

CHAPTER – VI

FEE BASED SERVICES OF IDBI

IDBI assists industry through a wide range of finance products. It has made continuous efforts to respond to the financial needs of Indian industry by extending its range of products and services.

With a view to supplement fund based business, IDBI would intensify its efforts in the areas of fee based activities like corporate advisory services, credit syndication, debenture trusteeship, forex services etc. These would enable corporates to approach IDBI as a one stop financial supermarket for all their needs.

In recent few years the IDBI has embraced fee based services such as a merchant banking and advisory services, trusteeship services, forex services and treasury operations. Currently it provide the following:

FUND BASED PRODUCTS

- Term Loan–Rupee–Foreign currency
- Underwriting/Direct subscription to equity and debt instruments.
- Guarantees.

- Venture Capital
- Equipment leasing
- Bills Finance
- Refinance to state level institutions/ banks.

FEE BASED SERVICES

a) MERCHANT BANKING

The IDBI has been providing a wide range of merchant banking services which include pre-project counselling, project appraisal, placement of equity with banks, foreign institutional investors, high net worth investors, mutual funds, institutional investors and private equity funds, placement of preference shares and debentures with domestic investors, structuring and syndication of bought out deals, loan syndication, syndication of structured debt instrument, co-ordinating the financial participation of multilateral agencies and international banks, issue management offering advice on the management of tender offer.

The stress of the Bank is on managing only select large sized equity issue which would attract investors interest.

Despite subdued stock market condition in the country the IDBI managed successfully 40 public and right issues involving mobilization of Rs. 5,136 crore during the period 1999-2000. During

1999-2000, the bank also executed two assignments for private placement of equity and bonds aggregating Rs. 120 crore. The Bank also carried out appraisal of 4 number of large capital investments planned by 'Navaratna' PSUs.

Till early 1960s, there was no merchant banking in the Indian Banking System. It was the Grindlays Bank which started merchant banking services as far back as 1967. After Grindlays bank, other foreign banks like Citibank and Chartered Bank, started these services in India. Till 1970s, the main services rendered were management of share issues and sub-aspects of financial consultancies. In mid 1970s, there was a boom in the capital market with the introduction of "Foreign Exchange Regulation Act (FERA) (1973)." This created awareness in the investing public about the capital market. This also encouraged a few commercial banks and financial institutions to set up merchant banking divisions. In addition, private financial brokers also started private merchant banking organizations. Today, the Merchant Banking set up in the country is broadly divided into the following groups:

Merchant banking divisions diagram

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- 1- **Foreign Banks:** Along with Grindlays Bank, Citibank, Chartered Bank and Hongkong Bank are also active in merchant banking.
- 2- **Indian Banks:** State Bank of India took the lead among Indian banks and is at present well established in the merchant banking field. The other Banks that followed suit are Bank of India, Central Bank of Baroda, Punjab National Bank, UCO Bank and Canara Bank which have established similar divisions at their respective head offices and other important centres.
- 3- **Private Merchant Bankers:** Leading private broker firms were already doing consultancy for Portfolio Investment. They took advantage of the situation and started 'Merchant Banking and Consultancy' services in a big way. Today, firms like J.M. Financial Consultants, Champaklal Investments and Financial Consultancy, V.B. Desai Consultants etc, are some of the leading private merchant banker in our country.
- 4- **Financial Institutions:** Industrial Credit and Investment Corporation of India (ICICI) has a well established merchant banking office. Recently, Industrial Reconstruction Corporation of India (IRCI) has also started its merchant

banking operations though its main concentration and attention is on mergers, amalgamations and takeovers.

In the early stages, the role of merchant banking in India was largely confined to the management of public issues of equity capital. This was due to the fact that several public issues (which came to be popularly known as FERA issues) came to the market at that time and there was, at that stage, an almost total absence of competent issue management services in the country. Today, the scope of merchant banking has gone much beyond just issue management. Banks' merchant banking divisions are now engaged in providing a wide spectrum of financial and related services to their customers.

Project Finance

Once a client decided upon the specific project he wishes to set up, the Merchant Banking Division provides a comprehensive package of services for financial structuring and funding. The Division works in close collaboration with the customer and the technical consultants for the preparation of a complete financial dossier, negotiates on behalf of the client with financial institutions and banks for the term finance, and assists him in the preparation of the complex loan documentation.

A project finance assignment fully tests the creativity of the merchant banker; and, quite often, the entire gamut of merchant banking services, including loan syndication, issue management, euro-currency financing and supplier or buyer credits are brought to bear on a single large assignment.

Corporate Finance

The pioneering role and expertise of the Merchant Division in the sphere of public issue management is well known. This product has been important in the banks' portfolio of services; and its continuing importance seems assured in the foreseeable future in the context of the recent and welcome growth witnessed in the capital markets in India.

The involvement of the Merchant Banking Division with a public issue, be it of equity, convertible debentures or non-convertible debentures, includes the structuring of the issue, obtaining all approvals (including the consent of the Controller of Capital Issues), appointment of underwriters, brokers and bankers to the issue, preparation of the prospectus, and coordination of all the agencies concerned with clock-work precision.

Objective diagram fom draw

The merchant banker's presence in all the major financial centres as well his long established relationships with the under writer and broker fraternities, makes possible the high degree of synchronisation required to ensure the success of an issue.

Entrepreneur Starting a New Project

An entrepreneur who is the promoter of a new project first obtains a Letter of Indent (LoI) from the Government of India and then gets it converted into an Industrial Licence for Setting up the proposed project. Generally speaking, the project report is ready and the company is incorporated, by the time the promoter approaches the merchant banker. Though, technically speaking, the promoter can take the help of the merchant banker for projects of any size, it is generally the projects costing over Rs. 1 crore which are taken by the promoters to the merchant bankers.

Existing Units

Companies planning modernization, expansion or diversification for their existing units need the help of merchant bankers. Amalgamation, absorption and reconstruction are some of the additional activities for which merchant banking assistance is availed of.

What Comprises Merchant Banking (MB) Assistance

For small size projects, a promoter can raise the required funds by recourse to the traditional source of finance, viz., bank finance. However, for medium and large size projects, the promoters cannot exclusively depend on banks who normally do not give large term loans. In such cases, the promoters have to find alternative sources of finance which are all-India and state level financial institutions, international markets and the capital market. A merchant banker, who is in constant touch with these different sources of finance, can help these promoters effectively in funding the project. There is a wide range of activities which may be grouped under merchant banking assistance. Broadly, these activities may be divided under two heads, viz., counselling and procuring finance. The main activities which are undertaken by a bank as merchant banking services are mentioned below:

- 1) **Project counseling or reinvestment studies for investors:** Under this head, merchant banker is expected to:
 - a) Identify promising projects,
 - b) Prepare feasibility studies (economic and financial),
 - c) Prepare in depth project reports,
 - d) Assist investors in obtaining licences,

- e) Do precise capital structuring,
- f) Arrange and negotiate foreign collaborations and
- g) Give guidance on amalgamation, mergers and take-overs.

2) **Syndication of loans and project finance:** Once the project is identified and clearance is obtained from the Government departments, the under mentioned steps are to be taken

- a) Aid in applying to financial institutions, banks and other sources of finance.
- b) Expert advice on government policies, demand-supply gaps, raw material availability, product-mix, plant capacity utilization, requirements of plant and machinery and the like.
- c) Consultation about alternative sources of finance, debt-equity ratio, 'over-run' finance.
- d) Liaison with government departments, financial institutions, banks etc.
- e) Advice and assistance for modernization, expansion and diversification.

3) **Issue management (including equity dilution):**

Management of the public issue of shares/ debentures (or even an offer for sales) has been the traditional service rendered by Merchant Bankers in India. Actually, with this service, the Merchant Banker was introduced in the Indian financial world. Following are the services rendered by the Merchant Banker under this head:

- a) deciding on the size and timing of a public issue in the light of the market condition,
- b) preparing the base of successful issue marketing from the initial documentation, liaison with the Controller of Capital issues for clearances etc., to the preparation of the actual launch of the proposed issue,
- c) optimum underwriting support,
- d) appointment of bankers and brokers as well as issue houses,
- e) issue management,
- f) professional liaison with share market functionaries like brokers, portfolio managers and financial press for pre-selling and media coverage,
- g) preparation of draft prospectus and other documents,

- h) wide coverage throughout the country for collection of applications and
 - i) preparation of advertising and promotional material.
- 4) **Provision of working capital:** Since Merchant Banking is a part of the banking system, the client has to be assisted in arranging for working capital finance especially for the new ventures. If the requirement of the client is substantially large, then it is desirable to arrange for the syndication on behalf of the promoters. There has been a recent change in arrangement for the working capital finance by issue of debentures on 'Rights' basis. Merchant Bankers play a great role in helping the clients in the preparation of the necessary forms for the financial institutions such LIC, GIC, UTI, who are the major supporters for such issue. He arranges for the trustees for the debentures and also ensures that the balance portion is tied up with the other bankers.
- 5) **Foreign Currency Loans:** The merchant banker also arranges for export credit for various countries. He also arranges for foreign currency loan like Eurodollar, IFCI loans etc.

- 6) **Portfolio management for non-residents:** The Merchant Banker assists in this area by identifying suitable arrangements of investment suitable to each Non-Resident Indian. In short, these include:
- a) guidance on purchase and sale of securities.
 - b) handling of such transactions.
 - c) advice on market conditions.
 - d) safe custody of documents.
 - e) collection of earnings (dividend, interest etc.)
 - f) service as a link between non-residents and Reserve Bank of India for obtaining necessary permission.

Besides this, leasing business is also being talked about in the banking as well as the financial sector. This is a new dimension in which the merchant bankers have been working on, and in fact, a few banks have already ventured into this field.

Moreover, marketing is also a very important function which the merchant banker has to take into account since he has to create the business for himself. He also has to have a close association with his own clients, understand their future expansion/modernisation programmes and advise them the way in which these programmes are to be carried out. His imagination and expertise plays a great role in this area.

He is also expected to be very active in finding out the new ventures opening up in the country. This information can be gathered from the Controller of Capital Issues, Registrar of Companies and State and Central financial institutions.

Project Counselling

If it consists of mere technical appraisal, the department makes use of the services of the Technical and Industrial Consultancy Division. Once convinced of the technical feasibility and commercial viability of the project, the merchant banker's next job is to prepare a structure of finance. To determine the structure of finance on the basis of different available sources, the department keeps in view :

- a) The norms laid down by term-lending institutions regarding the debt-equity ratio and the promoter's minimum contribution to the total cost of the project;
- b) The availability of various backward area subsidies;
and
- c) In case of equity issue the norms laid down by the stock exchanges for the listing of shares.

The structuring of finance also covers advice on setting up units in the 'joint sector', where state level financial institutions contribute 26% of the equity share capital, while the private promoter

contributes 25% and the balance of 49% of the shares are made available to the public. On the other hand, in a 'state assisted unit', state financial institutions contribute 11%, the promoters 40% and the public 49% of the equity shares capital. For listing purpose, stock exchanges required that the minimum 60% of the equity share capital should be offered to the public in case of units promoted by private promoters and 49% in the case of a joint sector or state assisted project.

b) CORPORATE ADVISORY SERVICES

Corporate advisory services rendered by the Bank include equity and business valuation, advice in mergers, acquisition and diversities, advice on business and financial restructuring, privatization advice and restructuring/rehabilitation advice for weak units.

Among non-fund business, the IDBI in view of its strengths has focused core on provision of advisory services to the corporate sector. The Bank has been mandated for several advisory and syndication assignments in large projects, mainly in power, petroleum, telecommunications and steel sectors. The Bank has acted as a consultant to the Government of India for its programme relating to disinvestment of its shareholding in two public sector

enterprises. The Bank also advised on financial restructuring of one of India's largest corporates in the public sector.

During 1999-2000, the IDBI completed 24 project and corporate advisory assignments, including those for several reputed public sector undertakings. It also completed three advisory and syndication assignments involving mobilisation of Rs. 6,085 crore. The Bank has at present 19 advisory and credit syndication assignments, involving mobilisation of over Rs. 13,300 crore.

IDBI provides project finance, both in rupee and foreign currencies, to boost capital formation and infrastructure development in the country. In addition to assistance for Greenfield Project, IDBI also funds project for expansion, diversification and modernization. In project appraisal and monitoring, Bank follows global best practices and in the process has created sizeable and well diversified assets portfolio in the recent years, Bank has been increasing providing non-project finance with short and medium term maturities in the form of short term loan. Working Capital and Treasury Projects to meet the ongoing requirement of corporates.

IDBI offers a wide array of corporate banking services under various business services. Central and State Government offering business (both direct and indirect taxes), Trade finance and Treasury Projects.

In respect of trade services, Bank has set up dedicated trade finance sales teams for products offerings at key locations and has been pursuing focused and special approaches in the business segment. Trade finance operations of Bank are available through designated branches, which provide Trade finance products viz., Letters of credit, Bank Guarantee Collections, Remittances, Forward Contracts, Packing Credit, Post shipment finance, Maturity factoring, Invoice Discounting and Trade Advisory services.

The Cash Management services of Banking have bagged several prestigious debt servicing redemption and dividends deals from lending corporates. IDBI is the first bank to offer payment facility of direct taxes through interest and is also the first bank to offer online payment of Central Excise Duty and Service Tax at select branches. Additionally, Bank has the mandate to collect sales tax and stamp duty for certain state governments and import / export licence fees over the internet.

c) TRUSTEESHIP SERVICES

The IDBI has been rendering trusteeship services since 1992-93. As a trustee, it seeks to represent and protect the interest of debenture/ bond holders. It also acts as security agent and mortgage trustee in respect of loans granted by domestic and foreign lenders to companies.

The Bank accepts trusteeship of those companies which have complied with SEBI ratio not exceeding 2:1, current ratio of 1.33:1 and have obtained satisfactory credit rating in case of public issue.

The trusteeship assignments with the Bank up to end March 2008 aggregated 464 in number and Rs. 28,510 crore in value terms.

Debenture trustee for holders of debentures issued by companies as also to the non-convertible debenture issues subscribed by financial institutions, banks and mutual funds on private placement basis.

While the large volume of assistance rendered by it to the industry directly helped in creating substantial capacities in various core and strategic industries, its assistance through the medium of refinance was responsible for the development of a large and well dispersed Small Scale Sector (SSS) in the industry. IDBI played a pioneering role in diverse areas such as entrepreneurship development, capital markets and technology and consultancy services. It was also instrumental towards balanced regional development. In its role as the apex institution. IDBI not only provided resources and other support to DFIs both at the all India and state levels but also coordinated their operations so as to channelise their assistance in tune with national priorities. While

playing this catalytic role, it has maintained itself in sound health, has grown in size and stature and today ranks, amongst the first ten largest development banks of the world.

To meet the diverse needs of industry, IDBI introduced new products such as equipment finance, asset credit equipment leasing corporate loans and bridge loans against public issues. IDBI also focused on non-fund based activities and financial services, making an entry in Merchant Banking, debenture Trusteeship and Forex services.

IDBI played a major role in the development of the capital market. IDBI set up the stock Holding Corporation of India Ltd. in 1987, providing custodial facilities. The Government entrusted IDBI with the responsibility for set up the Securities and Exchange Board of India (SEBI) and IDBI lent its organizational and resource support to SEBI in the initial years. IDBI is the nodal agency for establishing the National Stock Exchange. Other institutions promoted by IDBI include Credit Analysis and Research Limited and Investor Services of India Limited on the avail are a Commercial Bank and a Mutual Fund.

d) FOREX SERVICES

The Development Bank Strategic Business Unit (DBSBU) of IDBI opens Letters of Credit (LCs) and effect Foreign Currency (FC)

remittances on behalf of its assisted companies for imports of goods and services. The Bank also disburses FC loans to its clients for end-uses as permitted under the prevailing External Commercial Borrowing (ECBs) guidelines. During the period under review. Forex Services operations of the Bank's DBSBU continued to have Quality Management System as per ISO 9001:2000 standards.

The Commercial Bank Strategic Business Unit (CBSBU) of IDBI provides various trade finance products viz. Letters of Credit, Stand by Letters of Credit, Bank Guarantees, Collections, Remittances, Forward Contracts, Packing Credit, Post Shipment Finance, Maturity Factoring, Invoice Discounting and Trade Advisory.

e) TREASURY OPERATIONS

The IDBI has recently set up a separate treasury department with an Integrated Dealing Room (Comprising Rupee and FC) for exclusively monitoring the overall liquidity position, investment of surplus funds with the objective of enhancing fields and to take an integrated view of the developments in both money and forex markets.

The Bank has been trying to optimize returns on its short term surplus funds through efficient treasury operations. Risk management has been a focused area in treasury operations. The

Bank is taking steps for speedy processing of information through state of the art software package to facilitate quick decision making.

The new state of the art Treasury at IDBI Head Office became operational during the financial year. With this all the segment viz. Money Market, Foreign Exchange, Derivations Equity and Liquidity Management were placed under one roof for better management of Funds and enhanced customer service. With the single integrated IT platform online treasury services were extended to more branches.

IDBI's Treasury successfully managed to keep pace with the balance sheet growth by adopting Pro-active strategies to manage the liquidity requirements of the Bank. Liquidity was well managed by raising resources to meet to maturing bonds as well as the disbursements by using judicious mix of domestic and foreign currency liabilities.

IDBI also used instrument of varying maturities to manage the Asset Liability mismatch as well as to meet the liquidity requirements. These instruments included certificate of Deposits, Inter Bank borrowings, Bonds, Refinance from various institutions line of credit bulk deposits and Foreign Currency borrowings.

Treasury invested in central and state Government securities to progressively build the SLR portfolio for the Bank. The volatility in the domestic interest rate market was effectively used to optimize

the yield on investments. Further the SLR Portfolio was also used sporadically to manage the short term liquidity mismatches.

To enhance returns on the large corpus of funds available with it, IDBI plans to churn its portfolio and engage in more active treasury operations involving both cash as well as foreign exchange, including dealing in derivations like interest rate swaps. Incidentally, IDBI is the only financial institution in India to acquire an ISO certification for its treasury operations.

f) INSURANCE

The opening up of insurance has opened new opportunities for sourcing long term finance. IDBI proposes to launch insurance business in collaboration with an internationally renowned partner. The Bank also plans to enter into pension funds, besides enlarging the asset management/ mutual funds activities. The Banks insurance entry will complete its presence in the financial services areas.

The IDBI has of late decided to enter into insurance business.. For this purpose, it has tied the Dutch Financial Services giant, ING group for insurance. The tie up is one of the biggest in insurance sector. The IDBI is the largest financial institution in India and ING group is one of the largest financial group in the world.

The IDBI-ING alliance will stretch to be life and general insurance areas. The IDBI will give foreign equity in the venture to ING as per prevalent insurance guidelines.