



**National Bank
of the Kyrgyz Republic**

**THE FINANCIAL SECTOR
STABILITY REPORT OF THE
KYRGYZ REPUBLIC**

according to the results of 2020

June 2021

Bishkek

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Due to rounding of numbers, mismatch in the last number position is possible when summing up.

Other Publications of the National Bank of the Kyrgyz Republic

Annual Report of the National Bank of the Kyrgyz Republic

This publication is a complete report on the activity of the National Bank for the previous year. It contains assessment of changes in the real, financial and external sectors of economy, the description of decisions and actions of the National Bank in the monetary sphere, in the banking and payment systems, in the non-banking financial-credit organizations; it includes financial statements and general information on the National Bank, as well as the statistical appendices. It is published in the state, official and English languages.

Bulletin of the National Bank of the Kyrgyz Republic

The publication contains the statistical data on key macroeconomic and financial indicators of the Kyrgyz Republic. It is published on the official website of the National Bank in the state, official and English languages.

Monetary Policy Report

The Report informs the public of the decisions made by the National Bank in the monetary policy area based on the analysis and forecast of the key inflation factors and assessment of the economic development in the external and internal environment of the Kyrgyz Republic. It is published on the official website of the National Bank in the state, official and English languages.

Balance of Payments of the Kyrgyz Republic

The publication describes the recent development trends in the external sector and contains the data on the balance of payments, external trade, international reserves, external debt, and the international investment position, as well as the metadata and the information base to draw up the balance of payments. It is published quarterly - in February, June, August, and November in Kyrgyz, Russian and English languages.

Regulatory Acts of the National Bank of the Kyrgyz Republic

These are the regulations, instructions and other regulatory legal acts adopted by the National Bank of the Kyrgyz Republic. The estimated frequency of the journal publication is once a month in the state and official languages.

The publications of the National Bank are distributed according to the approved list, and are also posted on the official website of the National Bank at: www.nbkr.kg/Publications.

CONTENT

PREAMBLE	6
MAJOR CONCLUSIONS	8
I. MACROECONOMIC AND FINANCIAL ENVIRONMENT	9
1.1. Macroeconomic Conditions and Risks	9
1.2. Structure of the Financial Sector.....	16
1.3. Financial Markets	18
1.4. Real Estate Market.....	20
II. BANKING SECTOR	26
2.1. Major Trends of the Banking Sector.....	26
2.2. Banking Sector Risks	29
2.2.1. <i>Credit Risk</i>	29
2.2.2. <i>Liquidity Risk</i>	36
2.2.3. <i>Concentration Risk</i>	37
2.2.4. <i>Currency Risk</i>	38
2.2.5. <i>Interest Rate Risk</i>	40
2.2.6. <i>“Contagion” Risk</i>	41
2.2.7. <i>Country Risk</i>	42
2.3. “Reverse” Stress Testing of the Banking Sector.....	44
2.3.1. <i>“Reverse” Stress Testing of Credit Risk</i>	44
2.3.3. <i>“Reverse” Stress Testing of Market Risk</i>	46
III. NON-BANKING FINANCIAL-CREDIT ORGANIZATIONS	47
3.1. Main Trends.....	47
3.2. Risks of Non-banking Financial-Credit Organizations.....	50
3.3. Stress Testing of NBFCOs Sector.....	54
IV. PAYMENT SYSTEMS	56
V. IMPROVEMENT OF THE BANKING SECTOR REGULATION	60
GLOSSARY AND ABBREVIATIONS	65
LIST OF ABBREVIATIONS	66

PREAMBLE

National Bank of the Kyrgyz Republic has been publishing the Financial Sector Stability Report of the Kyrgyz Republic since 2012. The objective of the Report is to inform the public on the general assessment of the stability and soundness of the financial system of the Kyrgyz Republic.

Financial Stability in this publication means smooth and continuous functioning of financial institutions, financial markets and payment systems enabling to perform functions of the financial intermediation even in conditions of financial imbalances and shocks.

Results of the monitoring and analysis of financial stability are considered by the National Bank in forming the main directions of the National Bank's monetary policy, regulating the banking activity and development of the strategy for financial-credit organizations of the Kyrgyz Republic.

The Financial Sector Stability Report of the Kyrgyz Republic is oriented to financial market participants and the audience interested in the financial stability issues.

LIST OF BOXES

Box 1. Housing Affordability Index.....	24
Box 2. Stress Testing of Impact from Price Changes in the Real Estate Market on the Banking Sector ..	25
Box 3. The Survey Results of the Commercial Banks Clients	33
Box 4. Results of the Survey of the Commercial Banks' Largest Clients.....	34
Box 5. Credit and Currency Risks	39
Box 6. Concentration Indices based Assessment of NBFcos Sector Activity	52

MAJOR CONCLUSIONS

In 2020, the large-scale spread of the COVID-19 disease resulted in a sharp revision of the prospects for the world economic development downwards. Many industries were affected in many countries in the unfavorable pandemic environment due to disruptions in the supply chains and a decrease in demand resulted from quarantine restrictions. There was a sharp increase in volatility in the financial and commodity markets, which resulted in pressure on the national currencies exchange rates in the developing countries and on inflation. Support from the governments and the central banks in many countries around the world contributed to stabilization of the situation in the global financial markets through the monetary and fiscal measures.

The COVID-19 pandemic conditioned the slowdown of economic activity in our country. Necessary measures taken by the trading partner countries and the Government of the Kyrgyz Republic to prevent the spread of coronavirus infection, which resulted in a reduction of economic activity in the country, were the main factors of the economic recession.

In order to mitigate the negative economic consequences of the spread of COVID-19 for the population and the financial-credit organizations, the National Bank adopted a number of regulatory measures aimed at ensuring uninterrupted provision and protection of the financial services consumers' rights.

The National Bank monitored the situation and timely regulated the activities of the financial-credit organizations. Banking services were provided in full and in compliance with the sanitary standards. Certain risks for the banking sector were still observed, but their level was within acceptable limits and did not pose a threat to stability for the entire financial sector.

The level of risks was generally minimal in the systemically important and significant payment systems due to the risk management mechanisms provided for by the legislation of the Kyrgyz Republic and the payment systems rules, the current high level of liquidity, the system of insurance deposits and prepayment, as well as individual decisions of the emergency operations center under the National Bank on the emergency situation/the state of emergency to ensure uninterrupted operation of the payment systems in the epidemiological situation.

I. MACROECONOMIC AND FINANCIAL ENVIRONMENT

1.1. Macroeconomic Conditions and Risks

At the end of 2020, there was an acceleration in the inflation rate influenced by a number of non-monetary factors amid various shocks from the domestic demand and the external sector, which conditioned an increase in food prices.

In the reporting period, there was a negative dynamics of economic activity due to the spread of the COVID-19 pandemic and the restrictive response measures introduced by the Government of the Kyrgyz Republic and the partner countries to prevent the spread of the coronavirus infection. The tense socio-political situation in Q4 had an additional negative impact on the country's economy.

External Conditions

In 2020, the global spread of the COVID-19 disease resulted in a sharp revision of the prospects for the world economic development towards the worsening. The pandemic has affected a wide range of industries in many countries due to disruption to the supply chains and decrease in demand resulted from quarantine restrictions. Subsequently, the world experienced a sharp increase in volatility in the financial and commodity markets, which resulted in pressure on the national currencies exchange rates in the developing countries. At the same time, the urgent introduction of large-scale monetary and fiscal support measures by the governments and central banks of the world's largest countries contributed to some stabilization of the situation in the global financial markets.

In 2020, the economy of Kazakhstan was formed under the influence of the negative external and internal economic conditions. Unprecedented decrease in prices in the world oil market, which conditioned a sharp decline in oil production in Kazakhstan, was the main external challenge for the country amid dependence of the economy on the oil and gas market. The quarantine measures introduced due to the coronavirus pandemic and the subsequent slowdown in economic activity, affecting somehow almost all sectors, was the internal challenge. As a result, GDP of Kazakhstan decreased by 2.6 percent at the end of 2020. The National Bank of Kazakhstan kept the policy rate unchanged at 9.00 percent due to increased inflationary pressure and increased risks of further growth in food prices.

China was the only global power to demonstrate economic growth by 2.3 percent in 2020. Economy in China has escaped recession and has achieved a relatively rapid economic recovery due to a series of the government stimulus measures to revive economic activity, as well as strict isolation and population tracking policy focused on restraining the virus spread. However, despite the positive dynamics of economic recovery, there are risks and uncertainties in the Chinese economy due to tension with the United States and recession in its economy, which is China's largest export market, as well as closure of almost all world economy, where an increase in new cases of the coronavirus infection is still recorded.

The impact of COVID-19 on the economy in Russian was large-scale and was reflected on deterioration of the external economic conditions (decrease in demand and oil prices), introduction of the restrictive measures and a decrease of economic activity in Russia. The Bank of Russia continued to reduce the key rate from 6.25 to 4.25 percent per annum amid the pandemic. The fiscal and monetary measures taken in the country to combat the consequences of the crisis resulted in slight economic recovery in the second half of 2020. In turn, the international experts expect GDP growth recovery in the country in the medium term, based on the signs of resumed global economic growth and an increase in oil prices.

Internal Conditions

Gross Domestic Product

In 2020, a significantly deteriorated external environment, along with the internal political challenges, influenced the economy of the Kyrgyz Republic. Necessary measures taken by the trading partner countries and the Government of the Kyrgyz Republic to prevent the spread of coronavirus infection, which resulted in a decrease of economic activity in the reporting year, starting from March, and the tense political situation in the country in the second half of the year were the main factors of economic slowdown. Finally, at the end of 2020, the rate of GDP reduction constituted (-) 8.6 percent compared to the corresponding period of the last year (in January-December 2019, the growth was 4.6 percent).

In the reporting period, the production output growth rate at Kumtor was in the negative zone and constituted (-) 4.8 percent compared to 11.5 percent in 2019. Excluding enterprises for the development of gold mining “Kumtor”, GDP decreased by 9.0 percent (in January-December 2019, an increase by 4.1 percent). The GDP deflator increased by 1.9 p.p. compared to the same indicator in January-December 2019 (3.9 percent) and was formed positive at 5.8 percent.

Such sectors of the economy as trade (-2.8 p.p.), construction (-1.5 p.p.), industry (-1.4 p.p.) and transport (-1.2 p.p.) made the most negative contribution to the economic slowdown.

The decline in the sector of trade by 15.7 percent compared to January-December 2019 was due to a reduction in the volume of wholesale (18.4 percent) and retail (15.4 percent) trade.

Gross construction output decreased by 15.9 percent amid a reduction of investments in fixed capital compared to January-December 2019 from the internal (by 18.9 percent) and external (by 38.8 percent) sources of financing. There was a decrease in the volume of fixed capital investments in the construction of objects of all types of economic activity, except for healthcare.

Decrease in industrial production output by 7.5 percent compared to January-December 2019 was due to a reduction in the production output of petroleum products, textile products, clothes and footwear, leather and leather products, wood and paper products, in printing activities, etc. At the same time, there was an increase in production of the pharmaceutical and chemical products.

The transport sector demonstrated a significant downward trend of 30.9 percent at the end of 2020, conditioned by introduction of the restrictive measures that complicated the internal and external transport communication.

At the end of 2020, agriculture was the only sector with positive growth, having slightly increased by 1.1 percent compared to 2019 due to an increase in livestock production (by 2.0 percent).

Table 1.1.1. Contribution of Individual Activities in GDP

	2019			2020		
	Share, percent	Growth rate, percent	Contribution in growth, p.p	Share, percent	Growth rate, percent	Contribution in growth, p.p
GDP	100	4.6	4.5	100	-8.6	-8.6
Agriculture, forestry and fishery	11.7	2.5	0.3	13.5	1.1	0.1
Industry	19.0	6.6	1.2	21.2	-7.5	-1.4
<i>Mining</i>	1.9	22.2	0.2	1.6	-22.4	-0.4
<i>Processing sectors (Processing industry)</i>	14.7	7.8	1.1	17.0	-7.2	-1.1
<i>Provision (supply) of electric energy, gas, steam and conditioned air</i>	2.2	-3.7	-0.1	2.3	2.7	0.1
<i>Water supply, waste treatment and processing, receipt of recyclable materials</i>	0.2	-3.8	-0.01	0.2	-2.1	-0.00
Construction	9.5	10.7	1.0	8.3	-15.9	-1.5
Services	46.5	3.2	1.5	46.2	-10.0	-4.7
<i>Wholesale and retail trade; repair of cars and motor-cycles</i>	17.6	5.9	1.1	16.2	-15.7	-2.8
<i>Transportation activity and storage of cargo</i>	4.0	4.2	0.2	3.0	-30.9	-1.2
<i>Information and communication</i>	2.7	-0.5	-0.01	2.7	-3.9	-0.10
<i>Other</i>	22.3	1.2	0.3	24.4	-2.6	-0.6
Net (exclusive of subsidies) taxes on products	13.3	4.6	0.7	10.8	-8.6	-1.1

Source: NSC KR

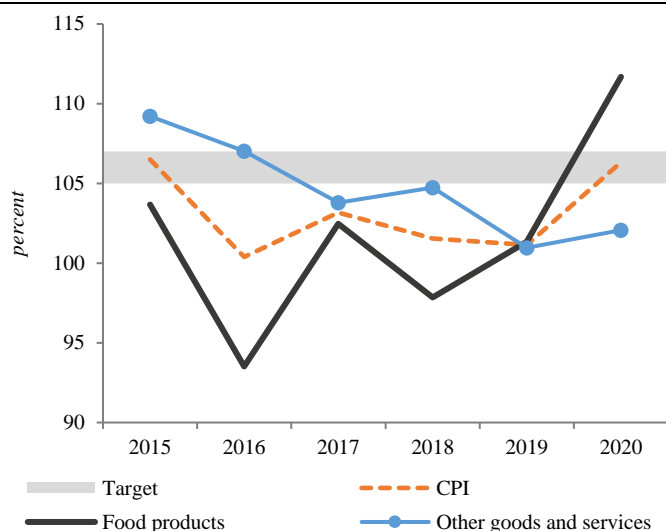
Inflation

In general, the formation of the current inflation in the country was mainly due to the influence of non-monetary factors: the consequences of the introduced restrictions due the spread of the COVID-19 disease. This caused an increase in prices for imported food products, a global trend of the US dollar strengthening, as well as an increase in prices for certain types of food resulted from rise in prices in the world food markets.

Despite the significant impact of several non-monetary factors on inflation, the National Bank managed to keep the inflation rate within the medium-term targets of the monetary policy. Thus, in 2020, the average annual inflation rate amounted to 6.3 percent, while during the year the annual inflation growth rates varied in the range from 3.2 to 9.7 percent. Market inflation remained moderate and constituted 3.4 percent at the end of 2020. The price index for the non-food commodity group and for paid services in annual terms made an insignificant contribution to the CPI - (+) 0.7 p.p. and (+) 0.5 p.p. accordingly.

In difficult economic and political conditions, the National Bank conducted a policy focused on ensuring price stability and maintaining the sustainability of the financial system in the country. At the same time, the monetary policy instruments of the National Bank were generally aimed at stimulating economic activity.

Chart 1.1.1. CPI in the Kyrgyz Republic (cumulatively year-to-date to the corresponding period of the previous year)



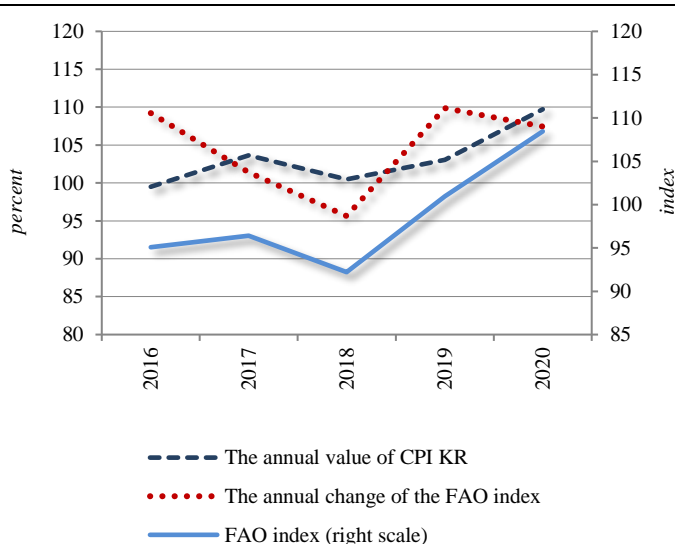
Source: NSC KR

Large volumes of exported meat and livestock from Kyrgyzstan to the neighboring countries influenced the dynamics of prices for meat products.

Formation of the prices for consumer goods and services, exclusive of food products, is relatively stable and is close to the target of the National Bank of 5-7 percent.

Taking into account the aforementioned facts, as well as the situation in the world food markets, in 2021 certain risks of volatility in prices for the main imported food products are expected amid an increase in the world food prices.

Chart 1.1.2. Dynamics of the Kyrgyz CPI and the FAO Index



Source: NSC KR, www.fao.org

The inflation growth was primarily conditioned by a sharp increase in food prices (+17.6 percent) in certain periods during 2020. In 2020, the total increase in prices for the groups “bakery products and cereals”, “meat” and “oils and fats” made more than 60.8 percent of the existing growth in CPI in annual terms. This is due to the influence of supply factors and import prices movement, while the food prices have increased significantly even in the producing countries. Within the commodity group, an increase in prices for meat products had the most significant impact on the growth of the general price level: prices for them increased by 23.3 percent (or input to the CPI + 2.4 p.p.) in annual terms, while they have a relatively large share in the consumer basket.

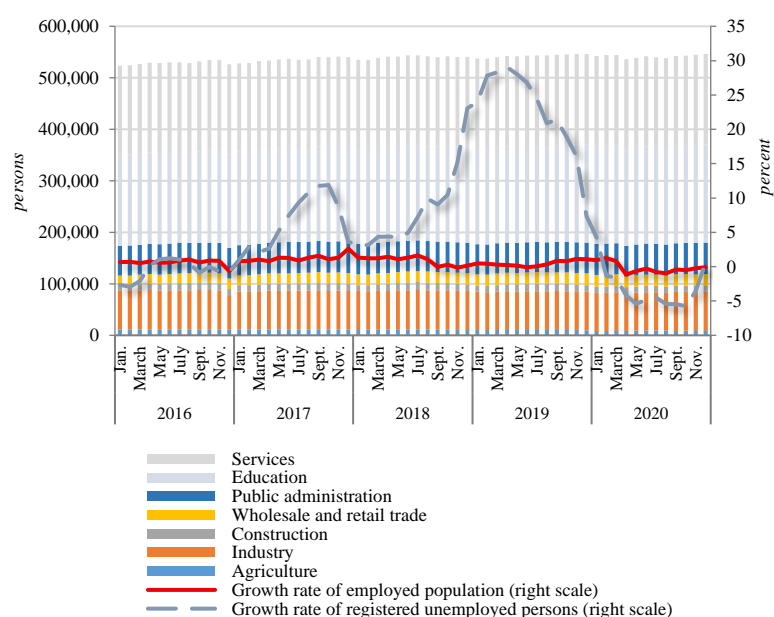
Since the second half of 2020, the FAO index (Food Price Index) has demonstrated an upward trend in prices due to rise in quotations for crops and vegetable oils. The sharp increase in prices for vegetable oils since the second half of 2020 was conditioned by a reduction in supply from the largest producing countries.

In addition, the decline in sunflower harvest in Russia and Ukraine, as well as active demand in the world market, contributed to rise in prices for sunflower oil. During the reporting period, the FAO price index increased for all commodity items, except for meat.

The price indices in the world food markets reached their maximum value during the previous three years, which posed inflationary risks for Kyrgyzstan.

Labor Market and Wages

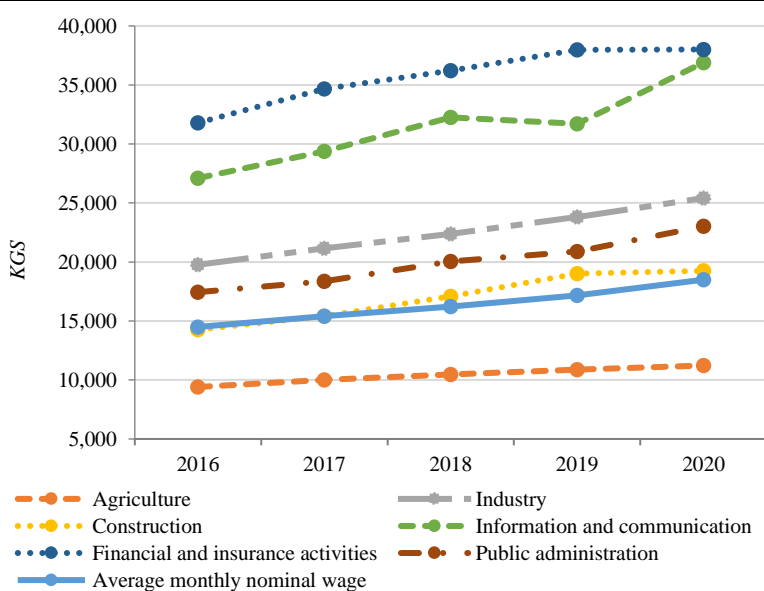
Chart 1.1.3. Number of Officially Employed and Unemployed People



Source: NSC KR

Education (35.0 percent), services (32.1 percent) and industry (13.9 percent) remained the main employment sectors of the able-bodied population. It can be noted that the official data do not indicate that the number of employed population has significantly changed over the past three years.

Chart 1.1.4. Average Monthly Nominal Wages of the Employees at the Enterprises and Organizations by Economic Activity



Source: NSC KR

According to the Ministry of Labor and Social Development of the Kyrgyz Republic, as of January 1, 2021, the number of unoccupied people in search of work registered at the state employment service increased by 4.8 percent compared to the same date in 2019 and amounted to 98.7 thousand people. As of January 1, 2021, the number of registered unemployed people increased by 0.7 percent compared to the same indicator of 2019 and constituted 76.7 thousand people. The registered unemployment rate made 3.0 percent of the economically active population.

In the reporting period, there was a multidirectional growth of wages in the Kyrgyz Republic. At the end of 2020, the average monthly nominal wage per an employee increased by 7.7 percent compared to the same indicator of 2019 and amounted to KGS 18.5 thousand. The largest increase in the average monthly wages growth rate was observed in administrative and support activities (20.0 percent), education (18.8 percent), information and communications (16.3 percent), in water supply, waste cleaning, treatment and receipt of recyclable materials (15.4 percent). In 2020, real wages increased by 1.3 percent compared to the previous year.

State Budget

In 2020, full or partial suspension of the business entities' activities, closure of the land and air borders due to the introduction of the emergency situation and the state of emergency in March-May, as well as the restrictive measures taken due to the threat of the COVID-19 disease spread, had a negative impact on the economy of the Kyrgyz Republic and, accordingly, on the tax and customs revenues to the state budget. The government has twice formed an emergency budget, it became necessary to optimize budget expenditures and direct funds to priority health care expenditures, social protection of the extremely poor citizens and arrangement and conduct of early presidential elections.

A large gap between the government revenues and expenditures conditioned a high level of the state budget deficit, which at the end of 2020 amounted to KGS 19.8 billion or 3.3 percent to GDP (in 2019 – 0.1 percent to GDP). At the same time, in 2020, the budgetary policy made a less noticeable pro-inflationary contribution to price movement compared to expectations, since the budget deficit at the end of the year was lower compared to the forecasts in the approved budget law. This was due to overfulfillment of the non-tax revenues plan and optimization of expenditures, while, according to the Ministry of Finance of the Kyrgyz Republic, all applications received from the state-financed entities for social payments and protected expenditure items were fully funded.

Table 1.1.2. Main Parameters of the State Budget of the Kyrgyz Republic

	Fact				Law*					
	Jan-Dec 2019		Jan-Dec 2020		2020		2021		2022	
	Billion of KGS	% to GDP	Billion of KGS	% to GDP	Billion of KGS	% to GDP	Billion of KGS	% to GDP	Billion of KGS	% to GDP
Total revenues	148.5	24.0	134.7	22.5	139.4	23.9	172.9	27.2	174.2	25.2
<i>of which:</i>										
Tax revenues	105.9	17.1	91.9	15.4	96.9	16.6	127.1	20.0	137.5	19.9
Non-tax revenues	29.1	4.7	30.9	5.2	29.1	5.0	27.7	4.4	25.4	3.7
Grants	13.5	2.2	11.9	2.0	13.4	2.3	18.1	2.8	11.3	1.6
Total expenditures	149.3	24.1	154.5	25.8	169.1	29.0	181.4	28.6	181.3	26.2
Current expenditures	122.4	19.8	133.8	22.4	142.2	24.4	144.9	22.8	145.8	21.1
Capital expenditures	26.9	4.3	20.7	3.5	27.0	4.6	36.4	5.7	35.6	5.1
Deficit(-) / Profit (+)	-0.9	-0.1	-19.8	-3.3	-29.8	-5.1	-8.5	-1.3	-7.1	-1.0

*According to the Law of the Kyrgyz Republic "On introduction of amendments into the Law of the Kyrgyz Republic "On the state budget of the Kyrgyz Republic for 2020 and forecast for 2021-2022" and "On the state budget of the Kyrgyz Republic for 2021 and forecast for 2022-2023"

Source: MF KR

All social obligations were fulfilled through the external borrowings, finally, at the end of 2020, the public debt increased by 27.4 percent compared to 2019 and amounted to KGS 407.1 billion or 68.04 percent to GDP. Taking into account the agreements reached on the temporary suspension (until the end of 2020) of external debt servicing to the main creditor countries due to the coronavirus pandemic and its negative consequences for the economy, KGS 30.7 billion or 5.1 percent to GDP were allocated to repay the public debt.

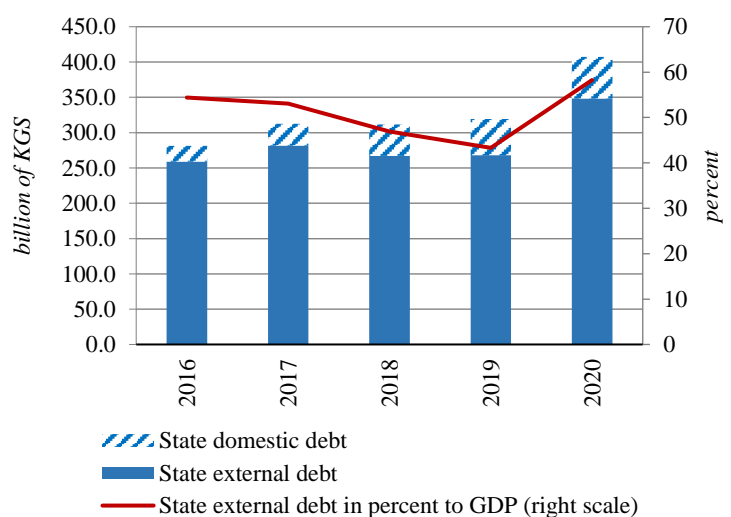
The current fiscal policy, when the government is forced to turn to the donors for financial assistance to fulfill its internal obligations, in the long term may result in an increase in the obligations to repay the public external debt and, accordingly, to an increase in the budget deficit.

Macroeconomic Risks

Severe restrictive measures to prevent the spread of coronavirus disease, taken by the Government of the Kyrgyz Republic since the second half of March 2020, resulted in sharp decline in economic growth until the end of 2020. Macroeconomic risks were still observed until the end of the reporting year due to the tense political situation after the parliamentary elections, amid the current epidemiological situation in the country.

According to forecasts of the National Bank, the inflation rate is expected to accelerate slightly in 2021, however it will remain in single values in the absence of other shocks and an increase in administered prices. Such inflation dynamics will be mainly conditioned by the growth of the world and regional food prices in the first half of 2021 (value in the CPI - 45.4 percent). While in the second half of 2021, the effect of pro-inflationary factors will be exhausted and by the end of 2021, the CPI dynamics in annual terms will be gradually stabilized. The inflation risks associated with the planned increase in excise taxes on the alcohol and tobacco products in the first quarter of 2021 and the discussed increase in tariffs for public transport will affect prices throughout the year.

Chart 1.1.5. Status of the Public Debt



The difficult situation in the labor market and the need to take further fiscal measures to reduce the state budget deficit will prevent from a faster recovery of domestic demand in the near future. A high share of external borrowing is still observed in the structure of public debt. Therefore, the sensitivity of external public debt to changes in the exchange rate of the Kyrgyz som in the future may have a negative impact on the sustainability of public debt.

Source: NSC KR

1.2. Structure of the Financial Sector

Institutional structure of the financial sector in the Kyrgyz Republic is represented by the commercial banks and other financial institutions.

Table 1.2.1. Institutional Structure of the Financial Sector

(number of the financial institutions)

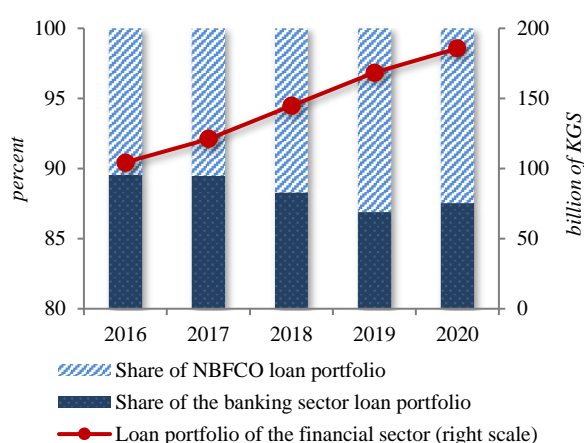
Financial institutions	2016	2017	2018	2019	2020
Commercial banks	25	25	25	24	23
Other financial companies, including:	704	688	695	667	646
Non-banking financial-credit organizations (NBFCO), including:	673	657	664	636	616
Microfinance organizations, including:	162	150	142	137	134
microcredit companies	103	96	95	89	87
microcredit agencies	53	47	39	39	38
microfinance companies	6	7	8	9	9
Specialized Financial-Credit Organization	1	1	1	1	1
Credit offices	0	0	2	2	2
Credit unions	116	110	106	95	92
Exchange offices	394	396	413	401	387
OJSC "Guarantee fund"	1	1	1	1	1
Insurance companies	19	19	19	19	17
Investment funds	9	9	9	9	9
Stock exchanges	1	1	1	1	1
Pension funds	2	2	2	2	2

Source: CBs, NBFCOs, NSC KR

At the end of 2020, assets of the banks and the NBFCOs constituted KGS 317.9 billion or 53.1 percent to GDP.

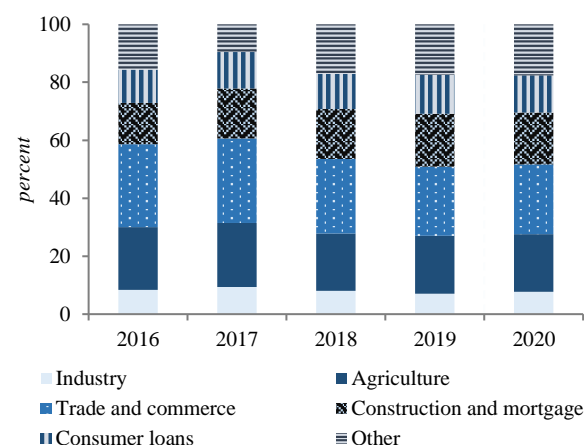
In 2020, the total loan portfolio of the financial sector constituted KGS 185.7 billion or 31.0 percent to GDP. The share of the banks' loans in the loan portfolio of the financial sector increased by 0.6 p.p. and at the end of 2020 made 87.5 percent (Chart 1.2.1).

Chart 1.2.1. Structure of the Loan Portfolio



Source: CBs and NBFCOs

Chart 1.2.2. Sectoral Structure of the Loan Portfolio in the Financial Sector



Source: CBs and NBFCOs

The high concentration of loans was still observed in the trading sector (banks) and agriculture (NBFCOs) within the sectoral structure of the loan portfolio in the financial sector. The aggregate share of the loan portfolio of the financial sector in the aforementioned sectors of the economy at the end of 2020 constituted 44.0 percent of total issued loans and amounted to KGS 81.7 billion (Chart 1.2.2).

1.3. Financial Markets

In 2020, the dynamics of the US dollar exchange rate developed mainly under the influence of negative external economic factors. The effect of external shocks was largely offset by the current freely floating exchange rate, as well as by the National Bank’s interventions, which smoothed significant fluctuations in the US dollar exchange rate against the Kyrgyz som. The volume of operations in the money market decreased significantly compared to 2019. The participants’ activity increased in the longer-term segment in the government securities market. The participants’ activity increased in the context of changes in the external environment and the current internal conditions in the market of the National Bank’s notes.

1.3.1. Currency and Money Market

Currency Market

Chart 1.3.1.1. Dynamics of Interventions of the NBKR in the US Dollar Market

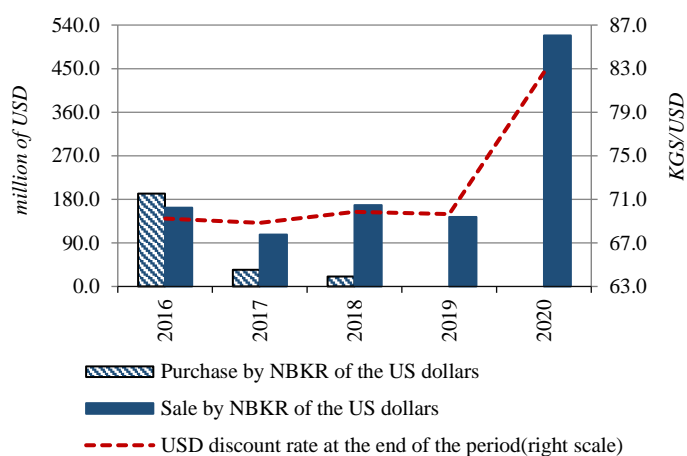
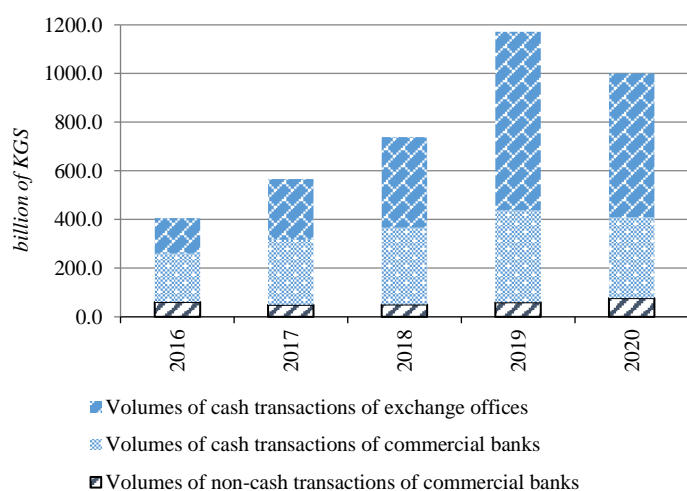


Chart 1.3.1.2. Volume of Purchase and Sale of Foreign Currency by Types of Operations (in KGS Equivalent)



Source: NBKR

The situation in the domestic foreign exchange market and the behavior of its participants largely depended on the external economic situation.

The negative economic consequences of the pandemic were the main reason for the national currency depreciation in the reporting period and were largely conditioned by the reduction in the volume of the foreign economic operations and the volatile environment in the world commodity and financial markets.

In 2020, the US dollar exchange rate against the Kyrgyz som increased by 18.9 percent, from KGS 69.5117 to KGS 82.6498 /USD 1. A similar trend of the US dollar strengthening was observed in the markets of most developed and developing countries. At the same time, the available sufficient stock of international reserves and the possibility to take operative measures by the National Bank through the foreign exchange interventions ensured the ability to maintain a stable situation in the domestic foreign exchange market.

In 2020, the decline in business activity worldwide and in the country was due to a slight decrease in the volume of operations on purchase and sale of foreign currency (-14.5 percent, down to KGS 1,001.2 billion). The volume of operations decreased for all major types of currencies.

Money Market

The money market is a component of the financial market that provides the economy with financial resources for a period of 12 months or less. The money market provides the lenders with the opportunity to receive profit by investing their money, and the borrowers – with the opportunity of flexible liquidity management. Thus, the money market performs the function of efficient distribution of financial resources in the economy. In 2020, activity in the interbank credit market decreased compared to the previous year, and the interest rates increased compared to 2017-2019. The interest rates in the money market are among the factors of their formation in the capital market.

In 2020, the volume of operations in the interbank credit market amounted to KGS 30.1 billion, which is by 23.4 percent lower compared to 2019. In the reporting period, 11 standard operations in foreign currency were conducted in the amount of KGS 1.2 billion, standard operations in the national currency were not conducted, and all other operations were conducted on repo terms. The average weighted rate in the interbank market significantly increased compared to 3.02 percent registered in 2019, up to 3.75 percent. In general, the volatility of rates was generally low and comparable to 2019. The average weighted maturities increased from 4.6 days in 2019 up to 7.0 days in 2020.

The volume of overnight loans provided by the National Bank to support the short-term liquidity of the banks increased by 12 times compared to 2019 and amounted to KGS 3,533.7 million at the end of 2020. The volume of funds placed by the commercial banks on overnight deposits amounted to KGS 1,175.6 billion (+20.4 percent compared to 2019).

1.3.2. Securities Market

During the reporting period, there was a slight decrease in the volume of investment in ST-Bills of the Ministry of Finance of the Kyrgyz Republic compared to the previous year due to the low activity of the participants. The volume of borrowings changed mainly due to the decline in the volume of issued 3- and 6-month securities. The results of auctions showed that the weighted average yield of ST-Bills increased from 5.1 percent in 2019 up to 5.9 percent in the reporting period. The volume of sales, taking into account additional placements, decreased from KGS 5.4 billion in 2019 down to KGS 1.0 billion in 2020.

Operations in the secondary market on ST-Bills purchase/sale were not conducted in the reporting period.

The dynamics of indicators in the ST-Bonds market, on the contrary, indicated existing attractiveness of these assets for the internal and external investors and their desire to reduce the risks in the long term by purchasing these securities with a relatively high yield. In the structure of ST-Bonds circulation, the main holders were the institutional investors, with the share of 56.1 percent.

In addition, during the reporting period, there was a slight increase in the activity of non-residents. The non-residents' demand reflected stabilization of the external investors' expectations. The weighted average yield of ST-Bonds increased up to 11.0 from 10.3 percent in 2019. The rates grew amid a negative situation in the external financial markets and accelerated inflation rate, which resulted in an increase in the cost of funds provided for longer periods. The total sales of ST-Bonds, taking into account additional placements in 2020, increased by 41.1 percent compared to the previous year and amounted to KGS 16.2 billion.

In the reporting period, the participants' operations in the secondary market of ST-Bonds increased by 3.2 times (up to KGS 4.1 billion in nominal terms).

In 2020, the National Bank increased the volume of issued notes to absorb excess liquidity of the banks and prevent stimulation of inflationary processes. Thus, in this market, there was redistribution of the investors' funds in favor of the shorter-term notes of the National Bank. The 7-day notes were primarily in demand, however, it should be noted that the participants' activity in the market of 14-day notes increased significantly, while the volumes of longer instruments remained low. In 2020, the volume of sales of the National Bank's notes increased by 2.1 times, up to KGS 276.7 billion.

1.4. Real Estate Market

At the end of 2020, there was an increase of the price index¹ in the real estate market of the Kyrgyz Republic due to the rise in prices for individual houses and apartments compared to 2019.

There was also an increase in the average wage level, which favorably affected the housing affordability index.

Risks to the financial sector from the real estate market remain moderate, which was conditioned by insignificant share of the mortgage loans² in the total loan portfolio of the banks.

At the end of 2020, property price index increased by 4.0 p.p. (up to 13.5 percent), the property basis price index – by 28.1 p.p. (up to 136.0 percent) in the Kyrgyz Republic due to growth in prices for individual houses by 18.0 percent and for apartments – by 9.4 percent compared to 2019.

Chart 1.4.1. Price Index Growth Rate in the Real Estate Market

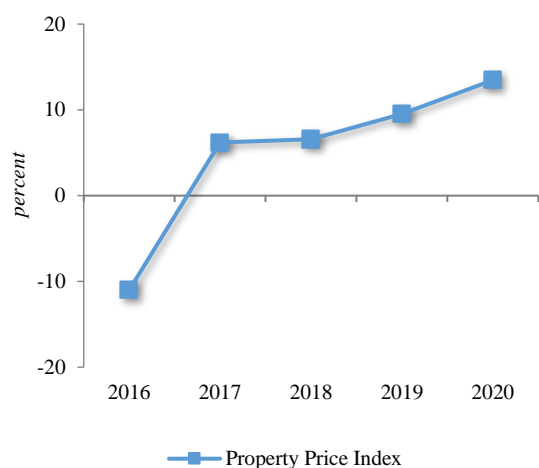
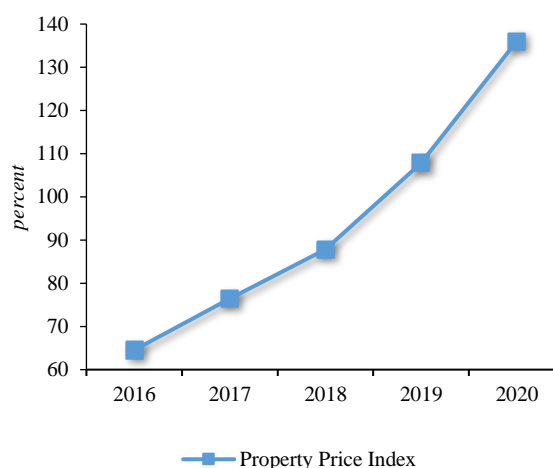


Chart 1.4.2. Basis Price Index Growth Rate in the Real Estate Market³



Source: SALR GKR, NBKR calculations

Source: SALR GKR, NBKR calculations

As of December 31, 2020, the average price for 1 square meter of housing (apartment) in Osh increased by 4.6 percent (up to KGS 37.5 thousand), in Bishkek – by 11.2 percent (up to KGS 55.0 thousand) compared to 2019. The average price for 1 square meter of individual houses in Osh increased by 24.0 percent (up to KGS 66.7 thousand), in Bishkek – by 14.7 percent (up to KGS 57.6 thousand).

In 2020, the number of transactions on the real estate purchase and sale decreased by 17.2 percent and amounted to 39,733. In particular, the number of transactions on purchase and sale of the apartments decreased by 18.7 percent, and the transactions on purchase and sale of the houses decreased by 15.2 percent compared to 2019 and amounted to 21,987 and 17,746, accordingly.

¹ The Laspeyres index method was used in developing price index for the real estate. In general, the Laspeyres index is computed as follows:

$$L = \left(\frac{\sum_{i=1}^K Q_{oi} P_{ti}}{\sum_{i=1}^K Q_{oi} P_{oi}} \right) * 100,$$

where

K = number of real estate types;

Q_{oi} = number of real estate of type i in the base period;

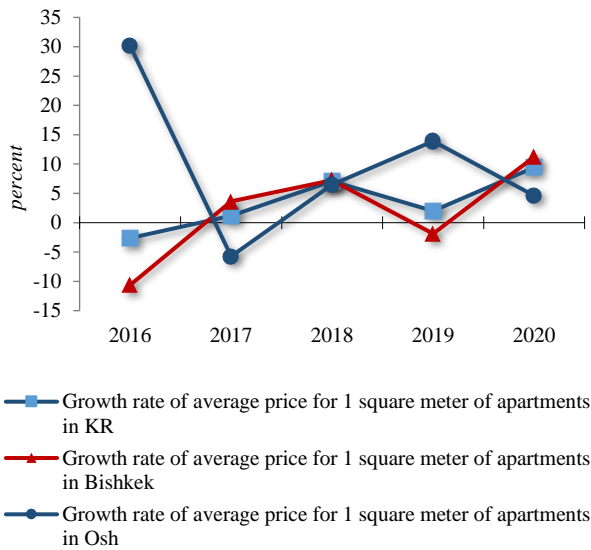
P_{oi} = price of real estate of type i in the base period;

P_{ti} = price of the real estate of type i in the current period.

² Currently, a mortgage loan is usually a long-term loan extended on security of the title to real estate in the Kyrgyz Republic.

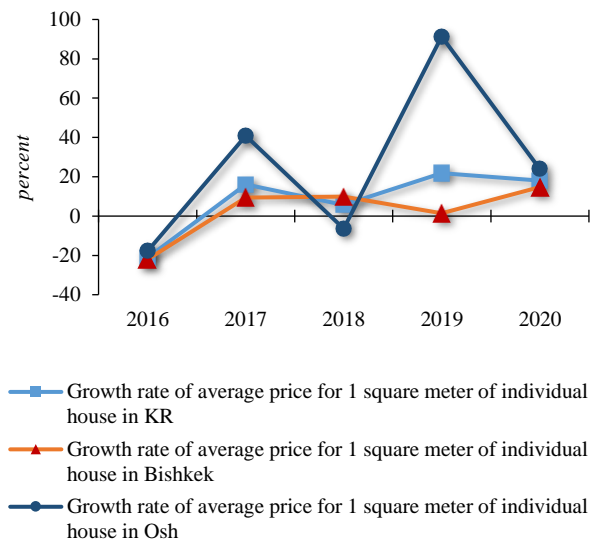
³ The year 2010 was taken as the base period.

Chart 1.4.3. Dynamics of Price Changes for Apartments



Source: SALR GKR, NBKR calculations

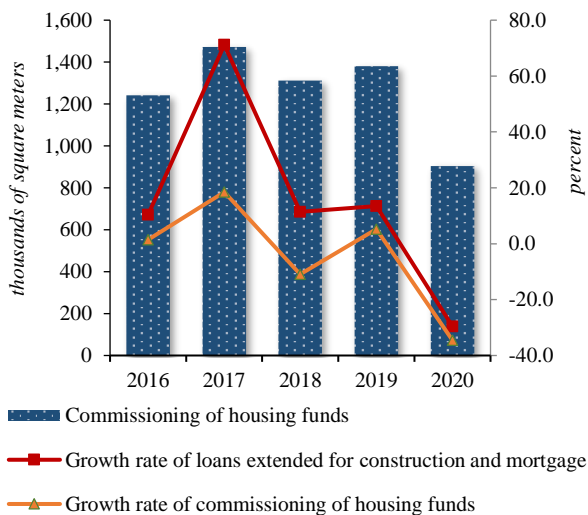
Chart 1.4.4. Dynamics of Price Changes for Individual Houses



Source: SALR GKR, NBKR calculations

There was a decrease in the level of commissioning of housing funds. At the end of 2020, the decrease in the aggregate level of commissioning of housing funds constituted 34.5 percent compared to 2019 due to the reduction in the volume of housing funds commissioning in all regions of the country, exclusive of Issyk-Kul, Naryn and Talas regions (Table 1.4.1).

Chart 1.4.5. Dynamics of Housing Commissioning and Loan Extended for Construction and Mortgage⁴



Source: SALR GKR, NSC KR, NBKR calculations

⁴ Data for the period.

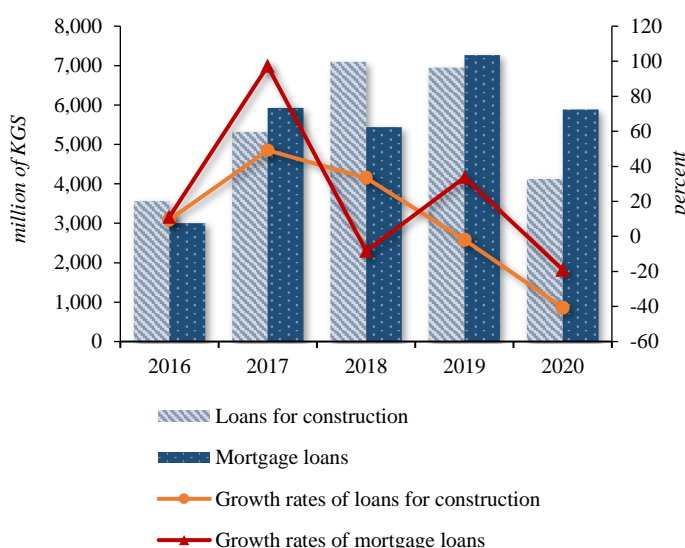
Table 1.4.1. Geographic Structure of Commissioned Housing

	2019		2020	
	<i>Total commissioned area thous. sq.m</i>	<i>Share of total area, %</i>	<i>Total commissioned area thous. sq.m</i>	<i>Share of total area, %</i>
Bishkek city and Chui region	662.4	48.0	305.6	33.8
Osh city and Osh region	265.9	19.3	201.2	22.3
Other regions of KR	451.8	32.7	396.5	43.9
Total	1,380.1	100.0	903.3	100.0

Source: NSC KR

As of December 31, 2020, there was a decrease in the volume of loans extended to finance construction and mortgage loans compared to 2019. So, in 2020, the volume of loans extended for construction decreased by 40.6 percent (down to KGS 4.1 billion), and the volume of mortgage loans - by 19.0 percent (down to KGS 5.9 billion). There was mainly a decrease in the volume of loans issued in foreign currency in the construction sector. There was a decline in the volume of mortgage loans issued in the national and foreign currencies.

Chart 1.4.6. Loans Extended for Construction and Mortgage⁵



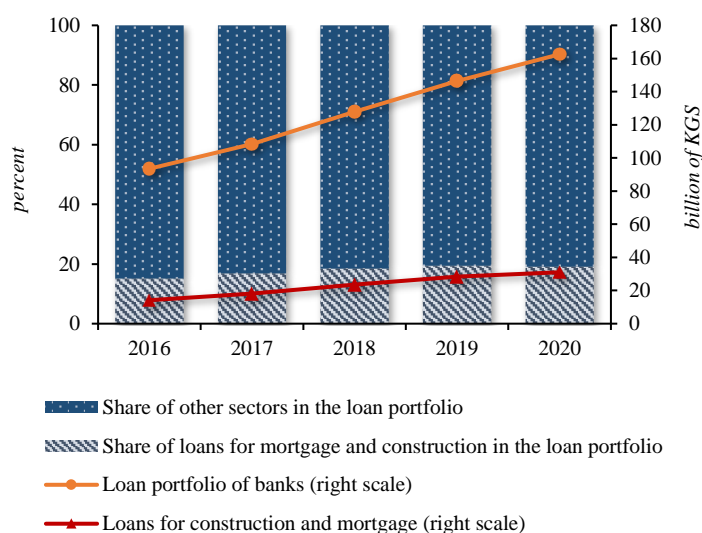
Source: CBs, NBKR

⁵ Data for the period.

At the end of 2020, residential houses are generally constructed and commissioned at the expense of the population (93.6 percent of their total commissioning)⁶.

As of December 31, 2020, the share of loans for construction and mortgages decreased by 0.3 p.p. and amounted to 19.1 percent (Chart 1.4.7) in the total loan portfolio of the commercial banks.

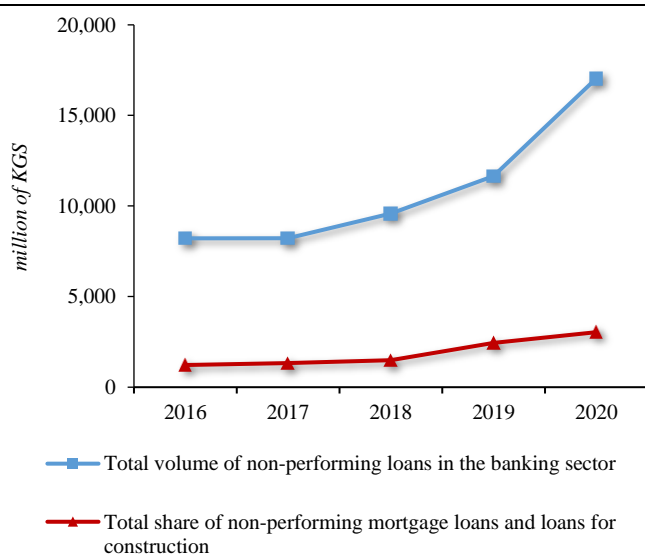
Chart 1.4.7. Total Share of Loans for Mortgage and Construction in the Loan Portfolio of Commercial Banks⁷



Source: CBs, NBKR

The total volume of non-performing loans for mortgage and construction increased by 24.6 percent and amounted to KGS 3,036.1 million. At the same time, in 2020, the aggregate share of non-performing loans for the aforementioned sectors decreased by 3.1 p.p. and amounted to 17.8 percent of the total volume of non-performing loans in the banking sector (Chart 1.4.8). The volume of non-performing loans for mortgage and construction in foreign currency increased by 9.0 percent and amounted to KGS 1,962.9 million.

Chart 1.4.8. Dynamics of Non-performing Loans



Source: CBs

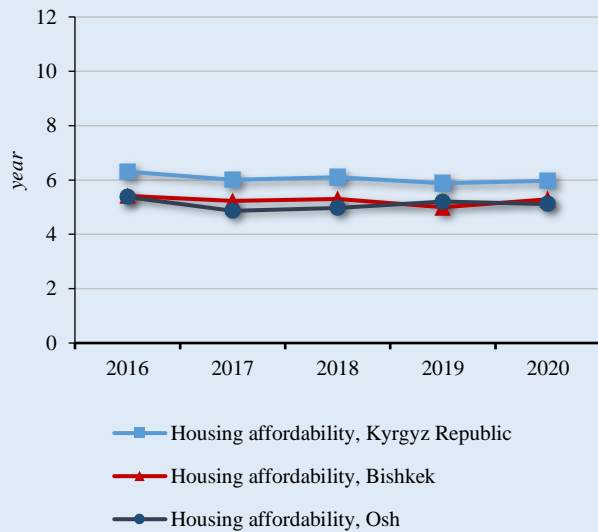
⁶ “Social and economic situation of the Kyrgyz Republic (January-December 2020)”, NSC KR.

⁷ Data as of the end of period.

Box 1. Housing Affordability Index

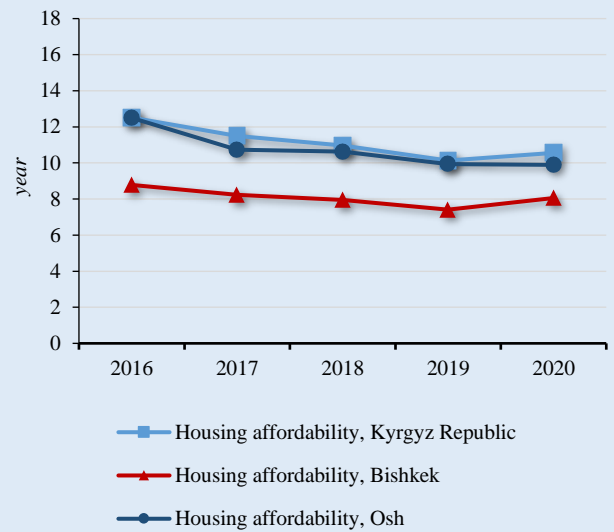
As of December 31, 2020, the level of the housing affordability in the Kyrgyz Republic increased from 5.9 to 6.0 years compared to 2019. This is due to the growth rates of real estate prices (by 9.4 percent) outrunning the growth rates of the average monthly nominal wages (by 7.7 percent) (Chart 1).

Chart 1. Housing (Apartments) Affordability Index without Minimal Consumer Budget



Sources: NSC KR, SALR GKR, NBKR

Chart 2. Housing (Apartments) Affordability Index including Minimal Consumer Budget



Sources: NSC KR, SALR GKR, NBKR

According to the results of 2020, to purchase an apartment of 54 square meters in the Kyrgyz Republic one should save the average monthly nominal wage of the family, where the income is received by two people, for 6.0 years with other conditions being equal.

According to the results of 2020, a family of three people in the Kyrgyz Republic with the minimum consumer budget of KGS 16,075.6 (43.5 percent of the total family income) will need 10.6 years in order to purchase housing (Chart 2).

Box 2. Stress Testing of Impact from Price Changes in the Real Estate Market on the Banking Sector⁸

As of December 31, 2020, the share of loans secured by pledged real estate constituted 34.3 percent of the total number of loans in the loan portfolio of the banks. The volume of pledged real estate (at pledge value) amounted to 73.5 percent of the total collateral for the loan portfolio.

Credit risks for the banking sector are conditioned by possible decrease in the value of pledged real estate below the loan payment balance and further potential refusal of a borrower from loan repayment.

Stress testing is focused on quantitative assessment of possible losses from outstanding loans and identification of the most vulnerable banks (groups of banks).

Scheme 1. Results of Stress Testing of Impact from Price Changes in the Real Estate Market on the Level of Credit Risk of the Banking Sector

Scenario	Potential losses of the banking sector	Potential losses of large banks	Risk of capital adequacy ratio violation
"Historical" scenario* (decrease in price for real estate by 23% per a year)	-----	-----	-----
"Alternative" scenario (decrease in price for real estate by 40% per 2 years)	KGS -6.6 billion	KGS -8.0 billion	3 banks
"Negative" scenario (decrease in price for real estate by 50% per a year)	KGS -21.2 billion	KGS -17.2 billion	5 banks

* At the end of 2008, prices for real estate in Kyrgyzstan decreased by 23 percent.

In addition to stress test, threshold level of decrease in prices for real estate, when banks potentially suffer losses, was calculated. The banking sector potentially suffers losses if prices for the real estate decrease by 33.5 percent, large banks - by 26.8 percent. The risk of capital adequacy ratio violation by the banking sector, as well as by the large banks, arises when prices for the real estate decrease by 53.5 and 43.8 percent, accordingly.

The possible difference in the estimated value of pledged real estate, which may be less than the market value by approximately 20 percent, was not taken into account by the banks in calculations of the stress test. Taking into account aforementioned facts, prices for real estate can decrease by 20 percent.

⁸ Stress test was conducted on the basis of the commercial banks' data provided in the course of the survey as of December 31, 2020.

II. BANKING SECTOR

Growth of the main indicators of the banking sector: assets, capital, deposit base, loan portfolio and indices of financial intermediation was observed at the end of 2020 compared to 2019.

At the end of the reporting period, systemic risks of the banking sector are available and estimated as moderate. The banking sector is characterized by a high level of capital adequacy, indicating the availability of the potential to further increase the level of financial intermediation, efficiency and sustainability of the banking sector in the future.

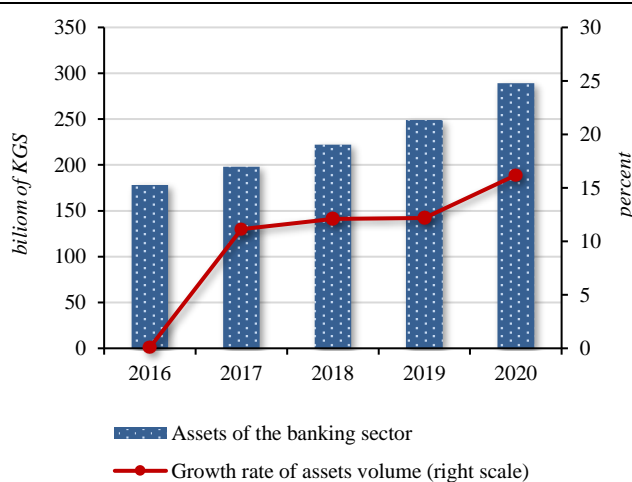
2.1. Major Trends of the Banking Sector

As of December 31, 2020⁹, 23 commercial banks (including the Bishkek branch of the National Bank of Pakistan) and 312 banks' branches worked in the territory of the Kyrgyz Republic, among which there were 16 banks with foreign participation in the capital, including 11 banks with foreign participation in the amount of more than 50 percent. All banking institutions of the country are universal by the type of business.

Assets

Generally, the growth in the volume of the banking sector assets was observed at the end of 2020. Assets of the banking sector amounted to KGS 289.3 billion, having increased by 16.2 percent compared to 2019 (Chart 2.1.1).

Chart 2.1.1. Dynamics of Assets in the Banking Sector



The growth of assets was mainly provided by increase of:

- the loan portfolio by 11.0 percent or KGS 16.1 billion;
- liquidity in the form of cash and cash on correspondent accounts by 23.4 percent or KGS 7.3 billion.

The share of loan portfolio in the structure of assets constituted 56.2 percent, having decreased by 2.6 p.p. compared to 2019.

Source: NBKR

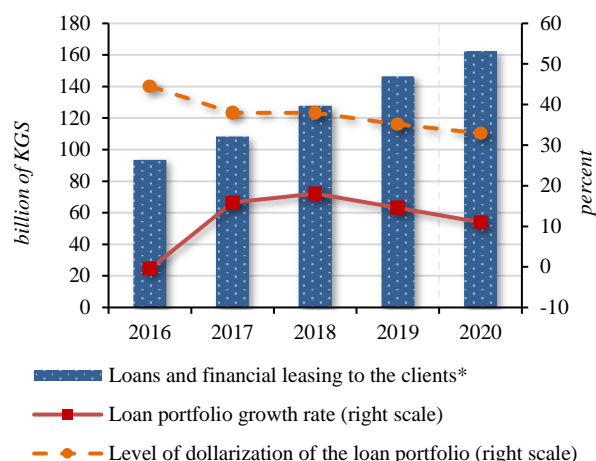
Loan Portfolio

In 2020, growth of the loan portfolio was observed in all sectors of economy.

At the end of the reporting period, the level of dollarization of the loan portfolio in the banking sector decreased by 2.2 p.p. compared to 2019 and amounted to 32.9 percent (Chart 2.1.2).

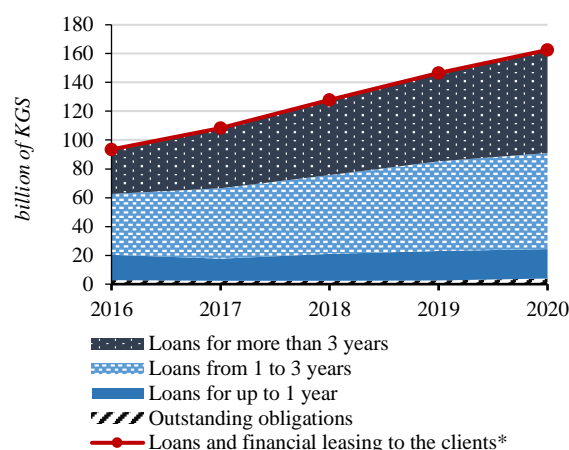
⁹ The data are submitted according to periodic regulatory reporting of the commercial banks (PRBR).

Chart 2.1.2. Dynamics of Loan Portfolio in the Banking Sector



* Exclusive of loans provided by FCO and special loan loss provisions
Source: NBKR

Chart 2.1.3. Structure of Loan Portfolio by Maturity



* Exclusive of loans provided by FCO and special loan loss provisions
Source: NBKR

The major shares were accounted for the long-term loans¹⁰ – 44.1 percent or KGS 71.6 billion, and for the medium-term loans¹¹ extended for 1-3 years – 41.0 percent or KGS 66.6 billion in the structure of loan portfolio by maturity (Chart 2.1.3).

Liabilities

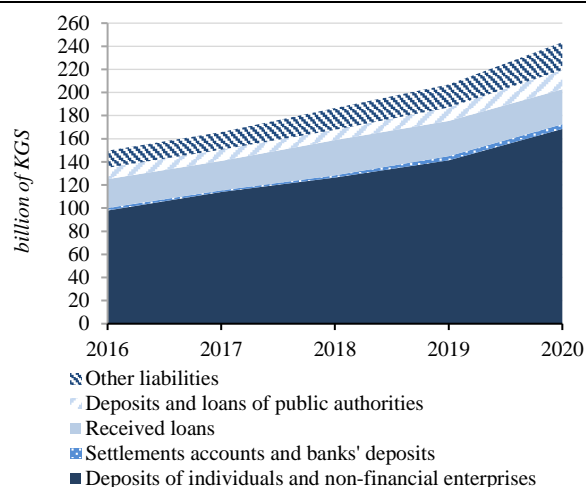
At the end of 2020, liabilities of the banking sector of the Kyrgyz Republic amounted to KGS 243.5 billion, having increased by 17.7 percent compared to 2019.

At the end of the reporting period, deposits of individuals and non-financial enterprises increased by 19.1 percent and amounted to KGS 168.5 billion (Chart 2.1.4). The share of individuals' and non-financial enterprises' deposits in the banks' liabilities increased by 0.8 p.p. and amounted to 69.2 percent.

The share of liabilities in foreign currency in the total volume of attracted funds increased by 2.9 p.p. and amounted to 42.0 percent (Chart 2.1.5).

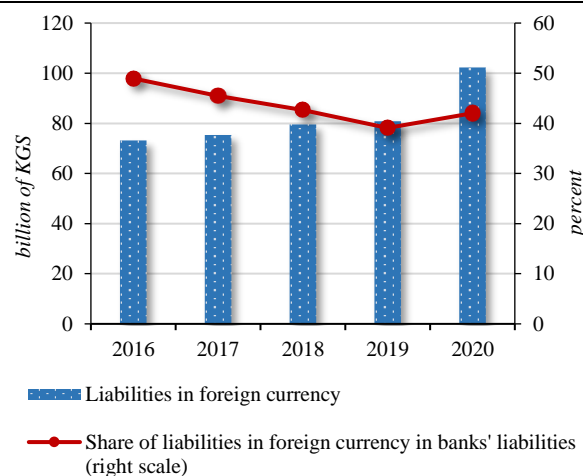
CONTENT

Chart 2.1.4. Structure of Banks' Liabilities by the Reserve Sources



Source: NBKR

Chart 2.1.5. Banks' Liabilities in Foreign Currency



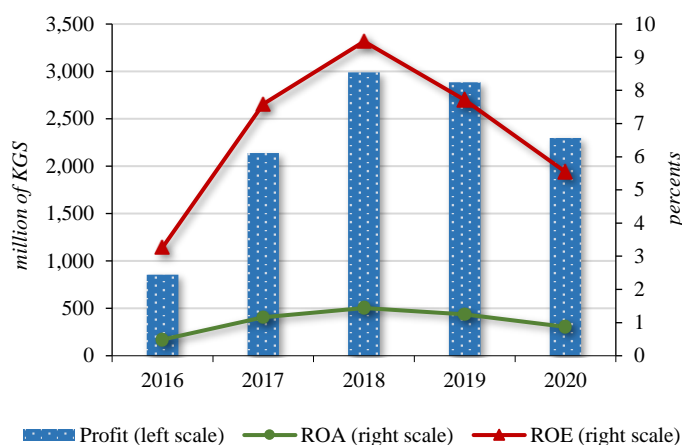
Source: NBKR

¹⁰ Long-term loans are the loans extended for more than three years.

¹¹ Medium-term loans are the loans extended for 1-3 years.

Financial Results

Chart 2.1.6. Profitability Indicators of the Banking Sector



Source: NBKR

The deterioration of profitability indicators in the banking sector at the end of 2020 was observed compared to 2019 due to increase of LLP expenses.

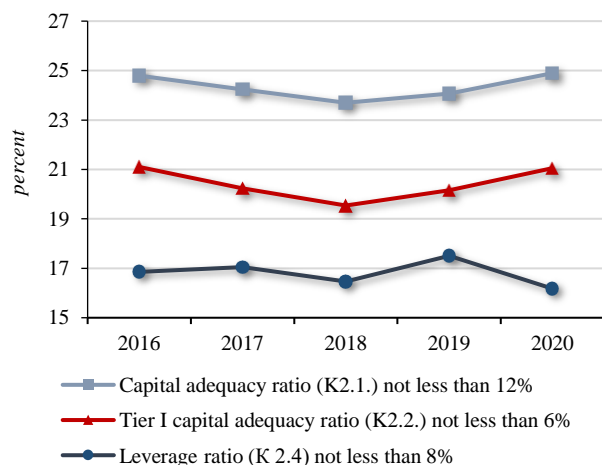
- ROA constituted 0.9 percent;
- ROE formed at 5.5 percent.

Net profit of the banking sector decreased by 20.4 percent and amounted to KGS 2.3 billion (Chart 2.1.6).

Capital Adequacy

With statutory minimum capital adequacy at 12.0 percent, at the end of 2020, this figure amounted to 24.9 percent (Chart 2.1.7), having increased by 0.8 p.p. compared to 2019.

Chart 2.1.7. Dynamics of Capital Adequacy Ratios



Source: NBKR

At the same time, the actual level of capital adequacy in the banking sector, generally formed according to the results of 2020, can further increase the volume of risky and earning assets by two times, without exceeding established level of capital adequacy.

The abovementioned information indicates relative stability of the banking sector to negative shocks and the presence of certain potential to increase the level of financial intermediation and efficiency of the banking sector activity in the future.

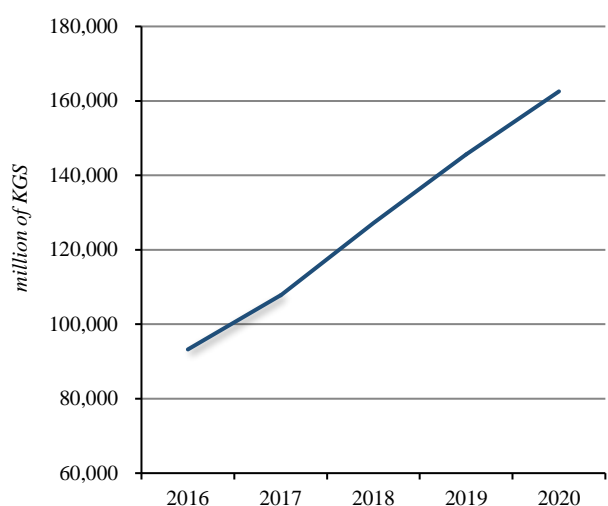
2.2. Banking Sector Risks

2.2.1. Credit Risk

A credit risk is one of the main risks that accompany banking activity.

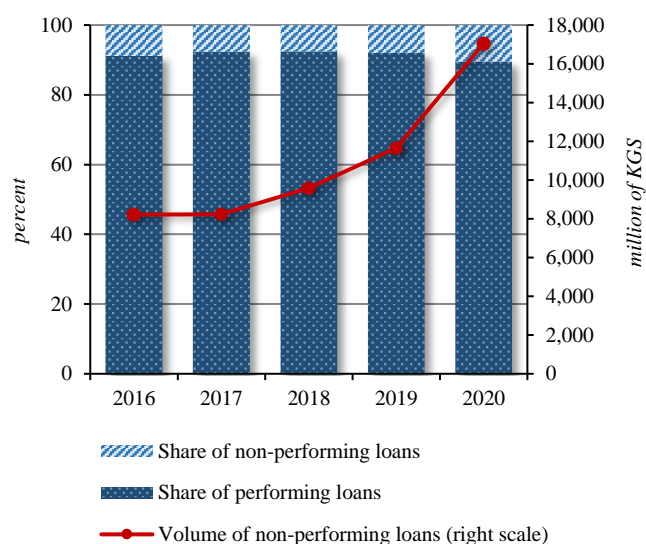
In the reporting period, the share of non-performing loans in the loan portfolio of banks increased from 8.0 percent up to 10.5 percent compared to 2019 (Chart 2.2.2).

Chart 2.2.1. Dynamics of Loan Portfolio



Source: NBKR

Chart 2.2.2. Loan Portfolio Quality

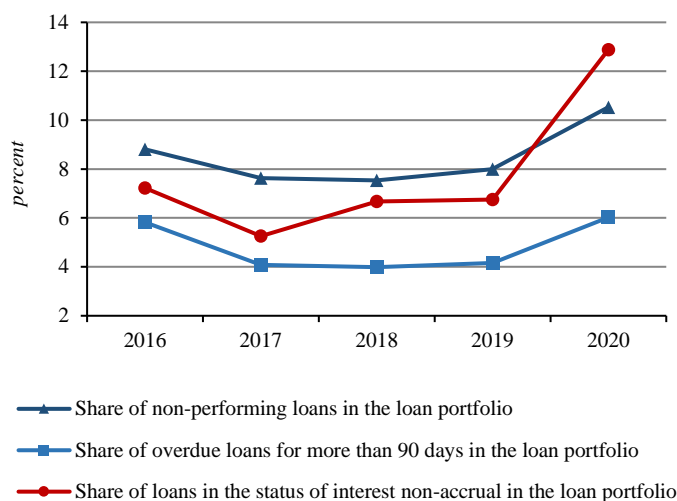


Source: NBKR

In order to assess the quality of the loan portfolio, the commercial banks use a loan classification system, which contributes to determining the possible level of potential losses from bad loans and compensating them in time through creation of appropriate reserves (Chart 2.2.3).

The indicator of the risk of default on assets (the ratio of special loan loss provisions and loan portfolio) increased by 1.7 p.p. compared to 2019 and constituted 6.2 percent.

Chart 2.2.3. Indicators of the Loan Portfolio Quality



Aggregate reserves created by the commercial banks increased by 2.0 p.p. compared to 2019 and constituted 9.0 percent of the total loan portfolio.

Meanwhile, the share of special loan loss provisions in 2020 constituted 69.3 percent of the total reserves (Chart 2.2.4).

Source: NBKR

Chart 2.2.4. Total and Special Reserves

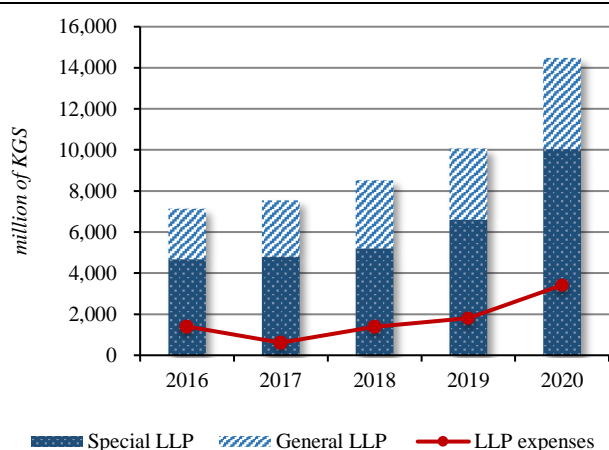
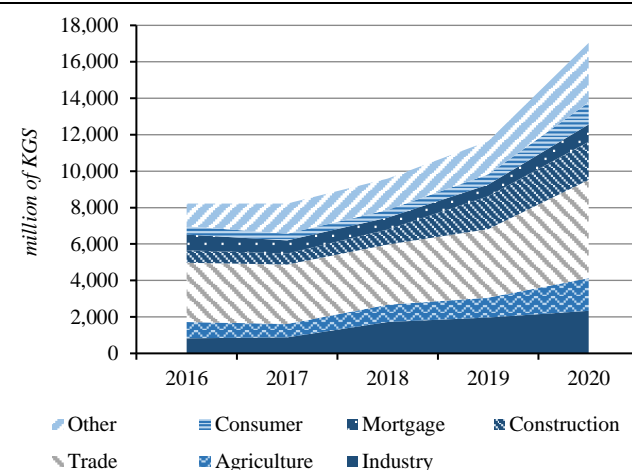


Chart 2.2.5. Volume of Non-performing Loans by Sectors of Economy



Source: NBKR

Source: NBKR

As of the end of 2020, the highest concentration of credit risks was still observed in the trade sector of economy (Chart 2.2.5).

Financial Status of Households¹²

The financial sustainability indicators of households decreased slightly because the growth of population debt to the financial sector outran the growth of their incomes.

As of June 30, 2020, the households' debt ratio to GDP increased from 18.8 percent to 20.1 percent compared to the same period in 2019 (Chart 2.2.6).

Chart 2.2.6. Indicators of Households' Financial Soundness

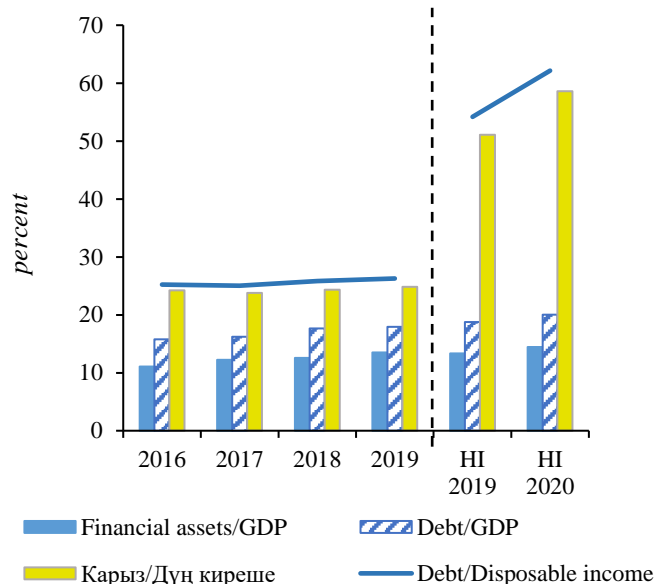
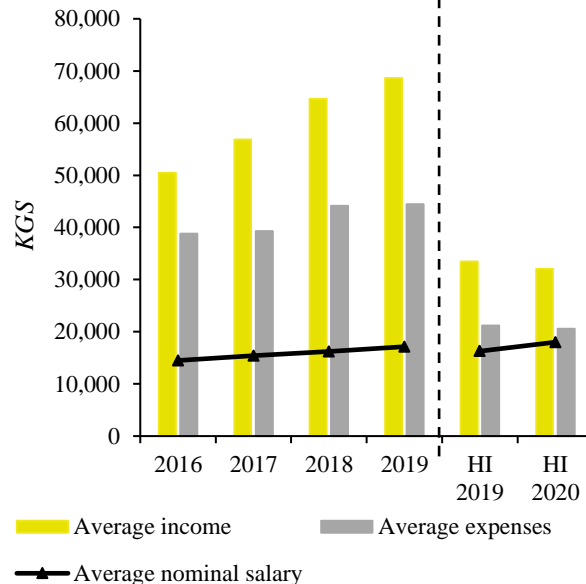
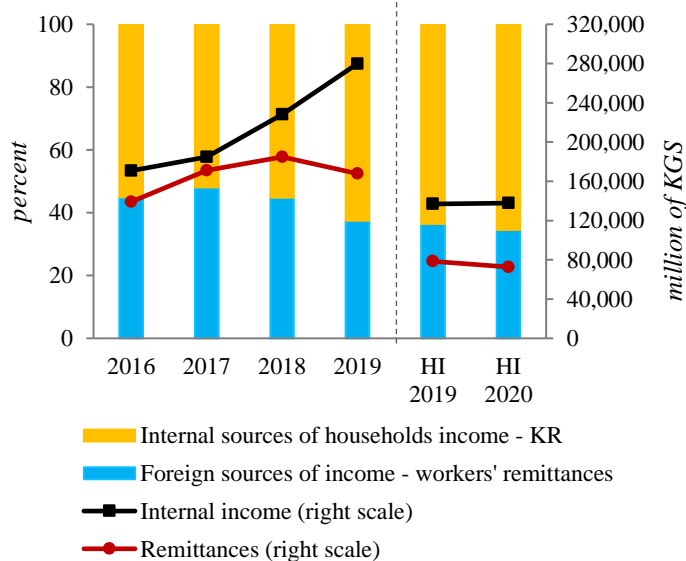


Chart 2.2.7. Factors of Population Balance Financial Soundness



At the end of the first half of 2020, the share of remittances decreased by 1.9 percentage points, down to 34.5 percent of the population gross incomes (Chart 2.2.8). Meanwhile, remittances of migrant workers were still a significant source of household income.

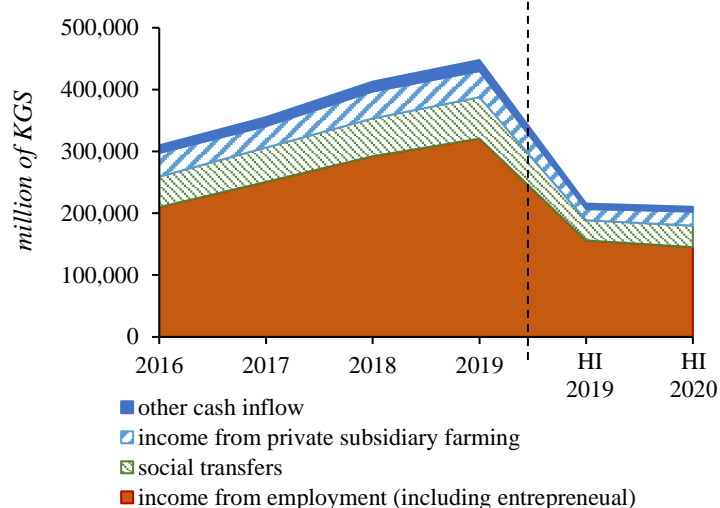
Chart 2.2.8. Structure of Households' Income by Sources



In the first half of 2020, in the structure of households' income, the major share was accounted for labor income, which constituted 69.0 percent of the population gross incomes (Chart 2.2.9).

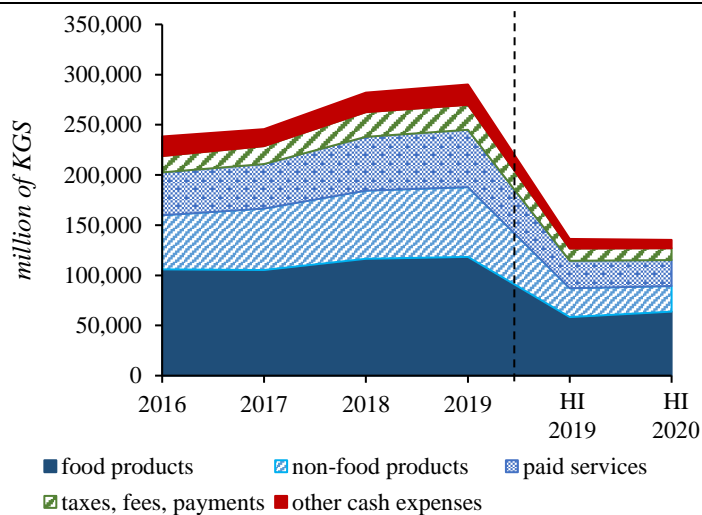
¹² According to the official statistics data of NSC KR based on the random sampling method of households' survey.

Chart 2.2.9. Structure of Households' Income



In the structure of household expenditures, the main share fell on consumption (Chart 2.2.10), which limited the growth of savings and investments.

Chart 2.2.10. Structure of Households' Expenses

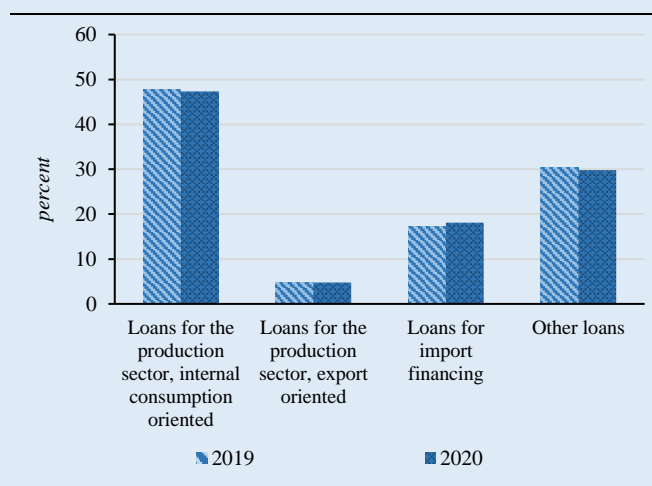


A significant share of consumer expenditures, that constituted 85.1 percent of total expenditures in the first half of 2020, may affect the ability of households to meet their obligations in case of revenue reduction.

Box 3. The Survey Results of the Commercial Banks Clients (Sectoral Structure)

According to the results of the commercial banks survey, at the end of the reporting period, a significant share of extended loans (47.3 percent of total borrowers' loans) was still concentrated in the production sector of the economy¹³, thereby reflecting contribution of the banking sector in creation of the country's GDP, meanwhile, 18.1 percent of issued loans were forwarded for financing of imports (Chart 1).

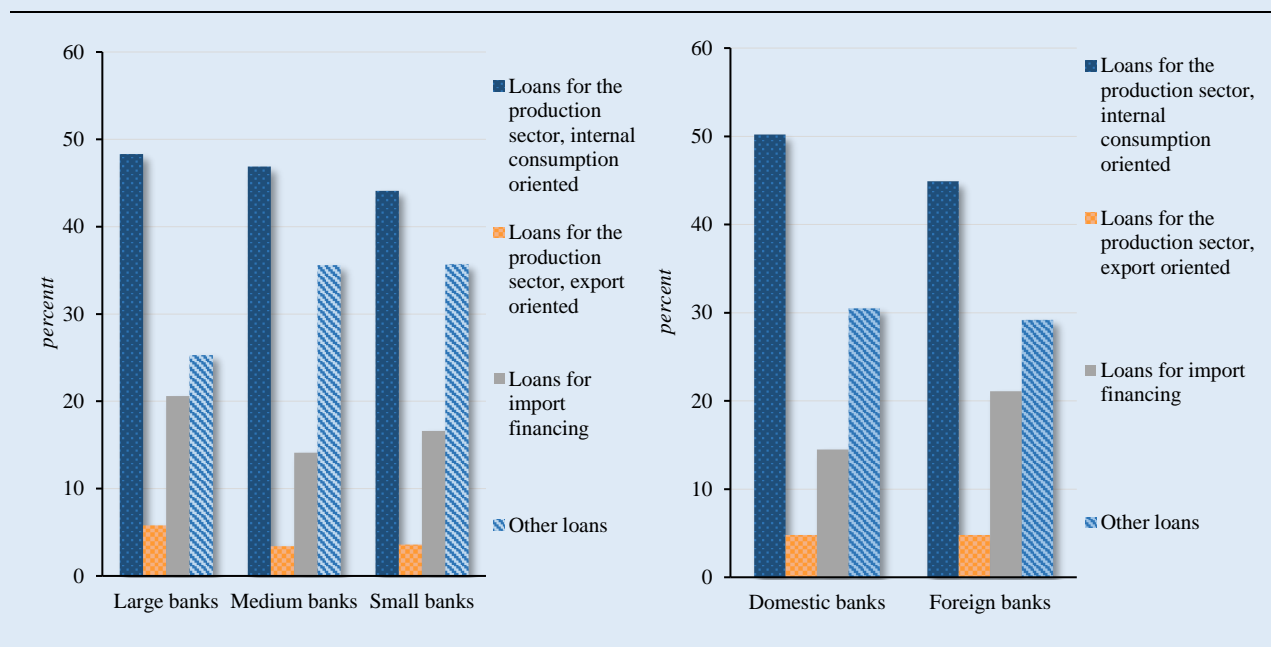
Chart 1. Sectoral Structure of Loans as of December 31, 2020



Source: CBs

Domestic banks forwarded 50.2 percent of the loan portfolio to the production sector (GDP) and 14.5 percent – to finance imports. Generally, foreign banks also provided loans to the production sector of economy (44.9 percent). In 2020, the share of loans forwarded to finance imports constituted 21.1 percent of the loan portfolio (Chart 2).

Chart 2. Sectoral Structure of Loans by the Groups of Banks as of December 31, 2020



Source: CBs

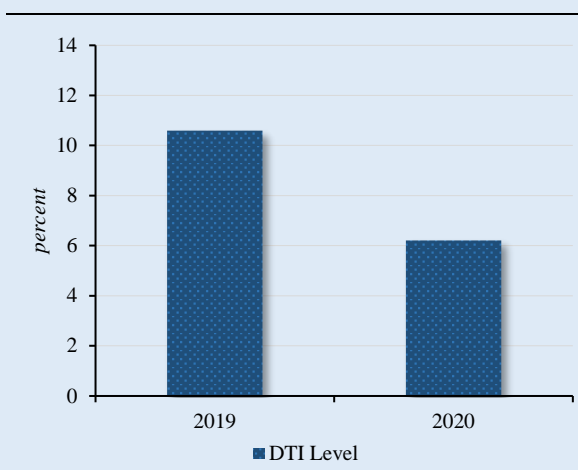
¹³ The production sector means the activity of the bank clients connected with the production of goods and services (construction, communication and automobile repair shop services, transport services, real estate leasing, hotels, restaurants, etc.).

Box 4. Results of the Survey of 15 Commercial Banks' Largest Clients

Borrowers solvency

At the end of 2020, the level of debt burden of 15 banks' largest clients calculated through DTI index¹⁴ increased by 4.4 p.p. compared to the same indicator in 2019 and constituted 6.2 percent.

Chart 1. DTI Level on 15 Banks' Largest Borrowers



Source: CBs, NBKR

By the groups of banks, the largest debt burden was observed in the major borrowers of the *large banks* (8.5 percent of the borrowers' basic income) (Table 1). At the same time, the lowest level of debt burden was observed at the same level in the major borrowers of the medium banks and constituted 3.8 percent.

Table 1. Debt Burden of 15 Banks' Largest Borrowers at the end of 2020

	Banking sector	Large banks	Medium banks	Small banks
Loan balance, <i>billions of KGS</i>	40.8	23.5	8.3	9.0
Share of loans in 15 largest borrowers in the total volume of loan portfolio in the banking sector, <i>in %</i>	24.8	25.6	16.5	39.9
Ratio of expenses for loan debt servicing to the borrowers' total income, <i>in %</i>	6.2	8.5	3.8	5.9

Source: CBs, NBKR

In 2020, the level of debt burden in the foreign banks was higher than in the domestic banks (Table 2).

Table 2. Debt Burden in the Domestic and Foreign Banks at the end of 2020

	Domestic banks	Foreign banks
Loan balance, <i>billions of KGS</i>	17.9	22.9
Share of loans in 15 largest borrowers in the total volume of loan portfolio in the banking sector, <i>in %</i>	23.4	26.0
Ratio of expenses for loan debt servicing to the borrowers' total income, <i>in %</i>	3.0	10.3

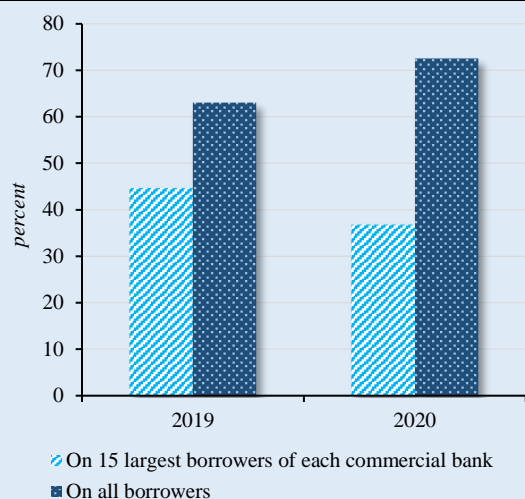
Source: CBs, NBKR

¹⁴ DTI (debt-to-income) is the ratio of the amount of the borrowers' payments on loans (including the amount of principal and interest payments for the reporting period) to the main annual income of the borrower declared at the time of issuing a loan.

Security of the borrowers' loans

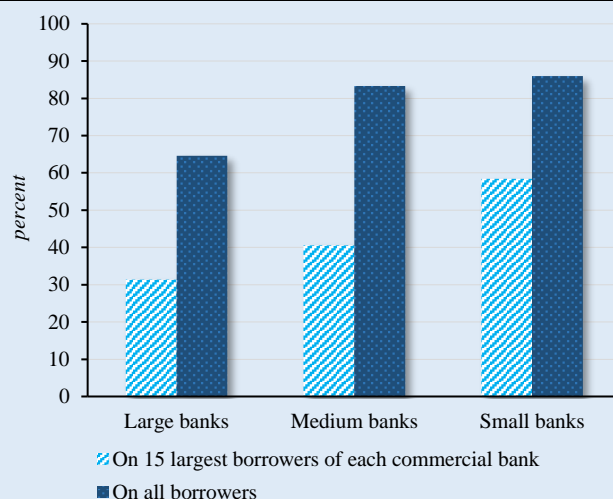
At the end of 2020, the LTV actual level¹⁵ in the banking sector amounted to 72.6 percent. The existing level of collateral indicates a relatively high level of the loans secured by the pledged property (Chart 2).

Chart 2. LTV Level on All Borrowers and on 15 Largest Borrowers of Each Commercial Bank as of December 31, 2020



Source: CBs, NBKR

Chart 3. LTV Level on All Borrowers and on 15 Largest Borrowers by the Banks' Groups as of December 31, 2020



Source: CBs, NBKR

Meanwhile, the LTV value in the large banks is lower than in the small and medium banks and in the banking sector as a whole (Chart 3).

¹⁵ LTV (loan-to-value ratio) is the ratio of issued loans to the value of collateral.

2.2.2. Liquidity Risk

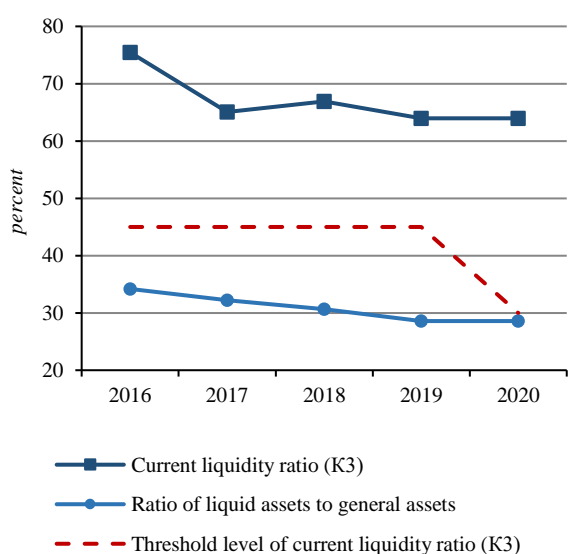
Since April 1, 2020, the National Bank reduced the value of the economic liquidity ratio (K3.1.) from 45.0 to 30.0 percent to maintain the stability of the banking sector due to the spread of coronavirus infection.

In addition, compliance with prudential standards for short-term liquidity (K3.2) and instant liquidity (K3.3) has been temporarily suspended since April 30, 2020.

This measure, along with other decisions of the National Bank, was aimed at the timely fulfillment by the commercial banks of their short-term obligations to the clients.

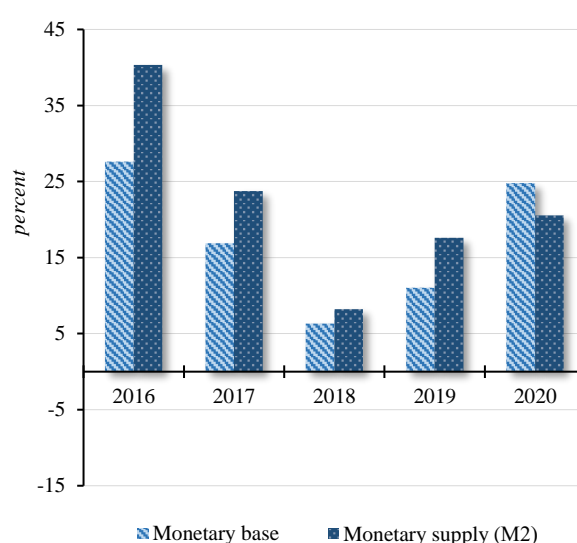
At the end of 2020, current liquidity ratio increased from 64.0 percent (as of the end of 2019) to 64.9 percent (Chart 2.2.11).

Chart 2.2.11. Liquidity Indicators in the Banking Sector



Source: NBKR

Chart 2.2.12. Growth Rates of Money Supply (M2) and Monetary Base



Source: NBKR

Liquidity ratio of the banking sector increased due to excess of liquid assets growth rates over current liabilities.

Table 2.2.1. Maturity of Financial Assets and Liabilities

as of December 31, 2020, millions of KGS

Name	Maturity					Total
	up to 1 month	1-3 months	3-6 months	6-12 months	more than 12 months	
Total financial assets	113,426	12,228	14,019	26,128	139,482	305,284
including loans and financial leasing to the clients	7,016	6,232	9,395	24,155	115,049	161,846
Total financial liabilities	131,926	11,571	21,445	32,099	42,358	239,400
including deposits of individuals and time deposits of legal entities	54,928	7,529	11,392	22,143	19,289	115,282
Gap	-18,500	658	-7,426	-5,971	97,124	65,884
including on loans and deposits	-47,913	-1,297	-1,998	2,011	95,760	46,564

2.2.3. Concentration Risk

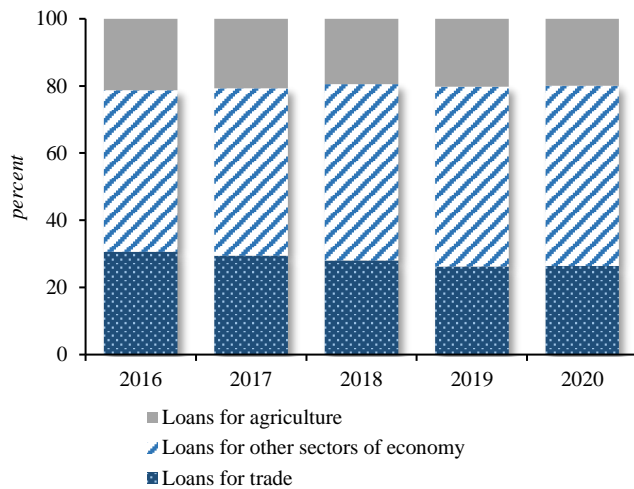
Concentration of the Largest Sources of Financing

The results of “reverse” stress testing show that some banks could not withstand the shock related to outflow from one to five large clients, when the liquidity ratio decreases below the threshold level of 30 percent.

Loan Concentration

Potential default from one to five largest borrowers in separate banks may decrease regulatory capital below prudential standard of the NBKR.

Chart 2.2.13. Sectoral Concentration of the Loan Portfolio



Decrease of the concentration level of loans to agriculture was observed in the sectoral structure of loan portfolio. At the end of 2020, the share of loans issued to finance agriculture decreased from 20.2 percent to 19.9 percent (Chart 2.2.13).

Source: CBs, NBKR

2.2.4. Currency Risk

At the end of 2020, the annual average level of *currency risk* in the banking sector was at a moderate level.

Chart 2.2.14. Dynamics of USD/KGS Nominal Exchange Rate

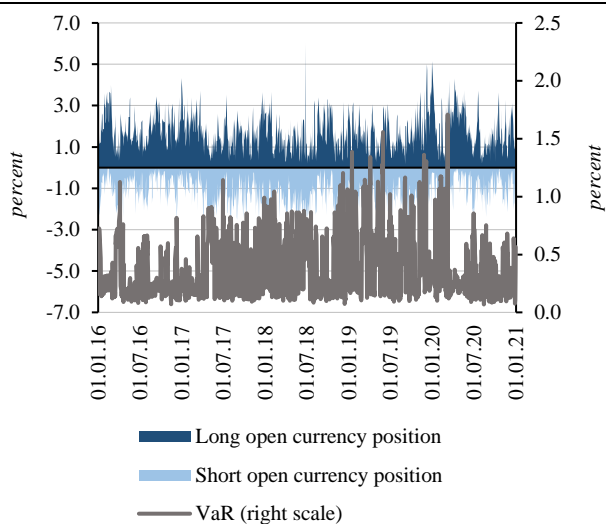


In general, the banks kept open currency positions of assets and liabilities within the limits set by the prudential standards of the National Bank of the Kyrgyz Republic.

In 2020, the risk of currency position overestimation in the banking sector was minimum (VaR: 0.1– 1.7 percent of the net total capital, Chart 2.2.15) i.e. the banks adhered to a conservative policy when conducting operations with foreign currency and were weakly exposed to currency risk.

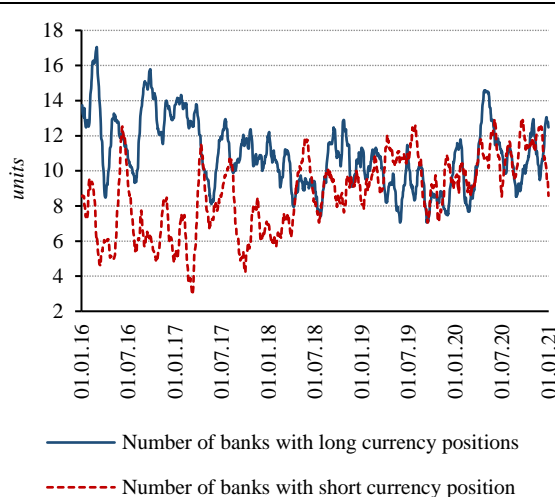
Source: NBKR

Chart 2.2.15. Dynamics of Open Currency Position (OCP) and Revaluation Risk (VaR) in percent of NTC



Source: NBKR

Chart 2.2.16. Currency Position of the Banks



Source: NBKR

Box 5. Credit and Currency Risks

At the end of 2020, 20.4 percent of the total loan portfolio was accounted for the loans, which were repaid in foreign currency, while the income of the borrowers was generated in the national currency (Chart 1). This volume of the loan portfolio was potentially exposed to credit and currency risks.

The impact made by the currency risk on the credit risk is given in Chart 2 that displays the proportion of non-performing loans by groups of loans:

- Group 1 – 19.4 percent, basic incomes of the borrower are generated in the national currency, and the loans are repaid in foreign currency;
- Group 2 – 8.2 percent, basic incomes and loans payable by the borrower are generated in the same currency;
- Group 3 – 9.5 percent, basic incomes of the borrower are generated in foreign currency, and the loans are repaid in the national currency.

Chart 1. Loan Portfolio by Groups of Loans¹⁶

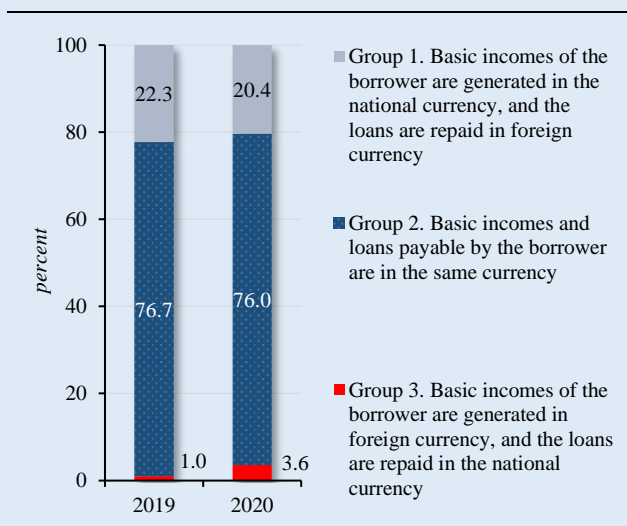
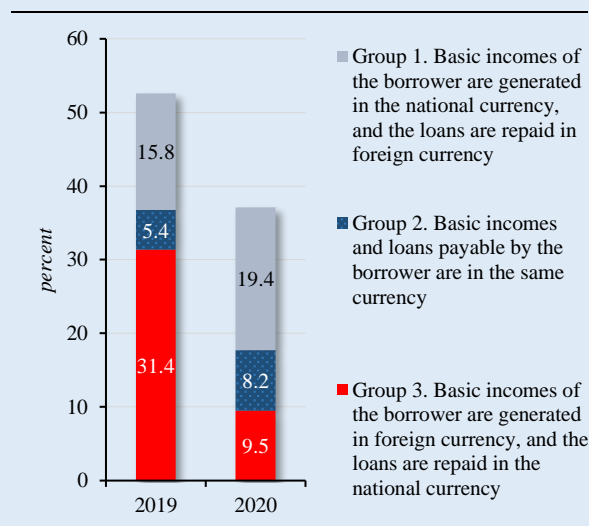


Chart 2. Share of Non-performing Loans by Groups of Loans¹⁷



Source: CBs, the volume of loan portfolio is specified exclusive of overdraft loans.

¹⁶ Breaking of loans into groups is presented in this chart. For example, the volume of loans for Group 1 as of December 31, 2020 amounted to KGS 32.7 billion or 20.4 percent of the total loan portfolio.

¹⁷ This chart shows the shares of non-performing loans in the loan portfolio by each group of loans. For example, the volume of non-performing loans for Group 1 as of December 31, 2020 amounted to KGS 6.3 billion or 19.4 percent of the loan portfolio for Group 1 (KGS 32.7 billion).

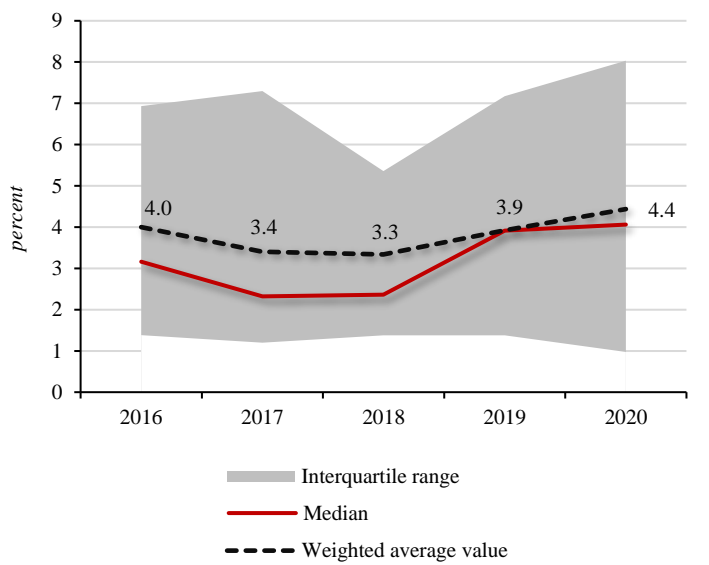
2.2.5. Interest Rate Risk

At the end of the reporting period, there was an increase in the *interest rate risk* due to higher growth rates of risk-weighted assets compared to the net total capital.

Average value of interest rate risk during the period of 2010 - 2020 was within accessible limits (2.4-4.4 percent of net total capital).

Chart 2.2.17. Dynamics of Interest Rate Risk (VaR)

in percent of NTC



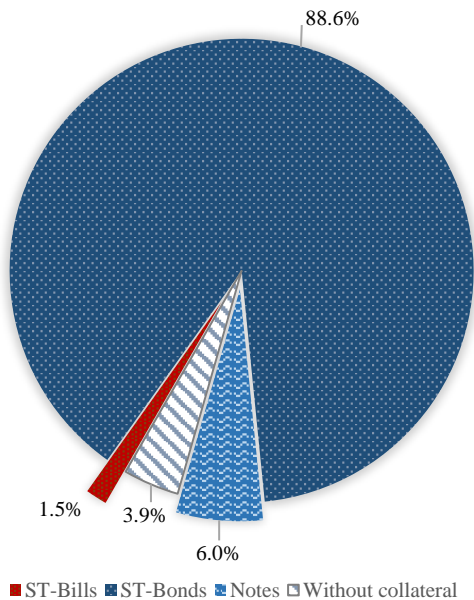
Source: NBKR

2.2.6. “Contagion” Risk

The purpose of this analysis is to assess the “contagion” risk in case of interbank lending, which can set off chain-reaction upon occurrence of problems with liquidity in one bank.

At the end of 2020, the volume of interbank loan transactions amounted to KGS 30.1 billion¹⁸.

Chart 2.2.18. Distribution of Interbank Loan Transactions Made during 2020 between Resident Banks, Depending on Collateral



The loans in the interbank market are generally covered by collateral in the form of highly liquid government securities (Chart 2.2.18) in the banking sector of the Kyrgyz Republic.

In general, the probability of the “contagion” risk materialization in the interbank credit market of the country is minimal, which is caused by highly liquid collateral.

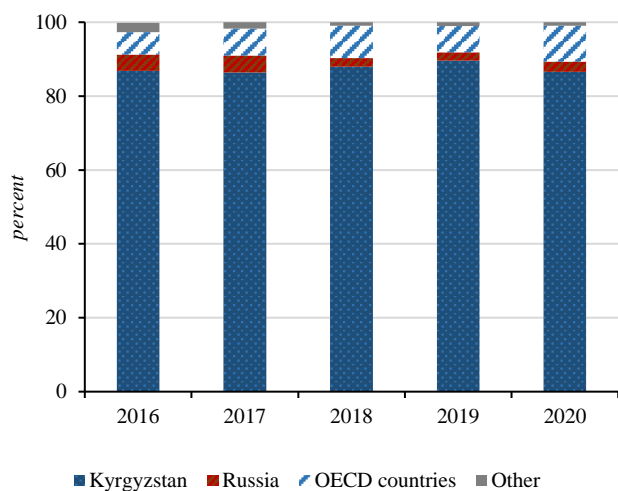
Source: NBKR

¹⁸ The total volume of transactions made between the resident banks during 2020 is meant here.

2.2.7. Country Risk

According to the data submitted by the commercial banks, the aggregate volume of disposed assets of non-residents as of December 31, 2020, constituted KGS 41.3 billion or 13.5 percent of total banking sector assets. The highest concentration of placement was observed in the OECD countries – 10.5 percent (KGS 29.7 billion) of non-residents’ disposed assets.

Chart 2.2.19. Geographic Structure of Assets

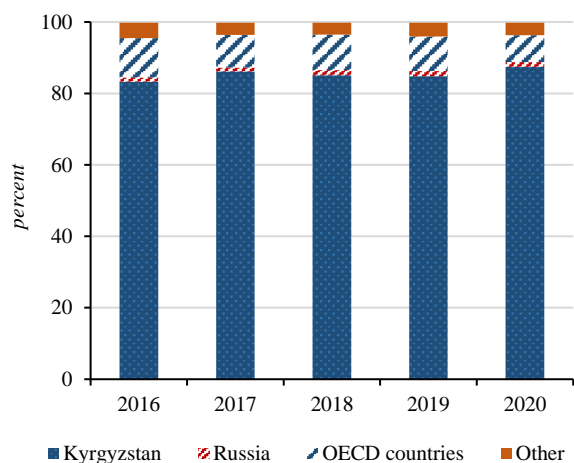


Source: NBKR

The main share of the assets placed abroad was focused on correspondent or deposit accounts and constituted KGS 39.2 billion or 95.0 percent of total disposed assets of non-residents.

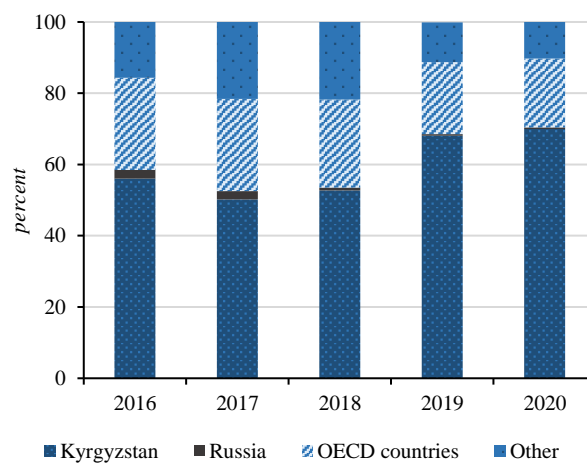
At the end of 2020, banks’ liabilities to non-residents of the Kyrgyz Republic totaled KGS 30.0 billion or 12.6 percent of the total liabilities of the banking sector. Significant volume of these resources was drawn by the non-resident banks in the form of loans and deposits, which amounted to KGS 28.8 billion or 96.0 percent of the total liabilities to non-residents. 59.6 percent of the liabilities to non-residents were accounted for the OECD countries, 15.0 and 10.6 percent – for Russia and Kazakhstan, accordingly (Chart 2.2.20).

Chart 2.2.20. Geographic Structure of Liabilities



Source: NBKR

Chart 2.2.21. Authorized Capital by Countries



Source: NBKR

At the end of 2020, foreign capital amounted to KGS 9.4 billion or 30.0 percent of the total authorized capital of the banking sector. The structure of foreign capital by countries is distributed among (Chart 2.2.21):

- residents of the OECD countries – 64.5 percent;
- residents of Kazakhstan – 23.7 percent;
- residents of Russia – 1.3 percent;
- residents of other countries – 10.5 percent.

2.3. “Reverse” Stress Testing of the Banking Sector

2.3.1. “Reverse” Stress Testing of Credit Risk¹⁹

Maximum allowable share of “performing” loans²⁰ in the loan portfolio, which upon categorized as “non-performing” loans can reduce the CAR (capital adequacy ratio) down to the threshold level of 12 percent, is calculated by means of the “reverse” stress testing of the credit risk.

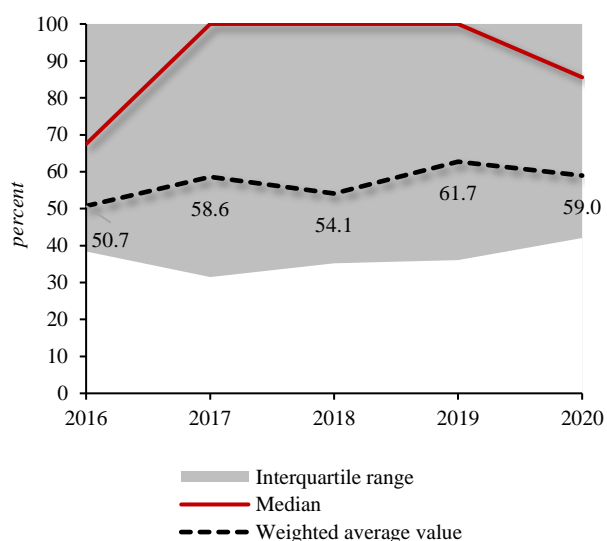
This method allows detecting a buffer stock of capital (net total capital) of banks, which can cover the additional allocations to LLP in connection with the transformation of “performing” loans into the category of “non-performing” loans²¹.

Moreover, the maximum growth rate of “non-performing” loans, where capital adequacy (K2.1) will be reduced to the threshold level of 12 percent, can be calculated by means of this method.

Based on the results of the “reverse” stress testing of the banking sector as of December 31, 2020, the maximum allowable share of “performing” loans, transferring to the category of “non-performing” in the banking sector, amounted to approximately 59.0 percent (Chart 2.3.1).

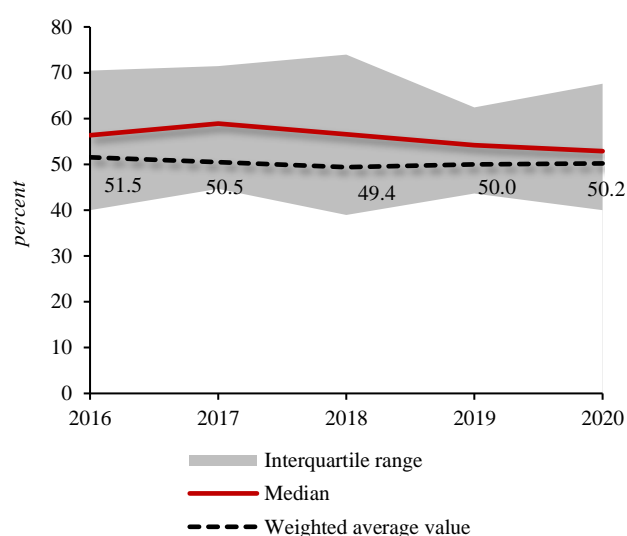
Thus, the banking sector can sustain a significant deterioration in the quality of the loan portfolio, which may require the creation of additional LLP approximately up to 50.2 percent of net total capital (Chart 2.3.2).

Chart 2.3.1. Maximum Possible Share of “Performing”²² Loans that May Become “Non-performing” Loans²³
percent of performing loans



Source: NBKR

Chart 2.3.2. Additional LLP, in Creating thereof CAR Decreases to 12 Percent
percent of NTC



Source: NBKR

¹⁹ Exclusive of troubled banks.

²⁰ Exclusive of “normal” loan category, which are risk free.

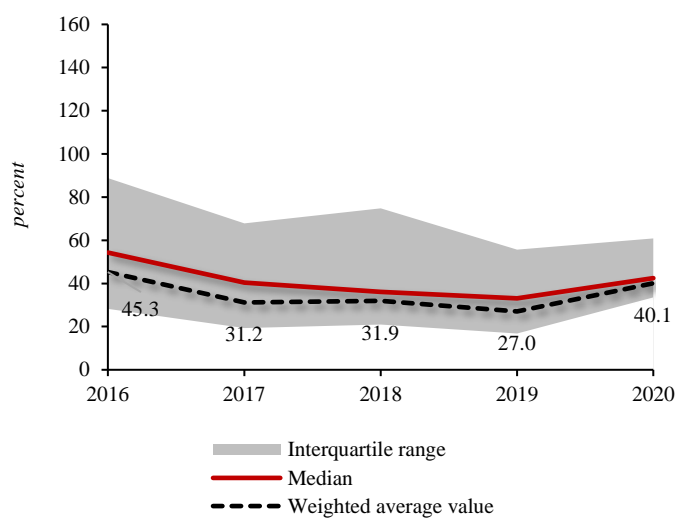
²¹ Herewith, transition of “performing” loans to the category of “non-performing” loans is fulfilled smoothly by three categories (“substandard”, “doubtful” and “losses”).

²² Exclusive of “normal” loan category, which are risk free.

²³ When CAR decreases to the threshold level of 12 percent.

2.3.2. “Reverse” Stress Testing of Liquidity Risk

Chart 2.3.3. Scope of Deposits Outflow when K3.1 May Drop to 30 Percent,
percent of clients’ total deposits



Source: NBKR

The reserve of liquid assets, which can cover a massive outflow of deposits of the clients’ total deposit base, without violating the NBKR prudential standard on the current liquidity, was calculated for the evaluation of the liquidity risk in the banking sector.

Shock is the maximum volume of the outflow of the individuals’ and non-financial enterprises’ deposits, which may reduce the liquidity ratio down to the threshold level of 30 percent.

The results of the “reverse” stress testing show (Chart 2.3.3), that as of the end of 2020 the actual amount of liquid assets of the banking sector was able to cover the deposits outflow of an average of 40.1 percent of the clients’ total deposit base (Table 2.3.1).

2.3.3. “Reverse” Stress Testing of Market Risk

The results of the “reverse” stress testing of the market risk indicate that the banking sector as of the end of 2020 has little sensitivity to the interest rate and currency risks.

Interest Rate Risk

Scenario 1 – decrease of average weighted interest rate on loans, when the level of capital adequacy decreases to the threshold level (12 percent).

The results of the “reverse” stress testing indicate little sensitivity of the banking sector to the direct interest rate risk. Decrease of the average interest rates on loans by 15.7 p.p. can reduce the level of capital adequacy ratio to 12 percent (Table 2.3.1).

Generally, the results of the “reverse” stress testing show that the banking sector is characterized by low level of interest rate risk.

Currency Risk (Revaluation Risk)

Maximum increase level of the KGS/USD exchange rate, which will influence capital adequacy and net profit, is calculated for valuation of the currency risk in the banking sector.

Scenario 1 – maximum increase level of the KGS/USD exchange rate, when the level of capital adequacy (K2.1) declines to the threshold level (12 percent).

Calculations of the “reverse” stress testing indicate that the banking sector is characterized by low risk of assets and liabilities revaluation and confirms availability of low sensitivity to currency risk (Table 2.3.1).

Scenario 2 – maximum increase level of the KGS/USD exchange rate, when net profit of the commercial banks decreases to zero level.

The results of stress testing indicate that the commercial banks can stand the impact of currency risk (Table 2.3.1).

Table 2.3.1. General Results of the “Reverse” Stress Tests as of December 31, 2020

		Banking sector
Credit risk		
Scenario 1	Share of performing loans transferring to the category of “non-performing” loans, <i>in percent</i>	59.0
Interest rate risk		
Scenario 1	Decrease of weighted average interest rate on loans, when CAR declines to 12%, <i>in percentage points</i>	15.7
Currency risk		
Scenario 1	Growth rate of USD/KGS (±) exchange rate, when CAR decreases to 12%, <i>in percent</i>	change of currency rate by 100 percent (KGS/USD)
Scenario 2	Growth rate of USD/ KGS (±) exchange rate, when net profit decreases to zero level, <i>in percent</i>	
Liquidity risk		
Scenario 1	Outflow of clients’ deposit and received loans of the total deposits and loans, when current liquidity ratio declines to 30%, <i>in percent</i>	40.1

III. NON-BANKING FINANCIAL-CREDIT ORGANIZATIONS

In general, the state of the non-banking financial-credit organizations (NBFCOs) system is assessed as stable. Increase of major indicators: assets, loan portfolio, resource base is observed. Stress test results indicate that the credit risk of the NBFCOs system is moderate.

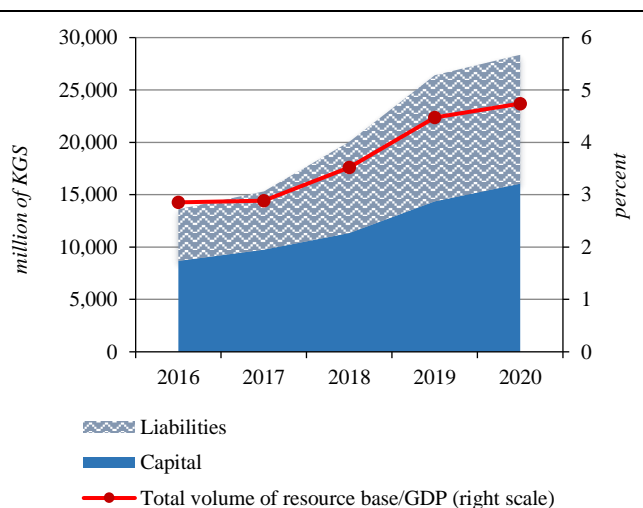
The weighted average interest rates on loans of the microfinance organizations and credit unions slightly decreased compared to 2019.

3.1. Main Trends

The system of non-banking financial-credit organizations subject to licensing and regulation by the National Bank as of December 31, 2020 in the Kyrgyz Republic, included: the specialized financial and credit institution – “FCCU” OJSC; 92 credit unions, 134 microfinance organizations (including 9 microfinance companies, 87 microcredit companies and 38 microcredit agencies), and 386 exchange offices and 2 credit bureaus.

Resources

Chart 3.1.1. Dynamics of NBFCOs Liabilities and Capital

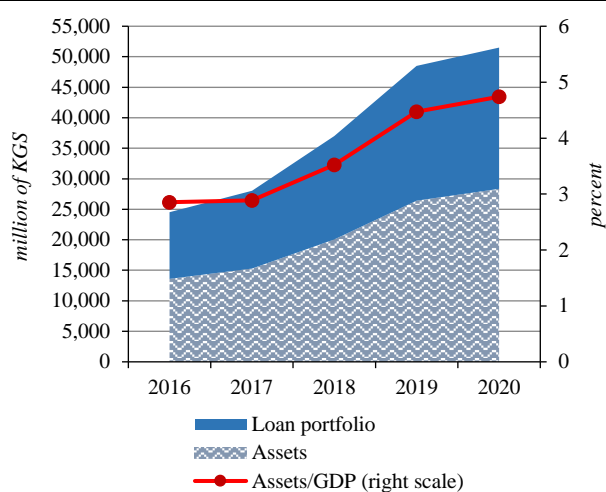


At the end of the reporting period, NBFCOs liabilities increased by 2.1 percent compared to 2019 and were formed in the amount of KGS 12.3 billion. NBFCOs capital demonstrated an increase by 11.9 percent and totaled KGS 16.1 billion (Chart 3.1.1).

Source: NBKR

Assets

Chart 3.1.2. Dynamics of NBFCOs Assets and Loans



According to periodic regulatory reporting, the total assets of NBFCOs in 2020 increased by 7.4 percent and amounted to KGS 28.4 billion²⁴. This increase was due to growth in the loan portfolio of NBFCOs (Chart 3.1.2).

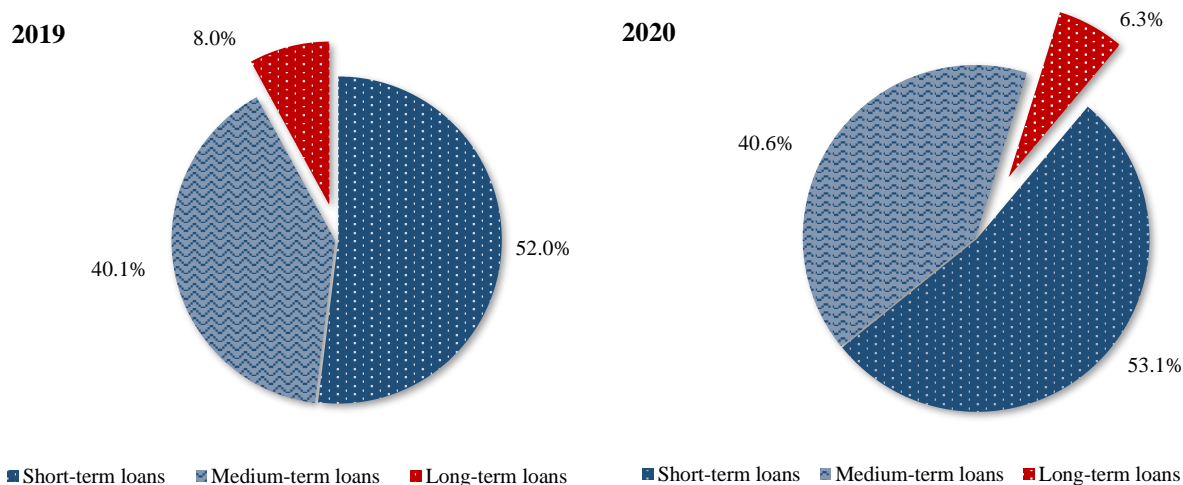
Source: NBKR

Lending remains the main activity of NBFCOs. As of December 31, 2020, the loan portfolio of NBFCOs increased by 4.7 percent and was formed in the amount of KGS 23.1 billion.

At the end of the reporting period, the number of borrowers decreased by 1.4 percent compared to 2019 and amounted to 433,364 borrowers.

During the reporting period, there was a decrease in the share of long-term credit resources and an increase in the share of short- and medium-term loans within the maturity structure of the loans provided by NBFCOs. (Chart 3.1.3).

Chart 3.1.3. Structure of the NBFCOs Loan Portfolio by Maturity²⁵



Source: NBKR

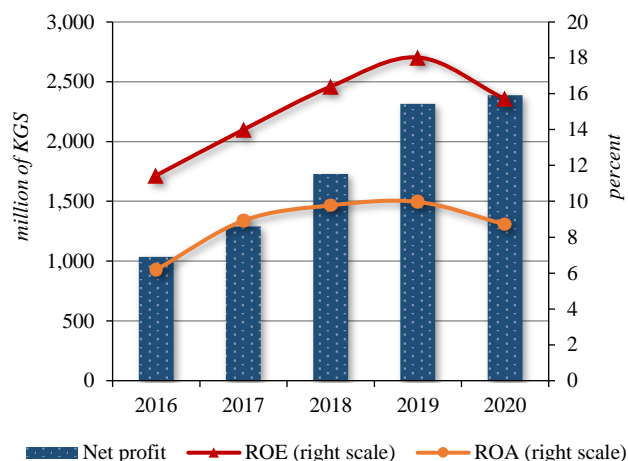
²⁴ Exclusive of SFCOs.

²⁵ Data for the period.

The main regions where the major share of NBFCOs loan portfolio is concentrated (72.0 percent of the total loan portfolio) are Bishkek city, Chui, Osh and Jalal-Abad regions, which is due to the highest level of business activity in these regions of the republic.

*Revenue Position*²⁶

Chart 3.1.4. Dynamics of NBFCOs Revenue Position²⁷



At the end of 2020, net profit of NBFCOs increased by 3.1 percent compared to 2019 and amounted to KGS 2.4 billion. In 2020, ROA decreased by 1.2 p.p. and amounted to 8.7 percent. ROE decreased by 2.3 p.p. and constituted 15.7 percent (Chart 3.1.4).

Source: NBKR

²⁶ ROA and ROE indices are provided in annual terms.

²⁷ Exclusive of SFCOs.

3.2. Risks of Non-banking Financial-Credit Organizations

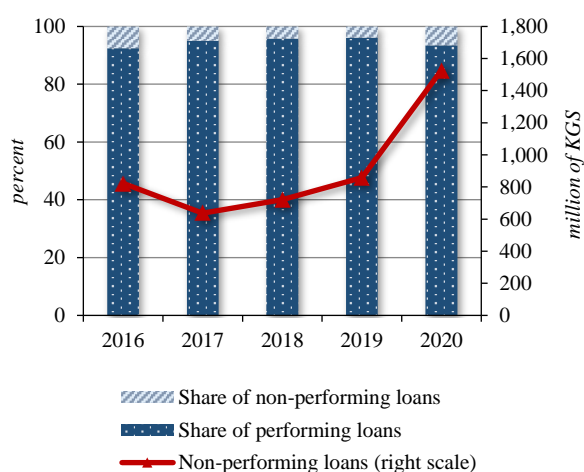
Major risk factors of the activities of NBFCOs are the quality of the loan portfolio, sectoral and institutional concentration, as well as status of the NBFCOs external debt.

Quality of the NBFCOs Loan Portfolio

As of the end of the reporting period, the share of non-performing loans in the loan portfolio of NBFCOs constituted 6.6 percent, meanwhile, their nominal volume increased by KGS 668.4 million or 77.8 percent compared to 2019 (Chart 3.2.1).

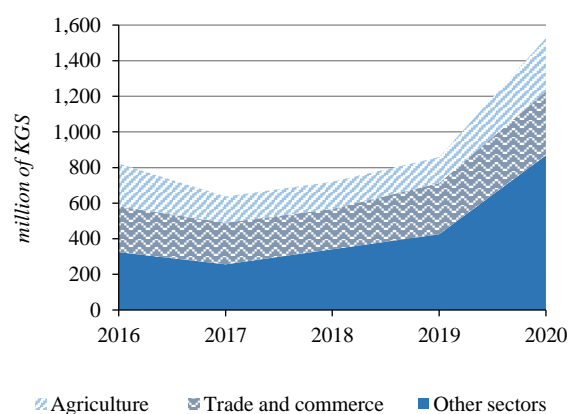
At the end of 2020, the structure of NBFCOs non-performing loans demonstrated increase in the share of defaulting loans issued to agriculture (by 2.7 p.p.), and decrease in the share of defaulting loans to trade (by 10.1 p.p.) compared to 2019. The share of defaulting loans issued to agriculture and trade in the total non-performing loans of NBFCOs constituted 19.7 and 23.5 percent, respectively (Chart 3.2.2).

Chart 3.2.1. Quality of NBFCOs Loan Portfolio



Source: NBKR

Chart 3.2.2. Structure of NBFCOs Non-performing Loans by Sectors of Economy



Source: NBKR

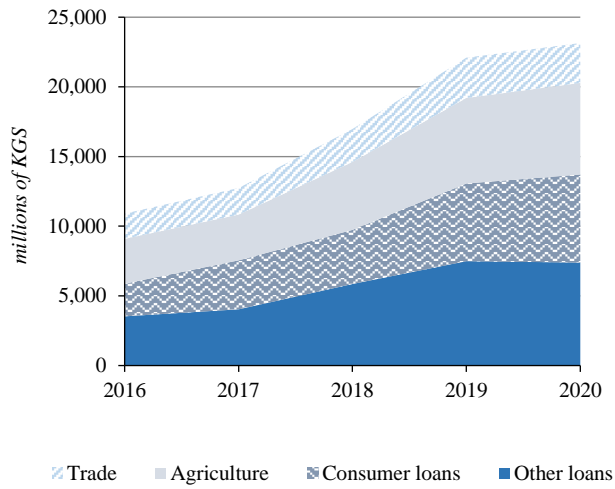
Sectoral Concentration

NBFCOs loan portfolio is concentrated in the sphere of agriculture (28.4 percent of NBFCOs total loans), as well as consumer loans and trade (27.4 percent and 12.3 percent of the total loan portfolio, accordingly, Chart 3.2.3). Lending of agriculture is associated with significant dependence on climate conditions.

Institutional Concentration

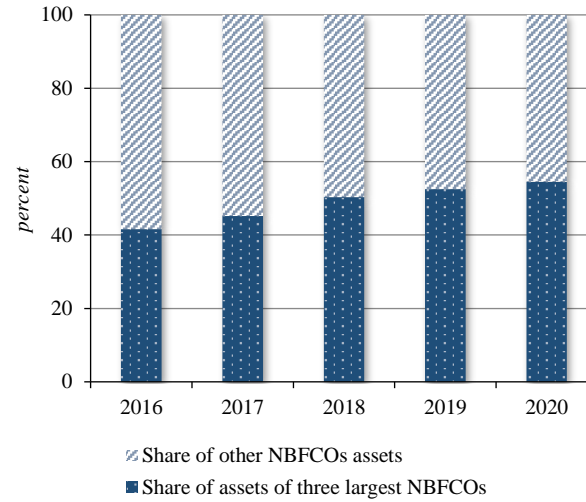
According to the results of the reporting period, the share of assets of three largest NBFCOs increased by 2.0 p.p. compared to 2019 and amounted to 54.5 percent of the total assets of NBFCOs sector (Chart 3.2.4).

Chart 3.2.3. Sectoral Structure of NBFCOs Loan Portfolio



Source: NBKR

Chart 3.2.4. Institutional Structure of NBFCOs Assets



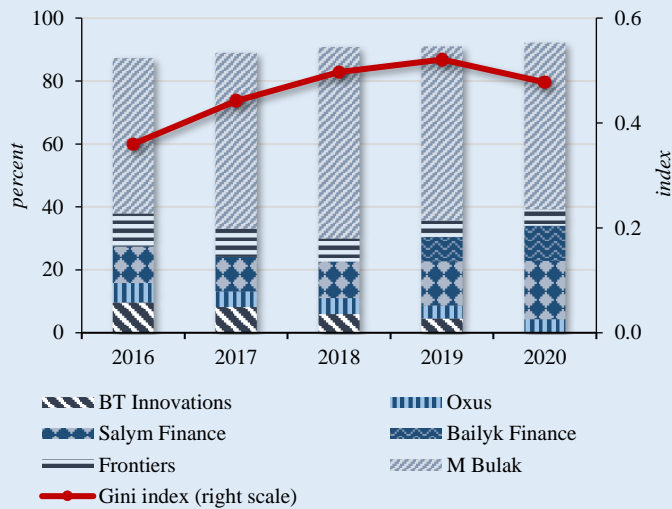
Source: NBKR

Box 6. Concentration Indices based Assessment of NBFCOs Sector Activity²⁸

The Herfindahl-Hirschman Index

Herfindahl-Hirschman²⁹ index was calculated for the purposes of concentration risk analysis in the NBFCOs sector. As of the end of 2020, Herfindahl-Hirschman index for the NBFCOs sector constituted 1,472.0 points. According to the rule of thumb³⁰, resulting value indicates availability of moderate concentration of NBFCOs assets or moderate concentration of microfinance market.

Chart 1. Dynamics of the Gini Index and Assets of 6 Largest NBFCOs



The Gini Index

The Gini index was calculated for estimating the uniformity of the NBFCOs assets distribution. As of the end of 2020, the index value constituted 0.48 with a simultaneous decrease of concentration level (Chart 1).

Source: NBKR

²⁸ Concentration indices are calculated on the basis of data submitted by 6 largest NBFCOs.

²⁹ $H = \sum_{i=1}^n (share\ i)^2$.

³⁰ The following rule of thumb was used for determining the level of market concentration:

- index value is below 0.1 (or 1,000) – insignificant market concentration;
- index value is from 0.1 to 0.18 (or from 1,000 to 1,800) – average market concentration;
- index value is above 0.18 (or 1,800) – high market concentration.

External Debt Status of NBFCOs

As of the end of the reporting period, the external debt of NBFCOs amounted to USD 73.8 million. Major part of the external debt of NBFCOs are loans provided by the foreign financial-credit organizations (88.1 percent of total external debt of NBFCOs), and the rest (11.9 percent) are loans of the international financial institutions.

At the end of 2020, external debt of the largest NBFCOs decreased by 14.7 percent compared to 2019 and amounted to USD 62.6 million.

3.3. Stress Testing of NBFCOs Sector

Stress Testing of the NBFCOs Credit Risk

Stress testing was conducted to assess the effect of deterioration of the loan portfolio quality on the NBFCOs sector.

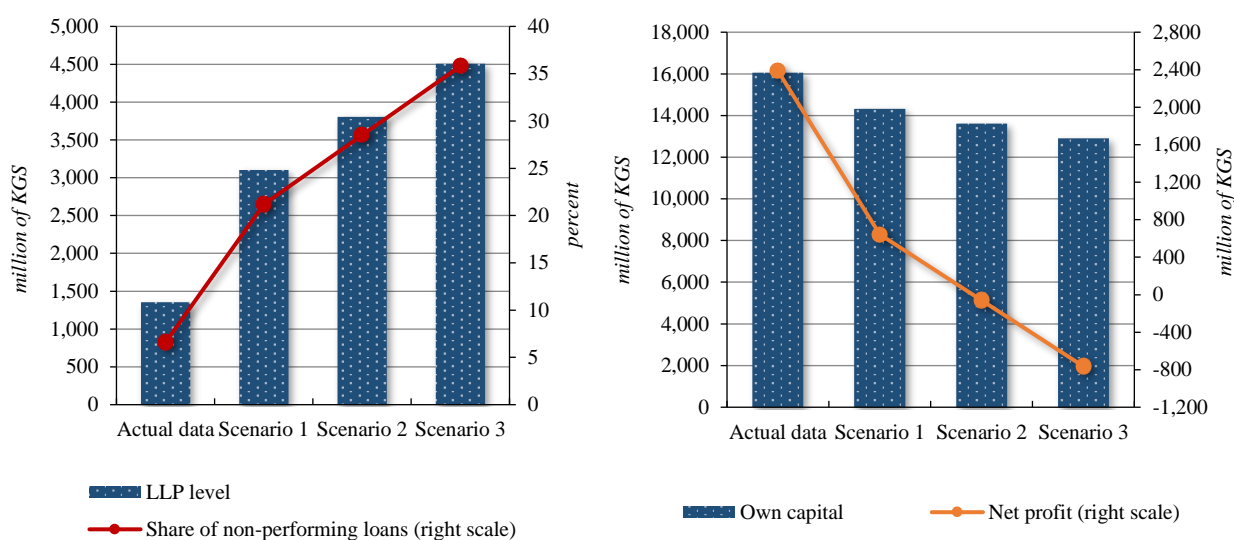
Three scenarios were considered when conducting stress testing:

- scenario 1: 50% of loans transition from one category to another;
- scenario 2: 75% of loans transition from one category to another;
- scenario 3: 100% of loans transition from one category to another.

The transition of loans from one category to another occurs uniformly by such categories as: “standard”, “under supervision”, “substandard”, “doubtful” and “losses”.

The level of loan loss provisions³¹ in the loan portfolio of NBFCOs increased from 128.6 to 232.3 percent, depending on the scenario in conducting this stress testing (Chart 3.3.1).

Chart 3.3.1. Results of Stress Testing of the Credit Risk as of December 31, 2020



Source: NBKR

It should be noted that the deterioration of the loan portfolio quality entails a gradual decline in equity and net profit of NBFCOs. In case of the first scenario implementation, the NBFCOs sector remains profitable, but the level of profit decreases down to KGS 642.4 million. In case of the second and third scenarios implementation, the NBFCOs sector will experience losses in the amount of KGS 60.9 and 764.2 million, respectively (Chart 3.3.1).

³¹ MFOs create general and special loan loss provisions for relevant categories of classifications implementing the following allocations indicated in percentage from the amount of assets:

- Standard, in %	-	from 0 to 5
- Assets under supervision, in %	-	10
- Substandard, in %	-	25
- Doubtful, in %	-	50
- Losses, in %	-	100

Table 3.3.1. Results of Stress Testing of the Credit Risk, percent

	Share of non-performing loans in the loan portfolio of NBFCOs
Scenario 1: transition of 50% of loans from one category to another	21.2
Scenario 2: transition of 75% of loans from one category to another	28.5
Scenario 3: transition of 100% of loans from one category to another	35.8

Source: NBKR

Implementation of the first scenario may result in an increase in the share of non-performing loans in the loan portfolio of NBFCOs by 14.6 p.p., to the level of 21.2 percent. In the case of the second scenario, non-performing loans may increase by 21.9 p.p., to the level of 28.5 percent, and in the implementation of the third scenario – by 29.2 p.p. and may reach the level of 35.8 percent.

IV. PAYMENT SYSTEMS

The period from the end of March till December 2020 was characterized by an increase in the level of operational risk in the payment system of the Kyrgyz Republic due to the COVID-19 pandemic and introduction of the emergency situation and the state of emergency regimes in Bishkek and a number of other regions of the Kyrgyz Republic.

In addition, a high level of operational risk was recorded in October 2020 due to the temporary suspension of the national and cross-border payments/transfers during the unstable social and political situation in the country.

The level of risks was within acceptable limits in the systemically important and significant payment systems. It was ensured by the risk management mechanisms and the payment systems rules provided for by the legislation of the Kyrgyz Republic, the current high liquidity level, the system of insurance deposits and prepayment, as well as individual decisions of the emergency operations center under the National Bank on an emergency situation/a state of emergency, aimed at ensuring uninterrupted operation of the payment systems in an epidemiological situation.

In the reporting period, the National Bank took measures to adjust the regulations for the payment systems operation, with the National Bank being an operator thereof, to minimize the identified risks. Inspections were temporarily suspended, the deadlines to submit the regulatory reports to the National Bank were revised due to the epidemiological situation. Moreover, interaction with the payment system operators and the government agencies was carried out to ensure smooth operation of the systems and payment infrastructure, and work was conducted with the population by providing consultations and considering complaints.

Effective and uninterrupted payment system is one of the main factors, which determine stability of the financial sector in the country.

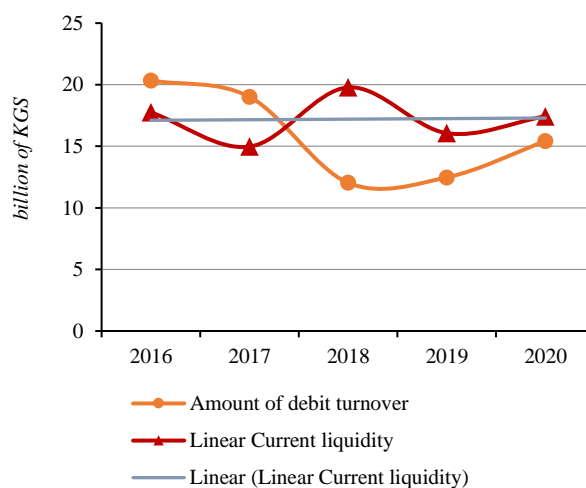
As of December 31, 2020, the following components of the payment system operated in the Kyrgyz Republic:

1. Large Value Payment System of the National Bank – Real Time Gross Settlement (RTGS).

2. Systems of Retail Payments: the System of Batch Clearing of Small Retail and Regular Payments (SBC), Systems of Payment Cards Settlement, Money Transfer Systems, E-money Payment Systems.

3. Financial Messages Receiving and Transfer Infrastructure (SWIFT Service Bureau, Interbank Communication Network (hereinafter – ICN).

Chart 4.1. Dynamics of Changes of Daily Average Indicator of Payment Volumes and Liquidity in the RTGS



Source: NBKR

At the end of 2020, in accordance with the criteria of the payment systems³² importance, the following systems were recognized as:

1. the systemically important payment systems - the RTGS and SBC systems;
2. national payment systems – the RTGS, SBC and “Elcart” systems.

These systems are the key participants in the payment system of the Kyrgyz Republic. Failures in the operation of the systemically important payment systems can entail systemic risks for the payment and banking system of the country, therefore increased requirements are applied to them.

The **RTGS** functioned normally during 2020.

The level of financial risks in the RTGS remained low due to high level of liquid funds on the participants’ accounts in relation to the turnovers in the system: average daily volume of liquid assets of participants showed increase by 8.53 percent (compared to 2019) and amounted to KGS 17.4 billion.

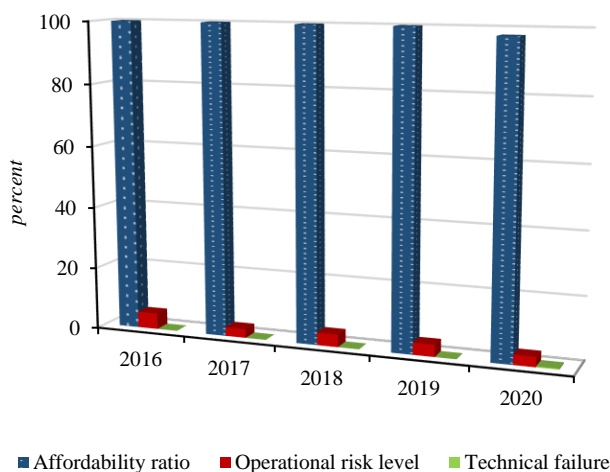
During 2020, the RTGS affordability ratio remained rather high and constituted 97.7 percent. Meanwhile, the level of operational risk, taking into account prolongation of the transaction day, was 3.2 percent.

In functioning of the **SBC** the level of financial risks in the reporting period was also low. Reserves exhibited by the participants to cover a debit net position were 5.1 times higher than the required level. According to the results of the SBC operation monitoring, the system affordability ratio remained rather high during the reporting period and amounted to 98.0 percent (a decrease in the affordability ratio by 2.0 percent). However, the level of operational risk in the system was 3.1 percent taking into account failures and extensions of the operating procedure upon request of the system participants.

Systems of Bank Payment Cards Settlements. As of January 1, 2021, five international systems, the local system “Elcart” and co-badging cards “Elcart-UPI”³³ operated in the Kyrgyz Republic.

In the reporting period, 23 commercial banks worked with the **national system “Elcart”**. The results of operation monitoring and analysis indicated that the system affordability ratio was 99.9 percent, and the level of operational risks in the system, taking into account technical failures, was 0.1 percent.

Chart 4.2. Ratio of Affordability and Operational Risk in the RTGS



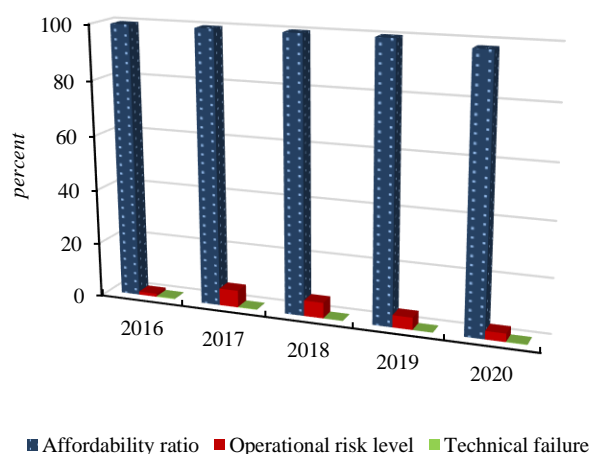
	2016	2017	2018	2019	2020
Technical failure, %	0.0	0.0	0.0	0.0	0.3
Affordability ratio, %	100.0	100.0	100.0	100.0	97.7
Operational risk level, %	5.2	2.9	4.1	3.9	3.2

Source: NBKR

³² Approved by the Resolution of the Board of the National Bank of the Kyrgyz Republic No. 2021-P-14/6-1-(PS) dated February 10, 2021.

³³ According to the Regulation “On bank payment cards in the Kyrgyz Republic”, a co-badging card is a card issued within two payment systems. Thus, “Elcart-UPI” in the territory of the Kyrgyz Republic is served according to the rules of the system “Elcart”, and outside the country - Union Pay.

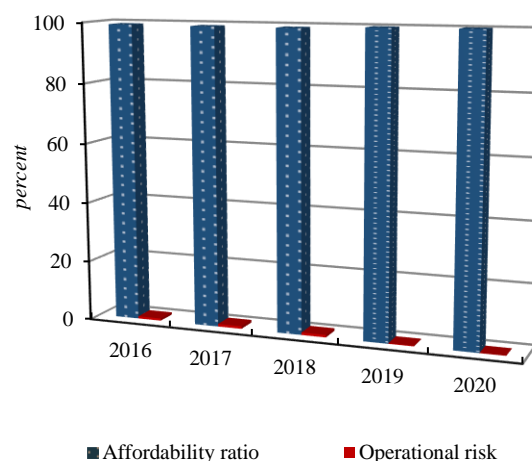
Chart 4.3. Ratio of Affordability Index and Operational Risks in the SBC



	2016	2017	2018	2019	2020
Technical failure, %	0.3	0.2	0.0	0.0	0.1
Affordability ratio, %	99.7	99.8	100.0	100.0	98.0
Operational risk level, %	1.2	6.2	5.8	4.5	3.1

Source: NBKR

Chart 4.4. Ratio of Affordability Index and Operational Risk in the SIPC



	2016	2017	2018	2019	2020
Affordability ratio, %	99.2	99.1	99.2	99.8	99.9
Operational risk, %	0.8	0.9	0.8	0.2	0.1

Source: NBKR

Money transfer systems. During 2020, receipt and transfer of international remittances without opening an account in the commercial banks was carried out through nine international money transfer systems.

Regarding **local money transfer systems**, relatively even distribution among five local money transfer systems is currently observed, the banks of the Kyrgyz Republic are operators thereof.

Table 4.1. Distribution of Flows among International Money Transfer Systems

Money transfer system	Incoming		Outgoing	
	Share of the total number, in %	Share of the total volume, in %	Share of the total number, in %	Share of the total volume, in %
Zolotaya Korona	69.0	68.2	81.2	79.7
Unistream	2.4	4.4	1.5	2.9
Western Union	24.5	18.9	6.2	9.4
CONTACT	2.5	5.0	10.2	7.0
Money Gram	0.9	2.1	0.8	1.0
Other	0.6	1.5	0.1	0.0
Total	100.0	100.0	100.0	100.0

Source: NBKR

E-money payment systems. As of January 1, 2021, the number of e-purses increased by 78.8 percent compared to the same period in 2019 and amounted to more than 3.5 million purses. The indicators on turnover with e-money for 2020 compared to 2019 are as follows:

- the volume of money transfer operations between e-purses increased by 49.8 percent compared to 2019 and amounted to KGS 6.9 billion, the number of money transfers increased by 2.8 times and constituted 1.9 million operations;
- the volume of operations on redemption (cashing out) of e-money increased by 40.0 percent and amounted to KGS 19.8 billion, the number of operations increased by 42.6 percent and constituted 3.0 million operations;
- the volume of operations on payment for goods and services with e-money in the reporting year increased by 20.8 percent compared to 2019 and amounted to KGS 7.2 billion, while the number of operations decreased by 3.9 percent and constituted 15.8 million operations;
- the volume of e-money issue increased by 36.1 percent and amounted to KGS 27.5 billion, while the amount of e-money issue increased by 21.8 percent and constituted 13.2 million operations.

Financial messages exchange channels. At the end of 2020, the exchange of cross-border financial messages was carried out through the SWIFT network, bank-client services, while the main flow fell on the SWIFT telecommunications network. SWIFT is the main channel for the banking system to exchange securely cross-border financial messages with its correspondent banks.

On January 1, 2019, the National Bank established a SWIFT service bureau to minimize the financial burden and dependence of the banks on the foreign service bureaus. Currently, the National Bank and 15 commercial banks of the Kyrgyz Republic operate through the SWIFT service bureau.

The payment infrastructure of the Kyrgyz Republic also includes 20 (among them one payment system operator has temporarily suspended the acceptance of payments since August 2020) non-banking systems to accept payments in favor of third parties. In the reporting period, licenses were revoked from three payment system operators.

Based on the analysis of the data received in the reporting period, the payment system operators processed 146.7 million payments for a total amount of KGS 44.94 billion. The volume of payments increased by 41.22 percent compared to 2019, while their number decreased by 13.82 percent.

Given that there are a large number of systems to accept payments in favor of third parties in the market, competition is developed in this segment.

V. IMPROVEMENT OF THE BANKING SECTOR REGULATION

In the reporting period, development of the regulatory legal framework governing the activities of the financial-credit organizations was mainly aimed at maintaining stability in the banking and financial systems of the country and protection of the financial services consumers' rights due to the situation caused by the COVID-19 pandemic and the spread of this virus in the Kyrgyz Republic.

1. The Board of the National Bank adopted the Resolution “On introduction of amendments into some regulatory legal acts of the National Bank of the Kyrgyz Republic on commission fees and other payments” No. 2020-P-12/8-8-(NPA) on February 26, 2020 to ensure fair approach when the banks set commission fees and other payments within the framework of loans issuing.

2. The Board of the National Bank adopted the Resolution “On temporary rules to regulate the activities of the financial-credit organizations due to the COVID 19 disease” No. 2020-P-12/13-1-(BS) on March 18, 2020.

According to this Resolution, the commercial banks and NBFCOs:

- are prohibited to charge and collect commission fees and other payments related to revision of the loan agreement terms;

- are prohibited to impose and levy penalties, including forfeit (fines/charges), from the borrowers for non-performance/improper performance of obligations;

- are recommended to provide a deferral for payments of issued loans for at least three months;

- are allowed not to worsen the category of loan classification when the terms of loan agreements are changed;

- information on overdue payments transferred to the credit bureaus should not be included as negative credit information and the reasons for delays should be taken into account.

3. The Board of the National Bank adopted the Resolution “On the procedure for operation and regulation of the activities implemented by the banks, non-banking financial-credit organizations and other legal entities supervised by the National Bank of the Kyrgyz Republic upon introduction of an emergency situation in the territory of the Kyrgyz Republic due to the spread of the COVID-19 disease” No. 2020-P-12/14-1-(BS) on March 23, 2020.

This document was developed to determine measures for operation of the banks, non-banking financial-credit organizations and other entities supervised by the National Bank during introduction of an emergency regime in the Kyrgyz Republic due to the spread of the COVID-19 disease to ensure uninterrupted provision of financial services to the population and protection of the bank personnel.

4. The Board of the National Bank adopted the Resolution “On some temporary decisions of the National Bank of the Kyrgyz Republic on establishment of the prudential standards and requirements mandatory for the commercial banks and non-banking financial-credit organizations of the Kyrgyz Republic” No. 2020-P-12/15-7-(NPA) on March 24, 2020 to reduce the risk of non-compliance with certain prudential standards and requirements by the banks.

The Resolution:

- suspended a number of resolutions recently adopted by the Board of the National Bank on calculation of the total capital adequacy ratio, leverage and liquidity coverage ratio, taking into account the new standards;

- suspended the regulatory legal act on disclosure of information on the commercial banks' activities;

- relaxed the requirements for liquidity ratios, as well as for the level of weighting the credit risk on loans extended in foreign currency;

- increased the time threshold, if being exceeded the banks must create 100% reserves for accrued interest on loans, from 90 to 270 days.

5. On March 24, 2020, the Board of the National Bank adopted the Resolution “On introduction of amendments into the Resolution of the Board of the National Bank of the Kyrgyz Republic “On some regulatory legal acts of the National Bank of the Kyrgyz Republic” No. 52/4 dated June 30, 2010” No. 2020-P-12/15-6-(NPA) due to the need to revise the standards upon sharp decrease in the portfolio of the banks’ group loans that actively extended loans to the joint liability groups, and occurrence of a risk of non-compliance with the standards in future.

6. Amendments in some regulatory legal acts of the National Bank regarding operations with securities conducted by the financial-credit organizations were approved by the Resolution of the Board of the National Bank No. 2020-P-12/15-5-(NPA) on March 24, 2020. The requirements for acquisition and classification by the banks of the securities owned by the issuers-residents of the Kyrgyz Republic were lowered in the regulatory legal acts of the National Bank in order to develop the securities market.

7. On March 25, 2020, the Board of the National Bank adopted the Resolution “On introduction of amendments into some regulatory legal acts of the National Bank of the Kyrgyz Republic” No. 2020-P-12/16-3-(NPA) regarding establishment of the requirements to the commercial banks for lending on security of the warehouse certificates.

In order to minimize the risks when extending the loans secured by the warehouse certificates, the Resolution established the minimum requirements:

- to the issuer of the security (warehouse), providing services on products storage in the warehouses with released (issued) warehouse certificate;
- to the documentation to conduct analysis of the borrower’s solvency;
- to quarterly monitoring of seasonal fluctuations in prices for agricultural products, analysis of the impact of changes in prices for products (goods) on the cost of collateral;
- to classification of the assets secured by the warehouse certificates within the framework of financing;
- to the documentation for assessing the collateral quality.

8. On March 30, 2020, the Board of the National Bank adopted the Resolution “On the procedure for operation and regulation of the activities conducted by the banks, non-banking financial-credit organizations and other legal entities supervised by the National Bank of the Kyrgyz Republic upon introduction of a state of emergency in the territory of the Kyrgyz Republic due to the spread of the COVID-19 disease” No. 2020-P-12/19-1-(BS).

This document was developed to minimize the risks in the activities conducted by the commercial banks, non-banking financial-credit organizations and other legal entities supervised by the National Bank in case of mass infection of the population in a state of emergency amid epidemic of infectious diseases and to provide the methods of taking a set of measures applied before, during and/or after occurrence of a threat of mass infection of the personnel to ensure functioning of the critical business processes of the banks, non-banking financial-credit organizations and other legal entities supervised by the National Bank of the Kyrgyz Republic and providing their implementation.

9. The Board of the National Bank adopted the Resolution “On the time frames for submitting the reports by the commercial banks and non-banking financial-credit organizations of the Kyrgyz Republic to the National Bank of the Kyrgyz Republic” No. 2020-P-12/20-1-(NPA) on April 3, 2020 to maintain stability of the banking and financial systems in the country.

The Resolution is related to extension of the deadlines for submission of the reports by the banks and non-banking financial-credit organizations (FCOs) to the National Bank and is focused on reducing the risks of non-compliance by the FCOs with the requirements of the National Bank on reporting issues in a timely manner.

10. The Board of the National Bank of the Kyrgyz Republic adopted the Resolution “On extension of the terms of audit, approval, submission and publication of the bank’s financial statements” No. 2020-P-12/23-1-(BS) on April 16, 2020 in view of introduction of a state of emergency in certain territories of the Kyrgyz Republic due to the spread of the COVID-19 disease.

11. On April 29, 2020, the Board of the National Bank adopted the following resolutions:

1. “On additional temporary measures to regulate the activities of the commercial banks in the Kyrgyz Republic” No. 2020-P-12/25-6-(NPA), focused on softening and temporarily suspending the execution of the National Bank’s certain requirements by the commercial banks and protecting the rights of the banking services consumers.

The Resolution prior to adoption of the relevant decision by the Board of the National Bank for the commercial banks:

- relaxed the requirements for monitoring the borrowers’ loans by reducing the frequency of conducting thereof. At the same time, payment monitoring should be conducted for consumer loans, implying an analysis based on payments made on the loan;

- suspended execution of the requirement for movable property monitoring;

- gave an opportunity to issue consumer loans to the borrowers in the national currency, provided that certain conditions are observed;

- allowed, when issuing loans, not to require the registration documents (certificates, patents) issued by the state authorities from the individual entrepreneurs;

- allowed not to demand from the individual entrepreneurs, when opening a bank account, a certificate on tax registration of a taxpayer issued by the tax service. A similar relief was provided to the legal entities (residents) when opening an account to receive a loan under the programs related to the issuance of preferential unsecured loans for the small and medium-sized businesses.

2. “On temporary rules for classification of the assets and implementation of the commercial banks’ appropriate deductions to ensure loan loss provisions” No. 2020-P-12/25-7-(NPA), which will allow the banks to redistribute the costs, to mobilize resources for lending to the business entities and the population and to ensure the stable functioning of the banking system.

The Resolution establishes indulgences for classification of the assets, the quality of which has deteriorated or deteriorates due to the spread of coronavirus disease, as well as for classification of the loans that will be issued within the framework of targeted government programs or programs focused on restoring/revitalizing the activities of the business entities and the population in the country.

12. On May 13, 2020, the Board of the National Bank adopted the Resolution “On the procedure for identifying and verifying clients in the remote mode” No. 2020-P-12/27-1-(NPA), which outlines the procedure for remote identification and verification of the clients via video communication, as well as other channels of interaction with the clients.

13. Amendments in some resolutions of the Board of the National Bank of the Kyrgyz Republic, including the Regulation “On licensing the banks’ activities” were approved by the Resolution of the Board of the National Bank of the Kyrgyz Republic No. 2020-P-12/39-1-(NPA) on July 8, 2020 to improve the regulatory legal acts of the National Bank, as well as to resolve the issues related to reorganization of the banks and approval of the officials, including the subsidiary commercial banks and the guarantee funds.

14. On August 12, 2020, the Board of the National Bank of the Kyrgyz Republic adopted Resolution “On approval of the Regulation “On special regulatory regime” No. 2020-P-12/45-3-(NPA)”. The Resolution was adopted to bring it in line with the legislation of the Kyrgyz Republic and reduce the barriers for introduction of the innovative services/technologies into the banking and payment systems market by the existing and new players in order to increase the services availability, as well as in the regions of the Kyrgyz Republic.

15. On August 12, 2020, the Board of the National Bank of the Kyrgyz Republic adopted the Resolution “On amendments to certain regulatory legal acts of the National Bank of the Kyrgyz Republic on licenses under special regulatory regimes” No. 2020-P-12/45-4-(NPA). This Resolution provides for entrusting the Supervision Committee and the Payment System Committee of the National Bank with the powers to consider the issues related to granting the permits within the framework of a special regulatory regime.

16. As part of implementation of the Decree of the President of the Kyrgyz Republic “On declaring 2020 - the Year of regional development, digitalization of the country and support for children” UP No. 1 dated January 8, 2020, as well as to ensure the availability of banking services for the residents of remote

regions of the country, the Order “On amendments to the joint order of the Ministry of Internal Affairs of the Kyrgyz Republic and the National Bank of the Kyrgyz Republic “On unified requirements for the technical strength of the financial-credit institutions and the procedure for their protection in the Kyrgyz Republic” was signed on September 22, 2020, in terms of establishing the requirements for technical strength of the mobile offices.

17. Amendments in some regulatory legal acts were approved by the Resolution of the Board of the National Bank of the Kyrgyz Republic No. 2020-P-12/67-2-(NPA) on November 25, 2020 as part of further improvement of the methods of risk-oriented supervision over the banks’ activities, increasing the access of the population to the banking services, as well as bringing the regulatory legal acts of the National Bank in line with the international financial reporting standards.

According to the amendments, the clients with a bank account are allowed to use a driver’s license to replenish their bank account, the number of the card copies with signature patterns and seal imprints submitted by the legal entities to the bank when opening an account has been reduced, calculation of the indicator of the maximum investment in real estate has been revised (fixed capital).

In addition, it is possible for the inspectors to send requests to the bank to provide relevant information for assessment of the banking system risks. Requirements have been established for storage by the banks and provision of access to corporate e-mail of certain bank employees to the regulator within the framework of inspections.

18. On December 23, 2020, the Board of the National Bank of the Kyrgyz Republic adopted the Resolution “On amendments to certain regulatory legal acts of the National Bank of the Kyrgyz Republic” No. 2020-P-12/73-10-(NPA) in order to obtain information from the commercial banks to determine the degree of exposure of the banking portfolio economic value to the interest rate risk. In addition, the Resolution provides for a change in the procedure for calculating liquidity ratios (K3.1, K3.2) and introduction of a rule for notifying the commercial banks by the National Bank of their systemic importance based on the quantitative indicators.

19. Amendments in some regulatory legal acts of the National Bank, according to which the requirements for classification of the restructured loans were revised and additional requirements were established for classification of the banks’ off-balance sheet liabilities and assets, were approved by the Resolution of the Board of the National Bank of the Kyrgyz Republic “On amendments to certain regulatory legal acts of the National Bank of the Kyrgyz Republic” No. 2020-P-12/73-11-(NPA) on December 23, 2020 to reduce the risks of inaccurate reflection of the quality of the banks’ assets and off-balance sheet liabilities.

20. Amendments in the regulatory legal acts of the National Bank, in terms of improving the procedure for pledged property assessing by the banks, improving the quality of internal control over work with other property of the banks and strengthening the requirements for classification of the non-residential property accepted by the bank for loans repayment, were introduced by the Resolution of the Board of the National Bank of the Kyrgyz Republic No. 2020-P-12/75-3-(NPA) on December 28, 2020 to reduce the risks of overestimating or underestimating the value of collateral, to prevent the growth of non-performing assets in the banking system.

Principles of Islamic Finance

1. Amendments were approved in some regulatory legal acts of the National Bank of the Kyrgyz Republic by the Resolution of the Board of the National Bank of the Kyrgyz Republic No. 2020-P-12/8-7 (NPA) on February 26, 2020 to clarify some issues of corporate governance in the banks conducting operations according to the principles of Islamic finance, and preparation of financial statements by the banks that have an “Islamic window”.

2. Amendments concerning operations of the financial-credit organizations conducting operations in accordance with the principles of Islamic finance, with the securities, and on credit risk management were approved in some regulatory legal acts of the National Bank of the Kyrgyz Republic by the Resolution

of the Board of the National Bank of the Kyrgyz Republic No. 2020-P-12/15-5-(NPA) on March 24, 2020 to develop the Islamic securities market and create equal conditions for the market participants.

3. Amendments focused on determining the procedure for calculating an open position and monitoring compliance with the limits of an open position in precious metals by the Islamic banks and the banks having an “Islamic window” were approved in the Instruction “On the procedure to observe the limits of open foreign exchange position by the banks conducting operations in accordance with the principles of Islamic banking and finance” by the Resolution of the Board of the National Bank of the Kyrgyz Republic No. 2020-P-12/39-2-(NPA) on July 8, 2020.

4. Amendments were approved in:

- the Regulation “On operations conducted in accordance with the principles of Islamic banking and finance”;

- the Regulation “On implementation of the principles of Islamic finance in the Kyrgyz Republic within the framework of a pilot project”

by the Resolution of the Board of the National Bank of the Kyrgyz Republic No. 2020-P-12/51-1-(NPA) dated September 23, 2020 to expand the possibilities of transactions/agreements applied according to the principles of Islamic finance.

5. The Instruction on distribution of profit/losses on the bank accounts, the bank deposit accounts in accordance with the principles of Islamic banking and finance was approved by the Resolution of the Board of the National Bank of the Kyrgyz Republic No. 2020-P-12/67-3-(NPA) on November 25, 2020 to standardize distribution of profit/losses received from placement of the clients’ funds, as well as to establish requirements for management of the financing and deposits portfolio formed by the banks in accordance with the principles of Islamic banking and finance.

GLOSSARY AND ABBREVIATIONS

A *bank deposit* is the amount of money, accepted by a financial-credit organization under contract from another person on the terms of repayment, payment and maturity. Deposits can be time and demand. Demand deposits are made without specifying the shelf life, and time deposits are made for a certain period.

A *bank loan* is money provided by a bank for a fixed period under the terms of re-payment and payment of loan interest.

A *foreign exchange market* is a market in which the purchase/sale of foreign currencies is made. By the economic content, it is a sector of the money market, where supply and demand for a specific product such as currency are balanced. According to its purpose and form of organization, it is a set of specific institutions and mechanisms that in concert provide an opportunity to freely sell and/or buy domestic and foreign currency on the basis of supply and demand.

A *money market* is a market in which there is the giving and receiving of funds in the form of loans and securities for a short term within the range of participants.

Return on securities is the ratio of the annual return on the security to its market price; the rate of return received by the owner of the security.

The *housing affordability index* is an indicator of the state of the housing market in terms of the possibility of acquiring apartments by the people. Calculated as the ratio of the average market value of a standard apartment (total area of 54 sq. m.) to the average annual income of a family of three (two adults and a child).

The *payment system affordability index* is a measure of the availability of the system as access to services and information for users of the system on their demand. Downtime of the system due to technical failures, power outages, late opening or early closing of the trading day of the system reduce the time to access the system.

The *liquidity ratio of payment systems* characterizes sufficiency of liquid funds in the accounts of the participants of the system for the payments and settlements.

Macroprudential analysis is an assessment and monitoring of strong sides and vulnerable spots of the financial system taken as a whole.

Minimum consumer budget is the cost of a set of minimum benefits and services to the subsistence minimum.

A *securities market* is organized exchanges and structures (securities depository companies, accounting and clearing houses), as well as other companies that provide services related to the activities of the exchange. This category includes depositories and electronic clearing systems, the activity of which is ensured by financial corporations and national self-regulatory organizations of oversight over the activities of stock exchanges and related institutional units or their regulation.

Stress tests are methods used for assessment of portfolios vulnerability with respect to significant changes in the macroeconomic situation or exceptional but possible events.

An *unemployment rate* is the percentage of the actual number of unemployed to the total economically active population.

Financial assets include equity instruments and units/shares of investment funds, debt instruments, derivatives, stock options for employees and monetary gold.

LIST OF ABBREVIATIONS

CAR	– Capital Adequacy Ratio
CB	– Commercial Bank
COVID-19	(COroNaVIrus Disease 2019) is the coronavirus infection of 2019
CPI	– Consumer Price Index
DTI	(debt-to-income) is the ratio of the amount of the borrowers’ payments on loans (including the amount of principal and interest payments for the reporting period) to the main annual income of the borrower declared at the time of issuing a loan
FAO	– Food Agriculture Organization of the United Nations
FCO	– Financial-Credit Organization
GDP	– Gross Domestic Product
ICN	– Interbank Communication Network
K3.1.	– Economic Liquidity Ratio
K3.2.	– Short-term Liquidity Ratio
K3.3.	– Instant Liquidity Ratio
KR	– Kyrgyz Republic
LLP	– Loan Loss Provisions
LTV	(loan-to-value ratio) is the ratio of issued loans to the value of collateral
MF KR	– Ministry of Finance of the Kyrgyz Republic
MFO	– Microfinance Organization
M2	– Money Supply
NBFCOs	– Non-banking Financial-Credit Organizations
NBKR	– National Bank of the Kyrgyz Republic
NSC KR	– National Statistical Committee of the Kyrgyz Republic
NTC	– Net Total Capital
OCP	– Open Currency Position
OECD	– Organization for Economic Cooperation and Development
OJSC	– Open Joint-Stock Company
p.p.	– percentage points
PRBR	– Periodic Regulatory Bank Reporting
ROA	– Return on Assets
ROE	– Return on Equity
RTGS	– Real Time Gross Settlement System
SALR GKR	– State Agency for Land Resources at the Government of the Kyrgyz Republic
SBC	– System of Batch Clearing
SFCO	– Specialized Financial-Credit Organization
SIPC	– Single Inter-bank Processing Center
ST-Bills	– State Treasury Bills
ST-Bonds	– State Treasury Bonds
USA	– United States of America
VaR	– Interest Rate Risk