The Banking Sector in Disarray

by Tarek Rashid

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THE controversy over the Bangladesh Commerce and Investment Ltd (BCI) has raised various questions in the public mind regarding the existence, authority and future of privately managed financial institutions of the country. What went wrong, who is to blame for this, what is the future of banking and financial institutions in the country ? All this are important questions.

Generally, the BCI, as an investment company, has been defined by the Bangladesh Bank as a non-banking financial institution. While authorising in 1985, the central bank acted in the light of the Security and Exchange ordinance 1969 and the Bangladesh Bank Order 1972. It functions of were defined as (1) making advances or loans either from equity or by borrowing within the country or by syndication of foreign exchange loan, (2) purchase and sale of shares, stocks and debentures etc, (3) underwriting stocks and shares etc, (4) undertaking technical economic and financial feasibility studies of the projects on behalf of its clients, (5) providing managerial, technical, administrative personnel and services, (6) hire purchase transactions or financing of such transactions through lease or otherwise.

The Bangladesh Bank categorically stated that the investment companies like BCI and NCL (a) would not be allowed to accept any deposits, (b) would not be allowed to handle L/C business or wage earners' remittance, (c) would not open investors' account or issue unit trust.

Since they are not allowed to accept any customers' deposit, as the banking institutions do, it was stipulated that they should have a minimum authorised capital of Tk 15 crore out of which Tk 10 crore should be paid up. This was done to give adequate leverage to loan operations as well as maintenance of liquidity.

These investment companies, however, failed to maintain their operational and ethical standard in a limited investment and financial market like Bangladesh .

The BCI and NCL were offering better rates on deposits, at least two to three per cent higher than what was offered by the commercial banks. While banks were offering 12 per cent on term deposits, BCI and NCL were offering 14 to 15 per cent. They could only do that since they are not required to maintain any cash and security deposit with the Bangladesh Bank's statutory deposits, while commercial banks are required to maintain 21 per cent to 25 per cent cash and security deposit. So the cost of fund for a term deposit accepted at the rate of 12 per cent is around 14.5 per cent for the commercial banks while BCI's or NCL's fund was costing the face value of interest rate offered. That gave them the highest leverage. Moreover, instead of going to agriculture and industrial sectors, they were mostly investing in the trading portfolios with higher rate of interest as well as risk. So their earning gave them a more or less sound footing in the market. But they were not going as per the terms of the Bangladesh Bank. They were accepting deposit, investing in shares, stocks and so on. Bangladesh Bank in its intensive inspection on the operations of the investment companies detected gross irregularities and warned them to abide by the guidelines. It was observed by the Bangladesh Bank and Ministry of Finance that the NCL was gradually improving while BCI was not. It was decided at a meeting at the Ministry of Finance in April 89 that the Bangladesh Bank shall prepare a report on the 'above institutions and measures to be taken for the irregularities.

But nothing was done. The BCI continued with its irregularities. Out of Taka 190 crore deposit, Tk 180 crore was lent out, mostly among the directors. That pushed BCI to a tight liquidity position. They failed to meet the day-to-day requirement of their depositors (lenders, as defined by the Bangladesh Bank). Moreover, due to lack of security documentation and weak credit administration, a large portion of its loans were heading towards bad debt or awaiting decision in the court. Excessive profit motive and milching of money did not allow them to do a little bit homework to ensure smooth running in future; rather prompted other investment companies to come up with an intention to earn quick profit. They failed to understand the difference between trading and banking. The Bangladesh Bank or the concerned ministry also did not ask them for required homework or give them adequate guidance for strengthening their position as expected.

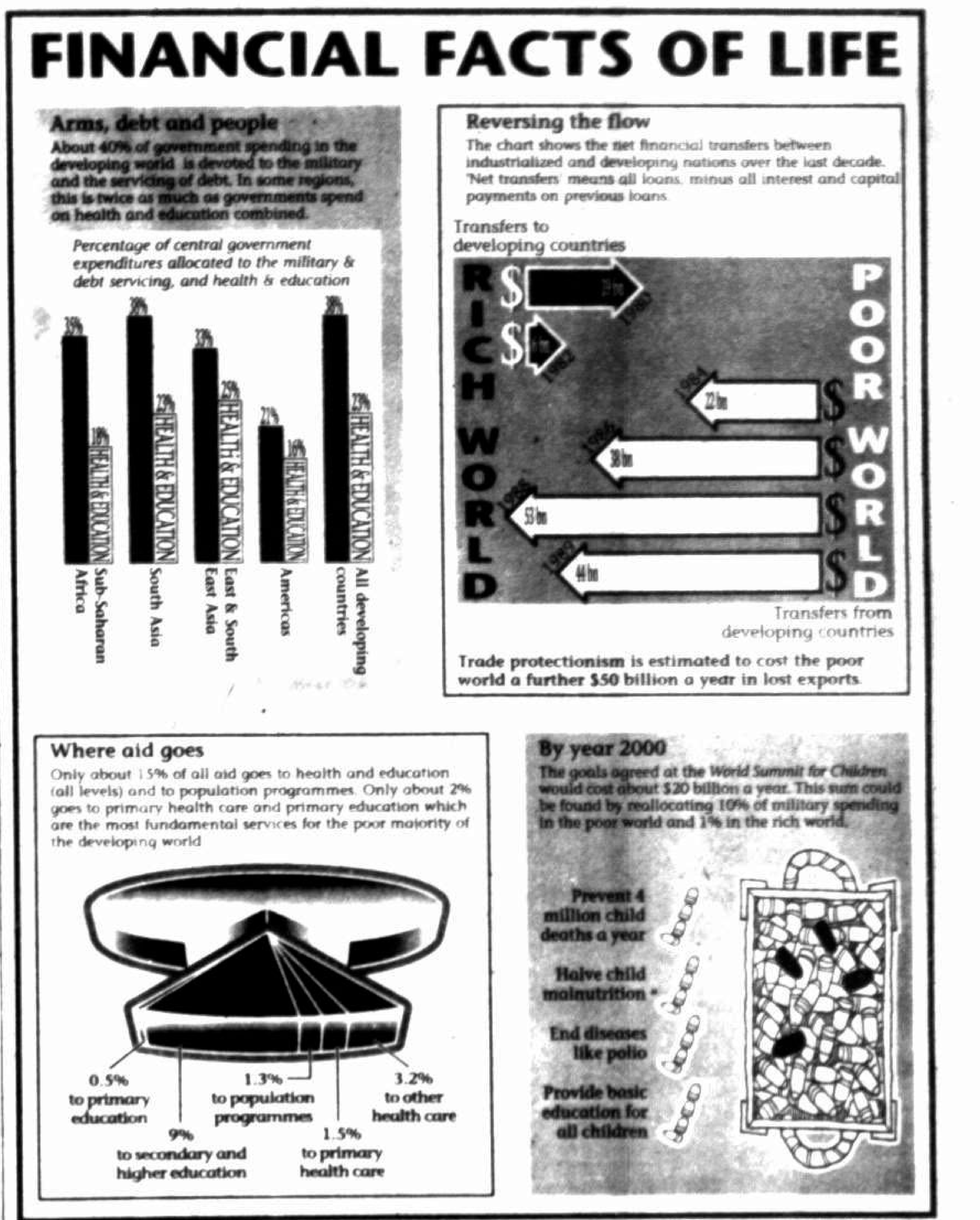
The suspension of operations of BCI, the issuance of warrants against its directors, decision to audit the accounts of the branches are all long overdue moves to have been taken by our central bank. The delay in taking these moves — due one year before as confirmed by a Bangladesh Bank source has greatly damaged the reputation of the central bank and raised new doubts about the credibility of the banking system in the country as well as created a fresh shock among the clients of our banks and financial institutions.

Are more such disasters coming? —the question inevitably follows.

One feels and firmly believes that the situation could easily be avoided by the concerned authorities. Nobody is ready to accept that our central bank was not aware of the situation. It is now revealed that the Bangladesh Bank authorities reprimanded but not served serious warnings in order to stop the said investment companies from illegal activities. There are reasons to believe that the central bank's signal is more too gentle to have any effect on the operations and motive of these institutions. Observers are reluctant to believe that there was any political pressure in taking serious steps against these institutions, specially BCI. The concerned ministry, i e, Ministry of Finance also cannot avoid its share of responsility in the debacle. Reports confirm its inability to judge the situation and pass on necessary instruction in time to Bangladesh Bank. Bureaucratic redtapism as well as our institutional drawbacks to adjust to the changed situation and on-the-spot decision has again been proved. Since the central bank is preparing report on the activities and crunch in BCI, it is expected that the report will cover the activities of other deposit taking investment companies and its future course of action in averting such a situation. All that is required now is a diagnosis of the crisis as well as homework on the part of the central bank. Homework also needs to be done by all other financial institutions.

The commercial banks as well as other financial institutions, specially the private ones have gone into free-style exercise in the absence of monitoring of credit operation. Before enacting the Banking Companies Ordinance 1991, they were very much crippled in the hands of the sponsoring directors. The situation has now begun to change. Bankers now have to improve the performance of the banks. Now they have to be cautious about the quality of their portfolios, liabilities and asset management. In a country like Bangladesh, where there is excess liquidity in the financial sector, an investment company or a bank was not at all expected to fail in meeting customer liabilities if they were little concerned about liquidity and gap management. In the entire cycle of activities from attracting and maintenance of deposits, paying interests to depositors, making advances to commercial and industrial ventures, supervision of the business or project in the use of loan and repayment of loans plus interest there of, concerned persons should practice to work within rules and bindings. Creativity and new thoughts are of course not contradictory to rules and regulations. Banks run or trust and goodwill. If they fail to create confidence among the clients, everything is lost. A disruption in confidence has already occurred in the case of BCCI all over and here in Bangladesh. Then came the BCI debacle. So no more. No one should be allowed to undermine the trust in Banking.

The central bank as well as the Ministry of Finance should understand that the publication of a defaulters' list, routine inspection and withdrawing the ceiling on rate of interest in lending will not improve the investment scenario of a problem -ridden country like Bangladesh. Little more is required for controlling the standard of credit, realisations of debts as well as ensuring the availability of deposits and advances. Only the role of a watch-dog is not adequate. The central bank and the ministry should also share and feel the pain of a financial sector undergoing transition and a development process.



Artwork by Stephen Hawking

Reichmann Landed in $20 Billion Debt

by Allan Thompson

In many parts of the western world tycoons are in deep trouble. None more so than the Reichmann brothers of Canada, who own large chunks of New York, Toronto and London. Their empire is in debt to the tune of $20 billion and a massive development in London has been thrown into crisis. Gemini News Service examines why this came about.

ONE of the world's biggest financial empires is in crisis. Olympia and York Development, a real estate and natural resources conglomerate owned by the Reichmann family, is trying to restructure $20 billion in debts it cannot pay.

The empire, known as O&Y, is based in Toronto, Canada's financial capital. It owns most of the gigantic office towers in that city's financial district, and is the biggest landlord in New York as well.

Its most massive project is a $7 billion office complex in the old docklands of East London. The project, called Canary Wharf, is the biggest in Europe and has so far cost the company $3.5 billion.

Now many are asking how what was once considered one of the strongest companies in the world got into so much trouble.

After months of rumours, O&Y finally admitted in late March it could not pay its debts. Family member Paul Reichmann, long considered chief company strategist, was replaced as President by a New York banker brought in to oversee the debt restructuring which will involve dozens of banks around the world.

How did it all happen? "Nobody is impervious to the times," said Edward Minskoff, the New York real estate entrepreneur who worked with the Reichmanns for many years. "The international real estate industry is a victim of this decline ... and because of their size, they are, on a much larger scale, no different than most other people."

The Reichmanns were supposed to be different. Their story is legendary. The Vienna-born brothers — Paul, 63, Albert, 61, and Ralph, 58 — emigrated to Canada in the Fifties from the international city of Tangier, where their family had ended up in the Forties after moving across Europe just ahead of the Nazis.

The tile-importing business they started in Toronto branched into real estate when the brothers discovered they could put up a warehouse for much less than any of the builders they had approached.

Their first big success — turning 500 acres of farmland on the Toronto outskirts into a sprawling office park in 1965 — followed the pattern that would become their trademark : buy land when it is cheap, build big, high-quality buildings that others could not or would not dare, and do it quicker than anyone else.

In the next decade the Reichmanns built a property empire in Toronto and Ottawa and in 1974, started work on First Canadian Place, at 72 storeys, the tallest office building in the Commonwealth.

While others had not figured out whether First Canadian Place was a good thing, the Reichmanns plunged into the United States market, buying eight Manhattan Skyscrapers at a time when New York was teetering on Bankruptcy.

New York turned around and the buildings they paid $320 million for were soon worth more than $1 billion and saw their rent revenues quadruple. It was dubbed the deal of the century.

Later they took the contract to develop Battery Park, a run-down corner of lower Manhattan on which they proposed a staggering eight-million-square-foot complex of office towers to be called the World Financial Center.

Along the way the Reichmanns had begun diversifying their millions in property earnings, buying control of Canada's newsprint and paper giant Abitibi-Price in 1981 and Gulf Canada oil and gas company in 1985.

Heading into the Nineties, estimates of the value of their intensely-private conglomerate ranged from $10-$30 billion. They were building Europe's biggest commercial complex at Canary Wharf, owned 50 million square feet of office space on two continents, controlled the world's biggest paper company, had a stock portfolio worth $ 6 billion and employed thousands of people.

Behind the sprawling empire were the brothers — dour, devout, Orthodox Jews who shunned the limelight with as much vigour as others of their stature sought it.

At the centre was the tall, stooping figure of Paul Reichmann, considered the chief strategist and brilliant, soft-spoken wonder kid of real estate, so much the apex of authority at O&Y that Canadian business author Peter Foster compared him to the Wizard of Oz, behind the curtain at the end of the yellow brick road.

So what happened? Among other things, Canary Wharf happened. The $7.5 billion, 71-acre project is a city-within-a-city being built on the Isle of Dogs in East London. With 10 buildings — one of them the tallest in Europe — and 5.5 million square feet of office space in its first phase alone, Canary Wharf was part of prime minister Margaret Thathcer's grand scheme to revitalise London's derelict docklands.

The Reichmanns came on board in 1987 and took over Canary Wharf. It is miles from London's financial district, but the land was cheap and its buildings, while of far superior quality to anything available in London, offered lower rents.

Transportation links to the isolated docklands are weak but will improve in January when a tunnel-road connection comes through and in 1996 with the proposed extension of London's subway system to Canary.

But the $3.5 billion the Reichmann's have sunk into Canary has been compounded by the most severe downturn ever in the British property market. Canary, while visionary, has become a cash drain.

Roger Parsons, of the docklands office of leasing agent Knight Frank and Rutley in London, says : "It's a stunning scheme and it will succeed. The question is if O&Y will be there to enjoy it."

O&Y called its situation a "liquidity crisis," that began to unfold in mid-February when a major bond rating service in Canada downgraded its opinion of some of O&Y's short-term loans. Investors stampeded to cash in their loans because they had lost confidence in O&Y.

Forced to come up with hundreds of millions of dollars to pay out a failed borrowing programme, the company could no longer keep up with its debt payments and had to admit it. It brought in New York banker Thomas Johnson as president to head the restructuring.

The real estate downturn and the general recession in North America and Britain had been taking its toll since the late Eighties. Like many successful builders O&Y borrows heavily against the value of its properties to raise money for other projects.

Canary Wharf, while 60 per cent full, was taking much longer to fill than anticipated, and was not providing enough cash to cover its debts.

With falling rents, the same was happening in New York and Toronto. Many of O&Y's prestigious buildings are partially empty. And an innovative O&Y technique for attracting new tenants to its projects could also be proving dear in a slump : to get American Express into the World Financial Centre, O&Y bought its old office.

To lure the Daily Telegraph to Canary Wharf O&Y bought the newspaper's hulking headquarters across the river, and now must lease it out in the worst market ever. It has also taken over many of its clients' leases over the years to get them into new buildings.

To add to the cash crunch, Paul Reichmann's dream of building a resource empire had failed. His companies Abitibi and Gulf Canada have been losing millions.

Experts disagree on how much trouble the company is in. Certainly enough to make the Bank of Canada and Bank of England scramble to help find emergency loans. Enough to prompt Canadian finance Minister Don Mazankowski to say the government would help to stabilise the situation, if necessary, by providing loan guarantees to O&Y. But not enough to sink them, analysts say.

"It think everything is probably exaggerated, it's not as bad as it seems," say one financial analyst who would not be named.

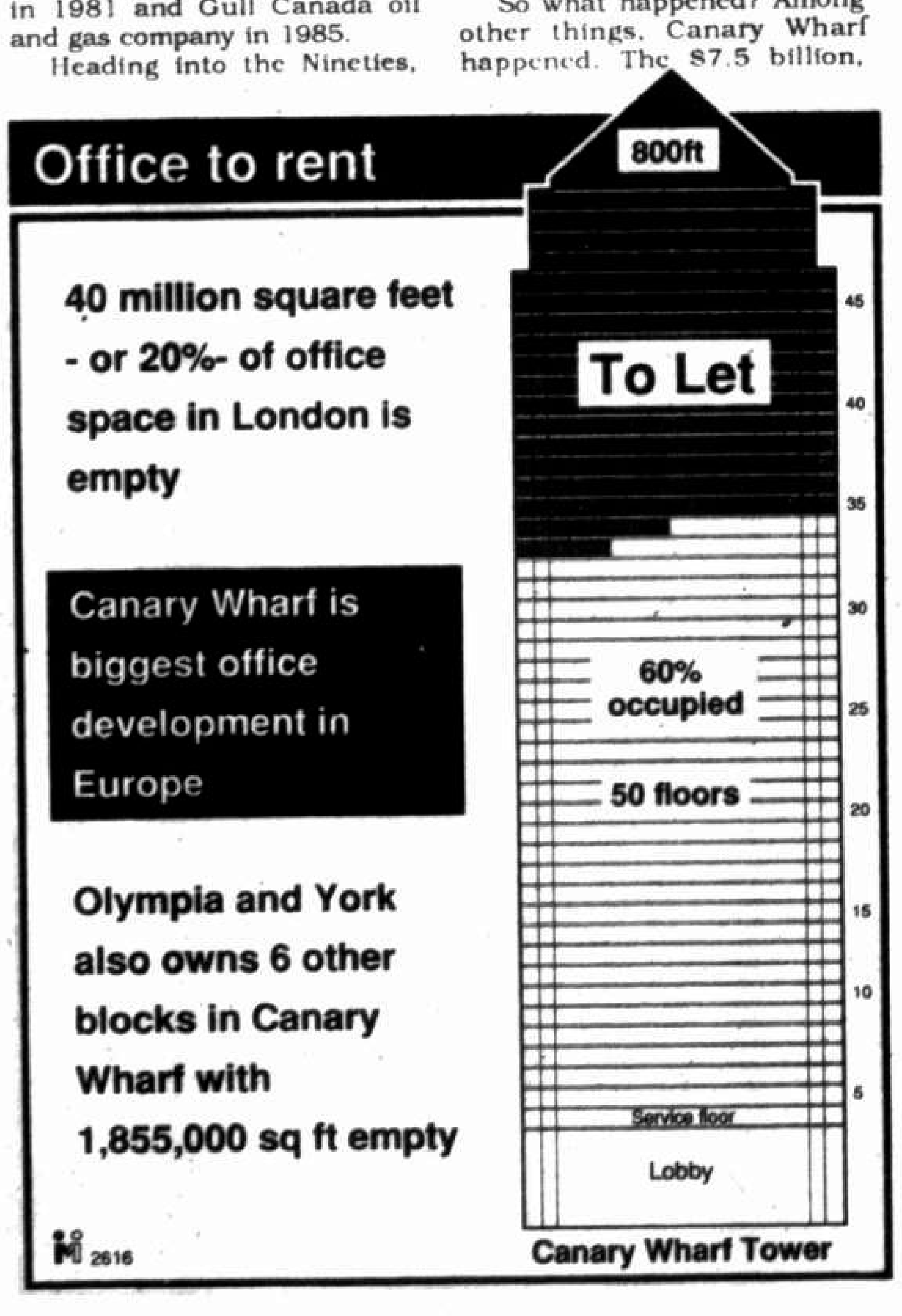
Former associate Minskoff said: "The media have been looking for 10 years to try to find an excuse to write negative articles about O&Y. Most of the real estate they own is in good locations and of good quality — sand as Mark Twain said, 'they ain't making the stuff anymore.'"

British analyst Soames said : "One can't afford to let them go down because the ramifications of that would be enormous."

Most likely O&Y will restructure its debts with banking partners who have as much to lose as it does in the event of failure, borrow more money and delay debt payments until the office buildings start bringing in more cash.

But the company's cherished name, and the reputation of its owners for financial wizardry, will be forever tarnished. — Gemini News

Allan Thompson is on the staff of the Toronto Star. He held the Gemini Fellowship from IDRC Canada for 1990-91. In 1991 he spent five months in North Africa and frequently visits Lebanon.



New Zealand Woos Asian Investors

by Derek Round

NEW ZEALAND, which admits it is well behind neighbouring Australian in attracting investment from Asian has sent two senior cabinet ministers to Asian countries in a bid to woo investors there.

Finance Minister Ruth Richardson went to Singapore, Hong Kong, South Korea and Japan, while Trade Negotiations Minister Philip Burdon visited Southeast Asian capitals.

Members of a 14-member private sector mission travelling with Miss Richardson also visited Taiwan which,does not have diplomatic relations with New Zealand.

"Our objective quite simply is to foster greater awareness of opportunities for investment in New Zealand," Ms Richardson says.

New Zealand has no investment promotion board and business organisations have for long complained that there was no body responsible for seeking investment from overseas. The country's Overseas Investment Commission is only a regulatory body with no responsibility for actively seeking foreign investment.

The influential Japan-New Zealand Business Council, which includes top business leaders and bankers, has been urging the government to do more to help bring in badly-needed investment capital.

Prime Minister Jim Bolger has appointed a foreign direct investment advisory committee headed by Andrew Meehan, a young merchant banker who had chaired the Japan-New Zealand Business Council's investment task force which reported on the lack of foreign investment two years ago.

The government has also adopted the task force's recommendation to appoint an investment counsellor at the New Zealand Embassy in Tokyo, the first time one has been appointed to any New Zealand diplomatic post. Philip Ashenden, 48, who has been Japan adviser to Fletcher Challenge, New Zealand's biggest public company, was picked for the job. He speaks Japanese.

Mr Ashenden has noted that Japanese investment was US $274 a head of population in Australia but just US $31 in New Zealand. "We're not getting our fair share of that capital flow," he said.

Japan's Ambassador to New Zealand, Takeo Iguchi, has proposed an investment pact between the two countries similar to the Nara Treaty with Australia signed in 1977.

Australia has since become Japan's second largest foreign investment destination after the United Stats. New Zealand and Japanese officials are now studying Ambassador Iguchi's proposal.

Japanese investors have become more cautious, according to businessman Susumu Naito, president of appliance manufacturer Rinnai Corporation which has a subsidiary in New Zealand.

"For the last few years there has been the so-called bubble economy and a lot of spare cash floating around Japan," he says. "I think we are now at the stage of the deflation of that bubble phenomenon. Japanese investors are essentially going to be much more cautious about which investments they get involved in, but that's not necessarily a bad thing."

Countries like New Zealand seeking foreign investment in sound, well-researched proposals would not be affected, Mr Naito said.

But a recent confidential survey of foreign investors by the New Zealand Forest Industries Council found New Zealand is still seen as suffering from "cultural immaturity."

Foreign investors still believe New Zealanders think locally rather than globally. Investors see the country negatively in terms of size, location and labour conditions, according to the survey.

The New Zealand government's case is that, with only 1 per cent inflation, deregulation and privatisation sweeping port and industrial reforms, liberal foreign investment rules, extensive forest resources and a big potential for the growth of tourism, the country is an attractive place to invest.

Mr Ashenden says some governments offer tax breaks and other incentives for Japanese companies.

Where New Zealand could provide investment potential was in forestry, horti-culture, pastoral farming, tourism and selected manufacturing industries; all areas where potential advantage was being heightened by low domestic inflation and greater efficiency in ports and other service industries.

It is this message that New Zealand ministers and business leaders are seeking to get through to Asian investors.

— Depthnews Asia.

More Than DM 30 Billion Spent On Welfare Assistance

MORE and more people are becoming dependant on welfare assistance. In western Germany, 1990 saw expenditure on welfare assistance pass the DM 30 billion mark for the first time, which was around ten times higher than the annual outlay 20 years earlier.

Over the same period, the number of recipients rose from 1.5 to 4 million, although the figures include people who only received short-term support.

For may of the needy, welfare assistance has increasingly become vital for survival.

The grounds for entitlement to welfare assistance are long-term unemployment or an inadequate pension; mothers bringing up children on their own are also looked after by welfare offices, as are people who need nursing care but cannot afford a place in a nursing home.

— (INP/GLOBUS)