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Ulviyya Azizaga Garazade
Baku State University
master
ulviyye.qarazade@gmail.com

LEGAL ASPECTS OF THE IMPACT OF THE FINANCIAL CRISIS ON THE ACTIVITIES OF CREDIT ORGANIZATIONS

Summary

The current article examines the legal aspects of solving the problems caused by the financial crisis and the impact of the financial crisis on the activities of credit institutions. The study focuses on the theoretical and legal basis of the financial crisis, analyzes the negative impact of the crisis on the banking sector, draws conclusions and analyzes the current situation in the sector.

Key words: *financial crisis, credit organizations, legal aspects, impact, financial stability, risk*

Introduction

The importance of legal measures increases especially in the event of a possible financial crisis in the economy when the monetary tension of the various links of the financial system and the impact on the system increases.

The legal status of credit organizations, the procedure for the creation and termination of the activities of credit and financial institutions are determined by the formation of banking legislation that is taking place under the steady influence of the economic needs of society and various sectors of the economy. The state strives for stability in the credit and banking system to ensure the stability of the economy as a result of the financial crisis. Reforms in the financial and banking sector, organization of credit and financial relations and legal regulation of its activities, legal means to prevent financial crises in terms of improving financial control are based on determining the legal status of legal entities and legal regulation of their activities.

Credit organizations. The banking system is a vast concept and a group or network of institutions that provide financial services. Banking legislation as a branch of law is included in the unified financial system of Azerbaijan law and, in turn, is a system of legal regulation of credit institutions, taking into account the standards and regulations developed within the framework of international cooperation.

According to of the Law of the Republic of Azerbaijan on Banks states: The banking system of Azerbaijan consists of the Central Bank of Azerbaijan and credit organizations. The country has a two-stage developed banking system based on market principles (the first stage is the Central Bank of the Azerbaijan, the second — commercial and other non-Bank credit institutions). Credit organization is bank, a local branch of foreign bank or a non-bank credit institution. Bank is legal entity, that attracts deposits and other returnable funds from individuals and legal entities, issues loans on its behalf and from its own funds, as well as makes transfers and cash settlements in aggregate at a client’s request. Non-bank credit institution is legal entity that has the status of a non-bank credit institution under the law. (1) According to the Law of the Republic of Azerbaijan on Non-banks, non-bank credit organization (hereinafter - NBCO) is a specialized credit organization that provides loans on the basis of a special agreement (license) and carries out other activities provided by this Law. (2) According to the Law of the Republic of Azerbaijan on credit unions, a credit union is a non-bank credit organization created by individuals and (or) legal entities that are small business entities for voluntary consolidation on the basis of common interests for mutual lending by accumulating free funds. (3)

In recent years, banks in many countries around the world have gone bankrupt, and global instability in financial institutions and money markets has led to widespread banking crises. World experience shows that the instability of the banking system can lead to serious economic shocks in the form of a drop in economic growth, an increase in unemployment, and acceleration of inflationary processes.

Financial crisis and its impact on credit organizations. Crisis defined as a short period of unexpected and notably unfavorable shift in the external environment that organizations face. (9, p 687) In the another article is defined as a high impact event that affects organizations’ viability and implies the need to make decisions quickly (7, p 61) The cause of the crisis - is the emergence of crisis symptoms, which are reflected in events and incidents, their qualities and crisis factors. (5, p 10) The stages of the crisis can be defined as symptoms (is manifestation of the "disease" of the organization, as well as "disease" reveals the causes of the crisis), reasons (inflation, large credit expansion, deterioration of trade conditions, liberalization of financial markets) and factors (increasing financial problems, increasing large debt on loans).

The financial crisis can be understood as a crisis threat that needs to be predicted. The consequences of the crisis can be both reversible and irreversible in terms of quantity and quality, which leads to significant changes in the development of the organization, as well as new opportunities for long and short-term processes.

The financial crises as type of economic crisis should be distinguished from economic crises in the real sector, as their root causes and social consequences are different. However, the main difference between the financial sector and the real sector is that in the real sector transactions, both parties win - the producer, the consumer, the buyer and the seller.

The actual economic and financial crisis has conditioned the environment from 2008 to present. The main characteristics of the economic and financial crisis are: reduction in credit available, reduction and price conscious consumer spending, increase in unemployment, significant move towards establishing cost efficiencies within the corporations, reduction in shareholder strategic development processes and return on investments (8, p 281-296). We can conclude that events like the economic and financial crisis strongly affected performance of credit organizations as an uncontrolled input.

There are three main types of financial crises: currency crises (also called money crises), debt crises, and systemic banking crises. Sometimes a fourth is added to this list - the effect of "sudden stop".

•***Currency crisis*** - is defined as a stressful situation in the economy caused by a sharp increase in demand for foreign currency.

•***Debt crisis*** - is a situation when a country is unable (or unwilling) to repay its foreign or domestic debts.

•***Systemic banking crisis*** - is a stressful situation accompanied by processes such as “bank anxiety” (sudden customer flows to withdraw deposits from banks), systemically significant losses, insolvency and bank liquidations, as well as “rescue packages”. In many cases, this type of financial crisis is accompanied by the following measures:

- purchase of significant assets (at least 5% of GDP);
- application of significant guarantees;
- extensive liquidity support (deposits of non-residents and liabilities to them in the amount of 5% and more);
- significant bank nationalizations;
- freezing of deposits and bank strikes (temporary suspension of banks);
- bank restructuring costs (at least 3% of GDP). (6, p 431)

Although the consequences of each of these factors has had a serious impact on the monetary system as a whole, increasing the risk of crisis, weakening of economic dynamics, allowing economic downturns, resulting in different trends in the country's national economic development.

In order to detect a banking crisis, the risks that can cause a banking crisis must first be identified. There are three main risk factors that can lead to a banking crisis. These include:

- credit risk-this risk arises as a result of untimely or incomplete fulfillment of the borrower's obligations to the bank;
- market risk-this risk arises in connection with changes in market interest rates, exchange rates, the value of securities and commodities;
- liquidity risk-this risk arises as a result of failure to meet planned and unforeseen obligations in a timely and effective manner. (4)

While price and quantity flexibility in financial markets and the consequent acceleration of speculative expansionary trends at the international level, financial markets offer various financial instruments to protect the assets of companies and credit institutions from risks such as exchange rate fluctuations, but do not minimize risks. However, there is a systematic risk increase in doing so.

The nature of banking risks associated with the nature of banking activities is reflected in the payment turnover, which reflects both the production process and the turnover of public goods. In terms of risk in banking, it is very important that the subjects of economic relations adhere to the value ratio, supply and demand ratios. Banking risks are a more social process, and the consequences for banks are more severe when they take risks not only with their own funds, but also with borrowed funds. When a bank fails, not only the bank but also the bank's customers (individuals and legal entities who put money in the bank) lose. Therefore, banking crises can have more serious consequences than production crises. Thus, banking crises are a type of financial crisis that causes numerous financial losses to participants in a chain of monetary obligations.

Banks create a risk management system adequate to the type, volume, nature and environment of their operations, complexity and the risks they face. (4)

The risk management system consists of the following elements:

- risk management strategy and risk appetite declaration;
- organizational structure of risk management;

- risk management policy, including risk management protection lines;
- risk limits;
- risk management for new products and services;
- data review and risk reporting;
- emergency plan. (4)

A stable and efficiently functioning banking sector is a key factor in intensive economic growth, which is especially important for Azerbaijan in the light of its task to increase the competitiveness of the economy. For this reason, it may lose its balance by failing to demonstrate high resilience to a financial crisis that reflects risk management objectives and does not have the right risk management strategy, organizational structure, risk management policy and process.

The various consequences of the crisis depend not only on its nature, but also on the form of adequate steps in terms of professionalism, responsibility and motivation in the organization of the anti-crisis process. World experience shows that the anti-crisis process is controlled, including two blocks of procedures - anti-crisis management and anti-crisis regulation.

Anti-crisis management - is such management that is aimed at getting the organization out of the crisis situation that has arisen (i.e. management in a crisis), as well as at preventing the manifestations of a crisis situation. Anti-crisis regulation - the impact on the debtor at the macro level, containing measures of organizational, economic and regulatory impact of the state, aimed at protecting organizations from crisis situations, preventing bankruptcy or liquidation in case of ineffectiveness of its further functioning.

There are also regulations in the banking legislation of Azerbaijan as a result of financial crises in credit organizations. According to law of the Republic of Azerbaijan on Banks, an insolvent bank is a bank that has lost or is in danger of losing its solvency, on the basis of which one or more of the grounds specified in articles that resolution of a bank who has lost its solvence of this law have been established and resolution - is the implementation of measures provided for in article that measures of resolution of the insolvent bank of this law by the financial market supervisory authority in order to remove an insolvent bank, including a bank holding company, from the financial market without delay and at the lowest possible cost. Action plan related to the resolution is a document reflecting the method, conditions, term and economic justification of the resolution of the insolvent bank. (1)

Financial crises and financial regulations applied as a solution to these crises are among the most common crisis types and regulations we encounter in practice. We can clearly see this from the crises and regulations applied both in the world and in our country. When we look at the stages of the formation of financial crises, it is seen that the wrong pricing and the lack of regulation come to the fore.

Conclusion. We can conclude that the relationship between financial crises and financial regulation should be established correctly in order to reduce financial vulnerabilities and to prevent financial fluctuations, that is, the causes, consequences and effects of the financial crisis should be reviewed in detail and the most appropriate financial regulations should be applied, so that a similar crisis or similar external crises should not affect our country. New strategic direction and goals and their corresponding strategic initiatives should be rehearsed to ensure that the strategic initiatives will contribute positively to the sustainability of credit sector. Therefore, strategic development processes, as an organizational capability, can only be effective if enacting strategy feedback loop is supported by the rehearsing strategy feedback loop in any circumstance, especially during financial crisis.

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