

<https://doi.org/10.36719/2706-6185/42/62-66>

Mehrab Karimli

Azerbaijan State University of Economics

Ph. D. student

mehrabkerimli96@gmail.com

<https://orcid.org/0009-0008-8229-4247>

Analyze of Profitability in Azerbaijan Banking Sector: A Study on Kapital Bank and Pasha Bank

Abstract

In modern times, the banking sector plays a major role in people's daily lives, in the activities of enterprises and in the economy. Especially in recent years, with the rapid development of technology and the expansion of the fields of activity of banks, the importance of banks has increased even more. As is known, the main goal of banks is to generate income from the services they provide and their activities. However, like all companies, banks also face or may face many types of risks in their activities and there are many other factors that affect their activities. Banks must take measures to prevent these risks and make decisions regarding factors that may affect their activities. One of these is decisions regarding capital structure. Capital structure has a significant impact on the profitability of the bank. This study first provides information about the capital structure in general, factors affecting the capital structure and decisions regarding capital structure. Then, a study was conducted on Kapital Bank and Pasha Bank regarding return on assets (ROA) and return on equity (ROE).

Keywords: banks, profitability, assets, equity, capital structure

Mehrab Kərimli

Azərbaycan Dövlət İqtisad Universiteti

doktorant

mehrabkerimli96@gmail.com

<https://orcid.org/0009-0008-8229-4247>

Azərbaycan bank sektorunda gəlirliliyin təhlili: Kapital Bank və Paşa Bank üzərində araşdırma

Xülasə

Müasir dövrdə bank sektoru insanların gündəlik həyatında, müəssisələrin fəaliyyətində və iqtisadiyyatda böyük rola malikdir. Xüsusən son illərdə texnologiyanın sürətli inkişafı, bankların fəaliyyət sahələrinin genişlənməsi ilə bankların əhəmiyyəti daha da artmışdır. Məlum olduğu kimi, bankların əsas məqsədi göstərdikləri xidmətlərdən, fəaliyyətdən gəlir əldə etməkdir. Lakin bütün şirkətlər kimi bankların da fəaliyyətlərində qarşılaşdıqları və ya qarşılaşa biləcəkləri bir çox risk növləri var və fəaliyyətinə təsir edən bir çox digər amillər mövcuddur. Banklar bu risklərin qarşısının alınması üçün tədbirlər görməli və onların fəaliyyətinə təsir edə biləcək amillərlə bağlı qərarlar qəbul etməlidirlər. Bunlardan biri də kapital strukturu ilə bağlı qərarlardır. Kapital strukturu bankın gəlirliliyi üzərində əhəmiyyətli təsirə malikdir. Bu araşdırmada ilk növbədə ümumilikdə kapital strukturu, kapitalın strukturuna təsir edən amillər və kapital strukturu ilə bağlı qərarlar haqqında məlumat verilmişdir. Daha sonra Kapital Bank və Paşa Bank üzərində aktivlərin gəlirliliyi (ROA) və kapitalın gəlirliliyi (ROE) ilə bağlı araşdırma aparılmışdır.

Açar sözlər: banklar, gəlirlilik, aktivlər, kapital, kapital strukturu

Introduction

The basic function of banks is to act as a bridge between individuals and institutions with excess funds in an economy and individuals and institutions in need of funds. Banks, which are one of the important elements of monetary and credit policy in the economy, aim to maximize profits while fulfilling the function of transferring resources from units with financing capacity to units with financing deficits. In order to maintain their profitability, banks need to operate more efficiently with a wider range of products in the face of pressures and risks brought about by certain factors such as technological developments, globalization, state intervention and capital adequacy. Especially as a result of globalization, the operation of foreign banks in domestic markets has increased competition between banks and narrowed profit margins (Gülhan & Uzunlar, 2011).

Capital structure decisions of banks play a significant role in the stability of the banking system, risk management and supporting economic growth. With the increasing globalization of financial markets, banks with international mandates face unique challenges as well as opportunities in determining optimal capital structures. Understanding the determinants of capital structure for such banks is important not only for academic discussions but also for policy makers and industry practitioners seeking to enhance the resilience and efficiency of banking systems and operations (Obi & Ebiringa, 2024).

To maximize the value of the firm, the cost of capital structure should be minimized. At this point, the optimum capital structure is achieved. The optimum capital structure is the capital structure (combination of debt and equity) that leads to the maximum value of the firm. The optimum capital structure is the capital structure where the Weighted Average Cost of Capital (WACC) is minimum and the value of the firm is maximum (Toader, Vintila, & Gherghina, 2022). Deciding on the appropriate capital structure, especially for banks, is a critical decision that the financial managers of the firm must make effectively because it is closely related to the value of the firm (Awah, Ebiringa, & Ugwu, 2020).

Research

There have been numerous studies conducted on the factors affecting capital structure and decisions regarding capital structure. As a result of the studies conducted, the factors that affect capital structure the most are generally divided into two as dependent and independent variables. Dependent variables include leverage ratios of firms. Independent variables include factors such as profitability and growth rates, size of the firm, tax shield and tax level (Central Bank of the Republic of Azerbaijan).

The profitability indicators of companies are generally divided into two as profitability of assets and profitability of equity. Profitability of assets shows how efficiently the company uses its assets to make a profit. This ratio is calculated by dividing the net profit of the period by the assets. In other words, profitability of assets refers to the profit the company makes per asset. Profitability of equity is the ratio that shows how efficiently the investments made by the partners and shareholders in the company are used. This ratio expresses how much profit the company makes in relation to its equity (Albayrak & Akbulut, 2008).

In the literature, the return on assets is known as ROA (return on assets) and the return on equity is known as ROE (return on equity). We can explain how these values are calculated as follows:

$$\text{ROA} = \text{Net profit} / \text{Total assets}$$

$$\text{ROE} = \text{Net profit} / \text{Total equity}$$

As part of this study, a study was conducted on Kapital Bank and Pasha Bank. The tables below show the return on assets and return on equity ratios of Kapital Bank and Pasha Bank.

Table 1
 Profitability of assets of Kapital Bank

Years	Net profit	Total assets	Return on assets
2019	134,708.00	4,143,322.00	3 %
2020	302,698.00	5,227,472.00	6 %
2021	179,963.00	6,709,523.00	3 %
2022	308,047.00	7,822,172.00	4 %
2023	242,209.00	8,659,618.00	3 %

Source: Prepared by the author based on the financial statements of Kapital Bank

This table reflects the profitability of Kapital Bank's assets in 2019-2023. Based on the table, it can be said that the bank's profitability ratio on assets has remained largely stable over the past 5 years. The highest indicator of this ratio was recorded in 2020 (6 %).

Table 2
 Profitability of equity of Kapital Bank

Years	Net profit	Total equity	Return on equity
2019	134,708.00	425,054.00	32 %
2020	302,698.00	634,195.00	48 %
2021	179,963.00	648,196.00	28 %
2022	308,047.00	824,654.00	37 %
2023	242,209.00	911,289.00	27 %

Source: Prepared by the author based on the financial statements of Kapital Bank

This table reflects the return on equity indicators of Kapital Bank in 2019-2023. According to the table, it can be seen that the bank's return on equity ratio is quite high and has changed to some extent over the years. The highest rate of return on equity in the bank in the last 5 years was recorded in 2020 (48 %) (Pasha Bank's financial statements).

Table 3
 Profitability of assets of Pasha Bank

Years	Net profit	Total assets	Return on assets
2019	65,040.00	4,767,450.00	1 %
2020	84,252.00	5,513,021.00	2 %
2021	90,180.00	6,408,381.00	1 %
2022	149,394.00	8,519,814.00	2 %
2023	199,209.00	8,651,371.00	2 %

Source: Prepared by the author based on the financial statements of Pasha Bank.

This table shows Pasha Bank's return on assets for the period 2019-2023. As can be seen, Pasha Bank's return on assets has remained largely stable over the last 5 years (Kapital Bank's financial statements).

Table 4
Profitability of equity of Pasha Bank

Years	Net profit	Total equity	Return on equity
2019	65,040.00	475,768.00	14 %
2020	84,252.00	541,145.00	16 %
2021	90,180.00	577,276.00	16 %
2022	149,394.00	662,997.00	23 %
2023	199,209.00	837,192.00	24 %

Source: Prepared by the author based on the financial statements of Pasha Bank.

This table also reflects the return on equity indicators of Pasha Bank in 2019-2023. We can say that the bank's return on equity indicators are also largely stable. In the last 5 years, the highest return on equity indicator of Pasha Bank was recorded in 2023 with 24 % (Tunay & Silpar, 2006).

Conclusion

Currently, the importance of the role that banks play in people's lives and the economy is increasing day by day. Like other commercial institutions, the goal of banks is to generate income. There are many factors that affect the profitability and effectiveness of banks' activities. In order to continue their activities for a long time, banks must analyze the risks they may encounter and make effective decisions on important issues. One of the most important decisions that banks have to make during their activities is decisions related to capital structure. There are also certain factors that affect capital structure and capital structure decisions. One of the most important of which is the profitability of assets and the profitability of capital.

This study analyzed the profitability of assets and capital of Kapital Bank and Pasha Bank, which are the largest and leading banks in the Azerbaijani banking sector. As part of the study, the profitability of assets and the profitability of capital ratios of the banks in question were calculated for the period 2019-2023.

As can be seen from the tables, the profitability of assets ratio in both banks has been positive and has remained largely stable over the last five years. It is observed that this ratio is slightly higher in Kapital Bank than in Pasha Bank. Thus, the return on assets in Pasha Bank was 1 % in 2019 and 2021 and approximately 2 % in the other years. The highest indicator in Kapital Bank was recorded in 2020 (6 %).

The return on capital ratios are also quite high in both banks. We can see that this indicator is also higher in Kapital Bank than in Pasha Bank. The highest indicator of the return on capital ratio in Kapital Bank was recorded in 2020 (48 %), and in Pasha Bank in 2023 (24 %).

Return on assets (ROA) and return on equity (ROE) show how effectively the bank uses its assets and capital, how much profit it makes in relation to each asset and capital it owns. According to the results of the study, it is observed that the return on assets and return on capital in Kapital Bank are also higher compared to Pasha Bank. However, in general, the ratios in question in both banks are at a fairly good level. This is an indicator of the effective use of the banks' assets and capital, the proper organization of the capital structure, and the financial stability of the banks.

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Received: 23.09.2024

Revised: 09.10.2024

Accepted: 10.12.2024

Published: 30.12.2024