STRONG INSTITUTIONS FOR GOOD GOVERNANCE

The need to transform the capital market

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It was not that derivatives did not work well, it was actually that they worked too well. To the extent that investors became too complacent about risk and reduced due diligence. In other words, it was absence of sufficient regulations and lack of transparency in trading these instruments which led to the financial crisis of 2008. In response, former US President Barack Obama unveiled the Dodd-Frank Act, a sweeping overhaul of financial regulations which brought heightened scrutiny, transparency as well as checks and balances to trading products like derivatives to protect people's money.

The lesson, then, for Bangladesh is pretty clear. Even before the necessary financial infrastructure including electronic trading systems to trade derivatives is setup in DSE, policy-makers will have to carefully outline a series of regulations that governs this market judiciously and allow market participants to contain systemic risk.

But above all, authorities will have to educate the public about the pros and cons of these financial products—derivatives, bonds and stocks alike. They will also have to coordinate better among themselves: our stock market's patchy history should remind us that lack of coordination between the securities regulator and the central bank led to dire consequences. 2010 should be a painful reminder.

Let us accept that policymakers face daunting challenges in their road towards creating a vibrant capital market, but sometimes the first steps are the hardest and it is those few steps which can pave the way for a modern financial system in Bangladesh.

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