

Internship Report

On

Investment Risk Management of
Islami Bank Bangladesh Limited



ইসলামী ব্যাংক বাংলাদেশ লিমিটেড
ইসলামী ব্যাংক বাংলাদেশ লিমিটেড
Islami Bank Bangladesh Limited

Internship Report on Investment Risk Management of Islami Bank Bangladesh Limited

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Date of Submission: 16 September, 2014



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Letter of Transmittal

16 September, 2014

Mr. MahmudulHaq

Assistant Professor,

Brac Business School, Brac University

Subject: Submission of Internship Report on “Investment Risk Management of Islami Bank Bangladesh Limited”.

Dear Sir,

With best respect and honour, I would like to inform you that I have completed my internship report on “Investment Risk Management of Islami Bank Bangladesh Limited”. It is an immense pleasure for me to place the same before you.

I made every endeavour to prepare this dissertation and tried my level best to accumulate relevant and insightful information. It is a great experience for me to work on this topic. I have tried to make the report vivid and comprehensive within the scheduled time and limited resources.

I sincerely hope that this report will help you to evaluate me. I will be obliged to clarify any matter or to provide any further information regarding this report.

Thanking you for your kind supervision.

Sincerely yours,

.....
Md. Moeid Hasan

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Major in Finance

Brac University

Declaration

I am **Md.MoeidHasan**, a student of MBA program, Brac University, hereby declare that the internship report titled“**Investment Risk Management of Islami Bank Bangladesh Limited**” is prepared after the completion of my internship at Islami Bank Bangladesh Limited, Mohakhali Branch under the intensive supervision and guidance of **Mr. Md. Faruque Al-Mamun**, Vice President and Head of Branch, Mohakhali Branch, Islami Bank Bangladesh Limited and **Mr. MahmudulHaq**, Assistant Professor ,Brac Business School, Brac University.

I also declare that the internship report is prepared for academic purpose only. This report is not submitted by others.

.....

Md. MoeidHasan

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MBA Program

Major in Finance

Brac University

Supervisor's Certificate

This is to certify that the Internship Report on “**Investment Risk Management of Islami Bank Bangladesh Limited**” is the authentic record and the report is done by **Md.MoeidHasan**, under my direct supervision as a partial fulfilment of the requirement of Master's of Business Administration (MBA) degree from the Department of Finance, Brac University

So far I know, **Md. MoeidHasan** has prepared this report by him and is not copied or borrowed from anywhere without proper acknowledgement.

I wish him every success in life.

.....
Mr. MahmudulHaq

Assistant Professor

Brac Business School,

Brac University

Acknowledgement

First of all, I would like to express my deep gratitude to the almighty Allah for fruitfully preparing this internship report.

It was a great pleasure to prepare an internship report on the various aspects of banking activities focusing **Investment Risk Management** by the **Islami Bank Bangladesh Limited**. I would like to thank and convey my gratitude to honourable supervisor, **Mr.MahmudulHaq**, Assistant Professor, Brac Business School, Brac University, for letting me to prepare this report. I would also like to express my sincere appreciation to him for his wholehearted support and guidance

I am also very grateful to the honourable Vice President and Head of Branch, **Mr.Md. Faruque Al-Mamunand Abdullah Al-Amin** of Islami Bank Bangladesh Limited, Mahakhali Branch for their priceless advice and kind effort, which help me a lot to collect information and data about **Investment Risk Management of Islami Bank Bangladesh Limited**. Their valuable cooperation is the undividable part of this internship report. I would like to give thanks to Them.

The officials of this branch specially Mr. Mohammad Mujibur Rahman, Senior Principal Officer and Investment In-charge, had been extremely helpful in providing necessary documents, annual reports, statements, brochures etc. that have helped me in preparing this internship report.

Shower of thanks to those entire respondents who responded each and every time in collecting necessary data.

Executive Summary

Islami Bank Bangladesh Limited started its commercial operation on March 30, 1983 under the ambit of Banking Company Ordinance-1962 later on the Banking Company Act-1991 as the first interest free Shariah based commercial bank with an objective of catering Islamic Shariah based financial products. At present IBBL is operating with 276 branches in different areas of the country.

The main objective of this report is to analyze and focus on the overall investment risk management operations of IBBL. This report gives an idea about investment and investment risk management of IBBL. I used trend analysis, ratio analysis and comparative analysis to describe the investment risk management of IBBL. So, the report will be descriptive in nature. I discussed with the officials and executives of the IBBL, Mohakhali Branch and found the approximate data which has been used in this report. I have also collected secondary data from the annual reports and business development conference reports of IBBL, CRM by Bangladesh Bank, IBBL's website, annual reports of AIBL, SIBL, EXIMBBL, FSIBL, SJIBL, ICBIBL, synopsis and training materials provided by the IBTRA. To analyze and present the numerical data and values I have used column chart, bar chart, line chart, pie chart, and the formula has generated and used in Microsoft Excel. To start with the investment trend and different investment and investment risk related ratios of the bank reveals that IBBL has proven to be quite mature and financial strength over the past five years. I also compare this bank year-wise and with other Islamic PCBs and national level as a whole. Here, all sorts of analysis have been executed, in order to analyze how efficient, liquid, secure and desirable the bank is in terms of its finance. I prefer it to work with audited data rather than unaudited one. Thus it gives a better insight about the change incurred in the each situation. Finally I have shown some findings from the qualitative and quantitative analysis of IBBL. I have found that the IBBL's investment management policies are effectively shaped with all rules and regulations of the Bangladesh Bank and the Islamic Shariah. The Investment Risk Assessing and Granting Policies of IBBL are prepared by following the manual of Bangladesh Bank. Then I concluded my report saying The bank should always be aware, ready to respond quickly against competitors' actions as well as different economic conditions, bring new and innovative investment products and services, utilize advanced technical and technological means to be quickest and errorless, arrange various investment risk related training and workshop for the employees regularly etc. in order to keep their leading position among the Islamic banks of the country as well as the banking industry of Bangladesh and be placed in a better position in the upcoming future.

So, overall investment performance of IBBL is increasing day by day. Because most of the people in our country are religious minded and they want to invest their money according to Islamic Shariah.

Moreover people of all walks of life can easily transact with IBBL compared to other Private Commercial Banks in the country.

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Acronyms

AIBL	Al-Arafah Islami Bank Limited
BB	Bangladesh Bank
BBA	Bachelor of Business Administration
BOD	Board of Directors
BUBT	Bangladesh University of Business and Technology
CAR	Capital Adequacy Ratio
CIB	Credit Information Bureau
CRG	Credit Risk Grading
CRISL	Credit Rating Information and Services Limited
CRM	Credit Risk Management
EXIMBBL	Export Import Bank of Bangladesh Limited
FSIBL	First Security Islami Bank Limited
HCRO	Head Office Credit Risk Officer
HDS	Household Durable Investment Scheme
HO	Head Office
HOBU	Head of Business Unit
HOCR	Head of Credit Risk
HPSM	Hire Purchase under Shirkatul Melk
IBBL	Islami Bank Bangladesh Limited
IBTRA	Islami Bank Training and Research Institute
ICAAP	Internal Capital Adequacy Assessment Process
ICBIBL	ICB Islamic Bank Limited
IDB	Islamic Development Bank
IDR	Investment Deposit Ratio
KYC	Know Your Customer
MPB	Mudaraba Perpetual Bond
NRB	Non Resident of Bangladesh
OIC	Organization of the Islamic Conference
PCB	Private Commercial Bank
PLS	Profit and Loss Sharing
RDS	Rural Development Scheme
REIP	Real Estate Investment Program
RM	Relationship Manager
ROA	Return on Asset
ROI	Return on Investment
SBIS	Small Business Investment Scheme
SIBL	Social Investment Bank Limited
SJIBL	Shahjalal Islami Bank Limited
SME	Small and Medium Enterprise
SRPT	Supervisory Review Process Team
TIS	Transport Investment Scheme
TR	Trust Receipt
UN	United Nations
VP	Vice President
ZCRO	Zonal Credit Risk Officer

Part One

Introduction





1.1 Introduction:

Banks are financial institutions engaged in boosting national savings and capital formation as well as constituting infrastructure through the financing of various development projects. It performs multi-dimensional activities like borrowing and lending of money, drawing, collecting and discounting bills, transferring funds, safe deposit, vault/locker service, foreign exchange transactions etc. The world of banking is undergoing a transformation. Banking today has evolved into a highly competitive and sophisticated business in which technology increasingly provides the edge. Today's customers want service and information to be provided at all times and places.

As Bangladesh is one of the largest Muslim countries in the world, the deep commitment of the people of this country to the Islamic way of life according to the Holy Quran and the Sunnah. Obviously, it remains a deep cry in their hearts to fashion and design their economic lives in accordance with the precepts of Islam. The establishment of Islami Bank Bangladesh Limited on March 13, 1983, is the exact reflection of this inner urge of its people. This Bank is the first of its kind in Southeast Asia. The bank is devoted to conducting all banking activities on the basis of interest free & profit and loss sharing system.

1.2 Origin of the Study:

The current world is changing rapidly. To face the challenge of competitive free market economy, to keep pace with the trend of every organization who demanded executive with modern knowledge and to provide fresh graduate with modern theoretical and professional knowledge in banking as well as all other different institutions, BracUniversity has assigned the internship program for the students to help them out to have a practical knowledge to work in a real office environment. Under this program the students are sent to gather practical knowledge about the working environment and activities. The report is a requirement of the internship program for my MBA degree. My University supervisor Mr. MahmudulHaqAssistantProfessor suggested me that the topic of my report would be **“Investment Risk Management of Islami Bank Bangladesh Limited”**.



1.3 Rationale of the Study:

There are three types of scheduled commercial banks in operation in our economy. They are Nationalized Commercial Banks, Private Commercial Banks and Foreign Private Commercial Banks. Islamic Banks have discovered a new horizon in the field of banking area, which offers different general banking, investments and foreign exchange banking services. I have chosen Islami Bank Bangladesh Limited, which has some special mission & vision to establish an interest free banking in the country. From the very beginning since inception the bank has been facing different kinds of problem due to lack of Islamic Banking Act and Islamic Money Market besides general people has no idea about the Islamic mode of operations. So, for obvious reason I have selected the topic **“Investment Risk Management of Islami Bank Bangladesh Limited”**. The dissertation report is an integral part of the MBA program of the university. So it is obligatory to undertake such task by the students who desire to complete and successfully end-up their MBA degree. This also provides an opportunity to the students to minimize the gap between theoretical and practical knowledge. Students are required to work on a specific topic based on their theoretical and practical knowledge acquired during the period of the internship program and then submit it to the respective authority. That is why I have prepared this report.

1.4 Scope of the Study:

The scope of the organizational part covers the organizational structure, background, products and services and the financial performance of Islami Bank Bangladesh Limited as a whole and the main part covers investment risk management of IBBL. This report helps us to understand the clear real-time experience about the investment business operations of IBBL. It also helps us to understand how they deal with the investment clients alongside the way of managing investment and investment risk.

This report is only done for gathering information about investment risk management of IBBL by focusing on the performance and management of investment business alongside investment risk of IBBL while ignoring any other department of the bank.

1.5 Objectives of the Study:

1.5.1 Broad Objective:

The prime objective of this report is to analyze the **“Investment Risk Management of Islami Bank Bangladesh Limited”**.



1.5.2 Specific Objectives:

In order to accomplish the broad objective following specific objectives are emerged,

- To depict the procedures of IBBL follow for lending to the customer.
- To know the policies of investment risk management of IBBL.
- To know the trend and growth of investment of IBBL over the year.
- To know and analyze the sector-wise investment, mode-wise investment, geographical distribution of investment etc. of IBBL.
- To evaluate the overall investment risk management system of IBBL through different ratios.
- To compare and analyze the investment and investment risk related performance of IBBL with other Islamic banks of Bangladesh as well as the banking sector.
- To recommend actions that may be necessary to redesign the investment risk management of IBBL.

1.6 Methodology of the Study:

In order to conduct such a study the report preparer must follow some specific methods. This report is based on an empirical method which is stated under.

1.6.1 Type of Research:

Trend analysis, ratio analysis and comparative analysis were used to describe the “**Investment Risk Management of Islami Bank Bangladesh Limited**” in this report. So, the report will be descriptive in nature which is possible through descriptive research. As investment risk management is a part of company’s internal management I have nothing to do with the variables other than stating what IBBL is doing for managing its investment and investment risk. According to the base of objective, this research is called descriptive research.

1.6.2 Sources of Data:

All the relevant data regarding this report are collected from two sources,

1.6.2.1 Primary Sources of Data:

I discussed with the officials and executives of the IBBL, Mohakhali Branch and found the approximate data which has been used and presented in this report. The study has been conducted through the assistance of Investment Department, Mohakhali Branch as per their operating and maintaining an investment business through applying modern and technological means. I have also physically observed the effectiveness of the efforts relating investment business effectively and efficiently managed by Islami Bank Bangladesh Limited, Mohakhali Branch.



Primary sources of data include the following:

- ➔ Practical work experience,
- ➔ Informal face to face conversation with the clients and officers of the bank.

1.6.2.2 Secondary Sources of Data:

I have collected secondary data from the following sources,

- ➔ Annual Reports of IBBL: 2008-2012.
- ➔ Business Development Conference Report: 2011 and 2012.
- ➔ Unpublished data from the IBBL, Mohakhali Branch.
- ➔ Manuals of IBBL regarding investment business.
- ➔ Credit Risk Manual by Bangladesh Bank.
- ➔ IBBL's website (www.islamibankbd.com).
- ➔ Annual Reports of AIBL, SIBL, EXIMBBL, FSIBL, SJIBL, ICBIBL: 2012.
- ➔ Synopsis and training materials provided by the Islami Bank Training and Research Institute.

For tertiary sources of data I have used references from the articles and journals utilized and have also utilized electronic data sources such as the Internet.

1.6.3 Data Analysis Tools and Techniques:

To analyze and present the numerical data and values associated with Investment Risk Management of Islami Bank Bangladesh Limited, I have used following tools and techniques,

- i. Column Chart,
- ii. Bar Chart,
- iii. Line Chart,
- iv. Pie Chart, and
- v. The formula has generated and used in Microsoft Excel.

1.6.4 Data Analysis and Reporting:

Both qualitative and quantitative analyses have been done while conducting this study. Microsoft Word and Microsoft Excel were used to analyze, process and graphically represents the gathered data.



1.7 Limitations of the Study:

Although I have obtained the whole hearted co-operation from the employees of Islami Bank Bangladesh Limited, Mohakhali Branch and Islami Bank Training and Research Academy but in the way of my study, I have faced the following problems, which may be termed as the limitations of the study. Some limitations are as under:

- The main constraint of the study was insufficiency of information, which was required for the study. There are various information the bank employee can't provide due to security and other corporate obligations.
- All the branches of the bank were not physically visited and all the concerned personnel of the bank have not been interviewed.
- Lack of in-depth knowledge and analytical ability for writing such report.
- Learning all the banking functions about the investment risk management within just 60 days was really tough.
- Data and information used in this study are mostly from secondary sources.
- Large scale research was not possible due to the constraints and restrictions posed by the bank.
- Another limitation of this report is the bank's policy of not disclosing some data and information for obvious reason, which might make the report more worthy.

The report has encountered these limitations that may hinder the progress of the study but with constant effort, I try to minimize the negative effects of these limitations.

Part Two

An Overview of Islami Bank Bangladesh Limited





2.1 Overview of Islami Bank Bangladesh Limited:

The interest based banking system and mechanism is very familiar to us. At the time of independence Bangladesh inherited an interest-based banking system introduced by the British government during the colonial period. At present four nationalized banks, four specialized banks, nine foreign banks and thirty one private commercial banks are operating in the financial market of Bangladesh. But the Islamic banking in Bangladesh dates back to 1983 when the Islami Bank Bangladesh Limited was established with a view to conducting its banking activities based on the principle of Islamic Shariah.

Islami Bank Bangladesh Limited was incorporated as the first Shariah based interestfree bank in SouthEast Asia on the 13th March 1983 as a public limited company. The first branch of the Bank was Local Office at Motijheel in Dhaka which started functioning informally on 30th March 1983. It was formally inaugurated on 12th August 1983. The Bank was established with Tk.80.00 million as paid up capital which has been increased to Tk.12,509.64 million as on December 31, 2012. Corporate Headquarter of the Bank, housed in an 18-storied own modern building, is located at 40, Dilkusha Commercial Area, Dhaka. Islami Bank of Bangladesh Limited has gained the first position in all private banks in terms of deposits, investment, export and import and remittance collection. According to the Bangladesh Bank, the Central Bank of Bangladesh, the total deposits of the Islamic banking systems are now 25 percent of all private banks' deposits and its investment are 30 percent.



2.2 Mission:

To establish Islamic banking through the introduction of a welfare oriented banking system and also ensure equity and justice in all economic activities, achieve balanced growth and equitable development through diversified investment operations particularly in the priority sectors and less developed areas of the country.

To encourage socioeconomic development and financial services to the low-income community particularly in the rural areas.

2.3 Vision:

The vision of IBBL is to always strive to achieve superior financial performance, be considered a leading Islamic Bank by reputation and performance:

- To establish and maintain the modern Banking techniques, to ensure soundness and development of the financial system based on Islamic principles and to become the strong and efficient organization with highly motivated professionals working for the benefit of peoples, based upon accountability, transparency and integrity in order to ensure the stability of financial systems.
- To encourage savings in the form of direct investment.
- To encourage investment particularly in projects, which are more likely to lead to higher employment.

2.4 Core Values and Commitments:

2.4.1 Core Values:

- | | |
|--|---|
| ▪ Trust in Almighty Allah. | ▪ Environmental Consciousness. |
| ▪ Strict Observance of Islamic Shariah. | ▪ Personalized Service. |
| ▪ Highest Standard of Honesty, Integrity & Morale. | ▪ Adoption of Changed Technology. |
| ▪ Welfare Banking. | ▪ Proper Delegation, Transparency & Accountability. |
| ▪ Equity and Justice. | |

2.4.2 Commitments:

- | | |
|------------------------|--------------------------|
| ▪ To Shariah. | ▪ To the Customers. |
| ▪ To the Regulators. | ▪ To the Employees. |
| ▪ To the Shareholders. | ▪ To other Stakeholders. |
| ▪ To the Community. | ▪ To Environment. |



2.5 Corporate Profile:

Name of the Company	Islami Bank Bangladesh Limited
Legal Status	Public Limited Company
Company Registration Number and Incorporation	C - $\frac{10589}{485}$ Dated March 13, 1983
Certificate of Commencement of Business	March 27, 1983
Inauguration of 1st Branch	March 30, 1983 (Local Office, Dhaka)
Formal Inauguration	August 12, 1983
Tax Payer Identification Number (TIN)	210-200-0887
VAT Registration Number	9015000857
Chairman	Prof. Abu Nasser Muhammad AbduZaher
Managing Director	Mohammad Abdul Mannan
Company Secretary	Abu Reza Md. Yeahia
Chief Financial Officer	Mohammad NesarUddin, FCA, FCMA
Number of Employees	12,188
Number of Branches	276
Number of Shareholders	60,302
Number of MPB Holders	27,723
Credit Rating Agency	Credit Rating Information and Services Ltd. (CRISL)
Auditors	M/S. A. Qasem& Co. M/S. ACNABIN
Tax Consultant	M/S. K.M. Hasan& Co.
Authorized Capital	Tk. 20,000.00 million
Paid up capital	Tk.12,509.64 million
<u>Share of Capital:</u>	
a. Local Shareholders	36.91%
b. Foreign Shareholders	63.09%
Registered Office	40, Dilkusha Commercial Area, Dhaka-1000, Bangladesh.
SWIFT	IBBLBDDH
Email	info@islamibankbd.com
Website	www.islamibankbd.com

Source: Annual Report 2012 (As on 31 December, 2012)



2.6 Five Years Performance of IBBL at a Glance:

Particulars	2008	2009	2010	2011	2012
Balance Sheet Matrix (In million Taka)					
Authorized Capital	10,000	10,000	10,000	20,000	20,000
Paid up Capital	4,752	6,177.60	7,413.12	10,007.71	12,509.64
Reserve Fund	9,308.49	13,927.94	16,081.14	17,792.50	27,245.87
Retained Earnings	1,425.60	1,853.28	2,594.59	3,202.47	3,127.41
Shareholders Equity	14,060.49	20,105.54	23,494.26	27,800.21	39,755.51
Deposits (including Bills Payable)	202,115.45	244,292.14	291,934.60	341,853.67	417,844.14
Investments (including Investment in Shares and Securities)	187,586.55	225,752.41	275,493.94	322,772.83	399,930.79
Investments (excluding Investment in Shares and Securities)	180,053.94	214,615.80	263,225.13	305,840.56	372,920.72
Investment Deposit Ratio	89.08%	87.85%	90.17%	87.29%	85.18%
Total Assets (including Contra)	288,017.19	340,638.49	443,684.79	502,613.05	592,580.50
Fixed Assets	4,407.22	6,512.36	6,748.44	7,100.19	14,808.23
Capital Matrix					
Total Risk Weighted Assets (RWA)	173,289.43	202,756.60	256,804.90	257,564.30	311,511.60
Core Capital- Tier- I	11,272.12	14,714.10	18,559.80	23,401.24	28,225.10
Supplementary Capital (Tier II)	7,299.96	8,905.70	9,840.20	10,315.49	13,803.20
Regulatory Capital (Tier I, II & III)	18,572.08	23,619.80	28,400.00	33,716.73	42,028.30
Statutory Capital (Paid up Capital & Statutory Reserve)	9,692.49	12,421.62	15,348.08	20,012.14	24,933.30
Equity/Capital Surplus/(Deficit)	1,243.14	3,344.16	5,287.58	7,960.24	10,877.10
Capital Adequacy Ratio	10.72%	11.65%	11.06%	13.09%	13.49%
Assets Quality					
Amount of Classified Investment	4,311.13	5063.40	4,655.63	8,292.32	14,212.80
Classified Investment to Total Investment	2.39%	2.36%	1.77%	2.71%	3.81%
Provision against Classified Investment	1,883.43	2,490.00	1,840.00	3,054.00	6,054.35
General Provision against Unclassified Investment	2,315.74	2,700.00	3,443.00	3,996.00	3,935.90
General Provision on Off Balance Sheet Items	570.83	510.00	930.00	1,120.00	1,100.45
Income & Expenditure Statement Matrix					
Investment Income	19,543.84	21,370.53	24,766.26	32,019.53	43,672.23
Profit Paid on Deposit	12,162.10	13,076.99	14,471.89	18,401.22	25,870.43
Net Investment Income	7,381.74	8,293.54	10,294.37	13,618.31	17,801.80
Total Income	23,756.33	25,404.37	30,128.90	38,401.29	50,345.77
Net Profit after Tax	2,674.80	3,403.55	4,463.47	4,841.45	5,524.44
Total Foreign Exchange Business	402,695	462,370	609,331	716,058	782,598
Distribution Networks					
Number of Correspondent Banks	275	295	295	313	320
Number of Foreign Correspondents	906	919	919	935	676
Number of Shareholders	33,686	52,164	58,923	60,550	60,302
Number of Employees	9,397	9,588	10,349	11,465	12,188
Number of Branches	206	231	251	266	276
Financial Indicators					
Gross Profit Ratio	46.80%	48.52%	51.97%	52.08%	48.61%
Cost of Fund	9.56%	8.76%	8.65%	8.86%	9.32%
Cost Income Ratio/Efficiency Ratio	0.73	0.74	0.72	0.73	0.76



Return on Equity (ROE)	19.02%	16.93%	19.00%	17.42%	13.90%
Return on Assets (ROA)	1.27%	1.34%	1.47%	1.35%	1.27%
Price Earnings Ratio (Times)	10.78	12.87	13.29	11.27	9.68
Spread	4.53%	4.86%	4.87%	4.03%	4.10%

Source: Annual Reports 2008-2012

2.7 Organogram of Islami Bank Bangladesh Limited:

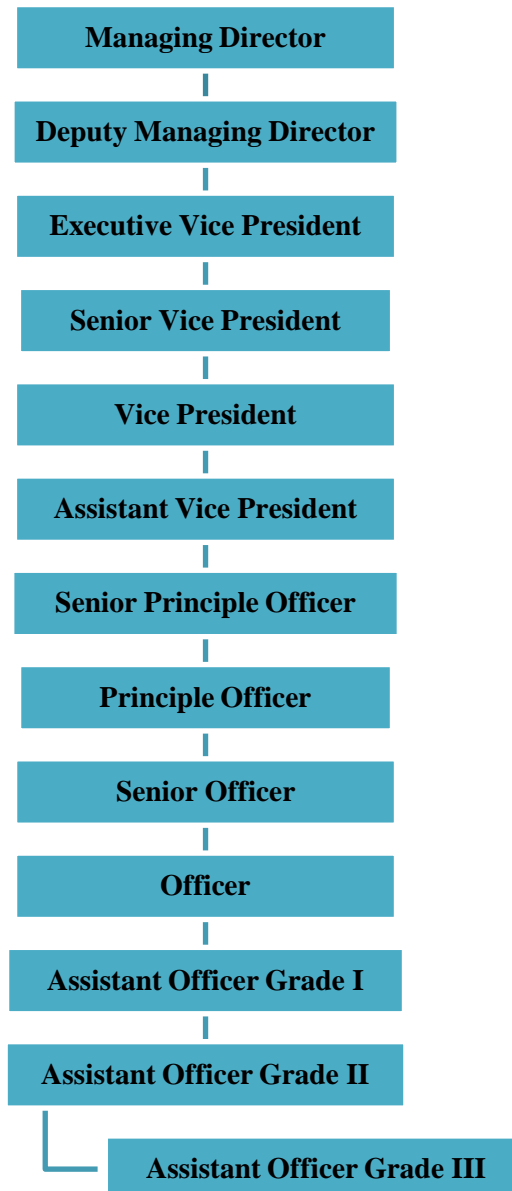


Figure 2.7: Organogram of IBBL

Source: Internal Report of IBBL, Mohakhali Branch



2.8 Board of Directors:

The present Board of IBBL consists of nineteen non-executive members including three Independent Directors and two Depositors Directors excluding ex-officio Managing Director. The Executive Committee, consisting of five members, is entrusted with the responsibilities of policy making and taking important and strategic decisions as authorized by the Board within the norms set by Bangladesh Bank. All the Directors of IBBL are non-executive Directors except the Managing Director.

2.9 Risk Management Wing of IBBL:

To ensure effective risk management, Risk Management Unit was introduced by IBBL in November, 2009. The unit was functioning like a committee comprising of members from different divisions. In April 2011, a separate Risk Management Unit headed by a senior executive has been formed. Later on, understanding the importance of risk management of such a leading entity in the industry, the Board of Directors of IBBL has given highest emphasis on risk governance and risk management and upgraded the unit into an independent and separate Risk Management Wing in its 193rd meeting held on 14 May, 2012.

2.10 Corporate Culture & Recognition:

Since inception, IBBL has been practicing corporate culture at all levels. IBBL has always been trying to run the Bank professionally and showed its competence during last 30 years of operation. The workforce of IBBL starting from the CEO down to a Messenger are very much involved and committed professionals and thus could develop the Bank as one of the highly complied one. They work under the guidelines of Bangladesh Bank, other Regulatory Authorities and policies framed by the Board of Directors without any interference from any corner. IBBL is the proud recipient of the ‘SAFA (South Asian Federation of Accountants) Corporate Governance Award for 2010 & 2011’, ‘SAFA Award for Best Presented Reports-2011’, ICAB’s (Institute of Chartered Accountants of Bangladesh) ‘SAARC Anniversary Award for Corporate Governance-2011’ & ‘ICAB Best Presented Annual Report-2011’, and ICMAB’s (Institute of Cost and Management Accountants of Bangladesh) ‘ICMAB Best Corporate Award for 2011 & 2012’, which are the obvious recognitions of the Bank’s sustained success in every aspects of its operations.



2.11 Products and Services of Islami Bank Bangladesh Limited:

Local Currency Deposit Accounts:

1. Al-Wadeah Current Account,
2. Mudaraba Savings Account,
3. Mudaraba Term Deposit Account,
4. Mudaraba Special Notice Account,
5. Mudaraba Special Savings (Pension) Account,
6. Mudaraba Hajj Savings Account,
7. Mudaraba Savings Bond Account,
8. Mudaraba Waqf Cash Deposit Account,
9. Mudaraba Monthly Profit Deposit Account,
10. Mudaraba Muhar Savings Deposit Account,
11. Students Mudaraba Savings Account,
12. Mudaraba Farmers Saving Account,
13. Mudaraba NRB Savings Bond.
5. Bai-Istisna,
6. Hire Purchase under ShirkatulMelk,
7. Mudaraba,
8. Musharaka,
9. Musharaka Investment in Potato Storage,
10. Murabaha Post Import,
11. Murabaha Import Bills,
12. Murabaha Import LC,
13. Bai-Muajjal Back to Back Bills,
14. Bai-as-sarf (Foreign Documentary Bill),
15. Bai-as-sarf (Foreign Currency Cheques/Drafts),
16. Murabaha Foreign Currency Investment,
17. Musharaka Documentary Bill,
18. Bai-Salam (Pre-shipment),
19. Mudaraba NRB Entrepreneur Investment Scheme.

Foreign Remittance Services:

1. Central Crediting of Remittances,
 2. Payment of 3rd Bank Remittance through TT & PO,
 3. Payment of Spot Cash Remittances - Online and Web-based,
 4. Centralised NRB Account Opening,
 5. SMS Notification,
 6. SMS Push Pull Service,
 7. Maintaining of NRD & NRT Accounts.
- Many others include,
- ➔ Deposit Products in Foreign Currency,
 - ➔ Products in Off-shore Banking Unit,
 - ➔ Foreign Remittance Products,
 - ➔ Welfare-oriented Special Investment Schemes,
 - ➔ ATM Services,
 - ➔ Other Banking and Value Added Services,
 - ➔ Treasury Activities,
 - ➔ Special Services through Islami Bank Foundation,
 - ➔ Training Services, and
 - ➔ Diploma in Islamic Banking.

Investment Products:

1. Bai-Murabaha,
2. Bai-Muajjal,
3. Bai-Istijrar,
4. Bai-Salam,

Part Three

Theoretical Aspects





3.1 Islamic Bank and Banking:

Islamic banking is a banking system that is based on the principles of Islamic law (also known as Shariah) and guided by Islamic economics. Two basic principles behind Islamic banking are the sharing of profit and loss and, significantly, the prohibition of the collection and payment of interest. The Islamic banking system uses methods of profit and loss sharing to facilitate financial transactions: for some types of loans, the borrower only needs to pay back the amount owed to the lender, but the borrower can choose to pay the lender a small amount of money to serve as a gratuity. Since this system of banking is grounded in Islamic principles, all the undertakings of the banks follow Islamic morals. Therefore, it could be said that financial transactions within Islamic banking are a culturally distinct form of ethical investing (for example, investments involving alcohol, gambling, pork, etc. are prohibited).

Islamic banking has been defined in a number of ways. The definition of Islamic bank, as approved by the General Secretariat of the OIC, is stated in the following manner. *"An Islamic bank is a financial institution whose status, rules and procedures expressly state its commitment to the principle of Islamic Shariah and to the banning of the receipt and payment of interest on any of its operations"*. Shawki Ismail Shehta viewing the concept from the perspective of an Islamic economy and the prospective role to be played by an Islamic bank therein opines: *"It is, therefore, natural and, indeed, imperative for an Islamic bank to incorporate in its functions and practices commercial investment and social activities, as an institution designed to promote the civilized mission of an Islamic economy"*.

It appears from the above definitions that Islamic banking is a system of financial intermediation that avoids receipt and payment of interest in its transactions and conducts its operations in a way that it helps achieve the objectives of an Islamic economy.

3.2 Islamic Investment:

Investment is the action of deploying funds with the intention and expectation that they will earn a positive return for the owner. Funds may be invested in either real assets or financial assets. When resources are used for purchasing fixed and current assets in a production process or for a trading purpose, then it can be termed as a real investment. The establishment of a factory or the purchase of raw materials and machinery for production purposes are examples in point. On the other hand, the purchase of a legal right to receive income in the form of capital gains or dividends would be indicative of financial investments. Specific examples of financial investments are: deposits of money in a bank account, the purchase of Mudaraba Savings Bonds or stock in a company. Ultimately, the savings of investors in financial assets are invested by the respective company into real assets in the



form of the expansion of plant and equipment. Since Islam condemns hoarding savings and a 2.5 percent annual tax (Zakat) is imposed on savings, the owner of excess savings, if he is unable to invest in real assets, has no option but to invest his savings in financial assets.

Conventional Loan or Credit	Islamic Investment
In conventional financing, lenders lend to borrowers to make a profit from the interest charged on the principal amount.	Islamic financing avoids interest-based transactions, and instead introduces the concept of buying something on the borrower's behalf, and selling it back to the borrower at a profit.
For loans, borrowers pay an interest on the outstanding principal amount. Interest rates can be a fixed rate or based on a floating rate.	In place of interest, a profit rate is defined in the contract. Like conventional financing, profit rates can be a fixed rate, or based on a floating rate.
The lenders have the certainty of getting interest.	The investor does not have the certainty of profit. The investor may face profit or loss both.
Loan is given to any sector.	Generally investment is given to productive and business sector.

3.3 Factors Related to Investment:

- ❖ Risk,
- ❖ Time,
- ❖ Interest Rate,
- ❖ Security or Collateral,
- ❖ Operating Expense,
- ❖ Legal Considerations,
- ❖ Inflation,
- ❖ Finance Charge.

3.4 Risk:

Risk implies a situation that threatens or limits an organization's ability to achieve its goal. Risk in a banking organization is the possibility that the outcome of an action or event could bring up adverse impacts. Banking operations are mainly exposed to investment risk, market risk, operational risk, and residual risk, investment concentration risk, liquidity risk, strategic risk, environmental risk, interest rate risk etc. Risk management means a process for identifying, measuring and mitigating all sorts of foreseeable risks for sustainable growth of an organization and its shareholders' value.



3.5 Investment (Credit) Risk:

Risk Management in Islamic banking is not significantly different from conventional banking. Credit risk is known as investment risk by the Islamic banks literally both of them are same.

Credit risk arises from the potential that a bank's borrower will fail to meet its obligations in accordance with agreed terms. Credit risk also refers the risk of negative effects on the financial result and capital of the bank caused by borrower's default on its obligations to the bank. Generally credits are the largest and most obvious source of credit risk. However, credit risk could stem from both on-balance sheet and off-balance sheet activities. It may arise from either an inability or an unwillingness to perform in the pre-committed contracted manner.

Like conventional banks, Islamic banks also face credit risk in most of the modes of financing that they use. It is well known that Murabaha, Istisna, and installment sale or sales with delayed payment thus generating debts in the accounts of the banks. The fundamental form of risk in all these contracts is credit risk. Salam gives rise to a commodity debt rather than a cash debt, but it also involves credit risk. Mudaraba and Musharaka, on the other hand, are contracts of participation, and the funds given by the bank to entrepreneurs are not liabilities. Yet, these two also bears a credit risk in two ways. First, in the case of tort or negligence, the entrepreneur is liable to guarantee the capital which means a debt liability. Second, when the capital of Mudaraba or Musharaka are employed in a deferred sale, which is what takes place in most Mudarabas, the owner of capital, the bank in this case, bears an indirect credit risk. This risk pertains to the ability of the counter parties to repay.

3.6 Investment (Credit) Risk Management:

The investment (credit) portfolio of a bank usually consists of a money market portfolio, capital market portfolio and general credit portfolio. Here a bank is highly exposed in the risks of capital market and general credit portfolio. In recent times, the awareness among the bankers has grown regarding the need for managing perceived risks in credit related activities. One of the goals of credit risk management in banks is to maximize a bank's risk-adjusted rate of return by maintaining credit risk exposure within the acceptable level. Hence, the credit risk assessment and grading system are being applied to evaluate, identify, measure and monitor the level or status of perceived risk associated with a credit proposal. A number of financial and non-financial factors or parameters are used by the banks for these purposes. The use of comprehensive credit risk assessment and grading techniques increasing very rapidly in the banking sector in Bangladesh because of deterioration in the credit standing of the clients, adoption of Basel accords, compliance of International Accounting Standards (IAS) & International Financial Reporting Standards (IFRS) and the vast revolution of technologies that has made the bankers user friendly in the adoption of these techniques.



3.7 Principles for the Assessment of Banks' Investment (Credit) Risk Management:

❑ Establishing an Appropriate Credit Risk Environment:

Principle 1: A board should have responsibility for approving and periodically reviewing the credit risk strategy and significant credit risk policies of the bank. The strategy should reflect the bank's risk appetite and the level of profitability the bank expects to achieve for incurring various credit risks.

Principle 2: Senior management should have responsibility for implementing the credit risk strategy approved by the board and for developing policies and procedures for identifying, measuring, monitoring and controlling credit risk. Such policies and procedures should address credit risk in all of the bank's activities and at both the individual credit and portfolio levels.

Principle 3: Banks should identify and manage credit risk inherent in all products and activities. Banks should ensure that the risks of products and activities new to them are subject to adequate procedures and controls before being introduced or undertaken, and approved in advance by the BOD or its appropriate committee.

❑ Operating Under a Sound Credit Granting Process:

Principle 4: Banks must operate under sound, well-defined credit-granting criteria. These criteria should include a thorough understanding of the borrower or counter party, as well as the purpose and structure of the credit, and its source of repayment.

Principle 5: Banks should establish overall credit limits at the level of individual borrowers, and group of connected counter parties that aggregate different types of exposures, both in the banking and trading book and on and off balance sheet.

Principle 6: Banks should have a clearly established process in place for approving new credits as well as the extension of existing credits.

Principle 7: All extensions of credit must be made on an arm's-length basis. In particular, credits to related companies and individuals must be monitored with particular care and other appropriate steps taken to control or mitigate the risks of connected lending.

❑ Maintaining an Appropriate Credit Administration, Measurement and Monitoring Process:

Principle 8: Banks should have in place a system for the ongoing administration of their various credit risk-bearing portfolios.

Principle 9: Banks must have in place a system for monitoring the condition of individual credits, including determining the adequacy of provisions and reserves.



Principle 10: Banks should develop and utilize internal risk rating systems in managing credit risk. The rating system should be in line with the regulatory instructions and consistent with the nature, size and complexity of a bank's activities.

Principle 11: Banks must have information systems and analytical techniques that enable management to measure the credit risk inherent in all on balance sheet and off-balance sheet activities. The management information system should provide adequate information on the composition of the credit portfolio, including identification of any concentrations of risk.

Principle 12: Banks must have in place a system for monitoring the overall composition and quality of the credit portfolio.

Principle 13: Banks should take into consideration potential future changes in economic conditions when assessing individual credits and their credit portfolios, and should assess their credit risk exposures under stressful conditions.

□ **Ensuring Adequate Controls over Credit Risk:**

Principle 14: Banks should establish a system of independent, ongoing credit review and the results of such reviews should be communicated directly to the board and senior management.

Principle 15: Banks must ensure that the credit-granting function is being properly managed and that credit exposures are within levels consistent with prudential standards and internal limits. Banks should establish and enforce internal controls and other practices to ensure that exceptions to policies, procedures and limits are reported in a timely manner to the appropriate level of management.

Principle 16: Banks must have a system in place for managing problem credits and various other workout situations

□ **The Role of Supervisors:**

Principle 17: Supervisors should require that banks have an effective system in place to identify, measure, monitor and control credit risk as part of an overall approach to risk management. Supervisors should conduct an independent evaluation of a bank's strategies, policies, procedures and practices related to the granting of credit and the ongoing management of the portfolio. Supervisors should consider setting prudential limits to restrict bank exposures to single borrowers or groups of connected counterparties.

3.8 Guidelines to Manage Investment (Credit) and Investment (Credit) Risk:

Credit Risk Management Guidelines involve in assessing and managing credit risks associated with the selection process of a potential borrower, credit structuring (amount, duration, purpose, repayment, and support), approval process of credit, credit documentation (security and disbursement), credit administration, credit monitoring and recovery functions of a bank or financial institution. At the selection stage, credit risk grading is essential to keep the credit risk exposure at a tolerable level.

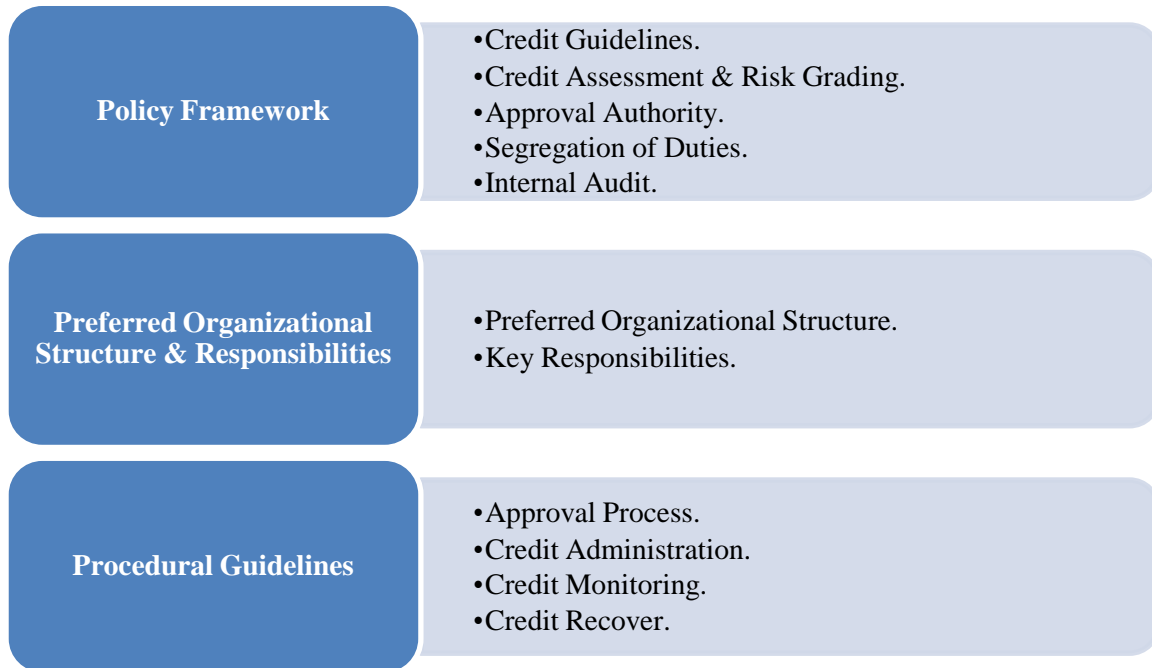


Figure 3.8: Guidelines for Investment (Credit) and Investment (Credit) Risk Management

Source: Managing Core Risks of Financial Institutions, Credit Risk Management, Industry Best Practice, Bangladesh Bank

This guideline will make us understand “To manage credit risk-

- ❑ How the credit will be “Assessed” and how the credit risk will be “Granted”?
- ❑ How the “Credit Approval Authority” will be worked and what are the processes?
- ❑ How “Internal Audit” can be used as a tool for managing credit risk?
- ❑ How the “Risk Management Structure” will be look like?
- ❑ What is the appropriate Credit Administration?
- ❑ How a bank can monitor its credit to Minimize Credit Risk?
- ❑ What are the effective steps to make an Effective Recovery Performance?



3.8.1 Policy Framework:

This section details fundamental credit risk management policies that are recommended for adoption by all banks in Bangladesh. The guidelines contained herein outline general principles that are designed to govern the implementation of more detailed lending procedures and risk grading systems within individual banks.

■ Credit Risk Policy:

Every bank should have a credit risk policy document that should include risk identification, risk measurement, risk grading or aggregation techniques, reporting and risk control or mitigation techniques, documentation, legal issues and management of problem facilities. Such policies and procedures shall provide guidance to the staff on various types of lending including Corporate, SME, Consumer, Housing etc.

■ Credit Risk Strategy:

The very first purpose of bank's credit strategy is to determine the risk appetite of the Bank. Once it is determined the bank could develop a plan to optimize return while keeping credit risk within predetermined limits. It is essential that the bank gives due consideration to their target market while devising credit risk strategy. The credit procedures should aim to obtain an in-depth understanding of the bank's clients, their credentials & their businesses in order to fully know their customers.

3.8.1.1 Credit Guidelines:

The Credit Guidelines should provide the key foundations for account officers or relationship managers to formulate their recommendations for approval, and should include the following:

- **Industry and Business Segment Focus:** Textiles: Grow, Cement: Maintain, Construction: Shrink.
- **Types of Facilities:** Lease, Term Loan, Home Loan, and Working Capital etc.
- **Single Borrower/Group Limits/Syndication**
- **Sector Lending Caps:** An important element of credit risk management is to establish exposure limits for single obligors and group of connected obligors. The bank may establish limits for a specific industry, economic sector or geographic regions to avoid concentration risk.
- **Product Lending Caps:** Bank should establish a specific product exposure cap to avoid over concentration in any one product.
- **Discouraged Business Types:** The bank may have segregated sectors to be discouraged based on the following,



Government Specified	<ul style="list-style-type: none"> ▪ Military equipment or weapons finance. ▪ Lending to companies listed on CIB black list or known defaulters.
Best Practice	<ul style="list-style-type: none"> ▪ Highly leveraged transactions. ▪ Logging, mineral extraction or mining, or other activity that is ethically or environmentally sensitive. ▪ Counter parties in countries subject to UN sanctions.
Company Specific	<ul style="list-style-type: none"> ▪ Finance of speculative investments. ▪ Share lending. ▪ Taking an equity stake in borrowers. ▪ Lending to holding companies. ▪ Bridge loans relying on equity/debt issuance as a source of repayment.

3.8.1.2 Credit Assessment & Risk Grading:

3.8.1.2.1 Credit Assessment:

A thorough credit risk assessment should be conducted prior to the granting of a facility, and at least annually thereafter for all facilities. The results of this assessment should be presented in a Credit Application that originates from the relationship manager or account officer, and is reviewed by Credit Risk Management (CRM) for identification and probable mitigation of risks.

It is essential that RMs know their customers and conduct due diligence on new borrowers, principals, and guarantors to ensure such parties are in fact who they represent themselves to be. All Banks should have established Know Your Customer (KYC) and Money Laundering Guidelines which should be adhered to at all times.

Credit Applications should summarize the results of the RMs risk assessment and include, as a minimum, the following details:

- Amount and type of facility(s) proposed,
- Purpose of facilities,
- Facility structure (tenor, covenants, repayment schedule, and interest),
- Security arrangements.
- Government and regulatory policies.
- Economic risks.

In addition, the following risk areas should be addressed:

- | | |
|------------------------------------|------------------------------------|
| ✓ Borrower Analysis, | ✓ Adherence to Lending Guidelines, |
| ✓ Industry Analysis, | ✓ Mitigating Factors, |
| ✓ Supplier or Buyer Analysis, | ✓ Facility Structure, |
| ✓ Historical Financial Analysis, | ✓ Purpose of Credit, |
| ✓ Projected Financial Performance, | ✓ Project Implementation, |
| ✓ Credit Background, | ✓ Foreign Currency Fluctuation, |
| ✓ Account Conduct, | ✓ Security, |



- ✓ Type of Control on Cash Flow,
- ✓ Exit Option, and
- ✓ Name Lending.

3.8.1.2.2 Risk Grading:

The risks associated with the borrower or counter-party need to be carefully and critically analyzed before funding for the client's business. To quantify the risk exposure, it should be graded as per credit risk score sheet by the individual banks in line with the guidelines of CRG Manual. Risk grading is a key measurement of a bank's asset quality and it is a robust process. Therefore borrower's risk grade should be clearly stated on the credit application form for using credit decision making process. In CRG Manual, five risk components viz. financial risk, industry/business risk, management risk, security risk and relationship risk have been identified which are responsible for failing to meet the obligations by the borrowers. These risk components are rated based on the some basic parameters. Note that there are twenty parameters under the five risk components to reflect the risk exposure.

- a. **Financial Risk:** Financial risk comes from the financial distress of the counterparty. It includes identification of the extent of leverage through debt-equity ratio, liquidity of the borrower through current ratio, profitability performance through operating profit margin and coverage through debt-service coverage ratio.
- b. **Business/Industry Risk:** Business risk arises due to adverse change in business or industry situation. In order to assess the borrower's business/industry risk the size of the borrower's business in terms of annual sales volume, age of business, industry growth, market competition and entry & exit barriers are to be assessed.
- c. **Management Risk:** Management risk is conducted in assessing the competence and risk taking propensity of the management. It covers the parameters like experience, second line/succession plan and team work of the management.
- d. **Security Risk:** Security risk is assessed by analyzing the primary security, collateral security and support.
- e. **Relationship Risk:** Relationship risk is considered under CRG in assessing the account conduct, utilization of limit, compliance of the covenants and balance of personal deposits. There is a wide range of risk exposure or grading system in the present practices where superior is the top position and bad & loss is the worst position. In between superior and bad & loss there are six types of risk exposures say, good, acceptable, marginal or watch list, special mention, substandard and doubtful.



Grade	Description	Weighted Score	Key Indicators
1	Superior (SUP)	None	-Facilities are fully cash secured, secured by Government/international bank guarantee.
2	Good (GD)	85 +	- Repayment capacity: Strong - Liquidity: Excellent - Leverage: Low - Earnings & Cash Flow: Consistently Strong - Track record/Account conduct: Unblemished
3	Acceptable (ACCPT)	75 - 84	- Repayment capacity: Adequate. - Liquidity: Adequate - Earnings & Cash Flow: Adequate & Consistent. - Track record/Account conduct: Good
4	Marginal /Watch List (MG/WL)	65 - 74	- Repayment: Routinely fall past due - Liquidity: Strained liquidity - Leverage: Higher than normal -Earnings & Cash Flow: Thin, incurs loss and inconsistent. -Track Record/Account conduct: Poor
5	Special Mention (SM)	55 - 64	-Repayment: Deteriorate repayment prospects -Net-worth: Negative -Management: Severe problems -Leverage: Excessive -Earnings & Cash Flow: Consecutive losses
6	Substandard (SS)	45 - 54	-Repayment: Capacity and inclination to repay is in doubt. -Financial condition: Weak
7	Doubtful (DF)	35 - 44	-Repayment: Unlikely and possibility of credit loss is extremely high
8	Bad & Loss (BL)	<35	-Repayment: Long outstanding, the prospect of recovery is poor, legal action have been pursued etc.

Table 3.8.1.2.2-1: A Typical Risk Grading (Credit Rating) System under CRG Manual

Source: Bangladesh Bank (2005), Credit Risk Grading Manual, Dhaka: Bangladesh Bank, Head Office.

The uses of CRG in credit decision making is shown in the Table. From the matrix presented in the Table it is found that after conducting CRG at pre sanction stage based on client information, a banker can select three risk categories viz superior, good and acceptable as feasible and marginal may be treated as exceptionally acceptable subject to the quality of security may be offered by the client, his reputation etc. However, a borrower with special mentions, sub-standard, doubtful and bad/loss rating at pre-sanction stage will be treated as not-feasible. A borrower with superior, good and acceptable rating at post-sanction stage is a performing one. A Borrower who is beginning to demonstrate above average risk i.e. marginal or watch list or special mention at post-sanction stage will require banker's attention because it has become as an early alert (warning) account. The rest of the ratings of a borrower at the post sanction stage exhibit as non-performing or classified status.



Pre-Sanction Stage	Grading Status	Post-Sanction Stage
(1) Feasible	Superior	(1) Performing
	Good	
	Acceptable	
(2) Conditional/ Exceptionally Acceptable	Marginal/Watchlist	(2) Early Warning Account
(3) Not -Feasible	Special Mention	(3) Non-Performing
	Sub-standard	
	Doubtful	
	Bad/Loss	

Table 3.8.1.2.2-2: Decision Matrix of CRG

3.8.1.3 Approval Authority:

All commercial activities, which commit the bank to deliver risk sensitive products, require prior approval by authorized committees or individuals. A bank may have the board, management or executive committee, and credit committees for reviewing and approving financing proposals. The bank may have threshold based on the percentage of equity that sets limits for review and approval of credit proposals in different committees. The board must approve the threshold limit. Besides, approval authority may be delegated further to individual executives based on security, the executive's knowledge and experience to ensure accountability and quick decision in the approval process. The concerned CRM officials should be the owner of their independent review and identification of risks based on the credit application.

3.8.1.4 Segregation of Duties:

Adequate segregation of duties is a prerequisite for an effective system of internal control. To be adequate, segregation must ensure that the following functions are performed by persons independent of each other, although, within limits, certain may be combined so long there is adequate supervision:

- Credit Approval/Risk Management/Recovery.
- Relationship Management/Marketing.
- Credit Administration.

3.8.1.5 Internal Audit:

- The bank should have a segregated internal audit/control department charged with conducting audits of all departments.
- Internal audit should verify the continuing adequacy and applicability of credit risk management policies and procedures, provide an independent assessment of the credit portfolios' existence, quality and value, the integrity of the credit process, and promotes detection of problems relating thereto.
- Every year, internal audit should prepare an auditing plan to be approved by the Board according to which the audits are carried out. This auditing plan should be carried out in a risk-oriented manner, taking into account size and nature of the credit institution, as well as type, volume, complexity, and risk level of the Bank's activities.
- It is the task of internal auditing to monitor the swift correction of any problems detected in the audit as well as the implementation of its recommendations in a suitable form, and if necessary to schedule a follow-up audit
- Credit audit is conducted on-site, i.e. at the branch which has appraised the advance and where the main operative credit limits are made available.

3.8.2 Preferred Risk Management Structure & Responsibilities:

3.8.2.1 Preferred Risk Management Structure:

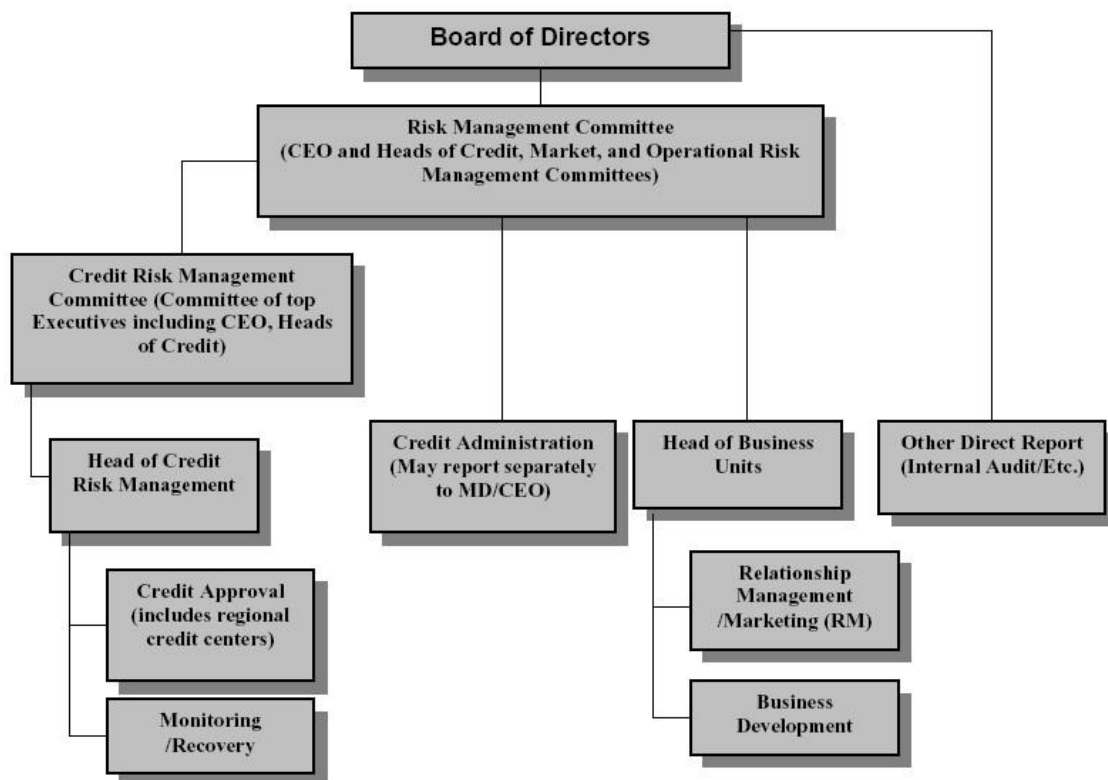


Figure 3.8.2.1: Risk Management Structure



3.8.2.2 Key Responsibilities:

The key responsibilities of the above functions are as follows. Please also refer to for sample job descriptions:

Credit Risk Management:

Risk Management Functions:

- Oversight of bank's credit policies, procedures and controls relating to all credit risks arising from corporate/commercial/institutional/personal/ treasury operations
- Oversight of the bank's asset quality.
- To ensure that lending executives have adequate experience and/or training in order to carry out job duties effectively.

Credit Functions:

- To review Credit Applications recommended by RM and to provide independent risk assessment and recommendation to MD/CEO/Board for approval.
- To provide advice/assistance regarding all credit matters to line management/RMs.

Monitoring Functions:

Directly manage all Substandard, Doubtful & Bad and Loss accounts to maximize recovery and ensure that appropriate and timely facility loss provisions have been made.

Credit Administration:

- To ensure that all security documentation complies with the terms of approval and is enforceable.
- To monitor insurance coverage to ensure appropriate coverage is in place over assets pledged as collateral, and is properly assigned to the bank.
- To control facility disbursements only after all terms and conditions of approval have been met, and all security documentation is in place.
- To maintain control over all security documentation.
- To monitor borrower's compliance with covenants and agreed terms and conditions, and general monitoring of account conduct/performance.

Relationship Management/Marketing:

- To act as the primary bank contact with borrowers
- To maintain thorough knowledge of the borrower's business and industry through regular contact, factory/warehouse inspections, etc. RMs should proactively monitor the financial performance and account the conduct of borrowers.



- To be responsible for the timely and accurate submission of Credit Applications for new proposals and annual reviews, taking into account the credit assessment requirements
- To highlight any deterioration in borrower's financial standing and amend the borrower's Risk Grade in a timely manner. Changes in Risk Grades should be advised to and approved by CRM.
- To seek assistance/advice at the earliest from CRM regarding the structuring of facilities, potential deterioration in accounts or for any credit related issues.

Internal Audit/Control:

Conducts independent inspections annually to ensure compliance with Lending Guidelines, operating procedures, bank policies and Bangladesh Bank directives. Reports directly to MD/CEO or Audit committee of the Board.

3.8.3 Procedural Guidelines:

3.8.3.1 Approval Process:

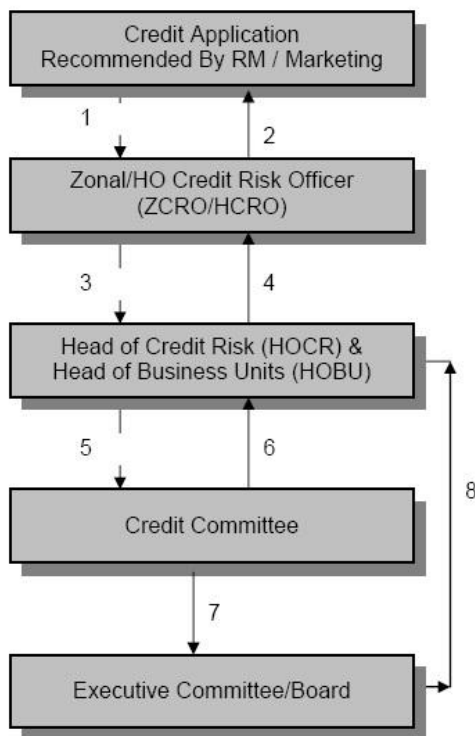


Figure 3.8.3.1: Credit Approval Process

1. Application forwarded to Zonal Office or Head Office for review by the ZCRO or HCRO.
2. Advise the review to recommending branches.
3. ZCRO/HCRO supports & forwarded to the Head of Business Units (HOB) within their delegated authority and to Head of Credit Risk (HOCR) for onward recommendation.
4. HOCR advises the review to ZCRO.



5. HOCR & HOBUS supports & forwarded to Credit Committee.
6. Credit Committee advises the decision as per delegated authority to HOCR & HOBUS.
7. Credit Committee forwards the proposal to the EC / Board for their approval within their respective authority.
8. The EC / Board advises the decision to HOCR & HOBUS.

3.8.3.2 Credit Administration:

The Credit Administration function is critical in ensuring that proper documentation and approvals are in place prior to the disbursement of financial facilities. For this reason, it is essential that the functions of Credit Administration be strictly segregated from Relationship Management/Marketing in order to avoid the possibility of controls being compromised or issues not been highlighted at the appropriate level.

Ongoing administration of the credit portfolio is an essential part of the credit process. Credit administration function is basically a back office activity that support and control extension and maintenance of credit. A typical credit administration unit performs following functions:

- ✓ Documentation,
- ✓ Disbursement,
- ✓ Credit Monitoring,
- ✓ Facility Repayment,
- ✓ Custodial Duties,
- ✓ Compliance Requirements.

3.8.3.3 Credit Monitoring

To minimize credit losses, monitoring procedures and systems should be in place that provide an early indication of the deteriorating financial health of a borrower. At a minimum, systems should be in place to report the following exceptions to relevant executives in the CRM and RM team:

- Past due principal or interest payments, past due trade bills, account excesses, and breach of facility covenants.
- Non-receipts of financial statements on a regular basis and any covenant breaches or exceptions made.
- Action not taken on time for findings of any internal, external or regulator inspection/audit.

All borrower relationships/facilities are reviewed and approved through the submission of a Credit Report at least annually. Refer to the Credit Report format attached as Computer systems must be able to produce the above information for central/head office as well as local review. Where automated systems are not available, a manual process should have the capability to produce accurate exception



reports. Exceptions should be followed up and corrective action taken in a timely manner before the account deteriorates further.

3.8.3.4 Credit Recovery:

The Recovery Unit (RU) of CRM should directly manage accounts with sustained deterioration (a Risk Rating of Sub Standard (6) or worse). Banks may wish to transfer EXIT accounts graded 4-5 to the RU for efficient exit based on the recommendation of CRM and Corporate bank. Whenever an account is handed over from Relationship Management to RU, a Handover/Downgrade Checklist should be completed.

The RU's primary functions are:

- Determine Account Action Plan/Recovery Strategy
- Pursue all options to maximize recovery, including placing customers into receivership or liquidation as appropriate
- Ensure adequate and timely loan loss provisions are made based on actual and expected losses
- Regular review of grade 6 or worse accounts

The management of problem facilities (NPLs) must be a dynamic process, and the associated strategy together with the adequacy of provisions must be regularly reviewed. A process should be established to share the lessons learned from the experience of credit losses in order to update the lending guidelines.

3.9 The Investment (Credit) Risk Process:

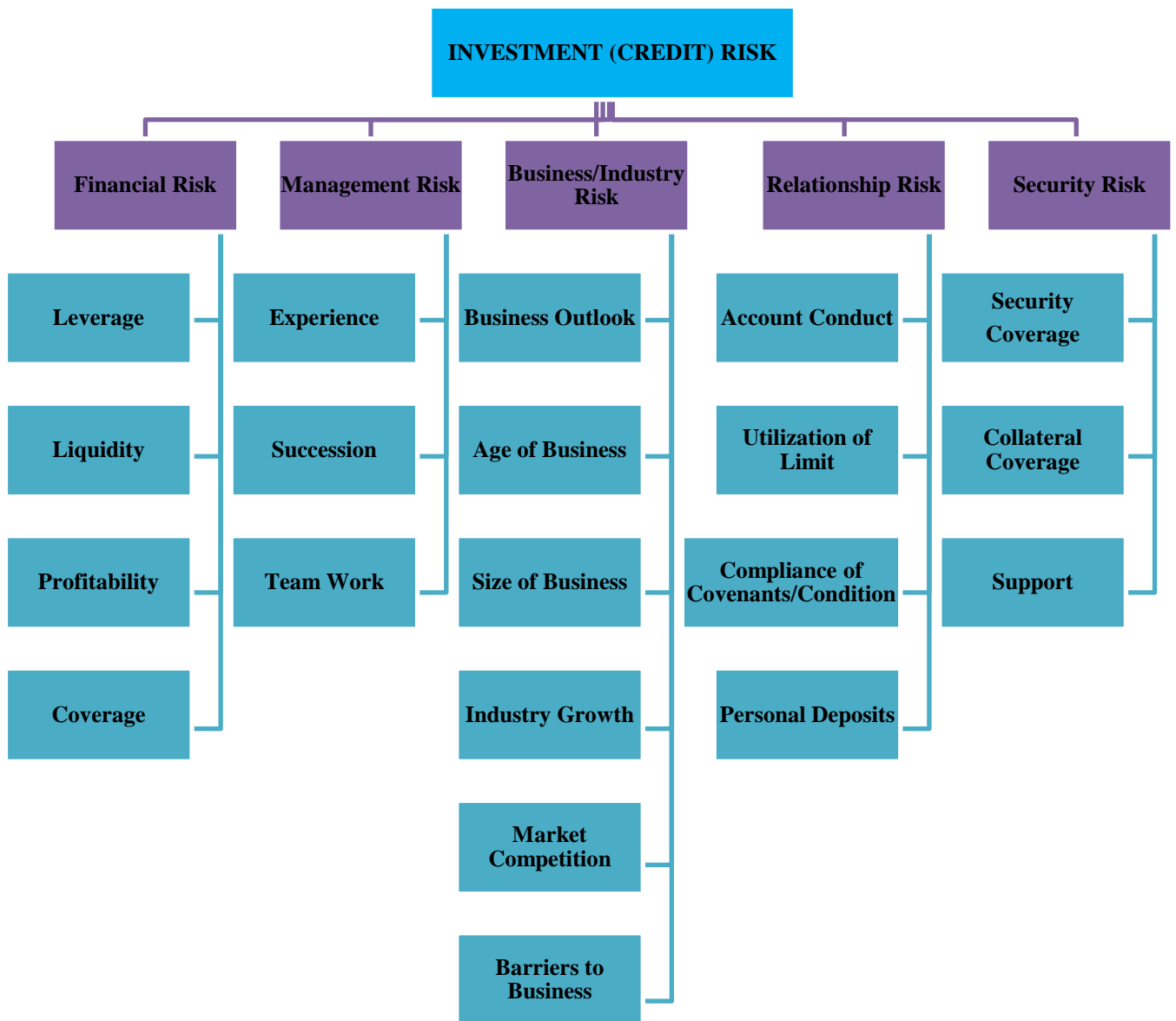


Figure 3.9: The Investment (Credit) Risk Process

3.10 Principles of Sound Investment Criteria:

It should be clearly understood that the principles are not inflexible laws & are given as guidelines for protecting credit. In a practical competitive world, risks are defined, accepted and credit is often granted even though a person does not strictly with some of the criteria described below. The basic investment criteria can be considered as eight main headings as follows:

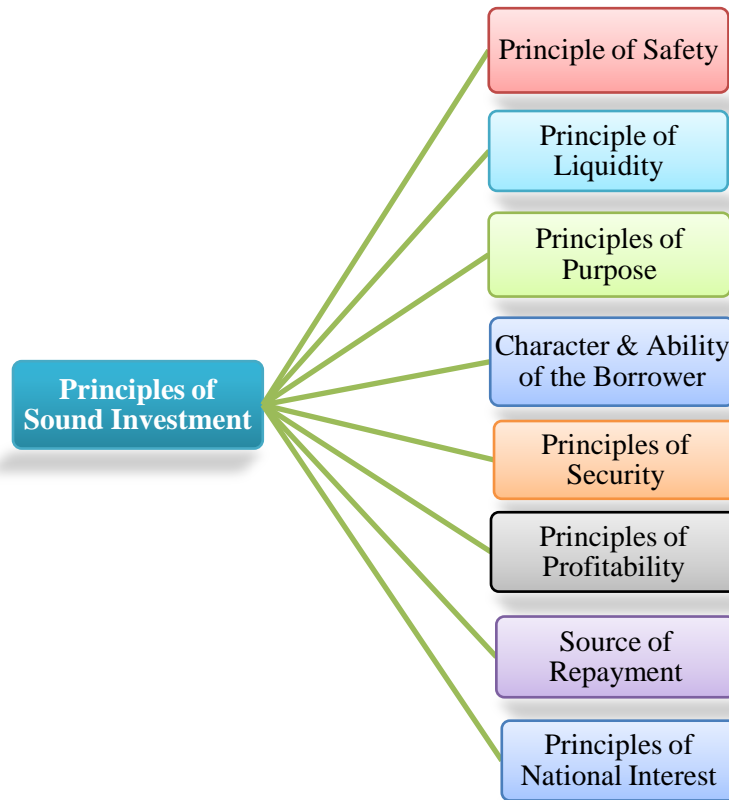


Figure 3.10: Principles of Sound Investment

- ❖ **Principles of Safety:** The first lending principle is safety. The very existence of a bank depends upon the safety of its advances. Safety should not be sacrificed for profitability. So utmost care should be exercised to ensure that the funds go to the right type of borrower, are utilized in such a way that they remain safe and the repayment comes in the normal course.
- ❖ **Principle of Liquidity:** Liquidity means the availability of bank funds on short notice. The liquidity of an advance means its repayment on demand on due date or after a short notice. Therefore, the banks must have to maintain sufficient liquidity to repay its depositors and tradeoff between the liquidity and profitability is must.
- ❖ **Principles of Purpose:** The bank should not invest money for any purposes for which a borrower may be free from all risks but if the funds borrower are employed for unproductive. Purpose like a



marriage ceremony, pleasure trip etc. or speculative activities, the repayment in the normal course will become uncertain.

- ❖ **Character & Ability of the Borrower:** The primary responsibility of the leading banker is “**know your customer and his business**”. While considering the character and of a borrower, the following point must be kept in mind.

- Do know your customer already?
- Was he respectively introduced?
- If he was previously a customer of another bank, why has he come to Islami Bank Bangladesh Limited, Try to previous bank statement?
- Have you made the account opening inquires required by the bank?
- What is the business its ownership?
- What are the customer’s background and financial track record?
- Customer’s honesty & integrity and personal stability?
- How has the customer managed his financial circumstances in the past?

The branch manager should have the answer of the above queries and should be to judge his ability to use the investment facilities to his advantage. The advance should be granted only to those borrowers in whom the branch manager has full confidence.

- ❖ **Principle of Security:** The security offered by a borrower for an advance is insurance to the banker. It serves as the safety value for an unforeseen emergency. So another principle of sound investment is the security of investment. The security accepted by a banker to cover a bank advance must be adequate, readily marketable, easy to handle and free from any encumbrance.
- ❖ **Principle of Profitability:** Banking is essentially a business, which aims at earning of a good profit. The working funds of a bank are collected mainly by means of deposit from the public and interest has to be paid on those deposits.
- ❖ **Sources of Repayment:** After the branch manager has ensured that the investment will be a profitable propositioning for the bank, he should then turn his attention to the cash flow situation of the borrower.
- ❖ **Principle of National Interest:** The above development of banking has reached a stage where a banker is required to identify his business with national policies. Banking Industry has a significant role to play in the economic development of a country. So, the savings of the people which are mobilized by banks must be distributed to those sectors which require development in the country’s planning program.

Part Four

Investment Risk Management of IBBL





4.1 Core Risk Management Committees of IBBL:

IBBL exclusively manages six core risks and has designed its own Risk Management Guidelines in accordance with the guidelines prescribed by the Central Bank and formed six core risk management committees which conduct a meeting periodically. The major concerns of the committees are as under:

- ❑ **Investment Risk Management Committee** supervises and monitors investment concentration, investment risk grading, corporate clients rating, non-performing investment, residual risk against investment, provision against classified investment, investment mix, asset quality etc.
- ❑ **Foreign Exchange Risk Management Committee** oversees foreign exchange risk, treasury, net open position, import & export business, dealing room operations and anti-money laundering aspects in foreign exchange transactions etc.
- ❑ **Information & Communication Technology Risk Management Committee** monitors and supervises the risks related to data security, physical security, network security, disaster recovery, fraud, forgery, system failure and business continuity etc.
- ❑ **Anti Money Laundering Risk Management Committee** looks after the money laundering activities, STR, CTR, KYC and TP related compliances. The Committee also supervises and monitors the entire transactional activities of the Bank including money laundering aspects involved with foreign exchange transactions.
- ❑ **Internal Control and Compliance Risk Management Committee** assesses and mitigates the risk related to compliance with regulatory requirements, set rules of the Bank, internal checking system, lapses, fraud, forgeries, violations of the set rules etc.
- ❑ **Asset Liability Committee (ALCO)** looks after the asset-liability risk, liquidity risk, Investment Deposit Ratio (IDR), deposit mix, investment mix, gap analysis etc. under direct guidance of the Managing Director.

4.2 Investment Risk Faced by IBBL:

Investment Risk is one of the major risks faced by the bank. This can be described as potential losses arising from the failure of counterparty to perform according to agreement with the bank. The failure may result from the unwillingness of the counterparty or decline in his/her economic condition, market situation etc. With each and every coin of investment, there is an involvement of risk. In abroad sense, credit risk includes:

- ❑ **Investment Default Risk:** The risk of loss when the bank considers that the obligor is unlikely to pay its investment obligations in full or the obligor is more than 90 days past due on any material investment obligation;



- ❑ **Concentration Risk:** The risk associated with any single exposure or a set of exposures with the potential to produce large enough losses to threaten a bank's core operations. It may arise in the form of single name concentration or industry concentration.
- ❑ **Country Risk:** The risk of loss arising when a sovereign state freezes foreign currency payments (transfer/conversion risk) or when it defaults on its obligations (sovereign risk). Political unrest, degradation of internal law and order are also included in country risk. In such situation, both entrepreneurs and the banks are discouraged in investment activities.
- ❑ **Environment Risk:** The risk of environmental calamities which arise while banks deploy its fund to industry, trade and service sector.

In this context, Investment Risk Management Committee (IRMC) of the bank is entrusted with the duties of maintaining asset quality, assessing risk in investment to a particular customer, appraising, sanctioning investment, formulating policy/strategy for investment operations, sectoral assessment, salvaging sick units, nursing the running units, diversification of its investment portfolio, consideration of environment impacts while financing etc. The Investment Risk Management Committee is also entrusted to comply with the CRM Guidelines, monitoring & updating the bank's investment policy. Moreover, the committee analyzes the investment portfolio on the basis of Basel Guideline and attempts to restructure the investment portfolio.

4.3 Basel Guidelines and its Compliance:

IBBL has constituted Stress Testing Committee and Assessment of Capital under Basel II Accord Committee to look after the Stress Testing & Basel-II related risk issues. Addressing the Investment Risk, Market Risk, Operational Risk and other risks associated with the banking operations, IBBL has been linking its risk profile with the capital which is the major risk absorbing tool. Currently the capital adequacy of IBBL is 13.49% wherein the industry average is only 10.46%.

IBBL is committed to continuous improvement of bank's internal procedure for assessing the specific risk situation, ongoing adjustment and further development of new methods of risk management and internal control, covering external factors and risk areas which are not taken into account or partially taken into account while calculating Minimum Capital Requirements, quantifying the risks under pillar 2 of Basel-II, stress testing, Internal Capital Adequacy Assessment Process (ICAAP), setting capital targets that are commensurate with the Bank's risk profile and control environment etc. For adequate supervision of capital functions and risks, Bank has formed a Supervisory Review Process Team (SRPT) as stipulated in Bangladesh Bank's guidelines.



4.4 Investment and Investment Risk Management Policies of IBBL:

Investment and investment risk management policy of Islamic banks and non Islamic banks are fully different. The policies followed by the IBBL are,

- To observe strictly the principles of Islamic Shariah in investment operations.
- To give emphasize on national priority sectors.
- To diversify the investment portfolio by size, sector, geographical area, economic purpose, securities and modes of investment to minimize risk as well as to achieve the goals of Islamic Banking.
- To give preference to invest in SME, Real Estate, Retail, Consumer and other special schemes including Rural Development Scheme for income and employment generation.
- To give preference to short-term investment to long-term investment in maintaining a balanced portfolio.
- To expand investment operations beyond the niche market by including new clients from all sectors.
- To ensure optimum utilization of the bank's investible fund.
- To look into the profitability of investments.
- To induct best of the best clients of the market.
- To encourage investment where the risk weight is less.
- To ensure safety and security of investments.
- To keep investment pricing competitive.
- To keep non-performing investment at the lowest possible level.
- To balance maturity of investment with the maturity of deposit to avert liquidity risk.
- To explore the possibility of investment in the existing Money and Capital Market and help organization of Islamic Money and Capital Market.

4.5 Investment Products of IBBL:

Islamic banks do not directly deal with money. They run business with money. The funds of Islamic banks are mainly invested in the following modes:

- | | |
|-----------------------------------|--|
| i. Mudaraba; | viii. IjarahMuntahiaBittamleek (Hire |
| ii. Musharaka; | Purchase); |
| iii. Bai-Murabaha; | ix. Hire Purchase MusharakaMutanaqisa; |
| iv. Bai-Muajjal; | x. Direct Investment; |
| v. Salam and Parallel Salam; | xi. Investment Auctioning etc. |
| vi. Istisna and parallel Istisna; | xii. Quard |
| vii. Ijara; | xiii. Quard Hassan etc. |

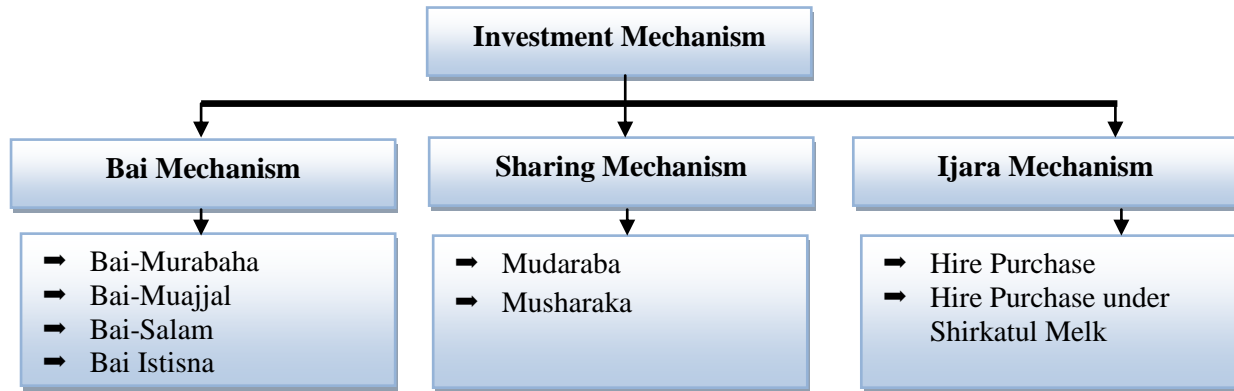


Figure 4.5 Investment Mechanisms of IBBL

- i. **Mudaraba:** Mudaraba is a shared venture between labor and capital. Here Bank provides with entire capital and the investment client conducts the business. The Bank, provider of capital, is called Sahib-Al-Maal and the client is called Mudarib. The profit is to be distributed between the bank and the investment client at a predetermined ratio while the bank has to bear the entire loss, if any.
- ii. **Musharaka:** Musharaka means partnership business. Every partner has to provide more or less equity funds in this partnership business. Both the bank and the investment client reserve the right to share in the management of the business. But the bank may opt to permit the investment client to operate the whole business. In practice, the investment client normally conducts the business. The profit is divided between the bank and the investment client at a predetermined ratio. The loss, if any, is to be borne by the bank and the investment client according to capital ratio.
- iii. **Bai-Murabaha:** Contractual buying and selling at a mark-up profit is called Murabaha. In this case, the client requests the bank to purchase certain goods for him. The bank purchases the goods as per specification and requirement of the client. The client receives the goods on payment of the price which includes mark-up profit as per contract. Under this mode of investment the purchase/ cost price and profit are to be disclosed separately.
- iv. **Bai-Muajjal:** "Bai-Muajjal" means sale for which payment is made at a future fixed date or within a fixed period. In short, it is a sale on Credit. It is a contract between a buyer and a seller under which the seller sells certain specific goods (permissible under Shariah and Law of the Country), to the buyer at an agreed fixed price payable at a certain fixed future date in a lump sum or within a fixed period by fixed installments. The seller may also sell the goods purchased by him as per order and specification of the buyer. In bank's perspective, Bai-Muajjal is treated as a contract between the bank and the client under which the bank sells the client certain specified goods, purchased as per order and specification of the client at an agreed price payable within a fixed future date in a lump sum or by fixed installments.



- v. **Salam and Parallel Salam:** Salam means advance purchase. It is a mode of business under which the buyer pays the price of the goods in advance on the condition that the goods would be supplied / delivered at a particular future time. The seller supplies the goods within the fixed time.

Parallel Salam: Parallel Salam is a Salam contract whereby the seller depends, for executing his obligation, on receiving what is due to him - in his capacity as purchaser from a sale in a previous Salam contract, without making the execution of the second Salam contract dependent on the execution of the first one.

The following conditions are essential in the contracts of Murabaha, Bai-Muajjal and Salam. The respective contracts must include the following aspects regarding the goods:

- | | |
|-------------------------------|---|
| ➤ Number/Quantity, | ➤ Place of supply, |
| ➤ Quality, | ➤ Who will bear the cost of supply?, |
| ➤ Sample, | ➤ Timeframe for payment in case of Bai- |
| ➤ Price and amount of profit, | Murabaha and Bai-Muajjal. |
| ➤ Date of supply/time limit, | |

- vi. **Istisna and Parallel Istisna:** A contract executed between a buyer and a seller under which the seller pledges to manufacture and supply certain goods according to the specification of the buyer is called Istisna. An Istisna agreement is executed when a manufacturer or a factory owner accepts a proposal placed to him by a person or an Institution to produce/manufacture certain goods for the latter at a certain negotiated price. Here, the person giving the order is called Mustasni, the receiver of the order is called Sani and the goods manufactured as per order is called Masnu. An order placed for manufacturing or producing those goods which under prevailing customs and practice are produced or manufactured will be treated as Istisna contract.

Parallel Istisna: If it is not stipulated in the contract that the seller himself would reduce/provide the goods or services, then the seller can enter into another contract with a third party for getting the goods or services produced/ provided by the third party. Such a contract is called Parallel Istisna.

- vii. **Ijara:** The mode under which any asset owned by the bank, by creation, acquirement or building-up is rented out is called Ijara or leasing. In this mode, the leasee pays the bank rents at a determined rate for using the assets/properties and returns the same to the bank at the expiry of the agreement. The bank retains absolute ownership of the assets/properties in such a case. However, at the end of the leased period, the asset may be sold to the client at an agreed price.



- viii. **IjarahMuntahiaBittamleak (Hire-Purchase):** Under this mode, the bank purchases vehicles, machineries and instruments, building, apartment etc. and allowed clients to use those on payment of fixed rents in installments with the ultimate objective to sell the asset to the client at the end of the rental period . The client acquires the ownership/ title of the assets/ properties subject to full payment/ adjustment of all the installments.
- ix. **Hire-purchase MusharakaMutanaqasa (HPMM):** Hire-purchase MusharakaMutanaqasa means purchasing and acquiring ownership by one party by sharing in equity and paying rent for the rest of the equity held by the bank/or other party. Under this mode, the bank and the client on a contract basis jointly purchase vehicles, machineries, building, apartment etc. The client uses the portion of the assets owned by the bank on rental basis and acquires the ownership of the same assets by way of paying bank's portion of the equity on the assets in installments together with its rents as agreed upon.
- x. **Direct Investment:** Under this mode, the bank can under its full proprietorship conduct business by directly investing in the industries, trading, transports etc. In these cases, the profit/loss fully goes to the bank.
- xi. **Investment Auctioning:** Selling by auction of those assets/goods acquired by the bank through direct investment is called investment auctioning. Generally, the bank establishes industrial units by direct investment, makes the same operation profitable and then sells out on the auction. This mode of investment is very helpful for industrialization of the country.
- xii. **Quard:**It is a mode to provide financial assistance/ loan with the stipulation to return the principal amount in the future without any increase thereon.
- xiii. **Quard Hassan:**This is a benevolent loan that obliges a borrower to repay the lender the principal amount borrowed on maturity. The borrower, however, has the discretion to reward the lender for his loan by paying any amount over and above the amount of the principal provided there will be no reference (explicit or implicit) in this regard. If a bank provides its client any loan, it can receive an actual expenditure relating to the loan as service charge only once. It cannot charge annually at a percentage rate. If a loan is provided against the money deposited by a client in the bank, it has the right not to pay any profit against the amount of money given as a loan. But profit should be paid on the rest of the amount deposited as per previous agreement.



4.6 Welfare-oriented Investment Schemes:

In addition to the normal commercial and industrial investment operations, IBBL has 14 Special Investment Schemes targeting different economic groups. The schemes are implemented and expanded to meet the specific and welfare oriented needs of different groups of people particularly the under-privileged downtrodden and the neglected section of the population of the country. To uplift the lifestyle of these people, some welfare-oriented special investment schemes as under have been undertaken:

- ❑ **Household Durable Investment Scheme:** Low-income people involved in diverse professions get benefit out of this scheme. They are provided with household products like refrigerator, TV, motor-cycle, furniture, ornaments, computer etc. under this financing scheme.
- ❑ **Housing Investment Scheme:** The bank has introduced this scheme to ease the serious housing problem in the urban areas and to make arrangement for comfortable accommodation of the fixed income group such as: officials of the defense services, permanent officials of government, semi-government and autonomous organizations, faculty members of the established universities, university colleges & medical colleges, graduate engineers, doctors and established professionals, international financial organizations, donor agencies, foreign embassies etc., officials of reputed local public limited companies.
- ❑ **Real Estate Investment Scheme:** Real Estate Finance plays a pivotal role in improving standard of living, empowering the middle-income and lower-income groups and thereby promoting equitable growth in the society. It does not only provide physical shelter but also upgrade the lives of the dwellers in terms of skills enhancement, income generation, increased security, health, self-confidence and human dignity. IBBL has steady growth in the Real Estate Sector.
- ❑ **Transport Investment Scheme:** To ease the existing transportation problem and to accelerate the pace of economic growth and development of the country, particularly through expansion of trade, commerce and industry, the bank has taken up this scheme.
- ❑ **Car Investment Scheme:** To enable officials, business houses and business executives and professionals to move by transports in discharging their responsibilities punctually, IBBL has introduced Car Investment Scheme for the mid and high ranking officials of the government and semi-government organizations, corporations, executives and directors of big business houses and companies and also for persons of different professional groups on easy payment terms and conditions.



- ❑ **Investment Scheme for Doctors:** The scheme is meant for fresh medical graduates intending to meet up medical centers. IBBL comes forward to their aid to help them procure medical equipment or to set up diagnostic laboratory, pharmacy, clinic etc.
- ❑ **Small Business Investment Scheme:** Small business persons and entrepreneurs of different cities and villages get investment facilities from this scheme which is contributing greatly to generate income and employment and to develop standard of life of different segments of low income people. This bank provides different types of agricultural instruments, equipment for operating small trade and finance, small shop, light transport, photocopy machine, tailoring machine, machinery for small and cottage industry etc. under this scheme.
- ❑ **Agricultural Implements Investment Scheme:** Keeping the view of the people-orientation and welfare objectives of the Bank, this scheme has been introduced to provide powers tillers, power pumps, shallow tube-wells, thresher machines etc. on easy terms to the unemployed rural youths for self-employment and to farmers to help them augment production in the agriculture sector.
- ❑ **Micro-Industries Investment Scheme:** To create a wider base for industries and to encourage the establishment of micro-industries in different areas of the country by the potential entrepreneurs and to diversify the Bank's investment portfolio, the bank has introduced 'Micro Industries investment Scheme'. Different sectors including food and agriculture based industries, plastic & rubber industries, forestry and furniture industries, engineering industries, service industries, electrical accessories industries, computer technology industries, paper products industries, handicraft industries, fishery & livestock farming, hollow bricks, roof tiles and any other viable micro-industries have been identified for financing under the scheme.
- ❑ **Rural Housing Investment Scheme:** This scheme was launched to extend housing facility to the rural people living within 5 kilometers area of an IBBL branch. Employees of the public, semipublic or autonomous institutions, non-resident Bangladeshis and businesspersons are preferred for this investment. Easy term investment is given for constructing new houses, repair of old houses and purchasing ready-made flats and houses etc.
- ❑ **Women Entrepreneurs Scheme:** IBBL has introduced "Women Entrepreneurs Investment Scheme" to help women contribute to GDP, generate income & employment and to develop their socioeconomic condition. Under this scheme Bangladeshi nationals aged between 18-50 years, genuine women entrepreneurs, women already engaged in business, self-employment activities as owners, skilled and semi-skilled female persons having practical experience in the respective field may apply for investment.



- ❑ **NRB Investment Scheme:** For promoting investment among non-resident Bangladeshis and for encouraging them to remit money through banking channel, IBBL has launched NRB Entrepreneurs Scheme. Expatriates aged between 18 to 60 years or their family members who run account with IBBL for remitting money are eligible for this investment.

4.7 Investment Risk Treatment with Different Financing Modes by IBBL:

Islamic Modes of Finance (Areas of Potential Risk)	Risk Mitigation or Preventive Techniques
Murabaha: Where the bank makes prompt delivery of assets but the client fails to make timely payment. The bank is in no position to take effective measures to cover its dues nor can it charge profit (interest) or impose a penalty on the outstanding balance.	Maintaining comprehensive database and reference checklist on the character and past performance of potential business partners to evaluate their personal and business attributes and to “determine the probability of default”.
Mudaraba: The bank as a silent partner has no means to monitor the investment or to participate in the management of the project. The bank is exposed to total loss of its investment (the amount advanced to the entrepreneur).	Using collateral as security against credit risk and accepting personal and institutional guarantees to minimize credit risk.
Musharaka: In case of proven negligence or wrongdoing by the business partner (the entrepreneur), the bank is entitled to recover its investment. However, the recovery process is not transparent since the rules of debt recovery rather than the rules of musharakah contracts are applied. As a PLS contract, both Mudaraba and Musharaka partnership arrangements are subject to loss of invested capital due to business losses.	Utilizing reliable monitoring measures. Being actively involved in the business venture throughout its various stages.

4.8 Investment Processing of Islami Bank Bangladesh Limited:

Generally a bank takes certain steps to deliver its proposed investment to the client. But the process takes deep analysis. Because banks invest depositors fund, not banks' own fund. If the bank fails to meet depositors demand, then it must collapse. So, each bank should take strong concentration on investment proposal. However, Islami Bank Bangladesh Limited makes its investment decision through successfully passing the following crucial steps:

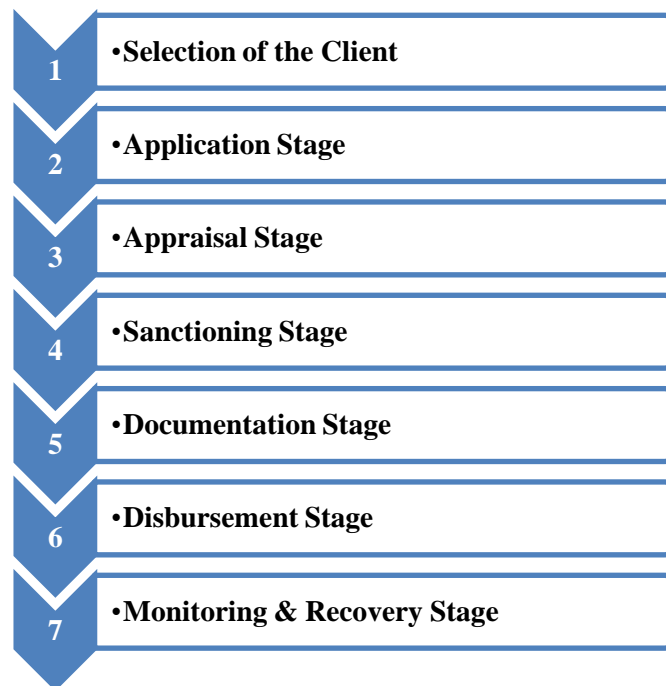


Figure 4.8: Process of Investment in IBBL

Source: Investment Department of IBBL, Mohakhali Branch

4.8.1 Selection of the Client:

In this stage investment taker (client) approaches to any of the branches of Islami Bank Bangladesh Limited. Then, he talks with the manager or respective officer (investment). Secondly, the bank considers five C's of the client. After successful completion of the discussion between the client and the bank, bank selects the client for its proposed investment. It is to be noted that the client/customer must agree with the bank's rules & regulations before availing investment. Generally, bank analyses the following five C's of the client:

- Character;
- Capacity;
- Capital;
- Collateral; and
- Condition.

Further the bank analyses the client by the following standard of measures,

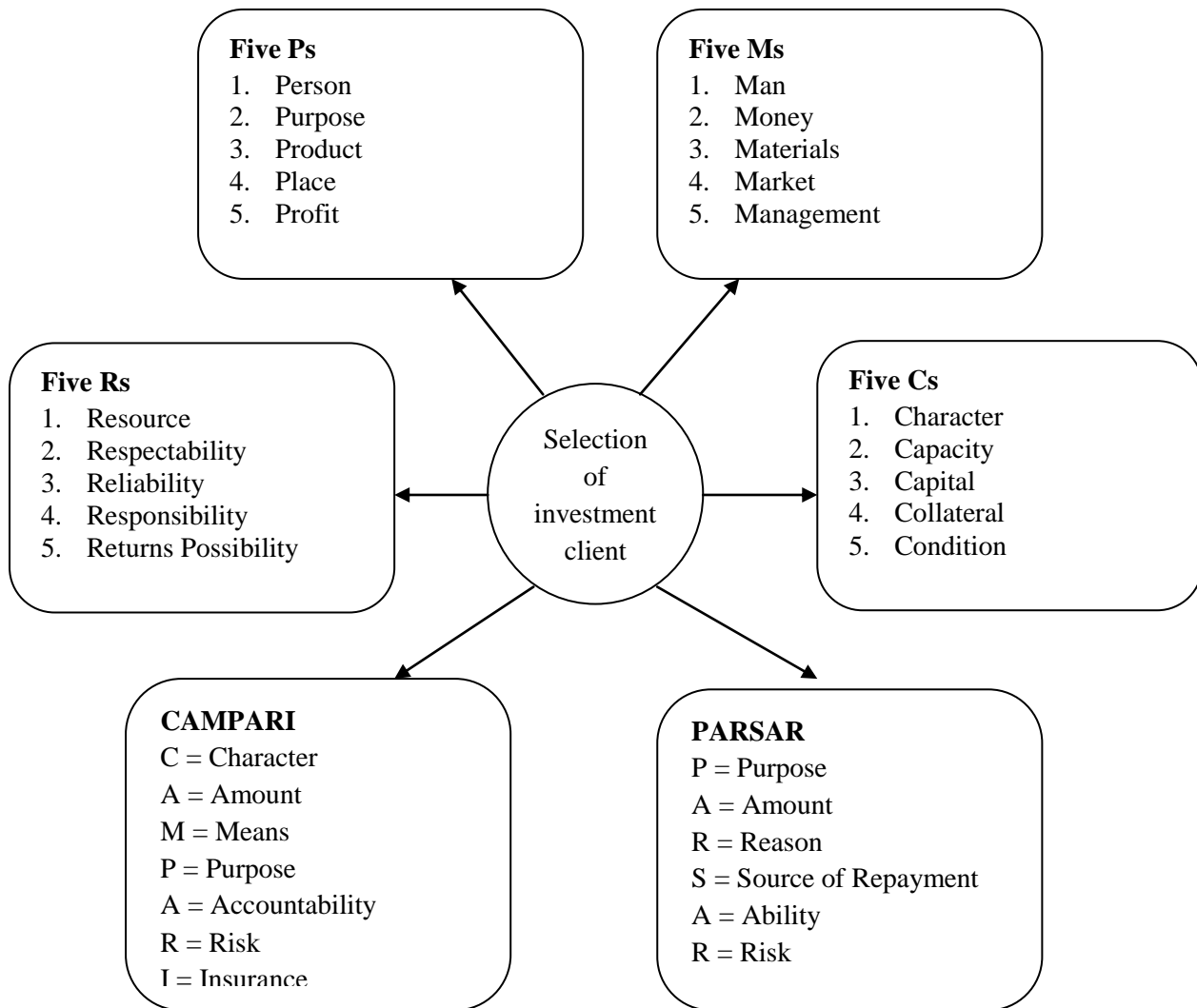


Figure 4.8.1: Selection of Investment Client Mechanisms

4.8.2 Application Stage:

At this stage, the bank will collect necessary information about the prospective client. For this reason, the bank informs the prospective client to provide and/or fill duly respective information which is crucial for the initiation of investment proposal. Generally, here, all the required documents for taking investment have to prepare by the client himself. Documents that are necessary for getting investment of IBBL are prescribed below:

- ✓ Trade License photocopy (for proprietorship);
- ✓ Abridged pro forma income statement;
- ✓ Attested copy of partnership deed (for partnership business);
- ✓ Prior three (03) years' audited balance sheet (for joint stock company);
- ✓ Prior three (03) years' business transaction statement for the Musharaka/Mudaraba investment;



- ✓ Abridged pro forma income statement for the Musharaka/Mudaraba investment;
- ✓ Attested copy of the Memorandum of Association (MOA) & Articles of Association (AOA) for the joint stock company;
- ✓ Attested copy of the Tax Identification Number (TIN) - including final assessment;
- ✓ Tenders of the proposed assets (in case of HPSM);
- ✓ Detailed summary of the sundry debtors and creditors (including both times & schedule);
- ✓ Summary of the personal movable & immovable assets; and others.

4.8.3 Appraisal Stage:

At this stage, the bank evaluates the client and his/her business. It is the most important stage. Because on the basis of this stage, the bank usually goes for sanctioning the proposed investment limit/proposal. If anything goes wrong here, the bank suddenly stops to make payment of investment.

In order to appraise the client, Islami Bank Bangladesh Limited provides a standard F-167B Form (Appraisal Report) to the client for gathering all the information. The original copy of the appraisal report is enclosed in the appendix chapter. However, the following contents are presented from that appraisal report:

- | | |
|--|--|
| ▪ Company's/Client's Information. | ▪ Relationship Analysis. |
| ▪ Owner's Information. | ▪ Asset-Liability position of the client as per Audited Balance Sheet. |
| ▪ List of Partners/Directors. | ▪ Working Capital Assessment. |
| ▪ Purpose of Investment/Facilities. | ▪ Risk Grade. |
| ▪ Details of Proposed Facilities/Investment. | ▪ Particulars of the storehouse for storing MPI/Murabaha goods. |
| ▪ Break up of Present Outstanding. | ▪ Insurance Coverage. |
| ▪ Other Liabilities of the Client/Group. | ▪ Audit Observation. |
| ▪ Previous Banker's Information. | ▪ Security Analysis. |
| ▪ Details of Sister/Allied Concerns. | |
| ▪ Allied Deposit as on. | |
| ▪ Business/Industry Analysis. | |

4.8.4 Sanctioning Stage:

At this stage, the bank officially approves the investment proposal of the respective client. In this case client receives the bank's sanction letter. Islami Bank Bangladesh Limited's sanction letter contains the following elements:

- | | |
|--------------------------------|-------------------------|
| ▪ Investment limit in million. | ▪ Period of investment. |
| ▪ Mode & amount of investment. | ▪ Rate of return. |
| ▪ Purpose of investment. | ▪ Securities. |



Cash/Goods Security:

In allowing Murabaha investment and the amount of cash security is generally realized from the client (amount depends on the nature of goods, creditworthiness of the client, collateral security obtained etc.) which is converted to goods security after the purchase of goods purchased out of the bank's investment and client's cash security is pledged to the bank, kept under bank's custody before its delivery to the client for payment. Example: If, for a Murabaha investment cash security is fixed at 25% Bank's investment stands at 75% of the total goods purchased. For example, if cost of total goods purchased is Tk.100000 Bank's investment will be Tk.75000 and client's cash security will be Tk.25000.

Bank	Client	Total Cost of Goods
Tk. 75,000 (75%)	Tk. 25,000 (25%)	Tk. 100,000 (100%)

4.8.5 Documentation Stage:

At this stage, usually the bank analyses whether required documents are in order. In the documentation stage, Islami Bank Bangladesh Limited checks the following documents of the client:

- i. Tax Payment Certificate.
- ii. Stock Report.
- iii. Trade License (renewal).
- iv. VAT certificate
- v. Liability statement from different parties.
- vi. Receivable from different clients.
- vii. Other assets statement.
- viii. AungkyarNama.
- ix. GhosonaPotra.
- x. Three (03) years net income & business transactions.
- xi. Performance report with the bank.
- xii. Account Statement Form of the bank.
- xiii. Valuation Certificate;
 - a. Particulars of the Proposal.
 - b. Particulars of the Mortgagor.
 - c. Particulars of the Properties.
- xiv. Outstanding liability position of the bank.
- xv. CIB (Credit Information Bureau) Report.



4.8.6 Disbursement Stage:

At this stage, the bank decides to pay out money. Here, the client gets his/her desired fund or goods. It is to be noted that before disbursement a “site plan” showing the exact location of each mortgage property needs to be physically verified.

4.8.7 Monitoring & Recovery Stage:

At this final stage of investment processing of the Islami Bank Bangladesh Limited. The bank will contact with the client continually, for example- the bank can obtain a monthly stock report from the client in case of micro investment. Here, the bank will keep his eye on over the investment taker. If needed, the bank will physically verify the client’s operations. Also if the bank feels that anything is going wrong then it tries to recover its investment fund from the client.

4.9 Credit Risk Grading followed by IBBL:

Bangladesh Bank instructed all commercial Banks to develop its own credit risk grading system build its Guidelines on Credit Risk Management. In the said Guideline, Bangladesh Bank provided a sample Risk Grading Model and advised Banks to design their own model in line with that one.

Credit Risk Grading:

IBBL adopts a credit risk grading system. The system defines the risk profile of borrower's to ensure that account management, structure and pricing are commensurate with the risk involved. Risk grading is a key measurement of a Bank's asset quality, and as such, it is essential that grading is a robust process. All facilities are assigned a risk grade. Where deterioration in risk is noted, the Risk Grade assigned to a borrower and its facilities are immediately changed. Borrower Risk Grades are clearly stated in Credit Applications.

The following Risk Grade Matrix is followed by IBBL which is provided by Bangladesh bank Lending Guidelines. With it, IBBL also follows the Risk Grade Scorecard. The more conservative risk grade (higher) is applied if there" is a difference between the personal judgment and the Risk Grade Scorecard results. It is recognized that the banks may have more or less Risk Grades; however, monitoring standards and account management are appropriate given the assigned Risk Grade:

Risk Rating	Grade	Definition
Superior - Low Risk	1	Facilities are fully secured by cash deposits, government bonds or a counter guarantee from a top tier international bank. All security documentation should be in place.
Good - Satisfactory Risk	2	The repayment capacity of the borrower is strong. The borrower should have excellent liquidity and low leverage. The company should demonstrate consistently strong earnings and cash flow and have an



		unblemished track record. All security documentation should be in place. Aggregate Score of 95 or greater based on the Risk Grade Scorecard.
Acceptable - Fair Risk	3	Adequate financial condition though may not be able to sustain any major or continued setbacks. These borrowers are not as strong as Grade 2 borrowers, but should still demonstrate consistent earnings, cash flow and have a good track record. A borrower should not be graded better than 3 if realistic audited financial statements are not received. These assets would normally be secured by acceptable collateral (1 st charge over stocks / debtors / equipment / property). Borrowers should have adequate liquidity, cash flow and earnings. An Aggregate Score of 75-94 based on the Risk Grade Scorecard.
Marginal - Watch list	4	Grade 4 assets warrant greater attention due to conditions affecting the borrower, the industry or the economic environment. These borrowers have an above average risk due to strained liquidity, higher than normal leverage, thin cash flow and/or inconsistent earnings. Facilities should be downgraded to 4 if the borrower incurs a loss, loan payments routinely fall past due, account conduct is poor, or other untoward factors are present. An Aggregate Score of 65-74 based on the Risk Grade Scorecard.
Special Mention	5	Grade 5 assets have potential weaknesses that deserve management's close attention. If left uncorrected, these weaknesses may result in a deterioration of the repayment prospects of the borrower. Facilities should be downgraded to 5 if sustained deterioration in financial condition IS noted (consecutive losses, negative net worth, excessive leverage), if loan payments remain past due for 30-60 days, or if a significant petition or claim IS lodged against the borrower. Full repayment of facilities is still expected and interest can still be taken into profits. An Aggregate Score of 55-64 based on the Risk Grade Scorecard.
Substandard	6	Financial condition IS weak and capacity or inclination to repay is in doubt. These weaknesses jeopardize the full settlement of loans. Loans should be downgraded to 6 if loan payments remain past due for 60-90 days, if the customer intends to create a lender group for debt restructuring purposes, the operation has ceased trading or any indication suggesting the winding up or closure of the borrower is discovered. Not yet considered non-performing as the correction of the deficiencies may result in an improved condition, and interest can still be taken into profits. An Aggregate Score of 45-54 based on the Risk Grade Scorecard.
Doubtful and Bad (non-performing)	7	Full repayment of principal and interest IS unlikely and the possibility of loss is extremely high. However, due to specifically identifiable pending factors, such as litigation, liquidation procedures or capital injection, the asset is not yet classified as a loss. Assets should be downgraded to 7 If loan payments remain past due excess of 90 days, and interest income should be taken into suspense (non-accrual). Loan loss provisions must be raised against the estimated unrealizable amount of all facilities. The adequacy of provisions must be reviewed at least quarterly on all non-performing loans, and the bank should pursue legal options to enforce security to obtain repayment or negotiate an appropriate loan rescheduling. In all cases, the requirements of Bangladesh Bank in CIB reporting, loan rescheduling and provisioning must be followed. An Aggregate Score of 35-44 based on the Risk Grade Scorecard
Loss (non-performing)	8	Assets graded 8 are longer outstanding with no progress in obtaining repayment (in excess of 180 days past due) or in the late stages of wind up/liquidation. The prospect of recovery is poor and legal options have been pursued. The proceeds expected from the liquidation or realization of security may be awaited. The continuance of the loan as a bankable



		asset is not warranted, and the anticipated loss should have been provided for. This classification reflects that it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may be affected in the future. Bangladesh Bank guidelines for timely write off of bad loans must be adhered to. An Aggregate Score of 35 or less based on the Risk Grade Scorecard At least top twenty five clients/obligors of the Bank may preferably be rated by an outside credit rating agency.
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The Early Alert Report is completed in a timely manner by the RM and forwarded to CRM of IBBL for approval to affect any downgrade. After approval, the report is forwarded to Credit Administration, who is responsible to ensure the correct facility/borrower Risk Grades are updated on the system. The downgrading of an account is done immediately when adverse information is noted, and is not postponed until the annual review process.

Classification Procedure:

After the date of expiry, if the borrowers do not adjust their loan, IBBL at first gives a notice to them. The period of giving notice depends on the nature of the loan. For continuous loan, IBBL gives notice for three months. For five-year term loan, IBBL gives notice for six months. And for more than five-year term loan, IBBL gives notice for more than 12 months.

After giving notice, if the borrower does not repay the loan, the loan will be considered as classified. Pursuant to Bangladesh Bank's Banking Regulation and policy Department's Circular No. 16 (1998), loans and advances are classified both on aging and functional criteria as follows:

Unclassified: The loan account is performing satisfactorily in the terms of its installments and no overdue is occurred. This type of loan and advances are fall into this class.

Classification Status	Length of Overdue	Rate of Provision
Unclassified	Below 3 months	1%

Substandard: This classification contains where irregularities have occurred but such irregularities are temporary in nature. To fall into this class the loan and advance has to fulfill the following factors.

Category of Credit		Time Overdue (Irregularities)	Substandard
S-T Agri& Micro Credit		3 months & above but less than 6 months.	
Continuous Loan	Demand Loan	Not recovered for 3 months & above but less than 6 months from the date of the loan is claimed.	
	Fixed Term loan	<i>Repayable within 5years:</i> If the overdue installment equals or exceeds the amount repayable within 6 months. <i>Repayable more than 5years:</i> If the overdue installment equals or exceeds the amount repayable within 12 months.	



The main criterion for a substandard advance is that despite these technicalities or irregularities no loss is expected to arise for the bank. These accounts will require close supervision by management to ensure that the situation does not deteriorate further.

Doubtful: This classification contains where doubt exists on the full recovery of the loan and advance along with a loss is anticipated but cannot be quantifiable at this stage. Moreover if the states of the loan accounts fall under the following criterion can be declared as doubtful loan and advance.

Category of Credit		Time Overdue (Irregularities)	Doubtful
S-T Agri& Micro Credit		6 months & above but less than 12 months.	
Continuous Loan	Demand Loan	Not recovered for 6 months & above but less than 12 months from the date of the loan is claimed.	
	Fixed Term Loan	<i>Repayable within 5 years:</i> If the overdue installment equals or exceeds the amount repayable within 12 months. <i>Repayable more than 5 years:</i> If the overdue installment equals or exceeds the amount repayable within 18 months.	

Bad and Loss:

A particular loan and advance fall in this class when it seems that this loan and advance is not collectable or worthless even after all the security has been exhausted. In the following table the criteria to be fulfilled to fall in this category are summarized:

Category of Credit		Time Overdue (Irregularities)	Bad and Loss
S-T Agri& Micro Credit		Not recovered within more than 12 months.	
Continuous Loan	Demand Loan	Not recovered more than 12 months from the date of the loan is claimed.	
	Fixed Term Loan	<i>Repayable within 5 years:</i> If the overdue installment equals or exceeds the amount repayable within 18 months. <i>Repayable more than 5 years:</i> If the overdue installment equals or exceeds the amount repayable within 24 months.	

Following measures are available for non-repayment of a loan-

- To issue notice for adjustment,
- To issue legal notice for filing suite,
- To encash securities (in case of demand loan),
- To issue legal notice for selling the hypothecated goods (in case of transport loan, cash credit-hypo),
- To issue suite for foreclosure,
- Finally to sue in money loan court or insolvency court which is suitable.



4.10 Provision Maintained by IBBL:

4.10.1 General Provision:

The bank will be required to maintain general provision in the following way:

- 1% against all classified loans (other than loans under consumer financing, loans to brokerage house, merchant banks, stock dealers etc. and special mention account)
- 5% of the classified amount of consumer financing whereas it has to be maintained 2% of the classified amount for housing finance and loans for professionals to set up business under consumer financing scheme.
- 2% of the unclassified amount for loans to brokerage house, merchant banks, stock dealers, etc.
- 5% on the outstanding amount of loans kept in the “Special Mention Account” after netting off the amount of interest suspense
- 1% of the off-balance sheet exposure. (Provision will be on the total exposure and the amount of cash margin or value of eligible collateral will not be deducted while computing off balance sheet).

4.10.2 Specific Provision:

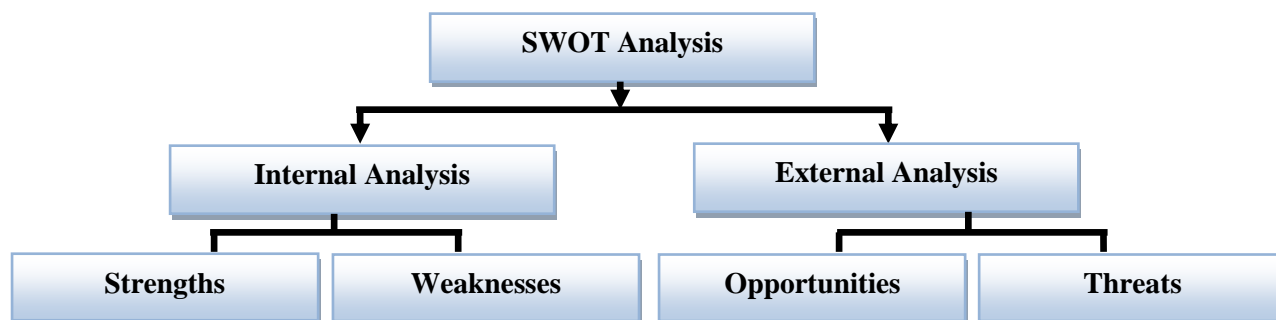
Banks will maintain provision at the following rates in respect of classified continuous, demand and fixed term loan:

- Sub-standard: 20%
- Doubtful: 50%
- Bad/loss: 100%

4.11 SWOT Analysis of Investment Operation of IBBL:

SWOT Analysis is the critical analysis about an organization, where the Strengths, Weaknesses, Opportunities and Threats to that organization are analyzed. It includes all internal and external aspects of the organization. It can be therefore defined as the analysis of external and internal environments. The major objective of doing the SWOT Analysis is to find out the internal strengths that is, in which areas it is more forward than its competitors and weaknesses that in which areas it has lacked. At the same time, the organization can know the opportunities that are available in the market for it and the threats ahead from its competitors or other regulatory bodies. Now showing the SWOT figure,

I worked as an internee for sixty days in the Islami Bank Bangladesh Limited, Mohakhali Branch. By this time, I tried to find out its Strengths, Weaknesses, Opportunities and Threats. I wish this would help the bank to make its service better and make a greater contribution to the society and to make a higher profit. The result of SWOT Analysis is as follows,



<u>Strengths:</u>	<u>Weaknesses:</u>
<ul style="list-style-type: none"> ▪ Adequate internal fund, ▪ Goodwill and market reputation, ▪ Confidence of common people of our country, ▪ Corporate culture and good governance ▪ Sovereignty in policy making, ▪ Collective efforts of the management in any situation of the bank, ▪ Experienced management team, ▪ Honest, sincere and reliable manpower, ▪ Banking software. 	<ul style="list-style-type: none"> ▪ CAR maintains, ▪ Lengthy investment procedure, ▪ Lack of diversification, ▪ Insufficient IT sector, ▪ Poor logistic support, ▪ Lack of specialized employees, ▪ Unethical influence.
<u>Opportunities:</u>	<u>Threats:</u>
<ul style="list-style-type: none"> ▪ Emergence of e-banking, ▪ Favorable environment for Islamic banking, ▪ Increasing importance for Islamic banking, ▪ To introduce new Islamic instruments, ▪ Accommodation of low income group to the banking industry, ▪ Decentralization of business geographically, 	<ul style="list-style-type: none"> ▪ High inflation view, ▪ Economic recession, ▪ Lack of financial stability, ▪ Instability in capital market, ▪ Absence of Islamic money market, ▪ Inappropriate Islamic banking by competitors.

Part Five

Analysis





5.1 Five Years Investment Performance of IBBL:

Particulars		2008	2009	2010	2011	2012
Deposit	Amount	202,115.45	244,292.14	291,934.60	341,853.67	417,844.14
	Growth	21.52%	20.87%	19.50%	17.10%	22.23%
Investments (including Investment in Shares and Securities)	Amount	187,586.55	225,752.41	275,493.94	322,772.83	399,930.79
	Growth	13.49%	20.35%	22.03%	17.16%	23.90%
Investment in Shares & Securities	Amount	7,532.61	11,136.61	12,268.81	16,932.27	27,010.07
Investments (excluding Investment in Shares and Securities)	Amount	180,053.94	214,615.80	263,225.13	305,840.56	372,920.72
	Growth	24.24%	19.20%	22.65%	16.19%	21.93%
Investment Deposit Ratio	%	89.08%	87.85%	90.17%	87.29%	85.18%
Amount of Classified Investment	Amount	4,311.13	5,063.40	4,655.63	8,292.32	14,212.80
Classified Investment to Total Investment	%	2.39%	2.36%	1.77%	2.71%	3.81%
Provision against Classified Investment	Amount	1,883.43	2,490.00	1,840.00	3,054.00	6,054.35
General Provision against Unclassified Investment	Amount	2,315.74	2,700.00	3,443.00	3,996.00	3,935.90
Investment Income	Amount	19,543.84	21,370.53	24,766.26	32,019.53	43,672.23
Profit Paid on Deposit	Amount	12,162.10	13,076.99	14,471.89	18,401.22	25,870.43
Net Investment Income	Amount	7,381.74	8,293.54	10,294.37	13,618.31	17,801.80

Note: All the amounts use and show in this table and analysis are in **million Taka**

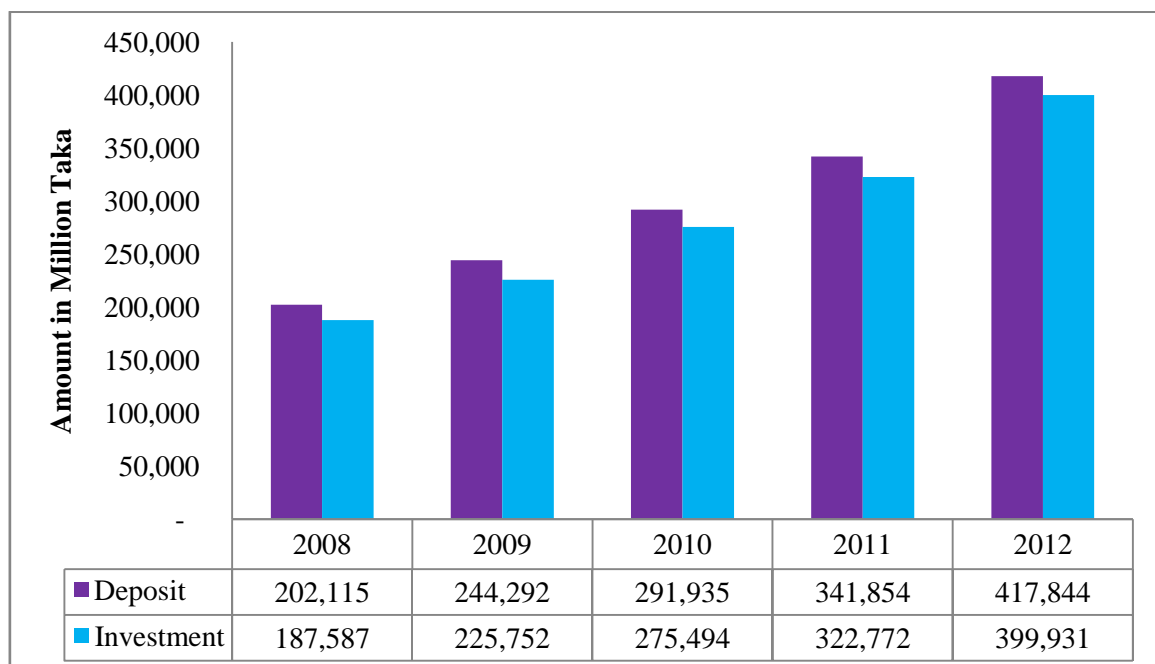


Figure 5.1: Total Deposit and Investment Business Trend of IBBL

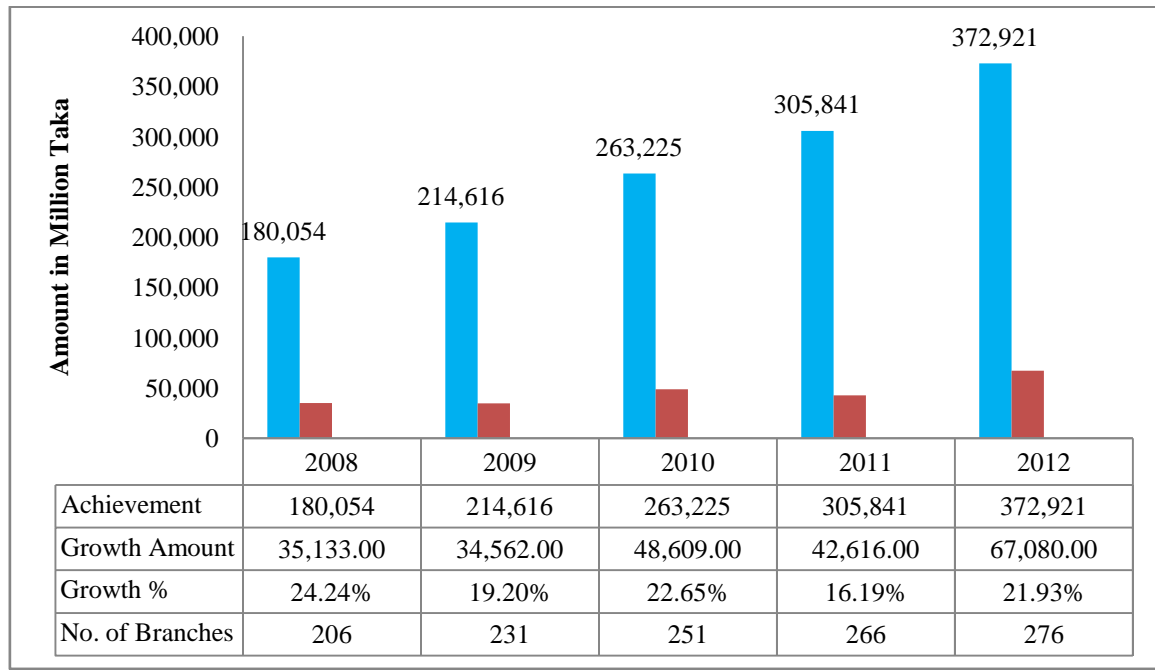
Source: Annual Reports 2008-2012

5.2 Analysis of Investment:

5.2.1 Year wise General Investment Trend:

General investments are stated in the balance sheet on gross basis. General investments and bills purchased and discounted are on the basis of their maturity/ repayment term.

Figure 5.2.1: General Investment Trend of IBBL



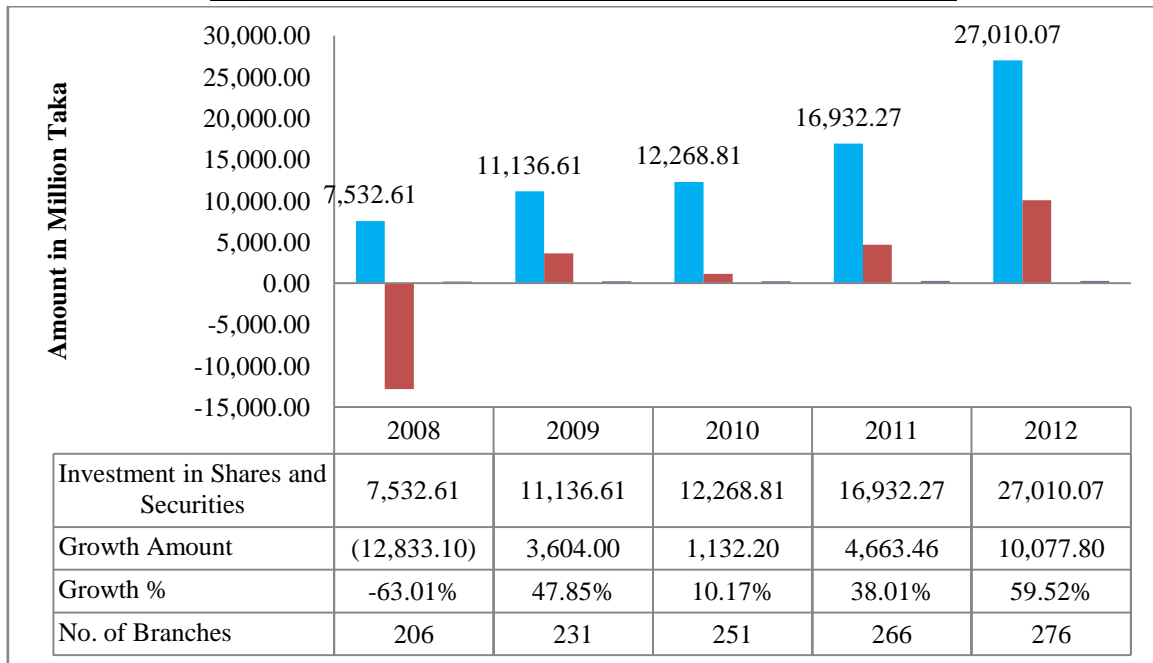
Source: Annual Reports 2008-2012

The bank's general investment increased to Tk.372,921 million as on December 31, 2012 from Tk. 305,841 million as on December 31, 2011 showing an increase of Tk.67,080 million, i.e., 21.93% growth against 10.03% investment growth of the banking sector. This higher investment growth of the bank in 2012 was due to the thrust given to promote investment for effective utilization of depositors' fund. The percentage growth of IBBL investment in 2011 was 16.19%. The share of investment of IBBL in the banking sector as on December 31, 2012 was 8.40%. Trend of investment shows a clear direction of doubling in last 5 years.

General investment of Islami Bank Bangladesh Limited was increasing year by year. In 2008 with 206 branches the bank's investment was Tk. 180,054 million which was almost doubled in 2012 of Tk. 372,921 million with the additional 70 branches (additional 34%). So, the bank did an excellent investment business during this period with different types of strategies and policies. The bank's average growth during this period was 20.84%.

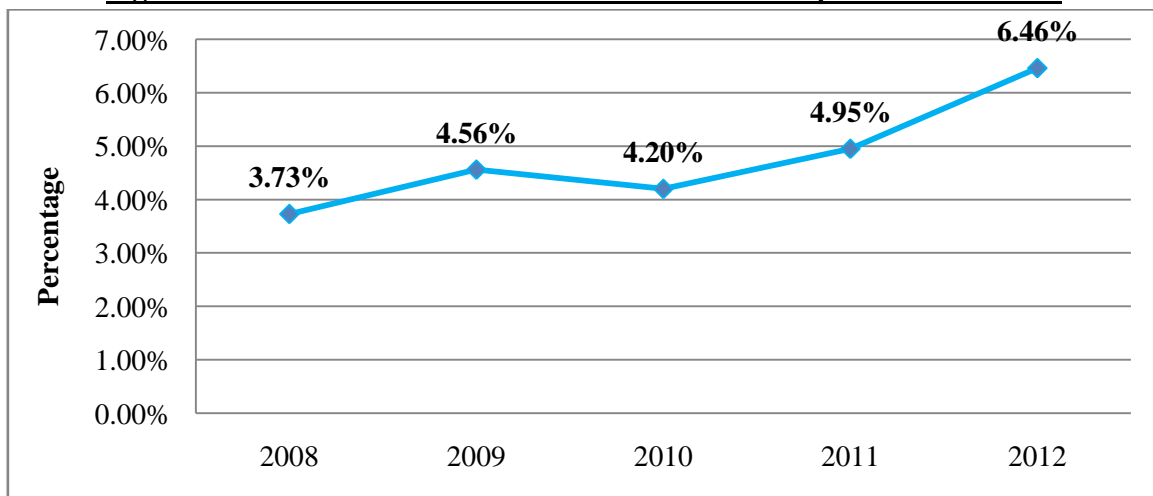
5.2.2 Year-wise Investment in Shares and Securities:

Figure 5.2.2.1: Investment in Shares and Securities of IBBL



Source: Annual Reports 2008-2012

Figure 5.2.2.2: Investment in Shares and Securities to Deposit Ratio of IBBL



Source: Annual Reports 2008-2012

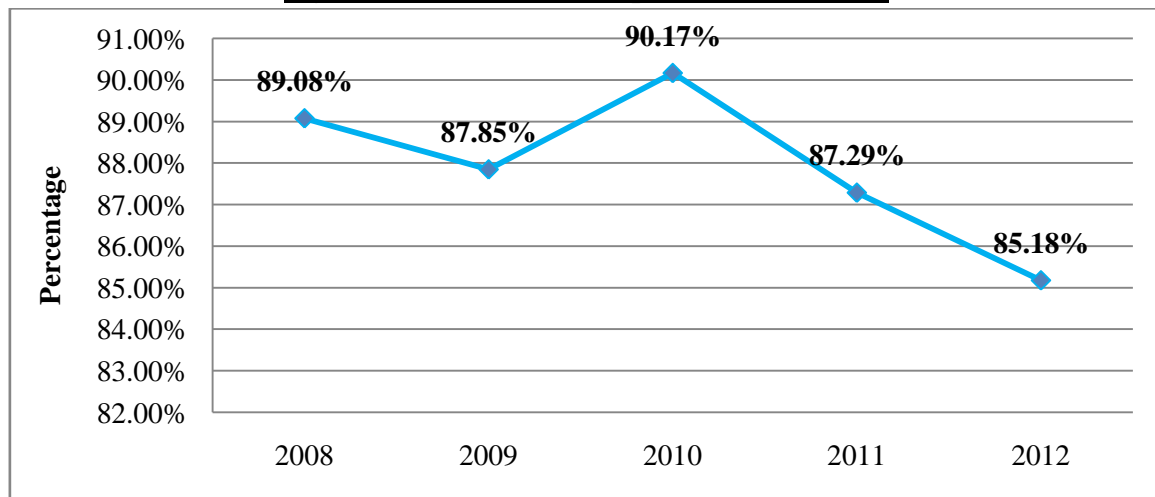
In 2008 the investment in shares and securities made by the bank was Tk. 7,532.61 million. It was in an increasing mode & was almost four times in 2012 than to 2008 resulted the figure was Tk. 7,532.61 million to Tk. 27,010.07 million. From the above figure it is seen that the average growth rate per year was 18.51%. We can also see from the second figure that the bank investment in shares and securities to deposit ratio was highest in 2012 to 6.46% during the last five years. The average investment in shares and securities to deposit ratio of IBBL during this period was 4.78%.

5.2.3 Investment Deposit Ratio:

An investment deposit ratio is a commonly used statistic for assessing a bank's liquidity by dividing the banks total investments by its total deposits. This number, also known as the IDR ratio, is expressed as a percentage. If the ratio is too high, it means that banks might not have enough liquidity to cover any unforeseen fund requirements; if the ratio is too low, banks may not be earning as much as they could be.

Particulars	2008	2009	2010	2011	2012
Total Deposits	202,115	244,292	291,935	341,854	417,844
Investment Deposit Ratio	89.08%	87.85%	90.17%	87.29%	85.18%

Figure 5.2.3: Investment Deposit Ratios of IBBL



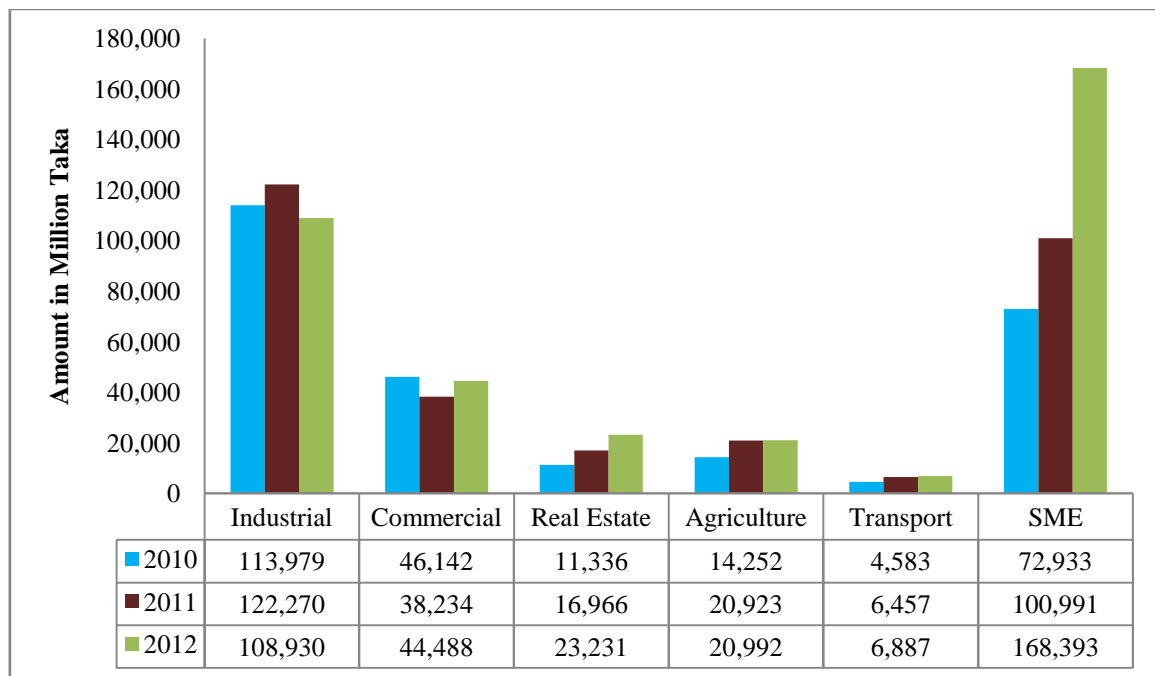
Source: Annual Reports 2008-2012

From the above graph it is seen that the investment deposit ratio of IBBL was fluctuating over the time. By considering the above graph it can be said that the bank is capable to utilize its deposit into an investment that indicates a good sign for the bank. The bank never faced less than 85% of the investment deposit ratio during the last five years and tried to exceed 90% of the investment deposit ratio as per the instruction of Bangladesh Bank.

5.2.4 Sector-wise Investment Position:

Sector	2010		2011		2012	
	Amount	% of Total Investment	Amount	% of Total Investment	Amount	% of Total Investment
Industrial (excluding SME)	113,979	43.30%	122,270	39.98%	108,930	29.21%
Commercial	46,142	17.53%	38,234	12.50%	44,488	11.26%
Real Estate	11,336	4.31%	16,966	5.55%	23,231	5.46%
Agriculture	14,252	5.41%	20,923	6.84%	20,992	5.78%
Transport	4,583	1.74%	6,457	2.11%	6,887	1.90%
SME	72,933	27.71%	100,991	33.02%	168,393	46.93%
Total	263,225	100%	305,841	100%	372,921	100%

Figure 5.2.4: Sector-wise Investment of IBBL



Source: Annual Reports 2010-2012

From the graph we can see that, in 2012 the bank's investment in major sectors except industrial sector (excluding SME) was increased than previous years. And in the same year investment in SME became the largest portion of total investment and also more than doubled in only two years from 2010. In 2012 the bank did not face any negative growth in any sector's investment except in industrial sector due to more emphasize on SME sector which results with an extraordinary growth.

5.2.5 Mode-wise Investment Position:

Mode	2010		2011		2012	
	Amount	% of Total Investment	Amount	% of Total Investment	Amount	% of Total Investment
Bai-Murabaha	146,135	55.52%	177,136	57.92%	221,632	59.43%
HPSM	80,093	30.42%	89,070	29.12%	96,056	25.76%
BaiMuajjal	12,393	4.71%	15,912	5.20%	18,295	4.91%
Bill Purchased & Negotiation	5,141	1.95%	2,744	0.91%	9,531	2.56%
Quard	2,095	0.80%	5,614	1.83%	9,156	2.46%
Bai- Salam	3,624	1.38%	3,528	1.15%	4,532	1.22%
Mudaraba	1,500	0.57%	2,266	0.74%	-	-
Musharaka	12,244	4.65%	9,571	3.13%	13,719	3.68%
Total	263,225	100%	3,05,841	100%	3,72,921	100%

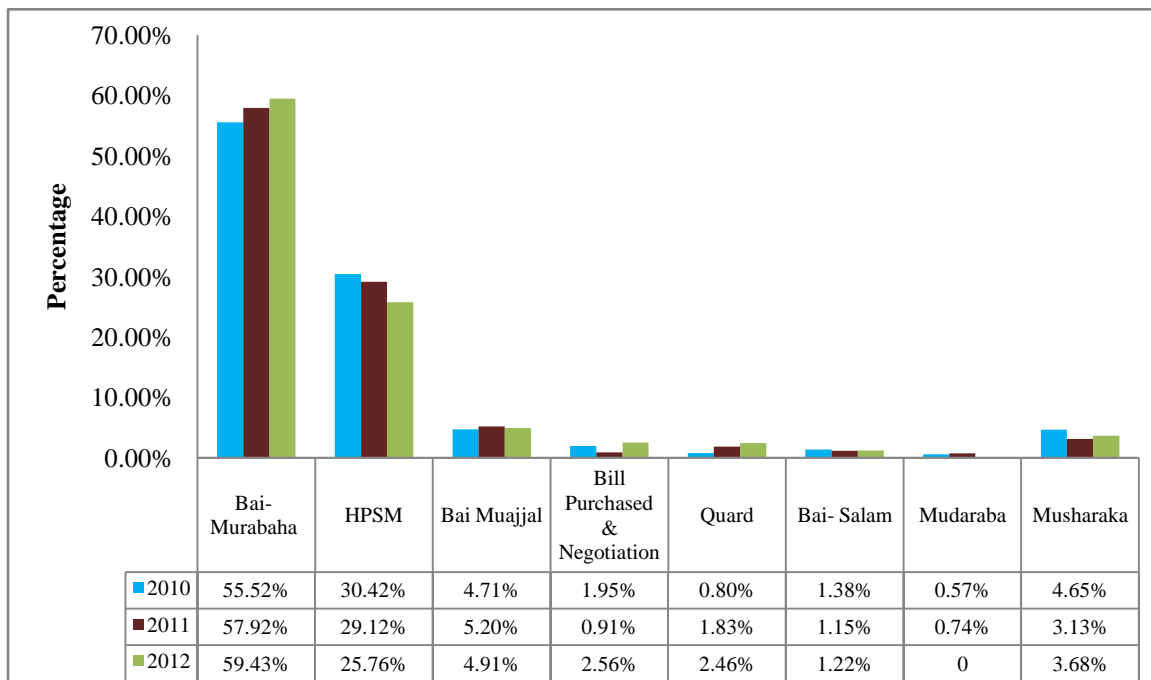


Figure 5.2.5: Mode-wise Investment of IBBL

Source: Annual Reports 2010-2012

The graph depicted above in 2012 the bank's investment in all modes except Mudaraba was in increasing mode from 2010 to 2012. Bai-Murabaha was the highest volume of investment the bank made over the years. Excellent growth has been achieved in the modes of investment of Bill Purchased & Negotiation and Quard by the bank from 2010 to 2012.



5.2.6 Industrial Investment of IBBL:

Particulars	2010			2011			2012		
	No of Projects	Amount	% of Total Investment	No of Projects	Amount	% of Total Investment	No of Projects	Amount of Investment	% of Total Investment
Textile-Spinning, Weaving & Dyeing	355	63,669	42.70%	186	75,031	46.31%	421	71,761	37.93%
Steel, Re-Rolling & Engineering	40	10,584	7.10%	60	7,579	4.71%	203	21,946	11.60%
Agro Based Industry	153	11,492	7.71%	381	17,219	10.70%	950	17,614	9.31%
Garments & Garments Accessories	259	11,733	7.87%	200	11,239	6.99%	575	13,092	6.92%
Food & Beverage	42	5,106	3.42%	24	6,678	4.15%	50	7,636	4.04%
Cement Industry	10	1,074	0.72%	9	2,097	1.30%	9	1,854	0.98%
Pharmaceuticals	12	1,064	0.71%	13	2,031	1.26%	36	2,289	1.21%
Poultry, Poultry Feed & Hatchery	14	404	0.27%	59	997	0.62%	110	624	0.33%
Sanitary Wares	1	368	0.25%	95	966	0.60%	49	275	0.15%
Chemicals, Toiletries & Petroleum	11	1,559	1.05%	17	4,095	2.55%	161	3,973	2.10%
Printing & Packaging	36	1,095	0.73%	47	2,912	1.81%	157	3,330	1.76%
Power (Electricity)	13	4,694	3.15%	4	4,281	2.66%	8	4,162	2.20%
Ceramic & Bricks	9	951	0.64%	10	2,011	1.25%	217	2,460	1.30%
Health Care (Hospital & Others)	13	1,249	0.84%	-	-	-	54	2,079	1.10%
Plastic Industries	26	1,743	1.17%	-	-	-	65	715	0.38%
Petrol-Pump & CNG Filling Station	20	416	0.28%	63	836	0.52%	63	940	0.50%
Information Technology	-	-	-	-	-	-	11	550	0.29%
Hotel & Restaurant	6	21	0.01%	-	-	-	177	656	0.35%
Other Industries	253	31,897	21.39%	198	22,926	15%	305	33,237	17.55%
Total	1,253	149,119	100%	1,366	160,898	100%	3,621	189,193	100%

Source: Annual Reports 2010-2012

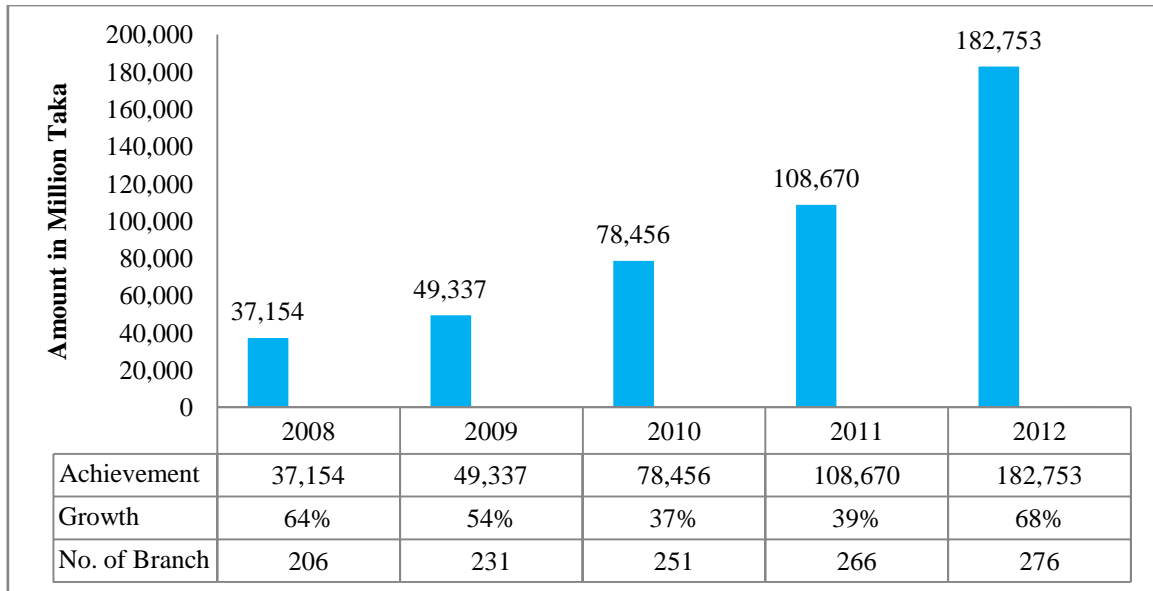
From the table we can see that the bank's investment reaches to almost all types of industries of the country. The bank has contributed significantly to the development of the industrial sector of the country. It is the only bank that has deployed 50.73% of its total investment in the industrial sector and out of which export-oriented garment industries occupied 44.85%. In addition to large scale



industries, bank also finance medium and small scale industries keeping its primary focus on need based industry.

5.2.7 Year-wise SME Investment of IBBL:

Figure 5.2.7: Year-wise SME Investment of IBBL



Source: Annual Reports 2008-2012

Year	IBBL	PCBs SME Exposure	% of IBBL to PBs	Total National Exposure	% of IBBL to Total National Exposure
2010	78,456	390,838.50	20%	695,265.80	11.28%
2011	108,670	464,292	22%	810,992	13%
2012	182,753	719,845	25%	1,008,132	18%

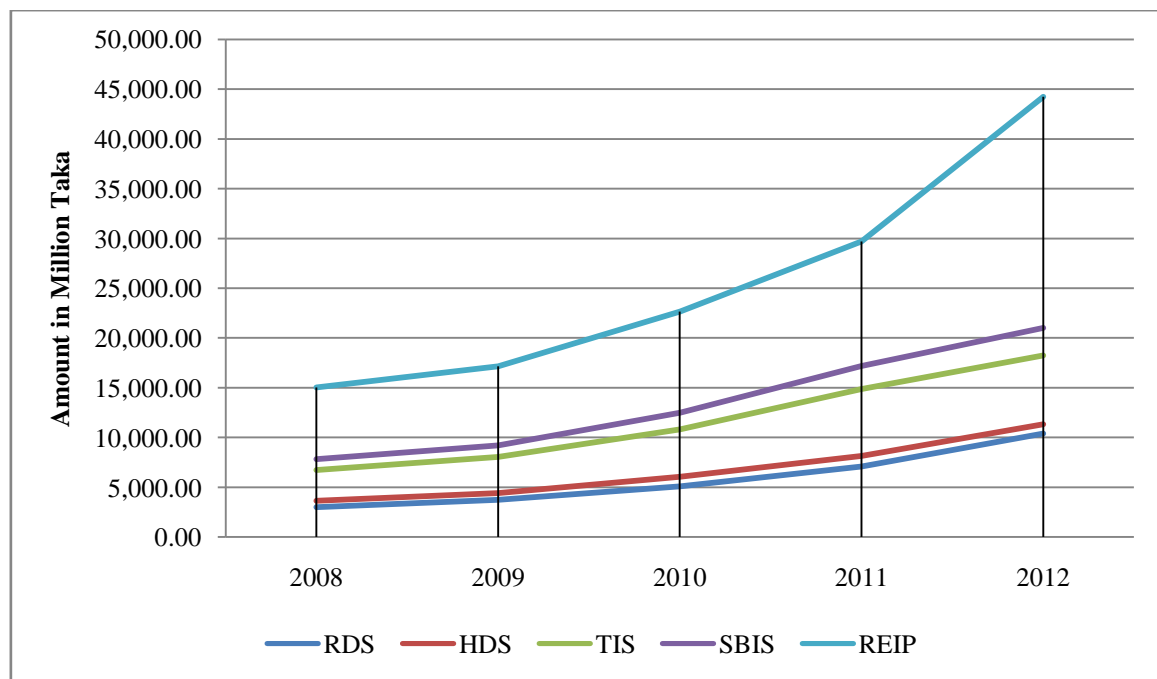
SME Investment of Islami Bank Bangladesh Limited was increasing very rapidly during last five years. In 2008 with 206 branches the bank's SME investment was Tk. 37,154 million which was almost tripled in 2012 of Tk. 182,753 million with the additional 70 branches (additional 34%). The bank did an outstanding SME investment business during this period with their more availability and excellencies.

In 2012, the bank was achieved all sorts the targets set by the Bangladesh Bank. Moreover IBBL took some measures in its own initiatives for the overall development of this sector. In 2012, 47% of total investment of the bank were in SME Investment.

5.2.8 Scheme-wise Investment of the Bank:

Name of Scheme	2008	2009	2010	2011	2012
Rural Development Scheme (RDS)	3,011.72	3,752.20	5,110.00	7,072.02	10,390
House-hold Durables Scheme (HDS)	638.40	686.49	961.64	1070.01	955
Investment Scheme for Doctors (ISD)	15.34	17.06	15.27	13.91	32
Transport Investment Scheme (TIS)	3,087.55	3,630.48	4,732.15	6,706.50	6,887
Car Investment Scheme (CIS)	1,104.65	1,159.63	1,703.44	2,347.60	2,774
Small Business Investment Scheme (SBIS)	1,104.65	1,159.63	1,703.44	2,347.60	2,774
Micro-Industries Investment Scheme (MIIS)	31.50	50.39	47.44	38.18	36
Agricultural Implements Investment Scheme (AIIS)	27.21	76.64	127.15	209.60	278
Housing Investment Scheme (HIS)	429.24	452.57	418.92	366.68	316
Real Estate Investment Program (REIP)	7,183.26	7,933.20	10,154.95	12,485.24	23,231
Sub-total (Investment under Schemes)	15,570.03	17,812.57	23,410	30,461.79	45,012
Total Investment	180,054	214,616	263,225	305,841	372,921
% to total Investment	8.65%	8.30%	8.89%	9.96%	12.07%

Figure 5.2.8: Trend of Some Major Investment Schemes of IBBL



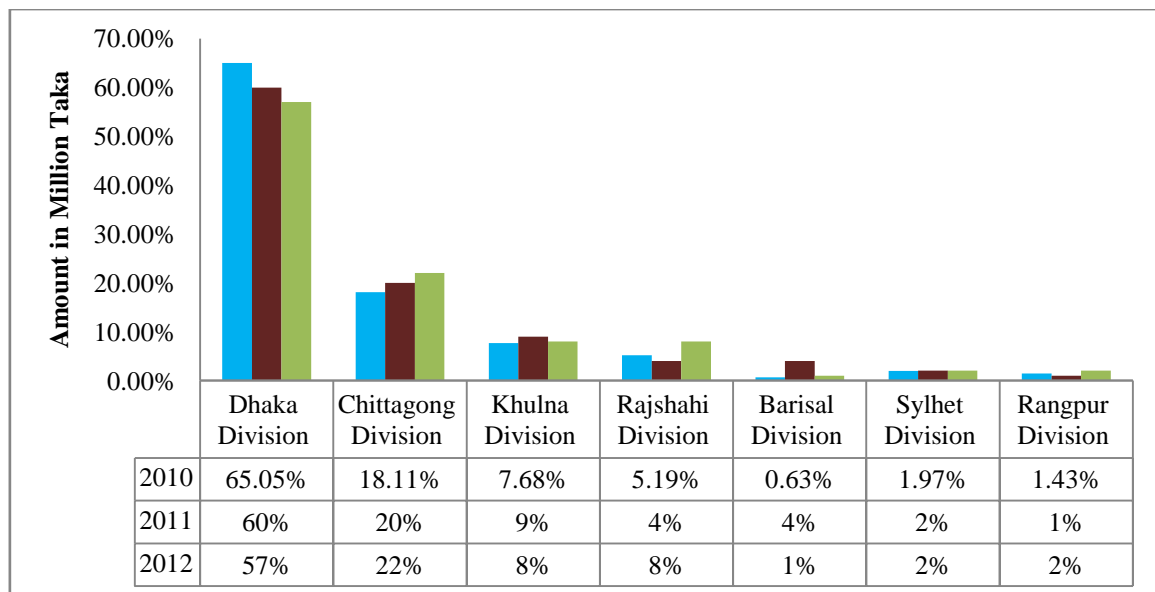
Source: Annual Reports 2008-2012

From the table and graph it can be seen that almost all the schemes are increasing year by year. Among them Rural Development Scheme, House-hold Durable Scheme, Transport Investment Scheme, Small Business Investment Scheme and Real Estate Investment Program have the highest volume of investment amount as well as a notable percentage of growth. From 2008 to 2012 almost all types of scheme became doubled to five times bigger in amount of investment.

5.2.9 Division-wise Distribution of Investment:

Particulars	2010		2011		2012	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
Dhaka Division	171,219.65	65.05%	183,456.54	60%	213608.99	57%
Chittagong Division	47,664.62	18.11%	61,255.47	20%	81072.97	22%
Khulna Division	20,047.67	7.68%	26,656.47	9%	31511.80	8%
Rajshahi Division	13,667.31	5.19%	12,989.77	4%	28304.68	8%
Barisal Division	1,657.24	0.63%	2,774.65	4%	3729.20	1%
Sylhet Division	5,192.84	1.97%	5,867.11	2%	7160.08	2%
Rangpur Division	3,775.82	1.43%	12,840.60	1%	7533.00	2%
Total	263,225	100%	305,841	100%	372,921	100%

Figure 5.2.9: Division-wise Distribution of Investment



Source: Annual Reports 2010-2012

From the table and graph we can see that more than 50% of total investment was distributed in Dhaka Division. It was happened due to the position of country's commercial hubs in Dhaka as well as maximum headquarters of different organizations are situated in Dhaka. Chittagong Division was in the second position for the same reasons. Others divisions got a lower distribution of investment due to the unwillingness of the bank besides less demand for investment aroused in these divisions.

5.3 Analysis of Classified Investment:

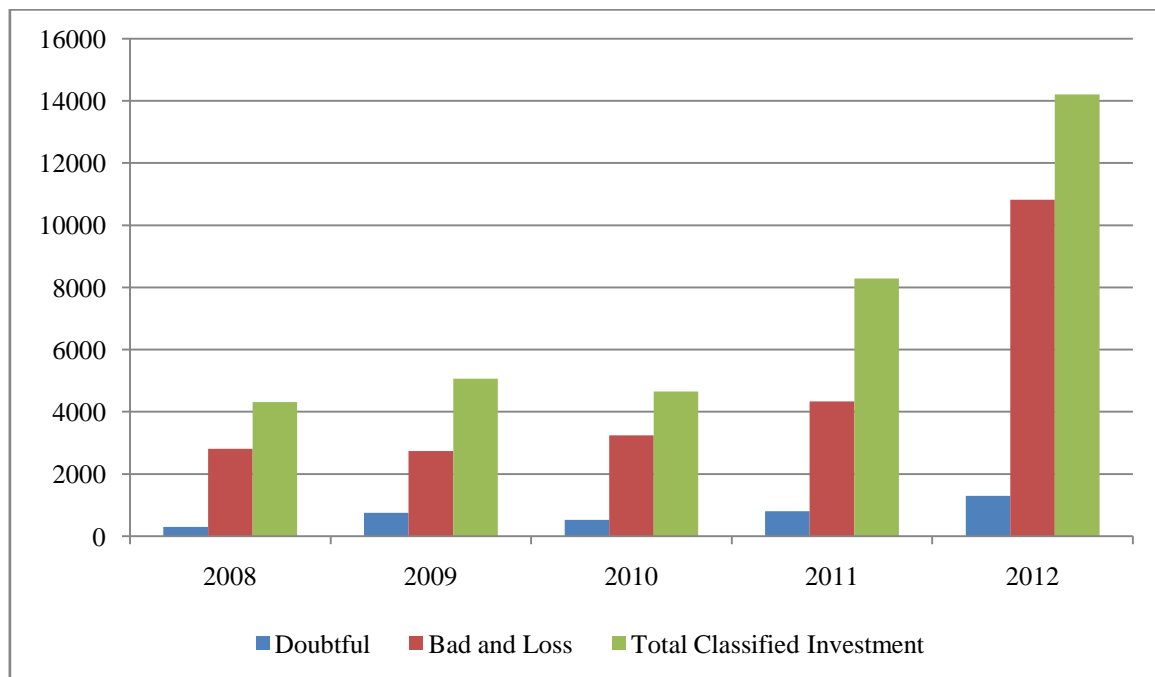
5.3.1 Classified Investments of IBBL:

Classified loan is categorized under following three (3) categories,

- ❖ Sub-standard,
- ❖ Doubtful, and
- ❖ Bad & Loss.

Particulars	2008	2009	2010	2011	2012
Substandard	1,199.34	1,576.53	896.40	3,152.33	2,094.31
Doubtful	301.73	751.16	520.70	802.79	1,295.18
Bad and Loss	2,810.07	2,735.71	3,238.40	4,337.20	10,823.31
Total Classified Investment	4,311.13	5063.40	4,655.63	8,292.32	14,212.80
Classified Investment during the year	65.11	752.27	-407.77	3,636.69	5,920.48

Figure 5.3.1: Classified Investments of IBBL



Source: Annual Reports 2008-12

From the above graph we can say that, there was a huge increase of classified investment in 2012. But from 2008 to 2012 the bank's total investment was increased to almost double on the other hand the bank's classified investment was increasing to almost triple. In this case there may not be a big deal of classified investment rising, it was then just increased by maintaining consistent with the total investment besides IBBL maintained sufficient and required provision against those investments. On the other hand in 2012 substandard investment decreased to Tk. 2,094.31 million from Tk. 3,152.33 million.

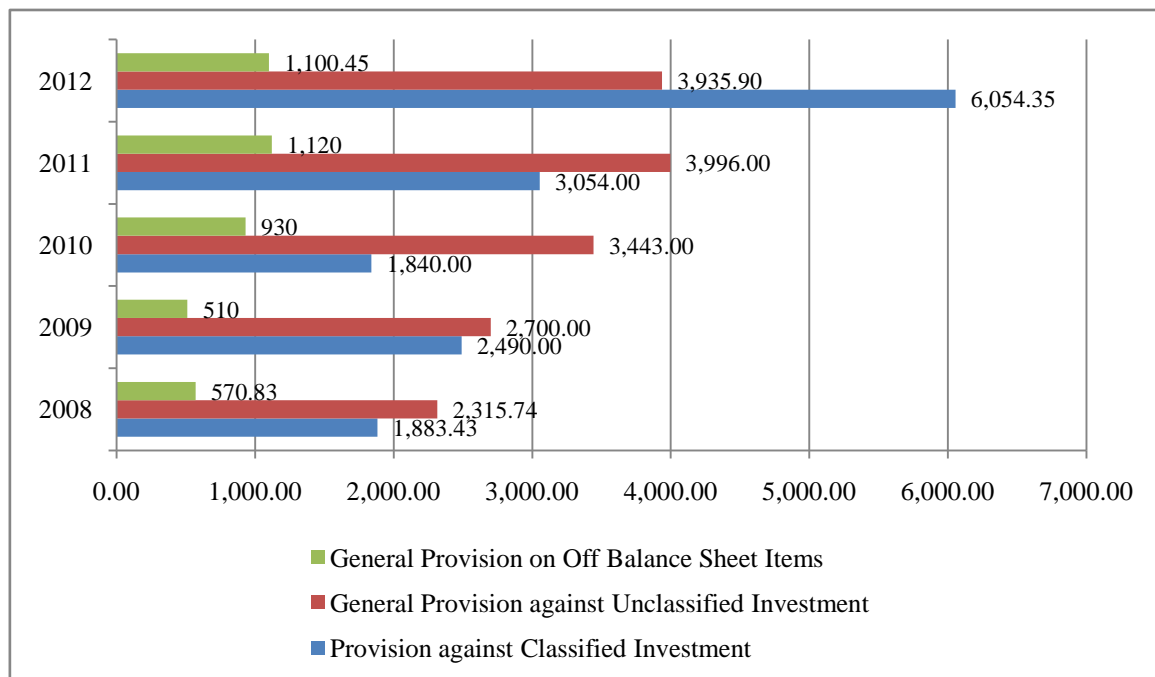


5.3.2 Provision against Investments:

Classifying investment under various heads such as, unclassified, sub-standard, doubtful or bad/loss through verification of borrower's repayment is needed to know the status of the loan. It is essential to determine the financial health and efficiency of a bank. In order to get rid of default loans Bangladesh bank introduced a circular (BCD circular No. 34) on 1989 for classification & provision of loan.

Particulars	2008	2009	2010	2011	2012
Provision against Classified Investment	1,883.43	2,490.00	1,840.00	3,054.00	6,054.35
General Provision against Unclassified Investment	2,315.74	2,700.00	3,443.00	3,996.00	3,935.90
General Provision on Off Balance Sheet Items	570.83	510.00	930.00	1,120.00	1,100.45

Figure 5.3.2: Provision against Investments of IBBL



Source: Annual Reports 2008-12

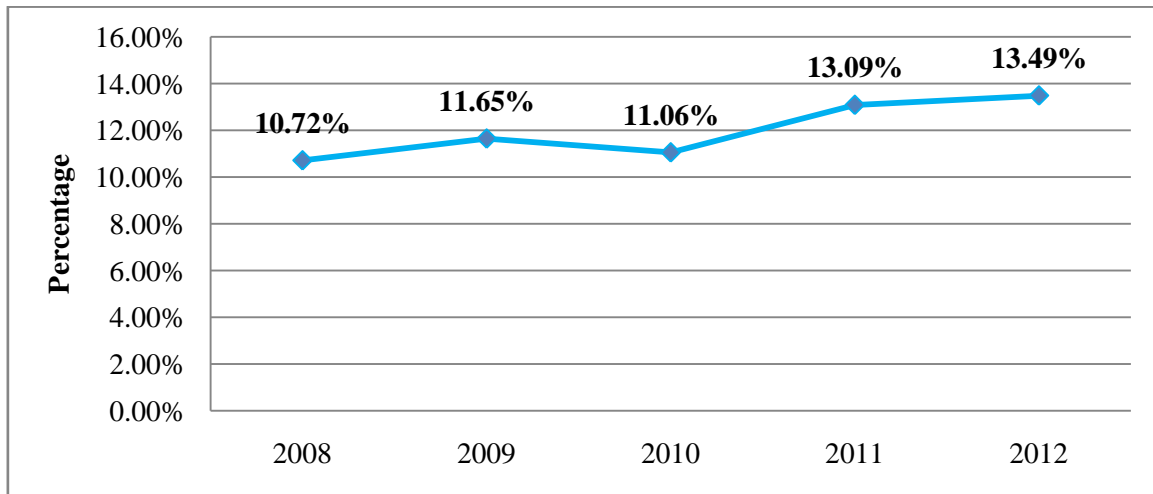
From the above graph we can see that, there was a natural increase of provision against classified investment in 2012 with consistent to an increase of classified investment. According to Basel II Accord imposed and regulated by Bangladesh Bank, IBBL kept required provision against classified investment as well as a general provision against unclassified investment and off balance sheet items.

5.4 Analysis of Investment Risk of IBBL:

5.4.1 Capital Adequacy Ratio:

Capital Adequacy Ratio, also known as Capital to Risk (Weighted) Assets Ratio (CRAR), is a ratio of a bank's capital to its risk. National regulators track a bank's CAR to ensure that it can absorb a reasonable amount of loss and complies with statutory capital requirements

Figure 5.4.1: Capital Adequacy Ratio of IBBL



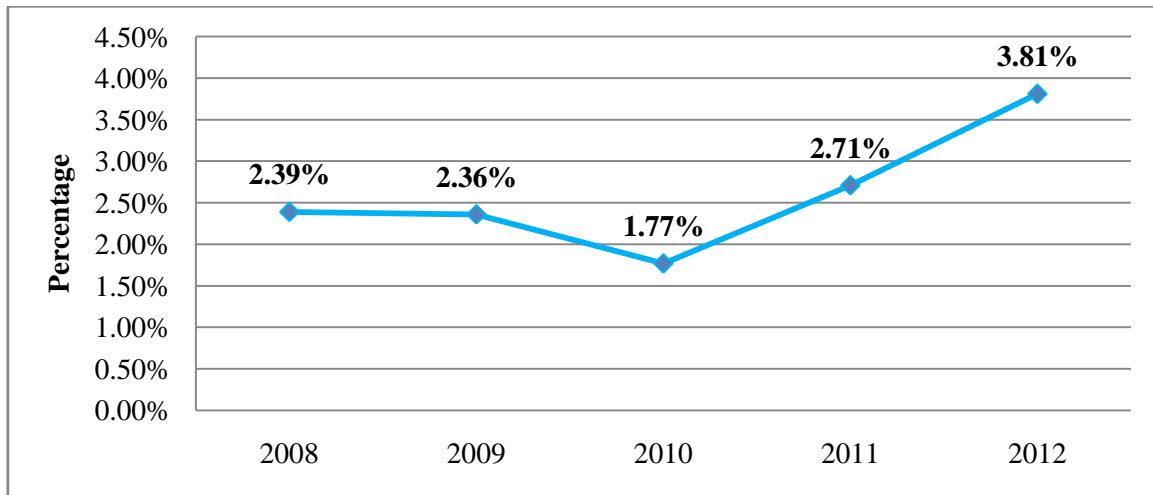
Source: Annual Reports 2008-2012

Capital Adequacy Ratio determines the capacity of the bank in terms of meeting the liabilities and other risk such as credit risk, operational risk etc. Generally, 10% is an acceptable line for this ratio in that senses the bank was good enough to maintain this requirement. The bank followed Basel II Accord in 2012, 2011, 2010 & 2009, followed Basel I Accord in 2008 for calculating capital adequacy ratios. From 2008 to 2012 the bank's capital adequacy ratios were above 10% all the time indicates that the bank's capacity to meet the liabilities and other risk such as credit risk, operational risk were satisfactory.

5.4.2 Classified Investment to Total Investment:

Particulars	2008	2009	2010	2011	2012
Amount of Classified Investment	4,311.13	5,063.40	4,655.63	8292.32	14,212.80
Classified Investment to Total Investment	2.39%	2.36%	1.77%	2.71%	3.81%

Figure 5.4.2: Classified Investment to Total Investment



Source: Annual Reports 2008-2012

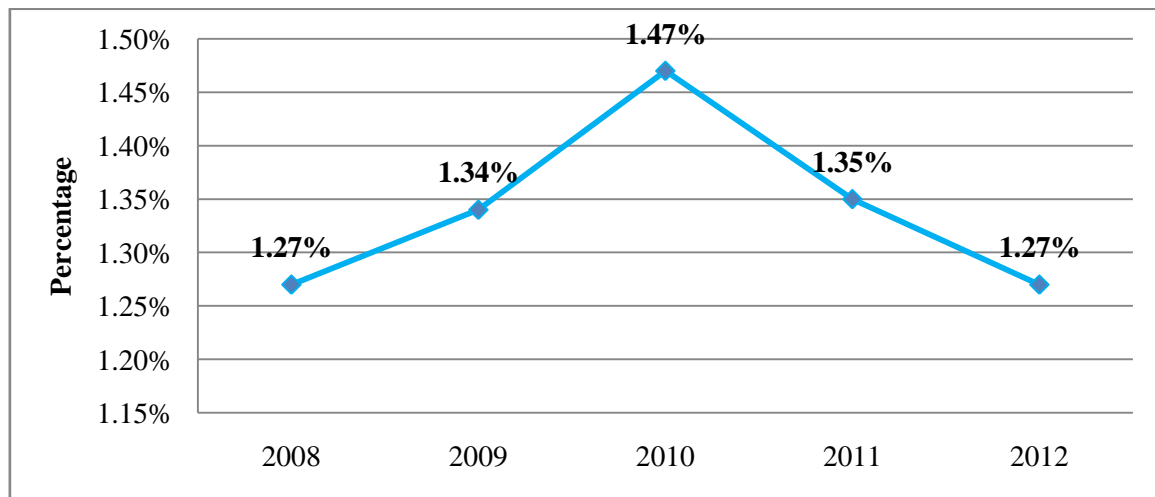
From the above graph it has been seen that, percentage of classified investment to total investment fluctuated slowly from 2008-2012. In 2007 & 2008 the rate was at 2.5%, it decreased to 1.77% in 2010. In 2010 the rate was increased to 2.71%. And in 2012 it was increased to 3.81% which was the highest during last five years. The bank should try to give more concentration to reduce their classified investment, and to become more efficient in managing its classified investment.

5.4.3 Return on Assets (ROA):

Return on Asset is an indicator of how profitable a company is relative to its total assets. ROA gives an idea as to how efficient management is at using its assets to generate earnings. Calculated by dividing a company's annual earnings by its total assets, ROA is displayed as a percentage.

Particulars	2008	2009	2010	2011	2012
Net Profit after Tax	2,674.80	3,403.55	4,463.47	4,841.45	5,524.44
Total Assets	230,879.14	278,302.84	330,586.12	389,192.12	482,536.32
Return on Assets (ROA)	1.27%	1.34%	1.47%	1.35%	1.27%

Figure 5.4.3: Return on Assets of IBBL



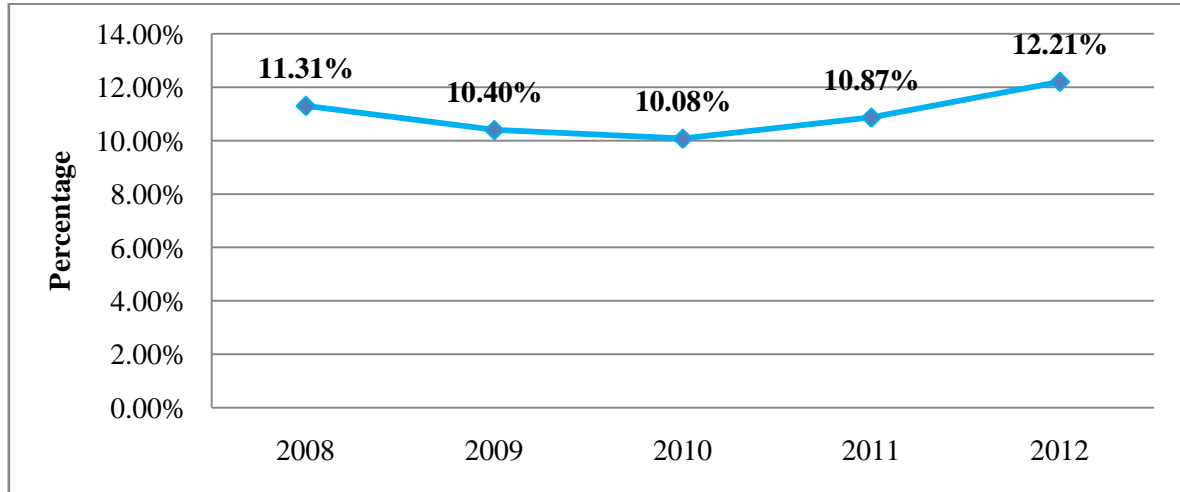
Source: Annual Reports 2008-2012

Return on Assets (ROA) ratios of Islami Bank Bangladesh Limited were fluctuating over the period of 2008 to 2012. In 2008 with 206 branches the bank's return on assets ratio was 1.27% which was equal to return on assets ratio in 2012 with the additional 70 branches (additional 34%). It happened because the bank's net profit after tax was increased with total assets of the bank almost simultaneously. So, the bank did an excellent investment business during this period with different types of strategies and policies. The Bank's average return on assets during this period was 1.34%.

5.4.4 Return on Investment:

Return on Investment is a performance measure used to evaluate the efficiency of an investment or to compare the efficiency of a number of different investments. To calculate ROI, the benefit (return) of an investment is divided by the cost of the investment; the result is expressed as a percentage or a ratio.

Figure 5.4.4: Return on Investment of IBBL



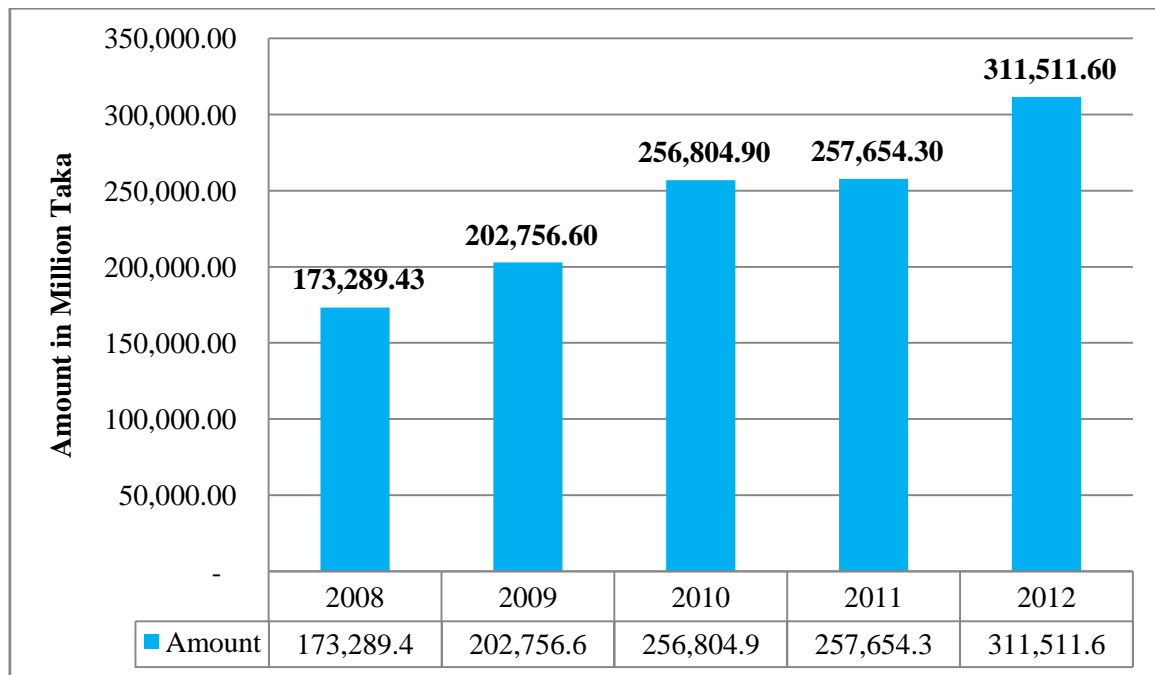
Source: Annual Reports 2008-2012

Return on Investment (ROI) ratios of Islami Bank Bangladesh Limited were fluctuating over the period of 2008 to 2012. In 2008 with 206 branches the bank's return on investment ratio was 11.31% which was gradually increased in 2012 to 12.21% with the additional 70 branches (additional 34%). It happened because the bank's increased gain from the investment and decreased cost of investment simultaneously. So, the bank did an excellent investment business during this period with different types of strategies and policies. The Bank's average return on investment during this period was 10.97%.

5.4.5 Total Risk Weighted Assets:

In terms of the minimum amount of capital that is required within banks and other institutions, based on a percentage of the assets, weighted by risk. The idea of risk-weighted asset is a move away from having a static requirement for capital. Instead, it is based on the riskiness of a bank's assets. For example, loans that are secured by a letter of credit would be weighted riskier than a mortgage loan that is secured with collateral.

Figure 5.4.5: Total Risk Weighted Assets Trend of IBBL



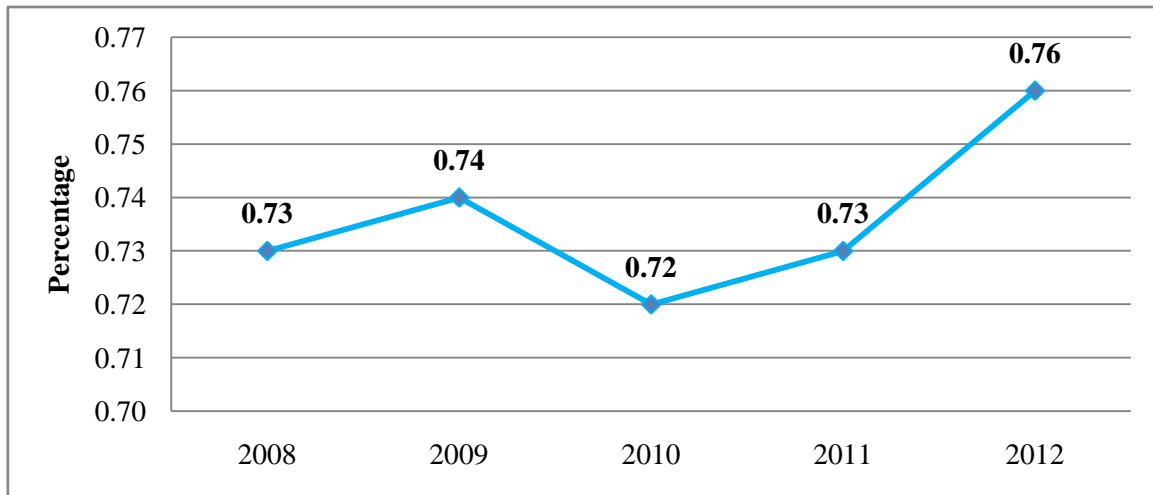
Source: Annual Reports 2008-2012

Total Risk Weighted Assets (RWA) of Islami Bank Bangladesh Limited were increasing over the period of 2008 to 2012. In 2008 the bank's total risk weighted assets was Tk. 173,289.43 million which became about doubled in 2012 of Tk. 311,511.60 million worth. It was the result of the bank's increased investments as well as the bank's total assets. The bank's average total risk weighted assets during this period was Tk. 240,403.37 million. Besides during the period of 2008 to 2012 the bank all the time faced a capital surplus.

5.4.6 Cost Income Ratio/Efficiency Ratio:

Efficiency Ratio that is typically used to analyze how well a company uses its assets and liabilities internally. Efficiency Ratios can calculate the turnover of receivables, the repayment of liabilities, the quantity and usage of equity and the general use of inventory and machinery.

Figure 5.4.6: Cost Income Ratio/Efficiency Ratio of IBBL



Source: Annual Reports 2008-2012

Cost Income Ratio or Efficiency Ratio is the ratio between operating expenses and operating income. It is a measure of how costs are changing compared to income. It is one of the main key performance indicators of a bank's efficiency: the lower the ratio the more efficient the bank. Islami Bank Bangladesh Limited's efficiency ratios were in a fluctuating move over the period of 2008 to 2012. In 2008 the bank's efficiency ratio was 0.73% which was very close to an efficiency ratio of 0.76% in 2012. The Bank's average cost income ratio during this period was 0.74%.



5.4.7 Credit Ratings of IBBL:

A credit rating is an evaluation of the credit worthiness of a debtor, especially a business (company) or a government, but not individual consumers. The evaluation is made by a credit rating agency of the debtor's ability to pay back the debt and the likelihood of default.

Table 5.4.7: Credit Ratings of IBBL

Year	Surveillance Rating		Outlook
	Long Term	Short Term	
2008	AA	ST-1	Stable
2009	AA	ST-1	Stable
2010	AA+	ST-1	Stable
2011	AA+	ST-1	Stable
2012	AA+	ST-1	Stable

Source: Annual Reports 2008-2012

CRISL has reaffirmed its Long Term rating to 'AA+' (pronounced as double A plus) and Short Term rating to 'ST-1' of Islami Bank Bangladesh Limited (IBBL) through an in-depth analysis of the operational and financial performance of the bank along with all its relevant quantitative and qualitative factors. The basis of its evaluation has been the consolidated financial up to December 31, 2012 and other prevailing factors up to the date of the rating.

Long Term Rating of AA+, AA, AA- (Double A); High Safety: Banks rated in this category are adjudged to be of high quality, offer higher safety and have high credit quality. This level of rating indicates a corporate entity with a sound credit profile and without significant problems. Risks are modest and may vary slightly from time to time because of economic conditions.

Short Term Rating of ST-1; Highest Grade: Highest certainty of timely payment. Short-term liquidity including internal fund generation is very strong and access to alternative sources of funds is outstanding, Safety is almost like risk free Government short-term obligations.



5.5 Comparative Analysis of Islamic Banks of Bangladesh:

Over the years, Islamic finance has become one of the fastest growing segments in the international financial system. Islamic banks showed stronger resilience during the global financial crisis due to their anchoring in the real economy and barring from investing in financial derivatives. Global Islamic Finance got its highest pace in the last few years. The asset of this real finance reached to USD1.6 trillion and is expected to grow at a higher rate than the industry average in next few years.

In Bangladesh, Islamic Banking retained more than 18% of total deposit and 21% of total loans and advances (investment) of the banking system. Considering the growth and its role in the country's financial sector, central bank took various steps to facilitate Islamic Banking. Last year Bangladesh Bank introduced Islamic Interbank Fund Market to mitigate the liquidity and to manage the fund in a better way under Shariah principles. In the year, Islamic Banks strengthened their strategic bondage in terms of liquidity, operational uniformity, manpower development and Shariah solutions. IBBL played a catalyst role in empowering fellow Banks towards Islamization of Banking in Bangladesh. The Islamic banking community participated in different international programs that helped showcase country's Islamic banking in global forums. World reputed media like Reuters, Gulf News and Islamic Finance published features/interview on Islamic banking in Bangladesh.

There are eight Islamic Banks in Bangladesh. These are:

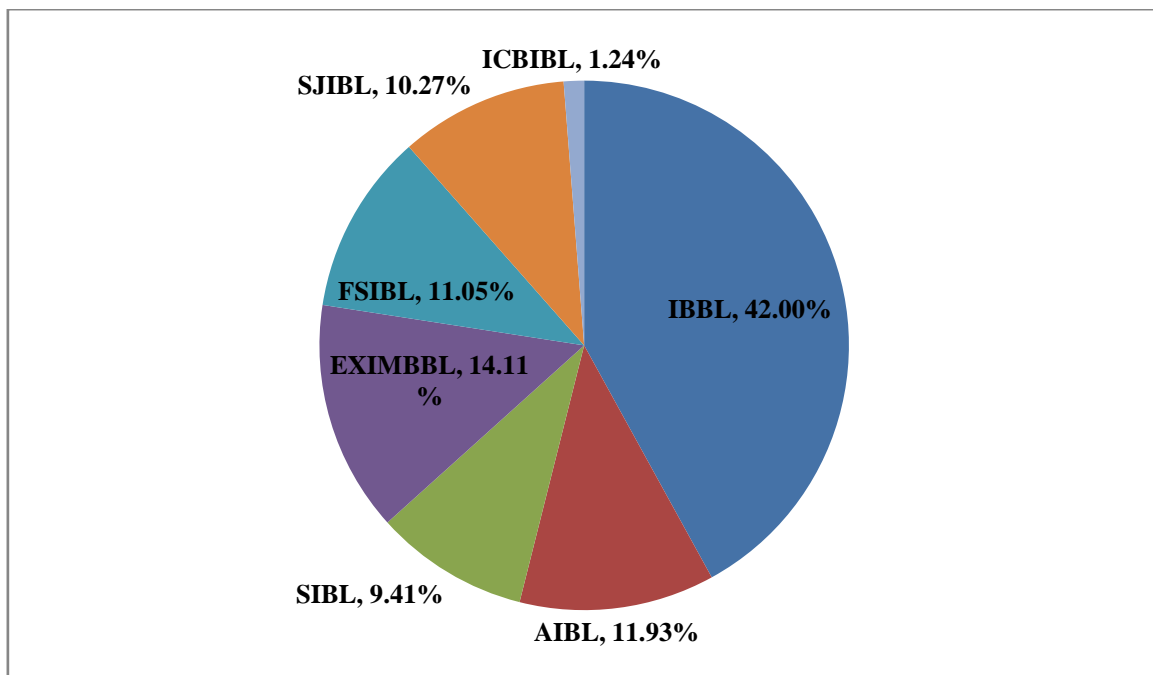
- Islami Bank of Bangladesh Limited,
- Al-Arafah Islami Bank Limited,
- Shahjalal Islami Bank Limited,
- First Security Islami Bank Limited,
- ICB Islamic Bank Limited,
- Export Import Bank of Bangladesh Limited,
- Social Islami Bank Limited,
- Union Bank Limited (Excluded due to no annual report has been published).

(For detailed calculation see annexure)

5.5.1 Total Deposits:

Name of the Bank	Deposits	% on Total	No. of Branches
Islami Bank Bangladesh Limited	417,844.14	42.00%	276
Al-Arafah Islami Bank Limited	118,683.39	11.93%	100
Social Investment Bank Limited	93,594.29	9.41%	86
Export Import Bank of Bangladesh Limited	140,369.66	14.11%	72
First Security Islami Bank Limited	109,905.56	11.05%	100
Shahjalal Islami Bank Limited	102,177	10.27%	84
ICB Islamic Bank Limited	12,381.39	1.24%	33
Total	994,955.43	100%	

Figure 5.5.1: Comparative Position of Total Deposits of the Islamic Banks of Bangladesh



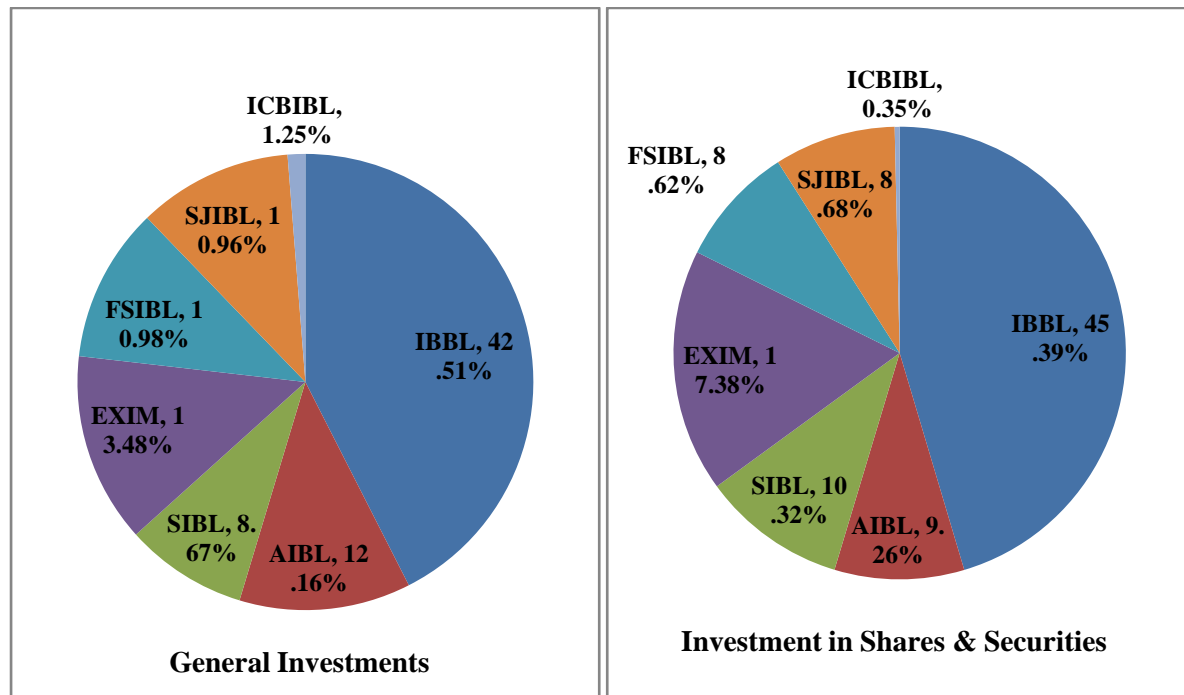
Source: Annual Reports of the Respective Banks 2012

In the comparative analysis among seven Islamic banks of Bangladesh, it has been seen that, in the year 2012, IBBL deposits are higher than other six Islamic banks of the country. By considering the number of branches and age of the bank, the total deposits of IBBL was Tk. 417,844.14 million in 2012 which is very natural for a larger and older bank in comparison with other banks. On the other hand EXIMBBL collected 14.11% deposits of total deposits of Islamic banks of Bangladesh with only 72 branches which is almost three times less than IBBL. Except ICBIBL all other Islamic banks are in a stable position in case of deposits mobilization and branch expansion.

5.5.2 Total Investments:

Name of the Bank	General Investments	% on Total	Investment in Shares & Securities	% on Total	No. of Branches
Islami Bank Bangladesh Limited	372,920.72	42.51%	27,010.07	45.39%	276
Al-Arafah Islami Bank Limited	106,650.42	12.16%	5,511.24	9.26%	100
Social Investment Bank Limited	76,024.97	8.67%	6,144.01	10.32%	86
Export Import Bank of Bangladesh Limited	118,219.99	13.48%	10,345.38	17.38%	72
First Security Islami Bank Limited	96,304.22	10.98%	5,128.48	8.62%	100
Shahjalal Islami Bank Limited	96,185	10.96%	5,163	8.68%	84
ICB Islamic Bank Limited	11,009.17	1.25%	210.57	0.35%	33
Total	877,314.49	100%	59,512.75	100%	

Figure 5.5.2: Comparative Position of Total Investments of the Islamic Banks of Bangladesh



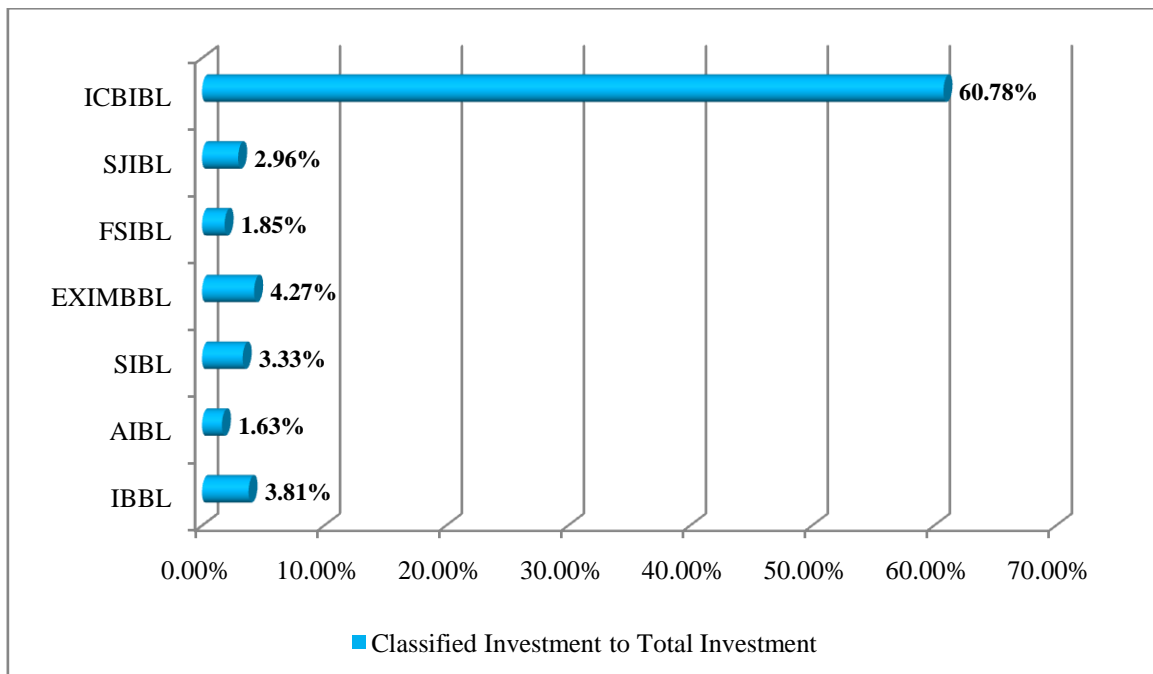
Source: Annual Reports of the Respective Banks 2012

In the comparative analysis among seven Islamic banks of Bangladesh, it has been seen that, in the year 2012, IBBL and EXIMBBL are in top positions among the Islamic banks of the country. In 2012, the general investments and investment in shares and securities of IBBL were respectively 42.51% and 45.39% of the total general investments and investment in shares and securities of the Islamic banks of the country. All other Islamic banks except ICBIBL hold within 8% to 18% of total general investments and investment in shares and securities.

5.5.3 Classified Investments:

Name of the Bank	Classified Investment	Classified Investment to Total Investment	Provision against Classified Investment
Islami Bank Bangladesh Limited	14,212.80	3.81%	6,054.35
Al-ArafahIslami Bank Limited	1,783.60	1.63%	711.63
Social Investment Bank Limited	2,532.86	3.33%	970.13
Export Import Bank of Bangladesh Limited	5,051.80	4.27%	1,460.30
First Security Islami Bank Limited	1,785.55	1.85%	779.4
ShahjalalIslami Bank Limited	2,842.27	2.96%	1,073
ICB Islamic Bank Limited	6,691.03	60.78%	3,841.38
Total	34,899.91		14,890.19

Figure 5.5.3: Classified Investment to Total Investment of the Islamic Banks of Bangladesh



Source: Annual Reports of the Respective Banks 2012

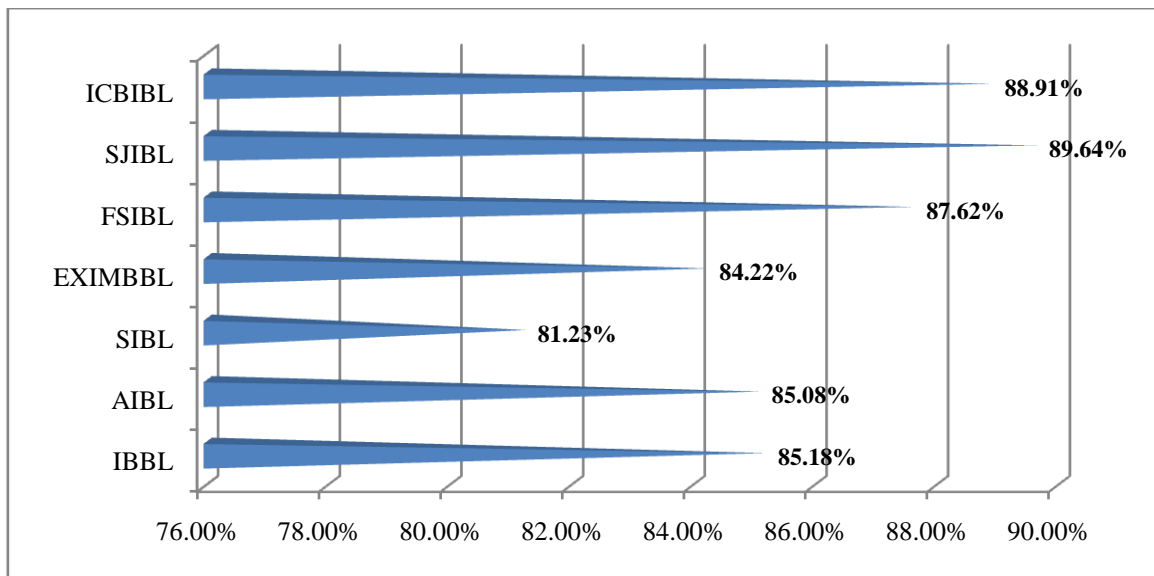
In the comparative analysis among seven Islamic banks of Bangladesh, it has been seen that, in the year 2012, AIBL and FSIBL had the lowest classified investment to total investment ratio of 1.63% and 1.85% respectively that means they efficiently distributed and recovers their investments. Although IBBL and EXIMBBL had a higher ratio of 3.81% and 4.27% respectively but by considering their total investments we may calculate a proportionate increase of their classified investment where nothing is significantly problematic or hazardous. On the other hand with fewer amounts of general investments AIBL faced a comparatively greater classified investment to total investment ratio of 3.33%. ICBIBL was in a way to make another biggest discrepancy.



5.5.4 Investment Risk related Ratios:

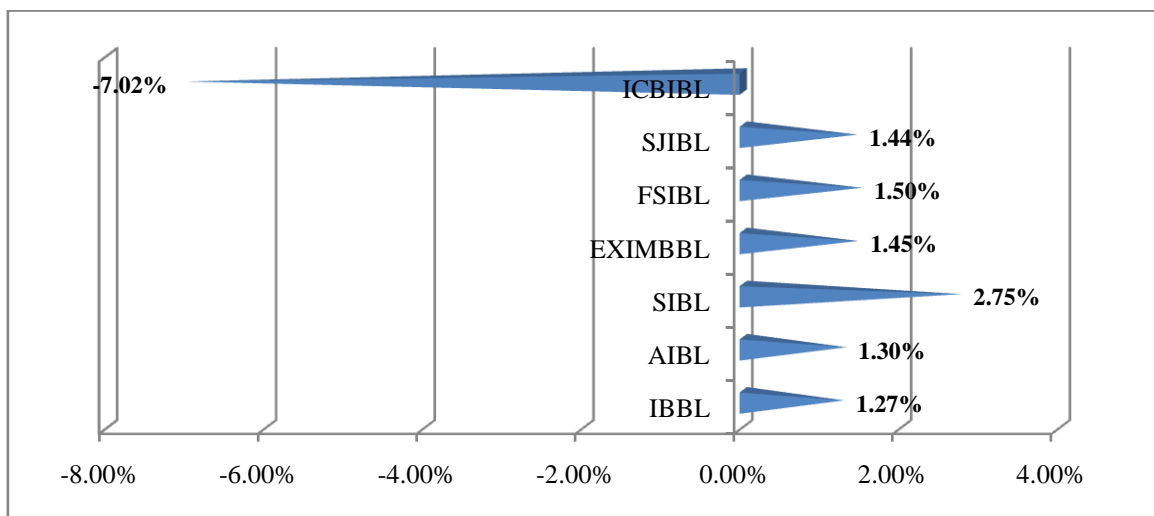
Name of the Bank	Investment Deposit Ratio	Return on Asset (ROA)	Capital Adequacy Ratio
Islami Bank Bangladesh Limited	85.18%	1.27%	13.49%
Al-Arafah Islami Bank Limited	85.08%	1.30%	11.75%
Social Investment Bank Limited	81.23%	2.75%	11.52%
Export Import Bank of Bangladesh Limited	84.22%	1.45%	10.94%
First Security Islami Bank Limited	87.62%	1.50%	10.27%
Shahjalal Islami Bank Limited	89.64%	1.44%	12.31%
ICB Islamic Bank Limited	88.91%	-7.02%	-70.51%

Figure 5.5.4.1: Investment Deposit Ratios of the Islamic Banks of Bangladesh



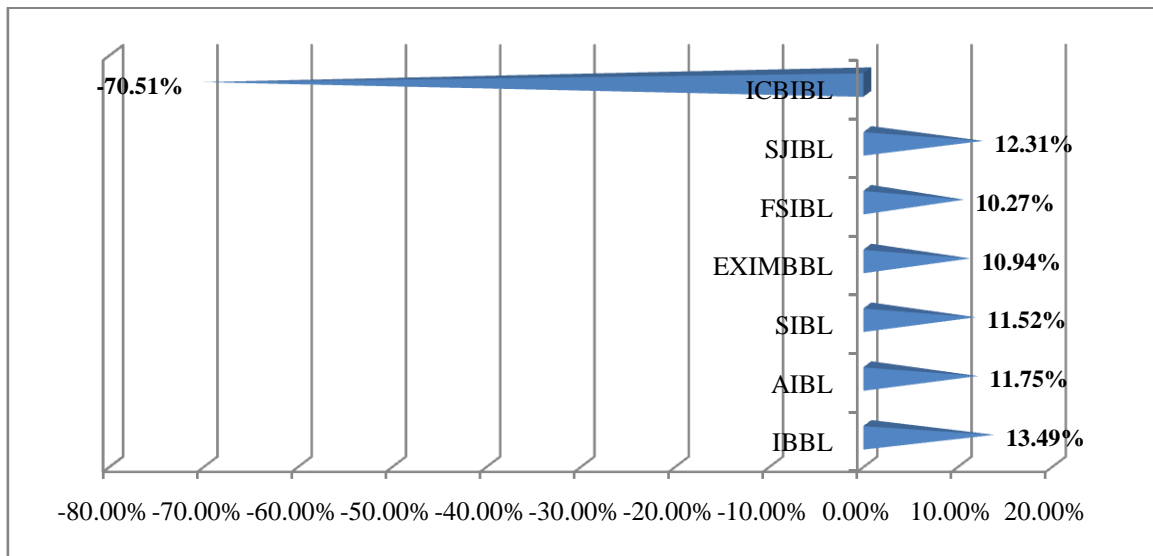
Source: Annual Reports of the Respective Banks 2012

Figure 5.5.4.2: Return on Asset (ROA) of the Islamic Banks of Bangladesh



Source: Annual Reports of the Respective Banks 2012

Figure 5.5.4.3: Capital Adequacy Ratios of the Islamic Banks of Bangladesh



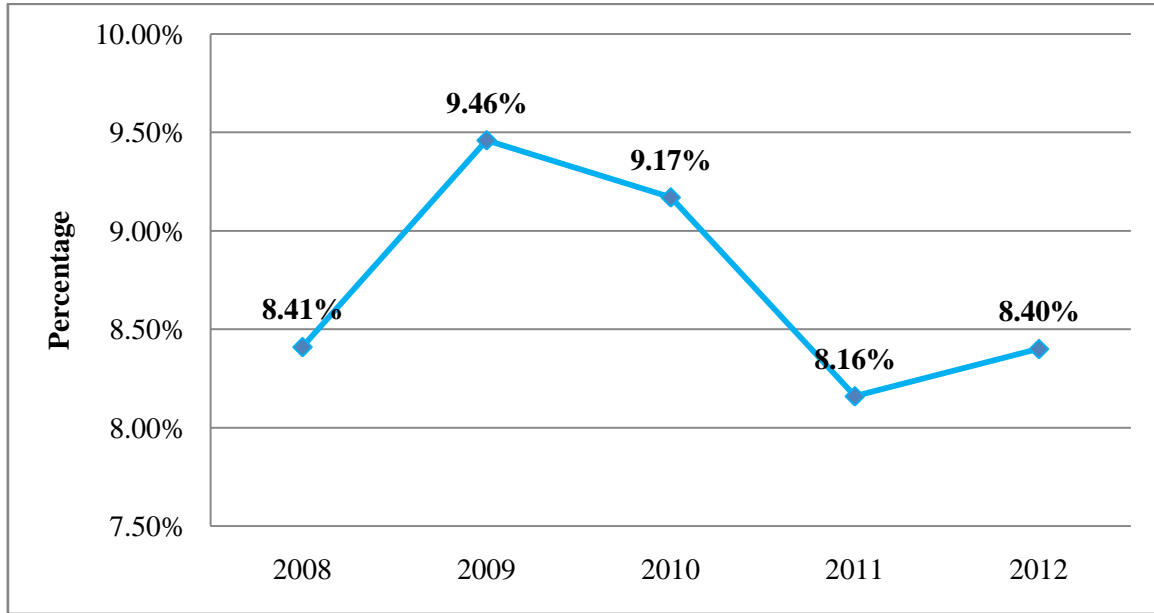
Source: Annual Reports of the Respective Banks 2012

Among the seven Islamic banks of Bangladesh, it has been seen that, in the year 2012, all the banks maintained an investment deposit ratio of less than or equal to 90% which was strictly capped by Bangladesh Bank in order to maintain sound liquidity availability. The ROA ratio of SJIBL was 2.75% where IBBL was 1.27% and other Islamic banks except ICBIBL were between them, as the largest Islamic banks of the country IBBL should have kept a larger ROA by their versatile area of Islamic banking products and services. Capital adequacy ratios of the seven Islamic banks were also maintained with the Bangladesh Bank regulations through Basel II Accord of minimum 10%. In 2012, IBBL's capital adequacy ratio was 13.49% which was highest among the other Islamic banks.

By considering and studying all the data, facts and ratio, we can make a conclusion that, Islami Bank Bangladesh Limited is the market leader among the Islamic banks of Bangladesh. They have the highest number of branches, the highest amount of deposits, general investments and investment in shares and securities. On the other hand they have the highest credit rating and maintain all the regulations imposed by Bangladesh Bank. They also implemented rigorously and properly Basel II Accord in order to maintain a sound banking environment specially a sound investment management and investment risk management. All their activities make them the strongest bank in Bangladesh as well one of the 1000 best banks in the world.

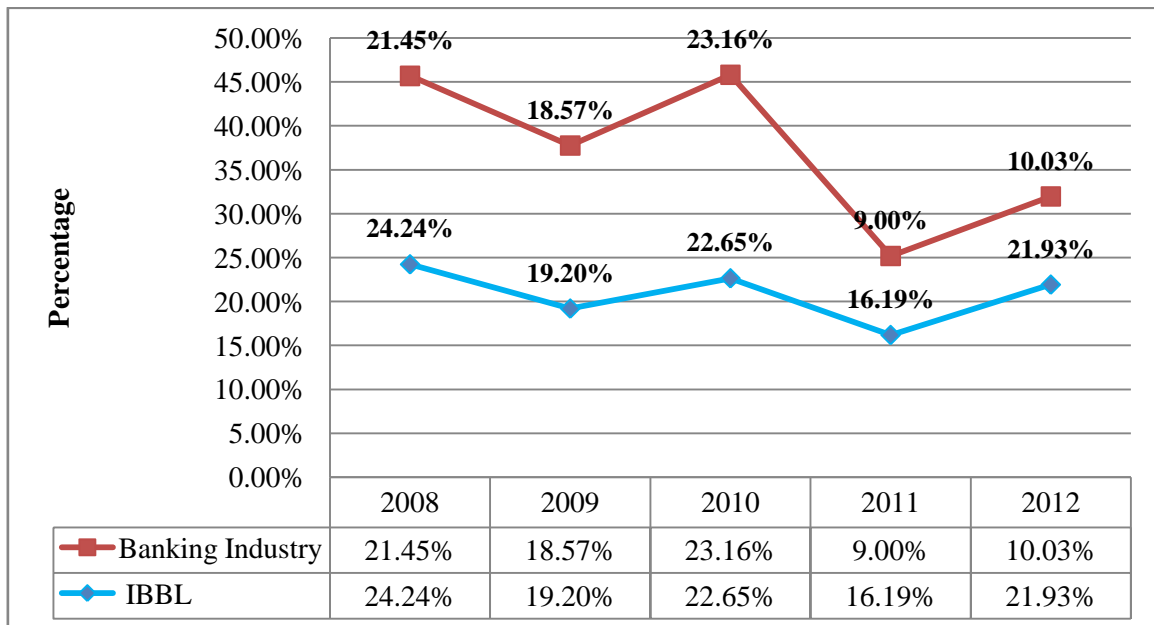
5.5.5 Market Share of General Investment of IBBL in Banking Sector:

Figure 5.5.5.1: Market Share of General Investment of IBBL in the Banking Sector



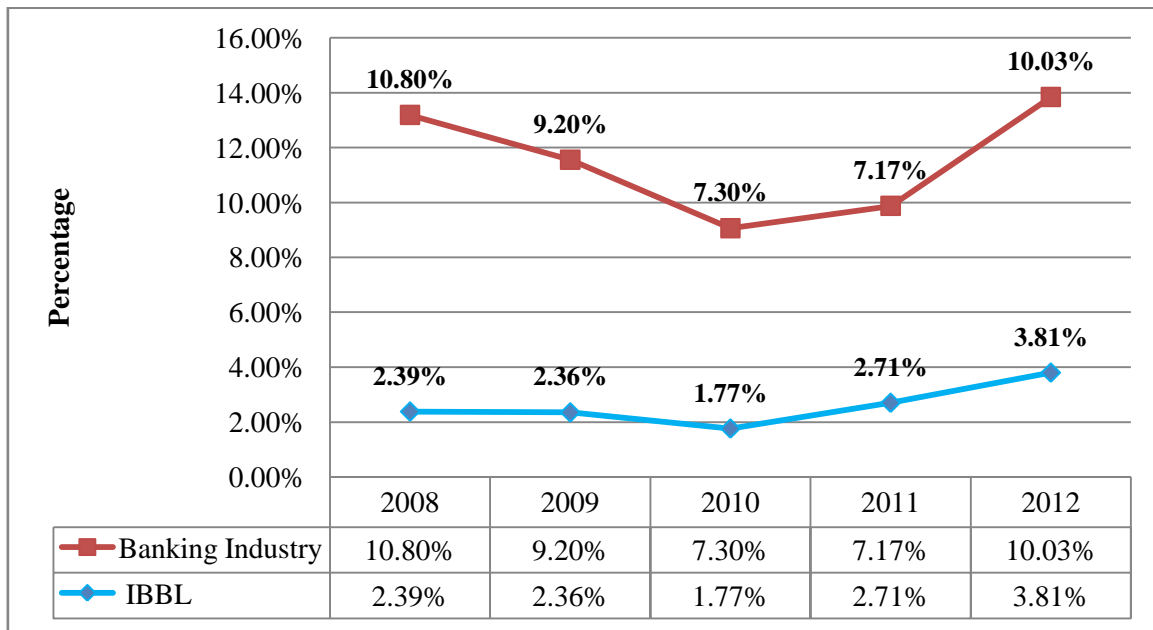
Source: Annual Reports of IBBL 2008-2012

Figure 5.5.5.2: Growth Rate of Investment of IBBL in Comparison to the Banking Sector



Source: Annual Reports of IBBL 2008-2012

Figure 5.5.5.3: Non Performing Investment Ratio of IBBL in Comparison to the Banking Sector



Source: Annual Reports of IBBL 2008-2012 and Bangladesh Bank 2011-12

By considering and studying all the data, facts and the ratio of IBBL in comparison to the banking sector of Bangladesh, we can again make a statement that, Islami Bank Bangladesh Limited has the largest market share in banking industry of Bangladesh. They have 30 years of banking experience in the banking industry and captured more than 8% total investment of the banking industry which may act as a powerful and influential participant of the industry. On the other hand IBBL's investment growth rates were higher than the banking industry average growth rates during the last five years. IBBL's non-performing investment to total investment ratios were far lower than the banking industry's average non-performing investment (loan) ratio's during the period of 2008 to 2012. All these facts give the testimony of IBBL's strongest position and contribution to the banking industry of the Bangladesh as well as to the economy of the Bangladesh.

Part Six

Findings, Conclusion and Recommendations





6.1 Findings:

Islami Bank Bangladesh Limited has now a name with its own brand both home and abroad within the 30 years of its hard and long journey. From the report I get some positive and negative findings about Islami Bank Bangladesh Limited. The findings are necessary for the bank to take corrective measures. So, I disclose the findings below:

- ➔ It has seen that, IBBL's investment management policies are effectively shaped with all rules and regulations of the Bangladesh Bank and the Islamic Shariah.
- ➔ The Investment Risk Management Committee of IBBL is entrusted to comply with the CRM Guidelines, monitoring & updating the bank's investment policy. Moreover, the committee regularly analyses the investment portfolio on the basis of Basel Guideline and attempts to restructure the investment portfolio.
- ➔ The Investment Risk Assessing and Granting Policies of IBBL are prepared by following the manual of Bangladesh Bank and the bank has formed a Supervisory Review Process Team (SRPT) as stipulated in the Bangladesh Bank's guidelines.
- ➔ General investment of IBBL was increasing year by year. Trend of general investment shows a clear direction of doubling in the last 5 years results the average growth rate per year is 20.84%. From 2008 to 2012 almost all types of welfare investment schemes became doubled to five times bigger in amount of investment.
- ➔ The bank never faced less than 85% of the investment deposit ratio during the last five years and tried to exceed 90% of the investment deposit ratio as per the instruction of Bangladesh Bank.
- ➔ According to the lending guideline of the Bangladesh Bank every bank need to segregate its investment (credit) to different sector by the basis of their credit strength, economic condition and institution's credit risk tolerance. In my analysis it has been seen that IBBL was giving 11.26% of investment in commercial sector and 29.21% credit in the industrial sector. The other sectors like real estate, agricultural and transport were neglected.
- ➔ Excellent growth has been achieved in the modes of investment of Bill Purchased & Negotiation and Quard by the bank from 2010 to 2012. But under Mudaraba mode they have very little investment because of less demand of clients and willingness of the bank.
- ➔ In 2008 with 206 branches the bank's SME investment was Tk. 37,154 million which was almost tripled in 2012 of Tk. 182,753 million with the additional 70 branches (additional 34%). The contribution of IBBL to the National SME has been raised by 5% and contribution to the total SME exposure of PCBs has been raised by 3% in 2012 from 2011.
- ➔ More than 50% of total investment was distributed in Dhaka Division. It was happening due to the position of the country's commercial hub in Dhaka. In 2010 the ratio was 9:91 which



became to 13:87 in 2012; there was a decrease of 4% gap between urban distributions of investments versus rural distributions of investments.

- ➔ The amount of classified investment in 2012 was Tk. 14,212.80 million which was 3.81% of their total investment; in the year of 2008 the classified investment was 2.39% of its total investment. So it is not a good sign for a bank and indicating the bank is in a weaker position than the previous while recovering the investment and managing its investment risk. In the classified investment the amount of “Bad & Loss” was 52.30% in 2011, which was increased to 76.15% in the year 2012. IBBL needs to focus to minimize its “Bad & Loss”.
- ➔ IBBL is keeping enough provision for classified and unclassified investments which is good enough to compare to the standard.
- ➔ From 2008 to 2012 the bank’s capital adequacy ratios were above 10% all the time indicates that the bank’s capacity to meet the liabilities and other risk such as credit risk, operational risk were satisfactory.
- ➔ In 2008 the bank’s return on investment ratio was 11.31% which was gradually increased in 2012 to 12.21%. It happened because the bank’s increased gain from the investment and decreased cost of investment simultaneously. The Bank’s average return on investment during this period was 10.97%. In 2008 the bank’s total risk weighted assets was Tk. 173,289.43 million which became about doubled in 2012 of Tk. 311,511.60 million worth. It was the result of the bank’s increased investments as well as the bank’s total assets.
- ➔ IBBL has the highest credit rating of ‘AA+’ for Long Term and ‘ST-1’ for Short Term among the PCB’s of Bangladesh according to CRISL, a renowned credit rating agency of Bangladesh which indicates the bank’s entity with a sound credit profile and without significant problems and the bank’s short-term liquidity including internal fund generation is very strong and access to alternative sources of funds is outstanding.
- ➔ In comparison among seven Islamic banks of Bangladesh, IBBL has the highest number of branches, the highest amount of deposits, general investments and investment in shares and securities. Although IBBL had a higher classified investment to total investment ratio of 3.81% in 2012 but by considering their total investments we may calculate a proportionate increase of their classified investment where nothing is significantly problematic or hazardous because they also had the highest capital adequacy ratio of 13.49% and comparable lower investment deposit ratio of 85.18% despite which caused a comparatively lower ROA of 1.27% than others.
- ➔ In comparison to the banking sector of Bangladesh, IBBL has the largest market share in the banking industry of Bangladesh. On the other hand IBBL’s investment growth rates were higher than the banking industry average growth rates during the last five years. IBBL’s non-performing investment to total investment ratios were far lower than the banking industry average non-performing investment (loan) ratio’s during the period of 2008 to 2012.



6.2 Conclusion:

Islami Bank Bangladesh Limited has been established with the aim of contributing to the balanced growth and equitable development of the country through diversification of its investment portfolio by size, sector, geographical area etc. for the bank's ultimate objective of ensuring justice and equity in the field of economy in the interest of all segments of people. The bank has been endeavoring hard towards the achievement of the above goals and making progress tremendously in this regard. With the unprecedented support of the stakeholders of all categories the bank now is handling investible fund of more than Tk. 320,000 million which is 9% of national investment and 58% of all Islamic Banks and thereby IBBL hold a strong position in the country's economy being appreciated by people of all walks of life.

The bank has been able to allocate its investible fund in such a manner that safeguards the interest of its stakeholders as well as meets the country's needs. The bank has been emphasizing on the industrialization of the country and giving due attention to the priority sectors. With this end in view and to reduce country's dependence on foreign countries a significant amount has been deployed in Spinning, Garments, Iron/Steel and Engineering. Food/Beverage, Ship Braking, Ship Building, Power (Electricity) sectors. At the same time, the bank has been laying stress on trade and imports of consumer goods/fertilizer etc. to meet the country's immediate needs.

Finally, Islami Bank Bangladesh Limited has been established with a view to conduct interest free banking to establish participatory banking instead of the debtor-creditor relationship and finally to establish welfare oriented banking through its investment operations that would lead to a justice based society.



6.3 Recommendations:

Based on findings it can be recommended to progress in future. The recommendations are disclosed below:

- ➔ The investment sanction procedure should be made quicker since competition is very hard today in the banking industry, it can be done through the creation of sub-department of investment department who will only be liable for sanctioning investment.
- ➔ An Islamic bank earns its principal revenue from profit on investment. To avoid investment risk as much as possible through minimizing adverse selection, before sanctioning any investment (loan) the officers of the bank have to observe whether every aspect of principles of lending is filled and other things such as credit requirement, accountability, prepayment of loans, collections, insurance and other required fields are covered or not.
- ➔ An energetic investment recovery unit should also be formed to manage directly accounts with sustained deterioration of investment. To encourage investment recovery unit incentive program may also be introduced.
- ➔ SME Investment of IBBL was increasing very rapidly during last five years. The bank should keep it up in order to make their position stronger and to take them as a role model as the contributor on SME sector in this country which will inspire others to come forward.
- ➔ The bank provided the maximum amount of investment focusing commercial and industrial sectors in urban areas mainly on Dhaka Division and Chittagong Division basis. To help the country's development regionally equal and take the bank as amiable to mass people countrywide, the bank should give more accentuate to make their fund available as functional to rural based industries and organizations alongside diversified industries which may act as the factors to minimize the investment risk of the bank.
- ➔ In order to lessen the classified investment, interested customers for investment should be analyzed more cautiously and flawlessly. It can be made by gathering and accumulating customers' information through the online CIB Report or historical activities of the customers toward investment so that their classified investment will be less.
- ➔ As IBBL holds the highest credit rating, regularly maintains all the CRM regulations imposed by Bangladesh Bank and implements Basel II Accord rigorously in order to maintain sound investment risk management. The bank should always be aware, ready to respond quickly against competitors' actions as well as different economic conditions, bring new and innovative investment products and services, utilize advanced technical and technological means to be quickest and errorless, arrange various investment risk related training and workshop for the employees regularly etc. in order to keep their current position among the Islamic banks of the country as well as the banking industry of Bangladesh and be placed in a better position in the upcoming future.



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Annexure

I. Investment Memorandum or Investment Proposal:

The Investment Memorandum or Investment Proposal should contain:

- Correct name of the borrower.
- Borrowers office, business, show room and factory adders with phone number.
- Account number and date of account opening.
- Nature of business.
- Date of establishment of business or date of incorporation.
- Date of commencement of business.
- Business net worth.
- Banking relationship history.
- Name of individual borrower or proprietor or partners or directors, status in the company, percentage of share holding of the director in the company or firm, age, present (residential) and permanent address with phone number.
- Personal net worth of the individual or proprietor or partners or directors.
- Name, present (residential), permanent address. personal net worth, A/C number, Business particulars, status of liability/allied liability etc of the guarantor.
- Liability of the client/allied concern with our and other banks.
- Recycling or periodical adjustment of the existing credit facility during last 3 years.
- CIB status.
- Assigned Risk Grade.
- Amount of facility (existing plus proposed)-on one obligor basis.
- Credit allowing capacity of our bank (as per Bangladesh Bank single exposure limit).
- Facility Structure:

<ul style="list-style-type: none">i. Nature of advance.ii. Amount of limit.iii. Purpose.iv. Margin or equity.	<ul style="list-style-type: none">v. Interest, commission, other charges.vi. Mode of repayment.vii. Validity/Expiry.
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- Security:

<ul style="list-style-type: none">i. Primary.ii. Collateral.iii. Others.iv. Cost of project (where applicable).v. Land.vi. Building.	<ul style="list-style-type: none">vii. Other structures.viii. Machineries etc.
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- Working capital assessment or assessment of the requirement.
- Business performance of the client or allied concerns with our bank/other banks (last 4 years).
- Earnings from the client (last 3 years) and projected earnings from the relationship.
- Sales profitability (last 3 years), projected sales.
- Important ratios (where applicable).
- Cash flow.
- Financial highlight.
- Management profile.
- Capital structure.
- Constitution.
- Experience of borrowers, business skills, management and successions.
- SWOT.
- Major 5 Competitors.
- Possible risks and risk mitigating factors



II. Comparative Analysis of Islamic Banks of Bangladesh:

Name of the Bank	Deposits	Investment (excluding Investment in Shares and Securities)	Investment in Shares & Securities	Total Classified Investment	Classified Investment to Total Investment	Total Provision against Classified Investment	Investment Deposit Ratio	Return on Asset (ROA)	Capital Adequacy Ratio	Number of Branches
Islami Bank Bangladesh Limited	417,844.14	372,920.72	27,010.07	14,212.80	3.81%	6,054.35	85.18%	1.27%	13.49%	276
Al-Arafah Islami Bank Limited	118,683.39	106,650.42	5,511.24	1,783.60	1.63%	711.63	85.08%	1.30%	11.75%	100
Social Investment Bank Limited	93,594.29	76,024.97	6,144.01	2,532.86	3.33%	970.13	81.23%	2.75%	11.52%	86
Export Import Bank of Bangladesh Limited	140,369.66	118,219.99	10,345.38	5,051.8	4.27%	1,460.3	84.22%	1.45%	10.94%	72
First Security Islami Bank Limited	109,905.56	96,304.22	5,128.48	1,785.55	1.85%	779.4	87.62%	1.50%	10.27%	100
Shahjalal Islami Bank Limited	102,177	96,185	5,163	2,842.27	2.96%	1,073	89.64%	1.44%	12.31%	84
ICB Islamic Bank	12,381.39	11,009.17	210.57	6,691.03	60.78%	3,841.38	88.91%	-7.02%	-70.51%	33

Source: All the data presented in this table are collected from the respective bank's most recent annual report for the year of 2012