Indian Journal of Economics and Finance (IJEF)
ISSN: 2582-9378 (Online), Volume-4 Issue-1, May 2024

Examining Global Resource Mobilization: Strategies and Hurdles in Accessing the International Capital Market

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Abstract: ***The role of finance is indispensable for business entrepreneurs as it fuels both fixed and working capital, driving growth and operational efficiency. Financial decisions are crucial for directing business growth from its inception through various phases. Corporate finance is pivotal in exploring alternative methods to finance fixed and working capital needs. Capital markets, including domestic ones like India's Securities Exchange Board-regulated and international markets, serve as vital platforms for businesses to secure funding and ensure smooth operations. Effective corporate governance, shareholder wealth maximization, regulatory compliance, profitable project funding, and global brand recognition are key goals for corporations to sustain and thrive. This paper aims to delve into the Overseas Depositories' role in international capital markets, highlighting their contribution to funding corporations globally. It will also discuss the significance of two-way fungibility in trading shares and depository receipts across borders, and how overseas depositories facilitate finance raising for corporations. Additionally, the paper will examine the trading dynamics of American and Global depository receipts vis-à-vis shares in the international capital market context.***

Keywords: Mobilization, Depository, Fungibility, Sponsored, Equity

I. INTRODUCTION

Resource mobilization in the international capital market is a crucial aspect of corporate finance. Securing funding is essential for the growth and development of business enterprises, and the international capital market serves as a significant source of funds where domestic companies can trade their shares across borders. While stock markets are foundational for funding arrangements, there came a pivotal policy shift for Indian business enterprises allowing them to raise funds through equity share issuance in the international capital market. This shift was observed during the 1990s when India's foreign exchange reserves depleted, leading to a decline in the country's rating. To address this, the government facilitated avenues for companies to meet their financial requirements.

Manuscript received on 05 April 2024 | Revised Manuscript received on 18 April 2024 | Manuscript Accepted on 15 May 2024 | Manuscript published on 30 May 2024.
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Foreign investors stepped in to assist by purchasing equity shares from Indian companies and initiating trading activities involving equity and bonds across international boundaries. As the option of international funding became available, companies worldwide began raising capital through various instruments such as global depository receipts (GDRs), American depository receipts (ADRs), foreign currency convertible bonds, and exchangeable bonds. Among these, foreign currency bonds are often considered as lenders of last resort, as corporations typically prefer to raise capital through equity and depository receipts. Studies show that the domestic and international capital markets intersect during cross-border transactions, particularly when foreign institutional investors invest in the equity of companies incorporated worldwide. This intersection reflects the global nature of modern capital markets, where investors and companies engage in cross-border activities to access diverse funding sources and investment opportunities.

II. DEPOSITORY RECEIPTS AND FOREIGN CURRENCY BONDS

From the perspective of the international capital market, depository receipts are negotiable instruments denominated in foreign currency and issued by overseas depository banks against equity shares. These receipts are traded and issued to foreign investors when they purchase shares from foreign companies as underlying assets, thereby raising funds from international capital markets [10][11][14]. When an Indian company intends to raise capital from cross-border sources, it can issue depository receipts and bonds to foreign investors through the following means:

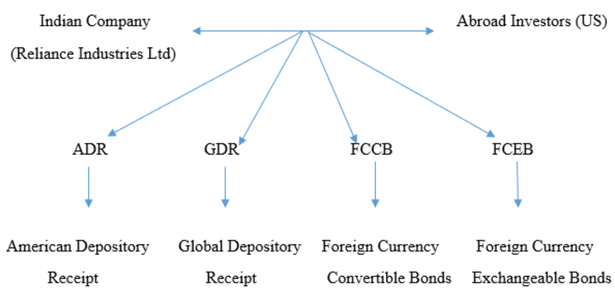

Fig. 1.0. Types of Depository Receipts and Bonds

Depository receipts are financial instruments that allow a corporation based in one country to issue shares or convertible securities outside its jurisdiction.

Retrieval Number:100.1/ijef.A257104010524
DOI:10.54105/ijef.A2571.04010524
Journal Website: www.ijef.latticescipub.com

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These instruments are negotiable and enable the corporation to raise funds from foreign investors. However, this process would not be feasible without the involvement of an overseas depository bank located outside the corporation's home country. The role of the overseas depository bank is crucial in facilitating international capital funding. It acts as an intermediary that issues share in the form of depository receipts or convertible bonds to foreign investors on behalf of the issuer company, thereby helping the company raise capital as needed.

The issuance of depository instruments by domestic companies is a lucrative source of international capital funding. It allows companies to access the international capital market and tap into a broader investor base, thereby fulfilling their capital requirements and supporting their growth and expansion initiatives.

III. AMERICAN DEPOSITORY RECEIPTS

It was J.P Morgan which was the first company to launch ADR in 1927 and created a platform for the American investors to capitalize in Selfridges shares, a British company [1]. American Depository Receipts (ADRs) are financial instruments issued by overseas depository banks located within the United States against shares issued by foreign companies. These instruments are traded in American markets under the supervision of the Securities and Exchange Commission (SEC). ADRs are issued by overseas depository banks when foreign investors purchase shares of a foreign company that are traded in the US during regular trading hours. The US securities markets currently allow the trading of thousands of ADRs representing shares of companies from various countries across the globe. The Securities and Exchange Commission (SEC) views trading in depository receipts as less risky compared to trading in domestic stocks, as it provides greater transparency and accountability due to the involvement of two securities commissions - one in the country of the issuing company and the other in the United States. This regulatory oversight helps enhance investor confidence and trust in the trading process. American Depository Receipts (ADRs) are documents or certificates issued by overseas banks representing shares issued by a foreign company. These ADRs are issued in compliance with regulations set forth by the Securities and Exchange Commission (SEC). The foreign shares are held in custody overseas, while the ADR certificates are traded on major U.S. equity markets such as the New York Stock Exchange, American Stock Exchange, and NASDAQ. ADRs are typically denominated in US dollars and are traded during regular trading hours.

One of the key features of American Depository Receipts is that they are traded similarly to other securities of US companies. Additionally, ADR holders are entitled to the same rights and benefits as shareholders of the issuing foreign company [2], just as they would have if they held shares directly in a foreign market. This makes ADRs an accessible and convenient way for investors to gain exposure to international companies while enjoying the protections and privileges afforded to shareholders in the US market. Under the mechanism of ADR issue, holders are paid dividends in US $ and can be traded as ordinary shares of US companies and pertinent to mention that the value of ADR fluctuates based on the price actions of the underlying shares.

IV. GLOBAL DEPOSITORY RECEIPTS

Global Depository Receipts (GDRs) are similar to American Depository Receipts (ADRs) but are designed to target investors in countries other than the United States. They serve as instruments that attract investors from various global stock markets. Companies worldwide issue their shares in the form of GDRs to raise capital for efficient governance and funding of their projects. Some companies even arrange for the issuance of equity on a global scale. These steps may include buying back shares from domestic investors and subsequently issuing them in international markets at higher rates. Many companies in India have expanded their stock trading operations in the international capital market with the support of domestic custodians and overseas depositories. This strategy allows companies to access a broader pool of investors and tap into international funding sources, contributing to their growth and expansion plans.

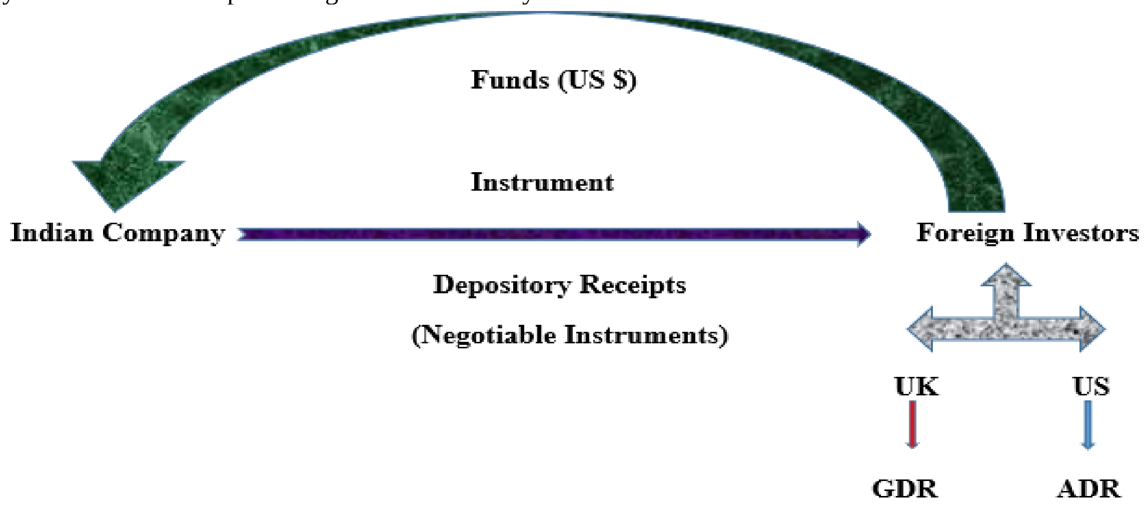

Fig. 1.1. Resource Mobilization from Foreign Investors

Retrieval Number:100.1/ijef.A257104010524
DOI:10.54105/ijef.A2571.04010524
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A. How does a Company Pool Fund from the International Capital Market?

Raising funds is a fundamental necessity for any company, as without adequate finance, a company cannot execute its business plans smoothly and effectively. Every business decision has financial implications, and any action that impacts a company's finances falls under the domain of corporate finance. Financing a company involves making financial decisions in consultation with the financial manager and other stakeholders of the company. Apart from domestic capital markets regulated by SEBI norms, the international capital market also plays a significant role in providing funding opportunities to companies globally. This global financial landscape allows companies to access diverse funding sources and expand their operations with international capital. Let us understand by an illustration, how Indian companies raise funds through Global Depository receipts:

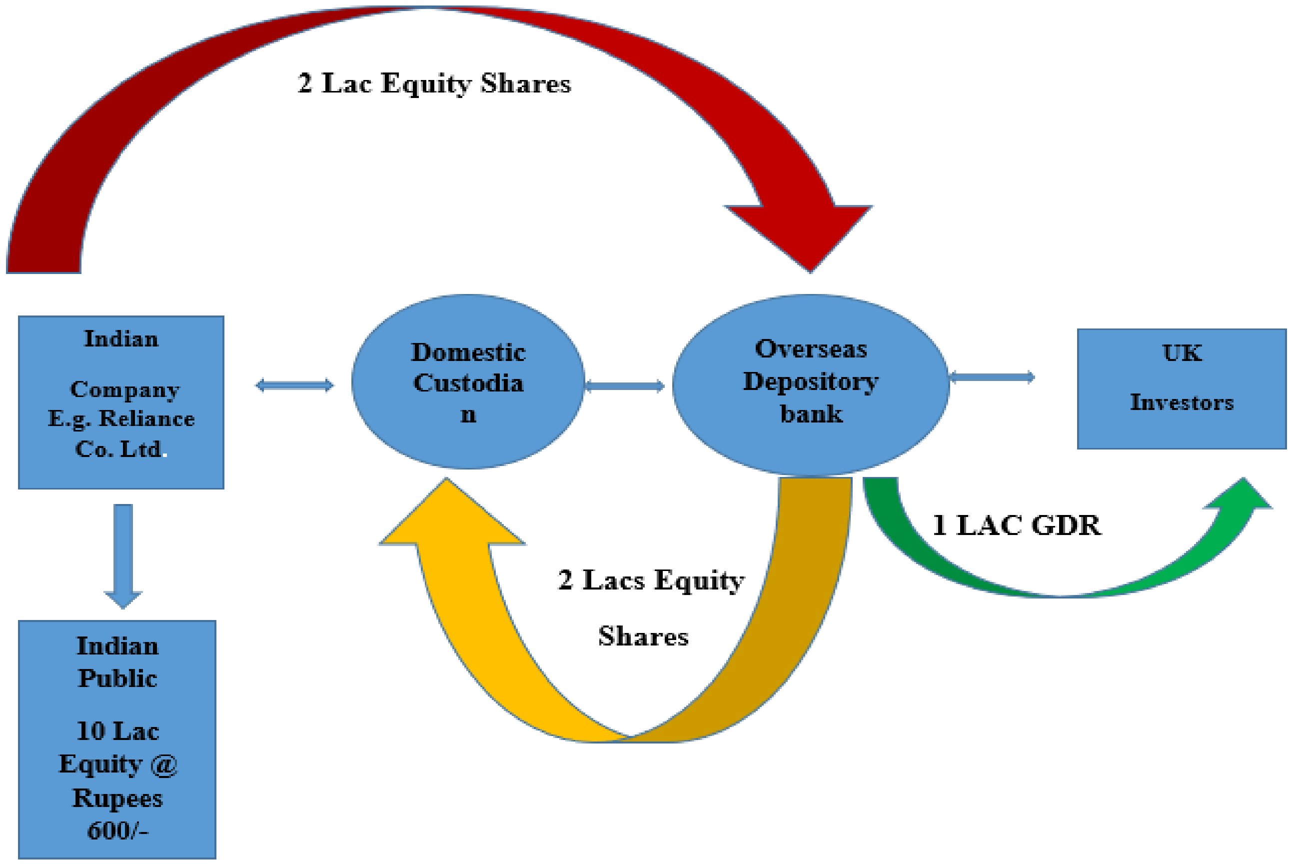

Fig 1.2 Process of Issuance of ADR

Reliance Ltd Issuing 10 Lacs Equity shares to the Indian Domestic Market @ Rupees 600 /-
1 GDR= 20 $
1$ = Rupees 60 /-
1 GDR = Rupees 1200/- in India
Therefore, 1 GDR =2 Equity Share (In India)
Then Overseas Depository Bank have to issue 1,00,000 /- GDR for 2,00,000 /- Equity Shares.

Shares issued by Reliance Ltd. first get deposited in Domestic Custodian which is located in India itself but the process is somewhat indirect as it can be apprehended from the diagram above. When shares are received by the Domestic Custodian, it acknowledges the share deposit which is then communicated to the Overseas Depository Bank located in the UK (Fig 1.2). Hence against the underlying shares of Reliance the overseas depository bank will issue GDR which are in turn purchased by the potential investors in the UK. Moreover, with the fluctuation in the price of the shares of the Indian company, the value of GDR will also be highly impacted and the investor can earn a profit if the shares price is on a hike. In this whole international security trading mechanism, the UK investors will purchase the GDR in European currency and the money of the investors is transferred by the Overseas Depository Bank to the company itself for which the depository bank will deduct some charges for arranging the whole mechanism.

B. Steps involved in Raising Funds through ADR/GDR

a. Deposit of Securities of an Indian company with a Custodian Bank located in India.
b. The Custodian bank acknowledges deposits to the Overseas Depositories Bank in the US/UK.
c. The depository bank then issues ADR/GDR against the underlying shares to the Indian Company.
d. Payment is made by foreign investors according to the currency and exchange norms.
e. ADR/GDR certificates are handed by Overseas Depository Bank to the Foreign Investors.

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C. Role of Overseas Depository Bank in Mobilizing Resources from Global Securities Market

Overseas depository banks play a crucial role in mobilizing resources from the global securities market. They facilitate foreign investment by offering access to securities issued in different countries through depositary receipts like American Depositary Receipts (ADRs) or Global Depositary Receipts (GDRs) [3]. These receipts represent ownership of shares in foreign companies, allowing investors to diversify their portfolios geographically and spread risk. Additionally, depositary receipts traded internationally enhance liquidity for underlying securities, attracting a broader investor base. Overseas depository banks also ensure regulatory compliance in both the issuer's home country and the host country where receipts are traded. Their presence contributes to market development, transparency, and capital formation for businesses operating globally.

D. The Key Role Played by the Depository Bank:

1. Expanding the market value for issuer-company and ensuring potential liquidity: Companies strive to ensure growth and increase their share capital value to its ultimatum. However, the growth of the business can be persistent in its present and future only if the flow of capital is smooth and continuous. Depository banks assist the issuer company in accessing the global equity markets and attracting potential foreign investors with depository receipts against the underlying shares.
2. Surge in the value of shares in local markets: Increased demand in global stock trading ensures an increase in opportunities and a surge in the value of shares in local markets. More finance would help the companies to boost their capital structure and profitable project funding which ultimately leads to the maximization of shareholders' wealth.
3. Enabling the corporations to build strategic corporate objectives: To ensure a concrete compliance framework and smooth governance of the corporations, entrepreneurs are required to frame strategic corporate objectives in indicating the effective Depository receipts program. However, this may include:

i. Increasing shareholder’s wealth
ii. Creating brand image across the global market
iii. Depository receipts as a source of capital funding
iv. Global recognition with an expedient investment vehicle

4. Promoting stock option plans and stock purchase plans across international frontiers: With the issuance of depository receipts, depository banks result in the intersection of issuer companies with the global stock market. It ultimately promotes the company's brand image and provides opportunities for investors to move with markets. Foreign investors and issuer companies thus get the chance to develop the stock option and purchase plan.
5. Clearance and Settlement in Trading: Depository banks are the key intermediaries in placating business doubts across the globe. The terms and conditions set forth between the depository banks and the issuer company with international stock dealings are apparent and investors can voluntarily invest in foreign shares due to the security provided by depository banks.
6. Impact on cross-border mergers and acquisitions: The Depository banks with their DR framework play a critical role in their multifarious cross-border transactions such as mergers and acquisitions, amalgamation, and takeovers across international frontiers. The DR framework has increased the simplicity of trading and settlement aspects connected to cross-border transactions. Some of the cross-border transactions that claimed to be successful through the Depository receipt mechanism are:

- Equity based acquisition of non- U.S subsidiaries.
- Equity-based acquisitions of non- U.S based entities.
- Spin-offs of non-US subsidiaries.

However apart from the overseas depository bank other different parties are involved in the issuance of Global Depository Receipts:

Merchant Banker: Merchant Banker acts as a responsible lead manager for evaluating, assessing, and managing public issues. It assists the issuer company in assessing the financial requirements and also in tracing the source for pooling funds both from the domestic market and international capital market. In addition to this merchant bankers also exercise due diligence in gathering information relating to the issuance of depository receipts [4].

Custodian: A domestic custodian is a capital market intermediary that is appointed by the overseas depository bank in consultation with the issuer company and plays a key function in international stock trading. The custodian retains the custody of all stock of shares, certificates, dividends, rights bonus shares, etc.

Clearing House: Clearing houses are corporations that keep records of all accounts related to depository instruments e.g. EUROCLEAR (Brussels), CEDEL (London) etc.

E. Understanding Two Two-Way Fungibility Scheme

Fungibility in an ordinary sense means the exchange of something with any other thing without compromising its value. Companies listed under a recognized stock exchange can raise their funds through the issuance of depository receipts across international frontiers. The issuer company after satisfying the listing requirement as per the securities rules and regulations for any recognized stock exchange deposits its physical scrips to its domestic custodian. After receiving the share certificates from the custodian, it intimates the overseas depository bank for the issuance of depository receipts listed on international frontiers. Hence under such circumstances, if a domestic investor holding shares of any particular company listed under a stock exchange migrates to some other nation where the depository receipts underlying such shares are listed, then such investor can convert his/her equity shares into DR by requesting the domestic depository herein (NSDL) and similarly any foreign investor can get his depository receipts surrendered to the overseas depository for converting them into ordinary shares. This process is called Two Way Fungibility.

Let us understand the process of two-way fungibility with the help of Figure No 1.3. Mr. X is migrating to the US for his permanent settlement and he requested the depository here in NSDL (National Securities Depository Limited) to convert that equity into ADR so that he can still hold the shares of the domestic issuer company in ADR form beyond the national frontiers. NSDL on such requisition will request the domestic custodian to channel the issue of American Depository Receipts by the overseas depository bank and on receiving confirmation from the depository bank NSDL will further transfer that equity to the domestic custodian located in the domestic territory itself. Acceptance of such securities by a domestic custodian will amount to the issue of ADR as per the value of the shares in the domestic market. This mechanism has a vice-versa reciprocity which helps the companies to retain their share-holders even beyond the territories.

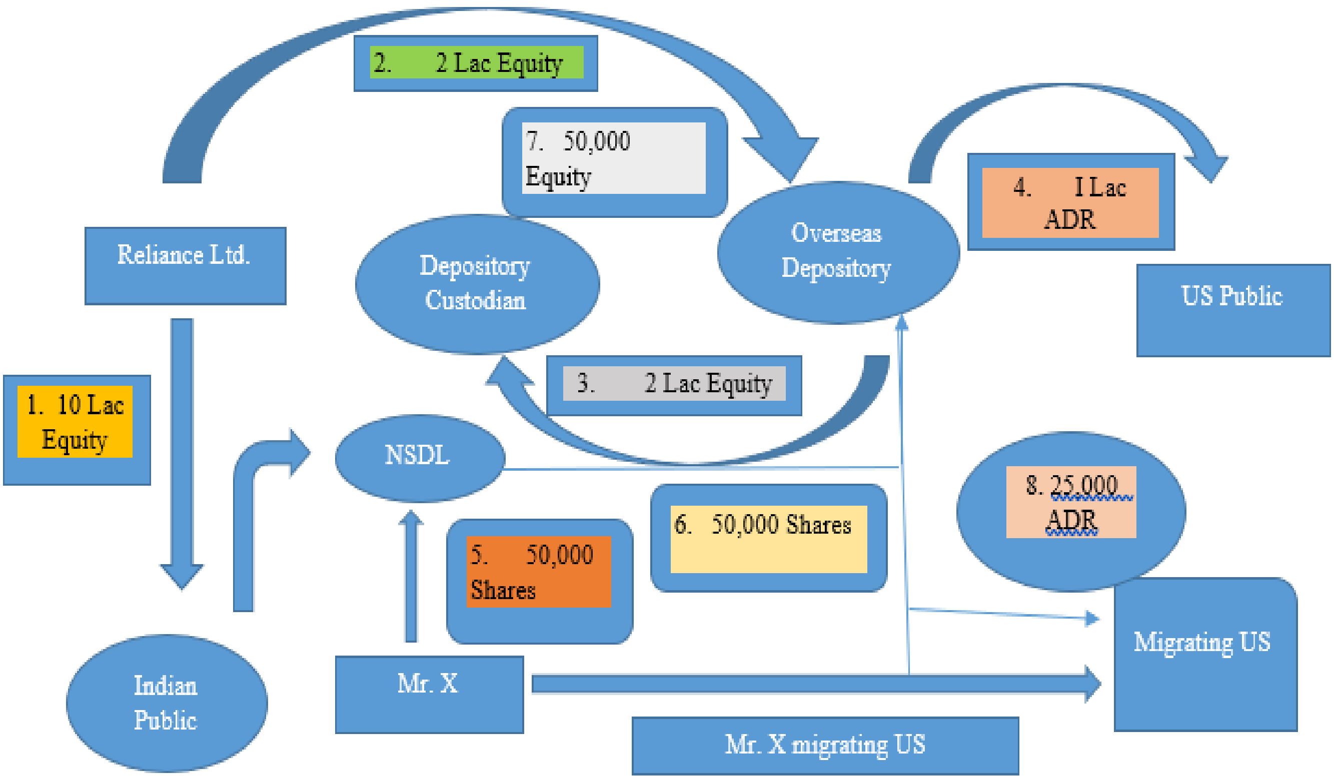

Fig 1.3 Two-Way Fungibility

F. Sponsored ADR/GDR

Sponsored ADR/GDR are instruments issued by an overseas depository bank against the shares of a foreign company. This means the equity shares issued by the domestic company are the underlying assets. The concept of Sponsored ADR and GDR establishes a legal connection between the issuer-company and foreign investors which includes the cost of issuing security. One of the landmark differences between unsponsored and sponsored ADR/GDR lies in the footing the former can be traded on the over-counter market while the latter is eligible to get listed on some registered stock exchange [5].

Companies across the world can widely use depository instruments to get access to the international capital market. Foreign investors are given the prospect to expect returns from international capital markets through the mechanism of ADR/GDR and as such they stereotypically focus on the global market. However, in the context of the Indian capital market, the process to issue sponsored ADR/GDR is the same except new shares are not issued rather shares are buy-back or repurchased from the domestic equity holders to issue ADR/GDR in the international capital market [6] [12][13]. Sponsored American Depository receipts include three levels:

1. A level I sponsored American depository receipts can be merchandized over the counter and cannot be listed under-recognized stock exchange.
2. Level II are those sponsored ADRs that can be listed under a recognized stock exchange and thus visible for trading across the globe.
3. Last but not least, Level III-sponsored ADR allows the corporation to issue equity to raise funds keeping in mind that compliance requirements must be strictly updated and satisfied.

A diagrammatic approach is given to understand how sponsored ADR/GDR are traded in the international capital market:

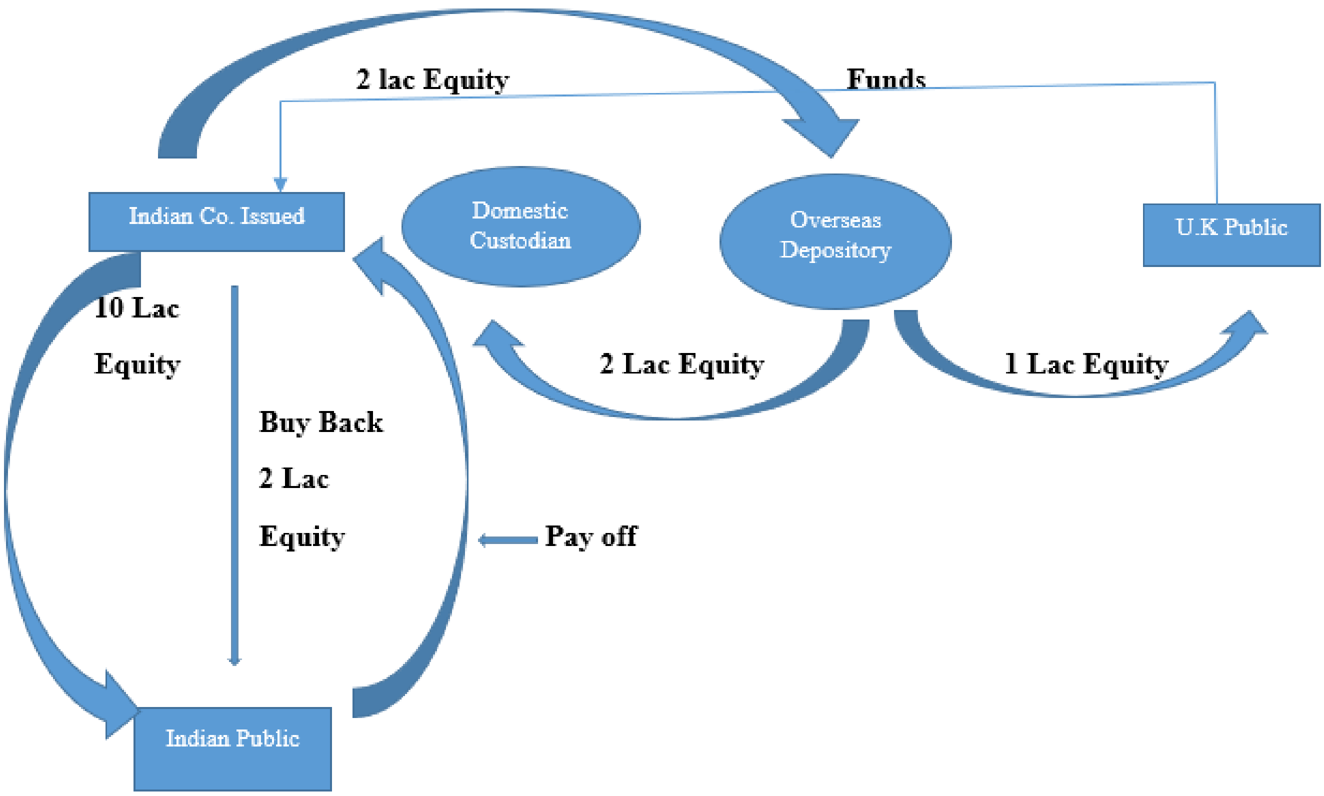

Fig. 1.4. Process of Issuance of Sponsored ADR/GDR

The above diagram is quite identical to the two-way fungibility process except the difference lies on the footing of buy back of shares. Generally, buyback of shares is prohibited by regulatory norms but there may be circumstances when the company is not able to bring fresh issues rather than buying back the equity from existing shareholders to raise funds through a depository mechanism in global markets.

V. INDIAN CONTEXT

The Securities and Exchange Board of India (SEBI) has undertaken significant initiatives to create a comprehensive framework for the issuance of depository instruments, enabling Indian companies to raise funds internationally [7]. This framework, including the depository receipt scheme, was developed under the guidance of the Indian Finance Minister, Srimati Nirmala Sitharaman. The scheme aimed to enhance Indian companies' access to foreign markets through the issuance of American and Global depository receipts. However, challenges arose due to concerns raised by SEBI.

SEBI, known for its stringent norms and regulations, stipulated that only listed companies could issue securities and allowed security holders to convert equities into depository receipts subject to specific mandatory requirements. These requirements included adherence to Listing Disclosure Obligations and ensuring that responsible stakeholders (such as promoters, directors, and compliance officers) did not default on listing mandates and obligations as per SEBI's requirements. Moreover, SEBI mandated that any listed company planning an initial public offering and seeking to register its shares on a recognized stock exchange to raise funds through depository receipts must also list on a global bourse. This required obtaining approval from both SEBI and the overseas stock market [8]. Additionally, the listed company had to ensure that all listing disclosures made on the global exchange complied with the permissible jurisdiction's requirements where the depository receipts were listed, and these disclosures must be filed with the recognized stock exchange within 24 hours of filing.

Furthermore, SEBI directed registered depositories in India to collaborate in developing a system to ensure that the collective holding of depository receipts by DR holders, including offshore derivative instrument holders, did not exceed the foreign holding limits prescribed by the Foreign Exchange Management Act (FEMA) and SEBI guidelines. These measures aimed to regulate and monitor the issuance and trading of depository receipts in a manner consistent with Indian regulatory frameworks and international standards.

A. Recent Challenges Faced by International Capital Market on Account of GDR Manipulation

One of the recent challenges confronted by the global depository market was on account of GDR manipulation done by IKF Technologies Limited with the involvement of other two entities administered by the managing director Mr. Arun Pancharia, invited the core investigation and inquiry by the SEBI. As per the latest report published by the Press Trust of India, the market regulator (SEBI) imposed a penalty of 12.1 crore and 1 crore each on the two officials including CCP for contravention of the norms and standards of security market regulations [9]. In addition to this it was also reported and alleged that IKF Technologies Limited was also accountable for making concocted and misleading announcements regarding issuance of GDR.

Further discovered that said IKF Technologies Limited along with the two official partners on two occasions, devised and implemented the structure of fraudulent issuance of global depository receipts and with oblique intention pledged the depository receipts with Banco Efisa SFE SA Bank and another with the EURAM BANK. The organization was also held liable for not furnishing requisite information within time thereby causing a delay in SEBI's investigation.

VI. CONCLUSION

Globalization has significantly impacted the world capital market, facilitating increased resource mobilization across global frontiers. Corporations now have various avenues to pool funds, with depository receipts playing a key role in accessing global markets. These receipts enable companies to tap into global capital through mechanisms such as IPOs, seasoned equity offerings, cross-listing depository receipts, private equities, and other equity capital channels. Depository receipts are highly valued in global markets, offering benefits to both issuer companies and global investors. They allow companies to expand and strengthen their investor base, making them crucial instruments in the capital market. Moreover, depository receipts appeal to international investors seeking to avoid cross-border custody charges. However, one of the primary challenges for issuer companies is choosing the right depository based on its experience and service offerings. Despite this challenge, access to global markets has become more accessible, leading to wide-ranging implications for firm strategies. In recent times, private equity and venture capital have evolved into global phenomena, influencing firms to participate in global markets and creating a unified platform for global business interactions.

DECLARATION STATEMENT

Funding	No, I did not receive
Conflicts of Interest	No conflicts of interest to the best of our knowledge.
Ethical Approval and Consent to Participate	No, the article does not require ethical approval and consent to participate with evidence.
Availability of Data and Material	The data access or material availability is not required.
Authors Contributions	All authors have equal participation in this article.

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