Central Bank of Iraq
Statistics & Research Department
Monetary and Financial Stability Division

Early Warning Report for the Banking Sector

Q2 2024

No. Twenty - eight

Statistics and Research Department

Monetary and Financial Stability Division

Early Warning Report for the Banking Sector
(The Second Quarter – 2024)

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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.

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Introduction:

The early warning report for the banking sector is considered as one of the most important oversight tools for this sector. By analyzing a range of indices, the report can forecast impending and potential crises, even if they do not materialize, and measure potential deviations and influencing variables within the banking sector.

The report is comprised of three chapters that comprehensively cover the indices affecting the monetary authority's operations. The first chapter delves into the analysis of currency value stability indices, notably the ratio of net foreign reserves to broad money supply (M2). This ratio experienced a slight decline to 79.7% in the second quarter of 2024, compared to 80.2% in the corresponding quarter of 2023, surpassing the benchmark of 20% in both periods. The decrease can be attributed to a 0.8% increase in broad money supply, coupled with a more modest 0.1% growth in net foreign reserves.

Chapter two, which analyzes bank performance indices, reveals that the ratio of total credit to total deposits reached 55.5% in the second quarter of 2024. This figure remained below the central bank's stipulated standard of 75%. Additionally, the money multiplier ratio experienced an increase in the second quarter of 2024, reaching 1.15, compared to 1.14 in the same quarter of 2023. This upward trend is attributed to a 0.3% decrease in the monetary base during the same period. Concerning the non-performing loans to total credit ratio, it stood at 6.9% in the second quarter of 2024, remaining relatively close to the 6.8% recorded in the second quarter of 2023.

Chapter three delves into an analysis of several macroeconomic indices that impact Iraq's banking system. When examining the inflation rate, it is observed that it recorded 3.3% in the second quarter of 2024. Notably, the base year for calculating the price index was revised from 2012 to 2022. Regarding total public debt, a 3.6% increase was recorded in the second quarter of 2024 compared to the same period in 2023, driven by an increase in domestic debt despite a decrease in foreign debt. Foreign debt constituted 48% of the total debt in the same quarter. Furthermore, Iraq's gross domestic product (GDP) at current prices experienced a significant growth of 22.2% in the second quarter of 2024, reaching IQD 96.4 trillion, up from IQD 78.9 trillion in the corresponding quarter of 2023.

Chapter One

Analysis of Currency Value Stability Indices

Chapter One: Analysis of Currency Value Stability Indices

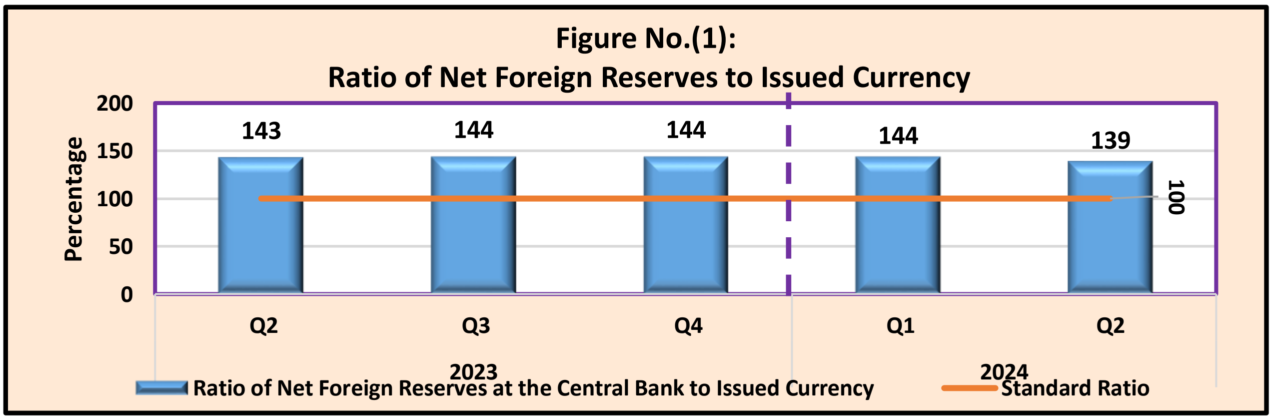
Currency value stability can be inferred by pursuing a range of important indices. The fact that all indices remain within acceptable ratios and without significant fluctuations indicates that the system is not exposed to external or internal shocks and that the currency's value trajectory remains stable. In case of significant fluctuations of indices, or part of them, it is considered a warning signal of possible currency value fluctuations in the coming months. Among the most important indices that provide an accurate analysis of fluctuations of the national currency value are the following:

First: Adequacy of Foreign Reserves:

The adequacy of foreign reserves in central banks is a key index of the stability of the financial and banking system and its ability to meet external challenges. These reserves enhance the protection of the national currency against fluctuations and increase investors' confidence in the economy. There are several indices to measure the adequacy of these reserves, including:

1. Adequacy of Net Foreign Reserves to Issued Currency Index:

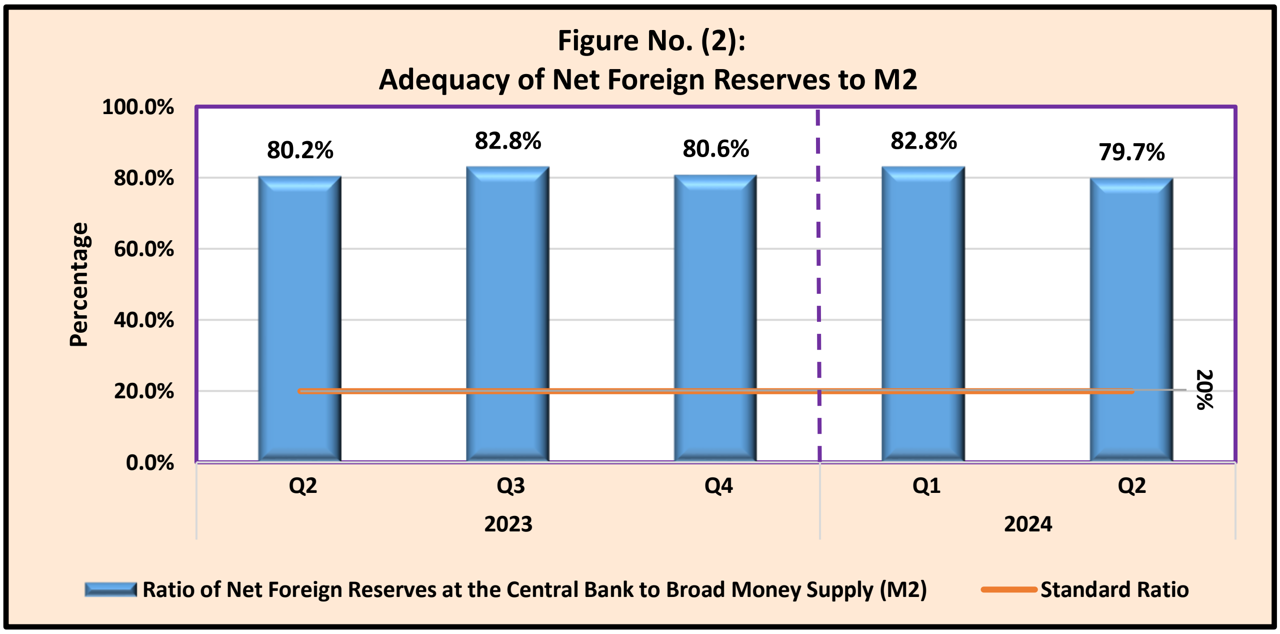
Net foreign reserves are the first line of defence to stabilize the national currency value and support the domestic economy, enabling the central bank to cope with foreign exchange fluctuations and protect the national currency value against such fluctuations, which requires maintaining an appropriate level of these reserves. The ratio of this index reflects the relationship between net foreign reserves and the value of the issued currency, as the ratio's rise is considered a positive index. Figure No. (1) shows a decrease of the coverage of net foreign reserves to the issued currency to (139%) for Q2 of 2024 compared to (143%) for the same period in 2023. This decrease is attributable to the persistent CBI defence of the value of the dinar by providing the required foreign currency by traders to import. In addition, the government's large demand for the central bank dinar to finance the expenditure led to issued currency growth of (2.3%), which is greater than the growth of net foreign reserves of (0.1%). However, this ratio remained positive and influential because it is higher than the standard ratio set at (100%).



Source: Central Bank of Iraq, Statistical Website.

2. **Adequacy of Net Foreign Reserves to Broad Money Supply (M2) Index:**

This index is measured by dividing net foreign reserves by (M2). Figure No. (2) shows that the ratio of net foreign reserves to (M2) for Q2 of 2024 reached (79.7%), well above the standard ratio of (20%). Although it decreased slightly by (0.6%) compared to the same quarter of 2023, as it was (80.2%) because of (M2) rise by (0.8%) with net foreign reserves rising by a less percentage reaching (0.1%) over the same period.



Source: Central Bank of Iraq, Statistical Website.

3. Coverage of Net Foreign Reserves to Total Imports Index:

This index is used to assess the quality of the country's economy and the stability of its financial system. International financial institutions such as the International Monetary Fund (IMF) and the World Bank (WB) are interested in monitoring this index to guide financial support when needed. In some countries, the minimum limit of this index varies from 4 to 5 months; it varies from one country to another according to its economic situation. Iraq's minimum acceptable limit of this index is 6 months [1].

The period of coverage of net foreign reserves to total imports for Q2 of 2024 decreased to 19 months, compared to 22 months for the same quarter of 2023 due to a rise of total CIF imports of IQD 22.5 trillion, from IQD 19.3 trillion during the same period, compared to a slight rise of net foreign reserves of IQD 142.7 trillion for Q2 of 2024 against IQD 142.6 trillion during the same quarter of 2023. As well as increasing the accuracy of balance-of-payments data after adopting the electronic

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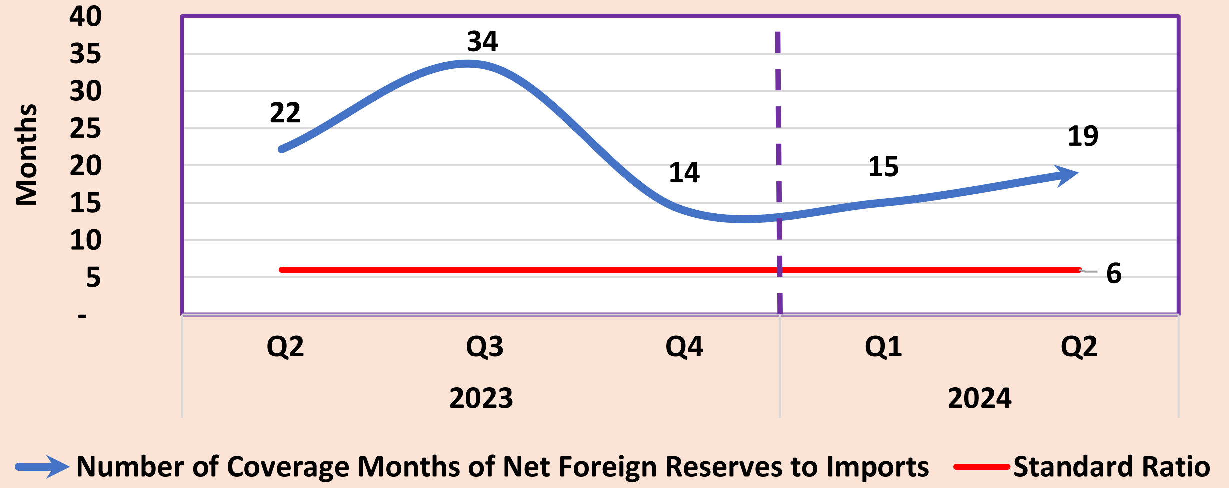
*1 Ali Mohsen Al-Alaq, International Reserves and Foreign Exchange Window at the Central Bank of Iraq, Central Bank of Iraq, Research and Studies, p. 7.

platform. It should be noted that the ratio is high and influential because it is higher than the standard ratio set at 6 months. As shown in Figure No. (3).

Figure No.(3):
Number of Coverage Months of Net Foreign Reserves to Imports



Source: Central Bank of Iraq, Statistical Website.

Second: Change of Interest Rates Averages:

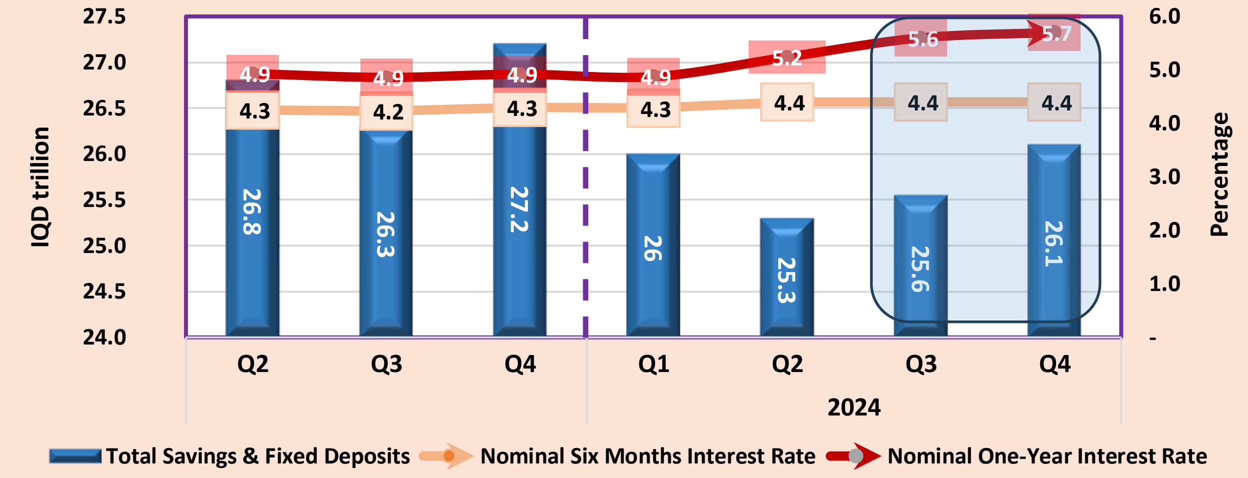
The change of interest rates averages is a vital index of the overall direction of the economy, as higher deposit rates are assumed to be an indicator of attracting currency in circulation and hoarding by individuals in favor of bank deposits. Thus, it increases banks' ability to grant credit and activate the economy because of increased fiscal depth. In the case of lower interest rates, deposits with operating banks will decrease owing to lower returns and higher currency in circulation, thus it lowers fiscal depth.

1. Short Term Interest Rates on Deposits:

The impact of interest rates on deposits volume depends on several factors, including the inflation rate, the banking awareness level of the public, and the level of services provided by the banking system. Figure No. (4) explains that higher or lower interest rates have a weak impact on deposits volume because of individuals' tendency to hoard rather than deposit with banks. The nominal six-month deposit interest rate rose slightly to (4.4%) for Q2 of 2024, while the nominal one-year deposit interest rate rose to (5.24%) for the same mentioned quarter. Total saving and fixed deposits decreased to reach IQD 25.3 trillion for Q2 of 2024 compared to IQD 26.8 trillion during the same quarter of 2023.

The nominal deposit interest rate is expected to stabilize on six months deposits at the same rate, while the one-year interest rate is expected to rise to (5.6%) and (5.7%) during Q3 & Q4 of 2024, respectively. As well as the deposits volume is expected to rise by a small percentage, meaning that the impact of interest rate change is weak on the deposits volume.

Figure No. (4):
Interest Rates and Total Savings & Fixed Deposits



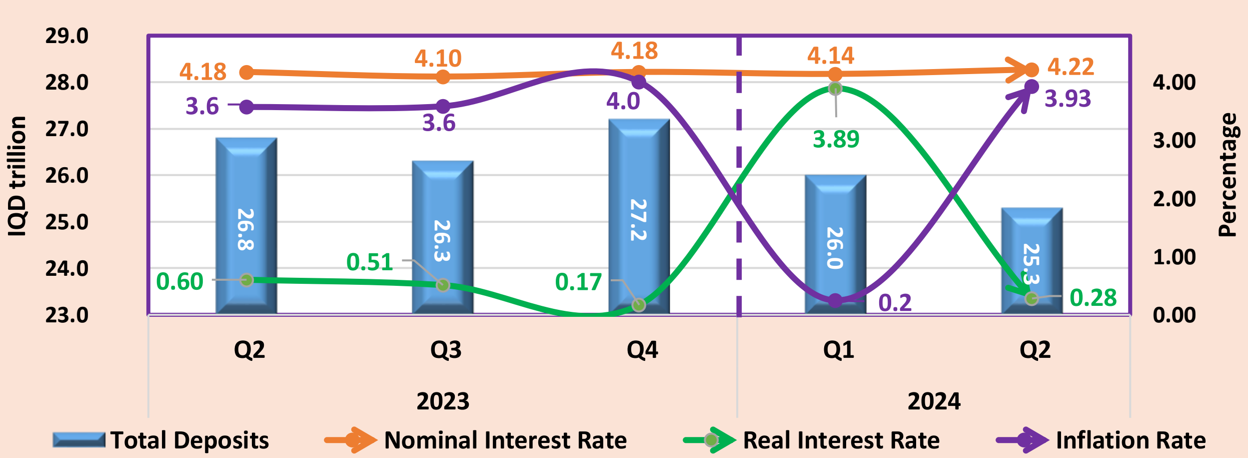
Source: Central Bank of Iraq, Statistical Website.

* Q3 & Q4 data for 2024 are forecasting data, based on the forecasts of Monetary and Financial Stability Division.

2. Real Interest Rate:

The real interest rate is an important index that takes into account inflationary pressures and their effects on nominal interest rates. Figure No. (5) shows a decline of real interest rate during Q2 of 2024 to (0.28%) compared to (0.60%) for Q2 of 2023 because of the rise of inflation rate from (3.6%) to (3.9%) during the same period. It should be noted that the base year was changed in calculating the consumer price index, as the data of 2022 was relied on instead of that of 2012, which was announced by the Ministry of Planning and reflected in the increase of real interest rate for Q1 of 2024 and the decrease of inflation rate during the same quarter.

Figure No. (5):
Nominal Interest Rate, Average of Real Interest Rate, and Inflation Rate



Source: Central Bank of Iraq, Statistical Website.

Table No. (1): Currency Value Stability Indices			
Index	**Q2 of 2023**	**Q2 of 2024**	**Change Rate %**
Net Foreign Reserves at the Central Bank (IQD trillion)	142,603	142,690	0.06
Issued Currency (IQD trillion)	99,998	102,312	2.31
Ratio of Net Foreign Reserves at the Central Bank to Issued Currency (%)	143%	139%	-2.8
Broad Money Supply (M2) (IQD trillion)	177,772	179,111	0.75
Ratio of Net Foreign Reserves at the Central Bank to Broad Money Supply (M2) (%)	80.2%	79.7%	-0.62
Total Imports Based on CIF (IQD trillion)	19	22	15.79
Number of Coverage Months of Net Foreign Reserves to Imports (Months)	26	19	-26.92
Total Fixed and Savings Deposits (IQD trillion)	27	25.3	-6.30

The table was prepared based on data of:

- Central Bank of Iraq, Statistics and Research Department - Statistical Website.
- Central Bank of Iraq, Statistics and Research Department – Balance of Payment and External Trade Division.

Chapter Two

Analysis of Banks' Performance Indices

Chapter Two: Analysis of Banks' Performance Indices

Banks' performance analysis is a fundamental pillar in assessing the efficiency of banks in investing their deposits and the credit they provide. This analysis reveals the strengths of banks and contributes to enhancing them. It also exposes weaknesses and helps find appropriate solutions. This is done by relying on a set of indices such as the total cash credit to total deposits index, the non-performing loans to total cash credit index, the non-performing loans to total deposits index, the money multiplier index, and the banks' profitability index, in addition to other indices that will be explained, as follows:

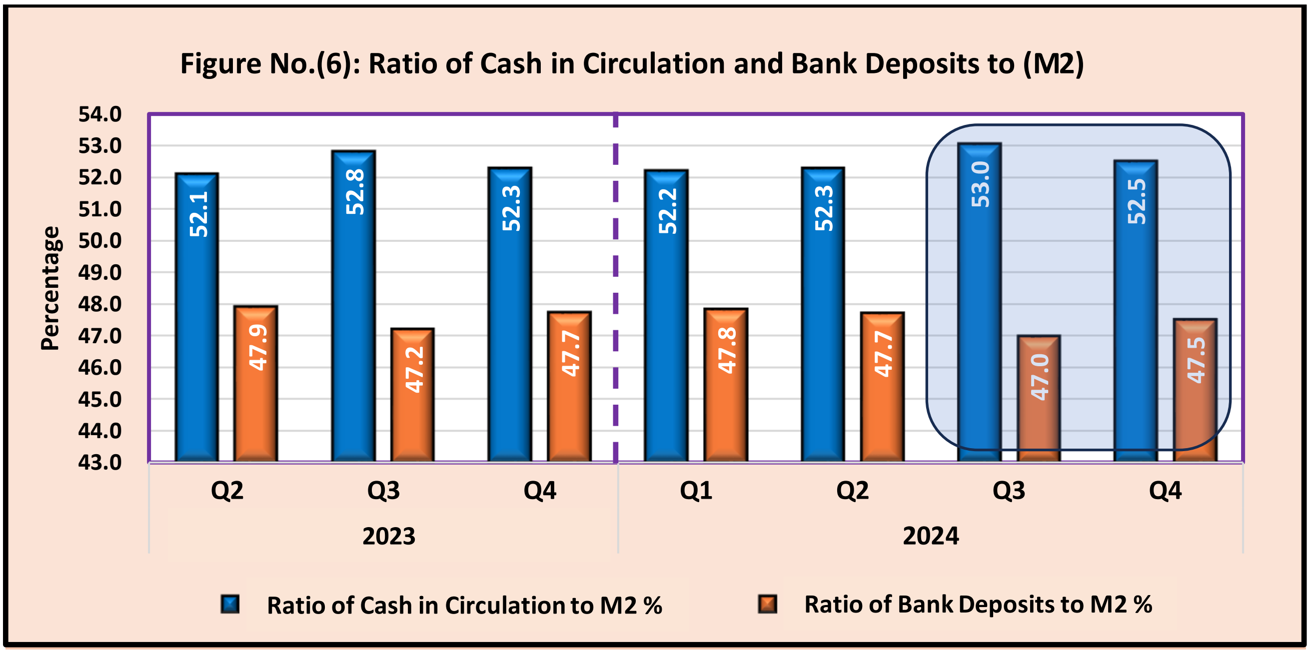
1. Outstanding Lending Facilities provided by the Central Bank to Total Banks' Liabilities

The existing lending facilities provided by the Central Bank of Iraq to banks as a last resort for lending vary according to the difficulties which banks are exposed to, as the facilities provide more financial support to banks. The Central Bank of Iraq Act No. (56) of 2004, in accordance with article 30, sets out the legal conditions for assisting banks experiencing financial crisis. The Central Bank of Iraq considers that banks must have sufficient liquidity to meet depositor withdrawals and to keep the banking system from collapse, so aid demand must be based on its need to improve liquidity, because the liquidity crisis reflects how much the banking sector is struggling. It is noteworthy that the Central Bank of Iraq did not provide loans to banks during Q2 of 2024, because banks did not need emergency liquidity or extraordinary withdrawals, or because they did not meet the aforementioned conditions.

2. Bank Deposits to Broad Money Supply (M2)

Bank deposits reflect the financial liquidity of banks, which can be obtained by diversifying the services provided to the public to attract a larger number of depositors to the bank. Therefore, this index represents the public's desire to turn to banks due to the need for the services that attract the public to them. In addition, the volume of deposits in a bank is an indicator of its activity on the one hand and the extent of the spread of its banking services on the other hand. This index is measured by dividing bank deposits by the broad money supply (M2). Figure No. (6) shows that the ratio of bank deposits to (M2) decreased slightly from (47.9%) in the second quarter of 2023 to (47.7%) in the same quarter of 2024. In turn, the index of cash in circulation to (M2) increased from (52.1%) in the second quarter of 2023 to (52.3%) for the same quarter of 2024. This indicates that a significant portion of the currency issued by the Central Bank of Iraq is going towards cash in circulation rather than bank deposits. This is due to a low level of banking awareness and the benefits of using the financial services offered by banks, despite the gradual improvement in the use of electronic payment tools.

The ratio of bank deposits to (M2) is expected to reach (47.0%) and (47.5%) respectively in the third and fourth quarters of 2024. Meanwhile, the forecast showed that the ratio of cash in circulation to (M2) will reach (53.0%) and (52.5%) respectively for the same period.



Source: Central Bank of Iraq, Statistical Website.

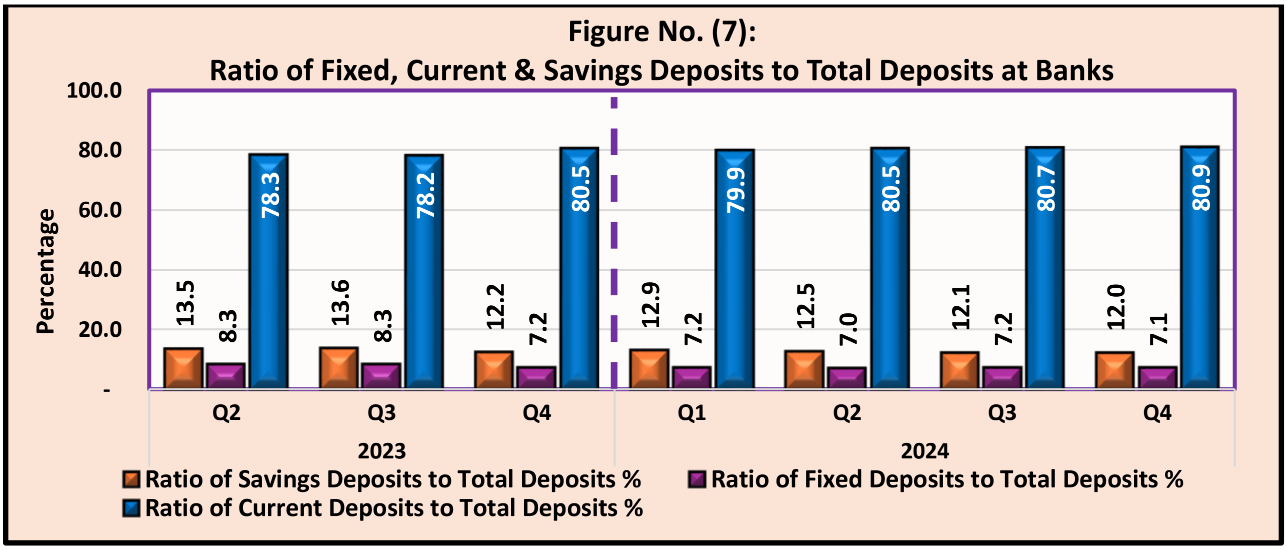
*** Q3 and Q4 of 2024 are forecast data based on estimates from the Monetary and Financial Stability Division.**

3. Types of Deposits at Banks in Iraq:

Through monitoring the types of deposits in banks, we find that current deposits have captured the largest share of total bank deposits. Their ratio to total deposits increased from (78.3%) in the second quarter of 2023 to (80.5%) in the same quarter of 2024. Meanwhile, the ratio of fixed deposits to total deposits decreased from (8.3%) in the second quarter of 2023 to (7%) in the same quarter of 2024.

As for the ratio of savings deposits to total deposits, it also decreased from (13.5%) in the second quarter of 2023 to (12.5%) in the same quarter of 2024. This means that banking awareness among individuals is still low, which requires operating banks to be more effective in attracting deposits by providing more services and increasing advertising that demonstrates the benefits of bank deposits. Figure No. (7) illustrates the volume of deposits in banks.

Forecasts indicate that the ratio of current deposits to total deposits will reach (80.5%) and (80.6%) in the second and third quarters of 2024, respectively. Forecasts show that the ratio of savings deposits to total deposits will be (12.4%) and (12.2%) respectively for the same period. As for fixed deposits, they are expected to record (7.1%) and (7.2%) respectively for the same period.



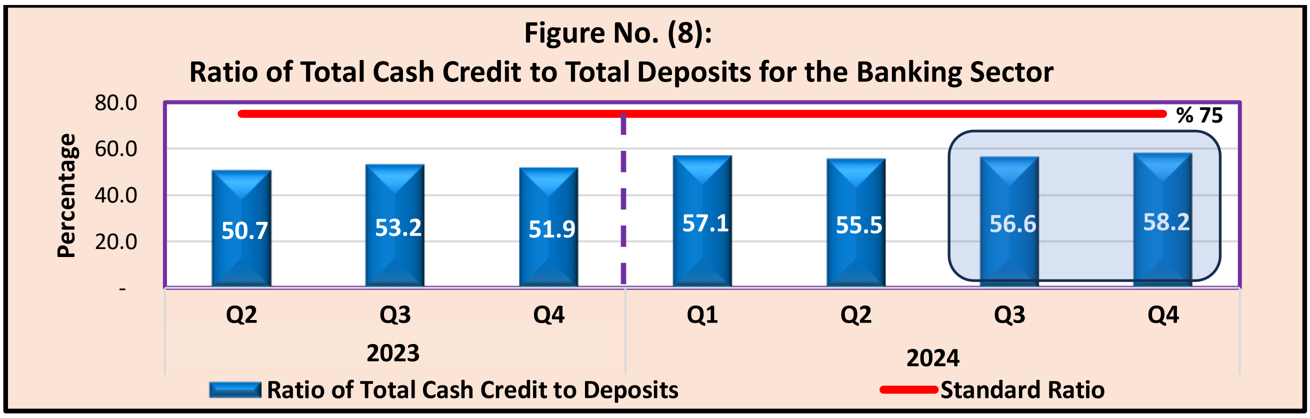
Source: Central Bank of Iraq, Statistical Website.

*** Q3 and Q4 of 2024 are forecast data based on estimates from Monetary and Financial Stability Division.**

4. Total Cash Credit to Total Deposits:

This index shows the banks' ability to utilize funds obtained from deposits to meet customer credit needs. The Central Bank of Iraq has set this ratio at (75%) to maintain sufficient liquidity for banks to meet customer withdrawals and conduct banking activities. This ratio is calculated by dividing total cash credit to total deposits at banks. It reflects the long-term liquidity position of the banking sector. Figure No. (8) shows that the ratio of total cash credit to total deposits increased from (50.7%) in the second quarter of 2023 to (55.5%) in the same quarter of 2024, due to a (13.6%) increase in the volume of credit granted compared to a (3.7%) increase in the volume of deposits for the same period. Despite this increase, the ratio of total credit to total deposits did not exceed the ratio set by the Central Bank of Iraq.

It is expected that the ratio of total cash credit to total deposits will increase to (56.6%) and (58.2%) for the second and third quarters of 2024, respectively.



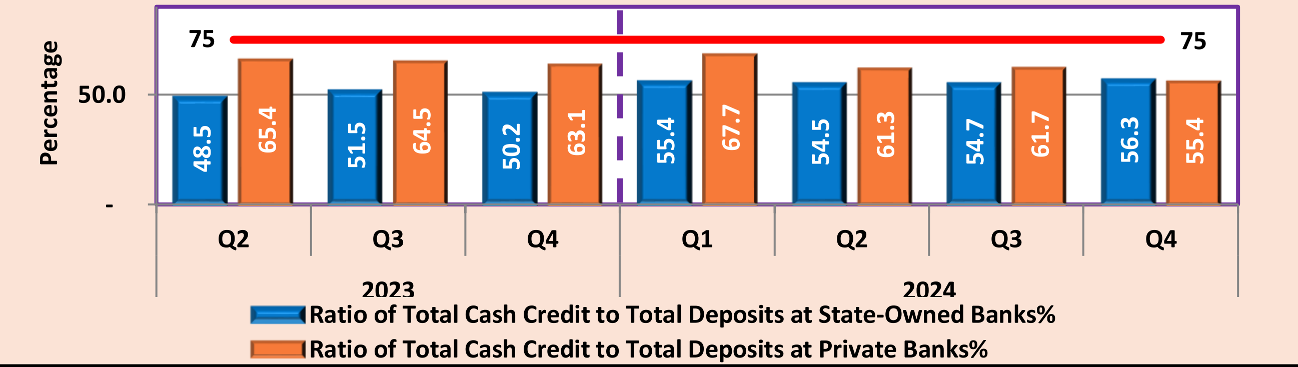
Source: Central Bank of Iraq, Statistical Website.

* Q3 and Q4 of 2024 are forecast data based on estimates from the Monetary and Financial Stability Division.

It is also shown that the ratio of total cash credit to total deposits at private banks is larger than that of state-owned banks, although the volume of deposits at state-owned banks is larger than the volume of deposits in private banks. Figure No. (9) shows that the ratio for private banks decreased from (65.4%) in the second quarter of 2023 to (61.3%) in the same quarter of 2024, because of a (18.9%) increase in total deposits at private banks. This is due to the continued increase in financial inclusion. This growth rate is higher than the 11% increase in credit extended by private banks. As for state-owned banks, the ratio experienced a growth from (48.5%) in the second quarter of 2023 to (54.5%) in the corresponding quarter of 2024.

It is expected that the ratio of total cash credit to total deposits for state-owned banks will reach (54.7%) and (56.3%) in Q2 and Q3 of 2024, respectively. For private banks, the ratio is expected to reach (61.7%) and (55.4%) respectively for the same period.

Figure No. (9):
Ratio of Total Cash Credit to Total Deposits for Both State-Owned & Private Banks



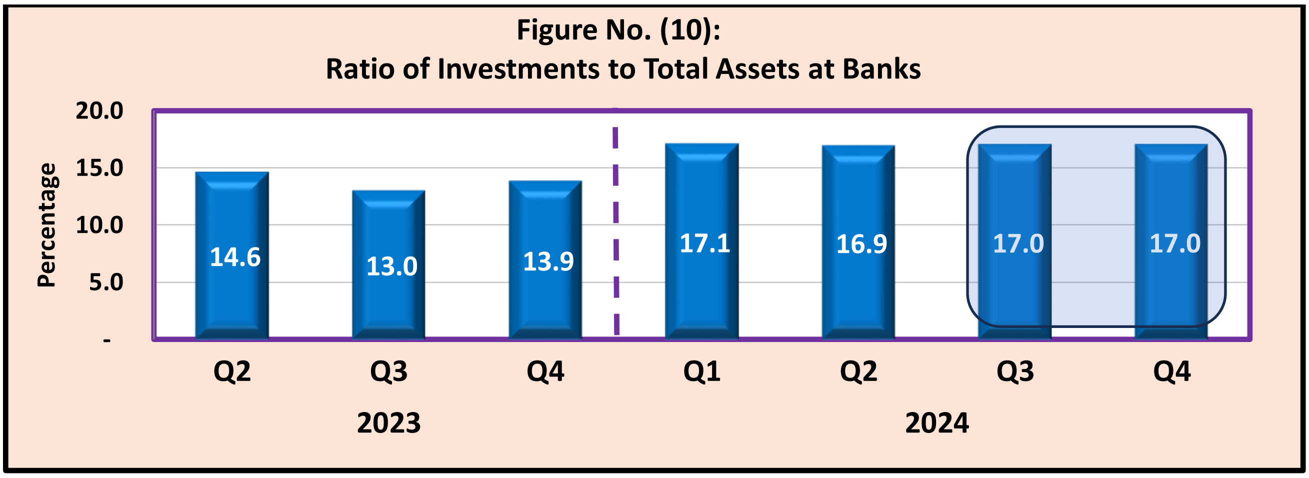
Source: Central Bank of Iraq, Monetary and Financial Statistics Division

* Q3 and Q4 of 2024 are forecast data based on estimates from the Monetary and Financial Stability Division.

5. Banks' Investments to Total Assets:

This index is considered a significant measure of the actual investments size within the balance sheet of banks. Investments are crucial because they generate returns for the bank and increase its profits, especially if these investments are in high-yield activities. Investments are funded by the bank's capital and available deposits and are listed as assets on the bank's budget. Therefore, they are measured against total assets to determine their size within the bank. Figure No. (10) shows that the ratio of total investments to total assets at banks increased from (14.6%) in the second quarter of 2023 to (16.7%) in the same quarter of 2024. This is the result of an increase in total investments by (22.9%) compared to an increase in total assets by (7.5%).

It is expected that the ratio of investments to total assets of banks will reach (17.0%) for Q3 and Q4 of 2024.

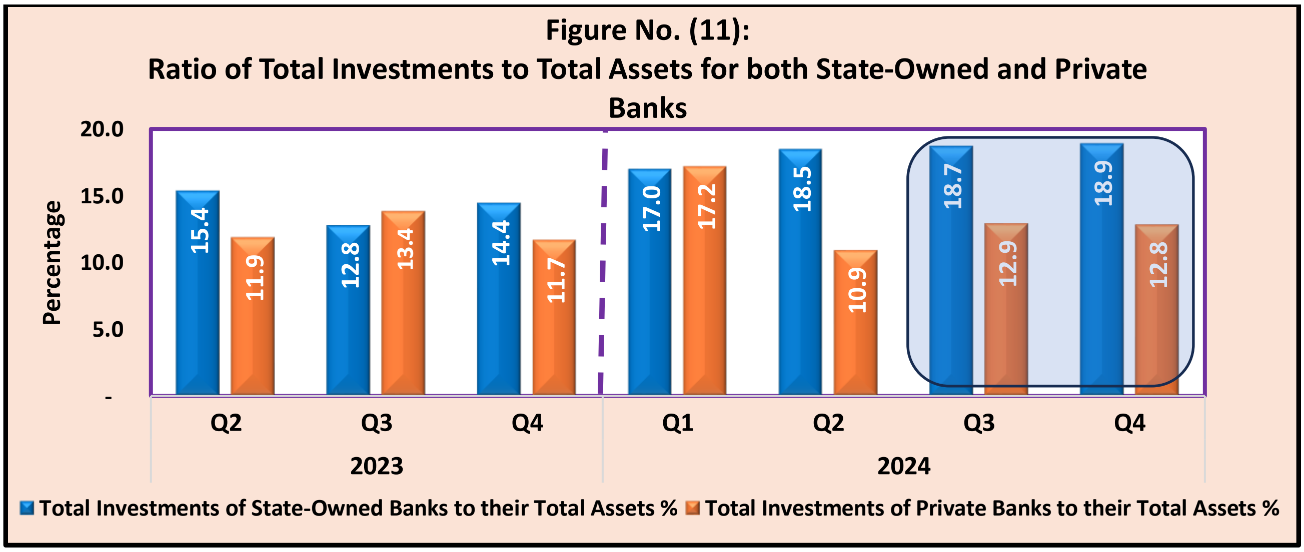


Source: Central Bank of Iraq, Monetary and Financial Statistics Division.

* Q3 and Q4 of 2024 are forecast data based on estimates from the Monetary and Financial Stability Division.

When looking at the classification of banks by ownership, we find that the ratio of investments to assets size for state-owned banks is higher than that of private banks. Figure No. (11) shows that the ratio of total investments to assets for state-owned banks has risen from (15.4%) in the second quarter of 2023 to (18.5%) in the same quarter of 2024, while the ratio of investments to total assets for private banks decreased from (11.9%) in the second quarter of 2023 to (10.9%) in the same quarter of 2024. It is worth noting that investments by state-owned banks accounted for (85%) of the total investments of all banks in the second quarter of 2024.

The ratio of total investments of private banks to their total assets is expected to be (12.9%) and (12.8%) during Q3 and Q4, respectively, and the ratio of total investments to total assets of state-owned banks to be (18.7%) and (18.9%) respectively for the same period.



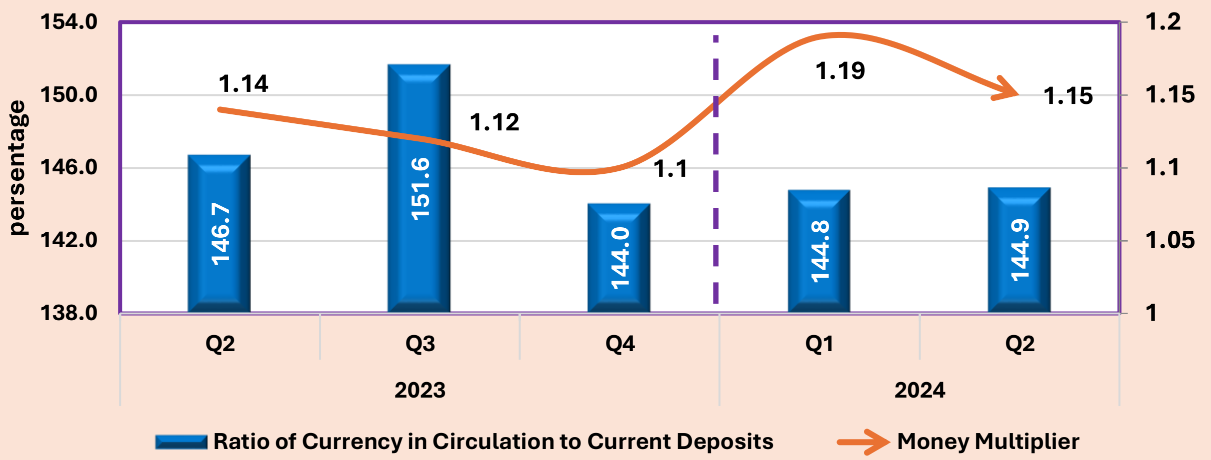
Source: Central Bank of Iraq, Monetary and Financial Statistics Division.

* Q3 and Q4 of 2024 are forecast data based on estimates from the Monetary and Financial Stability Division.

6. Money Multiplier:

A money multiplier is defined as the ratio that expresses the amount of new funds that banks can create through their existing reserves and is measured by dividing the broad money supply (M2) by the monetary basis. The money multiplier increased slightly in Q2 of 2024, reaching (1.15) compared to (1.14) for the same quarter of 2023, as a result of a rise in the broad money supply from USD (177.8) trillion to USD (179.1) trillion and a decrease in the monetary base from USD (156.1) trillion to USD (155.7) trillion. This reflects the banks' desire to keep their investment policy without significant changes during the same period despite the increase in their activity in Q1 of 2024, when the money multiplier reached (1.19). However, it returned to the same level during the aforementioned period. Figure No. (12) shows the money multiplier values during the same period.

Figure No. (12):
Currency in Circulation to Current Deposits and the Money Multiplier



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

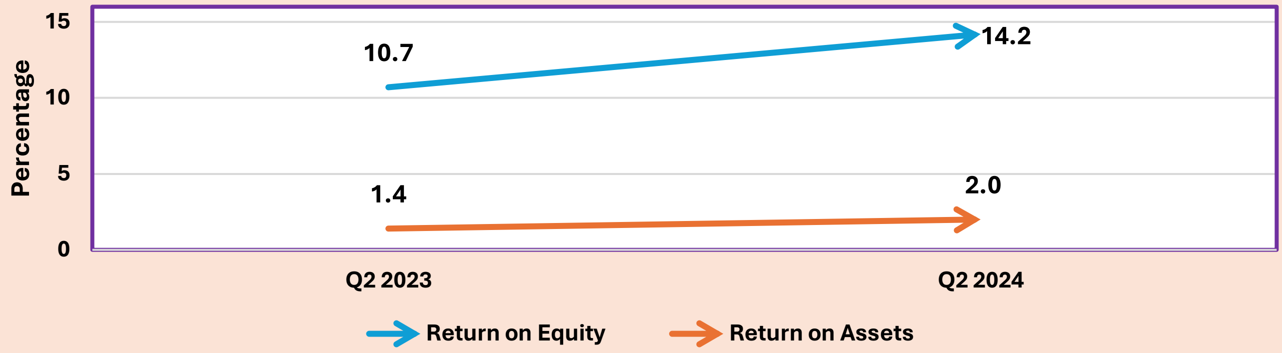
7. Banks' Profitability:

This index shows the profits earned or losses incurred by banks. Figure No. (13) illustrates return on equity and return on assets for banks operating within the banking system. We find that there has been an increase in the return on assets from (1.4%) in Q2 of 2023 to (2.0%) in the same quarter of 2024. However, the ratio of return on equity has increased from (10.7%) in Q2 of 2023 to (14.2%) in the same quarter of 2024. This is due to the increase in returns for banks during the same period.

Box (1)

In accordance with the Central Bank's Board of Directors' Decision No. (127), it has been decided to increase the capital of banks to a minimum of IQD (400) billion by December 31, 2024. This increase will be made in three installments, with each installment not less than IQD (50) billion. The first installment is due on December 31, 2023.

Figure No. (13):
Return on Equity and Return on Assets at Banks in Iraq

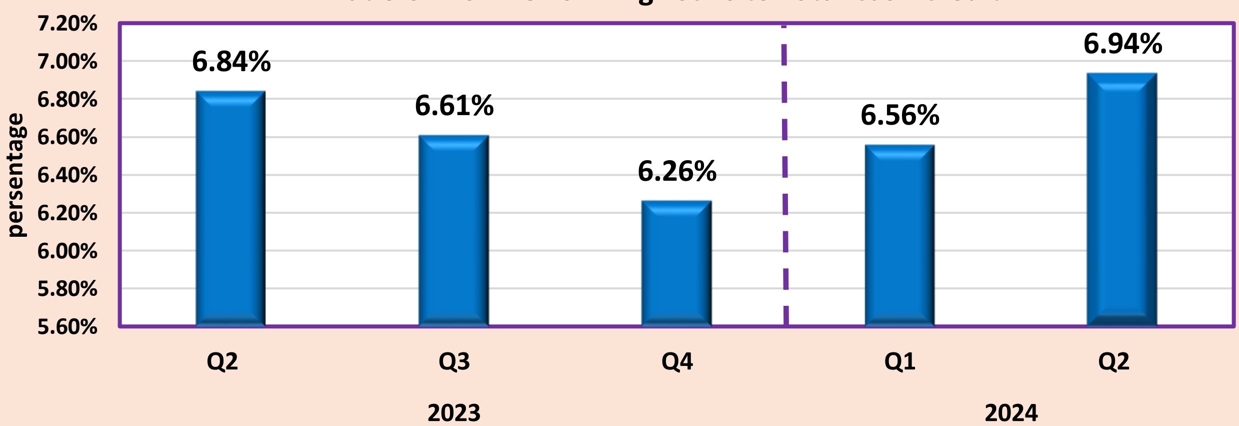


Source: Central Bank of Iraq, Statistics and Research Department, Monetary and Financial Statistics Division

8. Non-Performing Loans to Total Cash Credit:

This index is calculated by dividing non-performing loans by total cash credit. Figure No. (14) shows that the ratio of non-performing loans to total cash credit in Q2 of 2024 increased to (6.9%) from (6.8%) in the same quarter of 2023. This increase is due to the rise in the growth rate of non-performing loans by (14.8%), which is higher than the growth rate of total cash credit granted, which amounted to (13.6%).

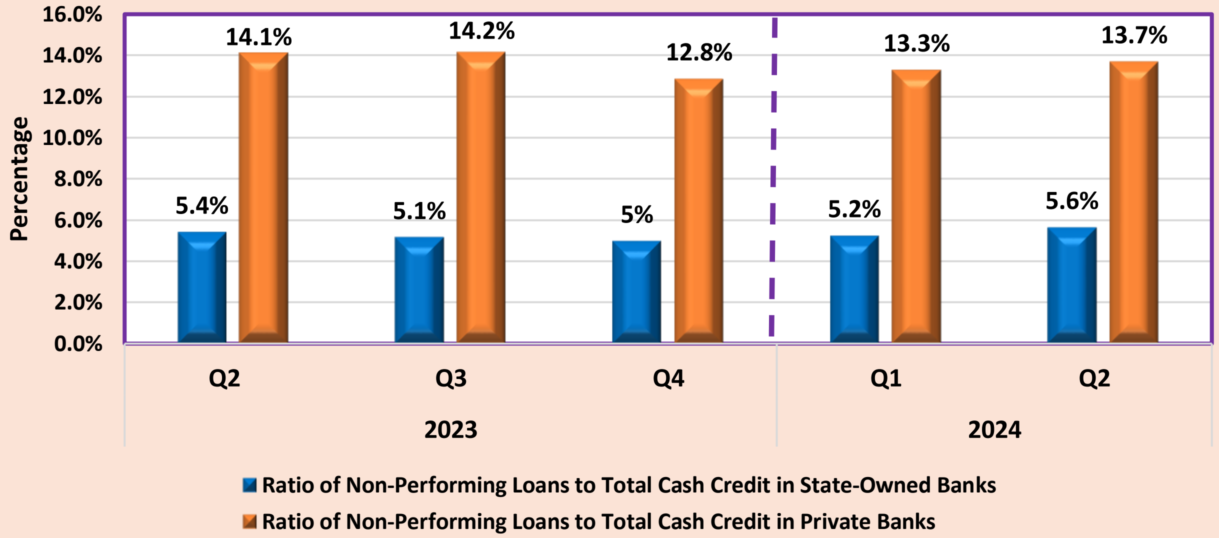
Figure No. (14):
Ratio of Non-Performing Loans to Total Cash Credit



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

When looking at the classification of banks by ownership, we find that the ratio of non-performing loans to total cash credit is higher for private banks compared to state-owned banks. Figure No. (15) shows that the ratio of non-performing loans to total cash credit for private banks decreased to (13.7%) in Q2 of 2024, compared to (14.1%) in the same quarter of 2023, due to the growth of total private credit by (11.4%), which is higher than the increase in non-performing loan increased by (8.2%), and the ratio of provision non-performing loans to private banks to their total non-performing debts reached (75.5%). While for state-owned banks, the ratio of non-performing loans to their total cash credit increased to reach (5.6%) Q2 of 2024, after it was (5.4%) for the same quarter of 2023. While the ratio of the provision for non-performing loans to state-owned banks to total non-performing debts (116.8%) during the same period.

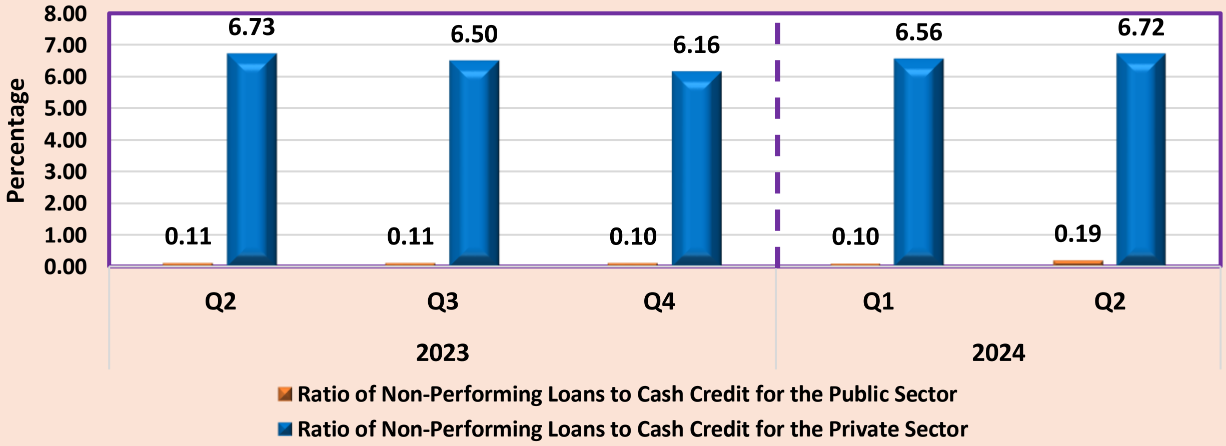
Figure No. (15):
Ratio of Non-Performing Loans to Total Cash Credit in both State-Owned & Private Banks



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

Regarding non-performing loans (NPLs) in both the private and public sectors to total cash credit. It is observed that the NPL ratio for loans in the private sector is higher than in the public sector (6.72%) during Q2 of 2024, while the ratio in the public sector (0.19%) during the same period and Figure No. (16) illustrate this.

Figure No. (16):
Ratio of Non-Performing Loans to Total Cash Credit in the Public and Private Sectors

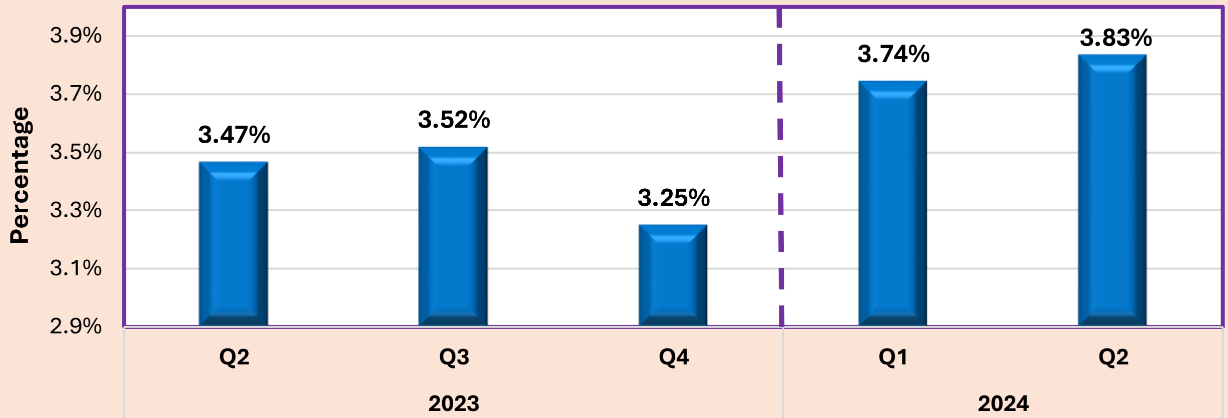


Source: Central Bank of Iraq, Statistics and Research Department, Annual Statistical Bulletin.

9. Non-Performing Loans to Total Deposits:

The index is calculated by dividing non-performing loans by the total deposits of banks. Figure No. (17) shows that the ratio of non-performing loans to total deposits increased to (3.83%) in Q2 of 2024 after being (3.47%) in the same quarter of 2023, this increase is due to the growth of total non-performing loans by (14.8%) which is higher than the growth rate of total deposits at (3.7%).

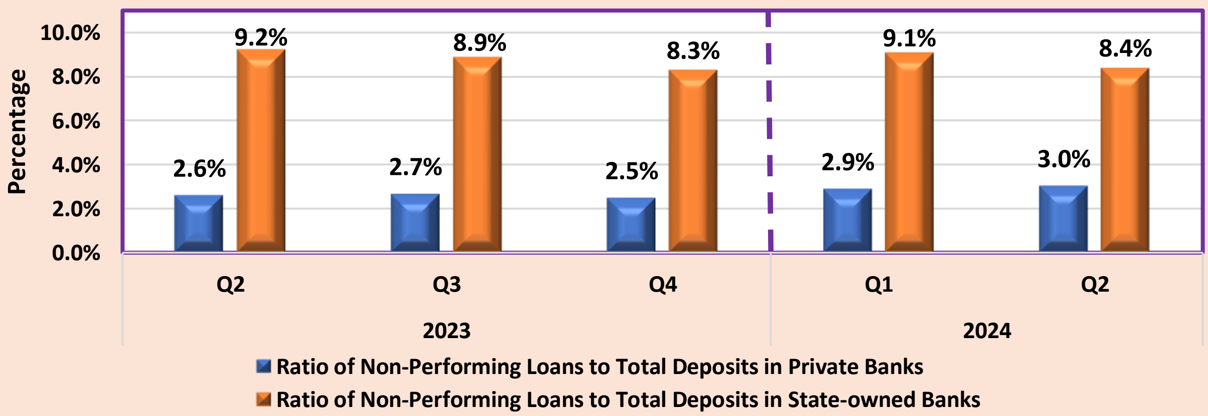
Figure No. (17):
Ratio of Non-Performing Loans to Total Deposits



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

Regarding the classification of banks by ownership, there is a decrease in this ratio for private banks. The ratio of non-performing loans to total deposits for private banks decreased in Q2 of 2024 to (8.4%) after being (9.2%) for the same quarter of 2023. While this ratio increased to (3.0%) for state-owned banks in Q2 of 2024 after being (2.6%) in the same quarter of 2023. This difference between state-owned and private banks is attributed to the increase in volume of deposits in the private banks by (18.9%) compared to an increase in deposits for state-owned banks by (1.6%).

Figure No. (18):
Ratio of Non-Performing Loans to Total Deposits in both State-Owned and Private Banks

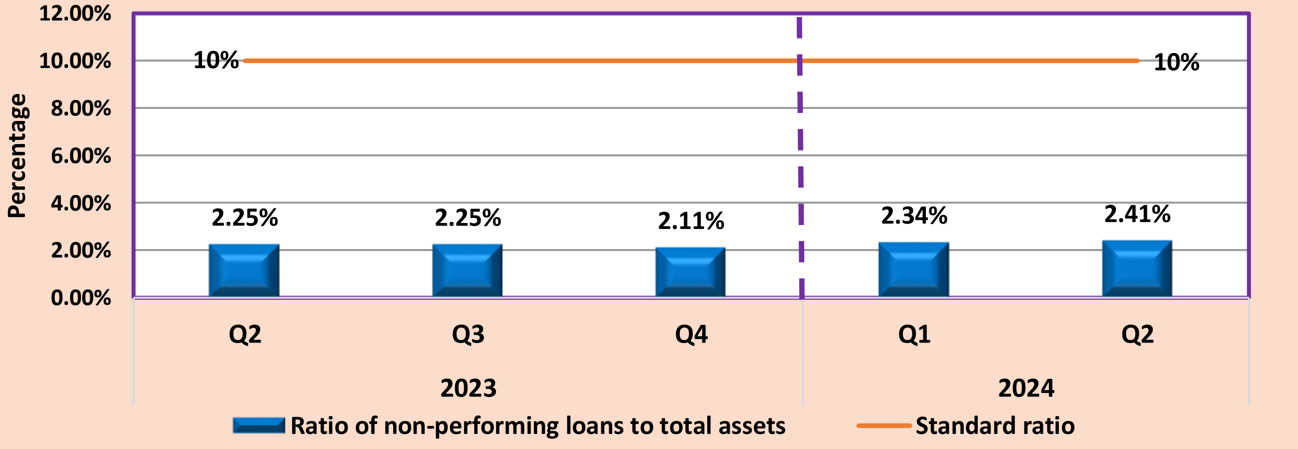


Source: Central Bank of Iraq, Statistics and Research Department, Statistical Website.

10. Non-Performing Loans to Total Assets:

This index is measured by dividing non-performing loans by total assets in banks, and the standard value for this index is (10%). Exceeding the standard value for the ratio of non-performing loans to total assets indicates a significant increase in the volume of non-performing loans [1]. Figure No. (19) shows the ratio of non-performing loans to total assets at banks in Iraq, as a slight increase in this ratio is noted to reach (2.41%) in Q2 of 2024 compared to (2.25%) for the same quarter of 2023. It is worth noting that the ratio of non-performing loans to total assets did not exceed the aforementioned standard ratio, and this is a positive indicator of the banks' ability to confront any potential financial crisis in the coming period.

Figure No. (19):
Ratio of Non-Performing Loans to Total Assets

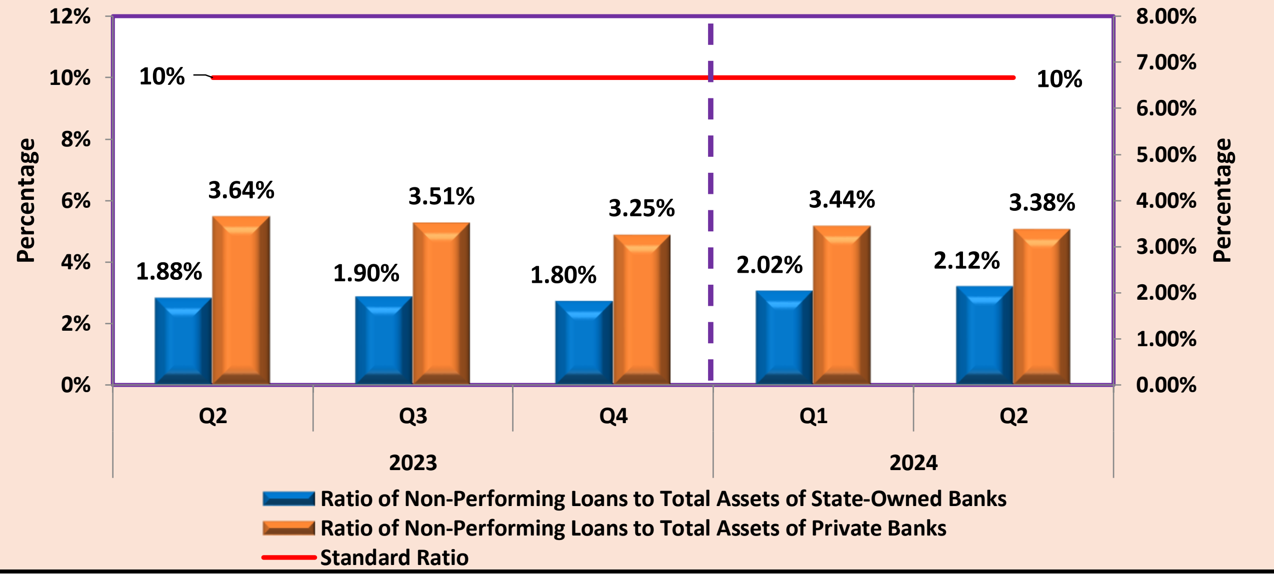


Source: Central Bank of Iraq, Statistics and Research Department, Statistical Website.

Considering the breakdown of banks according to ownership, it could be found that both private banks and state-owned banks did not exceed the aforementioned ratio as shown in Figure No. (20), noting that this percentage is higher for private banks compared to state-owned banks. Since it reached (3.38%) for private banks in Q2 of 2024, while this ratio reached (2.12%) for state-owned banks for the same period. This ratio does not indicate any cause for concern regarding financial stability.

[1] For more, see, CBI 2020, Early Warning Report for the Banking Sector, Issue Thirteen.

Figure No. (20): Ratio of Non-Performing Loans to Total Assets in both State-Owned and Private Banks

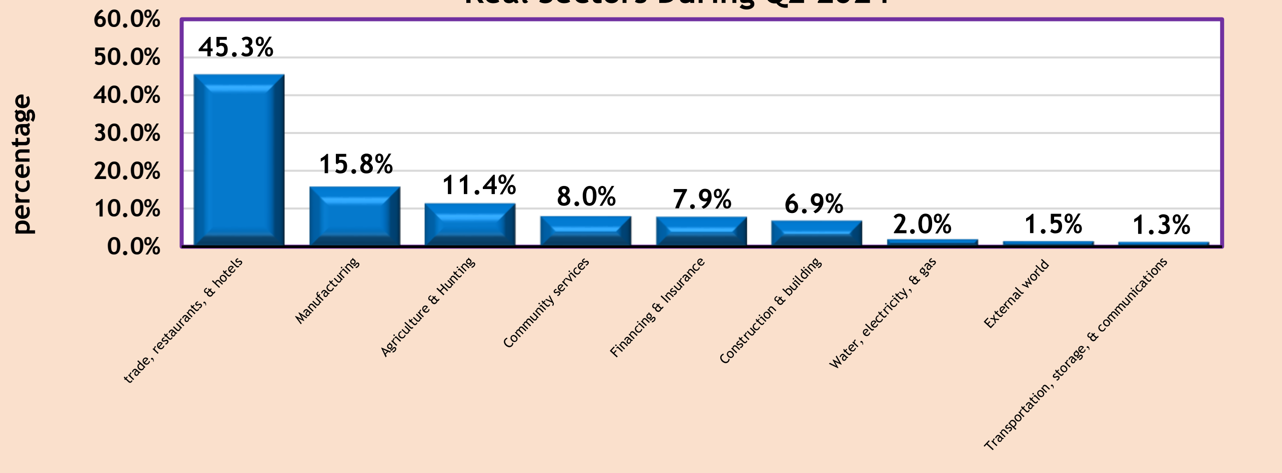


Source: CBI, Statistics and Research Department, Annual Statistical Bulletin.

11. Sectoral Distribution of Non-Performing Loans:

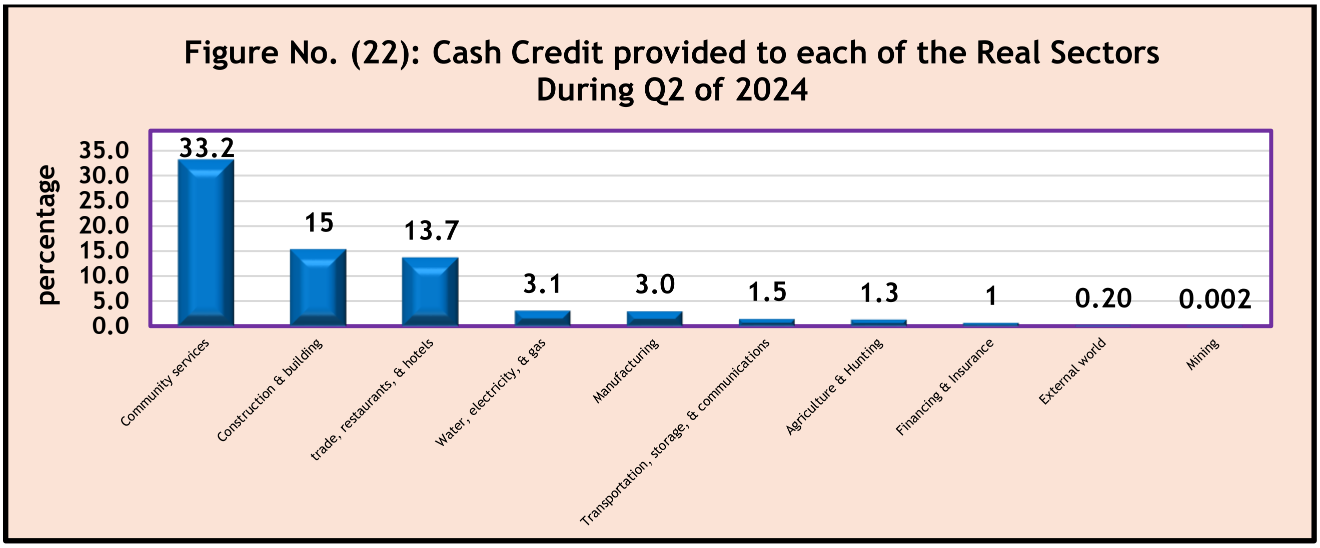
This index shows the sectoral distribution of non-performing loans, and Figure No. (21) shows that the trade, restaurants, and hotels sector recorded the largest percentage of non-performing loans, reaching (45.3%) during Q2 of 2024. This calls for the guarantees required by banks to be more robust to reduce the shocks that this sector may be exposed to if some of the existing projects in it stop due to default in repaying loans. This sector is followed by the manufacturing one, which recorded (15.8%) during the same period. Therefore, it is necessary for banks to be more cautious and careful in granting credit for these two sectors, to avoid faltering their activity and ensure the safety of depositors' funds. It is necessary to develop policies that enable these two sectors to recover and return to a sustainable growth path.

Figure No. (21): Ratio of Non-Performing Loans for Each Sector of Real Sectors During Q2 2024



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

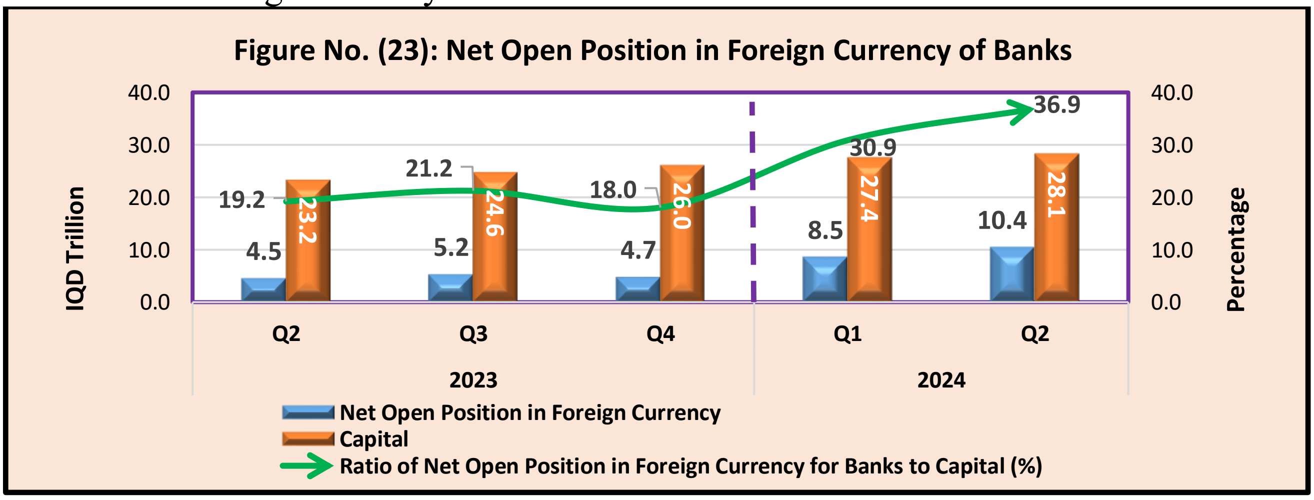
It is worth noting that the trade, restaurants and hotels sector does not represent the largest share of the volume of credit granted within the real sector, but it recorded the largest share of the volume of bad debts. While the community services sector recorded the largest share of cash credit granted to the real sectors at a rate of (46.1%) and an amount of IQD (33.2) trillion, followed by the construction and building sector at a rate of (21.2%), as shown in Figure No. (22).



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

12. Net Open Foreign Currency Position of Banks:

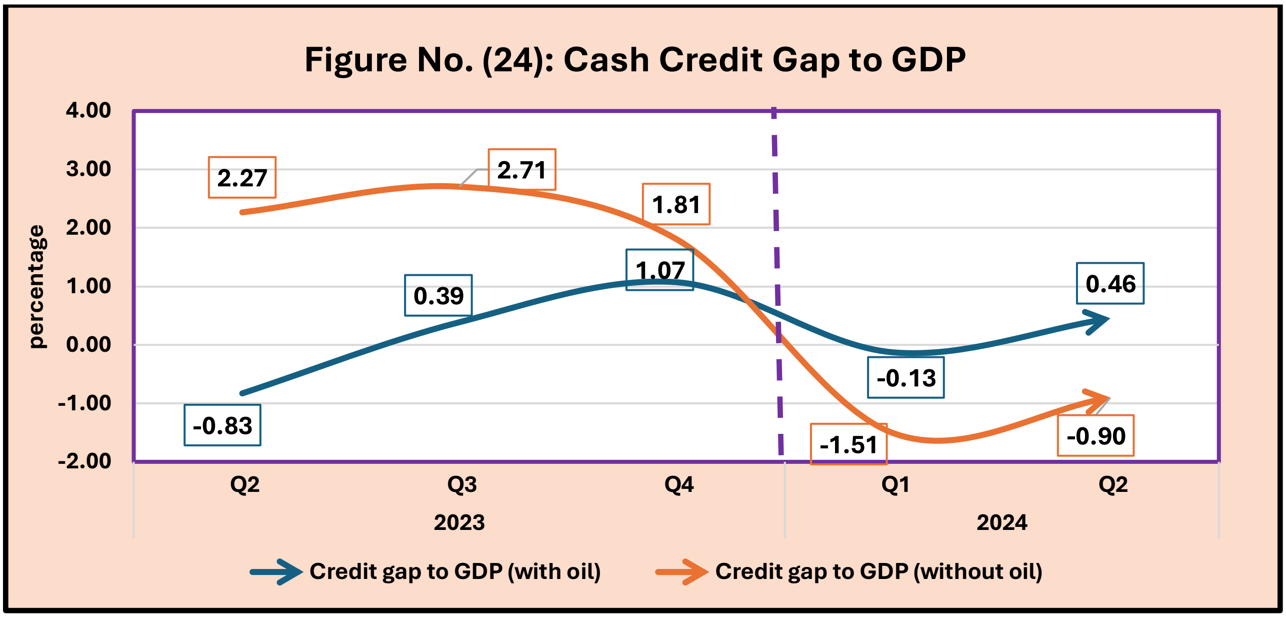
This index measures the net foreign assets of banks by calculating the difference between their foreign assets and foreign liabilities divided by capital. Consequently, a decrease in this ratio means a decrease in the volume of foreign assets of banks or an increase in foreign liabilities, and vice versa. Figure No. (23) shows an increase in the index ratio for banks from (19.2%) in Q2 of 2023 to (36.9%) in the same quarter of 2024, as a result of an increase in net foreign assets by (132.8%) with an increase in capital by (21.2%), which reflects the desire of banks to increase their assets such as deposits and securities in foreign currency.



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

13. Private Sector Cash Credit Gap to GDP:

The credit gap is defined as the ratio of cash credit provided to the private sector to GDP at current prices, minus the general trend of the ratio of credit (directed to the private sector) to GDP [2] at current prices. The standard value of this index ranges from (2.5%) to (10%). As the estimated ratio approaches the standard value, banks must create additional buffers from the capital, known as cyclical buffers, owing to increased credit growth at a higher rate than GDP growth, Figure No. (25) shows the credit gap to GDP with and without oil. This gap without oil reached (- 0.9%) in Q2 of 2024, while the gap when measuring GDP data with oil reached (0.46%) in the same period, thus showing that the two gaps in Q2 of 2024 are lower than the standard ratio, which means that cash credit provided to the private sector can be increased without fear of financial instability.



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

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[2] For more information on how to calculate the output gap, see CBI, Iraq's Early Warning Report No. 18, chap. I, 2020.

Table No. (2): Indices for Analyzing Banks' Performance			
Index name	**Q2 2023**	**Q1 2024**	**Growth Rate %**
Bank deposits to M2 (%)	47.9	47.7	-0.4
Cash in circulation to M2 (%)	52.1	52.3	0.38
Total cash credit to total deposits (%)	50.7	55.5	9.47
Total investment to total assets (%)	14.6	16.9	15.75
Money multiplier	1.14	1.15	0.88
Currency in circulation to current deposits (%)	146.7	144.9	-1.23
Return on property rights (%)	10.7	14.2	32.71
Return on assets (%)	1.4	2.0	42.9
Non-performing loans to total cash credit (%)	6.84	6.94	1.46
Non-performing loans to total deposits (%)	3.5	3.8	8.57
Non-performing loans to total assets (%)	2.25	2.41	7.11
Net open financial position in foreign currency of operating banks (%)	19.2	36.9	92.19

The prepared table was based on the following data:

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

Chapter Three

Analysis of Macroeconomic Performance Indices

Chapter Three: Analysis of Macroeconomic Performance Indices

Macroeconomic variables are among the most significant factors affecting the financial system, as they are affecting the banking sector directly and indirectly, as well as the financial sector. Therefore, The Early Warning Report provides an analysis of the most prominent macroeconomic indices, such as inflation rate and total public debt, together with calculating the GDP implicit deflator, which reflects the limits of production capacities in the Iraqi economy. The report also included the measurement of the GDP gap. The following are the most prominent Macroeconomic indices:

1. Inflation Rate:

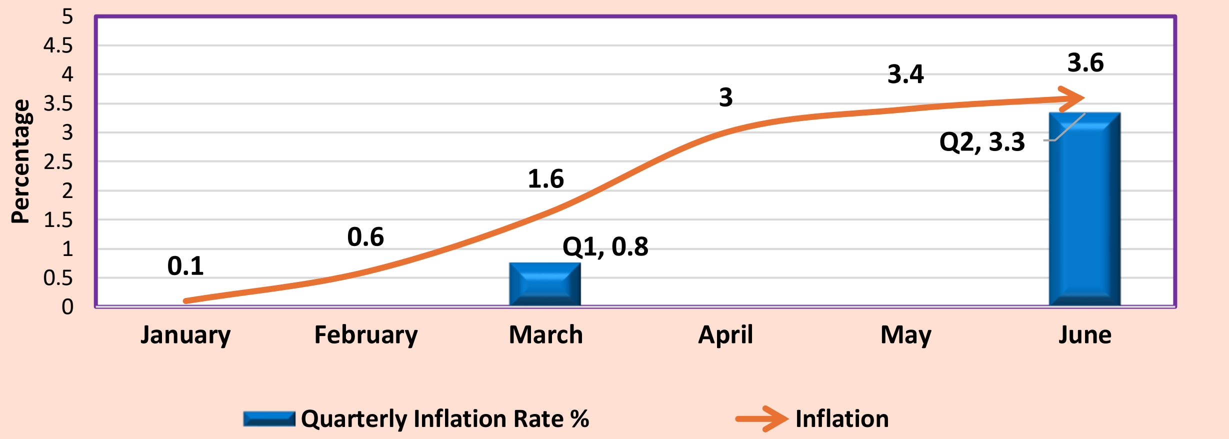
The inflation rate is measured by several indices, but the most important one is the consumer price index (CPI), because it reflects changes in the prices of goods and services that are consumed by individuals whether produced locally or imported. Iraq's inflation rate increased during the Q2 of 2024 to (3.3%) compared to (0.8%) for Q1 of the same year, as the inflation rate for 2024 was calculated by setting 2022 as the base year in calculating the consumer price index instead of 2012 as announced by the Ministry of Planning. The increase was due to the rise of most price indices totals as the following: tobacco, transportation, communications, miscellaneous goods & services, and restaurants categories registered a rise of (6.1%), (2%), (2%), (1.7%), and (1.6%), respectively, as shown in Table No. (3).

Table No. (3): Totals of Goods & Services

Details / Date	Tobacco	Transportation	Communications	Miscellaneous Goods & Services	Restaurants
Q1 2024	116.9	105.9	96.5	109.5	111.2
Q2 2024	124.1	108.1	98.4	111.4	113.0

Source: Central Bank of Iraq, Key Financial Data.

Figure No. (25):
Inflation Rate till Q2 of 2024

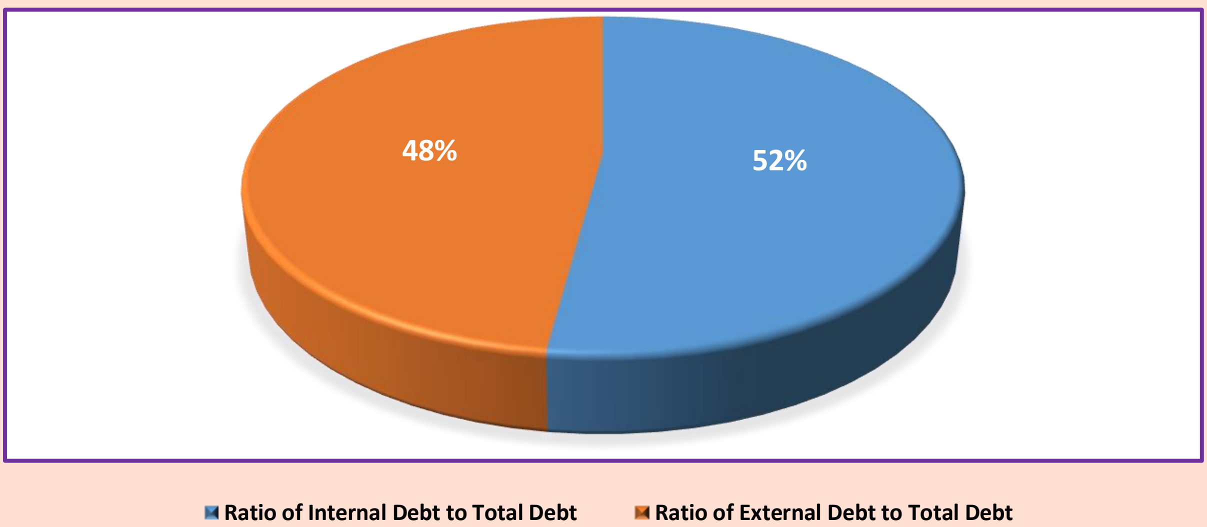


Source: Central Bank of Iraq, Key Financial Data.

2. Growth Rate of Total Public Debt:

Total public debt can be calculated through internal and external debt, which represent the Government's financial obligations, one to the interior of the country and the other to the external world. The growth rate of total debt (internal and external) for Q2 of 2024 increased by (3.7%) compared to the same quarter of 2023, since internal debt increased despite the decline of external debt. Figure No. (27) shows that the external debt ratio was (48%) and the internal debt ratio was (52%) of the total debt for Q2 of 2024.

Figure no. (26):
Ratios of Internal and External Debt to Total Debt for Q2 of 2024



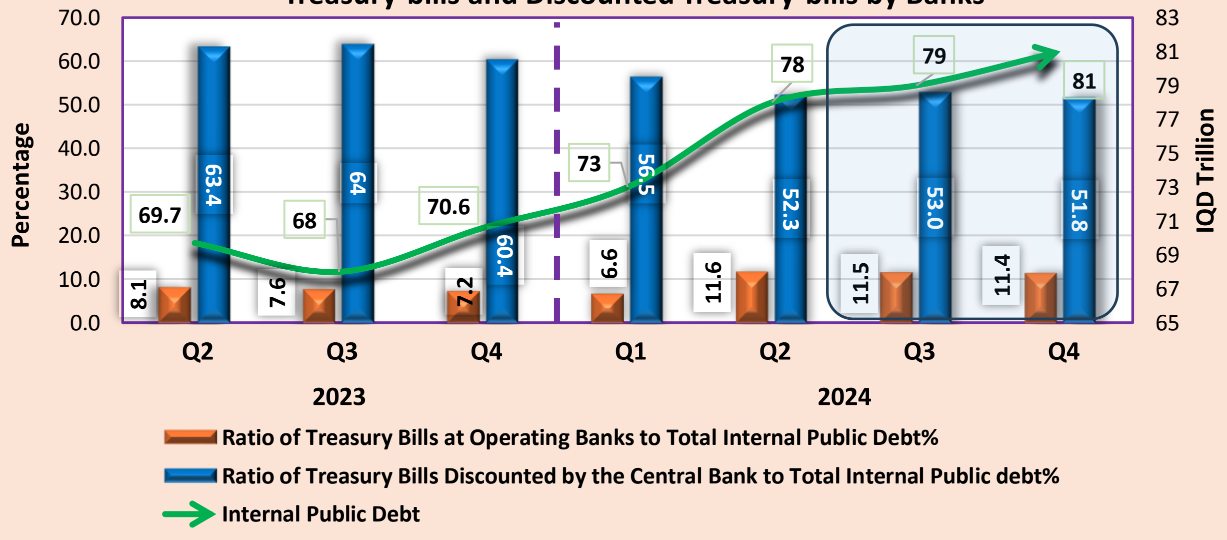
Source: Central Bank of Iraq, Statistics and Research Department.

A. **External Debt Growth Rate**: This indicator shows loans and financial obligations owed by a state to international lenders, such as governments, financial institutions, or foreign investors. The external debt rate decreased by (4%) for Q2 of 2024 compared to the same quarter of 2023. This is a result of the Iraqi government's efforts to avoid burdening the Iraqi economy with external obligations that could hinder national development.

B. **Internal Debt Growth Rate**: This indicator shows the government's commitments to banks and the central bank. Figure No. (28) shows that the ratio of treasury-bills at banks to total internal public debt increased by (11.6%) for Q2 of 2024 from (8.1%) for the same quarter of 2023. This may have a negative impact on the financial system due to the increased crowding out of the private sector in access to finance. As for treasury-bills discounted by the Central Bank of Iraq fto internal public debt, they fell to (52.3%) for Q2 of 2024 from (63.4%) for the same quarter of 2023 due to Government's payment of a part of these transfers and as a result of the issuance of T-bills by the government with an amount of IQD 4.225 trillion to State-owned banks, the internal public debt increased during the Q2 of 2024.

Internal public debt is expected to rise by (16%) and (15%) to reach IQD 79 trillion and IQD 81 trillion, respectively, for Q3 and Q4 of 2024.

Figure No. (27):
Treasury-bills and Discounted Treasury-bills by Banks



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

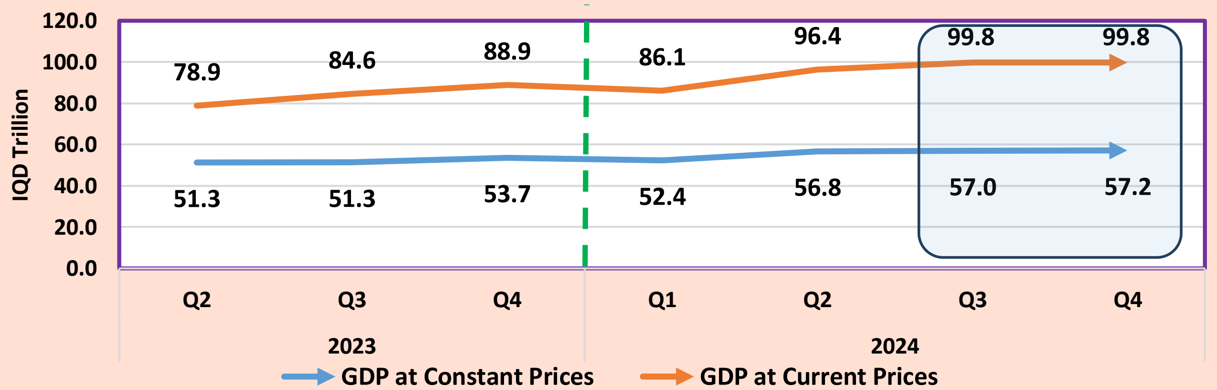
*Data of Q3 and Q4 of 2024 are forecasting data, based on forecasts of Monetary and Financial Stability Division.

3. Gross Domestic Product (GDP) Growth Rate:

Gross Domestic Product (GDP) represents one of the most important economic indices used to assess the volume and growth rate of the economy, reflecting the state's level of economic activity over a specified period of time. GDP at current prices in Iraq increased for Q2 of 2024 by (22.2%) to register IQD (96.4) trillion compared to the same quarter of 2023 reaching IQD (78.9) trillion, owing to high growth rate of most sectors such as (mining & quarries), manufacturing, construction and (electricity & water) by (30%), (74%), (90%), and (47%), respectively, as shown in figure No. (29).

GDP at current prices is expected to rise during Q3 and Q4 of 2024 to reach IQD 99.8 trillion and it is expected to rise at constant prices to IQD 57 trillion and IQD 57.2 trillion, respectively, for Q3 and Q4 of 2024.

Figure No. (28):
GDP Growth Rate at Constant and Current Prices



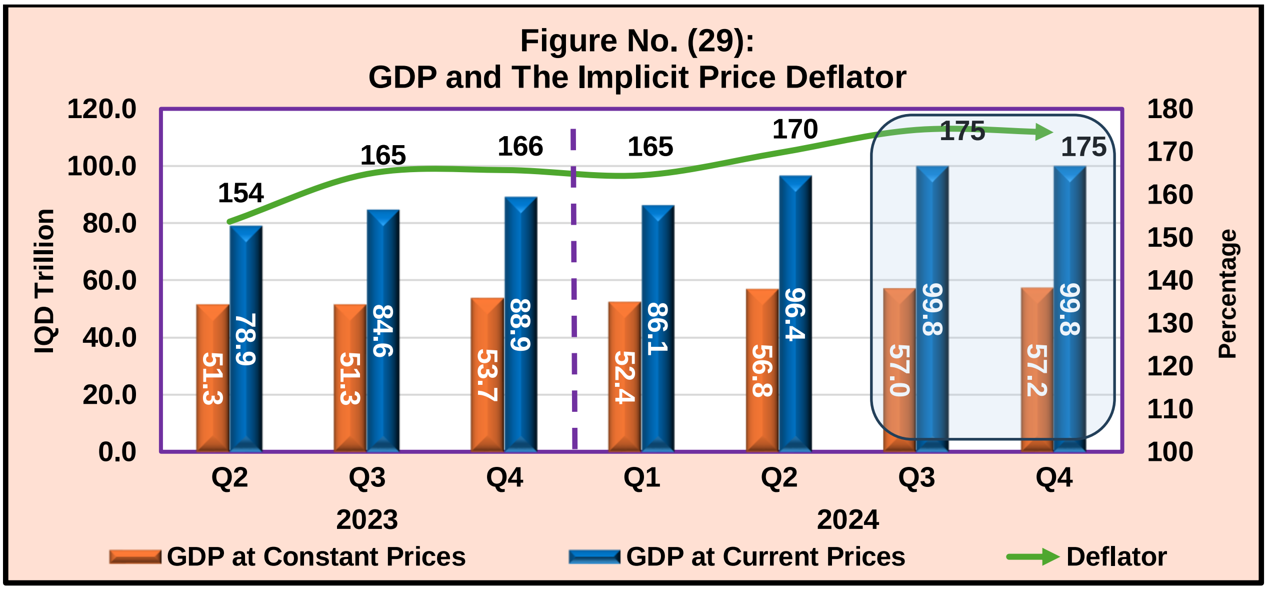
Source: Ministry of Planning, Central Statistical Organization – GDP Data.

*Data of Q3 and Q4 of 2024 are forecasting data, based on the forecasts of Monetary and Financial Stability Division.

4. Implicit Price Deflator:

The Implicit Price Deflator is considered one of the important indices used to measure the inflation rate, since it reflects changes in the prices of all goods and services produced within a country over a specific period of time. It can be calculated by dividing GDP at current prices by GDP at constant prices. A high value of the deflator indicates an increase in the overall price level. Figure No. (30) shows an increase of the implicit deflator value to (170%) for Q2 of 2024, compared to (154%) for the same quarter of 2023 due to positive inflation rates during the same period.

The implicit price deflator is expected to rise to (175%) during Q3 and Q4 of 2024.



Source: Central Bank of Iraq, Statistical Website.

*Data of Q3 and Q4 of 2024 are forecasting data, based on the forecasts of Monetary and Financial Stability Division.

5. GDP Gap

The GDP gap represents the difference between the actual GDP (at constant prices) and potential GDP. A positive gap indicates that the actual GDP is greater than the potential GDP, meaning the economy is operating above its production capacity. A negative gap, on the other hand, suggests that the actual GDP is less than the potential GDP, meaning that the economy is operating below its production capacity. It is accompanied by high unemployment levels and lower-than-potential output, causing deflationary pressures. Figure No. (31) shows that the potential GDP reached IQD 54.3 trillion for Q2 of 2024, while the actual GDP value increased to IQD 56.8 trillion for the same quarter of 2024 compared to IQD 51.3 trillion for the same quarter of 2023, which indicates that the economy is operating at higher than its available potential level and suffers from inflationary pressures.

The actual GDP is expected to increase for Q3 and Q4 of 2024, reaching IQD 57 trillion and IQD 57.2 trillion, respectively, with the rise of potential GDP for Q3 and Q4 of 2024 reaching IQD 54.6 trillion and IQD 54.9 trillion, respectively.

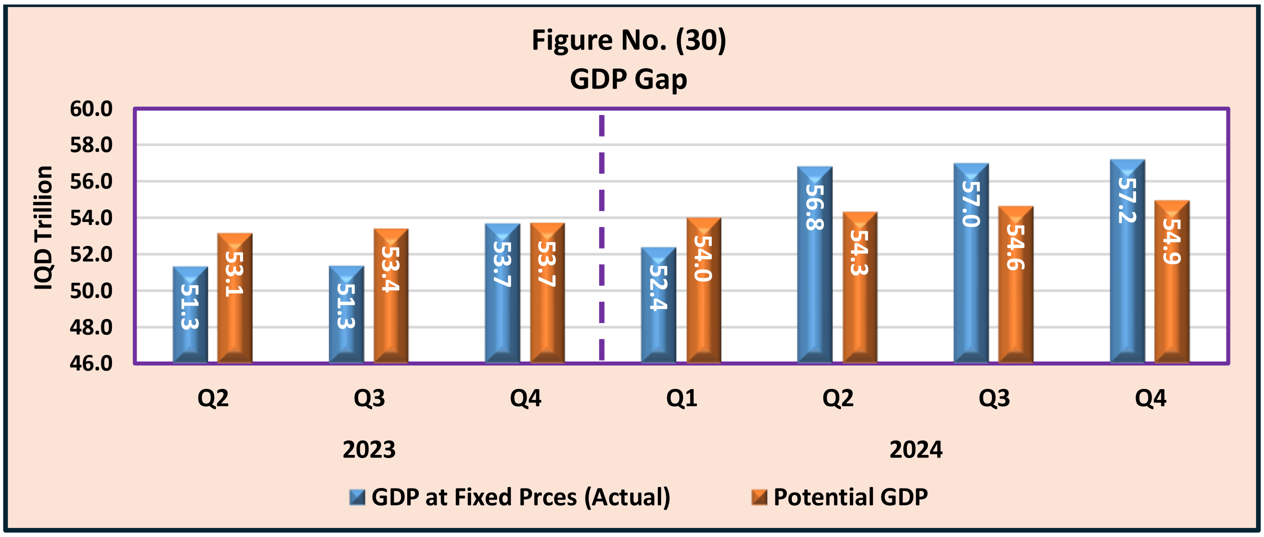


Figure No. (30)
GDP Gap

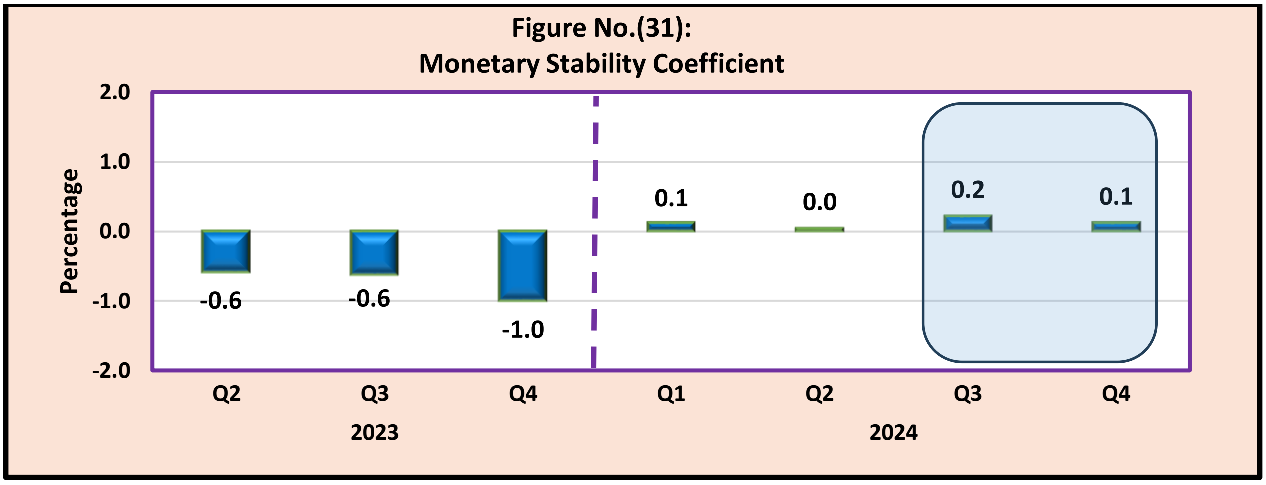
Source: Central Bank of Iraq - Financial and Monetary Stability Division estimates according to data of the Ministry of Planning - Central Statistical Organization.

*Data of Q3 and Q4 of 2024 are forecasting data, based on the forecasts of Monetary and Financial Stability Division.

6. Monetary Stability Coefficient:

The monetary stability coefficient indicates the balance between monetary and commodity blocs in the economy. It is calculated by dividing the growth rate of broad money supply (M2) by the growth rate of GDP at current prices. Monetary stability is achieved when the value of this coefficient equals one. If the value is greater than one, it indicates an increase of the money supply over the commodity supply, which will affect the economy's balance. But if its value is less than one, it indicates that the economy needs to increase the money supply to achieve balance. Figure No. (32) illustrates the changes in the value of this index; it recorded a value of (0.03) for Q2 of 2024, while it recorded (-0.6) for the same quarter of 2023. This decrease is due to a decline of the quarterly growth rate of M2 to (0.8%) for Q2 of 2024, as well as the rise in the nominal GDP growth rate to reach (22.2%) during the same period, meaning that the growth of broad money supply is not compatible with the growth of GDP at current prices.

The monetary stability coefficient for Q3 and Q4 of 2024 is expected to be (0.2%) and (0.1%) respectively.



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

*Data of Q3 and Q4 of 2024 are forecasting data, based on the forecasts of Monetary and Financial Stability Division.

Table No. (4): Macroeconomic Performance Indices			
Index	**Q2 2023**	**Q2 2024**	**Change Rate %**
Inflation Rate (%)	3.6	3.3	-8.3
Ratio of Treasury-bills at Banks to Total Internal Public Debt (%)	8.1	11.6	43.2
Ratio of Treasury-bills Discounted by the Central Bank to Total Internal Public Debt (%)	63.4	52.3	-17.5
GDP at Current Prices (IQD trillion)	78.9	96.4	22.2
GDP at Constant Prices (IQD trillion)	51.3	56.8	10.7
GDP Implicit Price Deflator	154	170	10.4
GDP Gap (IQD trillion)	1.8	-2.5	-238.8
Monetary Stability Coefficient	-0.6	0.03	105

Source:

- Central Bank of Iraq, Statistics and Research Department.
- Ministry of Planning, Central Statistical Organization - GDP data.

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