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DEVELOPMENT PROBLEMS OF RETAIL FINANCIAL SERVICES IN UZBEKISTAN

PROBLEMY ROZWOJU DETALICZNYCH USŁUG FINANSOWYCH W UZBEKISTANIE

Key words: retail financial services, retail lending, interest rate
Słowa kluczowe: detaliczne usługi finansowe, pożyczki, oprocentowanie detaliczne

Abstract. The paper aims to analyse the development of retail financial services in conditions of government intervention. It is argued that excessive state control of the market for retail financial services is needed in times of crisis and increased moral hazard occurrence but is not effective in the long term. Development could be achieved by expanding privatization in the banking sector and permitting the sector to function freely according to market rules.

Introduction

Since independence Uzbekistan has confidently engaged in the creation of the national banking system, which to date has a 22 year history. During this short period, a unified system of management of the entire banking sector was created. It is headed by the Central Bank of the Republic of Uzbekistan. All other banks are specialized commercial banks that strictly follow the rules of the Central Bank, regardless of their form of ownership. To date, the country has 30 commercial banks, 3 of which are state-commercial, 13 joint-stock commercial, 9 private and 5 with private foreign capital. There are 822 branches and 1,450 mini-banks spread throughout the region, covering even the most remote villages of the country.

To date, the activities of the banking system rigidly conform to international standards. They are one of the most stable of systems. This is proven by the estimations of international rating agencies such as "Standard & Poor's", "Moody's", "Fitch ratings" which have given a "stable" rating level in recent years. In particular, if in 2010 the "stable" international ranking of „Moody's" was obtained by a total of 13 commercial banks in the country, in 2013 the number of such banks reached 28 [*Our main goal*… 2013].

Despite the stability of the banking sector in Uzbekistan, the problem of the development of retail banking remains acute. According to the statistical figures in 2012 for retail lending, banks granted funds amounting to more than 1 trillion sums (the national currency of Uzbekistan), while for investment purposes to legal entities – over 5.7 trillion sums. These data show that the bulk of bank loans goes to large business. But even this amount of investment credits, according to the World Bank, does not exceed half of such loans in countries with economies in transition [*The partnership of World Bank*… 2013]. In other words, the volume of total loans in the country is not considered high and neither is the share of retail loans.

Objectives, materials and methods

This paper aims to provide a critical analysis of the development of retail financial services in conditions of government intervention. It aims to conduct comparative analysis of the retail financial market of Uzbekistan with other market-oriented economies. The basis for discussion will be a critical review of statistics data.

Analysis of the development of retail financial services

Under the conditions of the formation of a civil society, it is important to create an appropriate level of retail lending along with the development of industrial credit. Retail lending involves lending to consumers and entrepreneurs who are not a legal entity.

Although all commercial banks offer retail financial products, generally retail financial services in Uzbekistan are still at an early stage of development. For the development of retail banking services it is not enough for commercial banks to simply "turn their face" to customers. They need to develop a full-fledged strategy for promoting services in the financial market.

Retail banking in Uzbekistan retains the traditional method of customer service – direct contact of the bank with the customer, granting loans only after documentary confirmation of customer credit worthiness and compliance with numerous regulations. A ramified branch network of mini-banks and savings banks has been created for this purpose. The number of bank branches per 100 000 of the adult population in Uzbekistan is 45.4. By comparison, in Ukraine it amounts to – 1.1, Kazakhstan – 3.3, Russia – 38.2, UK – 24.2, France – 38.8. This suggests a high level of physical access to banking services by international standards. But on the other hand, Uzbek banks are skeptical of machines – the number of bank branches is higher than in the UK and France, but the number of ATMs is lower than in India (Fig. 1). Remote banking services in Uzbekistan covers less than 1% of the customer base of the banks. By comparison, in Russia the level is – 4.2%, Italy – 12.7%, UK – 51%, France – 56%, Canada – 65% (based on results in 2010) [*Finance retail* 2013].

The current situation in the financial sector of developed countries shows that the traditional approach is not an obstacle, but it also does not accelerate growth.
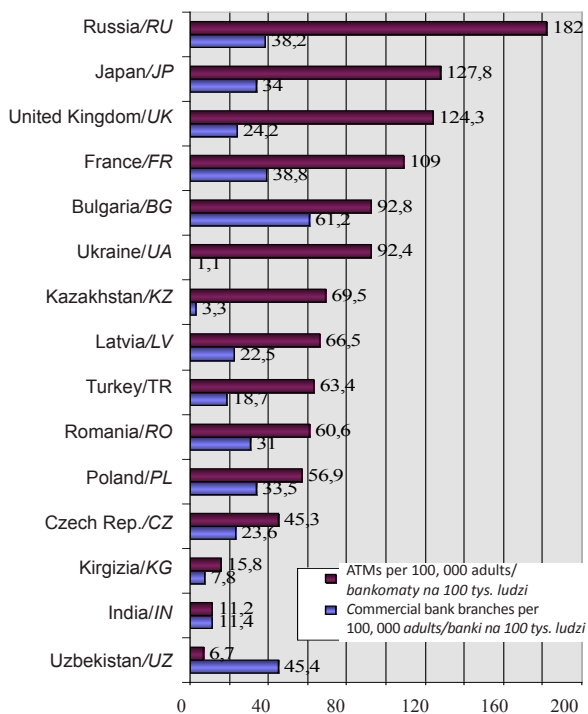

Figure 1. Number of banks and ATM machines to 100,000 of the adult population in some countries of the world (on the results 2012)
Rysunek 1. Liczba banków i bankomatów na 100.000 mieszkańców w wybranych krajach na świecie (na podstawie wyników 2012)
Source/*Źródło*: IMF, http://fas.imf.org/

It can be noted that retail lending in Uzbekistan is growing at a significant pace. The global financial crisis has had a short-term impact on the retail lending market. If before 2008 the pace of retail lending increased, then in 2009 it decreased because of a reduction in consumer loans, and in 2010 – at the expense of loans to entrepreneurs without legal entity. A recovery took place in 2011 – consumer loans increased by almost 44%, loans to entrepreneurs without legal entity – by 27%, while the overall retail loans by 41.1% (Fig. 2).

Such accelerated growth recovery was not achieved through the initiative of commercial banks, but with the government's efforts through the implementation of several major programs.

Figure 2. The rate of
growth in retail lending
in Uzbekistan
*Rysunek 2. Tempo wzrostu
kredytów detalicznych w
Uzbekistanie*
Source/*Źródło*: [*Finance
retail* 2013]
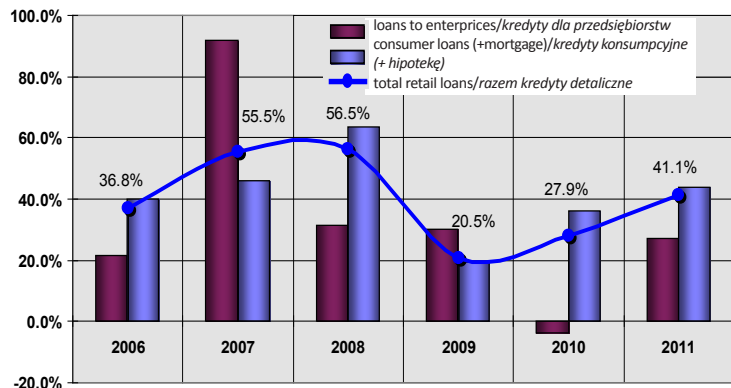
Firstly, the anti-crisis program for 2009-2012 included measures to expand consumer and mortgage lending. Secondly, the state program "Year of the Family," adopted in 2012 has been providing large-scale preferential interest rates of mortgage and consumer loans to young families, loans to support handicrafts and family businesses, as well as micro-loans to small farmers.

Such a rigidly-controlled approach to banking system development is particularly effective in time of crisis since in a pure market economy or in an economy with low government control, market relations between subjects (people) are of a speculative character. It is important to recall the views of Professor Robert Sheller of Yale University, about the imperfection of the market: "In the U.S. we are just beginning discussions on topics of morality and human values, treating them as an integral part of business life. The process is not fast. When I started working at the university, the most common opinion was the idea that the market is perfect, though I did not want to really believe in it then. I looked through all the old books in search of the chapter about speculative "bubbles", but I found nothing in them on this topic. Then I began to look for the chapter about fraud and again, to no avail. If we take modern textbooks, from this point of view, yet something has changed." The legendary George Soros is of the same opinion, who at the World Economic Forum in Davos said that during the crisis, earlier functioning market theory "irreversibly collapsed" [Abaturov 2013].

It is obvious that to build the model of a financial and banking system without considering a permanent aspiration of market participants one way or another, to cheat – is, of course, pure idealism that has nothing to do with the real economic relations.

But on the other hand, limitation just with the government's efforts and the configuration of the banking system as an executive institution will provide a lowly moderate level of the system's development. As a consequence, this leads to a moral hazard in the banking system itself that makes it quite vulnerable and inadequate to market conditions of doing business [Hülsmann 2006]. Despite the fact that the volume of retail lending in Uzbekistan is growing rapidly, total retail loans in relation to GDP are only 2.4% (in 2008 – 2.5%), which is relatively lower than a number of developing countries (Fig. 3).

Consumer loans, which in Uzbekistan comprise also mortgage loans, constitute 6% of the total assets of the banking system. By comparison, in a number of countries in Eastern Europe, despite the slowdown in retail lending, the ratio of consumer loans (excluding mortgages) to the total assets of banks remains relatively high: in Romania – 16%, Hungary and Bulgaria – 11%, Poland – 9%.

It can be concluded that the state initiative of banking sector development is very much needed and brings good results in terms of support for the sector. In other words, state support for the independent development of the banking sector, which must operate according to market rules, is of essential value.
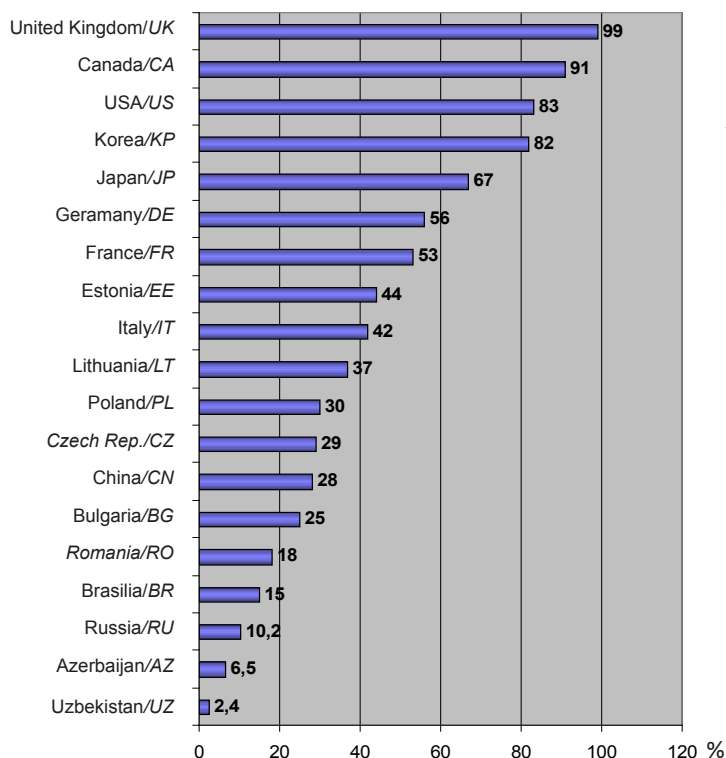
Figure 3. The volume of retail loans in relation to GDP in some countries, on results of 2011
Rysunek 3. Wolumen kredytów detalicznych w relacji do PKB w wybranych krajach, wyniki dla 2011 roku
Source/*Źródło*: [*Finance retail 2013*]

At this stage of banking system development in Uzbekistan it is necessary to increase the circulation of money through the banking system. The more money circulates through banks, the more financial resources will be available to the banks that will affect the volume of lending positively.

By initiative of the head of state a series of measures were adopted to attract idle funds of the population. In particular:

– a "Fund for reconstruction and development" was established, which guarantees a 100 percent refund of deposits belonging to citizens in the case of the insolvency of banks;
– banks will not require information from depositors about the origin of their invested funds and will keep all information about their deposits confidential;
– administrative and, in some cases, criminal liability was established for authorized persons of banks in the case of rejection to return deposits to citizens on their first demand.

As a result of these measures, deposits per capita increased 8 times from 14.5 U.S. dollars in 2005 to 116.8 dollars in 2011. But despite this, the potential of attracting free cash deposits of the population remains enormous. Index thrift industry (the level of deposits per capita) in Uzbekistan is only 5.2. That is only 5.2% of the income of the population are kept in banks in the form of deposits, and this figure should at least be increased to the level of 20-30% which is typical for developing countries [Finance retail 2013].

Interest which is paid by banks on term deposits is quite high in Uzbekistan. It reaches up to 25% a year, while the inflation rate of 7-8% and the interest on business lending is at an average of 13%. Because banks can't effectively use these deposits for lending they are unable to infinitely accept deposits from the public at such high interest rates and return them on the first demand of depositors. Of course, there are lower interest rates (12-18%) at which banks are able to take deposits, but they are less acceptable to the public, because there are more attractive investment options, such as buying a car, real estate, jewellery, the prices of which are rising at a higher rate.

Conclusions

The conducted analysis showed that the development of retail banking services is provided mainly by the government's efforts and a fluctuation in the financial market directly depends on its policy and financial resources. Although the banking system in Uzbekistan has widespread branches over the country, it lacks modern banking facilities such as ATMs which are preferred by developed and emerging countries. Another important issue is that the volume of retail loans in relation to GDP is considerably lower than that of a number of developed and emerging countries. This can be explained as a dependence of banks mainly on state finance rather than public. In other words, the majority of private means and savings are still beyond the banking system. The availability of a considerable state share in the banks' assets leads to moral hazard in the banking system itself, making it quite vulnerable and inadequate to market conditions of doing business. And finally, the fact that remote banking services in Uzbekistan cover less than 1% of the customer base of banks definitely emphasizes the necessity to reconsider the government's policy on the banking system since it aims to catch up with developed countries in upcoming decades.

Development could be achieved by expanding privatization in the banking sector and permitting the sector to function freely according to market rules. This could lead to an increase in the number of private banks and encourage rivalry as well as creative thinking of bank managers. Consequently, modern sophisticated bank facilities would be introduced and the level of moral hazard would be lowered.

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Our main goal – to resolutely pursue the path of large-scale reforms and modernization of the country. 2013: Report by the President of the Republic of Uzbekistan Islam Karimov at the meeting of the Cabinet of Ministers dedicated to the socio-economic development in 2012 and the most important priorities of economic program for 2013. http://www.press-service.uz/ru/news/show/dokladi/doklad_prezidenta_respubliki_uzbekist_1/#.

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Streszczenie

Celem badań było przedstawienie rozwoju detalicznych usług finansowych w warunkach interwencji rządu. Twierdzi się, że nadmierna kontrola stanu rynku detalicznych usług finansowych jest potrzebna w czasach kryzysu, ale nie jest skuteczna w dłuższej perspektywie. Dalszy rozwój można osiągnąć poprzez rozszerzenie prywatyzacji w sektorze bankowym i umożliwiając sektorowi funkcjonować swobodnie według zasad rynkowych.

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