

Situation on the summary of the monetary policy on 9 months of 2002

1. Situation on the monetary policy

Under the positive influence of the international price conjuncture of the foreign products, especially the products consisting the base of Azerbaijani export and under the favourable internal macroeconomic conditions, the National Bank has conducted the monetary policy related to the maintenance of the acceptable level of the inflation, prompt adjustment of the national currency rate, maintenance of the currency reserves meeting the international standards and the strengthening of the national banking system and improvement of the money supply in the economy within 9 months of 2002 and mainly achieved the targets.

Macroeconomic situation

As a result of a purposeful economical and monetary policy the macroeconomic stability was kept in Azerbaijan during 9 months of 2002.

The inflation rate was at 1.4% in Azerbaijan in 9 months of 2002. The inflation was expected to maintain its forecasted rate (2.5%) during the year.

Researches carried out according to the inflation model show that the price change of the food products 82.5%, the non-food products 16.4% and the price changes of the services 1% influenced the alteration of the price.

The alterations of the prices were related 49.4% to the monetary factors, 29.3% to the non-monetary factors and 21% to the seasonal factors.

The real amount of the gross domestic product as a main economical indicator has increased by 9.8%.

0.1% industrial and 3.3% agricultural growth were achieved.

The share of the private sector in the economy increased regularly which is an important condition to obtain the status of the country of the market economy. During 9 months 49% of the industrial product, 98% of the agricultural commodities, 80.2% of the investments, 76.1% of the communicational services, 55.1% of the freight forwarding and 85.4% of the passenger turnover was performed by the non-government sector.

The amount of the investment in the fundamental construction sphere as a main guarantee factor of the future economical development increased by 90.1% constituting 7.1 trillion manats, since 5.3 trillion manats or 75.9% of this was the foreign investment.

The improvement of the foreign commerce continued. During January - August months the foreign commerce was 2155.3 million USD, the amount of the export decreased by 20.1% constituting 1145.8 million USD and the import increased by 30% constituting 1009.5 million USD.

A positive balance of 705.1 million USD appeared in the foreign trade.

The improvement of the population's welfare continued. The income of the population during 9 months of 2002 increased by 10.4% constituting 15131.4 billion manats and expenses increased by 10.4% constituting 15176.6 billion manats compared to the same period of the previous year. The average salary rose up to 310.8 thousand manats and its real growth was 19.4%. In its turn the increase of population's income was the guarantee factor of the real sector development, enhancing purchasing capacity.

Inclinations in the world economy

The past period of 2002 was memorable due to start of some decelerations of the economical crisis begun in leading countries of the world in the year 2001.

After the traditional New Year improvement in the USA the stock indexes began to slowdown again at the beginning of the year. For the first time during the last year and half the growth of the industrial product was observed during the months of January – February. According to the summary on the first quarter of the year the GDP increased by 5.8%. The

increase of the new employment places was fixed firstly since July, 2001. The raise of the wholesale trade also has indicated the increase of the business activity. The Consumer Sentiment Index also began to rise. So the Federal Reserve System officially declared that the economical regress had been stopped and it would perform neutral monetary policy. Under the pressure of the industrial producers of the USA and for the purpose of the export stimulation the FRS began to soften exchange policy. It should be noted that the increase of the government spendings played an important role in the increase of the economical indicators. But the production activity index began to drop again which displayed a stagnation in the industry in the third quarter. Index of the new orders also dropped below the critical level (50). Meanwhile the supposed apprehension of this crisis began to worry the analysts.

Despite the descent in the exchange rate of euro from 0.9 USD to 0.8 USD, as well as the increase of the unemployment level, the other indicators of the economical activity displayed the development in Europe in the beginning of the year. For example, the index of the economical activity in the services sector went up to the top level during the last 13 months. The strengthening of the inclinations of the economical growth in Europe in the end of the year, as well as the policy of the FRS of the USA oriented to make dollar cheaper, increased the exchange rate of euro. As a result the exchange rate of euro to USD rose up to the parity level of 1.013. It should be noted that the appreciation of euro appeared sooner than expected by the analysts. But the production activity index, as well as the index on the services sector began to drop during the third quarter. It is mostly related to the negative tendencies in Germany possessing the most enormous economy in Euro region.

The economical indicators in Japan display the continuation of the economical crisis. The situation of the banks has become worse, the assurance for the deposits was eliminated by the government and the orders for the machinery and equipment dropped down to the level of 1987. In addition, the ratings of the leading insurance companies decreased in Japan. But the improvement of the variety of economical indicators was already observed in Japan by the end of the second quarter of the year. So, according to the summary of the second quarter of 2002, 0.6% growth of GDP and 5.7% growth of the export were fixed. The economical indicators began to deteriorate again at the end of the third quarter. Main stock index dropped to 19-year minimum in September 4 in Japan.

The demand for the government loans rose significantly as the shares went down. This allowed the profitability of the government loans to drop.

In spite of the influence of information that the oil reserves of America had increased and the demand had decreased during the period, the price of oil in the world market was characterized as appreciating. The price of oil for a barrel already was 30 USD by the end of September.

The raise in price of gold in the world market was fixed as well. Experts explain this as the result of joining companies - gold producers. Meanwhile 10 biggest corporations of gold producers maintain 40% of the world gold production.

2. Dynamics of money-and-credit indicators

According to the main directions of the monetary policy, the aims on the inflation rate and the exchange value of manat relative to the convertible foreign currencies were achieved due to the chasing of the amounts of the monetary program parameters.

The monetary base of manat compared to the same period of the previous year increased by 12.4% constituting 1691.6 billion manats by October 1, 2002.

The **broad monetary aggregate (M-2)** increased by 10.1% constituting 1765.2 billion manats.

The monetary multiplier characterizing the ability of banking system to create money went up. The reconstruction of the banking system, development of the banking infrastructure,

and especially improvement of the payment system resulted in the positive dynamics of this indicator.

The amount of the credit investment increased by 3% constituting 2436.9 billion manats during 9 months of 2002 compared to the same period of the previous year. The share of the expired credits decreased to 24.7% at the end of the period compared to 30.4% of the first 9 months of the previous year and 27.6% of the beginning of the year. The amount of the long-term credits increased by 5.5% and that of the short-term credits increased by 2% compared to the same period of the previous year. The share of the long-term credits in the total credits was 30.2% against 29.5% in the same period of the previous year.

83.5% of the credits were accrued by the banks and 16.5% of these were accrued by the other credit organisations.

The percentage of the credits had been slightly decreased by the end of the report period. This was related to the radical banking reforms resulted in the expansion of their base of the resources increasing the interest of the customers towards the banks. This was also related to the actions performed by The National Bank to improve money supply in the economy. It is beyond doubt that the reduction of the discount rate for the centralized credits had influenced the dynamics of the credit percentage.

During the period the savings were one of the main sources of the credits as well. The savings of physical persons were 688.4 billion manats, which is 29% more than same period of the previous year and 17.6% more than the beginning of the year.

During 9 months the amount of the Short-Term State Loans decreased by 10.5% or 20 billion manats constituting 170.56 billion manats (10.1% of monetary base) in October 1, 2002 and the average profitness of the STSL was 13.12%.

3. Improvement of the monetary management

The institutional improvement of the monetary management. For the successful fulfillment of the duties of the monetary policy the institutional improvement of the monetary management should also be considered.

Much was done to form a perfect research base - one of the most important elements of the monetary management mechanism. Especially complex actions performed to establish the monetary development models. As a result, a modern econometric apparatus of the macroeconomic researchs had been created and a wide implementation of the mathematical-economical methods maintained. The equilibrium models of the inflation and money market have been created and began to be used in the practical implementation of the monetary policy. It allowed to create the long-term economical forecasts by the use of the established models.

The system was created to monitor and analyze the processes in the international markets, as well as the inclination of growth in the world economy under the conditions of globalisation of the world economy. This establishes a favorable condition for the study of the influence channels of the world economy to the national economy, as well as macroeconomic aspects of the republics' integration to the global economy.

Variety of researches has been performed to create the modeled criterions and variants for the choice of the appropriate tools of the monetary regulation corresponding to the economical situation according to the inclinations of the development of the financial markets. Moreover, the base of the information processing and processing the forecasts of the short- and long-term monetary indicators were created and brought to the world standards in the monetary research and forecast sphere.

The important actions were performed for the establishment of the complete information database to guarantee an effective monetary management. The statistical database on processes in the economy of the world, as well as the CIS region and the country was enriched. Works within the frame of the project of the Automated Bank Statistical Accounts Systems completed. Besides, several documents as the procedure rules, methodical fundamentals were prepared

within the boundaries of the creation of the normative-methodological base for the collection, processing and transmitting of the statistical information.

The tools of the monetary policy. The National Bank has regulated the money market by participating at the credit auctions, securities and money market, as well as by the obligatory reserve norms during the report period.

The National Bank performed the refinance of the commercial banks on the ground of auctions upon the centralized credits.

By the decision of the Management Committee of the National Bank the discount rate of the centralized credits was lowered from 10% to 7% since September 16, 2002, with the aim of the implementation of the 5th item of the decree of the President of the Azerbaijan Republic number 783 “About additional measures in the sphere of the governmental protection on the development of the **proprietary** in the Azerbaijan Republic” dated September 10, 2002.

The obligatory reserve norms both for manat as well as currency were 10% during 9 month period of the year 2002. The implementation of the practice to join obligatory reserve norms with correspondent accounts began.

The actions for the realization of the strategy to set the open market operations as a main means of monetary policy also proceeded during 9 months of 2002. The participation of the National Bank in the market of the STSL (short-term state loans) aimed to regulate the short-term liquidity in the banking system. The National Bank performed the REPO and the reverse REPO operations depending on the liquidity of the banking system.

4. Currency market and monetary policy

Exchange rate policy. The alteration of the exchange rate of the national currency at the regime of the floating rates proceeded during 9 months of 2002 as well. During the period the exchange rate of manat against USD changed by 2.6% or 122 manats and by the end of the third quarter 1USD was equal to 4897 manats.

Situation on the currency market. The gross amount of the internal currency market increased by 210.4 million USD or 13.9% constituting 1.7 billion USD during 9 months of 2002 compared to the same period of the previous year.

The National Bank maintained balance in the currency market by the regulation of the demand and supply, and had the influence on exchange rate of manat. During the report period the sales of the National Bank were 260.2 million USD, purchases were 289.7 million USD in the internal currency market. The National Bank’s exact interference to the currency market amounted to 53.2 million USD (3.1%) and was purchase oriented.

Currency reserves. During the report period the amount of the official currency reserves exceeded the forecasted amount by 3% constituting 719.7 million USD by the end of the report period. The strategic currency reserves of the country had already exceeded 1.3 billion USD.