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**Working Paper**

# Financial inclusion, financial literacy, and financial education in Azerbaijan

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# FINANCIAL INCLUSION, FINANCIAL LITERACY, AND FINANCIAL EDUCATION IN AZERBAIJAN

Gubad Ibadoghlu

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**Abstract**

This paper discusses the status of financial inclusion, education, and literacy in Azerbaijan as well as measures to foster the development of SMEs, which currently have inadequate access to financial resources. The primary policy challenge faced by the government of Azerbaijan is defining its role in creating broader access to financial products and services.

This paper highlights the challenges faced in overcoming the barriers to financial inclusion, and solutions found, and discusses the main lessons learned and a potential way forward.

The first section of the paper provides detailed information on the national financial system. The second section covers the status of financial inclusion for individuals and SMEs. The third section analyzes different (supply and demand) aspects of barriers to financial inclusion, while the remaining sections present policies aimed at promoting financial regulation, literacy, and education. Finally, the paper presents key policy recommendations.

**Keywords:** financial inclusion, financial education, financial literacy, SME, household, Azerbaijan

**JEL Classification:** D14, D18, G21, G28, I28

**Abbreviations**

ABA – Azerbaijan Banks Association
ABTC – Azerbaijan Bank Training Centre
ADİF – Azerbaijan Deposit Insurance Fund
AIC – Azerbaijani Investment Company
AMFA – Azerbaijan Micro-Finance Association
ALB – average loan balance
ALC – Azerbaijan Library Confederation
ARC – American Resource Center
ATM – automatic teller machine
AZN – Azerbaijani manats
BEEPS – Business Environment and Enterprise Performance Survey
CBAR – Central Bank of Azerbaijan Republic
CCR – Centralized Credit Registry
CGFA – Credit Guarantee Fund of Azerbaijan
FDI – foreign direct investment
FL – financial literacy
FMSA – Financial Markets Supervisory Authority
FSA – Financial Stability Council
FSDS – Financial Sector Development Strategy
GDP – gross domestic product
GIZ – Germany International Cooperation Society
GLP – gross loan portfolio
MFI – microfinance institution
IFLA – International Federation of Library Associations
INFE – International Network on Financial Education
NBCIs – nonbank credit institutions
NFES – National Fund for Entrepreneurship Support
PAR – portfolio at risk
PIN – personal identification number
PWC – PricewaterhouseCoopers
OECD – Organisation for Economic Co-operation and Development
SBFIC – German Savings Banks Fund for International Cooperation
SRM – strategic road map
SMEs – small and medium-sized enterprises
SSC – State Statistical Committee
WB – World Bank
WBG – World Bank Group

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# 1. INTRODUCTION

During the last decade, the Azerbaijan economy experienced rapid growth, peaking at 35% in 2006, thanks to the increasing export of oil products on favorable terms. Over the past decade, the financial system has benefited from the government's investment of oil revenues in the nonoil economy, and the rapid expansion of higher margin retail and microlending. However, oil production started to peak between 2011 and 2013 and the continuing fall in oil prices led to a slowdown in oil production and economic growth in 2014, which caused the Azerbaijani manat to be devalued by 34% in February and consequently by 48% in December 2015. The reduction of oil prices and weaker macroeconomic fundamentals at the backdrop of negative external shocks have led to the devaluation of the national currency and erosion of public trust in the financial sector. During the last 3 years, some financial institutions ceased operations and are now in the process of leaving the sector. The licenses of 15 banks (2 banks in 2015, 11 banks in 2016, and 2 banks in 2017) were revoked due to their inability to meet capital requirements in the last 3 years.

The Azerbaijani financial sector faces a variety of challenges in the wake of the national currency devaluations. Over the last 2 years, the consistently observed double-digit inflation rate along with the decline in the oil revenue and industrial output have had a profoundly adverse effect on the financial sector.

Therefore, restoring financial stability, renewing consumer and investor confidence, reducing dollarization, and mobilizing higher savings in manats are the top priorities of Azerbaijani policy makers. The authorities increasingly discuss the issues of consumer and depositor protection, responsible lending, and access to finance. The consumer protection, financial inclusion, and financial literacy agenda is increasingly crucial for Azerbaijan in the light of the latest market developments and the need to enhance financial stability and restore public and investor trust. Consumer protection and financial capability are becoming an essential element of the financial sector stabilization and development agenda in Azerbaijan.

# 2. OVERVIEW OF FINANCIAL SYSTEM

The financial sector in Azerbaijan is dominated by banks, with the nonbanking sector continuing to offer limited opportunities. The share of the banks and non-bank credit organizations in the total assets of the financial system constituted 88% and 9.7%, respectively, in 2015 while the percentage of the insurance companies in the total assets was 2.3%. The nonbanking financial sector, particularly the microfinance sector, is underdeveloped but is an essential source of finance for small and medium-sized enterprises (SMEs).

Banks and nonbank credit institutions participating in the Azerbaijani financial market experienced positive development until the national currency devaluation and played a significant role as sources of financial services for individuals and SMEs.

In Azerbaijan, the primary sources of financial services for individuals and SMEs are divided into two groups: banking sector and nonbank credit organizations.

## 2.1 Banking Sector

Currently in Azerbaijan, of the 30 banks in operation, only two of them are state banks. The government announced privatization of one of them – the International Bank of Azerbaijan – in 2018. There are 15 foreign capital banks, including a number of local branches of foreign banks. The government lifted all restrictions on foreign capital in the sector in 2005, but large foreign banks have yet to penetrate the Azerbaijani market.

For comparison, note that 43 banks were operating in Azerbaijan at the end of 2015, down from 46 at year-end 2008 and from 200 banks at the end of 1996. During the period from 2008 to 2017, just one new bank opened (in 2010), while 15 closed. Although the number of intermediaries decreased, the total number of bank branches has increased since 2008 (although a decline occurred in 2012), and overall bank assets increased (in local currency terms) from year-end 2008 to 2016.

According to the Financial Markets Supervision Authority of the Republic of Azerbaijan, the assets of the Azerbaijani banking sector had reached AZN27,921.0 million by 31 December 2017,[1] which is 11.2% less than at the end of 2016. The credit portfolio of banks decreased by 28.5% in 2017 compared to the same period of 2016. Since the decline, the credit portfolio of banks in the banking sector has faced the problem of excess liquidity. According to Zakir Nuriyev, president of the Association of Banks of Azerbaijan,[2] "currently, the banking sector has liquidity of AZN4 billion, and therefore there is no need to raise funds from abroad. Shortly, the auction mechanism between banks will be involved and liquid funds distributed among the market participants. Solving liquidity problems created an opportunity to lower loan interest," he said.

At present, most banks offer short-term trade financing, long-term project financing, mortgage products, and other banking products. The overall lack of medium- to long-term capital is a constraint to financing private business in Azerbaijan. The credit supply is far too small to provide a suitable environment for the development of SMEs in the country. In fact, most SMEs have insufficient access to affordable credit lines given collateral requirements, loan terms, etc. Long-term trade and project financing are in their infancy.

According to the Economist Intelligence Unit (EIU)[3], the banking sector is uncompetitive, fragmented, poorly developed, and suffers from poor corporate governance. Lending is low as a share of GDP, and the banking sector plays only a marginal intermediation role in the economy. State and elite influence over the sector is high. Lending is overwhelmingly focused on Baku, the capital, and is largely directed toward established medium and large enterprises. EIU experts claim that the outlook for the banking sector in the near term is poor. Low oil prices will keep the economy in recession this year, resulting in a fall in demand for credit and deterioration in asset quality. A large share of loans is denominated in foreign currency and is now nonperforming following the two devaluations of the manat in 2015. Dollarization of the economy is high, exposing the banking sector to ongoing exchange rate risks. The EIU expects further consolidation of the sector in the coming 2 years. There remains a risk of further depreciation or fluctuations of the manat, which would put the financial sector under added strain.

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[1] https://www.fimsa.az/assets/upload/files/Bank%20icmal%C4%B1_31%20dekabr%202017(1).pdf

[2] http://marja.az/mobile/?module=news&id=14076

[3] Industry Report: Financial services 3rd Quarter 2017 www.eiu.com/financialservices © The Economist Intelligence Unit Limited 2017

According to the Fitch ratings, the banking sector outlook for Azerbaijan is still negative, due to continued asset quality pressures[4]. The banking system remains quite small relative to the size of the economy. Even with high assets and the growth of loans and deposits in Azerbaijani banks over a few years, total banking assets were about 52.4% of GDP, with loans accounting for about 27.4% and deposits by individuals only 12.4% at the end of 2016 – a much lower ratio than the 35%–60% of GDP characteristic of the advanced transitional economies of Central and Southeastern Europe.

Below, in order to provide a general picture, key indicators of the banking sector are presented in Table 1.

**Table 1: Summary Banking Sector Statistics**

| No. | Banking Sector | 2005 | 2010 | 2015 | 2016 |
|---|---|---|---|---|---|
| 1 | Number of banks | 44 | 45 | 43 | 32 |
| 2 | Number of state-owned banks | 2 | 1 | 2 | 2 |
| 3 | Number of private banks | 42 | 44 | 41 | 30 |
| 4 | Assets (mln. AZN) | 2,252.0 | 13,290.8 | 34,906.0 | 31,439.5 |
| 5 | *Assets in GDP, in %* | *17.9* | *31.3* | *64.2* | *52.4* |
| 6 | Gross capital | 388.3 | 1,897.1 | 3,654.0 | 1,908.8 |
| 7 | *Gross capital in GDP, in %* | *3.1* | *4.5* | *6.7* | *3.2* |
| 8 | Total credits (mln. AZN) | 1,441.0 | 9,163.4 | 21,730.4 | 16,444.6 |
| 9 | *Total credits in GDP, in %* | *11.5* | *21.7* | *39.9* | *27.4* |
| 10 | *Total credit portfolio of nonbank finance institutions in mln. AZN* | *39.6* | *191.6* | *578.4* | *473.4* |
| 11 | The total loans in national currency in mln. AZN | 542.9 | 5,865.3 | 10,994.5 | 8,663.2 |
| 12 | The total loans in foreign currency in mln. AZN | 898.1 | 3,298.1 | 10,735.9 | 7,781.4 |
| 13 | *The loans to households in mln. AZN* | *389.2* | *2,700.8* | *8,383.6* | *5,858.7* |
| 14 | Total deposits in mln. AZN | 1,368.7 | 7,625.8 | 23,431.4 | 22,091.0 |
| 15 | Deposits in national currency in mln. AZN | 280.2 | 3,205.3 | 4,301.7 | 5,459.0 |
| 16 | Deposits in foreign currency (mln. AZN) | 1,088.5 | 4,420.5 | 19,129.7 | 16,632.0 |
| 17 | *Dollarization of deposits* | *79.5* | *58.0* | *81.6* | *75.3* |
| 18 | Deposits of households in mln. AZN | 494.5 | 3,029.8 | 9,473.9 | 7,432,1 |
| 19 | Deposits of financial organizations in mln. AZN | – | 2,177 | 6,358.8 | 4,509,5 |
| 20 | Deposits of nonfinancial organizations in mln. AZN | 874.2 | 2,419 | 7,630.4 | 2,256,3 |
| 21 | Foreign debt of banking sector | 158.2 | 2,470.4 | 8,204.5 | 7,224.817 |

Source: Central Bank of Azerbaijan Republic (CBAR).

## 2.2 Nonbank Credit Institutions (NBCIs)

Microfinance first started in the middle of the 1990s with the participation of international NGOs, and over time, the sector grew steadily. However, double devaluations have affected not only the banking sector but also nonbank credit organizations. As a result of these devaluations, the number of nonbank credit institutions (NBCIs) and other participants in financial markets has decreased during the last 2 years due to the cancellation of the licenses of 13 NBCIs. At the end of 2016,

[4] http://en.apa.az/azerbaijan-economy/finance-news/fitch-our-sector-outlook-for-azerbaijan-still-negative-due-to-continued-asset-quality-pressure.html

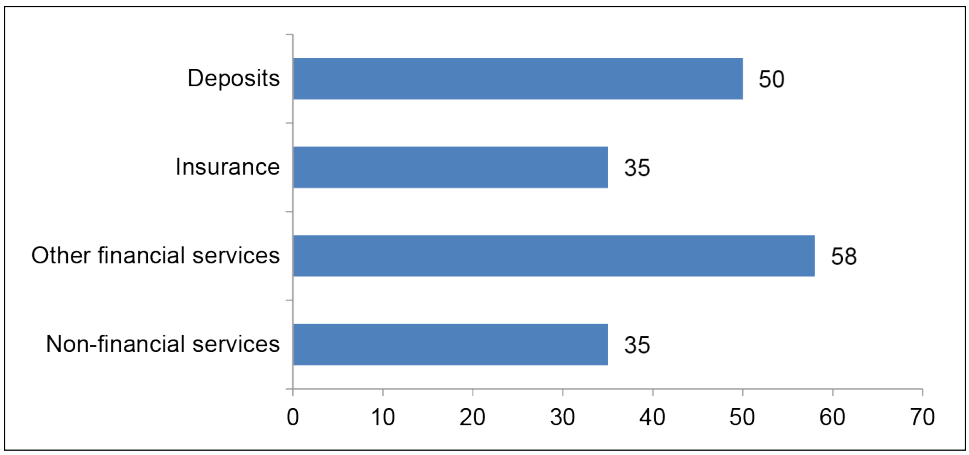
the number of NBCIs was 144, including nonbank credit organizations (47) and credit unions (97). For comparison, note that 157 NBCİs, including 48 nonbank credit organizations, and 109 credit unions were operating in Azerbaijan at the end of 2015. In the same period, a weakening in the quality of the portfolio reduced the number of customers and assets, resulting in NBCIs facing loss.

Even so, microfinance has not yet reached its potential. This has been strongly highlighted by the World Bank[5]: "The non-bank credit sector is underdeveloped and offers limited opportunities for Azerbaijani SMEs." The combined microfinance loan portfolio is still only about 1% of GDP, despite considerable demand for microfinance services. Sector concentration is high, with the two largest providers of microfinance, Access Bank and FINCA, together accounting for 46% of the market. According to Suleyman Kalashov, chairman of the Azerbaijan Microfinance Association (AMFA),[6] "customers of microfinance institutions have sharply declined in the past 3 years; the microfinance institutions had 600,000 customers in 2015. Customers fell to 298,000 in 2016 and 118,000 in the first 9 months of 2017. Besides, the microfinance institutions' loan portfolio amounted to $348 million in 2015, and $80.1 million in the equivalent period of 2017."

He noted that microfinance organizations issue loans at 40% per annum, but only solving liquidity problems would create an opportunity to lower loan interest.

Initially, the products offered for microfinance were mainly micro, small, and medium business loans and agriculture. However, as more and more institutions entered the market, they started to diversify their product range to include consumer loans, loans for travel or medical purposes, education loans, emergency loans, and other specialized loans. Nonbank Credit Institutions are not allowed to take deposits. Thus NBCIs offer only loan products while banks also offer mobile banking and express loans, along with their deposit products.

**Figure 1: Product and Service Offering NBCIs**




Source: Azerbaijan Micro-finance Association (AMFA).

[5] The World Bank's Report No. 89360 "Azerbaijan Economic Diversification and Growth, Access to Finance: Measure to Ease a Binding Constraint" September 2013.

[6] http://en.apa.az/azerbaijan-economy/finance-news/amfa-microfinance-institutions-see-sharp-decline-in-clients.html

Below, in order to provide a general picture, key indicators of the nonbanking sector are presented in Table 2.

**Table 2: Summary Microfinance Sector Statistics**

| Number | Microfinance Sector | 2015 | 2016 |
|---|---|---|---|
| 1 | Number of microfinance institutions | 157 | 144 |
| 2 | Number of nonbank credit organizations | 48 | 47 |
| 3 | Number of credit unions | 109 | 97 |
| | Number of customers | 600,000 | 298,000 |
| 4 | Assets (mln. AZN) | 614 | 3,897.7[7] |

Source: Central Bank of Azerbaijan Republic (CBAR).

# 3. STATUS OF FINANCIAL INCLUSION FOR INDIVIDUALS AND SMES

One of the major factors preventing the development of SMEs is inadequate access to financial resources. It is worth highlighting that the conducting of evaluation of an enabling business environment by different international agencies in the country has shown that entrepreneurship subjects are encountering difficulties in attracting the required financial resources.

The statistical data provided by the World Bank and State Statistical Committee in Azerbaijan do not disclose the process related to the distribution of allocated credit investments for entrepreneurship by the size of enterprises. In spite of this, it is worth emphasizing several factors contributing to the poor access of SMEs to credit resources based on conducted analysis and surveys.

Azerbaijan's overall score was 38, ranking it in 38th place out of 55 countries scored under Microscope 2014[8] for the financial inclusion level. Within the seven states covered in the report from Eastern Europe and Central Asia, Azerbaijan ranked in 5th place. In Eastern Europe and Central Asia three of the countries included in 2014 – Armenia, Azerbaijan, and Georgia – have been dropped from the Index, while the Russian Federation was added in 2015.

According to the 2014 World Bank Global Financial Inclusion (Global Findex) Database,[9] almost 30% of adults have accounts at a formal financial institution, and the operating environment in Azerbaijan is reasonably conducive to financial inclusion. The 2014 Global Findex Database shows that the Azerbaijan financial inclusion level is higher than Armenia and less than Georgia (see Table 3). The penetration rate in Azerbaijan is well below some transition countries and the EU.

[7] The sharp increase in assets is due to the International Bank's purification of toxic assets of 3 billion manat by Aqrarkredit, a stock credit organization (can you explain a bit more about "purification"?).

[8] https://centerforfinancialinclusionblog.files.wordpress.com/2014/11/eiu_global_microscope_2014.pdf

[9] http://documents.worldbank.org/curated/en/187761468179367706/pdf/WPS7255.pdf#page=3

**Table 3: Account Penetration**[10]

| | **Account** (% Age 15+) | | | | |
|---|---|---|---|---|---|
| | **All Adults** | **Women** | **Adults Belonging to the Poorest 40%** | **Young Adults** (% Ages 15–24) | **Adults Living in Rural Areas** |
| Azerbaijan | 29.2 | 25.9 | 26.9 | 10.0 | 30.1 |
| Armenia | 17.7 | 14.7 | 10.9 | 10.4 | 15.5 |
| Georgia | 39.7 | 39.8 | 28.6 | 9.9 | 40.1 |
| Europe and Central Asia | 51.4 | 47.4 | 44.2 | 35.6 | 34.7 |

Source: Financial Capability and Inclusion Survey Report (2015).

The results analyzed in the framework of FCIS[11] have proven that the Azerbaijan financial inclusion level rose from about 15% in 2011 to 29% in 2014 (Findex) and 36% in 2015 (FinCab).[12] When investments, private pensions, and insurance products were included as formal financial products, the survey found that 47.2% of Azerbaijani adults use some formal financial product. According to the FCIS, there is a strong correlation between income level and financial inclusion. In fact, the gap in financial inclusion between the richest and the poorest quartiles is 22.9%, corresponding to nearly half of that of the richest quartile. Adults who are out of the labor force were found to be 6% less financially included than the average employed. Size of household is correlated with financial inclusion. However, there is only a 3.1% average difference between the smallest and the largest size. There is only a small difference in financial inclusion between genders overall, but an in-depth analysis suggests that younger women have lower financial inclusion levels than younger men as the backdrop to their lower economic participation. When the sample is broken down into age groups, we note, overall, that there is a marked difference of inclusion in favor of younger male respondents in Azerbaijan (between the ages of 18 and 20, financial inclusion is 5.2% higher for men). Inclusion tends to become more or less gender-neutral between the ages of 21 and 55, and then it reverses in favor of female Azerbaijanis (from the age of 56 financial inclusion is 5.7% higher for women). This pattern suggests degradation in the younger generation of women compared to their elders.

According to the 2015 Financial Capabilities Survey, around 36% of the surveyed adults in Azerbaijan report owning an account at a formal financial institution (a bank, an MFI, or an e-money agent), a commonly used metric for international comparison. Compared to other upper-middle-income economies, Azerbaijan is behind the average level regarding financial inclusion, commercial bank branches, and domestic credit provided by the financial sector (see Tables 3 and 4).

The total number of bank branches in Azerbaijan per 100,000 inhabitants is about 10.7, which is much lower than in Armenia (22) and Georgia (27). As for the number of automatic teller machines (ATMs) per 100,000 adults in Azerbaijan, this indicator is behind that of its neighbors and the average region. Due to the decline in the number of ATMs and the increasing population over the past year, the number of ATMs per 100,000 people increased from 20.5 in 2010 to 28 in 2015. For comparison, the world average for 2015 was almost six ATMs per 1000 adults. This indicator is 50% better than the relevant index for Azerbaijan. The same trend was observed in the number of

[10] http://pubdocs.worldbank.org/en/215611483565355628/LDB-2015-final.pdf

[11] http://documents.worldbank.org/curated/en/880631470853969754/pdf/107748-WP-P125462-PUBLIC-10-8-2016-12-5-10-AzerbaijanEnhancingFinancialCapabilityandInclusionFINAL.pdf

[12] Data on formal account ownership are drawn from the 2015 Financial Capabilities Survey (Azerbaijan).

POS (point of sale) terminals in 2016. According to the CBAR, most ATMs and POS terminals are constructed in the capital city. Thus, in 2016, 53.87% of ATMs and 56.4% of POS terminals functioned in Baku, although, according to official figures, only a quarter of Azerbaijanis live in Baku.

**Table 4: Measures of Financial Inclusion and Development across Economies**

| | **Automatic Teller Machines (ATMs)** (per 100,000 Adults) | **Commercial Bank Branches** (per 100,000 Adults) | **Firms using Banks to Finance Investment** (% of Firms) |
|---|---|---|---|
| Azerbaijan | 32.72 | 10.7 | 27.1 |
| Armenia | 61.14 | 22.0 | 17.4 |
| Georgia | 74.31 | 27.0 | 22.0 |
| Europe and Central Asia | 59.99 | 22.3 | 24.3 |

Source: Data on formal account ownership are drawn from the 2015 Financial Capabilities Survey (Azerbaijan) and 2014 Global Findex (other economies).

According to the WBG Financial Capability Survey, Azerbaijan 2015, regional differences do exist in respect of financial inclusion. However, they remain small to moderate. Ganja-Qazakh has the highest level at 38.3%, which is 5.2% above the national average. Shaki-Zaqatala has the lowest level at 32.3%, which is 11.3% below the national average. The next highest levels are in Daglig-Shirvan and Absheron-Baku where financial inclusion is 3.5% and 1.1%, respectively, above the national average.

## 3.1 Accounts

In Azerbaijan, bank accounts are the most commonly used financial product. According to the FCIS report, about a third of the population reports having this product; however, almost everybody, whether men or women, urban or rural, rich or poor, know about the services offered by banks. The most notable difference is that about 17% more rich people than poor have bank accounts (44% versus 27%). In general, 34% of the population currently have a formal bank account, 84% claim to have used banks in the past, and 98% know about services offered by banks. At the regional level, the usage of bank accounts does vary moderately between regions: The spread between the highest and lowest usage of a bank account is 9%. There is a positive connection between the regional level of wealth as measured by income per capita and the holding of bank accounts. However, there is a strong negative correlation between the historical and current holding of bank accounts. In fact, regions with a high usage of bank services in the past tend to have the lowest holding of bank accounts at present and vice versa. This may suggest that many users of bank services in the past were dissatisfied and decided to revert to other mechanisms.

According to the latest data from 2017, the number of bank customers equaled 5,352,456 people, and the number of accounts equaled 15,161,312. Compared with the previous year, the total number of customers declined by 6.35%, the number of individual customers of banks fell by 5.78%, and the number of unique customers engaged in entrepreneurial activity fell by 4.71%. Bank customers as a legal entity sharply declined from 36% in 2016 compared with the equivalent period of 2015.

At the beginning of 2017, the number of bank customers accounted for 54.6% of the total population and 71.2% of the population aged above 15.

In 2016, there were more closed customer accounts than there were bank customers. This can be explained by the fact that most individual customers kept one of their many previous bank accounts. In the same period, credit accounts declined by 26.1% and deposit accounts fell by 17.83%. This negative trend can be explained mainly by the increase in credit risk and the depreciation of deposits with the national currency.

## 3.2 Credit

After the devaluation of the manat, the commercial banks changed their lending policy, refused to give loans in manat, and increased the number of loans in dollars, thereby reducing the number of citizens who went to banks. Azerbaijani banks offer costly lending terms, usually 10–15 %, but occasionally higher, in dollar-denominated loans with a maximum two-year term. Many Azerbaijani firms cannot afford such loans and turn to private sources (i.e., personal deals) for finance. According to the Central Bank of Azerbaijan, before the devaluation in 2015, the average lending rate of the banks in Azerbaijan amounted to 13.6% in local currency, compared to 13.81% in 2014. After devaluation at the end of 2015, the average interest rate was 13.76% in the national currency and 13.74% in foreign currency. There was a small difference between manat and US dollar loans in 2015, but after devaluation, the difference began to increase gradually. Thus, at the beginning of 2017, the average interest rate was 12.05% in the national currency and 8.60% in foreign currency. Nevertheless, due to the high risk and double-digits inflation rate, in 2017, loan interest rates increased again and as a result of this trend the difference between currencies decreased. Due to high inflation rates and economic uncertainty, banks find it disadvantageous to provide long-term loans or grace period loans, which are important for new businesses. As a rule, access to credit is on the banks' terms, which include interest rates, securitization of credit, and period of borrowing. Such conditions seem unfavorable for SMEs to take loans from the banks and show relatively high maintenance costs associated with small deposits or loans.

According to the CBAR, the average deposits and interest rates are going down; nevertheless, loan interest rates are high, especially in foreign currency. As for the loan interest rate in the national currency, at present, it is less than the inflation rate in the same period.

**Table 5: The Structure of Loans to the Economy by Type of Credit Institution**
(End of Period)

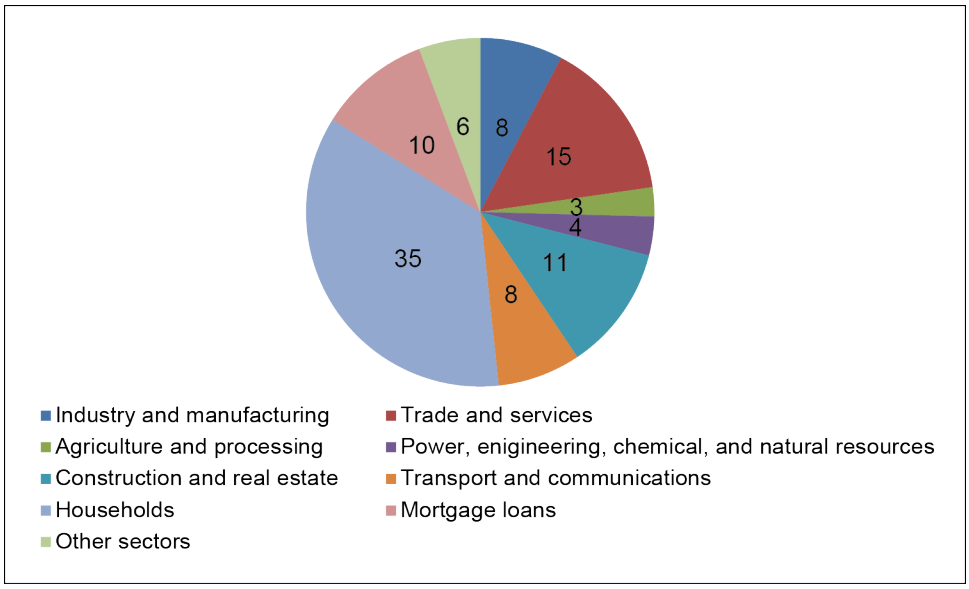
| Year | Total Loans | State Banks | | Private Banks | | Nonbank Institutions | |
|---|---|---|---|---|---|---|---|
| | | In AZN | % | In AZN | % | In AZN | % |
| 2005 | 1,441.0 | 748.3 | 51.9 | 653.1 | 45.3 | 39.6 | 2.7 |
| 2010 | 9,163.4 | 3,901.9 | 42.6 | 5,069.9 | 55.3 | 191.6 | 2.1 |
| 2015 | 21,730.4 | 7,289.3 | 33.6 | 13,875.2 | 63.8 | 566.0 | 2.6 |
| 2016 | 16,444.6 | 5,749.2 | 35.0 | 10,222.0 | 62.2 | 473.4 | 2.9 |

Source: Central Bank of Azerbaijan Republic.

As you can see from Table 5, the total loan portfolio of banks and nonbank institutions decreased by 24.3% at the end of 2016 compared to 2015. As a result of the structural change, the share of nonbank institutions in the total credit portfolio increased by 0.7%, but still, input from nonbank institutions remains low.

The sectoral breakdown of loans in 2016 is presented in Figure 2.

**Figure 2: Sectoral Breakdown of Loans in 2016**
(%)




Source: Central Bank of Azerbaijan Republic.

As you can see from Figure 2, 45 % of credits were invested in the industry and manufacturing, and trade and services sectors in 2016.

According to the 2014 Findex survey, bank credit was used by 19% of the population in Azerbaijan, as a result of formal borrowing over the age of 15 in Azerbaijan being higher than in Georgia, but less than in Armenia. Domestic credit provided by the financial sector accounted for 33.7% of GDP, almost twice less than the regional average (see Table 6).

**Table 6: Formal Saving and Formal Borrowing**

| | **Formal Saving** (% Age 15+) | **Formal Borrowing** (% Age 15+) | **Domestic Credit Provided by Financial Sector** (% of GDP) |
|---|---|---|---|
| Azerbaijan | 5 | 19 | 33.7 |
| Armenia | 2 | 20 | 47.2 |
| Georgia | 1 | 14 | 45.3 |
| All upper middle income | 32 | 10 | |
| Europe and Central Asia | 8 | 12 | 69.1 |

Source: Data on formal account ownership are drawn from the 2015 Financial Capabilities Survey (Azerbaijan) and 2014 Global Findex (other economies).

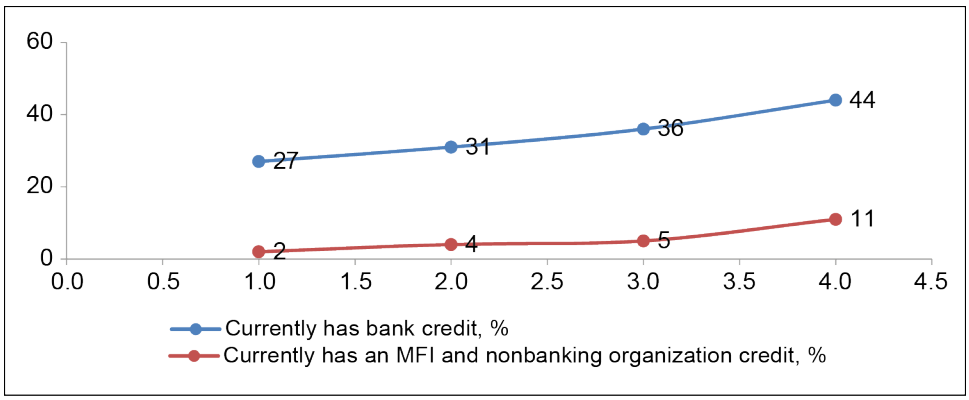
According to the Financial Capabilities Survey in Azerbaijan 2015, about 4% more people utilize bank credit in urban than in rural areas. About 3% more people have credit cards in Baku than in the rest of the country. The urban population uses formal credit (16%) and credit cards (9%) more than their rural peers (12% and 7%, respectively). Most people living in Baku use credit cards; in fact, 12% of Baku inhabitants hold credit cards compared to 8% nationally. On the other hand, most bank account holders (about 22%) own a debit card, which are utilized more by rich people (32%) than by poor people (18%).

As for transactions with debit and credit cards, trend analyses of financial transactions with debit and credit cards show that although the number of social and salary cards have increased, the number of total payment cards has declined in recent years. In terms of the structure of the cards, we can see that the number of salary and social cards accounted for 76.35% of all cards functioning in the last year. One of the results is that at least a quarter of the bank cards in Azerbaijan are for mandatory payments. At the same time, it is noteworthy that only 11.82% of the current cards are credit cards, and they decreased in number by 37.5% in 2016 compared to 2015.

The decline in the number of credit cards can be explained by the closing of 11 banks in the past 2 years, as well as the increased credit risk management and reduced trust in banks of the population. Another factor is that individual bank customers preferred to avoid risk by closing their card accounts during the crisis period due to the low financial literacy of the people.

According to the WBG Financial Capability Survey, Azerbaijan 2015, approximately half of the population does not borrow money, and among those who do borrow money, informal credit is the preferred mechanism. Furthermore, 11% more poor people than rich have informal credit and 6% more rich than poor have formal credit. As can be seen, 14.51% of the population has no credit whatsoever. Informal credit is the most popular borrowing method with 15% more than formal credit. There is little difference between men and women in borrowing statistics overall. Nevertheless, variations worthwhile mentioning are in respect of socioeconomic and demographic factors. In fact, 27% of informal credits are found among the poor and 20% among the rich. These findings seem to confirm the argument that poor people are more likely to work independently or informally in the private sector than their rich counterparts, and as such are less likely to obtain bank credit.

**Figure 3: Use of Banks, MFIs, and Other NBCIs by Income Quartile**




Source: WBG Financial Capability Survey, Azerbaijan 2015.

Banks are not interested in allocating financial resources to regions. Besides observing a decline in the flow of credit investments from the capital to regions, annual interest rates on credit are also skyrocketing. One of the financial problems faced by SMEs operating in the regions is high-interest rates and barriers to accessing long-term credit. It is worth underlining that those entrepreneurs that partook in the survey of the Qabus Research & Consulting Company have especially highlighted this problem.

## 3.3 Insurance

At present, Azerbaijan's insurance market is at the very beginning of the development process. That is, despite the fact that today's insurance market and the potential of the country's economy are higher than the current situation, the insurance market has been experiencing a decline in recent years. There are various objective reasons for this: the lack of information on the majority of insurance products, the lack of trust in the insurance companies, the insufficient types of compulsory insurance, and the lack of control mechanisms for the sale of existing mandatory insurance products.

According to the experience of developing countries with stable economies, a minimum of 2% of GDP should be insurance premiums. The insurance premiums/GDP ratio is low in Azerbaijan, standing at just 0.73% in 2016 (up from 0.68% in 2015). Nonlife insurance overwhelmingly dominates the take-up in insurance premiums. Tax incentives for life insurance schemes are currently limited to just 3 years, thereby reducing their attractiveness.

Insurance is still nascent in Azerbaijan, and the sector remains small, although the government has started to support its development by strengthening the environment and introducing mandatory insurance. Unfortunately, between 1995 and 2003 the total number of insurance companies declined from 71 to 29. By 2012, the sector comprised 29 insurance companies, one reinsurer, seven brokers, about 200 agents, and the Association of Azerbaijani Insurers. Total assets accounted for less than 1% of GDP. The industry is moderately concentrated, with the ten leading insurers accounting for 75% of premiums in 2012. Many insurance companies are linked with banks. However, most insurance companies focus on specific products, such as medical, motor, life insurance, and real estate.

According to the WBG Financial Capability Survey, Azerbaijan 2015, approximately one half of the population has used an insurance product in the past but less than one out of ten persons, and in particular only 3% of rural people, currently have an insurance policy, suggesting a strong need for improvement. Furthermore, 30% of the population has no idea about services offered by insurance companies. The usage of insurance products tends to increase with household size; however, there is a notable difference between urban and rural areas. In fact, four times more urban than rural people currently have an insurance policy. This is rather astonishing, especially for agriculture in rural areas where there are few buyers of harvest insurance allowing smooth fluctuations in household income due to seasonality.

The usage of insurance varies significantly between regions, and there is a correlation between the usage of such services and regional wealth. According to the 2015 Financial Capabilities Survey, the spread between the highest and lowest usage of insurance services is more than 10%. It is notable to see that the largest users of insurance products are based in Absheron-Baku and Daglig-Shirvan, the two wealthiest regions in Azerbaijan.

In summary, sector segmentation is high and competition limited, thereby having a negative impact on quality and product cost.

## 3.4 Pensions

At the beginning of 2018, the number of pensioners in Azerbaijan amounted to 1,320,400 people or accounted for 13.5% of the total population. Azerbaijan has a universal pension system. The state pension converted from a pay-as-you-go legacy system inherited from the Soviet era to a defined contribution system in 2001. This

pension reform concept in the Azerbaijan Republic lays the groundwork for a privately funded pension system. The Law on Nonstate Pension Funds is prepared but has still not been passed as the government is concerned that the financial markets are not yet well developed enough. Private pensions do not exist. The current average retirement pension is $120 per month. The International Bank of Azerbaijan and Kapital Bank are the only banks authorized to provide pension services. There is no existing private pension fund in Azerbaijan.

## 3.5 Remittances

In recent decades, permanent and temporary labor migration remarkably gained significance in all CIS countries. While some states, such as Armenia, Azerbaijan, Moldova, Tajikistan, and Uzbekistan, are predominantly labor-exporting regions, the Russian Federation is an immigration as well as an emigration country. According to unofficial data, around 2 million legal and illegal Azerbaijani workers are employed in the Russian Federation. Citizens from Azerbaijan can enter the Russian Federation without a visa, but they have to register with the local authorities to be eligible for a work permit. The majority of foreign workers from Azerbaijan in the Russian Federation are men, and they predominantly work in construction, services, trade, and agriculture. Connected to labor migration, the receipt of remittances (outflow) decreased between 2010 and 2016 (see Table 7). It should be additionally emphasized that official statistics on payments most likely underestimate the actual inflow of these resources to a considerable extent.

**Table 7: Transactions through Interbank Payment Systems**

| | Remittance system | | | | | |
|---|---|---|---|---|---|---|
| | Inflow | | | Outflow | | |
| **Year** | **Number of Transactions** (AZN thousand) | **Amount of Transactions** (AZN million) | **Amount per Transaction** (AZN thousand) | **Number of Transactions** (AZN thousand) | **Amount of Transactions** (AZN million) | **Amount per Transaction** (AZN thousand) |
| 2010 | 153.0 | 89.0 | 581.7 | 46.0 | 42.6 | 926.1 |
| 2015 | 215.8 | 130.4 | 604.6 | 116.9 | 76.5 | 654.4 |
| 2016 | 223.2 | 151.8 | 680.1 | 94.5 | 55.3 | 585.2 |

Source: Central Bank of Azerbaijan Republic.

Although the CBAR approved the “Guidelines on Cashless Settlements and Money Remittances in the Republic of Azerbaijan” on 17 September 2013,[13] so far, many migrants have transferred money outside the official channels, especially if they perform irregular work.

According to the WBG Financial Capability Survey, when receiving remittances from abroad, about one person in ten use Money Transfer Operators (MTOs), predominantly from poor and large households in urban areas, especially Baku. Some 12% of the population currently have money transfer products and more than a third have used such products in the past. Furthermore, three out of four persons know about services offered by MTOs. Such services were found to be utilized by 30% more people in urban areas (especially Baku), by 33% more people from poor households, and by about 20% more people living in the largest households. These facts underpin the notion that poor people receive more financial support from family and friends. In fact,

[13] https://en.cbar.az/assets/181/Guidelines_on_Cashless_Payments_and_Money_Remittances.pdf

37% of poor households declare receiving this kind of support as a household income source, while only 15% of the richest households affirm the same. MTO usage is linked to the remittance trend in Azerbaijan. In particular, Azerbaijan is among the top remittance-sending countries (25th position in the worldwide classification and 8th position among middle-income economies). Such remittances represent about 2.7% of GDP ($2.0 billions)[14].

## 3.6 Securities

According to the WBG Financial Capability Survey, more than one in 3 persons have used brokerage house products in the past, and a very small fraction of people currently have investments, whether male or female, urban or rural, rich or poor, which may highlight the lack of trust or interest in such products. Some 49% of the population know about the services offered by brokerage houses and 36% have utilized investment products in the past. However, only a mere 0.3% of persons currently hold an investment, perhaps due to bad performance. Rich people seem to know more about such products (57%) by a factor of 1.24 and have a 12% higher utilization rate than poor people (45% versus 33% of poor people). These results may also be associated with the fact that the brokerage industry is concentrated in Baku. In fact, there is only one authorized stock exchange in Azerbaijan, the Baku Stock Exchange (BSE). Furthermore, there are very few participants in the securities market: 12 brokerage companies, 13 dealers, three securities managers, one clearing house, two registrars, and two depositories.44 The first equity transactions at BSE were recorded in 2001. The corporate bonds market started in 2004. The number of joint stock companies registered in the stock market was 651.[15] People applying for membership shall meet the conditions set under the internal procedures of the Exchange. The eligibility of an applicant is assessed and decided by the Internal Membership Committee. Exchange membership is granted on the applicant's eligibility and conformity to the requirements. According to the BSE Membership Rules,[16] persons who apply for membership should be a joint stock company. Therefore, SMEs cannot be in the list on the stock market.

Although small, Azerbaijan's securities markets do contribute to capital mobilization. The basic institutional framework for the securities markets has been in place for more than a decade. The authorities are now strengthening it under the State Program for the Development of Securities Markets for 2011–2020 with World Bank support, alongside measures to strengthen the legal and regulatory framework.

## 3.7 Kinds of Financial Institutions Involved

Some other institutions are involved in this process, such as postal institutions and pawnshops. According to the FIMSA, the number of branches of postal institutions and the number of post offices of mail institutions with financial services equals, respectively, 63 and 1,111. There are 1,200 pawnshops.

[14] Migration and Remittances Fact Book 2016, World Bank Group 2016.

[15] OECD, Global Forum on Transparency and Exchange of Information for Tax Purposes Peer Reviews: Azerbaijan 2015, "Phase 1: Legal and Regulatory Framework," October 2015.

[16] http://bfb.az/wp-content/uploads/2015/06/Uzvluk-Qaydalari.pdf

# 4. BARRIERS TO FINANCIAL INCLUSION

## 4.1 Supply-Side Barriers

**4.1.1 Reduced number of banks and NBCIs and their branches.** During the last 3 years, the CBAR and FIMSA withdrew the licenses of 15 banks and 13 NBCIs. According to the report of the Financial Markets Supervision Authority, due to the crisis in the financial market, the number of branches of banks operating in Azerbaijan as of 31 December 2017 was 506. This is 63 branches less than at the end of 2016. The number of offices of banks operating in Azerbaijan as of 31 December 2017 was 142. This is 11 offices less than at the end of 2016. At the same time, according to the official information on 31 December 2017, the number of bank employees since the end of last year had decreased by 786 people, from 16,947 to 16,161. This means that there is not enough capacity to extend financial services to poorer households or SMEs.

**4.1.2 High interest rates on credits are one of the major factors preventing access of SMEs to credit resources.** The high interest rates on credit in the country are acknowledged at both the official level and by entrepreneurs as well. It should be noted that 38% of the respondents who participated in the survey conducted by the Qabus Research & Consulting Company with a view to finding out the level of access of SMEs to credit have indicated that due to high interest rates they did not address credit organizations. Moreover, 81% of the entrepreneurs who took part in this survey suggested lowering interest rates to increase access to credit funds. Additionally, the annual average interest rates of credit attracted by 85% of them were more than 20%. According to 87.4% of entrepreneurs, it is not a favorable environment for business when interest rates hit over 15%.

**4.1.3 Problems related to securing credit.** Azerbaijan legislation does not have a guarantee of credit mechanism for SME subjects. The same applies to both the insurance of risks concerning SME credit and guarantee of collateral security from this category. In other words, collateral is required for NFES credit just like other credit, and in this case, all responsibilities fall on the shoulders of entrepreneurship subjects.

**4.1.4 Lack of credit guarantee institutions.** One of the main reasons for refusal of commercial lending is the demand for credit guarantee requirements. An in-depth analysis shows that banks prefer real estate as collateral to secure credit. The fact that approximately 60% of entrepreneurs conduct their businesses on leased premises means that they can only use their living accommodation as collateral, which does not satisfy the banks. Also, because SME operations are not transparent, due to not keeping financial records, the banks cannot evaluate companies' operations, which in turn limits banks' ability to assess creditworthiness and possible loan issuance.

**4.1.5 Limited availability and quality of credit data.** The target market for these nonbanking credit institutions includes small farmers, trade and service SMEs, and individual enterprises, which mostly produce consumer goods, i.e., the target group for these microcrediting institutions mainly includes SMEs of various sorts. Not having accurate credit information on borrowers causes microcrediting organizations to introduce tougher requirements (e.g., higher interest rates, shorter terms) in order to

mitigate risk. Registry information does not offer a detailed analysis of the client. Unlike the registry, a credit bureau processes the information received: It generalizes, classifies, and sells clients' credit reports (histories) to the banks. The registry services include only a small portion of the bureau's possibilities.

**4.1.6 Poor and base types of financial products and services.** SMEs' and households' access to the modern variety of financial services is lower. There are not enough new players in financial markets, such as venture investment funds, business angels, crowdfunding platforms/campaigns, etc., and no access to alternative financial instruments like guarantees, bills, factoring, etc.

## 4.2 Demand-Side Barriers

**4.2.1 The poor mutual understanding between banks and SMEs**. All in-depth interviews with the entrepreneurs demonstrated that they had an imperfect knowledge and understanding of the services and information that banks offer. This corresponds to the lack of adequate and full information the banks have on their clients. Often business people who have never applied for credit complain about the terms and conditions offered by banks that they have learned by word of mouth rather than through direct experience with banks. Banks do not actively conduct information campaigns targeting SMEs and entrepreneurs insufficiently informed about the services they offer. In many respects, the attractiveness of any bank service often stems from advertisements and promotional campaigns aimed at promoting the service.

**4.2.2 Lower financial awareness.** A lack of financial literacy (management, procedures, and instruments) in an environment with complicated application procedures for bank loans and high financing costs (interest rates, transaction costs, etc.) creates a substantial disadvantage for SMEs. The increased incidence of parallel borrowing and raising of overindebtedness coupled with the massive dollarization or withdrawal of savings from banks indicates the need for increased financial literacy and education to reach a healthier and more stable microfinance sector through client-focused activities (along with other bank-level measures for internal pro-client campaigns, rescheduling, new risk management/hedging, etc.) and education for long-term saving and investment opportunities.

**4.2.3 Lost client trust.** Decreasing long-term savings, investments, and the need for banking services. This factor affects the reputation of the banking sector in the market and is negatively expressed by a worsening of the client repayment culture.

## 4.3 Institutional Aspects

The most significant institutional constraint noted by banks is the absence of a collateral registry system for movable collateral (other than vehicles). As a result, collateral requirements tend to be somewhat strict in Azerbaijan. Most lenders require that real estate collateral covers a significant portion of the loan value, and several only accept real estate collateral in practice. A draft law for a free collateral registry was prepared in consultation with the IFC. There are a few other constraints, although they are less critical than the collateral registry issue. The public credit bureau, which is managed by the central bank, does not include information from public utilities,

cellphone companies, and other providers who would be relevant for assessing credit risk and avoidance of overindebtedness. There is currently an effort underway to start Azerbaijan's first private bureau, which may help to resolve this issue. Another constraint is the long time to determine bankruptcy and low average recovery rates (1.5 years and 39.6 cents in the dollar, respectively, according to the World Bank's Doing Business 2017), which discourages lending, particularly to higher-risk applicants such as startup companies.

## 4.4 Bankruptcy Law

Azerbaijan's Bankruptcy Law, which does not function efficiently and is rarely used, continues to be a hindrance to economic development, as do the country's weak credit-reporting institutions. Under this law, which applies only to legal entities and entrepreneurs, not individuals, bankruptcy proceedings may be started either by a debtor facing insolvency or any creditor. In general, the legislation is focused on liquidation procedures. For example, a court-approved "rehabilitation plan" may not exceed 2 years.

In the country ranking of the World Bank's Doing Business Report on the ease of "resolving insolvency," Azerbaijan ranks 86th out of 189 countries in this category.

## 4.5 Land Registry

Registration of the land, as well as the property, takes place simultaneously at the State Committee on Property Issues of the Republic of Azerbaijan.

In accordance with the Resolution of the Cabinet of Ministers of the Republic of Azerbaijan No. 266 dated 31 July 2014, the electronic service on "receipt of applications and documents for issuance of technical documents (passport and plan) regarding real estate registered in the state registry of real estate at the discretion of the owner" added to the list of electronic services provided by the State Registry Service of Real Estate.

The Collegium of the State Committee on Property Issues approved on 18 November 2014 the administrative regulation on the receipt of applications and documents for the issue of technical documents (passport and plan) regarding real estate registered in the state registry of real estate at the discretion of the owner. With these materials, it has become possible to apply for technical documents (passport and plan) via an online procedure.

# 5. REGULATORY FRAMEWORK

The regulatory framework is conducive to the development of the banking sector, and the state has provided adequate, timely support to banks in the past in times of stress. Banking regulations are mostly in line with international standards, with no unusually burdensome requirements.

The CBAR, formerly known as the National Bank of Azerbaijan, was the central regulatory body until the creation of the Financial Markets Supervisory Authority in early 2016. The CBAR continued its policy of ensuring financial sector stability and sustainability in 2015 and undertook some policy actions to that end. New capital adequacy requirements came into force in January 2015, and all banks were either able to comply or given additional time to do so. The largest banks, which hold 85% of all banking assets, already met the new requirements. The FMSA is likely to continue

similar policies of financial sector stability. The CBAR now focuses on monetary policy and exchange rate stability.

As you can see from the activities mentioned above, the CBAR is the primary regulator implementing licensing, supervising, enforcement, and reporting requirements for all banks and NBCIs. The Law on Banks (2004) defines the principles, rules, and standards of organization, internal management, and regulation of activities and liquidation of banks. The purpose of aligning the legal framework of the banking system with international standards is to increase the role of banking services in the economy, enforce the protection of bank depositors and creditors, and maintain the stable and safe performance of the banking system.

The Ministry of Finance regulates insurance companies. Leasing companies are controlled by the Tax and Civil Code Authority of Azerbaijan. The CBAR does not regulate retail shops and informal sector financial service providers like pawnshops, moneylenders, and lotteries (informal savings mechanisms).

The Azerbaijan microfinance sector is served by a diverse set of financial service providers including regulated and nonregulated entities. The CBAR regulates banks and nonbank credit organizations. NBCIs include nonbank credit institutions that offer microfinance as well as credit unions. Also, the NBCI category comprises Azerpost, foreign exchange providers, consumer finance companies, and payment and money transfer service providers.

All financial institutions report performance statistics to the CBAR and online Centralized Credit Registry. Additionally, 38 members of the Azerbaijan Micro-Finance Association report to AMFA on a monthly basis through a MATRIX report covering 10 indicators.

The CBAR licensed exchanges in the country; however, after the devaluation of the manat by 50% in December 2015, the CBAR issued a decree on waiving the license of all transactions in the nation (13 January 2016). Therefore, exchanging currency can currently only be done in the banks.

Pawn businesses also play a part in meeting poor people's urgent need for cash. Opening a Lombard business in Azerbaijan does not require a license, and they are not regulated. They register as an LLC at the respective regional department of the Ministry of Taxes; therefore, their reporting requirements are similar to those of any LLC operating in the country.

## 5.1 Licensing, Status of MFIs

Registration, licensing, and regulation of financial institutions managed by the Central Bank of Azerbaijan. According to the legislation, charter capital for registering an NBCI (nonbank credit institution) should be AZN300,000 whereas for the banks this is AZN50 million.

The Law on Nonbank Credit Organization (2010) defines the rules on the establishment, management, and regulation of nonbank credit institutions with the aim of better meeting the demand of legal entities and individuals in the Republic of Azerbaijan for financial resources and creating suitable conditions for access to financial services. The Law on Credit Unions (2000) determines the economic, legislative, and organizational basis for the establishment and operation of credit unions.

Azerbaijan has laws for nonbank credit institutions rather than defined "microfinance" laws and allows for a greater number of permitted activities, although deposit-taking is expressly forbidden for nonbank credit institutions. In Azerbaijan, NBCIs are divided into two groups – those with the right to accept collateral deposits and those without that right. NBCIs that receive a license to provide loans can also undertake the following activities: (i) purchasing and selling liabilities (factoring, forfeiting); (ii) leasing; (iii) registering of notes; (iv) provision of guarantees; (v) provision of services or insurance agents; and (vi) provision of consulting services on financial, technical, and management issues to borrowers and collective borrowers. Azerbaijan is also the only country in Central Asia where insurance agent services are among the list of permissible activities. The NBCI Law does not provide for foreign exchange operations.

## 5.2 Scope of Supervision and Regulation, Including Provisions for Maintaining Financial Stability

The Financial Stability Council (FSC) was established to maintain macroeconomic and financial stability in the country at the decree of the president of the Republic of Azerbaijan on 15 July 2016. The FSC helps to achieve systemized coordination of activities aimed at ensuring macroeconomic and financial stability. The FSC mobilizes all resources to enable a more accurate determination of the macro-framework, and ensure that fiscal and financial policies supplement each other.

## 5.3 Consumer Protection, Including Disclosure, Interest Rate Caps

Consumer protection is becoming an important element of the financial sector stabilization and development agenda in Azerbaijan. The reduction of oil prices and weaker macroeconomic fundamentals at the backdrop of negative external shocks have led to the devaluation of the national currency and erosion of public trust in the financial sector. Restoring financial stability, renewing public and investor confidence, and mobilizing higher savings to finance growth are the top priorities of Azerbaijan policy makers. The authorities increasingly discuss the issues of consumer and depositor protection, responsible lending, and access to finance.

Another important finding of the WBG Financial Capability Survey is that 12% of the respondents experienced financial service provider conflicts, the majority of whom did not try to resolve the conflicts they encountered. Less than 20% of those Azerbaijani adults who encountered a dispute took action to try to resolve it. Interestingly, twice as many of those who did not experience a conflict (40%) stated that if they faced one, they would try to resolve it.

With regard to actions taken in the event of a dispute, internal complaints handling systems and legal courts were hardly ever sought by those who experienced conflict with their financial service provider. The most common actions taken to try to resolve disputes were submitting a claim to the appropriate government authority (57%) and stopping using the services before the contract expired (36%). Only around one in five reportedly submitted a grievance to the company that sold the product (19%), while around 7% approached the legal courts.

In general, the main causes of inertia are either related to perceived power imbalances between financial service providers and their clients or to a lack of trust in, or awareness of, respective government authorities that can be approached in the event of a dispute. More than two-thirds of those who did not take any action to resolve a

dispute reported that the main reason for the inertia was that they perceived financial institutions as being too powerful. Slightly fewer, 61%, indicated that they thought the government authorities did not work properly, followed by 52% who were not aware of any government agencies they could approach for help. Slightly more than a third of those who did not try to solve a conflict mentioned that they did not take any action because they thought the law does not adequately protect consumers. Only 3% of those who did not take any action to resolve a dispute declared that they were too shy to redress the dispute.

There are official guidelines from the Central Bank of Azerbaijan dated December 2013 on "Dealing with the Appeals of Financial Service Consumers," which provide clear guidance on how to build an effective system of responding to and processing complaints, suggestions, and any other appeals from clients.

## 5.4 Deposit Insurance

The Azerbaijan Deposit Insurance Fund (ADIF) was founded on 12 August 2007, after the law on deposit insurance adopted by the parliament of the Azerbaijan Republic. The purpose of establishing the deposit insurance scheme is to prevent the risk of losing money deposited by individuals and to ensure the sustainability and development of the financial and banking system whenever banks and local branch offices of foreign banks become insolvent. Since 24 February 2015, deposits with an annual interest rate of 12% and less have been protected deposits, and in the case of an insurance event only a maximum of AZN30,000 of preserved deposits are compensated. The original cap of AZN6,000 was raised to AZN30,000 recently to prevent bank runs in connection with the deepening global economic crisis. Starting on 2 March 2016, deposits were accepted by the fund's member banks with an annual interest rate of 3% in the foreign currency and 15% in the national currency, fully insured for 3 years. According to the rule of law "on deposit insurance," interest on deposits shall be paid in the amount accrued by the date of the insurance event.[17]

After the revoking of the licenses of 11 banks by the FMSA, as of 27 September 2017, AZN437,741,000 (99.2% of the total compensation obligation) and AZN3,413,000 were reimbursed to depositors protected by the ADİF. The ADİF only provides insurance for depositors, not for investors.

## 5.5 Fintech-related Regulation and Receptivity to Financial Innovation

According to the Global Innovation Index (Gİİ) 2017[18], Azerbaijan ranked 82nd among 127 countries. According to the 2016 Fintech index[19] results, in terms of demand versus country risk, Azerbaijan is in the list of lower Fintech needs that meet a relatively unstable political environment. In the unit of Fintech index results, in terms of demand versus supply, Azerbaijan is in the list with countries where more moderate Fintech needs meet a supportive Fintech environment. In the group of Fintech index results, in terms of infrastructure versus ecosystem, Azerbaijan includes easy implementers, while good support meets a favorable business environment. The 2016 Fintech index report shows that Fintech-related regulation is weak, but the potential is high due to good infrastructure.

[17] http://adif.az/?~/eng/content/full/45

[18] http://www.wipo.int/edocs/pubdocs/en/wipo_pub_gii_2017.pdf

[19] https://www.slideshare.net/ING/fintech-index-report-2016

After 2013, digital financial services started to be integrated into banks' operations and then gradually integrated by the large NBCIs. Mobile banking is also a part of most banks' services that are being developed and expanded by and within the financial institutions. Payments are available through national payment terminals – E-Manat, Million, etc.

# 6. POLICIES TO PROMOTE FINANCIAL INCLUSION

## 6.1 Contents of National Strategy

On 06 December 2016, the president of the Republic of Azerbaijan approved strategic road maps on national economic perspectives and 11 sectors. The Strategic Road Map for the prospects of the national economy of the Republic of Azerbaijan covers the short-, medium-, and long-term horizon and comprises the economic development concept and action plan for 2016–2020, the long-term outlook by 2025, and the target outlook for the period after 2025. According to the SRM, Azerbaijan will develop a competitive environment enabling equal access to the fourth wave of industrial revolution technologies, markets, and finance. One of the 11 Strategic Road Maps covers the development of financial services in the Republic of Azerbaijan.

The Strategic Road Map for the development of financial services contains the following strategic targets:

- Establish a financial system comprised of dynamic and sound institutions
- Develop the financial markets
- Strengthen the infrastructure
- Improve regulation and control mechanisms
- Improve financial literacy.

## 6.2 Level of Policy, National or Otherwise

Even though the level of access of SMEs and households in Azerbaijan to financial services is indicated as one of the problems both within conducted surveys and published researches in this direction, neither the government nor the Central Bank has a specific policy in this field.

## 6.3 Institutions Involved

The main institutions involved in policies to promote financial inclusion are the following:

The Center for Analysis of Economic Reforms and Communication (CAERC), which was established on 20 April 2016. The objective of the Center for Analysis of Economic Reforms and Communication is to develop proposals for the realization of economic reforms based on analytical data by conducting analyses and researches on macro- and microeconomic levels directed at ensuring sustainable economic development of the country, as well as to prepare mid- and long-term forecasts, provide government authorities and agencies with the same, and organize the promotion of the achievements of the Republic of Azerbaijan in various sectors of the economy.

The Financial Market Supervisory Authority (FMSA) was established on 3 February 2016. The mandate of the FMSA is financial market regulation and supervision to ensure financial sustainability and protection of the rights of investors and consumers.

## 6.4 Specific Strategies

There is no specific strategy for microfinance institutions and banks.

## 6.5 Credit Databases

Currently, there is only one credit registry, and it does not meet the typical credit bureau standards. Some limitations prevent the credit registry from expanding into a proper credit bureau: a) the registry information is closed to the nonbanking financial institutions. Currently, 144 nonbanking credit institutions operate in Azerbaijan. The target market for these nonbanking credit institutions includes small farmers, trade and service SMEs, and individual enterprises, which mostly produce consumer goods, i.e., the target group for these microcrediting institutions mainly includes SMEs of various sorts. Not having accurate credit information on borrowers causes the microcrediting organizations to introduce more stringent requirements (e.g., higher interest rates, shorter terms) to mitigate risk. b) Registry information does not offer a detailed analysis of the client.

Unlike the registry, a credit bureau processes the information received: It generalizes, classifies, and sells clients' credit reports (histories) to the banks. The registry services include only a small portion of the bureau's possibilities.

## 6.6 Credit Guarantees, Subsidies

Although in 2014 the government took a step toward the establishment of a legal framework for secured transactions, it has yet to be completed. Credit guarantee schemes with private sector participation are underdeveloped in Azerbaijan. Letters of credit, trade insurance, leasing, and factoring are also limited by both supply and demand factors. At the same time, stronger legal frameworks are required to create an enabling environment for venture capital activities.

As for state subsidies for SME development, the government of Azerbaijan provides three different plans for SME support:

1. The largest of them is the Azerbaijani Investment Company (AIC), which invests in companies by taking equity stakes of at least $1 million, providing venture capital.
2. The National Fund for Support of Entrepreneurship (NFSE) provides highly subsidized loans (up to $3.2 million in value) to SMEs.
3. Finally, the Mortgage Fund also provides highly subsidized credit for a particular purpose. All three funds rely heavily on the state oil revenues and issue debt at below-market rates.

## 6.7 Assessment of Effectiveness, Gaps, Issues

Technological factors, which are considered an essential element of ensuring access to finance, are sufficiently underdeveloped in the country. According to the research findings, problems of a supply nature in the field of access to financial resources are more than the difficulties in demand quality. A number of these issues originate from an

economic policy carried out by the government as well as the monetary credit and exchange rate policy implemented through the Central Bank. Although there has been a surplus across banks due to restrictions imposed over credit investments in the economy and the increase of risks, it is impossible to improve their financial, technical base and infrastructure at the expense of additional resources. The main reason is that this brings about an increase in expenditure and worsens the economic status of banks. It should be noted that overdue credits are overabundant and there is a lack of policy to resolve this issue and conduct expert discussions. Although there were high expectations from both the CBAR and FMSA to find a solution to this problem, neither of them can carry out an adequate policy on settling the existing issue in the new period. Similarly, existing deficiencies and gaps in the current legislation are limiting in terms of finding a fair solution to this problem in courts.

Regardless of a decrease in credit interest rates, the rates are creating substantial expenses for SMEs and households considering the current conditions. It is worth highlighting that costs accrued as a result of a difference between the pre-devaluation exchange rate and the rates on credit, including high interest rates, are paralyzing the business activities of SMEs and households. Thus, an absence of centralized and specific policy in this sphere is aggravating the relationships of banks and NBCs with their customers. This results in cases being taken to court. Consequently, a reliable customer database is disappearing, and trust and confidence in banks are dropping.

Even though there is a presidential order on the activities of credit guarantee foundations, problems regarding the access of individuals lacking collateral and property to credit remain, given that an order implementation process has not been launched yet.

It should also be underlined that the attitude of the Azerbaijan parliament toward changes in the legislation in this area is not good enough. Additionally, the current gaps related to the protection of the financial rights of customers are making it challenging to win court cases. Furthermore, the absence of specialized public unions and customer financial protection bureaus is leaving customers legally and publicly unguarded. Therefore, this requires revision of the current rules and procedures; however, there have not been any changes in recent years. It should be noted that the decline in modernization and innovation of the economy does not go unnoticed within financial markets. Moreover, both SMEs and households that are actors of financial markets are benefiting from innovative products, and banks cannot reduce their expenses through applying innovations in this direction.

Additionally, the difficulties related to the creation of a credit database and ensuring its access as a centralized resource remain, particularly for NBCIs.

Even though the adoption of the Strategic Road Map on access to financial services is commended, there has been no significant achievement in its execution. Moreover, the tasks set before the CBAR and FMSA with the aim of carrying out efficiently the responsibilities outlined in the Strategic Road Map are progressing slowly. The decisions regarding implementation are being delayed. Although there are some definite changes regarding ensuring access to financial markets on a national level in Azerbaijan, targets for a particular policy at the micro level have not been identified yet.

# 7. FINANCIAL EDUCATION AND FINANCIAL LITERACY[20]

## 7.1 Status of Financial Literacy

Financial capability and education are an important priority for the CBAR as it helps to empower people to become effective partners of these institutions as productive economic agents and to improve people's lives. To this end, the CBAR developed a national financial literacy strategy (NFLS) and a financial education website. Since 2010, the CBAR has launched and incorporated, under its mission plan, the Financial Literacy Project with five main objectives: "(a) make customers economically and financially more educated and skillful, (b) educate parents through children, (c) make changes to the financial behavior of people, (d) inspire corporate social responsibility, and (e) mitigate risks."

Given all these factors, the CBAR launched the Financial Literacy Project in 2010 under its mission plan. The promotion of financial and economic literacy as a public value can be acknowledged as one of the key goals[21].

## 7.2 Survey Results

The only "Financial Literacy Survey" conducted within the "Financial Services Development Project" supported by the Central Bank of the Republic of Azerbaijan, the World Bank, and Swiss SECO by the Azerbaijan Micro-Finance Association (AMFA) in 2009. AMFA evaluated the current and starting situation in the field of financial literacy through surveying respondents in 2009; however, it could not repeat it to measure the progress. An analysis of the starting situation has proved that nongovernmental organizations should work intensively with state agencies in this direction with the aim of filling existing gaps.

To support the authorities in Azerbaijan in their efforts to advance financial capability, the WBG has implemented a nationally representative financial capability survey of the adult population in Azerbaijan. This survey constitutes a key diagnostic tool that will inform the development of a detailed implementation action plan for the NFLS. Moreover, it will help the authorities to set quantifiable and concrete targets, and assess the effectiveness of future financial capability by enhancing programs.

The Azerbaijani authorities, with the support of the WBG, have conducted this financial capability survey, which will provide a detailed baseline for strategies regarding financial inclusion and literacy.

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[20] *According to the Guidance Note on the Development and Implementation of National Strategies on Financial Education and of Financial Education Programmes, each of the terms "financial education" and "financial literacy" has a different emphasis, although, in practice, the terms tend to be used interchangeably:*

*"financial education" refers to the provision of training, information, and advice to help people to manage their finances;*

*"financial literacy" refers to a person's knowledge, understanding, skills, and (sometimes) confidence to manage their finances.*

[21] CBAR, "Financial literacy project," http://en.cbar.az/lpages/finance-edu/about-the-project/

According to the WBG Financial Capability Survey, Azerbaijan 2015, knowledge of basic financial concepts is a significant challenge in Azerbaijan that is mirrored by the fact that on average, Azerbaijani adults were able to answer 3.9 out of seven financial capability-related questions correctly. Azerbaijani adults are most comfortable with performing simple financial calculations (90%), identifying better bargains (79%), and understanding the concept of inflation (67%). However, they were found to be less familiar with risk diversification (19%) and lacked the numeracy skills needed to calculate simple and compound interest (46%). An international comparison of 21 countries confirms that Azerbaijanis' financial knowledge and awareness are within the norm in general. In fact, respondents in Azerbaijan ranked 9th for inflation, 10th for simple division, and 19th for simple interest.

An international comparison of some countries confirms that Azerbaijanis' financial knowledge and awareness are within the norm in general, except for interest rate calculation. Table 10 shows, for Azerbaijan and Armenia, the proportion of adults with a good grasp of basic financial concepts.

**Table 8: Regional Comparison of Different Financial Literacy Scores**

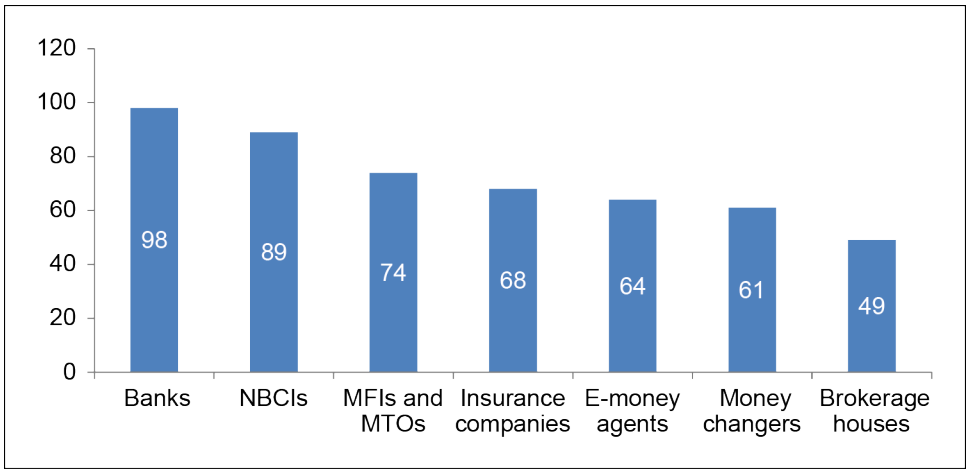
| Country | Year | Inflation | Simple Interest | Compound Interest | Simple Division |
|---|---|---|---|---|---|
| Azerbaijan | 2015 | 67 | 35 | 46 | 90 |
| Armenia | 2010 | 83 | 53 | 18 | 86 |

Source: WBG Financial Capability Survey, Azerbaijan 2015.

As far as the average number of financial products known is concerned, respondents were familiar with products provided by 5.8 out of eight different types of providers. The survey participants were found to be well aware of the financial products offered by the main financial institutions, except brokerage houses.

Product awareness reached 98% for banks, 89% for other NBCIs, 74% for MFIs and MTOs, 68% for insurance companies, 64% for E-money agents, and 61% for money changers, but only 49% for brokerage houses, which is most likely due to the fact that the capital market in Azerbaijan is currently in a nascent stage.

**Figure 4: Overview of Financial Product Awareness by Financial Institutions**
(%)




Source: WBG Financial Capability Survey, Azerbaijan 2015.

Respondents who are the most familiar with financial products offered by financial providers tend to have a higher income and be more than 54 years old.

Azerbaijani adults showed relative strengths in using information and advice, in choosing financial products, and, to a certain degree, they tend to be far-sighted and think about the future. Respondents scored highest in using information and advice for making an important financial decision (75), choosing financial products (59), and far-sightedness (54). On the other hand, such respondents scored lowest in making provisions for old-age expenses (21), saving and not overspending (25), and controlled budgeting (35).

A comparison to respondents in 14 countries confirms that Azerbaijani adults are mastering the task of choosing financial products but struggle to translate their far-sightedness into proper long-term action. Azerbaijan is ranked third out of 14 in choosing financial products, but given the difficulties above that respondents faced in understanding simple and compound interest, it may be questionable if people always end up selecting those products that best meet their needs. Moreover, the international comparison reveals that although Azerbaijani adults are ranked sixth out of 14 regarding their propensity to think about the future, they are at the back of the pack in the area of budgeting and in making provisions for old-age expenses.

The last of these findings is especially concerning given its implications for people's long-term well-being.

There is no clear evidence of a correlation between socioeconomic characteristics and financial behavior scores, suggesting that many people struggle with sound financial decision-making. While urban people achieved better scores than their rural peers in some financial capability areas, including their propensity to use information and advice, and to save and refrain from overspending, they were worse off regarding their ability to control their budgets and achievement orientation. Furthermore, the richest people fared better than the lowest income segments in controlling their budgets and demonstrated higher levels of achievement orientation. However, compared to the lowest income earners, people living on the highest incomes lack the propensity to think about the future and to use information and advice when making a financial decision.

## 7.3 Institutions Involved (Both Public and Private)

One of the main institutions, the Financial Literacy Council, was established on 7 March 2017, as an initiative of the ABA. Aimed at general discussion and coordination of planned activities related to financial literacy, it is envisaged to develop the Financial Literacy Council under the ABA, including top managers (members of boards of directors) among its members. Members will determine the main directions of the council's activities with the participation of ABEC. The council will serve as a platform for the discussion of ideas, information, and experiences in this sector.

AMFA encourages its members to offer nonfinancial services (for example, financial literacy education), and provides capacity-building assistance for these activities. Currently, 33% of members provide financial literacy and entrepreneurship development training.

There are initiatives aimed at increasing the financial literacy (FL) of the population by both the CBAR and AMFA as a local association, with some initiatives being supported by the foreign development and investment agencies. The Central Bank of Azerbaijan launched the Financial Literacy Project in 2010 under its mission plan. The Development Department of the Center for Research and Development implements

these activities on behalf of the CBAR. The Center for Research and Development of the Central Bank of the Republic of Azerbaijan held training for commercial banks jointly with the PwC (PricewaterhouseCoopers) Academy.

The Center for Research and Development of the Central Bank of the Republic of Azerbaijan has become a member of the International Network on Financial Education (INFE). Currently, the network is represented by more than 135 state agencies, mainly central banks, from 74 countries. Azerbaijan is the third country in the CIS to actively join the network, which is represented by such leading countries as the USA, Canada, Germany, and France.

Partners of the Development Department on Financial Literacy include the Azerbaijan Library Confederation (ALC), the Organization for Economic Cooperation and Development (OECD), the International Federation of Library Associations (IFLA), the American Resource Center (ARC), the Germany International Cooperation Society (GIZ), PricewaterhouseCoopers (PWC), the World Bank (WB), the German Savings Banks Fund for International Cooperation (SBFIC), and the Ministry of Education.

## 7.4 Target Groups and Programs

The key target audience of the Financial Literacy Project is high school students, the broader public, economic journalists, CBAR employees, commercial bank employees, and students majoring in banking.

## 7.5 Types of Programs

The Development Department's various activities to date include a study of international practice, communication with donor organizations, educational events for high school students and journalists, meetings with high school students jointly with the Ministry of Education, elaboration of curriculum recommendations, a series of "banks to schools, students to banks" events, the Economic Football interactive game jointly with VISA and the Ministry of Taxes, and the International Savings Day at the end of the previous year.

Future FL activities include enhancement of the socioeconomic growth of the country, support for the development of the Azerbaijani banking system, raising economic and financial awareness in the country, promoting financial literacy as a public value, and changes to people's behavior. The harmonized action plan incorporates surveys among the population to evaluate FL, elaboration of the FL strategy, improving financial, economic education in high schools, preparing optional programs for IV–VIII-year high school students on raising financial awareness and skills, and a series of "banks to schools, students to banks" events.

## 7.6 General Financial Education

Azerbaijan's population was targeted to promote financial inclusion through financial education. Under the EBRD support, a financial literacy training program was extended to 160,000 people in Azerbaijan, Armenia, the Kyrgyz Republic, Georgia, Moldova, and Tajikistan between 2011 and 2013. This initiative targeted the recipients of remittances, which make up 45% of GDP in the CIS countries. Nearly 27,500 new bank

accounts were opened as a result of this program and the equivalent of more than US$ 25 million was brought into formal financial institutions[22].

The EU-funded project called "Building female professionals and promoting women entrepreneurship development in rural regions of Azerbaijan"[23] was managed together with the Azerbaijan Micro-finance Association (AMFA). The results of the project serve as a successful model for addressing the issue of female participation in microfinance and, more generally, women's employment in the rural area.

Additionally, the CBAR developed a national financial literacy strategy (NFLS) and a financial education website.

## 7.7 Debt Management Programs

Since the double devaluation, there have been deteriorating debt problems in Azerbaijan. An overdue credit accounted for 13.83% of the total credit for 1 January 2018. Nevertheless, there is no systematic and centralized program for solving overdue credit problems and helping creditors to manage finance better.

## 7.8 Assessment of Effectiveness

AMFA had evaluated the current and starting situation in the field of financial literacy through surveying respondents in 2009; however, it could not repeat it to measure the progress. An analysis of the starting situation has proved that nongovernmental organizations should work intensively with state agencies in this direction with a view to filling existing gaps. Nevertheless, the controversial changes made to legislation regulating the activities of foreign donors in Azerbaijan starting from 2014 have weakened their operations and this has negatively affected the funding of programs in this direction. In particular, these changes have caused a reduction in the programs of AMFA.

# 8. CONCLUSIONS AND RECOMMENDATIONS

## 8.1 Conclusions

The financial sector is small, banking penetration rates are low, and the transmission mechanism between the cost of CBAR lending and the money supply is weak. Dollarization of the economy remains high, and oil prices will continue to play a dominant role in shaping inflation expectations, the exchange rate, and the money supply. Confidence in the manat is likely to remain low following the devaluation of the currency in December 2015 and the depreciation in the second half of 2016, and there is a risk of further currency volatility if oil prices fall back, which could prompt further CBAR interventions.

The microfinance institutions are weakening in terms of the quality of their portfolio and the decline in the number of customers and assets, and as a result of they are faced with losses.

[22] EBRD. "Financial Inclusion". http://www.ebrd.com/what-we-do/financial-inclusion.html.

[23] http://mfc.org.pl/financial-education-in-azerbaijan-read-the-case-study/

Financial education and literacy are not satisfactory in either a quantitative or qualitative context. The scope of these programs is small and nonsystematic, and is not of a continuous nature.

## 8.2 Recommendations

Recommendations are presented in four categories:

### 8.2.1 Financial Market

a. **The financial sector of Azerbaijan must liberalize.** Despite the financial market and the relatively open legal framework for foreign investment, government rules and regulations can complicate entry to market. Therefore, the liberalization of foreign investment policy should be part of the broader deregulation of the financial sector. In particular, the insurance market must be completely open to foreign investors. Foreign companies may enter the market without barriers. Azerbaijani insurance companies can compete with foreign companies in the domestic market. Azerbaijan should reaffirm its commitment on services to accede to the WTO and to enact all possible measures to intensify the process.

b. **Improvement of legal base of regulation of financial markets.** Completing key pieces of legislation (e.g. on facilitating the establishment of a private credit bureau, a movable collateral registry, and legal reforms regarding secured transactions) would fill the gaps in the country's financial structure.

c. **Acceleration of the structural reforms in the financial sector.** The policy on consolidation of bank capital should be pursued along with privatization of the IBAR with the participation of foreign investors through arranging an open and competitive investment contest.

d. **Promotion of innovation support in financial markets.** Innovative approaches could encourage banks to lend to SMEs, including the establishment of a credit guarantee scheme and improvements to current schemes.

e. **Establishment of a reliable credit database.** Credit risks should be managed more effectively through the creation of a single and centralized data system of responsible and reliable customers. The government must intensify its efforts to increase the level of detail and quality of loan statistics, and improve the accessibility of the data (e.g., by publishing regular updates on the websites of the national statistical offices) due to the functioning of the Credit Bureau.

### 8.2.2 Financial Inclusion

a. **Develop** a national strategy for financial inclusion **and promote the provision of financial services.** This policy should be geared toward specific needs of customers including through digital financial services (e.g., mobile financial services).

b. **Improve** access for a population of rural and other urban areas to financial services. Competition among institutions/organizations providing financial services should be increased, their service network upgraded, and service fees decreased. In particular, state support programs for financial institutions aimed at increasing coverage and the level of access to financial services in remote districts should be provided. In addition to this, an infrastructure meeting

minimum standards enabling financial operations and transactions to be carried out should be created in post offices.

c. **Enrich types of products and services.** Financial products and services offered to customers should be enriched through new actors and tools from the financial market. Access of SMEs and households to financial services should be increased through new financial market players (venture investment funds, business angels, crowdfunding platforms/campaigns, etc.) and alternative financial instruments (guarantees, mortgages, bills, leasing, factoring, etc.).

d. **Directions for services of NBCIs should be expanded.** Relevant amendments to the current legislation of NBCIs that will allow them to realize payment/remittance and business counseling services should be made.

e. **Growing range of financial services in rural and other urban areas.** The infrastructure in rural and remote regions should be developed for SMEs and households regarding access to consumer/business/mortgage loans, bank deposit accounts, insurance, current bank accounts, fiber-optic Internet, mobile banking, local and foreign money remittance, and other such financial services in those areas.

f. **Encourage use of payment cards.** To ensure broad use of payment cards in the purchase of goods and services, large-scale awareness-raising campaigns on the capacity of cards should be carried out, opportunities for the use of payment cards should be created in more places, the normal function of ATMs should be ensured, and the quality of Internet services increased. Thus, studies show that ATMs often contain no money and there are not enough of them in other urban and rural areas.

### 8.2.3 Financial Literacy

a. **Create a detailed implementation action plan to accompany the NFLS.** The action plan should address the key challenges identified through this survey and should outline (i) a concrete and self-explanatory description of the actions to be implemented; (ii) the entity (or entities) responsible for its execution (in the case of actions involving multiple stakeholders, a primary implementing entity is identified); (iii) the time frame for the implementation of said action; and (iv) the priority of execution of said action (high, medium, or low).

b. **Develop a monitoring and evaluation (M&E) framework to measure progress in the implementation of the NFLS.** The goal of the M&E framework is to outline a robust M&E system for the NFLS that extends beyond a simple list of national-level impact indicators to include program-level intermediate indicators, a theory of change, coordination details, and an emphasis on evaluation and improvements in data collection.

c. **Develop a targeted policy on increasing financial literacy in the specific area.** Financial literacy should be targeted at a population of rural and remote areas. Women, poor people, disabled people, pensioners, and other vulnerable groups should be given attention first. It is reasonable to involve financial service providers, line associations, NGOs, mass media, higher education institutions of the economic-financial profile, municipalities, and financial consultants in the process of increasing financial literacy.

d. **Strengthen awareness-raising activities.** Mass media should be actively involved in awareness-raising events and a wide range of programs should be used, including text messages, mobile phone applications, etc., to enhance financial knowledge and change attitudes and financial behaviors.

e. **Integrate financial capability content in the school curriculum.** Basic economic and financial concepts, simple accounting calculations (calculations of the interest rate on credit/deposits), financial services and mode of use and management of family budget should be taught at an early age.

f. **Increase the confidence of the population in financial organizations.** Control over a confusing/deceptive advertisement in the mass media should be improved and relevant issues regulated.

g. **Stimulate a general education campaign on products and services offered by banks.** The credit portfolio does not correspond to the institutional trend of lending institutions in Azerbaijan. Moreover, the study points to a profound lack of mutual understanding and information sharing between the banks and the intended clients, i.e., to a poor marketing strategy. This is partly an underlying cause of the low lending rate.

### 8.2.4 Consumer Protection

a. **A reliable system protecting the credit and financial rights of customers should be created.** Therefore, relevant changes should be made to the current legislation in this direction and the effectiveness of both state and nonstate institutions' functioning in this area should be increased. Along with this, opportunities regarding the protection of rights of customers should be increased through courts and noncourt institutions.

b. Establish a clear mandate of the financial regulator in the area of financial consumer protection, enforcement, and redress. Expand the content of the National Financial Education Website to include other financial services in addition to banking products and establish special sections with information on consumers' rights and complaint-handling mechanisms.

c. Establish an independent alternative dispute resolution mechanism. Enforce full compliance of FIs with consumer protection requirements including information disclosure, fair advertising, complaint handling and redress, and promote sound business practices by using adequate market conduct supervisory tools including mystery shopping.

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