



## **ENSURING FINANCIAL STABILITY AND GROWTH OF CAPITALIZATION OF THE BANKING SYSTEM OF UZBEKISTAN**

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### **Abstract**

*This paper analyzes the dynamics of the development of the banking system of the Republic of Uzbekistan, establishes factors for ensuring financial stability and increasing the capitalization of the banking system. According to the ensuring the financial stability of financial and credit organizations remains one of the key factors in the growth of the value of such organizations. In addition, development of the optimal combination (ratio) of the structure of assets and liabilities for each bank, which allows to ensure maximum profitability with minimal risk, while observing the requirements for the adequacy of equity*

*Keywords: Financial stability, value of equity, capitalization of banking system, assets and capital of banks*

### **INTRODUCTION**

The main directions of reforming the banking system of the Republic of Uzbekistan at the present stage are concentrated in increasing the level of capitalization and liquidity of commercial banks, improving management, and a system for assessing banking risks, expanding the spectrum and improving the quality of banking services.

The objective processes taking place in the modern banking business, significant changes in the conditions of functioning of banks around the world have led to the need for banks to increase their own capital to increase their reliability and economic growth, reduce the



likelihood of bankruptcy and avoid the risks of banking operations. International experience has shown that under current conditions, the problem of insufficient capitalization is relevant.

It should be noted that ensuring competitiveness and profitability, the growth of capitalization and the cost of equity of an individual bank is a target function for management and its shareholders. Financial stability, sustainability, as well as the reliability of a commercial bank in the banking system of a country first of all gains national significance.

It is no secret that a stable and reliable banking system is the key to the success of economic reforms in the economic and social spheres, ensuring the growth of the country's economy, and, accordingly, the welfare of its population.

By the Decree of the President of the Republic of Uzbekistan dated September 2, 2017 No. 5177 "On Priority Measures for the Liberalization of the Currency Policy", the problem of maintaining the stability of the banking system and increasing its risk tolerance, including through the adoption of effective preventive measures to mitigate the possible negative effects of liberalization of the currency policy on the financial condition of banks is defined as one of the priority areas of state policy in the field of further liberalization of the foreign exchange market.

In the set of measures for the further development of the banking and financial system based on best banking practice for the period 2017-2021, the priority is given to measures to increase the level of capitalization and liquidity of commercial banks. All commercial banks have been established to ensure that by January 1, 2019, the minimum size of authorized capital (funds) is up to 100 billion soums. It should be noted that as of January 1, 2018, 9 out of 28 commercial banks have authorized capital below the critical threshold.

## LITERATURE REVIEW

Against this background, the study of problems of increasing the level of capitalization and ensuring the financial stability of the functioning of the country's banking system in the new conditions is one of the most urgent tasks of scientific research in the field of finance, since the changes in the banking sector are directly reflected in the country's economy.

The author of the work believes that the stability of the banking system is the ability of the system to fulfill its functional purpose, regardless of the nature, strength and duration of external influences.

The research claims that the stability of a commercial bank is its ability to fully carry out its activities as a financial intermediary under the influence of a complex of external and internal factors and maintain its development on a set by management entities in the short, medium and long term.

According to the author of the work, financial stability of a commercial bank is understood as an asset and liability management that ensures maximum profitability with minimal risk, and at the same time an adequate level of capital to cover credit risks, liquidity to fulfill obligations in the short and long term, as well as high quality management.

From the foregoing, it is obvious that ensuring stability and increasing the capitalization of the banking system is not possible without an increase in the cost of equity of the commercial banks forming this system. Currently, both state and foreign-owned banks, private and joint-stock banks operate in the banking sector of the Republic of Uzbekistan. It must be emphasized that commercial banks are created in the legal status of a joint stock company on the basis of any form of ownership, while the legislative framework and regulatory requirements for functioning are the same for all banks.

## ANALYSIS AND RESULTS

Analysis of statistical data [3] shows that in 2005-2017, the gross domestic product increased by 15.6 times, total assets of the banking system increased by 29.6 times, bank loans by 28.5 times, the volume of attracted deposits increased by more than 34.7 times. At the same time, capital growth in the banking system amounted to 25.5 times.

Over the years under study, the ratio of the main indicators of the banking system to gross domestic product has grown significantly, this indicates an increasing role and importance of the banking sector in the country's economy. But it should be noted that the value of the ratio of the total capital of banks to gross domestic product lagged significantly behind other indicators. The position is well illustrated in the diagram shown in Fig. 1.

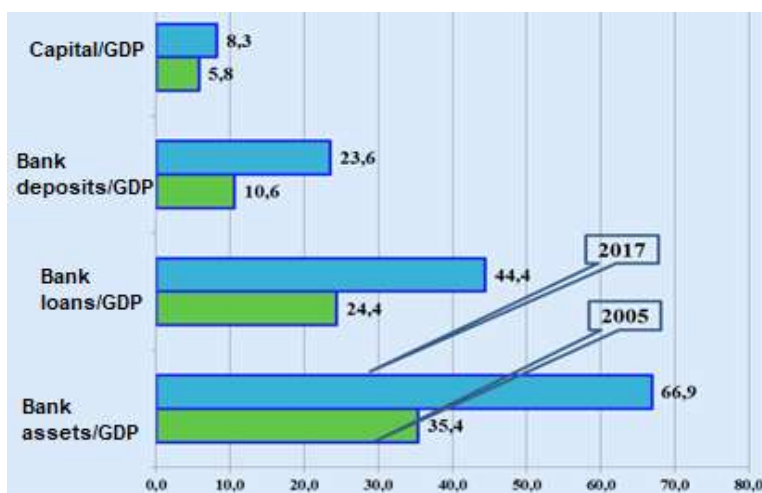


Figure 1. The ratio of the main indicators of the banking system to the GDP of the Republic of Uzbekistan in 2005 and 2017

In the context of the globalization of financial and economic relations and in the context of Decree of the President of the Republic of Uzbekistan dated September 2, 2017 No. 5177 "On Priority Measures for the Liberalization of the Foreign Exchange Policy", it is advisable to analyze the main indicators in freely convertible currency.

The analysis shows that for 2005 - 2017, not all indicators of the banking system of Uzbekistan grew dynamically, while the growth rates of indicators are mixed (Fig. 2). It should be noted that for three main indicators of the banking system, total assets, the volume of loans issued and attracting deposits for 2005-2016 there was a steady increase in indicators, but at the end of 2017, in our opinion, as a result of the adoption by the Government of the country of a course towards liberalization of monetary policy, the value of these indicators decreased significantly. The total assets of the country's banking system in 2016 amounted to 24.87 billion US dollars, in 2017 amounted to 20.52 billion US dollars, the volume of loans issued decreased from 16.52 to 13.62 billion US dollars, the volume of attracted deposits, from 13.80 to 7.23 billion US dollars. One of the key indicators of the banking system of the Republic of Uzbekistan - the total capital of commercial banks for 2005 - 2017 increased from 0.79 billion US dollars to 2.54 billion US dollars. The value of this indicator reached its maximum in 2012 - the total capital of the banking system amounted to 3.13 billion US dollars, starting from this year there has been a steady decline. But as we see the value of this indicator over the past 6 years, it shows a downward trend, which is an alarming sign of the development of the banking system.

This is largely relevant when you consider that the international rating agencies Moody's, —Standard & Poor's and —Fitch Ratings, when assigning stability ratings to commercial banks, evaluate the main economic and financial indicators for their compliance with international standards. In the course of studies to expressly assess the characteristics of the financial stability of the banking system of our country, we will dwell on the ratio of capital of the banking system to its assets. It should be noted that this indicator shows us what part of the assets of the banking system is financed from its capital. At the same time, we acknowledge that this indicator cannot serve as a full-fledged analytical indicator of the financial condition of the banking system, but the dynamics of the indicator allows us to assess the development trend of the banking system. For all years of observation, the ratio of the total capital of the banking system of the Republic of Uzbekistan to its assets was at a high level, in 2010 this indicator reached its maximum - 19.8 percent. At the same time, in 2011-2016, there was a downward trend; in 2016, the ratio of banks' total capital to their assets amounted to 11.6 percent and this value is the lowest indicator for 2005-2017 (Fig. 2). The value of this indicator in 2017 improved and amounted to 12.4%.

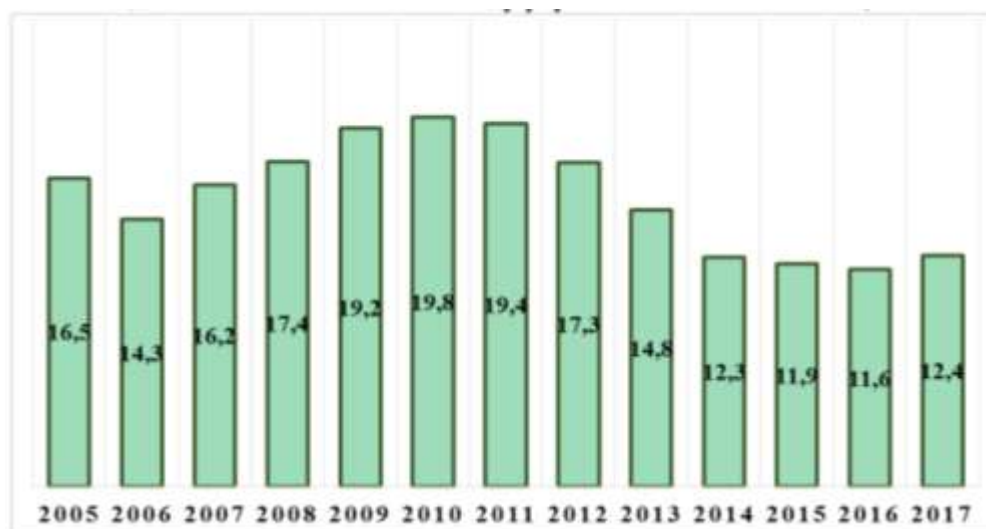


Fig. 2. The ratio of total capital to assets of the banking system of the Republic of Uzbekistan for 2005-2017, %

An important role was played by the adoption by the Government of the country of effective measures to ensure financial stability and increase the capitalization of the banking system. By the Decree of the President of the Republic of Uzbekistan dated June 16, 2017 No. PP-3066 “On additional measures to increase financial stability and the level of capitalization of commercial banks” at the expense of the Fund for Reconstruction and Development in the amount of \$ 500 million equivalent, they were directed to increase the authorized capital of individual systemically important commercial banks [9].

An analysis of World Bank data showed that in most economically developed countries the value of the ratio of the total capital of the country's banking system to its assets is lower than in our country, but the stability of the banking system is not in doubt.

For example, the value of this indicator at the end of 2016 in some countries was equal to the following size: Great Britain - 7.0% Germany - 6.0% Italy - 5.5%, Canada - 5.2%, China - 8.1%, USA - 11.6%, France - 5.9%, Switzerland - 7.1% and Japan 5.5%. This allows us to conclude that a low ratio of the total capital of the country's banking system to its assets is not always a negative indicator of the stability of the banking system. A study of domestic and foreign literary sources during the preparation of the article showed that ensuring the outstripping or at least adequate growth of the total capital of the banking system compared to other indicators is the basis of financial stability, stability and reliability of the country's banking system - this is an axiom.

Financial stability and stability of the country's banking system is provided under the influence of many external and internal factors.

External sustainability factors include: the organic and adaptive nature of the banking legislative base to international law and the level of its development, as well as the organic nature of established banking norms and standards to international requirements and norms. In addition, in our opinion, the development of banking infrastructure according to international standards can also be attributed to external factors.

The internal factors of financial stability of the banking system include the efficiency (profitability) of banking activities, ensuring capital growth, dividend policy, structure and quality of assets, as well as the structural composition, balance and the optimal structure of liabilities of each individual commercial bank of the country's banking system.

## CONCLUSIONS

The results of the study presented in the framework of this article allow us to draw the following conclusions: The methodology for ensuring the growth of capitalization of financial and credit organizations is quite complex and multifaceted. Nevertheless, ensuring the financial stability of financial and credit organizations remains one of the key factors in the growth of the value of such organizations.

The activities of financial and credit organizations have their own specifics, which must be taken into account when developing the assessment concept and its methodology, emphasizing the factors of ensuring financial stability.

The most promising indicator of a modern banking management system is the development of organizational and methodological mechanisms for managing the value of the bank, aimed at ensuring the growth of equity, the level of capitalization.

An empirical analysis of statistical data allows us to formulate proposals aimed at ensuring financial stability and growth in the capitalization of the banking system of our country:

1. Commercial banks, together with shareholders, should develop a long-term dividend policy, while providing for the direction of part of the net profit for capitalization;
2. Consider conducting an IPO on the stock exchange as an effective way to increase equity and attract additional investment.
3. In order to encourage commercial banks to increase the amount of equity, we propose to partially deduct from the tax base the income tax, the amounts allocated to increase the authorized capital. bank. Starting January 1, 2018, the corporate tax rate for commercial banks increased from 15% to 22% [11].
4. To analyze the asset structure of commercial banks while paying attention to optimizing and reducing the share of income of non-bringing or non-core assets;
5. Improving the quality and quantity of banking services provided, which is the basis for generating additional income and, accordingly, profit;
6. Development of the optimal combination (ratio) of the structure of assets and liabilities for each bank, which allows to ensure

maximum profitability with minimal risk, while observing the requirements for the adequacy of equity.

These conclusions and recommendations, in our opinion, will ultimately help ensure financial stability and sustainability, as well as increase the level of capitalization of the banking system of the Republic of Uzbekistan.

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