Rethinking bank supervision

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STAR

Tellers serve customers at a bank branch in Dhaka. About 36 percent of depositors' funds are located at bank branches outside the capital.

BANGLADESH Bank has been repositioning its focus on bank supervision in a strategic way. We are monitoring the condition and performance of the banking sector with sharpened risk focus, taking up new initiatives to improve our oversight, both on-site and off-site. As part of that initiative, we have been holding town hall meetings of BB supervision staff -- nationally and regionally -- to know from them the ground realities and then providing necessary guidelines to strengthen the quality of oversight. The core objective is to integrate all aspects of supervision and realise a new architecture where oversight focuses, especially on institutional and systemic risks in lending and other business activities taken up by banks, and on how well corporate governance and internal control processes in banks deal with these risks. Recently I inaugurated a regional town hall meeting in Chittagong following the national one held in Dhaka, where I provided some necessary guidelines to the field supervisors. Let me share with the readers some of those ideas.

I understand that some of the supervisors in the divisional offices can sometimes feel disconnected from the changes taking place in the financial sector. All of the scheduled banks are headquartered in Dhaka, along with most of the important conferences, media events, and policy discussions inside and outside of the government. Policies are made in the capital and announced from the capital. But we cannot forget that a significant number of our fellow citizens live outside the capital city, undertaking a significant share of economic activities. And our banks are here, too, with a significant presence in Chittagong and the other divisions. Of the total loans extended by our banks, about one-third of the funds were extended by branches of banks outside of the Dhaka division. Of those loans, 60 percent were originated in the Chittagong area.

Deposits are also substantial outside the Dhaka division. About 36 percent of depositors' funds in Bangladesh are located at bank branches outside of Dhaka. Of these, 56 percent are deposits gathered from your families, friends, and neighbours in the Chittagong area. So in both lending and deposit-taking, banks that have a presence in the Chittagong area contribute significantly to the national totals. In other words, the bank branches that Chittagong-based supervisors inspect throughout the year are responsible for about 20 percent of the growing banking market in Bangladesh. That makes the supervisors' job, in promoting banking excellence and integrity at these branches, extremely important.

But I want to step back from the local level for a moment, and talk about promoting banking excellence and integrity at the national level. As we all know, financial markets all over the world are undergoing dramatic changes. The global financial crisis, debt crisis in Europe, and recession and slow growth in much of the industrialised world have necessitated sweeping reforms in the manner in which banks are supervised and in which bank failures are handled.

Banks in Bangladesh escaped the turmoil of the past several years. But this does not mean that we can ignore the reforms taking place in the rest of the world. In fact, we have to speed up the reform process. We must put in place additional safeguards that will help prevent a local or national banking crisis from developing in Bangladesh

Banks in Bangladesh escaped the turmoil of the past several years. But this does not mean that we can ignore the reforms taking place in the rest of the world. In fact, we have to speed up the reform process. We must put in place additional safeguards that will help prevent a local or national banking crisis from developing in Bangladesh. We are a country of modest means, and we simply cannot afford to deal with the consequences of any banking crisis. We have to be alert and resourceful in doing whatever we can to avoid that painful outcome. Every banking crisis has a different origin. The savings bank disaster in the United States in the late 1980s was caused by risky investments in real estate development. The Asian financial crisis in the late 1990s was caused by poor liquidity management. The US meltdown of the last decade, from which nearly the entire industrialised world is still recovering, was caused by risky lending to the single-family housing market, which used to be thought of as the safest kind of private-sector loan. Now, in Europe, even government debt is viewed as risky and a threat to the solvency of many large banks. High and rising levels of government debt, relative to GDP, has called into question the ability of several eurozone countries to pay the interest of these debts without undertaking massive structural reforms and painful budget cuts. Greece is about to default on part of its debt, directly harming the capital and profitability of a great many of Europe's leading banks.

In short, banking has changed and as banking regulators we must also change. The old assumptions, old certainties, old procedures just are not sufficient anymore. There are risks and vulnerabilities in our own banking sector and we have to work harder and work smarter to uncover these risks and promote best practices in our banks. This is what we mean by promoting banking excellence. Above all, best practices mean sound judgment in the granting of credit, lending to legitimate borrowers who have the ability and the intent to repay. Best practices also mean diligent monitoring of all credits through their life cycles. Banks have to maintain an internal risk-rating system for all borrowers and monitor their ability and willingness to repay constantly. And they have to provision for expected loan losses when doubts arise that the borrower will pay back the loan.

Best practices also mean the prudent management of other risks in addition to credit risk, especially liquidity risk and the market risk arising from direct or indirect investment in shares. Best practices also mean an efficient, secure IT architecture that generates appropriate financial statements and management information reports, prevents the maintenance of separate, fraudulent books and records, and guards against data security breaches. Above all, best practices mean effective corporate governance, including a corporate culture that stresses compliance, respects internal audit, and implements strong internal controls. All of these best practices are the responsibility of bank management. As regulators, we must evaluate their performance, and make them take corrective action if there are deficiencies. This is what we mean when we say "promoting banking integrity."

Integrity in banking means making sure that the shareholders, directors, executive officers, and indeed all staff are honest and trustworthy individuals who will follow the laws and regulations, and implement best practices. Supervisors, in the Chittagong office, are an integral part of our efforts to promote banking integrity in Bangladesh.

How can they help achieve the objective we have been promoting? When they are visiting a bank branch as part of an inspection team, they have to pay close attention to the branch management. They need to talk to them, listen to them, ask them questions. They also have to assess their qualifications and assess their character. They should listen to the branch staff. In many cases, information about illegal or unethical activity taking place at a bank branch comes from lower-level employees. If they see something that looks wrong, in the loan files or anywhere at the branch, they should tell their supervisor. Very often, illegal or unethical conduct by branch managers or staff is indicative of the same kind of conduct at the head office.

TO BE CONTINUED

(The write-up is in light of the speech delivered by Dr Atiur Rahman, governor of Bangladesh Bank, on 'Regional Town Hall Meeting on Banking Supervision' held in Chittagong on March 18, 2012)

Ctg fair comes to a sudden close

Organisers exit venue to clear way for the ruling alliance's rally

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Visitors flock to Chittagong International Trade Fair in the port city. The fair came to an abrupt close yesterday.

THE 20th Chittagong International Trade Fair came to a close yesterday, four days ahead of schedule, depriving exhibitors of good sales and customers of shopping.

Both foreign and local traders, who were happy with sales in the last several days, said had it continued through the last day they could have recouped their investment.

The Chittagong Chamber of Commerce and Industry (CCCI) that organised the annual exposition said the ruling alliance's decision to hold a rally at the same venue on March 28 forced the organiser to wrap up.

The month-long show was supposed to close on March 24 but the participants had to leave the venue early to make room for the rally of the Awami League-led ruling alliance.

Despite the early wrap-up, CCCI officials were satisfied with the event, and termed it successful.

But traders said if the CCCI had been more serious about the exposition they could have avoided the situation. If the authorities had informed them about the decision earlier, they would not have invested so much money in the fair, they said.

Azam Qureshi, supervisor of Indian pavilion, said they had thought that they would win the hearts of local customers through their different items. But the fair came to an abrupt end before it could attract more customers.

He said they could not recover half of their investment, which was Tk 50 lakh.

Md Sohag, a supervisor of Thailand Pavilion, a partner of the exposition, said he has been participating in the fair for long. "We expected huge customers in the last week of the fair."

He said as the chamber was informed of the decision, they should have started the fair earlier.

Rafiqual Islam, an executive of Otobi, one of the top local furniture makers, said they had fixed a rational target for the fair.

The company set a Tk 4 crore sales target, only to reach half of it.

"Every year in the past, the CCCI expanded the deadline," he said. "We hoped the exposition would finish on March 31, and we set our plan accordingly."

Nurul Islam, owner of Sabuj Bangla stall, said the chamber should be more responsible in protecting interests of the traders.

The early closure irked port-city shoppers.

Lucky Akhter, a resident of Pathantuli, said it had become a tradition that the deadline of the fair extended. "We expected the same this year."

She said they spent the early days of the fair to check the quality of goods and products. "The time for shopping just ran out."

Murshed Murad Ibrahim, the CCCI president, said the chamber had to close the fair for some unavoidable reasons. "According to the rules of the exposition, we reserve the right to close it anytime."

India took part in the fair for the first time. Other participating countries were China, the USA, Pakistan, Iran, Thailand, Japan and Bangladesh. About 55,000 people visited the fair this year.