Economic activity continued to contract in June as activity in both oil and non-oil sectors plunged. GDP shrank by 7.4 percent year-on-year (yoy) in June bringing growth in the first half of 2020 to -2.7 percent. Oil GDP fell by 13.1 percent yoy in June as Azerbaijan adhered to OPEC+ imposed quota, leading to a 2.9 percent fall in output since the start of 2020. Activity in the non-oil sector remained depressed as the easing of restrictions was short-lived and a new round of lockdown measures was imposed in the second half of June. This led to a 4 percent yoy decline in the non-oil sector in June. With this, non-oil output contracted by 2.5 percent yoy in H1.2020. The contraction was broad-based, with output declining by 15 percent in construction, 48 percent in hospitality, 2 percent in trade. Agricultural growth slowed markedly in June due to the severe drought and posted 2.2 percent growth in the H1.2020. On the demand side, slowing wage growth, decline in credit, stagnant remittances (up 50 percent on monthly basis in June, but still 20 percent lower than a year ago) and continued restrictions affected consumption. Investments shrunk by 7 percent in June mostly due to lower non-oil sector investments as sentiments remained weak.

The second round of lockdowns predicates a slow recovery. The lifting of lockdown measures in May was short-lived as the coinciding resurgence in COVID infections prompted the authorities to impose another round of lockdown measures. The renewed restrictions reduced mobility in Baku by 13 percentage points in July compared to June, but appear to have had success in slowing down the spread of infections. Some lockdown measures will remain in place until late August (at least), shadowing the prospects for the recovery.

CPI inflation edged up to 3 percent yoy in June, due to higher prices of services. Food prices continued to decline on month-on-month basis in June driving down annual food inflation to 5.1 percent in June from 5.6 percent in May. Non-food prices barely grew in June while prices of services went up by 0.9 percent. This was due to a rise in electricity prices for households as most households exceeded the threshold for the discounted tariff. With inflation in the lower end of its target band (4 +/- 2%), on July 30, the Central Bank of Azerbaijan (CBAR) lowered its policy rate by 25 bps to 6.75 percent.

The trade balance remained in deficit in June. Goods exports dropped by 48 percent in June yoy mostly reflecting a 55 percent yoy drop in oil exports reflecting Azerbaijan’s adherence to the OPEC+ agreement and the low oil prices. Non-oil exports fell slightly in June by 1 percent yoy despite high season for food exports as external demand remained depressed. Weak domestic demand lowered imports by 30 percent in June yoy. This brought the trade surplus in the first half of 2020 to 13.6 percent of GDP from 17.4 percent recorded in May.

The manat remained stable amid an uptick in FX demand in July. The exchange rate remained at 1.7 AZN/USD amid a notable pick-up in FX demand in July resulting in a 38 percent increase in FX sales by the oil fund SOFAZ in July compared to June. Still, at USD515 million, FX sales were below the monthly limit. The official reserves of CBAR reached USD6.5 billion by end-July, while SOFAZ assets recovered to USD43.2 billion at end-June benefiting from positive trends on global financial markets.

The budget registered a deficit in June as spending surged. Budget spending was up by 53 percent yoy in June reflecting higher allocation for COVID related measures while budget revenues remained stable. This brought down the budget surplus in the first half of 2020 to 0.8 percent of GDP.

The 2020 Budget was amended to address anticipated financing gap by the end of the year. The amendment is based on a price of oil of USD 35/bbl, down from USD 55/bbl in the original budget. Revenues are reduced by 4 percent compared to the original budget, due to lower tax collection in oil and non-oil sectors. Additional spending to finance COVID measures (healthcare and economic measures) is estimated at 5 percent of original budget spending. To bridge the financing gap of AZN 2.3 billion (4 percent of GDP) the Government will increase SOFAZ transfers by AZN 880 million (7.5 percent more than originally planned). Overall, deficit of the state budget will climb to 5 percent of GDP. The consolidated budget deficit will rise to 12.4 percent of GDP in 2020 mostly financed out of SOFAZ reserves. Non-oil deficit will increase to 33.5 percent of non-oil GDP, 4.5 percentage point higher than in 2019.

Credit to economy continues to stagnate. The loan portfolio shrunk by 1 percent in June compared to May mostly due to lower corporate loans. Deposits fell by 3.4 percent in June compared to May mainly due to withdrawal of foreign currency deposits. After improving in April and May as few weak banks were closed, NPLs remained stable in June.

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1 Yandex self-isolation index

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Figure 1. Economy contracted by 2.7 percent in H1-2020 (ytd, %)

Source: State Statistics Committee

Figure 2. CPI inflation picked up slightly in June, driven by increase in services prices (yoy, %)

Source: State Statistics Committee

Figure 3. The trade balance remained in deficit in June, due to fall in hydrocarbons export (yoy, %)

Source: State Customs Committee

Figure 4. CBA reserves and SOFAZ assets increased in Q2-2020 and bounced back to January levels (USD billion)

Source: Central Bank of Azerbaijan

Figure 5. SOAZ transfers kept budget in surplus, even as spending soared in H1-2020 (% of GDP)

Source: Ministry of Finance

Figure 6. Credit to economy declined further in June while overdue loans ratio leveled (yoy, %)

Source: Central Bank of Azerbaijan

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