Sebi rights issue plan may hit merchant bankers' revenue

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RIGHTS ISSUES

	No. of issues	Amount (₹ crore)	Investment bankers fee (₹ crore)
2019	12	52,053	48.34
2020	20	64,984	41.32
2021	11	27,771	13.81
2022	10	3,884	14.07
2023	12	7,266	45.92
2024	14	17,336	137.69

Source: primedatabase.com

THE SECURITIES AND Exchange Board of India (Sebi)'s proposal to overhaul the rights issue process to boost its appeal as a fundraising route is likely to pose a serious threat to revenue streams of merchant bankers.

One of the key changes suggested by the regulator is the elimination of the mandatory role of investment banks in a rights issue. Not only does this jeopardise their earnings, but also pivots merchant bankers towards exploring other opportunities, bankers and legal experts said.

Prashant Rao, director and head, equity capital markets, Anand Rathi Investment Banking, said the proposal brings both opportunities and challenges for investment bankers. "While this change could disrupt the traditional advisory role of investment banks, and in a way, impact fees, it also opens up opportunities to explore new service areas or develop solutions to support issuers and RTAs."

Currently, merchant bankers are tasked with conducting due diligence, preparing draft letters of offer, marketing the issue and filing the documentation required for a rights issue with Sebi and the exchanges. This has been a lucrative business, with fees averaging around 0.7% of the total capital raised through rights issues over the past three years, according to Prime Database.

In 2024, the total amount raised through rights issues stood at ₹17,336.42 crore, with merchant bankers earning ₹137.69 crore, or 0.8%, in fees. In 2023, ₹7,266.33 crore was raised, generating ₹45.92 crore in fees for these bankers. The potential loss of revenue would also be substantial, since these proposals are aimed at increasing the number of rights issues.

Merchant bankers typically charge around 1.5% of the issue size as fees, which, for large rights issues, can run into millions. The removal of this income stream can significantly impact their revenue, as these transactions contribute a substantial portion of their fee income, experts said.

"This move will likely compress fees and push merchant bankers to focus more on other capital-raising activities like IPOs, QIPs or M&A deals to compensate for the loss," said Nilesh Tribhuvann, managing partner at White & Brief – Advocates & Solicitors, pointing out that bankers may still have a role in more complex transactions.

Echoing the view, Ketan Mukhija, senior partner at Burgeon Law, said the industry may see a shift as these firms could pivot towards more value-added services to compensate for potential loss in rights issue-related business.

Smaller firms reliant on rights issues are expected to be hit harder than larger players which may adapt more easily.

"The top-tier merchant bankers would still maintain a substantial chunk of their business as companies may continue to seek their services for ensuring the quality of disclosures and managing complex financial transactions despite regulatory relaxations," Mukhija said.