

PRACTICE OF MERCHANT BANKING IN NEPAL

(A study of NIDC Capital Markets Ltd, Citizen Investment Trust and Nepal Merchant Bank and Finance Ltd and Elite Merchant Bank Ltd.)

A THESIS

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(A study of NIDC Capital Markets Ltd, Citizen Investment Trust and Nepal Merchant Bank and Finance Ltd and Elite Merchant Bank Ltd.)

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ABBREVIATIONS

A.D.	Anno Domini
Amt.	Amount
B.S.	Bikram Sambat
C/D Ratio	Credit/Deposit Ratio
CAR	Capital Adequacy Rate
CBS	Central Bureau of Statistics
CIB	Credit Information Bureau
CIT	Citizen Investment Trust
Co.	Company
etc.	Etcetera
FY	Fiscal Year
GDP	Gross Domestic Product
i.e.	That is
IMF	International Monetary Fund
IT	Information Technology
Ktm.	Kathmandu
LC	Letter of Credit
Ltd.	Limited
Nabil	Nepal Arab Bank Limited
NBL	Nepal Bank Limited
NCC	Nepal Commerce Campus
NEPSE	Nepal Stock Exchange
NGOs	Non Government Organization
NMB	Nepal Merchant Bank
NIDC	Nepal Industrial Development Corporation
NRB	Nepal Rastra Bank
RBB	Rastriya Banijya Bank
Rs.	Rupees
S.D.	Standard deviation
SAARC	South Asian Association for Regional Cooperation
TU	Tribhuvan University
US	United States of America

CHAPTER I

INTRODUCTION

Background of the Study

Developed economy demands developed financial sector. Therefore, the development of national economy depends upon the sound development of financial sector of the country. Financial sector includes various financial institutions whose major activities are to deal on financial transactions. It can be grouped as Commercial Banks, Development Banks, Finance Companies, Insurance Companies, Investment Companies, Co-operatives, Employees Provident Fund and Non-government Organizations. Capital formation and its incessant flow is the crux in the process of economic development. Moreover, a well-organized sound financial system is another forte. A sound financial system consists of different financial intermediaries as well as the market itself, which is the platform to mobilize the fund to its demanders. It gathers scattered financial resources from the surplus sector to dispel the financial dearth of the fund demanders. In this way, the effective financial system creates a nexus between the demander and supplier of the fund.

Financial market is the place where the negotiations of the financial assets and liabilities take place. It conducts two important functions. Firstly, financial market provides an effective way of raising fund for commercial enterprises as well it provides investment opportunities for individuals and institutions on various financial assets. Indeed it provides value and significance to the financial assets. Secondly, financial markets establish a price mechanism for financial assets and based on this price mechanism investors allocate their savings to investment. Commercial enterprises requires adequate fund with optimum capital structure for their smooth functioning and promoting efficiency, thus they issue various kind of marketable securities flanked by the investment in the securities of these enterprise by the deserving investors to utilize their fund by sacrificing their current consumption with the expectation of commensurate return in future. This process of collection and utilization of funds take place in financial market.

Financial institutions in the wake of financial markets provides borrower with access to capital and liquidity to investors. Based on life span of securities, financial market can be classified into Money Market and Capital Market. Money market is a market where the transactions of short term and highly liquid debt securities takes place which have life span of one year or less then that. Unlike money market, capital market refers to that market where the transactions of long-term debt and corporate securities take place. “Capital market is further divided into two categories – securities market and non-securities market. Securities market refers to that market where financial assets such as share, debentures, bonds etc. are traded in accordance with prescribed rules and regulation. Securities market is also divisible into primary and secondary market. The primary market facilitates to raise funds from the market for first time and is often known as ‘new issue market’. Secondary market, which is popularly known as ‘stock exchange’ is concerned with the trading of already issued securities. And non-securities market represents the market where financial transactions are carried out between lender and borrower for a longer period without issuing and securities in the form of shares, debentures in the market.”
(Shrestha, 2000; 1)

According to Peter S. Rose “The capital market is designed to finance long-term investments; financial instruments traded in the capital market have original maturates of more than one year.”

The efficient functioning of a financial market requires a number of financial institutions. One of these institutions is an investment-banking firm, which is the traditional term of merchant banking. The firm acts as a middleman in the distribution of new securities to the public and creates a primary market. They buy the securities from the issuing company and sell them to deserving investors. This process of issuing securities to the public is called underwriting and in this sense, the investment bank is also called an underwriter. Under merchant banking, the investment banker performs various functions besides underwriting. Some of the major functions are- Issue management, Corporate counseling, Project planning, Portfolio management, Underwriting and Bridge Loan financing, Lease financing, finance Venture capital, Factoring, Merger and Acquisition services etc.

Conceptually, “Merchant Banking” refers to an activity that includes corporate finance activities such as advice on complex financings, merger and acquisition advice both international and domestic, and at times direct equity investment in corporations by the financial institutions. Similarly, Merchant Banks are banks that specialize in activities that facilitate trade and commerce. This typically involves international finance (because of their size and complexity), long-term loans to company and underwriting. Merchant banks do not offer usual banking services to the general public.

Merchant banks first arose in the Italian states in the middle Ages when Italian merchant houses—generally small, family-owned import-export and commodity trading businesses—began to use their excess capital to finance foreign trade in return for a share of the profits. This trade generally consisted of lengthy sea voyages. Thus, the investments were very high risk: war, bad weather, and piracy were constant threats, and by their nature the voyages were long-term and illiquid. Later, the center for merchant banking shifted from the Italian states to Amsterdam and then, in the eighteenth century, to London, where immigrants from Prussia, France, Ireland, Russia, and the Italian states formed the core of early British merchant banking. Like the Italian and Dutch houses before them, these British houses were generally small, family-owned partnerships, and most of them continued both to trade for their own businesses and to finance the trading by others. By the end of the eighteenth century, however, the British merchant houses had increased in size and sophistication and began specializing in trade, marketing, or finance. As the nineteenth century opened, virtually no mercantile houses remained focused on both trade and finance.

The role of merchant banking played by the financial institutions have made prominent contribution for mobilizing fund to different financial instruments assuring promising returns from investment to the investors. It has facilitated to meet the tremendous demand for fund in the economy. Establishment, expansion, modernization and diversification of the corporate enterprises have been possible only because of the practice of merchant banking by the financial institutions. Merchant banking includes various functions from corporate counseling to underwriting of securities. Government and its regulatory bodies impose statutory obligations and mandatory provisions time to time upon the corporate sectors and the merchant bankers with their multiple services assist the corporate sector to comply with all those incumbent obligations and provisions. Overall, merchant banking practice though incorporated with in some boundary has been procuring vital support and assistance to corporate sectors for financing their projects whether it is through corporate counseling or underwriting services. It is imperative for the skittishness of the economy.

Thus the development of merchant banking service is crucial for the growth of capital market. The development of merchant banking services is closely linked with worldwide move towards open and market oriented economic system. “With the development of liberalized and market oriented economy the banking and financial system is also expanding gradually, resulting with the introduction innovative financial services and instruments. As result, the financial system has been experiencing and there is though competition among the players of the financial system. Thus, “Merchant Banking activities” include all activities where merchant banker provides services for those institutions or individuals who need information on trading, industrial and other professional activities such as information of different financial resources, required procedure to achieve these resources or any other required managerial work for such activities.” **(Aryal, 2060; 63)**

History of Merchant Banking

“The term ‘Merchant Banking’ stem from leading merchants of early 1800’s ,whether trading in grain, paper or steel, which transitioned from merchandising to banking when they had built up a sufficient reputation for soundness, reliability and wealth to warrant their colleagues’ trust. The profits from banking the commodities of the day were greater and the risks were lower. Early examples of merchant banking often involved international trade between the United States and Europe due to the sheer period of time required to contract, ship and receive goods. Financing trade gave merchant banks the opportunity to deal the commodities on their own account. Merchant banking and its dealing in commodities is distinct from investment banking dealing in securities. The merchant banker’s role evolved in the 1920’s when leading firm became heavily involved in advising as well as financing their clients. **(Kathleen, 1989: 5)**

Merchant banking came into scene in USA in the early 19th century after the introduction of Blue sky Laws to protect investors from fraudulent promoters and security salesmen. In India though merchant –banking activities originated before its independence they got systematized form only after restoration of independence. As a result of recommendations of Banking Commission in 1972, that Indian banks should start merchant banking services as part of their multiple services they could offer their clients, State Bank of India started the Merchant Banking Division in 1972.

In the context of Nepal though Merchant banking exist from the establishment of Nepal Bank Limited in 1990 B.S, its existence was in a crude form. After the restoration of democracy in 2046 B.S. and an announcement of government’s economic liberalization policy, private sector investors are attracted to invest in different organized commercial ventures. As a result numerous new private and public limited companies were established in a very short span of time to reap the benefit of economic liberalization policy of the nation. The development activity through the country had created excess demand for the sources of funds by the ever-expanding industry and trade, which could not be met all by the local banks and financial institutions. In these circumstances, the corporate sector enterprises had the only alternative to avail themselves of the capital market services for meeting long-term fund requirements through issue of shares and market services for meeting long-term fund requirements through issue of shares and debentures. The growing demand for funds from capital market has enthused many organizations to enter into the field of merchant banking for managing the public issues.

The Finance Company Act 2042 gave birth to a new dimension to the merchant Banking Services as the act permits finance companies to sell and purchase the bonds issued by His Majesty’s Government or

securities issued by other companies or institutions, to underwrite them and to form syndicate for such purpose or to participate in such syndicates and to act as broker under the Securities Exchange Act, 1983. Similarly section 3(g) of the same act permits them to perform functions of merchant banking with prior approval of NRB.

Citizen Investment Trust (CIT) is a pioneer merchant banker of the country followed by other finance companies viz. NIDC Capital Market, national Finance Co., Nepal share Market etc. At present few financial institutions (basically finance companies) are involved in different merchant banking activities. However all the financial institutions carry out their merchant banking activities only as a subsidiary to their financing activities. Presently **Elite capital limited** has started its merchant banking activities in non fund basis. Unlike other companies it does not carryout financing activities. Securities Board's recent announcement for merchant banking should be separated from the other financing activities has forced other institutions carrying out merchant banking activities to carry out the merchant banking activities separately. This is expected to increase the merchant banking services provided by Merchant bankers to increase in Nepal

Focus of the Study

Merchant banking includes various kinds of services provided by the merchant bank such as corporate counseling, underwriting of securities, project planning, portfolio management, issue management, factoring, financing venture capital etc. Overall it stands for providing various services relating to capital market and finance to corporate sector.

Thus this research is focused on the activities of the financial institution that are entangled in merchant banking. Basically it is concerned with those financial institutions that conduct the merchant banking activities.

In Nepal, there are limited financial institutions that perform merchant banking, still these institutions; even merchant banks do not perform the merchant banking as their major functions. They are also performing other financial activities as their major function relinquishing the merchant banking function only as a part of their subsidiary function. Therefore, this research will be not be concerned with other activities. It will be focused only in merchant banking activities performed by those financial institutions. It will study and analyze practices and performance of the merchant banks with respect to merchants banking services. Similarly, it seeks about the problems of merchant bankers and tries to assess the panacea for the same, which have compelled them to divert their activities on other financial activities too.

Statement of the Problem

Development of the financial system is imperative for affluent economy. Thus sound financial system is the demand for developed economy. Capital market and money market in the wake of financial market is crucial to strengthen the financial system. And the strength of the capital market is highly dependent upon developed merchant banking system. Thus merchant bank plays a vital role in the economic development of the country.

In Nepal, the emergence of merchant banking can be linked with the development of the financial market and development of the financial market is linked with the establishment of Commercial Banks and Long Term Financing Institution like Nepal Industrial Development Corporation (NIDC), market capitalization started in 1994 B.S with the company act in 1992 B.S. The act of raising funds by issuing shares to the general public in Nepal started in 1973. A.D. At the moment Nepal is experiencing diversification in financial sector. Liberalization, privatization, membership with World Trade Organization (WTO) are the benchmarks of the diversified national economy. Numerous financial institutions have been established. As per the annual report of Securities Board of Nepal (SEBO) 2005/2006, 14 Commercial banks, 7 Development banks, 44 Finance companies, 14 Insurance companies, 8 Trading companies, 3 Hotels, 29 Manufacturing and Processing company are listed in Nepal Stock Exchange. Apparently it depicts the emerging glimpse of financial sector of the country and with the growth of this sector, merchant banking has also flourished. Nevertheless, Nepal is still lacking specific rules, regulations, regarding merchant banking. Commercial bank act, Finance company act, Act for NIDC (Nepal Industrial Development Corporation), CIT (Citizen Investment Trust) and other acts are the basic guidelines for undertaking merchant activities. However, it doesn't clearly address the definition of merchant banking. Thus, many corporate are still unaware on services provided by the merchant banks and difference between commercial banking and merchant banking. NIDC is the pioneer to render the merchant banking services in Nepal, however later it has diversified its services on other financial activities for its sustainable growth and survival. It apparently portrays the financial position of the country.

Merchant banking, though ahead of its infancy, is still in lethargic state in Nepal, despite its keen importance in the economy, it seems to be apathetic for government as well as corporate sector. Moreover, the financial institutions that render merchant services are limited basically to Underwriting, Issue Management, Bankers to the Issue and Leasing. Thus, merchant banking in Nepal has become synonymous to issue management and underwriting, though globally this word is understood as everything related to financial services.

Recently there has been a very positive step towards the development of merchant banking with the establishment of Elite capital limited. Elite Capital was incorporated in 2008 as a first specialized merchant bank in Nepal & has commenced its operation from the August 2008. The company provides various services to individuals & corporation for their resources management. The company has three business lines; issue manager, the registrar of shares and the consultancy services. The registrar of shares divides various companies listed in the Nepal Stock exchange Limited, the issue management division manages the initial part of corporate and the consultancy division provides the consultancy services for financial planning, asset management etc.

The company is committed to provide various services relating to the securities market to its customer. The Company provides awareness information to the general investors in the securities market. The company has set out the objective of client specific products and services that would be helpful to them in their path to prosperity.

The recent announcement of NRB to operate merchant banking activities separately by the companies carrying it as a subsidiary business has also expected to make positive development in the progress of merchant banking activities in Nepal as the companies will be forced to open various activities for their sustainability.

Objective of the Study

The main objective of the study is to analyze and evaluate the practices of the merchant banking undertaken by the merchant bankers of Nepal.

The specific objectives of the study are as follows:

- To evaluate and analyze the performance of merchant bankers in Nepal.
- To disclose the significance of merchant banking towards the development of securities industries in Nepal.
- To study and analyze the growth of merchant banking in Nepal.
- To assess the problems and prospects of merchant banking in Nepal
- To provide suggestions on the basis of major findings.

Significance of the Study

Merchant Banking is an unexplored field in Nepal. There is hardly very rare availability of research work, journal and articles on “Merchant Banking in Nepal”. In this context present study will serve as a source of literature in the field of merchant banking. The study attempts to fill a serious gap in this important area of capital structure practice with focus on merchant banking Services. The research would be helpful to the regulatory authorities like Securities Exchange board of Nepal, Nepal Rastra Bank and others.

It would also be of interest to development banks, commercial banks, financial companies, merchant banks etc. It may help the professionals in the industry to have better understanding on the impact of merchant

banking activities in the securities industry and also it may help the academicians and the researchers who study in these areas.

1.7 Limitations of the Study

This study is conducted for the partial fulfillment for Master's of Business Studies. The study is done bounded within certain limitations and constraints, which are as follows:

This study is only concerned with merchant banking practices of financial institutions of Nepal.

Though there are many financial institutions in Nepal, the study is focused only on the merchant banking activities of those financial institutions that are the leading merchant bankers.

The study is based on primary as well as secondary data. Any intentional default and reporting errors that may occur while obtaining the data will not affect the proposed study.

Research is based on reports provided by listed financial institutions and responses made through questionnaires and their reliability cannot be measured.

The daily, weekly, quarterly, monthly and yearly data is used as per their availability and the need of the study.

The study is conducted within limited period.

1.8 Organization of the Study

The study has been divided into five different chapters, viz. Introduction. Review of literature Research Methodology, Presentation and Analysis, Summary conclusion and Recommendation.

Chapter I: Introduction

The first introduction chapter deals with the introductory framework of the study. This includes background, statement of problem, objectives of the study, significance of the study, limitation of the study and organization of the study itself.

Chapter II: Review of Literature

This chapter includes the review of literature available and review of related theoretical background of the relevant field of study, which aims at forming a conceptual framework to the objective mentioned previously.

Chapter III: Research Methodology

Third chapter explains the research methodology used for the purpose of the study, which includes research design, sources of data, data gathering procedure, population and sample size of the study, data processing procedure and financial as well as statistical tools used for the analysis of data.

Chapter IV: Presentation and Analysis of Data

The fourth, which is the important chapter of the study, will include data classification analysis, and interpretation regarding the primary as well as secondary data.

Chapter V: Summary, Conclusion and Recommendation

The final and last chapter contains findings in aggregate, conclusions drawn through the findings, and the probable suggestions and solutions as 'recommendations' enlightened through the study.

CHAPTER II

REVIEW OF LITERATURE

Review of Literature is one of the important parts of the thesis. This study has been effectively conducted through study of various old thesis, dissertation, newspaper, Magazine and suggestion of the experts of related field. The basic concern of the study is to focus on the merchant banking activities in Nepal theoretical aspects of merchant banking activities are explored in this chapter through review of related materials. This chapter reviews some basic academic course books, journals articles and other related studies. Unfortunately, so far none of the researchers have performed research in this topic in Nepal. However, efforts have been made to gather information from all available arenas as possible.

2.1 Conceptual Review

2.1.1 Meaning of Merchant Banking

Merchant banking is a service banking concerned with providing non-fund based services of arranging funds rather than providing them. The merchant bank merely acts as an intermediary whose main job is to transfer capital from those who own it to those who need it. With the increase in the complexities and requirements of modern business, the role of merchant banker has undergone a substantial change. The merchant banker now acts as an institution which understands the requirements of the entrepreneur promoters on the one hand and financial institutions, banks, stock-exchanges and money markets on the other.

Although not defined in U.S federal banking and securities laws, today the term “merchant banking” is generally understood to mean “negotiated private equity investment by financial institutions in the

unregistered securities of either privately or publicly held companies”. Other investment banking services like raising capital from outside sources, advising on mergers and acquisition, and providing bridge loans while bond financing is being raised in a leveraged buyout-are also typically offered by financial institutions engaged in merchant banking. *(Craig, 1995; 24)*

Merchant banking in India starts with management of public issues and loan syndication and has been slowly and gradually covering activities like project counseling, portfolio management, investment counseling and mergers and amalgamation of corporate firms. Although, merchant banking organizations present a long list of services they contemplate to render their clients but the main services as far being rendered by them are those as authorized by the Securities & Exchange board of India under categories I, II, III and IV. A “merchant banker” has been defined under the Securities Exchange board of India (Merchant Bankers) Rules, 1992 as “any a person who is engaged in the business of issue management either by making arrangements regarding selling, buying or subscribing to securities as manger, consultant, advisor or rendering corporate advisory service in relation to such issue management.

“Merchant banking stands for providing various services relation to capital market and finance to corporate sector. This includes not only the activities for the above purpose in the country but at times arranging funds from outside the country. The merchant banker also provide consultancy to the corporate sector on the issues like finance, capital structure and investment, mergers, takeover and amalgamations, establishing coordination between the government and corporate sector. In fact the merchant bankers should be able to provide guidance to an entrepreneur on all matters from the stage of conception of a project in his mind till it goes into commercial production. A good merchant banker would be considered to be one who is expert, honest, have integrity and

capacity to develop public relations. Whenever a business concern needs funds from the capital market it would usually approach the Merchant banker rather than banks or financial institutions.” **(Toor, 2000: 1.30)**

“Investment bankers, also called merchant banks, purchase newly issued stocks and bonds from corporations and government. They then resell the securities to investor in small quantities. An investment bank makes a profit by selling securities at a higher price than it pays for them. The first merchant banks were formed by British merchants in 1800’s. From the 1930’s to the 1980’s, the U.S. government prohibited any institution that from engaging in investment Banking. Since then, however, government has that from engaging in investment Banking. Since then, however, government has permitted large commercial banks to buy and sell securities within limits.” **(World Book Millennium, 2000:21)**

“Investment banks provide long-term finance to industry. They are sometimes described as industrial banks or private banks. In French speaking countries, people use the term ‘Banques d’ affaires’. Most investment banks do not accept deposits from the general public, but deal with limited number of clients, and on their own capital and reserves, to finance their lending to industry. Investment banks provide long term finance to borrowers in two main ways. First, they grant long-term credit to companies usually for eight to ten years. In the second, they acquire a part of the share capital of companies. Many companies sell their shares through investment banks, and the banks sometimes retain some of the shares. Investment banks provide several important extra services for their customers. They act as economic and financial advisers. If customers intend to undertake new industrial ventures, the banks may give technical advice.” **(The World book Encyclopedia)**

“Investment bankers market new stock and bond offering to individual and institutional investors around the world.” **(Edmister, 199: 1988)**

“Most of the banks have now opened up “Merchant Banking” or “Management department which specialize in domestic corporate financing and associated business such as underwriting of capital, issues, acting as managers to new issues and evaluation of customers existing and proposed new business. These services are of a fairly wide of customers existing and proposed new business. These services are of a fairly wide range, which extend to examination of proposals for mergers and amalgamations of companies and arrangements of loans or short-term finance. The banks also, because of their international connections, assist in arranging foreign exchange element required by industries for their projects and loans with banks and other institutions outside India.”

(Tannan, 199: 581)

2.1.2 Functional Nature of Merchant Banking

In olden times, merchant banks were also known as “Accepting and issuing houses” in the U.K. and “Investment bank” (IB) in the USA. Except for this distinction in nomenclature, there is no essential functional difference between them. Usually, they handled coastal trade and master’s goods on a commission basis and financed risky venture projects, for which they charged heavy interest. They often incurred heavy losses. They accepted bills for payment. These were in addition to their merchant banking functions of commercial banking till 1932 A.D. Later, the Glass Steagall Act, 1933 A.D distinguished the functions of merchant banking / investment banks from commercial banking. But in 2000 A.D, the Clinton administration allowed investment banks to run the functions of commercial banks in addition to their usual functions of investment banking. This was affected through an amendment in the Glass Steagall Act., venture capital, and public deposits.

Merchant banking is a skill-based activity and involves servicing every financial need of the client. It requires a focused skill base to provide for

the requirements of a client. SEBI has made the quality of manpower as one of the criteria for renewal of merchant banking registration. These skills should not be concentrated in issue management and underwriting alone, which may have an adverse impact on business as witnessed in 1995. Merchant bankers can turn to any of the activities mentioned above, depending on resources, such as capital, foreign tie-ups for overseas activities and skills. They can provide the entire gamut of services or develop niche business. The depth and sophistication in merchant banking business are improving since the avenues for raising funds are widening and demand for funds is increasing.” ***(Marchiraju, 2001:212)***

2.1.3 Difference between Merchant Banks & Commercial Banks

The basic difference between merchant banking and commercial banking is that the merchant bank offers mainly financial advice and services for a fee and collects through the non-cash mode of finance i.e. security papers while commercial banks accept deposits and lend money in the mode of cash. Moreover, the merchant bank offers portfolio services to its customers (individual and corporate) while the commercial banks provide retail trade banking services to its customers. Merchant Banking Organizations

2.1.4 Categories of Merchant Bankers

Merchant bankers are classified into four categories having regard to their nature and range of activities and their responsibilities to SEBI, investors and issuers of securities. The minimum net worth and initial authorization fee depend on the category. The first category consists of merchant bankers who carry on any activity of issue management which will inter alia consist of preparation of prospectus and other information relating to the issue, determining financial structure, tie-up of financiers and final allotment and refund of the subscription and to act in the

capacity of managers, advisor or consultant to an issue, portfolio manager and underwriter. The second category consists of those authorized to act as underwriter, advisor or consultant to an issue. The fourth categories consist of merchant bankers who act as advisor or consultant to an issue. Since September 5, 1997 only Category 1 exists.

Net worth:

Minimum net worth for first category is Rs. 5 crores, second category Rs. 50 lakhs, third category Rs. 20 lakhs and fourth category nil.

Registration Fee:

Registration fee for first category is Rs. 2.5 lakhs annually in the first two years, Rs. 1 lakh in third year, second category Rs. 1.5 lakhs annually for first two years and Rs. 50,000 in third year, third category Rs. 1 lakh annually for the first two years and in third year Rs. 25,000; and fourth category Rs. 5,000 annually for first two years and Rs. 1,000 in third year.

Renewal Fee:

Category 1, Rs 1 lakh to be paid annually in first two years and thereafter Rs. 20,000; Category 2 Rs. 75,000 for first two years and Rs. 10,000 from third year, and Category 3 Rs. 50,000 for first two years and Rs. 5,000 third year, and Category 4 Rs. 5,000 annually first two years and Rs. 25000 from third year.

Number of Lead Managers:

The number of lead managers depends on the size of the public issue. The guidelines stipulate that for an issue upto Rs. 50 crores, the number of three, for issues between Rs. 100-200 crores, four, for issues above Rs.

2000 crores but less than Rs. 400 crores, five, and for issues above Rs. 400 crores, five or as may be agreed by SEBI.

2.1.5 Services rendered by Merchant Banker (MB)

The working of merchant banking agencies and units formed subsequently to offer merchant banking services has shown that merchant banks are rendering diverse services, and functions, such as organizing and extending finance for investment in projects, assistance in financial management, acceptance house business, financing of local authorities, financing export of capital goods, hydro-power installation, equipment leasing, mergers and takeovers, valuation of assets, investment management and promotion of investment trusts. Not all merchant banks offer all these services. Different merchant bankers specialize in different services. Merchant banking may cover a wide range of financial activities and in the process include a number of different financial institutions. Generally the services of a merchant banker can be summarized as follows:

- a. Corporate Counseling:** Corporate counseling function is the counsel services given to corporate clients to ensure better corporate performance. The merchant banker has to find out the problems of enterprises and suggest ways and means to solve the problems in achieving organization effectiveness. It suggests suitable locations, technical consultancy, and collaboration etc to the investor.
- b. Project Planning:** The preparation of feasibility report covering market aspect of the product, technical, financial and economic aspects of the enterprise. Project report specifies the cost of project and advises the financial pattern to finance. This is another area of services rendered by the merchant bankers.

- c. Issue management:** The management relating to subscribe the share capital through the public in general is another area of service rendered by Merchant Banker. Under this head it does all function relating to public issue from obtaining stock exchange approval, drafting prospectus, public issue announcement, collecting applications, allotment of shares, refund of excess money, distribution of share certificates, and listing of shares on stock exchanges.
- d. Underwriting & bridge Loan Financing:** Underwriting is the commitment of guarantee to take up all shares/debentures which will not be subscribed by the public in general and it eliminates the risk arising from uncertainty of public response to new issues. The bridge loan is the short-term loan against the issue itself. Such type of facilities is also provided by the merchant bankers.
- e. Portfolio Management Scheme:** Merchant Bankers render the services of Portfolio management of their clients. Merchant Bankers accepts the funds on behalf of the clients\ to play in the financial game on capital market with an aim to earn target return. Effective investment planning and constant review of portfolio are the two basics principles for effective portfolio management.
- f. Mutual Fund/Unit Trust Scheme:** Another area of merchant banking is to arrange the unit trust scheme. Mutual Fund is a group saving scheme whereby it collect the idle money of the various sectors of society and invest in different area especially on blue chip companies shares and bonds on the principal of diversification. Merchant Banker acts as trustee for the investor on such trusts.

- g. Venture Capital:** Venture Capital means providing long term start-up funds for high risk ventures, promoted by unknown technologies/entrepreneurs, which suffer from capital deficiencies, but which have a profit potential through ultimate capital gains rather than through a steady dividend or interest yield. The merchant bankers do finance on this field for investment too.
- h. Lease Finance:** leasing could be defined as an activity where the owner of an asset gives the asset to another party for his use for a specified period of time for a financial consideration. Merchant bank facilitates the customer in acquiring equipments through the leasing finance.
- i. Factoring:** Factoring is specialized financing scheme where the financing company, known as a factor, buys its clients receivable of trade credits or invoices outright. In order to provide the client with an additional source of capital, merchant bankers also render the factoring services.
- j. Brokerage Services:** Merchant Bankers are the agent of Money & Capital Markets. They can play the role as borker or market maker in the stock exchange. In addition they can also play active role on money market.
- k. Merger & Acqusition:** Merchant Bankers deals on negotiating and valuation of merger, amalgamation and take over tof the firms. Similarly the assets/ share valuation assets securitization functions are also done by Merchant Banker. In this line they lso arrange for the foreign collaboration of the project.
- l. Management Consultancies:** Merchant Bankers may help to do the management audit of the companies to ascertain existing

performance levels and to formulate plan for future growth. They conduct market research for both consumer and industrial products, develop and implement system design and production management and at the same time Operation Research functions are also done for effective and optimum uses of the resources. Thus the coverage of the merchant banking is enormous and vast. The area of functions is unlimited of merchant bankers. Merchant banking services, therefore, are of great help to entrepreneur customers who cannot afford a permanent staff of financial specialists.”
(Shrestha, 2051: 16)

2.1.6 Responsibilities of Merchant Banker

To the investors

Investor protection is fundamental to a healthy growth of the Capital Market Protection Investor protection is not to be conceived as that of compensating for the losses suffered. The responsibility of the Merchant Banker is ensuring the completeness of the disclosures is of paramount importance in view of the fact that entire reliance is based on offer Document entire Prospectus or Letter of Offer because an independent agency like a Merchant Banker has done the security.

Capital Structuring

The Merchant Bankers while designing the capital structure take into account the various factors such as Leverage effect on earnings per share, the project cost and the gestation period, cash flow ability of the company, the cost of capital, the considerations of management control, size of the company, and general economic factors. These excises are done mainly in order to meet the fund requirement of the company taking due cognizance of the investors' preference.

Project Evaluation and due Diligence

Due diligence and project evaluation is another major responsibility of the Merchant Banker. Where a bank/financial institution the Merchant Banker has already appraised the project relies on the said appraisal before acceptance and assignment. However, where a bank/financial institution has not appraised the project, the Merchant Bank undertakes a detailed evaluation of the project before taking up an assignment for issue management.

Legal Aspects

The factors that are looked into in case of the legal aspects

- Compliance with the SEBI guidelines, the Companies Act, the Securities Contracts Regulation Act and Rules and the various guidelines issued by the Ministry of Finance and Department of Company Affairs.
- Pending litigations, disputes, defaults, over dues to financial institutions and banks proceeding initiated for economic offences against the promoters in respect of any of their business ventures in India or against the promoter's ventures or associate/group companies.
- Pending litigation's towards tax liabilities or any criminal/civil prosecution any of the directors for any offences.
- Material litigation pertaining to either the matter likely to affect the operations and finances of the company.
- Criminal prosecution launched against the company and its directors for alleged offences under the enactment's specified in Part 1 or Schedule XIII of the Companies Act.

- Defaults in meeting statutory dues, institutional dues and dues towards instrument holders like fixed deposit holders.
- Material development after the date of the last Balance Sheet.
- Fair and adequate disclosures in the prospectus.

Pricing of the Issue

The merchant Banker looks into the various factors while pricing the issue. Some of the factors are past financial performance of the company, Book value per share, Stock market performance of the shares (for existing companies, stock market perception of the company/group promoters, Price earning ration of the company/industry, brand equity, if any. The Merchant banker has a vital role to play in pricing of the instrument.

Marketing of the issue

Marketing of the issue is a vital responsibility of the Merchant Banker. The first stage in the Pre-issue marketing for placement of the issue with the financial institutions, banks mutual funds, FII's and NRI's. The second stage is the marketing of the issue to the general public through various vehicles such as press, brokers, etc.

Bought out Deals

The concept of wholesale but out of public offerings by the Merchant Bankers started off with over the Counter Exchange of India where a Merchant Banker act also as a sponsor and either takes up the entire issue to be offered wholly or jointly with other co-investor and off-loads the same to the public at a later date by an offer for sale. The role of Merchant Banker on the OTC exchange is not only that of a Merchant Banker but that of an Investment banker too. Major amendments were made to the SEBI regulation regarding Merchant Bankers in December

1997 both the old and new regulatory framework for Merchant Bankers are presently in force. The duration of this transition period has not officially been announced.

2.1.7 Banker and Merchant Banker

“A banker has funds with him which he mobilizes through deposits and borrowing or other ways and then deploys or lends these funds, whereas a merchant banker does not have any fund in his own kitty but he has the expertise and access to various sources of funds as per needs of the client. The bankers find merchant banking activity to be highly remunerative because of:

- Deposits on short term basis
- The business helps to improve their profits and profitability
- The business also helps to get good corporate clients.

2.1.8 Merchant Banking: International Scenario

a. Merchant Banks in the United Kingdom

In the United Kingdom, Merchant Banks came on the scene in the late eighteenth century and early nineteenth century. Industrial revolution made England into a powerful trading and early nineteenth century. Industrial revolution made England into a powerful trading nation. Rich merchant houses who made their fortunes in colonial trade diversified into banking. Their principal activity started with the acceptance of commercial bills pertaining to domestic as well as international trade. The acceptance of the trade bills and their discounting gave rise to acceptance house, discount houses, and issue houses. Merchant banks initially include acceptance houses,

discount houses and issue houses. A Merchant banker was primarily a merchant rather than his customers entrusted with funds.

The term Merchant Bank in United Kingdom is used to denote no banks that are not merchants, sometimes for merchants who are not bankers and sometimes for business houses that are neither merchant or banks. The confusion has arisen because modern Merchant Banks have a wide range of activities. Merchant Banks in United Kingdom: (a) finance foreign trade, (b) issue capital, (c) manage individual funds, (d) Undertake foreign security business, and (e) foreign loan business. They also used to finance sovereign government through grant of long-term loans. They financed the British Government to the State of Louisiana from Napoleon by raising loans from money market in London' and Lazard Brothers granted loan to the Second World War commercial banks in Western Europe have been offering multiple services including Merchant Banking services to their individual and corporate clients. British banks set-up division or subsidiaries to offer their customers Merchant Banking services.”

b. Investment Banking in USA

English and European Merchant Banks played a prominent role in the United States until indigenous Investment Bankers emerged on the scene in 1880's. In the early nineteenth century English and European Merchant Bankers met the requirements of finance for railroad construction and international trade. Later they opened their own offices in USA. Kidder, Peabody & Co.'s set-up in 1824 and John Eliot Thayer banking firm in 1857. During 1850-60 several Merchant Banks were set-up to arrange capital and enterprise to promote railways, industrial projects and trade and commerce. To finance railroad construction, capital issues were arranging by Merchant Bankers. In the late 1890's and early 1900's Investment Bankers replaced brokers and promoters who earlier played a prominent role

in issue of securities. Investment bankers apart from launching and organizing industrial units and mergers, helped transform privately held companies into public owned companies.

Investment banking largely remained unregulated until the Blue Sky Laws were introduced in Kansas to protect investors from fraudulent promoters and security salesmen. However, their growth was facilitated by the enactments of Federal Act in 1941, emergence of US dollars as leading currency and expansion of activities of US banking system. Prominent Investment Bankers in 1920's were Kidder, Peabody, Drexel, Morgan & Co; Brown Bros. And T.P. Morgan who brought and sold corporate bonds and stocks on commission, dealt in federal, state and municipal securities, trading and investing in securities on their own account, originating and distributing new issues on their own account, originating and distributing new issues and participation in the management of corporations whose securities they have helped distribute or in which invested.

After the great crash 1929 and depression, the Investment Banking business considerably contracted and experience heavy financial losses. The Federal government enacted several laws, called New Deal Enactment, to reform Wall Street practices to protect the interest on the investors. Officially called the Banking Act of 1933, the Glass-Steagall Banking Act separated Investment Banking and commercial banking and prohibited commercial banks from underwriting. Securities Exchange Act of 1934 sought to correct practices in securities trading.

The Glass-Steagall banking act prohibits commercial banks from acting as Investment banks or owning a firm dealing in securities. The Act has been challenged by banks offering money market mutual funds and other investment services and is expected to be the subject of reform. The US Federal Reserve board decided in January 1997 to issue a sweeping proposal (subject to 60-day comment period) that

would loosen restrictions and their securities industry affiliates can offer 'One Stop Shopping' for their customers. The securities activities of banks are allowed under a special provision in Glass-Steagall allowing the existence of such subsidiaries it subjected them to strict provision, including the part of the recent changes to those provisions the Fed has voted to allow the securities affiliate of banks to generate as much as quarter of their revenue from the underwriting and dealing of securities-an increase from the previous limit of 10 percent.

Regulation of Investment banking in USA

Investment Banking in USA as compared to Merchant Banking in the United Kingdom is subject to following regulation:

- The Securities Exchange Commission (SEC) exercises advisory and regulatory role on Investment Bankers.
- Investment Bankers were restricted from undertaking reorganization of public corporations under the Chandler Act. The task was assigned to distinguished trustees.
- Association of trustee with either the issuer or its Investment Banker was prohibited under the Trustee Indenture Act, 1939. To protect the interest of security-holders the trust indenture had to be filed with SEC
- The investment and portfolio activities became subject to SEC supervision.

Investment trust was covered by Investment Company Act, 1940 which sought to regulate them; and investment advisors are required to be registered under the Investment Advisors Act, 1940. SEC was designated the supervisory and enforcement authority. Its powers were further strengthened in 1960 by authorizing it to inspect the records and accounts of firms engaged in the business. The increased regulation and control of domestic operations gave a fillip to large US

banks to markets. The US Investment banks have extended their operations to the international level. They are largely responsible and globalization of capital markets. They have prominent presence in London and other European financial centers. Investment Banks have today a strong parent, a strong balance sheet and a strong international network to play a global role.” **(Laskshmana, & Naik,2002: 92)**

c. Merchant Banking in India

Merchant banking activity was formally initiated into the Indian capital markets when Grindlays Bank receives the license from Reserve Bank in 1967. Grindlays which started with management of capital issues recognized the needs of emerging class of entrepreneurs for diverse financial services ranging from production planning and systems design to market research. A part from meeting specially, the needs of small-scale units, it provided management consultancy services to large and medium sized companies. Following Grindlays bank, Citibank set up its merchant banking division in 1970. The division took up the task of assisting new entrepreneurs and existing units in the evaluation of new projects and raising funds through borrowing and issue of equity. Management consultancy services were also offered.

Consequent to the recommendations of Banking Commission in 1972, that Indian banks should start merchant banking services as part of their multiple services they could offer their clients, State bank of India started the Merchant Banking Division in 1972. In the initial years the SBI's objective was to render corporate advice and assistance to small and medium entrepreneurs.

2.1.9 Qualities of Good Merchant Bankers

“Following are the qualities that good merchant bankers should possess:

- a. **Leadership:** Merchant Banker should possess all relevant skills, updated knowledge to interact with clients and effectively communicate. Leadership is synonymous with followers who follow the one who leads.
- b. **Aggressiveness action:** Aggressiveness is a personality trait of a good leader but in merchant banking it has a wider connotation. Aggressive merchant bankers are always looking for new business. A good merchant banker is the one who does not allow his client to think anything outside except what he has been advised. Therefore, promptness in grasping the clients' problems and providing better choice amongst alternative solutions evidence aggressive approach in the profession to hold the client's interest in entirely for the present as well as for the future.
- c. **Co-operation and friendliness:** No doubt, these two characteristics are the symbols of good leadership but it hardly needs to be stressed. Co-operation and friendliness coupled with persuasiveness are the main instrument with which a merchant banker mixes with the people, gathers information, obtain business mandate and renders satisfactory services to the clients. Business of an honest merchant banker spreads with geometrical propagation when he shares the thoughts of his clients with sympathetic gestures and offers pragmatic suggestions without greed or favors. These are the vices unbecoming of a merchant banker to win over the trust of the clients like a doctor or lawyer who retain their clients permanently.
- d. **Contacts:** Success of a merchant banker depends upon his sociable nature and the richness of wider contacts. A merchant banker is supposed to be acquainted deeply with all the constituents of merchant banking. Merchant bankers should widen contacts and references and continue to maintain the

relationship with goodness, honor and humor by meeting people in person through writing and in special gatherings.

- e. **Attitude towards problem solving:** The most important personality trait of a merchant banker is his attitude towards problem solving. Every client coming to him has got to return fully satisfied having consulted a merchant banker. Positive approach to understand the view points of other, their difficulties and their advise circumstance is possible only when a person is skilled in human relations communication and proper feedback are the pre-requisites for creating a positive attitude towards problem solving which could be gained partly through learning process and partly as in-born quality.
- f. **Inquisitiveness for acquiring new skills, information and know ledges:** Merchant Bankers live on their wits they earn by giving information to needy clients. Therefore, they should keep abreast with latest information in the area of the service product they market. This is possible if merchant bankers posses the quality of inquisitiveness.

2.1.10 Importance & need of Merchant Banking

Important reason for the growth of merchant banking has been the development activity throughout the country, exerting excess demand on the sources of funds forever expanding industry and trade, thus, and leafing widening gap unabridged between the supply and demand of invest able funds. All India financial institutions had experienced resources constraint to meet the ever-increasing demand for funds from the corporate sector enterprises. In the circumstances corporate sector had the capital market services for meeting their long-term financial requirements through capital issues of equity and debentures with the growing demand for funds there was pressure on capital market that

enthused the commercial banks, share brokers and financial consultancy firms to enter into the field of merchant banking and share the growing capital market. With the result, all the commercial banks in nationalized and public sector as well as in private sector including the foreign banks in India have opened their merchant banking windows and competing in this field. There has been a mushroom growth of financial consultancy firms and broker firms doing advisory functions as merchant bankers as well as managing public issues in syndication with other merchant bankers.

Notwithstanding the above facts, the need of merchant banking institutions is felt in the wake of huge public saving lying still untapped. Merchant banks can play highly significant role in mobilizing funds of savings to investible channels assuring promising return on investment and thus can help in meeting the widening demand for investible funds for economic activity with the growth of merchant banking profession. Corporate enterprises in both public and private sectors would be able to raise required amount of funds annually from the capital market to meet the growing requirements for funds for establishing new enterprises, undertaking expansion/modernization/diversification of the existing need for a vigorous role to be played by merchant banks.

Merchant banks have been procuring impressive support from capital market for the corporate sector for financing their projects. This is evidence from the increasing amount raised from the capital market by corporate enterprises year after year.

In view of multitude of enactments, rules regulations, guidelines and off shoot press release instruction brought out by the Government from time to time imposing statutory obligations upon the corporate sector to comply with all those requirements prescribed therein, the need of skilled agency excited which could provide counseling in these matters in a package form. Merchant bankers, with their skills, updated information

and knowledge, provide the service to the corporate units and advise them on such requirements to be complied with for raising funds from the capital market under different enactments viz. companies act, Income-tax Act, foreign exchange Regulation Act, Securities Contracts (Regulation) Act, and various other corporate laws and regulations.

Merchant bankers advise the investors of the incentives available in the form of tax relief other statutory relaxations, good return of investment and capital appreciation in such investment to motivate them to invest their savings in securities of the corporate sector. Thus, the merchant bankers help industry and trade to raise funds, and the investors to invest their saved money in confidence, safety and expectation for higher yield.

2.1.11 Role of Merchant Bankers

“The role of merchant banker is dynamic in the wake of diverse nature of merchant banking services. Merchant Bankers’ dynamism lies in promptly attending to the corporate problems and suggests ways and means to solve it. The nature of merchant banking service is development oriented and promotional to help the industry and trade to grow and survive. Merchant banker is, therefore, dedicated to achieve this objective through his dynamism. He is always awake to renew his skills, develop expertise in new areas so as to equip himself with the knowledge and techniques to deal with emerging new problems of corporate business world. He has to keep pace with the changing environment where government rules, regulations and policies affecting business condition frequently change where science and technology create new innovations in production process of industries envisaging immediate renovations, diversifications modernizations or replacements of existing plant and machinery or other equipments putting new demands for finance and necessitation overhauling of the capital structure of the firms. Merchant banker has to think and devise new

instruments of financing industrial projects. He has to assume wider responsibilities of saving industrial units from going sick and guiding industries to be set up in industrially backward areas to eliminate regional imbalances in industrial development of the country. He has to guide the wider section of the community possessing surplus money to invest in corporate securities and other productive investment channels. He has to help the industry in different forms to ensure that it runs risk free and devoid of uncertainty by assisting the promoters with his knowledge and skills to resolve the problems being faced by them. He has to watch the interest and win over the confidence of the government its agencies along with the entrepreneurs, the investors and the whole community. He must bridge the communication gap between different sections and resolve problem being faced in different areas concerned with the business world. To discharge the above role, a merchant banker has to be dynamic. For this reason, a merchant banker is sometimes called M. B. i.e. Moving Bottom i.e. who never sits at one place, always moving attending meetings and meeting clients and constituents doing business and getting business by attending meetings and conferences imparting knowledge to others and acquiring supremacy in possession of latest information. His role depicts a personality cult, which is unique and envious to be followed by others. In the days ahead, Merchant bankers have very significant role to play turning their activities to the requirements of the growth pattern of corporate sector, the industry and the economy as a whole which is in it a challenging task and to meet these challenges. Merchant bankers will have to be more vigorous and strategic in playing their role. They will have also to adopt new ways and means in discharging their role.

2.1.12 Business Development Approach and Strategy

Merchant Banking services are highly competitive business activities and to get business, merchant bankers have to stand on their heels and run

to grab the business opportunity. Each of the officers in merchant banking department, division, cell or bureau or company should have the requisite skills of marketing and salesmanship to ensure that the opportunity once found is not lost without obtaining mandate from the client. Therefore, a merchant banker has got to be a social person with mixing nature and temperament of liking others. The source for locating business opportunities would vary but merchant banker has to tap each source. Some of the sources could be located in the areas which give rise to new ideas, open avenues to new business and provide scope for additions in the existing business system by way of modification, modernization, diversification expansion, amalgamation or reconstruction etc. These sources of information could be the banker whose client is thinking in terms of such ideas; the financial and technical consultancy firms, which are working on such ideas for their clients; licensing authorities of the central Government or Registration Departments of the State approached by the prospective borrowers with loan application for grant of financial facilities. A close liaison with these institutions could provide a clue for business opportunity for a merchant banker. Besides the published information in different news dailies, weeklies and fortnightly or monthly magazines provide the source proceeding of annual general meeting of companies specially granted to the press opening opportunities for entrepreneurs to take up new activities, information published by chamber of Commerce and Industry, house journal of prominent industrial houses, press releases by Government, import licenses or capital goods committee's clearance, foreign collaboration permissions, etc.

The basic approach for merchant banker is to maintain close contact with other agencies involved in managing public issues like managing brokers, advertising agencies, firms of registrar to the issue, banks operation as bankers to the issue and advocates/solicitors who have

expertise in the area for corporate law and consultancy. These agencies could give clue to the new business opportunity to be explored by the merchant banker.

The basic strategy should be to get information, follow-up the same and materialize the business opportunity. To this end, the merchant bankers should frequently join clubs where the business magnates meet and freely mix with them, talk about their future business plans and converse with them on issues of interest to them, join association or club or merchant bankers and be inquisitive to trace new opportunities for the merchant banking business, explore the possibilities of working with existing merchant bankers to the forthcoming public issues or other merchant banking activities. He should develop contacts with agencies like India Investment Center which is helping the non-resident Indians in setting industrial licenses, Central Government clearances, foreign collaboration or approval from such like institutions and thus he can get business in areas of credit-syndication corporate/project consultancy, issue management portfolio management for NRIs etc. In addition to above, merchant banker should take steps to promote new business in following manner.

- Contact frequently the small business owners convince them of business growth through expansion of their activities by forming limited companies, pooling resources together through merger and amalgamation, etc.
- Helping private limited companies to convert into limited companies and take up new activities/expansion/modernization/diversification program etc. and assure them or requisite help,

- Acquaint the existing business houses/clients of incentives given by Government, new opportunities for business, to enthuse them to take up new activities; and
- Hold interviews with top business houses frequently and appraise them of merchant banking services and new areas of business activity to elicit business from them and develop business connections.

Merchant bankers, in addition to above, should assume the role of an experienced and skilled investigator and researcher to locate new business opportunities and expert marketing man to sell the service products instantaneously.

2.1.13 Investment Banking and Securities Trading

The basic difference between investment banking and securities trading is that investment banking is concerned primarily with new issues, whereas securities trading relates to existing securities. For example, Merrill Lynch is acting as an investment banker when it sell a new issues of American Telephone and Telegraph (AT &T) common stock, but is a securities trader when it participates in the exchange of existing AT&T common stock. Some investment firms, such as Merrill Lynch, Salomon Brothers, and Dean Witter Reynolds, perform both investment banking and securities trading function, while other, smaller firms specialize in one function. Investment bankers perform several important functions to bring new securities to the investing public. The major functions of investment bankers are:

- Origination
- Underwriting

- Distribution.

New securities are created during origination, bought by investment bankers during underwriting, and sold to investors during the distribution phase.

Origination: Security flotation is complex matters, and security issuers look to the investment banker for specialized assistance during origination. Origination is the important function of providing issuers investment advice, information, and assistance. The investment banker commonly:

- Advises the issuer on the type of security and specific terms which are most acceptable during current financial market condition.
- Prepares and assists in filing a prospectus with the Securities and Exchange Commission.
- Arranges for the efficient distribution of the new issue.
- Arranges for a number operational requirements such as trustees, security indentures (contracts), and safekeeping.

Issuers depend heavily upon investment bankers who are financial market specialists to create securities which meet most of the issuer's needs and, simultaneously, are acceptable for sale to investors.

Underwriting: Investment banking firms often purchase new issue or guarantee its sale at a specified price. The investment-banking firm underwrites the new issue when it assumes the marketing risk. If the security is not sold to investors at the offering price, then the underwriter incurs the loss. Underwriting is important to the issuer because it guarantees the amount of money which will be raised by the security issue.

Distribution: The investment bankers distribute the issue to many investors. To sell the issue quickly, a syndicate of many firms is formed

for each issue, and the securities are distributed through a large network reaching many potential investors.

2.2 Review of Related Studies

The study conducted by MR. Madhuban L. Shrestha (2051) in his article “Merchant Banking- an Outlook” in Nepal Bank Patrika has thrown light on merchant banking in Nepalese Perspective. Shrestha indicates that Merchant Banking in its crude form existed in Nepal from the advent of modern banking system with the establishment of Nepal Bank Limited. However, Security Exchange Center set up in 1976 was the pioneer institution on the capital market in Nepal. Modern and innovative services on Banking sector were introduced by the establishment of Joint Venture Bank in the country. The Finance company Act 2042 gave birth to a new dimension to the merchant Banking Services. After the restoration of democracy, the country launched financial liberalization and privatization programs. As a result maximum participation from the public took place and the country entered on the new industrialization process through rapid development on capital market. Consequently there is a call for the different services of the economy.

Citizen Investment Trust (CIT) is a pioneer merchant banker of the country followed by other finance companies viz. NIDC Capital Market, National Finance Co., Nepal Share Market etc. There are a few number of incorporated bodies who also render these services. Recently Rastriya Banijya Bank has opened a separate Merchant Banking Division. Thus this is the time to think seriously by the commercial banks that apart from their traditional business, they have to add such new ventures which will pay high return to them with nominal investment.

“Mr Ramesh Kumar Pokharel (2057) in the article “Merchant Banking Services in Nepal” in Banking Prabardhan, 2057 vol. 11 has mentioned on Regulatory Aspects of merchant Banking in Nepal. According to Mr.

Pokharel, Merchant Banking is a new concept for Nepal. Its role as an important financial intermediary cannot be challenged from anywhere in the growing financial system of Nepal. Although a few financial institutions (basically Finance Companies) are involved in different merchant banking activities, there is no clear definition of merchant banking in Finance Company Act, 1986 and no specific legal provisions to be complied by merchant banker. However section 3(e) of Finance Company Act, 1986 permits finance companies to sell and purchase the bonds issued by His Majesty's Government of securities issued by other companies or institutions, to underwrite them and to form syndicate for such purpose or to participate in such syndicates and to act as broker under the Securities Exchange Act, 2983. And section 3(g) of the same act permits them to perform functions of merchant banking with prior approval of NRB.

Since there is no separate entity to carry out the merchant banking activities in Nepal, these activities are associated with other transaction of finance companies. These institutions are expected to meet NRB's requirements on:

- Minimum paid-up capital and the prescribed risk – weighted capital ratio;
- The liquidity Ratio;
- Merchant Banking activities up to 60% of total Credit and Investment Portfolio.
- Issue Management and Underwriting up to maximum of 10% of total loan and advances of finance company.
- Likewise, there is no guideline issued by NRB especially for merchant banking in following respects;
- The minimum acceptable percentage of income from fee-based activities;

- Issuance of negotiable certificate of deposits; and
- Terms governing the acceptance of time deposits.

Mr. Pokharel has also pointed out on examination requirements for Merchant Banking. He writes that it is a matter of fact that no adequate directives have been issued for the regulatory and monitoring purpose pertaining to Merchant Banking, however Inspectors while making supervision to these services should basically focus on the following parts of these transactions;

- Agreement between the parties, specific terms and conditions.
- Legal and regulatory provisions related to public issue (Company Act, Securities Board's Regulations).
- Underwriting services and its accounting treatment.
- Volume of Underwriting and Issue management (to confirm whether these transaction fall under the NRB's directives or not)
- Other issues relevant to specific merchant banking function.

Mr. Pokharel also writes the problems and issues in Merchant Banking services in Nepal in eight points which is mentioned below:

- Normally in any business, there should not be confusion about the customer. However, merchant banking services, especially in issue management, some problems can be prevailed. MBs are commissioned and paid for the company issuing the share/debentures. Apparently, the issuing company is the customer of the MB. However, the fee received by the MB comes from the investors who subscribe to the shares/debentures. Thus it is not wrong to say that the fees to MB are ultimately paid by the prospective investors of the share/debentures. Thus it is very hard for MB to serve for the best interest of both investors and issuing company.

- MBs should ensure to the investor that all possible information about the issue is given, and that post-issue management i.e. allotment of shares, etc. and refund are effected with utmost expedition. In the pre-issue phase, MBs should ensure the investors that the issuer is having a good track record and thus MBS should give a clean cheat to the issuer. In case the issuer is found guilty then MBs ultimately suffers and should face the public or investors.
- Post issue management has become a difficult task in Nepal, especially because of heavy over-subscriptions of vast majority of issues due to unrealistically low floatation pricing of issues by existing company. The problems are accompanied by rigid rules of allotment prescribed by Stock-exchange that four small applicants and therefore increase the number of applicants. The banking system is extensively used for this purpose but it seems very hard to cope with load.
- To the issuing company, MBs should render high standards of professional services and also perform their role with due diligence.
- Merchant banking service has become more challenging for the monitoring system of Nepal especially for the central bank due to the lack of adequate legal and regulatory framework.
- There should be a prudent and sound financial market to adopt the different merchant banking services. Due to the limitation of financial market the services rendered by merchant banking are also limited in Nepal.
- In implementing self-regulatory mechanism, MBs would have to monitor the performance of other agencies that also provide services to the issuer. There are Advertising Agencies, Registrar to the issue and other financial institutions. But in Nepal MBs do not

have any control over these agencies, although MBs are help responsible for the performance of lack of it by the associated agencies.

- According to comprehensive guidelines formulated by Stock-Exchange, a company should either be already listed or should be listed in Stock-Exchange within three months of the closure of the issue. But generally listing I being done lately due to large numbers of shareholders, and provision regarding transferability.

In the article “An Overview of Merchant banking” in Prasichhin, Mr. K. B. Kayal (2065) writes challenges ahead to Merchant Bankers. According to Mr. Kayal, Merchant bankers have to tap the opportunities lying ahead with the developing pace of the economy. These opportunities arise in the form of challenges before the merchant bankers to test their skills, expertise and efforts to attune their activities with the programme of economic development of the country, adopt new instruments and innovative means of financing to meet the growing financial requirements of the corporate clients. Some of the areas of challenges, which have been explored on the basis of research, are classified as under.

- Merchant bankers will have to conduct management of capital issues in a different fashion then what is being done at present. If small industries are to be provided the full benefit of their services of corporate counseling project counseling and loan syndication then besides distribution of their securities to the public and arranging long-term institutional or banking finance, it would be necessary for merchant banks to make out-right purchase of capital issues in total and to retain the purchased equity of the company till the implementation of the project commencement of production and profitable working of the company when the issue may be treated as good for marketing to the general public, may be on premium, so as to make capital gains, on that. This course of

action will benefit the small industries in many ways; firstly they will have the quick liquidity and secondly, their project will be implemented under the skilled supervision and expert guidance of the merchant bankers. Beside, the investing public will be willing to purchase the issue at premium, have foreseen the dividend paying capacity of the only course, if adopted, would reduce cost of the issue to negligible extent.

- If the planned objective of economic decentralization and rapid development of rural economy is to be achieved, merchant bankers will have to make experts efforts in the interest of the national economy by mobilizing the savings from the rural sector and creating avenues for its investment in rural areas in industry, trade and commerce in different shapes and different magnitude encouraging the local people to espouse entrepreneurship in industrial undertakings in higher degree so as to reduce their dependence on land farming or other means of rural avocations. Alternatively, this poses a big challenge for the merchant bankers to manage the surplus money available with the villagers by holding portfolio on their behalf or by channelising it directly to industry in the shape of fixed deposits, etc.
- Increasing number of sick industries is the ever-growing threat for the industrial economy of the country. Merchant bankers have to find out ways and means for rehabilitating the sick industries and also devise the manner by which the running industry might be saved from going sick. They should so closely associate with the units so as to smell developing weakness in the management of the enterprise and suggest timely leading to –sickness of the industrial unit “Management buy-out” is one of the techniques which has been successfully tried in European countries as well as in USA, to check sickness in industry. This device encourages the executive

staff of the company to purchase the shareholdings of the proprietors and promoters and run the factory on professional basis. Venture capital funds contribute substantially in this area of finance.

- The millions of small savers of small saves are unable to manage their savings in Nepal in both rural and urban areas. These are mainly the people from the middle class and lower middle class. Merchant bankers must devise ways and means to provide services for portfolio management to these citizens. This may be by taking recourse to encouraging the “mutual funds”.
- Public and private sector institutions engaged in trade, commerce and industry have many times surplus funds lying with them awaiting opportunity outside. These funds should be tapped by the merchant bankers from time to time by mobilizing them to deficit areas in profitable return basis playing the interest rate games as is done in SWAP deals in international finance.
- IN the international field, where public and private enterprises are entering to raise foreign currency resources, Nepalese counterparts have to depend upon that assistance of foreign merchant bankers. Nepalese merchant bankers therefore will have to sharpen their skills and attain the requisite expertise in the field of internal merchant banking.
- Attention is required to be gathered to the point that the banks and the financial institutions which are running the merchant banking division can think in terms of taking up the activity of providing acceptance credit and re-discounting facility to certain number of their clients on experimental basis on the lines of the traditional activity of European merchant bankers. This will help for creation of secondary market for commercial papers as well.

- To tap the latest technology available internationally and procure the transfer of tours of foreign countries, organize meetings and conferences with the chamber of Commerce and Industry and other commercial, industrial and financial organizations so as to enthruse the foreigners to take interest in investment activity in Nepal Merchant Bankers, therefore, have to take latest information about the economic, social and political environment of our country to foreign countries and apprise the foreigners with the facilities and relaxations in carious rules and regulations of the Government and the policy framework available for their benefit in case they chose to invest in Nepal or lend their technological expertise to Nepalese entrepreneur and/or to collaborator in any other useful manner.

Mr. M. L Shrestha (2064) in his article “Portfolio Mangement. A Merchant Banking Service” in Nepal Bank Patrika- Ashwin Masanta, 2052 has written portfolio management as one of the merchant banking service. According to Mr. Shrestha, optimal portfolio produce the maximum return with the minimum portfolio, it has been purely a professional approach. Merchant bankers are one of those who render this service to the investors. He writes portfolio management, thus, means the personal commitment of Merchant Banker to take care of investment of investor with the prudence and astuteness of professional fund mange to given investor his money, worth.

Mr. Shrestha has mentioned two basic principles for effective portfolio management, which is as follow:

- a. Effective Investment Planning:** Merchant bankers must consider the factors such as fiscal, financial, monetary, credit policies of central bank and guidelines and directives issued time to time by stock exchange.

b. Constant Review of Portfolio: Merchant banker should constantly review their investment in securities and continue selling and buying the same to earn profits.

In connection to portfolio management in Nepali context, Mr. Shrestha writes there is no any regulatory framework made in this sector so far in Nepal. Neither the government has initiated any law nor has the stock exchange board of Nepal issued any rules and regulation regarding the operation of Portfolio Management Service. However, NIDC Capital Markets Ltd, 1st Merchant Bank of Nepal, has launched the step to render this service from its initial period.

As per their research and analysis, they are pointed out following sectors are attractive for the Nepalese investors.

- Construction material
- Financial Services
- Health and Pharmaceuticals
- Education and allied services and products
- Livestock (Diary, meat, production, leather products etc.)
- Tourism
- Textile
- Office services (software development, media planning and advertisement)

Minimum size of each account should not be less than Rs. 5 million to them to take up for portfolio management. The fund accepted for portfolio management by them, will be spread to into the above mentioned different investment opportunities, which yield better and provide better quality of investment. Their target is to maximize the earning via current income & capital gains. But the structure of return

will depend on the objectives and preferences of the investor. As a Manager, their paramount concern is the safety of portfolio of the investor.

After the advent of liberalization policy in Nepal, it went on a new direction on economic activities. As a result now in Nepal such kind of service is available. So, for those investors who really want to enjoy maximizing their wealth with liquidity and safety of investment, they can approach to the Merchant Banker and get rid of handling the day-to-day task of administering portfolios. One can handover all the investment decision to them enjoying better return from the surplus fund.

In the article "Merchant Banking and Mutual Fund in Nepal" by Mr. Kalyan Bandhu Aryal (2065) in Nepal Rastra Bank Samachar, 2060, Mr. Aryal highlight the scenario of merchant banking and mutual fund in Nepal. As far as Mutual Fund is concerned, Mr. Aryal says that the concept of mutual fund has been introduced in Nepal from last decade. He again writes, there is no separate entity or company to carry over this business in Nepal. NIDC Capital Market Ltd. Operated as a manager and NIDC had been acting this business as a trustee. Regarding NCM Mutual Fund, 2059 Mr. Aryal says NIDC

Capital Market Ltd. is recently launching NCM Mutual Fund, 2059. As a financial services or an scheme which aims to invest the fund/money collected from various investors, out of 10 million unit, 1.5 million units for trustee and manger, approximately 1.37 million units for unit holders of the first NCM Mutual fund, 2050 and approximately 7.17 million units for public. NCM Mutual Fund, 2059, manger can invest as follows: in share investment 65%, debt investment 15% and 20% credit to organization as short-term and medium term loan.

This scheme is suppose to close once the certificates of Mutual Fund units. But on the request and demand of the investors, scheme would

restart and transaction of the mutual fund is being done from stock exchange. Now the scheme is restructured and closed ended. All the decision regarding mutual funds are taken by a management committee.

Mr. Aryal also gives examination procedures for merchant banking and mutual fund as follow:

Merchant Banking: Inspectors should primarily focus on the following aspect while making supervision of the merchant banking activities;

- Agreement between the parties, specific terms and conditions.
- Legal and regulatory provisions related to public issue (Company Act., Securities Exchange Act and Nepal Securities Board's Regulations).
- Underwriting services and its accounting treatment.
- Other issue relevant to specific merchant banking function.

Mutual Fund: NRB has not issued specific directives on mutual fund related activities, but however the company carrying mutual fund activities may design specific norms and self-regulatory provisions with objective of diversifying risk. These provisions may include:

- Limit of investment in a company
- Maximum holding limit of shares/debentures of a company
- Listing of units with the stock exchange
- Liquidity provision
- Calculation of NAV and cost incurred by the managing company.

Mr. Gautam 'Biji' (2060) in his article "Leasing Finance in Nepal" in "Nepal Rastra Bank Samachar, 2060 writes about theoretical framework, present status of Leasing Finance in Nepal, types, problems and suggestions. The problems of leasing business in Nepal according to him are lack of legal provisions, insufficient regulation, lack of business

activities & mega projects, discriminatory treatment for loan loss provision and confusing procedure for depreciation. Mr. Gautam concludes at last that leasing is a long term financing business activity. It allows both lessor and lessee with various advantages like: cent percent financing, depreciation facility even on land, financing, depreciation facility even on land, financing flexibility and so on. This does not mean that leasing is risk free and does not have a stated interest cost. It creates some problems for rentals. It raises some questions during the transfer of ownership, on the realization of the salvage value of the asset and obsolescence in the leased asset. The new income tax act, just mentions the nature of lease, process for repayment, treatment of depreciation, sale of transfer of asset and process for treatment of tax.

Leasing is just a way to supplement the conventional methods of financing. It should be a mean not an end for the business activity. It requires competent manager to analyze and assign the limitation for the business activity. It requires the competence manager to analyze and assign the limitation for leasing business. Though, present scenario is not encouraging for the leasing, may be the right time to open up public voice and ask for the government in designation of legal framework and necessary arrangements and central bank for the proper banking regulation.

Recently NIDC Capital Market has introduced the concept paper of Nepal Industrial Venture Capital Fund (NIVCF) with the view to introduce venture capital in Nepal. Venture Capital investments were risky but in its success there were fantastic turnover on the investment. The professionally run VC have been encouraging and assisting the establishment, development and modernization of industries in private sector by providing financial, managerial and technical support.

The handicaps for venture capital companies in India like in other developing countries as mentioned on the concept paper are:

- Insufficient understanding of Venture Capital as commercial activity.
- Limited flexibility in investment area.
- Investor attitudes of retaining control over the business ensuring to pass over to their families.
- Exit from investment is limited.
- Some legal inadequacy such as inter corporate investment without prior approval is prohibited and trust funds cedes all rights relating to annual or extra ordinary general meeting in favor of public trustee.
- VCF has been limiting its role of financing only, the post investment support services are not taken care of.

Following are the objective of NIVCF:

- To support small yet expanding and successful companies, which are not yet mature for going public and new companies which are not big enough for going public, but where the entrepreneurs have excellent educational background, financial standing and a clear concept?
- To gear up the local potential entrepreneurs in adopting to emerging common market concept world wide by providing comprehensive management support to offset the entrepreneurs inexperience with the specific markets and technology.
- And also to secure good returns to the investment through capital gains beside current income.

The areas of investment by NIVCF are:

- Technology transfer
- Foreign Exchange Earning
- Agro-Processing
- Services and
- Services and Turn-around companies” (Concept Paper of Nepal Industrial Venture Capital Fund (NIVCF)

In the handout prepared by Nepal Merchant Banking & Finance Limited, the details of services provided by the company to its customer as Registrar to Share Issue have been given. According to the handout the services provided by NMB under Registrar to Share Issue are as follow:

Under this activity NMB provides following services:”

- a. Maintain and update shareholder’s files on regular basis/
- b. Maintain record of signatures of the shareholders.
- c. Verify shareholder’s signature as and when required
- d. Obtain documents in case of share transfer
 - Covering letter of Nepal Stock Exchange Limited (NSE)
 - Dakhil-Kharej form with verified signature.
 - Share certificates as per the covering letter of NSE
 - Transfer charge NPR 5.00 (In words Nepalese Rupees five Only) per certificate (to be borne by the concerned Shareholder).
 - A copy of citizenship certificate of the Shareholder in case of new shareholder.
- e. Transfer of Share Certificates
 - Register the name of the buyer/seller in the shareholder’s book

- Allocate registration number to each transaction
- Give Identity number
- Issue new share certificates by splitting the share certificate in case of partial transfer.
- Registration (Dhakila) of share certificates and transfer of the same to the buyer's (shareholders) Name.
- Affix authorized signature of the company secretary/director as appropriate and official seal of the Bank after the endorsement.
- Forward transfer share certificates to NSE for distribution along with transfer list
- Recover the transfer fee of NPR 5.00 (In words Nepalese Rupees Five Only) per transfer.

f. Split Ordinary Share certificate

- Split of certificate at the request of the holder.
- Sign on the split documents (Annexure 1 of ormat issued by Nepal Stock Exchange Limited)
- Recover the split fee of NPR 5.00 (In words Nepalese rupees Five Only)
- Per split (to be borne by the holder).

g. Pledge of Ordinary Share

- Maintain record of pledge of shares.
- Obtain Letter of the company pledging the share with details of Certificates
- Obtain certificates as per the covering letter of the company pledging the shares.

- Obtain authorization letter of the Shareholder for the pledge of certificates.
- Verify the signature of the concerned Shareholder.
- Record 'Rokka' of the pledged share certificates.
- Release of the certificates(s) upon subsequent advice to this effect from the financial institution pledging the Share(s).
- Release the certificates(s) upon subsequent advice to this effect from the financial institution pledging the Share(s).
- Release the certificate (s) to the holder if release letter is received from the company pledging the shares, after recording release of the database.

h. Documents required to be obtained in case of death of shareholder

- Original share certificates of the deceased shareholder.
- A copy of citizenship of the deceased shareholder
- A copy of death certificate.
- A copy of relationship certificate
- Application letter of transferee.
- A copy of citizenship of transferee
- Authority letters from other inheritors.
- Send letter to NSR for information and Rokka
- Publish 35 days notice in the daily newspaper after getting all the required documents and confirming that the application is valid
- Transfer the shares to the transferee after 35 days from the day of notice publication

- Issue new certificates in the name of transferee
 - Distribute the share certificates and recover notice publication charge from the concerned individuals (shareholders).
- i. Documents required to be obtained in case of loss of share certificates.
- Application letter from the shareholder
 - Signature verification of the applicants.
 - Record “Rokka” of the lost share certificates in computer record and inform NSE in writing.
 - Publish 35 days’ notice in the daily newspaper.
 - Issue new share certificates after 35 days.
 - Handover the certificates and recover notice publication charge from the concerned individual (shareholders).
- j. Provide list of shareholders to the concerned parties as and when required.
- k. Provide Certificate of Share holding to the Shareholder(s) as and when required.
- l. Maintain/update backup file of whole computer data on regular basis.
- m. Distribute undistributed Share certificates, dividend Warrants & Bonus share Certificates, if any, to the concerned Shareholders.
- n. Assist Bank in the conduction of Annual General Meeting (AGM)

Capital market is a crucial element in the national economy. Its role in reinvigorating and boosting the economic activities in the country holds significant. The strategic plan released by security board can, to a great extent, energize the investor’s dealer by increasing investor interest in it.

Security market experience both boom and bust soon after the beginning of securities trading through brokers' members in the stock exchange floor. Though the market started to function quickly boosting the prices of shares to an unexpected level, it could not be sustained.

There is an urgent need for proficient development of the market standard and information dissemination system focusing mainly on corporate financial disclosure practices and transparency, corporate accounting and auditing securities markets regulation and corporate governance. To implement the above, Security Board has a great responsibility as to reviewing and developing regulatory standards to make them relevant with the need of issuers, investors along with promoting efficient capital formation.

There are many loopholes in our Stock-Exchange Act. Investors feel insecure here. A few years back there was a company called Nimrod Pharmaceutical Company that floated in shares, but where are they now? Similarly, it has been more than a year that Bansbari Leather age has allotted its shares, but why didn't the company list its shares in the market? It has been three years that Gorkhali Rubber Udhog hasn't called for its AGM Government remained silent in all these cases. This is why the general public as well as the institutional buyers are not feeling secure in investing in stock market.

In its Annual Report for the fiscal year 2001/01, SEBO states that it has made some attempts to address the issues through issuance of guidelines, directives and disclosure formats to the market participants, codes of conduct for the stock brokers etc. It has also prepared a draft for the new securities exchange act, which was presented to the Ministry of Finance in 1998 to initiate the necessary legislative process. However, it is still to be enacted by the parliament.

Even though SEBO has made attempts to solve the problems, they are still there. It cannot escape its duty to explain the present state of the market and deficiencies existing in the system. Taking necessary support from the government it should take the required step to better coordinate the market participants to develop a healthy capital market in the country. Moreover it is important to discipline the market participants and educate them of their moral duty to comply and make others comply with the prevailing rules and regulation. Only this can create the atmosphere where scandals like this one are not repeated. (SEBO, Annual Report Fiscal Year 2001/02)

Merchant Banking History

“In late 17th and early 18th century in Europe, the large companies of the world were merchant adventures supported by wealthy groups of people and a network of overseas trading posts, they collected large amounts of money to finance trade across parts of the world. For example, The East India Trading Company secured a Royal Warrant from England, providing the firm with official rights to lucrative trading activities in India. This company was the forerunner in developing the crown jewel of the English Empire. The English colony was started by what we would today call merchant bankers, because of the firm’s involvement in financing, negotiating, and implementing trade transactions.

The colonies of other European countries were started in the same manner. For example, the Dutch merchant adventurers were active in Indonesia; the French and Portuguese acted similarly in their respective colonies. The American colonies also represent the product of merchant banking, as evidenced by the activities of the famous Hudson Bay Company. One does not typically look at these countries’ economic development as having been fueled by merchant bank adventurers.

However, the colonies and their progress stem from the business of merchant banks, according to today's accepted sense of the word.

a. The History Merchant Bank

Merchant Banking, as the term has evolved in Europe from the 18th century to today, pertained to an individual or a banking house whose primary function was to facilitate the business process between a product and the financial requirement for its development. Merchant banking services span from the earliest negotiations from a transaction to its actual consummation between buyer and seller.

In particular, the merchant banker acted as a capital sources whose primary activity was directed towards a commodity trader/cargo owner who was involved in the buying, selling, and shipping of goods. The role of the merchant banker, who has the expertise to understand particular transaction, was to arrange the necessary capital and ensure that the transaction would ultimately produce "collectable" profits. Often, the merchant banker also became involved in the actual negotiations between buyer and seller in a transaction.

b. The Modern Merchant Bank

During the 20th century, however, European merchant banks expanded their services. They became increasingly involved in the actual running of the business for which the transaction was conducted. Today, merchant banks actually own and run businesses for their own account, and that of other.

Since 18th century, the term merchant banker has, therefore, been considerably broadened to include a composite of modern day skills. These skills include those inherent in an entrepreneur, a management advisor, a commercial and/or investment banker plus that of transaction broker. Today merchant banker is ho has the ability to merchandise that is, create or expand a need and fulfill capital requirements. The modern

European merchant bank, in many ways, reflects the early activities and breadth of services of the colonial trading companies.

Most companies that come to U.S. merchant bank are looking to increase their financial stability or satisfy a particular, immediate capital need.

Professional merchant bankers must have: 1) an understanding of the product, its industry and operational management; 2) an ability to raise capital which might or might not be one's own (originally merchant bankers supplied their own capital and thereby took an equity interest in the transaction); 3) and most importantly, effective skills in concluding a transaction – the actual sale of the product and the collection of profit. Some people might question whether or not there are many individuals or organizations that have the abilities to fulfill all their areas of expertise. **(Bruce W. Barren, the EMCO/Hanover Group,** <http://www.emcohanover.com/merchant.htm>)

Merchant Banking Rule Finalized

Most compliance officers immediately think of privacy when the Gramm-Leach-Bliley Act is mentioned, but in actuality the most significant provisions of GLBA deal with banking powers.

Under GLBA, a bank holding company may elect to become a financial holding company. Under a new rule from the FRB and treasury that carries out amendments made of the Bank Holding Company Act by Gramm-Leach-Bliley Act, a bank holding company that has made an effective election to become a financial holding company⁷ is allowed to make investments in non financial companies as part of a bona fide securities underwriting or merchant or investment banking activity.

Under the new rules, investment may be made in any type of ownership interest in any type a non-financial entity (portfolio company), and may represent any amount of the equity of a portfolio company. Investments made under this new authority are referred to as “merchant banking

investments” these merchant banking power is an important addition to traditional bank activities.

If your bank wants to explore its options under these new powers, you should be aware that there are conditions on three aspects of the activity:

- The length of time that these investments may be held.
- The ability of the financial holding company to routinely manage or operate the portfolio company
- Their aspects of the relationship between the financial holding company and its affiliates on the one hand and the portfolio company on the other hand.

The effective date of the new merchant banking rules was February 25, 2001.” (<http://www.bankersonline.com/operations/merchant.html>)

2.3 Previous Thesis

Under this section, various master’s level thesis related to this study have been reviewed. These are as follows:

Pradhan (2005) conducted research on topic of “Merchant Banking in Nepal”. She used data from fiscal year 2050 to 2059; she has studied the performance of NIDC Capital Market, CIT and NMB.

The study of this study is to evaluate the performance of merchant bankers in Nepal and the growth of merchant banking in Nepal.

The findings of her study were:

- Public issue of the securities is in increasing trend.
- Most of the issuing companies are financial institution.

- Merchant banking activities are concerned on floating the public issue of securities.
- Most of the income of major merchant banks is from public issuer management.

Subedi (2007) conducted research on topic “Merchant Banking Practice of Financial Institution”, using data from fiscal year 2050 to 2059. he has studied the merchant banking performance of NIDC Capital Market, CIT and NMB.

The objectives of his study is to analyze the existing problem of merchant banking in Nepal and to study the relationship of merchant banking towards the development of securities industries in Nepal.

The findings of his study were.

- NIDC capital Market is not only found to be performing public issue management but also functions of underwriter and syndicate underwriting of public issue from 2050/51.
- CIT is providing service such as market maker of corporate and government securities and consulting service for designing capital structure, pricing of securities etc.
- Merchant banking income of NIDC Capital Market and CIT is in increasing very steady.

2.4 Research Gap

Previous researcher has used data from fiscal year 2056/57 to 2062/63. Data has been updated till fiscal year 2064//065.

Among the reviewed thesis only Pradhan (2003) has analyze primary data. Major concentration of this thesis is to analyze primary as well as secondary data.

Apart from this previous thesis contained all the merchant banks that existed then only. In the advent of establishment of specialized merchant bank 'Elite Capital Limited and announcement of NRB to separate banking activities with that of Merchant Banking Activities a new research work is seen to be the must.

CHAPTER III

RESEARCH METHODOLOGY

3.1 Introduction

A research has been defined as “the systematic search for pertinent information on a specific topic” **(Cordasco & Gatner, 1958:86)**. Research and report writing New York: Barnes and Noble. P.1) Research is common parlance that refers to a search for knowledge. As per the Webster International Dictionary, research is “a careful critical inquiry or examination in seeking facts and principles; diligent investigation in order to ascertain something.” **(Saravanavel, 1990:1)**

“Research Methodology is a way to systematically solve their research problem.” **(Kothari, 1994: 10)** It may be understood as a science of studying how research is done scientifically. A research methodology helps us to find out accuracy, validity and suitability. The justification on their present study cannot be obtained without help of proper Research Methodology. Hence this chapter looks into the research design, nature and sources of data, method of data collection, tool and techniques of data analysis and their limitations the research methodology used in present study is briefly mentioned below.

3.2 Research Design

“Research Design is the plan, structure and strategy of investigations conceived so as to obtain answer to research question and to control variances”. **(Kerlinger, 1986:275)** Thus, it means an overall framework or plan for the collection and analysis of data.

This research is based on recent historical data. It deals with the merchant banking activities of the companies taken as a case study

based on available information. This research is quantitative or analytical based as well as descriptive and exploratory.

3.3 Populations and Sample

There are lots of financial institutions like banks, finance companies, co-operatives, insurance companies etc in our country Nepal. Out of those entire companies, some acts like Commercial Bank Act, Development Bank Act, Finance Companies Act, NIDC Act, CIT Act etc permits them to perform merchant banking activities. We have 17 commercial banks, 17 development banks, 5 Gramin Development Banks, 58 finance companies, 1 Nepal Industrial Development corporation, 1 Citizen Investment trust and 1 specialized merchant bank Elite Capital Limited in Nepal at the time of research. Thus all those financial institutions that are allowed to perform merchant banking activities as per the act can be regarded as population of the study.

Since the concept of merchant banking is very new to our country only very few financial institutions are found to be performing specific merchant banking activities. Thus out of all those financial institutions three leading companies actively involve in merchant banking functions and one specialized company are taken as sample to conduct there research. They are;

- Citizen Investment Trust (CIT)
- NIDC Capital Markets Limited (NCML)
- Nepal Merchant Banking & Finance Limited (NMB)
- Elite Capital Limited

3.4 Natures and source of Data

This study is based on primary as well as secondary data which are collected from various sources as per their requirement. The detail of the sources of primary and secondary data is given below.

1. Primary Data

The primary data are those, which are collected fresh and for the first time and thus happen to be original in character. Logical aspect of the study I explored mainly through primary data, which is collected using questionnaire and observation survey. For this purpose a set of scheduled questionnaire is developed and distributed to various groups like executives and officers. Similarly observation of merchant banking activities of few institutions is conducted as far as possible. Formal and informal interviews with the concerned authorities were also helpful to ascertain reliable and accurate information regarding merchant banking.

2. Secondary Data

“The secondary data are those which have already been collected by some one else and already, been passed through the statistical process.” **(Kothari, 1994: 115)** The secondary data has been collected from published materials of different organizations such as Nepal Rastra bank, Securities Exchange Board of Nepal, financial Institutions and Citizen Investment Trust. Likewise various data and information are collected from the official websites of the concerned companies, economic journals, periodicals, bulletins, magazines, other published and unpublished reports and documents from various sources.

3.5 Method of Data Collection

In the process of collecting primary data, the methods like telephone enquiry, formal and informal interview and questionnaire analysis are adopted wherever necessary. The formal as well as informal interviews are conducted with high-level personnel of various fields.

As far a questionnaire method is concerned, a set of questionnaire is developed to meet the objective of the study. A number of questions were put up by means of three types namely yes/no questions, multiple-

choice questions and free opinion questions. The questionnaires included seven tick mark questions and three open-end questions and are distributed to the executives of various professions and fields.

Categories of Respondents of various field	Number	%
NRB	3	8%
Banks	9	23%
finance Companies	10	25%
CIT	2	5%
Securities Exchange Board of Nepal	3	8%
nepal Stock Exchange	1	3%
NIDC	1	3%
Chartered Accountants	6	15%
Teacher	1	3%
Elite Capital	4	10%
Total	40	100%

On the other hand secondary data are collected using methods like frequent visit of various libraries, organizations and websites. Library of Shanker Dev Campus, Tribhuvan University, Indian Library, American Library, British Council and even Nepal Rastra Bank and Securities Exchange board of Nepal helped as source for various useful books, journals, magazines and other published and unpublished reports.

Data are collected through annual reports, minutes, memorandum of association of several organizations and direct visit to Nepal Rastra bank, Securities Exchange board of Nepal, Banks, Finance companies and other organizations. Concept paper amide by few organizations,

newsletters, leaflet, bulletin, and brochure also helped in collection of data for the study.

Similarly methods like surfing in websites and personal visit to books shops like National Book Shop, Ratna Pustak Bhandar, and Bhrikuti Book Palace are also used for the collection of data and information.

3.6 Method of Analysis and Presentation

Data collected from secondary sources were analyzed by using various statistical tools like percentage analysis, ratio analysis, bar diagram, multiple a bar diagram, arithmetic mean, standard deviation, coefficient of variation etc. Similarly data collected from questionnaires were in raw form. They were classified and tabulated in the required form and analyzed through tool using percentile. Major findings were based on the analysis and interpretation of data. The major data analysis tools used of the analysis and presentations of data are as follow:

3.6.1 Percentage Analysis

The percentage analysis is done to compare the two or more data for general information. One can use this function to establish a threshold of acceptance. It is used as method to divide the opinions of the related sectors into two or more sectors.

3.6.2 Ratio Analysis

Ratio is the mathematical relationship between two accounting figures. “Ratio analysis is a part of the whole process of analysis of financial statements of any business or industrial concern especially to take output and credit decisions.” Thus, ratio analysis is used to compare a firm’s or to it overtime. The qualitative judgments regarding financial performance of a firm can be done with the help of ration analysis.

3.6.3 Bar Diagram

As far as bar diagram is concerned, simple as well as multiple bar diagram are being used for the purpose of the study. Simple bar diagram is a diagram for only one variable. It is used for the comparative study of two or more values of a single variable. On the other hand multiple bar diagram is used when two or more variables are to be compared at the same time.

3.6.4 Arithmetic Mean

Arithmetic mean is the sum of all the observations divided by the number of observations. The arithmetic mean is denoted by (\bar{X}) . It is computed as:

$$\text{In symbol, Arithmetic mean } (\bar{X}) = \frac{\sum X}{N}$$

Where, $\sum X$ = Sum of total value of observations

N= Number of observations

3.6.5 Standard Deviation

The standard deviation is the most important and widely used measure of dispersion or variability. The standard deviation is the square root of mean squared from the arithmetic mean and is denoted by S.D or σ . The standard deviation is also called “root-mean-squared-deviation” (R.M.S.D)

$$\text{Thus, for individual observations, } \sigma = \sqrt{\frac{1}{N} \sum (X - \bar{X})^2}$$

3.6.6 Coefficient of Variation

The coefficient of variation (C.V) is the relative measure based on the standard deviation and is defined as the ratio of the standard deviation to the mean expressed in percent.

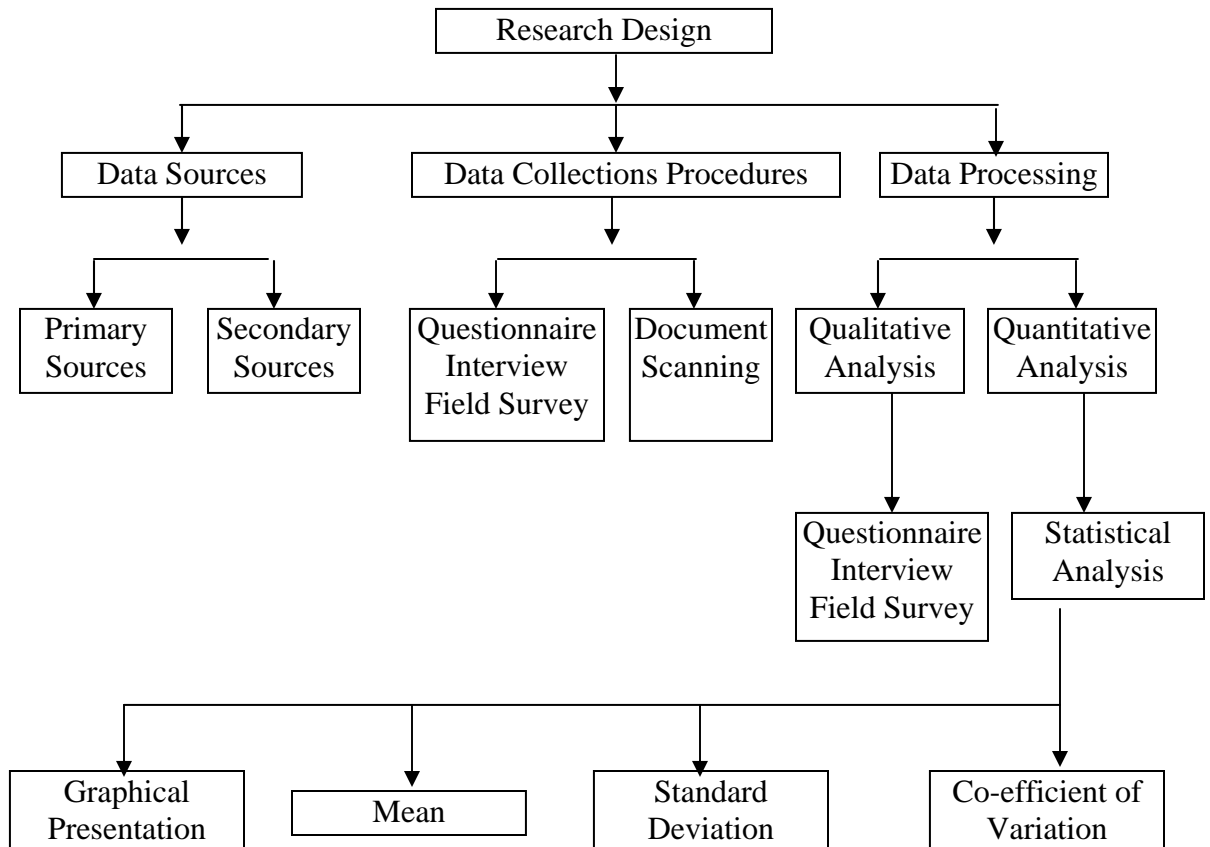
$$\text{In symbols, C.V} = \frac{\sigma * 100}{X}$$

The ratio is called the coefficient of standard deviation. It is obvious that C.V is independent of units. Hence the coefficient of variation is a suitable measure of comparing variability of two series (or set of data or distributions) with the same of different units. A series with smaller C.V. is said to be less variable (or more consistent or more homogeneous or more uniform or more stable) than other and the series with greater C.V. is said to be more variable (or less consistent or less homogeneous or less stable) than other.

3.7 Limitations of the Methodology

As the research in this topic is new, various difficulties and lack of proper knowledge in this particular subject make it comprehensive to achieve the objective. Due to the short period of time and other factors, all the methodologies applicable for the study are not applied. Therefore, in some cases assumption has been made to analyze those results comparatively with the view that it will not hampered the main stream of the study.

Research Methodology in Single Schematic Diagram is shown as follows:



CHAPTER IV

DATA PRESENTATION AND ANALYSIS

4.3 Introduction

Data presentation & analysis is the one of the important part of the research work. The basic objective of this chapter is to analyze and elucidate the collected data following the conversion of unprocessed data to an understandable presentation. Thus, this chapter presents the analysis and interpretation of the data related to merchant banking.

As it has been stated earlier in the Methodology section, this study consists of both primary as well as secondary data. Secondary data have been collected particularly from annual report of merchant bankers, securities Exchange Board of Nepal, websites and handouts prepared by the concerned companies. Similarly, data collected from primary sources (interview and questionnaire method have been analyzed to gather information on problems and remedies form merchant banking.

4.4 Presentation and Analysis of Secondary Data

Since most of the merchant banking activities in Nepal are performed by Finance Companies, our study starts from analysis of selected finance companies, which are actively participated, in merchant banking activities study of Citizen Investment Trust is also included here though it is excluded from the list of finance companies because its performance as merchant banking activities is high. Main sources of secondary data are Library, Magazine, and Newspaper etc.

This section provides interpretation and analysis of secondary data. Thus this section is exclusively devoted for the analysis of activity performance of leading merchant bankers in the context of Nepal.

4.4.1 Public issue analysis

Though the function of merchant banking includes a lot of activities, in case of our country the function of Merchant Banking is regarded as issue management. Thus, the analysis starts from the analysis of public issue of securities.

Public issue helps to develop capital market, which provides an important base for the development of industry, commerce and the economy. As the public issue goes on increasing the role and importance of merchant banks also increases for the reason that merchant bankers manage public issues in professional and systematic way. Tabular as well as graphical presentations of public issue in different fiscal years are presented in table no 1 and figure no. 1 as follow.

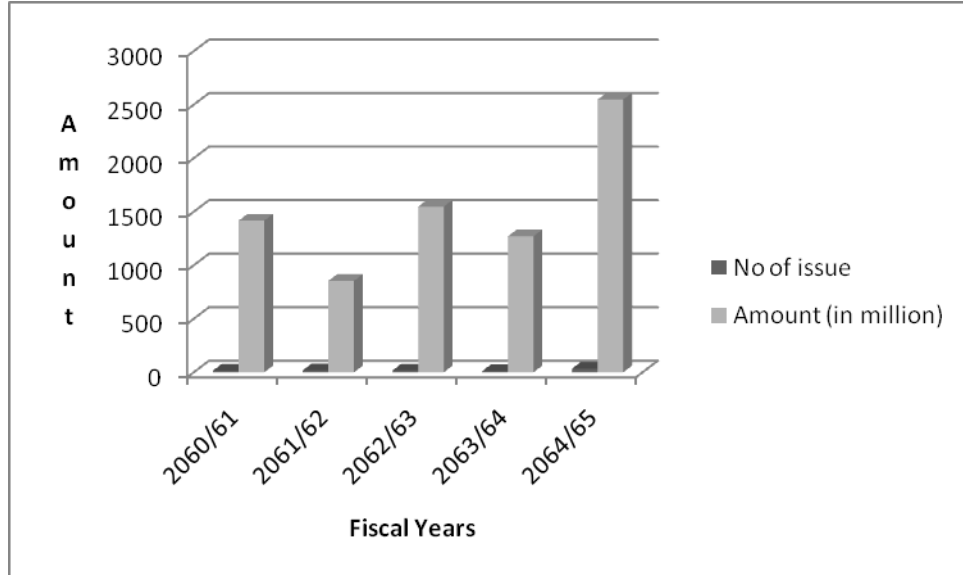
Table No 4.1

Public Issue of Securities

Fiscal Year	No of issue	Amount (in million)
2060/61	16	1416.63
2061/62	18	853.83
2062/63	17	1547.79
2063/64	12	1270.31
2064/65	34	2547.89
Total	129	7636.45

Source: Annual Report of NEPSE

Figure No 4.1



There have been 129 public issues of different companies amounting Rs. 10752.69 million till the fiscal year 2064/65. Out of 129 issues 16 were is fiscal year 058/59. The numbers of issues have been increased in the fiscal year 059/060 to 18 but the issue amount decreased from Rs1416.03 million to Rs 853.83 million. In the fiscal year 060/61 the no. of issue decreased to 17 but the issue amount increased to Rs 1547.79 million. In 061/62 the no. of issue and amount of issue both decreased to 12 and Rs 1270.31 million respectively. Similarly, in fiscal year 062/63 both number of issue and issue amount increase to 34 and Rs 2547.87 million respectively (highest among the reviewed period).

4.4.2 Institutions wise and instrument wise analysis of public issue

The institution wise analysis of public issues has been conducted to find out the sectors, which are benefited through merchant banking activities in the process activities in the process of public issue of securities. Similarly instrument wise public issue analysis helps to find out the instruments that have been preferred during the issue of securities.

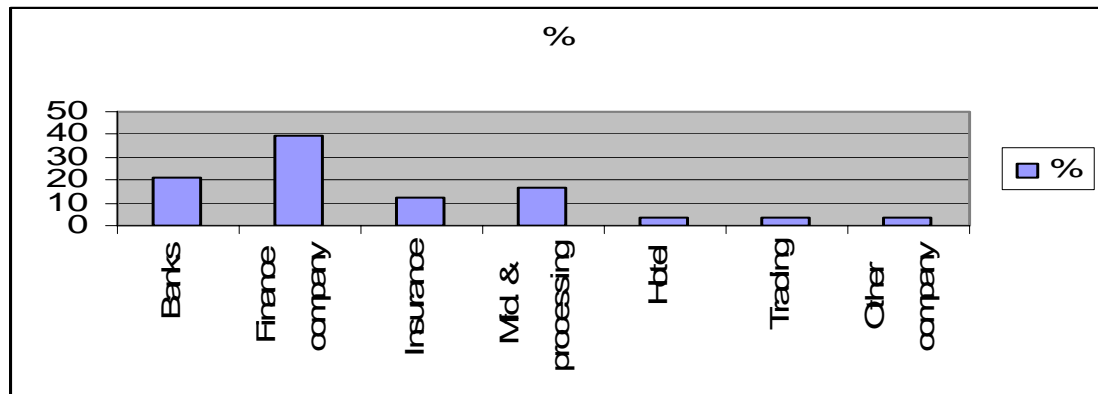
Table No 4.2

Institute Wise Public Issue in percentage

Group	No of issue	%
Banks	27	20.93
Finance company	51	39.53
Insurance	16	12.4
Mfd. & processing	21	16.28
Hotel	4	3.1
Trading	5	3.87
Other company	5	3.88
	129	

Source: Annual Report of NEPSE

Figure No 4.2



Above table and figure no. 2 shows the institute wise public issue till 2064/65. From the table it has been clear that most of the public issues during the period are of finance company, which is 39.53% as compared to 20.93% of banks, 12.40% public issue of insurance companies 16.28% of manufacturing companies, 3.10% of hotel, 3.87% of trading companies and 3.88% of other companies.

Table No 4.3

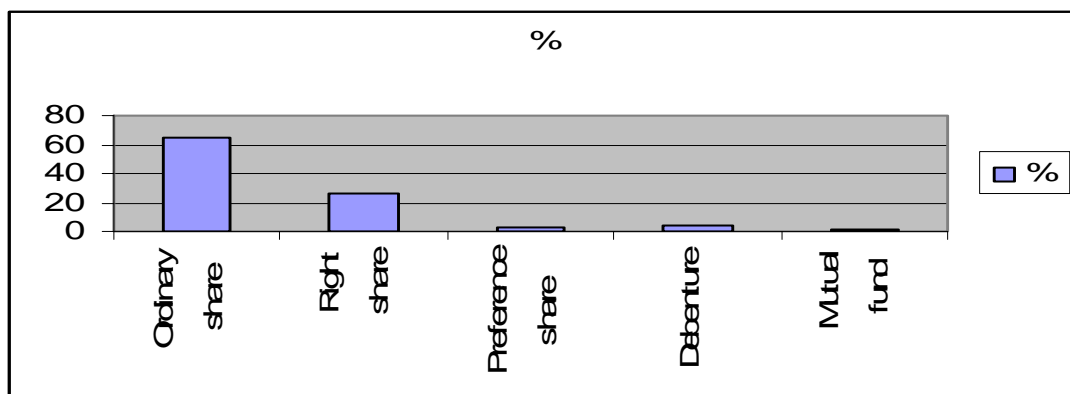
Instrument Wise Public Issue

Instrument	No of issue	%
Ordinary share	114	64.77
Right share	47	26.7
Preference share	4	2.27
Debenture	8	4.54
Mutual fund	3	1.7
	176	

Source: Annual Report of NEPSE

Figure No 4.3

Instrument Wise Public Issue



From table and figure no. 3, it is clear that the major sources of finance for most of the corporate bodies in Nepal are ordinary share. 64.77% of issues were through ordinary shares. The numbers of issues through ordinary shares were 114. Right shares were issued of 47 companies that

covered 26.70% of total issue. After this mostly issued instrument to raise capital was debenture, preference share and mutual/unit fund which were 4.54%, 2.27% and 1.70% respectively.

4.4.3 Merchant Bankers: Activity Performance

a. Elite Capital Limited

The Elite Capital Limited was incorporated in May 2008 as the first specialized merchant banking company in the history of Nepalese capital market. The Company was promoted by eminent businessman, bankers, chartered accountants, lawyers etc. The Company was incorporated under the Nepalese Companies Act 2007 and licensed by the Securities Board of Nepal under the Securities Act, 2007 to undertake merchant banking activities (Issue Management and Registrar to Shares). The Company has commenced its operations from August 2008.

The Elite Capital Limited provides various services to individuals and corporate for their resources management. The company is organized in three primary business lines; the issue manager, the registrar of shares and the consultancy services. The registrar of shares division provides share registration service for various company listed in the Nepal Stock exchange Limited, the issue management division manages the initial public offering and rights issue of shares by the corporate and the consultancy division provides the consultancy services for financial planning, asset management, feasibility study report, assets valuations etc.

The Company is committed to provide various services relating to the securities market to its customer. The Company offers various value added and investor awareness information to the general investors in the securities market. The Company has set out the objective of reaching out

to the common investor and the client specific products and services that would be helpful to them in their path to prosperity. The Company is confident to execute its objective efficiently by offering high quality and cost-effective services. The company operates in a highly automated environment in terms of information technology and communication systems, which enable it to offer speedy & cost effective services to the clients. The company made substantial effort and investment in acquiring the best technology available in the industry.

BUSINESS STRATEGY

o Short term Strategy

The Company will start with as a public issue manager and share registration. The Company is promoted by the banker, businessman, lawyer & chartered accountants and managed by the team of young, energetic and professional people. The Company will approach to the various companies who are preparing for the initial public issue or rights issues or any other debt instrument for the management of these issues. The listed company can outsource their share transfer related work to the merchant banker. Therefore, the Company will also approach to the listed companies to act as a share transfer agent for them.

o Long term Strategy

In the long run, the Company will start portfolio management services, underwriting of shares and securities, market maker, management of the mutual fund, central depository service, clearing house for securities transactions, consultancy services to the corporate for financial, managerial, capital restructuring, merger, acquisition & takeover etc.

Issues made by the Elite during the period

Company	Nature of security	No of security issued
Phewa Finance	Right Share	18200

Prabhu Finance	Right Share	80000
Ace Development Bank	Right Share	292864
Narayani Development Bank	Right Share	10000

b. Citizen Investment Trust (CIT)

Citizen Investment Trust (CIT) is incorporated under Citizen Investment Trust Act, 1990 with a view to expand investment opportunities encouraging general public to save capital and to bring the dynamism in the development of capital markets. CIT is basically the savings and investment institution and it statutorily derives a special status and privileges, which adds up its strength to emerge as a national institution reaching wider spectrum of the population. CIT, at the same time, achieves a high professionalism in the financial intermediation and has an ability to provide varied capital market services.

The major function of CIT includes saving mobilization, investment/financing, and capital market services. Under capital market service, it provides trustee services and corporate finance services. And merchant-banking service consists under corporate finance services. Out of various merchant-banking services, the services provided by CIT are as follow:

1. Public Issue Management:

As one of the major function of merchant banking, CIT has been actively participating in management of public issue of securities from its establishment. It has managed public issued of ordinary shares of various companies like banks, finance companies, manufacturing industries and others. CIT has introduced unit scheme of its own institution. It has issued preference share and right share of various companies. The no and issue amount of the issues managed by CIT is shown in table and figure below.

Table No 4.4

Public Issue Managed by CIT

Fiscal Year	CIT		Total		% (amount)
	No	Amount	No	amount	
2060/61	2	59.3	16	1416.63	4.19
2061/62	3	272.5	18	853.83	31.91
2062/63	1	150	17	1547.79	9.69
2063/64	3	565.41	12	1270.31	44.51
2064/65	3	257.5	34	2547.89	10.1
	12	1304.71	97	7636.45	17.08529

Source: Annual Report of CIT

Figure No 4.4

Public Issue Managed by CIT

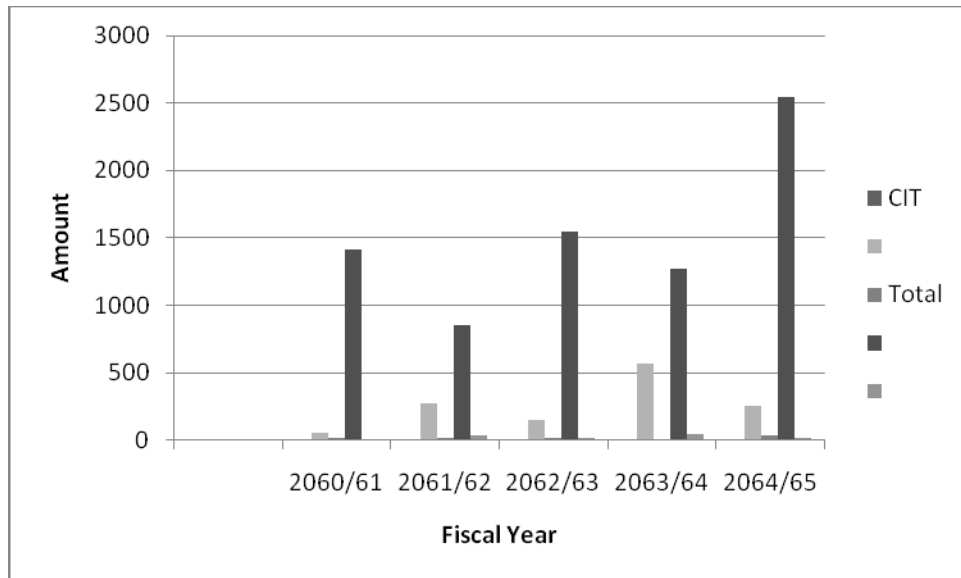


Table no. 4 show the performance of CIT as an issue manager of different companies during different fiscal year 2060/61 to 2064/65. During the five year period, the company has managed to raise Rs. 1304.71 million capitals of 12 different issuing companies that are 17.09% of aggregate public issue. The management of public issue was greatest in the fiscal year 2063/64 that covers 44.51% of total issue approved in the fiscal year.

a. Underwriting & syndication of underwriting public issue

Citizen Investment Trust also provided the service of underwriting as well as syndication of underwriting public issue of various companies.

CIT has underwritten public issue of four companies from fiscal year 2060/61 to 2064/65 out of which it has syndicated underwriting of 2 companies. The amount of underwriting was ranging from Rs. Ten Lakh to Rs. Seventy Lakhs.

b. Registrar to Share:

CIT, as one of the leading merchant banker is also providing service to registrar to share to Alliance Company Limited.

c. Consultancy Service:

CIT also provides consultancy services in the area of capital markets. Such services are available for designing capital structure, pricing of securities, corporate acts like merger, acquisition, privatization & other related activities.

c. NIDC Capital Markets Limited (NCML)

NIDC Capital Markets was established in 2049 BS as a first merchant banker in Nepal. When established, it was only merchant banker with an objective to render the merchant banking services. As a merchant banker, it also provides various services to its clients. The activities of NIDC capital market is to act as an issue and sales manager, to provide advice for it and arrange underwriting for public issues, to encourage public participation in the ownership of industrial and commercial institution, collecting medium or long term capital from public for the establishment and the expansion of industry. Besides these activities, it also has an active role to provide liquidity to securities, as a market maker involving itself actively in buying and selling of securities in the secondary market.

a. Issue management

NIDC Capital markets have handled public issue of various companies. During the five years of period from fiscal year 2060/61 to 2064/65, it has managed a lot of issues of ordinary shares, right shares, debentures and preference shares of various companies. The

brief detail of public issue handled by NIDC Capital Markets Limited is shown in the table no. 5

Table No 4.5

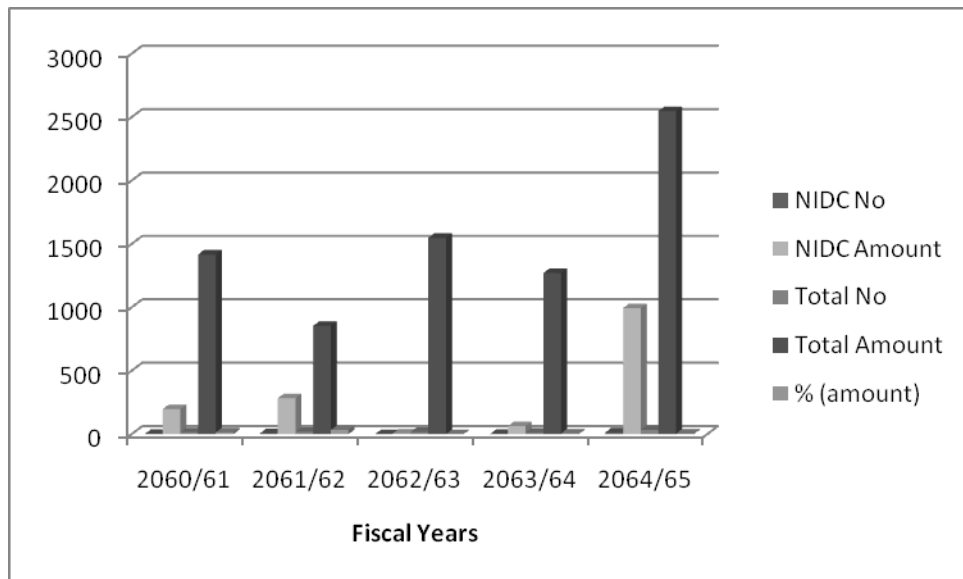
Public Issue Managed by NIDC Capital Market

Fiscal Year	NIDC		Total		% (amount)
	No	Amount	No	Amount	
2060/61	2	197.46	16	1416.63	13.93871
2061/62	7	283.24	18	853.83	33.17
2062/63	1	6	17	1547.79	0.003
2063/64	2	63.2	12	1270.31	4.98
2064/65	14	993.87	34	2547.89	3.9
	26	1543.77	97	7636.45	20.21581

Source: Annual Report of NIDC

Figure No 4.5

Public Issue Managed by NIDC Capital Market



From the table no. 5, it is clear that it has handled public issue of 26 companies amounting Rs. 1543.44 million, which is 20.22% of total issue. It has managed issue of Rs. 197.46 million of 2 companies in

fiscal year 2060/61 which is 13.96% of the total issue of that fiscal year. Similarly it has managed 33.17%, 0.003%, 4.98%, 3.90% in fiscal year 059/60, 060/61, 061/62 and 062/63 respectively. It would be easier to understand if we study the amount in figure, which is shown above.

b. Underwriting

Out of 26 issues handled by NIDC Capital Markets Limited, it has underwritten public issue of 7 companies from fiscal year 2060/61 to 2064/65.

c. Registrar to the share

NIDC Capital Market also provides service of registrar to the share service with an objective to provide help in the further activities of public Limited Companies. Its main objective is to maintain the record of shareholders, to fulfill the name transferring process and to assist in holding the preliminary and Annual General Meeting to behalf of those companies. Following are the list of companies to which, NIDC capital markets Limited provides services of registrar to share issue.

- Nepal Lever Limited
- Nepal Industrial & Commercial Bank Limited
- Orientals Hotels Limited. (Radisson)
- Life Insurance Company Limited
- Bhrikuti Paper Industry Limited
- Nepal Film Development board

d. Mutual Fund

NIDC Capital Market has also started NCM Mutual Fund from 2050 with approval of Securities Exchange board of Nepal. The total amount of the mutual fund was Rs. 100.00 million. It was an open-ended fund with a pare value of Rs. 10 per unit.

Table No 4.6

Performance of NCM Mutual Fund

Rs in million

S.N	Particulars	Fiscal Year			
		2061/62	2062/63	2063/64	2064/65
1	Investment(Rs)	72.56	72.56	72.563	73.288
2	No of invested co	27	27	27	27
3	Net assets value(Rs)	53.128	73.307	113.092	112.445
4	Net assets value per unit (Rs)	10.12	13.97	21.55	21.42
5	outstanding units	5250000	5250000	5250000	5250000
6	Face value(Rs)	52.5	52.5	52.5	52.5
7	No of unit holders	517	517	517	517

Public Issue Managed by NIDC Capital Market

Thus NIDC capital Markets has invested in 27 companies from the amount raised from 517 unit holders amounting Rs. 72.560 million in fiscal year 2061/62 and 2062/63 which increased to 72.563 million in 2063/64 and to Rs. 73.288 million in 2064/65. NIDC Capital Markets Ltd. Was successful to increase the net asset value per unit from Rs. 10.12 in fiscal year 2061/62 and to Rs. 21.42 per unit in the fiscal year 2064/65.

e. Portfolio Management

The company had managed portfolio of its customer with and objective to provide attractive returns from the deposited amount by buying and selling of securities in fiscal year 2051/52 but it had to leave in next fiscal years due to some problems.

f. Research and Development

The company has improved this service by analyzing in depth the economic situation of listed companies and has also started to prepare macro economic sector analysis; whereby sectors of investment possibilities are researched. These sectors include Textile with analysis on the area of cotton thread, garments and knitwear as well as tourism.

d. Nepal Merchant Banking & Finance Limited (NMB)

NMB commenced business in December 1996. The company is trying to become a leader in their market for financial services and merchant banking activities. NMB is involved in both primary and secondary markets. Under merchant banking activities it performs various activities.

a. Public Issue Management

NMB has successfully managed Initial Public Offering (IPO) of both common and preferred shares as Lead Managers of different companies. Table 9 shows the detail of public issue handled by NMB.

Table No 4.7

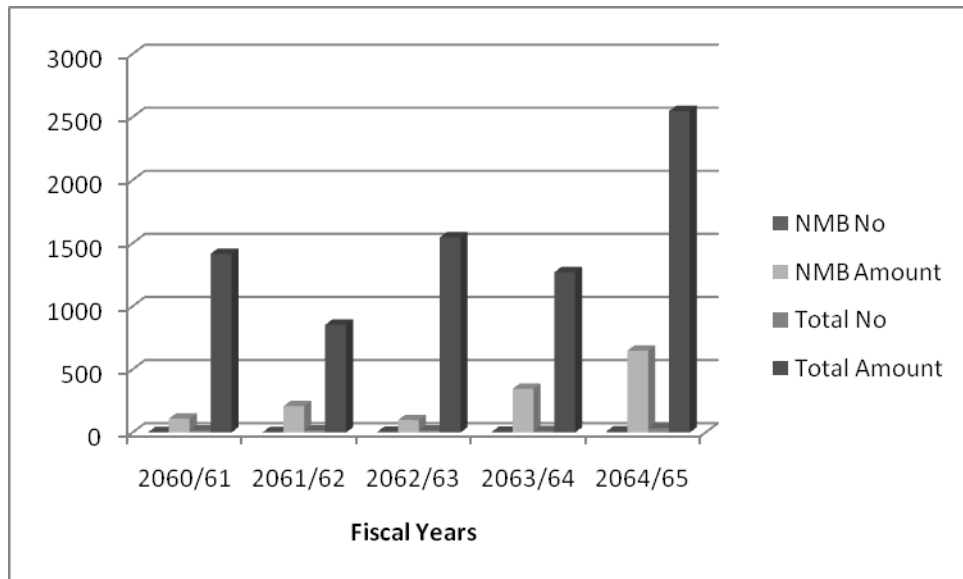
Public Issue Managed by NMB

Fiscal Year	NMB		Total		% (Amount)
	No	Amount	No	Amount	
2060/61	3	110	16	1416.63	7.77
2061/62	3	209	18	853.83	24.48
2062/63	6	99	17	1547.79	6.4
2063/64	6	346.41	12	1270.31	27.27
2064/65	10	648.5	34	2547.89	25.47
	28	1412.91	97	7636.45	18.50218

Source: Annual Report of NMB

Figure No 4.7

Public Issue Managed by NMB



From the table no. 7, it is clear that it has handled public issue of 28 companies amounting Rs. 1412.91 million, which is 18.50% of total issue. It has managed issue of Rs. 110 million of 3 companies in fiscal year 2060/61 which is 7.77% of the total issue of that fiscal year. Similarly it has managed 24.48%, 6.40%, 27.27%, 25.47% in fiscal year 059/60, 060/61, 061/62 and 062/63 respectively. It would be easier to understand if were study the amount in figure, which is shown above.

b. Underwriting of Public Issue

NMB has underwritten public issue of shares of two issuing companies naming Nepal Development Bank Limited and Development Credit Bank Limited amounting Rs. Seventy Lakhs each.

c. Registrar to Share Issue

It also provides share registrar functions to business and corporations. NMB was actively involved in the management of share registrar of two important commercial banks NABIL Bank Ltd. And Standard Chartered bank Ltd. At present it provides this service to NABIL Bank Ltd. Only.

d. Corporate Counseling

NMB under Corporate Finance Division is primarily also involved in providing necessary project evaluation for NMB itself and its clients. The services of this division range from project analysis to corporate Mergers & Acquisitions to debt finance and Equity Finance. It is also involved in consortium financing and project appraisal. This department has prepared detailed feasibility study report of a commercial bank and industrial ventures including for a joint venture project. Further, it has played key roles in arranging consortium financing. Further, this department also played an important role in the preparation of documentation for the privatization bid of Nepal Tea Development Corporation.

4.4.4 Analysis of Income from Merchant Banking

Generation of income is the major objective of each and every company without which survival and growth of a company is out of imagination. Income from each and every activity affects the performance of the company. Thus, in this sectional, it has been tried to analyzed and find

out the income from merchant banking activities to the merchant bankers.

a. Merchant Banking income of Citizen Investment Trust

Citizen Investment Trust is earning income from various merchant-banking activities like commission of share issue management, underwriting, registrar to share issue, consultancy, sale of government bond etc. The merchant banking income of Citizen Investment trust from the fiscal year 2058/059 in comparison to total income is shown in the table no. 8.

Table No 4.8

Statement of Income of CIT

In Million

Fiscal year	Share Issue Mgmt.	Underwriting Commission	Registration Fee	Commission From sale of Govt. Bond	Total Income from Merchant Banking	Total Income	% of Merchant banking income to Total income
2060/61	1.836	0.062	-	1.223	3.121	7.517	41.52
2061/62	0.437	-	-	0.855	1.292	7.720	16.74

2062/63	0.846	-	-	0.588	1.434	10.552	13.59
2063/64	0.847	0.037	0.043	0.347	1.272	14.395	8.85
2064/65	1.460	0.233	0.206	0.128	2.027	14.673	13.81

Source: Annual Report of CIT

From the above table it has been come to know that the merchant banking income of CIT in fiscal year 2060/61 was Rs. 3.121 million while it has decreased to Rs. 1.292 million in fiscal year 2061/62 and increased to Rs. 1.434 million in fiscal year 2062/63. CIT seems to be able to earn maximum amount of merchant banking income in the fiscal year 2060/61 which was 41.52% of total income. However the income decreased in next four consecutive years. From the table it is also clear that CIT is earning more than 10% of income in average from merchant banking activities. And, the company is able to earn commission from share issue management and sale of government bond regularly it has started to earn commission from registrar to share issue and underwriting of share from the fiscal year 2063/64 however it has also earned commission from underwriting from fiscal year 2063/64. The comparative graph of merchant banking income and ratio of total income and merchant banking income of CIT is shown in the chart below and the income from other activities is very nominal.

Figure No 4.8 (a)

Merchant Banking Income of CIT

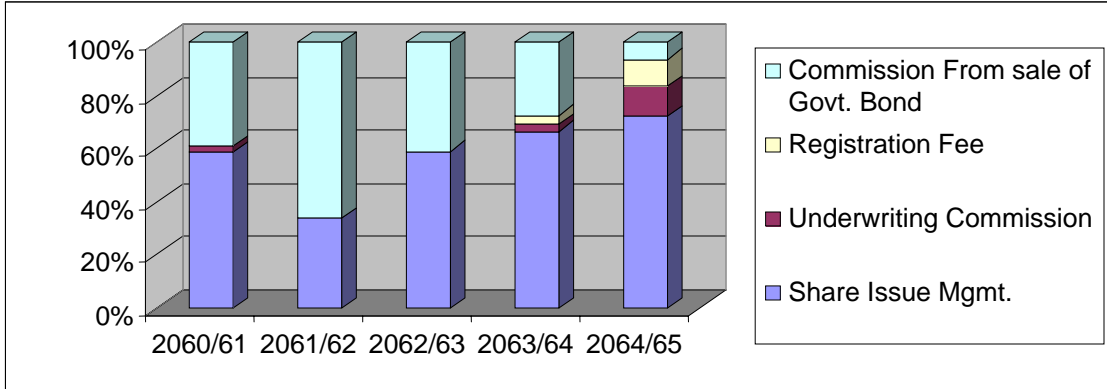
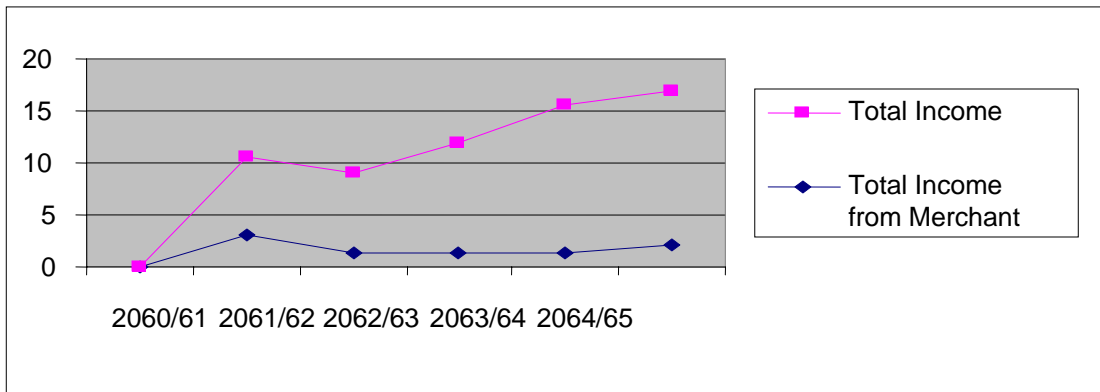


Figure No 4.8 (b)



Similarly the figure no. 8(b) shows that merchant banking income of CIT is not increasing in proportion to the total income.

b. Merchant Banking income of NIDC Capital Market Ltd.

The analysis of merchant banking income of NIDC capital market forms various activities in various fiscal years is shown in the table no. 9.

Table No 4.9

Income of NIDC Capital Market Ltd.

Fiscal year	Share Issue Mgmt.	Underwriting Commission	Registration Fee	Commission From sale of Govt. Bond	Total Income from Merchant Banking	Total Income	% of Merchant banking income to Total income
2060/61	0.656	0.865	0.60	0.043	2.163	12.644	17.11
2061/62	0.391	-	0.377	0.014	0.782	21.823	3.58
2062/63	1.160	-	0.682	0.179	2.021	34.275	5.9
2063/64	1.870	0.895	1.614	0.085	4.464	50.953	8.76
2064/65	2.170	0.197	1.055	0.012	3.435	58.250	5.90

Source: Annual Report of NIDC Capital Market

From the above table it is clear that most of the merchant banking income are from issue management and then from share registrar and underwriting commission. Similarly NIDC Capital Markets is earning from sale of government bond. Thus the total income from merchant banking is not found to be constant for NIDC capital markets Limited. Similarly the activity has contributed to total income by 17.11%, 3.58%, 5.90, 8.76% and 5.90% in the fiscal year 2060/61, 2061/62, 2062/63, 2063/64 and 2064/65 respectively. The table also shows that the merchant banking income of NIDC capital Markets Ltd. is zigzag and not being able to increase simultaneously with the increase in total income.

Figure No 4.9(a)

Merchant banking Income of NIDC Capital Market

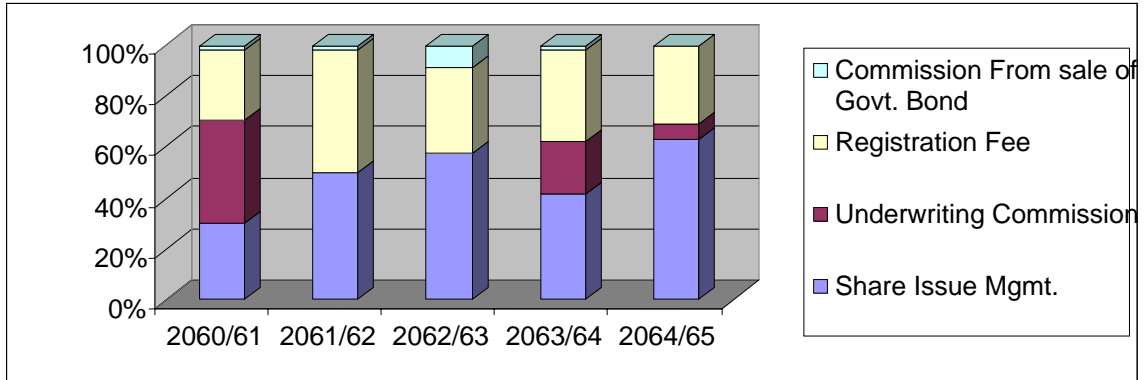
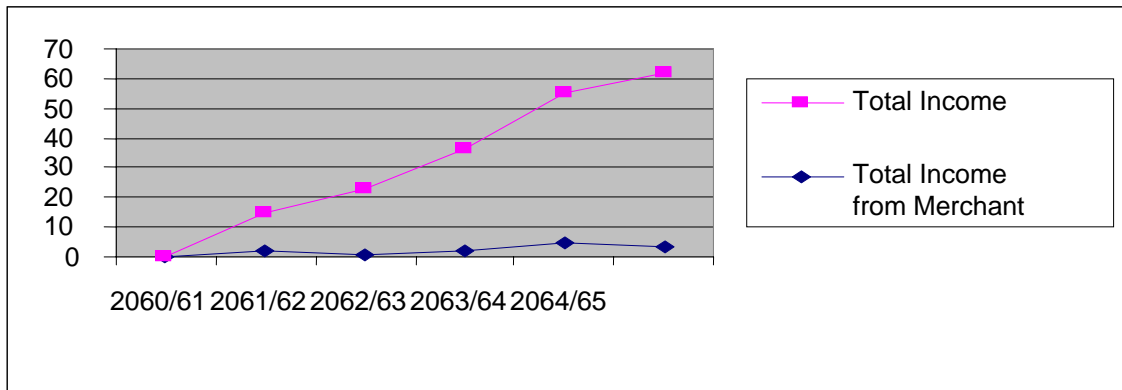


Figure No 9(a) Shows that NIDC capital Markets Limited is earning most of the merchant banking income through from share issue management and then from registrar to share issue and from underwriting commission. Similarly Figure No 9(b) shows that the company is not being able to earn from merchant banking activities as it is earning from other activities.

Figure no 9(b)



c. Merchant Banking income of Nepal Merchant Banking & Finance Ltd.

The analysis of income of the company as compared to its total income has been presented in the table no. 10

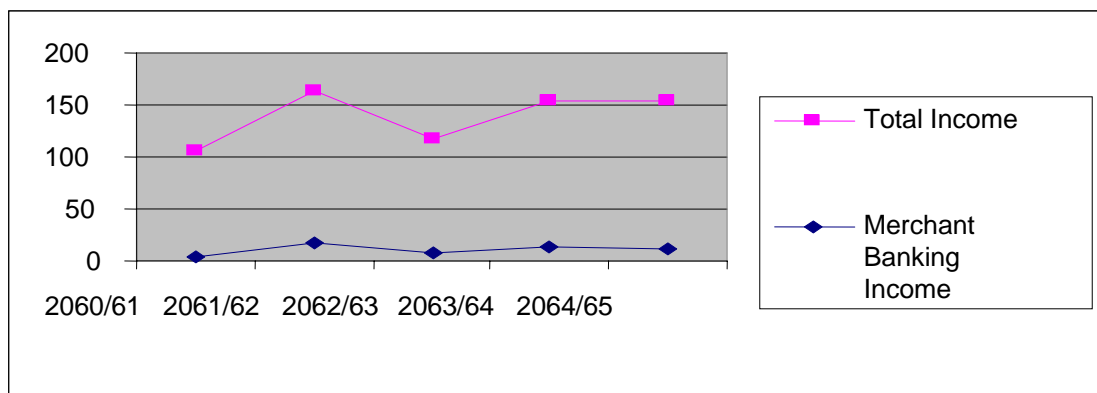
Table No 4.10

Income of NMB

Fiscal Year	Merchant Banking Income	Total Income	% of Income from Merchant Banking to Total Income
2060/61	3.158	103.198	3.06
2061/62	18.199	145.744	12.49
2062/63	8.379	108.78	7.72
2063/64	12.887	141.182	9.13
2064/65	12.485	141.343	8.83

Source: Annual Report of NMB

Figure No 4.10



Above figure and table shows that the merchant banking income of NMB was Rs. 3.158 million in fiscal year 2060/61 which was 3.06% of total income which increased to Rs. 18.199 million in fiscal year

2061/62 generating 12.49% tot total income. The income, however, decreased to Rs. 8.397 million in fiscal year 2062/63 making contribution of 7.72% to total income which increased to Rs. 12.887 million and Rs. 12.485 million making contribution of 9.13% and 8.83% of total income respectively in fiscal year 2063/64 and 2064/65.

4.4.5 Comparative Study of Income from Merchant Banking

This study ahs been conducted to study the income generated by various companies performing merchant–banking activities comparatively. The comparative table as well as chart of the merchant banking income is as follow:

Table No 4.11

Merchant banking Income of Various Companies

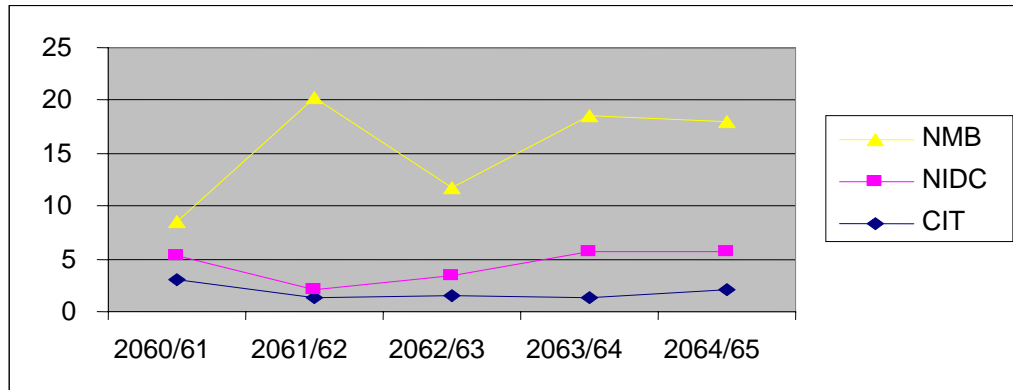
Rs in
Million

Fiscal Year	CIT	NIDC	NMB
2060/61	3.121	2.163	3.158
2061/62	1.292	0.782	18.199
2062/63	1.434	2.021	8.379
2063/64	1.272	4.464	12.887
2064/65	2.165	3.435	12.485

Source: Annual Report of NIDC Capital Market, NMB CIT

Figure No 4.11

Comparative figure of income of Merchant Banks



From the analysis of above table merchant banking income are not consistent of these institutions. NMB is younger than CIT and NIDC but its performance in term of earning is much higher in comparison to CIT and NIDC.

4.4.6 Test of consistency of Merchant Banking Income

Here, the attempt has been made to test the consistency of merchant banking income. The result of analysis obtained using statistical tools mean (\bar{x}), standard deviation (σ), co-efficient of variation (C.V) is given in the table 12.

Table No 4.12

Test of consistency of Merchant Banking Income

Rs. In Million

Tools	CIT	NIDC Capital Markets	NMB
Mean (\bar{X})	1.8572	2.573	11.0252
S.D (σ)	0.711422	1.264864	5.01719
C.V	0.383061	0.491591	0.455066

Source: Annual Report of NIDC Capital Market, NMB CIT

From the table, it is clear that the mean merchant banking income of Nepal Merchant Banking & Finance Ltd. is the highest among the three companies, which is Rs. 11.03 million. The merchant banking income of Citizen Investment Trust is Rs. 1.8752 million and that of NIDC Capital markets Ltd. is Rs. 2.573 million. As far as standard deviation of income is concerned the merchant banking income of Citizen Investment Trust has been found less dispersed as compared to other companies. The standard deviation of merchant banking income is Rs. 0.71142 million, Rs. 1.2648 million and Rs. 5.01719 million respectively of Citizen Investment Trust, NIDC Capital Markets Ltd and Nepal merchant Banking & Finance Ltd. Similarly when comparing the variation or the consistency of merchant banking income of three companies, the table shows that NIDC Capital Markets Ltd has high co-efficient of variation to 49.159%. The coefficient of variation of Citizen Investment Trust is 38.306% and that of Nepal Merchant banking & Finance Ltd. is 45.51%. Which means that the merchant banking income of Nepal Merchant Banking & Finance Ltd. has high consistency while that of NIDC Capital Markets Ltd. has less consistency comparing to other companies.

4.5 Presentations and analysis of Primary Data

Primary data plays the vital role to make the research task meaningful as well as concrete. In the course of availing first hand data, questionnaire analysis, formal and informal interview method have been adopted. Under questionnaire analysis, important question are set and provided to the related parties to take their opinion about merchant banking in Nepal. A number of questions were put up by means of 40 copies of questionnaire. Questionnaire format has been shown in appendix 1. The questionnaires so collected are related to find out on merchant banking. The responses from the respondents have been analyzed as follows:

4.5.1 Identification of Institutions involved in Merchant Banking

This first question tries to identify the institutions, which are involved in merchant banking activities. Regarding this question, it has been identified that the institutions involved in merchant banking activities are finance companies as 72.5% of respondents answered finance companies, 2.5% answered banks, 2.5% answered Citizen Investment Trust and remaining 22.5% respondents said not only finance companies but few banks and other institutions are actively participated in merchant banking function in Nepal. The table no 13 gives clear picture to the question.

Table No 4.13

Institutions participating activity in Merchant banking function

S.N	Research variable	No of Viewers	%of Viewers
a	Banks	1	2.5
b	Finance Companies	29	72.5
c	other Institutions (CIT)	1	2.5
d	All Above	9	22.5
	Total	40	100

Source: Annual Report of NIDC Capital Market, NMB and CIT

4.5.2 Regulatory Provisions Related to Merchant Banking Activities

This question has been asked to trace the specific rules, regulations and guidelines that would govern merchant banking activities. Concerning this question, 62.5% of respondents gave positive answer. According to them, the acts like company act, finance companies act, securities exchange act etc are the regulatory provision that regulates merchant banking activities in Nepal But 30% respondents rejected the view

regarding availability of specific rules, regulations and guidelines related to the topic while 7.5% of respondents are unknown about it.

Table No 4.14

Activity of Merchant banking Regulations

S.N	Research variable	No of Viewers	%of Viewers
A	Yes	25	62.5
B	No	12	30
c	Don't Know	3	7.5
	Total	40	100

4.5.3 Sufficiency of Merchant Banking Guidelines

As it has been come to know that merchant banks are under some acts like securities exchange act, company act, finance companies act etc., the question has been raised to find out whether these acts are sufficient for merchant banking functions or not. Regarding this question, 57.5% of respondents replied insufficient, 30% of respondents replied sufficient while 5% of respondents replied very sufficient and 7.5% of respondents replied that couldn't be said. Table no 15 shows the clear picture of the responses.

Table No 4.15

Sufficiency of merchant banking Regulations

S.N	Research variable	No of Viewers	%of Viewers
A	Very Sufficient	2	5
B	Sufficient	12	30
C	Insufficient	23	57.5

D	Can't say	3	7.5
	Total	40	100

Source: Annual Report of NIDC Capital Market, NMB CIT

4.5.4 Regulatory Body for Merchant Banking Activities

The question no 4 has been asked to find out the regulatory body for merchant banking. Regarding this question, there is a different answer from different respondents. According to 45% of respondents both Nepal Rastra Bank and Securities Exchange board of Nepal regulate merchant bankers. 30% of respondents replied Securities Exchange Board while 17.5% replied Nepal Rastra Bank and remaining 7.5% replied Nepal Rastra Bank and remaining 7.5% of respondents have said that it is not specified yet. The detail of the response is given in the table no 16 below.

Table No 4.16

Institutions participating activity in Merchant banking function

S.N	Research variable	No of Viewers	%of Viewers
A	Nepal Rastra Bank	7	17.5
B	Securities Exchange Board	12	30
c	Not Specific yet	3	7.5
D	Both NRB & SEBON	18	45
	Total	40	100

Source: Annual Report of NIDC Capital Market, NMB CIT

4.5.5 Development of capital Market

Merchant Bankers play an important role in the development of capital market. Similarly development of capital market also affects the development of merchant banking. Thus they are interrelated with each other. Here, this question is raised to find out the development position of capital market. Regarding this question 62.5% of respondents replied

underdeveloped, 32.5% of respondents replied moderate while only 5% of respondents replied that it is developed while none of the respondents replied the capital market to be fully developed. The details of the responses are presented in the table no. 17.

Table No 4.17

Position of Capital Market

S.N	Research variable	No of Viewers	%of Viewers
A	Fully Developed	0	0
B	Developed	2	5
C	Moderate	13	32.5
D	Underdeveloped	25	62.5
	Total	40	100

Source: Annual Report of NIDC Capital Market

4.5.6 Role Player for Merchant Banking Activities

As the word merchant banking is not familiar to everyone and is known by very few persons, this question has been asked to find out the main body that has to play a major role for the development of merchant banking activities. Regarding this question 12.5% of respondents said Nepal Rastra Bank, 15% respondents said Securities Exchange board of Nepal, 15% respondents said Merchant Banks itself have to play role for the development of merchant banks while 5% respondents said that both Securities Exchange Board of Nepal and Merchant Banks should jointly play role and 52.5% of respondents said not a single entity but all the parities should play their own role for merchant banking development. The brief summary of the responses are given in the table no 18.

Table No 4.18

Role Player of Merchant Banking

S.N	Research variable	No of Viewers	%of Viewers
A	NRB	5	12.5

B	SEBON	6	15
C	Merchant Bankers itself	6	15
D	SEBON & Merchant Banks	2	5
E	All Above	21	52.5
	Total	40	100

Source: Annual Report of NIDC Capital Market

4.5.7 Reason for more public issue of securities of Banks and Finance companies as compared to other Sectors

The institution wise public issue analysis reveals that most of the public issues prevailing in our country are of banks and finance companies. The issues of other sectors are very rare. Thus this question has been asked to find out the reason behind more public issue of bank and finance companies as compared to other sectors. The various responses from various respondents are shown in the table no. 19.

Table No 4.19

Reason for more public issue of banks and finance companies

S.N	Research variable	No of Viewers	%of Viewers
A	SEBON gives most of the approval to banks and finance companies	3	7.5
B	Other sector do not want to go for public issue	4	10
C	Public do not want to subscribe for share of other sectors in terms of return	9	22.5
D	Banks and finance companies need more capital than other sectors	2	5
E	Banks and finance companies have to go	22	55

	for public as per regulatory provision		
	Total	40	100

From the table no 19, it has been come to know that the closest reason behind more public issue of banks and finance companies is that banks and finance companies have to go for public issue as per regulatory provision. This answer was supported by 55% of respondents. 22.5% of respondents replied those publics do not want to subscribe share of other sectors in terms of return. According to the 10% of respondents, other sectors do not want to go for public issue. While 5% of respondents replied that banks and finance companies need more capital than other sectors.

4.5.8 Problems in the Performance of Merchant Banking Activities

This question has been raised to find out the concrete reason for the problems in the performance of merchant banking activities as it has been realized the lack of specific merchant bankers and sufficient merchant banking activities in our country. The question is also raised to high-level executives of different fields through questionnaire as well as formal and informal interview. Regarding this question various responses have been obtained through various respondents. The brief descriptions of the responses are as follow.

According to the most of the respondents the most important problem in the performance of merchant banking activities is lack of professionalism. There is less knowledge about not trained that is why they are not competent. The respondents also complained towards the conservative management style.

The majority of respondents also stated that the problem is also because of underdeveloped capital market, which generates low level of business opportunities and capital tools to investors and merchant bankers.

The respondents also seem to be unsatisfied toward the unclear policies and lack of proper and sufficient regulatory frame work that has absence of merchant banking guidelines. They are also not satisfied with unclear status between stock exchange and security board of Nepal and lack of co-ordination between different regulatory bodies and merchant banking itself.

The respondents also pointed out towards various problems like volatile political situation, unconscious investors, underdeveloped industries sectors, lack of strategic planning and implementation etc.

4.5.9 Reasons for Availability of Very Few Merchant Banking Services

According to the respondents the reasons for availability of very few merchant banking services are due to its problems in performance of merchant banking services. According to them merchant banking is in introductory stage in Nepal. That is why there is lack of knowledge among the corporate/individuals about the merchant banking services.

According to them though it is in its infancy government is also not playing incentive role. There is also lack of proper regulation and specific body to develop capital market and merchant banking. Similarly the respondents pointed out toward the slackness of economic and business activities in the country resulting low volume of business and opportunities and lack of modern technology, research and development related activities.

4.5.10 Improvements required for Boosting up Merchant Banking Activities in Nepal

The respondents gave a lot of suggestions for the improvement required for boosting up merchant banking activities in Nepal. According to the most of the respondents there should be clear-cut policies, guidelines specifying activities and role of merchant banking by regulatory authority. They create an environment for industrialization in Nepal and also should attract foreign investment in the local market.

Management should have clear business vision, financial discipline and good corporate culture. Level of specialization should be developed in the area of merchant banking and capital market. There should be provision of incentive to investors to invest in capital market and institutions to float their shares and other financial tools in the market. There should maintain transparent accounts by business to win public confidence so as to attract more public scripts for issue.

The respondents also stressed for political stability, public awareness programs to train more people and create awareness among businessmen about merchant banking activities.

Similarly respondents also gave various suggestions like government should play promotional role for improvement in overall economic condition and open capital market to foreign investors. There should also be proper planning and commitment for development.

CHAPTER V

SUMMARY, CONCLUSION AND RECOMMENDATIONS

This chapter presents the summary and conclusion drawn from the analysis of the study and recommendations are given to correct some aspects regarding improvement of merchant banking in Nepal.

5.1 Summary

Merchant bankers bridge the huge gap between demand of funds by the institutions and supply of untapped public savings. They are the intermediaries for the growth of capital market and one of the major supporting instruments for any ongoing business organization. The objective of the study is to evaluate the performance of merchant banks in Nepal, its significance toward the development of securities industry and to analyze its problems and prospects.

As per the requirement of the study, primary as well as secondary data has been used to meet the objective of the study. Secondary data were collected from annual report of Citizen Investment Trust, NIDC Capital Markets Ltd., Nepal Merchant Banking & Finance Ltd., Securities Exchange board of Nepal, Non-Bank Financial Statistics of Nepal Rastra bank, library search, daily newspapers, magazine, bulleting & other journals etc. questionnaires were distributed and interviews (formal and informal) were also made to gather information.

Information obtained as such were tabulated & presented as per the requirement of the study. The data obtained are analyzed through different elements like public issue analysis, activity performance of merchant bankers, income analysis, analysis of responses of questionnaire etc. to meet the objective of the research. The various

statistical tools and financial tools were also adopted as test methodology.

Before the analysis of selected merchant banks, analysis including institution and instrument wise public issue has been conducted from the perspective finding out the significance of merchant banking toward the development of securities industry in Nepal. There have been 129 public issues of different companies amounting Rs. 10752.69 million until 2064/65. Out the total public issue of securities during the period, finance companies stand first position which is 39.53% of the public issued, 20.93% of public issues are made by banks. Issue by insurance companies, manufacturing and processing companies, hotels, trading and other companies are 12.4%, 16.28%, 3.1%, 3.87% and 3.88% respectively. Similarly the most preferred instrument is issue of ordinary share. Out of the total public issue, 64.77% of issues are through ordinary shares. Other instrument like right share, preference share, debenture, mutual/unit fund are issued in 26.7%, 2.27%, 4.54% and 1.7% respectively.

To assess the performance of financial institution in relation to merchant banking activities, the analysis of the selected companies on the basis of secondary as well as primary data has been conducted. Citizen Investment trust as a pioneer of merchant banking, provides service of share issue management, underwriting, registrar to share issue and consultancy services Under share issue management, underwriting, registrar to share issue and consultancy services.

NIDC capital Markets Ltd is the first merchant banker in Nepal. It provides services like public issue management, underwriting, registrar to share, portfolio management, research and development. The research and development activities include listed companies in the area of cotton thread, garments, knitwear and tourism.

Nepal Merchant Banking & Finance Ltd, as a merchant banker, provides services of public issue management, underwriting, registrar to share issue and corporate counseling. NMB has been providing this service since the fiscal year 2057/58. NMB is also involved in providing necessary project evaluation for NMB itself and its clients.

Elite Capital is recently established special merchant bank. It has a vision to carry out the merchant banking activities in non fund basis. In the completion of one year it has made some right share issue.

Income analysis of selected merchant banks reveals that CIT is earning income form share issue management and from sale of government bonds regularly. NIDC Capital Markets Ltd. is also earning regular income from share issue management even though there are few loopholes in earning from underwriting. Nepal Merchant Banking & Finance Ltd. is earning from merchant banking since 054/55.

The test of consistency of merchant banking income of selected companies reveals that CIT ahs coefficient of variation of 38.30%, the coefficient of variation of NIDC Capital Markets Ltd is 49.15% and of Nepal Merchant Banking and Finance Ltd. is 45.51%. Similarly the mean income of CIT is Rs.1.85 million while that of NIDC capital Markets Ltd. is Rs. 2.57 million and of Nepal Merchant Banking & Finance Ltd. is Rs. 11.03 million.

From the analysis of response of questionnaire, it comes to know that finance companies are most actively involved in merchant banking functions while other institutions like few banks and other institutions (according to them "CIT") also are performing this activity. Everybody's eyes is now on the Elite capital Limited it has got a very positive atmosphere to flourish its business as Rastra bank announced instructed the banks and finance companies to carry out the banking and merchant banking activities separately.

Regarding the regulatory provision related to merchant banking though 62.55 of respondents agree on the availability of merchant banking regulatory provision 30% of respondents rejected it. According to them some acts like company act, finance companies act, securities exchange act etc are the regulatory provision that regulates merchant banking activities in Nepal. However maximum numbers of respondents i.e. 57.5% are not satisfied with the regulatory provision provided by the guidelines.

According to the majority of the respondents, both Nepal Rastra Bank and securities Exchange board of Nepal should regulate the merchant banking function as NRB is governing body of financial institutions on the other hand one of the mission of SEBO is to facilitate the orderly development of a dynamic and competitive capital market.

But regarding the major role player for merchant banking activities respondents view that merchant bank itself should be self-motivated. On the other hand Nepal Rastra Bank and Securities Exchange board of Nepal should motivate and provide favorable environment.

The respondents also pointed out lots of problems for the performance of merchant banking functions with their reasons. They also suggest reasons. They also suggest remedies so that merchant banking activities can be improved and boosted up in Nepal.

5.2 Conclusion

The coverage of the merchant banking is enormous and vast. The areas of functions are unlimited to the merchant bankers. Merchant Banking services, therefore, are of great help to entrepreneur customers who cannot afford a permanent staff of financial specialists. Their activities are one of the major supporting instruments for any ongoing business organization. They can play a highly significant role in mobilizing funds

from savers to invest through various channels assuring promising return on investments. Thus they serve as an important intermediary to provide needed capital to corporations. Hence the attempt has been made to find out the position of merchant banking in Nepal and the conclusion drawn under the support of presented data; facts and figures are given below.

- The importance of merchant banking is increasing gradually as a result of development activities after the restoration of democracy and economic liberalization in Nepal.
- Capital market provides an important base for the development of industry, commerce and economy. Merchant banking and capital market are interdependent with each other in many aspects. In this regard the analysis of public issue shows that merchant bankers are also playing a highly significant role towards the development of securities industry as well as capital market in Nepal.
- Merchant banking is a new concept in Nepal. The financial institutions participating actively in merchant banking sources are finance companies, citizen Investment Trust and few banks. Nepal Credit & Commerce Bank has also extended a separate department for investment banking. NIDC Capital Markets Ltd. is the first finance institution to introduce merchant banking in Nepal.
- The performance analysis of three leading merchant bankers like CIT, NCML, and NMB are found to be operating in limited areas of merchant banking services like share issue management, underwriting, syndication of underwriting, registrar to share issue management, sale of government bonds while their involvement in other merchant banking services like portfolio management, corporate counseling, project planning is very rare and the services

like venture capital, factoring, merger & acquisition etc are not yet introduced.

- Hence, merchant banking in Nepal is understood to be synonymous with issue management, though globally this word is taken to mean everything in financial services. However, NCML is in pipeline to introduce Nepal Industrial Venture Capital Fund (NIVCF) in Nepal.
- Generation of income is the main goal of any organization without which the company cannot sustain. In this connection, the analysis of income from merchant banking has been performed to study its growth. The analysis shows that CIT is generating most of the income from share issue management and sale of government bonds. NIDC capital market is also earning most of its merchant banking income from share issue management, underwriting, registrar to share issue and sale of government bonds. NMB is showing best performance in merchant banking which proves that merchant-banking activities can also be the best source of income for any fast growing financial institutions.
- The trend of merchant banking income of CIT and NCML are quite similar. They are generating merchant banking income of Rs. 1.85 million and Rs. 2.57 million in average respectively. NMB, though entered in merchant banking activities since 2054/55, is generating higher income in comparison to CIT and NCML. The average income during last five years is Rs. 11.03 million which is also unbelievably high.
- Co-efficient of variation shows the consistency of variables in the given period of time. Higher coefficient of variation indicates lower consistency and vice versa. Regarding merchant banking income,

the income of NCML is more inconsistent among the three companies taken for the study while that of CIT is more consistent.

- Regarding the regulations related to merchant banking though Finance Company Act, NIDC act, CIT act, Commercial Bank act etc permits to perform merchant banking activities none of them has given clear act, rules and regulation regarding merchant banking. Section 3(e) of finance Company cat permits finance companies to sell and purchase the bonds issued by His Majesty's Government or securities issued by other companies or institutions, to underwrite them and to form syndicate and to act as broker under the Securities exchange Act. And section 3(g) of the same act permits them to perform functions of merchant banking with prior approval of NRB. However, it has not specified the area or functions regarding merchant banking. Other acts are also facing similar problem.
- Because of insufficient information and propaganda merchant banking is still unknown to most of the public resulting to low demand of merchant banking services. It is also not being to prosper due to the less developed industrialization and financial marketing activities.
- Thus, in spite of the importance of merchant banking services many of the merchant banking services in our country is still poor. Nepalese merchant banks are still lagging behind and current political instability is also creating a question mark for the sustainability of merchant banking sector including industry, trading as well as the other business activities rather growth.
- Merchant banking has got a new atmosphere with the establishment specialized merchant bank Elite capital Limited. However the instruction of NRB to carry out the merchant banking

activities separately has made some confusion to the institute carrying out merchant banking activities

5.3 Recommendations

In view of the above facts, objectives and the present-day trend of merchant banking, the following recommendations are made to all concerned for consideration and implementation.

- Merchant banks should try to focus or specialize their services on merchant banking functions rather than making it only part of their function instead of sticking on selected merchant banking functions, similarly they should also make arrangement to introduce business and encourage severs outside Kathmandu valley to make them investors in the market.
- One of the major reasons for merchant banks moving toward diversifying their functions on other financial activities is because of the difficulty of survival by performing sole merchant banking function, The question of survival has risen due to unhealthy and underdeveloped capital market as well as money market. Thus financial policy should give attention toward development of financial market launching various programs and increasing investors' awareness. There should be clear rules and regulations regarding merchant banking in Nepal. The rule should be such that which would motivate financial institutions to perform merchant banking activities.
- Since Nepal Rastra Bank is the governing body of financial intermediaries, it should take continuous initiative to provide conducive environment to conduct the various merchant-banking activities.

- There should be continuous co-ordination with regulators like the Securities Exchange Board of Nepal, Nepal Rastra bank, the Institute of Chartered Accountants of Nepal, and the Office of Company Registrar.
- Merchant bankers themselves have to be more active to take latest information about the economic, social and political environment of our countries and appraise the foreigners with the facilities and relaxations in various rules and regulations of the government and the policy framework available for their technological expertise to Nepalese entrepreneur and or to collaborate in any other useful manner.
- Merchant bankers should frequently make exploring tours to foreign countries, organize meetings and conferences with the Chamber of Commerce and Industry and other commercial, industrial and financial organizations so as to enthuse the foreigners to take interest in investment activity in Nepal.
- Specific training related to various merchant banking activities should also be conducted by Nepal Rastra bank in association with Nepal Finance Companies Association. If required, experts of the different merchant banking activities should also be invited from the other countries to train and develop the local manpower.
- At this very early stage of development of companies and the capital market, it is particularly important to develop in Nepal venture capital companies, equipped with the skills, techniques and capital needed to invest in unquoted companies and help them grow to the point where they are ready for floatation on the stock market. Such venture capital companies would invest in companies at different stages of development from start-up to those requiring “development capital”.

- Merchant bankers should develop the OTC market for selling and buying the stocks that are not listed with the country's stock exchanges.
- NIDC capital Markets Limited should draw its attention to increase merchant banking activities to be parallel with other activities.
- NCML, instead of giving up its activities from portfolio management, should be more innovative and dynamic to be a leading merchant banker because managing portfolio is also one of the most challenging functions of merchant banking.
- CIT should not ignore other merchant banking activities like underwritten, share registrar, consultancy service etc.
- Though Nepal Merchant Banking & Finance Limited is trying to be a leading merchant banker in Nepal, should be more active in merchant banking activities and should diversify its activities to other merchant banking activities beside s issue management and sale of government securities.
- The merchant banking activities in Nepal is very limited. NRB's announcement to carry out the merchant banking activities separately has forced them to increase their activities to the broader spectrum
- Similarly, prevailing political uncertainty in the country should also be resolved so that capital market will start improve it space easily as expected. As the capital market activities starts growing other merchant banking activities will also follow together.

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APPENDIX-II

Public Issue of Securities

Fiscal Year	No of issue	Amount (in million)
2060/61	16	1416.63
2061/62	18	853.83
2062/63	17	1547.79
2063/64	12	1270.31
2064/65	34	2547.89
Total	129	7636.45

Institute Wise Public Issue in percentage

Group	No of issue	%
Banks	27	20.93
Finance company	51	39.53
Insurance	16	12.4
Mfd. & processing	21	16.28
Hotel	4	3.1
Trading	5	3.87
Other company	5	3.88
	129	

Public Issue Managed by NMB

Fiscal Year	NMB		Total		% (Amount)
	No	Amount	No	Amount	
2060/61	3	110	16	1416.63	7.77
2061/62	3	209	18	853.83	24.48
2062/63	6	99	17	1547.79	6.4
2063/64	6	346.41	12	1270.31	27.27
2064/65	10	648.5	34	2547.89	25.47
	28	1412.91	97	7636.45	18.50218

Instrument Wise Public Issue

Instrument	No of issue	%
Ordinary share	114	64.77
Right share	47	26.7
Preference share	4	2.27
Debenture	8	4.54
Mutual fund	3	1.7
	176	

Public Issue Managed by CIT

Fiscal Year	CIT		Total		% (amount)
	No	Amount	No	amount	
2060/61	2	59.3	16	1416.63	4.19
2061/62	3	272.5	18	853.83	31.91
2062/63	1	150	17	1547.79	9.69
2063/64	3	565.41	12	1270.31	44.51
2064/65	3	257.5	34	2547.89	10.1
	12	1304.71	97	7636.45	17.08529

Public Issue Managed by NIDC Capital Market

Fiscal Year	NIDC		Total		% (amount)
	No	Amount	No	Amount	
2060/61	2	197.46	16	1416.63	13.93871
2061/62	7	283.24	18	853.83	33.17
2062/63	1	6	17	1547.79	0.003
2063/64	2	63.2	12	1270.31	4.98
2064/65	14	993.87	34	2547.89	3.9
	26	1543.77	97	7636.45	20.21581

Performance of NCM Mutual Fund

Rs in million

S.N	Particulars	Fiscal Year			
		2061/62	2062/63	2063/64	2064/65
1	Investment(Rs)	72.56	72.56	72.563	73.288
2	No of invested co	27	27	27	27
3	Net assets value(Rs)	53.128	73.307	113.092	112.445
4	Net assets value per unit (Rs)	10.12	13.97	21.55	21.42
5	outstanding units	5250000	5250000	5250000	5250000
6	Face value(Rs)	52.5	52.5	52.5	52.5
7	No of unit holders	517	517	517	517

Fiscal year	Share Issue Mgmt.	Underwriting Commission	Registration Fee	Commission From sale of Govt. Bond	Total Income from Merchant Banking	Total Income	% of Merchant banking income to Total income
2060/61	1.836	0.062	-	1.223	3.121	7.517	41.52
2061/62	0.437	-	-	0.855	1.292	7.720	16.74
2062/63	0.846	-	-	0.588	1.434	10.552	13.59
2063/64	0.847	0.037	0.043	0.347	1.272	14.395	8.85
2064/65	1.460	0.233	0.206	0.128	2.027	14.673	13.81

Income of NIDC Capital Market Ltd.

Fiscal year	Share Issue Mgmt.	Underwriting Commission	Registration Fee	Commission From sale of Govt. Bond	Total Income from Merchant Banking	Total Income	% of Merchant banking income to Total income
2060/61	0.656	0.865	0.60	0.043	2.163	12.644	17.11
2061/62	0.391	-	0.377	0.014	0.782	21.823	3.58
2062/63	1.160	-	0.682	0.179	2.021	34.275	5.9
2063/64	1.870	0.895	1.614	0.085	4.464	50.953	8.76
2064/65	2.170	0.197	1.055	0.012	3.435	58.250	5.90

Income of NMB

Fiscal Year	Merchant Banking Income	Total Income	% of Income from Merchant Banking to Total Income
2060/61	3.158	103.198	3.06
2061/62	18.199	145.744	12.49
2062/63	8.379	108.78	7.72
2063/64	12.887	141.182	9.13
2064/65	12.485	141.343	8.83

Merchant banking Income of Various Companies

Rs in Million

Fiscal Year	CIT	NIDC	NMB
2060/61	3.121	2.163	3.158
2061/62	1.292	0.782	18.199
2062/63	1.434	2.021	8.379
2063/64	1.272	4.464	12.887
2064/65	2.165	3.435	12.485