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# THE SPECTRUM OF AZERBAIJAN'S INCREASING ECONOMY

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## **Abstract**

*This paper aims to underline the key measures that Azerbaijan took during the past 20 years in regards to sustainable development. Although the country broke up from the Soviet Union in the 1990s, there has been a particular and precise preoccupation regarding its evolution as a nation. It is important to underline the fact that, in present time, Azerbaijan is an important country in the South Caucasus, which has economic relations with other parties such as the European Union, Turkey, Russia, and others. These relationships are based, mostly, on the fact that Azerbaijan is a reach resource country that supplies many countries with oil and gas.*

**Keywords:** Azerbaijan, sustainable development, economy, plan, petroleum.

**JEL Classification** H6, L7, N7, O21, P00

## **Introduction**

The road of the economy has followed during the past 20 years a complicated but, nevertheless, a satisfying path, transforming Azerbaijan in a modern country. The result in Azerbaijan, and other countries, after the Soviet Union breakup in the 1990s was a complete chaos regarding economics, politics and social life. During that period, Azerbaijan was struggling with the military aggression that resulted from the Armenian policy of genocide and occupation, when 20% of the country was occupied.

Starting with this period, having a great leader in the person of Heydar Aliyev, important issues have been solved so that the country could revive and follow a developing path. A first step was the one of ensuring the independence of the state, making the political stability a sure thing inside the country. Another step was regarding stabilising the country's macroeconomics, regulating its indicators so that the hyperinflation to be reduced.

The "Contract of the Century" was also signed in that period, which meant that the Azerbaijan's hydrocarbon reserves to be used in and for the people's benefit. The aim of these institutional changes was to replace the administrative system that was inherited from the Soviet Union period, with a new system that enhances free competitive relations, measures so that a market economy system to be formed, changes regarding privatisation of state-owned companies and the formation of new ones. A higher level of development concerning socioeconomic prospect was possible through the deepening of the reforms that took place in the country after 2000.

The extraction and export of natural resources have ensured an increasing line in the country's dynamics of economic growth even in time of crisis such as the global one in 2009, this showing a successful implementation of the strategic line that has been

chosen. If we look at the non-oil sector, we can observe that significant achievements took place over the past years since the average annual growth rate reached almost 11% (Outlook For The Future, 2013).

### **Theoretical approach of Azerbaijan economy indicators**

According to IMF, for 2014, Azerbaijan has reported a gross national income per capita of \$8,303, meaning that it become part of the upper middle-income country group in a short period if we take into account that in 2001 the GNI per capita was \$660. This quick transformation was possible through the development of the exploitation concerning hydrocarbon resources, high level of public expenditure and with the help of substantial reforms that supported a market-based economy (World Bank, 2015). Another example regarding the country's development is its population that reached, in 2014, 9,48 million, of which 51% under the age of 30 years. Approximately 53% of the population lives in urban areas (Human Development Report, 2013)

The government created in 2012, a new document called —Azerbaijan 2020: Look into the Future— which aims to lay the foundation for the transition to a knowledge-based economy from a traditional economy, including the emergence of knowledge-intensive products. The document's vision entails Azerbaijan to become an internationally competitive, economically and politically developed, and having GDP per capita of \$13,000 by 2020. It also takes into account the prospect of an economic diversification and opportunities expanding for citizens through non-oil sector development. The document's agenda incorporates many factors, such as high social welfare, ample opportunities, sustainable economic growth, and a decrease in the unemployment rate, reduced regional inequalities, and greater accessibility to communication, health, education, and financial services (Look Into The Future, 2014).

According to the World Bank classification of GDP, in 2020 Azerbaijan is expected to become a full member of the group entitled “countries with high average income” with the primary objective of eliminating its dependence regarding the export of hydrocarbons, which is at the moment the main reason for its belonging to this group, and to reach the highest positions in the group, according to the human development classification of the UN.

Regarding economy, Azerbaijan will turn from the region's leading country into a very competitive participant in the international system of economic relations. It can take profit of its favourable geographical position along with its broad potential and turn itself into the commercial centre of the region targeting a volume of per capita non-oil export to 1,000USD (Asian Development Bank, 2014).

Since Azerbaijan is a country rich in resources that finds itself in the South Caucasus and that used these resources to its benefit well over the past decade, poverty has been very much reduced, contributing to the growth of the middle-class. According to World Bank, in Azerbaijan the incidence of poverty has fallen to 6% from a top of 15.8%, also managing a decrease in the unemployment rate to 5.2% in 2012. Taking into account the fact the population is very young (in 2014, people having the age under 25 years – 40% of total population, while individuals with the age under 35 years – 60% of total population), there is a need for institutional reforms. Their implementation will increase the employment in the private sector, train and develop young people skills

adequate for the future challenges that will occur ensuring competitiveness and entrepreneurship preparation.

Azerbaijan is looking to correct its dependency of employment on the agriculture sector. 37% of its workforce is in this low-productivity sector that is contributing to the GDP with nearly 5%. Opposite to this is the mining industry that is contributing to the GDP with over 40% but employs only 1% of total workforce (World Bank, 2015).

## **Research Process**

Worldwide relevant institutions and bodies have been the source of information which contributed to the qualitative and quantitative analysis. Yearly reports of the International Monetary Fund, World Bank and European Commission contributed with statistical data regarding main economic indicators that reflect the trends in Azerbaijan economy. The study conducted over the past months shows the evolution of an ex-Soviet country which had the power to develop its economy through a sustainable management process of the country's advantages (mainly mineral fuels).

## **Institutional importance in economic sustainability**

The government is working across all sectors on more than 60 state programmes and strategies, including the State Program on Poverty Reduction and Sustainable Development in the Republic of Azerbaijan for 2008–2015. These programmes, along with Azerbaijan 2020, emphasise some important objectives such as inclusive growth, poverty reduction, environmental sustainability, infrastructure development, job creation, social protection, education, private sector development, gender equity, and many others. The government also took initiatives so that the non-oil sectors to be developed such as developing industrial zones, providing concessional loans to small enterprises and subsidies to agribusinesses. The government prefers to borrow mainly in some areas like transport, energy, water supply, private sector development, finance, and public management, making this a real hub for the development partners of the country.

One of the institutional significant accomplishments of Azerbaijan was the creation of The State Oil Fund of Azerbaijan (SOFAZ), that represents the cornerstone of the country's natural resource revenue management strategy. SOFAZ was established in 1999 with support from the IMF and the World Bank playing the role to accumulate excess oil and gas revenues.

In 2006, Mr Shahmar Movsumov joined Azerbaijan's state oil fund, SOFAZ, back then it had under management assets in a value of 1,2bn dollars, only 30 personal staff and only one asset class to invest in (fixed income). In 2015, Mr Movsumov is CEO of SOFAZ that is the world's 29th largest sovereign wealth fund, having a 37bn USD pool of assets, which includes real estate in the main cities such as London, Paris, Seoul and Moscow and also equities in gold.

In the present time, the oil price has dropped to 50\$ per barrel, making these years the toughest one for Azerbaijan since the oil boom began and forced it to look towards SOFAZ to save the economy. The government will draw down some of its money for the first time since 1999 when the oil fund was founded. "This is exactly the role of the capital and the framework that was foreseen since the beginning. We are testing the concept of the volatility reducer, or buffer – Mr Movsumov" (Financial Times, 2015).

The oil price has repercussions also on Azerbaijan's currency, manat. Although the government insisted for months the fact that it would maintain the stability of its currency, regardless of the falling price of oil and neighbours currency devaluations, in the end, they had to devalue its currency. The central bank of Azerbaijan had stated that the decision for devaluating the manat by 34% to a rate of 1,05 manat/USD was based on the fact that it would support Azerbaijan's diversification of the economy, it would provide a balance of payments sustainability and strengthen exports and international compatibility (Financial Times, 2015).

Over a decade of increasing prosperity with an outcome of almost half of Azerbaijan population lifted out of poverty, this is an important result of President's Ilham Aliyev government, which faces today a severe test since the oil price has fallen to approximatively 45\$. Nowadays, oil and gas sales represent 95% of exports and more than 70% of government meaning that, until this participation of oil and gas sales in the Azerbaijan economy will not decrease, every change in oil price will have a direct impact on its budget.

In 2015, according to analysts from the Foreign Service of the European Commission, there are very close ties in economic terms between the European Union and Azerbaijan. The EU is the first trading partner of Azerbaijan, with 47% of total commercial trade. Also, for Azerbaijan, the EU represents the biggest exporter and importer, accounting for 53% and 34% of the total. EU exports in Azerbaijan are largely mechanical transport equipment and machinery, while imports from Azerbaijan are concentrated almost entirely on oil products, oil and gas (98% of total imports). The countries (from EU 28) with the highest value of exports in Azerbaijan are: Germany with 775 million Euros - 22.3% out of total, the United Kingdom with 701 million Euros - 20.1% out of total, Italy with 595 million Euros - 17.1% out of total, Netherlands with 292 million Euros - 8.4% out of total and France with euro 208 million Euros - 6% out of total (Tanase, 2016).

For 2015, the government based its budget on an oil price of \$90 a barrel, taking in account \$15bn in spending (by SOFAZ). But with an oil price of \$45, the revenues of SOFAZ would fall from \$16.3bn last year to just \$4.7bn (Financial Times, 2015).

The experts from the International Monetary Fund, have forecast 3,5% growth in Azeri GDP for 2015, they also urged Azerbaijan to reduce its dependence on oil as global energy prices fall. President Ilham Aliyev said that total investment in Azerbaijan's economy fell to 27bn USD last year (28bn USD in 2013), forecasting a total investment of more than 25bn USD this year, from which 7bn USD is coming from foreign investors (Reuters, 2015).

The State Oil Company of Azerbaijan Republic (SOCAR) is looking for ways to respond to the low oil price that affects its revenues. One way for compensating the decline in the crude oil production is to increase the production of gas and condensate from other fields, as Mr Elshad Nassirov, vice-president of SOCAR said. The centre of this strategic plan is the 45bn USD Southern Corridor project that was signed at the end of 2013 and which is expected, in 2020, to deliver Caspian gas directly to Europe (Financial Times, 2015).

Despite the project's importance, two partners, Total and Statoil, have already sold their stakes, based on the fact that its profitability is now questioning since the oil price is low that is also affecting the gas price in Europe. The project is supposed to have a breakeven point at an oil price of about 60 USD a barrel, meaning that it is at high risk since recent price is approximately 45 USD/barrel.

This is way Azerbaijan Republic is trying to speed up the economy diversification so that the non-oil sector will develop with an important goal of increasing its competitiveness and export possibilities, regardless of the oil price or its level of revenues. The primary task of “Azerbaijan 2020: Look into the Future”, is to boost non-oil exports, this is why the economic model that is taken into account for implementation and improvement is export-oriented.

Azerbaijan is trying to achieve these goals by fully using its possibilities such as existing economic, political and social resources so that it will strengthen its real potential. Taking this into account, it is planned to develop the sectors of energy, transit and logistical infrastructure, transport, regional development centres by using their competitive advantages.

In the end, any economic growth has the target of increasing the social welfare. Human capital and social development is one of the top priorities of the plan and is based on improving the quality of education and services, gender equality, social security and youth potential.

## **Conclusions**

The findings of this paper underline the path which a state could take towards its development. Nevertheless, the risk that can occur during the process can slow down the progression towards obtaining the target. This paper presents how Azerbaijan organised and managed its evolution during the past 20 years. Examples of national companies and institutions are given to emphasise their importance in the process. In an unstable world economy which is subject to many risks (oil prices, geopolitical tensions, low rate of international trade), and which reacts immediately to the turbulences that may occur, Azerbaijan struggles to remain a competitive economy which tends to develop through a sustainable evolution year after year.

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