

# Challenges that capital market faces

MOHAMMED NASIR UDDIN CHOWDHURY

**C**APITAL market provides an important alternative source of long-term finance for long-term productive investments. This helps in diffusing stresses on the banking system by matching long-term investments with long-term capital. In Bangladesh, the capital market has the opportunity to provide equity capital and infrastructure development capital for strong socio-economic benefits -- roads, water and sewer systems, housing, energy, telecommunications, public transport, and so on. The capital market can encourage broader ownership of productive assets by small savers to enable them benefit from Bangladesh's economic growth. The capital market can provide avenues for investment opportunities that encourage a thrift culture critical to increasing domestic savings and investment ratios that are essential for rapid industrialisation. Equity financing through the capital market can reduce the debt level of businesses.

In Bangladesh, companies raise money from the primary market through IPO (initial public offering) and rights offer. In the last nine years, on an average 15 new companies got listed through IPO each year. As of May 2015, a total of 324 companies are listed (including 41 mutual funds) on Dhaka Stock Exchange. In the last nine years, the average yearly capital raised through IPO and rights issue is Tk 1,495.65 crore and Tk 782.53 crore respectively.

Till date, bank financing has been the major source for companies despite the long-term benefits of fund raising from the capital market. Till 2014, the total issued capital of all listed companies is Tk 47,121 crore, and bank credit outstanding balance is Tk 543,407 crore. Though the capital market can provide equity capital to businesses, which can be an effective way to fetch long-term financing, we could not utilise the platform for public sector investments. There have been several challenges in the primary market and in the process of IPO. One of the challenges is an absence of regulatory measures or incentives to bring new companies in the market with strong fundamentals. Discovery of price also becomes very difficult due to a lack of analysts. Sometimes small companies face difficulties due to large pre-IPO capital rules. Weak activities of merchant banks are also to blame. Distribution in Bangladesh is uneven. Only retail investors can participate in the IPO, whereas, institutional investors and foreign

| YEAR | NUMBER OF NEW IPOs | IPO SIZE (Tk/crore) |
|------|--------------------|---------------------|
| 2006 | 7                  | 372.7               |
| 2007 | 14                 | 1,005.7             |
| 2008 | 12                 | 827                 |
| 2009 | 18                 | 1,904.7             |
| 2010 | 18                 | 2,865.3             |
| 2011 | 14                 | 1,689.9             |
| 2012 | 17                 | 1,817.5             |
| 2013 | 12                 | 1,664               |
| 2014 | 20                 | 1,314.1             |

| YEAR | RIGHTS OFFER (Tk/crore) |
|------|-------------------------|
| 2006 | 167.36                  |
| 2007 | 59.87                   |
| 2008 | 211.23                  |
| 2009 | 243.98                  |
| 2010 | 1,760.11                |
| 2011 | 1,858.95                |
| 2012 | 497.90                  |
| 2013 | 180.30                  |
| 2014 | 2,063.04                |

| YEAR | BANK CREDIT | CAPITAL IN STOCKS |
|------|-------------|-------------------|
| 2010 | 67,218      | 4,625             |
| 2011 | 60,318      | 3,548             |
| 2012 | 61,649      | 2,315             |
| 2013 | 45,874      | 1,844             |
| 2014 | 64,640      | 3,377             |

investors can participate in the IPO in fixed price method like general investors. Retail investors hold IPO shares for a very short period of time.

The market finds it difficult to price a security reflecting its fundamental value in both primary and secondary levels. Both 'fixed price' and 'book building' have resulted in huge price anomalies. The fixed price method fails to recognise the future earning potential, while the book building method is alleged to be biased. Rumour influences the price of a security in the secondary market more than the fundamental value of a security. Most of the recent IPOs have noted price jump on the first day of trading followed by a quick fall in prices after five or 10 trading days.

The capital market exposure of banks, the major institutional participant in the capital market, has been capped heavily at 25 percent of core capital (solo basis) and 50 percent of consolidated core capital (consolidated basis) and the deadline for compliance is July 2016. Considering the volume of banks' existing capital market exposure, the timeframe for compliance is short. Single borrower exposure for capital market subsidiaries is another issue as these subsidiaries are heavily burdened with negative equity margin accounts. Regulators should go for a long-term solution to this problem rather than taking short-term measures.

Public confidence in mutual funds is very low due to asset managers' involvement in the gross violations of securities rules and misappropriation of funds money.

Quality of disclosure is not up to the peer standards. Investors find it difficult to assess the portfolio holdings or quality of stated net asset value. Most of the mutual funds are generic rather than style based. Fund managers have selection errors and prefer passive management. While in peer markets open-end funds dominate, there are only nine open-end funds in

Bangladesh. Dividend in the form of Re-Investment Unit has not been welcomed by investors due to dilution effect. Fund managers are very reluctant to stick with the redemption of closed-end mutual funds.

Bangladesh's capital market has a very basic equity market. Bond market is non-existent. Although there are eight debentures and 221 treasury bonds listed in the market, these issues do not trade in the market. There are only two corporate bonds listed in the market. We are not aware of any regulatory vision or seldom see any guideline in introducing derivative products/new products. We have noticed fear in the derivative products but no initiative to gain knowledge on these products. Our institutions should increase professional capacity to deal with alternative products.

Bangladeshi regulators should be more proactive in developing derivative and a vibrant bond market. Alternative products like derivatives would not only facilitate us in better risk management but also create job opportunity for growing investment professionals.

High transaction cost in the bourses also hinders the trading of government securities. As the return of bond is fixed and volatility is also low, transaction cost similar to equity securities makes it totally unattractive to the investors. Presently there is 0.05 percent tax in source equivalent to equity securities. Secondary market for bonds is very illiquid. Secondary trading is mostly done over the counter. Road shows or campaigns can be arranged to reduce knowledge gap in bond market. In corporate bonds, private placement is getting popularity. Only two corporate bonds are presently listed on the bourses. For a vibrant bond market and better diversification of individual portfolios, bond listing in the market should be increased.

Despite having favourable economic factors

and a positive market outlook, foreign participation in equity market is very low. Permission for brokerage commission sharing by foreign brokers brought in lots of foreign trade in equity market in 2014. Weak corporate governance, less transparent market structure, low level of financial disclosure and a lack of research remain as bottlenecks. Bangladeshi corporate houses are yet to grow a culture of investor meetings. Even, they do not have any formal investor relationship department. While allowing foreigners, local institutions should also build capacity for better investment management.

We are lagging far behind our neighbouring countries in technology in investment management. Although neighbouring countries are adept at technology-based trading, we could not progress in this regard. Trading platforms are very weak for large executions.

For acquisition of more than 10 percent of shares of any company, an approval from the relevant authorities is needed. This is a bottleneck from investment perspective. More often boards acting in Bangladeshi companies are inefficient but hold significant control over their company.

Directors need to hold at least 2 percent shares in listed companies. This is a counter-productive approach. We should seek better corporate governance in the company and independent management to run the company in the long run. Remuneration of independent directors is very low. This is not at all good for the motivation of professional independent directors.

In summary, regulators and institutions operating in the capital market should come forward to address the issues for a better functioning market.

The writer is the managing director of LankaBangla Finance.

## Twitter says it wants full-time CEO

AFP, New York

Twitter said Monday it would only consider chief executive candidates who can commit full-time to the company, signaling that co-founder and interim head Jack Dorsey likely will not be picked.

Dorsey, in addition to stepping in for outgoing Twitter CEO Dick Costolo, leads Square, a growing mobile payments company.

"The Committee will only consider candidates for recommendation to the full Board who are in a position to make a full-time commitment to Twitter," the messaging-platform company said.

"The search is proceeding with a sense of urgency but the Committee will take the time necessary to find the right CEO to lead the next phase of Twitter's growth."

Twitter said it had hired the executive search firm Spencer Stuart to help identify CEO candidates. Costolo announced June 11 he was stepping down amid criticism of the social media company's slowing growth.

Some analysts had speculated that Dorsey, the author of the first "Tweet," might try to lead both Twitter and Square. But Twitter's statement was seen as pressuring Dorsey, who is Twitter's chairman, to make a choice between the two companies.

In mid-morning trade, Twitter shares fell 0.6 percent to \$35.64.



A number of young entrepreneurs, who are the children of the members of Grameen Bank, pose for photographs with Nobel Laureate Prof Muhammad Yunus at the 86th Social Business Design Lab in the capital yesterday.

## Six social businesses get go-ahead

STAR BUSINESS REPORT

The 86th Social Business Design Lab took place yesterday where six young entrepreneurs presented their project plans and got approval.

The lab, which aims to provide a platform to the children of the borrowers of Grameen Bank to showcase their ideas and get investment, took place at the auditorium of the microcredit bank in the capital.

About 150 participants and observers from national and international organizations and a large number of international visitors attended the programme, Yunus Centre said in a statement.

The six new social business plans are Complete Ladies Shop & Parlor, Lamea Bag House, Lima & Fatema Machinery Store, Amena Flower Nursery, Ritu Enterprise and Bhai Bhai Handmade Soap.

At the lab, the entrepreneurs shed light on the projects' marketing process and sustainability. All six projects were approved for funding from various social business funds.

Since starting its journey in January 2013, a total of 1,175 projects have been presented in the labs. Of them, 1,150 projects were approved for investment and most of them are already in operation, Nobel laureate Prof Muhammad Yunus said while chairing the

## Asia's exporters struggle to cope with a changing global economy

REUTERS, Jakarta

**I**N the good old decades, many Asian governments could stick to a simple economic strategy - ramp up exports, and reap solid growth rates.

Now, export-led growth no longer serves the region well and Asia is struggling to overhaul that economic model as it waits for world trade to recover.

And the rebound "is going to be capped", says HSBC economist Fred Neumann, because of changes in the world economy, including how American consumers are "much more frugal" than a decade ago.

Asian exports to the United States have risen this year, but Neumann says such growth now is more driven by investment in software development and shale-oil drilling than by activity that pulls in imports.

Stalled global trade talks and the shrinkage of manufacturing supply chains that stretch from China, the world's workshop, are making policymakers from Bangkok to Seoul consider new models as exports may never again grow rapidly as in the 2000s.

"The global trade pattern has changed," Paiboon Kittisrikangwan, a deputy governor at Thailand's central bank, told Reuters last week. The patchy recovery in advanced economies isn't producing the same import demand as before, he said. South Korean Finance Minister



People work near cargo containers loaded from trucks at a port in Tokyo.

Choi Kyung-hwan has called for a "strategic change" by exporters to target Chinese consumers rather than factories. Indonesian Trade Minister Rachmat Gobel, pressed on what he's doing to boost exports, says he will seek more access for local goods to Western markets.

So far this year, exports from East Asia - from Southeast Asia across to Japan - have fallen an average of around 5 percent in dollar terms. Poor performers include Indonesian coal, Malaysian palm oil, Singapore pharmaceuticals and Korean cars.

"Things are not looking up," said Neumann of HSBC, citing persistently weak export orders and purchasing managers' indexes. "They all

point towards no pick-up." Economists had hoped temporary factors such as Lunar New Year and U.S. winter weather might explain weakness. But Dan Martin at Capital Economics said these cannot explain the still-weak numbers, which are "something to worry about more than we did before".

Some of the weakness reflects strength of the dollar, which means earnings booked in local currencies are worth less when reported in the U.S. currency. However, concern is rising that rather than another cyclical slowdown from which demand will bounce back, Asian exporters face something structural - and there will be no return to strong growth.

## British business leaders plan campaign for EU exit

REUTERS, London

A group of British business leaders and entrepreneurs are preparing to launch a campaign for Britain to leave the European Union at a planned membership referendum, a major donor to the UK Independence Party said.

Prime Minister David Cameron has promised to renegotiate Britain's relationship with the EU ahead of a vote by the end of 2017, and is this week due to set out his reform plans in more detail at a summit of EU leaders in Brussels. The group, which the Sunday

Telegraph reported would be called "No Thanks - We're Going Global", is backed by UKIP donor Arron Banks and property investor Richard Tice. So far it has raised 7 million pounds (\$11 million) of a planned 20 million pounds.

"This is too important for politicians to be taking the lead, it has got to be business, and the wider public," Banks told the paper. "They can endorse it and support it but they will not be involved in the campaign."

Banks said the group, due to launch in September, had also been talking to sports stars and leading

figures in medicine, science and the military about getting involved in the campaign.

Lawmakers from Cameron's Conservatives and the opposition Labour Party have already formed two separate groups ready to campaign to leave the EU if the British leader does not succeed in his renegotiation efforts.

Cameron, re-elected for a second term last month, has spent the past few weeks meeting with EU leaders to discuss his plans ahead of Thursday's European Council summit. He has said he is confident of securing concessions and favours Britain

remaining in a reformed union.

The changes he is seeking include boosting the bloc's economic competitiveness, protections for non-members of the euro zone, an opt-out from the EU's principle of ever-closer union, and tighter curbs on EU migrants' access to British welfare payments.

The Sunday Times reported that aides to Cameron had told Eurosceptic Conservative lawmakers that his renegotiation plans go further than he has made public, including "rebranding" Britain as an associate or trading member of the bloc.

## German business leaders warn Merkel not to go soft on Greece

REUTERS, Berlin

German business leaders urged Chancellor Angela Merkel to take a tough line with Greece at an emergency summit of euro zone leaders later on Monday, saying only reform concessions from Athens could keep the country in the euro zone.

The comments, from the heads of the leading German business federations, reflect a hardening line towards Greece. In past years, the same associations had warned against risking a so-called "Grexit", fearful of the consequences for the European economy.

"Greece must deliver today," Ingo Kramer, head of Germany's BDA employers association, told German newspaper Bild.

"Only then can Greece actually avert its own insolvency and only then can Greece remain in the euro zone - and that has to be the common goal."

Over the weekend, the European Union welcomed new proposals from Greek Prime Minister Alexis Tsipras as a "good basis for progress" at the talks.

His government has so far resisted calls for pension spending cuts and is urging its creditors to provide it with debt relief in return for any concessions.