

# *Post-Soviet nation-building*

*the Azerbaijani path*

## **Aleksei Vlasov\***

### **Abstract**

*The article examines Azerbaijan's development strategy after regaining independence and analyzes the turning points on this path. The author reveal that 2005 marked a turning point for Azerbaijan, when its economy demonstrated the highest global growth rate, and explain how the decade of 1994-2004 established the preconditions for a pivotal moment. During this period, key growth centers were identified, a national modernization model was developed, and the key parameters of the "Azerbaijani Project" were established.*

*The author proceed to describe the various problems on this path and to provide a fresh perspective on the Russia-Azerbaijan forward-looking agenda, arguing that Russia and Azerbaijan are not sufficiently engaged in the joint innovative projects necessary for the deepening and intensifying of bilateral interaction at a project level. Russia and Azerbaijan are facing common problems related to building an innovative economy.*

---

\* Aleksei Vlasov is the director of Information and Analytical Center for the Study of the socio-political processes in post-Soviet space, Moscow State University.

2011 marked the 20<sup>th</sup> anniversary of the dissolution of the Soviet Union, and the establishment of independent states that once made up this vast empire. From a historical perspective, this is a relatively short period – just one-fifth of a century. In terms of a human lifetime, however, this twenty year period represents the epoch following the biggest geopolitical catastrophe of the 20<sup>th</sup> century: the collapse of the Soviet Union. Each of the former Soviet republics carved out its own path, generating its own nation-building experience by implementing economic and social policies, and ensuring the security of its citizens. There was no universal model.

Many decisions were made intuitively by the political elites across the CIS countries. There was simply no time for strategic planning and long-term reckoning; the circumstances of the collapse of USSR meant that each of the 15 republics was immediately confronted with the challenges of elementary survival.

Now that 20 years have passed since the dissolution of the Soviet Union in December 1991, we are able to compare the various levels of success of these national projects, and assess the sustainability of the nation-states. There is no doubt that the Republic of Azerbaijan holds one of the high-

---

*The signing of the “contract of the century” in 1994 determined the development path of the national economy for many decades, enabling the mobilization of additional resources, and ultimately the move from the “strategy of maintaining” to a “strategy of rapid development”.*

---

est rankings. Azerbaijan’s success is particularly impressive when we consider the context in which its nation-building took place. During the initial years following the break-up of the USSR, Azerbaijan faced serious economic and social problems exacerbated and intensified by the Nagorno-Karabakh conflict and domestic political turmoil. Part of the country’s territory was effectively cut off from Azerbaijan; hundreds of thousands of Nagorno-Karabakh refugees fled to Baku and other parts of the country, and required permanent support from a government that could not provide the minimum resources.

Azerbaijan’s GDP per capita fell three-fold between 1990 and 1995, by which time it was less than half that of Uzbekistan, not a rich country. In fact, in terms of GDP ranking across the newly independent states, Azerbaijan was second from the bottom. Only Georgia, a country in the throes of an even larger

socio-economic crisis and political turmoil, had a lower GDP. After 1991, the average real income for an Azerbaijani citizen fell by a factor of 8.2, and hyperinflation reached a shocking 1763.5 percent in 1994.

It must be mentioned that even in the problem-free year of 2004, per capita GDP in Azerbaijan was still only 75% of its 1990 figure. 2005 marked a turning point for Azerbaijan, when its economy demonstrated highest growth rate globally. The decade of 1994-2004 established the preconditions for a critical turning point. During this period, key growth centers were identified, a national modernization model was developed, and the key parameters of the “Azerbaijani Project” were identified.

Which particular circumstances pushed the country to a sustainable development trajectory?

Above all, it was the achievement of political stability. In this context, the coming to power of Azerbaijan’s third president, Heydar Aliyev, was a key factor in this process. It was Heydar Aliyev who managed to achieve what proved the most important thing for sustainable economic development: the mobilization of the country’s political class, overcoming the internal conflicts that were preventing the state structure and general

population from addressing critical strategic challenges. The second factor was the identification of the economic growth paradigm, based on the pre-eminent role of the oil and gas sector.

The signing of the “contract of the century” in 1994 determined the development path of the national economy for many decades, enabling the mobilization of additional resources, and ultimately the move from the “strategy of maintaining” to a “strategy of rapid development”. It would not be unreasonable to argue that until today, the strategy of economic modernization has been based on the priorities identified by President Heydar Aliyev in the early 1990s. Another important factor in this success is the establishment of a new national elite. Heydar Aliyev built up a pool of young managers, graduates of Russian universities, and gave them the opportunity to apply the skills they had learned in recognized universities and higher education institutions such as MGU, MGIMO and MVTU. This was a group of loyal managing staff who returned to Azerbaijan during the country’s hardest times and dedicated their careers to the recovery and growth of the country.

In this context, Aliyev’s qualities as a political leader are particularly pronounced, notably his ability to select staff to implement the

key areas of state policy and create motivation mechanisms which, in those days, did not include financial incentives.

In the mid 1990s, the state did not have sufficient resources to sustain government apparatus, and consequently, those young public service managers were doing less well than many of their peers, who were successful businessmen. It was this cohort of “young statesmen” who built modern Azerbaijan. The final component in the success of Azerbaijani statehood was the ideological mobilization of society, built upon clear goals, objectives and themes of development.

---

*Kazakh and Azerbaijani leaders were the first in the post-Soviet space to use strategic planning as a basis of sustainable development.*

---

In this respect it would be appropriate to compare Heydar Aliyev with Nursultan Nazarbayev, the leader of Kazakhstan. Kazakh and Azerbaijani leaders were the first in the post-Soviet space to use strategic planning as a basis of sustainable development. It is clear that the successful economic reforms that were carried out in Azerbaijan at the beginning of the new millennium were made possible by political stability.

Given these considerations, the assessment by Azerbaijani researcher Nazim Muzaffarli seems very apt. He observes that systemic political stability requires an effective system of economic motivations, but at the same time, political stability needs to be ensured by the political structure of the society. Both of these conditions for transitioning to a new level of development were implemented in Azerbaijan at the beginning of 21<sup>st</sup> century.

National leader Heydar Aliyev laid the foundations for economic prosperity that was driven by revenue from resource sector. The development of the independent national oil strategy was one of the most important areas of economic policy for Azerbaijan. The implementation of the strategy began with the signing of a 30 year production sharing agreement for the joint development of Azeri, Chrag and deep-water Guneshli field in the Azerbaijani sector of the Caspian Sea, between the State Oil Company of Azerbaijan (SOCAR) and a consortium of 12 international oil companies. President Heydar Aliyev’s view on this contract was clear: “While not all of our thoughts are reflected in this contract, I think the proposed version corresponds with the economic interests of the people of the Republic of Azerbaijan today, and in the future. Therefore, I have taken the decision to sign the contract...”

Taking stock of the oil industry of Azerbaijan and taking into account my 25 years of experience in the oil industry, and considering the current real state of the oil industry inherited from the Soviet Union, I took this decision and ordered the signing of the contract. I have taken enormous responsibility and am ready to carry it on today and tomorrow”.

Revenues from the contract of the century were used to finance modernization projects. They helped to build social infrastructure, address regional development issues, and create the preconditions for the transition from a resource-based economy to industrial and innovative development. Under President Heydar Aliyev, a number of documents determining the development of various economic sectors were adopted. These projects are part of the overall plan outlined by the leadership of the country.

One of these fundamental projects was the establishment through presidential decree of the State Oil Fund of the Republic of Azerbaijan (SOFAZ) in 1999. SOFAZ accumulates foreign exchange inflows from oil types of hydrocarbon activities of the international oil companies operating in the country.

The Oil Fund manages the accumulation and efficient use of the

funds received from oil and gas exports, as well as from the financial investments of the fund. Since oil and gas are non-renewable resources, it is important to ensure equitable distribution of resources among generations and to accumulate resources for future generations. In addition, the Oil Fund is used to directly finance significant socio-economic projects. Heydar Aliyev’s strategy determined the priorities of investments in Azerbaijan, which, in 2000, were:

- Expansion and upgrade of oil servicing sectors;
- Food processing;
- Highly efficient infrastructure, in particular in the power and telecommunications sectors.

These tasks have been successfully implemented, clearly demonstrating that there is consistency in the reform process in Azerbaijan.

In this respect, the policies carried out by the current president Ilham Aliyev are a direct continuation of the ideas formulated by his predecessor Heydar Aliyev.

The mid 2000s marked a breakthrough in the energy sector. The Baku-Tbilisi-Ceyhan oil pipeline was launched in June 2006. In the fall of the same year, the Baku-

---

*The Baku - Tbilisi - Ceyhan oil pipeline was launched in June 2006. In the fall of the same year, the Baku-Tbilisi-Erzurum (SCP) gas pipeline started operation. These routes ensured the country's energy security.*

---

Tbilisi-Erzurum (SCP) gas pipeline started operation. These routes ensured the country's energy security. Since 2004, several power plants have been built across various regions of the country, and have fully eliminated the electric power shortage. Azerbaijan has turned into an electric power exporter, and the growing economy has found new resources for effective development.

Regional development programs, personally overseen by President Ilham Aliyev, have been developed. Each region of the country has an individual development program that is based solely on the development of non-oil sectors.

Current priorities include the growth of manufacturing sectors. A number of major projects are currently being implemented. The government of Azerbaijan is making efforts to develop the manufacturing sector, encouraging businesses to innovate. The government uses public investment and stimulates

the private sector to work more actively in the public sector. A unique technopark is being established in Sumgayit, an industrial city near Baku, and efficient aluminium and pipe plants are now operational. The technopark is mainly designed to operate plants and production facilities supporting the power sector. Almost two dozen factories will be located in this area.

The consistency of political and economic policies ensured economic sustainability during the global financial crisis of 2007-2009. Azerbaijan has maintained high growth rates of investments. In 2010, Azerbaijan's economy was ranked the 72<sup>nd</sup> economy of the world by nominal GDP. The Moody Investor Service rating agency confirmed Azerbaijan's long-term default rating at Ba1 and modified its forecast from "stable" to "positive". During recent years, Azerbaijan has been showing highest growth rates of all the CIS countries: from 2003 to 2008 Azerbaijan's GDP rose 2.6 fold, and the poverty rate fell from 45% in 2003 to 9.1% in 2010. Non-oil growth in 2010 was 7.9% compared to 3.2% in 2009.

As scholar Y. Godin noted: "in addition to the extractive industries, Azerbaijan has been intensively developing processing sectors over the recent years. They do not face large-scale capital outflow, like in Russia and Kazakhstan, and they

are developing economic cooperation with the countries outside CIS. Economic growth is additionally driven by the rising purchasing capacity of the population. Azerbaijanis who work, for example, in Russia, earn well by their country's measures and transfer their earnings to their home country".

The economy grew four-fold in real terms over the last decade, exports expanded by a factor of 15, as did the state budget, investment expenses grew by a factor of 96, and strategic foreign exchange reserves increased 31 fold.

At the same time, the country's leadership recognizes the importance of cultural development. Major cultural centers are being constructed in Baku, Sheki, Qabala, Lankaran. A Mugam Center has been built in Baku to celebrate the country's musical and dance heritage.

Azerbaijan has made significant sporting achievements over the recent years. The country is among the top three in gymnastics, and free and classical wrestling. The Heydar Aliyev Foundation and its representative office in Moscow have been carrying out charity events in Azerbaijan, Russia, Ukraine and other countries.

Relations with Russia are important to the stable and sustainable development of Azerbaijan. Currently, Russian – Azerbaijani relations are at a new stage of development. While the geopolitics of South Caucasus raise new challenges, Moscow and Baku are aligning their positions on a number of areas: economy, security, humanitarian affairs, Caspian dialogue. As Russian President Dmitry Medvedev noted in a joint press conference after the Russian-Azerbaijani talks in late 2010, relations between the countries have multiple characteristics and potential for expansion.

Mutual appreciation and respect between the heads of state is an important factor in the development of bilateral dialogue, enabling the two governments to address the most complex and contentious issues in the relationship between Russia and Azerbaijan through personal contact.

In his interview with "Russia-24", President Ilham Aliyev emphasized that there is a "high level of political contact between the parties, through which we make decisions that bring real benefits. Owing to this, we characterize our relationship as a strategic partnership".

The most important international topic in bilateral relations is the settlement of the Nagorno-Karabakh conflict. Following the sign-

ing of the Maiendorf Declaration in November 2008, Russia has undertaken the role of a key moderator of the negotiations between Armenian and Azerbaijani leaders. While the final settlement of the conflict will require significant efforts, the initial results of this mediation mission are already visible. During the Sochi talks in March 2011, an agreement was reached between the parties to exchange prisoners of war, and outlines for the participation of civic diplomacy in the settlement are gradually developing. It goes without saying that this process needs to receive additional impetus in future; however, it is possible to state even now that Russia's role is having a positive impact on resolution of the Karabakh problem.

At the same time, Russia and Azerbaijan are not yet sufficiently engaged in implementing the joint innovative projects, which are necessary for a transition to a deeper, more intensive interaction at a project level. Russia and Azerbaijan are facing the common problems in building an innovative economy. The low share of R&D expenditure and irrational financing arrangements are obvious obstacles. Thus, uniting the innovation capacity of Russia and Azerbaijan is important not only for the practical introduction of modern technology, but, more importantly, for developing

---

*The consistency of political and economic policies ensured economic sustainability during the global financial crisis of 2007-2009. Azerbaijan has maintained high growth rates of investments*

---

competitive scientific and intellectual human resources.

Azerbaijan and Russia are facing the same set of challenges – achieving a new level of competition. The global agenda is changing, and the challenges facing our countries are evolving.

Azerbaijan and Russia are forward-looking countries. The new generation, born after the collapse of the USSR, will define the shape of this new world.