

The Global Crisis and the Anti-crisis Policy of the Central Bank of Azerbaijan

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A little more than a year has passed since the time when one of the largest American banks – Lehman Brothers Holdings Inc went bankrupt. Launch of the world financial crisis is namely connected with this event the scope of which may be compared with the Great depression of the 30s of the last century. Only a couple of years ago no one could have even assumed that a local crisis on the market of substandard mortgage loans in the USA would spread over to the entire world financial system and cause threat to crash of banking sectors of many countries. In the course of 2008 total capitalization of world stock markets double decreased, having lost USD 32 trillion, write-off by the banks of loan losses and in connection with revaluation of market portfolio made USD 2,8 trillion¹, and market value of the largest banks of just 10 leading countries of the world decreased by USD 1,5 trillion in 2008². Net flow of capital to developing countries and market economies under construction decreased from peak USD 697 bln in 2007 to USD 130 bln in 2008. It is expected that according to the results of 2009 there will be net outflow of capital from these countries (-USD 53 bln). Impact of the crisis on production and international trade was considerably hard which are going through the most significant downturn since the World War II. According to the evaluations of IMF³ in 2009 the world economy is going through downturn (by 1,1%) whereas in 2006 – 2007 its annual growth exceeded 5%. The crisis will touch more developed countries particularly hard where forecast of production downturn is by 3,4%. Volume of the world international trade will decrease by 11,9%. The global crisis gives rise to review principles of regulation of financial markets and financial institutions, discuss their efficiency. It is obvious that

the approaches used failed to prevent destabilization of the world financial system which challenges effectiveness of traditional methods of regulation and actualizes their reformation. Crucial part of this work is elaboration of new principles of activities of central banks taking into account their performance during crisis.

Key problems of anti-crisis policy

Financial crises are not rare. According to estimations of IMF experts⁴ there were 208 currency crises, 124 banking crises, 80 crises of sovereign debt and 52 complex crises incorporating some of its types in the world from 1970 through 2007. However, the current crisis has a number of distinctive features. We are talking not only about scales of the crisis, but also about its reasons and manifestations. As an important characteristic feature of the current crisis one may mention its end-to-end character, as well as both its occurrence and mechanisms of spread are in financial sphere. Besides, unlike, for instance, the international crisis of 1997 – 1998 it arose not in developing countries but in the country that was considered to be the world financial leader, - the United States of America.

These are key reasons of the current crisis:

global disbalance of savings and expenses, shaped as a result of “overheat” of demand in the leading countries, particularly in the USA. Considerably soft monetary policy and low interest rates in these countries mainly favored formation of such disbalances;

globalization of financial markets that led to growth of potential of mutual “contamination” by financial crises, growth of their reflectivity;

financial innovations and growth of transactions with virtual assets – derivatives, under the conditions of deregulation of financial markets;

informational asymmetry, non-transparency of financial tools and markets;

inefficient regulation of financial system, underestimation of risks by regulators and pro-cyclicality of their actions.

Anti-crisis measures, carried out by governments and central banks have taken unprecedented scales. Thus, in the countries of “top twenty” total size of such measures equal to 28% of annual GDP⁵. Today reassuring is

that due to mass support of financial sector (liquidity injections, recapitalization of banks, state guarantees on loans, and additional measures on insuring deposits etc) financial system is gradually recovering.

However, even preliminary results of the crisis clearly display that the scales of its consequences multiply exceed “the value” of prevention of crisis manifestations. It means that in future both macro economical policy and the policy of financial regulation should be re-directed at prevention of conditions for crisis development.

In parallel with measures to overcome the current crisis, governments and central banks are busy with establishment of principles of economical policy which would allow to overcome occurrence of such challenges in future. Particularly, suggestions on transfer to macro-prudential regulation targeted at provision of stability not of separate institutions but of the financial system as a whole seem perspective. To this extent, close integration of tasks of macro-economic management and financial regulation is required. Thus, classic mode of inflation targeting may be supplemented by the assignment of testing of overall level of prices (i.e. process for goods and assets). According to the concept, it should help central banks clearly track the level of economy overheat and timely respond to manifestations of speculative financial boom. Considerable attention should be paid to timely identifying systemic risks and preventing their dangerous accumulation. Solution of such a task requires differentiation of requirements to separate institutions taking into account their systemic importance. Prudential regulation should obtain dynamic measurement. Particularly, it is expedient to transfer from “point” evaluation of risks to their evaluation by overall economic cycle.

One may assume that a model of the central bank of the anti-crisis future – is a model based upon two-tier monetary policy. Tier 1 should comprise classic tools of the policy, directed at maintenance of stability not only of consumer prices, but also overall level of prices in economy. Tier II will be presented by mechanisms of counter cyclic macro prudential regulation. The bottom of such mechanisms is in establishment of sufficient capital and mandatory reserves by central banks that restrain undue expansion of

banks during economic booms. It means that a central bank should “go against wind”, herewith “wind” is strong economic growth.

Such a mechanism will primarily comprise three regulating principles:

capital adequacy: during boom banks should maintain more capital – efforts of asset expansion will be without fail accompanied by adequate capital growth, that is a restraining financial buffer against pro-cyclical growth of banks;

level of lending leverage –limiting of debt funds in the structure of bank liabilities;

provisioning: loan reserves collected during boom may serve as a financial buffer during downturns when portfolio deteriorates and banks suffer losses.

However, many experts doubt about compliance of existing standards of Basel II to these principles. It is obvious that these standards will have to be seriously reviewed in the nearest future.

Sensitivity of Azerbaijani economy to the global crisis

Overall characteristics of the economy of Azerbaijan determine its high sensitivity to external shocks. This is, first of all, connected with high share of oil-gas sector, which in 2006 – 2008 took over 60% of GDP. High level of financial liberalization in 2007 is an additional factor. Azerbaijan lifted restrictions on across-the-border operations with capital. Taking into account macroeconomic risks our government pursues the policy aimed at combination of dynamic growth with careful macroeconomic policy. In terms of this, in the period of comparatively high oil prices Azerbaijan had considerable profit of the account of current operations (in 2008 its volume constituted 36% of GDP) and budget profit (in 2008 consolidated budget was implemented through 19% of GDP and 48% of non-oil GDP). The State Oil Fund (SOF) became a crucial tool to provide long-term macroeconomic stability where all revenues of the country from hydrocarbon extraction flow within the framework of production sharing contracts. By the yearend of 2008 resources of the SOF amounted to USD 11,2 bln, and gold and foreign exchange reserves of the country amounted

to USD 8,2 bln (which is equivalent to 26 months of import). National debt at that moment constituted USD 3 bln, gross external debt of the country equaled to USD 9,3 bln (20% of GDP). Primary channel of the global crisis transmission to the economy of Azerbaijan was sharp decrease of oil prices in H2 of 2008. Decrease of world prices told on export of other fields (mainly, metallurgy, chemical industry). As a result in H1 of 2009 total volume of export decreased three times as much as compared with the similar period of the previous year. Moreover, external refinancing of banks sharply reduced.

The global crisis as well amplified impact of psychological factors on the status of economy. On the first place it concerned the currency market and the banking sector – *in Q1 of 2009 after a series of devaluations in neighboring countries demand for cash dollars sharply increased, deposits money supply growth rates went down.*

The scope and specifics of the current global crisis required adoption of non-standard decisions within the framework of monetary policy. To this extent, amendments made to the Law on the Central Bank of Azerbaijan quite corresponded to the spirit of global tendencies in legislations of central banks. According to adopted amendments, the Central Bank of Azerbaijan has the right to issue loans to banks as Lender of Last Resort for longer terms and in various currencies. In order to capitalize creditworthy banks encountering temporary challenges the Central Bank is entitled to grant them subordinated loans.

Key goals of the policy of the Central Bank of Azerbaijan in the crisis included were to provide the financial sector with liquidity, support cumulative demand, maintain stability of the financial sector. To this extent a wide range of measures was applied enumerated in Annex.

Since the end of 2008 the Central Bank of Azerbaijan has 6 times changed refinancing rate and borders of the corridor on operations on the open market in a declining manner. As a result, refinancing rate was decreased from 15% in 2008 to 2% today, corridor ceiling respectively from 20% to 7%, balance requirements of the Central Bank of Azerbaijan to banks from the beginning of the year up to now have increased by 20 times as much. Mandatory reserve norms on internal sources of funds attraction were decreased from 12% to 0,5%, and on external sources of attracted they are cancelled at all. Along with this, in order to diminish burdens of mandatory reserves maintenance, reporting period of averaging on mandatory reserves was prolonged from 15 days up to 1 month.

As a result, from October 2008 to the end of August 2009 *net volume of "injections" of liquidity* to the economy constituted about USD 2 bln. Of this amount banks, only through reduction of mandatory reserves, received over USD 730 mln, activation of discount window of the Central Bank was mainly oriented at maintenance of liquidity of system forming entities (e.g. the State Oil Fund) and banks (mainly for timely servicing of external debts).

The Mortgage Fund resumed its activity, which immediately told on stabilization of prices on the real estate market and expansion of activity on this market. Thus, in the course of two months of the Mortgage Fund functioning prices for real estate on a secondary market stabilized and even increased by 1,3%. Prices stabilization is of crucial importance for financial condition of the banking sector, since real estate is key in collateralization of about half of the credit portfolio of banks. Increase of activity of the real estate market is as well accompanied with reduction of terms of real estate sales and growth of its liquidity.

Exchange Rate Policy

Notwithstanding crisis manifestations on currency markets of the countries – trade partners of Azerbaijan, exchange rate of manat to the US dollar is

stable up today. According to the results of nine months of 2009 it fell in price against the US dollar only by 0,3%.

As in many countries with developing financial markets and specific structural features of the economy, exchange rate of manat against the US dollar is “nominal anchor” of maintaining macroeconomic stability in Azerbaijan. In other words, amidst all possible interim monetary indicators exchange rate of the manat is a more controllable and predictable benchmark to achieve final targets of monetary policy – stabilization of prices and financial system. In total, considered is that one of the following three indicators may be chosen as a champion of monetary policy – exchange rate, money supply and interest rate. It is impossible to simultaneously target all three indicators. Fixed exchange rate in such a case does not allow the central bank operate with interest rate. Moreover, according to Mundell - Fleming model, when transmitting to the system of floating exchange rates in highly mobile international capital flow environment effectiveness of fiscal policy as a macroeconomic regulator considerably diminishes. If such a case, monetary policy becomes the most effective tool to affect the level of output and employment in economy.

As monetization of GDP grows, financial markets deepen and complicate, capital market increases and structural distortions in transition economy are eliminated, demand for money becomes unstable and interest rate starts to act as a key benchmark for players of economic activity. Fixed exchange rate in such a case does not allow the central bank to handle interest rate.

Proceeding from the above, the Central Bank of Azerbaijan being guided by the principle of evolutionary modification of the monetary policy mode, de-facto pursues exchange rate policy in the mode of binding to the US dollar, though de-jure operational benchmark is currency basket comprising the US dollar and EURO. There are serious foundations for this. The point is that the year of 2009 proved out to be the period when excess volatility of the manat could have destabilized the financial sector. Standard use of the currency basket implies synchronization of the exchange rate of manat to the US dollar and EURO cross exchange rate of the dollar moving to EURO. Such a policy allows central banks gradually

reject unilateral fixation of the exchange rate to the dollar, attach flexibility to the exchange rate and smoothly switch to other monetary benchmarks (first of all to interest rate on interbank market). However, it requires relevant environment in the economy.

Decision on maintenance of stability of the exchange rate was taken on the basis of the analysis of the bunch of complex of macroeconomic factors. The following arguments were for devaluation of the manat.

1. It would allow improve foreign trade balance in the environment of price fall for export goods.
2. Protection of de-facto fixed exchange rate leads to significant losses of gold and foreign exchange reserves.
3. Devaluation of the monetary unit allows exporters obtain additional liquidity.

On the other hand, there were serious arguments to the favor of maintenance of stability of exchange rate.

1. Balance of payments – primary monetary basis for stabilization of exchange rate – is still favorable in Azerbaijan and issues no foundations for devaluation. Foreign exchange reserves in such a case fully cover money supply in national currency. The countries that encounter upward deficit of the balance of payments and danger of full loss of foreign exchange reserves employ devaluation.
2. Amidst reduction of global demand and shrinkage of foreign markets, positive effect of devaluation on export may prove out to be limited. As for the task of suppression of import, its volume in non-oil sector slightly decreased even without devaluation.
3. Devaluation will not promote quick import substitution due to restrictions of unloaded production capacity.
4. Amidst high specific weight of accessories, materials and semi-finished products in local production (according to some researches, 40% - 60% depending on fields of industry), devaluation of manat may undermine their foreign competitiveness.
5. Devaluation might result in rise in inflation and as a result decrease of real value of assets and savings, impoverishment of the population.

6. At current scale of dollarization of loans (46%) two thirds of loans in dollar have been issued to the sectors of economy that do not generate income in foreign currency. Consequently, devaluation could impact financial condition of these sectors, causing sharp deterioration of their capacity to repay bank loans.
7. Sharp devaluation could lead to panic among the population and sharp outflow of resources from banks, seriously worsening the problem of liquidity. At the same time, smooth devaluation could strengthen uncertainty, provoking dollarization and further pressure on currency reserves.
8. Devaluation would increase expenses on servicing external foreign currency debt and debt burden of banks.

Meanwhile on its long run, the Central Bank of Azerbaijan is aimed at gradual transition to flexible exchange rate mode. It is non-exceptional that during post-crisis period flows of foreign capital and export oil revenues will rise. It may be fraught with overheat of economy due to growth of money emission in fixed exchange rate environment. That's why, flexibility of exchange rate policy is crucial in long run for concentration of monetary policy to achieve target indicators of inflation.

Situation in Banking Sector

Since before the crisis bank regulation was triggered against excess overheat of the sector. Thus, there was set mandatory reserve norm on external borrowings of banks at 5% level. And capital adequacy (sufficiency) till the crisis (launch of 2008) constituted 19,6%, that considerably exceeded established minimum level (8%). Till the crisis aggravation, the Central Bank thoroughly prepared banks for all possible shocks carrying out measures on additional "financial immunization" of the system. Prudential limits were established so that to maintain sufficient liquidity and new provisioning was created to cover potentially problem loans.

Toughened were conditions of assets classification, increased was the ratio of collateral value to loan amount. In order to regulate credit risks there

were reviewed and toughened norms of risks per one borrower, terms of loans underwriting. Special attention was paid to minimization of currency risks assumed by banks. Simultaneously there were strengthened requirements on the level of data disclosure and overcome of informational asymmetry.

At the height of the global crisis for the purpose of further capitalization of banks and insurance entities through internal resources a decision was taken to exempt a portion of income directed at capitalization from taxation. In order to protect interests of depositors and stimulate flow of deposits to the banking sector maximum volume of deposit liable to state insurance was increased by 5 times. Simultaneously softened were conditions restricting insurance of deposits.

All these measures strengthened financial stability of the banking sector. Thus, liquidity of the banking sector today is very high, instant liquidity is 80% whereas established minimum norm is 30%. Long-term liquidity is favorable as well – difference between assets and liabilities of banks with 180 to 365 day maturity is positive and presently it takes +2% of the volume of assets. Capital adequacy is 19%. Share of overdue loans in the credit portfolio is comparatively low (4%). At the same time loan provisioning of banks makes 70% of the amount of overdue loans. Banks capital is stably growing in the course of 2009 and since the year launch growth was 11%. Financial results of banks activities are positive as well – ROA was 2,9% and ROE was 19,8% according to the results of nine months.

The results of stress-tests conducted by the Central Bank showed that even at unfavorable scenarios of development of macroeconomic situation the banking sector is capable to overcome hard shocks and absorb losses resulting from this. It is put down to the fact that most part of potential risks has already been admitted by banks and adequate reserves were created for their neutralization.

Currently, the situation in the banking sector is changing for better as compared with Q1 of 2009. Deposits of the population have been not only restored, but also demonstrate growth: according to the results of 9 months by 9,6%. At that large (in Q1 increased by 19%) and time deposits (growth of term deposits within 9 months was 17,2%) grow. Credit portfolio is

resuming its growth as well, from April through September of 2009 credit portfolio of banks increased by 26%, as a whole assets increased by 4,8% within this period. External financing of banks is being resumed as well, within 9 months banks attracted external borrowings amounting to about USD 716 mln.

Table

Key indicators of the banking sector in 2009, in %

	Q1	Q2	Q3
Assets (change against the previous quarter)	-14,2	4,3	17,2
Capital (change against the previous quarter)	4,4	6,0	3,6
Loans to economy (change against the previous quarter)	-14,0	4,1	20,9
Deposits of the population (change against the previous quarter)	-6,9	9,1	9,6
Instant liquidity	66,8	67,2	76,6
Share of overdue loans in portfolio	3,16	3,77	3,98
Capital adequacy (sufficiency)	19,2	19,5	19,4

The new qualitative tendency in the banking sector is the growth of micro financing. Its key advantages are high profitability, considerably low risk, expansion of industry coverage both from geographical standpoint and from the standpoint of client base. Micro financing is of crucial macroeconomic importance, employment of the population especially in rural areas increases.

Despite the global crisis, the Central Bank is as well continuing realization of big projects of national importance. At the initiative of the Central Bank a new phase of development of payment system is being realized that is unique both for its scale and economic importance. In the nearest future the population will have an opportunity to pay for all utility services through Internet without going out. Another not less ambitious project is launch of infrastructure of postal – banking system. Over 1500 post offices

throughout the country will provide the population with financial – banking services.

Results of anti crisis measures

Starting with Q2 of 2009 the situation in the economy of Azerbaijan stabilized. Economic growth in the country is continuing, growth rate of GDP constituted 6,1%, including 0,8% in non-oil sector of economy according to the results of nine months. Business confidence Index, calculated by the Central Bank, has been increasing within the latest months. For economy it means restoration of sales of goods of long run, reduction of collected warehouse reserves of unrealized production as a result of demand revival, restoration of growth of production in a number of non-oil export oriented fields, growth of optimism among producers and sellers.

It is particularly important to mention that balance of payments and strategic (international) reserves look encouraging - the country has sufficient safety cushion to maintain macroeconomic stability: as of 1 October 2009 currency reserves of the country constituted USD 18,6 bln, nearly the level of the year launch. It is sufficient to finance import of goods and services in the course of 24 months established minimum norm in international practice being 3 months. The Foreign Exchange market is currently in equilibrium, demand for currency stabilized (the Central Bank intervention in August was even positive).

Money supply, one of the key factors to maintain demand and economic growth, has commenced growing anew since Q2, just in August increase of monetary aggregate M2 constituted 4,8%. With growth of money resumed average interest rates on loans in manat decreased to 14,6% in September. In September deflation changed into inflation (0,4%), and base inflation seceded from negative to positive zone, that is the indicator of demand revival in economy. At that average annual inflation is still low (only 2,1%). Real effective exchange rate of manat decreased within nine months by 3,1%, which is primarily connected with high inflation in the countries – trade partners.

If to sum, economic diagnosis is thus according to the results of 7 months of 2009: macroeconomic stability in the country is rather high – it is first of all strengthened through solid foreign exchange reserves, just these reserves guaranteed soundness of the state budget and partially compensated reduction of external sources of liquidity in economy. Economic growth and employment as a whole were protected from fatal impact of the global crisis, within the last two months of the current year observed is revival of demand in the economy, balance of payments is improving anew, foreign exchange market and channels of money supply are being stabilized under the influence of anti crisis monetary policy.

Strategy for a Way out of the Crisis

As is noted in October report of IMF on global financial stability⁶, time for full cancellation of all taken non-traditional measures has not come yet. Moreover, in some countries some additional government resources may be required. True, the report as well says that “it is high time for directive authorities to consider how and in which sequence such measures should be wrapped up.”

That’s why, the Central Bank of Azerbaijan will carefully track the situation in money supply channels and in case of necessity to provide liquidity first of all to all system-forming banks and entities. Certainly, our key priority is still to maintain stability of prices at 3 – 5% level within its authorities. To achieve this goal doubtless, stability of exchange rate of manat will be key interim target of the Central Bank. *It should be once more noted that exchange rate stability in Azerbaijan is the anchor of macroeconomic stability, and namely the guarantor of low inflation, maintenance of the level of real income of the population, financial stability.*

Moreover, clear formulation of “the strategy out” will also be focused on. The philosophy of the package of financial stimuli realized during crises is in temporary purchase of assets by the government. After recession the assets are sold and the Central Bank resumes status quo. In post-crisis period the state budget should be discharged. Governments fail to cut and contrive having high budget deficit. Though it is admitted that it does not

concern the countries that originally had low volumes of budget deficit and national debt against GDP.

In 2010 there will be endured efforts on strengthening institutional base to introduce in future mechanisms of targeting level of prices in economy new global realities being considered.

Amid improvement of the balance of payments, "the strategy out" of the Central Bank will comprise gradual switch of monetary policy to employment of classic instruments. Interbank monetary market development acceleration is on focus as well.

As is noted by IMF, "...combination of pro-cyclicality of carried out micro-prudential and macroeconomic policy led to growth of the share of borrowings and increase of systemic risk." That's why, full-scale introduction of counter cyclic measures should become one of the key priorities of banking regulation. Currently the Bank is actively studying the method of counter cyclic regulation, implying grade up of the norm of creation of reserves in the course of growth, securing insurance of risks during downturn. *Further capitalization, consolidation and institutional development of banks and reform regarding small financial institutions* are utterly crucial.

In conclusion I would like to cite President of the Republic of Azerbaijan. Addressing one of the recent meetings, he mentioned that, *Azerbaijan is the country that was least affected by the crisis*. Indeed, many countries may envy resource of soundness of the economy of our country. Soundness of economic situation in Azerbaijan has been secured through thought-out economic policy pursued under the leadership of the President of the country. Boosted economic growth within the last years, creation of foreign exchange reserves keeping pace with the size of economy and reserved debt policy became guarantors of financial soundness of the economy, as a result of which the country was safely prepared for the global crisis. It refers both to the economy as a whole, and to its financial – banking sector.

Annex

Government	Central Bank
<p>1. Authorized capital of the State Oil Company of the Azerbaijan Republic (SOCAR) was increased by the government by the amount of AZN 600 mln.</p> <p>2. From the reserve fund of the state budget was allocated AZN 50,2 mln with the purpose to increase share of the government in the authorized capital of OJSC International Bank of Azerbaijan.</p> <p>3. From 1 January 2009 income of banks, insurance and reinsurance companies, directed at increase of authorized capital, is exempted from taxation for 3 years.</p> <p>4. The Ministry of Taxes took a decision to suspend (production enterprises, retail traders and services, wedding houses) selective tax inspections and reviews of taxpayers under</p>	<p>1. <u>14 October 2008:</u></p> <p>1.1. Refinancing rate decreased from 15% to 12%.</p> <p>1.2. Corridor ceiling decreased from 20% to 17%;</p> <p>1.3. Norms on mandatory reserves on liabilities in national and foreign currencies decreased from 12% to 9 %. Thereby liquid funds of the banking sector increased by AZN 220 mln.</p> <p>1.4. Average term of maintaining the level of mandatory reserves on liabilities in national and foreign currencies increased up to 1 month.</p> <p>2. <u>31 October 2008</u></p> <p>2.1. Refinancing rate decreased from 12% to 10%.</p> <p>2.1. Corridor ceiling decreased to 15%, corridor floor – 1%.</p> <p>3. <u>1 December 2008</u></p> <p>3.1. Refinancing rate decreased from 10% to 8%.</p> <p>3.2. Corridor ceiling decreased to 13%.</p> <p>3.3. Decreased are norms of mandatory reserves on liabilities in national and foreign currencies from 9% to 6%. Thereby liquid funds of the banking sector increased by AZN 125 mln.</p> <p>4. <u>1 February 2009</u></p> <p>4.1. Refinancing rate decreased to 5%.</p> <p>4.2. Corridor ceiling decreased to 10%.</p> <p>4.3. Decreased are norms of mandatory reserves on liabilities in national and foreign currencies from 6% to 3%. Thereby liquid funds of the banking sector increased by AZN 135 mln.</p> <p>5. <u>10 February 2009</u></p> <p>5.1. Central Bank launched SWAP operations.</p> <p>6. <u>2 March 2009</u></p> <p>6.1. Refinancing rate and corridor ceiling decreased respectively to 3% and 8%.</p> <p>6.2. . Decreased are norms of mandatory reserves on liabilities in national and foreign currencies from 3% to 0,5%. Thereby liquid funds of the banking sector increased by AZN 111 mln.</p> <p>7. <u>25 May 2009</u></p>

<p>timekeeping method to the end of this year.</p> <p>5. From 1 May 2009 resumed was VAT for import of wheat and grain. The Ministry for Emergency Situations is as well planning to launch the fund of grain and purchase of grain from farmers in the volume of 260 thousand ton grain.</p> <p>6. Expanded is activity of the Azerbaijan Investment Company as well as activated is lending to entrepreneurs by the National Fund of Assistance to Entrepreneurs. Advantage is issued to small loans. The Government has been given proposals on procedural improvements.</p> <p>7. Income tax rate decreased from 22% to 20%. Adopted are Amendments to the Tax Code, specifying review of other tax rates. Prolonged are tax remissions to the agrarian sector.</p> <p>8. Draft Code on Competitiveness</p>	<p>7.1. Refinancing rate and corridor ceiling decreased respectively to 2% and 7%.</p> <p>8. Activated are Central Bank operations on refinancing of the banking sector. For 7 months of 2009 credit portfolio of the CBA increased 3,5 times as much.</p> <p>9. 9 July 2009 amendments to the Law on the Central Bank of Azerbaijan</p>
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<p>delivered to the Parliament; adopted is the Law on Specific Economic Zones.</p> <p>9. President of the Republic signed Decree on “Combating Corruption at Handling State and Municipal Property.”</p>	<p>the Republic of Azerbaijan took effect through Decree of the President of Azerbaijan, that enhances flexibility of monetary policy of the CBA and the policy of regulation of the banking sector. On the basis of the amendments in question the Central Bank is entitled to issue loans in various currencies and for longer periods, including subordinated loans. At the same time CBA, in order to maintain the real sector, is entitled to issue loans to banks on the basis of the governmental guarantees.</p> <p>10. On the basis of legislative amendments of 28 June 2009 approved are “Regulations on issuing loans to banks by CBA”. The Regulations reflect questions on realization of monetary policy, maintenance of financial stability, regulation of problems of capital adequacy, as well as terms of granting of loans for state projects financing.</p> <p>11. Increased are reserve norms on assets group:</p> <p>11.1. on watch loans – from 6% to 10% (30.04.08)</p> <p>11.2. on non-satisfactory loans – from 25% to 30% (30.04.08)</p> <p>11.3. on doubtful loans – from 50% to 60% (30.04.08)</p> <p>12. Requirements on collateralization increased from 120% to 150% (30.04.08)</p> <p>13. limited is the share of subordinated debt in total capital (18.02.08).</p> <p>13.1. Maximum amount of subordinated debt is set within 50% of Tier I Capital.</p> <p>14. Risk level of mortgage loans increased from 50% to 100% (18.02.08).</p> <p>15. According to changes made to “Regulations on issuing loans to banks” increased are requirements to control over the quality of credit portfolio, monitoring of the borrower activity, evaluation of financial standing of the borrower and his/her creditability (18.11.08).</p> <p>16. Improved is the methodology of calculation of open currency position, including exactly identified off-balance accounts to be included to currency position, included are operations with precious metals. (17.02.08)</p>
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	<p>17. On the basis of additions made to “Regulations of Suspension of Interest Accruals on credit operations”, sequence on repayment of non-accrual debts, has been adjusted. (17.12.08).</p> <p>18. Provided is flexibility in limiting of annual interest rate on insured deposits. Maximum amount of insured deposits increased from AZN 6000 to 30.000 (08.05.09). Deposits with up to 15% interest rate are included to the insurance system (10.06.08).</p> <p>19. 0 risk level is established on securities issued by the Mortgage Fund under the Central Bank of Azerbaijan (17.06.09).</p> <p>20. On 7 August 2009 President of Azerbaijan signed Decree on “Order of the Governmental Participation in banks and non-banking credit institutions, in whose authorized capital there are shares owned by the state” implying enhancement of supervision of financial institutions.</p> <p>21. Banks improved risk management system. With this purpose on the basis of specific methodology enhanced is risk monitoring, established are ratings of evaluations of risk management, prepared is plan of measures on elimination of weaknesses and launched is the process of their realization. At the initiative of the Central Bank from June 2009 resumed was mortgage lending. Mortgage lending activated spheres like construction, banking, insurance, valuation activities, notary and real estate registration services, economically activated securities market and stabilized prices at the real estate market. Price stabilization, in its turn, prevented devaluation of bank lending collateralization.</p>
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