

CHAPTER - I

INTRODUCTION

1.1 Background

Today business activity has become more complex. Small firms with little investment can hardly survive in the competitive environment. To compete and to survive in the environment firms need to have large operating capacity with strong financial position. But getting such position is not possible without giant investment, and that is not affordable by an individual saver. Though the ultimate source of investment is the saving of individuals but it requires to be accumulated (formulate into capital) before occurring it. Now a day to securities overcomes. Such difficulties most of the business organization are establishing with corporate entity. They issues different types of securities, like bond, preferred stock, common stock etc. to raise fund from the public. Even governments are borrowing the funds form their public to invest in large development projects. In case of governments borrowing, saving bond, development bond, treasury bills etc. are issued a security. Issuing such financial instruments is not enough for raising funds. They are to be marketed and sold to the public after convincing them. This kind of most tough and challenging work is handed by financial market, the back-bone of national economy. Since financial market provides retired funds for productive investment, better development in this sector obviously helps to boost up the national economy.

The basic function of financial market is to mobilize funds from individual savers to institution user. There are several parties who actively involve in operation of a financial market. The systematic relationship between them and the flow of fund is presented as follows.

Figure No: 1. (Financial Market and Flow of Funds)

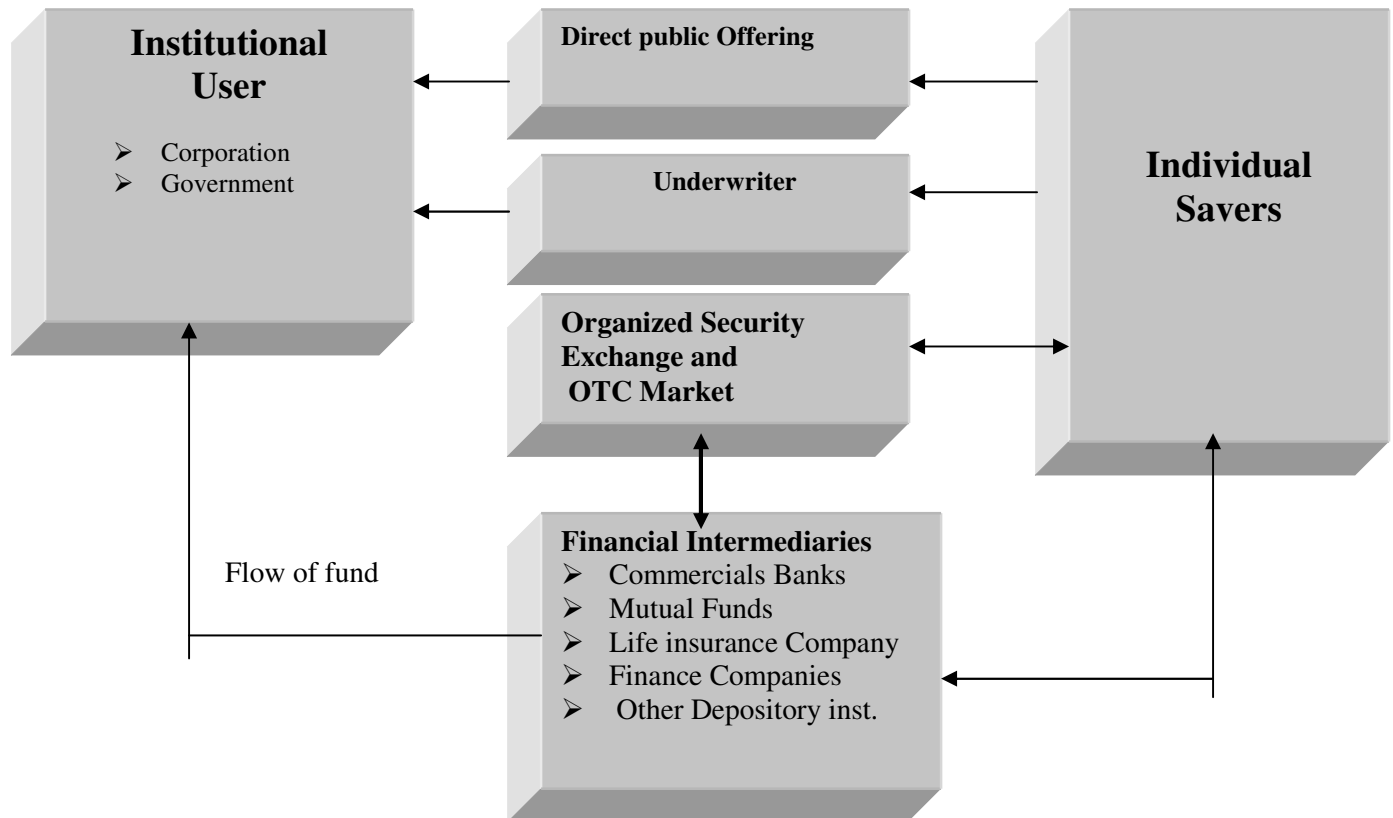


Figure 1.1 describes how the funds flow from individual saver to institutional user. Individual savers are those who have excess income over the consumption. They seek to employ their excess income (i.e., saving) which yields them certain return. Institutional users are those who requires fund to invest on their business activity or on development projects. Corporations and governments are the example of institutional user. The middle part between the individual saver (supplier) and institutional fund user (demander) is the capital market. Shares or stock market is a major component of the securities market. Stock market is a medium though which corporate sector mobilizes funds to finance productive projects by issuing shares markets. The efficient collection of small amounts of savings and transferring funds into the competitive and efficient user requires a well functioning capital market to facilitate the process (Mahat, 1981: 30-31).

The capital market is a financial relationship created by a number of institutions and arrangements that allows suppliers and demanders of long-term funds to make transactions. Included among long-term funds are securities issues of business and

government. The backbone of the capital market is formed by the various securities exchange that provides a forum for debt and equity Transactions. Mechanisms for efficiently offering and trading securities contribute to the smooth functioning of capital market, which is important to the long-run growth of business.

Financial market can be classified by whether the financial claims are newly issued or not. When issuer sells a new financial asset to the public, it is said to "issue" the financial assets. The market for newly issued financial assets is called primary market. After a certain period of time, the financial assets is brought and sold (i.e. exchanged or traded) amongst investors. The market where this activity takes places referred to as the secondary market. A company can make initial public offering either through underwriter or by itself. In some cases a company may make direct placement of security to the institutional investors. Wherever the way a company choose to issue its security for the first time, is regarded as primary market. Through the secondary market does not provide fund directly to the institutional user, its role is crucial in capital market. It is the platform for liquidation investments. Unless investors are confident that they can shift from one financial asset to another, as they may deem necessary, they would naturally be reluctant to buy financial assets.

Primary Market.

It is the market place where instead of goods and services securities are sold to mobilize the saving for the establishment and operations of the business. It is also known as original sales of securities. But this is misleading to some extent. This market is also known as IPO market because initial public offerings are done through this market. In this market, the securities can be sold either at par, premium or discount. But in case of Nepal, company act 1997 has restricted to sell the securities at discount. It means the securities can be sold at premium tool. In case of Nepal, NEPSE has issued license to interested organization to perform the issue manager by operating primary market. Securities board in Nepal, in order to regular the primary market issue management guidelines. Merchant bankers' manager

issues in India and USA, it is done by investment bankers generally hold the shares and paid the entrepreneurs and can be sold either through private placement or through primary and secondary market. There is also equal opportunity for all investors. The investors who have contact with investment banker can get the shares the investment bankers generally provide there basic services, which are:

- i) Advice and counsel
- ii) underwriting
- iii) Distribution

The job of issue managers can be grouped in three different categories for the simplicity of understanding they are mentioned below:-

a) Pre - issues Activities:-

Issue Manager is considered an expert in this area. They have to provide different services like consulting for the determination of appropriate timing for the floatation of securities, drafting prospectus on the request of issuing companies, drafting announcement - getting approval from the office of the company register SEBO/N, underwriting appointing co-issue manager, appointing co-issue manager depend upon the size of the issue. The issue Manager decides collection centers by consulting with issuing company. Appointing banker to the issue for the collection of application money of, publishing announcement, printing application forms on the request of issuing company arrangement of several documents in several places for the easy access of the probable investors.

Majority of these activities are related for providing assume to the entrepreneurs about collecting the required capital also providing assurance to the investors about the success of the business. The position of an issue manager is very critical if the issue manger deviates from its responsibilities, it will loose goodwill in the market. So while doing these entire jobs they must be very cautions. It is the responsibility of an issue manager to give true picture to the investor. If it did not happen then anybody will not trust tomorrow, so SEBO has issued primary issue guidelines making him or her highly responsible. SEBO/N has its own responsibility of monitoring the entire capital market, so it will also hold responsibility for the

deviation of the issue manager, so pre-issue activities starts with negotiation with entrepreneurs.

b) Issuing Activities:-

This is the major activity of the issue manager. The success of the issue manager depends mainly upon handling this job. This activity, different collecting center including the office of the issue manager distribute the application forms to all the probable investor and collect issued forms along with the bank voucher of the required amount as application money. The responsibility of issue manager is to get the day to day information about the application received, information dissemination to the general public as well as to concerned authority. The issue can be closed on the fixed date having upto the information.

Another responsibility is to maintain the record of the application. The collected application should be inserted into computer and the amount should be collecting in the bank account from different bank branches of the banker to the issue bank reconciliation should be done.

c) Post issue Activities:-

When every thing will be over and if the issued shares are under-subscribed then the problem of allotment does not arise but in case of over subscription the available share need to be allotted SEBO/N has issue share allotment guidelines. It has prescribed the allotment will be the shareholder of the company.

After selecting shareholder the issue manager, on the request of the company concerned print certificate and writers, the name and address of the shareholder, get signature of the concerned authority and distribute the share certificate to the concerned shareholder.

Primary market is growing in importance as it provides of a good source for corporate financing an alternative to the private and bank financing. In the past 10 years, capital issue in the tune of Rs.8.5 billion was offered to the public investors. However, there was uneven growth by sector, more than two-third of the amount issued was from bank and finance sector, a newly liberalized sector that requires mandatory public offer. Although companies from level hotel, trading,

manufacturing, mining, aviation and, of late hydroelectric sector have gone public, their operational and market performance continue to be weak. There is list of companies, especially small ones, that disappeared, got delisted or do not comply with the fiduciary duties, thus impairing investor's interest in the offering market.

Another feature of the primary market is the over whelming presence of retail investors and very small role of institutional investors. This may be attributed to the limited size of the new issue market and non-availability of risk financing and merchant banking type of intermediary institutions to support the growth of the market.

Instrument wise, more than three- fourth of the issue size is made up of equity shares. Other types of instruments offered in the market are debentures funds and preference shares. The market instruments need to be more innovative in order to meet the funding needs of the company that match the investment preference of the investors.

The intermediaries involved in the issuance of shares are issue and sales managers, underwriters and brokers. However, the role of brokers (selling agents) is not uniformly practiced in the primary issue and secondary market is yet to be properly integrated with the primary market. Similarly, underwrites are loosely regulated by securities Board of Nepal (SEBON) and are normally bank and financial institutions regulated by the central bank. The main player in the new issue market are issue managers functioning as professional advisors to the issue and prospectus who take due diligence responsibility on the disclosures and work as register to the issue and take a lead role together with the issuer in the allotment of securities. Though the issue managers can manage and commit underwriting, their servicing capacity is limited as they follow prudential banking norms. In many jurisdictions financial institution are the primary buyers of securities who ultimately distribute in favors of the public subscribes. The inadequacy of regulation and the absence of appropriate merchant banking institutions have resulted in cases where some underwriters do not stick to their commitments (SEBO, 2005: 26-27).

Secondary Market:

The secondary market is where already issued financial are traded among investors. The key distribution between a primary market and secondary market is that in the secondary market the issuers of the asset dose not receive funds form the buyer. Rather, the existing issue changes hands in the secondary market, and funds flow from the buyer of the asset to the seller.

A secondary market serves several needs of the firm or government unit that issue securities in the primary market. The secondary market provides the issuer with regular information about the value if its out standing stocks or bands, and it encourage investors to buy securities from the value of it offers them an ongoing opportunity for liquidating their investments in securities; Investors also get services from the secondary market. The market supplies them with liquidity and prices for the assets they are holding or want to buy; and the market brings interested investors together, thereby reducing the costs of searching for the other parties and of making trades secondary markets for securities exist around the world. Such market may be continuous, where trading and price determination go on throughout the day as orders to buy and sell reach the market. Some markets are call markets where prices are determined by executions of batched or grouped orders to buy and sell are specific time within trading day. Some secondary markets combine features of call and continuous trading.

Without a secondary market, investing in companies would be so difficult, time consuming and expensive that it might not be worth-while Imagine if we purchased shares of any company from primary market and wanted to sell them. Without a convenient secondary market, we should have to go out ourselves and try finding a buyer for our shares. This could take a long time, and we might have to spend a lot of money on advertising to let people known that we want to sell. With a strong secondary market, people can choose to buy from a wide range of available shares at any time, not just when they are newly issued. They can sell and buy when they want. Investors can make quick decision about the value of a company and act on them immediately.

The secondary market begins with the organized stock exchanges. It is the physical locations where stocks are bought and sold. In Nepal, we have only one stock exchange center i.e. Nepal Stock Exchange that is owned by the government, NRB and NIDC. It has small ownership holding of its members also. Securities business persons like stockbrokers, market makers and securities dealers; they have to get membership from the stock exchange for conduction securities business. Similarly, the issue manager, who engage in the primary issue activities also, have to get membership of stock exchange to operate their securities business (SEBO Reports:2001,4).

Historical Background:

Nepal is one of the least developed countries in the world. Nepal launched economic development planned more than four decades ago. Recently she has adapted the place of economic development though liberalization. However, any strategy for development requires a steady supply of medium to long- term capital as well as short-term capital fund for productive investment.

The history of security market is not too long; the government of Nepal passed a law relating to company registration and regulation in 1936 A. D (Frederick: 1975, 37). After the enactment of this law Biratnager Jute Mills and Nepal Bank limited floated their shares in 1937. The ownership of the shares was restricted mostly within Rana family subsequently the development of capital market remained stagnate. Almost two and half decades later, government issued treasury bills in for the first time in 1962 followed by issuance of development bonds in 1964. But there was no secondary market to provide liquidity for these bonds until the establishment of the securities Exchange center (SEC) in 1976. The establishment of the SEC under the company Act was the first foundation stone for the institutional development of the securities market in Nepal.

New York stock Exchange (NYSE) was the first stock market in history of investment literature. The U.S government issued debt certificates in 1970, then the market for securities expanded greatly and trading become more active since then America, Italy and other market in Nepalese context is remained like snail pace.

Listing of shares in stock exchange and their daily trading in the secondary market through the institutional Brokerage system started only after the restoration of democracy in 1990. Because of the world wide whim of Privatization and economic liberalization, economic changes have been brought about in the country.

Modern banking practices are of recent origin in Nepal, historical evidences show the presence of some crude banking practices in the earlier period of time. 'Tejarath Adda,' considered as the father of banking institutions in Nepal has been regarded as the first remarkable step in organized banking institution in Nepal, which was established in the government sector provided it service only to the civil servants and excluded the service to the general public. The grave need of a commercial bank was left to eliminate prevailing hindrances caused by private money lenders to the general public.

The first bank to be initiated in Nepal is Nepal Bank Ltd(NBL)which was established in the year 1937 A.D .to perform the function of central bank. Subsequently, another state owned commercial bank, RBB was established in 1965.

The Government of Nepal approved joint venture banks to operate in the country only in the year 1984. Then, the board of joint venture public limited commercial bank came. Such bank is Nepal Arab Bank ltd. that was established in 1984. Nepal Indosuez bank Ltd. and standard chartered bank Ltd. was established in 1984 respectively. Then after, in joint venture, Habib Bank of Pakistan, Nepal SBI bank, Himalayan bank, Nepal Bangladesh Bank Ltd, Everest bank Ltd, and Bank of Kathmandu Ltd. were established. Meanwhile, there had been many public limited commercial and development banks, which were established subsequently.

Securities Board, Nepal (SEBO) was established on 26 May, 1993 under the provision of the Securities Exchange Act, 1983(now 2006) which was the first amendment. It was established with the objective of promoting and protecting the interest of investors by regulating the securities market besides market in the country. So, SEBO had identified the policy development, legal and regulatory

reform, standardizing disclosure, bringing enforcement to ensure companies and promoting broad based market as a priority area to reform.

Securities Exchange center was renamed into Nepal stock Exchange in 1993 by Nepal Government under a program initiated to reform capital market. Nepal stock Exchange, in short NEPSE, is a non-profit organization, operating under securities Exchange Act, 1983.

The basic objective of NEPSE is to give information about free marketability and Liquidity to the Government and corporate securities by facilitating transaction in its trading floor through member, market intermediaries, like stock brokers, market makers etc. The trading floor of NEPSE was opened in 1994 January 13 through its licensed members. Presently, there are 23 stock brokers, two securities dealers, nine issue managers and one stock exchange and 141 listed companies in the Nepalese securities Market.

1.2 Statement of the Problem

Nepalese stock market has no long-history. It has only more than one and half decade. The numbers of listed companies in the Nepal Stock Exchange are increasing every year. But most of the companies are confined to the bank and finance companies sectors. There is a tremendous growth in the financial institutions over the period of time. Nepal Rastra Bank (NRB) has also made compulsion to issue at least 30 percent of shares to the public.

But the other sectors like manufacturing and trading are almost zero to issue share in the public. Since long, no new companies are established. Many of these companies are de-listed from Nepal Stock Exchange. In March 2007, Nepse has de-listed 12 companies from its list.

Investors are losing confidence on the share market mainly due to their experience of fraudulent and scandalous activities undertaken by a handful of market swindlers. There has been also some subtle problems involving misuse of insider information and growing tendency of frauds in securities transaction. Moreover, credulous investors too are responsible for showing irresponsible behaviors due to freedom for quick gains from share market.

Investors become miserable emerged from tactless advice of brokers through market disorders, price manipulation and fraudulent activities taken together have resulted the present bearish market in the country. How these securities frauds and manipulation have occurred and to what extent they can be overcome would be highlighted to draw adequate feedback to the regulating and controlling authorities to devise suitable laws to prevent such frauds and minimize manipulation in share price.

i) Losing Faith

The growing pessimism of the investors over the performance of share market is to be looked from broader company-industry economy framework. The frequent change in government has created political uncertainty regarding the coherent economic development strategy to the extent that entrepreneurs are not sure of what type of business policies to pursue.

In the absence of the appropriate relationship between business and government regarding privatization policies and economic liberalization thrust, public limited companies are in state of confusion since every change in government took different political ideological stand in the development of enterprises in the country, attraction to

direct foreign investment became a great setback as government cannot give clear-cut development agenda to further national development parameters. Again, development recovery program through revival of privatization has brought some favorable impact on the performance of capital market.

But, investors viewpoint it should have been made clear earlier so that an investor can take investment decision. The most reputed companies managed by a handful of professional is not managing and behaving well to regard the protection of investors by providing timely and adequate return on their investment. Take the case of Jyoti Spinning Mill, Agro Nepal, Himgiri Textiles, Harisidhi Brick, Bansbari Leather Shoe where management is excellent and managed by professional cadre, the return on investment has not yet been generated to investor.

Lack of actual investment return strategy in the management on most companies have made investors to believe that investing money in share of companies would be nothing more than inviting self exploitation by one's own act of wrong investment decision.

ii) Unfair Practice

The downfall of share market is mainly due to the unfair share market practices that went undetected for a long period in Nepal's share market. There has been a growing tendency to sell worthless and fraudulent securities since regarding their moral standing and hones integrity of professionalism. The unfair share market practices cover wash

sales, concerning of the share market, churning, formation of pools and cartels, misuse of insider information and so on. In wash sales, there is simply record of a sale but there is no sale of shares at all. The market makers have taken shares in name of their family, relatives and other employees who's were under their control but, as they raise prices artificially to the peak which is called forcefully created market boom by their own dishonest acts, they sold and later on put innocent investors to be the victims as they are made to buy at higher prices.

Some market maker have undertaken market pool activities by an institutional device through various unhealthy practices like acquiring the securities quietly and discreetly in order to keep them from driving up the share price while they were buying. During the stock market boom, the pool's tactic was successful in manipulating naïve investors into bidding up the price of pool's securities and they could reap the advantage to a considerable extent. By such market pools, a group of market maker could make fortunes by unfair share market practice in the absence of any control and investigation on their sharp activities.

At the same time, there is no denying the fact the investors too are responsible for not having self-control and self-judgment in the choice of securities for investment. In most cases, investors have considered share market as an important gambling place to make fortunes overnight without considering how such irrational behavior can put them in to possibility of grater losses. Many investors began to draw their money form saving account and also form matured fixed deposit certificate to canalize for trading as they

found higher return and lucrative gains from share transactions. Some investors are happy to inform that they could gain Rs. 5,000 immediately by investing just Rs. 20,000. But later on, they have to borne losses as share market depressed due to poor performance and financial losses of listed companies on one hand and many investors began to be cautious not to commit blunders further.

From the above fact, we can say that the current state of primary stock market in Nepal is not satisfactory. It gives the wrong impression when we look at the overwhelming response of the investors for majority of the public issues. However, if we analyze the present state of primary market, there exist a number of problems, which has hindered the long-term development of primary market in Nepal. The problems, which are affecting to the development of primary market, are the following:

iii) Insufficient knowledge of Investors about the Stock Market

When corporate bodies started offering public issues after the liberal economic policy adopted by government of Nepal, retail investors thought that it is the most suitable means of investment for higher return. Investors are investing their fund into stocks without studying the prospectus of the company or even without knowing about the company's area of business and its future business opportunities. This led to oversubscribing of the shares. Gurkha Development Bank, Himchuli Bikash Bank, Sanima Bikash Bank etc. are example of oversubscribed of the share at the time of public issues. But the companies failed to provide dividend as expected by the investors. Except companies in the banking and finance sectors, other failed to comply with disclosure

requirement and even failed to call AGM. This has a negative impact on the investors about performance of the companies in other sectors.

The regulatory authority's role to educate general investors about securities market is also not sufficient. Most of the retail investors do not know when and how to sell their shares. They do not know how the stock market functioning, what should be their return, whether their company is functioning satisfactorily or not etc. the investors are also unaware of the complaint procedure in the company fails to take care of the investor's interest.

iv) Lack of investors Confidence

Investors need sufficient information about the company before investing in the initial public offering of the company. However, there is a general feeling among the investors that the information disclosed through the public announcement and prospectus do not truly reflect the true picture of the future prospects of the company. It's found to be true in some extent, because some company's performances after the public issue were found to be very poor despite they showed very optimistic financial forecasts in the prospectus.

v) Shortcoming on Existing Securities Law and Regulations

Existing securities law and regulation do not clearly define the regulatory, supervisory and enforcement function of the Stock Exchange and Securities Board. The Securities Exchange Act and Companies Act are not clear on the division of authorities

between the Registrar of companies and the Securities Board regarding the filing of prospectuses and the periodic disclosure requirements by public companies. The prospectus (Company Act), registration (Securities Exchange Act) and listing (Securities Exchange Regulation and NEPSE bye-law) provision involve a multiplicity and absence of one window policy creates unnecessary hurdles, expense, confusion, complications and delay act as a disincentive to companies thinking of coming to the market by way of public issue.

The existing laws and regulation do not give and anticipatory powers of intervention by the Securities Board for the protection of investors. The Board does not have the investigatory powers for any company that does not comply with the existing laws and regulations.

vi) Lack of Coordination between Securities Board and NRB

There is no effective coordination between Securities Board and NRB to determine their respective supervisory responsibility over commercial banks and finance companies which are involved in securities businesses such as issue management, underwriting etc. as the banking and finance companies operate under banking and finance companies act and their activities are controlled by monitored by NRB. However, the involvement of these companies in securities business requires securities Board involvement also to monitor their activities.

vii) Restriction to Foreign Investors

After the policy of economic liberalization adopted by Government of Nepal, one of the prime objectives of the government is to attract foreign investment in various sectors such as hydropower, telecommunications, manufacturing and processing industries. Foreign investors are given attractive incentive through various act and policies. However, foreign investors are not allowed to invest in Nepalese capital market. This has caused restriction not only in the foreign investment but also the managerial expertise that can come through foreign investment.

viii) High Cost of Public Issues

With the objective of estimating cost and providing policy recommendation to reduce the cost of public issue, SEBO/N had conducted a research study recently. The cost associated with the public issue was classified into underwriting cost, advertising, printing, and other expenses, amount collection and refund charges and issue commission. The study covers the financial sectors (bank, finance companies and insurance companies). The finding of the study shows that the cost of public issue of the new companies in Nepal is relatively very high in comparison to that of the neighboring country India. However, in contrast to this fact, cost on rights issue in Nepal is relatively very low.

ix) Shortcoming in Accounting and Audit Practice of Non-financial Companies.

Shortcoming in accounting and audit practice of non-financial companies has led to the incomplete disclosure to investors and the Securities Board does not have powers to force these companies for making true and complete disclosure.

x) Institution Capabilities of Securities Board

Securities Board is responsible for regulating and monitoring of the entire securities business in Nepal. Its present organizational structure, the number of staffs and resources available, it is not possible for the board to perform its roles effectively and efficiently.

xi) Lack of Transparency and Integrity in Tax Collection

Tax Officers have wide discretionary powers and this leads to reluctance on part of companies to publish objectively audited accounts which in turn deprives the investors the essential basis for judging such company. In the absence of true information, investors are reluctant to invest in the shares of these companies.

xii) Lack of Corporate Culture and Corporatization

Development of corporate culture and corporatization of the companies is one of the important steps toward the development of primary market. The development of corporate culture encourages the private companies to go into public, which can bring professional expertise as well as the required funds from the public. Nepalese private companies are mostly run as a family business and they prefer to go to commercial bank

rather than to public for meeting capital requirement. As the healthy and good performing companies are reluctant to go to public, which can be attributed to lack of corporate culture, it has negatively affected the development of primary market.

xiii) Lack of Professionalism in Issue Management and Underwriting

The issue manager has to study and analyze the issuing company's nature of business, managerial and financial aspects, track record, and other relevant aspects minutely. After evaluating the prospectus and other aspects, the issue manager has to submit the Due Diligence Certificate to the Securities Board. The poor performance of the companies after raising capital through public issue has raise question about the validity of the analysis. Similarly, the underwriter is responsible for not only to purchase the share of the initial issue in case of under subscription, but also to evaluate thoroughly all the aspects of the company, including its financial aspects. As the majority of the companies after public issue are performing very poorly, it suggests the lack of proper analysis in the part of underwriters too.

A few companies have been going to the public from the insurance and hydropower sectors. Very large and profitable joint venture companies like Dabur Nepal, Surya Nepal, Barun Beverage are still to go in the public. Now, what are the problems in primary issues because of which these companies are not going in the public?

The number applicants in the public issue of the financial institutions are increasing day by day. The probability of receiving shares in the allotment is being very less. Is the present allotment model suggested by the NEPSE is appropriate?

Similarly, the issuing companies must list its share in the Npse within 45 days of allotment of shares but companies are not doing this. For example, Shikher insurance Company listed its share long after the specified time period.

Nepal Government is encouraging investors to initiate hydropower project. Some of the hydropower companies like Arun Valley Hydropower Company is preparing to issue shares in the public. Similarly, trading company like Salt Trading Corporation is planning to issue debenture amounting to Rs 500 million to build shopping complex to expand its business in the real sectors. In this situation, what is the future prospect of Nepalese primary market?

1.3 Objectives of the Study

The main objective of the study is to identify the existing problems and future prospect of Nepalese primary market. The other objectives of the study are as follows:

1. To analyze the problems and prospects of primary market in Nepalese capital market.
2. To examine the initial public offering procedures in Nepal.
3. To evaluate the future prospects of the primary market.
4. To analyze the role of IPO in the development of capital market.
5. To suggest on the basis of major findings.

1.4 Scope of the Study

Stock market reflects the situation of economy. When stock market is booming the economy is good and market is declining the economy is in recession. It represents also the countries policies towards industries. Policy is formulated of regularized by rules and regulation between different Act and Guideline (rules and regulation). This study is needed to find our problems and prospects in the near future. What policies can be formulated, what regulatory acts are needed and necessity of amendments regarding the rules and regulation to develop it and make the market perfect functioning.

It is also needed to find out the views of potential investors and government and other financial institutions about the related organizations. Similarly, it is needed to study about AGM held by organizations in time and disclosures of them. The standard is one of the elements for the stock market development. Financial statement should maintain according which fulfill the requirements of related party's needs information.

1.5 Limitation of the Study

The study is made for the partial fulfillment of Master in Business studies program of Tribhuvan University. So, it is not a comprehensive study and it focused to analyze certain aspects of primary market in Nepal. The result obtained from this study can not be generalized. Similarly the time and resources constraints are other limitation.

1.6 Organization of the Study

The study will be organized in to five chapters. Which are:-

Chapter I

Chapter one deals with introduction, problem of the study, objective of study, scope of the study, limitation of study and organization of the study.

Chapter II

Chapter two consists of review of literature. This chapter is subdivided into various sections such as conceptual framework, review from different studies, review from journal, article and magazine and review from master's thesis for the concerned topic. It includes all the Nepalese context's problem and prospect of primary market.

Chapter III

Chapter three present methodologies adopted for the research. It comprises research design, sources of data method of analysis and its descriptive presentation.

Chapter IV

Chapter four deals with the techniques used in analyzing the collected data and its presentation in the descriptive and analytical manner.

Chapter V

Chapter fifth consists of summary, conclusion and recommendation.

CHAPTER - II

LITERATURE REVIEW

2. Introduction

This chapter is divided into two parts. In the first part some conceptual framework has been provided and in the second part review of past research works, books, journals and articles has been provided.

2.1 Conceptual Framework

2.1.1 Financial Market

Financial Markets provide a forum in which suppliers of loans and investments can transact business directly. The loans and investments of intuitions are made without the direct knowledge of the suppliers of funds (savers), suppliers in the financial markets know where their funds are being lent or invested. The two key of financial markets are the money and the capital market. Transactions in short term debt instruments, or marketable securities, take place in the money market. Long term securities (bonds and stocks) are traded in the capital market (Gitman, 1988:345)

2.1.2 Money Market

Money market activities include primary and secondary market activities in short-term negotiable instruments such as Treasury Bills, Government Bonds, Certificates of Deposit, Banker's Acceptances and Commercial Paper or Promissory Notes. Merchant bankers are usually users and market-makers (dealers), rather than brokers in these types of paper.

In theory, the money market is different from the capital market. In practice, however, in most countries with efficient financial markets (that is, the money market and the capital market combined), the merchant banks are active in both. This is a simple function of the fact that a negotiable money market instrument for all practical purposes is simply a shorter-term capital market instrument. Therefore, the techniques and facilities needed to operate in the money market are essentially the same as those needed to operate in the capital market.

2.1.3 Capital Market

The capital market is defined as a place where finance is raised by companies for meeting their requirement of funds for new projects, modernization and expansion programs, long-term working capital needs and for various other purposes. The capital market mobilizes savings of individuals as investment in shares, debentures, Units of mutual funds and other like financial instruments, which are ultimately deployed for productive purposes in various sectors of the economy.

A place where long term lending and borrowing takes place is known as capital market. The capital market is the market for long-term loans and equity capital. Companies and the government can raise funds for long-term investments via the capital market. The capital market includes the stock market, the bond market, and the primary market. Securities trading on organized capital markets are monitored by the government; new issues are approved by authorities of financial supervision and monitored by participating banks.

Capital market refers to the links between lenders and borrowers of funds, arranging of funds-transfer process to seek each other's benefit.

Capital market consists of the various suppliers and users of long term finance. It is differentiated from the money market which embraces short-term Finance. The capital market serves as a link between suppliers and users of Finance. It is a mechanism for the mobilization of public savings and channeling them in productive investment. In this way, an important constituent of the capital market is the securities market. It has a wide term embracing the buyers and the sellers of securities and all those agencies and institutions which assists the sale and release of corporate securities.

Primary markets are absolutely vital to capitalistic economic if they are to function properly, since they serve to channel funds from savers to borrowers. Furthermore, they provide an important locatives function by channeling the funds to those who can make the best use of them-presumably, the most productive. In fact, the primary function of the capital market is to allocate resources optimally. A securities market with this characteristic is said to be other hand, is one with the lowest possible prices for transactions services.

The capital market is a financial relationship created by a number of institutions and arrangements that allows the suppliers and demanders of long term funds, funds within maturities of more than one year to make transactions. Included among long term

funds are securities issue of business and government. The backbone of the capital market is formed by the various securities exchanges that provide a forum for debt and equity transactions. The smooth functioning of the capital market, which is enhanced through the activities of investment bankers, is important to the long run growth of business.

The capital market also comprises two segments—the new issue of market that is commonly known as the primary market and the secondary market where already issued securities are traded. For the purpose of this manual, only primary market would be dealt in detail.

2.1.4 Security Market

Security market sets a price for the securities it trades and makes it easy for people to trade them. Securities market facilitates the sale and resale of transferable securities. The security market can be defined as a mechanism for bringing together buyer and sellers of financial assets to facilitate trading. Securities market is classified into two; the market in which new securities are sold is called the primary market and the market in which existing securities are resold is called the secondary market. Secondary markets are created by brokers, dealers and market makers. Brokers bring buyer and seller together with themselves actually buying or selling; dealers set price at which they themselves are ready to buy and sell (bid and ask price respectively). Broker and dealer come together organized market or in stock exchange (Gitman, 1992).

Securities are traded in a market called securities markets. Although, securities markets are concerned in few locations, they refer more to mechanism, rather than to place, designed to facilitate the exchange of securities by bringing buyers and sellers of securities together. In other words, people and organizations wanting to borrow money are brought together with those having surplus funds in the securities markets. Securities, such as equities, short and long term debt instruments, derivatives etc are the products that are traded in the markets, institutions such as investment bankers and security firms, securities issuing institutions such as government and corporate bodies and the participants of the securities markets. Securities markets major function is to provide line between saving and investment there by facilitating the creation of new wealth.

Securities market covers both primary and secondary. The difference between the two markets is, the primary market consists of the companies making the issue of securities and the members of the public subscribing to them. Whereas, secondary market involves the purchase and sale of securities already issued to the general public and is traded in the stock exchange. The primary market also comprises the offer of securities to the existing shareholders of the company on right basis.

This study is only concerned with initial public offerings so, it deals with the process and activities incurred in rising of funds from the primary market. The operation of the secondary market, though is an important operation scope of the merchant banking, is not covered in this manual.

Primary market and the secondary market are present in both the capital market and the money market.

2.1.5 The Primary Market

In the definition of primary market made above an addition is to be made. That is, depending upon the company offering securities for the first time or in succession, primary market can have public offerings as initial public offerings or the successive public offerings or so on.

2.1.6 Public Offerings

It is the raising of long-term funds for governments or corporation from a fund sufficient public group in the primary market. The most important aspect of public offerings is its role as the single most effective means by which government and corporate entities can obtain long-term (debt or equity) on a permanent basis. This not only permits them to broaden their sources of finance beyond the banking system but, because the banking system is usually a short–or medium term floating rate lender, the securities market is often the only means of obtaining large sums of fixed rate, long-term funds.

2.1.6.1 Advantages of an IPO

As discussed above, the primary reasons for conducting an IPO are to raise money and to create liquidity for investors. There are also important incidental benefits to going public. Objective benefits include (i) obtaining a readily ascertainable market value for the company's stock, (ii) the ability to make acquisitions through the payment of

securities rather than cash, (iii) greater access to financing through commercial lending, (iv) greater access to the financial markets for follow-up offerings, and (v) heightened name recognition and prestige among customers and suppliers. Less objective benefits are the sense of success and accomplishment that accompanies a successful IPO and becoming a publicly traded company.

2.1.6.2 Disadvantages of an IPO

The major disadvantage to becoming a publicly traded company may be compliance with the act reporting requirements. While registering under the act is quite simple, the periodic and event-based reporting obligations under the act require a significant amount of time and expense. In addition, the act obligations will compel disclosure of information that the issuer, its directors, management and controlling stockholders might otherwise want to keep to themselves. Financial and business information, executive compensation, transactions between the company and its directors, management and major stockholders, and certain employee benefits must all be disclosed in reports filed with the SEC, mailed to the stockholders, and made available to the public upon request. Directors and officers, as well as major stockholders, also must file reports with the SEC disclosing most transactions in the company's securities. Also, the failure to accurately make such reports may result in civil or criminal penalties.

The direct financial costs, including legal, accounting and printing fees, of conducting an IPO and of being a publicly traded company are substantial, as are the indirect costs of the time required to be spent on these matters by management.

Also, the management and governance of a publicly traded company is more difficult and less flexible. The solicitation of stockholder votes on any matter is strictly regulated under the act, and rules of the exchange on which the securities are listed require certain matters to be approved by stockholder vote even if not otherwise required by state law. Additionally, because of pressure to raise the price of the company's stock, management may feel persuaded to adopt policies aimed at achieving short-term results rather than long-term goals.

2.1.6.3 Timing of an Public Offering

Obviously, not all companies that would like to go public are in a position to do so. Factors relevant to a company's ability to successfully close an IPO include (i) its past financial performance, its financial projections for the future, and its ability to generate consistent increases in revenues and earnings, all of which are crucial for a public company to survive in the market place, (ii) the experience and depth of the company's management team, (iii) a solid product position in the market with growth potential, (iv) a focused mission set forth in a well written business plan to present to prospective underwriters, and (v) attorneys, accountants and public relations firms experienced in working with the SEC. Especially in the case of technology-based companies, the determining factor in the success of an IPO may ultimately be the receptivity of the stock market to new issuances in a Company's particular industry at the time that the IPO is undertaken.

The company will have to satisfy the underwriters that all of the above criteria are met, and even then the underwriter may insist on changes to the company's capital structure as a condition to its engagement. For example, the underwriters might require the company to affect a reverse stock split prior to the closing of the IPO in order to price the shares being offered in a typical IPO price range. If the underwriters do not feel that the company is offering a sufficient number of shares to ensure an acceptable "float" of publicly traded shares, they might require that certain stockholders participate in the offering by selling some of their own shares (a "secondary offering"). The underwriters might also insist on fundamental changes in the company's means of conducting its business as a condition to its engagement, such as the cessation of insider transactions and perceived conflicts of interest and the appointment of outside directors. Companies which are not willing to make such changes may not be able to attract an underwriter willing to manage the IPO.

If the issuer belongs to a certain industry that is particularly attractive to investors at the time of the proposed IPO, it will have more leverage in choosing and negotiating with an underwriter. Conversely, if market conditions are unfavorable at the time of the offering, the issuer will have less flexibility in how the deal is structured and may have to postpone the IPO altogether.

2.1.7 Types of securities offered in the primary market

Different types of securities offered in the primary market. They are:

2.1.7.1 Common Equity/ Stock

These are the offerings that entitle the holders or the buyers of the offerings the stake on the equity of the issuing company. In addition, they are entitled to:

- Voting right at the general meetings of the company and have the right to control the management of the company.
- Right to share the profits of the company in the form of distribution of dividend and bonus shares.
- In the event of the winding of the company, equity shares capitals are repayable only after repayment of the claims of all the creditors and preference shareholders.

2.1.7.2 Preference Share/ Preferred Stock

Preference shares capital mean, in the case of a company limited by shares, that part of the capital of the company which,

- Carries a preferential right to payment of dividend during the lifetime of the company;
- Carries, on a winding up, a preferential right to be repaid the amount of capital paid-up.

The different types of preference shares are:

- Cumulative Preferred stocks
- Non-cumulative Preferred stocks
- Redeemable Preferred stocks
- Non-redeemable Preferred stocks

- Convertible Preferred stocks

2.1.7.3 Bond/ Debenture

Debenture includes debentures stock, bonds and any other securities of a company, whether constituting a charge on the assets of the company or not. Debenture is a document that either creates a debt or acknowledges it, and any document, which fulfills either of these conditions, is debenture. The characteristic features of a debenture are as follows,

- It is issued by the company and is in the form of a certificate of indebtedness.
- It usually specifies the date of redemption. It also provides for the repayment of principle and interest at specified date or dates.
- It generally creates a charge on the undertaking or undertakings of the company.

The different types of debentures are:

- Secured debentures
- Unsecured debentures
- Redeemable debentures
- Perpetual debentures
- Convertible debentures

2.1.7.4 Warrants

The warrant gives a right to the holder to obtain equity shares specified in the warrant after the expiry of a certain period at a price not exceeding the cap price specified in the warrant. The warrant is a tradable and negotiable instrument and is also listed on the stock exchanges. It comes in different forms, mostly:

- Bonds with warrants
- Preferred stocks with warrants

Beside these instruments there is other instrumental mix available to the investment bankers to provide to the primary market investors. But, these are beyond the scope of this manual to describe.

2.1.8 Initial Public Offering (IPO) Manual

Initial Public Offerings (IPO) manual is the detail procedure of handling Initial Public Offerings of the companies seeking “going public” for the first time. This manual outlines all the activities and steps that have to be observed by all issuing companies and issue managers in respect to Initial Public Offerings (IPO). This manual has been prepared with a view to present a detailed, descriptive and step-by-step action sequences in the Initial Public Offerings, relevant to all the companies offering shares to the general public. But, it is subject to periodic amendments and supplements.

The Public Offering is not an easy task. There are many organizations involves during this periods. They are:

2.1.8.1 Issuing company

Issuing company is the company raising funds from the general public through the process of public offering. The purpose of public offerings is for the collection of funds from general public, a fund sufficient group, by the company as per its requirement of business expansion. The company seeking for public offerings could be a completely new company (initial public offerings), a new company set by the existing company (initial public offerings) or by existing listed company (successive public offerings).

As per the Company Act, only public companies are liable to go for public offerings. The Act specifically states that private companies are not allowed to sell their shares and debentures in the free market. For public company issuing debentures, the reasons for such issue, project to be financed and its estimated budget along with the information about secured or naked nature of the debenture, needs to be approved from the governing bodies.

NRB has made mandatory that financial institutions must go for common stock public offerings within specified time of operation commencement. NRB has also set forth different minimum percentage of equity holding to be offered to the public shareholders. For commercial banks, minimum shares to be held by public is 30%; for finance companies, it is 40%; for development bank it is minimum 30% and maximum of 50%. In the case of foreign participation, their equity holding would be arranged from the percentage allocated for the public. For finance companies, in the event of foreign

participation, the minimum percentage to be allocated to the general public is 25% of paid-up capital.

For other public companies such compliance to go into public offerings of equity holding are absent. For such companies, going into public signifies the need of funds for the company rather than the obligation.

The Provisions and Conditions for Securities Registration and Issue, 2051 has set the guidelines that before going into public offerings, issuing company should take into consideration that,

a. If the issuing company is industrial institutions

- The institution has bought the land or made other provisions in which necessary infrastructure like factory; office buildings, go downs etc. are already build in or made necessary arrangements for it.
- Necessary technology has been selected for which spare parts of machineries needed have been bought. If not, LC has been opened to buy the necessary technologies.
- Estimated budget has been proposed for the project to be implemented and for which if loans are required, such agreements are already made.
- In the absence of long-term loan agreement, issue securities are underwritten.
- Necessary approvals according to the existing Acts have been taken.

b. If the issuing company is financial institutions

- According to the nature of the business, required infrastructures are installed.
- Approval has been taken under the Company Ordinance 2063.
- For commencing other activities, authority and approval from governing bodies based on existing Acts has been taken.

2.1.8.2 Merchant Bankers

Merchant bankers are intermediaries in which they work as mediators in the fund mobilization from the general public to the business groups. The funds are raised from the hypothetical market that comprises widely spread fund surplus groups, mainly the general public and the concentrated fund deficient groups, mainly the business groups. Funds are raised under different tool names that have long term and short-term maturing period. According to such maturity period of the tools traded, market is identified as capital market for long-term and money market for short-term tools to be traded.

The role of merchant bankers in this market is to help create and expand securities underwriting, the secondary market for securities and money market. They also provide additional services in advising corporations and managing investment portfolio for the needing groups.

The concept of merchant Banking differs from other commercial and development banks in respect that they do not require large funds to be invested as a principle. Their sources of income are basically the service charge they charge to their clients for playing intermediary role in the fund mobilization and their advisory role. Typically, the activities of domestically oriented investment banks can be grouped under,

- Securities Underwriting
- The secondary market for securities
- The money market
- Corporate advisory services
- Investment portfolio management services, and also
- Venture capital
- Leasing/Hire purchase
- Other services (insurance, real estate etc.)

The role of merchant Banking in managing the public offerings comes under the heading of securities underwriting. The working process of which would be described comprehensively later.

For the working of merchant Banking function in Nepal, Nepal Rastra Bank (NRB) has set forth the working guidelines. Guidelines have identified working of merchant Banking into two sets of functions. The first set is the non fund-based functions and the second set is fund-based functions.

Fund-based activities identified for the merchant Banking are:

- Bridging finance
- Underwriting
- Project Finance
- Venture Capital
- Acquisition & Merger

Non fund-based activities identified for the merchant Banking are:

- Share issue management
- Mutual Fund
- Portfolio Management
- Corporate Counseling
- Project Counseling
- Debenture Trusteeship
- Arranging International Finance
- Investment Advisor
- Advising Corporate Mergers

NRB has set the directives as for non fund-based activities of merchant Banking, for underwriting and for bridging finance it is not necessary to take separate approval from NRB. But, for other fund-based activities of merchant banking, it is necessary to take separate approval from NRB for different activities to be undertaken.

Under the NRB directives of per client loan advancement and facility limit provision, such loan and facility can be provided to a client up to:

- In maximum of 25% of primary capital in fund-based activities.
- In maximum of 50% of primary capital in non fund-based activities.

In Nepal there are 7 merchant banks are already established. They are providing issue manager, lead underwriter, Register, Transfer of Shares etc. services to other institutions.

Securities Board

Securities board has been formed under the Securities Exchange Act, 2040 Clause 3. This legislation has required for the creation of an independent statutory Board to be an apex authority for the securities market, thus resulting into the formation of Securities Board.

The need of legislative body is for maintaining healthy and orderly development of the securities markets and to ensure adequate investor protection. Establishment of SEB is necessary to promote markets that ensure:

- **Fairness:** The markets must promote integrity in dealings, high standards of conduct and good business practice.
- **Efficiency:** The markets should with professionals and be well informed, offering high standards of service at reasonable cost.

- **Confidence:** The market must inspire confidence in both investors and issuers to actively participate in and rely more on the securities markets.
- **Flexibility:** The markets should be resilient, innovative and be continuously responsive to the needs of all market participants.

With the objective of providing this to the market, in accordance with the Act, the Security Exchange Bylaws 2054 has defined the work, responsibility and the authority of the Board as:

- To work in safeguarding the interest of investors and help develop capital market.
- To advise Nepal Government (NG) in formulating policies for the development of the capital market.
- To implement the policies set forth by NG regarding securities exchange.
- To supervise the work process management and working procedure of those involved in securities exchange to make issue management of securities regular and well managed.
- To approve registration of securities and issue of securities.
- To register the name of securities issue dealers and give them approval letter.
- To interrogate and supervise the workings of securities exchange dealers.
- To formulate clauses to be followed by the securities exchange market and the dealers in security exchange market.

- To supervise, interrogate the working of securities market, securities dealers and the listed companies and when necessary make needed directions or undertake necessary actions.
- To develop and implement directives for proper management of securities market and for regular and well managed securities exchange.
- To approve Securities Market Sub-directives.
- To collect notices, data and prospectus from the listed companies and companies with securities registered; make above available information to the interested investors.
- To work for the healthy, competitive, regular and managed operation of the capital market with the objective of safeguarding the interest of the investors for continuous growth of the market.

This Bylaw is the amendment of Securities Exchange Bylaws 2050.

Role of Securities Board in Issue of securities

In its approach to manage public issues of securities, the Board will bear in mind

- a. Protection of rights and interests of the investor, especially,
 - The right to adequate, true and fair information
 - The need for liquidity
 - Prompt, fair and equitable allotment
 - Easy and efficient service in allotments and transfers

- b. The need to encourage corporate entities to tap the securities markets for their diverse resources needs.

The Board would endeavor to evolve market and institutional structure, a set of instruments and methods of public offerings to cater the above objectives.

The legislative provisions relating to public issues of securities may be classified under:

- a. Capital control, governing issue of securities and the terms of their issues;
 - To regulate terms of issues of securities from the viewpoint of investor protection, issuers needs and overall development of the securities market; and
 - To promote sound capital structure of companies.
- b. Prospectus provisions, governing the disclosure of information at the time of issue of any security;
- c. Obligations of regular disclosure of financial and other information on entities making public issues;
- d. Listing requirements governing traded securities;
- e. Provisions governing allotment and transfer of securities.
 - Ensuring fair and equitable allotment; and
 - Promoting speedier and more efficient service in matters of allotment and transfer.

2.1.8.4 Offices of the Registrar of Companies (ROC)

Registrar of Companies (ROC) is the governing body for any institution registered under Company Act. In its governing role, it observes and regulates any company going into public examining whether the process of “going public” is in accordance with the rules and regulation set forth by the existing Company Act or not.

As per the Company Act 2063, public companies need to publish their prospectus before issuing securities to the public. Before publishing prospectus, one copy of the prospectus needs to be submitted to ROC. In this process, ROC approves the prospectus to be published. While approving the prospectus, ROC makes sure that important information is not missed out and unnecessary information is not mentioned. In the presence of such changes, ROC sends it back to the company for necessary changes. Upon satisfactory changes ROC grants approval to issuing company to issue the prospectus. Apart from approving the prospectus to be published by the issuing company before going into public, ROC does not play other major role.

2.1.8.5 Stock Exchange Market

Stock exchange has been defined as any body of individuals, whether incorporated or not, constituted for the purpose of assisting, regulating or controlling the business of buying and selling of or dealing in securities. The stock exchange therefore is the most important institution in the secondary market. In the primary market, it comes into play during primary share allotment, during issuing share in premium and when Securities Board asks Securities Exchange Market for its opinion.

Securities Exchange Act 2063 has stated that for the operation of the stock exchange market, approval needs to be taken from the Securities Exchange Board. Any registered institution except private companies willing to do or allow others to do security transaction should get approval for securities exchange market from the securities board.

After the issue of securities to the public, the Act requires that companies be listed in the Security Exchange Market before the floated shares can be traded in the market. Nepal Stock Exchange Limited (NEPSE) is the only stock exchange market in the country.

2.1.8.6 Financial Institutions

They are financial intermediaries like commercial banks, finance companies (merchant bankers), and development banks and cooperatives institutions. These institutions are established under the Company Act and Nepal Rastra Bank Directives. These financial institutions perform the role of intermediaries in the securities issue as per the authority received from the Securities Exchange Board. Financial Institutions are involved in securities issue process as:

- Issue managers
- Underwriters
- Collection centers
- Bankers to the issue

The role of financial institutions is to manage the issue process and be intermediaries in the process of transfer of funds from the investors to the issuing company. The financial institutions may also play a role of creditors to the issuing company by providing bridge finance.

Securities Issue By laws has specified required capital for intermediaries in the securities issue and transaction as,

Transaction Type	Authorized Capital (‘000)	Paid-up Capital (‘000)
Issue registration & issue management, Issue Underwriters	NPR. 20,000.00	NPR. 10,000.00
Dealer in securities market	NPR. 10,000.00	NPR. 5,000.00
Market makers in securities market	NPR. 10,000.00	NPR. 5,000.00
Brokers in securities market	NPR. 400.00	NPR. 200.00
Intermediaries in securities transfer, registration etc.	NPR. 400.00	NPR. 200.00

Source: SEBON Annual Report

2.1.8.7 Nepal Rastra Bank (NRB)

Nepal Rastra Bank is the central banking authority in Nepal. It is the governing authority in setting guidelines to all the financial institution regarding its area of operation. But, in the case of public offerings, its involvement is very minimal. Its role in the issue process is only to grant financial institutions approval to be involved with

different role in the issue process. Also for different fund based activities of merchant banking, approval needs to be taken from Nepal Rastra Bank.

2.1.9 Terms Involved in the Process of Initial Public Offerings of Common Stock

2.1.9.1 Initial Public Offering (IPO)

It is a process by which an institution raises desired capital through issuing of securities (common stock, preferred stock, bond, commercial paper and debentures) in the capital or money market for the first time.

For the purpose of public offerings, Company Act has specified that the public issue process of any public company should be managed through the institution receiving authority from SEBO. Internationally, financial institutions with the merchant banking operations, manage the overall issue process of any public limited company. Such institution managing the overall process of the public offerings is termed as an issue manager.

2.1.9.2 Issue Manager

Issue manager is the institution solely holding the responsibility of managing the public offerings of any issuing company. Securities Exchange Act, 2040 clause 18, has defined issue managers as institutions holding license from the Security Board to manage public offering process. The format of application letter and required information to be provided while registering for issue manager are given in the appendix.

2.1.9.3 Lead Manager

In the event of more than one issue managers managing the issue of securities of any company, the term lead manager is used to identify the individual issue managers. The existing Act and the Directives have not clearly identified the maximum number of lead managers managing securities issue of any company at the same time.

2.1.9.4 Underwriting

Underwriting is an agreement between the issuing company and a financial institution like bank, merchant banker, broker or other person, providing for their taking up the shares or debentures to the extent specified in the agreement between them, if it is not subscribed by the public. The underwriting agreements ensure that the public issued is fully subscribed. The commission paid to the underwriters as consideration for the underwriting arrangement is known as underwriting commission.

The existing Company Ordinance does not require that the underwriting of all securities issued to be mandatory. Clause 26 of Company Act has specified that “in the event of issued securities subscribed less than the 50%, such securities should not be distributed to the general public”.

The Securities Exchange Directive 2055 has made mandatory for underwriting for those institution stated as “institution established as manufacturing industry and has not appraised its venture project from the financial institution for the purpose of loan agreement, should underwrite its securities before being offered to the general public”.

But in the case of financial institutions, the governing body NRB requires that issue of securities by commercial banks and development banks are fully underwritten. But in the case of finance company the requirement has been relaxed. Similarly, Beema Summity has made the public issue of securities of insurance companies to be fully underwritten. Under the underwriting provision, such information is to be mentioned in the prospectus.

The reservation for preferential allotment for reserved categories should be excluded and underwriting is compulsory only to the extent of the offer to the public.

2.1.9.5 Lead Underwriter

Lead Underwriter is the one that arranges the whole underwriting process for the issuing company with the help of other sub-underwriters. The issuing companies and intermediaries should note that underwriting is a serious contractual arrangement having financial implications on the issuer and the underwriter. The business of underwriting, therefore, presupposes inherent financial strength on the part of the underwriters. In the process of identifying underwriters, therefore, issue manager must satisfy himself about the net worth of the underwriters and their outstanding commitments and disclose.

In the event that the issued shares are not fully subscribed by general public, the distribution of unsold share to the underwriters would be held on the pro-rata basis based on the number of shares committed by them to underwrite.

2.1.9.6 Underwriters or Sub-Underwriters

They are the smaller institution agreeing to underwrite fewer number shares. Underwriters and sub-underwriters work under the management of the lead underwriter. Their financial responsibility remains within the total amount of shares agreed by them to undertake.

2.1.9.7 Banker to the Issue

Banker to the Issue(s) is (are) normally a commercial bank(s), which provide(s) the custodian service to the issuing company and keep the subscription money. Bankers to the issue may or may not receive applications from the investors, issue acknowledgements for the same, and enter the application details in application schedules. It also involves in the process by realizing the proceeds of the cheques/draft and issue final certificates to the issue manager for the number of applications and amount collected. Issuing company in consultation with the issue managers makes the appointment of bankers to the issue.

The bankers to the issue generally comprises the consortium of bankers providing working capital finance to the company, the banks providing underwriting assistance for the issue, the bank associated with the issue managers and other banks which are regularly and efficiently handling public issue work.

2.1.9.8 Collection Centers

Collection Centers are normally financial institutions such as banks, finance companies, brokerage houses etc. Collection centers receive applications from the investors, issue acknowledgements for the same, and enter the application details in application schedules. They also realize the proceeds of the cheques/draft and issue final certificates to the issue manager for the number of applications and amount collected. The appointment of collection centers is made in consultation with the issue managers.

2.1.9.9 Prospectus

The prospectus is defined as, “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 shares in, or debentures of, a body corporate”.

The Company Act 2063 has made mandatory that any public institution going into public offerings must issue the prospectus before issuing the securities to the public. Act made provision before publishing for the public; the prospectus signed by the board of directors should be sent to get approval from the Office of Registrar of the Companies and Securities Board. The requirement is made to make sure that the information provided to the public is as per requirement and is not manipulated to mislead the public. The prospectus published for the public should state in the publication the approval from the Office of Registrar of the Companies.

The Company Act 2063 has stated that matters referred in the prospectus are the liability and responsibility of company publishing it. Board of Directors signing the documents is answerable to the matters stated in the prospectus. In the event that, company has knowingly published false statement in the prospectus and believing on which if securities has been purchased and loss incurred, such loss coverage would be the personal liability of the directors signing the prospectus.

In short, prospectus is a legal document containing important features of Article of Association, Memorandum of Association, and important decision taken by the board of the company affecting the future of the company and important conditions to be obeyed by the general applicants. The main purpose of the publishing prospectus is to inform public about the company and the issue.

2.1.9.10 Budget for the Issue

Budget for the issue is a tentative figure of expenses that is estimated to incur in the process of public offerings. The budget is to be born fully by the issuing company, if not, according to the understanding reached between issuing company and the issue manager/s.

2.1.9.11 Application form

It is a form provided to general public to apply for the issued securities by a company. The application forms needs to be filled both in English and Nepali. It contains:

- Information about the company and issue
- Space for applicants to fill in his/her information

Application form is the legal document that the investor provides to the company stating the number of shares of a company he/she is willing to accept. The applicants submitting the application forms would imply that he/she has accepted the terms and conditions stated in the application form with the full knowledge about the matters referred in the prospectus. Attached with the application form a photocopy of citizenship is collected as a proof to applicants' acceptance to terms and condition and a remedy to possible discrepancies in identification. In case of minor applicants, citizen certificate of parents or guardian is to be attached.

2.1.9.12 Bridge Financing

It is a short term lending provided to the issuing company till the date of share allotment, backed by the collection from public issue. The company is to make the payment after receiving allocated shares money from public offerings. Normally financial institutions provide bridge loans to companies against their underwriting commitments. The said loans are adjusted against allotment of shares/debentures. The bridge finance is issued when

- Companies require to meet their immediate requirement of funds
- If there is a substantial lead-time between making a public issue and commencement of commercial production
- If issues is to be deferred to the most opportune time.

2.1.9.13 Memorandum of Understanding

In the process of issuing securities to the public, besides issuing company, different intermediaries are involved. Memorandum of Understanding is the legal agreement made between issuing company and different intermediaries. This agreement states the terms and condition in respect to the function and authority of the involved parties. Securities Issue and Issue Manager Directives, 2054 (7) has provided guidelines while going into agreements.

Different MOU to be signed in the process of issue offerings are,

- MOU between issuing company and the issue manager/ lead managers:
This is required as the Company Act requires securities issue process of any public company is to be done through the registered issue manager. This legal agreement between issuing company and issue manager specifies terms & condition, responsibilities and the authorities of involved party.
- MOU between issue managers and the underwriters: Except for the finance companies and manufacturing industries (except identified in Securities Exchange Directive 2055), all other public institutions, as per their respective directives, underwriting is mandatory.
- MOU between issue manager and the bankers to the issue.
- MOU between issue manager and the collection centers.

Except for the MOU between issuing company and the issue manager, other MOU is to be signed by issue manager on behalf of issuing company with the notification and the consent of the issuing company.

In the case of MOU signed between issuing company and the issue manager, Company Act 2063 requires that copy of such agreements needs to be submitted to Office of Registrar of Companies within 7 days of such agreements made.

2.1.9.14 Issue Commission

It is the commission charged by the issue manager to the issuing company for the service it has provided. Issue commission is paid for issue management process. The responsibility of issue manager in the issue process and for which issue commission is to be charged is to be demarcated in the agreement itself. The commissions are normally set as per the negotiation.

Securities Issue Bylaws (2nd amendment), 2054 has set the maximum limit for issue commission as follows:

Particulars	Percentage (of the issued amount)
For issue up to NPR. 25 laths	2.25 %
For issue above NPR. 25 laths to 50 laths	2.00%
For issue above NPR. 50 laths to 1 core	1.75%
For issue above NPR. 1 corer	1.50%

2.1.9.15 Underwriting Commission

Underwriting commission is the amount charged by the underwriters for underwriting the securities issued. Securities Issue Bylaws (2nd amendment), 2054 has specified that underwriters may charge in maximum 3% of underwritten amount as the service charge to the issuing company. The commissions are normally determined as per the negotiation.

2.1.9.16 Collection Charges

Collection charges are the amount charged by the collection centers for collecting the application forms and other documentation process. The collection charges are also charged on percentage of the amount collected. The percentage charged also depends upon the negotiation between issue manager on behalf of issuing company and the collection centers.

2.1.9.17 Refund Charges

Refund charges are the amount charged by the collection centers for refunding the oversubscribed money to the general investors. The refund charges are charged on percentage of the total amount refunded. The percentage charged depends upon the negotiation between issue manager on behalf of issuing company and the collection centers.

2.1.9.18 Fix Charges to the Collection Centers – Finance Companies

It is a fix charged given to the collection centers like finance companies for making required preparation for collecting application from the investors and conducting other required activities. The fix charge amount provided to the collection centers is also based on the negotiation.

2.1.9.19 Listing in the Nepal Stock Exchange Limited

The Securities Registration and Issue Approval Provision and Directives 2051 has stated that securities issued publicly or procedurally should be listed in the registered securities exchange market or provision to be listed within 3 months of closure of the issue. For listing securities in the market, the issuing company should comply by the clauses as,

- Percentage of public issue stated by the securities exchange market
- Required number of public shareholders
- Easy transfer of ownership of issued securities
- Other stated directive for the listing of the securities in the market

Since, the securities listing is mandatory for the securities issued, SEBO/N requires that the issue process be approved from the securities exchange market before approving for the public offerings. Securities exchange market gives approval based on its criteria for approval.

2.1.9.20 Pre Issue & Post Issue

Pre-issue in the issue process is defined from the point of approach by the issue manager to the prospective issuing company to the point of allotment of securities and refund of oversubscribed money to the investors. This segregation has been made on the basis of Company Act, as it requires that the process of securities issue, allotment of securities, collection of subscription needs to be done through institutions approved to carry out issue management.

2.1.10 Importance of Primary Market

In the past few years, the liquidity is very high in Nepalese market. With higher liquidity and very few alternatives available for investment, Nepalese investors are forced to look at the government bond market and commercial banks and financial companies. Since the commercial bank and finances companies have not been able to fully utilize there funds the interest rate for deposits have considerably decrease and the real rate of return after adjusting inflation may go to negative. Therefore, the public investors are looking for other alternatives, which give them higher return for their investment. This may be one of the reasons for heavily oversubscribing the public issues offered by corporate bodies.

As discussed above, the primary market in Nepal can be divided into tow categories:

- Primary Market for Government debt instruments
- Primary market for corporate Stock and debt instruments.

The main aim of our Thesis is to study the primary Market in Nepal, so, in this chapter the various instruments used by the corporate bodies to raise capital from the primary market and the scenario of Nepalese primary market after the establishment of Securities board, i.e. from the fiscal year 2050/051 will be dealt in detail.

2.1.11 Function and Role of Primary Market

The main function of the New Issue Market is to facilitate the ‘transfer of resource’ from savers to users. Conceptually, however, the New Issue Market should not be conceived as seeing the purpose of raising finance for new capital expenditure. In fact, the facilities of the market are also utilized for selling existing concerns to the public as going concern through conversions of existing propriety enterprises of private companies into public companies.

The origination, however, thoroughly done, will not by itself, guarantee success in an issue. A second specialized service i.e. “underwriting” is required. Underwriting however is only a stop-gap arrangement to guarantee the success of an issue. It depends upon the ultimate analysis of their being acquired by the investing public.

The sale of securities of the ultimate investors is referred to as distribution; it is another specialize job, which can be performed by brokers and dealers in securities who maintain regular and direct contact with the ultimate investors.

Thus, the ability of the New Issue Market to cope with the growing requirements of the expanding corporate sector would depend on these triple-service function desires. Institutional been efficient in their functioning, leaving investors under priced. Efficient financial intermediation involves reduction of the transaction cost or transferring funds form original source to financial investors. The total cost of intermediation is influenced by financial layering, which makes the individual institution's costs additive in the total cost of intermediating between saver and ultimate borrows. The aggregate cost of financial intermediation from the origination saver to ultimate investors those in developing countries.

2.1.12 Relationship between Primary and Secondary Market

The New issue market and stock exchange are interlinked and work in conjunction with each other. It can't be described as two separate markets because of the kind of function perform. Although they differ from each other in the sense that the new issue market with new securities issued for the first time to the public and the stock exchange deals with those securities which have already been issued once to the public.

New issue market and stock exchange is the relative strength and public confidence in joint participation in the sale, purchase and transfer of securities. In Nepal, the new issue market and stock exchange are connected to each other even at the new issue. The usual practice by firm issuing securities is to register themselves on a stock exchange by applying for listing of securities. Further, the securities markets are closely

connected to each other because of the sensitive nature of the movements of stock price to a great extent affected by environmental condition such as:

- Political
- Economic and social condition
- Industrial pattern
- Monetary and fiscal policies of the government.

The long- term and short-term change in these factors have an effect on the changes in prices of stock. The new issue market focused to find out these prices movement and general economic outlook to forecast the climate for investing and the success of new issue floated. Thus, the prices of share in the new issue market are sensitive to change in the stock market and act and react accordingly.

The primary and secondary markets have as symbolic relationship, which is confirmed by Granger's causality test. While the primary market crates long term securities, the secondary market provides liquidity through marketability of those instruments. Fresh capital issues are influenced by the level and trend in stock prices at the time of issue. New issue activities in the primary market add depth to the secondary market by enlarging the supply of instrument for trading and investment in the secondary market. Stock prices in turn are influenced by the large size and bunching of new issues.

2.2 Review of past studies

2.2.1 Review of Articles, Books and Journals

Paul (1960) in his article "The Review of International Capital Markets" published in the journal "The American Economic Review" has pleaded that the

development of world capital market appears to be reaching the state where they can make significantly greater contribution to world economic growth and trade. More importantly, the groundwork has been laid for the healthy development and future growth of international capital markets. Barring the intervention of war or other major disturbances, world capital market give promise of being able to play and increasingly important, through no predominant role in the movement of capital internationally.

Simha (1960) In connection with the necessary of capital market in his book “The Capital Market in India” has observed that capital is an extremely fascinating subject and efficient capital market is an indispensable prerequisite to economic development. In fact, even as regards the resources for the public sector, the capital market has a rather important role to play.

Obstacle of growth and prospects of Capital Market is clearly analyzed in “Business manager”. Vol 2, no.3 may 200 journals (magazine) which is given in some short point:

- Lack of sufficient education of most of the brokers and the unreliability of a few brokers in financial matters would lead in other countries to immediate disqualification. The importance of transparency is not yet understood at all, partly due to an erratic tax system and an even more erratic tax collection.
- To issue share is an extremely time consuming and extremely expensive procedure as cases like Tragaon, NIC and now Radisson as well as Nepal

Bank of Ceylon prove to be this is the case ever though there are easy ways out.

- To handle the bigger volumes the trading floor will need to be also bigger and floor it inclusive the back office will be fully computerized. Computerized networks will replace open our cry system these networks will make it possible, to extend the trading hours significantly.
- The transfer of shares will under go a sea change. The transfer will be mostly paperless, like in Bombay and at the National Stock Exchange in India. The need of approval of boards of directors or transfer of share will be minimized and will be more or less a thing of the past.
- The board of the stock exchange up to now dominated by government official with little power, will be submitted by a board dominated by broker houses, banks and finance institutions added by government represented and will have full enforcement powers.
- The actual broker community has in its majority little educational background, little know-how and nearly no international experience. In addition the financial standing is in most of the cases rather weak. The brokers of today will have been transformed in the next 10 years to financially much stronger brokerage houses with longstanding experience. Others, who are no changing, will be gone by then.
- In depth research of companies and sectors by brokers has not yet started. In ten year leading brokers will have their own in house research; smaller

ones will rely on outside research. Rumors, today's bread and butter for brokers will still be influential, but much less than today.

- Up to now broker have nearly no assets management activities. In future the Assets Management activity will play an important role for successful brokerage houses.
- The role of shareholders value should be improved while the idea of shareholder value is seen up to now only in the banking sectors, the shareholder value idea will be spread in 10 years from now to other sectors as well. But nowadays institutional investors are rare at the stock exchange. If the development in other countries like India is any indication, this should change in the next 10 years dramatically. In 10 years from now we believe, that institutional investors like Mutual Funds and Pension Schemes will dominate, while the role of the individual investors will be much lower than it is today's. As far as foreign investors are concerned, we are as yet not much hopeful. Still we do not exclude it, if the rules and regulations are getting more investor friendly and the liquidity topic can be solved.
- At present available sectors for investment are extremely limited. Similarly, securities nowadays available are ordinary shares, preference shares, one debenture and one mutual fund.
- The development of debt securities will be very important for the finance of long term investment, where entrepreneurs find it actually hard to get the needed long term means from the banking sector- still the market will not be in a position to offer derivatives by then in a bigger extent.

Shrestha (2002) has analyzed why the share market is inactive and what problems are the main causes for inactiveness and what measures should be done etc are carefully defined. Similarly, how the securities frauds and manipulation have occurred and to what extent they can be overcome would be highlighted here to draw adequate feedback to the regulating and controlling authorities to devise suitable laws to prevent such frauds and minimize manipulation in share price.

2.2.2 Review of Thesis

There are many master degree thesis prepared by various researches in the past year. Among them, some theses are reviewed here for analysis of literature.

Shrestha (2000) Conducted research on the topic of “Growth and Prospect to Stock Market in Nepal” tries to show the role of the capital market which has been increasing as to mobilize the saving of the nations and canalizes them into productive activities. But, the major problems in the process of development are to increase the level of saving and the channels those saving into investment that leads to economic growth. Capital market is playing a crucial role in the process of growth. In this way, the important of capital market arises as to proper allocation of accumulated savings to various economic, objective of his study were:

- To identify the legal obstacle in the stock market development
- To study existing transaction system

Panta (2003) Conducted research on the topic of “current Status of Share market in Nepal” the trend of the Nepalese stock market and present status of primary and secondary market as well as problems and prospects of Nepalese stock market. The findings are as follows:

- The development of stock market primarily depends on program and their implementation.
- In Nepal, the overall policy environment has not been conducive to the development of the stock market therefore it is difficult to develop more efficient secondary market, trading system for both equity and debt security.
- Restriction on foreign portfolio investment hindered market development.
- NEPSE does not have appropriate policies and memberships are fee structure to attract members outside KTM.
- In Nepal, banks dominate primary market in government debt instruments. OTC trading is not permitted therefore secondary market is totally inactive.
- Lack of necessary provisions in the laws and regulation of the privatization and automatics of stock exchange as well as for the establishment of central depository of securities (CDS).

The transparency and openness of transaction, quality professional’s services, adequate. Corporate financial disclosures and improved legal, regulatory and supervisory frame – are the urgent needs of Nepalese stock market.

Therefore it is important that the basic assumption in any effort for protection investors interest or boosting their confidence or developing the stock market is that business, which should be enabled to operate in an environment that remains conducive to growth and expansion but complete replication of any tailor made, as applied anywhere, may not work because the specifics in Nepalese stock market is different from other developed market.

Mahat (2001) Conducted research on the topic of “Future prospect of NEPSE in capital mobilization” is able to analyzed situation in Nepal where the industrial sector has very little access to private saving. Also be indicating the availability of industrial securities is nearly absent and the development of financial institutions that link the surplus spending units with the deficit spending ones is in the rudimentary stage.

He further concluded notwithstanding the underdevelopment state of financial institution in the country, growth of invest able funds becoming available recent years. This study also demonstrated the relatively very limited financial contribution of other financial institution to this sector but he does no indicate these factors, which help to uplift the financial contribution to the other sectors like provident fund and NIC etc.

It is acknowledged that a much greater use of resources available in the financial system of the industrial development of the country may not be very smooth and easy. He only specified the growth and potential (measures) of security market, capital market

regarding primary and secondary market. It was absent to show the problems face by the NIDC and other industrial as well as financial sectors. He just shows the preliminary and basic problems of industrial sector but not in broad way. His topic was “future prospects of NEPSE in capital mobilization” but according to the topic the sufficient future prospects/measures are not available in this study but can find thin basic context. There is not indication in the relations of primary and secondary market with economic condition of country in his study. But it is able to give the theoretical version of relationship of capital market with economic growth.

The findings on the term nature of sources and uses of funds and the current ratios of various size and industry groups also do not give any ground for complacency. Some industries were found to have financed a large part of the increase in current assets with the long-term sources of funds, while for others the increase in long-term source was hardly sufficient even to finance the long-term assets formations. He was given high attention to the working capital management in Nepalese industries

Pandey (2001) Conducted research on the topic of "Public response to Primary Issue of Shares in Nepal," with the objective of: identify the problem s of primary share issue market, assess the growth of primary issue market, analyze the pattern of public response to shares & find the reasons of variation. He has summarized the finding as: Public response in primary market is high due to lack of opportunities for investment in other fields. No proper investment analysis is been made. Despite this, public are attracted towards shares than other sectors, basically to increase their value of investment,

be it dividend capital gain or bonus shares. It can be seen that public response to primary issues on Banking and Financial sectors is normally higher than that of the manufacturing and services sector. Major causes for poor response in the period 1995-1998 were; interest rates were higher as compared to dividend yield, the public companies were not performing well and people did not know about the importance of investing securities. Now the response is highly positive because people are aware, money flow in the market is higher, people have seen that most companies are distributing dividends, share prices are increasing for most companies and a lack of better alternatives for investment. Now that the average interest rates have gone down, more can be obtained from investment in stock.

Paudel (2002) Conducted research on the topic of "Investing in shares of Commercial Banks in Nepal: An assessment of Return and Risk Elements," Major finding of his studied were: The shares of commercial banks in Nepal are heavily traded in the stock market and, therefore, these shares play a key role in the determination stock exchange indicators. The average mean return on market portfolio, as measured by percent changes in the NEPSE index, was 5.51 percent over the sample period. All the shares produced higher rates of return than the return on market portfolio. However, the risk-return characteristics do not seem to be the same for all the shares reviewed. The shares with larger standard deviations seem to be able to produce higher rates of return. The portion of unsystematic risk is very high with the shares having negative beta coefficient. The risk per Units of return, as measured by the coefficient of variation, is less than that of the market as a whole for all the individual shares. Most of the shares fall

under the category of defensive stocks, (having beta coefficients less than 1), except the shares of Bank of Kathmandu Limited. Return on the shares of Nepal Arab Bank Limited is negatively correlated with the return on market portfolio and, therefore, it has negative beta coefficient. From the analysis, it appears that none of the shares are correctly priced. Theoretically, the market price of an over-priced (under-priced) share will fall (rise) in order to increase the expected return such that the expected return equals the required return. Therefore, shares of Nepal Arab Bank Limited, Nepal Indosuez Bank Limited and Himalayan Bank limited which are overpriced relative to equilibrium thus market forces, will decline.

Habibullah (1999), "Financial Markets in Least Development Countries," evidences that in some Asian countries including Nepal economic development reflected in economic growth leads the financial development measured in the ratio of broad money to gross national product (M2/GNP). This implies that economic development has preceded the financial market development in the case of Nepal. But several other studies conducted in other LDCs reveal that the financial development has preceded the economic development. The stock market development measured by market liquidity, market capitalization and total turnover is correlated with current and future economic growth, capital accumulation, and productivity growth, as evidenced by Levine and Zervos (1996). The efficient money, foreign exchange and capital markets increase investment to the most productive sector of the economy and thereby increase output through saving mobilization. Such markets also price the risk associated with any investment accurately.

Kviback (2001), "Nepal Survey: Issues in Local Bond Market Development". Major finding of his studies were: The financial market in Nepal is relatively undeveloped. The government market is more developed, but prices are not market oriented. The state of development of equity markets indicates how well versed issuers, investors, and intermediaries are in dealing with securities at the primary and secondary market levels. Nepal's overall market is still in its infancy, however. The Nepal Stock Exchange (NEPSE) is a late development, founded only in 1993. It is owned by the government and is a not-for-profit institution.

CHAPTER - III

RESEARCH METHODOLOGY

3.1 Introduction

Research methodology describes the methods and process applied in the entire aspect of the study. In other words, research methodology is a systematized way to solve the research problem. Research methodology refers to the various sequential steps (along with a rationale, of each step) to be adopted by a researcher in studying a problem with a certain object in view (Cothari, 1994). A focus is given to research design, sample selection and size, data collection procedure, data processing, definition of variables, meaning and definition of statistical tools used. This chapter highlights the research methodology used for the study.

3.2 Research design

A research design is a plan, structure, and strategy to obtain the objectives of the study. The research is based on the secondary as well as primary data and information. Hence, the explanatory or descriptive as well as analytical research design has been used. The variables related with the performance of the company, market information and relevant subjects are included in the study.

3.3 Population and Sample

In the Nepalese context, due to the lack of information and poor knowledge, potential investors are manipulated or exploited by the brokers, financial institutions, companies and

other market intermediaries. So brokers, investors, experts are taken as a population and from the population brokers, experts and investors as well as the official of the companies are taken as sample.

3.4 Source and collection of data

- Primary source of data
- Secondary source of data

Primary sources of data are mainly based on interview and queries and secondary data are mainly based on Booklets, trading Volume issued by Nepal Stock Exchange. Other primary data are collected from Nepal Security Exchange Board Nepal.

Primary and secondary source of data

- The major sources of secondary data are Nepal Stock Exchange (trading volume 2004/05), Rastra Bank, brokers and publication including daily papers. Secondary information was collected from these mentioned sources.
- Information has also been collected form Department of Industry, Banks, Financial institution and SEBO/N to asses the trend and the future potential.
- Interviews were conducted with the brokers and official of NIDC and stock exchange market and securities Board and selected experts to determine the quality, value and volume of transactions, identify reason

for fluctuation in price and volume of transactions and to assess the future trend.

- Interviews are making with a number of potential investors whose shares investment available in different companies to obtain their opinion and views regarding the present and future situation of stock market.
- Other related different statistical and financial tools are used.

This study is based on primary source of data and less on secondary sources of data for showing problems and prospects of primary and secondary market in Nepal. The primary sources of data used are interviews and questionnaire but the secondary sources of data used for analyzing areas follows:

- Trading report published by stock exchange Nepal.
- Financial statement and other transaction of listed companies listed by NEPSE/N.
- Out side published material directly related to problems and prospects of primary and secondary market.
- Booklets published by other related agencies like SEBO, ministry of finance, and T.U. Library as the relevant materials.

Analysis of data

Analysis is the careful study of available facts so that one can understand and draw conclusion from them on the basis of established principles and sound logic (Cottle etal: 1988)ⁱ. This study is mostly based on the analysis of secondary data with the help of

different statistical tools. The empirical results have been extracted in this study by using annual data of listed companies from 2050/051 to 2062/063.

3.5 Statistical tools

Statistical tools are used to implicit the comparative results are as follows:

3.5.1 Multiple Bar- diagrams and graphs

Diagrams and graphs are visual aids which give a bird's eye view of a set of numerical data which show the information in a way that enables us to make comparison between two or more than two sets of data. Diagrams are in different types. Out of these various types of diagram one of the most important form of diagrammatic presentation of data is multiple bar diagram which is used in cases where multiple characteristics of the same set of data have to be presented and compared.

3.6.2 Pie- diagram

A pie- diagram is a widely used aid that is generally used for diagrammatic presentation of the values differing widely in magnitude. In this method all the given data are converted into 360 degree as the angel of a circle is 360 degree and all components of the data are presented in terms of angels that total 360 degree for one set of data.

3.6.3 Percentage

Percentage is one of the most useful tools for the comparison of two quantities or variables. Simply, the word percentage means per hundred. In other words, the fraction with 100 as its denominator is known as a percentage and the numerator of this fraction is known as rate of percent.

CHAPTER-IV

DATA PRESENTATION AND ANALYSIS

4.1 Introduction

This chapter includes the presentation and analysis of data. Analysis is based on both primary and secondary data. Various types of data available in the market are used to analyze the primary market its problem and prospects in Nepalese capital market.

The chapter basically focused upon the analysis of collected data from different secondary sources. In this chapter the relevant and the available data/information regarding the primary market have been presented and analyzed.

4.1.1 Issue approved from SEBO

As per the provision of the Securities Exchange Act, 1983 (now 2006) and regulation and guidelines made there under, the issuing company should register the securities in SEBO/N and get issue approval before going to public. After getting approval from SEBO/N 162 companies issued securities from fiscal year 2050/051 to 2062/063. Most of the Commercial bank and finance sector are issued different types of securities to the public. Other remaining sectors are issued securities to the public lowest percentage in comparison to the commercial bank and finance sector. Number of primary issue is increasing day by day. It seems that companies are interested to issue different types of securities for the public. The detail situation of number of issued in different year is presented in Table 4.1.

Table 4.1**Year wise issue approved from SEBO**

Fiscal year	Number of issue	% Number of issue
2 050/051	16	9.88
2 051/052	10	6.17
2 052/053	12	7.41
2 053/054	5	3.09
2 054/055	12	7.41
2 055/056	5	3.09
2 056/057	6	3.70
2 057/058	9	5.56
2 058/059	12	7.41

2 059/060	18	11.11
2 060/061	14	8.64
2 061/062	14	8.64
2 062/063	29	17.90
T otal	162	100.00

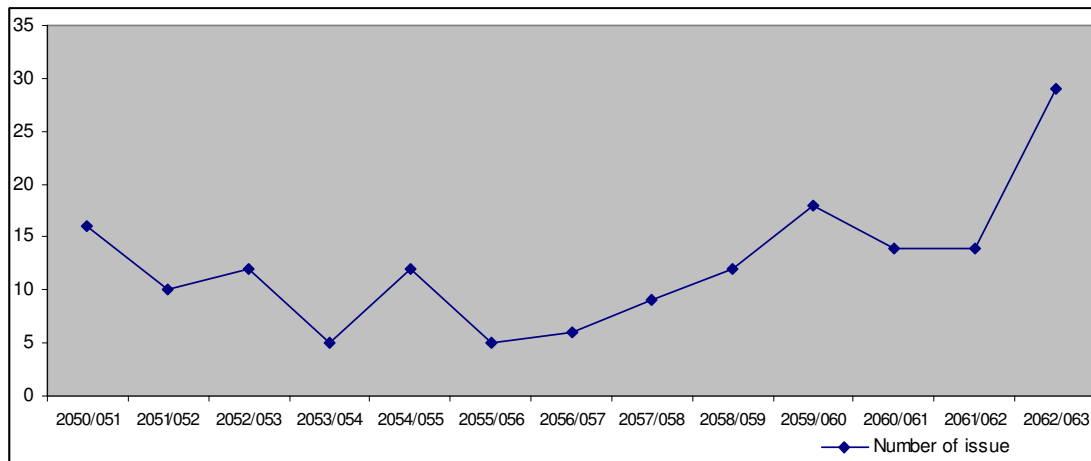
Table-4.1 shows varied number of issue approved by SEBO during the period. Highest numbers of issues were approved in the fiscal year 2062/063, forwarded by fiscal year 2061/062 and 2050/051. Lowest issue approved percentage 3.09 percent and equal in the fiscal year 2053/054 and 2055/056. Over the 13 year of issue approval the number of issue is fluctuating every year. The total number of issue varies at various time periods.

The number of issue was 16 in initial fiscal year 2050/051 but at the end of fiscal year 2062/063 the total number of issue approved was reached to the point of 162 issues. The highest number of issued was 29 (17.90%) in fiscal year 2062/063. The second highest issue was 18 issues (11.11%) in fiscal year 2059/060 number of issue were 16 (9.88%) and it was the third highest issue. In fiscal year 2061/062 and 2060/061

numbered of issue was 14 (8.64%) respectively. Similarly, the least three issued during the period were 5 issues (3.09%), in the fiscal year 2053/054 and 2055/056, 6 issues (3.70%) in the fiscal year 2056/057 and 9 issue (5.56%) in the fiscal year 2057/058 and 12 issues (7.41%) in fiscal year 2052/053 , 2054/055 and 2058/059 respectively.

Figure 4.1

Yearly no of Issue



4.2 Types of securities issued

Primary market is the place where company issues different types of securities to collect the needed fund. During the fiscal year 2050/051 to 2062/063 total amount issued on the basis of different types securities are presented in table 4.2.

Table 4.2

Securities wise issue approved

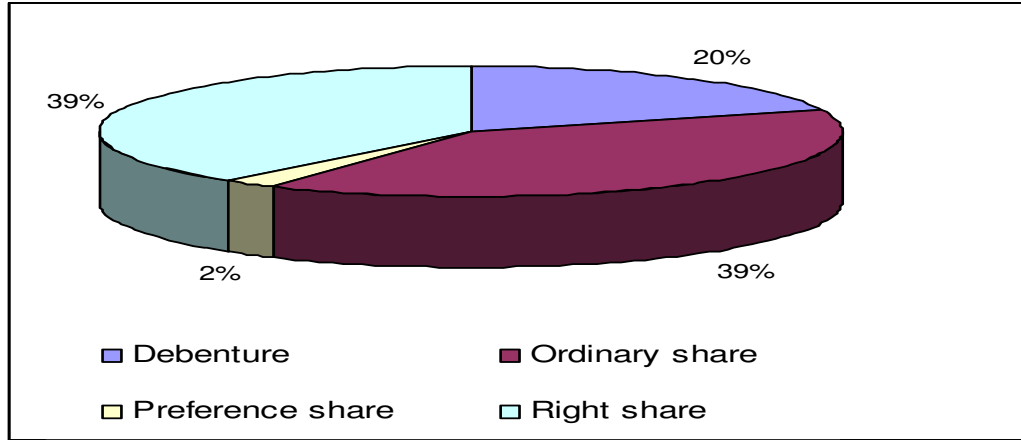
(Rs In Million)

Types of securities	Tot al	% of Total
Debenture	190 3	19.83
Ordinary share	376 0.53	39.18
Preference share	236. 5	2.46
Right share	369 7.45	38.53
Total	959 7.48	100

Above table 4.2 shows securities wise issue approved by SEBO. During the fiscal year 2050/051 to 2062/063 total issued amount is Rs. 9597.48 million. Ordinary share, right share, debenture and preference share are issued Rs. 3760.53, Rs.3697.45, Rs.1903 and Rs. 236.5 respectively. Out of it highest amount issue was ordinary shares which are approximate 40% of the total amount issued. Right share issue is around 39%, and which is the second highest. Debenture and preference share are issued approximately 19% and 2% of total issued amount. It shows that most popular security issued in Nepalese primary market is ordinary share.

Figure 4.2

Securities wise issue approved



4.3 Year wise issued amount

During the fiscal year 2050/051 to 2062/063 total amount issued is Rs.9597.48 million. Amount issued in different year are presented in table 4.3.

Table 4.3
Year wise issued amount

(Rs. in million)

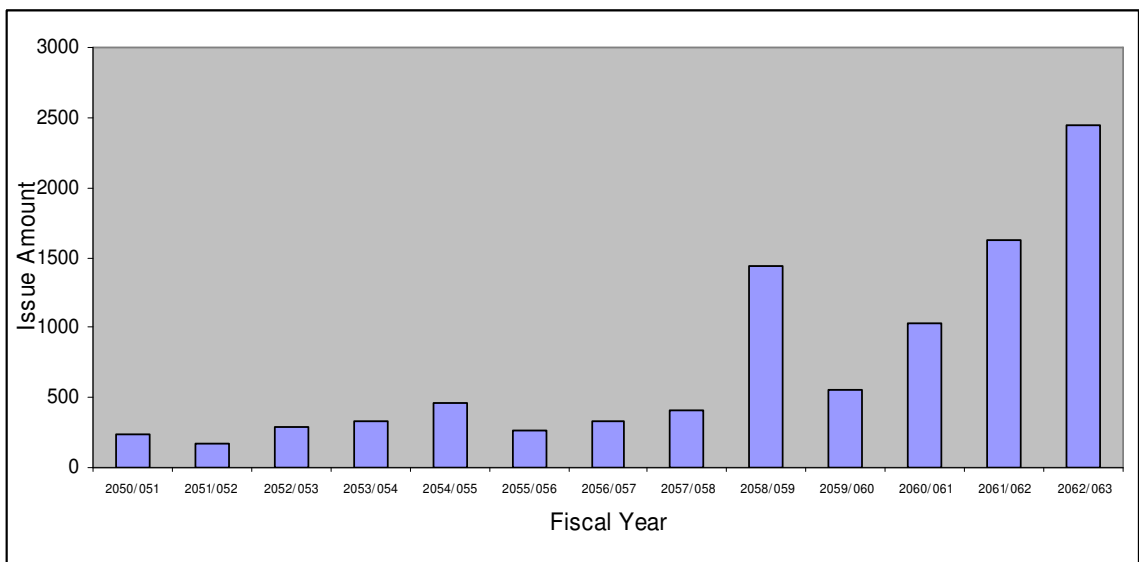
Fiscal Year	Yearly total amount	% of Total
2050	244.4	2
/051	0	.55
2051	173.9	1
/052	6	.81
2052	293.7	3
/053	4	.06

	2053	332.2	3
/054	0		.46
	2054	462.3	4
/055	6		.82
	2055	258.0	2
/056	0		.69
	2056	326.8	3
/057	6		.41
	2057	410.4	4
/058	9		.28
	2058	1441.	1
/059	33		5.02
	2059	556.5	5
/060	4		.80
	2060	1027.	1
/061	50		0.71
	2061	1626.	1
/062	82		6.95
	2062	2443.	2
/063	28		5.46
	Tota	9597.	1
1	48		00.00

Table 4.3 shows that the highest amount issue was Rs. 2443.28 million in fiscal year 2062/063. It is the 25.46 % of the total issued amount. In fiscal year 2061/062 total amount issued is Rs. 1626.82 million which is 16.95% of the total issued amount. Third and fourth highest public issue is Rs.1441.33 and Rs. 1027.50 million in fiscal year 2058/059 and 2060/061 which is 15.02% and 10.71% respectively of the total amount issued. Least amount issue is Rs.173.96 million in the fiscal year 2051/52 which is only 1.81%. Second and third lowest issue is Rs.244.40 and Rs.258.00 million respectively in the fiscal year 2050/051 and 2055/056. Similarly total amount issue is Rs.293.74, Rs. 326.86, Rs.332.20 Rs.410.49 Rs.462.36,and Rs.556.54 million in fiscal year 2052/053, 2056/057, 2053/054, 2057/058, 2054/055 and 2059/060 respectively which represents 3.06%, 3.41%, 3.46%, 4.28%, 4.82% and 5.80% of the total amount issued respectively.

Figure 4.3

Year wise issue amount



4.4 Year Wise Number of issue

Year wise analysis number of securities issued during the period of 2050/051 to 2062/063 varies differently which is presented in below at table 4.4

Table 4.4

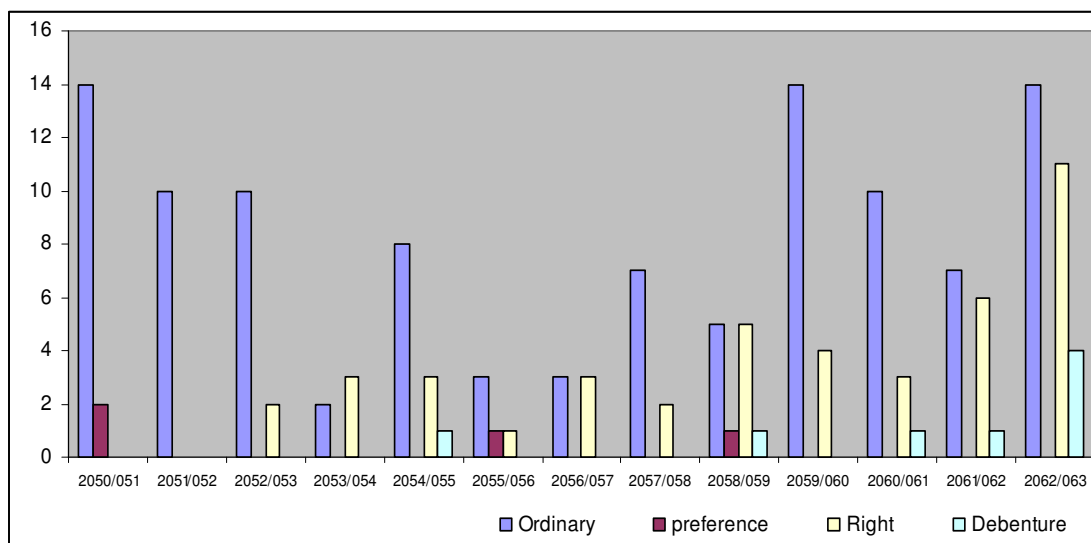
Year wise types of security issue

Fiscal Year	Types of securities & No. of securities			
	Ordinary	preference	Right	Debenture
2050/051	14	2	0	0
2051/052	10	0	0	0
2052/053	10	0	2	0
2053/054	2	0	3	0
2054/055	8	0	3	1
2055/056	3	1	1	0
2056/057	3	0	3	0
2057/058	7	0	2	0
2058/059	5	1	5	1
2059/060	14	0	4	0
2060/061	10	0	3	1
2061/062	7	0	6	1
2062/063	14	0	11	4
Total	107	4	43	8

Table 4.4 shows that the year wise number and types of securities issued in the Nepalese capital market. The number of issue was 162 in total. Among this highest issued security is ordinary share which is 107 in total of 162 issues. Second highest is right issue which are 43 issues in total number of issues. Preference share is the list issues. Only 4 issues are made during the period and eight are debenture issues among the total number issued and which is the second lowest issued number.

Figure 4.4

Number of issue securities year wise



4.5 Over and Under Subscription

When the demand of securities is higher than issued securities, the situation is called the case of oversubscription but if the demand of securities is lower than issued securities that situation is called under subscription.

Over subscription of the share are the great problems in the primary market. At present most of the primary issue being oversubscribed. Almost public issue is done by finance sector and commercial banks sector and this public issue is being over subscription.

Over subscription and under subscription of share issued by different companies are presented in the table 4.5

Table 4.5
Over and Under Subscription of Securities

Year	No. of share issued Co.	Over subscribed Co.		Under Subscribed Co.		Constant	
		No.	%	No.	%	No.	%
2050/051	14	16	100 %	0	0	0	0
2051/052	10	7	70 %	1	10%	2	20 %
2052/053	10	10	50 %	5	50 %	2	0
2053/054	2	2	100 %	0	0	0	0
2054/055	8	5	62.5 %	2	25 %	1	12 %
2055/056	3	2	66.67 %	1	33.33%	0	0
2056/057	3	3	100 %	0	0	0	0

2057/058	7	7	100 %	0	0	0	0
2058/059	5	4	80 %	1	20 %	0	0
2059/060	14	14	100 %	0	0	0	0
2060/061	10	10	100 %	0	0	0	0
2061/062	7	6	85.71 %	1	14.29%	0	0
2062/063	14	14	100%	0	0	0	0
Total	107	93	86.92%	11	10.28%	3	2.80%

Source: Issue managers

Table 4.5 shows that during the period of fiscal year 2050/051 to 2062/063 total companies 107 companies issued their common stock for public subscription and among them common stock issue of 93 companies (86.92 %) have been oversubscribed, common stock issue of 11 companies (10.28 %) have been undersubscribed and remaining 3 companies (2.80 %) issue have been fully subscribed. Furthermore, all those companies who issued their common stock in fiscal year 2050/051, 2053/054, 2056/057, 2057/058, 2059/060, 2060/061 and 2062/63 have been fully oversubscribed i.e. out of the 107 share issuing companies 64 companies (59.81 %) shares have been fully oversubscribed during the period.

Similarly, during the period 14 companies issued their shares for public subscription in year 2050/051, 2059/060 and 2062/063 in high range. And it is followed by 10 companies in year 2051/052, 2052/053, 2060/061 separately while in lowest range only 2 companies issue their common stock for public in year 2053/054 and it is followed by 3 companies in year 2055/056 and 2056/057 respectively.

4.6 Sector wise issue amount

NEPSE has categorized total companies into 8 sectors. The detail of sector wise issue during the period of 2050/051 to 2062/063 situations of the issue of such sectors have been presented in Table-4.6.

Table 4.6

Sector wise issued amount

(Rs. In Million)

Types of sectors	Total amount	% of Total
Commercial bank	5036.99	52.48
Development bank	260.2	2.71
Finance companis	1777.88	18.52
Hotel	796.45	8.30
Insurance	285.2	2.97
Manufacturing	878.38	9.15
Others	535.41	5.58
Trading	26.97	0.28
Total	9597.48	100

During the study period 162 companies have issued different types of securities to the public. The total amount of the issue is Rs. 9597.48 million. Among the issues Commercial bank sector has issued highest portion to the general public. The total issue amount of the Commercial bank is Rs. 5036.99 million which represent 52.48% of the total issue approved. Second highest amount of public issue is finance company and

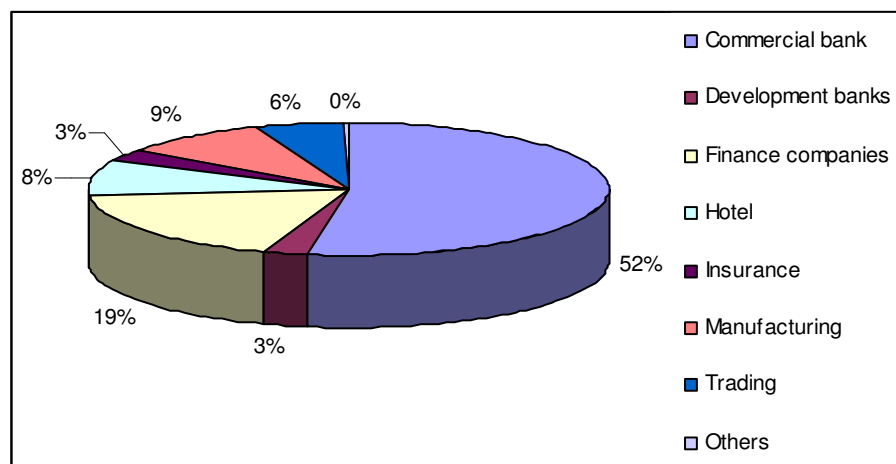
which is Rs. 1777.88 million respectively 18.52% of the total issued amount. Approximately 80% of the secondary market is covered by commercial bank and finance sector.

Similarly, manufacturing sector issued Rs.878.38 million which is 9.15% of the total issued amount. Development bank and other sector issued Rs.260.20 and Rs.535.41 million respectively. These covers 2.71% and 5.58% respectively of the total amount issued.

Similarly, insurance companies are also offered shares to the public. The total amount issued by insurance company is 285.20 million, which covers 2.97% of total amount issued. Hotel and trading sectors issued Rs.796.45 and Rs.26.97 million for the public respectively 8.30% and 0.28% of the total amount issued.

Figure 4.6

Sector wise issued amount



4.7 Sector wise number of over and under subscription

The public response to the sectoral issue during the period of fiscal year 2050/051 to 2062/063, are presented in the table 4.7.

Table 4.7

Sector wise over and under subscribed

Sector	No. of share issued Companies	Over sub-scribed Co.		Under Sub-scribed Co.		Constant	
		No.	%	No.	%	No.	%
Commercial Banks	14	14	100%	0	0	0	0
Finance Companies	50	45	90%	4	8%	1	2%
Insurance Companies	11	11	100%	0	0	0	0
Manufacturing & Processing	17	11	64.71%	4	2.53%	2	11.76%
Hotel	3	3	100%	0	0	0	0
Development Banks	8	7	100%	0	0	0	0
Other	4	3	100%	0	0	0	0
Total	107	95	89.22%	8	7.84%	3	2.94%

Source: Issue managers

Table 4.7 shows that out of 107 companies issued the different types of securities for the public. Among them the highest share issued companies are finance sector (50 companies) and it is followed by the manufacturing and processing sector companies (17 companies) whereas the least share issued companies are of hotel sector and service sector companies.

During the study period of fiscal year 2050/051 to 2062/063 all share issued companies of banking sector, insurance sector, hotel sector, development sector and other sector were fully over- subscribed. Similarly, 90 % of finance sector companies shares were over-subscribed, 8 % companies shares were under- subscribed and rest 2% companies share were constant while in case of manufacturing and processing sector 64.71 % companies share were over- subscribed, 2.53 % companies share were under-subscribed and 11.76 % companies were subscribed as issued.

4.8 Number of issue managed by different issue managers

Number of the total issue in different securities manage by different issue manager are presented in table 4.8.

Table 4.8

Number of issue manage by different issue managers

Issue Manager	Types of securities				Total
	Debt share	Ordinary share	Preference share	Right share	
AFC	3	0	0	6	9
CIT	2	21	1	7	31
CIT & NCML	0	2	0	0	2
CIT & RBB	0	1	0	0	1
NCML	1	36	1	9	47
NCML& NMB	0	1	0	0	1
NCML&NMB	0	1	1	0	2
NCML&NSM	0	1	0	0	1

L					
NEFINSCO	0	5	0	3	8
NFCL	0	4	0	3	7
NMB	2	20	0	8	30
NMB & CIT	0	1	0	0	1
NMB & NCML	0	1	0	0	1
NMB&NCM L	0	1	0	0	1
NSMB	0	0	0	2	2
NSML	0	9	1	5	15
NSML& NSMB	0	1	0	0	1
RBB	0	2	0	0	2
Total	8	107	4	43	162

Source: Issue managers

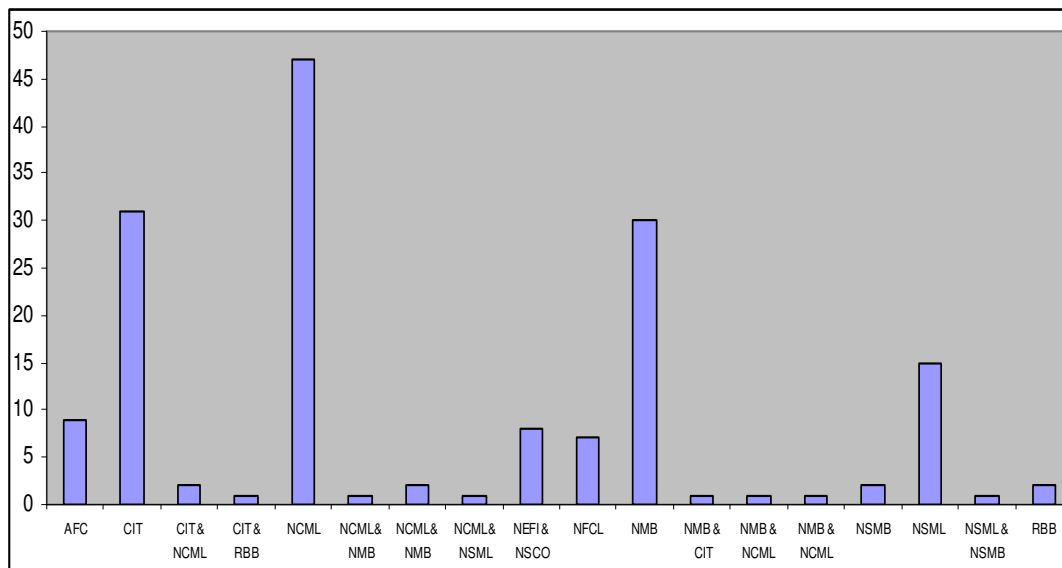
Table 4.8 shows the number of issues securities and their issue manager. Among the 162 issues highest issues are managed by NCML. The company was managed forty seven issues and other issues are jointly managed with NMB and CIT. Second highest issues are managed by CIT. It has managed thirty one issues alone and other are jointly managed with RBB and NMB. Third highest issued securities managed by NMB. It has managed thirty issues alone and other are jointly managed with NCML and CIT. NSML managed fifteen securities out of the total one hundred and sixty two securities which is fourth highest issue managed. It also managed two other securities jointly with NCML and NSMB.

The least issue was managed by RBB and NSMB. Both managed two issues and one issue managed jointly with other issue manager. Second lowest issue was managed by NFCL. It has managed seven issues. AFC managed nine issues out of total issues which is third lowest among the total issues managed by different issue manager.

At present out of them only six Issue Manager are doing issue manage activities. They are AFC, NMB, CIT, NFCL, NCML and NEFINSCO.

Figure 4.8

No of issues manage by each issue manager



Issue manager

4.9 Growth of Primary issue in different years

During the study period numbers of primary issues are increasing in every year. Primary market trend of the past 13 years shows the progress steady and public response

is positive toward this sector. Growth of the primary market is directly related with the lack of opportunities for the investment in other sectors. The liquidity position of our country is also high which would have also led to high public response to the public issue of the different companies. Most of the companies attract the investor by issuing the different types of securities. Companies are also interested to go to the public. Investor's are more attracted for the investment of the primary issue because of the higher return and low risk in comparison to the other investment. So, primary issues are increased in every year in all sectors. Growth of primary issue is almost positive in past history of Nepalese capital market. Growths of primary issues in different year are shown in table 4.9.

Table 4.9

Growth of Primary issue in different years

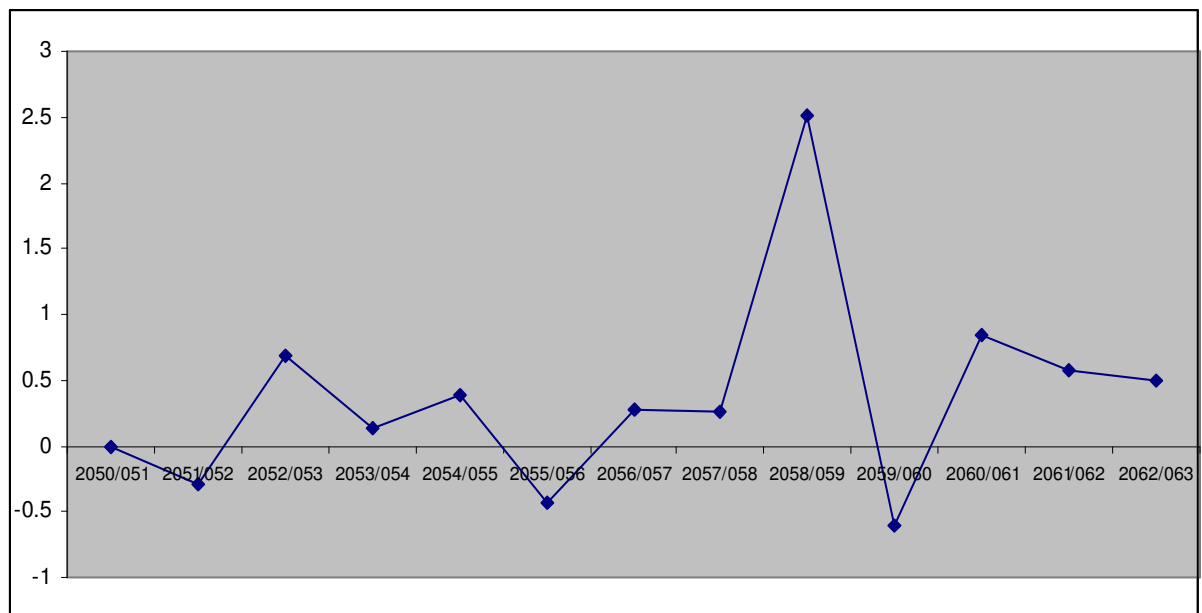
Fiscal Year	Total (Rs. In Million)	% yearly growth
2050/051	244.40	
2051/052	173.96	-29
2052/053	293.74	69
2053/054	332.20	13
2054/055	462.36	39
2055/056	258.00	-44
2056/057	326.86	27
2057/058	410.49	26
2058/059	1441.33	251
2059/060	556.54	-61
2060/061	1027.50	85
2061/062	1626.82	58

2062/063	2443.28	50
	Average growth	40

Above table shows that the growth of primary issue in different years. Highest percentage growth of primary issue securities was 251percentage in the fiscal year 2058/059. Second highest growth of primary issue securities was 85 percentages in the fiscal year 2060/061. Third, fourth and fifth highest percentage growth of primary issue was 69 percentages, 58 percentage and 50 percentage in the fiscal year 2052/053, 2061/062 and 2062/063 respectively. Average percentage growth of primary issue was 40 percentages during the period.

Figure 4.9

Yearly growth in percentage



4.10 Number of issues according to types of securities

There are many securities available in the stock market for the investment. In Nepalese capital market limited types of securities are issue for the public or securities available for the investment are limited. Types of securities issued and their number by different companies in primary market are shown in table 4.10.

Table 4.10

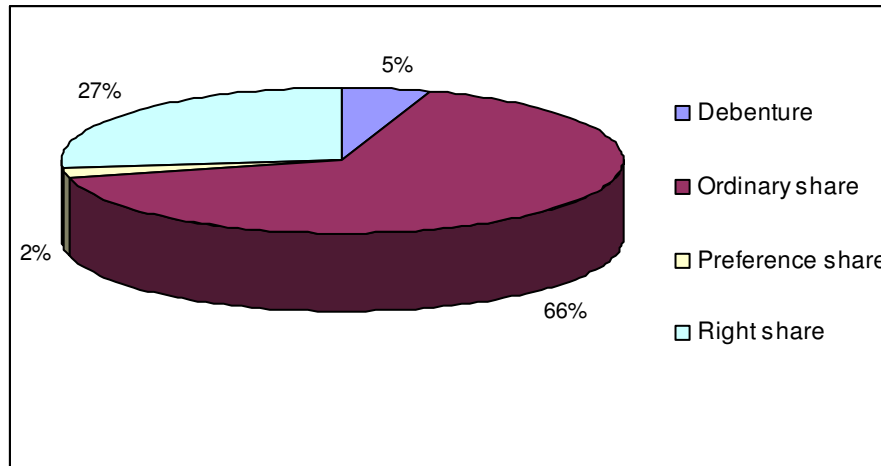
Types of securities and their number of issue

Type of securities	No of securities
Debenture	8
Ordinary share	107
Preference share	4
Right share	43

Table 4.10 shows different types of securities issued in Nepalese capital market. Most of the companies are seen to issue ordinary share. 107 companies issued ordinary share to the public in Nepalese capital market. Right share is another popular security for the companies to collect additional fund. Forty three companies issued right share until the fiscal year 2062/063. Debentures and preference shares are seen very less attractive securities in the Nepalese capital market. Only 8 companies have issued debentures and 4 preference shares. The past experience shows that investors are not very interested to invest in the debenture and preference share. Probably it is because of less return as comprised to common stock and lack of awareness.

Figure 4.10

Number of issues according to type of securities



4.11 Descriptive Analysis.

4.11.1 Analysis of the Response of the Brokers.

The major reasons cited for joining the stock exchange operations are personal interest, educational background, knowledge of share market, earn miner etc. However, no vision was expressed by a single broker, indicates that there is a definite lack of visionary and enthusiastic brokers, who could really develop the new capital market in Nepal. Lack of institutionalization or absence institutional partners are obvious as the stock exchange operators in the market. Similarly, response to expectations from the business of stock exchange business and capability to act as brokers are not very well spell-out. It clearly proves that initial brokers were engaged as another business rather than with some definite knowledge and expectations.

There is a definite need for defining proper criteria to become brokers and markets. It is reported that they were getting clients with their proper service, clients were being gathering through personal contacts and referrals, and no promotion was done about their business.

All brokers reported that initially they get their clients through personal relations. Afterwards clients and institutional recommendations and personal contact are the major sources of getting good intention toward investors, keeping contact with several persons by providing proper information by electronic media to promoting clients. Not a single broker seemed to be satisfied with the stock exchange business as there high overhead expenses due to lack of desirable transaction volume and heavy paper work required in the stock exchange market. It is comment that the government has not given due consideration towards the development of the capital market although it is a new concept in Nepal. There is, however, no mention of possibilities and potentialities of stock exchange than section in Nepal. However, most of the brokers reported that they will continue their business in future too because of their field of interest and potential hope of revival.

All brokers do not know about the forthcoming volume of shares of listed companies in advance in the stock exchange through interaction with other persons like brokers, institutions and concerned persons sometimes market pressure (Demand and supply) also helps to know in advance and helps to carry out transactions are expected. But majority responded that there is no way to know in advance about the volume of business.

4.11.2 Responses regarding stock exchange market Development.

i) About establishment of NEPSE, performance and their Development trend. Majority of brokers accepted the beginning of stock exchange market in Nepal at a right time because it started its operation when the government is pursuing liberal and open market policies. Every broker complained about poor performance of the Stock Exchange Market although, infrastructure setup like having their own building and computerized system could be considered as its achievement but the absence of efficient manpower has hampered the development of an effective administrative mechanism.

ii) Brokers are in the opinion that the present bearish trend of the share market is natural because in the beginning fluctuation in prices and transactions took place on the basis of rumor (ideas). It was not realistic due to lack of proper information and research. Heavy transactions and prices increase without foundation resulted in the market to fall and the bearish trend persisted. But they are optimistic. If the government pays attention and handles it into right track, its future is not dark as some might perceive. At present the volume of business transaction in stock exchange is more than one million per day over the last few months, however it is comparatively lower than the transaction volume of last 2-3 years ago. In the first eight months FY. 2005/06, security Board approved 16 financial institutions to issue ordinary shares and, right shares and debenture worth Rs.837.5 million and Taragons Regency Hotel to issue right shares amounting to Rs.446.5 million. The bullish trend in the stock market is reflected in the NEPSE index, the number of companies listed and the size of market capitalization y-c-y, NEPSE index increased by 59.14 points (21.1%) to 339.79 points in the review time. The number of listed companies in the stock exchange reached 141 in the review period. Commercial banks group dominated the stock market. It may be due to the fact that people started to lose faith in the share market. Brokers opined that there is no proper and authentic information available and tax system is not clear which creates low liquidity in the market. All brokers complained that the government and stock exchange are staying ideal watching the poor performance of capital market, not taking any measures to correct the situation. According to brokers there is no co-ordination among companies. So information is missing it time yet here is not penalty and punishment from the government legal framework is inadequate which is wreaking concerned departments.

iii) The overall business trend of stock exchange show relatively larger transaction of the shares has been providing profits and dividends to the investors. The investors then to have lost faith in the manufacturing and other sectors.

4.11.3 Responses gained from the SEBO about the growth trend and problems of primary market and how could be problems resolved.

- The growths of primary market in Nepal are growing slowly.
- There is still dominance of common stock issue as the practice of issuing different instruments such as debenture and other advanced modern instruments are yet to be popular.
- Accounting and auditing standards and practices should be improved.
- Disclosure and corporate governance practice should be improved.
- Initiatives should be taken to establish and promote C.R Agency.
- Open and Cry trading system hence should be improved and lack of adequate institutional development should be done.
- Trading system should be immediately automated, stock trading service should be available to the investors operating in all the five regions, and institutional capability of the major relating agencies should be strengthened.
- The government should keep stock market development under its priority programmes and efforts should be made to implement the programmes accordingly.

4.11.4 Responses gained from NRB and Others:

- People invest in shares to get higher return than other kinds of investment whereas some people invest in share with speculative motive.
- Stock market is not heading towards the right direction now it is the position of stagnant for the long time.
- The situation can be improved by making conducive (helping) policy strict implementation of policy making clarity in rules and regulations.
- There are some problems in primary issue of shares.
- In transparency in share allocation, company takes longer time to refund the invested amount if the shares are not allocated for them.
- Invested in shares, hoping to get more benefit.

4.11.5 Descriptive view regarding Regulatory Aspects.

- i) Brokers complain Regarding Rules and Regulations. “All brokers agreed that there should be right code of conducting and monitoring for brokers”

operations. It was observed that the prescribed code of conduct is sufficient but it is hardly enforced.

Brokers have complained about existing legal Provisions to operate stock exchange market. They suggested that

- Paper work should be reduced.
- Transfer of ownership should be completed with in seven days after it is sent to the concerned companies.
- Strict rules for information dissemination.
- Should have good share transfer laws.
- Punish inside trading and,
- Require companies to disclose financial information.(Which are hindering the development of stock market in Nepal).Some brokers cited (example) are:
 - i. Explanations of sec.53 of companies act 1997.
 - ii. Keeping Business income and capital gain at per in the income Tax act.
 - iii. Sec.83 of companies act is not comprehensive.
 - iv. More details are required in the annual report.
 - v. Companies act, 1997 is still not comprehensive.

They strongly suggested that the government should try to simplify them gradually and make it flexible depending upon the changing time and situations.

In the context of Primary share issue, there should be strict time frame for allotment of shares, refund of money, distribution of shares certificate and listening of shares. There should be strict punishment if the prospects is misleading and investor is affected by misleading prospectus So there should be a provision of comparing the prospectus with actual situation.

ii) The brokers do not have any problem with each other in share transactions and settlement. But they have experienced conflicts in buying and selling of share, mostly in signature verifications, and cash payment. Investors do not pay when prices fall and do not accept share price when prices rise shouting system is effective because sometime the board maker (person who writes in the board placed

in the wall) may not listen to the first brokers quote and writes another brokers number in the board. It creates conflicts in the floor.

iii) Majority of brokers agreed that certain requirement like minimum qualifications and experiences should be included some added that brokers should be allowed to operate according to volume of transactions.

4.12 Prospects of Nepalese Primary Market

At present, individual Nepalese savers have extremely limited opportunities for investing their long-term savings. To secure maximum returns, these investors should have opportunities to invest into long-term corporate equities rather than depositing on the bank. However, because of the present state of the stock market, both individuals and institutions are putting far more of their saving into bank deposits and fixed interests government securities that they would if the market were working properly. Thus, long-term savings that should be invested in the stock market are going into short-term instruments.

After the adoption of liberal economic policy by Nepal Government, a large number of companies established in the past 13 years. These companies cover a broad range of industries including airlines, hydropower, water supply, gas, pharmaceuticals, paper, food and beverages, cement, iron and steel, textiles, banking, insurance, finance services, hotels and resorts. Though, still there is enough liquidity in the market at present, investors are willing to invest in the common stocks of public companies but the corporate bodies are not coming ahead to collect fund from the primary market through

public issues. They are obtains loan from banking and financial institutions for their long-term capital requirement.

The retail investors are in search for long-term instrument with higher return for their savings. The number of insurance companies is growing and government is planning to establish a pension fund for its employees. Provident fund, pension fund as well as insurance companies would prefer to invest in the equity of profitable companies through IPO rather than depositing on the bank. Entrepreneurs, who are establishing new business in response to liberalizations, will be constrained in realizing their capital gains if they cannot sell part of their original equity in successful company after some years of growth. Thus, there exists opportunities for the investors to invest in the stock of corporate bodies and the corporate bodies have the opportunities of collecting required capital through the issue of stock through primary market. However, there are a lot of things to be done to transform the present state of primary market in to a healthy and efficient one where corporate bodies can easily raise funds according to their requirements and investors can invest their savings into a long-term instrument with higher return.

4.13 Impediment and Future Prospects.

The capital market needs laws that make the procedures for public issue simple, transparent and unambiguous and defines clear roles and responsibilities of regulatory bodies. Lack of such laws is the main hindrance to the development of capital market. Lacks of investor education, lack of professionalism in the part of the companies

involved in securities business and inadequate attention to enhance the institutional capabilities are some of the factors that are also contributing to the impediments to primary stock market development

Although there are many hurdles, the availability of enough liquidity in the market and the government's liberal economic policy, which is encouraging foreign as well as domestic investors to invest in various sectors such as hydropower, telecommunication, and infrastructure projects is certainly going to have high prospects for primary market in Nepal.

4.14 Major findings of the study

The major findings of the study are described as follows

- The total number of issue of the Nepalese capital market is increasing day by day. The number of issues was 16 in the fiscal year 2050/51 but at the end of the fiscal year 2062/63 it has reached 162 issues. The highest numbers of issue is 29 (17.90%) in the fiscal year 2062/63. The second highest issue is 18 issues (11.11%) in the fiscal year 2059/60 and it is the third highest issue.
- In the fiscal year 2060/061 and 2061/062 number of issues were 14 (8.64%) in each year. Similarly, the number of issues during the period were 5 (3.09%), in the fiscal year 2053/054 and 2055/056 each, 6 (3.70%) in the fiscal year 2056/057 , 9 (5.56%) in the fiscal year 2057/058 and 12 (7.41%) in the fiscal year 2052/053 , 2054/055 each and 2058/059 each.

- Total issued amount is Rs. 9597.48 million during the period. Ordinary share, right share, debenture and preference share are issued Rs. 3760.53, Rs.3697.45, Rs.1903 and Rs. 236.5 respectively.

- The highest amount issue is ordinary shares which is approximately 40% of the total issue amount. Right issue is around 39% of total issue amount which is the second highest. Debentures and preferences share are issue approximately 19% and 2% respectively of total issue amount. It shows that most popular and common security issue in Nepalese primary market is ordinary share.

- The highest amount issue of Rs. 2443.28 million in the fiscal year 2062/063. It is the 25.46 % of the total issue amount. In the fiscal year 2061/062 total amount issue is Rs. 1626.82 million which is 16.95% of the total issue amount. Lowest issue amount is Rs.173.96 million in the fiscal year 2051/052 which is 1.81% of the total issue amount. Second and third lowest issues are Rs.244.40 and Rs.258.00 million in the fiscal year 2050/051 and 2055/056.

- Commercial banks have issued highest amount issue as comprised to other sectors. Their issue amount is Rs. 5036.99 million which represent 52.48% of the total issue amount. Finance companies have issued Rs. 1777.88 million i.e. 18.52% of the total issue amount, Manufacturing sector issues Rs. 878.38 million i.e. 9.15% of the total issue amount. Development bank and other sector issues Rs.260.20 and Rs.535.41 million. It covers 2.71% and 5.58% respectively of the

total issue amount. Insurance companies issues Rs. 285.20 million i.e. 2.97% of total amount issue. Hotel and trading sectors issues Rs. 796.45 and Rs. 26.97 million to the public which is 8.30% and 0.28% of the total issue amount.

- Total number of issue securities during the period is 162. Highest issue managed by NCML. It has managed 47 issues and other issue jointly managed with NMB and CIT. CIT has managed 31 issue alone and other jointly with RBB and NMB which is the second highest. NMB has managed 30 issues alone and other issue jointly with NCML and CIT which is the third highest. NSML has managed 15 issue out of the total issue which is four highest issue managed. It also managed 2 issues jointly with NCML and NSMB. The lowest issue managed by RBB and followed by NSMB also. Both managed 2 issues alone and 1 issue managed jointly with other issue manager. Second lowest issue managed by NFCL. It has managed 7 issue securities. AFC has managed 9 issues out of total issue which is third lowest. At present out of them only six issue managers are doing issue manage activities. They are AFC, NMB, CIT, NFCL, NCML and NEFINSCO.
- Highest percentage growth of primary issue is 2.51 times in the fiscal year 2058/059. Second highest growth of primary issue is 85 percentage in the fiscal year 2060/061. Third, fourth and fifth highest percentage growth of primary issue is 69 percentage, 58 percentage and 50 percentage in the fiscal year 2052/053, 2061/062 and 2062/063 respectively. Average percentage growth of primary issue is 40 percentages during the study period.

- Total 107 companies issued different types of securities to the public. Forty three companies issue right until the fiscal year 2062/063. Debenture and preference share are issue very less in the Nepalese capital market. Only eight companies issues debenture and four preference shares to the public.

CHAPTER – V

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

Primary market is one of the important component of capital market. Capital market facilitates the exchange of financial assets by bringing together buyers and sellers of securities. Capital markets provide an effective way of raising money for commercial enterprises and in the meantime provide an investment opportunity for individuals and institutions. Thus, primary markets have both theoretical and practical perspectives. This study mainly aims to examine the primary market's problem and prospectus in Nepalese capital market. The specific objectives of this study are:

- To explore the problem of primary market
- To study the future prospects of the primary market.
- To analyze the pattern of public response to different securities and different sectors.
- To analyze the present situation of Nepalese capital market and its future prospectus.

Although, some studies regarding the different issues of primary market are already conducted in Nepal, the study based on the primary market its problem and prospectus in Nepalese capital market is probably the first in Nepal. This study is based on the secondary data with large sample of primary issue companies from different sectors. This study covers almost all sectors/companies (i.e. banking sector, finance sector, development bank sector, manufacturing and processing sector, hotel sector, insurance sector, trading sector and other sector) issuing securities to the public. For the purpose of this study, the necessary secondary data has been collected since 2050/051 to 2062/063 with respect to annual reports, other bulletin of NEPSE and its website: <http://www.nepalstock.com>, the annual reports of SEBO/N and its website: <http://www.sebonp.com> and the annual reports of specific companies. This study is based on time series data analysis of 162 observations of the sample companies. The time series data are used to trace out the current situation of primary market problem in Nepal. This study used different tools to accomplish its objectives. The multiple bar diagram, pie-chart were used to analyze the picture of primary market condition in Nepal.

5.2 Conclusions

Based on the findings of the study, it is concluded that companies have issued basically four types of securities in Nepalese capital market. (that are ordinary shares, preference shares, mutual fund's shares, debentures and right shares). The total number of issue of the Nepalese capital market is increasing day by day. The number of issues were 16 in the fiscal year 2050/51 but at the end of the fiscal year 2062/63 total number of issued is reached to 162 issues. The highest number of issue are 29 (17.90%) in fiscal year 2062/63. Lowest issues during the period are 5 (3.09%) in the fiscal year 2053/054 and 2055/056 each. Total issue amount is Rs. 9597.48 million during the study period. Ordinary share, right share, debenture and preference share are issues Rs. 3760.53, Rs. 3697.45, Rs. 1903 and Rs. 236.5 respectively.

The highest amount issue is ordinary shares which is approximate 40% of the total issue amount. Right issue is around 39% of total issue amount which is the second highest. Debenture and preference shares are issue approximately 19% and 2% of total issue amount. It shows that most popular and common security issue in Nepalese primary market is ordinary share.

NCML has managed 47 issues and other issues jointly managed with NMB and CIT which is the highest issue managed. CIT has managed 31 issues alone and other issues jointly with RBB and NMB which is the second highest. The lowest issue managed by RBB and followed by NSMB. Both managed 2 issues and 1 issue managed jointly with other issue manager. Second lowest issue managed by NFCL. It managed

seven issues. At present out of them only six issue manager are doing issue managing activities. They are AFC, NMB, CIT, NFCL, NCML and NEFINSCO

The total amount issue by during the study period is Rs. 9597.48 million. Commercial banks issues Rs. 5036.99 million which is the 52.48 percentage of the total issue amount. Finance companies issues Rs. 1777.88 million i.e. 18.52 percentage of the total issue amount. Manufacturing sector issues Rs.878.38 million i.e. 9.15 percentage of the total issue amount. Development banks and other sector issues are Rs.260.20 and Rs.535.41 million. It covers 2.71 percentage and 5.58percentage of the total issue amount. Insurance companies issue is Rs. 285.20 million i.e. 2.97 percentage of total issue amount. Hotel and trading sectors issue are Rs. 796.45 and Rs. 26.97 million to the public which is the 8.30 percentage and 0.28 percentage of the total issue amount.

The highest amount issue of Rs. 2443.28 million in the fiscal year 2062/063. It is the 25.46 percentage of the total issue amount. Lowest amount issue is Rs.173.96 million in the fiscal year 2051/052 which is 1.81 percentage of the total amount issue. Highest percentage growth of primary issues is 2.51 times in the fiscal year 2058/059. Average percentage growth of primary issue is 40 percentage during the study period.

Likewise, the situation of sector-wise issue also indicate that all share issued of banking sector, insurance sector, hotel sector, development sector and other sector are fully over-subscribed while in case of finance sector and manufacturing and processing sector companies majority of such issues were also over-subscribed by many times.

These all indicate the problem and prospectus of primary market in Nepalese capital market.

5.3 Recommendations

To develop and expand the Nepalese primary market more effective and efficient the following recommendations have been recommended:

- The government should make clear and specific plans and policies to expand the capital market and should implement these.
- The Securities Board Nepal and other concerned authorities should conduct public awareness and investors education programs to increase the level of investors' awareness.
- Large and ineffective government corporations should be privatized in order to develop the Nepalese stock market through the wide spread distribution of shares to public investors.
- The information and financial statements of the companies should be disseminated properly and timely.
- The market intermediaries should be educated, trained and professionalized.

- The government should allow foreign investors to invest in Nepalese Capital Market.
 - Independent rating agencies should be encouraged to establish so that the potential investors will have a confident picture of the financial health and future prospects of organizations/Instruments.
 - Encourage active participation of other sectors of the economy besides banks, finance companies and insurance through the enforcement of good corporate governance. Investment in corporate sectors should be encouraged
 - Encourage to the issue of debenture, preference share and other instruments to the public because most of the companies issues common stock for the public.
 - A professional independent analysis on the latest security offers in the capital market should be encouraged. Economic journalism is encouraged to come forward to fulfill their responsibility to the society and the expectation of the investor which help to take investment decision.
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