

## Post-cyclone Needs

As clearer pictures of the devastation wrought by last week's cyclone emerge, we are becoming increasingly convinced that loss of lives has indeed been minimal, though not negligible where human lives were involved. But the loss to properties has been beyond description. Now in the aftermath of the cataclysmic visitation, the victims are naturally exposed to nature's elements. Their homes and hearths destroyed, most people of the affected areas are in need of immediate help at this time of their distress. The government relief efforts, by all indications, have not yet been able to reach succour to the cyclone-affected people everywhere and sufficiently.

After an initial assessment of the damages, the government has made its position known: that it does not want to seek foreign help but if any country volunteers to give assistance, the same will be accepted with thanks. This can be interpreted as the administration's capacity to handle the situation on its own. We have no doubt about its ability to do the job. But what we would like to point out is that an emergency situation such as this calls for mobilising all the resources of the country for the relief effort.

We are noticing with dismay that political divide has started between the ruling party and the opposition over the respective merits of their handling situations, the BNP government during the 1991 cyclone and the AL government now. We think what is primarily at issue is the plight of the victims which needs to be attended to without any distraction whatsoever. The opposition may point out the government lapses in relief distribution and at the same time the government could have its own version; but the overall attitude on both sides should be to help matters, not enter onto a political duel. Dangers of cataclysmic proportion should at least remove the political divide for sometime. Why not stand by the victims together by conducting an integrated relief operation?

If the government and the opposition work together to help the victims, a lot of benefit will accrue. First, they can plan to provide the affected people with the first thing first and coordinate in the rehabilitation work and medical programmes to get the best result possible under the situation.

## CJ's Remarks

Chief Justice ATM Afzal has minced no words in expressing his dismay over the performance of subjudges and assistant sessions judges while awarding certificates to them on Friday at the end of a training programme they had attended.

Coming from a person who is at the apex of a justice system his diagnostic remarks about where things are going wrong at the lower tiers must be deemed to be of great meaning, authenticity and force by all concerned.

And that he has shared these with us in a forthright manner will only help increase public confidence in the highest judiciary which is manifestly initiating a process of introspection among the subjudges and assistant sessions judges.

The honourable Chief Justice has given us a gem of a quote to this effect: you do not need tall talks like rule of law, independence of judiciary and enforcement of human rights ... all such good words would be automatically implemented if everyone discharges his duty properly. The emphasis is clearly on sincerity, application and hard work, sterling qualities that can help accomplish many things in spite of all the limitations and constraints one is wont to cite when faced with criticism.

He has asked the junior judges to speed up disposal of cases at a rate of more than six in a month, ensure the quality of judgements that sometimes land on the doorsteps of the higher courts and contain the appetite for posting to Dhaka ignoring the need for judicial work in the outlying areas.

The ends of justice will never be truly served so long as these pitfalls are not avoided.

## Rural Infrastructure

Many people who have been to the interior tend to marvel at the shiny road stretches that today criss-cross Bangladesh, little realising that sordid tales lie buried under the lustre and silken smoothness of the bituminous exterior. The network could be still better in terms of mileage and uniformity in quality.

We have an authentic view on the subject from no less a quarter than the World Bank itself, the horse's mouth, as it were, from whom we regularly receive funds for rural infrastructure development. A WB study report reveals with a startling effect on the gullible who were going gaga over the picturesque thoroughfares that a yawning gap exists between the infrastructure development planned and the physical targets actually met over the '85-95 decade. The achievement falls short by as much as 61 per cent. Imagine how much more spectacular the infrastructural picture would have been with the missing networks of roads and markets in place! We have today 8,400 kilometres of feeder roads and 78 thousand kilometres of rural roads making up a rural road system that has about 'one gap' in every two kilometres which is technically regarded as an impediment to rural mobility.

The World Bank visualises, the total financial requirement for maintenance and development works at Tk 12,660 crore over the next ten years. Bangladesh needs raising a greater proportion of internal resources for the purpose than before, although the World Bank is expected to be forthcoming on this having research-based knowledge on the subject.

Equally important is the quality aspect of the roads coming up. It is often said that where local contractors were used the work has been sloppy. This has to be borne in mind with an overall stress laid on the standards of roads being planned.

# Twilight of the Stock Price Debacle in Bangladesh

by Dr. M Farid Ahmed

*It is possible that a temporary supply of ordemand for an extraordinary large amount of securities takes place sometimes. This may upset the balance between demand and supply. In order to stabilise the market, it is necessary to conduct some price supporting activities. Such activities are specially needed when the market is dominated by speculation and rumour.*

STOCK prices, in general, are determined by the interaction of demand and supply. Stock differs from other consumer goods to the extent that stock itself can't directly be consumed like other consumer goods rather the income generated by it can be used for consumption purposes. Accordingly, determination of a stock price may be governed by the volume of net assets it holds. However, in spite of its considerable bearing on the price of a stock, net assets are, in a sense, the liquidation value of the enterprise and thereby not considered most suitable measure for a going concern. Basically, the most important aspect in the stock price mechanism is the amount of earning the investor's earning the investor's money will realise in a certain period. This is usually related to the dividend rate which can play a crucial role behind demand and supply relationship and thereby price formation.

An anticipated future dividend is subject to uncertainties and influenced by many economic and non-economic factors. Fluctuations in security prices are the function of a variety of factors. Interest rates, industrial production, commodity prices, savings, investments, population, employment, political and economic developments, technological changes, corporate profits, earnings or dividends, investors' feelings etc. are the prominent ones that can influence stock prices. As a result, many indeterminate factors come into play to complicate the pricing mechanism.

### Stock Trading

Stock exchange is the legal platform for trading in the secondary market. Trading is conducted by the broker-members of the stock exchanges in Bangladesh. An investor can associate himself with the stock exchange trading only through a broker whom he can approach to execute his buy or sell order. DSE brokers are allegedly taking unnecessary long time to execute the order which often goes against the interest of the investor. In order to execute an order to buy or sell securities on behalf of his client, a broker is supposed to provide services at the time of executing a sell order as well as provide services and funds for a buy order. He charges a commission for such services which is 1 percent of the total value of the transaction. Thus, the stock markets in Bangladesh predominantly operate through

the agents without any responsible market makers. The members of the DSE do not operate margin accounts for general investors. There is no provision in Bye-laws of the Exchange for undertaking market making roles.

While the stock exchange brokers must carry out trading of the listed stocks on the floor of the exchange in principle, off-floor-transactions are carried out through a kerb market in Bangladesh, notably during recent times. Trading of shares during floor trading hours as well as beyond trading hours is conducted among large number of interested investors assembled outside the stock exchange. Transactions are usually conducted through physical delivery of share certificates in the kerb market. Very often transactions take place at a distorted price. Fraudulent practices entrap people through trading on the false certificates have become a regular phenomenon in the country's kerb market centering the DSE. The unregulated kerb market has exacerbated the stock market manipulation and inflicted extensive damage to the market. Such unrecognised markets, if not guided properly, might have negative impacts on sound development of stock markets.

The market operates through an open outcry with broker-members seated around a table with no access to outsiders. Dealing prices are recorded with a chalk on a blackboard by a member of the stock exchange staff. By the standards of large stock exchanges in developed countries, the technology is simple and not subject to technological failure. For a market of this size, the trading arrangements can, by and large, serve the purpose. However, in view of the growing size of the market, frequent allegations about the market manipulation, and recent upsurges followed by sharp downswings credibility of the system as a whole has been brought into question. Computerisation of the trading system and introduction of a central depository system (CDS) can bring improvement of the situation.

Under central depository system for securities, transac-

tions in securities are cleared on books merely by entering such transactions in the accounts concerned, with the stock certificates held in custody by a certain agency, instead of physically delivering them after each transaction.

Since this system offers the advantages of rationalising depository and delivery of large number of securities as well as preventing possible loss or misplacement, it has been in use now a days in many countries. Physical delivery of share certificates is not permitted under CDS. Consequently, people will be discouraged to go to the kerb market and thereby it may reduce the dominance of this market. It is true that computerisation has proved efficiency, accuracy and speed of trading in many markets. But liquidity of the market may suffer from entire computerisation. Order flows are generated, although at least partially, by subtle interactions of human activities on the floor, including behaviour of the rivals, floor atmosphere, floor gossips and so on, all of which can hardly be held by computer. That means prices might be 'overshooting' or undershooting if traders are just reacting to price moves on the screen without well understanding the reasons behind such moves.

This may result in rather market volatility due to lack of exchange of information among the traders. The system, therefore, needs to combine the advantages of the technology — efficiency, accuracy and speed — with those of human interaction, visibility and information exchangeability on the trading floor so that maximisation of liquidity and better market coordination can take place.

### Recent Price Swings

In the history of Bangladesh stock markets the most significant event occurred in 1996 when the market behaved irrationally. In DSE all share price index rose from 770 in January 1996 to about 3,700 points in the first week of November of the same year. But it plunged to 2,261.47 points on 29 December 1996 and again to less than 900 in April 1997. This abnormal price swings have taken place

ignoring all micro- and macro-economic fundamentals. The price of shares of a company, having negative worth, increased three to four times. Even share price of a closed company also increased. The abnormal rise in share prices created an urge for mindless gambling among the various segments of people. Some people took the situation to become rich overnight. Suddenly the market started experiencing nightmares as the overpriced share market began sliding toward its rational level every day and subsequently crashed.

The alarming fluctuation created a serious tension among investors. It is difficult to segregate any single factor responsible for this price upheaval rather a combination of some factors including some policy issues might have contributed to such development. The likely candidates that might have some bearing on it are price manipulation on the exchange, lack of proper implementation of a circuit breaker, withdrawal of lock-in system, absence of institutional traders on the exchange, lack of aggressive campaigning about economic fundamentals and its grave consequences and the like.

Fluctuation in equity price is a usual phenomenon throughout the world. It is possible that a temporary supply of demand for an extraordinary large amount of securities takes place sometimes. This may upset the balance between demand and supply. In order to stabilise the market, it is necessary to conduct some price supporting activities. Such activities are specially needed when the market is dominated by speculation and rumor. A circuit breaker implying a price limit and trading halt may work to stabilise the market especially when investors behave rather irrationally. The concept of a circuit breaker is not a new one.

Yet it is one of the most controversial issues among all financial discussions. In the final analysis it is explained as a trade off between financial efficiency and stability. When one emphasizes financial efficiency, he must do it at the cost of more systematic instability.

ties.

Similarly, when one emphasises financial stability, he must do it at the cost of more competitive inefficiencies. The choice will depend upon the circumstances in which the market is situated and eventually upon the value judgment of a society. It is found in many countries in some form or the other and the rules are framed according to their respective needs. Advocates of efficiency objective contend that a circuit breaker would unduly delay price discovery, injure the investors forcing them to accept incorrect prices anticipating trading halt. It is also argued that it causes deprivation of hedgers from market use when it is most needed. On the contrary, opponents argue for effectively limiting financial risks and hence systematic instability in critical times. They also contend that it may even facilitate price discovery by providing a 'time-out' during which counter orders can be generated.

Bangladesh's market is relatively small even if it is compared with other emerging markets of South Asia. The presence of foreign portfolio managers with their huge fund can easily create an imbalance between demand and supply. This is needless to say that they will try to manipulate price with their profit motive. In view of the market condition of Bangladesh, financial stability needs to be supported by the authorities concerned and hence a circuit breaker may be of help if executed effectively.

Similarly, when one emphasises financial stability, he must do it at the cost of more competitive inefficiencies. The choice will depend upon the circumstances in which the market is situated and eventually upon the value judgment of a society. It is found in many countries in some form or the other and the rules are framed according to their respective needs. Advocates of efficiency objective contend that a circuit breaker would unduly delay price discovery, injure the investors forcing them to accept incorrect prices anticipating trading halt. It is also argued that it causes deprivation of hedgers from market use when it is most needed. On the contrary, opponents argue for effectively limiting financial risks and hence systematic instability in critical times. They also contend that it may even facilitate price discovery by providing a 'time-out' during which counter orders can be generated.

Anyway, securities markets provide investors a means to trade freely and timely, issuers to raise funds cheaply and smoothly and the economy to allocate resources efficiently. But the securities markets in Bangladesh have not yet developed to accomplish these functions at a desired level. Institutional structure has also been suffering from various limitations. Lack of professionalism, alleged oligarchy among the exchange brokers, weak legal framework and execution thereof have significant impact on securities market development. Price manipulation and other market abuses like insider trading, underhand dealing and the like are likely to stem from such situations. The efforts need to be directed toward eliminating these weaknesses of the market. The authorities concerned should continue their efforts to such areas like broadening the active membership of the exchange, ensuring fairness and transparency, enhancing professionalism, increasing the number of securities listed, integrity, stability and liquidity of the market and so on.

The writer is a Professor of Finance at Nagasaki University, Japan

## For Ensuring Transparency in Corporate Income Taxation System

by Mushtaq Ahmed

*In certain situations and for making tax assessments and their finalisation easy, transparent and quick, our tax laws in 1990 provided a very convenient method at the disposal of our tax assessing officers.*

As our country's next budget is being formulated and the changes to our tax laws are being conceptualised, discussed and given shape, I put forward two issues which are very important and which, in my view, demand immediate attention of our respected tax law makers.

**1. The urgent need of provision for bad loans for the sake of financial health of our banks: Bangladesh Bank's strict mandate for making provision versus the diametrically opposite damper applied against such provision by Income Tax Department**

The stark injustices meted out to our banks unabatedly continue — not to speak of the one more effective step of trying to make our already cumbersome tax laws more non-transparent by our successive finance ministers and our distinguished finance secretaries and executives and officials at the helm of the National Board of Revenue. I have personally dwelt at this particular issue many times and at many forums, although without any luck so far. But since this issue continues to come back to me with a consistent repetition in my professional practice, I feel not inclined to give up in the interest of natural justice and fair play in the realms of taxation and framing of our tax laws. Let me make one more attempt to explain the situation.

Prior to passage of June 1990 budget all provisions for bad loans made in the books of account of banks were summarily disallowed for tax assessment purposes. One can see how big a disincentive it was for the banks in accounting their known loan losses as an expense and at the same time a boon for inflating both their profits and the loan portfolios with all their inherent ramifications. In the June 1990 budget this disincentive was removed from our tax laws and a tax deduction for provision for bad loans was made available to the banks up to a maximum of 4% (increased to 5 per cent in 1994) of total outstanding loans including all interests under clause (xviii) of section 29 of the Income Tax Ordinance 1984 on the condition that such a provision is actually made and shown as an expense in their books of account.

This was prompted to level with the pronouncement of Bangladesh Bank made, at the behest of the donors, immediately before, in 1989.

Bangladesh Bank had then mandated that all doubtful interest income was no more to be accounted for as income in the banks' profit and loss accounts but be kept hanging in balance

and to be treated as income and thus accounted for in the banks' books of account as well as profit and loss accounts. Subsequently, in 1994, Bangladesh Bank wrote to National Board of Revenue recommending non-imposition of tax on such interest suspense with full justification. But the Tax Department, disregarding Bangladesh Bank's recommendation, started — and to date continues — with some variation, the practice of adding such doubtful, notional and unreal income to the actual and realised income of the banks and taxing on equal footing the sum of the two types of income — one unreal, the other real.

As a result of persistent persuasion, this tax treatment was realised as being highly unfair and injurious and eventually Finance Act 1996 brought about an amendment to section 28(3) and mandated not to tax such interest suspense any more until realised in cash by the banks. Up to this, the decision was fully justified and very fair — although long overdue. But, surprisingly, the justice done with one hand was, at the same time, taken away by the other. The decision not to tax interest suspense was made conditional to not allowing the legitimate deduction of provision for bad loans up to the said maximum

of 5 per cent of total outstanding loans by adding a fresh proviso (although not very well worded) to the said clause (xviii) of section 29.

What therefore happened is that insertion of the said proviso negated the whole thing by equating interest suspense with provision for bad loans made in the books of account of the banks thereby taking the matter back to the proverbial square one. The rationale with the Tax Department being that an assessee should not and cannot be given benefit for the same expense (interest suspense) twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its interest suspense twice. Unfortunately, it has not been realised by the Tax Department (and this leads to all the subsequent problems) that a bank's claim for provision incorporated in its profit and loss account has absolutely nothing to do with its