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THE USE OF MODERN BANKING INSTRUMENTS IN SMALL BUSINESS LENDING: DEVELOPMENT TRENDS IN GUARANTEE FUNDS, FACTORING, LEASING, AND MICROCREDIT

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Abstract. This article examines several issues related to the current state of lending to small businesses and private entrepreneurship in the Republic of Uzbekistan, as well as potential areas for improving the existing mechanisms of guarantee funds and leasing as instruments of financial support for small businesses.

Keywords: guarantee fund, leasing services, lending, credit risk, collateral, credit history, interest rate.

Аннотация. В статье рассматриваются отдельные проблемы, связанные с современным состоянием кредитования субъектов малого бизнеса и частного предпринимательства в Республике Узбекистан, а также возможные направления совершенствования действующих механизмов гарантийных фондов и лизинга как инструментов финансовой поддержки малого бизнеса.

Ключевые слова: гарантийный фонд, лизинговые услуги, кредитование, кредитный риск, залоговое обеспечение, кредитная история, процентная ставка.

INTRODUCTION

In the contemporary economy, small business entities play an important role as one of the key structural components of an economic system based on free-market relations. Small businesses are characterized by their ability to respond rapidly and flexibly to changing conditions in both the external and internal environment. This flexibility contributes to the development of a competitive environment, facilitates the structural transformation of the economy, and promotes the development of production systems based on innovative technologies.

The banking sector plays a particularly important role in the development of small businesses in the Republic of Uzbekistan, as banks provide the financial services necessary for the efficient operation of business entities. At the same time, a number of challenges need to be addressed in order to strengthen the effectiveness of banking support for small businesses.

At present, obtaining long-term bank financing remains relatively difficult for small businesses, particularly for newly established enterprises, because they often lack sufficient assets that can be pledged as collateral for borrowed funds. In addition, financing small business entities is associated with relatively high administrative and transaction costs for commercial banks.

The Development Strategy of New Uzbekistan for 2022–2026, approved by Decree No. PF-60 of the President of the Republic of Uzbekistan dated 28 January 2022, identifies the creation of conditions for generating sustainable sources of income for business entities as an important prerequisite for the country's sustainable economic development. The Strategy also provides for increasing the private sector's share in gross domestic product to 80 percent and its share in exports to 60 percent, as well as reducing the tax burden on business entities from 27.5 percent to 25 percent of GDP by 2026 [2].

Furthermore, Resolution No. PQ-366 of the President of the Republic of Uzbekistan dated 15 November 2023, "On Additional Measures to Widely Engage the Population in Small and Medium-Sized Business," provides for the establishment of a system of financial and advisory support for business initiatives through the training of individuals and business entities. The Resolution also aims to create the necessary conditions for expanding entrepreneurial activity along the chain of "family entrepreneurship – microbusiness – small

business – medium-sized business.” In addition, measures have been introduced to support small and medium-sized business projects through an integrated system comprising the Business Development Bank, the Entrepreneurship Development Company, and partner commercial banks [3].

On this basis, relevant resolutions of the President of the Republic of Uzbekistan have defined measures aimed at increasing the accessibility of microfinance services, supporting entrepreneurial initiatives among broad segments of the population, and strengthening the financial support provided by non-bank credit institutions to small businesses. Target indicators and the volume of resources to be allocated for lending to small business entities and providing microfinance services in 2024 have also been established.

LITERATURE REVIEW

In his dissertation research devoted to improving lending practices for small business entities, economist I. Alimardonov proposed enhancing the methodology for assessing the creditworthiness of small businesses by supplementing the existing system of financial ratios with profitability ratios, the debt-service coverage ratio, and the accounts payable turnover ratio.

Researcher I. Rakhmonov substantiated several possibilities for improving commercial banks' microfinance practices for small business entities. In particular, he proposed reducing by 50 percent the mandatory reserve requirement established by the Central Bank for commercial banks' term deposits attracted for periods of up to one year, provided that the released funds are allocated in the form of microcredits. He also proposed exempting term deposits of microfinance institutions placed with commercial banks from the Central Bank's mandatory reserve requirements.

According to foreign economist A. Stakhnyuk, the main factors limiting small businesses' access to commercial bank lending include the insufficient development of mechanisms for supporting small businesses, the low quality of collateral, the lack of transparency in clients' business activities, and the shortage of financial resources required for investments in the real sector with maturities exceeding one year, particularly affordable and long-term funding.

American scholar J. Sinkey notes that commercial banks occupy a leading position in the provision of financial services to small businesses in the United States. Within the range of financial services provided to small business entities, term loans, leasing finance, and lending through credit lines play an important role.

N. Yamori analyzed the importance of the public credit guarantee system in financing small businesses and entrepreneurship in Japan. Before approving loans to small business entities, financial institutions generally require applicants to submit an application to a Credit Guarantee Corporation (CGC), which provides guarantees designed to facilitate access to bank financing.

RESEARCH METHODOLOGY

The study employed expert assessment, comparative analysis, structural analysis, and trend analysis methods. The empirical basis of the research consisted of statistical data from the Central Bank of the Republic of Uzbekistan on lending to small businesses, as well as relevant regulatory and legal documents governing small business financing.

ANALYSIS AND RESULTS

Lending to small business entities is one of the priority areas of commercial banks' credit activity in Uzbekistan. This reflects the significant role of small businesses in the country's economic development and the financial support provided by the state to facilitate their access to credit.

At present, the main sources of funding for loans extended by commercial banks to small business entities include attracted deposits, foreign credit lines, state budget resources, and funds from extra-budgetary institutions.

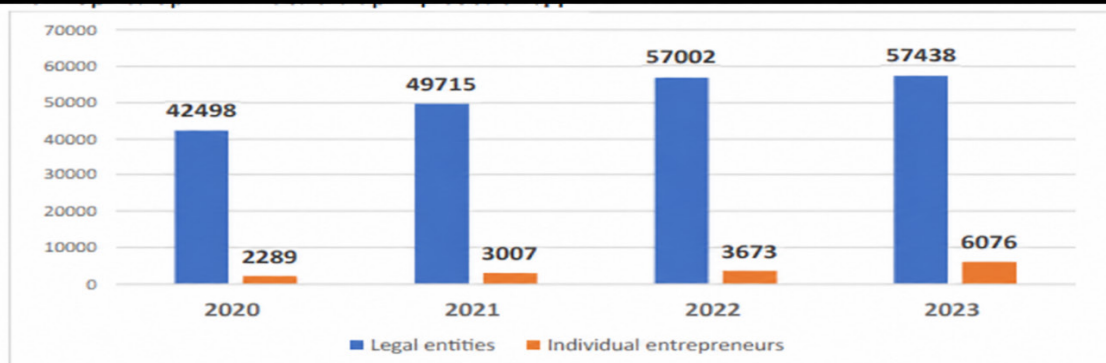


Figure 1. Loans Extended by Commercial Banks of the Republic of Uzbekistan to Small Business Entities with Legal Entity Status and Individual Entrepreneurs, UZS Billion¹.

As shown in Figure 1, the volume of loans extended by commercial banks in Uzbekistan increased during 2021–2023 both for small business entities operating as legal entities and for individual entrepreneurs.

Practical experience indicates that the successful development of small businesses largely depends on their access to both long-term and short-term financial resources. At present, Uzbekistan's credit market remains at a stage of institutional development and is characterized by a relatively limited range of financial instruments and services. The insufficient development of non-bank financial institutions further constrains the availability of financing for the real sector of the economy.

Among the main factors limiting the development of financial services, particularly lending services, experts emphasize relatively high credit risks and the lack of sufficient collateral among potential borrowers. This issue is especially relevant for newly established businesses, as the formation of fixed assets that can subsequently serve as reliable and readily realizable collateral generally requires a relatively long period of business activity.

International experience demonstrates that credit guarantee mechanisms can help address these constraints. As noted by N. Yamori in the case of Japan, financial institutions may require small business borrowers to apply to a Credit Guarantee Corporation (CGC) before a loan is approved. Once the CGC agrees to provide a guarantee, the financial institution may proceed with the loan. In addition to interest payments, borrowers pay a guarantee fee through the bank. If a borrower defaults, the lending institution may claim compensation from the CGC in accordance with the applicable guarantee arrangements.

In Japan, credit guarantee institutions are supported by the national and local governments through subsidies, financial contributions, and insurance mechanisms involving the Japan Finance Corporation. The credit guarantee system is primarily designed to facilitate access to finance for small businesses, although eligible borrowers must satisfy certain requirements related to business size, sector, and other established criteria.

A similar institutional approach to credit guarantees has also been introduced in Uzbekistan, with mechanisms established to support small businesses by facilitating their access to bank financing and reducing collateral-related constraints. The Fund was established as a joint-stock company with regional branches and was assigned several key functions. These included providing guarantees for the portion of commercial bank loans to small businesses that was not covered by collateral, particularly for the acquisition of modern technological equipment and other investment purposes; providing advisory assistance on the terms and conditions of bank financing; supporting the establishment and expansion of high-technology and innovative production; and systematically monitoring projects supported by guarantees.

The Fund was also responsible for monitoring the timely repayment of commercial bank loans and the fulfilment of obligations arising from guarantees provided for such financing. Guarantees were issued to small business entities for the term of the relevant commercial bank loan on the basis of repayment and compensation arrangements.

For this purpose, a guarantee agreement was concluded among the Guarantee Fund, the lending bank, and the borrower. This agreement served as security for the borrower's obligations under the relevant loan or leasing agreement. However, the amount of the guarantee could not exceed 50 percent of the total loan amount or the equivalent of USD 100,000. Consequently, borrowers were still required to provide additional forms of security for the uncovered portion of the loan.

¹ **Source:** Compiled by the author based on official statistical data from the Central Bank of the Republic of Uzbekistan.



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Figure 3. Characteristics of Credit and Leasing.³

An analysis of recent trends in Uzbekistan's leasing market shows that, as of the end of 2022, leasing accounted for 2.3 percent of total fixed capital investment, while the aggregate leasing portfolio of leasing companies represented 1.4 percent of GDP.

Despite the growing number of leasing companies and the expansion of leasing services, the demand of small business entities for machinery and equipment financed through leasing remains insufficiently met. This indicates the need to further expand the institutional capacity of the leasing market, including the development of companies specializing in services for small businesses.

Given the importance of leasing as a financing instrument for small businesses and private entrepreneurship, further measures could contribute to the development of this sector. Local authorities may also introduce incentives aimed at stimulating leasing activity. One possible measure is to encourage the capitalization of leasing companies by providing tax incentives for profits reinvested in their authorized capital.

At the same time, credit guarantee mechanisms remain an important instrument of public support for entrepreneurship, as they can facilitate greater access of small businesses to bank financing by reducing collateral-related constraints.

CONCLUSION AND SUGGESTIONS

In conclusion, simplifying lending procedures for small business entities can contribute to addressing shortages of financial resources required for investment activity and working capital.

The findings of the study suggest that support for small businesses can be strengthened through the development of new credit products, simplification of loan application procedures, improvement of methodologies for assessing borrowers' creditworthiness, and broader participation of commercial banks in regional government programs. Additional measures may include partial compensation of interest expenses and the further development of credit guarantee mechanisms.

Improving the financial and credit support framework for small business entities can therefore create a stronger institutional basis for expanding their access to finance and supporting their sustainable development.

³ <https://finlit.uz/oz/articles/credit/what-is-leasing/>

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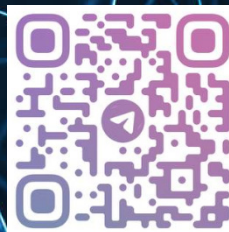
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