Aims of BANGLADESH

LOCKED IN OR LOCKED OUT?

October 23, 1999

The painful hangover from the 1996 crash of the Bangladesh capital market lingers on and no action seems curative or good enough to arouse investor's confidence. The regulators seem baffled and the market participants resigned to the ominous gloom and doom. The secondary market is in disarray and the primary market all but dried up. The pent up demand for capital from the corporate sector saw no lease of life during the last couple of years.

However, since there is always a silver lining beneath the darkest clouds, slowly but curiously the issuers started to test the water and some investors came forward to lend a helping hand. Consequently, the primary market had a sigh of relief in recent months with some IPOs being oversubscribed, thanks to the phenomenon of private placement, mostly from the brokers, dealers and their clients. There was renewed interest of investors in the primary market, a sign of turn around in the capital market in the long run.

The issuers regained the courage to raise capital through IPO, ensuring subscription of a good part through private placement and being saved from the tension and stigma of under-subscription. This also lowered the issue cost as underwriting requirement was slashed, saving 2.5% of direct underwriting cost and another 2.5% contingent liability in the form of take-up commission in cases of under-subscription, plus the broker and banker's commission.

Pre-IPO private placement has been contributing to a great extent to revitalize the sluggish primary as well as the secondary market. SEC has so far given consent of capital issues to five companies in 1999. They raised about 73% of the public float (public float normally being 50% of the total paid-up capital of the company, the rest 50% being held by the sponsors) through private placement.

Company	**Subs. Period**	**Total Share Tk**	**Size of the Issue Tk**	**IPO Offer Tk**	**Pre-IPO Placement Tk**	**% of Pre-IPO to Total Issue**	**% of free-float to total share**
Sinobangla Industries	Jan 99	99,988,000	33,000,000	20,000,000	13,000,000	39.39	20.00
Rangpur Foundry	Apr 99	100,000,000	50,000,000	20,000,000	30,000,000	60.00	20.00
Bangladesh Welding Electrodes	Jul 99	100,000,000	50,000,000	15,000,000	35,000,000	70.00	15.00
Prime Bank	Sep 99	400,000,000	200,000,000	27,500,000	172,500,000	86.25	6.88
Bionic Seafood	Sep 99	80,000,000	40,000,000	20,000,000	20,000,000	50.00	25.00
Total		**779,988,000**	**373,000,000**	**102,500,000**	**270,500,000**	**72.52**	**13.14**

The fact that pre-IPO private placement not only infuses fund in the primary market, but also boosts the secondary market is corroborated by the interesting fact that while all the recently listed companies which offered shares with pre-IPO private placement are trading at a premium, all the companies which did not opt for private placement are being traded below par.

Companies offered shares without private placement	**Face Value Tk**	**Current Market Price Tk**
Samata Leather	100.00	81.75
Mona Food	100.00	89.00
Aramit Cement	100.00	95.00

Companies offered shares with private placement	**Face Value Tk**	**Current Market Price Tk**
SinoBangla Industries	10.00	30.20
Rangpur Foundry	10.00	15.40
Bangladesh Welding Electrodes	10.00	13.80

An investor, who comes forward to take up issues at the primary market under private placement, much before the company goes public, in fact takes a risk and thereby creates a market. There is no guarantee that such an investor will make a profit out of the deal. But there is no denying of the fact that the investor creates a demand in the market, an essential element for the success of public issue, more so in a sluggish market like ours.

The Securities & Exchange Commission has reportedly started imposing a one year lock-in on private placement, except that made to financial institutions, on recently approved issues. This restriction has come all of a sudden and without any consultation with the market operators. We view that imposing lock-in on private placement is not a well-conceived measure, because of its possible adverse impact on the capital market.

In most of these companies 50% of the shares are held by the sponsors and are already under lock-in restriction for three years. Therefore, given the past trend of private placement, a total of 86% of the shares of the companies will be locked in, leaving only 13-14% share on free-float. Consequently, market liquidity in both the primary and secondary market would dry down. This invariably would hike the prices of these scrips artificially, devoid of fundamentals, through the mechanism of demand and supply.

It is feared that the issuers who have already applied for approval of their IPOs with the SEC, including AIMS First Guaranteed Mutual Fund, the first mutual fund of the country under private initiative, Legacy Footwear, Southeast Bank, Dhaka Bank, Miracle Industries, Super Board Paper Mill, National Credit & Commerce Bank Limited, Fu-Wang Foods, Hashem Foods and Modern Foods will now suffer a set-back as all of the issues have already received considerable amount of private placement. They would now either have to cancel the subscription or take the risk of entering the market without minimum assurance of even part subscription of their issue, more so as reportedly, the SEC is imposing the condition on even post-facto basis. For them, it is analogous to changing the goal post while the final whistle is about to be blown.

We may be in for a barren primary market for quite some time.

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