

**Report On
Departmental Operations of Orion Group, Moral Hazard & Excessive Risk taking**

By
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**An Internship Report Submitted to the BRAC Business School in partial fulfillment of
the requirements for the degree of MBA**

BRAC Business School,
BRAC University
November, 2021

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Declaration

It is hereby declared that

1. The internship report submitted is my/our own original work while completing degree at Brac University.
2. The report does not contain material previously published or written by a third party, except where this is appropriately cited through full and accurate referencing.
3. The report does not contain material which has been accepted, or submitted, for any other degree or diploma at a university or other institution.
4. I/We have acknowledged all main sources of help.

Student's Full Name & Signature:

FarihaHussain
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Supervisor's Full Name & Signature:

Riyashad Ahmed
Assistant Professor, Brac Business School
Brac University

Letter of Transmittal

Riyashad Ahmed
Assistant Professor,
Brac Business School
Brac University
66 Mohakhali, Dhaka-1212

Subject: Departmental Operations of Orion Group/ Moral Hazard & Excessive Risk Taking

Dear Sir,

It is indeed a great pleasure to be able to hand over the internship report prepared as a part of the requirement for my Bachelors program under BRAC Business School of BRAC University. I have worked with utmost sincerity and successfully completed my internship report.

Working with Orion was a great learning experience for me as it teaches the differences between practical and theoretical work. I hope you will find the report to be objective and reliable. I have to make this report as comprehensive as possible, which is why there may be some discrepancies due to various restrictions. For this reason, I beg your kind consideration in this regard.

I would like to take this opportunity to thank you for all the support and guidelines that you have provided, which I hope to continue getting in the future.

Sincerely yours,

Fariha Hussain

17264103

Brac Business School

Brac University

Date: November, 2021

Acknowledgement

I convey my sincere gratitude to my academic Supervisor Mr. Riyashad Ahmed from BRAC Business School. Without his kind direction and proper guidance, this study would have been impossible for me. In every phase of the project, his supervision and guidance shaped this report to be completed.

I would like to take this opportunity to thank my supervisor at Orion Group and my co workers for assisting me with any information needed regarding the report.

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Overview Of Internship

Name: Fariha Hussain

ID: 17264103

Program: MBA, Major in Finance

Period: 2017-2020

Company Name: Orion Group

Department/Division: Corporate Affairs

Address: 153-154 Tejgaon I/A, Dhaka

Supervisor's Name: Ferdous Jaman

Position: Company Secretary

Job Description

- Preparation of Annual Report of the listed concerns of Orion Group.
- Corresponding to emails of the Company Secretary on a daily basis.
- Checking and finalization of daily class wise and shift flyover report with analysis for top management on a daily basis..
- Preparing any official report assigned by the Supervisor.
- Corporate Affairs related activities like checking and finalizing meeting minutes, write up, briefing and other assigned activities.

My Contribution to the Company

My supervisor is Company Secretary therefore I need to correspond to many emails coming from abroad, communicate with foreign banks and also need to work on the Annual Report of the company. My communication skill is better in English as my background is English medium and that really helped to draft an email, write a report and make write ups for Annual Report. As my competency level lies in English, I can help my boss in preparing official documents in English and also maintain a network with the international stakeholders. My bachelors in Economics has also made me capable of making official reports consisting of economic data relevant to the business of the company.

Benefits to the student

It has been over 3 years I have been working as an Executive in the Department of Corporate Affairs in Orion Group and in these three years I gained the experience of working in a large corporate culture. The job has benefited me in developing my communication and interpersonal skills, working with people from various fields and dealing with them. It has also taught me to be punctual about any given assignment and how to be an effective team player. As I have been working for quite a long time, it has helped me to be more independent financially and socially. This 3-year job experience will make my resume stronger for seeking a better job in other local giants/multinational companies in future.

Recommendations

Orion group is a well recognized conglomerate of Bangladesh providing lucrative opportunities of working in various fields and gaining experience. As I am working in the Corporate Affairs department, my scope in the field of finance is very limited as my subject for my major is Finance. The Corporate Affairs department is confined within the tasks of working personally with the higher management of Orion, preparing Annual Report of the listed concerns and organizing meetings. It limits the scope of gaining practical skills in a diversified field which can enhance the skill level and also help to gain practical knowledge. The management must consider this issue and work on how to bring transformation by introducing more highly skilled tasks and diverse the scope of learning in the Corporate Affairs department as it will play a crucial role in the employee's future career development in terms of his/her working experience by focusing on diversification as well as specialization.

Objective

The objective is to analyse Orion Pharma Ltd, a renowned pharmaceutical company in Bangladesh and concern of Orion Group, its different business segments to gain concise knowledge about its entire corporate management system, operational and financial activities. The report has emphasized on the company's corporate governance policies, board of directors, management policies, financial operations, its competitive and industrial policies and how advanced the company is in terms of technologies. Company's strength and weakness has also been identified by SWOT analysis and the market forces which are responsible for driving the business.

Limitations & Significance

Due to Covid-19 pandemic, it was difficult to conduct primary research on the company as employers/employees were all working from home to maintain social distance. No survey was possible to run or take interviews from individual employees. All the information is collected from secondary sources provided that sources are all reliable and contain all valid information. The significance of the report is, it gives a comprehensive idea about the company's structure, its management system and policies.

Methodology

With a view to completing the report the information has been collected from the secondary source only. The report covers the organisational structures, its financial operations, corporate governance system, its industrial and competitive analysis and its IT system. All this information is collected from the recent Annual Reports, company's website and company's various business reports. The information is known to be precise and updated according to the current state of the company's position.

Overview of the Company

ORION GROUP is a leading and continuously thriving corporation and a legendary brand name in the business arena of Bangladesh and beyond. Orion has a long history of determination, commitment towards excellence, integrity, and a firm promise to deliver value to its consumers and clients since early '80s. Orion Group is endowed with a highly diversified portfolio of Pharma & Healthcare, Power Generation & Energy, Shipping, Infrastructure Development, Real Estate & Construction, Cosmetics & Toiletries, High-tech Agro Products, Consumer Products, Food & Restaurant Chain, Textiles & Garments, Home Appliance sectors and so on. Orion in recent times has exclusively focused in Power Generation & Energy, Consumer Products and Infrastructure sectors

Orion Pharma Limited (OPL) was formed as a pharmaceutical manufacturing company in 1965. With the mission to serve the ailing humanity around the globe, Orion Pharma started its operation nearly five(5) decades ago, and after a great run of success the company today has proliferated out into one of the leading pharmaceutical companies in Bangladesh. The company has its name listed with Dhaka Stock Exchange (DSE) and Chittagong Stock Exchange (CSE) from the year 2013. OPL also owns 21.76% shares of another concern of

Orion Group named Orion Infusion Limited (OIL) which is known for producing Large Volume Parenteral (LVP) & other life saving injectable products. OIL is also listed in DSE from the year 1994 and in CSE from the year 1996. With the number of pharmaceutical giants increasing spontaneously in our country, competition within the industry is fierce. OPL believes in exceeding boundaries to deliver life changing results. OPL is a healthcare company dedicated to the improvement of human health by producing world class general medicines of supreme quality and distributing them globally. The company always believes in 'Quality never ends' and refuses to settle for anything until it exceeds the existing standard. The company comprises the production of capsules, tablets, syrup, suspension, injection, dry powder for syrup / suspension under different classifications like anticancer, cardiovascular, antibiotics, anti-diabetics, anxiolytics and others. With growing markets and an increasing reach, this pharmaceutical powerhouse is operating with one hundred & twenty (120) brands and two hundred & thirty one (231) presentations with the anticipation of rapid growth and innovation in the years to come by staying compliant with the ISO-9001:2015 guidelines and Good Manufacturing Practices (GMP). The new pharmaceutical manufacturing plant of Orion Pharma Limited named as Pharma Park is located in Siddhirganj, Narayanganj, by the bank of river Shitalakshya. The plant is well designed and well equipped with all latest facilities and state-of-the-art technologies and contains facilities with the imported equipment like ETP, Air Compressor, Chiller, WTP, dust collector and many more with the aim to expand and upgrade the current quality & quantity production.

Management

At Orion Pharma Limited, the Board of Directors is independent of management and has no association that can interfere with their judgment or scope of work. The Nomination and

Remuneration Committee (NRC) has been assigned to assist the Board to review the independence of the Directors as well as the sub-committee members. Both the Independent Directors have submitted a signed and dated declaration to demonstrate their independence to the Board of Directors. The Board of OPL determines and declares at the end of the year that all of its members along with those of its sub-committees are independent.

Orion Pharma Limited has a flexible corporate culture which is always open to improvement. We are a team-oriented company and give plenty of room to our employees for opportunities to learn and fast-track their career. Our human resources practices are one of the best in the country and we are committed to establishing equal employee opportunity for our valued employees. Our philosophy is to make the appropriate compensation and benefits to the service employees provide the company. Integrity is one of our core values and we believe in being transparent and fair in all our dealings by providing the best quality to the customers along with fulfilling our responsibility towards the society.

Senior management team

In last financial year's annual report, we reported that we had a management team which was established by making the heads of different departments as its members with the headship of the Chief Executive Officer. During the year under review, there is a modification in the composition of our management team. Mr Md. Ibrahim Khalil, Head of Internal Audit and Compliance; Mr. Md. Zakir Hossain, AVP – Production and Mr. Md. Faisal R Ferdous, VP – HR have been included in the team. The other members of the team are Mr. Salman Obaidul Karim, Chief Executive Officer; Mr. Samaresh Banik, Chief Financial Officer; Mr. Md. Arif Hossain, SVP –Marketing Operations & Commercial. The senior management team of the company is involved in full control of the company's affairs and is also accountable to the Board. It builds the confidence of the Board by ensuring that all the activities carried out by

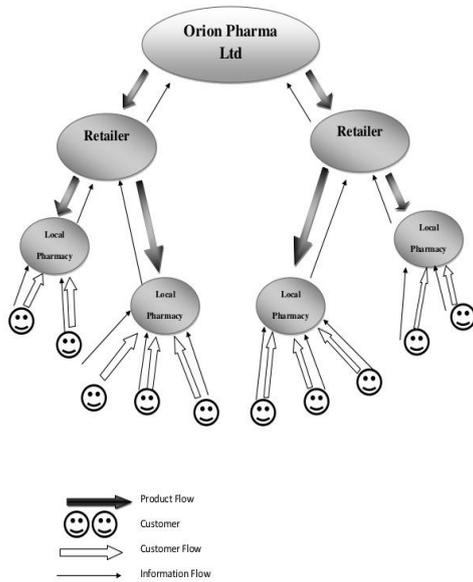
them are consistent with high ethical confidence of the Board by ensuring that all the activities carried out by them are consistent with high ethical standards. The Board of Directors of Orion Pharma Limited has always prioritized the assurance of protection of the interest of stakeholders by means of maintaining integrity of financial reporting, effectiveness of risk management and internal control systems and related corporate governance and compliance matters. The responsibility of ensuring these important matters is exclusively delegated to the Audit Committee (AC), a sub-committee of the Board, appointed by and responsible to the Board of Directors of OPL. At Orion Pharma Limited, the Board of Directors through its Nomination and Remuneration Committee is responsible for overseeing the succession planning. The management team is particularly assigned to assist the Board and the committee with senior leadership succession planning when necessary. The company always plans ahead the succession keeping factors such as skills and knowledge, diversity, professional background, expertise etc. into consideration.

Marketing Management

Customers and consumers are the key stakeholders of OPL. Their satisfaction is the foundation for our business growth and expansion. Serving them with the right products at the right time is always our prime concern. The company gives high importance to seek their opinion or complaints about our products and to gauge how the company is perceived by our customers and consumers. In line with this, product complaint forms are available and also customer satisfaction surveys and market surveys are carried out and the findings are considered to improve business, products and/or overall customer experience.

Orion Pharma Limited is dedicated to its valued customers with products of excellent quality, through continuous improvement in process & technology, sourcing of best quality raw

materials, complying with the guidelines of Good Manufacturing Practices (GMP) and the requirements of ISO 9001:2015.



Financial Performance & Accounting Practices

Financial capital represents the fund used to facilitate the process of building and strengthening the foundation for our ability to develop and create value for our providers of funds. The main sources of this capital are equity, debt, earned surplus etc. which are raised through the financing, operating and investing activities. After deduction of the dividend for shareholders, the surplus earnings generated from business activities ultimately make our financial capital base stronger and this is the main source of internal fund raising. We are operating in a capital-intensive pharmaceutical industry and are now in the business

expansion stage for which OPL tends to retain more of its earnings to reinvest rather than paying them out to shareholders. Other than internal fund raising options i.e. retained earnings, we also focus on availing long as well as short term loan facilities from different banks as we are expanding our business operation by increasing our product lines. Financing via Export Credit Agency (ECA) is currently one of our key external funding options. We plan the effective utilization of our financial capital and try to maintain optimum capital structure. We analyze various factors for the selection of fund providers particularly for loans, including project financing and working capital loan. Major issues considered includes However, the company are constantly focusing on our actions to sustain growth, develop operations and ensure the highest return for the shareholders and strengthen the financial position. Funds generated are being used for the maintenance of regular business operation, repayment of loan along with interest expenses, investing activities and dividend payment.

Information System

To illustrate progress towards achieving the performance goals of the company our Information Technology (IT) continues to and innovative ways to move forward with more advanced technologies. Our IT department is introducing new applications or updating the existing one to simplify the day to day official tasks and strengthening the technological base of Orion Pharma Limited. Desktop and Server Virtualization, Mobile Technology, renegotiating maintenance contracts, that provides security and reliability needed and looking into software applications that will create employee efficiencies. Many of our software were purchased from vendors; again many of OPL's software were developed by OPL's highly skilled internal software developers. The IT department is in charge of the following. There are some useful online applications which have been created by Orion Pharma's IT department to make all kinds of operations and tasks fast and accessible.

Orion Online Solution

Orion Online Solution is the application where different departments can access it and make utilization of it for various purposes. Orion Portal is a widely used mobile app by the employees because they can get information about their attendance, appraisals, monthly pay slip etc from anywhere they want to. Recently, Orion Pharma introduced few online applications which have eased the field force's regular job tasks. OPL also takes online exams for recruitment and promotion purposes using the software known as Orion Online Exam. Some of the applications Orion Online Solution includes e-bill process, MIS system, e-attendance & leave system, vehicle system, fund requisition etc.

Industry & Competitive Analysis

Orion Pharma Limited has made an effort to portray all its activities, carried out in its regular business to create value for its potential stakeholders, by a value chain model. In order to do this, OPL has adopted Porter's Value Chain Analysis to examine all of its activities, the way in which value chain activities are performed, to see how they are connected and how these activities are affecting costs and profits. This analysis helps OPL to understand the sources of value for our company and for society.

Support Activities

Firm Infrastructure

- The design of the building and factory is good and reflects modern concept
- Prevalence of good governance
- Practice of strong code of business conduct
- Structured departments and hierarchical system
- Improved communication between different departments through the intranet
- Better accounting and financial management practices

Human Resource Management

- Strong HR team to recruit, train and motivate employees
- Excellent corporate culture for teamwork and leadership development
- Competitive remuneration package and compensation benefits
- Ensuring employees' health and safety issues
- Offering safe and healthy working environment
- Non existence of gender discrimination

Technology Development

- IT department with required expertise and experience who supports both IT infrastructure and software
- Automated Central Distribution Centre, distribution channels and depots
- Real time access to sales records from all depots

- Strong IT department is continuously developing many customized software
- Efficient R&D departments continuously engaged with developing new products or upgrading existing one

Procurement

- Direct contact with suppliers
- Good cross border relationship
- IT based procurement planning and inventory management system
- Practice of strong code of business conduct
- Structured departments

Primary Activities

Inbound Logistics

- Good relationship with suppliers
- Sourcing supplies of high quality materials
- Efficient storage facilities- easy storage and retrieval
- Inventories are dealt with swiftness and efficiency
- Hired and owned vehicle fleet
- Supply schedules are matched with production

Operations

- Automated manufacturing processes
- Comply with compliance in every aspect and step of the production.
- Quality control and inspection

- Order fulfillment on time
- Real time inventory and sales tracking system

Outbound Logistics

- On time delivery through 58 customized vehicles
- Inventory management
- Efficient dispatch and delivery system
- Emergency resupply
- Emergency shipment
- 31 Regional Sales Offices and 19 depots all over the country
- 1 Central Distribution Cell

Sales & Marketing

- Efficient sales force of 1,106 number of employees
- Regular training of the sales team through sales training department
- Customer management
- Entering new and emerging markets
- Sales analysis
- Market research
- Branding and promotion of products

Service

- Product complain form
- Customer survey and seeking feedback

- Structured approach to understand the requirements of individual customers
- Fast response to customer requirement
- Expired product management

SWOT Analysis

This SWOT (strengths, weaknesses, opportunities and threats) analysis is a process where the management team identifies the internal and external factors that will affect OPL's performance. The company's strengths and weaknesses are the internal factors whereas opportunities and threats deal with factors external to the company. This helps the overall corporate planning process in which financial and operational goals are set for the upcoming year and strategies are created to accomplish these goals.

Strength

- OPL has overseas marketing network in eleven (11) countries, products of OPL have already been registered in other five (5) countries and in the process of registering products in more than ten (10) countries;
- Strong corporate and company brand image;
- Strong, transparent and professional management;
- Strong demand for our cardiovascular drugs;
- World leading generics are available in our product line;
- The biggest Pharma Park in the country with huge production capacity including capacity of hi-tech products;

- Strong and country wide distribution network ensures supply of products up to retail level;
- High quality products with extensive product lines;
- Active participation in CSR activities;
- Front runner of some generics for the 1st time launched in Bangladesh; and
- Existence of competitive advantages

Weakness

- Emerging new international markets;
- High annual growth rate of pharmaceutical industry in Bangladesh with lot of potentials;
- Increasing demand for quality healthcare products due to the increase in consciousness among people;
- Grant for the least developed countries, including Bangladesh, an exemption from obligations to implement patents and data protection for pharmaceutical products until 2033 as per trade related intellectual property rights (TRIPS); and
- Chronic diseases continue to be the major factors for mortality worldwide, with developing nations suffering from high levels of public health problems related to chronic diseases.

Opportunities

- Lack of presence in international market particularly in Europe and in USA;
- Sub standard position in few areas of HR indicators;
- Lack of branded product recognition in local market;
- Low investment in R&D; and
- Lagging behind in grabbing the opportunities to introduce new potential therapeutic products.

Threats

- Increase in competition both in local and overseas pharmaceutical market day by day;
- Change in rules and regulations from Bangladesh Food & Drugs Authority can make products out of the market;
- Exposed to foreign currency fluctuations in case of importing raw materials and exporting products;
- Interest rate fluctuations can have an adverse effect on the business sustainability; and
- Political instability and turbulence and disruption by the law enforcement agencies may disrupt supply chain, production and hamper cost competitiveness.

Analysis of Five Forces

Industry analysis is a vital part of the decision making process in business. In this case Michael Porter's model is a widely used tool for industry analysis. This model identifies five core competitive forces and by gaining knowledge about these forces and how they impact on the business, decision makers can make better decisions and plan better. From that point of view an analysis of the pharmaceutical industry of Bangladesh in terms of the five forces is given here:

Threats of entry posed by new or potential competitors: (*Low*)

- Economies of scale achieved by the established businesses;
- Huge capital intensive business;

- Access to the distribution channel is difficult;
- Government rules and regulations, particularly regulatory permission from the drug authority; and
- Customers' brand loyalty

Degree of rivalry among existing companies: (*High*)

- High rivalry exists among the companies in the industry as same medicines under different brand names are available;
- Industry is benefited from the strong demand of the consumers; and
- In the long run companies require low fixed cost and high working capital

Bargaining power of buyers: (*Low*)

- Price sensitivity is low as government strictly maintains the retail price of lifesaving medicines, so consumers have little room for switching;
- Companies influence medical practitioners, wholesale and retail shops for prescribing their products;
- If any drug is prescribed by medical practitioners or physicians, the end user prefers to buy that without thinking about any alternative; and
- As medicine is related to health issue which is one of the basic needs, it is very important for people and their bargaining power is low.

Threat of substitute products: (*Medium*)

- There exists threat from generic drugs, because generic drug companies do not expend in research and development of new drugs. So they can sell their medicines at cheaper rates. So threat exists in generic competition; and
- On the other hand if any drug is prescribed by medical practitioners then end user must have to buy that without any choice left. Even though end customers can switch to other brands due to the unavailability of suggested brands.

Summary & Conclusion

Orion Pharma is one of the very old pharmaceutical companies running in Bangladesh. Its production is on a massive scale, producing many varieties of medicines. To support its mass production and keep up with the revenues and gross profit every year, OPL has invested wisely on capital required, employing people with immense potential for its efficient management. The company is also ahead in terms of technologies and its infrastructural setup. Considering its financial positions in the last 5 years, the company has fluctuating figures of its revenues, gross profit and after tax profit which means the consistency is lacking. It has its highest profitable values in the year 2016 and lowest in the year 2018. Various economic factors and competition in the market have affected the company's business and its profit resulting in weak performance in recent years. To conclude, as the number of pharmaceutical companies are growing the competition is

getting more challenging as there are new innovations and products emerging in the market and OPL being one of the very first pharmaceutical companies , is pretty much lagging behind in competition which is also the reason for its deterioration in profit.

Recommendation

Orion Pharma Ltd is a distinguished company in Bangladesh which played a crucial role in the pharmaceutical industry for the past few decades. But its declined value in profit in recent years has made its financial position quite weak. The main reason is its poor marketing strategies. OPL's poor marketing structure has led to lower sales for which reason its profit margin stays low and also declined significantly in the past few years. According to the shareholders, the management must emphasize on its marketing policies and should come up with more innovative and modern ideas to be able to compete with the emerging pharmaceutical companies. As OPL has its own subsidiaries to support its financial operations, the company must look forward to investing more in its marketing segments to promote its supreme quality products which are being exported every year and are equally good as any other products produced by its competitors. The company must come out of its primitive selling strategies and be more flexible in adopting the modern marketing policies to survive in the competition which will eventually boost up its sales and revenues hence, increasing the profit margin.

Background

When money is given to someone, it must be ensured that it will be returned with interest. However, this is less likely if the money is misused or lost through excessive risk-taking. *Moral hazard* is the risk that the receiver of funds will not use the money as was intended or they may take unnecessary risks or not be vigilant in reducing risk. The primary reason why people give their money to financial intermediaries instead of lending or investing the money directly is because of the risk that is present from the *information asymmetry* between the provider of funds and the receiver of those funds. A seller knows more about the sale item than the buyer. Likewise, a borrower knows more about his financial condition and his future prospects than the lender. The 2 types of risks that are present when there is information asymmetry:

1. Adverse selection, which is a risk exposure that exists before the money is lent or invested and
2. Moral hazard, which is a risk after the financial transaction.

Selecting whom to give more of your money is a very important part of controlling risk. In fact, without precise and detailed information about those seeking funds, theory goes that one would have to charge an average price for the money or sale item. But an average price would cause those who are better risks or have better products to shun the offer, while those with higher risks will seek the offer, resulting in *adverse selection*.

The moral hazard problem of the Asian financial crisis and others could be a lesson to all the emerging nations including Bangladesh. Moral hazard can bring an outsized shock to the financial system of a country specifically to the banking sector. A design of optimal contract

among four parties including issuers, credit rating agencies, investors and regulators can help in reducing the negative impact of moral hazard problem.

Objective

In this paper, the performance of the financial institutions are discussed as well as its excessive risk taking and how moral hazard can be a barrier for the institutions when providing loans to a newer organization and making risky investments. The key objectives are to discuss the factors influencing the financial institutions' to take excessive risks and analyze the association between moral hazard and investments on risky assets during the financial crisis along with the role of government in restoring the stability in the financial system.

Significance

The significance of the study on excessive risk taking by the financial institutions will provide a precise idea on how the financial crisis and moral hazard turn the loan giving business more challenging. Undertaking excessive risk can lead to poorer performance and failure of the financial system. Financial institutions lose their confidence level of performing alone and always seek government support which can make the government spend more on giving backups to those institutions instead of spending money for development of the country and its nation. The following analysis and findings will also give a distinct idea of the impact of moral hazard and how the financial institutions are adopting and formulating new strategies to overcome the tendency of excessive risk taking.

Methodology

Based on the entire paper the information illustrated and discussed are mainly collected through secondary sources like published journals, newspaper articles like that. The data and analysis are done through qualitative research method describing the financial projects and

risk associated in making huge investments on risky assets to get higher return by the various banks worldwide and how undertaking excessive risky projects leading them to increasing moral hazard problems followed by the government coming forward to protect them so as to protect the sovereignty of a country as well as protecting the banks from getting collapsed. The data and analysis part consists of a chart and graph to highlight the reformation of the banking system from taking excessive risk and moral hazard with the support of government measures.

Data & Analysis

Based on the journal of Financial Regulation, bursting of the housing bubble triggered the financial crisis in August 2007 in the USA which also caused decline in credit quality of the subprime mortgage but rise in delinquency rate. Such convulsions in the subprime mortgage market lead to the disruption in the rest of the mortgage and structured finance products. As a result, there was a skepticism working within the financial market and the financial stakeholders were bound to lend each other. The interest rate spread grew in the asset backed commercial paper and in LIBOR as a result of running out of liquidity. There was a drastic drop in the asset values and mortgage backed securities which lead to write offs of the balance sheet of the financial institutions followed by pressure on cost and instruments and fall in the equity values. Government and central banks had to adopt immediate remedial measures to bring back the solvency in the financial market. The actions they took consisted of recapitalization, loans, implicit and explicit guarantees by government and central banks and the bigger companies got merged. After the Lehman Brothers tragic incident there were safety net arrangements by the government to provide infinite coverage on retail deposits and the countries which received the coverage are illustrated in the chart below.

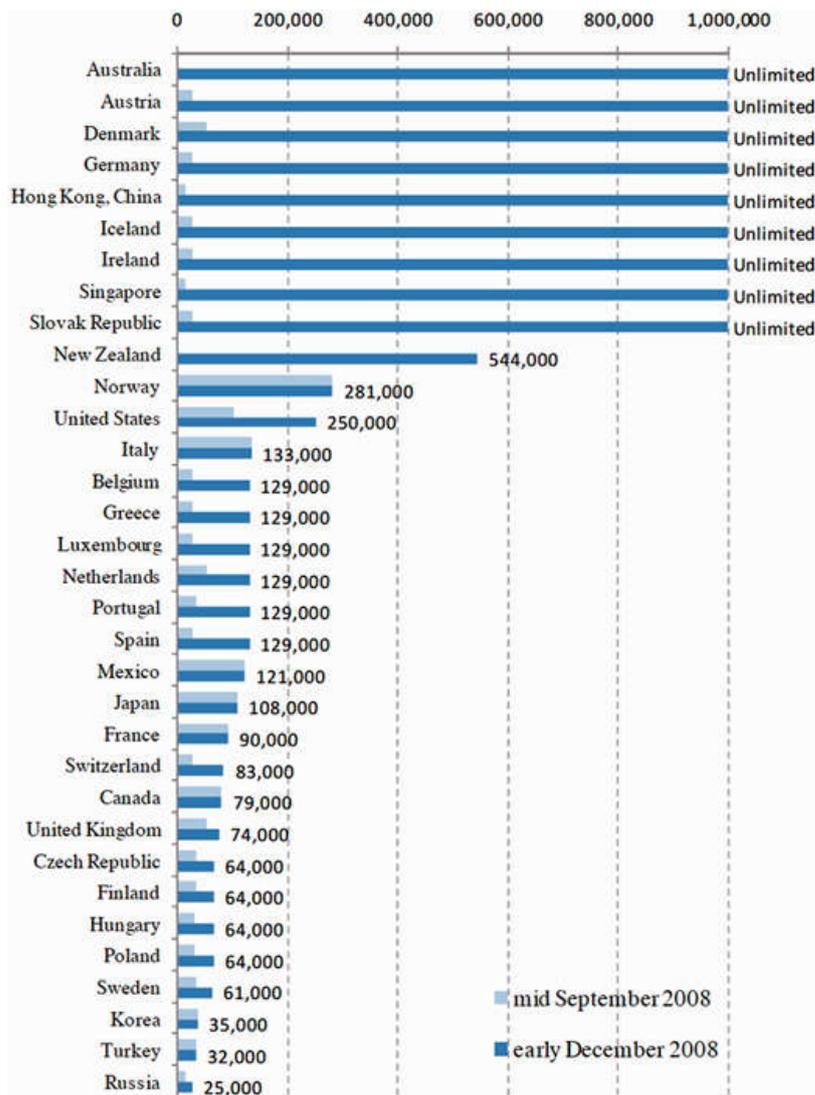


Fig: 1 Deposit insurance coverage limits.

The role of government guarantees in restoring the financial positions of the banks and other institutions has significantly improved the overall conditions as financial damage caused by the crisis. The tendency of banks taking excessive risk considering the government as backup is not any ideal strategy to increase profit as the government has to put taxpayers' money into saving the banks from getting indebted. This is why excessive risk taking and moral hazard problems are largely discouraged where the government has to come forward to rectify the financial situation thus preventing the country going into deficit.

According to IBSU scientific journal 2009, where the significance of deposit insurance is discussed and how it can be a vital part in stabilizing the banking system. Findings from the empirical data indicate that the large banks and banks with usually lower charter value and capital are most likely the high risk takers but the regulators are aware of this phenomenon because failure of any large banks can lead to economic disruptions. Risk and charter values are inversely proportional to each other. Charter value is defined as the economic growth of the future opportunities. Banks usually are less willing to adopt risky strategies when charter value is higher comparatively. If a bank fails it becomes difficult to sell the charter. When the creditor has larger funding than the stockholders the incentives to take risk increases which induces the stockholders to confiscate wealth from the creditors. Once the bank undergoes the reformation process the relation between risk and charter value goes weak as the government provides them with higher deposit insurance backup and in case the banks attempt to undertake risk the cost is higher insurance premium. Thus, the empirical evidence from the hypothesis elucidates the relation between risk, moral hazard and the charter values, asset values, equities which actually remain strong prior to the government interventions but to regain the stability of the financial institutions the regulators keep continuous connection with them in order to trace any anomalies in the financial system. Government backed deposit insurance has brought stability in the system, although it is contradictory to many researchers that this measure of government doesn't fully guarantee the long term stability. There might be other external factors as well behind the bank collapses. But deposit insurance might help to build confidence among the public so that they continue to put in more funds with higher security than before. Designing the insurance schemes more wisely can also prevent bank collapse, otherwise poorly designed schemes can also be a factor behind long term instability. Long term stability can be ensured only by redesigning the schemes so to avoid the moral hazard associated with deposit insurance minimizes the probability of any

instability in the long run. Also, increased regulations and monitoring can keep the financial system in control. Back in 1920s when Great Depression took place many banks collapsed until the deposit insurance emerged in 1933 as the saviour to the failed banking system, regaining a strong financial stability by 1941 and in the next 40 years the bank collapse dropped dramatically resulting an average of seven bank failures per year since 1979.

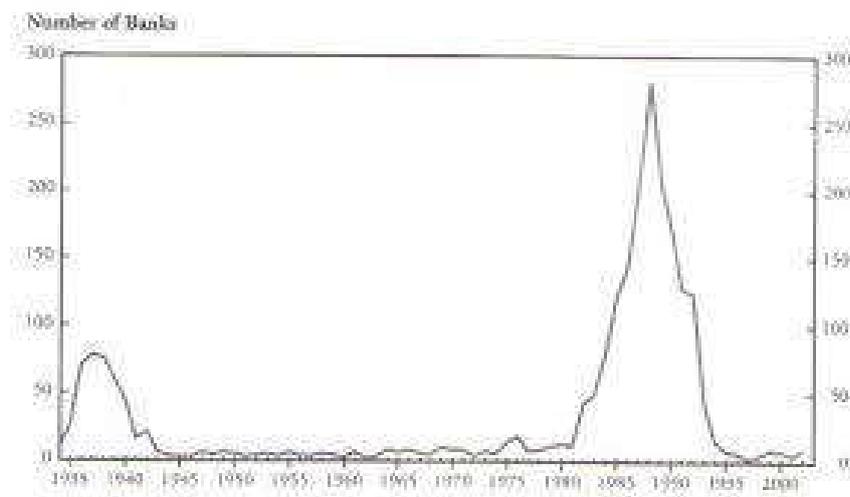


Figure 2: Insured Bank Failures

Summary & Conclusion

To sum up the discussions and assumptions elicited from the scenarios illustrated in the data & analysis are that banks taking excessive risk to maximize profit can lead to severe instability and disasters that can be a threat to the future economic growth and financial market. Moral hazards and risk taking is a common tendency of the banks which can be well-regulated by the government and also encouraging the banks to apply for deposit insurances. Banks going for deposit insurances are insured from any financial crisis or recessions. These

can prevent banks losing their reputation and incur huge losses and depositors losing faith in them. Moral hazard can result in even worse consequences if not kept in control. Banks tend to take risks when they are insured and also when they have the government at their back. In this case banks should be able to calculate the amount of risk they are capable of tolerating without harming their reputation, business and of course stakeholders' interests. In the above mentioned analysis it is illustrated how banks undertaking deposit and getting full coverage against retail deposits and government measures have kept the banks under control from excessive risks and reduced the number of bank failures.

Recommendation

Government interventions and bank guarantees play the role in favor of banks taking excessive risks. During the period of financial crisis when the assets value dropped drastically the government took measures like this but it's depicted that government measures can allow the institutions taking more risks by investing in riskier assets. Thus, it is suggested that becoming more strict and rigid as a government can make the banks take less risk and make sensible investments on the assets that contain less risk in order to divert the banks away from taking excessive risk followed by moral hazard. Insurance firms must design the insurance contract in a way which is beneficial to the banks keeping them away from moral hazards. Also bigger banks should split up to smaller ones in order to keep away from major failures.

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