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FINANCIAL STABILITY OF THE BANKING SECTOR OF KAZAKHSTAN

Today, the banks' financial stability remains one of the most important problems in both scientific and practical aspects.

Various factors play a role in achieving financial stability. The most important of which are the adequacy and quality of equity capital, which also serves as an indicator of financial stability. Based on this, this article examines the relationship of the Bank's equity capital with indicators of financial stability.

Based on the study of previously published literature, the authors show the degree of scientific and theoretical development of the problem by both domestic and foreign scientists. Based on the materials of the Kazakhstan' second-tier banks, was conducted a statistical analysis of the domestic second-tier banks equity capital for 2014-2019. A detailed analysis of the structure, quality and capital adequacy ratios of the banking sector of Kazakhstan for a five-year period was carried out. The article also examines the impact and role of the regulator-the National Bank on the financial stability of the country's banking sector.

Keywords: bank, second-tier banks, banking sector, National bank, financial stability, financial strength, equity, capitalization, modernization of the banking sector, Kazakhstan.

Кілт сөздер: банк, екінші деңгейдегі банктер, банк секторы, Ұлттық банк, қаржылық тұрақтылық, қаржылық орнықтылық, меншікті капитал, капиталдандыру, банк секторын жаңғырту, Қазақстан.

Ключевые слова: банк, банки второго уровня, банковский сектор, Национальный банк, финансовая устойчивость, финансовая стабильность, собственный капитал, докапитализация, модернизация банковского сектора, Казахстан.

Introduction. In Kazakhstan, issues of improving the financial stability of the banking sector are becoming particularly relevant with the development of digital technologies, the growth of legislative regulation, increased competition and the emergence of new market players.

In the recent Address of Kazakhstan's President dated 02.09.2019, it was noted that the insufficient effectiveness of monetary policy is becoming one of the brakes on the country's economic development.

The purpose of the study is to determine the role and significance of equity capital as an indicator of financial stability of second-tier banks. To achieve this goal, it is necessary to solve the following tasks: to study and systematize the theoretical basis of the essence of the Bank's financial stability, to analyze and evaluate the quality of its own capital and the current situation in the banking sector.

Based on the analysis of the literature and the practical situation, the tasks and prospects

of banks are justified in their activities to stabilize the financial condition and improve the quality of their own capital. The authors also conduct an analytical review of the current situation in the banking sector as a whole, the National Bank's activities to improve the financial stability of the banking sector and the results of asset quality assessment.

Research methods – statistical and economic analyses.

Literature review. In the course of the research and in the process of writing the article, the authors studied and investigated previously published publications, such as scientific articles, textbooks, monographs by domestic and foreign authors on the topic of the research. Such literary publications include the textbook «Banking» and scientific publications in periodicals of doctors of economic Sciences, professors Seitkasimov G.S.[1], Musina A.A. [2] and others.

The authors also used the reports and statistical bulletins of the National Bank of Kazakhstan as a basis for the analysis of statistical data. In the field of theory and practice of banking, regulation and supervision, the scientific works of such scientists as: Seitkasimova G.S.[1], Mussina A.A., Kerimkulova D.D.[2], Nikiforov I.[3] and others are known.

However, the causes of vulnerability and the factors of negative shocks and crises influence, as well as new challenges of the time on the stability of the banking sector are not fully studied, which causes the special significance and relevance of the chosen research topic.

Main part. In order to ensure financial stability, organize an effective system of state bodies interaction, as well as conduct a coordinated policy on risk management of financial relations, the Government of the Republic of Kazakhstan, the National Bank and the Agency for regulation and supervision of the financial market and financial organizations signed a Memorandum on financial stability on November 10, 2007.

Financial stability is defined as the absence of distortions in the economy that can lead to a

subsequent negative correction of financial markets, the emergence of a systemic crisis and the inability of financial institutions to ensure the smooth functioning of the financial system, as well as to support the business activity of the real sector of the economy.

Financial stability is ensured by the adequacy of state regulation of current and potential risks, the effectiveness of risk management and redistribution mechanisms, and the preservation of consumer confidence in the financial system [4].

The main principles of ensuring financial stability:

– coordination – a clear definition of the tasks and functions of each party in order to avoid duplication and implement a coordinated approach to the implementation of functions and tasks;

– timeliness – development and improvement of methods for analyzing financial stability indicators that allow timely identification of threats and risks to financial stability in order to make adequate decisions;

– efficiency – development and implementation of a measures' comprehensive system that ensures prompt adoption and effective implementation of decisions that are adequate to threats and risks to financial stability;

– lowest costs – the choice of a method (and tools, mechanism) for solving problems, taking into account the need to minimize financial costs, as well as losses in general for the financial system;

– openness – availability of information about the parties' activities in the field of financial stability in a volume and format that does not contradict the legislation of Kazakhstan and the task of maintaining confidence in the financial system;

– information exchange – submission of all necessary information in compliance with appropriate security measures and confidentiality.

Let's consider the current state of the banking sector in Kazakhstan at the present stage.

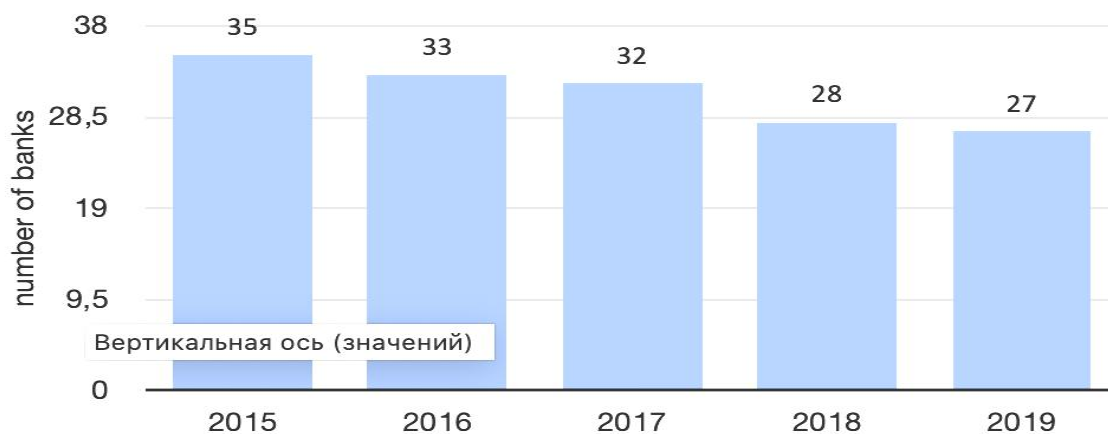


Figure 1. **Number of second-tier banks in Kazakhstan ***

* *Compiled by the author on the basis of statistical data of the National Bank. Data is shown at the end of each year [5]*

As you can see in the above figure 1, at the end of 2015, there were 35 banks operating in our country. Over the analyzed 5 years, their number has decreased by 8 banks and at the end of 2019 is 27 second-tier banks.

Improving the stability of the domestic banking sector is a priority task of the National Bank and in turn, the latter has been conducting a number of important events since 2017, such as: stress testing of second-tier banks, as a result of the financial stability adoption Program of the banking sector, the introduction of a unified methodology for assessing the regulatory provisions.

Today, during the third modernization of Kazakhstan, banks face a priority task-the availability of high-quality and sufficient equity capital.

The Bank's own capital is primarily required for starting the Bank's activities, such as purchasing offices, buildings, equipment, issuing salaries to employees, as well as paying for the Bank's expenses at the next stages of banking operations. The Bank's own capital is

the security and guarantee fund. Thus, equity is an important, necessarily, its role is very large in the structure of Bank funds, ensuring the stability of the Bank and effective operation.

The size of the equity capital of second-tier banks in our country is regulated by law and the increased requirements of the National Bank to the parameters of the equity capital of commercial banks are growing every year. Thus, in 2014, a draft resolution on amendments and additions to prudential regulations was developed, which required an increase in the Bank's equity capital from 10 billion tenge to 30 billion tenge in 2016 and to 100 billion tenge by 2019. However, after foreign economic shocks, the project was postponed and today remains at the level of 10 billion tenge [6].

The equity of a commercial Bank includes primarily authorized capital, reserve capital, undistributed net annual income, and so on.

Consider the structure of equity on the balance sheet of the banking sector in Kazakhstan (figure 2).

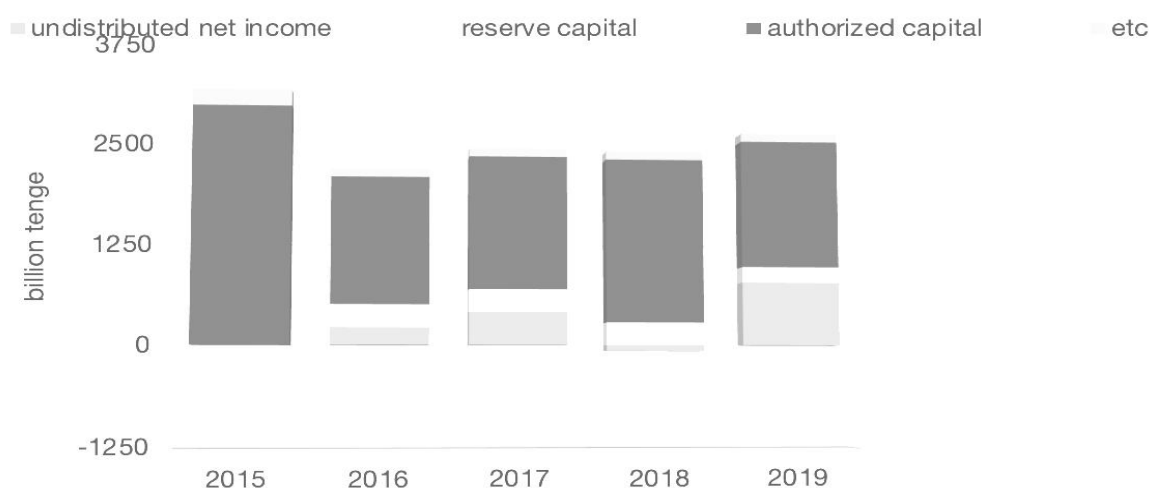


Figure 2. Structure of equity capital of the banking sector of Kazakhstan (by balance sheet) *

* Compiled by the author on the basis of statistical data of the National Bank. Data is shown at the end of each year [5]

As can be seen from figure 2, the main part of the equity capital is the authorized capital, which over the five-year period analyzed has significantly decreased by almost half from 2892.4 billion tenge in 2014 to 1547.3 billion tenge in 2018 (the same minimum level was noted in 2015).

It is also necessary to note the cyclical nature of undistributed net income of the banking sector. For the period up to 2016, there is an annual growth in net income, and in 2017, a record decline to -68.7 billion tenge, and by the end of 2018, a record growth to 764.4 bln tenge due to the growth of retail business.

The Bank's equity capital adequacy is characterized by the following coefficients:

1. capital adequacy ratio k 1-1,
2. tier one capital adequacy ratio k 1-2,
3. adequacy ratio of own capital k2.

The norms of the above coefficients in our country are regulated by law by the National Bank of the Republic of Kazakhstan (in the Resolution «on establishing the normative values and methods of calculating prudential standards and other mandatory norms and

limits of the Bank's capital on a certain date and the Rules for calculating and limits of the Bank's open currency position» dated 13.09.2017).

Analyzing the data in table 1, it can be noted that the regulatory capital of the banking sector of Kazakhstan is growing annually, so from 2502.6 bln tenge at the end of 2014 to 3835.3 bln tenge at the end of 2018.

The capital adequacy ratios k 1-1, first-tier capital k 1-2 and equity capital k2 of the banking sector of Kazakhstan are higher than the minimum regulatory values for the entire analyzed period.

Thus, the requirements of the National Bank are as follows: from January 1, 2015 to January 1, 2017, the main capital adequacy (k1) increased from 5 to 5.5%, the first level capital (k1-2) – from 6 to 6.5%, the equity capital adequacy (k2) – from 7.5 to 8%. Taking into account the buffer capital, we need to add another 2 p. p. to all the listed figures. The requirements for a backbone bank are even higher: the current coefficients k1 – 9.5%; k1-2- 10.5%; k2-12%.

Equity capital adequacy of the Kazakhstan banking sector *

Name	2014	2015	2016	2017	2018	Name	2014	2015	2016	2017
	bln tenge	%	bln tenge	%	bln tenge	%	bln tenge	%	bln tenge	%
First-level capital, including:	1865,6	77	2468,5	82,5	2819,6	85,7	3088	81,7	2934,6	76,5
Fixed capital			2353,2	78,7	2703,9	82,2	2991,7	79,2	2894,4	75,5
Additional capital			115,3	3,8	115,7	3,5	96,3	2,5	40,2	1
Second-level capital	637	23	521,9	17,5	470	14,5	691,5	18,28	900,7	23,49
Total estimated equity	2502,6	100	2990,4	100	3289,6	100	3779,5	100	3835,3	100
k 1-1	10	12,8	13,5	17,2	16,6					
k 1-2	12,1	13,5	14,1	17,7	16,9					
k2	16,3	16,3	16,4	21,7	22					

* The table is compiled by the author based on statistical data of the National Bank.
Data is shown at the end of each year [5]

In order to increase the level of banks capitalization and their ability to cover losses on credit risk, a Program to improve the stability of the banking sector was launched in 2017. At the same time, additional capitalization by shareholders, including banks participating in the Program, is a key factor in the sustainable development of banks.

Postponing the recognition of losses on the loan portfolio to future periods leads to the acceptance of risks that do not correspond to the actual level of capital. As a result, a Bank without capital poses a risk of losing value to minority investors, Bank guarantors, and the public sector [5].

Stress testing conducted by the National Bank in 2017 on the basis of the methodology for assessing the probability default of an individual loan showed that the actual level of impaired assets significantly exceeds the values reflected in the actual statements of banks,

which requires further implementation of a set works to clean up banks' balance sheets.

Non-recognition of problem loans and accrual of interest income on loans that do not actually generate cash flows reduce the quality of profit and stability of the Bank as a whole, as well as overestimate the profitability and capital adequacy indicators.

Based on the results of the work carried out to assess the potential shortage of banks' provisions and in order to further consistently improve the banks' health, the National Bank adopted a Program to improve the financial stability of the banking sector, aimed at providing financial support to banks with significant social significance, with the mandatory joint participation of shareholders. The program has improved the stability of the banking sector and expanded the potential for lending to the economy [6].

In 2017, the National Bank introduced a

unified methodology for assessing regulatory provisions, which provides for adjusting the Bank's equity by reducing it by the difference between the calculated regulatory provisions and the provisions formed by banks under IFRS.

The introduction of the new methodology actually provides the National Bank with a basis for recognizing losses on the loan portfolio and using the quality assessment of the loan portfolio on an ongoing basis as part of the Supervisory process. This requires significant additional capital injections from Bank shareholders.

As a result of regulatory deductions, equity indicators will more objectively reflect the real state of the Bank and improve the quality of regulatory reporting. The introduction of regulatory provisions to adjust equity capital will significantly reduce the capital adequacy indicators of commercial banks. Therefore, in order to reduce the burden on banks' capital as a result of simultaneous recognition of losses, the deduction from capital will be implemented in stages until 2022.

Financial support, totaling 654 bln tenge, is provided to banks on the terms of subordinated debt that meets the criteria for inclusion in the Bank's regulatory capital. In particular, the Program operator, represented by a subsidiary of the National Bank – Kazakhstan stability Fund, repurchased the Bank's subordinated bonds with a maturity of 15 years. The terms of issue subordinated debt provide for the conversion of subordinated debt to common shares of the Bank in the event of a violation the Bank's equity ratios or the discovery of the facts asset withdrawal. At the same time, before converting subordinated bonds, banks will have to recognize all losses in order to prevent dilution of the state's share. The funds received under the Program are used for the purchase of state securities, which, if necessary, banks can gradually sell or use as collateral for REPO operations.

As a result of the adoption of the Program, the total equity and stability of the banking sector increased. This, in turn, will contribute to expanding the lending capacity of the coun-

try's economy, as well as further development of related the economy sectors and improving the financial condition of the final borrowers-enterprises in the real economy sector.

This Program was attended only by large banks that depend on the activity and state of the financial system of Kazakhstan as a whole, such as the system-forming Kazkommertsbank and Halyk Bank, as well as socially significant banks.

Thus, within the framework of the above-mentioned Program, in 2017, after the purchase by Halyk Bank, Kazkommertsbank was cleared of problems that it experienced after joining BTA Bank. This saved the savings of the population, financial resources of public and private organizations in the amount of 4 trillion tenge.

It also provided support to five large socially significant banks, whose assets account for about 30% of the assets the entire banking sector. These include: RBK Bank (bought out by Kazakhmys LLP), Tsesnabank JSC (bought out by First Heartland Bank JSC), Bank Center-Credit, Eurasian Bank and ATF Bank.

Now the Bank of banks – the National Bank faces the task of increasing the financial stability of the banking sector and, as a result, the confidence of the population, international organizations, investors and rating agencies in domestic banks. In this regard, the national Bank is working to implement the Basel III standards in 2021 [6].

To date, a huge amount of work has been done to assess and analyze the quality of assets of commercial banks in the first years in our country.

According to the results of the asset quality assessment, as of 01.04.2019, there is no capital deficit at the consolidated level (aggregation of results of all participating banks); the prudential standards k1 and k2 are implemented at the system level, taking into account the results of the asset quality assessment program:

– At the consolidated level, the excess of k1 capital relative to the regulatory minimum is ~70%, taking into account the additional level of asset quality adjustments received

during the QA and from the revaluation of financial instruments (compared to ~105% before the QA).

– Similarly, according to the results of the QA, the reserve of prudential capital k2 is sufficient at the system level to fully cover risks from a prudential point of view (for example, in terms of evaluating collective reserve models, evaluating real estate, and applying conservative credit impairment triggers) [7].

As part of the audit, positive aspects of the development of business processes and risk management systems in banks in recent years were identified in a number of aspects, including the following:

– Banks in general have successfully passed the complex transition to the IFRS 9 standard, including the development of new approaches to the classification of financial assets, new approaches to the calculation of provisions and the book value of assets that correspond to the new, more complex, standard;

– Significant progress is also seen in the development of Bank data and systems, increasing available historical statistics, and detailing available data;

– In general, there is a high level of derivative correctness estimates financial instruments and bonds on banks' balance sheets, and we

also see that banks do not assume significant risks in these areas;

– A number of banks have used fairly accurate estimates of the value of collateral, and within the framework of the QA, this property was valued even higher than the estimates that the Bank uses for calculating provisions;

– Banks have tightened their lending criteria over the past few years, which has significantly reduced the scale of problems associated with this line of business [8].

Conclusions. In the course of the analysis of the availability of the Kazakhstan's banking sector equity capital, we can conclude that today the domestic banking sector continues to eliminate the consequences of the past global crisis in 2008 and economic shocks in 2013.

Weak banks lose their positions and disappear from the domestic market. The regulatory body of the National Bank has implemented a number of particularly significant and positive measures to improve the banking sector. In this way, support was provided to the backbone Bank and five major socially significant banks, as a result of the adoption in 2017 of the financial stability improvement Program, which in terms of Bank recapitalization completed its work in February 2018 and The assessment of the asset quality of second-tier banks.

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ҚАЗАҚСТАННЫҢ БАНК СЕКТОРЫНЫҢ ҚАРЖЫЛЫҚ ТҰРАҚТЫЛЫҒЫ

Андатпа

Бүгінгі таңда банктердің қаржылық тұрақтылығы ғылыми-теориялық және практикалық аспектіде маңызды проблемалардың бірі болып қалып отыр.

Қаржылық тұрақтылыққа қол жеткізуде түрлі факторлар роль атқарады. Олардың ішінде меншікті капиталдың жеткіліктілігі мен сапасы маңызды болып табылады, бұл сондай-ақ қаржылық тұрақтылық индикаторы. Осыны негізге ала отырып, осы мақалада банктің меншікті капиталының қаржылық тұрақтылық көрсеткіштерімен өзара байланысы қарастырылған.

Бұрын шығарылған әдебиеттерді зерттеу негізінде авторлар отандық және шетелдік ғалымдар проблеманың ғылыми-теориялық әзірлену дәрежесін көрсетеді. Қазақстан Республикасының екінші деңгейдегі банктерінің материалдарында 2014-2019 жылдардағы отандық екінші деңгейдегі банктердің меншікті капиталына статистикалық талдауы жүргізілді. Қазақстанның банк секторының құрылымын, сапасы және бес жылдық кезеңде Қазақстанның банк секторының меншікті капиталының жеткіліктілік коэффициенттері есептелген. Мақалада сондай-ақ реттеуші – Ұлттық банктің банк секторының қаржылық тұрақтылығына әсері мен ролі қарастырылады.

Әдебиетті талдау және практикалық жағдай негізінде банктердің қаржылық жағдайын тұрақтандыру мен меншікті капиталдың сапасын арттыру жөніндегі қызметінің міндеттері мен

перспективалары негізделді. Авторлар тұтастай алғанда банк секторындағы ағымдағы жағдайға, банк секторының қаржылық тұрақтылығын арттыру жөніндегі Ұлттық банктің қызметіне және активтердің сапасын бағалау нәтижелеріне талдау жасады.

Д.Д. Керимкулова, Г.Б. Алина, М.Т. Жоламанова

ФИНАНСОВАЯ УСТОЙЧИВОСТЬ БАНКОВСКОГО СЕКТОРА КАЗАХСТАНА

Аннотация

На сегодняшний день финансовая устойчивость банков остается одной из важных проблем как в научно-теоретическом так и практическом аспекте.

В достижении финансовой устойчивости играют роль различные факторы. Важными из которых являются достаточность и качество ссудного портфеля, что также служит индикатором финансовой устойчивости. Исходя из этого в данной статье рассмотрена взаимосвязь собственного капитала банка с показателями финансовой устойчивости.

На основании изучения ранее изданной литературы авторы показывают степень научно-теоретической разработанности проблемы как отечественными, так и зарубежными учеными. На материалах банков второго уровня Республики Казахстан проведен статистический анализ собственного капитала отечественных банков второго уровня за 2014-2019 годы. Проведены детальный анализ структуры, качества и рассчитаны коэффициенты достаточности собственного капитала банковского сектора Казахстана за пятилетний период. В статье также рассматривается влияние и роль регулятора – Национального банка на финансовую стабильность банковского сектора страны.

На основе анализа литературы и практической ситуации обосновываются задачи и перспективы деятельности банков по стабилизации финансового состояния и повышению качества собственного капитала. Авторы также проводят аналитический обзор текущей ситуации в банковском секторе в целом, деятельности Национального банка по повышению финансовой устойчивости банковского сектора и результатов оценки качества активов.

