PROJECT FINANCING IN SLOVAK COMPANIES

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Abstract:
This paper investigates the possible resources of project financing in Slovak companies. More specifically, this paper will focus on the criteria which influence the companies by selection of resources of project financing. In order to establish a better understanding of the this problem, this paper will identify who is responsible for whole selection process of project financial resource to provide some background and depth to the research

Key Words: Project financing, financial resources, Slovak companies

Introduction

Project financing is one of a key success factor for any projects. In this research we try to identify the criteria which influence the Slovak companies by selection of resources of project financing.

According to J.D.Finnerty (2007, p. 1) project financing may be defined ”as the raising of funds on a limited-recourse or nonrecourse basis to finance an economically separable capital investment project in which the providers of the funds look primarily to the cash flow from the project as the source of funds to service their loans and provide the return of and a return on their equity invested in the project.”

A. Slivker (2011, p. 2) argues, that the project financing is “a method of financing where the lender accepts future revenues from a project as a guarantee on a loan.”

According to Ayano (2008, p. 1) project financing is “an innovative and timely financing technique that has been used on many high-profile corporate projects.”

Project financings typically include the following basic features:

1) An agreement by financially responsible parties to complete the project and, toward that end, to make available to the project all funds necessary to achieve completion.

2) An agreement by financially responsible parties (typically taking the form of a contract for the purchase of project output) that, when project completion occurs and operations commence, the project will have available sufficient cash to enable it to meet all its operating expenses and debt service requirements, even if the project fails to perform on a account of force majeure or for any other reason.

3) Assurances by financially responsible parties that, in the event a disruption in operation occurs and funds are required to restore the project to operating condition, the necessary funds will be made available through insurance recoveries, advances against future deliveries, or some other means (Finnerty, 2007).

Generally the top-managers provide a control and support of resources usage, which are supervised by a functional manager (Tukel, O.I., Belassi, W, 1996). The level of support and control has to be determined according to the needs of the industry or project specification, and always varies from company to company. One of the important issues of the top-management is to create a better communication between all managerial levels and provide a communicational support and eliminate agency conflicts and agency costs. The responsibility for the selection of financial resources is an intrinsic part of the research described in the second part of this paper.

Among the standard resources of project financing in Slovakia we can include:
- external resources,
- internal resources (own capital),
- alternative resources (for detailed description see Fig. 1).

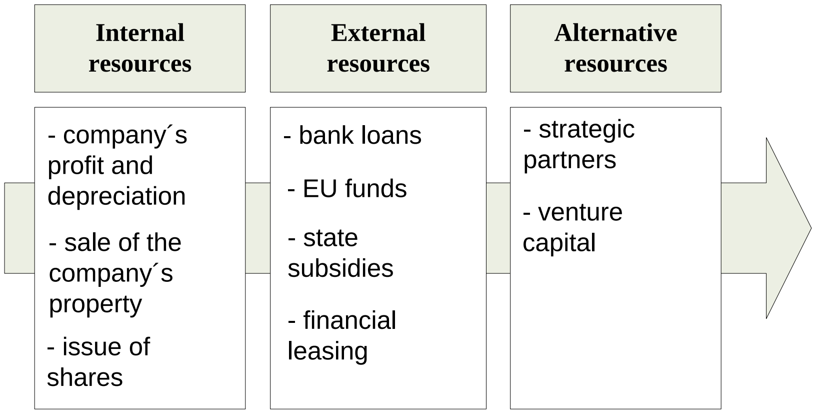

Fig. 1 Selected sources of project financing in Slovakia
Source: own processing

In practice, most projects are financed by a combination of the sources mentioned above.

Subsidy is “a benefit given by the government to groups or individuals usually in the form of a cash payment or tax reduction. The subsidy is usually given to remove some type of burden and is often considered to be in the interest of the public.” (Manteaw, 2012)

A subsidy is a financial reimbursement of contribution from the public budget – at national level (state or municipal budget) or from the EU budget at international level. The subsidies coincide with the company’s own sources – it extends the company’s own capital. Subsidies can be a significant source of project funding.

Bank loans are most used to funding of asset acquisition rather than to direct project financing. Innovative projects are connected with risks, which have to be compensating with guarantees as such as history of company, solvency, and project proposal.

In 2011, there were 14 commercial banks and 15 branches of foreign banks which operated in Slovak financial market. Nine of them offer medium- and long-term financing of construction, purchase, extension and reconstruction of real property. Documents required by the banks for project evaluation are mostly following:

- business plan stating the project description and location,
- overall project cost budget,
- project realization schedule,
- information about the permissions - planning permit, building permit,
- information about building contractor,
- ownership title and cadastral map,
- expert's opinion (in the event of existing real property),
- information about project yields,
- information about costs of real property operation,
- client's participation in the total project costs (the amount of own resources) (www.tatrabanka.sk).

Bank loans are often used by Slovak companies as a source of co-financing of the projects supported by European Union.

Financial leasing is a simple way to asset acquisition. It is suitable for small and medium sized companies with short-term history.

Issue of shares is typical for joint-stock companies. This is the method of basic capital increasing. This way of financing isn’t used in small- and medium-sized companies, which legal form is rarely in form of joint-stock company.

Venture capital is financial resource provided to growth start-up, high risk or high-potential companies. Venture capital is generally used to projects uncertain success (high risk and high valuation). Venture capital may take the form of seed financing, start-up financing or business angels.

Each project is unique, however, parts of projects may be included in the same class, for such reasons as the required resources and network of tasks. In this case, the required resources (including the financial resources) can be estimated using the past experiences of the enterprise that made the projects (Relich, 2010).

For the purposes of this paper we will use three phases within the project life cycle: project definition (initiation) and project planning, project execution and control, and the phase of project evaluation and closeout. Each of the three phases includes different tasks, behaviors and skills that are necessary to be successful. During the project initiation project manager have to initiate with the problem, create a business case which should provide the information with possible solutions of the problem and get a feasibility study. Choosing the most suitable solutions and proposing recommendations before implementation to form a project and find a people with whom the project will be run and maintain. An inherent part of the project initiation is the financial analysis of the costs and benefits including a budget. This phase includes also the selection of an appropriate way of project financing. The process of selection depends on financial conditions of each company and on the total costs of the project. The availability of the financial resources necessary to cover all project costs varies from type of the project.

Factors influencing the selection of type of resource in project financing

Our research was realized in 2012 in a sample of 79 Slovak companies and was an intrinsic part of the project VUGA N. I-11-001-05 with the title “The possibilities of project financing in conditions of Slovak companies.” The research problem in this paper is to investigate which criteria influence the Slovak companies by selection of resources of project financing.

Research Design and Data Collection

The method used in the research was in the format of a questionnaire consisting of 15 questions. The questionnaire was delivered via e-mail to Slovak companies. A comprehensive survey was design mostly for identification of criteria which influence the selection of type resource within the process of project financing. The target Slovak companies were selected randomly from various industries.

Survey Findings on project financing

Of the organizations surveyed, 43% were micro companies (< 10 employees), 22% were large companies (> 250 employees), 24% were small companies (< 50 employees) and 11% were medium-sized companies (< 250 employees). The companies were asked to identify their industry which is detailed described on the chart 1.

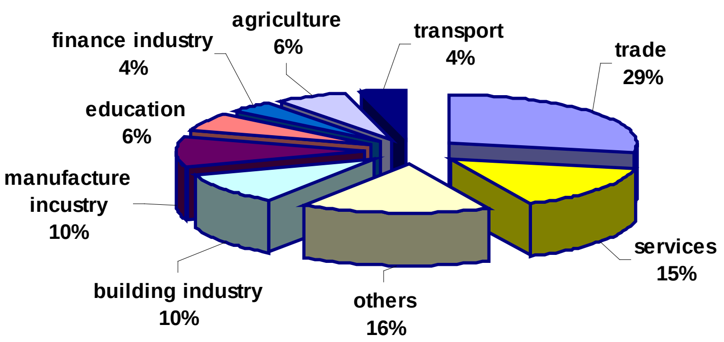

Chart 1 Types of industries of the respondents

Source: survey data

The respondents were asked to identify the number of project realized in 2011 in their companies. Most of them (29% realized one or two projects), 15% completed three or four projects and 13% finish five or six projects in 2011. These projects mainly focused on implementation of new products or systems.

The respondents were asked to identify the person responsible for whole selection process of project financial resource. A half of the respondents (50%) indicated that this person is the company director, 17% of companies stated that it is financial manager, only 8% of respondents confirmed the responsibility of project manager.

The analysis of questionnaire identified that the most important criterion for the Slovak companies by the selection of financial resources are the total costs (58%). Several respondents (19%)

stated that their own previous experience with the financial resource is important. For the rest of respondents were important for example the administrative seriousness (8%) and the experience of other companies (4%).

According to our survey 50 % of Slovak companies used in 2011 the external resources. More specifically, there were bank loans (39 %) and the resources from European Union (27 %). More detailed description we can see on the chart 2. Finally, only 36 % of the respondents preferred internal resources (80 % company's profit and depreciation) and 14 % the alternative resources.

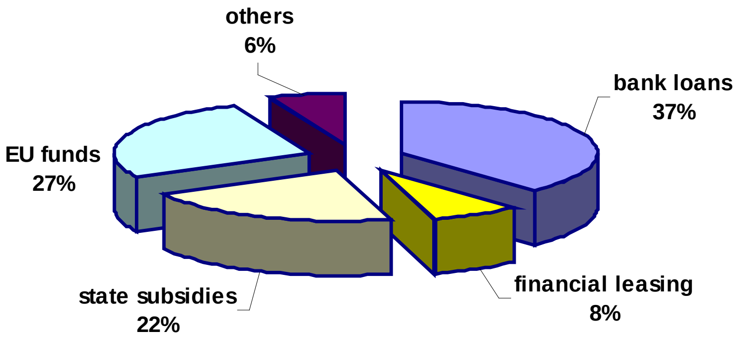

Chart 2 Types of external resources
Source: survey data

The respondents (65%) also confirmed that they are good informed about existing resources of project financing. We conclude from our research that the websites of state institutions and electronic or printed media can be considered as a relevant source of information for asked companies.

The data returned by the respondents provides some interesting information with respect to the propositions that were made in designing the questionnaire. According to the responses, the Slovak companies prefer the external financial resources and they are focused on their own experience and total costs.

Conclusion

The project financing represents a complex and difficult problem. The key objective is to select an appropriate way of project financing. It depends on financial conditions of each company and on the total costs of the project. The availability of the financial resources varies from project to project.

Project finance permits countries and companies to build new infrastructure, to develop new products or to develop new technologies. It allows increasing growth and development of each country. Without project finance, many interesting and important projects may have never been undertaken.

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