CHAPTER 13

MONETARY AND BANKING POLICY AND PERFORMANCE

Key Aspects of Monetary Policy Approved for 2017/18

The realization of a single-digit rate of inflation at 9.0 percent in 2016/17 after 26 years entailed a revised framework and reform in banking deposit rates, aimed at rationalizing the financing costs of production. Hence, a new approach was adopted by the CBI for 2017/18 regarding the rules on determination of deposit rates, with the aim of reducing unsound competition among banks and credit institutions as well as lowering liquidity pressures on the banking system. To this end, the CBI initiated preparations for the proper implementation of deposit rate reductions by taking measures in terminating the operations of unlicensed credit institutions, intervening in the rial interbank market, making the necessary arrangements with the Ministry of Economic Affairs and Finance for transfer of transactions of government bonds (Treasury Bills) in the secondary market to the capital market, altering the share of CDs and bank deposits in the total assets held by fixed-income mutual funds, and concurring with automakers on setting profit rates on car sales based on joint contracts.

Upon setting the necessary grounds, the CBI communicated Circular No. 96/173793 dated August 27, 2017, containing eight paragraphs, to the banking system, to be in effect as of one week later on September 2. The objective was to regulate the deposit rates in the money market and to reduce the mobilization costs of banking resources, which could in turn lead to a decline in financing costs of the economy. In line with the mentioned objectives and emphasizing the provisional nature of deposit rates on the date of the conclusion of contract with clients as per the prior approvals by the MCC (ratified through its 1220th Meeting on June 28, 2016), the CBI determined the provisional profit rate of one-year deposits at a maximum of 15 percent and that of the ordinary short-term deposits on a daily basis at 10 percent at most.

Prior to the implementation of the above policy, which required the banks to observe the stipulated ceilings, the banking system was suffering from an unsound competition on raising deposit rates for attracting more depositors. This unhealthy competition was also expanded to include even the ordinary short-term deposits and those deposits whose profit was calculated on a daily basis. The reason behind the depositors' tendency to open ordinary short-term deposits with banks was the high profit rates along with easy access to cash deposits and the opening and closing of such accounts. The said Circular managed to regulate banks' behavior in this regard, paving the way for a reform in the composition of banking deposits. As a result, the share of long-term deposits in total banking deposits increased and far better conditions were set for the more efficient management of the money market. Large-scale oversight by the CBI has pointed to banks' sound behavior in terms of observing the ceilings declared in the Circular.

Another significant measure adopted by the CBI in 2017/18 for raising the effectiveness of the monetary policy in the money market was the restructuring of unlicensed credit institutions and resolving the related challenges. Therefore, with the pursuance of the process started in 2014/15 as per the Approval by the Supreme National Security Council in the form of a four-stage plan for the restructuring of unlicensed non-bank financial institutions, the CBI managed to successfully terminate the operations of unlicensed institutions in 2017/18, with the coordination of relevant agencies, which was a fundamental step in bringing discipline back to the money market. Therefore, in coordination with the relevant judicial bodies, a credit line of Rls. 183.0 trillion was opened to agent banks by March 2018, with the aim of repayment of deposits to deposit holders. This was an important step in the process of a complete halt in the financial operations of unlicensed institutions.

In light of the CBI policies in reforming banks' deposit and lending rates in 2017/18, key economic variables, such as the exchange rate, also enjoyed favorable trends during April-December 2017. During January-March 2018, however, the foreign exchange market experienced some turbulence, which was in turn due to some external factors and negative expectations resulting from the likely withdrawal of the US from the nuclear deal. This negative trend was aggravated due to the prevalence of speculative activities in the foreign exchange market, which led to further uncertainty by the public. In response to these negative developments and with the aim of bringing stability back to the foreign exchange market, the CBI took measures to issue a short-term policy package in coordination with the government. The main items on this package included the issuance of rial Certificates of Deposit (CDs) with a 20-percent rate of return, one-year and two-year dollar-indexed CDs with annual returns of respectively 4.0 and 4.5 percent, and a plan for the advance sales of gold coins at the conclusive prices of Rls. 14 million and Rls. 13 million for gold coin delivery after 6 months and one year, respectively. This policy package was declared on February 17, 2018. Among the items on this package, the 20-percent rial CD plan was favored by the public more than the other two, lasting from February 17 until March 1, 2018. As a result, the sales of rial CDs came to the remarkable amount of Rls. 2,436.2 trillion. The CBI measures of September 2017 and February 2018 culminated in some remarkable achievements including the reduction of the share of short-term deposits in total non-public sector deposits from 45.4 percent in August 2017 to 26.5 percent in March 2018 and the mopping up of high liquidity in the foreign exchange and gold markets.

Banking System[1] Performance

Banking system assets and liabilities increased by 22.1 percent to Rls. 31,130.8 trillion in 2017/18. Other assets, with 24.2 percent (Rls. 2,006.3 trillion) increase were the main factor contributing to the rise in assets. Claims on non-public sector (including profit and revenue receivables) and foreign assets, with respectively 19.0 and 25.7 percent growth (Rls. 1,741.3 trillion and Rls. 1,498.0 trillion increase) were the other two factors raising the assets. On the liabilities side of the

[1] Includes the CBI, public commercial and specialized banks, private banks, and non-bank credit institutions.

banking system, liquidity (M2), with 22.1 percent (Rls. 2,765.9 trillion) increase and other liabilities (including capital account of the banking system, advance payments on public sector's L/Cs, and order registration deposit of non-public sector), with 17.5 percent (Rls. 1,584.7 trillion) growth, were the major factors contributing to the rise of banks' liabilities.

Banking System and External Sector

In 2017/18, the net foreign assets of the banking system increased by about 13.6 percent (Rls. 342.4 trillion) to Rls. 2,855.0 trillion. This was attributable to the increase in CBI net foreign assets by Rls. 235.2 trillion on the one hand and rise in the net foreign assets of the public and private banks as well as non-bank credit institutions by Rls. 107.2 trillion on the other. The reason behind the rise in the CBI net foreign assets was Rls. 676.0 trillion increase in its foreign assets as well as Rls. 440.8 trillion growth in its foreign liabilities. The increase in the net foreign assets of public and private banks and credit institutions was attributable to the rise in their foreign assets and liabilities by Rls. 822.0 trillion and Rls. 714.8 trillion, respectively.

Figure 13.1. Major economic variables

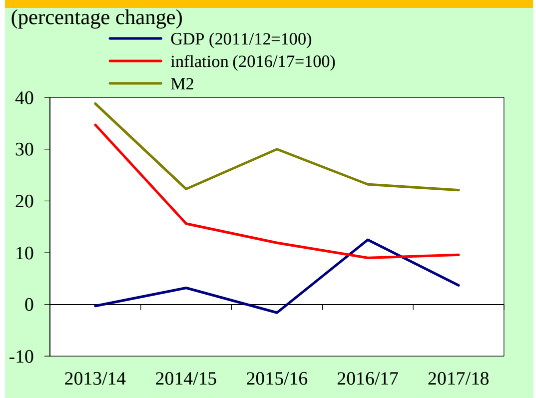


Table 13.1. Major Assets and Liabilities of the Banking System[1] (trillion rials)

	Year-end balance			Percentage change	
	2015/16	2016/17	2017/18	2016/17	2017/18
Assets	**22,591.7**	**25,496.6**	**31,130.8**	**12.9**	**22.1**
Foreign assets	5,823.0	5,823.5	7,321.5	*	25.7
Central Bank	3,517.5	3,394.1	4,070.1	-3.5	19.9
Public banks	854.7	982.7	1,268.1	15.0	29.0
Private banks and non-bank credit institutions	1,450.8	1,446.7	1,983.3	-0.3	37.1
Claims on public sector	1,738.6	2,197.5	2,586.1	26.4	17.7
Claims on non-public sector	7,362.2	9,177.2	10,918.5	24.7	19.0
Others	7,667.9	8,298.4	10,304.7	8.2	24.2
Liabilities	**22,591.7**	**25,496.6**	**31,130.8**	**12.9**	**22.1**
Liquidity (M2)	10,172.8	12,533.9	15,299.8	23.2	22.1
Loans and deposits of public sector	635.5	614.4	742.4	-3.3	20.8
Foreign liabilities	3,358.7	3,310.9	4,466.5	-1.4	34.9
Central Bank	1,581.1	1,469.5	1,910.3	-7.1	30.0
Public banks	574.7	696.5	951.5	21.2	36.6
Private banks and non-bank credit institutions	1,202.9	1,144.9	1,604.7	-4.8	40.2
Others[2]	8,424.7	9,037.4	10,622.1	7.3	17.5

[1] Excludes below the line items.

[2] Includes other liabilities, capital account, advance payments on public sector's L/Cs, and order registration deposit of non-public sector.

Banking System and Public Sector

Banking system's net claims on the public sector increased by Rls. 260.6 trillion to reach Rls. 1,843.7 trillion in 2017/18. The CBI's claims on the public sector decreased by 8.3 percent (Rls. 48.1 trillion), which was due to 1.8 percent fall in the CBI's claims on the government and 14.3 percent decline in public corporations' and institutions' debt to the CBI. Of the total CBI's claims on the government, Rls. 39.2 trillion (14.6 percent) was due to the deficit in the foreign exchange obligations account[1] and Rls. 8.9 trillion, to the unification of the exchange rate in 2002. Public sector's deposits with the CBI increased by 25.9 percent (Rls. 96.6 trillion) in 2017/18, mainly attributable to the increase in government's deposits with the CBI by Rls. 101.5 trillion and decrease in public corporations' and institutions' deposits with the CBI by Rls. 4.9 trillion.

Public sector's indebtedness to banks and non-bank credit institutions surged by 26.9 percent (Rls. 436.7 trillion) in 2017/18, mainly due to 27.8 percent (Rls. 440.9 trillion) growth in banks' and non-bank credit institutions' claims on the government. The government's debt to banks and non-bank credit institutions reached Rls. 2,025.0 trillion in March 2018.

Banking System[2] and Non-public Sector[3]

In 2017/18, the outstanding facilities[4] extended by the banking system to the non-public sector increased by 18.5 percent (Rls. 1,520.6 trillion) to Rls. 9,761.3 trillion. This shows 5.3 percentage points decrease as compared with 23.8 percent growth in 2016/17. The share of the outstanding facilities extended by the banking system to the non-public sector equaled 82.6 percent of total facilities extended to public and non-public sectors. This indicated one percentage point decrease compared with the respective figure in the year before (83.6 percent).

Table 13.2. Change in Net Claims of Banking System on Public Sector (trillion rials)

	2016/17	2017/18
Public sector	**480.0**	**260.6**
Central Bank	20.4	-144.7
Commercial and specialized banks (public)	228.3	205.9
Private banks and non-bank credit institutions	231.3	199.4
Government	**449.2**	**303.2**
Central Bank[1]	-0.1	-106.3
Commercial and specialized banks (public)	229.7	200.5
Private banks and non-bank credit institutions	219.6	209.0
Public corporations and institutions	**30.8**	**-42.6**
Central Bank	20.5	-38.4
Commercial and specialized banks (public)[2]	-1.4	5.4
Private banks and non-bank credit institutions	11.7	-9.6

[1] Includes the deficit in the foreign exchange obligations account, resulted from the unification of the exchange rate in 1993, as well as government debt to the CBI due to the unification of the exchange rate in 2002.
[2] Includes indebtedness for the exchange rate differential, resulted from the unification of the exchange rate in 1993.

[1] The foreign exchange obligations account was opened in 1993, upon the unification of the exchange rate.

[2] Includes state-owned and private banks as well as non-bank credit institutions.
[3] Figures in this section exclude profit and revenue receivables and are therefore different from the figures in Appendix.
[4] Includes overdue and non-performing loans.

The outstanding facilities extended by public commercial banks to non-public sector (excluding profit and revenue receivables) rose 20.6 percent (Rls. 261.9 trillion) to reach Rls. 1,532.2 trillion in March 2018. The outstanding facilities extended by specialized banks to the non-public sector grew by 14.8 percent (Rls. 243.7 trillion) to Rls. 1,888.0 trillion. For private banks and non-bank credit institutions, this variable grew by 19.1 percent (Rls. 1,015.0 trillion) to Rls. 6,341.1 trillion. Therefore, the share of public commercial banks increased from 15.4 percent in March 2017 to 15.7 percent in March 2018 and that of private banks and non-bank credit institutions rose from 64.6 percent to 65.0 percent in the same period. The share of specialized banks, on the other hand, decreased from 20.0 percent to 19.3 percent. In 2017/18, the highest share (40.0 percent) of the increase in net outstanding facilities extended by the banking system to the non-public sector belonged to "construction and housing", followed by "exports" and "domestic trade, services, and miscellaneous" by 37.9 percent, "manufacturing and mining" by 15.7 percent, and "agriculture" by 6.4 percent. The composition of the outstanding facilities extended by banks to the non-public sector according to Islamic contracts shows that civil partnership and installment sale held the highest shares by 37.8 and 26.5 percent.

Figure 13.2. Public & non-public sectors' debt to banks and non-bank credit institutions (excluding profit and revenue receivables)

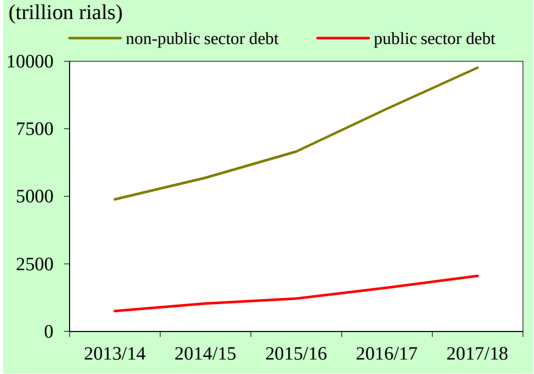


Table 13.3. Facilities Extended by Banking System to Non-public Sector[1] (trillion rials)

	Year-end balance			Percentage change		Share (percent)	
	2015/16	2016/17	2017/18	2016/17	2017/18	2016/17	2017/18
Public commercial banks	1,026.6	1,270.3	1,532.2	23.7	20.6	15.4	15.7
Specialized banks	1,460.3	1,644.3	1,888.0	12.6	14.8	20.0	19.3
Private banks and non-bank credit institutions	4,168.4	5,326.1	6,341.1	27.8	19.1	64.6	65.0
Total	**6,655.3**	**8,240.7**	**9,761.3**	**23.8**	**18.5**	**100.0**	**100.0**

[1] Excludes profit and revenue receivables.

Table 13.4. Share of Economic Sectors in Increase in Net Outstanding Facilities[1] Extended by Banking System to Non-public Sector (percent)

	2016/17			2017/18		
	Public banks	Private banks & non-bank credit institutions	Banking system	Public banks	Private banks & non-bank credit institutions	Banking system
Agriculture	14.4	1.8	5.5	17.1	0.0	6.4
Manufacturing and mining	14.5	12.7	13.2	21.8	12.0	15.7
Construction and housing	20.2	4.6	9.1	18.9	52.5	40.0
Exports	-0.7	0.0	-0.2	1.9	0.2	0.8
Domestic trade, services, and miscellaneous	51.6	80.9	72.4	40.3	35.3	37.1
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

[1] Calculated after deduction of outstanding debts of customers and extended facilities related to the exchange rate differential, profit receivables, profit and commission receivables, receipts from Mudarabah, civil partnership (bank's share), outstanding profit, and outstanding commission; including legal partnership and direct investment contracts.

The share of facilities extended in the form of Murabaha, installment sale, Ju'alah, Gharz-al-hasaneh, and forward transactions was higher while that of civil partnership, legal partnership, Mudarabah, and direct investment was lower than 2016/17.

The ratio of overdue and non-performing loans to total rial facilities extended by banks and non-bank credit institutions to public and non-public sectors increased by 0.8 percentage point from 9.5 percent in March 2017 to 10.3 percent in March 2018. This variable declined by 0.4 percentage point for public commercial banks while it increased by 2.2 percentage points for specialized banks and 0.6 percentage point for private banks and non-bank credit institutions.

Given the important role of the SMEs in job creation and realization of the objectives of the resistance economy, the Guideline on Financing the SMEs was drafted by the CBI in May 2016 and announced for implementation to the banking system[1]. Accordingly, as of implementation until March 2018, a sum of Rls. 362.9 trillion of facilities was allocated to 52.4 thousand eligible manufacturing establishments, within the framework of the provincial working groups' approvals and direct facilities extended by banks.

Table 13.5. Composition of Outstanding Facilities Extended by Banking System to Non-public Sector by Contracts (percent)

	Banking system	
	2016/17	2017/18
Installment sale	25.6	26.5
Mudarabah	1.8	1.6
Civil partnership	42.3	37.8
Gharz-al-hasaneh	5.1	5.5
Hire purchase	0.3	0.3
Forward transactions	0.3	0.6
Legal partnership	3.6	2.9
Direct investment	0.9	0.7
Ju'alah	3.6	4.2
Murabaha	5.3	8.1
Others [1]	11.2	11.8
Total	**100.0**	**100.0**

[1] Includes debt purchase, machinery and housing units transacted under Islamic contracts, Istisna, and overdue and non-performing loans.

Table 13.6. Ratio of Overdue and Non-performing Loans to Total Facilities Extended by Banking System (in rials) [1] (percent)

	2016/17	2017/18	Change (percentage points)
Public commercial banks	7.6	7.2	-0.4
Specialized banks	7.8	10.0	2.2
Private banks and non-bank credit institutions	10.7	11.3	0.6
Banking system	**9.5**	**10.3**	**0.8**

[1] Includes overdue, non-performing, and doubtful claims of public and non-public sectors.

[1] Circular No. 95/27577 dated April 20, 2016.

Banks' and credit institutions' scheduled facilities reached Rls. 450.1 trillion in 2017/18, of which Rls. 146.4 trillion (32.5 percent) was related to Gharz-al-hasaneh facilities and Rls. 303.7 trillion was related to other uses. Of total Gharz-al-hasaneh facilities, Rls. 122.5 trillion (83.7 percent) was exclusively allocated as marriage facility and Rls. 23.9 trillion was extended for employment of help-seekers of welfare organizations, release of needy prisoners, and home-based businesses. A sum of Rls. 43.5 trillion of other scheduled facilities was related to the guaranteed purchase of strategic agricultural products and Rls. 40.4 trillion was related to Mehr Housing Program[1].

Broad Money (M2)

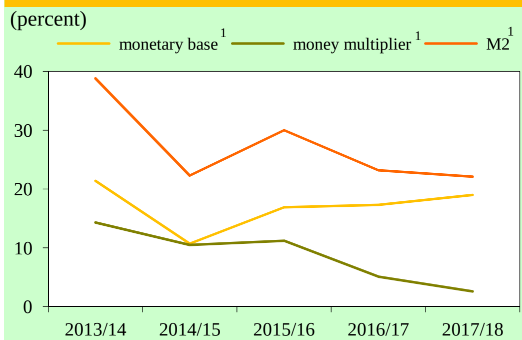
In 2017/18, broad money (M2) grew by 22.1 percent to reach Rls. 15,299.8 trillion, indicating 1.1 percentage points decrease compared with 23.2 percent growth in the year before.

The positive growth of broad money was mainly attributable to the 19.0 percent rise in the monetary base, which was in turn due to the increase in CBI claims on banks. Moreover, money multiplier reached 7.150 in 2017/18, up by 2.6 percent compared with the year before.

Table 13.7. Banks' Performance on Scheduled Facilities in 2017/18 (trillion rials)

Purposes	Paid facilities in 2017/18
Gharz-al-hasaneh facilities	**146.4**
Marriage	122.5
Other	23.9
Other scheduled facilities	**303.7**
Guaranteed purchase of strategic agricultural products	43.5
Rural housing	5.5
Mehr Housing Program	40.4
Old buildings	5.5
Veterans' Home Facility	7.4
Financing of SMEs	195.0
Sustainable employment (subject to Note 18, Budget Law for 2017/18)	6.4
Total	**450.1**

Figure 13.3. Growth of M2 and its determinants



[1] In 2013/14, the homogenous growth figures for M2, money multiplier, and monetary base, comparable with corresponding figures of previous years, were 25.9, 7.7, and 16.9 percent.

Table 13.8. M2 and its Determinants

	Year-end balance		Percentage change	
	2016/17	2017/18	2016/17	2017/18
Monetary base (trillion rials)	1,798.3	2,139.8	17.3	19.0
Money multiplier	6.970	7.150	5.1	2.6
M2 (trillion rials)	12,533.9	15,299.8	23.2	22.1

[1] As per the MCC Approval dated September 22, 2015, the ceiling on Mehr housing facilities was set at Rls. 555.4 trillion, which was in effect for 2017/18 as well.

Among the factors affecting M2 growth in 2017/18, net domestic assets of the banking system, with 24.2 percent growth compared with 2016/17, had an increasing share of 19.4 percentage points in raising M2. Among the items of net domestic assets, banks' and non-bank credit institutions' claims on non-public sector (excluding profit and revenue receivables), with 18.5 percent growth and an increasing share of 12.1 percentage points, and net other items with 319.6 percent growth and a positive contribution of 5.1 percentage points, were the main factors contributing to M2 growth. Banking system net claims on public sector had an increasing share of 2.2 percentage points in raising M2. Moreover, net foreign assets of the banking system, with 13.6 percent increase compared with 2016/17, had a positive share of 2.7 percentage points in M2 growth.

Table 13.9. Contribution of Factors Affecting M2 Growth (percentage points)

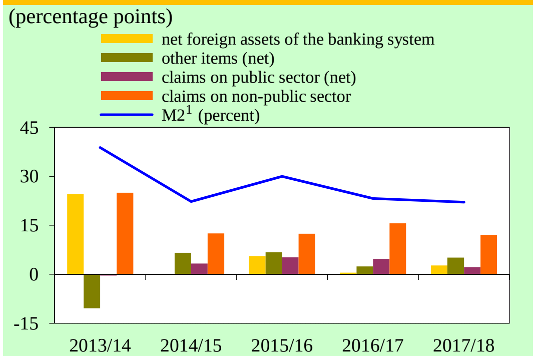
	2016/17	2017/18
Net foreign assets of the banking system	**0.5**	**2.7**
Net domestic assets of the banking system	**22.7**	**19.4**
Claims on public sector (net)	4.7	2.2
Government	4.4	2.5
Public corporations	0.3	-0.3
Claims on non-public sector [1]	15.6	12.1
Other items (net)	2.4	5.1
M2 (percent)	**23.2**	**22.1**

[1] Excludes profit and revenue receivables.

Monetary Base

CBI claims on banks, with 32.4 percent growth and an increasing share of 18.0 percentage points, were the most important factor behind the rise in monetary base which, compared with the previous year (an increasing share of 10.5 percentage points in the 17.3 percent growth of monetary base), indicated 7.5 percentage points increase. In spite of CBI efforts in restricting banks' and credit institutions' access to CBI overdraft facilities as well as converting overdrafts to lines of credit through depositing in the interbank market, banks' indebtedness to the Central Bank continued to increase in 2017/18, upon further deepening of banks' balance sheet difficulties.

Figure 13.4. Factors affecting M2 growth



[1] In 2013/14, the homogenous growth figure for M2, comparable with corresponding figures of previous years, was 25.9 percent.

CBI net foreign assets, with 12.2 percent increase compared with March 2017 and an increasing share of 13.1 percentage points, was the other factor positively affecting the monetary base. CBI net claims on public sector, with 71.4 percent decrease compared with March 2017 and a negative effect of 8.0 percentage points, was another factor responsible for the decline of monetary base. This was attributable to 8.3 percent decrease in CBI claims on public sector (with a share of -2.7 percentage points) as against 25.9 percent rise in public sector's deposits with the CBI (with a share of -5.3 percentage points in the growth of monetary base). CBI other items (net), with 5.5 percent fall and a decreasing share of 4.1 percentage points, was the other factor adversely affecting monetary base in March 2018. If the effect of the exchange rate revaluation account is eliminated from the CBI's balance sheet, the share of CBI net other items in the growth of monetary base will increase from -4.1 percentage points to 6.9 percentage points.

Table 13.10. Breakdown of Factors Affecting Monetary Base Growth (percentage points)

	2016/17	2017/18
CBI net foreign assets	-0.8	13.1
CBI net claims on public sector	1.3	-8.0
CBI claims on banks	10.5	18.0
CBI other items (net)	6.3	-4.1
Monetary base (percent)	**17.3**	**19.0**

Composition of M2

The share of narrow money (M1) in M2 declined from 13.0 percent in March 2017 to 12.7 percent in March 2018. The share of quasi-money, however, rose 0.3 percentage point to 87.3 percent, partly attributable to customers' interest in non-sight deposits' profit rates as compared to cash as well as growth in the use of electronic banking and payment cards connected to short-term deposits.

The share of one-year deposits in total long-term deposits increased by 9.1 percentage points from 85.6 percent in 2016/17 to 94.7 percent in 2017/18. On the other hand, the share of five-year deposits in total long-term deposits fell by 8.3 percentage points from 13.1 percent in 2016/17 to 4.8 percent in 2017/18 and shares of two-, three-, and four-year deposits decreased from respectively 0.9, 0.2, and 0.2 percent in 2016/17 to 0.3, 0.1, and 0.1 percent in 2017/18.

The ban set in May 2014 on the opening of deposits with maturities of more than a year, which was also in effect in 2015-2017, was the major reason behind the fall in the share of long-term deposits of more than one year in 2017/18.

Table 13.12. Composition of Long-term Deposits (percent)

	Year-end		
Deposits	2015/16	2016/17	2017/18
One-year	77.1	85.6	94.7
Two-year	4.0	0.9	0.3
Three-year	0.4	0.2	0.1
Four-year	0.3	0.2	0.1
Five-year	18.2	13.1	4.8

Table 13.11. Composition of Broad Money (trillion rials)

	Year-end balance			Percentage change		Share in M2 (percent)	
	2015/16	2016/17	2017/18	2016/17	2017/18	2016/17	2017/18
M1	**1,367.0**	**1,630.3**	**1,946.7**	**19.3**	**19.4**	**13.0**	**12.7**
Notes and coins with the public	371.9	393.3	442.7	5.8	12.6	3.1	2.9
Sight deposits of non-public sector	995.1	1,237.0	1,504.0	24.3	21.6	9.9	9.8
Quasi-money	**8,805.8**	**10,903.6**	**13,353.1**	**23.8**	**22.5**	**87.0**	**87.3**
Gharz-al-hasaneh savings deposits	469.8	602.9	801.9	28.3	33.0	4.8	5.2
Term investment deposits	8,187.4	10,123.1	12,339.1	23.6	21.9	80.8	80.7
Miscellaneous deposits	148.6	177.6	212.1	19.5	19.4	1.4	1.4
M2	**10,172.8**	**12,533.9**	**15,299.8**	**23.2**	**22.1**	**100.0**	**100.0**

Sources and Uses of Funds of Public Commercial Banks

The value of non-public sector's deposits with public commercial banks grew by 33.0 percent (Rls. 749.6 trillion) in 2017/18. Deposits of non-public sector held with commercial banks included sight deposits, the value of which rose Rls. 68.2 trillion and non-sight deposits whose value increased by Rls. 681.4 trillion. The non-usable resources of public commercial banks increased by Rls. 83.5 trillion, mainly owing to Rls. 84.7 trillion increase of reserve requirement and Rls. 1.2 trillion decrease in notes and coins kept with commercial banks. Moreover, the balance of the capital account of public commercial banks decreased by Rls. 0.8 trillion while public sector's deposits and funds went up by Rls. 18.7 trillion. Accordingly, non-public sector indebtedness[1] and public sector indebtedness[2] rose by Rls. 261.9 trillion and Rls. 101.7 trillion, respectively.

Sources and Uses of Funds of Specialized Banks

In 2017/18, non-public sector's deposits held with specialized banks grew by Rls. 389.9 trillion. The value of sight deposits increased by Rls. 35.2 trillion and that of non-sight deposits rose by Rls. 354.7 trillion. In this year, the non-usable resources of specialized banks rose by Rls. 30.7 trillion, resulting from Rls. 30.0 trillion increase in reserve requirement and Rls. 0.7 trillion rise in the value of notes and coins. Free resources out of non-public sector's deposits held with specialized banks increased by Rls. 359.2 trillion. Total free credit resources of specialized banks, including other sources (debt to the Central Bank, external debt, debt to other banks, and other funds), increased by Rls. 314.7 trillion. This included rise in non-public sector's debt to specialized banks by Rls. 243.7 trillion and increase in public sector's debt by Rls. 71.0 trillion. CBI claims on specialized banks declined by 4.5 percent (Rls. 22.3 trillion) to Rls. 472.1 trillion in March 2018.

Sources and Uses of Funds of Private Banks and Non-bank Credit Institutions[3]

In 2017/18, non-public sector's deposits with private banks and non-bank credit institutions rose by 18.2 percent (Rls. 1,577.0 trillion) compared with the year before. In this regard, the value of sight deposits increased by Rls. 163.6 trillion and that of non-sight deposits went up by Rls. 1,413.4 trillion. The non-usable resources of private banks and non-bank credit institutions increased by Rls. 175.4 trillion in 2017/18, mainly due to Rls. 174.8 trillion rise in reserve requirement and Rls. 0.6 trillion growth in notes and coins held with private banks and non-bank credit institutions.

Furthermore, the balance of the capital account of private banks and non-bank credit institutions decreased by Rls. 141.0 trillion compared with 2016/17 while public sector's deposits and funds kept with private banks and non-bank credit institutions increased by Rls. 9.6 trillion in 2017/18. Consequently, private banks' and non-bank credit institutions' claims on the non-public sector increased by Rls. 1,014.2 trillion and public sector's debt to private banks and non-bank credit institutions rose by Rls. 177.3 trillion in 2017/18.

[1] Excludes profit and revenue receivables.

[2] The sources and uses of funds' data in the text and tables exclude participation papers issued by the government. Hence, the figure for public sector debt is different from the figure in "Major Assets and Liabilities" table.

[3] Includes banks privatized under Article 44 of the Constitution.

Banking Units and Personnel

In 2017/18, the number of banking units, including branches and counters in both domestic offices and representative offices abroad, fell by 1.7 percent to 23,009 units, 22,962 of which were located in Iran and the remaining were on foreign lands. Bank Melli Iran and Bank Saderat Iran held the highest shares in the number of domestic units by 14.3 and 12.2 percent, respectively. In 2017/18, the number of banking system employees decreased by 2.5 percent to 217,127 persons, with the number of employees in public commercial banks, public specialized banks, and private banks and non-bank credit institutions falling by 3.3, 2.9, and 2.0 percent, respectively. The ratio of banking sector employees to banking units (domestic and foreign branches) was 9.4 on average, down by 1.1 percent. Moreover, the ratio of total population to each domestic banking unit rose by about 111 persons to reach 3,531.

Banking Sector Developments

The following includes the major banking measures adopted by the CBI for 2017/18.

Section One- Major Regulations, Bylaws, Guidelines, Circulars, and Amendments

- Design and announcement of Guideline on Corporate Governance in Non-public Credit Institutions, with the aim of strengthening and improving governance, attaining operational goals and sound financial reporting, and complying with rules and regulations in non-bank financial institutions (subject of Circular No. 96/51935 dated May 14, 2017);

- Design and announcement of the Guideline on Investment in Securities, aimed at streamlining the investment strategy of banks and non-bank credit institutions, containing the risks in their investment activities, and restraining high direct ownership by banks in their non-core businesses (subject of Circular No. 96/61277 dated May 22, 2017);

- Revision and announcement of Executive Guideline on Establishment, Operation, and Supervision of Credit Cooperatives, with the aim of rationalizing the credit process of credit cooperatives and preventing unregulated cooperative activities (subject of Circular No. 96/111554 dated July 8, 2017);

- Revision and announcement of Guideline on Supervisory Capital Assessment and Capital Adequacy of Credit Institutions, aimed at sustaining stability and soundness of the banking system via maintaining adequate capital by credit institutions in line with covering risks concerned with banking operations (subject of Circular No. 96/111597 dated July 8, 2017);

Table 13.13. Number of Banking Units [1]

	2016/17	2017/18
Domestic branches	**23,370**	**22,962**
Commercial banks	5,488	5,452
Specialized banks	3,838	3,784
Private banks and non-bank credit institutions	14,044	13,726
Foreign branches	**45**	**47**
Total	**23,415**	**23,009**

[1] Excludes representative offices.

- Revision and announcement of Guideline on Open market Operations by Credit Institutions, considering the latest financial condition of credit institutions, aimed at the optimal management of assets and external liabilities as well as risks associated with exchange rate fluctuations (subject of Circular No. 96/143113 dated August 1, 2017);

- Formulation and announcement of the Executive Guideline on Identification and Settlement of Inoperative and Dormant Rial Accounts, with the aim of protecting the rights of holders of inactive accounts, preventing abuse of such accounts, raising banks' financial transparency, and designing a uniform accounting rule for registration and maintenance of such funds in banks (subject of Circular No. 96/165650 dated August 21, 2017);

- Formulation and announcement of the Guideline on Credit Institutions' Compliance with Rules and Regulations, with the aim of encouraging compatibility, congruent with the international norms and standards (subject of Circular No. 96/235076 dated October 19, 2017);

- Formulation and announcement of the minimum requirements regarding liquidity risk management in credit institutions, with the aim of ensuring credit institutions' access to appropriate liquidity and the timely fulfillment of loans and commitments by these institutions, protection of deposit holders' rights, and control of liquidity risks (subject of Circular No. 96/251081 dated October 31, 2017);

- Revision and announcement of Guideline on Governing Rial Bank Guarantees, with the aim of prevention of violations and abuse as regards bank guarantees (subject of Circular No. 96/255755 dated November 5, 2017);

- Approval and announcement of the Guideline on Paragraph B, Article 17, 6th FYDP Law and Paragraph A, Article 20 of Permanent Clauses of Development Plans of the Country, upon the joint recommendation of the CBI, the Ministry of Economic Affairs and Finance, and the Plan and Budget Organization (subject of Circular No. 96/307074 dated December 18, 2017);

- Preparation and announcement of the selected sections of Basel II and III documents on precautionary measures regarding credit institutions, troubled assets, rescheduling procedures, and non-performing loans;

- Preparation and announcement of the selected sections of Basel II and III documents, with the aim of raising awareness regarding Basel's conceptual framework and facilitating the implementation of this framework and its standards.

Section Two- Major Measures on Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT)

- Adopting a comprehensive supervisory framework to check banks' compliance with the Anti-Money Laundering rules;

- Adopting a case by case supervisory scheme on banks' compliance with the AML measures and implementation of the AML software;

- Tracking the sources of initial capital for the establishment or capital increase of banks and credit institutions, according to the National Security High Council's Approval;

- Tracking the sources of initial capital for the establishment or capital increase of insurance companies, as per the Approval of the High Council of Anti-Money Laundering;

- Design and announcement of the Approvals of the High Council of Anti-Money Laundering and their dispatching to the banking system;

- Holding elementary and advanced training courses on Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) measures in the CBI, with the coordination of Training and Human Resource Department, Monetary and Banking Research Institution, and Iran Banking Institute of the CBI;

- The exchange of information with international organizations as per the rules and standards, on their experience in terms of the execution of AML measures;

- Active participation in international forums on AML/CFT measures and elaboration on CBI policies in this regard;

- Establishment, operationalization, and expansion of NAHAB (Electronic Banking Authentication System), aimed at executing Article 20 of Executive Bylaw on AML/CFT Law approved in 2009 and ensuring observation by institutions based on the comprehensive authentication of banks' clients;

- Preparation of the draft executive bylaw on AML/CFT;

- Taking preliminary measures for the development of a comprehensive oversight questionnaire on the execution of the AML Law in the Iranian banking system.

Section Three- Bank Licensing[1]

In line with the Monetary and Banking Law of Iran, the Law on Rationalization of the Unorganized Money Market, and the five-year development plans of the country, the Central Bank has been vested with the mission to review the applications submitted by monetary institutions for the establishment, operation, and registration procedures of foundations willing to start operating in the money market. In this respect, the CBI issued establishment and operation licenses for 8 credit cooperatives, 21 Gharz-al-hasaneh Funds, 5 leasing companies, and 235 exchange bureaus in 2017/18.

Meanwhile, the work permits for 126 institutions, which used to have temporary work permits, were renewed in this year and licenses of 4 exchange bureaus as well as 3 credit cooperatives were revoked by March 2018.

Table 13.14. Number of Licenses Issued, Renewed, and Cancelled for Institutions Active in Unorganized Money Market in 2017/18[1]

	Initial licenses		Renewed licenses	Total	Revoked licenses
	Establishment	Operation			
Credit cooperatives	2	6	14	**22**	3
Gharz-al-hasaneh Funds	9	12	1	**22**	0
Leasing companies	3	2	11	**16**	0
Exchange bureaus	102	133	100	**335**	4
Total	**116**	**153**	**126**	**395**	**7**

[1] Establishment licenses are issued at the initial phase to allow the establishment of the monetary foundation. Operation licenses allow the foundations to start operating.

[1] There is a time gap between the CBI's granting of a license to banks and credit institutions and their forwarding of the standard general ledger to the CBI for inclusion in the monetary and banking data.