



# Azerbaijan

## Unopened Potential of Debt Market

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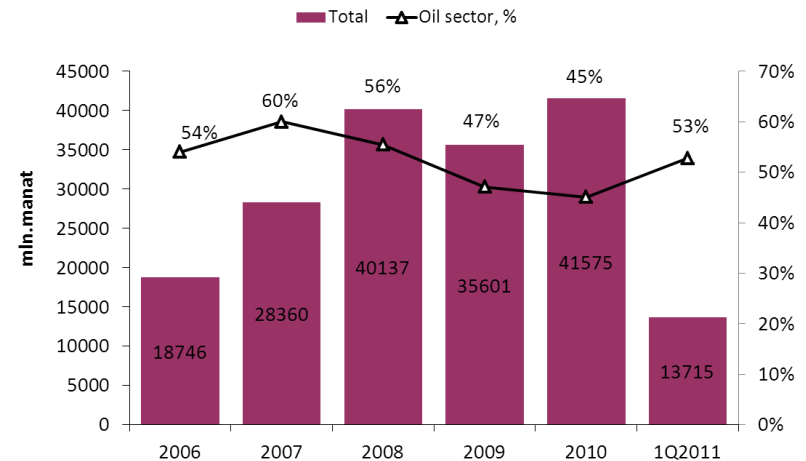
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**September 15- 16, 2011**

## Dynamic growth and healthy financial indicators

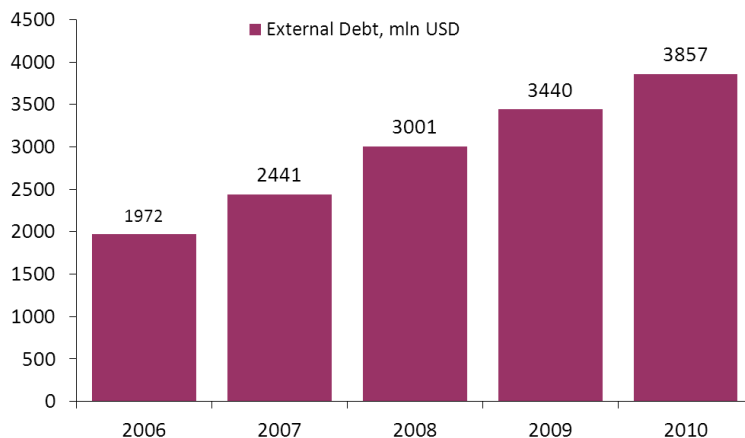
- Average annual increase of GDP during the last five years - 17% per annum
- Forex/gold holdings reached USD32.7bln in the 1Q 2011
- At the end of the year 2010 they amounted to 56% of GDP
- External debt to GDP ratio is about 7%
- External Debt to forex/gold holdings ratio - 13%

### Azerbaijan's Nominal GDP



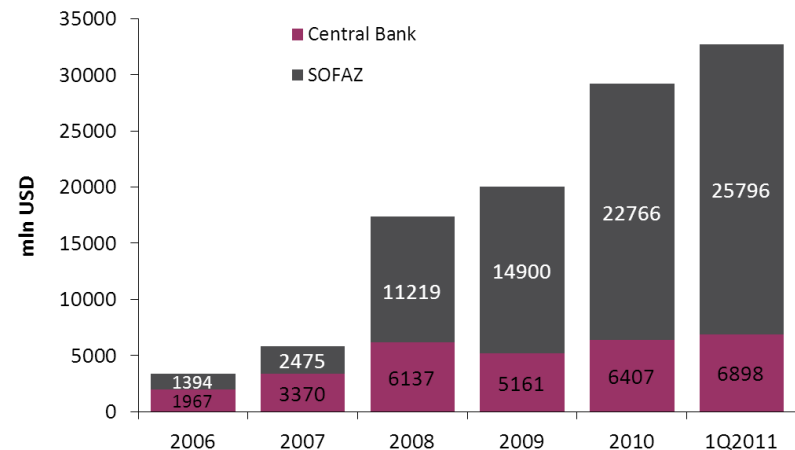
Source: State Committee for Statistics

### External Debt



Source: Ministry of Finance

### Forex/ Gold Holdings - Central Bank And State Oil Fund of Azerbaijan

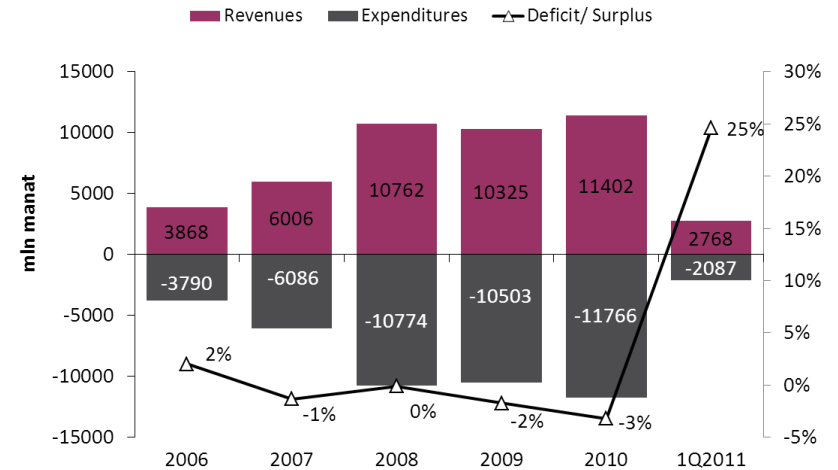


Source: Central bank and SOFAZ

## Crisis is behind, the economy continues to grow

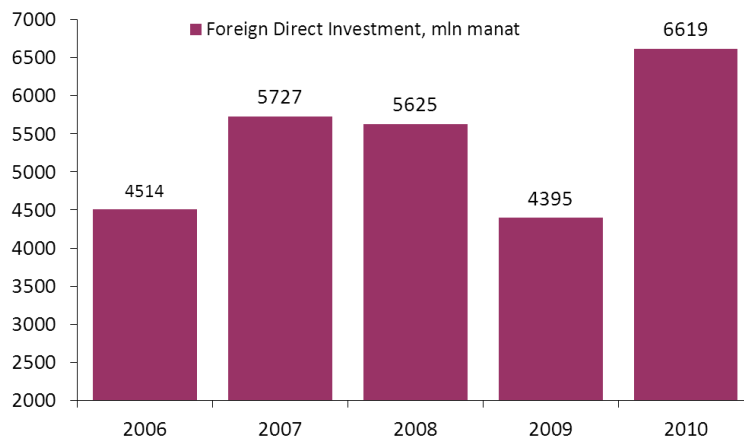
- ▶ Balanced budget - deficit is less than 3%. Even sufficient decrease of oil prices will not cause budget deficit to rise
- ▶ During the crisis Central Bank managed to keep manat stable

### Budget Deficit



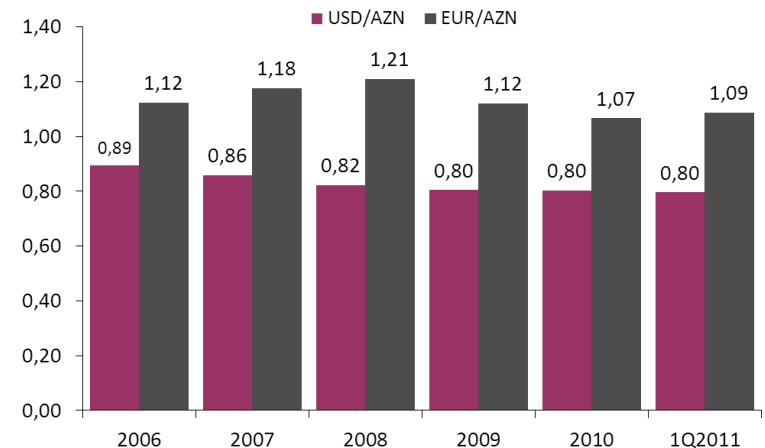
Source: State Committee for Statistics

### Foreign Direct Investments



Source: State Committee for Statistics

### Average Official Dollar and Euro Exchange Rates

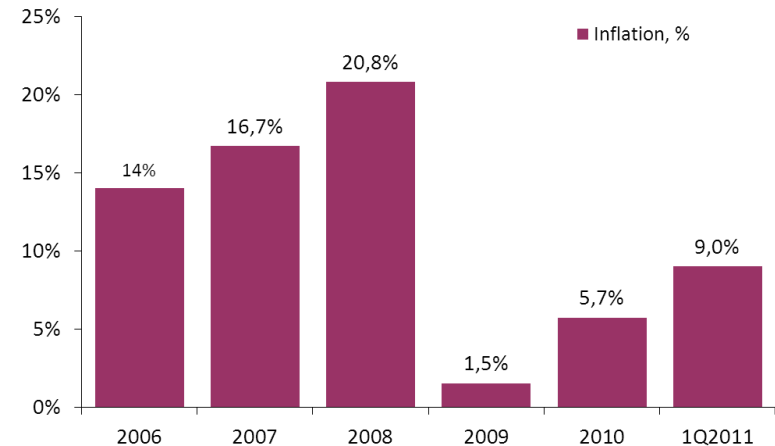


Source: Central Bank

## Welfare of people is gradually increasing

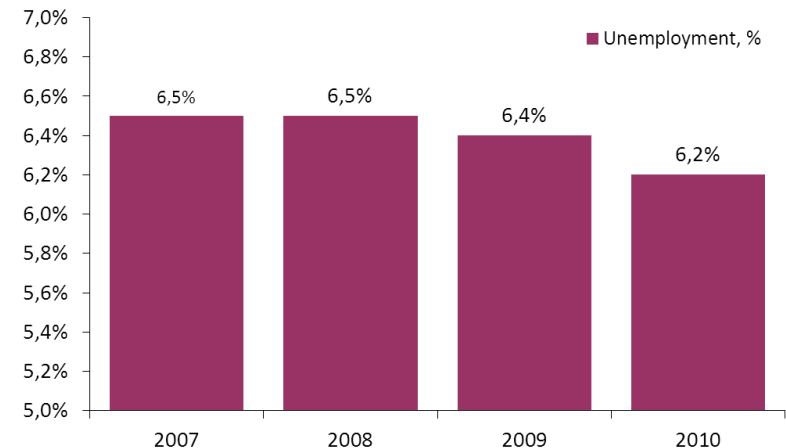
- During the crisis unemployment was not up owing to state support of the economy
- Since 2009 the inflation started to rise again due to sufficient inflow of funds to the country and increase of income of the population

### Inflation



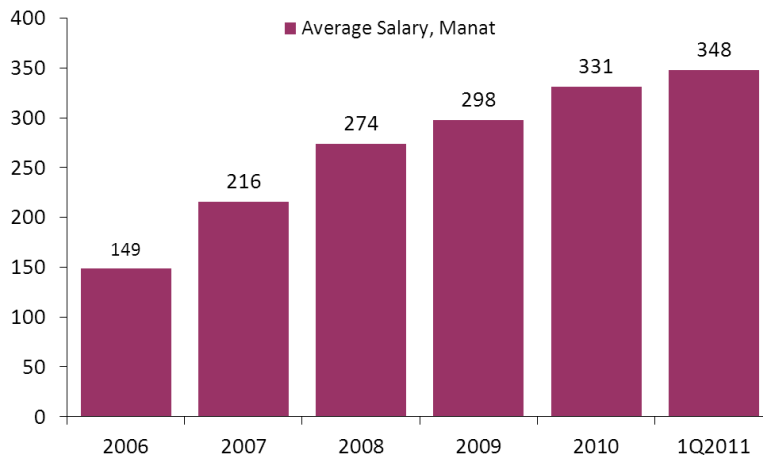
Source: State Committee for Statistics

### Unemployment Rate



Source: State Committee for Statistics

### Average Monthly Salary



Source: State Committee for Statistics

### Fitch

- In its rating category Azerbaijan ranks second for forex/gold holdings to GDP ratio in the world
- Economical and reasonable management of oil revenues
- The budget is balanced and is able to withstand deep correction of oil prices
- During the crisis, the Azerbaijan Central Bank managed to contain the manat exchange rate
- Structural reforms are necessary for growth of the non-oil sector of economy
- Condition of the banking system causes concern, NLP volume as assessed by Fitch is higher than the official data

**BBB-**

**«Positive Outlook»**

### Moody's

- High level of liquidity, low debt burden
- Budgeted deficit has not exceeded 3%
- Rating forecast has raised to positive due to increase of forex holdings of the country and government efforts to develop non-oil sector of the economy
- Banking system development forecast - "stable", reflecting recent stabilization of asset quality and liquidity of banks, as well as improvements in their profitability and capitalization

**Ba1**

**«Positive Outlook»**

### Standard & Poor's

- Sufficient budgetary and international reserves, low debt level, large oil reserves
- Debt level (without account for guarantees), relative to GDP for sovereign issuers with BB and BBB ratings in 2010 averaged to 42.3% and 39% respectively, which is considerably higher than the figure for Azerbaijan - 5.6%
- Level of the rating is restricted by geopolitical risks, centralized and relatively nontransparent process of decision making, high concentration of production in oil-and-gas industry, relative weakness of monetary-and-credit and banking systems

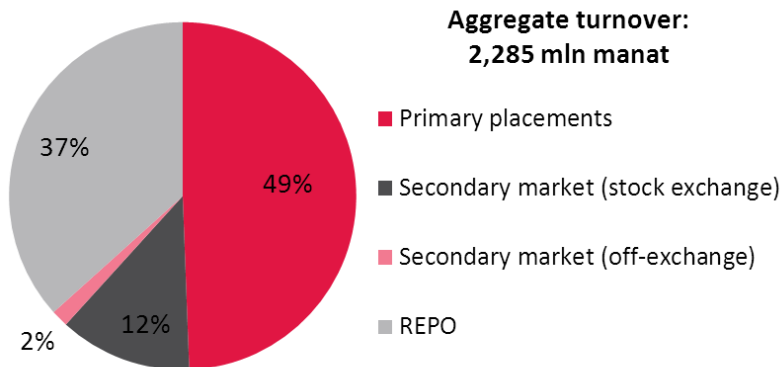
**BB+**

**«Positive Outlook»**

## Market volume is low so far

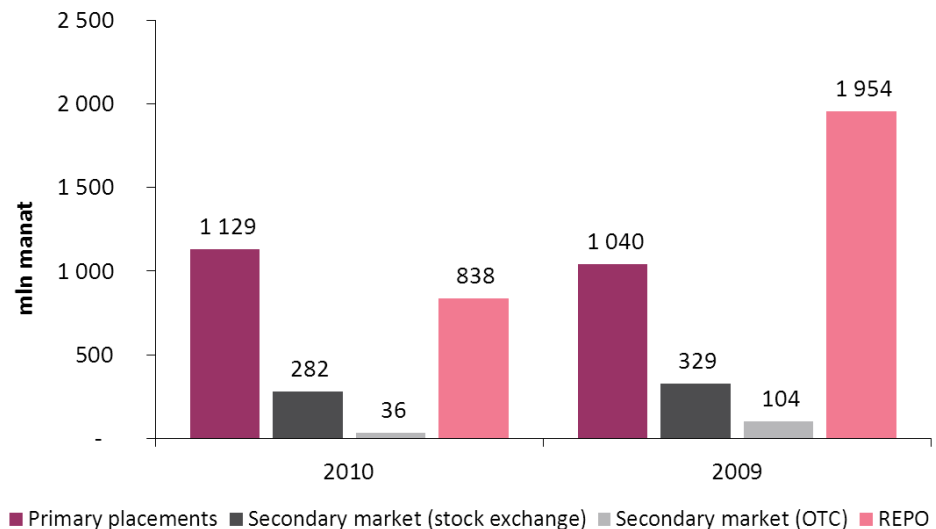
- The observed decrease of aggregate turnover is associated with decline in government bonds offering and reduction in REPO transactions volume due to excess liquidity of banks
- Turnover structure has changed
  - There is a 29% reduction of primary government bonds offering
  - Primary offering of shares and corporate bonds has increased by a factor of 2.2
  - Secondary market turnover has declined, but corporate bonds have gone up by a factor of 2.7

2010, by Types of Transactions, %



Source: State Committee for Securities

Total Volume of Transactions on Azerbaijan's Securities Market in 2009-2010

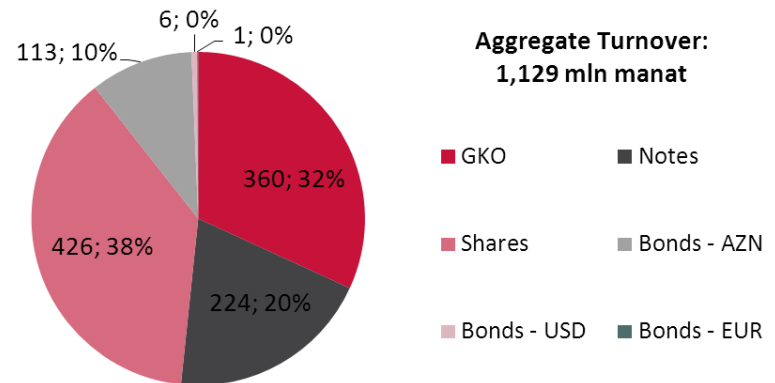


Source: State Committee for Securities

## Secondary market liquidity is low

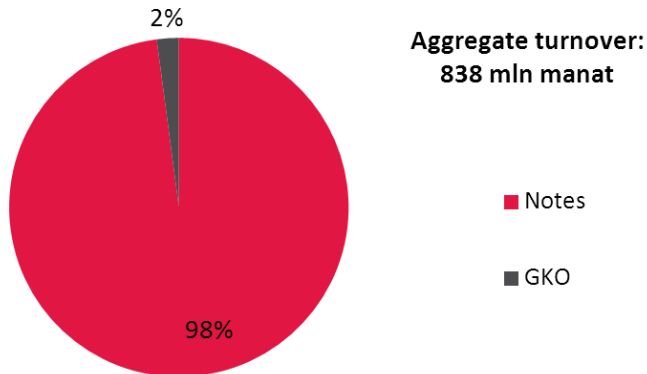
- Its turnover is four times less than that of the primary market
- In 2010 shares account for the highest placement volume (38%), whereas share turnover on the secondary market amounted to less than 4% of the primary placement
- Notes of the Central Bank (20% of the primary market) featured low liquidity at the secondary market, but were actively used in REPO transactions - volume of these transactions exceeded primary placement 3.6 times
- Corporate bonds feature the highest liquidity at the secondary market - trading volume was 27% higher than primary placement

Primary Placement in 2010, mln manat



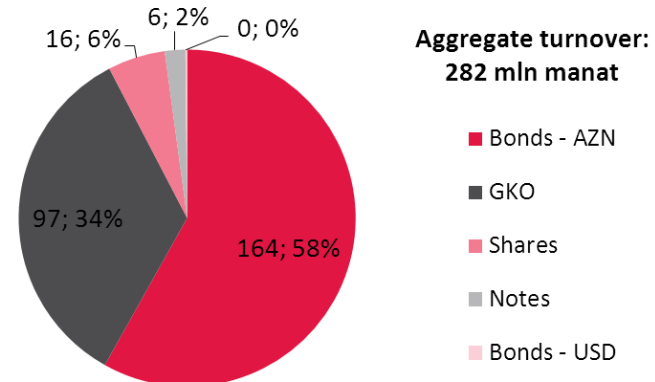
Source: State Committee for Securities

REPO Market in 2010



Source: State Committee for Securities

Secondary Market Turnover in 2010, mln manat



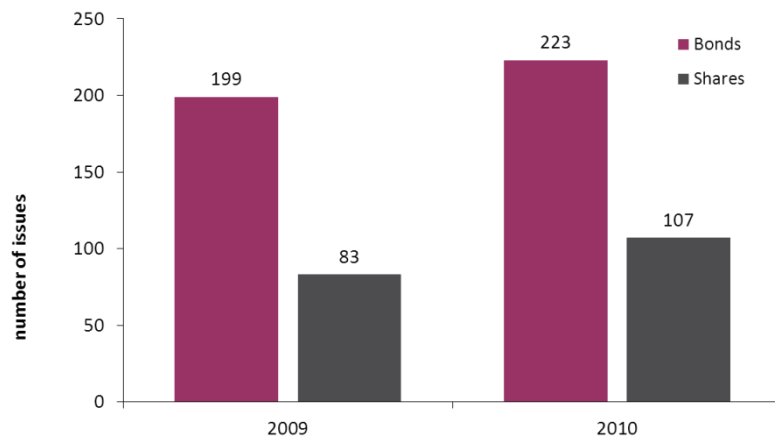
Source: State Committee for Securities

## Transaction volumes

- Total number of transactions is not considerable- 5,430 transactions with all securities at both primary and secondary market during the year
- GKO securities (government short-term bonds) are placed in tranches averaging to 4.8 mln manat The largest GKO issue amounts to 40 mln manat
- Big players dominate the secondary market: in fact there are no private investors

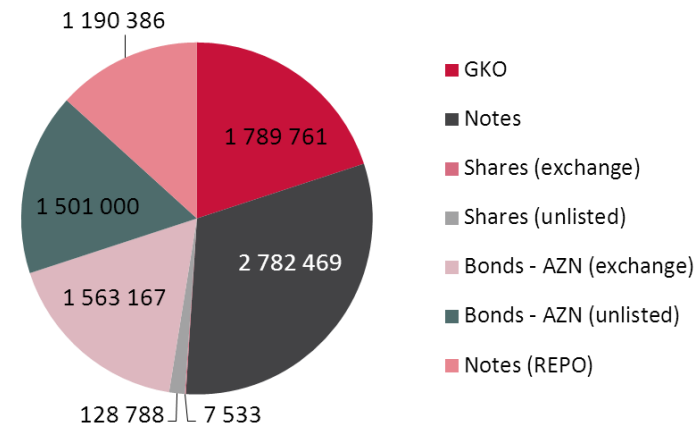
Source: data by the State Committee for Securities, Cbonds

Number of Issues Registered by the State Committee for Securities



Source: State Committee for Securities

2010 Average Secondary Market Transaction Volume, manat



Source: State Committee for Securities



### Strength

- Infrastructure of the securities market is well developed
- Major instruments are already there and work
- Bonds issue is possible in various currencies
- Banks have plenty of free liquidity which must be invested

### Deficiencies

- Small market volume, low liquidity
- Few market participants
- Regulatory framework needs improvement
- Impossibility to attract considerable funds within a single transaction

### We believe in growth of the local market

- Recently a program of long-term development of the market has been adopted
- People welfare improvement and strengthening of banking system of the country
- Availability of attractive credit stories
- Absence of restrictions on flow of funds
- Economic and political stability

### Pro

- Most probable borrowers - largest governmental and private banks, infrastructure companies working in oil, energy, transport sectors, etc.
- Possibility to attract medium-term resources in US dollars is quite advantageous for them, taking into account sufficiently high level of interest rates in manats at the local market.
- The 'Loan Participation Notes' format of transactions is already in use
- The largest companies already have their reports prepared in compliance with IFRS and audited

### Contra

- Special feature - presence of about 10% withholding tax (tax on income of foreign lenders collected inside Azerbaijan)
- For private companies disclosure of beneficiaries is sometimes a problem
- Insufficient level of companies' transparency and small experience of dealing with investors
- Most of the borrowers do not have ratings
- Absence of indicative issues in Azerbaijan

### Forecast

- **Issue of indicative volume of Eurobonds for SOCAR is expected**
- **Borrowers from Azerbaijan will receive increasing recognition at the bond market**
- **Number and volume of transaction will be growing**

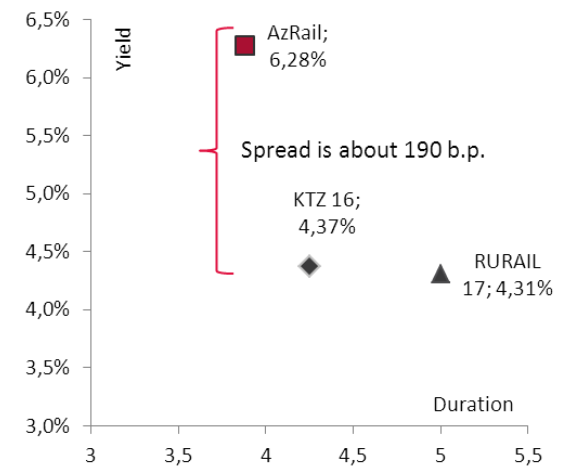
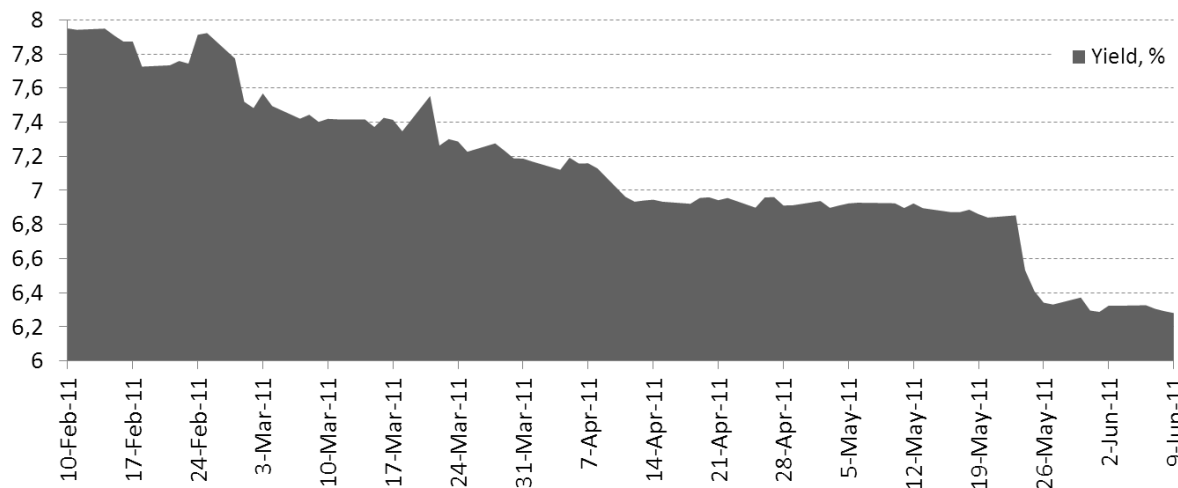
## Azerbaijan Railways (LPN)

- Placement Date - February 18, 2011
- Term - 5 years, duration - 3.88 years
- Issued Amount – \$125 mln
- Coupon - 8.25%
- Put Option - none, call option - from 18.02.2014 @ 104.125, from 18.02.2015 @ 102.0625
- Current Quotations: price 107.85%, yield to maturity 6.28%
- Format - LPN with listing
- Disclosure – no prospectus

## Investment highlights

- **100% of the company belongs to the state**
- **Monopoly in rail traffic**
- **Oil, other cargo and passenger transportation**
- **Low debt burden**
- **Comparable with "Kazakhstan – Termir Zholy" (BBB-)**
- **After the SOCAR placement yield on the issue might further decrease approximately by 140 b.p.**

AzRail 2016 - Yield to Maturity, % per Annum



Source: Bloomberg

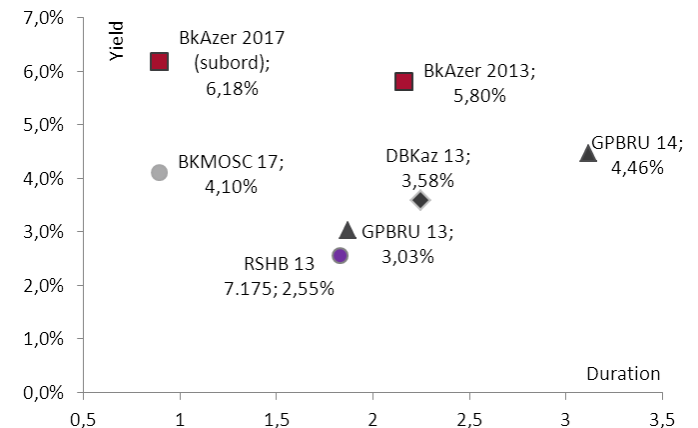
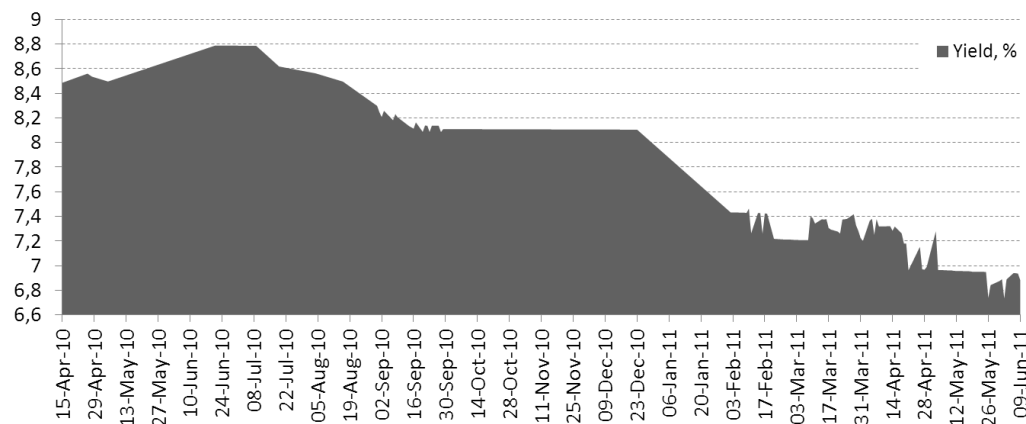
## International Bank of Azerbaijan (LPN)

- Placement Date - May 10, 2007
- Term - 10 years with call option in 5 years at 100% face value
- Duration to Call Option - 0.9 years
- Issue Amount – \$100 mln
- Coupon - 8.4%
- Rating - Ba1
- Current Quotations: price 101.25%, yield to maturity 6.88%, yield to call – 6.18%.
- Format - LPN with listing, disclosure – no prospectus

## Investment highlights

- Majority interest in the bank belongs to the state
- Universal bank, to the share of which falls almost half of the assets and deposits of Azerbaijan banking system
- High system significance
- Sufficient liquidity and profitability of principal activity

BkAzer 2017 Subordinated– Yeild to Maturity, % per Annum



Source: Bloomberg

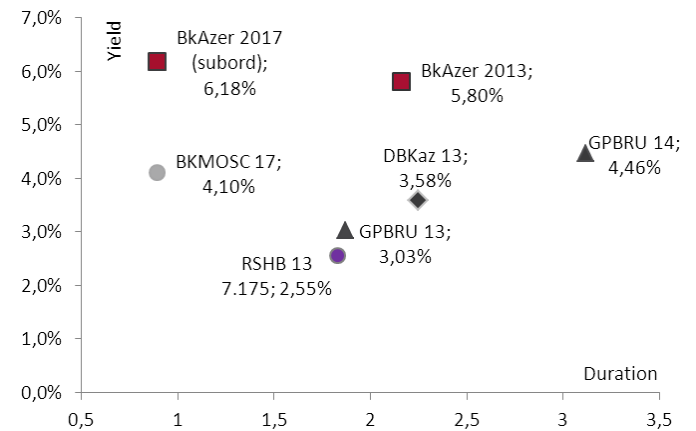
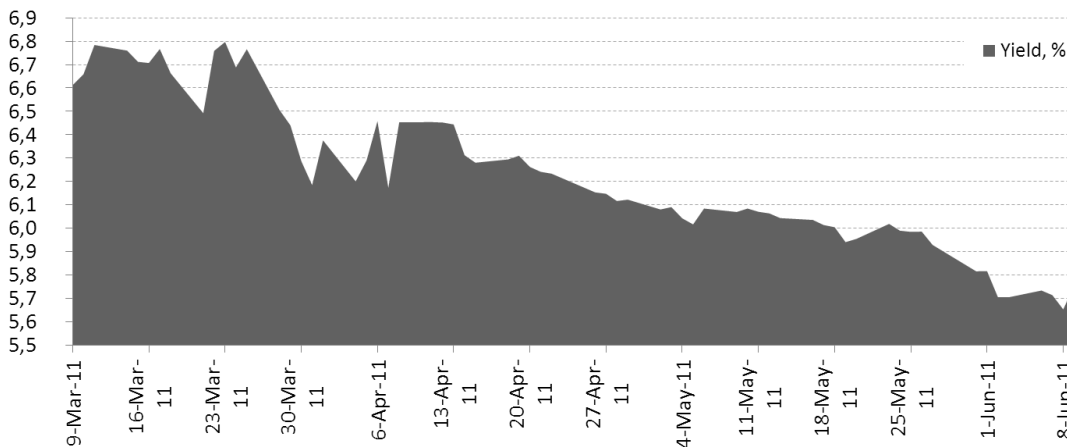
## International Bank of Azerbaijan (LPN)

- Placement Date - October 22, 2010
- Term - 3 years, duration - 2.16 years
- Issue Amount– \$130 mln
- Coupon - 8.5%
- Rating - Baa3
- Current Quotations: price 106%, yield to maturity 5.8%
- Format - LPN with listing
- Disclosure – no prospectus

## Investment highlights

- Spread to UST - 513 b.p.
- Yield drop potential - by 200 b.p.

**BkAzer 2013 - Yield to Maturity, % per Annum**



Source: Bloomberg

**Thank you for your  
attention!**