

COVID-19 Pandemic and Azerbaijan's Economy: Policy Lessons In Hard Times

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Abstract

Any fluctuation in oil prices and supply has a direct effect on Azerbaijan's economy. The government has started the implementation of several state programs to diversify its economy and to develop the non-oil sectors, using energy revenues. COVID-19 has broken out in such a period that the oil prices were already low. The Second Karabakh War has complicated impacts of the pandemic. Facing health, military and economic problems, Azerbaijan has fought on three different fronts. This study evaluates the effects of the pandemic on Azerbaijan's economy, suggesting that it will affect the oil and gas industry negatively in near future. It is argued that in a long term, the state will be pushed to restructure and transform the economy, to increase the share of the non-oil sectors and to open more space for renewable energy sources, taking advantage of the incomes of The State Oil Fund.

Keywords

Azerbaijan
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About Article

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COVID – 19 Pandemisi ve Azerbaycan Ekonomisi: Zor Zamanlarda Politika Dersleri

Özet

Petrol fiyatlarındaki ve arzındaki herhangi bir dalgalanma Azerbaycan ekonomisini doğrudan etkilemektedir. Hükümet, enerji gelirlerini kullanarak ekonomisini çeşitlendirmek ve petrol dışı sektörleri geliştirmek için çeşitli devlet programlarının uygulanmasına başlamıştır. COVID-19, petrol fiyatlarının zaten düşük olduğu bir dönemde patlak vermiştir. İkinci Karabağ Savaşı, pandeminin etkilerini daha karmaşık hale getirmiştir. Sağlık, askeri ve ekonomik sorunlarla karşı karşıya kalan Azerbaycan, üç farklı cephede savaşmıştır. Bu çalışma, pandeminin Azerbaycan ekonomisi üzerindeki etkilerini değerlendirmekte; onun yakın gelecekte petrol ve gaz endüstrisini olumsuz etkileyeceğini; uzun vadede ise devleti, Devlet Petrol Fonu'nun gelirlerinden yararlanarak ekonomiyi yeniden yapılandırmaya ve dönüştürmeye, petrol dışı sektörlerin payını artırmaya ve yenilenebilir enerji kaynaklarına daha fazla alan açmaya zorlayacağını öne sürmektedir.

Anahtar Kelimeler

Azerbaycan
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Makale Hakkında

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Introduction

Multidimensional economic and political interdependencies between actors have blurred the distinction between domestic and foreign policy, starting a debate among theorists of International Relations whether Security Studies should maintain its traditional emphasis on military threats to the security of states or widen its focus (Hough, 2008). While traditional security comprehension refer to military threats, widened focus of security understanding involves a broad range of issues, such as health, rights, environment and climate change, natural disasters, industrial accidents, crimes, social identity, famine or hunger (Hough, 2008). A new approach emerging through the 1990s has been characterized as the "Copenhagen School", focusing on the widening scope of security studies. According to it, existential threats and vulnerabilities that need endorsement of emergency measures taken by a securitizing actor must be considered within the security issues (Buzan et al., 1998). Next studies, supporting the arguments of Copenhagen School, attracted attention to the concept of "human security" rather than state security or security of the sub-state groups. Since 1990's states deal with issues of environment, climate change, crime, clean energy, identity based problems at the international area rather than military issues. Considering that these issues directly threat the individuals, it is inevitable to place human at the center of the security.

Similarly, an increasing importance of economic interactions between states after 1960's made the national economies more vulnerable to foreign developments, which is one of main reasons of redefining security also. Since 1970's oil shocks, security of demand and security of supply of fossil energy resources are the issues of non-traditional security studies as well (Belyi, 2012). Oil price fluctuations can be considered as a serious threat for both oil importing and oil exporting countries with their remarkable impacts on macro-economic indicators (Taghizadeh Hesary et. al., 2015). Analysing the significance of oil for oil exporting states, Kitous et al. (2016) evaluated the impacts of lower oil prices on their political and economic stabilities. Using income per capita data of oil exporting countries, Human Development Index of the UNDP and Political Stability Index of the World Bank, Norway has been considered as a reference country with highest income per capita and human development opportunities and Canada has been considered as a reference country with highest political stability. The research findings shows that any change in oil prices has a direct effect on GDP and government revenues (per capita) of all oil exporting countries. However, producing oil quantities, production costs, share of fossil energy related sectors in total economic activities, degree of economic diversification, dependence rate on oil sector are the variables that determine the level of vulnerability of oil exporting countries, effect of price fluctuations and elasticity of response to changes (Kitous et al., 2016). Findings of research made by Alekhina and Yoshino (2018) also confirm the notable and negative effects of oil price fluctuations on the main macroeconomic indicators of oil exporting countries, exactly real GDP, CPI inflation rate, interest rate, and exchange rate. Examining the impacts of oil price uncertainty on industrial production and the exchange rates in oil exporting countries, Smiech et al. (2021) found that uncertain oil prices lead to continuous decrease in industrial production, whereas the permanency of drop varies from country to country. Price uncertainty causes the exchange rate depreciations in oil-exporting countries. Similarly, the development level of countries determines how long this effect will continue (Smiech et al. 2021). Oduyemi and Owoeye (2020) attracted attention to poor human development indicators and unsustainable social spendings of oil exporting countries as a result of high dependence of government finance on oil incomes.

On the other hand, in the Preamble part of the World Health Organization (WHO) Constitution it is emphasized that “the health of all peoples is fundamental to the attainment of peace and security (WHO, 2006). COVID-19 is a new experience for the world countries in globalization era regardless the development level of their economies. While globalization has encouraged the unrestricted moving of goods, services and financial sources all over the world, facilitating the movement of people as well, “new normal” order requires a social distance and disconnections. The consequences of the outbreak not yet accurately measured due to continueing cases in several countries. But in any case, beginning from March 2020, it has slowed the growth of even the most developed countries. However, in this process, the socio-economic impacts of pandemic are not same in countries that took strict preventions to manage the course of pandemic. While some states compete with pandemic crisis more cautiously, for some countries the consequences are more costly than others.

Azerbaijan - an oil exporting country - is the largest economy among the post-Soviet states, which is often criticized by international organizations for its high dependence to oil sector. COVID-19 pandemic has revealed how dangerous this dependency is for the Azerbaijanian economy. As the previous fluctuations in oil prices caused relatively smaller crises, the country's economy has recovered quickly. The effects of pandemic period are compared with the impacts of the Great Depression and the Azerbaijanian economy is faced with a situation that has not experienced before. In addition to the internal dynamics of the country, the fact that all world states are affected by the crisis makes the situation more complex and multi-dimensional.

Therefore, economy of Azerbaijan is shaped by internal and external factors during the pandemic period more than before. The conflict with neighboring Armenia requires a significant cost, both due to military expenditures and socio-economic problems of internally displaced people from the occupied areas. On the other hand, country's budget revenues decreased as a result of low oil prices. Underdeveloped non-oil sectors cannot provide sufficient contribution to the country's economy. On the other hand, oil depreciated due to economic, political and geopolitical reasons. Meanwhile, the pandemic has broken out and the world economies have entered a serious recession period. Sectors such as transportation, tourism, and agriculture that could contribute to the Azerbaijanian budget have lost a business. Although the 44-day war with Armenia has ended in victory, the government has a serious agenda with a large number of political and socio-economic issues that needs urgent and permanent solutions.

The overwhelming majority of previous studies for Azerbaijan have focused on the impacts of oil price fluctuations in ordinary periods of time. The novelty of this study is that it analyze the effects of energy prices volatility in extraordinary times, when the COVID-19 pandemic has already paralyzed all economic activities worldwide. Thus, reviewing relevant literature, analytical reports and recent data, this chapter tries to analyse the impacts of the COVID-19 on the Azerbaijanian economy in the light of oil price fluctuations. In the first section, it is aimed to present a brief outlook of Azerbaijanian economy just before the COVID-19 pandemic period in the light of official statistical data. It is considered that such an outlook will be useful to estimate and evaluate future developments in the oil and gas industry, which is a backbone of Azerbaijanian economy. The second section of study focuses on the assessments, taking into account the impacts of the coronavirus on Azerbaijanian economy. Paper's final part involves the concluding remarks about the subject.

Materials And Methods

The article focuses on Azerbaijan's economy during the COVID-19 pandemic, impacts and responses during crisis. Azerbaijan's economy is highly dependent on oil revenues. Oil price fluctuations and the Second Karabakh War have enforced to deal with the effects of the pandemic. The analyses included herein should be seen as a case study. The submitted findings are results of evaluations taking into the consideration the simultaneous impacts of oil price fluctuations and the war during the COVID-19 pandemic. Research is conducted using the data collected by various methods, including a review of the literature, public documents and statistics, reports and official declarations and news. The data obtained allowed to analyse the impacts of the COVID-19 on Azerbaijan's economy and government's responses.

The following hypotheses were formulated in the study preparation phase:

- High dependency of Azerbaijan's economy on oil sector affect the country's economy more negatively during the unexpected situations such as war, pandemic or instability of energy prices.
- Considering that unexpected crises such as climate change, pandemic, and natural disasters will occur more frequently in the future, it is necessary to ensure sustainable development of non-oil sectors urgently.

The research limitations included the availability of the academic articles and studies about the subject due to its newness.

Azerbaijani Economy In The Pre-Pandemic Period

It is not a surprise that the energy sector has been a driving force of Azerbaijani economy after gaining independence as a country is well-known with its rich oil and natural gas resources for a long time. Azerbaijan's diversified economic structure has failed after the collapse of the USSR. It has faced with Armenian military aggression since 1988 - the last years of the Soviet Union and lost 20% of its territory. The ceasefire agreement was signed on May 12, 1994, however, an armed conflict has continued for years between sides.

Leaving behind the challenged economic transformation period of the 1990s, Azerbaijan has achieved a rapid development exporting its oil to the world markets through the Baku-Tbilisi-Ceyhan pipeline. "Contract of the century" of 1994 (Masimov, 2018) and adopted constitution of 1995 has been the main motivations for improvement of legal and regulatory structure of the market economy and large amounts of foreign investment to the country. Azerbaijan's economy has become one of the fastest growing economies among the former USSR states as a result of large amounts invested in fossil energy production.

"Contract of the century" forms the basis of Azerbaijan's oil strategy. The significant volume of hydrocarbon reserves and investments involved in mentioned agreement has laid the foundation of the reconstruction of Azerbaijan's oil production facilities in accordance with international standards both financially and technically. "Contract of the century" opened the way for signing of thirty-four agreements with foreign companies in addition (Masimov, 2018). Involvement of foreign giants in Azerbaijan's oil industry has significantly increased production volumes. It made the pipeline capacities inadequate to transport oil to the world markets. The Baku-Tbilisi-Ceyhan pipeline has been built due to the low capacity of existing pipelines and, most importantly, in order to diversify the pipelines to the energy markets without being dependent on a single route.

Thus, the oil strategy of Azerbaijan has focused to the following goals: Firstly, to involve the oil giants in country's oil industry, by this way, to recover, strengthen capacity and modernize its infrastructure, to increase the production capacity, to reach world energy markets. Secondly, to diversify the transportation routes as well as to secure the accessibility both technically modernizing them and creating alternative pipelines. Thirdly, to use oil incomes for economic recovery and social development as well as non-oil sectors. The country's oil strategy has been founded on these three pillars mainly. On the other hand, a structure dependent on oil has emerged in the Azerbaijani economy in terms of production and foreign trade.

In the last thirty years a crude oil composes approximately 80% of country's total export revenues (The State Statistical Committee, 2021a). A significant increase in its GDP and GDP per capita has been observed especially after kick-off the alternative pipeline projects (Table 1). Since the rapid growth in the Azerbaijani economy has been based on the oil sector, it has been easily affected by the world economic crisis and oil price fluctuations.

First operation years of giant companies in the oil and natural gas sector of Azerbaijan have coincided with a period of pick up of globalization when the demand for energy resources has increased. This situation has created a challenge in terms of diversification of the Azerbaijani economy. On the other hand, during the same period, the amount of expenditures on multidimensional socio-economic problems and defense has increased due to the occupation of country's territories by Armenia.

In 2008-2009 all major economies have faced a recession. Consequently, there has been a decrease in the oil production of Azerbaijan, mainly exporting its oil to European countries. Simultaneously, decline in oil demands has led to a reduction in state revenues. Recovery in world economies beginning from mid-2010 has been reflected oil sector dominated Azerbaijanian economy also (Table 1).

Table 1. The Share of Oil and Non-Oil Sectors in GDP

Years	GDP in total (million USD)	GDP per capita (USD)	Contribution of oil-gas sector to GDP (%)	Contribution of non-oil sector to GDP (%)
2005	13238,7	1579,8	44.1	48.4
2006	20983,0	2471,6	53.8	40.7
2007	33050,3	3841,7	56.1	37.3
2008	48852,5	5603,3	55.4	37.9
2009	44297,0	5018,2	45.1	47.0
2010	52909,3	5922,0	48.1	45.2
2011	65951,6	7285,0	49.6	44.5
2012	69683,9	7594,3	44.7	49.1
2013	74164,4	7977,4	40.9	52.5
2014	75234,7	7990,8	36.3	56.3
2015	52996,8	5561,5	28.3	62.8
2016	37862,8	3928,6	32.4	59.5
2017	40867,9	4198,5	35.6	57.3
2018	47112,9	4797,8	40.2	52.0
2019*	48047,6	4851,2	36.8	54.4

* On the base of primary data

Source: Author's creation based on data of The State Statistical Committee (2021a & 2021b).

Country's socio- economic development strategy has been supported by implementation of state programs of 2004-2008, 2009-2013, 2014-2018 and 2019-2023. With these programs, it is aimed to take important and wide-ranging steps towards effectively assess and develop the economic potential and natural resources of the regions, thus to diversify the economic activities, to achieve high employment rate and living standards.

Table 2. GDP by sectors of economy (% at factor cost)

Years	Industry	Agriculture, forestry and fishing	Construction	Transport and communication	Net taxes	Other sectors
2005	49,5	9,1	9,0	7,3	7,6	17,5
2006	57,4	7,1	7,7	6,6	5,5	15,7
2007	59,7	6,7	6,4	7,3	6,6	13,3
2008	58,7	5,6	7,0	6,7	6,7	15,3
2009	49,2	6,1	7,2	8,6	7,9	21,0
2010	51,7	5,5	8,1	7,4	6,8	20,5
2011	53,8	5,1	8,0	6,7	5,9	20,5
2012	49,4	5,1	10,1	6,6	6,2	22,6
2013	45,4	5,4	11,6	6,1	6,7	24,8
2014	41,0	5,3	12,6	6,3	7,5	27,3
2015	32,9	6,2	12,0	8,0	8,9	32,0
2016	37,1	5,6	10,5	8,5	8,1	30,2
2017	40,1	5,6	9,6	8,3	7,1	29,3
2018	44,5	5,2	7,7	7,8	7,7	27,1
2019	41,4	5,7	7,3	7,8	8,7	29,1

* On the base of primary data

Source: The State Statistical Committee (2021).

In order to recover the economy in a short time, the Azerbaijanian government has focused on the oil sector, as a result of what the fossil resources have become the main determinant in almost all areas of the country. The "lion's share" of Azerbaijan's state budget has been contributed by the State Oil Fund and taxes paid by oil companies. The fact that oil is a non-renewable resource and the fluctuations in oil prices on the world energy markets make it necessary to develop the non-oil sectors. Thus, huge amount of oil revenues has expanded the state's ability to influence the non-oil sectors. Table 1 shows that the share of non-oil sectors in GDP has increased in last years in total. However, analysing general macroeconomic data, it is understood that this is a relative rise as a result of decreasing share of oil sector in GDP. Table 2 shows the share of GDP by sectors of economy. Similarly, analyzing the table, no any significant jumping is observed on a non-oil sector basis. Although an agricultural sector is one of the main sectors with its share in Azerbaijan's GDP and contribution to job creation, the amount of foreign investment in this field has been overshadowed by the country's oil and gas industry. Considering that 15% of silk, 2.4% of wool, 7% of raw cotton, 29% of grapes, 4.6% of

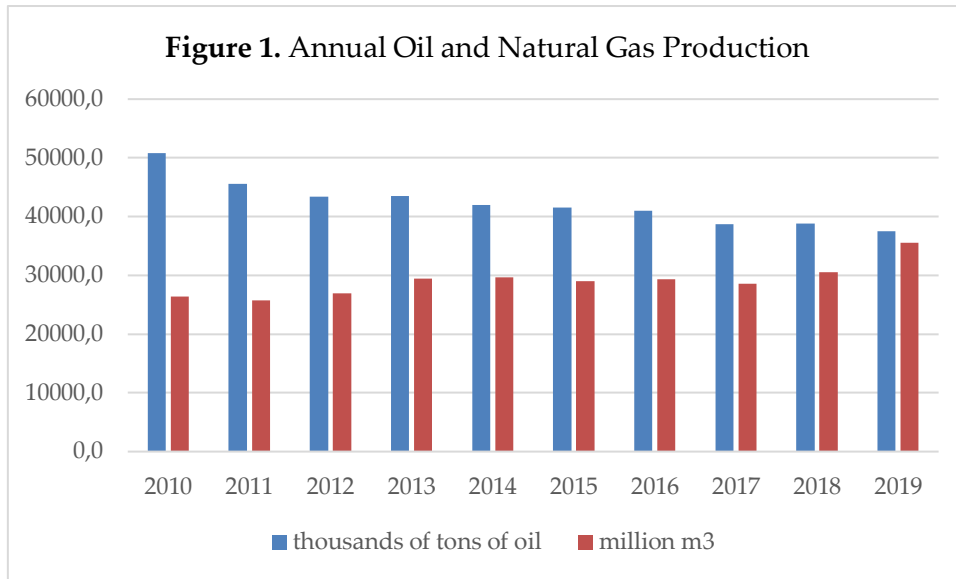
tea and 10% of fruit have been produced by Azerbaijan during the Soviet Union (Huseyn, 2011), it is detected that the agricultural sector has decreased significantly among the economic sectors.

In fact, government's oil strategy has been successful in achievement of the goals determined in the first two pillars. In recent years, the country's oil industry has strengthened financially and technically with foreign investments. However, analysing the level of achievement of the purposes stated in the third column, it is seen that the industrial sector has developed based on oil and natural gas, the other sectors cannot exceed a certain level and remain weak. Therefore, socio-economic development has been limited to some parts of economy as well as society accordingly. The seriousness of the situation has appeared more clearly beginning from mid-2014, enforcing the government to implement the devaluations.

Following the price uptrend - 107.95 USD per barrel - in June 2014, sharp drop - 44.08 USD per barrel - has been recorded in January 2015. Not surprisingly, a drop of 59.2% in a such short time has deeply affected economy of Azerbaijan, resulting in 3% slowing down of country's growth.

Progress in economy sharply slowed following a price escalation between 2003-2007, when GDP boomed by an average of 21 % yearly. In 2013 it was recorded 5.8 % (Bagirova and Antidze, 2015). Due to the decrease in oil prices, it has become necessary to adapt the foreign exchange rates and Manat to new oil prices. The decision of Central Bank of Azerbaijan (CBA) to experience the floating exchange rate system has resulted in two devaluations in the same year – in 2015. First devaluation has happened on February 21, 2015, when the Manat has lost 33.8% value against the Euro and 33.9% against the US dollar. Facing second devaluation by the end of 2015, the Azerbaijanian currency has hit 47.88% lows against the Euro and 47.63% against the US dollar (Hurriyet, 2015).

Since 2008 global financial crisis that has also strongly affected oil prices, Azerbaijan has started to participate at OPEC meetings as a non-OPEC member country. Similarly, beginning from mid-2014 Azerbaijan has started to reduce oil production in parallel with the decrease in prices, supporting the decisions taken within the scope of OPEC + (Figure 1). On the other hand, Azerbaijan has been among the twenty four largest oil producing countries of 2019. 0.8% of 95.192 thousands of barrels of oil per day has been produced by Azerbaijan in 2019 (BP, 2020). In the shade of the insufficiency of non-oil sectors, the government has tried to compensate the loss of income due to lower oil prices with natural gas exports (Figure 1). Increasing demand tendency for natural gas worldwide within the framework of climate change and environmental issues has created an advantageous situation for Azerbaijan in this sense. Timely construction of the TANAP and TAP natural gas pipelines transporting Azerbaijani natural gas to the energy-dependent European countries and Turkey is a logic option in the current circumstances.



Source: Author's creation based on data of SOCAR Azerbaijan (2021).

While the state programs and measures implemented by the government have laid the foundation for the development of the non-oil sectors and has been accepted as a priority area by the state, recession due to unpredicted decrease of oil prices has questioned an effectiveness of the reforms in non-oil economic activities in Azerbaijan.

On the other hand, conflict with Armenia has enforced Azerbaijan to allocate a significant part of its budget to defense expenditures. Thus, in spite of economic recession beginning from mid-2014, military spendings of Azerbaijan have been increased. According to the World Bank (2020), there has been a steady rise in country's military budget in last five years (Table 3).

Table 3. Azerbaijan's Military Expenditures

Years	Military expenditure (% in GDP)	Military expenditure (billions USD)
2010	2.79	1.477
2011	4.67	3.080
2012	4.66	3.246
2013	4.54	3.368
2014	4.56	3.427
2015	5.47	2.901
2016	3.69	1.397
2017	3.82	1.529
2018	3.62	1.672
2019	3.10	1.854

Source: The World Bank (2020a).

It is predicted that Azerbaijanian government will allocate 2.33 billion USD for its defence and security in 2021, which was 2.27 billion USD in 2020 (Mammadov, 2020). As stated in revisions in budget law of 2020, the total amount of state budget for 2021 has been determined 15.2

billion USD. A share of defence and security spendings will constitute 15.3% of total budget expenditures.

Table 4. The Main Macroeconomic Indicators

Description	2014	2015	2016	2017	2018	2019
Gross domestic product, mln. Manats	59014,1	54380,0	60425,2	70337,8	80092,0	81896,2
Income of population, mln.Manats	39472,2	41744,8	45395,1	49187,9	53103,7	57035,0
Income of population, mln.Manats	444,5	466,9	499,8	528,5	544,6	635,1
State budget revenue:						
mln.Manats	18400,6	17498,0	17505,7	16516,7	22508,9	24398,5
as a percentage of GDP	31,2	32,2	29,0	23,5	28,1	29,8
State budget expenditure:						
mln.Manats	18709,0	17784,5	17751,3	17594,5	22731,6	24425,9
as a percentage of GDP	31,7	32,7	29,4	25,0	28,4	29,8
State budget deficit (-), profit:						
mln.Manats	-308,4	-286,5	-245,6	-1077,8	-222,7	-207,8
as a percentage of GDP	0,5	0,5	0,4	1,5	0,3	-0,03
Population savings in banks (end of the year), mln.Manats	7188,4	9473,9	7448,7	7561,2	8375,4	8637,9
Population number (end of the year), thsd.persons	9593,0	9705,6	9810,0	9898,1	9981,5	10067,1
Fixed assets (end of the year), mln.Manats	110677,9	124008,4	169120,3	182788,5	198970,4	208940,2
Loans to economy (end of the year), mln.Manats	18542,6	21730,4	16444,6	11757,8	13020,3	15298,2
Investment to economy, mln.Manats	21890,6	20057,4	22706,4	24462,5	25877,0	24986,6
Current account balance, USD mln.	10430,5	-222,5	-1363,4	1684,6	6051,1	4364,9

Source: The State Statistical Committee (2021c).

Table 4 reflects the outlook of the Azerbaijanian economy before the pandemic. While the population of the country has constantly growing, the economy has contracted, budget revenues have felt, and there have been the deficits in the budget. As stated earlier, the most important reason is that the economy is heavily dependent on oil. On the other hand,

ineffective usage of the revenues collected in the Oil Fund during periods with high oil prices and unreadiness of the budget for a possible extraordinary situation has also made the situation even more difficult.

In the light of the above mentioned, it can be considered that Azerbaijan has entered into the worldwide pandemic period in the shadow of harsh conditions. Occupied territories, the frequently violated ceasefire regime and possibility of war with Armenia, lower oil prices and insufficient investments and reforms in non-oil sectors for successful economic diversification have already created a wide range of socio-economic problems in total.

COVID-19 And Azerbaijanian Economy: Assessments For The Future

When the virus named COVID-19 has been first identified in the Chinese city of Wuhan in autumn of 2019, nobody could predict such heavy consequences for the countries and humanity. The WHO announced a highly infectious coronavirus as a worldwide health danger. In a short time the speed of infection has determined the level of protection that has involved a large number of measures taken by the governments, not desiring to import COVID-19. Border closures between countries and travel restrictions have been the pick point resulting in the greatest disconnection of the world since the Second World War. Imposing lockdowns and limited free movements have disrupted the economic circulations among sectors, where only aviation industry has lost 90% of its business (IATA, 2020). The unexpected situation has enforced the IMF to update its growth forecasts for countries, calling 2020 as "a year like no other" (IMF, 2020a). IMF has estimated an overall increase at -4.9% for 2020 that has been 1.9% lower than its predictions in April 2020. The updated estimates have proved that an effect of pandemic on economies has been greater than it expected. Anticipating the global growth at 5.4% in 2021, this forecast for the 2021 GDP is still 6,5% points lower comparing with pre-pandemic estimations in January 2020 (IMF, 2020b).

Economic recession of the countries also reduced the global oil demands, causing hit of oil prices, which had already been at low levels since mid-2014. Booming shale oil production by the USA from mid-2014 has made it a cost determinant in international oil markets (Stocker et al., 2018).

Imperative drastic measures taken by China due to the COVID-19 outbreak have reduced Chinese industrial production. Simultaneously, the demand for oil in China has declined, who is one of the the largest oil importers. Combining with the disruptions in the global supply chain and the reductions in transportation, oil demands have began to drop more than predicted. On the other side, OPEC members, led by Saudi Arabia, have planned to reduce oil production in order to interfere with falling prices. However, it has been difficult to convince Russia. Thereupon, negotiations between Saudi Arabia and Russia under the OPEC+ umbrella have been failed. Thus, oil prices started to decrease rapidly.

This situation has doubly affected Azerbaijan's economy. Azerbaijan itself is an oil country. Moreover, two other oil giants – Russia and Iran are the neighboring countries has respectively 8% and 1% share in Azerbaijani foreign trade in the last decade. Thus, recession in Russian and Iranian economies has also indirect negative effects on Azerbaijan's foreign trade. Drop in oil prices has followed by two waves of mitigation measures to keep spread of virus under control. These have reduced the country's GDP 2.7% in the first half of 2020 (The World Bank, 2020b). GDP has accounted 72432,2 million Manat in 2020 (The State Statistical Committee of the Republic of Azerbaijan, 2022). The overall economy contracted by 4.3%, while the oil sector fell by 7%. Production of crude oil was 8% lower compared to 2019. The decrease in production

is mainly related to the realization of Azerbaijan's commitment to the OPEC+ deal. Meanwhile, natural gas production increased by 6.3%. Coming to the non-oil GDP, it decreased by 2.6% and accounted for 70.1% of the total GDP. The non-oil sector grew by 0.7% if the stagnating construction and COVID-19 affected tourism stripped out. Tourism sector experienced a 58.9% downfall due to travel restrictions constraining non-oil GDP growth, while the construction sector shrank by 8.7%. Non-oil manufacturing is the highest growing industry in the economy (18%), which is mainly thanks to the effect of "whitening" and realization of public investment on specific segments of the industry, like chemicals, metallurgy, and pharmaceuticals. Inflation remained stable in 2020 maintaining inside the lower interval of the Central Bank's target range (IMF, 2021). As mentioned earlier, the non-oil sectors have not been developed already enough to compensate for the contraction in the country's economy caused by low oil prices. The measures taken due to the pandemic have negatively affected the existing capacity in the non-oil sectors. Service sectors, particularly retail, hospitality and construction have been strongly affected during the quarantine regime (The World Bank, 2020b). The same has happened with natural gas sector. Compared with oil sector, natural gas export can be considered a new income source for the Azerbaijanian budget. Low oil prices and anti-COVID-19 restrictions have dealt a double blow to Azerbaijan's economy (Konarzewska, 2020), on the back of what external and fiscal surpluses have turned into deficits (EBRD, 2020a). Economic decline has revealed the vulnerabilities of country's banking system to crises. In fact, the 2008 financial crisis, developments in 2014 and the devaluations in Manat in 2015 were serious warnings for it. On the other hand, the level of public debt is still not highly dramatic in Azerbaijan and there is still fiscal space due to that The State Oil Fund is still able to reduce the economy's burden (CAREC Institute, 2020).

After detection of pandemic cases confirmed by the state authorities on February 29, 2020, The COVID-19 Operational Headquarters has been established by the government and operational teams within several public offices. Action Plan has been prepared by the Cabinet of Ministers for the implementation of the president's order dated March 19, 2020. It involves a series of acts for minimizing effects of the COVID-19 outbreak as well as acute shifts in world energy and stock markets on macroeconomic stability. CBA has been assigned to take specific response measures.

On the other hand, government has provided supportive financial packages valued at 2.5 billion Manat – nearly 1.597,26 million USD (Table 5) for balancing the losses during COVID-19 period. It corresponds to 3.39% of GDP of 2019. It is aimed to assist entrepreneurs, employees and unemployed citizens. However, experts have found the packages too limited comparing with the impacts of outbreak (Konarzewska 2020).

Table 5. Key Economic Responses Taken by Azerbaijan

Measure	Details
Liquidity Support - Forex operations	April 2020: CBA, with the contribution of the State Oil Fund, conducted scheduled and extraordinary foreign exchange auctions, and satisfied all demands for foreign currency at the announced 1.7AZN/USD rate.
Credit creation - Interest rate reductions	March 2020: CBA left the refinancing rate unchanged, but raised the floor of the interest rate corridor (within a de facto floor system). May 2020, CBA lowered the ceiling of the interest rate corridor. June 2020: CBA decided to reduce the discount rate. September 2020: CBA has lowered its interest rates.

Credit creation - Other measures supporting long-term lending	March 2020: The authorities have announced their intention to extend the blanket deposit guarantee until December 2020 irrespective of deposits' amount, currency and banks' financial standing. April 2020: Suspension of inspections of credit institutions. December 2020: regulatory requirements for the classification of loans have been relaxed and dividened payments have been limited until April 2021. Loan classification concessions were applied to interest-subsidized business loans and restructuring of loans issued at the expense of state funds.
Credit creation - Loan guarantees	April 2020: Entrepreneurs get state guarantee for 60% of their new bank loans and the government subsidizes half of the interest on guaranteed loans from the state budget; overall state support at 294 million USD. CBA also extended its guarantees on insurance premiums.
Direct long-term lending - Forbearance	April 2020: CBA announced a moratorium on late fees and interest rate penalties. December 2020: Credit organizations were advised not to accrue additional penalty interest, penalties, and other penalties until 1 April 2021, as well as to submit negative information on borrowers to the credit bureau with a special note.
Health and income support - Health support	July 2020: Installation of modular hospital complexes in various regions of the country. August 2020: Increase in salaries of medical personnel. Foreign medical staff with extensive experience were brought to the country to work with Azerbaijan's medical personnel. January 2021: Start of import of new vaccines against coronavirus.
Health and income support - Income support - Tax and contribution rates reduction	April 2020, Tax exemptions for micro-enterprises and value-added tax (VAT) exemption for some food and medicinal products, as well as the raw materials that are necessary.
Health and income support - Income support - Subsidies to individuals and households	April 2020: Announced social package included creation of 50,000 paid public jobs, tuition support for socially vulnerable students, financial support for mortgage and credit guarantee mechanism, support for communal fees, financial support for vital passenger transport activities, payments in the amount of living wage to 200,000 unemployed citizens.
Health and income support - Income support - Subsidies to business	April 2020: 588 million USD for the government's subsidization of 10% of the interest for one year of existing company loans. May 2020: 50 million USD (of the USD200 million swap with the European Bank for Reconstruction and Development (EBRD)) is allocated as support to local firms, including smaller viable enterprises experiencing temporary difficulties. August 2020: The government announced two financial support packages for pandemic-affected industries that did not implement significant reductions in the number of employees and for individual (micro) entrepreneurs.
Budget reallocation	August 2020: The Parliament passed a revised 2020 budget which reflected a lower oil price (USD 35 a barrel) and growth assumptions (-5%).
Non-Economic Measures -	The government imposed travel restriction measures, including border closures, restriction of domestic and international movements, public

Measures affecting travel and transport (local and international)	transportations, closure of airports and transportation. Restrictions have been gradually relaxed in parallel with the number of pandemic cases.
Others	A special quarantine regime has been introduced by the government, involving restrictions on mass activities such as commercial activities, gatherings, food and beverage, entertainment, education and etc.. The spread of infection has enforced the authorities to prolong a strict quarantine regime. Restrictions have been gradually relaxed in parallel with the number of pandemic cases.

Source: Author's creation based on data of Asian Development Bank (ADB) (2021).

Alongside taken measures in order to remove or at least to reduce the impacts of pandemic, the government has decided to restructure the economy. Within the context of the Action Plan, Azerbaijan Investment Holding has been created on November 07, 2020. The aim of establishment such an organization is the management of all state-owned companies and enterprises from a unique center on behalf of the state, to ensure the transparency and economic effectiveness of their activities, competitiveness and investment programs. Among the activities of Azerbaijan Investment Holding it is planned to improve the management of state-owned companies, to apply corporate standards and ensure financial transparency and to develop the privatization program for state-owned enterprises. This decision is one of the significant steps taken in recent years to ensure transparency in public activities and fight against corruption. Corruption and lack of transparency in Azerbaijan is an issue frequently criticized by international organizations. In this sense, the government must ensure transparency, fair competition and the well operation of free market conditions in order to ensure and maintain socio-economic stability in the current situation and to overcome future economic crises that may arise due to unpredictable reasons like COVID-19.

While the economic difficulties have reached their peak with the pandemic restrictions, in July 2020 Armenia's cease firing in the Tovuz region, which is far from the Karabakh region of Azerbaijan, but close to the strategically important Baku-Tbilisi-Ceyhan oil pipeline, has brought many developments that have totally changed the balances in the South Caucasus region. The deaths of high-ranking Azerbaijani officers during fights have caused serious social reactions in the country. Groups of young people in particular have organized demonstrations in the streets of Baku, calling the government for war with the slogans: "Let's die fighting instead of pandemic". As stated before, peace negotiations between the two countries were inconclusive, and the Azerbaijani officials have frequently made statements about war and military operations. Thus, the war has started on September 27, 2020 and ended with the victory of Azerbaijan on November 10, 2020. Although the reclaim of the lands has made forget the socio-economic problems of the society for a short time, it has loaded serious costs for the government for a long term. Reconstruction of reclaimed lands, resettlement of internally displaced people from these regions, state aid to martyrs and veterans are only a part of this cost.

It is difficult to measure the full cost of pandemic for the Azerbaijanian economy for now. But in Transition Report 2020-2021, EBRD has explained its expectation by 3.0% contraction in 2020 and recovery by 2.5% in 2021 (EBRD, 2020b). However, the World Bank (2020b) has projected 4.2% decrease in Azerbaijan's economy, estimating 1.9% growth for 2021. ADB's forecasts for

Azerbaijan is close to the World Bank's projections. Forecasting 4.3% contraction in 2020, ADB predicts 1.9% growth in 2021 (ADB, 2020). However, IMF expects -4.0% of decrease in real GDP of Azerbaijan. Its estimation for 2021 is 2.0% growth in real GDP (IMF, 2020c).

It is clear that lower oil incomes restricts the government's opportunities to fund the rest of the economy and any price fluctuation in world oil markets directly affect the other sectors also (Zulfigarov and Neuenkirch, 2020).

On the other hand, in their statements officials of the WHO warn states and governments about the possibilities of similar outbreaks again in the future. In this sense, a significant part of the fight against any pandemic, like COVID-19 may be possible by reducing the mobility of people and goods. Such a measure means restricting traditional economic activities as do the states now (Uste and Aydin 2020). In any case, serious economic, social, political and cultural changes are experienced all over the world due to the COVID-19 outbreak. "New normal order" will cause many people to be unemployed. Most businesses already adopted to work distantly. Educational institutions are planning to deliver a certain part of the lessons online. Examples in this regard can be diversified.

In the light of the above mentioned, profound governmental reforms are urgently needed in the Azerbaijanian economy. These reforms must be multidimensional, addressing following objectives:

- * To pave the way for development of private sector; to decrease the role of state in economy, to speed up the structural changes, to improve operational experiences of market economy and corporate governance.

- * To encourage the non-oil sectors. Robust environment for development of private sector will develop the non-oil sectors also.

- * To invest in renewable sector and to create new job opportunities. It must be considered that world oil giants are in transition due to the climate and environmental issues.

- * To develop national labour force in digitalization era.

- * To create new generation labour force.

- * To address assistance packages for socially vulnerable citizens.

- * To give priority to the transport, agriculture and health sectors.

- * To regulate the financial sector.

- * To normalize the relations with Armenia.

- * To promote regional cooperations.

But in any case, in order to achieve these goals, it is needed to benefit usefully from the funds of State Oil Fund of Azerbaijan. It should be considered that oil-dependent economies can no longer be as sustainable as before in the "new normal order". Obviously, diversifying economic activities in an digital-dominated era will also reduce the risks that may occur during the crisis. The private sector of Azerbaijan needs to be developed rapidly in order to eliminate its financial vulnerabilities, to expand and diversify its economic activities. It must be noted that liberal economic models that dominate the world in the globalization process, with their emphasis on free movement and trade, have predicted an environment where fewer wars and conflicts will take place, promoting social peace and welfare (Uste, 2020b).

Conclusion

In this paper, it was tried to analyze the current situation of Azerbaijan's economy in the light of oil price fluctuations and the COVID-19 pandemic impacts. Considering that Azerbaijan is an oil exporting country and its economy highly depends on fossil energy incomes, it is

extremely difficult times for the country. During the 2008 global financial crisis, Azerbaijan had an experience due to the decreasing oil demand. However, COVID-19 is a pandemic resulting in an emerging, rapidly evolving situations. From an international politics's perspective, the pandemic period has also started a new era in which the basic motivations that have been influential in the functioning of the international system throughout history are no longer valid (Uste, 2020a). Oil prices, which have been falling sharply since mid-2014, have made Azerbaijan's economy more vulnerable to the effects of pandemic. Coincidence of two different crises has seriously threatened the Azerbaijani economy. War with Armenia has additional costs for Azerbaijan. Majority of previous researches have investigated the effects of oil fluctuations on the oil exporting countries. However, this paper focuses on impacts of both crises and war simultaneously, reviewing recent literature and data of international organizations. This is justified by scarcity of academic studies investigating the effects of both oil fluctuations and COVID-19 on economies of oil exporting countries during wartime. In this context, it is expected to contribute to the literature with current study.

It is clear that macroeconomic indicators of oil exporting countries are highly sensitive to oil price fluctuations. Unexpected pandemic and unpredictable war with Armenia made the situation more complicated for Azerbaijan's economy. Overlapping these three issues in an inopportune time enforces the government to achieve the sustainable and stable development of economy. Therefore, ensuring transparency, increasing the share of non-oil sectors in GDP, providing market economy conditions for the development of the private sector and encouraging the transition to renewable energy sources are the most important lessons that must be learned in such difficult period.

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