Journal of Corporate Finance Management and Banking System
ISSN: 2799-1059
Vol : 02 , No. 04 , June-July 2022
http://journal.hmjournals.com/index.php/JCFMBS
DOI: https://doi.org/10.55529/jcfmbs.24.36.39

Comparative Analysis of the Level of Liberality of the Banking System Across Countries

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Received: 28 March 2022 **Accepted:** 13 June 2022 **Published:** 16 July 2022

Abstract: ***The main goal of the study is the creation of an economic model - an index that allows measuring the level of public intervention in the banking system at the global level, taking into account the characteristics of the latest prudential innovations and changes at the modern stage. The regulatory instruments that allow the central banks to conduct regulation in the monetary sphere and which can be fully or partially determined by the central banks have been taken as the aim of the study. The subject of the study is the measurement of government intervention or regulatory intervention in the banking sector.***

Key words: ***Liberalism, Dirigisme, Government Intervention, Central Banks Intervention, Economic Freedom, Banking Regulation, Commercial Banking Regulation.***

1. INTRODUCTION

The subject of the study is the measurement of state intervention or regulatory intervention in the banking sector.
The market-oriented approach to the regulation of the banking system manifested itself for the first time in the Basel Accord (Basel I) developed in 1988. From this historical event, which is considered a leap from the perspective of banking regulation, the banking system regulation enters its evolutionary process and steps towards further perfection with each new Accord. Although each new accord has been subjected to serious modifications, it has almost preserved the basic principles of the previous document. According to the Basel I Accord, international banks of 12 member countries of BIS (Bank for International Settlements) had to maintain their capital at the rate of 8% of their risk-weighted assets starting from 1992 [3]. The main objective of the Basel norms is the formation of capital reserves in proportion to the risks taken by banks. Since the rapid development and complexity of financial markets in a very short period of time after the introduction of regulations resulted in the emergence of more complex financial instruments, the capital adequacy framework established by the Basel I Accord is found to be too simple in the context of mixed transactions.

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Already in 1997, before the application of the Basel I Accords by the G10 and a number of other developing countries, the Basel Committee on Banking Supervision announced its "Basic Principles" containing the minimum requirements for bank supervision. The document also contains guidelines on the powers that the bodies responsible for regulating banks should have. Studies conducted by various international organizations, think-tanks and research institutes on the assessment of the government intervention in various aspects of the economy can be considered preliminary comparative evaluations carried out in this field. “Index of Economic Freedom” prepared jointly by the Heritage Foundation and The Wall Street Journal, "Economic Freedom Index" and "Human Freedom Index" published annually by the Fraser Institute, “Doing Business” of the World Bank (note that the index has been suspended since September 16, 2021 due to the discovery by the Independent Audit of the fact that the data of 2018 and 2020 were distorted by the officials of the World Bank), “The Global Competitiveness Report” of the World Economic Forum, “The Social Progress Index” of the Social Imperative Non-Profit Organization and studies of a number of other organizations in relevant fields can be cited as an example [2]. However, the phenomenon of measuring the level of government intervention in the banking system is not found in any research work.
The horizontal assessment of government intervention in the economy was first conducted by professor N. Muzaffarli at the Institute of Economics of the Azerbaijan National Academy of Sciences. The non-complex mathematical methodology proposed by him is remarkable for its practicality as well as its flexibility. The opportunities allowed by the applied pragmatism led to the wide use of the method proposed by the scientist by other researchers and scientists and helped to determine whether the government intervention is right-wing or left-wing in many different areas of the economy.

2. METHODOLOGY

In the book "Sociality of the Economy in Right-Winged and Left-Winged Systems" published for the first time by Professor N. Muzaffarli in 2014, the scientist put forward the methodology "Index of Leftness (Rightness) of Economy -IL(R)E".
The said index was calculated on the basis of 6 sub-indices listed below [1]:

1. Public finance sub-index (PF);
2. Price adjustment sub-index (PA);
3. Foreign trade sub-index (FT);
4. Licensing sub-index (L);
5. Employment adjustment sub-index (EA);
6. Minimum wage sub-index (MW).

As a follower of this theory, I additionally compiled his own sub-index - the Charter Capital sub-index.
The Charter Capital sub-index (CC) reflects the minimum authorized capital required when obtaining a license to perform banking activities as required by the relevant legislation of the countries. The charter capital requirement can also be evaluated as a mechanism that facilitates or complicates entry into the banking sector. When this demand is high, a decrease in the number of those who want to perform banking activities can be observed, and when it is the opposite, an increase can be observed. However, if we use the authorized capital itself as a number for comparison between countries, this is a gross mistake from an economic point of

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view and may lead to misinterpretations. The fact that this requirement is high in Japan does not at all mean that it is dirigiste compared to Azerbaijan. As Japan has a relatively larger economy, to differ from the requirement of a country with a smaller economy like Azerbaijan is normal. A more realistic and unbiased comparison is possible only after this indicator is corrected for the capacity of the countries' economies.
For this purpose, the charter capital requirement for each country was converted into US dollar equivalent and divided by the country's GDP in US dollar equivalent. This ratio allows for a more realistic comparison between countries by indicating the amount of the minimum authorized capital requirement in relation to GDP. Then the obtained ratio was indexed by the formula

$$\frac{(V_i - V_{max})}{(V_{min} - V_{max})} \quad \textbf{(1)}$$

and the CC sub-index was formed.

3. RESULTS

It is clear that the ratio is a much smaller number compared to GDP. For this purpose Vmax = 0,001 and Vmin = 0 are accepted. Indeed, since some countries do not impose any charter capital requirements for entry into the banking system, the minimum indicator is taken taken as 0 [4].

Table 1. Results of the Charter Capital sub-index.

№	Country	CC Index
1	Japan	0.001
2	Turkiye	0.002
3	Russia	0.003
4	China	0.008
5	India	0.019
6	South Korea	0.039
7	Kazakhstan	0.112
8	Uzbekistan	0.144
9	Azerbaijan	0.538
10	Georgia	0.955

Source: Calculations of the author.

According to our calculations, the most liberal country in terms of the charter capital requirement is Japan and the most dirigiste country is Georgia. The moving average of the sub-index is 0,182. 2 countries are located to the left of the moving average and 8 countries are located to the right. Azerbaijan is one of the 2 countries located to the left of the average with an indicator of 0,538. In other words, it is the second most dirigist among the studied countries. The average value of the sub-index for high-income countries is 0,020, for middle-income countries is 0,041, and for low-income countries is 0,332. Thus, Azerbaijan implements a more left-oriented or dirigiste regulative banking policy.

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Let's note that the charter capital sub-index is only one of the constituent indices of the **Index of Liberalism (Dirigisme) of Banking System – IL(D)BS** which is the final integral index proposed by the author. IL(D)BS is an integral index that reflects the level of modelcreating interventions in the banking system by central banks or other relevant regulatory authorities. Although the index is in its earliest version, it allows to measure the intervention of the state in the monetary system in different countries and future researches in this field will serve to improve the results of the index. Additionally, the results of the index can be integrated into IL(R)E in the future and contribute to the improvement of its results. Final integral index was calculated in the form of the formula

$$\boldsymbol{IL(D)BS = 0,30 \times CC + 0,30 \times RR + 0,20 \times IR + 0,20 \times LR} \quad \textbf{(2).}$$

The charter capital sub-index is given a weight of 30%, which indicates that this sub-index is more important than other indicators. In the Formula RR means – Reserve Requirement ratio, IR means- Interest Rate, LR means-Leverage Ratio. When determining the weights of the final integral index, the practical direct and indirect importance of the sub-indices was taken into account. However, in the future, mathematical optimization of applied weights can be performed if there is access to a large database.

4. LITERATURE

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