THESIS WORK

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Comparative Analysis of Oil Policies in Venezuela and Azerbaijan

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Abstract

Purpose

The purpose of this research is to explore the reasons standing behind the current crisis in Venezuela and Azerbaijan, identify the similarities in economic environments in both countries, and define the possible common solutions that may be helpful to rescue them from the default.

Methodology

The main similarities of these two countries were determined by conducting descriptive researches based on existing works. Data collection was carried out by dividing the story line of the topic into 3 main periods. These periods explore pre-crisis, crisis circles, and after crisis – future perspectives. Furthermore, the post oil crisis policies of Venezuela and Azerbaijan and their relevance is also demonstrated.

Findings

Findings of this research confirm that overdependence on natural resource extraction can be beneficial in short run in order to develop the financial and economic infrastructure. However, when countries rely on the export of the natural resource too much, they end up with the export crisis when the prices go down, or the demand to that particular resource decreases. Based on the experience of Venezuela and Azerbaijan, it is suggested that countries involved in Dutch syndrome should decrease their dependence on natural resource.

Limitations

In particular topics it was hard to find reliable data and conducted research. In some particular cases, the information was available only in local news agencies that were pro-government.

Implications/Contributions

This research can be suggested to the economists who are working on the latest records of “Dutch disease” and its extreme effects on countries, and the ways of fight against it in particular countries.
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Chapter 1. Introduction.

This chapter describes the overall introduction of my master thesis. I discuss in this chapter the background information for the research, topic motivation, present the research question, objectives and importance of this topic. Moreover, methodology is also briefly introduced for the readers. At the end of this chapter there is a literature review that gives the information about the scholars that conducted the researches on related topics.

1.1. Background information

Most of the oil producing countries, starting with the USA and Russia, are experiencing downward shift in profits these days. In the middle of January 2016 the OPEC oil basket price went down to USD 26.5 per barrel that lead to the sharp decrease in world oil prices. No one was happy with the current situation, as the most of the oil producing countries became involved in export crisis and either their debts increased, or they had to use their accumulated savings. As a result, most of these countries decided to freeze their current oil projects as in some cases even the production costs exceeded the market price. The biggest cartel of the oil producing countries – OPEC has been conducting several meetings by the request of the members (mainly by Venezuela that suffered the most) in order to avoid economic turmoil caused by the overproduction of oil that many of the producing countries are experiencing.

The mentioned decrease in oil prices one more time demonstrated that the using natural resources as the main driving power of a country’s economy is good idea only in short run. This policy should be implemented as a “springboard” effect for the economy that can push the country forward, reduce the poverty, give a chance to implement social projects to increase the social welfare and raise the competitiveness. In other words, those countries that did not use the chance to use the benefits from the export of the crude oil in developing the non-oil and service sector, transmitting from the export of primary products to the export of secondary goods are now staying face to face with economic trouble that is needed to be solved in a short term.

However, it also should be mentioned that, especially in the poor countries abundant with natural resources it is always challenging to use the gained money
from resource export in a most sustainable way. What I mean by sustainability is social programs and policies that focus to diminish the poverty, and lessen dependency on resource exports. Hence, it is important to find the “golden balance” in money spending. Unfortunately, the mentioned countries struggle to do that due to the several reasons, such as lack of economic experience, weak infrastructure, high level of bureaucracy and corruption, etc. That is why, these countries sometimes find themselves inside of the “Dutch syndrome” that may lead to the different economic and political problems inside of the country, even end up with the public demonstrations.

The countries whose cases I will research are currently inside of the sharp economic crisis due to the dropping oil prices in world market. Both Venezuela and Azerbaijan struggles to set up the governmental budget based on the new oil prices and both of them still keep the hope that once fastest growth period will come back. Especially being an OPEC member, Venezuela periodically requires the other OPEC countries to freeze or decrease the production in order to increase the demand for oil. Venezuelan president Nicolas Madura even visited other oil producing countries that are not members of the OPEC, in order to persuade them also stop the oil projects. However, these affords are only enough to keep the low prices in a short run, not letting them decrease any more. Azerbaijan President made a joke in Davos Economic Forum, saying that “every time when OPEC members meet, the oil prices get lower, and we are now afraid of the next meeting”. Both countries understand that serious steps are needed to be taken and discover the policies that may be implemented in order to rescue from the crisis. Hence, this thesis explores these taken and possible steps of both Venezuela and Azerbaijan in comparison to each other.

1.2. Topic motivation

There are several factors that motivated me to research this topic. The main factor was the similarities in a way that both countries’ economic activities are conducted. Both Venezuela and Azerbaijan concentrated their economies on oil exports over the last decades. However, it should be mentioned, that in comparison to Azerbaijan Venezuela is considered to be the one of the major oil exporters with more oil reserves than Saudi Arabia. Today Venezuela relies on oil for 95% of its
state revenue, and imports almost everything it consumes, while Azerbaijan is in the list of the 5 most vulnerable countries in the world that can be hit by the current export crisis, simply because the fiscal breakeven oil price per barrel for Azerbaijan is almost three times more than the current market price.¹ In Venezuela the decreasing oil prices are resulted with a strikes in the country. At the same time in Azerbaijan the currency reserves dropped dramatically and the national currency devaluated for almost 100% due to the weak banking sector and difficult business environment this number is expected to grow even further.

All the mentioned factors one more time demonstrate the negative historical and current similarities of both countries. My main motivation is to research these similarities, find out what has been done wrong in past, and “learn on the mistakes”. In our case, as Venezuela is the country that is in worse situation that Azerbaijan, it would be beneficial to study research topic in order to give concrete suggestions for both countries that can help them to survive from the crisis.

1.3. Objectives

The aim of this research to identify the possible solutions that can be used in both Venezuela and Azerbaijan. As mentioned before, the relevance of this topic comes from the similarities in economic downturn that both countries are experiencing. To summarize, these similarities may be concluded as following: significant income and welfare increase and poverty reduction due to the oil money, once fastest growing economies of the region, resource curse and/or the “Dutch syndrome”, chronically mismanaged oil revenues, inflation, recession.

The main objective of this research is to provide an overview of Venezuela and Azerbaijan’s oil strategy with policy discussion on achievements and challenges ahead. In my thesis I intend to research the common ways of economic development that can be applied for both countries. By assessing the current situation in oil revenue management in both countries I will try to identify the key problems, research the alternative methods that economists are suggesting for this particular situation and find out the solutions that may lead to the development. Main analyses will be carried out in macroeconomic environment, fiscal rules and

legal bases for the management of the oil revenues. Moreover, in order to fully describe the picture of the current situation, comparative analysis will be demonstrated not only between these two countries, but also each country’s oil policy will be compared to one of the other counties from the same region, or integration unit with Venezuela and Azerbaijan. Venezuela will be compared with other OPEC members, while for Azerbaijan the main comparative countries will be Kazakhstan and Russia.

Several researches and investigations were conducted by the local scientists, and economists in order to suggest the economic roadmap for Venezuela and Azerbaijan. However, this research intends to explore some of them, and bring a new suggestion of the economic policy in a way that will be relevant to be used both in these states. In order to reach to this point, I will take into account several factors that are common for the both countries. I will also describe the previous policy implications by headlining their positive outcomes and disadvantages.

Moreover, the thesis will investigate the common tendencies for both of the countries and find out what kind of mutual, bilateral agreements may be signed in order to develop the international relationship between Venezuela and Azerbaijan in a way, that both of them benefit from it.

1.4. Research question

My main question of the research is: “what are the common policies that possible to implement in order to “save” both Venezuela and Azerbaijan from the export crisis caused by the dropping oil prices”? My preliminary hypothesis is: “in order to achieve a sustainable growth in long run both Venezuela and Azerbaijan must decrease the dependency of the economy on oil prices”. During the research I will test this hypothesis.

Although these two countries might not be considered similar countries due to the differences in economic geography, resources, economic activities and the scale of the downturn, and they almost have no international relationship, except a joint statement that was signed in October 2016, all these several similar factors mentioned above related to both countries lead to the fact that both Venezuela and Azerbaijan are in need of finding an economic solution for the oil export crisis. It should be mentioned that the sharp decrease in oil prices is slowed down nowadays.
However, the countries should not take this as granted and must use this opportunity to adjust the economy into the new rules.

1.5. **Methodology.**

I explore the main similarity of these countries that are suffering from the economic crisis, by conducting descriptive researches based on the existing papers and articles of different economists and scholars whose main research areas have been Venezuela and Azerbaijan. In order to present the relevance of these works I review and collect different data from the reliable resources, such as OECD, World Bank, UNCTAD, Central Banks and Statistical Committees of both countries. Data is presented by tables and graphs, and explained.

Mainly, data collection is divided into three different periods. The first period is the beginning of 1990s and mid-2000s. The reason why I start from the 1990s is that, for both countries this period was painful from the economic and socio-political point of view. For Venezuela this period is considered as a shock therapy from the economic malaise of 1980s, while in Azerbaijan that was the first years of independence from the Soviet Union, years of economic ruins, and war with Armenia. The second time period starts from mid-2000s and continue till 2015. This period is characterized for the both countries as years of oil boom and oil money inflow that brought economic progress, social development and success in fight against poverty. The third period is the current crisis period that started from 2015 with the decrease in oil prices. In this period both countries experienced the economic downturn and found themselves inside of the “Dutch syndrome” and resource curse. I explain the effects of this resource curse for the researched countries demonstrating it with collected data.

The story line of the thesis is also divided into three parts. In first part I preview the historical tendencies in both Venezuela and Azerbaijan in order to show “how it all has started”. This part describes the policies that the countries implemented in the beginning of the oil boom analyzing how successful these policies were. The second part describes the crisis period. Here I explain how both countries became involved in “Dutch syndrome” and what were the main reasons hiding behind this situation. By demonstrating the data of pre-crisis and crisis period in a comparison, I give the picture of the damage that was done to the
In the third part of the thesis I explore the policies that Venezuela and Azerbaijan has accepted so far in order to fight the crisis, analyze them and detect the weaknesses that can be developed. Moreover, I bring the suggestions that can be implemented and find the common possible ways of rescuing from the crisis and conducting negotiations between each other.

Moreover, in this research the post oil crisis policies of Venezuela and Azerbaijan is also demonstrated. On the following chapters I answer the question of my research topic and try to give possible solutions that can be helpful in fighting the crisis.

1.6. Literature review

The oil policies of different countries, their successful implementation, Dutch syndrome created by overdependence on natural resource extraction, economic dependency on oil prices and other related topics have several times been researched by different economists and scholars. In this sense, Venezuela and Azerbaijan has been attractive case to examine and a lot of researchers have worked on these topics. However, the comparative analysis of these two countries that are experiencing an economic downturn resulted with the drops in oil prices, have never been researched in an interaction with each other.

Economists have different arguments about the possible positive and negative outcomes of the declining oil prices. Some of them are worried that the low energy prices will push the economy into a tailspin. They explain it with the fact that, the decrease in incomes in the oil rich countries can result in decline in the different sector of economy. For instance, Apple Inc. announced that their sales declined significantly in most of the oil producing countries. Many of the oil exporters have to cut spending significantly, and this will have an impact on the economic growth.

On the other hand, some other economists are not worried at all, and consider the price declines as an opportunity for a more sustainable growth. They headline that, drop in oil prices brought by rising supply (like the current one), should boost the global growth by up to 0.4% points\(^2\). The authors explain it with

the fact that, in oil exporting countries the spending will increase, that will exceed the decline in expenditure by oil exporters.

Some economists reveal the two main aspects of declining oil prices. One aspect is about the drivers of the decline. They think that decreasing oil prices may give a shock driving effect to other causes that drive the global economy. The second aspect is about the persistence of oil prices decline, which emphasizes that the effects of this decline depends whether the lower oil prices will be temporary or permanent. If temporary, people will tend to save the real income gains. If permanent, people will have to adjust their saving patterns to the current economic situation.

There have been several researches conducted individually for both countries to investigate their economic environments. In this sense, Venezuela’s case was much more attractive mainly because of a much longer oil policy history. Azerbaijan became popular for the scientific investigations after the collapse of the Soviet Union and the “Contract of the Century” signed in 1994 that accelerated the development of offshore oil and gas fields in the country.

The presence of oil was known in Venezuela even before the Discovery of Americas in 1492; back then, Indians were aware of the existence of hydrocarbons that appear on the surface of their lands. After the first gusher was discovered along Lake Maracaibo in 1922, oil became the major dominant factor in the country’s economy. Venezuela as one of the world’s leading oil exporters experienced a complex story of petroleum-induced economic boom in the 1930s and 1970s and economic crisis in the 1980s. In the 1960’s Venezuela started the nationalization of the oil industry by implementing “no more concessions” policy. By 1970 the country was one of the twenty wealthiest countries in the world - GDP per capita was almost the same with the United Kingdom.

After Hugo Chavez officially took the power in the country in 1999 the entire oil sector of Venezuela was damaged by the policies due to the lack of

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investment and cash, and corruption\(^7\). The policies that Chavez brought resulted with overspending\(^8\) and as a result the inflation rate of Venezuela hit the highest rates in the world\(^9\).

Generally, crude oil production in Venezuela averaged 2425.99 BBL/D/1K (barrels per day), reaching an all-time-high of 3453 BBL/D/1K in 1997 and the lowest 594 BBL/D/1K in 2003\(^10\).

**Table 1. Venezuela crude oil production (1994-2017)**

![Graph of Venezuela crude oil production (1994-2017)](image)

Source: *Organization of the Petroleum Exporting countries (OPEC)*

However, during the last years there were some negative trends that contrasted with the high oil prices and immense resource endowment of Venezuela. The first and the most important trend has been the drop of production\(^11\). This drop occurred while reserves increased with the incorporation of resources and dramatically increasing oil prices.

Today the country’s financial system is one of the smallest and least developed in the world. Bank credit to the private sector amounts to just around 9% of GDP, ranking the country 132\(^{nd}\) of the 157 countries that have available data for the 2000s.\(^12\) Social problems are being escalated each day because of the economic

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crack-ups. According to Bloomberg, “Venezuela has one of South America’s highest rates of HIV infection”. Currency devaluation hits the prices so intense that some of the lively essential commodities became scare or disappear from the markets. Some newspapers write that people can’t even find toilet paper, calling it as a toilet paper crisis and even a box of condoms is now worth $755.

Researchers indicate several reasons behind this economic crisis in Venezuela. One of the most presumed reasons is the independent and unauthorized policy of the State Oil Company – Petroleos de Venezuela (PDVSA) and weak control over its activities. By the time Chávez came to power, PDVSA had gained significant autonomy - he called it a “state within a state” - but his government then brought the company back under its authority by changing the constitution and the hydrocarbons law. Becoming a political actor, PDV transformed the traditional national oil policy, which concentrated on fiscal revenues, into a new and essentially sectorial oil policy that concentrated on the development of the oil industry. To put it differently, the policy issue was no longer prices, but volumes.

Edgardo Lander indicates the several reasons of the crisis. He headlines the historical over-valuation of the currency and the so-called “Dutch disease” as the serious problems that confront the economy. According to him, “apart from oil, practically everything is cheaper to import than to produce in Venezuela”, hence the efforts of promoting the domestic production is being undermined. As a result, bureaucratic mechanisms that had to control the use of the foreign exchange, had problems with the scarcity in imports and massive corruption. According to Edmee Betancourt, President of the Venezuelan Central Bank at the time, of the total of US$59 billion in subsidized foreign exchange allocated in 2012, some US$20 billion went to “shell companies” – an “artificial demand” unrelated to productive activities. According to the IMF estimations, the inflation rate for this year is expected to be 475%. There are also several scientific papers, researchers and news agencies that are keeping the situation.

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When it comes to Azerbaijan, it should be mentioned that, the country is one of the oldest oil producers in the world. The first oil well in the world was built in Azerbaijan in 1847: 11 years earlier that it was done in Pennsylvania, United States. Under the Soviet Union the economy was centrally planned. After getting independence the main idea was to transform to the market economy by privatization and liberalization. However, privatization could not be started because of political instability and ongoing war with Armenia. In Azerbaijan, unavailability of alternative resources and low level of political contestation induced the state leaders to choose full state ownership over their energy reserves and to invite foreign investors to develop them in 1994. Later, in that year a “Contract of the Century” was signed with the several Western oil companies such as BP, Statoil, etc. Initially, the State Oil Company of Azerbaijan (SOCAR) had 20% of the shares, however, they were obliged to cede 10% of it to other companies due to the lack of the resources to finance the program participation.

In November 1997, Azerbaijan began producing oil under the agreement on the “Joint Development and Production Sharing for the Azeri and Chirag fields and the deep water portion of the Gunashli field in the Azerbaijan sector of the Caspian sea”.

Between 2001 and 2009, Azerbaijan was able to develop its oil and gas sector. Strong oil and gas production gains, high international oil prices and sharply higher public spending propelled growth to an average of 27% a year between 2003 and 2009.


Table 2. Azerbaijan crude oil production (1994-2017)

Source: Organization of the Petroleum Exporting countries

One interesting fact is that, the year when Venezuela’s oil production hit the maximum number (1997) Azerbaijan’s oil production was in the lowest rate. On the other hand, in 2003 Azerbaijan’s production was the highest one among all these years, while Venezuela decreased the oil production to the minimum. Even though the mentioned numbers are different, this factor can be considered as one of the relatedness of these two countries to each other in a global scale.

Azerbaijan nowadays is strongly dependent on oil. Almost 93 percent of total exports of the country was composed of oil and oil products while 73 percent of its state budget was made of oil revenues in 2012.\textsuperscript{21} That was the year after which the government decided to accept a program “Vision 2020” in order to decrease the dependence from on oil revenues. As a result, in 2015, the oil sector generated 31% of the country’s GDP (compared with 52% in 2011), and oil revenues accounted for 63% of the state budget and amounted to 86% of total exports.\textsuperscript{22} In Azerbaijan, the bulk of the state’s share of oil revenue is accumulated in the state oil fund SOFAZ. Of about US$108 billion windfall revenue over the last 10 years, the government spent US$70 billion from the oil fund or nearly 65% of its overall assets.\textsuperscript{23} The author also headlines that the attempts of Azerbaijan to diversify its economy was unremarkable, mainly because of the state elites who freely used the

\textsuperscript{21} Ibadoglu, Gubad, et al. 2013
\textsuperscript{22} Ahmadov, Ingilab. 2016. “Azerbaijan’s New Macroeconomic Reality: How to Adapt to Low Oil Prices”. Caucasus Analytical Digest 83: 2-5.
\textsuperscript{23} Guliyev, Farid. 2015. “After Us, the Deluge”: Oil Windfalls, State Elites and the Elusive Quest for Economic Diversification in Azerbaijan”. Caucasus Analytical Digest 69: 2-5.
oil revenues to finance different government projects “undertaken under the banner of diversification to capture rents on a larger scale”.

Fakhri Hasanov, who observed the elements of the “Dutch disease” in Azerbaijan, headlines that “one can observe that in the Azerbaijani economy the real effective exchange rate has appreciated substantially since 2004. It can be considered as an evidence of the Dutch Disease” 24. In country the non-oil tradable sector improves more slowly than the service sector and this can be considered as a main symptom of the “Dutch disease”.

The final consequence of the decreasing oil prices for the Azerbaijani economy was the sharp currency devaluation against dollar. In comparison to the other oil-rich Caspian Basin countries, such as Russia and Kazakhstan that started to weaken their currencies from 2014, Azerbaijan tried to hold its currency at a firmly stable rate in the hope of a return to favorable oil prices. Another peculiarity in this case is that both times that Azerbaijan devalued its currency, it did so sharply and not smoothly, which differs from the approach taken by Russia and Kazakhstan. 25 The currency devaluated twice with 100%, after which the Central Bank announced the transmission to the floating exchange rate policy.

All these researches done by different scholars and economic organizations demonstrate the similarities and differences in the economic pathways and oil policies of these countries, and their relatedness to each other. However, it would be beneficial to study the economic cases of Venezuela and Azerbaijan in comparison to each other, in order to find out their weaknesses, and “learn on each other’s mistakes”. Hence, my aim is to fill this gap in economic literature with this research paper.

Chapter 2. Economic and political map of Venezuela

Several features and indicators of Venezuelan economy will be described in this part of the study. The economic activities that led to the crisis will be investigated deeply again. Moreover, I will show the GDP per capita, unemployment and inflation rates of the country in order to give a broader picture of the situation to the reader.

2.1. Current economic and political situation

In the beginning of the XX century the oil was discovered in the country after what the oil became the main export commodity, exceeding coffee and cocoa export. As a result, today Venezuela has market based mixed economy that is based on the petroleum sector. In the first half of the century a big amount of US oil companies were involved in Venezuela, initially interested only in purchasing concessions.26 Venezuela is one of the countries that founded OPEC, however, in a comparison with other OPEC members, the government did not save funds for future economic hardships. Starting from early 2000s rising oil prices helped the country to initiate the policies that boosted the economy and reduced the poverty and economic inequality. Now, there is a huge frustration in the society due to the food and commodity shortages in the markets. The government has installed fingerprint scanners in state-run grocery stores to track purchases and deployed the National Guard to maintain order at supermarkets and pharmacies.27 In 2013, the country devaluated its currency against dollar nearly a third because of this shortages. “The oil party was over”. According to Wall Street Journal, the reason standing behind this shortage of products, such as milk, meat, chicken, coffee, rice, toilet paper and etc., is withholding the dollars from the importers with price control.28

Venezuela has the weakest property rights in the world: 5 on a scale of 100.\textsuperscript{29} The country is keeping more than 60\% of its international reserves in gold. However, after spending the $11 billion obtained from the first gold repatriation in just two years, the government was obliged to add the dollar reserves of state owned companies to those of the national bank in order to reassure the international bond market.\textsuperscript{30} Consequently, the country is suffering the worst economic crisis in its history. The growth rate was -8\%, and the inflation rate was 482\% in 2016 – the worst indicators in the world.

The exploration, production and export of oil in Venezuela is under the control of PDVSA (Petroleos de Venezuela). It is considered as the fifth biggest oil exporter in the world.

The studies that examine the country risk assessment headline that the oil reserves of the country, and geographic proximity of Venezuela to the United States can be considered as strengths. Moreover, the growing of active population of country is also a strong reason to conduct business here. However, the economy is strongly dependent on oil and loans from China, and there is a huge risk of default – that listed as weaknesses. Moreover, the country is facing hyperinflation, and political instability.

In order to describe the country’s economic condition more accurately I examine some economic indicators.

\subsection*{2.2. GDP per capita.}

Per capita GDP is a measure of the total output of a country that takes gross domestic product (GDP) and divides it by the number of people in the country.

According to World Bank data, Venezuela faced a fiscal deficit estimated at 20 percent of GDP at the end of 2015. Table 3 shows the change in the Venezuela GDP per capita between 1990 and 2014, while table 4 demonstrates the changes during the last 5 years.

Table 3. Venezuela GDP per capita

![Graph showing Venezuela GDP per capita](image)

Source: World Bank

Table 4. Venezuela GDP per capita

![Bar chart showing Venezuela GDP per capita](image)

Source: World Bank

As is seen from the Table 4 the deterioration started from 2013 and expected to shrink significantly till 2020.

### 2.3. Unemployment rate

Unemployment rate is defined most basically as the percentage of the total labor force that is unemployed but actively seeking employment and willing to work.

The all-time high unemployment rate in Venezuela was observed in 2003 with 20.73 percent.\(^{31}\) However, the expansion of the public sector in country during the last 15 years keeps the employment rate stable, fluctuating around 6-7.5 percent.

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2.4. Inflation rate.

Inflation rate in Venezuela averaged 29.61 percent from 1973 until 2015. However, consumer prices increased 180.9 percent year on year at the end of 2015, reaching an all-time high. In order to fight it, the government is planning to have larger denomination bills circulated in the economy. They will print 20,000 VEF banknotes, 200 times higher than the current largest denomination of 200 VEF bills.

Table 6. Venezuela inflation rate

Source: World Bank | Central Bank of Venezuela

As is seen, the economic indicators and the future expectations are not optimistic. Even though the oil prices are expected to gradually rise in 2017, the recession in the Venezuelan economy is supposed to continue. The legal environment in the country is damaging the private companies with tools such as arbitrary seizures, intrusive state audits and inspections. Thus, the public

investments is expected to continue to fall. In terms of trade, the oil export – almost the only export of the country – will decline as well for the following years.

According to the forecasts, in 2017 GDP growth in Venezuela still will be negative, however less than it was in 2016 of -10%. This year this number is expected to be -4.5%. As was demonstrated in the table 6, the inflation rate will increase drastically almost 4 times, and will be 1660%. However, a public debt is predicted to be decrease.
Chapter 3. Economic and political map of Azerbaijan

Almost same with the Chapter 3, this chapter discusses the historical insights of the oil policy of Azerbaijan deeply, and introduces the current economic and political situation in country, together with economic indicators such as GDP per capita, unemployment and inflation rates.

3.1. Current economic and political situation

Azerbaijan proclaimed its independence in 1918. Two years after the country was incorporated into Soviet Union and regained its independence again only in 1991. Right after that the country decided to lead a market economy way and opened its “doors” to foreign investors. In order to strengthen its objective, the country joined several integrations, such as International Monetary Fund, World Bank, European Bank for Reconstruction and Development and etc. The World Bank’s Doing Business report announced Azerbaijan as one of the top 10 reformers in the world in 2008, and ranked 57th in the Global Competitiveness Report in 2010-2011. However, even then the high rate of inflation appeared as a result of the increasing prices in non-oil sector demonstrated that the country needs to take serious steps in order to challenge the “Dutch disease”.

There was a drastic economic collapse in Azerbaijan after gaining independence from the Soviet Union. During the first three years the inflation rate was above 1000%. In order to fight this hyperinflation Azerbaijan launched an IMF-backed stabilization program in 1995. The program was successful and as a result fiscal deficits were reduced and the country was able to implement a tight monetary and credit policy. The inflation was reduced to 20% and economic growth was positive first time after the independence. During 1997-2004 there was almost 10% of growth in the country. Starting from 2005 the Azerbaijan economy started a new period of growth that started the dependence of the country on oil. The country faced a challenge of successfully using the oil revenues in order to diminish or reduce the poverty. It should be taken into account that Azerbaijan inherited from the Soviet Union a collapsed economy and the war with Armenia that ignited right

after the collapse of the USSR threw the country into a humanitarian crisis. For instance, the initial oil revenues were spent to provide normal life conditions for the victims of the war - internally displaced persons. Additionally, the infrastructure in the country struggled the transit into market economy. Funding all these problems required huge amount of investments. That was the reason, the public expenditures increased significantly starting from 2005. However, the huge inflow of oil money helped the country to achieve an unsustainable development till 2016, despite the high level of bureaucracy and corruption.

After long period of development Azerbaijan economy started to contract in 2016, due to low oil prices that decreased the government investments that are important for the non-oil sector. According to World Bank, poverty is going to be the main problem in the country over 2016-18 and further poverty reduction requires the Government to undertake bold reforms to facilitate private sector activity and strengthen the labor market.

In current situation, the country risk assessment studies indicate the abundance of hydrocarbon resources and skilled labor force as strengths of the country. Moreover, Azerbaijan is developing new energy routes to the EU. As weaknesses, the studies headline the inadequate economic diversification, armed conflict with Armenia and governance problems with high level of corruption.

3.2. GDP per capita.

If we have a look to the trend of GDP development of the country we can see a huge and stable increase starting from 2004. However, the growth rate turned to be negative starting from 2014. The country’s GDP contracted by 3.4% in the first half of 2016, reversing 5.7% growth in the same period of 2015. However, there expected a growth by 1% in 2017 largely because of the government incentives to develop non-oil sector, mainly tourism.
Table 7: Azerbaijan GDP per capita

Source: World Bank

Table 8: Azerbaijan GDP per capita

Source: World Bank

Unfortunately, the data for 2016, when the oil prices started dropping, is not available. However, according to World Bank economic models, Azerbaijan GDP is expected to trend around $6159 in 2020.

3.3. Unemployment rate.

The highest unemployment rate in Azerbaijan was experienced in 2000 by 11.8 percent and it took almost one decade to decrease this percentage to 5-6 percent. This decreasing trend was over in 2014 and in 2015 unemployment rate increased from 4.9% to 5%.
3.4. Inflation rate.

As headlined before, Azerbaijan is constantly experiencing the increasing prices of goods, largely due to the increase in the prices of the imports. That increase is directly related with the devaluation of the national currency that was resulted from the dependence of economy on the oil prices. In other words, the boost in the inflation rate is linked with this dependence.

Moreover, monopolistic competition almost in all fields of the economy predominantly leads to the inflation. As is seen on the Table 10, the inflation rate in Azerbaijan has almost never been stable. According to World Bank estimations, despite of increasing inflation rate in 2016 and 2017, for the following years there will be low and stable level, if government is able to fulfil its programs successfully. The country decided to cut its production of oil in a respect to OPEC’s plans. This may badly hurt the economy in the first months, but it will allow for a better recovery if the oil supply diminishes and oil prices go up.
If to compare to Venezuela, the rise in the oil and gas prices is expected to recover the economy in 2017 from the recession in 2016. Surprisingly, the sharp devaluation of the national currency suddenly stabilized, and this factor can decrease the rise in prices of goods and services, despite of the opposite expectations. However, due to the cuts in governmental spending, the service and construction sectors, that together contain 35% of GDP will likely be hit. Private investment is also supposed to diminish because of the limits in lending resulted from the weakness of the banking sector and the sharp rise in interest rates (from 3% in February to 15% in September).

According to the forecasts, in 2017 the increase in GDP growth will be 1% that is quite optimistic in a comparison with -3.2% of 2016. Inflation is expected to fall to 10% of GDP from 12%, and current account balance will be 0.4%. The amount of public debt will stand constant.
Chapter 4. The “Dutch syndrome”, or resource curse

This chapter first will explain the definitions for the “Dutch syndrome” and resource curse, showing their differences and determining why this phenomenon should be considered legit for Venezuela and Azerbaijan. Then some other countries that experienced this syndrome and their relatedness to these both countries will be examined. Moreover, the chapter discusses the negative and some positive effects of the resource curse in the topic countries, and in order to better describe these effects some economic data and graphs will be introduced.

4.1. A brief explanation

This term was first used in 1977 by “The Economist” referring to the exploitation of a large natural gas field discovered off the coast of Holland to a considerable decline in Dutch manufacturing. When a country’s revenues from resource boom increase, the currency of a given nation appreciates. A real appreciation reduces the international competitiveness of other tradeable sectors because resource-based exports crowd out commodity exports produced by these sectors. This process ends up by de–industrialization. Mainly this syndrome affects the economy in two ways: the resource movement effect, and the spending effect. Basically, an increase in energy price pushes the value of the marginal product of labor up and raises the equilibrium wage rate. As a result, the labor moves from the manufacturing and non-tradable sectors to the energy sector.

The resource curse (also known as the paradox of plenty) refers to the failure of many resource-rich countries to benefit fully from their natural resource wealth, and for governments in these countries to respond effectively to public welfare needs. In other words, the resource curse happens when a country concentrates all of its power and attention on a single industry, such as mining, and neglects other major sectors.

The difference between the Dutch syndrome and resource curse phenomenon is that, resource curse can refer not only to currency inflow resulted

from natural resource boom, but also to any development that results in a large inflow of foreign currency, including a sharp surge in natural resources prices, foreign assistance and foreign direct investment.

Ideally, according to main trade models, a country would be better off, if it specializes in industries in which it has a comparative advantage. Thus, theoretically, country abundant with natural resource should specialize in the natural resource extraction. However, it is dangerous for the economy to shift away from the manufacturing. Because, if the natural resources run out, or their prices decreases (the problem that Venezuela and Azerbaijan are experiencing nowadays), country will hardly return back to the competitive manufacturing industries. This situation is difficult to recover. Further, the Dutch disease leads to the cut in investments, because firms will not invest if they are not sure about the future economic stability in the country.

Basically, there are two ways of reducing the negative effects of the Dutch syndrome: slowing the appreciation of the real exchange rate and increasing the competitiveness of the manufacturing sector. The main idea here is preventing the all the revenues from resource boom to be brought into the country at once. This can help country to save money for the future generations and invest in education and infrastructure that, in turn will boost the competitiveness of the manufacturing sector. However, in developing countries such as Venezuela, Azerbaijan it is hard to maintain, as all the revenues should be transferred into the country in order to fight the poverty and develop the living condition of the people.

4.2. The experience of other countries and their relatedness to Venezuela and Azerbaijan

Several countries have experienced the Dutch disease syndrome and most of them are developing countries that are abundant with natural resources. From the developed European countries Spain case may be an example. Two regions of the country (Balearics and Canary Islands) had evidence that the country experienced the Dutch disease in tourism.

As headlined before in introduction part, in order to fully describe the level of the expected perils of Dutch syndrome into the economy, experience of the neighborhood countries will be discussed.
In Colombia – Venezuela’s neighbor country, the booming sector was coffee and drug export. The industrial development and the foreign earnings were mainly result of the coffee export and government’s protectionism policy by a strategy of import substitution. ¾ of total revenue in Columbia came from export, while internal production increased the export of non-tradable goods. Generally, the symptoms of the Dutch Disease in Colombia were followings: during the coffee boom, the relative price of home goods increased as well; the growth rate of the non-coffee exports slowed down. After the coffee exports slowed down more than $500 million (or 24%), oil and derivatives sectors started the development by increase of 12.3%. This decrease in coffee sector affected the whole agriculture sector as well and led to the nationwide strikes as a result of what the government decided to grant a subsidy. Colombian case should be considered as a special one, because the investment inflow was not hit hardly, just changed the route from one sector to another. Together with the successful monetary policies of the Central Bank, this investment inflow into oil sector generated positive effects in short term, but in long term affected the economy negatively.

Colombian case shows that Latin America countries are vulnerable in terms of the Dutch disease mainly because of the strong importing neighborhood countries such as Canada, the USA. Thus, these countries are obliged to focus on the one single sector that they have competitive advantage that further leads to the downward shift in all the other tradable and non-tradable sectors.

The Dutch disease symptoms in Azerbaijan may be compared to the other oil producing countries of the Caspian Basin Russia and Kazakhstan. Taking into account that there is a strong relationship between the decreasing oil prices and economic sanctions of the USA and EU against Russia, the mentioned situation played negative effect almost on all the economic partners of the Russian Federation.

Russia is the world’s largest producer and exporter of the natural gas, and in the second place in crude oil production and export. The country is strongly

dependent on oil and gas production. Two third of the merchandise export of the country is about oil and gas that contains 50% of federal budget revenues. However, oil sector is responsible only for the 2% of the employment\textsuperscript{40}.

The research done by N. Oomes and O. Panomarenko (2015) indicates that Russia’s oil dependency increased the prices for the basic goods. They found a strong relationship between oil price and real exchange rate and determined that changes in oil prices have strong effect on real exchange rate of the country’s currency. Moreover, by using regressions they found out that the region that is more dependent on oil has more possibility to experience Dutch syndrome.

Dutch disease in Russia has begun from the beginning of the 1990s with the beginning of transition period. Bernardina Algieri indicates five signs of Dutch syndrome in Russia\textsuperscript{41}: real exchange rate appreciation, economic development based on higher oil prices, a relative de-industrialization, the decrease of export in non-developing sectors, growth of real wage. Generally, suggestions for Russia on how to avoid Dutch syndrome are almost the same with the suggestions to other countries: diversifying the economy, and stop the appreciation of the exchange rate through the fiscal and monetary policies.

Right after the sanctions against in Russia became in power, the country started feeling the “breath” of the Dutch Disease more considerably. As a result of decreasing oil prices the Russian Ruble lost the value by 25% in 2014, and this number kept on increasing on following years. Although Russian Finance Minister headlined that, Dutch disease is over for the country and the ruble is no longer overvalued in real terms, the other Caspian Basin countries such as Azerbaijan, Kazakhstan and Turkmenistan are still suffering because of the mentioned oil price decrease.

Russian case is the indicator of the special form of the Dutch syndrome, where the economic situation in one country is strongly dependent not only on the prices of exported resources, but also on the neighborhood country, that is the significant exporter of that particular resource. However, it is hard to implicate Russia’s anti Dutch syndrome policy models in Azerbaijan in a hope of success,
mainly because of the differences in scales and resource endowments between these two countries.

4.3. General indicator and effects of the resource curse in Venezuela and Azerbaijan

As mentioned before, an increase in a production of natural resources causes a decline other economic sectors. Discovery of the oil and gas had almost the same effect in Venezuela and Azerbaijan. These effects can be grouped as following:

a) An increase in exports of oil lead to the increase in demand of Venezuelan Bolivar and Azerbaijani Manat. Upon the different policies of the governments, this demand had different effects. In 2003 the government of Hugo Chavez established strict control over the currency, as a result of what, Bolivar devaluated five times, damaging the economy. Meanwhile in Azerbaijan, the inflow of the oil dollars forced the strengthening of the national currency against dollar. In 2005 it appreciated by 8%, and in 2006 further 5%.

b) Manufacturing sectors experienced a substantial fall, as a result of higher exchange rate. The difference was that, in Venezuela economy shifted gradually towards the primary sector, while Azerbaijan did not even have an attempt to create sustainable manufacturing sector. In other words, an “absolute de-industrialization” has not taken place in Azerbaijan, hence, the country suffers from a “relative de-industrialization” in the non-oil tradable sector.42

c) Both countries experienced high demand for the service sector workers, due to increased wealth and spending on the service sector. This demand increased the real salaries, and manufacturing sectors had to increase the wages of their workers as well, that resulted with further increase in costs and decline in competitiveness.

d) Unequal distribution of the oil and gas benefits among the population. In both countries, an increase in GDP is only concentrated in the hands of small number of people. Moreover, those who are working in the oil sector are getting much more salary than those in other sectors.

42 Hasanov, Fakhri. 2013
However, after the decrease in the oil prices both countries started struggling in economic terms. As results of the factors mentioned above:

a) Manufacturing export industries fell behind because of the decreasing investment and output: Together with public investment, foreign direct investment has also declined. In Venezuela, this declining environment started from 2009, mainly due to the political uncertainty. However, the abundant resources and labor gave a hope to the investors that economic climate in country might recover. According to Central Bank of Venezuela, if in the beginning of 2014 FDI in Venezuela increased by $2395 million, after one year this number was just 12. Azerbaijan had also experienced drop in FDI by 13% in 2016. With its favorable geographic location, cheap and qualified labor, competitive costs of production Azerbaijan can be considered as a good destination for the foreign investors. However, the poor infrastructure, high level of corruption, lack of developed sectors rather than oil sector, insecurity and destabilization fears because of the Karabakh conflict, etc. negatively effects FDI inflow;

b) Huge drops in the oil prices lead to the current account deficit: starting from the fourth quarter of 2014 Venezuela is recording a current account deficit and in the first quarter of 2015 it reached a record of -$6088 million43. That was a result of drop in the trade surplus generated from the slowed oil exports – the most important component of Venezuelan trade – to $15.5 billion, while imports remained almost unchanged. Azerbaijan is also continuously experiencing a current account deficit since the fourth quarter of 2015 and in the third quarter of 2016 this number was -$312 million44. To compare, deficit in current account of the balance of payments for 2016 exceeded the 2015 indicators by 6.1 times.

c) In order to maintain the budget both countries became obliged to bring new taxation policies that is leading to the lower living standards.

Venezuela’s new tax policies are mainly focused on the large financial transactions. For banks and insurance companies, the income tax increased from 34% to 40% after the new taxation decree that was enacted in December 2015 and became on power in January 2016. Azerbaijan also accepted new tax rates for banking transactions. From the beginning of 2017 for transferring money into the “electronic purse” of non-residents by residents of the Republic of Azerbaijan, the ban conducting the operation holds a levy of 10% of the amount of the transfer. Moreover, legal entities and private entrepreneurs pay 1% of taxes for cashing money from their bank accounts. These new rules apply to the purchase of the services online, not goods. However, for instance, buying travel tickets online is also considered as a service.

d) As mentioned before, both Venezuela and Azerbaijan experiences the decline in GDP. In turn, the demand for the high service sector decreases and it creates a huge unemployment.

e) National currency devalues. To put it simple, exported oil is sold for dollars in world market that flood the exporting country. Then these dollars compete to buy the national currency. As a result, the national currencies of both countries appreciated. When the oil prices were high, people in both Venezuela and Azerbaijan preferred to import a lot of international goods, especially the luxury things. Consequently, the imports bypassed the domestic production. Seeing that people are benefitting from this situation, both governments tried to keep the currency strong. Thus, when the prices went down, governments were unable to keep the currencies strong, and they started depreciating. As a result, people became unable to have enough finance to buy import things.
Chapter 5: Post-oil-crisis policies

This chapter describes the period that starts after the damaging effects of the crisis. Experiencing the negative circumstances of the dependence on oil export, both countries have tried to implement new policies that would help them to avoid the economic perils. Thus, in this chapter I describe the non-oil sector and its development in Venezuela and Azerbaijan, and the potential fields that may be developed in both countries in order to boost the economy. Moreover, I discuss the current crisis management policy and its analysis for the both countries.

5.1. Non-oil sector and its development

As headlined before, the single, most important sector in Venezuelan economy is mining. Before the development of oil industry, the country has predominantly been an agricultural economy. Nowadays, only service sector considered to be the alternative to the mining sector. The development of service sector is related with the increase in wealth generated by the oil exports. Once, oil prices are decreasing, service sector is also living its problematic days. However, till 2014, these 3 sectors, accounted the main shares of GDP of country till 2014.

Table 11 reveals the share of those economic sectors in the GDP in Venezuela from 2004 till 2014.

Table 11: The share of economic sectors in the GDP in Venezuela (2004-2014)

Source: World Bank
In Azerbaijan, the oil boom and the huge investments into public infrastructure altered the structure of the national economy. The country mainly focused on the oil sector till 2007, and as a result in 2007, the oil sector accounted for 53.7% of GDP. However, the non-oil sector started increasing in 2006, and the share of oil in GDP decreased to 34% in 2014.

Azerbaijan government has put a huge amount of investment on the agriculture sector. However, the results were under the expectations. The reason was, the unsustainable management of this finance and lack of control over the subsidy. However, mainly due to the drop in oil production and governmental efforts on tourism and service sector, the share of service sector in GDP exceeded the share of mining in country.

Table 12. The share of economic sectors in the GDP in Azerbaijan (2005-2015)

![Graph showing the share of economic sectors in the GDP in Azerbaijan (2005-2015)](image)

Source: World Bank

Growth in the non-oil sector in Azerbaijan was mainly investment-driven, rather than productivity-driven. Due to the high investments and public expenditures demand for non-tradable goods (service, construction) has increased. Thus, main productive resources have migrated to the oil and non-tradable sectors and as a result non-tradable goods sector developed more than tradable goods sector (agriculture, manufacturing, forestry, etc.). According to the State Statistical

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Committee of Azerbaijan, starting from 2007 there was a gradual growth in non-oil GDP.

5.2. Non-oil development potential of both countries

As mentioned before, even though Venezuela and Azerbaijan struggled to diversify the economy over these years, they both have large potential of possible development of the non-oil sector. However, due to the several reasons, these sectors were either not discovered and undermined, or failed despite of the huge governmental investment. Mainly, the reasons of this failure had been corrupted local governmental representatives and majority of the low skilled and less educated people in project management.

One of the major non-oil industries in Venezuela is considered to be the heavy industry. In 1980s Venezuela became a leading international producer of steel, iron, coal, aluminum and gold. Over 1% of the labor force was involved in this industry and it accounted for less than 1% of the GDP, by providing 13% of the exports. From those, steel and iron industry played a representative role because of the huge reserves. Steel industry was nationalized and had high ambitious goals in 1980s. However, these goals were unable to meet. The reason was the slower internal growth that barely met the local demand, and international demand decrease by other steel producing developing countries. The main steel company of the country, Sidor’s exports eventually exceeded the imports in 1985, mainly due to the help of government subsidies through special foreign exchange rates that later led to the complaints. The United States Department of Commerce accused Sidor that it sells its steel in the USA 40% cheaper than the local price and both countries signed a Voluntary Restraint Agreement in 1985 that set a limit in export. Sidor was privatized in 1997, and renationalized in 2008 whose 60% shares belong to Argentina’s company “Ternium”.

Moreover, steel industry is presenting one of the most essential of more than 123 projects agreed through Venezuela-China agreement and financed by China Venezuela Joint Fund. In 2014 Venezuelan iron and aluminum companies Sidor and Venalum signed two agreements of $750 million with China’s Minmetals Engineering. The aim of the agreements is to increase the production against the economic war. Moreover, the projects are planning to extend the iron ore haulage
system of the Palua dock, with an export capacity of 7.3 million tons of fine iron ore, iron ore lumps and pellets, per year.

Today, Venezuela’s steel industry is exploited by Sidor and Sivensa. Sivensa’s subsidiary – wholly private company Sidetur was expropriated by the government without any compensation. Steel Production in Venezuela averaged 269.81 thousand tons from 1980 until 2016, reaching an all-time high of 479 thousand tons in March of 2007 and a record low of 10 thousand tons in August of 2016.

**Table 13. Venezuela steel production (1980-2016)**

![Graph showing steel production from 1981 to 2016](image)

**Source:** *World Steel Association*

Among all the other Latin America countries Venezuela has smallest share of agriculture in economy, mainly because the country does not have the rich soil like other LA countries have. As mentioned before, discovery of the huge oil fields resulted in decline in this industry that was dominating in Venezuelan economy.

Upon the last 70-80 years agriculture and land reforms were undermined and neglected in Venezuela. The country heavily relies on food and agricultural products. 70% of cereals and 98% of oilseeds consumed in the country are imported mainly from Colombia and the United States. The sector only provides 5% of GDP, however before the oil era began coffee was the main export item in the country. The main field crops are sugarcane, rice, corn and sorghum, while the most important agricultural items for industrial use are cotton, tobacco, and sisal. Even though today approximately only 20% of the land is used for agriculture, it remains an important source of employment where around 14 percent of the labor force is concentrated.

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The worse growth of agriculture was experienced in early 1980s, after which some development programs designed in order to revive the sector. Government policies towards the agriculture often differed between deregulation and extensive government intervention. Due to the mentioned policies the annual growth rates reached to 8% in 1984 and 1985. However, these government programs involved high levels of subsidization, thus, they were too costly to maintain. Apart from the agricultural programs, land reforms also had been done by the government after 1960. However, they had made only some slight adjustments in Venezuelan land tenure. Today the landholdings are divided into expansive latifundios, and small, subsistence-based minifundios. According to current estimates, in 1980 smallest 42.9 percent of all farms covered only 1% of the arable land, while the largest 3% accounted for as much as 77 percent of arable land.

Venezuela’s abundance of arable land and temperate climate provide ideal conditions for the development of agriculture. Government should consider this sector by eliminating several problems and developing the post production management.

There always were fluctuations in tourist arrivals in Venezuela. For instance, as the Bolivar appreciated in 1983, there was a decline, however, during the following 3 years the tourist arrivals increased more than twice.

Nowadays, because of the food and beverages shortage the foreign tourists have almost disappeared in the country. Another reason of this decline is the new visa requirement for the USA citizens.

Even though Venezuela has different landscapes, hot beaches, and cool mountains, rich plant and wildlife, the tourism sector in the country is considered to be underdeveloped. The tropical climate of the country enables each region and beaches to be affordable. Apart from beaches, there are a lot of sightseeing places, some of which are the world heritage, such as Coro city, University City of Caracas, etc. Moreover, the largest rainforest in the world Amazon rainforest starts from the country’s area. The highest waterfall of the world Angel Falls increase the tourism potential of Venezuela. Even though government has some incentives in development of the seaside tourism, ecotourism in the savannas and jungles has not been exploited.
Azerbaijan is also abundant with the possibilities of the development of other non-oil sectors. For the last 2 decades, the main sectors in the country after oil sector were construction and agriculture.

Construction sector generates 11.7% of GDP in Azerbaijan and till 2014 this sector enjoyed huge growth. Even though in the end of 2015 there was a 13.4% contraction, there still was 1.9 million square meters of new housing put in use and according to the Statistical Committee of the country, GDP from construction increased 176.10 million Manat in the second quarter of 2016.

Table 14. Azerbaijan GDP from construction

![Graph showing Azerbaijan GDP from construction]


Generally, during the last decade the building work in the country flourished enormously and much of this works were done in road infrastructure. Just for the purpose of comparison, during the last 3 years 77 road bridges and overpasses, 13 road intersections, 23 pedestrian crossings have been put into operation. There also were several projects that can be considered as an architectural masterpiece. One more advantage of this growth was that, the local construction companies started to penetrate into international markets in countries such as, Russia, Ukraine, Kazakshtan, etc. The market itself evolved from the state controlled to the private design and building companies that are widely using the latest Western technologies.

However, this sector started experiencing after the oil crisis. The main reason of this downturn is that, Azerbaijan is importing almost all of the construction materials. For instance, for the import of iron, plastics, wood and glass products, the country has spent approximetly $2.5 billion in 2015.47 As there a some

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huge projects that have not been concluded yet, this number is going to increase because of the devaluation of the national currency. Thus, the decrease in construction sector may also be considered to be related with the results of the oil dependence. It should be headlined that from January 2017 a new free trade zone is set to operate at Baku International Sea Trade Port. This can make the shipping prices of construction materials cheaper. My opinion is, as Caspian Sea has no direct access into the World Ocean, the new trade zone is not estimated to be of big help in short run. However, this belated decision can be counted as a serious step done by the government to obtain a competitive advantage in trade sector.

Moreover, as in all the other sectors in the country, the lack of transparency in budget management is a key problem in this sector as well. Even before the crisis started, the huge amount of money were spent on the quality of the new bridges, building and other construction projects, but the problems in constructions started appearing just in 2-3 years of utilizing. Apparently, not all the money that supposed to be go to the quality increase was spent in an appropriate way.

Agriculture is the third biggest sector in Azerbaijan after oil and construction sectors. In 2006, more than 39% of the employed population was working in the agriculture sector (only 1% in oil sector)\textsuperscript{48}, mainly because half of the population lives in the rural areas. Due to the geographic and climate conditions the agriculture sector is very diverse. These conditions allow 2 to 3 growing cycles per year. The products are mainly exported to Russia, Turkey, Ukraine and some EU countries. As of 2013, the agricultural sector accounts for 5.3% of GDP, or 57.7 billion AZN\textsuperscript{49}. The country produces a wide variety of high quality crops, fruits, vegetables, tea leaves, nuts with minimal unit production costs and strong brand recognition in former Soviet countries.

In order to develop this sector, there were several governmental projects conducted. For instance, all the producers of the agricultural products are exempted from all taxes, except the land tax. In abolished districts the economic subjects’ debts were forgiven. Moreover, half of the farmers’ costs for fuel, lubricants and fertilizers is paid by the government. As a result, the share of the private sector in agricultural production increased up to 99.7% that can be considered as a huge


\textsuperscript{49} "The State Statistical Committee Of The Republic Of Azerbaijan". 2017.
number for a former Soviet country. As mentioned before, in order to avoid the oil dependence the program called “Azerbaijan 2020: Vision into future” has been accepted by the government. The program is planning to double the GDP till 2020, mostly with the help of development in the agriculture.

However, all these programs are experiencing problems in implementing. Some farmers are unable to enjoy these incentives due to the lack of transparency. Sometimes several bureaucratic difficulties are making the process of obtaining discounted loans. Moreover, the monopoly in rural areas leaves no motivation for the people in agricultural workers.

Tourism is also an important part of the Azerbaijan economy. The major advantages of this sector is existence of the untouched and unexplored wilderness, mineral springs, ancient architecture, cuisine, etc. The country has the potential both for developing internal and external tourism. Especially in the recent years, Azerbaijan is becoming a popular destination for health care, spa and winter tourism. The country has the world’s only oil field treatment – naphthalene.

In order to raise the image of the country in the world, the government is instantly conducting different big scale sport and music tournaments in the country that attract tourists. Among of them, Eurovision Song Contest in 2012, the first European Games in 2015, and continuously taking place Formula 1 rallies are considered to be the biggest ones. As a result, the country is successfully becoming the popular tourist destinations during the last few years. Furthermore, some factors, such as the devaluation of the national currency and other political events in neighborhood countries, such as terror attacks in Turkey and last year’s political conflict between Russia and Turkey, have positive effects on tourists’ decisions in destination selection. The government simplifies the visa and other travel related issues that attracts a lot of tourists, especially from Iran and other rich Arabic countries.

During the Soviet period, the country had been a popular tourist spot, especially in the 1980s. However, after the collapse of Soviet Union, Azerbaijan became in war with Armenia that damaged all the industries, including the tourism. The industry began recover only after 2000. During the period of 2007 - 2011, the amount of income received by Azerbaijan from international tourism increased from around USD 200 million to USD 1.3 billion. The estimated direct contribution
of travel and tourism to the country’s national GDP in 2012 was over USD 1.1 billion. Just for comparison, total GDP of the country in 2012 was $68.7 billion.

The factors headlined above indicate the potential of the country in tourism. However, there are still a big amount of problems that need to be solved in order to increase the competitiveness of the tourism industry in Azerbaijan.

First of all, the whole tourist infrastructure is underdeveloped. Nowadays, there are more than 450 hotels in Azerbaijan, most of which are world chains, such as Marriott, Hilton, Four Seasons. However, the related infrastructure, such as transport, catering, entertainment industry needs some strong attention. Moreover, supply and demand, environmental requirements, and the economix expediency of creating new facilities should be kept in mind.

As is seen, both Venezuela and Azerbaijan can diversify the economy by using their potentials in non-oil sectors. However, this steps are too cost weighted, and seem to be impossible in current situation without foreing direct investment. However, the foreign investors require guaranteed safe economic environment that both countries lack.

5.3. Current crisis management policy and its analysis

Economic problems in both Venezuela and Azerbaijan brought the necessity of implementing new, completely different policies in economy. This kind of economic turmoil level is not new for both countries: in 1989 Venezuela and right after the collapse of Soviet Union Azerbaijan has experienced the sharp level of inflation. However, this time the scale of the damage is too considerably big, mainly because of the higher dependency on oil. For instance, if in 1989 Venezuela economy’s dependency on oil was 80%, now this number is 95%, while Azerbaijan started to transmit from centrally planned economy to market oriented one by simply basing the whole economy on oil. Now, facing the sharp shortages in budget, both countries looking for the ways of diminishing the negative effects in economy. Unfortunately, the steps that the governments are taking mainly either belated, or leading to the budget refill by increase in social problems and poverty.

In Venezuela, government struggles to adequately respond to the crisis due to the several factors, such as organized economic sabotage and violent destabilization by the opposition, the high level of corruption, little political intend to stabilize the weakened institutions, and the lack of strong community-based organizations. There are several policies suggested to the government by the economists, National Bank, National Assembly and the opposition as well.

The opposition suggests neoliberal program that is related with the fiscal austerity. They say that, the Central Bank should be politically independent in order to stop printing money upon the requests of the government to finance social spending. This cut in social spending may help the State Oil Company to focus on new oil activities.

As a contrary idea to this suggestion there is also a market-based reform suggestions. They define the markets as socially constructed institutions that can bring positive outcomes if the government manages them well.

There are some economists that are favoring to move toward socialism with the state, that includes in itself the policies, such as tax reform, foreign commerce nationalization by the control of government, an audit of the external debt (that may lead to the refusal of some part of it), fighting against the subcontracting in all workplaces, an increase in the wages, defining a national plan for industrialization, cancellation of the non-priority costs, especially for the holding of the governmental apparatus.

There are also some other economic suggestions to make the country move forward, and all of them considered to have both advantages and disadvantages. Unfortunately, Maduro’s government has taken only few serious actions in order to save the country from the expected default. Contrary, the policies the government implements worsens the social condition of the population. One of them was an unexpected demonetization decision. Following India’s experience, Venezuelan government announced that citizens are given 3 days to get rid of the 100 Bolivar – the most widely used currency (almost 77% of the nation’s cash). Moreover, the people are given 10 days to transfer their money into the bank account. The explained reason for this drastic action was to vent the inflation that is going to hit 475%, according to IMF forecast. Furthermore, the transnational mafias are flourish in the country, thus this decision is expected to make them run out of black money.
However, the promised higher denomination bills that are supposed to replace 100 Bolivar did not arrive in banks in time that led to the catastrophic chaos. People reacted to the situation immediately by closing the streets, blocking the roads, destroying the shops and ATM machines.

Another attempt to increase the citizens’ purchasing power was raising the minimum wage. In 2014 the government increased it by 30%. Till July 2015, the minimum wage was increased 4 times reaching 30$ per month by the black market rate. However, even during the first attempt the inflation rate was more than 59%, thus this measure helped temporarily. Contrary, it worsened the situation of the companies that were struggling because of the currency shortage, because now they were obliged to pay more salaries.

Additionally, increasing the price of the domestic gas is considered to be another attempt to survive from the crisis. Venezuela has cheapest gasoline prices in the world, and even after increasing the prices 60 times, the country still enjoys low prices. However, this policy is focused on refilling the governmental budget without creating value added in long-term period.

In Azerbaijan the second currency devaluation gave a red alarm for the government. Even though there were not serious demonstrations among the population, government realized that with this temps of economic contraction the default can be unavoidable. Thus, the government hired the consulting firm Mckinsey & Kompany to develop a road map for the country’s economy up to 2025. As a result a decree has been signed by the President of the country Ilham Aliyev that is called “Strategic road maps for the national economy and main economic sector. The decree includes in itself different road maps for developing almost all the sectors in country with high potential of growth and benefit, such as, oil and gas, agriculture, SME, heavy industry, tourism, logistics, financial services, etc.

The accepted economic and monetary policy is focused to be compatible with the current post – oil period. The problem was that, the crisis started in an unexpected for the government time. Even the presidential aide of the country Natig Amirov headlined that “we were expecting to enter the post oil era in about 10-15 years, but we have practically found ourselves in that situation already today”.

However, it should be taken into account that Azerbaijan had quite enough time before to adjust the economy of the country to the current situation, as the country was not hit seriously by the financial crisis in 2008. So now, there are two main priorities for the government and Central Bank:

- overtake the inflation;
- prevent potential national currency exchange rate fluctuations.

However, the last problem seems to be hard to solve in current situation. The point is that, monetary policy today is focused to complete the dollarization (a situation where a country, either officially or unofficially, uses a different country's currency as legal tender for conducting transactions) process and start anti-dollarization. This dollarization process will prolong till the time that the demand for dollar will be entirely met. Otherwise, the Central Bank will not be able to reach its targets. However, the dollarization process is being done in a wrong way, founded on shortage of dollar that leads to the creation of the “black market”. People are struggling to find dollars, as all the exchange points are shut down, and banks do not want to sell dollar without any concrete predictions for the future exchange rates. The State Oil Fund organizes tenders to sell the dollars to the banks, but sometimes the distribution is unfair, so that the great amount of the available dollars is summed in 2-3 banks. The restriction in dollar sale creates problems for the entrepreneurs who are importing from abroad, because their demand in currency is not met. 52

The Central Bank used to afraid of the huge devaluation of the national currency, that is why they did not switch to the floating exchange rate in time – after the first devaluation on 21st of February, 2015. Only after the second devaluation in December, the Central Bank announced to switch to the floating exchange rate, where the rate is determined in the market.

Apart from that, the huge problem for the economic development in Azerbaijan was the high level of bureaucracy that confronts free business conduction. According to the annual reports, currently Azerbaijan is in the 65th place in terms of starting the business. 53 The main problems have been the huge

52 Bayramov, Vugar. 2016
amount of inspections by the different governmental bodies. Hence, one of the main requirements of the President was decreasing this number of. As a result, the amount of conducted inspections from November 2015 to March 2016 was 49, as compared to 33000 checks in the same period of the previous year.
Chapter 6: What can be implemented?

In this chapter I will answer the research question about what is needed to be implemented in order to survive from current crisis. It will discuss the existing individual policy suggestions that can be adjusted in Venezuela and Azerbaijan. From these suggestions, I will draw the policies that can be implemented in a common way in both countries. Moreover, future perspectives and estimated chances of development will also be predicted.

6.1. Adjustment of the existing policies

As mentioned before, both countries are being suggested different strategies to implement by the economists and oppositions. However, the lack of intend from the both governments to fulfill the suggested policies lead to the deepening of the poverty. All the previous attempts towards the poverty reduction are becoming in vain. As a result, both oil rich Venezuela and Azerbaijan are currently one of the world’s biggest economic basket case.

There are several reasons why these countries avoid to change the main policy in economic maintenance, but the main factor is, both countries have been ruled by the same policies during the last 2 decades, and it is hard to revert the existing policy. It is mainly accurate for Venezuela, where president Maduro, and his predecessor Hugo Chavez have been keeping the power for almost 17 years.

The steps that the country has to take are clear: avoiding the price and exchange rate controls and subsidies. During all these years when the oil prices were high the government has been using the money of oil in unsustainable ways to provide money for the life of the citizens by regulation almost all the day to day activities by subsidies. This aim of price control was gaining the support of the nation that in short term with the help of oil money tsunami seemed to be effective. Now, with the low oil prices there is nationwide shortage of the essential products such as toilet paper, sugar, milk, etc. In other words, it is like a shopaholic, who is getting crazy by the credit card and then end up by nothing.54

Naturally, after avoiding the price control, the prices will increase drastically. The percentage of increase will depend on the goods. However, this

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issue is also may be solved by implementing this policy gradually together with other policies.

As mentioned before, in Venezuela the exchange rate of Venezuelan Bolivar is also fixed. This action has been taken by Hugo Chavez in order to support the currency, and also to gain the support of the companies that obtain an access to the foreign currency. As a result, the companies that supported Chavez got dollars at official exchange rates as an indirect subsidy, while those who were against him struggled to get dollars and lost the chance of importing raw materials. However, this issue created struggles for the transnational companies that are the source of the foreign investments. Fixed exchange rates mean that they can’t send their profit back to their home country. As a result, they either diminished the scale of their activities in Venezuela, or “packed their bags up” and left. Lifting the currency control would encourage the multinationals to pour the capital into country and strengthen the bolivar. The Venezuelan government may apply to the experience of Argentine that in 2011 loosened some of the restrictions on currency control that has been in power since last ten years.

This policy is considered to be belated one, because avoiding the currency controls would be painful for the country, increasing the prices of basic consuming goods that are imported. Government should implement this policy gradually as well, and try to prop up the bolivar when it slums. However, for this purpose the country needs plentiful foreign currency reserves that are steadily shrinking in the budget since 2014. Another option to prop up the bolivar may be the supplementing money for the poor families to buy the basic needed goods. However, it also requires huge amount of budget.

Government subsidies is another factor that weakens the Venezuelan economy, and government needs to avoid it as well in order to increase revenue. According to the economists, Venezuela would be better off if spend more subsidies on health and education, rather than on gasoline and electricity. Over 2 decades the subsidies have been a tool to reward the allies of the government, regardless their level of management. In its turn, it led to the corruption and decay that negatively affected the economy. Government can encourage the companies to run the business more fiercely, that again may end up with disasters and increase the level of unemployment. However, as mentioned before, if government avoids price and
currency rate controls, it will increase the prices that can be beneficial for the companies to make more profit in a situation of fierce competition. It is also possible to reduce the budget gap of Venezuela by reducing the spending on subsidies.

The government is trying to take some little steps towards the mentioned economic options. For instance, the foreign exchange system has been pared down from 3 different rates, to two: a fixed rate; a floating rate. Moreover, Maduro’s government is trying to renegotiate the terms of debts with the country’s creditors. However, it is obvious that, the country will need economic aid to fulfill its plans. Thus, the last possible solution may be the applying for the loan from the agencies, such as International Monetary Fund. The country can use oil as a collateral to obtain more loan that will give the government more confidence to fulfill the policies mentioned above. However, some economists argue that using oil as a collateral may help the country to fund the social programs in a short term, but in long term it will increase the dependency of the country on oil extraction by giving the country no other option rather than produce enough oil to pay for the credits. In current world economic structure one thing is obvious for Venezuela: avoiding the dependency on oil is a must.

As a conclusion for this topic, it should be strongly emphasized that no matter what policy will be implemented in Venezuela, it should be done in a cautious and well-organized way. There should be a strong political will to implement new changes and escape the country from default. More important, the country should forget about its oil addiction by closing the oil windfall and avoiding use the oil when the prices are high.

There are several policy suggestions for Azerbaijan as well, and mainly they are focused on the financial system of the country.

After the second devaluation of the national currency in December 2016, the Central Bank of Azerbaijan announced the new monetary policy that was about the transition to the floating exchange rate. That was a belated decision, as the national currency had lost its value twice for that time. Some economists argue that depreciation of the national currency encourages exports and diminishes imports. However, international trade mainly responses on real exchange rates, not
nominal\textsuperscript{55}. Central Bank has been implementing exchange rate targeting policies that was risky in terms of losing the control over inflation rate. Hence, in current situation Azerbaijan would be better off by implementing inflation targeting regime.

Together with monetary policy new fiscal policy is also needed to be implemented. As mentioned before, after the independence from the Soviet Union the economy of Azerbaijan was collapsed because of the lack of strong management and the war with Armenia. Thus, since mid-2000s the country spent huge investments into the infrastructure. The investments were being made through the State Oil Fund (SOFAZ) and helped the government to significantly develop public infrastructure. To compare, in 2013 the share of transfers from the Fund reached 58.2\% of the total budget revenues, while the share of the public expenditures reached 32.9\% of GDP\textsuperscript{56}. For that time, this amount of investments were essential in order to create sustainable infrastructure for secure and reliable provision of public goods and services. However, today the main focus should be the development of tradable non-oil sector, and for this purpose Azerbaijan should reconsider its fiscal policy. New fiscal rules are needed to be adopted that will impose strong rules to both transfers from SOFAZ and public expenditures. In other words, the share of the transfers from SOFAZ should be decreased, at least to one-digit level. The decrease of transfers may rescue the fall of the accumulated wealth of the country and diminish the dependence of budget and public expenditures on the oil sector. Moreover, these reductions may help the country to avoid vulnerabilities in economy during the oil price crisis.

Reductions in transfers from SOFAZ should be done together with reductions in public expenditures, as both of them are related to each other. If the transfers from SOFAZ will be cut, this will reduce total revenues, and hence the public expenditures. Even though Azerbaijan is still in war condition with Armenia, the main cuts should be in military – defense expenditures. The main destinations of the investments should be investments in the non-oil tradable sector and investments that have positive effect on total productivity. It requires an attentive


\textsuperscript{56} "The State Statistical Committee Of The Republic Of Azerbaijan". 2017.
analysis costs and benefits of public investments. The investments that has no direct effects on the tradable sector development should be limited or absolutely removed.

However, under the current circumstances, this policy can seem to be unrealistic to implement, as the devaluation of the national currency does not let the government decrease this amount, as the imports of the public goods and services need to be financed. If the transfers from SOFAZ will be limited, this will probably deepen the deficit in budget. Nowadays, in order to avoid this deficit Azerbaijan government increases the tariffs and tax rates. However, in these occasions the better solution would be to issue debt instruments, such as bonds and treasury bills in domestic financial markets. In any case, if budget deficit exceeds 2-3% of GDP, this situation should be concerned as an urgent problem, and deficit must be limited.

6.2. Common trends and policies

As mentioned before, these 2 countries barely had any economic relatedness or cooperation before the crisis.

In October 2016, both countries’ presidents met first time in Baku. Obviously the main purpose of visit of the president of Venezuela to Baku (and later to Iran, Qatar, and Saudi Arabia) was to reach the support on preliminary agreement of the OPEC countries to reduce the oil extraction. Azerbaijan announced its support claiming to freeze the oil production in order to diminish the supply and increase the prices of oil. However, the probability of this consensus is under question, because of the several factors. For instance, Iran as an OPEC member and Russia as an observer is against of freezing the oil production. Moreover, the USA and European countries are not interested in the rise of oil prices. The lack of the strong communication and agreement between the OPEC countries may negatively affect this policy. In this sense, the decision of Azerbaijan – the country that holds only the half percent of the world oil production - on decreasing or freezing the oil production looks ridiculous. However, the successful implementation of this agreement may make both Venezuela and Azerbaijan to reconsider their economy more strictly in order to decrease the oil dependence.

In the past Azerbaijan government used to have a friendly relationship with Venezuela president Hugo Chavez, and was involved in swapping operations for sale of Venezuelan oil in Belarus. This fact can be considered as a first step to
construct a bridge of relationships between Venezuela and Azerbaijan. Moreover, Azerbaijan is going to succeed Venezuela as a head of the Non-Aligned Movement that has attracted the countries of the Third and Fourth World, in 2019 and this organization also helps to Azerbaijan to establish ties with Venezuela and other Latin American countries. As a result of these ties some LA countries, such as Guatemala, Colombia, Peru, Panama, Paraguay, Honduras, support Azerbaijan in conflict with Armenia and recognize the Khojaly massacre that was done by Armenians in 1992 in a city Khojaly, Azerbaijan.

As is seen, currently neither Venezuela, nor Azerbaijan has direct economic interests in conducting bilateral cooperation. Both of them only politically motivated in relationship: Venezuela needs all the oil producers to stop the production; Azerbaijan needs to gain the support of the Latin American countries in conflict with Armenia. Currently, the geographic locations of these countries, and their economic situation does not allow them to organize an agreement on cooperation. In order words, both countries have nothing to trade, but oil. However, new free trade zone in Baku can allow the Venezuelan government and especially the state oil company of Venezuela - PDVSA to reconsider their ties with Azerbaijan.

6.3. Future perspectives

The economist and scientists are sceptic about the future of Venezuela, calling it “uncertain as failing state”. For instance, swaps traders from Wall Street headline that, there is 97% possibility of default of the country within the next 5 years, while 75% of estimation expects the default within the next year. As mentioned in previous chapters, the chances for long-term survival still exist. However, the lack of the political willingness by the government brings all these chances down. Critics put blame on government in driving the economy into the crisis through economic and resource mismanagement. The drops on oil price and its consequences should have made the government reconsider some vital policies, such as price controls on basic goods, such as milk, sugar, etc. However, this policy started by Hugo Chavez in 2003 in order to help the poor families to get out from the poverty and proceeded by Maduro made the producers of these goods to operate at a loss, and increase the dependency on imports. Instead of taking serious steps
towards the economic reforms the government strengthens the control over media. The government is struggling to obtain an access to the international financing that is crucial for establishing the non-oil economy.

However, it should be mentioned that, Venezuela has the largest oil reserves in the world, and the production costs are relatively low, but significant above-ground risks. The government should consider improving the oil sector in order to attract the foreign investment and this consideration should be done in a planned way by several steps. First of all, the price control policy and foreign exchange regime should be changed, because foreign firms are struggling to pay employees and suppliers at the expensive official rate. Fiscal framework also needs to become more favorable. Moreover, the role of the PDVSA in the ownership of almost all the projects should be decreased.

This process may take a lot of time, and the considerable growth may require 4-5 years. World community also should give a hand to the country in a way of international financing. Hence, if the government achieves the political stability the inflow of investment may refresh.

Apart from that, Venezuela should implement a serious anti-inflation plan. If population enjoys a rise in their real income, this will naturally increase demand, that is detoriating nowadays due to the lack of money. As a result, producers can work hard to increase the production in order to meet the local demand.

Opinions about the future of Azerbaijan are diversified, and in a comparison to Venezuela, the country is still in a better position. In other words, the country is experiencing the economic situation that of Venezuela had in the very beginning of the crisis.

Azerbaijan has rich resources that helped the country’s economy to impoverish. Even though the oil boom is over now, the country still makes a bid to become a significant gas supplier of Europe. Country has good ties with its big neighbors Iran and Russia, and the government always tries to build relations with Western governments and energy companies.

In a situation of the decrease in oil prices, the country can focus on natural gas projects, or concretely on Trans Adriatic Pipeline, that is going to provide the European countries with 10 billion cubic meters of natural gas. According to Brenda Shaffer, the professor of University of Haifa, the declining oil prices are not that
dangerous for Azerbaijan, because the country regularly bases its state budget on an oil prices lower than the actual. However, the world gas market is more volatile than the oil market and the prices are lower.

Generally, Azerbaijan economy is suffering from the unsustainability problem. The economists headline that, the economy of the country is only sustainable in short-term, in long term, there are several fiscal risks. There is a huge lack of economic diversification into the non-energy sector. The reserves of national fund are rapidly declining and with the current price of oil this tendency is expected to go on.

Thus, the future of the country strongly relies on the successful implementation of the “Azerbaijan – 2020: Outlook for the future”. The aim of this project is to terminate the dependency of the economy on oil, and make the country more competitive through the improvement of social welfare, human rights and freedom, the supremacy of low, etc.
Chapter 7: Conclusion

The following chapter discusses summary of the thesis and implications and contributions of this research. Furthermore, the limitations of this research are explained below. Finally, the possibilities of further researches are suggested at the end of the research.

7.1 Conclusion

The purpose of this mixed research was to examine the current economic situation in Venezuela and Azerbaijan, conduct the analyses of the past policies, implementation of which brought the both countries into this trap of crisis. Moreover, I discussed the policies that have been implemented in order to “rescue” the country from the crisis, and suggested my own policy ideas. As headlined in methodology, the story line was divided into 3 parts, first of which was pre-crisis period of Venezuela and Azerbaijan. Before discussing the results and scales of economic crisis it is important to find out the reasons that led to this situation. Examination of the different works of the economists who have researched the economic cases of Venezuela and Azerbaijan in the period when these countries enjoyed the inflow of oil money demonstrated that both countries had concrete mission in the beginning of the mentioned period: reduction of poverty. The indicators present that this aim was actually reached in both of the countries. The huge increase in GDP per capita after the 2000s may be considered as a proof to that. However, once there was a significant increase in the social welfare of the people, instead of using the opportunity for decrease the dependency on oil exports and give a support to the development of small and medium sized enterprises, both countries continued to invest on oil and gas projects, increasing the export of natural resources. As a result, the import of the basic goods into the country became cheaper than their production.

It should be mentioned that, both countries paid huge attention on development of infrastructure spending big amount of money on it. However, one of the main problems for both Venezuela and Azerbaijan was the lack of the sustainability in conduction of the economic projects. In order to achieve the popularity among the citizens, both governments spent huge amount of money on the increasing of the social welfare that was successful in short-run, but not
sustainable in long-run. Apart from that, the lack of the control over the state budget maintenance resulted with the increase in spending. In other words, sometimes the amount of money that was subsidized from the budget for financing the infrastructure projects was more than the amount needed and spent. On the shadow of this projects, the education and medical sectors in both countries suffered the low development, as most of the money accounted for these sectors were spent on building of the new school and hospital buildings, instead of quality increase. As a result, the new generation of the governmental workers were less educated than their American and European counterparts.

High level of natural resource dependency resulted with a “Dutch syndrome” in both countries. This syndrome started creating problems after the drop in the oil prices. Both countries were obliged to devaluate their national currency. Venezuela struggled to provide the population (more than 31 million) with the basic goods, such as milk, sugar, toilet paper, etc. The food shortages drove to the demonstrations against the government. People who stayed on a huge lines in front of the markets were unhappy with situation. When the first devaluation happened in Azerbaijan, the country was preparing to the first European Games that was going to be held in Baku, budget of which was more than $8 billion. National reserves of both countries keeps on decreasing rapidly and approach to the dangerous line in an absence of serious steps.

However, there are still several economic suggestions, implementations of which can rescue the countries from economic crisis. The basement logic of all these suggestions is decreasing the dependency of economy on oil with all possible options. Achieving this, the countries will be able to develop through monetary and fiscal policies, and positive trade balance.

All these factors that led the economies of Venezuela and Azerbaijan to the crisis, and policies that the countries are implementing nowadays have been researched and delivered to the reader in this thesis.

7.2. Implications and contributions

Findings of this thesis can be suggested to the economists who are researching the latest records of “Dutch disease” and its extreme effects on countries. It can be seen from the research that the major reason why poor countries
abandoned with natural resources are unable to avoid this syndrome is the huge need of the money for financing the projects that are planned to reduce or eliminate the poverty. Therefore, the economic decision makers of the countries should be aware of these dangers for the economy and work on the policies that would save the country from deep crisis.

Furthermore, this thesis can be helpful for them who are planning to study the economic cases of these countries as a complex divided into 3 main periods: pre-crisis, crisis and after crisis.

Additionally, the phenomena of economic downturn of the once fastest growing economies has also been introduced in an example of Venezuela and Azerbaijan. Those who are interested in the social policies of these countries and the sustainability researches of them can utilize this thesis.

As a contribution, there are several researches conducted to study an economy of the particular period of either Venezuela, or Azerbaijan. However, the cases of these two countries have never been studied before in a comparison to each other and this work paper covers the gap in literature.

7.3. Limitations of the study

Despite of the resemblance in current economic situation of Venezuela and Azerbaijan, some aspects of the research was limited due to the geographic and politic difference, absence of economic ties, different level of development of neighborhood countries, cultural difference, history of economic independence, etc.

Moreover, the number of researches and reliable data conducted about Venezuela and Azerbaijan was not much. In most cases, the official data of indicators after the crisis period presented by the statistical committees of the countries was either far from the reality, or limited till 2013 – the beginning of the crisis.

Another limitation was language barrier in case of Venezuela, where the official governmental news and information was in Spanish. On the other hand, the big part of the researches about Azerbaijan has been conducted by Azerbaijani economists, and in some cases their political views apparently had effect on their researches.
The possibilities of close economic cooperation in some non-oil sectors, such as tourism, agriculture could be analyzed. Furthermore, the membership of these both countries in Non-Aligned Movement is another important topic, and studying the opportunities that this integration can bring can be beneficial not only for Venezuela and Azerbaijan, but also for the other members.
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