Banking Sector Performance, Regulation and Bank Supervision

5.1 With a view to maintaining a sound, efficient and stable financial system; Bangladesh Bank (BB) has initiated a number of policy measures, giving augmented emphasis on risk management in the banks, the periodic review of stability of individual banks as well as the whole banking system, exercise of stress testing, inclusion of underserved/unserved productive economic sectors and population segments in the financial system, etc. Focus has also been made on Corporate Social Responsibility (CSR) and Green Banking activities, and a dedicated department has been formed to monitor the initiatives being undertaken by banks. A revised risk management guideline has already been put into effect for banks, aiming at developing more shock resilient capacity of banks in the future. The following paragraphs highlight the recent regulatory and supervisory measures initiated by BB for banks and financial institutions, the industry statistics, and performance of the banking sector.

A. Banking Sector Performance

5.2 The banking sector of Bangladesh comprises four categories of scheduled banks. These are State-owned Commercial Banks (SCBs), State-owned Development Financial Institutions (DFIs), Private Commercial Banks (PCBs) and Foreign Commercial Banks (FCBs).The number of banks remained unchanged at 47 in 2012. These banks had a total number of 8322 branches as of December 2012 compared to 7961 in December 2011. At the end of June 2013, the total number of banks and their branches increased to 55 and 8427 respectively due to opening of new PCBs and bank branches during the year (Appendix-4, Table-I). The structure of the banking sector, with a breakdown by type of banks, is shown in Table 5.1.

Table 5.1 Banking systems structure

(billion Taka)

Bank types	2011						2012					
	Number of banks	Number of branches	Total assets	Percent of industry assets	Deposits	Percent of deposits	Number of banks	Number of branches	Total assets	Percent of industry assets	Deposits	Percent of deposits
SCBs	4	3437	1629.2	27.8	1235.6	27.4	4	3478	1831.9	26.0	1377.9	25.5
DFIs	4	1406	328.8	5.6	214.4	4.8	4	1440	385.5	5.5	260.4	4.8
PCBs	30	3055	3524.2	60.0	2787.5	61.8	30	3339	4371.5	62.2	3430.7	63.6
FCBs	9	63	385.4	6.6	272.2	6.0	9	65	441.8	6.3	327.0	6.1
Total	**47**	**7961**	**5867.6**	**100**	**4509.7**	**100**	**47**	**8322**	**7030.7**	**100**	**5396.0**	**100**

Note: Banks prepare their balance sheet on calendar year basis, and are obliged to submit their audited balance sheet at the end of every calendar year. That is why banks' performance-related figures are stated in calendar year basis.

5.3 In 2012, the SCBs held 26.0 percent of the total industry assets as against 27.8 percent in 2011. The PCBs' share in the total assets of the banking sector is increasing

Chart 5.1

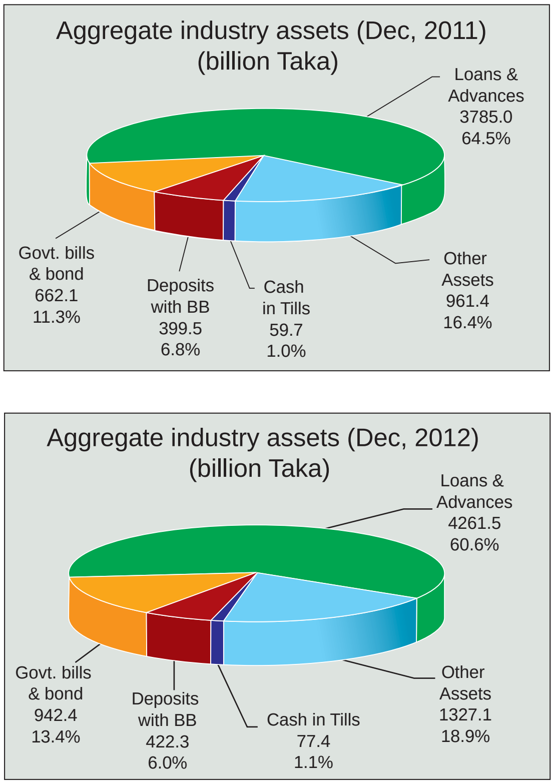
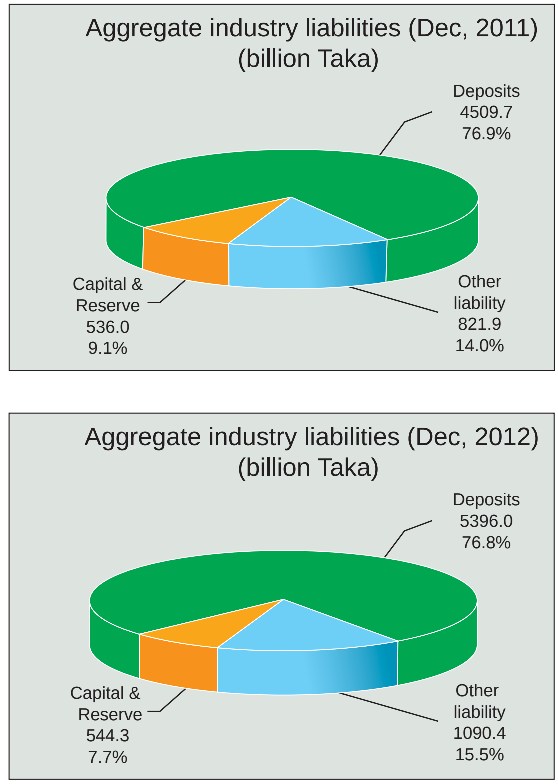


Chart 5.2



continuously over the last 12 years, showing a persistently faster growth than other subsectors. Their share rose to 62.2 percent in 2012, as against 60.0 percent in 2011. The FCBs held 6.3 percent of the industry assets in 2012, showing a decline by 0.3 percentage point over the previous year. The DFIs' share of assets was 5.5 percent in 2012 against 5.6 percent in 2011.

5.4 Total deposits of the banks in 2012 rose to Taka 5396.0 billion from Taka 4509.7 billion in 2011 showing an overall increase of 19.7 percent. The SCBs' share in deposits decreased from 27.4 percent in 2011 to 25.5 percent in 2012. PCBs' deposits in 2012 amounted to Taka 3430.7 billion or 63.6 percent of the total industry deposits against Taka 2787.5 billion or 61.8 percent in 2011. FCBs' deposits in 2012 slightly rose by Taka 54.8 billion over the year. The DFIs' deposits in 2012 were Taka 260.4 billion against Taka 214.4 billion in 2011, showing an increase of 21.5 percent over the year.

A. 1. Aggregate Balance Sheet

5.5 **Assets:** Aggregate industry assets in 2012 showed an overall increase of 19.8 percent over 2011. During this period, the SCBs' assets increased by 12.4 percent and those of the PCBs' increased by 24.0 percent. Loans and advances of Taka 4261.5 billion constituted the most significant portion (60.6 percent) of the sector's aggregate assets of Taka 7030.7 billion. Cash in hand including foreign currencies was Taka 77.4 billion; deposits with BB were Taka 422.3 billion; other assets were Taka 1327.1 billion and investment in government securities were Taka 942.4 billion (Chart 5.1).

5.6 **Liabilities and capital:** Deposits continued to be the main sources of funds of the banking industry and constituted 76.8 percent (Taka 5396.0 billion) of its aggregate liability and capital portfolio in 2012. Capital and reserves of the banks were Taka 544.3 billion (7.7 percent) in 2012, as against Taka 536.0 billion (9.1 percent) in 2011 (Chart 5.2). It is worth mentioning here that capital and reserves of the banks stood at Taka 498.6 billion at end June 2013.

A. 2. Capital Adequacy

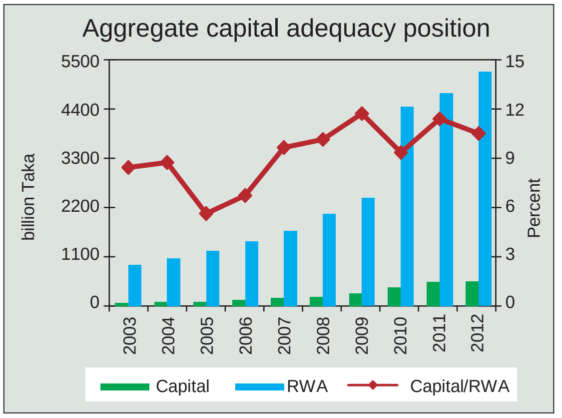
5.7 Capital adequacy focuses on the total position of banks' capital and the protection of depositors and other creditors from the potential shocks of losses that a bank might incur. It helps absorb all possible financial risks like credit risk, market risk, operational risk, residual risk, core risks, credit concentration risk, interest rate risk, liquidity risk, reputation risk, settlement risk, strategic risk, environmental & climate change risk etc. Under Basel-II, banks in Bangladesh maintain the Minimum Capital Requirement (MCR) at 10.0 percent of the Risk Weighted Assets (RWA) or Taka 4.0 billion in capital, whichever is higher. Under the Supervisory Review Process (SRP), banks are directed to maintain a level of "adequate" capital, which is higher than the minimum required capital and sufficient to cover all possible risks in their business. This higher level of capital for the banks is usually determined and finalised through dialogue between the SRP and the SREP (Supervisory Review Evaluation Process, the central bank's assessment) teams. The amount of capital was Taka 205.8 billion as on 31 December 2008 and it stood at Taka 498.9 billion as on 30 June 2013, amounting to a 142.3 percent capital growth.

Table 5.2 Capital to risk weighted assets ratio by type of banks

(percent)

Bank types	2005	2006	2007	2008	2009	2010	2011	2012	End June 2013
SCBs	-0.4	1.1	7.9	6.9	9.0	8.9	11.7	8.1	1.2
DFIs	-7.5	-6.7	-5.5	-5.3	0.4	-7.3	-4.5	-7.8	-9.0
PCBs	9.1	9.8	10.6	11.4	12.1	10.1	11.5	11.4	11.4
FCBs	26.0	22.7	22.7	24.0	28.1	15.6	21.0	20.6	20.3
Total	**5.6**	**6.7**	**9.6**	**10.1**	**11.6**	**9.3**	**11.4**	**10.5**	**9.1**

Chart 5.3



5.8 Table 5.2 shows that on 30 June 2013 in aggregate the SCBs, DFIs, PCBs and FCBs maintained a Capital Adequacy Ratio (CAR) of 1.2, -9.0, 11.4 and 20.3 percent respectively. However, individually, 4 SCBs, 2 PCBs, 1 FCB and 3 DFIs did not maintain the minimum required CAR. The CAR for the banking industry as a whole was 9.1 percent at end of June 2013 as against 10.5 percent at the end of 2012.

The CAR of the banking industry has decreased. The main reason for this deterioration is the implementation of BB's new guidelines (BRPD Circular No. 14/2012 and 19/2012) on loan classification & provisioning which were recently revised in line with international standards. As a result, the Risk Weighted Assets (RWA) as well as the classified loans of the banks have increased.

According to the Basel-II standard, the Basel Committee of Banking Supervision (BCBS) prescribed the CAR to be maintained at 8 percent. In Bangladesh, BB implemented a minimum CAR of 8.0 percent up to June 2010, 9.0 percent up to June 2011 and 10.0 percent from July 2011 onwards.

A. 3. Asset Quality

5.9 Loans and advances are the major components in the asset composition of all commercial banks. The high concentration of loans and advances increases the vulnerability of assets to credit risk. Other assets of banks include investments in bills, bonds, shares, etc., which constituted 27.2 percent of the total assets in 2012.

5.10 The most important indicator intended to identify the asset quality in the loan portfolio is the ratio of gross non-performing loans (NPLs) to total loans and net NPLs to net total loans. In 2012, FCBs have the lowest and DFIs have the highest ratio of gross NPLs to total loans. SCBs had a gross NPLs to total loans ratio of 23.9 percent, whereas PCBs, FCBs and DFIs, had ratios of 4.6, 3.5 and 26.8 percent respectively at the end of December 2012 (Table 5.3). The gross NPLs ratios to total loans for the SCBs, PCBs, FCBs and DFIs were recorded as 26.4, 6.6, 4.7 and 26.2 percent respectively at the end of June 2013.

Chart 5.4

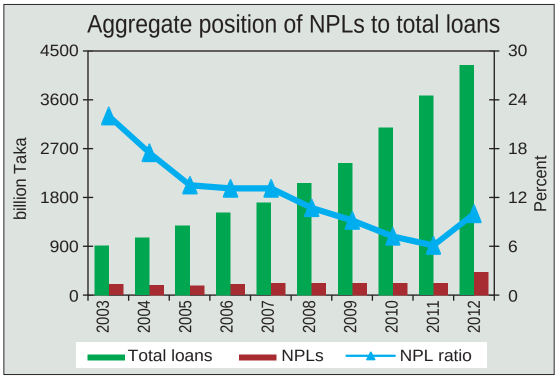


Table 5.3 NPL ratios by type of banks

(percent)

Bank types	2005	2006	2007	2008	2009	2010	2011	2012	End June 2013
SCBs	21.4	22.9	29.9	25.4	21.4	15.7	11.3	23.9	26.4
DFIs	34.9	33.7	28.6	25.5	25.9	24.2	24.6	26.8	26.2
PCBs	5.6	5.5	5.0	4.4	3.9	3.2	2.9	4.6	6.6
FCBs	1.3	0.8	1.4	1.9	2.3	3.0	3.0	3.5	4.7
Total	**13.6**	**13.2**	**13.2**	**10.8**	**9.2**	**7.3**	**6.1**	**10.0**	**11.9**

5.11 The ratio of NPL to total loans of all the banks had shown an overall declining trend from its peak (34.9 percent) in 2000 up to 2011 before it increased to 10.0 percent in December 2012. The ratio further increased to 11.9 percent at the end of June 2013 (Table-5.3). While the rise in the gross NPL ratio has been attributed in part to the high NPL of the SCBs and the DFIs, there has also been implementation of BBs new loan classification and provisioning guidelines, which have raised reported as well as intrinsic problem loan ratios.

5.12 The SCBs and DFIs continue to have high level of NPLs mainly due to substantial loans provided by them on considerations other than commercial criteria. Poor appraisal and inadequate follow-up and supervision of the loans disbursed by the SCBs and DFIs in the past eventually resulted in these poor quality assets. Furthermore, these banks were reluctant to write-off the historically accumulated bad loans because of poor quality of underlying collaterals. Recovery of NPLs, however, has witnessed some signs of improvement, mainly because of the steps taken with regard to internal restructuring of these banks to strengthen their loan recovery mechanism and recovery drive and write-off measures initiated in recent years.

5.13 Table 5.3(a) and Chart 5.4(a) show that in 2012, the ratio of net NPLs (net of provisions and interest suspense) to net total loans (net of provisions and interest suspense) was 4.4 percent for the banking sector and 20.4 percent for DFIs.

It is revealed in the table that DFIs' non-performing portfolios were still high after adjustment of actual provision and interest suspense, whereas SCBs, FCBs and PCBs had excess provision against their NPLs. The net NPLs to net total loans ratios were 8.1, 19.5, 2.4, 0.1 and 4.4 percent for the SCBs, DFIs, PCBs, FCBs and all banks respectively at the end of June 2013.

5.14 Chart 5.5 displays the amount of NPLs of the 4 types of banks since 2003 through 2012. The amount of NPLs of the SCBs increased from Taka 105.7 billion in 2003 to Taka 215.1 billion in 2012. The PCBs recorded a total increase of Taka 81.8 billion in their NPL accounts, which stood at Taka 130.3 billion in 2012 as against Taka 48.5 billion in 2003. The amount of NPLs of the DFIs increased to Taka 73.3 billion in 2012 from Taka 47.3 billion in 2003.

It can be seen from Chart 5.4(a) that the decline in NPLs to total loans ratio in recent years till 2011 can be attributed partly to some progress in recovery of long outstanding loans and partly to write-off of loans classified as 'bad' or 'loss'. But it went up again in 2012 due to the reasons of issuance of the circular regarding new classification and rescheduling of loans and a few notable scams in the banking industry.

Table 5.3 (a) Ratio of net NPL to total loans by type of banks

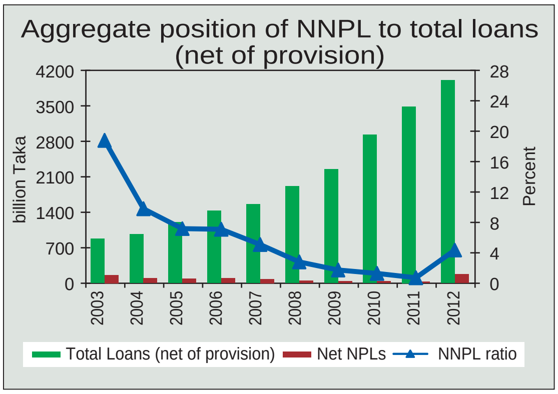
Bank	2005	2006	2007	2008	2009	2010	2011	2012	End June 2013
SCBs	13.2	14.5	12.9	5.9	1.9	1.9	-0.3	12.8	8.1
DFIs	22.6	23.6	19.0	17.0	18.3	16.0	17.0	20.4	19.5
PCBs	1.8	1.8	1.4	0.9	0.5	0.0	0.2	0.9	2.4
FCBs	-2.2	-2.6	-1.9	-2.0	-2.3	-1.7	-1.8	-0.9	0.1
Total	**7.2**	**7.1**	**5.1**	**2.8**	**1.7**	**1.3**	**0.70**	**4.4**	**4.4**

Table 5.4 Required provision and provision maintained -all banks

(billion Taka)

All banks	2005	2006	2007	2008	2009	2010	2011	2012	End June 2013
Amount of NPLs	175.1	200.1	226.2	224.8	224.8	227.1	226.4	427.3	523.1
Required Provision	88.3	106.1	127.2	136.1	134.8	149.2	148.2	242.4	299.0
Provision maintained	42.6	52.9	97.1	126.2	137.9	142.3	152.7	189.8	274.4
Excess(+)/ shortfall(-)	-45.7	-53.2	-30.1	-9.9	3.1	-6.9	4.6	-52.6	-24.6
Provision maintenance ratio (%)	48.2	49.9	76.3	92.7	102.3	95.4	103.0	78.3	91.8

Chart 5.4 (a)



5.15 Table 5.4 shows the aggregate amount of NPLs, the required loan loss provision and the actual provision maintained by the banks from 2005 to June 2013.

5.16 Table 5.4 and Chart 5.6 depict that in aggregate, the banks have been continuously failing to maintain the required level of provisions against their NPLs from 2003 through 2012 except in the year 2009 and 2011. Table 5.4 shows that in 2009 and in 2011, the banking sector was able to maintain 100 percent or more of the required provisions. Banks maintained 40.3 percent of the required provision in 2003; which increased thereafter to 103.0 percent in 2011. The main reasons for the shortfall in provision adequacy from 2000 through 2012 was the inability of some SCBs, DFIs and PCBs, including those in the problem bank category, to make sufficient provisions due to inadequate profits and transferred provisions for write-offs. Notably, the FCBs are in a much better position in that they have been able to make adequate provisions during the period under consideration. A comparative position of loan loss provisions as of end 2011, 2012 and June 2013 is shown in Table 5.5.

5.17 Twenty seven out of thirty PCBs were able to maintain the required provision, but the remaining 3 failed due to their poor asset portfolios and earning levels, at the end of December 2012.

5.18 **Writing off Bad Debts.** To correct an unnecessarily and artificially inflated size of the balance sheet, uniform guidelines of write-off were introduced in 2003. According to the policy, banks may, at any time, classify write-off loans as bad/loss. Those loans, which have been classified as bad/loss for the last 5 years and above and loans for which 100 percent provisions have been kept, should be written-off immediately. The total amount of written-off bad debts from June 2007 to June 2013 in different bank categories is given in Table 5.6.

Chart 5.5

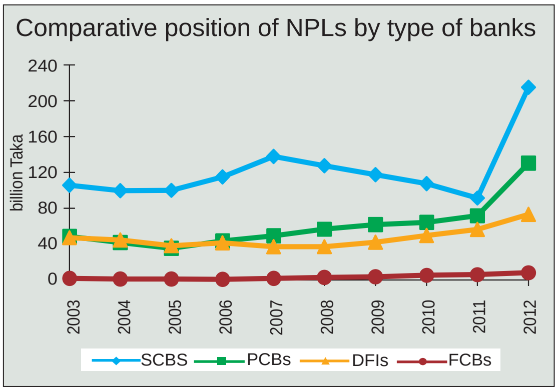


Chart 5.6

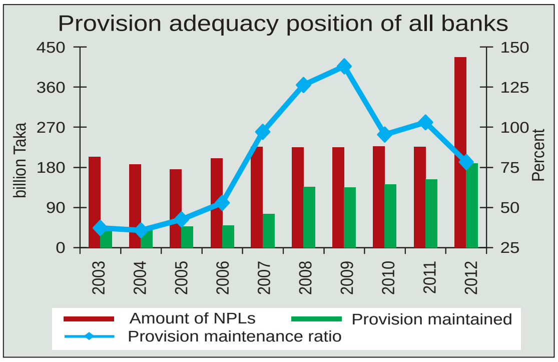


Table 5.5 Comparative position of provision adequacy

(billon Taka)

Year	Items	SCBs	SBs	PCBs	FCBs
2011	Required provision	60.8	21.7	58.3	7.4
	Provision maintained	69.0	13.9	61.2	8.5
	Provision maintenance ratio (%)	113.5	64.1	105.0	114.9
2012	Required provision	119.2	29.8	84.4	8.9
	Provision maintained	81.9	13.6	84.9	9.3
	Provision maintenance ratio (%)	68.7	45.7	100.6	104.3
30/06/13	Required provision	149.7	34.8	104.9	9.6
	Provision maintained	145.7	15.4	103.8	9.5
	Provision maintenance ratio (%)	97.4	44.3	98.9	98.2

A. 4. Management Soundness

5.19 Sound management is the most important and inescapable pre-requisite for the strength and concrete growth of any financial institution. Since indicators of management quality are primarily specific to individual institutions, these cannot be easily aggregated across the sector. In addition, it is difficult to draw any conclusion regarding management soundness based on quantitative indicators, as characteristics of a good management are rather qualitative in nature. Nevertheless, the total expenditure to total income, operating expenses to total expenses, earnings and operating expenses per employee, and interest rate spread are generally used to portray management soundness. Technical competence & leadership of mid and senior-level management, compliance with banking laws and regulations, adequacy and compliance of sound internal policies, the ability to plan and respond to changing circumstances, etc., are all also taken into consideration in evaluating the quality of management.

5.20 As evident from Table 5.7 and Chart 5.7, in 2012 the expenditure-income (EI) ratio of the DFIs was the highest among the displayed bank clusters, due to poor non interest income and higher operating expenses particularly incurred by BKB and RAKUB. The EI ratio of the PCBs was 76.0, the second highest, which could mainly be attributable to high administrative and operating expenses. The EI ratio of SCBs increased from 62.7 in 2011 to 73.2 in 2012.

Table 5.6 Writing-off bad debts in different bank categories

(billion Taka)

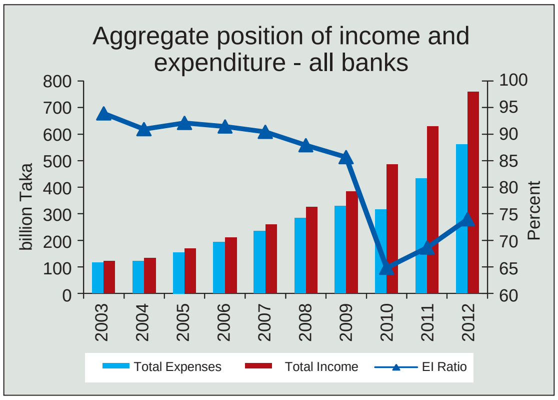
Bank types	30 June 07	30 June 08	30 June 09	30 June 10	30 June 11	30 June 12	30 June 13
SCBs	42.8	48.4	64.5	70.5	82.4	72.9	107.2
DFIs	30.4	31.0	31.8	31.8	32.0	24.5	32.6
PCBs	45.5	49.4	54.7	69.6	77.1	64.9	109.7
FCBs	1.6	1.7	2.0	2.1	2.4	2.6	3.7
Total	**120.3**	**130.5**	**153.0**	**174.0**	**193.9**	**164.9**	**253.3**

Table 5.7 Expenditure-income ratio by type of banks

(percent)

Bank types	2004	2005	2006	2007	2008	2009	2010	2011	2012
SCBs	102.3	101.9	100.0	100.0	89.6	75.6	80.7	62.7	73.2
DFIs	104.0	103.9	103.5	107.7	103.7	112.1	87.8	88.6	91.2
PCBs	87.1	89.3	90.2	88.8	88.4	72.6	67.6	71.7	76.0
FCBs	76.3	70.8	71.1	72.9	75.8	59.0	64.7	47.3	49.6
Total	**90.9**	**92.1**	**91.4**	**90.4**	**87.9**	**72.6**	**70.8**	**68.6**	**74.0**

Chart 5.7



A. 5. Earnings and Profitability

5.21 Strong earnings and profitability profile of a bank reflect its ability to support present and future sound operation, absorb future contingent shocks and strengthen resilience capacity. More specifically, earnings strongly

Table 5.8 Profitability ratios by type of banks

(percent)

Bank types	Return on assets (ROA)									Return on equity (ROE)								
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2004	2005	2006	2007	2008	2009	2010	2011	2012
SCBs	-0.1	-0.1	0.0	0.0	0.7	1.0	1.1	1.3	-0.6	-5.3	-6.9	0.0	0.0	22.5	26.2	18.4	19.7	-11.9
DFIs	-0.2	-0.1	-0.2	-0.3	-0.6	0.4	0.2	0.1	0.1	-2.1	-2.0	-2.0	-3.4	-6.9	-171.7	-3.2	-0.9	-1.1
PCBs	1.2	1.1	1.1	1.3	1.4	1.6	2.1	1.6	0.9	19.5	18.1	15.2	16.7	16.4	21.0	20.9	15.7	10.2
FCBs	3.2	3.1	2.2	3.1	2.9	3.2	2.9	3.2	3.3	22.5	18.4	21.5	20.4	17.8	22.4	17.0	16.6	17.3
Total	**0.7**	**0.6**	**0.8**	**0.9**	**1.2**	**1.4**	**1.8**	**1.5**	**0.6**	**13.0**	**12.4**	**14.1**	**13.8**	**15.6**	**21.7**	**21.0**	**17.0**	**8.2**

influence the capacity to absorb losses by building an adequate capital base, finance its expansion, and pay adequate dividends to its shareholders. Although there are various indicators of earnings and profitability, the most representative and widely used indicator is Return on Assets (ROA), which is supplemented by Return on Equity (ROE) and Net Interest Margin (NIM).

5.22 Earnings as measured by Return on Assets (ROA) and Return on Equity (ROE) differ greatly within the industry. Table 5.8 shows ROA and ROE by types of banks and Chart 5.8 shows the aggregate position of these two indicators for all banks. Analysis of these indicators reveals that the ROA of the SCBs was less than the industry average. The ROA of SCBs was gradually increasing up to 2011, but it dropped down to 0.6 percent in 2012 due to a huge net loss in 2012. The DFIs' situation is not getting better due to persistent operating losses incurred by BKB and RAKUB. PCBs' ROA shows a consistently strong position up to 2010, but the ROA positions of PCBs' slightly dropped in 2011 and 2012 due to a decrease of net profit during the period. FCBs' ROA has been consistently strong during the last couple of years.

Chart 5.8

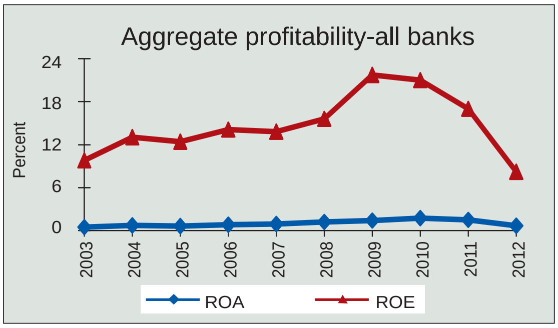


Table 5.9 Net interest income by type of banks

(billion Taka)

Bank types	2005	2006	2007	2008	2009	2010	2011	2012
SCBs	7.7	9.0	7.4	7.9	12.1	19.8	34.3	14.9
DFIs	1.0	1.7	1.4	1.9	1.9	6.2	4.9	4.7
PCBs	21.0	25.4	36.1	48.5	56.7	82.8	91.4	114.7
FCBs	5.6	8.2	9.9	12.6	10.7	13.0	16.1	19.6
Total	**35.3**	**44.3**	**54.8**	**70.9**	**81.5**	**121.9**	**146.7**	**153.8**

5.23 SCBs' ROE increased to 19.7 percent in 2011 from 18.4 percent in 2010. However, it dropped to 11.9 percent in 2012, due to an increased amount of provisioning required against an increased amount of NPLs. In the case of DFIs, the ROE was still negative in 2012. The ROE of PCBs has been robust for last five years. The ROE of FCBs showed gradual declines in 2010 and 2011, due to an increase of equity. The ROE of FCBs in 2009

Table 5.10 Liquidity ratio by type of banks

(Percent)

Bank types	Liquid assets									Excess liquidity								
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2004	2005	2006	2007	2008	2009	2010	2011	2012
SCBs	22.8	20.0	20.1	24.9	32.9	25.1	27.2	31.3	29.2	6.8	2.0	2.1	6.9	14.9	17.6	8.2	12.3	10.2
DFIs	11.2	11.2	11.9	14.2	13.7	9.6	21.3	6.9	11.5	4.7	6.2	3.8	5.6	4.9	7.1	2.3	1.3	1.4
PCBs	23.1	21.0	21.4	22.2	20.7	18.2	21.5	23.5	26.3	8.8	5.1	5.6	6.4	4.7	5.3	4.6	6.6	9.5
FCBs	37.8	41.5	34.4	29.2	31.3	31.8	32.1	34.1	37.5	21.9	23.6	16.4	11.2	13.3	21.8	13.2	15.3	18.7
Total	**23.4**	**21.7**	**21.5**	**23.2**	**24.8**	**20.6**	**23.0**	**25.4**	**27.1**	**8.7**	**5.3**	**5.1**	**6.9**	**8.4**	**9.0**	**6.0**	**8.4**	**9.9**

stood at 22.4 percent, which fell to 17.3 percent in 2012.

5.24 **Net Interest Income.** Aggregate net interest income (NII) of the industry has consistently increased from Taka 35.3 billion in 2005 to Taka 153.8 billion in 2012. However, the NII of the SCBs was a negative Taka 1.1 billion in 2004 and started to become positive (Taka 7.7 billion) only from 2005. In 2012, the NII of SCBs was Taka 14.9 billion. The DFIs had a positive trend since 2002 reaching Taka 4.7 billion in 2012.

5.25 Since 2005, SCBs have been able to increase their net interest income (NII) by reducing their cost of funds up to 2011. In 2012, the NII of SCBs dropped, due to higher interest expenses which grew faster than interest earnings.

The NII of the PCBs has been incredibly high over the period from 2005 through 2012. Overall industry NII shows a consistently upward trend. The trend of NII may indicate that the PCBs and FCBs' interest spreads were higher than that of SCBs and DFIs.

A. 6. Liquidity

5.26 Currently the scheduled commercial banks have to maintain a CRR (Cash

Chart 5.9

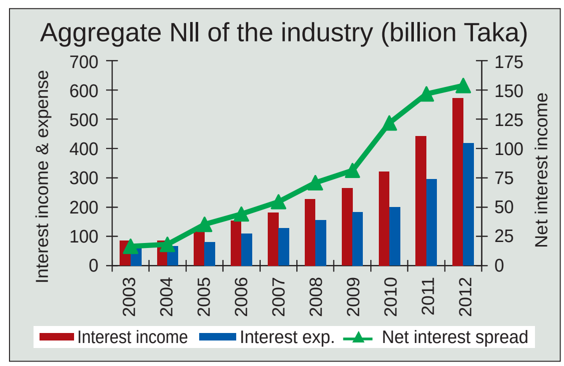
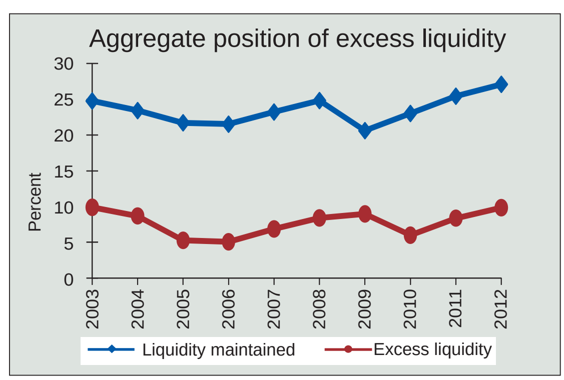


Chart 5.10



Reserve Ratio) averaging 6.0 percent daily on bi-weekly basis against Average Total Demand and Time Liabilities (ATDTL) of the preceding 2nd of the month, with an obligation to maintain a daily minimum 5.5 percent cash against the same ATDTL hold by the bank. The current rate of SLR (Statutory Liquidity Reserve) for conventional banks is 19.0

percent (inclusive of CRR) of time and demand liabilities. In case of Islamic Shariah-based commercial banks and conventional banks that have Islamic branches, the rate of SLR is 11.5 percent (inclusive of average 6.0 percent CRR on bi-weekly basis and at least 5.5 percent in any day) of their time and demand liabilities. The specialised banks (except Basic Bank Ltd) are exempted from maintenance of SLR, but they have to maintain the CRR at the stated rate. The banks maintain CRR cash with Bangladesh Bank. However, they are allowed to hold government approved securities (unencumbered portion) for maintenance of the SLR.

5.27 Table 5.10 and Chart 5.10 show that the FCBs have the highest liquidity ratios followed by the SCBs. There is an increasing trend in the percentage of liquid assets in total assets of the banks during the last two years.

A. 7. CAMELS Rating

5.28 CAMELS rating is a supervisory tool to identify those banking companies which have problems and require increased supervision. Under this rating system, banking companies are assigned two sets of ratings- (i) performance ratings, based on six individual ratings that address six components of CAMELS (Capital, Assets, Management, Earnings, Liquidity and Sensitivity to Market Risk); and (ii) an overall composite rating, based on a comprehensive assessment of the overall condition of the banking company. Both the ratings are expressed by using a numerical scale of "1" to "5" in ascending order of supervisory concern, "1" representing the best rating, while "5" indicating the worst. Any bank rated 4 or 5, i.e., 'Marginal' or 'Unsatisfactory' under the composite CAMELS rating is generally identified as a problem bank, the activities of which are closely monitored by the BB.

5.29 BB introduced the Early Warning System (EWS) of supervision from March 2005 to address the difficulties faced by the banks in any of the areas of CAMELS. Any bank found to have faced difficulty in any areas of operation, is brought under the Early Warning category and monitored very closely to help improve its performance. Presently, no banks are monitored under EWS.

5.30 As of end 2012, the CAMELS rating of 3 banks were 1 or Strong; 29 banks were rated 2 or Satisfactory; rating of 6 banks were 3 or Fair; 6 banks were rated 4 or Marginal and 3 banks received 5 or Unsatisfactory rating.

A. 8. Operations of Banks in Urban and Rural Areas

5.31 The number of branches and outstanding deposits and advances in the banking system classified by rural and urban area are displayed in Table 5.11. At end December 2000, the number of rural branches was 3659 (59.8 percent of total branches), which increased to 4827 (57.3 percent of total branches) at end of June 2013. The number of branches in urban areas increased from 2460 (40.2 percent of total branches) as of end December 2000 to 3600 (42.7 percent of total branches) at end June 2013. The number of rural branches increased at a lower rate compared with the number of urban branches.

Table 5.11 : Branch, deposit and advance in the banking system - rural and urban

(billion Taka)

Year	Number of Branch*			Deposit**			Advance**		
	Rural	Urban	Total	Rural	Urban	Total	Rural	Urban	Total
2000	3659	2460	6119	160.6	549.2	709.8	100.1	493.5	593.6
2001	3680	2502	6182	160.2	656.3	816.5	97.2	590.6	687.8
2002	3693	2538	6231	177.6	753.2	930.8	100.0	667.7	767.7
2003	3694	2526	6220	190.8	883.3	1074.1	102.5	744.8	847.3
2004	3724	2579	6303	192.0	1023.8	1215.8	103.4	847.9	951.3
2005	3764	2638	6402	218.3	1197.6	1415.9	117.6	999.7	1117.3
2006	3834	2728	6562	241.5	1445.8	1687.3	128.4	1163.3	1291.7
2007	3894	2823	6717	263.0	1689.1	1952.1	130.1	1335.6	1465.7
2008	3981	2905	6886	306.2	2009.8	2316.0	148.5	1667.0	1815.5
2009	4136	3051	7187	369.9	2424.0	2793.9	169.6	1920.9	2090.5
2010	4393	3265	7658	436.9	2942.3	3379.2	206.9	2367.5	2574.4
2011	4551	3410	7961	536.0	3579.9	4115.9	254.5	2958.3	3212.8
2012	4760	3562	8322	853.1	4011.0	4864.1	405.6	3453.7	3859.3
2013 (June)	4827	3600	8427	1030.9	4690.2	5721.1	434.3	3813.8	4248.0

Note : * As of end December. ** As of end June.

Total deposits of rural branches increased to Taka 1030.9 billion (18.0 percent of total deposits) at end June 2013 from Taka 160.6 billion (22.6 percent of the total deposits) as of end June 2000. The amount of urban deposits increased to Taka 4690.2 billion (82.0 percent of total deposits) at end June 2013 compared to Taka 549.2 billion (77.4 percent of total deposits) as on 30 June 2000. The amount of advances in rural areas increased from Taka 100.1 billion as of end June 2000 to Taka 434.3 billion at end June 2013. However, the share of rural advances decreased to 10.2 percent as of end June 2013 from 16.9 percent of the same period in 2000. The amount of urban advances increased from Taka 493.5 billion (83.1 percent of total advances) at end June 2000 to Taka 3813.8 billion (89.8 percent of total advances) as on 30 June 2013.

A. 9. Islamic Banking

5.32 Alongside the conventional interest-based banking system, Bangladesh entered into an Islamic Banking system in 1983. In FY13 out of 47 banks in Bangladesh, 7 PCBs operated as full-fledged Islamic banks, and 16 conventional banks (including 3 FCBs) were involved in Islamic banking through Islamic banking branches. The Islamic banking industry continued to show strong growth since its inception in 1983 to December 2012, in tandem with the growth in the economy, as reflected by the increased market share of the Islamic banking industry in terms of assets, financing and deposits of the total banking system. A brief picture is given in Table 5.12. Total deposits of the Islamic banks and Islamic banking branches of the conventional banks stood at Taka 1017.9 billion at end December 2012. This was 18.9 percent of deposits of the total banking system at the end of December 2012. Total credit of the Islamic banks and the Islamic banking branches of the conventional banks stood at Taka 910.1 billion at end December 2012. This was 21.1 percent of the credit of the total banking system of the country.

Table 5.12 Comparative position of the Islamic banking sector (as of end December 2012)

(billion Taka)

Particulars	Islamic banks		Dual banking (Conventional+ Islamic)		Islamic banking sector		All banking sector	
	2012	2011	2012	2011	2012	2011	2012	2011
1	2		3		4=2+3		5	
Number of banks	7	7	16	16	23	23	47	47
Deposits	961.2	751.2	56.7	56.2	1017.9	807.4	5396.0	4509.7
Credits	858.9	693.0	51.2	45.8	910.1	738.8	4318.6	3642.6
Credit deposit ratio	89.4	90.9	90.3	81.4	89.4	172.3	76.6	80.8
Liquidity: excess(+)/shortfall(-) @	51.0	31.0	0.8	0.5	51.9	31.5	505.4	358.5

@ Conventional banks which have Islamic banking branches do not maintain SLR individually.
The head offices of the respective bank maintain combinedly SLR and liquidity position.

B. Legal Framework and Prudential Regulations

B.1. Amendments to the Banking Companies Act

5.33 In FY13, BB continued to participate actively in a working group to amend the Banking Companies Act (1991), the aim of which was to strengthen BB's regulatory powers over the banking sector. (The Amendments were submitted to the Parliament during FY13, and were ultimately enacted in the first month of FY14.)

5.34 As part of the ongoing efforts to strengthen the banking system through the adoption of policies aimed at both improving the financial strength of banks as well as bringing greater transparency in their operations, several policy measures were initiated during FY13.

B.2. Risk Based Capital Adequacy (RBCA) for Banks

5.35 BB introduced the Risk Based Capital Adequacy (RBCA) framework for banks from January 2010 as regulatory compliance. Under the new capital adequacy framework, BB is entrusted with ensuring that banks are accurately assessing all material risks they are exposed to and maintaining the required capital commensurate with their risk profile. Pertinently, banks have been instructed to raise their capital to Taka 4.0 billion of which paid up capital shall be a minimum Taka 2.0 billion with effect from 11 August 2011. Moreover, BB reviewed the minimum regulatory Capital Adequacy Ratio (CAR) and the Minimum Capital Requirement (MCR) of the banks in the year 2010 through revising the existing RBCA policy and banks' past capital adequacy reporting. Banks are required to maintain the CAR at greater than or equal to 10 percent of Risk Weighted Assets (RWA) from July 2011. According to Pillar-1 of Basel-II, RWA of banks is calculated against credit risk, market risk, and operational risk. Banks are instructed to submit their Capital Adequacy Statement at the end of each quarter to BB. BB is now on the move to implement the Supervisory Review Process of RBCA framework. The key principle of the Supervisory Review Process (SRP) is that "banks have a process for assessing overall capital adequacy in relation to their risk profile and a strategy for maintaining their capital at an adequate level". Banks are now instructed to form a SRP team, where the risk management unit is an integral part, and to develop a process document called Internal Capital Adequacy Assessment Process (ICAAP) for assessing their overall risk profile and an adequate requirement of capital. Adequate capital means enough capital to compensate for all the risks in their business. Basel II has linked capital to the level of risk management. Therefore, banks should have "best practice" risk management techniques in monitoring and managing their risks.

5.36 The Supervisory Review Evaluation Process (SREP) of BB includes dialogue between BB and the bank's SRP team, followed by findings/evaluation of the bank's ICAAP. During the SRP-SREP dialogue, BB will review and determine any additional capital that would be required of banks on the basis of quantitative as well as qualitative judgment. To facilitate the dialogue, a revised evaluation process was prepared by BB in May 2013. On the basis of the revised process document and return format, banks have been advised to submit their quantitative information regarding ICAAP based on 31 December 2011 and 31 December 2012. Under the process document, BB provided guidance to calculate required capital against residual risk, credit concentration risk, interest rate risk, liquidity risk, reputational risk, settlement risk, strategic risk, appraisal of core risk management practice, environmental & climate change risk and other material risks in a specified format and submit the same to BB. In this process, information of banks' ICAAP would be counter checked with the information available from both on-site inspection and off-site supervisory departments of BB. During the SRP-SREP dialogue, if the bank fails to produce their own ICAAP backed by proper evidence and rigorous review regarding risk management, the SREP team of BB would apply their prudence and also use the available information from the inspection departments in determining the adequate capital.

B.3. Loan Classification and Loan-Loss Provisions

5.37 Near the end of FY12, BB significantly strengthened its policies on loan classification and loan-loss provisions. BB also introduced and clarified the difference between a "defaulted loan," which is a legal concept granting the bank the right to take certain actions against the borrower, and a "classified loan," which is an accounting concept that implies a certain required level of provisioning for expected losses. As a result, during FY 2013, banks endeavoured to meet the new requirements (see subsection A.3. above).

B. 4. Corporate Governance in Banks

5.38 Liquidity and solvency problems caused by poor governance in banks can have harmful systematic consequences in the broader economy reliant on banks for credit and payment services. High priority is, therefore, accorded to corporate governance in banks, putting in place checks and balances comprising a mix of legal, regulatory and institutional provisions specifying the roles and accountabilities of the Board, the executive management, external and internal audit, disclosure, and transparency prescriptions. BB has taken several measures in recent past to put in place good corporate governance in banks. These include: a "fit and proper" test for appointment of chief executive officers of PCBs, specifying the constitution of audit committee of the Board, enhanced disclosure requirements, etc. In continuation of the above reforms, the roles and functions of the Board and Management were redefined and clarified with a view to specifying the powers of the management and restricting the intervention of directors in day-to-day management of the bank. (In this connection, it is noteworthy that at the end of FY13 amendments of the related clauses of the Bank Company Act, 1991 have been placed in the parliament for final approval.)

C. Consumer Protection Regulations

C.1. Rationalisation of Schedule of Charges

5.39 Bangladesh Bank has rationalised the charges of some services to protect the interest of depositors/ investors/ customers and advised all scheduled banks to display the complete schedule of charges in suitable visible places in their branches and head offices and upload the same in their respective websites for the convenience of the customers. In the interest of small depositors it has been decided that no charge can be imposed as account maintenance fee for an average deposit balance up to Taka 5000. It has also been decided that a maximum of Taka 100 may be imposed as an account maintenance fee for average deposit balances up to Taka 25000, and a maximum Taka 300 for average balances above Taka 25000 on a six-month basis.

C. 2. Rationalisation of Rate of Interest

5.40 The cap on the rate of interest on lending in all sectors other than pre-shipment export credit (7.0 percent) and agricultural credit (13.0 percent) has been withdrawn. Banks are advised to limit the difference between the lending rate and the weighted average rate of interest on deposit, or intermediation spread, to the lower single digits in different sectors, other than the high risk consumer credit (including credit card), and SME loans. Banks are allowed to differentiate the interest rate up to a maximum of 3.0 percent in consideration of the diverse risk elements applicable to borrowers in the same lending category. Banks have been advised to announce the mid-rate of the interest rate for different sectors and they may change a lower or higher interest rate of up to 1.5 percent around this pre-announced mid-rate based on the comparative credit risk for each customer. Banks have also been advised to upload their deposit and lending interest rates on their respective websites.

D. Regulations to Promote Financial Inclusion and Socially-Responsible Financing

D.1. Policy Guidelines for Green Banking

5.41 Bangladesh is one of the many countries vulnerable to adverse impacts from climate change. Financial institutions of

Bangladesh can play an important role to prevent and mitigate environmental degradation. Comprehensive policy guidelines for Green Banking have been issued with a view to developing a strong and environment friendly banking system. The top ten banks have been graded based on their overall Green Banking activities. More emphasis has been given on the bank`s operational policy, as reflected in the allocation of its budget for promoting Green finance, environmental risk rating, and expansion of programmes to foster greater access to online banking, ATM, internet and Mobile/SMS banking. In-house activities covering building an inventory of savings on utilities and energy, encouraging Green marketing, enhancing capacity building and disclosure of the bank's practices are considered part of Green activities.

5.42 Bangladesh Bank has set up a new department, namely, Green Banking and CSR Department, for implementing the guideline of Green Banking, managing the funds of the refinance schemes regarding green activities, and initiating and promoting financial inclusion activities.

D.2. Guidelines on Environmental Risk Management (ERM)

5.43 A detailed guideline on Environmental Risk Management (ERM) has been introduced to assess environmental risk along with the credit risk in the overall credit risk methodology prior to the disbursement of the loan/credit facility.

D. 3. Bank Account for Farmers

5.44 A farmer can open an account by depositing Taka 10 only at any state owned commercial and specialised bank, against his or her national ID card/birth registration card and 'agricultural equipment assistance card' issued by the Department of Agricultural Extension. There are no provisions for maintaining a minimum balance on the said account, and banks shall not impose any charges/fees on these accounts. Due to the close monitoring of BB, the number of farmers' accounts has gone up to 9,632,731 as of end-June 2013.

D. 4. Bank Account for Unemployed Youth

5.45 An unemployed youth can open a bank account by depositing Taka 50 at any scheduled bank under the National Services Programme.

D. 5. Bank Account for Hardcore Poor

5.46 A hardcore poor person can open a bank account by depositing Taka 10 only at any state owned commercial and specialised bank against his or her national ID card and registration card issued by the Ministry of Food & Disaster Management. There are no provisions for maintaining minimum balance on the said account and banks shall not impose any charges/fees on these accounts.

D. 6. Bank Account for Freedom Fighters

5.47 A freedom fighter can open a bank account by depositing Taka 10 only at any state owned commercial and specialised bank against his or her national ID card and Payment Receipt Book for freedom fighter's allowance. There are no provisions for maintaining minimum balance on the said account and banks shall not impose any charges/fees on these accounts. The total number of freedom fighters' accounts is 109,999 as of end-June 2013.

D.7. Bank Account for Beneficiaries under Social Security Programme

5.48 Beneficiaries under the Social Security Programme can open bank account by depositing Taka 10 only at any state owned commercial and specialised bank against his or her national ID card and Payment Receipt Book containing Pension Payment Order (PPO) for the beneficiaries. There are no provisions for maintaining minimum balance on the said accounts and banks shall not impose any charges/fees on these accounts. Transactions may also be carried on through vouchers in case of insufficiency of check books. Total number of accounts for beneficiaries under Social Security Programme is 2,663,720 as of end-June 2013.

D.8. Banking Services for Physically Handicapped People

5.49 Banks have been advised to designate an official as 'Focal Point' at each branch of their bank with a view to making the banking services beneficial and easily accessible to the physically handicapped people.

D.9. Corporate Social Responsibility (CSR)

5.50 All banks had undertaken CSR practices in different forms in 2012. As shown in Table 5.13, the CSR expenditure in 2012 was higher than that in 2011 and around six times higher than 2009. As in preceding years, CSR initiatives of banks continued in 2012, which focused on i) financial inclusion of less privileged population segments and underserved economic sectors; ii) emergency relief in humanitarian distresses; iii) promotion of health, education and cultural/recreational activities for advancement and well-being of underprivileged population segments; iv) promotion of environmentally-friendly projects; and v) adoption of energy efficient, carbon footprint-reducing internal processes and practices in own offices and establishments.

Table 5.13 CSR Expenditures of banks during 2008 to 2012

(millon Taka)

Year	2008	2009	2010	2011	2012
CSR Expenditure	410.7	553.8	2329.8	2188.3	3046.7

5.51 Besides CSR initiatives involving direct expenditure, all banks participated actively in promoting SMEs and agricultural financing. PCBs were particularly active in these areas. Banks proceeded ahead on multiple fronts including presence of increased rural bank branches for broader, deeper financial inclusion, mobile phone banking, and opening of bank accounts with Taka 10 as initial deposit for farmers/poor/ultra poor and thereby increasing transactions in these bank accounts.

E. Supervision of Banks

5.52 With a view to promoting and maintaining soundness, solvency and systematic stability of the financial sector as well as to protecting interest of depositors, BB carries out two types of supervision namely (i) on-site inspection and (ii) off-site monitoring. The Department of Off-site Supervision (DOS) is vigilant to conduct off-site monitoring of banks. Some of the operations of DOS were discussed in earlier sections of this chapter; namely, assessing compliance with minimum requirements for capital, liquidity, provisioning, etc. The details of on-site supervision are given below:

E.1. On-site Inspection of Banks

5.53 As part of Bangladesh Bank's statutory function, currently six departments of BB namely Department of Banking Inspection-1 (DBI-1), Department of Banking Inspection-2 (DBI-2), Department of Banking Inspection-3 (DBI-3), Department of Foreign Exchange Inspection (DFEI), Financial Integrity and Customer Services Department (FICSD), and Bangladesh Financial Intelligence Unit (BFIU) are conducting inspection activities. These six departments conduct on-site inspection on SCBs, DFIs, PCBs (including banks under Islamic Shariah), FCBs and other institutions including the Investment Corporation of Bangladesh (ICB) and money changers. These departments conduct different types of inspection which may be summarised in three major categories: (i) comprehensive/ regular/ traditional inspection; (ii) risk based/ system check inspection, and (iii) special/ surprise inspection. The broad objectives of on-site inspection are as follows:

- To promote soundness, solvency and systemic stability of the financial sector as well as to protect depositors' interests;
- To ensure safety, stability and discipline in the banking sector;
- To ensure compliance of banking laws, rules and regulations;
- To combat money laundering and terrorist financing activities;
- To evaluate quality and performance of bank management and Board of Directors;
- To identify weaknesses which are to be addressed to strengthen the banks; and
- To evaluate financial soundness and operational efficiency of the banks.

5.54 In a comprehensive inspection, the overall performance/ condition of the banks in areas such as capital adequacy, asset quality, liquidity, earnings, management competence, etc. are evaluated. Based on their performance, banks are rated from 1 to 5 grades in ascending order. The on-site inspection departments also monitor implementation of the suggestions or recommendations made in the inspection reports. Risk-based inspection is conducted to examine the compliance with the Core Risk Management Guidelines issued by BB as well as to evaluate and monitor risk management systems and control environment of the banks. The frequency of the inspection is annual and areas covered are risks associated with credit, internal control and compliance, asset liability management and information systems. Special inspections are conducted on the banks on specific/particular issue(s) as well as to investigate complaints received from the depositors, public or institutions.

5.55 Commercial banks having CAMELS rating between 3 and 5 are inspected every year. Banks rated 1 or 2 are inspected once in every two years. Based on the findings about provisions, income and expenditure entries, banks are asked to correct their final account. This system has been adopted to enhance the effectiveness of on-site inspection and reduce the time gap between on-site and off-site supervision.

5.56 During the period from 1 July 2012 to 30 June 2013, DBI-1 conducted inspection on 1411 branches of 36 banks including head offices. On the basis of 30 June 2012, a total of 189 branches of 7 banks (including head office) were inspected. At the same time, Core Risk Inspections were conducted on 8 banks that are under the jurisdiction of DBI-1 to review the progress of implementation of the core risk guidelines (Asset-Liability Management, Credit Risk Management, Information System Security and Internal Control & Compliance) issued by Bangladesh Bank. Head/Country Offices of the bank as well as one branch of each bank have been taken under the purview of the core risk inspection. On the basis of 30 September 2012, 262 branches including head offices of 9 banks were inspected. Head offices and 346 big branches of 20 banks were inspected on the basis of 31 December 2012. The banks were directed to arrange a tri-partite meeting with their Management Committee (MANCOM), inspectors of Bangladesh Bank and external auditors before finalisation of annual financial statements of the banks. The other 19 banks that were not inspected on the basis of 31 December 2012 were directed to submit statements of rescheduled, de-classified and written-off loans in prescribed formats, and these issues were discussed in a tri-partite meeting of the bank management, external auditors and the inspection team of Bangladesh Bank. Pre-opening inspections were conducted on the newly opened 9 banks, and on the basis of these inspection reports, banks were permitted to start their operational activities.

5.57 DBI-2 conducted comprehensive inspection on 557 bank branches including 8 head offices, 129 big branches and 420 small branches. At the same time a total number of 152 special inspections were conducted on state owned commercial banks and specialised banks, 25 risk-based inspections on 6 banks and 14 surprise inspections were conducted on 4 banks. The Department also conducted comprehensive inspections on 88 branches, 28 head offices and 14 special inspections among the 31 financial Institutions (FIs).

5.58 DBI-3 conducted a total of 818 comprehensive inspections on banks, including 5 head offices, 134 big branches, 679 small branches and 219 SME service centres, plus SME/Agriculture branches (including inspection on some of the branches of different banks involved in SME activities). At the same time a total number of 16 special inspections were conducted on 4 banks (including SME) and 7 risk based inspections on 2 banks.

5.59 DFEI conducts inspection on foreign trade financing, treasury functions and foreign exchange risk management of banks, foreign exchange transactions of banks and money changers. In FY13, the department conducted a total of 182 comprehensive inspections on banks, including 11 head offices and 124 authorised dealer branches. The department

Box 5.1

Bangladesh Bank's Role for Protecting Bank Customers' Interest

1.1 General customers of banks and financial institutions (FIs) used to find it difficult to air their grievances against banks/FIs. It was also not easy to get answers to queries relating to services provided by banks and FIs. In this regard, with a view to answering queries of customers related to banks/FIs and also to redressing any grievances promptly Bangladesh Bank launched a 'Help Desk' under the Foreign Exchange Inspection & Vigilance Department, Head Office, Bangladesh Bank on 16 March 2011. Later, the name of Help Desk has been converted to "Customers' Interest Protection Center" abbreviated as CIPC. Giving more importance to customer protection, a full-fledged department named Financial Integrity and Customer Services Department (FICSD) was formed in July 2012 by integrating the Customers' Interests Protection Center and Vigilance Division.

1.2 Customer Service Division of FICSD has been equipped with modern logistics i.e. phone, dedicated number (16236), fax, internet etc., so that aggrieved customers within and outside the country can submit their complaints. After getting complaints over telephone or by e-mail, CSD endeavors to dispose of those complaints as quickly as possible. FICSD also monitors the activities of "Complaint Cells" set up in all the head offices and regional offices of the scheduled banks, financial institutions and in the branch offices of Bangladesh Bank. To increase the awareness of customers, the auto hunting number (16236) was formally inaugurated by the Governor in the presence of all banks' representatives and journalists of print & electronic media in the BB conference hall and from the same day the short code was also advertised both in print & electronic media. Necessary measures have been taken to affix the **STICKER** containing the short code (16236) at the cash counter of each branch of banks & financial institutions so that customers can easily lodge their complaints when they are harassed. Arrangement has also been made to keep the **DESK DISPLAY** containing the short code (16236) on the table of the front desk officer of each branch of banks & financial institutions. The short code number is delivered to all the mobile phone users through SMS with the help of Bangladesh Telecom Regulatory Commission (BTRC). The Phone & FAX number, e-mail ID, address of the FICSD are also published in the web-site of Bangladesh Bank. Besides, a complainant can immediately lodge his grievances just filling up the electronic complaint form on the web-site of Bangladesh Bank. Apart from these, the short code number is advertised on the television & widely circulated on National Dailies after three months of interval for the benefit of financial customers and general public at large across Bangladesh.

1.3 During July 2012 to June 2013, Vigilance and Anti-Fraud Division handled 1323 complaints and so far 314 numbers of special inspections have been carried out during the period under review. Customer Services Division (CSD) also dealt with 4296 complaints during FY13 and disposed of 2941 complaints up to the satisfaction of the stakeholders. In the FY13, the amount of complaints handled increased by 70 percent than that of the previous FY12. The complaints so far handled during FY13 revealed that almost 38 percent of the total complaints remained concentrated among four state-owned commercial banks and the nature of complaints were about general banking, loans & advances, remittances, accepted bills (local & foreign), cards & ATM Booth, mobile banking and others.

1.4 The FICSD is aiming at preparing a comprehensive customer protection framework to ensure that customers have adequate access to information to bargain with banks and FIs. Under the customer awareness initiatives, the department has planned to increase publicity in print and electronic media for the benefit of customers and general public at grass root levels. FICSD is looking for alternative means for amicable settlement of disputes/complaints without reference to the court. FICSD is looking ahead to develop itself as a center of excellence for handling the customer grievances on a par with International standard in future.

also conducted 47 special inspections on foreign exchange risk management, 94 inspections on money changers and a good number of special inspections on foreign trade and foreign exchange related irregularities.

5.60 A special centre was formed under this department on 21 March 2011 named Customers' Interests Protection Centre (CIPC). Later, it was reconstituted as a department named Financial Integrity and Customer Services Department (FICSD) on 26 July 2012. FICSD is acting as a watchdog for spotting the early warning signs of internal and external fraud at banks and FIs, investigating frauds and making criminal referrals when necessary. This department is also continuing its efforts to promote security, efficiency, effectiveness, transparency and risk management of the information and communication technology (ICT) structures of banks and FIs.

5.61 During 12 July 2012 to 13 June 2013, 1323 complaints were received by the department. Out of them, 1009 cases were sent to banks and FIs for their opinion and necessary action. The respective banks and FIs have settled those cases accordingly. On the basis of the rest of the complaints so far received, 314 special inspections have been conducted and necessary actions have been taken based on the inspection reports.

5.62 Apart from the Customer Service Division of Head Office, the CIPCs established in 10 branch offices of Bangladesh Bank also deal with the complaints received from the bank customers of their respective areas.

5.63 In FY13, Bangladesh Financial Intelligence Unit (BFIU) the conducted system check inspections in 47 head offices and 141 bank branches under the core risk programme. The Department also conducted special inspection on 5 branches of 5 banks. Besides, some other special inspections are also conducted for further analysis of some STRs (Suspicious Transaction Reports). During FY13, 25 branches of 19 banks have been inspected for this purpose. In addition to this, on the basis of allegations/complaints received from different media, persons, organisations, some special inspections are also conducted to look into the matter. BFIU has conducted special inspections in 111 branches of 34 banks during FY13.

5.64 On the basis of the on-site inspections, BFIU has undertaken some corrective measures, including imposing fines on the non-compliant banks. Under the provision of the Money Laundering Prevention Act (MLPA), 2012, 8 banks have been fined for non-compliance of the Act during FY13.

E. 2. Off-site Monitoring of Banks

5.65 Off-site monitoring continued as a necessary complement to on-site inspection in FY13, with the introduction of new tools and procedures for more intensive and rapid analysis.

5.66 Quick Review Report

With the existing supervisory tools like CAMELS Rating, Stress Testing, Financial Projection Model etc., Bangladesh Bank started determining the financial position of the banks, quarterly through Quick Review Report. This report focuses on major risks existing in the bank and provides possible solutions to problems.

5.67 Reviewing Minutes

Minutes of the Board, executive committee, and audit committee meetings of all scheduled banks along with the appointed observers' reports have been reviewed in order to find out irregularities and violations of existing laws, regulations, circulars, policies, etc. Along with the minutes of the Board and executive committee meetings, banks have to submit information regarding the sanction of new loans, extension of existing loans, large loans, rescheduled loan & forced loans, as decided in the meeting, in BB's prescribed format. During 2012, on reviewing of 1,657 (703 board minutes, 316 audit committee minutes and 638 executive committee minutes) minutes, various gross irregularities and violations of banking laws, circulars, etc. were detected. Accordingly, the banks have been advised to regularise the same so that major financial indicators as well as the internal control system of the banks become regular and can achieve shock-resilient capacity.

5.68 SCB Monitoring Cell

With a view to developing the financial soundness and operational efficiency of the then-nationalised commercial banks, the Government of the People's Republic of Bangladesh (GoB) corporatised three of the state-owned commercial banks (Sonali, Janata and Agrani Bank Ltd.) in 2007. At the time of corporatisation, the cumulative loss of Sonali, Janata and Agrani Bank was transformed into Intangible Assets with a condition to amortise the losses within 10 years. Rupali Bank had earlier been converted into a public limited company on 14 December 1986. After restructuring, a positive impact in the financial indicators of these four banks was observed as the performance of the State-owned Commercial Banks (SCB) became comparatively better than that of the previous years. However, in these times, Bangladesh Bank is monitoring the SCBs closely under Memorandums of Understanding (MoUs) since 2003 signed with these banks. The MoUs encompass: Fixing a ceiling on the net loan growth and single borrower exposure limit; imposing a penalty for exceeding the net loan growth limit; limit for the growth of operating expenses and imposing restrictions on taking over loans from other banks without prior approval of Bangladesh Bank; a demand to reduce classified loans, to decrease court cases filed to recover bad loans and to reduce unadjusted entries of inter-bank reconciliation accounts; setting up a target on cash recovery from classified loans, focusing on agricultural and SME loans, ensuring better fund management, developing human resources, implementing Core Risk Management Guidelines and other corrective measures are incorporated in the signed MoUs. In the meantime, differentiated net loan growth targets have been given to SCBs based on their last year's performance. In addition, a special diagnostic examination has been done by Bangladesh Bank in the SCBs on Asset Quality, Liquidity Management and Internal Audit and Control system to find out the legacy lapses of these banks. Moreover, Bangladesh Krishi Bank (BKB) and Rajshahi Krishi Unnayan Bank (RAKUB) are also being monitored and reviewed under the MoUs of

FY12. The preparation of MoUs for BKB and RAKUB for FY14 is currently under process.

E. 3. Risk Management Activities of the Banks

5.69 The need for an efficient risk management framework is paramount in order to ensure the financial soundness of any bank. Therefore, to ensure robustness, efficiency and effectiveness of risk management systems and keep pace with international best practices for the banking sector, BB previously issued several prudent guidelines on risk management. This set includes six core risk management guideline, risk based capital adequacy, and stress testing. On 15 February 2012, BB issued another guideline called Risk Management Guideline for Banks which is a supplement to, and not a substitute for, those guidelines already issued before. This document promotes an integrated, bank-wide approach to risk management that will facilitate banks in adopting contemporary methods to identify, measure, monitor, and control risks throughout their institutions.

5.70 For better risk management practices, each scheduled bank was advised to form an independent Risk Management Unit (RMU) in June 2009. Banks were also instructed to prepare a Risk Management Paper (RMP), place the same in their regular monthly meeting of the RMU, and submit the RMP along with the minutes of the meetings (that is supposed to contain specific decisions based on the analyses/recommendations made in the risk management paper) to the Department of Off-site Supervision. For its part, the Department of Off-site Supervision has been focusing on effective analysis and reporting of the risk management activities of the banks.

5.71 In November 2012, DOS arranged several workshops with the active participation of all banks to develop awareness regarding risk management practices in banks. A model risk management paper and a questionnaire regarding the organisational set-up of risk management activities were provided in the workshop. The purpose of this model was to ensure minimum risk analysis in the RMP and to determine the actual risk exposure along with the organisational set-up of each bank. Subsequently, banks were also instructed to rename their RMU as Risk Management Division (RMD) and to appoint a Chief Risk Officer (CRO) from a senior management position (at least from the Deputy Managing Director level) with an aim to give more emphasis on risk management practices.

5.72 Based on the RMP according to the prescribed format (as a minimum requirement), DOS regularly evaluates the risk management activities of each bank and provides constructive recommendations to improve their conditions. Banks have to execute all the recommendations and submit their compliance report within a specified time frame.

5.73 Recently, a Risk Rating procedure has been developed to quantify all possible risks based on the available information in the RMP and other sources. This risk rating carries 15 percent weight in the Management component of CAMELS rating. Therefore, a bank's risk management practices will have a material effect on its CAMELS rating.

5.74 In addition to regular risk management activities, recently all the banks have been instructed to submit a self-assessment report on internal control systems which needs to be signed and counter-signed by the CEO/MD and the chairman of Audit Committee respectively (DOS Circular No. 17, Dated 07/11/2012). For this purpose, BB has formulated a reporting format with 53 questionnaires regarding anti-fraud internal controls and a statement of fraud and forgeries that have occurred during a period and the action taken against those incidences. The objective of this self-assessment process is to keep the operational risk at a minimum level by strengthening the internal control and compliance system of a bank.

E.4. Financial Stability and Macroprudential Supervision

5.75 In light of the global economic turmoil and the rapidly growing and evolving financial sector in Bangladesh, Bangladesh Bank created the Financial Stability Department (FSD) on 29 May 2012.

5.76 The Financial Stability Report is the major publication of this department. Since inception, this department has produced Financial Stability Report 2011 and the current issue of the same has already been prepared for publication. The department also engaged in continuous efforts to evaluate stress conditions through stress testing reports of bank and generating different industry-wide scenarios. To improve the understanding of the overall bank liquidity and solvency positions, the department is also going to implement the Financial Projection Model (FPM). This model has been developed through the technical assistance of the World Bank. The department is also working on the identification of Domestic Systemically Important Banks (D-SIBs), and on determination of a countercyclical capital buffer and a capital conservation buffer in line with Basel-III guidelines.

5.77 A macroprudential regulation framework and macro stress testing are additional tools that have been under development. This department has already produced an analytical framework to understand contagion effects and to identify the presence of cluster behavior among the banks and FIs.

F. Banking Sector Infrastructure for Financial Stability and Risk Management

F. 1. Deposit Insurance Scheme

5.78 The Deposit Insurance Scheme (DIS) is designed to minimise or eliminate the risk of loss of funds that the depositors may incur by placing funds with a bank that subsequently fails. The direct rationale for deposit insurance is customer protection. The indirect rationale for deposit insurance is that it reduces the risk of a systemic crisis involving, for example, panic withdrawals of deposits from sound banks and breakdown of the payments system. From a global point of view, deposit insurance provides many benefits and, over the long term, appears to be an essential component of a viable modern banking system.

5.79 In Bangladesh, DIS was first introduced in August 1984, in terms of "The Bank Deposit Insurance Ordinance 1984". In July 2000, the ordinance was repealed by an Act of parliament called "The Bank Deposit Insurance Act 2000". DIS in Bangladesh is now being administered by the said Act. In accordance to the Act, Bangladesh Bank (BB) is authorised to administer a fund called the Deposit Insurance Trust Fund (DITF). The Board of Directors of BB acts as the Trustee Board for DITF. The DITF is now being administered and managed under the guidance of the Trustee Board. In addition, Bangladesh Bank is a member of the International Association of Deposit Insurers (IADI).

5.80 In accordance with "The Bank Deposit Insurance Act 2000," the main functions of DITF are: collecting premium from all scheduled banks on a half yearly basis (30 June/31 December) and investing the proceeds in Government securities. The income derived from such investments is also credited to the DITF account for further investment. In case of winding up of an insured bank, as per said act, BB will pay to every depositor of that bank an amount equal to his/her deposits not exceeding Taka one hundred thousand.

5.81 To enhance the effectiveness of market discipline, BB has adopted a system of risk based deposit insurance premium rates applicable for all the banks effective from January-June 2007. Very recently the premium rate has been increased, effective from January-June 2013. Along with the scheduled banks, BB has also taken the initiative to bring the FIs under the umbrella of DIS, an initiative which is now under the consideration of the MoF.

5.82 The effectiveness of DIS in reducing systematic risk would surely increase if the public became well aware of its existence and scope.

Table 5.14 The recent position of DITF

Particulars	Unaudited Figure (as on 31 December 2012)	Premium Rate*
Total Fund	24.1 (billion Taka)	-
Total Investment	24.0 (billion Taka)	-
Covered Deposit of Total Insurable Deposit	35.25%	-
Fully insured Depositors	84.34%	-
Sound bank categories	-	0.08%
Early Warning Bank Categories	-	0.09%
Problem bank Categories	-	0.10%

* Effective from 2013.

5.83 With this end in mind, BB has already issued a circular regarding public awareness about DIS and more information and updates are available in the Bangladesh Bank website so that the general public can be informed on an ongoing basis about the benefits and capabilities of the DIS.

F. 2. Activities of Credit Information Bureau

5.84 Credit Information Bureau (CIB) was set up on 18 August of 1992 in Bangladesh Bank under the Financial Sector Reform Project (FSRP) of the World Bank. The main objective was to minimise the extent of potential default loans by facilitating the banks and financial institutions with credit reports of the loan applicants, so that the lending institutions can better estimate any credit risk while extending any lending or rescheduling facility.

5.85 CIB online services were opened up on 19 July 2011. The CIB database consists of detailed information on borrowers, owners and guarantors. It has brought huge advantages in CIB related operations over the previous system. The total number of borrowers was 844,404 at the end of June 2013, recording an increase of 18.9 percent over the previous period (710,020 as of end-June 2012).