Department with Insurance Act
- Maintain proper control and supervision of the sector
- Protect the interests of policy holders and beneficiaries under the insurance policy
- Strengthen the financial base of insurance sector and
- Build capacity to manage the sector

Capital Market

Although capital markets of different countries of the world collapsed in the face of global recession, the capital markets of Bangladesh remained quite buoyant at that time. The market capitalisation and the general index increased remarkably during the period. Market capitalisation of the Dhaka Stock Exchange (DSE) rose from 21.4 percent of GDP in June 2009 to 39 percent of GDP in June 2010 indicating keen interests showed by the investors in the capital market. By the end of June 2010, the number of BO (Beneficiary Owner) accounts has increased to 25.64 lakh from 14.15 lakh at the end of June 2009. Given the growing number of ordinary investors in capital markets, limited supply of securities and investors' expectations for more profit at times made the market volatile. Nevertheless, various steps have been taken to maintain market stability and to establish a transparent and vibrant capital market while deepening it. The Government has also started off-loading state-owned companies' shares. Already, 5 state-owned companies have completed off-loading of shares. As a result, confidence on capital market of local and foreign investors has increased. The Securities and Exchange Commission (SEC) has strengthened its surveillance on securities transactions and supervision on market intermediaries so that market operates in transparent manner. The following steps have been taken to streamline the capital market during FY2009-10:

- **New Investment in the Capital Markets:** During FY2009-10, SEC allowed 10 companies to raise Tk.1,398.92 crore (including premium) as capital through Initial Public Offering (IPO). The subscription money received against the said companies was Tk. 9,125.96 crore, which was 27.74 times higher than the amount of public issues, indicating huge demand of securities in the market.
- **Mutual Funds:** SEC has given approval of 8 companies to publish prospectus of mutual funds for raising capital (total Tk.850 crore) through IPO under Securities and Exchange Commission (Mutual Fund) Rules, 2001 during FY2009-10.

- **Raise Paid-up Capital:** During FY2009-10, SEC has given consent to 50 private limited companies and 52 public limited companies to raise paid up capital of amount Tk.1,354.59 crore and Tk. 4,496.35 crore respectively.
- **New Registration:** During FY2009-10, SEC has given registration certificate to 52 stock broker/dealer of DSE and to 44 stock broker/dealer of CSE. During this period, registration certificate were given to 1,289 authorised representatives of DSE and to 222 authorised representatives of CSE. Besides, 19 depository participant certificates were also issued.
- **Enforcement Action:** During FY2009-10, SEC has taken enforcement actions against 263 issuer companies and other market intermediaries for non-compliance of securities related laws.
- **Central Depository Systems (CDS):** At the end of June 2010, the number of active BO accounts in Central Depository Bangladesh Ltd (CDBL) was 25.64 lakh and the number of eligible companies was 267. They hold around 99 percent of market capitalisation. As a result of dematerialisation, time required for settlement reduced and existence of fake shares is abolished, which plays a significant role in development of market infrastructure.
- **Implementation of Book Building Method:** As an alternative IPO valuation method, the book building method was introduced in Bangladesh capital market for the first time through a notification issued on 11 March 2009. This will attract private companies with good track record and sound fundamentals to raise capital from the market, where issuer may get better price of their shares depending on institutional demand for the shares.
- **Establishment of OTC Market at DSE:** To facilitate transaction of companies delisted by DSE, DSE has established Over-the-Counter (OTC) market since September 6, 2009 upon instruction of the Commission.
- **Bangladesh Institute of Capital Market:** To educate the investors and market intermediaries; and to train the companies in corporate governance in the listed companies 'Bangladesh Institute of Capital Market' has been established.
- **Capital Market Governance Project:** To reform the market, improve the institutional capacity and human resources and enhance the market surveillance system, SEC has taken a project named 'Improvement of Capital Market Governance Program' with assistance of the Government and Asian Development Bank (ADB), which is now under implementation.
- **Training Programme:** The Commission, in association with the Dhaka and Chittagong Stock Exchanges arranged 24 investors training programme, where a total of 705 participants attended. Besides, a total of 953 authorized representatives of the members of the stock exchanges have been trained during this period.

Market Scenario

Dhaka Stock Exchange

The comparative statement of DSE at the end of FY2008-09 and FY2009-10 is shown below:

Table 5.6: Comparative Statement of Dhaka Stock Exchange

Indicators	As on 30th June 2009	As on 30th June 2010	% Increase
Number of listed securities (including mutual funds, debentures and bonds)	443	450	1.58
Issued capital of all listed securities (Tk. in crore)	45,794.40	60,726.30	32.60
Market Capitalisation of all listed securities (Tk. in crore)	1,31,277.30	2,70,074.46	105.73
All Share Price Index	2,520.15	5,111.63	102.83

Source: Dhaka Stock Exchange.

Note: All share price index is calculated on General Share Price Index (excluding 'Z' group) by withdrawing weighted average method from 9 December, 2003.The index base earlier was 100 for DSE. The DSE reintroduced All Share Price Index on March 28, 2005.

The number of securities (including mutual funds, debentures and government bonds) listed with the DSE increased from 443 of June 2009 to 450 by June 2010. By the end of June 2010, the issued capital of listed securities stood at Tk. 60,726.3 crore, which is 32.6 percent higher than that of June 2009. Up to June 2010, market capitalisation of securities stood at Tk. 2,70,074.46 crore (39 percent of GDP) which is 105.73 percent higher than that of June 2009. General share price index of the DSE stood at 5,111.20 in June 2010, which was 2,520.15 in June 2009. The trading operation in the Dhaka Stock Exchange since 1995 to June 2010 is shown in table 5.7 below:

Table 5.7: Trading Operation in the Dhaka Stock Exchange

Calendar Year/ Month-End	No. of Listed Securities	Initial Public Offering (IPO)	Issued Capital (In crore Tk.)	Market Capitalisation (In crore Tk.)	Turnover (In crore Tk.)	Price Index*
1995	201	24	1983.98	5651.81	638.00	835.00
1996	205	24	2305.24	16810.62	3013.30	2300.15
1997	222	12	2820.78	7130.16	1740.34	756.78
1998	228	6	2862.57	5025.40	3436.84	540.22
1999	232	11	2877.46	4478.12	3896.44	487.77
2000	241	7	3119.20	6292.40	4036.48	642.68
2001	249	11	3345.43	6522.28	3986.83	817.79
2002	260	8	3520.30	7126.20	3498.49	822.34
2003	267	14	4605.50	9758.70	1915.21	967.88
2004	256	2	4953.20	22492.30	5318.11	1971.31
2005	286	22	7031.30	23307.50	6483.48	1275.05
2006	310	12	11843.70	32336.80	6506.93	1321.39
2007	350	14	21447.00	75395.00	32282.01	2535.96
2008	412	12	37215.60	105953.00	66796.47	2309.35
2009	415	18	52209.90	188717.70	147530.08	3747.53
June, 2010	450	7	60726.30	270074.46	165324.26	5111.63

Source: Dhaka Stock Exchange.

**All share price index is calculated on weighted average method from 24 November, 2001.The index base earlier was 100 for DSE.*

**All share price index is calculated on General Share Price Index (excluding 'Z' group) by withdrawing weighted average method from 9 December, 2003.The index base earlier was 100 for DSE. The DSE reintroduced All Share Price Index on March 28, 2005.*

Chittagong Stock Exchange

The comparative statement of CSE at the end of FY2008-09 and FY2009-10 is shown below:

Table 5.8: Comparative Statement of Chittagong Stock Exchange

Indicators	As on 30th June 2009	As on 30th June 2010	% Increase
Number of listed securities (including mutual funds and debentures)	245	232	-5.30
Issued capital of all listed securities (Tk. in crore)	13,742.05	20,111.56	46.35
Market Capitalisation of all listed securities (Tk. in crore)	96,247.70	2,53,439.33	163.32
All Share Price Index	10,477.67	18,116.05	72.90

Source: Chittagong Stock Exchange.

**All share price index is calculated on General Share Price Index (excluding 'Z' group) by withdrawing weighted average method from 9 December, 2003.The index base was 1000 for CSE from the year 2000. Previously it was 100.*

The number of securities (including mutual funds and debentures) listed with the CSE stood at 232 as of June 2010 which was 245 as of June 2009. By the end of June 2010, the issued capital of listed securities stood at Tk. 20,111.56 crore which is 46.35 percent higher than that of end June 2009. As of June 2010, market capitalisation of securities reached Tk.2,53,439.33 crore (36.6 percent of GDP) which is 163.32 percent higher than that of end June 2009 . General share price index of the CSE reached 18,116.05 as on June 2010, which was 10,477.67 on June 30, 2009. The trading operation in the Chittagong Stock Exchange since 1995 to June 2010 is shown in table 5.9 below:

Table 5.9: Trading Operation in Chittagong Stock Exchange

Calendar Year/ Month-End	No. of Listed Securities	Initial Public Offering (IPO)	Issued Capital (In crore Tk.)	Market Capitalisation (In crore Tk.)	Turnover (In crore Tk.)	Price Index*
1995	61		1036.80	2413.90	1.97	409.43
1996	117	16	1872.60	14704.30	608.90	1157.90
1997	141	19	2276.14	5283.23	854.51	332.98
1998	150	6	2418.03	4138.25	1403.60	232.80
1999	159	9	2508.09	3654.24	1153.79	197.83
2000	165	3	2726.60	5776.55	1293.38	1412.25
2001	177	9	2965.27	5636.35	1479.62	1836.87
2002	185	9	3107.99	6046.77	1358.61	1841.14
2003	199	10	4196.76	8531.23	668.86	1642.78
2004	195	3	4697.87	21501.08	1755.13	3597.70
2005	210	16	5551.93	21994.28	1404.27	3378.68
2006	213	6	6937.84	27051.07	1589.31	3724.39
2007	227	13	8917.39	61258.00	5259.03	7657.06
2008	238	-	12160.32	80768.40	9980.37	8692.75
2009	217	18	15512.49	147080.70	16256.26	13181.37
June 2010	232	7	20111.56	253439.33	12956.29	18116.05

Source: Chittagong Stock Exchange.

**All share price index is calculated on weighted average method from 24 November, 2001.The index base was 1000 for CSE from the year 2000. Previously it was 100.*

**All share price index is calculated on General Share Price Index (excluding 'Z' group) by withdrawing weighted average method from 9 December, 2003. The index base was 1000 for CSE from the year 2000. Previously it was 100*