

AZERBAIJAN

Table 1 **2021**

Population, million	10.2
GDP, current US\$ billion	54.6
GDP per capita, current US\$	5358.1
School enrollment, primary (% gross) ^a	95.8
Life expectancy at birth, years ^a	73.0
Total GHG Emissions (mtCO ₂ e)	79.9

Source: WDI, Macro Poverty Outlook, and official data.
a/ WDI for School enrollment (2020); Life expectancy (2019).

Russia's invasion of Ukraine poses downside risks to Azerbaijan's economic outlook, particularly in the non-energy sector. This follows a strong rebound in 2021, as recovering domestic and external demand supported growth in both energy and non-energy sectors, while rising global energy prices aided external and fiscal balances. Soaring energy prices will provide a short-term windfall, but mounting inflationary pressures and lower remittances are expected to weigh on poverty.

Key conditions and challenges

Azerbaijan faces structural challenges in developing a vibrant non-energy private sector. These include a large state footprint, institutional challenges, an undiversified asset mix with a low and stagnant level of investment in human capital, the lack of a level playing field, and shallow financial markets. This, in turn, has contributed to low private investment in the non-energy sector.

Following military tension with Armenia in 2020, a tripartite statement on armistice was signed between the two countries and Russia in November 2020. The reconstruction effort has progressed in 2021, even as the situation remains fragile, especially along the border.

Recent developments

Azerbaijan experienced a strong economic rebound in 2021, with output recovering to pre-COVID-19 levels by end-year. The energy sector grew by 1.8 percent, with production constrained by OPEC+ quotas for some parts of the year. Non-energy sectors' growth was more robust at 7.2 percent, led by services (especially transport, hospitality, and retail trade) and manufacturing.

On the demand side, consumption rebounded strongly, while investment

declined by 7.3 percent in 2021, with a 9.6 percent drop in non-energy sector investment, driven largely by lower private investment.

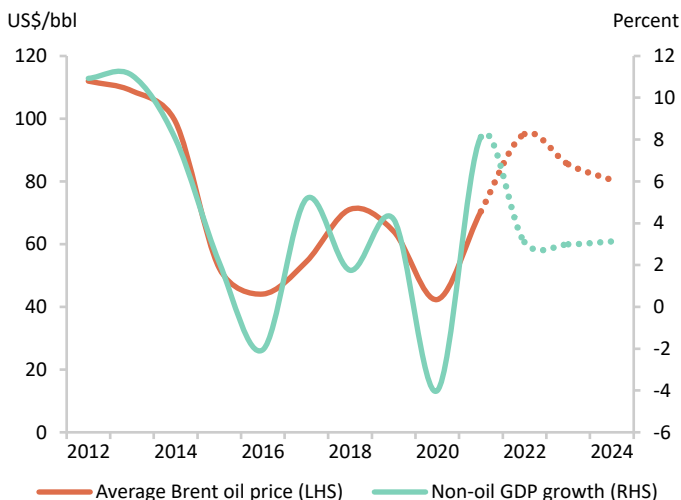
Rebounding domestic demand, rising global commodity prices, and increased administrative prices pushed inflation to 6.7 percent in 2021, overshooting the central bank's target range of 4±2 percent and prompting a 150-basis point policy rate increase since August 2021, pushing it to 7.75 percent in March 2022.

Soaring energy prices boosted external revenues, and the current account recorded a surplus of 15.2 percent of GDP. This was offset by financial outflows (9.2 percent of GDP). Yet the overall balance of payments was in surplus at 5.6 percent of GDP in 2021.

Rapid economic recovery and high State Oil Fund (SOFAZ) revenues supported fiscal revenues, which jumped 38.7 percent, while fiscal spending increased by 2.8 percent in 2021. As a result, the fiscal balance recorded a surplus of 4.2 percent of GDP in 2021.

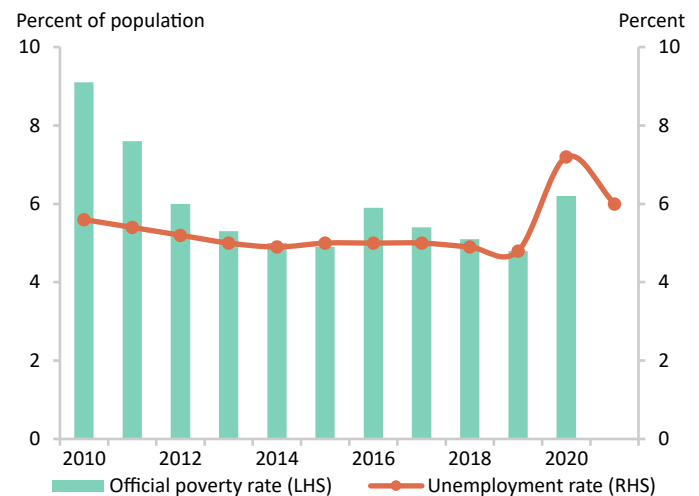
According to official data, the unemployment rate fell to 6 percent in 2021, from 7.2 percent in 2020, but was still above pre-pandemic trends. The official national poverty rate reached 6.2 percent in 2020, on a rise of 1.4 percentage points from 2019. Rural poverty increased disproportionately, as households experienced job and income losses in the COVID-19 induced crisis period. The economic rebound in 2021, and increased public wages and pensions, likely led to improved household income in 2021, although in real terms, this was offset partly by higher inflation.

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



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

FIGURE 2 Azerbaijan / Official poverty rate and unemployment rate



Source: State Statistical Committee of Azerbaijan. Note: The World Bank has not reviewed the official poverty rates for 2013–20.

Outlook

Economic growth is currently forecast at 2.7 percent in 2022, which represents a 0.9 percentage point downgrade from the baseline forecast prior to the invasion of Ukraine.

A short-term increase in oil and gas production would propel growth in the energy sector in 2021, but this increase is expected to subside beyond 2023. After a strong rebound in 2021, growth in the non-oil/gas sectors is expected to moderate in 2022. At the same time, spillovers from Russia's invasion of Ukraine and associated sanctions on Russia are expected to adversely affect export-oriented non-energy sectors, especially agriculture and tourism. Other sectors, e.g., manufacturing, are also expected to face difficulties in accessing critical imports such as wood, steel, and fertilizers.

In the medium term, assuming a stabilization of the geopolitical situation, growth is projected to average at 2.4 percent during 2022-24, close to its potential, as oil and gas

production stabilizes and the non-energy sectors face headwinds from low investment levels, subdued agriculture yields (due to still stressed water supplies) and remaining spillover effects from regional supply chain disruptions.

On the demand side, consumption will remain the principal driver of growth in 2022, as there is still some pent-up demand accumulated from 2020 and early 2021. Investment is expected to remain subdued with public investment stable and private investment anemic amid persisting structural challenges. External demand is likely to moderate, as growth in major trading partners declines. Non-energy exports, even though relatively small, will be hard hit as Russia was the destination for 32 percent of these exports in 2021 (2.5 percent of GDP).

Inflation is projected to stay elevated in 2022, above the central bank's target, due to higher import prices. Food prices are forecast to continue rising, as disruptions to global commodity markets linger. In the medium-term, inflation is projected to moderate, as consumption growth slows, pressure from imported

prices eases and global monetary conditions tighten.

The external balance is expected to record a sizable surplus in the medium-term, supported by high energy prices. Imports are projected to grow in 2022, in line with the continued recovery in domestic demand, and moderate in the medium term as growth slows.

The fiscal balance is estimated to be in surplus in the medium term, averaging at 4.7 percent of GDP, supported by higher oil and gas prices even as spending remains elevated.

The negative impact on poverty in 2022 is expected to be amplified by higher inflation and reduced remittances from Russia. Even though these remittances accounted for only about 1 percent of GDP in 2021, they disproportionately benefit the poor, especially those in small towns and rural areas.

This forecast is subject to uncertainty given the evolving global and regional environment, with elevated downside risks around protracted war and disruption to global commodity markets.

TABLE 2 Azerbaijan / Macro poverty outlook indicators

(annual percent change unless indicated otherwise)

	2019	2020	2021e	2022f	2023f	2024f
Real GDP growth, at constant market prices	2.5	-4.3	5.6	2.7	2.2	2.3
Private Consumption	4.2	-5.1	7.0	4.0	4.1	4.2
Government Consumption	7.9	4.8	3.8	3.9	3.2	2.3
Gross Fixed Capital Investment	-2.4	-7.1	-6.0	-3.6	-1.4	-1.0
Exports, Goods and Services	1.5	-8.1	5.6	2.7	1.7	1.8
Imports, Goods and Services	2.2	-10.5	2.5	2.6	2.7	2.7
Real GDP growth, at constant factor prices	2.5	-4.4	5.6	2.7	2.2	2.3
Agriculture	7.3	1.9	3.3	1.1	1.8	3.2
Industry	0.4	-5.2	4.1	2.6	1.1	1.1
Services	5.1	-4.4	8.6	3.2	4.0	4.0
Inflation (Consumer Price Index)	2.7	2.8	6.7	9.0	6.6	6.0
Current Account Balance (% of GDP)	9.1	-0.5	15.2	22.7	16.5	12.3
Net Foreign Direct Investment (% of GDP)	-2.9	-1.5	-4.1	-1.7	-1.2	-1.2
Fiscal Balance (% of GDP)	9.0	-6.5	4.2	6.4	4.2	3.5
Debt (% of GDP)	18.8	18.4	16.2	16.1	16.2	15.8
Primary Balance (% of GDP)	9.7	-5.7	4.8	6.8	4.7	3.9
GHG emissions growth (mtCO2e)	1.6	-2.3	2.7	0.7	0.3	1.0
Energy related GHG emissions (% of total)	42.9	44.1	46.6	48.1	49.3	50.6

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