



**Central Bank of Iraq
Statistics and Research
department
Monetary and Financial
Stability Division**



Early Warning Report for The Banking Sector

**Number
Twenty-Four**

Q2 2023

Statistics and Research Department

Monetary and Financial Stability Division

Early Warning Section

**Early Warning Report for the Banking Sector
(Q2 2023)**

Central Bank of Iraq

2024

Name: (Early Warning Report for the Banking Sector Q2 2023) / Issue No. Twenty-Four.

Description: Central Bank of Iraq - Baghdad/ issued quarterly since 2017.

Address: Central Bank of Iraq - Al-Rasheed Street - Baghdad - Iraq.

Tel: 8165171

P.O. Box 64

Fax: 0096418166802

Email: cbi@cbi.iq

Early warning: is an index that gives a clear picture of the reality and magnitude of the potential risks that may occur to the financial sector and economy in general. Thus, it enables decision-makers to take necessary measures and formulate policies in a timely manner to avoid financial crisis.

You can quote from the report in the following format:

Central Bank of Iraq/ Early Warning Report for the Banking Sector Q2 2023, Issue No. Twenty-four, Baghdad, 2023.

***Requests for this issue should be sent electronically to the following address:**

mfs.dept@cbi.iq

Contents	Page No.
Introduction	
Chapter One (Currency Value Stability Indices)	1-5
1. Foreign Exchange Market Pressure Index	1
2. Foreign Reserves Adequacy to Broad Money Supply (M2)	2
3. Change of Interest Rates Averages	3
Chapter Two (Banks' Performance Indices)	6 – 19
1. Central Bank's Loans/ Total banks' liabilities	6
2. Banking Deposits and Currency in Circulation to Broad Money Supply (M2)	7
3. Total Cash Credit/ Total Deposits	8
4. Banks' investments	9
5. Money Multiplier	10
6. Banks' Profitability	11
7. Non-performing loans/ total cash credit	13
8. Non-performing loans/ total deposits	14
9. Non-performing loans/ total assets	15
10. Sectoral distribution for non-performing loans	16
11. Net open position in foreign currency for capital	17
Chapter Three (Macroeconomic Performance Indices)	20-34
1. Inflation Rate	20
2. Internal Debt Growth Rate	21
3. Change Rate of Gross Domestic Product (GDP)	21
4. Implicit Price Deflator	22
5. GDP Gap	23

List of Figures	Page No.
Chapter One	1 – 5
Figure No. (1) Foreign Exchange Market Pressure Index	2
Figure No. (2) Foreign Reserves at CBI to Broad Money Supply (M2)	2
Figure No. (3) Interest rate on savings, fixed deposits and inflation rate	4
Chapter Two	6 – 19
Figure No. (4) Ratio of Deposits to Broad Money Supply (M2) and Currency in Circulation to Broad Money Supply (M2)	7
Figure No. (5) Ratio of Fixed, Current, and Saving Deposits at Commercial Banks for Q2 2023	8
Figure No. (6) Ratio of Cash Credit to Total Deposits at State-Owned Banks, Private Banks, and Banking Sector as a Whole	9
Figure No. (7) Ratio of Total Investments to Total Assets with State Owned Banks, Private Banks, and Banking Sector as a Whole	10
Figure No. (8) Money Multiplier and Its Relation to Legal & excess Reserves	11
Figure No. (9) Banks' Profitability	12
Figure No. (10) Indices of Return on Equity and Return on Assets with State Owned Banks & Private Banks	12
Figure No. (11) Ratio of Non-Performing Loans with State Owned Banks & Private Banks to Total Cash Credit	13
Figure No. (12) Ratio of Non-Performing Loans with Public & Private Sector to Total Cash Credit	14
Figure No. (13) Ratio of Non-Performing Loans Ratio to Total Deposits with State- Owned Banks & Private Banks and Banking Sector as a whole	15
Figure No. (14) Ratio of Non-Performing Loans to Total Assets at State-Owned Banks, Private Banks and Banking Sector As a whole	15
Figure No. (15) The Percentage of Cash Credit Granted to Each Real Sector	16
Figure No. (16) The Percentage of Non-Performing Loans to Each Real Sector	17
Figure No. (17) Net Open Position in Foreign Currency	18
Chapter Three	20 – 24
Figure No. (18) Inflation Rate	20
Figure No. (19) Domestic Debt Growth	21
Figure No. (20) GDP Change Rate at Constant Prices	22
Figure No. (21) Implicit Price Deflator and Inflation Rate	22
Figure No. (22) GDP Gap	23

List of Tables	Page No.
Table No. (1) Currency Stability Indices	4
Table No. (2) Indices of Banking Sector Performance	18
Table No. (3) Macroeconomic Performance Analysis Indices	24

Introduction

The early warning indices report helps to understand the most important risks that may face the banking sector, as the report provides information about the performance of banks and solutions to address future crises. Since it adopts an evaluation of the main performance indices of the banking sector and provides an assessment of the impact of government policies and legislation on the work of the banking sector.

The value of the foreign exchange market pressure index for Q2 2023 witnessed stability within the upper and lower limits, as a result of the increase in foreign reserves at the CBI by (32%), and the decline in the dollar exchange rate in the parallel market for Q2 2023 as a result of the rise in the value of the official Iraqi dinar from 1,450 dinars to 1,300 dinars per dollar. In addition to other measures undertaken by the Central Bank of Iraq to maintain the stability of the value of the local currency. While the ratio of foreign reserves to the broad money supply (M2) rose to (79.9%), which exceeds the specified minimum amount of 20%.

As for the performance of banks, the ratio of deposits to the broad money supply (M2) continued to decline during (2022-2023), with the rise of the currency outside banks to the broad money supply, which means an increase in the amount of hoarding, and the total cash credit granted by the banking sector to its total deposits decreased to (50.7%). While the return on equity and the return on assets recorded a rise in Q2 2023. As for the level of non-performing loans, the ratio of non-performing loans to the total cash credit continued to decline. It is noticed that agriculture, trade, restaurants, hotels, and community services recorded an increase in non-performing loans for Q2 2023. On the other hand, the net open position of banks-maintained ratios below the standard limit set by the Central Bank of (20%).

As for the macroeconomic performance, inflation recorded an acceptable rate during this quarter amounted to (3.6%) on an annual basis, but the gross domestic product growth rate recorded a decline of (-5.7%) compared to the same quarter of the previous year. Despite its increase by (3.4%) compared to the previous quarter of the same year, the output gap recorded a negative value, which means that there is an economic contraction.

Chapter One: Currency Value Stability Indices

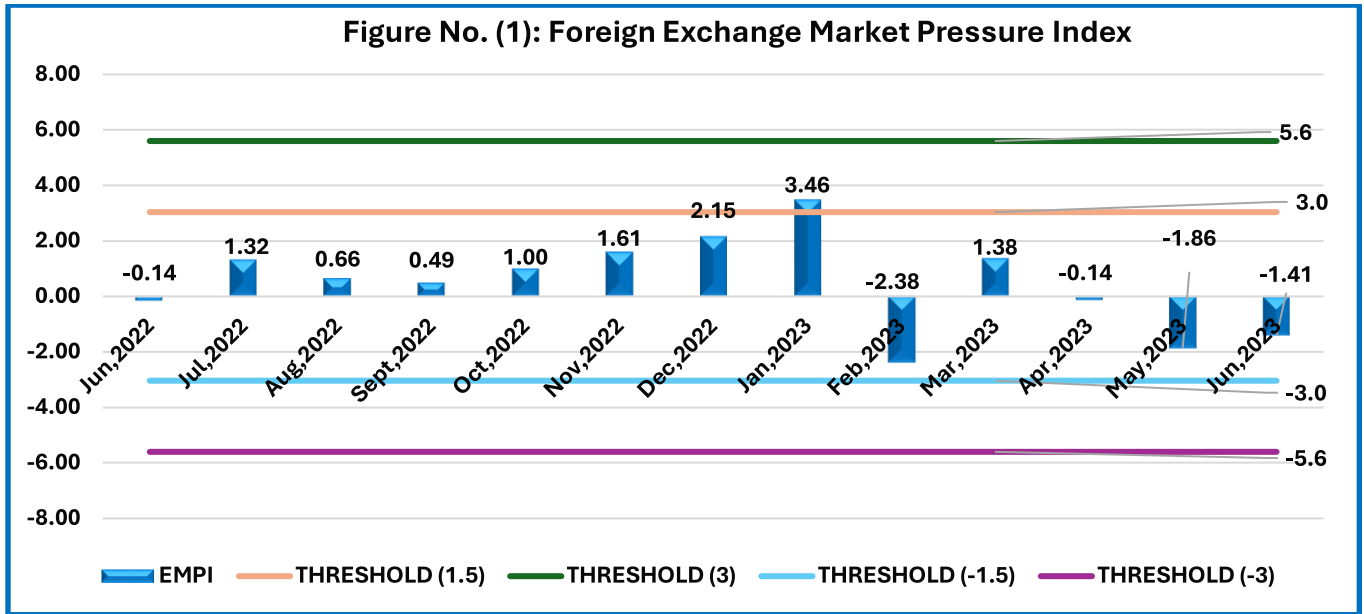
The currency value index is an important index affecting the Iraqi economy and its relationship with regional economies. The depreciation or appreciation of the currency negatively or positively affects foreign trade, the ability to repay internal and external debt and the country's credit position. Other factors affect the exchange rate of the Iraqi dinar, including the domestic economy's internal climate, the nature of the imports and the economic policies pursued, as well as foreign reserves and other non-economic factors directly affecting the exchange rate such as rumors and expectations and enhances the efficient handling of economic and non-economic factors from the value and purchasing power of the Iraqi dinar. The Iraqi dinar stability is a critical indicator of fiscal planning, economic health, and financial stability. There are several indices that can be analyzed to recognize fluctuations or changes in currency value, such as foreign exchange market pressure indices, the adequacy of foreign reserves index and interest rate average.

1- Foreign Exchange Market Pressure Index ¹

The Foreign Exchange Market Pressure Index is a measure used to assess the pressure of foreign exchange market demand against domestic currency generated in the foreign exchange market when foreign exchange demand exceeds its supply. It considers several variables, including the parallel market exchange rate, foreign exchange reserves and the monetary base (M0), because of its significant impact on the domestic economy and foreign trade. The depreciation of the domestic currency due to the rise in the foreign currencies exchange rate in the foreign exchange market causes a rise in the price of imported goods which leads to decreased demand for them, thus in turn decreases the imported quantity.

Figure No. (1) shows a decrease in the value of the foreign exchange market pressure index from (-0.14%) for Q2 2022 to (-1.41%) for the same quarter of 2023. The index has maintained its levels within the index's upper and lower limits (5.6% & -5.6%) as a result of the Central Bank's change in the official exchange rate from (1450) dinars per dollar to (1300) dinars per dollar beginning 2023 to maintain the stability of the value of the local currency, as well as the application of the electronic platform for external remittance, in coordination with international entities for the purpose of tightening the operations of the sale and purchase of foreign currency and regulating them to maintain the stability of the local currency value, which resulted in the net foreign assets rising by 30.8% versus the recording of the monetary base up by (31.8%). The exchange rate in the parallel market to Q2 2023 was 0.8% lower than the same quarter the previous year despite the said platform's application.

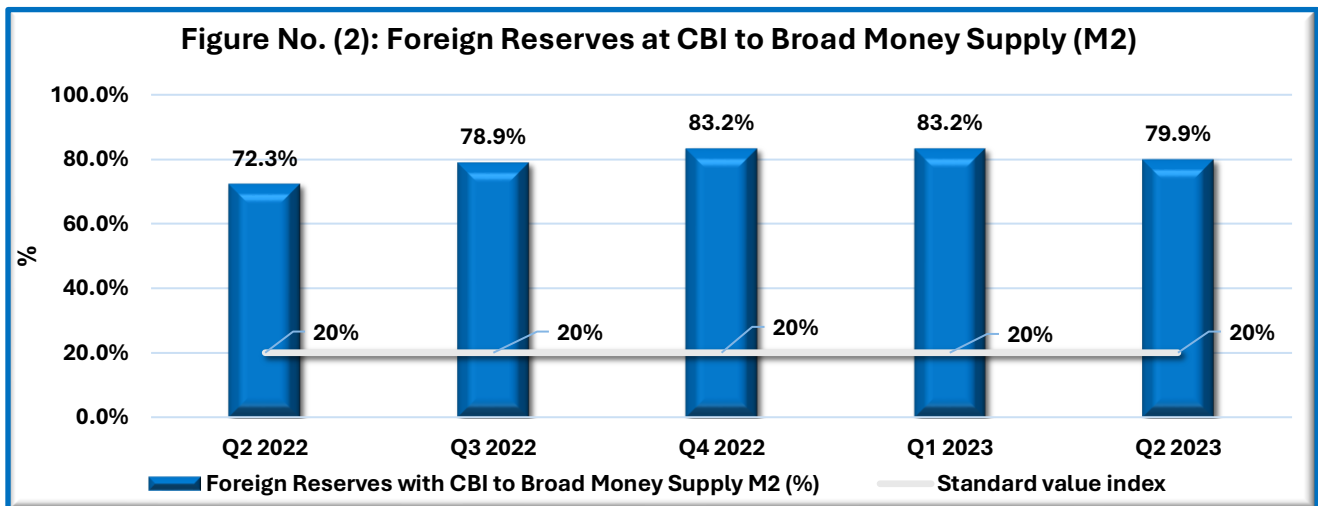
¹ Central Bank of Iraq, Early Warning Report 2020, Issue No. 14, page 3.



Source: Central Bank of Iraq, Estimates of Monetary & Financial Stability Division 2023.

2- Foreign Reserves Adequacy to Broad Money Supply (M2)

Broad money supply is one of the most covered monetary indices from the foreign reserves, measuring the potential demand for foreign assets from domestic sources. The International Monetary Fund (IMF) recommended that the standard ratio of this index (20%) for countries that followed a fixed exchange rate system¹, foreign reserves constituted (79.9%) of broad money supply (M2) in Q2 2023, which was lower than (72.3%) in the previous quarter 2022. They are considered within safe limits because they exceed the standard ratio (20%) and due to higher reserves compared to the broad money supply, as shown in figure No. (2).



Source: Central Bank of Iraq, Statistical website

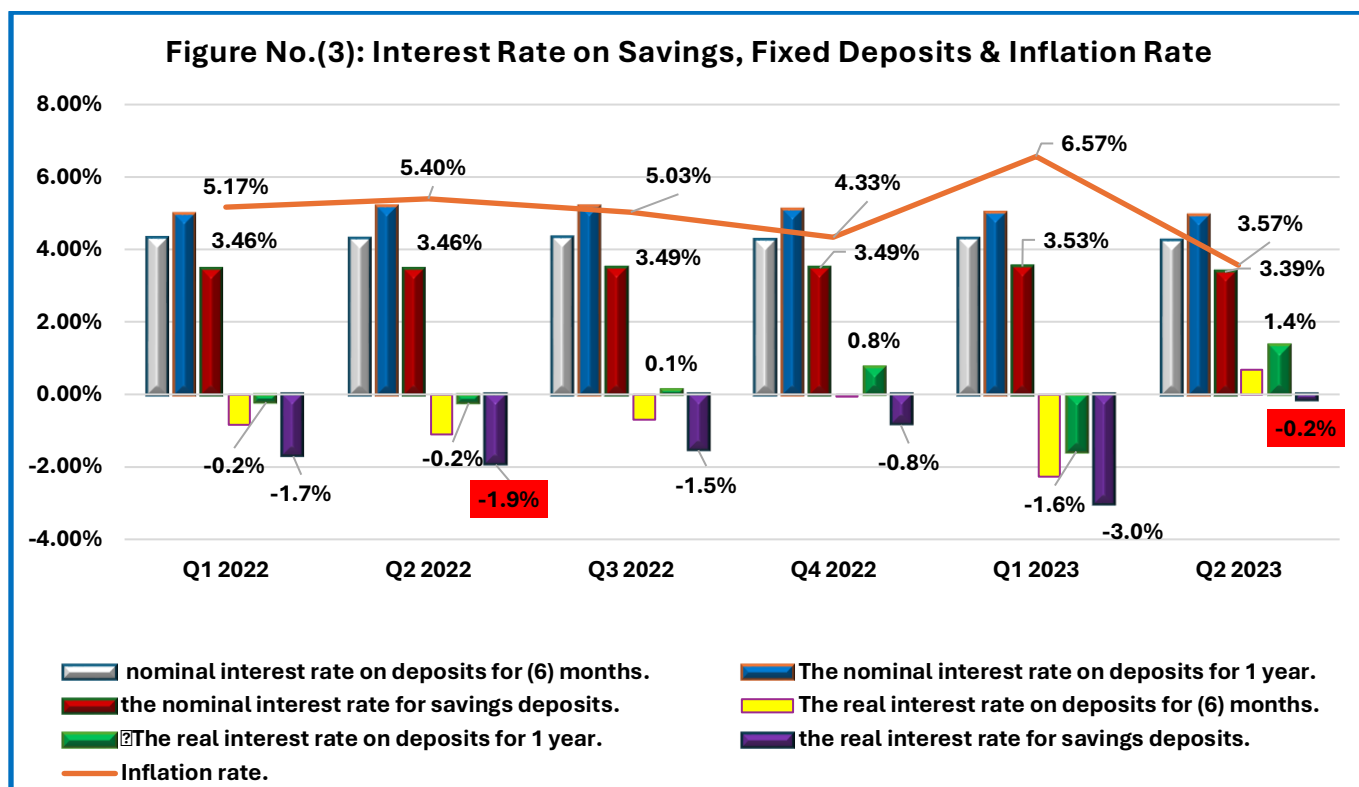
¹Volume of foreign exchange reserves. Big papers No. 104.PP5.

3- Change of Interest Rates Averages

Interest rate is one of the most important instruments used by central banks to control economic cycles and is one of the variables that has a significant impact on the value of domestic currency if the country has an advanced financial markets and free movement of capital. It is determined according to the directions of monetary policy to deal with different variables such as investment, inflation, and unemployment to achieve the targeted economic growth of country. As Iraq still has a weak financial market with an unattractive investment environment, the interest rate has little impact on foreign currency demand as well as is quite absent from controlling the movement of financial flows across borders, and financial market has little impact on its instruments. Therefore, the interest rate has little impact on the value of the domestic currency. The following is an analysis of nominal and real interest rates.

• Nominal and Real Interest Rates on Savings Deposits, Fixed Deposits, and Inflation Rates

The average of nominal interest rate on deposits for (6) months during this quarter recorded a decrease of (-1.2%) to (4.25%) against (4.30%) for the same quarter of 2022, while the real interest rate on fixed deposits for (6) months recorded a positive rate of (0,7%) against (-1.1%) for the same quarter of the previous year. The nominal interest rate on fixed deposits for one year recorded a decline of (-4.7%) for Q2 2023 to (4.92%) against (5.17%) for the same quarter the previous year, while real interest increased by (1.36%), despite that, medium-term interest rates are low in today's uncertainty that discourages deposit. As the nominal interest rates on savings deposits for Q2 2023 recorded a decrease of (-2.1%) to (3.39%) against (3.46%) for the same quarter of the previous year, and excluding inflation rates, the real interest rate for savings deposits for Q2 2023 was (-0.18) % against (-1.94%) for the same quarter the previous year. The improvement in real interest rates is attributable to lower inflation levels, as lower nominal interest rates result in lower real interest rates assuming steady inflation rates, and real interest rates rise if inflation rates fall more than the decline in nominal interest rates. The inverse relationship between inflation and real interest rates is noted in figure No. (3).



Source: Central Bank of Iraq, Statistical Website

Table No. (1): Currency stability indices

Index name	Q2 2022	Q2 2023
Official Exchange Rate Average IQD per Dollar	1450	1300
Foreign Exchange Market Pressure Index (%)	- 0.14	- 1.41
Central Bank's Total Foreign Reserves (1 billion dinars)	108.44	142.105
Broad Money Supply M2 (1 billion Dinars)	150.01	177.772
Foreign Reserves Average to Broad Money Supply M2 (%)	72.3	79.9
Nominal Interest Rate on Fixed Deposits (6) Months (%)	4.30	4.25
Nominal Interest Rate on One Year Fixed Deposit (%)	5.17	4.92
Nominal Interest Rate on Savings Deposits (%)	3.46	3.35
Inflation Rate (%)	5.4	3.57

Source: Central bank of Iraq, Statistics & Research Department, Monetary & Financial Stability Division

Source: Central Bank of Iraq, Statistics & Research Department, Balance of Payments and External Trade Statistics Division

Conclusion

- 1. The official Iraqi dinar value increased from 1450 dinars per dollar to 1300 dinars per dollar.**
- 2. Foreign Exchange Market Pressure Index stabilizes at -1.14%.**
- 3. Foreign reserves ratio increased to broad money supply which is much higher than the standard ratio of 20%.**
- 4. Central Bank's foreign reserves increased by 31%.**
- 5. Relative stability in nominal interest rates on deposits.**

Chapter Two (Banks' Performance Indices)

This chapter explains the analysis and measurement of some indices of the banking sector's performance aiming to provide a comprehensive picture of the sector's stability and its ability to meet its financial obligations, which is achieved by monitoring several key indicators as the following:

1- Central Bank's Loans/ Total Banks' Liabilities

The high index ratio reflects banking sector fragility and the increased risks facing the sector. This high index indicates the potential for a liquidity crisis in the banking sector and the magnitude of its distress, which reinforces the risks associated with the economy and the banking system in general. It should be noted that the Central Bank of Iraq did not provide any loans to banks during Q2 2023, which reflects the lack of need for any of the operating banks to obtain urgent liquidity or deal with exceptional withdrawals during that time. This index is considered a positive signal, demonstrating banking sector's stability and ability to manage its liquidity effectively under current economic conditions.

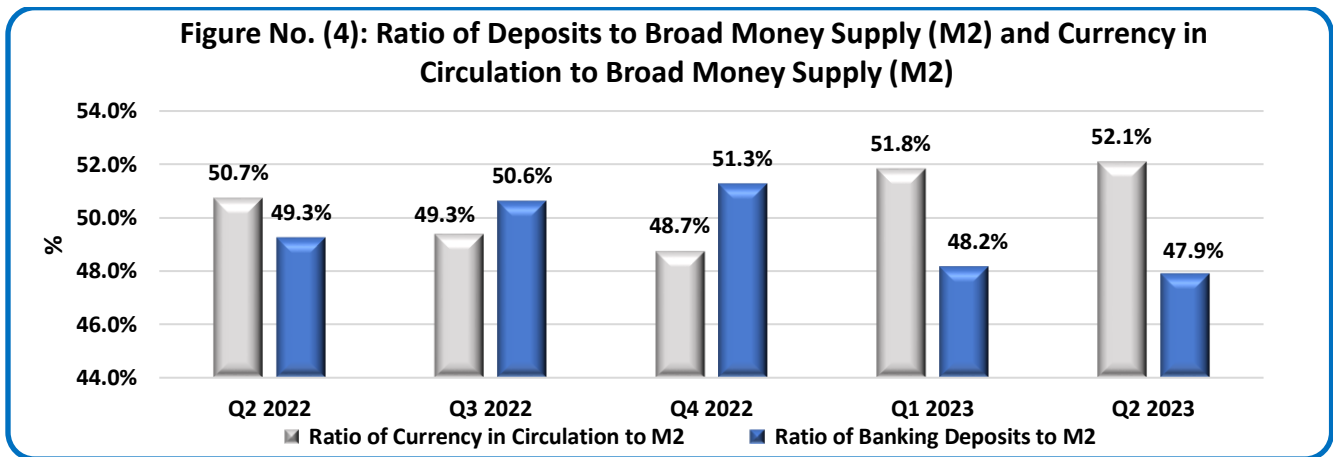
According to the Central Bank of Iraq (CBI) Law No. 56 of 2004 /Article 30 thereof, Iraqi banks resort to the Central Bank in the event of financial distress or shortage of liquidity, as it is considered the last source of financing. The following legal conditions are required for that operation:

- The Central Bank considers it is necessary for a bank to have sufficient liquidity to meet withdrawal of depositors to maintain the stability of the banking system and prevent its collapse. In the event of a shortage of liquidity, the bank could turn to the Central Bank to enhance its liquidity on strict terms.
- The law stipulates that liquidity enhancement comply with the conditions set out in CBI law, which include adherence to banking laws & regulations, and provide adequate guarantees of access to funding.

Thus, enhancing liquidity by the Central Bank is considered important to maintain financial system stability and ensure banking services continuity in the country.

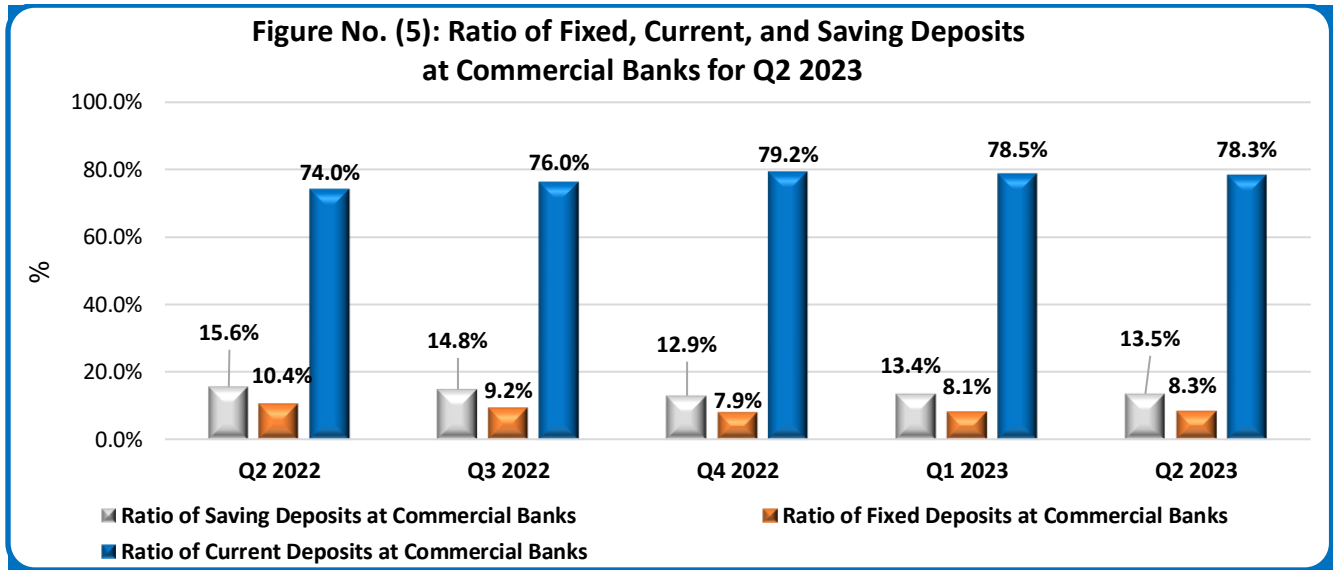
2- Banking Deposits and Currency in Circulation to Broad Money Supply (M2)

The ratio of total banking deposits to (Broad Money Supply (M2)) is considered an important index of banks' liquidity and individuals' confidence. When this index is high, it indicates that banks function well and enjoy depositors' confidence, being able to attract deposits and maintain a stable deposit volume, and therefore are not exposed to a liquidity crisis. It is noted through figure No. (4) a decrease of the ratio of banking deposits to broad money supply (M2) for Q2 2023 to reach (47.9%) against (49.3%) for the same quarter of the previous year despite that these deposits recorded a growth of (20%) for the same period. On the other hand, the ratio of out-of-bank currency to broad money supply (M2) increased to (52.1%) against (50.7%) for the same period of the previous year. However, despite a slight decline in the ratio of banking deposits with commercial banks, they are excluded from being exposed to liquidity crisis. It is important that the Central Bank continue to follow these indices of the banking sector carefully to ensure banking system stability and depositors' confidence through the development of banking services.



Source: Central Bank of Iraq, Statistical Website.

Regarding the distribution of banking deposits, it is noted from figure No. (5) that current deposits for Q2 2023 recorded a percentage (78.3%) of total deposits, while savings and fixed deposits for the same period of 2023 recorded a moderate percentage (13.5%) and (8.3%) of total deposits, respectively. Current deposits recorded a growth (26.9%) over the same quarter of 2022 and savings deposits recorded a growth of (3.9%), while fixed deposits recorded a decrease of (5%). The rise of current deposits is mainly attributed to an increase of government current deposits by (42.4%), public institutions' deposits by (24.5%), and private sector's deposits by (16.2%). In addition to the increase of the effectiveness of services and facilities provided by banks and facilitation of current transactions, however, the diversity and distribution of deposits between different types should be monitored to achieve a balance of deposit structure and ensure sustainability of the banking system and its ability to meet the demand for loans and better manage liquidity.

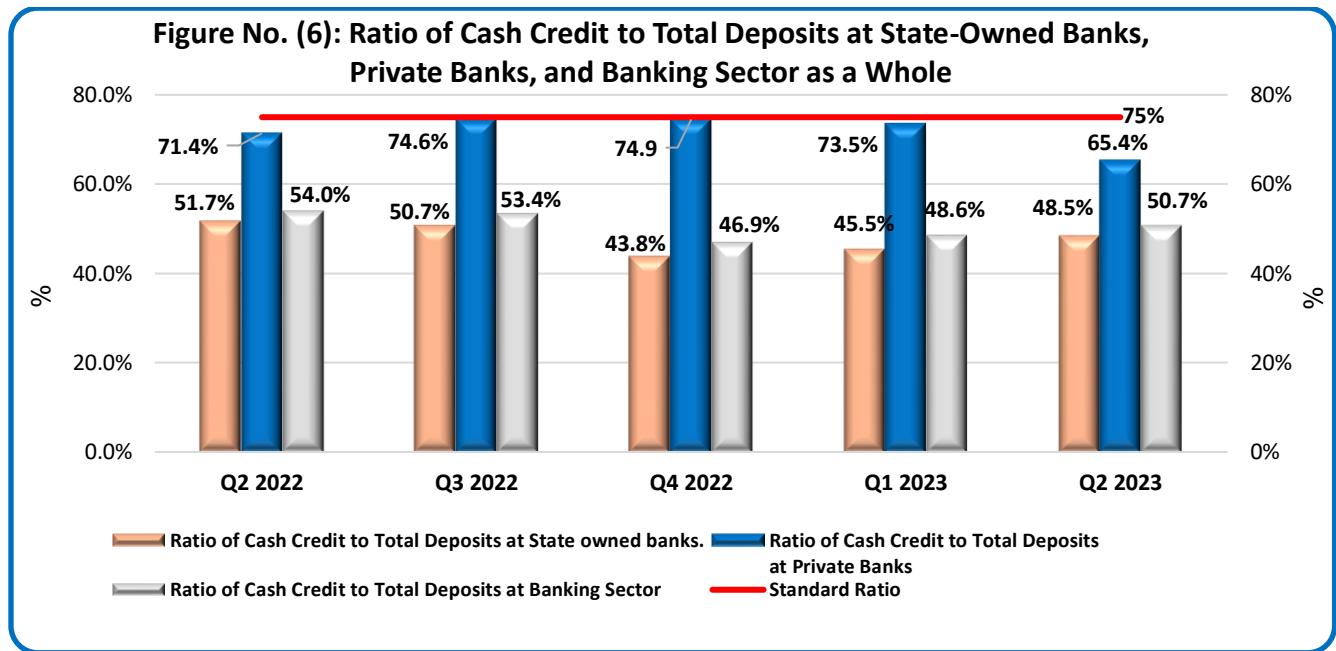


Source: Central Bank of Iraq, Statistical Website.

To measure the degree of development of the financial depth of the banking sector, broad money supply (M2) for Q2 2023 recorded (114.1%) of narrow money supply against (116.8%) for the same quarter of 2022. This decline of the fiscal depth index is attributed to a decrease the ratio of saving deposits to total deposits at the banking sector from (15.6%) to (13.5%) of total deposits, which means a decrease of the savings of household sector, as well as a decrease in the ratio of fixed deposits to total deposits from (10.4%) to (8.3%) attributable to the decline of investment at the banking sector.

3- Total Cash Credit/ Total Deposits

This index is calculated by dividing total cash credit into total deposits, as the rise of this index above its standard ratio and reflects a risk to the bank in its obligations to depositors. Figure No. (6) shows the decrease of total cash credit extended by the banking sector to its total deposits to reach (50.7%) compared to (54%) for Q2 2022, which is lower than the standard ratio of (75%) specified by the Central Bank, attributed to the growth of total deposits for the same period by (20%), which is greater than the growth ratio of extended cash credit of (12.6%).



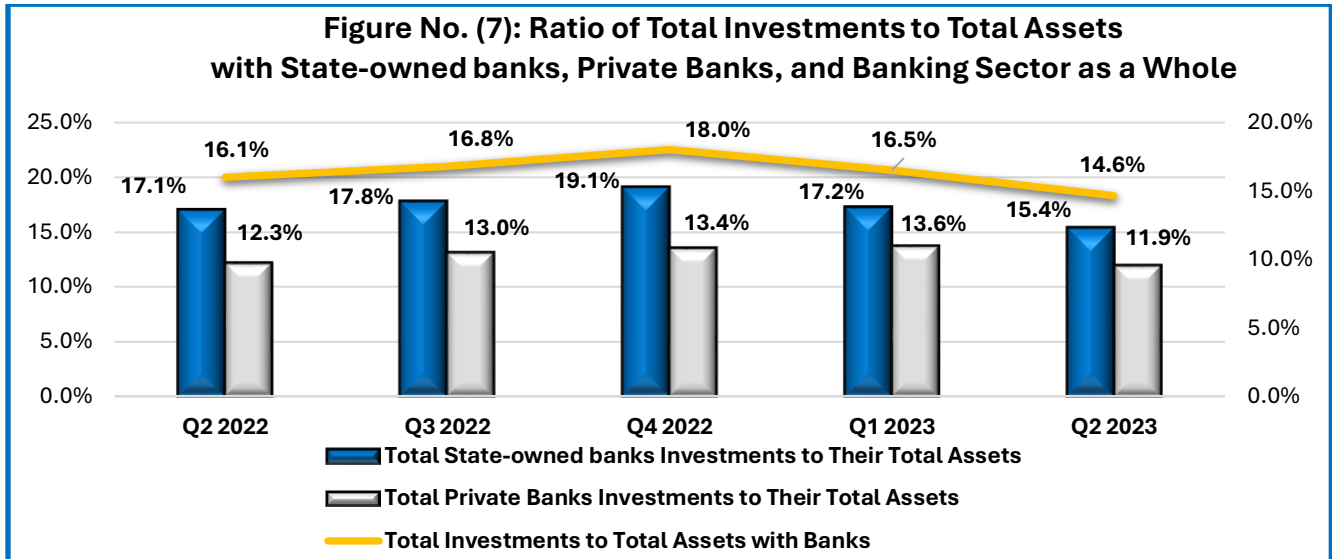
Source: Central Bank of Iraq, Monetary & Financial Statistics Division, Statistical Website.

It is noted that this index decreased for private banks from (71.4%) for Q2 2022 to (65.4%) for the same quarter of 2023, which is lower than the limit approved by the central bank due to the decrease of the extended cash credit with the rise of total deposits. In comparison with State owned banks, this percentage decreased over the previous years, falling from (51.7%) for Q2 2022 to (48.5%) for the same quarter of 2023, due to the rise of total deposits, particularly State-Owned Banks, which is within the safe limits approved by the Central Bank of Iraq.

4- Banks' Investments

The Banks' Investment Index is one of the important indices that shows the volume of actual investments in banks' budgets and highlights the importance of such investments contributing to the realization of returns and increased profits for banks, especially if these investments strengthen economic sectors and contribute positively to the national economy. Investments are financed by bank's own capital and available deposits, as they appear on the assets side of bank's budget. Investment volumes are measured against total assets to determine its importance and volume for the bank. If the ratio of active banks' investments is high, it reflects the bank's efficiency in managing liquidity, generating returns, and increasing profits for the bank; it may have a positive impact on the real sector of the economy by financing projects and promoting economic growth. Figure No. (7) illustrates the decrease of total investment volume to commercial banks' total assets from (16.1%) for Q2 2022 to (14.6%) for the same quarter of 2023 due to the growth of assets volume by (12.7%), which is greater than the growth of investment volume of (2.5%). As well as the decrease of the ratio of State-Owned Banks investments to their total assets from (17.1%) for Q2 2022 to (15.4%) for the same quarter of 2023. As for private banks investments to their total assets, it decreased from (12.3%) for Q2 2022 to

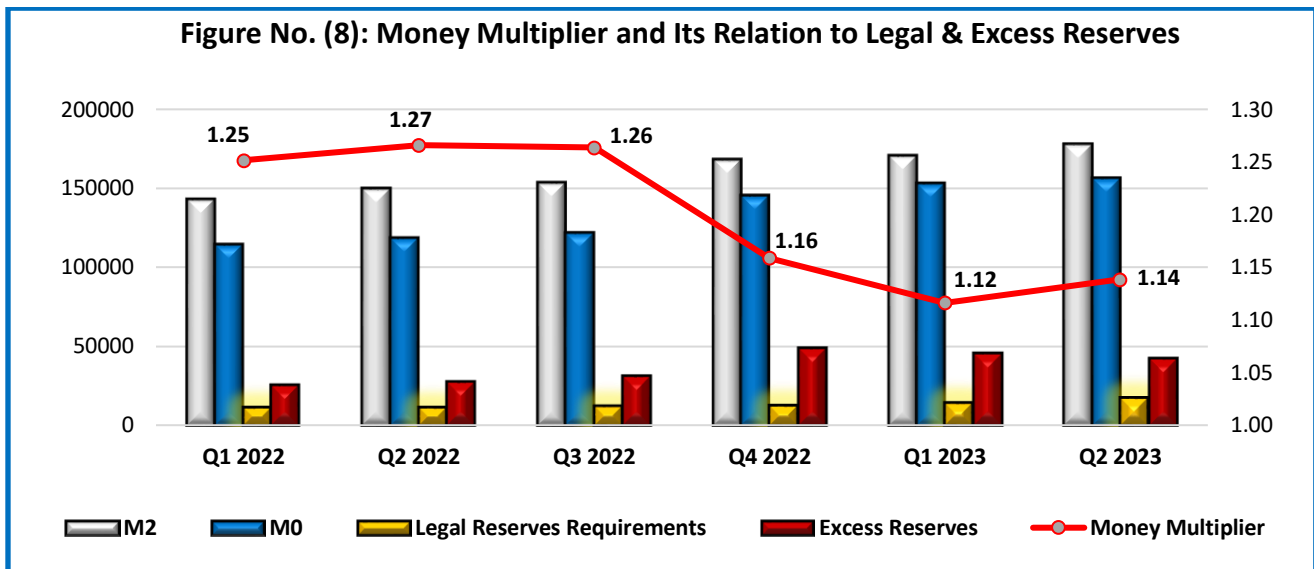
(11.9%) for the same quarter of 2023. Total State-Owned Banks investments constituted (82.9%) of the total investment of the banking sector because of the public confidence attributed to the large banking activity provided by these banks and the network of branches that are spread across the governorates of Iraq, while private banks investments accounted for only (17.2%) of banking sector total investments.



Source: Central Bank of Iraq, Statistics and Research Department, Monetary & Financial Statistics Division.

5- Money Multiplier

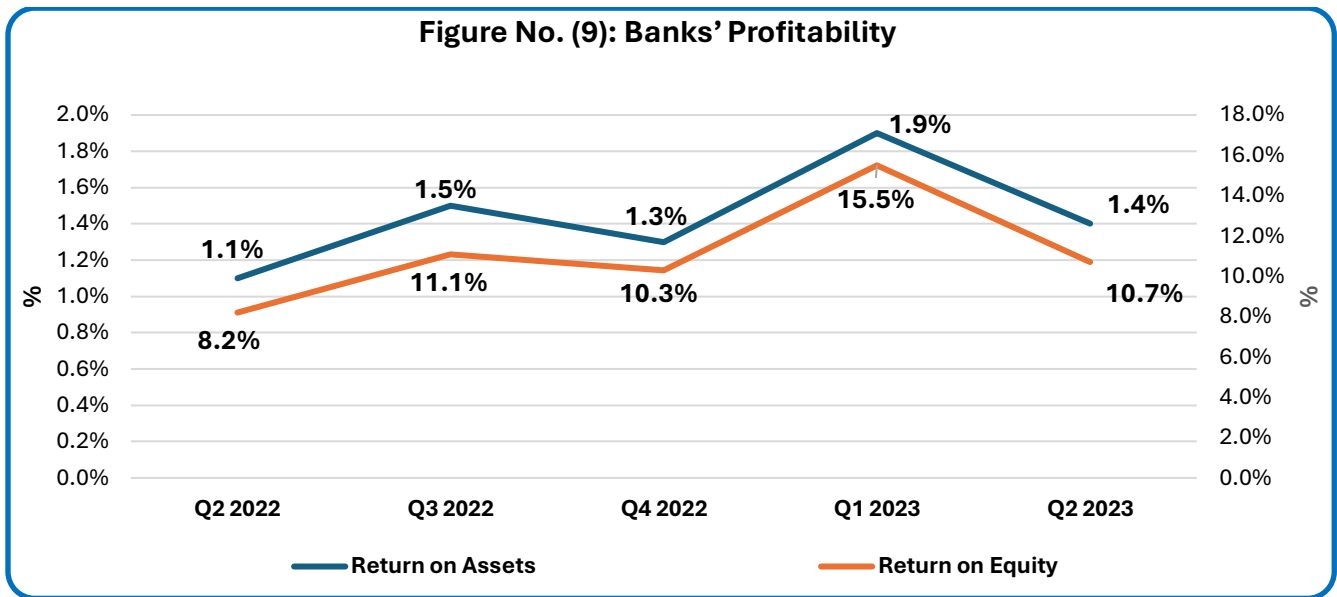
The Money multiplier reflects banks' ability to create money through the process of creating deposits; it is calculated by dividing broad money supply (M2) on the cash basis (M0). Figure No. (8) illustrates the decrease of money multiplier ratio to (1.14%) for Q2 2023 compared to (1.27%) for the same quarter of last year. The decrease of money multiplier ratio is due to the growth of cash basis by (31.8%), which exceeded the growth of broad money supply of (18.5%). The high growth of cash basis in terms of uses is attributable to growth of legal reserves requirement with the central bank, which recorded a growth of (50.3%) as the Central Bank increased legal reserves requirements rate from (15%) for Q2 2022 to (18%) for the same quarter of the current year. Excess reserves, which constituted (27.1%) of total cash basis, achieved a growth of (54%) over the same quarter of the previous year because of increased total banking deposits (except for central government). As for the extended credit to central government, which is part of the central bank's net domestic assets, it recorded a decline of (21.5%) due to the central government paying a percentage of its discounted drafts with the central bank.



Source: Central Bank of Iraq, Statistics and Research Department, Estimates of Monetary & Financial Stability Division.

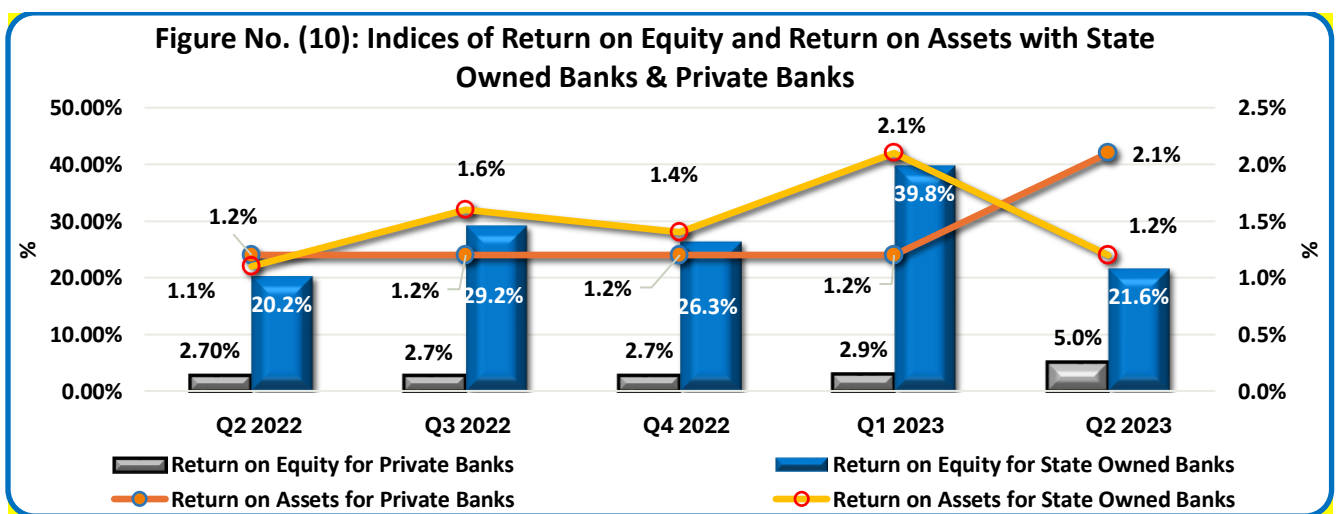
6- Bank’s Profitability

This index is used to measure the profits achieved by banks or losses they may incur. The index assesses two main aspects: Return on Equity Ratio, which assesses the efficiency of shareholders in using the bank's funds and their ability to make profits, and Return on Assets ratio, which reflects the bank's operational capability and efficiency in using assets to make profits. Figure (9) shows the increase in the return on equity ratio for the banking sector from (8.2%) in Q2 2022 to (10.7%) for the same quarter of 2023, and this indicates the effective use of its contribution in generating profits, and Figure (9) shows the increase in the return on assets ratio from (1.1%) in Q2 2022 to (1.4%) for Q2 2023. This indicates that banks make good use of the surplus part of their resources to achieve profits. The high percentages of these ratios reflect the effectiveness and efficiency of banks in managing their funds and achieving returns on them. This enhances confidence in the financial performance of banks and makes them attractive to investors and depositors. It is important that the Central Bank and supervisory authorities carefully monitor these ratios to ensure the sustainability and stability of the banking system.



Source: Central Bank of Iraq, Statistics and Research Department, Monetary and Financial Statistics Division.

The ratios mentioned in Figure No. (10) show an increase in the ratio of return on equity and return on assets with State Owned Banks, as the rate of return on equity increased from (20.2%) in Q2 2022 to (21.6%) for the same quarter of 2023, and the rate of return on assets for these banks for the same period increased from (1.1%) to (1.2%), and the return on equity and return on assets of private banks increased from (2.7%) for Q2 2022 to (5.0%) for Q2 2023, and the return on assets increased from (1.2%) to (2.1%) during the same period, and this indicates that government banks have the ability to achieve profits by investing its resources and assets effectively.

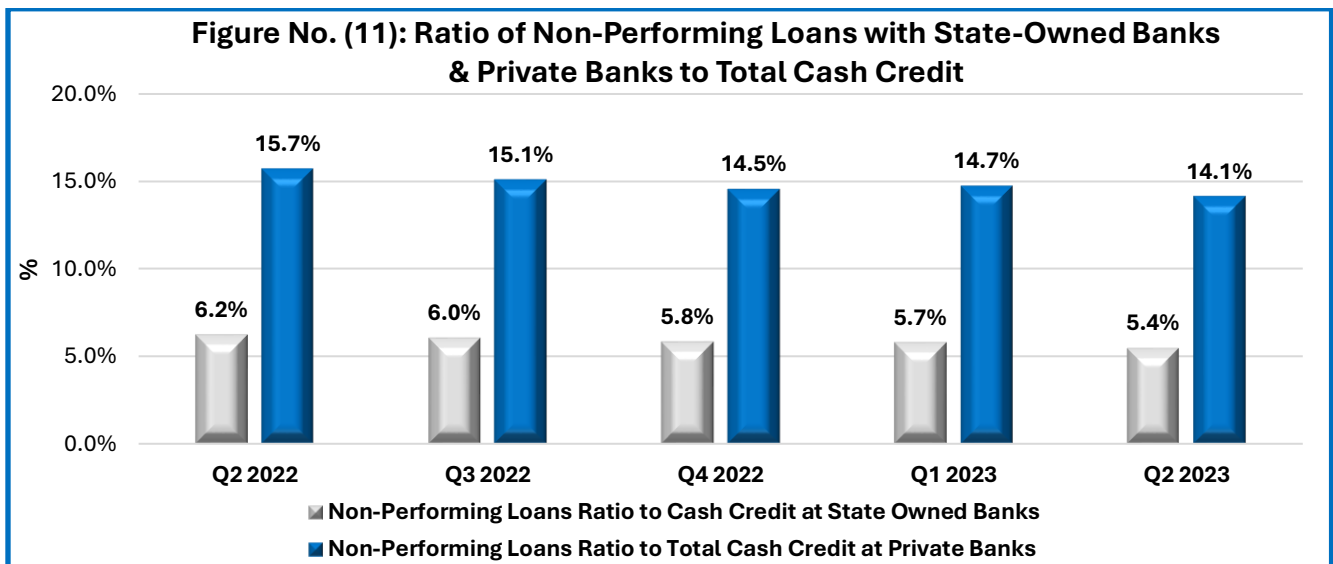


Source: Central Bank of Iraq, Statistics and Research Department, Monetary and Financial Statistics Division.

7- Non-performing Loans / Total Cash Credit

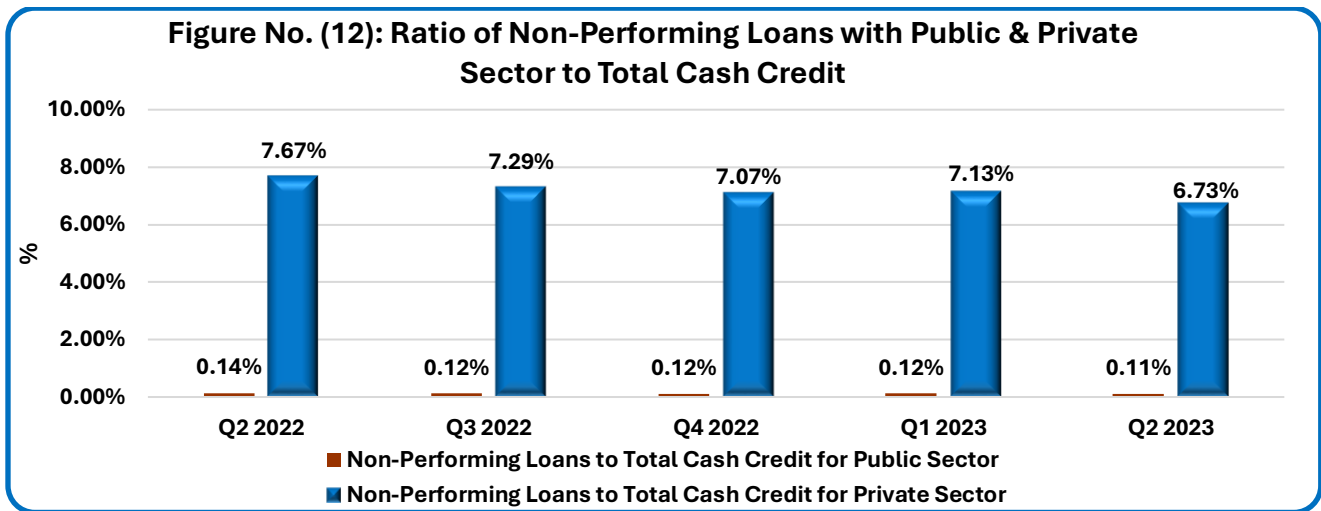
The ratio of non-performing loans compared to the total cash credit of banks decreased from (7.7%) in Q2 2022 to (6.8%) for the same quarter of 2023. This is due to a decrease in non-performing loans in the banking sector by (0.6%). This is a result of the conservative policies followed by banks in granting loans.

On the other hand, the ratio of non-performing loans to total cash credit with government banks decreased from (6.2%) for Q2 2022 to (5.4%) for the same quarter of 2023. The ratio of non-performing loans to total cash credit in private banks also decreased from (15.7%) for Q2 2022 to (14.1%) for the same quarter of 2023, while the ratio of non-performing loans was higher in banks.as shown in figure No. (11).



Source: Central Bank of Iraq, Statistics and Research Department, Monetary and Financial Statistics Division.

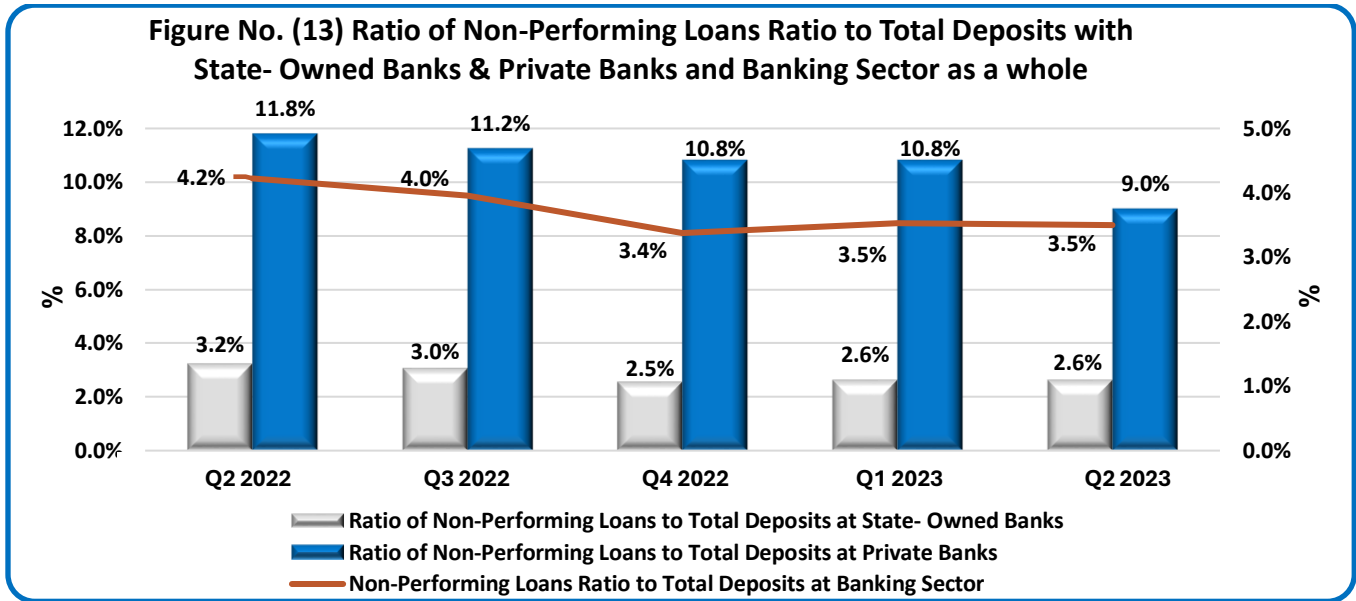
As for the distribution of non-performing loans to the ratio of cash credit, it is noted from Figure (12) that this ratio decreased in the private sector from (7.67%) for Q2 2022 to (6.73%) for the same quarter of 2023. And its decrease in the public sector from (0.14%) to (0.11%) for the same period of 2023 in the governmental sector, while non-performing loans of the private sector constitute (98.3%) of the total non-performing loans compared to the public sector, which constitutes (1.7%).



Source: Central Bank of Iraq, Statistics and Research Department, Monetary and Financial Statistics Division.

8- Non-performing Loans / Total Deposits

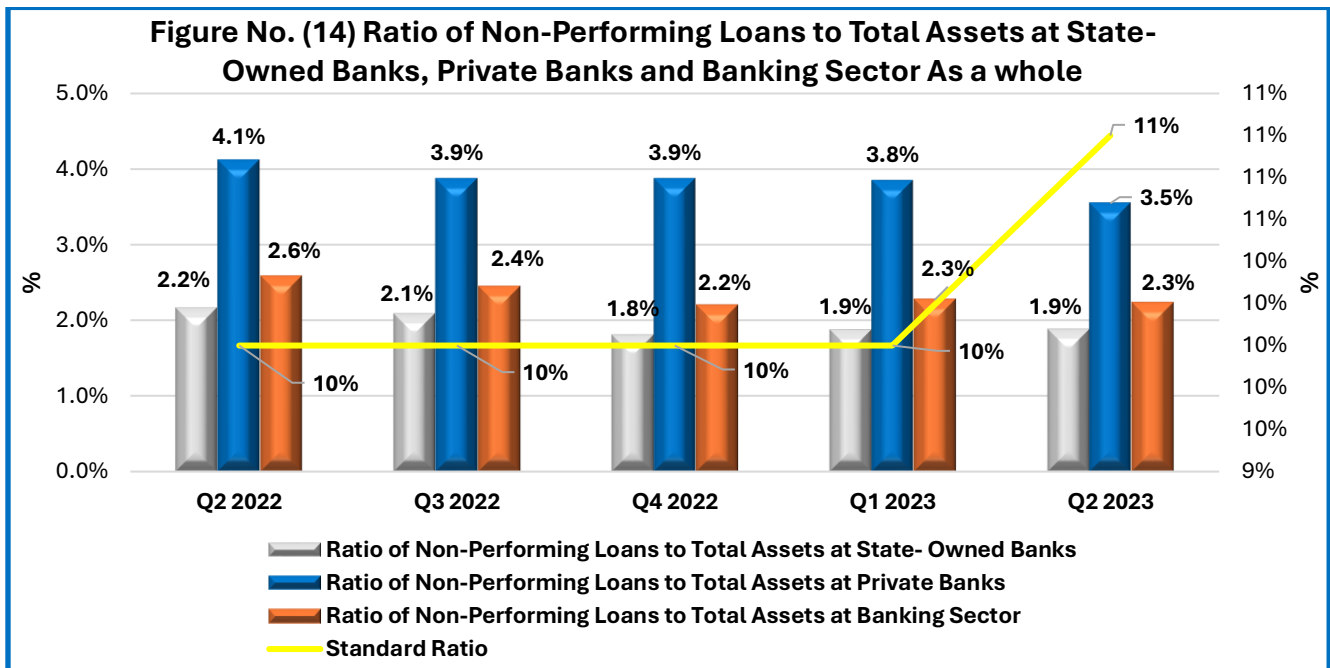
This index is measured by dividing non-performing loans to total deposits in banks. Figure (13) shows the decrease in the ratio of non-performing loans to total deposits in the banking sector from (4.2%) for Q2 2022 to (3.5%) for the same quarter of 2023, and this decrease in the ratio of non-performing loans to total deposits indicates an improvement in the performance of the banking sector in managing its loans, as the ratio of non-performing loans to total deposits in private banks decreased from (11.8%) to (9.0%), making good progress, although it is still high compared to state- owned banks. This is due to the volume of large state- owned banks deposits, in which the ratio of non-performing loans to total deposits decreased from (3.2%) for Q2 2022 to (2.6%) for the same quarter of this year, and these ratios reflect an improvement in the non-performing loans index to total deposits in the banking sector to reflect the increased ability of banks to deal with challenges related to non-performing loans.



Source: Central Bank of Iraq, Statistics and Research Department, Monetary and Financial Statistics Division.

9- Non-Performing Loans / Total Assets

This index is measured by dividing non-performing loans by the total assets of banks, that the standard value of this ratio is (11%)¹, and Figure (14) shows the decrease in the ratio from (2.6%) for Q2 2022 to (2.3%) for the same quarter of 2023, so the ratio of non-performing loans to total assets did not exceed the standard ratio, indicating that banks manage their loan portfolio effectively and control credit risk well.



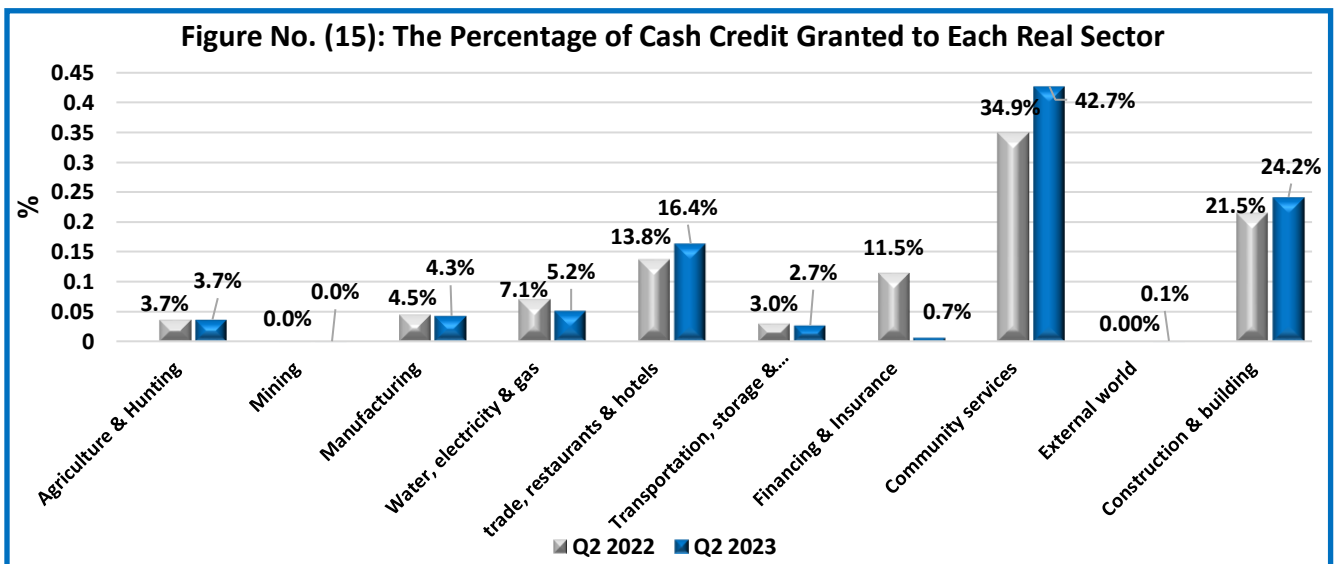
Source: Central Bank of Iraq, Statistics and Research Department, Monetary and Financial Statistics Division

¹ ASli Demirguc – Kunt and Enrica Detragiache ,The Determinants of Banking Crises in Developing- and Developed Countries, International Monetary Fund, 1998, Vol 45.

It is noted that the index of the ratio of non-performing loans to total assets in private and state- owned banks shows an improvement for the period (Q2 2022 - Q2 2023), as the ratio in private banks decreased from (4.1%) to (3.5%). The percentage also decreased in State-Owned banks from (2.2%) to (1.9%). This low ratio in both banks indicates that there are no significant asset quality risks in the banking sector. It should be noted that State-Owned banks have a larger share of the total assets of the banking sector, which shows the stability of the banking system in general.

10- Sectoral Distribution of Non-Performing Loans

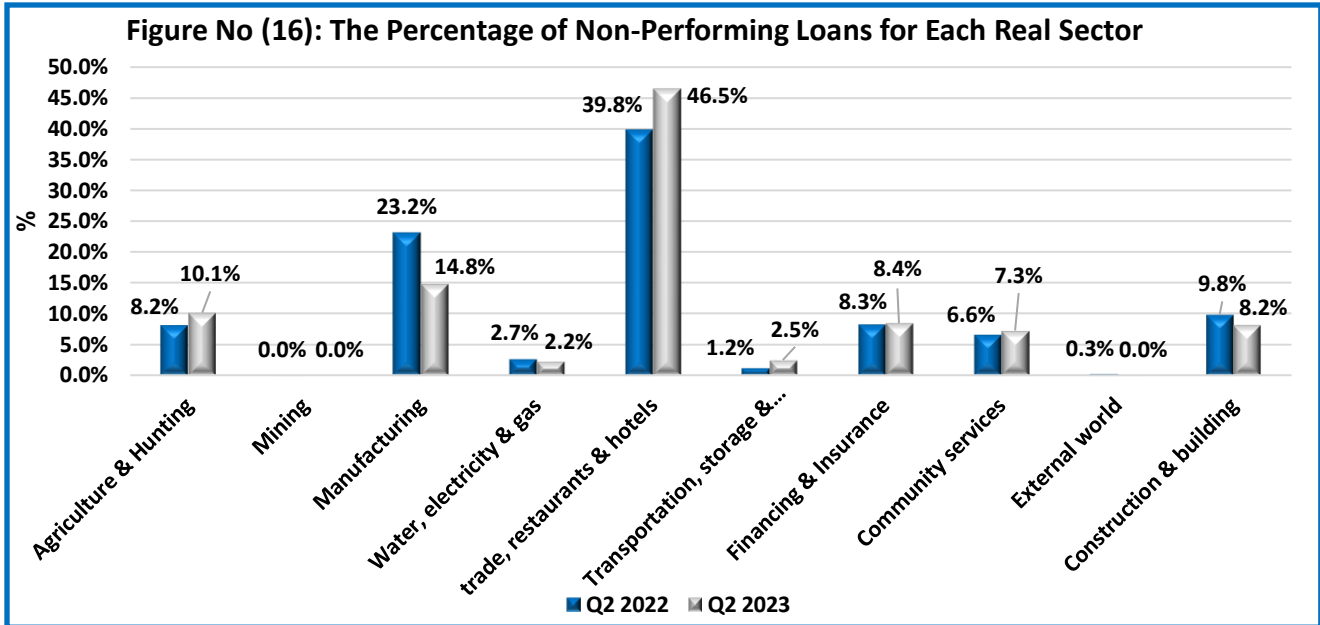
The trade, restaurants, hotels, community services, construction and building sectors, and the external world witnessed an increase in their contribution rates to the cash credit granted for these sectors, reaching rates of (16.4%), (42.7%), (24.2%), and (0.1%) respectively, as shown in figure No. (15).



Source: Central Bank of Iraq, Statistic and Research Department, Monetary and Financial Statistic Division.

As for the distribution of non-performing loans across sectors, it is noted from the figure No. (16) an increase in the percentage of non-performing loans in the trade, restaurants, and hotels sector to (46.5%) in Q2 2023, compared to (39.8%) for the same period in 2022. This is followed by a decrease in the percentage of non-performing loans in the manufacturing sector for the same period from (23.2%) to (14.8%). In addition to a decrease in non-performing loans in the construction and building sector from (9.8%) for Q2 2022 to (8.2%) for the same period in 2023. Whereas non-performing loans of the agriculture sector increased from (8.2%) for Q2 2022 to (10.1%) for the same quarter in

2023. This requires banks to take more cautious measures in granting loans, including the type of guarantees applied.

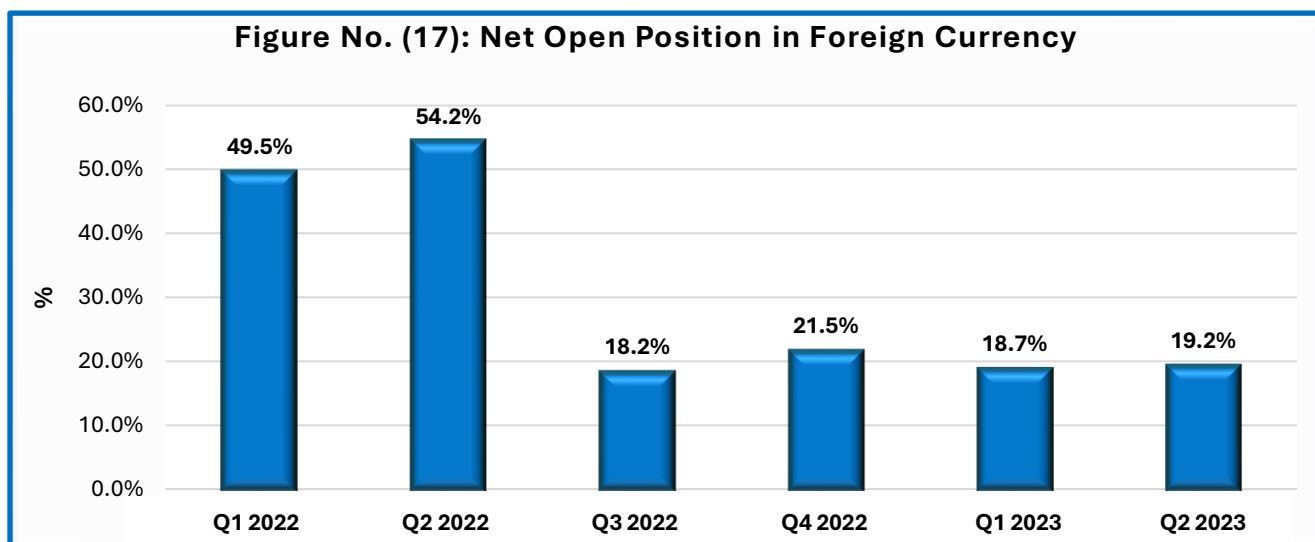


Source: Central Bank of Iraq, Statistics and Research Department, Monetary and Financial Statistics Division.

11- Net Open Position in Foreign Currency for Capital

The Banks’ involvement in the banking businesses makes them more vulnerable to financial losses resulting from market risks, and exchange rate risks are considered one of its most important components. In addition, some countries allow banks to engage in stock markets trading, which exposes them to stock price risks. The net open position in foreign currency, which is calculated through the difference between (foreign assets and liabilities) to (capital), is the most common measure of exchange rate risks.

The net open position for Q2 2023 recorded a decrease to (19.2%) compared to (54.2%) for the same quarter of the previous year. This rate is within the limits of the standard percentage specified by the Central Bank of (20%). This decrease is attributed to the decline in net foreign assets by (63.2%) in addition to the achievement of banks' capital growth by (4%), as shown in figure No. (17).



Source: Central Bank of Iraq, CBI Official Website.

Table No. (2): Indices of Banking Sector Performance

Index	Q2 2022	Q2 2023	Rate of Change %
Deposits in broad money supply to M2 (%)	49.3	47.9	-2.8
Currency in circulation to M2 ratio (%)	50.7	52.1	2.8
Total cash credit to total deposits (%)	54.0	50.7	-6.1
Money multiplier (%)	1.27	1.14	-10.2
Currency in circulation to current deposits (%)	144.3	6.7	-95.4
Return on equity (%)	8.2	10.7	30.5
Return on assets (%)	1.1	1.4	27.3
Return on equity of private banks (%)	2.7	5.0	85.2
Return on assets of private banks (%)	1.2	2.1	75
Non-performing loans to total cash credit (%)	7.7	6.8	- 11.7
Non-performing loans to total deposits (%)	4.1	3.5	- 14.6
Non-performing loans to total assets (%)	5	2.3	-54.0
Net foreign assets to bank capital (%)	54.2	19.2	-64.6

The table was prepared based on data from:

- Central Bank of Iraq, Statistics and Research Department, Monetary and Financial Statistics Division.
- Central Bank of Iraq, Statistics and Research Department, Balance of Payments and Foreign Trade Statistics Division.

Conclusion

- 1- The decline continued in the rate of deposits to the broad money supply during the period of (2022-2023), which shows the weak performance of banks in attracting deposits.
- 2- The rise continued in the rate of currency outside banks to the broad money supply, which is attributed to the monetary nature of the Iraqi economy, in addition to the rise in prices. This situation made individuals keep a larger amount of money to obtain the same previous goods and services.
- 3- The rise continued in the rate of government deposits to total deposits to record (56.41%) of total deposits.
- 4- The return on equity took an upward tendency since Q2 2022. While it is noted that the return on assets increased in Q2 2023 after decreasing for the first time in Q1 2023 since Q2 2022. This is due to its decline in government banks during this quarter.
- 5- The decline continued in the rate of non-performing loans to total cash credit, as well as the rate of non-performing loans to deposits.
- 6- The non-performing loans recorded a low rate of (2.2%) to assets, which is much lower than the standard rate of (11%).
- 7- Agriculture, trade, restaurants, hotels, and community services recorded an increase in non-performing loans for this quarter compared to the same quarter of the previous year.
- 8- The service sector accounts for the largest percentage of the volume of credit granted. However, its default rate is low, which indicates the strength and stability of this sector. While the trade, restaurants and hotels sector recorded the highest default rate, although it records a rate of (16.4%) from the total cash credit granted.

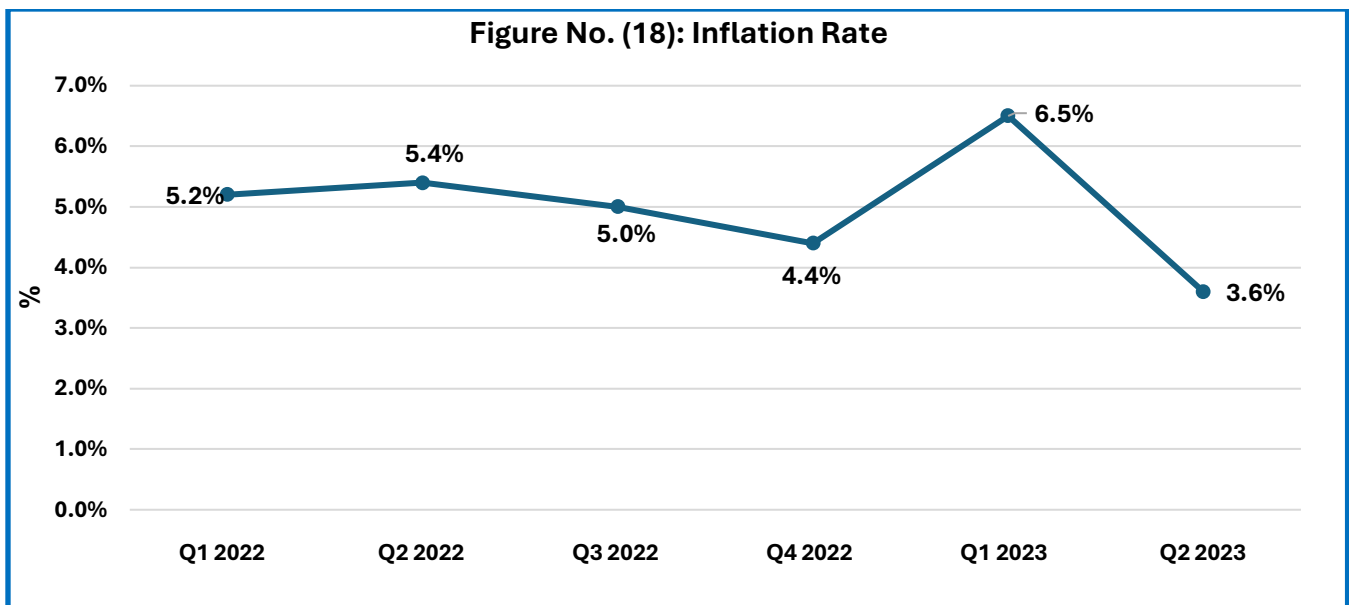
Chapter Three: Macroeconomic Performance Indices

This chapter analyzes and measures macroeconomic indices to identify the economic variables affecting the economy. The most important of these variables are inflation, internal public debt index, and implicit GDP deflator that shows the limits of production capabilities within the Iraqi economy, in addition to measuring GDP gap index.

Those macroeconomic indices are as follows:

1- Inflation Rate

The consumer price basket in Iraq recorded an increase for Q2 2023 to (120.8) points compared to (116.6) points for the same quarter of the previous year causing inflation of (3.6%) on an annual basis lower than Q1 2023, in which inflation rate reached (6.5%). This is attributed to the measures taken by Central Bank of Iraq in changing the exchange rate of IQD to US Dollar from (1450) to (1300) Iraqi dinar per US dollar to achieve the bank's goal of stabilizing the general price level and protecting the purchasing power of citizens. Especially, since the official exchange rate finances imports and allows greater stability in the prices of goods and services, as shown in figure No. (18).

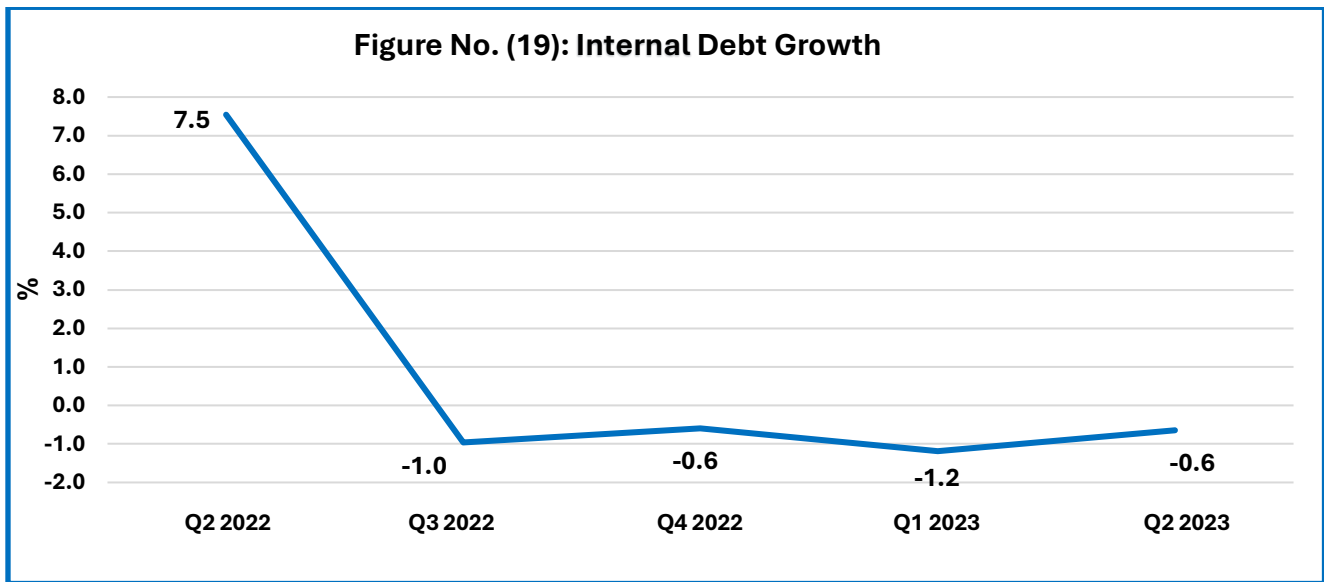


Source: Central Bank of Iraq, Basic Financial Data.

2- Internal Debt Growth Rate

The internal public debt recorded a decrease of (-0.6%) to reach (69.7) trillion dinars in Q2 2023 compared to (70.12) trillion dinars in Q2 2022. This is attributed to a decrease in bonds by (-32.12%) to reach (1.99) trillion dinars for the current year compared to Q2 the previous year, which was amounted to (2.94) trillion dinars.

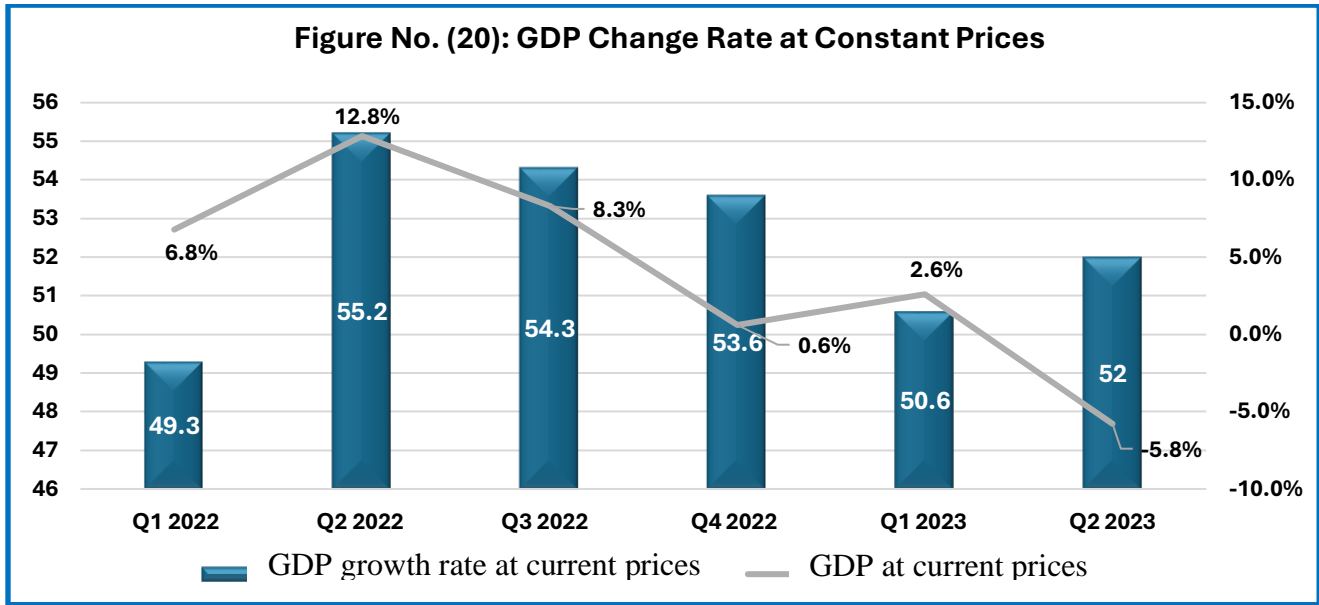
While treasury bills at commercial banks increased to the total internal public debt by (8.15%) in the current quarter compared to (7.93%) for Q2 2022. As well as the treasury bills discounted by Central Bank of Iraq to the total internal debt are increased from (63.1%) for Q2 2022 to (63.4%) for the same quarter of the current year, as shown in figure No. (19).



Source: Central Bank of Iraq, Statistics and Research Department.

3- Change Rate of Gross Domestic Product (GDP)

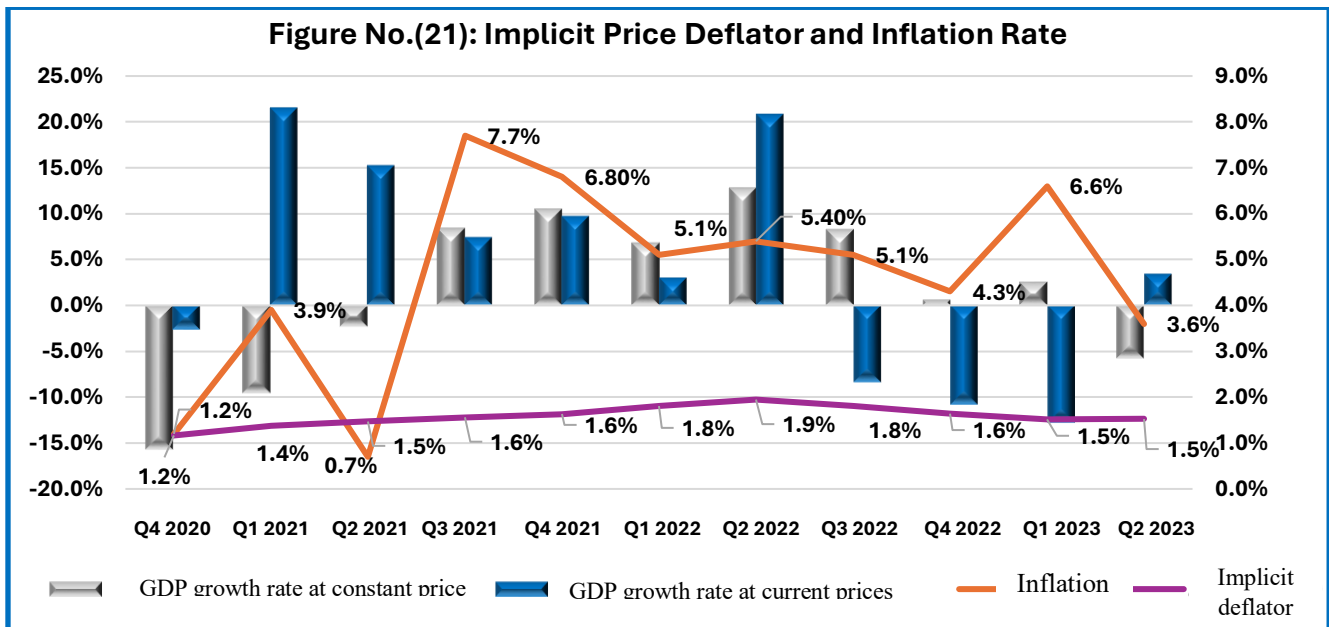
The GDP for Q2 2023 recorded a growth rate of (3.4%) compared to Q1 2023, reaching (79.2) trillion dinars, compared to (76.6) trillion dinars for Q1 2023, as shown in Figure No. (20). This is due to improvement in global oil prices, as crude oil constituted (41.5%) of the total GDP at current prices, and this increase indicates that the economy is affected by changes in global oil prices, which leads to economic challenges that require measures to stimulate the economy and diversify sources of revenue to ensure economic stability and reducing the negative effects on economic growth. While the real GDP growth rate decreased in Q2 2023 by (-5.8%) to reach (52.03) trillion dinars, compared to (55.2) trillion dinars for the same quarter of the previous year, and this is due to a decrease in crude oil production after the voluntary reduction approved by OPEC+ to maintain crude oil prices.



Source: Ministry of Planning, Central Statistical Organization, GDP data for Q1 2023.

4- Implicit Price Deflator

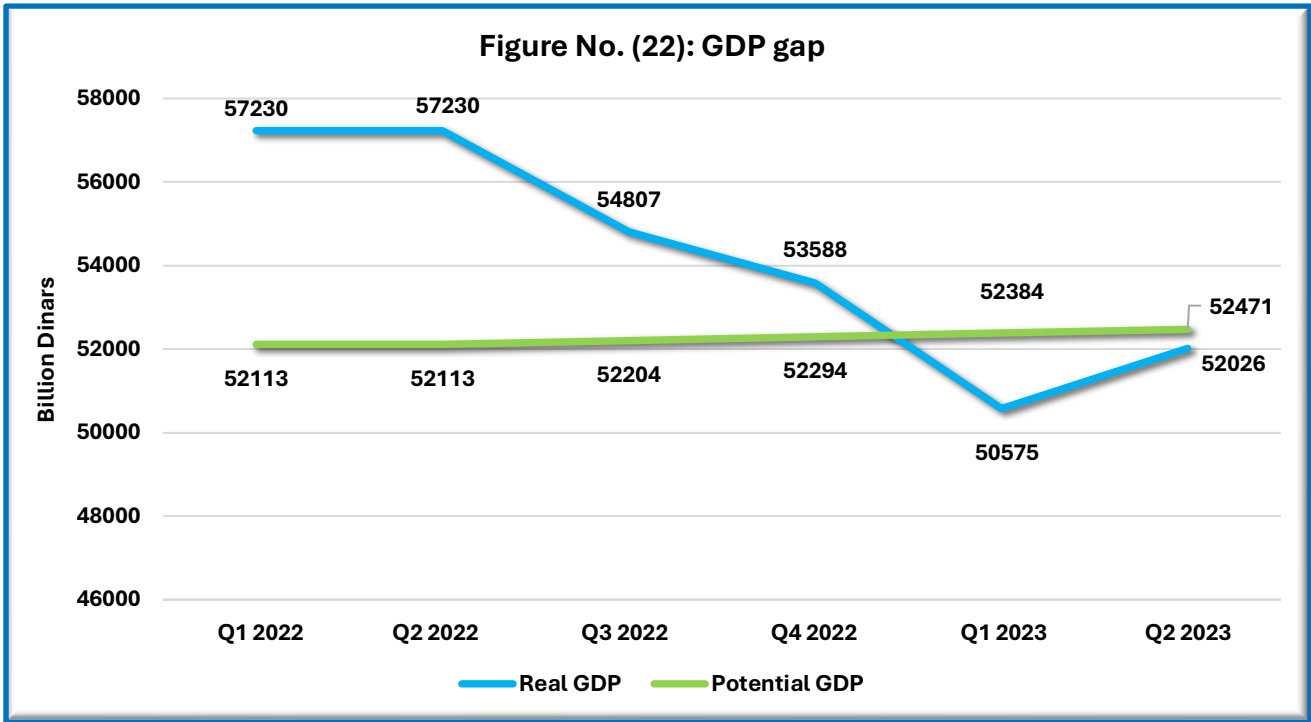
The implicit price deflator (IPD) for Q2 2023 recorded a decrease to reach (1.5%) compared to its rate of (1.9%) for the same quarter of 2022, due to the decline in the value of the GDP at current prices from (107.56) trillion dinars for Q2 2022 to (79.24) trillion dinars for the same quarter of 2023. The real GDP for Q2 2023 decreased to (52.03) trillion dinars compared to its value of (55.2) trillion dinars for the same quarter of the previous year, a decrease rate of (5.8%), as shown in figure No. (21).



Source: Ministry of Planning, Central Statistical Organization, GDP data for Q2 2023.

5- GDP gap²

GDP gap recorded a negative value of (- 445) billion dinars for Q2 of this year, after registering a positive value of (5117) billion dinars in the same quarter of 2022. This situation shows that there is a slowdown in economic growth and challenges affecting the growth of the economy, indicating that the economy's potentials are not fully exploited as shown in figure No. (22).



Source: Central Bank of Iraq, Estimates of Monetary and Financial Stability Division and according to Ministry of Planning, Central Statistical Organization.

² Measures the difference between real (actual) GDP and possible (potential) GDP as a percentage.

Table No. (3): Macroeconomic Performance Analysis Indices

Index name	Q2 2022	Q2 2023	Rate of change %
Inflation rate (%)	5.4%	3.57%	33.9%
Growth of Internal Public Debt (%)	7.5	-0.6	-108.5
Treasury bill ratio at commercial banks to total Internal Public Debt (%)	7.93	8.15	2.8
Treasury bill ratio deducted from the Central Bank to total internal public debt (%)	63.1	63.4	0.5
Average of change in GDP for the first and second quarters of 2023 (%)	20.8	3.4	-83.7
Implicit Price Deflator to GDP (%)	1.9	1.5	-21.1
Real GDP (trillion dinar)	55.219	52.026	5.8
Current GDP (trillion dinar)	107.563	79.240	-26.3
GDP gap (billion dinar)	5117	-445	-108.7

The table was prepared based on data from:

- Central Bank of Iraq, Statistics & Research Department, Monetary & Financial Stability Division.
- Central Bank of Iraq, Statistics & Research Department, Balance of Payments and External Trade Statistics Division.

Conclusion

- 1- Inflation recorded an acceptable rate of (3.6) year on year during this quarter.**
- 2- Economic growth rate decreased by (-5.7 %) compared to the same quarter of previous year, despite it is increase by (3.4%) compared to previous quarter of the same year.**
- 3- Implicit price deflator decreased for this quarter compared to the same quarter of the previous year due to the decline in real and current GDP.**
- 4- GDP gap recorded a negative value which means that there is an economic contraction.**
- 5- The internal public debt recorded a decrease during this quarter, indicating the financials' ability to meet its obligations and not to resort to additional debt, but on the contrary, it began to pay off its debts.**

