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The Importance of Improving the Quality of the Credit Portfolio in Commercial Banks

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Annotation: *This article examines the issues of credit portfolio quality and risk management, improving asset quality, and maintaining a balanced growth rate in lending volumes, supported by statistical analysis. The discussion highlights the importance of enhancing credit portfolio and risk management quality, as outlined in the 2020-2025 banking sector reform strategy of the Republic of Uzbekistan. Additionally, an analysis of non-performing loans (NPLs) in commercial banks as of April 1, 2025, is presented. The paper provides conclusions and recommendations on managing credit portfolios and distressed loans, as well as ensuring the efficiency of credit issuance and recovery systems in this sector.*

Keywords: *credit policy, credit risk, credit portfolio, banking system, liquidity ratio, bank assets, loan capital*

Introduction. Today, many countries are faced with the problem of increasing bad debts in the banking system, so the issue of improving the system of working with problem loans of banks is still of great importance. Therefore, along with creditors, there are problems with the repayment of loans by clients that have not found a solution. Since credit operations of commercial banks are an activity that forms bank income, ensuring the stability of the quality level of the loan portfolio is one of the main tasks of banks. Lending is a type of activity of primary importance for commercial banks. A decrease in the quality of the loan portfolio of commercial banks negatively affects their financial stability, while an increase in the share of overdue loans in the volume of loan deposits leads to a decrease in the bank's liquidity level. Therefore, commercial banks pay special attention to the correct formation of the loan portfolio. The increase in the volume of bank loans aimed at developing the economy, the increase in the number of various ownership and business entities using them, the rational allocation of loans issued by banks, increasing their efficiency, and ensuring the timely repayment of interest accrued on loans issued require the importance of constant control over the loan portfolio of banks.

It is worth noting that the following measures are envisaged to optimize the growth of banks' loan portfolios and reduce loan risks:

- banks should use macroeconomic flexibility to optimize the growth rate of their loan portfolio;
- regulating the debt burden of large debtors of the banking system, including setting limits on lending to the largest debtors with excessive debt burdens and the permissible level of debt burden [4]

Therefore, it is envisaged to improve the quality of the loan portfolio and risk management, adhere to moderate growth in lending volumes, and ensure that lending is carried out only on market terms. It is noteworthy that this strategy includes significant work on increasing the accessibility of financial services by strengthening state participation and implementing targeted measures in underserved and vulnerable groups, expanding remote services for the population and small businesses, and creating sufficient conditions for the formation and development of non-bank credit organizations. Indeed, the acceleration of the privatization process of the banking system, as part of the ongoing priority tasks, reflects the importance of the banking system in the economy by mobilizing domestic and foreign investments in banks, commercializing their activities, and increasing investor confidence.

Today on the day credit portfolio quality and risk management , its improving the quality, in line with the growth of lending volumes to the formation achieving , pursuing a balanced macroeconomic policy through The goal is to ensure the financial stability of the banking system. is appropriate . However , financial to a stable farm achieve It is defined as one of the priority areas of reform of the banking system of the Republic of Uzbekistan. The current state of the loan portfolio not only determines the quality of the bank's credit policy, but also allows analyzing the results of credit activities for the bank in the future. Formation, optimization and quality management of the loan portfolio of a commercial bank is considered the main stage of implementing the credit policy. This at the time credit portfolio situation bank credit politics of quality It also expresses its effectiveness. Credit portfolio effective formation for first in line credit process correct and own instead of done increase brought Credit politics commerce bank only credit system to the body brings .

Analysis and results. The primary objective of effective credit portfolio management in commercial banks is to achieve optimal levels of risk, profitability, and liquidity indicators for this portfolio. There are numerous factors involved in improving credit portfolio quality in commercial banks, some of which include:

Strengthening the mechanism for resolving problematic situations related to bank assets by conducting continuous monitoring of asset quality, enabling early detection and elimination of issues;

Developing risk management measures aimed at asset diversification and improving credit portfolio quality;

Organizing the implementation of regulatory documents governing banking system decisions and credit relations, which allows for proper assessment, study, and analysis of potential risks in the lending process, monitoring business plan performance indicators, and forming new methods for managing non-performing loans. Within the framework of development strategy tasks aimed at rapid development of the national economy and ensuring high growth rates:

This involves completing transformation processes in state-owned commercial banks and increasing the private sector's share in bank assets to 60% by the end of 2026. Specifically, the volume of banks' credit operations will grow, ensuring stable increases in interest income from loans.

Particular importance is given to improving the system for assessing clients' creditworthiness. The existence of problems in evaluating clients' creditworthiness in the practice of our republic's commercial banks negatively affects credit portfolio quality and its stable growth.

Key Aspects of Credit Portfolio Management

First and foremost, fair assessment of a client's creditworthiness ensures timely full repayment of loans. Achieving improvements in credit portfolio quality requires:

- increasing the responsibility of banks' credit committees and officers in loan approval decisions;
- properly structuring mechanisms for monitoring loan use and repayment;
- timely identification, quality assessment, and elimination of potential risks.

Minimizing overdue loan amounts on a regular basis is directly related to approved credit policies. Current legislation requires regular analysis of bank credit portfolios, which helps identify credit quality while emphasizing the importance of credit process management and quality assessment criteria.

Regulatory compliance and financial stability

Banks must comply with regulatory requirements set by the central bank in their operations. These indicators play a crucial role in maintaining financial stability. High levels of non-performing loans pose risks to banks and indicate problems in credit portfolio management.

To assess commercial banks' compliance with regulations, we will review some key regulatory indicators:

- adherence to central bank requirements is essential for ensuring stable banking operations;
- all banks must form adequate reserves for non-performing loans, which improves their risk management approach;
- through debt restructuring, commercial banks can help clients restore repayment capacity.

as practical evidence of the above arguments, we will examine the following table data:

Commerce banks problematic on non-performing loans (NPL) as of April 1, 2025 information				
No.	Bank name	Credits	Problematic loans (NPL)	Problematic of loans total in loans share
1	National Bank of Uzbekistan	108,593	3 457	3.2%
2	Uzbek Industrial and Construction Bank	68,860	2,805	4.1%
3	Agrobank	64,633	2,900	4.5%
4	Asaka bank	39,577	1,868	4.7%
5	Xalq bank	29 186	1 223	4.2%
6	Business development bank	23 271	1,875	8.1%
7	Microcredit bank	18,808	1 243	6.6%
8	Aloqa bank	14,080	361	2.6%
9	Turon bank	12 582	393	3,1%

(Table 1) Commerce banks problematic loans about information (billion soums) [4]

The presented data reflects the status of non-performing loans (NPLs) in Uzbek commercial banks as of April 1, 2025. Non-performing loans (NPLs) are a key indicator for assessing the quality of bank assets, the effectiveness of credit risk management, and financial stability. They can significantly impact a bank's future profitability, liquidity, and capital base.Variation in NPL Ratios Among Banks As shown in the table, there are notable differences in the share of non-performing loans relative to total loans among commercial banks. The lowest ratio was recorded at Aloqa Bank (2.6%), while the highest was observed at the Business Development Bank (8.1%). This reflects disparities in credit policies, risk management systems, customer segments, and business orientations across banks.

Business Development Bank (8.1%)**:** This bank's NPL ratio is the highest among the analyzed banks. This may indicate elevated risk levels in its loan portfolio or inefficiencies in loan recovery. The bank's focus on business development often involves financing high-risk projects, which could contribute to its higher NPL ratio.

Microcreditbank (6.6%)**:** By nature, microcredits—typically smaller in amount but extended to a larger number of clients-carry higher default risks compared to other loans. While this may objectively explain the higher NPL ratio, it still highlights the need to improve the bank's credit risk management system.

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Asaka Bank (4.7%) and Agrobank (4.5%)**:** These banks exhibit moderately high NPL ratios, underscoring the importance of ongoing monitoring of credit risks.

Aloqa Bank (2.6%), Turon Bank (3.1%), and National Bank of Uzbekistan (3.2%)**:** The relatively low NPL ratios at these banks reflect the high quality of their loan portfolios and their effective risk management capabilities. Notably, O'zmilliybank's low NPL ratio-despite its large loan portfolio-demonstrates the robustness of its lending processes and risk assessment mechanisms. The table data does not reveal a direct proportional relationship between the size of the loan portfolio and the NPL ratio. For instance, National Bank of Uzbekistan has the largest loan portfolio but maintains a low NPL ratio, whereas the Business Development Bank, with a mid-sized portfolio, has the highest NPL ratio. This suggests that a bank's size is less determinative than its credit policy, sectoral focus, risk management system, and resilience to macroeconomic factors.

Implications of NPL Levels:

Financial Stability: Banks with high NPL ratios, such as the Business Development Bank and Microcreditbank, may face challenges related to capital adequacy, liquidity, and profitability. The need to allocate provisions for non-performing loans reduces earnings and limits the capacity to issue new credits.

Lending Activity: Elevated NPL levels can weaken banks' lending capabilities, potentially reducing investments in the economy.

Systemic Risks: While each bank's NPL level reflects its individual risk, a sharp increase in NPLs across several major banks could negatively impact the stability of the entire financial system. The currently low NPL ratios at large banks somewhat mitigate systemic risks.

Recommendations:

1. In-Depth Portfolio Analysis: Banks with high NPL ratios should conduct thorough analyses of their loan portfolios, including loan purposes, collateral quality, customer segments, and regional distribution.
2. Enhanced Risk Management: Banks, particularly those with high NPL levels, must improve their credit risk assessment, monitoring, and recovery processes.
3. Monitoring Macroeconomic Factors: Continuous analysis of macroeconomic drivers—such as economic growth, inflation, employment, and sectoral trends—is essential to anticipate potential deteriorations in loan quality.
4. Regulatory Oversight: The central bank and other regulators should regularly monitor NPL levels, enforce compliance with lending standards, and take corrective measures when necessary.

Conclusion

Significant disparities exist in NPL ratios among Uzbek commercial banks, with some banks exhibiting high-risk exposure. These findings underscore the need to continuously strengthen risk management and regulatory oversight to ensure the stability of the banking system.

To improve the qualitative efficiency of commercial banks' loan portfolios, we propose the following measures:

1. Continuous Monitoring**:** Implement robust, real-time monitoring of asset quality to identify and address issues at early stages.
2. Diversification**:** Enhance loan portfolio quality through diversification, reducing concentration risks.

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3. Regulatory Framework**:** Ensure that decisions and normative-legal documents governing credit relations account for potential risks and incorporate thorough risk analysis.

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