Keys for the Development of Financial Service Sector of Bangladesh

Particularly looking at the Ongoing Negotiations on the GATS Financial Services Agreement (FSA) and it's effect on the financial sectors of Bangladesh

By

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Abstract

In this paper, I tried to capture the impact of ongoing negotiations on the GATS Financial Services Agreement (FSA) on the financial sectors of Bangladesh. The GATS FSA covers all additional measures unique to the financial services sector as the Annex on Financial Services and the Understanding on Commitments in Financial Services, popularly known as *Fifth Protocol.* Commitments in specific sectors are taken in the form of *four* different modes of supply referred to as *Mode 1- cross-border, Mode 2- consumption abroad, Mode 3- commercial presence and Mode 4- presence of natural persons*. At first, I presented a general overview of the financial service sector of Bangladesh including *banking sector, insurance sector* and *NBFI and* some problems regarding these sectors. I also examined the flexibilities offered by Modalities for Special Treatment for LDCs in GATS Negotiations and the opportunities for Bangladesh due to these modalities. Finally I recommended some measures to develop the recent scenario of financial service sector of Bangladesh.

Acronyms

LDC- Least Developed Countries

GATS- General Agreement on Trade and Services

WTO- World Trade Organization

NBFI- Non Banking Financial Institution

BB- Bangladesh Bank

FSA- Financial Services Agreement

NCB- Nationalized Commercial Bank

PCB- Private Commercial Bank

SB- State-owned Specialized Bank

IRS- Interest Rate Spread

BIA-Bangladesh Insurance Association

CCI-Chief Controller of Insurance

FDI- Foreign Direct Investment

PART-1: GENERAL FINDINGS

1. GATS and Bangladesh

1.1 Overview of GATS

The Uruguay Round (UR) of trade negotiations brought the trade in services, for the first time, within the ambit of the multilateral trade negotiations. The General Agreement on Trade in Services (GATS) is the first and the only multilateral agreement to bring under its purview the entire range of the services trade. The GATS divides services activities into 12 broad sectors – business; communication; construction and engineering; distribution; educational; environmental; financial; health; tourism and travel; recreational, cultural and sporting; transport; and other services not included elsewhere – and further sub-divides these l2 sectors into 161 sub-sectors.

1.2 Services Negotiations under GATS

GATS included a built-in agenda. Negotiations during the Uruguay Round were incomplete. Hence new negotiations began in January 2000. In March 2001, Negotiating Guidelines and Procedures were adopted by the WTO. Negotiations in GATS focus on three main areas:

1) Specific commitments on market access (MA) and national treatment (NT)
2) Unfinished agenda from the Uruguay Round on 'rules'
3) Implementation of Article IV relating to increasing the participation of developing countries in world trade in services.

As per the 2000 Guidelines, market access negotiations on services were initially following the *bilateral 'request-offer' approach*. Since the Hong Kong Ministerial Declaration, the services negotiations at the WTO have been mainly following the plurilateral approach. The Hong Kong Declaration mainly reiterated the principles and objectives of the GATS negotiations, especially relating to the development perspective: the right to regulate, the right to flexibility for developing countries and the special situation of LDCs. The rules relate to Domestic Regulation (Article VIA), Emergency Safeguard Measures (Article X), Government Procurement (Article XIII), and Subsidies (Article XV). Regarding the increasing participation by developing countries (GATS Article IV), clear provisions are laid down in the Negotiating Guidelines and Procedures (S/U93) adopted by WTO Members in March 2001[1].

1.3 Specific Commitments and Limitations

'Specific Commitments' apply *only to those services sectors* which are scheduled by a member in its GATS commitments. Two main pillars of the 'Specific Commitments' are obligations regarding Market Access (Article XVI) and National Treatment (Article XVII).

Market Access: Market access (MA) commitment for a sector or a sub-sector means that there should not be any limitations inscribed in the Member's schedule. However, if a Member wants to impose one or more restriction on MA, it may do so as long as it specifies them in its schedule of GATS commitments.

National Treatment: The National Treatment (NT) provision implies that the Member concerned does not discriminate between national and foreign providers for the sector or sub-sector where specific commitment has been made.

1.4 Requests Received by Bangladesh

Bangladesh has received requests from nine different countries for liberalizing its trade in services. The countries are Singapore, EC, Japan, Norway, Korea, Hong Kong (China), Malaysia, Sri Lanka, and U.S.A. Notably, India did not make any requests to Bangladesh. The requests cover 10 out of 12 sectors, and 127 sub-sectors out of the total of 161 sub sectors. The sectoral market access requests were limited to modes 1-3 (except in the case of telecoms), while there were national treatment requests on all sub-sectors. Under 'horizontal commitments', requests were made for mode 4 and on the removal of certain MFN exemptions in telecoms (For details see Box 2 of the present Report).

[1] "Study on the service sector of Bangladesh", published by The Bangladesh Trade Support Programme (BTSP)

1.5 Requests Made by Bangladesh

Bangladesh has so far not submitted initial GATS requests to trading partners, although reportedly the country during the negotiations prepared a request for special commitments for mode 4.

1.6 Offers Made by Bangladesh Under GATS

Bangladesh has so far made specific commitments in two sectors, namely, *Tourism and Travel-related services* during the Uruguay Round, and *Telecommunication services* after the completion of the Uruguay Round. A close look at Bangladesh's schedule will indicate that Bangladesh's liberalization commitment is very limited and largely favors the domestic suppliers. For example, commitments in modes 1 and 2 are unbound, and restrictions are imposed under modes 3 and 4 in both tourism and communication services.

1.7 Autonomous Liberalization of Financial Sector

Apart from undertaking liberalization commitments under the WTO, Bangladesh autonomously liberalized its financial sector as part of the country's economic reform programmes. There is no minimum domestic equity requirement and they are allowed to open branches with the permission of the Bangladesh Bank (BB). They have full access to credit from the BB, local financial markets, deposit insurance, and clearing facilities. They are free to take deposits from and grant loans to domestic companies and residents[2]. Foreign banks may also establish subsidiaries in Bangladesh with their own capital base. They require a license from the BB to operate a branch.

[2] WTO Document WT/TPR/S/168

2. The Financial Services Agreements (FSA) under the GATS

2.1 Introduction

The GATS FSA contains market opening commitments made as a result of global negotiations on financial services, including areas such as insurance, merchant and consumer banking. A key provision of the FSA is *the prudential carve-out*, which is not common for other services. It preserves the right of countries to maintain or introduce measures for prudential reasons, including for the protection of investors, depositors, policyholders or persons to whom a fiduciary duty is owed by a financial service supplier. The financial services deal also brings the financial sector under other general important disciplines of the WTO. For example, the dispute settlement and enforcement provisions of the WTO will also apply in case of FSA. A unique feature of financial services is the assurance of the participation of financial experts in dispute settlements panels involving financial matters.

2.2 Definition of the Financial Services in FSA

A financial service is defined in the FSA broadly as any service of a financial nature Offered by a financial service supplier[3]. Financial services are separated in two sub-sectors:

1) All insurance and insurance-related services; and
2) All banking services and other financial services (excluding insurance).

"Understanding on Commitments in Financial Services" is a voluntary “high” standard of commitments in the financial services sector. It encompasses broader liberalization commitments than those required under the general provisions of the GATS. One key element of the "Understanding" is a *standstill commitment*, i.e. a freeze on the introduction of additional restrictions for all financial services. The "Understanding" also embodies MFN and national treatment with respect to government procurement of financial services from suppliers established in the market. Countries signatory to the

[3] Source: GATS Agreement (FSA), WTO, 1997.

"Understanding" also guarantee foreign financial institutions the right to offer new financial services products as they are developed, the right to move and process data across the border, and the right to let personnel enter the country on a temporary basis. The instrument used by a GATS signatory to undertake commitments in services sectors, including financial services, is referred to as Schedule of Commitments. Each member who undertakes a commitment in a specific sector must inscribe that sector in its Schedule of Commitments. In those sectors where commitments are offered, a member is allowed to take reservations from market access and national treatment. For example, a country committing to include "financial services" in its offer may take a reservation to not allow foreign institutions to establish subsidiaries. The Schedule is therefore essentially a "negative list" of commitments; these barriers are presented in the country commitments as "exemptions"[4].

Commitments in specific sectors are taken in the form of four different modes of supply (Article I) – referred to as:

Mode 1- cross-border- the supply of the service is from the territory of one country into the territory of another country.

Mode 2- consumption abroad- the supply of the service is in the territory of a country to a consumer of another country.

Mode 3- commercial presence- the service supplier of a country establishes a commercial presence in the territory of another country through which it intends to provide a service.

Mode 4- presence of natural persons- the supplier of a country provides a service in the territory of another country through the presence of natural persons (e.g., self-employed), e.g., independent financial consultants or bank managers, of one Member in the territory of another Member.

[4] Source: GATS Agreement (FSA), WTO, 1997.

3. Overview of Financial Service Sector of Bangladesh

3.1 Structure of Bangladesh's Financial System

Except for the transformation of three nationalized commercial banks into public limited companies which are now known as state-owned commercial banks (SCBs), the structure of the financial system remains almost unchanged since June[5]. Bangladesh's financial sector consists of the Bangladeshi Bank (the central bank), four nationalized commercial banks (NCBs), 5 state-owned specialized banks (SBs), more than 30 private sector commercial banks (PCBs) and more than 9 foreign commercial banks (PCBs). The rest of the financial sector consists of more than 29 non-bank financial institutions, the capital market, the insurance companies, the cooperative banks and the micro-finance institutions. Activities in the financial sector which was dominated by the inefficient NCBs a few years back are being replaced by the relatively more efficient PCBs and PCBs. The share of the financial sector in GDP is about 1.70% (FY06), which has remained quite steady over time. The contribution to GDP mostly comes from the banking sector. Its share in GDP has declined from 1.35 per cent in FY1995 to 1.27 in FY 2006. The contribution of insurance to GDP, although has shown a rising trend, is less than 0.40 per cent. Overall employment in the financial sector is about 0.10 million with the private sector employment rising while the public sector employment falling. Currently, the sector contributes about 1.50 per cent in government revenue.

3.2 Banking Sector

Savings products: Deposit rate offered by NCBs exceeded those of PCBs and FCBs during the 1990-2002 period. However, since 2004 PCBs are paying higher deposit rates leading to faster growth in deposit mobilization. The deposit rate paid by FCBs has been consistently lower than those paid by the other two groups. Lending rate charged by PCBs has been the highest, followed by that of NCBs and FCBs till 2002. Since 2004 lending rate of FCBs exceeded that charged by NCBs though it remained lower than that of PCBs. The share of SCBs in total deposit fell during Q3 2007, while

[5] Financial Sector Review, Volume III, No. 1, February, 2008

the share of PCBs increased. Between December 2001 and September 2007, the share of rural deposits declined while the share of urban deposits increased from 80.4 percent to 86.9 percent. Total deposit mobilization by the banking system as percentage of GDP has been growing over time and stood at 43.1 percent at the end of September 2007.

Loan products: Disbursement of bank credit somewhat slowed down during the first three quarters of 2007 largely due to low demand by the borrowers. Nominal bank credit grew by 8.6 percent during the first three quarters of 2007. The disbursement of term lending to industrial sector in Q2 FY08 showed a 7.0 percent growth over previous quarter and was 26.5 percent higher compared with the level of Q2 FY07[6].

Interest rate spread: The IRS of commercial banks showed a declining trend till the end of 2004 after which a rising tendency is observed Available data, moreover, show that IRS in Bangladesh is higher than the spread in some of the neighboring countries (e.g. 5.25 in India in September 2007) indicating the need to reduce the spread in Bangladesh.

FCBs have been able to target a niche market of relatively large depositors. Since there exists economies of scale in operating large transactions resulting in lower average costs, FCBs are able to offer advances at somewhat lower interest rate relative to PCBs. This may, however, also be a reflection of two other factors. First, FCBs, set lending rate at lower level to remain competitive in business. Second, unlike NCBs and PCBs they are not heavily burdened with non-performing loans. Foreign investment in the banking sector has brought modern technology like computerization of banking operations, introduction of ATM services, Smart Card, Credit/Debit Card, and On Line Banking. These services have quickly been adopted by the PCBs. The banking sub-sector in Bangladesh has been greatly liberalized in the course of the past one and a half decades. FCBs and PCBs hardly operate in rural areas. Currently the high-risk loans such as agricultural loans are primarily supplied by the NCBs and the SBs. The contribution of the PCBs and the FCBs in this regard is very small. Further liberalization of the banking sector may yet shift away low-risk businesses from the NCBs to the FCBs and PCBs

[6] Financial Sector Review, February, 2008.

and it may greatly undermine the rationale for equity as opposed to efficiency.

3.3 Insurance Sector

The insurance sector is dominated by five big companies, which have control over 60 per cent of the premium income. The share of state-owned companies in both life and non-life insurance has been declining over the years. The state-owned life insurance company, JBC, had a share of 17.55 percent in 1997 and after 8 years in 2005 it came down to 12.14 percent. Similarly, the state-owned non-life insurance company, SBC, had a share of 23.18 percent in total assets of the insurance industry in 1997, but it came down to 8.24 percent in 2005.

The investment portfolio of insurance companies usually consists of listed shares, government securities and bonds, corporate debt, real estates, and money market instruments like fixed deposits. The share of investment of life insurance companies increased substantially over the years (from 53 percent of total investment in 1997 to 78 percent in 2005), whereas that of nonlife companies declined from 47 percent to 22 percent during the period.

The contribution of private sector insurance companies to investment has been increasing over the passage of time, whereas the share of state-owned companies (JBC and SBC) has been steadily declining. This happened due to the lack of innovative products offered by the state-owned companies, which did not permit them to gain business in the present-day competitive environment.

At present, there is no exclusive reinsurance company in Bangladesh that can provide specialized reinsurance services to the life and general insurance companies of the country. As a result, insurance companies face problems in dealing with reinsurance facilities. They have to depend on the state-owned and private (both domestic and foreign) companies for reinsurance.

The Bangladesh Insurance Association (BIA) is of the opinion that the state-owned

SBC, which lacks in efficient professionals, is not competent in dealing with the reinsurance matters of general insurance companies. BIA also says that life insurance companies, too, face problems in arranging their reinsurance due to refusal from the major insurers of the world and the *Jiban Bima Corporation*. Data provided in the Insurance Yearbook indicate that insurance companies of Bangladesh, including the public sector ones, cede reinsurance worth several billions of Taka every year abroad.
The regulatory agency of the insurance industry in this country, the Chief Controller of Insurance (CCI), is not equipped with adequate manpower and resources to supervise this growing industry, which limit the agency's role in the development of the sector. It is therefore essential that the CCI recruit competent professionals who will be able to analyze the financial soundness of the companies and prepare financial reports for taking appropriate measures.

3.4 Non-Banking Financial Institutions (NBFIs)

In September 2007, total investment of NBFIs stood at Tk.97.1 billion increasing from Tk.92.0 billion in June 2007. The major business of most NBFIs is leasing, though some are also diversifying into other lines of business like term lending, housing finance, merchant banking, equity financing, and venture capital financing[7].

The NBFIs have experienced rapid growth in number and assets and diversification in business activity. Lease financing, term lending, and housing finance constituted 94% of the total financing activities of all NBFIs up to 'June 2006. The share of leasing and house financing in the total portfolio of NBFIs has decreased gradually from-50 and 15 percent, respectively, in 2002, to 46 and 14 percent, respectively, in June 2006. The share of loan, on the other hand, has increased from 20 percent to 34 percent during the same period implying increased concentration on term lending. Outstanding lease/loan of NBFls at the end of June 2006 stood at Tk 7.3 billion, which reflects a 15.50 percent growth over December 2005.

[7] Financial Sector Review (FSR), prepared by the Policy Analysis Unit (PAU) of the Bangladesh Bank (February, 2008)

Annual average growth over the last four years (2002-2005) was 23.89 percent.

The current ratio of the industry during the first 6 months of 2006 was 2.66. The volatility, as measured by the coefficient of variation, dropped to 3.72 in 2006 from 6.23 in 2005. Therefore, the industry as a whole is capable of meeting the current debts with their current assets. However, the current ratios of individual firms varied from 0.47 to 16.58 percent indicating widely diverse performances.

4. Domestic Regulations related to Financial Services Sectors

In the case of banking services, foreign banks are allowed to open branches in Bangladesh after obtaining permission from Bangladesh Bank. However, the ratio of urban and rural banking branch in the case of domestic banks is 4:1 whereas, as per the Guidelines of the Bangladesh Bank, foreign banks are required to open a branch outside Dhaka and Chittagong only when the number of their branches reaches 5. The law itself does not, however, have any specific provision in this regard. Offshore banking in the EPZ and outside EPZ is governed by different rules and regulations. Banking service by credit card/ATM card is very popular now but the laws are not clear enough to deal with any problem arising out of Credit card/ATM services.

In the Insurance sector, there is no specific law under Modes 1 & 2. In Mode 3**,** in view of section 2C of the Insurance Act, 1938, insurance business may be conducted in Bangladesh only by a public company, or a society registered under any law for the time being in force in Bangladesh If a foreign insurance company wants to carry on insurance business in Bangladesh, then the Government of Bangladesh may impose reciprocal conditions for carrying on insurance business in Bangladesh. There is no specific law under Mode 4 in respect of insurance service.

PART-2: RESEARCH PART and RECOMMENDATIONS

1. Modalities for Special Treatment for LDCs in GATS Negotiations and Opportunities for Bangladesh

WTO Members in September 2003 adopted a Document entitled "Modalities for the Special and Differential Treatment for Least-Developed Countries (LDCs)", which strengthens the special treatment provided by the GATS for LDCs. The flexibilities provided by LDC Modalities constitute the main benefits that LDCs stand to gain from proactive participation in the negotiations. However, such participation requires careful analysis and decision making in view of the irreversible nature of WTO commitments. The flexibilities bring, among others, the following opportunities to Bangladesh:

Flexibilities offered by LDC Modalities	Opportunities for Bangladesh
WTO Members- shall, in view of the LDCs' special economic situation, exercise restraint in seeking commitments from these countries.	Bangladesh may limit the number of sectors for liberalization offers
LDCs shall not be expected to offer full national treatment, nor to undertake additional commitments under Article XVIII of the GATS on regulatory issues which may go beyond their institutional, regulatory, and administrative capacities.	Bangladesh is entitled to offer preferential treatment to domestic service providers in sectors where commitments are made.
There shall be flexibilities for LDCs for opening fewer sectors and liberalizing fewer types of transactions	Bangladesh may limit the types of transactions in the sectors in which liberalization is offered.

WTO Members shall give special priority to providing effective market access in sectors and modes of supply of export interest to LDCs.	Bangladesh can prepare schedules for sectors of export interest and request Members to open up those sectors
Members shall consider undertaking commitments to provide access in mode 4, taking into account all categories of natural persons identified by LDCs.	Bangladesh can propose special categories of natural persons identified in its requests
LDCs shall be granted appropriate credit for their autonomous trade liberalization.	Bangladesh may seek deeper concessions in major sectors of export interest against autonomous liberalization
WTO members shall provide technical assistance to LDCs in order to strengthen their domestic services capacity, build institutional and human capacity, and enable them to undertake appropriate regulatory reforms.	Bangladesh may Identify its specific technical assistance needs and claim them

2. Undertaking Liberalization Commitments of GATS in Financial Sector and Their Likely Impact

2.1 Banking Sector

Experience with past liberalization: Bangladesh's financial sector has already been opened up. Reforms undertaken in the recent years have produced good result. However, the banking system still suffers from relatively high interest spreads, lack of diversification and depth, high transaction cost, and financial fragility.

Contribution to GDP: The share of banking services in Bangladesh's GDP is very small (only 1.27 percent) but the sector plays a crucial role in maintaining macroeconomic stability. Since Bangladesh does not have enough resources for development, foreign banks should be encouraged to open branches and bring new capital investments. The existing liberalization policies should be locked-in. The local stakeholders are not afraid of facing competition from foreign entities, if there is level playing field vis-a-vis the foreign banks.

Trade Performance: In banking services, trade balance has turned positive in the most recent years. Diversification of products and improvements in efficiency standards will enhance the positive balance further.

FDI Potential: Further liberalization may enhance foreign participation and bring more foreign investment.

Employment Potential: There is not much opportunity for increasing employment in the banking sector because of intense competition among banks and the labor-saving technology that is being increasingly used in banking operations.

Regulatory Regime: There should be a sound regulatory regime with greater operational autonomy of the central bank.

Recommendation: The sector has already been liberalized unilaterally. Bangladesh may formally schedule its commitments to WTO with certain limitations regarding modes 3 and 4, and claim credit in the ongoing Doha Round negotiations.

2.2 Insurance Sector

Experience with past liberalization: There is one foreign insurance company since 1974. The sector has not been opened up further.

Contribution to GDP: The share of insurance services in GDP is very small and has remained stagnant at about 0.36 percent over the past few years.

Trade Performance: The sector has been perennially in trade deficit.

FDI Potential: Liberalization will bring in new foreign participation in the sector but stakeholders do not consider it necessary or desirable. The presence of a large number of insurance companies in a small market has created problems in the smooth functioning of the insurance industry. It is alleged that competition has not brought any benefit to the insurance industry. Merger of some of the companies could be a solution, which would get rid of unnecessary competition and also enable the advantages of economies of scale. The government, too, is reportedly in favor of merger of weak companies. Given the small size of Bangladesh's market and the degree of competition already prevailing, the opportunity for foreign presence in the industry is very much limited.

Regulatory Regime: There is the need for effective monitoring and surveillance of insurance companies.

Recommendation: There is no need to open up the sector to foreign competition at the present stage

3. Recommendations

- The growth of an efficient services sector is essential for the overall growth of the economy. An efficient financial services sector is crucial for raising the competitiveness of the countries. For this reason, appropriate government policies and measures need to be designed for a sustained growth of the services sector.
- Bangladesh needs to enhance the education and skill level of its workforce as it is important for the financial service firms to employ skilled workforce for delivery of their services to foreign clients or attract firms to employ skilled workforce foreign multinationals into the country.
- Computer literacy level along with the general education level needs to be enhanced to boost Mode1 export.
- In sectors in which regulatory bodies exist, e.g., Securities and Exchange Commission (SEC) etc. there is the need to strengthen the capabilities of

these institutions in order to transform them into effective regulators who are responsive to the modern needs of the financial services sector.

- Special emphasis needs to be given to introduce E-governance to improve transparency and reduce transaction costs. E-governance can also counter the menace of corruption that is all pervasive in the Bangladesh society.
- Regulatory institutions in collaboration with associations for different services sectors should make efforts for standardization, recognition and accreditation of service institutions, facilities and professional qualifications with international standards, qualifications and bodies.
- Improvements in law and order situation and political stability are vital in attracting foreign investment. Bangladesh should improve its country image abroad by having political stability, adopting sound macroeconomic policies, clamping down on extremism and militancy, and improving the law and order situation.
- Bangladesh's commitments to GATS are very limited but in practice most of the country's services sectors have been liberalized as part of its general economic reform programme.
- Bangladesh Bureau of Statistics (BBS) needs to improve statistical coverage of the financial services sector. Inclusion of more reliable data on financial service sector would increase awareness among foreign investors.
- Government should take initiatives to start short training programme on GATS for all stakeholders on a regular basis. The resource person can be drawn from the Ministry of Commerce, universities, and research organizations of the country as well as from the professional staff of the WTO, ITC and UNCTAD.
- *Attracting FDI:* Bangladesh badly needs FDI. More emphasis needs to be given to attract FDI to financial services. The country may benefit from "commercial presence" in these services by way of improvements in quality and supply. Commercial presence should be welcome in banking services as it will bring better technology and best practices, which will improve the efficiency in the sector.

- *Enhancing Trade in Mode 4:* Trade in Mode 4 will provide maximum opportunity to Bangladesh in the short and medium term. To derive maximum gains, there should be a policy in place to impart appropriate skills training in workers that have proven demand in the principal import markets. The developed counties will need to remove the many restrictions e.g., economic needs test, which hinder developing country services exports under Mode 4. For that purpose, LDCs as a group should actively participate in the GATS negotiations
- *Promoting Growth of Banking:* Since Bangladesh doesn't have enough resources for development, foreign banks should be encouraged to open branches and bring new capital investment.
- The high lending rates and high interest rate spreads symptomatic of an oligopolistic banking structure needs to be rationalized through prudent intervention of Bangladesh bank.
- There should be a sound regulatory regime with greater operational autonomy of the central bank.
- Further liberalization doesn't appear necessary for the insurance subsector. Stakeholders do not consider any foreign participation desirable either. The presence of large number of insurance companies in a small market has created problems in the smooth functioning of the insurance industry. Merger of some of the companies could be a solution, which would get rid od unnecessary competition and also enable the advantages of economies of scale.
- *Enhancing Capital Market Activities:* NBFIs around the world carry out a significant role in the development of the capital market. Strong institutional support is necessary for a vibrant capital market which is the core of economic development in any market based economic system. NBFIs through their merchant banking wing can act in this regard. Active participation of merchant banks is essential to accelerate the capital market activities which can expedite the economic growth of the country.
- There is the need for effective monitoring and surveillance on insurance companies. The regulatory agency of the insurance industry, the CCI, is not

equipped with adequate manpower and resources to supervise this growing industry. The efforts of CCI should also be equipped with proper logistical support, such as computer facilities, internet communication etc., which will enhance the efficiency of its day to day work.

- The finance and leasing companies across the world are using different sources for collecting funds. NBFIs in Bangladesh may also explore the possibilities of gaining access to new sources of funds like issuance of commercial paper and discounting or sale of lease receivables. However, in releasing such new products, some regulatory changes have to be made. Another innovative and promising source of funds may be the securitisation of assets.
- On undertaking liberalization commitments under GATS, the banking sector of Bangladesh has already been liberalized unilaterally. Bangladesh may formally schedule its commitments to WTO with certain limitations regarding mode 3 and 4, and claim credit in the ongoing Doha Round negotiations.
- There is no need to open up the insurance sector to foreign competition at the present stage on liberalization commitments under GATS.
- NBFIs in Bangladesh are operating in a highly competitive environment. The competition for NBFIs is even more challenging as they have to compete with banks. Given the changes in the business environment, the need for product diversification is very important. NBFIs should also venture into diversified use of their funds such as merchant banking, venture capital financing, factoring, etc. for a healthy growth of the capital market.
- *Financial policy and poverty reduction in Bangladesh*: The direct effects of financial sector policies on poverty can be mediated through different ways, such as cost and other conditions for access to credit, level and pattern of private investment, and means of financing fiscal deficits. Several financial policies in Bangladesh are likely to contribute positively to poverty reduction through their efforts of directing adequate credit to structurally disadvantaged sectors like agriculture, SMEs, and the rural nonfarm sector. The Bangladesh Bank has

encouraged the commercial banks, especially the private ones, to provide credit to agriculture and other pro-poor sectors.

- Other important elements that require supportive environment for financial deepening include a fully functioning bond market, both primary and secondary, where government and corporate debts could be traded freely; a viable mechanism for delivering agricultural (typically short-term), industrial, and infrastructure finance; and more active equity and insurance markets catering to improved and efficient allocation of risks in the economy.

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