SUMMARY OF FINDINGS AND SUGGESTIONS

Findings:

The institutionalisation of merchant banking services in India began with the establishment of MBD in 1969 by a foreign bank, viz., Grindlays Bank which later was followed by an Indian Nationalised Bank, i.e., SBI in 1972. Since then MBs have been accepted as the apt intermediaries between the savers and investors. Their key position in the financial intermediation has elevated the role as both pivotal players and operative agencies in the economic development of a nation. They have emerged as the most vital agencies which augment the flow of funds to the requirements of corporate sector. They have to channelise savings not only from the 'mass' to the 'class' but also to see that the corporates are being developed on healthy lines.

The efficient and transparent functioning of capital markets and development of the equity cult among the investing public are the twin responsibilities of MBs. Unless the MBs play a catalysts role, the healthy development of corporates and capital markets on sound footings cannot be foreseen. Absence of MBs may cause technocrats to fall in shelve and defer the expansion, modification plans.
The amendment to the Indian Banking Regulation Act, in 1984 brought another phase in the MBs' history. The need to venture into leasing and hire-purchase activities made the erstwhile MBDs to shift towards independent subsidiaries. The subsidiaries being the first of its kind in India, occupied cardinal position in the economic development embedded 'within' the 'social responsibility' and 'welfare'.

The subsidiaries for their survival and profitability combined fee based and fund based activities under the dual authority of RBI and SEBI, while RBI controlled the latter activities and SEBI the former activities. The multiple activities and dual control neither helped MBs to carry effectively the merchant banking activities nor the regulators to control better the 'net-worth' position of MBs. As a result, MBs drifted in their strategy to develop human resources and tangible assets and moved far away from the professionalisation of the services.

The satisfactory performance of the corporate sector, specially capital intensive industries, experienced a capital market boom in 1992-93 when 'liberalisation' was still in its infant stage.

Though the issues were priced according to the norms of CCI, the IPOs of the FERA Companies boosted the investors' confidence and morale with sizeable returns and capital appreciation.

The spread of the liberalisation message under the free price regime of SEBI, led to the buoyant capital market conditions and Pls in 1995-96 touched with a record of 1,428 issues. This boom in capital
market also acted as safe heaven for unscrupulous entrepreneurs and market players to play mischief with the market and investors' psyche. The companies made good of the situation by charging high premiums without strong fundamentals.

The market realised follies of capital market operators with the failure of corporates to generate expected returns from 1995-96. Further, it also made small investors to feel shy of capital market and equity instrument. Consequently, the debenture and bond issues became popular. The Euro issues, private placement, etc., were adopted by the corporates to raise their funds.

The year 1997 was a crucial in the annals of merchant banking activities in India when the market regulator classified the MB activities into fee based and fund based. The sudden change has taken MBs by surprise and is the bane of contention between SEBI and MBs. The change made the working of MBs highly skeptical and fluctuating. The erstwhile profitable MBs have seen the worst of the days and some have closed their offices too. The merchant banking subsidiaries of public sector banks are no exception to this phenomenon.

In the light of the above developments, the present study entitled, Working of Merchant Banking Institutions in India: A Study of Selected Subsidiaries of Nationalised Banks, is an humble effort to provide comprehensive, historical, structural and quantitative analysis of the activities of MB subsidiaries of nationalised banks. For this
purpose the study selected four subsidiaries, viz., SBICAP, BOIFIN, BOB Caps and IBMBS. Using the prime data and annual reports of MBs, an attempt is made in the study to evaluate public issues management activities, underwriting, leasing and other allied activities and financial performance. A useful set of hypotheses was also constructed to have a deeper insight into the working of the units. The following pages present a brief summary of major findings of the study.

(A) Capital Market Trends in General:

1) A comprehensive, qualitative and quantitative survey of the theoretical literature reveals that there are a number of issues relating to merchant banking institutions which need to be analysed for the healthy growth of capital markets in particular and Indian economy in general.

2) Though much is said about the concept of ‘Merchant Banking’ it still eludes a clear definition. The concept in its origin called for the co-existence of business and banking activities. A survey of literature reveals that all the efforts to define the term rotate around the functions performed by an institution.

3) An analysis of number of MBs that registered with SEBI shows that, there are four different categories of MBs. The entry of Financial Institutions as category-I MB had set a competitive trend in Pls and RIs business. On the other hand, the absence of minimum net worth requirements enhanced the number of advisors to the issue under
category-IV. Their disproportionate increase created a yawning gap between active and inactive MBs as revealed by the difference between the number of MBs registered with SEBI and participated in PIM activity. The modifications brought to the MBs regulation in 1997 abolished all the categories except category-I. This is a welcome modification.

4) The trends in the issue market support the view that Indian capital market has completed two business cycles between 1977 and 1999 in terms of PIs and operating intermediaries. Beginning with hardly 97 PIs in 1976-77, the number reached a peak of 756 issues in 1983-84 and came down to 122 in 1986-87. It recovered in 1989-90 with 187 issues and reached a high of 1,428 in 1995-96 before crashing down to a low of 32 issues in 1998-99. It is evident that, both the highest and lowest points were more severe in the second phase of the business cycle than in the first phase.

5) The health of the economy is denoted by the efficient working of financial intermediaries. Hence, a progressive capital market is sine qua non for the development of intermediaries. There is a high degree of positive correlation between the number of issues managed and number of operators. The extremes of capital market have affected the MBs similarly resulting in a volatile operations of MBs. It is more evident in Indian scenario as the PIM continues to be the bread and butter of MBs.
(B) Organisational Profile:

1) A perusal of organisational profile reveals that the independent subsidiary structure was favoured by sample units in the initial period. The deputed services of experienced personnel, clientele link, equity contribution, well knit branch network, etc., are some of the contributing factors. In subsequent periods, the subsidiaries have gone for modest recruitment methods. The expert and manager oriented management hierarchy and the adoption of different communication models are the distinctive features of MB subsidiaries. The SBICAP has shown quick adaptations to the changes taking place in the capital market than other subsidiaries considered for the study.

2) The branch expansion policy of sample subsidiaries during flourishing conditions has proved unproductive and added to the overhead cost. This is more true with BOIFIN as withdrawal of branches highlights the opportunistic ideology of MBs.

(C) Public Issue Management:

1) The increased number of market intermediaries has led to the unhealthy competition, thereby decreasing the average business of issue amount. The MBs with professional attitude are continued in the merchant banking activity whereas the foreign banks, Indian private sector banks, etc., have been disappearing by slow degrees from the scene.
2) The domination of private merchant bankers in PIM is quite perceptible. Their share in total business showed a continuous increasing trend up to 1998-99. The market share of remaining participants, viz., financial institutions, private sector banks, foreign banks, bank subsidiaries, etc., have shown a decreasing trend. This could be attributed to corporate India's growing confidence and dependence on professional MBs and lack of marketing approach in others.

**PIM of Sample Subsidiaries:**

3) The sample subsidiaries being category-I MBs, differ in their abilities from PIM. The SBICAP leads the PIM both in number and amount throughout the study period. The initial experience and interest are not continued and capitalised by BOB Caps, IBMBS and BOIFIN. Further, they have failed to maintain their hold in PIM in the last two years whereas SBICAP has improved its position thus, proving its organisational capabilities.

4) The average amount of PIs handled by MBs in India presents a mixed trend. Initially a very few MBs managed the large amount but the upsurge in their number has brought down the average size. The hike in average size of SBICAP is due to the application of the principle of 'survival of the fittest'.

5) An analysis of different roles played by sample subsidiaries shows that both in PIM and RIM, lead managership tops the list. In
rare instances, the subsidiaries have acted as co-manager and advisors to the issues.

6) The size-wise analysis of the PIM shows the predominance of small issues with 72 per cent market share followed by medium and mega issues. The sample MBs' preference for various sizes, in relative terms, speaks the organisational strength and capabilities. Except SBICAP, other MB subsidiaries have managed more than 70 per cent of the total small issues followed by medium and mega issues.

7) There exists a high degree of volatility in the IPOs of new companies. All the sample subsidiaries too have similar trend barring SBICAP. The other sample units have failed to attract the business of new entities or have failed to promote the first generation entrepreneurs.

8) In case of FOs, the preference of SBICAP is evident both in number and amount of issues. The last three years of the study period reveals the monopolised position enjoyed by the SBICAP while other sample units have shown a poor performance in the management of FOs of existing companies.

9) There has been a perceptible shift in the type of instruments issued and managed in India in recent years. The slow down in capital market has further worsened the situation with debt and bonds emerging the most preferred route of fund mobilisation. The downfall in equity
instrument is a real cause as it may severely affect the growth of equity cult.

10) Though the equities continued to be the most preferred route for new companies, the amount raised through equity premium issues exceed the equity issues at par. The flooding of premium issues during the flourish conditions and further failure of corporates has become an unbearable trend in the Indian capital market. All the sample subsidiaries have handled more amounts of premium issues except IBMBS. However, the existing companies have issued more number of premium issues but the amount raised is just 1/3rd of bond issues. The SBICAP shows an inclination towards this trend.

11) An analysis of area-wise concentration of PIM shows that the sample subsidiaries have higher inclination towards the city of Mumbai. The BOB Caps has managed the issues of entrepreneurs hailing from all places except Coimbatore while the market leader, i.e., SBICAP has no presence in the major industrial metros of India., viz., Coimbatore, Lucknow and Pune.

12) The increased participation of NRIs is a sign of positive growth. The study reveals that SBICAP continued to be the only champion of merchant banking in recent years. Corporates have shown the least interest with other subsidiaries in managing issues designated purely for NRIs.
13) The developing economies desire the growth of infrastructure to keep pace with the changing scenario. The participation of sample subsidiaries, in such issues is most desired. A perusal of the sector-wise PIM activity reveals certain gaps in the organisation of sample units in managing issues of different sectors. The SBICAP has its domination in industries like sugar, communication, textiles, etc., whereas BOB Caps, BOIFIN and IBMBS have managed more number of financial services, pharmaceuticals and textile sectors issues.

14) There is a continuous increasing trend of 'under subscription rate' of the issues managed by the sample subsidiaries. The rate of under subscription of the issues managed by BOB Caps and BOIFIN is still higher than the all India average under subscription rate. There are few instances of over subscription raising above 75 and 100 times. The under subscription trend is a cause for worry to the corporates and capital market operators.

15) A comparative analysis of all India response and response to the issues managed by sample subsidiaries reveals that SBICAP has shown paradoxical performance with higher over and under subscription rates. The BOB Caps and BOIFIN with 16.61 and 18.90 per cent respectively are above the total subscription at the rate of 15.44 per cent in case of 1 and below 1 time subscription rates, whereas IBMBS has 13.60 per cent. This is also a sign of efficiency of BOB Caps and BOIFIN.
16) Though the MBs are expected to create and float new instruments, they should see that they are market friendly too. An analysis of response to the varied instruments proves that the efforts made by sample subsidiaries have experienced a severe setback. The shift from equities to debentures and bonds has resulted in more issues with under subscription.

17) The efforts to push issues during flourishing conditions to attain favourable subscription have proved unsuccessful for sample subsidiaries. An evolution of the rate of under-subscribed issues during the peak period supports the above statement with under-subscribed percentage at 60.

18) The public apathy towards the issues managed by sample units is evident in the analysis of ECD. The increased percentage of deferring the ECD reflects two things: one, the lack of marketing abilities of subsidiaries and other management of the unviable issues.

**Rights Issue Management:**

19) An analysis of MBs performance with regard to RIs shows that the SBICAP has managed more number of RIs than the other subsidiaries. The average amount of RIs handled by the subsidiaries shows that except SBICAP, in respect of remaining sample subsidiaries, the amount is lower than the national average calculated for majority of years.
20) The size-wise issue and preference of sample subsidiaries point out that there is a constant domination of large size issues. The study reveals that there is a considerable decline in the number of RIs of Rs.1 crore and below Rs.1 crore. The share of issues of the size of Rs.10 crore and above is 400 per cent more than small issues. The sample subsidiaries too have shown more inclination towards this trend due to less number of risks associated with the RIM.

21) The presumption of easier marketing of RIs has gone wrong with the analysis of the ECD. The percentage of RIs deferring their ECD reveals the failure on the part of the existing companies as well as MB subsidiaries while evaluating their expansion programmes, viability of modifications, justifications for high pricing of their issues. The ratio between the RIs closed on ECD and after ECD was the lowest at 1.47:1 in case of IBMBS. This means for every 1.47 issues, 1 issue got postponed its ECD, i.e., lack of subsidiaries ability to convince the members.

Performance Evaluation:

22) An attempt to make a comparative performance evaluation of sample units by adopting ‘Ranking through Rating Scale’ supports the hypothesis that ‘the performance of SBICAP is better than other subsidiaries in PIM.’ In order to assign different ranks based on their score in the rating scale, the variables were drawn from different dimensions to explore qualitative relations. The total scores thus
obtained were tested by ANOVA technique. The ANOVA values revealed that at 5 per cent level of significance, the calculated F value is more than the table F value. Hence there is a significant difference within each category of sample subsidiaries in PIM. Since the average score of SBICAP is the highest, the hypothesis was proved.

SWOT Analysis:

23) PIM is a complex process and an art by itself. An outstanding performance should be due to the internal strengths or core competencies and capabilities to exploit marked opportunities. A SWOT analysis reveals that SBICAP was able to exploit the capital market and other environmental opportunities with its organisational strengths by overcoming the weaknesses. The concerted efforts to face the threats have favoured the SBICAP’s total performance. On the other hand, for the other sample units Weaknesses and Threats far outweigh the Strengths and Opportunities.

A comparison of SWOT analysis of SBICAP and other subsidiaries bring out the causes for outperformance of SBICAP and poor performance of other sample units.

D) Underwriting and Advisory Services:

1) The underwriting activity in India has experienced wide fluctuations since its introduction. The obligatory underwriting era of CCI and SEBI up to 1994 was largely responsible for higher volumes of
underwriting business. The number of issues underwritten increased from 74 per cent in 1989-90 to 98 per cent in 1992-93 and 1993-94.

2) The post-liberalisation period witnessed the emergence of varied underwriting agencies comprising of FIs, IBs, FBs, Brokers, MBs, etc., to take advantage of the policy and issues penchant for underwriting business. Though, brokers participated more in number, the FIs with sound financial base dominated the underwriting business by managing almost 42 per cent of the total underwritten amount in 1990-1991 and 77 per cent in 1998-1999.

3) The optional underwriting policy introduced by the SEBI in order to reduce the cost of raising the capital was accountable for declining trend in underwriting activities since 1994. The trend touched as low as 11 per cent in 1996-1997 for the total number of underwritten issues and 2 per cent of the underwritten amount. The optional underwriting policy was held good for reputed concerns.

Underwriting and Subsidiaries:

4) The amount underwritten by the sample units clearly discloses the fact that the subsidiaries as underwriters, have played a minor role as underwriting can result in financial risks on account of development. In one way, this policy has freed the sample units from financial obligations but at the same time an opportunity for earning an underwriting commission has been sacrificed.
5) The average amount underwritten by the sample units supports the earlier finding that the amount is lower than all India average amount of underwriting. Except SBICAP, none has shown an inclination towards the recent increase in the average amount of underwriting. The SBICAP continues to be the front player in PIM.

6) A comparison between PIM and underwriting reveals that BOB Caps, BOIFIN and IBMBS have an over dependence on underwriting as the number of underwritten by them exceeds the number of PIM. But, SBICAP has maintained parity between the underwriting and PIM. It depicts that except for SBICAP, the underwriting has become an income generating activity for the other three subsidiaries.

7) The increased devolvement on the part of MBs will convert their business from fee based to fund based since devolvement ultimately to be met by the MBs. This defeats the very purpose of classifying activities into fee based and fund based. However, devolvement in 1998-99 and 1999-2000 is almost conspicuous by its absence for all selected subsidiaries. The subsidiaries, move specifically the SBICAP has the highest number of devolvement.

Leasing Activity:

8) The leasing activity which was analysed since subsidiaries inception shows that the growth of the activity has gone a long way with the growth of sample subsidiaries organisation. The leasing has overtaken the activity profile both qualitatively and quantitatively. The
sample subsidiaries except BOB Caps have shown an over dependence on leasing and hire-purchase by pooling their financial resources in the form of leased assets. Though this has earned enormous amount of income to MBs its prohibition by the SEBI in 1997, has compelled them to equip themselves for the new situation. They still have to go a long way in this process.

**Advisory Services:**

9) Though all the sample subsidiaries have accepted and adopted the fee based activities as per SEBI’s modified regulations, there exists a degree of difference among them. The SBICAP, since inception, has diversified its various fee based activities. Its contribution in the areas of project counselling, corporate counselling, bought out deal, etc., is quite commendable. The BOB Caps has performed varied activities under the banner of project advisory services. The IBMBS has concentrated on stock broking and bought out deals. On the other hand the BOIFIN has concentrated on the stock broking and project advisory activities.

10) An analysis of the clientele profile provides the glimpses about the selectivity of sample subsidiaries. Under the ‘Globalised Economic Scenario’, the subsidiaries still have to go a long way in the process of adjustments to the changes.
E) **Financial Analysis:**

1) The MB subsidiaries were established to undertake activities such as leasing, hire-purchase and merchant banking services. The higher inclination towards the fund based activities has greatly influenced the financial structure and performance of subsidiaries. The increased requirements for funds to perform leasing and fund based activities has led to increased dependence on outsiders’ debt capital. This has led to increased interest burden and has eroded severely the sample units’ profitability and equity base. The weak equity base does not augur well for the future of these units. The sample units’ concentration on fund based activities has resulted into heavy investment in fixed assets.

2) An analysis of the financial structure of MB subsidiaries reveals that the equity share capital is fully contributed by parent banks. In case of SBICAP the Asian Development Bank has a share of 13 per cent in the equity fund. The subsidiaries, except BOB Caps have tapped the debt sources to undertake fund based activities.

3) The study shows that the share of the owned funds in the TFR has increased for all subsidiaries over a period but the growth rate of debt is very high. The percentage of debt in the TFR stood above 90 per cent in the initial periods. This indicates that the financial structure of the sample units except BOB Caps is over dependent on debt capital.
4) The subsidiaries have adopted a conservative financing policy as most of them finance their current assets with long term debt. This has resulted into exceptionally high current ratio.

As far as profitability aspects are concerned the sample MBs have larger share of fund based income than fee based income.

5) A paradigm shift in the financial results of sample units begun with the SEBI's rule of segregating the fee based and fund based activities. The MBs are now expected to concentrate only on fee based activities. The change has made MBs to struggle hard to manage the balance sheet by repaying the debt capital thereby reducing the interest burden.

6) The SEBI's modified regulation has resulted into a decreased proportion of leased assets and building up of strong human resources, which is evident in the gradual increase in the operating expenses. In this process of transformation, those with merchant banking activity profile are flourishing in the business while others are experiencing loss. Though the interest burden has decreased, the high proportion of operating expenses has completely engulfed the thin contribution of advisory service income, thus creating a wide gap between GS and NS.

7) The expectations of owners were scarcely met by the subsidiaries except SBICAP and BOB Caps as revealed by ROSE. The negative EPS and DPS for majority of years of study period in case of BOIFIN and IBMBS has affected the retention policies of these sample units.
8) The testing of hypotheses reveals that gross-spread improvement acts positively on net-spread. However, this truth holds good for SBICAP and BOB Caps. Net-spread has depicted varied relations with the constituents of gross income. For SBICAP, the fee based income is the predominant factor whereas for BOB Caps, the fund based income is predominant one. The fund based activities are the major income generating activity as net profit after tax has a better correlation with the fund based activity. The financial performance of SBICAP is better than other sample subsidiaries considered for the study.

Suggestions:

Merchant banking, which was considered as a money spinning activity a few years ago, is now regarded as a redundant and unviable segment by one and all. Most of the MBs that made their entry in the early 90’s have closed their offices and those surviving are optimising revenue. The failure of a number of MBs has been primarily due to their entry without proper understanding of the dynamics of the business. The undue emphasis on PIM activity has led to the collapse of many MBs because of downslide in primary market.

The temptation to make quick money without adequate value addition and professionalisation made many public sector banks to establish their offices in merchant banking field. The initial success of some subsidiaries goaded many others to join the band wagon. However, when the primary market collapsed, the existence became
very difficult and many MBs became red. A perusal of PIM and financial performance of sample MBs shows that barring SBICAP, the rest of the units lack any justification for their existence in future.

Merchant banking is basically a professional job and primary function of a merchant banker is raising resources for his customers. In other words, the MB is an important market intermediary. The World Bank in its report entitled ‘Development Briefs’ comments on the role of market intermediaries and says that, “financial intermediaries are essential for economic growth and development. The main contribution of financial intermediaries in promoting growth through increasing the fraction of resources of society saves or improving the way the society allocates savings. They improve allocation of resources and diversify risks and exploit economies of scale. They also stimulate individual to save more besides mobilising and allocating savings”

The Indian financial system is poised for dramatic changes in the years to come or in the new millennium. Full convertibility, free flow of FDI and FIIs investment, issue of GDRs and ADRs in foreign markets, Euro-currency loans and debt, entry of global players in Indian capital markets, etc., are some of the sweeping changes bound to occur in the new century.

Merchant banking institutions with professional outlook, penchant for efficiency, intensive human skills, relationship, market
strategy, good governance, ethical practices, etc., can only be expected to prosper and survive in the new millennium.

The sample MBs are no exception to this dictum. The following suggestions, if adhered to, can make the sample MBs vibrant and fit to meet the future challenges.

1. **Leaner Balance Sheet and Profit and Loss Account**

The MBs are affected very much by SEBI's Regulation of 1997 which dovetailed the activities into fee based and fund based. This means that the MBs, henceforth, have to concentrate on the former activities which include PIM, Underwriting, Corporate Counselling, Merger and Amalgamations, etc. They have to weed out activities like lease and hire-purchase. However, the SEBI has allowed them to continue the existing contracts.

This classification is expected to make a serious dent to the financial statements. The future balance sheet would be very simple containing assets like building, cash, etc., and liabilities like only owner's contribution. The income statement is expected to contain only fee based income.

The sample MBs can initiate actions towards leaner financial statements by offloading, leased and hire-purchase assets and by repaying debt obligations. They can make use of securitisation process for this purpose. Securitisation is an approach which widely followed
by lending institutions to sell out assets which are long term in nature. For this purpose, the originators, i.e., MBs or their parent organisations need to create Special Purpose Vehicles (SPV) and sell all the leased and hire-purchase assets to such SPVs for the purpose of creation of securitised debt. The money that is received from SPV can be used to off-load all the fixed income obligations. Being MBs of nationalised banks, the marketing of secured debt would not be a difficult proposition for MBs. With this one measure, the sample MBs can concentrate only on fee based activities and improve overall performance. The SPV can be wound up upon the completion of all the obligations.

2) **Broadened Activity Profile**:

The PIM still continues to be the core activity of MB subsidiaries. The opening up of Indian economy to the world economy by liberalisation, privatisation and globalisation policies since 1991 has created wide open opportunities. The emerging corporate sector will heavily depend on MBs in managing their finance. Corporate restructure, joint ventures, mergers and amalgamation, innovative financial products, disinvestment in public sector undertaking by the Government, etc., are the order of the day. Under changing environment, subsidiaries need to widen the activity spread to move towards ‘one stop banking’ and ‘globalised financial services’. Though SBICAP has widened activity, other sample subsidiaries in general need to widen their activity mix. This widened activity profile would enable
MBs to collect their fee based income from diverse sources and reduce
dependence on PIM which is ‘fair-weather friend’.

3) **Dispersal of PIM Activities:**

The MBs in their concentration of PIM activity have restricted
their activity to only metros and other big cities. The equity culture or
security investment culture is yet to percolate down the system. The
savings of other cities and rural areas need to be tapped and made
available to corporate India. This does not mean the MBs should
establish their offices in all the areas and suffer subsequently. To
develop wide investment culture, as issue managers of corporate
securities, they can make use of the existing network of branches of
their parent organisations which are the nationalised banks. This
approach leads to better subscription of the issues and improved
reputation of MB. This can be expected to bring more business and
income.

4) **Coverage of Agro-sector:**

The MB activities are directed towards industrial sector and kept
aside the agriculture sector. MB subsidiaries should join hand with
parent banks in rural areas to evaluate the agro-based industries,
projects, market requirements, rural entrepreneurs, export avenues,
marketability of projects, etc. With this, the MB subsidiaries of
nationalised banks enable themselves to discharge the social
responsibility in assisting the Indian agro-economy which is struggling hard under the delicensed import policies of government.

5) **Human Resource Management:**

The success of merchant banking activities is larger dependent on the human skills available. The business is skill intensive in every function, beginning from sensing market directions and new opportunities, pitching for business, structuring of instruments, to negotiation of deals and ensuring of legal and regulatory compliance in all transactions. The MBs are required to recruit people who fulfil the above expectations rather than deputing people working in the parent organisations. Parent bank may insist and may force such individuals, however, merchant banking is a specialised activity by itself and needs to be taken very seriously. People who are wedded to the profession and who have practical exposure should be on the rolls of sample subsidiaries in future.

Further, senior level appointments have to be made by the respective boards of directors by accessing the market place and offering market related salaries and incentives. The board of directors, based on performance should renew senior level appointments. The institutions should have right to compulsorily retire existing 'non-performing employees' and recruit new staff without guaranteeing the life time employment. Even the threat of action will improve performance and productivity.
6) Cautious Pricing:

The MB subsidiaries should be very cautious while pricing the issues, more particularly, the premium issues. The premium payable should not be arbitrarily determined, lest it may seriously damage the investors' confidence in premium issues. Premium should not be the sweet will of issuers and MB. MBs should discourage ambitious promoters without viable projects.

MB subsidiaries should go for 'book building process' where an issue price is fixed at an acceptable level of investors with a few intermediaries and least failures. The current scenario of free pricing has increased the MBs' responsibilities. An MB ideally would need to ask himself the following questions.

(a) Can I lend my name to this issue?
(b) Is the product appropriate and price fair?
(c) Are the agencies well equipped to discharge their duties?
(d) Are the disclosures fair and factual?
(e) Is the company willing to co-operate in ensuring compliance of above? etc.

7) Strategic Alliances with Global Operators:

The entry of Global operators in the Indian economy has perfored the Indian MBs to go for tie-up arrangements with global operators. Indian corporate sector is widening its horizons and is
raising foreign funds. The subsidiaries will have to incorporate requisite expertise in the international merchant banking.

Further, the Indian capital market may be opened for foreign corporates to issue their securities. This two-way approach of Indian Government enables MBs to be more professional and competent. Strategic alliances and foreign collaborations can equip the sample MBs with necessary expertise, skill, manpower and resources to handle issues of Indian corporates abroad and foreign issues in Indian strategic alliances are essentially agreements between two or more companies to share the costs, risks and benefits associated with development of real business opportunities. The Indian capital market scenario is undergoing dramatic change with the permission of foreign banks and private sector banks to operate and foreign investment in Indian insurance sector. Like insurance sector, opened to foreign players, the Central Government should permit foreign MBs to participate in equity investment of Indian MBs and help in developing strategic competence of Indian MBs. Even alliances between foreign banks MBs, private sector MBs, etc. and sample MBs could be thought of.

8) Merger, Reconstruction, etc. :

It has been found in the study that barring SBICAP and BOB Caps, the remaining subsidiaries have shown negative financial performance for four to five years. Further, their participation in MB activities is dismal to say the least. The poor working of such MBs is
affecting the performance of even the parent banks. The best example is Indian Bank, the parent bank of IBMBS, is one of the samples MB has been considered for the study. The Indian Bank is in great financial difficulties in recent years and has depended on the Central Government financial help for capital adequacy requirements.

In this context, the question is “is it worthwhile to continue such subsidiaries?” If the above suggestions cannot work wonders for the units, the parent bank can consider the option of absorbing these units and run merchant banking activities on divisional basis. Once strength is gained and proficiency established, the parent bank could think of spinning off activities into fully owned subsidiaries.

This measure can enable parent bank to develop skills, reduce increasing overheads, personnel expenses and nurture internal skills for future expansion.

9) Relationship Management:

Merchant Banking is a relationship business and is rarely sustainable on transaction basis. The client as well as merchant bank must exercise sufficient discretion prior to placing or accepting a merchant banking mandate. The client needs to be sure that his merchant banker is capable of delivering the objectives of mandate while merchant banker needs to be sure of the client’s commitment to the mandate objective.
The MB needs to maintain a good amount of consistency not only for deals executed but also in sharing information towards arousing awareness in the client fraternity for which he may not necessarily expect fees. This sort of exercise should also involve diverse but related areas such as investment options and acquisition of units.

10) Underwriting Capabilities:

An MB must be adequately capitalised for several reasons. One, this is a working capital intensive because fees are largely back ended and linked to success. Besides, ‘Underwriting Capability’ is a crucial factor. The rule “put your money where your mouth is” holds very true for investors. The lead merchant banker in any offering usually heads the list of underwriters for this very reason. Opportunities such as bought out deals also presume substantial upfront financial commitment by the merchant banker and his entire earnings in such deal is the difference between his entry and exit price.

The parent banks must infuse fresh funds into the coffers of sample MBs to enable them to meet commitments arising out of firm underwriting and development of underwritten issues. Though underwriting can be both fee based and fund based activity, it becomes fund based only on devolvement. However, adhering to SEBI classification, sample MBs can hold such investment for time being and sell them when things are good in the market.
There is a need to make underwriting a serious business by ensuring that underwriting commitments are strictly enforced so that, underwriters do not support weak issues.

11) Control of Overhead Expenditure:

The sample MBs should remember the relation between gross spread and net spread. The gross spread is the difference between gross income and interest expenses. While net spread is calculated by deducting operating expenses from gross spread. For banking institutions in general and for merchant banking institutions in particular spread is the bread and butter. Business performance should always be evaluated on the basis of spread percentages.

The net spread can be positive, provided attempts are made at reducing overhead expenses like management cost. The control of this expenditure through better planning and control exercise can go a long way in improving the net spread as well as return on capital employed. At the same time, as mentioned above, better activity planning would improve the gross spread.

12) Effective Marketing:

Marketing is always a challenging function. To market any issue, the MBs should select agencies such as advertisers, media, printers, etc., in a proper manner. The sample subsidiaries are working in the buyers’ market where ample opportunities are available to issuing
corporates. In the midst of cut-throat competition for the business, it becomes imperative on the part of MBs to market or place an issue with adequate preparations. It is the responsibility of the MB to convince himself of the strength of the issues which will enable him to market it successfully with the help of other agencies.

13) Support Small Issues or Technocrats:

The small issues always experience myriad problems in floating their issues. The MB subsidiaries should frame a distinct plan to support the small issues, specially of technocrats. The subsidiaries can privately place these issues with their parent banks to ensure materialisation of ideas and projects till such companies' performance meets the requirement of investment community or capital market. This provides 'triple-benefit' in the form of capital gains to parent banks, commercialisation of technocrats' projects or small issues and assured returns to the MB subsidiaries.

14) Portfolio Management:

In the wake of fluctuating mutual funds performance, the millions of small investors hailing from middle class and lower middle class segments are extremely in need of specialised services like portfolio management. The subsidiaries of nationalised banks are the right MBs, having the necessary experience to enter this field. Though household sector is the hallmark of Indian saving community, its share of investment in industrial sector is meagre which augurs the MBs to
mobilise the savings effectively and efficiently. MBs are apt intermediaries to operate in the changing pattern of investment of household sector in favour of corporate securities. This would support the very object of disintermediation, thereby reducing the cost of raising the capital for corporates and ‘safe investment’ for the savers.

15) **Effective and Efficient Research and Development Department:**

The subsidiaries should not manage the public issue on chance factor. They should ensure that issues are floated at right time, right price, right investor, etc. The MBs’ research and development department be established, equipped with necessary infrastructure to analyse the investment environment, conduct security research, corporate research, policy research, etc., in the prevailing capital market. This would increase success rate of issues managed. A continued introspection by MBs with R&D findings would heighten the morale and rebuild internal strength.

16) **Imbibe Ethical Practices:**

Merchant Banking outfits needs to accept radical changes as far as business philosophy is concerned. While maximising revenue and profits will remain the foremost business objective, necessary importance and emphasis should be provided for conservativeness, good governance and ethical practices which in the long run would improve
the fundamental strength of the market, broad base the market, make it more resilient and also pleasant for the foreign eye.

Compliance is not essential for avoiding penalties but also crucial for protecting credibility. Hence, the sample merchant bankers have to take extra precaution in their selection of officers and executives and ensure a high level of business ethics within the organisation.\textsuperscript{5}

17) **Congenial Atmosphere** :

Merchant Banker should offer his services by way of impartial adviser and assist the entrepreneurs as their clients and not as borrowers. The meeting between these should be of mutual trust and it must create an atmosphere of relaxation in which the entrepreneur would feel at ease to unfold his plans, narrate antecedents, qualifications, experience, concept of new project, resources at his disposal, etc. This congenial atmosphere is \textit{sine qua non} to acquire an insight into the clients' character and build credibility in the minds of entrepreneurs as well as investors.

18) **Special Care to NRIs** :

The huge contributions of NRIs is expected in the light of establishment of capital intensive industries in the developing economy. The sample subsidiaries can concentrate on these NRIs for profitable investment proposals or for setting up of industries in
collaboration with Indian industrialists and *vis-a-vis*. These subsidiaries can arrange for the transfer of funds through banks with necessary Government permission. They should act as 'Ready Reckoner' for the opportunities that need foreign participation.

19) **Segregation of Due Diligence Certificate Procedure**:

The present system of drafting the prospectus and issuing due diligence certificate should be segregated. No doubt, it pinpoints the responsibility of MB but it has become boon for MBs. An independent authority under the SEBI should issue the due diligence certificate. This will help in screening the MBs' performance in the beginning itself by curbing promotion of unviable project by inexperienced merchant bankers.

20) **Don't Kill the Hen**:

The Indian MBs have made a lot of money in 1993 and 1994. The sample MBs should always remember the adage that 'it is always better to have one egg a day from a golden hen. Killing the hen would also kill them.' The issues floated by promoters with flamboyant styles of running their business should be weeded out. They are today paying a heavy price. The MBs should adhere to the professional ethics while handling each issue. They should step into the shoes of investor while evaluating the commercialisation or economic viability of the projects.
21) **Stricter Licensing**:

The SEBI should further strengthen its licensing requirements and make merchant banking activity as a business place for serious players rather than for fly-by-night operators. The strict licensing will leave the place only for efficient and social consciousness MBs. Few players and efficient working by sample MBs can lead to better performance in the form of higher average issues handled and higher fee based income level.

Thus, the above suggestions, if properly heeded and adhered to, may enable the sample merchant banking subsidiaries of nationalised banks to become self-reliant financially and viable operationally, efficient and effective merchant banking units in the merchant banking field in India.
References:


4. Ibid., p. 107.

5. Ibid., p. 107.