

Azerbaijani Banks in 2018 (from January through September)

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Introduction

We have bid farewell to the old year 2018 and ushered in the new year 2019. It is now time to review Azerbaijan's social and economic processes in 2018. This Bulletin, prepared by a group of experts from the Baku Research Institute (BRI), has sought to assess the country's banking sector and changes within it. However, as the official statistical data available allow us to see the sector for the first three quarters, the Bulletin could only look into the period from January to September 2018.

The initial section of this Bulletin considers changes in banking legislation in 2018, changes in the number of banks, their branches and departments operating in the country, and the degree of concentration in the banking system.

The Bulletin further analyzes the resources of operating banks, formation sources and an avenue for their use, especially the status of loan and deposit markets, and reveal major trends in the level of dollarization in the country's lending and deposit markets.

We at the Baku Research Institute hope that this Economic Bulletin available to you, and that characterizes the overall banking sector situation in Azerbaijan, describes the real picture of the changes the country faced in January-September 2018.

Azerbaijan's banking sector has remained relatively stable with a moderate improvement throughout the first nine months of the year 2018. The overall tendency in the banking sector looks at overcoming capital shortages, a revival triggered in lending, a decrease in interest rates on deposits, an increase in excess liquidity in the banking system, and banks' preferences to alternative sources of income.

Changes in banking legislation

The banking sector legislation has experienced changes on the following fronts during the reporting period:

- *The Regulations for the operation of the State Registry for Encumbrance of Movable Property and the Fees for usage of the State Registry for Encumbrance of Movable Property were approved by Decree No. 1901 of the President of the Republic of Azerbaijan, dated 29 March 2018. These Regulations identify and govern the operating procedures, as well as the use and data security arrangements of the State Registry for*

Encumbrance of Movable Property. And the state registry for encumbrance of movable property shall be created through the operatorship of the Financial Market Supervisory Authority of the Republic of Azerbaijan (FIMSA) under these Regulations.

- *Rules of Foreign Currency Transactions of Residents and Non-Residents of Republic of Azerbaijan* were amended by decision No 4/1, dated 26 February 2018, of the Central Bank's management board. These Rules have toughened requirements for foreign currency transactions of residents and non-residents through banks. Among the amendments, upon advance payment for goods and services imported into Azerbaijan, imports shall be proven by a customs declaration and a proof of services having been rendered, respectively, in 270 days from the day of payment, compared to the previous term of 180 days.
- The maximum term of office for members of supervisory and management boards was reduced according to amendments to *the Law on Banks*. In accordance with the changes, members of supervisory and management boards will be elected for a maximum term of three years. Previously, the term was four years. At the same time, other amendments expand the powers of the supervisory boards.
- *Regulations on Electronic Mortgage and Credit Guarantee System* were approved by Decree No 30 of the President of the Republic of Azerbaijan, dated 1 May 2018. Under the Regulations, the purpose of the system is to improve the quality and efficiency of the services provided by simplifying the access to mortgage and entrepreneurship loans, creating equal conditions for persons wishing to obtain a loan, ensuring transparency and efficiency during the consideration of applications, as well as time and cost savings by using the real-time access to the required documents by taking advantage of the information and communication technologies

Besides, the *Financial Market Supervisory Authority (FIMSA)* has adopted a number of normative acts to rehabilitate insolvent banks, and to enhance banks' stability:

- *Rules to create a bridge bank, issue and register its shares, special simplified procedure for granting license to bridge bank and its activity;*
- *Rules to determine an insolvent bank's resolution measure and to hold an auction*
- *Rules for the substantiation and comparative analysis of expenses to choose any of the resolution measures;*
- *Rules to create special reserves for the classification of assets and compensation of possible losses;*
- *Rules to determine limits on open currency positions in banks;*
- *Rules to calculate banking capital and its adequacy;*
- *Rules to regulate credit risks regarding related borrower.*

Banks and concentration level

The concentration in the banking sector that had slackened since 2017 tended to rise again in 2018. During 2013-2016, the market share of five banks in the banking sector increased from 55% to 68.2%, but fell to 65.2% in 2017, with a moderate growth rate [65.3%] recorded during the first nine months of 2018.

The assets and market share of the *International Bank of Azerbaijan (IBA)*, the largest bank in Azerbaijan by the asset, have continued to decrease over the reporting period, with its assets being down 4.3%, or AZN 374.8 million, but market share dropping to 28.5% from 31.1% 28.5%. However, *Paşa Bank*, which was ranked in second place, saw a 22% increase in its assets, while market share was 14.8% up from 12.7%. Further, the banks with moderate growth in assets are *Kapital Bank* (from 6.5% to 6.6%), *Xalq Bank* (from 6.5% to 6.6%), while Azerbaijan Sanaye

Bank1 had a stable market share (3.4%) (see *Table 1*).

Table 1: Changes in assets of top 10 Azerbaijani owned banks, AZN million

Banks	Assets		Change (+ increase, - decrease)
	2017	2018 (9 months)	
1. <i>International Bank of Azerbaijan OJSC</i>	8695,1	8320,3	- 374,8
2. <i>PAŞA Bank OJSC</i>	3551,8	4332,0	780,2
3. <i>Kapital Bank OJSC</i>	3184,5	3457,5	273
4. <i>Xalq Bank OJSC</i>	1813,6	1941,0	127,4
5. <i>Azərbaycan Sənaye Bankı OJSC</i>	945,2	1007,2	62
6. <i>Bank Respublika OJSC</i>	702,1	976,0	273,9
7. <i>AccessBank CJSC</i>	844,8	836,5	-8,3
8. <i>Unibank KB OJSC</i>	601,8	669,3	67,5
9. <i>Rabitabank OJSC</i>	727,2	656,2	-71
10. <i>Silk Way Bank</i>	411,3	614,1	202,8
Total:	27921	29201,8	

Source: Azerbaijan Banks Association – www.aba.az

The results of our assessment based on **Herfindahl–Hirschman Index**, an index widely deployed internationally to assess industry concentration, have showed a drop from the concentration of 1382.3 to 1293 in the banking sector for the first 9 months of 2018, which is a medium concentration level.

The reductions in banking networks due to the post-devaluation cost optimization have been replaced by a tendency towards further expansion of these networks. At the end of 2017, the license of *Demirbank OJSC* was revoked by a rule of the Board of Directors of the Financial Market Supervisory Authority dated December 22, 2017 (*in the first half of 2017, two banks – Atabank OJSC and Caspian Development Bank OJSC merged*). The reason for this decision is that the aggregate capital of the banks was lower than the minimum amount of a capital defined to the banks and the adequacy ratio of the aggregate capital was less than three per cent intended by the legislation, as well as failure to fulfill liabilities to the creditors. Thus, the number of Azerbaijani based banks decreased to 30 (see *Table 2*).

Table 2: Number of active Azerbaijani banks

Banks	9M 2017	2017	9M 2018	Change (+ increase, - decrease)	
				Compared to 9 months 2017	Compared to 2017
Number of banks	31	30	30	- 1	0
- Banks with foreign capital, including:	16	15	15	-1	0
<i>with the share of foreign capital ranging from 50 to 100 percent</i>	8	8	8	0	0
<i>with the share of foreign capital not exceeding 50 percent</i>	8	7	7	- 1	0
<i>local branches of foreign banks</i>	2	2	2	0	0
Local bank branches	557	509	511	- 48	+2
Local bank departments	142	142	143	+1	+1
Number of employees	16340	16171	17066	+726	+ 895

Source: FIMSA.

The closure of *Demirbank OJSC*, as well as a worsening in financial health of the banks led to a decrease in the number of branches. The number of branches during the first 9 months of 2018 fell 8.6% to 511 from 557 compared to the same period of 2017, while two more branches were launched during the first nine months of 2018. The number of branches per bank fell from 18 to 17. Plus two new bank departments were opened during the past year (see *Table 2*).

Unlike the slight growth in the number of branches, banks were seen to employ highest number of employees during January-September 2018, increasing by 5.5% to 17,066. The number of employees was roughly 4.4% up, compared to the same period of 2017 (see *Table 2*).

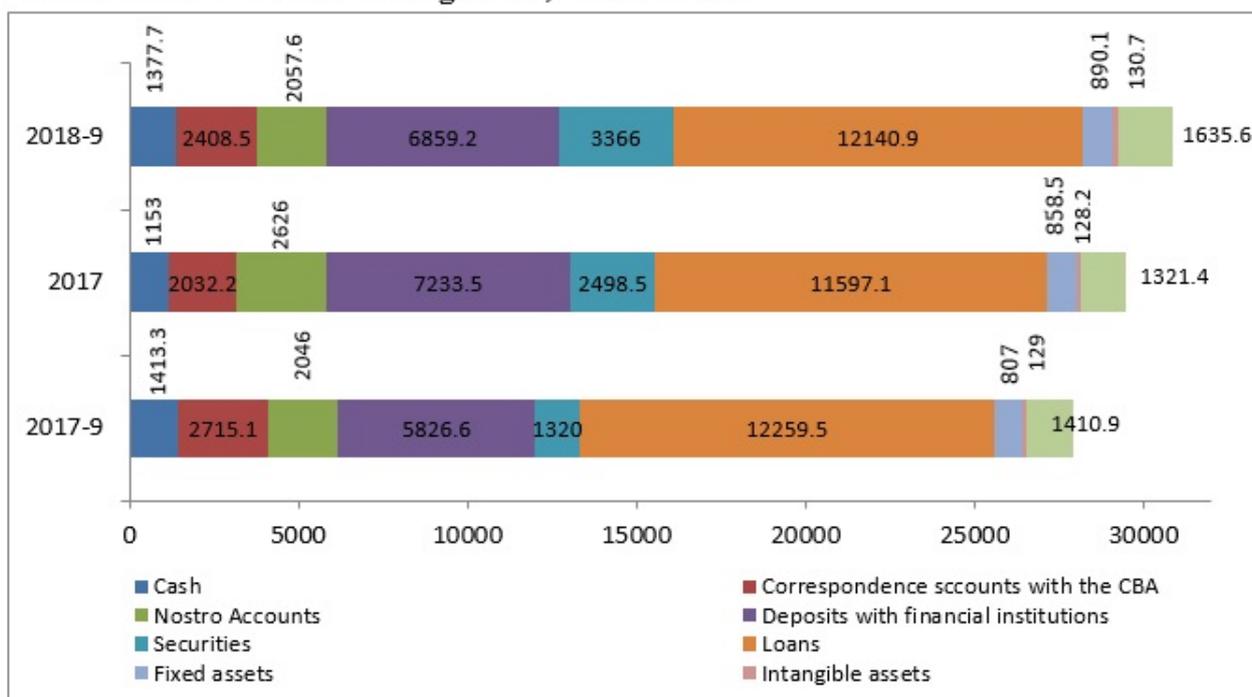
Bank resources: formation sources and their use

The decrease in Azerbaijan's banking assets seen in recent years has been replaced by an increase during the first 9

months of 2018. Statistical data provided by the Financial Market Supervisory Authority (FIMSA) found that the bank assets were 4.6% up to AZN 27.92 billion in the same timeframe, which represents an 11.6% increase compared to the same period a year earlier.

The banking sector assets rebounded as a result of a growth in specific indicators of the asset structure. The banking sector demonstrated significant progress in other indicators, other than *Nostro Accounts* and *deposits with financial institutions* during the first nine months of 2018. The bank assets that significantly expanded included *securities* (34.7%), *other assets* (23.8%), *cash* (19.5%) and *the correspondence accounts of the Central Bank* (18.5%), while the total volume of *Nostro Accounts* dropped quit significantly (21.6%) (see *Chart 1*).

Chart 1: Structure of banking assets, AZN million



Source: Financial Market Supervisory Authority.

Comparing to the same period of the previous year, the most significant increase was at the *securities* level. Thus, banks' investment to *securities* nearly tripled (see *Chart 1*).

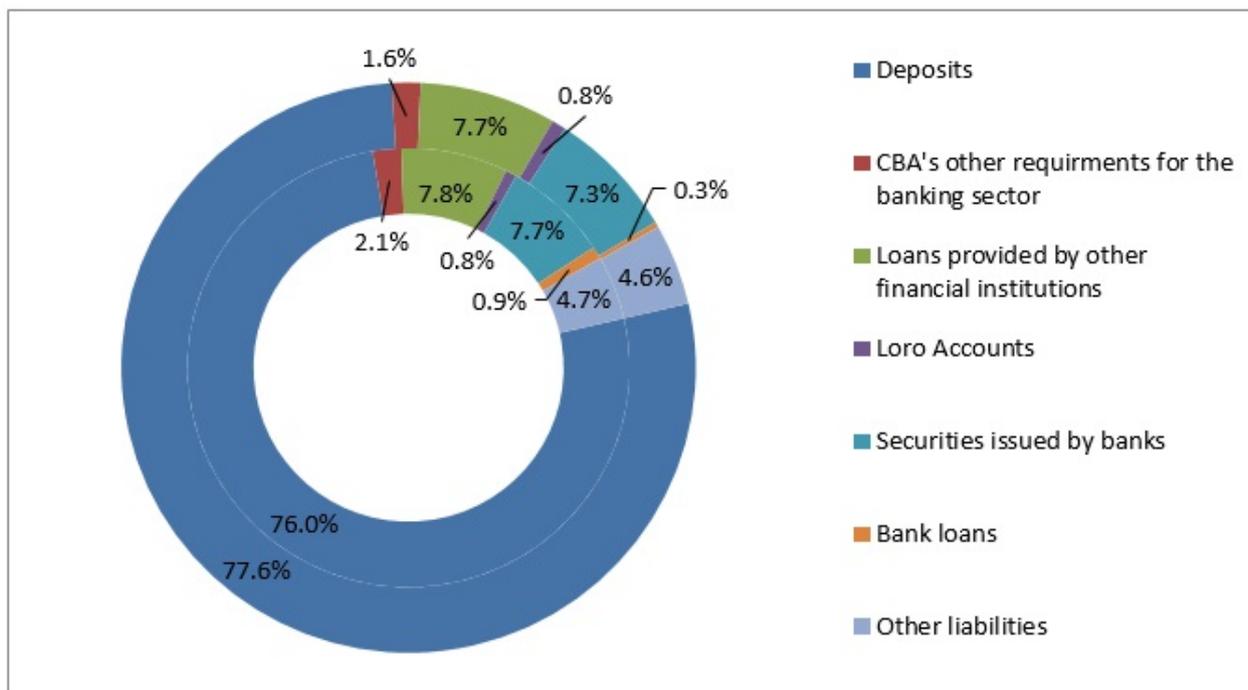
To strengthen the stability for banks, the process of increasing their capital has continued. The banks' total

capital rose by 10.9% from AZN 3.71 billion to AZN 4.11 billion over the first nine months of 2018. As a result of this increase, the share of capital in banks' assets increased from 13.3% to 14.1%.

The following banks have experienced major increases in their bank capital: Bank Respublika (46.7%), Bank VTB (36.5%), International Bank of Azerbaijan (35%), Unibank OJSC (33.5%), Silk Way (24.6%), while Amrahbank (28.5%), Accessbank (18.7%), AGBank (10.9%), Nikoilkbank (7.6%) experienced decreases. [\[i\]](#)

Deposits (with both physical and legal persons, including financial institutions) constituted 77.6% of *bank liabilities* as at 1 October 2018, which represents a 76% increase compared to the same period a year earlier. *Loans raised from other financial institutions* were the second major financial source. As raising loans from this source shrank, its share in total bank liabilities dropped from 8.7% to 8%. The shrinkage was attributable to a decrease in loans directed by banks. Over the reported period, the share of *securities issued by banks* in total liabilities dropped from 7.7% to 7.3% (see *Chart 2*).

Chart 2: Structure of banking sector liabilities (% of total)

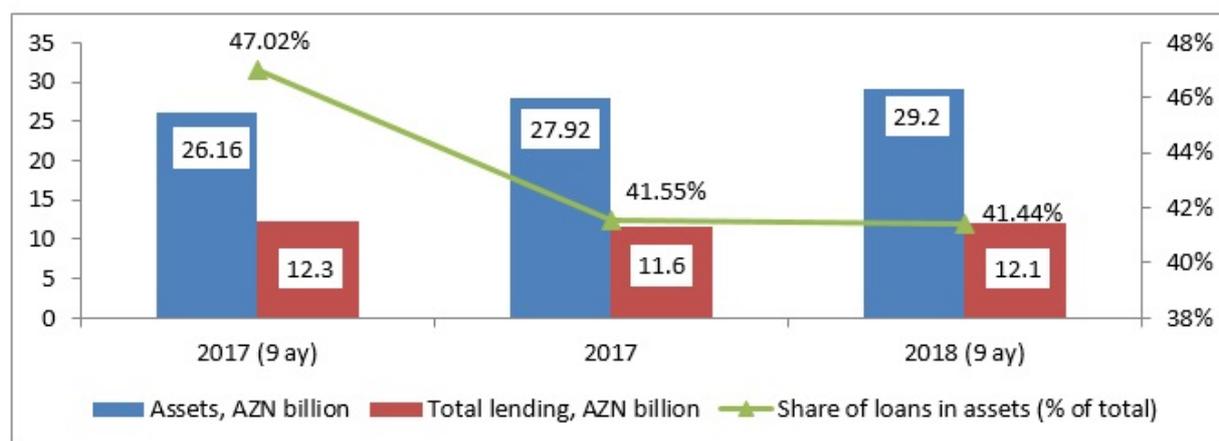


Source: Financial Market Supervisory Authority.

The origins of a sharp increase in banks' investments to securities lie to a large extent in their decreased interest in providing loans after the devaluation. The volume of lending grew in January-September 2018, yet its share in total assets had continued to decline. The lending by country grew by 4.3% from AZN 11.6 billion to AZN 12.1 billion, a figure which had not been attained since 2015, while its share in total assets dropped from 41.55% to 41.44%. The highest indicator – 47.02% had been recorded during the first nine months of 2017 (see *Chart 3*).

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Chart 3: Banking sector assets, AZN billion



Source: Financial Market Supervisory Authority.

The lending organizations that are unable to direct their assets to active lending prefer to invest in securities. Consequently, the share of securities in assets grew from 5.1% to 11.5% from September 2017 to September 2018. [\[iii\]](#)

Loan market

Lending growth in this period can be attributed to private banks, particularly ones with local capital. The total lending provided by The Open Joint Stock Company International Bank of Azerbaijan (IBA), which holds the state-owned shares, and Azer Turk Bank OJSC dropped by 3% from AZN 1916.2 million to AZN 1858.8 million, while lending by private banks rose by 6.6% AZN 9421.4 million to AZN 10042.6 million during January-

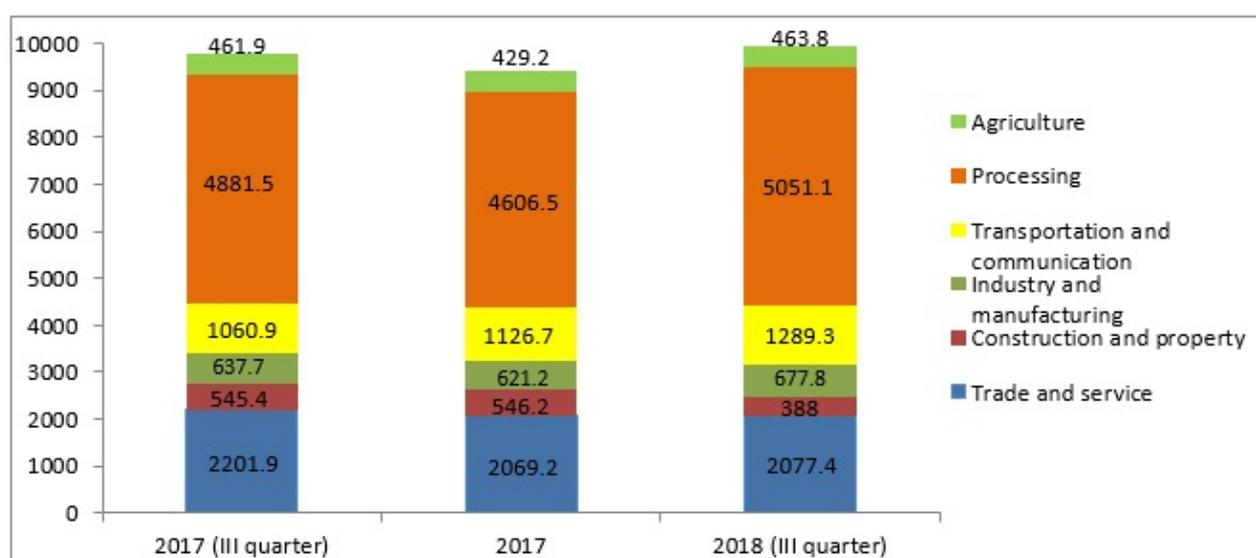
September 2018. This growth was attributed to private banks with local capital. The lending by local banks and banks with the share of foreign capital ranging from 50 to 100 percent, surged to AZN 621.2 million, and AZN 25.9 million, whereas the lending by banks with the share of foreign capital not exceeding 50 percent was down AZN 53 million. [\[iii\]](#)

Unlike the banks, financing of the economy by non-bank credit organizations (NBCO) has demonstrated a downward trend, falling by 4.6% from AZN 420.2 million to AZN 401.1 million over the reported period, the lowest level since 2013.

Analysis of lending by sectors found out that apart from the construction and property sector, all sectors saw growth during the first nine months of 2018. Thus, lending to the *trade and service* sector rose by 0.4%, while *industry and manufacturing* 9.1%, *transportation and communication* 14.4%, *agriculture and processing* by 8.1% and *consumer loans* 9.7%. The *construction and property* sector saw a 29% drop in the same timeframe (see *Chart 4*).

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Chart 4: Trends in lending by sectors, AZN million



Source: Central Bank of Azerbaijan.

The share of *consumer sector loans* that had preserved a

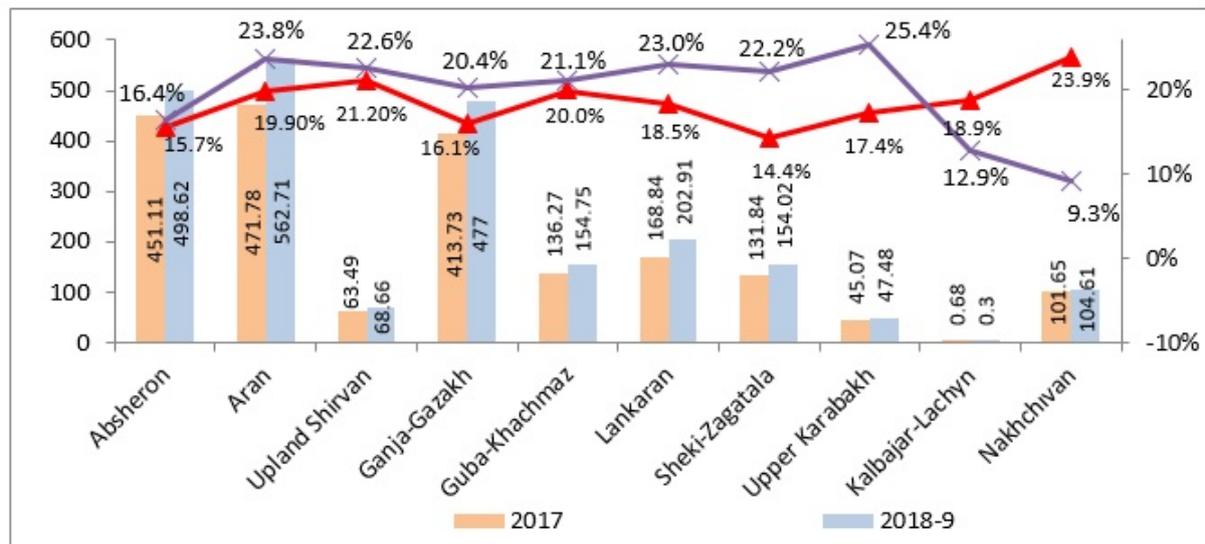
downward trend since 2014 has surged over recent months, which was up 41.1% from 39.2%, compared to the beginning of the reporting year. The shares of *trade and service and construction and property*, respectively, fell from 17.6% to 16.9% and 4.6% to 3.2%, while the shares of *agriculture, industry and manufacturing*, and *transportation and communication*, respectively, rose from 3.7% to 3.8%, from 5.3% to 5.5%, and from 9.6% to 10.5%. [\[iv\]](#)

The currency structure of loans showed that ***growth was observed in lending in national currency*** other than that in foreign currency. The lending in national currency was 8.7% up to AZN 7557.2 million during January-September 2018. Moreover, lending in national currency had been the lowest level since 2011, while lending in foreign currency was 1.2% down to AZN 4745.2 million. [\[v\]](#)

Lending, when the dollarization level rose by 49.4% due to the 2015 devaluation, has further contracted despite the stability of the national currency. The loan de-dollarization process has continued over the reporting period of 2018, dropping from 40.9% to 38.6%.

Concerning the loan term, ***banks have chosen to provide short-term loans***. Regardless of the currency structure, the amount of *short-term* and *long-term* loans were up 17.2% and 1.9%, accordingly. National currency lending saw growth for both short-term (+24.8%), and long-term (+5.9%) loans. However, foreign currency short-term lending was up 9.9%, but long-term was down 4.4%. [\[vi\]](#)

Regions have seen a slight increase in lending. The amount of lending to regions increased by 14.4% over the first nine months of 2018, while lending to Baku only grew by 2.6%. As a result of this growth, the share of region in total loan assets rose from 16.9% to 18.5%. Despite this, Baku has retained prevalence of total lending (81.5%).

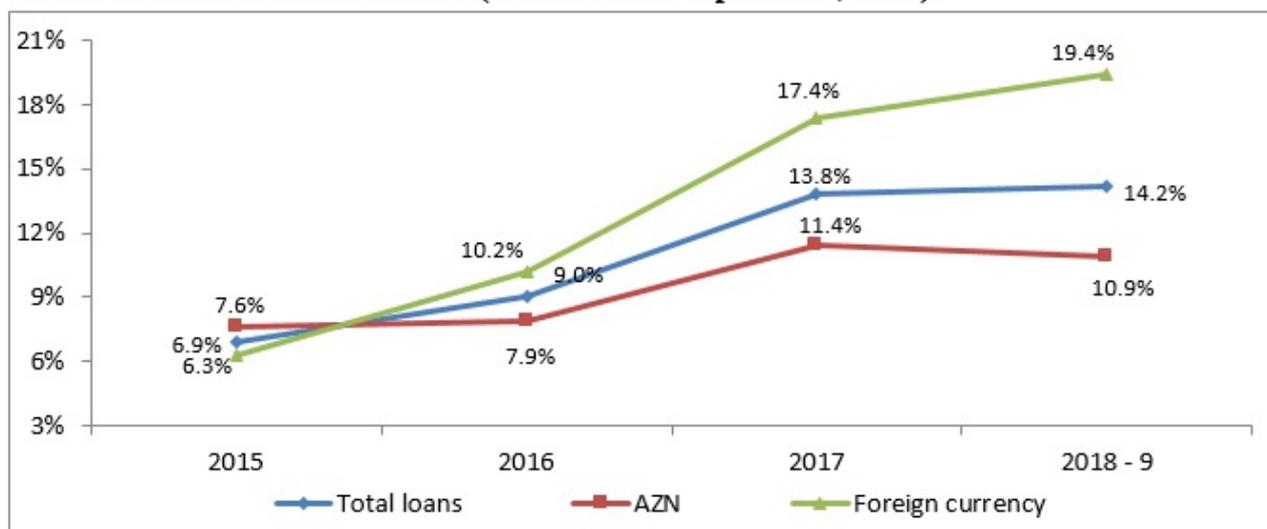
Chart 5: Amount and interest rate of loan assets by regions, AZN million

Source: Central Bank of Azerbaijan.

The annual interest rate for national currency loans by country total was 14.2%, while this figure for *Baku* was lower – 12%, while for regions (excluding *Nakhchivan AR*) ranges between 16% and -25%. For example, the average annual interest rate for the *Aran economic region* is 23.2% and for the *Upper Karabakh economic region* 25.4%. Customers prefer to take loans in Baku due to higher annual interest rates offered by banks in regions. The share of Baku in total lending fluctuates between 80% and 85% by years. The lowest interest rate is the *Nakhchivan Autonomous Republic* (.93%), but its share in total lending is small (0.9%) (see *Chart 5*).

The **overdue loans** that led to waning banking interest in financing the economy, **have continued to increase**. [According to the Central Bank of Azerbaijan](#), the share of overdue loans in total loans rose from 13.8% to 14.2% in January-September 2018, increasing by AZN 122 million, or 7.5%, from AZN 1626.7 million to AZN 1748.7 million compared a year earlier. Of the total growth 31% and 69%, respectively, went to local and foreign currencies (see *Chart 6*).

Chart 6: Share of overdue loans (from 2015 to September, 2018)



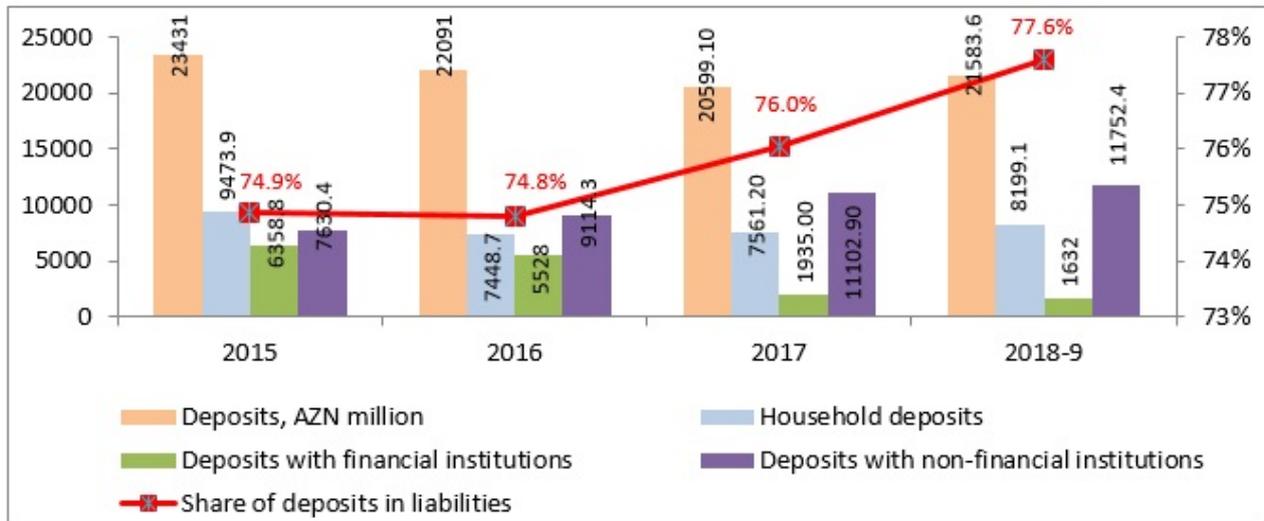
Source: Central Bank of Azerbaijan.

The increase in problem loans occurred mainly due to loans in foreign currency. The volume of problem loans in national currency rose by AZN 37.9 million, yet its share in manat loans slid from 11.4% to 10.9%. The volume of overdue loans in foreign currency increased by AZN 84 million, with its share increasing from 17.8% to 19.4%. The bulk of problem loans constituted long-term loans (79.5%). Delays in short-term loans have increased by 11% and in long-term loans by 6.6% over the reporting period.

Deposit market

The decline in the deposit market observed 2015-2017 tended to rebound again. Total deposit assets were up 4.8% to AZN 21.6 billion in January-September 2018. The growth in deposits has also been reflected in bank liabilities. **The increasing dependence of banks on the deposits has continued.** In 2015, although the share of deposits in total liabilities was 74.9%, it touched 76% in 2017, and 77.6% as of 1 October 2018 (see *Chart 7*).

Chart 7: Trends in volume of deposits and share of banking sector liabilities, 2015-2018



Source: Central Bank of Azerbaijan.

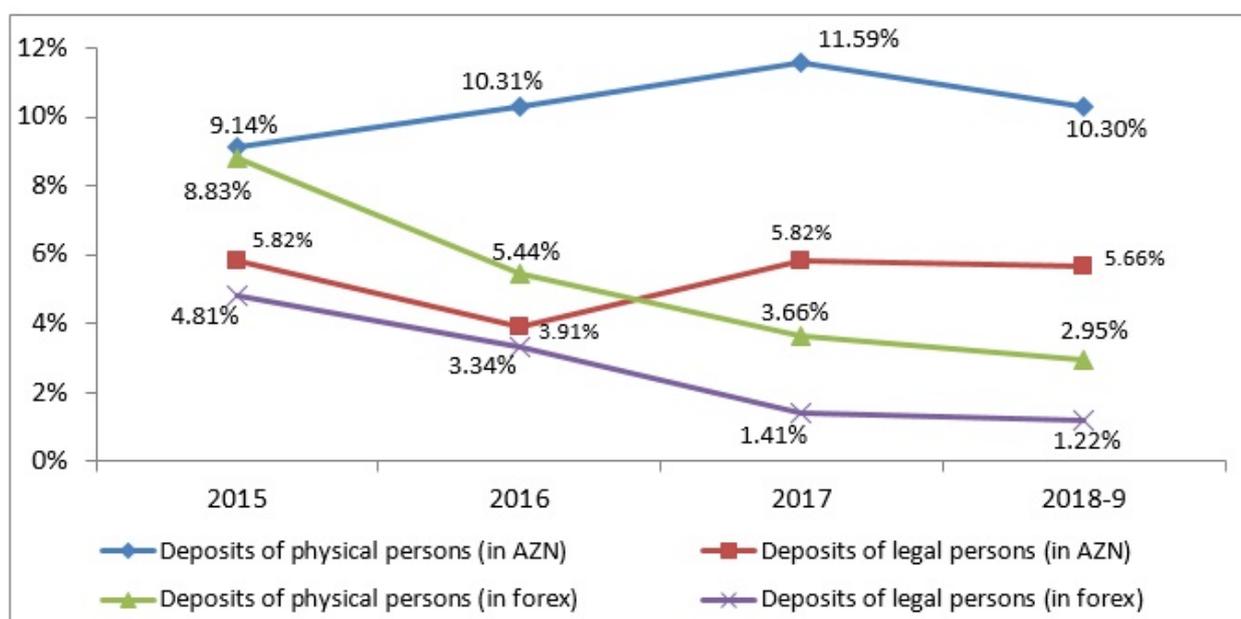
The reason for the increase in deposit volumes are banks' gradual rejection from foreign liabilities and the restriction of abilities to take loans from banks or other financial institutions. According to the CBA, the foreign liabilities of the banks decreased from \$2.3 billion to \$1.9 billion in January-September 2018. In the same timeframe, the loans provided by banks and other financial institutions slid from AZN 2.12 billion to AZN 2.02 billion. [\[vii\]](#)

Unlike the growth in total deposits, *financial institutions* saw a decrease in their deposits, down 15.7% to AZN 1.6 billion during the reporting period, while *household deposits* rose 8.4% to AZN 8.2 billion, while *non-financial deposits* by 5.8% to AZN 11.75 billion.

The currency structure of deposits showed that the total deposit growth was attributable to the national currency deposits, which represent a 23.8% increase, while foreign currency deposits slid by 2.5%. *Population deposits* in national currency rose 21.2%, while *deposits with financial and non-financial institutions*, respectively, by 10.2% and 27.8%. *Population deposits* in foreign currency rose 2%, while *deposits with financial and non-financial institutions*, respectively, slid by 21.2% and 1.6%.

The increasing growth in manat deposits recorded in the banking sector has been due to the stability of national currency and high national currency yields. **The decreasing tendency in annual interest rates on manat deposits has not diminished the attractiveness of deposits in this currency.** For example, the annual interest rate of manat deposits dropped from 11.59% to 10.3% compared to the end of 2017. The average annual interest rate of deposits for legal persons dropped from 5.82%-to 5.55%. The same reduction was also observed in the annual interest rate of foreign currency deposits. Deposits for physical persons dropped from 3.66% to 2.95%, while for legal persons from 1.41% to 1.22% (see *Chart 8*).

Chart 8: Dynamics of average annual interest rates of deposits, 2013-2018



Source: Central Bank of Azerbaijan.

The annual interest rate of national currency deposits that had seen growth after the devaluation, started to decline in 2018. The annual interest rate of foreign currency has also continued to decline. Deposits of individuals fell from 8.83% to 2.95% and legal persons from 4.81% to 1.22% in 2015-2018. As a result of the decline in annual returns on foreign currency, the individuals and legal persons' interest in investing foreign currency money has decreased (see *Chart 8*).

The growth in demand deposits is indicative of the fact that deposit holders' are uncertain about the sustainability of the banking sector. Demand deposits increased 9.6% to AZN 11.3 billion in the first nine months of 2018. Thus, the share of demand deposits in total deposits increased from 50% to 52.3%. The reason for the growth were the deposits in national currency (34.8%). On the contrary, deposits in foreign currency decreased by 2.2%.[\[viii\]](#) The growth in national currency demand deposits was attributable to non-financial institutions (42.8%).

By virtue of the *Law on Full Insurance Coverage of Deposits* adopted on 19 January 2016, all deposits that are within the frames of the annual interest rates on deposits, constituting 3% in relation to a foreign currency deposits and 15% for the local currency will be insured irrespective of their amount for the period of three years since the effective date of the Law. Unless the law is extended, it will be invalid from 19 January 2019 and compensations will be regulated by the *Law on Insurance of Deposits* effective from December 29, 2006. Under Paragraph 26.1 of the said law, the Fund fully covers deposits amounting to AZN 30,000.

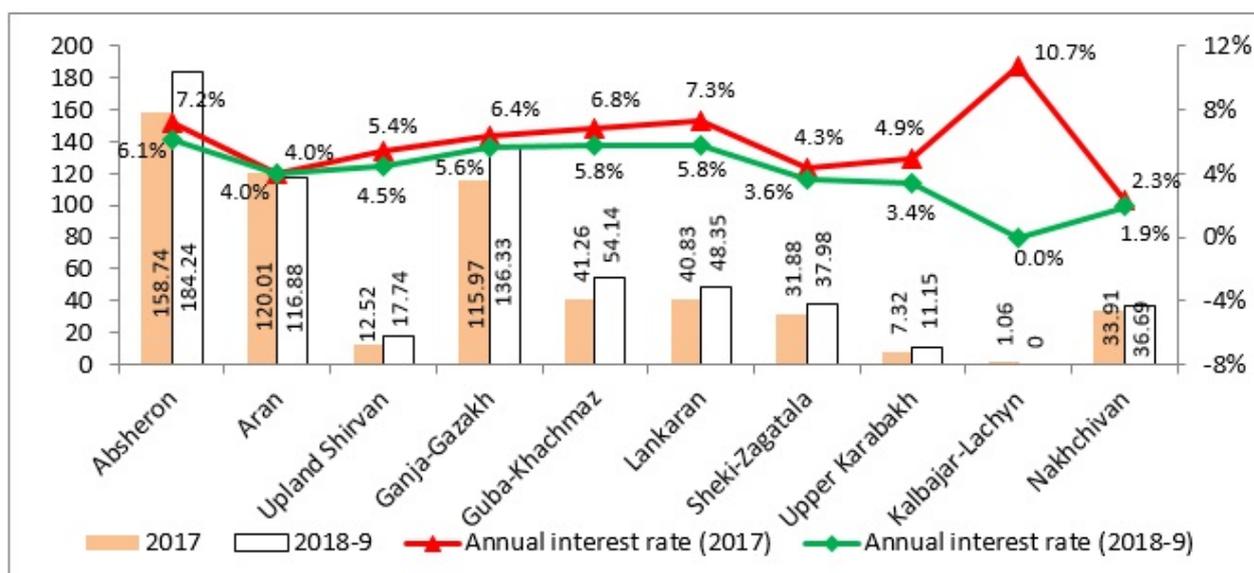
The *Law on Full Insurance Coverage of Deposits* sidelined the outflow of retail deposits from banks. Therefore, the share of on-demand deposits in retail deposits is about 32%, but has tended to grow in recent months. As the said law does not extend to legal persons, their deposits are unsecured. Therefore, the share of time deposits in deposits with non-financial organizations remains high, and even increased by 70.6% in January-September 2018. The growth tendency was also observed in the deposits with financial institutions (from 18.2% to 22.6%).[\[ix\]](#)

According to the Central Bank, the annual interest rate of demand deposits in local currency for the country is 0.2%, while in foreign currency 0.1%, while these figures for time deposits, respectively, are 10.2% and 2.9%.

The level of regional breakdown of deposits showed that deposits were mainly concentrated in Baku. As growth tendency in deposits for Baku (+8%) was lower than that for regions (+14%), the share of Baku was reported to drop (from 92.6% to 92.2%) during the first nine months of 2018. The main growth across the economic regions was observed in Upper Karabakh (52.3%), Upland Shirvan (41.7%), Guba-Khachmaz (31.2%), while there was a 2.6% decline in the Aran economic region (see *Chart 9*).

Generally, the share of the regions in deposits has remained low. **The reason for the low deposits is due to the low interest rate offered for attracted deposits.** The average interest rate in national currency for Baku fluctuates between 7% and 8%, while for the regions between 2.5% and 7%, including, for example, 2.6% for the Nakhchivan AR, 4.1% for Sheki-Zagatala and 4.4% for Aran economic regions.

Chart 9: Volume and interest rate of deposits by regions, million



Source: Central Bank of Azerbaijan.

Financial support for banks provided by Central Bank

The Central Bank has continued to support banks through financial instruments to reduce the excessive liquidity by them not only due to a significant increase in the leverage of deposits, but also due to the reduction in lending.

In January – September 2018, a total of 41 *deposit auctions* were held by the Central Bank of Azerbaijan. [\[x\]](#) These deposits were short-term – 14 days. The total turnover period of attracting deposits at three auctions are 10, 13 and 20 days. The amount of deposit transactions fluctuated between AZN 200-350 million. The demand of banks at all auctions, except for one, exceeded supply by several times. The annual interest rate on the deposit auctions held by the the Central Bank ranged between 8.01% and 14.79%. The average annual interest rate on 34 auctions out of 41 was 8.01%. The banks earned more than AZN 41 million in interest income.

The CBA has also supported banks through short-term notes. The CBA has placed short-term notes 40 times through the Baku Stock Exchange (BSE) over the reporting period. [\[xi\]](#) The turnover period was 28 days. The turnover period for two placements were 27 days and for one placement 364 days only. The volume put-up in auction was mainly AZN 250-300 million. The banks demand for these notes exceeded supply by 2-3 times. The annual yield ranged between 8.01% and 14.52%. The banks earned AZN 69 million in interest income through these notes.

Central Bank's other liquidity management transactions – one, three- and seven-day *repo* and *counter-repo transactions* have not been executed.

Centralized loans given by the Central Bank are considered one of the bank resources. However, the share of this source has gradually declined, and this trend continued in the current year. Over the first 10 months of 2018, the volume of centralized loans has slid by 19.2% to AZN 746.3 million. At present, the volume of such loans has been at the lowest level for the past ten years. The highest credit support from the Central Bank was in 2015 (AZN 6.2 billion). [\[xii\]](#)

The decline in the volume of centralized loans has led to a decrease in their share. During the reporting period, the share of centralized loans in the loan portfolio of banks

decreased from 8% to 6.2%, while the annual interest rates decreased from 15% to 10%. The reason for this is that the Central Bank has gradually reduced the discount rates from 15% to 10%.

Bank customers and their accounts

The *number of bank customers* stood at 6.23 million as at October 1, 2018, which represents a 7.9% increase compared to a year earlier. This is the all-time record. Of the total, 6.13 million, or 98.4% constituted *physical persons*, while 99.6 thousand, or 1.6% *legal persons*. The *number of customer's accounts* rose 8.5% to 17.5 million in the same timeframe. Of this, 83.4% accounted for *current accounts*, 14.6% *credit accounts* and 2% *deposit accounts*. The recent decline in credit and deposit accounts has led an increase in the share of current accounts. The share of current accounts was 74.7% in the pre-devaluation year 2014, touching 83.4% as at the end of September 2018. The share of credit and deposit accounts, respectively, had dropped from 22.4% to 14.6% and from 2.9% to 2% over the reported period. There were 1.7 accounts per bank client in 2013, growing by 2.8. [\[xiii\]](#)

Dollarization of the banking system

The downward trend towards the dollarization of the banking system continued in 2018 that lead to de-dollarization observed in both lending and deposit attraction.

The loan dollarization that had peaked 49.4% in 2015 since 2006 tended to reduce in subsequent years. The share of loans in foreign currency dropped from 40.9% to 38.6% in January-September 2018, which is the lowest indicator recorded since 2014 (see *Chart 10*).

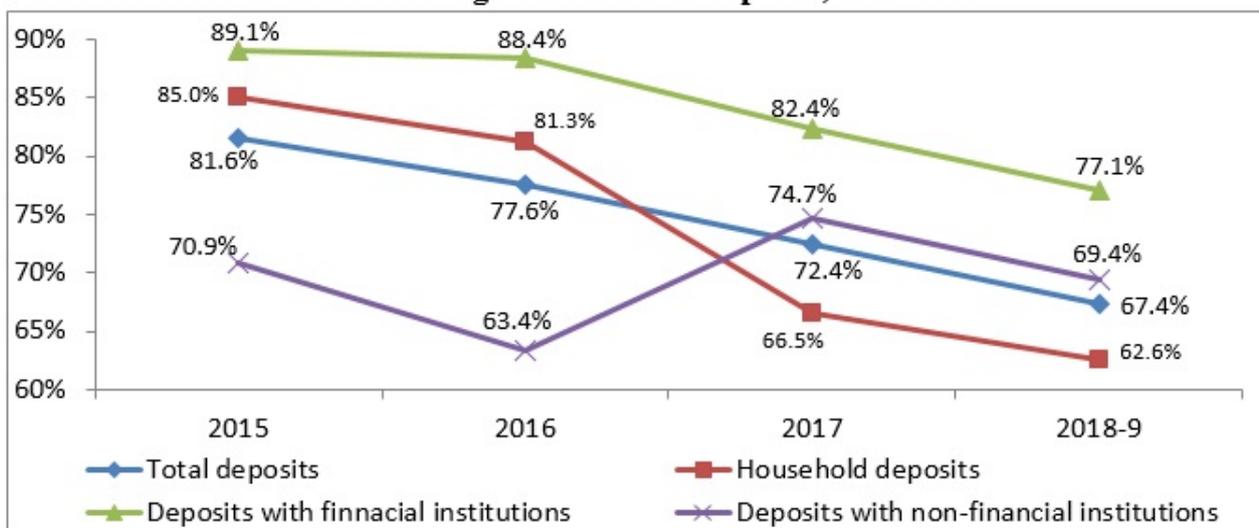
Chart 10: Percentage of foreign currencies in lending (2014-2018)



Source: Central Bank of Azerbaijan.

The stability of the national currency and low profitability offered by banks in foreign currency decreased the interest of individuals and legal entities in investments in foreign currency, which, in turn, had a detrimental effect on the level of dollarization of deposits. The downward tendency towards the dollarization of *total deposits* continued in 2018, dropping from 72.4% to 67.4% as of the end of quarter III. The lowest level of dollarization was observed in household (retail) deposits, dropping from 66.5% to 62.6% as of the end of September 2018. The share of foreign currency in the *deposits with financial institutions* that saw the highest dollarization due to the devaluation (89.1%) shrank to 77.1% as of October 1, 2018. Although *deposits with non-financial institutions* tended towards dollarization in 2017, it has been replaced by dedollarization since 2018 (see *Chart 11*).

Chart 11: Trend in share of foreign currencies in deposits, 2015-2018



Source: Central Bank of Azerbaijan.

Major trends

Analysis of official statistical data has revealed the following tendencies observed in Azerbaijan's banking system during the first nine months of 2018:

- The concentration in the banking sector that had slackened since 2017 has been replaced by a moderate growth rate.
- The number of bank networks (branches and departments) and staff has grown.
- The decrease in Azerbaijan's banking assets observed in recent years has been replaced by an increase during the first nine months of 2018.
- Banks have continued to invest in securities and nearly tripled compared to the same period of 2017.
- Lending has seen growth thanks to private banks, particularly those with local capital.
- The share of consumer sector loans has surged by 41.1%, the highest figure for the past four years.
- Lending in national currency has surged, but that in foreign currency has shrunk.
- Banks have chosen to provide short-term loans.
- Regions have seen more growth in lending compared with

lending to Baku.

- Overdue loans have continued to increase.
- The dependence of banks on deposit resources has continued.
- The total deposit growth has been attributable to national currency deposits, while foreign currency deposits have narrowed.
- The decreasing tendency in annual interest rates on manat deposits has not diminished the attractiveness of deposits in this currency.
- The demand deposits have increased.
- The share of centralized loans given by the Central Bank of Azerbaijan has continued to decrease.
- The number of bank customers is reported to have increased and the banking sector set a record for number of customers.
- Dollarization of the banking system has started showing a decline.

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