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New debt policy in Azerbaijan : hopes, realities, risks and perspectives

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Reference: Hasanov, Rashad (2018). New debt policy in Azerbaijan : hopes, realities, risks and perspectives. Baku, Azerbaijan : CESD Press, Center for Economic and Social Development (CESD).

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New Debt Policy in Azerbaijan: Hopes, Realities, Risks and Perspectives

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Baku
September 2018

Abstract

From the second half of 2014, Azerbaijani public debt increased considerably along with several new challenges facing the domestic economy. During this period, the ratio of foreign debt to GDP rose from 8.6% (01.01.2015) to 22.8% (01.06.2018). The increase was 3.4 billion US dollars in nominal terms. At the beginning of 2018, Azerbaijan's public debt amounted to 10 billion 100 million US dollars, while the value of loans taken with state guarantees reached 12 billion 682 million US dollars, raising the ratio of debt to GDP to 55%.

The increase in the debt burden, particularly external debt liabilities, has caused concern both in the local community and in the government. Specifically, the deterioration of the financial situation of publicly-funded state institutions has raised the likelihood that the debt burden on this category will turn into a fiscal burden. As a result, the "Medium and long-term strategy for public debt management in the Republic of Azerbaijan" was approved on 24.08.2018.

Content

Abstract 2
Public Debt of Azerbaijan: Current Situation and Trends 4
Classification of public debt 4
Brief analysis of the current situation 4
Loans guaranteed by the government 6
Reasons for necessity of increasing government oversight 8
A new strategic look on public debt: medium- and long-term Action Plan 11
Goals, targets and priority activities of the strategy 11
Weak sides of the strategy 14
Possible difficulties for strategic targets 14
References 16

Public Debt of Azerbaijan: Current Situation and Trends

Classification of public debt

Public borrowing in the Republic of Azerbaijan is conducted in line with the requirements of the laws of the Republic of Azerbaijan "on public debt" and "on budget system". According to the legislation, funds to be paid on contractual obligations made on behalf of the Republic of Azerbaijan are considered public debt[1].

According to national legislation, Azerbaijan's public debt consists of three main components:

- *Debts of the government to financial and credit institutions;*
- *Debts created from issuing and placing of securities by the state;*
- *Contingent liabilities considered to be public debt (the amount determined by the fiscal year and the risk-expense analysis on state-guaranteed loans)*[2].

According to geographical structure, public debt is divided into two categories: internal and external. At the same time, national legislation allows the government to borrow in national, as well as foreign currencies. It should be noted that in no case can state-owned assets and international reserves be used as a mortgage for public debt[3]. The upper limit of public debt, ratio of debt to GDP, ratio of debt to volume of goods and services exported, and ratio of public debt repayments to overall budget expenditures is determined by the law on the state budget for each year[4].

Brief analysis of the current situation

According to the Chamber of Accounts, the public debt of Azerbaijan was 17 004.7 million manat (9 967 million US dollars)[5] and per capita debt was 1 718.3 manat (1 010 US dollars) at the beginning of 2018[6]. The ratio of public debt to GDP was 24.3%, and the ratio to

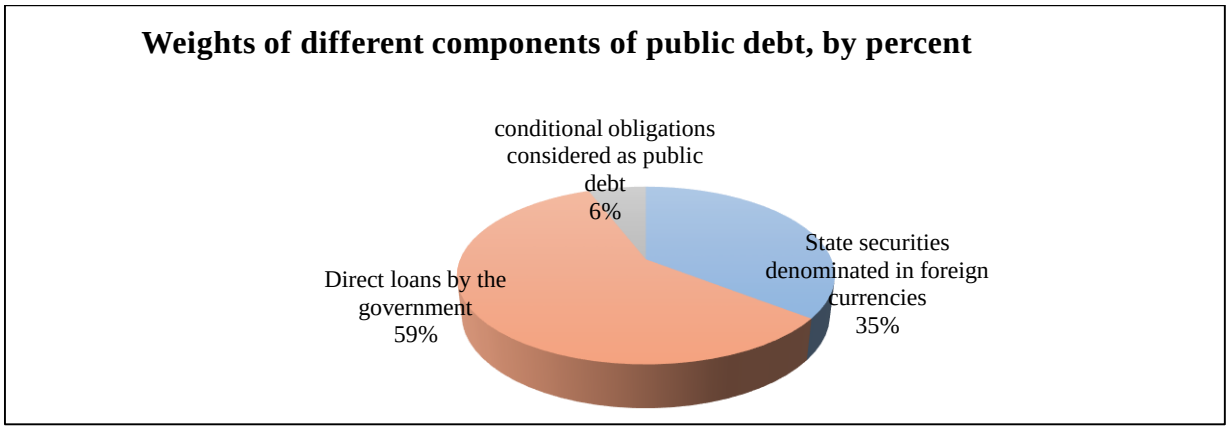
[1] "Dövlət borcu haqqında" Azərbaycan Respublikasının Qanunu, 22.05.2007, maddə: 1.1
http://www.e-qanun.az/framework/13680
[2] "Azərbaycan Respublikasında dövlət borcunun idarə edilməsinə dair orta və uzun müddət üçün Strategiya", 24.08.2018, səh: 8
https://static.president.az/media/W1siZiIsIjIwMTgvMDgvMjcvMjI0ODFuN2NnYl9fRE9WTEVUX19CT1JDVV9TVFJBVEVRX1lBXy5wZGYiXV0?sha=67f1b296c90ca1f2
[3] "Dövlət borcu haqqında" Azərbaycan Respublikasının Qanunu, 22.05.2007, maddə: 3.2
http://www.e-qanun.az/framework/13680
[4] "Dövlət borcu haqqında" Azərbaycan Respublikasının Qanunu, 22.05.2007, maddə: 6.0
http://www.e-qanun.az/framework/13680
[5] **NOTE**: the conversions used in this paper are calculated according to the exchange rate provided by the Central Bank on the appropriate day.
[6] Hesablama Palatası, ""Azərbaycan Respublikasının 2017-ci il dövlət büdcəsinin icrası haqqında" Azərbaycan Respublikasının Qanun layihəsinə və dövlət büdcəsinin icrasına dair illik hesabata Azərbaycan Respublikası Hesablama Palatasının Rəyi", baxış tarixi: 02.09.2018, səh: 256
http://sai.gov.az/upload/files/REY_ICRA2017_final.pdf

the country's strategic currency reserves was 23.8%[7]. During the same period, 1 029.3 million manat (605.1 million US dollars), or 6.1%, was internal debts while external debts amounted to 15 978.1 million manat (9 393.4 million US Dollars), which constitutes 93.9% of the total[8].

The structure of foreign debt at the beginning of 2018 was as follows:

- government securities denominated in foreign currencies: 3 331.4 million US dollars,
- direct loans taken by the government: 5 510.4 million US dollars,
- contingent liabilities recognized as foreign public debt: 556.5 million US dollars.

Figure 1: Structure of foreign debt, by percent



Source: Medium and Long Term Strategy on Public Debt Management in the Republic of Azerbaijan, 2018

81.1% of foreign debt is in US dollars, the rest is euro, SDR (Special Drawing Rights), Japanese yen and other currencies [see: Table 1].

Table 1: Structure of foreign debt by currencies, million US dollars

Currency	External debt as of 01.01.2018	Change from 01.01.2017
US Dollar	7623.5	30.2%
Euro	888	24.8%
SDR	570.4	6%
Japanese Yen	209.3	3.6%
Other	107.2	0
Total	**9398.3**	**26%**

Source: Chamber of Accounts of the Republic of Azerbaijan, "Comment on 2017 State Budget Implementation", 2018

[7] "Azərbaycan Respublikasında dövlət borcunun idarə edilməsinə dair orta və uzun müddət üçün Strategiya", 24.08.2018, səh: 9
https://static.president.az/media/W1siZiIsIjIwMTgvMDgvMjcvMjI0ODFuN2NnYl9fRE9WTEVUX19CT1JDVV9TVFJBVEVRX1lBXy5wZGYiXV0?sha=67f1b296c90ca1f2

[8] Hesablama Palatası, ""Azərbaycan Respublikasının 2017-ci il dövlət büdcəsinin icrası haqqında" Azərbaycan Respublikasının Qanun layihəsinə və dövlət büdcəsinin icrasına dair illik hesabata Azərbaycan Respublikası Hesablama Palatasının Rəyi", baxış tarixi: 02.09.2018, səh: 256
http://sai.gov.az/upload/files/REY_ICRA2017_final.pdf

As can be seen, foreign debt liabilities of the Republic of Azerbaijan increased by 26% in 2017. During the corresponding period, the aggregate public debt increased by 26.2%, or 3 533.3 million manat (2 078.3 million US dollars). Thus, at the beginning of 2017, aggregate public debt amounted to 13 471.4 million manat[9].

96.3% of the external public debt of Azerbaijan is included in the category of debt which should be repaid in 20 years [see: Table 2].

Table 2: Distribution of loan agreements by term, million US dollars

Repayment term	Amount as of 01.01.2018	Weight in total external debt
Up to 10 years	4241.3	45.1%
10 to 20 years	4807.1	51.2%
More than 20 years	350	3.7%

Source: Chamber of Accounts of the Republic of Azerbaijan, "Comment on 2017 State Budget Implementation", 2018

As predicted, growth in public debt continued in 2018. Thus, within the first six months of the current year, the foreign debt of Azerbaijan increased by 2.1% and reached 9.6 billion US dollars[10].

Loans guaranteed by the government

At the beginning of 2018, the total amount of loans taken with a state guarantee amounted to 21 billion 561.4 million manat, or 12 billion 682.4 million US dollars. 45.7% and 54.3% of the state guaranteed debt (which is 30.7% of GDP) is coming from external and internal sources, respectively.

54.3% of debts taken from foreign sources with state guarantees belong to the Southern Gas Corridor (SGC). In general, the major organizations that get state-guaranteed loans from external sources include:

- "Southern Gas Corridor" CJSC – 3 147.3 million US dollars;
- "Azerenerji" OJSC – 928.2 million US dollars;
- "Azerbaijan Railways" CJSC – 478.9 million US dollars;
- SOCAR – 460.6 million US dollars;
- Other institutions – 778.3 million US dollars.

The ratio of loans taken with state guarantees from external sources to GDP at the beginning of the year was 14%. It should be noted that the total amount of debt expected to be

[9] Hesablama Palatası, ""Azərbaycan Respublikasının 2016-ci il dövlət büdcəsinin icrası haqqında" Azərbaycan Respublikasının Qanun layihəsinə və dövlət büdcəsinin icrasına dair illik hesabata Azərbaycan Respublikası Hesablama Palatasının Rəyi", baxış tarixi: 02.09.2018, səh: 414
http://sai.gov.az/upload/files/ICRA-2016-SON_FINAL.pdf

[10] Maliyyə Nazirliyi, "Dövlət borcunun idarə edilməsinə dair orta və uzun müddət üçün Strategiya ölkənin maliyyə dayanıqlılığını daha da gücləndirəcək", 30.08.2018
http://www.maliyye.gov.az/node/2218

taken from foreign sources with state guarantees during the 2018-2025 period is 2 billion 735 million US dollars.

Debts incurred from domestic sources with state guarantees:

- Debts from securities issues by "Aqrarkredit" CJSC non-bank financial institution – 10 590.5 million manat (6 229.3 million US dollars);
- SOCAR - 321.7 million manat (189.2 million US dollars);
- Deposit Insurance Fund – 800 million manat (470.6 million US dollars)[11].

It should be noted that the borrowing of state-owned legal entities with state guarantee in Azerbaijan is carried out within the requirements of the Law "on Public Debt" and the Decree of the President of the Republic of Azerbaijan "on the Rules for Concluding Agreements of Taking Loans with State Guarantee"[12]. Under the current legislation, state-owned enterprises must obtain special approval from the Ministry of Finance since 2016 even when they are borrowing without a state guarantee[13].

In general, certain steps have been taken in recent years to improve the mechanisms of borrowing by state owned enterprises. However, public awareness and the transparency of public debt management in Azerbaijan is still assessed poorly. That is, short information about public debt can be obtained from the comments given by the Chamber of Accounts on the state budget. Yet, this information does not include indicators such as the use of borrowed funds, the effectiveness of borrowing, the total amount of guaranteed loans, the debt structure of the borrower, and the level of credit repayment of the borrower organizations. The Ministry of Finance publishes quarterly and yearly numbers on foreign public debt that reflects only a few common indicators, which are very weak in terms of information capacity. This problem reduces the responsibilities of organizations engaged in public borrowing by weakening public oversight mechanisms, increases risk of corruption and diminishes the effectiveness of the funds.

[11] "Azərbaycan Respublikasında dövlət borcunun idarə edilməsinə dair orta və uzun müddət üçün Strategiya", 24.08.2018, səh: 21-23
https://static.president.az/media/W1siZiIsIjIwMTgvMDgvMjcvMjI0ODFuN2NnYl9fRE9WTEVUX19CT1JDVV9TVFJBVEVRX1lBXy5wZGYiXV0?sha=67f1b296c90ca1f2

[12] "Dövlətə məxsus olan hüquqi şəxslərin daxili və xarici borcalması Qaydası"nın təsdiqi haqqında Azərbaycan Respublikasi Prezidentinin Fərmanı, 28.12.2018, maddə: 1.3
http://www.e-qanun.az/framework/34534

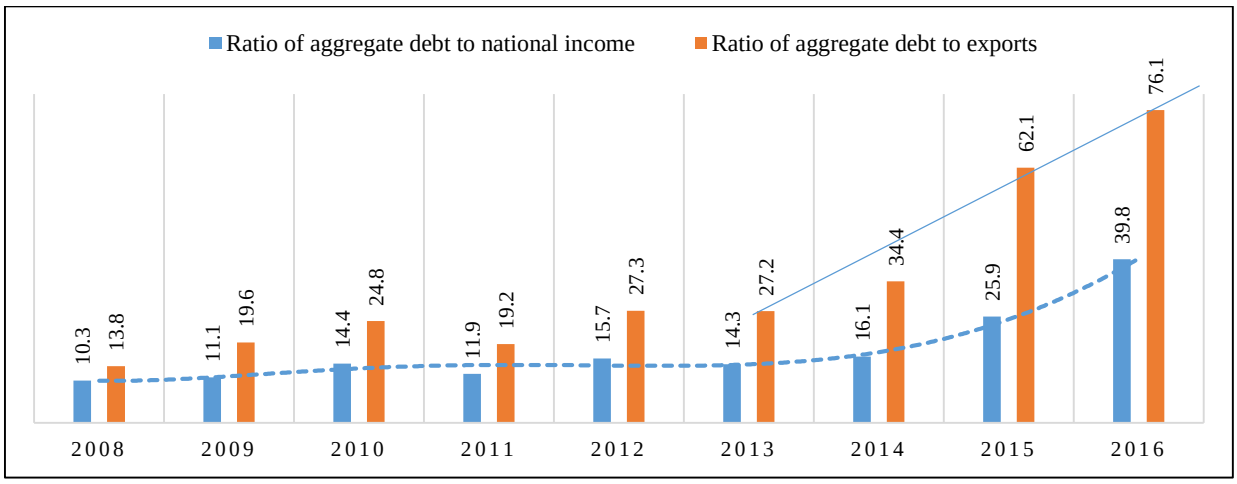
[13] "Dövlətə məxsus olan hüquqi şəxslərin daxili və xarici borcalması Qaydası"nın təsdiqi haqqında Azərbaycan Respublikasi Prezidentinin Fərmanı, 28.12.2018
http://www.e-qanun.az/framework/34534

Reasons for necessity of increasing government oversight

From the second half of 2014, external factors relevant to the Azerbaijani economy have changed significantly. The sharp decline in oil prices in global markets has led to a decline in the fiscal revenues of Azerbaijan. At that time, the government had large commitments in a number of areas, including the implementation of the Southern Gas Corridor project. In addition, there was a deficit in the balance of payments due to declining oil revenues, which ultimately made it impossible to keep the value of the national currency stable. Thus, the national currency (manat) lost 49.6% of its value in 2015 alone. As a result, the country's banking sector faced colossal losses. It should be noted that the situation made it impossible to continue the inefficient and corrupt management system found in many state-owned banks, which resulted in the government taking over responsibility of large debt obligations through restructuring.

With the problems indicated above, Azerbaijan's foreign debt liabilities, including the foreign debt of the state, began to increase dramatically. According to the World Bank, the amount of public debt was 19.5% in 2014-2016. Let us note that the growth of debt further accelerated with the transfer of the foreign debt of the International Bank of Azerbaijan in 2017.

Figure 2: Dynamics of the ratio of foreign debt of Azerbaijan to national income and exports (in public and private sectors), by percent



Source: World Bank, International Debt Statistics - 2018[14]

As can be seen from Figure 2, the ratio of foreign debt to GNI and exports has sharply increased since 2014. The main reasons for the increase are the following:

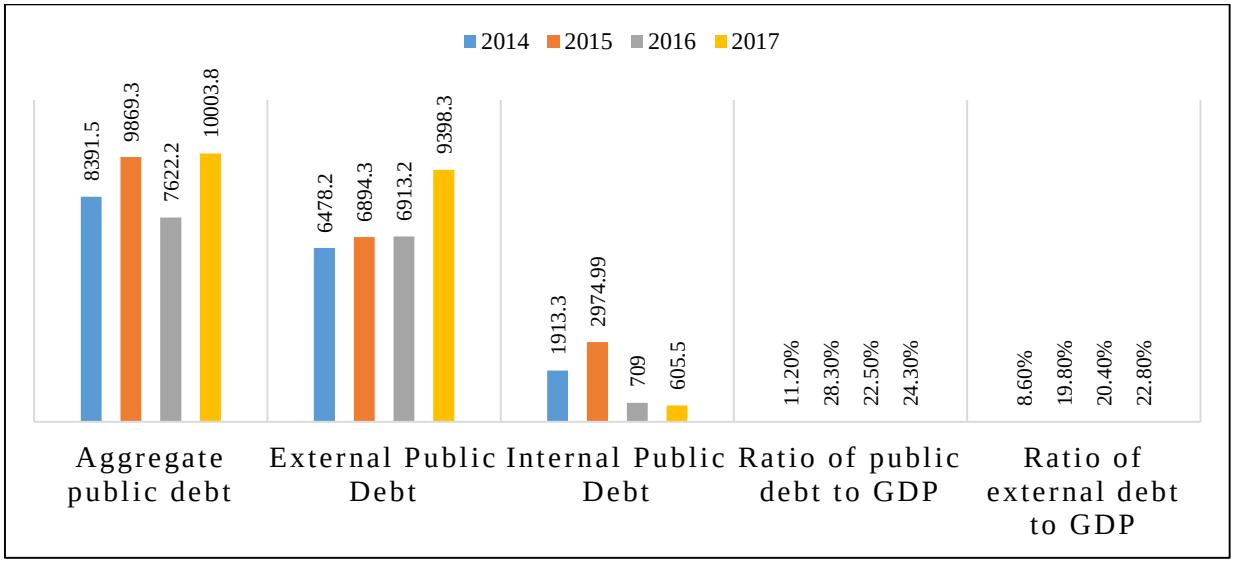
- Increase in the actual amount of debt;
- Decrease in national income denominated in foreign currencies after devaluation;
- Shrinkage in export volume due to lower oil prices.

The above-mentioned factors have resulted in a significant weakening of the country's foreign debt indicators.

[14] World Bank, «2018|İnternational Debt Statistics», baxış tarixi: 02.09.2018 http://datatopics.worldbank.org/debt/ids/country/AZE

In general, during the 2014 – 2017 period, Azerbaijan's aggregate public debt increased by 19.2% and foreign debt by 45.1%. The ratio of total public debt to GDP increased from 11.2% to 24.3%, and the ratio of external debt to GDP increased from 8.6% to 22.8%.

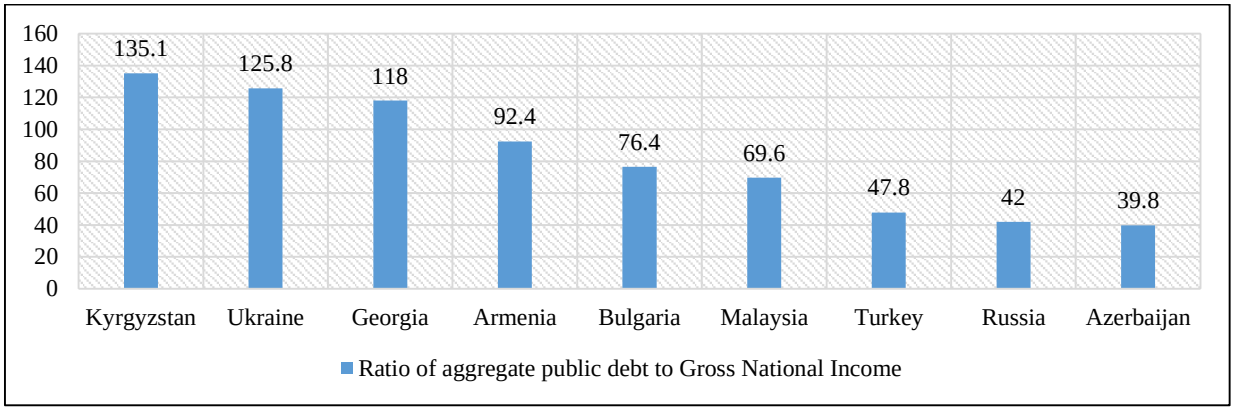
Figure 3: Dynamics of some public debt indicators (2014-2017)



Source: Comments by the Chamber of Accounts on execution of the state budget[15], Information by the Ministry of Finance on foreign debt[16], 2018

In spite of the above mentioned dynamics, the present level of public debt in Azerbaijan can be included in a relatively low risk group. That is, the ratio of debt to gross national income can be considered better in Azerbaijan than in many countries [See diagram 4].

Figure 4: Ratio of total public debt to gross national income, by percent



Source: World Bank, International debt statistics - 2018[17]

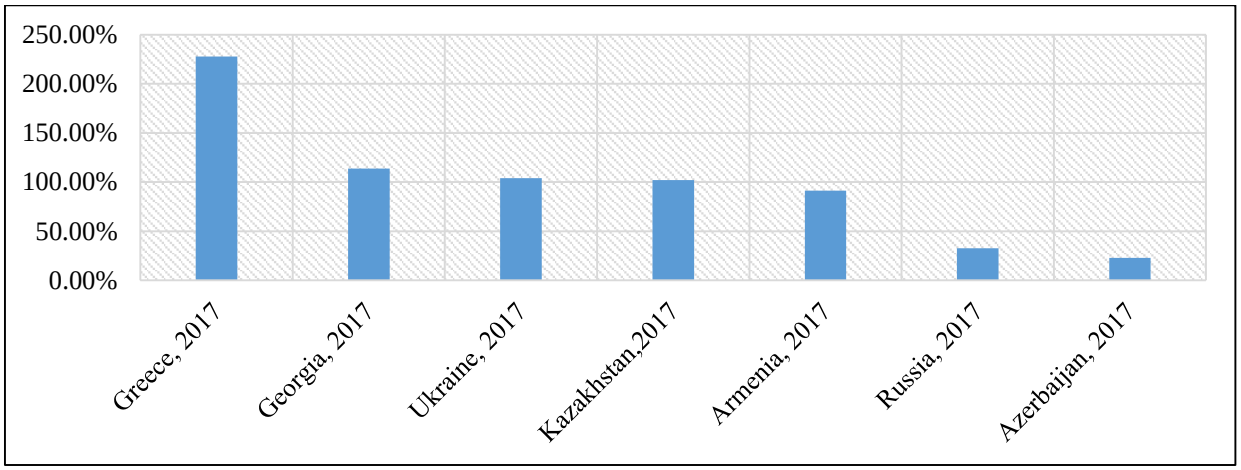
It should be noted that the ratio of aggregate public debt to gross national income at the end of 2016 was 53.3% for European and Central Asian countries, which is 13.5 percentage

[15] Azərbaycan Respublikası Hesablama Palatası
http://sai.gov.az/1/reyler/
[16] Azərbaycan Respublikasının Maliyyə Nazirliyi
http://www.maliyye.gov.az/en/node/1892
[17] World Bank, «İnternational Debt Statistics, 2018», baxış tarixi: 02.09.2018, səh: 13-14
http://databank.worldbank.org/data/download/site-content/IDS-2018.pdf

points higher than Azerbaijan's. However, the corresponding figure for middle income countries (including Azerbaijan) was 25.9%[18]. In other words, it is understandable that the state's debt policy has been revised.

The fact that about 95% of public debt is foreign debt liabilities is one of the factors increasing the risk level for the country.

Figure 5: Ratio of external public debt to GDP at the end of 2017



Source: CEIC[19], 2018

As can be seen, the ratio of Azerbaijan's foreign debt to GDP is the lowest in the region. However, weak diversification of the country's economy and exports as well as the dependence of fiscal revenues on the oil sector increase the risk of foreign debt obligations.

Another source of risk for public debt is the poor financial position of state-owned enterprises. Some of the loans taken by state-owned enterprises with state guarantees cannot be repaid and increases the state's fiscal burden. It should be noted that, as Minister of Finance Samir Sharifov said in his speech in Parliament in 2015, failure to repay state guaranteed credits by a number of state-owned enterprises is one of the key reasons behind the increases in foreign debt[20].

Thus, we can list several reasons for the necessity of increasing government oversight of public debt in Azerbaijan:

- Fast growth of public debt (starting from 2014);
- High level of dependence of fiscal revenues on oil;
- Poor ability of state-owned enterprises to pay back credits, obligation of repayment of debts taken with state guarantee at the expense of budgetary funds;
- Poor development of financial markets and lack of using alternative financial instruments by state institutions;
- Financial stability and expected risks for the country's credit rating.

[18] World Bank, «İnternational Debt Statistics, 2018», baxış tarixi: 02.09.2018, səh: 14
http://databank.worldbank.org/data/download/site-content/IDS-2018.pdf
[19] CEİC, External debt: % of GDP
https://www.ceicdata.com/en/indicator/greece/external-debt--of-nominal-gdp
[20] Modern.az, "Nazir Beynəlxalq Bankdakı yoxlamadan DANIŞDI: "Külli miqdarda vəsait girov olmadan kredit verilib", 02.10.2015
http://modern.az/articles/85987/1/#gsc.tab=0

A new strategic look on public debt: medium- and long-term Action Plan

Goals, targets and priority activities of the strategy

On August 24, 2018, the "Medium- and long-term strategy for public debt management in the Republic of Azerbaijan" has been approved[21]. Steady and manageable debt, improving risk management, and strengthening government infrastructure and control mechanisms over borrowing have been identified as key targets for the 2018 – 2025 strategy.

The objectives of the strategy are divided into three groups as below:

I. ***Ensuring sustainability of public debt with consideration to the needs of the economy.***

Main measurement indicators:

1. *Holding aggregate public debt / GDP < 30% principle during the 2018 - 2025;*
2. *Ensuring aggregate public debt / GDP < 20% target in 2025*

II. ***Borrowing with the lowest risk and minimal costs at the time of the government's financial needs.***

Main measurement indicators:

1. *Providing that the share of public debt denominated in foreign currencies does not exceed 87% of aggregate public debts by 2025;*
2. *Borrowing with variable interest rates not exceeding 56% of total debt portfolio*

III. ***Development of domestic financial markets.***

Main measurement indicators:

1. *Formation of a secondary market;*
2. *Matching issuance practices with market requirements.*

The priorities identified for achieving the goals of the strategy are as follow:

1. Ensuring aggregate government debt service expenses / total state budget expenditures < 15% in 2018 - 2025, and, if this is not possible, compensation of expenses by the means of internal borrowing;
2. Suspending borrowing by the state, excluding the projects included in the strategy. These projects include:

- Policy Based Loans (Asian Development Bank) – 500 million US dollars;
- Improvement of "Azerbaijan Railways" CJSC restructuring project of Baku – Yalama railroad line (Asian Development Bank and French Development Agency) – 325 million US dollars;

[21] "Azərbaycan Respublikasında dövlət borcunun idarə edilməsinə dair orta və uzun müddət üçün Strategiya", 24.08.2018
https://static.president.az/media/W1siZiIsIjIwMTgvMDgvMjcvMjI0ODFuN2NnYl9fRE9WTEVUX19CT1JDVV9TVFJBVEVRX1lBXy5wZGYiXV0?sha=67f1b296c90ca1f2

- Refinancing of government securities with foreign currency nominal value – 1 250 million US dollars;
- "Southern Gas Corridor" project – 2 250 million US dollars;
- Purchase of 30 passenger wagons from "Stadler" for "Azerbaijan Railways" CJSC – 134.8 million US dollars;
- Reconstruction works at "Azerikimya" PU – 350 million US dollars.

It is expected that the public debt of the above-mentioned projects will be 4 billion 809.8 million US dollars over 2018 – 2025. Of this amount, 2 075 million US dollars, or 43.1% of the funds, belongs to those directly borrowed by the state, while 2 734.8 million US dollars, or 56.9%, is included in the category of funds taken with state guarantees[22].

In order to achieve the targets set out in the strategy, it is planned to implement the following changes relevant to the institutional and legal framework:

- Strengthening legal support for strategic targets by making changes to the Law "on State Debt";
- Improving accounting mechanisms - Organization of accounting of debts by state-owned enterprises without state guarantees by the Ministry of Finance;
- Strengthening the internal institutional and logistical base:
    1. *application of IT system for public debt management;*
    2. *appointment of staff on analytical work (cost / risk analysis, as well as credit risk identification);*

As a result of the above-mentioned activities, it is projected that significant changes will be made in the amount of public debt, its ratio to GDP, geographical distribution (internal and external), currency structure, and component structure (direct debts, guaranteed loans, state bonds). According to forecasts, despite expecting growth in foreign public debt during 2018 and 2019, it will decline in later years. As a result, a 30.1% decline is expected when 2025 figures will be compared to those of 2017. During these years, expenses related to the repayment of foreign public debt will amount to 8 billion 500 million US dollars [see Table 3].

According to forecasts, over the next seven years the volume of domestic public debt will increase by 82%. During this period, the costs related to internal debt are expected to be 948 million manat (558 million US dollars).

[22] "Azərbaycan Respublikasında dövlət borcunun idarə edilməsinə dair orta və uzun müddət üçün Strategiya", 24.08.2018, səh: 12; 23, https://static.president.az/media/W1siZiIsIjIwMTgvMDgvMjcvMjI0ODFuN2NnYl9fRE9WTEVUX19CT1JDVV9TVFJBVEVRX1lBXy5wZGYiXV0?sha=67f1b296c90ca1f2

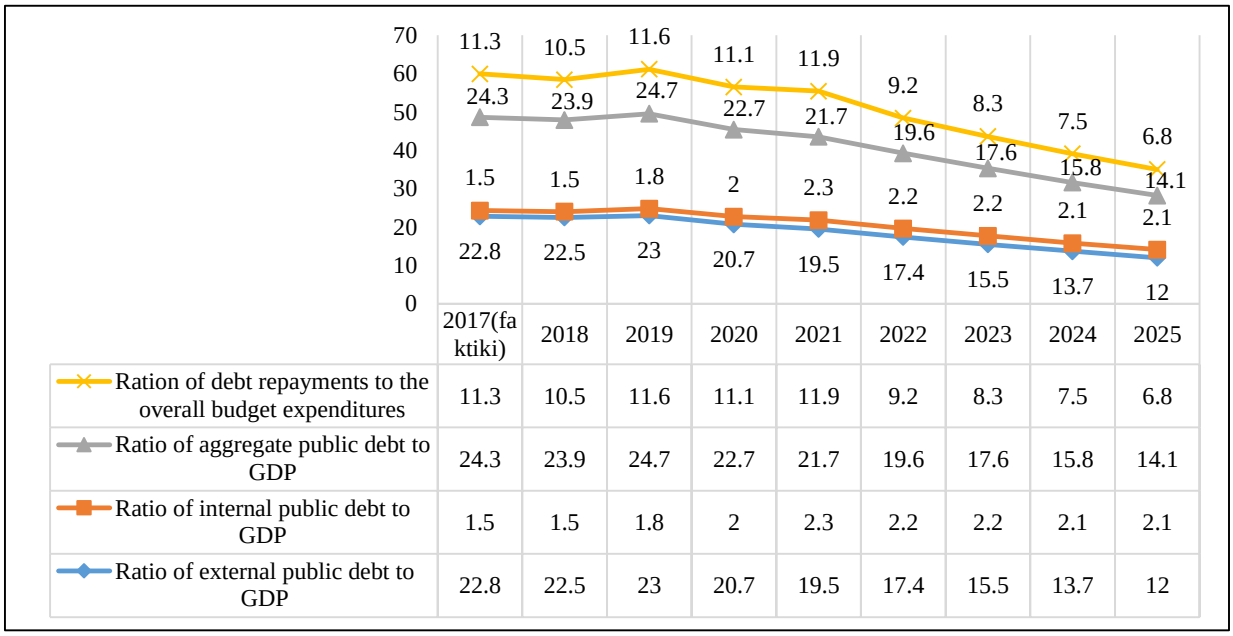
Table 3: Volume of internal and external debt and forecast of dynamics of expenditures towards debt, in billion

	Amount of external debt (US dollar)	Expenditures towards external debt (US dollar)	Amount of internal public debt		Expenditures towards internal debt	
			Manat	US dollar	Manat	US dollar
2018	9.7	1.242	1.1	0.647	0.090	0.053
2019	10.1	1.235	1.3	0.765	0.100	0.059
2020	9.8	1.193	1.6	0.941	0.110	0.065
2021	9.2	1.229	1.8	1.059	0.114	0.067
2022	8.5	0.987	1.9	1.118	0.124	0.073
2023	7.8	0.930	1.9	1.118	0.127	0.075
2024	7.2	0.863	1.9	1.118	0.137	0.080
2025	6.5	0.820	2.0	1.176	0.147	0.086

Source: Medium and long-term strategy for public debt management in the Republic of Azerbaijan, information has been generalized by the author, 2018 (note: conversions were based on the current official exchange rate when preparing the table)

By 2025, it is planned to reduce total debt to 7.7 billion US dollars. At that time, the ratio of aggregate public debt to GDP is expected to fall to 14.1%. Naturally, this indicator will also depend on factors such as the volume of GDP and the exchange rate of the national currency [see Figure 6].

Figure 6: Forecast of some indicators on public debt assessment, by percent



Source: Medium- and long-term strategy for public debt management in the Republic of Azerbaijan, information has been generalized by the author, 2018

Give that there is no change in state policy on borrowing during the upcoming years and the risk environment is stable, then the ratio of state debt to GDP is projected as shown in Diagram 6. In the next 7 years, the government estimates it will reduce the external debt rate from 22.8% of GDP to 12%, decrease expenditures towards debt repayments from 11.3% of the budget to 6.8%, and increase the ratio of internal debt to GDP from 1.5% to 2.1%.

Weak sides of the strategy

Activities that are planned to be implemented based on the "Medium- and long-term strategy for public debt management in the Republic of Azerbaijan" have more of a quantity characteristic. That is, the strategy envisages decreasing state debt, terminating debts on new projects over the next 7 years, resourcing borrowing from external to internal sources, and creating oversight of the currency structure of debt, all in order to ensure strengthened financial sustainability. However, no specific activities have been identified for debt management, improving borrowing mechanisms, and increased transparency in businesses that borrow with state guarantees, including strengthening their accountability and ensuring targeted and effective spending of the borrowed funds. This weakens the strategy, making it more of a 'problem solving' than new, quality approach.

In addition, the strategy does not analyze the needs of the Azerbaijani economy, including the needs of the public sector for financial support over the years 2018 - 2025. This observation reveals a risk to the targets of the strategy, shall the need for higher state borrowing arise.

Possible difficulties for strategic targets

Although the "Medium- and long-term strategy for public debt management in the Republic of Azerbaijan" envisages implementation of certain activities in these areas, we believe certain problems will arise in the realization of predicted public debt targets. These problems can be grouped as follow:

1. ***Inadequate infrastructure in the country to reach such targets*** – Targets such as ensuring sustainability and diversification of the economy, eliminating dependence on natural resources, and improving the production environment are only possible if infrastructure is further developed. However, the reconstruction process of the infrastructure of Azerbaijan cannot be considered as finished. Two months ago, the problem with the country's network of electricity supply showed that increasing demand in a short period of time could lead to failure of the low-quality system. Similar problems can also be observed in natural gas, water and sewage systems. In recent years, the development of agriculture has become one of the priority areas for employment and diversification of exports. This will increase the cost of land melioration in the following years. The need to reconstruct the railway infrastructure has arisen as a result of the country's transformation into a transit hub. Let us note that financial sustainability of state enterprises, including those listed above, has

significantly weakened over recent years as a result of long-term inefficient and non-transparent governance. For example, at the beginning of 2018, the retained losses of "Azerenerji" OJSC were 2 billion 123 million manat[23], net losses of "Azersu" OJSC for 2017- 508.3 million manat, while its retained losses were 5 billion 904 million manat[24], and the debt of "Azerbaijan Railways" CJSC was 2.83 times more than its capital[25].

2. ***Failure to maintain financial sustainability in public companies*** – Many state-owned enterprises fail to meet their debt obligations as a result of weak liquidity and inefficient management. It should be taken into consideration that the total amount of loans guaranteed by the state is 12.7 billion US dollars, or 30.7% of GDP. The likelihood of this debts becoming a burden for the state budget in the future is high. For example, 49.1% of domestic debt has been generated from securities emitted by "Aqrarkredit" CJSC. The existence of serious shortcomings in the operation of the organization and lack of transparency and accountability creates a major risk for the debt repayment process.

3. ***Volatility of the legal system*** – The practice of making frequent changes to Azerbaijani legislation is widely spread. This, in turn, increases the likelihood of target indicators for revenues of the state budget and state debt becoming a subject of amendments. As a result, the rules might be replaced by new ones and, consequently, the state's borrowing policy may follow an entirely different path.

4. ***Weak transparency and accountability in public funds management*** – In many state-owned enterprises, financial and operating activities are not transparent (ex. "Azerenerji" OJSC, "Azersu" OJSC etc.) and some other state-owned enterprises do not publicize their annual financial statements, in violation of the requirements set by law (ex. "Azerbaijan Railways" CJSC). This increases the risk of corruption during the management of funds and reduces their efficiency (ex. the experience of the International Bank of Azerbaijan: at the end, it was officially recognized that the bank attracted funds in an irresponsible way, with unofficial deals that did not require collateral with high liquidity levels[26]).

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