



Extended Annual Review Report

Project Number: 34908
Investment Number: 7177
March 2009

Equity Investment Bangladesh: Central Depository Project

In accordance with ADB's public communications policy (PCP, 2005), this extended annual review report excludes information referred to in paragraph 126 of the PCP.

Asian Development Bank

CURRENCY EQUIVALENTS

Currency Unit – taka (Tk)

		At Appraisal 30 April 2002	At Project Evaluation 31 December 2008
Tk1.00	–	\$0.01754	\$0.014680
\$1.00	–	Tk57.00	Tk70.69

ABBREVIATIONS

ADB	–	Asian Development Bank
CAGR	–	compounded annual growth rate
CDBL	–	Central Depository Bangladesh Limited
CDS	–	central depository system
CMDPL	–	Capital Market Development Program Loan
CSE	–	Chittagong Stock Exchange
DMC	–	developing member country
DSE	–	Dhaka Stock Exchange
FIRR	–	financial internal rate of return
IMF	–	International Monetary Fund
PER	–	price-to-earnings ratio
PSD	–	private sector development
ROIC	–	return on invested capital
TA	–	technical assistance
WACC	–	weighted average cost of capital
XARR	–	extended annual review report

NOTES

- (i) The fiscal year (FY) of the Central Depository Bangladesh Limited ends on 30 June. FY before a calendar year denotes the year in which the fiscal year ends, e.g., FY2009 ends on 30 June 2009.
- (ii) In this report, "\$" refers to US dollars.

Vice-President	X. Zhao, Operations 1
Director General	P. Erquiaga, Private Sector Operations Department (PSOD)
Director	R. van Zwieten, Capital Markets and Financial Sectors Division, PSOD
Team Leader	J. Klein, Investment Specialist, PSOD
Team Members	H. Ahmed, Principal Investment Specialist, PSOD I. Chua, National Officer, PSOD

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EXECUTIVE SUMMARY

In July 2002, the Asian Development Bank (ADB) approved an equity investment of Tk30 million (approximately \$526,000) in the equity capital of Central Depository Bangladesh Limited (CDBL) for the establishment of an automated central depository system (CDS). Having long recognized the importance of a well-developed, modern financial sector and capital market as a foundation for development of the real economy, ADB had previously provided investment and policy-based support for financial sector development in Bangladesh in a number of different forms. In 1997, ADB approved the Capital Market Development Program Loan (CMDPL) for Bangladesh, one element of which was the establishment of an automated CDS. Under the old paper-based delivery system, settlement and transfer procedures were handled manually and plagued by lengthy delays; risks of damage, loss, forgeries, and duplication; and wasteful investment in time and capital. Bangladesh's stock markets were then experiencing growth that, were it to continue, would over time make the physical handling of certificates cumbersome, costly, and time-consuming. Most of these impediments were expected to be addressed through the creation of an electronic CDS, and CDBL was set up to meet this need. In the nearly 7 years since its inception, CDBL has become a highly successful electronic depository, which has "dematerialized" (i.e., rendered paperless) virtually all securities transactions for the Dhaka Stock Exchange (DSE) and Chittagong Stock Exchange (CSE).

The evaluation criteria used for CDBL are based on the *Guidelines for Preparing Performance Evaluation Reports on Nonsovereign Operations*, released by ADB in 2007. ADB's support of and investment in CDBL was evaluated against four criteria: (i) development impact, (ii) ADB's investment profitability, (iii) ADB's work quality, and (iv) ADB's additionality. On the basis of the foregoing, the overall rating of the project is "excellent."

The development impact of ADB's support of CDBL is rated "excellent." The overall development impact was evaluated against four criteria: (i) private sector development; (ii) business success; (iii) economic development; and (iv) environmental, social, health, and safety performance. With regard to private sector development, CDBL is rated as "excellent" for both "direct company" impacts and "beyond company" impacts. With regard to direct company impacts, CDBL performed well between 2004 and 2008, with investor accounts increasing by a factor of 15, trades settled growing by a factor of 24, shares settled growing by a factor of more than 46, and shares dematerialized growing by a factor of 10. CDBL significantly outstripped expectations for both income and profit before tax. CDBL's performance with regard to beyond-company impacts was also very good. It played a central role in the positive expansion of the stock markets, with a thirty-fold increase in turnover and a more than eight-fold increase in market capitalization in 5 years, exceeding expectations regarding the anticipated scale of capital market development.

With respect to the other evaluation criteria for development impact, business success was rated as "excellent," based on return on invested capital (ROIC), which outstripped the weighted average cost of capital (WACC) significantly, and underscored by key financial indicators and ratios that have strengthened progressively over time. Economic development is rated as "satisfactory," based on CDBL's contributions to job creation, private sector development, and improvements to the capital market infrastructure. CDBL is rated as "satisfactory" with regard to environmental, social, health, and safety performance.

ADB's investment profitability is rated as "excellent."

ADB's work quality is rated as "excellent," based on ratings for: (i) screening, appraisal, and structuring of the project; (ii) monitoring and supervision; and (iii) ADB's role and contribution. With regard to screening, appraisal, and structuring, ADB staff were involved in many aspects of project design. ADB supported the design and implementation of the project through multiple technical assistance grants that funded consultants who assisted with management and technical support, assessed implementation of the CDS, assisted with setting of fees, and participated in other elements of project design. The investment of time and consultant expertise during the project preparation stage was unusually high for a private sector project, and ADB's performance in screening, appraisal, and structuring is thus rated as "excellent." Performance with regard to monitoring and supervision is rated as "partly satisfactory," although involvement appeared adequate for this particular project. (Monitoring has primarily taken the form of reviews undertaken by ADB staff in Manila of CDBL's quarterly and annual reports, and preparation of quarterly review notes as appropriate. ADB has a permanent board member on CDBL's board of directors, but directors have attended board meetings only intermittently, largely leaving CDBL to run independently.) ADB's role and contribution is rated as "excellent," based on its fit with: (i) ADB's Private Sector Development Strategy, (ii) ADB's prior activities in the Bangladesh capital markets (key among which was the CMDPL), (iii) the work of other development agencies, and (iv) the recommendations of experts in the field.

ADB's additionality is rated as "excellent." ADB contributed significantly to the project design—the CDBL project was initiated by ADB, and ADB played a significant catalytic role in structuring the project and coordinating the various elements that contributed to its success. The project originally resulted from a recommendation of a small-scale study under technical assistance that was implemented in connection with the CMDPL. Additionally, ADB's participation helped in attracting other international investors into the project.

The main lessons that can be drawn from the project illustrate the contribution of good project planning to a project's ultimate success. They also underscore, however, the work that remains in Bangladesh with regard to upgrading the country's infrastructure so that an electronic depository can function without anxiety related to poor telecommunications links, inconsistent power supply, lack of phone lines, etc. Many aspects of the capital markets in Bangladesh still require development, such as the debt market, and markets for options, futures, and derivatives. ADB thus has the opportunity to contribute further to development of the capital markets in the country. In summary, the project provides a good example of establishment of an electronic depository, which may be replicated in other countries.

I. THE PROJECT

A. Project Background

1. The Asian Development Bank (ADB)—having long recognized the importance of a well-developed, modern financial sector and capital market as a source of funds for development of the real economy—has provided investment and policy-based support for financial sector development in Bangladesh in a number of different forms, and has coordinated closely with the International Monetary Fund (IMF) and the World Bank to provide assistance to Bangladesh in this sector. Throughout the 1990s, the IMF and the World Bank focused on interventions related to the central bank and the banking system, while ADB concentrated its activities on the development of the capital market as a channel for resource mobilization.

2. In 1997, ADB approved the Capital Market Development Program Loan (CMDPL),¹ which strengthened the market regulation and supervision role of the Securities and Exchange Commission, developed capital market infrastructure, modernized capital market support facilities, and paved the way for investment of long-term institutional funds through the stock exchange. ADB also provided ongoing technical assistance (TA) to strengthen key institutions responsible for market regulation and market infrastructure support that are essential to a fair, transparent, and efficient domestic capital market and increased investor confidence.² One of the conditions for disbursement of the second tranche of the CMDPL, which was disbursed in 2000, was the establishment of an automated central depository system (CDS).³

3. Bangladesh's two stock markets (in Dhaka and Chittagong) had experienced modest growth during the 1990s, resulting in increased trading volumes that would over time make the physical handling of certificates cumbersome, costly, and time-consuming, if growth continued as anticipated. The prevailing delivery, settlement, and transfer procedures were plagued by lengthy delays; risks of damage, loss, forgeries, and duplication; and considerable investment of time and capital.⁴ The delivery and settlement of securities would have become unmanageable in the absence of automation and dematerialization of certificates. Implementation of a CDS—an electronic book-entry system used to record and transfer the ownership of securities—was envisioned as a means of addressing these problems.

B. Project Features

4. The CDS, Central Depository Bangladesh Limited (CDBL), was established for the principle purpose of providing automated depository and settlement services for securities listed on the Dhaka Stock Exchange (DSE) and Chittagong Stock Exchange (CSE), to hold custody of share certificates issued by listed companies on behalf of intermediaries and institutional investors, and to arrange settlement of trades through a computerized book entry

¹ ADB. 1997. *Report and Recommendation of the President to the Board of Directors on a Proposed Loan and Technical Assistance Grants to the People's Republic of Bangladesh for the Capital Market Development Program*. Manila.

² ADB. 2000. *Technical Assistance Capacity Building of the Securities and Exchange Commission and Selected Capital Market Institutions*. Manila.

³ Disbursed on 19 December 2000.

⁴ The problem of counterfeit share certificates had been a concern for many years. These fake certificates are held by investors or by brokers who hold securities for their clients for safekeeping; as many as 10% of customers' certificates in brokers' custody are estimated to be counterfeit. Compounding the problem, forged share allotment letters (which are printed on poor quality, easily forgeable paper) have been circulated. Defunct allotment letters of some companies have also been traded, resulting in a trading volume of those companies' shares that exceeds the free legal float, i.e., the number of shares outstanding and available for trading.

system. It was the first project of its kind in Bangladesh, and the first securities depository to be established in any developing member country (DMC) with direct investment from ADB.

5. The problems associated with the old paper-based delivery system and settlement and transfer procedures (e.g., delay, risk of damage, loss, forgery) were expected to be largely addressed through the creation of the CDS, which would help ensure risk-free and cost-effective transactions and settlement. By computerizing the securities deposit and registration system, facilitating processing of post-trade securities transactions, and eliminating the lengthy (up to 2-month) period taken to record share transfers, the CDS was anticipated to contribute to the efficient functioning of the securities market. Such a modernized capital market, in compliance with international standards and with an increased transaction processing capacity, was foreseen to be a significant advantage in attracting both local and foreign investors. It was thus anticipated that establishment of a CDS would both eliminate existing inefficiencies and help develop the capital market.

C. Project Highlights

6. In the nearly 7 years since its inception, CDBL has become a successful electronic depository. Its core business is (i) providing central securities depository services related to electronic book entry, recording and maintaining securities accounts and registering transfer of securities; (ii) changing the ownership of securities without any physical movement or endorsement of certificates; (iii) execution of transfer instruments; and (iv) various other investor services, including providing a platform for the secondary market trading of treasury bills and Bangladesh Government treasury bonds. Its customers are depository participants, who are mainly stock brokers and dealers, banks, and merchant banks, as well as publicly listed companies and Bangladesh Bank.

7. The primary services performed by CDBL include account opening,⁵ dematerialization and rematerialization,⁶ buying and selling of securities, pledging of shares as collateral, and internet balance inquiry and portfolio valuation services (available online).⁷ Today, through the operation of CDBL, changes in securities ownership can be processed with no physical movement of certificates or documents. The necessity to execute transfer deeds was rendered obsolete. Virtually all securities transactions for DSE and CSE have effectively become paperless.

8. CDBL's performance has been strong, exceeding targets on all metrics, as discussed below.

II. EVALUATION

A. Project Rationale and Objectives

9. The CDBL project came about as a direct response to the Government's request for assistance to strengthen the capital market infrastructure and help generate investor

⁵ Investors may open an account with any CDBL depository participant (who then opens an account with CDBL on the investor's behalf), or can open an account directly with the CDBL.

⁶ Dematerialization is the process by which physical certificates are converted into electronic form; rematerialization is the process of converting electronic securities records back into physical certificates.

⁷ CDBL continues to be market-responsive and is exploring the possibility of introducing an SMS alert via cell phone for credits and debits to accounts; it launched internet banking (balance inquiries and portfolio valuation services) in 2006.

confidence. The investment was consistent with, and complemented, ADB's work in promoting capital market development in Bangladesh, and was seen to demonstrate ADB's commitment to the development of the Bangladesh capital market by significantly improving market efficiency. It was also viewed as an opportunity to leverage ADB's institutional knowledge with respect to CDS establishment.⁸ It was anticipated that the creation of CDBL would ultimately contribute to Bangladesh's economic growth by mobilizing additional savings through improvements to domestic capital market infrastructure, with these savings invested in expansion of new service, industrial, and infrastructure projects, which over time would lead to greater income generation and employment opportunities. Additionally, the existence of an advanced and vibrant capital market, brought about by the establishment of an efficient and secure central depository, was foreseen to build investor confidence; combined with the other initiatives and financial sector reforms that had been undertaken, it was anticipated this would contribute to the achievement of higher economic growth rates and per capita incomes.

B. Development Impact and Outcomes

10. Development impacts and outcomes encompass the effects of a project on a country's economic and social environment. Development impacts and outcomes are evaluated by comparing: (i) what happened with the project, and (ii) what would have happened without it. The rating is a synthesis of the overall impact of the project in the DMC's economy, and addresses how well the project contributed to fulfilling ADB's development objectives. The development rating is based on an assessment of the impact of the project outcomes within the investment environment context.

1. Private Sector Development

11. The project to establish and invest in CDBL had a number of objectives, both for the company and for the market overall. The company itself was established to: (i) hold custody of share securities issued by listed companies in dematerialized (i.e., electronic) form on behalf of private and institutional investors and financial intermediaries; (ii) provide rematerialization services for shares; and (iii) facilitate stock lending and borrowing among depository participants. The project was more broadly conceptualized to promote ADB's work in the financial sector and have a significant catalytic impact on capital markets by mobilizing domestic resources and increasing domestic confidence and participation in the local capital market, which would over time increase credibility, confidence and participation by foreign investors. The performance of CDBL is rated "excellent" with regard to both direct company impacts and beyond company impacts.

a. Direct Company Impacts

12. CDBL performed very well in both absolute and relative terms with regard to the objectives for the company itself, surpassing every anticipated metric, and its performance is rated "excellent" (a summary of the private sector development impacts is in Appendix 1.)

13. **Absolute Performance.** CDBL's absolute performance, in terms of business intermediated, was very robust. The number of depository participants in CDBL grew from 107

⁸ ADB was instrumental in helping establish a central depository in the Philippines, which became operational on 10 January 1997. ADB also assisted in the establishment of a central depository and settlement system in Indonesia, as part of the reform measures under ADB's Financial Governance loan (ADB. 1998. *Report and Recommendation of the President Financial Governance Reforms: Sector Development Program*. Manila).

in 2004 to 258 in 2008. The number of investor accounts⁹ grew fifteen-fold from 2004 to 2008. The number of trades on the DSE and CSE settled in the depository increased from 683,708 in 2004 to almost 17 million in 2008, and the number of shares settled in the depository went from 109.5 million in 2004 to 5.1 billion in 2008. Shares dematerialized in the depository increased from 61 million in 2004 to 613.7 million in 2008.

14. **Relative Performance.** CDBL's performance against the business performance targets established for the company at inception has also been very good, with both total income and profit before tax far in excess of expectations.

b. Beyond Company Impacts

15. The project was also anticipated to have an impact on overall capital market development, and CDBL's contribution is rated "excellent" from this perspective as well.

16. **Absolute Performance.** At inception (in October 2003), CDBL was operating in a market environment that remained depressed from the effects of the 1996 stock market crash. Over the next 6 years, the stock markets experienced tremendous growth in aggregate turnover and capitalization, which was significantly facilitated by CDBL. Aggregate turnover of the DSE and CSE increased from Tk25.8 billion in 2003 to Tk770.8 billion in 2008 (a thirty-fold increase), and market capitalization increased from Tk97 billion to Tk852 billion (a more than eight-fold increase) over the same period. In percentage terms, market capitalization increased from about 4% of Bangladesh's GDP in 2003 to around 17% in 2008. The progress of the markets is shown in Table 1.

Table 1: Bangladesh Capital Market Development

Calendar Year	Enlisted Issues (incl. mutual funds / debentures) (DSE) ^a	Tk Million			General Index (DSE)
		Issued Capital and Debentures (DSE)	Market Capitalization (DSE)	Turnover During the Year (DSE+CSE)	
2003	267	46,055	97,442	25,843	967.88
2004	242	49,532	224,159	68,274	1,971.31
2005	268	70,313	228,575	78,797	1,677.35
2006	276	118,437	315,446	81,609	1,609.51
2007	281	214,472	742,196	375,195	3,017.21
2008	301	372,156	852,210	770,841	2,795.34

CSE = Chittagong Stock Exchange, DSE = Dhaka Stock Exchange, incl. = including.

^a Excluding Government of Bangladesh Treasury Bonds listed at the Exchange 2004–2014, 2005–2004, 2006–2016, 2007–2035, and 2008–2042 (111 in total). These listed bonds are not traded.

Source: Central Depository Bangladesh Limited.

17. **Relative Performance.** A number of assumptions were made at the inception of CDBL regarding the anticipated scale of the capital markets and of market development. Market development has generally been well in excess of expectations, with market capitalization reaching Tk852 billion in 2008, 11 times higher than anticipated. Stock exchange turnover, which was anticipated to equal Tk150 million by 2008, actually reached Tk3 billion. Other metrics also exceeded expectations (Table 3).

⁹ Including individual, joint, omnibus, and company accounts.

Table 3: Bangladesh Capital Market Performance – Assumptions vs. Reality

Metric	Projected/Actual	2003	2004	2005	2006	2007	2008
Listed securities	Assumptions	263	273	283	293	303	313
	Reality	267	242	268	276	281	301
Market capitalization (Tk billion)	Assumptions	60	63	66	69	73	77
	Reality	97	224	228	315	742	852
Number of participants	Assumptions	35	50	65	80	92	105
	Reality	n.a.	107	184	211	234	258
Number of issuers	Assumptions	20	60	80	100	115	130
	Reality	n.a.	43	90	105	135	164
Investor accounts	Assumptions	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
	Reality	n.a.	128,636	587,101	896,959	1,631,469	1,976,272
Stock exchanges daily turnover in Tk million	Assumptions	30	66	119	121	135	150
	Reality	103	273	315	326	1,500	3,083

Source: Central Depository Bangladesh Limited.

18. In summary, the project's success with regard to private sector development, both via direct company impacts and impacts beyond the company, was superior. CDBL handily achieved the goals and objectives set out for it at the project's inception. It has provided efficient and reliable infrastructure for the electronic registry of scripless securities, bringing Bangladesh in line with best practices of advanced economies with regard to securities operations, and offering virtually unlimited scope for growth of stock exchange trades and markets.¹⁰ The performance of CDBL as a business and its contribution to the development of the capital markets have both been impressive.

2. Business Success

19. The project's contribution to business success is measured primarily by the real after-tax financial internal rate of return (FIRR), which is compared to the real weighted average cost of capital (WACC) for the project to determine whether the project is covering its opportunity cost on capital employed. ADB provided an equity investment in CDBL, and return on invested capital (ROIC) was therefore used as a proxy indicator and evaluation standard. The ROIC exceeds the WACC significantly, yielding a rating of "excellent" with regard to business success (which, according to the *Guidelines for Preparing Performance Evaluation Reports on Nonsovereign Operations*,¹¹ is achieved if ROIC exceeds WACC by 700 basis points or more).

20. CDBL has been very successful in terms of overall business performance. Despite the current global economic crisis—which is affecting stock markets worldwide—CDBL has continued to show robust operating performance. Income from operations, total assets, and shareholders equity all increased substantially between 2002 and 2008.

¹⁰ This delivers numerous benefits to both corporations and individual investors, freeing corporations from the lengthy process of verifying and registering transfers of market-traded securities, and avoiding problems with fraudulent and duplicate certificates. Benefits to individual investors include hassle-free delivery on settlement, faster settlement, elimination of the risks associated with physical certificates, reduced paperwork, the convenience of consolidating accounts, the ability to hold multiple types of securities in a single account, electronic credit of new issues into investor accounts, and regular account status updates on demand.

¹¹ ADB. 2007. *Guidelines for Preparing Performance Evaluation Reports on Nonsovereign Operations*. Manila.

21. The financial ratios of CDBL have strengthened progressively during this period of rapid growth, with return on assets, return on equity, and net asset value per share increasing markedly. CDBL has pursued a conservative funding strategy, as reflected in its low use of leverage; this low debt-to-equity ratio allows CDBL substantial headroom to borrow for future business expansion.

22. Based on the comparison of ROIC to WACC, and the generally robust business performance of the company, the project's rating with regard to business success is "excellent."

3. Economic Development

23. A project's contribution to economic development is measured primarily by the economic internal rate of return. The economic return on invested capital is used as a proxy for corporate loan and equity funding that is not targeted at specific capital investment projects. CDBL is rated "satisfactory" with regard to economic development, as a result of its contribution to job creation, private sector and SME development, and improvements to the capital market infrastructure, as described below.

24. **Job Creation.** It is not possible to determine how the project has contributed to Bangladesh's overall standard of living, but it is anecdotally clear that it has created many jobs in Bangladesh, both directly and indirectly.¹² At CDBL's inception, for example, brokerage houses were located in shabby offices with limited numbers of employees; today, brokers have large, modern offices staffed with many people engaged in many activities. With 258 depository participants admitted thus far to CDBL, at least a thousand new depository-related white collar jobs have been created among depository system participants, and numerous technical jobs have been created by the service providers that link CDBL's operations to depository participants and issuers via fiber optic and radio links in major cities.

25. **Private Sector and SME Development.** CDBL's depository participants and 90% of issuers belong to the private sector, and can be classified as SMEs. They have prospered from the introduction of the depository—this is particularly true for depository participants, with the intrinsic worth of their businesses increasing at least seven-fold since the start-up of CDBL.¹³ The barrier to entry for retail participation in the Bangladesh capital market is very low: retail investors with \$30 or \$40 are able to buy and sell securities directly through the depository, and the existence of a CDS has greatly facilitated participation by individual investors in the private sector economy.

26. **Market Infrastructure Development.** By converting physical certificates into electronic form, CDBL has made it possible for the stock exchanges to reduce settlement cycles from seven days to three days, thereby substantially increasing the liquidity of the market. Freed from the difficulties of dealing in paper certificates, the stock exchanges have been able to accommodate large growth in trading volumes with resultant increases in income, some of which has been invested in upgrading the trading infrastructures of the exchanges, thus making the market more efficient.

4. Environmental, Social, Health, and Safety Performance

¹² This analysis derives from discussion with CDBL management.

¹³ CDBL management estimate.

27. This project was classified as category C, and no reporting on environmental or social issues was required of CDBL. This assessment has not been changed during project implementation. CDBL was not required to (and does not) have processes or standards in place with regard to environmental and social safeguard compliance. Their performance is in keeping with ADB's requirements, and is rated "satisfactory".

C. ADB Investment Profitability

28. ADB's profitability has been assessed and rated "excellent."

29. The *Guidelines for Preparing Performance Evaluation Reports on Nonsovereign Operations* provide three options for evaluating the profitability of direct and indirect ADB equity investments. The first option requires that minimum return expectations exist at the time of approval. Although this method is most commonly used in extended annual review report (XARR) evaluations, the RRP for the project¹⁴ did not state a minimum return expectation, and therefore this approach cannot be used for evaluation. The second option applies to projects with no hurdle rate set at approval and no available market-based comparators, and requires derivation of minimum multiples of proxy gross earnings from actual or notional senior ADB loans to similar projects. This approach cannot be used because there are no existing senior ADB loans to similar projects in Bangladesh (CDBL is the only ADB financial intermediary project in Bangladesh.) The third option also applies to projects with no hurdle rate set at approval, and requires the use of market-based comparators within the country in determining risk-adjusted returns. CDBL is the first and only central securities depository company in Bangladesh, however, and thus no private or publicly listed company in Bangladesh can be used as a comparator.

30. Given that none of the proposed profitability evaluation options is fully applicable, the third option has been modified, using a proxy from a similar industry in India as a market-based comparator, with the required return adjusted by a premium or discount based on perceived sovereign and market risk in Bangladesh versus India. ADB has an equity investment in the State Bank of India Discount and Finance House Inc. (SBI DFHI), a 67% state-owned market leader in the primary dealer segment of the domestic debt market in India. Its primary objective is to support the book building process in primary auctions of government securities and provide necessary depth and liquidity to the secondary market in government securities.

31. In comparison with SBI DFHI, CDBL has a larger market capitalization (making it less risky), stronger corporate governance (also less risky), and faces greater political instability (more risky). The risk-adjusted expected return for CDBL was adjusted accordingly.

32. The project is given a rating of "excellent," based on an equity return multiple that exceeds the benchmark in the *Guidelines for Preparing Performance Evaluation Reports on Nonsovereign Operations* of 1.5.

D. ADB Work Quality

33. ADB's performance is rated "excellent" based on the following: (i) "excellent" performance in screening, appraisal, and structuring of the project; (ii) "partly satisfactory" performance in monitoring and supervision; and (iii) "excellent" performance in terms of ADB's

¹⁴ ADB. 2002. *Report and Recommendation of the President to the Board of Directors on a Proposed Equity Investment Central Depository Project to Bangladesh*. Manila.

role and contribution. Project structuring and ADB's role were particularly important to this project, while the monitoring and supervision function was—for this particular project—less important, leading to the “excellent” overall rating for ADB work quality.

1. Screening, Appraisal, and Structuring

34. ADB staff were involved in screening, appraising, and structuring the project. ADB first became involved in the project through a TA processed in 1997,¹⁵ which recommended the establishment of a CDS.¹⁶ ADB undertook missions to Bangladesh to explore the concept in September 2000, December 2000, and March 2002. Three consultants (a project management adviser, depository technical adviser, and network adviser) financed by ADB under TA for Central Depository Capacity Building¹⁷ worked with CDBL to provide management and technical support, to facilitate making the CDS fully operational by the end of 2002. Under TA for Capacity Building of the Securities and Exchange Commission and Selected Capital Market Institutions¹⁸, ADB also assisted the company in conducting a quality check on implementation of the CDS, evaluating the system as it was installed, and providing advice and training on matters such as the regulatory responsibilities of the Securities and Exchange Commission. ADB's consultants provided inputs on the fee and deposit structure that the depository adopted, and helped interview technical staff as part of the recruiting process. Finally, ADB requested specific and regular reporting from CDBL with regard to project implementation, articulated accounting standards for the business, and secured the right to appoint one director to the board. The project sponsor felt that the consultancy services, which included both intermittent support (including advice from the former head of the Philippine depository) and longer-term, ongoing support, was very useful.¹⁹

35. Projects are rarely undertaken with such an extensive investment of time and consultant expertise during the project preparation and implementation stage. ADB's performance in project screening, appraisal, and structuring met a high standard, and is rated "excellent."

2. Monitoring and Supervision

36. ADB has monitored CDBL's performance since making the equity investment in 2002, but has been less deeply involved during this period than during project preparation. CDBL submits quarterly unaudited and annual audited information on its financial performance. The information is reviewed by ADB staff, who use it in preparing quarterly Private Sector Investment Management notes. One annual review was completed for CDBL (in 2006). Since project inception, ADB has had the authority to appoint one representative to CDBL's board of directors. This position has generally been filled by staff from the Bangladesh Resident Mission. ADB's directors have periodically attended board meetings, but have largely allowed CDBL to

¹⁵ ADB. 1997. *Report and Recommendation of the President to the Board of Directors on a Proposed Loan and Technical Assistance Grants to the People's Republic of Bangladesh for the Capital Market Development Program*. Manila (Loan 1580-BAN, and TA 2913-BAN and 2914-BAN, for \$80 million, approved on 20 November).

¹⁶ A member of Bangladesh's Parliament secured approval of the depository act that allowed the project to be undertaken, but ADB was instrumental in developing the idea for the depository.

¹⁷ ADB. 2001. *Technical Assistance to Bangladesh for Central Depository Capacity Building*. Manila.

¹⁸ ADB. 2000. *Technical Assistance Capacity Building of the Securities and Exchange Commission and Selected Capital Market Institutions*. Manila.

¹⁹ The project sponsor had one negative observation to offer with regard to project structuring: it would have been helpful for the project if ADB had invested more money at the outset, as it would have shortened the time required to raise the prescribed capital of Tk250 million as required by the regulators. However, it is not clear that that would have been more appropriate from the standpoint of ADB's catalytic role, one aspect of which was to create a diversified shareholder base for CDBL. Thus, this aspect of project structuring is considered to be adequate.

manage its own affairs, and have not been as involved as some CDBL board members. In general, contact with CDBL by ADB staff has been rather light over the last several years.

37. ADB did not monitor and supervise CDBL as intensively as it does many other equity investments; many investments require greater involvement than did CDBL, which has been run competently and without incident since inception. ADB's monitoring and supervision appears in retrospect to have been sufficient to keep staff informed of any material changes to project performance and to take timely action in response, which the *Guidelines for Preparing Performance Evaluation Reports on Nonsovereign Operations* indicates is the standard for being ranked "satisfactory." However, ADB's monitoring was only successful because the project performed very well independently, with few issues that arose; accordingly, ADB's supervision has been rated as "partly satisfactory".

3. ADB's Role and Contribution

38. ADB's *Private Sector Development Strategy* (PSD Strategy), approved by the Board on 30 March 2000,²⁰ makes specific references to ADB's role in strengthening the capital markets of DMCs. The strategy notes that well functioning financial systems are critically needed to promote the private sector. Many DMCs need to strengthen their financial institutions and create diversified financial markets to develop the domestic capacity to finance private sector-led growth. The PSD Strategy mentions that ADB, through PSOD, would complement funding with capacity-building and governance strengthening for financial institutions, and would continue its support for policy reform to enhance regulation and supervision, develop sound banking systems, and deepen and broaden securities markets. Consequently, the investment was entirely consistent with the strategy.

39. The investment was also an integral component and condition for disbursement in 2000 of the second tranche of ADB's CMDPL to Bangladesh, and was thus consistent with ADB activities in the country's capital markets since 1997. These activities were coordinated with the IMF and the World Bank, and were therefore also appropriate in the context of the work of other multilateral development institutions. CDBL's establishment also fulfilled a key recommendation made by the Group of Thirty, (i.e., the establishment of securities depositories by major stock exchanges worldwide to facilitate delivery and settlement of transactions).²¹

40. ADB's performance related to its role and contribution is rated "excellent", due to its strong alignment with (i) the PSD Strategy, (ii) ADB's activities in the capital markets in Bangladesh since the late 1990s, (iii) the work of other development institutions, and (iv) the recommendations of experts in the field.

D. ADB's Additionality

41. Evaluation of ADB additionality is based on whether: (i) ADB finance was a necessary condition for the timely realization of the project, either (a) directly, or (b) indirectly by providing

²⁰ ADB. 2000. *Private Sector Development Strategy*. Manila. At the time the project was prepared, this was the most current version of the Private Sector Development Strategy, and ADB's role and contribution is thus assessed in part based on its alignment with this document.

²¹ The Group of Thirty (www.group30.org) is a private international body composed of very senior representatives of the private and public sectors and academia. The organization's goal is to raise awareness and understanding of major international and financial issues. Its objective is to standardize the settlement procedures and reduce associated inherent risks on a global basis. The Group of Thirty's recommendations have been adopted by the International Federation of Stock Exchanges and are supported throughout the international securities community.

sufficient comfort to attract private financiers; and (ii) the ADB contribution to project design and function improved the development impact.

42. ADB's additionality is rated "excellent". ADB contributed strongly to project design—the CDBL project was initiated by ADB, and ADB played a significant catalytic role in structuring the project and coordinating the various elements that contributed to its success. The project originally resulted from a recommendation of a small-scale study undertaken through ADB TA, implemented in connection with the CMDPL. Additionally, ADB's participation helped in catalyzing the involvement of other international investors. In their XARR questionnaire response, CDBL's management stated that, "Without ADB's sponsorship we don't think that this project would have seen the light of day" and that "the foreign banks' participation [was] largely on account of ADB's sponsorship of the project."²²

E. Overall Evaluation

43. The overall rating of ADB's investment in CDBL—as justified by the underlying rating of development impact, ADB investment profitability, ADB work quality, and ADB additionality—is "excellent."

Table 7: Evaluation of the Central Depository Bangladesh Limited

Indicator/Rating	Unsatisfactory	Partly Satisfactory	Satisfactory	Excellent
Development Impact				
Private sector development				X
Business success				X
Economic development			X	
Environment, social, health, and safety performance			X	
ADB Investment Profitability				X
ADB Work Quality				X
ADB Additionality				X
	Unsuccessful	Partly successful	Successful	Highly successful
Overall Rating				X

ADB = Asian Development Bank.
Source: ADB staff.

III. ISSUES, LESSONS, AND RECOMMENDED FOLLOW-UP ACTIONS

44. **Determination of Fee Schedules.** Fee schedules of depositories in Asia and the Pacific (particularly in neighboring countries such as India, Pakistan, and Sri Lanka) were studied in depth at the project's implementation stage, and CDBL chose to model its own fee schedule on that of Pakistan. The project sponsor states this was a good decision, because the fee schedule worked out well both for CDBL and its users, many of whom have grown significantly wealthier over the past few years.

²² One important role that ADB played in giving comfort to international investors was simply requiring the drafting of a shareholders' agreement. In Bangladesh some investors would likely have been comfortable simply investing based on personal relationships, but this would likely have been inadequate for international investors, who gained comfort from the formalized relationship developed through the legal documentation.

45. **Importance of Infrastructure.** CDBL rates its own business performance as satisfactory, stating that it has been handicapped from achieving what it considers to be consistently excellent performance by the poor state of infrastructure in the country.²³ Its business activities are hampered by frequent interruptions in power supply, unreliable telecommunication links, lack of telephone lines, paucity of skilled personnel, and other factors.

46. In general it should be noted that there were no significant issues that arose, or substantive changes that would in retrospect have been made to improve the overall quality of the project.

47. With regard to follow-up activities, in accordance with the observation that infrastructure has been a constraint to CDBL's operations, ADB may consider appropriate investments in the infrastructure sector that could alleviate some of these constraints. Additionally, the project sponsor has highlighted the fact that Bangladesh's capital markets remain immature and incomplete; there is no debt market of any consequence in Bangladesh, and the equity market is one-sided (or in the words of the project sponsor, "fundamentally flawed"), because participants can only go long, but cannot short-sell. There are no options or futures markets, nor any derivatives trading. It appears that ADB could consider both public and private sector activities to address these issues and build more robust and sophisticated capital markets in Bangladesh.

²³ These difficulties notwithstanding, CDBL has managed to settle each day's transactions overnight (as mandated) throughout its 5 years of operations, with the exception of delays of a few hours on rare occasions.

PRIVATE SECTOR DEVELOPMENT INDICATORS AND RATINGS: DEPOSITORIES

Indicators	Ratings ^a	Justifications/Annotations
1. Beyond Intermediary and Investee Company Impacts		
1.1. Private sector expansion and institutional impact		
1.1.1 Contributes to pioneering or materially increasing the private sector share of and role in the economy.	Satisfactory	Borne out by the huge growth in the size of the market. Since the startup of the depository, the market capitalization has risen from 4% of GDP in 2003 to over 17% in 2008.
1.1.2 Contributes to institutional development by:		
(i) improving the supply of capital in the market;	Excellent	Issued capital of the market has increased from Tk46 billion in 2003 to Tk372 billion in 2008.
(ii) demonstrating the merits of depositories to the public, firms, banks, and others;	Excellent	Investors opened over 1.9 million accounts in the depository since startup. Virtually all banks are users of depository services, as are other financial institutions.
(iii) bringing liquidity to local stock exchanges;	Excellent	Stock exchange aggregate turnover increased from Tk25 billion in 2003 to Tk770 billion in 2008.
(iv) helping the maturation of capital markets; and	Satisfactory	The depository is a significant step towards bringing the market in line with that of more advanced economies.
(v) increasing capital market expertise via migration of depository personnel to other institutions, etc.	Partly satisfactory	Only four staff have moved from CDBL to other institutions since startup; more CDBL staff members have gone abroad for higher studies and to emigrate.
1.2. Competition. Contributes to new competitive pressures in key markets and/or in the financial sector.	Excellent	Investors have a choice of 258 depository participants of different standing, including stock brokers, banks & other financial institutions, with healthy competition to attract investors.
1.3. Innovation. Helps introduce effective new products, services, and new technologies, thereby supporting reform and transformation of business sectors, industries, and/or maturing financial markets (item 2.2).	Satisfactory	Overall, the depository has transformed how share dealings take place and has made new products—such as options, futures and derivatives trading—possible.
1.4. Linkages. Adds notable upstream or downstream link effects to companies and/or financial markets for growth.	Satisfactory	The depository is at the center of the links between issuers, market players (i.e., investors and depository participants) and the market (exchanges), and there is free electronic movement of securities through the depository system. Issuers can deliver their securities directly to the depository accounts of investors, and investors can receive securities from and deliver them to each other by executing buy–sell transactions through the stock exchanges.

Indicators	Ratings ^a	Justifications/Annotations
		<p>its clients. It will be equipped with up-to-date Information Technology to ensure prompt customer response and provide innovative solutions to the needs of the capital market playing a pivotal role in Bangladesh's financial services sector.</p> <p>CDBL will build a sound management team with carefully-chosen, highly-motivated staff and foster a "new spirit of enthusiasm" balanced with prudent policies to achieve a high level of sophistication and expertise in the performance of its personnel by consistently striving to provide high quality services by:</p> <ul style="list-style-type: none"> (i) emphasizing the importance of the customer, (ii) unleashing employee initiative by empowering them, and (iii) viewing activities of the business as processes and the goal of continuous improvement. <p>Management's leadership endeavors will be to forge a cohesive and integrated team to operate from a truly common bottom line, sharing the same agenda, driven by the same vision: to achieve the best possible results, not only for the shareholders and the employees but also to boost public confidence in CDBL's growing strength as an independent, professionally managed institution." – CDBL Management.</p>
Overall PSD Rating	Excellent	

ESHS = environmental, social, health, and safety; IPO = initial public offering; SME = small and medium-sized enterprise; PSD = private sector development; RRP = report and recommendation of the President.

^a Ratings scale: unsatisfactory, partly satisfactory, satisfactory, and excellent. The rating is not an arithmetic mean of the individual indicator ratings, and the ratings have no fixed weights.

Source: ADB staff.