

AZERBAIJAN

Table 1	2022
Population, million	10.2
GDP, current US\$ billion	76.8
GDP per capita, current US\$	7533.4
School enrollment, primary (% gross) ^a	94.3
Life expectancy at birth, years ^a	69.4
Total GHG emissions (mtCO ₂ e)	53.2

Source: WDI, Macro Poverty Outlook, and official data.
a/ Most recent WDI value (2021).

Economic growth slowed sharply to 0.5 percent in H1 2023, dragged down by contracting oil production and moderate non-energy sector activity. Growth is projected at 1.5 percent in 2023 as a whole. Inflation eased, although it remains in double digits as of June 2023, and is expected to continue to decline. The current account surplus is expected to reduce in 2023 due to a reduction in exports and money transfers.

Key conditions and challenges

Azerbaijan's continued reliance on hydrocarbons as a major source of export and fiscal revenues remains its main vulnerability. It challenges long-term growth prospects because of declining oil production, oil price volatility, and the global transition away from fossil fuels.

Constraints to private sector development include a large state footprint in the economy, lack of a level playing field for companies, shallow financial markets, and a weak human capital base. Azerbaijan's 2022–2026 Socio-Economic Development Strategy lays out a reform plan to move to a private sector-led growth model and the development of human capital, with a sustained 5-percent growth target in non-energy sectors in 2022–2026.

Recent developments

In H1 2023, real growth slowed to 0.5 percent, compared to 4.6 percent in 2022. The energy sector contracted due to a fall in oil production because of aging oil fields, while natural gas grew at a slower pace, with gas production nearing full capacity. The non-energy sector expanded by 3.1 percent, with service sectors (transport, hospitality, retail trade) cooling after strong growth in 2022.

On the demand side, consumption growth eased due to a decline in real wages and moderation in money transfers from Russia. Investment growth remained robust, supported by public investment largely directed toward reconstruction in liberated territories and the energy sector.

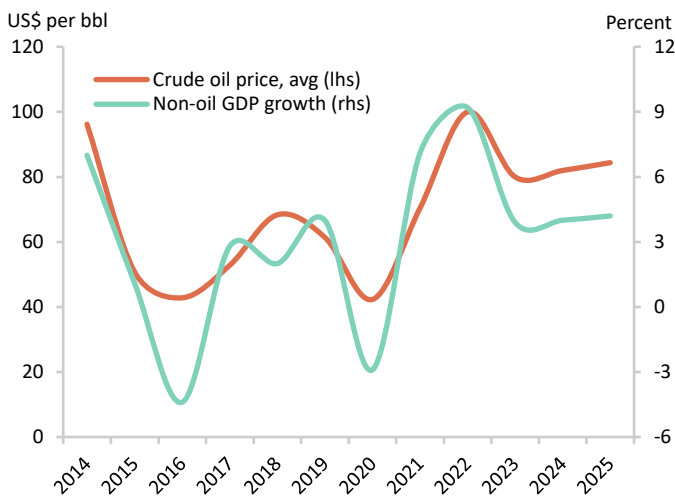
The latest official figures show that the national poverty rate decreased from 5.9 in 2021 to 5.5 in 2022. In the first months of 2023, the unemployment rate remained stable at 5.6 percent.

Inflation moderated to 10.7 percent (yoy) in H1 2023, from 14.3 percent at the end of 2022, driven by a slowdown in food inflation. With inflation still in double digits, the Central Bank of Azerbaijan (CBA) raised the policy interest rate by 75 bps in H1 2023, to 9 percent (which remains negative in real terms).

Falling energy prices and falling oil production in H1 2023 negatively impacted exports, with a decline of 2.9 percent (yoy) in USD terms, while imports increased by 29 percent (yoy), largely driven by public sector investment. Despite faster growth in imports, the trade surplus reached 27.5 percent of GDP in H1 2023. Money transfers dropped by 48 percent in H1 2023 (yoy). Foreign currency reserves increased by 2.7 percent compared to year-end 2022, reaching USD 9.2 billion or 5.4 months of import cover.

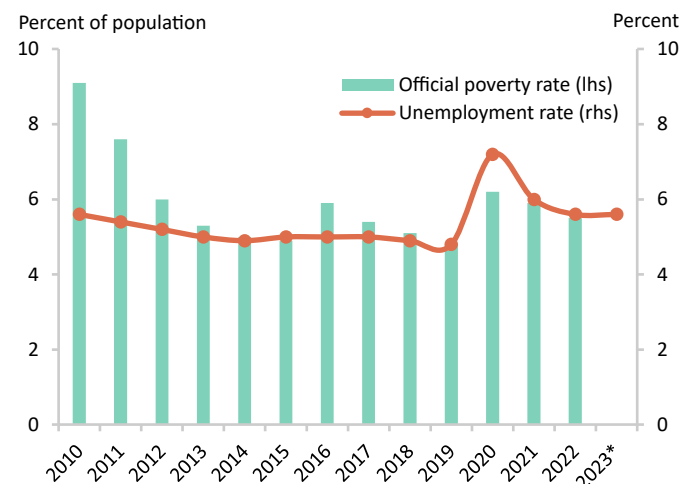
The fiscal balance recorded a large surplus in H1 2023, at 18.4 percent of GDP. This is due to surge in revenue to 44 percent of GDP, supported by higher tax receipts from sales of natural gas.

FIGURE 1 Azerbaijan / Non-oil GDP growth and oil price



Sources: State Statistical Committee, World Bank data, and World Bank staff estimates.

FIGURE 2 Azerbaijan / Official poverty rate and unemployment rate



Source: State Statistical Committee.

Notes: The World Bank has not reviewed the official national poverty rates for 2013–2022. * Preliminary data.

Spending expanded to 26.5 percent of GDP, with public investment increasing to 6.5 percent of GDP, while current spending lagged. Due to a high revenue outturn, the Government increased the 2023 planned budget spending by 10 percent in nominal terms (from the original budgeted amount). Sixty percent of the increase will be allocated to reconstruction needs. Fiscal buffers remain strong, with reserves of the State Oil Fund of the Republic of Azerbaijan (SOFAZ) increasing by 12 percent, to USD 55 billion (70 percent of 2022 GDP). Public debt edged up to an estimated 14.5 percent of GDP.

Credit to the economy rose by 9 percent in H1 2023, driven by a 10 percent increase in consumer lending. The NPL ratio fell to 2.3 percent by the end of June, from 3.5 percent recorded a year ago, while bank profits increased substantially.

Outlook

GDP growth is projected at 1.5 percent in 2023 due to the expected reduction in oil production and slow growth in non-energy sector activity as growth converges to pre-COVID levels.

On the demand side, consumption will ease in 2023 while increased social transfers enabled by the revision of the budget are expected to limit the slowdown. Capital formation will largely be driven by public investment. In the medium term, in the absence of structural reforms, growth is expected to average 2.4 percent.

Inflation is projected to slow to 9 percent in 2023, as food prices continue to fall and external pressures ease while remaining above the CBA's upper range. Inflation is expected to return to CBA's target interval of 4+/-2 percent by the end of 2024.

The impact on poverty and inequality will depend on the extent of the reduction in food prices and the impact of slower economic activity on employment.

In 2023, the external balance is estimated to remain in surplus, supported by stable energy prices. Imports are expected to grow in 2023, largely driven by public investment. The fiscal balance is projected to remain in surplus in the medium term, averaging 3.4 percent of GDP, as energy revenue continues to offset higher spending in reconstruction and implementation of the development strategy.

The main downside risks are related to the uncertainty around the economic implications of Russia's invasion of Ukraine, including the risk of reversals of money transfers from Russia. In addition, a fall in energy prices could impact economic activity, as occurred in 2016. Upside risks include the potential increase in natural gas production due to a new gas field becoming operational.

TABLE 2 Azerbaijan / Macro poverty outlook indicators

(annual percent change unless indicated otherwise)

	2020	2021	2022	2023e	2024f	2025f
Real GDP growth, at constant market prices	-4.3	5.6	4.6	1.5	2.4	2.5
Private consumption	-5.1	7.0	4.9	4.0	3.6	3.6
Government consumption	4.8	3.8	7.4	7.1	3.1	3.1
Gross fixed capital investment	-7.1	-6.0	4.5	3.5	2.3	2.0
Exports, goods and services	-8.1	5.6	3.3	-1.0	1.7	1.8
Imports, goods and services	-10.5	2.5	3.2	2.2	2.7	2.7
Real GDP growth, at constant factor prices	-4.4	5.6	4.6	1.5	2.4	2.5
Agriculture	1.9	3.3	3.4	3.2	3.0	3.0
Industry	-5.2	4.1	2.4	-0.9	1.1	1.2
Services	-4.4	8.6	8.5	4.9	4.2	4.2
Inflation (consumer price index)	2.8	6.7	13.8	9.0	5.8	5.2
Current account balance (% of GDP)	-0.5	15.2	26.5	14.6	13.5	13.0
Net foreign direct investment inflow (% of GDP)	-1.5	-4.1	-1.5	-1.0	-1.0	-0.9
Fiscal balance (% of GDP)	-6.5	4.2	5.5	3.1	3.0	2.9
Revenues (% of GDP)	33.7	36.5	32.4	34.6	34.1	32.7
Debt (% of GDP)	18.4	16.2	11.7	13.3	14.0	15.0
Primary balance (% of GDP)	-5.7	4.8	5.9	3.4	3.3	3.2
GHG emissions growth (mtCO₂e)	-1.6	0.7	1.4	0.0	0.7	1.3
Energy related GHG emissions (% of total)	62.5	63.9	64.3	64.0	64.2	64.5

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices. Emissions data sourced from CAIT and OECD.

Notes: e = estimate, f = forecast.