Banks should focus on ethical behaviour

India's former central banker says in a memorial lecture in Dhaka

STAR BUSINESS REPORT

FINANCIAL institutions should build a culture that insists on ethical behaviour and putting societal welfare ahead of short-term profits, said a former central banker from India.

"If an institution targets societal welfare, profits automatically roll in," said Duvvuri Subbarao, a former governor of the Reserve Bank of India.

Subbarao's comments came at the 16th Nurul Matin Memorial Lecture on Ethics in Banking, held at the auditorium of the Bangladesh Institute of Bank Management in the capital on Tuesday.

Since 2001, the BIBM has been organising the annual lecture in memory of AFM Nurul Matin, a former deputy governor of the Bangladesh Bank, who made significant contribution toward rehabilitating the banking system after the emergence of Bangladesh.

"If we look around today, many of our venerable firms are those that have a reputation for ethical behaviour and value-based business practices."

They have not merely survived but have prospered, whereas firms that compromised ethics have vanished.

The notion that good ethics weigh against profitability is wrong and must be demolished.

"Indeed, the opposite is true," said Subbarao, who served the central bank of India from 2008 to 2013.

Ethics in banking recognises two realities.

One, banking can add value to collective societal welfare if, and only if, it is based on ethical foundations.

Two, the deep anguish that somewhere along the way banking has lost its moral core to such an extent that some people think of ethics and banking as a quintessential oxymoron.

As per popular perception, unethical behaviour is not only common in the financial sector but is becoming pervasive, he said.

The environment in the financial sector -- the pressure and opportunity to bend the rules, the high pay-off and the low-risk of getting caught -- encourages ethical compromises, said Subbarao, also a former lead economist of the World Bank.

He believes it is possible to build an ecosystem of ethical finance provided everyone involved -- the individual financial firms, the finance industry as a collective and the financial sector regulators -- makes a commitment to building an ethical ecosystem of finance.

"It should be obvious that the effort to build financial business on ethical standards must begin at the firm level."

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Duvvuri Subbarao, a former governor of the Reserve Bank of India, speaks at the 16th Nurul Matin Memorial Lecture on Ethics in Banking at BIBM auditorium in the capital on Tuesday.

It is now common practice for financial firms, especially banks, including those in emerging economies like Bangladesh and India, to adopt a mission statement laying out its business philosophy.

"Such a charter exhorting values, ethics and good behaviour is undoubtedly an important first step. Disappointingly, it most cases, it remains the only step."

No concerted effort is made to operationalise that mission statement into the day-to-day business of the institution.

Subbarao went on to advise financial firms to build and nurture an institutional culture that believes that the long-term net worth of a company is maximised not by driving short-term profits but by driving enduring contribution towards societal welfare.

He also urged the firm management to set an example of ethical behaviour.

Most managements exhort their staff to be ethical, but such exhortations remain just empty words because managements themselves routinely breach ethics, and to add insult to injury, implement an incentive structure that encourages unethical behaviour down the entire hierarchy, Subbarao said.

His third recommendation is to tailor human resource policies at the firm level to reflect the ethical values of the institution.

Every segment of the financial industry such as banks, non-banks, insurance companies, pension funds, hedge funds, private equity and investment banks should agree on a self-regulating code of conduct for their segment of the industry, Subbarao said.

"They are best placed to do this because they are best aware of the operational realities of their respective businesses segments."

About the role of regulators in fostering ethics, Subbarao said they should not stop at just checking for risk management and consumer safety.

They should also make sure that the firm is conducting its business in a prudent and socially responsible manner.

The former RBI governor also talked about the microfinance sector in India, which took a lot of lessons from Bangladesh's pioneering experience.

The backlash against the microfinance sector in the northern state of Andhra Pradesh in 2010 was a choppy period for Subbarao.

In late 2010, the microfinance sector in Andhra Pradesh was pelted with allegations of usurious interest rates, coercive recovery practices and unscrupulous business practice to lure in borrowers with multiple loans.

"There were, of course, excesses and malpractices but we could not risk throwing out the baby with the bath water."

He put an upper limit on the interest rate that the microfinance institutions could charge their borrowers.

"The industry is back on track and is growing at a healthy clip," he added.

Fazle Kabir, governor of the BB, and Toufic Ahmad Choudhury, director-general of the BIBM, also spoke.

Markets may have hands but not soul

Former BB governor Atiur Rahman speaks on sustainable finance in Dubai

STAR BUSINESS DESK

THE key challenge in developing economies is how to nudge the banks beyond short-termism and to serve the medium- to long-term goals of sustainable development, said Atiur Rahman, former governor of Bangladesh Bank.

"Developing economies often have small, rudimentary and bank-based financial system. Financing generally is short-term in nature, with a large presence of state-owned banks and supervisory challenges," he said.

In today's post-Paris Climate Agreement and UN mandate for financing SDGs, it is imperative that finance reaches the real economy and the base of the pyramid to deliver prosperity for all, poverty for none, and respect for nature, he said.

Rahman spoke at a discussion on sustainable finance in developing countries, in Dubai organised by UNEP and UAE on Tuesday.

"Unfortunately, as we have seen in the past and across the world, financial system or market alone left to its own device may not spontaneously bridge these gaps with its invisible hands and missing markets."

"We must not forget that markets may have hands but not soul or conscience. That said, we also cannot be naive and blame the markets for the failures in policy gaps."

"I am happy to share that some policy innovations in countries facing the climate change vulnerabilities are already taking place," Rahman said.

"In Bangladesh, despite being a victim of climate change not of our own creations, we were already investing our meagre resources to fight back."

Bangladesh's central bank came out of its conventional narrow shell and has been playing a broader developmental role by ingraining socially responsible, inclusive, and environmentally sustainable ethos in finance, he said.

"Green finance has become imperative. To start with, our priorities have been agriculture, MSMEs enterprises and women entrepreneurs, green businesses and industries for equity and impact consideration."

Besides greening its own energy supplies, Bangladesh Bank also offered a revolving refinance scheme of Tk 200 crore in 2009 for supporting small and medium scale solar, bio-gas and effluent treatment plants.

Bangladesh Bank expanded the refinance schemes with support from the World Bank and as well as from its own resources, he said.

Supported by ADB, BB established a $50 million "Financing brick kiln efficiency improvement project" as brick kilns are known to be large polluters in South Asia, he said.

At present, there are more than 50 green products in supply. In addition, massive digitisation of the payment and supervisory systems were introduced to make the sector paperless and modernised.

Atiur Rahman

Top 10 performers in green banking are annually awarded by the central bank. Banks are also encouraged to share a part of their CSR fund with green initiatives taken by community based organisations, he said.

Around 40,000 projects received green financing worth $7 billion, mostly through private banks. Solar home systems (SHS), solar assembly plants, biogas, solar irrigation pumps, green bricks, effluent treatment plants, bio-fertiliser have received major share of this fund, he said.

Around 13 million beneficiaries are having off-greed solar energy. The SHS reaching around 4.5 million households replaced 180,000 tonnes of kerosene worth $225 million per year.

Also the programme saved 41,000 tonnes of firewood. Scaling up solar-powered irrigation will save huge amount of foreign exchange now spent on purchase of diesel.

"I strongly feel that greening finance is a journey and not a destination. Much more need to be done in institutionalization, experimentation, and implementation."

"Central banks cannot do this alone."

Ease challenges of export to India: SANEM

STAR BUSINESS REPORT

BANGLADESH, Nepal and Bhutan are facing escalated challenges to increasing and securing their exports to India's nearly $460 billion market, despite enjoying a duty free and quota free access, officials of South Asian Network on Economic Modelling (SANEM) said yesterday.

"These challenges are related to their limited export capacities, lack of diversification of export baskets, various non-tariff measures (NTMs) and procedural obstacles (POs) both at home and in the Indian market," said SANEM Executive Director Selim Raihan.

The non-profit research organisation shared its views at a press briefing at its office on the future of regional integration in South Asia, a move that comes after the cancellation of the Saarc Summit to be held in Islamabad in November.

SANEM said cancellation of the summit casts a dark shadow over progress towards a unified South Asia. But it observed that Bangladesh, Bhutan, India and Nepal (BBIN), an initiative for sub-regional cooperation, can be an answer to the deadlock of regional integration in South Asia.

"Larger and effective achievements in such sub-regional architecture can exert some positive pressure on the region as a whole to avoid conflict," said Raihan, also an economics professor at Dhaka University.

However, deeper integration among the BBIN countries has been impeded by several NTMs and associated POs, which are exacerbated by a lack of trade facilitation and cumbersome custom procedures at the land border ports, said the SANEM paper.

The organisation said there is substantial potential for a rise in intra-regional trade under the BBIN initiative. The largest export market in South Asia is India, said Raihan, citing India's import data in 2014.

Pakistan, Bangladesh and Sri Lanka are three other major markets with a market size of $59 billion, $46 billion and $21 billion, he said adding that Nepal's market size is nearly $8.5 billion and Bhutan's is $1 billion.

Citing BBIN, Raihan said India should play a more generous role, particularly to ensure access of products from these three countries to its market and to facilitate increased intra-regional trade.

There is sizeable scope to increase bilateral trade even among these smaller countries, although Bangladesh, Bhutan and Nepal primarily aim to increase their export to the Indian market, he added.

But the NTMs, POs and a lack of trade facilitation are responsible for high transaction costs in bilateral trade among the South Asian countries, according to the organisation. Streamlining the NTMs and removal of POs may intensify further market integration in the BBIN sub-region through the development of regional value chains.

"This will also encourage larger intra and extra regional investments in the BBIN sub-region, which can be instrumental in growth integration among these countries," said the paper.

Citing the BBIN Motor Vehicle Agreement, Raihan said there are some signs of heightened commitments among the political elites of the BBIN countries to make the initiative effective.

Large infrastructural development is needed along with resolution of issues related to NTMs and POs to make this happen, according to the organisation.

It suggested improvement of roads, port infrastructure, customs services and a reduction of costs to facilitate trade. Integrated Check Posts (ICPs) at land ports can be established, it said.

SANEM also recommended exporters in Bangladesh, Bhutan and Nepal should develop their capacities to meet international standard requirements and become more competitive.

It also recommended cooperation, particularly among the standards organisations, for harmonisation of standards.

"Finally, there is a need to put much weight on regional investment and trade nexus," said Raihan, adding that promotion of intra-regional investments in energy and infrastructure will be a key driver for greater success in the BBIN sub-region.

Rich countries may take lead in recession-proof debt project

REUTERS, *London*

SOME of the world's most advanced economies may club together to sell growth-linked bonds, creating a market that could help avert future debt crises, sources familiar with discussions among Group of 20 policymakers told Reuters.

Countries like Britain and Germany could breathe life into an academic theory intended to offer poorer, emerging economies some respite if they fall on hard times. Growth-linked bonds allow a government's debt repayments to fluctuate during economic cycles - meaning it pays less if its revenues are hit by recession.

The only existing such bonds - sold by Argentina, Greece and most recently Ukraine - emerged from debt restructurings, as a way of coaxing creditors to accept writedowns. That has created a stigma which has put off other investors and borrowers alike.

But one source familiar with discussions between Group of 20 finance ministers and central bankers said developed countries are being urged to take the lead in creating a market for growth-linked bonds that will help improve their image.

REUTERS

A shop cash register is seen with both sterling and euro currency in the till at the border town of Pettigo, Ireland.

A second source said, "It is clear that emerging markets, at least absent leadership from elsewhere, are not going to be first movers here ... there could be a case for collective action." The G20 discussions were at "early stages", he said.

The Bank of England has been pushing the idea in recent years. It has published numerous papers, organised workshops and steered a market group to develop a legal framework or "term sheet", which is being tested with investors by the capital markets association ICMA. Term sheets create a market standard, contributing to the widespread use of new instruments.

Sources said the Bank of England has also helped get growth-linked debt on the G20's agenda. At a meeting of finance chiefs in July, the G20 called for further analysis of "state contingent debts, including GDP-linked bonds" and asked the International Monetary Fund to report on the subject in 2017.

For countries vulnerable to macroeconomic shock, the appeal of growth-linked debt is obvious. Most recently in early 2015, Greece proposed swapping debt held by its euro zone creditors for growth-linked bonds to help it break a vicious debt spiral.

But they can be a hard sell. Fund managers say they might struggle to match the returns on growth-linked bonds to the demands of their clients, who are used to the fixed-rate interest offered on most bonds.

The bonds also depend on economic data, which investors may or may not trust. Argentina, for example, spent years dodging payouts on its inflation-linked debt after reporting consumer prices that differed wildly from private estimates.

But Ali Abbas, who works in the debt policy division at the IMF, said the initial investor feedback on its review of growth-linked bonds had been promising.

"While noting the complexity of state-contingent instruments, some investors do appear to have interest in the idea of GDP-linked bonds and similar instruments, particularly because investors are looking for higher returns in an environment of record-low bond yields," he said.

The IMF aims to complete the review early next year, in time for the G20's spring meeting, Abbas said. Starla Griffin, a lawyer who worked with the Bank of England on the term sheet, said the issue of data integrity meant the first country to sell a GDP-linked bond must have a strong credit rating and be respected by investors.

"What this initiative is trying to do is to really try to get away from the stigma and show that in fact it is only the most credible issuers that can issue one of these," Griffin said.