

## Azerbaijan economy in 2020

### **Stable economic growth in the previous 3 years was interrupted by COVID in 2020:**

- The overall economy contracted by 4.3%, while the oil sector fell by 7%. Production of crude oil was 8% lower compared to 2019. It fell by 8.8% m-o-m to 2.9 mln. tonnes in December. 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%. Reconstruction work in the liberated territories is expected to revive the construction sector;
- 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:**

- The price level increased by 0.8% in December and annual inflation stood at 2.6%. It was lower than Central Bank's target band (2%-6%) center 4%;
- Prices of 79.2% of the products & services (412 out of 520) included in the consumer basket increased on a y-o-y basis, 10.8% decreased, and 10% remained unchanged. Price increase of 52.7% (274) of items is less than headline annual inflation of 2.6%;
- If decomposed into the consumer basket, food prices went up by 4.5%, non-food prices 1.2%, and services by 1.1% y-o-y. The contribution of food, non-food products, and services to the annual headline inflation made 1.9, 0.3, and 0.4 percentage points (total 2.6%), respectively;
- In general, shrinking demand due to national lockdown had a disinflationary effect.

### **Despite low oil prices and decreased oil exports trade balance yielded a surplus equivalent to 4.2% of total GDP:**

- In 2020, total exports decreased by 30%, and imports\* fell by 6.8%. Ultimately, trade surplus\* decreased by 62.9% and accounted for \$3010 mln. or 4.2% of total GDP;
- The decrease in exports is mainly related to crude oil exports. Sharp fall in oil price had a strong impact as crude oil exports decreased by 36.8% in nominal terms, while it fell by 5.9% in real terms;
- The main contributors to import decline were fuels, machinery & equipment, textiles and metals:

- Imports of fuels fell by 66.1% as lockdown-induced restrictions on mobility harmed demand for transportation;
  - Imports of machinery & equipment abated by 4.7% as importers deferred non-essential expenditures;
  - Imports of metals fell by 9.5% as demand of inputs for production was constrained due to COVID-19;
  - Pharmaceutical product imports rose by 27.2%, while imports of cleaning products increased by 21.5% showing the impact of the pandemic;
  - During the analyzed period, non-oil exports fell by 5.3% y-o-y, amounting to \$1851 mln., equivalent to 17.3% of total imports;
  - Trade surplus contributed to CBAR reserves, as of end-2020, CBAR reserve was USD 6369.4 mln. which is 1.8% y-o-y or USD 111.4 mln. higher compared to 2019;
  - The assets of SOFAZ, as of end-2020, increased by 0.6% y-o-y compared to 2019 and stood at USD 43564.3 mln. or 102.2% of total GDP.
- \*Note:** excluding semi-manufactured gold – HS code 71, which is the gold import of State Oil Fund of Azerbaijan.

**License withdrawal of four banks & the pandemic led to 5% decrease in loan portfolio and 4.4% fall in deposits:**

- In 2020, the total assets of the sector decreased by 2% making 32.1 bln. AZN. Excluding license withdrawal of four banks – AtaBank, AmrahBank, AGBank, and NBC in April-May, total assets rose by 2.4%. Gross loans decreased by 5%. Excluding the banks with license withdrawals, loans rose by 1.7%;
- The corporate loan portfolio contracted by 1.7%, driven by loans to the firms in transportation & communication (29.5%↓), energy, mining & natural resources (16.2%↓), while loans to industry & manufacturing (43.2%↑) and trade & services (4.6%↑) sectors grew;
- Loans to households decreased by 3.9%, including 14.5% fall in consumer loans. It seems that the macro-prudential measures taken by the supervisory authority to restrict the excessive growth of consumer loans proved fruitful. The COVID-19 pandemic, liberation war that ended with Azerbaijan's victory and license withdrawal of four banks also played their roles. Mortgages grew by 8% continuing its stable trajectory;
- According to Electronic Loan Platform more than 3,300 businesses applied for loans which were negatively affected by the pandemic and ₼169 mln. of loans were granted to 529 entrepreneurs in 2020. In addition, ₼127 mln. of loans were granted to businesses by Entrepreneurship Development Fund to finance 908 investment projects in 2020;
- NPL amount has seen a 29.8% decrease compared to the end of 2019. The total NPL ratio stood at 6.1% that is 2.2 p.p. lower than 2019 year-end. License withdrawal of problematic banks with high NPL was the main driver of this fall. Moreover, easing in macroprudential measures helped NPL to decrease;
- The deposit base experienced a decline of 4.4% and made 23.7 bln. AZN. Excluding the banks with license withdrawals, the deposit portfolio contracted by 1.1%.

Demand deposits experienced an increase at the rate of 4.4%, while time deposits fell by 14.9%, amounting to 9.6 bln. AZN. License withdrawals and cash needs of households and firms due to lower income induced by the lockdown were the main sources of deposit outflow. Households' deposits and NFCs' deposits fell by 5.3% and 5.4%, respectively;

- The dollarization rate of the total deposit portfolio stood at 56.4% falling by 4.6 p.p. compared to Dec 2019. The dollarization rate for time deposits fell by 1.8 p.p., while demand deposits experienced a 4.9 p.p. dollarization decrease compared to Dec 2019;
- Return on equity of the banking sector was 12.1% (2019: 11.7%), calculated as the ratio of total net profit to the end of year equity. Interest income decreased by 0.1%, while non-interest income fell by 7.1% y-o-y resulting from fewer transactions in branches due to the pandemic.

**Insurance premiums grew by 7% in 2020 driven by endowment and property insurance segments:**

- In 2020, total insurance premiums increased by 7% y-o-y and accounted for 782.6 mln. AZN. The net premiums (premiums minus claims) have experienced a 30.6% fall and accounted for 0.5% of non-oil GDP (2019: 0.8%). In the economy, this indicator is considered to be one of the main sources of investments;
- Based on the market segment analysis, total life insurance (LI) premiums increased by 13.6% and made 303.7 mln. AZN. The share of LI premiums in total premiums of the market grew by 2.4 p.p. and comprised 41.7%;
  - Voluntary LI premiums increased by 13.9% and made 249.8 mln. AZN. The share of VLI in total LI premiums rose by 0.2 p.p. to 82.2%.
- Premiums of non-life insurance (NLI) rose by 2.7%. The share of NLI in total premiums decreased by 2.4 p.p. to 58.3%;
- The claims to premiums ratio of the life insurance market was 93.2% (2019: 46.7%), while this ratio was 42.9% (2019: 44.3%) for the non-life insurance market.

**CBAR decreased the refinancing rate by 25 bps to 6.25% at the December MPC meeting:**

- The lower bound of the interest rate corridor was reduced by 25 bps to 5.75%, while the upper bound decreased by 25 bps to 6.75% to support the liquidity;
- Central Bank stated that pandemic-induced fall in external and aggregate demand enabled easing in monetary policy;
- CBAR mentioned that fiscal stimulus to support pandemic-affected households & businesses and macro-prudential easing measures are expected to increase lending activity;
- Central Bank stated that recent developments related to COVID-19 vaccination in major economies is a positive sign for the global economy and will help external demand to recover faster, while uncertainty remains in access to vaccines;
- CBAR forecasts inflation to approach 4% in 2021;



- According to Central Bank, trajectory of inflation, impact of fiscal and monetary policies and recovery pace of consumption will affect the next interest rate decision.

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