Tapping Global Investors Through
Depositary Receipts

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Investing in a company that is listed overseas is very difficult due to variety of reasons. And hence, there is a simplified option in the form of Depositary receipts.

Depository Receipts mechanism is preferred for over 75 years.

Many actively listed companies wish to make their shares accessible to investors outside their home country – more particularly to investors based in the United States. These companies can then easily focus on raising new capital abroad, diversifying their shareholder base, improving their profile with foreign investors and even using own shares to make international acquisitions.

Investing money in companies which are listed on domestic stock exchange is very simple. However, investing in a company that is listed overseas is very difficult due to variety of reasons. And hence, there is a simplified option in the form of Depositary receipts (DRs).

Depositary receipts (DRs) are certificates that represent an ownership interest in the ordinary shares of stock of a company, but that are marketed outside of the company's home country to increase its visibility in the world market and also access greater amount of investment in other countries. Depository Receipts mechanism is preferred for over 75 years and can be divided into 2 broad categories:

- American Depositary Receipts (ADRs)
- Global Depositary Receipts (GDRs)

Major difference between ADRs and GDRs lies in their structures.

American Depositary Receipts

In case of American Depositary Receipts, non-US shares are converted into domestic US securities which are also denominated in US dollars. ADRs enable US investors to acquire and trade non-US securities denominated in US dollars without any concerns the differing settlement time-table and other problems associated with overseas markets. They also provide non-US companies with easy access to the US capital markets which has the largest investor base in the world.

ADRs are created when a broker, acting on behalf of a potential ADR investor, buys domestic shares in a non-US company and places them in custody with a depository bank. The depository bank then issues US dollar-denominated receipts conveying beneficial ownership of those shares. These depository receipts are deemed by the Unites States Securities and Exchange Commission (SEC) to be domestic US securities and their trading and settlement is done in United States.

There are several types of ADR, each of which involves different level of disclosure of information and compliance with the regulations of the SEC that provide a mechanism which makes it easy for US investors to buy and trade existing shares.

Level I ADRs

Level I ADRs do not involve raising of capital or listing on leading US Stock Exchange. However, they provide enhanced exposure to US based investors with minimal additional reporting. These ADRs can only be traded over-the-counter.

Level II ADRs

Level II sponsored programs are initiated by non-US companies to give US investors access to their stock in the US. They do not involve capital raising, however, they can be listed on leading US Stock Exchange. A sponsored Level

II ADR must comply with the SEC's full registration and reporting requirements.

Level III ADRs

Level III sponsored ADRs are similar to Level II ADRs in that the issuer initiates the program, deals with one depositary bank, lists on one of the major US exchanges, and complies with other statutory formalities of the SEC. The major difference is that a Level III program allows the issuer to raise capital through a public offering of ADRs in the US.

Global Depositary Receipts

Global Depositary Receipts (GDRs) also work on similar principle, with trading and settlement taking place in Europe. If they are placed with qualified US buyers then trading and settlement will happen in the United States. GDRs are usually denominated in US dollars or Euro.

There are 3 types of GDRs – The Reg S GDRs, Rule 144A GDRs and the pairing type.

Reg S Type GDRs

The Reg S Type GDR is similar to ADR. It is issued to the public through a sponsor bank / brokerage. Once issued, this GDR is either listed on European Stock Exchange or remain unlisted. This type of a GDR is open for every kind of investor except US-resident investors. Unlike ADRs, where each type of ADR determines the investors that can trade it, the Reg S type GDR can be traded from any kind of investor to different kind of investors.

Rule 144A Type GDRs

Rule 144A Type GDRs are used to raise capital but are placed exclusively with Qualified Institutional Buyers (as defined by SEC) in the United States. Due to sophisticated investor base, registration and reporting requirements are very minimal.

Pairing Type

It is a combination depositary program of Reg S type GDR and Rule 144A GDR. Often Rule 144A GDRs are placed with US investors in conjunction with a Reg S GDR offering to non-US investors.

Due to its unique structure, depositary programs are highly beneficial for investors as well as issuer companies. Domestic capital markets are not doing well due to delayed monsoon, slow growth, political uncertainty, etc. Perhaps, there can be an opportunity for growing companies to explore the possibility of using this mechanism to tap overseas investors on selective basis.

From Readers' Desk...

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CS P. Jagannatham
Past Chairman - SIRC

The 101 edition of the news letter is excellent.

CS P Chiranjeevulu
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Thank you for sharing. Really appreciate it!

Olive W.
Corporate Secretary and Administrative Manager at Mercatus Capital Pte Ltd, Singapore

Very Informative and moral booster edition specifically the "LIVING ROOM" article

CS Manoj Kumar Panda
KOLKATA

I found e-Magazine very interesting and have good content. Thanks to all for this nice initiative.

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