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SECTION 31. Economic research, finance, innovation, risk management.

ROLE OF STATE REGULATION IN THE DEVELOPMENT OF THE AZERBAIJAN REPUBLIC STOCK MARKET

Abstract: *The article determines the main problems in this area based on the analysis of the process of formation and development of the stock market of the Azerbaijan Republic which have led to a false front capital market. The author also explores the emergence and development of the stock market in foreign and post-Soviet countries and reveals their distinctive features and defines ways to apply stock market regulation in local conditions in order to increase the effectiveness of the stock market activity in Azerbaijan*

Key words: *Azerbaijan Republic stock market, stock market infrastructure, investment mechanism of the real sector of economy, joint-stock activity, stock market monopolization.*

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Introduction

The stock market is an integral element of the financial system of many advanced economies. It is a means of attracting investment to the 'real' economy of manufacture, production, and service sectors. This financial market mobilizes financial resources in any modernized economy, develops potential scientific-technological progress, spurs innovation and drives economic growth. The stock market serves as a market sorting mechanism for the capital flow into the most promising economy sectors and the transformation of inert savings into dynamic investments.

Materials and Methods

Histories of the formation and subsequent development of stock markets, both foreign and domestic bear out the conclusion that self-regulating mechanisms are not justifiable and the state regulation of this field becomes necessary. Recent waves of financial crises on a global scale once again proved the failure of self-regulating mechanisms of the stock market in overcoming crisis situations and eliminating the consequences [1;2]. The problem of state regulation of the stock market is currently important. Despite the fact that in many post-Soviet countries the infrastructure of a stock market has been created, and its economic, organizational and legal principles has been formed, these stock market(s) do not adequately realize their functions in attracting investments for the development of the respective national economy(s) [3;4].

After the global financial crises, many economists have come to the conclusion that financial markets again need a rigid framework for their operation. The crisis has also resulted from the ubiquitous deregulation (weakening or even lack of regulation) of financial markets.

The process of formation and development of the stock market in foreign countries differs significantly from the practice of the post-Soviet countries. The main differences are that in most foreign countries the stock market was formed under the influence of the development of joint-stock activity, and the growing demand for capital stimulated tough competition between issuers for investors' financial assets [5]. But in the post-Soviet countries, even at the present time, the mechanisms of healthy market competition are still not sufficiently formed. The stock market in most post-Soviet countries is at the stage of formation and is unduly monopolized.

The main characteristics of the stock market in Azerbaijan may be summarized as follows:

1. Underperformance of the self-regulating mechanism;

2. Imperfection of state regulation of the stock market;

3. Mistrust of potential and domestic investors in securities market instruments (mainly due to the imperfection in regulatory and legal framework, establishing administrative and criminal liability for offences in this field of human activity);

An analysis of trends in the development of the domestic securities market showed that this market has a number of significant problems. First, it is highly speculative. Secondly, the stock market is characterized by a high concentration of issuers' capitalization and exchange turnover, this factor does not allow the market to effectively perform the function of an investment generator for economic development [6]. Thirdly, the domestic stock market is very monopolized, since the largest market participants account for about 80% of the total exchange turnover of securities

Most investments into the real sector of Azerbaijan's economy are transformed as revenue transferred from the oil sector, which turns the state into the main investor in the investment market. The state, acting as the main participant of most major investment projects and the main holder of controlling interests in many joint-stock companies, creates additional risks and threats to financial stability of most large issuers. In the event of a drop in energy prices and a reduction in government revenues, the financial situation of many issuers will worsen, which will create a crisis situation in the country's stock market [7;8].

Precisely because of the drawbacks in the field of weak state regulation, speculative flows dominate the domestic stock market. Since acting as a money generator, the stock market can generate a fictitious capital from nothing. In the usual turnover of capital in the economy, money consistently passes through all stages of the cycle. On the self-regulating stock market there are shortened money turnovers, which occur mainly between contractors and do not reach the issuers. That negatively affects the increase in the real national wealth. Those speculative factors in the stock market allow by artificially manipulating domestic financial flows and mixing fictitious and real capital to use it for the purpose of distributing labor products. It results in the generation of fiat money, violation of the trade balance and acceleration of inflation in the economy of the country.

Many researchers are in favor of the paradigm of active state regulation of the stock market. This regulation cannot be limited only by monitoring compliance with the requirements of legislation by professional participants of the stock market. That is, we are talking about strengthening state regulation of the stock market. The domestic stock market for the period of its formation and development has not turned yet into an effective mechanism for investing into the real sector of the economy. To do this, first of all, it is necessary to determine the strategic ways of formation and development of the domestic stock market, and we must bear in mind that government intervention into the sensitive mechanism of the stock market should be strictly limited to the need. Measures and the degree of state influence on the stock market should be justified and clearly predicted.

In the strategic plan, it is necessary to form a domestic stock market, which will serve as an effective mechanism for attracting and redistributing capital in the economy, and it will also stimulate domestic investment activity and strengthen the country's position in the global capital market.

The domestic stock market should be as open to the individual investor as possible and be attractive to issuers of stock. The stock market should be regarded as a complex intertwining of two interrelated processes: the accumulation and acquisition of income from the exploitation of production capital. Here, the object of research is the financial flows that characterize both these processes. The main elements of these flows are formed based on the indicators of investment costs and net income.

The development of the domestic stock market is adversely affected by many unresolved problems. These factors do not allow turning the stock market into an efficient mechanism for attracting investments into the real sector of the economy. Among these problems we should especially highlight the lack of tools to combat the use of insider information. The domestic stock market is an insider oriented one, where there is a possibility of good earnings, by obtaining in advance confidential information about the activities of issuers or large investors. Advanced economies h fight tough against such practices. In the Azerbaijani legislation, there is no consensus to establish a ban on the use of insider information and determine ways to counteract this activity; yet conversely and incongruously there is a significant and regulatory requirement bureaucracy for the registration of emissions leading to a decrease in operational efficiency in the process of preparing for the issuance of securities. Therefore, there are cases when issuers, having made a decision to issue bonds, receive all necessary permits, while the situation on the debt market has changed dramatically, and it is no longer profitable to place this bond.

Some researchers have determined by 5 principles of state regulation of the stock market as follows:

1. legality; or governed by the rule of law;
2. unity or coherence;
3. openness or transparency;
4. independence or autonomy in self-regulation
5. responsibility; or accountability

These principles allow for a stable yet flexible constant development and improvement of all elements of regulatory activity in accordance with changes in the political and economic situation in the country.

Researchers distinguish two basic models of building an organizational and economic regulatory mechanism: on a sectorial and functional principle. [9;10]

The stock market in comparison with other financial markets - is a more complex object of state regulation. Since there is a wide variety of types of securities. Each of them has a specific technology of functioning. And also, the degree of risk of operations with securities in comparison with currency and money operations is higher. Since the stock market has a large number of participants (legal entities and individuals) and the variety of interrelations between them, differences in their economic and legal status, etc. In this case, the state regulation of the stock market should be aimed at reducing the overall risk of the stock market.

When considering the growth rates of the securities market, it is possible to trace the development of a dynamic process of the stock market, and the development of the domestic stock market gradually provides large alternative opportunities for attracting and placing money. This creates the prerequisites for improving state regulation of the stock market.

Improvement of the stock market regulation should be aimed at an optimal combination of early warning of crises and risk assessment of emerging new risks. First of all, it is necessary to analyze and forecast the threats that contribute to the onset of risks, which are called risk factors.

At the moment, the system of state regulation of the domestic stock market is characterized by the distribution of regulatory powers among several state bodies. There is no legally fixed mechanism of interaction of the State Committee for Securities of the Republic of Azerbaijan with other government securities market regulators - the Central Bank, the Chamber for Control over Financial Markets and the Ministry of Finance of the Republic of Azerbaijan. Uncoordinated actions of these bodies negatively affect the integrity of state regulation of the stock market.

Conclusion

As a result of the fragmentation of powers and the low level of interaction between regulatory and supervisory bodies, the efficiency of regulation decreases, an overlapping of functions arises, and there is no uniform state policy to regulate the domestic stock market: These factors do not allow to effectively counteracting to unlawful processes in the stock market.

Being one of the main elements of the institutional system of the stock market, self-regulating organizations should theoretically contribute to the efficient functioning of the securities market by increasing the level of regulation of market participants through interaction with state bodies. But these organizations are not the main regulators of the market, they do not use the existing powers to implement regulation of professional market participants.

An analysis of the regulation systems of the stock markets in advanced economies such as the United States and Great Britain, allows for the conclusion that regulators with the legal status of a state agency or a professional association are effectively performing their functions. The experience of the United States can be used to effectively operate the stock market. Here, the state regulation body of the stock market is given broad powers to conduct special investigations with respect to professional market participants. This allows the state to more effectively combat such violations as market manipulation, the use of insider information, the legalization of shadow revenues or money laundering. A mega-regulator of the financial market would eliminate the disunity of state regulation and the experience of the United Kingdom on the formation of a single body that would regulate all participants of the financial market, may be used.

A synthesis of the Azerbaijan stock market regulatory framework is needed to increase the efficiency and effectiveness of the domestic stock market.

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