MERCHANT BANKING AND FINANCIAL SERVICES

PREPARED AND COMPILED BY

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MERCHANT BANKING AND FINANCIAL SERVICES
UNIT 1

Subject Code : UNOM /Com 212

Merchant Banking and Financial Services

Objective: To provide conceptual understanding and in depth knowledge of merchant banking services concerning financial markets in India and to provide knowledge of financial services

UNIT I Merchant Banking – merchant bankers – corporate counseling – project counseling – preinvestment studies – capital restructuring services – credit syndication – issue management – portfolio management – working capital finance – mergers and acquisition – foreign currency financing – brokering fixed deposits – project appraisal – merchant banking – regulatory framework – SEBI guidelines

UNIT II Public issue management – functions – categories of securities issue – issue manager – role of issue manager – activities involved I issue management – marketing of new issue – pure prospectus method – offer for sale method – private placement method – IPO method – rights issue method – bonus issue method – book-building – ESOP – OTCEI – Credit Syndication Services

UNIT III Post-issue activities – major activities – steps – factors in public issue proposal – pricing of issues – law relating to issue management – SEBI regulations – Prospectus – information – abridged prospectus – misstatement in prospectus – golden rule – types of prospectus – red-herring prospectus – shelf prospectus – M & A services – Portfolio Management Services

UNIT IV Underwriting – meaning – types – mechanism – benefits and functions – Indian Scenario – underwriting agencies – underwriter – underwriting agreement – SEBI guidelines – Bought-out deals – grey market – capital market instruments – types – preference shares – equity shares – CCPS – company deposits – warrants – debentures and bonds – SEBI guidelines – global debt instruments – indexed bonds – floating rate Bonds – ECBs

UNIT V Depository receipts – meaning and mechanism – benefits – steps in issue of GDR – IDR – Stock exchange – history – functions – Indian stock exchanges – SEBI regulations – mechanics of settlement – margin trading – stock trading system -0 dealer trading system – NSMS – ISE – INDONEXT – NSE – Financial Services – leasing – hire-purchase finance – bill financing – factoring – consumer finance – real estate financing – credit cards – credit rating venture capital

Book References

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Merchant Banking in India

The first merchant bank was set up in 1969 by Grind lays Bank. Initially they were issue mangers looking after the issue of shares and raising capital for the company. But subsequently they expanded their activities such as working capital management; syndication of project finance, global loans, mergers, capital restructuring, etc., initially the merchant banker in India was in the form of management of public issue and providing financial consultancy for foreign banks. In 1973, SBI started the merchant banking and it was followed by ICICI. SBI capital market was set up in August 1986 as a fully-fledged merchant banker. Between 1974 and 1985, the merchant banker has promoted lot of companies. However, they were brought under the control of SEBI in 1992.

Recent Developments in Merchant Banking and Challenges Ahead:

The recent developments in Merchant banking are due to certain contributory factorsin India. They are

- The Merchant Banking was at its best during 1985-1992 being when there were
- Many new issues. It is expected that 2010 that it is going to be party time for
- Merchant banks, as many new issues are coming up.
- The foreign investors –both in the form of portfolio investment and through foreign
- Direct investments are venturing in Indian Economy. It is increasing the scope of
- Merchant bankers in many ways.
- Disinvestment in the government sector in the country gives a big scope to the
- Merchant banks to function as consultants.
- New financial instruments are introduced in the market time and again. This basically
- Provides more and more opportunity to the merchant banks.
- The mergers and corporate restructuring along with MOU and MOA are giving
- Immense opportunity to the merchant bankers for consultancy jobs. However the challenges faced by merchant bankers in India are

1. SEBI guideline has restricted their operations to Issue Management and Portfolio Management to some extent. So, the scope of work is limited.

2. In efficiency of the clients are often blamed on to the merchant banks, so they are into trouble without any fault of their own.

3. The net worth requirement is very high in categories I and II specially, so many professionally experienced person/ organizations cannot come into the picture.

4. Poor New issues market in India is drying up the business of the merchant bankers. Thus the merchant bankers are those financial intermediary involved with the activity of transferring capital funds to those borrowers who are interested in borrowing. The activities of the merchant banking in India is very vast in the nature of

- The management of the customers securities
- The management of the portfolio
- The management of projects and counseling as well as appraisal
- The management of underwriting of shares and debentures
- The circumvention of the syndication of loans
- Management of the interest and dividend etc.

Functions of merchant Banking:

Merchant banking functions in India is the same as merchant banks in UK and other European countries. The following are the functions of merchant bankers in India.

- Corporate counseling
- Project Counseling
- Capita l Structuring
- Portfolio Management
- Issue Management
- Credit Syndication
- Working capital
- Venture Capital
- Lease Finance
- Fixed Deposits

(i) Corporate counseling: Corporate counseling covers counseling in the form of project counseling, capital restructuring, project management, public issue management, loan syndication, working capital fixed deposit, lease financing, acceptance credit etc., The scope of corporate counseling is limited to giving suggestions and opinions to the client and help taking actions to solve their problems. It is provided to a corporate unit with a view to ensure better performance, maintain steady growth and create better image among investors.

(ii) Project counseling Project counseling is a part of corporate counseling and relates to project finance. It broadly covers the study of the project, offering advisory assistance on the viability and procedural steps for its implementation.

a. Identification of potential investment avenues.

b. A general view of the project ideas or project profiles.

c. Advising on procedural aspects of project implementation d. Reviewing the technical feasibility of the project

e.Assisting inthe(TechnicalselectionConsultancyOrganizations)of forTCOspreparing project reports

f. Assisting in the preparation of project report

g. Assisting in obtaining approvals, licenses, grants, foreign collaboration etc., from government

h. Capital structuring

i. Arranging and negotiating foreign collaborations, amalgamations, mergers and takeovers.

j. Assisting clients in preparing applications for financial assistance to various national and state level institutions banks etc.,

k. Providing assistance to entrepreneurs coming to India in seeking approvals from the Government of India.

(iii)Capital Structure Here the Capital Structure is worked out i.e., the capital required, raising of the capital, debt-equity ratio, issue of shares and debentures, working capital, fixed capital requirements, etc.,

(iv) Portfolio Management It refers to the effective management of Securities i.e., the merchant banker helps the investor in matters pertaining to investment decisions. Taxation and inflation are taken into account while advising on investment in different securities. The merchant banker also undertakes the function of buying and selling of securities on behalf of their client companies. Investments are done in such a way that it ensures maximum returns and minimum risks.

(v)Issue Management: Management of issues refers to effective marketing of corporate securities viz., equity shares, preference shares and debentures or bonds by offering them to public. Merchant banks act as intermediary whose main job is to transfer capital from those who own it to those who need it. The issue function may be broadly divided in to pre issue and post issue management.

a. Issue through prospectus, offer for sale and private placement.
b. Marketing and underwriting
c. pricing of issues

(vi) Credit Syndication: Credit Syndication refers to obtaining of loans from single development finance institution or a syndicate or consortium. Merchant Banks help corporate clients to raise syndicated loans from commercials banks. Merchant banks helps in identifying which financial institution should be approached for term loans. The merchant bankers follow certain steps before assisting the clients approach the appropriate financial institutions.
a.Merchant banker first makes an appraisal of the project to satisfy that it is viable b. He ensures that the project adheres to the guidelines for financing industrial projects. c. It helps in designing capital structure, determining the promoters amount of term loan to be raised. d. After verifications of the project, the Merchant Banker arranges for a preliminary meeting with financial institution. e. If the financial institution agrees to consider the proposal, the application is filled and submitted along with other documents.
(vii) Working Capital: The Companies are given Working Capital finance, depending upon their earning capacities in relation to the interest rate prevailing in the market.

(viii)Venture Capital: Venture Capital is a kind of capital requirement which carries more risks and hence only few institutions come forward to finance. The merchant banker looks in to the technical competency of the entrepreneur for venture capital finance.

(ix). Fixed Deposit: Merchant bankers assist the companies to raise finance by way of fixed deposits from the public. However such companies should fulfill credit rating requirements.

(x)Other Functions

•**Treasury Management**- Management of short term fund requirements by client companies.

•**Stock broking**- helping the investors through a network of service units

•**Servicing of issues**- servicing the shareholders and debenture holders in distributing dividends, debenture interest.

•**Small Scale industry counseling**- counseling SSI units on marketing and finance

•**Equity research and investment counseling** –merchant banker plays an important role in providing equity research and investment counseling because the investor is not in a position to take appropriate investment decision.

•**Assistance to NRI investors** - the NRI investors are brought to the notice of the various investment opportunities in the country.

•**Foreign Collaboration**: Foreign collaboration arrangements are made by the Merchant bankers.

An overview of Indian Financial System

The word system implies a set of complex and interrelated factors organized in a particular form. These factors are mostly interdependent but not always mutually exclusive. The financial system of any country consists of several ingredients. It includes financial institutions, markets, financial instruments, services, transactions, agents, claims and liabilities in the economy.

Financial system‘sto canalize the funds from the surplus units to the deficit UnitsDeficit. Unitsiscase where current expenditure exceeds their current income. There are other entities whose current income Surplusexceeds Units.

An efficient financial system not only encourages savings and investments, it also efficiently allocates resources in different investment avenues and thus accelerates the rate of economic development. The financial system of a country plays a crucial role of allocating scarce capital resources to productive uses. Its efficient functioning is of critical importance to the economy.

FINANCIAL SYSTEM:

•It is a system for the efficient management and creation of finance. According to **Robinson**, financial system provides a link between savings and investment for the creation of new wealth and to permit portfolio adjustment in the composition of the existing wealth. According to **Van Horne**, financial system is defined as the purpose of financial markets to allocate savings efficiently in an economy to ultimate users –either for investment in real assets or for consumption. Thus the financial system mainly stands on three factors

- Money
- Credit
- Finance

1.Moneysthe unit of exchange or medium of payment. It represents the value of financial transactions in qualitative terms.

2. Credit, on the other hand, is a debt or loan which is to be returned normally with interest.

3. Finance is monetary wealth of the state, an institution or a person. Comprising these factors in a systematic order forms a financial system.

Objectives

The objectives of the financial system are

1. Accelerating the growth of economic development.

2. Encouraging rapid industrialization

3. Acting as an agent to various economic factors such as industry, agricultural sector, Government etc.

4. Accelerating rural development

5. Providing necessary financial support to industry

6. Financing housing and small scale industries

7. Development of backward areas, infrastructure and livelihood

8. Imposing price control in need

9. Protecting environment. Functions of financial system are distributed from creation of money to efficient Management. It is the sum total of the functions of the various intermediaries.

The functions of financial system can be classified into two broad categories:

1. Controlling functions

2. Promotional functions.

Components of Financial System:

Financial system Institutions Markets Financial Institutions Instruments Services **Structure of**

Financial Institutions:

COMMERCIAL BANKS:

Commercial Banks Classification of Commercial Banks

- Financial Institutions
- Banking
- Non Banking
- Companies
- Non Banking
- Financial companies
- Central Bank
- Commercial
- Banks
- Co-Operative
- Banks
- Non Banking
- Financial
- Intermediaries
- Joint Stock companies

Classification of Co-operative Banks NON BANKING FINANCIL INTERMEDIARIES
Classification of Non Banking Financial Intermediaries
(B) FINANCIAL MARKETS: Components of Financial Market Co-operative Banks

- State Co-operative
- Apex Banks
- State Co-operative Urban
- Banks
- Co-operative Land
- Development

- Banks
- Central Co-operative
- Banks Primary Co-operative
- Land Development
- Banks
- Primary Co-operative
- Banks

Limitations of the financial system in India

The following are the limitations of the Indian financial system. • The Indian Financial system has failed to meet the financial needs of small scale Industries. It has rather patroned the big industrial houses who are already well off. • The mushrooming of financial institutions has deteriorated the quality and effectiveness of the sector to some extent. • In many cases, it could not impose adequate control towards financial irregularities and frauds, often influenced by politically and economically organized pressure groups. • The Indian financial system fails to create a well defined and organized capital market. • It fails to motivate economically marginal or small entrepreneurs by providing micro credit to them. • The Indian financial system is not flexible at the desired level. It takes abnormal time to cope with the changing situation.

- Factoring Asset Liability Management
- Leasing Housing Finance
- Forfeiting Portfolio Finance
- Hire Purchase Finance Underwriting
- Credit Card Credit rating
- Merchant Banking Interest and Credit Swap
- Book Building Mutual fund

Securities and Exchange Board of India (Merchant Bankers) Rules, 1992 — A merchant banker has been defined as any person who is engaged in the business of issue management either by making arrangements regarding selling, buying or subscribing to securities or acting as manager, consultant, adviser or rendering corporate advisory services in relation to such issue management.

RandomHouse Dictionary

Merchant banker is writesan securitiesorganization for corporations, advices such clients on mergers and is involved in the ownership of commercial ventures. These organizations are sometime banks which are not merchants and sometimes merchants who are not banks and sometimes houses which are neither merchants nor banks.

Charles P. Kindleberger —Merchant banking is the development which frequently encountered a prolonged intermediate stage known in England originally as merchant banking. **The Notification of the Ministry of finance** defines A merchant banker as any person who is engaged in the business of issue management either by making arrangements regarding selling, buying or subscribing to the securities as manager, consultant, adviser or rendering corporate advisory service in relation to such issue management.

Objectives

- Channelizing the financial surplus of the general public into productive investments avenues
- Co-coordinating the activities of various intermediaries like the registrar, bankers, advertising agency, printers, underwriters, brokers, etc., to the share issue
- Ensuring the compliance with rules and regulations governing the securities market.

MERCHANT BANKING AND LEGAL REGULATORY FRAME WORK

1. **Companies Act**

(i). Company means a company formed and registered under this Act or an existing company as defined in clause (ii);

(ii). Existing company means a company formed and registered under any of the previous companies laws specified below:

a. any Act or Acts relating to companies in force before the Indian Companies Act, 1866 (10 of 1866) and repealed by the Act;

b. The Indian Companies Act, 1866

c. The Indian Companies Act, 1882 d. the Indian Companies Act, 1913 e. the Registration of Transferred Companies Ordinance 1942.

iii. Private company means a company which has a minimum paid-up capital of one lakh rupees or such higher paid-up capital as may be prescribed, and by its articles,

a. Restricts the right to transfer its shares, if any;

b. Limits the number of its members to fifty not including i. persons who are in the employment of the company, and ii. persons who, having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment ceased; and

c. Prohibits any invitation to the public to subscribe for any shares in, or debentures of, the company;

d. Prohibits any invitation or acceptance of deposits from persons other than its members, directors or their relatives Provided that where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this definition, be treated as a single member;

iv. Public company means a company which a. is not a private company; b. has a minimum paid-up capital of five lakh rupees or such higher paid-up capital, s may be prescribed c. is a private company which is a subsidiary of a company which is not a private company.

In this Act, unless the context otherwise requires,

1. Abridged prospectus means a memorandum containing such salient features of a prospectus as may be prescribed

2. Banking company has the same meaning as in the Banking Companies Act, 1949

3. Company Law Board means the Board of Company Law Administration constituted under section 10E

4. Debenture includes debenture stock bonds and any other securities of a company, whether constituting a charge on the assets of the company or not;

5. Derivative has the same meaning as in clause (aa) of section 2 of the Securities Contracts (Regulation) Act, 1956

6. Hybrid means any security which has the character of more than one type of security, including their derivatives;

7. Issued generally means, in relation to a prospectus, issued to persons irrespective of their being existing members or debenture-holders of the body corporate to which the prospectus relates;

8. Prospectus means any document described or issued as a prospectus and includes any notice, circular, advertisement or other document inviting deposits from the public or inviting

offers from the public for the subscription or purchase of any shares in, or debentures of, a body corporate;

9. Recognized stock exchange means, in relation to any provision of this Act in which it occurs a stock exchange whether in or outside India, which is notified by the Central Government in the Official Gazette as a recognized stock exchange for the purposes of that provision;

10. Registrar means a Registrar, or an Additional, a Joint, a Deputy or an Assistant Registrar, having the duty of registering companies under this Act;

11. Securities means securities as defined in clause (h) of section 2 of the Securities Contracts (Regulation) Act, 1956

12.Securities and Exchange Board of India means the Securities and Exchange Board of India established under section 3 of the Securities and Exchange Board of India Act, 1992

13.Share means share in the share capital of a company, and includes stock except where a distinction between stock and shares is expressed or implied;

2 Provisions under Companies Act

The various regulations which govern the merchant bankers on the capital issue are prescribed by the companies act, and the other enactments mentioned below.

1. Provisions of the Companies Act, 1956

a. Prospectus (Sec. 55 to 68A)

b. Allotment (Sec. 55 to 75)

c. Commissions and discounts (Sec. 76 & 77)

d. Issue of shares at premium and at discount (Sec. 78 & 79)

e. Issue and redemption of preference shares (Sec. 80 & 80A)

f. Further issues of capital (Sec. 81)

g. Nature, numbering and certificate of shares (Sec. 82 to 84)

h. Kinds of share capital and prohibition on issue of any other kind of shares (Sec. 85 & 86)

- Matters to be specified in prospectus and reports to be set out therein (Schedule 11)

- The Securities Contracts (Regulations) Act, 1957 regarding transactions in securities
- The Securities Contracts (Regulation) Rules, 1957.

2. Their capital adequacy

3. Their track record, experience and general reputation

4. Adequacy and quality of personnel employed by them and also the available infrastructure.

3 SCRA (Security contract regulation Act):

The Securities Contracts (Regulations) Act was passed in 1956 by Parliament and it came into force in February 1957. An act to prevent undesirable transactions in securities by regulating the business of dealing therein, by providing for certain other matters connected therewith.

1. This Act may be called the Securities Contracts (Regulation) Act, 1956. 2. It extends to the whole of India.

2.It shall come into force on such date as the Central Government may, by notification in the Official Gazette, appoint.

Definitions

a. Contract means a contract for or relating to the purchase or sale of securities;

b. Corporatization means the succession of a recognized stock exchange, being a Body of individuals or a society registered under the Societies Registration Act, 1860 (21 of 1860), by another stock exchange, being a company incorporated for The purpose of assisting, regulating or controlling the business of buying, selling or dealing in securities carried on by such individuals or society;

c. demutualization means the segregation of ownership and management from the trading rights of the members of a recognized stock exchange in accordance with a scheme approved by the Securities and Exchange Board of India;

(d) **Derivative includes:**

a. a security derived from a debt instrument, share, loan, whether secured or unsecured, risk instrument or contract for differences or any other form of security;
b. a contract which derives its value from the prices, or index of prices, of underlying securities;
c. Government security means a security created and issued, whether before or after the commencement of this Act, by the Central Government or a State Government for the

purpose of raising a public loan and having one of the forms specified in clause (2) of section 2 of the Public Debt Act, 1944 (18 of 1944);
d. Member means a member of a recognized stock exchange;
e. Option in securities means a contract for the purchase or sale of a right to buy or sell, or a rightto buy and sell, securities in future.
f.Recognized stock exchange means a stock exchange which is for the time being recognized by the Central Government under section 4;
g. Stock exchange which may provide for
(i) The issue of shares for a lawful consideration and provision of trading rights in lieu of membership cards of members of a recognized stock exchange;

(ii) The restrictions on voting rights;

(iii) The transfer of property, business, assets, rights, liabilities, recognitions, contracts of the recognized stock exchange, legal proceedings by, or against, the recognized stock exchange, whether in the name of the recognized stock exchange or any trustee or otherwise and any permission given to, or by, the recognized stock exchange;

(iv) The transfer of employees of a recognized stock exchange to another recognized stock exchange;

(iv) any other matter required for the purpose of, or in connection with, the corporatization or demutualization, as the case may be, of the recognized stock exchange

h. Securities include i.e., shares, scrips,stocks,bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;

(h) Government securities;

i. Such other instruments as may be declared by the Central Government to be securities; and
ii. rights or interest in securities;

(j). Stock Exchange means a anybody of individuals, whether incorporated or not, constituted before corporatization and demutualization under sections 4A and 4B, or b. a body corporate incorporated under the Companies Act 1956 whether under a scheme of corporatization and demutualization or otherwise, for the purpose of assisting, regulating or controlling the business of buying.

ISSUE MANAGEMENT INTRODUCTION

INTRODUCTION

Merchant Banking, as a commercial activity, took shape in India through the management of Public Issues of capital and Loan Syndication. It was originated in 1969 with the setting up of the Merchant Banking Division by ANZ Grind lays Bank. The main service offered at that time to the corporate enterprises by the merchant banks included the management of public issues and some aspects of financial consultancy. The early and mid-seventies witnessed a boom in the growth of merchant banking organizations in the country with various commercial banks, financial institutions,thefieldof merchantand bankingbrokers. Reform measures were initiated in the capital market from 1992, starting with the conferring of statutory powers on the Securities and Exchange Board of India (SEBI) and the repeal of Capital Issues Control Act and the abolition of the office of the Controller of Capital Issues. These have brought about significant improvement in the functional and regulatory efficiency of the market, enabling the Merchant Bankers shoulder greater legal and moral responsibility towards the investing public.

MERCHANT BANKERS AND CAPITAL ISSUES MANAGEMENT

Merchant Banker has been defined under the Securities & Exchange Board of India (Merchant Bankers) Rules, 1992 as ―any person who management either by making arrangements regarding selling, buying or subscribing to securities as manager, consultant, advisor or rendering corporate advisory service in relation to such issue management. The capital issue management comprises of the effective management of market related factors. They are • Transition to rolling settlement on the equity market • Impact on different classes of market users • Obtaining a liquid bond market • Impact of reforms of 1990s • Law and taxation • Taxation of capital • Legal reforms • Political economy of financial sector reforms • Market design, market inefficiencies, trading profits.

Issue Management: The management of issues for raising funds The management of issues for raising funds through various types of issue management. The function of capital issues management in India is carried out by merchant bankers. The Merchant Bankers have the requisite skill and competence to carry out capital issues management. The funds are raised by companies to finance new projects, expansion / modernization/ diversification of existing u contained in SEBI (Merchant Banker) Rules and Regulations, 1992 clearly brings out the significance of Issue Management as follows: issue management either by making arrangement regarding selling, buying or subscribing to securities as manager, consultant, advisor or rendering corporate advisory services in relation to such issue management.

1 MERCHANTS OF PUBLIC ISSUE MANAGEMENT

Classification of Securities Issue

1. Public Issue

2. Right Issue

3. Private Placement

Decision to Raise Capital Funds Preparation and Finalization of Prospectus Obtaining SEBI Approval Arranging underwriting Selection of Registrars, Brokers, Bankers, etc. Printing and Publicity of Public Issue Documents Arranging Press for investor Conference Issue Launch SEBI Compliance

1. Public Issue of Securities When capital funds are raised through the issue of a prospectus, itis called public issue of securities. It capital market. A security issue may take place either at part, or at a premium or at a discount.

The Prospectus has to disclose all the essential facts about the company to the prospective purchasers of the shares. Further, the prospectus must conform to the formal set out in Schedule II of the Companies Act, 1956, besides taking into the account SEBI guidelines. SEBI insists on the adequacy of disclosure of information that should serve as the basis for investors to make a decision about the investment of their money.

2. Rights Issue When shares are issued to the existing shareholders of a company on a privileged basis, it is called as Rights Issue. The subscribe to the new issue of shares. Rights shares are offered as additional issues by corporate to mop up further capital funds. Such shares are offered in proportion to the capital paid up on the shares held by them at the time of the offer. It is to be noted that the shareholders, although privileged to be offered on the issue, are under no legal obligation to accept the offer. Right shares are usually offered on terms advantageous to the shareholders.

3. Private Placement When the issuing company sells securities directly to the investors, especially institutional investors; it takes the form of private placement. In this case, no prospectus is issued, since it is presumed that the investors have sufficient knowledge and experience and are capable of evaluating the risks of the investment. Private placement covers shares, preference shares and debentures. The role of the financial intermediary, such as the merchant bankers and lead managers, assures great significance in private placement. They involve themselves in the task of preparing an offer memorandum and negotiating with investors.

MERCHANT BANKERS FUNCTIONS

The different functions of merchant bankers towards the capital issues management are 1. Designing Capital Structures. 2. Capital Market Instruments. 3. Preparation of prospectus. 4. Selection of bankers. 5. Advertising Consultants. 6. Choice regarding registrar to the issue. 7. Arranging for underwriting the proposed issue. 8. Choice for the bankers to the issue. 9. Choice for the brokers.

1. DESIGNING CAPITAL STRUCTURE DECISIONS The term capital structure refers to the proportionate claims of debt and equity in the total long-term capitalization of a company.

According to **Weston and Brigham, —**Capital structure is the per represented primarily by long-term-debt, preferred stock and common equity, but excluding all short-term credit. Common equity includes common stock, capital surplus and accumulated retained earnings.

Optimal Capital Structure An ideal mix of various sources of long-term funds that aims at minimizing the overall cost of capital of the firm, and maximizes the market value of shares of a firm is known as _Optimal capital structure_. An optimal capital structure should possess the following characteristics:

a. Simplicity An optimal capital structure must be simple to formulate and implement by the financial executives. For simplicity, it is imperative that the number of securities is limited to debt and equity.

b. Low Cost A sound capital structure must aim at obtaining the capital required for the firm at the lowest possible cost. For this purpose, financial executives must pay attention to keep the expenses of issue and fixed annual payments at a minimum. This would help maximize the shareholdersvalue.

c. Maximum Return and Minimum Risks An ideal capital structure must have a combination of debt and equity in such a manner as to maximize the firm's profits.
Similarly, the firm must be guarded against risks such as taxes, interest rates, costs, etc. with the aim of either reducing them or removing them.

d. Maximum Control The capital structure must aim at retaining maximum control with the existing shareholders. The issue of securities should be based on the pattern of voting rights. It must affect favourably the voting structure of the existing shareholders, and increase their control on the company's affairs.

e. Liquidity In order to have a sound capital structure, it is important that the various components help provide the firm greater solvency through higher liquidity. To attain a high order of liquidity, all such debts that threaten the company's solvency must be avoided.

f. Flexibility The capital structure should be so constructed that it is possible for the company to carry out any required change in the capitalization in tune with the changing conditions. Accordingly, the firm must be able to either raise a new level of capital, or reduce the existing level of capital.

g. Equitable Capitalization An ideal capital structure must be neither over capitalized nor under-capitalized. Capitalization must be based purely on the financial needs of the

enterprise. An equitable capitalization would help make full utilization of the available capital at minimum cost.

h. **Optimum Leverage** The firm must attempt to secure a balanced leverage by issuing both debt and equity at certain ideal proportions. It is best for the firm to issue debt when the rate of interest is low. Conversely, equity is suitable where the rate of capitalization is high.

Factors Affecting Capital Structure Decisions

The following factors significantly influence the capital structure decision of a firm: **Economy Characteristics** The major developments taking place in the economy affect the capital structure of firms. In order words, the way the economy of a country is managed determines the way the capital structure of a firm will be determined. Factors that are active in the economy are:

1. Business activity: The quality of business activity prevailing in the economy determines the capital structure pattern of a firm. Under conditions of expanding business activities, the firm must have several alternatives to source the required capital in order to undertake profitable investment activities. Under these circumstances, it is advisable for a firm to undertake equity funding rather than debt funding.

2**. Stock market**: The buoyancy, or otherwise, of the capital market greatly influences capital structure decisions. A study of the capital market trends would greatly help a firms decision on the quantum and cost of issue. Accordingly, if the stock market is expected to witness bullish trends, the interest rates will go up and debt will become costlier.

3. **Taxation:** The rates and rules of taxation prevalent in an economy also affect capital structure decisions. For instance, higher rates of taxation will be advantageous due to the tax deductibility benefit of debt funding. Similarly, the taxes on dividend income, if any, would adversely affect the ability of firms to raise equity capital.

4. **Regulations:** The regulations imposed by the state on the quantum, pricing etc. of capital funds to be raised also influences the capital raised by a firm. For instance, restrictions have been imposed by SEBI on the issue and allotment of shares and bonds to different type of investors. A finance manager should take this factor into consideration while designing the capital structure.

5. **Credit Policy:** The credit policy pronouncements made by the central monetary authority, such as the RBI, affects the way capital is raised in the market. For instance, the interest rate liberalization announced by RBI has been dominating the lending policies of financial institutions. This affects the ability of finance managers to raise the required funds.

6. **Financial Institutions:** The credit policy followed by financial institutions determines the capital structure decisions of firms. For instance, restrictive lending terms by financial

institutions may deter firms from raising long-term funds at reasonable rates of interest. Easy terms, on the other hand, may encourage firms to obtain a higher quantum of loans.

CAPITAL MARKET INSTRUMENTS

Financial instruments that are used for raising capital resources in the capital market are known as Capital Market Instruments. The changes that are sweeping across the Indian capital market especially in the recent past are something phenomenal. It has been experiencing metamorphic in the last decade, thanks to a host of measures of liberalization, globalization, and privatization that have been initiated by the Government. Pronounced changes have occurred in the realm of industrial policy. Licensing policy, financial services industry, interest rates, etc. The competition has become very intense and real in both industrial sector and financial services industry. As a result of these changes, the financial services industry has come to introduce a number of instruments with a view to facilitate borrowing and lending of money in the capital market by the participants.

Types of Capital Market Instruments The various capital market instruments used by corporate entities for raising resources are as follows: 1. Preference shares 2. Equity shares 3. Non-voting equity shares 4. Cumulative convertible preference shares 5. Company fixed deposits 6. Warrants 7. Debentures and Bonds

1. PREFERENCE SHARES: Shares that carry preferential rights in comparison with ordinary shares are called Preference Shares regardingpayment. The dividend and the distribution of the assets of the company in the event of its winding up, in preference to equity shares.

Types of Preference Shares

1. Cumulative preference shares: Shares where the arrears of dividends in times of no and/or lean profits can be accumulated and paid in the year in which the company earns good profits.

2. Non-cumulative preference shares: Shares where the carry forward of the arrears of dividends is not possible.

3. Participating preference shares: Shares that enjoy the right to participate in surplus profits or surplus assets on the liquidation of a company or in both, if the Articles of Association provides for it.

4. Redeemable preference shares: Shares that are to be repaid at the end of the term of issue, the maximum period of a redemption being 20 years with effect from 1.3.1997 under the Companies amendment Act 1996. Since they are repayable, they are similar to debentures. Only fully paid shares are redeemed. Where redemption is made out of profits, a Capital Redemption Reserve Account is opened to which a sum equal to the nominal value of the shares redeemed is transferred. It is treated as paid-up share capital of the company.

Fully convertible cumulative preference shares: Shares comprise two parts viz., Part A and B. Part A is convertible into equity shares automatically and compulsorily on the date of allotment. Part B will be redeemed at par/converted into equity shares after a lock-in period at the option of the investor, conversion into equity shares taking place after the lock-in period, at a price, which would be 30 percent lower than the average market price. The average market price shall be the average of the monthly high and low price of the shares in a stock exchange over a period of 6 months including the month in which the conversion takes place.

6. Preference shares with warrants attached: The attached warrants entitle the holder to applyfor equity shares for cash, at a premium, at any time, and fifth year from the date of allotment. If the warrant holder fails to exercise his option, the unsubscribed portion will lapse. The holders of warrants would be entitled to all rights/bonus shares that may be issued by the company. The preference shares with warrants attached would not be transferred/sold for a period of 3 years from the date of allotment.

2. EQUITY SHARES:

Equity shares, also known as „ordinary shares are the shares held by the owners of a corporate entity. Since equity shareholders face greater risks and have no specified preferential rights, they are given larger share in profits through higher dividends than those given to preference shareholders, provided the companys performance is ex dividends in case there are no profits or the profits do not justify dividend for previous years even when the company makes substantial profits in subsequent years. Equity shareholders also enjoy the benefit of ploughing back of undistributed profits kept as reserves and surplus for the purposes of business expansion. Often, part of these is distributed to them, as bonus shares. Such bonus shares are entitled to a proportionate or full dividend in the succeeding year. A strikingly noteworthy feature of equity shares is that holders of these shares enjoy substantial rights in the corporate democracy, namely the rights to app of dividend, enhancement of managerial remuneration in excess of specified limits and fixing the terms of appointment and election of directors, appointment of auditors and fixing of their remuneration, amendments to the Articles and Memorandum of Association, increase of share capital and issue of further shares or debentures, proposals for mergers and reconstruction and any other important proposal on which members approval is required under the Companies Act. Equity shares in the hands of shareholders are mainly reckoned for determining the managements control over the company. Where for the management to retain the control, as it is not possible for all the shareholders to attend the company's meeting in full strength. Furthermore, the management group can bolster its controlling power by acquiring further shares in the open market or otherwise. Equity shares may also be offered to financial institutions as part of the private placement exercise. Such a method, however, is brought with the danger of takeover attempt by financial institutions. Equity shareholders represent proportionate ownership in a company. They have residual claims on the assets and profits of the company. They have unlimited potential for dividend payments and price appreciation in comparison to these owners of debentures and preference shares who enjoy just a fixed assured return in the form of interest and dividend. Higher the risk, higher the return and

vice-versa. Share certificates either in physical form or in the demat (with the introduction of depository system in 1999) form are issued as a proof of ownership of the shares in a company. Fully paid equity shares with detachable warrants entitle the warrant holder to apply for a specified number of shares at a determined price. Detachable warrants are separately registered with stock exchange and traded separately. The company would determine the terms and conditions relating to the issue of equity against warrants. Voting rights are granted under the Companies Act (Sections 87 to 89) wherein each shareholder is eligible for votes proportionate to the number of shares held or the amount of stock owned. A company cannot issue shares carrying disproportionate voting rights. Similarly, voting right cannot be exercised in respect of shares on which the shareholder owes some money to the company.

Capital Equity shares are of different types. The maximum value of shares as specified in the Memorandum of Association of the company is called the authorized or registered or nominal capital. Issued capital is the nominal value of shares offered for public subscription. In case shares offered for public subscription are not taken up, the portion of capital subscribed is called subscribed capital. This is less than the issued capital Paid-up capital is the share capital paid-up by shareowners which is credited as paid-up on the shares.

Par Value and Book Value

The face value of a share is called its Par value. Although shares can be sold below the par value, it is possible that shares can be issued below the par value. The financial institutions that convert their unpaid principal and interest into equity in sick companies are compelled to do if at a minimum of Rs.10 because of the par value concept even though the market price might be much less than Rs.10. Par value can also lead to unhealthy practices like price rigging by promoters of sick companies to take market prices above Rs.10 to get their new offers subscribed. Par value is of use to the regulatory agency and the stock exchange. It can be used to control the number of shares that can be issued by the company. The par value of Rs.10 per share serves as a floor price for issue of shares. Book value is the intrinsic value of a share that is calculated to reflect the net worth of the shareholders of a corporate entity. **Cash Dividends** These are dividends paid in cash. A stable payment of cash dividend is the hallmark of stability of share prices.
Stock Dividends These are the dividends distributed as shares and issued by capitalizing reserves. While net worth remains the same in the balance sheet, its distribution between shares and surplus is altered.

3. NON-VOTING EQUITY SHARES

Consequent to the recommendations of the Abi amendment to the Companies Act, corporate managements are permitted to mobilize additional capital without diluting the interest of existing shareholders with the help of a new instrument called non-voting equity shares. Such shares will be entitled to all the benefits except the right to vote in general meetings. Such non-voting equity share is being considered as a possible addition to the two classes of

share capital currently in vogue. This class of shares has been included by an amendment to the Companies Act as a third category of shares. Corporates will be permitted to issue such share up to a certain percentage of the total share capital. Non-voting equity shares will be entitled to rights and bonus issues and preferential offer of shares on the same lines as that of ordinary shares. The objective will be to compensate the sacrifice made for the voting rights. For this purpose, these shares will carry higher dividend rate than that of voting shares. If a company fails to pay dividend, non-voting shareholders will automatically be entitled to voting rights on a prorate basis until the company resumes paying dividend. The mechanism of issue of non-voting shares is expected to overcome such problems as are associated with the voting shares as that the ordinary investors are more inclined towards high return on capital through sizeable dividends and capital appreciation through the issue of bonus shares and the inability of corporate to respond to the investors just aspiration for reasonable dividends. Moreover, there is every need for corporate to spend huge sums of money on a variety of not-so useful items including colourful and costly annual reports. For all these above-mentioned reasons, non-voting equity shares are expected to have a ready and popular marker. In effect, this kind of share is similar to preference shares with regard to non-voting right but may get the advantage of higher dividends as well as appreciation in share values through entitlement to bonus shares which is not available to preference shares.

4. CONVERTIBLE CUMULATIVE PREFERENCE SHARES (CCPS)

These are the shares that have the twin advantage of accumulation of arrears of dividends and the conversion into equity shares. Such shares would have to be the face value of Rs.100 each. The shares have to be listed on one or more stock exchanges in the country. The object of the issue of CCP shares is to allow for the setting up of new projects, expansion or diversification ofexistingprojects, normal capital expenditure for modernization and for meeting working capital

requirements. Following are some of the terms and conditions of the issue of CCP shares :

1. Debt-equity ratio: For the purpose of calculation of debt-equity ratio as may be applicable CCPS is be deemed to be an equity issue.

2. Compulsory conversion: The conversion into equity shares must be for the entire issue of CCP shares and shall be done between the periods at the end of three years and five years as may be decided by the company. This implies that the conversion of the CCP into equity shares would be compulsory at the end of five years and the aforesaid preference shares would not be redeemable at any stage.

3. Fresh issue: The conversion of CCP shares into equity would be deemed as being one resulting from the process of redemption of the preference shares out of the proceeds of a fresh issue of shares made for the purposes of redemption.

4. Preference dividend: The rate of preference dividend payable on CCP shares would be 10 percent.

5. Guideline ratio: The guideline ratio of 1:3 as between preference shares and equity shares would not be applicable to these shares.

6. Arrears of dividend: The right to receive arrears of dividend up to the date of conversion, if any, shall devolve on the holder of the equity shares on such conversion. The holder of the equity shares shall be entitled to receive the arrears of dividend as and when the company makes profit and is able to declare such dividend.

7. Voting right: CCPS would have voting rights as applicable to preference shares under the companies Act, 1956.

8. Quantum: The amount of the issue of CCP shares would be to the extent the company would be offering equity shares to the public for subscription.

5. COMPANY FIXED DEPOSITS:

Fixed deposits are the attractive source of short-term capital both for the companies and investors as well. Corporates favour fixed deposits as an ideal form of working capital mobilization without going through the process of mortgaging assets. Investors find fixed deposits a simple avenue for investment in popular companies at attractively reasonable and safe interest rates. Moreover, investors are relieved of the problem of the hassles of market value fluctuation to which instruments such as shares and debentures are exposed. There are no transfer formalities either. In addition, it is quite possible for investors to have the option of premature repayment after 6 months, although such an option entails some interest loss.

Regulations Since these instruments are unsecured; there is a lot of uncertainty about the repayment of deposits and regular payment of interest. The issue of fixed deposits is subject to the provisions of the Companies Act and the Companies (Acceptance of Deposits) Rules introduced in February 1975. Some of the important regulations are:

1. Advertisement: Issue of an advertisement as approved by the Board of Directors in dailies circulating in the state of incorporation.

2. Liquid assets: Maintenance of liquid assets equal to 15 percent (substituted for 10% by Amendment Rules, 1992) of deposits (maturing during the year ending March 31) in the form of bank deposits, unencumbered securities of State and Central Governments or unencumbered approved securities.

3. Disclosure: Disclosure in the newspaper advertisement the quantum of deposits remaining unpaid after maturity. This would help highlight the defaults, if any, by the company and caution the depositors.

4. Deemed public Company: Private company would become a deemed public company (from June 1998, Section 43A of the Act) where such a private company, after inviting public deposits through a statutory advertisement, accepts or renews deposits from the public other than its members, directors or their relatives. This provision, to a certain extent, enjoins better accountability on the part of the management and auditors.

5. Default: Penalty under the law for default by companies in repaying deposits as and when they mature for payment where deposits were accepted in accordance with the Reserve Bank directions.

6. CLB: Empowerment to the Company Law Board to direct companies to repay deposits, which have not been repaid as per the terms and conditions governing such deposits, within a time frame and according to the terms and conditions of the order.

7. WARRANTS

An option issued by a company whereby the buyer is granted the right to purchase a number of shares of its equity share capital at a given exercise price during a given period is called a 'warrant'. Although trading stockmarketsfor morein warrant than 6 to 7 decades, they are being issued to meet a range of financial requirements by the Indian corporate. A security issued by a company, granting its holder the right to purchase a specified the Indian context are called sweetenersand were issued by a few Indian companies since 1993. Both warrants and rights entitle a buyer to acquire equity shares of the issuing company. However, they are different in the sense that warrants have a life span of three to five years whereas; rights have a life span of only four to twelve weeks (duration between the opening and closing date of subscription list). Moreover, rights are normally issued to effect current financing, and warrants are sold to facilitate future financing. Similarly, the exercise price of warrant, i.e. The price at which it can be exchanged for share, is usually above the market price of the share so as to encourage existing shareholders to purchase it. On the other hand, one warrant buys one equity share generally, whereas more than one rights may be needed to buy one share. The detachable warrant attached to each share provides a right to the warrant holder to apply for additional equity share against each warrant.

8. DEBENTURES AND BONDS

A document that either creates a debt or acknowledges it is known as a debenture. Accordingly, any document that fulfills either of these conditions is a debenture. A debenture, issued under the common seal of the company, usually takes the form of a certificate that acknowledges indebtedness of the company. A document that shows on the face of it that a company has borrowed a sum of money from the holder thereof upon certain terms and conditions is called a debenture. Debentures may be secured by way of fixed or floating

charges on the assets of the company. These are the instruments that are generally used for raising long-term debt capital.

Following are the features of a debenture

1. **Issue:** In India, debentures of various kinds are issued by the corporate bodies, Government, and others as per the provisions of the Companies Act, 1956 and under the regulations of the SEBI. Section 117 of the Companies Act prohibits issue of debentures with voting rights. Generally, they are issued against a charge on the assets of the company but at times may be issued without any such charge also. Debentures can be issued at a discount in which case, the relevant particulars are to be filed with the Registrar of Companies.

2. **Negotiability:** In the case of bearer debentures the terminal value is payable to its bearer. Such instruments are negotiable and are transferable by delivery. Registered debentures are payable to the registered holder whose name appears both on the debenture and in the register of debenture holders maintained by the company. Further, transfer of such debentures should be registered. They are not negotiable instruments and contain a commitment to pay the principal and interest.

3. Security: Secured debentures create a charge on the assets of the company. Such a charge may be either fixed or floating. Debentures that are issued without any charge on assets of the company are called 'unsecured or marked debentures.

4. **Duration:** Debentures, which could be redeemed after a certain period of time are called Redeemable Debentures. There are debentures that are not to be returned except at the time of winding up of the company. Such debentures are called Irredeemable Debentures.

5. **Convertibility:** Where the debenture issue gives the option of conversion into equity shares after the expiry of a certain period of time, such debentures are called Convertible Debentures. Non-convertible Debentures, on the other hand, do not have such an exchange facility.

6. **Return:** Debentures have a great advantage in them in that they carry a regular and reasonable income for the holders. There is a legal obligation for the company to make payment of interest on debentures whether or not any profits are earned by it.

7. **Claims:** Debenture holders command a preferential treatment in the matters of distribution of the final proceeds of the company at the time of its winding up. Their claims rank prior to the claims of preference and equity shareholders.

KINDS OF DEBENTURES

Innovative debt instruments that are issued by the public limited companies are described below: 1. Participating debentures 2. Convertible debentures. 3. Debt-equity swaps 4. Zero-coupon convertible notes 5. Secured Premium Notes (SPN) with detachable warrants 6. Non-Convertible Debentures (NCDs) with detachable equity warrant 7. Zero-interest Fully Convertible Debentures (FCDs) 8. Secured zero-interest Partly Convertible Debentures (PCDs) with detachable and separately tradable warrants 9. Fully Convertible Debentures (FCDs) with interest (optional) 10. Floating Rate Bonds (FRB)

1. Participating debentures: Debentures that are issued by a body corporate which entitle the holders to participate in its profits are cal corporate debt securities. They are popular among existing dividend paying Corporates.

2. Convertible debentures

a. Convertible debentures with options are a derivative of convertible debentures that give an option to both the issuer, as well as the investor, to exit from the terms of the issue. The coupon rate is specified at the time of issue.

b. Third party convertible debentures are debts with a warrant that allow the investor to subscribe to the equity of a third firm at a preferential price vis-à-vis market price, the interest rate on the third party convertible debentures being lower than pure debt on account of the conversion option.

c. Convertible debentures redeemable at a premium:

Premium are issued at face value with a put option entitling investors to sell the bond to the issuer, at a premium later on. They are basically similar to convertible debentures but have less risk.

3. Debt-equity swaps:

They are offered from an issue of debt to swap it for equity. The instrument is quite risky for the investor because the anticipated capital appreciation may not materialize.

4. Zero-coupon convertible note:

These are debentures that can be converted into shares and on its conversion the investor forgoes all accrued and unpaid interest. The zero-coupon convertible notes are quite sensitive to changes in the interest rates.

5. SPN with detachable warrants:

These are the Secured Premium Notes (SPN) with detachable warrants. These are the redeemable debentures that are issued along with a detachable warrant. The warrant entitles

the holder to apply and get equity shares allotted, provided the SPN is fully paid. The warrants attached to it assure the holder such a right. No interest will be paid during the lock-in period for SPN. The SPN holder has an option to sell back the SPN to the company at par value after the lock-in period. If this option is exercised by the holder, no interest/premium will be paid on redemption. The holder will be repaid the principal and the additional interest/ premium amount in instalments as may be decided by the company. The conversion of detachable warrant into equity shares will have to be done within the time limit notified by the company.

6. NCDs with detachable equity warrants:

These are Non-Convertible Debentures (NCDs) with detachable equity warrants. These entitle the holder to buy a specific number of shares from the company at a predetermined price within a definite time frame. The warrants attached to NCDEs are issued subject to full payment of the NCDs value. The option can be exercised after the specific lock-in period. The company is at liberty to dispose of the unapplied portion of shares if the option to apply for equalities is not exercised.

7. Zero interest FCDs:

These are Zero-interest Fully Convertible Debentures on which no interest will be paid by the issuer during the lock-in period. However, there is a notified period after which fully paid FCDs will be automatically and compulsorily converted into shares. In the event of a company going in for rights issue prior to the allotment of equity (resulting from the conversion of equity shares into FCDs), it shall do so only after the FCD holders are offered securities.

8. Secured Zero interest PCDs with detachable and separately tradable warrants:

These are Secured Zero Interest Partly Convertible Debentures with detachable and separately tradable warrants. They are issued in two parts. Part A is a convertible portion that allows equity shares to be exchanged for debentures at a fixed amount on the date of allotment. Part B is a non-convertible portion to be redeemed at par at the end of a specific period from the date of allotment. Part B which carries a detachable and separately tradable warrant provides the warrant holder an option to received equity shares for every warrant held, at a price worked out by the company.

9. Fully Convertible Debentures (FCDs) with interest (optional):

These are the debentures that will not yield any interest for an initial short period after which the holder is given an option to apply for equities at a premium. No additional amount needs to be paid for this. The option has to be indicated in the application form itself. Interest on FCDs is payable at a determined rate from the date of first conversion to the date of second/final conversion and in lieu of it, equity shares will be issued.

10. Floating Rate Bonds (FRB"s):

These are the bonds where the yield is linked to a benchmark interest rate like the prime rate in USA or LIBOR in the Euro currency market. For instance, the State Bank of India's floating rate bond, issue was linked to the maximum interest on term deposits that was 10 percent at the time. The floating rate is quoted in terms of a margin above of below the benchmark rate. Interest rates linked to the benchmark ensure that neither the borrower nor the lender suffer from the changes in interest rates. Where interest rates are fixed, they are likely to be inequitable to the borrower when interest rates fall and inequitable to the lender when interest rates rise subsequently.

SEBI Regulations on merchant bankers:

SEBI has brought about a effective regulative measures for the purpose of disciplining the functioning of the merchant bankers in India. The objective is to ensure an era of regulated financial markets and thus streamline the development of the capital market in India. The measures were introduced by the SEBI in the year 1992. The measures were revised by SEBI in 1997. The salient features of the regulative framework of merchant banking in India are discussed below.

Registration of Merchant Bankers Application for Grant of Certificate

An application by a person for grant of a certificate shall be made to the Board in Form A. The application shall be made for any one of the following categories of the merchant banker namely:

1. **Category I-** To carry on any activity of the issue management, which will inter alliance consist of preparation of prospectus and other information relating to the issue, determining financial structure, tie-up of financiers and final allotment and refund of the subscription; and to act as adviser, consultant, manager, underwriter, portfolio manager.

2. **Category II-** To act as adviser, consultant, co-manager, underwriter, portfolio manager.

3. **Category III-** To act as underwriter, adviser, consultant to an issue.

4. **Category IV-** To act only as adviser or consultant to an issue. **5.** With effect from 9th December, 1997, an application can be made only for carrying on the activities mentioned in category I. An applicant can carry on the activity as underwriter only if he contains separate certificate of registration under the provisions of Securities and Exchange Board of India (Underwriters) Regulations, 1993, and as portfolio manager only if he obtains separate certificate of registration under the provisions of Securities and Exchange Board of India (Portfolio Manager) Regulations, 1993.

5. **Conformance to Requirements** Subject to the provisions of the regulations, any application, which not complete in all respects and does not conform to the instructions specified in the form, shall be rejected. However, before rejecting any such application, the applicant will be given an opportunity to remove within the time specified such objections and may be indicated by the board.

6. **Furnishing of Information** The Board may require the applicant to furnish further information or clarification regarding matter relevant to the activity of a merchant banker for the purpose of disposal of the application. The applicant or its principal officer shall, if so required, appear before the Board for personal representation.

7. **Consideration of Application**: The Board shall take into account for considering the grant of a certificate, all matters, which are relevant to the activities relating to merchant bankerandinparticularwhethertheapplicantcomplieswith the following requirements;

1. That the applicant shall be a body corporate other than a non-banking financial company as defined by the Reserve Bank of India Act, 1934.

2. That the merchant banker who has been granted registration by the Reserve Bank of India to act as Primary or Satellite Dealer may carry on such activity subject to the condition that it shall not accept or hold public deposit.

3. That the applicant has the necessary infrastructure like adequate office space, equipments, and manpower to effectively discharge his activities.

4. That the applicant has in his employment minimum of two persons who have the experience to conduct the business of the merchant banker.

5. That a person (any person being an associate, subsidiary, inter-connected or group Company of the applicant in case of the applicant being a body corporate) directly orindirectly connected with the applicant has not been granted registration by the Board.

6. That the applicant fulfils the capital adequacy as specified.

7. That the applicant, his partner, director or principal officer is not involved in any litigation connected with the securities market which has an adverse bearing on the business of the applicant.

8. That the applicant, his director, partner or principal officer has not at any time been convicted for any offence involving moral turpitude or has been found guilty of any economic offence.

9. That the applicant has the professional qualification from an institution recognized by the Government in finance, law or business management.

10. That the applicant is a fit and proper person.

11. That the grant of certificate to the applicant is in the interest of investors.

8.Capital Adequacy Requirement According to the regulations, the capital adequacy requirement shall not be less than the net worth of the person making the application for grant of registration. For this purpose, the net worth shall be as follows:

Category	**Minimum Amount**
Category I	Rs.5, 00, 00,000
Category II	Rs.50, 00,000
Category III	Rs.20, 00,000
Category IV	Nil

For the purpose of this regulation _net worth means in the partnership firm or a body corporate, the value of the capital contributed to the business of such firm or the paid up capital of such body corporate plus free reserves as the case may be at the time of making application.

Procedure for Registration The Board on being satisfied that the applicant is eligible shall
grant a certificate in Form B. On the grant of a certificate the applicant shall be liable to pay the fees in accordance with Schedule II.

Renewal of Certificate Three months before expiry of the period of certificate, the merchant banker, may if he so desired, make an application for renewal in Form A. The application for renewal shall be dealt with in the same manner as if it were a fresh application for grant of a certificate. In case of an application for renewal of certificate of registration, the provisions of clause (a) of regulation 6 shall not be applicable up to June 30th, 1998. The Board on being satisfied that the applicant is eligible for renewal of certificate shall grant a certificate in form B and send intimation to the applicant. On the grant of a certificate the applicant shall be liable to pay the fees in accordance with Schedule II.

Procedure where Registration is not granted:

Where an application for grant of a certificate under regulation 3 or of renewal under regulation 9, does not satisfy the criteria set out in regulation 6, the Board may reject the application after giving an opportunity of being heard. The refusal to grant registration shall be communicated by the Board within thirty days of such refusal to the applicant stating therein the grounds on which the application has been rejected. Any applicant may, being aggrieved by the decision of the Board, under sub regulation (1), apply within a period of thirty days from the date of receipt of such intimation to the Board for reconsideration for its

decision. The Board shall reconsider an application made under sub-regulation (3) and communicate its decision as soon as possible in writing to the applicant.

Effect of Refusal to Grant Certificate:

Any merchant banker whose application for a certificate has been refused by the Board shall on and from the date of the receipt of the communication under sub-regulation (2) of regulation 10 cease to carry on any activity as merchant banker.

Payment of Fees Every applicant eligible for grant of a certificate shall pay such fees in such manner and within the period specified in Schedule II. Where a merchant banker fails to any annual fees as provided in sub-regulation (1), read with Schedule II, the Board may suspend the registration certificate, whereupon the merchant banker shall cease to carry on any activity as a merchant banker for the period during which the suspension subsists.

CODE OF CONDUCT FOR MERCHANT BANKERS

The SEBI regulations have outlined the following code of conduct for the merchant bankers operation in India;

- A merchant banker shall make all efforts to protect the interests of investors.
- A Merchant Banker shall maintain high standards of integrity, dignity and fairness in the conduct of its business.
- A Merchant Banker shall fulfill its obligations in a prompt, ethical, and professional manner.
- A Merchant Banker shall at all times exercise due diligence, ensure proper care and exercise independent professional judgment.
- A Merchant Banker shall Endeavour to ensure that enquiries from the investors are adequately dealt with, grievances of investors are redressed in a timely and appropriate manner, where a complaint is not remedied promptly, the investor is advised of any further steps which may be available to the investor under the regulatory system.
- A Merchant Banker shall ensure that adequate disclosures are made to the investors in a timely manner in accordance with the applicable regulations and guidelines so as to enable them to make a balanced and informed decision.
- A Merchant Banker shall endeavor to ensure that the investors are provided with true and adequate information without making any misleading or exaggerated claims or any misrepresentation and are made aware of the attendant risks before taking any investment decision.
- A Merchant Banker shall endeavor to ensure that copies of the prospectus, offer document, letter of offer or any other related literature is made available to the investors at the time of issue of the offer.
- A Merchant Banker shall not discriminate amongst its clients, save and except on ethical and commercial considerations.

• A Merchant Banker shall not make any statement, either oral or written, which would misrepresent the services that the Merchant Banker is capable of performing for any client or has rendered to any client.
• A Merchant Banker shall avoid conflict of interest and make adequate disclosure of its interest. • A Merchant Banker shall put in place a mechanism to resolve any conflict of interest situation that may arise in the conduct of its business or where any conflict of interest arises, shall take reasonable steps to resolve the same in an equitable manner.
• Merchant Banker shall make appropriate disclosure to the client of its possible source or potential areas of conflict of duties and interest while acting as Merchant Banker which would impair its ability to render fair, objective and unbiased services.
• A Merchant Banker shall always endeavor to render the best possible advice to the clients having regard to their needs.
• A Merchant Banker shall not divulge to anybody either oral or in writing, directly or indirectly, any confidential information about its clients which has come to its knowledge, without taking prior permission of its client, except where such disclosures are required to be made in compliance with any law for the time being in force.
• A Merchant Banker shall ensure that any change in registration status/any penal action taken by the Board or any material change in the Merchant Banker_s financial status, which may adversely affect the interests of clients/investors is promptly informed to the clients and any business remaining outstanding is transferred to another registered intermediary in accordance with any instructions of the affected clients.
• A Merchant Banker shall not indulge in any unfair competition, such as weaning away the clients on assurance of higher premium or advantageous offer price or which is likely to harm the interests of other Merchant Bankers or investors or is likely to place such other Merchant Bankers in a disadvantageous position while competing for or executing any assignment.
• A Merchant Banker shall maintain arms length relationship between its merchant banking activity and any other activity.
• A Merchant Banker shall have internal control procedures and financial and operational capabilities which can be reasonably expected to protect its operations, its clients, investors and other registered entities from financial loss arising from theft, fraud, and other dishonest acts, professional misconduct or omissions.
• A Merchant Banker shall not make untrue statement or suppress any material fact in any documents, reports or information furnished to the Board.
• A Merchant Bankers shall maintain an appropriate level of knowledge and competence and abide by the provisions of the Act, regulations made there under, circulars and guidance, which may be applicable and relevant to the activities carried on by it. The merchant banker shall also comply with the award of the Ombudsman passed under Securities and Exchange Board of India (Ombudsman) Regulations, 2003.
• A Merchant Banker shall ensure that the Board is promptly informed about any action, legal proceedings etc., initiated against it in respect of material breach or non-compliance by it, of any law, rules, regulations, directions of the Board or of any other regulatory body.

• A Merchant Banker or any of its employers shall not render, directly or indirectly, any investment advice about any security in any publicly accessible media, whether real-time , unless a disclosure of his interest including a long or short position, in the said security has been made, while rendering such advice. In the event of an employee of the Merchant Banker rendering such advice, the merchant banker shall ensure that such employee shall also disclose the interests, if any, of himself, his dependent family members including their long or short position in the said security, while rendering such advice.
• A Merchant Banker shall demarcate the responsibilities of the various intermediaries appointed by it clearly so as to avoid any conflict or confusion in their job description.
• A Merchant Banker shall provide adequate freedom and powers to its compliance officer for the effective discharge of the compliance officer_s duties.
• A Merchant Banker shall develop its own internal code of conduct for governing its internal operations and laying down its standards of appropriate conduct for its employees and officers in carrying out their duties. Such a code may extend to the maintenance of professional excellence and standards, integrity, confidentiality, objectivity, avoidance or resolution of conflict of interests, disclosure of shareholdings and interests etc.
• A Merchant Banker shall ensure that good corporate policies and corporate governance are in place.
• A Merchant Banker shall ensure that any person it employs or appoints to conduct business is fit and proper and otherwise qualified to act in the capacity so employed or appointed
• A Merchant Banker shall ensure that it has adequate resources to supervise diligently and does supervise diligently persons employed if appointed by it in the conduct of its business, in respect of dealings in securities market.
• A Merchant Banker shall be responsible for the acts or omissions of its employees and agents in respect of the conduct of its business.
• A Merchant Banker shall ensure that the senior management, particularly decision makers have access to all relevant information about the business on a timely basis.
• A Merchant Banker shall not be a party to or instrumental for creation of false market; price rigging or manipulation; or passing of unpublished price sensitive information in respect of securities which are listed and proposed to be listed in any stock exchange to any person or intermediary in the securities market.

UNIT 2

PUBLIC ISSUE MANAGEMENT

Classification of Securities Issue

1. Public Issue

2. Right Issue

3. Private Placement

Decision to Raise Capital Funds Preparation and Finalization of Prospectus Obtaining SEBI Approval Arranging underwriting Selection of Registrars, Brokers, Bankers, etc. Printing and Publicity of Public Issue Documents Arranging Press for investor Conference Issue Launch SEBI Compliance

1. Public Issue of Securities When capital funds are raised through the issue of a prospectus, itis called ‘‘public issue of securities’. It capital market. A security issue may take place either at part, or at a premium or at a discount.

The Prospectus has to disclose all the essential facts about the company to the prospective purchasers of the shares. Further, the prospectus must conform to the formal set out in Schedule II of the Companies Act, 1956, besides taking into the account SEBI guidelines. SEBI insists on the adequacy of disclosure of information that should serve as the basis for investors to make a decision about the investment of their money.

2. Rights Issue When shares are issued to the existing shareholders of a company on a privileged basis, it is called as ‘Rights Issue. The subscribe to the new issue of shares. Rights shares are offered as additional issues by corporate to mop up further capital funds. Such shares are offered in proportion to the capital paid up on the shares held by them at the time of the offer. It is to be noted that the shareholders, although privileged to be offered on the issue, are under no legal obligation to accept the offer. Right shares are usually offered on terms advantageous to the shareholders.

3. Private Placement When the issuing company sells securities directly to the investors, especially institutional investors; it takes the form of private placement. In this case, no prospectus is issued, since it is presumed that the investors have sufficient knowledge and experience and are capable of evaluating the risks of the investment. Private placement covers shares, preference shares and debentures. The role of the financial intermediary, such as the merchant bankers and lead managers, assures great significance in private placement. They involve themselves in the task of preparing an offer memorandum and negotiating with investors.

BANKERS TO AN ISSUE

The bankers to an issue are engaged in activities such as acceptance of applications along with application money from the investors in respect of issues of capital and refund of application money.

Registration

To carry on activity as a banker to issue, a person must obtain a certificate of registration from the SEBI. The SEBI grants registration on the basis of all the activities relating to banker to an issue in particular with reference to the following requirements: a) The applicant has the necessary infrastructure, communication and data processing facilities and manpower to effectively discharge his activities, b) The applicant/any of the directors of the applicant is not involved in any litigation connected with the securities market/has not been convicted of any economic offence; c) The applicant is a scheduled bank and d) Grant of a certificate is in the interest of the investors. A banker to an issue can apply for the renewal of his registration three months before the expiry of the certificate. Every banker to an issue had to pay to the SEBI an annual fee of Rs.2.5 lakhs for the first two years from the date of initial registration, and Rs.1 lakh for the third year to keep his registration in force. The renewal fee to be paid by him annually for the first two years was Rs.1 lakh and Rs.20,000 for the third year. Since 1999, schedule of fee is Rs.5 lakhs as initial registration fee and Rs.2.5 lakhs renewal fee every three years from the fourth year from the date of initial registrations. Non-payment of the prescribed fee may lead to the suspension of the registration certificate.

General Obligations and Responsibilities Furnish INFORMATION

When required, a banker to an issue has to furnish to the SEBI the following information; a) The number of issues for which he was engaged as a banker to an issue; b) The number of application/details of the application money received, c) The dates on which applications from investors were forwarded to the issuing company /registrar to an issue; d) The dates/amount of refund to the investors.

Books of Account/Record/Documents

A banker to an issue is required to maintain books of accounts/records/documents for a minimum period of three years in respect of, inter-alia, the number of applications received, the names of the investors, the time within which the applications received were forwarded to the issuing company/registrar to the issue and dates and amounts of refund money to investors.

Disciplinary Action by the RBI

If the RBI takes any disciplinary action against a banker to an issue in relation to issue payment, the latter should immediately inform the SEBI. If the banker is prohibited from carrying on his activities as a result of the disciplinary action, the SEBI registration is automatically deemed as suspended/cancelled.

1 Code of Conduct for Bankers To Issue

A banker to an issue should:

1. Make all efforts to protect the interest of investors.

2. Observe high standards of integrity and fairness in the conduct of its business.

3. Fulfill its obligations in a prompt, ethical and professional manner.

4. At all times exercise due diligence, ensure proper care and exercise independent professional judgment

5. Not any time act in collusion with other intermediates over the issuer in a manner that is detrimental to the investor

6. Endeavour to ensure that a) inquiries from investors are adequately dealt with; b) grievances of investors are redressed in a timely and appropriate manner; c) where a complaint is not remedied promptly, the investor is advised of any further steps which may be available to the investor under the regulatory system.

7. Not a) Allow blank applications forms bearing brokers stamp to be kept the bank premises or peddled anywhere near the entrance of the premises; b) Accept applications after office hours or after the date of closure of the issue or on bank holidays; c) After the closure of the public issue accept any instruments such as Cheques/ demand drafts/stock invests from any other source other than the designated registrar to the issue; d) Part with the issue proceeds until listing permission is granted by the stock exchange to the body corporate; e) Delay in issuing the final certificate pertaining to the collection figures to the registrar to the issue, the lead manager and the body corporate and such figures should be submitted within seven working days from the issue closure date.

8. Be prompt in disbursing dividends, interests or any such accrual income received or collected by him on behalf of his clients.

9. Not make any exaggerated statement whether oral or written to the client, either about its qualification or capability to render certain services or its achievements in regard to services rendered to other client.

10. Always Endeavour to render the best possible advice to the clients having regard to the clients‘ needs and the environments and his own professional skill.

11. Not divulge to anybody either orally or in writing, directly or indirectly, any confidential information about its clients which has come to its knowledge, without taking prior permission of its clients

12. Avoid conflict of interest and make adequate disclosure of his interest.

13. Put in place a mechanism to resolve any conflict of interest situation that may arise in theconduct of its business or where any conflict of interest arise, should take reasonable steps to resolve the same in an equitable manner.

14.Make appropriate disclosure to the client of its possible source or potential areas of conflict of duties and interest while acting as banker to an issue which would impair its ability to render fair, objective and unbiased services.

15.Not indulge in any unfair competition, which is likely to harm the interests of other bankers to an issue or investors or is likely to place such other bankers to an issue in a disadvantageous position while competing for or executing any assignment.

16. Not discriminate amongst its clients, save and except on ethical and commercial considerations. 17. Ensure that any change in registration status/any penal action taken by the SEBI or any material change in financials which may adversely affect the interests of clients/ investors is promptly informed to the clients and business remaining outstanding is transferred to another registered person in accordance with any instructions of the affected clients/investors.

18.Maintain an appropriate level of knowledge and competency and abide by the provisions of the SEBI Act, regulations, circulars and guidelines of the SEBI. The banker to an issue should also comply with the award of the Ombudsman passed under the SEBI (Ombudsman) Regulations, 2003. 19. Ensure that the SEBI is promptly informed about any action, legal proceedings, etc., initiated against it in respect of any material breach of non-compliance by it, of any law, rules, regulations, and directions of the SEBI or of any other regulatory body.

20. Not make any untrue statement of suppress any material fact in any documents, reports, papers or information furnished to the SEBI.

21. Not neglect or fail or refuse to submit to the SEBI or other agencies with which it is registered, such books, documents, correspondence, and papers or any part thereof as may be demanded/requested from time to time.

22. Abide by the provisions of such acts and rules, regulations, guidelines, resolutions, notifications, directions, circulars and instructions as may be issued from time to time by the Central Government, relevant to the activities carried on the banker to an issue.

23. (a) Not render, directly or indirectly, any investment advice about any security in the publicly accessible media, whether real-time or non-real-time, unless a disclosure of its interest including long or short position in the security has been made, while rendering such advice; (b) in case an employee of the banker to an issue is rendering such advice, the banker to an issue should ensure that he discloses his interest, the interest of his dependent family members and that of theMake appropriate disclosure to the client of its

possible source or potential areas of conflict of duties and interest while acting as banker to an issue which would impair its ability to render fair, objective and unbiased services.

24.Not indulge in any unfair competition, which is likely to harm the interests of other bankers to an issue or investors or is likely to place such other bankers to an issue in a disadvantageous position while competing for or executing any assignment.

25. Not discriminate amongst its clients, save and except on ethical and commercial considerations. 17. Ensure that any change in registration status/any penal action taken by the SEBI or any material change in financials which may adversely affect the interests of clients/ investors is promptly informed to the clients and business remaining outstanding is transferred to another registered person in accordance with any instructions of the affected clients/investors.

26.Maintain an appropriate level of knowledge and competency and abide by the provisions of the SEBI Act, regulations, circulars and guidelines of the SEBI. The banker to an issue should also comply with the award of the Ombudsman passed under the SEBI (Ombudsman) Regulations, 2003. 19. Ensure that the SEBI is promptly informed about any action, legal proceedings, etc., initiated against it in respect of any material breach of non-compliance by it, of any law, rules, regulations, and directions of the SEBI or of any other regulatory body.

27. Not make any untrue statement of suppress any material fact in any documents, reports, papers or information furnished to the SEBI.

28. Not neglect or fail or refuse to submit to the SEBI or other agencies with which it is registered, such books, documents, correspondence, and papers or any part thereof as may be demanded/requested from time to time.

29. Abide by the provisions of such acts and rules, regulations, guidelines, resolutions, notifications, directions, circulars and instructions as may be issued from time to time by the Central Government, relevant to the activities carried on the banker to an issue.

30. (a) Not render, directly or indirectly, any investment advice about any security in the publicly accessible media, whether real-time or non-real-time, unless a disclosure of its interest including long or short position in the security has been made, while rendering such advice; (b) in case an employee of the banker to an issue is rendering such advice, the banker to an issue should ensure that he discloses his interest, the interest of his dependent family members and that of the employer including employer's long or short position in the security, while rendering such advice.

Inspection

Such inspection is done by the RBI upon the request of the SEBI. The purpose of inspection is largely to ensure that the required books of accounts are maintained and to investigate into the complaints received from the investors against the bankers to an issue. The foregoing rules and regulations have brought the bankers to an issue under the regulatory framework of the SEBI with a view to ensuring greater investor protection. On the basis of the inspection report, the SEBI can direct the banker to an issue to take such measures as it may deem fit in the interest of the securities market and for due compliance with the provision of the SEBI Act.

Action In Case of Default

With a view to ensure effective regulation of the activities of the bankers to an issue, the SEBI is empowered to suspend/cancel their registration certificate. The grounds of suspension are: a) The banker violates the provisions of the SEBI Act, rules/regulations; b) Fails to/does not furnish the required information or furnishes wrong/false information; c) Fails to resolve investor complaints/to give satisfactory reply to SEBI; d) Is guilty of misconduct/unprofessional conduct inconsistent with the prescribed code of conduct; and e) Fails to pay fees and carry out his obligations as specified in the regulations. The SEBI can cancel registration in case of i. Repeated defaults leading to suspension of a banker, ii. The deterioration in is financial position which likely to adversely affect the interest of the investors, and iii. The being found guilty of fraud/convicted of a criminal offence.

Marketing of New Issues

Following are the steps involved in the marketing of the issue of securities to be undertaken by the lead manager:

1. Target market: The first step towards the successful marketing of securities is the identification of a target market segment where the securities can be offered for sale. This ensures smooth marketing of the issue. Further, it is possible to identify whether the market comprises of retail investors, wholesale investors or institutional investors.

2. Target concentration: After having chosen the target market for selling the securities, steps are to be taken to assess the maximum number of subscriptions that can be expected from the market. It would work to the advantage of the company if it concentrates on the regions where it is popular among prospective investors.

3. Pricing: After assessing market expectations, the kind and level of price to be charged for the security must be decided. Pricing of the issue also influences the design of capital

structure. The offer has to be made more attractive by including some unique features such as safety net, multiple options for conversion, attaching warrants, etc.

4. Mobilizing intermediaries: For successful marketing of public issues, it is important that efforts are made to enter into contracts with financial intermediaries such as an underwriter, broker/sub-broker, fund arranger, etc.

5. Information contents: Every effort should be mad3e to ensure that the offer document for issue is educative and contains maximum relevant information. Institutional investors and high net worth investors should also be provided with detailed research on the project, specifying its uniqueness and its advantage over other existing or upcoming projects in a similar field.

6. Launching advertisement campaign: In order to push the public issue, the lead manager should undertake a high voltage advertisement campaign. The advertising agency must be carefully selected for this purpose. The task of advertising the issue shall be entrusted to those agencies that specialize in launching capital offerings. The theme of the advertisement should be finalized keeping in view SEBI guidelines. An ideal mix of different advertisement vehicles such as the press, the radio and the television, the hoarding, etc. should be used. Press meets, brokers and investor's conference, etc. shall be arranged by the lead manager at targeted in carrying out opinion polls. These services would useful in collecting data on investors' opinion and reactions relating to the public issue of the company, such a task would help develop an appropriate marketing strategy. This is because; there are vast numbers of potential investors in semi-urban and rural areas. This calls for sustained efforts on the part of the company to educate them about the various avenues available for investment.

7. Brokers and investors conferences: As part of the issue campaign, the lead manager should arrange for brokers and investors conferee centre which have sufficient investor population. In order to make such endeavours more successful, advance planning is required. It is important that conference materials such as banners, brochures, application forms, posters, etc. reach the conference venue in time. In addition, invitation to all the important people, underwriters, bankers at the respective places, investors associations should also be sent.

8. A critical factor that could make or break the proposed pu8blic issue is its timing. The market conditions should be favourable. Otherwise, even issues from a company with an excellent track record, and whose shares are highly priced, might flop. Similarly, the number and frequency of issues should also be kept to a minimum to ensure success of the public issue.

OFFERS FOR SALE METHOD

Where the marketing of securities takes place through intermediaries, such as issue houses, stockbrokers and others, it is a case sale of securities takes place in two stages. Accordingly, in the first stage, the issuer company makes an end-block sale of securities to intermediaries such as the issue houses and share brokers at an agreed price. Under the second stage, the securities are re-sold to ultimate investors at a market-related price. The difference between the purchase price and the issue price constitutes profit for the intermediaries. The intermediaries are responsible for meeting various expenses such as underwriting commission, prospectus cost, advertisement expenses, etc. The issue is also underwritten to ensure total subscription of the issue. The biggest advantage of this method is that it saves the issuing company the hassles involved in selling the shares to the public directly through prospectus. This method is, however, expensive for the investor as it involves the offer of securities by issue houses at very high prices.

Brokers to The Issue

Brokers are the persons mainly concerned with the procurement of subscription to the issue from the prospective investors. The appointment of brokers is not compulsory and the companies are free to appoint any number of brokers. The managers to the issue and the official brokers organize the preliminary distribution of securities and procure direct subscriptions from as large or as wide a circle of investors as possible. The stock exchange bye-laws prohibits the members from the acting as managers or brokers to the issue and making preliminary arrangement in connection with any flotation or new issue, unless the stock exchange of which they are members gives its approval and the company conforms to the prescribed listing requirements and undertakes to have its securities listed on a recognized stock exchange. The permission granted by the stock exchange is also subject o other stipulations which are set out in the letter of consent. Their active assistance is indispensable for broad basing the issue and attracting investors. By and large, the leading merchant bankers in India who act as managers to the issue have particulars of the performance of brokers in the country. The company in consultation with the stock exchange writes to all active brokers of all exchanges and obtains their consent to act as brokers to the issue. Thereby, the entry of experienced and unknown agencies in to the field of new issue activity as issue managers, underwriters, brokers, and so on,isdiscouraged.

PRIVATE PLACEMENT METHOD

A method of marketing of securities whereby the issuer makes the offer of sale to individuals and institutions privately without the issue of a prospectus is known as 'Private Placement Method'. This is the most popular method gaining momentum in recent times among the corporate enterprises. Under this method, securities are offered directly to large buyers with the help of shares brokers. This method works whereby securities are first sold to intermediaries such as issues houses, etc. They are in turn placed at higher prices to individuals and institutions. Institutional investors play a significant role in the realm of private placing. The expenses relating to placement are borne by such investors.

Advantages

1. Less expensive as various types of costs associated with the issue are borne by the issue houses and other intermediaries.

2. Less troublesome for the issuer as there is not much of stock exchange requirements connecting contents of prospectus and its publicity etc. to be complied with.

3. Placement of securities suits the requirements of small companies.

4. The method is also resorted to when the stock market is dull and the public response to the issue is doubtful.

Disadvantages

1. Concentration of securities in a few hands. 2. Creating artificial scarcity for the securities thus jacking up the prices temporarily and misleading general public. 3. Depriving the common investors of an opportunity to subscribe to the issue, thus affecting their confidence levels.

INTIAL PUBLIC OFFER (IPO) METHOD

The public issue made by a corporate entity for the first time in its life is called 'Initial Public Offer'(IPO). Under this method of marketing, securities are issued to successful applicants on the basis of the orders placed by them, through their brokers. When a company whose stock is not publicly traded wants to offer that stock to the general public, it takes the form of 'Initial Public Offer'. The job of selling the stock is entrusted to a popular intermediary, the underwriter. An underwriter is invariably an investment banking company. He agrees to pay the issuer a certain price for a minimum number of shares, and then resells those shares to buyers, who are often the clients of the underwriting firm. The underwriters charge a fee for their services. Stocks are issued to the underwriter after the issue of prospectus which provides details of financial and business information as regards the issuer. Stocks are then released to the underwriter and the underwriter releases the stock to the public. The issuer and the underwriting syndicate jointly determine the price of a new issue. The approximate price listed in the red herring (the preliminary prospectus – often with words in red letters which say this is preliminary and the price is not yet set) may or may not be close to the final issue price. IPO stock at the release price is usually not available to most of the public. Good relationship between the broker and the investor is a prerequisite for the stock being acquired. Full disclosure of all material information in connection with the offering of new securities must be made as part of the new offerings. A statement and preliminary prospectus (also known as a red herring) containing the following information is to be filed with the Registrar of Companies:
1. A description of the issuer's business

2. The names and addresses of the key company offers, with salary and a 5 year business history on each
3. The amount of ownership of the key officers
4. The company's capitalization and description of how the proceeds from the offering will be used and
5. Any legal proceedings that the company is involved in. Applications are made by the investors on the advice of their brokers who are intimated of the share allocation by the issuer. The amount becomes payable to the issuer through the broker only on final allocation. The allotment is credited and share certificates delivered to the depository account of the successful investor.

The **essential steps** involved in this method of marketing of securities are as follows:

a. **Order** Broker receives order from the client and places orders on behalf of the client with the issuer.

b. **Share allocation:** The issuer finalizes share allocation and informs the broker regarding the same**.** c. **The client:** The broker advises the successful clients of his share allocation Clients then submit the application forms for shares and make payment to the issuer through the broker.

d. **Primary issue account:** The issuer opens a separate escrow account (primary issue account) for the primary market issue. The clearing house of the exchange debits the primary issue account of the broker and credits the issuer's account.

e. Certificates: Certificates are then delivered to investors. Otherwise, depository account may be credited. The biggest advantage of this method of marketing of securities is that there is no need for the investors to part with the money even before the shares are allotted in his favour. Further, the method allows for elimination of unnecessary hassles involved in making a public issue. Under the regulations of the SEBI, IPOS can be carried out through the secondary market and the existing infrastructure of stock exchanges can be used for this purpose.

RIGHTS ISSUE METHOD

Where the shares of an existing company are offered to its existing shareholders, it takes the form of 'rights issue'. Under this method, the existing company issues shares to its existing shareholders in proportion to the number of shares already held by them. The relevant guidelines issued by the SEBI in this regard are as follows;

1. Shall be issued only by listed companies

2. Announcement regarding rights issue once made, shall not be withdrawn and where withdrawn, no security shall be eligible for listing up to 12 months

3. Underwriting as to rights issue is optional and appointment of Registrar is compulsory

4. Appointment of category I Merchant Bankers holding a certificate of registration issued by SEBI shall be compulsory

5. Rights shares shall be issued only in respect of fully paid shares

6. Letter of Offer shall contain disclosures as per SEBI requirements

7. Agreement shall be entered into with the depository for materialization of securities to be issued

8. Issue shall be kept open for a minimum period of 30 days and for a maximum period of 60 days

9. A minimum subscription of 90 percent of the issue shall be received

10. No reservation is allowed for rights issue as regards FCDs and PCDs

11. No Complaint CertificatetheLeadMerchanttobe Banfield21 days from the date of issueof offer document

12. Obligatory for a company where increase in subscribed capital is necessary after two years of its formation or after one year of its first issue of shares, whichever is earlier?

Advantages

Rights issue offers the following advantages:

1. Economy: Rights issue constitutes the most economical method of raising fresh capital, as it involves no underwriting and brokerage costs. Further, the expenses by way of advertisement and administration, etc. are less.

2. Easy: The issue management procedures connected with the rights issue are easier as only a limited number of applications are to be handled.

3.Advantage of shareholders: Issue of rights shares does not involve any dilution of ownership of existing shareholders. Further, it offers freedom to shareholders to subscribe or not to subscribe the issue.

Drawbacks

The method suffers from the following limitations:

1. Restrictive: The facility of rights issue is available only to existing companies and not to new companies.

2. Against society: The issue of rights shares runs counter to the overall societal considerations of diffusion of shares ownership for promoting dispersal of wealth and economic power.

Bonus Issues Method

Where the accumulated reserves and surplus of profits of a company are converted into paid up capital, it takes the form of issue of 'bonus shares'. It merely implies capitalization of exiting reserves and surplus of a company. The issue of bonus shares is subject to certain rules and regulations. The issue does not in any way affect the resources base of the enterprise. It saves the company enormously of the hassles of capital issue. Issued under Section 205 (3) of the Companies Act, such shares are governed by the guidelines issued by the SEBI (applicable to listed companies only) as follows:

SEBI Guidelines

Following are the guidelines pertaining to the issue of bonus shares by a listed corporate enterprise:

1. Reservation In respect of FCDs and PCDs, bonus shares must be reserved in proportion to such convertible part of FCDs and PCDs. The shares so reserved may be issued at the time of conversion(s) of such debentures on the same terms on which the bonus issues were made.

2. Reserves The bonus issue shall be made out of free reserves built out of the genuine profits or share premium collected in cash only. Reserves created by revaluation of fixed assets are not capitalized.

3. Dividend mode The declaration of bonus issue, in lieu of dividend, is not made

4. Fully paid The bonus issue is not made unless the partly paid shares, if any are made fully paid-up.

5. No default The Company has not defaulted in payment of interest or principal in respect of fixed deposits and interest on existing debentures or principal on redemption thereof and has sufficient reason to believe that it has not defaulted in respect of the payment of statutory dues of the employees such as contribution to provident fund, gratuity, bonus etc.

6. Implementation A company that announces its bonus issue after the approval of the Board of Directors must implement the proposal within a period of 6 months from the date of such approval and shall not have the option of changing the decision.

7. The articles The articles of Association of the company shall contain a provision for capitalization of reserves, etc. If there is no such provision in the Articles, the company shall pass a resolution at its general body meeting making provisions in the Articles of Associations for capitalization.

8. Resolution Consequent to the issue of bonus shares if the subscribed and paid-up capital exceeds the authorized share capital, the company at its general body meeting for increasing the authorized capital shall pass a resolution.

BOOK BUILDING METHOD

A method of marketing the shares of a company whereby the quantum and the price of the securities to be issued will be decided on the basis of the 'bids' received from the prospective shareholders by the lead merchant bankers is known as 'book-building method. Under the book-building method, share prices are determined on the basis of real demand for the shares at various price levels in the market. For discovering the price at which issue should be made, bids are invited from prospective investors from which the demand at various price levels is noted. The merchant bankers undertake full responsibility for the same. The option of book-building is available to all body corporate, which are otherwise eligible to make an issue of capital to the public. The initial minimum size of issue through book-building route was fixed at Rs.100 crores. However, beginning from December 9, 1996 issues of any size will be allowed through the book-building route. Book-building facility is available as an alternative to firm allotment. Accordingly, a company can opt for book-building route for the sale of shares to the extent of the percentage of the issue that can be reserved for firm allotment as per the prevailing SEBI guidelines. It is therefore possible either to reserve securities for firm allotment or issue them through the book-building process. The book-building process involves the following steps:

1. **Appointment of book-runners:**

The first step in the book-building process is the appointment by the issuer company, of the book-runner, chosen from one of the lead merchant bankers. The book-runner in turn forms a syndicate for the book-building. A syndicate member should be a member of National Stock Exchange (NSE) or Over-the-Counter Exchange of India (OTCEI). Offers of bids‘ are to be made by investors to the syndicate members, who register the demands of investors. The bid indicates the number of shares demanded and the prices offered. This information, which is stored in the computer, is accessible to the company management or to the book-runner. The name of the book-runner is to be mentioned in the draft prospectus submitted to SEBI.

2. Drafting prospectus:

The draft prospectus containing all the information except the information regarding the price at which the securities are offered is to be filed with SEBI as per the prevailing SEBI guidelines. The offer of securities through this process must separately be disclosed in the prospectus, under the caption ‘placement portion category’. Similarly, the extent of shares offered to the public shall be separately shown under the caption 'net offer to the public'. According to the latest SEBI guidelines issued in October 1999, the earlier stipulation that at least 25 percent of the securities were to be issued to the public has been done away with. This is aimed at enabling companies to offer the entire public issue through the book-building route.

3. Circulating draft prospectus

A copy of the draft prospectus filed with SEBI is to be circulated by the book-runner to the prospective institutional buyers who are eligible for firm allotment and also to the intermediaries who are eligible to act as underwriters. The objective is to invite offers for subscribing to the securities. The draft prospectus to be circulated must indicate the price band within which the securities are being offered for subscription.

4. Maintaining offer records:

The book-runner maintains a record of the offers received. Details such as the name and the number of securities ordered together with the price at which each institutional buyer or underwriter is willing to sub scribe to securities under the placement portion must find place in the record. SEBI has the right to inspect such records.

5. Intimation about aggregate orders:

The underwriters and the institutional investors shall give intimation on the aggregate ofthe offers received to the book-runner.

6. Bid analysis:

The bid analysis is carried out by the book-runner immediately after the closure of the bid offer date. An appropriate final price is arrived at after a careful evaluation of demands at various prices and the quantity. The final price is generally fixed reasonably lower than the possible offer price. This way, the success of the issue is ensured. The issuer company announce the pay-in-date at eh expiry of which shares are allotted.

7. Mandatory Underwriting:

Where it has been decided to make offer of shares to public under the category of 'Net Offer to the Public'; it is incumbent that underwritten. In case an issue is made through book-building route, it is mandatory that the portion of the issue offered to the public be underwritten. This is the purpose; an agreement has to be entered into with the underwriter by the issuer. The agreement shall specify the number of securities as well as the price at which the underwriter would subscribe to the securities. The book-runner may require the underwriter of the net offer to the public to pay in advance all moneys required to be paid in respect of their underwriting commitment.

8. Filling with ROC:

A copy of the prospectus as certified by the SEBI shall be filed with the Registrar ofCompanies within two days of the receipt of the acknowledgement card from the SEBI.

9. Bank accounts:

The issuer company has to open two separate accounts for collection of applicationmoney, one for the private placement portion and the other for the public subscription.

10. Collection of Completed Applications:

The book-runner collects from the institutional buyers and the underwriters theapplication forms along with the application money to the extent of the securities proposed to be allotted to them or subscribed by them. This is to be done one day before the opening of the issue to the public.

11. Allotment of securities:

Allotment for the private placement portion may be made on the second day from theclosure of the issue. The issuer company, however, has the option to choose one date for both the placement portion and the public portion. The said date shall be considered to be the date of allotment for the issue of securities through the book-building process. The issuer company is permitted to pay interest on the application moneys till the date of allotment or the deemed date of allotment provided that payment of interest is uniformly given to all the applicants.

12. Payment schedule and listing:

The book-runner may require the underwriters to the 'net offer to the public to pay in advance all moneys required to be paid in respect of their underwriting commitment by the eleventh day of the closure of the issue. In that case, the shares allotted as per the private placement category will become eligible for being listed. Allotment of securities under the public category is to be made as per the prevailing statutory requirements.

13. Under-subscription:

In the case of under-subscription in the ‘net offer to the extent of under-subscription is to be permitted from to the condition that preference is given to the individual investors. In the case of under- subscription in the placement portion, spill over is to be permitted from the net offer to the public to the placement portion.

Advantages of Book Building

Book-building process is of immense use in the following ways: 1. Reduction in the duration between allotment and listing 2. Reliable allotment procedure 3. Quick listing in stock exchanges possible 4. No price manipulation as the price is determined on the basis of the bids received.

STOCK OPTION OF EMPLOYEES STOCK OPTION SCHEME (ESOP)

A method of marketing the securities of a company whereby its employees are encouraged to take up shares and subscribe t scheme on the encouraged to take up shares and subscribe to it is known as 'stock option'. It is a voluntary scheme on the part of the company to encourage employee’s participation in the company. The scheme is particularly useful in the case of companies whose business activity is dominantly based on the talent of the employees, as in the case of software industry. The scheme helps retain their most productive employees in an industry, which is known for its constant churning of personnel.

SEBI Guidelines Company whose securities are listed on any stock exchange can introduce the scheme of employee’s stock option. The offer can be below:

1. Issue at discount Issue of stock option at a discount to the market price would be regarded as another form of employee compensation and would be treated as such in the financial statements of the company regardless the quantum of discount on the exercise price of the options.

2. Approval The issue of ESOPs is subject to the approval by the shareholders through a special resolution.

3. **Maximum limit** There would be no restriction on the maximum number of shares tobe issued to a single employee. However, in case of employees being offered more than 1 percent shares, a specific disclosure and approval would be necessary in the AGM.

4. **Minimum period** A minimum period of one year between grant of options and its vesting has been prescribed. After one year, the company would determine the period during which the option can be exercised.

5. **Superintendence** The operation of the ESOP Scheme would have to be under the superintendence and direction of a Compensation Committee of the Board of Directors in which there would be a majority of independent directors.

6. **Eligibility** ESOP scheme is open to all permanent employees and to the directors of the company but not to promoters and large shareholders. The scheme would be applicable to the employees of the subsidiary or a holding company with the express approval of the shareholders.

7. **Director's report** The Director's report shall make a disclosure of the following: a. Total number of shares as approved by the shareholders b. The pricing formula adopted c. Details as to options granted, options vested, options exercised and options forfeited, extinguishments or modification of options, money realized by exercise of options, total number of options in force, employee-wise details of options granted to senior managerial personnel and to any other employee who receive a grant in any one year of options amounting to 5 percent or more of options granted during that year d. Fully diluted EPS computed in accordance with the IAS **IPO** SEBI's stipulations prohibiting initial public offerings by companies having outstanding options should not apply to ESOP. If any ESOPs are outstanding at the time of an IPO issue by an unlisted company, the promoters 'contribution shall be calculated with reference to the enlarged capital that would arise if all vested options were exercised.

Stock Option Norms for Software Companies

The relevant guidelines issued by the SEBI as regards employees' stock option for so companies are as follows:

1. **Minimum issue** A minimum issue of 10 percent of its paid-up capital can be made by a software company which has already floated American Depository Receipts (ADRs) and Global Depository Receipts (GDRs) or a company which is proposing to float these is entitled to issue ADR/GDR-linked stock options to its employees. For this purpose, prior permission from the Department of Economic Affairs is to be obtained.
2. **Mode of Issue** Listed stock options can be issued in foreign currency convertible bonds and ordinary shares (through depository receipt mechanism) to the employees of subsidiaries of InfoTech companies.

3. **Permanent employees** Indian IT companies can issue ADR/GDR linked stock options to permanent employees, including Indian and overseas directors, of their subsidiary companies incorporated in India or outside.

4. **Pricing** The pricing provisions of SEBI's prefer the scheme. The purpose is to enable the companies to issue stock options to its employees at a discount to the market price which serves as another form of compensation.

5. **Approval** Shareholders approval through a special resolution is necessary for issuing the ESOPs. A minimum period of one year between grant of option and its vesting has been prescribed. After one year, the company would determine the period in which option can be exercised.

BOUGHT OUT DEALS

A method of marketing of securities of a body corporate whereby the promoters of an unlisted company make an outright sale of a chunk of equity shares to a single sponsor or the lead sponsor is known as bought-out deals.

The following are the characteristics of Bought out deals

1. Parties: There are three parties involved in the bought-out deals. They are promoters of the company, sponsors and co-sponsors who are generally merchant bankers and investors.

2. Outright sale: Under this arrangement, there is an outright sale of a chunk of equity shares to a single sponsor or the lead sponsor.

3. Syndicate: Sponsor forms syndicate with other merchant bankers for meeting the resource requirements and for distributing the risk.

4.Sale price: The s ale price is finalized through negotiations between the issuing company and the purchaser, the sale being influenced by such factors as project evaluation, promoters image and reputation, current market sentiments, prospects of off-loading these shares at a future date, etc.

5. Fund-based: Bought-out deals are in the nature of fund-based activity where the funds of the merchant bankers get locked in for at least the prescribed minimum period.

6. Listing: The investor-sponsors make a profit, when at a future date, the shares get listed and higher prices prevail. Listing generally takes place at a time when the company is performing well in terms of higher profits and larger cash generations from projects.

7. OTCEI: Sale of these shares at Over-the-Counter Exchange of India (OTCEI) or at a recognized stock exchanges, the time of listing these securities and off loading them simultaneously are being generally decided in advance.

BOUGHT OUT DEALS vs. PRIVATE PLACEMENTS BENEFITS

Bought-out deals provide the following benefits:

1. Speedy sale: Bought-out deals offer a mechanism for a speedier sale of securities at lower costs relating to the issue.

2. Freedom: Bought-out deals offer freedom for promoters to set a realistic price and convince the sponsor about the same.

3. Investor protection: Bought-out deal's facilities better investor protection as sponsors are rigorously evaluated and appraised by the promoters before offloading the issue.

4. Quality offer: Bought-out deals help enhance the quality of capital floatation and primary market offerings.

Limitations Bought-out deals pose the following difficulties for the promoters, sponsors and

investors:

1. Loss of control: The apprehensions in the minds of promoters, particularly of the private or the closely held companies that the sponsors may control the company as they own large chunk of the shares of the company.

2. Loss of sales: Bought-out deals pose considerable difficulties in off-loading the shares in times of unfavourable market conditions. This results in locking up of investments and entailing losses to sponsors.

3. Wrong appraisal: Bought-out deals cause loss to sponsors on account of wrong appraisal of the project and overestimation of the potential price of the share.

4. Manipulation: Bought-out deals give great scope for manipulation at the hands of the sponsor through insider trading and rigging.

5. No accountability: Bought-out deals pose difficulty of penalizing the sponsor as there are no SEBI guidelines to regulate offerings by sponsors.

6. Windfall profits: Bought-out deals offer the advantage of windfall profits by sponsors at the cost of small investors.

7. Loss to investors: Where the shares taken up by issue brokers and a group of select clients are being bought back by the promoters at a pre-fixed higher price after allotment causing loss to investors of the company.

OTCEI (Over the Counter Exchange of India)

It is a Stock Exchange without a proper trading floor All stock exchanges have a specific place for trading their securities through counters. But, OTCEI is connected through a computer network and the transactions are taking place through computer operations. Thus, the development in information technology has given scope for starting this type of stock exchange. This stock exchange is recognized under the Securities Contract (Regulation) Act and so all the stocks listed in this exchange enjoy the same benefits as other listed securities enjoy. OTCEI has been incorporated under Section 25 of the companies Act. As a result of which the word limitedneed not be used since it is promoted for a common case of promoting the interest of small and medium companies. This privilege has been given to the company by the Central government. This company was promoted by a group of financial institutions owned by Government of India, consisting of UTI, ICICI, IDBI, SBI Capital Market, IFCI, LIC, GIC and CAN BANK financial Services.

FEATURES OF OTCEI

(1) Use of Modern Technology: It is an electronically operated stock exchange.

(2) Restrictions for other stocks: Stocks and shares listed in other stock exchanges will not be listed in the OTCEI and similarly, stock listed in OTCEI will not be listed in other stock exchanges.

(3) Minimum issued capital requirements: Minimum issued equity capital should be Rs.30 lakhs, out of which minimum public offer should be Rs.20 lakhs.

(4) Restrictions for large companies: No company with the issued equity share capital of more than Rs.25 crores is permitted for listing.

(5) Base Capital requirement for members: Members will be required to maintain a minimum base capital of Rs. 4 lakhs to trade on the permitted or on listed segment.

(6) All India network: The network of counters links OTCEI members, located in different parts of the country.

(7) Satellite facility: The satellite required for OTCEI for its operations is jointly held with Press Trust of India

(8) Computerization of transactions: Computers at each counter enable the dealers to enter various transactions or queries or quotes through a central OTCEI computer, using telecommunication links.

Objectives of OTCEI:

The following are the objectives of OTCEI

1. Assisting and guiding small companies to raise funds from the capital market in a cost-effective manner 2. Providing a convenient and an efficient avenue of capital market investments for small investors 3. Strengthening investors' confidence in the financial market by offering them the two-way best prices to them 4. Ensuring transparency, redressing investors complaints and unifying the country securities market to cover even those places which do not have a stock exchange 5. Acting as a launch pad to an IPO 6. Providing

liquidity advantage to the securities traded 7. Promoting organized trading in Unlisted Securities 8. Providing a source of valuation for securities traded OTCEI offers the following benefits: Benefits to Listed Companies The benefits that are offered to companies listed with OTCEI are as follows:

1. Negotiability: The Company can negotiate the issue price with the sponsors who have to market the issue. It provides an opportunity for fair pricing of an issue through negotiation with the sponsors.

2. Fixation of premium: In consultation with the sponsors, the company can fix an optimum level of premium on issue with minimum risk of non-subscription of the issue.

3. Savings in costs: Lots of costs associated with public issue of capital are saved through this mode. It provides an opportunity to companies to raise funds through capital market instruments at an extremely low cost as compared to a public issue. The method of sponsors placing the scrip‘s with members who in turn will offload the scrip‘s to public will obviate the need for a public issue and its associated costs.

4. No take-over threat: OTCEI lists scrip‘s even with 40 percent of the capital offered for public trading. The limit has now been brought down to 20 percent in the case of closely held companies and new companies. As a result, the present management of the companies are saved of threats of takeover if they restrict public offer.

5. Large access: Accessing a large pool of captive investor base through the OTCEI_s computerized network is made possible for companies. Though nationwide network for servicing of investors, companies listed on OTC Exchange can have a larger investor base.

6. Other benefits: a. Helpful to small companies b. Shares of all unlisted companies can now be traded on OTCEI c. Platform for issuers and first-level investors like financial institutions, state level financial corporations, Foreign Institutional Investors, etc. d. System for defining benchmark for securities e. Increasing business for the market constituents Benefits to Investors OTCEI offers the following benefits for investors:

1. Safety: OTCEI_s ring less and scrip less electronic trading ensure safety of transactions of the investor. For instance, every investor in a OTCEI is given an _Invest-OTC-Card free. This code is allotted on a permanent basis and should be used in all OTC transactions and applications of OTC issues. This card provides for the safety and security of the investors investments. The mechanism offers greater security to investors as the sponsors investigate into the company and the projects, before accepting sponsorship thus building up much needed greater investor confidence.

2. Transparency: OTC screens at every OTC counter display the best buy/sell prices. The exact trading prices are printed in the trading documents for confirmations. This protects the investor interest and there by minimize disputes.

3. Liquidity: A great advantage of the OTC is that the scrip‘s traded are liquid. This is because there are at least two market-makers who indulge in continuous buying and selling. This enables investors to buy and sell the scrip‘s any time.

4. Appraisal: OTC members sponsor each scrip listed in an OTC counter. The sponsor makes an appraisal of the scrip‘s for investor worthiness. This ensures quality of investments.

5. Access: Every OTC counter serves as a single window to the entire OTC exchange throughout the country and throughout the world too. Therefore, buying and selling may be resorted to from any part of the world. It offers the facility of faster deal settlement for investors across the counters spread over the entire country.

6. Transfer: It is important that OTC shares are transferable within 7 days, where the consolidated holdings of the scrip‘s do not exceed 0.5 percent of the issued capital of the company.

7. Allotment: There is not much waiting for the investors when it comes to allotment of scrip‘s. Allotment is completed in all respects within a matter of 35 days and trading begins immediately thereafter.

8. Other benefits : a. Derivatives such as futures and options, forward contracts on stock, and other forms of forward transactions and stock lending are allowed on OTCEI b. Scrip less trading makes dealings simper and easier c. Market-making system in OTC Exchange gives sufficient opportunities for the investors to exit d. Acts as a benchmark to value securities e. Creating an exit option for illiquid stocks/venture capitalists f. Shuffling portfolios for the investors g. Organizing and broad-basing trading in the existing market

Benefits to Financial System

The OTCEIs role has been laudable in as far as it helps contribute improving the financial system of India in the following ways: 1. National network of OTCEI operations facilitates the integration of capital market in the country.

2. Boon to closely-held companies as they are encouraged to go public because scrip‘s can be listed even if only 40 percent of capital (now a minimum of 20 percent in case of closely held and new companies) is offered for public trading.

3. Facilities wider dispersal of economic activities by encouraging small companies and small investors.

4. Promoting savings and investments by offering easier avenues for raising capital.

5. Providing over-all stimulation to venture capital activities thereby promoting entrepreneurship.

6. Market-making assistance by the sponsors on the OTCEI that helps in making appraised future projections in the issue documents which in turn helps prospective investors in determining the usefulness of the issues for investment purposes, promoting investment environment in general.

7. Those members of the OTCEI who did not have multiple memberships can now have an opportunity to trade in some of the large capital index stocks.

8. Encourage venture capital activities and boost entrepreneurship

9. Spread of stock exchange operations geographically all over India Securities Traded Following are the securities that are traded on the OTCEI:

1. Listed equity (exclusive): These are equity shares of the companies listed exclusively on the OTCEI. The shared can be bought or sold at any of the member/ dealers office all over India. The securities, which are listed exclusively on the OTCEI, cannot be traded on other stock exchanges.

2. Listed debt: These are the debentures/bonds that are issued through a public issue or a private placement and are listed on OTCEI. Any entity holding the entire series of a particular debt instrument can also offer them for trading on the OTCEI, by appointing an OTCEI member/dealer to carry out compulsory market making in those securities.

3. Gilts: The securities issued by the Central and State Governments are called gilts. Government of India Dated Securities, Treasury Bills and special securities are traded in this segment. Banks, Foreign Investors, Foreign Institutional Investors, NBFCs and Provident Funds can trade in these securities through OTCEI designated members/dealers. PSU Bonds, Commercial Paper, and Certificates of Deposit will also be traded in this segment.

4. Permitted securities: These are the securities listed on other exchanges, which are permitted for trading on OTCEI. Securities of Blue-Chip companies like ACC, Reliance Industries Ltd., State Bank of India, ITC, etc. are traded in this segment.

UNIT 3

Post Issue activities and Right issues

1. Collect figures of applications money from the controlling branches and as far as possible from other key branches, and send one day report to the SEBI. If the issue is subscribed obtain the certificates from the registrars for 30 per cent/100 percent (as the case may be) subscription and send the copy of the same to the SEBI and the regional stock exchange.

2. Write to the related stock exchange regarding closure of subscription list and advertisements declaring issue to be closed is published.
3. Compliance reports to the SEBI are to be sent. There were four different types of reports in case of subscribed public issues (7, 45, 70 and 90 days reports) and six reports in case of unsubscribed public issues (7, 30, 45, 60, 90 and 100 days reports). With effect from July 1995, only two post-issue reports for public issue are to be submitted (3 and 78 days post-issue monitoring reports) (Annexures 10 (a) and 10(b)). The merchant bankers have to keep the SEBI informed on important developments about the particular issues being lead managed by them during the intervening period of the reports.
4. The following are to be submitted the regional stock exchange:
(a)Statement of valid application
(b)Certificate of 90 percent subscription
(c) Bank certificates

5. Obtain letter from regional stock exchange approving basis of allotment for different categories.
6. Send copy of the letter of regional stock exchange to other exchanges where listing permission is sought.
7. Make public a copy of basis of allotment in two national dailies
8. Publish advertisements mentioning the various dates on which refunds/ allotments and listing were dispatched and sought respectively.
9. In case of delay by more than 78 days the lead manager should see that the interest for the delayed period is paid by the issuer.
10. Confirm that the listing formalities have been completed where the listing has been sought
11. Arrange for permission for dealing in securities
12. Confirm that various commissions/brokerage/payments to various intermediaries ranged by the merchant banker have been paid by the company.
13. Obtain RBI permission of allotment of shares/debentures to NRIs and FIIs.

The lead manager should submit the draft of the letter of offer to the SEBI six weeks before the issue is scheduled to open for subscription. The suggestion, if any would be conveyed within three weeks from the date of receipt of such draft, should be incorporated /complied with by the merchant bankers before fling a copy of the letter of offer. A copy of the letter of offer should be submitted by the merchant bankers to the SEBI two weeks before the issue opens for subscriptions. The merchant banker should submit along with the letter of offer a due diligence certificate to the SEBI in the form, already prescribed by the SEBI. The merchant banker submitting he letter of offer is responsible for ensuring compliance with he SEBI rules, regulation and guidelines and requirements of other laws , which are for the time being, in force. Rest of the reports and regulations are to be complied with by the merchant bankers as already specified. The changes being made are only in respect of submission of letter of offer and the rest remains the same.

FACTORS IN PUBLIC ISSUE PROPOSAL

Before selecting a Public Issue proposal, the Merchant banker has to keep in mind the following aspects: Background of the Promoters/Management: Success of a company is very much dependent on the background of the promoters and the management viz., their education, business/technical expertise, financial strength capability and reputation, Issue Management etc. If a new company is launched from the platform of an already existing group, having successful track record, it is well received in the market. Performance of the group/associate concerns or the holding company, against the promises made by them at the time of their public issues is also looked into seriously by the prospective investors. If the group/associate concerns are financially strong enough, they can also lend support to the public offering. Another important aspect, which should be considered by the Merchant banker before picking a Public Issue proposal is to see whether there is any pending litigation, defaults and disputes of the promoters for the company with any person, bank or institution.

Company Profile: Merchant Banker also has to look at the track record of the company and the quality of its management, industry in which it operates, product mix of the Company and business prospects of the product proposed to manufacture. He also needs to decide the profitability of the product and sustain ability of the project. Financial health also has to be

gauged by probing the existing capital structure, debt equity ratio, level of gearing, nature and extent of various resources/provisions etc.

Project Profile: It is also considered whether the project is appraised by a Financial Institution, whether there is participation of Institutions in the financing of project, if any, and the level of financial participation of the Institution. Appraisal and funding of project by an Institution also certifies the viability of the project to an extent.

Capital Market Position: If the group/associate concerns are already listed on stock exchanges, the pattern of their share price movement should be analysed. Trading behaviour of shares of leading companies in the similar field should be compared with the share quotations of the group concern companies to see the stability in share quotations.

Other Important Factors: Other important factors which influence selection of a project include outlook of the: investors generally towards other companies operating in similar industries which are already listed and towards the group in particular. Investor's response to previous Public Issues of similar companies will also have a bearing on the decisions to come out with a Public Issue. Dividend payment schedule of the Company and its associate concerns should also be considered. From the point of view of Merchant Banker, the cost benefit analysis is also important before accepting assignment of issue management

PREPARATION OF PROSPECTUS

Prospectus is defined a document through which public are solicited to subscribe to the share capital of a corporate entity. Its purpose is inviting the public for the subscription/purchase of any securities of a company.

PROSPECTUS FOR PUBLIC OFFER

1. Regular prospectus 2. Abridged prospectus 3. Prospectus for rights issue 4. Disclosures in prospectus 5. Disclosures in abridged prospectus and letter of offer

1. REGULAR PROSPECTUS The regular prospectus is presented in three parts

PART I a. General Information about the company e.g. Name and address of the registered office consent of the Central Government for the issue and names of regional stock exchanges etc., b. Capital Structure such as authorized, issued, subscribed and paid up capital etc., c. Terms of the issue like mode of payment, rights of instruments holders etc., d. Particulars of the issue like project cost, means of financing etc., e. Company, Management and project like promoters for the project, location of the project etc. f. Disclosures of public issues made by the Company, giving information about type of issue, amount of issue, date of closure of issue, etc., g. Disclosure of Outstanding Litigation, Criminal Prosecution and Defaults h. Perception of Risk factors like difficulty in marketing the products, availability of raw materials etc.

PART II a. General Information b. Financial Information like Auditors Report, Chartered Accountants Report etc., c. Statutory and Other Information

PART III a. Declaration i.e., by the directors that all the relevant provisions of the companies Act, 1956 and guidelines issued by the Government have been complied with. b. Application with prospectus

2. ABRIDGED PROSPECTUS The concept of abridged prospectus was introduced by the Companies (amendment) Act of 1988 to make the public issue of shares an inexpensive proposition. A memorandum containing the salient features of a prospectus as prescribed is called as Abridged Prospectus

3. SELECTION OF BANKERS Merchant bankers assist in selecting the appropriate bankers based on the proposals or projects. Because the commercial bankers are merely financiers and their activities are appropriately arrayed around credit proposals, credit appraisal and loan sanctions. But merchant banking includes services like project counselling, corporate counselling in areas of capital restructuring amalgamations, mergers, takeover etc., discounting and rediscounting of short-term paper in money markets, managing, underwriting and supporting public issues in new issue market and acting as brokers and advisers on portfolio management in stock exchange.

4. ADVERTISING CONSULTANTS Merchant bankers arrange a meeting with company representatives and advertising agents to finalize arrangements relating to date of opening and closing of issue, registration, of prospectus, launching publicity campaign and fixing date of board meeting to approve and sign prospectus and pass the necessary resolutions. Publicity campaign covers the preparation of all publicity material and brochures, prospectus, announcement, advertisement in the press, radio, TV, investors conference etc., The merchant bankers help choosing the media, determining the size and publications in which the advertisement should appear. The merchant Bankers role is limited to deciding the number of copies to be printed, checking accuracy of statements made and ensure that the size of the application form and prospectus conform to the standard prescribed by the stock exchange. The Merchant banker has to ensure that the material is delivered to the stock exchange at least 21 days before the issue opens and to brokers to the issue, branches of brokers to the issue and underwriter in time. Securities issues are underwritten to ensure that in case of under subscription the issues are taken up by the underwriters. SEBI has made underwriting mandatory for issues to the public. The underwriting arrangement should be filed with the stock exchange. Particulars of underwriting arrangement should be mentions in the prospectus. The various activities connected with pre issue management are a time bound program which has to be promptly attended to. The execution of the activities with clockwork efficiency would lead to a successful issue.

5. REGISTRARS TO AN ISSUE AND SHARE TRANSFER AGENTS REGISTRATION The registrars to an issue, as an intermediary in the primary market, carry on activities such as collecting application from the investors, keeping a proper record of applications and money received from investors or paid to the seller of securities and assisting companies in determining the basis of allotment of securities in consultation with stock exchanges, finalizing the allotment of securities and processing/dispatching allotment letters, refund orders, certificates and other related documents in respect of issue of capital. The share transfer agents maintain the records of holders of securities or on behalf of companies, and

deal with all matters connected with the transfer/redemption of its securities. To carry on their activities, they must be registered with the SEBI which can also renew the certificate of registration. They are divided into two categories; a. Category I, to carry on the activities as a registrar to an issue and share transfer agent; b. Category II; to carry on the activity either as a registrar or as a share transfer agent. The registration is granted by the SEBI on the basis of consideration of all relevant matters and, in particular, the necessary infrastructure, past experience and capital adequacy. It also takes into account the fact that any connected person has not been granted registration and any director/partner/principal officer has not been convicted for any offence involving moral turpitude or has been found guilty of any economic offence.

6. CAPITAL ADEQUACY FEE The capital adequacy requirement in terms of net worth (capital and free reserves) was Rs.6 lakh and Rs.3 lakh for Category I and Category II of registrars and share transfer agents respectively. However, the capital adequacy requirements are not applicable since November 1999 for a department/division of a body corporate maintaining the records of holders of securities issued by them and deal with all matters connected with transfer/ redemption of securities. The two categories of registrars and transfer agents had to pay an annual fee respectively of Rs.15, 000 and Rs.10, 000 for initial registration a well as renewal. With effect from November 1999, while Category I is required to pay a registration fee of Rs.50,000 and a renewal fee of Rs.40,000 every three years, Category II has to pay Rs.30,000 and Rs.25,000 respectively.

MERGERS

A type of business combination where two or more firms amalgamate into one single firm is known as a merger. In a merger, one or more companies may merge with an existing company or they may combine to form a new company. In India mergers and amalgamations are used interchangeably. In the wider sense, merger includes consolidation, amalgamation, absorption and takeover. It signifies the transfer of all assets and liabilities of one or more existing companies to another existing or new company.

Objectives

The main purpose of merges is to achieve the advantage of fusion and synergy through expansion and diversification.

STEPS IN M & A

Following are the steps involved in M&A: 1. Review of Objectives: The first and foremost step in M&A is that the merging companies must undertake the review of the purpose for which the proposal to merge is to be considered. Major objectives of merger include attaining faster growth, improving profitability, improving managerial effectiveness, gaining market power and leadership, achieving cost reduction, etc. The review of objectives is done to assess the strengths and weaknesses, and corporate goals of the merging enterprise. In addition, the need for elimination of inefficient operations, cost reduction and productivity improvement, etc. should also be considered. Such a move would help the acquiring company to decide as to the kind of business units that must be acquired.

2. Data for analysis: After reviewing the relevant objective of acquisition the acquiring firm needs to collect detailed information pertaining to financial and other aspects of the firm and the industry. Industry-centric information will be needed to make an assessment of market growth, nature of competition, case of entry, capital and labor intensity, degree of regulation, etc. Similarly, firm-centric information will be needed to assess quality of management, market share, size, capital structure, profitability, production and marketing capabilities, etc. The data to be collected serves as the criteria for evaluation.

3. Analysis of information: After collecting both industry-specific and firm-specific information, the acquiring firm undertakes analysis of data and the pros and cons are weighed. Data is to be analysed with a view to determine the earnings and cash flows, areas of risk, the maximum price payable to the target company and the best way to finance the merger.

4. Fixing price: Price to be paid for the company being acquired shall be fixed taking into consideration the current market value of share of the company being acquired. The price shall usually be above the current market price of the share. A merger may take place at a premium. In such a case, the firm would pay an offer price which is higher than the target firms premerger market value. This would happen where the acquiring firm is of the firm opinion that such an option would augment operational results of the target firm owing to synergic effect.

5. Finding merger value: Value created by merger is to be found so that it is possible for the merging firms to determine their respective share. Merger value is equal to the excess of combined present value of the merged firms over and above the sum of their individual present values as separate entities. Any cost incurred towards the merging process is subtracted to arrive at the figure of net economic advantage of merger. This advantage is shared between the shareholders of the merging firms.

Take Over

Takeover is the case where one company obtains control over the management of another company. Under both acquisition and takeover, it is possible for a company to have effective control over another company even by holding minority ownership. For instance, the Monopolies and Restrictive Trade Practices (MRTP) Act prescribes that a minimum of 25 percent voting power must be acquired as to constitute a takeover. Similarly, section 372 of the Companies Act defines the limit of a company's investment in the shares of another company as anything more than 10 percent of the subscribed capital so as to constitute a takeover.

Distinction between Mergers vs. Takeovers

The following are the differences between Mergers and Takeover: Distinction Mergers Takeover

1.Definition Defined as an arrangement whereby the assets of two companies become vested in, or under the control of, one company (which may or may not be one of the original two companies), which has as its shareholders all, or substantially all, the shareholders of the two companies. Defined as a transaction or series of transactions whereby a person (individual, group of individuals or company) acquires control over the assets of a company, either directly by becoming the owner of those assets or indirectly by obtaining control of the management of the company

2. Mode Effected by the shareholders of one or both of the merging companies exchanging their shares (either voluntarily or as the result of a legal operation) for shares in the other or a third company, the arrangement being frequently effected by means of a takeover bid by one of the companies for the shares of the other, or of a takeover bid by a third company for the shares of both Effected by agreement with the holders of the whole of the share capital of the company being acquired, where the shares are held by the public generally, the takeover may be effected by agreement between the acquirer and the controllers of the acquired company, or by purchases of shares on the Stock Exchange, or by means of a takeover bid

3. Control over assets Shareholding in the combined enterprise will be spread between the shareholders of the two companies Direct or indirect control over the assets of the acquired company passes to the acquirer

4. Bid Bid is generally by the consent of the management of both companies Bid is frequently against the wishes of the management of the offeree company.

Major Issues of M&A in India

Business combinations and re-structuring in the form of merger, etc. have been attempted to face the challenge of increasing competition and to achieve synergy in business operations. The major issues of M&A are as follows: Depreciation The acquiring firm claims depreciation in respect of fixed assets transferred to it by the target firm. The depreciation allowance is available on the written down value of fixed assets. Further, the depreciation charge is based on the consideration paid and without any revaluation. R&D Expenditure It is possible for the acquiring firm to claim the benefit of tax deduction under section 35 of the Income Tax Act, 1961 in respect of transfer of any asset representing capital expenditure on R&D. Tax Exemption The fixed assets transferred to the acquiring firm by the target firm are exempt from capital gains tax. This is however subject to the condition that the acquiring firm is an Indian Company and that shares are swapped for shares in the target firm. Further, as the swap of shares is not considered as sale by the shareholders, profit or loss on such swap is not taxable in the hands of the shareholders of the amalgamated company. Carry Forward Losses The Indian Income Tax Act, 1961 contains highly favourable provision with regard to merger of a sick company with a healthy company. For instance, section 72A (1) of the Act gives the advantage of carry forward of losses of the target firm. The benefit is however available only: • Where the acquiring from is an Indian Company; • Where the target firm is not financially viable; • Where the merger is in public interest, • Where the merger facilities the revival of the business of the target firm; and • Where the scheme of amalgamation is approved by a specified authority.

PORTFOLIO AND MANAGEMENT SERVICES:

A list of all those services and facilities that are provided by a portfolio manager to its clients, relating to the management and administration of portfolio of securities or the funds of the client, is referred to as portfolio management services. The term Portfolio means the total holdings of securities belonging to any person. Portfolio Manager According to SEBI, Portfolio Manager means any person who pursuant to a contract or arrangement with a client, advises or directs or undertakes on behalf of the client (whether as a discretionary portfolio manager or otherwise) the management or administration of a portfolio of securities or the funds of the client, as the case may be. Discretionary Portfolio Manager According to SEBI, discretionary portfolio manager means a portfolio manager who exercises or may, under a contract relating to portfolio management, exercises any degree of discretion as to the investments or management of the portfolio of securities or the funds of the client, as the case may be.

Objectives

a. Provide long term capital appreciation with lower volatility, compared to the broad equity markets.

b. Takes long positions in the cash market and short positions in the index futures markets.

c. Invests in the model portfolios thus downside the risk by selling index futures in the derivatives market.

Functions of Portfolio and Management:

The objective of portfolio management is to develop a portfolio that has a maximum return at whatever level of risk the investor deems appropriate.

Risk Diversification An essential function of portfolio management is spread risk akin to investment of assets. Diversification could take place across different securities and across different industries. Is an effective way of diversifying the risk in an investment. Simple diversification reduces risk within categories of stocks that all have the same quality rating.

Asset Allocation An important function of portfolio management is asset allocation. It deals with attaining the operational proportions of investments from asset categories. Portfolio managers basically aim of stock-bond mix. For this purpose, equally weighted categories of assets are used. Bets Estimation Another important function of a portfolio manager is to make an estimate of best coefficient.

Its measurers and ranks the systematic risk of different assets. Best coefficient is an index of the systematic risk. This is useful in making ultimate selection of securities for investment by investment by a portfolio manager. E-Balancing Portfolios Rebalancing of portfolios involves the process of periodically adjusting the portfolios to maintain the original conditions of the portfolio. The adjustment may be made either by way of Constant proportion portfolio or by way of Constant best portfolio.

In Constant proportion portfolio, adjustments are made in such a way as to maintain the relative weighing in portfolio components according to the change in prices. Under the constant beta portfolio, adjustments are made to accommodate the values of component betas in the portfolio Strategies.

A portfolio manager may adopt any of the following strategies and part of an efficient portfolio management. Buy and Hold Strategy Under the buy and holdstrategy, the portfolio manager builds a portfolio of stock which is not disturbed at all for a long period of time. This practice is common in the case of perpetual securities such as common stock. Indexing Another strategy employed by portfolio managers is indexing. Indexing involves an attempt to replicate the investment characteristics of a popular measure of the bond market.

Securities that are held in best-known bond indexes are basically high-grade issues. Laddered Portfolio Under the laddered portfolio, bonds are selected in such a way as that their maturities are spread uniformly over a long period of time. This way a portfolio manager aims at distributing the funds throughout the yield curve. Barbell Portfolio Under the laddered portfolio, bonds are selected in such a way as that their maturities are spread uniformly over a long period of time. This way a portfolio manager aims at distributing the funds throughout the yield curve can also benefit from lower transaction costs because of better liquidity.

UNIT 4

UNDERWRITERS

Another important intermediary in the new issue/primary market is the underwriters to issues of capital who agree to take up securities which are not fully subscribed. They make a commitment to get the issue subscribed either by others or by themselves. Though underwriting is not mandatory after April 1995, its organization is an important element of the primary market. Underwriters are appointed by the issuing companies in consultation with the lead managers/merchant bankers to the issues.

A statement to the effect that in the opinion of the lead manager, the underwriter's assets are adequate to meet their obligation should be incorporated in the prospectus. Registration To act as underwriter, a certificate of registration must be obtained from the SEBI. In granting the certificate of registration, the SEBI considers all matters relevant/relating to the underwriting and in particular,

a) the necessary infrastructure like adequate office space, equipment and manpower to effectively discharge the activities

b) past experience in underwriting/employment of at least two persons with experience in underwriting

c) any person directly/indirectly connected with the applicant is not registered with the SEBI as under or a previous application of any such person has been rejected or any disciplinary action has been taken against such person under the SEBI Act/ rules/regulations,

d) capital adequacy requirement of not less than net worth (capital + free reserves) of Rs.20 lakhs; and

e) the applicant/director/principal officer/partner has been convicted of offence involving moral turpitude or found gully of any economic offence.

FEE Underwriters had to, for grant or renewal of registration; pay a fee to the SEBI from the date of initial grant of certificate, Rs. 2 lakhs for the first and second years and Rs.1 lakh for the third year. A fee of Rs.20, 000 was payable every year to keep the certificate in force or for its renewal. Since 1999, the registration fee has been raised to Rs.5 lakhs. To keep the registration in force, renewal fee of Rs.2 lakhs every three years from the fourth year from the date of initial registration is payable. Failure to pay the fee would result in the suspension of the certificate of registration.

General Obligations and Responsibilities

Code of Conduct for Underwriters An underwriter should:

1. Make all efforts to protect the interests of its clients.

2. Maintain high standards of integrity, dignity and fairness in the conduct of its business.

3. Ensure that it and its personnel will act in an ethical manner in all its dealings with a body corporate making an issue of securities (i.e. the issuer).

4. Endeavour to ensure all professional dealings are affected in a prompt, efficient and effective manner.

5. At all times render high standards of service, exercise due diligence, ensure proper care and exercise independent professional judgment.

6. Not make any statement, either oral or written, which would misrepresent (a) the services that the underwriter is capable of performing for its client, or has rendered to any other issuer company; (b) his underwriting commitment.

7. Avoid conflict of interest and make adequate disclosure of his interest.

8. Put in place a mechanism to resolve any conflict-of-interest situation that may arise in the conduct of its business or where any conflict of interest arises, should take reasonable steps to resolve the same in any equitable manner.

9. Make appropriate disclosure to the client of its possible source or potential in areas of conflict of duties and interest while acting as underwriter which would impair its ability to render fair, objective and unbiased services.

10. Not divulge to other issuer, press or any party any confidential information about its issuer company, which has come to its knowledge and deal in securities of any issuer company without making disclosure to the SEBI as required under these regulations and also to the Board directors of the issuer company.

11. Not discriminate amongst its clients, save and except on ethical and commercial considerations.

12. Ensure that any charge in registration status/any penal action taken by SEBI or any material change in financials which may adversely affect the interests of clients/ investors is promptly informed to the clients and any business remaining outstanding is transferred to another registered person in accordance with any instructions of the affected clients/investors.

13. Maintain an appropriate level of knowledge and competency and abide by the provisions of the SEBI Act, regulations, circulars and guidelines issued by the SEBI. The underwriter should also comply with the award of the Ombudsman under the SEBI (Ombudsman) Regulations, 2003.

14. Ensure that the SEBI is promptly informed about any action, legal proceedings, etc. initiated against it in respect of any material breach or non-compliance by it, of any law, rules, regulations, and directions of the SEBI or of any other regulatory body.

15. Not make any untrue statement or suppress any material fact in any documents, reports, papers or information furnished to the SEBI.

16. (a) Not render, directly or indirectly any investment advice about any security in the publicly accessible media, whether real-time or non-real-time, unless a disclosure of his interest including its long or short position in the security has been made, while rendering such advice; (b) In case an employee or an underwriter is rendering such advice, the underwriter should ensure that he should disclose his interest, the interest of his dependent family members and that of the employer including their long or short position in the security, while rendering such advice.

17. Not either through its account or their respective accounts or through their associates or family members, relatives or friends indulges in any insider trading.

18. Not indulge in any unfair competition, which is likely to be harmful to the interest of other underwriters carrying on the business of underwriting or likely to place such other underwriters in a disadvantageous position in relation to the underwriter while competing for, or carrying out any assignment.

19. Have internal control procedures and financial and operational capabilities which can be reasonably expected to protect its operations, its clients and other registered entities from financial loss arising from theft, fraud, and other dishonest acts, professional misconduct or commissions.

20. Provide adequate freedom and powers to its compliance officer for the effective discharge of his duties.

21. Develop its own internal code of conduct for governing its internal operations and laying down its standards of appropriate conduct for its employees and officers in the carrying out of their duties. Such a code may extend to the maintenance of professional excellence and standards, integrity, confidentiality, objectivity, avoidance of conflict of interest, disclosure of shareholdings and interests, etc.

22. Ensure that good corporate policies and corporate governance is in place.

23. Ensure that any person it employs or appoints to conduct business is fit and proper and otherwise qualified to act in the capacity so employed or appointed (including having relevant professional training or experience).

24. Ensure that it has adequate resources to supervise diligently and does supervise diligently persons employed or appointed by it to conduct business on its behalf.

25. Be responsible for the acts or omissions of its employees and agents in respect to the conduct of its business.

26. Ensure that the senior management, particularly decision makers have access to all relevant information about the business on a timely basis.

27. Not be party to or instrumental for

(a) certain of false market,

(b) price rigging or manipulation, or;

(c) passing of unpublished price sensitive information in respect of securities which are listed and proposed to be listed in any stock exchange to any person or intermediary. Agreement with Clients Every underwriter has to enter into an agreement with the issuing company. The agreement, among others, provides for the period during which the agreement is in force, the number of underwriting obligations, the period within which the underwriter has to be subscribe to the issue after being intimated by/on behalf of the issuer, the amount of commission/brokerage, and details of arrangements, if any, made by the underwriter for fulfilling the underwriting obligations.

General Responsibilities

An underwriter cannot derive any direct or indirect benefit from underwriting the issue other than by the underwriting commission. The maximum obligation under all underwriting agreements of an underwriter cannot exceed twenty times his net worth. Underwriters have to subscribe for securities under the agreement with 45 days of the receipt of intimation from the issuers. Inspection and Disciplinary Proceedings The framework of the SEBIs right to undertake the inspection of the books of accounts, other records and documents of the underwriters, the procedure for inspection and obligations of the underwriters is broadly on the same pattern as applicable to the lead managers.

Action in Case of Default

The liability for action in case of default arising out of i. non-compliance with any conditions subject to which registration was granted. ii. contravention of any provision of the SEBI Act/rules/regulations, by an underwriter involves the suspension/cancellation of registration, the effect of suspension/ cancellation are on the lines followed by the SEBI in case of lead managers.

TYPES OF UNDERWRITING

Securities underwriting

Securities underwriting is the process by which investment banks raise investment capital from investors on behalf of corporations and governments that are issuing securities (both equity and debt capital). The services of an underwriter are typically used as part of a public offering in a primary market.

This is a way of distributing a newly issued security, such as stocks or bonds, to investors. A syndicate of banks (the lead managers) underwrites the transaction, which means they have taken on the risk of distributing the securities. Should they not be able to find enough investors, they will have to hold some securities themselves. Underwriters make their income from the price difference (the "underwriting spread") between the price they pay the issuer and what they collect from investors or from broker-dealers who buy portions of the offering.

Risk, exclusivity, and reward

Once the underwriting agreement is struck, the underwriter bears the risk of being unable to sell the underlying securities, and the cost of holding them on its books until such time in the future that they may be favourably sold.

If the instrument is desirable, the underwriter and the securities issuer may choose to enter into an exclusivity agreement. In exchange for a higher price paid upfront to the issuer, or other favourable terms, the issuer may agree to make the underwriter the exclusive agent for the initial sale of the securities instrument. That is, even though third-party buyers might approach the issuer directly to buy, the issuer agrees to sell exclusively through the underwriter.

In summary, the securities issuer gets cash up front, access to the contacts and sales channels of the underwriter, and is insulated from the market risk of being unable to sell the securities at a good price. The underwriter gets a profit from the markup, plus the possibility of an exclusive sales agreement.

Also if the securities are priced significantly below market price (as is often the custom), the underwriter also curries favour with powerful end customers by granting them an immediate profit (see flipping), perhaps in a quid pro quo. This practice, which is typically justified as the reward for the underwriter for taking on the market risk, is occasionally criticized as unethical, such as the allegations that Frank Quattrone acted improperly in doling out hot IPO stock during the dot-com bubble.

In an attempt to capture more of the value of their securities for themselves, issuing companies are increasingly turning to alternative vehicles for going public, such as direct listings and SPACs.

Bank underwriting

In banking, underwriting is the detailed credit analysis preceding the granting of a loan, based on credit information furnished by the borrower; such underwriting falls into several areas:

Consumer loan underwriting includes the verification of such items as employment history, salary and financial statements; publicly available information, such as the borrower's credit history, which is detailed in a credit report; and the lender's evaluation of the borrower's credit needs and ability to pay. Examples include mortgage underwriting.

Commercial (or business) underwriting consists of the evaluation of financial information provided by small businesses including analysis of the business balance sheet including tangible net worth, the ratio of debt to worth (leverage) and available liquidity (current ratio). Analysis of the income statement typically includes revenue trends, gross margin, profitability, and debt service coverage.

Underwriting can also refer to the purchase of corporate bonds, commercial paper, government securities, municipal general-obligation bonds by a commercial bank or dealer bank for its own account or for resale to investors. Bank underwriting of corporate securities is carried out through separate holding-company affiliates, called securities affiliates or Section 20 affiliates.

Of late, the discourse on underwriting has been dominated by the advent of machine learning in this space. These profound technological innovations are altering the way traditional underwriting scorecards have been built, and are displacing human underwriters with automation. Natural language understanding allows the consideration of more sources of information to assess risk than used previously.[3] These algorithms typically use modern data sources such as SMS / Email for banking information, location data to verify addresses, and so on. Several firms are trying to build models that can gauge a customer's willingness to pay using social media data by applying natural language understanding algorithms which essentially try to analyse and quantify a person's popularity / likability and so on, with the premise being that people scoring high on these parameters are less likely to default on a loan. However, this area is still vastly subjective.

Insurance underwriting

Insurance underwriters evaluate the risk and exposures of potential clients. They decide how much coverage the client should receive, how much they should pay for it, or whether even to accept the risk and insure them. Underwriting involves measuring risk exposure and determining the premium that needs to be charged to insure that risk. The function of the underwriter is to protect the company's book of business from risks that they feel will make a loss and issue insurance policies at a premium that is commensurate with the exposure presented by a risk.

Each insurance company has its own set of underwriting guidelines to help the underwriter determine whether or not the company should accept the risk. The information used to

evaluate the risk of an applicant for insurance will depend on the type of coverage involved. For example, in underwriting automobile coverage, an individual's driving record is critical. However, the type of automobile is actually far more critical. As part of the underwriting process for life or health insurance, medical underwriting may be used to examine the applicant's health status (other factors may be considered as well, such as age & occupation). The factors that insurers use to classify risks are generally objective, clearly related to the likely cost of providing coverage, practical to administer, consistent with applicable law, and designed to protect the long-term viability of the insurance program.

The underwriters may decline the risk, or may provide a quotation in which the premiums have been loaded (including the amount needed to generate a profit, in addition to covering expenses) or in which various exclusions have been stipulated, which restrict the circumstances under which a claim would be paid. Depending on the type of insurance product (line of business), insurance companies use automated underwriting systems to encode these rules, and reduce the amount of manual work in processing quotations and policy issuance. This is especially the case for certain simpler life or personal lines (auto, homeowners) insurance. Some insurance companies, however, rely on agents to underwrite for them. This arrangement allows an insurer to operate in a market closer to its clients without having to establish a physical presence.

Two major categories of exclusion in insurance underwriting are moral hazard and correlated losses. With a moral hazard, the consequences of the customer's actions are insured, making the customer more likely to take costly actions. For example, bedbugs are typically excluded from homeowners' insurance to avoid paying for the consequence of recklessly bringing in a used mattress. Insured events are generally those outside the control of the customer, for example in life insurance, death by automobile accident is typically covered, but death by suicide is typically not covered. Correlated losses are those that can affect a large number of customers at the same time, thus potentially bankrupting the insurance company. This is why typical homeowner's policies cover damage from fire or falling trees (usually affecting an individual house), but not floods or earthquakes (which affect many houses at the same time).

Other forms

Continuous underwriting

Continuous Underwriting is the process in which the risks involved in insuring people or assets are being evaluated and analysed on a continuous basis. It evolved from the traditional underwriting, in which the risks only get assessed before the policy is signed or renewed. Continuous underwriting was first used in Workers' Compensation, where the premium of the insurance was updated monthly, based on the insured's submitted payroll. It is also used in Life Insurance, as well as Cyber Insurance.

Real estate underwriting

In evaluation of a real estate loan, in addition to assessing the borrower, the property itself is scrutinized. Underwriters use the debt service coverage ratio to figure out whether the property is capable of redeeming its own value.

Forensic underwriting

Forensic underwriting is the "after-the-fact" process used by lenders to determine what went wrong with a mortgage. Forensic underwriting is a borrower's ability to work out a modification scenario with their current lien holder, not to qualify them for a new loan or a refinance. This is typically done by an underwriter staffed with a team of people who are experienced in every aspect of the real estate field.

Sponsorship underwriting

Underwriting may also refer to financial sponsorship of a venture, and is also used as a term within public broadcasting (both public television and radio) to describe funding given by a company or organization for the operations of the service, in exchange for a mention of their product or service within the station's programming.

BOUGHT OUT DEALS

A method of marketing of securities of a body corporate whereby the promoters of an unlisted company make an outright sale of a chunk of equity shares to a single sponsor or the lead sponsor is known as bought-out deals.

The following are the characteristics of Bought out deals

1. Parties: There are three parties involved in the bought-out deals. They are promoters of the company, sponsors and co-sponsors who are generally merchant bankers and investors.

2. Outright sale: Under this arrangement, there is an outright sale of a chunk of equity shares to a single sponsor or the lead sponsor.

3. Syndicate: Sponsor forms syndicate with other merchant bankers for meeting the resource requirements and for distributing the risk.

4. Sale price: The s ale price is finalized through negotiations between the issuing company and the purchaser, the sale being influenced by such factors as project evaluation, promoters' image and reputation, current market sentiments, prospects of off-loading these shares at a future date, etc.

5. Fund-based: Bought-out deals are in the nature of fund-based activity where the funds of the merchant bankers get locked in for at least the prescribed minimum period.

6. Listing: The investor-sponsors make a profit, when at a future date, the shares get listed and higher prices prevail. Listing generally takes place at a time when the company is performing well in terms of higher profits and larger cash generations from projects.

7. OTCEI: Sale of these shares at Over-the-Counter Exchange of India (OTCEI) or at a recognized stock exchanges, the time of listing these securities and offloading them simultaneously are being generally decided in advance.

BOUGHT OUT DEALS vs. PRIVATE PLACEMENTS BENEFITS

Bought-out deals provide the following benefits:

1. Speedy sale: Bought-out deals offer a mechanism for a speedier sale of securities at lower costs relating to the issue.

2. Freedom: Bought-out deals offer freedom for promoters to set a realistic price and convince the sponsor about the same.

3. Investor protection: Bought-out deal's facilities better investor protection as sponsors are rigorously evaluated and appraised by the promoters before offloading the issue.

4. Quality offer: Bought-out deals help enhance the quality of capital floatation and primary market offerings.

Limitations

Bought-out deals pose the following difficulties for the promoters, sponsors and investors:

1. Loss of control: The apprehensions in the minds of promoters, particularly of the private or the closely held companies that the sponsors may control the company as they own large chunk of the shares of the company.

2. Loss of sales: Bought-out deals pose considerable difficulties in off-loading the shares in times of unfavourable market conditions. This results in locking up of investments and entailing losses to sponsors.

3. Wrong appraisal: Bought-out deals cause loss to sponsors on account of wrong appraisal of the project and overestimation of the potential price of the share.

4. Manipulation: Bought-out deals give great scope for manipulation at the hands of the sponsor through insider trading and rigging.

5. No accountability: Bought-out deals pose difficulty of penalizing the sponsor as there are no SEBI guidelines to regulate offerings by sponsors.

6. Windfall profits: Bought-out deals offer the advantage of windfall profits by sponsors at the cost of small investors.

7. Loss to investors: Where the shares taken up by issue brokers and a group of select clients are being bought back by the promoters at a pre-fixed higher price after allotment causing loss to investors of the company.

ADVERTISING STRATEGIES SEBI

Guidelines for Issue Advertisement (11.10.1993) SEBI issued Guidelines in 1993 to ensure that the advertisement is truthful fair and clear and do not contain statements to mislead the investors to imitate their judgment. All lead managers are expected to ensure that issuer companies strictly observe the code of advertisement set-out in the guidelines. For the purpose of these guidelines the expression advertisement, means notices, brochures, pamphlets, circulars show cards, catalogues, boarding 's, placards, posters, insertions in newspapers, pictures, films, radio/television program or through any electronic media and would also include the cover pages of the offer documents.

CAPITAL MARTKET INSTRUMENTS

Financial instruments that are used for raising capital resources in the capital market are known as Capital Market Instruments. The changes that are sweeping across the Indian capital market especially in the recent past are something phenomenal. It has been experiencing metamorphic in the last decade, thanks to a host of measures of liberalization, globalization, and privatization that have been initiated by the Government. Pronounced changes have occurred in the realm of industrial policy. Licensing policy, financial services industry, interest rates, etc. The competition has become very intense and real in both industrial sector and financial services industry. As a result of these changes, the financial services industry has come to introduce a number of instruments with a view to facilitate borrowing and lending of money in the capital market by the participants.

Types of Capital Market Instruments

The various capital market instruments used by corporate entities for raising resources are as follows: 1. Preference shares 2. Equity shares 3. Non-voting equity shares 4. Cumulative convertible preference shares 5. Company fixed deposits 6. Warrants 7. Debentures and Bonds

1.PREFERENCE SHARES: Shares that carry preferential rights in comparison with ordinary shares are called _Preference Shares_. The preferential rights are the rights regarding payment of dividend and the distribution of the assets of the company in the event of its winding up, in preference to equity shares.

Types of Preference Shares

1. Cumulative preference shares: Shares where the arrears of dividends in times of no and/or lean profits can be accumulated and paid in the year in which the company earns good profits. 2. Non-cumulative preference shares: Shares where the carry forward of the arrears of dividends is not possible.

3. Participating preference shares: Shares that enjoy the right to participate in surplus profits or surplus assets on the liquidation of a company or in both, if the Articles of Association provides for it.

4. Redeemable preference shares: Shares that are to be repaid at the end of the term of issue, the maximum period of a redemption being 20 years with effect from 1.3.1997 under the Companies amendment Act 1996. Since they are repayable, they are similar to debentures. Only fully paid shares are redeemed. Where redemption is made out of profits, a Capital Redemption Reserve Account is opened to which a sum equal to the nominal value of the shares redeemed is transferred. It is treated as paid-up share capital of the company.

5. Fully convertible cumulative preference shares: Shares comprise two parts viz., Part A and B. Part A is convertible into equity shares automatically and compulsorily on the date of allotment. Part B will be redeemed at par/converted into equity shares after a lock-in period at the option of the investor, conversion into equity shares taking place after the lock-in period, at a price, which would be 30 percent lower than the average market price. The average market price shall be the average of the monthly high and low price of the shares in a stock exchange over a period of 6 months including the month in which the conversion takes place.

6. Preference shares with warrants attached: The attached warrants entitle the holder to apply for equity shares for cash, at a premium, at any time, in one or more stages between the third and fifth year from the date of allotment. If the warrant holder fails to exercise his option, the unsubscribed portion will lapse. The holders of warrants would be entitled to all rights/bonus shares that may be issued by the company. The preference shares with warrants attached would not be transferred/sold for a period of 3 years from the date of allotment.

2. EQUITY SHARES: Equity shares, also known as „ordinary shares are the shares held by the owners of a corporate entity. Since equity shareholders face greater risks and have no specified preferential rights, they are given larger share in profits through higher dividends than those given to preference shareholders, provided the company's performance is excellent. Directors declare no dividends in case there are no profits or the profits do not justify dividend for previous years even when the company makes substantial profits in subsequent years. Equity shareholders also enjoy the benefit of ploughing back of undistributed profits kept as reserves and surplus for the purposes of business expansion. Often, part of these is distributed to them, as bonus shares. Such bonus shares are entitled to a proportionate or full dividend in the succeeding year. A strikingly noteworthy feature of equity shares is that holders of these shares enjoy substantial rights in the corporate democracy, namely the rights to approve the company's annual accounts, declaration of dividend, enhancement of managerial remuneration in excess of specified limits and fixing the terms of appointment and election of directors, appointment of auditors and fixing of their remuneration, amendments to the Articles and Memorandum of Association, increase of share capital and issue of further shares or debentures, proposals for mergers and reconstruction and any other important proposal on which member's approval is required under the Companies Act. Equity shares in the hands of shareholders are mainly reckoned for determining the management's control over the company. Where shareholders are widely disbursed, it is possible for the management to retain the control, as it is not possible for all the shareholders to attend the company's meeting in full strength. Furthermore, the management group can bolster its controlling power by acquiring further shares in the open market or otherwise. Equity shares may also be offered to financial institutions as part of the

private placement exercise. Such a method, however, is brought with the danger of takeover attempt by financial institutions.

Equity shareholders represent proportionate ownership in a company. They have residual claims on the assets and profits of the company. They have unlimited potential for dividend payments and price appreciation in comparison to these owners of debentures and preference shares who enjoy just a fixed assured return in the form of interest and dividend. Higher the risk, higher the return and vice-versa. Share certificates either in physical form or in the demat (with the introduction of depository system in 1999) form are issued as a proof of ownership of the shares in a company. Fully paid equity shares with detachable warrants entitle the warrant holder to apply for a specified number of shares at a determined price. Detachable warrants are separately registered with stock exchange and traded separately. The company would determine the terms and conditions relating to the issue of equity against warrants. Voting rights are granted under the Companies Act (Sections 87 to 89) wherein each shareholder is eligible for votes proportionate to the number of shares held or the amount of stock owned.

A company cannot issue shares carrying disproportionate voting rights. Similarly, voting right cannot be exercised in respect of shares on which the shareholder owes some money to the company. Capital Equity shares are of different types. The maximum value of shares as specified in the Memorandum of Association of the company is called the authorized or registered or nominal capital. Issued capital is the nominal value of shares offered for public subscription. In case shares offered for public subscription are not taken up, the portion of capital subscribed is called subscribed capital. This is less than the issued capital Paid-up capital is the share capital paid-up by shareowners which is credited as paid-up on the shares. Par Value and Book Value The face value of a share is called its Par value. Although shares can be sold below the par value, it is possible that shares can be issued below the par value. The financial institutions that convert their unpaid principal and interest into equity in sick companies are compelled to do if at a minimum of Rs.10 because of the par value concept even though the market price might be much less than Rs.10. Par value can also lead to unhealthy practices like price rigging by promoters of sick companies to take market prices above Rs.10 to get their new offers subscribed. Par value is of use to the regulatory agency and the stock exchange. It can be used to control the number of shares that can be issued by the company. The par value of Rs.10 per share serves as a floor price for issue of shares. Book value is the intrinsic value of a share that is calculated to reflect the net worth of the shareholders of a corporate entity. Cash Dividends These are dividends paid in cash. A stable payment of cash dividend is the hallmark of stability of share prices.

Stock Dividends

These are the dividends distributed as shares and issued by capitalizing reserves. While net worth remains the same in the balance sheet, its distribution between shares and surplus is altered.

3. NON-VOTING EQUITY SHARES

Consequent to the recommendations of the Abid Hussain Committee and subsequent to the amendment to the Companies Act, corporate managements are permitted to mobilize additional capital without diluting the interest of existing shareholders with the help of a new instrument called non-voting equity shares. Such shares will be entitled to all the benefits except the right to vote in general meetings. Such non-voting equity share is being considered as a possible addition to the two classes of share capital currently in vogue. This class of shares has been included by an amendment to the Companies Act as a third category of shares. Corporates will be permitted to issue such share up to a certain percentage of the total share capital. Non-voting equity shares will be entitled to rights and bonus issues and preferential offer of shares on the same lines as that of ordinary shares. The objective will be to compensate the sacrifice made for the voting rights. For this purpose, these shares will carry higher dividend rate than that of voting shares. If a company fails to pay dividend, non-voting shareholders will automatically be entitled to voting rights on a prorate basis until the company resumes paying dividend. The mechanism of issue of non-voting shares is expected to overcome such problems as are associated with the voting shares as that the ordinary investors are more inclined towards high return on capital through sizeable dividends and capital appreciation through the issue of bonus shares and the inability of corporate to respond to the investors_ just aspiration for reasonable dividends. Moreover, there is every need for corporate to spend huge sums of money on a variety of not-so useful items including colourful and costly annual reports. For all these above-mentioned reasons, non-voting equity shares are expected to have a ready and popular marker. In effect, this kind of share is similar to preference shares with regard to non-voting right but may get the advantage of higher dividends as well as appreciation in share values through entitlement to bonus shares which is not available to preference shares.

4. CONVERTIBLE CUMULATIVE PREFERENCE SHARES (CCPS)

These are the shares that have the twin advantage of accumulation of arrears of dividends and the conversion into equity shares. Such shares would have to be the face value of Rs.100 each. The shares have to be listed on one or more stock exchanges in the country. The object of the issue of CCP shares is to allow for the setting up of new projects, expansion or diversification of existing projects, normal capital expenditure for modernization and for meeting working capital requirements.

Following are some of the terms and conditions of the issue of CCP shares :

1. Debt-equity ratio: For the purpose of calculation of debt-equity ratio as may be applicable CCPS is be deemed to be an equity issue.

2. Compulsory conversion: The conversion into equity shares must be for the entire issue of CCP shares and shall be done between the periods at the end of three years and five years as may be decided by the company. This implies that the conversion of the CCP into equity shares would be compulsory at the end of five years and the aforesaid preference shares would not be redeemable at any stage.

3. Fresh issue: The conversion of CCP shares into equity would be deemed as being one resulting from the process of redemption of the preference shares out of the proceeds of a fresh issue of shares made for the purposes of redemption.

4. Preference dividend: The rate of preference dividend payable on CCP shares would be 10 percent.

5. Guideline ratio: The guideline ratio of 1:3 as between preference shares and equity shares would not be applicable to these shares.

6. Arrears of dividend: The right to receive arrears of dividend up to the date of conversion, if any, shall devolve on the holder of the equity shares on such conversion. The holder of the equity shares shall be entitled to receive the arrears of dividend as and when the company makes profit and is able to declare such dividend.

7. Voting right: CCPS would have voting rights as applicable to preference shares under the companies Act, 1956. 8. Quantum: The amount of the issue of CCP shares would be to the extent the company would be offering equity shares to the public for subscription.

5. COMPANY FIXED DEPOSITS: Fixed deposits are the attractive source of short-term capital both for the companies and investors as well. Corporates favour fixed deposits as an ideal form of working capital mobilization without going through the process of mortgaging assets. Investors find fixed deposits a simple avenue for investment in popular companies at attractively reasonable and safe interest rates. Moreover, investors are relieved of the problem of the hassles of market value fluctuation to which instruments such as shares and debentures are exposed. There are no transfer formalities either. In addition, it is quite possible for investors to have the option of premature repayment after 6 months, although such an option entails some interest loss. Regulations Since these instruments are unsecured; there is a lot of uncertainty about the repayment of deposits and regular payment of interest.

The issue of fixed deposits is subject to the provisions of the Companies Act and the Companies (Acceptance of Deposits) Rules introduced in February 1975. Some of the important regulations are:

1. Advertisement: Issue of an advertisement as approved by the Board of Directors in dailies circulating in the state of incorporation.

2. Liquid assets: Maintenance of liquid assets equal to 15 percent (substituted for 10% by Amendment Rules, 1992) of deposits (maturing during the year ending March 31) in the form of bank deposits, unencumbered securities of State and Central Governments or unencumbered approved securities.

3. Disclosure: Disclosure in the newspaper advertisement the quantum of deposits remaining unpaid after maturity. This would help highlight the defaults, if any, by the company and caution the depositors.

4. Deemed public Company: Private company would become a deemed public company (from June 1998, Section 43A of the Act) where such a private company, after inviting public deposits through a statutory advertisement, accepts or renews deposits from the public other

than its members, directors or their relatives. This provision, to a certain extent, enjoins better accountability on the part of the management and auditors.

5. Default: Penalty under the law for default by companies in repaying deposits as and when they mature for payment where deposits were accepted in accordance with the Reserve Bank directions.

6. CLB: Empowerment to the Company Law Board to direct companies to repay deposits, which have not been repaid as per the terms and conditions governing such deposits, within a time frame and according to the terms and conditions of the order.

6. WARRANTS

An option issued by a company whereby the buyer is granted the right to purchase a number of shares of its equity share capital at a given exercise price during a given period is called a warrant. Although trading in warrants is in vogue in the U.S. Stock markets for more than 6 to 7 decades, they are being issued to meet a range of financial requirements by the Indian corporate. A security issued by a company, granting its holder the right to purchase a specified number of shares, at a specified price, any time prior to an expirable date is known as an arrant. Warrants may be issued with either debentures or equity shares. They clearly specify the number of shares entitled, the expiration date, along with the stated/exercise price. The expiration date of warrants in USA is generally 5 to 10 years from the date of issue and the exercise price is 10 to 30 percent above the prevailing market price. Warrants have a secondary market. The exchange value between the share of its current price and the shares to be purchased at the exercise price represents the minimum value of warrant. They have no floatation costs and when they are exercised, the firm receives additional finds at a price lower than the current market, yet higher than those prevailing at the time of issue. Warrants are issued by new/growing firms and venture capitalists. They are also issued during mergers and acquisitions. Warrants in the Indian context are called sweetenersand were issued by a few Indian companies since 1993. Both warrants and rights entitle a buyer to acquire equity shares of the issuing company. However, they are different in the sense that warrants have a life span of three to five years whereas; rights have a life span of only four to twelve weeks (duration between the opening and closing date of subscription list). Moreover, rights are normally issued to effect current financing, and warrants are sold to facilitate future financing. Similarly, the exercise price of warrant, i.e. The price at which it can be exchanged for share, is usually above the market price of the share so as to encourage existing shareholders to purchase it. On the other hand, one warrant buys one equity share generally, whereas more than one rights may be needed to buy one share. The detachable warrant attached to each share provides a right to the warrant holder to apply for additional equity share against each warrant.

7. DEBENTURES AND BONDS

A document that either creates a debt or acknowledges it is known as a debenture. Accordingly, any document that fulfils either of these conditions is a debenture. A debenture, issued under the common seal of the company, usually takes the form of a certificate that acknowledges indebtedness of the company. A document that shows on the face of it that a

company has borrowed a sum of money from the holder thereof upon certain terms and conditions is called a debenture. Debentures may be secured by way of fixed or floating charges on the assets of the company. These are the instruments that are generally used for raising long-term debt capital.

Following are the features of a debenture

1. Issue: In India, debentures of various kinds are issued by the corporate bodies, Government, and others as per the provisions of the Companies Act, 1956 and under the regulations of the SEBI. Section 117 of the Companies Act prohibits issue of debentures with voting rights. Generally, they are issued against a charge on the assets of the company but at times may be issued without any such charge also. Debentures can be issued at a discount in which case, the relevant particulars are to be filed with the Registrar of Companies.

2. Negotiability: In the case of bearer debentures the terminal value is payable to its bearer. Such instruments are negotiable and are transferable by delivery. Registered debentures are payable to the registered holder whose name appears both on the debenture and in the register of debenture holders maintained by the company. Further, transfer of such debentures should be registered. They are not negotiable instruments and contain a commitment to pay the principal and interest.

3. Security: Secured debentures create a charge on the assets of the company. Such a charge may be either fixed or floating. Debentures that are issued without any charge on assets of the company are called _unsecured or marked debentures

4. Duration: Debentures, which could be redeemed after a certain period of time are called Redeemable Debentures. There are debentures that are not to be returned except at the time of winding up of the company. Such debentures are called Irredeemable Debentures.

5. Convertibility: Where the debenture issue gives the option of conversion into equity shares after the expiry of a certain period of time, such debentures are called Convertible Debentures. Non-convertible Debentures, on the other hand, do not have such an exchange facility.

6. Return: Debentures have a great advantage in them in that they carry a regular and reasonable income for the holders. There is a legal obligation for the company to make payment of interest on debentures whether or not any profits are earned by it.

7. Claims: Debenture holders command a preferential treatment in the matters of distribution of the final proceeds of the company at the time of its winding up. Their claims rank prior to the claims of preference and equity shareholders.

KINDS OF DEBENTURES

Innovative debt instruments that are issued by the public limited companies are described below: 1. Participating debentures 2. Convertible debentures. 3. Debt-equity swaps 4. Zero-coupon convertible notes 5. Secured Premium Notes (SPN) with detachable warrants 6. Non-Convertible Debentures (NCDs) with detachable equity warrant 7. Zero-interest Fully Convertible Debentures (FCDs) 8. Secured zero-interest Partly Convertible Debentures

(PCDs) with detachable and separately tradable warrants 9. Fully Convertible Debentures (FCDs) with interest (optional) 10. Floating Rate Bonds (FRB)

1. Participating debentures: Debentures that are issued by a body corporate which entitle the holders to participate in its profits are called _Participating Debentures_. These are the unsecured corporate debt securities. They are popular among existing dividend paying Corporates.

2. Convertible debentures a. Convertible debentures with options are a derivative of convertible debentures that give an option to both the issuer, as well as the investor, to exit from the terms of the issue. The coupon rate is specified at the time of issue. b. Third party convertible debentures are debts with a warrant that allow the investor to subscribe to the equity of a third firm at a preferential price vis-à-vis market price, the interest rate on the third party convertible debentures being lower than pure debt on account of the conversion option. c. Convertible debentures redeemable at a premium: Premium are issued at face value with a put option entitling investors to sell the bond to the issuer, at a premium later on. They are basically similar to convertible debentures but have less risk.

3. Debt-equity swaps: They are offered from an issue of debt to swap it for equity. The instrument is quite risky for the investor because the anticipated capital appreciation may not materialize.

4. Zero-coupon convertible note: These are debentures that can be converted into shares and on its conversion the investor forgoes all accrued and unpaid interest. The zero-coupon convertible notes are quite sensitive to changes in the interest rates.

5. SPN with detachable warrants: These are the Secured Premium Notes (SPN) with detachable warrants. These are the redeemable debentures that are issued along with a detachable warrant. The warrant entitles the holder to apply and get equity shares allotted, provided the SPN is fully paid. The warrants attached to it assure the holder such a right. No interest will be paid during the lock-in period for SPN. The SPN holder has an option to sell back the SPN to the company at par value after the lock-in period. If this option is exercised by the holder, no interest/premium will be paid on redemption. The holder will be repaid the principal and the additional interest/ premium amount in instalments as may be decided by the company. The conversion of detachable warrant into equity shares will have to be done within the time limit notified by the company.

6. NCDs with detachable equity warrants: These are Non-Convertible Debentures (NCDs) with detachable equity warrants. These entitle the holder to buy a specific number of shares from the company at a predetermined price within a definite time frame. The warrants attached to NCDEs are issued subject to full payment of the NCDs value. The option can be exercised after the specific lock-in period. The company is at liberty to dispose of the unapplied portion of shares if the option to apply for equalities is not exercised.

7. Zero interest FCDs: These are Zero-interest Fully Convertible Debentures on which no interest will be paid by the issuer during the lock-in period. However, there is a notified period after which fully paid FCDs will be automatically and compulsorily converted into

shares. In the event of a company going in for rights issue prior to the allotment of equity (resulting from the conversion of equity shares into FCDs), it shall do so only after the FCD holders are offered securities.

8. Secured Zero interest PCDs with detachable and separately tradable warrants: These are Secured Zero Interest Partly Convertible Debentures with detachable and separately tradable warrants. They are issued in two parts. Part A is a convertible portion that allows equity shares to be exchanged for debentures at a fixed amount on the date of allotment. Part B is a non-convertible portion to be redeemed at par at the end of a specific period from the date of allotment. Part B which carries a detachable and separately tradable warrant provides the warrant holder an option to received equity shares for every warrant held, at a price worked out by the company.

9. Fully Convertible Debentures (FCDs) with interest (optional): These are the debentures that will not yield any interest for an initial short period after which the holder is given an option to apply for equities at a premium. No additional amount needs to be paid for this. The option has to be indicated in the application form itself. Interest on FCDs is payable at a determined rate from the date of first conversion to the date of second/final conversion and in lieu of it, equity shares will be issued.

10. Floating Rate Bonds (FRB"s): These are the bonds where the yield is linked to a benchmark interest rate like the prime rate in USA or LIBOR in the Euro currency market. For instance, the State Bank of India's floating rate bond, issue was linked to the maximum interest on term deposits that was 10 percent at the time. The floating rate is quoted in terms of a margin above or below the benchmark rate. Interest rates linked to the benchmark ensure that neither the borrower nor the lender suffer from the changes in interest rates. Where interest rates are fixed, they are likely to be inequitable to the borrower when interest rates fall and inequitable to the lender when interest rates rise subsequently.

SEBI Guidelines: The preferential issue of equity shares/Fully Convertible Debentures (FCDs/Partly Convertible Debentures (PCDs) or any other financial instruments which would be converted into or exchanged with equity shares at a later date, by listed companies whose equity share capital is listed on any stock exchange, to any selected group of persons under the Companies Act, 1956 on private placement basis shall be governed by these guidelines. Such preferential issues by listed companies by way of equity shares/Fully Convertible Debentures (FCDs)/Partly Convertible Debentures (PCDs) or any other financial instruments which would be converted into/exchanged with equity shares at a later date, shall be made in accordance with the pricing provisions mentioned below

PRICING OF THE ISSUE

Preferential Issue of Shares: The issue of shares on a preferential basis can be made at a price not less than the higher of the following:

a. The average of the weekly high and low of the closing prices of the related shares quoted on the stock exchange during the six months preceding the relevant date (thirty days prior to

the date on which the meeting of general body of shareholders is held in terms of Section 81(1A) of the Companies Act, 1956 to consider the proposed issue) (or)

b. The average of the weekly high and low of the closing prices of the related shares quoted on a stock exchange (any of the recognized stock exchanges in which the shares are listed and in which the highest trading volume in respect of the shares of the company has been recorded during the preceding 6 months prior to the relevant date) during the two weeks preceding the relevant date. Pricing of Shares arising out of warrants, etc Where warrants are issued on a preferential basis with an option to apply for and be allotted shares, the issuer company shall determine the price of the resultant shares. The relevant date for the above purpose may, at the option of the issuer be either the one referred to above or a date 30 days prior to the date on which the holder of the warrants becomes entitled to apply for the said shares. The resolution to be passed in terms of section 81(1A) shall clearly specify the relevant date on the basis of which price of the resultant shares shall be calculated. An amount equivalent to at least ten percent of the price fixed in terms of the above shall become payable for the warrants on the date of their allotment. The amount referred to above shall be adjusted against the price payable subsequently for acquiring the shares by exercising an option for the purpose. The amount so referred to above shall be forfeited if the option to acquire shares is not exercised. Pricing of shares on conversion: Where PCDs/FCDs/other convertible instruments, are issued on a preferential basis, providing for the issuer to allot shares at a future date, the issuer shall determine the price at which the shares could be allotted in the same manner as specified for pricing of shares allotted in lieu of warrants as indicated above. Currency of Financial instruments: In case of warrants/PCDs/FCDs/or any other financial instruments with a provision for the allotment of equity shares at a future date, either through conversion or otherwise, the currency of the instruments shall not exceed beyond 18 months from the date of issue of the relevant instrument.

Non-Transferability of Financial Instruments:

The instruments allotted on a preferential basis to the promoter/promoter group shall be subject to lock-in period of 3 years from the date of their allotment. In any case, not more than 20 percent of the total capital (equity share capital issued by way of public/ rights issue including equity shares emerging at a later date out of any convertible securities/ exercise of warrants and equity shares or any other security convertible at a later date into equity issued on a preferential basis in favour of promoter/promoter groups) of the company, including capital brought in by way of preferential issue, shall be subject to lock-in of 3 years from the date of allotment. The lock-in on shares acquired by conversion of the convertible instrument/exercise of warrants shall be reduced to the extent the convertible instrument warrants have already been locked-in. For computation of 20 percent of the total capital of the company, the amount of minimum promoter ‘s contribution held and locked-in, in the past as per guidelines shall be taken into account. The minimum promoter ‘s contribution shall not again be put under fresh lock-in, even though it is considered for computing the requirement of 20 percent of the total capital of the company, in case they said minimum promoter ‘s contribution is free of lock-in at the time of the preferential issue. These locked in shares/instruments can be transferred to and amongst promoter/ promoter group subject to

continuation of lock-in the hands of transferees for the remaining period, and compliance of Securities and Exchange Board of India (Substantial Acquisition of shares and Takeovers) Regulations, 1997, if applicable. Currency of Shareholders Resolutions: Allotment pursuant to any resolution passed at a meeting of shareholders of a DFI granting consent for preferential issues of any financial instrument, shall be completed within a period of 3 months from the date of passing of the resolution. If allotment of instruments and dispatch of certificates is not completed within three months from the date of such resolution, a fresh consent of the shareholders shall be obtained and the relevant date referred to above will relate to the new resolution. Certificate from Auditors: In case of every issue of shares/warrants/FCDs/PCDs/other financial instruments having conversion option, the statutory auditors of the issuer DFI shall certify that the issue of said instruments is being made in accordance with the requirements contained in these guidelines. Copies of the auditor‘s certificate shall also be laid before the meeting of the shareholders convened to consider the proposed issue.

Preferential Allotments to FIIs:

Preferential allotments, if any to be made in case of Foreign Institutional Investors, shall also be governed by the guidelines issued by the Government of India/Board/Reserve Bank of India on the subject. Non-applicability of the Guidelines: The above guidelines shall not be applicable where the further shares are allotted in pursuance to the merger and amalgamation scheme approved by the High Court and where further shares are allotted to a person/group of persons in accordance with the provisions of rehabilitation packages approved by BIFR. In case, such persons are promoters or belong to promoter group lock-in provisions shall continue to apply unless otherwise stated in the BIFR order. Similarly, the above guidelines are not applicable where further shares are allotted to all India public financial institutions in accordance with the provision of the loan agreements signed prior to August 4, 1994.

Global Debt Instruments Following are some of the debt instruments that are popular in the international financial markets: Income Bonds Interest income on such bonds is paid only where the corporate command adequate cash flows. They resemble cumulative preference shares in respect of which fixed dividend is paid only if there is profit earned in a year, but carried forward and paid in the following year. There is no default on income bonds if interest is not paid. Unlike the dividend on cumulative preference shares, the interest on income bond is tax deductible. These bonds are issued by Corporates that undergo financial restructuring. Asset Backed Securities These are a category of marketable securities that are collateralized by financial assets such as instalment loan contracts. Asset backed financing involves a disinter- mediating process called securitization, whereby credit from financial intermediaries in the form of debentures are sold to third parties to finance the pool. REPOS are the oldest asset backed security in our country. In USA, securitization has been undertaken for the following the oldest asset backed security in our country.

In USA, securitization has been undertaken for the following: 1. Insured mortgages 2. Mortgage-backed bonds 3. Student loans 4. Trade credit receivable backed bonds 5. Equipment’s leasing backed bonds 6. Certificates of automobile receivable securities 7. Small business administration loans 8. Credit and receivable securities Junk Bonds

Junk bond is a high risk, high yield bond which finances either a Leveraged Buyout (LBO) or a merger of a company in financial distress Junk bonds are popular in the USA and are used primarily for financing takeovers. The coupon rates range from 16 to 25 percent. Attractive deals were put together establishing their feasibility in terms of adequacy of cash flows to meet interest payments. Michael Milken (the junk bond king) of Drexel Burnham Lambert was the real developer of the market. Indexed Bonds These are the bonds whose interest payment and redemption value are indexed with movements in prices. Indexed bonds protect the investor from the eroding purchasing power of money because of inflation. For instance, an inflation-indexed bond implies that the payment of the coupon and/or the redemption value increases or decreases according to movements in prices. The bonds are likely to hedge the principal amount against inflation. Such bonds are designed to provide investors an effective hedge against inflation so as to enhance the credibility of the anti-inflationary policies of the Government. The yields of an inflation-indexed bond provide vital information on the expected rate of inflation. United Kingdom, Australia, and Canada have introduced index linked government securities as a segmented internal debt management operation with a view to increase the range of assets available in the system, provide an inflation hedge to investors, reduce interest costs and pick up direct signals, and the expected inflation and real rate of interest from the market.

Zero-Coupon Bonds (ZCBs)/Zero Coupons Convertible Debentures Zero Coupon Bonds first came to be introduced in the U.S. securities market. Initially, such bonds were issued for high denominations. These bonds were purchased by large security brokers in large chunks, who resold them to individual investors, at a slightly higher price in affordable lots. Such bonds were called Treasury Investment Growth Receipts(TIGRs) or Certificate of Accruals on Treasury Securities(CATSs) or ZEROs as their coupon rate is Zero. Moreover, these certificates were sold to investors at a hefty discount and the difference between the face value of the certificate and the acquisition cost was the gain. The holders are not entitled for any interest except the principal sum on maturity.

Advantages: Zero-Coupon Bonds offer a number of advantages as shown below

a. No botheration of periodical interest payment for the issues

b. The attraction of conversion of bonds into equity shares at a premium or at par, the investors usually being rewarded by way of a low premium on conversion

c. There is only capital gains tax on the price differential and there is no tax on accrued income

d. Possibility of efficient servicing of equity as there is no obligation to pay interest till maturity and the eventual conversion. Mahindra & Mahindra came out with the scheme of Zero-Coupon Bonds for the first time in India along with 12.5 percent convertible bonds for part financing of its modernization and diversification scheme. Similarly, Deep Discount Bonds were issued by IDBI at Rs.2, 000 for a maturity of Rs.1 lakh after 25 years. These are negotiable instruments transferable by endorsement and delivery by the transferor. IDBI also offered Option Bonds which may be either cumulative or non-cumulative bonds where interest is payable either on maturity or periodically. Redemption is also offered to attract

investors. Floating Rate Bonds (FRBs) Bonds that carry the provision for payment of interest at different rates for different time periods are known as Floating Rate Bonds. The first floating rate bond was issued by the SBI in the Indian capital market. The SBI, while issuing such bonds, adopted a reference rate of highest rate of interest on fixed deposit of the Bank, provided a minimum floor rate payable at 12 percent p.a. and attached a call option to the Bank after 5 years to redeem the bonds earlier than the maturity period of 10 years at a certain premium. A major highlight of the bonds was the provision to reduce interest risk and assurance of minimum interest on the investment provided by the Bank.

Secured Premium Notes (SPNs) Secured debentures that are redeemable of a premium over the issue price or face value are called secured premium notes. Such bonds have a lock-in period during which period no interest will be paid. It entitles the holder to sell back the bonds to the issuing company at par after the lock-in period. A case in point was the issue made by the TISCO in the year 1992, where the company wanted to raise money for its modernization program without expanding its equity excessively in the next few years. The company made the issue to the existing shareholders on a rights basis along with the rights issue.

The salient features of the TISCO issue were as follows:

1. Face value of each SPN was Rs.300

2. No interest was payable during the first three years after allotment

3. The redemption started at the end of the fourth year of issue

4. Each of the SPN of Rs.300 was repaid in four equal annual instalments of Rs.75, which comprised of the principal, the interest and the relevant premium. (Low interest and high premium or high interest and low premium, at the option to be exercised by the SPN holder at the end of the third year)

5. Warrant attached to each SPN entitled the holder the right to apply for or seek allotment of one equity share for cash payment of Rs.80 per share. Such a right was exercisable between first year and one-and-a-half year after allotment by which time the SPN would be fully paid up. This instrument tremendously benefited TISCO, as there was no interest outgo. This helped TISCO to meet the difficulties associated with the cash generation. In addition, the company was able to borrow at a cheap rate of 13.65 percent as against 17 to 18 percent offered by most companies. This enabled the company to start redemption earlier through the generation of cash flow by the company's projects. The investors had the flexibility of tax planning while investing in SDPNs. The company was also equally benefited as it gave more flexibility. Euro Convertible Bonds that give the holders of euro bonds to have the instruments converted into a wide variety of options such as the call option for the issuer and the put option for the investor, which makes redemption easy are called

Euro-convertible bonds.

A euro convertible bond essentially resembles the Indian convertible debenture but comes with numerous options attached. Similarly, a euro-convertible bond is an easier instrument to

market than equity. This is because it gives the investor an option to retain his investments as a pure debt instrument in the event of the price of the equity share falling below the conversion price or where the investor is not too sure about the prospects of the company. Popularity of convertible euro bonds A convertible bond issue allows an Indian company far greater flexibility to tap the Euro market and ensures that the issue has a better market reception than would be possible for a direct equity issue. Moreover, newly industrialized countries such as Korea have chosen the convertible bond market as a stepping-stone to familiarity and acceptance of their industrial companies in the international market.

The convertible bonds offer the following advantages:

a. Protection: Euro convertible bonds are favoured by international investors as it offers them the advantage of protection of their wealth from erosion. This is possible because the conversion is only an option, which the investors may choose to exercise only if it works to their benefit. This facility is not available for equity issues.

b. Liquidity: Convertible bond market offers the benefit of the most liquid secondary market for new issues. Fixed income funds as well as equity investment managers purchase convertible bonds.

c. Flexibility: The feature of flexibility in structuring convertible bonds allows the company to include some of the best possible clauses of investors protection by incorpo0rating the unusual features of equity investments. A case in point is the issues made by the Korean corporate sector, which contained a provision in the issue of convertible euro bonds. The provision entitled the holders to ensure the due compliance of the liberalization measures that had already been announced within a specified period of time. Such a provision enabled the investor to opt for a putoption.

d. Attraction investment: The issue of convertible debentures facilitates removal of many of the unattractive features of equity investment. For investors, convertible bond market makers are the principal sources of liquidity in their securities.

Bond Issue

Indian Experience In recent times, all-India financial institutions have come to design and introduce special and innovative bond instruments exclusively structured on the investorspreferences and funds requirement of the issuers. The emphasis from the issuers view point is the resource mobilization and not risk exposure. Several financial institutions such as the IDBI, the ICICI, etc. are engaged in the sale of such bonds.

A brief description of some these bonds are presented below: 1. IDBIs Zero Coupon Bonds, 1996: These bonds are sold at a discount and are paid no interest. It is of great advantage to issuers as it is not required for them to make periodic interest payment.

2. IDBIs Regular Income Bonds, 1996: These were the bonds issued by the IDBI as 10-year bonds carrying a coupon of 16 percent, payable half-yearly. The bonds provided an annualized yield equivalent to 16.64 percent. The bonds, which were priced at Rs.5, 000 can

be redeemed at the end of every year, after the third-year allotment. There was also a call option that entitled the IDBI to redeem the bonds five years from the date of allotment.

3. Retirement Bonds, 1996: The IDBI Retirements Bonds were issued at a discount. The issue targeted investors who are planning for retirement. Under the scheme,. Investors get a monthly income for 10 years after the expiry of a wait period, the wait period being chosen by the investor. Thereafter, the investors also get a lump sum amount, which is the maturity value of the bond.

4. IFCIs Bonds, 1996 These bonds include: a. Deep Discount Bonds – Issued for a face value of Rs.1 lakh each. b. Regular Income and Retirement Bonds – They had a five-year tenure, a semi-annual yield of 16 percent and a front-end discount of 4 percent. The bonds had three-year put option and an early bird incentive of 0.75 percent. c. Step-up Liquid Bond – The five-year bonds with a put option every year with a return of 16 percent, 16.25 percent, 16.5 percent, 16.75 percent, and 17 percent at the end of every year. d. Growth Bond – An investment of Rs.20, 000 per bond under this scheme entitles investors to a Rs.1 lakh face-value bond maturing after 10 years. Put options can be exercised at the end of 5 and 7 years respectively. If exercised, the investor gets Rs.43, 500 after 5 years and Rs.60, 000 after a 7 year period. e. Lakhpati Bond – The maturity period of these bonds varied from l5 to 10 years, after which the investor gets Rs.1 lakh. The initial investment required was Rs.20,000 for 10 years maturity, Rs,.23,700 for 9 years, Rs,28,000 for 8 years, Rs.33,000 for 7 years, Rs.39,000 for 6 years and Rs.46,000 for 5 years maturity.

5. ICICIs Bonds, 1997 ICICI came out with as many as five bonds in March 1997. These are encash bonds, index bonds, regular income bonds, deep discount bonds, and capital gain bonds. The bonds were aimed at meeting the diverse needs of all categories of investors, besides contributing to the widening of the bond market so as to bring the benefits of these securities to even the smallest investors.

a. Capital gains bond - Also called infrastructure bonds incorporated the capital gains tax relaxations under Section 54EA of the Income Tax Act announced in the Union Budget for 1997-98. They are issued for 3 and 7 years maturity. 20 percent rebate was available under Section 88 of the I.T. Act for investors on the amount invested in the capital gains bonds up to a maximum of Rs.70, 000. They can avail benefit under Section 88. The annual interest rate worked out to 13.4 percent while the annual yield came to 20.7 percent.

However, investment through stock invest will not qualify for the rebate. b. Encash Bond – The five-year encash bonds were issued at a face value of Rs.2,000 and can be redeemed at par across the country in 200 cities during 8 months in a year after 12 months. The bond had a step-up interest every year from 12 to 18.5 percent and the annualized yield at maturity for the bond works out to 15.8 percent. The encashing facility, however, is available only to the original bondholders. The bonds not only offer higher return but also help widen the banking facilities to investors. The secondary market price of the bonds is likely to be favorably influenced by the step-up interest that results in an improved YTM every year.

c. Index Bond – It gives the investor both the security of the debt instrument and the potential of the appreciation in the return on the stock market. Priced at Rs.6,000 the index bond has

two parts: Part A is a deep discount bond of the face value of Rs.22,000 issued for a 12 year period. Its calculated yield was 15.26 percent. It also has a call and a put option attached to it assuring the investor a return of Rs.9, 300 after 6 years option is exercised.

Part B is a detachable index warrant issued for 12 years and priced at Rs.2,000. The yield was linked to the BSE SENSEX. The face value of the bond will appreciate the number of times the SENSEX has appreciated. The investors returns will be treated as capital gains.

6. Tax Free Bonds: The salient features of the tax-free Government of India bonds to be issued from October 1, 2002 are as follows: a. Interest rate – The bonds will carry an interest rate of 7 percent. b. Tax exemption – The bonds will be exempt from Income-tax and Wealth-tax. c. Maturity – The bonds will have a maturity period of six years. d. Ceiling –The bonds investment will have no ceiling. e. Tradability - The bonds will not be traded in the secondary market. f. Investors – The eligible investors include individuals and Hindu Undivided Families, NRIs are not eligible for investing in these bonds. g. Issue price Bonds will be issued for a minimum amount of Rs.1,000 and its multiples. h. Maturity value – The cumulative maturity value of the bond will be Rs.1.511 at the end of six years. i. Form of issue – The bonds will be both in demat form as well as in the traditional form of stock certificates. Option once chosen cannot be changed. j. Transferability – Bonds will not be transferable except by way of gift to relatives as defined in the Companies Act. k. Collaterals – The bonds cannot be used as collaterals for obtaining loans from banks, financial institutions and non-banking financial companies. l. Nomination – A sole holder or a sole surviving holder of the bond being an individual can make a nomination.

UNIT 5

Depositary Receipt

A depositary receipt is a negotiable instrument issued by a bank to represent shares in a foreign public company, which allows investors to trade in the global markets.

Understanding Depositary Receipts

Depositary receipts allow investors to invest in companies in foreign countries while trading in a local stock exchange in the investor's home country. It is advantageous to investors since shares are not allowed to leave the home country that they trade in.

Depositary receipts were created to minimize the complications of investing in foreign securities.

Previously, if investors wanted to buy shares in a foreign company, they would need to exchange their money into foreign currency and open a foreign brokerage account. Then, they would be able to purchase shares through the brokerage account on a foreign stock exchange.

The creation of depositary receipts eliminates the entire process and makes it simpler and more convenient for investors to invest in international companies.

How are Depositary Receipts Issued?

An investor needs to contact a broker in a local bank if he/she is interested in purchasing depositary receipts. The local bank in the investor's home country, which is called the depositary bank, will assess the foreign security before making a decision to purchase shares.

The broker in the depositary bank will purchase the shares either on the local stock exchange that it trades in or purchase the shares in the foreign stock exchange by using another broker in a foreign bank, which is also known as the custodian bank.

After purchasing the shares, the depositary bank will request the shares to be delivered to the custodian bank.

After the custodian bank receives the shares, they will group the shares into packets, each consisting of 10 shares. Each packet will be issued to the depositary bank as a depositary receipt that is traded on the bank's local stock exchange.

When the depositary bank receives the depositary receipts from the custodian bank, it notifies the broker, who will deliver it to the investor and debits fees from the investor's account.

Types of Depositary Receipts

1. **American Depositary Receipt (ADR)**

It is listed only on American stock exchanges (i.e., NYSE, AMEX, NASDAQ) and can only be traded in the U.S. They pay investors dividends in U.S. dollars and are issued by a bank in the U.S.

ADRs are categorized into sponsored and unsponsored, which are then grouped into one of three levels.

2. **European Depositary Receipt (EDR)**

It is the European equivalent of ADRs. Similarly, EDRs are only listed on European stock exchanges and can only be traded in Europe. It pays dividends in euros and can be traded like a regular stock.

3. Global Depositary Receipt (GDR)

It is a general term for a depositary receipt that consists of shares from a foreign company. Therefore, any depositary receipt that did not originate from your home country is called a GDR.

Many other countries around the world, such as India, Russia, the Philippines, and Singapore also offer depositary receipts.

Advantages of DRs

1. Exposure to international securities

Investors can diversify their investment portfolio by gaining exposure to international securities, in addition to stocks offered by local companies.

2. Additional sources of capital

Depositary receipts provide international companies a way to raise more capital by tapping into the global markets and attracting foreign investors around the world.

3. Less international regulation

Since it is traded on a local stock exchange, investors do not need to worry about international trading policies and global laws.

Although investors will be investing in a company that is in a foreign country, they can still enjoy the same corporate rights, such as being able to vote for the board of directors.

Disadvantages of DRs

1. Higher administrative and processing fees, and taxes

There may be higher administrative and processing fees because you need to compensate for custodial services from the custodian bank. There may also be higher taxes.

For example, ADRs receive the same capital gains and dividend taxes as other stocks in the U.S. However, the investor is subject to the foreign country's taxes and regulations aside from regular taxes in the U.S.

2. Greater risk from forex exchange rate fluctuations

There is a higher risk due to volatility in foreign currency exchange rates. For example, if an investor purchases a depositary receipt that represents shares in a British company, its value will be affected by the exchange rate between the British pound and the currency in the buyer's home country.

3. Limited access for most investors

Sometimes, depositary receipts may not be listed on stock exchanges. Therefore, only institutional investors, which are companies or organizations that execute trades on behalf of clients, can invest in them.

Global Depository Receipt

Definition of Global Depository Receipt

Global Depository Receipt (GDR) is an instrument in which a company located in domestic country issues one or more of its shares or convertibles bonds outside the domestic country. In GDR, an overseas depository bank i.e. bank outside the domestic territory of a company,

issues shares of the company to residents outside the domestic territory. Such shares are in the form of depository receipt or certificate created by overseas the depository bank.

Issue of Global Depository Receipt is one of the most popular ways to tap the global equity markets. A company can raise foreign currency funds by issuing equity shares in a foreign country.

Global Depository Receipt Mechanism

- The domestic company enters into an agreement with the overseas depository bank for the purpose of issue of GDR.
- The overseas depository bank then enters into a custodian agreement with the domestic custodian of such company.
- The domestic custodian holds the equity shares of the company.
- On the instruction of domestic custodian, the overseas depository bank issues shares to foreign investors.
- The whole process is carried out under strict guidelines.
- GDRs are usually denominated in U.S. dollars

Let's now look at the advantages and disadvantages of Global Depository Receipt.

Advantages of GDR

The following are the advantages of Global Depository Receipts:

- GDR provides access to foreign capital markets.
- A company can get itself registered on an overseas stock exchange or over the counter and its shares can be traded in more than one currency.
- GDR expands the global presence of the company which helps in getting international attention and coverage.
- GDR are liquid in nature as they are based on demand and supply which can be regulated.
- The valuation of shares in the domestic market increase, on listing in the international market.
- With GDR, the non-residents can invest in shares of the foreign company.
- GDR can be freely transferred.
- Foreign Institutional investors can buy the shares of company issuing GDR in their country even if they are restricted to buy shares of foreign company.
- GDR increases the shareholders base of the company.

- GDR saves the taxes of an investor. An investor would need to pay tax if he purchases shares in the foreign company, whereas in GDR same is not the case.

Disadvantages

The following are the disadvantages of Global Depository Receipts:

- Violating any regulation can lead to serious consequences against the company.
- Dividends are paid in domestic country's currency which is subject to volatility in the forex market.
- It is mostly beneficial to High Net-Worth Individual (HNI) investors due to their capacity to invest high amount in GDR.
- GDR is one of the expensive sources of finance.

STOCK EXCHANGE

A stock exchange, securities exchange, or bourse is an exchange where stockbrokers and traders can buy and sell securities, such as shares of stock, bonds, and other financial instruments. Stock exchanges may also provide facilities for the issue and redemption of such securities and instruments and capital events including the payment of income and dividends.

Securities traded on a stock exchange include stock issued by listed companies, unit trusts, derivatives, pooled investment products and bonds. Stock exchanges often function as "continuous auction" markets with buyers and sellers consummating transactions via open outcry at a central location such as the floor of the exchange or by using an electronic trading platform.

To be able to trade a security on a certain stock exchange, the security must be listed there. Usually, there is a central location at least for record keeping, but trade is increasingly less linked to a physical place, as modern markets use electronic communication networks, which give them advantages of increased speed and reduced cost of transactions. Trade on an exchange is restricted to brokers who are members of the exchange. In recent years, various other trading venues, such as electronic communication networks, alternative trading systems and "dark pools" have taken much of the trading activity away from traditional stock exchanges.

Initial public offerings of stocks and bonds to investors is done in the primary market and subsequent trading is done in the secondary market. A stock exchange is often the most important component of a stock market. Supply and demand in stock markets are driven by various factors that, as in all free markets, affect the price of stocks (see stock valuation).

There is usually no obligation for stock to be issued through the stock exchange itself, nor must stock be subsequently traded on an exchange. Such trading may be off exchange or over-the-counter. This is the usual way that derivatives and bonds are traded. Increasingly, stock exchanges are part of a global securities market. Stock exchanges also serve an

economic function in providing liquidity to shareholders in providing an efficient means of disposing of shares.

Stock Exchange:

Definition, Meaning & Basics

A stock exchange is a marketplace, where financial securities issued by companies are bought and sold. They are part of the broader capital market ecosystem. Securities issued by companies, such as shares and bonds, are traded on the stock exchanges, after they have been issued in the primary market. A company, desirous of listing its securities on a stock exchange, has to enter into an agreement with the exchange to ensure that its securities are allowed for trading on that particular exchange. Stock exchanges play a key role in creating liquidity for financial securities. Securities trading on stock exchanges, is based on an order matching algorithm, which ensures that the best buy order matches with the best sell order. Stock exchanges ear

HISTORY

The term bourse is derived from the 13th-century inn named "Huis terBeurze" (center) in Bruges. From Dutch-speaking cities of the Low Countries, the term 'beurs' spread to other European states where it was corrupted into 'bourse', 'borsa', 'bolsa', 'börse', etc. In England, too, the term ‘bourse’ was used between 1550 and 1775, eventually giving way to the term ‘royal exchange’.

There is little consensus among scholars as to when corporate stock was first traded. Some see the key event as the Dutch East India Company's founding in 1602, while others point to earlier developments (Bruges, Antwerp in 1531 and in Lyon in 1548). The first book in history of securities exchange, the Confusion of Confusions, was written by the Dutch-Jewish trader Joseph de la Vega and the Amsterdam Stock Exchange is often considered the oldest “modern” securities market in the world.[8] On the other hand, economist Ulrike Malmendier of the University of California at Berkeley argues that a share market existed as far back as ancient Rome, that derives from Etruscan "Argentari". In the Roman Republic, which existed for centuries before the Empire was founded, there were societatespublicanorum, organizations of contractors or leaseholders who performed temple-building and other services for the government. One such service was the feeding of geese on the Capitoline Hill as a reward to the birds after their honking warned of a Gallic invasion in 390 B.C. Participants in such organizations had partes or shares, a concept mentioned various times by the statesman and orator Cicero. In one speech, Cicero mentions "shares that had a very high price at the time". Such evidence, in Malmendier's view, suggests the instruments were tradable, with fluctuating values based on an organization's success. The societas declined into obscurity in the time of the emperors, as most of their services were taken over by direct agents of the state.

Tradable bonds as a commonly used type of security were a more recent innovation, spearheaded by the Italian city-states of the late medieval and early Renaissance periods.

The historian Fernand Braudel said on this matter:

"It is not quite accurate to call [Amsterdam] the first stock market, as people often do. State loan stocks had been negotiable at a very early date in Venice, in Florence before 1328, and in Genoa, where there was an active market in the luoghi and paghe of Casa di San Giorgio, not to mention the Kuxen shares in the German mines which were quoted as early as the fifteenth century at the Leipzig fairs, the Spanish juros, the French rentes sur l'Hotel de Ville (municipal stocks) (1522) or the stock market in the Hanseatic towns from the fifteenth century. The statutes of Verona in 1318 confirm the existence of the settlement or forward market ... In 1428, the jurist Bartolomeo de Bosco protested against the sale of forward loca in Genoa. All evidence points to the Mediterranean as the cradle of the stock market. But what was new in Amsterdam was the volume, the fluidity of the market and publicity it received, and the speculative freedom of transactions."

National Stock Exchange of India Limited (NSE)

The National Stock Exchange of India Limited (NSE) is India's largest financial market. Incorporated in 1992, the NSE has developed into a sophisticated, electronic market, which ranked fourth in the world by equity trading volume. Trading commenced in 1994 with the launch of the wholesale debt market and a cash market segment shortly thereafter.

KEY TAKEAWAYS

- The National Stock Exchange of India Limited (NSE) is India's largest financial market and the fourth largest market by trading volume.
- The National Stock Exchange of India Limited was the first exchange in India to provide modern, fully automated electronic trading.
- The NSE is the largest private wide-area network in India.
- The NSE has been a pioneer in Indian financial markets, being the first electronic limit order book to trade derivatives and ETFs.

Understanding the National Stock Exchange of India Limited (NSE)

Today, the National Stock Exchange of India Limited (NSE) conducts transactions in the wholesale debt, equity, and derivative markets. One of the more popular offerings is the NIFTY 50 Index, which tracks the largest assets in the Indian equity market. US investors can access the index with exchange-traded funds (ETF), such as the iShares India 50 ETF (INDY).

The National Stock Exchange of India Limited was the first exchange in India to provide modern, fully automated electronic trading. It was set up by a group of Indian financial institutions with the goal of bringing greater transparency to the Indian capital market.

Special Considerations

As of June 2020, the National Stock Exchange had accumulated $2.27 trillion in total market capitalization, making it one of the world's largest stock exchange. The flagship index, the NIFTY 50, represents the majority of total market capitalization listed on the exchange.

The total traded value of stocks listed on the index makes up almost half of the traded value of all stocks on the NSE for the last six months. The index itself covers 12 sectors of the Indian economy across 50 stocks. Besides the NIFTY 50 Index, the National Stock Exchange maintains market indices that track various market capitalizations, volatility, specific sectors, and factor strategies.

The National Stock Exchange has been a pioneer in Indian financial markets, being the first electronic limit order book to trade derivatives and ETFs. The exchange supports more than 3,000 Very Small Aperture Terminal (VSAT) terminals, making the NSE the largest private wide-area network in the country. Girish Chandra Chaturvedi is the Chairman of the Board of Directors and Vikram Limaye is the Managing Director and CEO of the exchange.

Benefits of the NSE

The National Stock Exchange is a premier marketplace for companies preparing to list on a major exchange. The sheer volume of trading activity and application of automated systems promotes greater transparency in trade matching and the settlement process.

This in itself can boost visibility in the market and lift investor confidence. Using cutting-edge technology also allows orders to be filled more efficiently, resulting in greater liquidity and accurate prices.

REAL ESTATE FINANCING

INTRODUCTION

The Real Estate financing has become so popular, that the procedure for obtaining a loan has become so simplified that housing loans are easily available. This may be attributed to the change in the housing policy of both the Central and Sate Governments. A redeeming feature of Indian real estate finance is the recent entry of real estate commercial banks in a big way.

REAL ESTATE FINANCING: It is financing for the purchase of real property, where real property refers to land or buildings. Its a set of all financial arrangements that are made available by housing finance institutions to meet the requirements of housing. Housing finance institutions include banks, housing finance companies, special lousing finance institutions, etc.

Factors Determining the Real Estate Finance Assistance:

Real estate finance companies consider the following factors before making any financial assistance for housing: 1. Loan Amount 2. Tenure 3. Administrative and processing costs,

etc. 4. Pre-payment charges 5. Services 6. Value Addition 7. Sources of finance like HFC_s and Banks 8. EMI calculation methods:

1. The Loan Amount The amount of loan that any HFC decides to provide to a loan seeker depends on the following variables: 1. Customers repayment capacity 2. Rate of interest charged 3. Term of the loan

2. Tenure: Repayment it is done through EMI, which includes principal and the interest. As a rule, an HFC fixes the EMI between 30 and 40 percent of the customers gross monthly income, or 50 percent of the net monthly income. For instance, considering a loan of Rs.10, 00,000/- for 10 years, at 13 percent flat interest rate, the EMI would be Rs.19,166.66/-. This way the gross earnings of the loan-seeker must be Rs.54, 761.88 per month, where the instalment to income ratio is 35 percent. The general trend in the market is that customers try to obtain loans for longer tenures, without realizing that the longer the duration the more will be the amount paid by them. An increase in the tenure from 10 to 15 years increases the amount payable by 28 percent. In case the tenure of the loan is decreased from 15 years to 10 years, the monthly EMI becomes Rs.16,388.77/-.

3. Administrative and processing cost: The effective cost of the loan depends on the type of method used by banks or finance companies. Based on the method, the principal component, which is paid monthly, is deducted from the outstanding principal amount. The two methods, which banks and finance companies generally follow, they are:

a. Monthly rest system Under this system, the principal amount is deducted every month from the outstanding amount, and the interest for the following month is calculated on the outstanding amount.

b. Annual rest system Under this system, although the principal amount is paid every month, it is accounted only at the end of the year. This is illustrated as follows: c. Fixed and Floating Rate Customers should check whether the rates offered are fixed or floating (varies with PLR). Floating rates are better in a falling rate scenario, but expensive in an increasing rate scenario. The borrower should check whether it is viable to shift the loan from fixed rate to the floating rate in a decreasing rate scenario by carrying out a cost benefit analysis.

4. Pre-payment Charges: This is an important factor to be considered, especially in situations where the ability to repay the loan matters. There are certain HVCs which charge pre-payment, in case the loan is repaid before schedule. This pushes up the cost of fund of the borrower. Borrowers who desirous of repaying ahead of schedule should approach HFCs which do not have a pre-payment charge.

5. Value addition: The value addition includes the additional or supplementary services that HFCs provide, such as fast disbursals of loan, legal services, meeting with brokers, builders etc., 6. Sources of Finance 1. The National Housing Bank (NHB): The National Housing Bank (NHB) was set up in July 1988, under an Act of Parliament, and is wholly owned by RBI, NHB, at present, has a paid-up capital of Rs.350/- Crores. It was conceived and promoted to function as the apex institution in the housing sector. The need to set up this institution stemmed from the fact that the housing sector had not received the attention it

required, not only in terms of finance for individual loans, but also in terms of buildable or serviced land, building materials and cost effective technology. Loan Amount (Rs.) Tenure (Years) Interest (%) EMI (Rs.) Total Payment

Hire Purchase System

Hire Purchase System is a special system of purchase and sale. When goods are purchased on hire-purchase system, purchaser pays the price in instalments, these instalments may be Monthly, Quarterly or Yearly etc. Goods are delivered to the purchaser at the time of Hire Purchase Agreement but purchaser will become the owner of goods only on the payment of the last instalments. All the instalments paid are treated as hire till the last instalment is paid off.

Under the Hire-purchase system, goods are delivered to a person who agrees to pay the owner by equal periodical instalments, such instalments are to be treated as hire of these goods until a certain fixed amount has been paid, when these goods become the property of the hire.

Hire Purchase Agreement [Section 2]:

Hire purchase agreement means an agreement under the which goods are let on hire and under which the hire has an option to purchase them in accordance with the terms of the agreement and includes the agreement under which:

1. Possession of goods is delivered by the owner thereof to a person or condition that such person pays the agreed amount in periodical instalments.
2. The property in the goods is to pass to such a person on the payment of the last instalment and
3. Such a person has a right to terminate the agreement at any time before the property so passes. Every Hire Purchase Agreement shall be in writing and signed by all the parties thereto.

Characteristics of Hire Purchase System

1. Goods are delivered by the seller to the buyer.
2. Buyer agrees to pay hire purchase price (i.e., cash price + interest) in
3. Instalments paid are treated as hire charges till the payment of the last instalment.
4. After the payment of the last instalment, ownership is transferred in the name of the buyer.

In the case of default, in the payment by the buyer, the seller has got a right to repossess the goods, as ownership lies with the seller, till the payment of last instalment.

FACTORING

Peter M. Biscose defines the term Factoringin his treatise Law and Practice of Credit Factoring as a continuing legal relationship between a financial institution (the factor) and a business concern (the client) selling goods or providing services to trade customers, whereby the factory purchases the clients_ book debts, either with or without recourse to the client,

and in relation thereto, controls the credit extended to customers, and administers the sales ledger.

C.S. Kalyansundaram, in his report (1988) submitted to the RBI defines factoring as, ―a continuing arrangement under which a financing institution assumes he credit and collection functions for its client, purchases receivables as they arise (with or without recourse for credit losses, i.e., the customers financial inability to pay), maintains the sales ledger, attends to other book-keeping duties relating to such accounts, and performs other auxiliary functions. According to the study Group appointed by the International Institute for the Unification of Private Law (UNIDROTT), Rome, 1988".

A domestic factoring means an arrangement between a Factor and his client, which includes at least two of the following services to be provided by the Factor. a. Finance b. Maintenance of accounts c. Collection of debts d. Protection against credit risk. Factoring is a receivables management and financing mechanism which is designed to improve cash flows and cover the credit risk of the seller. Unlike other forms of receivables financing, like bills discounting and forfeiting; factoring involves a continuous relationship between a factor and a seller, to finance and administer the receivables of the latter. Factors are financial companies which pay cash against the credit sales of the client, and obtain the right to receive the future payments on those invoices from the debtors of the client.

Functions of a factor Factoring

Constitutes a suite of financial services offered under a factoring agreement, which includes receivables financing, credit protection, accounts receivables collection and management, sales ledger administration and advisory services.

I.Receivables financing: The factoring institution advances a proportion of the value of the book debts immediately to the client and the balance is paid on maturity of the book debts. This improves the cash flow position of the client, by replacing the credit sales for cash.

II. Credit protection: The factoring institution takes over the credit risk of the client, and agrees to bear the loss in case of default by the debtor. Credit protection is provided by the factor only in case of non-recourse factoring.

III. Accounts receivables collection and management: The factoring company collects the receivables of the client and also manages the credit collection schedule. By reducing the time invested by the client in such activities, it allows the client to focus on business development.

IV. Sales Ledger management: The factor undertakes sales ledger management, including maintenance of credit records, collection schedules, discounts allowed and ascertainment of balance due from all debtors.

V. Advisory Services: A factoring company advises the client on its export and import potential, and also helps the client in identification and selection of potential trade debtors, based on the credit information available with it. The factor also advises on the prevailing

business trends, Policies, impending developments in the commercial and industrial sector etc.

Factoring mechanism

The parties involved in a factoring arrangement are:

1. The Client, or the seller

2. The Debtor, or the buyer

3. The Factor (International factoring may have a correspondent factor in addition to the domestic factor)

Detailed Steps:

1. Client approaches Factor Company and requests for factoring facility.

2. Factor asks for Client's financial statements (last three years balance sheet).

3. Client fills the application form and submits his last three years financial statements.

4. Factor company conducts Client appraisal by conducting his credit assessment on the quantitative (this includes analysis of current ratios, gearing ratios, profitability ratios, etc.) and qualitative parameters such as integrity, management etc and approves/ disapproves client request.

5. Once approved, the Factor Company assigns overall factoring limit to the client. The client is required to submit sales ledger of his customers to the factor, who assesses the customers to determine limit of sanction according to the quality of customers.

6. Bank NOC / Letter of Disclaimer (LOD) are called for after sanction of limit but before Operationalisation of the account.

7. In case of approval of client request, client is asked to submit following documents: a. documents for collateral, if any b. Personal guarantee of directors, etc

8. Factor Company examines the sales ledgers of client 's customers and conducts Buyers'due diligence. For this, it seeks bank reports, credit reports from credit bureaus, D&B report, etc.

9. Based on the credit assessment of each customer of the client, Factor company sets credit limits for each customer.

10. Factor Company grants in-house approval.

11. Factoring Company is required to send letter of notification to the clients buyers and the buyers are required to accept the same and send it to the factor company.

12. A factoring agreement is signed between the client and the factoring company.

13. Client is required to submit original invoices with assignment clause written on these and proof of delivery of these invoices.

14. Factor Company makes advance prepayment (Up to 80% of invoice value).

15. Factoring company manages client‘s ledger, sends due date reminders to client‘s customers and collects payments as and when due.

16. Factoring company uses appropriate software to manage the above processes.

17. Factoring company pays balance due to the client upon receipt of full payment.

Detailed Steps in International Factoring (Two Factor Model)

1. The importer places the order for purchase of goods with the exporter

2. The exporter approaches the export factor (in the exporter‘s country) for limit approval on the importer. Export Factor in turn requests the import factor in the Importer's country for the arrangement

3. The import factor assesses the importer and approves/rejects the arrangement and accordingly conveys to the export factor

4. Exporter is informed of the commencement or otherwise, of the factoring arrangement

5. The exporter delivers the goods to the importer

6. Exporter produces the documents to the export factor

7. The export factor disburses funds to the exporter up to the prepayment amount and forwards the documents to the Import factor as well as the Importer

8. On the due date of the invoice, the Importer pays the Import Factor, who in turn remits the payment to the export factor.

9. The exporter receives the balance payment from the export factor. Charges applicable Usually, a onetime setup fee, a service fee and an interest charge is levied for a factoring transaction.

The service fee is levied for the additional services of the factor, besides financing. It is calculated as a percentage of the gross value of the invoices factored, and is based on: I. The gross sales volume II. The number of customers/debtors of the client III. The number of invoices and credit notes IV.

The characteristics of Factoring are as follows:

1. The Nature The nature of the Factoring contract is similar to that of a bailment contract. Factoring is a specialized activity whereby a firm converts its receivables into cash by selling them to a factoring organization. The Factor assumes the risk associated with the collection of receivables, and in the event of non-payment by the customers/debtors, bears the risk of a bad debt loss.

2. The Form Factoring takes the form of a typical Invoice Factoringsince it covers only those receivables which are not supported by negotiable instruments, such as bills of exchange, etc. This is because, the firm resorts to the practice of bill discounting with its banks, in the event

of receivables being backed by bills. Factoring of receivables helps the client do away with the credit department, and the debtors of the firm become the debtors of the Factor.

3. The Assignment Under factoring, there is an assignment of debt in favour of the Factor. This is the basic requirement for the working of a factoring service.

4. Fiduciary Position The position of the Factor is fiduciary in nature, since it arises from the relationship with the client firm. The factor is mainly responsible for fulfilling the terms of the contract between the parties.

5. Professionalism Factoring firms are professionally competent, with skilled persons to handle credit sales realizations for different clients in different trades, for better credit management.

6. Credit Realizations Factors assist in realization of credit sales. They help in avoiding the risk of bad debt loss, which might arise otherwise.

7. Less Dependence Factors help in reducing the dependence on bank finance towards working capital. This greatly relieves the firm of the burden of finding financial facility.

8. Recourse Factoring: Factoring may be non-recourse; in which case the Factor will have no recourse to the supplier on non-payment from the customer. Factoring may also be with recourse, in which case the Factor will have recourse to the seller in the event of non-payment by the buyers.

9. Compensation A Factor works in return for a service charge calculated on the turnover. Actor pays the net amount after deducting the necessary chares, some of which may be special terms to handle the accounts of certain customers.

Types of Factoring

Factors take different forms, depending upon the type of specials features attached to them. Following are the important forms of factoring arrangements:

1. Domestic Factoring: Factoring that arises from transactions relating to domestic sales is known as Domestic Factoring_. Domestic Factoring may be of three types, as described below.

2. Disclosed factoring: In the case of disclosed factoringthe name of the proposed actor is mentioned on the face of the invoice made out by the seller of goods. In this type of factoring, the payment has to be made by the buyer directly to the Factor named in the invoice. The arrangement for factoring may take the form of recourse, whereby the supplier may continue to bear the risk of non-payment by the buyer without passing it on to the Factor. In the case of nonrecourse factoring, Factor, assumes the risk of bad debt arising from non-payment.

3. Undisclosed factoring: Under undisclosed factoring, the name of the proposed Factor finds no mention on the invoice made out by the seller of goods. Although the controls of all monies remain with the Factory, the entire realization of the sales transaction is done in the name of the seller. This type of factoring is quite popular in the UK.

4. Discount factoring: Discount Factorings a process where the Factor discounts the invoices of the seller at a pre-agreed credit limit with the institutions providing finance. Book debts and receivables serve as securities for obtaining financial accommodation.

5. Export Factoring: When the claims of an exporter are assigned to a banker or any financial institution, and financial assistance is obtained on the strength of export documents and guaranteed payments, it is called export factoring. An important feature of this type of factoring is that the Factor bank is located in the country of the exporter. If the importer does not honour claims, exporter has to make payment to the Factor. The Factor-bank admits a usual advance of 50 to 75 percent of the export claims as advance. Export factoring is offered both as a re-course and as a non-recoursefactoring.

6. Cross-border Factoring: Cross-border Factoring_ involves the claims of an exporter which are assigned to a banker or any financial institution in the importers country and financial assistance is obtained on the strength of the export documents and guaranteed payments. International factoring essentially works on a non-recourse factoring model. They handle exporters overseas sales on credit terms. Complete protection is provided to the clients (exporter against bad debt loss on credit-approved sales. The Factors take requisite assistance and avail the facilities provided for export promotion by the exporting country. When once documentation is complete, and goods have been shipped, the Factor becomes the sole debtor to the exporter.

7. Full-service Factoring: Full-service factoring, also known as Old-line factoring, is a type of factoring whereby the Factor has no recourse to the seller in the event of the failure of the buyers to make prompt payment of their dues to the Factor, which might result from financial inability/ insolvency/bankruptcy of the buyer. It is a comprehensive form of factoring that combines the features of almost all factoring services, especially those of non-recourse and advance factoring.

8. With Recourse Factoring: The salient features of the type of factoring arrangement are as follows 1. The Factor has recourse to the client firm in the event of the book debts purchased becoming irrecoverable 2. The Factor assumes no credit risks associated with the receivables 3. If the consumer defaults in payment, the resulting bad debts loss shall be met by the firm 4. The Factor becomes entitled to recover dues from the amount paid in advance if the customer commits a default on maturity 5. The Factor charges the client for services rendered to the client, such as maintaining sales ledger, collecting customer‘s debt, etc.

9. Without Recourse Factoring: The salient features of this type of factoring are as follows: 1. No right with the Factor to have recourse to the client 2. The Factor bears the loss arising out of irrecoverable receivables 3. The Factor charges higher commission called del credere commission_ as a compensation for the said loss 4. The Factor actively involves in the process of grant of credit and the extension of line of credit to the customers of the client

10. Advance and Maturity Factoring: The essential features of this type of factoring are as follows: 1. The Factor makes an advance payment in the range of 70 to 80 percent of the receivables factored and approved from the client, the balance amount being payable after collecting from customers 2. The Factor collects interest on the advance payment from the

client 3. The Factor considers such conditions as the prevailing short-term rate, the financial standing of the client and the volume of turnover while determining the rate of interest

11. Bank Participation Factoring: It is variation of advance and maturity factoring. Under this type of factoring, the Factor arranges a part of the advance to the clients through the banker. The net Factor advance will be calculated as follows: (Factor Advance Percent x Bank Advance Percent)

12. Collection / Maturing Factoring: Under this type of factoring, the Factor makes no advancement of finance to the client. The Factor makes payment either on the guaranteed payment date or on the date of collection, the guaranteed payment date being fixed after taking into account the previous ledger experience of the client and the date of collection being reckoned after the due date of the invoice.

CREDIT CARDS

INTRODUCTION

The commercial banks extend different functions to customers. The most important in the modern days are credit card facilities to customers. These facilities are not extended to not only customers in the urban areas or cities but also to customers residing in rural areas. Agriculturist are enjoying the facility of credit card and the card extended to them are called as green card. A credit card is given by the banker to the customer in which the name of the customer is embossed in block letters. The name of the bank and the date of issue and expiry are also mentioned on the face of the card. The reverse side of the card will bear the specimen signature of the customer. A list of vendors or sellers will be gibe by the banker to the customers. A credit card is a thin plastic card, usually 3 1/8 inches x 2 1/8 inches in size that contains identification information such as signature or picture or both and authorizes the person named on it to charge for purchases or services to his account. In addition to this, the card can be used in automated teller machines for withdrawing cash and the machine stores the information and also transactions through electronic date processing system.

Origin of Credit Cards in India:

The usage of Credit Cards in India is less when compared to the usage of credit cards in China, Taiwan and Malaysia. It picked up only in the last 10 years until then the Indian looked it as a luxury. The idea of owning a credit card has had its roots in the minds of millions of Indians. They started viewing the card as a convenient substitute to carrying cash. The change in mindset is clear from the growth, both in terms of absolute numbers and growth rates. The industry has grown at the rate of 30% and strongly counts for steady years to come. Credit Cards in India: According to Visa International an average Indian cardholder uses his card 9.3 times, spending about Rs.23, 000 per year. A number of card owners do not use their cards and almost 20-23% cards are inactive. In India, two players dominate the credit cards industry. Visa and Master Cards and 15 out of 17 banks provide credit card services through Visa or Master Cards. The importance of having a pie in the credit cards segment was not lost on any bank, and most banks started their credit card operations. Currently, there are more than 20 banks offering credit cards, but the market share of the top

five exceeds 75%. Credit card is a low margin, high volume business. The initial investments required by a bank are very high. The income per card is low, thereby requiring large volumes in terms of cards issued and the transactions finance to make the operations profitable. Another reason for the inability of players to upstage the well-entrenched ones is lower patronage by the merchant and business outfits. The bigger businesses and merchants are already acquired by the existing players, so far new banks, braking into this business and convincing a merchant is increasing because the banks are shifting towards lower end merchants. Secondly, because of competition in acquiring business, new categories of merchants are coming up. The foreign banks have a dominant share due to various reasons like having been in the field for decades, sound operational and financial strength, strong brand recognition etc. They were catering to the upper segments and charged high annual fees. Later, with aggressive entry of SBI, ICICI Bank and HDFC Bank, the rules of the game changed. The cards were positioned in manners which gave an impression that the cards can be acquired by people from not only the upper class, but also the middle-income categories. This was the strategy followed by SBI-GE as a result of which it is the third largest issuer of credit cards today. It positioned itself in a segment as to be of mass appeal and at the same time reinforced a clean and dependable image of the bank. The new private banks like ICICI and HDFC are also aggressively increasing their share. They adopted a strategy of reaching lower down the income strata by lowering down their eligibility norms. Of course, the credit limits are set at lower levels as compared to the foreign banks. As a result of this strategy, the credit cards base is widening day by day with the increase of base in B-grade cities.

Types of Credit Cardsor Types of Cards:

1. Charge Card 2. Debit Card 3. Deferred Debit card 4. Affinity card 5. Standard card 6. Classic card 7. Gold card 8. Platinum card 9. Best Platinum credit card 10. Fleet Platinum credit card 11. Next card Platinum credit card 12. Titanium card 13. Secured card 14. Smart card

1. Charge card in this card, the cardholder has to make full payment of the charge by the due date. Unlike other credit cards, here dues are not allowed to carry forward. It is meant for people who spend responsibly.

2. Debit Card: A debit card is different from credit card. Debit card is issued by a bank. The following are the differences between credit and debit cards:

3. Deferred debit card: When a debit card carries the benefit of the credit card, allowing the payment after certain period, it is called deferred debit card. Credit Card Debit Card 1 It is issued by an agency such as Master or Visa

1. A debit card is issued by a bank in which the customer has an account.

2. A credit card allows certain period for making payment for the purchases made which may vary from 30 to 45 days. 2. The bank account in a debit card is debited immediately the moment the card is used. They have no credit period.

3. The credit worthiness of the customer is based on income eligibility criteria on the basis of which the credit card is issued. 3. There are no such income criteria but the credit balance, maintained in the account is the criterion.

4. A credit card holder has a ceiling limit for his purchases and also for his cash withdrawals through ATM.

5. A debit card holder has his purchases restricted to his credit Balance.

6. Credit card can be used for withdrawing money only from ATMs.

7. A debit card can be used even for withdrawing money from the bank and hence it is account holders_ mobile

8. When the purchase are made by using The Credit Card, the retail seller swipes the card over an electronic terminal at his outlet, and enters the personal identification number (PIN) and the transactions are recorded by the card issuing authority.

9. Any use of debit card by a similar method will be immediately recorded by the bank and the account of the customer is debited. Thus, it is an online transaction.

10. Loss of credit card should be reported to the issuing agency.

11. Loss of debit card should be reported to The issuing bank.

4. Affinity card: A card offered by two organizations of which one is a lending institution and the other a non-financial group. Here, schools, non-profit groups, airlines, petroleum companies issue affinity cards. These cards carry special discounts.

5. Standard Card: It is a normal credit card which carries limit on transactions, according to the credit worthiness of the card holder.

6. Classic card: A credit card issues by Visa, carrying the logo of Visa.

7. Gold card: A higher line of credit is given than a standard card. The income eligibility for getting this card is higher. Gold card is given to very rich customers or persons with high social status.

8. Platinum card: In order to distinguish credit cards belonging to certain companies, platinum credit cards are issued. Some companies use these to denote their best premium credit card.

9. Best Platinum credit card: Companies which set highest standard in customer service issue these cards. There is lowest interest rate for the outstanding, and the cards will have no annual fee or application fee and can be applied online in seconds.

10. Fleet Platinum credit card: It is a zero liability guarantee for purchases. It protects the credit card holder from any unauthorized use.

11. Next card platinum credit card: This is given to those with a good credit and it offers a low introductory rate.

12. Titanium card: A card which has a higher credit limit than a platinum card.

13. Secured card: A credit card is given to a card holder who has Savings deposit which will take care of his outstanding balance, in case of his default on payment.

14. Smart card: The revolution in Information Technology is responsible for the invention of Smart card. The development in semiconductors has advanced so much that computing power that was available in a computer matching a room size in the early days, is now available on a visiting card-sized plastic.

Kit is an embedded micro-chip card and it can store 1280 times more data than the magnetic strip card. The can store data for more than 10 years and can be read or written for more than 1 lakh times. For example: Visa is converting 22 million Brazilian debt and credit cards to Smart cards. Sim card in the mobile phone is an example for the use of Smart cards in the telecom sector.

There are 3 types of Smart cards. 1. Storage/memory cards 2. Intelligent cards and 3. Hybrid cards. • Storage card has an inherent monetary value associated with it._ • Intelligent card acts as a store-house of information. • Hybrid card contains a micro processor chip and a magnetic strip and bar coding.

Benefits of Credit Cards Benefits derived from credit card

The following persons derives benefits from the credit card system: (1) Customer (2) Seller (3) Wholesaler (4) Manufacturer (5) Commercial banks (6) Central bank (7) Government (8) Economy

1. Customer i. A customer can make purchases at any time ii. One need not carry cash for making purchases iii. In case of losing credit card, one can immediately inform the bank and prevent misuse by others iv. One can take benefit of lower prices by purchasing goods before the hike in prices. v. During inflation period, credit card benefits customers as the payments are made after one month from the date of purchase. vi. Railway ticket or Air ticket reservation can be done by using credit card even during night when banking facility is not available. vii. Credit card can be used even through computers and purchases can be made by sitting at home. viii. More customers will come forward to avail banking facility ix. At any point of time, the customer will be able to know the available credit even after purchases. x. Credit card can be used even for withdrawing cash through ATM (Automatic Teller Machine) up to a certain limit. xi. The holders of credit card are given insurance cover by the banks.

(2) Seller The benefits to seller are as follows: i. Sales are affected throughout the year. ii. With increasing sales, the turnover of the seller increases. iii. The seller can go for competitive price as he can get credit from the bank. iv. Due to credit card facility, he can attract customers from far off places also. v. Durable goods can be sold easily through credit card. vi. Bad debts can be avoided as the bank arranges for payment under credit card. vii.

Sellers extending sales through credit card can also extend additional credit to customers as they can receive payment in installment through the credit card.

(3) Wholesaler i. The wholesaler will be getting more orders from the retailer as the sales will go up due to credit card. ii. The wholesaler will be dealing products of different manufacturers due to credit extended by them iii. The wholesaler will also be given credit by the banks. iv. The wholesaler will be able to place orders throughout the year and hence can get trade credit as well as cash credit from the manufacturers.

(4) Manufacturer i. With orders continuously received from the wholesalers, the manufacturer can increase his production. ii. Due to large scale production, the cost of production will come down and the manufacturer will be able to sell at a lower price. iii. Since the orders are received throughout the year, there will be continuous production even for goods which are seasonal in nature. Example: Manufacture of umbrellas. iv. The manufacturer will also diversify his production due to the goodwill he has enjoyed due to increased production. v. The profit of the manufacturer will also increase and he will extend a higher commission to his wholesalers.

(5) Commercial banks Due to credit card facility i. More customers will avail the banking facility. ii. There will not be cash withdrawals from the bank as most of the customers use credit card for their purchase. iii. The bank, by extending credit to customer, retailer, wholesaler and manufacturer is able to earn interest on the credit. iv. The credit facility is extended only in the books of accounts and there will be no cash withdrawals. The account of the customer is debited for the purchases while the account of the seller is credited. Both the parties are given credit and the bank enjoys interest on the loan. v. All the transactions in the country are done through the banking system, as a result of which, the role of money lenders and other financiers is reduced. vi. The profit of the bank will also increase due to the extension of credit to different parties.

(6) Central bank: It is a national bank that provides financial and banking service for its country government and commercial banking system and issues currency. Central bank for India is Reserve Bank of India. i. A better control on the banking system is evolved by the Central bank. ii. During inflation, the Central bank can control the price level by instructing the head office of commercial banks to reduce the quantum of credit extended to customers under credit card. This will reduce the demand and thereby prices will come down. iii. Central bank is able to take instantaneous action on the economy as credit card provides information regarding purchases and sale in the country. iv. The activity of Non-Banking Financial Companies will also be reduced due to the credit card facility extended by commercial banks. So, the Central bank need not control NBFCS. v. By extending credit card facility to agriculturists, agricultural finance is improved and this relieves the farmers from the clutches of money lenders.

(7) Government: Whenever any sale is made, it is properly billed. That means sales tax; commercial tax due to the government will not be evaded. ii. It prevents the growth of unaccounted money as all transactions are recorded. iii. It improves the revenue of the government due to increase in production by the manufacturers. Excise duty will be paid to

the government. iv. Government employees can also avail credit card facility against their salaries.

(8) Economy: Economy gets benefited in all its different sectors like primary, secondary and territory sectors. . Transport system will improve with movement of goods to different places. Exports will improve, increasing the earnings of foreign exchange. Employment opportunities will increase not only in production centres but also in the service sector. Marketing will develop with increasing advertisements. Stiff competition will bring out good products for the benefit of consumers. Credit card which was considered to be a luxury has become one of necessity. It was considered to be used only by higher income group. But today, with development in banking and trading activities, fixed income group or salaried class has also started using the same. There may be the criticism that it induces far more purchases or makes people Spend-thrift. This may be so in the initial stage, but when once a customer gets used to the credit card, he/she will know how to use the same in a discretionary manner.

VENTURE CAPITAL

INTRODUCTION

An entrepreneur, with a good technical knowledge, raising of capital in the conventional method will be very difficult. So, by a new technique of financing, long term capital is provided to small and medium sector through an institutional mechanism. So capital assistance against high growth oriented along with managerial assistance was felt necessary. This gave to the birth of Venture Capital Assistance. VENTURE A business enterprise involving considerable risk.

Meaning of Venture Capital:

It is a long term capital invested in companies which involves high risk. The financing involves high risk but is compensated by high return.

FEATURES OF VENTURE CAPITAL

The following are the features of venture capital 1. It is the financing of capital for new companies. 2. This finance can also be loan-based or in convertible debentures 3. Providers of venture capital aim at capital gain due to the success achieved by the borrowing concern. 4. Venture capital is always a long-term investment and made in companies which have high growth potential. 5. The venture capital provider take part in the business of borrowing concern simultaneously provides managerial skill. 6. Venture capital financing contains risks. But the risk is compensated with a higher return. 7. It involves financing mainly small and medium size firms, which are in their early stages. When the assistance of venture capital, these firms will stabilize and later can go in for traditional finance.

Objectives of Venture Capital

• To finance new companies who find it difficult to go to capital market • To provide long term finance to small and medium scale industries • To provide managerial assistance • To bring in rapid growth in the business

Financing By Venture Capital Institutions:

Before going in for venture capital finance, the venture capital institution will have to assess the potentiality of the borrowing concern by a proper appraisal. This appraisal will be similar to the project appraisal undertaken by commercial banks. There are three stages involved in the venture capital finance.

Stages/Process

1. Seed capital It is the capital provided for testing the product and examining the commercial viability of the product. It enables the venture capital institution to find out the technical skill of the borrowing concern and its market potentially. So, we can say seed capital is more of a product development and all the finance required at this stage is provided by the venture capital institution.

2. Start up Start up of the product refers to the tested in the market and after being satisfied with its acceptability by the market, financing will be provided for further development of the product and marketing of the product. The startup may be classified into four categories: 1. A new high technology, introduced by the entrepreneur. 2. A new business started by an entrepreneur who has a thorough working knowledge and experience – normally started by persons who were working in an established firm and having gained sufficient experience.

3. New projects started by existing companies. Example: Retail business started by Hindustan Lever Limited.

4. A new company promoted by existing company. Here, the venture capital institution is keen to have a first-rated management which may have a second rated product. But not vice versa i.e., venture capital will not be provided for a concern having a second-rated management but a first-quality product. 3. Second round finance It is the second round of finance after the initial stage after being commercially successful for want of some more finance. 4. Later stage financing It is the financing after second round finance. The business concern which has borrowed venture capital has now become a well-established business. But still, it is not able to go in for public issue of shares. At this stage, the venture capital institution will provide finance.

5. Messanine capital This is a stage where the borrowing company is not only well established but has overcome the risks and has started earning profits. But they have to go for some more year before reaching the stage of self-sustenance. This finance is used by the borrowing company for purchase of plant and machinery, repayment of past debts, and entering new areas.

6. Bridge capital A capital of medium-term finance ranging from one to three years and used for extending a business Example: bridge loan for acquiring other firms.

7. Management Buy-outs (MBO) It is the capital used for acquiring all the shares and the voting rights to remove external control. Example: An Indian company's shares may be purchased by NRIs at the initial stage and after sometime these shares are bought back by the company with the help of profits and finance by venture capital institutions.

8. Management buy-in (MBI) Management buy in is the case where the funds are provided for an outside group to buy an ongoing company.

9. Turn Around Turn around may be Financial Turnaround: When the company is able to improve its conditions financially, it is called financial turnaround, which is due to the financial assistance by venture capital institution. Management Turn around: similarly, when the management of the company makes a turn around by becoming self dependent and is able to face the challenges of business, it is called management turn around.

Venture Capital in India

The venture capital institutions (VCIs) in India can be broadly classified into 5 types.

1.Venture Capital companies promoted by Development Banks 2. State level Venture capital companies 3. Commercial banks promoted Venture capital companies 4. Private sector Venture capital companies 5. Foreign venture Capital funds. 1. VC companies promoted by Development banks a) IDBI – VFC (Venture Fund Company) : IDBI promoted venture fund company in the year 1986.

It is promoted by the Technology Development Wing of IDBI. b) TDICI - Technology Development and Information company of India Ltd. This was started in January 1988 with the support of ICICI and UTI. This is the country_s first venture fund (Venture Capital Unit Scheme). It was started with an initial fund of Rs.20 Crores and it has financed nearly 37 small and medium scale enterprises. At present, it has a total fund of Rs.120 crores. The initial fund has yielded a return of Rs.16 crores. c) RCTC – Risk Capital and Technology Finance Corporation Ltd: It is a subsidiary of IFCI, started in January 1988. Its resource base has Rs.30 crores which has contributions from UTI, IFCI and World Bank. 2. State level Venture Capital companies There are two state-level venture fund companies in India.

They are 1. Gujarat Venture Finance Ltd. 2. Andhra Pradesh Venture Capital Limited (AVCL). Gujarat Venture Finance Ltd: Gujarat Industries Investment Corporation Ltd., along with Gujarat Lease Finance Corporation Ltd., Gujarat Alkalies& Chemicals Ltd., and Gujarat State Fertilizer Ltd., promoted Gujarat Venture finance Ltd. It has a venture fund of Rs.24 crores and was started in 1990. Andhra Pradesh Venture Capital Limited (AVCL): This was promoted by APIDC (Andhra Pradesh Industrial Development Corporation), IDBI, Andhra Bank and Indian Overseas Bank. 3. Venture Capital Companies promoted by Commercial Banks Notable among the venture companies promoted by the commercial banks i. Canara Bank venture Capital Fund (CVCF) : ii. Grind lays Bank has promoted India Investment Fund and Second India Investment Fund. iii. SBI Capital Venture Capital Fund. 4. Private sector Venture Capital companies in private sector, we have Larazd Credit Capital Venture Fund and Indus Venture Management Ltd. (IVML). 5. Foreign Venture Capital funds The Hong Kong Bank has promoted venture fund. Alliance Capital of U.S.A. has also promoted venture capital fund.

Guidelines For Providing Venture Capital: The venture capital companies have been given certain guidelines for providing venture capital. Accordingly, the venture capital companies must obtain a detailed report from the borrowing company. The report should contain the following details: - 1. History of the borrowing company 2. Available facility for the borrowing company 3. Description of the products manufactured by the company 4. Market trend of the products 5. Cash flow position of the concern 6. Operating profit 7. Key personnel. It takes about 6 months for a venture capital company to process the application during which period, aspects such as the organizational structure, competition for the company's product, etc., are studied.

Investment Pattern In Venture Capital:

The investment plan will consist of 3 stages – a). Basic stage b). Operating stage c). Exit stage

• Basic stage involves the study and evaluation of the project.

• Operating stage deals with monitoring the functioning of the management of the borrowing concerns and advice for providing new round of finance. In the course of studying the managerial skill, the following aspects will be taken a) product quality b) Market size c) rate of return d) venture location e) growth potential f) state of entrepreneur

• Exit stage – The borrowing company may be sold to a third party or the company may be left to look after itself. While studying the managerial skill, he following aspects will be taken: a) Product quality b) Market size c) Rate of return d) Venture location e) Growth potential f) State of entrepreneur