ORIGIN AND GROWTH OF MERCHANT BANKING IN INDIA

Origin in General:

The term Merchant Bank (MB) has its origin in the merchanting activities of the 13th century. During this period, a few families owned and managed firms, which engaged in coastal trade and finance, started spreading throughout the European continent. The first such known firms were ‘Riccardi of Lucca Medici’ and ‘Fugger’.

Principally, these merchants were engaged in overseas trade. They used their own or chartered ships to transport manufactured goods from the developed countries of Europe to the countries of North and South America and Far East. They sold the goods either directly or indirectly through local agents or through their offices set up in those countries. These branches were managed by the merchants’ own families. Initially, the products were exchanged for the indigenous products under a ‘barter system’ of trading. Over the years, Merchant Bankers developed a network of overseas connections in international trade and started buying on their behalf in Europe.

Later on, the firms started banking activities in addition to their trading activities. The overseas connections brought them the banking clients, who deposited the sale proceeds of their products in Europe.
Through these merchant bankers, the overseas customers became investors in UK and started investing in shares and bonds of the overseas countries. The faith in these traders facilitated the explosion of international investment.

Further, these firms also engaged in financing kings of European States, Monarchs and State Governments who engaged in continued wars thereby borne all the risks associated with it. Another reason for such a development in those days was that wealth concentrated mostly in the hands of a very few people. Therefore, instead of borrowing the savings of the general public, the kings and princes got their money by arranging loans with big merchant bankers.

The high profitability in the initial stages made these merchant bankers to lend aggressively to kings, monarchs, etc. However, the increased incidence of bad debts, denouncement of obligations by debtors, etc., made early beginners, viz., Riccardi, Medici, Fugger, etc., either to close down or suffer heavy losses. However, a few others continued with bitter experiences till 16th century.

The concept of Merchant Banking owes its genesis to the Dutch, who were specialised in the trade and finance, during 17th and most of the 18th century. The emergence of ‘British’ as dominant competitors in trade, compelled the Amsterdam traders to shift their capital to financial dealings wherein they developed several financial instruments for facilitating the international trade. With such a shift, the ‘Dutch’
financiers started appointing 'London Merchants' as their agents, thereby making the beginning of 'international houses' which were instrumental in expanding the international trade in the 19th century.

The French war forced the merchants to flee to London with their mercantile expertise, capital and specific trading experience which also helped the development of 'merchant banking tribe'. In the later periods, there took place a separation between trading and finance for various reasons.

The later developments led to further refinement of financial activities. The American Revolutionary War and Napoleon wars crushed down the merchant houses of Liverpool and London, resulting into abrupt increase in bankruptcy rate. This gave an impetus to the emergence of 'Commission Agents' and 'Acceptance Houses' formed by the foreign commercial centres as specialists in the pure finance functions.

'Acceptance Houses' were the stepping stones in the development of merchant banking. They provided 'bread and butter' to the merchant bankers. During 18th century and early 19th century, the trade between the countries was financed by bills of exchange drawn on principal merchanting houses. As the international trade grew and other lesser known names entered the international trade regime, the established merchants 'lent their names' by agreeing to accept bills of
exchange on their behalf, for a commission. Acceptance Houses’ business, thus, became the ‘hallmark’ of true MB.\textsuperscript{11}

The ‘Industrial Revolution’ also contributed to the growth of merchant banking activities. The transshipment of machine made goods from European nations to other nations and raw materials from British colonies to Europe\textsuperscript{12} expanded the merchant banking activities considerably. The timely rise of acceptance houses that assumed the ‘financial risk’ of exporting business, encouraged the emergence of commission agents and small merchants across the world.

Thus, merchanting developed into a banking the commodity trading through foreign exchange and accepting bills of exchange into issue house.\textsuperscript{13} The heroic records of those great MBs whose name is engraved in the history includes, Baring (1770), M.M.Rothschild (1805), Antony Gibbs & Co. (1808), Fruhling and Goschen (1814), Kleinwort (1830), Morgan Grenfell & Co. (1830), A Ruffer and Sons Ltd., (1872), London Merchant Bank Ltd., (1873), Lanzard Brothers & Co. Ltd., (1877)\textsuperscript{14}, etc.

Though the merchant banking concept was the brain-child of some Dutch and Scottish traders,\textsuperscript{15} it was later nourished and nurtured in London. The need for merchant banking services in Britain arose partly due to historical reasons and partly to the requirements of trade and industry. The seeds sown by migrant merchants’ community grew with trade and expanded over the continents and London city emerged
as the financial centre of the world. The term merchant banking is used in equal connotation with that of ‘Investment Banking’ of USA.

Chart 2.1 presents the historical background and various stages of the growth of ‘Merchant Banking’ in UK and ‘Investment Banking’ in USA.

In the rest of the world too, merchant banking started developing on a large scale. The merchant banking institutions in Australia were established between 1960 and 1970 as a result of liberal economic policy of the Government.16

The West Germany’s merchant banking was influenced by European International Trade and Finance, in which the functions of commercial banking and merchant banking were closely related.17

In 1955, London city influenced the merchant banking in South Africa by establishing the first MB, viz., Union Acceptance Ltd., with Anglo-American resources in association with Lazard Brothers.18

Origin in India:

The concept of ‘HUNDI’ remains the hallmark of merchant banking activities in India since the time immemorial.19 The ‘indigenous bankers’ who carried on their profession on hereditary basis, used to receive deposits, deal in hundies and perform other functions. They combined money lending and trading by discounting hundies related to finance, industry and trade.
CHART – 2.1
Historical Background of the Growth of Merchant Banking

In UK

- Industrial Revenue 1697-1760
- 1780 Entry of European Merchants Trade/Industry
- 1793-1815 European wars Migrants, French, Jews, Greek, Handers, Bearing
- MBs tribe Financial Centre of world Mercantile and Financial Enterprise
- 18th-19th century Power, Competency of International Trade of MBs
- 1960 onwards MBs, Clearing Banks, Subsidiaries
- Post I and II War Merger, Amalgamation, Issue Management, Issue House Association
- End of 19th Century. MBs Controlled, Banking, Foreign Trade, Exchange, Bank of England AFB

In USA

- Financial Entry of Resources Europe/British Merchants to USA
- 1824 IMB K. Peabody & Co Capital Raising, Counselling, Corporate Services, Securities Trade
- Promotion of Large Corporation, IB’s members, Fls/CBs
- 20th Century Merger & Amalgamations. Issue of securities
- Securities Exchange Commission. Regulatory Body
- 1933. IBs Association New Deal Enactments
- 1914. FR Act Blue Sky Laws Investors Protection
Thomas Skinners Annual Directories ‘The London Banks (1880)’ made an interesting study on the origin and growth of merchant banking activities in India. The ‘Agency House’ was the traditional name given to merchant banking in India and in the Far East. During 1813, the trade and commerce developed in India through the London based agency houses, viz., John Palmer & Co., Edward Bousted, Mathesons, Dent Parmer and Co., David Sassoon and E.D.Sassoon & Co.20

These agency houses lent loans to local merchants by recycling their home resources and the deposits of Indian based foreign merchants, which initially met the fund requirements of trading community. This state prevailed till the formation and appearance of East India Co., on the trade scene of India.

By the year 1820, India was under the influence of foreign merchant bankers operating through their East India House (EIH). There were 18 such firms with major interest in India acting as representatives of European Merchants. A severe turn took place in EIH business which favoured India by establishing its own bank, known as Joint Stock Banks (JSB)21 and on the other hand, it crushed the growth of indigenous merchant bankers.

The EIH failed to face the stiff competition posed by Persian Finance Houses (a well recognised name in Calcutta by 1836) and most of them diverted their activities to real estate business and a very few of them remained in the field. Since East India Merchants had enough
capital to invest, in the late 1860's, a few of them initiated the establishment of ‘JSB’ with their own investment. Despite this, opposition from East India Company, a few new banks were established, viz., Orient Bank in 1845, Chartered Bank of India and Asia in 1853, Chartered Mercantile Bank of India in 1857, etc.

These banks were controlled by London based merchant bankers through their ‘Managing Agents’ (MA). The earlier ‘Agency Houses’ with a new responsibility of managing these enterprises, successfully met the needs of local traders, affecting further the growth of merchant banking in India.

The ‘Managing Agency System’ (MAS) was the ‘Gateway’ through which London based merchants and MBs performed the functions such as financing, promoting, project development, venture capital, guaranteeing the loans and advances, public deposits, interlocking of funds, etc. They emerged as financial intermediaries by managing corporate issues. They became the backbone of economic development by controlling the Indian industry. However, neither did it develop a right capital market in India nor it went for underwriting of shares of Indian business houses.

The Indian capital market underwent a change with an amendment brought into the Indian Companies Act 1936, insisting companies to disclose the ‘underwriting’ details in prospectus. The Companies Act 1956, further streamlined the procedure of ‘Capital
Issues'. The post-independence era witnessed the Government of India's planned attempt to improve the underdeveloped capital market with institutional and legislative support.

The Government of India, in order to streamline the investment environment, established specialised financial institutions such as Industrial Finance Corporation of India (1948), State Finance Corporations (1950), Industrial Credit and Investment Corporation of India (1955), The Refinance Corporation for Industry Ltd., (1958), Industrial Development Bank of India (1964), Unit Trust of India (1964), National Industrial Development Corporation (1965), State Industrial and Investment Corporations (1966), etc. The growth shown by these institutions, since their establishment, further accentuated the growth of merchant banking activities in India.

After having built the sound base for capital market, the GOI abolished the MAS in 1969 - a long standing hurdle in the growth of merchant banking activities.

Chart 2.2 presents the historical background and various stages of the growth of 'Merchant Banking’ in India.

**Concept of Merchant Bank:**

The term 'merchant bank' is used in a very loose sense, as its usage varies according to place, functions and regulations. Traditionally, the 'merchant' turned 'bank' was named as 'merchant bank'. It is proper to call a merchant banker primarily a merchant rather than a banker, though he is entrusted with the funds of his customers.

A perusal of the historical evidences reveals that the merchants who financed domestic and international trades, financial needs of kings, princes and the governments gradually identified themselves more with banking activities such as short-term loans, bills discounting, long-term loans, foreign exchange, etc., and emerged themselves with the label called ‘merchant banker’.

C.J.J. Clay and B.S. Wheble, in their book *Modern Merchant Banking*, define merchant banking as “the so called merchant banks in London are now seldom merchants and by no means always bankers: the title is often misused as a generic description of firms that operate in
CHART – 2.2
Growth of Merchant Banking in India

The initial Mark ‘HUNDI’

1813. Entry of European MBs
London/France

1820. UK’s MBs
East India’s House. Agency
Houses

1845-1860
Joint Stock
Banks. MAs of
London MBs

Abolition of MAs.
Cap. issues
procedures.

1936. Investors
Protection Act

Indian
Agency
Houses. Pre-World
wars II

Subsidiaries of
British
Firms. Control
by Managing
Agency system

Regulatory Framework,
WT, OT, IT,
MRTP, Capitalisation
Act. Sec, Control Act,
1950-1970

Special Fls, IFCI,
ICICI, LIC, UTI,
IDBI, NIDs, IRDs,
GIC, SFC
1950-1970

1969 MBD of
Grindlays
National Bank:
Beginning of MB
Era

1972, Bkg
Commission
CBs & MBDs, SBI,
MBD, Fls.

1984 Stock Exch.
Reforms 1986. CBs
Subsidiaries. SBI
Cap.

1986-1987
Credit Rating
Agencies. CARE
SHCIL, DFHI

1988-1992
SEBI Regn.
Regulations. Abolition of
CCI

1997 Dec 7
SEBI MBg
Reforms

35
financial sector whether they perform pure banking services or merchanting services or not". An inference that could be drawn from the above statement is that the –

"Merchant Banks are neither merchants nor bankers".

It is indeed difficult to say precisely as to what constitutes merchant banking. The conceptual clarity is difficult to assess unless the "functional" aspects are brought into it. Herbert, J.A.P. opines that MB as "Merchant Bank is what a merchant banker does".25

The Dictionary on Banking Terms and Concepts ‘A’ to ‘Z’ compiled by Lobo Prabhu explains that "Merchant Banking is an innovation in the field of services rendered by the banks, which consists of obtaining government consents, project feasibility, raising of foreign exchange, managing the public issues, corporate restructuring, corporate counselling, assisting in widening and strengthening the capital base of small scale industries."26

The modern merchant banks render a variety of services, which cannot be abridged in a definition as their services are, in fact, flexible and client oriented. The concept till today evades a clear definition. "Merchant Banks are basically development banks, but they do not lend."27 Similarly, "Merchant Banking is largely a project banking but does not lend against securities.28 In USA ‘Investment Banking’ term is used to describe merchant banking functions performed in UK."
In the Indian context, merchant banking is understood as an ‘innovative financial services’. The regulatory body for merchant banks in India, viz., SEBI in its Rules and Regulations for Merchant Bankers 1992 defines, “Merchant Banker means any person who is engaged in the business of issue management either by making arrangement regarding selling, buying or subscribing to securities as manager, consultant, adviser or rendering corporate advisory services in relation to such issue management”.

*Prima facie,* it appears that, the definition of SEBI lays more emphasis on the issue management activity, as it continues to be the ‘core function’ of Indian MBs. In conclusion, it can be said that, merchant bank means –

* A non-banking organisation,
* A catalytic financial intermediary,
* A service unit providing the entire range of advisory services, and
* A fee based activity.

MBs are necessarily financial intermediaries who play a vital role in transforming the ‘stored wealth’ of investors into ‘productive wealth’ of corporates.

Merchant Banking is not commercial banking, though the terms ‘merchant’ and ‘commercial’ have similar connotations. In fact, MBs do some commercial banking and commercial banks may do some
merchant banking. 'Intermediation' is common both for commercial bank and an MB with a difference in customers and the context of service rendered.

There is a close relationship between the merchant banking and development banking in the project oriented activities, wherein the former acts as a 'project advisor' and the latter as 'project financier'.

In the light of the SEBI's modified rules and regulations for merchant bankers, the merchant banking has been confined to 'service' activity. Hence, the hallmark of modern MBs is the quality of their services, objectivity and soundness of their advice to clients, which in turn depends upon the professional experts behind it. Hence, MBs live on their wits.

Functions of MBs:

The MBs in India as financial intermediaries play a vital role in the capital market between the savers and users of funds. Intermediaries can promote growth by increasing the fraction of resources that the society saves or by improving the way the society allocates the savings.

In foreign countries MBs perform varied functions. Initially, MBs in London engaged in acceptance of credit, sponsoring the issue, term lending, bills discounting, foreign exchange transactions, etc.
before moving to issue management functions. The functions of MBs in India can be studied in two stages, viz., pre- and post-SEBI period.

Pre-SEBI Period:

The historical evidences indicate that merchant banking in India was under the great influence of European trade links. The Indian stock broking firms traditionally performed a few merchant banking activities in their own fashion. The Merchant Banking Divisions (MBDs), established by the foreign banks, viz., Grindlays Bank Ltd. and Citibank Ltd. undertook functions such as pre-investment studies, project finance, market research, systems design, management audit, production management and operations research, export markets and foreign collaborations, recruitment and organisational development. With the passage of time, functional spectrum of these banks has undergone a change.

The public sector banks established their MBDs from 1972 onwards. Under the regime of Controller of Capital Issues, these divisions specialised themselves in areas such as project finance, advice, project appraisal, capital structuring, bills discounting, issue management, underwriting, relief to sick industrial units, etc. The amendment that was brought to Banking Regulation Act in 1984 permitted the subsidiaries to undertake leasing and hire-purchase activities also.
Post-SEBI Period:


The authorised activities of merchant bankers during this period have been:

* Corporate Issue Management,
* Corporate Advice Services relating to issue,
* Underwriting,
* Portfolio Management, and
* Manager, Consultants/Advisor in the issue.

In India, the Public Issue Management (PIM) of corporate issues continues to be the core competency activity of the registered merchant bankers in their various capacities as lead managers, advisers, etc.

The SEBI modified its regulations on 7th December, 1997 which were termed as 'mile-stone' in the history of 'Indian Merchant Banking'. The SEBI categorised activities into fund based and fee based and made MBs to concentrate only on the latter than on the former activities. With these modifications, the merchant banking activities received a professional touch. In the light of this metamorphosis in the capital market and financial services, the
merchant banking sector adopted quickly by incorporating the modern services.

The functions of modern MBs are presented in Chart 2.3.

**Organisation of MBs:**

In India, the merchant banking activities were carried on in an unorganised manner during the colonial period. The MAS, in its real sense, was the unique effort made by foreign merchants to carry on merchant banking activities in an organised way. The MAS undertook the basic issue management. The Government of India’s effort to build an organised capital market, led to the establishment of specialised financial institutions. These financial institutions along with their developmental activities performed a few of merchant banking related activities.

The foreign banks are the forerunners of merchant banking activities in India. The Grindlays Bank was the first to initiate merchant banking activities by establishing its MBD. This was followed by the commercial banks and all India financial institutions which established their own MBDs from 1972 onwards. This divisional activity remained as the most viable form of merchant banking organisation in India till the incorporation of subsidiaries by commercial banks. The SBI Capital Markets Ltd., was the first of its kind to be established by the public sector banks in 1986. Other banks
followed suit by establishing their own subsidiaries to meet the increased demand of the specialised merchant banking services.

The private sector MBs comprise of stock brokers, partnership firms, private limited companies, etc. Historically, many of these organisations were founded during the colonial period working under the pressure of MAS. The stock brokers are the licensed operators in the recognised stock exchange.

Chart 2.4 presents in brief the organisations rendering the merchant banking services in India.

Each of the above organisations depicted in Chart 2.4 has to itself register with the SEBI, as category merchant bankers which were classified under four authorised categories, viz., I, II, III and IV. This categorisation is based on the functional specialisation. Table 2.1 shows the classification of MBs adopted by the SEBI.

**TABLE – 2.1**

Classification of MBs

<table>
<thead>
<tr>
<th>Category</th>
<th>Net worth Rupees</th>
<th>Functions</th>
</tr>
</thead>
<tbody>
<tr>
<td>I</td>
<td>5,00,00,000</td>
<td>Lead Manager, Adviser, Consultant, Co-manager, Portfolio Manager, Underwriter</td>
</tr>
<tr>
<td>II</td>
<td>50,00,000</td>
<td>Co-manager, Consultant, Underwriter, Portfolio Manager</td>
</tr>
<tr>
<td>III</td>
<td>20,00,000</td>
<td>Underwriter, Adviser, Consultant</td>
</tr>
<tr>
<td>IV</td>
<td>Nil</td>
<td>Adviser, Consultant</td>
</tr>
</tbody>
</table>

Source: SEBI – Annual Report.

These organisations may adopt any type of ‘organisational pattern’ to suit their requirements. There are different patterns, viz.,
CHART 2.4

Organisation of Merchant Banking Activities in India

Financial Institutions

National Level

State Level

Banks

Indian

Foreign

Private Merchant Banks

Stock Brokers

Sole Proprietors

Partnership Firms

Private Company

Public Pvt. Co.

Consultancy Firms
functional oriented, expert oriented, combination of functional and experts, manager oriented, proprietary oriented, etc., which are adopted by most of the merchant banking institutions for their organisations. The pattern, thus adopted, depends upon the nature of services rendered by the MBs.

In India, the manager oriented pattern is highly preferred in which manager heads the organisation and looks after the entire gamut of activities with the help of assistant managers. But the merchant banking subsidiaries have gone for a combination of expert and functional oriented form of organisation. The organisational pattern can be taken as the criteria to evaluate the efficiency of an organisation.

**Growth of MBs in India:**

Since the establishment of Grindlays Bank's division of MB in India, the activity has seen the tremendous growth. In the following pages, the growth of MB activities is analysed with the help of the following criteria:

* Number of MBs registered,
* Number of issues managed,
* Amount of issues handled,
* Participation of various agencies,
* Variety of instruments issued,
* Number of initial public offers, etc.
Number of MBs Registered:

The GOI's effort to renew the Indian capital market and market intermediaries are evident throughout the history. A remarkable development was the constitution of Securities Exchange Board of India (SEBI) in 1988, as an apex Board to promote the orderly and healthy growth of securities market and abolition of the office of the Controller of Capital Issues.

The SEBI was established on the lines of 'Securities and Exchange Commission' of USA and 'Securities and Investment Board' of UK.

The SEBI promulgated distinct rules on merchant banking activities in the year 1992. Every individual or institution intending to undertake merchant banking activities has to register with the SEBI. It is done according to categorisation prescribed by the SEBI. Table 2.2 gives information regarding number of registered MBs in India since the establishment of the SEBI. gives information regarding number of registered MBs in India since the establishment of the SEBI.

A perusal of Table 2.2 reveals that –

- There is a continuous increase in all categories of MBs up to 1997. This surge could be attributed to the abolition of CCI office and introduction of 'Free-Pricing' of issues.
TABLE – 2.2

Number of Registered MBs in India

<table>
<thead>
<tr>
<th>Year</th>
<th>Categories</th>
<th></th>
<th></th>
<th></th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>I</td>
<td>II</td>
<td>III</td>
<td>IV</td>
<td></td>
</tr>
<tr>
<td>1992-93</td>
<td>127</td>
<td>09</td>
<td>08</td>
<td>29</td>
<td>173</td>
</tr>
<tr>
<td>1993-94</td>
<td>211</td>
<td>28</td>
<td>35</td>
<td>148</td>
<td>422</td>
</tr>
<tr>
<td>1994-95</td>
<td>NA</td>
<td>NA</td>
<td>NA</td>
<td>NA</td>
<td>790</td>
</tr>
<tr>
<td>1995-96</td>
<td>404</td>
<td>72</td>
<td>158</td>
<td>364</td>
<td>998</td>
</tr>
<tr>
<td>1996-97</td>
<td>440</td>
<td>107</td>
<td>172</td>
<td>444</td>
<td>1163</td>
</tr>
<tr>
<td>1997-98</td>
<td>343</td>
<td>82</td>
<td>91</td>
<td>286</td>
<td>802</td>
</tr>
<tr>
<td>1998-99</td>
<td>243</td>
<td>31</td>
<td>14</td>
<td>127</td>
<td>415</td>
</tr>
<tr>
<td>1999-2000</td>
<td>174</td>
<td>Nil</td>
<td>Nil</td>
<td>12</td>
<td>186</td>
</tr>
</tbody>
</table>

Source: SEBI –Annual Reports.

* After 1997, the trend has reversed and number of MBs registered declined from 1,163 in 1996-97 to 186 in 1999-2000. This decline can be attributed completely to increased competition among MBs, sluggish conditions in capital markets, reduced number of issues, increased reliance on private placement route by corporate houses, etc.

A further analysis of Table 2.2 shows that only category-I MBs have remained in the market while the rest of the categories have almost ceased to exist. Out of 186 MBs registered, category-I has 174 MBs while the rest belong to category-IV MBs doing only advisory and consultation services. Further, the category-I MBs have grown and fallen with the overall trend of MBs in India.

**Number of Public Issues Handled:**

The growth of merchant banking is related with a number of developments in the Indian economy in general and capital market in particular. The shift from the era of administered prices to market
determined prices, deregulation of interest rates and the process of liberalisation, globalization and privatisation have brought a sea change in the pattern of financing adopted by the corporate entities. The disintermediation process has set in India and the corporate world is inclined more to raise funds directly from savers than the traditional time tested route of raising through financial institutions. This change has tremendous impact on the growth of MBs in India in terms of number of issues handled and average amount of issues handled. Table 2.3 shows the number and amount of issues handled.

A perusal of Table 2.3 reveals the following:

* In all the years, the number of public issues floated exceed the number of companies going for public issues. It means on an average each company has made more than one issue to mobilize the funds.

* Number of issues handled in all the years of the period covered exceed the number of MBs handling issues except in 1998 and 1999. This indicates each MB in a given year has managed more than one issue. This is a welcome sign for the development of capital market.

* A continuous increasing trend in capital market issues is evident up to 1996 followed by sluggishness and slump in the remaining years.

* The average amount handled by each MB has shown a mixed trend. After showing a decrease in 1991, it increased in 1992 and 1993 and has decreased continuously in later years till 1996. In the last four years of the study period, the average amount
Source: Prime Data, RBI Currency and Finance Reports.

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of companies floating the Public issues</th>
<th>Number of Public issues</th>
<th>Percentage of increase or decrease over previous</th>
<th>Number of MBs participated in public issues</th>
<th>Percentage of increase or decrease over previous</th>
<th>Total amount of public issues Rs. crore</th>
<th>Percentage of increase or decrease over previous</th>
<th>Average amount handled by MB</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980-81</td>
<td>192</td>
<td>199</td>
<td>--</td>
<td>--</td>
<td>--</td>
<td>113.00</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>1983-84</td>
<td>756</td>
<td>120</td>
<td>120</td>
<td>--</td>
<td>--</td>
<td>401.00</td>
<td>+254.87</td>
<td>--</td>
</tr>
<tr>
<td>1986-87</td>
<td>141</td>
<td>120</td>
<td>2793.26</td>
<td>+116.62</td>
<td>23.28</td>
<td>222.20</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>1989-90</td>
<td>187</td>
<td>199</td>
<td>2793.26</td>
<td>+116.62</td>
<td>23.28</td>
<td>1292.00</td>
<td>+222.20</td>
<td>--</td>
</tr>
<tr>
<td>1992-93</td>
<td>528</td>
<td>536</td>
<td>+155.24</td>
<td>100</td>
<td>+26.58</td>
<td>6060.83</td>
<td>+254.15</td>
<td>60.61</td>
</tr>
<tr>
<td>1993-94</td>
<td>770</td>
<td>778</td>
<td>+45.15</td>
<td>253</td>
<td>+153.00</td>
<td>12544.04</td>
<td>+106.97</td>
<td>49.58</td>
</tr>
<tr>
<td>1994-95</td>
<td>1343</td>
<td>1364</td>
<td>+75.32</td>
<td>420</td>
<td>+66.01</td>
<td>13311.60</td>
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<td>31.69</td>
</tr>
<tr>
<td>1995-96</td>
<td>1428</td>
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<td>+5.42</td>
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<td>10981.72</td>
<td>-17.50</td>
<td>20.04</td>
</tr>
<tr>
<td>1996-97</td>
<td>753</td>
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<td>442</td>
<td>+19.34</td>
<td>11648.20</td>
<td>+6.07</td>
<td>26.35</td>
</tr>
<tr>
<td>1997-98</td>
<td>62</td>
<td>63</td>
<td>-91.69</td>
<td>99</td>
<td>-77.60</td>
<td>3061.22</td>
<td>-73.72</td>
<td>30.92</td>
</tr>
<tr>
<td>1998-99</td>
<td>32</td>
<td>32</td>
<td>-49.21</td>
<td>42</td>
<td>-57.58</td>
<td>7910.74</td>
<td>+158.42</td>
<td>188.35</td>
</tr>
<tr>
<td>1999-2000</td>
<td>65</td>
<td>66</td>
<td>+106.25</td>
<td>58</td>
<td>30.10</td>
<td>7673.14</td>
<td>-3.00</td>
<td>132.30</td>
</tr>
</tbody>
</table>
collected has shown an increasing trend. The sudden slump from 1994-95 to 1996-97 could be attributed to two reasons:

- decrease in number of issues by companies, and
- increase in number of MBs operating in the capital market.

Though there is no dramatic increase in number of companies floating public issues, the dependence on a few top ranked MBs for PIM has increased the average amount handled in 1999 and 2000.

**Participation of Various Agencies:**

The upsurge in the capital market between 1990 and 1996 has increased the participation of varied types of financial intermediaries. Further, a successful merchant banking activities in issue management, underwriting, etc., require active participation of multiplicity of agencies such as Bankers to Issue, Registrars, Brokers, Underwriters, Advertising Agencies, Printers, Solicitors, MBs, etc. A banker to the issue manages the funds collected from the issue; the registrar looks after the legal records, a broker underwriter assures minimum subscription in the event of under-subscription, an advertising agency publicise the concerned issue, printing of application, etc., are carried on by the printers to the issue. The solicitors manage the legal aspects. The MBs play a dominant role in co-ordinating the activities of all these agencies for successful issue management besides rendering the other corporate counselling services.
Table 2.4 depicts the information regarding various types of intermediaries participating in merchant banking activity.

<table>
<thead>
<tr>
<th>Year</th>
<th>Bankers to issue</th>
<th>Registrar to issue</th>
<th>Broker underwriters</th>
<th>Advertising agencies</th>
<th>Printers</th>
<th>Solicitors</th>
<th>MBs</th>
</tr>
</thead>
<tbody>
<tr>
<td>1989-90</td>
<td>61</td>
<td>47</td>
<td>517</td>
<td>36</td>
<td>16</td>
<td>93</td>
<td>120</td>
</tr>
<tr>
<td>1990-91</td>
<td>61</td>
<td>36</td>
<td>573</td>
<td>32</td>
<td>12</td>
<td>70</td>
<td>94</td>
</tr>
<tr>
<td>1991-92</td>
<td>74</td>
<td>39</td>
<td>851</td>
<td>35</td>
<td>11</td>
<td>114</td>
<td>79</td>
</tr>
<tr>
<td>1992-93</td>
<td>71</td>
<td>80</td>
<td>1296</td>
<td>73</td>
<td>39</td>
<td>279</td>
<td>100</td>
</tr>
<tr>
<td>1993-94</td>
<td>68</td>
<td>88</td>
<td>1478</td>
<td>101</td>
<td>71</td>
<td>--</td>
<td>253</td>
</tr>
<tr>
<td>1994-95</td>
<td>71</td>
<td>101</td>
<td>1712</td>
<td>146</td>
<td>66</td>
<td>--</td>
<td>420</td>
</tr>
<tr>
<td>1995-96</td>
<td>72</td>
<td>131</td>
<td>1207</td>
<td>194</td>
<td>70</td>
<td>--</td>
<td>548</td>
</tr>
<tr>
<td>1996-97</td>
<td>69</td>
<td>126</td>
<td>336</td>
<td>158</td>
<td>64</td>
<td>--</td>
<td>442</td>
</tr>
<tr>
<td>1997-98</td>
<td>48</td>
<td>35</td>
<td>03</td>
<td>32</td>
<td>23</td>
<td>--</td>
<td>99</td>
</tr>
<tr>
<td>1998-99</td>
<td>44</td>
<td>22</td>
<td>01</td>
<td>12</td>
<td>13</td>
<td>--</td>
<td>42</td>
</tr>
<tr>
<td>1999-2000</td>
<td>58</td>
<td>17</td>
<td>12</td>
<td>16</td>
<td>13</td>
<td>--</td>
<td>58</td>
</tr>
</tbody>
</table>

Source: Prime Data.

A perusal of able 2.4 reveals that –

* There is a continuous increase in the number of all agencies participating in the capital issue market up to 1996.

* The downward trend from 1997 onwards can be attributed to sluggish primary capital market conditions.

* The optional underwriting policy and strict entry norms of the SEBI together decreased the number of underwriters and MBs in the post SEBI modified regulations period (1997).

**Instrument-wise Analysis:**

In recent years, the capital markets in India have been revolutionised with the introduction of new instruments. As a result of
this, the household savings have got directed to the corporate entities. The MBs have a definite role to play in successful issue of various securities. The need of the hour is to develop equity cult among the investors. This would rejuvenate the capital markets and lead to enhanced capital formation.

With this end in view, an attempt has been made to analyse the security-wise issue management.

Table 2.5 presents data regarding the security-wise funds mobilisation.

An analysis of data presented in Table 2.5 shows that only two instruments, namely, equity and debentures continue to be the market preferred instruments, though the amount mobilised through debenture instrument is the second most preferred route than preference share in the years after 1993. The introduction of liberalisation, privatisation and globalisation policies in 1991 saw the introduction of bonds with various alternate features. The upsurge in bonds can be attributed to financial institutions' preference for bonds and debentures in fund raising activities than the manufacturing and trading sectors. As a result, the amount mobilised from the year 1997 onwards through bonds exceeds even the equity instrument. In the year 2000, the amount raised through bonds is Rs.4,698.43 crore whereas equity instrument is just Rs.266.45 crore which indicates that bonds are the
**TABLE - 2.5**  
Security-wise Funds Mobilisation.  
(Rs. crores)

<table>
<thead>
<tr>
<th>Year</th>
<th>Equity shares</th>
<th>Preference shares</th>
<th>Debentures</th>
<th>Bonds and others</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>No.</td>
<td>Amount</td>
<td>No.</td>
<td>Amount</td>
</tr>
<tr>
<td>1989-90</td>
<td>154</td>
<td>351.19</td>
<td>01</td>
<td>05.10</td>
</tr>
<tr>
<td>1990-91</td>
<td>109</td>
<td>604.34</td>
<td>01</td>
<td>01.00</td>
</tr>
<tr>
<td>1991-92</td>
<td>159</td>
<td>552.77</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>1992-93</td>
<td>487</td>
<td>2762.54</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>1993-94</td>
<td>713</td>
<td>6202.69</td>
<td>03</td>
<td>51.03</td>
</tr>
<tr>
<td>1994-95</td>
<td>1304</td>
<td>8945.80</td>
<td>05</td>
<td>74.98</td>
</tr>
<tr>
<td>1995-96</td>
<td>1406</td>
<td>7754.36</td>
<td>05</td>
<td>62.48</td>
</tr>
<tr>
<td>1996-97</td>
<td>735</td>
<td>4600.66</td>
<td>02</td>
<td>24.01</td>
</tr>
<tr>
<td>1997-98</td>
<td>55</td>
<td>1024.99</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>1998-99</td>
<td>19</td>
<td>399.71</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>1999-2000</td>
<td>60</td>
<td>2967.94</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>5281</td>
<td>36166.99</td>
<td>17</td>
<td>218.60</td>
</tr>
</tbody>
</table>

Source: Prime Annual Report and SEBI Annual Reports.
market preferred instrument. The preference issues have lost their significance with no issues from 1998 onwards.

**IPOs Management:**

The Government of India's effort to improve the capital market operations and procedures to raise the public fund has supported the morale of new entrepreneurs. The new liberalised industrial licensing policy has increasingly recognised the need of supporting technocrats to materialise their ideas. The MBs can assist the entrepreneurs in this respect by formulating and financing the business plans. Their function is mainly to act as sponsors and underwriters, rather than as financiers. The efficiency with which MBs perform can decide the success of new entrepreneurs. With no past track record, the direct sale of securities would be a difficult task. Further, lack of capital would jeopardise the very idea of being commercialised. The lead managers with proper placing and management of issue can ensure the initial success of the enterprise.

The social role of MBs demands that the IPOs must be managed successfully. In the successful management of IPOs lies, the revival and prospects of capital markets in general and MBs performance in particular.

With this end in view, an attempt has been made to analyse how far MBs have successfully managed IPOs of the new entrepreneurs. Table 2.6 provides this data.
TABLE – 2.6
Management of IPOs by MBs

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of IPOs</th>
<th>Percentage increase or decrease over previous year</th>
<th>Amount issued</th>
<th>Percentage increase or decrease over previous year</th>
<th>Average amount of issue</th>
<th>Total number of public issue</th>
<th>Percentage of IPOs to total issues</th>
</tr>
</thead>
<tbody>
<tr>
<td>1989-90</td>
<td>92</td>
<td>--</td>
<td>354.33</td>
<td>--</td>
<td>3.85</td>
<td>187</td>
<td>49.20</td>
</tr>
<tr>
<td>1990-91</td>
<td>57</td>
<td>-38.04</td>
<td>367.15</td>
<td>+3.62</td>
<td>6.44</td>
<td>141</td>
<td>40.43</td>
</tr>
<tr>
<td>1991-92</td>
<td>83</td>
<td>+45.61</td>
<td>397.58</td>
<td>+8.29</td>
<td>4.79</td>
<td>196</td>
<td>42.35</td>
</tr>
<tr>
<td>1992-93</td>
<td>231</td>
<td>+178.31</td>
<td>3224.36</td>
<td>+710.99</td>
<td>13.96</td>
<td>528</td>
<td>43.75</td>
</tr>
<tr>
<td>1993-94</td>
<td>695</td>
<td>+200.87</td>
<td>8269.76</td>
<td>+156.48</td>
<td>11.90</td>
<td>770</td>
<td>90.26</td>
</tr>
<tr>
<td>1994-95</td>
<td>1231</td>
<td>+77.12</td>
<td>9919.12</td>
<td>+19.95</td>
<td>8.06</td>
<td>1343</td>
<td>91.66</td>
</tr>
<tr>
<td>1995-96</td>
<td>1351</td>
<td>+9.75</td>
<td>5509.65</td>
<td>-44.45</td>
<td>4.08</td>
<td>1428</td>
<td>94.61</td>
</tr>
<tr>
<td>1996-97</td>
<td>716</td>
<td>-47.00</td>
<td>4645.87</td>
<td>-15.68</td>
<td>6.49</td>
<td>753</td>
<td>95.09</td>
</tr>
<tr>
<td>1997-98</td>
<td>52</td>
<td>-92.74</td>
<td>907.90</td>
<td>-80.46</td>
<td>17.46</td>
<td>62</td>
<td>83.87</td>
</tr>
<tr>
<td>1999-2000</td>
<td>52</td>
<td>+188.89</td>
<td>2643.94</td>
<td>+597.06</td>
<td>50.85</td>
<td>65</td>
<td>80.00</td>
</tr>
</tbody>
</table>

Source: Prime Data.

A perusal of Table 2.6 depicts that MBs have cultivated the new business enterprises particularly the small and medium scale ones. There is a continuous increase in the number of new issues and amount raised by the MBs. Though, the total number of issues has shown decreasing trend from 1997 onwards, the year 2000 again shows a positive sign. The average amount raised has moved from a low of Rs.3.85 crore to high of Rs.50.85 crore between 1990 and 2000 period. The sponsorship of the IPOs would help in enlisting the confidence of investors who would need to have the assurance that the issue was scrutinised by the financial experts on reasonable terms.

The percentage of IPOs to total issues shows that in the recent years IPOs are the only things which are occurring. It also indicates that sluggishness of capital market is partly explainable for the lack of
issues from existing companies in primary market. However, from entrepreneurship development point of view, the increased management of IPOs speaks highly of the role of MBs.

Conclusion:

The trend in the merchant banking industry and capital market was closely monitored by the SEBI which brought a few changes in the 'Merchant Banking Regulations' on 7th December 1997. Prior to these amendments, there were a few ‘contradictory issues’ in the management and business carried on by MBs in India. These include:

* Most of the MBs carried on both ‘fund based’ (Lease, Hire Purchase, etc.) and ‘fee based’ (merchant banking, underwriting, etc.) activities under the same roof.

* Fund based and fee based activities were being monitored by RBI and SEBI respectively, i.e., two separate entities monitoring the (same entity) one entity.

* Fund based activities made MBs to use more of debt sources and the resulting interest burden has led to the erosion of net-worth of MBs. The close monitoring of the fund based activities on continuous basis was possible neither by the RBI nor by the SEBI.

Thus, it was decided to segregate the activities carried on by the same entity. To achieve this, the Merchant Banking Regulations were amended w.e.f. December 9, 1997. As per the amendments—
* A category -I MB (excluding banks and financial institutions) is disallowed from carrying on any activity other than any activity relating to securities market.

* A merchant banker carrying on fund based merchant banking activities would have to either discontinue the activities not related to the securities market or hive off its merchant banking activity.

* Multiple categories of MBs (I, II, III and IV) were abolished and only category-I was retained. Category-II merchant bankers could carry on activities of a portfolio manager and underwriter, whereas category-III merchant banker could carry on activities of underwriters only under separate regulations framed by SEBI. Thus, there is only one entity, i.e., category-I merchant banker who can carry on issue management activity.

Thus, the Indian merchant banking has been marching towards perfection. The regulations introduced by SEBI would promote and guide the capital market and intermediaries. Future is bright for Indian MBs with wide-open opportunities under the ‘Globalization process’. It is expected that Indian merchant banking becomes an ‘ABODE’ of professionalised financial services in the new millennium.
References:


3. Ibid., p. 12.


8. Ibid., p. 111.

9. Ibid., p. 112.

10. Ibid., p. 113.


15. Ibid., p. 168.
16. J.C. Verma, op. cit. p. 15
21. Ibid., p. 32.
23. Ibid., p. 81.


30. Grindlays Bank, Brochure