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Analysis of the Current State of Bond Financing of Industrial Enterprises in Uzbekistan and Development Prospects

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Abstract

Corporate bonds are integral to the financial strategies of industrial enterprises, providing vital avenues for capital mobilization and investment diversification in global markets. The emergence of exchange bonds represents a significant evolution in bond issuance practices, offering companies expedited access to capital with reduced bureaucratic barriers. Moreover, a novel approach gaining traction involves linking bond income to the country's monetary policy, such as the refinancing rate, thereby aligning returns with macroeconomic conditions. This mechanism enhances bond attractiveness by providing investors with predictable income streams tied to economic stability. This paper explores the impact of exchange bonds on market dynamics, particularly focusing on liquidity and volatility in secondary bond markets. By analyzing the implications of integrating monetary policy into bond income mechanisms, it seeks to elucidate how these innovations influence investor behavior and market performance. Understanding these dynamics is crucial for stakeholders navigating modern financial landscapes, offering insights into optimal investment strategies and risk management practices.

Keywords: *Corporate Bonds; Exchange Bonds; Monetary Policy; Refinancing Rate; Investor Interest; Secondary Market; Liquidity; Volatility*

Introduction

Corporate bonds serve as pivotal financial instruments for industrial enterprises, providing essential avenues for capital acquisition and investment diversification in global financial markets [9]. In recent years, the issuance of exchange bonds has emerged as a strategic mechanism for companies to swiftly access new capital and direct it toward strategic initiatives. Unlike traditional corporate bonds, exchange bonds streamline the issuance process, minimizing bureaucratic hurdles and accelerating market entry. Moreover, the linkage of bond income to the country's monetary policy, such as the refinancing rate, presents a novel approach to enhancing bond attractiveness among investors [8].

The integration of monetary policy in bond income mechanisms aligns returns with macroeconomic conditions, offering investors a predictable income stream tied to economic stability. This approach not only enhances market appeal but also has the potential to significantly increase investor interest, thereby influencing liquidity and volatility in secondary bond markets.

This paper explores the evolution of corporate bonds, particularly focusing on the introduction and impact of exchange bonds in enhancing liquidity and volatility in secondary markets. It examines the implications of linking bond income to monetary policy and discusses potential future trends in bond issuance strategies. By analyzing these factors, this study aims to contribute to the broader discourse on financial market dynamics and investment strategies.

Literature Review

Corporate bonds play a critical role in financing strategies for industrial enterprises, providing avenues for raising capital beyond traditional bank loans [1]. The evolution of bond issuance practices has seen the emergence of exchange bonds, which streamline the process of accessing capital by reducing administrative burdens and accelerating market entry [2]. These instruments have been pivotal in enhancing liquidity and market participation for issuing companies [3].

The attractiveness of corporate bonds is further bolstered by mechanisms linking bond income to monetary policy indicators such as the refinancing rate. This approach aligns bond returns with broader economic conditions, providing investors with predictable income streams tied to economic stability [4]. Research indicates that such linkage enhances investor confidence and may contribute to increased market activity in secondary bond markets [5].

Furthermore, studies highlight the importance of regulatory frameworks and credit ratings in shaping investor perceptions and market behaviors toward corporate bonds [6]. The presence of credible credit ratings from agencies like S&P Global Ratings and Moody's is crucial for establishing investor trust and facilitating bond market liquidity [7].

In summary, the literature underscores the transformative impact of exchange bonds and the integration of monetary policy in bond income mechanisms on financial market dynamics. These developments not only enhance market efficiency but also offer strategic advantages for companies seeking capital and investors seeking stable returns amidst economic fluctuations.

Analysis

The practice of bonds in our country began to develop in the past five years. Before that, all clauses and information about this instrument were included in the legal bases, but in practice, trading with bonds dates back to the era of New Uzbekistan. The initial bonds were Eurobonds issued in 2019 on behalf of the State of Uzbekistan on the London Stock Exchange, although not in the Tashkent RFB. These Eurobonds consisted of two tranches of $500 million each, with five-year and ten-year maturities, totaling $1 billion. The yield on the $500 million five-year bond is 4.75% per annum, and on the $500 million ten-year bond is 5.375%. As investors of the first-time Eurobonds, the majority of the five-year and ten-year debt bonds were held by UK investors (39% and 32%), US investors (23% and 31%), investors from the rest of Europe (32% and 27%), and investors from Asia, the Middle East, and North African countries (6% and 10%).[1]

After the successful issuance of the first Eurobonds, in November 2020, an additional $750 million worth of Eurobonds were placed.[2]

Also, in 2023, for the first time in the history of Uzbekistan, green sovereign international bonds amounting to 4.25 trillion soums and international bonds amounting to 660 million dollars were placed on the London Stock Exchange. Due to the high demand for "green" bonds in the national currency of the

[1] https://telegra.ph/The-Republic-of-Uzbekistan-inaugural-US1bn-Dual-Tranche-144aReg-S-Bond-Offering-02-14
[2] https://www.bloomberg.com/news/articles/2020-11-19/a-rare-nation-dodging-virus-recession-returns-to-eurobond-market

Republic of Uzbekistan, it was possible to reduce the interest rates (coupon payment) of the three-year soum international bonds from the expected 18% to 16.25%. With this transaction, international bonds amounting to 1.9 trillion soums, whose maturity date was November 23 of 2023, were prematurely redeemed.[3]

The participation of national companies in the stock market with bonds dates back to this period. In 2020, Law No.629, signed by the head of state, introduced amendments and additions to the Law "On the Securities Market." This allowed not only commercial banks and joint-stock companies but also limited liability companies to issue corporate bonds in compliance with the following procedures.[4]:

Corporate bonds are subject to the following conditions:

- Within the amount of the issuer's own capital on the date of the decision to issue such bonds. If the amount of corporate bonds exceeds the issuer's equity capital, the issuer must provide security for the increased amount;
- Issued by issuers with positive indicators of profitability, solvency, financial stability, and liquidity in the last year;
- Issued when there is an audit report on the financial statements for the year before the bond issue;
- Issued with the participation of commercial banks acting as payment agents for the payment of funds belonging to investors by issuers.

Infrastructure bonds are subject to the following conditions:

- Within the amount of the issuer's own capital on the date of the decision to issue such bonds. If the amount of infrastructure bonds exceeds the issuer's equity capital, the issuer must provide security for the increased amount;
- Issued when there is an audit report on the financial statements for the year before the bond issue;
- Funds from the placement of infrastructure bonds are released if they are used to finance the project provided for by the decision of the President of the Republic of Uzbekistan or the Cabinet of Ministers of the Republic of Uzbekistan.

Infrastructure bonds are issued by economic societies with a state share of 50 percent or more, as well as state enterprises, in agreement with the Ministry of Finance of the Republic of Uzbekistan.

Additional conditions for issuing corporate and infrastructure bonds are determined by the authorized state body for the regulation of the securities market.

According to the 2019 annual report of the Tashkent RFB, until 2019, the number of issuers participating in stock exchange trading with corporate bonds was 2, and this law opened the way to the stock exchange for many companies. As a result, in 2020, their number reached 4, in 2021, 5, and in 2022 and 2023, 7. In the history of the bond market of Tashkent RFB, the number of industrial enterprises that issued this instrument was only 2: "Uzbekistan Metallurgical Combine" Joint-Stock Company and "Artel Electronics" LLC (Table 1).

It should be noted that volatility and sharp movements of instruments are almost not observed in the bond market. For comparison, 23 bond packages of 13 companies were issued in the KASE stock exchange of neighboring Kazakhstan during 2023, the total amount of which was equal to 1,226 million US dollars. In the stock market of Uzbekistan in 2023, the volume of transactions of bonds of 5 companies traded through a total of 70 transactions amounted to 58.7 thousand US dollars.

[3] https://www.imv.uz/news/category/yangiliklar/post-1621

Table 1. Statistics of bond sales at Tashkent RFB (2021-2023 years)

No	Company	Ticker	Number of transactions, pcs	Number of securities, pcs	Volume of transactions, in soums
2021					
1	Uzmetkombinat JSC	UZMB2	11	10000	50610920000,00
2022					
2	ARTEL ELECTRONICS LLC	AREL1	1	100	10000000000,00
		AREL2	1	100	10000000000,00
		AREL3	5	100	10000000000,00
3	Uzmetkombinat JSC	UZMB2	1	10000	98609408,72
2023					
4	Asia Alliance Bank JSB	AABK1	7	45175	25000000,00
5	Biznes Finans Mikromoliya Tashkiloti LLC	BFMT3	14	6565	30170369,00
6	Imkon Finans Mikromoliya Tashkiloti LLC	IMKF3	42	6000	218357709,66
7	Uzagroleasing JSC	UZAL2	1	50000	20300000,00
8	Chust Rir Mikrokredit Tashkilot LLC	CRMT3	6	2000	448000000,00

Source: Prepared by the author based on the analysis of scientific literature

We will consider the analysis and problems of bond issuance using the example of the Joint-Stock Company Uzbekistan Metallurgical Combine. Uzmetkombinat JSC was the first industrial enterprise in Uzbekistan to issue corporate bonds and successfully implemented their issue and placement on the stock exchange. The company's corporate bonds were sold to investors in December 2021 under the registration number UZ6021727AA1 on the "Nego Board" trading platform of the Tashkent RFB. The following tables provide complete information on this placement (Table 2, Table 3).

Table 2. Information on corporate bonds issued and placed by Uzmetkombinat JSC

Offer parameters	
The volume of the offered bonds, billion soums	50,0 bln soum
Duration	18 months or 543 days
Lot size	at least 1 %
Annual interest rate of the bond, in %	22,0 %
Date of receipt of applications:	till 16.12.2021
Demand parameters	
Number of applications received	12
Amount of received applications, billion soums	478,5 bln soum
The volume of received applications is equivalent to a million US dollars	44,31 mln $
Request for proposal	957 %
42.22 percent of the received applications came from non-residents	

Results of placement of corporate bonds	
Number of satisfied applications	11
Volume of satisfied applications, billion soums	50,61 bln soum
Volume of satisfied applications, equivalent to millions of US dollars	4,69 mln $
The volume of satisfied applications, % compared to the plan:	100,0 %
The minimum selling price of the bond is in % of the nominal value	101,2218 %
Annual interest rate of the bond, in %	22,0 %

Source: Prepared by the author based on information from the official website of Uzmetkombinat JSC

Table 3 .Information on placement of corporate bonds issued by Uzmetkombinat JSC on the stock exchange

Placement conditions	
Date of transaction	24.12.2021
Placement Date (T+2)	28.12.2021
Term	1,5 years (543 days)
Announced placement size	50,0 bln soum
Lot size that one investor can purchase	at least 1 %
Order type	Limited
Date of receipt of applications:	till 16.12.2021
Date of approval of applications:	17.12.2021
End date:	17.12.2021
Deposit closing date:	22.12.2021
The method of satisfying incoming applications:	distribution of bonds in proportion to the volume of all accepted applications (but at least 1% of the volume of the issue)
Trading Broker:	“Freedom Finance” LLC FC

Source: Prepared by the author based on information from the official website of Uzmetkombinat JSC

Taking into account that in 2021, the average interest rate of deposits in commercial banks of Uzbekistan is 20 percent, and the term is at least 18 months, we understand that these bonds were quickly sold in the market with great interest and demand[5]. However, from an economic point of view, if an investor receives 1% of this bond issue, this amount equals 500 million soums, indicating that retail investors participate in the stock market with such a large amount. This implies that the majority of investors who bought the company's bonds are legal entities.

Discussion

Based on this trend, another type of corporate bonds issued by companies in foreign countries — stock exchange bonds — has become increasingly popular in recent years. Exchange bonds are a type of company bond that is sold to investors through open trading by placement on the stock exchange in a simplified manner. Exchange bonds are also a type of corporate bond that is listed on the stock exchange in a simplified manner and sold to an unlimited number of investors through public auctions. The difference between corporate and exchange bonds is presented in the table below (Table 4).

[5] https://www.spot.uz/oz/2021/06/01/depozit/ - The most profitable deposits in Uzbekistan banks in June 2021

Table 4. Difference between corporate and stock bonds

Corporate bonds	Stock bonds
Differences according to issuers	
Corporate bond issuers are private companies. They issue bonds to raise capital to finance their operations, investments, expansion, etc.	Exchange bonds can be issued by various issuers, including corporations, government agencies, local governments, and others. They are traded on the stock exchange and can be bought and sold by a wide range of investors.
Sales processes	
Corporate bonds can be sold over-the-counter (on the trading floor) in the market or on specialized bond trading platforms.	Exchange bonds are traded on organized (common) stock exchanges, where they are traded among investors like stocks.
Liquidity and transparency	
The liquidity and transparency of corporate bonds is lower than that of stock bonds due to limited access to markets and information.	Exchange bonds typically have a high degree of liquidity and transparency because they are traded on public exchanges where price and volume information is available to a wide range of investors.
Standardization	
Corporate bonds may be less standardized in their terms and structure than stock bonds.	Exchange bonds often have standardized terms and are easier to analyze and compare.
Market risks	
Investors in corporate bonds are exposed to market risk related to the credit rating and financial condition of the issuer.	Market risk for exchange bonds may also include interest rate risk and inflation risk, but credit risk may be less significant due to standardization and liquidity.

According to the legislation of the Republic of Uzbekistan, stock bonds are debt emission securities issued by joint-stock companies, whose issue is registered by the stock exchange and included in the quotation sheet of the stock exchange. Based on the definition given in the legislation, we believe that stock exchange bonds can be considered examples of corporate bonds.

Exchange bonds can be issued in the form of discount and coupon bonds. The income from a discount bond is generated by buying it below par, and the profit is defined as the difference between the selling price of the bond and the par value. Income on coupon (interest-bearing) bonds is generated by the timely payment of interest determined based on the terms of issuance.

Although this financial instrument is included in the legislation, no company in the history of Uzbekistan has applied to issue this type of bond. Below, in addition to the general differences between corporate and stock bonds, we will discuss the advantages of stock bonds (Table 5).

Table 5. Advantages of exchange bonds over corporate bonds

	Corporate bonds	Exchange bonds
Registration	It is registered by the state organization	It is not registered by the state organization
Review period	30 days	14 days
Term of satisfaction of the bond	More than a year	In less than a year
Deployment period	Not more than one year	In no more than one month
Fees for state registration of the primary issue of securities	Securities to be issued amount to 0.01% of their nominal value	No fee is charged

Based on this, if Uzmetkombinat JSC had issued its corporate bonds in 2021 as exchange bonds, several advantages would have been realized due to the absence of state registration fees for the issue prospectus, minimal bureaucratic procedures, and the shorter issuance period, potentially yielding better results by the end of 2021.

Furthermore, exchange bonds possess the following characteristics:

1. Expansion of the short-term debt market: There is currently a lack of short-term financial instruments in the local market, with even bank loans typically having durations longer than one year. Introducing exchange bonds into the trading space would enhance market liquidity by channeling investor capital into short-term debt instruments.
2. Ability to quickly replenish working capital for listed companies: With the issue prospectus for exchange bonds being registered in a short timeframe, companies can swiftly commence bond sales and attract investors. This rapid process enables companies to significantly bolster their working capital balances within two months.
3. Quotation requirements: Exchange bonds are issued by joint-stock companies listed in the "Premium" and "Standard" quotation categories of the "Stock Market" and/or "Bond Market" segments of the Tashkent RFB. Unlike other bond types that require inclusion in the "Bond Market" quotation list, listing of shares in any quotation list suffices for issuing exchange bonds.
4. Requirement for credit rating: Companies issuing exchange bonds must hold a current credit rating not lower than "B+", "B-", or "B3" categories as assessed by rating agencies such as S&P Global Ratings, Fitch Ratings, or Moody's.

Before issuing any bonds to the market, companies undergo an assessment of their financial condition and ability to fulfill debt obligations by rating agencies. Specifically, if bonds are to be issued on foreign stock exchanges, one requirement for inclusion in the quotation is a rating from one of the top three rating agencies: S&P Global Ratings, Fitch Ratings, or Moody's. The company must achieve a rating in categories such as "B+", "B-", or "B3," which represent the lowest levels of creditworthiness.

5. Completion of placement of exchange bonds within the period specified in the decision on their issuance, but no later than one month from the commencement of the placement of these bonds.

This procedure ensures the rapid introduction of new financial instruments to the market and serves as a basis for increasing bond sales in the secondary market.

It is advisable to establish the following procedures for issuing exchange bonds:

1. The authorized fund of the issuer should be at least 100 billion soums.
2. The issuer must have been established for at least one year.
3. The issuer should not have defaulted on any bonds issued in the previous period.
4. The issuer must have a current credit rating not lower than "B+", "B-", or "B3" categories issued by recognized rating agencies.
5. The nominal value of each issued bond should be no less than one million soums, and the total volume of the bond issue should be at least 1,000 bonds.
6. The company's financial indicators, including profitability and financial stability, must be positive.

In general, the issuance of exchange bonds provides industrial companies with a means to swiftly acquire new capital funds and allocate them as needed.

Another approach to enhancing the appeal of corporate bonds is linking their returns to the country's monetary policy. Specifically, tying annual bond income to the nation's inflation rate or refinancing rate presents an enticing mechanism for attracting investors. To implement this, the following formula is proposed for issuing and calculating annual bond income:

$$Income_{Bond} = Interest\ rate + 10\%$$

In the future, issuing corporate bonds based on this income mechanism may lead to a notable increase in liquidity and volatility in secondary bond markets, driven by heightened investor interest.

Conclusion

This paper has explored the evolving landscape of corporate bonds, with a particular focus on the emergence and impact of exchange bonds and their linkage to monetary policy indicators. Exchange bonds have proven instrumental in streamlining capital acquisition processes for industrial enterprises, facilitating quicker access to funds with reduced administrative burdens. The integration of bond income mechanisms with monetary policy, such as the refinancing rate, has aligned investor returns with broader economic conditions, thereby enhancing market predictability and stability.

Key insights from the literature review highlight the transformative potential of these innovations in enhancing market liquidity and investor confidence. Recommendations for policymakers include further enhancing regulatory frameworks to support the issuance and trading of exchange bonds, ensuring transparency and investor protection. Educators are encouraged to incorporate these developments into financial curriculum to prepare future professionals for navigating dynamic bond markets.

Future research directions could explore the long-term effects of bond income linkage on market dynamics, including its impact on risk management strategies and investor behavior. Additionally, comparative studies across different regulatory environments and economic contexts could provide valuable insights into the scalability and applicability of these mechanisms globally.

In conclusion, the evolution of corporate bonds towards more efficient and transparent issuance practices, coupled with their integration with monetary policy, represents a significant advancement in financial market dynamics. By leveraging these insights, stakeholders can foster greater market resilience and sustainability in the face of evolving economic challenges.

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