Securities rules to see major tweaks

A BSEC member speaks on the upcoming changes

SARWAR A CHOWDHURY

THE stockmarket will see massive changes in the next three months as the regulator will modify a good few securities rules and regulations in an extensive and advanced way.

Bangladesh Securities and Exchange Commission (BSEC), which was restructured after a price debacle in 2011, has already brought some reforms.

But the regulator now wants to widen its reach and thinks of a future market.

"The modifications will ensure more transparency and accountability in the market," said Arif Khan, a member of the BSEC, in an interview with The Daily Star recently.

"If an investor subscribes for an IPO, he or she has to deposit the money before the IPO lottery, and the deposited money remains in an escrow account for a long time."

"Now we are thinking to introduce a mechanism so that an investor does not need to deposit the IPO money before the lottery. It will be deposited only when he or she gets confirmation on allotment of IPO shares," Khan said.

Apart from amendment to IPO (initial public offering) rules, he said, the commission will bring massive changes to mutual fund rules, repeat-IPO rules, rights issue rules, and foreign investment and corporate governance guidelines.

All amendments will be made in an advanced way, he said. "There is no end to the reform process, it's an ongoing process."

The BSEC, however, will not only amend the securities rules, it will also focus on introducing future markets and products in the capital market in the coming days.

"We have started working on setting up a clearing corporation, taking the Hong Kong, Singapore and Indian markets as models to make the trading settlements easier and less time consuming," the BSEC member said.

"Besides, we have started the preliminary work on how a commodities exchange can be established in our country," he said.

The BSEC is examining the pros and cons, such as the relationship between the commodities exchange and the economy, the available commodities and the regional experiences of commodities exchanges.


Arif Khan

Referring to the equity-based stockmarket in Bangladesh, Khan said derivatives should be introduced here. "We will form a committee with private sector representatives on the introduction of derivatives in our market," he said.

About the ongoing projects, Khan said a separate tribunal for securities related cases will be set up within the next few months.

"The law ministry is now working on it, and once the tribunal is set up, stock-related cases that have been pending in courts for long will be settled in a short time."

The demutualisation process of stock exchanges is also going on to separate the bourses' management from ownership, he said.

"The bourses will submit a demutualisation scheme to the commission by this month, and we will approve it within the next 60 days."

The demutualisation of a stock exchange transforms it into a for-profit company owned by shareholders. It also ensures alternative business models and operational efficiency.

In the last two years, the BSEC has made amendment to several securities rules, including public issue rules, rights issue rules, private placement rules, book building method, margin rules, corporate governance guidelines and mutual fund rules.

The BSEC has also introduced a new regulation on research analysis rules, and another one on investment advisory services is awaiting regulatory approval.

The government also empowered the regulator, enabling it to frame its own budget, appoint human resources, set own remuneration and seek account information from banks anytime.

"We have implemented the recommendations made by a government probe committee on 2011's share market scam," he said.

"It's not our duty to see why the market is going up or down. Our duty is to see whether any manipulation is taking place or anybody is trying to manipulate it," Khan said.

New-age trade clubs: A guide for the perplexed

ANDY MUKHERJEE

GLOBAL trade is going private. After a frustrating 12-year-long wait for the World Trade Organisation to hammer out an accord acceptable to its 159 members, businesses and governments are now hedging their bets. Enter the Trans-Pacific Partnership, or TPP, which received a boost this week with Japan joining the negotiations.

What is the Trans-Pacific Partnership?

It's a proposed 12-nation trade bloc that economist Richard Baldwin calls a "mega-regional" group. Between them, Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States and Vietnam are home to 800 million people and $28 trillion in annual output. A deal is expected later this year, or in 2014.

Some countries are notable by their absence. Russia has declined membership, and China is waiting and watching. That suits the United States and Japan just fine - they have a chance to write the commerce rule book, and hope that the large developing nations will play along.

What will it do?

Market access will be top of the agenda. Californian rice growers want to enter Japanese homes more aggressively. Japan wants to protect its farmers, but it also wants to sell more cars in the United States.

In fact though, the TPP might not be the best place for such deals to be cut. Any nations not included, which includes the whole of Africa and South Asia, would be left out. A goal to open up protected markets for government procurement looks more useful. That's one of the WTO's failings: its limited agreement covers just 15 members outside the European Union.

Countries outside the TPP could benefit too. Imagine Malaysia agrees through the TPP to treat Japanese and American contractors on par with local suppliers. After that, there will be little point in protecting the government-tender market from vendors from China, India or anywhere else.

Will China and India join?

Perhaps, but probably not for years. While the TPP is sometimes characterised as an attempt to freeze China out, the real issue is that the TPP's principles may be at odds with China's way of running an economy. It's likely members will be asked to reduce subsidies, state guarantees and other advantages that government-controlled companies enjoy. The structure of Chinese industry, which is dominated by state-owned enterprises, would need to change dramatically.

India too has quirks that the TPP may not easily accommodate. India is a signatory to a 1995 WTO accord on intellectual property, but it makes cheap generic copies of patented drugs for its own citizens as well as for Aids and cancer patients in other developing countries. The TPP may insist on stronger protection of innovators' rights. Both China and India will need significant additional benefits from the TPP before they agree to further open up their consumer markets.

Will it get public support?

Even if governments buy in to the TPP, electorates may not. First, negotiations are somewhat secretive. There has been only a token attempt to engage with civil society, which may promote the sense that the whole exercise is rather undemocratic.

Second, the TPP could further empower big business. Other private trade agreements have allowed aggrieved investors from member countries to sue foreign governments directly, which isn't allowed under the WTO. Swiss-based tobacco company Philip Morris has started arbitration against Uruguay's anti-smoking policies, using the two countries' bilateral trade accord as a framework.

Many small nations already worry about being able up to stand up to powerful multinationals; a further tilt toward business interests won't go down well with environmentalists and public-health activists.

Why so many trade accords?

The list of acronyms grows ever longer: the TPP joins Nafta, Asean, Asean-plus-3, MERCOSUR, EFTA, COMESA and many more. The gloomy view is that the mushrooming of separate alliances means trade has fragmented, and the spirit of post-World War II internationalism is dead.

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Internet companies, stung by earnings, still look pricey

REUTERS, *New York*

EXPEDIA Inc can send people to destinations around the world, but it can't send investors back in time so they can avoid the stock's massive selloff on Friday.

The stock's 25 percent fall is its worst in seven years, becoming the latest in what is shaping up as a rough quarter for Internet company earnings. Expedia, Netflix and Google were hit hard after reporting earnings in the last two weeks.

Investors have chased this group higher in 2013, lured by expanding user bases and profit growth that eclipsed the broader market. But that has raised concern among analysts who see the sector as a whole as overvalued and ripe for a sell-off.

That appears to be what befell Expedia on Friday, as it suffered its biggest one-day loss since May 2006 after its results fell short of expectations.

"I don't see any Internet stock that looks like a value," said Kim Forest, senior equity research analyst at Fort Pitt Capital Group in Pittsburgh. "I'm a fan of them as a customer, but wouldn't pay anywhere near the multiple we're seeing for them."

One measure of the valuation of these companies, intrinsic value as calculated by StarMine, a Thomson Reuters company, shows that of the 55 or so industries among the top 1,000 U.S. companies, Internet and catalog retailers are the most overvalued, and Internet software and services companies are the seventh-most overvalued.

Intrinsic value evaluates a stock based on projected growth over the next decade, using a combination of analyst forecasts and industry growth expectations.

The most overvalued name in the S&P 500 is Amazon.com Inc, which has climbed more than 20 percent this year to $309 a share and has a mammoth P/E ratio of 133.72. The online retailer's price is 681 percent greater than its intrinsic value of $38.85.

Late Thursday, Amazon reported it had unexpectedly swung to a quarterly loss and gave a third-quarter outlook that was below forecasts. But despite the disappointment and elevated levels, its shares were up 2.8 percent on Friday.

"It is really looking down the line for other areas of profitability, and that could represent a positive play in the future," said Chris Hobart, chief executive of Hobart Financial Group in Charlotte, North Carolina. "I'd be a buyer of it right now, but cautiously."

That Amazon rose after its results "shows that investors are willing to just shrug off the negativity," said Ryan Detrick, senior technical strategist at Schaeffer's Investment Research in Cincinnati, Ohio, adding that options activity before the earnings suggested investors had not been bearish on the company before the news.

To justify its current price, Amazon would need to grow earnings 44 percent on a compound basis each year for the next 10 years, according to StarMine.

Shares of Netflix Inc are up 160 percent so far this year as investors bet the online movie renter's expansion into original content will lead to strong subscriber gains. While earnings topped expectations earlier this week, its additions were in the middle of a range it forecast in April.

Netflix shares would need to drop 82 percent to reach its intrinsic value. Since hitting a new high on July 18, the stock has since been beaten down, falling nearly 10 percent.

Salesforce.com, meanwhile, is 83 percent above its intrinsic value. The maker of online sales software reports results next month.

Google Inc, another investor favorite this year, with gains of 25 percent, also saw a pullback after its results were issued last week, coming in below expectation despite a 20-percent jump in its core business revenue.

Almost all Internet stocks have high valuations. Netflix has a 12-month forward price-to-earnings ratio of 92.9, while Salesforce.com Inc's is even higher at 100.5. The average stock in the S&P 500 has a P/E ratio of 14.6, according to Thomson Reuters data.

THE FACEBOOK EXCEPTION

While Facebook's P/E ratio of 40.69 is more than twice the 18.57 ratio of its social media peers, it differs from other online companies in that it has traded fairly flat for most of this year.

After its highly anticipated initial public offering in 2012, the stock has been unable to regain its $38-per-share IPO price, as investors questioned whether it would be able to monetize its massive user base and mobile usage.

When its July 24 results indicated it was making progress in those areas, buyers jumped on the stock, pushing it up about 30 percent in its biggest-ever daily increase.

"Facebook is doing a good job on the innovation front, going from a weak area - mobile advertising - to creating something pretty damn powerful," said Hobart.

History shows growth woes will override rupee defence

REUTERS, *Mumbai*

IF one thing is clear from India's impulsive strategies this month to defend a plunging currency, it is that the Reserve Bank of India's policy bias towards supporting growth is innate, even in a crisis.

When the rupee hit a record low on July 8, the RBI withdrew cash from money markets, making bets against the currency significantly more expensive. It intervened to stop the currency from dropping beyond 60 per dollar and at the same time tried to assure investors the shock measures were temporary.

To most RBI watchers, this amounted to a menu of stop-gap measures that failed to account for lasting pressure on the currency. To the central bank, it was doing enough to support the rupee without tightening cash conditions so much that it threatened the longer-term growth of an already weak economy.

The eye on growth means it has avoided following its emerging market peers Indonesia, Turkey and Brazil, who all raised their policy rates in anticipation of a long spell of capital outflows as the United States prepares to tighten policy.

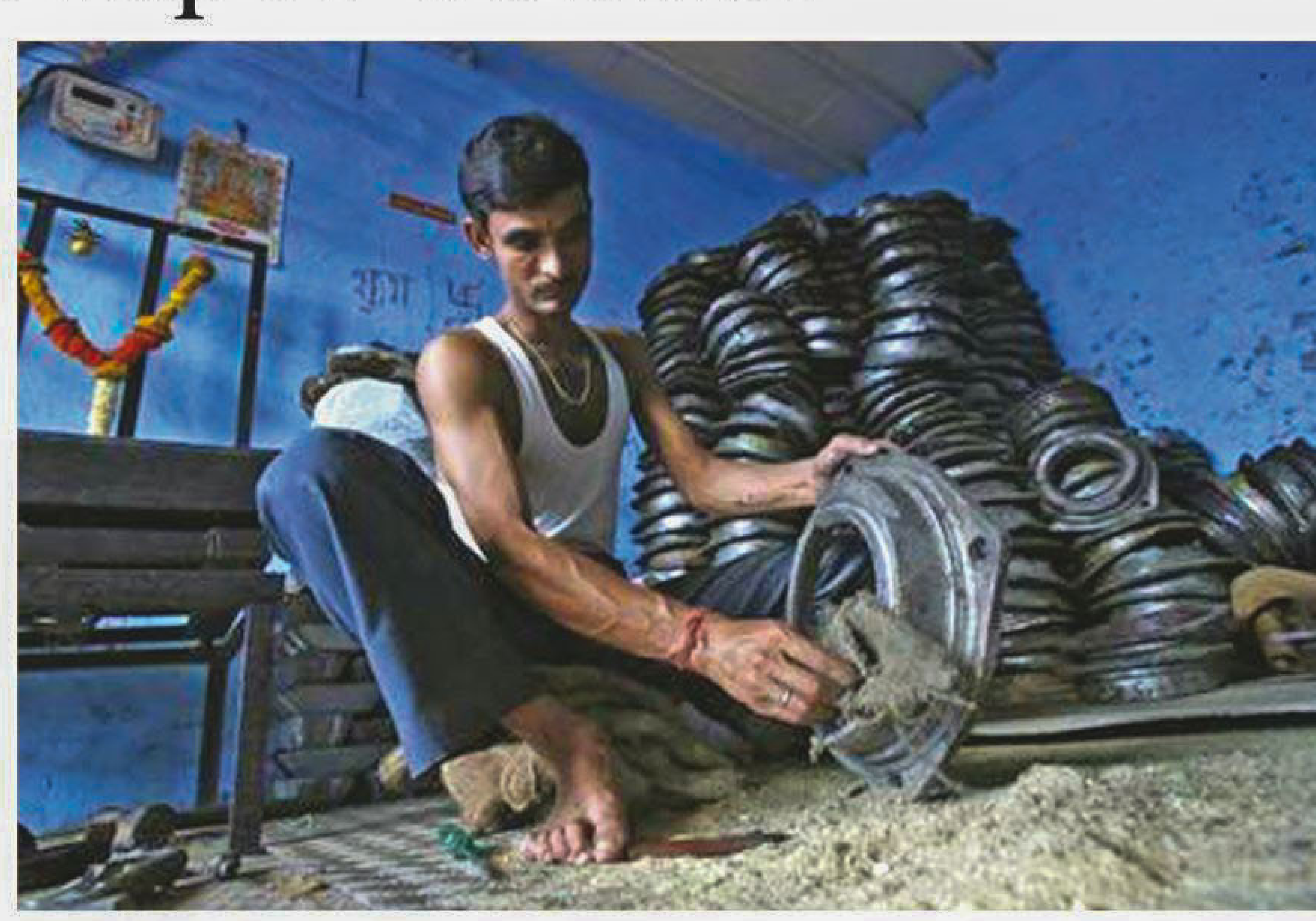
It is unlikely to raise rates either on Tuesday, when it reviews policy, even though analysts argue it should do so if it wants to signal its determination to attract foreign funds and defend the currency.

History suggests these decisions are deliberate and ultimately growth is the overriding factor.

The rupee has fallen 33 percent against the dollar since 2007. As recently as 2010, the RBI's reluctance to raise interest rates for fear of affecting growth allowed inflation to remain at near double-digit levels for two years.

"The right approach would have been to move the official policy levers," said Rajeev Malik, senior economist at CLSA in Singapore.

Malik feels the central bank might be hoping a temporary tightening of money markets will stabilise the rupee. And that the RBI is either too optimistic or it is wary of announcing a turn in monetary policy.


REUTERS
A labourer sands wheel parts inside a factory at an industrial area in Mumbai.

"Ultimately, at least how I see global liquidity developing, it will be a lose-lose proposition," he said. "India will suffer a GDP downgrade and the rupee will also break 60 in a sustained manner. They have boxed themselves into a corner."

To be fair to the central bank, the country's balance of payments problems are beyond its control.

India has historically been a capital-starved economy, with imports and foreign debt servicing bills that far exceed revenues. Capricious governments have done little to ensure a steady stream of foreign investment flows, and India remains one of the most difficult countries in which to do business.

No wonder, critics say, that the current account deficit has blown out to a record 4.8 percent of gross domestic product, or about $88 billion, in an economy whose growth has slowed to a decade low of 5 percent and where consumer inflation is nearly 10 percent.

"Yes, exchange rate stability is the focus now in the short-term," said a central bank official, declining to be named as he was not authorised to speak to the media. "But that is because, in the long-term, we want to protect growth for which we have to focus on the exchange rate in the short-term."

That view point was backed up by India's chief economic adviser, Raghuram Rajan, who told a television channel on Thursday that policy measures were geared to stabilising the currency with "minimal damage" to growth.

Tasked with controlling inflation, keeping the economy growing and ensuring financial stability, plus the pressure of pleasing its political masters, it is often of no surprise that the RBI makes growth a priority.

Even though rates were raised 13 times between 2009 and 2011, economists often felt the RBI was behind the curve and allowed prices to stay too high for too long.

Likewise, while the RBI raised rates to defend the rupee during periods of turmoil in 1998, 2000, 2008 and 2011, the policy tightening was often quickly reversed within two to six months, analysts said.

This time, the central bank is in more of a bind than normal. With currency reserves falling rapidly - at $280 billion they cover just 7 months of imports - and external debt worth $172 billion, a fast-slipping currency could eventually risk financial stability.

Yet, raising its 7.25 percent overnight repo rate would be politically difficult as the ruling coalition has to call a general election by May.

"Policymakers are trying to achieve a fine balance by squeezing liquidity at the short-end even as they try to cap yields at the long-end," JPMorgan Chase said in a client note. "Yet, some transmission to long rates, funding costs and investment decisions is inevitable."

The RBI's decision to raise its short-term emergency funding rate by 300 basis points has already driven 10-year government bond yields up 100 basis points and short-term corporate debt up 200 basis points across the board.

It is inevitable that growth and therefore foreign inflows into the equity market will be adversely affected, JPMorgan said.