Executive Summary

This internship report is based on the twelve weeks long internship program that I have successfully completed in BRAC Bank Limited (BBL) under Finance Division from 24th July, 2011 to 20th October, 2011. It is a requirement for the BBA program in BRAC University. I worked in the Finance Division of BBL.

I mainly worked in Regulatory Reporting; and Business Planning and Analysis wing of Finance division. My faculty advisor and the on-site supervisor helped me choose the topic- "*Basel II Implementation in BRAC Bank Limited: Risk Based Capital Adequacy Requirement of Bangladesh Bank*". It is a complex yet very important international requirement for banks. The value of the knowledge attracted me the most.

Bangladesh Bank (BB) is the governing body of all the commercial banks in this country. To be in line with the international standard for regulation of banking industry (Basel Accord), BB has introduced Risk Based Capital Adequacy guideline relating to Basel II. All banks have to follow this guideline and report to BB effective from 1st January, 2010. The guidelines are structured in three aspects or pillars: (1) banks should have minimum capital to guard against different kinds of risks (credit, market and operation risk); (2) assessing capital adequacy with risk profile of the bank and capital growth plan and (3) public disclosure of bank's position on risk, capital and management.

The three main risks that a commercial bank faces are: Credit risk, Market risk and Operational risk. Credit risk is the risk that arises from the probability that the borrowers of the bank will not pay back. Market risk is the risk that puts the bank in adverse situation when interest rate, foreign exchange or equity price move in unfavorable direction. Operational risk stems from the internal environment, occurring when internal processes, people or system fail. The banks can become resilient and fend off these risks with adequate capital. This is where the regulatory guidelines come to play. BB categorizes capital into three tiers. Tier 1 Capital, also known as the Core Capital, which are the top quality capital for the bank. The Components include: Paid up capital, general and statutory reserves, retained earnings, minority interest, non cumulative non putable preference

shares, etc. Tier 2 Capital, also known as supplementary capital, supports Tier 1 capital. Components include: general provision; revaluation reserves for Fixed Assets, Securities and equity investments; other preference shares and subordinated debt. Tier 3 Capital, also known as additional supplementary capital, whose components include: short term subordinated debt to solely guard against market risk. There are more specific guidelines for eligibility of the capital tiers. To measure adequacy; Capital Adequacy Ratio (CAR) is calculated with Risk Weighted Asset (RWA) on the basis of credit, market and operational risk.

Capital planning is an important part to face the risks of the bank. One of the measure or technique to assess the potential damage is stress testing. It is just a type of what-if-analysis. The financial situation of the bank is given some unfavorable "shocks" and potential worst case scenario is observed. BB provides reporting format for the banks. Banks have to follow the regulatory rules; otherwise BB can impose penalty and/or punishment as per Bank Company Act of 1991.

BBL fulfilled all major requirements of Basel II in 2010. It has been maintaining a CAR ratio of above 10% requirement for the last two years. In June 2011 Basel II report to BB, BBL recorded CAR ratio of 11.9% on actual capital. According to the same report, it has a total eligible capital of nearly BDT 13,274 million and a Total RWA of nearly BDT 111,511 million whose 10% must be kept as capital, i.e. BDT 11,151 million. Thus BBL has a surplus of capital. Most of its Tier 1 capital is covered by paid up capital which is high quality and major part of its Tier 2 capital consists of subordinated debt. BBL can smoothly implement all the pillars of Basel II further if the impediments are removed. Data and reporting should be centralized; reasonable time should be given for report submission, unnecessary complex measures can be neglected to help banks adopt Basel II. Stress Test can be improved to show realistic results regarding Pillar 2.

Basel II has been enthusiastically adopted by all the scheduled banks. 28 out of 30 banks have adequate CAR ratio as on June, 2011. Even though banks of our country have less international market exposure, the Basel II international guideline will safeguard them in any unforeseen economic condition of home and abroad.