IOSCO World Investor Week-2020

Keynote Speech on
The Role of Capital Market for Bangladesh's Development

by
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3 October 2020

Chair of the Inaugural Webiner, Hon. BSEC Chairman, Professor Shibli Rubayat-ul-Islam
Chief Guest and Hon. Minister of Finance, Mr. AHM Mustafa Kamla FCA, MP;
Special Guest, Hon. Private Sector Industry and Investment Advisor to the Prime Minister, Mr. Salman F Rahman, MP;
Special Guest, Hon. Economic Advisor to the Prime Minister, Dr. Mashiur Rahman;
Very distinguished guests from the Ministry of Finance, Bangladesh Bank, Industry Associations, Dhaka and Chittagong Stock Exchanges, DSE Brokers' Associations, Merchant Banks' Association, Association of Asset Management Companies and other capital market intermediaries;
Dear Journalist friends from print and electronic media; and
Ladies and gentlemen. As Salamu Alaikum.

Bangladesh was one of the fastest growing emerging economies in the world until 2020. The country's real economy expanded 5 times since 1991. The five-year average economic growth rate accelerated from 4.15% in 1991-95 to 7.9 percent in 2015-2019. As population growth rate persistently declined, the per capita GDP growth rate accelerated even faster than the economic growth rate. Over the past decade, Prime Minister Sheikh Hasina has not only delivered an extraordinary episode of economic growth, her government has also produced broad-based gains in health, education, infant mortality and life expectancy. Since 2009, Bangladesh has reduced economic vulnerabilities across many critical areas. The country thus met all three criteria to be a developing country in 2018 and was set to graduate by 2024. Whereas PM Sheikh Hasina was successfully pursuing her Vision-2021, her government was moving towards achieving a broader set of sustainable development goals (SDGs) by 2030. Then came the global coronavirus pandemic together with government policies that essentially locked down modern life, businesses included. The world economy is still facing a risk of prolonged recession. Bangladesh is no exception. Covid-19 threatened to reverse many of our critical developments of the last decade. Government of Bangladesh has been bold to address the initial phase of this unprecedented challenge.

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As early as March 2020, the Government of Bangladesh floated a series of monetary interventions in the form of "targeted lending programs" by the central bank. Collectively, those are worth $12 billion dollars. The schemes were separately designed for export-oriented businesses, large corporations, small and medium enterprises, agriculture and professionals. The schemes were meant to inject huge liquidity to households and firms so that they can navigate covid-induced disruptions and business uncertainties. Furthermore, a substantial part of the fiscal spending plan of $71 billion for 2020-21 has also been geared towards improved public health and expanded social safety net. Hon. Finance Minister, AHM Mustafa Kamal, further offered a large number of fiscal incentives to help businesses and individuals. The targeted lending programs of the central bank incorporated interest subsidies within the framework. Interest rates were mostly capped within single-digits, a public policy goal of Prime Minister Sheikh Hasina. Those stimulus schemes are in-progress and driving credit & liquidity flow to households and businesses. Bangladesh Bank has also played an accommodative monetary policy. The central bank brought down the repo rate by 125 basis points to 4% & the risk-free interest rates on T-bills by 200 basis points to 5.55%. I must argue that this monetary development happened very fast and decisive. The fundamental criteria of these lending programs should be that liquidity flows to those businesses which were otherwise profitable & solvent until 31 December 2019.

Bangladesh economy is showing early symptoms of recovery. Factories have reopened. Export production has resumed. Workers returned to factory floors. Life is returning to small businesses across the nation. Many economic fears are seemingly averted. Surprisingly, many experts predicted an unsustainable external account imbalance in 2020. That did not happen. The current account deficits stood at $4.8 billion, which was less than the previous year. The surging flow of inward remittances kept its momentum. Bangladesh earned a record $18.8 billion in the form of inward remittances in the last fiscal year. A number of innovative fiscal measures enacted by Hon. Finance Minister in 2020-21 are driving capital flow to Bangladesh. Bangladesh Bank is reporting new record of foreign exchange reserve at the end of every month during this pandemic. It is now $39.3 billion at the end of September 2020. This continued reserve accumulation further increased liquidity in the financial system. I will do a disservice if I do not explain another pillar of Bangladesh's macroeconomic sustainability.

I will safely argue that Bangladesh is better positioned than many other developing countries. The country can finance a fiscal deficit of 10-20% of its GDP over the next 18-24 months. I predict a wide range of fiscal deficits over an extended period because of uncertainty surrounding both revenue & expenditure plans of the government. Is this a critical problem for the government? The answer is no. Bangladesh's debt/GDP ratio is 35%, of which external debt is about 18% of GDP. This is considered "very low" by sovereign rating agencies. It is true that covid-19 pandemic has decimated parts of our aggregate demand. Household consumption, private sector investment, government spending, and net foreign spending on domestic goods are all depressed. Aggregate supply too is contracting for variety of reasons including nationwide lockdown, lack of labor mobility, & global supply chain disruptions. But the prudential fiscal and monetary policies of the Government, under the guidance of Hon. Prime Minister Sheikh Hasina, are leading Bangladesh to avert a prolonged economic slump and to return to growth. The critical challenge is that money & liquidity directly flow to public health system, vulnerable households, and businesses.

Before the onslaught of covid-19 pandemic in this January 2020, the entire Bangladesh was preparing for observing the Birth Centenary of the **Father of the Nation Bangabandhu Sheikh Mujibur Rahman**. Bangabandhu envisioned for a prosperous Bangladesh. His dream was to grant economic freedom to the hundreds of millions of his people. Bangabandhu was not allowed to bring about this change. On 15 August 1975, a criminal force opposed to **'Independent Bangladesh'** killed Bangabandhu and innocent members of his family. They wanted to erase Bangabandu from the minds of Bengali people. They miserably failed to achieve their goal. The rule of law prevailed and the killers were punished for their crimes against humanity. Hon. Prime Minister Sheikh Hasina, one of the surviving daughters of Bangabandhu, is now ruling the country and has devoted her life to realizing what Bangabandhu dreamt of. In her election manifesto in 2018, HPM Sheikh Hasina announced her big plan to transform Bangladesh into an upper-middle-income country by 2030. She envisioned that in order to do so, Bangladesh would require its investment-GDP ratio to increase by 10 percentage points over the next decade. She further articulated that capital market would be the platform for meeting a large part of this demand for new investments. Capital market in Bangladesh is however yet underdeveloped. The stock market capitalization was only 12 percent of GDP in 2019. It is 75 percent in India and 55 percent in Vietnam. This implies that Bangladesh will have to pursue major reforms and substantial capacity building for capital market development. Hon. Prime Minister entrusted the new Commission in this May 2020 to bring about this change in collaboration with other key regulators of the government.

The new Commission is committed to pursuing a number of capacity building initiatives, major policy reforms and enforcement actions for building a good governed, transparent, and vibrant capital market in Bangladesh. Investors have seemingly regained their trust in the market. Daily turnover in our stock exchanges surged from less than 100 crore to more than 1,000 crore over the last six months. We take no solace from this short-term development. The present Commission will collaborate with its partners and other stakeholders to achieving the long-term goal. I will briefly highlight priority areas for building a good governed, broad-based and dynamic capital market.

1. **Capacity Building of BSEC**: A long-term capacity building is underway for Bangladesh Securities and Exchange Commission (BSEC) in areas of skilled human capital, modern technologies and prudential regulations. A new organizational structure of BSEC is in-progress. The Commission is also redefining securities laws and regulations in order to ensure prudential regulations and to enforce the same for issuers, stock exchanges, and other capital market intermediaries.

2. **Governance of Primary Market:** BSEC shall act with stock exchanges and other capital market intermediaries and build a transparent, and good-governed primary market. Acts and regulations concerning public issue of debt and equity securities are being redefined so that securities are fair valued and the long-term interest of investors is protected. **Good governance and long-term solvency of issuers will comprise one central tenet of the Commission.** In this process, the role of auditor, audit firms and credit rating agencies is always critical. Their regulations and enforcement will undergo major reforms.

3. **Reducing Transaction Costs:** The operation of secondary market shall also undergo gradual but decisive reforms. **Transaction costs (broadly defined) are high in Bangladesh's capital market. A particular factor which contributed to this prohibitive cost of investing in securities is dismal functioning of margin loan market.** Margin loan market is supposed to be near risk-free and so associated with low borrowing costs. This is not the case in Bangladesh. We will closely work with stock exchanges and capital market intermediaries so that margin rules are enforced without fear and favour. A prolonged phase of depressed capital after 2010 was largely caused by excessive borrowings and non-enforcement of margin rules in time.

4. **Real-time Reporting and Transparency:** A technology platform of extensible business reporting language (XBRL) shall prove critical for transparency and accountability for stock exchanges, listed companies and other market intermediaries. Companies and capital market intermediaries can make corporate submissions real-time using XBRL platform. BSEC will invest heavily to enforce compliance by issuers and market intermediaries with International Financial Reporting Standards (IFRSs), International Standards of Auditing (ISAs) and best-practice corporate governance codes. During the 7th five-year plan period, the Government formed the Financial Reporting Council (FRC) to upgrade the accounting and auditing standards to global level. FRC is now operational and we look forward to collaborating with FRC in the enforcement of accounting and auditing standards across companies.

5. **New Markets in Bonds and Derivatives:** Government is committed to building a diversified capital market involving both bond and derivative markets so that long-term financing of business moves from banking system to the capital market. A well-functioning derivative market is indispensable for prudential risk management for the investors. An organized market for trading in options, futures and derivatives is an essential component of a modern capital market. It works like an automatic stabilizer putting downward pressure in times of bubble and a support in times of depressed pricing. Had there been a market for equity derivatives in our stock exchanges, the unsustainable bubble in 2010 and its inevitable crash would be unlikely. The Commission shall closely work with stock exchanges and other strategic partners for this important capacity building.

6. **Reviving Mutual Funds:** Households and individual savers will like to invest via professional fund managers. Mutual funds across advanced and emerging economies play a pivotal role to this end. Mutual funds in Bangladesh are far from this standard. The Commission is deeply engaged with Asset Management Companies to redefine mutual fund regulations so that their investment risk management and reporting regime undergo major changes. We are committed to ensuring unfettered liquidity of mutual funds, low risk, transparency, and sustainable returns to unit holders.

7. **Technological Upgrading of Stock Exchanges:** The Government will improve the surveillance software/systems to prevent manipulative transactions in capital market securities and to ensure greater transparency. To this end, BSEC will guide stock exchanges in upgrading their trading platforms, order management system (OMS) and a dynamic real-time trade settlement infrastructure. Our stock exchanges are expected to undergo serious

governance reforms and substantial capacity building in their management. No stock regulator can prove effective unless stock exchanges are technologically competitive, endowed with efficient human capital and its management is effectively separate from the boards. We will keep pursuing the actual goal of demutualization. These are long-term challenges to be overcome.

8. **Enhanced Supervision and Enforcement of Securities Laws:** Inquiry, supervision and enforcement of securities laws will comprise a critical capacity building for BSEC and stock exchanges. The new organogram of BSEC has made provisions for new human capital and other resources to deliver these core functions. Securities laws are also continuously evolving to make a big difference to this end. Regulators will take measures to ensure that companies comply with corporate governance code, and financial reporting and disclosure rules. Strict accountability will be enforced in cases where companies fail to comply with securities laws, corporate governance code, and reporting standards.

9. **Prudential Monetary and Fiscal Policies:** Monetary policies, interest rates, and tax policies do directly affect corporate cash flows and hence market price of securities listed in stock exchanges. Interest rates, stock market liquidity and portfolio rebalancing are deeply interdependent. Any change in monetary policy will affect all these outcomes and so capital market stability. Tax laws are undeniably important for capital market. The Government will improve the tax incentives further for the private sector companies to become listed with stock exchanges and to commit to enhanced transparency and accountability. An option to go for listing shall have to be made attractive for an issuer of capital and tax policies will be geared to this end. Hon. Finance Minister is deeply committed for a transition from the current bank-based borrowing to capital market-based financing.

10. **Inter-organizational Coordination:** Continuous coordination is needed between key regulators including Bangladesh Securities and Exchange Commission, Bangladesh Bank and National Board of Revenue (NBR) for a good-governed capital market. The Government may consider an institutional mechanism to facilitate this coordination between NBR, Bangladesh Bank and BSEC for building a modern capital market.

11. **Financial Literacy for Investors:** Financial literacy is very low in Bangladesh. Bangladesh Academy of Securities Market (BASM) and Bangladesh Institute of Capital Market (BICM) are two institutes of the Government to enhance financial literacy in Bangladesh. The Government is committed to investing in both the institutes and making them effective for financial literacy.

Capital market is complex, forward-looking, behaviorally sensitive, and strongly interdependent with monetary and fiscal policies. The future of Bangladesh's development will critically depend on how the burgeoning demand for new investments is met. The traditional bank-based borrowing is incompatible with this goal. In order for Bangladesh to transition to an upper-middle income country, a good governed, transparent and relatively efficient capital market will prove pivotal. We are committed to achieving this goal.

Thank you very much. Joy Bangla. Joy Bangabandhu. Long Live Bangladesh!