

AZERBAIJAN

PART THREE

Monday, August 27, 2007

BANKING SECTOR

Petrodollars fuel financial world

Liquidity is not a problem in Azerbaijan. In 2007, the economy will grow at a galloping rate of 29.2 percent, according to an IMF projection. High oil prices are turning the gears of this Caspian Sea republic of 8.1 million people. Pipeline infrastructure, both for crude oil and natural gas, will net \$140 billion in revenue over 20 years, according to President Ilham Aliyev. As the Oil Fund captures petrodollars, the banking sector is busy creating multiplier effects.

"Frankly, our need for equity is not high. Our aim is to facilitate better access to international capital markets for our banks," says Elman Rustamov, Chairman of the National Bank of Azerbaijan (NBA, the central bank). The New Man-



ELMAN RUSTAMOV
Chairman of the
National Bank of
Azerbaijan

at, Azerbaijan's re-denominated currency, now circulates in 95% of the country. Designed by Robert Corino, who also signed off on the euro, its aesthetics have anchored the country in the global context. Now, tighter monetary policy at the NBA will pave the way for competitiveness of the non-oil sector.

Meanwhile, Rustamov is happy to see the number of banks drop from a peak of 253 to 44. Technical assistance by the EBRD and World Bank have proven key in mergers, as well as in implementing good corporate governance. "After the oil sector, banking is the second-fastest growing part of the economy. Assets, deposits and credits in the banking sector have attained a level of 50 percent [of GDP]. This is a logical result of all the efforts:



Oil revenues flow into Baku banks as sector matures in world's fastest-growing economy

liberalization, consolidation, institutional development and the establishment of a legislative framework," says Rustamov.

Foreign capital is now present in 19 Azeri banks. As in Russia, private bankers are conscious the oil bonanza offers a unique time window. Since 1995, the Azerbaijan Banks Association (ABA) has enhanced the com-

petitive framework by driving reforms. In 2000, ABA set up a banking training center with EU backing. The program has infused new life into the financial system with market research and strategic planning. "More opportunities in the financial sector will arise when Azerbaijan joins the WTO," says Eldar Ismayilov, the ABA president.

The extraordinary boom in Azerbaijan requires sound management. For the banking sector, this means allocating resources to value-creating companies. The European Bank for Reconstruction and Development (EBRD) plays an enabler role by helping to build institutions and making loans of up to \$6.9 million available to SMEs. It has also proven key in minimizing risk for budding companies in the non-oil sector.

"Azerbaijan is officially the

EBRD: less risk in non-oil

fastest-growing economy in the world. At the EBRD, we have played an important role in developing the oil and gas industry. Now that revenue is flowing, we're focused on non-oil projects," says Aygen Yayikoglu, head officer of the EBRD in Baku. There are three areas that the EBRD has staked out as its mission in Azerbaijan: SME promotion, banking and infrastructure.

"We're working together with nine banks, and we are shareholders in four of them," says Yayikoglu, who is instrumental in designing new products for trade finance and leasing. The EBRD also acts as a lending institution to local entrepreneurs. As an example, Yayikoglu cites Garadagh Cement, the largest cement-maker in south Caucasus, which is co-owned by Switzerland's Holcim. "Our third

pillar is infrastructure financing," says Yayikoglu. By paying for roads and railways, the EBRD hopes to have a direct impact on the private sector. After all, Azerbaijan will not be able to diversify its economy as long as infrastructure deficits remain in place.

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AZERBAIJAN

Rebranding is trend for new banking sector

Kapital Bank leads the way as Azerbaijan's savvy, newly-strengthened banking sector works to project a fresh image that more accurately reflects its durability, force and modernization after more than five years of tough consolidation and sector reform

Starting in 2000, Azeri banks began to climb up the value ladder. The central bank had implemented wide-ranging reforms that effectively shut down under-capitalized institutions. In the consolidation process, asset portfolios at banks were shifted and poor performers merged with more adaptive players. Only 44 entities survived. Today, robust oil prices underlie the stability of the Azerbaijan's financial system. But quality and reliability are the new hallmarks of financial intermediaries. To prove that

times have changed, many of them are busy remaking their image.

"We've successfully implemented a rebranding campaign, preserving what was positive historically while giving new meaning to the bank as a modern institution," says Rauf Rzayev, Chairman of the Board at Kapital Bank. His institution is the result of a merger that took place after 133 years



RAUF RZAYEV
Chairman of the Board
at Kapital Bank

of activity. A new management team took over in 2004. According to Rzayev, there was no business plan or credit ratings to speak of—and the balance sheet was unimpressive. Still, international financial groups began opening credit lines based on the country's growth

projections. This allowed Kapital Bank to finance projects in telecommunications, transportation, construction, pharmaceuticals and natural gas.

"By mid-2007, the number of blue-chip clients had grown to 450," says Rzayev, adding, "Of course, our ultimate goal is to

"We've successfully implemented a rebranding campaign, preserving the positive meaning as a modern institution"

Azerbaijan. It is a state-owned bank with a mandate to foster economic development. But this does not preclude netting profits. Revenue grew 122 percent in 2005 to \$3.4 million while total assets climbed 60 percent to \$107.3 million.

Now Kapital Bank has decided to move into an ultramodern office building in Baku. "Today, the bank needs a new face that will convey the message that we are a modern financial institution with best international practices," says Rzayev.

SME portfolio pays off

Efficiency measures have opened the gates to private players like Technikabank. An open joint-stock company, Technikabank was founded in 1993 during one of Azerbaijan's worst years of economic contraction. It diversified its credit portfolio early on, finding market niches in SMEs and up-and-coming telecoms that had been turned down by larger institutions.

Today, Technikabank's corporate profile includes 5,000 companies and 20,000 private depositors. In first quarter 2006, the bank posted 10 percent growth in assets, totaling \$76.7 million. By January 2007, the number had grown to \$154.6 million.

"The bank grew 109 percent last year as a result of the proper legal framework. The reforms enacted by President Ilham Aliyev have affected all sectors of the economy," comments Etibar Aliyev, Chairman of the Supervisory Board. With the economy expected to continue to boom through 2010, interaction with foreign financial institutions such as the EBRD, the IFC and the Asian Development Bank will give Technikabank an additional edge.

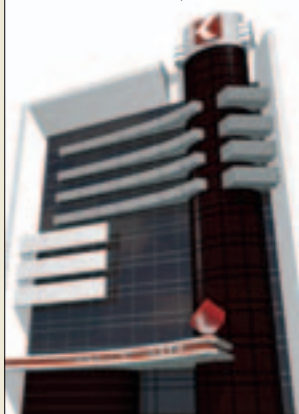
ETIBAR M. ALIYEV
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AZERBAIJAN

IBA: first in line

National leaders in providing credit to boost non-oil sectors such as agriculture, the International Bank of Azerbaijan is backing the diversification of the country's economy

Jahangir Hajiyev, Chairman of the Board at the International Bank of Azerbaijan (IBA), is somewhat of a visionary. He speaks of capital inflows as a source of risk and of making inroads into unknown markets. A few years ago, he devised a plastic card for the Pension Fund of Azerbaijan. Retirees were told they could collect benefits by swiping their cards at an ATM. While only 450,000 signed up the first year, today the word has spread, and the card-holding population is in the millions.



JAHANGIR F. HAJIYEV
Chairman of the
Board of IBA

As with the plastic cards, IBA has a number of all-time firsts in Azerbaijan. It was the first Azeri bank to receive ratings from international credit agencies. It was also the first to raise capital in international financial markets. The credit lines that IBA opened now underlie 50 percent of assets of Azerbaijan's banking system. In

addition, IBA is number one when it comes to private deposits. According to IBA officials, overall assets exceeded \$2.1 billion in the first quarter of 2007. Net profits over the same period amounted to \$15.6 million.

"We were the first bank to obtain a credit line from the Export-Import Bank of the United States without any sovereign guarantees. It was purely based on the relationship between our institutions," says Hajiyev. The loan was worth \$20 million over a 10-year period. Hajiyev has obtained

similar deals with France's COFACE, Germany's HERMES and the Export-Import Bank of Italy. "They've all taken into account our reputation as a reliable bank," says Hajiyev. The latest syndicated loan is worth \$130 million and is sourced from 26 banks in 12 different countries.

As a national development



Innovation has long been a tradition at the International Bank of Azerbaijan

bank, IBA is unlike any other financial intermediary. It has been ahead of competitors in re-routing petrodollars to the non-oil sector. In a country in which 50 percent of the population is rural, agribusiness could be an economic runner-up after oil & gas. IBA has facilitated contacts between local entrepreneurs and US-based outfits specialized in farm machinery, which is how Nebraska-based Valmont Tubing came to furnish irrigation equipment for the local cotton industry. Cotton in Azerbaijan is considered a strategic sector, offering long-term revenue and new jobs. "The next step is the development of a tobacco industry, from seeding to re-drying, thrashing and blending—all the way to the end product," says Hajiyev.

Euromoney named IBA the 'Best Bank in Azerbaijan' from 1997 to 2004. Global Finance Magazine has named it the 'Best Emerging Market Bank' in the Caucasus Region. From his Nizami Street headquarters in Baku, Hajiyev refuses to take credit. Instead, he gives it completely to the bank's 1,314 employees, whom, he says, have ultimately been responsible for protecting the shareholders' best interests and furthering Azerbaijan's economic diversification. "We are very glad when we receive international recognition. But behind all these awards there is the day-to-day work of an entire institution, which is what makes IBA such a successful bank," says Hajiyev.

IBA branches out in region

To prove its name, the International Bank of Azerbaijan (IBA) decided to venture beyond national borders six years ago. Its presence is especially strong in the Russian Federation. According to a July press release, IBA will soon be ranked among the top 250 banks in Russia by assets. In the second quarter of 2007, capitalization at IBA's Moscow office amounted to \$28.12 million. In 2008, a new IBA branch will open in the industrial city

of Nizhny Novgorod, which accounts for 25 percent of trade turnover between Russia and Azerbaijan. It also has a presence in cities like St. Petersburg and Yekaterinburg.

"We have representative offices in London and Frankfurt, and are also planning to open one in New York," says Jahangir Hajiyev, IBA chairman. "Our main task is to develop our institution as a universal bank that can offer all kinds of banking services to our customers."

In light of the digital revolution, the geographic location of a bank is not as relevant as it used to be. What's really important are the services...

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The International Bank of Azerbaijan



IBA is the strongest bank in the Caucasus region according to independent international rating agencies.

IBA possesses over half of the aggregate bank assets on the local market, which comprises 10% of the national GDP, 26.3% of the total banking system's share capital, 56.1% of total deposits, 47.3% of loans and 60% of plastic card issuance.

IBA owns the widest service network in Azerbaijan consisting of 36 branches, over 100 sub-branches, a network of 520 ATMs and 1500 POS-terminals.

IBA owns the following subsidiaries:

- IBA Moscow, LLC, the only Azerbaijani bank in the Russian Federation
- IBA Georgia, LLC, a subsidiary bank
- The International Insurance Company, which possesses the largest statutory capital among insurance companies in Azerbaijan
- AzeriCard, the country's largest card processing company
- Azerileasing Company
- IBA maintains representative offices in Frankfurt-am-Mein and London