

Investment Banking

Chapter Objectives

This chapter will enable you to develop an understanding of the following:

- 1 *Investment banks*
 - 2 *Functions of investment banks*
 - 3 *Types of investment banks*
 - 4 *Investment-banking services*
 - 5 *Merchant-banking services*
- Investment banks are financial intermediaries in the business of providing investment and advisory services to companies, governments and investors.

INTRODUCTION

Investment banks are financial intermediaries in the business of providing investment and financial advisory services to companies, governments and institutional investors. Investment banks issue securities on behalf of both public as well as private companies, trade securities in the primary and secondary markets on behalf of individual and institutional investors, manage portfolios for high net-worth clients and corporates, and provide financial advisory services to corporates, private equity groups, public entities, non-profit clients and institutional investors.

Investment banking differs from commercial banking in the sense that they do not accept deposits and grant retail loans. While commercial banks mobilize savings in the form of deposits and lend these funds to individuals, corporates and government, investment banks bring both the lender as well as the borrower together and help the lenders invest directly in the business of the borrowers. The services of commercial banks are accessible by all, while investment banks serve mainly the large companies and high net-worth individuals.

Investment banks were known as merchant banks in the United Kingdom. In the United States, a commercial bank could not undertake share broking or investment in shares till late 1990s. Because of the stock-market crash of 1929 and the high risk involved in the capital-market activities, the Glass–Steagall Act, 1933 prohibited commercial banks from undertaking investment banking. Hence, the stand-alone investment-banking model was born in the United States. The five big stand-alone investment banks, called ‘bulge-bracket,’ in the order of their establishment, were Lehman Brothers (1850), Goldman Sachs (1869), Merrill Lynch (1914), Bear Sterns (1923) and Morgan Stanley (1935). The Glass Steagall Act, 1933, was repealed by Gramm–Leach–Bliley Act of 1999. The commercial banks in the United States could undertake investment- banking activity and are now known as ‘universal banks.’ Citigroup, JP Morgan Chase and Credit Suisse are examples of Universal Banks. The acquisition of the merchant banks in the United Kingdom by the investment banks of the United States and the boom in the stock markets in the 1990s popularized the concept of investment banking. In India, commercial banks and financial institutions set up subsidiaries in 1972 to undertake this activity and it was known as ‘merchant banking’ till late 1990s. The ANZ Grindlays Bank was the first to set up a merchant-banking division in 1969 which offered issue-management services to corporates. With the advent of foreign-investment banks in India in the late 1990s, merchant banking started being referred as ‘investment banking.’ Merchant-banking activity comes under the purview of the SEBI and regulations have been framed to regulate the activities of merchant bankers.

FUNCTIONS OF INVESTMENT BANKS

Investment banks perform two types of functions, as follows:

They help public as well as private corporates in issuing securities in the primary market, provide guarantee by standby underwriting and act as intermediaries in trading for clients. They help government in the disinvestment of public-sector enterprises.

They give companies advice on mergers and acquisitions (M&A)—both sell side as well as buy side, divestitures, corporate restructuring and spin-offs. They provide financial advice to investors and assist them in purchasing securities, managing financial assets and trading.

Types of Investment Banks

- Full service global investment banks
- Regional investment banks
- Boutique firms

TYPES OF INVESTMENT BANKS

There are three types of investment banks, which can be classified as:

Full-service global-investment banks which operate on a global basis and provide a complete set of services to their clients. These are large investment firms that serve large corporates, usually multinational corporations. Jefferies, Goldman Sachs, JP Morgan Chase & Co. and Kotak Investment Banking are some of the full-service investment banks.

Regional-investment banks concentrated in a particular region with specialized geographic knowledge and a variety of product offerings. These firms are also known as 'speciality investment banks.' For example, Piper Jaffray Companies is a leading, international middle-market investment bank and institutional securities firm serving the needs of middle market. Simmons & Company is the only independent investment bank specializing in the entire spectrum of the energy industry in Europe.

Boutique firms are small investment banks organized at a local level and specialize in a particular industry or product. They are independent firms whose focus is on advisory services such as M&A. Because of their expertise, they are better advisors in particular deals. They provide personalized services to their clients and try to be more of partners rather than merely being advisors. Avendus Capital, a boutique-investment-banking outfit in India, has carved a niche in the small and middle-market M&A space and private-equity transactions. Veda, a Chennai-based boutique-investment bank, provides advisory services in venture capital (VC), private equity (PE) and M&A, to emerging corporates and established groups in the manufacturing, technology, consumer products and services domains. Montague Partners is a boutique-investment bank founded in 1989 and headquartered in San Francisco. The firm works with privately-owned middle-market companies throughout the United States, in a range of industries, specializing in M&A and private placements of debt and equity.

INVESTMENT-BANKING SERVICES**Fund-raising Services**

Investment banks help clients to raise funds through the following:

- Initial Public Offerings (IPOs).
- Follow-on Public Offerings (FPOs).
- Qualified Institutional Placements (QIPs).
- Rights Issues.
- Preferential Allotments.
- Foreign-Currency Convertible Bonds (FCCBs).
- Global Depository Receipts (GDRs).

The investment bank is an indispensable player in the success of the offering. It assists the issuer in a number of critical functions: analyzing the industry and company to determine if there is a demand with investors for such an offer, designing the offering, pricing the offering and marketing the offering to investors. The investment bank leads and directs the issuer's team of professional advisors and coordinates their roles to ensure that the funds are successfully raised.

Advisory Services**(a) Export and Project Finance**

Export-credit Finance: They provide both single- as well as multi-sourced export-credit facilities by developing relationships with many of the principal export-credit agencies in different countries.

Project Advisory They provide advisory services to governments, project sponsors, contractors and special-purpose project companies in a range of industrial sectors.

Project-debt Arranging They also deliver a range of debt products, including commercial bank debt, capital-market bonds, export credit, local-currency bank debt and multi-lateral agency debt.

Forfeiting They can structure and execute the non-recourse off-balance-sheet facilities worldwide using bills of exchange, letters of credit, guarantees and formal loan agreements.

(b) Mergers and Acquisitions (M&A)

Investment banks give M&A guidance regarding strategic alternatives, financial restructurings and ownership transitions. The package of services includes strategic advice, sell-side and buy-side advisory, divestitures, recapitalizations, management and leveraged buyouts, and capital raising. Their scope of services include undertaking of legal documentation in vertical and horizontal mergers such as scheme of amalgamation, notice to shareholders, resolutions, and preparation of documents to be filed with high court. They also perform valuation of the amalgamated and amalgamating companies with a view to arrive at the ratios of equity swaps. Investment banks provide both buy-side as well as sell-side advisory services as part of their M&A advisory offering.

Buy-side Advisory They work with clients who have identified particular acquisition targets and assist them in negotiation, structuring, due diligence, financing and documentation of the transaction.

Phase 1: Target short-listing In this phase, the investment banker helps the client prioritise among the targets to create a shortlist, based on the acquisition criteria, investment parameters, and complete market analysis. It also uses its network of relationships with companies, private-equity funds and other intermediaries extensively in this phase to identify the right targets.

Phase 2: Preparing and executing term sheet After the companies are short-listed, the investment banker creates valuation and structuring models for the short-listed companies, prepares the term sheet which outlines all commercial terms and conditions of the transaction, drives deal negotiations with targets and also ensures that the client enters into a term sheet with the target company.

Phase 3: Due diligence and transaction closure Acquisitions are risky. Due diligence is investigating the deal from a commercial, financial and legal view point to confirm to the client that he is getting what he thinks he is buying. It involves verification of assets and liabilities, identification and quantification of risks, and protection needed against such risks. In this phase, the investment banker helps the client on preliminary business, due diligence on the target, and coordinates the overall due-diligence process.

Phase 4: Transaction closure Once the due-diligence process is complete, the investment banker negotiates on the final agreement with the target company to close the deal in the defined time frame. It even arranges finance for the transaction, if required.

Sell-side Advisory The investment bank helps corporates in the sale of a minority interest, a majority interest, or 100% of the stock or assets of the company, by identifying the specific qualified buyers unique to each engagement, which may include private companies, public companies, private-equity funds, hedge funds and international buyers.

Sell-side engagements have the following phases:

Phase 1: Collateral preparation An investment banker prepares a complete packet of information based on the company's business profile and its own knowledge of the market, which enables the transaction to be presented in front of potential acquirers/partners in a structured way.

Phase 2: Target short-listing After a complete market analysis and identification of potential buyers, the investment banker helps the client decide on the kind of strategic partners who will be the right partner for the client, meeting the potential partners and helping the client prioritise among the strategic partners to create a shortlist. It uses its network of relationships with companies, private-equity funds and other intermediaries, extensively in this phase to identify the right partners.

Phase 3: Preparing and executing term sheet In this phase, the investment banker helps the client analyse the various offers from potential partners, drives deal negotiations with partners and ensures that the client enters into a term sheet with the partner company, which meets the client's strategic objectives.

Phase 4: Due diligence and deal closure In this phase, the investment banker helps the client in coordinating the overall due-diligence process, and negotiates on the final agreements with the potential acquirer to close the deal.

Investment banks assist the corporates in reverse mergers such as merger of an unlisted company with a listed company and merger of a healthy company with a sick company under the provisions of Section 72 of the Income Tax Act.

Investment Banking Services

- Fund raising
- Advisory
- Export and Credit Finance
- M&A
- Promoter and Acquisition Financing Advisory
- Private-equity Advisory
- Infrastructure Advisory
- Strategic Advisory
- Debt syndication and structured finance
- Financial Restructuring and Turnaround Financing
- Private client services
- Sales and Trading
- Equity Research & Broking

(iii) Promoter and Acquisition-financing Advisory

Investment banks structure the appropriate financing solutions for client-specific needs. They arrange for: Promoter Financing and Acquisition Financing.

Promoter Financing: It is mostly done to enable promoters to raise their stake in the company. The financing is usually against collateral of shares or other securities held by the promoter in any of the group company. It can also be structured to refinance a loan raised against the same shares by the promoter earlier.

Acquisition Financing: Indian companies are now on a spree of acquisitions, both domestic as well as overseas. Acquisition financing plays a critical role in the success of inorganic growth planned by the acquirer. An investment banker advises and arranges on acquisition financing through financing structures which comprise foreign currency, senior-secured debt with a recourse to parent companies, rupee senior-secured debt with a recourse to parent companies, equity investment by the promoters, non-recourse debt and guaranteed mezzanine debt.

(iv) Private-equity Advisory

They also provide advice on private-equity funding to both the corporates as well as private-equity funds. They help the private-equity fund identify the emerging industries and firms with a good potential to invest therein. They help these investors explore transactions with target firms, help investors meet the target companies and help the investor prioritise among the targets short-listed. They also advise promoters and companies on the key considerations in a Private Equity (PE) fund-raising exercise.

(v) Infrastructure Advisory

Infrastructure development on a commercial viable basis is the need of the hour. Infrastructure advisory encompasses power generation, airport construction and transportation including air-cargo transportation and development of roads, airports, and associated infrastructures. This sector has unique financing requirements. Investment bankers provide infrastructure-project companies and developers infrastructure capital and advisory services. Infrastructure-capital services include raising capital through private equity, project equity, structured finance, and external commercial borrowings (ECBs). Their advisory services include providing specialized project services from concept to commissioning—from pre-investment feasibility studies and appraisals to development of joint ventures and company formation, assisting international companies in identifying and implementing projects in India, and providing specialized information for profitable and economic implementation of projects.

(vi) Strategic Advisory Services

Investment banks help corporates frame and implement key strategies relating to their business. These key strategies relate to entry into new geographies/services, exit from certain businesses/corporate restructuring and off-shoring for end-customers/on-shore vendors. They also help companies form strategic business alliances and assess capital-structure alternatives that create flexibility for executing on-growth opportunities.

(vii) Debt Syndication and Structured Finance

Investment banks help corporates raise debt capital and structured debt from the market, which includes cash-flow securitization and factoring under various structured financing options for various purposes, including projects, expansions, modernizations, and in-structuring and syndicating funds for acquisitions in India and overseas. They prepare corporate profiles, financial profiles and information memoranda for loan syndication-arranging loan from a single development finance institution or a syndicate of consortium.

(viii) Financial Restructuring and Turnaround Financing

Investment banks assist sick corporates with financial turnaround objectives to structure their capital. They design innovative structures and revival plans for implementing turnaround strategies and financial restructuring of liabilities. They also assist these corporates to raise funds. Investment banks play a significant role in leveraged buyouts of companies in distress. They also work with domestic and foreign banks in India in selling as well as buying NPA portfolios.

(ix) Private-client Services

Investment banks provide financial services to corporate clients and their senior executives, private-equity firms, middle-market institutions and high net-worth individuals, including wealth management and stock-trading services. They provide a high level of client service in terms of providing valuable investment decisions and guiding the high net-worth investor to make money.

(x) Sales and Trading

Investment banks provide trade execution and liquidity services to institutional investors. Sales and trading include trading in bonds, equity, currency, futures and options, and commodities.

(xi) Equities Research and Broking

An investment bank through its research team offers research and analysis of specific industries and offers advice for equities to its clients.

MERCHANT-BANKING SERVICES

Securities and Exchange Board of India (Merchant Banker) Regulations, 1992, define 'merchant banker' as any person who is engaged in the business of issue management, either by making arrangements regarding selling, buying, or subscribing to securities, or acting as a manager, consultant, or advisor, or rendering corporate-advisory services in relation to such issue management.

It is mandatory to appoint a merchant banker in case of public issues, rights issues, open offers and buy-backs. Merchant bankers facilitate the issue process by directing and coordinating the activities with underwriters, registrars and bankers, appropriately pricing and marketing the issue and complying with SEBI guidelines. Merchant bankers have been prohibited from carrying on any fund-based activity such as acceptance of deposits, leasing and bill discounting. They are not allowed to borrow funds from the market and engage in the acquisition and sale of securities on a commercial basis.

SEBI (MERCHANT BANKER) REGULATIONS, 1992

A merchant banker to carry on any activity of the issue management, which will inter-alia consist of preparation of prospectus and other information relating to the issue, determining financial structure, tie-up of financiers, and final allotment and refund of the subscription, has to get a certificate of registration from the SEBI. There are 189 merchant bankers registered with the SEBI.

The Securities and Exchange Board of India (Merchant Bankers) Regulations, 1992 define merchant banker as Merchant Banker means any person who is engaged in the business of issue management either by making arrangements regarding selling, buying or subscribing to securities or acting as manager, consultant, adviser or rendering corporate advisory service in relation to such issue management.

The SEBI shall take into account, for considering the grant of a certificate, all matters, which are relevant to the activities relating to merchant banker and, in particular, the applicant complies with the following requirements, namely:

1. The applicant shall be a body corporate other than a non-banking financial company, as defined under Clause (f) of Section 45-I of the Reserve Bank of India Act, 1934 (2 of 1934), as amended from time to time.
2. Provided that the merchant banker, who has been granted registration by the Reserve Bank of India to act as a primary dealer, may carry on such activity subject to the condition that it shall not accept or hold any public deposit.
3. a. The applicant has the necessary infrastructure like adequate office space, equipments, and manpower to effectively discharge his activities.
- b. The applicant has in his employment a minimum of two persons who have the experience to conduct the business of the merchant banker.
- c. A person directly or indirectly connected with the applicant has not been granted registration by the Board; 'directly or indirectly connected' means any person being an associate, subsidiary, inter-connected, or group company of the applicant, in case of the applicant being a body corporate.
- d. The applicant fulfils the capital-adequacy requirement, which is a net worth of not less than five-crore rupees. 'Net worth' means the sum of paid-up capital and free reserves of the applicant at the time of making application.
- e. The applicant, his partner, director or principal officer is not involved in any litigation connected with the securities market which has an adverse bearing on the business of the applicant.

- Merchant banker is a person who is engaged in the business of issue management, either by making arrangements regarding selling, buying or subscribing to securities, or acting as a manager, consultant or advisor or rendering corporate-advisory services in relation to such issue management.

Some of the Leading Merchant-bankers Registered with SEBI

- SBI Capital Markets Ltd
- ICICI securities Ltd
- Kotak Mahindra Capital Company Ltd
- Reliance Securities Ltd
- IFCI Financial Services Ltd

- f. The applicant, his director, partner or principal officer has not at any time been convicted for any offence involving moral turpitude or has been found guilty of any economic offence.
- g. The applicant has the professional qualification from an institution recognized by the government in finance, law, or business management; and the applicant is a fit and proper person.
- h. The grant of certificate to the applicant is in the interest of investors.

The certificate of registration granted under Regulation 8 and its renewal granted under Regulation 9, shall be valid for a period of 3 years from the date of its issue to the applicant. No merchant banker, other than a bank or a public financial institution, who has been granted a certificate of registration under these regulations, shall after 30 June 1998 carry on any business other than that in the securities market.

SEBI has classified merchant bankers into following categories namely:

- a. Category I, that is— (i) to carry on any activity of the issue management, which will, *inter alia*, consist preparation of prospectus and other information relating to the issue, determining financial structure, tie up of financiers and final allotment and refund of the subscriptions; and (ii) to act as adviser, consultant, manager, underwriter, portfolio manager;
- b. Category II, that is to act as an adviser, consultant, co-manager, underwriter, portfolio manager;
- c. Category III, that is to act as underwriter, adviser, consultant to an issue;
- d. Category IV, that is to act only as an adviser or consultant to an issue.

A merchant banker can carry on the activity as portfolio manager only if he obtains separate certificate of registration under the provisions of the Securities and Exchange Board of India (Portfolio Manager) Regulations, 1993.

Appointment of Lead Merchant Bankers

The lead manager plays an important role in designing the instrument, pricing the issue, timing the issue, marketing, preparing the offer document, listing and allotment/refund. They can act as Book-running Lead Manager/Lead Manager for the IPOs/FPOs/Right issues/Debt issues.

No lead manager shall agree to manage or be associated with any issue unless his responsibilities relating to issue mainly, those of disclosures, allotment and refund are clearly defined, allocated and determined and a statement specifying such responsibilities is furnished to the Board at least one month before the opening of the issue for subscription:

Provided that where there are more than one lead merchant bankers to the issue, the responsibilities of each of such lead merchant bankers shall clearly be demarcated and a statement specifying such responsibilities shall be furnished to the Board at least one month before the opening of the issue for subscription.

A lead merchant banker shall not be associated with any issue if a merchant banker who is not holding a certificate is associated with the issue.

Merchant Banker not to act as Such for an Associate

A merchant banker shall not lead/manage any issue or be associated with any activity undertaken under any regulations made by the Board. If he is a promoter or a director or an associate of the issuer of securities or of any person making an offer to sell or purchase securities in terms of any regulations made by the Board.

Provided that a merchant banker who is an associate of such issuer or person may be appointed, if he is involved only in the marketing of the issue or offer.

Explanation: For the purposes of this regulation, a merchant banker shall be deemed to be an “associate of the issuer or person” if (i) either of them controls, directly or indirectly through its subsidiary or holding company, not less than fifteen per cent of the voting rights in the other; or (ii) either of them, directly or indirectly, by itself or in combination with other persons, exercises control over the other; or (iii) there is a common director, excluding nominee director, amongst the issuer, its subsidiary or holding company and the merchant banker.

Underwriting Obligations

In respect of every issue to be managed, the lead merchant banker holding a certificate under Category I shall accept a minimum underwriting obligation of five per cent of the total underwriting commitment or rupees twenty-five lacs, whichever is less.

Provided that if the lead merchant banker is unable to accept the minimum underwriting obligation, that lead merchant banker shall make arrangement for having the issue underwritten to that extent by a merchant banker associated with the issue and shall keep the Board informed of such arrangement.

Acquisition of Shares Prohibited

No merchant banker or any of its directors, partner or manager or principal officer shall either on their respective accounts or through their associates or relatives, enter into any transaction in securities of bodies corporate on the basis of unpublished price sensitive information obtained by them during the course of any professional assignment either from the clients or otherwise.

Information to the Board

Every merchant banker shall submit to the Board complete particulars of any transaction for acquisition of securities of anybody corporate whose issue is being managed by that merchant banker within fifteen days from the date of entering into such transaction.

Provided that complete particulars of any transaction for acquisition of securities made in pursuance of underwriting or market making obligations in accordance with Chapter XA of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009 shall be submitted to the Board on quarterly basis.

Disclosures to the Board

1. A merchant banker shall disclose to the Board, as and when required, the following information, namely— (i) his responsibilities with regard to the management of the issue; (ii) any change in the information or particulars previously furnished, which have a bearing on the certificate granted to it; (iii) the names of the body corporate whose issues he has managed or has been associated with; (iv) the particulars relating to the breach of the capital adequacy requirement as specified in regulation 7; (v) relating to his activities as a manager, underwriter, consultant or adviser to an issue, as the case may be.
2. The merchant banker shall submit a periodic report in such manner as may be specified by the Board from time to time.

PRE-ISSUE OBLIGATIONS

Merchant bankers play an important role in issue-management process. They have to comply with SEBI rules and regulations, and also guidelines for Disclosures and Investor Protection (DIP).

Documents to be Submitted Along with the Offer Document by the Lead Manager

(i) Memorandum of Understanding (MOU)

Memorandum of understanding (MOU) has to be entered into between a lead merchant banker and the issuer company, specifying their mutual rights, liabilities and obligations relating to the issue. The lead merchant banker responsible for drafting of the offer documents shall ensure that a copy of the MOU entered into with the issuer company is submitted to the Board, along with the draft-offer document.

(ii) Inter-se Allocation of Responsibilities

In case a public or rights issue is managed by more than one merchant banker, the rights, obligations and responsibilities of each merchant banker shall be demarcated as specified in Schedule II. In case of undersubscription at an issue, the lead merchant banker responsible for underwriting arrangements shall invoke underwriting obligations and ensure that the underwriters pay the amount of devolvement and the same shall be incorporated in the inter-se allocation of responsibilities.

(iii) Due-diligence Certificate

The lead merchant banker shall exercise due diligence and is required to submit to SEBI a due-diligence certificate, confirming that the disclosures made in the draft prospectus or letter of offer are true, fair and adequate to enable the prospective investors to make a well-informed investment decision. The lead merchant banker shall furnish to the Board a due-diligence certificate as specified in Schedule III along with the draft-offer document. In case of a fast-track issue, the lead merchant banker shall furnish a

Pre-issue Obligation of Merchant Banker

- Submitting Offer Document
- Submitting an undertaking
- Submitting, list of promoters group
- Appointment of intermediaries
- Appointment of underwriter
- Making offer Document public
- Filing a No-complaint certificate
- Appointing Authorized collection agents
- Entering into an agreement with Depository/ies

due-diligence certificate to the Board as per the format specified in Schedule III, after including therein additional confirmations /certification to Schedule III, as specified in Schedule VI-A, along with the copy of the red-herring prospectus, prospectus or letter of offer, as the case may be. In case of a debenture issue, the lead merchant banker shall also furnish to the SEBI a due-diligence certificate given by the debenture trustee in the format specified along with the draft-offer document or in case of a fast-track issue, along with the copy of the red-herring prospectus, prospectus or letter of offer.

(iv) Certificates Signed by the Company Secretary or Chartered Accountant, in Case of Listed Companies Making Further Issue of Capital in Respect of the Following points:

1. All refund orders of the previous issues were despatched within the prescribed time and in the prescribed manner.
2. All security certificates were despatched to the allottees, within the prescribed time and in the prescribed manner.
3. The securities were listed on the stock exchanges as specified in the offer documents.

Undertaking

The issuer shall submit an undertaking to the SEBI to the effect that transactions in securities by the 'promoter,' the 'promoter group,' and the immediate relatives of the 'promoters' during the period between the date of filing the offer documents with the Registrar of Companies or stock exchange as the case may be and the date of closure of the issue, shall be reported to the stock exchanges concerned within 24 hours of the transaction(s).

List of Promoters' Group and Other Details

The issuer company shall submit to the SEBI the list of the persons who constitute the Promoters' Group and their individual shareholding.

The issuer company shall submit to the stock exchanges on which securities are proposed to be listed, the permanent account number, the bank account number and the passport number of the promoters, at the time of filing the draft-offer document to them.

Appointment of Intermediaries

A merchant banker shall not lead manage the issue if he is a promoter or a director or an associate of the issuer company.

Provided that a merchant banker holding the securities of the issuer company may lead manage the issue if;

1. the securities of the issuer company are listed or proposed to be listed on the Over the Counter Exchange of India (OTCEI) and
2. the market makers have either been appointed or are proposed to be appointed as per the offer document.

Provided further that a merchant banker who is an associate of the issuer company may be appointed as a merchant banker for the issue, if it is involved only in the marketing of the issue. A merchant banker shall be deemed to be an associate of the issuer if:

1. either of them controls directly or indirectly, through itself, its subsidiary or the holding company, not less than 15% of the voting power of the other; or
2. either of them, directly or indirectly, by itself or in combination with other persons, exercises control over the other; or
3. there is a common director, excluding nominee director, among the body corporate/its subsidiary or the holding company and the merchant banker.

Appointment of Other Intermediaries

The lead merchant banker shall ensure that the other intermediaries are duly registered with the Board, wherever applicable. Before advising the issuer on the appointment of other intermediaries, the lead

merchant banker shall independently assess the capability and the capacity of the various intermediaries to carry out the assignment.

The lead merchant banker shall ensure that issuer companies enter into an MOU with the intermediary(ies) concerned, whenever required, and also take note of the deemed agreement with the Self-certified Syndicate Banks, as provided in the Application Supported by Blocked Amount (ASBA) process.

The lead merchant banker shall ensure that bankers to the issue are appointed in all the mandatory-collection centres.

The lead merchant banker shall not act as a registrar to an issue in which it is also handling the post-issue responsibilities.

The lead merchant banker shall ensure that;

1. The registrars to issue registered with the Board are appointed in all public issues and rights issues.
2. In case where the issuer company is a registered registrar to an issue, the issuer shall appoint an independent outside registrar to process its issue.

The registrar to an issue which is associated with the issuer company as a promoter or a director shall not act as the registrar for the issuer company.

Where the number of applications in a public issue is expected to be large, the issuer company in consultation with the lead merchant banker may associate one or more registrars registered with the Board for the limited purpose of collecting the application forms at different centres and forward the same to the designated Registrar to the Issue as mentioned in the offer document. The designated Registrar to the Issue shall be primarily and solely responsible for all the activities as assigned to them for the issue management.

Underwriting

The lead merchant banker shall satisfy themselves about the ability of the underwriters to discharge their underwriting obligations. There are 5 underwriters registered with the SEBI.

The lead merchant banker shall:

1. incorporate a statement in the offer document to the effect that in the opinion of the lead merchant banker, the underwriters' assets are adequate to meet their underwriting obligations;
2. obtain the underwriters' written consent before including their names as underwriters in the final-offer document.

In respect of every underwritten issue, the lead merchant banker(s) shall undertake a minimum underwriting obligation of 5% of the total underwriting commitment or ₹25 lakhs, whichever is less. The outstanding underwriting commitments of a merchant banker shall not exceed 20 times its net worth at any point of time.

In respect of an underwritten issue, the lead merchant banker shall ensure that the relevant details of underwriters are included in the offer document.

Offer Document to be Made Public

The draft-offer document filed with the SEBI shall be made public for a period of 21 days, from the date of filing the offer document with the SEBI.

The lead merchant banker shall,

1. while filing the draft-offer document with the Board can also file the draft-offer document with the stock exchanges where the securities are proposed to be listed;
2. while filing the copy of the red-herring prospectus, prospectus or letter of offer, as the case may be, with the Board, can also file the copy of the red-herring prospectus, prospectus or letter of offer with the stock exchanges on which the securities to be offered in the fast-track issue are proposed to be listed;
3. make copies of the draft-offer document available to the public, host the draft and final-offer documents on the websites of the all the lead managers / syndicate members, associated with the issue, and also ensure that the contents of documents hosted on the websites are the same as that of their printed versions; and

4. obtain and furnish to the SEBI, an in-principle approval of the stock exchanges, for listing of the securities, within 15 days of filing of the draft-offer document with the stock exchanges.

No-complaint Certificate

After a period of 21 days from the date the draft-offer document was made public, the lead merchant banker shall file a statement with the Board:

1. giving a list of complaints received by it;
2. a statement whether it is proposed to amend the draft-offer document or not, and;
3. highlight those amendments.

Mandatory-collection Centres

The minimum number of collection centres for an issue of capital shall be:

1. The four metropolitan centres situated at Mumbai, Delhi, Calcutta and Chennai.
2. All such centres where the stock exchanges are located in the region in which the registered office of the company is situated.
3. The regional division of collection centres.

The issuer company shall be free to appoint as many collection centres as it may deem fit in addition to the above minimum requirement.

In respect of issues where ASBA is () applicable, all designated branches of Self-certified Syndicate Banks shall be deemed as mandatory-collection centres.

Authorized Collection Agents

The issuer company can also appoint authorized collection agents in consultation with the lead merchant banker, subject to necessary disclosures including the names and addresses of such agents made in the offer document. The modalities of selection and appointment of collection agents can be made at the discretion of the lead merchant banker. The lead merchant banker shall ensure that the collection agents so selected are properly equipped for the purpose, both in terms of infrastructure and manpower requirements.

The collection agents may collect such applications, as are accompanied by payment of application monies paid by cheques, drafts and stock invests.

The authorized collection agent shall not collect application moneys in cash.

The applications collected by the collection agents shall be deposited in the special share-application account with the designated scheduled bank, either on the same date or latest by the next working day.

The application forms, along with the duly reconciled schedules, shall be forwarded by the collection agent to the Registrars to the Issue, after realization of cheques and after weeding out the applications in respect of cheque-return cases, within a period of 2 weeks from the date of closure of the public issue.

The offer documents and application forms shall specifically indicate that the acknowledgement of receipt of application moneys given by the collection agents shall be valid and binding on the issuer company and other persons connected with the issue.

The investors from the places other than the places where the mandatory-collection centres and authorized collection agents are located, can forward their applications along with stock invests to the Registrars to the Issue, directly by registered post with acknowledgement due.

The applications received through the registered post shall be dealt with by the Registrars to the Issue in the normal course.

Abridged Prospectus

The lead merchant banker shall ensure the following:

1. Every application form including ASBA forms, distributed by the issuer company or anyone else, is accompanied by a copy of the abridged prospectus.
2. The application form including ASBA forms may be stapled to form a part of the abridged prospectus. Alternatively, it may be a perforated part of the abridged prospectus.

3. The abridged prospectus shall not contain matters which are extraneous to the contents of the prospectus.
4. Enough space shall be provided in the application form to enable the investors to file in various details like name, address and so on.

Agreements with Depositories

The lead manager shall ensure that the issuer company has entered into agreements with all the depositories for dematerialization of securities. He shall also ensure that an option be given to the investors to receive the allotment of securities in a dematerialized form, through any of the depositories.

POST-ISSUE OBLIGATIONS

Post-issue Monitoring Reports

Irrespective of the level of subscription, the post-issue lead merchant banker shall ensure the submission of the post-issue monitoring reports, as per the formats specified by the SEBI.

These reports shall be submitted within 3 working days from the due dates.

The due date for submitting the post-issue monitoring report, in case of public issues by listed and unlisted companies:

1. A 3-day monitoring report in case of issue through book-building route, for book-built portion:
The due date of the report shall be the 3rd day from the date of allocation in the book-built portion or 1 day prior to the opening of the fixed-price portion, whichever is earlier.
2. A 3-day monitoring report in other cases, including fixed-price portion of book-built issue:
The due date for the report shall be the 3rd day from the date of closure of the issue.

Final post-issue monitoring report for all issues:

The due date for this report shall be the 3rd day from the date of listing or 78 days from the date of closure of the subscription of the issue, whichever is earlier.

The due dates for submitting the post-issue monitoring report in case of rights issues:

1. 3-day Post-issue Monitoring Report:
The due date for this report shall be the 3rd day from the date of closure of subscription of the issue.
2. 50-day Post-issue Monitoring Report:
The due date for this report shall be the 50th day from the date of closure of subscription of the issue.

Due-diligence certificate to be submitted with the final post-issue monitoring report. The post-issue lead merchant banker shall file a due-diligence certificate in the format specified, along with the final post-issue monitoring report.

Redressal of Investor Grievances

The post-issue lead merchant banker shall actively associate himself with post-issue activities, namely, allotment, refund, dispatch and giving instructions to Self-certified Syndicate Banks and shall regularly monitor the redressal of investor grievances arising there from.

Coordination with Intermediaries

1. The post-issue lead merchant banker shall maintain a close coordination with the Registrars to the Issue and arrange to depute its officers to the offices of various intermediaries at regular intervals, after the closure of the issue, to monitor the flow of applications from the collecting-bank branches and/or Self-certified Syndicate Banks, processing of the applications including application form for Applications Supported by Blocked Amount and other matters, till the basis of allotment is finalized, despatch security certificates and refund orders completed, and securities listed.
2. Any act of omission or commission on the part of any of the intermediaries noticed during such visits, shall be duly reported to the Board.

Post-issue Obligation

- Submitting post-issue monitoring reports
- Redressal of investor grievances
- Maintaining a close coordination with intermediaries
- Ensuring full subscription of the issue
- Verifying Post-issue Advertisements details
- Finalizing basis of allotment and allotment procedure

Underwriters

1. a. If the issue is proposed to be closed at the earliest closing date, the lead merchant banker shall satisfy himself that the issue is fully subscribed before announcing the closure of the issue.
b. In case there is no definite information about the subscription figures, the issue shall be kept open for the required number of days to take care of the underwriters' interests and to avoid any dispute, at a later date, by the underwriters in respect of their liability.
2. In case there is a devolvement on underwriters, the lead merchant banker shall ensure that the underwriters honour their commitments within 60 days from the date of closure of the issue.
3. In case of undersubscribed issues, the lead merchant banker shall furnish information in respect of underwriters who have failed to meet their underwriting devolvement to the SEBI in the format specified.

Bankers to an Issue

The post-issue lead merchant banker shall ensure that moneys received a pursuant to the issue and kept in a separate bank (*i.e.*, Bankers to an issue), as per the provisions of Section 73(3) of the Companies Act, 1956, is released by the said bank, only after the listing permission under the said Section has been obtained from all the stock exchanges where the securities were proposed to be listed as per the offer document.

Post-issue Advertisements

A post-issue lead merchant banker shall ensure that in all issues, an advertisement giving details relating to oversubscription, basis of allotment, number, value and percentage of all applications including Applications Supported by Blocked Amount, number, value and percentage of successful allottees for all applications including Applications Supported by Blocked Amount, date of completion of despatch of refund orders/instructions to Self-certified Syndicate Banks by the Registrar, the date of despatch of certificates and the date of filing of listing application is released within 10 days from the date of completion of the various activities at least in an English National Daily with wide circulation, one Hindi National Paper and a Regional language daily, circulated at the place where the registered office of the issuer company is situated.

The post-issue lead merchant banker shall ensure that the issuer company/advisors/brokers or any other agencies connected with the issue, do not publish any advertisement stating that the issue has been oversubscribed or indicating the investors' response to the issue, during the period when the public issue is still open for subscription by the public.

An advertisement stating that 'the subscription to the issue has been closed' may be issued after the actual closure of the issue.

Basis of Allotment

In a public issue of securities, the Executive Director / Managing Director of the designated stock exchange, along with the post-issue lead merchant banker and the Registrars to the Issue, shall be responsible to ensure that the basis of allotment is finalized in a fair and proper manner in accordance with the DIP guidelines.

Proportionate-allotment Procedure

An allotment shall be on a proportionate basis within the specified categories, rounded off to the nearest integer, subject to a minimum allotment being equal to the minimum application size, as fixed and disclosed by the issuer.

The above-proportionate allotments of securities in an issue, that is oversubscribed, shall be subject to reservation for the retail individual investors as described in the following:

1. A minimum 50% of the net offer of securities to the public shall initially be made available for allotment to retail individual investors, as the case may be.
2. The balance net offer of securities to the public shall be made available for allotment to:
 - a. individual applicants other than retail individual investors, and
 - b. other investors including corporate bodies/institutions, irrespective of the number of shares, debentures, and so on, applied for.
3. The unsubscribed portion of the net offer to any one of the categories specified in (1) or (2) shall/ may be made available for allotment to applicants in the other category, if so required.

Other Responsibilities

The lead merchant banker shall ensure that the despatch of share certificates/refund orders/and demat credit is completed and the allotment and listing of documents submitted to the stock exchanges within 2 working days of the date of allotment.

The post-issue lead manager shall ensure that all steps for completion of the necessary formalities for listing and commencement of trading at all stock exchanges, where the securities are to be listed, are taken within 7 working days of the finalization of basis of allotment.

A lead merchant banker shall ensure the payment of interest to the applicants for the delayed dispatch of allotment letters, refund orders, and so on, as prescribed in the offer document.

The post-issue lead merchant banker shall ensure that the dispatch of refund orders/allotment letters/share certificates is done by way of registered post/certificate of posting, as may be applicable.

In case of all issues, an advertisement giving details relating to oversubscription, basis of allotment, number, value and percentage of all applications received, including Applications Supported by Blocked Amount, number, value and percentage of successful allottees for all applications including Applications Supported by Blocked Amount, date of completion of despatch of refund orders/instructions to Self-certified Syndicate Banks by the registrar, date of despatch of certificates and date of filing of listing application. Such advertisement shall be released within 10 days from the date of completion of the various activities.

The post-issue lead merchant banker shall continue to be responsible for the post-issue activities, till the subscribers had received the shares/debenture certificates or refund of application moneys and the listing agreement is entered into by the issuer company with the stock exchange and listing/trading permission is obtained.

CHANGING LANDSCAPE OF INVESTMENT BANKING

Investment banking was a lucrative business till 2007. The revenues during the year 2007 were the highest for the investment-banking industry as a large number of deals worth \$51 billion were struck. However, the sub-prime mortgage crisis took a toll on the global-investment banks. These investment banks were not under the control of either the Federal Reserve Bank or the US Securities and Exchange Commission (SEC), which made it easier for them to take higher risks. Wall Street's oldest and biggest investment banks collapsed in the late 2008 as a result of the financial turmoil. Bear Stearns was acquired by JP Morgan Chase in March 2008. Lehman Brothers filed for Chapter 11 Bankruptcy and was declared bankrupt in September 2008. The Asian and European operations of Lehman Brothers were bought by Nomura and the North American Lehman operations by Barclays Capital. Merrill Lynch was acquired by Bank of America for \$50 billion. Goldman Sachs and Morgan Stanley converted themselves into bank-holding companies or commercial banks.

The impact of the collapse of these banks has been felt on the Indian investment banks. There will be a drop in big deals and fat fees and revenues. Even in the midst of this gloomy environment, investment banks have opportunities which they can tap with properly designed strategies and go global. The growth rate of the Indian economy has slowed down but it is fairly good when compared to the growth rate of the developed countries. Even though the capital markets are in a dismal state, India is still an attractive market for investment. Even foreign investment banks have planned to start their operations in India. The Indian investment banks need to design new strategies for survival and growth, such as focusing on key business areas, exploring new and alternate markets and market segments, creating alliances with boutique firms, developing strong and long-term relationship with the existing and new clients, giving quality advice to clients and assisting them in every stage of their growth, hiring qualified staff and promoting ethical behaviour.

Some Leading International Investment Banks Operating in India

- Goldman Sachs
- Credit Suisse
- Bank of America–Merill Lynch
- City group Global Markets India Pvt Ltd
- Barclay's Bank
- Morgan Stanley
- The world's No.1 investment bank in 2009 was JP Morgan Chase & Co.

KEY TERMS

Investment Banking

Merchant Banking

SUMMARY

1. Investment banks are financial intermediaries in the business of providing investment and financial advisory services to companies, governments and institutional investors.
2. Investment banks perform two types of functions:
They help public and private corporates in issuing securities in the primary market, provide guarantee by standby underwriting and

act as intermediaries in trading for clients. They give companies and investors financial advice.

3. There are three types of investment banks. They can be classified as: Full-service global-investment banks, Regional-investment banks and boutique firms.
4. Securities and Exchange Board of India (Merchant Banker) Regulations, 1992 define 'merchant banker' as any person who is engaged in the business of issue management, either by making arrangements

regarding selling, buying or subscribing to securities or acting as a manager, consultant, advisor or rendering corporate advisory services in relation to such issue management.

5. Merchant bankers facilitate the issue process by directing and coordinating the activities with underwriters, registrars and bankers, appropriately pricing and marketing the issue, and complying with the SEBI guidelines.
6. They have to ensure compliance with the SEBI rules and regulations, as also guidelines for DIP.

REVIEW QUESTIONS

1. What is investment banking? How is it different from commercial banking?
2. What is the role of investment banks? State the different types of investment banks?

3. What kind of financial advisory services do investment banks provide?
4. Define merchant banker? What is the role of a merchant banker in the capital market?
5. What are the pre- and post-issue obligations of merchant bankers?

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