



Internship Report On Book Building Method Of Bangladesh

Submitted To

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Subject: Submission of Internship Report.

Dear Ms,

It is a great pleasure for me to submit the report on “**Book Building Method of Bangladesh**”. I am submitting this report as the part of my internship program.

I have tried my best to gather the complete information available in order to prepare this report. I have prepared this report using the experience that I have gained during my internship. It is true that it could have been done in better way if there were no limitation like time and cost.

I will be highly encouraged if you kindly accept this report. Your kind advice will encourage me to do further research in future.

Thank You

Sincerely Yours

Md. Meshbahul Alam

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Acknowledgement

Generally the success of a research report depends on the contribution of many people. This is why I would like to show deep gratitude to a number of people for their greatness and kind co-operation in writing report. I remain ever grateful to them. I must extend acknowledgement to all those, who helped me by answering queries pertinent to the project related data collection.

I am very grateful to **Ms. Sharmin Shabnam Rahman , Senior Lecturer**, Faculty of BRAC Business School for her kind co-operation and guidance in preparing this report. Her professional and practical experience enriched me to a great extent at the time of preparing this report.

I would like to convey my gratitude to **Hafiz Mohammad Harunur Rashid, Dept. Director, Securities & Exchange commission** for his kind co-operation in every step of fulfilling my report.

I would also like to give thanks to **Mr. Anuar Hossain, librarian of SEC** and **Mr. Rosidul Alam, Assistant Officer of SEC** for their kind co-operation.

This report is not free from limitations. There might still be some minor typing error despite my utmost care. I do apologize for this.

Executive Summary

Practical knowledge is fundamental for the application of theoretical intelligence. Bearing this in mind, I have chosen such kind of topic so that I can get practical knowledge. I gladly acknowledge my indebtedness to the ideas and information providers.

I selected “Book Building Method and its impact on capital market of Bangladesh”. In this report I have given a short review of Securities & Exchange Commission (SEC) and also given an overview of capital market of Bangladesh. But my whole concentration was on the effectiveness of Book Building Method in BD. I have described the Procedures to be followed for determining price under book-building method & advantages-disadvantages of it.

To do this I have analyzed some case studies on selected companies following different flotation methods. After analyzing I got some fruitful findings which are given in this report. I have also proposed some amendments regarding this method.

The main purpose of my report is to show the effectiveness of Book Building Method on stock market. To fulfill my objective I have used some methodologies by which I collected data for the report. Information has been collected from primary sources and secondary sources. After gathering data I analyzed and made adjustment of data for attaining the purpose.

While preparing the report I found the following things:

- ❖ Book-building pricing method introduced into Bangladesh’s market has not reduced price manipulation as expected; on the other hand, it has significantly increased possibly due to other external effects.
- ❖ Increase the pricing capabilities of institutional investors to some extent.
- ❖ SEC & the relevant authorities should come forward to implement the best IPO pricing method specially the BBM to gain the confidence of investors.

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Chapter One

Introduction

1.1. Origin of the Report

As a part of my MBA Program I have completed my internship at Securities and Exchange Commission (SEC). I have been working there for three (3) months as an internship student from 07th October 2012 to 07th January 2013. I have made my internship report on Book Building Method which is considered as a new tool for issuing capital in the capital market of the country like Bangladesh. For this purpose, I have used some useful methodologies.

1.2 Objectives

- a. Broad objective- To find out the effectiveness of Book Building Method in Bangladesh.
- b. Specific objectives-
 - To find out the present scenario of Securities and Exchange Commission.
 - To show the overview of capital market of Bangladesh.
 - Build awareness of sustainable capital market among the investors.

1.3. Methodology

I have prepared this report with the data collected from various sources which are primary sources and secondary sources.

Primary sources

- ❖ Conversation with DSE and SEC professional
- ❖ From Workshop arranged by SEC
- ❖ Consultation with supervisor teacher
- ❖ Group discussion (classmates)
- ❖ Conversation with DSE investors

Secondary sources

- ❖ Journals and relevant books
- ❖ Bangladesh govt. budget 2012-13 materials
- ❖ Various Bengali and English newspapers
- ❖ Various capital market related websites
- ❖ DSE index analysis

1.4. Scope

As there are many scopes to study on Book Building Method in Bangladesh, e.g., contribution of SEC in the overall economic condition, current market affairs regarding rapid fall of share price etc., but in this study I will try to find out only the the rationality of introducing Book Building Method for issuing capital in the capital market of Bangladesh.

1.5 Limitations

- ❖ This is a descriptive and analysis based report. So, it needs sufficient time.
- ❖ Need sufficient fund to carry out the study.
- ❖ Data unavailability
- ❖ Accessibility

Chapter Two

Overview of Securities and Exchange Commission (SEC)

2.1 History of SEC

- ❖ SEC was established on 8 June, 1993 under the Securities and Exchange Commission Act, 1993.
- ❖ The Chairman and Members of the Commission are appointed by the government and have overall responsibility to administer securities legislation.
- ❖ The Commission, at present has three full time members, excluding the Chairman.
- ❖ The Commission is a statutory body and attached to the Ministry of Finance.

2.2 Mission of SEC

- ❖ To protect the interest of the investors
- ❖ To develop and maintain fair, transparent and efficient securities markets,
- ❖ To ensure proper issuance of securities and compliance with securities laws.

2.3 Establishment of the Commission

- ❖ After the commencement of SEC act, government established a commission by the name of SEC for the carrying out the purpose of the act.
- ❖ The commission is a corporate body and have perpetual succession.
- ❖ SEC has a common seal and power to hold and shall transfer property both movable and immovable.
- ❖ SEC shall sue and be sued by its name.
- ❖ The head office address is: 15th, 16th & 20th floor, Jiban Bima Tower, 10, Dilkusha Commercial Area, Dhaka-1000. If needed the SEC may establish branch office at any place of the country with the approval of the government.

2.4 Composition of the Commission

- ❖ The commission consists of a chairman and four members.
- ❖ They are appointed by the government. But there is a provision that one eligible and experienced non-government person must be appointed for the member of the commission.
- ❖ The chairman and the members are the full time employee.
- ❖ They shall be the experts in matters of companies and security market, in law, economics, keeping of accounts and also other matters which are necessary for the commission.
- ❖ The chairman is the chief executive of the commission.
- ❖ They are appointed for three years and shall be eligible for reappointment for only one further such period.
- ❖ No person who has completed sixty five years shall be eligible for the post of chairman or member of the commission.
- ❖ The chairman and the members may resign the office before the expiry of the term but they have to pay an advance notice to the government before three months.
- ❖ But a provision is that until the government has accepted the resignation, the chairman and the members continue their respective works.
- ❖ There are 60 officers in the commission.

2.5 Functions of the Commission

- ❖ Regulating the business of the Stock Exchanges or any other securities market.
- ❖ Registering and regulating the business of stock-brokers, sub-brokers, share transfer agents, merchant bankers and managers of issues, trustee of trust deeds, registrar of an issue, underwriters, portfolio managers, investment advisers and other intermediaries in the securities market.
- ❖ Registering, monitoring and regulating of collective investment scheme including all forms of mutual funds.
- ❖ Monitoring and regulating all authorized self regulatory organizations in the securities market.
- ❖ Regulating the business of the Stock Exchanges or any other securities market.
- ❖ Registering and regulating the business of stock-brokers, sub-brokers, share transfer agents, merchant bankers and managers of issues, trustee of trust deeds, registrar of an issue, underwriters, portfolio managers, investment advisers and other intermediaries in the securities market.
- ❖ Registering, monitoring and regulating of collective investment scheme including all forms of mutual funds.
- ❖ Monitoring and regulating all authorized self regulatory organizations in the securities market.

2.6 Annual Budget Statement

The Commission every year, within such period as the Government may direct, submit to the Government an annual budget statement for the following financial year showing the amount of money which may be required from the Government for the said financial year.

2.7 Accounts and Audit

- ❖ The Commission maintains its accounts properly and prepares annual statements of accounts.
- ❖ The Controller and Auditor-General of Bangladesh, hereto after referred to as the Auditor-General, shall every year audit the accounts of the Commission and shall send a copy of the audit report to the Government and the Commission and the Government shall provide for its presentation at the national assembly.
- ❖ For the purpose of an audit under sub-section (2), the Auditor-General or any person authorized by him shall have access to all records, documents, cash and money deposited with banks, securities, stores and other property of the Commission and may examine any member, officer and employee of the Commission.
- ❖ The Government may, if necessary, call for reports and statements from the Commission on any matter of the Commission and the Commission shall be bound to supply such reports and statements.
- ❖ The Commission shall, within sixty days after completion of every financial year, submit to the Government a report together with the account-books on its activities during the preceding financial year and the Government shall, as fast as possible, provide for its presentation at the national assembly.

2.8 Power of the Government to Give Directions

The Government may give the Commission any direction for carrying out the purposes of this Act and the Commission shall be bound to comply with such directions.

2.9 Delegation of Power

The Commission may, subject to well-defined conditions, delegate to the Chairman, any other member or any officer any of its powers or responsibilities except the power to make rules.

- ❖ This means that the officers, chairman or members are powerful just like the SEC. There are now well defined areas or department with well defined responsibility and power in SEC. For example...

Departments	
Department	Power And Responsibility
Chairman's office	Conduct and coordination of commission's meeting.
Administration & Finance	Logistics, finance & accounting
Capital Issue	The issuance of securities IPO & Other than PO
Capital Market Regulatory Reforms & Compliance	Amendment of securities laws & suggest reforms of the market and provide clarifications
CDS	Supervise the activities of CDBL etc.
Corporate Finance	Supervises and monitors the listed companies in light of the securities laws.
Enforcement	Takes legal measures.
Legal Department	Assists lawyers engaged by the commission.
MIS	Automation, development of capital market monitoring system and information systems.
Research & Development	Investor education, organizing & reporting.

2.10 Punishment

Whoever contravenes or intends to contravene or aids and abets to contravene any provision of SEC Act shall be punishable with a term of rigorous imprisonment not exceeding five years or a fine of at least five lac Takas or both.

Under this act if any person fails to:

- ❖ Comply with any order or direction

- ❖ Furnish any required information; or
- ❖ Provide require facility during the investigation process

Then, commission may

- ❖ Give him a chance of hearing a warning in writing through an authorised representative. or
- ❖ A fine of at least one lakh taka and
- ❖ In case of continuing failure, a further sum calculated at the rate of ten thousand taka per day delayed.

Chapter Three

Daily Activities of different Departments of Securities & Exchange Commission (SEC)

3.1 Research and Development:

Research and Development Department of the Commission conducts investors' education program for the general investors, impart capital market related seminar for various government and non-government organizations, prepares and publishes Commission's various publications regularly, furnishes various reports and information to the government and other institutions including Ministry of Finance and different regulatory authorities, and makes paper clipping from most of the daily newspapers (20 dailies) and circulate it to the Commission and executives. The department also deals the training program of the authorized representatives jointly with the stock exchanges.

Research and Development Department has carried out regular activities as mentioned in the table below:

- Training Program for General Investors (Two-days program)
- Training for Authorized Representatives (Two-days program)
- Quarterly Report
- Monthly Work Plan to MOF

3.2 Corporate Finance:

The Corporate Finance Department (CFD) supervises and monitors the listed companies after issuance of primary shares in light with the securities laws and accounting standards. CFD examines appointment of the auditor by the issuer company as per securities laws and compliance of the matters concerning corporate governance guidelines including examination of the audited annual financial statements and un-audited half yearly financial statements, ensures the proper utilization of capital raised through initial public offering (IPO), ensures discipline in financial activities as well as in corporate governance among the issuer companies listed in stock exchanges as part of its supervision.

3.3 Mutual Fund and Special Purpose Vehicle (MF & SPV):

Mutual Fund and SPV Department has performed the following duties and responsibilities:

- Completed the process for approval of lottery of NCCBL Mutual Fund One (Closed-end).
- Also completed the process of approval for deployment of fund of NCCBL Mutual Fund One (Close-end).

3.4 Surveillance:

MIS Department is responsible for assisting different departments of SEC through development of automation in their activities, development of capital market monitoring system based on computerized data analysis, informing all about securities laws and other related matters through website and thus enabling the Commission with modern information technology capacity. At present all officers of SEC use computers in their daily activities. All

computers are connected through local area network (LAN). Different modules of integrated Securities and Exchange Commission Automated System (SECAS) have been developed at SEC for different department's use. Officers of SEC can use broadband internet connection from their workstation through connected LAN. SEC's website (www.secbd.org) is enriched with various information like securities laws, IPO prospectus, eligible securities, depository participants, enforcement actions, annual and quarterly reports, investors information etc, which are updated regularly and many users visit the website.

3.4 Supervision and Regulation of Markets and Issuer Companies :

SRMI Department of the SEC supervises activities of stock exchanges, over the counter (OTC) markets and issuer companies in accordance with the securities laws. Besides, the department also resolves complaints received against issuer companies under the securities laws. The functions of SRMIC are enumerated below:

- Monitoring the declaration of sale/purchase/transfer of securities by the sponsor /director of the listed companies.
- Monitoring the position of monthly shareholding of sponsors/directors.
- Monitoring disclosure of price sensitive information of listed companies.
- Approval of transfer of share of listed companies outside the stock exchanges.
- Monitoring all activities of stock exchanges (except securities transactions).
- Taking effective measures to resolve complaints related to capital market.

3.5 Capital Issue:

Capital Issue Department of the Commission accords consent to issue equity and debt securities through initial public offering and capital raising including approval of all type of securities issues. Public and private limited companies are required to obtain consent of the Commission for raising capital whose capital exceeds Taka 10 million and 100 million respectively. This Department also approves the offer of right shares, direct listing of securities on the exchanges and issuance of asset-backed securities.

3.5 Registration:

All market intermediaries associated with capital market are required to be licensed by the SEC in order to ensure the proper functioning of the capital market. Licensing of intermediaries help the Commission to discharge its oversight functions more effectively.

3.6 Capital Market Regulatory Reforms and Compliance (CMRRC):

CMRRC Department makes drafts and issues securities related rules/regulations for the development of the capital market, amends those rules/regulations as and when necessary and conducts activities related to capital market reforms.

3.7 Supervision and Regulation of Intermediaries (SRI):

The functions of SRI Department are supervising and regulating the activities of stock-dealers/stock brokers, depository participants, security custodian banks, merchant bankers, security lenders and borrowers and other market intermediaries. This department conducts the regular inspection of stock brokers/dealers, DP's and Merchant Banks on monthly basis and also conducts special inspection as and when required. The SRI department also deals with the complaints lodged by the general investors and other stakeholders.

3.8 Enforcement:

Under the Securities laws, the Enforcement Dept takes legal measures including imposition of penalty against those who break /violate securities laws in consideration of the nature of offences they commit. Prior to taking measures it follows due process that includes carrying out inspection and enquiry. On the basis of violations of securities laws detected during the inspection/enquiry process, explanations are sought from the concerned issuer and person or institution alleged and then hearing is conducted as per the concerned securities laws and thereafter a report is submitted before the Commission. The Commission takes necessary legal action as per securities laws.

3.9 Law:

Total 395 cases filed by or against SEC are pending in different courts. Name of the courts are given below along with number of pending cases: Supreme Court of Bangladesh 164, Special Judge Court and Paribesh Appeal Adalat, Dhaka 01, Additional District Judge 3rd Court Dhaka 01, Metropolitan Sessions Judge Court, Dhaka. 01, Additional Metropolitan Sessions Judge 1st Court, Dhaka. 02, Additional Metropolitan Sessions Judge 5th Court, Dhaka. 01, Joint Sessions Judge 1st Court, Dhaka 01, Metropolitan Sessions Judge 1st Asst. Court, Dhaka 01.

3.10 Management Information Systems (MIS):

MIS Department is responsible to assist different departments of SEC through development of automation in their activities, development of capital market monitoring system based on computerized data analysis, and informing all about securities laws and other related matters through website. At present all officers of SEC use computers in their daily activities. All computers are connected through local area network (LAN). Different modules of integrated Securities and Exchange Commission Automated System (SECAS) have been developed at SEC for use of its different departments. Officers of SEC can use broadband internet connection from their workstation through connected LAN. SEC's website (www.secbd.org) is enriched with various information like press release, securities laws, IPO prospectus, eligible securities, depository participants, enforcement actions, reports etc. which are updated regularly and many users visit the website. MIS department works on development, modification and maintenance of the mentioned systems.

Chapter Four

Articles Review

4.1 Capital Market of Bangladesh: Volatility in the Dhaka Stock Exchange (DSE) and Role of Regulators

Md. Tariqur Rahman (Corresponding author)
Senior Research Associate, Centre for Policy Dialogue (CPD)

Khondker Golam Moazzem
Senior Research Fellow, Centre for Policy Dialogue (CPD)

International Journal of Business and Management Vol. 6, No. 7; July 2011
Published by Canadian Center of Science and Education.

This journal mainly focuses on identifying the volatility of the share prices of DSE and the role of SEC in the capital market. Authors discuss many things about the volatility of the share prices and rules and regulations, and the role of SEC. They also suggest some steps that should be taken by SEC, in order to smooth the DSE's operation.

Authors point out few reasons about the volatility of DSE, which is narrated below:

- The lack of efficient regulation over the securities market and business is viewed as a major reason which is hindering the healthy development of the securities market.
- The volatility of the securities market is also associated with governance problems of the market.
- The speculative nature of the market can be a serious barrier to capital formation, and efficient functioning of the financial markets.
- Trend analysis on the volatile nature of DSE, we have found that over time the market is becoming more volatile which has been captured by the major indices of the market.
- The causal relationship between decisions taken by the regulatory authority and market volatility is statistically highly significant and the SEC increases volatility.

Role of SEC in Capital Market:

- The decisions should be as much as predictable with providing adequate explanation for the investors.
- Making relevant information available, this requires transparency and accountability of audit firms.
- Building a stable market through tapping the growing interest of general people in the market by increasing supply of shares.
- Spread of capital market educational program in order to protect the interest of new investor's minimum level of knowledge on capital market.

4.2 Current Status of the Corporate Governance in Bangladesh: A Critical evaluation with legal aspect

Md. Gulam Sharoar Hossain, A.K.M. Zahirul Islam

Bangladesh Research Publication Journal. 2009

ISSN: 98-03, Vol-3, Issue-2, Pg-971-981

This study examines the state of corporate governance (CG) in Bangladesh. Since the early 1990s, CG has been receiving increasing attention from regulatory bodies and practitioners worldwide. Corporate sectors are still in its initial stage; nevertheless awareness of the importance of CG is growing. Bangladesh has a liberal policy towards foreign direct investment (FDI). However, when compared to those of the India, Sri Lanka, Pakistan, Thailand and Malaysia, CG in practice and philosophy have up till now remained relatively under - developed in Bangladesh. Further, there appears to be a lack of either market or structural governance mechanisms to discipline errant managers. To govern the corporate environment in Bangladesh, Major guidelines are as follows

- Securities and Exchange Ordinance 1969
- Bangladesh Bank Order 1972
- Bank Companies Act 1991
- Financial Institutions Act 1993
- Securities and Exchange Commission Act 1993
- Companies Act 1994
- Bankruptcy Act 1997

In case of institutionalize the practice of CG in Bangladesh, first initiative was undertaken by the Securities and Exchange Commission (SEC). SEC issued a notification on Corporate Governance Guidelines (CG Guidelines) for the publicly listed companies of Bangladesh under the power vested on the Commission by Section 2CC of the Securities and Exchange Ordinance, 1969. The CG Guidelines were issued on a 'comply or explain' basis, providing some 'breathing space' for the companies to implement on the basis of their capabilities. However the overall frame work for investor protection and CG has a number of important weaknesses that have hindered the capital market development. Most of the companies depend on the banks as their major source of financing. Capital market in Bangladesh is still at an emerging stage with market capitalization amounting to only 6.5% of GDP with low investor confidence on corporate governance and financial disclosure practices in many companies listed in the stock exchanges.

CG practices in Bangladesh are gradually being introduced in most companies and organizations. 66.7 percent of the companies have adopted CG and 43.3 percent have compliance policy with national or international benchmarks. A considerable percentage of the top management does not fully understand the concept of CG. However, Bangladesh has lagged behind the global economy in CG. One reason for this slow progress in adopting CG is that most companies are family oriented. Such concentrated ownership structures affects the effectiveness of corporate governance mechanisms, which weaknesses cannot be rectified by laws and regulations. Motivation to disclose information and improve governance practices by companies is also felt negatively. There is neither any value judgment nor any consequences for CG practices. The current system in Bangladesh does not provide sufficient legal, institutional and economic motivation for stakeholders to encourage and enforce CG practices.

4.3 Corporate Governance of Mutual Fund In Bangladesh

Mohammad Nayeem Abdullah and Kamruddin Parvez
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Mutual Fund is a professionally managed collective investment scheme that pools money from many investors and invests typically in securities (stocks, bonds, short term money market instruments, other mutual funds and other securities) on behalf of the investors/unit holders and distributes the profits. Investment in share capital is becoming more risky business due to affecting of lots of factors but mutual fund is less risky than stock. So, all the big corporations and financial institutions allow public to invest the money in their mutual funds. Investment Corporation of Bangladesh (ICB) launched by government in 1980 was the first ever Mutual Funds for the sake of investors and of the capital market. The first private sector to take initiative of organizing a mutual fund was Asset & Investment Management Services of Bangladesh Limited (AIMS) in 1999. Now the total no of mutual fund in Bangladesh are 36, including thirty two are of Open- Ended Mutual and four are of close ended. SEC (Securities and Exchange Commission) prescribed a structure to be followed by the financial institutions and mutual funds alike.

In case of mutual funds it's applicable that they will invest in these shares and it's important that there is good corporate governance to make sure

- Streamlining the Guidelines with the Code of Corporate Governance
- Protection of depositors
- Improvements in prudential regulation

There might be varieties of mutual funds that differ in terms of their investment objectives, underlying portfolios of shares, risks and returns, fees and expenses, etc. Mutual funds are professionally managed investment schemes that collect funds from small investors and invest in stocks, bonds, short term money market instruments, and other securities. This ensures a diversified portfolio for the investors at much less efforts than through purchasing individual stocks and bonds. There are two types of mutual funds open ended and close ended. Generally, mutual funds are organized under the law as companies or business trusts and managed by separate entities. Merchant banks & portfolio manager are licensed to operate under SEC (Merchant Banker & Portfolio Manager Rules) 1996.

Mutual funds have four-tiered structure

- Sponsors
- Trustees
- AMC's (Asset Management Companies)
- Custodian

According to rules, all asset backed securitizations and mutual funds must have an accredited trusty and security custodian. For that purpose, SEC has licensed 8 institutions as Trustees and 8 institutions as custodians. All mutual funds are required to be registered with the SEC before they launch any scheme.

SEC plays a major role in controlling regulations of mutual funds

1. A minimum size of the board and its factions is set by the SEC regulations.
2. For better governance, guidelines should be fairly followed by each company to expose their financial operations. The statement should have:
 - IAS followed in preparation of the financial statements
 - Disclosure on company's ability as a growing concern and if not so then the fact along with the reasons there of,
 - Explanation on the significant deviation from last year in operating results, if so happened
 - Summarize of at least last three years key operating and financial data
 - Significant plans and decisions along with future prospects and risks
 - Number of Board Meetings held during the year and attendance by directors,
 - Aggregate number of shares held by: Parent/Subsidiary/Associate companies, Directors, CEO, Company Secretary, CFO, Head of Internal Audit. etc
3. The numbers of auditors are very limited and this might be a source of risk to the investors.

Chapter Five

Overview of the Capital Market

5.1 Introduction

Capital market is absolutely a vital consider for the proper functioning of capitalistic economy, since they serve the channel funds from savers to borrowers. The securities market allows sound listed companies to raise additional capital quickly and cheaply, as they enjoy reputation. A vibrant and liquid securities market encourages increase in savings by offering attractive and rewarding securities in terms of higher return, lower risk and easy option for conversion to cash. Capital markets Include Primary Market, where new securities are sold & Secondary Market, where existing securities are traded. Primary Markets involve investment bankers, who specialize in selling new securities. Secondary Markets consist of equity markets, bond markets and derivative markets.

It is encouraging to see that the capital market of Bangladesh is growing, though at a slower pace and still at an emerging stage. The market has faced a lot of developments since the inception of Securities and Exchange Commission (SEC) in 1993. After the bubble and burst of 1996, capital market has attracted a lot more attention, importance and awareness that have led to whatever infrastructure we have in the market today. This flow of experience for market further improved the awareness and knowledge level of investors as well as issuers.

5.2 Structure of Capital Market Of Bangladesh

The capital market of Bangladesh can be divided into securities segments & non-securities segment. Securities segment in turn may be divided into the markets for primary issues and the markets for secondary trading.

5.2.1 Non- Securities Segment:

The non-securities segment of the capital market provides long term loans both in local & foreign currencies. This segment also covers merchant banking. The following are the players in this field:

(I) DEVELOPMENT FINANCE INSTITUTIONS: The major Development Finance Institutions (DFIs) are Bangladesh Development Bank, and House Building Finance Corporation (HBFC). The primary source of capital of these DFIs is the government. The DFIs are owned and managed by the government. The DFIs provide long term loans both in local and foreign currencies with 8-12 years repayment period with a grace period of 2-5 years.

(II) COMMERCIAL & SPECIALIZED BANKS: The nationalized and private commercial banks and other specialized banks like Bangladesh Krishi Bank (BKB) and Bank for Small Industries and Commerce (BASIC) have been engaged in providing long-term loans to the agro-based and industrial enterprises and small scale industries. The major sources of funds

of these institutions have been their resources including equity capital, deposits and borrowing from government.

5.2.2 Securities Segment:

The securities segments are concerned with the process a firm distribute its securities to the public in the primary market & the securities are then traded in the secondary markets. The principal instruments are stocks, preference shares, debentures, bonds, treasury bonds etc. the following are the major players in the securities segments of Bangladesh:

(I) STOCK EXCHANGES: There are two stock exchanges in Bangladesh, namely, the Dhaka Stock Exchange (DSE) & Chittagong Stock Exchange (CSE). DSE is the first bourse of the country established in 1954. Bangladesh government approved the CSE as the second bourse of the country on 12 February, 1995, to accelerate industrial growth for overall benefit of the economy. The CSE was incorporated as the Public Limited Company on 1 April, 1995.

(II) INVESTMENT CORPORATION OF BANGLADESH (ICB): ICB underwrites issue of securities and provides bridging loan, maintains investment accounts and floats & manages closed-end and open-end Mutual Fund and closed-end Unit funds to ensure the supply of securities as well as generate demand for securities. ICB also operates on the DSE and CSE as dealers.

5.3 Salient Features of The Capital Market

The salient features of capital market are discussed below:

- ❖ **LOW FOREIGN INVESTMENT:** The role of Foreign Direct Investment (FDI) and Foreign Portfolio Investment (FPI) in the development of capital market of Bangladesh is undeniable. However the share market crash of late 1996 had particularly distanced foreign investors.
- ❖ **LOW LIQUIDITY LEVEL:** The stock market in BANGLADESH is characterized by a thin market having small market capitalization ratio & low level of liquidity. If a big investor takes any attempt at selling a relatively large quantity, this will cause a large decrease in prices, i.e. an erosion of capital value, hence contributing to illiquidity. It is observed that trading on some stocks takes place once a month or even some longer intervals.
- ❖ **LACK OF INVESTORS' AWARENESS:** A major portion of our educated population is yet to be attracted to the stock market. They need to be persuaded, informed and trained. An investment culture needs to be developed in our country.
- ❖ **INFORMATION ASYMMETRY:** The access to the information remains a major problem in the market. While a handful of institutional investors may enjoy certain benefits since they have an investment unit manned with qualified officers, nothing exists for retail investors. And, in the absence of independent research houses, retail investors primarily

focus on advices given by their brokers, and rumors. This is frightening and it often leads to enormous losses for small investors who are vital for a low-income and pre-emerging market like Bangladesh.

- ❖ **INSIGNIFICANT INVESTMENT FROM INSTITUTIONAL INVESTORS:** An estimate suggests that the ratio of institutional-to-retail investors is between 20-25%. This is considered low for a developing market like ours. Institutional investors bring long-term commitment hence stability in the market. The presence of institutional investors also ensures better level of valuation due to their specialized skills.
- ❖ **WEAK CORPORATE GOVERNANCE:** The level of corporate governance of international standard is lacking. Inadequate disclosure requirement and culture of family-owned conglomerates deter the expansion of corporate governance into the local industry.
- ❖ **OTHER CHARACTERISTICS:** the other remarkable features of BANGLADESH stock markets are laid down as follows:
 - ✓ Existence of only dealer-broker member (no specialist/ market maker)
 - ✓ Inefficient capital market operational & informational
 - ✓ Lack of proper or adequate disclosures of information
 - ✓ Certifiers of capital statements & property values of the company are the same identical
 - ✓ Lack of enforcement with the compliance of rules and regulation.

Bangladesh Capital Market Summary
As on 30 June, 2012

Indicators	Dhaka Stock Exchange	Chittagong Stock Exchange
No. of companies	232	200
No. of mutual funds	35	35
No. of debentures	8	3
No. of treasury bonds	212	-
No. of corporate bonds	3	-
Total No. of Listed Securities	490	238

5.4 Budget 2011-2012 Highlights Related To The Capital Market

The Hon'ble Finance Minister in his speech discussed on the capital market in details. His speech covered the following aspects related to the capital market as highlighted below:

1) The Government has taken various steps to implement the recommendations made recently:

a) A Training institute on Capital Market named Bangladesh Institute of Capital Market (BICM) has been established to promote good governance among the investors, intermediaries and companies.

b) In order to separate the ownership, management and trading of stock-exchange and to contain manipulation in the capital market, the process of demutualization in Dhaka and Chittagong Stock Exchanges has begun.

c) To regain investors' confidence in the capital market, contain continuous price fall, maintain stability and bring about strategic development, a Tk 5000 crore open end mutual fund known as Bangladesh Fund has been established. The Govt. will remain vigilant about the utilization of the fund and future negative impact on fiscal sector.

2) In order to contain irregularities in the capital market the following steps have been taken which are highly appreciable:

- i. To develop surveillance software in the Securities and Exchange Commission (SEC).
- ii. An initiative has taken to frame Financial Reporting Act to maintain stability in the capital market.
- iii. The Government is considering a plan to establish a Financial Reporting Council to oversee the audit and accounting standards and their transparency.
- iv. Other than this they have taken up the task of amending the SEC Act, different rules and Companies Act.
- v. SEC also took initiative to amend Security and Exchange Commission (Public Issue) Rules, 2006 to avoid the misuse of book building method in the capital market.
- vi. The Govt. has also taken steps to establish a separate Clearing and Settlement Company to settle stock exchange transactions within the shortest possible time.
- vii. Within the next financial year, the Govt. shall establish an oversight mechanism to see whether the conditions like margin lending and collateral requirement are met.
- viii. The Govt. shall make the regulatory structure of share market transparent according to international system.

3) The government is determined to ensure growth and stability of capital market. For this reason the Finance Minister has proposed which are also highly appreciable:

- a) To continue the existing tax exemption benefits on capital gain to investors even if their income is above the threshold limit.
- b) Those investors will not be required to produce TIN.
- c) That to make the government bond market popular, investment in Bangladesh Infrastructure Finance Fund Limited (BIFFL) or Treasury Bond be accepted without any question subject to payment of tax at the rate of 10 percent. DSE strongly proposes to extend these facilities for the listed securities with the

New Inclusions in the proposed budget

1. Collection of tax from Member of Stock Exchanges: Increases from 0.05% to 0.1%.
2. Special Tax treatment in respect of investment in the purchase of Bangladesh Government Treasury Bond at 10% without any questions being asked regarding source of fund.

Chapter Six

Book Building Method

6.1 What is Book Building Method?

Book-Building Method, scientific process of discovering prices of shares, is introduced in our country's Capital Market. Book building is a process of price discovery for security that is intended to be issued through public offering. Company that intends to issue share sets number of shares to be sold and suggest a price range. Initial price band is fixed on basis of past performance, expected future earning of the issuer and the P/E ratio of the other peer group companies of that industry. When the issuer company goes for the road show, it gets the first hand views of the investors about the issue which plays an important role in deciding the floor price or price band. Usually institutional investor/ syndicate members bid electronically by auction deadline, saying how many shares they would buy for how much. Investment banker and company executives assemble bids until they reach number of share to be sold. Shares are issued at bid price of individual investor or weighted average at cut off or cut off price. Issuer may issue share below cut off price with the approval of the Regulator.

6.2 Why Book Building Method?

There are some fundamental weaknesses in existing fixed pricing method. These weaknesses are compelling the relevant parties to introduce a new pricing system which would create benefits for all parties (investor along with the issuer). The first and most common flaw of existing fixed pricing method to all over the world is that it is, almost in each case, underpriced. As we know companies issue IPO to raise capital from the primary market, but they cannot earn fair price through fixed pricing method, as it is most often under pricing the offer price as reflected in the post IPO in the securities. In addition there are other flaws of fixed pricing method, which are:

- Existing fixed pricing method cannot catch the demand of the market, resulting oversubscription which create aims match between the demand and supply of market. In fact fixed price offering are priced without first soliciting investor demand, with price discovery mainly taking place in the aftermarket.
- If there is an oversubscription, allocation is done in prorata basis in fixed pricing method and underwriter does not have any control over allocation.
- In fixed pricing method money is blocked for a certain period, which create liquidity crisis in the market.
- The ownership depends on the winning of the lottery. No one can become an owner of share in existing fixed pricing method if investor does not win the lottery.

Under the fixed pricing method, IPO does not attract the investors due to-

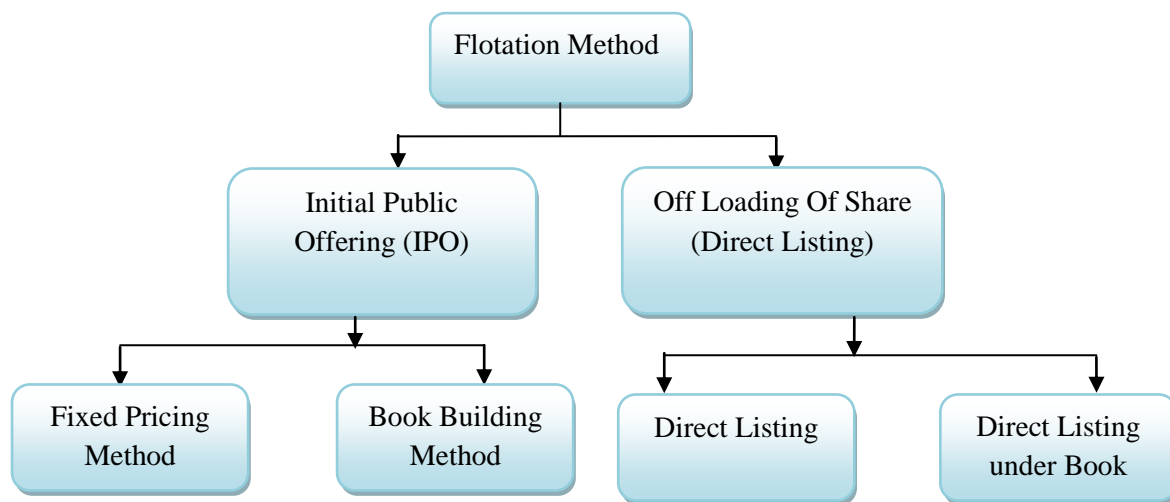
- The inherent weakness of the system, leading companies having good and authentically strong fundamental cannot set appropriate price for their issues.
- It seals the way of attracting more fund in near future.
- In the prevailing system, retail investors gain more than entrepreneurs (sponsors) of well performing companies.

In fact stock market is not reaping much benefit under the existing disclosure based distribution system-

- As most of the shareholders who are allotted with primary shares dispose off the same immediately, generally in the first three days. The stock market cannot be developed in such a way where millions of small traders remained glued for applying in the primary shares of new issues.
- It does not help to build depth and maturities of securities market.

So, due to the above flaws of fixed pricing method concepts of book building Method has emerged.

6.3 Types of Flotation Methods



There are two ways of floating share:

1. Initial Public Offering (IPO) Flotation Method
2. Off-loading of Shares (Direct Listing)

6.3.1 Initial Public Offering (IPO) Flotation Method

IPO is an acronym for Initial Public Offering which is the first sale of stock by a private company to the public. IPOs are often issued by smaller, younger companies seeking the capital to expand, but can also be done by large privately owned companies looking to become publicly traded. In an IPO, the issuer obtains the assistance of an underwriting firm, which helps it determine what type of security to issue (common or preferred), the best offering price and the time to bring it to market. IPOs are also referred to as "public offering" because the general public becomes the partial owner of the company after buying the shares through IPO.

This Initial Public Offering can be made through the fixed price method, book building method or a combination of both.

- a) Single Stage Method (Fixed Price Method):
- b) Two Stage Method (Book Building) Method:

(a) Fixed price method:

Fixed price issues are issues in which the issuer is allowed to price the shares as he wishes. The basis for the price is explained in an offer document through qualitative and quantitative statements. This offer document is filed with the stock exchanges and the registrar of companies. Fixed pricing do not provide the comfort to the big companies in regard to actual price discovery of their particular issue and they feel shy to go public for inadequate pricing of their securities. This feeling lead many companies looking at other avenues for raising funds instead of equity market.

- It is the process of selling shares at a single fixed price.
- In this method, the company, or 'issuer', values the company and prices the share at a pre-determined price.
- Basically it determines price to offer an IPO based on corporate fundamentals

Example: IPO Process under Fixed Pricing Method

Marico Bangladesh Ltd. (MBL), a wholly owned subsidiary of Marico Limited India, was incorporated in the year 1999 as a private limited company. It converted to a public limited company on 21st September 2008. It offered 40 million ordinary shares at tk. 10 each with a premium of 80 per share. So their offer price of share is fixed at Tk. 10.

(b) Book-building method:

Book-building is a process of price discovery used in public offers. The issuer sets a base price and a band within which the investor is allowed to bid for shares. The investor had to bid for a quantity of shares he wished to subscribe to within this band. The upper price of the band can be a maximum of 1.2 times the floor price. Every public offer through the book-building process has a book running lead manager (BRLM), a merchant banker, who manages the issue.

- Book-Building Method, scientific process of discovering prices of shares, is introduced in the country's Capital Market
- It is a process by which an underwriter attempts to determine at what price to offer an IPO based on demand from institutional investors.

Example: IPO Process under Book Building Method

RAK Ceramics Bangladesh Limited is the First Company who has used for IPO in Book Building System. Their public offering was 30 lac ordinary shares of Tk. 10 face value and indicative price was Tk. 40. The cut off price was determined as Tk.48 with the price band of 20% up and down of indicative price.

6.3.2 Off-loading of Shares (Direct Listing)

Direct listing means listing of a company by directly offering the securities to the public through a stock exchange. In case of direct listing the shares are traded on the secondary market from the beginning and there is no primary market of the securities. Direct Listing Method helps owners to divest their shares to the general public for making their issue listed in the bourse to obtain its genuine market value.

- a) Direct Listing:
- b) Direct Listing under Book Building

6.4 Differences between Fixed Pricing Method and Book Building Method

Differences between fixed pricing mechanisms with book-building method are shown below:

Features	Fixed Price process	Book Building process
Pricing	Price at which the securities are offered/allotted is known in advance to the investor.	Price at which securities will be offered/allotted is not known in advance to the investor. Only an indicative price range is known.
Demand	Demand for the securities offered is known only after the closure of the issue.	Demand for the securities offered can be known everyday as the book is built.
Payment	Payment if made at the time of subscription wherein refund is given after allocation.	Payment only after allocation.

6.5 Approval of SEC for Book Building

The stock market regulator approved the 'book building,' method a widely practiced price fixing mechanism for initial public offering (IPO). Capital market experts showed it as an encouragement for private-sector entrepreneurs to list their companies on bourses at fair prices. However the existing IPO system will remain intact. BBM is expected to enhance market depth, turnover and the supply side. Many big and profitable companies keep them

aloof from listing on bourses, as they feared to be denied proper prices of their shares under the existing IPO process. After initiating this method, such companies will be interested to enter the market for capital rising, as this method will ensure a fair price of their shares. Book building is the process by which a price will be determined by institutional investors on the basis of an indicative price the issuer company offers. It was believed that the introduction of book building in Bangladesh capital market will facilitate inclusion of large and profitable corporate houses in the market. There are some preconditions that a company will have to fulfill first to float shares under the book building method.

6.6 Eligible Institutional investors for participating in price discovery system

The institutions which can participate in the price discovery system under the book building are:

- ❖ merchant banks (excluding the issue manager of the issuer company),
- ❖ foreign institutional investors registered with or approved by the SEC,
- ❖ recognized pension and provident fund,
- ❖ banks and financial institutions,
- ❖ insurance companies,
- ❖ institutional venture capital registered with or authorized by the SEC,
- ❖ Stock dealers and any institution authorized by the SEC.

Share prices of an intending issuer company will be discovered and fixed for both institutional and general investors through various measures.

Eligibility of an issuer for book-building method

An issuer may determine issue price of its security being offered following book-building method (i.e. price discovery process) subject to compliance with the following:

- (I) Must have at least Tk. 30 crore net-worth;
- (II) Shall offer at least 10% shares of paid up capital (including intended offer) or Tk. 30 crore at face value, whichever is higher;
- (III) Shall be in commercial operation for at least immediate last three years;
- (IV) Shall have profit in two years out of the immediate last three completed financial year;
- (V) shall have no accumulated loss at the time of application;
- (VI) shall be regular in holding annual general meeting;
- (VII) shall audit at least its latest financial statements by a firm of CA from the panel of auditors of Commission;
- (VIII) Shall appoint separate person as issue manager and registrar to the issue for managing the offer
- (IX) Shall comply with all requirements of these Rules in preparing prospectus.

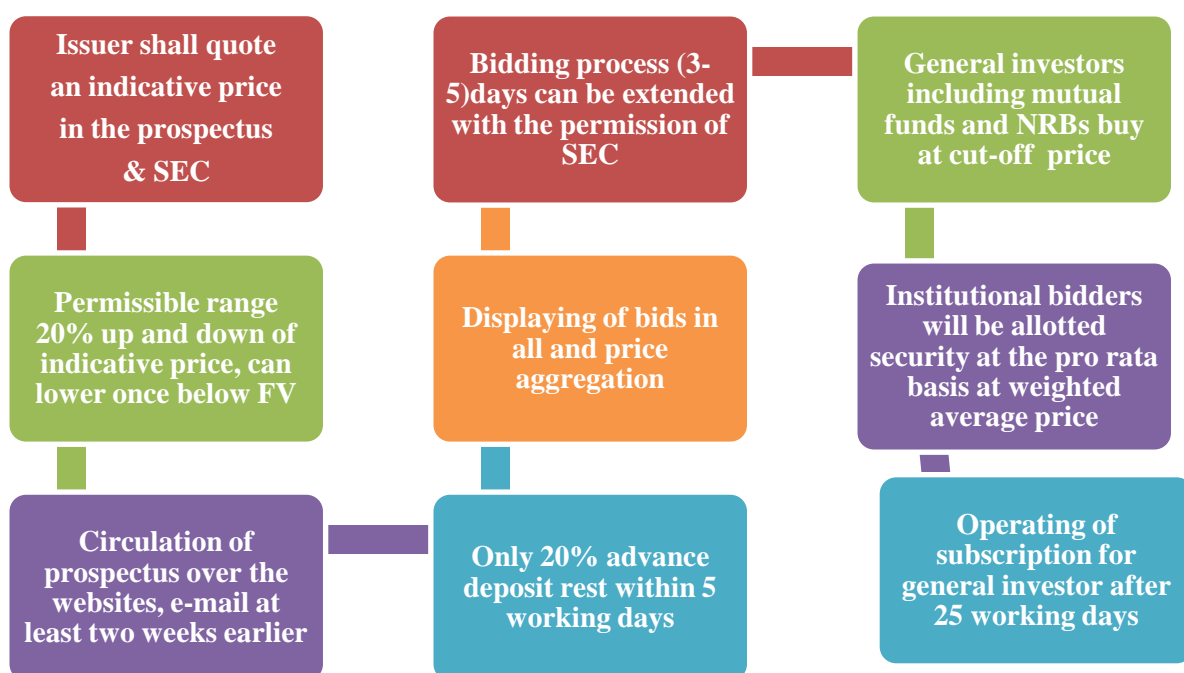
The Commission, if it deems appropriate for the interest of investor or development of capital market, may exempt or relax any of the above prerequisites.

6.7 Price discovery for determining indicative price

The price discovery process for determining indicative price of security will involve the following institutional investors registered with or approved by the Commission in this regard:

- (a) Merchant bankers excepting the issue manager concerned to the proposed issue;
- (b) Foreign institutional investors registered with or approved by the Commission;
- (c) Recognized pension funds and provident funds;
- (d) Bank and non-bank financial institutions under regulatory control of Bangladesh Bank;
- (e) Insurance companies regulated under Insurance Act, 1938 (Act No. IV of 1938);
- (f) Institutional venture capital and institutional investors registered with or approved by the Commission;
- (g) Stock Dealer registered with the Commission; and
- (h) Any other artificial juridical person permitted by the Commission for this purpose

Procedures to be followed for determining price under book-building method



- ❖ Issuer shall invite for indicative price offer from the eligible institutional investors through proper disclosure, presentation, document, seminar, road show, etc;
- ❖ Issuer in association with issue manager and eligible institutional investors shall quote an indicative price in the prospectus and submit the same to the Commission with copy to the stock exchanges;
- ❖ Such indicative price range shall be determined as per price indications obtained from at least five eligible institutional investors covering at least three different categories of such investors;
- ❖ Rationale for the indicative price must be included in the prospectus the issuer is required to disclose in detail about the qualitative and quantitative factors justifying the indicative price;

- ❖ The indicative price shall be the basis for formal price building with an upward and downward band of 20% (twenty percent) of indicative price within which eligible institutional investors shall bid for the allocated amount of security;
- ❖ Eligible institutional investors bidding shall commence after getting consent from the Commission for this purpose;
- ❖ If institutional quota is not cleared at 20% (twenty percent) below indicative price, the issue will be considered cancelled unless the floor price is further lowered within the face value of security : Provided that, the issuer's chance to lower the price shall not be more than once;
- ❖ Prospectus will have to be posted on the Websites of the Commission, stock exchanges, issue manager and issuer at least two weeks prior to the start of the bidding to facilitate investors to know about the company and all aspect of offering ;
- ❖ No institutional investor shall be allowed to quote for more than 10% (ten percent) of the total security offered for sale, subject to maximum of 5 (five) bids ;
- ❖ Institutional bidding period will be 3 to 5 (three to five) working days which may be changed with the approval of the Commission ;
- ❖ The bidding will be handled through a uniform and integrated automated system of the stock exchanges, or any other organization as decided by the Commission, especially developed for book building method ;
- ❖ The volume and value of bid at different prices will be displayed on the monitor of the said system without identifying the bidder ;
- ❖ The institutional bidders will be allotted security on pro-rata basis at the weighted average price of the bids that would clear the total number of securities being issued to them;
- ❖ Institutional bidders shall deposit their bid with 20% (twenty percent) of the amount of bid in advance to the designated bank account and the rest amount to settle the dues against security to be issued to them shall be deposited within 5 (five) working days prior to the date of opening subscription for general investors ;
- ❖ In case of failure to deposit remaining amount that is required to be paid by institutional bidders for full settlement of the security to be issued in their favor, 50% (fifty percent) of bid money deposited by them shall be forfeited by the Commission. The securities earmarked for the bidder who defaulted in making payment shall be added to the general investor quota.
- ❖ General investors, which include mutual funds and NRBs, shall buy at the cut-off price;
- ❖ There shall be a time gap of 25 (twenty five) working days or as may be determined by the Commission between closure of bidding by eligible institutional investors and subscription opening for general investors ;
- ❖ Subscription for general investors shall remain open for the period as specified by the Commission;
- ❖ General investors shall place their application through banker to the issue; and
- ❖ All application money shall be kept in a separate escrow account opened with a designated bank with prior intimation to the Commission. Issuer will not be allowed to utilize such money until all the process of issue is completed and Commissions consent to this effect is obtained.

6.8 Distribution mechanism for the issuance of security

Book Building System will deal with only institutional investor's distribution/allocation at this stage and the percentage of securities' quota for institutional investor will be according to following schedule.

Size of Total issue (in TK.)	Eligible institutional Investors' Quota	General Investors' Quota		
		Mutual Fund Portion	NRB Portion	Public Portion
30 to 50 crore	20%	10%	10%	60% or balance amount
Over 50 crore to 100 crore	30%	10%	10%	50% or balance amount
Over 100 crore to 500 crore	40%	10%	10%	40% or balance amount
Over 500 crore	50%	10%	10%	30% or balance amount

There shall be lock-in of 15 trading days from the first trading day on the security issued to the eligible institutional investors.

6.8.1 Lock-in period

There shall be lock-in of 15 (fifteen) trading days from the first trading day on the security issued to the eligible institutional investors.

6.8.2 Fee of issue manager and registrar to the issue

Fee of issue manager and registrar to the issue could be on negotiated basis but not exceeding 5% (five percent) in total of the issue size.

6.9 Advantages of Book Building Method

Introduction of book building is a big step towards developing Bangladesh capital markets. Book Building is basically a capital issuance process used in Initial Public Offer (IPO) which aids price and demand discovery.

- Book building reduces risk of undervaluation for issuers
- Ensures fair pricing by factoring in demand, likely to encourage listing of large, well-reputed companies

- It enables small and riskier companies to access equity markets as compared to auction method
- It provides early investors with liquidity
- It encourages underwriters to provide important after market services.
- For large issuer book building is less expensive.
- It enables issuer to raise large amounts of capital.
- SEC qualifying conditions for book-building set certain criteria for companies to be eligible

6.10 Criticism on Book Building Method

Book building method is not out of drawbacks. The first problem associate with this mechanism is that it gives underwriter discretion in setting the offer price and allocating shares to investors. In addition there are other disadvantages of book building method:

- Book building method favors institutional investors
- It is a mechanism of giving special favor to exclusive favor at the expenses of everyone else
- For general investor book building method is expensive
- In the IPOs through the Book-Building route, it would be difficult to find dubious issues of the kind that put off investors.
- In fact book building method reduces under pricing is somewhat controversial.

6.11 Probable Impact of Book Building Method on Bangladeshi Capital Market

Positive Impacts

- ❖ Good issuers would be encouraged to raise fund from capital market;
- ❖ Difference between issue price and first day trading price will be narrowed down.
- ❖ There will be a balance between the demand for and supply of the security since book-built price will be close to the market price.

Probable Negative Impacts

- ❖ Institutional Investors may tend to bid higher price disregarding fundamentals of the company in bullish market and lower price in the bearish market.
- ❖ Retail investors may be disinclined to buy security at higher price of the issue.
- ❖ Shares may be issued at price which is more than the real value of underlying assets.

Chapter Seven

Effectiveness of book building method in Capital Market of Bangladesh

7.1 Effectiveness of book building method in Capital Market

Book building method has come into the market in order to ensure fair pricing of a stock to prospective large local and foreign profitable firms enlisting in the stock exchanges. It enhances the depth of local market, and allows the local investors to be the part of large business entities and to strengthen corporate governance. The method was expected to make, disclose and report to public by more transparent and credible way and to accelerate industrialization. It may be used as a mechanism to raise money from capital market by inflating the stock price even before start of trading on the same in the stock exchanges .

Basically Book building is a rational way price discovery by which an issuer attempts to determine the price to offer its security, based on demand from institutional investors. It is a market mechanism-based initial public offering (IPO) pricing method where market demand for a security is identified first to set a fair price of that security.

In Bangladesh, a large difference is observed between the offer price and closing price on the first day of trading of an IPO under the fixed pricing method and Securities and Exchange Commission (SEC) has the exclusive right to justify the offer price of a stock, intended for going public with no mechanism in place to assess its market demand. Book building came into existence with appreciation from to all players and participants in our capital market. Today it has ironically become the reason to blame itself. There's arises the Questions whether the book building method itself is faulty or it is getting misused. In case of being faulty, why it has been used successfully in both developed and developing countries. In reality capital market must be allowed to operate on its mechanism where like any other market.

Recently, a few companies got green signal from the SEC to go public under the book building method and a number of companies have completed their road shows where price of the proposed issue has been determined using methods like price earnings multiple, market value multiples, price to book value multiple of the similar companies, expected earnings per share (EPS), and so forth. In the price earning multiple, the issuer company takes P/E ratios of the similar listed stocks in the related sector etc., and then multiply it with the issuer company's latest audited EPS, or weighted average EPS to determine the price. Strong allegations are there that there is a prior understanding among the issuer company and the institutional investors participating in the road shows. The situation is further worsened when formal bidding is arranged with such inflated indicative price where it is observed that all the bidders offers at upper band (+20% of indicative price) although lower band (-20% of indicative price) is allowed.

Perhaps only 15 days lock-in period provides incentives to bid for such higher prices. In a recent study carried out by the CPD, it was observed that out of three companies going to public under the book building method, the prices of the two company's shares fall significantly below the offer price and a handsome amount of money was taken out of the market. book building method already have faced strong criticism though a good numbers of large and profitable companies are in pipeline to go public under this method.

although the book building mechanism in Bangladesh capital market has not yielded the expected success yet the market is not likely to move in the way other international ones do,

without with sufficient success with book building systems by undertaking some measures such as:

- ❖ Forcing issuer company to be conservative in using methods like P/E multiples,
- ❖ Looking primarily on its inherent ability to generate future cash flows in offering indicative pricing,
- ❖ Increasing lock-in period to discourage higher bidding by the institutional investors and devising specific and consistent pricing mechanism to be used by all companies intending to go public.

7.2 Companies Followed BBM in Bangladesh

Some important companies which are listed under the Book Building Method in Bangladesh are as follows:

7.2.1 RAK Ceramics: First Company under book-building method

RAK Ceramics, a Bangladesh-UAE joint venture, has started process under book-building method to hit the country's stock market. It is the first company, which made debut on Dhaka Stock Exchange (DSE) and Chittagong Stock Exchange (CSE), using such modern pricing mechanism for initial public offering (IPO) introduced in March of last year. As part of the process, the tiles and sanitary-ware maker held an IPO road show to woo the eligible institutional investors in a city hotel Saturday. RAK received primary approval for floating shares from the securities regulator in December Within next three weeks; it began to sell shares among the institutional investors after receiving SEC consent's on bidding. Institutional bidding was executed by DSE and CSE. Subscription for general investors opened 25 days from the closure of the institutional bidding. IDLC Finance was the lead issue manager of the RAK Ceramic IPO, while BRAC-EPL Investments Ltd was the joint issue manager. RAK offers 34.51 million equity shares worth Tk 10 each in face value under the book-building method. Of which, 20 per cent was funded by eligible institutional investors, 10 per cent by mutual funds, 10 per cent by non-resident Bangladeshis and 60 per cent by public. An indicative price for each RAK share had already been built at Tk 40, including a premium of Tk 30, through bidding by seven institutions from four sectors. According to the book building method, bidders cannot quote 20 percent more or less than the indicative price, meaning they had to offer between Tk 32 and Tk 48 for each share. Fixing the indicative price is required to obtain regulatory approval. As of December 31, 2009, RAK's pre-IPO paid-up capital was Tk 1.86 billion. The company's net asset value was Tk 13.69 a share and earnings per share (EPS) was Tk 1.83.

7.2.2 Khulna Power

Khulna Power Company Limited (KPCL), the country's first independent power producer in private sector. The company sold more than 52.15 million shares to the general investors and its opening price was Tk 194.25, which was determined by the institutional investors in line with book building method. The institutional investors participated in bidding for KPCL shares from April 4-6. The face value of each share was Tk 10 and market lot 100 shares. Its earnings per share were Tk 2.79 and net asset value Tk 18.53 as of December 2009.

7.2.3 Mobil Jamuna Bangladesh Limited

Mobil Jamuna Bangladesh Limited came to the capital market under the book building method and raised Tk 508 crore. The company floated 40 million shares with a face value of Tk 10. Indicative price per share was Tk 127, which means that the investors would bid for the share and the lowest price among the bidders would be fixed as the IPO price. According to the financial statement of 2009, against each share with face value of Tk 10, the MJBL had income of Tk 2.45 and asset worth Tk 11.70. The company had paid-up capital of Tk 140 crore and Prime Finance worked as the issue manager for MJBL. Market regulator had also Okayed issuance of right shares for Exim Bank and Agni Systems Limited.

7.2.4 MI Cement IPO

MI Cement Factory Ltd that makes Crown brand cement raised Tk 334 crore floating three crore ordinary shares of Tk 10 each using the book-building method. The cut-off price for each share had been fixed at Tk 111.60, meaning an individual had to apply with Tk 11,160 for a market lot of 100 shares. With the funds raised, the cement maker will expand its business. The EPS of MI Cement as of 2009 was Tk 16 and NAV per stock was Tk 15.78. MI Cement is the sixth cement maker in the stock market.

Chapter Eight

Case Study Analysis

8.1 Marico Bangladesh Limited

(IPO Process under Fixed Method)

Brief Overview of the Company

1. Date of Incorporation : 6th September, 1999
2. Year of Commencement of Business : 2000 (30th January 2000)
3. Authorized Capital : Total Tk. 400.00 million (40.00mn ordinary Shares of Tk. 10 each)
4. Paid up Capital (Pre IPO) : Total Tk. 283.50 million

Details of the Issue

Description	Ordinary Shares	Face Value per share	Offer Value In Taka	Premium per share (Tk.)	Premium in Taka	Capital in Taka
Pre-IPO	28,350,000	10	10	–	–	283,500,000
Public Offering	1,492,100	10	90	80	119,368,000	14,921,000

Paid up Capital after IPO

Particulars	No. of Ordinary Shares	Face Value (Tk.)	Capital in Taka
Pre-IPO Paid up capital	28,350,000	10	283,500,000
IPO	1,492,100	10	14,921,000
Paid up capital after IPO	29,842,100	10	298,421,000

Offer Price Determination of MBL

MBL has ISSUED 1,492,100 ordinary shares at a price of Tk. 90 per share with face value of Tk. 10 and premium of Tk. 80 totaling Tk. 134,289,000. Face value of the issue is Tk. 14,921,000. The Offer Price of MBL is set through averaging the Net Asset Value (NAV) per share and the other values derived under different valuation methods (Weighted Average Historical EPS, Projected EPS, and Average Market Price of Similar Stocks).

8.2 Grameenphone Limited

(IPO Process under Book Building Method)

Brief Overview of the Company

1. Date of Incorporation : October 10, 1996 converted into public ltd. co. On June 25, 2007
2. Commencement of Business : March 26, 1996
3. Authorized Capital : Tk. 40,000 million
4. Paid up Capital : Tk. 12,151.75 million

Determination of Offering Price

The Book Value per share has been determined as follows:

(Tk. in millions)

Shareholders' Equity	31-03-2008
<i>Paid up Capital</i>	12,152
<i>Share premium</i>	14
Retained Earnings	9,051
Capital Reserve	14
Deposit from shareholders	2
General reserve	2,140
Total Shareholders' equity	23,372
Total Number of Shares	12,152
Book value per Share of BDT 1 each	1.92

Offer Price Determination

Grameenphone has issued 69,439,400 ordinary shares at taka 10.00 each at an issue price of taka 70.00 per share, including a premium of taka 60.00 per share. The public offering price of Grameen Phone has been determined by applying a discount to the median enterprise value ("Enterprise Value") to EBITDA for the last twelve months ("LTM EBITDA") ratio of comparable listed mobile telecommunications operators in Asia (excluding Japan) and then calculating a resulting market capitalization and value per share of their shares.

By applying EBITDA multiple they have calculated price per share in the public offering Tk. 7.00 (before par value change) and Tk.70.00 (after par value change). Whereas price per share in the placement Tk. 7.00 (before par value change) and Tk. 74.00 after par value change.

8.3 R A K Ceramics (Bangladesh) Limited

(IPO under Book Building method)

Brief Overview of the Company

Date of Incorporation	: 26 November 1998
Commencement of Business	: 12 November 2000
Authorized Capital	: Tk.3000.00 million
Indicative price	: Tk. 40

Details of the Issue

Description	Ordinary Shares	Face Value per share	Offer Value In Taka	Premium Amount	Amount
Pre-IPO Paid up-capital	185,563,500	10	-	-	1,855,635,000
Public Offering	30,000,000	10	40	9,00,000,000	300,000,000

Paid up Capital after IPO

Particulars	No. of Ordinary Shares	Face Value (Tk.)	Capital in Taka
Pre-IPO Paid up capital	185,563,500	10	1,855,635,000
IPO	30,000,000	10	300,000,000
Paid up capital after IPO	215,563,500	10	2,155,635,000

8.4 IPO process under Book Building Method

8.4.1 Features of IPO

RAK Ceramics Bangladesh Limited is the First Company who has applied for IPO in Book Building System. Book Building is a process through which an issuer attempts to determine the price to offer its security based on demand from institutional investors. Under the process, the price of an IPO share will be determined through an automated bidding to be participated by different financial institutions and then the share will be opened for the IPO participant at the cut-off price determined during the book building process. The bidding will be handled through a uniform and integrated automated system of the stock exchanges, or any other organization as decided by the Commission, especially developed for book building method.

They have taken a general approach of valuation, primarily from institutional investor's viewpoint in determining the acceptable price.

They have also concluded that relative valuation would be the most suitable approach for determining RAK price. For determination of an appropriate primary valuation method for a company, it requires profound knowledge on several factors including economic climate, the stages of development of the company, the position of the company in the market, industry life cycle, nature of production, production cycle, the situation of the stock market and the prospect of the sector in which the company operates.

8.4.2 Determination of Indicative Fair Price

The offer price of RAK is derived under different applicable valuation methods. Finally, the fair value of RAK share is derived by calculating the weighted average price of the fair values derived under different valuation techniques. Since, RAK has appeared to be a capital-intensive company, highest weight is assigned to the price derived through Primary Valuation Method and equal weights are assigned to the prices derived through other valuation technique.

Particulars	Values (Tk.)	Assigned wt.	Weighted Value (Tk.)
Price Based on Average P/BV Multiple of Similar Stocks	48.02	0.650	31.21
Price Based on Average P/E Multiple of Similar Stocks	22.88	0.175	4.00
Price Based on DDM	38.6	0.175	6.76
Price (Fair Value)			41.97

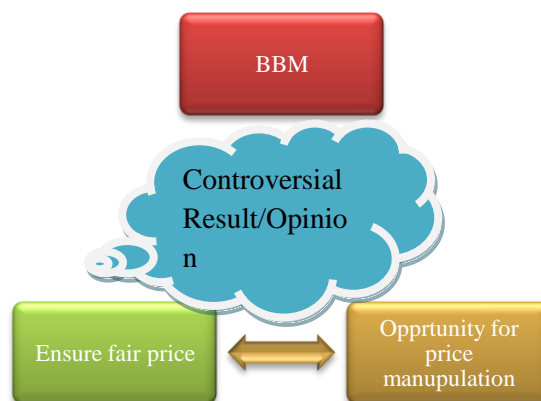
8.4.3 Consent of the Eligible institutional Investors regarding indicative price

7 (Seven) Institutional Investors have consented to the proposed indicative price of Tk. 40 each, including a premium of Tk. 30 per share. The following table illustrates the list of Eligible Institutional Investors (EIIs) consenting to the indicative price:

Name	Category
Prime Bank Limited	Bank & Merchant Banker
Southeast Bank Limited	Bank & Merchant Banker
IFIC Bank Limited	Bank
Prime Finance & Investment Limited	FI & Merchant Banker
LankaBangla Finance Limited	FI & Merchant Banker
Mercantile Insurance Limited	Insurance Company
Royal Green Securities Limited	Stock Dealer

8.5 Analysis on the Price Effect of Bangladesh's Book-building

Our concern is impact of BBM on share price. Two view points:



Now let us take a short view on the following news to identify what has happened in Bangladesh:

DSE seeks probe into book building 'scam'

Says it won't allow overpriced cost to get listed

FE Report

The Dhaka Stock Exchange (DSE) won't allow overpriced companies to get listed on the premier bourse and has demanded a probe into firms which manipulated the Book Building method to jack up their share prices.

So what have happened on the BBM in Bangladesh? To get the answer of this question let look news:

Book building: a recipe for disaster

Daily Star-08.10.12 Monday

The book-building method has turned out to be a tool for manipulating market prices in Bangladesh, although it is a widely practiced price fixing mechanism for initial public offering.

Analysts say the companies that have been listed under the book-building system should be reviewed to find out how the distortion of price took place by deceiving retail investors. Book building was introduced in Bangladesh in 2009. But a number of companies, which are in the pipeline to be enlisted in the market under the system, might cause a huge flight of capital.

An analysis found that those who hold the private placements take out a substantial amount of money by selling shares at high prices during the first one month.

- ✚ In one case, share prices of KPCL fell by 33 percent within one month and 50 percent in the next two months and did not rise thereafter.
- ✚ A share of the power company traded at only Tk 90.8 yesterday, but it reached its peak of Tk 341 during the initial days of trading.
- ✚ The total capital flight during the first 15 days from the transaction of the KPCL shares was estimated at Tk 83.7 crore.
- ✚ In another company, the total flight of capital was Tk 64.8 crore only in the first two days of trade.
- ✚ Jamuna Mobil's price was set at Tk 152 against a book value of Tk 12 only and MI Cement at Tk 120 against its book value of Tk 10.
- ✚ "Jamuna Mobil took five years to make it Tk 12 from Tk 10. So, the investors will take how many years to get return on his investment at the highly artificial price nobody knows.

The artificial price is being maintained for some time, particularly till the lifting of the lock-in period (15 days), and after that the investors offload their shares at higher prices.

“We don't oppose the book-building system, but we want a monitoring into the system,” said Debapriya Bhattacharya, CPD's distinguished fellow.

“Inherently, book building is a good system. But if there was any manipulation, that should be investigated,” said former finance adviser, AB Mirza Azizul Islam

Therefore BBM is not out of question that it always ensures fair price of companies' shares in the market. In our inefficient capital market the BBM has been misused hence share price manipulation has created disaster in the market as well as general investors have got a negative impression regarding BBM.

An Example of Book Building Method (BBM) & its Impact on Share Price

Dhaka Stock Exchange Ltd.

Company Name: **RAK CERAMICS (BANGLADESH) LIMITED**

Market Info:
 Last Trade: **104.70** (circled in red) Close Price: 105.2
 Last Update: **Jun 9, 2011** Day's Range: 104.1 - 107.2

Basic Information:
 Authorized Cap(mn tk.): 3000.00
 Face value: 10.00

Profit Status :
 Current Price Earning Ratio (P/E): 35.54
 Current Price Earning Ratio (P/E): 41.25

Financial Performance:

Year	Basic EPS	NAV Per Share	Net Profit (mn tk.)
2000	n/a	n/a	n/a
2005	0.46	18.48	86.28
2009	1.83	13.69	
2010	2.81	21.34	606.52

Other Information of the Company:
 Listing Year(Book Building): 2010

- This simple example of RAK Ceramics is enough to show the impact of Book Building Method (BBM) on share price.
- RAK started with Tk 10 each in face value under the book-building method in March, 2010.
- An indicative price for each RAK share was built at Tk 40 through bidding by seven institutions from four sectors.
- In the price discovery phase, bidders cannot quote 20 percent more or less than the indicative price, meaning they offered between Tk 32 and Tk 48 for each share.
- The Offer Price per Share was Tk.48.00 (Cut-off Price).
- EPS (as per prospectus) Tk. 10.99 as on 30.06.2009, Half-yearly (against face value of Tk. 100).
- NAV per Share (as per Prospectus) Tk. 12.62 (as on 30.06.2009).

Source: DSE Web

8.6 Thoughts on Recent Stock Market Crash in Bangladesh and BBM

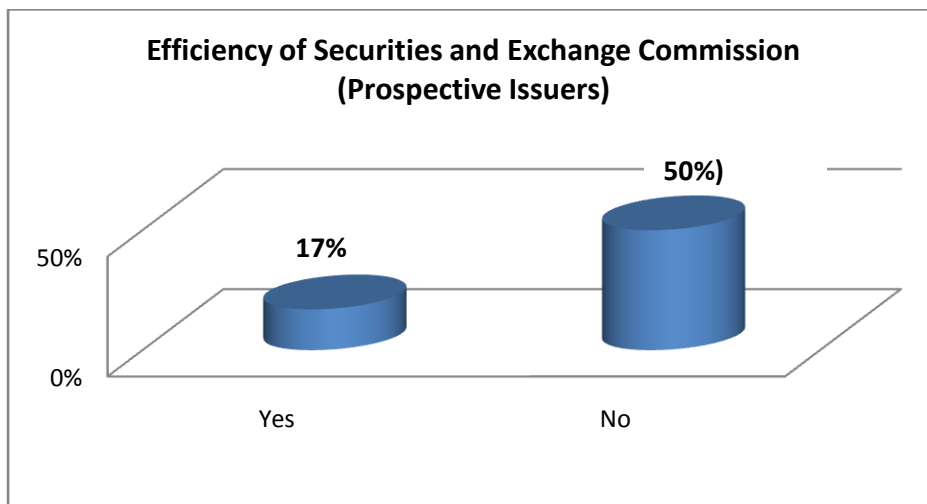
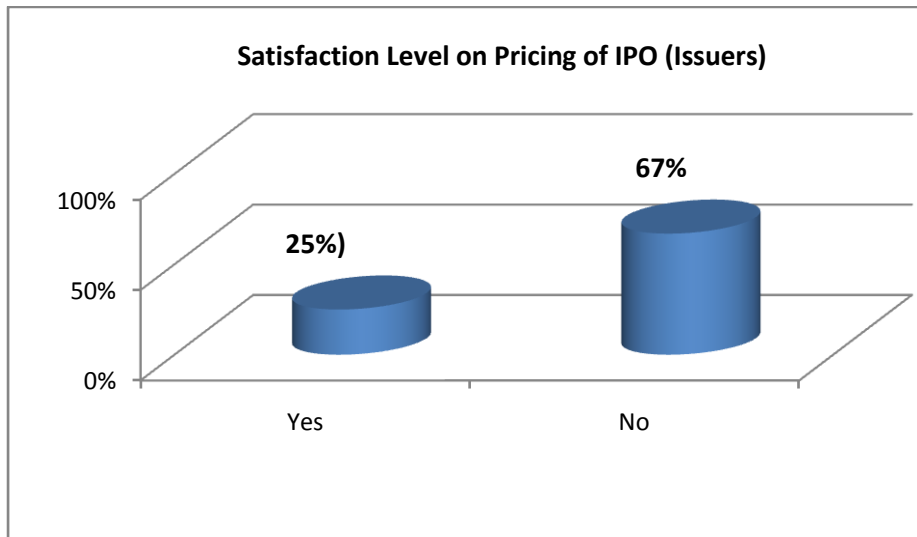
Very recently, Bangladesh has experienced severe financial crashes in stock market. Several reasons are found behind this. Banks and other financial institutions have increased their participation directly in the markets and also through loaning money to BO account holders for trading on margins. Many brokerage houses have been allowed to open brokerage houses in divisional and district headquarters making it easier and attractive to trade in shares. As a result, the number of BO accounts shoots up to 33 lakh from below five lakh. The lure of making a fast buck always attracts people and like in 1996 they rushed in thousands. The upsurge began a year or so back when Grameen Phone offered a large IPO (over 4000 crore) with much higher values over the face value of Tk. 10 only. Even then the issue was only about 10 percent of the total capital of Grameen Phone. When trading began with such higher value and it was included in the DSE index for the entire capital value of Grameen there was a big jump in the index about 1000 points. When the index reached 6000 or so from under 3000, journalists asked the finance minister about it and he quickly dismissed that the market was not overheated. Since there was no capital gain tax on the earnings and no restrictions were placed by Bangladesh Bank on transferring their capital plus gains they took advantage of super returns and transferred money out of the country by buying dollars from the curb markets.

The book building method was allowed to raise prices of IPOs by using faulty accounting practices and many low earning companies took advantage of the system in private placements and then going to market with much higher valued IPOs without due regard to P/E ratios. During the last two weeks of the crisis Bangladesh Bank supplied Tk.200 plus 200 crore to ICB to hold prices up by buying shares. That gave investors signal that more such bailout funds would be forthcoming. That did not come and the market collapsed in a free fall due to failure in the circuit breaker on the last day before it was closed for four days at a stretch.

Bangladesh also needs huge bailout programmers to rescue the small investors but where will the money come from. And again it raises the issue of moral hazards in economics when government support is offered to rescue people in crisis. That may set a pattern for the people and provide a basis for another bubble after a few years. Combination of wrong information

to the investors, illegal participation of banks and institutions in the stock markets, weak accounting functions are at the core of the crisis that saw billions of taka wiped out.

The current scenario of Satisfaction Level on Pricing of IPO is given below:



Source: Survey Results.

Findings and Recommendation

Book-building is regarded as an effective pricing method that causes lower under pricing according to literatures and is adopted by the majority of world's primary markets. SEC of Bangladesh therefore introduced book-building in IPO pricing process in 2009 in order to-

- 1) Increase the accuracy of pricing
- 2) Increase the pricing capabilities of institutional investors.

Whether or not the original objectives have been achieved, due to the limitation of data, there are not many empirical studies conducted so far to test the effectiveness of book-building in Bangladesh. However all literature agreed that book-building should reduce under-pricing and increased the pricing accuracy.

In summary, we have received the following implications:

- 1) Book-building pricing method introduced into Bangladesh's market has not reduced price manipulation as expected; on the other hand, it has significantly increased possibly due to other external effects.
- 2) Book-building has to some extent reduced the signaling and ex-ante uncertainty effect on under-pricing. That is probably because through the delivery of due diligence report to investors and two rounds of book-building, more information has been disclosed from the issuer-side that reduced the unnecessary price discount.
- 3) IPOs on Dhaka Stock Exchange after book-building that have higher initial return have significantly under-perform more than IPOs with lower initial returns. This is probably due to the overwhelming demand for blue-chip stocks.
- 4) Large number of institutional investors involved in book-building are distorted as signal of "hot issue" and cause "herding behavior" that sarcastically increased price manipulation, as public investors on secondary market in Bangladesh closely observe the actions from institutions. Besides, under-writers tend to over-adjust offer price based on the information collected from book-building.

Under this poor satisfaction level SEC & the relevant authorities should come forward to implement the best IPO pricing method specially the BBM to gain the confidence of investors, issuers as well as ensure an efficient capital market in Bangladesh.

Conclusion

In Bangladesh Capital Market, There is a huge gap of Supply and Demand side in the Capital market. So, the book building method will encourage big and established companies, from both home and abroad, to be listed on the stock exchanges, as the book building method ensures a fair price of a company's stocks. The book building method will lead to a price discovery and ensure fair stock prices which cannot be attained by the current fixed-price method of pricing IPOs. Moreover, investors expressed their positive opinions that the book building method would enhance market depth, volume and value turnover, market capitalization, supplies of IPOs among others.

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