

Top story	3
PASHA Bank	5
Interview	6
Sector	8
Economics & finance	10
Chart	14
News in brief	15



## UK and Azerbaijan to increase local participation in energy sector

The UK Trade and Investment (UKTI), Azerbaijan's Ministry of Economy and Industry, and oil companies Socar and BP have launched a programme that would increase the local participation in the Azerbaijani energy sector. Azerbaijan has already achieved a high percentage of local content in the energy sector as far as human resources are concerned, with over 80% of the workforce being local. The recently launched programme would address other areas, such as manufacturing of equipment locally.

The programme would initially focus on increasing local manufacturing capabilities of components

and spares used in drilling, of machinery assembly, and training of local personnel in specialist services, with the aim of improving efficiency and reducing production costs in the oil and gas sector. On October 29, a delegation of 26 British energy companies met with 30 Azerbaijani companies to set the basis for a three-year cooperation in knowledge transfer.

"Socar has been paying great attention to local content development in the oil and gas sector and, in cooperation with BP, we have achieved successful results in this area in recent years. For example, most of manufacturing and construction



contracts in SD2 projects have awarded to joint ventures consisting of local and international companies. Therefore, there is huge potential for local and international companies, and we believe that this cooperation will bring a lot of success in nearest future," said Rovnag Abdullayev, president of the Azerbaijani oil company Socar.

Meanwhile, Irfan Siddiq, British ambassador to Baku, told the media that the UK is "determined to make this partnership programme an integral part of our overall commercial activities in Azerbaijan. We see Azerbaijan as a key for the wider Caspian region". His Azerbaijani counterpart in London, in the meantime, stressed the economic benefits of the programme to Azerbaijan's economic growth.

Commercial relations between the UK and Azerbaijan are already very strong, with the UK

being the leading foreign investor in Azerbaijan. UKTI, the institution that promotes British commercial interests abroad, placed Azerbaijan on the list of high value opportunities (HVO) in February, reflecting the strong interest that the UK continues to have in the Caucasian country.

According to Campbell Keir, director of UKTI's energy and infrastructure teams, future opportunities in Azerbaijan for British energy companies are the development of the Shah Deniz II gas field, which will deliver 16bn cubic metres (cm) of Azerbaijani gas to Turkey and Europe starting in 2018; enhanced recovery techniques at Azerbaijan's largest oilfield - Azeri, Chirag and Guneshli; and the Absheron gas field, which will be operated by France's Total and could export as much as 7.8bn cm of gas starting in 2021. ●



## Supporting Non-oil Sector Development in Azerbaijan



**European Bank**  
for Reconstruction and Development



— [www.aic.az](http://www.aic.az) —

T: +994 12 488 8010

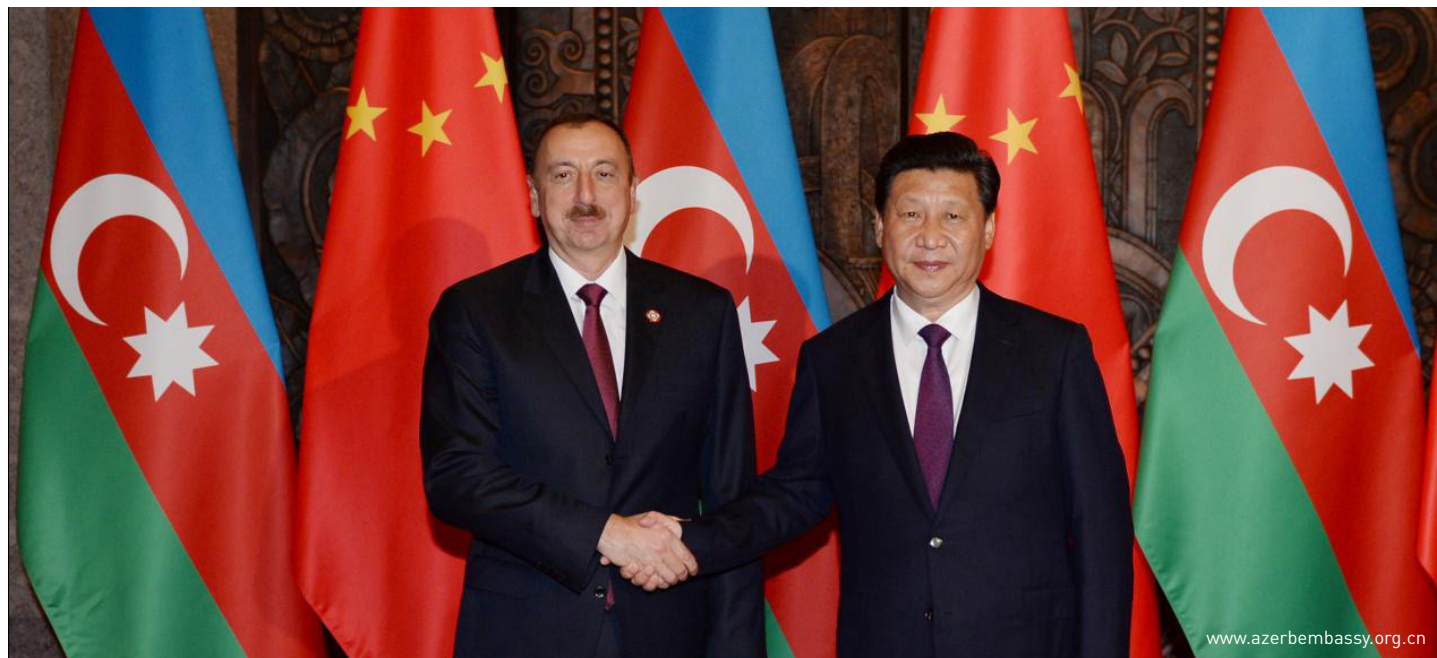
F: +994 12 488 8012

[info@aic.az](mailto:info@aic.az)





## Top story



### China and Azerbaijan show the Silk Road way

On the occasion of Azerbaijani President Ilham Aliyev's historic visit to China in early December, he and his Chinese counterpart Xi Jinping signed a number of agreements furthering bilateral co-operation, most notably a memorandum of understanding (MOU) on the construction of the Silk Road Economic Belt.

"The signing of the MOU shows that the substantial cooperation between the two countries has entered into a new stage," Xi told Aliyev according to CCTV.

Meanwhile, President Aliyev noted that, "China and Azerbaijan provide stable and safe conditions for successful and sustainable development. We intend to protect mutual interests and fruitful cooperation. Therefore, the development of cooperation in all spheres... is very important. There is a long-term connection between Azerbaijan and China."

After the two heads of state witnessed the signing of bilateral agreements on trade, education, transport, energy and the judiciary, Xi told reporters that the two countries would work together on big projects in energy, communications and infrastructure. He added that China was willing to increase financing for such projects and to work together on the transport corridor, as well as to expand people-to-people ties through exchanges between parliaments, social organisations, youth groups and media.

Shortly afterwards, Aliyev met with Chinese Prime Minister Li Keqiang to discuss avenues of future cooperation. The former welcomed Chinese companies to come and invest in Azerbaijan, and to set up manufacturing and industrial facilities there, calling China "a close friend of Azerbaijan". Seconding him, Li encouraged Chinese companies to tap into the opportunities in Azerbaijan.

## Building on a solid foundation

Aliyev's visit to China builds on solid foundations for bilateral cooperation, for the two countries already engage in more than \$700mn in trade annually and there have been growing investment flows between them. Between 2004 and 2011, 40 Chinese companies set up shop in Azerbaijan and 16 Azerbaijani companies in China. And the numbers are growing, with Chinese telecommunications giant Huawei recently announcing plans to expand in Azerbaijan in 2015- 2016.

But the crown jewel for bilateral cooperation, and the topic that has been the subject of negotiations for many years has been the Silk Road trade corridor – the re-emergence of an ancient route linking East Asia and Europe through Central Asia. Through the Silk Road Economic Belt and the 21st-century Maritime Silk Road (also known as The Belt and Road) projects, the route could significantly enhance China's trade with Europe and Central Asia, would integrate the economies of the countries it traverses and generate direct and indirect investment and jobs in Eurasia.

"Considering the geographic local of Azerbaijan, it could play an important role in the new Silk Road and would develop our sea, air, road and railway connections. Azerbaijan is one of the most important points along the Silk Road. We are confident about building this transportation corridor, and we are also one of its initiators," President Aliyev said in a 2014 interview.

Xi revealed the plans for the new route, which would include a land and a maritime component, in September and October 2013. To finance the giant project, China set up a \$40bn fund in November 2014 called the Silk Road Fund, and set up a multilateral lender with an authorised capital of

\$100bn called the Asian Infrastructure Investment Bank (AIIB) to help provide financing for other countries involved in the project.

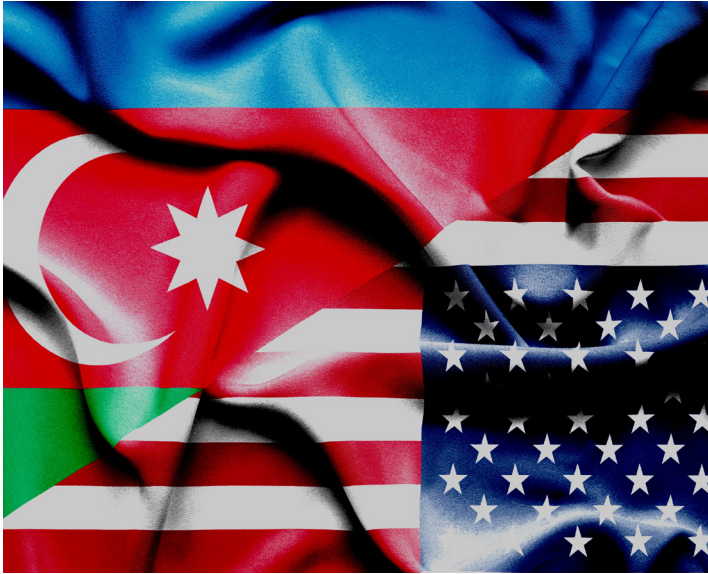
But Azerbaijan is unlikely to need a lot of financing for the project, because it has been hard at work improving its connectivity for years. The country boasts a new deep-water seaport in Alat, 60km from the capital Baku; an expanded Heydar Aliyev International Airport in Baku, a new terminal at which was inaugurated this year; a multitude of road projects aimed at improving north-south and east-west connectivity; a modern railway system, which is integrated with the Georgian and Turkish railway networks through the Baku-Tbilisi-Kars line, and which will be similarly integrated with the Iranian railway system. So the relatively tiny Azerbaijan is well positioned as a transit point for freight from China to Europe and vice versa.

The speed at which the country adapted its freight capacity and regulations to accommodate Turkish trucks after they were banned from crossing the Russian border points to the fact that Azerbaijan already has a great capacity for freight transport, and that it can quickly adapt to changing geopolitical factors that affect trade, aspects which were likely not lost on its partner China.

Meanwhile, Aliyev's visit to China and the MOU on the The Belt and Road corridor could not have come at a better time. Just as his visit was wrapping up, the first container train carrying consumer electronics from South Korea was shipped to China, loaded on a train via East and Central Asia, shipped across the Caspian Sea from Kazakhstan to Azerbaijan, and again loaded on a train heading to Istanbul via Georgia. The entire journey took 15 days – 25 days less than it would have taken if the freight were shipped by sea. ●



# PASHA Bank



## PASHA Bank participates in US trade mission to Baku

PASHA Bank participated in business meetings held on the occasion of a US trade mission visit to Baku on November 18-20. Organised by the US Azerbaijan Chamber of Commerce with support from other institutions, the event aimed to diversify trade between the US and Azerbaijan away from energy.

According to Taleh Kazimov, chairman of the board of PASHA Bank, the visit enabled US companies to learn more about the Azerbaijani market, which could result in greater bilateral trade. "As an active supporter of Azerbaijan's real

economy, PASHA Bank greatly supports foreign businesspeople visiting Azerbaijan, as this helps to improve business relations, expand trade and increase investment flows into the country. PASHA Bank is ready to contribute to developing international business relations and be the financial partner of choice for businesspeople looking to enter the Azerbaijani, Georgian, or Turkish markets."

Bilateral trade, which reached \$927.9mn in January-October, points to a greater potential to expand commercial ties in other areas, including telecommunications, information technology, petrochemicals, healthcare and engineering.

"Azerbaijan is a very important trading partner for American business. During my time serving in Baku, I saw first hand the tremendous potential for bilateral commercial cooperation," Michael Lally, deputy assistant secretary at the US Department of Commerce, said in a statement. "The goal of this trade mission is to open doors to tremendous new export opportunities and work to attract new investment to Azerbaijan, which will further develop the close relationships between the two economies.

Meanwhile, thanks to its subsidiaries in Georgia and Turkey, PASHA Bank is uniquely positioned to support foreign investors interested in the burgeoning Azerbaijan-Georgia-Turkey economic triangle. ●



# Interview



## AccessBank sees Azerbaijani businesses thinking consolidation and efficiency

The 34% February devaluation of the Azerbaijani currency, the manat, and the decline in oil prices over the last year have negatively impacted banks in Azerbaijan, but some like AccessBank have weathered the storm better than others.

Founded by international financial institutions in 2002, the country's sixth largest bank by assets, AccessBank's investment grade rating of 'BBB-', the highest in the Azerbaijani banking sector, was recently affirmed by rating agency Fitch, reflecting its "sound financial standing", according to Michael Hoffmann, chairman of the management board. "The bank's asset quality is very good and

we are outperforming the market in this important indicator, just like in previous years," Hoffmann explains.

Indeed, at a time when the rate of non-performing loans (NPLs) at the country's largest banks has risen to double digits, AccessBank has managed to maintain its NPLs to less than 5% of its total loan portfolio. "This is the result of our responsible lending practices and the close relations we enjoy with our clients," Hoffmann elaborates.

Many international observers believe that the devaluation was necessary and a natural step for Baku to take to protect its foreign currency reserves against the external pressures on the manat. Helping in the aftermath has been Azerbaijan's central bank, Hoffmann says, which is providing currency swaps and hedges and by "injecting local currency liquidity into the banking sector" at critical moments.

That is not to say that 2015 has been an easy year for the bank, for it has been "facing a weakening demand for new loans and lower loan amounts on average...compared to the past". But it has managed the situation well enough to prompt Hoffmann to be cautiously optimistic. "We expect a solid growth result in 2015, which will, however, be more modest compared to previous years," he says. Case in point, AccessBank stayed in profit in January-September, although profits declined from AZN32mn (\$41mn at the pre-devaluation exchange rate) in January-September to AZ6.8mn (\$6.5mn) in 2015.

Banks and businesses in general have been focusing on efficiency and consolidation this



year, and AccessBank is no exception. In October, the bank recently launched its internet banking platform and will continue to invest in e-banking technologies, “in order to further enhance efficiency and service quality”. But while Internet banking makes client operations more efficient, AccessBank does not have plans to “cut back on its branch network at a large scale. AccessBank has a strong foothold and an extensive client base, especially in the agricultural sector in rural areas” – a segment that will continue to be strategic for the bank and which requires a physical presence in the areas it services.

## What's in store

Hoffmann notes that Azerbaijan has started to diversify its economy in reaction to the decline in oil prices, by enhancing the value chain of its oil and gas production. “The petrochemical park in Sumgait is a good example of this,” he says, and it will be one of the drivers for economic growth in 2016.

Another factor is Russia, which many believe has reached the bottom of its economic slowdown this year. “The development of the Russian economy could represent an upside for the economic development in the next year... The agricultural sector could benefit from such a development, as Russia has always been an important export destination for Azerbaijani agricultural producers,” he adds.

Regarding the banking sector, there are two important trends to watch out for in 2016. One

is the evolution of oil prices, which could lead to a second devaluation, and another one is consolidation in the sector, although that has been a topic for discussions for several years and there are inconclusive results so far.

While Hoffmann did not want to dwell on the likelihood of a second devaluation, he said that banks should be prepared in case it does take place. “Our bank is prepared should there be any significant changes in the exchange rate, since we maintain a balanced currency position. At the same time, AccessBank strives to provide manat-denominated loans to its customers as much as possible, in order to mitigate potential risks that arise for clients from changes in the exchange rate.”

The banking sector has seen a minor consolidation in recent years, thanks to the fact that the regulator increased the minimum capital requirement for banks up from AZN10mn (\$9.5mn) to AZN50mn (\$47.6). Since January, the central bank revoked the licenses of seven banks, leaving 41 banks operating in the market. But whether the trend will continue is uncertain, Hoffmann believes. “Consolidation in the banking sector has been discussed for many years, but has not started to take place yet. Discussions keep going back to the same question of what is the adequate number of banks for such a market. The adequate number is difficult to determine since, even if the total number of ... banks sounds high, they are operating in many different market segments,” he concludes. ●

# Sector

## Bakutel



### **Bakutel brings international tech to Azerbaijan as local companies eye global markets**

December is the month of telecommunications in the Azerbaijani capital of Baku, when local and international telecom and IT companies gather at the largest information and communications technology (ICT) event in the Caucasus. This year's edition of Bakutel attracted representatives from 203 companies and 21 countries, who arrived on the Caspian shores to tout their products in one of the region's most promising markets.

And touting they must, for Azerbaijan has numerous plans in the works, ranging from the upcoming launch of its second satellite to a national broadband connection, 4G and 5G technologies, fibre optic projects, e-government, and cloud computing. For those with ideas but without a line of production, the country's High Tech Park offers the setup to incubate tech-related ideas and to turn them into patents.

The highlight of the exhibition and conference was undoubtedly the national space company Azercosmos, which signed an agreement with France's Arianespace for the launching of its second telecom satellite into orbit. The country already has one telecom satellite on orbit, Azerspace-1,

which was launched in February 2013 and which services clients in Azerbaijan, but also from the Middle East, Europe, Africa and Central Asia. The new satellite will be named Azerspace-2 and join a fleet of three, which also includes Earth observation satellite Azersky launched in June 2014.

"This new satellite will provide Azercosmos with additional capacity for the increasing demand in the region, and will allow us to continue to bring the best service to our customers," Rashad Nabiyeu, Azercosmos chairman and CEO, told local media in November.

#### **An outward-looking sector**

Azerbaijan has been on the radar of the world's leading tech companies for several years now. As recently as October, Chinese giant Huawei announced plans to expand on the Azerbaijani market, while Western companies like Google, which participated in Bakutel for the first time this year, appear to have similar intentions.

But for all of Azerbaijan's domestic potential, its budding IT sector is looking to export its solutions to markets as far away as Africa and Latin America. Leading companies like navigation software producer Sinam, IT services provider Ultra and application developer Simbrella have been exporting their know-how for several years now, inspiring their competitors to join the export bandwagon.

At Bakutel, Sinam created a consortium together with two other local companies, Bestcomp and Cybernet, and filed a bid with the government of Tanzania for the provision of an integrated profit management system. The consortium, which will be working with Tanzanian company MFI Document Solutions, won the bid after competing against 40 other submissions.



Azerbaijan Export & Investment  
Promotion Foundation



AZERBAIJAN INVESTMENT COMPANY



Sinam is best known for its navigation software, but the company had provided numerous IT solutions throughout the years, ranging from e-government solutions to freight management systems. After running projects in Central Asia, the company also participated in a bid to provide software solutions for the exploration of the Arctic.

Other IT companies that originated in Azerbaijan now boast global networks and operations that span several continents. Application developer Simbrella, for instance, started off modestly in Baku in 1999, but has since expanded to 15 other markets, including the Ghana, Russia, Georgia, Canada, Hungary and Uzbekistan, and boasts a subscriber base of 120mn for its various applications. Simbrella's leading solution has been Simkredit, an application that allows users top up their SIM card balance using their phone, but the company has dabbled in projects as diverse as tourism applications and taxi applications.

## Incubating ideas

The future looks promising for Azerbaijani innovation, which is being fostered by several public institutions, including the High Tech Park launched two years ago. While the park is still in its early days, it has already spurred an interest in innovation and tech entrepreneurship among young Azerbaijani, by organising school trips to its premises and competitions for startups. To date, its startup incubator Picampus has become home to 35 startups, which range from online food order services to travel, voice encryption and online television projects.

Judging by the interest in and financing available for tech entrepreneurship in the country, Azerbaijan is likely to become a household name in IT in the coming years, as its companies export the solutions that they developed at home to emerging countries that are looking to develop their IT infrastructure. ●

## Tickets for Baku Formula One: catch them if you can

With tickets expected to go on sale soon, Azerbaijan's debut in the Formula One circuit in June 2016 is likely to be sold out. That is because only 28,000 tickets will be up for grabs, a fairly small number compared to the number of tickets typically sold for such events.

Arif Rahimov, CEO of Baku Grand Prix Limited, explained to journalists present at a Grand Prix race in Dubai that Baku can accommodate 10,000 visitors in 7,000 hotel rooms, and that Formula One stakeholders would take up another 2,500 rooms.

"This is the maximum capacity we have in Azerbaijan. We are confident we will sell out

on the international tickets, because this is a very limited amount of tickets that will go fast," advising those interested to book accommodation before purchasing the tickets.

According to Rahimov, there will be 20,000 seats in grandstands and another 8,000 general admission tickets.

Named the Grand Prix of Europe – a Formula One event that was introduced during the mid-1980s and held regularly from 1999 until 2012 with Valencia in Spain the last host – the Baku race is just the beginning for Azerbaijan. The country plans to remain part of the circuit in the coming years.



# Economics & finance

## Azerbaijani economy adapts to changing environment, but bank sector faces uncertain prospects in 2016

Azerbaijan's GDP is poised to grow by 3-4% in 2015, according to Demetrios Efsthaliou, head of trading strategy at London-based investment bank ICBC Standard Bank, who visited Baku in late November. Just like the European Bank for Reconstruction and Development (EBRD), which is upbeat about the prospects of the Azerbaijani economy in 2016 despite the steep drop in oil prices in the last year and a 34% devaluation of the national currency in February, Efsthaliou anticipates that Azerbaijan will be among the fastest-growing economies in the region in 2015.

In his trip notes on Azerbaijan published on December 2, Efsthaliou made a straightforward observation regarding the possibility of a second devaluation of the Azerbaijani currency, the manat, this year, which many in the country fear but few dare mention. "Many locals and market commentators expect an imminent second 30-35% devaluation of the manat. However, on this occasion, while I appreciate the arguments for a move to float [the manat], I stand on the camp of those who believe that neither external conditions yet dictate, nor is the country ready for such a move," he notes.

Efsthaliou's opinion has a caveat; "ultimately, the price of oil is key in determining the need and timing of a second devaluation". However, since his visit to Baku, the Organisation of the Petroleum Exporting Countries (Opec) met in

Vienna and decided to keep oil production at current levels, which are above Opec target levels, sending oil prices plunging to under \$35 a barrel for the Brent in mid-December.

So his prediction regarding the free floating of the Azerbaijani currency, the manat, over the next 18 to 24 months might be precipitated by the volatility of oil prices, which the Azerbaijani economy is heavily dependent on.

### Economy adapting to a more depressed operating environment

The devaluation of the manat might have sent banking profit margins and asset quality plunging, but it was a natural response to the regional economic downturn, and it improved the government's balance sheet, Efsthaliou writes. As a result, "the planned reduction of the [Azerbaijani sovereign wealth fund Sofaz's] reserves will be very small in 2016, just \$1bn, assuming an oil price for the [predominant oil variety exported out of Azerbaijan] Azeri light of \$50 per barrel." Meanwhile, the devaluation ensured that the current account would remain in surplus in 2015, although it would be more modest compared to 2014- 2-3% of GDP compared to 16% of GDP in 2014.

The collapse in oil prices had the added benefit of accelerating Baku's economic diversification programme, which was already underway but which may see increased public investment in the medium term. While sectors like real estate and construction might see stalled growth in 2016-2017, agriculture, telecommunications, manufacturing, transport, logistics and other services are expected to drive economic growth in the short term.



Azerbaijan Export & Investment  
Promotion Foundation



AZERBAIJAN INVESTMENT COMPANY

Meanwhile, the government's modest debt levels, which are less than 15% of GDP, and the generous savings amassed by Sofaz will ensure that Azerbaijan weathers the current economic crisis relatively well.

## Banking trouble

One of the worst performers in Azerbaijan this year was the banking sector, which suffered declining profit margins and asset quality, depressed lending as a result of low consumer confidence, and a skyrocketing dollarisation rate, which reached almost 45% of loan portfolios and 75% of deposits in October.

On December 9, rating agency Fitch downgraded the outlook for the Azerbaijani banking sector to rating watch negative, citing "heightened vulnerabilities in banks' asset quality, performance and capital due to increased dollarisation and the devaluation of the manat by 34%." Fitch further noted that the quality of corporate loans, which represent 61% of total lending, is "undermined by considerable project finance lending to start-ups, long tenors/grade periods on principal repayments and the limited financial transparency of the corporate sector", meaning that the trouble might only just be starting for Azerbaijani banks and their endangered assets, if their opaque corporate clients default on loans en masse.

Consumer lending is no more secure after it grew rapidly between 2012 and 2014, and is bound to weaken portfolios, the rating agency notes. The prospects of short-term retail lending are hampered by increased regulation in 2015, which caps it at 29% of loan portfolios, as well as weakened internal capital generation capacity and heightened indebtedness of the population.

On a positive note, the central bank has been supportive of banks throughout the year, and provided swaps and hedges after the February devaluation to help them meet short-term liquidity needs. Fitch anticipates that the regulator will continue to support the sector with local currency swaps, although local bankers claim that this form of support can be counterproductive, because panicked local banks- and companies, convert most local currency in foreign denominations straightaway.

The increased dollarisation of banks' deposits contributes to their inability to hedge short-term open currency positions by any other means except for issuing foreign currency-denominated loans, which, in Fitch's view, increases their credit risk. "Many banks in the sector operate with unhedged short foreign currency positions and are exposed to significant one-off translation losses in case of further manat devaluation, which, in some cases, could seriously hit their capital," the rating agency concludes. ●



## ICBC Standard Bank advises to buy Azerbaijani bonds

Investment bank ICBC Standard advises markets to buy bonds from cheap commodity exporters like Kazakhstan and Azerbaijan and special value bonds like Armenia's in a special report on emerging market (EM) bonds published on December 14.

While acknowledging the uncertainty around EM bonds this year, and the unpredictability of markets in light of an anticipate rate hike by the US Federal Reserve on December 16, ICBC Standard notes that, "emerging market commodity importers have outperformed not only commodity exporters, but also US investment grade corporates".

But as securities issued by commodity importers are becoming safer but more expensive, Kazakhstan and Azerbaijan are good investment opportunities at a time when oil prices are low, because of their "large pools of hard currency assets, and flexible exchange rates should survive in this harsh external environment".

Azerbaijan is "not quite in the same category as Kazakhstan, because its currency is managed and its institutions are weaker, but its national oil fund is equivalent to a massive 60% of GDP", the report notes, while adding that Kazakhstan successfully floated its currency in August, which has since moved to KZT330 to the dollar, compared to KZT180 previously.

## Inflation in Azerbaijan increases by 0.4% m/m in November

Consumer prices of goods and services increased by 0.4% m/m in November, according to Azerbaijan's State Statistics Committee (Azstat). The increase was primarily driven by the rise in food prices, which were up by 0.9% m/m.

Azerbaijan has managed to contain inflation in consumer prices this year, despite a 34% devaluation of the national currency, the manat, against the dollar in February. The central bank is targeting an inflation rate between 5% and 6%, although the International Monetary Fund (IMF) estimated that it could reach as much as 8.5% in 2015 in its June review but revised it down to 5% in the November outlook update.

Meanwhile, producer prices of agricultural products increased by 1.8% m/m, driven primarily by the 3.7% m/m increase in the producer price of fruit and vegetable crops.

Producer prices of industrial goods declined by 7.1% m/m in November. In mining, the index was 8.2% down m/m, and in the processing industry by 1.4% m/m. Azstat includes oil and gas extraction in its mining statistics. Producer prices in metallurgy decreased by 6.8%; in the oil industry by 1.9%; and in the chemical industry by 5.8%. Producer prices of the extraction of metal ores increased by 2.3%, of the production of construction materials by 2.2% and of beverages by 1.2%.

## Azerbaijan's foreign trade declines by 36.6% in Jan-Oct

Azerbaijan's foreign trade declined by 36.6% y/y to \$21.7bn in January-October, according to the Azerbaijani State Statistical Committee (Azstat). During the first ten months of 2015, exports declined by 47% y/y to \$14.2bn, while imports increased by 1% y/y to \$7.4bn, resulting in a 65.2% y/y contraction in the current account deficit, to \$6.8bn.

Azerbaijan's primary export commodity is oil, the price of which dropped by more than 60% in the last year, resulting in a severe contraction in the country's export turnover. Meanwhile, the economic downturn in the region and in the country's main trading partners for non-oil commodities - Turkey, Georgia and Russia - contributed to the contraction of trade.

However, Baku has been working to diversify its economy and increased its manufacturing and agribusiness output and exports to counterbalance these trends. Between January and October, Azerbaijan increased the value of its exports of non-oil products by 3.7% y/y to \$1.3bn. But oil remains the main export commodity, accounting for 91% of export earnings in January-October.

## Azerbaijani central bank reserves drop by \$589mn to \$6.2bn in November

The Azerbaijani Central Bank (CBA) confirmed that its foreign exchange (FX) reserves declined by \$589mn to \$6.2bn in November and by \$7.5bn since January. CBA's reserves peaked at \$15.2bn in August 2014.

CBA has used its reserves to bolster the national currency, the manat, which suffered a 34% depreciation in February, ending eleven years of exchange-rate stability and four-year peg to the dollar. The markets are fearful that the steep decline in CBA's reserves since September could lead to another depreciation.

However, Demetrios Efsthathiou, head of trading strategy at ICBC Standard Bank, believes that a second wave of devaluation is unlikely at the moment. "The currency has been an anchor of stability in a country where stability matters hugely," he noted in his trip notes on Azerbaijan published on December 2.

# Chart

## Azerbaijan improves position on ICT development index

Azerbaijan continues to further improve its position in the information and communication development in the region and throughout the world.

The latest report from the International Telecommunication Union for 2015 said Azerbaijan took 67th place on the index of information and communication technologies development (IDI), rising three places from 2013, and nine from 2010. Azerbaijan's IDI was 5.79 in 2015.

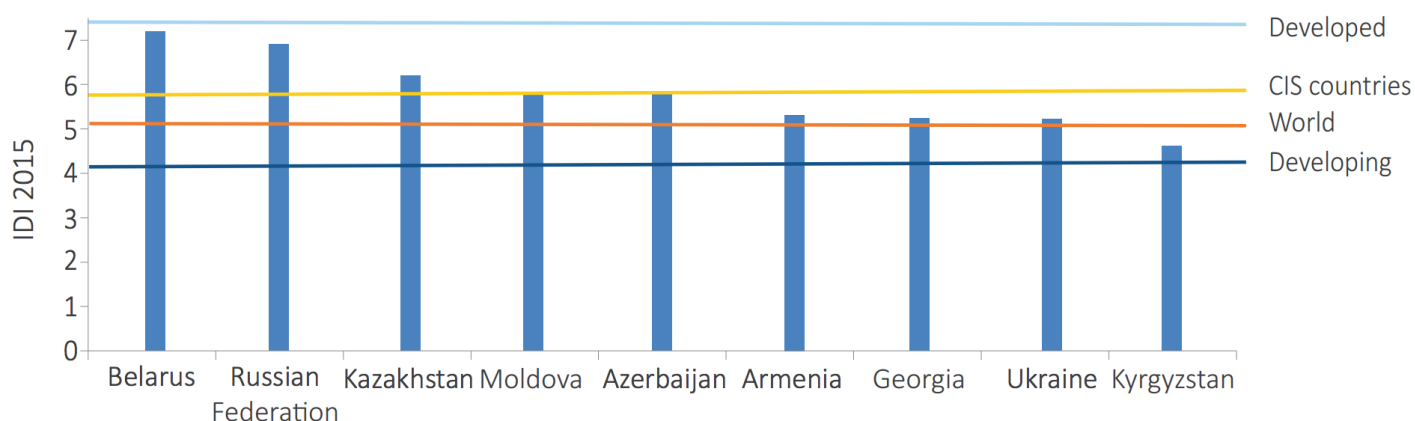
In addition, Azerbaijan took 60th place among 170 countries of the world for an average cost of ICT services. The price of ICT services includes the average price for services in fixed telephony, mobile communications and broadband internet access. The average cost of ICT services in Azerbaijan amounted to 1.4% of GDP per capita, according to ITU.

The level of Internet penetration in Azerbaijan is 61%. This means that for every 100 people in the country there are about 20 users of fixed broadband Internet and 47 users of mobile broadband access.

Today, Internet is an integral part of life for many Azerbaijanis. The internet is not only a way to gain access to information, video services and social networks, but also a necessary tool in the activities of banks, financial institutions, airlines, etc.

The country recently faced with an internet outage of several hours when a fire cut lines connected to the DATA-center of Delta Telecom – Azerbaijan's primary provider. The outage for several hours affected the functioning of some organizations in the country. Azerbaijan plans to create a backup so as not to experience this problem in the future. ●

IDI values, CIS region, 2015



Source: ITU



## News in brief

### **ADB to lend \$2.2bn for energy, transport, utility projects in 2016-2018**

The Asian Development Bank (ADB) reveals plans to lend \$2.24bn to Azerbaijan for projects focused on transport, energy, and utilities in 2016-2017 in its country operations business plan for Azerbaijan 2016-2018 published on December 11. Baku's contribution to ADB-financed projects will be an additional \$760mn.

Energy will be the focal point of ADB's financing in Azerbaijan, with the multilateral lender allocating \$790mn for projects in biomass; transmission and distribution of electricity; storage, transmission and distribution of liquid fuels and gas; and storage, liquefaction and compression of natural gas.

Likewise, ADB has earmarked \$200mn for transport projects, which span road and rail infrastructure and policy; and \$125mn for utilities like water distribution and waste management.

Since 1999, ADB has extended Azerbaijan 20 project loans and one grant totalling \$1.6bn, including six non-sovereign loans worth \$143mn and technical assistance grants worth \$14.4mn.

### **Eurasian countries see sizeable capital flight in 2004-2013**

Eurasian countries topped the ranking of illicit financial flows from developing countries compiled by the Washington-based Global Financial Integrity. According to the ranking, illicit capital flight from the developing world averaged \$784bn a year between 2004 and 2013 to total \$7.8tn, with Russia losing \$1.05tn and Kazakhstan \$167bn in the period.

The non-profit organisation defines "illicit financial flows" as money involved in the drugs trade, tax evasion and money laundering that flows via shell companies, human trafficking and terrorism funding. The lack of trust in political stability and the financial systems of Kazakhstan and other former Soviet countries encourages capital flight. Government seizures of assets owned by people who fall out of favour with the authoritarian regimes also encourage the moneyed to stash their cash in Western countries where former Soviet governments cannot easily get their hands on it.

According to the ranking, Kazakhstan lost \$167bn in the decade, which unfavourably compares to the country's GDP of \$134bn expected in 2015. Russia at number two in the ranking lost \$105bn a year on average, or the equivalent of 50% of the country's GDP in 2013.

Another oil-exporting country in the region, Azerbaijan, saw an annual outflow of capital that averaged \$9.5bn in the decade between 2004 and 2013. Azerbaijan was ranked 17th in the index. The cumulative flow of \$95bn in the decade was equivalent to 129% of its 2013 GDP.



Azerbaijan Export & Investment  
Promotion Foundation



AZERBAIJAN INVESTMENT COMPANY

## **Fitch affirms Azerbaijan's Kapital Bank 'BB-' with stable outlook, withdraws rating**

Rating agency Fitch has affirmed Kapital Bank's long-term issuer rating as 'BB-' with a stable outlook, and withdrew the rating because "the issuer has chosen to stop participating in the rating process, and Fitch will therefore no longer have sufficient information to maintain its ratings. Accordingly, Fitch will no longer provide ratings or analytical coverage for Kapital Bank."

Fitch upgraded Kapital Bank's rating from 'B+' to 'BB-' with a stable outlook on September 21, citing a strong support for the bank from the Azerbaijani government, the fact that it belongs to one of the largest and most liquid holdings in the country, Pasha Holding, and that, together with Pasha Bank, it commands a large market share.

The second largest bank in Azerbaijan by assets after International Bank of Azerbaijan (IBA), Kapital Bank maintains a reasonable asset quality and good capital position, despite the headwinds facing the Azerbaijani banking sector this year. Fitch cited the bank's modest balance sheet dollarisation and limited exposure to foreign currency risks when it upgraded its rating in September.

However, the bank's rate of nonperforming loans (NPLs) had increased to 9% in June, up from 6.1% in December. Asset quality has been an issue for many Azerbaijani banks ever since the national currency was devalued by 34% against the dollar in February. Asset quality has depreciated across the board, with banks like AG Bank (NPL ratio of 29% as of June), IBA (18.5%), Pasha Bank (14.6% as of September) and VTB Bank (11.7% as of June) among the worst performers.

## **Azerbaijani president, Turkish PM say TANAP to be completed before 2018**

Turkey will receive the first volumes of Azerbaijani gas through the Trans Anatolian Pipeline (TANAP) before 2018, the original date when the pipeline was to be commissioned, according to Turkish Prime Minister Ahmet Davutoglu and Azerbaijani President Ilham Aliyev.

The two leaders met in Baku on December 3 at a critical time for Turkey, which has been staving off the effects of a diplomatic standoff with Russia. Russia has begun enforcing economic sanctions on Turkey over an SU-24 plane that the latter shot down on November 24.

In addition to the sanctions on Turkish companies and exports related to textiles, construction, tourism and agriculture, Moscow announced that it was considering reducing its exports of liquefied petroleum gas to Turkey by as much as 25% in 2016. Russia is the second largest provider of LPG to Turkey. In turn, Ankara announced that it would seek to diversify its gas import base faster to include countries like Algeria, Nigeria, and Azerbaijan. In parallel to Davutoglu's visit to Baku, Turkish President Recep Tayipp Erdogan is visiting Qatar.

TANAP was originally designed to deliver 6bn cubic metres (bcm) of Azerbaijani gas to Turkey by 2018 and an additional 10bcm to Europe through the Trans Anatolian Pipeline (TAP) by 2019.



## Azerbaijan cuts freight trucking costs by 40%

Azerbaijan cut the cost of freight trucking to the Caspian Sea ports of Aktau (Kazakhstan) and Turkmenbashi (Turkmenistan) by 40%, according to the country's Council for Transit Cargo Transportation.

Azerbaijan is seeking to develop its transport and logistics sectors and to position the country as a transit hub between Europe and Central Asia, by attracting freight trucks to cross its territory and then transfer them on ships that would carry them across the Caspian Sea. In order to facilitate trade in agricultural products with Central Asia, Azerbaijani company Azersun built an 8,730-square-metre logistics centre in Aktau that will come on stream before the end of December.

The cut in freight transport costs could also benefit Turkish trucks heading to Central Asia that have been banned from crossing through Russia after Turkey shot down a Russian SU-24 plane on November 24.

## Azerbaijan names company to launch its second satellite into orbit

Azerbaijan's second satellite will be launched into orbit by France's Arianespace, according to Elmir Velizade, deputy telecommunications minister. He added that the country's second satellite would be launched into orbit in 2017 and that national airspace company Azercosmos is to sign an agreement with Arianespace.

Arianespace also launched Azerbaijan's first satellite, Azerspace/Africasat-1, into orbit on February 8, 2013, from its base at the Guiana Space Centre in the French Guiana. The satellite

is used for telecommunications and broadcasting and has been servicing clients in the Middle East, Europe, Africa and Central Asia, in addition to Azerbaijan.

Azerspace-2 will be used for similar purposes, and will be designed and built by Canadian company Space Systems/Loral (SSL), with which Azercosmos reached an agreement for an undisclosed sum in October. "This new satellite will provide Azercosmos with additional capacity for the increasing demand in the region, and will allow us to continue to bring the best service to our customers," said Rashad Nabiyev, Azercosmos chairman and CEO.

## Statoil sells 20% share in Trans Adriatic Pipeline to Italy's Snam

Norway's Statoil will be selling its 20% share in the Trans Adriatic Pipeline (TAP), which will deliver 6bn cubic metres (bcm) of Azerbaijani gas to Europe starting in 2020, to Italian infrastructure company Snam for €208mn, according to a press release on December 1.

According to Statoil, the reasons behind the sale are the optimisation of its portfolio and capital prioritisation. The sale will be completed before the end of 2015.

Snam has been courting Statoil and BP for a share in TAP for months, and its CEO Carlo Malacarne broke the news about Statoil's possible pullout from TAP in October. Snam has also bid for a 17% share in Greek gas distribution utility Desfa, which Socar, the Azerbaijani oil company, is seeking to sell.

The other shareholders in TAP are BP (20%), Socar (20%), Spain's Enagas (16%); Belgium's Fluxys (19%); and Switzerland's Axpo (5%).

