- *Growth picked up in December, driven by the non-hydrocarbon sector, bringing the growth in 2023 to 1.1 percent.*
- *Annual inflation further fell in December, to 2.1 percent, and the CBAR cut the policy rate to 7.75 percent.*
- *The trade surplus moderated in December.*
- *The budget recorded a deficit in December amid a hike in spending.*
- *Credit to the economy expanded at a moderate pace while deposits saw a marked increase in December.*

The economy expanded by 4.2 percent (yoy) in December bringing annual growth in 2023 to 1.1 percent (in real terms). Hydrocarbon sector output declined by 2.9 percent (yoy) in December, driven by a 10 percent (yoy) fall in crude oil production, while natural gas production was similar to a year ago. The non-hydrocarbon sector grew strongly in December, at 7.5 (yoy), as growth accelerated in construction (21.3 percent, yoy) and ICT (17.5 percent, yoy). Growth slowed in hospitality (7.9 percent, yoy) and retail trade (3.5 percent, yoy) and declined in the transport sector (- 2.5 percent, yoy). Overall, in 2023, the hydrocarbon sector contracted by 1.7 percent, while the non-hydrocarbon sector expanded by 3.7 percent (yoy). On the demand side, investments declined by 29.7 percent (yoy) driven by a fall in hydrocarbon sector investment, while non-hydrocarbon investments grew by 2.4 percent (yoy). High frequency indicators point to a pick-up in consumption in December: small payments rose by 30 percent (mom), credit card operations increased by 16.7 percent (mom), and money transfers edged up by 5.1 percent (mom).

Inflation further decelerated in December, with annual inflation reaching 2.1 percent. CPI inflation rose by 0.5 percent (mom) in December, supported by a 1 percent (mom) increase in food prices. Service prices grew by 0.1 percent (mom) while non-food prices remained stable in December. The housing price index increased by 1.7 percent in Q4 2023 compared to Q3 while housing prices were 9.7 percent higher in 2023 compared to 2022.

Amid declining inflation, the Central Bank cut the policy rate in early February. Annual inflation settled at the lower bound of the CBA's 4+/-2 percent target interval, which prompted the CBA to cut the policy rate by 25 basis points, to 7.75 percent. The CBA highlighted several factors that helped disinflation processes in 2023, including declining world food prices (10.1 percent drop compared to 2022) and an 18.9 percent appreciation of the NEER in 2023. Interbank rates also fell in line with the policy rate cut.

The trade surplus moderated in December. Exports expanded by 32 percent in December, as hydrocarbon exports increased by 38 percent (yoy), driven by natural gas exports. Non-hydrocarbon exports edged up by 3.8 percent in December, driven by exports of fruits and vegetables, electricity, and chemicals. Overall, in 2023 exports were down by 11 percent compared to 2022. Imports fell 11.2 percent (yoy) in December, while cumulatively growing by 19 percent in 2023 (yoy). The trade surplus reached 23 percent of GDP in December from 30 percent in 2022.

The exchange rate remained unchanged at 1.7 AZN/USD, while CBAR reserves surged in December. In December, the State Oil Fund sold USD 150 million or 36 percent lower than in November. Due to low FX demand, the CBAR bought excess FX from the market, which resulted in a 9.4 percent (mom) increase in reserves, which reached USD 11.4 billion by end-December. State Oil Fund reserves increased by 14 percent (yoy) in 2023, reaching USD 56 billion or 77 percent of GDP.

The budget recorded a deficit in December as spending picked up markedly. The budget revenue increased by 3.5 times in December (yoy). This large increase is explained by the surge in SOFAZ transfers in December. Transfers, which had been low throughout 2023, were boosted to meet higher spending needs. Non-hydrocarbon sector revenues increased by 14 percent (yoy) in December, supported by robust collection of VAT and customs receipts. Budget spending increased by 20 percent (yoy) in December as capital spending increased by 11.2 percent (yoy) while current spending expanded by 42 percent (yoy). The state budget balance recorded a deficit of AZN 1.4 billion, or 1.1 percent of GDP, in December bringing the cumulative deficit to 0.8 percent of GDP in 2023 as a whole. At the same time, the consolidated budget surplus amounted to 8.2 percent of GDP propelled by strong revenue flows to SOFAZ. The non-oil primary deficit balance was estimated at 21 percent of non-hydrocarbon GDP in 2023, lower than the initially planned 25 percent as well as the 22.4 percent recorded in 2022, pointing to compliance with fiscal rule targets.

Credit to economy expanded robustly in December. Banks' loan portfolio rose by 1.5 percent (mom) in December, supported by a 1.6 percent (mom) increase in business loans and a 1 percent (mom) expansion in consumer lending. Overall, credit to the economy expanded by 19 percent (yoy) in 2023. The deposit portfolio increased by 5.2 percent (mom) in December, with manat deposits expanding by 4.7 percent (mom). Dollarization of deposits inched down to 40 percent in December. Bank profits increased by 17.7 percent (yoy) in December.

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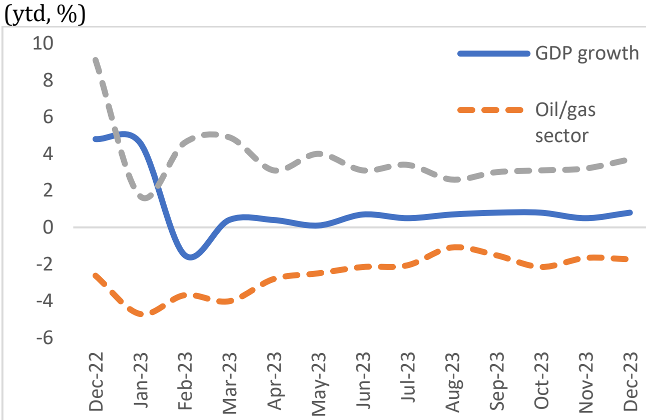
Figure 1. Economic growth picked up in December 2023, driven by the non-hydrocarbon sector

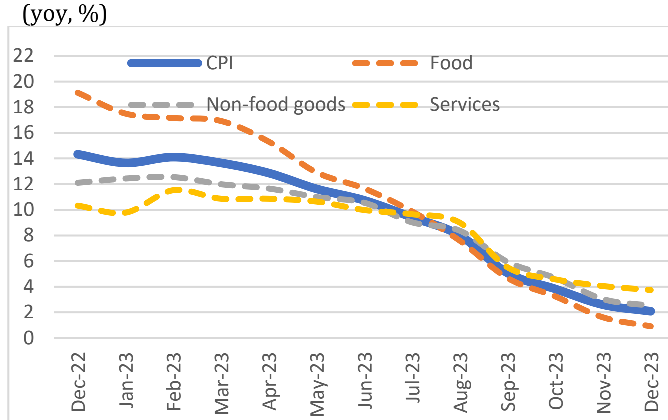
(ytd, %)



Source: State Statistics Committee

Figure 2. Annual inflation fell to 2.1 in December 2023

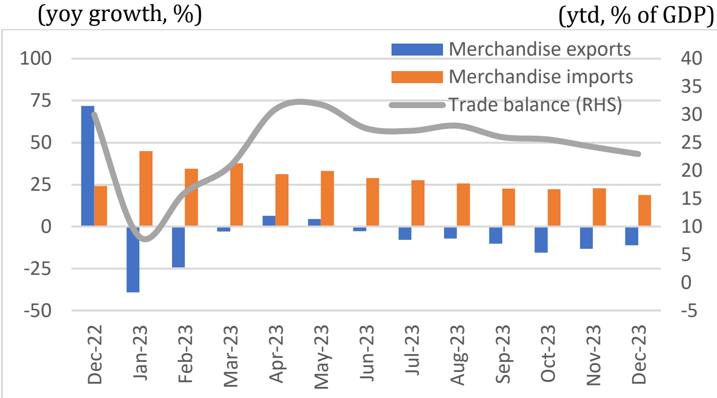
(yoy, %)



Source: State Statistics Committee

Figure 3. The trade surplus moderated in December

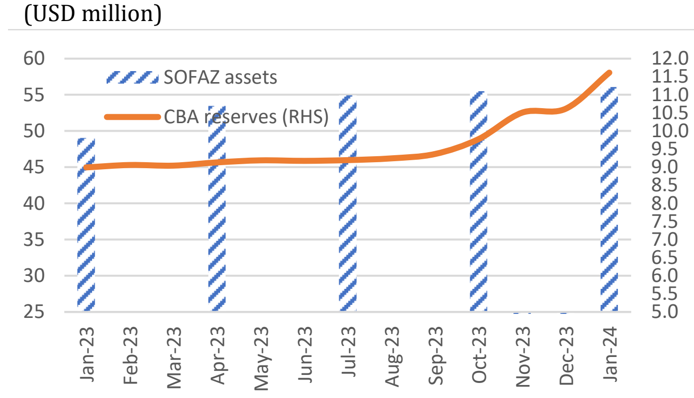
(yoy growth, %) (ytd, % of GDP)



Source: State Customs Committee

Figure 4. CBAR reserves surged in December amid low FX demand

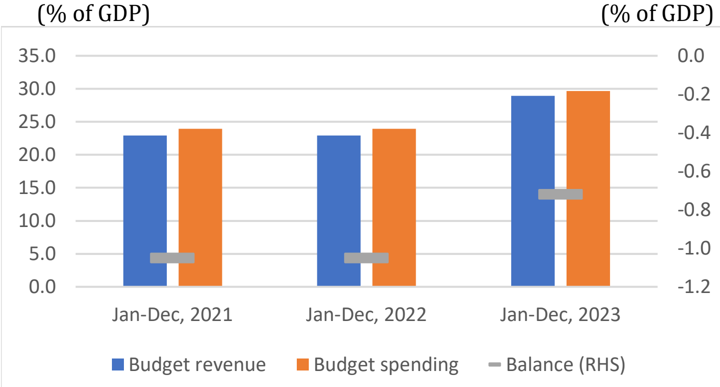
(USD million)



Source: CBA

Figure 5. The state budget posted a smaller deficit than in previous years

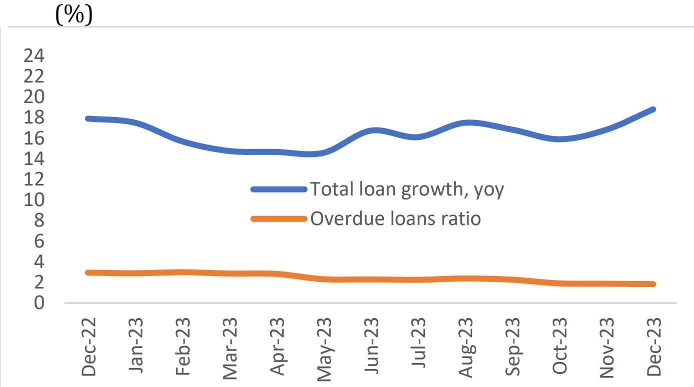
(% of GDP) (% of GDP)



Source: Ministry of Finance

Figure 6. Credit to the economy accelerated in December 2023

(%)



Source: CBA

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