

Investments into Economic Branches of Azerbaijan Republic and Their Effectiveness

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Abstract

The article is devoted to detail analysis of investments into the economic branches of Azerbaijan, contributed from local and foreign investors, as well as the implementation and the effectiveness of these investments from economic and geographical point of views. The priorities and perspective ways of development of non-oil sector in condition of market economy are determined in the research work. Besides this, necessity of realization of corresponding investment policy for achieving sustainable development of country's regions is substantiated and shown.

Key Words: economic branches, investment, non-oil sector, sustainable development, regional strategy, industry, agriculture

In recent years, growth of investments from domestic sources and foreign donors were observed in the Republic of Azerbaijan as a result of successfully implemented economic policy. Nevertheless, the preparation of complex activity plan in order to create effective management strategy capable to provide this growth in condition of market economy, as well as direct these investments to more perspective economic branches are needed.

Currently, investment policy is considered as a significant component of strategy of economic development in many developed countries. Investments favorably influence manufacturing and employment of population, as well as capital collecting. In this regard, investments must be used effectively in order to develop various business activities in condition of market economy.

In general, investment (investment resources) include cash incomes, bank amounts, target bank allocations, portions, share capital, other securities, technologies, tools and appliances, patents and trademarks, credits, other properties and property rights, intellectual riches invested into businesses and other activities, as well as positive economic and social purposes (Allahverdiyev & Mammadov, 2003).

Investments play significant role in the social and economic development of country's regions and the development of new manufacturing areas. Increase of investments favorably influences the growth of

population's income. Investments into various branches of economy as well as their efficiency are mostly investigated from economic aspect. In terms of economic geography, investments must be investigated considering the efficient use of natural resources, the territorial organization of economic branches and their principles, the objective laws of development and distribution of relevant activities, and also perspectives of economic branches. In this regard, for the first time regional analysis of investments is studied in this research.

Azerbaijan has been an integral part of Russian Empire. The republic was under the control of central government in Soviet period until 18 October, 1991. Despite of many advantages of the economic structure of Soviet state (for instance in terms of development of human capital), appropriation of natural resources was conducted almost inadequately. Transportation costs were exceeding cost price of production. These and other shortcomings in economy led to the collapse of Soviet Union at the end of 20th century (Imrani & Zeynalova, 2014).

New created states faced certain economic and political problems in the first years of their independence. Previous economic relations were disrupted whereas the new relations were requiring long time for establishment. The Republic of Azerbaijan experienced economic and political crisis in this period, too. The experienced depression was reflected in almost all spheres of human activity.

Sustainability of economic development was needed to escape this hard situation in the country. Favorable condition for the investment activity was to be secured as well. In the meantime, efficient distribution of investments were to be determined with considering distinguishing peculiarities of economic security in globalized world. There was a need in the determination of foreign sources of investment as well as fiscal and credit policy of foreign investors with taking into account national security.

The following features of investment policy were characteristic for Azerbaijan in the first years of independence:

- Restriction of state investment and fostering of private investments;
- Attraction of foreign investment;
- Restoration of enterprises, privatized at the expense of capital gained in process of privatization;
- Application of concessions, and abatement of rates in regard to investors in accordance with tax legislation;
- Motivation of creation of local productive forces with applying customs tariff;
- Development of national entrepreneurship;
- Cancellation of taxes and other debts of enterprises, as well as relevant permission for concessional payment (Nadirov, Muradov, Alasgarov, Nuriyev & Huseynov, 2003, pp. 233-238).

Motivation of investing activity in economic branches is connected with political and economic interests of government. In order to implement investment activity, the needs in major economic branches is to be taken into consideration. With the purpose of providing sustainability in economy, investment policy is to be realized with defining priority economic activities and businesses. When conducting this policy, extent of risk, period, form of realization and also relevant branch of economy is to be defined, too.

It is notable that sources of finance play key role in implementation of both national and foreign investment policies. Domestic (national) investment policy is composed of measures on reaching aims at the expense of domestic sources of funding, while foreign investment policy deals with long-term international capital investment. Currently, investment activities of foreign investors and also transnational corporations are planned as usual by long period. In this regard, there is a favorable condition for relevant long-term activities in Azerbaijan (Shakaraliyev, 2011).

In Azerbaijan, Law on 'Protection of foreign investments' dated to January 15, 1992 was accepted in order to regulate activities of investors. According to this Law, social, economic and juridical conditions of

foreign investment in the territory of Azerbaijan Republic are determined, whereas equal support of rights of all investors by any form of property is guaranteed. The active attraction of investments into the national economy, and also the effective use of these investments in sake of development of economic base, international economic cooperation and integration are reflected in the Law. The rational development of economic branches through the involvement of advanced foreign equipment and technology, and the support of rights of foreign investors are guaranteed. According to the noted document, foreign investors are eligible to invest in Azerbaijani economy in the following forms:

- * Have participation share in enterprises and entities created by companies and individuals of Azerbaijan Republic;
- * Creation of enterprises, belonging to foreign investors;
- * Privatization of foreign investors' enterprises, buildings, installations, loans and securities and properties in the future;
- * Use of land and other natural resources.

As the Law on 'Protection of foreign investments' ensures protection of foreign investors' interests from possible negative impacts made because of changes in the legislature in the upcoming 10 years, it favorably influences investment condition in the country. Azerbaijan has signed agreements with a series of foreign countries on mutual protection of investments which are focusing on obligations taken concerning capital investment, as well as protection of foreign estates and consideration of possible conflicts at international courts.

Economic progress of the Republic of Azerbaijan and huge investments into national economy were observed after the signing of 'Contract of Century' on joint operation at Azerbaijani deep-water deposits 'Azeri', 'Chirag' and 'Gunashli', and relevant partition of share on September 20, 1994. The following years, Azerbaijani economy experienced huge flow of investment. However, investments were made chiefly into exploitation of oil deposits and export of produced oil to world markets (Imrani, 2009, pp. 151-155). By the way, it is remarkable that in Soviet period, around 20% of yearly national income as well as over 50% of investments were spent for growth and enhancement of fixed capital of petroleum industry (Hajizadeh & Abdullayev, 2013).

Contracts concluded between Azerbaijani government and foreign companies on joint exploitation of oil- and gas fields allowed expedite the integration of national economy in world economic system, as well as improve the level of living in the country. Huge investments into Azerbaijan's oil- and gas industry, and the application of modern technology in these activities were bringing considerable dividends to the national economy in recent years. The State Program of 'Development of fuel- and energy complex in Azerbaijan Republic' (2005-2015) was adopted and implemented. Within the Program, measures on continuity of exploration works, drilling of exploration wells, construction of hydrotechnical installations for production, enlargement and reconstruction of system of gas industry and infrastructure, and strengthening and development of energy industry have been put into reality.

Major part of state investments is driven at the expense of revenues, i.e. incomes into the state budget provides the expenditures. In case of break of this balance, investments into state economy may be reduced. In 1991-1996, volume of investments decreased by 4 times, and this fall was reflected obviously on the budget. Analysis of difference between incomes and expenditures of state budget in 2005-2012 shows that deficit was fixed in the state budget with the exception of only 2006 and 2011 years. This deficit made up 178 million manats in 2009, and 362,9 manats in 2010 (Figure 1).

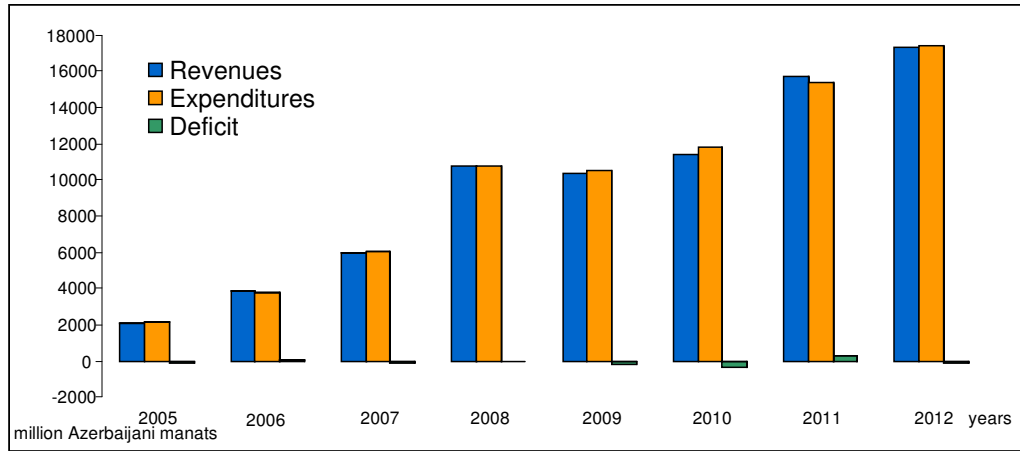


Figure 1. Revenues, expenditures and deficit in state budget of Azerbaijan Republic in 2005-2012.

International economic relations of Azerbaijan are very versatile while the increase of investment flow into country’s budget is one of the topical priorities. The increase of foreign investment resources and particularly the creation of effective proportions in the national economy through the regulation of priorities of use of incomes, gained due to investment activities, as well as the creation and development of social infrastructure in accordance with strong manufacturing potential make necessary the elevation of regulatory role and function of government more in Azerbaijan. In 2012, investments into Azerbaijan Republic made up USD 25,7 billion. The volume of domestic investments made up 15,4 billion USD, whereas the volume of foreign investments was USD 10,3 billion (Figure 2).

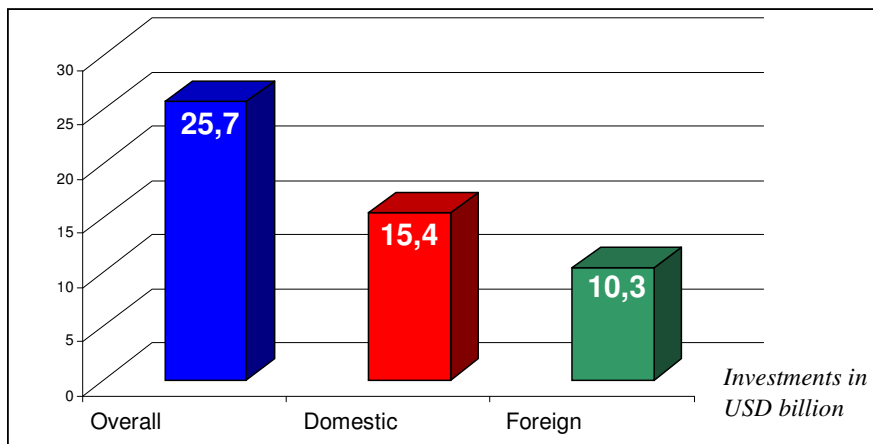


Figure 2. Investments into Azerbaijan in 2012.

As is seen from Figure 2, in 2012, the volume of finances invested into Azerbaijan’s economy from domestic sources was increased while the share of foreign sources was reduced. This allowed accelerate the development of not only oil industry but also non-oil sector and the economy of Azerbaijan as a whole.

The study of condition of investing activities of foreign investors is of interest for the companies in Azerbaijan, as well as for potential countries-investors. Foreign direct investments can provide the elimination of deficiency of finances in enterprises, and also the creation of competitive manufacturing branches through supply of foreign technology and appliances in the country. The increase of foreign direct investments will contribute to the increase of employment and the proficiency of employees in Azerbaijan.

In 2012, the foreign investments were directed to petroleum industry (46,6%), whereas the rest fell to the share of fiscal and credit activities (25,3%), business activities of foreign companies (9,68%), operation of oil pipelines (0,02%), and other areas (18,4%).

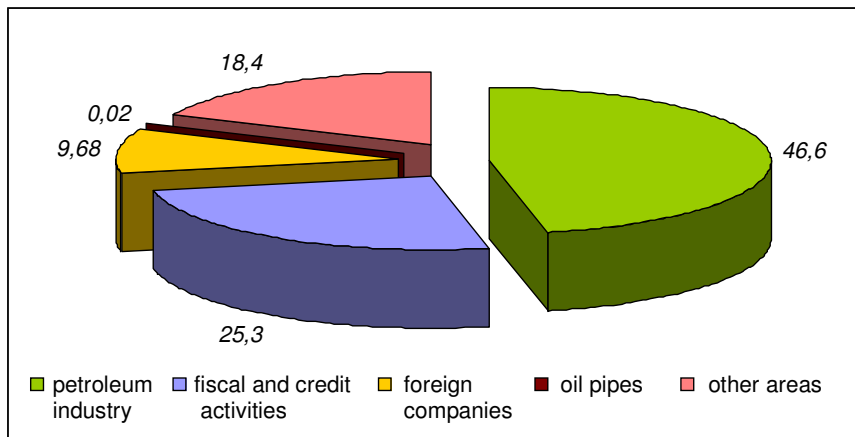


Figure 3. Foreign investments into Azerbaijani economy in 2012 (in percent).

Investing in economy of Azerbaijan, international organizations played an important role in the implementation of economic and social projects, the development of bank sector, the eradication of poverty, the development of domestic industries, entrepreneurship and also education, the growth in production and transportation of oil and gas, the improvement of social infrastructure, as well as the development of small and medium entrepreneurship in the country. The international organizations participated also in the consulting projects.

Effective management of investments is considered as one of priorities of effective management of market structures. Studies show that the solution of this problem leads to the rise of gross domestic products and the creation of effective production and non-production structures. Since the distribution of investments is multi-stage economic process, management of this process should be studied as an issue of dynamic programming character (Bayramov, 2007). 42% of investments into a fixed capital are directed to industry in Azerbaijan. The rest is shared by transport (20%), state and municipal management (7,7%), education (4,3%), construction (4%), agriculture (3,2%), trade (2,9%), communication (1,1%) and other areas (14,8%).

Investment into industrial branches

The Republic of Azerbaijan supplies its demand for fuel due to the available rich oil- and gas resources, and provides sustainability of its economy. The use of energy resources, the effective organization of energy production, the consideration of interests of neighboring countries regarding energy security, the regional cooperation for sake of careful attitude towards natural resources of energy importance, the common and joint use of natural resources, the study and spread of advanced experience as well as the international cooperation and assistance in energy sector are the topical issues at contemporary stage of relation between nature and society.

Located between Europe and Asia or the geopolitical space of high strategic importance, Azerbaijan with its huge energy resources is at the center of interests of leading world countries and also international organizations. Sustainable use of energy resources and provision of relevant security is a major priority of policy of the government of Azerbaijan. Foreign investors express their interests in the existence of big reserves of oil and gas in the country.

Currently, 58,7% of industrial production are shared by mining, while 30,9% by processing industrial areas, 9,4% by production, distribution and provision of electricity, gas and vapor, and 1,0% by water provision, and waste management in Azerbaijan. 90,8% of investments into fixed capital in the industry falls to the share of mining, whereas 1,4% to processing industrial areas, 1,4% by production, distribution and provision of electricity, gas and vapor, 6,4% to water provision and waste management.

In 1993-2010, 2265 manufacturing enterprises were commissioned in Azerbaijan. In 2010, Granit and Marble Plant in Baku, Elevator Plant of Sanghachal, the car plant and the concrete mill in Nakhchivan, 'Bilav' hydroelectric power plant in Ordubad, 'Gamigaya' Industrial Complex of Construction Materials, the cannery as well as the factories of tea and ice-cream in Lankaran, the milk- and tobacco-processing factories in Zagatala, a salt factory in Absheron, a wine-mill in Jalilabad, a cannery in Bilasuvar, a mill of mineral water in Aghstafa, a refrigerating storehouse in Salyan, 'Gilan' Piano Mill, a storehouse for fruits and vegetables, and also a bus terminal in Gabala, as well as other manufacturing enterprises were put into operation in various regions of the country.

Investments into agriculture

In condition of dynamic development of Azerbaijani economy, the commissions for producers of agricultural crops, as well as tax exemption for producers in agroindustry with the exception of the ground tax until 2009, caused investments to rise in the agrarian sector. In order to motivate investment into the agriculture, a series of measures were implemented in the country. Among them, the most remarkable ones were: the transition from progressive system to proportional system in regard to taxation of activities of legal entities, as well as the gradual reduction of tax rate from 35% to 24%; the reduction of value-added tax from 28% to 18%; the reduction of highest limit of the profit tax rates applied for individuals from 55% to 35%; the reduction of assignments for social insurance from 40% to 22%, etc.

The conducted researches show that the continuing decrease of the portion of agriculture within investments into economy was accompanied with the emergence of problems in the satisfying of needs of agricultural producers in financing. The lack of a program on melioration and irrigation impeded the assignation of finance for agrarian infrastructure from the budget, while the restriction of investing into fixed capital curbed sustainability of economic development in Azerbaijan in a certain period of time. In this regard, the specific features of investment had to be studied in order to determine priorities of agrarian investment policy. The adoption of respective programs was in need of as well. The implementation of state programs on 'Social and economic development of the regions of Azerbaijan Republic' in 2004-2008, 2009-2013 and 2014-2018 years enabled the country to create its national agrarian market, to increase employment in the regions, to improve the branch structures of agrarian and industrial complexes, and to create new enterprises and services. These programs were and are being implemented on the basis of principles of long-term and sustainable strategy. Consequently, the tendency of growth was observed in the agro-industrial enterprises.



Granite and Marble Plant in Baku



Cannery in Lankaran



Concrete Mill in Nakhchivan



Milk-processing Factory in Zagatala

Figure 4. New industrial enterprises commissioned in Azerbaijan

Positive changes observed recently in the country were not enough for the complete solution of the existing problems characteristic for agrarian and industrial complexes. In spite of growth as from 758,9 to 2783,1 Azerbaijani manats in production of agricultural crops within 2000-2012, the respective percentages of agriculture in GDP of the country dropped from 16,5% to 5,2%.

Currently, 3,2% of investments into fixed capital is shared with agriculture while it is much less compared to industry, transport and construction sectors. In the structure of agricultural products, the share of individual farmers, family rural farms and housekeeping farms make up 93,4%, while agricultural farms and other enterprises make up 6,6%. The area of lands usable in agriculture is 4768,3 thousand ha in Azerbaijan. The number of persons per 100 hectares makes up 196, whereas the area of usable lands per capita is 0,51 ha. The total area of irrigated lands in agriculture makes up 1424,3 thousand ha, of which 88,3% falls to the share of sowing areas as well as 11,7% to perennial sowings.

In Azerbaijan, investment programs must concern such issues as sustainable development of non-oil sector, enhancement of satisfaction of requirements of population, reduction of differences between country's regions for development, elevation of export potential, as well as environmental protection. 'State investment program' by 2008-2011 years was adopted in the country. The program is prepared and implemented based on principles of Long-term Strategy on management of incomes of petroleum industry. These incomes were directed to the development of non-oil sector, the improvement of available infrastructure and the construction of new service facilities, the import of up-date technologies, as well as financing of measures planned in accordance with state programs.

Later in order to improve investment policy, 'State Program on reduction of poverty and sustainable development in the Republic of Azerbaijan' (2008-2015) was adopted on September 15 of 2008. According

to the Program, priorities such as improvement of management of investments, development of fair competition, support of small and medium entrepreneurship in peripheral regions, strengthening of country's export potential, etc. were specified as priorities. In this connection, State Program on social and economic development of regions of the Republic of Azerbaijan was adopted, as it is earlier remarked. This was a significant event also in terms of attracting domestic and foreign investments into economies of country's regions. Hundreds of social and economic measures were implemented in accordance with this program. Positive consequences of these works were evident. During the implementation of the two state programs (2004-2008 and 2009-2013 years), mechanisms of financial support of the government were improved, while advancement of economic relations between government and businesses were observed. Significant changes took place concerning the state regulation of entrepreneurship and the creation of new workplaces, too. Meanwhile, some problems did not find their solution. Thus, the volume of investments into economic areas of regions is much lesser than that of Baku. In 2012, 64,8% of investments into fixed capital fell to the share of Baku city, while the remain 35,2% was shared by the peripheries. Such proportion led to the increase of structural differences between the capital and other regions of Azerbaijan. The development of non-capital regions depends on weakly-developed manufacturing as well as agriculture as yet. The availability of too big differences between Baku and other regions is undesirable condition for Azerbaijan. The elimination of these differences is considerably connected with development of regional economies (Huseynova, 2011).

Choosing of sources of investment must be conducted properly, whereas these sources are being determined mostly by the operators of investment. Regarding investments, Azerbaijan is not only recipient but also donor country, investing into economy of its neighbors. Energy market of Turkey, Romania, Ukraine and other countries are partially occupied by State Oil Company of Azerbaijan Republic which manages gas supply. Over 60% of needs of Georgia in fuel are being satisfied by Azerbaijan as more than 100 filling stations of SOCAR are functioning in this country.

Economic growth can be ensured sustainably through the keeping of macroeconomic stability and development of non-oil sector in the country. Sustainable economic growth will accelerate socioeconomic development and improve level of living in country's regions. In 2012, 41,6% of foreign investments (USD 4287,8 million) into economy of Azerbaijan were observed in the oil sector, as well as 58,4% (USD 6026,2 million) in the non-oil sector.

High potential of development of non-oil sector must play a motivating role for the diversification of economy. It is expected that Azerbaijan will boost its non-manufacturing branches in the future in order to be one of large exporters of products of this sector. Through the realization of investment programs, other areas of national economy will be currency-intensive, and facilitate the economic growth. Through the implementation of relevant measures on basis of innovative and high technologies, the favorable condition for development of competitive economic areas was created. In order to develop the non-oil sector, numerous new enterprises were created in the country as a result of successfully conducted economic policy. Meanwhile, the creation of manufacturing enterprises significantly depends on foreign direct investments.

In order to define investment policy and its future priorities in Azerbaijan, the following actions seem necessary:

- Preparation of system of evaluation criteria in order to determine priorities of investment activity;
- Determination of the priority measures on sustainable development of country's regions, as well as substantiation of conceptual approach regarding investments;
- Improvement of structure of investment activities in order to reach balanced economic development in the regions of Azerbaijan;

– Further enhancement of condition for the investment activity in Azerbaijan with considering the experience of foreign countries, as well as preparation of regional programs of development.

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