

Economic Diversification and Economic Security in Contemporary Azerbaijan: Structural Priorities, Global Risks, and Post-Pandemic Development Strategies

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Abstract

In the era of profound global economic volatility—accelerated by geopolitical tensions, technological disruptions, energy market fluctuations, transportation corridor realignments, and ongoing post-pandemic effects—the need for resilient, diversified, and security-oriented economic development models has become increasingly urgent. As the largest economy in the South Caucasus, Azerbaijan continues to strengthen national economic stability by expanding the non-oil sector, modernizing institutional mechanisms, and embedding economic security as a key development pillar. This study provides an updated (2024–2025) theoretical-conceptual analysis of Azerbaijan's diversification model by examining the transformation of national economic structures, the evolution of regional development strategies, and the country's integration into global value chains and transcontinental logistics systems. It evaluates critical challenges arising from global geopolitical fragmentation, energy transition processes, the emergence of new green economy requirements, digital transformation, and the implications of regional conflicts and sanctions regimes. Particular attention is given to the state's efforts to strengthen macroeconomic stability, stimulate competitive non-oil industries, increase human capital productivity, and enhance economic security in line with global standards. The study concludes with a set of forward-looking policy recommendations designed to improve institutional governance, accelerate sectoral diversification, support SMEs and innovation ecosystems, ensure food and energy security, and enhance Azerbaijan's strategic position as a regional transport-logistics hub. The proposed framework serves as a scientific platform for economic debate and future research on national resilience and long-term sustainable development.

Keywords

Azerbaijan; economic diversification; non-oil sector; economic security; global risks; structural transformation; geopolitical instability; energy transition; digital economy; transport corridors; sustainable development; national resilience; macroeconomic policy.

1. Introduction

The question of economic diversification in Azerbaijan remains one of the most decisive strategic issues shaping the country's development trajectory in the 21st century. Following independence in 1991 and the subsequent transition from a centrally planned to a market economy, Azerbaijan faced the challenge of constructing an

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independent macroeconomic model under severe internal and external constraints. The signing of the Contract of the Century in 1994 laid the foundation for the modern oil strategy, which enabled the state to overcome economic collapse, rebuild its national institutional framework, and enter global energy markets.

The early post-Soviet period (1991–2003) was characterized by the formation of national governance institutions, restructuring of economic sectors, stabilization efforts, and the initial strengthening of statehood. Oil revenues in the 2000s served as the main financial engine for socio-economic reconstruction, poverty reduction, infrastructure development, and the establishment of the State Oil Fund of Azerbaijan (SOFAZ), which became a cornerstone of fiscal stabilization and intergenerational equity.

From 2004 onward, Azerbaijan initiated a fundamentally new stage of development: the expansion of the non-oil sector, the intensification of regional socio-economic programs, the modernization of infrastructure, and the implementation of major international energy and transport projects—including the Southern Gas Corridor, Baku-Tbilisi-Kars railway, and multimodal Caspian transit routes.

The 2015–2017 global oil price crisis underscored the vulnerability of excessive dependence on hydrocarbon revenues, prompting strategic reforms and the launch of *Strategic Road Maps* covering key sectors such as industry, agriculture, ICT, tourism, education, and logistics. This period marked a conceptual shift from resource-driven to innovation- and human-capital-oriented economic policy.

By 2024–2025, Azerbaijan faces new challenges that extend beyond the COVID-19 pandemic:

- global geopolitical fragmentation and regional conflicts,
- volatility of global energy prices,
- acceleration of renewable energy deployment worldwide,
- digital and technological disruptions,
- supply chain restructuring,
- climate change impacts,
- new forms of hybrid economic threats,
- transformation of international transport corridors,
- intensification of sanctions-based economic competition, and
- increasing global demand for food, energy, and water security.

These realities increase the urgency of diversification, structural modernization, and the strengthening of economic security mechanisms in Azerbaijan.

1. Introduction

The challenges of economic diversification in Azerbaijan represent not only a theoretical issue but also a practical concern rooted in the country's socio-economic history and contemporary development trajectory. The author's long-standing professional experience in the real sector has revealed the complexity of addressing structural transformation in a resource-dependent economy. Following the dissolution of the Soviet Union, Azerbaijan assumed the difficult task of building an independent national economic model after decades of centralized planning, rigid administrative controls, and limited self-determination in resource allocation. Although the republic was considered self-sufficient within the Soviet framework, key strategic resources—particularly in the oil sector—were controlled by central authorities in Moscow, leaving Azerbaijan without autonomous mechanisms of economic decision-making.

The early years of independence (1991–1995) were marked by severe economic decline, institutional instability, and the urgent need to create a national cadre of economic professionals capable of designing and implementing a new development strategy. During this transitional period, national economic research increasingly focused on issues such as macroeconomic stabilization, formation of national governance structures, and development of an independent economic security framework. A major turning point came with the signing of the "Contract of the Century" in September 1994 between Azerbaijan and a consortium led by BP, which laid the foundation for a

modern hydrocarbon strategy and enabled the country to access foreign investment, technological expertise, and global energy markets (Aliyev, 2018; Ciarreta & Nasirov, 2012).

Between 1995 and 2003, the implementation of structural reforms, stabilization policies, and the effective management of oil revenues helped Azerbaijan build the foundations of national economic resilience. Oil income financed large-scale infrastructure development, strengthened the social protection system, reduced poverty, and supported macroeconomic stability. During this period, Azerbaijan gradually integrated into the global economic system and modernized its public administration and regulatory frameworks.

A new phase began in 2004 with the intensification of non-oil and non-gas sector development. The government strengthened regional development policies, deepened privatization programs, and completed its transition to a market economy. Entrepreneurship reforms and improvements in the business environment stimulated private-sector activity, while strategic energy and transport projects enhanced the country's geo-economic importance. Azerbaijan became a key energy partner for Europe and an essential node in emerging Eurasian transport corridors.

Over the following decade, significant achievements were recorded in non-oil sectors such as petrochemicals, metallurgy, light industry, tourism, ICT, agriculture, and the space and defense industries (Bayramov & Orujova, 2017; Humbatova & Hajiyev, 2020). Efforts were also made to strengthen food security, reduce import dependency, and promote export-oriented production. Foreign direct investment (FDI) attraction mechanisms were renewed to support diversification, while institutional reforms targeting corruption, transparency, and the shadow economy were intensified.

With the adoption of the **Strategic Road Maps (2016–2025)**, Azerbaijan launched a comprehensive restructuring program aimed at strengthening macroeconomic resilience, improving competitiveness, and reducing vulnerability to global financial and commodity market shocks. Despite these efforts, diversification remains incomplete. The dominance of the oil and gas sector continues to pose structural risks, especially amid volatile global energy prices, accelerating energy transition policies, and geopolitical uncertainties.

In the early 2020s, diversification efforts encountered new constraints arising from the impacts of the **COVID-19 pandemic**, global supply chain disruptions, increasing inflationary pressures, and shifts in investment priorities worldwide. Although the acute phase of the pandemic has passed, its economic consequences continue to shape global and national development strategies (Farzaliyev, 2020; "COVID-19 and Human Capital," 2020). A more complex challenge emerged with the intensification of geopolitical tensions, reconfiguration of regional transport routes, sanctions-related economic fragmentation, and the global transition toward green growth and renewable energy—factors that have reshaped international economic relations in 2024–2025.

These trends have underscored the need for a more agile and innovation-oriented diversification strategy in Azerbaijan. Enhancing the efficiency of human capital, strengthening intellectual production capacities, and accelerating the development of high-technology sectors are now essential components of national economic security. This study therefore aims to provide an updated analysis of diversification and economic security in Azerbaijan within the broader context of global economic turbulence, regional transformations, and post-pandemic development imperatives.

2. Literature Review (Rewritten, Expanded, and Updated for 2024–2025)

The literature on economic diversification, structural transformation, and economic security has expanded significantly in recent decades, reflecting intensified global economic volatility and the increasing importance of resilience-oriented development strategies. Studies on resource-rich economies emphasize the need for efficient institutional mechanisms, innovation-driven growth, and risk-mitigating economic policies to ensure long-term stability (Abdurazzakov, 2016; Massol & Banal-Estanol, 2014).

In the context of Azerbaijan, a wide range of national and international scholars have analyzed various aspects of diversification, macroeconomic adjustment, and structural modernization. Alam and Shah (2013) highlight the multiplier effects of investment flows and their role in supporting diversification. Aliyev (2014, 2015, 2018, 2020) provides a comprehensive assessment of national economic sustainability, the structural challenges of the oil-

driven economy, and strategic directions for enhancing economic security and reducing dependence on hydrocarbons.

Other researchers have evaluated Azerbaijan's economic growth patterns, the efficiency of oil and gas resource management, and the potential of non-oil sectors. Ciarreta and Nasirov (2012) and Bergmann (2019) emphasize the need to balance resource-based revenues with long-term productivity gains, while Gaspareniene (2015) forecasts investment flow dynamics and identifies key constraints in attracting FDI to non-oil sectors.

Studies focusing on innovation and export diversification—such as those by Simon-Moya (2020) and Massol & Banal-Estanol (2014)—argue that building innovative capacity is essential for transitioning from a resource-driven economy to a knowledge-driven one. These approaches align with broader global trends where digitalization, technological upgrading, and green transformation play a central role in economic competitiveness.

Contemporary works also reflect the post-2020 realities, highlighting challenges associated with global supply-chain disruptions, weakened investment activity, and heightened geopolitical risks. Fankhauser and Lavric (2020), as well as Farzaliyev (2020), examine the increasing importance of strengthening non-oil export capacity and adopting new mechanisms for supporting diversified growth under crisis conditions.

Gurbanov (2016) and Gurbanov et al. (2017) analyze practical and theoretical issues of national economic development, focusing on productivity, institutional quality, and risk management. Hamidova (2016) identifies priority industrial sectors with potential for diversification, while Humbatova and Hajiye (2020), Tanriverdiyev and Mammadov, and others explore the financial-institutional mechanisms required to stimulate growth in non-oil industries.

Furthermore, Huseynov (2015), Khalilov et al. (2020), Gasimli (2014), and Quluzadə (2021) address the modernization of economic structures and strategies to enhance the efficiency of the non-oil sector. Mahmudova (2019), Mammadov (2017), and Manafov (2019) emphasize the priority role of non-oil sectors in raising national productivity and ensuring sustainable development.

Research related to competitiveness and economic security—such as works by Muradov et al. (2019), Hasanli (2019), Nuriyev (2017), and Rzayeva (2017)—highlight the interconnection between diversification, institutional reform, and national resilience. Shakaraliyev and Shakaraliyev (2016) stress the conceptual importance of designing a sound economic security framework, especially in a turbulent global environment.

Several studies also focus on governance reforms, reduction of bureaucracy, and the improvement of investment conditions (Suleymanov, Alirzayev, & Talibli, 2019). Muzaffarli and Ismayilov (2010) contribute a methodological basis for organizing economic revival in post-conflict territories—an issue of particular relevance after the liberation and reintegration of Azerbaijani territories in 2020–2023.

Taken together, the literature indicates that while Azerbaijan has made substantial progress, new strategic mechanisms are required to achieve deep structural diversification and strengthen economic security under the rapidly changing conditions of 2024–2025. These realities underscore the necessity of developing innovative policies resilient to global risks, technological disruptions, and geopolitical uncertainties.

3. Methods and approaches.

Most of all in the development of the article there were used methods on approaches to solve the new problems in economic processes first of all in modern conditions, primarily from the global point of view, as well as at the regional and macro levels. The author's views and opinions are reflected in the interaction with economic analysis. Based on the analysis materials the generalization method was preferred and assessments were conducted. The author's economic opinion of consistent character on the process of development of Azerbaijan as an independent state during the last 30 years was formed and stated in the introduction to the article. The author believes that the current global shocks, and goals arising from the concept of independent economic development of Azerbaijan, principles of adequate use of global experience in these conditions underlie the methodological approaches. He tries to diversify the regional and international integration processes by contributing to region development in Azerbaijan. Justification of these factors and assessment of perspective

activities are also kept in the spotlight. In order to determine solutions of the problems covered in the article the operation directions are given, and efforts were given to justify them.

4. Practical importance of the article and expected effect for global economics

Opinions and opinions, approaches and suggestions given in the article can be useful in development of mechanisms adequate to modern challenges in terms of minimization of negative effects of the COVID-19 pandemic, improvement of the national economics structure, exaggeration of diversification problems. Azerbaijan tries to use the development stages and ways passed by the economically developed countries in accordance with characteristics of its economical development model. Therefore the measures taken for diversification of the national economics structure and strengthening of economic security mechanism, the applied state support mechanisms, implemented macroeconomic policy, regional and international integration priorities can arise interest for the other countries and researches which pass through similar development processes. The issues and approaches of discussion nature are given in the work economists and researches, scientific and economic analysis centres and institutes dealing with this type of problem can conduct investigations in those areas of research not only at the level of Azerbaijan, but also at the international level. Basic scientific and economic hypotheses, recommendations and suggestions are likely to be used in development of new mechanisms and formation of operation strategies adequate to global challenges in accordance with the requirements of modern times sustainable economic development of different countries.

5. Materials and discussions

National economics diversification and the issues of economic security is not a new problem, and ongoing researches were conducted in this direction of economy science. If approach from the experience in taking adequate measures in disclosure and solution of the essence of economic security problems in different countries of the world, a group of issues can be more infaled: 1) Availability of specific national security and national economic security approaches, concepts and strategies of each country is one of the important factors observed in global economic processes and in strengthening the national economic development system of the countries in the last 70 years. The economic security issue is a key component of the state economic policy; 2) Optimal provision of balanced and efficient development of economic security in economics as a whole, its dynamic growth, economic sustainability, economic production and consumption processes, the maximum productive use of natural and economic resources creating favorable conditions for the development of the national economy is characterized as the sum of processes of ensuring the highest level of national economic interests in the regional and international contexts of the country; 3) The main objects of economic security are the economic system of the country and its main mechanisms, infrastructure facilities, in-mine and land-based resources, labor resources, production and non-production funds, all types of property, financial resources, economic entities, human resources, family, personality and other important indicators.

It is worth to be noted that, there are certain factors that create economic risks including first of all the circumstances contrary to the national economic interests of the country, processes reflected in the economic interests of the state, individual and society, factors and trends threatening the main mechanisms of the national economy, barriers to the dynamics of production and consumption processes, etc. from the other hand important indicators of economic security should be sufficiently assessed, and special attention should be paid to the state economy policy. Conducting fundamental research on the GDP of the country and the volume of GDP per capita, gross national income and per capita income, indicators of life and living standards of the population and taking adequate measures has strategic significance. Timely implementation of preventive and necessary measures on the level of inflation, unemployment and poverty in terms of macroeconomic stability, adequacy of the structure of the national economy, industry development dynamics, food safety indicators condition the systematic approach. Besides, such factors as efficiency of production structure, indicators of entrepreneurship and business development, human development indicators, level of education and security, development of science and technology, innovation processes of national economy, adequacy of funds for development of high technologies and science, state of production, service and social infrastructure network in the country, currency reserves, indicators of the banking and credit system, internal and external debts, and etc. should be comprehensively analyzed, assessed and improved. All these issues and key indicators should be adapted and updated in accordance with 'Azerbaijan 2030: National Priorities on social economic development' (Azerbaijan 2030: National Priorities for Socio-Economic Development, 2021).

Alongside with this, new economic targets were set in order to improve the structure of the national economy in recent years, and they were reflected in the 'Strategic Road Map on national economics perspective in the Republic of Azerbaijan' approved by the Decree of the President of the country dated after December 6, 2016 (Strategic

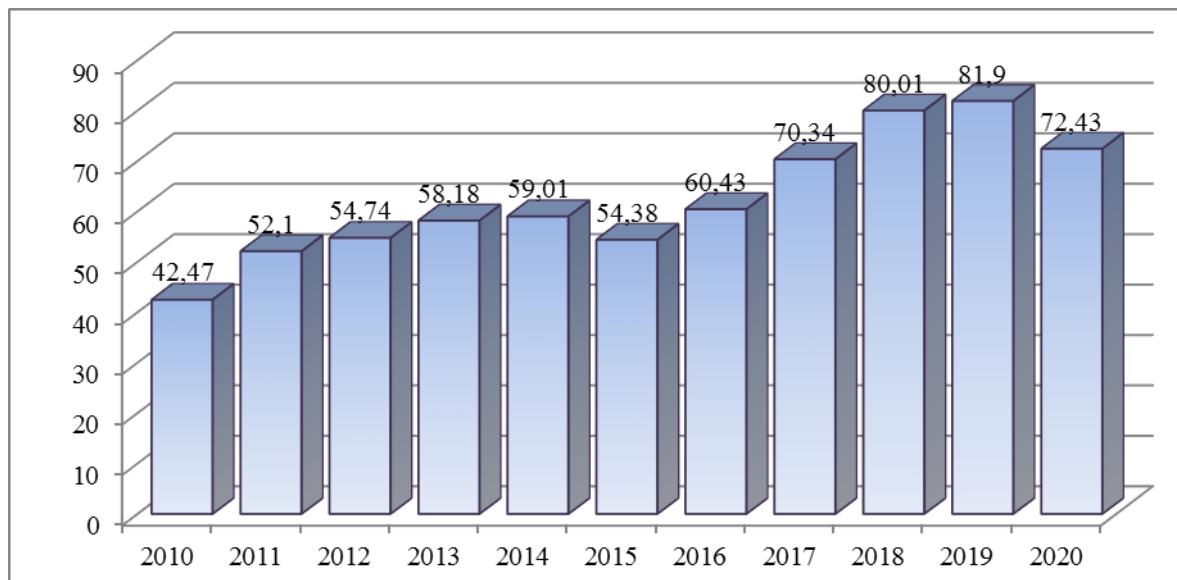
Roadmaps for National Economy and Key Sectors of the Economy, 2016). We would also like to draw attention to an important issue and the problem of global influence. Thus, implementation of new mechanisms on existing issues under the new conditions caused by the COVID-19 pandemic is one of the important issues. The activity strategy for each type of economic activity or enterprise is required to be developed in accordance with requirements of the period, directions of development and changes at the global level. In particular, the development of newly organized Garabagh and East Zengezur economic regions on the basis of the highest technology, including 'smart' technologies should be accelerated. Zengezur Transport Corridor to be opened will create new opportunities for expansion of the integration of the countries of the region and to productive use of development potentials in different sectors of the economy. It will be possible to take more effective measures in diversification of economics in Azerbaijan and reduce its dependence on oil and gas.

5.1. Economic diversification in Azerbaijan and analysis of economic security level

Diversification of the economics of the country condition the consistent implementation of many measures and development of action mechanisms in this regard. Besides, diversification of the economics structure and efficient use of the potential of perspective economic sectors plays an important role in strengthening of the economic security in the country. Systematic review of economic security issues, analysis of key indicators in this direction and taking adequate measures are of great importance. Economic security issues has been being more in the spotlight since the independence of Azerbaijan. Thus, after the processes of realization of strategic tasks in the first years of independence of Azerbaijan, formation of state attributes, creation of mechanisms of political and economic systems, and identification of practical tools undoubtedly first of all it was necessary to cope with the task of formation of national security and economic security concepts in the framework of national and national economic interests. In this connection the intensification of the processes of strengthening the main mechanisms of the national economy and ensuring of development within the framework of national economic interests was started. In this context regarding to implementation of the 'Oil strategy' the modeling of development of other sectors of the economics, and acceleration of the economic reforms processes in whole was achieved. In 1995-2003 the macroeconomic stability was ensured, at the same time during that period the main phase of economic reforms was implemented within the framework of national economic interests. Market economy mechanisms were developed, agrarian reforms were carried out, and mechanisms for efficient land use were developed, land distribution was resolved for ensuring more productivity engagement of population in the region in agriculture, crop production and livestock, development mechanisms of entrepreneurship, farms, business entities, as well as stimulating mechanisms were prepared and applied.

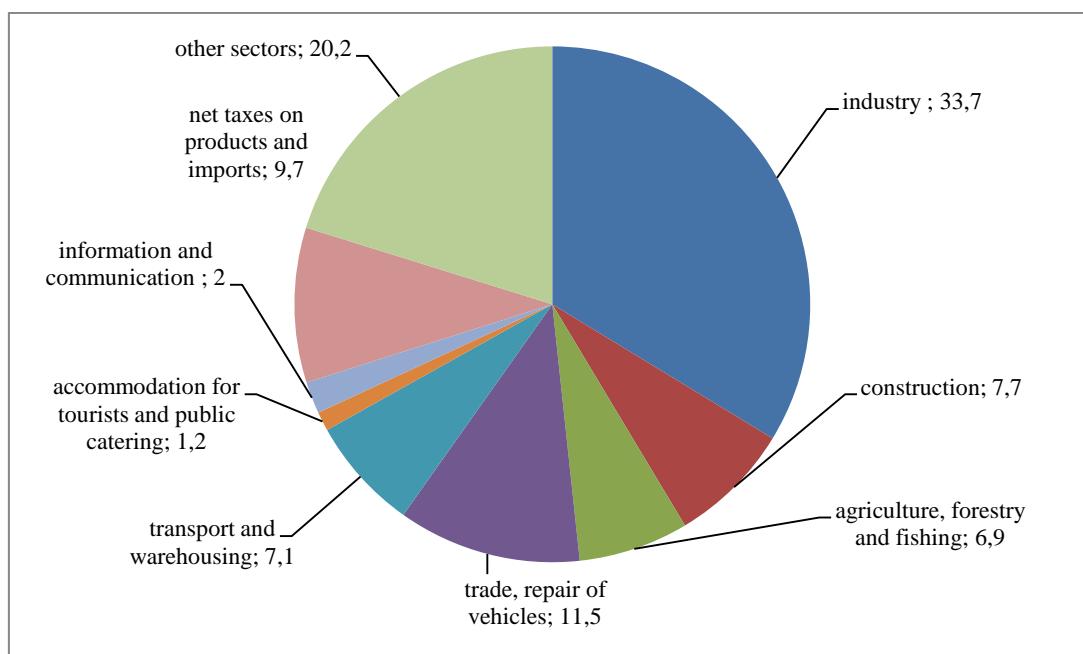
At the same time, special attention was paid to strengthening the legislative framework to ensure the national economic security in Azerbaijan. These priorities are conceptually formed on the basis of national security strategy and priorities in Azerbaijan. In the law of the Republic of Azerbaijan about the national security adopted on June 29, 2004 economic security criteria and principles alongside with conceptual approaches on national security took a special place (National security). Inefficient use of available resources, weakening of economic potential, dependence of our economy on other countries, as well as hazards related to the operation of transport and pipeline systems, weak maneuverability of the economic system, instability of the financial and credit system, low investment activity and etc. as the main economic threats and challenges for Azerbaijan were abolished by this law. The article No.17 of the law covers the key principles and criteria of the national economic security in Azerbaijan. It includes first of all consideration of internal and external factors threatening the balanced and dynamic development of the national economy, and taking adequate measures, deepening the development of market economy mechanisms and strengthening the economic potential in the country, ensuring efficient use of existing internal and external financial resources for sustainable development of the national economy and improving the welfare of the population, strengthening the banking and transport sectors, balancing of strategic resources, etc. Strategic and conceptual approaches on strengthening the economic security in Azerbaijan also took an important place in the other important document - National security conception of the Republic of Azerbaijan approved by the Decree of the President of the country dated after May 23, 2007 (National Security Concept Of The Republic Of Azerbaijan, 2007). Paragraph 4.3.4 of this concept focuses on economic and social development issues, as well as conceptual approaches to national security on energy security policy in paragraph 4.3.8 and transport security policy in paragraphs 4.3.9. draw attentions. The conception emphasizes that sustainable economic development of the country is a basic principle of state economic policy. As a result of taking such systematic and consistent measures Azerbaijan achieved the adequacy of important economic security indicators in recent decades. In order to review them more objectively and visually we analyzed a group of economic security indicators.

In Picture 1 the GDP dynamics in Azerbaijan in 2010-2020 is expressed. But we consider that, pandemic had already impacted this tempo (Action Plan to reduce the negative impact of the coronavirus (COVID-19) pandemic on the economy of the Republic of Azerbaijan, 2020). In recent years additional effective measures will need to be taken in order to make this tempo more dynamic, thus, the volume of GDP in 2020 decreased approximately by %11.6 in comparison with 2019.



Picture 1. GDP dynamics in Azerbaijan in 2010-2020, in billion manat. (Prepared on the basis of ARSSC data - <https://www.stat.gov.az/>).

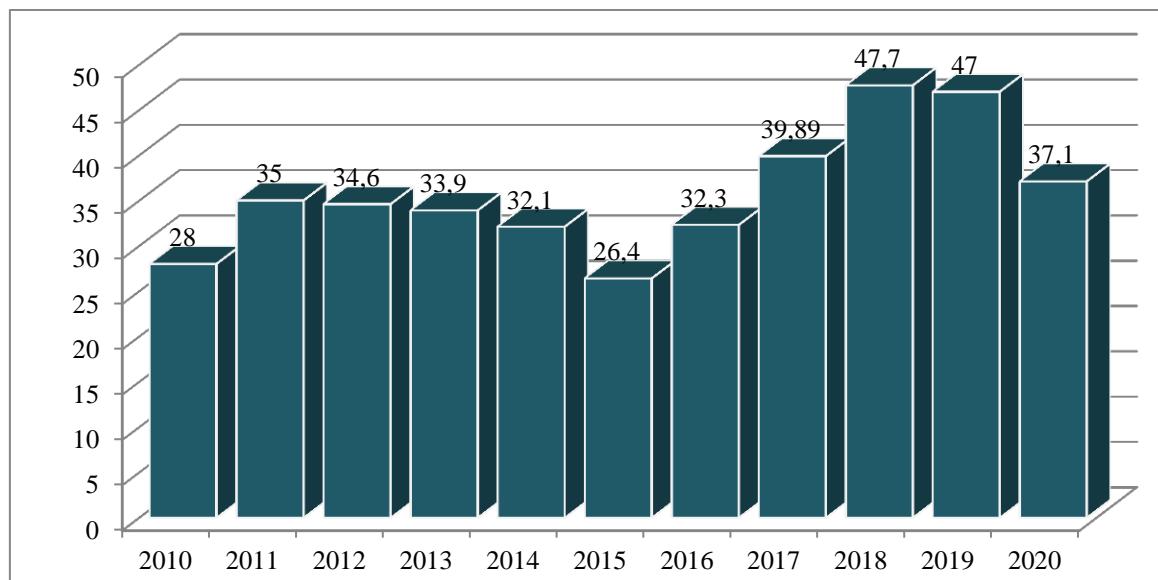
In Picture 2 the sector structure of GDP in Azerbaijan in 2020 was analysed, and from here we can see that the share of industrial sector in the GDP of the country is % 33,7, trade, repair of vehicles - %11,5, construction sector - %7,7, agriculture, forestry and fishing - % 6,9 and etc. (Development of non-oil sector (for 2020), 2021).



Picture 2. Sector structure of GDP in Azerbaijan in 2020, in per cent (Prepared on the basis of ARSSC data – <https://www.stat.gov.az/>).

During the pandemic, many sectors of the economy, especially the activities of the service and tourism sector was paralyzed. For this reason the problems of faster and more efficient recovery of the activities of these sectors of the economics in the postpandemic period must be resolved.

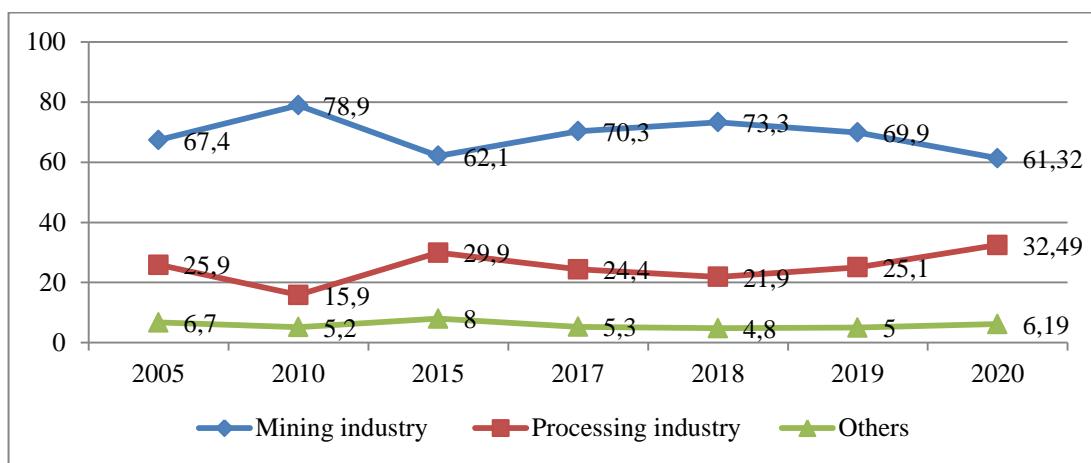
In Picture 3 the dynamics of total volume of industrial production in Azerbaijan in 2010-2020 is given, and as it can be seen during 2018-2020 the growth dynamics was decreased, and in 2020 it was decreased by more than %21 in comparison with 2019.



Picture 3. Dynamics of total volume of industrial production in Azerbaijan in 2010-2020, in billion manat. (Prepared on the basis of ARSSC data – <https://www.stat.gov.az/>).

If in 2018-2019 this reductions took place primarily because of decrease in oil prices on global markets, in 2020 it is associated with the COVID-19 pandemic, and such a situation for Azerbaijan is considered as quite undesirable elements of economic security. Therefore, under the postpandemic conditions there are required the approaches to the problems of industrial development through more effective mechanisms of action. It is important to renew the industrial potential on the basis of high technologies according to the level of requirements of the 4.0 industrial revolution. Important directions of the 5.0 global industrial revolution should be worked out, and in this regard the development priorities and goals of the industrial sector which plays an important role in strengthening the economic security in Azerbaijan should be improved to the maximum.

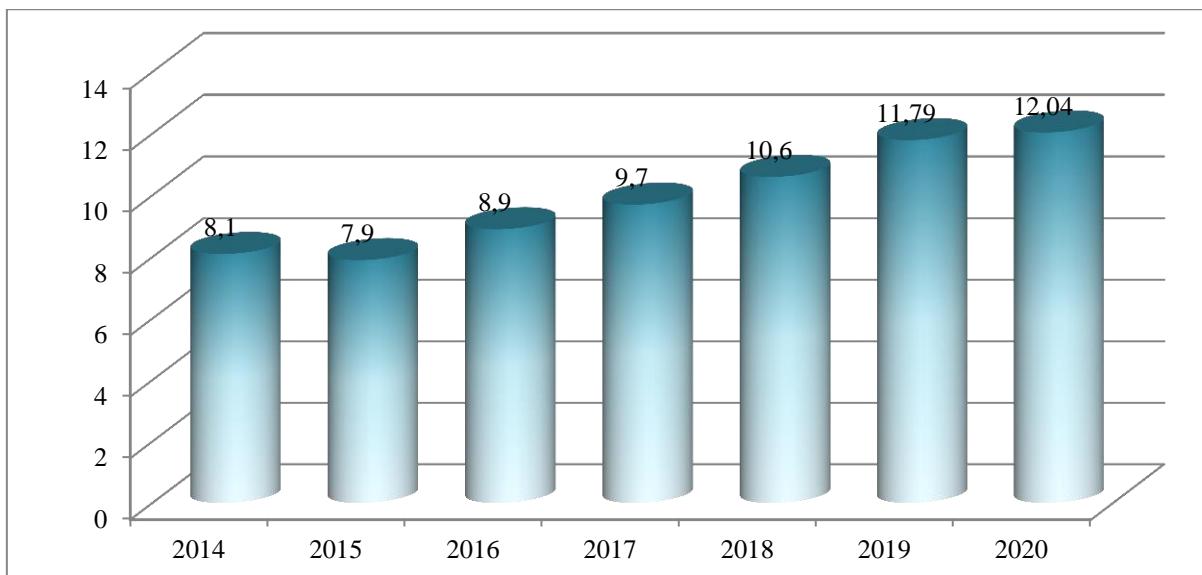
In Picture 4 the share of mining and processing industry in the structure of industrial output in Azerbaijan in 2020 was analysed, and from this analysis it can be concluded that in recent years, the potential of the processing industry is used more efficiently. Thus, the production in the processing industry in 2020 increased by %29.4 in comparison with 2019.



Picture 4. The share of mining and processing industry in the structure of industrial output in Azerbaijan in 2020, in per cent (Prepared by the author on the basis of ARSSC data - <https://www.stat.gov.az/>).

This shows that there are opportunities for the more increase of potential in processing industry and diversification of this sector. Diversification of the processing industry development in the economic development goals of Azerbaijan is assessed as strategic factors of strengthening of economic security. Because of this, strengthening of the measures on diversification and modeling of non-oil and non-gas sectors deveopment which are currently in the intensive phase through higher technologies and science-based mechanisms emerged as an essential necessity (Development of non-oil sector (for 2020), 2021). Taking more effective measures in the direction of solving problems on development of science and technology market in the country, strengthening of the knowledge economy can create additional potential for our economic security.

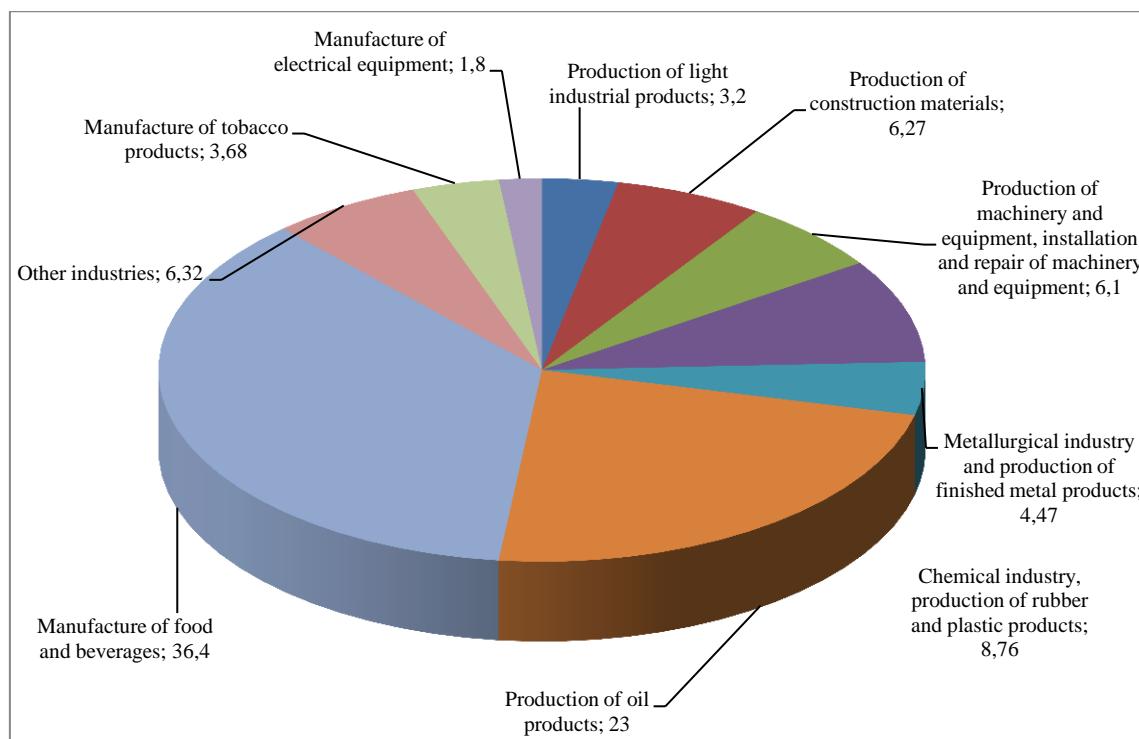
In Picture 5 the dynamics of processing industry products in Azerbaijan in 2014-2020 was analysed, and as we mentioned in the beginning this industry includes activities related to the non-oil and non-gas sector. The total volume of the products of processing industry in 2020 increased by %2.1 in comparison with 2019 and composed 12.04 billion manat by the end of 2020.



Picture 5. Dynamics of processing industry products in Azerbaijan in 2014-2020, in billion manat. (Prepared by the author on the basis of ARSSC data - <https://www.stat.gov.az/>).

In a postpandemic environment much efforts will be required to restore the intensity of activity of a group of non-oil and non-gas sector areas, as well as tourism, vehicle repair, and the other service areas. There were taken measures in order to restore the activity in this sectors during pandemic, but much work still remains to be done to achieve the restoration of previous pace of development. We believe that, if the expansion of the processing enterprises network in the non-oil and non-gas sector with perspective opportunities is ensured, it is possible to form more added value, deepen the economic diversification, and make important contributions to ensure the economic security of the country as a whole in order to achieve the growth of the economy in this important industrial area.

In Picture 6 the structure of the total output of the non-oil industry in Azerbaijan in 2020 was analyzed, and the volume of food and beverage products in a general structure is % 36.4.



Picture 6. The structure of the total output of the non-oil industry in Azerbaijan in 2020, in per cent. (Prepared by the author on the basis of ARSSC data - <https://www.stat.gov.az/>).

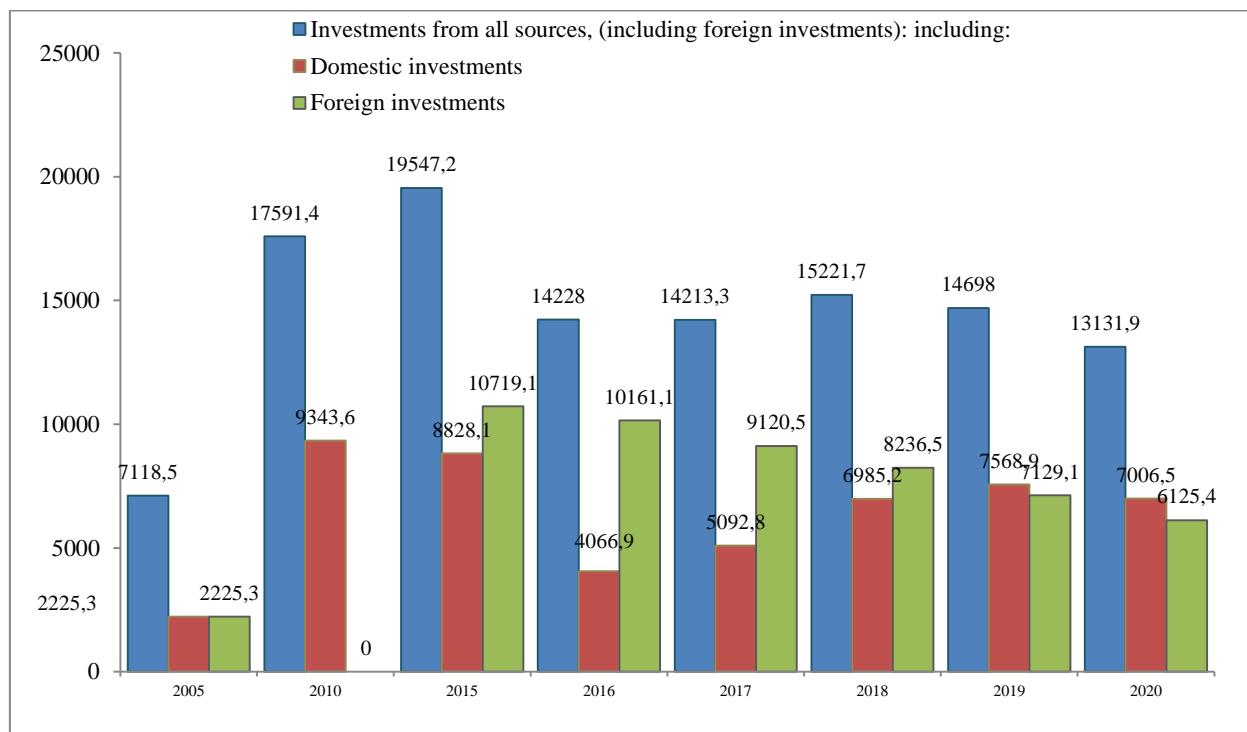
However, the share of a number of strong economic sectors, including production of light industry products, construction materials, chemical industry, as well as the metallurgical industry and the production of finished metal products is much lower than its potential. In the postpandemic period the much more use of opportunities of increase in construction materials and light industry production is possible. Thus, there are sufficient raw material resources and manpower for maximum efficient and intensive development of these sectors. For ensurance of the economics diversification and sustainable economic security in the country in the postpandemic period more attention is required to be paid to taking adequate measures in this regard, improvement of existing mechanisms of action, especially to strengthening of the technological development.

5.2. Assessment of the role of investments in diversification and strengthening of the economics in Azerbaijan

Even before the impact of the COVID-19 pandemic during the last ten years the problems in economics diversification in Azerbaijan existed, and some of them still wait for their solution. The main issue is to solve the problems of diversification of non-oil and non-gas sectors, and problems in attracting investments in these sectors. Unfortunately, the foreign investors are not in hurry to invest in these sectors, and the main reason of this is failure to meet existing risks, non-adaptation of the investment climate to the requirements and conditions of

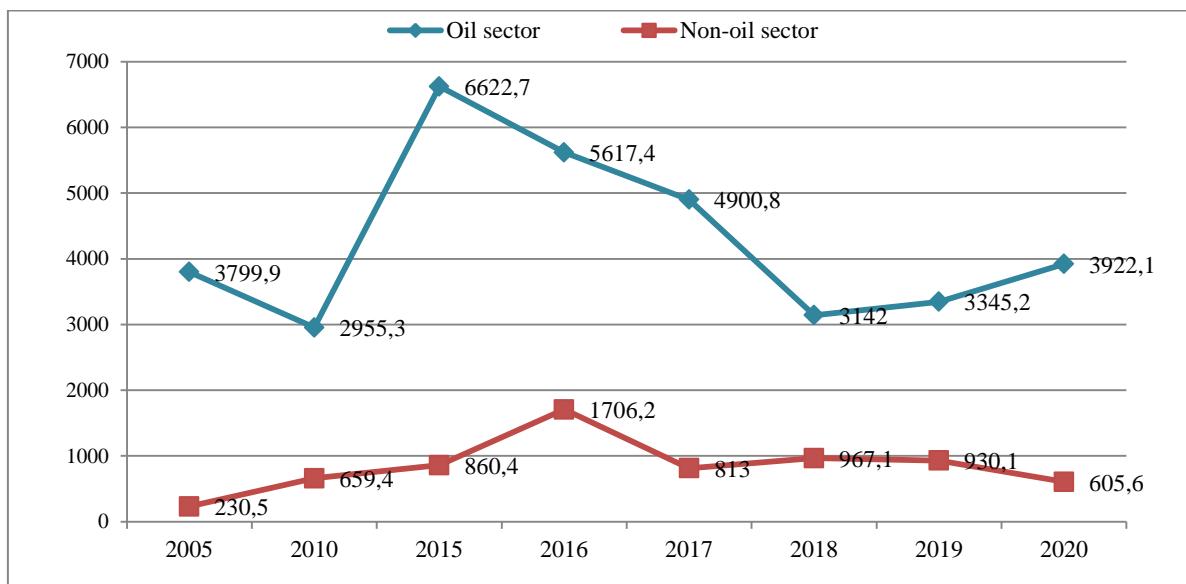
potential investors. Therefore development and implementation of the more effective mechanisms in the direction of attracting foreign investment required for economic structure diversification, intensification of modernization measures is important (Qasimli, V.A., 2014). In this regard, identification of conceptual aspects of modern problems of the national economy and the ways to solve them, and the need to adapt to global challenges occurring over time should be taken into account to the maximum (Mammadov, E.Y., 2017). At the same time the concept of sustainable and balanced regional development alongside with the development priorities balancing in different sectors of national economics should be implemented (Nuriyev, A.X., 2017). The systematic implementation of measures and targeted programs in these directions began in recent years. Under such conditions there are a number of indicators in ensuring and strengthening the economic security of Azerbaijan which are important in terms of solution of sensitivity, and employment problems of the population, income increase, poverty reduction, mitigating food problems. These include development of the agriculture fields, achieving dynamic growth of national income and per capita income, effective use of retail trade development opportunities, regulation of the consumer market, and eliminating dependence of the production of essential foodstuffs on imports; minimizing this dependence at least, and so on (Aliyev, Sh.T., 2018). From the other hand, the need for measures on formation and development of the potential of the currently perspective sectors, as well as fields related to the knowledge economy occurred. There are enough labor resources in our country and more intensive steps are required for formation of highly professional human capital and efficient use of intellectual resources (Aliyev, Sh.T., 2015).

In Picture 7 the structure of foreign investment on sectors in Azerbaijan in 2005-2020 and its dynamics is given, and as it can be seen, the volume of investments from all sources composed 19.5 billion US Dollars in 2015, but this indicator decreased in the further years. During last three years this reduction accelerated and by the end of 2020 it composed only 13.1 billion US Dollars. From this point of view, there should be taken measures on identification of more productive and intensive sources of investment for the economy in Azerbaijan and first of all on attracting maximum foreign investment.



Picture 7. The structure of foreign investment on sectors in Azerbaijan in 2005-2020, in mln. US Dollars (prepared on the basis of ARSSC data - <https://www.stat.gov.az>).

The volume of direct investments to oil-and-gas and non-oil and non-gas sector in Azerbaijan in 2005-2020 is given in Picture 8, and as it can be seen during the period under review the volume of direct investments in the non-oil and non-gas sector was not high in all periods. Investments in the oil and gas sector are characterized by instability, they decreased more than twice during 2015-2018, but during last three years the growth tempo was restored. (see: Picture 8).



Picture 8. The volume of direct investments to oil-and-gas and non-oil and non-gas sector in Azerbaijan in 2005-2020, in mln.US Dollars (Prepared on the basis of ARSSC data - <https://www.stat.gov.az>).

It is worth to be noted that, investments in the industrial sector in Azerbaijan are important, and sustainable investment in fixed assets impacts the growth of industrial output positively. Thus, sustained investment in fixed assets in the industrial sector in 2005-2020 allowed for the dynamic growth of gross industrial output, and the indicators related to this are given in Table 1, the regression model was developed on the basis of this information:

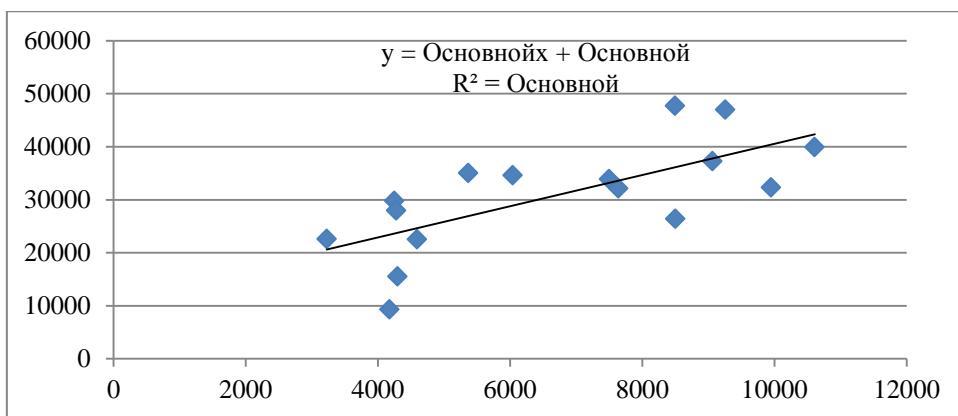
Table 1.

fixed capital investments into industrial sector and gross industrial output dynamics in Azerbaijan in 2005-2020 (in mln. man.)

Indicators		2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Fixed capital investments, in mln. manat	X	4176,0	4297,0	4591,0	4249,0	3225,0	4276,0	5370,0	6040,0	7499,6	7639,5	8499,9	9949,8	10610,1	8497,2	9258,0	9065,3
The total cost of industrial products, in actual prices, in mln. manat	Y	9308,8	15544,0	22495,6	29773,3	22563,6	27978,2	35026,9	34565,0	33898,1	32110,3	26369,4	32300,2	39892,5	47677,0	46999,2	47269,9

Regression statistics						
R		0,699014				
R ²		0,488621				
Normalized R		-1,14286				
Default error		7590,626				
Observations		1				
Analysis of variance						
	df	SS	MS	F	F	
				-	-	

					<i>Significance</i>			
Regression	16	7,71E+08	48171743	13,37695				
Residue	14	8,07E+08	57617607					
Total	30	1,58E+09						
	<i>Coefficients</i>	<i>Default error</i>	<i>t-statistics</i>	<i>P-Value</i>	<i>Low 95%</i>	<i>Upper 95%</i>	<i>Low 95,0%</i>	<i>Upper 95,0%</i>
Y- intersection							0	0
X 1 Factor - X 6 Factor							0	0
X 7 Factor							8,07E+08	8,07E+08
X 8 Factor							7,71E+08	7,71E+08
X 9 Factor	14	8,07E+08	1,74E-08	1	-1,7E+09	1,73E+09	-1,7E+09	1,73E+09
X 10 Factor	13,37695	7,71E+08	1,74E-08	1	-1,7E+09	1,65E+09	-1,7E+09	1,65E+09
X 11 Factor	7590,626	14	542,1876	1,16E-31	7560,599	7620,653	7560,599	7620,653
X 12 Factor	0,488621	13,37695	0,036527	0,971378	-28,2021	29,17933	-28,2021	29,17933
X 13 Factor	5724,731	7590,626	0,754184	0,463236	-10555,5	22005	-10555,5	22005
X 14 Factor	0,805802	0,488621	1,649135	0,121369	-0,24219	1,85379	-0,24219	1,85379
X 15 Factor	11106,64	5724,731	1,940115	0,072781	-1171,69	23384,96	-1171,69	23384,96
X 16 Factor	2,947182	0,805802	3,657451	0,002586	1,218908	4,675455	1,218908	4,675455



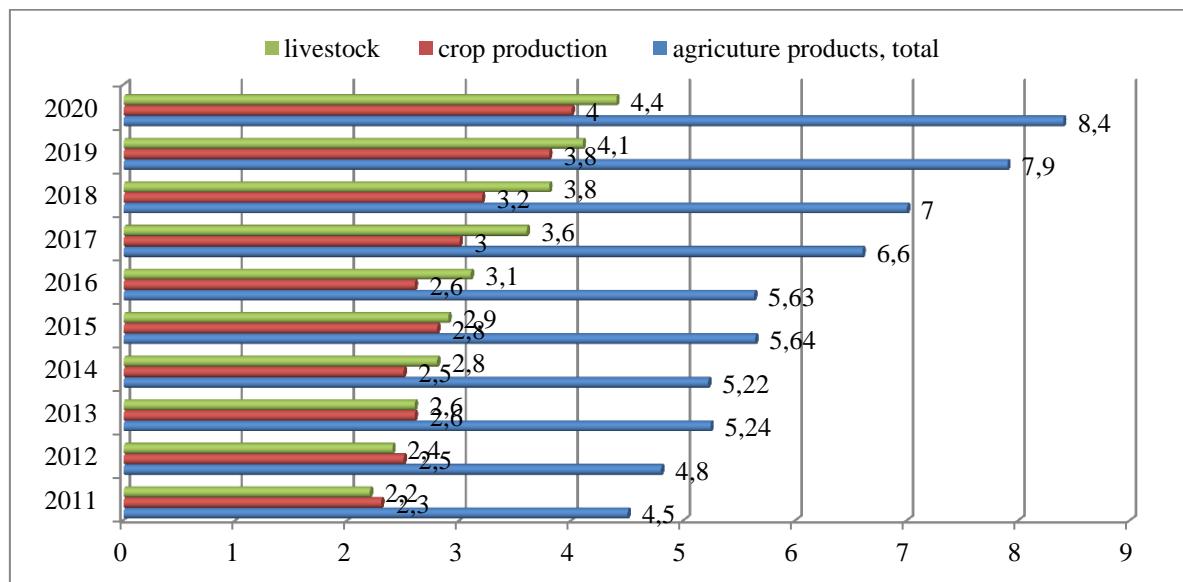
$$y = 2,9472x + 11107$$

Using the data indicated in Table 1 and indicators of the regression model, due to an increase in investments in fixed assets in the industrial sector on 1 manat in 2005-2020 causes an increase in gross industrial output by 2,9472 manat.

Undoubtedly, this is a high figure, and we believe that increase of the volume of investments into the perspective non-oil and non-gas sector fields in Azerbaijan, as well as priority non-oil and non-gas industries, and especially development and implementation of mechanism of intensive attraction of foreign investments must be provided.

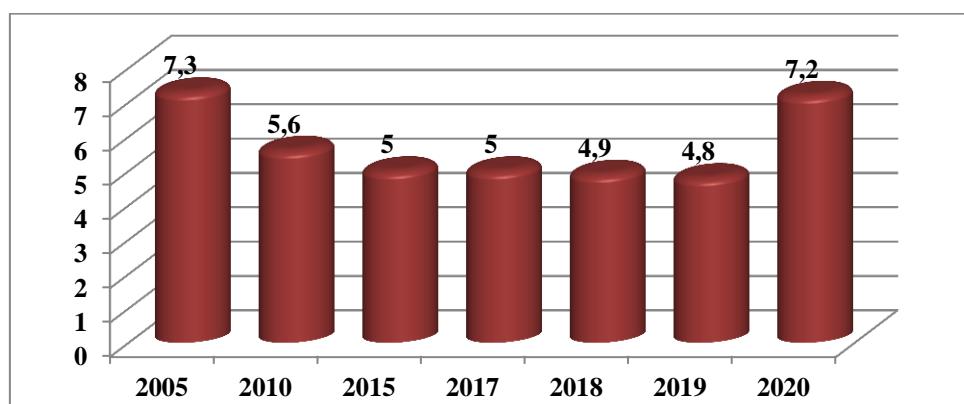
In Picture 9 the gross agricultural output in Azerbaijan in 2011-2020, as well as the dynamics on product cost in crop production and livestock sectors were analysed. If in 2011 the gross agricultural output composed 4.5 billion manat, this indicator in 2015 became 5.64 billion manat, in 2018 - 7 billion manat, in 2019 - 7.9 billion manat, and in 2020 it reached 8.4 billion manat, and this is %6.3 more than in 2019. It means that in the pandemic period the growth dynamics in the crop production and livestock sectors increased, and also we see that under

the post-pandemic conditions this sector has the potential not only to maintain but also to increase the growth rate.



Picture 9. Gross agricultural output in Azerbaijan, in billion manat, 2011-2020 (prepared by the author on the basis of ARSSC data - <https://www.stat.gov.az/>).

It is worth to be noted that, one of the important indicator of the economic security is decrease of unemployment level in the country, creation of more decent jobs, and strengthening of population's employment (Huseynov, T.H., 2015). In recent decades in order to strengthen the employment continuous measures were taken one after another, the attention to this problem was increased, consistent employment strategies were implemented in the processes of social economic development of the regions, and the employment strategy which is currently in execution covers the period up to 2030 (The Employment Strategy of the Republic of Azerbaijan for 2019-2030, 2018). The unemployment level dynamics of our country is given in Picture 10.

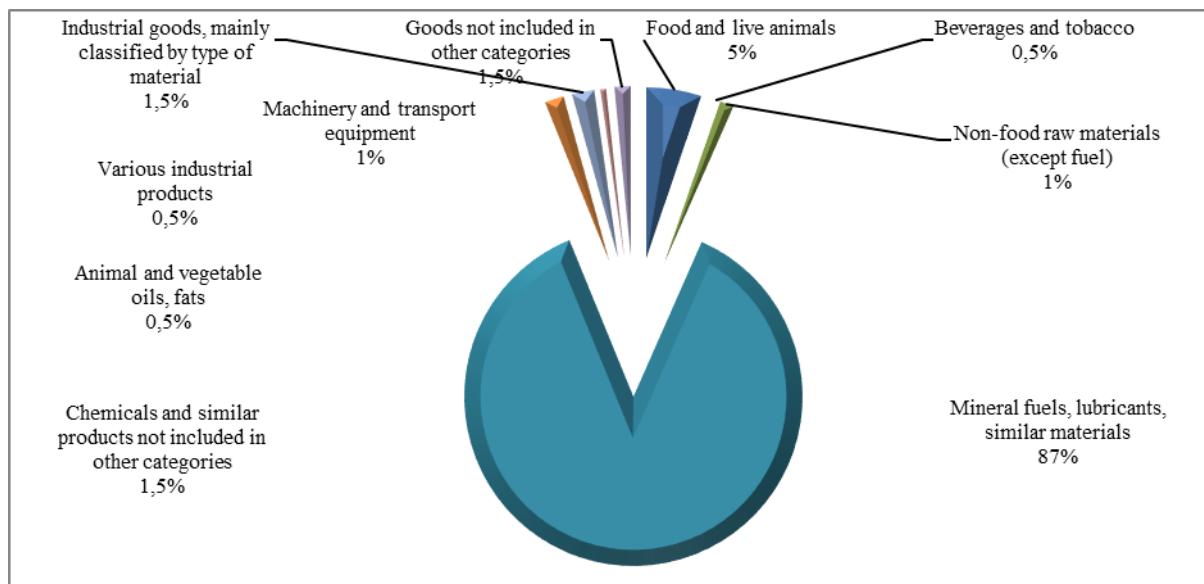


Picture 10. Unemployment level of Azerbaijan, in %, 2005-2020 (prepared on the basis of ARSSC data - <https://www.stat.gov.az/>).

Starting with 2005 unemployment level in Azerbaijan decreased to 7.2% and to the end of 2019 it decreased to 4.8%. However, because of the negative impact of the pandemic, especially because of restriction of service sector activity the unemployment level increased, and to the end of 2020 it composed 7.2%. In the current situation the measures targeted to economics diversification and economic security strengthening gives reason to predict the decrease of unemployment rate again. In regards to this, in the coming years and primarily in the post-pandemic period the more efficient organization of the activities which are important for the economic security of our country and acceleration of improvement of the existing mechanisms are required.

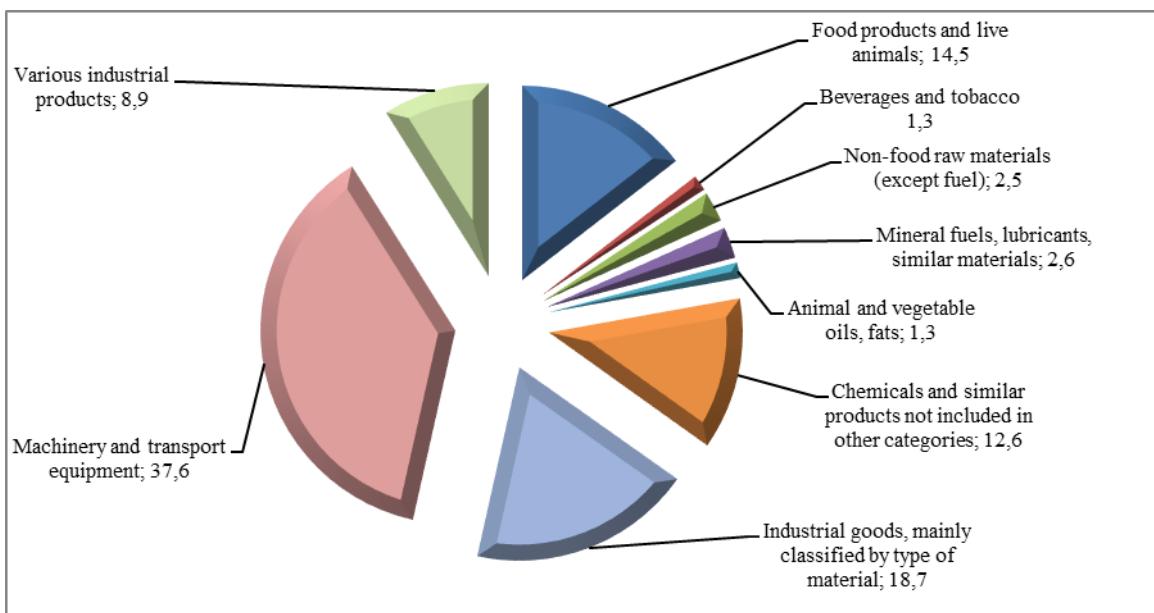
5.3. The issues of diversification of the foreign trade structure and export potential increase in the diversification of the economics in Azerbaijan

2005-2020 years in Azerbaijan are remembered for domestic production stimulation among the positive effects of foreign and domestic investment in economics and significant reduction in import dependence. During that period % 60-70 of the demand for most food and other consumer goods is provided by domestic production. At the same time, more fertile conditions were created to increase the export potential of non-oil and non-gas products. Thus, the processes of formation of national brands, state stimulation of access to world markets, application of the incentive mechanism in the amount of %3 of total value of exports for exporters attracts attentions. However, diversification of the export structure of the country remains to be one of the most difficult problems. In general, for many years the share of oil and gas raw material in the exports of Azerbaijan was more than %90, needless to say that Azerbaijan is mainly oil and gas country (see: Picture 11).



Picture 11. The export structure According to the International Standard Trade Classification in the Republic of Azerbaijan, in %, 2020 (prepared on the basis of ARSSC data - <https://www.stat.gov.az/>).

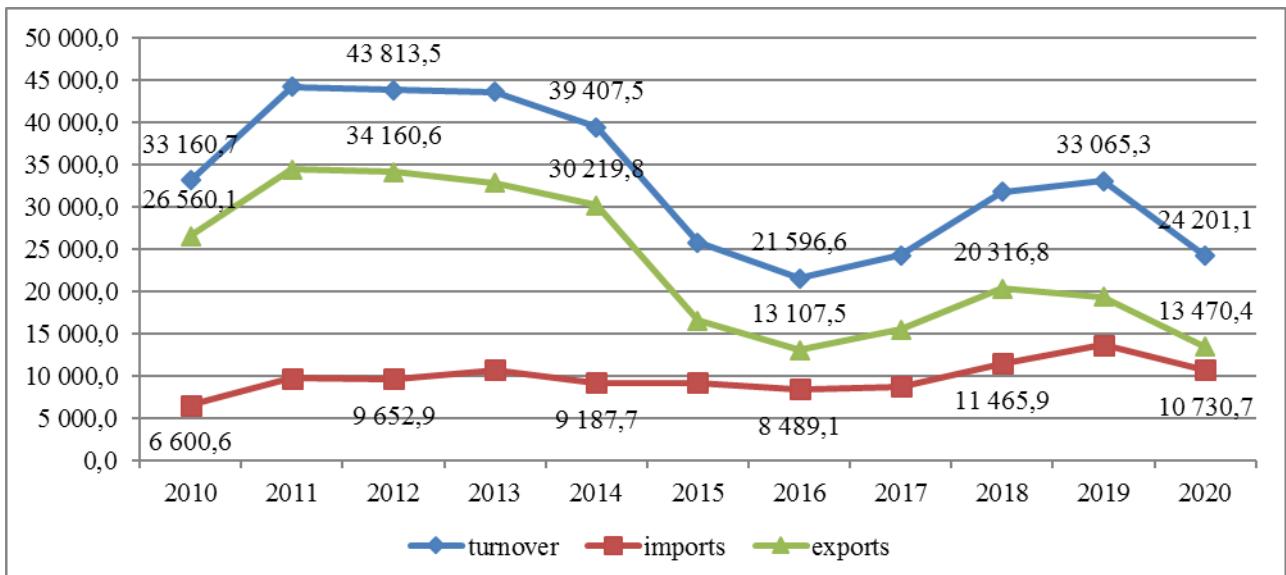
However the production and potential of export increase of the other export-oriented products, as well as products of competitive heavy industries remains strong. For example, there is a great possibility of increase in volume and expansion of the range of export oriented products on additional production chain in the chemical and petro-chemical industries. From the other hand, there are perspectives for increase of the food products and agricultural products export, and in recent years exactly in this direction the volume of non-oil and non-gas exports was significantly increased. As a strategic task the increase in the number of national brands depends on maximum efficient use of available export opportunities, as well as the volume of oil and gas refining in the food and light industries. In this case, the raw material basis is formed to increase the production of export-oriented products of processing industry, and mainly chemical and petrochemical complex. If we review the analysis of the import structure according to the International Standard Trade Classification in the Republic of Azerbaijan, we can see that more than %14 of the import in the country composes the food products (see: Picture 12).



Picture 12. Import structure according to the International Standard Trade Classification in the Republic of Azerbaijan, in %, 2020 (prepared on the basis of ARSSC data - <https://www.stat.gov.az/>).

In our opinion, it is possible to produce a significant part of these products in the country, but for this the stimulation of domestic production should have more active and attractive mechanisms.

In Picture 13 we gave the general dynamics of the foreign trade relations in the Republic of Azerbaijan, and as it can be seen foreign trade turnover, as well as the volume of import-export operations continues to decline in recent years. For example, in 2020 the general foreign trade turnover decreased by % 36.8 in comparison with 2019, the export turnover decreased by %44.8 and import - by % 28.



Picture 13. The general dynamics of the foreign trade relations in the Republic of Azerbaijan, in mln. US Dollar, 2010-2020 (prepared on the basis of ARSSC data - <https://www.stat.gov.az/>).

As we mentioned above earlier the impact of the Covid-19 pandemic is huge, but at the same time it would be great to take measures on diversification of non-oil relations and restoring the growth rate of total trade turnover

in the structure of foreign trade relations. Taking these into consideration can increase significantly the foreign trade activity factor in improving of the structure of the national economy, and in the formation of additional potential to increase the economic security and etc.

6. Discussion

Today Azerbaijan set the task of updating its economic development model and reducing the dependence of the national economy on oil and gas as a main target. Besides, the targeted measures are taken to increase the export potential and efficiency of export-oriented industries due to the expansion of the national brands structure. In 2020 a new model of economic zoning was formed in Azerbaijan, and Garabagh economic region as well as East Zengezur economic region was established. These regions have strong natural resources and high potential for tourism development. In addition, Azerbaijan increases natural gas production every year and had already started the natural gas exports to European markets. All these formed favorable opportunities for improvement of the national economics structure, taking important steps for more optimal diversification and economic security strengthening ways.

In connection with the above mentioned a group of questions can be submitted for discussion, and we hope that scientists and researchers from different countries of the world will join the controversy in these areas and will share their valuable insights: 1) What should be the main mechanisms of maximum efficiency of the economy in countries that do not produce energy resources in modern times? 2) How do you see the diversification of the national economy structure in the context of global threats? 3) Which components should be included into the components of the economic policy model of the state in economics diversification? 4) What is the importance of the selection and improvement of economic security indicators during a pandemic and especially under the post-pandemic conditions? 5) What should they do differently in the current situation for maximum efficiency of the state economics 6) How do you assess the current state of the national economy in Azerbaijan possessing the largest economy in the South Caucasus? 7) Was Azerbaijan able to create a national economic model which has durable mechanisms in terms of more balanced, diversified and economic health using oil and gas resources, and your thoughts on this?

We are pleased to express our readiness for joint research and discussions of the questions, and we consider that these shown questions and their content is one of the problems that worries most countries in the world. We hope that, joint research and identification of the more adequate solutions can accelerate the solution of the problems described in the article, and will accelerate the development of optimal mechanisms of action for this.

Methodology

This research adopts a qualitative and analytical methodology, combining:

Document and Policy Analysis

- Review of Azerbaijan's national development strategies, Strategic Road Maps (2016–2025), regional development programs, SOFAZ reports, and central bank policy documents.
- Examination of international datasets from the IMF, World Bank, UNCTAD, OECD, and regional organizations.

Comparative Economic Analysis

- Comparison of Azerbaijan's diversification trajectory with other resource-rich economies (Norway, UAE, Saudi Arabia, Kazakhstan).
- Examination of regional dynamics in the South Caucasus and wider Caspian basin.

Theoretical Framework

The research integrates:

- **Modern Portfolio Theory** (risk diversification and economic resilience)

- **Institutional Economics** (governance, transparency, rule of law)
- **Economic Security Frameworks** (anti-crisis resilience, vulnerability analysis)
- **Structural Transformation Theory** (sectoral shifts and productivity growth)

Expert Judgment and Observational Analysis

The author's long-term experience in practical economic management and teaching is used as an interpretive tool to assess structural constraints and opportunities within Azerbaijan's economy.

Conclusion

In the contemporary global environment, the pace, depth, and unpredictability of economic transformations have increased significantly. International economic systems face prolonged instability driven by geopolitical tensions, technological disruptions, climate transition pressures, supply chain restructuring, and the lingering socio-economic effects of the COVID-19 pandemic. These developments reveal that traditional models of economic management and resource utilization have become insufficient to address systemic vulnerabilities. As global challenges intensify, the need for adaptive, innovation-oriented, and security-centered development strategies becomes more apparent.

For resource-rich transition economies such as Azerbaijan, the imperative of comprehensive economic diversification and the strengthening of national economic security is both strategic and unavoidable. Azerbaijan's experience over the past three decades demonstrates substantial achievements—macroeconomic stabilization, the establishment of major energy corridors, regional development programs, and significant investments in infrastructure. However, the dominance of the hydrocarbon sector still constitutes a structural constraint, limiting resilience in the face of global oil price volatility and emerging competitive pressures associated with green transition and technological transformation.

In this context, Azerbaijan must prioritize a next-generation development paradigm that integrates **economic diversification, technological modernization, institutional strengthening, and proactive economic security policies**. Based on the analysis provided in this study, the following strategic conclusions and policy directions are essential for ensuring long-term sustainable development and national economic resilience:

Deep Structural Modernization and Resilient Development Model

Azerbaijan must advance a comprehensive re-evaluation of its national economic development model, embedding global trends such as the digital revolution, regional integration, energy transition, and post-pandemic restructuring. Fundamental research-based modeling should guide policy choices to ensure that development pathways are compatible with international challenges and future uncertainties.

A resilient economic model should be grounded in structural diversification, expanded value-added production, and robust economic security mechanisms capable of absorbing shocks and minimizing systemic risks.

Formation of High-Technological, Competitive Non-Oil Industries

Strengthening non-oil and non-gas sectors must become the core pillar of Azerbaijan's long-term economic architecture. This requires establishing:

- high-technology enterprises,
- sector-specific technoparks,
- multifunctional industrial parks,
- regional industrial districts, and
- innovation-driven export-oriented clusters.

The expansion of industrial output, particularly in chemicals, petrochemicals, metallurgy, machinery production, ICT, agro-processing, and textile industries, will significantly enhance diversification and reduce import dependence.

Regional Development, Industrial Clustering, and Investment Climate Improvement

Regional economic diversification requires intensifying industrial clustering, developing competitive agro-industrial enterprises, creating free economic zones, and building investment-friendly ecosystems. Strengthening the production base in medium-sized cities, including Sumgayit, Ganja, Mingachevir, and the liberated territories, will stimulate balanced regional development and reduce concentration risks. The proposed **Sumgayit Industrial Logistics Center**, a **household appliance production plant**, and a **Weaving and Sewing Special Economic Zone** represent practical, high-impact projects that could increase non-oil industrial output, reduce import dependence, and generate new export streams.

Establishment of a Modern Petrochemical and Gas-Chemical Complex

Given Azerbaijan's competitive advantage in hydrocarbons, the country should prioritize the construction of a modern petrochemical complex capable of producing at least 5 million tons of high-value-added products annually. This strategic project would contribute USD 5-6 billion in non-oil output, with over 90% export potential, thereby strengthening the country's balance of payments, industrial capacity, and economic security.

Innovation System Development and Human Capital Strengthening

The creation of a national innovation system remains a critical requirement. Developing legislation, institutions, and financing mechanisms for innovation-oriented industries is essential. Accelerated adoption of high technologies, industrial innovations, digital manufacturing, and advanced engineering solutions should be supported through:

- R&D incentives,
- university-industry collaborations,
- innovation financing mechanisms,
- technology transfer programs, and
- objective, transparent statistical systems for monitoring innovation performance.

Human capital development—especially in engineering, ICT, applied sciences, and management—must remain a priority.

Institutional Reforms, Transparency, and Competitive Economic Environment

Strengthening transparency, accountability, and institutional quality is central to forming a competitive, innovation-driven non-oil economy. The fight against corruption, enhancement of corporate governance standards, and reduction of administrative barriers must continue systematically to encourage entrepreneurship, innovation, and foreign investment.

Enhanced Role of the Private Sector and Foreign Investment

A vibrant private sector is indispensable for sustainable diversification. Thus, Azerbaijan must:

- increase private sector participation in industrial processing,
- expand entrepreneurial support mechanisms,
- attract competitive foreign investors into non-oil industries, and
- strengthen investment security and investor rights protections.

Sector-specific investment strategies are necessary to channel FDI into high-value-added industries rather than low-productivity, short-term sectors.

Strengthening Economic Security and Adapting to Post-Pandemic Realities

Economic security mechanisms must be modernized to reflect post-pandemic realities, including supply chain vulnerabilities, inflationary pressures, technological disruptions, and geopolitical fragmentation. Updated indicators, predictive analytical tools, and multi-sector early-warning systems should be integrated into national planning.

The post-pandemic period requires the identification of new value-added sources, productivity increases, service-sector expansion, and income growth strategies to maintain economic stability and social resilience.

GDP Structure Optimization and Export Diversification

Azerbaijan must continue improving the structure of GDP by increasing non-oil value creation, advancing service-sector development, and supporting productivity-enhancing industries. Export diversification—both in product range and geographic markets—is critical for reducing vulnerability to external shocks and strengthening foreign exchange inflows.

National Branding and Global Market Penetration

The formation of strong national brands in textiles, food products, machinery, chemicals, and digital services will increase the visibility and competitiveness of Azerbaijani products in global markets. Brand formation and quality certification must be integrated into national industrial and export strategies.

Macroeconomic Stability and Strategic Foreign Trade Expansion

Ensuring sustainable macroeconomic stability remains a cornerstone of economic security. Continuous foreign exchange inflows, improved trade balances, and diversified export baskets will minimize vulnerability to oil price fluctuations. Strategic expansion of trade relations—especially through Eurasian, Middle Eastern, and European markets—will further strengthen Azerbaijan’s geoeconomic position.

Final Remark

In conclusion, the future of Azerbaijan’s economic development depends on accelerating structural reforms, fully integrating diversification and innovation into national strategy, and modernizing economic security mechanisms to reflect the realities of a rapidly transforming global environment. The policy directions outlined in this study represent a comprehensive roadmap for strengthening the resilience, competitiveness, and long-term sustainability of Azerbaijan’s national economy. Building an innovation-driven, diversified, and export-oriented economic structure will not only reduce strategic vulnerability but also position Azerbaijan as a dynamic and influential economic actor in the South Caucasus and the wider Eurasian region.

Ethical Considerations

This study is based solely on publicly available documents, official statistical data, and academic literature. No human subjects, personal information, or sensitive datasets were involved.

All sources were reviewed and cited following academic integrity standards.

The research adheres to ethical guidelines for transparency, objectivity, and avoidance of conflict of interest.

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Conflict of Interest

The author declares **no conflict of interest** related to the analysis, interpretation, or publication of this study.

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