OVERVIEW OF INVESTMENT BANKING

CA. Rajkumar S. Adukia
B.Com (Hons.), FCA, ACS, ACWA, LL.B,
DIPR, DLL & LP, MBA, IFRS(UK)
098200 61049/09323061049
email id: rajkumarradukia@caaa.in
Website: www.caaa.in

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To receive regular updates kindly send test email to
rajkumarfca-subscribe@yahoogroups.com
rajkumarfca+subscribe@googlegroups.com

Finance and Financial System

The term "finance" in our simple understanding is perceived as equivalent to 'Money'. But finance exactly is not money, it is the source of providing funds for a particular activity. Providing or securing finance by itself is a distinct activity or function, which results in Financial Management, Financial Services and Financial Institutions. Finance therefore represents the resources by way funds are needed for a particular activity. We thus speak of 'finance' only in relation to a proposed activity. Finance goes with commerce, business, banking etc. Finance is also referred to as "Funds" or "Capital", when referring to the financial needs of a corporate body.

A financial system or financial sector functions as an intermediary and facilitates the flow of funds from the areas of surplus to the areas of deficit. A Financial System is a composition of various institutions, markets, regulations and laws, practices, money manager, analysts, transactions and claims and liabilities.
The word "system", in the term "financial system", implies a set of complex and closely connected or interlined institutions, agents, practices, markets, transactions, claims, and liabilities in the economy. The financial system is concerned about money, credit and finance-the three terms are intimately related yet are somewhat different from each other.
Financial System of India (or any country) consists of financial markets, financial intermediation and financial instruments or financial products.

Meaning of Commerce

While business refers to the value-creating activities of an organization for profit, commerce means the whole system of an economy that constitutes an environment for business. The system includes legal, economic, political, social, cultural, and technological systems that are in operation in any country. Thus, commerce is a system or an environment that affects the business prospects of an economy or a nation-state.

The exchange of goods is a complex process beset with several types of hindrances. Commerce is the sum total of those processes which are engaged in the removal of hindrances of persons (trade), place (transport, packing and insurance) and time (warehousing) in the exchange (banking) of commodities.

Commerce and Banking

Buying and selling of goods between persons living in different places requires a common medium of payment. Money serves as common medium of payment.

However, convenient, and safe means of payment are required to settle the transaction. Banks help to remove this obstacle in the process of exchange by making and collecting payments on behalf of their clients. Businessmen can send money from one place to another in the form of bank-draft, cheque, etc. without facing any risk. Banks also provide credit in the form of overdrafts, letter of credit, cash credit, discounting of bills, etc.

The mixture of banking and commerce is hardly a revolutionary concept. Banking and commerce have been mixed in the United States since the birth of the republic, and they remain mixed today. It was not until 1956, when the Bank Holding Company Act prohibited nonbanking corporations from owning two or more commercial banks, that "the basic principle of separation of banking and commerce was established".

Meaning of Banking

A bank is a financial institution and a financial intermediary that accepts deposits and channels those deposits into lending activities, either directly or through capital markets. A bank connects customers that have capital deficits to customers with capital surpluses.

Due to their critical status within the financial system and the economy generally, banks are highly regulated in most countries. They are generally subject to minimum capital requirements which are based on an international set of capital standards, known as the Basel Accords.

The Bank for International Settlements (BIS) is an international organisation which fosters international monetary and financial cooperation and serves as a bank for central banks.The Basel Accords refer to the banking supervision Accords (recommendations on banking regulations)—Basel I, Basel II and Basel III—issued by the Basel Committee on Banking Supervision (BCBS). They are called the Basel Accords as the BCBS maintains its secretariat at the Bank for International Settlements (BIS) in Basel, Switzerland and the committee normally meets there.

History of Investment Banking in the World

Traditionally, banks either engaged in commercial banking or investment banking. In commercial banking, the institution collects deposits from clients and gives direct loans to businesses and individuals.

The stock market crash of 1929 and ensuing Great Depression caused the U.S. government to reach the conclusion that financial markets needed to be more closely regulated in order to protect the financial interests of average Americans. This resulted in the separation of investment banking from commercial banking.

From 1933 (Glass–Steagall Act) until 1999 (Gramm–Leach–Bliley Act), the United States maintained a separation between investment banking and commercial banks.In the United States, it was illegal for a bank to have both commercial and investment banking until 1999, when the Gramm-Leach-Bliley Act legalized it.

The Glass–Steagall Act of 1933 introduced the separation of bank types according to their business (commercial and investment banking). In order to comply with the new regulation, most large banks split into separate entities.
This act separated investment and commercial banking activities. At the time, "improper banking activity", or what was considered overzealous commercial bank involvement in stock market investment, was deemed the main culprit of the financial crash. According to that reasoning, commercial banks took on too much risk with depositors' money.

Commercial banks were accused of being too speculative in the pre-Depression era, not only because they were investing their assets but also because they were buying new issues for resale to the public. Thus, banks became greedy, taking on huge risks in the hope of even bigger rewards. Banking itself became sloppy and objectives became blurred. Unsound loans were issued to companies in which the bank had invested, and clients would be encouraged to invest in those same stocks.

In the United States, The Securities Act of 1933 became a blueprint for how investment banks underwrite securities in the public markets. The act established the practices of due diligence, issuing a preliminary and final prospectus, and pricing and syndicating a new issue. The 1934 Securities Exchange Act addressed securities exchanges and broker-dealer organizations. The 1940 Investment Company Act and 1940 Investment Advisors Act established regulations for fiduciaries, such as mutual funds, private money managers and registered investment advisors.

Provisions of the Glass-Steagall Act that prohibit a bank holding company from owning other financial companies were repealed on November 12, 1999, by the Gramm–Leach–Bliley Act.The repeal of the Glass–Steagall Act of 1933 effectively removed the separation that previously existed between Wall Street investment banks and depository banks. The Gramm-Leach-Bliley Act allowed banking institutions to provide a broader range of services, including underwriting and other dealing activities.

The financial crisis in 2007/2008, led to questioning of the business model of the investment bank. The Investment Banking industry began to collapse. Investment banks Bear Stearns (founded in 1923) and Merrill Lynch (1914), were acquired by commercial banks. Lehman Brothers (1850) filed for bankruptcy and Goldman Sachs (1869) and Morgan Stanley (1935) abandoned their status as investment banks by converting themselves into traditional commercial banks.

However, the period of 2010-2011 marked the return of confidence in investment banking. JP Morgan, Bank of America, Merrill Lynch and Goldman Sachs were the leading investment banks in 2010. Mergers and Acquisitions and Private Equity fundings are on the rise again and deal-activity has increased.

Meaning of Investment Banking

Investment banking is a field of banking that aids companies in acquiring funds. In addition to the acquisition of new funds, investment banking also offers advice for a wide range of transactions a company might engage in.

An investment bank is a financial institution that assists individuals, corporations and governments in raising capital by underwriting and/or acting as the client's agent in the issuance of securities. An investment bank may also assist companies involved in mergers and acquisitions, and provide ancillary services such as market making, trading of derivatives, fixed income instruments, foreign exchange, commodities, and equity securities.

Investment bankers identify capital opportunities, negotiate and structure deals, and execute private and public financial transactions. The essential function of an investment bank is to act as an intermediary between potential investors and those who seek capital. Investors include individuals, mutual funds, municipalities, public corporations, and private institutions.

An investment banking firm also does a large amount of consulting. Investment bankers give companies advice on mergers and acquisitions, for example. They also track the market in order to give advice on when to make public offerings and how best to manage the business' public assets. Some of the consultative activities investment banking firms engage in overlap with those of a private brokerage, as they will often give buy-and-sell advice to the companies they represent.

Unlike commercial banks and retail banks, investment banks do not take deposits. There are two main lines of business in investment banking. Trading securities for cash or for other securities (i.e., facilitating transactions, market-making), or the promotion of securities (i.e., underwriting, research, etc.) is the "sell side", while dealing with pension funds, mutual funds, hedge funds, and the investing public (who consume the products and services of the sell-side in order to maximize their return on investment) constitutes the "buy side". Many firms have buy and sell side components.

Investment Banks and Investment Banking in India

Investment Banks are financial intermediaries who help businesses in fund raising.

An investment bank or an investment banking firm is a kind of a financial institution, which assists governments, corporations and even individuals in raising assets by underwriting or acting as an agent of client for issuing securities. Such an organization even assists companies in Mergers and Acquisitions and offer ancillary services like market making, foreign exchange, trading of derivatives, commodities, equity securities and instruments of fixed income.

Investment Banking in India has evolved over a period of time. As per Indian Regulations, it is not allowed for one legal entity to perform all investment banking functions. Bankruptcy remoteness is a key feature while structuring the business lines of an investment bank. Therefore, Indian Investment banks follow a conglomerate structure by keeping their business segments in different corporate entities to meet regulatory norms.

The following are the largest full-service global investment banks;

- Bank of America
- Barclays Capital
- BNP Paribas

- Citigroup
- Credit Suisse
- Deutsche Bank
- Goldman Sachs
- JPMorgan Chase
- Morgan Stanley
- Nomura Securities
- UBS
- Wells Fargo Securities

Top 10 Investment Banking Firms in India include:

- Australia and New Zealand Banking Group Limited: Popular as A. N. Z. - http://www.anz.com/india/en/about-us/
- Citi Bank - http://www.citibank.co.in/
- Deutsche Bank - https://www.db.com/india/
- J. P. Morgan - https://www.jpmorgan.com/cm/ContentServer?pagename=Chase/Href&urlname=jpmorgan/ap/in/home
- Goldman Sachs - http://www.goldmansachs.com/worldwide/india/index.html
- Hong Kong and Shanghai Banking Corporation (HSBC) Limited - http://www.hsbc.co.in/1/2/homepage
- D. S. P. Merrill Lynch Limited - http://www.dspml.com/
- Morgan Stanley India Company Private Limited - http://www.morganstanley.com/about/offices/india.html
- ABN - Amro Bank - ABN - AMRO Large Corporates and Merchant Banking - http://www.abnamro.com/en/index.html

Objectives of Investment Banking

An Investment Banker is an intermediary between the capital markets (investors) and corporations (borrowers). He offers strategic advice and performs financial analysis. He also does research and analyses all public information to give advice on publicly listed stocks and bonds to investors and sales and trading groups.

The objectives of Investment Banking include:

- Guidance
- Project Formulations
- Implementation
- Modernization
- Diversification
- Mobilizing resources
- Raising Capital

Investment banks work for companies and governments, and profit from them by raising money through the issuance and selling of securities in capital markets and insuring bonds, and providing the necessary advice on transactions such as mergers and acquisitions. Most of investment banks provide strategic advisory services for mergers, acquisitions, divestiture or other financial services for clients, like the trading of derivatives, commodity, fixed income, foreign exchange, and equity securities.

An Investment Banker can be considered as a total solutions provider for any corporate, desirous of mobilizing its capital. The services provided range from investment research to investor service on the one hand and from preparation of the offer documents to legal compliances & post issue monitoring on the other.

Investment banks carry out multilateral functions. Some of the important points regarding functioning of investment banking are as follows:

- Investment banking helps public and private corporations in issuance of securities in the primary market. They also act as intermediaries in trading for clients.

- Investment banking provides financial advice to investors and helps them by assisting in purchasing and trading securities as well as managing financial assets
- Investment banking differs from commercial banking as investment banks don't accept deposits neither do they grant retail loans
- Small firms which provide services of investment banking are called boutiques. They mainly specialize in bond trading, providing technical analysis or program trading as well as advising for mergers and acquisitions

Investment Banking Activities

Investment Banks provide a wide range of financial services to clients. They structure Mergers and Acquisition deals, raise capital, analyze prospects of listed companies and offer advice, trade in securities on behalf of clients etc.

Therefore, Investment Banking can be defined to encompass many activities such as-

- Intermediary between issuer and investor
- Offering brokerage services to public & institutional investors
- Provide access to equity and fixed income capital
- Underwriting and distributing new security issues
- Providing financial advice to corporate clients especially on security issues, M&A Deals
- Due Diligence
- Providing financial research to investors, corporate customers
- Providing fee-based asset management services
- Merchant Banking, Venture Capital Investing
- Providing Bridge Loans For M&A, New Financing
- Arranging & Funding Syndicated Loans
- Foreign Exchange Trading & Hedging
- Arranging Swaps, Other Risk Management Tools

Corporate Advisory Services:

- Identify promising projects
- Prepare feasibility studies - economic and financial
- Prepare in-depth project reports
- Capital structuring
- Arrange and negotiate foreign collaborations
- Give guidance on amalgamations, mergers and takeovers

Raising Capital, Syndication of loans and project finance

- Aid in applying to financial institutions, banks and other sources of finance
- Expert advise on government policies, demand-supply gaps, raw material availability, product-mix, plan capacity utilization, requirements of plant and machinery etc
- Consultation about alternative sources of finance, debt-equity ratios, etc
- Liaison with government departments, financial institutions, banks etc
- Advise and assistance for modernization, expansion and diversification
- Private equity deals

Issue management

- Deciding on the size and timing of a public issue in the light of market conditions
- Preparing the base of successful issue marketing from initial documentation, liaison with Securities and Exchange Board of India (SEBI), and preparation of actual launch
- Optimum underwriting support
- Appointment of bankers and brokers as well as issue houses
- Issue management
- Professional liaison with share market functionaries like brokers, portfolio managers and financial press for pre-selling and media coverage

- Preparation of draft prospectus and other documents
- Wide coverage throughout the country for collection of applications advertisement

Sales and trading - Depending on the needs of the clients, the main function of a large investment bank is buying and selling products. In market making, the traders will buy and sell securities or financial products with the goal of earning an incremental amount of money on every trade. Sales is the term that is used for the sales force, whose primary job is to call on institutional and high-net-worth investors to suggest trading ideas and take orders

Research - is the division of investment banks which reviews companies and makes reports about their prospects, often with "buy" or "sell" ratings. Although the research division generates no revenue, its resources can be used to assist traders in trading, can be used by the sales force in suggesting ideas to the customers, and by the investment bankers for covering their clients.

Key Laws Governing Investment Banking Practices

In the absence of a comprehensive piece of legislation governing financial services in India, various services are regulated through a variety of Acts and Rules and by different regulators. Investment Banking in India is regulated by various legislations and the regulatory powers are also distributed between different regulators depending on the constitution and status of the investment bank. Pure investment banks that do not have presence in the lending or banking business are governed primarily by the capital market regulator Securities and Exchange Board of India (SEBI). However, multi-national banks and non banking financial corporations which are investment banks are regulated primarily by the Reserve Bank of India (RBI) in their core business of banking or lending and insofar as the investment banking segment is concerned, they are also regulated by SEBI. An overview of the regulatory framework is as under:

a. All investment banking companies incorporated under the Companies Act 1956, are governed by the provisions of that Act.

b. Multi-national banks are regulated by the Reserve Bank of India under the Reserve Bank of India Act, 1934 and the Banking Regulation Act, 1949.

c. Investment banking companies that are constituted as non-banking financial companies are regulated operationally by the RBI under Chapter IIIB of the RBI Act, 1934.

d. Functionally, different aspects of investment banking are regulated under the Securities and Exchange Board of India (SEBI) Act, 1992 and the guidelines and regulations issued thereunder. These are as follows:

- SEBI (Issue of capital & Disclosure Requirements) regulations 2009
- SEBI (Substantial Acquisition of Shares and Takeovers) Regulations 2011
- SEBI (Prohibition of Insider Trading) Regulations 1992
- SEBI (Foreign Institutional Investors) Regulations 1995
- SEBI (Venture Capital Funds) Regulations 1996
- SEBI (Foreign Venture Capital Investors) Regulations 2000
- SEBI (Mutual Funds) Regulations 1996
- SEBI (Merchant Bankers) Regulations 1992
- SEBI (Buy-Back of Securities) Regulations, 1998
- Private Limited Company and Unlisted Public Limited Company (Buy-Back of Securities) Rules, 1999
- SEBI (Underwriters) Regulations, 1993
- Securities Contracts (Regulation) Act,1956

e. Investment banks that are set up in India with foreign direct investment are governed in respect of the foreign investment by the Foreign Exchange Management Act, 1999.

f. Apart from the above specific regulations relating to investment banking, investment banks are also governed by other general laws applicable to all other businesses in India like tax laws, contract laws, arbitration law etc.

Professional Opportunities in Investment Banking Industry

There are a plethora of job titles available in the investment banking industry. They include:- Corporate Finance, Mergers and Acquisitions, Project Finance, Sales and Trading, Structured Finance, Derivatives, Advisory, Equity and Fixed Income Research, International Sales/Emerging Markets, Public Finance, Retail Brokerage, Institutional Sales, and Ratings Analyst.

Some of the most prominent fields in the investent banking industry include:

a. Corporate Finance - The job of the corporate finance officer is to create value for a company. Those in this field work for a company in order to help it generate money to run the business, grow the business, make acquisitions, plan for its financial future and manage any cash on hand. Corporate Finance professionals determine the funding needs of their clients and analyze the best alternatives to meet these needs, such as debt or equity issuance. Typical clients include corporations and public institutions. Other duties may involve working with investors interested in financing these ventures.

Corporate finance professionals are trying to maximize shareholder value. They do this through managing cash flow, negotiating terms with leaders and suppliers, monitoring liquidity, managing risk, and raising funds. Typical job titles in this area include treasurer, credit analyst, cash manager, investor relations officer, and controller. Corporate Finance opportunities can be found in both large and small companies and in diverse industries. The skills most needed for a career in corporate finance include analytical and negotiation skills, computer and communication skills, a willingness to take risks, a strategic way of thinking, and a competitive spirit.

b. Sales & Trading - Positions in this area involve analyzing stocks, bonds, and other securities for potential trading. This information is then shared with institutional investors and corporations. These positions require an in-depth knowledge about financial markets, as well as the ability to make quick decisions that may involve a great deal of risk.

c. Mergers & Acquisitions - Companies utilize investment banks when they want to sell all or a portion of their corporation. A career in this area involves analyzing the value of assets and negotiating the sale. M&A professionals are responsible for determining how much involvement their clients should have.

d. Analysts - This entails following the economy and key indicators of market stability. The investment bankers in this field may research individual companies and industries or the overall market. Forecasting future activity and risks involved are their key responsibilities.

e. Research - Most major investment banks employ a research staff that performs the risk, economic, and financial analysis used to support internal operations, from acquisitions and mergers to formulating trading positions in world, US, and regional markets. The profitability of an investment bank is directly related to the quality of its research analysis.

Investment Banking requires high level of proficiency in Financial Management and MS Excel. An Investment Banking career has many sub-branches viz. Private Equity, IPO Support, Investment Banking, Portfolio Management, etc.

About the Author

Rajkumar S. Adukia
B. Com (Hons.), FCA, ACS, AICWA, LL.B, M.B.A, Dip IFRS (UK), Dip LL & LW
Senior Partner, Adukia & Associates, Chartered Accountants
Meridien Apts, Bldg 1, Office no. 3 to 6
Veera Desai Road, Andheri (West)
Mumbai 400 058
Mobile 098200 61049/093230 61049
Fax 26765579
Email rajkumarfca@gmail.com

Mr.Rajkumar S Adukia is an eminent business consultant, academician, writer, and speaker. A senior partner of Adukia & Associates he has authored more than 34 books on a wide range of subjects. His books on IFRS namely, "Encyclopedia on IFRS (3000 pages) and The Handbook on IFRS (1000 pages) has served number of professionals who are on the lookout for a practical guidance on IFRS. The book on "Professional Opportunities for Chartered Accountants" is a handy tool and ready referencer to all Chartered Accountants.

In addition to being a Chartered Accountant, Company Secretary, Cost Accountant, MBA, Dip IFR (UK), Mr. Adukia also holds a Degree in Law and Diploma in LaborLaws. He has been involved in the activities of the Institute of Chartered Accountants of India (ICAI) since 1984 as a convenor of Kalbadevi CPE study circle. He was the Chairman of the Western Region of Institute of Chartered Accountants of India in 1997 and has been actively involved in various committees of ICAI. He became a member of the Central Council in 1998 and ever since he has worked tirelessly towards knowledge sharing, professional development and enhancing professional opportunities for members. He is a regular contributor to the various committees of the ICAI. He is currently the Chairman of Committee for Members in Industry and Internal Audit Standard Board of ICAI.

Mr. Adukia is a rank holder from Bombay University. He did his graduation from Sydenham College of Commerce & Economics. He received a Gold Medal for highest marks in Accountancy & Auditing in the Examination. He passed the Chartered Accountancy with 1st Rank in Inter CA & 6th Rank in Final CA, and 3rd Rank in Final Cost Accountancy Course in 1983. He started his practice as a Chartered Accountant on 1st July 1983, in the three decades following which he left no stone unturned, be it academic expertise or professional development. His level of knowledge, source of information, professional expertise spread across a wide range of subjects has made him a strong and sought after professional in every form of professional assignment.

He has been coordinating with various professional institutions, associations' universities, University Grants Commission and other educational institutions. Besides he has actively participated with accountability and standards-setting organizations in India and at the international level. He was a member of J.J. Irani committee which drafted Companies Bill 2008. He is also member of Secretarial Standards Board of ICSI. He represented ASSOCHAM as member of Cost Accounting Standards Board of ICWAI. He was a member of working group of Competition Commission of India, National Housing Bank, NABARD, RBI, CBI etc.

He has served on the Board of Directors in the capacity of independent director at BOI Asset management Co. Ltd, Bharat Sanchar Nigam Limited and SBI Mutual Funds Management Pvt Ltd. He was also a member of the London Fraud Investigation Team.

Mr. Rajkumar Adukia specializes in IFRS, Enterprise Risk Management, Internal Audit, Business Advisory and Planning, Commercial Law Compliance, XBRL, Labor Laws, Real Estate, Foreign Exchange Management, Insurance, Project Work, Carbon Credit, Taxation and Trusts. His clientele include large corporations, owner-managed companies, small manufacturers, service businesses, property management and construction, exporters and importers, and professionals. He has undertaken specific assignments on fraud investigation and reporting in the corporate sector and has developed background material on the same.

Based on his rich experience, he has written numerous articles on critical aspects of finance-accounting, auditing, taxation, valuation, public finance. His authoritative articles appear regularly in financial papers like Business India, Financial Express, Economic Times and other professional / business magazines. He has authored several accounting and auditing manuals. He has authored books on vast range of topics including IFRS, Internal Audit, Bank Audit, Green Audit, SEZ, CARO, PMLA, Antidumping, Income Tax Search, Survey and Seizure, Real Estate etc. His books are known for their practicality and for their proactive approaches to meeting practice needs.

Mr. Rajkumar is a frequent speaker on trade and finance at seminars and conferences organized by the Institute of Chartered Accountants of India, various Chambers of Commerce, Income Tax Offices and other Professional Associations. He has also lectured at the S.P. Jain Institute of Management, Intensive Coaching Classes for Inter & Final CA students and Direct Taxes Regional Training Institute of CBDT. He also develops and delivers short courses, seminars and workshops on changes and opportunities in trade and finance. He has extensive experience as a speaker, moderator and panelist at workshops and conferences held for both students and professionals both nationally and internationally. Mr. Adukia has delivered lectures abroad at forums of International Federation of Accountants and has travelled across countries for professional work.

***Professional Association:** Mr. Rajkumar S Adukia with his well chartered approach towards professional assignments has explored every possible opportunity in the fields of business and profession. Interested professionals are welcome to share their thoughts in this regard.*