

*Azerbaijan Gap Analysis*  
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**Highlights.** Of the five Monitoring Country Progress (MCP) indices, Azerbaijan's development progress is below Eurasian average in democratic reforms, well-above Eurasian average in economic performance, and roughly Eurasian average in economic reforms, human capital, and peace & security. In all of the second stage **macroeconomic reforms** (in governance, the financial sector, infrastructure, and competition policy), as well the first stage reforms in large-scale privatization, significant challenges remain. Only Belarus and Turkmenistan trail Azerbaijan in progress towards large-scale privatization. No measurable advances have occurred since 2002 in first stage reforms in Azerbaijan and since 2004 in the second stage reforms.

Well more than a majority of Azeri businesses surveyed in 2008 identified three constraints in particular as problematic: corruption (66% of firms identified it as problematic); tax rates (65%); and access to land (61%). Four business constraints appear to have significantly worsened since 2005: corruption; access to land; access to financing; and the skills and education of the labor force.

Five of the six **democratic reform** dimensions tracked by Freedom House have backslid significantly since 1999 in Azerbaijan. Independent media and the electoral process reforms have regressed the most. Governance reforms is the one area which saw little net change from 1999 and 2009, though these reforms have been gradually deteriorating since 2003. Civil society is the most advanced area but is still below Eurasian average; independent media and the electoral process are the least advanced. According to Freedom House, of the CEE and Eurasian countries, only Turkmenistan and Uzbekistan have greater corruption than does Azerbaijan.

Azerbaijan's **macroeconomic performance** exceeds Southern Tier CEE and Eurasia average performance; of the nine Southern Tier CEE countries, only the economies of Bulgaria and Romania outperform Azerbaijan's economy as measured by the MCP economic performance index. However, progress across the economic performance dimensions in Azerbaijan is very uneven; and the effects of Azerbaijan's dependence on oil are very substantial.

Economic growth in Azerbaijan has been exceptional by many standards for most of the transition years. From 2002 to 2010, Azerbaijan's economy expanded by an annual average rate of 16%, well above both global standards and Eastern European standards. Azerbaijan's economy weathered the global economic crisis in 2009 well, due in no small part to its robust oil sector. The oil output share of GDP in Azerbaijan increased from 20% in 1995 to 60% by 2008. Oil exports increased from 40% of total exports in 1995 to more than 95% by 2007. Oil revenues as a percent of total government revenues have grown from less than 10% in 1998 to 75% in 2008. A key variable is the price of oil which experienced a rapid and substantial increase from 1998 to 2008 to historically high levels, followed by a very significant drop in 2009 and significant recovery in 2010.

The impact of Azerbaijan's dependence on oil is evident in key indicators of Azerbaijan's integration into the global economy. The volatility in Azerbaijan's current account balance and in foreign direct investment (FDI) flows, even its export share of GDP, has been extraordinarily high.

Azerbaijan is highly energy independent by global standards; energy exports are roughly 3.5 times greater than domestic energy use in Azerbaijan. However, energy efficiency in Azerbaijan remains relatively low; output per unit of energy use in Azerbaijan is slightly lower than the global average of 5.8.

**Human capital.** The challenges in Azerbaijan's *education* system are substantial. Education enrollment rates vary tremendously according to the level of education. Gross enrollments rates in primary and secondary schools are actually greater than 100% (i.e., some students are "repeaters" and hence are older than the school age category). In contrast, pre-primary enrollment rates and tertiary enrollments rates are very low. Tertiary enrollment in Azerbaijan is roughly 15%, well below what it was in Azerbaijan at the outset of the transition and well below tertiary rates in the large majority of E&E countries today.

In addition, there is evidence that the quality of the education at least at the secondary level is notably below OECD standards and is deteriorating. There is also evidence of a significant mismatch between skills developed in schools and skills needed by businesses. Public spending on education in 2008 in Azerbaijan was 1.9% of GDP; this is the lowest percentage dedicated to education in the E&E region. Azerbaijan's public spending on education has continually declined since the collapse of communism; it was 7.6% of GDP in 1993.

Most *health* indicators suggest that the general health of the Azeri population is improving, though health standards remain quite low by E&E norms. Life expectancy in Azerbaijan has been increasing since 1998 and at a faster pace than the rate of increase in Eurasia on average in more recent years. The incidence of tuberculosis has been gradually decreasing in Azerbaijan, though it remains high by E&E standards; only four of the five Central Asian Republics (less Turkmenistan), plus Moldova and Romania had higher incidences of TB in 2008.

Consistent with improving health and a rapidly expanding economy, has been a substantial reduction in the poverty rate in Azerbaijan in recent years, from 40% in 2003 to roughly 10% in 2009. In 2005, 15% of the population in Baku was living in poverty vs. 27% in the rest of the country.

Azerbaijan's *peace and security* score is roughly average by Eurasian standards; six Eurasian countries are less peaceful and secure than is Azerbaijan. Azerbaijan is most advanced in counter-narcotics and well above Eurasian average on that dimension; it lags the most in combating weapons of mass destruction, and is notably below the Eurasian average on that dimension.

**Introduction.** This analysis draws largely on the dataset and methodology of the Europe & Eurasia Bureau's *Monitoring Country Progress* (MCP) system. The core of the MCP system consists of five indices: (1) economic reforms; (2) democratic reforms; (3) macroeconomic performance; (4) human capital; and (5) peace and security. We draw on readily available public data and standardize the metrics to a 1 to 5 scale in which a 5 represents the most advanced standards worldwide. Supplemental data and analysis are drawn from a handful of Azerbaijan-specific documents, primary among them are the World Bank, *A New Silk Road: Export-led Diversification* (December 2009); the Asian Development Bank, *Azerbaijan Statistics* (2010); the European Commission, *Progress Report: Azerbaijan* (December 2010); the Economist Intelligence Unit, *Azerbaijan* (December 2010); and the U.S. Energy Information Administration, *Country Analysis Brief Azerbaijan* (November 2010).

**Overview of progress across the five MCP dimensions.** *Figure 1* shows the distribution of the scores for the 29 E&E countries across the five dimensions measured by the MCP system, as well as the average scores for the three geographic sub-regions (countries of the Northern Tier Central and Eastern Europe (CEE), the Southern Tier CEE, and Eurasia) in each of the dimensions. Azerbaijan's progress is below Eurasian average in democratic reforms, well-above Eurasian average in economic performance, and roughly Eurasian average in economic reforms, human capital, and peace & security. On all five indices, average progress in Eurasia is well below progress in the countries of Central and Eastern Europe.

**Economic and democratic reforms.** *Figure 2* highlights economic and democratic reform progress across the 29 country transition region. Economic reform data are drawn from the EBRD, *Transition Report* (November 2010); democratic reform data are drawn from Freedom House, *Nations in Transit* (June 2010). Reform changes from the previous year are highlighted by arrows; they represent changes in 2010 for economic reform data and 2009 for democratic reforms.

Of the 29 E&E countries, only Uzbekistan, Turkmenistan, and Belarus lag significantly more in democratic reforms than does Azerbaijan. Only five E&E countries are farther behind in economic reforms than is Azerbaijan: Turkmenistan; Belarus; Uzbekistan; Tajikistan; and Kosovo. No measurable economic reform progress was made in Azerbaijan in 2010 by EBRD measures; backsliding in democratization occurred in Azerbaijan in 2009 (latest year available) according to Freedom House scores.

**Economic reforms (Figures 3-7).** We categorize the economic reform indicators into two stages. First-stage reforms involve liberalization (of domestic prices and of trade and foreign exchange) and privatization (small- and large-scale); i.e., reforms which reduce government intervention in the economy. Second-stage economic reforms entail building government capacity to regulate and oversee the private sector; in some sense, they involve getting government back in the economic sphere, albeit in a market-friendly way. Second-stage reforms include enterprise reform, competition policy, banking reform, infrastructure reform, and non-bank financial reform. More explicit elaboration of all the MCP indicators and our methodology is provided in the appendix of the annual *Monitoring Country Progress in Eastern Europe and Eurasia* report, available on our website ([http://www.usaid.gov/locations/europe\\_eurasia/wp/](http://www.usaid.gov/locations/europe_eurasia/wp/)).

As shown in *Figure 3*, Azerbaijan made substantial gains in first-stage reforms early on in the transition. However, since 2002, first stage reform progress has stagnated. As is the common E&E profile, second-stage economic reforms in Azerbaijan lag considerably behind first-stage; these reforms in Azerbaijan have stagnated since 2004.

*Figure 4* highlights Azerbaijan's economic reform progress across the nine dimensions, underscoring the notable differences in first stage vs. second stage gains. In no areas are reforms completed. In all of the second stage reforms, as well the first stage reforms in large-scale privatization, significant challenges remain. Only Belarus and Turkmenistan trail Azerbaijan in progress towards large-scale privatization. Azerbaijan has yet to join the World Trade Organization placing Azeri exporters at a distinct disadvantage to competitors as their products lack the tariff protection granted by membership in the group. With regards to competition policy, Azerbaijan has made little progress towards establishing procurement processes that promote competition. The banking sector is still dominated by state players with a considerable portion of loans provided to state-owned enterprises effectively increasing the borrowing costs to non-state entities. Infrastructure is currently a major focus of the government as 45% of Azeri roads have reached, or are beyond, their useful life. In an effort to increase the international competitiveness of the transportation industry the government has invested in three major projects; the North-South Rail corridor linking Azerbaijan with Russia and Iran, the East-West corridor linking Baku and Tbilisi, and the New International Sea Trade Complex located at the intersection of both rail lines near Baku.

We supplement the analysis of the macroeconomic reform trends with microeconomic reform estimates drawing from the World Bank's *Doing Business*<sup>1</sup> global database (*Figures 5 & 6*) as well as the Business Environment and Enterprise Performance Survey (BEEPS) jointly conducted by the World Bank and the EBRD (*Figure 7*). According to the World Bank's *Doing Business* analysis, Azerbaijan's business environment is quite favorable by transition country standards, slightly below the percentile rank of the Northern Tier CEE countries, comparable to that found in Bulgaria and Romania, and much improved since 2007.

Overall, Azerbaijan's business environment ranks 54 out of 183 countries by this measure. Of the ten indicators which comprise the *Doing Business* ranking, Azerbaijan scores the poorest (with a ranking of 177) in *trading across borders*; hampered by a lengthy time to export (43 days vs. Europe and Eurasia average of 26) and a cost per container 80% higher than the Europe and Eurasia average.

The BEEPS survey results (*Figure 7*) seem to provide a much less favorable view of Azerbaijan's business environment than do the *Doing Business* indicators. From a menu of fourteen possible business constraints, enterprises are surveyed on the extent to which such issues are problematic toward doing business. The most recent BEEPS survey was conducted in 2008 and we compare that with the previous results taken in 2005.

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<sup>1</sup> The analysis is based on 10 business environment aspects: starting a business; dealing with construction; hiring and firing workers; registering a property; getting credit; protecting investors; paying taxes ; trading across borders; enforcing contracts; and closing a business.

Well more than a majority of Azeri businesses surveyed in 2008 identified three constraints in particular as problematic: corruption (66% of firms identified it as problematic); tax rates (65%); and access to land (61%). Other indicators of corruption which we highlight below in the discussion on democratic reforms are consistent with these survey results. The challenges stemming from access to land are largely the result of property rights and disputes between local and national agencies over zoning authority.

Four business constraints appear to be significantly growing challenges; i.e., substantially more businesses identified these issues as problems in 2008 than in 2005: corruption; access to land; access to financing; and the skills and education of the labor force. Between 2005 and 2008 the proportion of firms citing access to land as a problem increased from 10% to 61%. During this same time period the percentage of Azeri firms citing the skills and education of workers as a problem increased from 6% to 35%. As evidence of this, the World Bank noted that at the November 2007 Baku Job Fair, no suitable candidates could be found for 50% of the 7,000 jobs offered (World Bank, 2009, p. 136).

Access to financing was noted as a hindrance by 48% of firms surveyed in 2008; a notable increase from 34% in 2005. These perceptions seem to be at odds with the data which show that the availability of credit has been growing at an average of 11.2% per year from 2005 to 2008. Nevertheless, the proportion of domestic credit to GDP remains very low in Azerbaijan: 17% in 2008 compared to 50% for the new EU member countries.

*Figure 7* also highlights areas of perceived improvements in the business climate. Two are notable. In 2004, 65% of Azeri businesses felt the tax administration posed an obstacle to doing business; in 2008, fewer than 40% of businesses felt as such. Second, there was perceived improvements in customs and trade regulations: almost 40% of businesses felt these regulations were burdensome in 2005; by 2008 it had been reduced to 24% of businesses.

***Democratic reforms*** (*Figures 8-12*). *Figure 8* highlights democratic reform trends over time in Azerbaijan and in the E&E region. Four stages are apparent in the case of Azerbaijan: (1) rapid and significant democratic liberalization occurred in the years under Gorbachev leading up to the dissolution of the Soviet Union; (2) democratization backsliding at the outset of the collapse of communisms; (3) a sustained period of stagnation of democratic reforms from 1992 to 2001; followed by (4) steady democratic reform backsliding through 2009 (latest data available).

*Figures 9 and 10* disaggregate the democracy trends in Azerbaijan by democracy sectors or components from 1999 to 2009. Five of the six democratization areas witnessed some notable backsliding in this time period. Independent media and the electoral process reforms regressed the most. Governance reforms are the one area which saw little net change from 1999 and 2009, though these reforms have been gradually deteriorating since 2003. Civil society, rule of law (judicial framework and independence), and national governance in Azerbaijan all witnessed backsliding in Azerbaijan in 2009 according to Freedom House's most recent estimates (in its *Nations in Transit 2010*). According to Freedom House, "no election has been assessed as free and fair since the adoption of the country's constitution in 1995." Freedom House in its just released *Freedom in the World 2011* concludes that Azerbaijan's scores on political rights and civil liberties did not change in 2010.

*Figure 11* displays the seven democracy components in 2009 as measured by Freedom House. Civil society is the most advanced area but is still below Eurasian average; independent media and the electoral process are the least advanced. In Azerbaijan libel is a criminal offense and is frequently used to punish government critics. As of January 2009 a law banning foreign broadcasting on national frequencies effectively silenced international radio transmissions. The lack of media independence has carried over into the electoral process, preventing a robust public debate. In March of 2009 a referendum eliminated the constitutional limit of two consecutive presidential terms, enabling the possibility of a president for life. According to Freedom House, of the CEE and Eurasian countries, only Turkmenistan and Uzbekistan have greater corruption than Azerbaijan (*Figure 12*). The perception of corruption in Azerbaijan, according to Transparency International's *Corruption Perception Index*, aligns quite closely with the estimate of the magnitude of corruption according to Freedom House.

***Economic performance and human capital (Figures 13 & 14).*** *Figure 13* shows the bird's eye view of progress across the transition region in macroeconomic performance and human capital. *Figure 14* shows the components of the two indices. The economic performance index includes key structural economic indicators as well as macroeconomic stability and growth. The human capital index includes indicators of health, education, and income.

By these aggregate measures, Azerbaijan's economic performance exceeds Southern Tier CEE and Eurasia average performance; of the nine Southern Tier CEE countries, only the economies of Bulgaria and Romania outperform Azerbaijan's economy as measured by the MCP economic performance index (*Figure 13*). However, progress across the economic performance dimensions in Azerbaijan is very uneven (*Figure 14*). This may call into question the ability of Azerbaijan's economy to sustain the gains and continue to move forward unless key gaps are sufficiently addressed and, in particular, challenges in diversifying its economy and exports are overcome.

Human capital in Azerbaijan is on par with the Eurasia average, which is itself low compared to the CEE countries (*Figure 13*). The population has witnessed a rapid rise in income but still suffers from health concerns and an education that has prepared them poorly for a modern economy (*Figure 14*).

***Economic performance (Figures 15-19).*** Economic growth in Azerbaijan has been exceptional by many standards for most of the transition years (*Figures 15-18*). From 2002 to 2010, Azerbaijan's economy expanded by an annual average rate of 16%, well above both global and Eastern European standards (*Figure 15*). Azerbaijan's economy weathered the global economic crisis in 2009 well, due in no small part to its robust oil sector, but augmented by the strong growth of its service sector. Of the CEE and Eurasian countries, Azerbaijan's GDP growth in 2009 was the highest; and comparable to the magnitude of growth in China (*Figure 16*). Azerbaijan's economy is estimated to have expanded by 4% in 2010, one of the better performances in E&E (*Figure 17* and *Figure 18*). Recognizing a number of caveats in making this comparison, the current size of Azerbaijan's economy is virtually twice as large as what it was in 1989 (*Figure 19*). This is well above economic growth trends elsewhere in the region; the

Northern Tier CEE countries have economies today on average which are 40% larger than the economies prior to the collapse of communism.

The effect of Azerbaijan's dependence on oil is difficult to overstate. Oil production and GDP in Azerbaijan are closely intertwined, increasingly so (*Figure 20*). The World Bank estimates that the oil share of GDP in Azerbaijan increased from 20% in 1995 to 40% by 2005 to 60% by 2008. Oil exports increased from 40% of total exports in 1995 to more than 95% by 2007. Oil revenues as a percent of total government revenues have grown from less than 10% in 1998 to 40% by 2002 to 75% in 2008 (World Bank, 2009, p 8).

With recent oil discoveries, oil production is now forecast to remain roughly constant through 2024 and decline thereafter (*Figure 22*). *Figure 21* suggests that the contribution of oil to Azerbaijan's GDP may have peaked in 2008. However, a key variable is the price of oil which experienced a rapid and substantial increase from 1998 to 2008 to historically high levels, followed by a very significant drop in 2009 and partial recovery in 2010. In any event, oil's contribution to Azerbaijan's economy is generally far larger than even among the other energy producers in Eurasia.

The impact of Azerbaijan's dependence on oil, largely adverse, is evident in key indicators of Azerbaijan's integration into the global economy (*Figure 23*). The volatility in Azerbaijan's current account balance and in foreign direct investment (FDI) flows, even its export share of GDP, has been extraordinarily high. The current account balance has fluctuated from a deficit of 30% of GDP in 2004 to a surplus of almost 40% of GDP in 2008 as the price of oil skyrocketed. This substantial swing contributed to a significant appreciation of the currency from early 2006 to mid-2008 of close to 20% which in turn made it much more difficult for the Azeri non-oil exports to compete in the world economy, decreasing the prospects for much-needed diversification of the economy. Some sectors such as construction and manufacturing are closely linked to oil production and revenue; while others, such as transportation, trade, and finance continued to expand even as income from the oil sector decreased and the global economy contracted (*Figure 24*). The World Bank has singled out these sectors as focal points for diversifying the Azeri economy. Net FDI as a percent of GDP has ranged from 35% in 2003 to -20% in 2007 (as oil foreign nationals repatriated significant profits home). The export share of GDP fell substantially in one year from 70% of GDP in 2008 to 50% of GDP in 2009.

While the oil economy has constituted at least 50% of GDP in Azerbaijan's economy in recent years, the oil and gas sector employs only 1% of the total work force. Services and agriculture employ the greatest percentage of workers, roughly 48% and 40% respectively. Agriculture in Azerbaijan has averaged growth of more than 5% per year since 2001, yet it remains a very inefficient enterprise. Productivity in the sector remains dismally low, and has only increased marginally in recent years (*Figure 25*). To contrast, agricultural value added per worker is almost four times higher in Armenia and almost two times higher in Georgia; productivity growth in agriculture in Armenia in particular has been very impressive.

*Figure 26* highlights the growing gap between energy production and energy consumption in Azerbaijan; i.e., Azerbaijan's growing energy independence. This is particularly prominent in oil production and consumption. Oil production first exceeded oil consumption in 1998. However, since 2005, such production has increasingly outstripped domestic demand. In

contrast, natural gas production has only recently, since 2007, exceeded domestic consumption in Azerbaijan.

*Figure 27* is an effort to capture broadly both energy independence (or dependence) and energy efficiency across the world. It highlights that Azerbaijan is highly energy independent by global standards; in particular, energy exports are roughly 3.5 times greater than domestic energy use in Azerbaijan. However, *Figure 27* also highlights that energy efficiency in Azerbaijan remains relatively low. More specifically, output per unit of energy use in Azerbaijan is slightly lower than the global average of 5.8. However, the trend over time in energy efficiency has been very favorable; from 2005 to 2007, energy efficiency by this measure increased by 120% in Azerbaijan (*Figure 28*).

Another aspect of global economic integration pertains to communication technology, or the extent to which the population is connected to the world via such technology. The growth of mobile telephone subscriptions as well as internet users has been impressive in recent years in Azerbaijan (*Figure 29*). By 2008, almost a third of the population had access to the internet; this is highest among the Eurasian countries, comparable to that of Romania, yet below Southern Tier CEE average overall (*Figure 30*).

**Human capital** (*Figures 31-36*). The challenges in Azerbaijan's education system are substantial. Education enrollment rates vary tremendously according to the level of education in Azerbaijan. Gross enrollments rates in primary and secondary schools are actually greater than 100% (i.e., some students are "repeaters" and hence are older than the school age category, *Figure 32*). In contrast, pre-primary enrollment rates and tertiary enrollments rates are very low by E&E standards. The pre-primary enrollment rate in 2008 in Azerbaijan was 22% according to UNICEF (and shown in Table 22, *Monitoring Country Progress in E&E*, #12, May 2010); only a handful of other E&E countries have a comparably-low rate, including four of the Central Asian Republics (all except Kazakhstan), Armenia, Bosnia-Herzegovina, and Macedonia. Tertiary enrollment in Azerbaijan is roughly 15%, well below what it was in Azerbaijan at the outset of the transition and well below the large majority of E&E countries today (*Figure 32*). There is, in other words, a precipitous drop off of student enrollments in the Azerbaijan system from the secondary to the tertiary level.

In addition, there is some evidence that the quality of the education at least at the secondary level is notably below OECD standards and is deteriorating (*Figure 31*). The Program for International Student Assessment (or PISA) attempts to measure "functional literacy" or how well 15 year old students are likely to function in a market economy, drawing on practical skills derived from reading, math, and science. Azeri students tested at 81% of the OECD level of performance in 2006 and at 72% in 2009. The 2009 results in Azerbaijan are roughly comparable to test results in Albania and Kazakhstan. Reading and science results lag considerably behind results in mathematics in Azerbaijan.

Public spending on education in 2008 in Azerbaijan was 1.9% of GDP; this is the lowest percentage dedicated to education in the E&E region. Azerbaijan's public spending on education has continually declined since the collapse of communism, from 7.6% of GDP in 1993 to 3.9% in 2000 to 2.7% in 2006 and 1.9% of GDP in 2008 (World Bank, 2009, p. 135). According to



the World Bank, the quality of teaching has declined considerably due to a sharp drop in teacher salaries and deteriorating conditions of the school environment. In addition to the low tertiary enrollment rates, there is also a significant mismatch between skills of graduates and skills needed by businesses. Half of the graduates of higher education are specialized in education, yet this sector of the economy provides less than 10% of total employment. We noted earlier (referring to *Figure 7*) that the percentage of Azeri firms citing the skills and education of workers as an obstacle to doing business increased from 6% in 2005 to 35% in 2008.

Most health indicators suggest that the general health of the Azeri population is improving, though health standards remain quite low by E&E norms. Life expectancy in Azerbaijan has been increasing since 1998 and at a faster pace than the rate of increase in Eurasia on average in more recent years (*Figure 33*). Hence, life expectancy in Azerbaijan at 70 years exceeds the Eurasian average of 68 years. In the CEE countries, life expectancy is closer to 75 years. Under five mortality and infant mortality rates have been falling in Azerbaijan. The incidence of tuberculosis has been gradually decreasing in Azerbaijan as well, though it remains high by E&E standards; only four of the five Central Asian Republics (less Turkmenistan), plus Moldova and Romania had higher incidences of TB in 2008 according to the World Health Organization estimates (*Figures 34 and 35*).

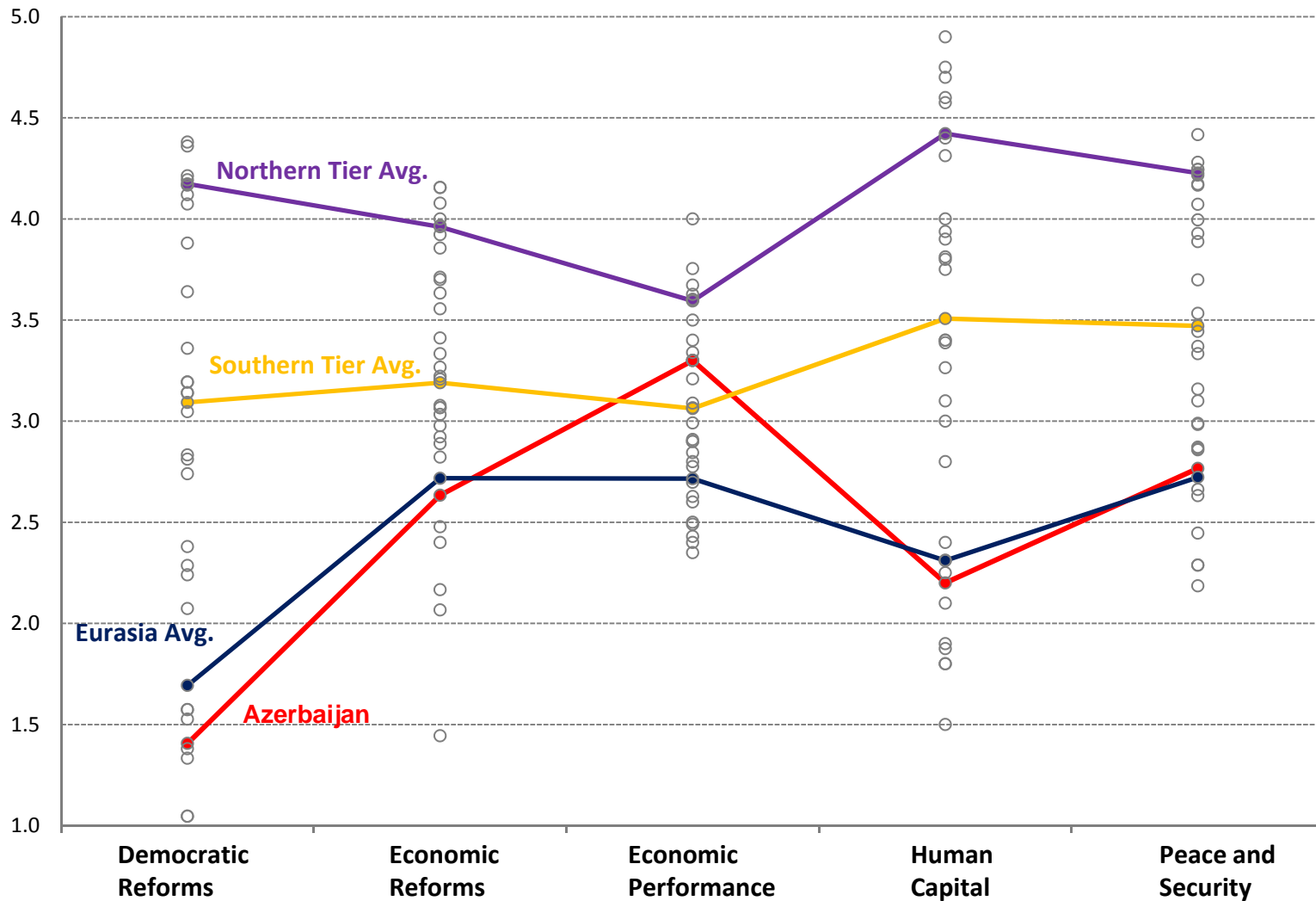
Approximately 18% of adults in Azerbaijan are likely to die before the age of 60. This represents one of the lower adult mortality rates in Eurasia, though it is high by CEE standards (*Figure 36*). Particularly in much of E&E, adult mortality tracks the non-communicable disease and injury rates, which reflect the chronic diseases familiar to more developed countries, and also may highlight risk factors such as tobacco and alcohol use, inactivity, and/or unhealthy diets that lead to chronic disease.

Public spending in health in Azerbaijan as a percentage of GDP was the lowest in the E&E region in 2008 (1.8% of GDP; *Monitoring Country Progress in E&E*, #12, May 2010).

Finally, consistent with improving health and a rapidly expanding economy, has been a substantial reduction in the poverty rate in Azerbaijan in recent years (*Figure 37*), from 40% in 2003 to roughly 10% in 2009. While poverty rates have fallen across the population in Azerbaijan, urban and rural, these rates have fallen significantly more in Baku followed by other urban areas and have decreased the slowest in the rural areas. In 2005, 15% of the population in Baku was living in poverty vs. 27% in the rest of the country.

***Peace and Security*** (*Figures 38-40*). The MCP peace and security index was developed to mirror the six primary elements of the peace and security objective developed several years ago by the Director of Foreign Assistance. These elements include combating weapons of mass destruction, combating transnational crime, counter-narcotics, counter-terrorism, stabilization operations and security sector reforms, and conflict mitigation. Overall, Azerbaijan's peace and security score is roughly average by Eurasian standards; six Eurasian countries are less peaceful and secure than is Azerbaijan (*Figure 38*). Azerbaijan is most advanced in counter-narcotics and well above Eurasian average on that dimension; it lags the most in combating weapons of mass destruction, and is notably below the Eurasian average on that dimension (*Figures 39 and 40*).

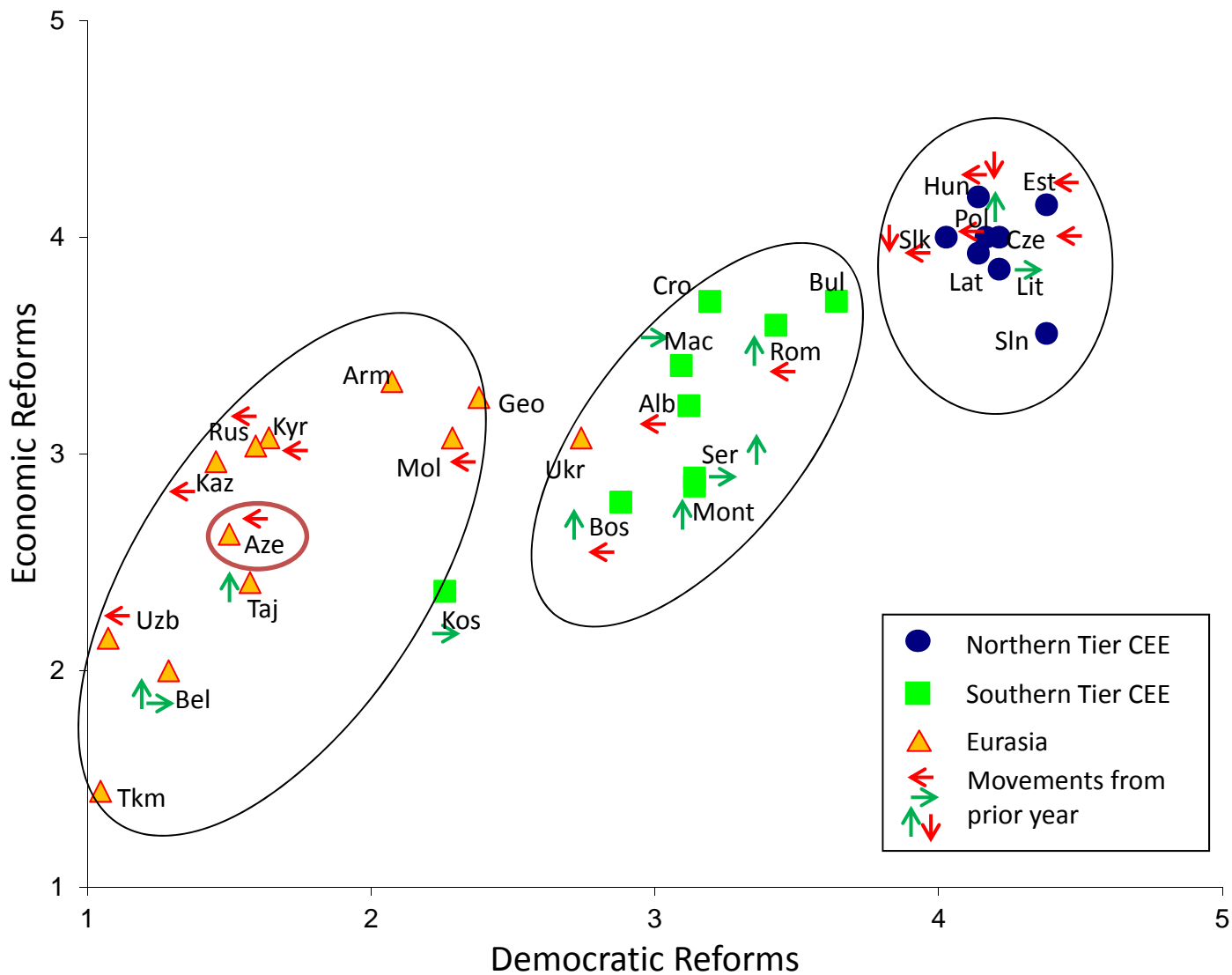
# Azerbaijan- MCP Index Scores 2009/2010



Ratings are based on 1 to 5 scale, with 5 representing the most advanced. Each circle represents an E&E country's score on that Index. The countries of Europe and Eurasia included are: (1) Northern tier countries of Croatia, Czech Rep., Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia, Slovenia; (2) Southern tier countries of Albania, Bosnia, Bulgaria, Kosovo, Macedonia, Montenegro, Romania, Serbia; and (3) Eurasian countries of Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine, Uzbekistan.

Figure 2

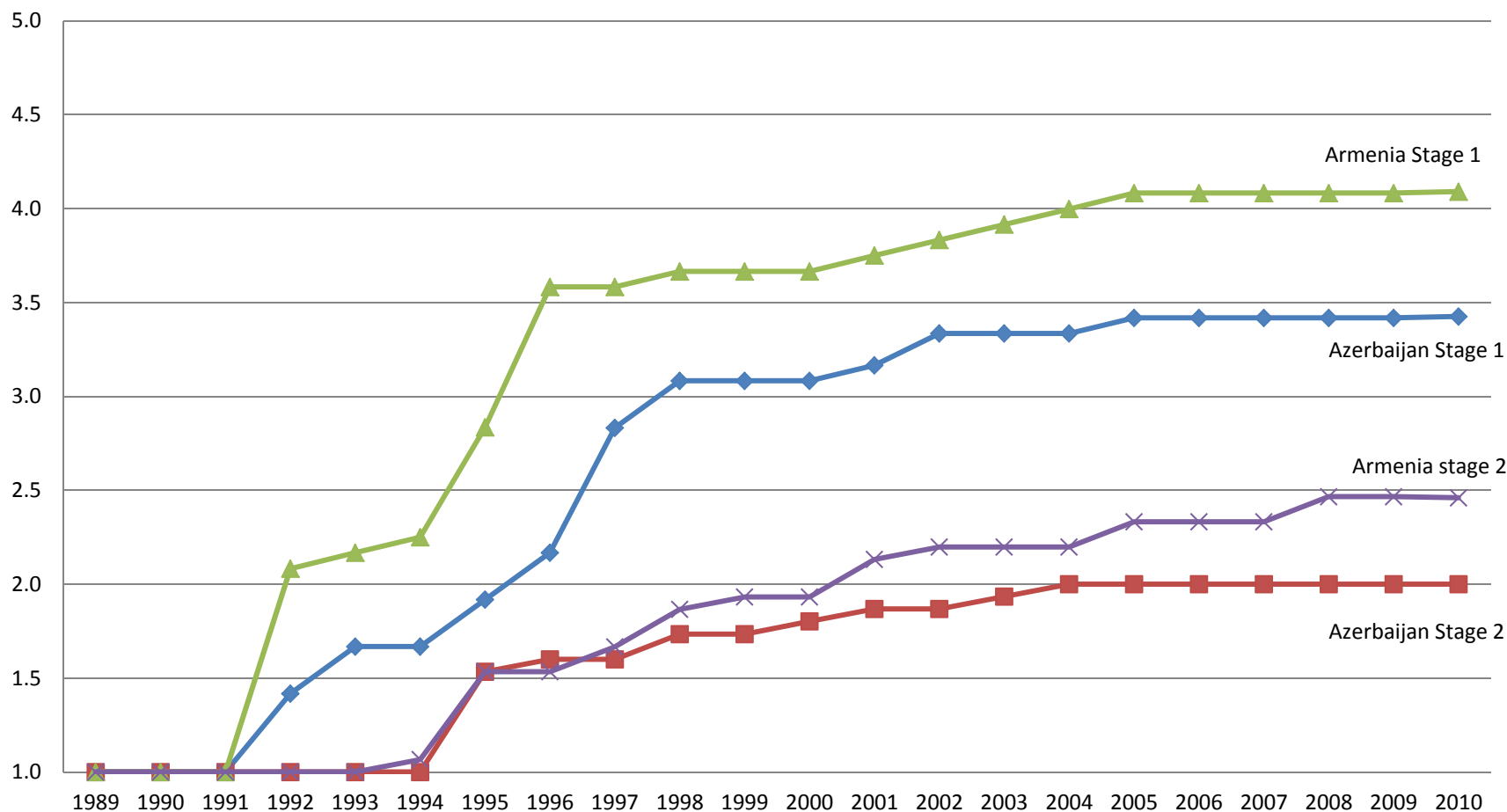
## Economic and Democratic Reforms in 2009-2010



Ratings are based on a 1 to 5 scale, with 5 representing most advanced. Freedom House, *Nations in Transit 2010* (2010); and EBRD, *Transition Report 2010* (November 2010). Economic reforms data are 2010 Democratic Reforms 2009.

Figure 3

# Economic Reform in Azerbaijan (& Armenia) Stage 1 vs. Stage 2 Reforms

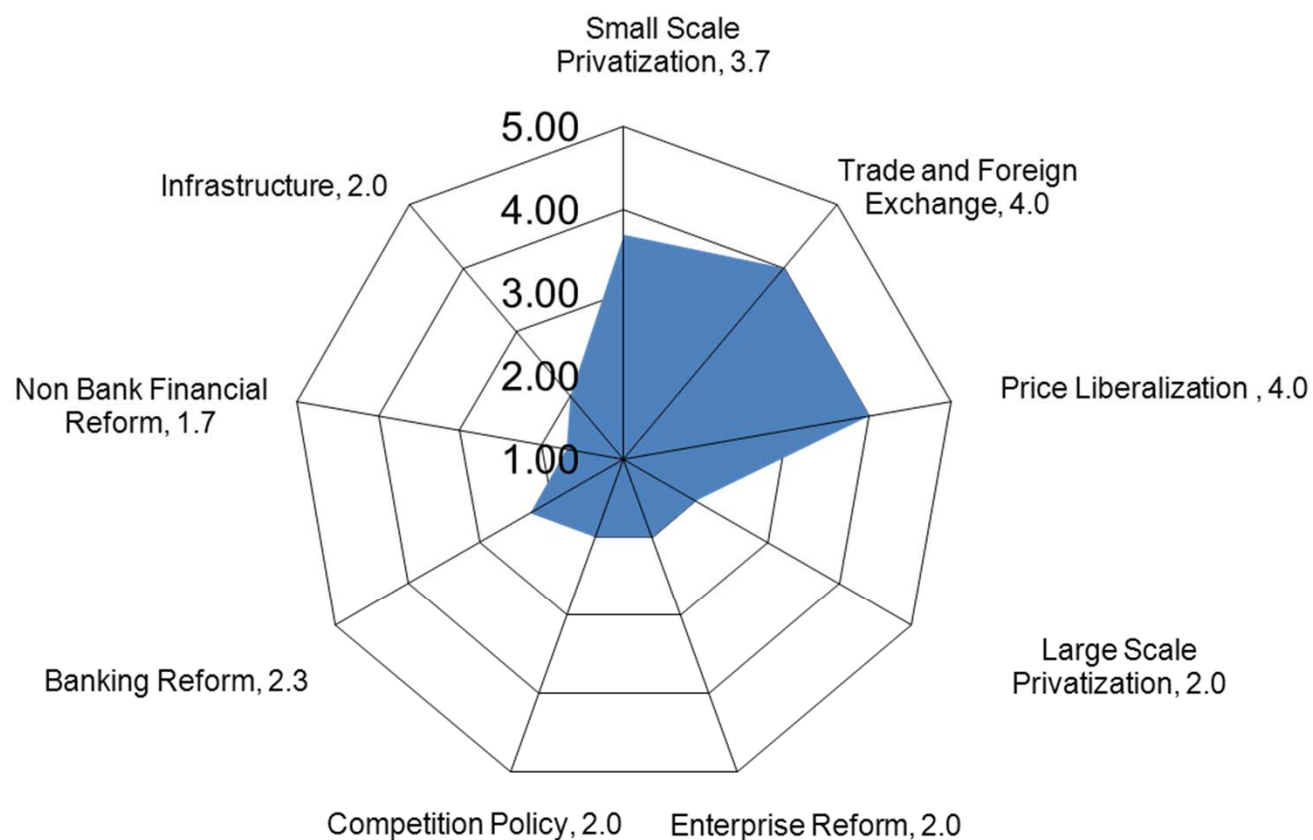


Stage 1: Small Scale Privatization, Trade and Foreign Exchange, Price Liberalization, Large Scale Privatization. Stage 2: Enterprise Reform, Competition Policy, Banking Reform, Non-Bank Financial Reform, Infrastructure.

Ratings are based on a 1 to 5 scale, with 5 representing most advanced. Data are drawn from the EBRD, *Transition Report 2010*

Figure 4

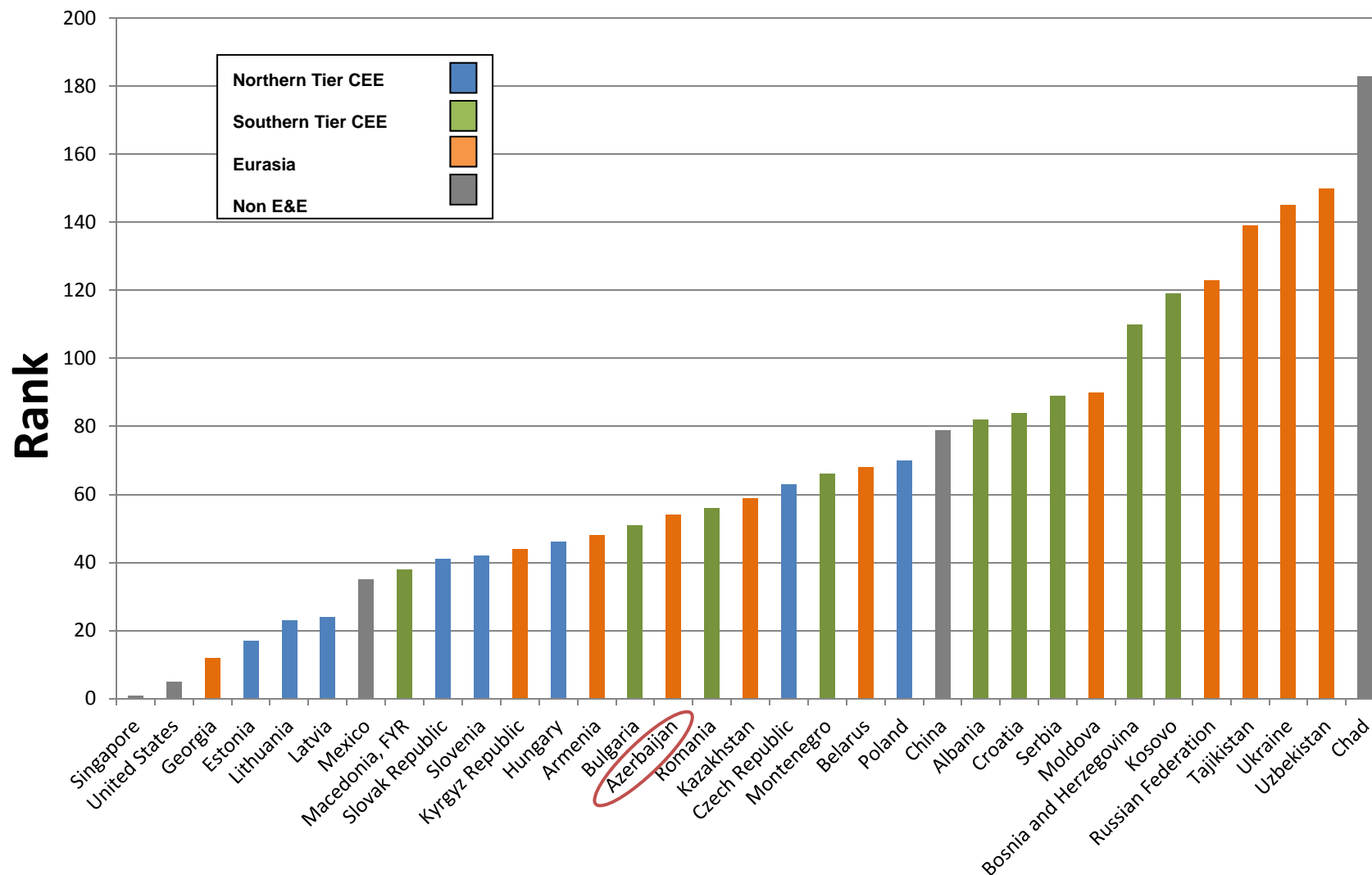
# Economic Reforms in Azerbaijan 2010



Ratings are based on a 1 to 5 scale, with 5 representing most advanced. Data are drawn from the EBRD, *Transition Report 2010*

Figure 5

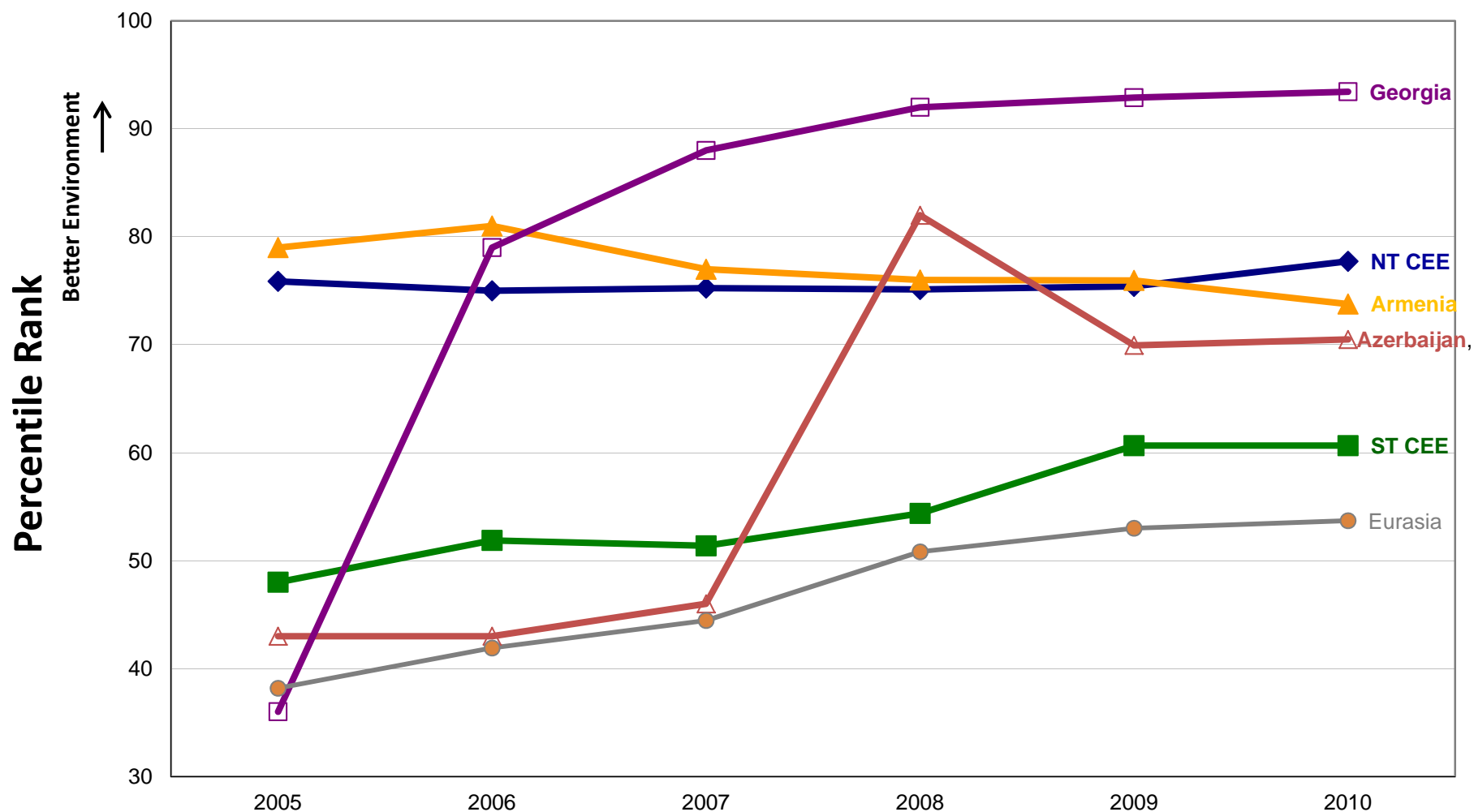
# Business Environment in 2010



World Bank *Doing Business in 2011* (October 2010), 183 countries are included in the analysis. The business environment is gauged based on 10 aspects: starting a business; dealing with construction; hiring and firing workers; registering a property; getting credit; protecting investors; paying taxes; trading across borders; enforcing contracts; and closing a business.

Figure 6

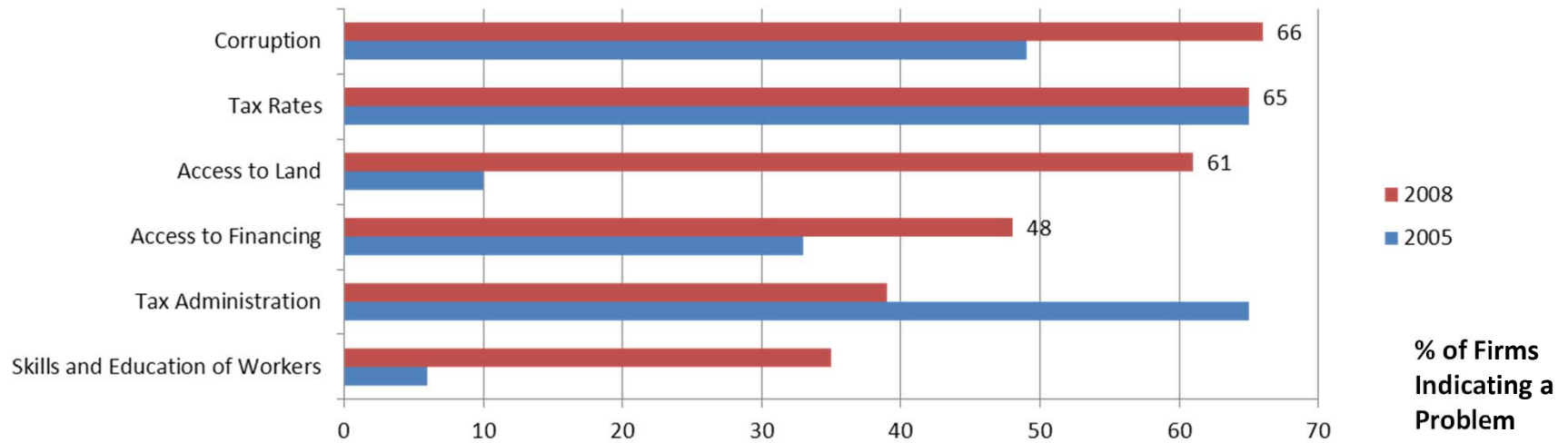
# Business Environment



World Bank, *Doing Business 2011* (October 2010). The analysis is based on 10 aspects: starting a business; dealing with construction; hiring and firing workers; registering a property; getting credit; protecting investors; paying taxes; trading across borders; enforcing contracts; and closing a business.

Figure 7 **Business Problems as Indicated by Firms**

**Biggest Challenges**



**Areas of Progress**

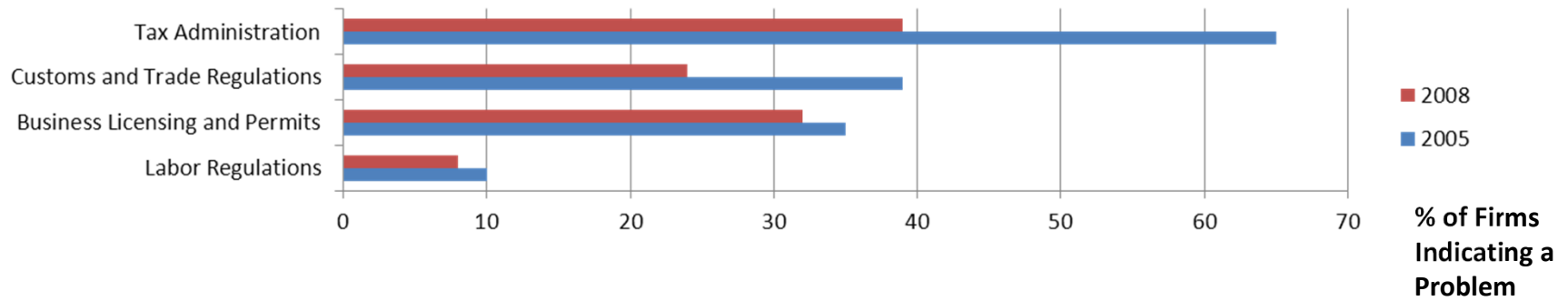
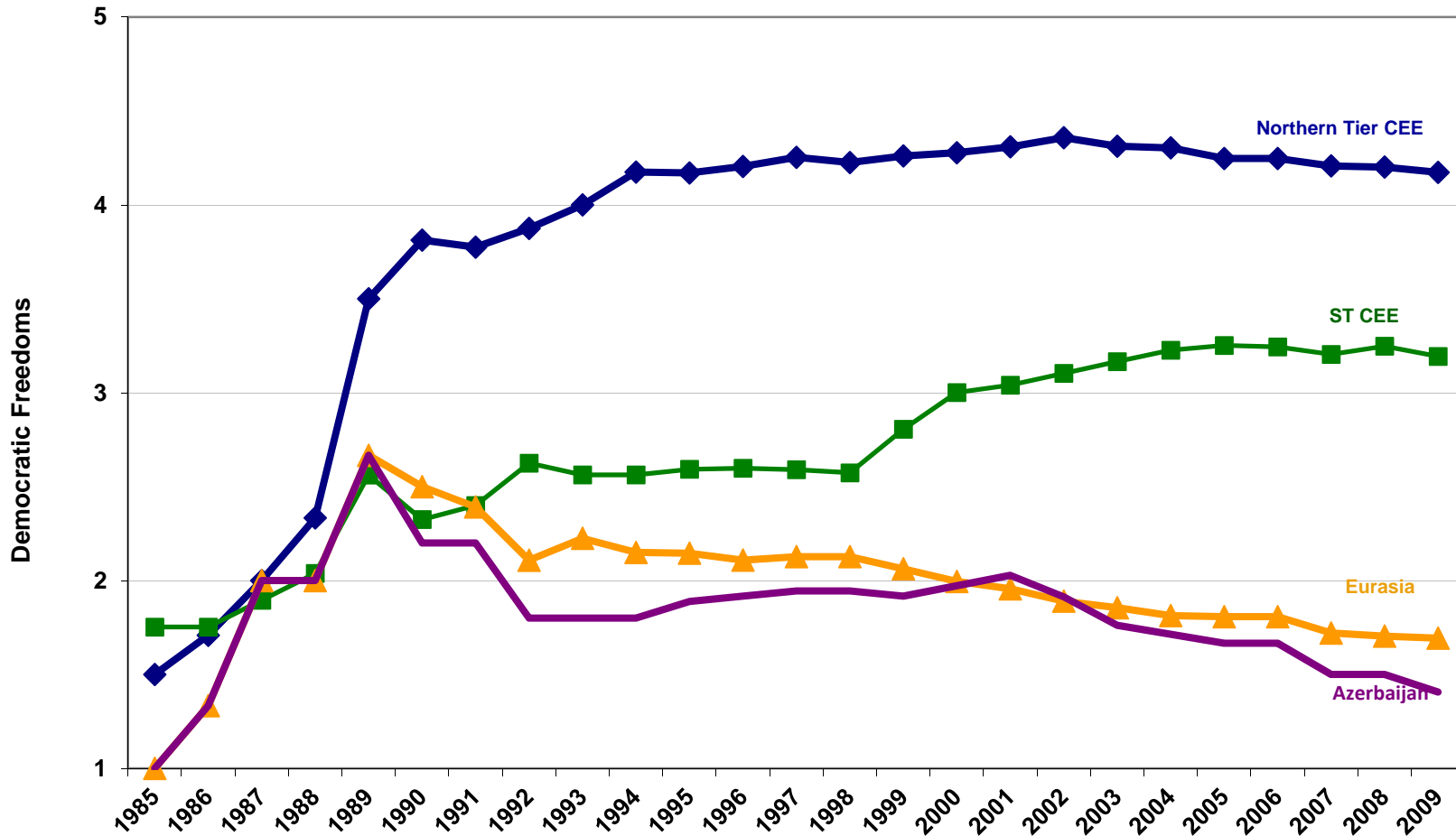




Figure 8

# Democratic Reforms in Azerbaijan



Ratings from 1 to 5, with 5 representing greatest development of democratic reforms. Freedom House, *Nations in Transit* 2010 and *Freedom in the World* (earlier years).

Figure 9

# Democratic Reforms in Azerbaijan over Time

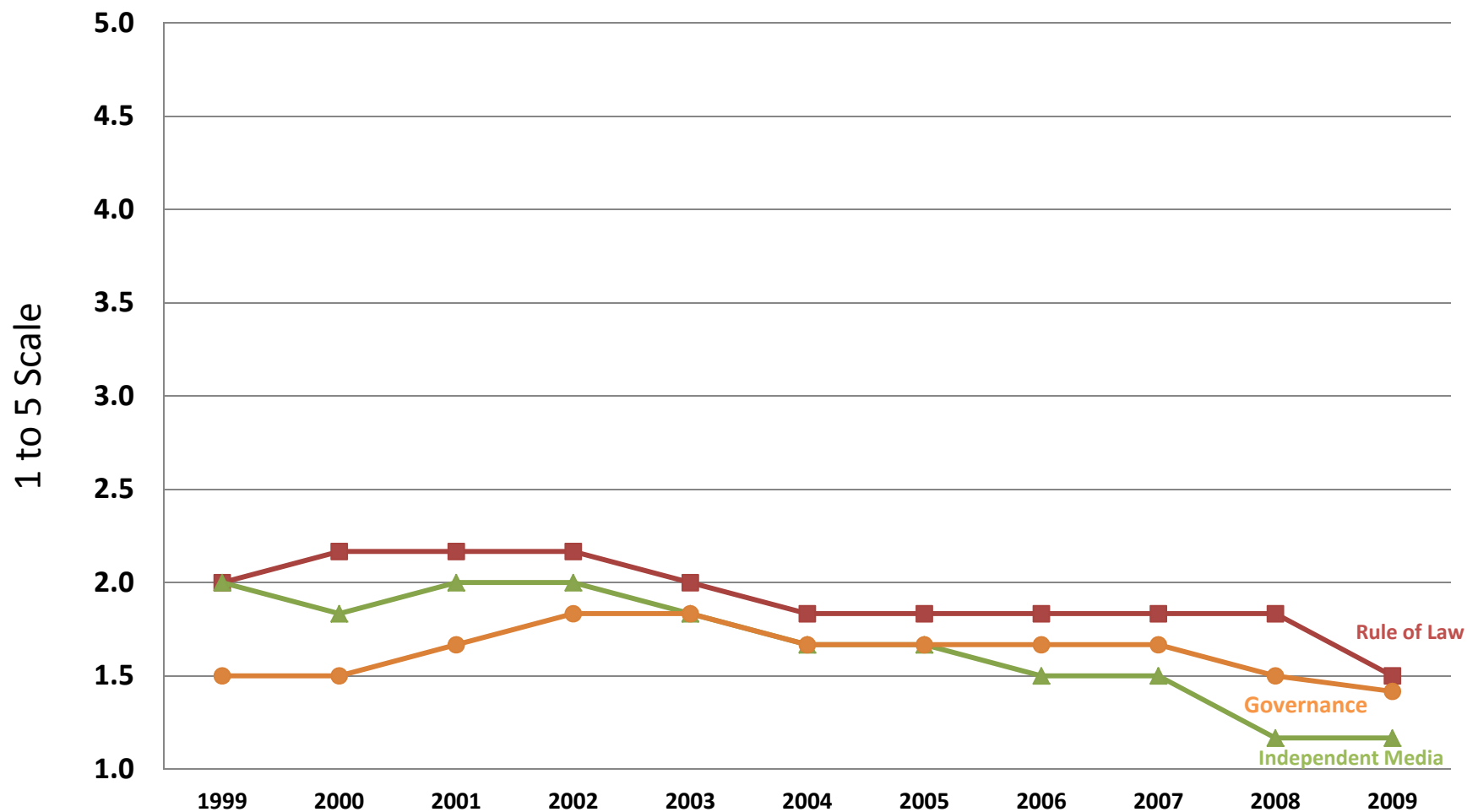


Figure 10

# Democratic Reforms in Azerbaijan over Time

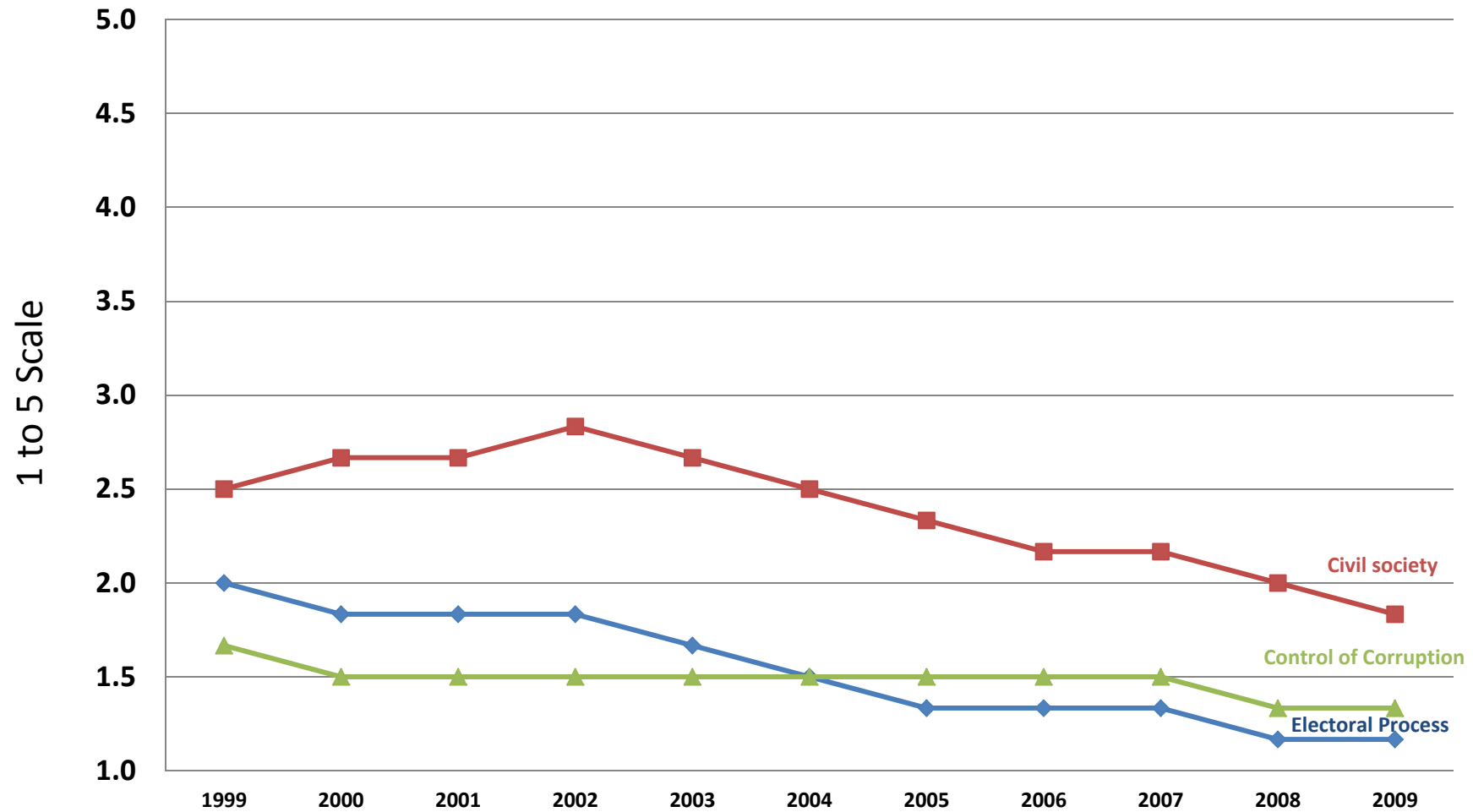


Figure 11

# Democratic Reforms in Azerbaijan in 2009

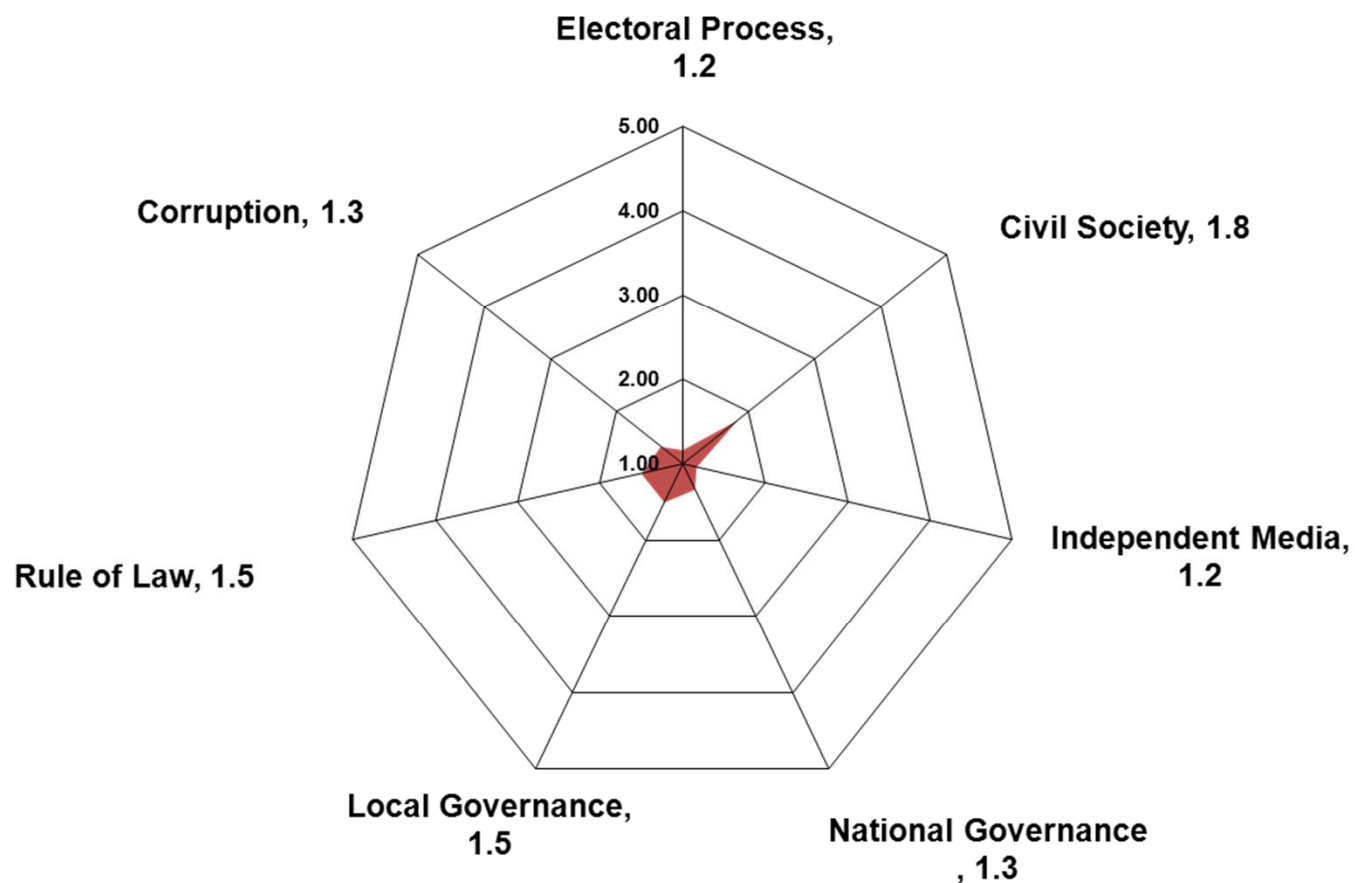
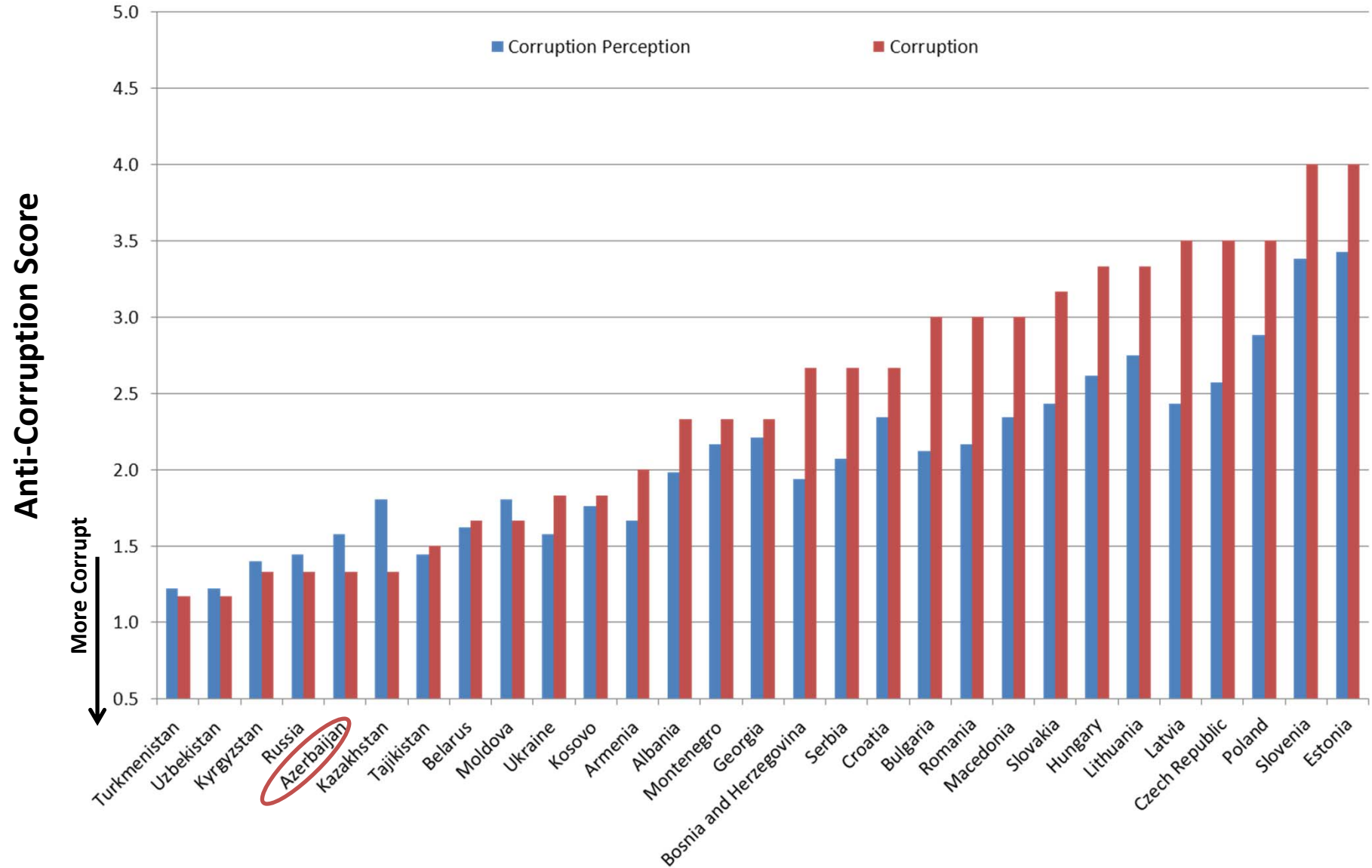


Figure 12

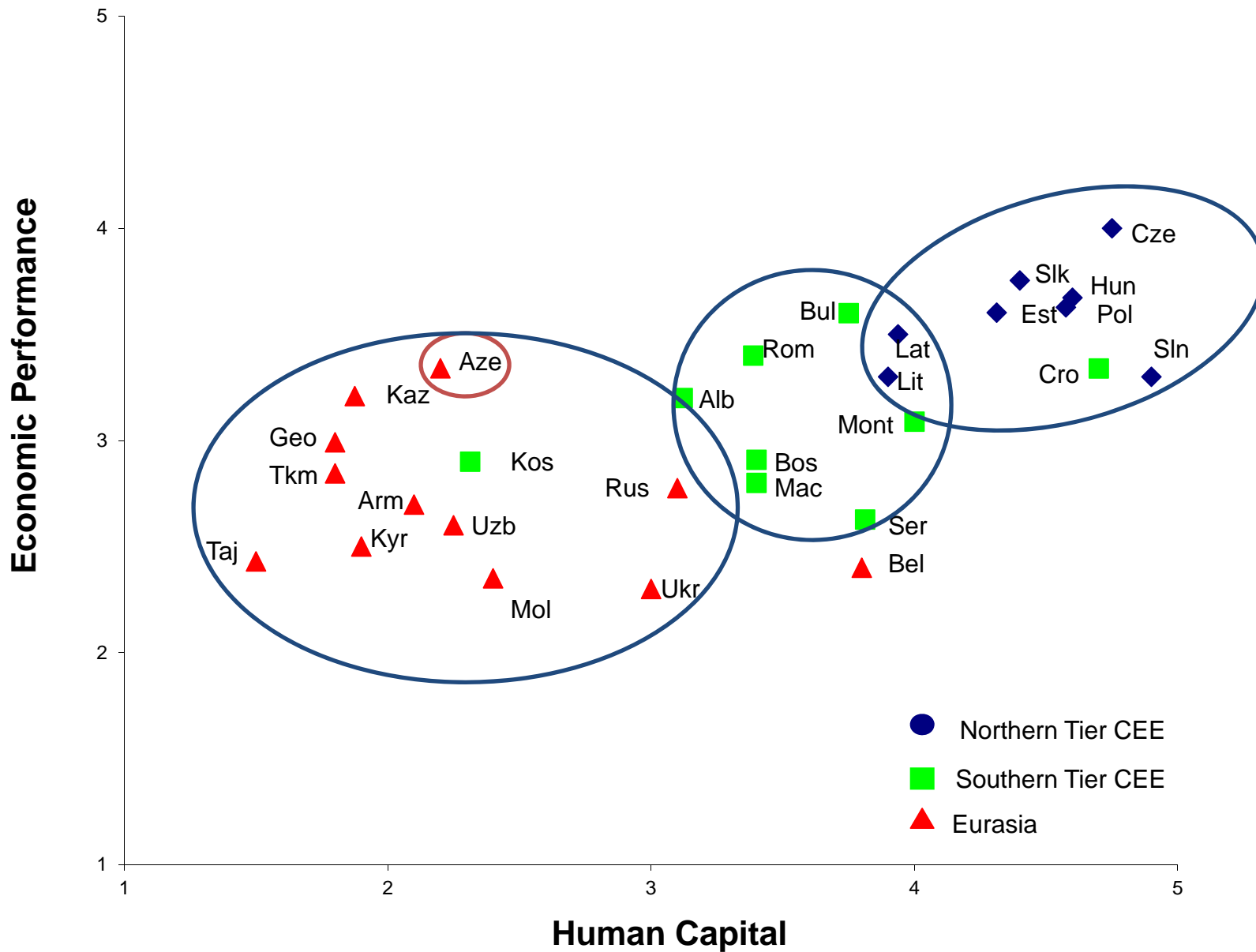
## Corruption and Perceptions of Corruption Central and Eastern Europe and Eurasia



Freedom House *Nations in Transit* 2010 and Transparency International, *Corruption Perception Index* (2010).

Figure 13

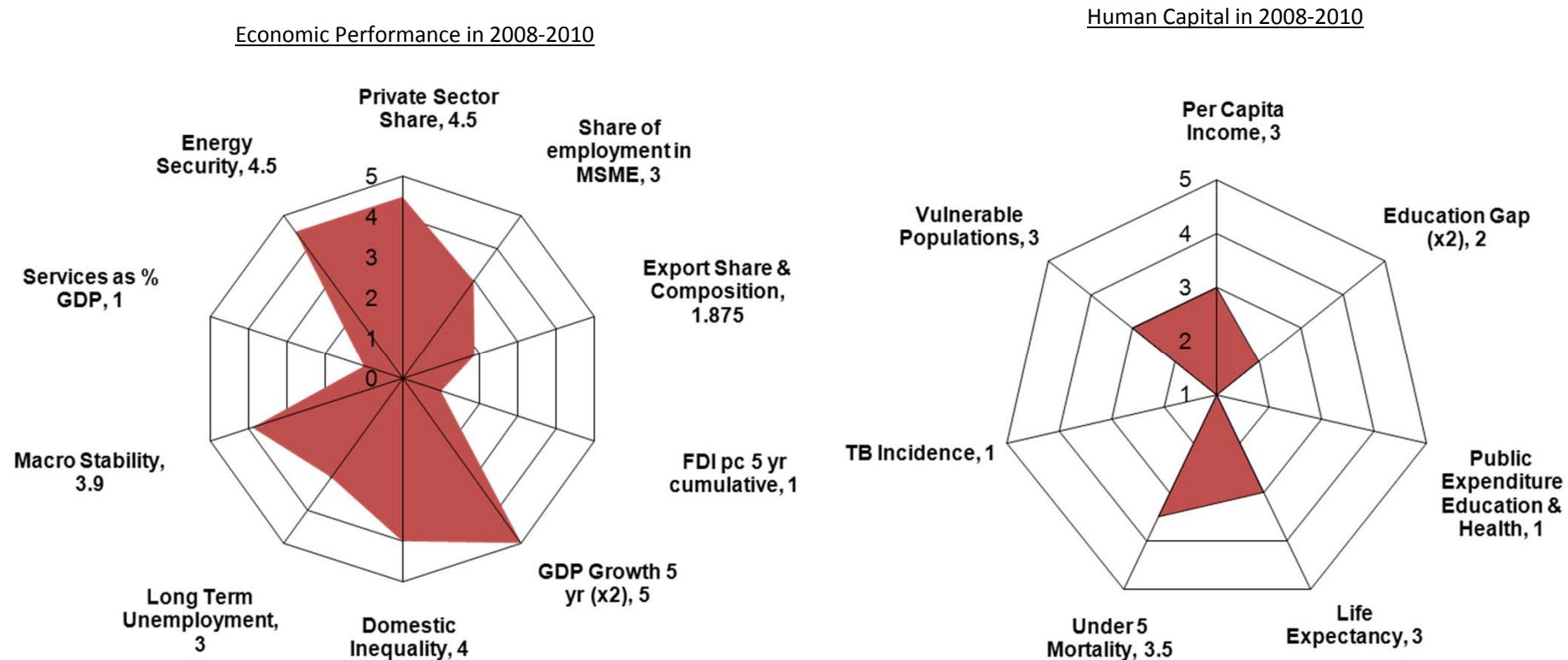
### Economic Performance and Human Capital in 2008-2010



Ratings are based on a scale from 1 to 5, with 5 representing the best score. World Bank, *World Development Indicators 2008* (April 2008); EBRD, *Transition Report 2010* (November 2010).

Figure 14

## Economic Performance & Human Capital in Azerbaijan



Ratings are based on a scale from 1 to 5, with 5 representing the best score. World Bank, *World Development Indicators 2008* (April 2008); EBRD, *Transition Report 2010* (November 2010).

Figure 15

# Economic Growth in Azerbaijan compared to The World and EE

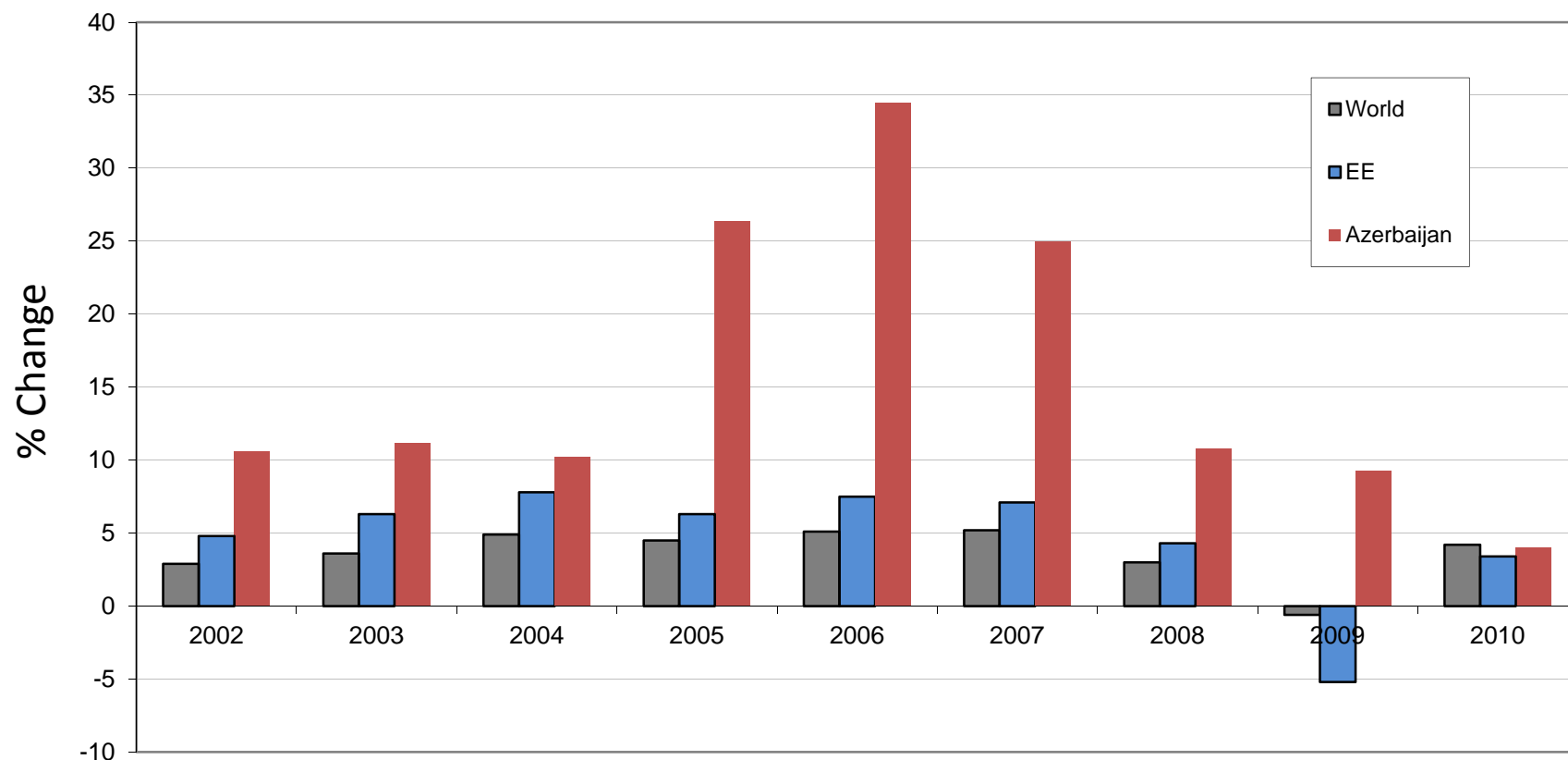




Figure 16

### GDP Growth Estimates, 2009

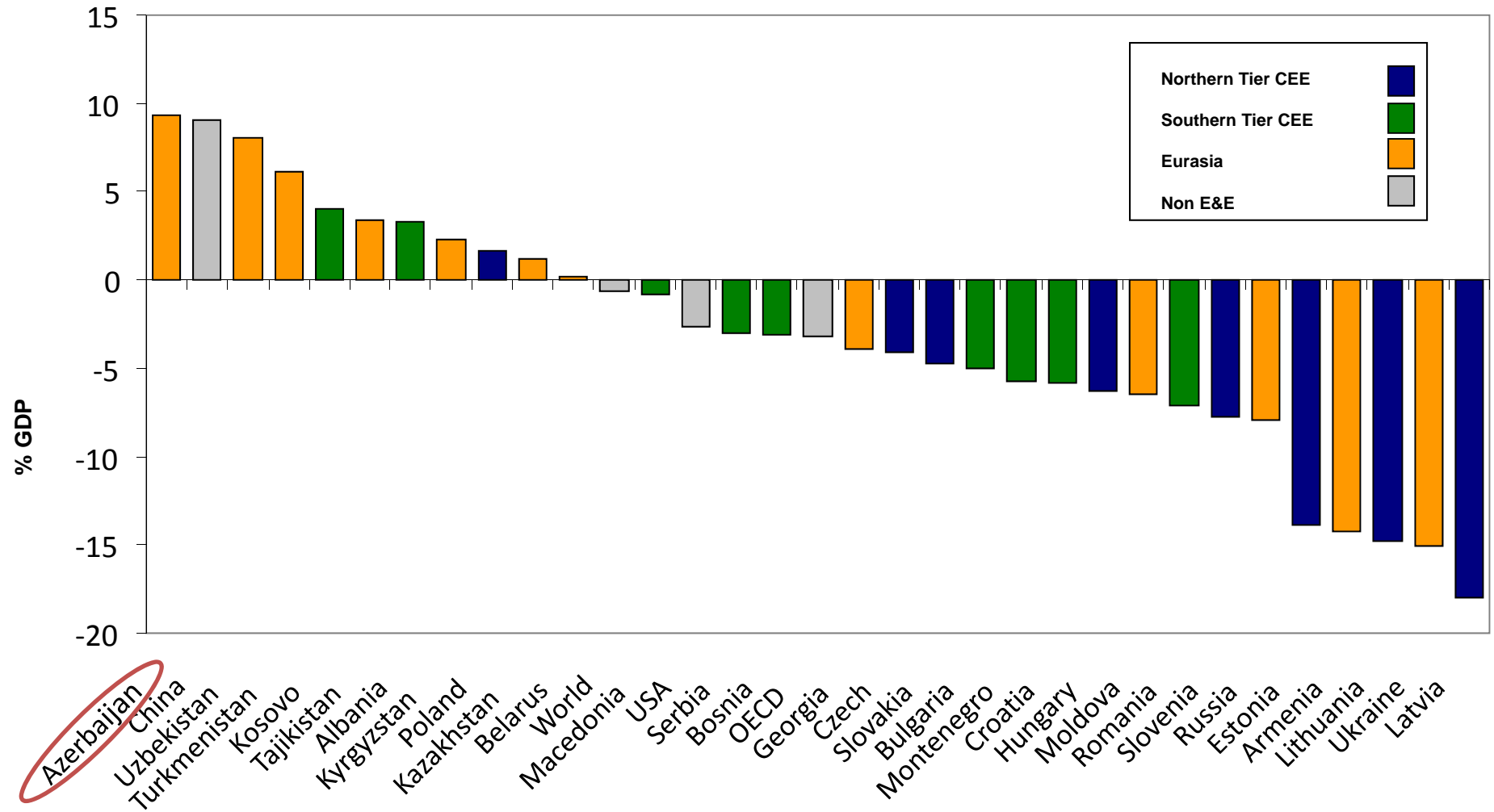


Figure 17

### Economic growth and contraction: the better performers in 2010

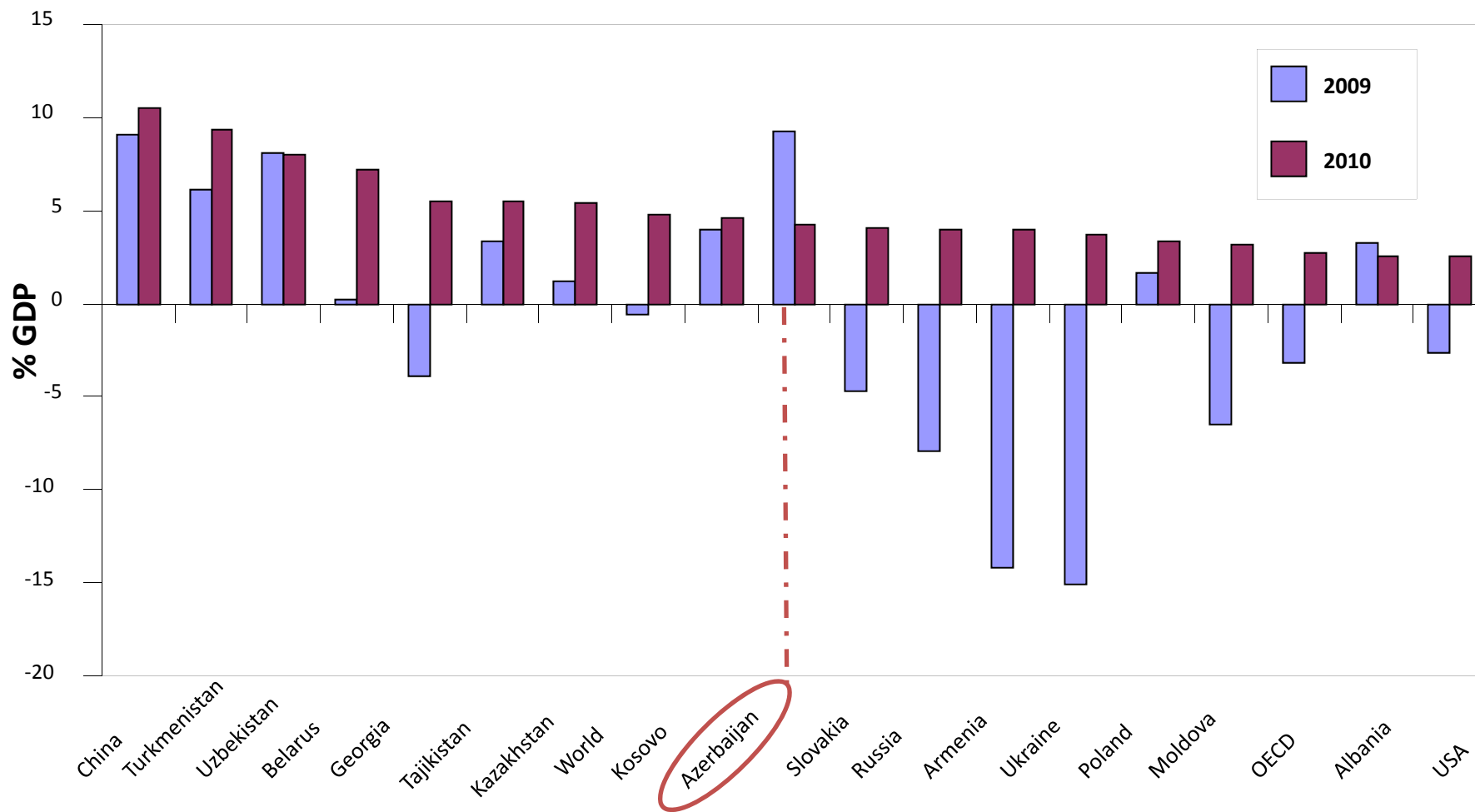


Figure 18

## Economic growth and contraction: the poorer performers in 2010

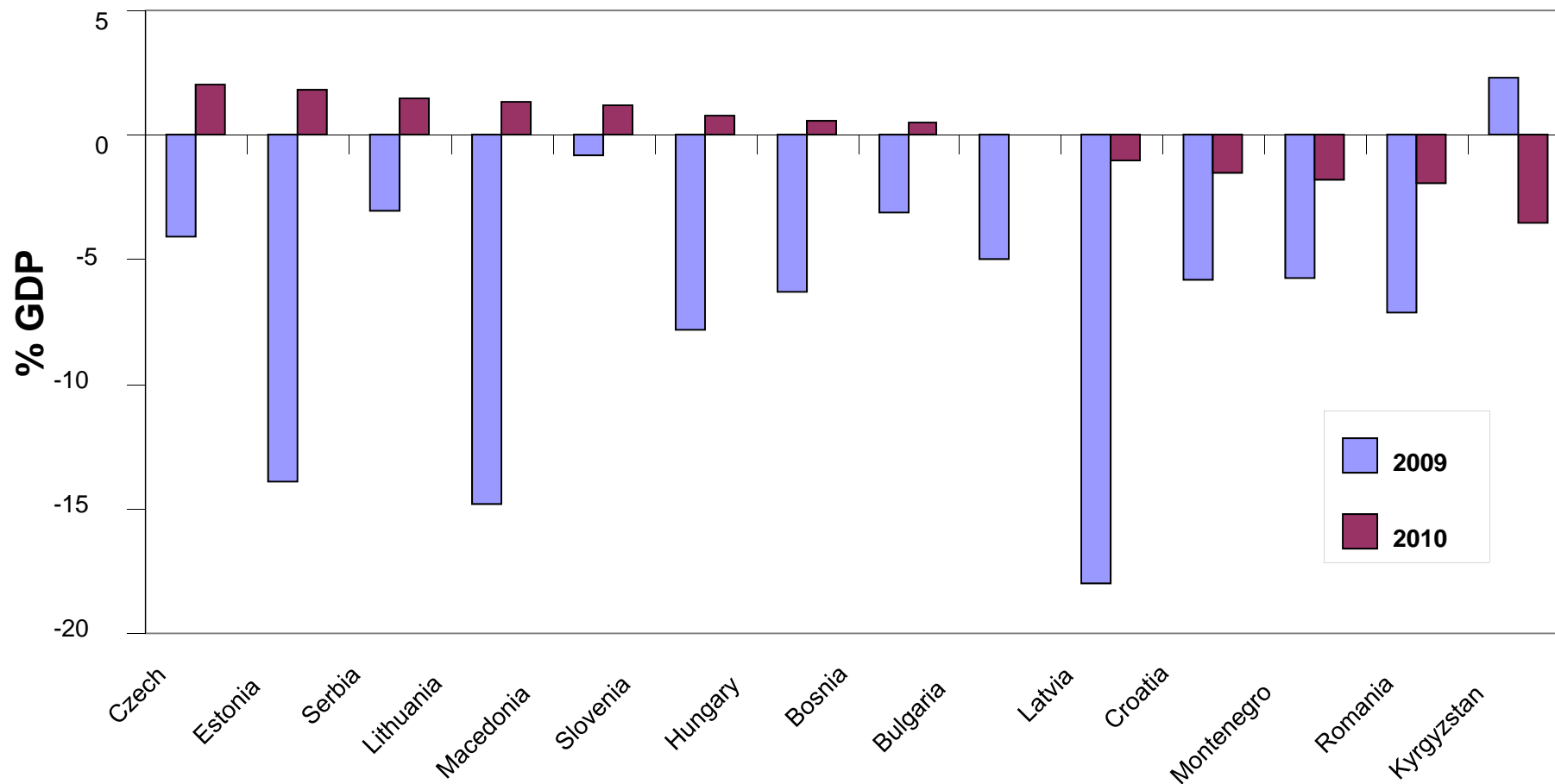


Figure 19

# GDP as % of 1989 GDP

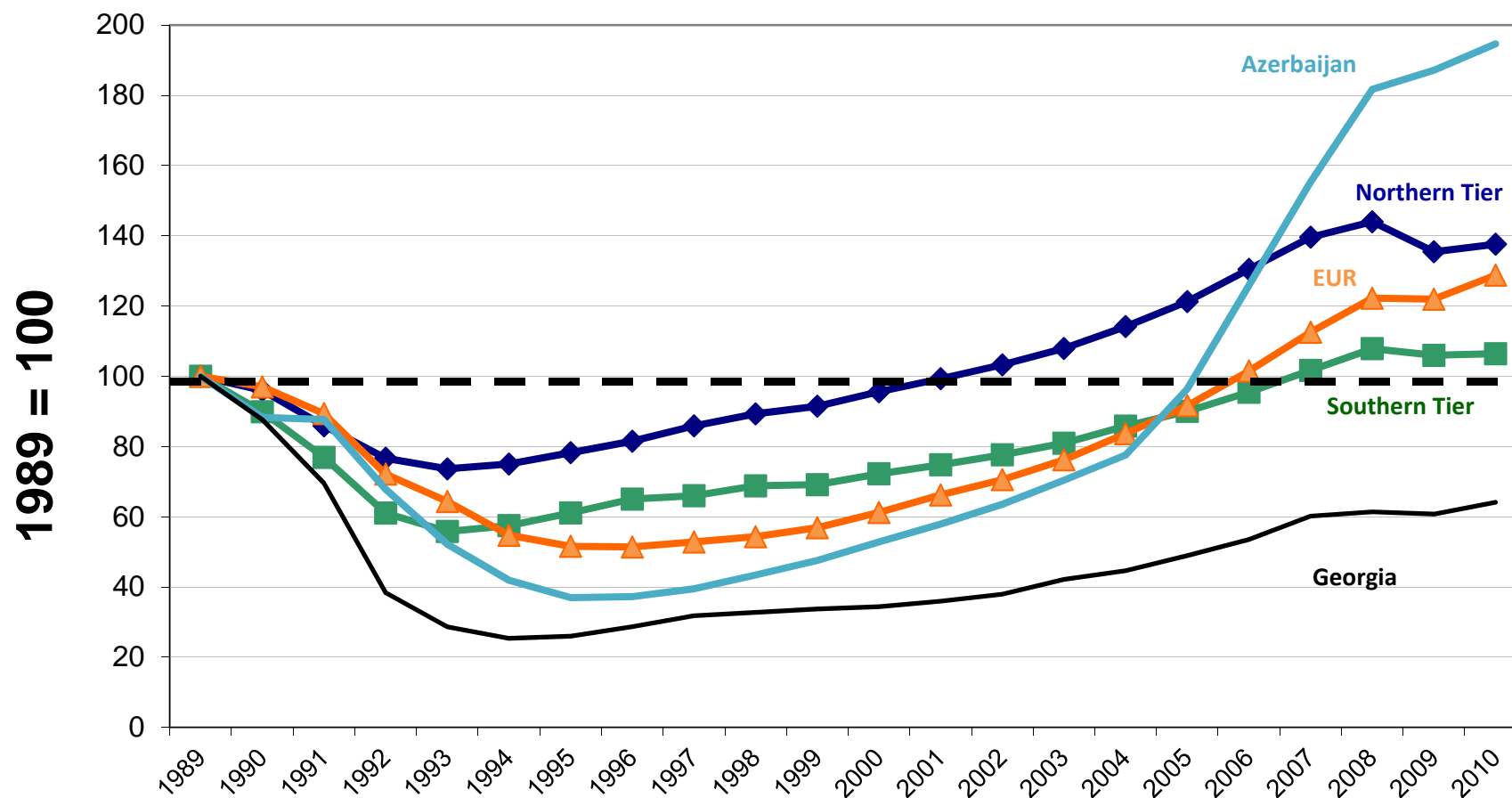


Figure 20

# GDP and its relationship to Oil Production in Azerbaijan

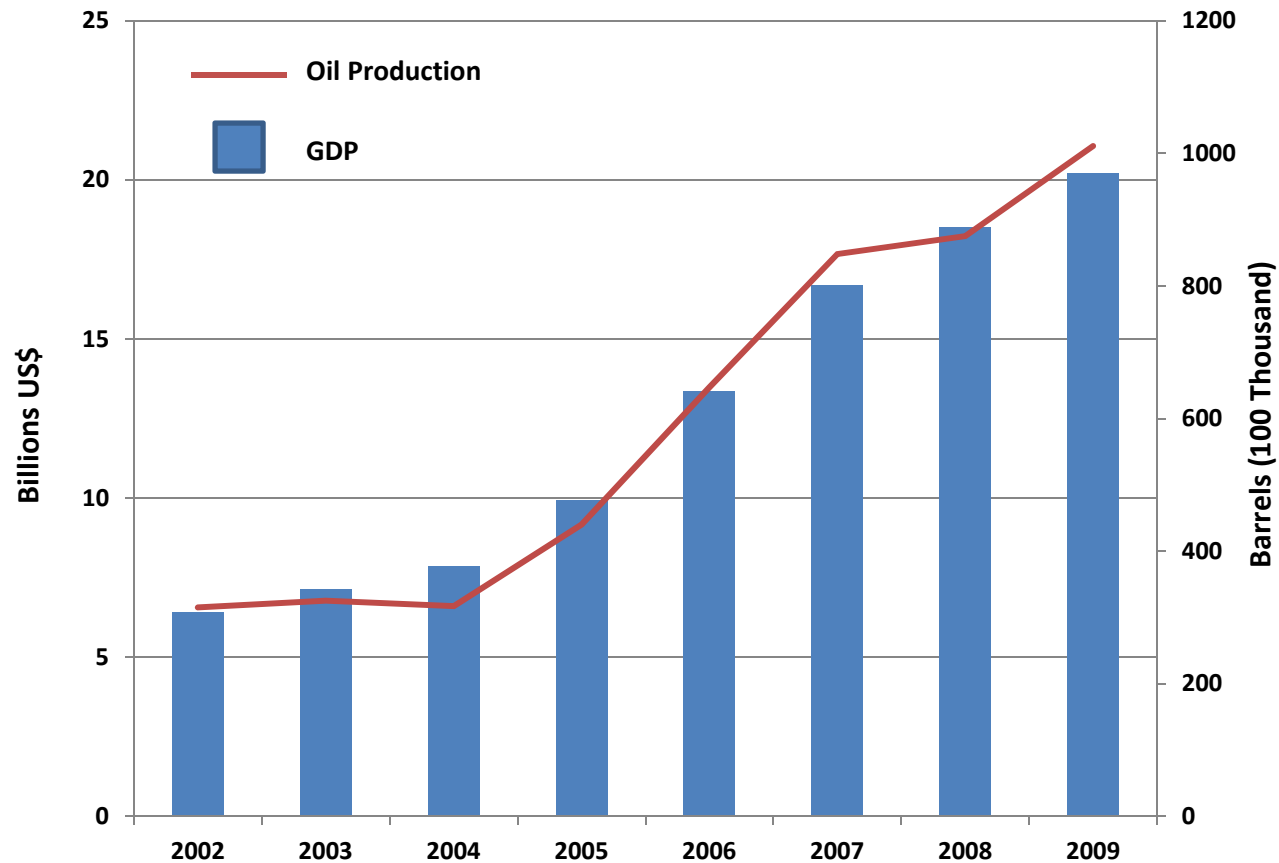


Figure 21

# Export of Fuels, Ores and Metals % of GDP 2007-2009

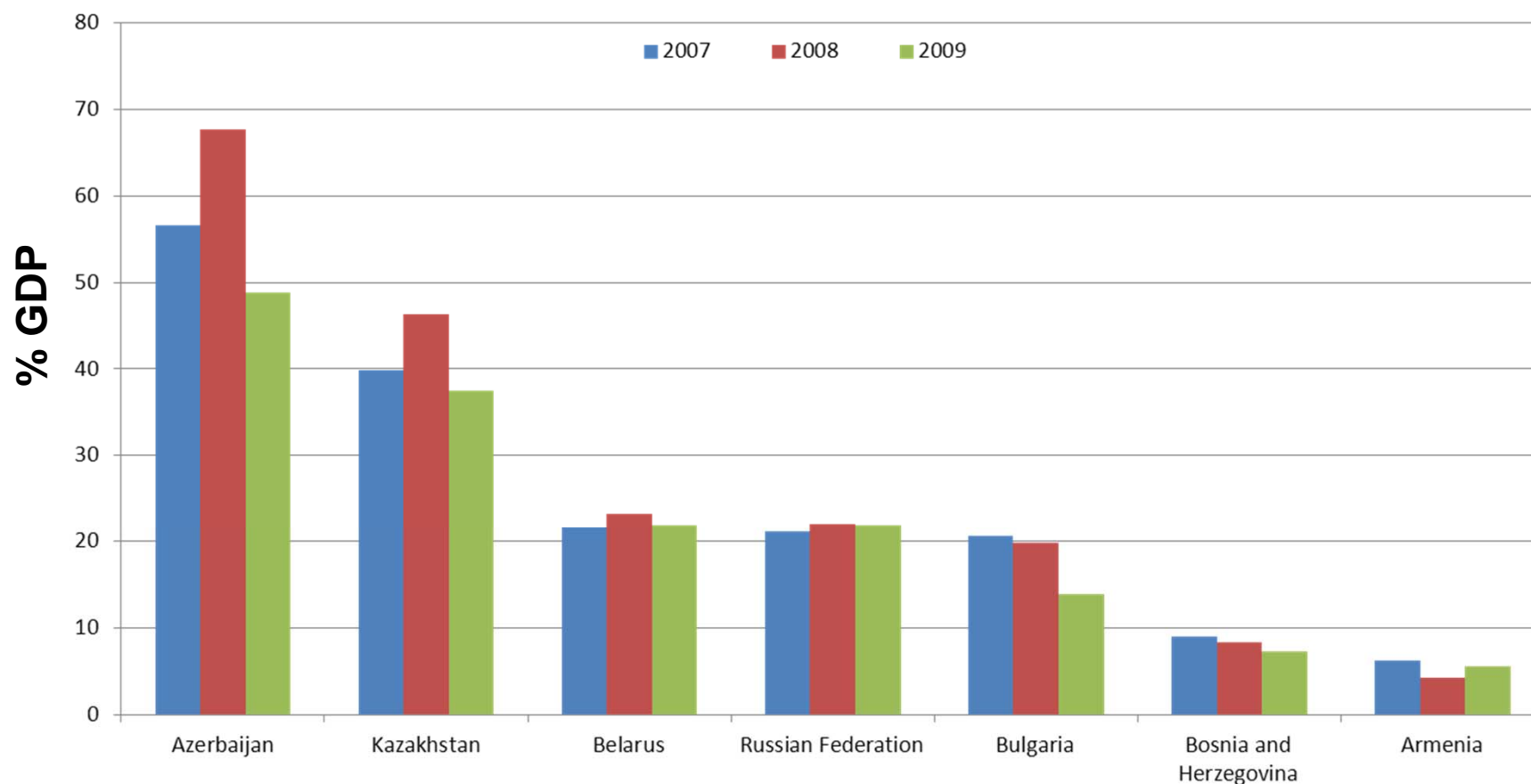


Figure 22

# Oil Production Profile for Azerbaijan

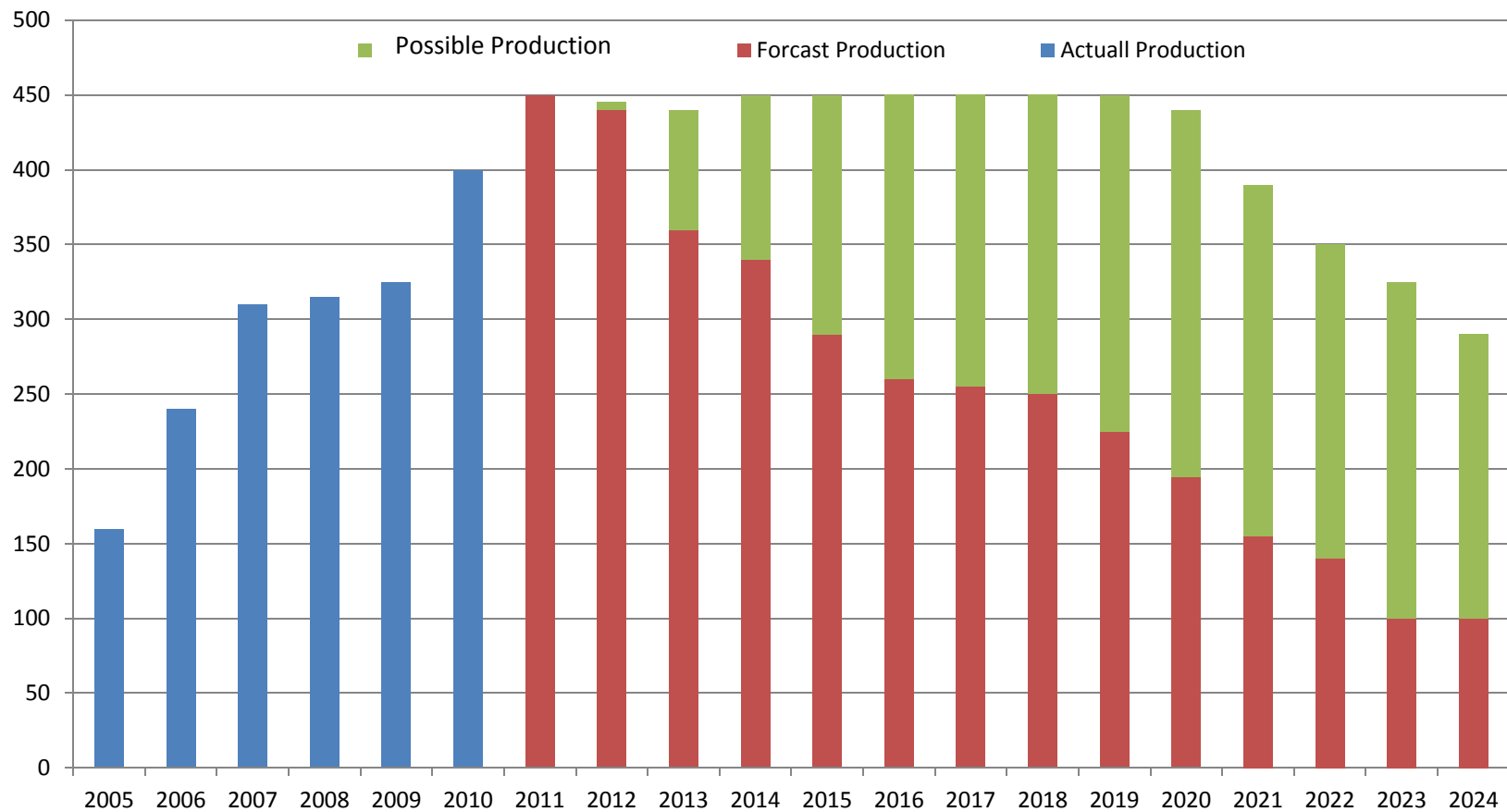
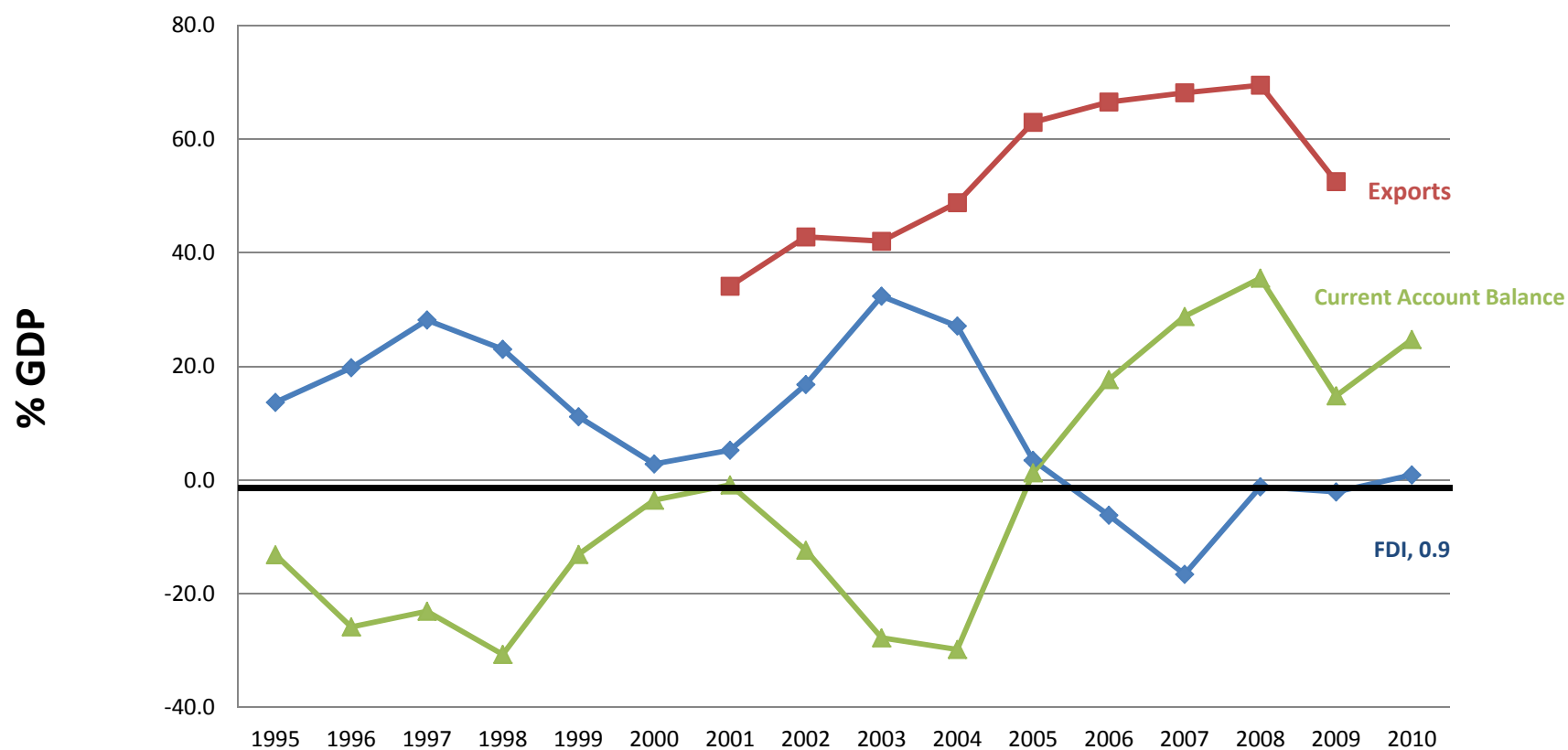


Figure 23

# Azerbaijan's Integration into The Global Economy



EBRD, *Transition Report 2010* (November 2010), *World Economic Outlook Update* (October 2010).



Figure 24

## Azeri Sector Growth in Relation to Oil Prices

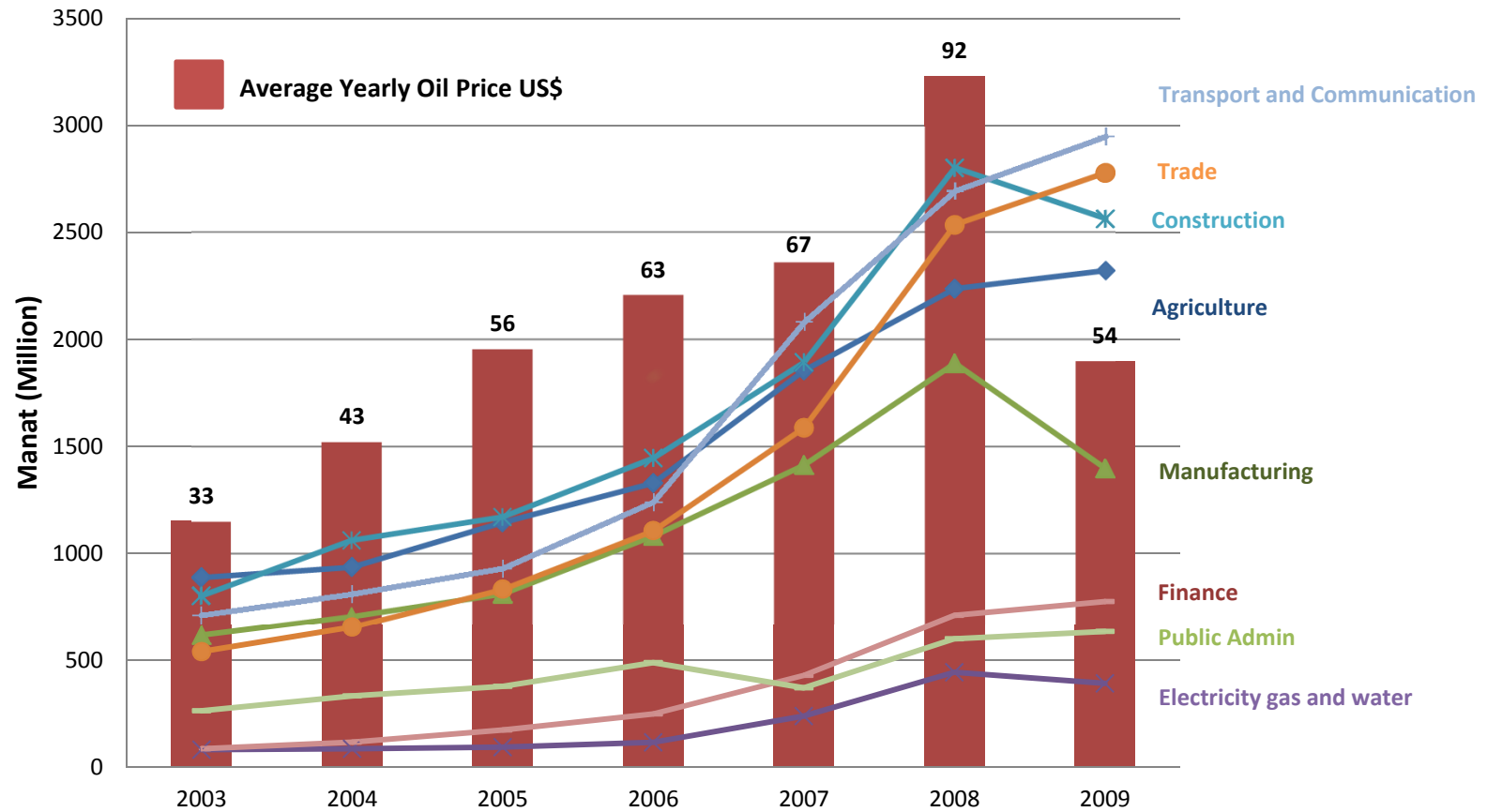


Figure 25

# Agricultural Productivity

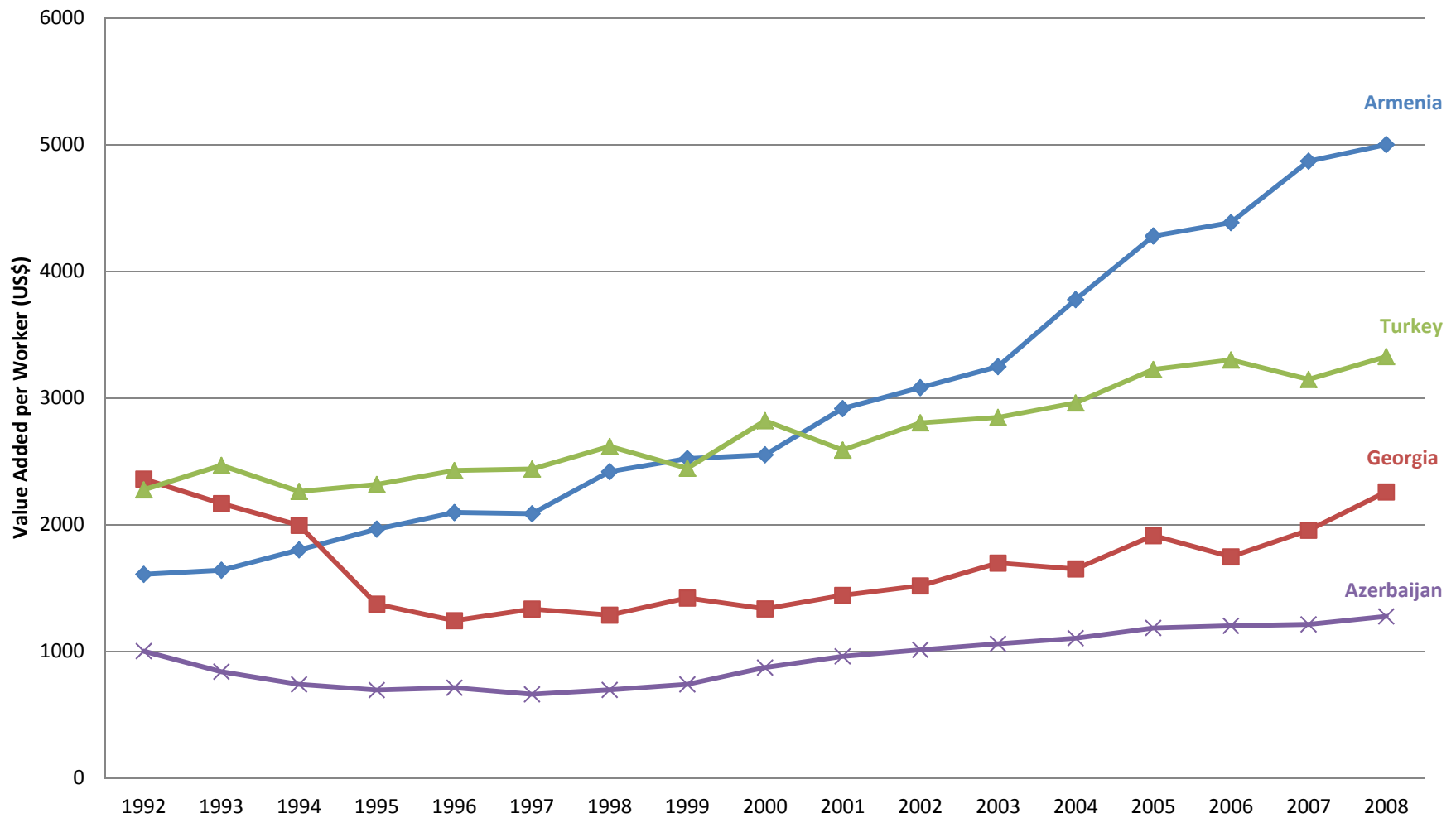
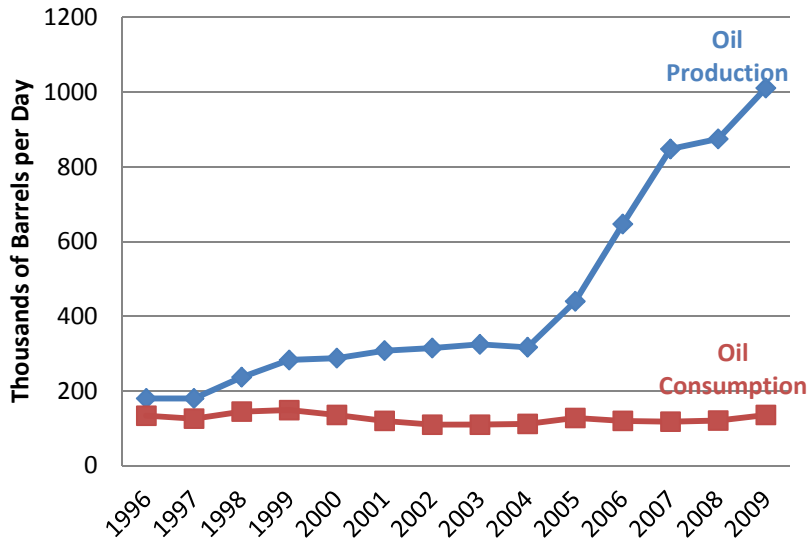
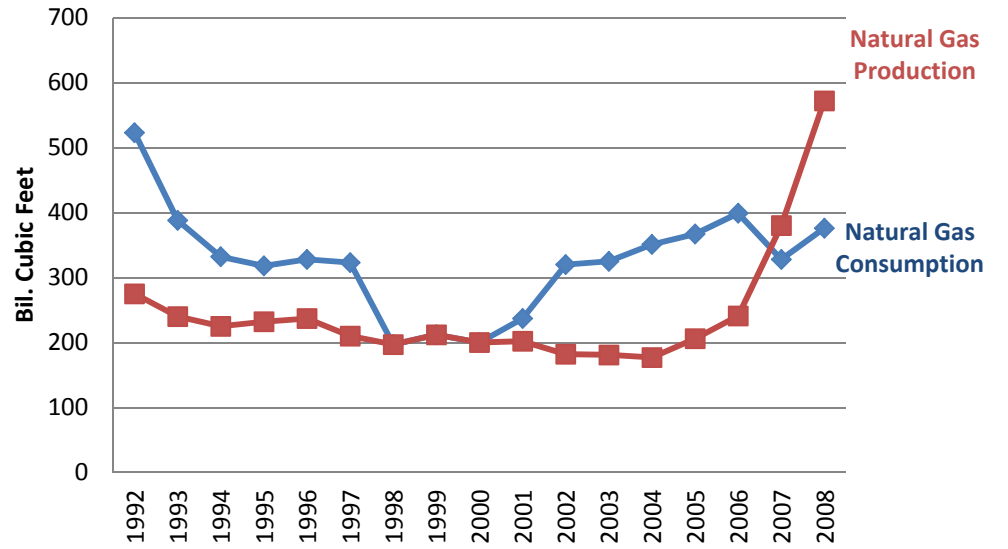


Figure 26

### Oil Production and Consumption



### Natural Gas Production and Consumption



### Electricity Production and Consumption

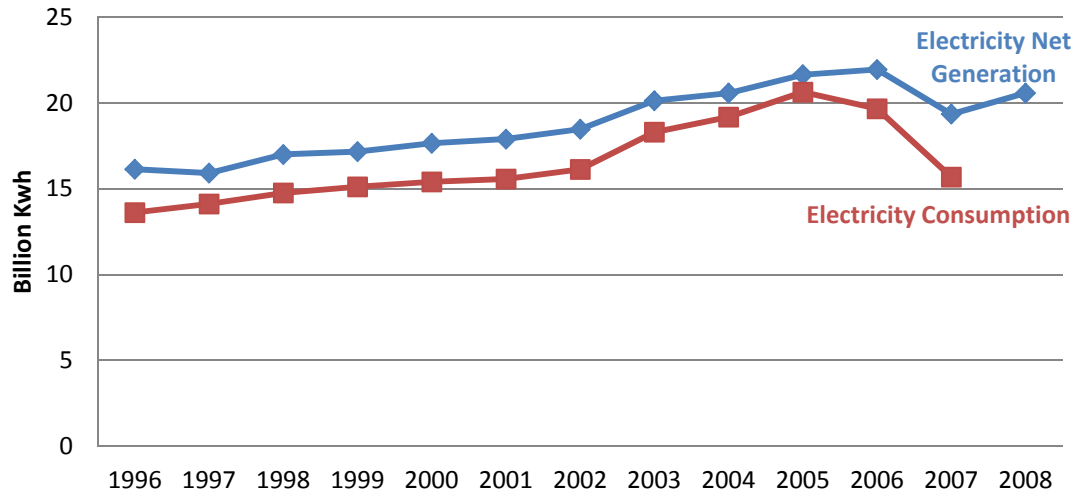


Figure 27

# Energy Dependence and Efficiency

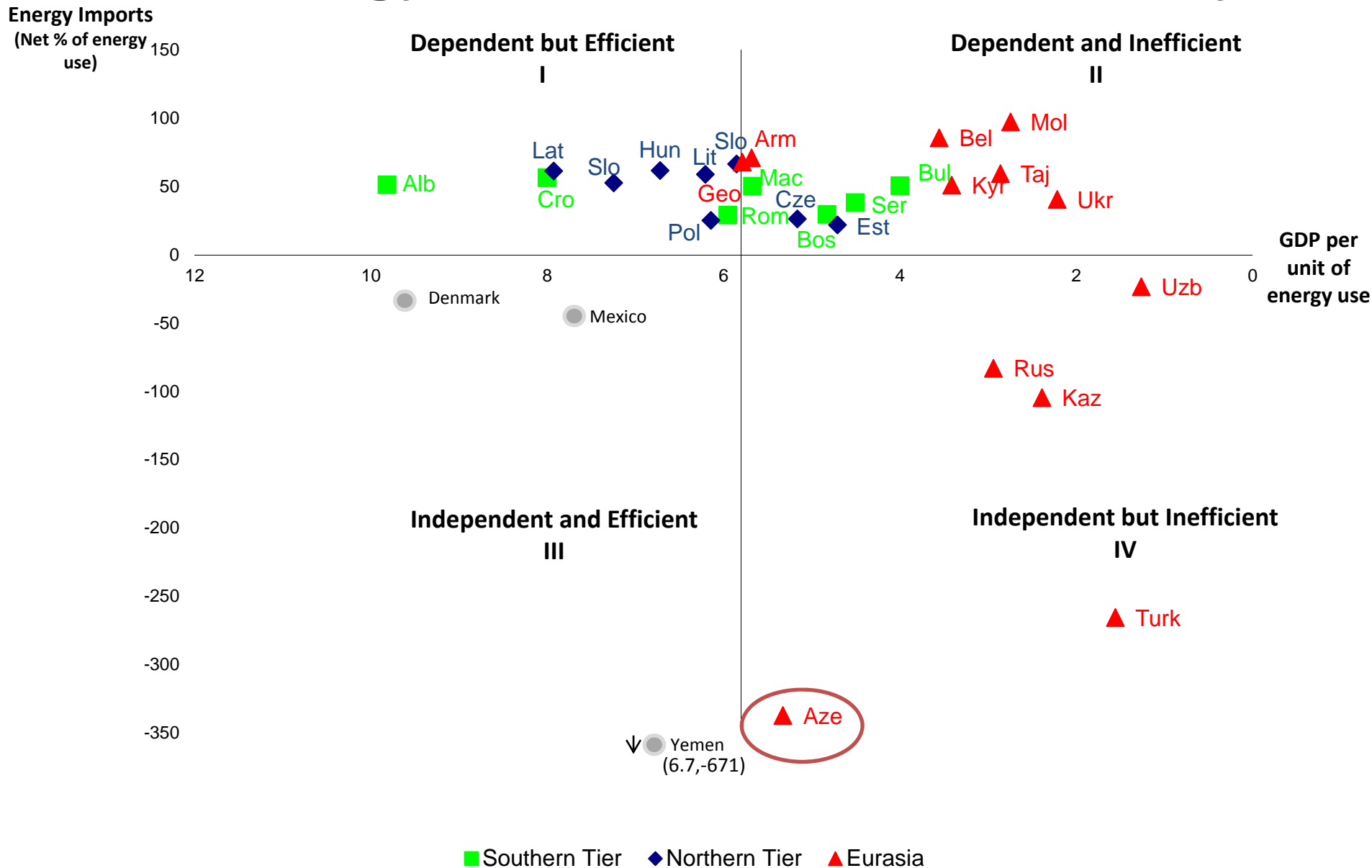


Figure 28

# Energy Efficiency Over Time

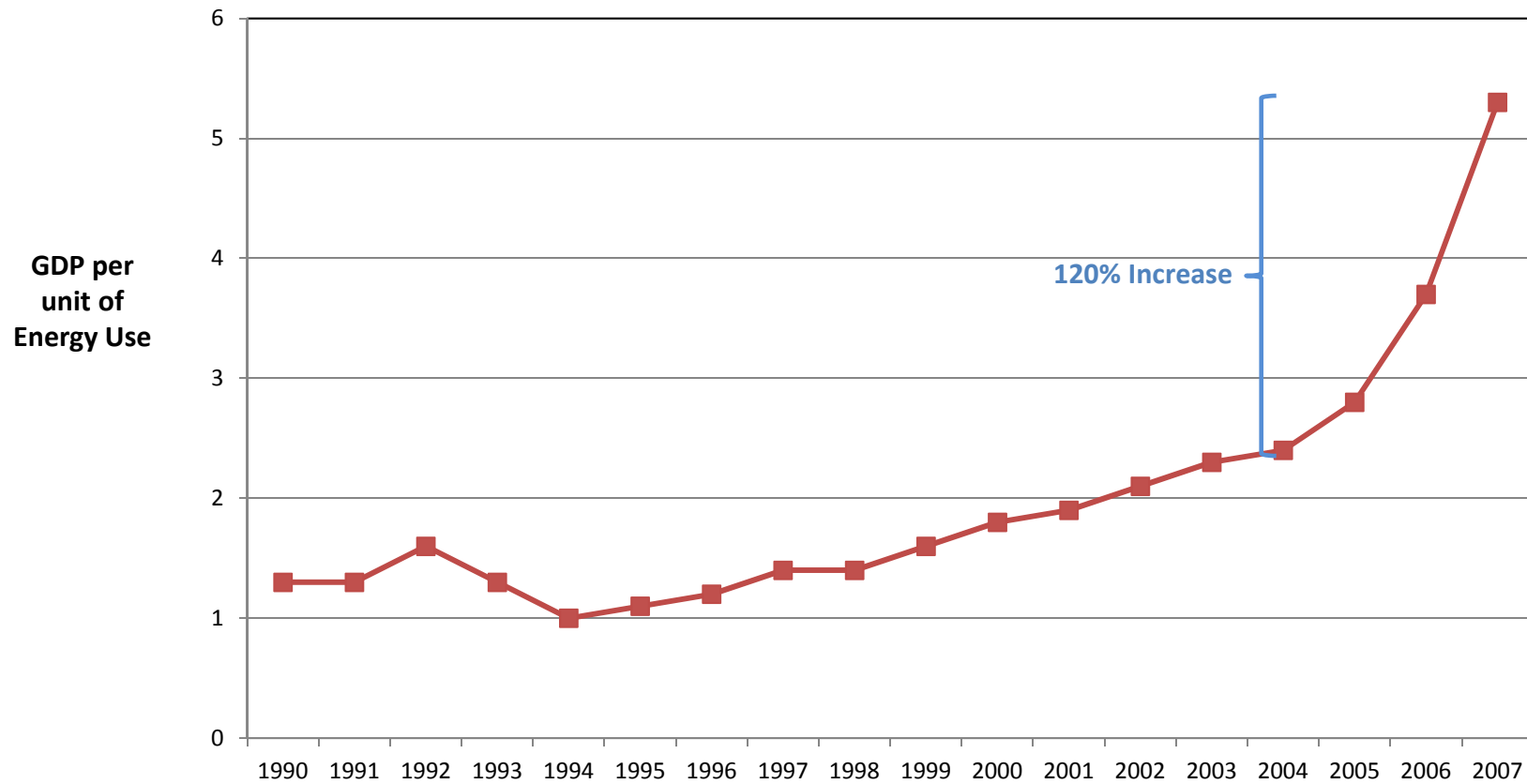


Figure 29

# Communication Technology in Azerbaijan

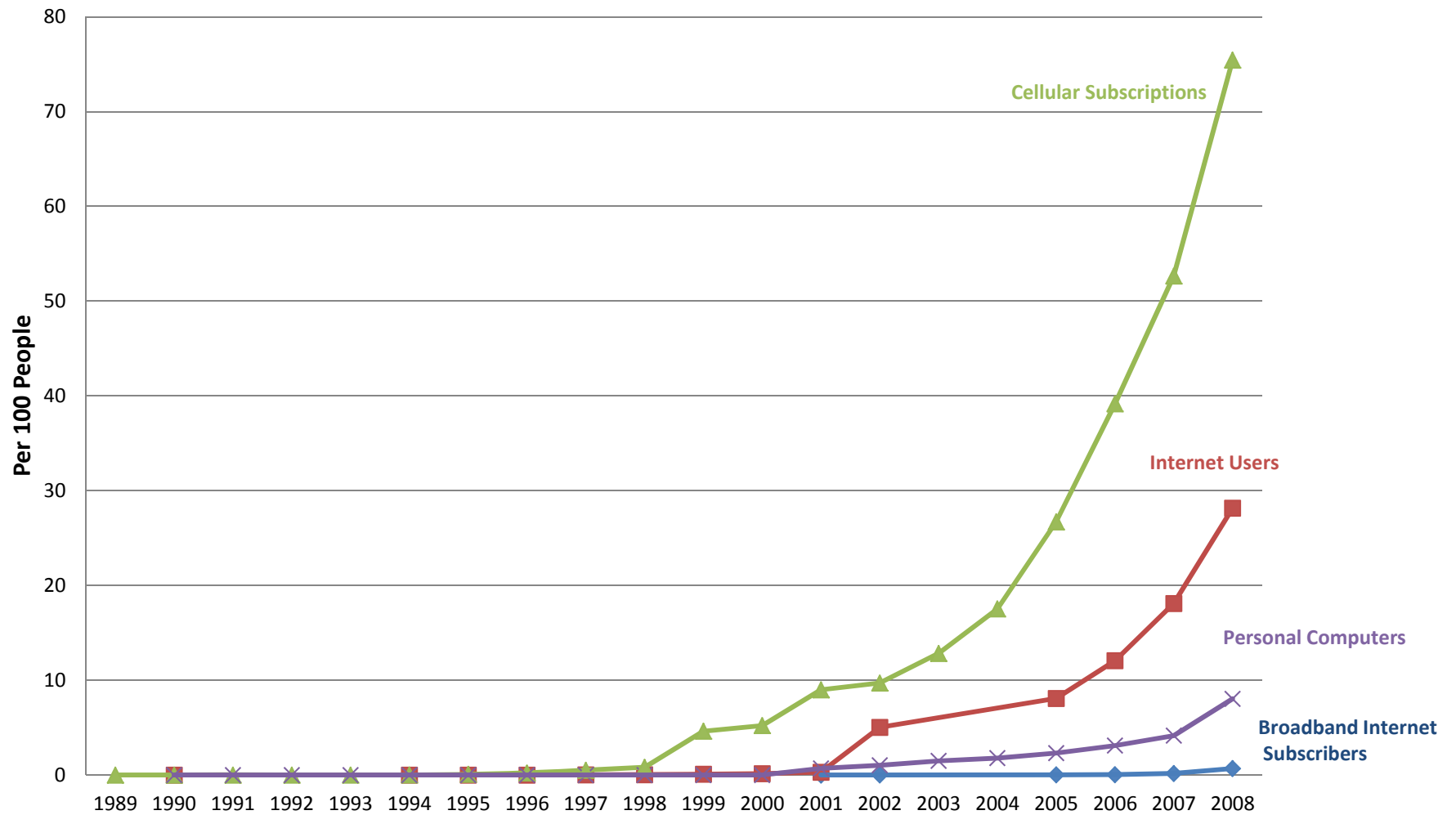


Figure 30

# Internet Users

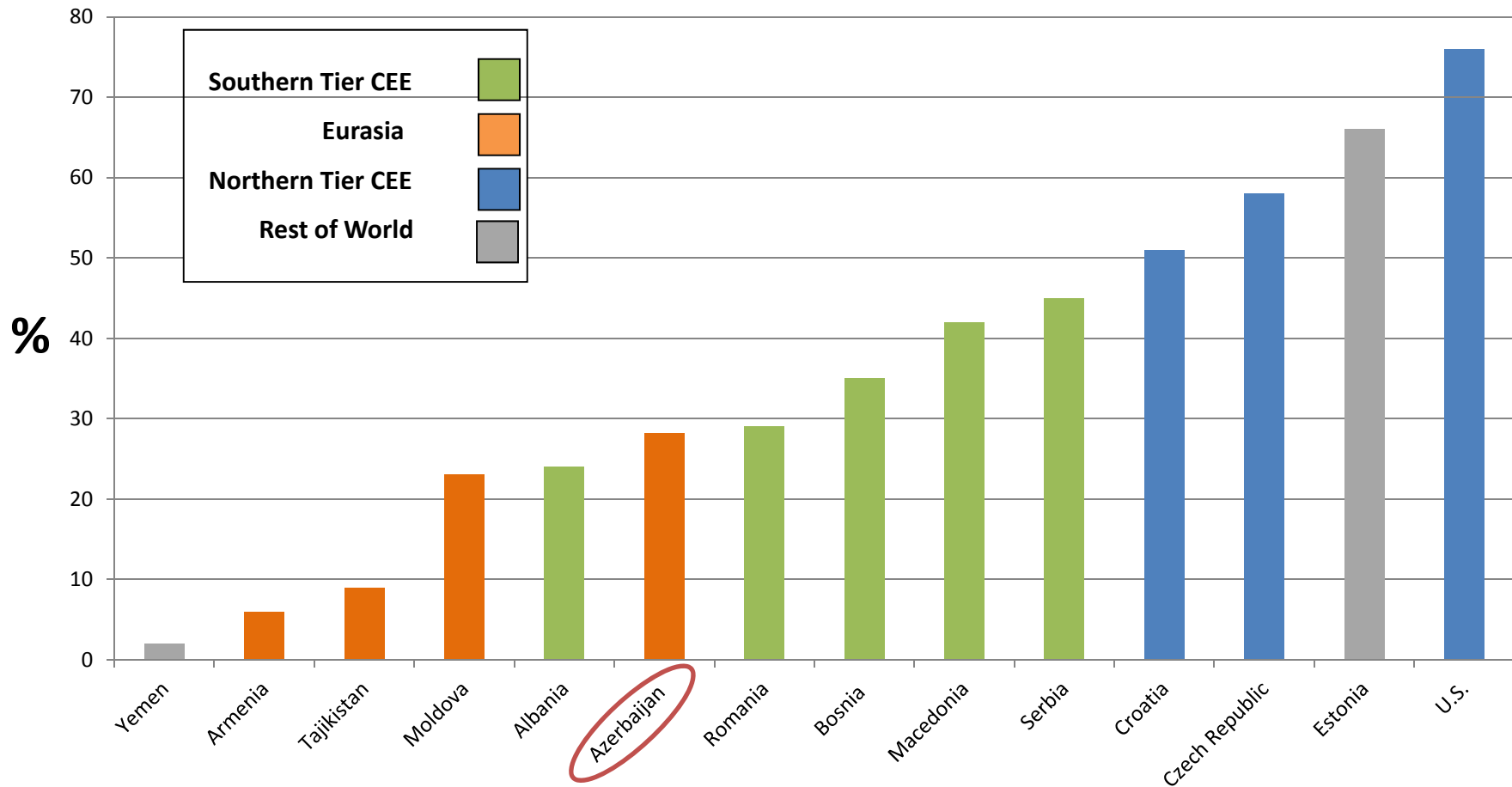
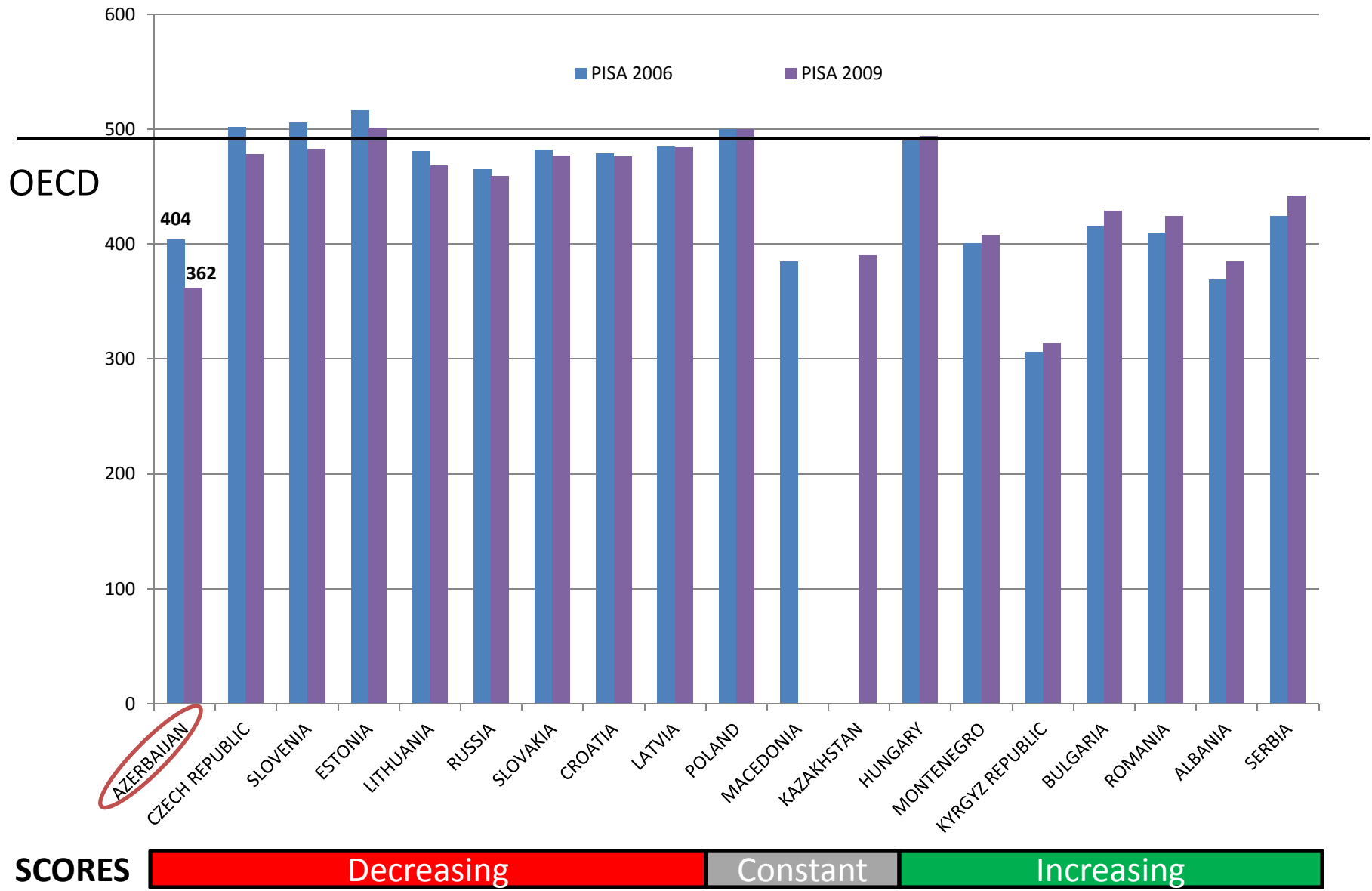


Figure 31

# Functional Literacy PISA 2006 vs PISA 2009



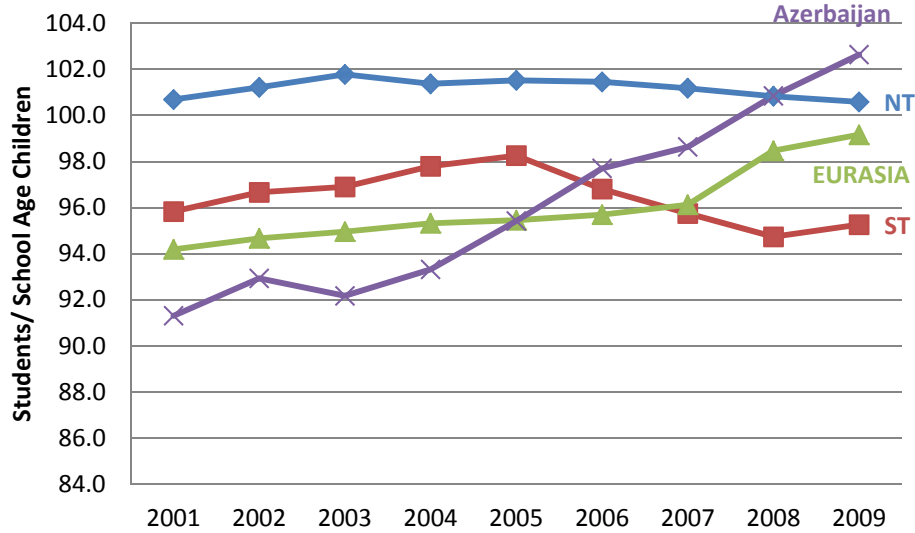
Organization for Economic Cooperation and Development (OECD), *First Results from PISA 2006* (2007) and *Pisa 2009* (2010).



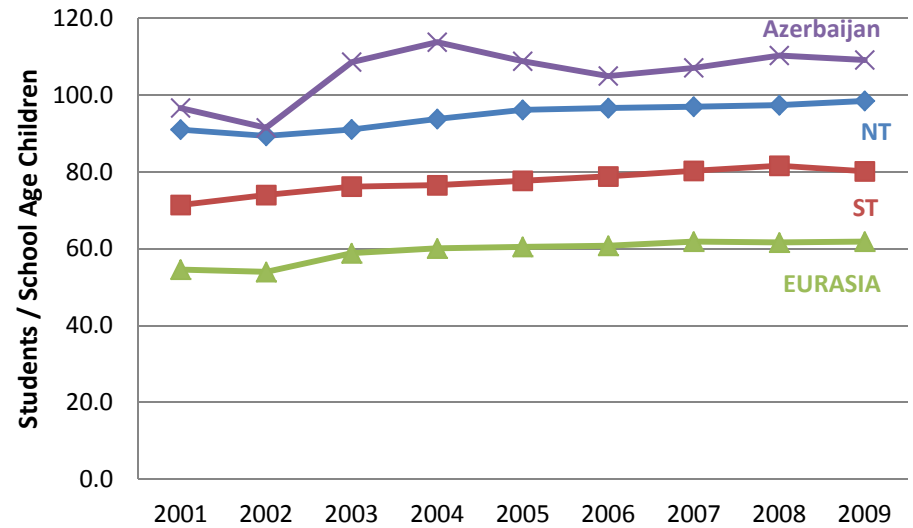
Figure 32

# Education Overview

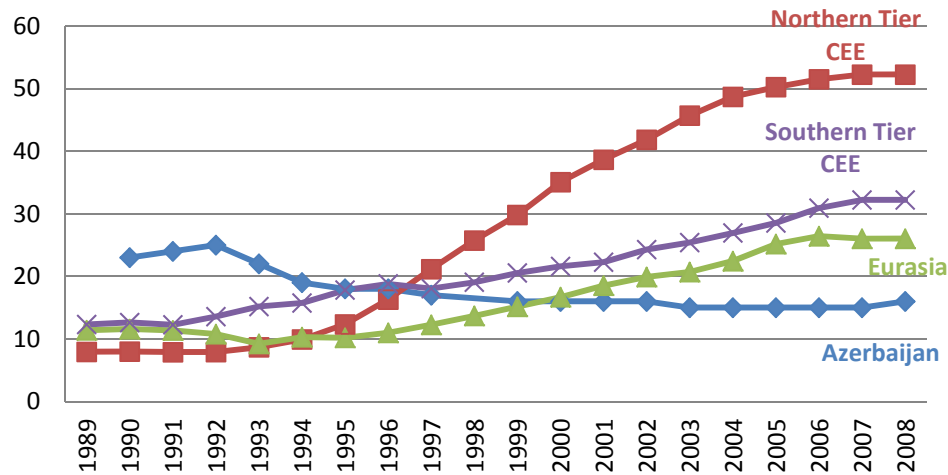
## Primary Enrollment Ratio



## Upper Secondary Enrollment Ratio



## Tertiary Enrollment



## Student Teacher Ratio

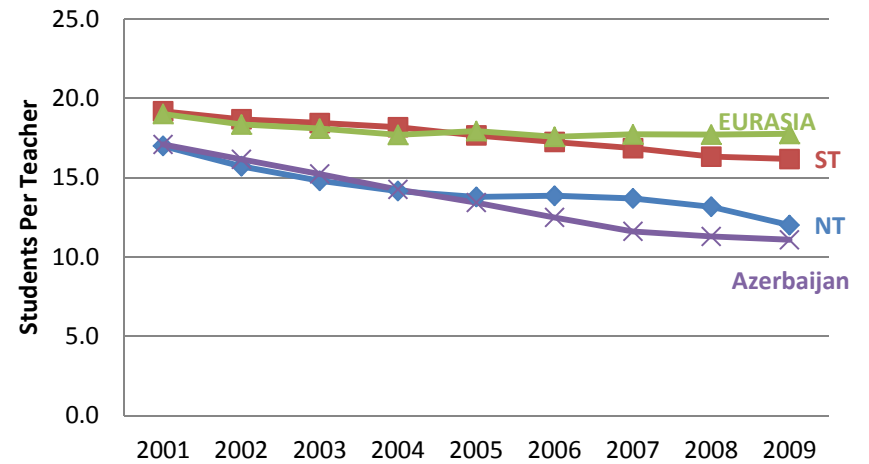


Figure 33

# Life Expectancy at Birth

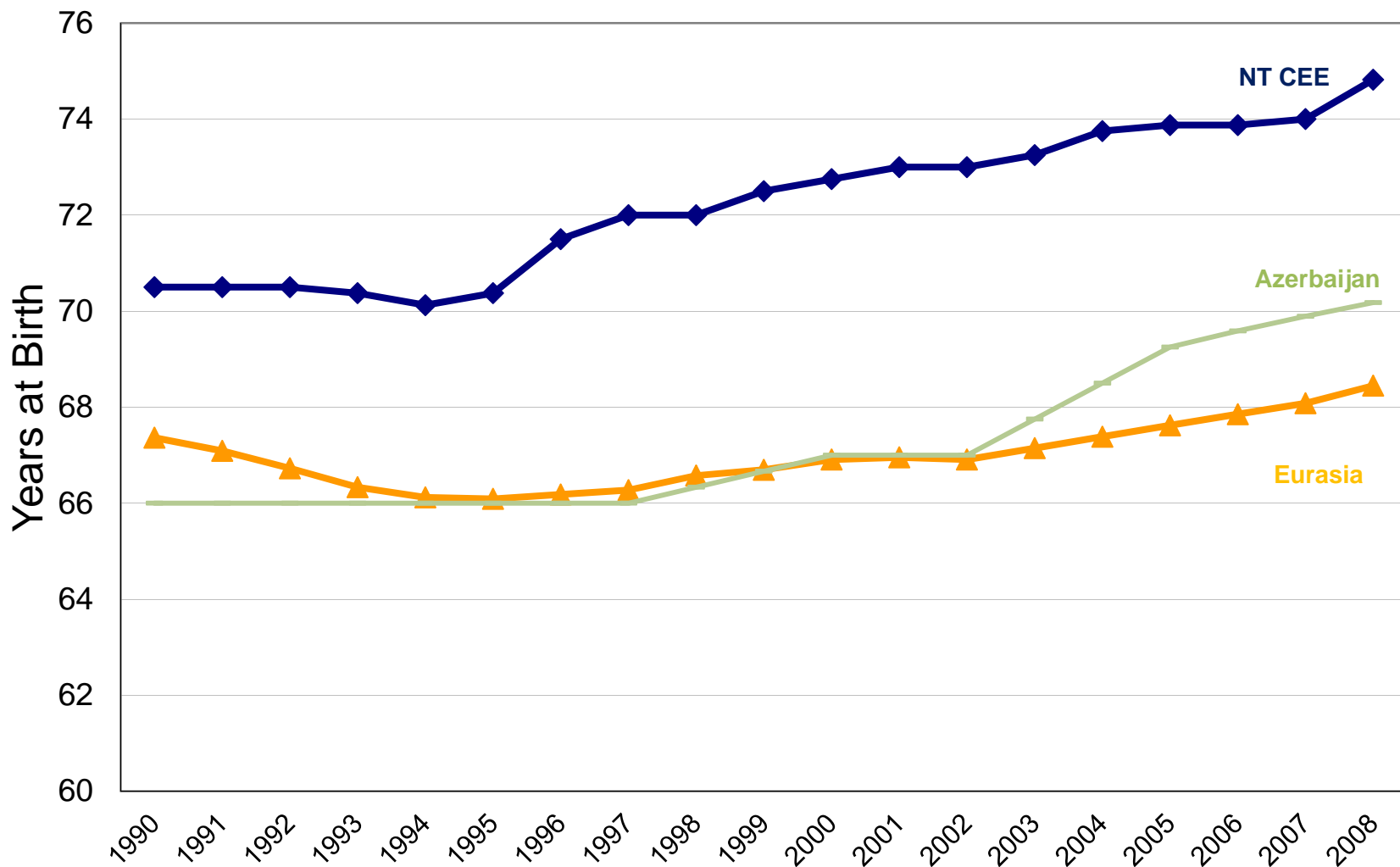


Figure 34

# Tuberculosis Incidence 2008

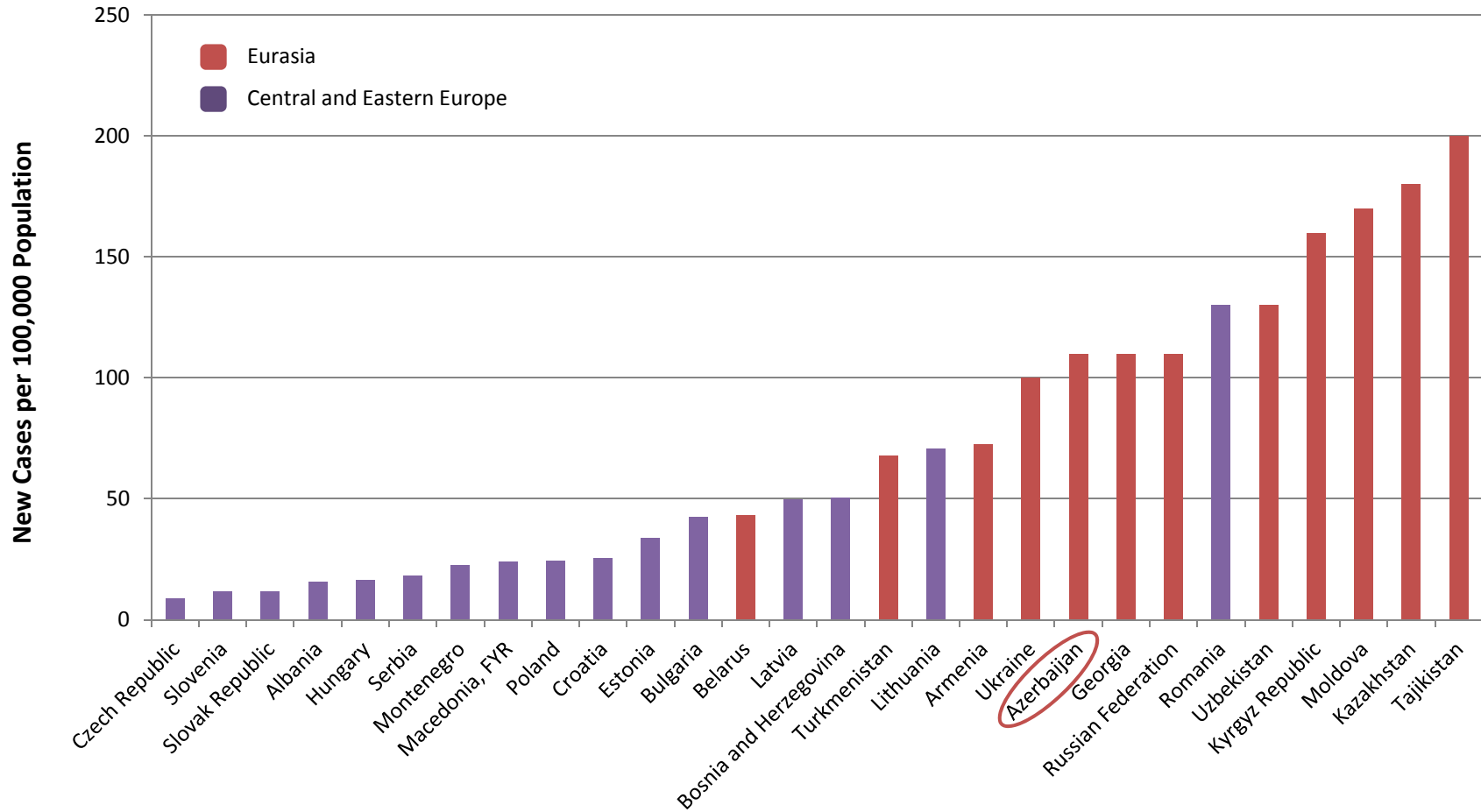


Figure 35

# Tuberculosis Incidence

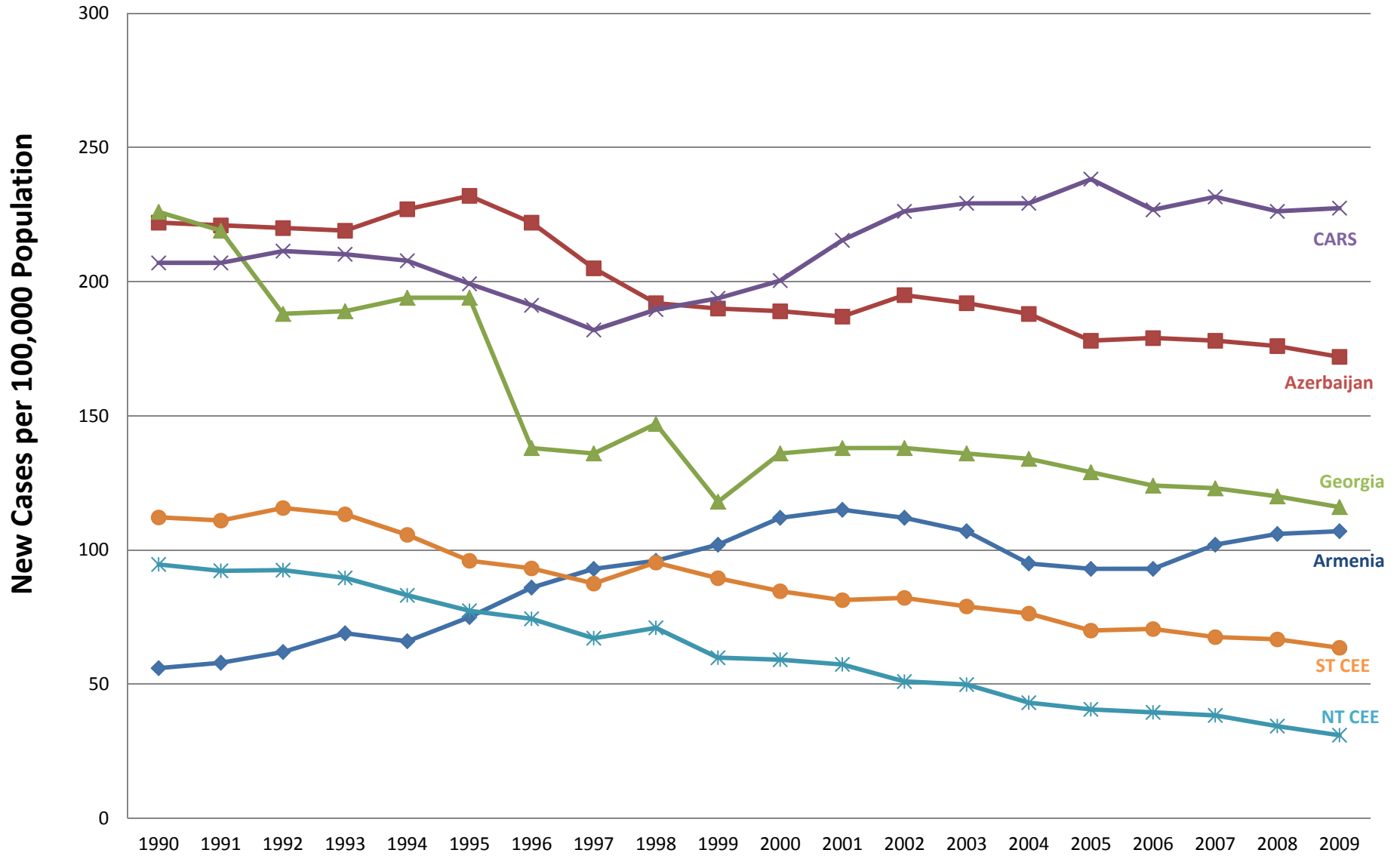
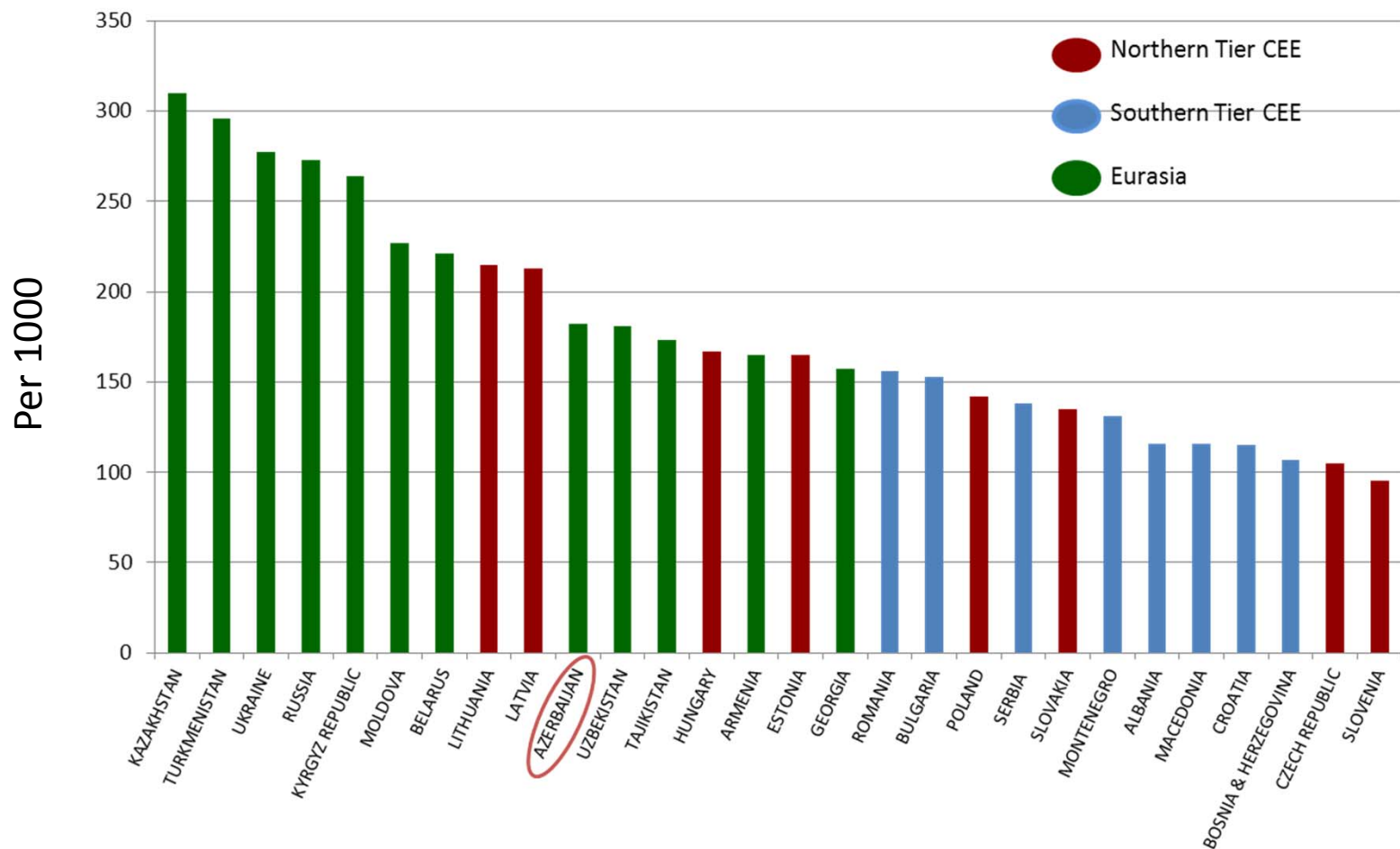


Figure 36

## Adult Mortality Rate - Eastern Europe and Eurasia, 2008



AMR is chance of dying between the ages of 15-60 per 1000 population. Source: WHO World Health Statistics, 2010.

Figure 37

# Poverty Rate vs. GDP Growth in Azerbaijan

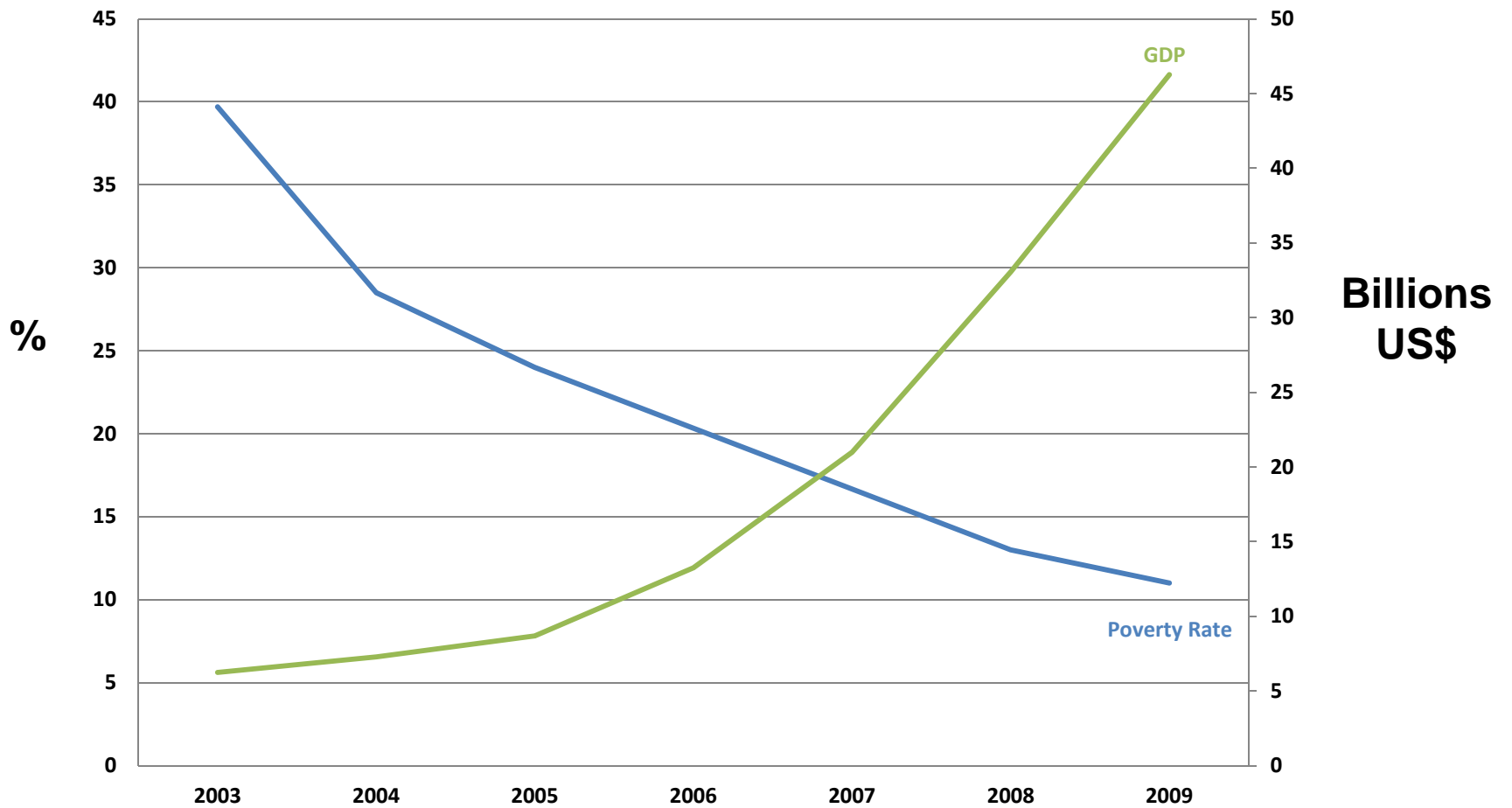


Figure 38

# Peace and Security Score

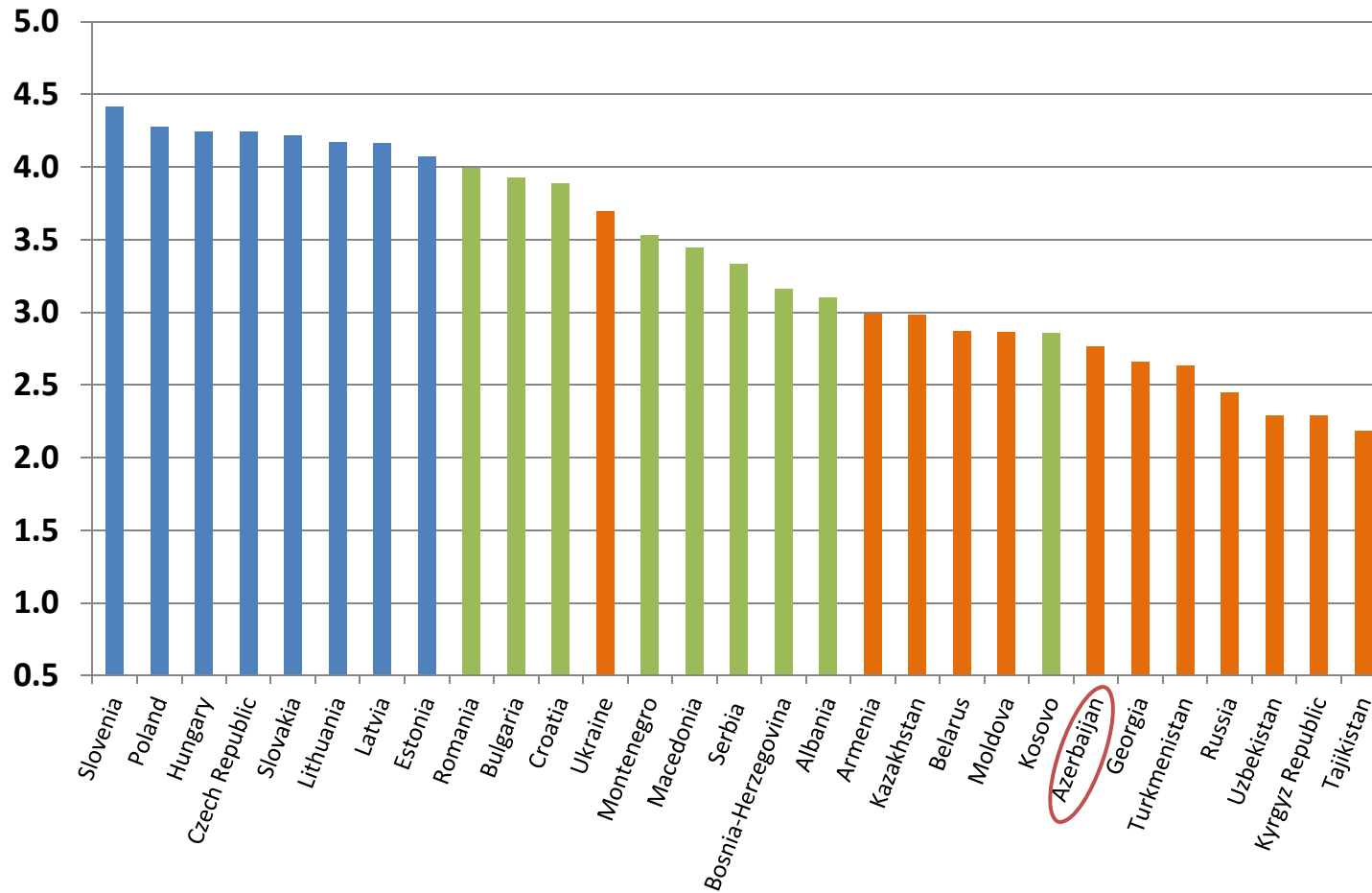


Figure 39

# Peace and Security in Azerbaijan

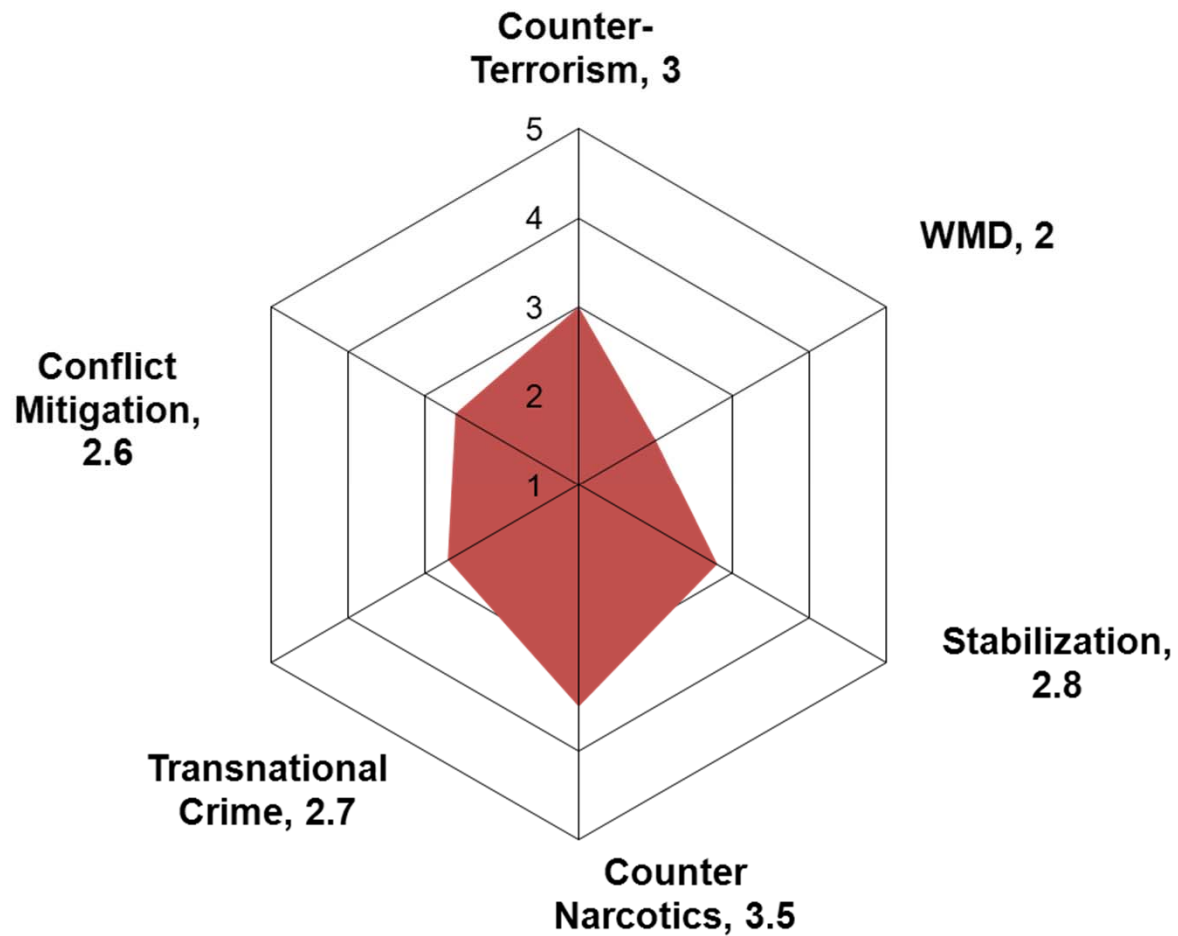




Figure 40

# Peace and Security in Azerbaijan

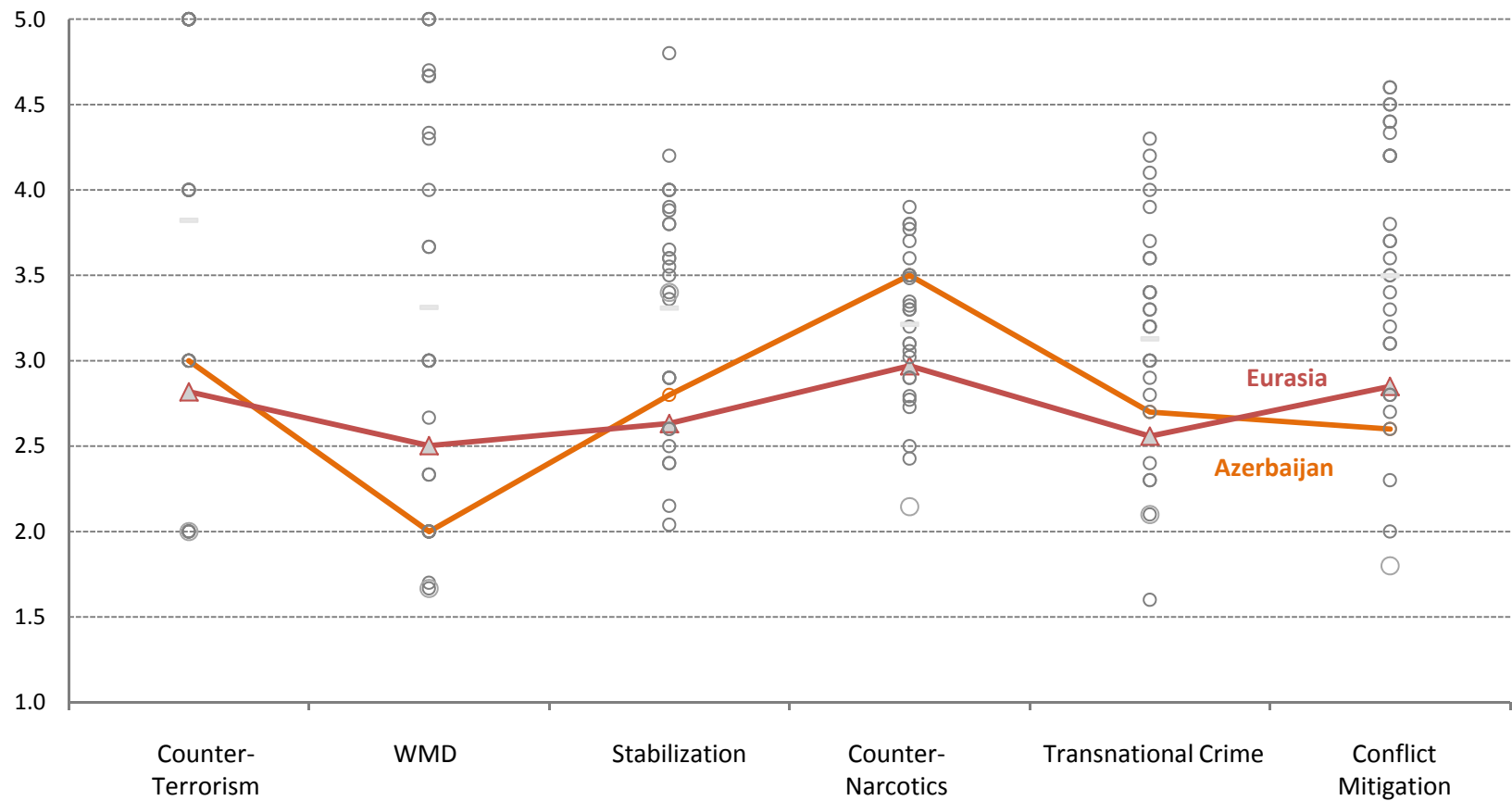
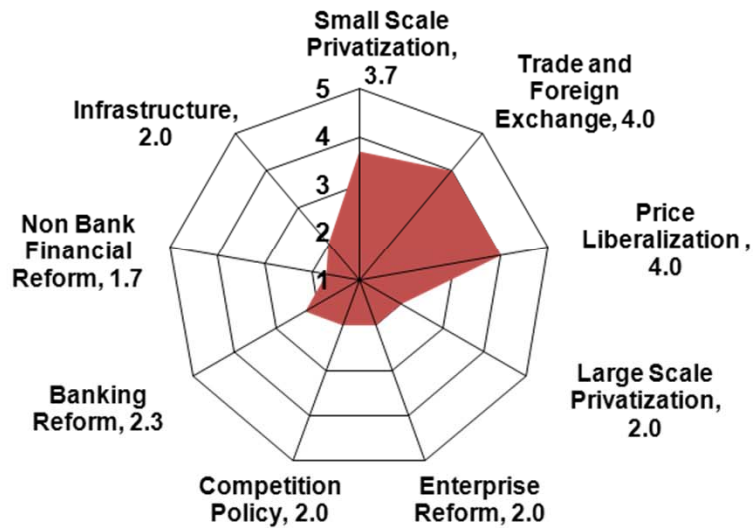
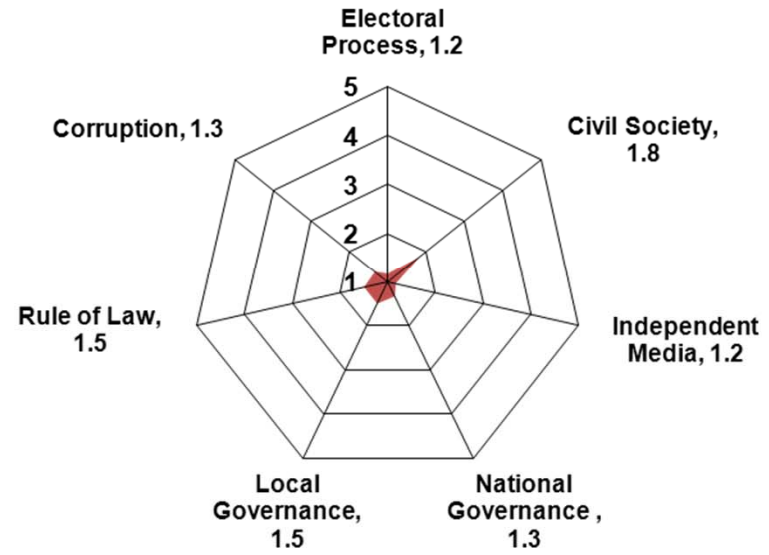


Figure 41:  
Azerbaijan

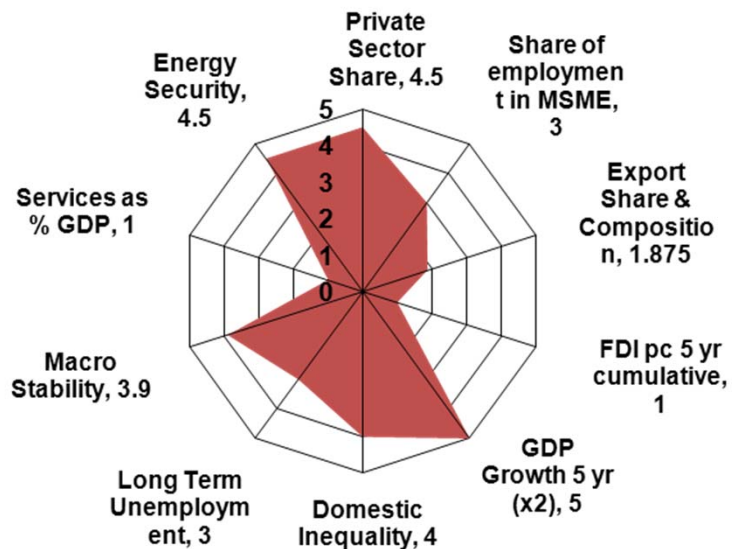
Economic Reforms in 2010



Democratic Reforms in 2009



Economic Performance in 2008-2010



Human Capital in 2008-2010

