MANAGEMENT OF NON-PERFORMING LOANS (NPLS) IN COMMERCIAL BANKS AND THEIR COMPARATIVE ANALYSIS (BASED ON STATE-OWNED BANKS)

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Abstract: *Non-Performing Loans (NPLs) present significant risks to the stability and profitability of commercial banks, particularly those with substantial state ownership. This study evaluates the effectiveness of NPL management strategies in state-owned banks through a comparative analysis. The findings provide actionable recommendations for enhancing risk management frameworks, offering insights to policymakers, regulators, and banking executives to strengthen financial stability and operational efficiency.*

Keywords: *Non-Performing Loans (NPLs), State-Owned Banks, Risk Management, Comparative Analysis, Banking Sector, Asset Quality, Financial Stability, Loan Recovery, Provision Coverage, Government Ownership, Banking Regulation, Credit Risk Management.*

NPLs represent a major challenge to the stability of financial institutions. As a non-performing asset, it decreases a bank's ability to lend to other borrowers, as funds are tied up in problematic loans. When NPLs are high, banks often face liquidity issues and struggle to maintain the necessary capital adequacy ratios required by regulators. This can result in reduced financial stability within the banking sector and even contribute to broader economic instability if widespread.

Non-performing loans erode the profitability of banks. Banks must allocate a significant portion of their resources to provisioning for loan losses, which directly impacts their profitability. Higher levels of NPLs often mean that a bank has to make larger provisions for potential loan defaults, reducing the funds available for reinvestment, growth, and dividends to shareholders. As a result, the cost of risk management rises, leading to diminished overall returns.

NPLs are a direct indicator of a bank's credit risk management. A high level of NPLs often signals weaknesses in the bank's credit assessment, monitoring systems, and risk management processes. It may indicate poor lending practices, inadequate collateral, or an inability to foresee borrowers' financial difficulties. Managing NPLs effectively is critical for ensuring that banks operate sustainably and avoid systemic risks in the financial system.

On a broader scale, high levels of NPLs can hamper economic growth. Banks with large portfolios of bad loans are less likely to extend new credit to businesses and consumers, which can lead to a credit crunch. This, in turn, stifles business expansion, investment, and consumer spending, creating a negative feedback loop that can deepen a country's economic troubles. Therefore, effective management and resolution of NPLs are critical not only for the health of individual banks but also for the overall economic environment.

NPLs significantly affect a bank's asset quality, which is a key factor considered by investors when assessing a bank's financial health. High NPL ratios can lead to diminished investor confidence, resulting in a decline in the bank's stock price and a reduction in its ability to raise capital. Conversely, banks with low NPL ratios are perceived as having strong asset quality and risk management, which can attract investors and improve their market reputation.

State-owned banks often face unique challenges in managing NPLs due to their structural characteristics and the influence of government policies. Unlike private banks, which generally operate based on profit motives and market forces, state-owned banks are subject to political considerations, government mandates, and economic policies that can influence their lending practices. These institutions may be tasked with supporting national development goals or financing priority sectors, even at the risk of higher loan defaults. Consequently, this can lead to a higher accumulation of NPLs, which requires specific management strategies to ensure the sustainability and solvency of these banks.

In Uzbekistan, state-owned banks play a vital role in the economy, often supporting state-driven initiatives such as financing infrastructure projects, supporting small and medium-sized enterprises (SMEs), and promoting economic development in underserved regions. However, these objectives can sometimes lead to more lenient credit policies and higher exposure to NPLs. As a result, the banks face challenges in managing the increasing levels of NPLs, which can negatively impact their financial health and their ability to support further economic growth.

Uzbekistan's state-owned banks are generally subject to a combination of political and economic pressures that affect their lending strategies. Unlike private banks, which are profit-driven and focused on financial sustainability, state-owned banks must balance economic policy goals with sound risk management practices. The government's involvement in these banks can influence their decisions on loan approvals, terms, and collection practices, which can increase the risk of higher NPL ratios.

In contrast, private banks in Uzbekistan—while also facing some regulatory constraints—tend to focus more on risk management, using more stringent credit assessment tools and early-warning systems to identify potential NPLs. Private banks are generally more responsive to market signals and are quicker to take actions such as restructuring loans or writing off bad debts, which enables them to manage NPLs more effectively.

Information on Non-performing loans of commercial banks as of December 1, 2024					Information on Non-performing loans of commercial banks as of December 1, 2023			Information on Non-performing loans of commercial banks as of December 1, 2022		
				billion UZS			*billion UZS*			*billion UZS*
№	Bank name	Total loan portfolio	NPL	share in % of loans	Total loan portfolio	NPL	share in % of loans	Total loan	NPL	share in % of loans
Banks with State ownership		**363,939**	**14,982**	**4.1%**	**331,070**	**13,750**	**4.2%**	**318,788**	**13,828**	**4.3%**
1	NBU	107,289	3,621	3.4%	96,689	3,423	3.5%	87,730	2,911	3.3%
2	Uzpromstroybank	63,996	1,904	3.0%	56,760	1,499	2.6%	47,776	1,581	3.3%
3	Agrobank	59,641	2,135	3.6%	54,673	1,888	3.5%	41,575	1,688	4.1%
4	Asaka bank	38,206	1,798	4.7%	40,085	1,815	4.5%	36,523	1,600	4.4%
5	People's bank	30,045	1,517	5.0%	24,344	1,960	8.1%	21,451	3,094	14.4%
6	Business development bank	22,696	2,275	10.0%	22,052	1,881	8.5%	20,049	819	4.1%
7	Microcreditbank	17,703	1,066	6.0%	14,439	706	4.9%	12,935	652	5.0%
8	Turon bank	12,501	367	2.9%	11,511	329	2.9%	9,333	349	3.7%
9	Aloqa bank	11,862	299	2.5%	10,442	248	2.4%	8,744	254	2.9%

Table 1 (Information on Non-performing loans of commercial banks)[1]

The analysis of non-performing loans (NPLs) among commercial banks with state ownership in Uzbekistan reveals significant insights over the years 2022, 2023, and 2024. The total loan portfolio has shown a steady increase, reaching 363,939 billion UZS in 2024, up from 318,788 billion UZS in 2022. Despite this growth, the NPL amount has also increased, although the NPL share as a percentage of total loans has slightly decreased from 4.3% in 2022 to 4.1% in 2024. This trend indicates a gradual improvement in loan quality across the banking sector.

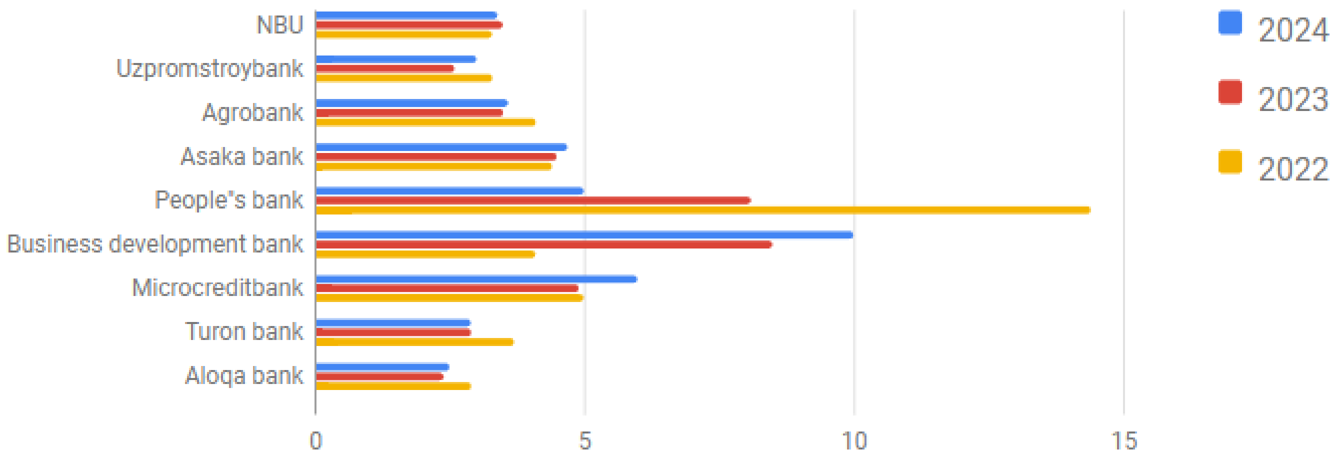

Table 2 (NPL indicators of commercial banks with a state share in December of the last three years (%)

1* https://cbu.uz/en/statistics/bankstats/

To enhance financial health and reduce NPLs, banks should consider implementing several strategies:

Banks must enhance their credit risk assessment processes to identify potential defaults early and take proactive measures. Reducing concentration in high-risk sectors and diversifying lending across various industries can minimize exposure to sector-specific risks.Developing efficient loan recovery strategies, including restructuring loans for borrowers facing temporary financial difficulties, is crucial. Banks with high NPL shares should prioritize improving their loan approval processes and recovery mechanisms. Utilizing advanced analytics and AI tools can help predict and prevent loan defaults, while automating loan monitoring systems can identify potential risks in real time.Strengthening internal controls and increasing transparency in reporting NPLs will build investor and customer confidence.By adopting these strategies, banks can improve their financial health, reduce NPLs, and contribute to the overall stability of the banking sector in Uzbekistan.

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