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The World Bank

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IMPLEMENTATION COMPLETION AND RESULTS REPORT
(IDA-32850)

ON A

LOAN / CREDIT IN THE AMOUNT OF
US$ MILLION46.49

(SDR 34.50 MILLION CREDIT)

TO THE

PEOPLES REPUBLIC OF BANGLADESH

FOR A

FINANCIALINSTITUTIONS DEVELOPMENT PROJECT (FIDP)

August 07, 2006

Finance & Private Sector Development
World Bank Office: Dhaka
South Asia Region

CURRENCY EQUIVALENTS

(Exchange Rate Effective 06/30/2006)

Currency Unit = Taka

Taka 1.00 = US$ 0.01439

US$ 1.00 = Taka 69.49

Fiscal Year

July 1 - June 30

ABBREVIATIONS AND ACRONYMS

AAE	Accounts and Audit Expert
ABS	Asset Backed Security
ADB	Asian Development Bank
ALM	Asset Liability Management
BB	Bangladesh Bank
CAS	Country Assistance Strategy
CBSF	Credit, Bridge and Standby Facility
CBSP	Central Bank Strengthening Project
CDBL	Central Depository Bangladesh Limited
CLO	Collateralized Loan or Lease Obligations
CRAB	Credit Rating Agency of Bangladesh
CRISL	Credit Rating Information and Services Limited
DCA	Development Credit Agreement
DNS	Directorate of National Savings
DO	Development Objective
DOE	Department of Environment
DVP	Delivery vs. Payment
EGBM	Enterprise Growth and Bank Modernization
ERD	Economic Relations Division
FA	Facility Adviser
FAPAD	Foreign Aided Project Audit Directorate
FI	Financial Institutions
FID	Financial Institutions Department
FIDP	Financial Institutions Development Project
FMA	Facility Management Agreement
FSAC	Financial Sector Adjustment Credit
GDP	Gross Domestic Product
GOB	Government of Bangladesh
GSP	GSP Finance Co. (Bangladesh) Ltd.
ICB	Investment Corporation of Bangladesh
IDA	International Development Association
IDLC	Industrial Development Leasing Company of Bangladesh Limited
IMF	International Monetary Fund
IP	Implementation Progress
IPDC	Industrial Promotion and Development Company of Bangladesh Ltd.
IPFF	Investment Promotion and Development Project

IRD	Internal Resources Division
IRR	Internal Rate of Return
ISR	Implementation Status Results & Report
IT	Information Technology
M & E	Monitoring and Evaluation
MDG	Millennium Development Goals
MIS	Management Information System
MOF	Ministry of Finance
NBFI	Non-Bank Financial Institution
NBR	National Board of Revenue
NCB	Nationalized Commercial Banks
NPV	Net Present Value
NSS	National Saving Schemes
OD	Operational Directives
PAD	Project Appraisal Document
PCB	Private Commercial Bank
PDO	Project Development Objective
PFI	Participating Financial Institution
PFIL	Prime Finance & Investment Ltd.
PMRs	Project Monitoring Reports
PRSP	Poverty Reduction Strategy Paper
PSIC	Private Sector Industrial Credit
QAG	Quality Assurance Group
REPO	Repurchase Agreement
ROE	Return On Equity
SEC	Securities and Exchange Commission
SPV	Special Purpose Vehicle
TA	Technical Assistance
TB	Treasury Bond/ Bill
TDS	Tax Deducted at Source
TOR	Terms of Reference
UFIL	Uttara Finance & Investment Ltd.
ULC	United Leasing Company
WBG	World Bank Group

Vice President:	Praful C. Patel
Country Director:	Christine I. Wallich
Sector Manager:	Simon C. Bell
Project Team Leader:	Shamsuddin Ahmad

Bangladesh
Financial Institutions Development Project

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1. Basic Information

Country:	Bangladesh	Project Name:	Financial Institutions Development
Project ID:	P044811	L/C/TF Number(s):	IDA-32850
ICR Date:	10/31/2006	ICR Type:	Core ICR
Lending Instrument:	SIL	Borrower:	GOB
Original Total Commitment:	XDR 34.5M	Disbursed Amount:	XDR 34.5M

Environmental Category:C

Implementing Agencies

Bangladesh Bank

Cofinanciers and Other External Partners

2. Key Dates

Process	Date	Process	Original Date	Revised / Actual Date(s)
Concept Review:	03/24/1998	Effectiveness:	01/27/2000	01/27/2000
Appraisal:	11/15/1998	Restructuring(s):		
Approval:	09/16/1999	Mid-term Review:		11/20/2003
		Closing:	06/30/2005	02/28/2006

3. Ratings Summary

3.1 Performance Rating by ICR

Outcomes:	Satisfactory
Risk to Development Outcome:	Moderate
Bank Performance:	Satisfactory
Borrower Performance:	Moderately Satisfactory

3.2 Quality at Entry and Implementation Performance Indicators

Implementation Performance	Indicators	QAG Assessments (if any)	Rating:
Potential Problem Project at any time (Yes/No):	No	Quality at Entry (QEA):	Moderately Unsatisfactory
Problem Project at any time (Yes/No):	No	Quality of Supervision (QSA):	None
DO rating before Closing/Inactive status:	Satisfactory		

4. Sector and Theme Codes

	Original	Actual
Sector Code (as % of total Bank financing)		
Central government administration	1	
Law and justice	1	1
Banking	98	
Non-compulsory pensions, insurance and contractual savings		1
Payment systems, securities clearance and settlement		1
Capital markets		48
General finance sector		49
	Original Priority	**Actual Priority**
Theme Code (Primary/Secondary)		
Legal institutions for a market economy	Primary	Primary
Regulation and competition policy	Primary	Primary
Other financial and private sector development	Primary	Primary

5. Bank Staff

Positions	At ICR	At Approval
Vice President:	Praful C. Patel	Mieko Nishimizu
Country Director:	Christine I. Wallich	Frederick Thomas Temple
Sector Manager:	Simon C. Bell	Marilou Jane D. Uy
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6. Project Context, Development Objectives and Design

6.1 Context at Appraisal

Country Context, Government Strategy, and Main Sector Issues
High growth rates in Bangladesh and steady progress towards the Millennium Development Goal (MDG) targets have put forth the necessary conditions and timing for emphasis on financial development in the country. Accordingly, one of the four pillars outlined in the Country Assistance Strategy (CAS) 2001-05 continues to be enabling private sector-led growth through regulatory and structural reforms in the financial sector. The 2006-09 CAS and Poverty Reduction Strategy Paper (PRSP) 2003 emphasize the pillars of improved investment climate, including deepening of banking and financial sector reforms, and empowering the poor. The government's poverty reduction strategy, which relies heavily on promoting rapid, job-creating economic growth, points to improved financial intermediation in banks, non-bank financial institutions (NBFIs), and capital markets as a major development component.

The financial sector of Bangladesh is characterized by the strong presence of commercial banks. Nationalized Commercial Banks' (NCB) performance traditionally has been below par, and their portfolios have been riddled with bad debt issues. Private banking has shown more promise, but it remains small and can reach only a tiny portion of the private sector. As a result, financing to the private sector is small, and long-term funds, particularly important for growth and investment, are not available. The non-banking sector and capital markets are of limited size. The relatively young NBFI industry is showing promise and dynamism, with fresh and qualified human resources, improved balance sheets, and more efficient functioning. The main impediment to NBFI development is the lack of viable options to obtain loanable funds at long maturities and relatively low cost. In keeping with international practice, a major source of financing for NBFIs is the debt securities market; however, it has historically been underdeveloped in Bangladesh.

Debt market deficiencies in Bangladesh preclude NBFIs from raising major financing through fixed-income securities. In particular, regulatory bodies have imposed heavy costs of market access and regulatory compliance, including taxes and Securities and Exchange Commission (SEC) fees. Furthermore, low investor, institutional, and regulatory awareness and expertise on securities topics hamper development in this area. Finally, the debacle in 1996 during which debenture issuers massively defaulted is still fresh in the minds of the investing public, eroding confidence in debt instruments. The ever-increasing budget deficit has resulted in heavy borrowing from the general public as well as the banking sector through unsustainably high-yielding savings schemes and other sovereign instruments, which are also discouraging general investors from investing in other financial products. To strengthen the Bangladesh financial sector, a strong focus is needed to develop debt securities markets, as well as NBFIs and the sector's access to term financing, particularly through fixed-income securities.

Project Rationale

Banking sector issues have been addressed in the Financial Sector Adjustment Credit (FSAC), carried out by IDA (1990–95), which aimed to improve regulations and supervision of the banking sector, liberalize interest rates, and recapitalize NCBs. Furthermore, the Private Sector Industrial Credit (PSIC) project (1993–97) promoted private sector development by strengthening term lending by private financial institutions (FIs) and supported reforms under FSAC for interest rate liberalization and loan recoveries. The Central Bank Strengthening Project (CBSP) (1993–2007) is part of this ongoing effort and is focused on fostering a strong and effective regulatory and supervisory system for the banking sector. A concomitant project supporting this goal is the Enterprise Growth and Bank Modernization (EGBM) (2004–09) work on NCB privatization (Rupali, Agrani, and Janata Banks). The Asian Development Bank (ADB) carries out a fair amount of work on capital markets - market infrastructure and capacity, and more recently, governance arrangements, with limited if any focus on fixed-income securities. Given ongoing financial sector work by World Bank and other donors, the FIDP project was focused on the remaining gap in the donor agenda: strengthening NBFI term financing via debt security issuance.[1]

The FIDP was structured to assist the government in implementing its policy goals as declared in the GOB statement of Reform Policy for the Non-Bank Financial Sector.[2] In particular, the project addresses the following sector issues: (1) strengthening the high-performing part of the FIs by funding only those that meet stringent eligibility criteria; (2) providing assistance to eligible FIs to develop their own funding mechanisms for term financing; (3) ensuring that the government takes adequate steps to eliminate constraints to the development of markets for term financing; and (4) strengthening the institutional framework for term financing.

1 Given the commonality of regulations required for banks and non-banks, a strategic choice was made to leave the recommended improvements of the regulatory framework for NBFIs—provided for under project preparation—to CBSP. Similarly, streamlining court procedures for loan recoveries and establishing alternative dispute resolution mechanisms was considered under the Judicial and Legal Reform Project (JLRP) (2001–07). These choices allowed a sharper focus for FIDP, while addressing two important related activities as the core focus under CBSP and JLRP.

2 Specifically, the following constraints were identified in the Government of Bangladesh (GOB) Policy Note issued at the FIDP negotiations in 1999: (1) restrictions to institutional investors—life insurance companies and provident funds are not allowed to purchase private bonds; (2) issuance costs for corporate bonds are significantly higher than in other countries because of taxes and high service charges; (3) there are no benchmark interest rates from Treasury paper; (4) government saving rates—the National Saving Schemes (NSS)—are much higher than market, crowding out any other investment instruments; (5) there is a lack of a comprehensive set of guidelines by the SEC for issuing bonds and debentures; and (6) there is no secondary bond market. Although markets have improved in Bangladesh along each of those dimensions during the FIDP, further work remains in most areas.

6.2 Original Project Development Objectives (PDO) and Key Indicators (as approved)

Project Development Objective (PDO)

The FIDP objective was to promote the development of NBFIs, in particular, and investment financing, in general, on a sustainable basis that would contribute to improvements in the quality of intermediation and the speed and efficiency of industrial growth in Bangladesh.

The sector-related CAS goal for FIDP was to support the government's poverty reduction strategy of promoting rapid, job-creating economic growth by fostering the development of investment financing on a sustainable basis. Measures on the increase in investment financing served as key performance indicators. The critical assumptions made were that the political and investment climate in Bangladesh was improved or maintained and that the GOB would display an adequate commitment to implement financial sector reforms and avoid policies that distort financial markets.

The Project Appraisal Document (PAD) lists the key performance indicators as follows:

- Increased term financing by eligible NBFIs and other FIs (defined as cumulative disbursements of credit subcomponents to eligible FIs as a share of available funds, with the following target levels: 30 percent by the first year; 70 percent by the second year, and 100 percent by the third year).

- Increased share of market sources of funds for eligible NBFIs and other FIs (defined as the market funds raised by FIs via bonds, debentures, and Asset Backed Security [ABS], as a share of disbursed IDA funds, with the following target levels: 10 percent by the first year, 25 percent by the second year, 50 percent by the third year, and 100 percent by the fourth year).

6.3 Revised PDO and Key Indicators (as approved by original approving authority), and reasons/justification

Not Applicable.

6.4 Main Beneficiaries, original and revised

The project was expected to generate the following benefits:

- **Financial sector benefits.** It would support the expansion of a more sound and more efficient part of the financial sector while the rest is being restructured. It would support the availability of term financing on a sustainable basis through strengthened FIs, increased availability of funds for term lending, and the development of the bond and securities markets. Specifically, the main beneficiaries of the TA component include Participating Financial Institutions (PFIs), other FIs, investors (insurance companies, pension funds, banks, other investors, individuals), and regulators (Bangladesh Bank [BB], the SEC, Ministry of Finance [MOF], Directorate of

National Savings [DNS], and Foreign Aided Project Audit Directorate [FAPAD]).

- **Overall economic benefits.** It would promote increased efficient private investment in competitive projects that could generate economic growth and employment and provide the population with additional savings opportunities. Direct beneficiaries from the FIDP lending component include the companies borrowing from the program and increasing their investment, the new employees hired as a result (especially women), and customers who receive more (and arguably cheaper) goods.

6.5 Original Components (as approved)

The project comprises two components: (1) resource mobilization and (2) strengthening FIs.

Component I: Resource Mobilization

The resource mobilization component addresses the external factors that delay or constrain resource mobilization from the market. It aims to simplify and streamline regulations on bond issues, create an even playing field for individual investors between market-traded financial instruments and government-backed saving schemes, and develop benchmarks for issuing term paper by strengthening government bond markets. These initiatives are aimed at directly facilitating the development of NBFIs and improvement in the quality of intermediation on a sustainable basis. The resource mobilization component contains the following subcomponents:

- Development and implementation of issue rules for bonds and debentures.
- SEC training on fixed-income securities.
- BB training on fixed-income securities.
- Reform of NSS to bring the benefits of NSS closer to market-oriented instruments.
- Development of procedures for the secondary Treasury bond (T-bond) market.

Component II: Strengthening Financial Institutions

The component to strengthen FIs consists of a Credit, Bridge and Standby Facility (CBSF) to encourage the development of term financing through the NBFI sector.

- CBSF development: organizational structure, accounting and Management Information Systems (MIS), GOB / BB training, and the CBSF communications program.
- CBSF management: CBSF operation, advice to FIs, maintenance of documentation, monitoring FIS and their eligibility, reporting and audit functions.
- CBSF funding – provision of IDA support to FIs through a variety of mechanisms that increase their funding while enabling and encouraging them to mobilize medium- to long-term resources from the local market.
- Capacity enhancement of FIs' business planning, resource management, and FI MIS.
- PFI resource mobilization to develop capacity for issuing bonds, debentures and CLOs.
- Revision of the CBSF mechanism as needed.

6.6 Revised Components

Not Applicable.

6.7 Other Significant Changes

Fund Reallocation

The midterm review noted that PDOs were being achieved (participating FIs were raising debt finance as well as term credit) without making use of the Standby and Liquidity inducements provided under the project. Those mechanisms were not being demanded by the market, because the debt securities issued by the participating FIs were placed privately with investors, not issued publicly on the stock exchange. This was due, to a large extent, to the fact that the legal and cost framework precluded public issues of fixed-income securities, to which the abovementioned facilities were particularly tailored (this shortcoming is discussed in detail in section 7). The midterm review found it expedient to reallocate the Standby and Liquidity funds (US$17 million) to the Credit and Bridge facility toward a combined fund of US$45 million (IDA portion was US$40 million). As noted, the new funds were linked to matching debt issues, ensuring that future use of the Credit facility would be tied to continued promotion of market debt instruments.

Extension of Project

At the project's completion, the government requested an extension because of the popularity of the CBSF mechanism and, at that stage, IDA reallocated an additional US$2.6 million from unused TA subcomponents toward CBSF funding (toward an overall allocation of US$47.6 million/IDA portion US$42.6 million).

7. Key Factors Affecting Implementation and Outcomes

7.1 Project Preparation, Design and Quality at Entry

A detailed background analysis was carried out during project preparation to determine potential demand for funding by NBFIs and underlying corporate borrowers, and therefore gauge the viability of the CBSF project component. During project preparation, an assessment was made showing that a potential pipeline of sound projects exists. The project preparation further included a thorough investigation of the NBFI sector, inquiring into the availability of eligible NBFIs that would be interested in the project. Potential investors' interest was also analyzed, with the conclusion that, indeed, this interest was present and substantial, which also had been confirmed by the PSIC experience. Finally, the project aimed to ensure government commitment to reform by requesting (and receiving) the GOB statement of Reform Policy for the Non-Bank Financial Sector. These preparatory actions show a sound judgment and careful assessment of the project viability, and (with the benefit of ex-post vision) contributed significantly to project success.

Several lessons learned from prior experience were reflected in the project design:

- **Focusing on main activities.** Experience in Bangladesh has shown that focused operations have a much higher chance of success. Therefore, the project focused on a limited number of activities considered necessary and sufficient for achieving its objectives.
- **Addressing institutional capacity issues.** Because of the complexity and innovative nature of the CBSF and its transitional nature, which does not require GOB institutional strengthening, the project financed an independent manager with international experience to administer the CBSF that reported to the BB.
- **Ensuring sustainability.** The FIDP predecessor project, PSIC (see above), showed that beneficiary FIs in Bangladesh achieved limited increases in their own sources of funding, because there was no explicit mechanism to encourage or support FIs' development of funding sources. FIDP enhanced the possibility that participating FIs would raise funds from the market by (1) supporting the development of sources of funds for term lending through its 1:1 credit and other facilities, (2) increasing FIs fund-raising capabilities through TA and training, and (3) assisting in the development of regulations for bond markets, regulator training, and the elimination of cost barriers, crowding-out factors, and other impediments to bond market use.
- **Developing a realistic timetable.** Although efforts were made to shorten the implementation timetable through TA and the choice of government agencies committed to the project, a realistic timetable was developed based on past experience, taking into account the procedures required to implement government actions in Bangladesh (for example, selection of consultants and issuing of decrees).

The project objectives were clearly defined, bearing a solid link to the country strategy and needs, and addressing gaps in existing donor work. The three CBSF subcomponents formed the core of the project: the development, management, and funding of the facility. The need for each of the remaining subcomponents arose either as facilitation measures for the CBSF functioning or as a risk-mitigation strategy. For example, SEC, BB, GOB, FI, and investor training and capacity building were heavily emphasized because of the novelty of the project subject matter. The debt issue rules subcomponent provided a legal basis for smoother functioning of fixed-income securities issuance and securitization, on which the CBSF focused. The Treasury paper subcomponent promoted liquid government securities with a wider maturity structure and market-based rates, which facilitated fixed-income instruments pricing. The NSS reform attempted to eliminate the risk of NSS certificates crowding out the new debt instruments.

In contrast to the project structure and organizations, which were streamlined and simple, its subject matter was technical and complex. Indeed, concerns were raised at project design that the CBSF was ambitious, and with good reason. Suggestions were made to limit the project to simple debt issues, instead of taking a further step to securitize these issues. Hindsight suggests that the complexity created by securitization was not a hampering factor, and the Bangladesh financial system absorbed the innovation smoothly. Rather, the mechanisms designed to service the public issuance of debt remained unused, while adding a layer of complexity. This development, stemming directly from the lack of SEC commitment to planned reforms could have been in principle foreseen at project design (and indeed was identified as a risk) – a detailed discussion of the issue is presented in section 7.2 below. Partly out of such considerations, the Quality Assurance Group (QAG) rated the project moderately unsatisfactory at entry. A detailed discussion of the QAG assessment is presented in section 10 and annex 7.

The innovative nature of the project was addressed at project design by allocating an adequate budget for regulator training and capacity building. A further step in this regard could have been made, that is, to provide for a requirement that each regulating institution prepare a training needs assessment. Planning training needs would have permitted coordination among the agencies in the organization of training events, and could have further improved matching between training needs and events offered by the project. A separate communications program could have been outlined and budgeted for at the project design phase to provide ongoing investor education and awareness raising in view of the project's heavy innovative content. These omissions were caught and addressed at the midterm review. The project complexity and innovative nature necessitated (and achieved) the active development and involvement of the institutional investor base into debt securities market issues.

Although the BB was designated as the implementing agency, the SEC and MOF were to be closely involved in the project. The project designers were concerned about government commitment and project manageability, so they limited to the extent possible the number of government agencies involved. Because the BB and SEC both report to the MOF, they ensured that the group was coordinated. Indeed, BB exhibited strong commitment to the project, especially in the latter half of the project life cycle. The dedication sported by SEC was more uneven.

The strictness of the eligibility criteria for FI participation in the CBSF determined the ease of FI access to the securities financing program. More relaxed requirements would result in a larger number of beneficiaries under the project and a wider impact. However, that also carried the risk of lower-quality financial intermediation. The alternative approach of more exigent screening would create the impression of benefiting a "select few" and would fail to motivate medium-quality FIs to make the extra effort to improve their performance to the requisite level. The project's complexity was already a factor for FI access to CBSF. Given this trade-off, the fact that there were few mid-quality FIs, and the vital importance of avoiding a second investor confidence failure in debt financing, a relatively more stringent set of eligibility criteria was selected.

The project had environmental implications to the extent that the ultimate private sector investments financed through the CBSF and external debt funding mechanisms would have an environmental impact. To ensure proper environmental safeguards, all subprojects financed through the participating FIs were subject to approval from the Bangladesh Department of Environment (DOE). At project implementation, this presented a challenge because of the inefficient operation of the DOE and associated delays (this issue is discussed further in this section under "Implementation" and in section 8 under "Other Unintended Outcomes and Impacts").

Government commitment risk was foremost in the mind of the project architects, because of the fact that the project spanned a government election period, as well as because of the close structural relationship that exists within a financial system between government and private FIs and taxation issues. A particular concern voiced in the PAD was the risk that "NBR [National Board of Revenue] may not reduce stamp duties and taxes on bonds," which was mitigated by the GOB's formal announcement of its decision to eliminate or reduce the stamp duty on bonds during negotiations and in the Policy Notes that the GOB issued in preparation for the FIDP. In fact, the project experienced a slow removal of regulatory obstacles and generally weak responsiveness at some levels of government, including the NBR. Throughout the life of the project, in spite of gradual advances in suggested measures facilitating the development of fixed-income securities markets, an unstable tax framework prevailed. This contributed to poor predictability of market returns from different types of fixed-income securities, as well as excess and unnecessary costs borne by the participating FIs.

The PAD outlined several risk factors that stemmed from FI and underlying borrower (supply) risks, investor (demand) risk, market environment risks, and policy (regulatory) risks. Although the first three groups of market-related risks appear to have been successfully mitigated, the policy (regulatory) concerns materialized to a large extent and were dealt with continuously during the project. In addition to obtaining the GOB commitment before project effectiveness, further remedial actions were taken during implementation. The risks identified at appraisal were to the point and adequately addressed, which moved the project to more solid ground. This mid-term improvement was due, in part, to the correction of some design shortfalls, but mostly to the revamped government ownership, capacity, and commitment to the project.

7.2 Implementation

Implementation Arrangements

The BB acted as the implementing agency of FIDP on behalf of the GOB's Finance Division in the MOF, with support from the SEC and the DNS. A project steering committee—headed by the secretary of finance and representatives of the Economic Relations Division (ERD), Internal Resources Division (IRD), SEC, and Finance Division—managed the project and was responsible for policy decisions and major implementation aspects of the project.

Key Factors Affecting Implementation and Outcome

Training, capacity building, awareness raising, and reporting/monitoring systems development

GOB, SEC, and BB training. Training needs were met through a combination of theoretical training and practical on-site study tours to build capacity and meet FIDP objectives. The BB staff secondees to the CBSF developed the BB's capacity on debt instruments, securitization, and CBSF management. A number of training opportunities and study tours were organized under the FIDP. Training opportunities for government officials financed under the project included training tours to several countries to visit the securities and financial sector regulators, institutions, and private market participants, and to exchange experiences and best practice on debt instruments and asset securitization. Knowledge acquired from the training program has significantly contributed to furthering the regulators' understanding of the issues and increased awareness for the need of reform as well as for the achievement of project goals. Market participants noted the capacity enhancement of BB staff as a result of the training provided under the project.

PFI training and capacity building. With the assistance of the CBSF, various seminars, training programs, periodic workshops, and teleconference events were arranged to assist the PFIs in enhancing their capacity to develop strategic and business plans. PFIs have received TA to strengthen their governance, reporting, monitoring, credit evaluation, ALM and management practices, to name a few. Capacity was also built in environmental and audit matters. CBSF has provided regular advice to PFIs on debt issuance planning, execution, and documentation.

The project additionally heightened awareness of the importance of the debt securities markets and related matters among key government agencies, including the SEC, MOF, and IRD/NBR, as well as improved institutional investor awareness of and participation in the NBFI sector through regular communications with the PFIs, prospective investors, merchant banks and underwriters, credit rating agencies, insurance companies, journalists, and other stakeholders.

CBSF reporting and monitoring systems development. CBSF developed an MIS and systems for accounting, reporting, and monitoring. In addition, FIDP provided TA on MIS and information technology (IT) systems development for PFIs. Several strategies were debated here, ranging from a stand-alone PC solution for the CBSF, to an integrated harmonized system linking CBSF to all PFIs. The harmonized MIS would maximize benefits of scale achieved through CBSF connectivity and would facilitate monitoring; however, differences in IT-readiness of PFIs caused deliberations and a delay in MIS implementation. Additional delays were experienced as PFIs researched opportunities to finance the required TA and software/hardware, which resulted in a disagreement with the BB over the nature of financing allowed (grants versus loans), a detail that the FIDP documents failed to specify clearly at project inception. The CBSF management successfully argued against an integrated solution at the initial stages, instead implementing a functional standalone system and preparing an MIS report assessing possible strategies for extensions.

Development and implementation of requisite market infrastructure for fixed-income securities

Three major areas were identified that required reform to make the market placement of fixed-income securities possible: SEC rules of issue, lower NSS rates, and a liquid TB market. FIDP undertook actions in all three areas, as planned.

Developing and adopting SEC rules of issue. Draft SEC rules of issue were prepared by expert consultants and submitted to the SEC, some legal modifications were implemented in the capital markets rules, and training on corporate debt issuance was provided to GOB, BB, and SEC officials. Primary dealers formed a committee and conducted meetings concerning trade and reduction of transaction charges; stock exchanges, the central depository company, brokers, and dealers agreed to lower their respective fees for trading bonds. The extensive public-private brainstorming, discussions, and debate around the fixed-income securities issue have generated considerably more awareness in the country of securitization and bonds, and have so far resulted in a follow-up securitization deal which occurred independently of FIDP.

In spite of continual efforts on the part of most stakeholders and some government entities, public issues of fixed-income securities were not achieved under the project. The GOB's commitment to lower costs and to introduce legal changes, as professed in the GOB statement of Reform Policy for the Non-Bank Financial Sector, wavered during the project. The PAD notes the risk that "MOF and SEC may not coordinate adequately on Developing the Bond Market," and the respective mitigation measure adopted, "[p]articipation of both institutions under the project will ensure full coordination." In spite of these precautions and the extensive cooperation of the SEC, the latter failed to adopt adequate Bond Issue Rules during the life of the project. Instead, SEC has provided guidelines for the interim on issuance (SEC Issue of Capital Rules 2001 on private debt and equity placements) and issued the Asset Backed Security Issue Rules 2004. Those actions left the Bangladesh capital markets without consolidated and updated rules for the issue of fixed-income securities.

Analysis in retrospect in cooperation with market participants, SEC, and the BB provides the following insights into the possible reasons for this shortcoming. The specifications drawn out in the draft debt issue rules, as cleared by the SEC and BB, might have involved too large a package of diverse issues. As a result, the final draft created objections on the part of the BB in the area of government securities issue rules, and on the part of the SEC in the area of fixed-income securities rules. Tensions between the BB and SEC on the content of the rules, and differing concerns on perceived shortcomings of the rules, ultimately eroded support for the reform. These differences are being resolved and the expectation is to have the issue rules reform moved forward. The SEC identified an additional reason for its reluctance to adopt the issue rules, namely, their perception of the low need to reform the rules because of the lack of market interest in issuing simple bonds and debentures at the prevailing high costs of issue.

<u>Lowering NSS rates.</u> High-yielding government subsidized NSS instruments crowded out potential issues of fixed-income securities. The alignment of interest rates of NSS with market-oriented instruments was gradually addressed via the elimination of longer-maturity NSS instruments, imposing a 10 percent withholding tax on NSS instruments from June 1999, and lowering NSS rates on three-year and five-year Sanchay Patras since 2003.[3]

Finally, FIs were made ineligible to hold NSS instruments, consistent with their social objective of fostering savings among the very poor. NSS performance and economic role were further analyzed under FIDP; the results of which are currently being reviewed by the

3 The decrease in interest was from 12.5 percent and 12 percent on 3 and 5-year Patras to a low point of 10.5 percent and 10 percent, respectively; rates were raised again in March 2005 to 12 percent and 11.5 percent, respectively. The 10 percent withholding tax rate was further reduced to 5 percent in July 2002.

GOB. Structuring follow-up IDA work in this area would greatly benefit from applying the recommendations from this study.

A considerable challenge faced throughout FIDP implementation was the delay in hiring consultants. Two particular cases stand out: (1) retaining consultants on fixed-income issue rules discussed above and (2) hiring consultants for reform of NSS. The former procurement suffered from a scarce supply of highly qualified bidders, which necessitated the repeated issue of several expressions of interest. The issuance of the expressions of interest was delayed mainly due to the lengthy process of finalizing the terms of reference (TOR), which involved approvals at several government levels. Such delays derail the momentum for implementation and impede the full achievement of project goals. Specifically, the time available to reach government consensus over the issue rules was curtailed, thus lowering the chances of successful reform in this area. Regarding the NSS, consultant procurement delays left little time for further implementation of NSS structural and operational reform. Difficulties with consultant retention might have been avoided at project design by pre-identification of prospective consultant interest.

<u>Developing a liquid TB market.</u> For the purposes of the project, the most pressing needs included the creation of procedures for a secondary TB market, as well as regular primary auctions of 5- and 10-year TBs. Periodic auctions of T-bills have been held since October 2000. The BB operationalized the repo (repurchase agreement) system for the 28-day T-bills in 2002, and the first repo transaction in Bangladesh was undertaken in January 2003. The Central Depository of Bangladesh Ltd. (CDBL) opened the electronic registry for Treasury paper in October 2003, and banks began secondary trading of scripless paper. The BB issued 5- and 10-year T-bonds for the first time in December 2003. Currently, auctions of T-bonds are held bimonthly, but they do not involve many participants or large amounts. T-bills are auctioned weekly. A provision was made to start trading T-bonds on the stock exchanges in 2005. A considerable role in these positive developments was played by the BB Governor, in part under FIDP influence and lobbying.

Development, management, and funding of CBSF

<u>CBSF development.</u> The CBSF was established by the BB through FID Circular No. 07, dated July 19, 1999. The GOB approved all CBSF founding documents. The BB issued Operational Directives (ODs) for the CBSF. A Facility Adviser (FA) was competitively selected to manage the CBSF. Because of the complexity and innovative nature of the CBSF and its transitional nature, the project elected an independent manager with international experience to administer the CBSF. An FMA was signed by the winner of the competitive bid for CBSF management and the BB on December 28, 1999, for five years. The guidelines for the Bridge and Standby facility were issued by the BB in 2001, followed by the guidelines for the Liquidity facility in 2002. There were delays in instituting CBSF management staff in place, as well as turnover in senior management, in part due to the inexperience of the internally-hired consultant firm with local Bangladesh conditions, and a gestation period of adjustment of BB mode of doing business with that of the FA company. These hurdles could have been avoided by hiring a locally-savvy FA; however, the selection

was based, with good reason, on finding the highest professional quality FA given project complexity.

Pricing CBSF funds presented a challenge to the success of the project, because of changing financial market conditions, on the one hand, and the lack of a reliable market Treasury paper rate, on the other. As a second-best and only feasible solution, the pricing of CBSF funds was set at a variable markup over a moving average of all Treasury paper in existence. These considerations illustrate the difficulties of pricing CBSF debt at true market value in underdeveloped financial market conditions.

<u>CBSF management.</u> The FA moved quickly to assess the eligibility of interested FIs, clear their project participation with the BB, and sign Master Facility Agreements. CBSF offices were set up and local staff were hired by the first half of 2001, and CBSF internal control, accounting, management, and IT systems were set up with the assistance of an Accounts and Audit Expert (AAE) in cooperation with the BB. Ongoing management issues were carried out on a rolling basis, including staffing, reporting, monitoring, conducting internal reviews, assessing the suitability of FIs, conducting regular reviews of the PFIs and the subloans and leases, monitoring PFI debt issuance in connection with the matching credit facility, investing CBSF liquid assets, administering requests for access to facilities, and providing continual reports to the BB on CBSF and FIDP development.

A challenge that arose during the CBSF management was presented by the state audit body, FAPAD, which was also slated to perform the external audit for CBSF. In particular, the auditor lacked sufficient specialization in financial matters to understand the complex functioning of the CBSF, causing delays in requiring multiple clarifications and issuing a number of objections (mostly of a trivial nature) to the audit statements. To clarify the issues and observations, as well as to reduce future FAPAD observations, tripartite "exit" meetings were held with IDA, the project team, and FAPAD before audit reports were finalized. These meetings reduced trivial audit issues and improved qualitative observations that reflected technical specifics of the project.

<u>CBSF funding.</u> FIDP effectively injected into the Bangladesh economy scarce long-term funds for investment and private sector growth (see section 8.2 for details), while experiencing no delays or defaults in payment by PFIs. These results relied heavily on a number of other outcomes that have been achieved under the FIDP, including the following: (1) progress in alignment of NSS rates with the market, (2) stimulation of liquidity and trading of TBs (the first reverse repo transaction occurred under the project), (3) advances in the regulatory framework for bond issuance, and (4) intensive regulator and other stakeholder training.

The midterm review was instrumental in quickly addressing the challenges encountered during the CBSF funding operations and, specifically, the lack of market interest in the Standby and Liquidity Facilities (discussed in section 6.5, "Other Significant Changes"). Funds were promptly reallocated to their best alternative use and the refocused project was enabled to continue functioning smoothly.

7.3 Monitoring and Evaluation (M&E) Design, Implementation and Utilization

The project has set forth benchmarks and performance indicators to evaluate progress on individual subcomponents (see annex 1 of the PAD). These indicators were agreed upon during negotiations and were reviewed periodically to determine their effectiveness against performance standards and implementation schedules (see Implementation Status Results and Reports [ISRs] 1–12). IDA undertook a midterm review during project implementation.

The focus of the project, to promote the development of investment financing on a sustainable basis and improve the quality of intermediation, translates well into the two performance indicators used to monitor progress of the PDO: (1) "increased term financing by eligible NBFIs [and] other FIs," and (2) "increased share of market sources of funds for eligible NBFIs and other FIs." The data for measuring these indicators were sourced directly from the projects, as well as the financial sector statistics prepared by the BB, and were reliable, high quality, up to date, and amply available. Perhaps advancing one step further, the indicators devised for the TA subcomponents of the project, as reflected in the PAD, could have been quantified at the design stage as well (which, indeed, was done at the ISR stage). The Measurement and Evaluation (M&E) framework, which indeed might not withstand the high standards currently imposed on new projects, in view of the considerable recent emphasis on the M & E agenda, can be found generally adequately designed when compared with projects of this older generation, and the performance indicators were sufficiently specific, measurable, attributable, realistic, and targeted.

The FIDP has several levels of M&E arrangements built in by design. First, because of the financial nature of the operation, internal controls were implemented at the BB-CBSF-PFI level to ensure timely detection of problems, if any. Specifically, PFIs (1) verified the status of subprojects supported under the CBSF by on-site inspection; (2) prepared periodic subloan portfolio management and progress reports covering operations under the credit; and (3) undertook quarterly and annual assessments of the demand for funds from the CBSF. In turn, the CBSF and BB monitored PFIs and presented regular reports to IDA, including (1) CBSF monthly reports with key data on utilization and status of its facilities and financial statements; (2) CBSF quarterly reports on facilities' implementation; (3) CBSF semi-annual assessments of the FIs' demands for CBSF facilities; and (4) CBSF annual cash flow and balance sheet projection. The BB reported to IDA on a quarterly basis on the progress of each of the TA subcomponents. Additionally, the CBSF had an internal MIS and accounting, reporting, and monitoring systems.

As noted in the discussion of M&E design and implementation, the data used to monitor the project and inform decision making and resource allocation were reliable. The two PDO-linked numeric performance indicators, as well as the qualitative indicators used to measure progress along the TA subcomponents of the project, were of considerable value to ensuring that the project was maintained on track and ultimately were successful. Performance indicators were collected largely in a timely fashion, and the indicators helped determine the fund reallocation at the midterm review (see section 6.5, "Other Significant Changes").

As designed, the CBSF M&E arrangements would have been sustainable beyond the FIDP implementation period and could have been utilized by the BB to continue to monitor and evaluate the CBSF operations, had the CBSF been kept in operation by the BB, as originally planned. Instead, focus currently is being shifted to infrastructure finance (the Investment Promotion and Financing Facility [IPFF]), which is a natural extension and successor operation of the FIDP (see discussion in section 7.5, under "Postcompletion Operations: The Next Phase").

7.4 Safeguard and Fiduciary Compliance

Financial Management, Procurement, and Disbursement

Procurement
The BB ED, who was the FIDP director, was responsible for procuring goods, consultant services, and training for Component I (resource mobilization). He was also responsible for contracting the facility manager and training the GOB/BB personnel under Component II (strengthening FIs). Per the FIDP ISRs, there appear to be no obvious and systematic procurement or financial management issues.

Financial management and reporting arrangements
The BB maintained a computerized financial management, accounting, disbursement, and reporting system for the project in accordance with generally accepted accounting principles and practices. The accounts and records were verified and audited by the FAPAD, the supreme audit body in Bangladesh. To facilitate financial management and reporting arrangements, the project engaged a full-time AAE external to the BB, who reported to the project director and supervised accounting and reporting issues. The AAE prepared quarterly and annual accounts and generated quarterly reports to ensure consistency with IDA's requirements under Operational Policy/Bank Procedure (OP/BP) 10.02. Internal controls included a separate Project Audit Committee, proper segregation of functional responsibilities, signing of checks after clearance by the AAE, verification of procurement proposals, monthly reconciliation of bank accounts, and regular detailed reporting. Participating FIs submitted annual audit reports to BB/CBSF management and IDA.

Disbursements
A special account was opened with the BB. Disbursements were made by the BB to the beneficiary agencies on a reimbursement basis directly from the special account. The Project Monitoring Reports (PMRs) have been prepared accurately and submitted to the Bank in a timely manner. The project, however, did not computerize its accounts for two reasons. First, the stand-alone PC-based solution used during the life of the project was judged to be adequate until the CBSF was closer to becoming an independent entity (a plan that was later revised). Second, the expediency of harmonizing the computer systems of all PFIs was reconsidered (see the PFI Capacity Enhancement subcomponent).

FIDP was a FIL operation (Financial Intermediary Loan), and as such is subject to OP8.30. Specifically, relevant issues under the rule include the eligibility criteria for participating FIs, onlending terms, as well as the procedures in support of market-based interest rates. While the mid-term review does not discuss compliance with OP 8.30, it can be noted that the rule has been closely observed, and has contributed to the success of the project. For example, take the requirements for onlending terms, namely, that funds be priced competitively and based on market prices, and in the absence of a market, that rates be non-negative in real terms, provide adequate margin to FIs, and not discourage resource mobilization from the market. Referring to the discussion of procedures used by CBSF to price onlent funds, rates were set administratively in the absence of a market, but linked to Treasury paper rates, and assuring both an adequate margin for PFIs (resulting profit figures quoted in section 8.2) as well as encouraging PFIs to raise their own funds (resulting funds raised outside of CBSF during the project also discussed in section 8.2).

Environmental Assessment
Industrial development has an impact on the environment. Accordingly, the project was classified in environmental category B, because some of the subprojects selected for financing through the CBSF mechanisms were likely to fall under the red or orange categories as classified by the Bangladesh DOE. Based on OD 4.01, no separate Environmental Analysis or Environmental Management Plan was undertaken because any potentially polluting subloans required a separate clearance from the DOE.

To address environmental concerns, three types of actions were taken:

- As criteria of eligibility for participation under the CBSF, FIs had to prove that their subproject approval procedures include verification of DOE clearance.
- Processing the subprojects under the credit facility depended on whether they fell under the red, orange, or green industrial categories, as established by the DOE. Applications for subproject disbursement required DOE clearance for those subprojects that fell under the orange and red categories.
- To ensure that appropriate training is available for FI staff to fulfill the role of environmental compliance officer, the project includes an environmental compliance course in its FI capacity building subcomponent.

In practice, DOE clearances proved problematic to obtain because of DOE inefficiency of operation and associated considerable delays in obtaining clearances (see section 7 under "Project Preparation, Design, and Quality at Entry" and section 8 under "Other Unintended Outcomes and Impacts").

7.5 Post-completion Operation/Next Phase

Transition Arrangements
During the initial stages of the FIDP, the CBSF was contemplated as a sustainable entity, which could continue its existence beyond the project end and potentially be privatized. The proposal to privatize the CBSF was not supported by the GOB at the midterm review or at earlier implementation stages. Subsequently, the MOF and the steering committee of the project agreed to keep the CBSF within the FID of the BB. Necessary arrangements were made for transferring facility management skills to qualified local professionals and local

consultants as well as to the BB's secondees. The CBSF was transferred to the FID on February 14, 2005. The final decision was to stop new lending and eliminate the CBSF altogether, following the retirement of all outstanding loans and full collection of proceeds. In the interim, and while FIDP operations are ongoing on a retirement basis, continued project monitoring might be linked to FSAP and / or financial sector indicators as prepared by the FPD anchor, such as volume of new fixed income securities issuance relative to GDP / stock market size. Considerations for this decision included the inability of the CBSF to operate the liquidity facility, because of its status as a government entity, and existing investment restrictions in the banking sector by government entities. Additional considerations might have played a role, such as GOB budget constraints and the fact that the coming year is an election year. The funds were transferred into the GOB Treasury, while new funds in roughly the same amount have been committed by the GOB as co-financing of IPFF.

Next Phase: Follow-up Operations
Several new avenues for potential IDA involvement have opened up as a result of the FIDP, including some of the following: (1) further strengthening of the fixed-income securities market, (2) stronger enforcement powers for the SEC, (3) delays of SEC public issue clearances, (4) accumulation of credit rating experience and capacity, (5) further development of CDBL and dematerialization of securities, (6) computerization of NSS and overhauling of the DNS, and (7) development of an interbank money market. These issues are discussed in more detail below.

<u>Strengthening of the fixed-income securities market</u> to continue the work of FIDP, especially in areas where the project fell short of fully achieving its objectives or the underlying potential. One such area remains the issue of adequate fixed income securities public issue rules. SEC's ongoing reform work on fixed-income securities issue rules, in cooperation with the Reserve Bank of India and ULC, demonstrates continued reform for further improvement of the framework and should be supported. Furthermore, if the public debt market is to take off, there is a need to encourage a greater variety of institutional investors with a long-term investment horizon like mutual funds, pension funds, and so. Issuance and transacting debt instruments in a dematerialized form would help reduce costs further.

Mortgage-backed bonds could be considered as a market for development and promotion assistance on the part of the World Bank. Mortgage-backed bonds pool housing loans and match the investment needs of institutional investors within permitted regulatory guidelines. There would be a significant need for coordination with government in overcoming regulatory and market hurdles. The mortgage-backed market development hinges on the adequate resolution and sound functioning of the legal, regulatory, institutional, and structural aspects of primary markets. The development of this market is a high priority given the lack of housing finance (and significant and growing demand for it), as well as the expected further increase in the importance of financial institutions who require high returns on long-term funds, such as pensions, investment funds, and insurance companies.

In the area of mortgage-backed finance, there is considerable potential for cooperation with the International Finance Corporation (IFC). A July 2006 study commissioned by the IFC provides further details on priorities in the development of the mortgage-backed debt market. The study suggests, in particular, that "a housing finance project could serve as a stand-alone project for the WBG, representing a combination of policy and institutional reforms led by IDA/IBRD along with direct interventions and targeted TA from the IFC."

SEC enforcement.To assure market confidence and provide a strong framework for debt issuance capable of supporting the various initiatives suggested above, such as mortgage-backed securities, the SEC would require training, adequate staffing, and strong monitoring and enforcement powers on the book and in practice. As part of the needed SEC overhaul, some lengthy procedures could also be trimmed and streamlines. For example, the time taken by SEC to vet prospectuses for public issues could be aligned to market reality and needs.

Improved financial market information is needed in the Bangladesh environment. Two credit rating agencies—Credit Rating Information and Services Ltd. (CRISL) and Credit Rating Agency of Bangladesh (CRAB)—have opened in Bangladesh, and are in the process of developing adequate capacity. A promising avenue for public-private partnership for reform might focus on establishing an information clearing house, to remedy the existing constraints of access to and availability of needed market information.

NSS analysis. Further follow-up should be implemented using the NSS analysis carried out under FIDP and its recommendations, including the computerization of NSS which was not addressed under FIDP. NSS follow-up would permit an assessment of the impact on the GOB budget, and structural and operational reforms of the DNS in view of effective market-oriented savings schemes. Structuring the follow-up IDA work in this area would greatly benefit further development of the financial sector, by helping create an efficient, customer-oriented, viable, and modern DNS, which would reduce the cost of borrowing for the government and give an impetus to the development of the capital market.

Electronic registry. Following recent advances in CDBL in the TB area, further facilitation and development of the securities market is in order. Clearing outstanding legal ambiguities, depository participants licensing issues, reporting arrangements, and decision-making prerogatives among the BB, MOF, SEC, and CDBL would vitalize these markets. Over time, the CDBL has the potential to cover all transactions related to primary issues of T-bills, government bonds, secondary trading of TBs, interbank repos, and repos between the BB and commercial banks, as well as operate an equity share registry and a registry for corporate fixed-income securities. In addition to their direct effect on debt markets, these developments would aid the formation of a yield curve in the TB market and the pricing of bond issues, along the lines of the FIDP subcomponent on the Treasury Paper Market.

8. Assessment of Outcomes

8.1 Relevance of Objectives, Design and Implementation

The FIDP remains highly relevant to the development of Bangladesh, as measured against the current objectives of the 2005 CAS/PRSP update. The current high growth rates of the country (5 to 6 percent) put a strain on the capacity of the financial system to fund the private sector investment needed to sustain this pace of growth. Failure to develop the long-term lending capacity of the financial system threatens the maintenance and further increases of the country's growth rates. The stable macroeconomic environment, high economic growth, and declines in population growth, accompanied by significant improvements in education and poverty reduction, render the country situation ripe for an active push toward financial development.

The 1998 CAS pillar of building a supportive environment for private sector growth, especially in the financial sector, has been re-echoed in the latest 2005 CAS/PRSP update, which emphasizes an improved investment climate, including a deepening of banking and financial sector reforms. The Bank was responsive to the changing needs of the country and the operation remained important to achieving country and Bank objectives. Follow-up work undertaken under the FIDP also remains important (see section 7, under "Next Phase: Follow-up Operations").

The project design and implementation aptly address the financial sector gaps in development, in particular issues related to the NBFIs. To summarize (see section 6), a preponderant commercial banking sector in Bangladesh remains inefficient and in need of restructuring (Bank work is ongoing in this regard), and a dynamic non-banking sector is starved of long-term funding, which is particularly important for growth and investment. Accordingly, the FIDP was designed to (1) help directly increase the long-term financing of NBFIs; (2) focus on developing the capacity of NBFIs to raise term finance in the most promising mechanism in existence, namely the debt securities market; and (3) ease regulatory and market obstacles to such financing going forward. In terms of project implementation, the country needs didn't change during the project; however, the extent of feasible implementation was decreased (that is, public issuance of fixed-income securities proved unattainable during the project) and the project responded to these changing circumstances by a budget reallocation during the midterm review (see section 6.5, "Other Significant Changes").

8.2 Achievement of Project Development Objectives

The sector-related CAS goal for FIDP was to support the government's poverty reduction strategy of promoting rapid, job-creating economic growth by fostering the development of investment financing on a sustainable basis. The FIDP objective was to promote the development of NBFIs, in particular, and investment financing, in general, on a sustainable basis that would contribute to improvements in the quality of intermediation and the speed and efficiency of industrial growth in Bangladesh.[4] The project activities can be broadly

4 The DCA presents the PDO as "to promote the development of financial institutions and improvements in investment financing on a sustainable basis through strengthening the quality of intermediation with the aim of increasing industrial growth in Bangladesh", in a slight inconsistency with the PAD. This more general version of the PDO is somewhat unsuitable as it is difficult to measure and does not come with any baseline indicators.

captured as contributing to this end, though it might be difficult to formally establish the causal link between FIDP activities and the PDO. The following measures on the increase in investment financing served as key performance indicators:

- Increased term financing by eligible NBFIs and other FIs (defined as cumulative disbursements of credit subcomponent to eligible FIs as a share of available funds, with the following target levels: 30 percent by the first year, 70 percent by the second year, and 100 percent by the third year)
- Increased share of market sources of funds for eligible NBFIs and other FIs (defined as the market funds raised by FIs via bonds, debentures, and ABS, as a share of disbursed IDA funds, with the following target levels: 10 percent by the first year, 25 percent by the second year, 50 percent by the third year, and 100 percent by the fourth year)

One could consider that the utilization of the facility is a weak performance indicator for the attainment of the PDO, as it might be considered more of an input indicator. Given the generality of the PDO, adequate measurement call for the achievement to be inferred from associated outcome indicators, and the ICR does do this through looking at the amount of "matching funding" obtained by the NBFIs from the marketplace, the second measure listed above. This appears a robust and measurable indicator and it does reflect a healthy use of market instruments. The key indicators' performance over the life of the project is presented in table 1.

Impact of the Project

FIDP established the CBSF and disbursed term funding of US$45.6 million (Tk 2.6 billion). Under the project, the participating FIs raised term finance by issuing US$38.4 million (Tk 2.4 billion) in fixed-income securities to outside investors such as banks and insurance companies. Effectively, FIDP injected into the Bangladesh economy scarce long-term funds for investment and private sector growth. The first securitized asset sale in Bangladesh took place under the project in November 2004. The project mitigated or completely overcame some of the existing impediments to securitized transactions, including lack of legal and institutional infrastructure, high issuance costs, high regulatory compliance costs, and lack of sufficient local skills, and came a long way toward creating an enabling environment for securitization in Bangladesh.

Table 1. Performance of Key Indicators

PSR date	PDO1	Target1	PDO2	Target2
10-Apr-00	0%	0	0%	0
22-Sep-00	0%	0	0%	0
27-Feb-01	33%	30%	0%	0
05-Sep-01	41%	30%	0%	0
04-Mar-02	41%	70%	4%	10%
08-Sep-02	59%	70%	40%	10%
06-Mar-03	80%	100%	56%	25%
06-Sep-03	81%	100%	55%	25%
31-Mar-04	59%	100%	68%	50%
30-Sep-04	68%	100%	60%	50%
16-May-05	99%	100%	90%	100%
11-Nov-05	99%	100%	92%	100%
30-Jun-06	100%	100%	94%	100%

Source: BB data.
Note: PSR = Project Status Report; PDO = Project Development Objective.

The newly raised funding was used by six PFIs to finance the setting up or expansion of 147 subprojects in various sectors, such as ready-made garments, food, textiles, transportation, ceramic, power, education, medical, accessories, and so on. Till end of the project, these subprojects had generated direct additional employment of 14,218 employees, a major portion of which included women, and additional profits of Tk 3,842 million for the borrowing subprojects.

A total of Tk 957 million (US$16.2 million) in simple credit was disbursed throughout the life of the project to all six PFIs, which was used for 53 leases and eight loans. In contrast, much more was disbursed to all six PFIs in 1:1 credit: Tk 1,570 million (US$26 million) was used for 63 leases and 11 loans. The bridge financing was used by two PFIs, in the total amount of Tk 119 million (US$2.1 million), for 12 leases. The reason for the sparse usage was that the debt issues were immediately matched by 1:1 credit, which was disbursed upon security issuance, thus making the bridge financing redundant in the CBSF structure that actually was implemented. The total credit disbursed under the project amounted to US$43.3 million. Each of the six PFIs issued bonds and debentures (a total of 23 issues to 22 investors) in the amount of Tk 1,408 million (US$23 million), and three PFIs issued ABS for a total of Tk 949 million (US$15 million). Issuing debentures and bonds to private investors is not an initiative that would have taken place without the FIDP support and this should be seen as one of the key achievements of the project. For example, the Tk 5 billion debt raised by PFIs from CBSF financing and their own resource mobilization efforts under the FIDP can be put into a capital markets context by comparing it with the Tk 5.9 billion of total equity capital raised via the Bangladesh capital markets during the same five-year period. The FIDP was the first and (at the time) sole source of debt transactions in Bangladesh.

The project also strengthened the financial condition of the PFIs. By November 2003, these PFIs increased their assets by US$192.67 million and generated total profits of US$20.81 million, of which US$11.02 million was retained in the business as reserves and retained earnings. PFIs have been introduced to the practice of continually meeting the prudential eligibility requirements established by the CBSF, such as capital adequacy; loan loss provisions; acceptable debt-equity and collection ratios; prudent single borrower, group, and industry/subsector exposures; and minimum debt service cover ratios. In addition, PFIs have received TA to strengthen their governance and management practices; Treasury operations; credit evaluation techniques; and ALM capabilities, to name a few.

Moreover, CBSF's activities have added significant value to the development of financial markets in Bangladesh. The CBSF has provided liability diversification for the PFIs, as well as matching funds that have helped strengthen the PFIs' balance sheets and improve their asset liability matching. Thus, their five-year loans have been matched with FIDP's five-year money. These loans, otherwise, would have been funded with short-term borrowing by these PFIs. The CBSF funding has enabled the PFIs to develop scale and momentum in their debt issuance, in the process helping improve practices in related areas, such as the use of issue trustees. CBSF's operations were carried out without a single PFI default throughout the life of the project.

A number of other outcomes have been achieved under the project, such as progress in alignment of NSS rates with the market, stimulation of liquidity, trading of TBs (the first reverse repo transaction occurred under the project), advances in the regulatory framework for bond issuance, and intensive regulator and other stakeholder training. Details on the project results by subcomponent are provided in annex 4 of the Implementation Completion and Results Report.

The first securitized asset sale in Bangladesh took place under the project in November 2004. FIDP took various steps under several of its subcomponents to create an enabling environment for securitization, overcoming impediments such as the lack of legal and institutional infrastructure to support such instruments; high issuance costs; high regulatory compliance costs; and lack of sufficient local skills to manage such deals.[5] Despite the shortfall in expected results under some FIDP subcomponents (see section 8.4), market participants opined that the project came a long way toward creating a facilitating environment for securitization in Bangladesh. Further, after the project closed, a securitization of microcredit receivables by the Bangladesh Rural Advancement Committee took place in July 2006, which was a pioneering transaction in financial markets.

8.3 Efficiency

A conservative estimate of the project's impact during its implementation phase, taking into account the revenues generated by the investment subprojects minus the cost of funding, shows an external rate of return of 14 percent (over the IDA funds) and a net present value (NPV) of US$5.49 million (base case) (see annex 5). Given the absence of any credit defaults in this operation and the positive return to GOB, the exercise has been essentially self financing (GOB has a surplus having repaid IDA in full). OP 8.30 establishes a methodology for the extension of directed credit, in view of the risks of crowding out and misallocation of capital. A Bank FIL may support directed credit programs to promote sustained financing for underserved sectors, provided the programs are accompanied by reforms to address the underlying institutional infrastructure problems and any market imperfections that inhibit the market-based flow of credit to these sectors. In this sense, FIDP passes the OP 8.30 test. The further requirements include, among others, that such reforms include measures to address obstacles that impede the flow of funds to the credit recipients. In this case, CBSF played such a role.

The long-run benefits are expected to be higher. An overall benefit of the project is that it supports the expansion of a more sound and efficient part of the financial sector, providing alternative opportunities for savers and increasing the supply of term funds for competitive projects that generate economic growth and employment. The project increased available funds for investors through eligible FIs, strengthening the efficient FIs and increasing the number of investment projects. The main economic benefit is the establishment of a self-sustainable efficient system of intermediation for term financing; the assessment of this fact requires a longer observation period. Until now, we have observed one follow-up operation

5 Specific measures achieved under the FIDP subcomponents were as follows. The NBR waived the SPV, a legal entity engaged in securitization, from paying income tax, stamp duty, and VAT. The SEC reduced its issue and consent fees, and adopted the new Asset Backed Security Issue Rules 2004. Income taxes were waived on ABS interest income up to Tk 25,000, and taxed at the rate of 10 percent thereafter (subsequently repealed). PFI, investor, and regulator training on securitization considerably contributed to the process.

(outside of the project) of securitizing assets and issuing ABSs for microfinance. A pretty convincing argument suggests that the deal was structured as a result of the awareness raising and capacity building efforts of the CBSF. Whether the market will further pick up the mechanism and use it more readily in the future is a matter of longer-term verification; however, preliminary indications from discussions with market participants are promising, and there has already been a history of one independent securitization deal following FIDP closing.

8.4 Justification of Overall Outcome Rating

Rating: Satisfactory

The project exhibited high relevance of objectives, design, and implementation. It achieved its PDOs (PDO1 was fully achieved, while PDO2 was achieved at 94 percent). The project was efficient per standard measures of the internal rate of return and NPV, as presented above and in annex 5. Furthermore, the project subcomponent objectives were largely achieved, with minor shortcomings, specifically the following: (1) issue rules were developed and implemented, but not at the high-quality standard that one could desire; (2) the GOB, BB, and SEC training was fully achieved; (3) NSS deviations from market terms were reduced, but more can be done; (4) a secondary market for Treasury securities was developed; (5) the CBSF was developed, managed, and funded adequately; and (6) PFI capacity was enhanced and they were helped to mobilize resources, although the life of the CBSF ideally would have been prolonged even if that was not part of the FIDP objectives. The broad activities achieved through the technical assistance component and the private sector activities prompted (and at least assisted) by this project suggest a satisfactory assessment for the Overall Outcome Rating.

8.5 Overarching Themes, Other Outcomes and Impacts

(a) Poverty Impacts, Gender Aspects, and Social Development

The financing provided under the FIDP generated investment and employment, and ultimately, growth in key sectors of the Bangladesh economy. Such analyses typically suffer from attribution difficulty; therefore, we present here only direct impacts immediately resulting from the corporate investments funded by the PFIs, as reported by each borrowing company. The following impact of CBSF's term financing on the development of priority and emerging sectors can be reported.

- Financing the development/priority sectors: Ready-Made Garments (RMG), Food, Textile, and Transportation are the four sectors that have received a major part of CBSF's term financing. These four sectors are priority sectors of the country for development, and other emerging sectors like Ceramic, Power, Accessories, and so on have received substantial support from the project.
- Capacity enhancement: The subprojects have added good value to the production capacity of the priority and emerging sectors. While overall measures are difficult to quote (mainly due to measurement and aggregation issues), one example of enhanced

capacity in the RMG sector alone, is that six subprojects supported by the CBSF between 1999 and 2003 have increased the production capacity of the sector by 613,500 dozen garments per year.

- Employment generation and gender impact: 147 subprojects were supported by the CBSF, which have created direct employment of 14,218 employees, a major part of which included women. Although it is hard to estimate a precise number, through industrial links the subprojects have generated indirect employment for many others.
- Additional profit generation: These subprojects generated additional profits of Tk 3,842 million for the borrowing subprojects.

(b) Institutional Change/Strengthening

The technical assistance component of the project contributed importantly to institution building both at Government agencies (BB, SEC, FAPAD, etc) and in the private sector. According to market participants, the BB was significantly strengthened, and partial success can also be accounted for in the case of the SEC and the PFIs. Specifically, knowledge acquired from the GOB training program (BB, SEC, MOF and others) has contributed considerably to furthering the regulators' understanding and awareness for the need of reform. PFI institutional capacity has been enhanced in important aspects of conducting business, including governance and management practices, strategic vision, monitoring and reporting, technical facets of debt issuance, ALM capabilities, and environmental and audit matters. The CBSF market development program involving financial intermediaries, and various stakeholders (such as journalists) has developed institutional awareness and investment interest in debt and securitization issues.

(c) Other Unintended Outcomes and Impacts

Inefficiencies and delays in obtaining DOE clearances (see section 7.1) caused PFIs to redirect their financing mostly to projects in green and orange categories, including the services sector.

8.6 Summary of Findings of Beneficiary Survey and/or Stakeholder Workshops

Not applicable.

9. Assessment of Risk to Development Outcome

Rating: Moderate

The following risks to the development outcome – to promote NBFI progress, improvements in intermediation quality, and industrial growth—could be considered relevant going forward.

Risks Specific to the Operation and Sustainability

Sustainability of the project beyond implementation depends on four factors:

- Capacity of NBFIs for term lending and fund-raising. This risk is negligible in view of the considerable capacity for resource mobilization developed under the project. Several NBFIs have improved their skills in project evaluation, as well as gained experience with term lending and asset securitization; this experience is likely to be transferred throughout the financial system via learning by example.
- Capacity of regulators on term lending. The advances achieved in GOB/BB/SEC awareness and understanding of debt securities issues are sustainable and unlikely to be reversed in the medium term, and even in the long term, provided that the current low rates of civil servant staff turnover are maintained. Capacity in both private sector and government agencies has developed tremendously over the life of this project. It is difficult to imagine that there could ever be a turning back to the ways of 1998, when government bonds physically could not be traded. Bangladesh has taken some giant steps in the development of its term finance markets and FIDP has been central to those achievements.
- Supply of funds by institutional investors. Achievements in augmenting the supply of funds by institutional investors run a negligible risk of being reversed, once awareness has been raised and institutional investors have been familiarized with the new debt instruments. Current efforts of NBFIs (outside of the project) are focused on developing a clientele among the potential individual investors as well. Note the related risk of changing market factors (for example, interest rates) discussed below. Once could add the caveat, however, that there has been no material change in terms of the mobilization of retail savings through contractual savings institutions in Bangladesh, which represents a considerable risk. Though capacity might be argued to be in place, the mechanism for bringing finance to market is largely lacking.
- Demand for term funds by high-quality projects. This risk is negligible due to the relatively low scale of term financing currently available in the country, which is disproportionately small relative to existing private sector term financing needs. The risk likelihood would rise in the long run as the supply of long-term financing increases, but international experience shows that the impact is low because of the improvements in sophistication of project assessment and other innovations in the industry that render it profitable to serve even higher-risk projects.

Risks from Factors Outside of the Operation

The following four factors present risks outside of the operation:

- Changing market conditions. Market conditions present a significant risk (decreasing to moderate in the medium term and negligible in the long term) of temporarily dissuading NBFIs to raise fund capital through debt security issuance. Specifically, high interest rates make debt securities costly for NBFIs to issue and their returns appear unattractive to investors when compared with the returns of other lower-risk instruments. Despite the significant likelihood of temporary abatement in debt securities issue activity because of changing interest rates, the impact is moderate to low (especially in the medium term) because of the adaptability of NBFIs, the flexibility of the financial instruments involved, and the increasing confidence of NBFIs with debt and ABSs. The impact will, of course, depend on the severity and nature of the interest rate change; however, the low risk of a financial crisis is mitigated by the IMF's continued involvement and monitoring.

- Development of market sources of funding for term lending. The advances achieved in Treasury markets are sustainable and unlikely to be reversed. Prospective change at NSS should be far from taken for granted, in as much as this process has not been currently initiated. The risk is mitigated by follow-up WB work on NSS, which serves to maintain the momentum of the advances achieved thus far. The risk of reversal in SEC reforms revamping issuance rules, lowering issuance costs, and modifying other related regulations is negligible, and further improvements will be pushed via future WB work. A risk is presented from the side of NBR and tax issues––changes and revisions in taxation and stamp duties are a continuing source of uncertainty and should be adequately addressed in future WB work (see section 7.5). More objectively, the tax holiday provided to zero coupon bonds should be regarded as an anomaly that is not seen in other successful markets. Tax issues are within government control, and would be predicated on GOB's broader commitment to financial market development, which seems to be in place. Further, the fiscal cost of bringing about the liberalization of the tax system required to facilitate market development would be very modest and the obstacles are primarily administrative.
- Credit rating may take too long to start being effectively used. The two established credit rating agencies still lack the experience of international-level credit rating. Furthermore, investors have not developed an appreciation of the relationship between risk and return, instead using the reputation of the issuer as a proxy for risk and disregarding the risk characteristics of the instrument itself. International competition from multinationals like Moody's and Fitch would help the development of this market to reach world-class levels. Additionally, increasing the use of ABS and simple debt securities would promote investor education on the risk characteristics of each instrument. That being said, international experience shows that markets can develop without credit rating agencies, which have been a phenomenon in developed markets for only the last century and outside North America for only two or three decades, well after the establishment of vibrant debt markets.
- Potential risk of contagion of NBFIs. Going forward, this risk is assessed as negligible, in view of the performance of subprojects under the FIDP. Among PFIs, there was not a single default, and although some subprojects experienced payment delays, there were no defaults. As noted above, the market is starved of long-term funds, permitting to hand select a steady stream of high-quality projects to finance. By the nature of the project, it is designed so that funds flow from NCBs to NBFIs (because NCBs are investing in NBFI-issued debt securities), which also limits contagion risk.

Taking into account the above, it is possible that some of the aspects of the PDO may not be sustained (for example, because of tax considerations), consequently rating the overall risk to Development Outcome as moderate.

10. Assessment of Bank and Borrower Performance

10.1 Bank

(a) Bank Performance in Ensuring Quality at Entry

Rating: Satisfactory

The project is highly relevant and responds closely to the needs of the country at this level of development. The approach, as noted in section 7, was complex and ambitious and has achieved its goals. The FIDP technical, financial, and economic aspects were characterized by an innovative strategy, and specifically targeted the young, dynamic NBFI sector, which carried a likelier promise for developing term financing markets than the ailing Bangladesh NCB sector. The project came at an opportune time, when access to finance was becoming a palpable barrier for maintaining and raising existing private sector growth rates in Bangladesh. The project was structured to link the development of the NBFI sector and intermediation improvements to financing of the real sector, job creation, and growth. In particular, the newly generated long-term financing has resulted in many new jobs, particularly for women, in the garment industry and related sectors. The environmental aspects of the project were addressed by providing DOE clearance for all subprojects that were financed, although the inefficiencies associated with this government agency were not taken into account and mitigated at project entry (a parallel WB project was addressing the issue).

Procurement, financial management, and reporting arrangements of the project were adequate. The policy and institutional aspects of the project suffered somewhat from weak government commitment in certain areas, such as tax and stamp duty regulations, in spite of clearly declared government intentions to the contrary that mitigated government commitment risk. Implementation arrangements were satisfactory, although the need for training of the selected project auditor (FAPAD) could have been foreseen. The project benefited from a good system of M&E. In view of the significant development of M&E in the WBG in the past five years, hindsight suggests perhaps a more detailed approach to subcomponent output measurement. The project underwent a detailed risk assessment (see section 9). Bank inputs and processes were satisfactory. In view of the above considerations, the Bank-provided services have ensured that the quality at entry of the operation was satisfactorily.

The QAG at entry rating was moderately unsatisfactory. The report notes the sound financial sector work that served as the background preparation for the project, the high quality of selected participating FIs, and the adequate expected demand from borrowing enterprises and from the FIs on the credit line facility. The report acknowledges the significance of some policy changes already achieved under the project, particularly reducing the stamp duty on fixed-income securities registration; constraining NCB lending; and allowing insurance, companies, pension funds, and NCBs to invest in securities.

While the QAG agrees on the need to develop NBFI term debt security markets, it expresses serious doubts about the need for the complexity of asset-backed securitization as opposed to simple fixed-income securities. Undoubtedly the project suitably addressed the issue of term finance, at the appropriate time for Bangladesh, yet, one could express some sympathy for the QAG arguments. The FIDP technical assistance has been invaluable in enabling both Government and private sector to raise standards and has supported a trend that was nascent at the time of appraisal. Equally, however, the structure of the project was undoubtedly excessively complex and perhaps expensive. The PIU embodied in the CBSF goes against modern views in terms of mainstreaming and the fact that it has been discontinued is a reflection of its lack of utility. The complex secondary market mechanisms envisaged in FIDP have not evolved at all. The challenges in running the CBSF were significant and it never really reached the standards which were necessary for it to be effective.

This being said, securitization is turning out to be the right product for Bangladesh. Quite separate to the "supply" of this project, private sector entities are actively promoting securitization in Bangladesh (most notably of microfinance receivables). Without the ground breaking work of FIDP, this advance would probably not have taken place. The technical expertise is present in Bangladesh (much having returned from overseas markets) and if the QAG team felt that securitization was "too complex" for Bangladesh, they have been proven wrong.

While designing the project, an issue arose regarding NBFI supervision and prudential regulation reforms, which could be placed under this project or alternatively under the CBSP described above. The QAG disagreed with the strategic choice made at project design to place supervision issues under CBSP, while focusing the FIDP on developing the term debt finance framework. Yet, QAG noted that it "found a lot of merit in the underlying country strategy in Bangladesh which argues for simple projects with clear objectives within a coherent long-term framework." The same CAS goal is also cited in the PAD as motivating the placement of NBFI supervision under CBSP, "to allow a sharper focus for the proposed FIDP while assigning two important related activities to those projects under which they constitute the main focus of their operation."

(b) Quality of Supervision

Rating: Satisfactory

Project implementation has benefited from the following aspects of supervision quality:

- Implementation has been carried out with a focus on maximizing the project's development impact. In particular, project supervision has resulted in continual readjustment and emphasis on institutional and regulatory training and awareness raising; capacity creation in the non-banking financial sector; and TA on regulatory and institutional improvements to facilitate the functioning of financial markets. The midterm review budget reallocation tried to make the most of the prevailing institutional and regulatory framework and to achieve the highest possible mobilization of term finance.
- Procurement, fiduciary, reporting, and financial management were closely supervised. Delays in procurement of consultants were promptly addressed and repeatedly attended to, as needed, until the problems were resolved. In response to the issues with FAPAD, a series of tripartite meetings were organized, creating a forum in

which the issues could be resolved.

- Supervision inputs and processes have been adequate. Swift resolution of issues and problems is again the main theme evident to an outside observer. For example, a cul-de-sac reached in GOB's commitment to further reform in 2002 was resolved by calling for (1) a retreat of the main GOB parties involved, and the Bank, and (2) brainstorming and creating solidarity until the issues were resolved. As another example, DOE inefficiencies were repeatedly targeted through a variety of approaches in an attempt to eliminate or speed up DOE functioning, including an approach to the DOE's reporting ministry (the Ministry of Environment and Forests). Finally, numerous consultations were held with PFIs on upgrading the MIS and other systems to achieve a consensus on the best approach to monitoring systems for the industry.
- Regular ISRs have been produced, which are candid and detailed, well targeted to outline important events, and well argued. More tables and a sense of a big picture would have improved the presentation (template permitting); however, presentation issues aside, the ISRs contain exhaustive information relevant to the project and permit the formulation of a clear and complete picture of the advance of the FIDP's work.
- The project implementation team had a paramount role in ensuring the adequate transition arrangements for the FIDP. Upon the GOB's expression of lack of support for privatizing the CBSF, the team moved to ensure a smooth transition of the CBSF from the international consultant to the BB's management. Necessary arrangements were made for transferring facility management skills to qualified local professionals and local consultants as well as to the BB's secondees.

Based on the above considerations, the Bank-provided services have supported satisfactorily the effective implementation through appropriate supervision (including adequate transition arrangements for regular operation of supported activities after project closing).

(c) Justification of Rating for Overall Bank Performance
Rating: Satisfactory

Combining the two ratings for quality at entry and quality of supervision, overall Bank performance is rated as satisfactory.

10.2 Borrower
(a) Government Performance
Rating: Moderately Satisfactory

Government performance in the project is rated moderately satisfactory due to incomplete (though fully adequate) ownership of the project by the GOB (see detailed reasons outlined below). An alternative standpoint could be taken that the project design might have placed taxing demands upon GOB. Equally, there is room for higher achievement in terms of the leadership and capacity at the SEC and improvements at NSS.

- Government ownership and commitment was a particular issue in some aspects of the project, such as the reform of stamp duties by NBR and the adoption of integrated, high-quality public issuance regulations by the SEC.

- The GOB maintained an enabling environment, including supportive macro- and sectoral policies. Several institutions were created and strengthened, which contributed to the achievements of the project, such as the CDB electronic registry, the BB functions of auctioning Treasury securities, and successful SEC reforms on ABS, private issuance, and reduced issuance costs.
- Consultations with government agencies related to the project were not adequate. Securing the involvement of some government agencies such as FAPAD, DOE, DNS, and NBR was difficult.
- GOB preparation for implementation was adequate. A steering committee was appointed on time.
- GOB was deficient in contributing to the timely resolution of implementation issues (for example, in the case of procurement delays, FAPAD, DOE, and the SEC reform of the Public Issue Rules).
- Fiduciary arrangements were adequate. Inefficiency issues were experienced and addressed with the DOE. Provision of counterpart funding was implemented as agreed. GOB complied with the DCA as negotiated.
- GOB's coordination with donors, partners, and stakeholders fell short of achieving satisfactory results, although attempts were not lacking. This is the case, for example, with the Bank requests for coordination with NBR and FAPAD.

The borrower ensured quality of preparation and implementation moderately satisfactorily.

(b) Implementing Agency or Agencies Performance
Rating: Satisfactory

Implementing Agency	**Performance**
Bangladesh Bank	Bangladesh Bank has been key to the success that this project has enjoyed. Starting with limited capacity and an extremely antiquated system, the Bangladesh Bank has come a long way, managing the complex administrative arrangements of the CBSF. The energy applied to development of securities markets by the Governor and his advisor has been extremely important. Agency performance in the project is rated satisfactory for the following reasons: The BB displayed adequate commitment to developing the long-term lending capacity of the NBFI sector. • Beneficiary and stakeholder consultations were adequate. NBFIs and investors demonstrated activism and interest in the project. • The BB was adequately prepared for implementation, ensured implementation arrangements and capacity, and cooperated on appointments of key staff. It further seconded staff to the CBSF for training and learning, and smoothly took over the CBSF at the end of the FA's term in office. • Implementation issues were resolved by the BB in a relatively timely

fashion, with minor exceptions (for example, procurement of the NSS consultant).

- Fiduciary issues management by the BB was adequate
- M&E was adequate in the context of contemporary projects, but note the double-supervision work of the CBSF adviser and the BB discussed in section 7. M&E data were utilized successfully in decision making and resource allocation (for example, the budget reallocation at the midterm review).
- The BB coordination with SEC was insufficient (for example, in terms of training and in discussions of issue rules).
- Transition arrangements for regular operation of supported activities under the FIDP were adequate. The transfer of the CBSF to the BB in February 2005 was smooth and successful.

The implementing agency ensured quality of preparation and implementation satisfactorily.

(c) Justification of Rating for Overall Borrower Performance
Rating: Moderately Satisfactory

Combining the two ratings for government and implementing agency performance, overall borrower performance is rated moderately satisfactory.

11. Lessons Learned

Following are the lessons learned from the Bangladesh FIDP

1. A concern identified during mid-term review was that SEC training was undertaken on an ad-hoc basis without a proper needs assessment. By that time, BB had used the training sub-component relatively sparingly, and in particular there was weak exposure to training of the staff and officials in the Financial Institutions Department. BB and SEC training activities had not benefited from coordination of arrangements. In response, SEC and BB both carried out a training needs assessment to develop a training program, which was followed for the latter part of the project. ***A training needs assessment at project design or early in the implementation stage permits efficient structuring of training events, fully utilizing training funds, organizational synergies, advance coordination among all government agencies to benefit from the training, and maximizing efficiency while lowering costs.***

2. ***For projects with innovative components, a separate communications program outlined and budgeted at project design phase can improve project understanding and buy-in.*** In this particular case, the communications program could have provided from project inception (and did since mid-term review) ongoing investor education and

awareness-raising in view of the heavy innovation content of the project, as well as the highly technical mechanisms involved, with which the investor and financial community needed more detailed familiarization.

3. ***Reforms planned during the project implementation phase can benefit from a careful assessment of their champions and opponents.*** Reforms should only be pushed by the project if at least one champion has resolved all their issues with the reform and is ready to unconditionally back it up. In the case of this project, both BB and SEC has small unresolved issues with the draft SEC Fixed-Income Securities Issue Rules, so that tensions between the two champions left the draft legislature as the victim of the disagreement, unsupported by any government agency. Reforms can increase their chances of being implemented if they deal with a narrow set of issues, involving a minimal number of government agencies (possibly a single agency).

4. The project goals were noted to be highly complex. In spite of the good reasons that backed up this decision, project complexity raises risks of delivery failure. The project addressed several reforms simultaneously (Treasury paper market, NSS, and private debt instruments) and involved several agencies (SEC, DNS, BB, and NBR). These factors made it difficult to successfully manage all components, while maintaining government commitment and project momentum. ***In projects involving complex and innovative components, project phasing helps streamline goals and account for progress and existing commitment before moving to a subsequent step.*** For example, the FIDP could have benefited from the following phases: (1) preparing the market and regulatory environment (NSS and NBR reforms); (2) preparing the legal environment (SEC reforms); and (3) launching the CBSF funding facilities.

5. By Bangladesh laws, project director liability (for projects overseen by government entities) constrains innovative decisions and deviations from established business practice. In these cases, any auditor's failure in understanding the entity's actions results in audit comments that increase the personal liability of the government official involved. Unfortunately, undertraining and turnover at the supreme audit body (FAPAD) makes for frequent and multiple deficiencies in understanding. As a result, IDA projects might incur excess cost, or delays, as well as other barriers to implementation. For example, the FIDP experienced a double level of control without added benefits, in which BB staff duplicated the functions of the CBSF adviser (an international professional who was specifically hired to perform these tasks), wasting money and time.[6] There is no liability insurance and no business judgment rule that would allow reasonable risk-taking in good faith to go unpunished. ***The assurance of a reasonable amount of liability that still would provide proper fiduciary duty without paralyzing the project director's actions because of excessive strictness would facilitate the undertaking of business risks in good faith and allow for efficient project management, implementation, creativity, and functioning.***

6 There is an argument that the BB’s double effort might have promoted BB staff learning. Excessive liability might also be considered less of a dead-weight loss in the Bangladesh environment of poor governance than in other countries.

6. The project failed to foresee the training needs of FAPAD, the supreme audit body. ***Careful review of all potentially important actors involved in a project, and all their expected impacts and needs, would increase the chances of successful and smooth project implementation.***

12. Comments on Issues Raised by Borrower/Implementing Agencies/Partners

(a) Borrower/implementing agencies

- As the implementing agency BB had the responsibility to supervise and oversee CBSF activities. To reduce risk BB reached all funding applications before disbursement. However this did not hamper smooth disbursement of CBSF funding.

- IDA may take necessary initiative with the coordination of GOB for the new avenues as identified in section 7.5(next phase: follow up operations).

- For better understanding and smooth implementation, communication program may be initiated at the early stage of project implementation where regulators, beneficiaries, stakeholders, donors and FAPAD may participate.

(b) Cofinanciers

Not Applicable.

(c) Other partners and stakeholders

- The SEC feels that training events would have benefited from more details and depth and perhaps would have been more productive if they had been conducted over a longer duration.

- FIs felt that the FIDP helped bridge the asset liability maturity gap and provided competitive funding. Building a clientele for fixed-income securities is the next step for PFIs, both by raising awareness with institutional investors and developing a clientele of individuals along private wealth management lines. Mixed feelings were expressed about ABS, mainly because the market failed to price the lower risk embodied in the ABS and discount it appropriately in view of its risk characteristics. After the end of the project, NBFIs still face the problem of obtaining long-term funding.

Annex 1. Results Framework Analysis

Project Development Objectives (from Project Appraisal Document)

Project Development Objective (PDO)
The FIDP objective was to promote the development of NBFIs, in particular, and investment financing, in general, on a sustainable basis that would contribute to improvements in the quality of intermediation and the speed and efficiency of industrial growth in Bangladesh.

The sector-related CAS goal for FIDP was to support the government's poverty reduction strategy of promoting rapid, job-creating economic growth by fostering the development of investment financing on a sustainable basis. Measures on the increase in investment financing served as key performance indicators. The critical assumptions made were that the political and investment climate in Bangladesh was improved or maintained and that the GOB would display an adequate commitment to implement financial sector reforms and avoid policies that distort financial markets.

The Project Appraisal Document (PAD) lists the key performance indicators as follows:

- Increased term financing by eligible NBFIs and other FIs (defined as cumulative disbursements of credit subcomponents to eligible FIs as a share of available funds, with the following target levels: 30 percent by the first year; 70 percent by the second year, and 100 percent by the third year).

- Increased share of market sources of funds for eligible NBFIs and other FIs (defined as the market funds raised by FIs via bonds, debentures, and Asset Backed Security [ABS], as a share of disbursed IDA funds, with the following target levels: 10 percent by the first year, 25 percent by the second year, 50 percent by the third year, and 100 percent by the fourth year).

Revised Project Development Objectives (as approved by original approving authority)

Not Applicable.

(a) PDO Indicator(s)

Indicator	Baseline Value	Original Target Values (from approval documents)	Formally Revised Target Values	Actual Value Achieved at Completion or Target Years
Indicator 1 :	Increased term financing by eligible NBFIs and other FIs.			
Value (quantitative or Qualitative)	Increase in term financing by FIs severely limited by lack of fund mobilization	Term financing by FIs increased by at least US$45 million.	Not Applicable.	Term financing by FIs increased by at least US$45.6 million

	sources.			
Date achieved	01/31/2000	02/28/2006	02/28/2006	02/28/2006
Comments (incl. % achievement)	100%			
Indicator 2 :	Increased share of market sources of funds for eligible NBFIs and other FIs.			
Value (quantitative or Qualitative)	Negligible share of market sources of funds in the total funding structure of PFIs.	PFIs raise an equal amount from the market as provided under CBSF.	Not Applicable.	PFIs raise from the market 94% of the amount provided under CBSF.
Date achieved	01/31/2000	02/28/2006	02/28/2006	02/28/2006
Comments (incl. % achievement)	94%			

(b) Intermediate Outcome Indicator(s)

Indicator	Baseline Value	Original Target Values (from approval documents)	Formally Revised Target Values	Actual Value Achieved at Completion or Target Years
Indicator 1 :	Cumulative disbursements of credit subcomponent to eligible FIs to reach 100 percent of credit allocation by the closing date.			
Value (quantitative or Qualitative)	No disbursement.	Cumulative disbursements reach US$40 million.	Not applicable.	Cumulative disbursements reach US$43.5 million.
Date achieved	01/31/2000	02/28/2006	02/28/2006	02/28/2006
Comments (incl. % achievement)	100% (simple credit + 1:1 credit disbursements)			
Indicator 2 :	Participating FIs increase market sources of funding by 100 percent of IDA funds provided under CBSF.			
Value (quantitative or Qualitative)	Market sources of funding is Nil.	Market sources of funding increased to US$40 million.	Not applicable.	Market sources of funding increased to US$38.4 million.
Date achieved	01/31/2000	02/28/2006	02/28/2006	02/28/2006
Comments (incl. % achievement)	96%			

Annex 2. Restructuring (if any)

Not Applicable

Annex 3. Project Costs and Financing

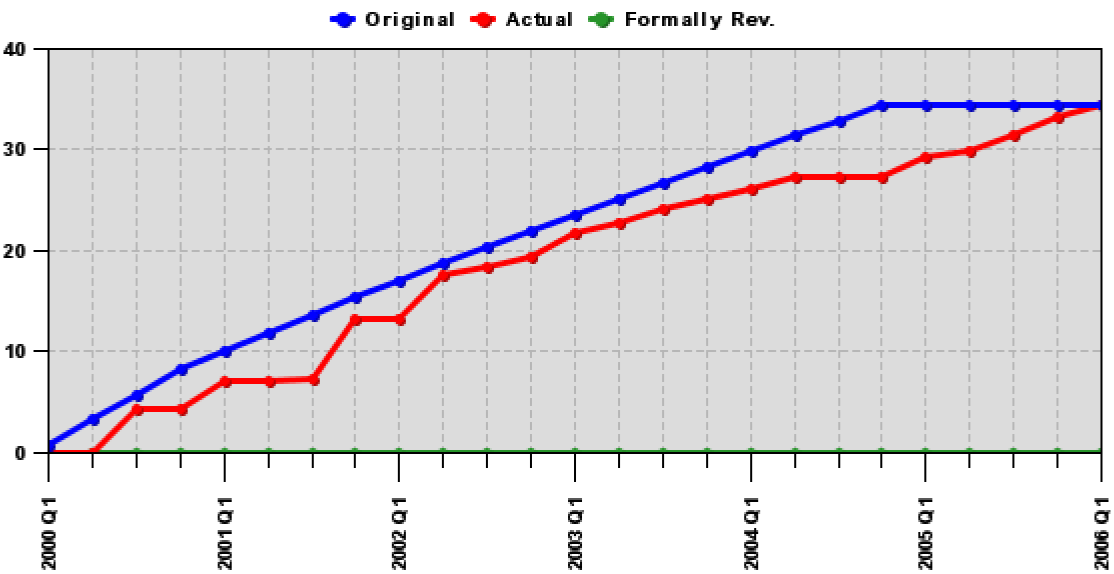
(a) Project Cost by Component (in USD Million equivalent)

Components	Appraisal Estimate (USD M)	Actual/Latest Estimate (USD M)	Percentage of Appraisal
Development and implementation of Issue Rules for Bonds / Debentures	0.35	0.34	97.14
SEC Training on Debt Instruments	0.05	0.05	100.00
BB Training on Debt Instruments	0.05	0.00	.00
Reform of Government Savings Schemes	0.67	0.15	22.06
Development of Procedures for Secondary TB Market	0.40	0.00	.00
Development of CBSF	1.30	0.50	38.46
Management of CBSF	2.50	2.85	114.00
Funding of CBSF	49.00	47.58	97.10
Capacity Enhancement of PFI Business Planning	2.30	0.08	3.48
Resource Mobilization for PFIs	0.43	0.13	30.23
Revision of CBSF Mechanism	0.64	0.00	.00
Total Baseline Cost	**57.69**	**51.68**	**89.6**
Physical Contingencies	0.00	0.00	0.00
Price Contingencies	0.00	0.00	0.00
Total Project Costs	**57.69**	**51.68**	**89.6**
Front-end fee PPF	0.00	0.00	0.00
Front-end fee IBRD	0.00	0.00	0.00
Total Financing Required	**57.69**	**51.68**	**89.6**

(b) Financing

Source of Funds	Type of Cofinancing	Appraisal Estimate (USD M)	Actual/Latest Estimate (USD M)	Percentage of Appraisal
Borrower		5.41	5.19	95.93
IDA		46.90	46.48	99.10

(c) Disbursement Profile



Annex 4. Outputs by Component

Tables of Implemented Measures

Development and Implementation of Issue Rules for Bonds and Debentures:

2% registration fee for issuance of bonds and debentures was waived in 2000.
Stamp duty of 2.5% of total amount of issue reduced to Tk 2,500 on April 26, 2001.
SPV exempted from VAT, income tax, transfer duty, and capital gains tax.
SEC public issue /consent fee (for public and private issues) was reduced from a flat 0.1% to 0.1% for an issue less than Tk 50 million (US$719,528) and 0.02% for higher amounts. In addition, the SEC consent fee for public issues was reduced from Tk. 10,000 + 0.3% of the issue amount, to Tk. 10,000 + 0.15% of the total amount raised.
Prospectus publication (for public issues) needed to be published in two papers, in full, at the cost of Tk. 400,000 (US$5,756). Modified to allow summary publication, with a reference to the online location where the full information is available (including SEC, stock exchange, and company websites).
Underwriting commission (for public issues) was effectively reduced in half.
Bankers' commission (Banker to the issue fee) – reduced from 0.25% to 0.1% (for public issues).
Broker's commission /Seal commission of 1% was abolished.
Issue management fee of 1% (for public issues) was capped at Tk. 2m (US$28,781).
SEC Issue of Capital Rules, 2001 were adopted.
Asset Backed Security Issue Rules, 2004 were adopted.
SEC Public Issue Rules, 2006 were adopted.
Detailed draft issue rules submitted to SEC.

SEC /BB / GOB /PFI training and capacity building on fixed income securities

31 Jan – 4 Feb, 2000, Workshop on Non Bank Financial Institutions: Development and Regulations, World Bank, Washington. Participants: Mr. M.A. Sayeed, Chairman, Securities and Exchange Commission.
29 Feb – 1 Mar, 2000, Workshop on FIDP Launching. Participants: Financial Institutions Representatives.
31 Mar - 1 Apr, 2000, Conference on " Emerging Markets in the New Financial System: Managing Financial and Corporate Distress", World Bank, Washington. Participants: Mr. Suvro Kanti Chowdhury, Deputy Director, Securities and Exchange Commission.
16-20 July, 2000, Training on "Procurement, Disbursement and Financial Management", Bangladesh Arsenic Mitigation Water Supply Project (BAMWSP), BRAC , CDM Centre , Rajendrapur, Gazipur, Bangladesh. Participants: Mr. Md. Mofazzal Hossain, Deputy Director, Bangladesh Bank.
1-11 May, 2001, Banking and Capital Markets familiarization Program on Senior Officials, Bank of England, UK, HSBC, UK, Federal Reserve Bank, USA, CITI Bank , New York, USA, Securities & Exchange Commission, USA, New York Stock Exchange, USA, IDA, USA. Participants: Mr. A H Toufiq Ahmed, Deputy Governor, Bangladesh Bank; Mr. Habib Abu Ibrahim, Joint Secretary, Finance Division; Mr. Ziaul Hassan Siddiqui, Executive Director, Bangladesh Bank.
3-14 December, 2001, Financial Management and Disbursement Course, ILO Training Center, Turin, Italy. Participants: Mr. Sheikh Mozaffar Hossain, Deputy Director, Bangladesh Bank.
Retreat for BB, CBSF & WB staff August 20-21 2002.
11-15 March , 2002, Training On Debt Instruments, Securities & Futures Commission, Hong Kong. Participants: Mr. K. Iftikher Ahmed, Member , SEC, Mrs. Ruksana Chowdhury, Director, SEC, Mr. A K M Ziaul Hassan Khan, Deputy Director, SEC, Mr.Md. Nasir Uddin Ahmed, Senior Assistant Secretary, Finance Division, Ministry of Finance.
27 May-4 Jun 2002, Study Tour on " Debt Market" and "Asset Securitization", Reserve Bank of New Zealand, National Bank of New Zealand, New Zealand Securities Commission, New Zealand Stock Exchange, Reserve Bank of Australia, Bay Corp. Advantage, Australia, Standard and Poor , Australia, Australian Securities and Investment Commission, Australian Prudential Regulatory Authority. Participants: Mr. Ziaul Hassan Siddiqui, Executive Director, Bangladesh Ban, Mr. Abdul Hannan Zoarder, Executive Director, Securities and Exchange Commission, Mr Saifuddin Ahmed, Deputy Secretary, Finance Division , MoF, Mr. Mofiz Uddin Chowdhury, General Manager, Bangladesh Bank, Mr. Md. Mofazzal Hossain, Deputy Director, Bangladesh Bank, Ms. Rubayet Jesmin, Asstt. Director, Bangladesh Bank.

3 Sep, 2002, How Can NBFIs Play Greater Role In a Bank Based Economy, Bangkok, Thailand, Mr. Munir Uddin Ahmed, Chairman, Securities and Exchange Commission.
3-8 Feb, 2003, International Management Development Programme on Financial Management of the World Bank Funded Project, National Institute of Financial Management, Hariana, India. Participants: Mr.Md. Nasir Uddin Ahmed, Senior Assistant Secretary, Finance Division, Ministry of Finance, Mr. A K M abu Raihan, Senior Asstt. Chief, Planning Commission, Mr. Abdul Wahab, Asstt. Director, Bangladesh Bank.
5-6 Mar, 2003, Communication Program. Participants: High Officials of Bangladesh Bank.
12 May, 2003, Workshop on Environmental Compliance. Participants: Representative from participating financial institutions (PFIs), Bangladesh Bank, and Directorate of Environment Officials.
8-20 Feb, 2005, Australia Study Tour, Reserve Bank of New Zealand, New Zealand Securities Commission, NewZealand Securities Commission, NewZealand Stock Exchange, Reserve Bank of Australia, Australian Securities and Investment Commission, Australian Prudential Regulatory Authority, ABN Amro, Sydney , Australia. Participants: Mr. Sudhir Chandra Das, Deputy General Manager, Bangladesh Bank, Mr. Chowdhury Md. Firoz Bin Alam, Joint Director, Bangladesh Bank, Mr. Abdul Wahab, Asstt. Director, Bangladesh Bank, Mr. Md. Alamgir, Asstt. Director, Bangladesh Bank, Ms. Khaleda Akhter, Joint Chief, Planning Commission, Mr. Arijit Chowdhury, Senior Assistant Secretary, Finance Division, MOF, Mr. Saiful Islam, Asstt. Chief , ERD, Mr. Hassan Mahmood, Deputy Director, SEC.
17 Jun – 2 Jul 2005, Development and Implementation of Issue Rules and Regulations to foster Secondary Market Development, Securities and Exchange Commission , Sri Lanka, Central Bank of Sri Lanka, Reserve Bank of India, Mumbai, Fixed Income Money Market Dealers Association of India, Mumbai, India, Clearing Corporation India, Mumbai, National Stock Exchange, India, Mumbai Stock Exchange, Securities and Exchange Board of India , Mumbai, Rating Agency of Malaysia, Kualalampur, Bnak Negara , Malyasia, Securities and Exchange Commission , Kualampur. Participants: Mr. Abdul Hannan Zoarder, Executive Director, Securities and Exchange Commission, Ms. Fahima Yasmin, Senior Assistant Secretary, Finance Division, MOF, Mr Safiul Azam, Deputy Director, SEC, Ms. Kakoli Zahan Ahmed, Deputy Director, Bangladesh Bank, Ms. Husne Ara Shikha, Deputy Director, Bangladesh Bank, Mr. Rathin Kumar Paul, Assistant Director, Bangladesh Bank, Ms. Farhana Faroki, Assitt. Director, SEC.
12-20 Dec, 2005, Market, prudential guidelines and supervision of financial institutions, Central Bank, Philippines, Stock Exchange, Manila, Securities and Exchange Commission, Manila, CITI Bank NA , Manila, Stock Exchange, Jakarta, Securities and Exchange Commission, Indonesia, Citibank, Indonesia. Participants: Mr. Murshid Kuli khan, Executive Director, Bangladesh Bank, Mr. Abdus Samad, General Manager, Bangladesh Bank, Mr. Masum Patwary, Joint Director, Bangladesh Bank.

Reform of National Savings Schemes

Reports on NSS reform (situation report, IT assessment report, MIS automation plan, Financial market report) filed with MoF, currently under GOB consideration.
10% withholding tax on interest income over Tk. 25K per year on National Savings Certificates was imposed.
The DNS withdrew the high interest bearing Paribar Sanchaypatra (5 years).
The DNS withdrew the high interest bearing Pratirakha sanchay patra.
The DNS withdrew the high interest bearing 6 monthly profit bearing sanchay patra (5 years).
The number of categories of Sanchay Patras has been decreased to 2.
The interest rates on NSS on 5-year Sanchay Patra were reduced in 2002-4 (but raised again thereafter).
The interest rates on NSS on 3-year Sanchay Patra were reduced in 2002-4 (but raised again thereafter).
Financial institutions were made ineligible to hold NSS instruments.

Development of Procedures for Secondary Treasury Bond (TB) Market

BB operationalized the repo system for 28-day T-bills in 2002, the first repo transaction in Bangladesh was carried out in Jan 2003.
Reverse Repo systems have been introduced in 2003.
BB issued for the first time 5- and 10- year T-Bonds in Dec 2003.

Development and Management of the Credit, Bridge and Standby Facility (CBSF)

FIDP communications activities and PFI and market development programs.

CBSF internal control, management, and IT systems were set up.
Integrated development of BB staff seconded to CBSF.
Exposure of PFIs to international best practice in Credit Management and ALM.
Discussions with journalists to raise awareness on capital markets and international best practice.
Continuous advice and reporting to BB on CBSF and FIDP development.
Annual PFI eligibility reviews were conducted on 31/12/2000, 31/12/2001, 31/12/2002, 31/12/2003, 31/12/2004, plus continuous quarterly monitoring of PFI edibility.
A repo transaction was undertaken with Janata Bank in early 2003 and the first reverse repo transaction was completed with Dutch Bangla Bank in Mar 2004, followed by a reverse repo with Eastern Bank in Dec 2004.

Funding the Credit, Bridge and Standby Facility (CBSF)

Simple credit of Tk. 957 million (US$16.2m) was used by all 6 PFIs, for 53 leases, and 8 loans.
Total 1:1 credit disbursed to 6 PFIs was Tk. 1,570 million (US$27.1 million), used for 61 leases, and 11 loans.
Bridge finance disbursed: 2 PFIs, for a total amount of Tk. 119,121,189 (US$2.1 million), used for 12 leases.
Stand-by finance – not used.
Liquidity mechanism: not used.
The total credit disbursed under the project amounted to US$43.3 million.
The total financing disbursed under the project amounted to US$45.4 million.
A total of US$38 million was raised by the 6 PFIs in debenture, bond, and asset-backed securities financing.
Total funds raised through securitization by 3 PFIs was Tk. 948.58 (US$15 million).

Capacity Enhancement of FIs Business Planning, Resource Management and MIS

TA on governance and management practices; treasury operations; credit evaluation techniques; and asset liability management capabilities, lending and debt issue documentation, environment, audit, business planning.
CBSF prepared a report on MIS with an assessment of software solutions in Feb 2005.

List of Training Events undertaken by PFIs:

Feb 29-Mar 1, 2000, Workshop on FIDP Launching. Participants: Financial Institutions Representatives.
Video-conference on Issuance of Debt Instruments in Bangladesh, Washington, DC, August 7, 2001.
25-27 Sep, 2001, Workshop on Securitization. Participants: Financial Institutions Representatives.
26-28 Aug, 2002, Investor Mini Forum. Participants: Prospective investors comprising representatives from insurance companies, commercial banks, corporate bodies with liquid funds and other micro finance institutions.
12 May, 2003, Workshop on Environmental Compliance. Participants: Representative from participating financial institutions (PFIs), Bangladesh Bank, and Directorate of Environment Officials.
9 Jul, 2003, Workshop to inform about debt instruments issued by PFIs. Participants: NCB Representatives.
12,14 and 16 Aug, 2004, Workshop on Securitization. Participants: Representative from PFIs.
1-2 Dec, 2004, Workshop on Development of Band Market in Bangladesh. Participants: Prospective investors comprising representatives from insurance companies, commercial banks, corporate bodies with liquid funds and other micro finance institutions with resource persons from home and abroad.
29-30 Aug, 2005, International Workshop on Infrastructure in Bangladesh. Participants: Prospective investors comprising representatives from different corporate bodies concern for infrastructure, insurance companies, commercial banks with resource persons from home and abroad.

PFI resource mobilization

Securitization reports: monthly, inception, and final reports, overviewing the key elements of securitization, their implementation in the conditions of Bangladesh, SPV structure, underlying assets, credit risks, regulation of securitization in Bangladesh, accounting treatment, documentation of transactions, rating of issues, educational support, and detailed recommendations / roadmap for implementation of securitization in the country.
AIMS report on asset securitization by Financial Institutions in Bangladesh of Sep 2002.
Heightened awareness of the importance of the public and private debt markets amongst key government agencies, such as, SEC, MOF, and IRD/NBR; improved institutional investor awareness of and participation in the NBFI sector; support to PFIs with investor marketing, issue structuring and documentation in the context of securitization

Revision of CBSF Mechanism

CBSF Action/Implementation Plan, including transfer issues.
CBSG successfully transferred to BB on Feb 13, 2005.

Annex 5. Economic and Financial Analysis

The overall economic benefit of the project was its support of the expansion of the sound and more efficient part of the financial sector, providing alternative opportunities for savers and an increased supply of term funds for competitive projects. Since the project was designed to have a catalytic role in supporting NBFIs' efforts to raise term funds for investment lending it is difficult to quantify its long term impact. This long term impact would consist in the additional benefits to the economy arising from the more efficient use of savings to finance investment projects (increase in consumer's and producer's surplus) during and beyond the project's life when NBFIs continue to raise funds without the project's support.

However, an attempt has been made to quantify the short term impact during the project's life based on the stream of long term financing generated in the NBFI system during the project, directly by IDA funding as well as indirectly through PFI's own securities issuance. This yields a positive NPV ($0.9 million) and an IRR of 6% on IDA credit, and an indirect contribution to the tune of an NPV of $4.44 million and an IRR of 30%. The economic benefit from the overall project over its life-cycle was calculated at an NPV of $5.34 million and a modified IRR of 9%. These figures do not take into account the additional employment and profits generated by the enterprise recipients of the long-term funding. The long term effects are expected to be much higher.

Cost Benefit Analysis Summary

Direct IDA contribution

Increase in available term financing directly funded by IDA	**Present Value @ 10%**
Simple Credit facility to PFIs	$15.52
1:1 Credit to PFIs	$17.72
Bridge Financing to PFIs	$1.81
Total Discounted Direct Benefits	**$35.05**
Direct Costs financed by IDA:	
IDA Project Expenses (Disbursed)	$33.48
2% cost of funds on Project Disbursements from IDA	$0.67
Total Discounted Cost for IDA	**$34.15**
Net Financial Cost/Benefit (Present value)	**$0.90**
Internal Rate of Return - Financial analysis (direct benefit)	**6%**

Indirect contribution of the project

Increase in available term financing indirectly created by the project	
Bonds, Debentures and ABS Issued by PFIs	**$26.72**
Total Discounted Indirect Benefits	**$26.72**
Indirect costs financed by other counterparts :	
GOB Discounted Disbursements	$4.97
PFI Discounted Disbursements	$0.01
Service payment to Bond, Debenture and ABS	$12.97
Service payment to credit (simple, 1:1 and Bridge)	$4.34
Total Discounted Indirect Cost	**$22.28**
Net Additional Cost / Benefit (Present value)	**$4.44**
Internal Rate of Return - Additional benefit	**30%**

Overall contribution of the project

Net Economic Cost / Benefit (Present value)	**$5.34**
Internal Rate of Return – overall project[7]	**9%**

Main Assumptions:

1. The NPV calculation is based on the actual project life cycle of 6 years (01/27/2000 to 02/28/2006), with no scrap value at the end of the project;
2. The cost of funds was assumed to stand close to the 5-year interest on bonds, and all flows were discounted at 10%;
3. Actual disbursements under the IDA credit were taken into account to estimate NPV and IRR;
4. Actual cost of credit figures and term financing raised was used in calculations.

Effectively, FIDP injected into the Bangladesh economy scarce long-term funds for investment and private sector growth, which generated 14,218 additional employment, a major part of which were women. Immediate beneficiaries were 147 sub projects that made additional profits of US$55 million during the project period. Also CBSF's contribution to the development of financial market, the capacity building and increased profitability of PFIs, advances in the regulatory framework for bond issuance, intensive regulator and other stakeholder training, and other spill over effects of these activities on the economy has been difficult to quantify and has therefore not formed part of the analysis.

7 Modified IRR used, the simple IRR does not exist for this cash flow pattern.

Annex 6. Bank Lending and Implementation Support/Supervision Processes

(a) Task Team members

Names	Title	Unit	Responsibility/Specialty
Lending			
Shamsuddin Ahmad	Sr. Financial Sector Specialist	SASFP	Team Leader
Imran Farid Darvesh	Finance Assistant	LOAG2	Finance Assistant
Antonio S. Davila-Bonazzi	Portfolio Officer	ACTCF	Loan Accounting Officer
Eilen J. Diamante	Finance Assistant	LOAG2	Finance Assistant
M. Aminul Haque	Consultant	SARPS	Procurement Specialist
Radha Raju	Finance Analyst	LOAG2	Finance Analyst
Chau-Ching Shen	Senior Finance Officer	LOAG2	Finance Officer
Suraiya Zannath	Sr. Financial Management Specialist	SARFM	Financial Management Specialist
Supervision/ICR			
Shamsuddin Ahmad	Sr. Financial Sector Spec.	SASFP	Team Leader
Christopher Juan Costain	Lead Financial Sector Specialist	AFTPS	Financial Sector Specialist
Alfredo J. Dammert	Sr. Private Sector Development	SASFP	PSD Specialist
M. Aminul Haque	Consultant	SARPS	Procurement Specialist
Ziaun Nahar Joya	Program Assistant	SACBD	Program Assistant
Varsha Marathe	Financial Specialist	SASFP	Financial Sector Specialist
Tatiana Nenova	Senior Economist	SASFP	Senior Economist
Shah Nur Quayyum	Junior Professional Associate	SASFP	J. P. A
Bridget Rosalind Rosario	Program Assistant	SACBD	Program Assistant
Sadruddin Muhammad Salman	E T Consultant	SASFP	Research Analyst

(b) Ratings of Project Performance in ISRs

No.	Date ISR Archived	DO	IP	Actual Disbursements (USD M)
1	04/10/2000	Satisfactory	Satisfactory	5.82
2	09/22/2000	Satisfactory	Satisfactory	9.46
3	02/27/2001	Satisfactory	Satisfactory	9.46

4	09/05/2001	Satisfactory	Satisfactory	17.24
5	03/04/2002	Satisfactory	Satisfactory	22.76
6	09/08/2002	Satisfactory	Satisfactory	28.13
7	03/06/2003	Satisfactory	Satisfactory	31.31
8	09/06/2003	Satisfactory	Satisfactory	34.21
9	03/31/2004	Satisfactory	Satisfactory	35.83
10	09/30/2004	Satisfactory	Satisfactory	38.77
11	05/16/2005	Satisfactory	Satisfactory	42.18
12	11/17/2005	Satisfactory	Satisfactory	46.49

(c) Staff Time and Cost

Stage of Project Cycle	Staff Time and Cost (Bank Budget Only)	
	No. of staff weeks	USD Thousands (including travel and consultant costs)
Lending		
FY96		4.47
FY97		1.98
FY98		90.93
FY99		161.13
FY00	15	25.33
FY01		0.00
FY02		0.00
FY03		0.00
FY04		0.00
FY05		0.00
FY06		0.00
FY07		0.00
Total:	**15**	**283.84**
Supervision/ICR		
FY96		313.61
FY97		315.77
FY98		0.00
FY99		0.00
FY00	21	0.72
FY01	26	75.37
FY02	20	61.42
FY03	13	69.14
FY04	24	28.84

FY05	15	46.03
FY06	10	15.46
FY07		9.27
Total:	**129**	**935.63**

Annex 7. Detailed Ratings of Bank and Borrower Performance

Bank	Ratings	Borrower	Ratings
Ensuring Quality at Entry:	Satisfactory	Government:	Moderately Satisfactory
Quality of Supervision:	Satisfactory	Implementing Agency/Agencies:	Satisfactory
Overall Bank Performance:	Satisfactory	**Overall Borrower Performance:**	Moderately Satisfactory

Annex 8. Beneficiary Survey Results (if any)

Not Applicable.

Annex 9. Stakeholder Workshop Report and Results (if any)

Not Applicable.

Annex 10. Summary of Borrower's ICR and/or Comments on Draft ICR

Bangladesh Bank :

1.1 Background of FIDP :

The financial sector of Bangladesh is characterized by strong presence of commercial banks, especially the Nationalized Commercial Banks (NCBs). Most of the available funds go to these NCBs in the form of deposits and channeled for investment through lending. However, the NCBs had a substantial bad loan portfolio. The dominance of banks, with their huge bad loan portfolios and non-transferability of most of the debt/savings instruments are regarded as the prime hindrance in the development of a debt market. Besides, lack of institutions with expertise in debt products, not so high credibility of the corporate borrowers, ever-increasing budget deficit resulting in heavy borrowings from the general public as well as the banking sector through high yielding savings schemes and other sovereign instruments, etc are also discouraging general investors from investing in other financial products. Financial intermediaries do not also feel comfortable in launching new debt products anticipating lack of interest from investors. To strengthen the financial sector of Bangladesh, it appears that the focus should be on the development of the non-bank financial institutions. However, the non-bank financial institutions of Bangladesh suffer from two core problems, namely- mismatch between the maturity of assets and liabilities and the quality of assets.

To support the Financial Institutions (FIs), consisting of eligible non-banks and banks, engaged in medium / long-term lending to private sector enterprises, and to develop the capability of these FIs to raise and mobilize medium/long-term resources from the market, the project named Financial Institutions development Project (FIDP) was launched in 2000.

Bangladesh Bank (BB) acted as an implementing agency of FIDP on behalf of Finance Division, Ministry of Finance, Government of Bangladesh (GoB). FIDP was implemented under Financial Institutions Department (FID) of Bangladesh Bank with support from the Securities and Exchange Commission (SEC) and the Directorate of National Savings (DNS).

1.2 Objective of FIDP :

The objective of the project was to promote the development of non- bank financial institutions (NBFIs) in particular and investment financing, in general, on a sustainable basis contributing to improvements in the quality of intermediation, and the speed and efficiency of industrial growth in Bangladesh. FIDP aimed at broadening and deepening the financial sector, with particular emphasis on the NBF sector, as well as improving the supply of and access to term finance for private investment. This objective was planned to achieve through a combination of mutually reinforcing policy, regulatory, and institutional reforms and provision of investment finance for private sector development.

1.3 Components of FIDP

The project comprised of the following two main components:

a. Resource Mobilization : This component was set to address the external factors that delay or constrain resource mobilization from the financial market aimed at simplifying / streamlining regulations for market traded debt instrument to facilitate bond and security issues, creating an even playing field for the investors between market traded instruments and government saving schemes, and developing market oriented mechanisms, for raising funds by the government through strengthening government treasury bond markets.

b. **Strengthening of Financial Institutions :** This component consisted on creating a Credit, Bridge and Standby Facility (CBSF), a facility within Bangladesh Bank to provide funding to Participating Financial Institutions (PFIs) through a variety of mechanisms that would increase their funding while enabling and encouraging them to mobilize medium to long term resources from the market. That would increase the development of term financing by more efficient and healthy financial system.

1.3.(a) Resource Mobilization Component consisted of several sub-components:

- Development of Issue Rules for Bonds and Debentures
- Implementation of procedures for Market Traded Instruments
- SEC training on Debt Instruments
- Training of BB on Debt Instruments
- Reform of National Saving Schemes
- Development of Procedures for Secondary Treasury Bond (TB) Market

Development of Issue Rules for Bonds and Debentures and Implementation of procedures for market traded Instruments: These two sub-components were merged together and were renamed as "Development and Implementation of issue rules for market traded instruments and regulations to foster secondary debt market". To implement these components consultants were hired. International Science and Technology institute, Inc., USA provided the required consultancy to SEC as per agreement signed with them on 02.06.04. The contract value was US$0.32 million. The consultants completed their task by June 2005.

SEC training on Debt Instruments and BB training on Debt Instruments: The subcomponent "SEC training on debt instrument" aimed to finance travel expenses for SEC staff to learn about security exchange commissions abroad in regulating debt instruments. However, "BB training on debt instrument" component was merged with the BB/ GoB training under development of CBSF.

Reform of National Saving Scheme (NSS): This aimed at reducing distortions that repress potential demand for market traded instruments caused by the GoB's NSS and to be accomplished by bringing benefits of NSS closer to market oriented instruments. Under this sub-component an implementation plan was thought to be executed to facilitate access for small savers including the establishment of a computerized system and an analysis on the impact on GoB's revenues with recommended measures if needed.

Development of procedures for secondary Treasury Bond (TB) Market:

Establishment of a secondary TB market would increase liquidity of TBs thus promoting the development of a government bond market. BB did this task with the assistance from the Reserve bank of India (RBI). Although this subcomponent is not funded from IDA, the project has been benefited from its implementation.

1.3. (b) Strengthening of Financial institutions component consisted of several sub-components.

- Development of CBSF
- Management of CBSF
- Funding of CBSF
- Capacity Enhancement of FIs Business Planning, Resources Management and MIS
- Resource Mobilization for FIs :
- Revision of CBSF Mechanism:

Strengthening of Financial institutions component consisted of creating Credit Bridge and Standby Facility that was hoped to encourage the development of term financing by the more efficient and healthy segment of the financial system. The CBSF was established to provide funding from IDA through a variety of mechanisms that has increased their funding while enabled and encouraged the FIs to mobilize medium to long-term resources from the local market. The eligible FIs obtained fund from the CBSF as a credit line on "first come first serve basis ".

Credit : Credit Line in local currency priced at market rate which was determined time to time. It was disbursed to the PFIs . Credit part was divided into two i.e. Simple credit and One: One credit. Total allocation was US$ 28.00 million.

Bridge Finance: After the maximum amount permitted under the credit line had been reached FIs may require additional financing to accumulate earning assets to sell as Collateralized Loan/Lease Obligations (CLOs). PFIs were provided bridge financing with a maximum period for take-out arrangements.

Standby Support: Under the standby support, it was planned to purchase the bonds/ debentures or CLOs of the PFIs, which were, not sold into the financial market subject to the event that the underwriters were unable to successfully market the bonds/debentures or CLOs. Under FIDP all the PFIs issued bonds/ debentures through private placement. No PFIs approached for standby support and that is why standby support was not necessary. The budget was recollected to one:one credit.

Liquidity Mechanism: The CBSF had also a mechanism to provide liquidity to investors who had purchased CLOs and bonds/debentures. Under a Repurchase Agreement or "Repo" the CBSF would purchase the bonds/Debentures or CLOs at discount below their fare market value, as determined by the CBSF in its own judgment. The CBSF did not assume the credit, market or interest rate risks associated with the FIs CLOs or bond/debentures. The investors holding these instruments continued to carry these risks. The investor must agree to repurchase the instruments within a predetermined period. Due to absence of legal entity CBSF could not enter into any REPO (Repurchase agreement) with the investors. However the re-flow income from FIDP were invested in Treasury bills and REPO/ reverse REPO in the Treasury bond market.

Development of the CBSF : This subcomponent consisted of (i) implementation of the CBSF's organizational structure including role of Government and Facility advisor;(ii) Development and Implementation of accounting and MIS systems (iii) training of GOB/BB staff and (iv) development/implementation of a communication programme for the CBSF.

Management of the CBSF: A CBSF advisor was required to (i) advise and assist BB with the operation of the CBSF (ii) develop details of the operating systems of CBSF (iii) advise FIs on use of the CBSF (iv) manage development of the system as necessary (v) handle documentation for formation of the CLOs of the FIs (vi) implement the availments under the CBSF (vii) recommend modifications of CBSF's policies and procedures (viii) recommend modifications of CBSF's policies and procedures and (ix) submit reports and audits of the CBSF.

Funding of CBSF: Cost of this component was estimated at least at US$ 49.00 m (IDA US$40m, GoB US$5m, and FIs direct contribution to the subprojects US$4m). Initially US$28m and US$ 17m of this fund was allocated for Credit Line and Bridge, Backdrop & Liquidity Mechanism respectively. Later on all the funds were pooled together and declared available for one: one credit upon the recommendation of mid term review mission.

Capacity Enhancement of FIs Business Planning, Resources Management and MIS : Assistance to the eligible FIs in : (i) enhancing their capacity to develop strategic and business plans to enable them to adjust to economic, policy changes and environmental compliance (ii) strengthening their risk and resource management in particular credit assessment and management and asset liability management, and (iii) modernizing support systems in treasury operations, accounting, internal audit, legal and human resources management were aimed.

Resource Mobilization for FIs : Assistance to FIs (including merchant banks) to develop their capacity to mobilize medium to long term resource through issuance of bonds/debentures and CLOs. Assistance will be provided in two steps (i) preparation of internal systems for issuing bonds/debentures and CLOs (ii) advice and close coordination in actual issuance of these instruments were the objectives.

Revision of CBSF Mechanism: Under this component some tasks i.e. preparation of business plan (BP) and financial model for the CBSF, review of the liquidity mechanism and strengthening of FI certification process were planned to be finished. This was dropped in the revised financing plan.

2.0 Implementation

2.1 Establishment and Management of Credit, Bridge and Standby Facility (CBSF):

The Credit, Bridge and Standby Facility (CBSF) was established in Bangladesh Bank through FID Circular No. 07, dated 19 July, 1999 and Vinstar Limited, a New Zealand-based consulting firm was appointed as the FA in December 1999.Facility Management Agreement was signed with Vinstar Ltd. and Bangladesh Bank on 28-12-99 for 5 years. Total Contract value was US$ 2.86 million. Vinstar Ltd. was entitled success fee in addition to this contact amount. Under this contract 2 foreign and 3 local consultants along with 1 office secretary worked from 14 February 2000 to 13 February 2005.

As per terms of reference the facility adviser's role were the following

- The facility adviser developed details of the operating systems of the CBSF.
- They assisted BB and PFIs in carrying out with prudence, diligence and care the operations of the CBSF.
- They also assisted in the coordination of technical assistance (TA) components relating to the development of CBSF internal system and various institutional building programmes for the benefit of FIs.

Initially total allocation for CBSF was US$49.00 m which includes IDA US$.40.00 m, GoB US$.5.00 m and FIs US$.4.00 m (Later IDA reallocated additional US$.2.4 m from TA components for CBSF funding. The GoB's US$5.00 m. was divided into two parts. US$. 3.00 m was for CBSF funding and US$2.00 m was for liquidity mechanism). The PFIs had to finance firstly and then was reimbursed against eligible sub project from CBSF.

Credit and bridge facility under CBSF was introduced but Standby facility and Liquidity mechanism could not be introduced. The Bridge and Standby funds were designed to act as incentive for debt issues by PFIs, in practice they had not been effective in inducing FIs to issue debt instruments. On the other hand, the credit component had been used more actively due to the dearth of long-term sources of funds. Therefore further use of credit funds needed to be linked to the issuance of debt instruments by the PFIs under one: one credit. This is to mention here that under one:one credit facility the PFIs were required to mobilize local resources. For every 1 $ resource mobilization the PFIs got another 1 $ from FIDP through CBSF. Moreover all the funds were reallocated to a pool so that the PFIs could use the credit, bridge and standby facilities as per their needs without being constrained by individual constraints. A total of US$ 45.399 mill. was disbursed to 6 PFIs against 147 subprojects in various sectors, such as readymade garments, food, textiles, transportation, ceramic, power. education, medical, accessories etc. These subprojects generated direct additional employment and additional revenues.

2.2 Resource Mobilization:

Resource mobilization by the PFIs took place through two methods.

1. Non-Securitized Debt Instruments (like- bonds and debentures)

2. Securitized Debt Instruments (like-CLOs, CMOs, etc.).

Under the first method PFIs mobilized domestic resources of Tk. 1408.33 million through issuing plain bond and debentures to different institutional investors i.e private commercial banks, insurance companies etc.

The second method involved the securitization and sale of its assets (credits). Under this method, the PFIs spinned off accumulated quality-earning assets and sell participation on these assets to investors in the form of certificates in a pool of loans or lease contracts called collateralized loan obligation or lease obligations (CLO). The issuance of a securitized instrument could not be done immediately after project launching because of the following

(i) Lack of a legal and institutional infrastructure to support such debt instrument
(ii) High issuance cost
(iii) Lack of sufficient local skills to manage such deals.

Various steps were taken to create enabling environment for Securitization under FIDP. Hong Kong based consulting firm named International Securities Consultancy Limited (ISC) was hired in May 2004 under which two international consultants and one local consultant were engaged. The consultants worked with PFIs , BB, CBSF and relevant market participants and authorities such as potential investors , merchant banks/underwriters, credit rating agencies, Securities & Exchange Commission (SEC), Controller of Insurance, National Board of Revenue to undertake the following tasks

- Provide a working model including full documentation for securitization in light of existing legal tax, accounting and market conditions in Bangladesh.
- Establish the economies of securitization under current market conditions for individual PFIs by modeling the securitization of a pool of selected lease and loan assets from their portfolios. Such economic modeling should account of any market requirements for credit enhancement and of the proposal in the FIDP documentation for a “first loss” approach, of up to 30%, to be born by the PFI originator and of creation of cash reserves for debt servicing. Alternative economic models with different approaches to credit enhancement and debt servicing reserves can also be suggested.
- Provide a roadmap to achieve full best practice securitization by identifying the existing impediments and specifying legal, tax and accounting treatment changes and any other action necessary to remove such impediments and achieve full securitization in Bangladesh;
- Oversee the establishment of securitization infrastructure by PFIs including the establishment of Special Purpose Vehicles, Trusteeships (SPV and securities) Servicing and Asset Management, Custodial and paying agency arrangements and the like; and
- Oversee the preparations by each PFI for public issuance of debt securities in an initial securitization transaction. Such preparations will include obtaining any necessary credit ratings, establishing firm underwriting arrangements and meeting any other SEC requirements; and ideally would involve issuance.

- Report on regulatory best practices for securitization, including the respective roles and responsibilities of the SEC and BB, noting any impediments to best practice arising from the definitions of their role under current legislation. In case of BB, the consultant should suggest prudential supervision guidelines for the undertaking of securitization by both banks and NBFIs
- Provide report aimed at policy markers on the macro-economic benefits of securitization, which can be used by the FIDP to engage and obtain commitment from the governing authorities in Bangladesh to deliver the environmental reforms necessary to permit full securirtization
- Advise PFIs on recommended practice of the public issue of debt secured on the assets of the issuer

The consultants of ISC submitted their final report on May 2005 describing various issues on Securitization. They provided technical support to the PFIs who actively participated in the Securitization process.

To pave the way of securitization in the financial market of Bangladesh, BB recommended to the national Board of revenue (NBR) to take some regulatory measures. NBR accordingly waived Special Purpose Vehicle (SPV), a legal entity engaged in Securitization, from paying income tax, stamp duty and VAT.

In fact FIDP came a long way in creating a facilitating environment for securitization in Bangladesh. Though the first securitized issue was delayed yet at last securitization process came true.

The following steps were taken to create congenial environment for Securitization Process.

1. Special Purpose Vehicle (SPV) a legal entity engaged in Securitization was waived from paying income tax, stamp duty and VAT.
2. Securities And Exchange Commission (SEC) reduced consent fee applicable in case of Securitization .
3. SEC issued Securities and Exchange Commission Rules 2004 on issuance of asset backed security.
4. Interest income up to Tk.25,000/- from investing asset backed security were waived from paying income tax . The rest interest income would be subject to 10% tax. However the National Board of Revenue (NBR) repealed this later.
5. Workshop on "Securitization" was arranged to make awareness about securitization among PFIs.

The above factors as well as technical assistance from FIDP encouraged the PFIs in mobilizing domestic resources through securitization. During the FIDP tennure three PFIs mobilized local resources by issuing zero coupon bond of Tk. 948.58 million under securitization. Two other PFIs were awarded approval from BB for further issuance under securitization. But due to repeal of respective circular regarding tax advantage by the NBR the PFIs were discouraged towards further issuance. A leading micro finance institution was awarded NOC for issuance of securitized debt instruments for US$ 180.00 recently.

2.3 Development and implementation of issue rules for market traded instruments and regulations to foster secondary debt market.

Since inception SEC promulgated many rules and regulations for regulating the capital market in orderly manner but SEC had no clear rules for raising capital through issuance of corporate and municipal bonds. It was required to develop regulations on bonds to pave the way for establishment of primary and secondary bond markets. On the other hand, although Bangladesh Bank, on behalf of the government issues different types of governments bonds regularly, there existed no comprehensive rules for issuing government bonds. So in view of developing rules to create the framework for issuing corporate, municipal and government debt instruments, including Asset Backed Securities (ABS) and securitized issues and trading them in the secondary market International Science and Technology Institute Inc. USA was engaged for the following :

1. Development of rules governing the issuance of corporate, municipal and government fixed income securities, including ABS and securitized issues;
2. Development of rules governing trading of corporate, municipal and government fixed income securities, including ABS and securitized issues in the secondary market
3. Preparation of manuals for;
    a. The investors on how to invest in different types of debt instruments;
    b. The market intermediaries for the diligence mechanism;
    c. The SEC staff on how to process debt issuance applications
    d. Bangladesh Bank staff for issuance of government bonds.
4. Completion of the tasks associated with the implementation of the aforesaid rules at the Commission, Bangladesh Bank, Municipal Authority, Stock Exchanges and any other related organization;
5. Recommendations for introduction of credit derivatives and draft rules for issuance, trading and settlement of these securities;
6. Recommendations for reducing cost of issuance and trading of fixed income securities
7. Imparting training to SEC, Bangladesh Bank, Municipal Authority and Stock Exchange staff and also to issuers and other intermediaries and investors;
8. Suggesting rectification of the deficiencies of existing securities and other laws related to issuance of bonds, and trading of the same in the secondary market;
9. Finding reasons of failure and non performances of debentures issued as part of securities in Bangladesh Capital Market and recommendations for addressing those problems/ shortcomings;
10. Suggesting incentive structure for the market participants
11. Assessing adequacy of the current market infrastructure to support transactions of debt instruments
12. Suggesting settlement procedures for debt securities;
13. Suggesting micro economic issues affecting bond market and remedy to correct distortions if any

14. Arranging study tours for SEC and Bangladesh Bank staff.

The consultants submitted their final report containing the proposed rules, forms and models for adopting by the Securities and Exchange Commission while promulgating respective rules. In respect of implementation, the Ministry of Finance, Bangladesh Bank and Securities and Exchange Commission took the following measures:

- Withholding tax of Govt. Bond was previously 45% then brought down to 20% and in the fiscal year 2005-06 10% upfront at the time of issuance of Govt. Bond.
- A provision was made to start trading of Govt. bonds on the stock exchanges.
- A committee was formed comprising senior officials of BB and SEC and representative from primary dealers.
- A series of meetings held with the stock exchanges, primary dealers and lending dealers concerning trade and reduction of transaction charges; stock exchanges, the central depository company, brokers and dealers agreed to lower their respective fees for trading bonds.
- SEC reduced consent fee and listing fee.
- Bangladesh Bank is examining reducing the number of Govt. bond.
- Credit Rating of bond issue has been mandatory.

2.4 Reform of the National Savings Scheme in Bangladesh

FIDP's one of the main objective was to create congenial environment so that the FIs can mobilize domestic resources through issuing different debt instruments. One of the impediments towards doing that was a high rate offered by different National Savings Scheme (NSS). Though the rates offered by NSS were fair enough to small savers but it was required to revise the national savings scheme to align their returns to those available in the market providing certain concession for small savers.

These were planned to accomplish by aligning government saving schemes to market oriented instruments considering measures such as tax rebates, steepening of yield curves by lowering rates payable prior to maturity, lowering interest rates and making the national savings certificates subject to the ten percent withholding tax applied to interest on bank deposits. In light of the above, one of the components of FIDP is to reform the national savings scheme. For implementation of the said component consultants from International Science and Technology Institute, Inc, USA was hired. The consultants were required to do the following:

- Analyze historic and current performance of the NSS to determine how well it is meeting its objective;
- Identify the impact of the NSS on savings and investment mobilization activities by other borrowers in the market;
- Present selected similar savings schemes and provident funds are referents;
- Evaluate the status of NSS record-keeping and determine future MIS requirements;
- Recommend reforms to and restructuring of the NSS to fully meet its primary objective and ensure its impact on other borrowing activity in the market is

minimized;

- Prepare a comprehensive plan for computerization of the NSS, to include

  (i) Data collection, manipulation and report requirements

  (ii) Recommended operating systems and applications

- Design of the evaluation process for the procurement decision;
- Organize a regional study tour program for IRD, DNS and BB officials to share the international best practice in this area.

The consultants submitted their report recommending various measures including structural and operational reforms of the Directorate of National Savings (DNS) in view of effective market oriented savings schemes. In order to minimize the interest cost to the government as well as to avoid market distortion of the interest rate structure the DNS withdrew three high interest bearing instruments i.e Paribar Sanchaypatra (5 years), Pratirakha sanchay patra and 6 monthly profit bearing sanchay patra (5 years) towards making the debt market more competitive. It was stated in the report of the consultants that the implementation of their recommendations would gradually but progressively transform DNS into an efficient, customer oriented, viable and modern institutions, reduce the cost of borrowing for the government and give an impetus to the development of the capital market. It was hoped that reformed DNS would make a positive contribution to improve the macro economic situation of Bangladesh and to the national effort.

2.5 Success :

- FIDP established Credit, Bridge and Standby Facility (CBSF) and disburse the CBSF fund i.e a total of US$ 45.399 m (equivalent Tk. 263.34 crore) out of US$ 45.4 to the 6 PFIs against 147 subprojects in various sectors, such as readymade garments, food, textiles, transportation, ceramic, health, education, power and accessories. These subprojects generated direct additional employment and additional revenues.
- FIDP utilized about 100% of the IDA credit
- Under the auspicious of FIDP financial market of Bangladesh had been acquainted with the practice of Securitization. Upon receipt of recommendations from Bangladesh Bank the NBR issued different SRO waiving Special Purpose Vehicle (SPV) a legal entity engaged in Securitization from paying income tax, stamp duty and VAT. The SEC reduced consent fee applicable in case of debt issuance and technical support was provided to the PFIs so that they could mobilize domestic resources through securitization . All these measures had a positive impact on the PFIs. Three of the PFIs had come forward to issue asset backed securities. They mobilized Tk. 948.58 million by issuing zero coupon bonds in accordance with securitization process. In addition to that PFIs had mobilized a total of Tk. 1408.33 million through issuing plain bond and debentures to different institutional investors i.e private commercial banks, insurance companies etc.
- PFIs are making repayment as per amortization schedule without any default. The reflow income from FIDP is being used as Liquidity Management Account.

- Scrip less Treasury Bills have been introduced in Bangladesh Bank along with REPO -Reverse REPO mechanism.
- GoB reduced interest rate and number of saving certificates.
- A number of training /study tour along with some workshop have been arranged under FIDP. Officials from MoF, ERD, Planning Commission, SEC and DNS participated in the training programme. Knowledge acquired from the training programme and workshop had contributed FIDP a lot.
- 35 PCs, 35 UPS, 23 Leaser printer, 3 laptop, 8 photocopiers, 2 Fax machines, 2 scanners, 1 Jeep and 1 Car had been procured under FIDP. Bangladesh Bank, Finance Division, SEC and DNS had used all these equipments in implementing the project.

2.6 Constraints

- In spite of having provision of standby facility in the FIDP, it could not be introduced. As all the PFIs issued bonds/debentures through private placement avoiding listing in the stock exchanges they did not feel the necessity of stand by facility. If listing in the stock exchanges were easier as well as deep capital market existed than standby facility could be exercised by the PFIs.
- Hiring of consultants for Development and implementation of issue rules for market traded instruments and regulations to foster secondary debt market and reform of savings scheme were delayed. In case of issue rule's consultants it was delayed due to receiving inadequate expression of interest and consultants for reform of savings scheme was delayed as finalization of TOR was delayed. If these consultants were hired earlier it would be better for implementation of FIDP.
- A number of measures were taken to introduce securitization under FIDP. So, during the FIDP tenure three PFIs mobilized domestic resources by issuing zero coupon bond of Tk. 948.58 million under securitization. Interest income up to Tk.25,000/- from investing asset backed security were waived from paying income tax . The rest interest income was subject to 10% tax. However, the National Board of Revenue (NBR) repealed this later so the enthusiasms regarding issuing securitized bonds could not be sustained.
- As hiring of consultants for reform of savings scheme was delayed procurement of software for reform of savings scheme could not be done finally.

Due to absence of legal entity, CBSF could not enter into any REPO (Repurchase agreement) with the investors.

Comments on Draft ICR:

Urgent/By Special Messenger

Government of the People's Republic of Bangladesh
Ministry of Finance
Economic Relations Division, Dhaka

No: ERD/IDA-5/4/2002/422 Dated: 15 October 2006

Subject: Financial Institutions Development Project IDA # Cr. 3285-BD: Implementation Completion and Results Report.

With reference to your letter of 04 October 2006 on the subject, I am directed to forward herewith the comments of Bangladesh Bank on the report for necessary actions at your end.

Attachment: (As stated)

Sincerely yours,

15/10/2006
(Quzi Munirul Islam)
Senior Assistant Chief
Phone: 8120930

Mr. Shamsuddin Ahmed
Senior Financial Sector Specialist
Private Sector Development and Finance Team
World Bank, BDO
E-32, Agargaon, Sher-e-Bangla Nagar, Dhaka

CC:
Governor, Bangladesh Bank, Motijheel, C/A, Dhaka

Letter IDA-5 2006 (2)

BANGLADESH BANK
(Central Bank of Bangladesh)
Head Office
Motijheel, Dhaka-1000
Bangladesh

Financial Institutions
Department
(Financial Institutions
Development Project)

Ref . FID (P)1052 / 2 /43/2006-

Date: 15/10/2006

Secretary
Economic Relations Division
Ministry of Finance
Peoples' Republic of Bangladesh
Sher-e- Bangla Nagar
Dhaka.

Attn: Mr. Qazi Monirul Islam, Senior Assistant Chief, IDA-5

Dear Sir ,

Financial Institutions Development Project (FIDP), IDA Cr.3285-BD
Implementation Completion and Results Report

Please refer to your letter no.ERD/IDA-5/4/2002/421 dated 09-10-2006 on the captioned subject.

Bangladesh Bank's comment on the draft Implementation Completion and Results Report on the Financial Institutions Development Project (FIDP) is being sent herewith for necessary action at your end.

Encl: As stated

Sincerely Yours,

sd/-

(Md. Abul Quasem)
Executive Director, Bangladesh Bank
&
Project Director
Phone : 7167988

End.No.FID(P)/1052/2/43/2006- 3676 dated : 1[illegible]-10-2006

1. Secretary, Finance Division, Ministry of Finance, Peoples' Republic of Bangladesh Bangladesh Secretariat, Dhaka. (Attn: Mr.Arijit Chowdhury, Senior Assistant Secretary, Banking)
2. Mr. Shamsuddin Ahmed , Senior Financial Sector Specialist, PSD and Finance Team, World Bank Office, Sher-e- Bangla Nagar, Dhaka.

Project Director

Phone: 88-02-7126101-20 Fax : 88-02-9566212, 7114706 www.bangladeshbank.org.bd

Comments on

Draft Implementation Completion Report (ICR) prepared by the World Bank.

FIDP, Bangladesh Bank

Section/para & page reference	**Comments**
Section 1 (Page-1)	Organization's Telephone: 88 0 2 7167988 E mail address: ed7bb@bangla.net Web address: www.bangladeshbank.org.bd
Section 6.3 (Page-8)	"The proposed project is expected to generate the following benefits" may be replaced by- "The *project was expected* to generate the following benefits"
Section 6.5 Extension of Project (Page-9)	It has been stated that IDA reallocated an additional US$ 2.4 million from unused TA subcomponents toward CBSF funding (toward an overall allocation of US$ 47.4 million/IDA portion US$42.40 million). *In fact finally IDA reallocated an additional amount of US$ 2.58 million from unused TA subcomponents toward CBSF funding (toward an overall allocation of US$47.58 million/IDA portion US$.42.58million). [DCA has been amended for the 2nd time on 27 June 2006 in this regard]*
Section 7.2 Lowering NSS rates (2ns para, 3rd line) (Page-14)	Contents of Sl (2) will be replaced by- " hiring of consultants for reform of NSS "
Section 7.2 CBSF management (3rd line) **(Page-15)**	The word "staff" should be stated as "local staff"
Section 7.3 (Page-17, 3rd para, 4th and 5th line)	IPFF= Investment Promotion & Financing Facility
Section 7.5 Transition Arrangement (7th line) (Page-19)	The CBSF was transferred to the FID, BB on ***14 February 2005***
Section 8.2 Impact of the Project, 2nd para 1st line) (Page-22)	It has been stated that the newly raised funding was used by six PFIs to finance the setting up or expansion of 145 subprojects. *In fact up to June 2006 the number of **subprojects** financed under FIDP raised to 147.*
Section 8.2 Impact of the Project, 2nd para,	A total of Tk.957 million (US$ 16.2 million in simple credit was disbursed throughout the life of the project to all six PFIs, which was used for 53 leases and eight loans. In contrast, much more was disbursed to all six

FINANCIAL INSTITUTIONS DEVELOPMENT PROJECT IDA CREDIT NO.3285 BD

Comments on

Draft Implementation Completion Report (ICR) prepared by the World Bank.

FIDP, Bangladesh Bank

<table>
<tr><th>Section/para & page reference</th><th>Comments</th></tr>
<tr><td>1st line)
(Page-22 & 23)</td><td>PFIs in 1:1 credit Tk.1,557 million (US$ 26 million) was used for 61 leases and 11 loans . The bridge financing was used by two PFIs, in the total amount of Tk.119 million (US$.2.1 million) for 12 subleases. The total credit disbursed under the project amounted to US$43.3 million
In fact CBSF funding under FIDP (as on June 30 2006) was as follows:
<table>
<tr><th rowspan="2">Name of the Credit</th><th rowspan="2">Amount in US$ (in million)</th><th rowspan="2">Amount in Tk. (in million)</th><th colspan="2">Number of</th></tr>
<tr><th>Sublease</th><th>Subloan</th></tr>
<tr><td>Simple Credit</td><td>17.26</td><td>957.06</td><td>53</td><td>8</td></tr>
<tr><td>1:1 Credit</td><td>26.23</td><td>1,569.88</td><td>63</td><td>11</td></tr>
<tr><td>Bridge Component</td><td>2.09</td><td>119.12</td><td>12</td><td>0</td></tr>
<tr><td>Total</td><td>45.58</td><td>2,646.06</td><td>128</td><td>19</td></tr>
</table></td></tr>
<tr><td>Section 8.5 Poverty Impacts, Gender Aspects and Social Development (3rd bullet)
(Page-25)</td><td>Number of subprojects was 147.</td></tr>
<tr><td colspan="2">Section 12.1. Borrower/implementing agencies comments (page 34):
<u>BB Comment</u>

As the implementing agency BB had the responsibility to supervise and oversee CBSF activities. To reduce risk BB rechecked all funding applications before disbursement. However this did not hamper smooth disbursement of CBSF funding.
IDA may take necessary initiative with the coordination of GOB for the new avenues as identified and stated in section 7.5 (next Phase: follow up operations)
For better understanding and smooth implementation, communication program may be initiated at the early stage of project implementation, where regulators, beneficiaries, stakeholders, donors and FAPAD may be participated.
</td></tr>
<tr><td>Abbreviations and Acronyms (Page-ii)</td><td>IPFF= Investment Promotion & Financing Facility</td></tr>
</table>

Annex 11. Comments of Cofinanciers and Other Partners/Stakeholders

N.A.

Annex 12. List of Supporting Documents

1. FIDP: Project Appraisal Document (PAD), August 24, 1999
2. FIDP : Project Negotiation Documents
3. FIDP : Development Credit Agreement between GoB and IDA
4. CBSF Reports prepared by Vinstar Limited (April 2000 to February 2005)
5. Asset Securitization by the FIs in Bangladesh, AIMS of Bangladesh Limited, September, 2002
6. Bangladesh Country Assistance Strategy: 2006-2009, The World Bank
7. Developing a Model for Securitization in Bangladesh-International Securities Consultancy Limited(ISC),June 2004 to May 2005
8. Reports on Reform of National Savings Scheme in Bangladesh, by International Science and Technology Institute (June 200 5 to February 2006)
9. Final Drafts of Laws, Rules and Forms of Documents delivered to the SEC for issue of fixed income instruments, by Inter national Science and Technology Institute (Volume I, II, III), dated March 3, 2005
10. Aide Memoires, Mid-Term Review Report, Project Status Reports
11. FIDP: Final Quality at Entry Assessment (QEA3) Report, April 12, 2000
12. Database of sub-projects financed by PFIs
13. Bangladesh - Poverty Reduction Strategy Paper
14. Bangladesh Bank: Eligibility Assessment Reports on PFIs
15. Bangladesh Bank: A Guide to Assessing Eligibility Criteria For FIs, CBSF, FIDP, May 2004
16. Bangladesh Bank: Quarterly Project Management Reports (PMRs)
17. Bangladesh Bank : FIDP ICR, Comments on Draft ICR, Project Database, and Impact Analysis of CBSF