

# EXTERNAL CAPITAL AND POLITICAL STRUCTURES: THE CASE OF AZERBAIJAN

*Oksan Bayulgen*  
*University of Texas at Austin*

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## **Introduction**

Interest in the extensive natural resources of post-communist states coupled with the hopes of economic and political development attached to it, have brought to surface the long standing debate about the effects of external capital inflows on political structures. Most of the political economy literature has shown the effects to vary by *type* of external capital; such as international loans, development aid, foreign direct investment, equity investments, labor remittances, oil rents, etc. (Stallings 1993, Haggard and Kaufman 1993, Mahon 1995, Maxfield 1997, Chaudry 1997).

However, what is often missing from these analyses is the role of pre-existing institutional structures which mediate the local effects of external capital. The institutional relationship in existence before a state is integrated into capital flow networks plays a determining role in the state's ability to allocate resources in the service of coherent economic policies and development. Therefore, the question I seek to answer in this paper is whether there is something unique about the post-soviet transition; in other words, whether or not the institutional design of the Soviet past has stunted the institutional capacities of these states as they prepared to utilize this external capital to boost their economic and political developments.

Among all the former Soviet republics, Azerbaijan, which based its projections of growth on its extensive oil resources, is especially vulnerable to the effects of foreign capital that characterize the petro-states. However, whether or not Azerbaijan will become a petro-state depends on the pre-existing institutional capacities of its state. Thus, I make two arguments in this paper. First, the institutional capacity of the Azerbaijani state--measured by its ability to extract and deploy resources, enforce property rights, and resist the demands of rent-seekers-- has been shaped both by the unique legacies of its Soviet past and by the magnitude of the task of state-building. Second, the Azerbaijani state's institutional capacity is likely to be further weakened once oil rents start flowing into the economy.

## **Literature Review**

According to the literature on petro-states<sup>1</sup>, inflows of external capital in the form of oil rents have a significant impact on the political structures of oil exporting states (Mahdavy 1970, Gelb 1986, Hughes 1975, Delacroix 1980, Katouzian 1981, Shafer 1994, Chaudry 1997, Karl 1997). Three main points can be summarized from this literature. First, dependence on oil revenues produces a distinctive type of institutional setting, which expands state jurisdiction and weakens accountability. This is because oil revenues precipitate the decline of the extractive and regulatory institutions while expanding the distributive ones. "Unlike welfare states, which are redistributive, rentier states do not exist by extracting surplus from the local population because oil revenues enable governments to stop taxing altogether"<sup>2</sup> Hence, with no revenue-gathering motive, these states are financially autonomous from their citizenry and therefore are not accountable to them<sup>3</sup>. In addition, because oil rents and revenues are highly centralized and accrue

directly to the state, the role of the public sector and the distributive institutions of the state are enhanced. This rapid expansion of jurisdiction is also accompanied by the intensive centralization of resources in the executive branch where decisions about petroleum are made.

Second, the massive capital and organizational requirements associated with exploiting oil affects the power of the domestic bourgeoisie. "Countries that export petroleum as their main economic activity generate specific types of social classes, organized interests, and patterns of collective action that are linked directly to the state and that benefit from oil rents"<sup>4</sup>. These states not only reorganize, encourage or disband existing occupational groups but they also actually create entire sectors<sup>5</sup>.

Lastly, dependence on oil rents creates obstacles to development. "The high barriers to change arising from their leading sector produce inertia: both organized interests and state bureaucrats tend to fight to maintain the status quo and to prevent modifications"<sup>6</sup>. As a result, oil rents have the effect of destroying the institutional mechanisms required to carry out economic reforms.

### **The Argument**

Although this literature has produced scores of explanations for the resource curse, it has rarely distinguished the significance of different pre-institutional settings. In their comparative analyses, scholars tended to focus more on the convergence of the experiences of petro-states in managing the entry of the petroleum industry and handling the subsequent booms. They have rarely explained the variation in their performance. The case of Norway has been regarded as an exception with its strong preexisting institutions and democratic decision-making in providing a type of 'creative resistance' to the overwhelming impact of the bonanza that was simply unavailable to the developing countries<sup>7</sup>.

The lack of a systematic comparison of the pre-oil institutional settings of oil exporting states in the literature becomes even more problematic with the appearance of former Soviet republics as independent states with extensive natural resources. What clearly distinguishes the transition from communism is its institutional point of departure. "The unique symbiosis of the state with society and the economy" has constrained the efforts to build the rule of law, democracy or competitive markets in the newly independent states<sup>8</sup>. The institutional capacity of the state vis-a-vis the society is certainly different in a totalitarian regime than in an authoritarian one that recognizes private property, has market economies and does not fully destroy the autonomy of its respective society. This paper argues that, two states with different pre-institutional structures and regime types can experience differences in the effects of oil rents. Among oil-exporting states, there may be similarities in the 'structuration of choice' as the petro-state literature predicts, but the degree of 'petro-stateness' may differ depending on the institutional capacities of these states. This paper is an attempt to illustrate this shortcoming in the literature and to provide a case study for post-Soviet petro-states.

### **The Case Selection**

Azerbaijan provides an especially suitable setting to study this relationship between external capital and political structures. First of all, given its potential oil resources, external capital inflows in the form of oil rents are expected to form the main source of revenue for this newly independent state. Being one of the oldest oil producing regions of

the world, Azerbaijan's proven oil reserves are approximately 3 billion barrels. Some experts estimate its ultimate potential to be as high as 40 billion barrels and argue that the Caspian Sea is one of the largest oil reservoirs in the world after the Middle East<sup>9</sup>. Oil sector activities currently under way are concentrated on the exploration and development of oil fields and are financed by oil companies via foreign direct investment. To date 9 production sharing agreements have been signed and oil-related inflows moved from zero in 1994 to about US \$1/2 billion in 1996. Of this amount US\$ 64 million was in oil bonus payments- currently the main source of government revenue from oil production<sup>10</sup>. However, according to rough estimates, production which has barely started could increase to around 85% of total exports by 2005 and could contribute more than 50% of total budgetary revenues<sup>11</sup>.

Second, Azerbaijan depends on external capital inflows as the engine for its economic development. The disintegration of the SU led to a breakdown of the all union Soviet market, which had negative repercussions for the economies in all of the newly independent states. Disruption of trade links was in fact a principal reason for the very sharp fall in production, which was particularly intense in Azerbaijan. The economic slump resulted directly from the fact that this republic was strongly oriented towards the production of raw materials and thus heavily dependent on the other Soviet republics for other goods. As a result of this macroeconomic instability inherited from the Soviet state, oil has come to dominate the economy and has become the industry on which hopes for a richer future are pinned.

However, given the onerous legacies from the past and the awesome tasks involved in state building, early expectations about the oil wealth and hopes of a speedy turnaround in economic and political development are unrealistic. In order to prove this point, in this paper I will analyze the capacity of the Azerbaijani state in terms of its extractive, distributive, and regulatory institutions. More specifically, I will analyze the impact of the Soviet legacy and state-building on the ability of the Azerbaijani state to extract and deploy resources, enforce property rights and resist the demands of rent-seekers. In the final analysis, it will be clear that early symptoms experienced by petro-states are in evidence well before the oil has started flowing in earnest.

### **The Independent Variables: The Soviet Legacy and State-Building**

At the time of independence, the Soviet republics were quasi-states with their own presidents, prime ministers, councils of ministers, national and local legislatures and large social-welfare bureaucracies. However, the Soviet republics' ready-made government apparatus created a false expectation that these newly independent states had the structures in place to meet the challenge of development. In fact, "the existing political, economic and social institutions have been as much of a hindrance as a help"<sup>12</sup>.

The former Soviet republics have inherited not only economic hardships such as specialized rather than diversified economies, technologically backward capital stocks, massive environmental degradation, large interpublic trade dependencies and protected enterprises and populations but also political institutions that entailed near-universal state ownership of property, near absence of a financial system capable of carrying out economic rather than accounting functions and a civil bureaucracy imbued with an autocratic and interventionist mentality<sup>13</sup>.

The scale of these enduring legacies is especially great in post-Soviet states due to the fact that concentration of political and economic decision making in Moscow offered local elites in these newly independent states little opportunity to gain relevant experience and made the state-building even more difficult. Moreover, the lack of a constitutional design outlining the rights and responsibilities of the levels of government has undermined public finance and the state's ability to supply services. Such a weak institutional capacity has created an environment conducive to corruption and organized crime.

Against this backdrop, a few persisting elites from the communist era have consolidated their power and set the rules for the economic and political development in

these states. Guillermo O'Donnell's concept of 'delegative democracy' is useful to capture the dynamics of political development in these post-Soviet republics<sup>14</sup>.

In Azerbaijan, Aliev has attempted to construct an aura of democratic legitimacy while at the same time acquiring the machinery of a presidential dictatorship<sup>15</sup>. President Aliev, who was the leading Azeri communist and the 4<sup>th</sup> ranking leader in the SU during the Brezhnev era came to power in 1993 when the Popular Front government of Elchibey fell from power. Since then, the Azerbaijani government has granted broad powers to Aliev and the parliament, with little opposition, has been following the initiatives of the president. In economic life, the decrees of the president become law, rubberstamped by the parliament. In essence, the decision-making apparatus is almost exclusively controlled by the president and a few elites around him.

#### **Dependent Variable: The State Capacity**

Defining state capacity is often a contentious issue in the political economy literature. Statists and neo-Marxists equate state capacity with the ability to act autonomously from social forces- that is, with a government's ability to achieve the goals it sets for itself. Conversely, organizational theories reject the reduction of state capacity to a question of size and jurisdiction and use the coherence of the bureaucracy, the organizational forms adopted by both the public sector and private interests and the predominant symbolic notions of the state itself as indicators of state capacity. How one defines and operationalizes this concept have important consequences for categorization of states.

Here, I borrow the definition utilized by Terry Lynn Karl (1997) in her analysis of petro-states. Accordingly, state capacity is understood as "the sum total of a state's material ability to control, extract and allocate resources as well as its symbolic or political ability to create, implement and enforce collective decisions"<sup>16</sup>. Capacity is thus an aggregate measure of the strengths or weaknesses of the regulatory, extractive and distributive institutions of the state. Therefore, in order to show the effects of the Soviet legacy and state-building on the capacity of the Azerbaijani state, I will now analyze the rule of law and corruption as indicators of regulatory capacity; levels of taxation as an indicator of extractive capacity; and government spending and credit allocation as the indicators of the distributive capacity of the Azerbaijani state.

#### **The Regulatory Capacity:**

##### *The Rule of Law*

The legal framework inherited from the Soviet Union is unsuitable for dealing with the demands of capitalism. Regulation is characterized by weak administration and a lack of transparency. Although necessary laws are being adopted under the guidance of the World Bank and IMF, Azerbaijani laws are often vague and take on a meaning only through implementing decrees and regulations. Importantly too, since there is no official gazette, regulations are not known to everybody. There are often differences between policies established by the government and procedures followed by executive agencies<sup>17</sup>. Furthermore, there are no effective means for enforcing property rights and contractual agreements. Officially government does not interfere in the court system but in practice courts are not independent<sup>18</sup>.

##### *Corruption*

The regulatory institutions are not only weak and ineffective but they are also contaminated with corruption. Graft is pervasive at every level of the government, though at the top it is difficult to prove.

However, little doubt exists that political elites live rather better than they could on their official salaries (which is around \$600 a month for a minister). Mid-ranking corruption is far more formalized. In Azerbaijan, virtually all public positions that involve the collection of money must be bought. The job of a tax inspector, for instance, might cost about \$50,000 up front<sup>19</sup>. Ranking compiled by the EBRD suggest that Azerbaijan is the fifth most corrupt country in the region but other sources disagree on the order, claiming that oil-rich Azerbaijan is even more prone to corruption than the rest. (Table 1)

In part, corruption is a legacy of the old Soviet regime. In its declining years, the communist system lived on bureaucratic fiddling. In addition, the transition to a market economy without the necessary regulatory institutions has led to a burgeoning of corruption. Factories with no clear owners employ numerous phantom workers, companies with no markets resort to complex barter deals, with every party taking a cut and state banks with no shareholders dole out credit to friends.

### **The Extractive Institutions:**

#### *Taxation*

Corruption is not only a phenomenon in the regulatory institutions of the state but also takes place within the extractive institutions. According to EBRD, throughout the former Soviet Union “taxation is one of the biggest problems facing foreign investors”<sup>20</sup>. Unfair and unpredictable tax regimes encourage tax avoidance, which in turn breeds corruption. Much of the corruption could thus be viewed as an alternative tax system.

In addition to the unpredictability of the tax regime, low levels of tax collection- a characteristic attributed to rentier-states- also depicts the weak extractive capacity of the Azerbaijani state. In terms of fiscal revenue, Azerbaijan has reached a low of 17.6% of GDP in 1995 and has slightly increased to 19.7% in 1997<sup>21</sup>. Of this amount, the indirect taxes (VAT, excises and customs duties) comprise the 7.2%, whereas the direct taxes comprise 5.1%. Royalties on oil production were only introduced at the end of 1995 and are now making a significant contribution to revenue. Other revenues, consisting of land and property taxes and non-tax revenues including grants from the EU and profits from the central bank have declined in importance during the period 1995-97 (Table 2). Hence, even before the inflow of oil rents, fiscal accountability which creates a separation between public and private in state income is very low in Azerbaijan. Such a fiscal structure delays the development of a modern consciousness of the state and contributes to the perpetuation of traditional concepts of authority as the personal patrimony of the ruler.

An analysis of the regulatory and extractive institutions of the state depicts the weak accountability and authority of the Azerbaijani state. Lack of a transparent regulatory system and fiscal accountability limits its ability to penetrate society in order to change actors’ behavior, to develop and implement comprehensive, autonomously determined policies and to place issues of purpose above the tug and pull of political pressures. Despite its weak accountability and authority, its jurisdiction, meaning its scope or degree of intervention in the economy, has been extensive since independence. Consequently, there already exists a gap between the jurisdictional role of the Azerbaijani state and weak mechanisms of its authority. Fiscal dependence on oil revenues in the future can only work to intensify this gap.

#### *The Distributive Capacity:*

The unusually large role of the state vis-à-vis civil society in the former Soviet republics cannot only be attributed to late development (Gercshenkon, 1962), but should also be understood in light of the legacy of the command economy and ‘social bargain’

between the Soviet state and the society. During the Soviet period, with no private property, everything belonged to the state and all forms of development were initiated by the state. The lack of entrepreneurial skills and capital to bring about a bourgeois class in the newly independent states has made state intervention in the economy ever more necessary. Given the already strong role of the state in the economy, as measured by the level of government expenditures and credit allocation, the massive capital and organizational requirements associated with exploiting oil will in the future have the dual effect of further weakening the domestic bourgeoisie while simultaneously thrusting the state even further onto center stage.

### *Government Spending*

The transparency and efficiency of the public sector is vital for an effective government anywhere but is all the more so for natural-resource rich countries. To ensure that oil revenue is not wasted on immediate consumption or inefficient projects, governments must plan carefully. Although Azerbaijan has started discussing public-sector reforms with the World Bank, for the moment its public sector books are far from transparent. For example, SOCAR, the state oil company, formally consists of 17 companies with 17 sets of accounts. They are not consolidated, leaving plenty of loopholes for money to disappear<sup>22</sup>.

As for government expenditures, so far the IMF has ensured that the early oil bonus payments and revenues go into a special account at the central bank, and only a portion of it is used to finance the budget deficit while the balance remains overseas and forms part of international reserves. However, the current arrangement is viewed as deficient for several reasons. In particular, this account has no formal operating rules which may lead to problems in determining what income to allocate to the account, deciding how the funds are invested and deciding how and when to spend these resources. Only the president can authorize the use of these funds, and ownership of the funds is not clearly specified<sup>23</sup>.

An analysis of the pattern in government expenditures so far can tell us much about the government machinery that will manage the oil wealth in the future. In order to contain the large fiscal deficits that developed during 1992-94, when general government revenue sources declined from 51% of GDP to 34% of GDP, Azerbaijan focused on compressing expenditures and raising additional revenues. Although the cash fiscal deficit fell from a high of over 15% of GDP in 1993 to under 2% in 1997, the reasons for this success can be found in the decreasing costs of the conflict in Nagorno-Karabakh together with a surge in foreign investment and not so much in the shrinkage of the state<sup>24</sup>.

In Azerbaijan, expenditure as a percentage of GDP was halved in 1995 compared to 1994 and reduced further in 1996. The amount spent on wages and salaries and goods and services was broadly stable during 1994-96, but rose sharply in 1997, while subsidies and net lending have declined, reflecting the elimination of subsidized communal services for certain sectors of the population (Table 2). However, this decline in subsidies was offset by the introduction of a compensation package and additional cash allowances to targeted groups.

Although the degree of government control in the economy can be depicted by an analysis of government expenditures, the patterns of ownership and control of the financial sector can offer better indicators of the structural power of private capital and

the jurisdiction of the state in Azerbaijan. This is mostly because the structure of the financial system reflects the alternative sources of financing available for the private sector and the degree of government control in the economy.

#### *Credit Allocation: The Banking System*

In the socialist framework, the banking system was used mainly for distributing, collecting, and controlling the flow of resources based on central plans. Thus banks did not perform the functions associated with banks in a market economy- in a centralized planning system, banks were mainly extensions of different government ministries, performing budgeting, accounting, treasury and taxation functions.

Today to the extent that there is any recognizable financial system, it is of the French statist variety in Azerbaijan. The banking in Azerbaijan represents a credit-based system in which the allocation of funds is left to executive discretion. Given the absence of capital markets, firms must turn to lending institutions for the funds they need. Credit is the core of the system of corporate finance and the banking system's ability to extend industrial credit is therefore crucial<sup>25</sup>.

The attempts to reform the banking system in Azerbaijan have been very slow and painful and the dependence on foreign capital is likely to contribute to further resistance to financial liberalization. One needs to analyze therefore 1) the ownership and the degree of concentration of the commercial banking system and 2) the degree of financial debt to depict the Soviet legacy of state intervention.

#### 1) Ownership and Degree of Concentration

The banking system in Azerbaijan is characterized by both concentration and fragmentation. Although the number of banks has declined significantly in recent years- from 210 in 1995 to 99 in 1998-, the structure of the system has changed very little. As of 1998, 4 out of 99 banks were state-owned, 10 were majority owned by state enterprises, 13 were majority foreign-owned and the rest were controlled by private investors<sup>26</sup>. The state-owned banks- the Agroprom Bank, the Prominvest Bank, the Savings Bank and the International Bank- accounted for 83% of total banking assets, 83% of total outstanding loans, 82% of deposits, 67% of branches and 70% of employment in the banking system in 1996 (Table 3). While all licensed banks are free to enter any authorized activity, the state-owned banks specialize in certain sectors (industry, agriculture) and services (savings depository and international transactions).

Many of the domestic private banks in Azerbaijan are essentially vehicles for financing particular enterprises and thus provide a limited banking service and do little to mobilize deposits. Furthermore, the licensing regulations, which limit the number of branches a new bank may open, give advantage to "old," mainly state-owned banks which created a network before the regulation was implemented<sup>27</sup>.

In sum, rehabilitation and privatization of the state-owned banks has not yet occurred in Azerbaijan. The injection of credit into the private sector through state banks has given the government complete control of fixed investments in industry, agriculture and construction. This persistence of state dominance and resistance to reform is likely to be reinforced by the control of huge sums of foreign capital that will be injected into the economy in the future.

#### 2) Financial Depth of the Banking Sector

Azerbaijan's measures of financial depth are among the lowest of transition economies. Broad money as a percent of GDP declined from 79% in 1991 to 14% in

1995- the comparable ratios for OECD and the advanced reformers among transition economies were 72% and 50% respectively. In addition local currency outside banks as a percent of Manat broad money has more than doubled- from 30% in 1992 to 63% in 1995. Cash transactions predominate as reflected in low levels of Contract Intensive Money (CIM)<sup>28</sup> Furthermore, domestic credit as a percentage of GDP fell from 36% in 1993 to 13% in 1995, with only 5% representing domestic credit to the private sector. Finally, the level of manat deposits has remained virtually unchanged over the past year around 1% of GDP<sup>29</sup>.

All of these statistics clearly indicate that banks suffer a lack of trust, mostly due to the use of banking and payments systems as instruments of control by the authorities, the fragility of the banking system and the regulations limiting cash withdrawals<sup>30</sup>. Massive injection of foreign capital into the economy is likely to reinforce extensive state control of fixed investments, leaving a marginalized role for the commercial banking system. Such low levels of financial intermediation has appeared even more problematic in Azerbaijan, which lacks alternative financial institutions such as private pensions, investment funds, mutual funds or stock markets. The lack of stock markets and portfolio investment is especially detrimental to the development of a private sector which is left with no other alternative sources of financing other than government-controlled lending.

#### **Conclusion**

The effects of oil rents on the political structures of oil-abundant states are accepted without much dispute in the political economy literature. However, what is often ignored is that these effects are distinguished by the institutional relationships in existence before these countries are integrated into capital flow networks. The pre-oil institutional setting has become even more important with the appearance of post Soviet states on the world stage. The totalitarian regime and the institutional legacies of the Soviet state need to be taken into consideration to better speculate on the future effects of oil rents in these newly independent states. Consequently, this paper has attempted to illustrate the demand for a theoretical framework that would encompass a wide range of cases with different institutional backgrounds. A further systematic research project comparing pre-oil institutional settings to explain the variation in the responses of petro-states is needed to illustrate this institutional perspective.

The fact that the approach used in this paper is not necessarily path-dependent merits emphasis here. In other words, the future institutional trajectories of these states are not already ordained by the past. The legacy of the Soviet state is a necessary but not a sufficient condition to predict the outcome. An analysis like this one only proves to us the daunting tasks that these states face during their political-economic transformation. The institutional legacies cannot be overcome overnight but it does not mean that they will never be overcome. The picture becomes gloomier however, as we insert the intervening variable of oil rents in some of these states such as Azerbaijan. The resource curse depicted in other petro-states will only work to weaken the capacity of the state by expanding its jurisdiction and wearing away its accountability. It will further destroy the institutional mechanisms required to carry out economic and political reforms.

With only early production in progress and relatively little accumulation of wealth, it is still too early to draw a conclusion in Azerbaijan. Furthermore, the recent fall of oil prices to \$11.13 per barrel brings into question whether or not international oil companies will continue to invest large sums of money into these oil fields, and whether

or not Azerbaijan will ever be able to reach the projected export capacity. Moreover, some sources argue that the estimated oil reserves of the Caspian region is very much overrated and that expectations of extensive resource wealth have no realistic basis.

Based on the study of the institutional capacity of the Azerbaijani state, one can almost argue that despite what would seem logical, it is for the better that oil prices are falling. Less dependence on easy money may pressure these governments to devote themselves to more economic and political reforms. Hence, whether or not low oil prices will be a blessing or curse remains to be seen.

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Public Information Notice: IMF Concludes Article 4 Consultation with Azerbaijan, 1998  
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## Notes

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<sup>1</sup> According to Terry Lynn Karl in *The Paradox of Plenty: Oil Booms and Petro-States*, petro-states can be considered a special subset of mining states. The natural characteristics shared by all petro-states are 1) dependence on a single resource, 2) dependence on an industrial sector that is highly capital-intensive and an enclave, 3) reliance on a primary commodity that is depletable, 4) dependence on a resource capable of generating extraordinary rents, and 5) the fact that mineral rents accrue directly to the state.

<sup>2</sup> Mahdavy, H., "*The Patterns and Problems of Economic Development in Rentier States*" in M.A. Cook, ed., *Studies in the Economic History of the Middle East*, London, Oxford Univ. Press, 1970

<sup>3</sup> Chaudry, Kiren Aziz, *The Price of Wealth: Economies and Institutions in the Middle East*, Cornell Univ., 1997

<sup>4</sup> Karl, Terry Lynn, *The Paradox of Plenty*..., p.16

<sup>5</sup> Chaudry, Kiren Aziz, *The Price of Wealth*..., p.26

<sup>6</sup> Shafer, D. Michael, *Winners and Losers: How Sectors Shape the Development Prospects of States*, Ithaca, N.Y.: Cornell Univ.Press, 1994

<sup>7</sup> Karl, Terry Lynn, *The Paradox of Plenty*..., p.216

<sup>8</sup> Kaminski, Bartłomiej, "*Introduction*" in Bartłomiej Kaminski (ed) *Economic Transition in Russia and the New States of Eurasia*, 1996

<sup>9</sup> *Azerbaijan: Economic and Trade Overview*, 1997, BISNIS

<sup>10</sup> *Azerbaijan Republic: Recent Economic Developments*, IMF Staff Country Report No. 98/83, Aug.1998. It is estimated that oil related FDI over 1998-2005 could be in the range of US\$10-15 billion. However, there is considerable uncertainty attached to the future development of the export capacity as well as to the prospects for international oil prices. Considering the drop of oil price to \$11.13 recently, such projections about the amount of capital that will be invested in this industry look too optimistic.

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<sup>11</sup> According to IMF Staff Country Report, by way of comparison the shares of oil exports in total exports in Kuwait, Oman and Norway are 94%, 92%, and 45% respectively. As for the share of revenue in total budgetary revenues, they are 73%, 78% and 22% respectively.

<sup>12</sup> Olcott, Martha Brill, "*The Caspian's False Promise*," Foreign Policy (Summer 1998), pp.95-112

<sup>13</sup> Schroeder, Gertrude, "*Economic Transformation in the Post-Soviet Republics*" in Bartlomiej Kaminski (ed) Economic Transition in Russia and the New States of Eurasia, 1996, p.12

<sup>14</sup> Guillermo O'Donnell argues that 'delegative democracy' is one which meets the formal requirements of a democracy but whose actual practice resembles that of an authoritarian state. It is grounded on a basic premise: the elected president is entitled to govern the country as he sees fit, with little or no regard to other institutions that may try to check or limit his power. See O'Donnell, G., "*Delegative Democracy*," Journal of Democracy, 5 (1), 1994, pp.55-69

<sup>15</sup> Kubicek,Paul "*Authoritarianism in Central Asia: Curse or Cure*," Third World Quarterly 19(1), 29-43, 1998 March

<sup>16</sup> Karl, The Paradox of Plenty...p.45

<sup>17</sup> Country Commercial Guide for Azerbaijan, BISNIS, 1998, p. 12

<sup>18</sup> Ibid.

<sup>19</sup> Central Asia Survey, The Economist, Feb.7<sup>th</sup> 1998, pp. 3-18

<sup>20</sup> Ibid.

<sup>21</sup> Azerbaijan Republic:Recent Economic Developments, IMF Staff Country Report No.98/83, August 1998

<sup>22</sup> "Central Asia Survey," The Economist... , p.15

<sup>23</sup> Azerbaijan Republic: Recent... , p.55

<sup>24</sup> Ibid.

<sup>25</sup> Zysman, John, Governments, Markets, and Growth: Financial Systems and the Politics of Industrial Change, (Cornell:1983), Ch.2

<sup>26</sup> Azerbaijan Republic: Recent Economic Developments, IMF Staff Country Report No.98/83, Aug.98

<sup>27</sup> Ibid.

<sup>28</sup> Contract-Intensive Money(CIM), as explained in Lewis W.Snider, Growth,Debt,and Politics,1996, is the ratio of non-currency money M2 (minus the money held outside banks) divided by the total money supply. CIM will be low, as in Azerbaijan with 47%, where institutions are highly informal, i.e. where contract enforcement and security of property rights are inadequate, and the policy environment is uncertain.

<sup>29</sup> Azerbaijan, Financial Sector Review,1997, Country Department III, Europe and Central Asia, The World Bank Group

<sup>30</sup> Ibid.