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INCREASING THE PROFITABILITY OF COMMERCIAL BANKS AS A WAY TO ENSURE FINANCIAL STABILITY

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Abstract: The article examines the theoretical and scientific foundations of the financial stability of commercial banks, with a focus on the specific features of bank profitability. The research systematizes foreign and domestic scientific studies conducted on the topic and develops the author's own approaches to the issue. Based on the conducted research, the theoretical foundations of ensuring financial stability through bank income growth have been systematized.

Key words: bank income, interest income, non-interest income, financial stability.

Annotatsiya: Maqolada tijorat banklarining moliyaviy barqarorligining nazariy va ilmiy asoslari, bank daromadliligining o'ziga xos xususiyatlariga e'tibor qaratilgan holda o'rganiladi. Tadqiqot mavzu bo'yicha olib borilgan xorijiy va mahalliy ilmiy tadqiqotlarni tizimlashtiradi va muallifning bu masalaga o'z yondashuvlarini rivojlantiradi. O'tkazilgan tadqiqot asosida bank daromadlarining o'sishi orqali moliyaviy barqarorlikni ta'minlashning nazariy asoslari tizimlashtirildi.

Kalit so'zlar: bank daromadi, foizli daromad, foizsiz daromad, moliyaviy barqarorlik.

Аннотация: В статье рассматриваются теоретические и научные основы финансовой устойчивости коммерческих банков, особое внимание уделяется особенностям их рентабельности. В исследовании систематизированы зарубежные и отечественные научные исследования по данной теме, а также разработаны авторские подходы к ее решению. На основе проведенного исследования систематизированы теоретические основы обеспечения финансовой устойчивости посредством роста доходов банков.

Ключевые слова: доходы банков, процентные доходы, непроцентные доходы, финансовая устойчивость.

INTRODUCTION

The profitability of commercial banks is widely recognized as one of the most fundamental and comprehensive indicators of their operational efficiency and financial sustainability. In the modern financial and economic system, profitability not only reflects the efficiency of a bank's resource utilization but also serves as a key determinant of its long-term competitiveness, solvency, and capacity for sustainable development. A stable level of profitability demonstrates the bank's ability to generate income consistently, maintain sufficient capital reserves, and withstand internal and external shocks. Hence, the profitability indicator is increasingly viewed as a critical criterion for evaluating the quality of financial management and the resilience of the banking institution in both national and international contexts.

In contemporary global practice, commercial banks face complex challenges associated with fluctuating macroeconomic conditions, geopolitical instability, and the growing interdependence of financial markets. These circumstances require banks to focus not only on short-term financial performance but also on building a robust framework for financial stability. Ensuring profitability in such conditions demands a systematic approach to identifying, assessing, and mitigating risks that may arise from internal operational inefficiencies or external economic and political uncertainties. In this regard, the balance between profitability and stability becomes a pivotal component of sustainable banking strategy.

The experience of leading financial institutions worldwide demonstrates that profitability plays a decisive role in ensuring financial stability through mechanisms such as improved asset quality, capital adequacy, and effective risk management. For instance, many commercial banks have developed strategies to enhance return on assets (ROA) and return on equity (ROE) by optimizing their income structures, diversifying revenue sources, and adopting innovative financial instruments. The emphasis is placed not only on interest-based income but also on non-interest income — including fees, commissions, and investment returns — which serve as vital elements in maintaining income stability during periods of economic turbulence.

As noted in the analytical studies of the Bank for International Settlements (BIS), the long-term resilience of banks depends largely on their capacity to sustain profitability under stress scenarios. According to J.

Caparusso and colleagues from the BIS, the assessment of global trends in bank profitability should rely on a multidimensional framework that incorporates capital adequacy ratios, the market-to-book value ratio, and the scale of excess capital above regulatory requirements. Their findings suggest that the increase in market valuation exerts a positive influence on both return on capital and the creation of a management buffer, which acts as a safeguard during periods of economic volatility [1].

Moreover, the BIS researchers emphasize that profitability and financial stability are interdependent and mutually reinforcing. High profitability strengthens a bank's capital position, enhances its ability to absorb losses, and contributes to investor confidence. Conversely, financial stability creates a favorable environment for maintaining sustainable profitability by reducing funding costs, improving market perception, and enabling long-term investment strategies. Therefore, the interaction between these two dimensions should be viewed as a dynamic equilibrium that underpins the overall robustness of the banking system.

In the context of Uzbekistan's ongoing banking sector reforms, this relationship between profitability and financial stability becomes particularly significant. As the national economy continues its transition toward market-based mechanisms and increased integration into global financial systems, commercial banks must adopt advanced management practices that align with international standards of capital adequacy, risk assessment, and corporate governance. Ensuring profitability under such circumstances is not merely an operational goal but a strategic necessity for safeguarding the resilience of the financial system as a whole.

In summary, enhancing the profitability of commercial banks serves as a vital mechanism for ensuring their financial stability and long-term sustainability. The global and domestic experiences analyzed in this study underscore the importance of developing adaptive strategies that integrate profitability management with comprehensive financial stability frameworks. This theoretical and empirical foundation lays the groundwork for further exploration of best practices, methodological approaches, and policy measures aimed at strengthening the financial resilience of commercial banks in Uzbekistan and beyond.

LITERATURE REVIEW

The analysis of existing scientific literature reveals that the profitability of commercial banks is a central determinant of their financial stability, directly influencing their resilience, competitiveness, and long-term development capacity. Numerous international and domestic scholars have examined this interrelation from various theoretical and empirical perspectives, emphasizing that profitability not only reflects operational efficiency but also serves as a critical mechanism for absorbing external shocks and maintaining confidence in the banking system.

The increase in a bank's market value has been shown to exert a positive influence on its profitability, reinforcing its capital base and managerial effectiveness. Consequently, enhancing profitability through sound income diversification and efficient asset management remains a key strategic direction for ensuring financial stability. This interdependence suggests that maintaining the stability of profitability-related indicators—such as return on assets (ROA), return on equity (ROE), and net interest margin—is essential for sustainable financial performance. Effective management of these factors enables banks to strengthen their capital adequacy, optimize liquidity, and mitigate systemic risks in volatile economic environments.

A seminal study conducted by P. Lamoze et al. explored the relationship between profitability and financial stability across more than 2,000 banks operating in 110 countries [2]. Using a random effects regression model, the researchers assessed the influence of both internal and external factors on bank profitability. According to their findings, internal factors such as restructured loans, interest income growth, and capitalization play a significant role in shaping profitability outcomes. Meanwhile, external factors—including asset ratings of the respective countries, inflation levels, unemployment rates, interest rate fluctuations, and overall economic growth—exert measurable effects on banks' income stability. The study underscores the multidimensional nature of profitability management, suggesting that sustainable financial stability requires a balanced consideration of internal operational efficiency and external macroeconomic conditions.

In a complementary study, E. Kohlscheen and co-authors analyzed the developmental trends of bank profitability in emerging economies [3]. Their research highlighted that higher long-term interest rates tend to strengthen profitability by supporting stable income flows, while higher short-term interest rates can diminish profitability due to increased reserve requirements and higher funding costs. Moreover, they emphasized that in stable economic environments, the expansion of credit activity exerts a more substantial influence on profitability than the overall growth of gross domestic product (GDP). This indicates that proactive credit policies, when aligned with prudent risk management, can significantly enhance a bank's income-generating capacity.

The results of these studies collectively demonstrate that profitability serves not only as a measure of operational efficiency but also as a buffer mechanism that enhances the financial resilience of banks. The interaction between profitability and financial stability reflects a dual causality: while profitability strengthens

capital and ensures liquidity, financial stability, in turn, fosters a favorable environment for sustainable profit generation.

In the context of developing economies—particularly in Uzbekistan—these findings acquire special relevance. The ongoing transformation of the national banking sector requires the adoption of best international practices for managing profitability and stability in tandem. This includes enhancing income diversification, strengthening capital adequacy in line with Basel III standards, and improving corporate governance mechanisms. By doing so, commercial banks can ensure that their profitability contributes not merely to short-term financial gains but also to the broader objective of systemic financial stability and sustainable economic growth.

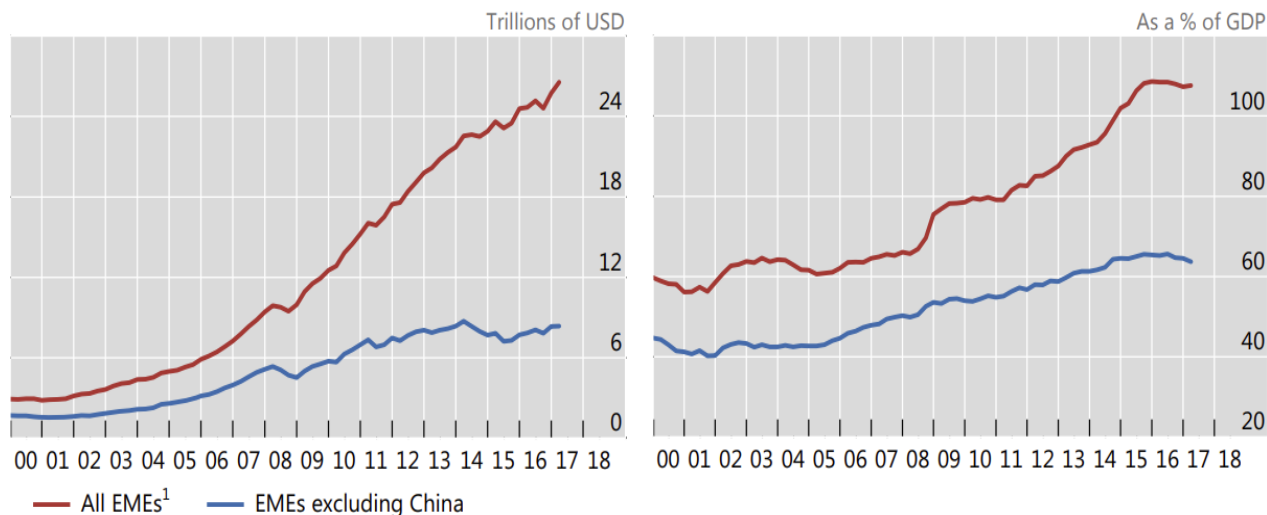


Figure 1. Volume of Bank Loans to the Non-Financial Sector in Developing Countries, 2000–2018 (in trillion USD)

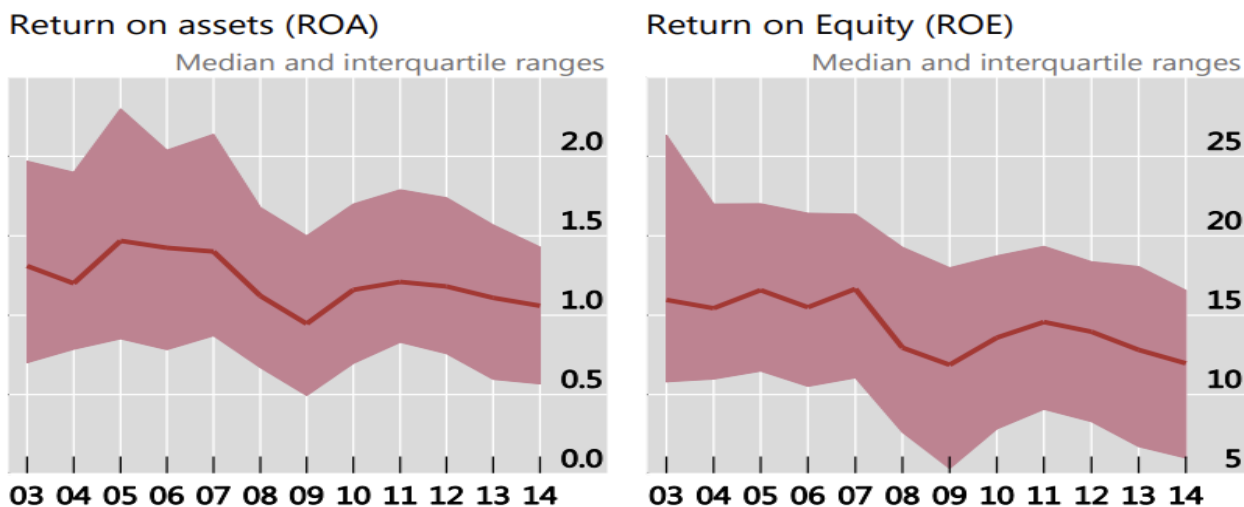


Figure 2. Profitability of the Banking System in Developing Countries, 2003–2014

The data presented in Figure 2 illustrate the dynamics of profitability in the banking systems of developing countries between 2003 and 2014. During this period, fluctuations in profitability reflected the sensitivity of the banking sector to both global and domestic economic cycles. The trends suggest that financial cycles—rather than traditional business cycles—play a more decisive role in forecasting bank profitability. In particular, the reduction of sovereign credit risk, while improving overall stability, has paradoxically been associated with a decline in profitability, indicating the complex trade-off between risk minimization and income generation in the modern banking environment.

It should be noted that the profitability of banks evolves in close connection with macroeconomic stability. Changes in both global and local economic conditions can significantly affect banks' rates of return and income composition. In this regard, the nature of macroeconomic conditions determines the design and implementation of lending policies, influencing the volume, quality, and profitability of credit portfolios. Therefore, aligning

banks' credit and investment strategies with the prevailing macroeconomic policies of the country serves as an essential prerequisite for ensuring sustainable financial performance.

From a broader theoretical perspective, the interaction between banking profitability and macroeconomic policy underscores the need for integrated analysis. Banks operating in economies undergoing structural transformation—such as Uzbekistan—must carefully consider how fiscal discipline, monetary policy, and exchange rate regimes affect their profitability patterns. Ignoring these factors could lead to distorted assessments of financial performance and expose institutions to systemic risks.

In this context, the empirical research conducted by F. Khasanov et al. provides valuable insights [4]. Their study focused on the Azerbaijani economy, characterized by heavy dependence on natural resource revenues, particularly oil. Using the Panel Generalized Method of Moments (GMM), the authors analyzed how various bank-specific and macroeconomic variables influence profitability under conditions of declining oil prices, national currency devaluation, and financial instability. Their findings revealed that factors such as bank size, capital adequacy, credit volume, business cycle phase, inflation expectations, and oil prices have a positive impact on profitability. Conversely, deposits, liquidity risks, and currency devaluation exert a negative influence, underscoring the vulnerability of profitability to both financial and external shocks. Importantly, the study concludes that excluding macroeconomic conditions from profitability assessments may result in incomplete or misleading conclusions about a bank's true financial position.

Similarly, P. Athanasoglou and co-authors conducted an extensive analysis of Greek banks' performance between 1985 and 2001 [5]. Their study emphasized the dual influence of bank-specific and macroeconomic indicators on profitability. According to their results, almost all internal variables—except for bank size—significantly affect profitability. They further demonstrated that business cycles exert a continuous influence, particularly pronounced during the expansion phase, when credit activity and investment opportunities increase. This finding reinforces the notion that profitability is inherently cyclical and responsive to broader economic dynamics.

Based on the comprehensive review and comparative analysis of these studies, several scientific conclusions can be drawn:

1. Systematization of influencing factors: Each bank's financial stability is shaped by a complex set of internal and external factors. Classifying these determinants into coherent groups allows for more accurate risk assessment and targeted policy responses.

2. Identification of determinants of profitability: Recognizing and managing the variables that drive fluctuations in profitability—such as capital structure, lending efficiency, and market conditions—are crucial for stabilizing income streams and mitigating volatility.

3. Integration of macroeconomic analysis into decision-making: Effective financial decision-making should be grounded in the continuous assessment of the macroeconomic environment. This includes evaluating how inflation, GDP growth, exchange rates, and fiscal policy influence bank profitability. By incorporating these dimensions, banks can formulate strategic financial decisions that enhance their profitability while reinforcing long-term financial stability.

Overall, the reviewed literature and empirical evidence highlight the interdependence between micro-level bank performance and macroeconomic dynamics, underscoring the need for a multidimensional analytical approach in both academic research and practical policy formulation.

ANALYSIS AND RESULTS

In the course of our research, we focused on studying several international trends and empirical findings aimed at ensuring the profitability of banks. In particular, we examined the experience of Japan, whose banking sector provides an illustrative case of transformation and resilience following a major financial crisis.

The Experience of Japan

The Japanese banking system underwent significant structural changes in the years following the 1990 financial crisis. The crisis, often referred to as the “lost decade,” was triggered by the bursting of the asset price bubble, which resulted in widespread loan defaults and a severe decline in banks' profitability. In response, Japan's monetary and regulatory authorities implemented a series of reforms to address non-performing loans and enhance prudential regulation.

The Financial Services Agency (FSA) of Japan emerged as the primary governmental body responsible for maintaining the stability of the banking system, protecting depositors, and improving the efficiency of financial markets. Currently, the Japanese banking sector operates under the requirements of Basel III, designed to strengthen the system's resilience against economic shocks through the development of capital adequacy standards, stress testing mechanisms, and market liquidity frameworks.

According to X. Liu et al., who analyzed the profitability and development trends of Japanese banks [6], the post-crisis recovery period highlighted the importance of ownership structure and diversification. Their research demonstrated that regional banks, through diversification of services, achieved higher profitability, while industrial orientation and the overall development of financial markets played crucial roles in sustaining income levels.

Furthermore, V. Kumar and colleagues conducted a comprehensive study on how financial inclusion influences bank profitability in developed economies [7]. Based on the performance of 122 Japanese banks during the period 2004–2018, their analysis confirmed that financial inclusion exerts a significant impact on bank profitability, even in highly developed markets. The authors found that banks offering a wider range of financial services tend to outperform competitors in terms of income generation. However, excessive branch reduction negatively affects profitability, while the number of credit accounts and ATMs does not directly enhance profitability. Instead, cost management, bank size, and credit risk control were identified as the primary determinants of sustainable profitability.

In addition, Japanese banks operate under stricter capital adequacy standards than those prescribed by Basel III. Specifically, the Common Equity Tier 1 (CET1) ratio must not be lower than 4.5%, the Tier 1 capital ratio must be at least 6%, and the total capital adequacy ratio must meet or exceed 8%. Furthermore, banks are required to maintain a capital conservation buffer equivalent to at least 2.5% of risk-weighted assets. These measures are aimed at ensuring the robustness of the banking sector and preventing systemic instability in the event of financial turbulence.

Drawing from Japan's experience, we believe that the following lessons and policy directions could be effectively applied within the context of Uzbekistan's banking sector:

1. Expansion of financial service diversification — To enhance profitability, banks should broaden the range of financial products and services they offer, tailoring them to different customer segments. Diversification across service categories reduces dependence on a single income source and improves income stability.

2. Strengthening customer outreach both online and offline — Banks should expand accessibility to financial services by maintaining physical service points in densely populated areas while simultaneously developing digital channels. This dual approach increases financial inclusion and enhances customer trust and satisfaction.

3. Developing national capital adequacy standards — In addition to complying with international Basel III requirements, it is advisable to design capital adequacy benchmarks that reflect the specific characteristics of the national economy and the operational environment of domestic banks.

In conclusion, Japan's experience demonstrates that profitability and financial stability are inseparable elements of an effective banking strategy. The Japanese model underscores the critical importance of diversification, sound capital management, and regulatory discipline in achieving sustainable profitability. Building upon these insights, our research continues to explore advanced international practices in improving bank profitability and strengthening financial stability.

The Experience of Turkey

The banking sector of Turkey has developed through a distinctive trajectory shaped by both domestic reforms and global financial dynamics. Following the severe financial crisis of the early 2000s, Turkey undertook profound reforms to restructure its banking system, restore confidence, and align its regulatory framework with international standards. One of the most notable aspects of Turkey's experience is the large-scale restructuring of state-owned banks and the liberalization of financial markets to attract foreign investment and enhance competitiveness.

According to H. Akbaş et al., the determinants of bank profitability in Turkey were analyzed using financial data from 26 banks covering the period 2005–2010 [8]. Their study identified return on assets (ROA) and return on equity (ROE) as the primary indicators of profitability. The findings revealed that credit risk management and efficient cost control were among the key internal factors influencing profitability. The relationship between asset profitability and lending operations was found to be positive, whereas deposit activities exhibited a negative correlation. Furthermore, macroeconomic indicators such as inflation expectations were observed to have an adverse effect on profitability, while other macroeconomic factors showed only marginal influence.

In a broader analysis, M. Topak and colleagues examined the determinants of bank profitability from both microeconomic and macroeconomic perspectives [9]. Using monthly panel data regression models covering the years 2005–2015, they investigated the influence of various internal and external variables on profitability. Their results demonstrated that the loan-to-deposit ratio, net interest margin, non-interest income to operating expenses ratio, and bank size exerted a positive and statistically significant impact on both ROA and ROE. Conversely, the volume of non-performing loans (NPLs), credit risk, capital adequacy ratio, and operating expenses to income ratio were found to negatively affect profitability.

These studies collectively underscore that effective credit risk management, cost efficiency, and balanced income diversification are essential elements in sustaining profitability and ensuring financial stability within the Turkish banking sector. The experience of Turkey highlights several important lessons:

1. Post-crisis restructuring as a foundation for resilience — The systematic reorganization of state-owned banks, coupled with enhanced transparency and privatization, contributed to restoring investor confidence and improving operational performance.

2. Importance of risk-sensitive management practices — Banks that prioritized prudent lending, credit risk assessment, and cost optimization achieved more stable profitability levels over time.

3. Macroeconomic discipline and policy coordination — The alignment of monetary and fiscal policies with the banking sector's strategic objectives proved instrumental in minimizing inflationary pressures and maintaining financial equilibrium.

The Turkish case provides valuable insights for countries such as Uzbekistan, where the banking sector is also undergoing rapid transformation. Strengthening the institutional framework, improving risk management mechanisms, and ensuring macroeconomic stability remain crucial for enhancing the profitability and financial resilience of commercial banks.

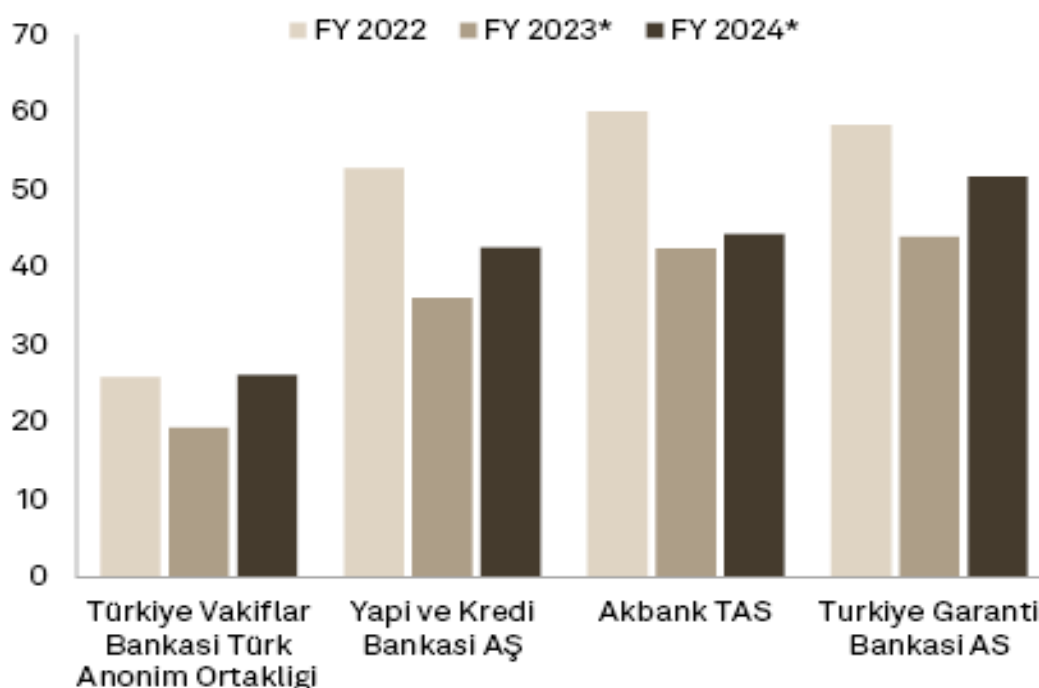


Figure 3. Net Profit of Major Turkish Banks, 2022–2024 (in billion Turkish liras)

As illustrated in Figure 3, the profitability of Turkey's leading banks demonstrated a notable upward trend in 2022, reflecting the sector's strong post-pandemic recovery and favorable interest rate environment. However, by 2023, a downward tendency in net profits became evident, largely attributable to rising inflation, currency depreciation, and tightening global financial conditions. Despite these challenges, the first half of 2024 shows signs of gradual improvement, suggesting cautious optimism for a recovery in profitability in the medium term.

The decline in profitability during 2023 can be primarily linked to the devaluation of the Turkish lira, which significantly increased foreign-exchange-related expenses and affected banks' net interest margins. The volatility of the exchange rate also created uncertainty in financial markets, compelling banks to adopt more conservative lending and investment policies. These developments highlight the importance of incorporating macroeconomic and external risk factors into the decision-making process for managing profitability and ensuring financial stability.

Key Findings and Policy Recommendations

Based on the analysis of Turkey's banking system and profitability trends, the following scientific conclusions and recommendations have been formulated:

1. Strengthening the financial autonomy of state-owned banks.

Enhancing managerial and financial independence, along with reinforcing capital adequacy ratios, is crucial to improving the resilience and long-term profitability of state banks.

2. Continuous assessment of return on assets and equity.

Regular evaluation of asset and capital profitability enables the identification of emerging risks and helps in adjusting financial strategies promptly. Maintaining a comprehensive monitoring framework for factors influencing profitability—such as credit quality, cost efficiency, and liquidity—is essential.

3. Stabilizing macroeconomic conditions.

Policymakers should focus on mitigating excessive exchange-rate volatility and controlling inflationary pressures, as these factors directly influence the profitability and stability of the banking system. Measures aimed at preventing the overheating of the currency depreciation cycle would contribute to sustainable financial performance.

CONCLUSION AND RECOMMENDATIONS

In conclusion, ensuring the profitability of banks requires a systematic approach to identifying and managing both internal and external factors that affect financial outcomes. Developing adaptive financial management strategies based on the analysis of these determinants is essential for achieving stable profitability.

Overall, numerous studies have emphasized that systematizing the factors influencing bank profitability plays a decisive role in strengthening financial stability. International experience demonstrates the importance of distinguishing between internal factors—such as capital structure, risk management, and operational efficiency—and external factors—including macroeconomic indicators, exchange-rate dynamics, and inflation trends. For countries like Uzbekistan, where the banking sector is undergoing rapid transformation, adopting this multidimensional analytical framework can significantly enhance the effectiveness of profitability management and contribute to long-term financial resilience.

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