

- *Economic growth in May stabilized at 7.2 percent. Given the strong economic performance in early 2022, World Bank growth forecasts are planned to be upgraded during the next round of projections.*
- *Inflation continued to increase in May (0.7 percent mom), while the policy rate remained unchanged.*
- *The trade surplus further improved in May amid rising imports, doubling that of the previous year (in % of GDP).*
- *The state budget recorded a deficit in May as spending increased. Amendments to the budget introduce fiscal stimulus for the rest of the year.*
- *Credit to the economy picked up in May on the back of consumer lending.*

Activity remained strong in May, growing at 7.2 percent. This was supported by a 2.7 percent (yoy) expansion in energy sectors and 9.6 percent (yoy) growth in non-energy sectors. The expansion in non-energy sectors was driven by non-oil/gas manufacturing (up 18.9 percent, yoy), ICT (up 14.8 percent), transport (up 33.2 percent), and hospitality (up 78.4 percent). Meanwhile, agriculture sector growth moderated to 2.8 percent in May from the 4.0 the percent (yoy) recorded in April. The construction sector shrunk by 18 percent (yoy) after recording strong growth in April (23 percent, yoy). On the demand side, investment picked up by 3.6 percent (yoy) in May, largely driven by non-energy sectors (up by 5.3 percent yoy), while investment in energy sectors continued to fall.

Inflation continued to climb in May. CPI inflation rose by 0.7 percent (mom) in May, bringing annual inflation to 13.7 percent. Food prices rose by 0.7 percent in May, with annual food inflation reaching 20.1 percent. Service inflation rose by 0.5 percent in May while annual service inflation stabilized at 10.3 percent. During January-May 2022, the agriculture Producer Price Index (PPI) rose by 16.7 percent compared to the same period of the previous year, while the non-energy non-oil manufacturing PPI picked up by 20 percent, affected by imported inflation.

The CBA kept the key policy rate unchanged citing favorable external accounts. The Bank kept the policy rate at 7.75 percent amid rising inflation, stating that the decision was backed a large current account balance (CAB) surplus (22.5 percent of GDP) in Q1 2022, supporting the use of the exchange rate as a nominal anchor. The CBA also increased note issuance in June by 23 percent (mom), in order to reduce AZN liquidity.

The trade surplus continued to increase as exports growth outpaced a pick-up in imports. Exports more than doubled in May compared to a year ago, largely driven by energy exports, which expanded substantially both in terms of volume and prices. In May, the export price of natural gas climbed to USD 816.6, the highest on

record. Non-energy sector exports increased by 10 percent (yoy). In contrast, imports expanded by 26.7 percent in May, in line with strengthening domestic demand, bringing cumulative import growth for the first five months of the year to 17 percent. The trade surplus rose to 34.4 percent of GDP during January-May, double that of the same period of 2021. Remittances continued to surge in May, rising by 3.6 times (yoy) largely due to inflows from Russia.

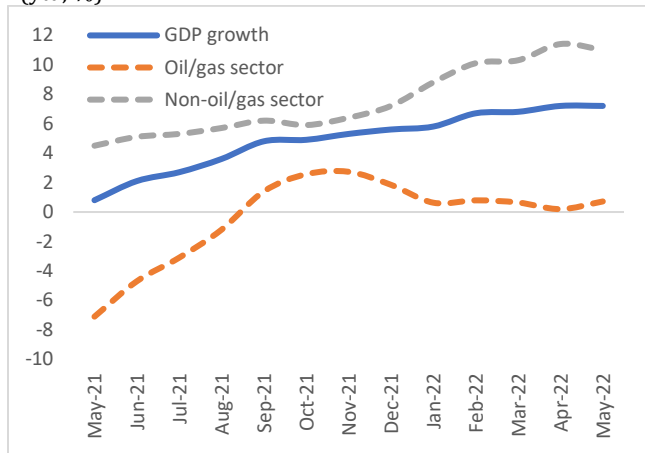
The exchange rate remained unchanged at AZN/USD 1.7, while CBA reserves rose. FX sales by SOFAZ slowed further in June to USD 278 million, 11 percent lower than year ago, amidst weaker demand for foreign currency. This allowed the CBA to build up reserves in June (with a 2 percent increase compared to May) and cover 6.2 months of imports.

The state budget recorded a deficit in May amid robust spending growth. Budget revenues increased by 17 percent in May. Oil revenues increased by 23.7 percent (yoy) in nominal terms, while non-oil revenues rose by 12 percent (yoy), partly driven by rising imports. Budget spending rose by 24 percent (yoy) in May in nominal terms, driven by capital spending (83 percent growth, yoy), while current spending rose modestly (6.1 percent, yoy). Overall, spending grew by 11.6 percent during the January-May period, compared to a year ago, which implies stagnation in real terms. The state budget recorded a deficit of AZN 526 million in May, while remaining in surplus during the first five months of the year (at 3.9 percent of GDP).

Amendments to the state budget for 2022 were approved on June 29, allowing a boost in budget spending. Revenues are projected to increase by 8.8 in nominal terms percent compared to the previous budget. This increase reflects higher projected non-energy tax receipts due to expected stronger activity and higher taxes from oil companies as the benchmark oil price for the budget is raised to USD 85 per barrel (from USD 50 under the previous assumption). Against the backdrop of higher revenue collection, transfers to SOFAZ are budgeted to be cut by 9.4 percent. Meanwhile, budget spending has been revised up by 8.1 percent. Over half of the spending increase will be directed to public investment for reconstruction while the rest will be spent on defense, social protection, and food security measures. The revised budget deficit is estimated at 2.7 percent of GDP in 2022.

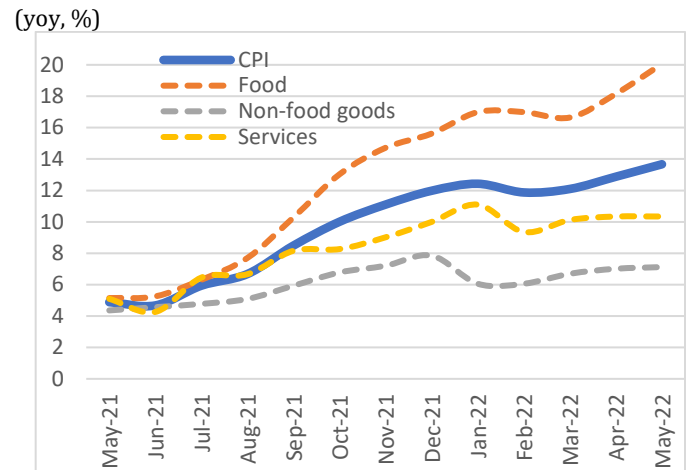
Credit to the economy is expanding at a steady pace. In May, Banks' loan portfolio expanded by 1.4 percent (mom) in nominal terms, driven by a 2.7 percent (mom) increase in consumer lending. Lending increased by 8.5 percent year-to-date (ytd) by end May. Deposit portfolio increased by 3.7 percent (mom) in nominal terms in May, bringing ytd deposit growth to 10.3 percent. The banking sector, overall, remained profitable overall, with profits rising by 6 percent (yoy) in May.

Figure 1. Economic growth remained strong in May, 2022.
(ytd, %)



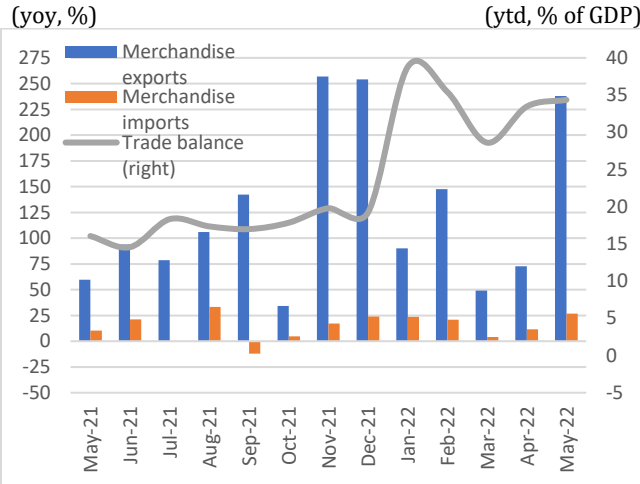
Source: State Statistics Committee

Figure 2. Inflation continued to rise in May, 2022.



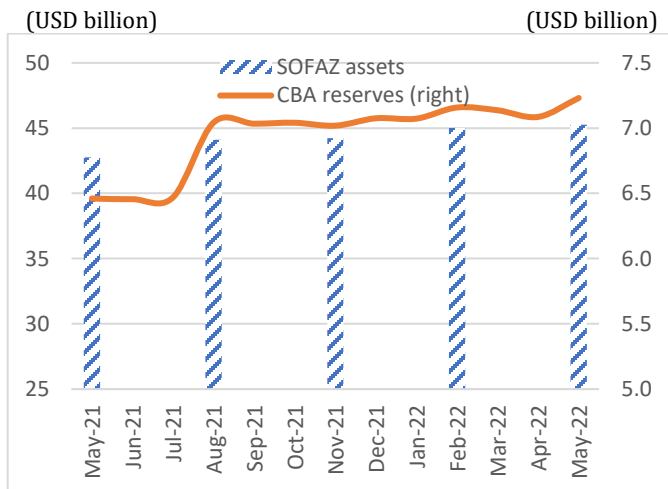
Source: State Statistics Committee

Figure 3. The trade surplus further strengthened in May, 2022.



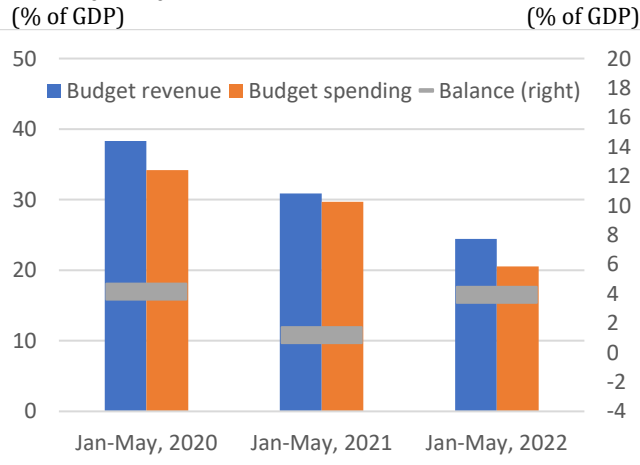
Source: State Customs Committee

Figure 4. CBA reserves rose in May, 2022.



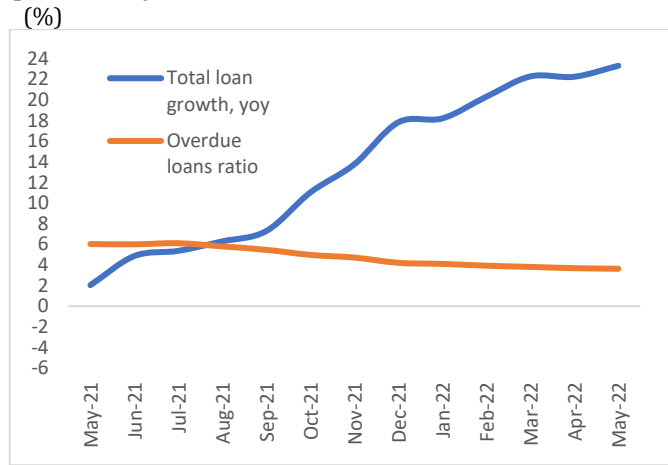
Source: Central Bank of Azerbaijan

Figure 5. State budget remained in surplus in January- May, 2022.



Source: Ministry of Finance

Figure 6. Credit to the economy expanded at healthy pace in May, 2022.



Source: Central Bank of Azerbaijan