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Ensuring the Stability of Commercial Banks in the Conditions of Transforming the Banking System

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Abstract: The main goal of transforming the country's banking system is to create the necessary conditions to ensure the stability of the activities of commercial banks. In particular, the development of the infrastructure necessary for the activities of commercial banks, the implementation of a balanced macroeconomic policy, and the reduction of state participation in the banking system are important conditions. The article develops scientific proposals aimed at ensuring the stability of the activities of commercial banks in the context of the transformation of the banking system of Uzbekistan.

Keywords: banking system, commercial banking, transformation, credit, problem credit, deposit, financial stability, reserve, capital, interest rate

1. Introduction

The Strategy for Reforming the Banking System of the Republic of Uzbekistan for 2020-2025, approved by the Decree of the President of the Republic of Uzbekistan No. 5992 dated May 12, 2020, reflects the following urgent tasks related to ensuring the stability of the activities of commercial banks through the transformation of the country's banking system[1]:

- reducing the dependence of banks on state resources;
- modernizing the provision of banking services;
- creating an effective infrastructure of banks and automating their activities;
- phasing out functions that are not inherent in the activities of banks;
- improving the quality of credit portfolio and risk management;
- pursuing moderate growth in lending volumes;
- pursuing a balanced macroeconomic policy;
- improving corporate governance in banks and attracting managers with international practical experience;
- implementation of technological solutions for financial risk assessment;
- introduction of modern banking standards, information technologies and software products;

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- sale of a package of state shares in banks to investors with the necessary experience and knowledge on a competitive basis[2].

This, in turn, creates the need to ensure the stability of commercial banks in the context of reforming the country's banking system.

2. Materials and Methods

The purpose of the study is to develop scientific proposals aimed at ensuring the stability of the activities of commercial banks in the context of the transformation of the country's banking system.

The subject of the study is the financial relations that arise in the process of ensuring the stability of the activities of commercial banks in the context of the transformation of the banking system.

The information base of the study includes statistical data on the activities of commercial banks of the Republic of Uzbekistan and foreign banks, as well as empirical studies conducted by international experts[3].

According to E. Shakirova, the Bank Payment Obligation is an irrevocable obligation of the recipient bank (Obligor Bank), which guarantees the transfer of the payment amount to the notifying bank, but there should be no discrepancies when comparing documents[4].

It should be noted that blockchain technology is widely used in stock exchanges, which are mainly carried out in the securities market. In particular, the NASDAQ exchange, which specializes in trading shares of high-tech companies, has conducted several experiments on the use of blockchain technology, and the JEG company, which unites the London Stock Exchange (LSE) and the Japanese stock exchange, is also conducting experiments on the use of blockchain technology.

One of the promising payment technologies that has begun to be used in international trade is the electronic letter of credit technology. The main difference between the electronic letter of credit and the traditional letter of credit is that the exchange of documents in the electronic letter of credit is carried out through electronic communication channels, while in the traditional letter of credit, it is carried out in the form of mutual exchange of documents in the form of paper sent by couriers.

It is worth noting that the document verification technology in an electronic letter of credit does not fundamentally differ from a traditional letter of credit. The reason for this is that in an electronic letter of credit, the bank, which has received the goods documents through electronic carriers, prints them out from the printer and then checks them for compliance with the terms of the letter of credit. In the traditional letter of credit, the goods documents in paper form are checked by the receiving bank.

The analyzes conducted by a group of economists showed that sending a package of documents through paper carriers costs USD 75-100 to the parties involved in the letter of credit and takes 3 to 7 days. If the terms of the letter of credit allow for the shipment of goods in installments, the number of documents to be submitted will increase several times. Using an electronic letter of credit allows you to get rid of such expenses and quickly receive export proceeds. In addition, receiving documents via electronic carriers reduces the number of errors and fraud. There was a case when DHL employees mistakenly read the country code SA (Saudi Arabia) and confused this code with USA (United States), sending documents from Russia to the United States, not Saudi Arabia. Thanks to an electronic letter of credit, the level of transparency of the obligation increases and it becomes possible to open it for a short period of time. This, in turn, allows you to reduce the amount of commission charged for opening a letter of credit, since in most cases the amount of commission is set depending on the term of the bank's obligation under the letter of credit.

According to V. Dorofeev, the bank's growth strategy involves an aggressive competitive policy, which is aimed at squeezing out competitors using extremely harsh methods, including not always legitimate ones[5]. The implementation of this strategy is associated with a priority focus on relatively profitable and high-risk financial operations.

N. Kunitsina concludes that "firstly, the quantity and quality of income received by banks are an important factor in the formation of their income base; secondly, the decrease in banks' income is an objective indicator of their financial difficulties; thirdly, interest income is more important than interest income"[6].

In our opinion, this conclusion of N. Kunitsina is of practical importance. Because, firstly, the quantity and quality of income received by banks determine the stability of the net profit of commercial banks; secondly, the main indicator characterizing the quality of commercial banks' income is the ratio of income to expenses; thirdly, the lack of a proportionality between the growth rate of income-generating assets and the growth rate of income from income-generating assets prevents the stability of net profit.

J. Heckman's cross-sectional selective model argues that the formation of "holes" in the capital of commercial banks is the result of a violation of the balance sheet in the term structure of bank operations[7]. This model differs from standard regression models that determine the level of a certain indicator, for example, linear models. For example, selective models retain the possibility of introducing an incomplete sample into the object under study (sample selection bias). In this case, the model considers two groups of economic agents - households and companies, and for each group the following three types of imbalance are provided:

- imbalance in operations with a term of up to 1 year;
- imbalance in operations with a term of 1 to 3 years;
- imbalance in operations with a term of more than 3 years.

A joint study by M. Goetz, L. Laeven, and R. Levin found that commercial banks that are geographically diversified across U.S. states are less risky[8]. Moreover, geographic complexity does not affect loan quality. They used statistical data on bank expansion across U.S. states, distinguishing geographic diversification from line of business diversification, but did not examine international diversification.

3. Results and Discussions

A positive experience that is of practical importance and worth studying in ensuring the stability of commercial banks in the context of the transformation of the banking system in developed countries is the full implementation of the new requirements of the Basel Committee on banking supervision (Basel III).

Table 1. The amount of regulatory capital and its level relative to gross assets at Deutsche Bank in Germany

Indicators	2019	2020	2021	2022	2023
Amount of regulatory capital, mln. euro	55857	54786	58027	61959	64486
The ratio of regulatory capital to gross assets, %	4,3	4,1	4,4	4,6	4,9

The data presented in Table 1 clearly shows that the amount of regulatory capital at Deutsche Bank had an increasing trend in 2020-2023. Moreover, the amount of

regulatory capital increased significantly in 2023 compared to 2017. This is a positive situation from the point of view of ensuring the competitiveness of Deutsche Bank[9].

The data presented in Table 1 clearly shows that the level of regulatory capital to gross assets at Deutsche Bank was stable at no less than 4.0 percent in 2020-2023. Moreover, the level of this indicator increased significantly in 2023 compared to 2019.

Table 2. Changes in the amount of primary reserves and investments in government securities at Bank of America, billion US dollars

Indicators	2019	2020	2021	2022	2023
Primary Reserves	161	380	348	230	333
Investments in government securities	274	304	250	267	280

Table 2 clearly shows that the amount of primary reserves at Bank of America had a decreasing trend in 2020-2022. However, the amount of primary reserves increased at a higher rate in 2023 compared to 2022. This is a positive situation from the point of view of ensuring the bank's liquidity. Since the absolute majority of primary reserves are funds in the bank's "Nostro" correspondent accounts[10].

Table 2 clearly shows that the amount of Bank of America's investments in government securities had a growth trend in 2021-2023. Moreover, the amount of investments in government securities increased at a higher rate in 2023 than in 2019. This is a positive situation from the point of view of ensuring the bank's liquidity[11]. Because investments in government securities are highly liquid assets for commercial banks.

According to official data from the Central Bank of the Republic of Uzbekistan, the following important measures were taken to transform the country's banking system in 2023:

*In 2023, work continued on improving legislative documents related to the transformation of state-owned banks and the introduction of a modern corporate governance system in them. In particular, amendments were made to the Law "On Banks and Banking Activities" to gradually increase the minimum authorized capital of the bank from 100 billion soums to 500 billion soums by January 1, 2025[12];

*In 2023, the President of the Republic of Uzbekistan adopted relevant resolutions on additional measures to strengthen the financial stability of JSCB "Uzsanoatqurilishbank" and accelerate the privatization of state-owned enterprises, including commercial banks, in order to increase their financial stability, investment attractiveness and operational efficiency, prepare for privatization, and attract strategic investors to the banking system;

*The reduction of the state share in Ipoteka-Bank JSC, the increase in the capitalization of commercial banks, and the entry of 3 new banks into the banking services market contributed to the reduction of the state share in total banking sector assets from 78% to 68% in 2022, and its share in total bank capital from 78% to 65%. In 2023, the Hungarian bank OTP Bank purchased 75% of the shares of Ipoteka-Bank JSC belonging to the Ministry of Economy and Finance of the Republic of Uzbekistan;

*In order to increase operational efficiency at Asakabank JSC, the efficiency of the bank's head office and several branches was assessed by KPMG Tax and Advisory, and the organizational structure of the bank was revised based on the results obtained;

* Portfolio Investments LLC was selected as the underwriter for the initial public offering (IPO) of Aloqabank shares on the stock exchange[13].

Table 3. The amount of regulatory capital of JSC "UzSanoatqurilishbank" and the weight of liabilities

Indicators	2019	2020	2021	2022	2023
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Amount of regulatory capital, bln. soum	6 246	6 704	7 700	7 828	8 728
The weight of regulatory capital in the volume of liabilities, %	17,9	13,7	13,6	12,2	11,7

As can be seen from Table 3, the regulatory capital of Sanoatqurilishbank had a tendency to grow in 2017-2023. This is a positive situation from the point of view of ensuring its competitiveness.

As can be seen from Table 3, the share of Sanoatqurilishbank's regulatory capital in the volume of liabilities had a tendency to decrease in 2019-2023[14]. This is a negative situation from the point of view of ensuring its competitiveness.

The adequacy of the deposit base of a commercial bank is a unique indicator of its position in the loan capital market.

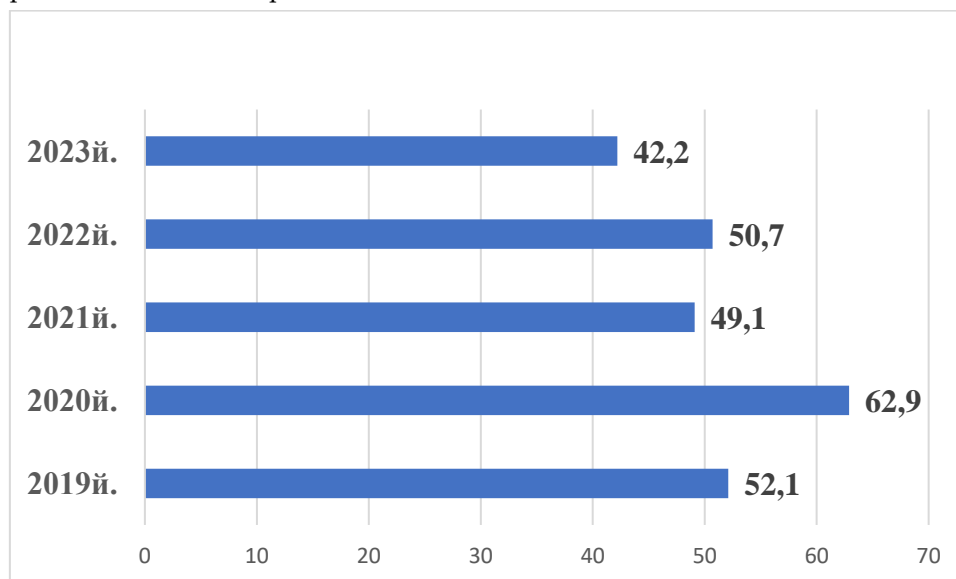


Figure 1. Share of demand deposits in total deposits at UzSanoatqurilishbank, in percent (as of December 31 of each fiscal year)

It can be seen from Figure 1 that the weight of demand deposits in Sanoatkurilishbank in total deposits decreased significantly in 2023 compared to 2019, but the adequacy of the deposit base was not ensured during the analysis period.

4-жадвал

About problem loans of commercial banks of the Republic of Uzbekistan

Indicators	2019	2020	2021	2022	2023
Amount of problem loans, bln. soum	3169	5785	16974	13992	16621
The weight of problem loans in the volume of gross loans, %	1,5	2,1	5,2	3,6	3,5

The data in Table 4 allow us to draw the following conclusions:

The volume of problem loans of commercial banks of our republic had a growth trend in 2017-2021. Moreover, the volume of problem loans in 2023 increased at a higher rate (12.5 times) compared to 2017. This is a negative situation from the point of view of ensuring the competitiveness of commercial banks;

The share of problem loans in the total volume of loans of commercial banks of the country had a growth trend in 2017-2021. Moreover, the level of this indicator increased at a higher rate (2.3 percentage points) in 2023 compared to 2017[15]. This is a negative situation from the point of view of ensuring the competitiveness of commercial banks.

4. Conclusion

In the course of the research, we have formed the following conclusions:

*Bank Payment Obligation is an irrevocable obligation of the recipient bank (Obligor Bank), which guarantees the transfer of the payment amount to the notifying bank, but there should be no discrepancies when comparing documents;

*The bank's growth strategy involves an aggressive competitive policy, and this competitive policy is aimed at squeezing out competitors using extremely harsh methods, including not always legitimate ones. The implementation of this strategy is associated with a priority focus on relatively profitable and high-risk financial operations;

*It is argued that the formation of "holes" in the capital of commercial banks is the result of a disruption in the balance in the term structure of bank operations. This model differs from standard regression models, for example, linear models, which determine the level of a certain indicator;

*The fact that the regulatory capital of the Industrial Construction Bank had a growth trend in 2017-2023 is considered a positive situation from the point of view of ensuring its stability;

*The weight of the regulatory capital of the Industrial Construction Bank in the volume of liabilities had a decreasing trend in 2019-2023;

*The weight of demand deposits in the total deposits of the Industrial Construction Bank decreased significantly in 2023 compared to 2019, but the sufficiency of the deposit base was not ensured during the analysis period;

*While the volume of problem loans of commercial banks of our republic had a growth trend in 2019-2023, the weight of problem loans in the total volume of commercial banks' loans had a growing trend in 2019-2022.

In our opinion, in order to ensure the stability of commercial banks in the process of transformation of the country's banking system, the following measures should be taken:

1. It is advisable to increase the efficiency of the organizational and functional structure of the bank by transferring the work carried out under state programs to the Operational Block of the bank, and by dividing the underwriting and project financing departments into directions by type of business.

After transferring the work carried out under state programs to the Operational Block of the bank, while preserving these functions, the main focus will be on working with clients and selling products. Naturally, in such conditions, the focus will be on strengthening the activities of the back office, not the front office.

In such conditions, attracting clients, working with clients, and underwriting will remain in the Corporate business.

2. In order to ensure a high and stable level of net profit of commercial banks relative to gross assets, it is necessary to improve the composition of classified loans, ensure a low and stable level of reserve provisions for loans, ensure a proportionality between the growth rates of gross income and income-generating assets, increase the amount of interest income of commercial banks by developing investment operations with securities, and ensure a proportionality between the growth rate of interest income and the growth rate of interest expenses.

The low level of the return on assets indicator in Uzsanotskurilishbank in 2019-2023 is explained by the following reasons:

- the fact that the amount of interest expenses had high growth rates during the analyzed period;

– the fact that the amount of reserve provisions intended to cover losses on loans had a growth trend and high growth rates during the analyzed period.

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