

THEORETICAL AND PRACTICAL ANALYSIS OF STRENGTHENING THE INCOME BASE OF COMMERCIAL BANKS

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Abstract. This article examines the issues of strengthening the income base of commercial banks of the Republic of Uzbekistan from a theoretical and practical perspective. Within the framework of the study, the indicators of profitability, net interest margin, loan portfolio profitability and return on equity of banks for 2021–2025 were analyzed using the example of the activities of JSC "Asakabank". The "CAMELS" rating system, IMF and IMF methodologies, and the advanced experience of foreign banks such as Bank of America, Deutsche Bank, BNP Paribas were studied.

Based on the results of the research, scientific proposals and practical recommendations were developed to strengthen the revenue base of commercial banks.

Keywords: commercial bank, income base, net interest margin, loan portfolio, return on equity, CAMELS, risk management, banking system of Uzbekistan.

INTRODUCTION

In our republic, special attention is paid to achieving stability in the share of stable liabilities in the volume of gross liabilities, ensuring stability in the profitability of loan operations, increasing the volume of interest income based on improving the investment practices of banks, reducing the cost of financial services through the digitization of their services, reducing the amount of losses associated with assets through the development of a risk management system, and increasing the efficiency of the transformation of liabilities by increasing the level of diversification of financial resources. "Developing a system for assessing and managing financial risks based on advanced foreign experience, implementing lending exclusively on market terms, reducing the dependence of banks on state resources, "Improving the quality of credit portfolio management, pursuing moderate growth in lending volumes, and comprehensively transforming state-owned banks"¹ identified as priority areas for reforming the national banking system.

Strengthening the income base of commercial banks is a prerequisite for ensuring the stability of the banking system. Trends observed in global banking practice show that the failure to optimize returns on assets poses a serious threat to the financial stability of banks. In particular, at the US bank Bank of America, the profitability of loans increased by 1.8 percentage points in 2023 compared to 2022, while at the German bank Deutsche Bank, the profitability of funded assets increased by 2.1 percentage points.

¹Decree of the President of the Republic of Uzbekistan dated May 12, 2020 No. PF-5992 "2020-2025-yillarga mo'ljallangan O'zbekiston Respublikasining bank tizimini isloh qilish strategiyasi to'g'risida" // QHMMB: No. 06/205992/0581. 13.05.2020.

In the Republic of Uzbekistan, special attention is being paid to strengthening the income base of banks by expanding the volume of stable liabilities, ensuring the profitability of loan operations, and digitizing financial services. The President's 2020 "Strategy for Reforming the Banking System for 2020–2025" identifies lending exclusively on market terms, improving the quality of loan portfolio management, and comprehensive transformation of state-owned banks as priority tasks.

Literature Review

In Western economic literature, including that of developed countries, the issue of strengthening the income base of commercial banks is a subject of scientific debate.

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. The implementation of this strategy is associated with a priority focus on relatively profitable and high-risk financial operations.²

In fact, the aggressive growth strategy is based on a policy of chasing profits. High profits come from high-risk financial operations. It should be remembered that the pursuit of profits can put a commercial bank in a difficult financial situation and, ultimately, lead to a sharp deterioration in the bank's financial condition.

According to the conclusion of a group of economists led by S. Kumok, "at the present time, it is practically impossible to increase the rate of return on capital by reducing capital adequacy. Fierce competition and the rise in the cost of credit resources do not allow achieving the optimal level of capital in relation to assets. Therefore, the main reserve for increasing the rate of return on total capital is to increase the rate of return on assets."³

Indeed, an increase in the cost of commercial banks' liabilities reduces the amount of net interest income in banks, which ultimately reduces the return on capital.

N. Kunitsyna concludes that "firstly, the quantity and quality of income received by banks is an important factor in the formation of their income base; secondly, a decrease in banks' income is an objective indicator of their financial difficulties; thirdly, interest income is more significant than interest income"⁴.

In our opinion, this conclusion of N. Kunitsyna 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 the income of commercial banks is the ratio of income to expenses; thirdly, the lack of a balance between the growth rate of income-generating assets and the growth rate of income from income-generating assets prevents the stability of net profit.

This conclusion of A. Abdullayev is of practical importance from the point of view of ensuring the stability of the income of banks in our republic. This is due to the fact that the amount of non-revenue cash assets in the total volume of assets of commercial banks in our republic is significantly high. As of January 1, 2024, the share of cash assets in the total volume of assets of

²Dorofeev V.D. Strategicheskoye planirovaniye kommercheskogo banka//Izvestiya vysshikh uchebnykh zavedeniy. Povolzhsky region. Obshchestvennye nauki. - 2013. - No. 2 (26). - P. 168.

³Analyz deyatelnosti kommercheskikh bankov / pod obshch. ed. SI Kumok. - M.: Veche, 1996. - P. 153.

⁴Kunitsyna, N.N. Business planning and commercial bank. - M.: Finance and statistics, 2007. - 304 p.

commercial banks of the Republic of Uzbekistan was 16.3 percent⁵. This is a significantly high figure.

According to F. Kholmatov, "it is necessary to prevent an increase in the standard level of reserve provisions intended to cover losses incurred on loans in commercial banks and to increase the share of interest income from loans in the gross income of commercial banks by ensuring a stable level of the net interest margin indicator."⁶.

This proposal by F. Kholmatov is based on the analysis of practical data and is of practical importance in terms of improving the lending practices of the country's banks. This is due to the fact that, firstly, the level of loan reserves in the country's banks relative to gross assets is higher than the generally accepted level; secondly, the regulatory level of net interest margin (4.5%) is not ensured in large commercial banks in the banking system of the republic.

Research Methodology

The following methodological approaches and sources of information were used in the study:

1. Official statistics of the Central Bank of the Republic of Uzbekistan (2021–2025).
2. Annual financial reports of JSC "Asakabank" and JSC "Aloqabank".
3. Public financial statements of Bank of America, Deutsche Bank and BNP Paribas.
4. The "CAMELS" rating system developed by US banking regulators, the IMF and the International Bank for Reconstruction and Development assessment methodologies.

During the analysis, comparative, grouping, dynamic analysis, coefficient analysis, and statistical evaluation methods were used in combination.

Analysis and Results

The main indicators used to assess the sustainability of banks' income base are net interest margin (NIM), return on assets (ROA), return on equity (ROE), loan portfolio profitability, and the ratio of reserve provisions to gross assets.

When setting the regulatory threshold levels, the recommendations of the IRB experts (reserve provisions $\leq 1.0\%$; problem loans $\leq 5.0\%$) and the criteria of the "CAMELS" system were used. The regulatory level of the net interest margin was taken as 4.5%. The duration of the study covers the years 2021–2025.

In international banking practice, three main methodologies are used to assess the stability of the income base of commercial banks: the US "CAMELS" rating system, the IMF methodology, and the IBRD assessment methodology. In the "CAMELS" system, income stability is assessed in five groups:

Table 1.

⁵Consolidated balance sheet of commercial banks//www.cbu.uz

⁶Kholmatov FK Improving the lending practices of commercial banks. Ifd diss. author ref. – Tashkent, 2019. - P. 25.

Criteria for assessing bank income in the CAMELS rating system⁷

	Rating	Criterion
1	Strong	Gross income covers all expenses and reserves; interest and non-interest income meet quality criteria.
2	Satisfactory	Gross income covers expenses and reserves; there is a relative decline in indicators.
3	Average	Revenue is not enough to fully cover expenses; there is a decline in quality standards.
4	Borderline	It is impossible to build reserves; the net interest margin is not sustainable.
5	Unsatisfactory	Losses are not being covered; the amount of capital is decreasing.

In the CAMELS system, bank earnings are rated on a scale of 1 to 5, from the highest ("strong") to the lowest ("unsatisfactory"). The table data is based on three main factors in assessing the financial security and strength of a bank's income base - the ability to cover costs, the ability to build reserves, and the quality and stability of earnings.

In the case of Bank of America, the loan portfolio and its profitability trends for 2019–2023 are as follows:

Table 2.**Bank of America's loan portfolio and profitability⁸**

Indicator	2019	2020	2021	2022	2023	2024	2025
Loans (billion USD)	4.0	97	90	96	1,03	1,04	1,08
Profitability (%)	4.4	9.1	6.7	3.1	0.4	2.6	172.5
Non-interest income (USD billions)	4	42.	2	42.	2	46.	42.5
Non-interest expense (USD)	9	54.	2	55.	7	59.	61.4

⁷Supervision and Regulation. CAMELS rating system. <https://www.federalreserve.gov>.

⁸Table Annual Reports. Consolidated Balance Sheet. <http://investor.bankofamerica.com> Compiled by the author based on data from (Bank of America).

Indicator	2019	2020	2021	2022	2023	2024	2025
billions)							

The data in Table 2 shows that the volume of loans decreased in 2020 compared to 2019 and had an increasing trend from 2021 to 2025.

This is explained by the bank's increased activity in the market and the volume of lending to economic sectors.

Although loan yields showed a downward trend in 2021, falling to 3.0 points, they rose sharply in 2023, rising to 5.5 points.

This is due to the fact that the growth rate of interest income from loans granted in 2023 is higher than the growth rate of gross loans. This will have a positive impact on the strengthening of the bank's net interest margin.

Non-interest income is expected to be \$41.7 billion in 2023, down from \$46.2 billion in 2021.

Non-interest expenses, on the other hand, have been steadily increasing year by year over the years under review, reaching \$65.8 billion in 2023.

During 2019-2025, the balance between non-interest income and non-interest expenses was not ensured. That is, the growth rate of expenses was higher than that of income. This situation creates the need to improve the bank's operational efficiency and optimize expenses.

At the same time, it is worth noting that the bank's main income has been strengthened by interest income, that is, mainly from lending. In turn, the increase in the amount of retained earnings will allow the bank, like other transnational banks, to increase its capital and improve its material and technical base.

The profitability of loans directly depends on the quality of credit, interest rate and liquidity risk management. The table shows that the bank strives to maintain long-term strategic stability for 2024-2025.

We will analyze the activities of JSC "Asakabank" in 2019-2024 in terms of the current state of the income base of commercial banks in Uzbekistan.

Table 3.

Loan portfolio and profitability of JSC "Asakabank" (billion soums)⁹

Indicator	2019	2020	2021	2022	2023	2024
Loans, billion soums	26,321	34,122.3	37,685.4	36,741.7	39,213.3	38,717.3
Interest income from loans, billion soums	1,724	2,137	2,398	2,824	3,728.0	4,324.0

⁹The table was compiled by the author based on data from the annual reports of JSC "Asakabank".

Indicator	2019	2020	2021	2022	2023	2024
1 soum loan income (%)	6.5	6.3	6.4	7.7	9.5	11.2

From the data in Table 3, we can see that the loan portfolio of JSC "Asakabank" has increased from 26,321 billion soums in 2019 to 39,213.3 billion soums by 2023. This indicates that the role of JSC "Asakabank" in lending to national economic entities, in particular the automotive industry, is increasing.

Such a rapid growth in the nominal value of the loan portfolio is also explained by the impact of inflation in the domestic market and the devaluation of the national currency, which led to an increase in the cost of imports.

By 2024, the size of the loan portfolio had moderated slightly, amounting to 38,717.3 billion soums.

The amount of interest income from loans increased at a very high rate during the analysis period. In particular, in 2019 this figure was 1,724 billion soums, in 2023 it reached 3,728 billion soums, and at the end of 2024 it reached 4,324.0 billion soums.

This consistent growth in interest income is a very positive trend in terms of ensuring the stability of the bank's gross income and financially strengthening its income base.

The rate of return on a loan of 1 soum showed a slight downward trend (from 6.5% to 6.4%) in 2019–2021. However, starting in 2022, the indicator began to grow actively, reaching 9.5% in 2023 and 11.2% in 2024.

This significant increase in profitability is characterized by the fact that the growth rate of interest income collected on loans issued is higher than the growth rate of gross loans. This indicates that the efficiency of bank assets is increasing.

Macroeconomic factors in the Uzbek economy have a significant impact on the revenue base of commercial banks.

Table 4.

Dynamics of inflation and the Central Bank's key rate, %¹⁰

Indicator	2019	2020	2021	2022	2023	2024	2025
Annual inflation (%)	15.	11.	10.	12.	8.8	9.8	7.3
MB key rate (%)	16.	14.	14.	15.	14.	14.	14.
Commercial bank	24.	22.	20.	21.	23.	23.	22.

¹⁰The table was compiled by the author based on official statistical data from the Central Bank of the Republic of Uzbekistan (www.cbu.uz).

Indicator	2019	2020	2021	2022	2023	2024	2025
lending rate (%)	2	3	8	9	2	6	6

Table 3 shows that the annual inflation rate in the country decreased from 15.1 percent in 2019 to 10.0 percent in 2021, but rose again in 2022 to 12.3 percent due to external shocks, disruptions in logistics and supply, and increased consumer demand. Although inflation decreased to 8.8 percent in 2023, it increased by 1 point in 2024 to 9.8 percent and fell to 7.3 percent in 2025. The current level of inflation directly affects the real value of bank assets and the price of deposits attracted.

The central bank's key rate has been changing in line with inflationary processes in the economy. In 2019–2021, when inflation declined, the key rate was reduced from 16.0 percent to 14.0 percent.

In 2022, when inflationary pressures intensified, the Central Bank was forced to increase the key rate to 15.0 percent. In 2023–2025, this rate remained consistently unchanged at 14.0 percent in order to curb inflation and maintain moderate monetary conditions.

The average annual interest rate on loans in the national currency of commercial banks was directly proportional to the change in the key rate of the Central Bank. In the years when the key rate decreased (2019–2021), lending rates also decreased from 24.2 percent to 20.8 percent.

In 2022, when the key rate increased by 1.0 percentage points, the lending rate also increased to 21.9 percent. It is noteworthy that in 2023–2024, the Central Bank's key rate decreased to 14.0 percent and remained at 14.0 percent, while the lending rates of commercial banks continued to grow to 23.2 percent and 23.6 percent. This is explained by the fact that banks continue to have unbalanced liquidity levels and an increase in the cost of the resource base.

Conclusion and Recommendations

During the research process, we formed the following conclusions:

Based on the results of the study, a number of urgent problems related to strengthening the income base of Uzbek commercial banks were identified.

First, the concentration risk of the loan portfolio is high. In JSC "Asakabank", the share of loans to the industrial sector in 2019–2025 was 63–71%. According to generally accepted practice, it is not advisable for the share of one sector to exceed 25%. The low level of diversification of the loan portfolio increases the level of credit risk and negatively affects the stability of income.

Secondly, the underdevelopment of fund asset operations. The share of investments in securities in the assets of Uzbek commercial banks in 2023 was only 5.7%. In foreign banks, fund assets account for 15–20% of assets. The turnover in the stock market is 147 times smaller than in the foreign exchange market.

Third, a high share of transactional deposits increases liquidity risk and leads to instability of the deposit base. In European banking practice, transactional deposits are not seen as a source of resources, but only as their stable balance.

Fourth, inflation and currency depreciation pose a serious threat to commercial banks. The som's exchange rate against the US dollar steadily depreciated between 2010 and 2023, reducing the real value of banks' assets.

Based on the research results, we have developed the following scientific proposals and practical recommendations:

1. Ensuring a regulatory level of net profit. Commercial banks should have a net profit ratio of at least 2.0%. This requires ensuring a stable ratio of interest expenses to interest income and strengthening the diversification of the loan portfolio.

2. Diversification of the loan portfolio. The credit policy should establish a criterion that the share of loans granted to one sector should not exceed 15% of the loan portfolio. A 5% fluctuation may be allowed, taking into account the sector's situation.

3. Formation of a system of indicators characterizing the profitability of loans. The recommended group of indicators: the level of provisioning (norm $\leq 1.0\%$); the ratio of the growth rate of loan income to the growth rate of loans; the level of overdue loans (norm $\leq 5.0\%$); net interest spread (norm $\geq 1.25\%$).

4. Development of fund asset operations. It is necessary to exempt from profit tax the income received by commercial banks from investments in highly liquid securities. In addition, it is an effective method to direct excess funds from "Nostro" accounts to Government securities, provided that the instant liquidity standard is met.

5. Improve the management of transaction deposits. Only stable balances of transaction deposits should be used to finance credit and investment operations.

6. Achieving a target level of net interest margin (4.5%). To do this, it is necessary to maintain the growth rate of net interest income above the growth rate of gross assets.

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