

The Main Features of Syndicated Loan in the Process of Financing Investment Projects

Ruzibaeva Nargiza Khakimova¹, Khotamkulova Madina Sanjar kizi²

¹Head lecturer of Samarkand Institute of Economics and Service

²Student of Samarkand Institute of Economics and Service

Abstract:

this article discusses the types of external financing of investment projects, the must-be condition of the company to receive syndicated loan, significant financial indicators for syndicated loan, and the role of financial advisors in the financing process of the investment project.

Key words: syndicated loan, interest rate, financing, investment project.

Introduction

companies often face the challenge of finding funds to finance large projects, especially when it comes to multi-billion dollar infrastructure, industrial or energy projects with a long construction period. At the planning stage, business owners must decide whether to use equity capital, finance a project with the help of business partners, shareholders, investors, or use loans from banks and other financial institutions. One of the preferred options is the syndicated loan and this article discusses its main features and the practical implementation of the syndicated loan in Uzbekistan.

Literature Review

According to the World Bank[1], financing large projects is a major challenge for fast growing economies. Today a business can choose the following sources of project financing: leasing, factoring, issue of shares and bonds, bank loans, etc.

All external financing instruments have different purposes and usually mean different costs for the companies that use them. All of the above sources of project financing can be used in various combinations, based on the characteristics of a particular business[2]. Following table 1 illustrates main types of external financing of investment projects and provides information about their main features. It should be noted that we have not stated at the costs of these financings as they vary based on the projects.

Table 1 Main types of external financing of investment projects[3]

Types	Main features
Factoring	This is an early redemption of all payable bills by the bank with which the company has signed an agreement, on mutually beneficial terms. This financial instrument is recommended for companies experiencing temporary problems with maintaining financial liquidity.
Leasing	This instrument refers to a leased item (machines, devices or vehicles). It is a way of financing the purchase of a certain object, but not a source of funds for the current activities of the company. The advantage of leasing is that it is much easier to access than a loan. But it is also usually a more expensive financing instrument.
Issue of bonds	This is one of the most interesting types of project financing. A bond issue can serve as the basis for long-term financing or as a way to reduce the cost of financing (for example, through short-term issues that replace revolving loans or overdrafts). Because of their universal nature, bonds are considered the most common way to finance large businesses after bank loans.
Bank loan	Loans can be provided by both banks and other institutions. Their disadvantages are usually short maturities and high interest rates.

Firstly, if it comes to syndicated loans of the organizations we should note about the origination of them. The syndicated loan market is the dominant way for large corporations in the U.S. and Europe to receive loans from banks and other institutional financial capital providers. Financial law often regulates the industry. The U.S. market originated with the large leveraged buyout loans of the mid-1980s, and Europe's market blossomed with the launch of the euro in

1999 . A syndicated loan is a long-term loan usually used to finance a specific project. A syndicated loan is provided by at least two institutions[4].

The main features of syndicated financing are listed below:

1. Long term maturity: usually several years, but there are known examples with maturities up to several decades, especially in the oil and gas sector, energy and environmental projects.
2. The loan is intended to finance specific activities, including the construction of a new thermal power plant or laying of a gas pipeline.
3. The funds are partially provided in the form of a revolving loan up to a certain limit established by the agreement[5].

A syndicated loan is a highly customized financial instrument, which means there are no strict rules. Loan agreements are very flexible and take into account the specifics of each company, its financial health and market position. One of the features of a syndicated loan is its wide application in project financing. In these cases, the loan amount often exceeds the value of the assets of the entire enterprise; therefore banking institutions tend to apply very restrictive loan agreements. Obtaining a loan exceeding the value of the company's assets within the framework of project financing is possible if several conditions are met:

- The industry in which the borrower operates is very stable and shows good development prospects (for example, the renewable energy sector).
- The borrower receives guarantees from partners or the contract includes other conditions for recapitalizing the company in the event of certain events.
- The syndicated loan is secured not only by all the assets of the given company, but also by the future cash flows of the project. In addition, banks usually reserve the right to unblock subsequent loan tranches only when certain events occur. For example, the allocation of the next part of funds becomes possible after the completion of a certain stage of construction. Such agreements are usually concluded for significant amounts of financing, incomparably larger than in the case of traditional loans received from one bank. This is explained by the concentration ratios established by law per organization and the internal policy of banks regarding financing a specific sector.

In the case of a large loan, one bank may not be able to provide sufficient funds to implement the project on its own. The first reason is that the bank runs the risk of violating the legislation, which in some countries imposes strict limits on the concentration of funds for one legal entity or even a sector. On the other hand, each bank develops its own procedures (some of them even more stringent than national laws) that govern how much funds can be allocated to a particular enterprise or sector. For the combination of these reasons, banks are showing a willingness to organize syndicates in large projects. An exception to the rule is financing provided in recent years by some Chinese banks, for which it is generally considered unusual to finance large investments by a single institution. Examples of this approach are financing telecom projects in Europe and financing large mining sector projects in Africa and South America. However, these decisions are often made in a centrally controlled economy and are usually aimed at bringing certain products to this market (usually projects are associated with Chinese manufacturers).

In the European context, the amounts of syndicated loans range from several tens of millions to several billion Euros. The largest syndicated loans in the EU are usually issued in the energy and infrastructure sectors, where the loan amount can exceed 1 billion Euros. Such large amounts require special conditions for the distribution of funds and control over their subsequent use. These conditions are determined long before the conclusion of the loan agreement itself and require special preparatory measures.

The literatures on this type of external financing refer that [6] the role of a financial advisor in obtaining a syndicated loan is important. High-quality preparation and organization of project financing is the first and most significant step in this process. Company managers need to understand that preparation determines the subsequent success of the entire operation, and the better company is adapted to the demands of the financial markets, the sooner and on better terms the process will be completed. When the company first enters the syndicated finance markets with a major project, it is advisable to hire a financial advisor from the start. In the global level, such advisory functions are performed by renowned European and American banks such as Merrill Lynch, Goldman Sachs, JP Morgan, Citibank, Deutsche Bank, RBS, West LB and many other world famous brands. In addition, businesses can hire a financial advisor from companies that are professionally engaged in such activities, such as Deloitte & Touche, Ernst & Young, PricewaterhouseCoopers, TDI Corporate Finance, etc. Of course, the cost of such services from market leaders can be

very high. These companies are ready to provide businesses with a full range of advisory services, including financial modeling, selection of optimal funding sources and assistance in obtaining a syndicated loan on favorable terms. The financial advisor is usually selected through a competition announced by the company. His role is to guide the company through the entire financing process in an optimal way. However, this is often limited to optimization of the financing structure without legal advice. The consultant's fee depends on the loan amount. For the largest loans of about 1 billion euros, this fee can amount to hundreds of thousands of euros. The advisor's excellent knowledge of the financial market (both domestic and international) will be an advantage for the borrowing company. The role of a financial advisor in obtaining a syndicated loan:

- Conducting a detailed analysis of the financial market. Choosing the most appropriate moment to enter the market to obtain a loan on the best terms.
- Selection of alternative sources of financing for the project, which will supplement or replace the syndicated loan. Determination of the most suitable banks or financial institutions to manage funds. Providing a list of institutions interested in the project.
- Professional assistance in drawing up a business plan at the request of the bank. Execution of official documentation and negotiations with interested parties. Only companies that have experience in syndicated financing or are part of an international group using such financing can enter the market without the assistance of a financial advisor.

If it comes to the stages of obtaining a syndicated loan for a large project, most of the financiers and economists note that there are several main stages for it and they are given below [7]. In fact, in foreign practice, preparing documents and arranging syndicated financing usually takes more time than applying for a loan from one bank. A simple contract with standard market terms can take up to 3 months to prepare, while more complex options can take 6 months or more. At this stage, a professional financial consultant helps to clearly divide the organizational process into several stages with deadlines for their implementation. In general, the stages of obtaining a syndicated loan include:

- Hiring a financial advisor (optional).
- Selection of proposals, selection of the organizing bank for the consortium and signing of a mandate letter (a document authorizing this bank to organize a syndicate on agreed terms). In some cases, it is possible to sign an underwriting letter, a document guaranteeing a company to organize financing on agreed terms.
- Drawing up a project financing schedule, taking into account the specifics of a particular business, technical and other possibilities for the implementation of a particular project.
- Prepare a term sheet, a document that contains a funding request detailing the financial needs of the borrower.
- Preparation and signing of an information memorandum.
- A syndication process for arranging financing on specified terms.
- Selection and signing of an agreement with a law firm.
- Development of a loan agreement and approval of collateral.
- Obtaining the necessary official and legal approvals.
- Signing the agreement.

Bank requirements depend on many factors, including the following:

- The size and position of the company in the market.
- The amount of the syndicated loan and its maturity.
- History of cooperation with agent bank.

The agent bank is the financial institution through which the company contacts the rest of the syndicate. Thus, the bank acts as a coordinator between the borrower and the funding banks. The agent charges a commission for this service. This commission is also negotiated before signing the loan agreement and usually does not exceed 100 thousand euros per year, which is quite a sufficient amount for a large syndicate. Further responsibilities of the borrowing company should include maintaining certain financial ratios within specified limits.

In fact, the syndicated loan provides stable financing at relatively low costs. Preparation in this case is extremely important, since the subsequent success of the entire operation often depends on professional planning and competent

paperwork. When using syndicated financing, companies should maintain certain ratios within specified limits. These actions are in the best interests of the business as it will minimize subsequent costs[8].

Methodology of the research

The methodology includes historical analyzes, systematic analyzes, and graphic methods. Statistics have been made by the help of official statistics of Uzbekistan

Results

Conducted researches revealed that during the last years significant projects like blockchain-based projects, renewable energy-based projects and other green environment-based projects are being financed with the help of syndicated loan as they are big and new projects that's why they require large amount of investment and long time to cover its expenses and syndicated loans are the best options for these kind of projects.

It should be noted that in the domestic level, syndicated loans are not as well-known in above mentioned areas because these fields themselves are new for Uzbekistan as our country is one of the developing countries of the world. However, syndicated loan is developing year by year in financing of both local and foreign investment projects in our country and government has also been supporting this sector. In fact, center to initiate the syndicated crediting set up in accordance with the Decree of the President of the Republic of Uzbekistan dated November 7, 2007, №PD-726 "On measures for further development of banking system and implication of available assets to the banking turnover." [9]

In accordance with the objectives set in the above decree, the Centre developed the Regulation "On the center to initiate the syndicated credit," which detailed services and how they are implemented and cooperation with commercial banks.

Each made up regulations for the implementation of the syndicated crediting, refined the procedure and rules for the development of such documents as business plans for investment projects in sectors of the economy, feasibility studies, technical design and so on. Also signed a general agreement with "Qishloq Qurilish bank ", " SAVDOGARBANK ", "Asaka " "Uzsanoatkurilishbankom", "Halkbank", " Microcredit ", " Ipotekabank ", " Turon ", " Capitalbank " and the bank of " Credit Standard " for implementation services related to the organization and the conclusion of the syndicated credit agreements and to establish the Syndicate[9] . More than 200 specialists of commercial banks have been trained at the Center organized seminars and conferences on syndicated lending.

Given that syndicated credits related mainly to large investment projects, along with the work being done with banking professionals need at this stage to continue the preparatory and outreach to customers of banks.

Following figure 1 provides information on two major businesses of Uzbekistan that is planning to use foreign syndicated loan in their businesses

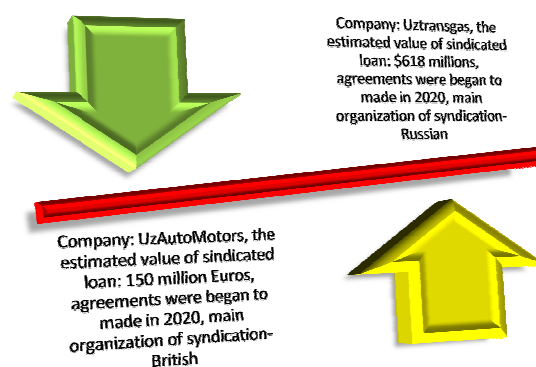


Figure1

Two major businesses of Uzbekistan that is planning to use foreign syndicated loan in their businesses[10].

It should be also stressed that almost every bank of the Republic of Uzbekistan have been actively participating in the processes of syndicating the loans for the investment projects in the country. Following figure2 gives data about the main banks of Uzbekistan that provide syndicated loan.

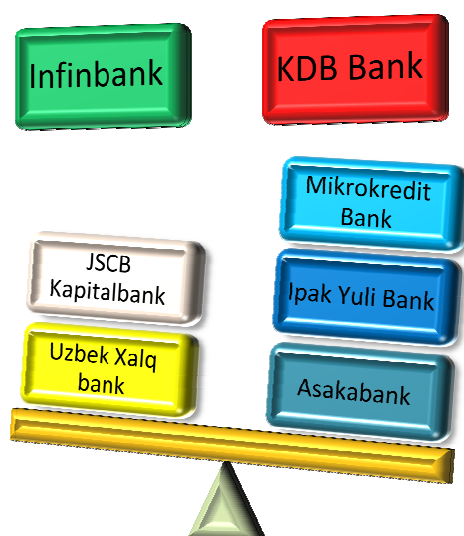


Figure 2

Main banks of Uzbekistan that provide syndicated loan[10]

Conclusion

In conclusion, it can be stated that syndicated loans arise when a project requires too large a loan for a single lender or when a project needs a specialized lender with expertise in a specific asset class. Syndicating the loan allows lenders to spread risk and take part in financial opportunities that may be too large for their individual capital base. For suggestion for further developments in this sector, we can say followings:

- More projects that are brand new for our local market should be implemented;
- Government should support this sector by imposing new laws to develop banks ;
- Foreign collaborations on syndicating investment project should be encouraged .

References

1. Based on the information of www.worldbank.org
2. Mugasha 'The Law of Multi-bank Financing' Chapters 1 and 3, (2007) OUP
3. Based on the data of <https://esfccompany.com/en/articles/economics-and-finance/syndicated-loan-for-business/>
4. Taylor, Alison; Sansone, Alicia (2007). *The Handbook of Loan Syndications & Trading*. New York: McGraw-Hill. ISBN 0-07-146898-6
5. *Habibsons Bank Ltd v Standard Chartered Bank (Hong Kong)* [2010] EWCA Civ 1335
6. Allen, T (1990): "Developments in the international syndicated loan market in the 1980s", Quarterly Bulletin, Bank of England, February.
7. Pennacchi, G (2003): "Who needs a bank, anyway?", Wall Street Journal, 17 December.
8. Dennis, S and D Mullineaux (2000): "Syndicated loans", Journal of Financial Intermediation, vol 9, October, pp 404–26.
9. Based on the information of <https://uba.uz/en/about/organizations/center-for-the-initiation-syndicated-crediting/>
10. Based on the information of www.cbu.uz