

EBRD Country Strategy Comments

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CEE Bankwatch Network comments on the draft EBRD strategy for Azerbaijan

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CEE Bankwatch Network's mission is to prevent environmentally and socially harmful impacts of international development finance, and to promote alternative solutions and public participation.

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CEE Bankwatch Network welcomes the opportunity to comment on the draft EBRD Country Strategy (CS) for Azerbaijan and is looking forward to see how the EBRD takes our comments into account. We hope that the issues we raise will be reflected in concrete changes to the strategy.

Overall we agree with the bank's aim of supporting the diversification of the Azeri economy. However the draft strategy is **missing an analysis of the clear social and environmental development outcomes that the EBRD seeks to achieve** over the strategy period and the concrete impacts on people's lives that are expected.

We agree with the EBRD's statement that *"the government's human rights record is poor and many serious shortcomings are reported, most notably in the area of freedom of the media and the freedom of expression"* (p.28) and we also emphasize that, as noted on p.28, the overall media environment has worsened in recent years and that criminal defamation is limiting media freedom."(p.28)

We believe that the EBRD's strong message to the Azeri government regarding the above mentioned issues in the CS may help to bring changes and improvements.

The EBRD notes that *"...the latest ENP progress report notes that more efforts are required to implement existing strategies and to enhance monitoring and enforcement."* (p.10) Thus, we hope that in the Bank's operations and among its clients *"The Bank will ensure that all operations in Azerbaijan conform to the Bank's Environmental and Social Policy as well as ILO and national labour standards."*

The Bank's priorities for the strategy period

Financial sector

"The Bank's main transition objective in the financial sector will be to strengthen financial intermediation to ensure efficient financing of the private sector particularly SMEs and MSEs including in Azerbaijan's regions." (p.18)

As stated elsewhere in our communications with the EBRD, we believe that in principle

financial intermediation can be a useful tool for reaching MSMEs, provided it is clear that the financing benefits socially and environmentally beneficial activities. However so far the general public has no insight into who the final beneficiaries are of these operations or what development impacts have been attained. It would be possible and desirable to show which sectors and which sizes of business have benefited from sub-projects and what the average size of financing has been, as well as publishing in advance any planned sub-loans that would have been categorized as environmental category A or B had they been direct lending projects by the EBRD. Efforts need to be made to support forms of intermediaries such as co-operative banks and credit unions, and to ensure that EBRD standards are rolled out across banking operations. This is in order to avoid situations where EBRD financing is used for less environmentally and socially dubious projects but the intermediary may use its other financing to support projects that the EBRD standards would not allow.

Transport and MEI Sectors

“A presidential decree established Azerbaijan Railways as a state-owned closed joint stock company in July 2009. This new company is expected to commercialise its activities and introduce private sector participation in a number of railway services such as passenger and freight transport.” (p.16)

“In the infrastructure sector, the Bank is interested to finance urban transport, solid waste and water supply and sanitation projects. Where appropriate the Bank will seek to support private sector participation in urban transport and solid waste management including through ETC instruments. Projects in the municipal sector are likely to require substantial support from the local and national authorities to introduce necessary sector reforms. The Bank is currently discussing with Ganja municipality to structure an urban transport project. If successful the project could be replicated in other regions.

The Bank is also interested to finance the new shipyard in Baku as well as other transport related infrastructure.” (p.20)

The first issue here is that the EBRD does not lay out

almost any details about what it wants to achieve in the transport and MEI sectors. The **Bank should state clearly its aims in the sectors and what these mean for the people who use the services** and for the environment.

Secondly, and on a related issue, the EBRD in the second statement states its intention to support private sector participation in public services. **We would like to emphasize the need for proper evaluation and analysis of whether private sector participation is the most appropriate route**, taking into account the mixed experience of private sector participation in public services in Central European countries, where it was already introduced. In order to increase the effectiveness of public services in transition countries, **the EBRD should also consider public-public partnerships.**

Energy

The EBRD admits that in Azerbaijan, *“The Bank’s transition impact in the energy sector was moderate till now. In the natural resources sector the Bank participated in the financing of the construction of the BTC pipeline and the related development of Phase 1 of the Azeri, Chirag and deep water Gunashli (ACG) offshore fields in the Caspian Sea. According to an independent valuation conducted during the strategy period, the project objectives were only partly achieved due to the limited progress on the Regional Development Initiative (RDI) which aimed to support the economic development of the communities living alongside the BTC pipeline.” (p.6)*

However the Bank should recognize that the so-called “limited progress” in supporting the BTC affected communities is not just due to the just vaguely formulated RDI, but due to the overall nature of the oil and gas infrastructure development model promoted by the Bank, which mainly benefits multinational companies and undemocratic governments.

The EBRD’s significant investments in the Azeri oil and gas sector (BTC pipeline, Chirag, Azeri, Guneshli Oil field, Sha Deniz gas field etc.) in recent years resulted in extremely high GDP growth in Azerbaijan combined with extremely high inflation levels for ordinary Azeris. In

addition, the global economic crisis represents a challenge for Azerbaijani economy development as oil prices remain below their mid-2008 highs, highlighting Azerbaijan's reliance on energy exports and the lackluster attempts to diversify its economy. In 2009 the government continued to rely on financial transfers from the State Oil Fund to bridge its budget shortfalls. In general, these investments do not support Azerbaijan in making progress on instituting market-based economic reforms, while pervasive public and private sector corruption and structural economic inefficiencies remain a drag on long-term sustainable growth. The major obstacle impeding Azerbaijan's economic progress is the need for non-oil sector development.

With this in mind it is welcome that the Bank aims to support the fact that "To reduce Azerbaijan's dependence on oil and gas the government has made *economic diversification a cornerstone of its development strategy.*" (p.1) To achieve that goal the EBRD underlines the potential of the Azeri agricultural sector.

"The Bank will continue to pursue investment opportunities in all enterprise sectors to support the development of Azerbaijan's non-oil economy. Given the potential of Azerbaijan's agricultural sector and its importance in terms of regional development, the Bank will place a special emphasis on the agribusiness sector." (p.17)

Despite this recognition and the intentions stated in the EBRD Country Strategy, in reality the controversial investments of recent decades look set to continue. The Bank openly states that it "is ready to consider contributing to the funding of the Nabucco Gas Pipeline Project" (p.3) and "mobilise co-financing for this strategic energy security project" (p.20).

This reflects an intention to significantly invest in the natural energy resources sector, that contradicts the objective of the development of diverse regional economies and putting efforts into support for renewable energy sources and energy efficiency improvements. It should be also noted that the Bank's intention clearly contradicts the European Parliament's

November 2007 resolution on trade and climate change, calling for "*discontinuation of public support via export credit agencies and public investment banks, for fossil fuel projects.*"

We recommend the bank to consider investments in the Energy and Infrastructure sector of Azerbaijan that will be beneficial for local people and to concentrate on energy efficiency and small renewables that can reap numerous ancillary benefits ("double dividend") for social cohesion and economic development such as reducing energy bills for households and providing new employment and business opportunities, especially in the sector of small and medium enterprises.