Chapter 5

Investment Banks
5.1 Introduction

At a very macro level, 'Investment Banking' as the term suggests, is concerned with the primary function of assisting the capital market in its function of capital inter­mediation, i.e. the movement of financial resources from those who have them (the Investors), to those who need to make use of them for generating GDP (the Issuers). Banking and financial institutions on the one hand and the capital market on the other are the two broad platforms of institutional intermediation for capital flows in the economy. Therefore, it could be inferred that investment banks are those institutions that are the counterparts of banks in the capital market in the function of intermediation in resource allocation. Nevertheless, it would be unfair to conclude so, as that would confine investment banking to a very narrow sphere of its activities in the modern world of high finance. Over the decades, backed by evolution and also fuelled by recent technological developments, investment banking has transformed repeatedly to suit the needs of the finance community and thus become one of the most vibrant and exciting segment of financial services. Investment bankers have always enjoyed celebrity status, but at times, they have paid the price for excessive flamboyance as well.

To continue from the above, in the words of John F. Marshall and M.E. Ellis, 'investment banking is what investment bank do'. This definition can be explained in the context of how investment banks have evolved in their functionality and how history and regulatory intervention have shaped such an evolution. Much of investment banking in its present form thus owes its origins to the financial markets in USA, due to which, American investment banks have been leaders in the American and Euro markets as well. Therefore, the term 'investment banking' can arguably be said to be of American origin. Their counterparts in UK were termed as 'merchant banks' since they had confined themselves to capital market intermediation until the US investment banks entered the UK and European markets and extended the scope of such businesses.
5.2 Investment Banking and Merchant Banking Distinguished

At this stage, it would be relevant therefore, to draw a fine line of distinction between the terms 'Investment Banking' and 'Merchant Banking'. 'Merchant Banking' as the term suggests, is the function of intermediation in the capital market. It consists of assisting issuers to raise capital by placement of securities issued by them with investors. However, merchant banking is not merely about marketing of securities in an agency capacity. The Merchant Banker has an onerous responsibility towards the investors who invest in such securities. The regulatory authorities require the merchant banking firms to promote quality issues, maintain integrity and ensure compliance with the law on account and on behalf of the issuers as well. Therefore, merchant banking is a fee based service for management of public offers, popularly known as 'issue management' and for private placement of securities in the capital market. In India, the Merchant Banker leading a public offer is also called as the 'Lead Manager'. [1]

On the other hand, the term 'Investment Banking' has a much wider connotation and is gradually becoming more of an inclusive term to refer to all types of capital market activity, both fund-based and non-fund based. This development has been driven more by the way the American investment banks have evolved themselves over the past century. Given this situation, investment banking encompasses not merely merchant banking but other related capital market activities such as stock trading, market making, underwriting, broking and asset management as well. Besides the above, investment banks also provide a host of specialized corporate advisory services in the areas of project advisory, business and financial advisory and mergers and acquisitions. [1]
5.3 Business Portfolio of Investment Banks

Globally, investment banks handle significant fund-based business of their own in the capital market along with their non-fund service portfolio which is offered to clients. However, these distinct segments are handled either on the same balance sheet or through subsidiaries and affiliates depending upon the regulatory requirements in the operating environment of each country. All these activities are segmented across three broad platforms—equity market activity, debt market activity and merger and acquisition (M&A) activity. In addition, given the structure of the market, there is also a segmentation based on whether a particular investment bank belongs to a banking parent or is a stand-alone pure investment banks. Figure 5.1 represents the broad spectrum of global investment activities.
Figure 5.1 Investment Banking Spectrums

INVESTMENT BANKING

CORE BUSINESS PORTFOLIO

Non-fund based

Equity portfolio-Merchant Banking (Issue Management), private placements

Debt portfolio-Issue Management, private placement, structure finance issuances such as

M & A-M & A advisory, corporate advisory, project

Fund Based

Equity portfolio-Underwriting, market making

Debt portfolio-Underwriting, market making

M & A portfolio-Investing in private equity, LBOs and MBOs

SUPPORT ACTIVITY PORTFOLIO

Non-fund based

Equity portfolio-Equity broking, distribution, asset management, custodial services, wealth management (private banking), research and analysis

Debt portfolio-Debt market broking, distribution, asset management, research

Derivative portfolio-Derivative broking, risk management, custodial services

Fund Based

Equity portfolio-Proprietary trading and portfolio investing, managing private equity funds and asset management funds

Debt portfolio-Trading, underwriting, market making and investing on own account in debt products and securitised instruments,

Derivative portfolio-Proprietary trading, managing hedge funds
From this diagram, it may be appreciated that investment banking encompasses a wide area of capital market based businesses and services and has a significant financial exposure to the capital market. Though investment banks also earn a significant component of their income from non-fund based activity, it is their capacity to support clients with fund-based services, which distinguishes them from pure merchant banks. In the US capital market, investment banks underwrite issues or buy them outright and sell them later to retail investors thereby taking upon themselves significant financial exposure to client companies. Besides, being such large financial power houses themselves, the global investment banks play a major role as institutional investors in trading and having large holdings of capital market securities. As dealers, they take positions and make a market for many securities both in the equity and derivative segments. They hold large inventories and therefore influence the direction of the market. JP Morgan, Bank of America Merrill Lynch, Morgan Stanley, Goldman Sachs and others are significant Market Investors both on their own account and on behalf of the billions of dollars of funds under their management.

The global mergers & acquisitions business is very large and measures up to trillions of dollars annually. Investment banks play a lead advisory role in this booming segment of financial advisory business. Besides, they come in as investors in management buy-outs and management buy-in transactions. On other occasions, wherein investments banks manage private equity funds, they also represent their investors in such buy-out deals.

In the case of universal banks such as the Citigroup or UBS Warburg, loan products form a significant part of the debt market business portfolio. Pure investment banks such as Goldman Sachs, Merrill Lynch and Morgan Stanley Dean Witter do not have commercial banking in their portfolio and therefore, do not offer loan products. Besides the larger firms, there are a host of other domestic players presents in each
country and min-sized investment bank, which either specialize in local markets or in certain product segments.

Some investment banks in the overseas markets also specialize in niche segments such as management of hedge funds, bullion trade, commodity hedges, real estate and other exotic markets.

5.4 Management of Public Offers and Private Placements

5.4.1 Initial Public Offers (IPO)

5.4.1.1 Significance of an IPO

It is important to evaluate whether the IPO decision is purely market driven or not. Before discussing determinants of the IPO decision, it is imperative to understand the significance of an IPO and what it does to a company. Every company when it is unlisted offers and ownership or equity opportunity to an outside investor which, for the purpose of the present discussion, has been termed as the 'private window'. The investors who invest in an unlisted company are either the promoters or strategic long-term investors or pure financial investors who come in for a time bound period. The differentiator between a promoter, strategic investor and financial investor is in terms of the investment objective. A promoter's prime concern is 'control' while that of a strategic investor is 'business opportunity'. On the other hand, the financial investor looks at 'return on investment'. These investors invest through the private window that cannot offer the facility of any time entry or exist into the company's equity capital. The private window also does not provide any price validation for the company's unlisted stock, which has to be derived from time to time through complex valuation methodologies.
When a company makes an IPO, what it actually creates is a second ownership opportunity that can be termed as the 'market window'. The market window, unlike the private window, provides any time entry and exit facility to investors from the company's equity capital. Therefore, it is meant either for the retail investors who would with to have instant liquidity for their investments or for speculators who intend to make profits through regular trading in the company's stock. In order to serve the interests of retail investors, the market window also performs the function of validating the company's worth on a continuous basis through an organized trading mechanism called the stock exchange which provides market quotes for the company's stock. Being a continuous evaluation mechanism, the market window is market driven—it can be overheated at times or be completely indifferent to the company's fundamentals. During times of frenetic market activity, the market window may overvalue a company's share while in dull phases; the market price can be extremely low. Due to this phenomenon, though empirically peaking, the market price tends to conform to the trends in the intrinsic worth of a share in the long term, at any given point of time, it represents the instant entry or exit price for an investor.

Unlike the market window, the private window need not be driven by the market price of a company's share, though it has some influence in its determination. A strategic investor would be prepared to pay an entry premium for the company's share, which may result in the company's share being valued at much more than its current market price. The premium that a strategic investor would want to pay is arrived at based on long-term considerations that have more of a business perspective than a pure financial perspective. Similarly, the promoters of a company would be prepared to pay more than the current market price as their concern is about controlling stakes in the company. On the same count financial investors could pay more than the current market price since they wish to take a long-term view on their investment.
Continuing on the same lines, wholesale investors may look for exist routes that are different from the market window available to retail investors. The private window provides exist routes such as a strategic sale to another wholesale investors, buy back by promoters and a merger with or takeover by another company. But in some cases, the market investors would with to make use of the market window as an exit route. This is achieved by taking the company public through an IPO, which opens up the market window. Alternatively, the financial investors may exist by making an 'offer for sale' of their shares to the retail investors which also opens up the market window. Lastly, financial investors may just want the company to make an IPO and open up the market window which can be used by them from time to time to make gradual sale of their holdings at the best available market prices.

This brings us to the discussion on how exactly an IPO should be perceived. Since an IPO is a significant milestone in the life of a company, it could have several implications such as the following mentioned below: [2]

- It can be source of finance if it is meant to finance a specific end use.
- It creates a new ownership opportunity called the market window and a class of investors called the 'retail investors'.
- It can be liquidity event since it creates an exit route for the existing and future investors of the company.
- It creates market capitalization for the company, which the aggregate value of all its issued shares as multiplied by the current market prices.
- The market capitalization of the company can both as an enhancement or a deterrent for future fund raising by the company in the equity route.
- Being listed can open up the gates for hostile takeover attempts on the company.
- It makes future acquisition of stakes in the company by the promoters quite expensive and cumbersome.
- It brings with it additional costs of regulatory compliance, certain restrictions on future capital transactions and cumbersome procedures.
Form the above implications; it is quite evident that an IPO can act as a double-edge sword. In good times it enhances shareholder wealth but in difficult times, listed status can become a hindrance and a drag on the company’s performance and prospects.

5.4.1.2 The IPO Decision

The moot point can therefore be stated thus—‘when does having a market window make sense to a company?’ This can be answered with reference to two stages the pre-IPO stage and the post-IPO stage. The pre-IPO discussion elates to the timing of the IPO decision, while the post-IPO discussion is about countenance or discontinuance of the listed status.

Timing an IPO is a strategic, financial and merchant banking decision. The strategic decision to make is to determine whether listing fits into the company’s overall corporate philosophy and if so, whether the company is mature enough for it. The financial decision to make is to decide whether the company needs the capital proposed to be raised, how much is to be raised and how effectively it should be deployed. The merchant banking decision is made to determine the appropriate structure, pricing, timing and marketing strategy for the IPO.

5.4.1.3 The Role of the Investment Banker in the IPO Process

The success of the IPO will to a large extent depend on the capabilities of the investment banker selected. However, in the absence of a model to guide issuers of securities in selecting investment banks, how does a company come up with the right investment banker to manage its IPO? Weston and Copeland (1989) identified three main functions or roles investment banks play in the IPO process and these include: Underwriting, Distribution and, Advice and Counsel.
Underwriting: This is the insurance function of bearing the risk of adverse price fluctuations during the period in which a new issue of securities is being distributed. There are two fundamental ways of doing this, and they are the firm commitment and best efforts underwriting agreements. The firm commitment agreement obligates the investment banker to assume all the risks inherent in the issue. On the other hand, the best efforts agreement absolves the investment banker from any risks in the issue. Under this underwriting agreement, the investment banker undertakes to help sell at least a minimum amount of the issue with any unsold amounts returned to the issuing firm. Where the investment banker is not able to sell the minimum quantity agreed upon, the whole issue is cancelled and reissued when the market is ready to accommodate the issue.

Distribution: Another related function to the one described above is the ability of the issuing firm to reach as many investors as possible with its security. According to Weston and Copeland (1989), investment banks play a very crucial role here, because of their expertise, network and long experience.

Advice and Counsel: This involves the investment banker making valuable inputs into decisions concerning its client ability to succeed in the capital market with an IPO. Its ability to make valuable inputs in this direction may largely depend on its experience in origination and selling of securities.

5.4.2 Right Issue

5.4.2.1 Concept of Rights

A rights issue is made to the existing shareholders of a company. The 'right' herein refers to the entitlement of a shareholder to apply for and receive additional shares in the company. Since the rights issue is made only to existing shareholders, such entitlement to apply for additional shares is also available to existing shareholders alone. However, the application for additional shares is only a right and not an
obligation on the shareholder. For the purpose of ascertaining the right, a 'record date' is fixed. All persons whose names appear in the register of members of the company as of the record date are eligible for the rights. The entitlement is fixed on a proportionate basis according to the entitlement ratio fixed under the rights issue. For example if rights issue is being made in the ratio of 1:2, it denotes that for every two existing shares held by a shareholder, the entitlement would be one new share under the rights issue. Therefore, if a shareholder presently holds 500 shares in the company as of the record date, such person's entitlement under the rights issue would be to apply for and receive 250 new shares in the right issue. 

As has been mentioned above, the entitlement is only a prerogative of the shareholder and not an obligation. Therefore, under the terms of the issue the shareholder would be given the right to subscribe for and receive the rights shares or to 'renounce the rights' in favour of any third person of the choice of the shareholders. Once the rights are renounced, the renounce is entitled to subscribe for and receive the rights shares. However, if the shareholder neither applies nor renounces the shares, the rights entitlement lapses and to that extent the rights issue is under-subscribed. Normally, the promoters of a company seek the right to apply for and take rights shares to the extent of the under-subscription in the rights issue. Such right for the promoters should form part of the terms of the issue and be disclosed in the letter of offer sent to the shareholders. In a rights issue, if all the shareholders subscribe for their rights, the pre-issue shareholding pattern remains intact after the issue. However, if the issue is under-subscribed and to that extent, the promoters take up the rights, the stake of the promoters in the company post-issue goes up. In a rights issue, there can be a situation of over-subscription since every shareholder can apply to the extent of the entitlement or more. The letter of offer has to specify the right of shareholders to apply for additional shares. The concerned stock exchange may waive such requirement if the company proposes to dispose-off the un-subscribed shares at the ruling market price or above. The allotment in the case of over-subscription would be made on pro-rata basis.
5.4.2.2 Pricing a Rights and Value of a Right

The next step to be discussed is based on the significance of the 'right' and when it makes sense to apply for it. A rights issue by definition is to the existing members of the company to provide additional financial assistance to the company. In that sense, a rights issue is the primary source for a listed company to seek additional capital from the primary market. Since existing shareholders had provided funds to the company when it reached out to them in its IPO, it is but natural to consider them in future as the first option. However, hidden herein is also the fact that since they had financed the company in the past, the company has to provide them better terms to finance to a second time as compared to the terms it would offer to first time subscribers. In other words, a rights issue has to price more favourably for an investor than a public issue. For a listed company, the market price becomes a ruling benchmark and if the rights issue is priced equivalent to or more than the ruling market price, the shareholder is better off buying the shares from the market than to subscribe to the rights. This factor has to be borne in mind for pricing a rights offer.

This brings us to the discussion on how to price a rights issue. Unlike in an IPO, where the company has no prior record of a quoted market price, in the rights issue of a listed company, the market price plays a major factor in pricing the rights. Though the fundamentals such as the EPS, book value of share and industry related P/E ratios are important considerations, what is of primary relevance in pricing the right share is the ruling market P/E ratio of the company. If a company is quoting at a P/E multiple which is above its peers in the industry, the rights can be priced accordingly. However, if the company is under-valued in the market, the pricing of the rights is also impacted to that extent. The pricing of the rights would impact the capital structure and the post-issue equity base of the company as well. The quantum of funds to be mobilized in the rights issue should be determined in conjunction with the pricing of the rights as per the above criteria.
5.4.2.3 Considerations for a Rights Issue

Considerations for Issuer

Before embarking on a rights issue, the issuer company has to weigh in the implications vis-a-vis alternative methods to achieve its objectives. The evaluation could be in terms of: [1]

- The primary objective of the rights issue is to raise funds or to reward shareholders or to seek consolidation of promoter's stakes.
- If the objective is to raise funds, is the rights issue an adequate source of finance for the company's fund requirement considering the likely price and desirable expansion in equity capital.
- If the objective is to provide an incentive for shareholder loyalty, the rights option has to be evaluated vis-a-vis alternatives such as a bonus issue or a higher dividend payout. If the company refers to retain cash, bonus issue is a better option. If the company proposes to raise funds while rewarding shareholders, a rights issue is a better option. However, rights issue involves floatation costs.
- The overall conditions in the primary market and the likely response of shareholders to the issue at the proposed price.
- The likelihood of the rights evoking a mediocre or poor response and its repercussions on the market price of the share.
- Availability of alternate sources of raising equity capital such as private equity or private placement apart from opportunities to seek additional borrowings.

Considerations for Investor

As far as an investor is concerned, a rights issue needs to be evaluated from a cost-benefit perspective in the line of: [1]
• The cost of the rights share vis-a-vis the carrying cost of the holding or the cum-rights price in the market. If the investor is an existing shareholder, the entitlement is automatic. However, for a market investor, the entitlement to the rights is possible only if the company's shares are acquired from the market at the cum-rights price.

• The future prospects of the company and the proposed utilization of the funds.

• The medium term expectation of the company's market performance considering that there would be a drop in the market price ex-rights and that it would take some time for the price to go back to the present levels or even more.

• The expansion in equity base and the consequent free float in the market. Since there would be an additional liquidity in the market, the market price could also be influenced by it in future. A well-performing company with less free float is likely to trade at higher levels. However, this is not sacrosanct since institutional investors normally prefer companies with higher free float. Companies with lesser free float may also suffer from lack of institutional buying support.

• The dividend and bonus track record of the company thus far and the prospects for realization of shareholder value.

5.4.2.4 Role of Investment Banker in Listed Companies [1]

Listed companies have several areas where investment bankers play significant role as advisors and issue managers. In some of these areas, apart from playing the statutory role of merchant bankers, they also take significant financial exposure in underwriting, providing safety nets, market making and in placement obligations to issuer companies. The functional areas for investment bankers in listed companies are thus listed subsequently: [1]
• Acting as advisers and arrangers in raising debt and equity finance through the capital market.
• Acting as advisers and arranges for private placement of debt and equity.
• Acting, as merchant bankers for transactions relating to secondary public offers, rights issues and composite issues.
• Advise companies on pricing and valuation for various types of offers.
• Advise companies on post-listing issues and offerings.
• Advise promoters and help in transactions relating to creeping acquisitions, dilution management, open offers and preferential allotments.
• Advise companies on delisting and act as merchant bankers for the delisting offers.
• Advise companies on buy banks and act as merchant bankers for such offers.
• Advise companies on market capitalization and related issues.
• Advise companies on issue of sweat equity, shares with differential rights, ESOPs and ESPS.
• Act as sponsor/merchant banker for private equity deals/bought out deals with subsequent offers for sale.

5.4.3 Public Offers of Debt Securities

Public offer route for debt instruments would mean making a public issue of pure debt instruments such as-bonds and non-convertible debentures (NCDs) and debt convertibles such as-partly convertible debentures (PCDs), fully convertible debentures (FCDs), convertible bonds and fully convertible zero coupon debt instruments. It may be interesting to note some of the primary considerations for a company to look at raising funds through public offering of debt instruments. They are:

• The issuer company requires debt finance for which accessing the capital market may be a better option than raising term loans from financial institutions and banks. This situation holds good in a buoyant primary debt
market wherein the costs of a public floatation taken together with the coupon rate payable on the debt instrument works out cheaper than the interest and other costs payable on term loans. Secondly, the syndication process for a term loan may itself be a longer process than accessing the capital market if the chances of the public float meeting with an encouraging response are bright.

- Accessing the public issue market is a better option than looking towards private placement of debt securities. Again, this condition would hold good only if the company finds that access to the retail debt market is a better option to raise large amount of funds rather than accessing primarily QIB investors in the private placement market. In the nineties, whenever huge amount of debt funds had to be raised from the primary market, issuers preferred the public issue market to the private placement route. However, over past 8-9 years, it is the private placement market that has met most of the debt financing requirements from the capital market. Each of these routes has its own advantages. While the public offer route provides greater dispersal and liquidity for the instrument, its secondary market volumes may not be high if there is no significant retail trade. On the other hand, debt securities that are issued privately but listed subsequently are traded mostly in the wholesale debt segment of the market driven by institutional demand.

- Sometimes, accessing the public issue market with a pure debt instrument or a convertible is triggered off since the company cannot afford to expand its equity base immediately with a public offering of pure equity. This happens in large capital-intensive projects wherein the gestation time for the project to yield good cash flow to equity is significantly long. Equity issues cannot be marketed in such cases with a promise to yield good returns in the distant future. Therefore, a debt convertible would be ideal in such situations by providing the investor with a coupon rate during the gestation period with the comfort of looking at the upside when the project begins to yield cash flow to equity. As far as the issuer company is concerned, its equity capital is explained in stages so that the earnings per share are not unduly depressed in
the initial phase. Secondly, during the initial years, if the instrument that has to be traded in the secondary market is pure equity, it would trade at low prices thereby jeopardising the company's market capitalization. On the other hand, during such phase, if the company floats a debt instrument with a reasonable coupon rate, it may find some trading volumes. In the past several major projects such as Reliance Petroleum, Essar Oil, MRPL and others had relied on the debt convertible route to raise funds from the public issue market.

5.4.3.1 Key Aspect for Merchant Bankers in Debt Issues

5.4.3.1.1 Structuring the Offer

One of the key areas for a merchant banker is to assess the credit-worthiness of the issuer company in the context of its existing long-term debt obligations and the assets that have been offered as security for the same. There are two important considerations in raising debt-(a) the future expected cash flow generation that would need to service the future debt obligations and (b) the future financial cost that has to be met out of the future pre-debt servicing profits. If the financial costs were steep, the profits would take on the burden. On the contrary if the cash flows were not robust enough, the principal repayments would come under pressure. It is also imperative to create a DRR to the extent stipulated under the DIP guidelines. Keeping these factors in mind and the overall financial health of the company, the end use of the proposed debt issue and the security to be created to backup the debentures, the merchant banker comes up with the structure of the proposed debt issue. The debt-equity ratio before and after the proposed offer, the debt service coverage ratio, the asset cover and interest cover play an important role in determination of the amount of debt that can be raised, the coupon rate, the yield to the investor, the accounting costs for the issuer company, tax breaks on the financial costs, redemption terms and other important parameters.
5.4.3.1.2 Structuring the Instrument

While examining the instrument that has to be offered, the merchant banker keeps in mind the probable rating that the instrument may manage to get. If it is evident that the instrument would not get a good rating, suitable credit enhancements have to be built in so that the structure manages to get a rating better than that of the stand-alone instrument. The rating also determines the coupon rate and the yield that has to be built into the instrument. Apart from the return to the investors, other features such as the marketability of the instrument, its unit value, minimum lot, tax benefits that it can be entitled to etc., also need to be examined. If required, sweeteners such as a convention option, step up rates, call option etc need to be provided so that the offer becomes attractive. Suitable exit options to the issuer company need to be factored in as well.

5.4.3.1.3 Marketing Plan

The marketing of a debt instrument through a public offer is a challenge to the merchant banker in a good market situation where investors show an unsuitable appetite for equity. In such a situation, generating retail interest for a debt offering is difficult. On the contrary, if the market conditions are not very bright, it would be even more difficult to elicit response for a public offer from the retail investors. Keeping these various factors in mind, the target market has to be assessed and the issue positioned accordingly. If QIBs are the target, pre-marketing would be required through firm allotments and reservations. Similarly, if retail interest seems to be in doubt, suitable underwriting arrangements need to be tied up. The structure of the instrument should be based on the target investors and the marketing efforts need to be organized to access the target market through road shows and other means.
5.4.4 Overseas Capital Market Issues

The international capital market is only a part of the larger international financial market that may broadly be defined as a financial market that transcends national geographical boundaries. In other words, in the international financial market, funds are raised from lenders or investors in a country by borrowers or issuers from another country or conduct transactions in currencies other than the domestic currencies of respective countries. Considering this character of the international financial market, it can be outside the regulatory purview of any single country. The international capital market consists of the global bond and equity markets and the bond market includes convertibles as well. Besides, there is also a huge derivative market with the underlying assets ranging from stocks to commodities, foreign currencies and other exotic varieties. The segments that are relevant to the present discussion are the bond and equity markets.

The importance of the global capital market can be accessed from the magnitude of finances raised in such a market. The basic function of the capital market is to perform the function of capital intermediation from investors to issuers of financial securities. The American and European capital markets have preformed this function for several decades in the previous century. The need for raising global finance from external capital market arises due to the imbalance in global capital flows over a period of time due to which, the excesses in certain economies need to be diverted to the deficit and more needy economies. These imbalances are reflected in the current account balances of each country in its trade with its global trading partners. If cross border global capital flows do not happen, the trade imbalances will deepen and bring global trade to a standstill. Post Second World War, given the dependence of the world on oil from OPEC countries, these countries built up huge surpluses. Given the consumption economy that the USA had been, it’s trading partners such as Japan and Germany built up vast current account surpluses. By the mid-eighties, investment opportunities in the developed economies were becoming lesser requiring the investors to look elsewhere for growing their money. The huge
infrastructural and development projects undertaken in the developing economies and the opening up of their economies to global investors provided the answer to this. The economies of the 'Asian Tigers' provided a huge growth opportunity till the south-east Asian crisis in 1997 came in between and reversed the fortunes. The emerging markets such as China, Latin America and India are the other markets that attracted global capital flows, though the India's share therein had not been as significant as that of China.

It is important to appreciate the necessity of free capital flows across economies of respective countries for the development of an international capital market. Most developed economies such as the USA, the UK, Germany and Japan had removed restrictions on capital flows. The eighties and nineties saw a greater integration and cross-broader floats in the international capital market. Despite the growth and sophistication in this market, it is far from being a perfect market. Market inefficiencies give rise to arbitrage opportunities for global investors.

Historically, beginning with the fifties, a truly international financial market developed in Europe, mainly centred in London. What led to the establishment of the international financial market in a big way was the creation of the 'euro' market in the fifties and sixties. The euro market is a market in which financial instruments—both short and long term that are denominated in a variety of currencies other than the domestic currency of the host country where they are transacted. Gradually, the financial markets of other developed countries such as the USA, Canada, Switzerland, France, Japan and Australia opened up to offshore investors through the euro market.

5.4.4.1 Overview of Process Flow for an International Offering

The most important part of the process of an overseas flotation of securities is to put in place the issue team. The investment banker is the most important entity in the issue team. Globally, there are several varieties of investment banks ranging from
full service international firms to local specialised firms. While selecting the
investment bank careful assessment has to be made about the size and status of the
issuer company and the relative importance of its mandate to the proposed
investment bank. The main criterion would be the distribution capability of the
investment banking team. In the case of private placement of euro bonds and 144A
securities, such distribution strength has to be mainly with institutional investors
while in public offers, it has to extend to retail investors as well. Since the investment
banker and the other syndicate members perform the role of underwriters, their
financial standing and past track record needs to be assessed as well. For non-US
companies, the investment banking team should have the additional experience of
listing foreign companies in the US markets. Indian companies generally appoint a
domestic investment banker to act as an advisor to the issue from India who would
advise and help in identification of the foreign investment bank that would lead
manage the issue.

The other important issue team members are the lawyers, the accountants, the
depository bank and the domestic custodian bank. Selecting each of these team
members would generally be done in consultation with the investment banker who
would be the lead manager for the issue. Domestic custodian bank is generally
selected on the basis of their presence in the custodial business and their working
relationship with the proposed global depository bank abroad. The law firm plays a
very vital role in being the issuer’s attorney to deal with the SEC, the NASDR, the
stock exchange and the local state securities authorities. Unlike in India where the
investment banker prepares and files the offer document with SEBI and interfaces on
behalf of the company, this function is performed for a global issue by the issuer’s
attorney. It would be advisable to hire a full service law firm that have capabilities in
not just public issue regulations but in attendant matters such as intellectual
property protection, labour and environmental law, industry and corporate law,
state and local regulations, tax matters etc. The accounting firm for a US public offer
has to be member of the American Institute of Certified Public Accountants (AICPA)
and additionally be a part of the AICPA’s SEC Practice Section. One of the important
documents furnished by the accountants apart from re-statement of accounts as per the relevant GAAP would be to furnish 'Comfort Letter' on the unaudited financial data appearing in the prospectus and its compliance with the relevant GAAP. The depository is usually a large banking corporation or a trust company. The Bank of New York is the leading depository bank in USA managing substantially more depository receipt program that any other depository bank. [6]

The other important steps in floating of an overseas capital market offered by an Indian company are listed subsequently: [6]

1. The first step would be to get the proposal for an overseas issue approved by the board of directors and seek necessary approval from the shareholders in general meeting under the relevant provisions of the Companies Act. For the issue of euro bonds and FCCBs, the provisions are similar to the issue of debentures.

2. The next step is to seek regulatory clearances in India if required. For the issue of bonds and FCCBs, necessary approval is required based on the applicable policy for ECBs in force at that time. For the issue of ADRs/GDRs, approval would be required only if they do not fall under automatic route. The approval from the RBI/GOI would be subject to conditions that may be prescribed in the approval which need to be complied with, for proceeding with the issue.

3. Other approval that would be required are as follows:
   a. The stock exchanges would have to be informed of the euro issue/US public issue before the board meeting, after the board meeting and on completion of the issue so that the fresh issue of underlying shares can be made to the domestic custodian.
   b. A copy of the euro issue prospectus should be filed with SEBI for the purpose of record.
   c. No RBI approval would be required for issue of shares and receipt of remittances from abroad on the ADRs/GDRs if these are covered
under the automatic route under FEMA. Otherwise, suitable approvals need to be taken for the same.

d. Approval from the DCA would be required for FCCBs under section 81(3) (b) of the Companies Act and for issue of shares to the domestic custodian without the issue of a prospectus in India in terms of section 56.

4. The next step would be to appoint the lead managers for the offer abroad and advisors in India. In parallel, the other issue team members such as co-lead managers or underwriters, issuer’s attorney law firm, independent auditors and depository bank need to be appointed. The issuer company and the lead manager have to sign a letter of intent stating the issue parameters, fee structure and other details as required.

5. The preparation of the registration statement has to be commenced at the earliest. As stated, the law firm has to be involved completely on the drafting of the narrative with vital information being provided by the company and the lead managers. The company’s business details, the MDA, the offer structure and other important sections need to be drafted as per the requirement of the SEC on one hand and from the marketability of the issue on the other. It may be appreciated that the prospectus is also the only marketing literature for the issue.

6. While the attorneys are busy with the preparation of the prospectus, the investment banker and the accountants conduct the process of due diligence for the issue. The investment banker will examine the company’s management, nature of business and operations, financial position, past performance, competitive strengths and the stated business plan for the future. Incidental issues such as supply chain dynamics, customer relationships, labour relations etc. would also be examined since they have a bearing on the performance of the company. The accountants will examine financial information and all material supporting documents such as contracts, invoices, legal agreements, vouchers and other evidence in
assessing the fairness of the accounting statements. Accounting policies and adherence to the relevant GAAP is examined in great details.

7. After the filing of the registration statement with the SEC in the case of a US public offering, it would be available for circulation among potential investors. The syndicate members are then assembled for a closed-door meeting to assess their interest and the extent of allocations that need to be made. This meeting will establish the marketability of the issue as well.

8. The road shows are commenced with the help of the investment banking team and a series of meetings are held with potential investors and analysts in all key financial centres where the issue is being floated or where the potential investors are located. The road show usually consists of formal presentations and question answer sessions, followed by one-to-one interactive meetings set up by the investment bankers and their affiliates.

9. The prospectus has to be then revised according to the observations made by the SEC and the NASDR. Upon the completion of this process, the SEC would state that the registration statement can be made effective from a particular date. The preliminary prospectus would then be circulated at least two days before such effective date and thereafter; the final prospectus goes into print.

10. Unlike in India where the public offer is priced at its cut-off before filing with the ROC, in the US the offer is priced a day before the effective date upon the recommendations of the investment banker. The pricing is a function of the response to the road shows, the timing of the issue, the economic and market conditions and the company's selling points. The law firm of the issuer files the final registration statement with the SEC by including the offer price. The accounting firm delivers the final comfort letter. The investment banker and the syndicate of underwriters sign the underwriting contracts.

11. On the opening day, the trading of the company's securities begins. The prospective investors are given a fixed time usually, five to seven days for responding to the offer. Based on the responses received, the subscriptions lists are drawn up and the over-subscription is determined. The allocations are made on a proportionate basis. The first closing happens around the fifth
day from the opening date and the second closing by the eight day. Based on the subscriptions received, the accounting firm delivers the 'bring-down' comfort letter to re-affirm what is stated in the comfort letter issued earlier. The lead manager transfers the amounts received from subscriptions to the issuer company after deducting underwriting and selling commissions. The law firm has to update the closing documents.

5.4.5 Exist Offers

Exist offer is a new concept in the Indian context. Essentially it refers to a sale option for a shareholder of shares in a company otherwise than through the secondary market. Till recently, Indian companies were not allowed to buyback equity shares from their shareholders. So the only exit option that was open for the common investor was to sell through the secondary market. With the recent amendments to the Companies Act, companies are allowed to buyback their shares subject to certain restrictions. Therefore, buyback has become an exist route that companies can provide to their shareholders as an additional option. Apart from it, when companies wish to voluntarily exit the stock market and go private or they are directed by the stock exchanges to do so, the public shareholders are to be provided an exit option. Therefore, the company has to make a de-listing offer to the public. Thirdly, when an acquire makes a substantial acquisition in a company, a compulsory open offer has to be made to the public within the terms of the Takeover Code of SEBI. This constitutes a third exit option to investors. All these offers are in the nature of reverse offers or exit offers since the shareholders are asked to surrender their shares for consideration.

While buyback as an exit offer has become a reality through amendments in the Companies Act, the exit offer arising due to a substantial acquisition, which was hitherto a part of the listing agreement, has been given the force of law with the promulgation of the Takeover Code. The de-listing offer has been introduced recently to curb companies from using the buyback as a route for de-listing. In exit
offers, the merchant Banker plays a very significant role not only in pricing issues but in ensuring compliance with law and in advising the company at every stage as well.

5.4.5.1 Strategic Issues in Exit Offers

Exit offers involve complex regulatory mechanisms and therefore need to be carefully planned. Promoters, acquires and company managements would do well to plan their strategy based on the requirements of the situation keeping in mind the regulatory provisions at each stage. Listed below are some strategic considerations in exit offers.[4]

1. Under the current regulatory framework, the mechanism of buy-back of shares cannot be used to its full extent in strategic financial management. However, there is room for some flexibility in using it effectively in capital structuring decisions. Equity share buy-back is allowed up to 25% to the equity paid-up capital in a given financial year and there can be a buy-back offer in every financial year as per the provisions of Section 77 A. Similarly, the company can make an issue of similar shares that have been bought back after a period of six months from the date of the earlier buy-back. These two provisions can be used in tandem to buy-back shares when the markets are depressed and to re-issue capital when the markets look up. However, care has to be exercised to ensure that the proceeds of an earlier issue are not utilized in a subsequent buy-back as such practice is prohibited under the law.

2. The buy-back mechanism allows for a company to purchase its shares from the open market within a specified period. In a depressed market, this is a cost-effective tool to consolidate promoter holdings rather than an open offer by the promoters. An open offer is based on fixed pricing with reference to the benchmark market price as per the stipulated guideline, while an open market buy-back can be at different market prices. Secondly, promoter open
offers would require fund mobilization by the promoters while in a buy-back; the company's resources could be utilized.

3. Open offers are to be used only when a de-listing or a strategic acquisition is on the cards since the law prohibits de-listing through a buy-back route. For all other strategic financial decisions involving equity capital reduction through return of shareholder capital, buy-back is a very positive and effective tool.

4. Buy-backs can be used to a limited extent to offset dilution or expansion of equity base consequent upon bonus issues, conversion of convertibles, stock splits etc. It can also be used effectively to curb the phenomenon of liquidity overhang in companies that have a significantly large free float.

5. De-listing can be used strategically when the market is depressed and there is no fund raising contemplated from the market in the medium term. However, the difference between de-listing and a buy-back offer is that in the former case, the promoters have a pool in funds from their resources to buy out the public shareholding. In such situations, it would be better to offer a stake to a financial investor such as a private equity fund to buy out the public stake. Once the company is de-listed, there would be future opportunities to list it again at higher market capitalization by timing the re-entry appropriately. The guidelines allow for re-listing after two years. The re-listing could be through an offer for sale by the private equity investors so that an exit route is created for such an investor as well. Companies can use this strategy in a limited way to beat the negative effects of depressed markets on their fund raising capabilities.

6. The de-listing guidelines can be used in two situations-(a) wherein a de-listing is contemplated and (b) when due to an open offer under the Takeover Code, the public shareholding falls below the statutory minimum. In both these cases, the reserve book-building route has to be adopted. Therefore a situation could arise in a takeover open offer when there has to be an open offer initially for 20% and a residual de-listing offer for the balance. Since the
second offer would be through reverse book building, it could be at a higher price than the open offer.

7. The acquirer in an open offer has to be clear about the percentage of acquisition being aimed at. If there is a strategic minimum quantity required which would be in excess of the minimum 20% stipulated under the offer, it would be worthwhile to make the offer for the percentage required. For e.g. if the acquirer requires a strategic minimum 20%. In order to ensure success of the offer, it may be necessary to peg the offer price at higher than the statutory minimum price. An alternative to this would be to make a conditional offer with a 50% cash escrow. But this may not serve the purpose since the acquirer has to acquire 20% anyway if the escrow is not to be forfeited.

8. Those acquirers, who do not wish to acquire 20% but are making the open offer to meet the statutory requirements, may deposit 50% of the consideration in cash in escrow so that the right to accept less than 20% is retained. The offer should also be made at the statutory price. This strategy may work if the offer is under-subscribed. However, this strategy could prove to be an expensive proposition if the offer has been received well by the shareholders. In such a case there is a risk of the deposit being forfeited for non-compliance.

9. Acquisitions under the Takeover Code are designed for acquirers rich in cash since there is not enough time available from the time the open offer is triggered off to the date of making the public announcement. In addition, escrow requirements make it stringent upon the acquirer to have adequate resources at hand. Considering that most takeover attempts start with open market purchase by the acquirer, a strategy has to be put in place for the ultimate stake aimed at including the open offer and the financing thereof.
5.4.6 Private Placement of Equity

Most companies, both in the listed and unlisted categories, make issues of equity shares to different shareholders without making a public offer. Such issues can be clubbed under the term ‘private issue of equity’. The term ‘private issue of equity’ has to be interpreted in terms of issue of equity shares in the non-public route either through a private offering or by other means. The various issues of equity that are possible in the non-public offering route are depicted in Figure 5.2.

Figure 5.2: Overview of Private Placements of Equity


5.4.6.1 Preferential Allotment and Private Placement

Preferential allotments are those that are made to selected investors or existing shareholders on preferential basis to the exclusion of everyone else. In a company, if the promoters want to increase their stake by subscribing to a fresh issue of equity shares by the company, the company makes a preferential allotment of such shares exclusively to the promoters without involving the other shareholders. Similarly, preferential allotment is required to be made whenever there is an issue of shares on private placement basis so that selected investors have to be issued shares to the exclusion of other existing shareholders or the general public. The term ‘preferential
allotment' and 'private placement' are sometimes used interchangeable though they have a subtle distinction. The difference between a private placement and a preferential allotment is that in the case of the former, the investors may not be known at the time of the issue while in the case of the latter, the investors would be known beforehand at the time of seeking necessary approvals from shareholders.

Preferential allotments are generally made to promoters, persons belonging to the promoter group, collaborators, joint venture partners and strategic investors. Private placements on the other hand, are made to institutional and non-institutional investors.

5.4.6.2 Bonus Issues

Bonus issues of equity shares are made by companies as a means of rewarding shareholders and creating a means for liquidation of value locked up in the reserves. As a company performs well and makes profits, the reserves of the company swell and despite the distribution of cash dividends from time to time, there could still be considerable reserves that are available as distributable surpluses. However, the company may not wish to distribute the whole of such reserves as dividends since that option has the potential to deplete the company of cash that it may require in the immediate future. At the same time, looking at it from a shareholder’s perspective, it may not serve any purpose to keep the shareholder value locked up in the business of the company. A bonus issue strikes the right balance in such cases. It rewards the shareholder through issue of additional shares by the capitalization of reserves. The accumulated reserves are then converted into share capital without the receipt of any consideration by the company. These additional shares are listed and rank pari passu with the existing shares of the company. The shareholder may then liquidate these shares in the market in order to unlock the value. However, it has to be realized that the share price of a company often drops in the short-term after a bonus issue to adjust for the excess liquidity in the market. Therefore, a shareholder may have to wait for a suitable opportunity to realize a good price. Nevertheless, the
fact remains that a bonus issue creates an opportunity to encash the built-up value in a company.

Before making a bonus issue of shares, the effect thereof on the share capital of the company should also be considered carefully. Since a bonus shares increase the issued capital, it depresses the EPS. In addition, there could also be a short-term selling pressure as some shareholders try to liquidate the bonus shares since they were issued to them free of cost. These developments could also slow down the fund raising by the company. Though the company’s net worth is not impacted, due to the changes in market capitalization, fund raising through the equity route could be affected in the short-term. By capitalizing free reserves, the company actually reduces its distributable surplus, which is available to pay dividends. This could even impact the future dividend payouts, as the company may not be in a position to dip into its reserves for the payment of dividends. However, a bonus issue is a tremendous tool for rewarding shareholders both psychologically and in actual terms without any cash outflow for the company. As such it is very popular tool for managements. Several Indian companies habitually reward shareholders through this route.

Bonus issues can be made out of revenue reserves of capital reserves as long as they are unencumbered and are received in cash. Therefore capital reserves not earmarked for any specific purpose such as capital profit on sale of an asset, share premium account etc are available for being capitalized as bonus shares. However, reserves whether revenue or capital, created out of book entries and not received in cash are not available for issue of bonus shares. The SEBI DIP guidelines are very specific on this issue stating that bonus issues shall be made only out of free reserves built up out of genuine profits or share premium collected in cash only. Revaluation reserves created by revaluing fixed assets are not allowed to be capitalized. Similarly, for unlisted companies, the Guidance Note issued by the ICAI states that revaluation reserves cannot be used for issue of bonus shares and in such cases, the auditors have to qualify their reports.
Bonus issues can be made both by listed and unlisted companies. Unlisted companies are governed by the provisions of the Companies Act and the articles of association, while listed companies have to follow section XV of the DIP guidelines as well.

5.4.6.3 Sweat Equity and ESOPs/ESPS

Sweat equity is concept of recent origin in the Indian context mainly useful only for knowledge-based companies. Sweat equity has been given statutory recognition under the Indian law with the Companies Act inserting section 79A. Sweat Equity shares are defined in Explanation II to sub-section (1) of section 79A of the Companies Act as 'equity share issued by the company to employees or directors at a discount or for consideration other than cash for providing know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called'.

Employee incentive schemes can be by way of stock options, stock appreciation rights, or stock purchase schemes or any other such measures. These became extremely popular in the wake of the boom in knowledge intensive businesses and their valuations. Section 2(15A) of the Companies Act defines Employees Stock Option as 'the option given to the whole-time directors, officers or employees of a company, which gives such directors, officers or employees the benefit or right to purchase or subscribe at a future date, the securities offered by the company at a pre-determined price'.

The tax treatment for sweat equity shares and stock options are the same—the difference between the exercised price and the final sale price in the sale/transfer of such shares would be taxable as long term or short term capital gain depending upon the period of holding. The company cannot treat the discount on issue of such shares as business expenditure as per decided cases.
Reliance Industries Ltd. adopted a Stock Appreciation Rights Plan. Under this plan, the employee does not incur any cash outflow to buy the shares. Instead, the employee will be paid the price appreciation that happens between the date of granting of the option and the date of exercise thereof. Zee Telefilms Ltd. Implemented an ESOP wherein shares were issued at Rs. 212 when the ruling market price was around Rs. 4225. Several Indian companies in software, pharmaceuticals, banking and financial services have issued ESOPs. [6]

Apart from the above, there could be alternatives such as incentive plans, which are long term in nature, spin-off of business activities into companies in future to accommodate each core member at the helm, business outsourcing models etc. that can provide permanence in the structure. The bottom line is to establish the availability of the core team expertise to the business over a fair period of time.

5.4.6.4 Venture Capital Finance

The only category of investors that is exclusive to unlisted and to be listed companies is that of venture capital investors. Under the present investment guidelines for venture capital, even later stage financing as private equity can also be made by venture capital investors as long as the company is unlisted or is to be listed.

The emergence of the venture capital industry in India in a significant way has only been of recent origin. The Venture Capital Guidelines notified on 25th November, 1988 went on to define the scope of venture capital to mainly include assistance provided to enterprises where the risk element is comparatively high and/or the entrepreneurs being relatively new. The investment size was restricted to Rs. 10 crore and the technology was relatively new, untried or very closely held or being taken from pilot to commercial scale or which incorporates some significant improvement over the existing ones in India. [1]
Pursuant to the guidelines, several institutional Venture Capital Fund (VCFs) were promoted to provide VC assistance as per the eligibility norms. However, the main hindrance was the definition given to the scope of VC assistance so as to mean risky and start up technologies. VC was perceived as a high-risk high-return game. Therefore, the unit that were supported were mainly the technocrat-promoted variety wherein, but for the assimilation of technology; the promoters were first generation entrepreneurs with a lack of business background and in particular, industrial experience.

The traditional concept of VC being risk capital was broad-banded by SEBI in 1996 notifying a new set of regulations for the VC industry called the SEBI Regulations, 1996. The concept of private equity was thus born for investment in later stage and turn around companies. Though the concept of private equity is essentially meant for investment in later stage companies, the VC funds operating in India have caught on to it in a significant way only after dotcom bust in 2001. [3]

As far as the domestic VCFs are concerned, there is no regulation on the type of investee companies in which VCFs can make investments except that they shall be domestic companies and unlisted at the time of investment by a VCF. Investment may also be made through the Prospectus of a to-be-listed VCU. VCUs may be engaged in any type of manufacture or service activity excepting those mentioned in the negative list. Therefore, hypothetically, VCFs may invest in sick and turnaround companies too, though there has not been any such interest from VCFs so far. There are further restrictions that 75% of the investible funds of a VCF shall be deployed in equity or equity linked instruments. Out of the balance 25%, a VCF may invest in pure debt instruments only funding in a VCU wherein it already has equity exposure. [1]
5.4.6.5 Current Investment Banking Services for Raising Private Equity

In the area of private equity financing, the role is more transaction oriented than in venture capital fund raising. This is because, the business model of the company is more established, the organisation is fully in place and the cash flow model is proven. Therefore, the value addition of the investment banker in such deals is in valuation and transaction advisory. However, there are certain caveats that the investment banker has to be fully aware of while raising private equity for listed companies. These primarily relate to the disclosure of information to potential investors. Some of which can be classified as price sensitive information. While SEBI guidelines on disclosure of price sensitive information of a listed company are quite stringent, these are more in the context of insider trading or fraudulent manipulation of market price. However, in a private equity deal, the disclosure is for the purpose of enabling the potential investor to take an informed investment decision. In this context, the whole process has to be handled with extreme confidentiality and through suitable documentation by way of non-disclosure agreements so that none of the connected parties are put to hardship at a later date. However, there being no specific SEBI guidelines on private equity investment in listed companies, information disclosure in connection with it is largely a grey area at this point of time. The investment banker has to structure the offer literature including the information memorandum keeping this issue in mind. Secondly, the offer literature has to captures the true value proposition of the company and provides an investor friendly offer structure. While the value capture helps the company to get an appropriate valuation for the deal, the offer structure helps in striking the right chord with the investors.

Usually, the mandate letter for an investment banker spells out the scope of the ‘engagement’ in detail so that there are no exclusions or lack of understanding. The ‘engagement’ in connection with a private equity transaction can be summarized in the words of an investment banker as:
• Identify and initiate contact with prospective investors, including arranging road shows, and following up as necessary.
• Represent or accompany the company in meetings, presentations and ensuring negotiations with prospective Investors.
• Review the outcome of such meetings with the company, and recommend to the company further action as may be required.
• Assist the company in coordinating information dissemination and due diligence program.
• Review and advice on proposals/offers from prospective investors.
• Oversee the orderly and timely execution of each financial transaction, in cooperation and coordination with other professional parties appointed by the company and/or the investors, and the various regulatory authorities including the Securities and Exchange Board of India (SEBI) and the Reserve Bank of India (RBI).
• Provide such other services deemed necessary to ensure a successful outcome to this engagement.

5.4.6.6 Current Investment Banking Services for Raising Venture Capital

The investment banker plays a key advisory role in formulating the business of a start-up company and also helps it to raise its finances. The key area wherein the investment banker plays an important role in transaction services, in the context to a start-up is essentially in fund raising and allied functions. Broadly, the following services can be delivered by the investment banker to a start-up company:

• Strategy and business advisory services in formulating the business model for the company’s stated business objective.
• Perform a study of the industry landscape and competitor analysis, product pricing strategy and SWOT analysis.
• Conduct a preliminary due diligence and advice the company on the necessary steps to be taken to make the business model credit worthy and
investors friendly. These aspects relate to the business and financial structuring of the company.

- Formulate the investment offering to be made by the company, which comprises of valuation and deal structuring.
- Prepare the business plan and the Information Memorandum or the Project Report as the case may be for the company's fund raising including the detailed financial modelling and other promotional materials for the purposes of dissemination to prospective debt financiers and investors.
- Act as the arranger for the company's debt or equity financing as per the financial plan that includes representation and negotiations.
- Raise financing for the company in the most efficient way possible.

In the course of performing his functions, the investment banker has to also work closely with other professionals both inside and outside the company such as the CEO, CTO, CFO, the Company Secretary, the Auditor, the Legal Advisor and the Financial Advisor.

Considering the fact that investment banks provide transaction-oriented services, it is found that most of the top line investment banks do not prefer to work with start-ups in pure advisory role unless the company's business plan is large enough to their liking. This is because most of them would want to have a minimum deal size that would justify the time spent on the assignment and the fee charged to the client. It also does not make sense for companies with smaller deal sizes to appoint larger investment banks, as their fee would make the exercise un-remunerative. However, there are several mid-sized and smaller investment banks, financial companies and consultancy firms that handle proposals relating to start-up companies. Since most start-up companies raise funds from private and institutional sources, no public offering of debt or equity is involved. This makes it convenient for arranges without a merchant banking licence from the SEBI to handle such proposals for fund raising. Some of the larger consulting firms also deliver advisory and fund raising services to start-up companies.
5.5 Corporate Advisory Services

5.5.1 Business Advisory Services

Business advisory services relate to advising a company on its present and future businesses from a strategic and financial perspective. Such services can encompass the areas as given below:

- *Entry Strategy Plans:* Entry strategy advice is required when a company plans to start a new business initiative either in a new area of business or in a new market whether geographically or otherwise. The entry strategy could be in terms of a corporate structure or a product and pricing strategy, target market segment, strategic alliance or in other such definitions. For e.g. a multi-national company wanting to set up shop in India could require an entry strategy to be formulated for the roll out of its business in India. The entry strategy recommendation in terms of corporate structure for such a company can be a decision between establishing a wholly owned subsidiary in India vis-a-vis a joint venture with an Indian partner. Generally formulation of entry strategy plans requires looking at the business and financial aspects, regulatory and tax aspects of an envisaged business keeping in mind the existing corporate and business structure. One other major consideration in the formulation of an entry strategy is the visa policy of the relevant state and the residential status of the concerned individuals who would be operating in the other country.

- *Project Feasibility Plans:* These relate to setting up of new businesses wherein the viability of the proposed business from a business, technology and financial perspective needs to be examined. Unless the commercial feasibility and financial viability is well established beyond doubt, projects normally do not go for fund raising. Therefore, a feasibility study is often being undertaken before proceeding along with other steps in implementing a project. Investment banks are ideally placed to conduct such feasibility
studies from a business and financial perspective since they have in-depth information on each industry space. In some cases wherein a market survey needs to be done or a specialised technology needs to be assessed, the investment bank teams up with the relevant specialists concerned.

- **Corporate Plans:** Companies require formulating medium to long-term corporate plans that define their expansion and business strategy. While many established companies have in-house corporate planning departments, they also believe in getting the same formulated or vetted by an external agency such as an investment bank or a consulting firm. Formulation of corporate plans requires in-depth examination of the industry and business of the client, identification of growth drivers, market positioning, product policies, diversification strategies, corporate and group structure and other parameters. At the same time, the strategic financial aspects relating to fund requirement for future growth and financing there-of, the long-term holding structures and shareholding pattern, scope for further fund raising from the capital market, shareholder value creation and investor perspective, spinning off subsidiaries, entering into new business alliances, cross-border investments or acquisitions, etc need to be explored and incorporated into such corporate plans. Investment banks are competent to handle such assignments due to the fact that they are well versed in strategic financial issues.

- **Business Alliances:** Business alliances relate to joint ventures, collaborations and other such strategic relationships between two corporate entities that are brought about due to business compulsions or for harnessing synergies and complementary strengths. Business alliances form an important service area for investment banks as they involve transaction support in terms of identification of partners with complementary strengths or synergies. Such deal also involves due diligence and valuation aspects apart from negotiation and deal making. Usually, if an investment bank is representing a client, it does not perform the support services in due diligence or valuation as that would amount to a conflict of interests. In such deals, therefore, more than
one advisor will be involved to handle different aspects of the assignment. In addition, the legal due diligence and documentation or certification of financial statements, etc may also need to be outsourced from various professional firms.

- **Cross-Border Investments:** Cross-border investments are made by a corporate in one country across other countries. Strategic business investments could be made in foreign entities owned or controlled by the investing corporate in the parent country or in other foreign entities. Cross-border investments may also be made without creation of a separate legal entity in the foreign country. As far as India is concerned, foreign investments in India are governed by the FDI policy of the Government of India from time to time. Similarly, overseas investments by Indian companies are also governed by government policy. Investment banks may advice either the investing company or the investee company depending upon whom they represent in the transaction. In providing such advice, an in-depth examination of the financial and regulatory issues is necessary to arrive at the optimum size of the investment, valuation methodology, investment structure and taking necessary regulatory clearances.

As may be appreciated from the above, business advisory services relate to considerations involved in corporate structuring, joint ventures, collaborations and cross-border investments.

**5.5.2 Project Finance**

Project Finance is a specialized area in corporate finance that deals with the financing of an economic vehicle which can generate economic returns to its stakeholders. From a lender's perspective, project financing can be defined as the financing of an economic unit, based on an assessment of such unit's capacity to services the loan and interest thereon, out of the profitability and cash flow generated by the proposed project. The assets proposed to be created in the project
would be used to collateralise the loan. Peter K. Nevitt defines it as 'a financing of a particular economic unit in which a lender is satisfied to look initially to the cash flows and earnings of that economic unit as the source of funds from which a loan will be repaid and to the assets of the economic unit as collateral for the loan'.

5.5.2.1 Relevance of Project Finance

Project finance performs a significant role in the economic development of a country. When India attained independence in 1947, there was a serious requirement of industrial development to rebuild the nation. For this reason, various financial institutions such as IFCI, IDBI, ICICI, and state-level financial institutions such as the State Financial Corporations and State Industrial Development Corporations were established to administer project finance to proposed projects in various parts of the country. In the past 50 years, project financing has provided yeoman service to the industrialization of the country and in attaining economic development. In the next few decades, project finance will play a crucial role in creation of adequate infrastructure in the country.

The main source of project finance in India is financial institutions and commercial banks. For larger projects, foreign banks and multilateral institutions are sometimes involved. While the principal business of financial institutions has been project financing, commercial banks have been more into asset financing by way of terms loans and leasing.

5.5.3 Financial Restructuring Advisory

'Financial restructuring' as the term denotes is the art of restating the financial position of a company as reflected by its balance sheet as on a given date. In order to achieve such restatement, a complex financial and legal process is involved as it concerns several conflicting interests. Financial restructuring can be triggered off either from the asset side of the balance sheet or the liabilities' side. If the asset side
is to be restated, it involves revaluation of the assets, so as to arrive at their true values, and restate the asset side accordingly. Once the asset side is restated, the corresponding adjustment is made on the liabilities' side to arrive at the restated balance sheet. Such adjustment would depend upon whether there is a net increase or decrease in the value of the assets upon revaluation. If the net total on the asset side is an increase, it results in an increase in the 'reserves' so as to equate the liabilities' side and vice versa.

Financial restructuring is triggered off from the liabilities' side as well. This happens due to a change in the status of the outside liabilities of a company either due to negotiations or statutory provisions or any other reason. In contrast, a change in the values of the shareholders' funds is necessitated normally due to a change in the values of assets as discussed above. Therefore, financial restructuring encompasses restructuring of debt capital as well as equity capital.

5.5.3.1 Debt Restructuring

Restructuring of debts refers to that part of the reconstruction of a balance sheet insofar as it relates to the borrowing obligations of a company. Debt restructuring can form a component of the overall financial restructuring exercise undertaken by a company, which might include inter alia, reduction of capital or other forms of equity restructuring. But in several instances debt restructuring could be the only financial restructuring undertaken by a company. This could be so because equity restructuring is a more profound exercise and is not undertaken unless the circumstances warrant it. However, debt restructuring is a much more routine process and can be triggered off even as a financial management tool. One of the main functions of a finance manager is to optimize the cost of capital of the company. In order to do so, he needs to constantly look for increasing the efficiency of borrowing and reduction of financing costs. This would call for continuous review of the debt portfolio and recycling the same to maximise efficiency.
Debt restructuring in India has been an age-old practice triggered off partly by the high-cost funds and more importantly, due to industrial sickness. In the early days, prior to the passing of the Sick Industrial Companies Act 1985, debt restructuring was undertaken by the term lending institutions and banks in their capacity as secured creditors. The Industrial Reconstruction Bank of India was established primarily to rehabilitate sick units requiring relief and financial support through restructuring of their balance sheets without the intervention of courts. With the advent of the Board for Industrial and Financial Reconstruction, sick industrial units came under the purview of this board with the financial institutions and banks acting as the operating agencies. This mechanism still left out a large number of units which required debt restructuring as the definition of sickness under the Act was very narrow. Over the years, the RBI, the institutions and banks have evolved several mechanisms for debt restructuring of such units. Similarly, under the BIFR mechanism, operating agencies have evolved different methods of rehabilitating sick units through suitable debt restructuring.\textsuperscript{[8]}

5.5.3.1.1 Rational for Debt Restructuring

As stated above, debt restructuring can take several shapes and happen in different circumstances. Broadly, all these situations can be brought under the following three major heads:

- **Scenario I**: A healthy company would want to restructure its debt portfolio by substituting existing high-cost debt with fresh low-cost borrowings.
- **Scenario II**: A company without servicing capacity and liquidity problems would want to restructure its debt portfolio to reduce the cost of borrowing and improve working capital position.
- **Scenario III**: A company that is insolvent would need a wholesale restructuring of its debt portfolio to rehabilitate it and make it solvent.
5.5.3.2 Equity Restructuring

Equity restructuring refers to the process of alteration of the structure of the shareholders' funds. In other words, it is the re-organization of the share capital and/or the reserves appearing in the balance sheet of a company. Shareholders' funds include paid up equity share capital, preference capital, reserves and surplus and all other liabilities of a company that are not in the nature of debt obligations owned to outsiders. In other words, shareholders' capital includes all types of capital provided by the owners of the company and all accumulations in the balance sheet that belong to them. In this module, the term 'equity restructuring' has been used in the context of a restructuring of shareholders' funds.

Restructuring of shareholders' funds is often termed as 'equity restructuring' since more often than not, it involves inter alia, restructuring of the paid up equity capital appearing in the balance sheet. While alteration of reserves alone is not strictly considered as equity restructuring in the legal sense of the term, a restructuring of the equity share capital is a much more complex and legal mechanism. Notwithstanding this difference, alteration of reserves has to be done with due consideration to this distinction between 'general reserves' and 'specific reserves'. General reserves are available for utilization in a way that the shareholders feel appropriate and therefore, these can be appropriated with necessary resolutions passed in shareholder meetings. However, specific reserves need to be handled more carefully by examining the purpose for which they were created in the first place. These reserves can only be used in fulfilling the objects of their creation and if such objects were stipulated under law, appropriation to any other purpose would require statutory clearance. Examples of reserves with specified modes of utilization are 'Securities Premium', Capital Redemption Reserve', 'Debenture Redemption Reserves, etc.

Equity restructuring involving the equity or preference share capital of a company is a much more complex process which invariably involves a process of law.
Conceptually, restructuring of the share capital involves variation in shareholders' interests and is therefore, a closely regulated area. Regulators are particularly interested in ensuring that indiscriminate equity restructuring does not lead to undermining the confidence in the corporate system.

5.5.3.3 Current Investment Banking Services in Debt Restructuring [1]

Investment bankers, of late, have developed a service area in advising and representing companies in debt restructuring programmes. The various steps involved are as follows:

1. The first stage would be to formulate a viability plan for the company. For this purpose, the investment banker has to understand the business model, present financial position, existing borrowings and their carrying cost, future business opportunities and the resulting cash flow therefrom.

2. Once the company's viability and future operating plan have been formulated, the next step would be to float the 'Debt Restructuring Scheme (DRS)'. The DRS has to comply with statutory norms and applicable guidelines issued by the RBI. The investment banker has to use his expert knowledge and prior experience in formulating the scheme, so as to envisage workable terms of sacrifice from lenders and attractive terms of liability and cost reduction for his client.

3. The next step would be to present the DRS to lenders and represent the client in discussions and negotiations with the consortium of lenders of individual lenders as the case may be. This would require detailed presentations, site visits by lenders and establishing the future viability of the company's business beyond doubt, after taking into account the proposed debt restructuring. Of utmost importance is the justification for the proposed terms of the restructuring and the sacrifices if any, being sought from the lenders.

4. In most debt restructuring proposals involving either bankrupt or sick companies, suitable contribution are also expected from the borrowing
company to establish its commitment to the proposal and to re-capitalise the company to improve its net worth. The additional capital infusion requires financing either through sale of some assets by the company or from external sources, since the company would hardly be in a position to generate funds from internal accruals. The external sources could be additional promoter contribution, rights issue to existing shareholders, bringing in strategic or financial investors, or through a suitable merger or acquisition transaction with or without change in the existing management. In all such situations, the investment banker plays an additional role in providing transaction services, which becomes crucial for meeting the stipulated requirements.

5. After the proposed DRS in approved in principle, it is to be ratified by the approving authorities in each lender's organization. Thereafter, the borrower is issued confirmation of the terms and sanction for the scheme. The investment banker's role would then be to provide transaction services to generate the necessary funds, to meet the requirements stipulated for the borrower. The mandate generally extends till such time that the transactions are completed and the DRS goes through smoothly.

6. Debt restructuring services would involve a lot of compliance and legal work for which the investment banker works closely with other professionals such as the CFO, auditor, company secretary and legal advisor of the borrowing company.

5.5.3.4 Current Role of Investment Banker in Equity Restructuring

The investment banker plays an important role in the equity restructuring of a company, in the area of share buy-back. More often than not, companies that intend to restructure their equity capital are listed on the stock exchange and therefore, such restructuring may need to comply with the relevant provisions of the SEBI guidelines. However, the real need for an investment banker inequity restructuring is to play the role of a merchant banker for a proposed share buy-back if any, as part of the restructuring programme. Since SEBI guidelines stipulate that share buybacks
have to comply with SEBI guidelines and a merchant banker holding a valid licence should manage the offer, it becomes imperative for the company to appoint a merchant banker as manager to the offer. The major contribution that the merchant banker makes in such assignment, apart from managing the offer, is in advising the company on the proper method to be adopted for the buy-back accordingly. The pricing become critical because if the buy-back is under-priced, the offer may not be successful. On the other hand, if the buy-back is over-priced, it may erode shareholder value for those who remain with the company post-buyback. Pricing also has its bearing on the market capitalization of the company. Therefore, the role of the merchant banker becomes extremely important.

Apart from helping the company with the buy-back, the merchant banker has to offer expert advice in structuring the equity capital pre- and post-restructuring, according to the provisions of the Companies Act and other statutory provisions. However, all necessary accounting work, statutory approvals and representation before judicial authorities is handled by other appropriate professionals.

5.5.4 Mergers and Acquisitions Advisory

5.5.4.1 Overview of Corporate Re-organizations

Corporate re-organizations consisting of restructuring, mergers and amalgamations are by far, the most important business segment for investment bankers after management of public offers. Globally, in the traditional days of investment banking, this business segment, popularly known as M&A, contributed to a significant share of the bottom line of investment banks, sometimes becoming the largest revenue stream. USA and Europe have traditionally been the favourite hunting grounds for mergers and acquisitions and over the decades, they influenced the growth and transition of corporate America and transactional corporations. The M&A segment received a further boost with the popularity of junk bonds and leveraged buy-outs, or LBOs in the US market in the eighties. The biggest of them all
was the LBO of RJR Nabisco in 1998, valued at $24.6 billion. Between 1986 and 1989, LBOs had accounted for about a one-fifth market share in the total M&A industry. [1]

The M&A activity was further spurred on in the nineties by the increased global capital flows. It continued to grow and touched about $3.5 trillion dollars per annum by the start of the new millennium. During this time the LBO market went through a correction and by 1999, LBOs represented only 4% of the market. In addition, over the years, individual deal sizes have gone up considerably. Some of the biggest deals made towards the end of the nineties were all in excess of $50 billion such as MCI Worldcom-Sprint, Exxon-Mobil, Travelers Group-Citicrop and several others. The new millennium saw big ticket deals such as AOL-Time Warner and HP-Compaq. This pattern indicates that while the trend in the eighties was that of buying companies through cash deals financed considerably through leveraging, the trend in the past decade or so has been more towards predominantly stock deals. The first eleven months of 2003 produced deals worth $1,334 billion as compared to $1,271 billion in the whole of 2002. [1]

The Indian M&A scenario is much more modest both in terms of the size of the industry and the number of deals. Partly, this has been due to regulatory hurdles such as the MRTP Act that curbed companies from growing, both in terms of assets and in terms of control. The second major bottleneck was the lack of a structured mechanism for takeover in India. The M&A activity got a boost, post-liberalization, due to the consolidation wave sweeping Indian industry and due to the introduction of a structured code on takeovers. There were more than 400 open offers under the Takeover Code of SEBI in the five years after it was introduced in 1997. Cases of consolidation through mergers have been quite a few in recent years such as the HLL mergers, TOMCO, Godrej Group, AV Birla Group, Idea Cellular, India Cements-Raasi-Vishun, Gujarat Ambuja-ACC, Nicholas Piramal group, Lafarge, all the bank mergers, etc. [1]
5.5.4.1.1 Rational for Corporate Re-organization

Mergers, acquisitions and corporate restructuring are a part of business portfolio re-organization by companies that happen on a continuous basis to handle business dynamics. Restructuring is the process by which companies respond to changes in the operating environment and is often a tool for change management. The objectives of corporate restructuring could be many and based on the objective, the method of restructuring varies. Given below is an illustrative list of some corporate objectives that trigger corporate re-organization, and related examples in the Indian context.

- To create long term holding structures: The Tata Group conducted a group restructuring some years ago to build cohesiveness in group structure and corporate objectives.
- To grow at a rate faster than an organic growth rate: An acquisition strategy is often driven by the objective of attaining faster inorganic growth. The Nicholas Piramal group is an example.
- To enter a new market or grow beyond a saturated market: Sometimes mergers and acquisitions help in becoming an entry strategy. The acquisition of Tetley in UK by Tata Tea Ltd. is a good case in point.
- To capture forward and backward linkages in the value chain: Often group company mergers are triggered off to provide a complete value chain within the same company. Similarly, such mergers are also possible in companies with complementary strengths. The group company mergers in the Reliance group and the mergers in the Hindustan Lever group are examples.
- To attain control on a larger fund/manufacturing base: Mergers and acquisitions are also triggered off for larger market shares or economies of scale. At a time when the Indian industry is going through the consolidation phase in several sectors, these mergers and acquisitions are many. Examples are those made by the cement industry, the telecom mergers, bank mergers, pharma mergers, etc. The formation of Novartis, Galxo SKB, UBS Warburg,
ICICI Ltd-ICICI Bank, Times Bank and HDFC Bank merger, India Cements acquisition of Raasi Cements and Vishnu Cements, Hindalco’s acquisition of Indian Aluminium etc., are specific cases in point.

- **To attain or better utilise tax covers:** Harnessing tax efficiencies through mergers of profit-making and loss-making companies has been an age-old technique of tax planning which continues to thrive.

- **To facilitate distribution of assets and family settlements:** Restructuring of companies through splitting existing companies is necessitated due to family splits or settlements. Indian industry goes through such phases whenever there is a succession in a group. Some of these result in acrimonious battles such as those in the Chhabria group, the Modis, the Apollo Tyres Group, etc.

- **Achieve synergies of operations**

- **To exit non-core businesses:** In times of increased competition and business volatility, companies look for sustenance in areas of core competence. This could mean increased investments in such areas for which funds are raised through divestiture of non-core businesses. Examples are the sale of TOMCO, Times Bank, TISCO’s cement business, etc.

- **Bail-out mergers and acquisitions are common when a company is in trouble and seeks financial strength.** For e.g. Centurion Bank’s takeover by the Rana Talwar group, GTB’s mergers with OBC are cases in point.

- **Strategic divestitures:** These are instances where a company is nurtured with a strategic sale in mind. Many a time, venture backed companies are looked at as good exist vehicles for venture capitalists if they make good candidates for strategic sales at a later date. Sale of Customer Asset to ICICI, Spectra mind to Wipro, India World to Satyam Infoway is examples.

- **To facilitate the entry or exit of business partners:** Corporate reorganizations may be necessary when there is an entry or exit of a JV partner. Businesses may have to be hived off into separate entities to accommodate the partners in such ventures as distinct from the other businesses in the group.
5.5.4.1.2 Types of Corporate Re-organizations

As indicated above, corporate re-organizations take the form of (a) corporate restructuring of an existing company or a group of companies or (b) through the integration process of M&A. The entire spectrum of corporate re-organization is mapped in the Figure 5.3.

Figure 5.3: Types of Corporate Re-organization

[Diagram showing types of corporate re-organizations]


5.5.4.2 Introduction to Corporate Restructuring

The term ‘corporate restructuring’ denotes the entire process through which an existing company re-oriens itself, as a response to changing business environment and operational dynamics. Therefore, corporate restructuring encompasses several facets of change according to the circumstances and different methods are adopted for such change to achieve different objectives. Corporate restructuring can be internal to a company without a change in its legal entity or as an external process with the creation of one or more new entities or by the split-up of the existing balance. Internal restructuring consists of (a) operational restructuring, (b) financial restructuring and (c) divisionalization. Operational restructuring is either a technical...
exercise such as a business process re-engineering or a managerial initiative such as a change in the organizational structure. The other commonly executed internal restructuring is financial restructuring, which entails a change in the capital structure of a company. Divisionalization refers to setting up separate division within the same company for better operational control and accountability. Figure 5.4 illustrate the different types of corporate restructuring.

Figure 5.4: Types of Corporate Restructuring

<table>
<thead>
<tr>
<th>Internal Restructuring</th>
<th>External Restructuring</th>
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<tbody>
<tr>
<td>a) Financial Restructuring Debt or Equity</td>
<td>a) Subsidiarisation</td>
</tr>
<tr>
<td>b) Operational Restructuring</td>
<td>b) Hive off</td>
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<tr>
<td>c) Divisionalisation or setting up of SBUs</td>
<td>c) Deemerger</td>
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<td></td>
<td>Through transfer of assets</td>
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<td></td>
<td>a) Divestiture</td>
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<td>b) Spin-off</td>
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<tr>
<td></td>
<td>c) Equity Carve Out</td>
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5.5.4.3 Role of Investment Banker in Corporate Re-organization

As may be appreciated from discussion on corporate re-organization here, the importance of the role played by the investment banker cannot be over-emphasized. It has already been indicated that this area forms a key segment in their business portfolio. In all corporate re-organizations, the investment banker performs the pivotal role of transaction service, acting as a catalyst for the entire deal. In a corporate restructuring involving a split-up or a divestiture by a company or disinvestment by the promoters, the investment banker prepares the entire feasibility plan, deal structure, prepares the necessary deal specific literature, identifies the buyers of the sellers as the case may be, conducts the valuation and
due diligence and negotiations for arriving at the term sheet. The investment banker also works closely with other professionals such as accountants and legal advisors in order to look at the legal, accounting and tax issues involving such corporate reorganizations. Based on the deal structure arrived at, the scheme is prepared by the lawyers to be presented to the shareholders and the High Court under Sections 391-394 of the Companies Act. With the powers of the High Court now being shifted to the Tribunal, this function may also be performed by other professionals.

In transactions involving mergers and acquisitions, the task is even more onerous. In a merger, the key function of an investment banker is the search and identification of the other party to the deal. Thereafter, there are critical functions relating to preparation and circulation of information memoranda, deal structuring and negotiations apart from ancillary functions of valuation and due diligence that could be done by third party investment bankers. Since a merger involves statutory compliance and petitioning the Court, it involves teamwork with other professionals such as accountants, lawyers or company secretaries. It is worthwhile to note that it is only after the deal structure is firmed up that the scheme of the merger is drawn up to draft it in a legal language. Therefore, the deal structure is critical as it has financial and strategic implications for both parties. From this point of view, the investment banker's function has utmost significance.

The structure of the post-merger balance sheet is critical since it impacts the distributable reserves, the fund raising capability and book value of the share. This could have market repercussions as well. The investment banker has to have a clear view of these implications and advise the client suitably in arriving at the optimum strategy for the merger and post-merger balance sheet. Discussion with accounting professionals working on the balance sheet would help in this respect to come out with creative ideas. Similarly the tax implications also determine the rights strategy, especially in split-ups. As may be appreciated, a group restructuring could be quite a complicated assignment that could involve a combination of a split-up, merger and
an acquisition. The investment banker should work closely with accounting, legal
and tax experts in such cases to bring out a holistic solution.

In acquisitions and takeovers involving open offers, the investment banker plays the
dual role of an investment bank as well as a merchant bank. The merchant banking
role is in managing the public offer and ensuring compliance with the SEBI Takeover
Code. The Takeover Code places onerous responsibility on the merchant banker for
the purpose of the open offer in terms of the public announcement and disclosures
in the offer letters. The other critical functions are in valuation and deal advisory
based on the strategic and financial issues.

In transactions related to M&A, the investment banker has to represent a client either
from the buy side or the sell side. This would mean that in each such deal, there
would be least be two investment bankers representing either party to the
transaction. Usually, an acquisition leads to spin-off transactions, which provide
additional work for the investment banker such as raising finance for the takeover
through debt or equity offerings.

To sum up, Investment Banking offers the complete breadth and depth of high-
quality financial advisory services and capital market solutions to domestic and
multinational clients across sectors. It mainly includes Equity and Debt Capital
Market issuances, M&A Advisory, Private Equity Advisory, Restructuring and
Recapitalization services, and Infrastructure Advisory & Fund Mobilization.
Investment Banks have a deep understanding and strong domain knowledge of all
major industry sectors through a team of dedicated sector experts.

Key Strengths of a Typical Investment Bank:

- A solid reputation for unmatched advisory services and deal execution skills,
  with continued leadership on the league tables for both Equity offerings and
  M&A transactions.
- An in-depth understanding of the local market and intimate knowledge of industry verticals through dedicated sector experts
- Focused on maintaining the highest ethical standards with a approach to keep clients' interests first
- The ability to leverage the organization's intellectual capital and wide-ranging experience to customize innovative solutions for the clients
- Strong relationships with all the leading business houses in the country cultivated through several years of client servicing

To bring to a close, Chapter 5 has covered introduction to investment banks, investment banking and merchant banking distinguished, business portfolio of investment banks, about initial public offer, about right issue, about public offers of debt securities, about overseas capital market issues, about exit offers, about private placement of equity, about business advisory services, about project finance, about debt restructuring and about merger & acquisitions advisory. Now, let's move to the core part of this study, that is critical analysis of data and summarizing findings of primary research. Same is described in next Chapter.

5.6 Bibliography