



CENTRAL BANK
OF THE REPUBLIC OF AZERBAIJAN

CREDIT CONDITIONS SURVEY



2022
Q4



ACRONYMS

MCGF - The Mortgage and Credit Guarantee Fund of the Republic of Azerbaijan

NBCI – Non-Bank Credit Institution

IT – Information Technologies

SME – Small and Medium Enterprises

LTV – Loan to value ratio

MSME – Micro, Small and Medium Enterprises

NPL- Non-performing loans

SL – Salary

RE – Real estate

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Introduction

The purpose of this survey is to monitor and analyze the credit activities of banks, identify and assess threats to financial stability early on, determine the appropriate prudential policy, and inform the financial sector participants about relevant trends. The respondents of the credit conditions survey are banks' senior loan officers or the members of the Management Board responsible for the relevant area. This survey includes an assessment of supply and demand factors with respect to business, consumer and mortgage loans, as well as identification and assessment of banks' risks:

- *Dynamics of changes in credit standards (policy);*
- *Factors affecting the dynamics of credit standards;*
- *Changes in credit terms and conditions;*
- *Dynamics of changes in loan demand;*
- *Factors affecting the dynamics of loan demand;*
- *Changes in risk dynamics.*

The survey contains qualitative questions and does not require quantitative assessment. The balance statistics method is used to convert survey results into quantitative data. The index varies from negative 100% to positive 100%. A positive 100% indicates that 100% of respondents observe a significant softening or an increase in the trend, while a negative 100% indicates that 100% of respondents observe a significant tightening or decline. When the index is 0%, this means that the trend has not changed from the previous quarter. When calculating the index, respondents' answers are equally weighted regardless of the bank's size.

This quarterly survey of banks concerning the conditions of crediting has been conducted since the first quarter of 2022. This report presents the results of the Q4 2022 survey. The expectations included in this report do not reflect the expectations of the Central Bank of the Republic of Azerbaijan, but only the respondents' (banks') views on current and future credit trends.

Overview of results

According to the results of the survey on credit activity for the fourth quarter of 2022, there was an easing of banks' credit policy. Credit policy easing occurred in all segments of the credit portfolio, especially for consumer and business loans. For consumer loans, easing occurred mainly on credit cards and salary-based loans, and for business loans, on loans granted to MSMEs. Banks reported that the credit policy was expected to continue to ease in Q1 2023, especially for consumer and mortgage loans. In the last quarter of 2022, banks mostly relaxed credit standards applicable to loans in national currency and short-term loans, and tightened credit standards on loans in foreign currency. According to the survey results, demand for business loans increased in the last quarter amid the working capital needs, changes in banks' credit conditions and digitalization, while consumer confidence, digitalization and changes in interest rates were the main factors contributing to increased growth in consumer and mortgage loans. Banks reported that level of indebtedness increased because of increased demand from MSMEs.

Business loans

Credit policy: Banks eased credit standards applied to business loans. The easing occurred mostly on loans granted to MSMEs.

Loan demand: In Q4 2022, demand for business loans increased as in the third quarter of that year. Demand increased mainly on the part of MSMEs and on loans in national currency.

Expectations for Q1 2023: Banks forecast an increase in demand for business loans in Q1 2023. At the same time, banks reported that credit standards for business loans were expected to continue to ease, except for loans to large businesses.

Mortgage loans

Credit policy: In Q4 2022, there was a softening of loans provided both internally by banks and by the MCGF.

Loan demand: Demand for mortgage loans increased during the last quarter of 2022. As in Q3 2022, the main driver of demand was an increase in demand for loans granted at the expense of the MCGF.

Expectations for Q1 2023: In Q1 2023, banks expect high demand for MCGF loans and easing of credit policy.

Consumer loans

Credit policy: Softening of consumer loan standards was higher than in other segments. As in Q3 2022, loan approval standards were relaxed in Q4 of that year mainly for credit cards and salary-based loans.

Loan demand: During the last quarter of 2022, growth in demand for consumer loans came mainly from salary-based loans and credit cards amid softening credit policy.

Expectations for Q1 2023: Banks reported expectations of softening in consumer credit standards and increased demand for consumer loans, especially for salary-based loans, in Q1 2023.

Chart 1. Changes in credit standards for Q4 2022*

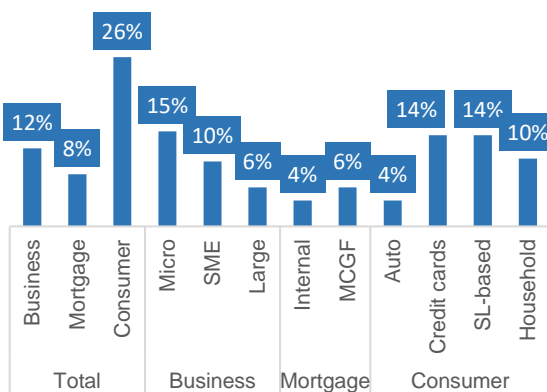


Chart 2. Expectations on credit standards for Q1 2023

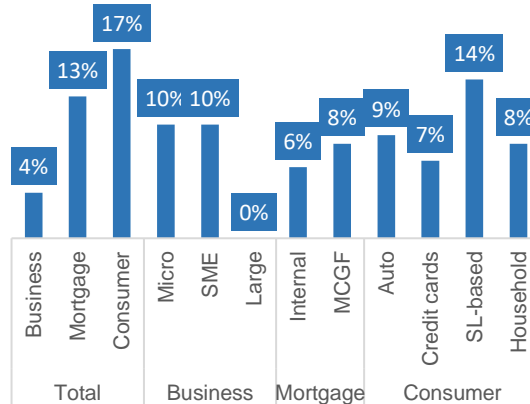


Chart 3. Changes in loan demand for Q4 2022**

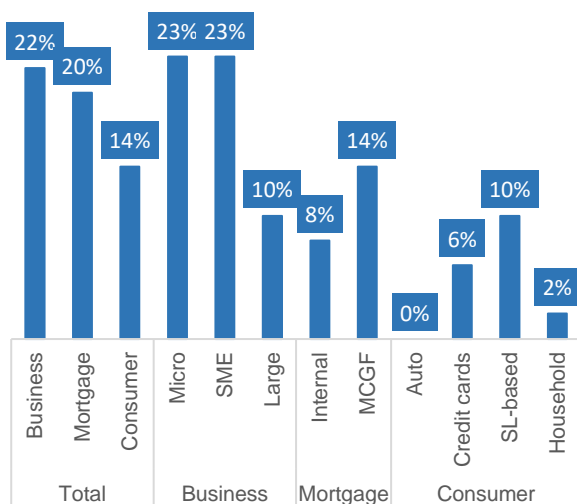
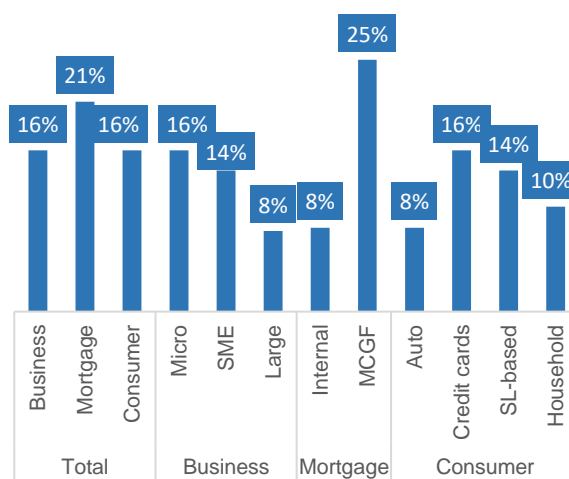


Chart 4. Expectations on loan demand for Q1 2023



*A Diffusion Index varies between [-100,+100]. A positive 100% index means that 100% of respondents reported a significant relaxation of credit standards, while negative 100% means that 100% of respondents reported a significant tightening.

**A Diffusion Index varies between [-100,+100]. A positive 100% index means that 100% of respondents reported a significant increase in loan demand, while negative 100% means that 100% of respondents reported a significant decrease.

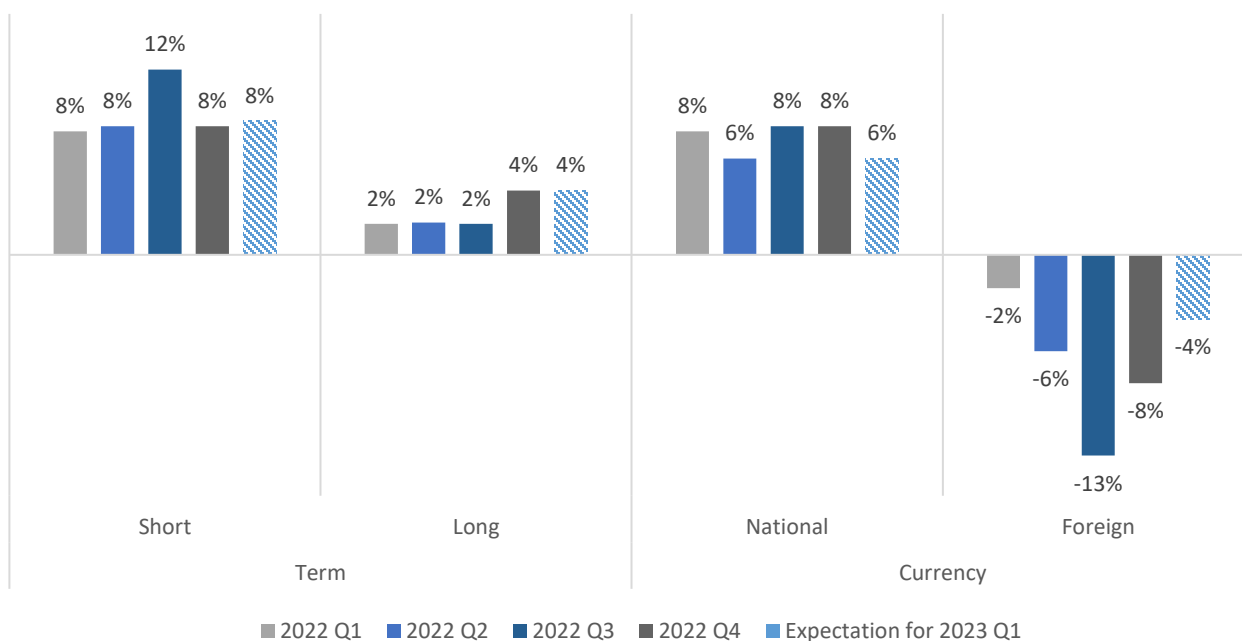
Analysis of loans across sectors

Business loans

Credit policy on business loans. In Q4 2022, banks eased credit standards for business loans. The easing mainly affected short-term business loans and loans in national currency, but it was also observed for credit conditions on long-term loans. According to the survey, although banks tightened their credit policy for loans in foreign currencies, there was less tightening in the fourth quarter than in previous quarter. In general, banks expect credit standards for business loans to continue easing in Q1 2023.

Chart 5. Changes in term and currency standards for business loans

(Diffusion Index: positive = softening, negative = tightening)



Banks' positive expectations with regard to certain economic sectors, as well as increased loan demand had a softening effect on credit standards for business loans, especially on credit standards for SME loans in Q4 2022. According to the survey, inflation and refinancing rate were the main macroeconomic factors that led to the tightening. Banks reported that, unlike previous quarters, general economic expectations had a softening effect on credit standards during Q4 2022. Compared to Q3 2022, the impact of banks' capital and liquidity position on business credit standards was lower.

Chart 6. Factors affecting credit standards for business loans

(Diffusion Index: positive=softening, negative=tightening)

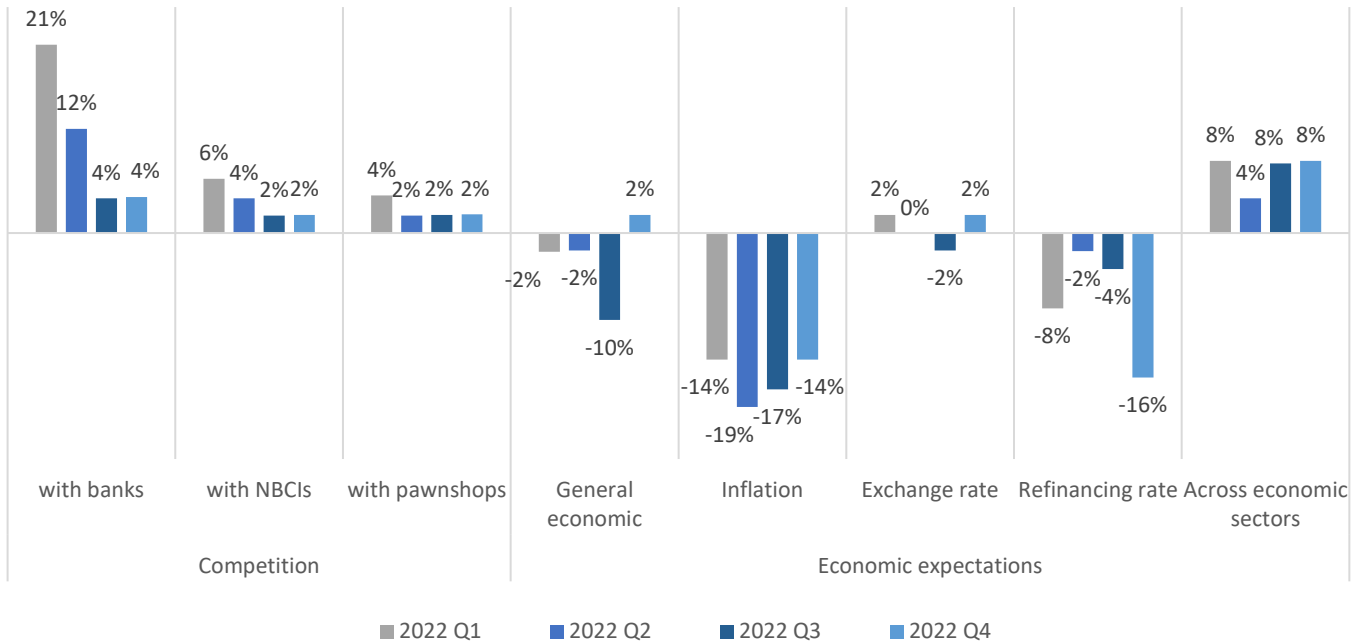


Chart 7. Factors affecting credit standards for business loans

(Diffusion Index: positive=softening, negative=tightening)

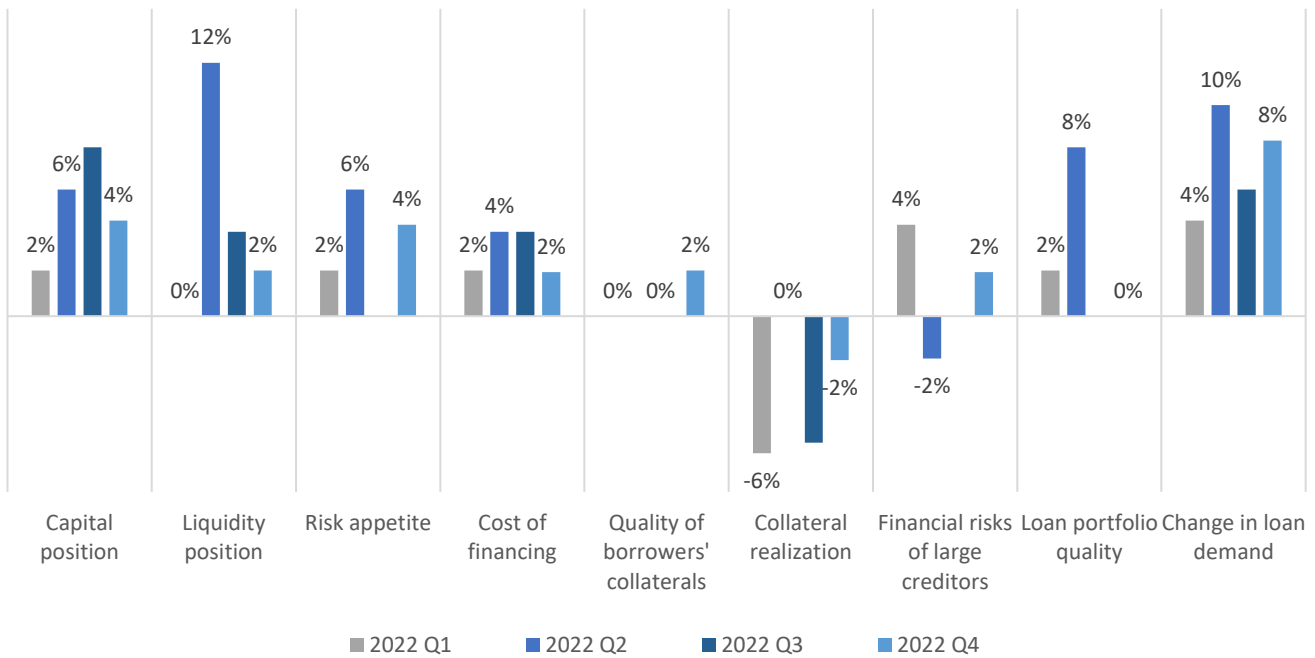


Chart 8. Factors affecting credit standards for loans to SMEs

(Diffusion Index: positive = softening, negative = tightening)

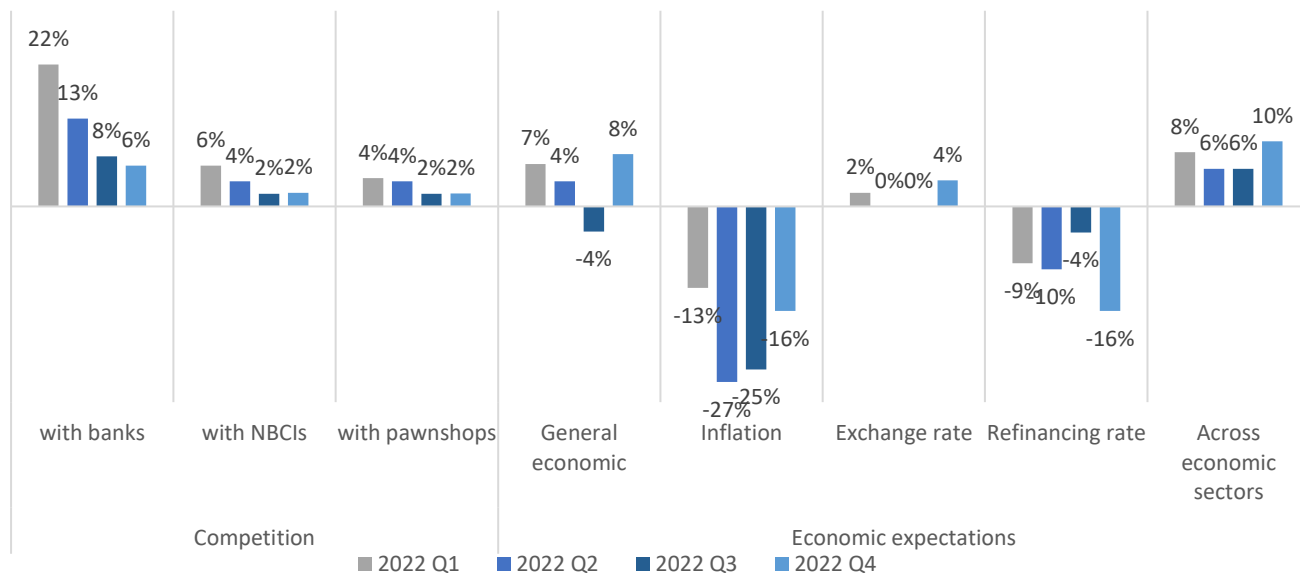
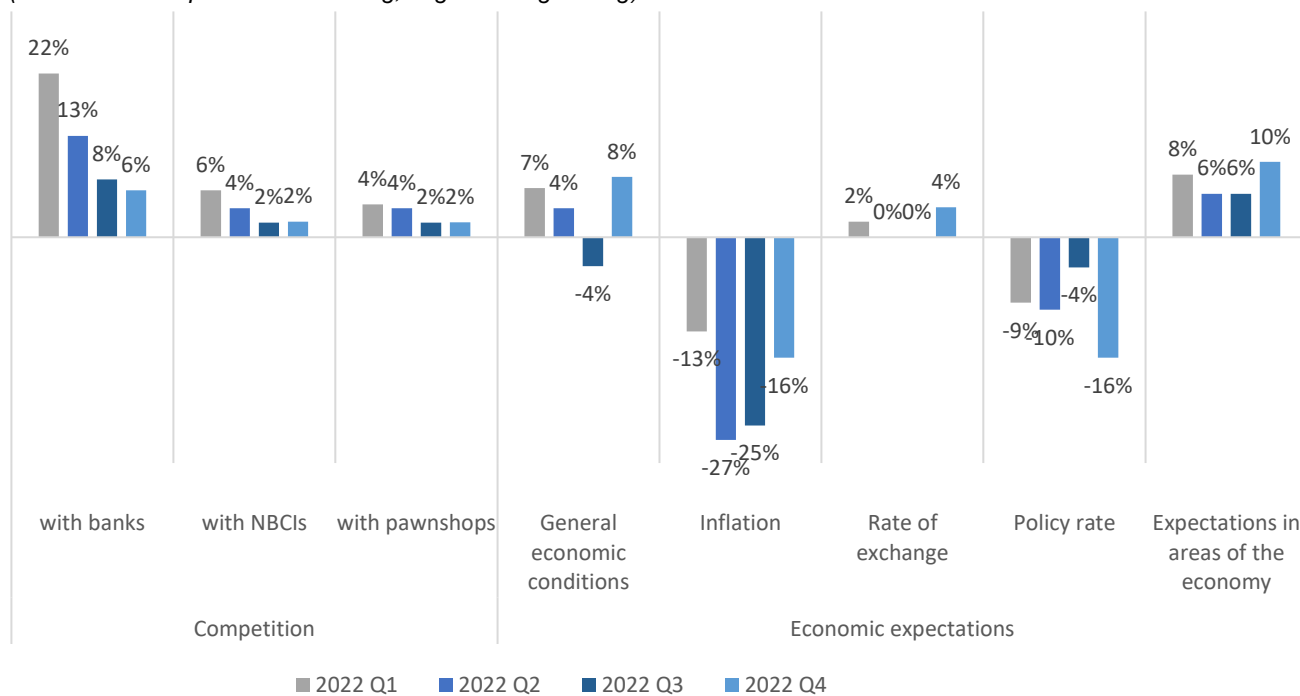


Chart 9. Factors affecting credit standards for loans to SMEs

(Diffusion Index: positive = softening, negative = tightening)



Credit easing for businesses continued in the last quarter of 2022. The tightening of credit conditions was mainly based on restrictive criteria.

Chart 10. Changes in terms and conditions for business loans

(Diffusion Index: positive = softening, negative = tightening)

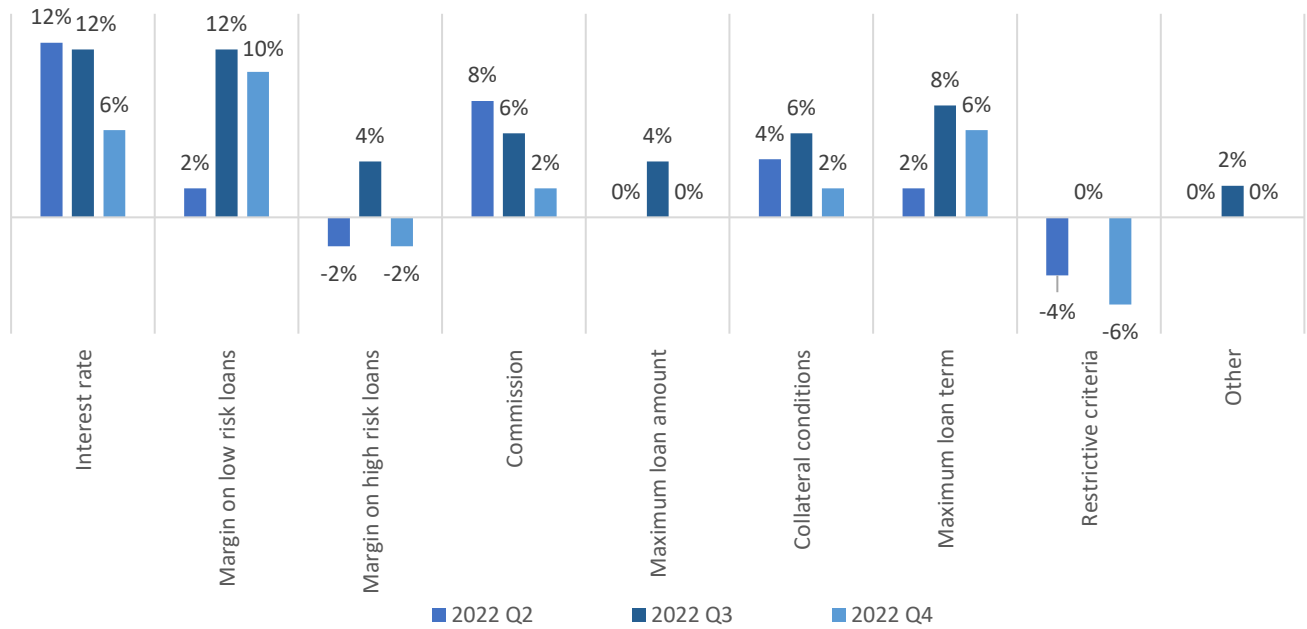


Chart 11. Changes in terms and conditions for loans to SMEs

(Diffusion Index: positive = softening, negative = tightening)

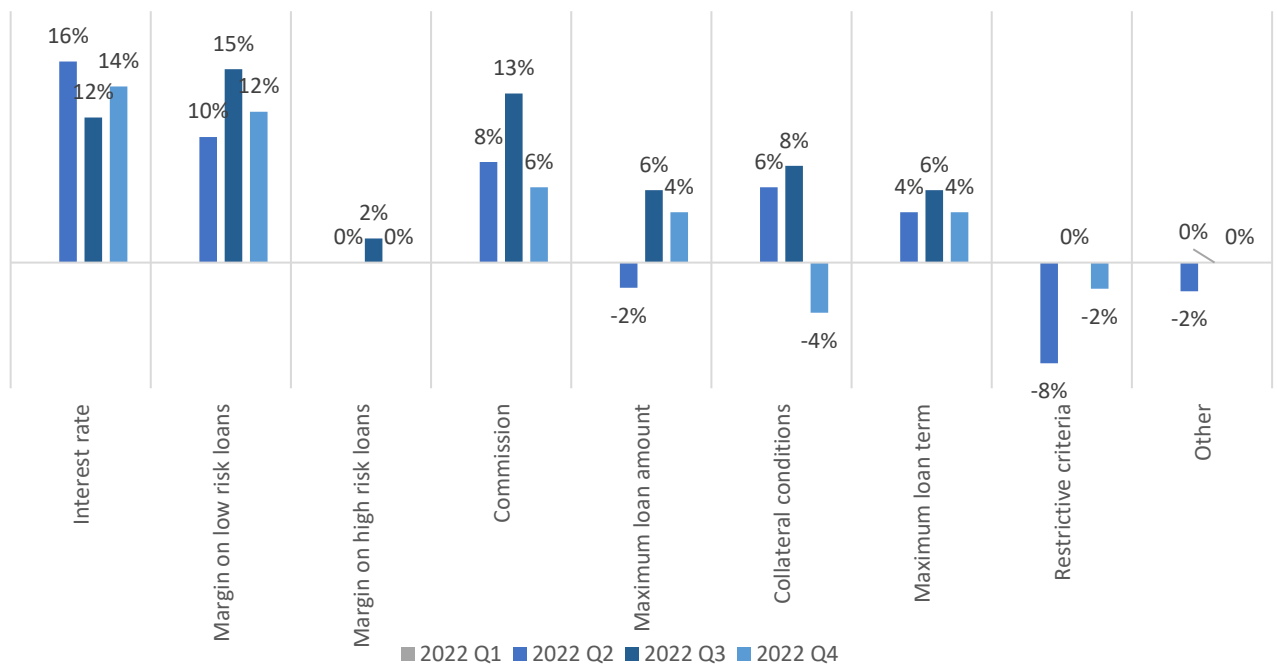


Chart 12. Changes in terms and conditions for loans to large enterprises

(Diffusion Index: positive = softening, negative = tightening)

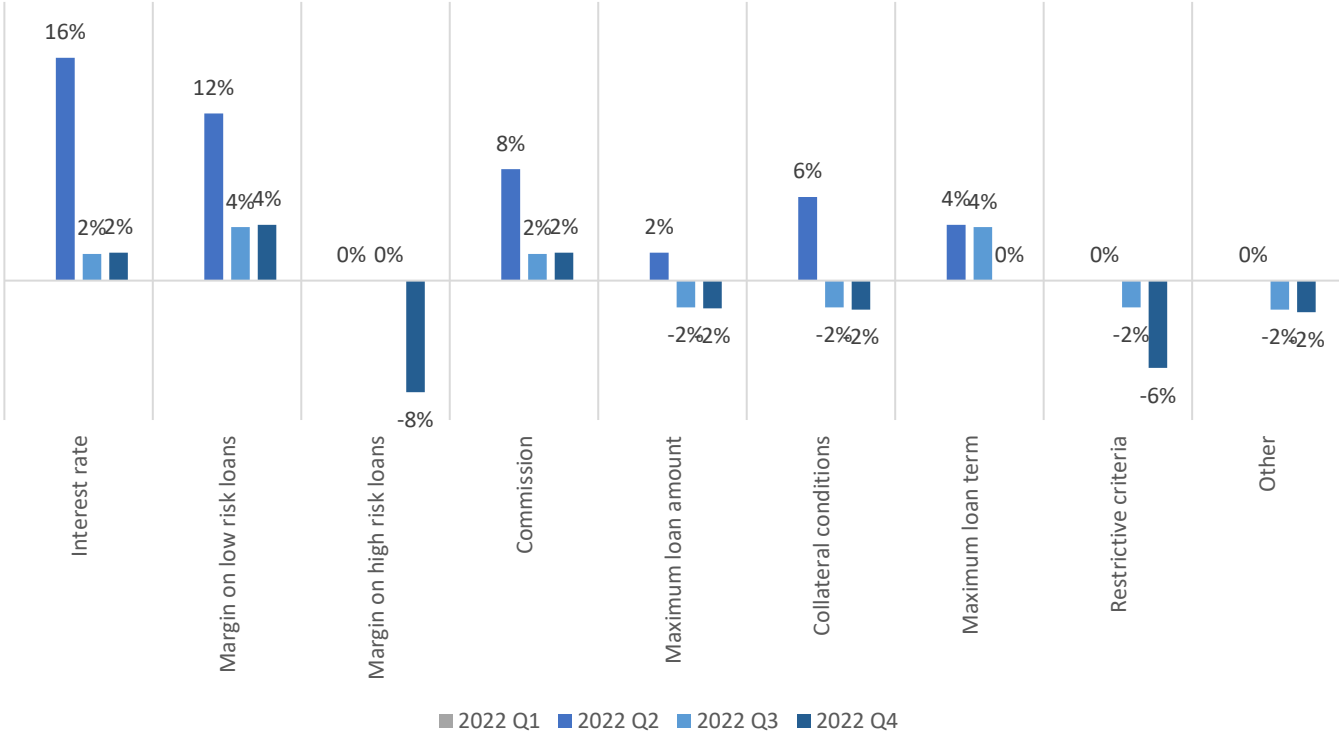
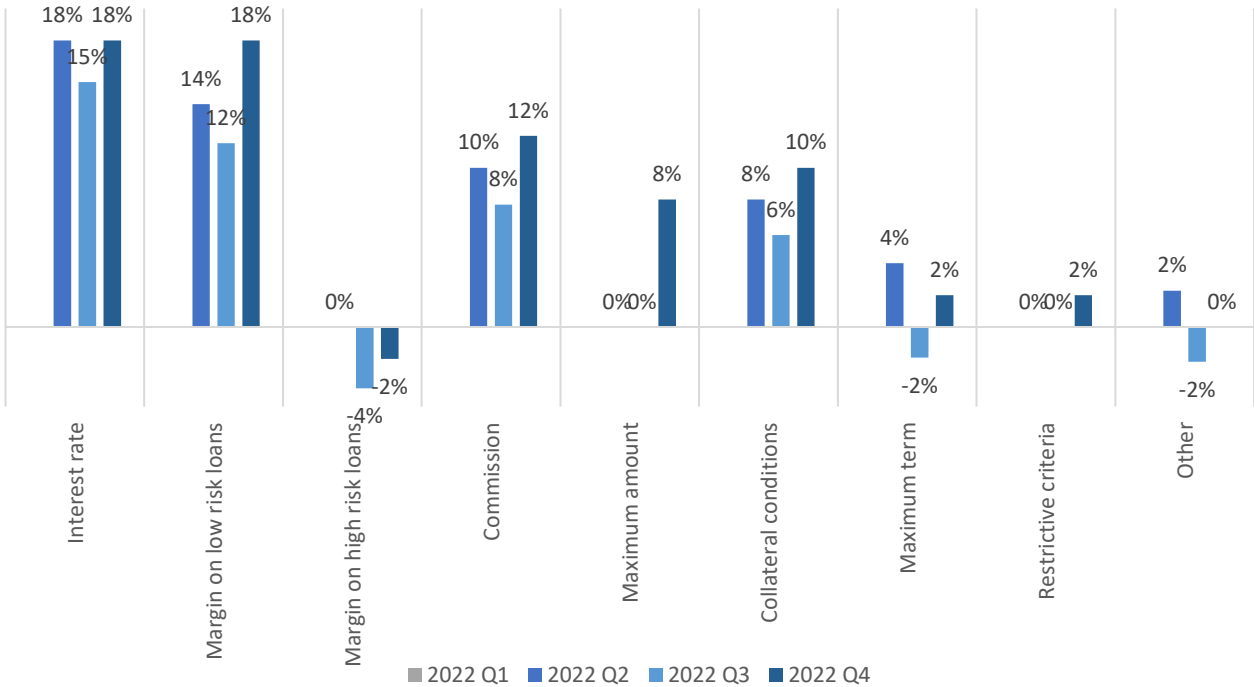


Chart 13. Changes in terms and conditions for loans to micro enterprises

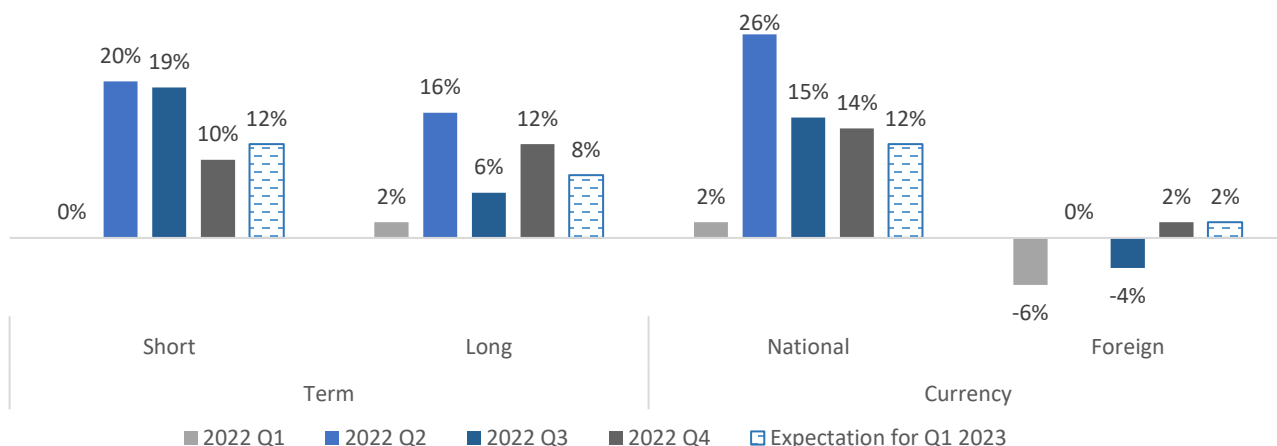
(Diffusion Index: positive = softening, negative = tightening)



Business loan demand. According to the results of the survey, banks reported an increase in demand for short-term and long-term business loans in local currency in the fourth quarter of 2022. Banks expect an increase in demand for business loans in Q1 2023.

Chart 14. Changes in demand for business loans

(Diffusion Index: positive = increase, negative = decrease)



The main factors influencing an increase in demand for business loans and loans to SMEs included interest rates, digitalization and working capital needs. Compared to previous quarters, changes in banks' credit conditions in Q4 2022 were also important factors affecting business lending.

Chart 15. Factors affecting demand for business loans

(Diffusion Index: positive = increase, negative = decrease)

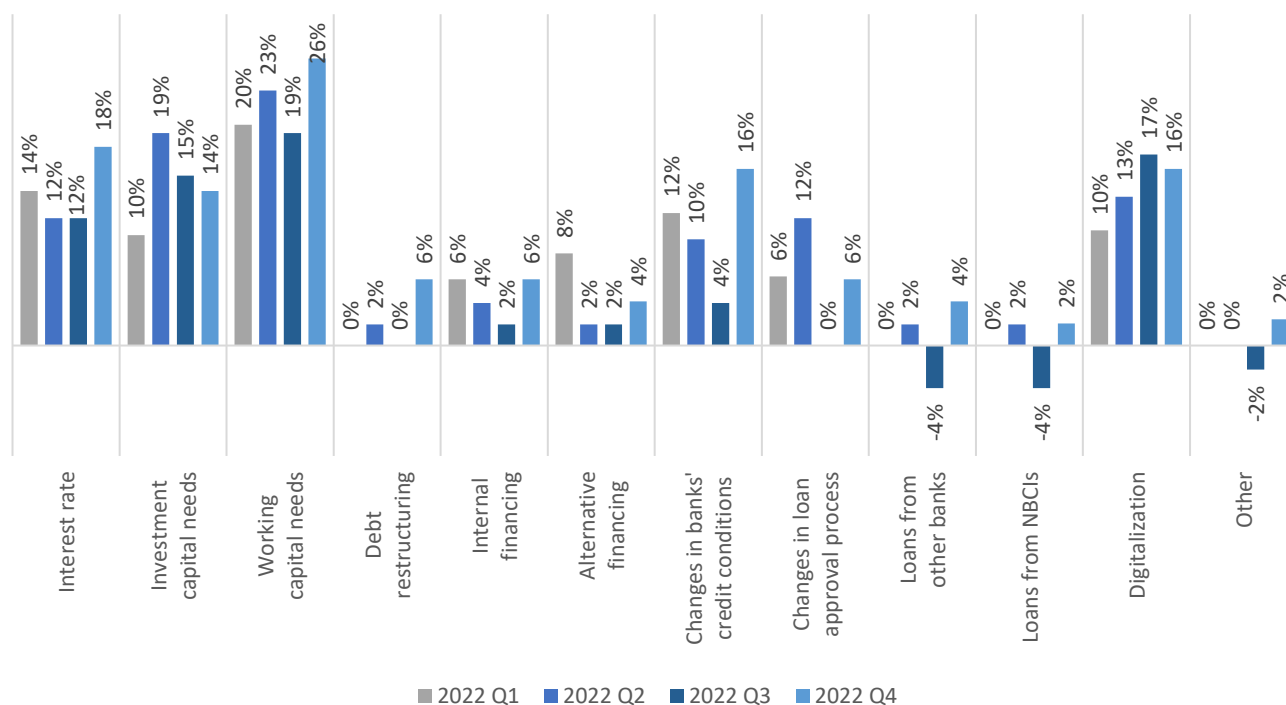
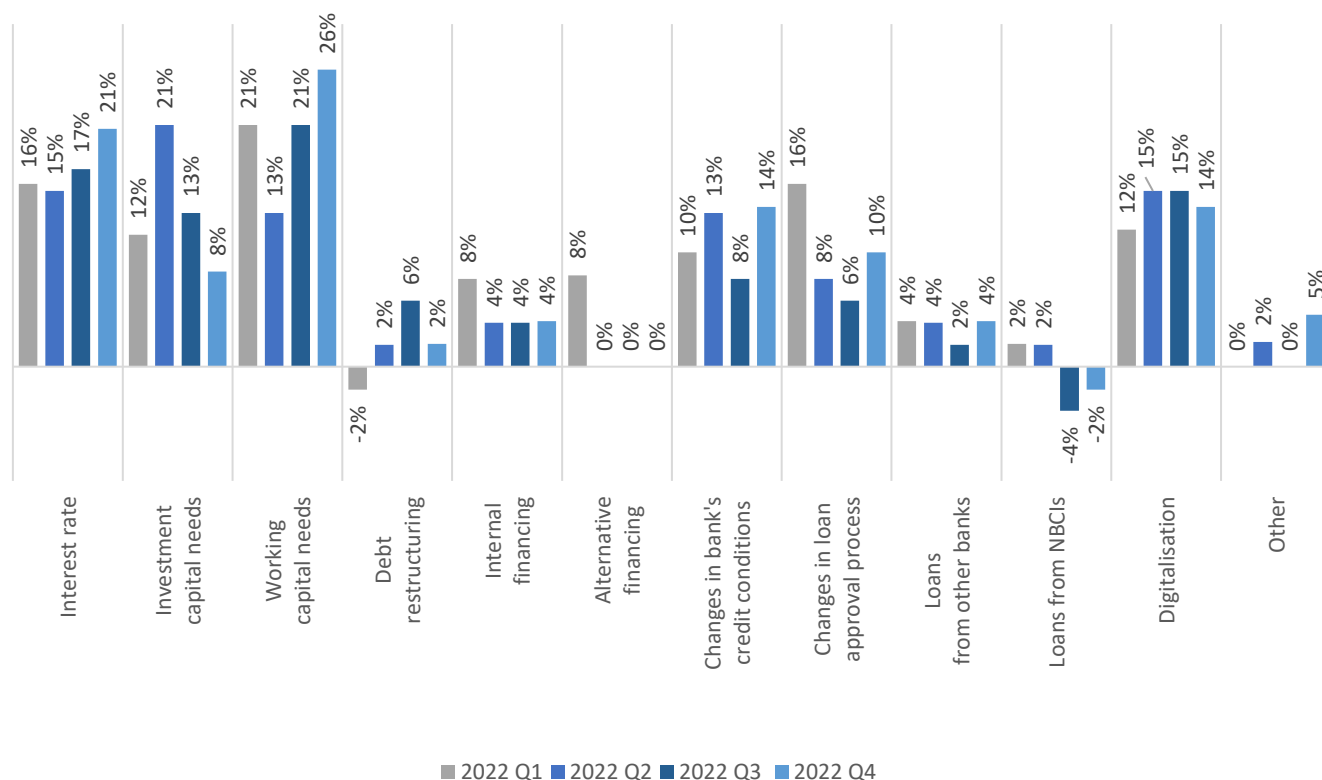


Chart 16. Factors affecting demand for loans to SMEs

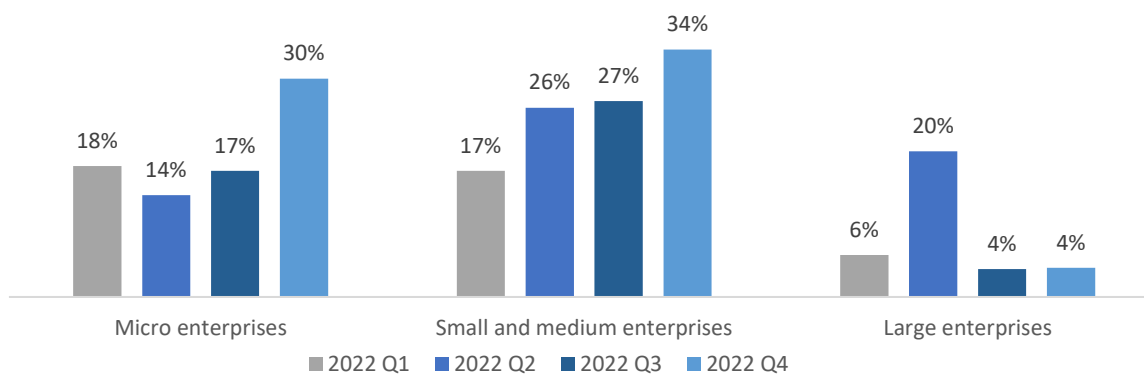
(Diffusion Index: positive = increase, negative = decrease)



In the last quarter of 2022, the indebtedness level of MSMEs was higher compared to previous quarters. Thus, compared to Q3 2022, micro enterprises accounted for the largest increase in the level of indebtedness. The level of indebtedness of large enterprises remained stable.

Chart 17. Changes in indebtedness level of business entities

(Diffusion Index: positive = increase, negative = decrease)

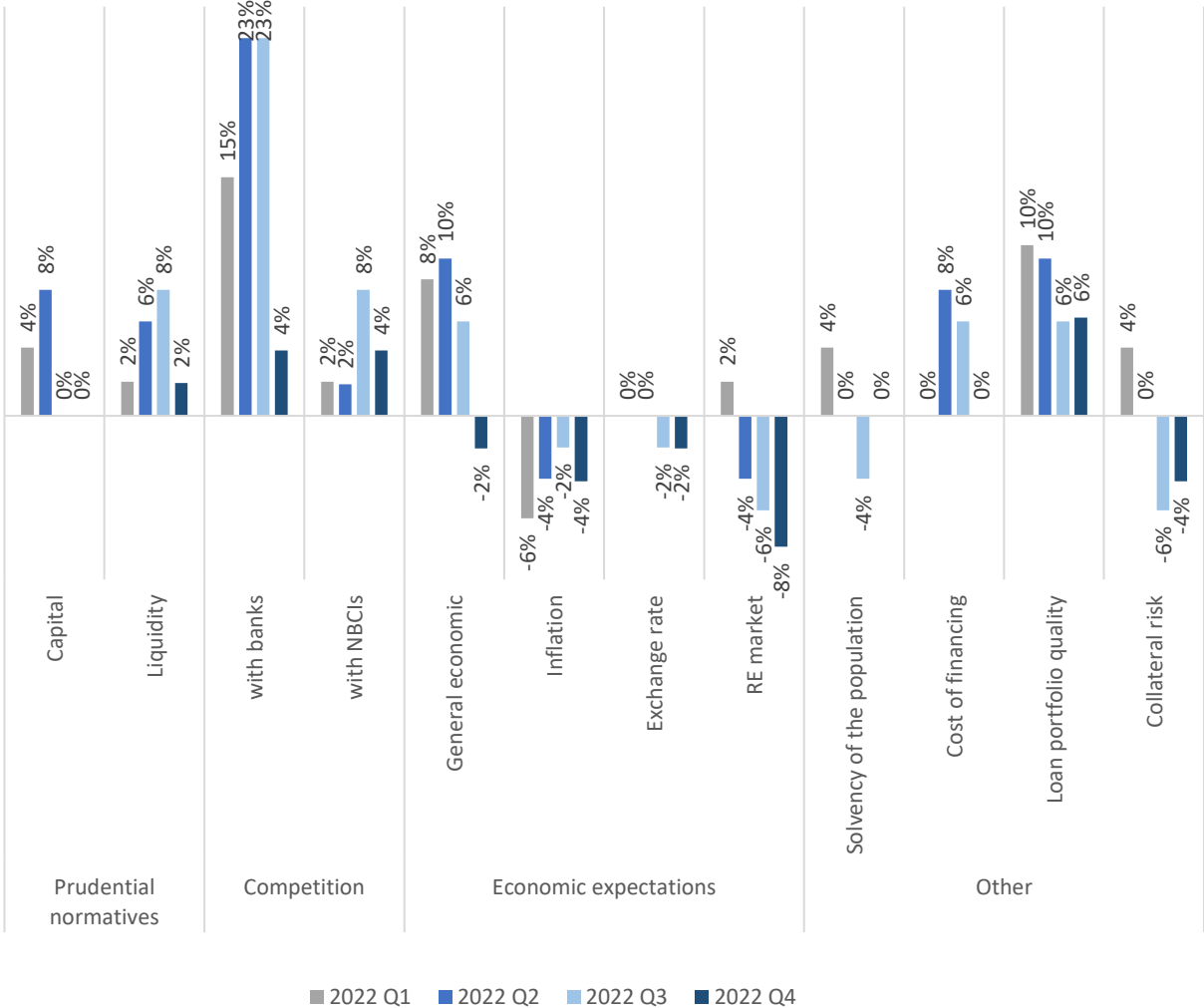


Mortgage and consumer loans

Credit policy on mortgage and consumer loans. In the last quarter of 2022, the softening effect of the competition with banks was lower than in previous quarters. According to the results of the survey, economic expectations act as main factors that have a tightening effect on mortgage lending standards.

Chart 18. Factors affecting credit standards for mortgage loans

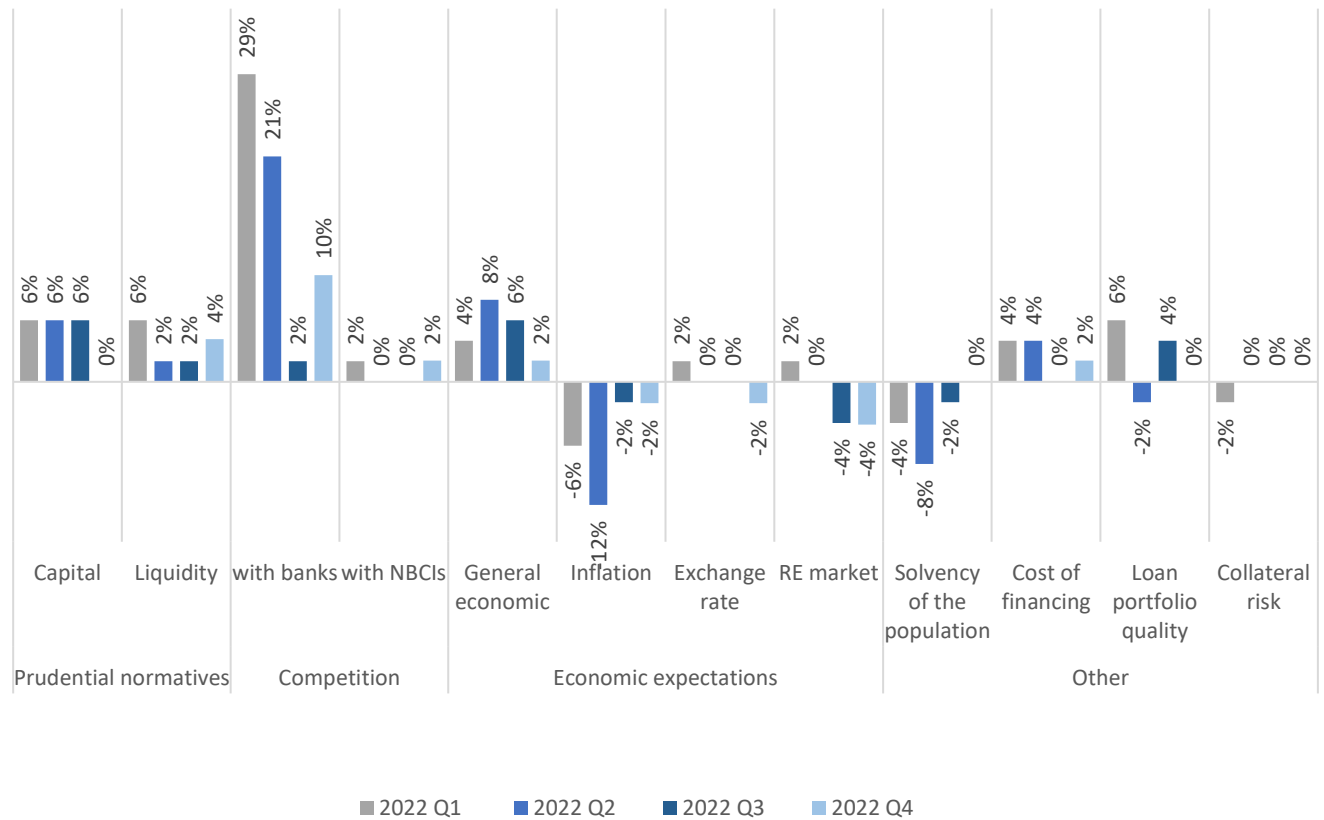
(Diffusion Index: positive = softening, negative = tightening)



Competition with banks was a major factor that softened credit standards for consumer loans. Economic expectations tightened credit standards for consumer loans.

Chart 19. Factors affecting credit standards for consumer loans

(Diffusion Index: positive = softening, negative = tightening)



In Q4 2022, mortgage and consumer credit conditions were softened on all factors. Thus, the easing concerned the interest rate, commission and maximum loan term for consumer loans, and the interest rate and collateral conditions for mortgage loans.

Chart 20. Changes in terms and conditions of mortgage loans

(Diffusion Index: positive = softening, negative = tightening)

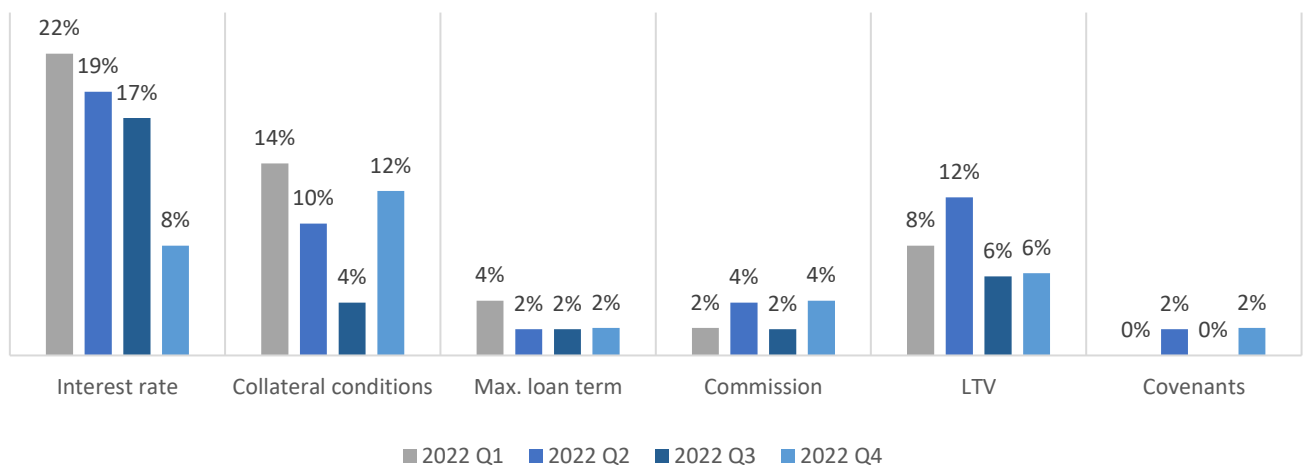
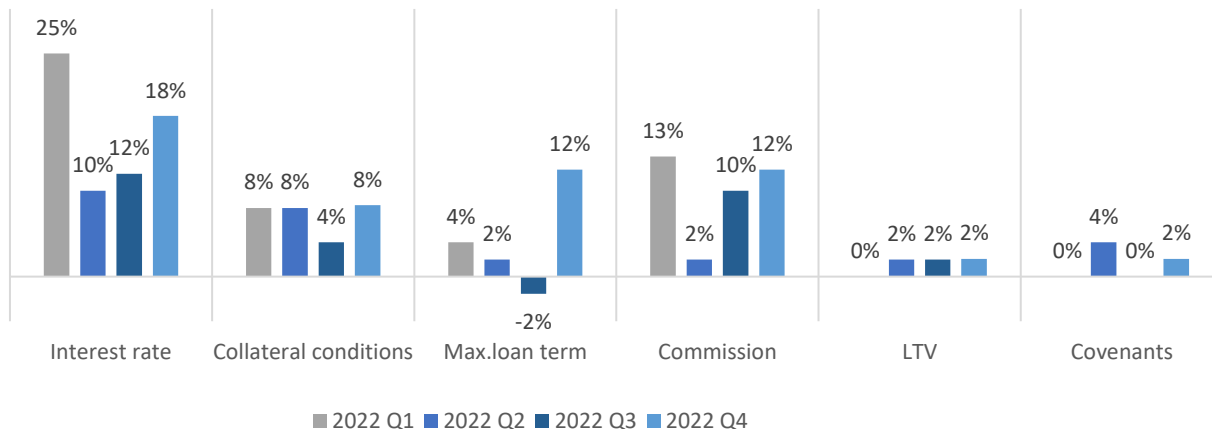


Chart 21. Changes in terms and conditions of consumer loans

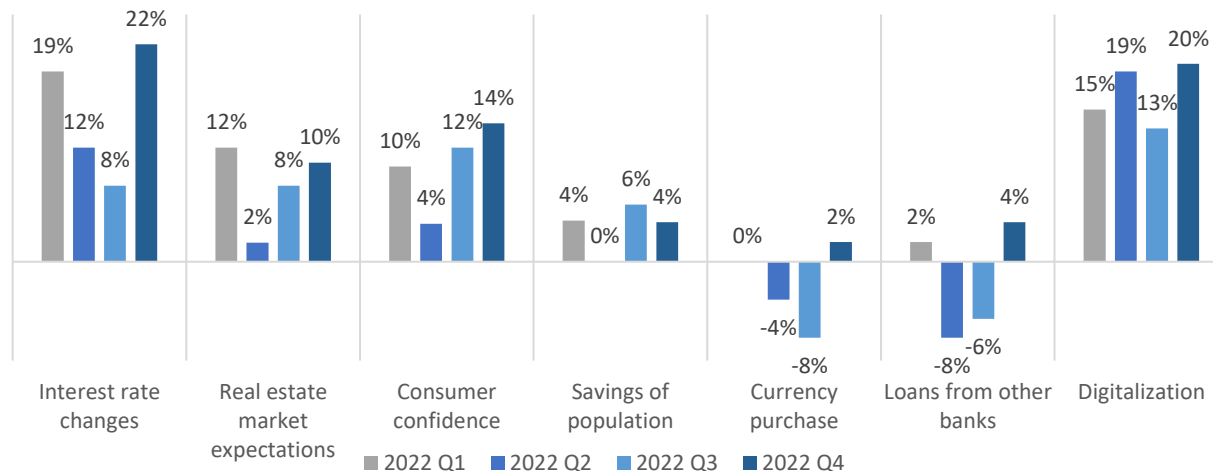
(Diffusion Index: positive = softening, negative = tightening)



Mortgage and consumer loan demand. Demand for mortgage and consumer loans increased in Q4 2022. Digitalization, consumer confidence and changes in interest rates were the main drivers of demand growth.

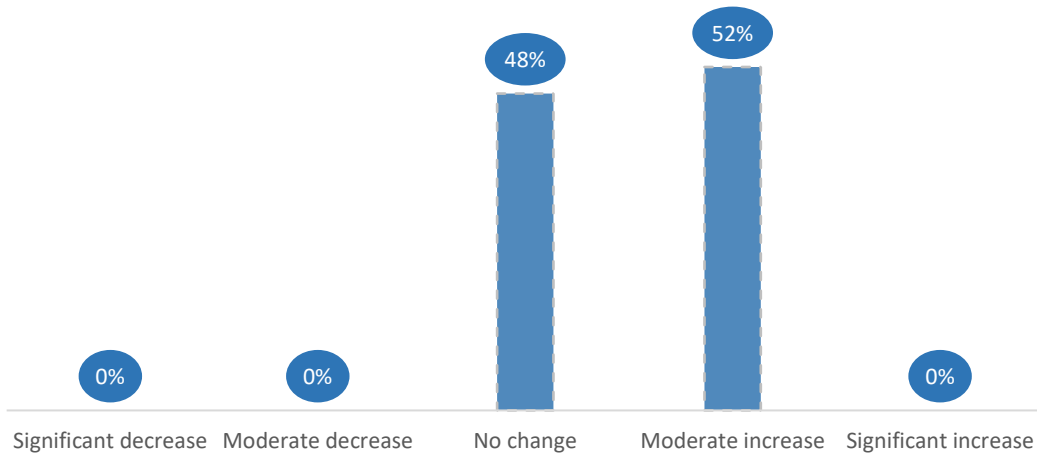
Chart 22. Factors affecting changes in demand for mortgage and consumer loans

(Diffusion Index: positive = increase, negative = decrease)



According to the results of the survey, there was increase in the level of indebtedness of the population during the fourth quarter of 2022. Thus, 48% of the sector’s banks reported that indebtedness remained unchanged, while 52% reported a moderate increase in the indebtedness level.

Chart 23. Changes in the indebtedness level of population in Q4 2022

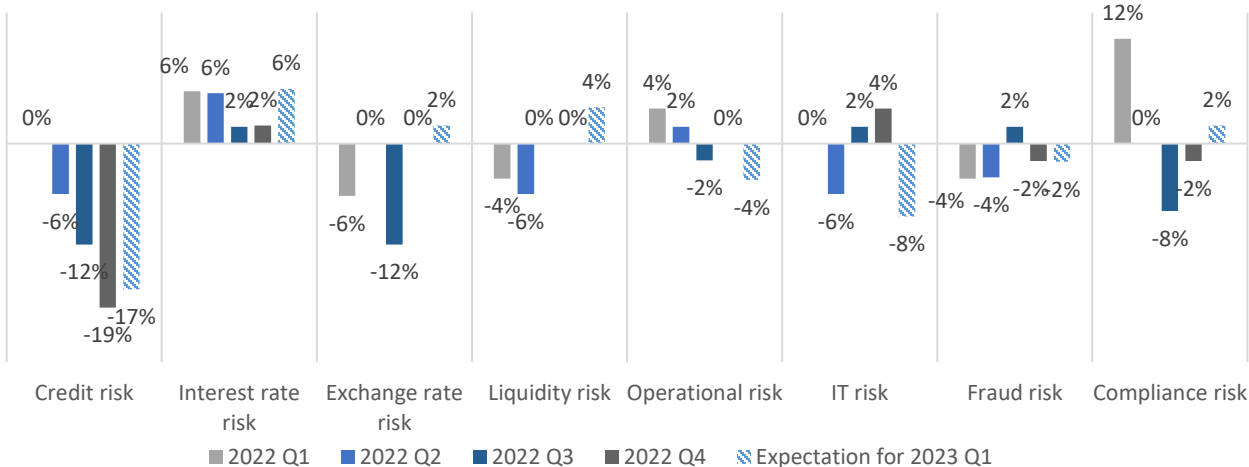


Risk profile

According to the survey, banks noted that credit risk in the sector declined in Q4 2022, while there were no significant changes in other risks. As in previous quarters of 2022, credit risk was the most declining risk. Banks forecast an increase in interest rates and liquidity risks and a decrease in IT risks for the first quarter of 2023.

Chart 24. Changes in banks' risks***

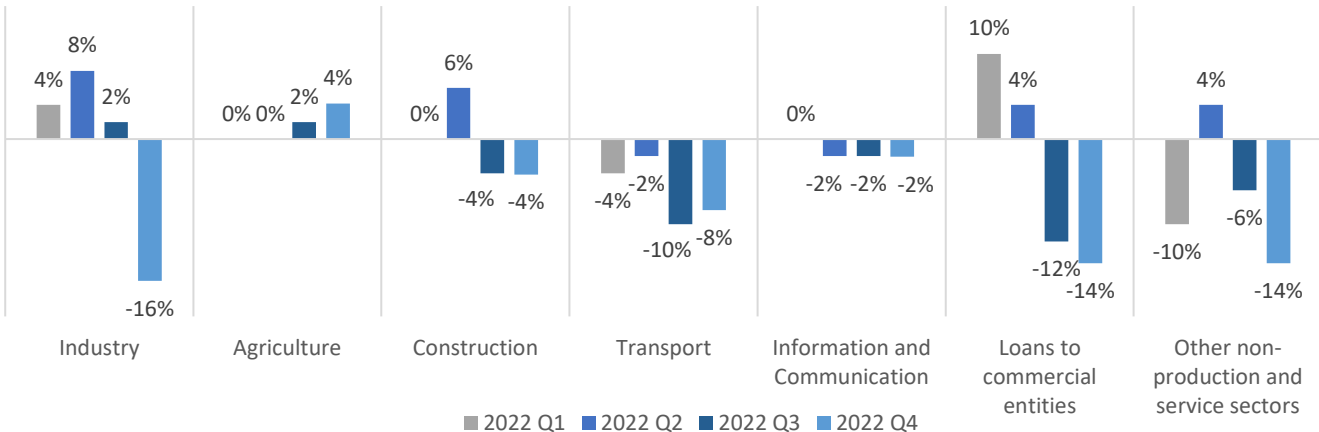
(Diffusion Index: positive = increase, negative = decrease)



In the last quarter of 2022, a decrease in credit risk was observed in most sectors of the economy. The decrease in credit risk occurred mainly on loans granted to industrial and commercial entities, as well as to other non-production and service sectors.

Chart 25. Credit risk changes across sectors

(Diffusion Index: positive = increase, negative = decrease)

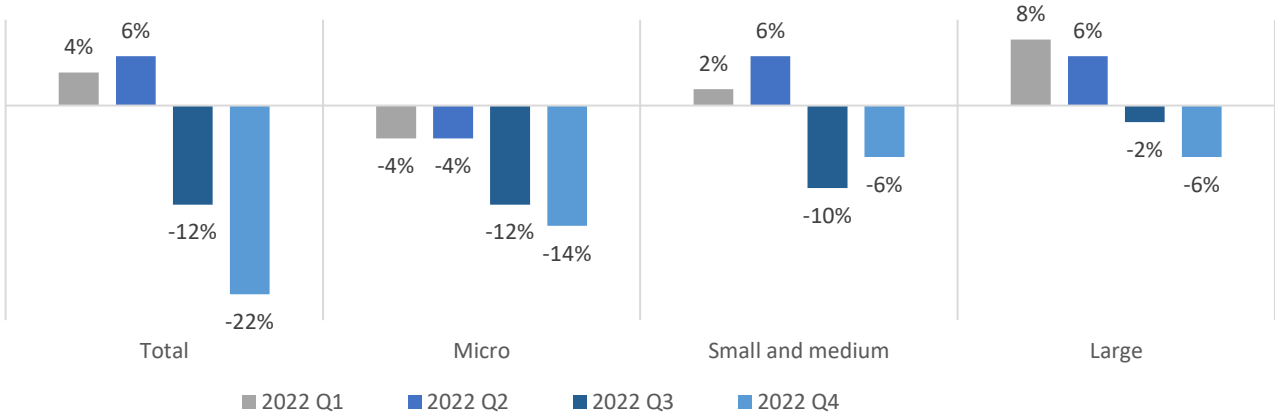


*** A Diffusion Index varies between [-100,+100]. A positive 100% implication indicates that 100% of respondents reported a significant increase in loan demand, while a negative 100% implication indicates a significant decrease.

According to the responses of the respondent banks, as in Q3 2022, the decrease in credit risk of business entities was also observed in Q4. The decrease in the total credit risk of business entities was mainly driven by MSMEs.

Chart 26. Credit risk changes across business entities

(Diffusion Index: positive=increase, negative=decrease)



According to the results of the survey, banks reported a decrease in the level of default rate of the sector's loan portfolio in the last quarter of 2022. At the same time, there was a decrease in the default rate on loans issued to business entities, especially to micro enterprises.

Chart 27. Changes in loan portfolio default rates across sectors in Q4 2022

(Diffusion Index: positive=increase, negative=decrease)

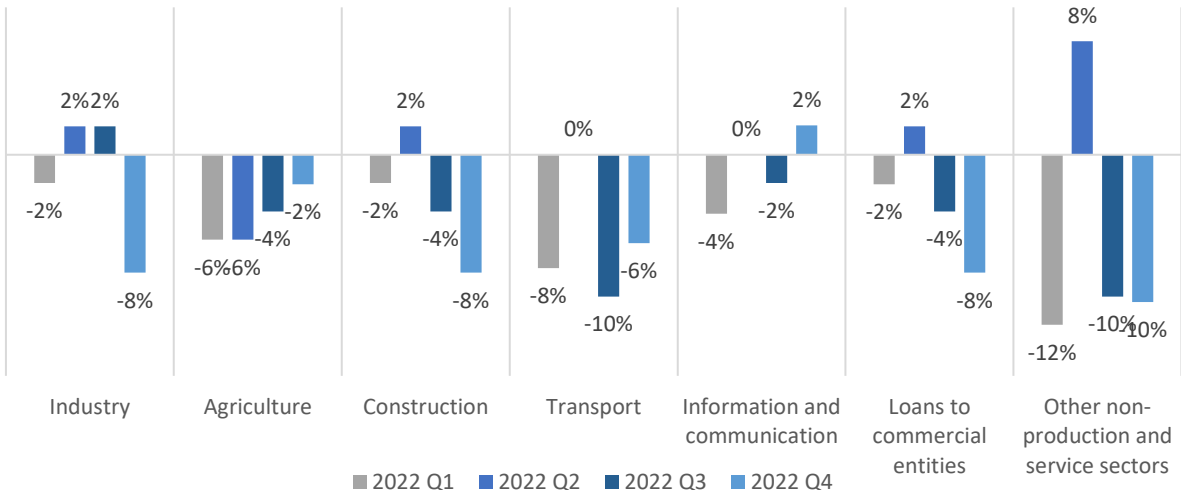
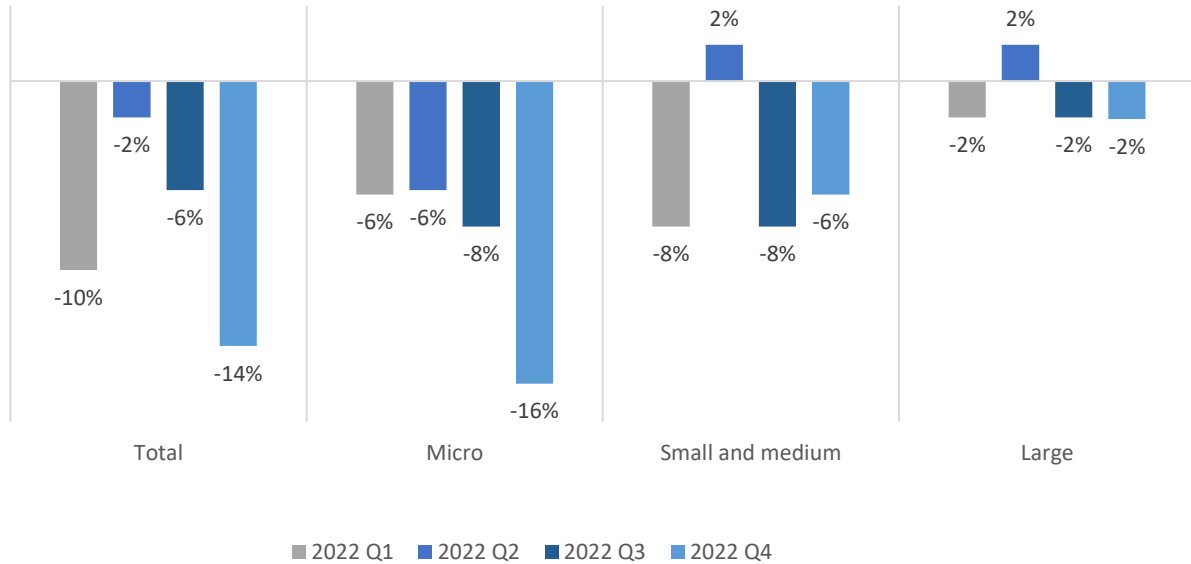


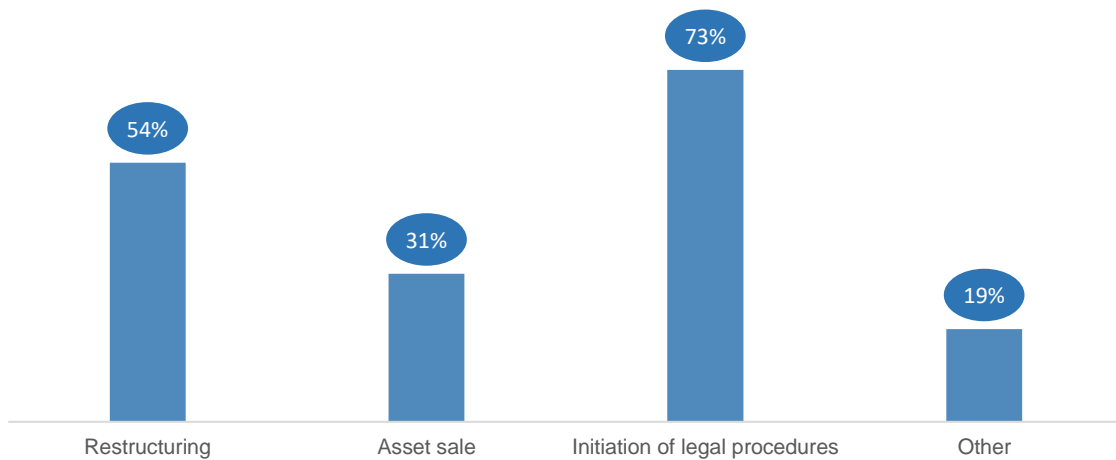
Chart 28. Changes in loan portfolio default rate across business entities in Q4 2022

(Diffusion Index: positive=increase, negative=decrease)



According to the survey results, banks widely used legal proceedings for reducing the NPL portfolio in Q4 2022 as in previous quarter. Banks also reported the use of restructuring, asset sale and other methods to reduce credit risks.

Chart 29. Mechanisms applied to decrease NPL portfolio in Q4 2022



44% of banks reported no change in the applicability level of NPL resolution methods in the fourth quarter, 32% reported a moderate increase, while 24% reported a moderate decrease.

Chart 30. Changes in the applicability of NPL resolution mechanism in Q4 2022

