



IIM Vishakhapatnam  
Executive Certificate Program in Business Finance & Financial Modelling

# Investment Banking

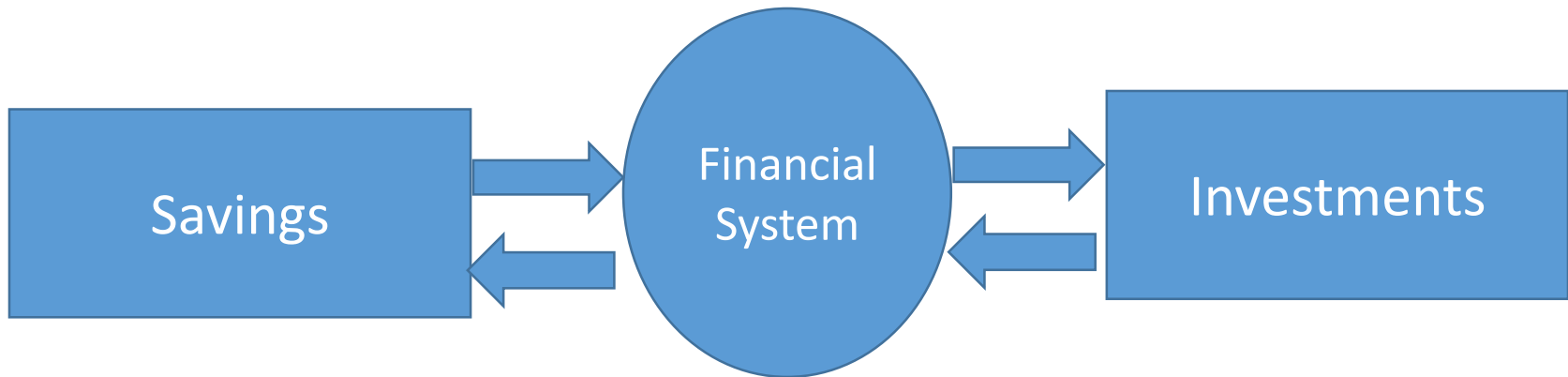
Amol Agrawal  
Ahmedabad University

Picture associated with i-banking



# Flashback

- We reviewed working of financial system
- We said financial system intermediates savings from surplus units and gives it to deficit units. The deficit units in turn invest the savings and give returns in form of dividend, interest etc.



# Flashback

- Financial System comprises different kinds of institutions that intermediate these savings
  - Commercial Banks
  - Investment Banks or Merchant Banks
  - Mutual Funds
  - Insurance
  - Pension Funds
- We will study Investment Banks in this session.

# Difference between Commercial Banks and Investment Banks

- Commercial Banks
- Fund based business
  - Take Savings from savers as Deposits
  - Give Loans to the investors
- Income of the bank
  - Loan interest rate minus deposit interest rate

# Difference between Commercial Banks and Investment Banks

- Investment Banks
  - Also take funds from surplus savers
  - Provide these funds to deficit investors
- However, they don't take deposits or give loans
- Instead they help companies issue shares & bonds which are invested by the savers.
- IB is mainly a fee Based business
  - They get fee from offering companies multiple services

# Fee Activities of I-Banks

- Capital raising for companies
  - Equity: Initial Public Offer, Offer for Sale, Private Placement
  - Debt: Debentures, Bonds, Private Placement
- Underwriting
- Mergers and Acquisitions
- Financial consultancy
- Sales and Trading
- Brokerage Services
- Investments
- Research

# Capital raising for companies - Equity

- If you 've ever bought stock in a company, be it an individual firm like Microsoft or an index fund that invests in companies in the Standard & Poor ' s (S&P) 500, you 've been on the investor end of an equity deal.
- Investment bankers help companies raise money by selling ownership stakes, or equity, in the company to outside investors.
- After the securities are sold by the investment bank, the owners are free to buy or sell them on the stock market.
- Equity is first sold as part of an equity offering called an initial public offering (IPO).

# IPO, FPO, OFS

- Initial Public Offer: New shares issued by a company
- Follow-up Public Offer: New Shares issues by an existing company
- Offer for Sale: Existing shareholders sell their shares

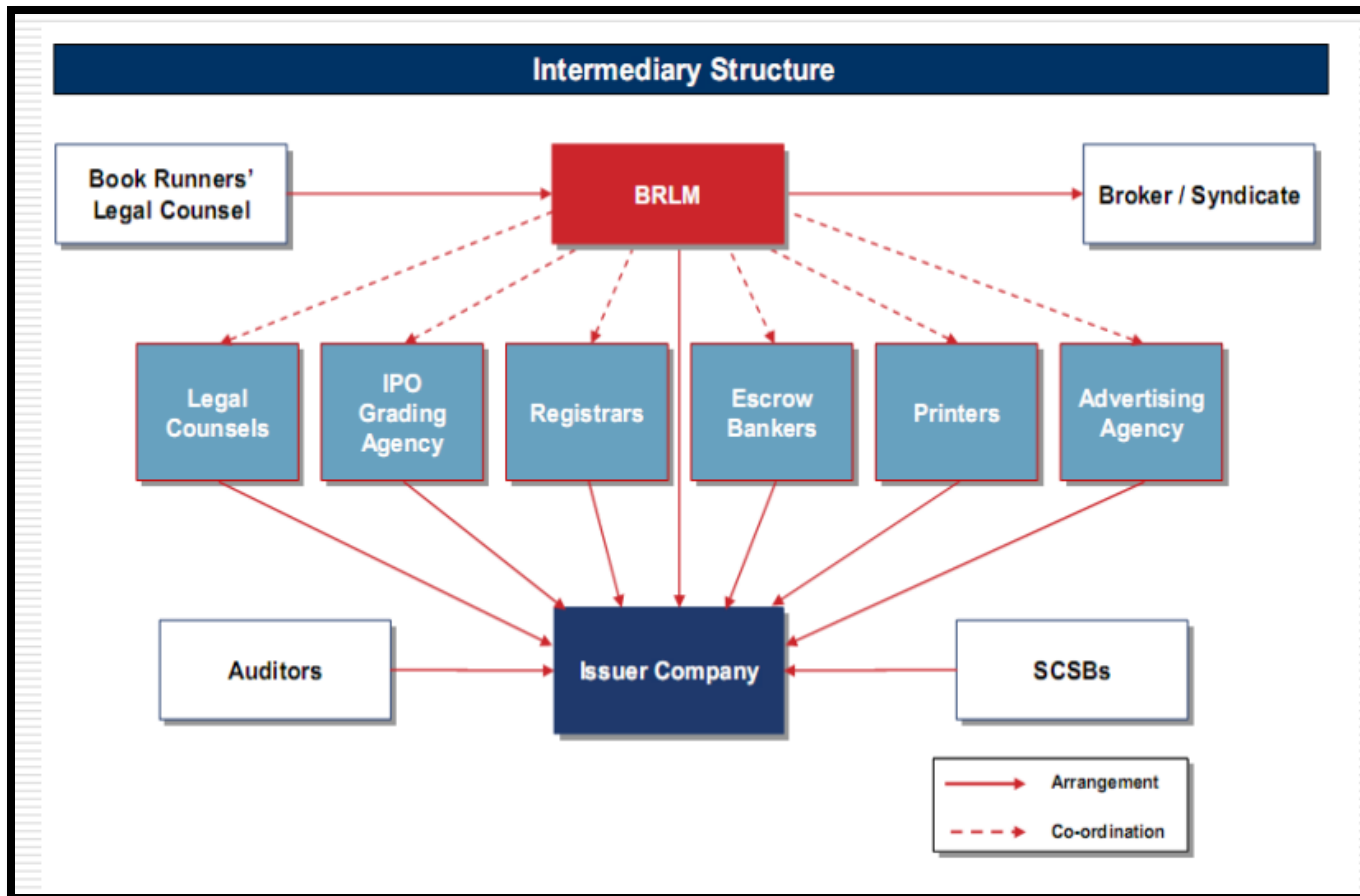
# Why IPO

- For Funding Needs
- Funding Capital Requirements for Organic Growth
- Expansion through Projects
- Diversification
- Funding Global Requirements
- Funding Joint Venture and Collaborations needs
- Funding Infrastructure Requirements, Marketing Initiatives and Distribution Channels
- Financing Working Capital Requirements
- Funding General Corporate Purposes
- Investing in businesses through other companies
- Repaying debt to strengthen the Balance Sheet
- Meeting Issue Expenses

# IPO Process

- Step 1: Appointment of Merchant Banker
- Step 2: Approval from SEBI / Exchange on Draft Offer Documents
- Step 3: Filing of Offer Documents with Exchange/s
- Step 4: IPO Road Shows
- Step 5: Price Determination
- Step 6: IPO Bidding Period and Allotment of Shares
- Step 7: Listing of Shares
- Step 8: Post-IPO Documentation

# IPO process: Intermediaries



# IPO process: Intermediaries

<u>Intermediaries and their Roles</u>		
Party	Key Responsibility	Appointment
<b>Lead Managers</b>	<ul style="list-style-type: none"> <li>• Overall Co-ordination</li> <li>• Conduct due diligence and finalize disclosure in Offer Document</li> <li>• Assist the legal counsel in drafting of Offer Document</li> <li>• Interface / ensure compliance protocol with SEBI / NSE / BSE</li> </ul>	<b>Upfront</b>
<b>Domestic &amp; International Legal Counsels</b>	<ul style="list-style-type: none"> <li>• Legal Due Diligence</li> <li>• Drafting the offer document</li> <li>• Guidance on any other incidental legal matters</li> <li>• Assistance in complying with requirement for selling in international geographies</li> </ul>	<b>Upfront</b>
<b>Auditors</b>	<ul style="list-style-type: none"> <li>• Reviewing and auditing financials and preparing financial statements for inclusion in the Offer Document</li> <li>• Verify/audit various financial and other data used in the Offer document and provide Comfort Letter</li> </ul>	<b>Existing Auditors</b>
<b>Registrars</b>	<ul style="list-style-type: none"> <li>• Co-ordination with the Issuer and Bankers regarding collections, reconciliation, refunds etc</li> <li>• Securing allocation approval from Stock Exchanges</li> <li>• Post issue co-ordination collation and reconciliation of information</li> </ul>	<b>4 weeks before filing DRHP with SEBI</b>

# IPO process: Intermediaries

<b>IPO Grading Agency</b>	<ul style="list-style-type: none"> <li>Provides IPO Grading</li> </ul>	<b>2 weeks before filing RHP with ROC</b>
<b>Depository (NSDL, CDSL)</b>	<ul style="list-style-type: none"> <li>Tripartite Agreement</li> <li>Dematerialization of Company's shares</li> <li>Demat transfer of Shares</li> <li>Credit of Shares to Allottees</li> </ul>	<b>After Appointment of Registrar</b>
<b>Printers</b>	<ul style="list-style-type: none"> <li>Bulk printing of the Red Herring Prospectus Bid Forms, final Prospectus, CAN, Refund orders etc.</li> <li>Ensure timely dispatch and distribution of stationery to all centers</li> </ul>	<b>Before Filing DRHP with SEBI</b>
<b>Advertisers</b>	<ul style="list-style-type: none"> <li>Preparing and getting published all statutory notices</li> <li>Creating all advertisement materials</li> </ul>	<b>Before Filing DRHP with SEBI</b>
<b>Escrow Collections Banks &amp; Bankers of the Issue</b>	<ul style="list-style-type: none"> <li>Acting as collecting agents</li> <li>Escrow Account &amp; Refund account</li> </ul>	<b>Before Filing RHP with ROC</b>
<b>Self Certified Syndicate Bank (SCSB)</b>	<ul style="list-style-type: none"> <li>To receive bids and block bid amount in the investor's bank account based on applications submitted;</li> <li>To provide FC on account transfer/ unblock funds post finalization of basis of allotment,</li> <li>To address investor grievances on account of ASBA bids</li> </ul>	<b>Approved by SEBI</b>

# IPO process: Agreements

## Various Legal Agreements undertaken by the Issuer Company

Agreements	Parties to the Agreement	Purpose of Agreements
<b>Engagement Letter</b>	Company and individually with Investment Bankers, Counsels to the Company, Auditors, Registrar and other intermediaries	Engaging the intermediaries for the Services
<b>BRLM MoU</b>	Company and BRLMs	Lays down the roles, responsibilities, reps of BRLM and Company
<b>Registrar MoU</b>	Company and Registrar	Lays down the roles, responsibilities of the Registrar
<b>Escrow Agreement</b>	Company, BRLMs, Syndicate Members, Registrar and Escrow Bankers to the Issue	Lays down the process for receipt of Issue proceeds and release of funds to the Company

# IPO process: Agreements

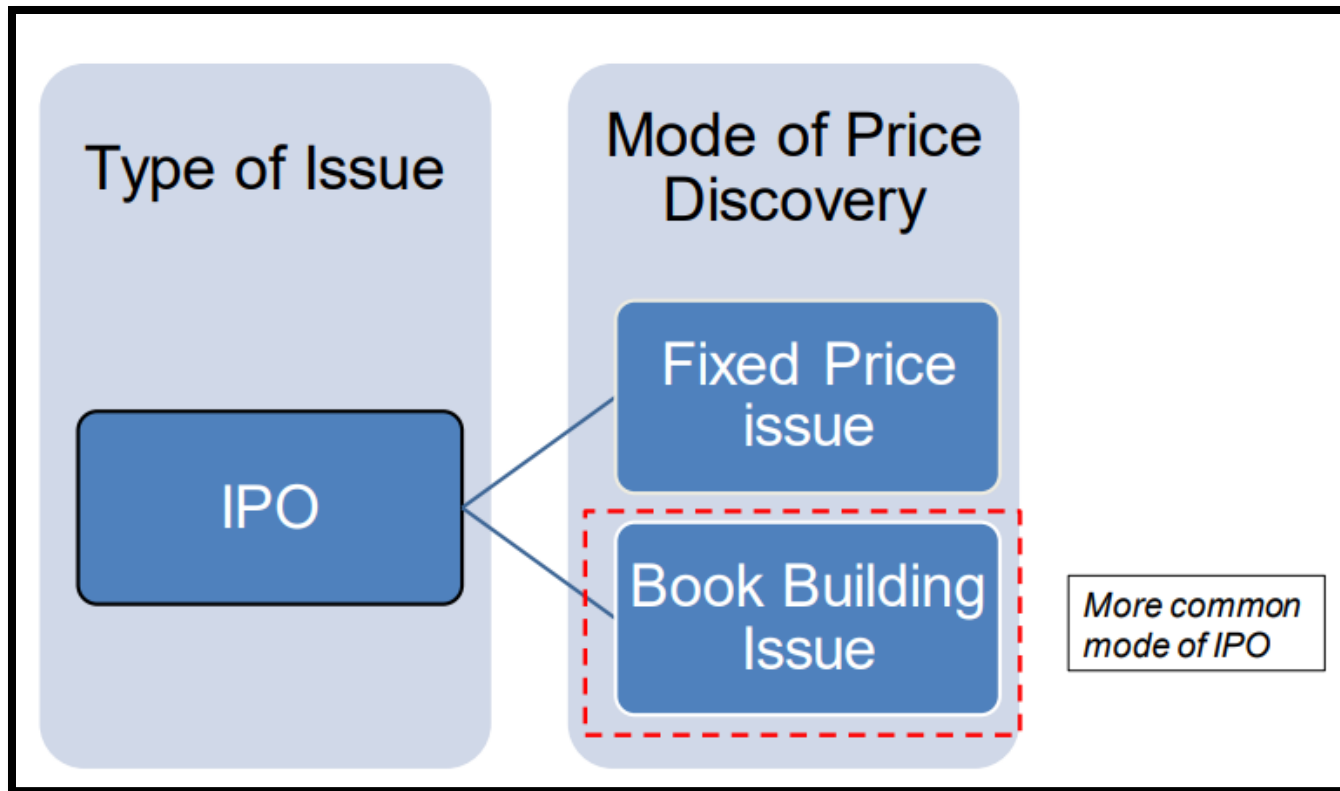
## Various Legal Agreements (Cont..)

Agreements	Parties to the Agreement	Purpose of Agreements
<b>Syndicate Agreement</b>	Company, BRLMs and Syndicate Members	Lays down the process of marketing and handling the forms
<b>Underwriting Agreement</b>	Company and the Underwriters (BRLM and Syndicate members)	Lays down the terms of Underwriting and the extent of underwriting
<b>Tripartite Agreement with Depository</b>	Company, NSDL and CDSL	Lays down the provisions of NSDL / CDSL acting as the Depositories of the Company
<b>Listing Agreement</b>	Company and Stock Exchanges	Binds the Company to the requirements of the Listing rules of the Stock Exchanges

# Offer document

- [https://www.sebi.gov.in/filings/public-issues/nov-2024/saatvik-green-energy-limited\\_88728.html](https://www.sebi.gov.in/filings/public-issues/nov-2024/saatvik-green-energy-limited_88728.html)

# Price Discovery of Shares in a Public Offering



# Price Discovery of Shares in a Public Offering - Fixed price issue

## **Fixed price issue:**

Price at which the securities are offered and will be allocated is fixed by Company along with Merchant banker



Fixed price is printed in the Offer Document, usually along with reasoning behind the price at which shares are offered.



Demand for the securities offered is known only after the closure of the issue.



50% of the shares offered are reserved for applications below Rs. 2 lakh and the balance for higher amount applications.

# Price Discovery of Shares in a Public Offering - Fixed price issue

## Illustration of Fixed Price Issue:

- First page of the prospectus contains:
  - Number of shares to be issued
  - Price of issuance



- Price is already fixed prior to the IPO. No price discovery mechanism is used.
- All application for shares **have to be made at the price mentioned else they are considered as invalid bids.**

# Book Built Issue

## Book Built Issue:

Company may offer a maximum of 20% price band in which one can bid for shares.

Price Band is independent of Face Value (FV) of shares.

Floor Price: Lower end of Price Band  
Cap Price: Higher end of Price Band  
Eg: Rs.100/- to Rs.120/-

Issuance Price discovered on the basis of demand at various price levels (within Price band)

Investors must specify:

- Number of shares they want to buy.
- Price they are willing to pay per share (within the price band).

# Stages in Book Building

## Stages in Book Building:

Company who is planning an IPO appoints the Lead Merchant banker(s) as “Book Runner”.

Investors give their bids for these shares to “Syndicate Members”. Bids have to be entered within the specified price band. Investor can revise a bid before the book closes.

Syndicate members input the orders into an “Electronic Book” through process called “Bidding”.

Book normally remains open for a period of 5 days.

On closure of the book building period, the Book Runner evaluates the bids on the basis of the demand at various price levels.

Book runners and the issuing Company decide the final price at which the securities shall be issued.

Finally allocation of securities is made to the successful bidders. Money gets unblocked in bank accounts of rest of the bidders.

# Book Built Issue

## Illustration of Book Building issue:

- Price band = Rs. 20.00 (Floor Price) to Rs. 24.00 (Cap Price) per share
- Total available shares (issue size) = 3,000 shares.
- Company received five bids from bidders as mentioned below:

Bid Quantity	Bid Price (Rs.)	Cumulative Bid Quantity	Subscription
500	24	500	16.67%
1,000	23	1,500	50.00%
1,500	22	3,000	100.00%
2,000	21	5,000	166.67%
2,500	20	7,500	250.00%

- Price discovery is a function of demand at various prices.
- Highest price at which the issuer is able to issue the entire size of 3000 shares is the price at which the “book cuts off” = Rs. 22.00.
- The issuer, in consultation with the Book Running Lead Manager will finalize the issue price at or below such cut-off price, i.e., at or below Rs.22.00.
- Valid Bids: All bids **at or above this issue price** and **cut-off bids** (allowed for retail investors only) and they are considered for allocation in the respective categories.

# BB Allocation

- Up to 50% of the Net Issue to Public is for allocation to QIBs.
- At least 35% of the Net Issue to Public is for allocation on a proportionate basis to the Retail Individual Bidders
- at least 15% of the Net Issue to Public is for allocation on a proportionate basis to Non-Institutional Bidders, subject to valid Bids being received on or above the Issue Price within the Price Band.

<b>Book Building IPO</b>	<b>Fixed Price IPO</b>
Introduced by SEBI in 1995 for efficient pricing.	The traditional old method for IPO issues.
A book-built issue has a price range.	A fixed price IPO has a fixed price.
The offer price is determined at the end of the bidding process.	The offering price is set in advance.
The demand for the book-built issue is known daily as the book builds.	The demand for a fixed price IPO is known at the end of the subscription period for the issue.
QIBs can place bids by paying 10% of the application amount at the time of application and the balance at the time of allotment.	The QIB must pay 100% of the subscription amount at the time of application.
A book-building IPO prospectus is filed with the RoC upon completion of the offering.	A fixed-price IPO prospectus is filed with the RoC before the issue opens.
Popular method	Less commonly used method
The price range can be revised in a book-built issue while the issue is open.	The offering price cannot be changed once the issue is open for subscription.
The chances of fair pricing are good as the price is set based on supply and demand.	The price can be undervalued or overvalued.
Investors can bid at any price within the price range.	Investors can only subscribe at a fixed price.
Generally adopted by Mainboard IPO companies.	Generally adopted by SME IPO companies.

# Top IPOs in India

<b>Top IPOs</b>	<b>Issued IPO Amount</b>	<b>Date Issued</b>
LIC IPO	Rs 21,000 crore	May 4, 2022
Paytm IPO	Rs 18,300 crore	November 2021
Coal India IPO	Rs 15,200 crore	October 2010
Reliance Power IPO	Rs 11,700 crore	January 2008
SBI Life IPO	Rs 10,341 crore	September 2017
GIC IPO	Rs 11,372 crore	October 2017
ONGC IPO	Rs 10,530 crore	March 2004
DLF IPO	Rs 9,187 crore	June 2007
ICICI Prudential Life Insurance IPO	Rs 6,057 crore	September 2016

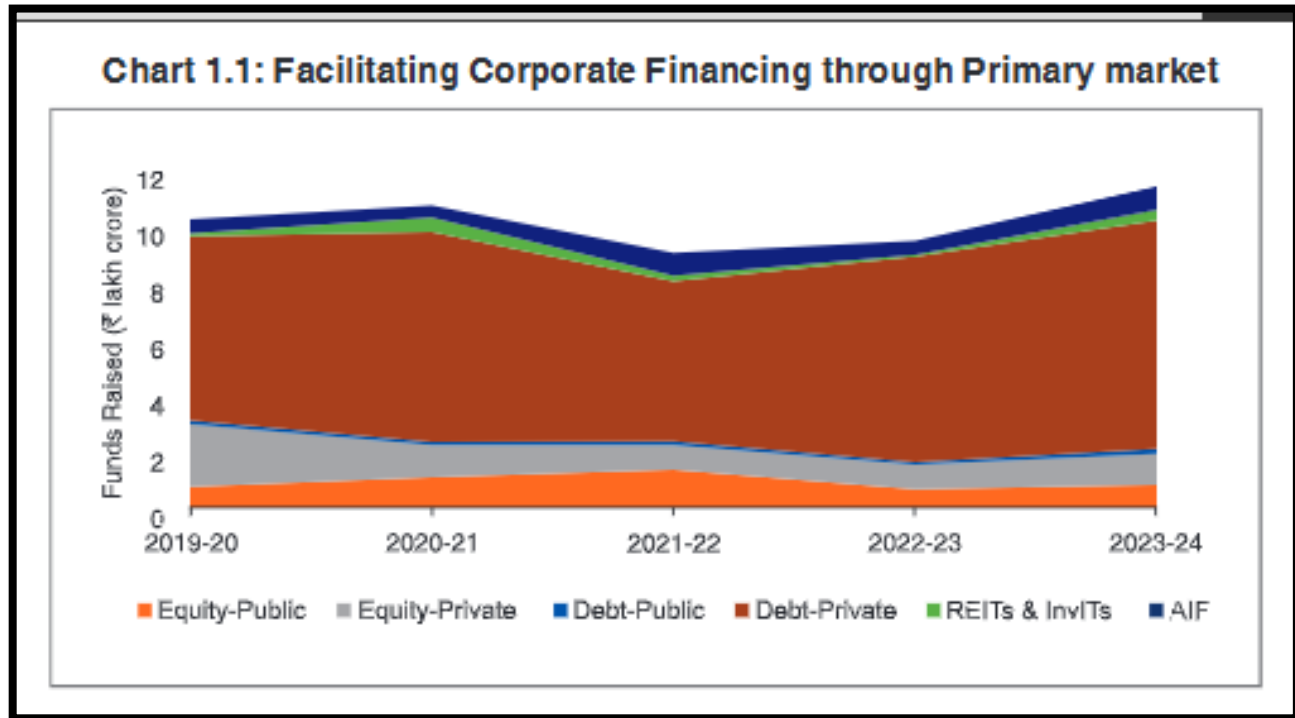
# Capital raising for companies - Debt

- Debt capital: Some investors have no interest in owning a piece of the company, but they are more than willing to lend money to it, for a price.
- That 's the role of debt capital. Investment banks help companies borrow money by issuing bonds, or IOUs, that are sold to investors.
- The company must pay the prearranged rate of interest, but it doesn't give up any ownership of the company.
- If a company falls onto hard times, though, the owners of the debt have a higher claim to assets than do the equity owners if a liquidation of the company is necessary.

# Capital raising for companies - Hybrid securities

- Most of what investment banks sell can be classified as either debt or equity.
- But some securities take on traits of both, or are an interesting spin on both.
- One example is preferred shares, which give investors an income stream that's higher than what's paid on the regular equity.
- But preferred shares don't come with as high a claim to assets as bonds, and this income stream can be suspended by the company if it chooses.

# Primary Market: Fund Mobilization



# Raising funds through Equity Markets

**Table 3.1: Resource Mobilisation through Public and Rights Issues**

Particulars	2022-23		2023-24		Percentage Share in Total Amount Raised	
	No.	Amount	No.	Amount	2022-23	2023-24
1) Public Issues, of which	165	59,072	273	67,982	89.7	81.8
A) IPOs of which	164	54,772	272	67,955	83.2	81.8
a) OFS* Component	11	29,046	13	16,839	44.1	20.3
b) Fresh Issues	114	3,700	181	14,618	5.6	17.6
c) Both (OFS + Fresh Issues)	39	22,027	78	36,499	33.5	43.9
Breakup of Both (OFS + Fresh Issue)						
OFS	-	9,264	-	19,910	14.1	24.0
Fresh	-	12,763	-	16,589	19.4	20.0
B) FPOs	1	4,300	1	27	6.5	0.03
2) Rights Issues	73	6,751	67	15,110	10.3	18.2
<b>Total (1+2)</b>	<b>238</b>	<b>65,823</b>	<b>340</b>	<b>83,093</b>	<b>100.0</b>	<b>100.0</b>

**Note:** The primary market resource mobilization is inclusive of amount raised on the SME platform

\* OFS - Offer for Sale

Source: BSE and NSE

# Raising Resources Through Debt Markets

**Table 3.7: Resource Mobilization through Public Issues and Private Placement of Debt**

(Amount in ₹ crore)

Period / Category	2022-23		2023-24	
	No. of Issues	Amount	No. of Issues	Amount
Public Issues #	34	9,221	45	19,168
Private Placement*, of which	1,524	7,54,467	1,347	8,37,756
EBP Issues	862	7,13,596	1,125	8,16,356
<b>Total</b>	<b>1,558</b>	<b>7,63,688</b>	<b>1,392</b>	<b>8,56,924</b>

**Note:** # Data for public debt issues have been taken on the basis of final post issuance reports received.

\*Listed issues; EBP - Electronic Book Provider issues included in the total.

Source: BSE and NSE.

# Underwriting

- Underwriting - 'An agreement with or without conditions to subscribe to the securities of a body corporate when the existing shareholders of such body corporate or the public do not subscribe to the securities offered to them'. (SEBI)
- Underwriter – 'A person who engages in the business of underwriting of an issue of securities of a body corporate'.
- It is an agreement by the underwriter to subscribe to the securities being issued in case the persons to whom they are offered do not subscribe to them. Hence it is a *service* that consists of taking a contingent obligation.

# Mergers and Acquisitions

- Companies may opt to merge with or be purchased by another firm rather than going public.
- M&A deals can give existing shareholders liquidity while also providing prospects for expansion through synergies with the acquiring firm.
- M&A transactions can take several forms, including stock purchases, asset purchases, and mergers of equals.

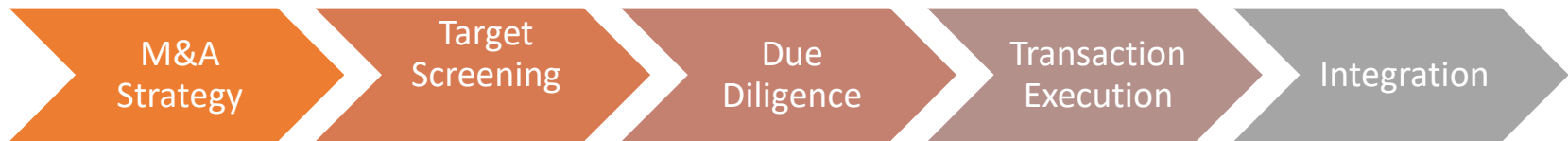
# Reasons for M&A

- Growth
- Synergies
  - Combining business activities, overall performance efficiency tends to increase and overall costs tend to drop, due to the fact that each company leverages off of the other company's strength
- Increase Supply Chain Pricing Power
  - By buying out one of its suppliers or distributors, a business can eliminate an entire tier of costs.
  - Specifically, buying out a supplier, which is known as a vertical merger which usually let a company save on the margins that the supplier previously add to its costs.
  - By buying out a distributor, a company often gains the ability to sell their products at a lower cost.
- Eliminate Competition
- Succession and Retirement

# Types of M&A

- Horizontal:
  - when the two companies are in direct competitions and share the same product lines and markets.
- Vertical
  - when the two companies are in difference production stages (e.g. the merger between a company and its supplier)
- Concentric
  - when the two companies have the same customer base but different products
- Conglomerate
  - when the two companies have different businesses

# M& A Life Cycle



# Sales and Trading

- The [Sales & Trading \(S&T\) group](#) at an investment bank helps institutional investor clients, such as [hedge funds](#) and asset management firms, to buy and sell securities such as stocks, options, and bonds.
- These clients buy and sell these securities to earn a high return and make more money for their clients such as pension funds, endowments, insurance firms, and wealthy individuals.
- This process is more difficult than it sounds because these institutional investor clients often place large orders that would disrupt market prices if they were executed all at once.
- So, the salespeople and traders at banks must divide up these orders, match buyers and sellers, and get the clients prices that are as close as possible to what they desire.

# Brokerage Services

- Some investment banking operations include brokerage services where they may hold clients' assets or help them conduct trades.
- Offers equity, fixed income, alternative investments and money market investment products and services to individual and institutional clients
- For alternative investment products, the firm co-invests with clients in hedge fund, private equity and real estate funds.

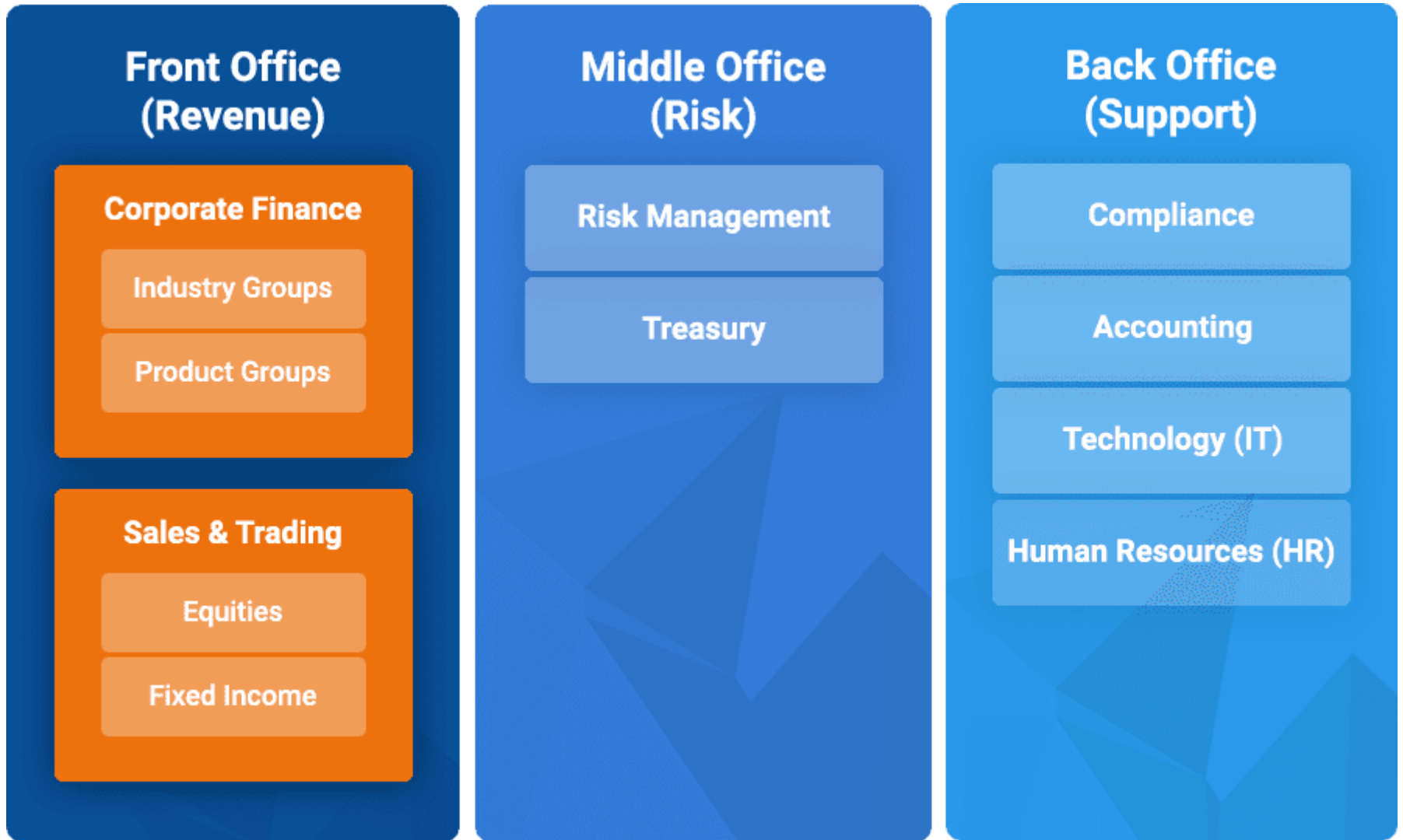
# Investments

- Periodically, units of investment banking operations also invest their own money in promising companies or projects.
- This type of investment, often made in companies that don't have investments that the public can buy, is called private equity.

# Research

- The research division writes reports about companies and their prospects, often accompanied by “Buy,” “Sell,” or “Hold” ratings.
- Historically, banks issued these reports to encourage higher trading volume and to solicit orders from institutional investors for the sales & trading division.
- For example, if a bank liked a company’s prospects and wanted to encourage more trading to earn higher commissions, it might have issued a favorable “Buy” report about the company.
- Banks may use research for internal purposes as well, such as for salespeople who want to recommend ideas to clients or for investment bankers who want to read up on companies in a specific sector.

# Investment Banks Organisation



# List of Merchant Bankers in India

- <https://www.sebi.gov.in/sebiweb/other/OtherAction.do?doRecognisedFpi=yes&intmId= 9>