

## **30 years of independence without free enterprise**

### **Interview**

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***At a meeting on August 8, President Ilham Aliyev spoke about the liberalization of the economy in Azerbaijan. The head of the state criticized large state-owned companies such as AZAL and SOCAR, and at the same time, proposed the privatization of many state-owned companies that receive funds from the state budget. "More reforms are needed in the field of privatization. We should have both private and foreign companies been interested in this. Because in some cases, companies apply and their applications are not considered, in some cases, it is extended. Some projects are being implemented, some are not. We must be interested in ourselves. We need to give a business plan to foreign and local investors - there is this area, there is this enterprise, let's privatize it. If a strategic investor invests a lot there, it can be privatized at a symbolic price. If he/she guarantees that he/she will invest a lot here. We can launch these enterprises only in this way," the President said at the meeting. On the same day, the President signed a decree on the establishment of the Azerbaijan Investment Holding as a public legal entity. Is it possible to liberalize the economy and privatize large state-owned companies in Azerbaijan? Economist expert Azer Mehtiyev, head of the Public Union for Support of Economic Initiatives, spoke to ASTNA about this.***

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**- Azer bey, the President spoke about the liberalization of the economy at a meeting on August 8. Do you think it is possible to do this in the present circumstances and under the present conditions?**



- First of all, it is necessary to clarify what the President means by liberalization. Because when you say liberalization in general, it usually means equal rights before the law in the country, the creation of equal conditions for everyone. Equality before the law - means that no one has a different status from the conditions prescribed by law. The most important condition here is a fair and independent judiciary. This has been the issue

most talked about and raised in Azerbaijan for a long time. Because this is the main condition for building a competitive economy. In particular, the protection of property rights, the impossibility of seizing property without a court decision, and so on. These problems were also identified in the Strategic Roadmap for Economic Development, and it was noted that reforms would be implemented in these areas. Unfortunately, despite certain steps taken in recent years, we do not see any change in ensuring these principles, which form the basis of a liberal economy. From this point of view, the foundation of building a liberal economy in the country begins here. This is an approach to the issue from a legal institutional point of view. On the other hand, Azerbaijan is approaching the 30th anniversary of its independence. Unfortunately, normal, free has not been formed in the country so far. There are more businesses of officials in countries. This has led to a severe monopoly on the country's economy. There is no competitive environment. So far, the country has not been able to train entrepreneurs who can operate in a normal, fair competition, which greatly complicates those conditions of liberalization.

**- The President also spoke about the privatization of large state-owned companies (AZAL, SOCAR, ADY), which receive annual assistance from the budget. The proposal sounds very tempting. However, this step will probably not benefit the curators of these areas and the army of officials leading them, and they will create artificial obstacles. What steps do you think should be taken to prevent this? Is it possible to look at this proposal realistically in general?**

- The head of the state sharply criticized the economic principles of large state-owned companies, noting that these companies were very wasteful. However, a long time has passed to talk about these. Even in the 2000s, the issue of long-term management of large state-owned companies in Azerbaijan, attracting foreign investors in the utility sector, was on the agenda, and this process was started. There was even a certain legal basis for this. However, these issues were later forgotten with the inflow of large oil money into the country, and the transfer of control of this sector with the involvement of foreign investors was also forgotten. Even despite the allocation of funds from the state budget, almost no serious steps have been taken to improve the management of these utilities, ie large state-owned companies. Their names were simply changed from "State Company", "State Concern" to Open or Closed Joint-Stock Company. However, these names did not justify themselves in any way. No corporate administration was applied. No serious steps have been taken to establish the transparency and accountability of these companies. These companies have not developed a serious accountability mechanism. On the one hand, there was

no accountability scheme for the use of funds allocated by the state. On the other hand, it was not disclosed where and how the companies spent their revenues. Despite the fact that the managers of these state-owned companies received large salaries, the lack of improvement in management led to the fact that the processes of public procurement and organization of their activities were carried out behind closed doors, which increased opportunities for corruption and embezzlement. As companies developed, tax payments decreased instead of paying more taxes to the state budget. It is true that during the crisis of 2015, companies began to collect more taxes, but this was also temporary. Again, the stabilization of oil prices on the world market has resulted in a decrease in attention to these companies. Every time when oil prices fall, this issue comes up. However, even after the crisis of 2015, various decisions were made to increase the activities of large state-owned companies but we have not yet witnessed a serious step in this direction. The issue of privatization of these companies is also a complicated one. Because the vast majority of these companies have a monopoly place in the Azerbaijani economy. For example, this applies to AZAL, SOCAR, and Azersu. All of these companies are, in fact, areas of natural monopoly. For example, AZAL or Azerdemiryol. Freight and passenger transportation using airport services and railways should be liberal. Numerous operators can operate here. But in our country, all these areas of activity are monopolized by companies. And this monopoly has become an element that serves the development of the businesses of officials. In this regard, state-owned companies have serious problems.

**- The President also said that there are many large areas of destroyed enterprises of the Soviet era in Baku, where new industrial enterprises can be established. How do you assess the realization of this proposal?**

- The territories of several small and medium-sized industrial enterprises, such as mechanical and other types of enterprises, are in place. The question of their privatization or sale to investors is long overdue. In fact, this issue was raised after the 2015 crisis. Here are some issues that need to be addressed. First of all, if we look at the website [privatization.az](http://privatization.az) in Azerbaijan, we can see that several such enterprises have been declared open for privatization, and even investment competitions have been announced. But it is strange that the debts of these non-functioning enterprises have long accumulated. It is as if the state wants to repay those debts to that investor. This is something that is not attractive for investors, especially foreign investors. Because in reality, it is impossible for those enterprises to continue their previous activities. They need to be completely rebuilt and new technologies need to be applied there. In fact, if those enterprises are privatized, there can only be a question of land. It is even questionable whether many enterprises are useful in any form at all. From

this point of view, first of all, there is a need to write off those debts once and for all in those investment competitions. Second, well-known foreign companies in these areas should be attracted to the country. This raises the question of how attractive Azerbaijan is for foreign investors. Within the country, the number of entrepreneurs who can privatize such enterprises is limited. If there are some entrepreneurs, these can only be officials. Only officials have the opportunity to get so much wealth in Azerbaijan. This could be a step that will lead to the concentration of wealth in the name of a smaller group in the country.

**- Although the privatization of large state-owned companies is an attractive proposal, will the written and unwritten laws in the country encourage foreign investors to come to the country?**

- Attracting foreign investors to the country is a special issue. Because foreign investors have been attracted to Azerbaijan for many years, mainly in the oil sector. The oil sector is attractive to investors due to its high profitability. A special legal environment has been developed for investors coming to the oil sector. These are production sharing agreements, each of which is adopted by the Milli Majlis at the legislative level, signed by the President, and acquires the status of an international agreement. Violations of the terms of these agreements are considered in international courts. However, the number of investors in the non-oil sector is very small. And all those investors come to the country under the patronage of government officials by directly contacting them. Only they act by means of this. In fact, they have a monopolistic position in the field in which they come. This is possible due to their relations with officials. However, foreign investors are aware of international indices and ratings about the lack of laws in the country, the lack of protection of property rights in the country, the lack of an independent and fair judiciary, and the prevalence of bribery and corruption in government. From time to time, they witness how government officials loot business from reports on lawsuits in Azerbaijan. When individual ministers are arrested, they become aware of the information about how those ministers caused troubles to business entities. And, of course, in such circumstances, it is difficult for investors to come to the country in the non-oil sector. Indeed, factors such as market size and market growth opportunities also play a role in attracting foreign investors. However, Azerbaijan's geographical location actually allows the market to grow. However, Azerbaijan has not used these opportunities normally so far. Because the level of bribery and corruption at the customs checkpoints of Azerbaijan was so high that even if foreign investors came to the country in these conditions, they were deprived of the opportunity to grow the market. This leads to the small size of the Azerbaijani market, which is not attractive for investors. In this regard, along with improving the legislative

environment, we must resolve the issue of customs once and for all, so that it is possible to establish relations with the world economy. Finally, there is the issue of Azerbaijan's membership in the World Trade Organization (WTO). It is very important for investors that they have the opportunity to freely export their products to the whole world and benefit from international law. At present, Azerbaijan does not have these opportunities. Conditions for attracting foreign investors in Azerbaijan remain very difficult. For this reason, the government has to talk to investors individually. They can usually attract rich businessmen from Arab countries. But attracting foreign investors is not just about attracting money. Our biggest expectation from attracting foreign investors to the country is to bring modern business culture, management, and technology to the country. It is what we need.

**- How is it that large state-owned companies receive assistance from the budget every year, but no one is questioning them about a large amount of property owned by those in charge of them and has not been so far? Why does the government, which wants to build a liberal economy, turn a blind eye to corruption?**

- In general, the issue of corruption in public administration, and especially in large companies, remains serious. Unfortunately, despite the fact that this issue has been discussed for many years, the costs of large companies are growing every year and they receive large sums of money from the state budget. Nevertheless, they are provided with high salaries. However, in return, there have been no mechanisms to ensure transparency and accountability in their activities. Therefore, if we look at the activities of large state-owned companies, either the companies themselves or the people under the management of these companies have created a large number of companies abroad, in offshore zones. It can be said that they carry out their relations through these companies. Most of the revenue goes to companies registered in those offshore zones. The companies themselves make a small profit. This leads to misappropriation of income, diversion, and the spread of corruption. In fact, it results in a huge wealth of the management of a company, who does not have such a large amount of salary. Failure to take action on all this has created a mechanism of irresponsibility. Under these mechanisms, changing company executives does not solve anything. Although the company's management has changed, new ones come and continue the old mechanisms. In this regard, the reform of state-owned companies should be very broad.

**- The President talks about economic liberalism and the privatization of large state-owned companies. But we have experienced this many times.**

**For example, we have witnessed that the state-owned AZAL Bank was secretly privatized by those in power, its name was changed, and it operated under another name. Or it was circulated in all the media that a lot of taxis were recently brought to the country and given to one of the taxi companies at the expense of the state budget. This fact indicates that other taxi companies, which are more competitive and free, will fail. Now, who can guarantee that those in power will not abuse the privatization of large state-owned companies and not privatize them for themselves?**

- The probability of such a risk is very high. Because, in fact, there are very few institutions in Azerbaijan that can accumulate great wealth and capital, except for entrepreneurs, who are officials, and their entourage. There may even be very few entrepreneurs who can participate in the privatization process with their own funds. But it does not mean there is none. If they create a normal competitive environment and keep officials-related entrepreneurs out of such a privatization process in any way, and if talented entrepreneurs are involved in these activities, of course, different processes can take place. However, in general, the privatization of large state-owned companies with the participation of one or two entrepreneurs is unacceptable. World experience shows that such large state-owned companies in the utility sector should always be done through equity, by attracting more investors. That would be truer. Because there must be a large number of investors with a large share. For example, it is important to form not only hundreds of thousands of small investors but also 50-100 shareholders with 4-5 percent shares, so that the division of property becomes an element that expands the opportunity of control. However, in all cases, separate mechanisms must be developed for the privatization of state-owned companies. Even if necessary, separate legislation should be prepared. Because these are complex processes. It is not right to privatize them by general legislation like the privatization of some small enterprises.

**- On August 8, the President also signed a decree on the establishment of Investment Holding as a public legal entity. Do you think this decree is enough to liberalize the economy, privatize large state-owned companies, and attract foreign investors to the country? In general, what is the purpose of establishing an Investment Holding? And what problems must be solved in order to liberalize the economy and create conditions for foreign investors to come to the country?**

- Back in the days, especially after the 2015 crisis, certain decisions were made on the privatization of non-core enterprises within state-owned companies. The Cabinet of Ministers approved a list of state-owned

enterprises banned from privatization in the medium term. The decision includes about 50 companies, which are not expected to be privatized in the medium term. In the current situation, in reality, the creation of the Investment Holding is aimed at the management of these companies and the improvement of the mechanisms. Investment Holding must monitor the activities of all those companies. It must monitor the establishment of their transparency and accountability. It must control the establishment of corporate administration in those companies. Such practices have been applied in various forms in different countries around the world. In Azerbaijan, the government is talking about the privatization of state-owned companies, but on the other hand, is taking other steps. For example, in 2015, due to loans from the International Bank of Azerbaijan, there were funds for the construction of many companies, both in the country and abroad. As entrepreneurs could not pay those funds, those companies were declared bankrupt, and instead of attracting foreign investors by selling them, the Azerbaijan Industrial Corporation was established to control them. That corporation is engaged in the rehabilitation of those companies. But there has been no report on their activities so far, whether the corporation has achieved its goal or not. If they succeed, is it possible to privatize and sell those companies? Is it possible to recoup the costs incurred by the state and attract additional funds for their rehabilitation? This was an example. If that example has not justified itself, what will the creation of a new version of it - Azerbaijan Investment Holding - do now? If the Azerbaijan Investment Holding is again run by officials appointed by the President, there will be no results. Because the idea of an official is not a business idea. As long as a business in Azerbaijan is governed by the idea of an official, there will never be a normal competitive environment and a normal business. On the contrary, this will not go far beyond the newly established ministry or committee.