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GLOBAL SECURITY AND ECONOMIC ASYMMETRY: A COMPARISON OF DEVELOPED AND DEVELOPING COUNTRIES

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Abstract. This paper tackles the asymmetry of economic interests and geopolitics between developed and developing countries. Currently, the geopolitics presupposes that the majority of novel technologies are devised and designed in developed countries with their subsequent transfer to the developing countries. Moreover, in the context of the global crisis, the issue of de-dollarization is relevant from the political and economic points of view. Our specific focus is on the small oil countries and the issue how to get off the oil needle in the painless way. Furthermore, the paper analyzes the rise of cryptocurrency that is envisaged as the substitute of the U.S. dollar which has been the world most dominating currency for the last several decades.

This paper considers the global asymmetry which has the greatest impact on countries with economies dependent on energy exports. In the light of the diminishing returns from the sale of oil, we examine the ways for escaping this asymmetry. The authors consider the geopolitical asymmetry stemming from the dominance of the U.S. dollar, analyze the political situation and offer the pathways for the development of those economies where oil become an obstacle for economic development. The paper examines the ways of solving the above-mentioned problem by other states in detail and conduct the comparative analysis of the above issues in relation to the economy of Azerbaijan. From this case study we conduct a comparative analysis of the developed and developing countries taking into account the economic asymmetry and global economic and financial security.

Keywords: geostrategy, instability, anti-dollarization, business development, stock markets, gold standards, cryptocurrency,

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JEL Classifications: F30; F52; P10; P20

1. Introduction

International global security is pre-supposed by the asymmetry and polarization of hydrocarbon resources in a small group of developing countries and countries that yield the signs of the economies in transition (Balitskiy *et al.* 2014; Andreeva *et al.* 2016; Jobling and Jamasb 2017; Niño-Amézquita *et al.* 2017; Lisin *et al.* 2018). Historically, commodity markets have used U.S. currency as means of payment. However, active anti-dollar campaign is gradually unfolding in the world (Guliyeva and Rzayeva 2017). These efforts often lead to serious and not always positive and fruitful developments in global politics (Kalyugina *et al.* 2015; Koudelková *et al.* 2015; Andreeva *et al.* 2017). The purpose of the work is in discussing the following questions: What should be done to ensure that the rejection of the U.S dollar could be real and non-harming? What can the small develop-

ing country's economy expect in global crisis, falling prices for raw materials and devaluations? The novelty of our work is in studying the structure of the Azerbaijani economy, aimed at getting rid of the "resource curse" - a theory that points to the relationship between large revenues from the export of natural resources and the weak economic development. The Azerbaijani economy is used as an example and a case study that is capable of revealing valuable information and insights.

The aim of this paper is to investigate the global asymmetry which is caused by the dominance of the dollar and has the greatest impact on countries whose economies depend on energy exports. Namely, the following problems need to be tackled and the following questions need to be answered:

- What would be the suggestions for the ways for escaping the global asymmetry in the light of the diminishing returns from the oil sale?
- How to conduct a critical analysis of internal market's structure and find out why raw materials and semi-finished products are mainly dominated in the exports of developing countries?

With regard to the objectives outlined above, this paper is set to examine the steps that Azerbaijani policy-makers should take towards the development of the non-oil sector. For the purposes of this paper, we are not taking into consideration such sectors of economy as tourism, agriculture, ICTs and other related branches. Moreover, this paper is aimed as presenting the authors' own novel vision of solving the de-dollarization problem from positions of a small developing country represented hereinafter by Azerbaijan.

2. Background and literature review

According to Lemann (2011), it was Andrew W. Marshall, the director of the United States Department of Defense's Office of Net Assessment, who was one of the first to apply the term "asymmetry" to the military-political sphere. Marshall paid attention to possible asymmetric warfare with such, apparently, symmetric opponent as the USSR. Actually, at first the term "asymmetric relations" had a military strategic importance and only later became widely used in the political and economic reasoning. In addition, Scholvin (2016) reveals in detail how asymmetry turned out to be an important aspect mostly in each known form of geopolitical relations. Furthermore, Meinhardt (2002) points out that the asymmetric strategy always presents in relationships. Arreguin-Toft (2001) suggests that all modern asymmetric conflicts can be understood when they are considered through the prism of the strategy and concludes that asymmetry is a strategy and strategy is an asymmetry.

Moreover, Bourguignon and Morrison (2002) describe national economics in the framework of the world economy and international economic relations in the 1990s and 2000s are also characterized by the asymmetry of the states' developments. This was reflected primarily in the greater inequality between them. The system transformation crisis of the 1990s changed the place of the post-Soviet countries quantitatively and qualitatively, throwing them back far back (Zlyvko *et al.* 2014). According to King (2009) and Lau *et al.* (2000), successful development of China's economy against the background of post-Soviet countries' national economies also increases asymmetry of the world economy. Investigating relations with Asia (Schaffer, 2002) determines that even within certain, especially large multinational countries, there is practically no homogeneity of economies and asymmetry in their development is also observed. This fact also applies to such a stable regional community as the European Union (EU).

The greatest asymmetry of interdependence is inherent in the relations of developed countries with the most backward and poor countries of the world. The latter do not have the resources of strategic raw materials, they are not competitive producers of industrial and consumer goods and are not promising markets for the products of developed countries. These countries incidentally, depending on environment of commodity markets, can influence reproduction in the industrial center; however, essential dependence on this center dominates in system of their world economic relations. Including Azerbaijan, the economic dependence of developing countries on developed countries is manifested primarily in the fact that developed countries are "pure" exporters of capital to developing countries, whereas developing countries are in fact the debtors of developed

ones. In foreign trade, economic dependence is manifested not only in the overall asymmetry of exports and imports, but also primarily in their market's commodity structure (Ehrenberger *et al.* 2015; Varanavicius *et al.* 2017). Raw materials and semi-finished products are mainly dominated in the exports of developing countries. Today USA represents the largest importer of oil and the only "superstate" which monopolized the right – in the sphere of geopolitics of fuel – to convert geopolitics of spaces into geopolitics of streams, geostrategy to geo-economy and vice versa. In response, there is a tightening of access policy for hydrocarbon resources by oil-producing countries, called "resource nationalism". The geopolitics of asymmetry, unexpectedly forming the fanciest combinations for reaching the real horizons of multipolarity, today is not restrained by any ideological, confessional, political or social criteria (Strielkowski *et al.* 2016).

With regard to the above discussion, one can see that the Azerbaijani government put its bet on the development of non-oil sector. Currently, such fields of economy as agriculture, tourism, information technologies and textile industry are being invested as an alternative to the "oil needle" (Tvaronavičienė *et al.* 2015; Zemlickiene *et al.* 2017; Veselovsky *et al.* 2018). With regard to this, the development of entrepreneurship which occupies an important place in social and economic policy, might be seen as a key element of the investment processes. In addition, investment processes define scientific and technical progress, modernization of economy, growth rates of branch and regional economies in essential degree (see e.g. Vasylichak and Halachenko 2016; Jankeľová *et al.* 2017; Melas *et al.*, 2017; Tvaronavičienė *et al.* 2018). Our paper considers the current state of this economic area, presents the dominant indicators for Azerbaijan in this sector. As a continuation of the theme of entrepreneurship development, the authors examine in detail the stock market, considering that economy is based on the functioning of the corresponding financial system, and the most important place is occupied by the financial market on which there is the movement of money (capital).

3. Main research focus: issues and controversies

Modern researches note a relatively high degree of asymmetry in the geopolitics of energy and fuels. This is because the processes of the global economy are often characterized by both uniqueness and high degree of uncertainty (Brożyna *et al.* 2018; Iorio *et al.* 2018). As a result, forecasting the situation with geostrategic instability is difficult to assess, and therefore, there are difficulties associated with obtaining reliable information about it. The authors' research aims to assess the degree of information asymmetry in the context of this phenomenon's significance for developing countries, taking into account their absolute dependence on the dollar.

It is difficult to overestimate the role of oil in the economy of Azerbaijan. In Azerbaijan, smaller proportion of employed in the industry gives more of GDP, reflecting the predominantly mineral-raw material orientation. Recently there was a favorable situation on the world market for raw materials. Thanks to the global economic crisis, the "resource blessing" has turned into a "resource damnation". This theory points to the interrelation between large revenues from the natural resources' export and the weak economic development of the country and reflects the suppression of market development and the decline of other economic sectors' competitiveness, the increase of the national currency, inflation and unemployment.

One can see that the abnormal revenues from the mineral resources' export, as well as an excess of this resource within the country generate deformation of economy in all cases, regardless of the political system and the applied economic policy (Karl, 2007). Correlation of the rate of Azerbaijan GDP's growth with the oil prices' growth rate on world markets represents a parallel process. It is important to emphasize that this is not even a correlation with the rate of oil prices, namely with the rate of prices' growth, i.e. for the growth of the Azerbaijani economy. How to solve the resource damnation problem?

Quickly coping with the Dutch disease, the symptoms of which are evident in Azerbaijan is impossible. There are no simple recipes here. Nevertheless, the problem of price volatility and export revenue is solved quite simply. If we know that oil prices sharply change, we can save them for a rainy day, for those periods when there is a decrease in income. Countries that export resources - oil, gas, and so on - can create so-called national welfare funds that have two goals. The first is the savings purpose designed to postpone a part of the income from

oil for pensions and tax exemption in future. The second purpose of such funds is stabilization funds directly connecting with volatility. Oil prices are falling: we take means from these funds and spend for current needs. When the prices are high, then, on the contrary, we keep our large income in the fund. Accordingly, we smooth out state revenues and solve budget problems. However, there are problems with stabilization funds. Oil prices are volatile, but, as economists often say, they are sustained, and if they fall, they can stay on a very low level for a very long time (Knittel and Pindyck 2016).

Not only the oil countries possess the national welfare funds, there are metal funds, copper funds, there are funds completely unrelated to raw materials, as in China and Singapore. The largest fund is the Government Pension Fund of Norway. The Norwegian government does not spend money coming from oil and gas but lives only on interest.

The State Oil Fund of the Azerbaijan Republic was established in 1999 (actually began to operate in 2001). The revenues of the State Oil Fund are formed, first, by selling oil remaining at the disposal of Azerbaijan in accordance with production sharing agreements. In addition, the fund receives income from the concession of land in oil-bearing areas, the leasing of fixed assets, oil transit, the difference between the contractual and sales price of exported oil, as well as bonuses and income from the profitable use of assets.

The oil exporting countries are trying to change the development model based on the export of this raw material. However, the strategies of economic modernization need to be reoriented to new sources of national income. A purposeful economic policy can ensure the effective use of foreign exchange earnings from oil exports, and therefore the role of financing advanced sectors of the economy based on ICT raises. Developing countries seek to shift economic growth from the oil and gas production sector to sectors not related to the extraction and sale of crude oil and natural gas in order to reduce dependence on exhaustible oil reserves, the volatility of the world oil market, to change the economic structures based on foreign labor, to solve the problem of social burden on the budget.

4. Entrepreneurship and economic development

At the present stage of Azerbaijani economy development, foreign investments are directed mainly to the oil industry. However, proportional economic development requires redirection of revenues from the sale of oil and oil products to the development of the non-oil sector. The increase in investments is necessary for the purposes of economic growth, limiting inflation and unemployment, creating new jobs. Registration of companies in Baku is carried out on the basis of unified principles, which are prescribed at the legislative level. The process of creating a limited liability company is very simple: it requires only 7 procedures and 11 days. This is much faster than the corresponding average for the countries of Eastern Europe and Central Asia. The whole process can be done online and registration usually takes 2-3 days. Currently, there are no restrictions on the minimum authorized capital. Article of the Civil Code of the Republic of Azerbaijan states that the amount of the authorized capital cannot be less than the amount established by the relevant executive authority.

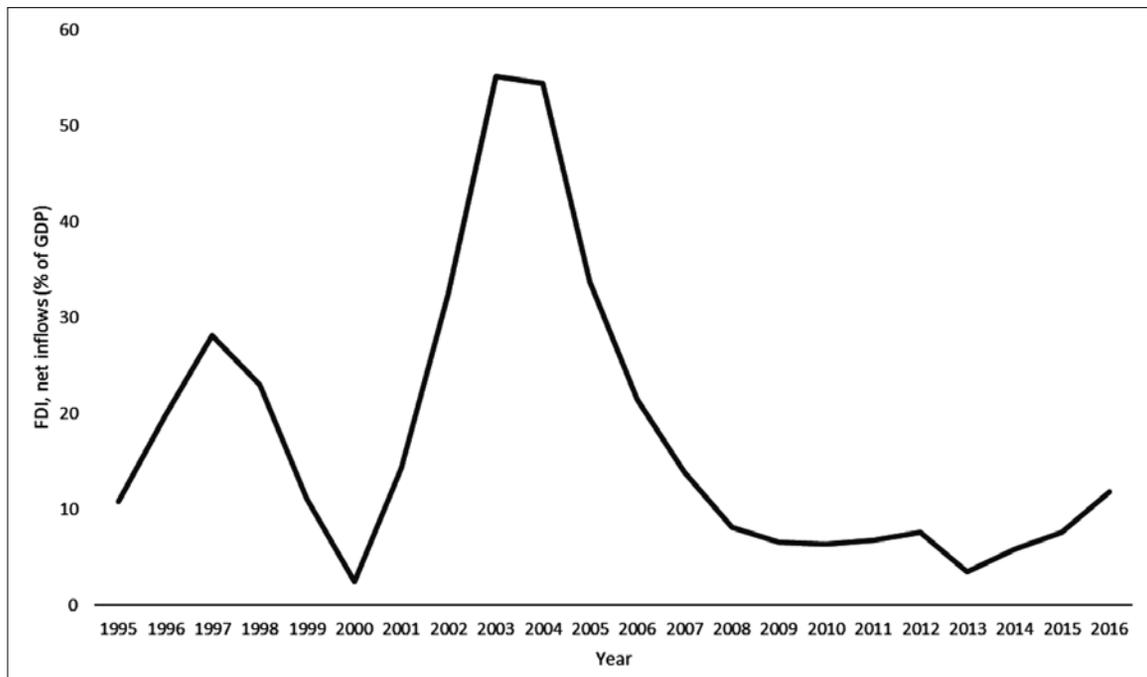


Fig. 1. Foreign Direct Investment (FDI) in Azerbaijan (1995-2016), % of GDP

Source: World Bank (2018)

Land is granted only for rent to persons who are not citizens of the Azerbaijan Republic, individuals and legal entities of foreign countries. Some lands constitute the exclusive property of the state; rules of their usage and leasing are carried out in the order prescribed by law. The lease cannot be longer than 99 years. As a rule, contracts are usually concluded for 30 years and give the right to divide the land into sublease or leased land. There are no restrictions for the maximum quantity of land resources, which can be concentrated in one hands. In Azerbaijan a geographic information system providing the collection, storage, processing, access, display and dissemination of spatially coordinated data (spatial data) and, accordingly, centralization of information in one access point is absent. Foreign direct investments in Azerbaijan in the fourth quarter of 2016 increased by 1895 million US dollars, reaching a record level of 2231 million US dollars in the fourth quarter of 2014 and a record of 586 US million dollars in the third quarter of 2009 (Figure 1). Compared to the beginning of the 21st century, the overall investment climate in Azerbaijan is gradually improving, although serious problems remain.

The paradox is that everyone knows about these problems, but they remain unresolved, giving rise, in turn, to new problems. Over the past few years, the Azerbaijani government has worked to integrate the country more fully into the world market, attract foreign investment, diversify economy and support growth. GDP growth of 2.8% in 2014 was due to non-oil economy and long-term public investment (Figure 2).

About 95% of the export income of Azerbaijan is the share of oil and gas products (Figure 2). Economic diversification and large foreign investment for the further development of energy sector are declared as government's goals but ineffective state bureaucracy, weak legal institutions, requests for illegal payments for cross-border operations and predatory behavior of related monopolistic interests prevent investments at non-oil sector and present problems for foreign companies. Over the past few years Azerbaijan has been working to improve its regulatory system, but limited transparency and allegations of corruption remain key problems in this area. According to the legislation of Azerbaijan, foreign investors can engage in investment activities not prohibited by law.

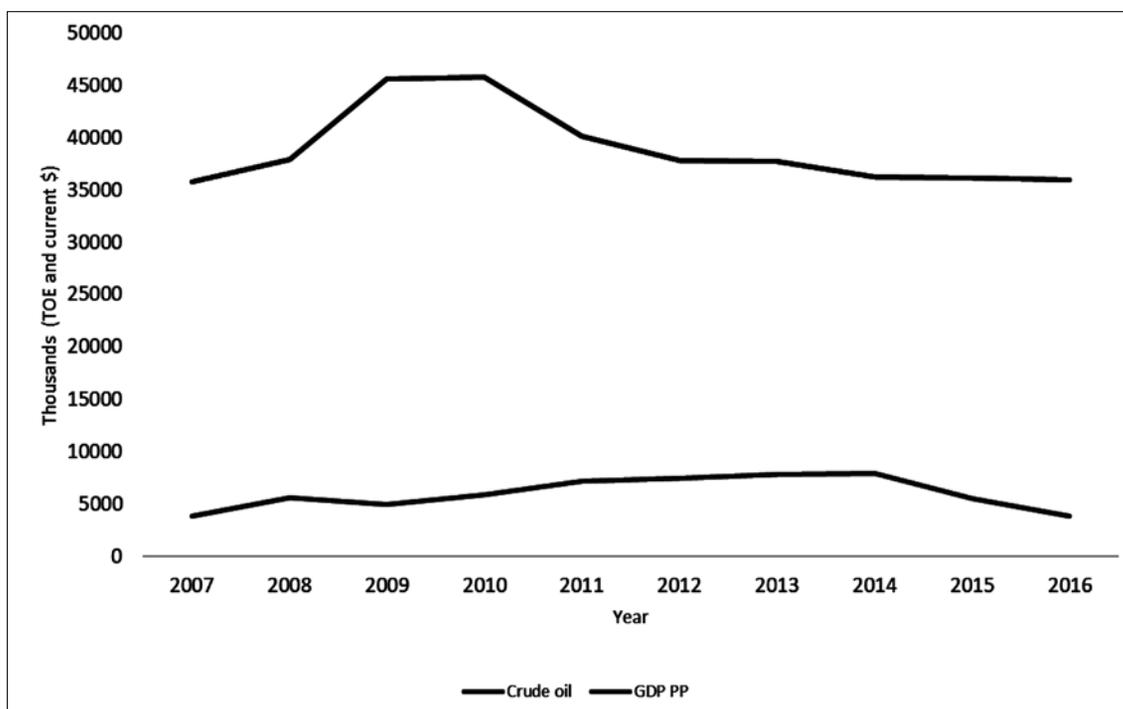


Fig 2. Azerbaijan GDP per capita (current \$) and crude oil extraction (thousana of TOE) in 2007-2016

Source: World Bank (2018) and Azerbaijan Statistical Committee (2018)

When it comes to business acquisition in Azerbaijan, private entities can freely create, acquire and dispose of interests in enterprises. The Law on the Protection of Foreign Investments protects foreign investors from nationalization and requisition, with the exception of certain circumstances. In February 2015, Azerbaijan devalued its local currency manats (AZN) by 35% in order to adapt to the decline in oil prices, putting pressure on the currency reserves of the Central Bank. Then in December 2015 there was a second devaluation of 48%. In general, however, there are no restrictions for converting or transfer of the means connected with investments in freely used currency at the market rate. The sphere of financial services is weakly competitive both on the external and internal markets. Corporate social responsibility is a relatively new concept in Azerbaijan, and is associated only with assistance programs.

5. Securities market and the investment policy

In the economy, there is a constant turnover of financial resources, which subjects are households, enterprises, the state and various financial institutions acting as intermediaries in the system of relations. In the process of management, some subjects have a need for means to expand their activities, while others accumulate savings. The distribution of means occurs through the formation of funds: centralized or owned by the state and decentralized or owned by the subjects of production. Until recently, the Azerbaijani government has practically ignored the possibility of attracting the population's financial resources for infusion into the national economy. Practically bank deposits remained the only financial instrument to fill up the budget for the population. Nevertheless, two waves of devaluation of the national currency called "manat", and further closing of some banks (as of today, from 45 banks remained acting 33 credit institutions) considerably lowered trust of population to the banking system. In the developed countries of the world, income from securities is an important additional source of money for the population. The population provides the bulk of investment in the stock market, if it has incomes that exceed consumption costs. If the consumer has a larger disposable income, then more goods will be produced and imported. There are special indicators characterizing the willingness of consumers to spend money on the acquisition of various goods. Some of these indicators are important for foreign exchange markets, as well as high consumer demand stimulates the recovery of production in many sectors and can serve as a basis for economic growth. Conversely, the weakness of consumer demand or its decline are the signals and may become the cause of a slowdown in the economy. Focusing on these indicators, central banks can change interest rates or use other levers of financial policy, which directly affect the exchange rates.

In view of the fact that many economic indicators show economic cycles, but each of them does it in its own way, it is natural to attempt constructing from several indicators one which, thanks to the generalization (averaging), would better predict the cycles than each does individually. The composite leading indicator – *Leading Economic Indicator (LEI)* combines 11 indicators for this purpose:

- Average duration of the working week in the manufacturing sector;
- Average weekly number of applications for payment of state unemployment insurance;
- New production orders for consumer goods and materials;
- Efficiency of deliveries;
- Contracts and orders for capital goods and equipment;
- Obtaining permits for housing construction;
- Unfulfilled production orders on durable goods;
- Change in prices for raw materials;
- Stock Index S & P500;
- M2 Monetary aggregate;
- Consumer expectations index (University of Michigan's Consumer Expectations Index).

The LEI is based on the idea that the main motivating force in the economy is the expectation of future profits. In anticipation of profit growth, companies are expanding production of goods and services, investing in new plants and equipment; accordingly, this activity decreases when a decline in income is foreseen. In Azerbaijan the GDP YoY (year over year) shrank 0.9 percent year-on-year in January-May of 2017, compared to 4.2 percent contraction a year ago. LEI in Azerbaijan averaged 9.87 percent from 2006 until 2017, reaching an all time high of 116.10 percent in September of 2012 and a record low of -4.50 percent in April of 2016.

Index of Consumer Confidence is an attempt to measure consumer optimism, has a limited impact on the market, as it may not reflect the real state of the economy. However, it is traditionally used to forecast trends in employment and the general state of the economy. The growth of the index value is a positive factor for the development of the national economy. As a reflection of the economic situation, consumer confidence in Azerbaijan declined in the third quarter of 2014 to 23.80 points, being 25 points in the second quarter of 2014. Consumer confidence in Azerbaijan averaged 25.25 from 2013 to 2014, reaching a maximum of 26.35 points in the first quarter of 2014 and a record low of 23.80 points in the third quarter of 2014. Personal Income index includes the salaries of workers and employees, income from rent, dividends, income from bank interest, payments for social insurance, etc. Personal income in Azerbaijan increased from 35.924.80 million manats in 2014 in to 37,948.30 million manats in 2015. This indicator averaged 24101.00 million manats from 2000 to 2015, reaching a record level of 37.948 million manats in 2015 and a record low of 3748.00 million manats in 2000.

Personal Spending (Consumption) index reflects the change in spending of funds to meet personal needs. Has a limited impact on the market. Consumer spending in Azerbaijan increased from 9.94 bn manats in the third quarter of 2016 to 9.125 bn manats in the fourth quarter of 2016. This indicator in the period from 2001 to 2016 averaged 3.767.86 million manats, reaching a maximum of 9,190.40 million manats in the fourth quarter of 2015 and a record low of 700 million manats in the first quarter of 2001. CPI represents the main indicator of inflation, measures the changes in the goods and services' prices included in a fixed consumer basket. This indicator increased from 141.40 points in December 2016 to 144.70 points in January 2017, an average of 115.69 points from 2011 to 2017 and reaching a record level of 144.70 points in January 2017. The minimum record was fixed at the level of 105.30 points in January 2011.

As mentioned above, population is the main supplier of resources to the stock market. Credible figures for Azerbaijan, disclosed above, leave no chance on successful development of this economic sector. Let us consider this situation in more detail. The securities market in Azerbaijan was established at the beginning of the 20th

century. Back in 1900, promissory notes and interest-bearing securities were issued in banks operating in Baku. The first shares were issued in 1913 after the approval of the Baku Merchants Bank's Charter. In the era of the Azerbaijan Democratic Republic, the bill market also developed, but during the Soviet period it was limited.

On December 30, 1998, after the restoration of independence the State Committee for Securities was established to create and develop the securities market. The Committee is engaged in the adoption of regulations in the securities market, the emission and turnover of shares, the activities of securities market participants and investment funds, the licensing of related activities, as well as the market for debt securities. As shown in Musayev (2012), the economic reforms carried out in Azerbaijan in recent years have ensured the creation of an economic system operating on the basis of free market relations. The fundamental institutions of the market economy have been formed, including the legislative framework that consolidates new economic relations. For the stock exchange's work securities that will interest all must be issued. In Azerbaijan, such large joint-stock companies as the State Oil Company of the Azerbaijan Republic (SOCAR), the organization for providing electricity to the country AzerEnerji, etc. belong to the state. As for public companies, they are open only formally, but in reality, too, belong to the state. Potential buyers do not believe that over time competitive monopoly organizations will give an opportunity to develop enterprises.

Nobody wants to share with part of own enterprise. However, the shares are essentially related to the transfer of part of the ownership rights to the shareholders. In addition, finally, as another reason of underdevelopment of the stock market in the country, we can cite the following argument – in Azerbaijan, there are few qualified personnel able to become, for example, independent brokers. Thus, the model of the undeveloped securities market in Azerbaijan is characterized by the fact that there are practically no national investment resources, national production cannot effectively consume foreign investment.

As noted above, oil is a trump card of all geopolitics, and the countries that have this card try to use it. The fact that foreign oil companies with billions of debts' dollars, will pay for Iranian oil in euro, create the idea of the similar practices' introduction in our country. Nevertheless, can Azerbaijan refuse the dollar in foreign trade and switch to the euro after two devaluations? And do we need this? For Azerbaijan, such step would be extremely dangerous, because limited influx of dollars is the main cause of instability in the financial market at present. The fact is that 90% of our exports are oil and oil products. The country has very few other dollar revenues. The price of oil is falling: the volume of the dollar coming to the republic is dropping, and the Central Bank is beginning to spend its foreign exchange reserves. The value of gold expressed so far in U.S. dollars, immediately starts to grow rapidly, both against the dollar, and against all goods-works and services. After a while in a certain market-defined trading range the oil-gold ratio will be stabilized naturally and the dollar will simply fall out of the formula which determines the price of oil and gold. On the contrary, the value of the dollar will begin to be measured in gold, as it should be and as it was throughout the entire monetary history of humankind. The value of national currencies has always been valued in money (i.e. in gold).

6. Conclusions and discussions

All in all, our results indicate that the accumulation of huge monetary and financial resources has an ambiguous impact on the economy of oil-producing countries. On the one hand, it creates unprecedented financial conditions for boosting the economic development of these countries. On the other hand, it generates such problems as, for example, inflation growth, deepening of structural disproportions (flawed development of the "non-oil" sector), and difficulties in the social sphere. The development of entrepreneurship is closely linked with the development of small enterprises, the formation of the middle class and is conditioned by both internal and external factors. Investment activity is associated with the processes of the labor international division, attracting foreign investment, the investment projects' development.

The modern structure of the world in the postindustrial information space becomes very vulnerable. Therefore, in the very near future the development of oil fields with the correct configuration of the innovation process can move from massive technologies, requiring huge economic and industrial resources to point high-tech modules,

whose development requires not so much capital investment, as creative flexibility and avant-garde approach. The developing countries, of which Azerbaijan is an integral part of, should develop this side of strategic asymmetry in priority.

The main problem is the issue of the possibility of financial resources' rational usage within the country for the purpose of its social and economic development. The desire to master other markets in the face of the declining efficiency of investments in the development of new oil resources can be considered as the most important prerequisites for the transition to a non-primary economy. This process disposal of raw dependence can be intensified by increasing investments in entrepreneurship and development of the stock market. The strategic goal of economic development of any country is foreign investments' attraction. Foreign direct investments are of significant importance, they characterize the long-term interest of foreign investors in the development of economic activity. The stock market develops when investors appear on it.

In today's world and under the current conditions, one has to state that countries like Azerbaijan should treat the idea of de-dollarization more restrainedly. First, if the country switches to calculations for oil and gas in manat, then the budget will lose additional income from devaluation. To date, since the beginning of the year, manat has depreciated more than 100% against the dollar and the euro. Transformation of manat into the international currency with a high probability will not lead to the stabilization of the national currency, but to its even greater volatility. Conversion of currency into freely convertible means that its circulation is not limited in any way, the state cannot influence it in any way, and its rate is determined only by speculation on the stock exchange. In this case the dependence on the dollar is only strengthened.

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