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Bankruptcy of Securities Begins With the Implementation of Additional Issuance Operations in Developing Countries

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Abstract: This study investigates the underdeveloped state of emission operations with securities by commercial banks in Uzbekistan, with a pronounced reliance on deposits and foreign loans, unlike the practices implemented in the developed economies. The global upward trend in securities based resource mobilization has made little headway with Uzbek banks due to a critical knowledge gap in adapting global strategies to local realities. The research tests financial reports with a mixed methods approach and uses portfolio theory to perform risk and return analysis. However, compared to substantially higher figures in developed nations, banks in Uzbekistan show security based liabilities amounting to no more than 2.4% of the liabilities of the banks. The evidence shows that strategic improvements in securities management, including active and passive portfolio strategies, can improve liquidity, profitability, and financial stability. Apart from the regulatory and technical implications for the banking sector in Uzbekistan, there are implications for the policymakers and the banking practice which have advocated that the banking practices of Uzbekistan be reformed into international banking standards and to develop a robust and diversified financial ecosystem.

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1. Introduction

The strategy for reforming the banking system of the Republic of Uzbekistan for 2020-2025 aims to reduce the dependence of banks on state resources, improve management in corporate commercial banks, and reduce the state's share in the banking system through the comprehensive transformation of state-owned banks and state enterprises. It also emphasizes the implementation of technological solutions for risk assessment as priority directions for the country's banking system reform. This necessitates strengthening the resource base of commercial banks by developing emission operations with securities.

However, at present, the level of development of emission operations with securities by commercial banks in our republic is low. As of January 1, 2024, the share of funds raised from the sale of bank securities in the total liabilities of commercial banks in the republic was only 2.4%. Meanwhile, in developed countries, the operations of commercial banks with securities are well-developed, and the funds raised from the sale of bank securities

constitute a significant portion of total liabilities. For example, as of January 1, 2024, the share of funds raised from the sale of bank securities in the total liabilities of Germany's Deutsche Bank was 29.6%, and in the Bank of America in the USA, it was 14.6%.

Literature Review:

Based on his research, F. Mishkin concludes that "government guarantees for bank deposits and other liabilities do not apply to corporate securities, and capital serves as an important security for them. However, because common shares are a relatively expensive form of financing bank operations, banks, in order to reduce costs, try to use more debt instruments" [5].

According to E. Meshkova's conclusion, "commercial banks issue shares, bonds, mortgage bonds, deposit certificates, and savings certificates to form their resource base. A part of the funds raised from the sale of these securities is reflected in the bank's regulatory capital, while the other part is reflected in the liabilities. The market price of the shares and certificates is an economic indicator that evaluates the bank's activity in this market" [6].

In the practice of developed countries, the investment attractiveness of corporate securities, including commercial bank securities, is widely assessed using H. Markowitz's Portfolio Theory. According to H. Markowitz's Portfolio Theory:

- The future profitability and risk for each stock are determined based on analyzing the actual quotes of the securities;
- Securities with relatively higher profitability and lower risk are selected for the portfolio;
- Portfolio optimization is carried out based on the principle of achieving good profitability and minimal risk under acceptable conditions;
- The future profitability is a random quantity, and its exact value is unknown [7].

According to M. Chekulaev's opinion, the value of the raised funds, i.e., the interest rates paid on them, has a positive impact on the premium of "call" options. However, the effect of this factor must be considered as limited, meaning that even a small share of an option position in the portfolio can alter the interest rate levels [8].

According to B. Berdiyarov, "To ensure the payment capacity of banks at the second level of the banking system, the weight of regulatory capital in the volume of liabilities should be maintained, and optimal profitability in relation to assets can be ensured through the balance of the growth rate of net profit and the growth rate of total assets" [9].

V. Aksenov concludes that the key characteristics of an active strategy for managing a securities portfolio include:

- Selecting securities necessary for portfolio formation;
- Determining the timing of the purchase or sale of financial assets [10].

In Western countries' banking practices, the following four types of swap-based securities portfolio management strategies are widely used [11]:

1. Selecting a fixed income strategy: In this strategy, two securities with similar nominal values but different ratings are exchanged. As a result, a security with lower profitability is sold, and one with relatively higher profitability is bought.

2. Swap replacement strategy: In this strategy, two similar but not identical securities are exchanged. It is used to gain additional income.

3. Sector swap strategy: This is the most complex form of swapping. Here, an investor exchanges securities issued by entities from different sectors of the economy, considering their maturity and profitability.

4. Interest rate analysis and forecast-based strategy: In this strategy, when interest rates are falling, the maturity of the securities portfolio is extended, and when interest rates are rising, the portfolio's maturity is shortened.

2. Materials and Methods

This research employs a holistic analytical framework based on Uzbekistan's commercial banks with securities, where the methodology was developed to integrate the emission operations. Secondary data from financial reports and national regulations are used by the study to undertake a comparative analysis of the practices observed in Uzbekistan, compared to that of developed economies like Germany and the United States. It finds key trends, challenges and opportunities that impact on emission operations and banking system stability. 1. Patterns and correlations that contribute to operational effectiveness of securities are discerned by analyzing quantitative data – including profitability rates and liability compositions. Regulatory Frameworks are evaluated by a qualitative approach which brings down into practice the extent of alignment with the current International Standards. An input also to this work is getting insights from existing theoretical constructs, such as Markowitz's Portfolio Theory, to understand the aspect of risk and return optimization in the securities realm. Further practical strategies, including passive and active securities management, are studied from the point of view of their applicability to local banks. This methodology is intended to propose resource base enhancement in commercial banks through the development of emission operations, measure of liquidity, financial stability, and based on specific economics and regulations of Uzbekistan.

3. Results

In this section, we will examine and summarize the advanced foreign experience in developing emission operations with securities by commercial banks, using the example of transnational banks from developed countries.

Table 1

The profitability rates of loans and investments in securities at Deutsche Bank, in percentage. [12]

Indicators	2019	2020	2021	2022	2023
Profitability of loans	3,20	2,68	2,22	2,91	5,49
Profitability of investments in securities	0,96	0,16	0,15	0,25	2,32

From the data in Table 1.4, it can be seen that the profitability of Deutsche Bank's loans showed a declining trend in 2019-2021. This can be explained by the decrease in interest rates on loans during this period. In 2023, the profitability of Deutsche Bank's loans increased at a higher rate (2.29 percentage points) compared to 2019. This is considered a positive development in terms of strengthening the bank's income base.

The profitability of investments in securities by Deutsche Bank showed an upward trend from 2021 to 2023. This is also seen as a positive development in terms of strengthening the bank's income base.

According to the revised Law on the Central Bank of the Republic of Uzbekistan, ensuring the stability of the country's banking system is one of the main objectives of the Central Bank's activities. The Central Bank applies mandatory reserve requirements to commercial banks, and these reserves are maintained by transferring funds to special accounts at the Central Bank and/or maintaining the average reserve amount calculated

from the reserve coefficient on representative accounts opened at the Central Bank. The Central Bank regulates and supervises the activities of credit institutions, including the operations of commercial banks. As part of its supervisory function, the Central Bank is authorized to set the conditions and procedures for writing off non-performing assets, to require banks and main banks of banking groups to develop and submit recovery plans aimed at restoring their financial position in case of deterioration, and to request and obtain information regarding the financial condition and business reputation of direct and indirect shareholders of commercial banks, including ultimate beneficial owners.

According to the regulation approved by the decision of the Board of the Central Bank of the Republic of Uzbekistan and the Center for Coordinating and Supervising the Activities of the Securities Market under the State Property Committee of the Republic of Uzbekistan, titled "On the Approval of the Regulations on the Requirements for Professional Activities in the Securities Market as an Investment Intermediary, Investment Asset Manager, and Investment Consultant," the following provisions apply:

When performing professional activities as an investment intermediary in the securities market, the bank must keep records of each client's securities and cash funds, carry out transactions and operations related to securities in accordance with agreements made with the client, and provide reports on the transactions and operations carried out.

There must be a structural division in the bank responsible for operations related to professional activities as an investment intermediary, investment asset manager, and investment consultant.

Banks must comply with the requirements for registering over-the-counter (OTC) transactions in the securities market, maintain a register of such transactions, and provide information on registered transactions to the authorized state body regulating the securities market in accordance with the law.

Branches of banks operating as investment intermediaries, investment asset managers, and investment consultants in the securities market in the regions of the republic must submit information on securities market regulation to the relevant regional departments of the authorized state body in accordance with the law.

The monitoring and regulation of professional activities of banks as investment intermediaries, investment asset managers, and investment consultants in the securities market will be carried out by the Central Bank of the Republic of Uzbekistan together with the authorized state body responsible for regulating the securities market.

During the analysis, the main focus will be on identifying existing trends and problems and forming scientific and practical conclusions.

Table 2

Composition of the liabilities of commercial banks in the Republic of Uzbekistan, as a percentage of the total [15]

Analysis:

Liability Composition	2018	2019	2020	2021	2022
Deposits	37,3	41,1	37,3	41,8	45,4
Central Bank representative account	0,27	0,8	0,4	0,2	0,2
Other banks' funds-residents	3,4	4,5	4,2	3,6	3,9
Other banks' funds-non-residents	0,3	0,4	1,0	1,2	4,8
Borrowed loans and leasing	55,6	47,5	49,3	46,5	39,1
Issued securities	0,01	1,3	3,1	2,84	2,3
Subordinated loans	0,0	1,8	1,3	1,1	1,4
Accrued interest payable	1,2	1,1	1,2	1,1	1,1
Other liabilities	2,0	1,7	2,2	1,8	1,8
Total liabilities	100,0	100,0	100,0	100,0	100,0

From the data in Table 2, it is evident that from 2018 to 2022, the largest share of liabilities for commercial banks in Uzbekistan has been occupied by deposits and foreign-sourced international loans and international leasing. This indicates that, firstly, deposits are the primary internal source used to finance the bank's active operations, and secondly, international loans and international leasing are widely used to finance investments in the country's economy.

The proportion of liabilities arising from securities issued by banks showed an increasing trend during 2018-2022. However, this indicator consistently reported low results throughout the entire period, which is seen as a negative situation in terms of ensuring the stability of the bank's liabilities.

From 2019 to 2021, the share of reserve capital in the regulatory capital of commercial banks showed an upward trend. However, in 2022, this indicator decreased significantly compared to 2021. Similarly, during 2018-2022, the share of retained earnings in the regulatory capital of commercial banks showed instability.

One of the key indicators describing the stability of commercial banks' liabilities is the sufficiency of the deposit base.

Table 3

Composition of the liabilities of "Aloqabank" JSCB, as a percentage of the total[16]

Indicators	2018	2019	2020	2021	2022
Deposits	74,6	81,8	75,3	61,9	53,8
Funds received from the sale of bank securities	0,0	0,0	0,0	0,0	0,0
Loans received from other banks	4,8	7,7	13,0	20,7	22,5
Other liabilities	20,6	10,5	11,7	17,4	23,7
Total liabilities	100,0	100,0	100,0	100,0	100,0

Analysis:

From the data presented in Table 3, it is evident that from 2018 to 2022, the largest share of liabilities in "Aloqabank" JSCB was occupied by deposits. Notably, there were no funds derived from the sale of bank securities in the bank's liabilities during 2018-2022. This indicates an unfavorable situation for ensuring the stability of "Aloqabank"'s liabilities.

Over the same period, the share of loans received from other banks in the bank's liabilities showed an increasing trend. This is also considered an undesirable situation for the stability of "Aloqabank"'s liabilities. The growth in interbank loans leads to higher interest expenses, which could impact the overall financial stability of the bank.

4. Conclusion

Developing methods for improving the emission operations of commercial banks with securities can be achieved by addressing the following issues:

1. In international banking practices, both passive and active strategies for managing commercial bank securities portfolios are widely used. The passive strategy involves investing in two types of securities—risk-free government bonds and common stocks. On the other hand, in the active strategy for managing securities portfolios, banks

purchase securities for short-term resale to make a profit, requiring constant adjustments to the composition of the securities portfolio.

2. If non-income-generating assets in the form of cash are placed in loans and liquid securities, it will lead to several positive outcomes. First, the current liquidity level of commercial banks will improve, as the amount of liquid assets and assets to be repaid within the next 30 days will increase. Second, the profitability of assets will rise. Third, the likelihood of encountering an unbalanced liquidity issue will decrease.

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