THE MINISTRY OF EDUCATION OF THE REPUBLIC OF AZERBAIJAN

AZERBAIJAN STATE UNIVERSITY OF ECONOMICS

INTERNATIONAL CENTER OF GRADUATE EDUCATION

MASTER DISSERTATION

on the topic

“WAYS OF ATTRACTING FOREIGN INVESTMENTS IN KARABAKH ECONOMIC REGION”

Rasul Alizada Tabriz

BAKU – 2022

THE MINISTRY OF EDUCATION OF THE REPUBLIC OF AZERBAIJAN

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Elm andı

Mən, Əlizadə Rəsul Təbriz oğlu and içirəm ki, “Ways of Attracting Foreign Investments in Karabakh Economic Region” mövzusunda magistr dissertasiyasını elmi əxlaq normalarına və istinad qaydalarına tam riayət etməklə və istifadə etdiyim bütün mənbələri ədəbiyyat siyahısında əks etdirməklə yazmışam.

QARABAĞ İQTİSADİ RAYONUNA XARİCİ İNVESTİSİYALARIN CƏLB EDİLMƏSİ YOLLARI

XÜLASƏ

Tədqiqatın aktuallığı: Qarabağ iqtisadi rayonunun işğalda olan ərazilərinin azad olunmasından sonra əsas tapşırıq həmin bölgənin iqtisadi bərpası və inkişafıdır. Hökumət tərəfindən bu istiqamətdə mühim investisiyalar edilsə də, xaricdən cəlb ediləcək sərmayeyə böyük ehtiyac vardır. İqtisadiyyatın dirçəldilməsi və inkişafı üçün bölgəyə xarici investisiyaların gətirilməsi yollarının araşdırılması olduqca aktualdır.

Tədqiqatın məqsədi: Tədqiqatın əsas məqsədi Qarabağ İqtisadi Rayonuna xarici investisiyaların cəlb edilməsi yollarını tapmaqdır. Bu çərçivədə regionun mövcud vəziyyətinin təhlili, investisiyalar üçün üçün ən yaxşı sahələrin müəyyənləşdirilməsi və görülməli olan işlərin dəqiqləşdirilməsi aparılıb.

İstifadə olunmuş tədqiqat metodları: Tədqiqatda regionun investisiya potensialı baxımından cari vəziyyətinin öyrənilməsi üçün GZİT təhlil metodundan, dünyanın oxşar bölgələrində sınanmış metodların Qarabağda tətbiqi imkanlarının qiymətləndirilməsi üçün müqayisəli təhlildən istifadə edilib.

Tədqiqatın informasiya bazası: Beynəlxalq investisiyalara dair son illərdə nəşr olunmuş elmi məqalələr və kitablar, həmçinin beynəlxalq təşkilatlar və yerli dövlət qurumları tərəfindən təqdim olunan statistik məlumatlar tədqiqatın əsas informasiya bazasını təşkil edir.

Tədqiqatın məhdudiyyətləri: Hazırda regionun mövcud vəziyyətin ətraflı təhlili, demək olar ki, yoxdur. Bu, tədqiqat üçün məlumat bazasının kasad olmasna gətirib çıxarır. Bölgədə məskunlaşmış əhalinin və iqtisadiyyatın olmaması "sahə tədqiqat"ını mümkünsüz edir.

Tədqiqatın elmi yeniliyi və praktiki nəticələri: Qeyd edildiyi kimi, hazırda regionun investisiya potensialının ətraflı təhlili mövcud deyil. Bu tədqiqat işində bölgədə investisiya baxımından cari vəziyyət araşdırılaraq təqdim edilib, digər ölkələrdə işlədilmiş mümkün həllər qiymətləndirilib.

Nəticələrin istifadə oluna biləcəyi sahələr: Bu tədqiqatın işğaldan azad edilmiş bölgəyə xarici investisiyaların cəlb edilməsində tətbiqi sahələrinin öyrənilməsi və onların həmin ərazilərdə tətbiqi üçün stimullaşdırıcı qüvvə olması mümkündür. Tədqiqatın nəticələri və verilən təkliflər dövlət investisiya siyasətində işlədilə, həmçinin Şərqi Zəngəzur rayonuna da şamil oluna bilər.

Açar sözlər: Xarici investisiyalar, Qarabağ iqtisadi rayonu, investisiya mühiti, dövlətin investisiya siyasəti.

WAYS OF ATTRACTING FOREIGN INVESTMENTS IN KARABAKH ECONOMIC REGION

SUMMARY

The actuality of the subject: After liberation of occupied territories of Karabakh Economic Region, main task is economic recovery and development of the region. Although the government has made significant investments in this area, there is a great need for foreign investment. It is very important to study ways to bring foreign investment to the region to revive and develop the economy.

Purpose and tasks of the research: The main purpose of study is to find ways to attract foreign investment to Karabakh Economic Region inlcuding analysis of the current situation, deciding the best areas to for investment and defining works that need to be done.

Used research methods: The study used SWOT analysis method to study current investment potential of region and comparative analysis to analyze feasibility of applying methods tested in similar regions of the world in Karabakh.

The information base of the research: Scientific articles and books on international investments published in recent years, statistics provided by international organizations and local government agencies, form main information base of the study.

Restrictions of research: The region is newly liberated. Thus detailed analysis of the current situation is almost non-existent. This leads to lack of database for research. Also, the lack of inhabited population and economy in the region makes field research impossible.

The novelty and practical results of investigation: As noted, there is currently no detailed analysis of the region's investment potential. This study examines and presents the current investment climate in the region and evaluates possible solutions used in other countries.

Scientific-practical significance of results: Areas of application of this research in attracting foreign investment to the liberated region will be studied and will be a stimulating force for its application in those areas. Results of the study and the proposals made can be used in public investment policy and can also be applied to East Zangazur Region.

Keywords: Foreign investments, Karabakh economic region, investment climate, state investment policy.

ABBREVIATIONS

UN	United Nations
SNA	System of National Accounts
EU	European Union
OECD	Organization for Economic Co-operation and Development
FDI	Foreign Direct Investment
IMF	International Monetary Fund
SEZ	Special Economic Zone
SME	Small and Medium Enterprise
SOE	State-Owned Enterprise
ICAO	International Civil Aviation Organization
IATA	International Air Transport Association
PSA	Production Sharing Agreement
AFEZ	Alat Free Economic Zone

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INTRODUCTION

Relevance of the research topic: The territory of the Karabakh Economic Region has been liberated from the occupation in 2020. The next task that has to be done is to reconstruct the infrastructure, build the economy and create facilities for social services to integrate the region into the economy of the country and make proper conditions for displaced people who are going to live there.

Rebuilding the economy is a very difficult and complex issue. It requires large resources, enough time, and competent management. Of course, the main burden in this area falls on the state. He, in turn, must allocate a budget to the region and carry out construction work. However, in the current period - in the context of globalization and close integration of the country's economies, the role of public investment in the economic revival of the regions should not be decisive. It is very important to attract foreign investors to these regions and attract investment. Especially in regions such as Karabakh, where infrastructure and the economy have been destroyed, the field for foreign investment is more favorable and the need is greater.

Foreign investment can ensure the rapid development of the region by bringing with it world experience, fast and cheap construction methods, efficient management technologies, money, and other resources. it will also lead to the parallel implementation of huge projects that the state and domestic investors cannot do on their own.

On the other hand, thanks to foreign investment, it is possible to gain the support of the investor country in the international political arena. This is very important, given how much attention the region we are talking about is in the political context.

Thus, taking into account many factors, it is now quite important to research the ideas of attracting investments to the Karabakh Economic Region. The above makes the topic of the dissertation very relevant.

Statement of the problem and learning level: The process of researching the topic is reflected in the scientific works of various foreign and local experts including Ph.D. Ahmadov B., Ph.D. Mammadov Z, doc. Mehtiyev A., Ph.D. Brueckner M., Ph.D. Broers L., Rober E. Lipsey and so on. The topic is also analyzed in international and national statistical reports.

Research shows that a large number of scientific articles, books have been published on the subject, and also relevant international statistics from World Bank, IMF, OECD, State Statistical Committee of Azerbaijan and so on. All this greatly simplifies the research.

The study is based on scientifically researched foreign and local specialists on the subject, official information from local and foreign media, and other official internet resources.

Purposes and objectives of the research: The study's main purpose is to find ways of attracting foreign investments in Karabakh Economic Region. In this regard, objectives of the research are followings:

1.Analysing the current situation and investment potential of the Karabakh economic region.

2.Deciding the best areas to attract foreign investment in.

3.Suggesting the ways of attracting foreign investment in the region to boost economic reconstruction.

Object and subject of the research: The object of the study was identified as the Karabakh Economic Region. The subject of the study is the investment climate of the region and the investment policy of the state.

Research methods: Countries have been investing in each other for a long time as part of the integration of world economies. As a result, there is a fairly comprehensive international experience in this area. The research of this experience and the possibility of its application in Karabakh will be quite useful for the study. The comparative analysis method is suitable for analyzing the suitability of the methods used for our country and region and the feasibility of their application. In this way, the investment climate in the relevant regions and the methods used can be compared with the situation and opportunities of the Karabakh Economic Region.

To study the economic potential and investment opportunities of the region, there is a need for a detailed study of the current situation from both positive and negative aspects. SWOT analysis is the most suitable method for the universal research of the above. This method is very useful for a comprehensive assessment of the situation, to identify the strengths and opportunities of the region, to see the points of interest to investors, as well as to identify nuances that could weaken the economic potential of the region and to create a reliable basis for suggestions to attract foreign investment in the region.

Research database: The study is based on scientific works of local and foreign scientists on the subject, reports and statistics issued by international and local organizations including World Bank, IMF, OECD, State Statistical Committee of Azerbaijan, Central Bank of Azerbaijan, information published in foreign media and other Internet sites.

Research limitations: First, there is little research in our country to attract foreign investment to the regions. Besides, the region was liberated only two years ago. For this reason, a detailed analysis of the current situation in the region is almost non-existent. This leads to a lack of a database for research.

Also, the lack of inhabited population and economy in the region makes field research (which is really beneficial for finding potential investment opportunities) impossible.

Scientific novelty of the research: Karabakh Economic Eegion was liberated two years ago, and there is almost no detailed study of the region's socio-economic, including investment potential. This study provides an overview of the current situation in the region and highlights the region's strengths and weaknesses, opportunities and threats.

In addition, the study provides a comparative analysis of other regions of the world with similar characteristics to the bog and the steps taken to attract investment there.

Scientific and practical significance of the results: As a scientific and practical result of the research, the areas of application of this research in attracting foreign investment to the liberated region will be studied and will be a stimulating force for its application in those areas. At the same time, from a scientific point of view, this type of research can be a way for more extensive research in this area. The results of the study and the proposals made can be used in public investment policy. In addition, the results can also be applied to another liberated region - East Zangazur.

CHAPTER I. UNIVERSAL BASIC INCOME: SURROUNDING ARGUMENTS

1.1. Theory of foreign investment

The value of the part of the output produced in the economy in any period in the form of new structures, new sustainable supplies, and inventory changes is called investment. The investment makes it necessary to curb current consumption to increase future consumption. For an expense to be considered an investment, it must be aimed at providing a new capital commodity or increasing production capacity. The change in capital reserves is net investment. Net investment can be both positive and negative. Positive net investment is called expansion investment. Part of the investment cost is also aimed at eliminating the wear and tear (depreciation) of existing capital reserves or the depreciation of technologically fashionable capital goods. Such investments are renewable investments, and these costs also lead to a net increase in production capacity. The sum of renewable investments and net investments is defined as total investments.

It should be noted that domestic and foreign capital investments can be of two types depending on the form of implementation. Thus, the portable price or material value in which the investment is made is either created for the first time or already exists. The construction of a factory by a domestic or foreign investor in one country or the purchase of a newly issued share document (share) is an example of the first group and the purchase of a previously built factory or acquisition of a movable property that is the subject of a sale in the capital market.

Acquisition, renewal, or expansion of a previously established factory by a foreign investor may be the purpose. However, the purchase of an existing factory, building, or facility, while an individual investment, is not considered an investment from a macroeconomic point of view. Because this operation, if it is not an investment for renewal and expansion, ie does not increase production capacity, it simply provides for the manual replacement of the existing facility. Similarly, the purchase of financial assets such as stocks, financing bonuses, treasury bonuses, and government bonds is not considered an investment in the economic sense; these investments are financial investments. Just as no added value is created here, the individual is simply changing the shape of the being in his hands (Branchard O. 1997). As such, the manual replacement of existing investments is called placement.

United Nations (UN) classified investments in the System of National Accounts (SNA) in 1953, 1968, and 1993. This has officially ensured that statistics around the world are comparable. The 1993 SNA divided economic assets into financial economic assets and non-financial economic assets. Financial economic assets consist of the following (Andrei L, Andrei D., 2021):

- Bonus;
- Bond;
- Stock;
- Gold, which performs the function of money;
- Cashier-bank;
- Advances;
- Debit accounts.

As you can see, among these are assets that are considered an investment from the firm's point of view. Financial expenditures are outside the scope of investment in terms of national accounts. Because such expenditures, as we have already emphasized, do not lead to an increase in the country's existing fixed capital reserves, but only show the cash flows on these reserves and the change of these cash flows.

Non-financial economic assets are also divided into produced and non-produced assets. Non-produced assets include land, naturally grown forests, and mines. Locally, such assets are beyond the concept of investment.

SNA's definition of produced non-financial economic assets corresponds to the definition of total investment. In this context, total investments are grouped under three main headings:

- Fixed capital investments;
- Stock (inventory);
- Valuables.

Fixed capital investment is the use of factors of production in an economy to increase real capital. According to SNA (1993), a commodity must meet the following four conditions in order to be considered a fixed capital asset:

- The commodity should be owned by production units (firms), not consumers (households);
- The commodity must be actively used in the production process. A commodity in reserve is not valued as fixed capital;
- The commodity must be used for a period of more than one year;
- The commodity must be used permanently or repeatedly;
- The commodity itself must also be produced. The cost of acquiring non-produced assets such as land is not an investment.

Goods that do not meet any of these conditions cannot be considered investment goods. In addition, the European System of Integrated Economic Accounts (ESA) has set a minimum value condition for investment goods. Even if all of the above conditions are met, goods that require a certain amount of cost are not considered an investment. The SNA identified fixed capital investments under three main headings:

- Tangible fixed assets;
- Intangible fixed assets;
- Significant improvement on the existing asset;

The second important asset is inventories. Inventories, as semi-finished and manufactured goods, are part of total investment, with the feature that they cover the various goods available in the hands of economic units.

Valuables, on the other hand, are precious metals and stones, jewels, works of art, antiques, etc., purchased to protect the value of money in the face of price increases over time. Valuables cover the costs of goods produced and acquired for the purpose of preventing losses of liquidity over time, not primarily for use in production or consumption.

In general, investments can be classified as follows:

- Study-project investments;
- New investments;
- Continuation and renewal investments;
- Expansion investments;
- Extreme investments to overcome difficult situations;
- Modernization and improvement investments;
- Research and development (R&D) investments

According to the Investment Law of the Republic of Azerbaijan investment consists of financial resources invested in the objects of entrepreneurship and other activities for the purpose of gaining income (profit) or social benefits, as well as material and intellectual resources. Such funds and assets include cash, targeted bank deposits, loans, shares, stocks, and other securities; property (buildings, installations, equipment, and other material assets); duly formalized scientific-experimental and other intellectual resources; a set of technical, technological, commercial and other knowledge necessary for the organization of this or that type of production, but not patented, compiled as technical documentation, habits and production experience (know-how); rights to use land, water, and other resources, buildings, structures, equipment, as well as copyright and other property rights; other riches.

Foreign capital is defined as a financial or technological resource that a country can add to its economic power in the short term from other countries in return for various forms of repayment in the future (Bhattacharya A. 2022).

In the European Union (EU), According to EU Directive 1988/361 / ees of for the free movement of capital adopted in 1988 and effective July 1, 1990, capital movements consist of thirteen followings:

- Direct investment;
- Real estate investments;
- Transfers related to documents normally auctioned in the capital market;
- Transfers related to documents of participation in collective investment companies;
- Transfers related to documents put up for auction in the money market;
- Operations regarding current accounts and deposits in financial institutions;
- Loans related to commercial operations or provision of services in which a person that is a member of a community is a party;
- Commercial debts and loans;
- Letters of guarantee, other guarantees, and pledges;
- Transfers related to the implementation of insurance agreements;
- Private capital movements;
- Physical import and export of financial resources;
- Other capital movements. These are also divided into sub-sections.

According to Organization for Economic Cooperation and Development (OECD), foreign capital includes:

- The share of the foreign investor in the company's profits, which is not distributed, but converted into reinvestment;
- Receipt of shares and debt documents (short, medium, and long-term debt documents) from the parent company by a foreign investor in cash or in-kind;
- Loans provided to the company by a foreign investor;

- Receipts of non-cash production fees from the company by a foreign investor;
- Commercial and other loans provided by a foreign investor.

As can be seen from the above classifications, wealth acquired in foreign countries can have either a financial or real (physical) quality. International (foreign) portfolio (indirect) investment in the purchase of a financial instrument (prices such as foreign borrowings and equity documents) from another country's money and capital markets in order to obtain interest, dividends, and capital gains for a period of more than one year (international portfolio investments). If the party carrying out this operation is a foreign state, an international official body, or organization, it is also called medium and long-term official foreign capital movements. Purchase of a financial instrument (such as foreign borrowings and equity documents) from another country's money and capital markets in order to obtain interest, dividends and capital gains for a period of more than one year is called international portfolio investments. For example, long-term loans from the International Monetary Fund (IMF) and the World Bank (International Bank of Reconstruction and Development (IBRD)) or interstate debt relations (the purchase of a country's official bond by another country or a direct loan) is of this kind.

Private and official financial flows, such as trade bonuses, financing bonuses, treasury bonuses, certificates of deposit, term bank deposits, export loans, pre-financing loans, correspondent openings, etc., with a term of less than one year, are short-term capital movements. Material values acquired or created in foreign countries, such as buildings, territories, factories, production facilities, machinery and equipment, are referred to as direct foreign capital investment (FDI). There are many definitions of FDI in the economic literature. According to one of them, foreign direct investments (FDI) are financial flows caused by global production.

According to one of the most common definitions, FDI is an investment made in a foreign country with a sufficient shareholding to have a say in the long-term management of the company. The IMF defines foreign direct investment as "an international investor owning more than 10% of the capital of any local company".

In other words, FDI is an investment by firms established in one country by purchasing a firm in another country or by providing construction capital for a newly established firm or by increasing the capital of an existing firm and which brings technology, management knowledge and gives authority of control for the investor. According to another definition, the acquisition of wealth (establishment of a manufacturing enterprise or acquisition of existing production facilities) by individuals or legal entities (state-owned enterprises, private firms) located outside the country's borders is called international investment or FDI.

This study will adopt a definition published under the title "The Benchmark Definition of Foreign Direct Investment" by IMF and OECD. According to this definition, which is valid in the international arena, the foreign direct investment reflects the goal of an institution (investor) located in one country to obtain long-term lasting economic benefits in another country. The concept of lasting profit refers to a long-term relationship with a foreign capital investor in terms of investment and investment control. Foreign capital investment is a public or private sector institution or entity that invests in a country other than the country in which it is located by setting up a branch, affiliated company or partnership.

In terms of our topic, the FDI is more important. There are two main reasons for this. First, as a quantitative measure, the FDI has a large share in other types of foreign investment. In fact, portfolio investments and short-term capital movements can also increase in large amounts, but this situation is temporary. International portfolio investments can make large inflows and outflows. However, the FDI is looking for growth in a more stable line.

The second and, more importantly, the FDI is a desirable form of capital movement because it stays in the host country for a long time, increases investment reserves, and creates new jobs. Highly liquid international portfolio investments and short-term private capital movements based on relatively short-term dividends and interest income are leaving the country en masse in the face of the slightest expectation of economic and political change in the country (White R, 2020). The crises created by private capital movements in Mexico in 1994, Asia in 1997, Russia in 1998, and Turkey in November 2000 and February 2001 led to a decline in demand and a decline in production and foreign trade in real economies. However, during the Asian crisis, foreign trade banks withdrew billions of dollars in loans from the region in a few days, while direct investment maintained its level, and in some cases even exceeded optimistic expectations. For this reason, in the past, some countries, especially those with speculative and short-term restrictions on capital movements, have been extremely liberal in their approach to the FDI and have enacted liberal laws on the subject.

The experience of some countries has shown that even without full liberalization, the economy can attract foreign direct investment. China is a good example. China, which has attracted a large amount of long-term foreign investment, has been careful to prevent full liberalization of the financial market and has made some adjustments in this regard (D'Andrea C.D., M. Zhi, J. Chen, 2021).

Given the high savings rates in East Asia, it is clear that the region did not need much additional funding before the crisis. This left those countries with the difficult task of effectively transforming the flow of savings into productive investments. Consequently, domestic savings tend to increase when countries implement the necessary regulations to improve the investment climate, even without full liberalization. The establishment of this confidence environment also encourages long-term and lasting foreign investment (even if the country does not need an urgent foreign fund).

International capital currents, in spite of all opposing views, are not the sole cause and culprit of any crisis. For example, the real cause of the crisis in South Asia was the over-indebtedness of the private sector in the region (South Korea), government openings and short-term high-interest rate borrowing to finance these openings, and artificially fixed exchange rates to make this borrowing attractive. Foreign capital movements simply acted as a catalyst and hastened the timing of the impending crisis. According to some economists, the crisis would have been deeper and more severe if it had not been for short-term international capital movements. Proponents of this viewpoint out that the negative effects of the financial crisis are limited to the regional level and have not spread worldwide. At the same time, they note that the negative effects of short-term private loans from private sources, which are not in the form of portfolio investments, are greater in the crisis. In short, sudden short-term capital movements were a logical consequence of wrong macroeconomic policies (short-term private-source loans with unsustainable budget discipline and insufficient infrastructure, shallow capital exchanges, uncontrolled and unlimited portfolio investments, etc.).

In developing countries, financial markets are often very shallow and very conducive to development. In addition, the fact that the portfolio size of individual investors is much lower than that of legal investors shows that a developed consciousness in the assessment of individual funds has not yet been formed. In this case, a very uneven (asymmetric) distribution of information can have an effect. In these countries, the financial market, which is designed to cover a wider range of capital, is not fully widespread, not only in material terms but also in economic terms (the most basic theoretical and practical information about the market is not known to the general public). As we can see in Table 1, the most FDI receiving countries are highly developed countries.

This table includes a list of countries of the world sorted by received foreign direct investment (FDI) stock, the level of accumulated FDI in a country. The US dollar estimates presented here are calculated at market or government official exchange rates.

The list estimates for recent year's statistics, according to the OECD.

Table 1: List of countries by received FDI (top 10 and Azerbaijan)

Rank	Country	Stock of FDI at home (millions of USD)
—	EU	6,938,000
1	The Netherlands	4,888,000
2	United States	4,084,000
3	United Kingdom	2,027,000
—	Hong Kong (China)	1,901,000
4	China	1,514,000
5	Ireland	1,477,000
6	Germany	1,455,000
7	Singapore	1,285,000
8	Switzerland	1,230,000
9	Belgium	1,093,000
10	Canada	1,045,000
49	Azerbaijan	80,630

Source: OECD International Direct Investment Statistics (2021) (https://doi.org/10.1787/e6696186-en.)

Despite the fact that investment funds and partnerships in both developed and developing countries have a significant share in the financial markets, in developed economies the financial markets are deeper and larger, and the institutional investment structures are more numerous, So it is unlikely that several investment structures or individuals will be able to influence the entire market. Again, because financial markets appeal to large masses and, consequently, capital is spread over a wide base, decisions are dominated by groups (institutional investors) made up of small investors rather than a few large investors.

The implication of the above is the need to further promote FDI in countries with less developed financial markets, which are less speculative due to their potential for long-term, physical and human investment. Consequently, privatization, liberalization and macro stabilization need to create conditions that will attract investment.

Improving investment conditions are encouraging foreign direct investment inflows into developing countries, where local financial institutions are weak. For example, foreign investment has played a major role in highly successful economic development models such as Singapore, Malaysia and China.

In a globalizing world, global and multinational companies value the controversial advantages that countries have. In assessing these advantages, the quality of the FDI plays a crucial role. For example, if a company operates in the field of information and communication technologies, then the resource to looking for in the destination country will be an educated and high-quality workforce. But for global companies that will invest in other sectors, especially in the mining and agricultural sectors, cheap labor and an abundance of natural resources in the country are becoming more important.

1.2. Foreign investment's economic effects

It is very difficult to measure the impact of foreign capital investment on the economic performance of the host country. Because foreign capital investments often have direct effects such as bringing high technology to the host country, creating new jobs, as well as indirect effects such as increasing the level of total productivity in the country (through a new form of organization, technical knowledge, etc.). many of which cannot be fully measured. In general, the net contribution of the IMF to the national income of the host country can be disclosed using the following model (F. Bruckner, A.Chong, 2020):

F – Payments for labor, capital and land - factors of production

(salary, interest, rent);

R - Profit of the organization;

T - Tax paid on income;

R* - Net profit after tax;

R - T = R*

N - The opportunity cost of local production factors

L - External economic value;

E - Payments for foreign factors of production (foreign investment cost).

If we formulate the above variables, the net profit/loss ratio of foreign capital investment is as follows:

$$\frac{(F + R^* + T) - N + L}{E}$$

A ratio greater than 1 indicates that the benefits of foreign capital to the country's economy outweigh the costs. The opportunity cost (N) of the local factors of production in the formula indicates the value of the output they will create if these factors are not used by the foreign capital structure. Thus, if labor and other local resources valued by foreign capital would otherwise remain empty and dead, the opportunity cost is zero. Conversely, if there were no firms with foreign capital, if the factors of local production were to be used with the same productivity by local structures, the opportunity cost would be equal to the value paid by the firm with foreign capital for those resources.

Therefore, in order to create added value in the invested country, the TNC must produce more value than the opportunity cost of the production factors it uses. From this point of view, in order to determine the profit more effectively, it is necessary to deduct the opportunity cost from the production cost of the firm with foreign capital. Although opportunity costing is difficult to measure, it is highly likely that opportunity costing will be low (even zero) in a developing country, where unemployment is high and quality labor is scarce, and labor and domestic savings are valued in unproductive areas.

The external economic value (L), which shows the indirect effect of foreign capital on the country's economy in the formula, is formed from the sum of positive external economies (Le) and negative external economies (Ld). The technology, strong organization, management and technical knowledge brought by foreign capital as a result of the positive external economic effect, the increase in the total quality of employees (knowledge, skills and abilities) lead to the development of many sectors, especially the manufacturing and service sectors. This leads to a decrease in costs, and an increase in domestic production and consumption capacity. There are strong research findings, especially in ICT investments, that the social benefits outweigh the firm's private (commercial) benefits.

The negative external economic effect, on the other hand, leads to the opposite development. With the entry of foreign capital into the market, local structures may lose the chance to compete, the imported capital and information-intensive advanced technology may lead to labor force problems, and so on. As a result, the net external economic value can be formulated as L = Le – Le.

Theoretically, the net production growth that foreign capital will create under a free market economy and full competition is greater than the value returned to the foreign investor due to the law of diminishing returns. Because the increase in the inflow of foreign capital into a country reduces the marginal productivity of capital in all investments, which results in a decrease in the profitability of all foreign capital investments. Even if this assumption is not taken into account, the state can prevent the transfer of more foreign capital to the country's economy by its tax legislation.

It should be noted that there are factors that are not included in the formula but affect the net profit/loss ratio of foreign direct investment. For example, various incentives such as money and taxes applied in the country reduce the benefits of foreign investment to the country.

Both theoretical and empirical research has shown that foreign direct investment often has a net positive effect on the host country. For example, according to Brash's study of US firms in Australia, foreign direct investment has boosted the country's GDP.

A study that researched the effects of foreign direct capital investment on economic performance in Turkey, covering 1973, 1975 and 1976, found that the return/cost ratio of foreign capital was more than 1%, and therefore the net effect on the country's economy was positive. Thus, in 1973 this ratio was 1.2, in 1975 it was 0.84 and in 1976 it was 1.22. This ratio was calculated as 5.4 in 1966 for US foreign direct investment in Latin America (United Nations, 2021).

Positive economic effects foreign direct investment

In the country where the foreign capital goes (host country - host country), it generally has the following effects:

- Ensures economic development by increasing the national income level of the country. Profit transfers in foreign direct investment, while changing on a sectoral basis, have fallen to very low levels today. Profits remain in the country and are converted into fixed capital investments, technological innovation and re-investment for R&D needs, thus contributing to economic growth. In addition, foreign capital is the most effective tool in restructuring and privatization, as well as supporting the establishment and development of by-products.

- Helps reduce unemployment by increasing employment. Foreign direct investment has a direct and indirect effect on the level of employment in the host country (J.Paul, M.Feliciano-Cestero, 2021). The level of employment created by foreign capital investment in developing countries generally ranges from 1% to 6% of total employment in these countries. The contribution of global companies to employment remains very limited in backward sectors such as mining and agriculture. However, the employment capacity of the services and manufacturing sectors has reached significant levels.

- Brings advanced know-how and technologies and management techniques, ensures the transfer of new technologies and imposes important functions on the economic development of countries that have difficulty in producing technology. However, empirical observations have shown that global companies tend to develop relatively strong technological capabilities in the field of process engineering with production planning and organization rather than new product design of subsidiaries.

That is, if special conditions (quality and skilled workforce, effective incentive system, appropriate legal framework, etc.) are not provided, global companies are concentrating R&D units (research departments and employees) in the country where the parent company is located.

- Helps to balance the country's balance of payments by creating long-term effects that replace imports and increase exports, facilitate access to international and global markets. In addition, while developing countries can produce with high quality and low cost, they may have difficulty accessing world markets. Global companies are transporting local resources to global markets through well-known brands in the international arena. In addition, global companies have close trade relations with their subsidiaries with vertical organizational ties.

- Gives vitality and dynamism to the country's economy, increases domestic competition, and provides foreign convertible currency savings by producing for the domestic market. Competition is one of the most important means of ensuring productivity and technological transfer in production. In addition, foreign capital firms are striving to adopt a system of free competition based on international private property as a fundamental order in the host country, which will have a positive impact on the development of democratic practices and traditions in the country.

- Often makes a positive contribution to the protection of the environment to the countries invested in. In terms of environmental effects, the standards of the invested country and the technological composition of the ICRC are important. For example, BP, which operates in the oil industry in the United Kingdom, which has a high level of environmental regulation, is more sensitive to the environment than it is in developing countries, where environmental regulations are weak. Empirical observations have shown that high-tech foreign investment is more sensitive to the environment, that it has voluntarily set up waste treatment facilities, that it attaches importance to recycling, and that it uses environmentally friendly green technologies.

- Increases financial resources and investments, has a positive impact on stability by diversifying the sources of funds. This reduces the country's need for foreign debt.

- Brings tax revenue to the country. Foreign capital structures are a source of tax revenue for local governments on the scale of their profits. This has a positive effect on the country's potential budget deficits.

- Foreign direct investment has a positive impact on ensuring the foreign economic integration of the host country, protecting it to be a closed society. The function of global integration, which was performed by the trade of goods and services in the 1950s and 1960s, is now being performed by foreign direct investment. In addition, host countries expect foreign direct investment to provide political and economic support to developed and capital-exporting countries.

- Foreign direct investment is forcing political governments to manage the economy more competently and carefully. Because in this case, the state is feeling the pressure of large countries and international organizations (such as IMF, IBRD) and institutions (agreements that protect foreign investment, such as ICSID, MIGA, CIME) behind foreign investment firms that suffer from the wrong economic policies..

Negative economic effects foreign direct investment

Comparatively, In addition to the benefits mentioned above, IFRS may also have some negative effects on the host country:

- When global companies come to the country, they often create an unfair competitive climate, eliminate local competitors and break the will of small businessmen who want to develop local industry. Given the global networking and innovation capacity of global companies, it is true that they have an advantage in a local competition (A. Niyungeko, 2020). However, given the high share of small and medium-sized enterprises (SMEs) in total production, employment, and exports in developed countries, this view is weakening. It should be noted that despite the capital advantage of global companies, small and medium-sized enterprises have the advantage of behavior (flexible production, quick decision-making, easy adaptation, innovation, etc.).

- One of the biggest criticisms of the FDI is that global companies have a decisive say in the country's economy. In particular, the fact that key sectors of the country's economy are under the control of foreigners is a cause for great concern. This raises the issue of the political and economic national hegemony of the country. In some cases, especially in developing countries, global companies are able to persuade governments to grant them special privileges, such as customs tax protection. In this case, the FDI is coming to the country only at the expense of damaging the democratic system. This is especially true for investments in mining, oil, diamonds, gold and natural resources, where foreigners have a real motive to buy labor at low prices.

- By consolidating R&D activities in the parent company's country, global companies can make the country where they carry out the production process technologically dependent. This hinders the development of local resources, abilities, skills, and initiatives.

- Direct investments made by global companies, especially in the mining sector, cause the country's natural resources to go to the country where the parent company is located without development, and the country is deprived of a serious economic added value.

- Global companies can increase profits by going for transfer pricing. However, this situation increases the foreign exchange outflows of the host country. Global companies are turning to transfer valuation practices for the following reasons (R.L. Parr, 2018):

- - Fundraising in one place. This method is used as a fund positioning effect by transferring cash funds from one place to another between the departments of a global company. For example, if a parent wants to transfer central funds from a dependent entity in a foreign country to a home country, it applies higher prices to the goods it sells to its branch in that country and lower prices to the goods it buys from it. Thus, the funds are collected in the main center.

- - Income Tax Effect. With a global company transfer channel, profits from a branch with a high-income tax can be transferred to a branch in another country where these taxes are lower.

- - Customs Tariffs and Quotas. This practice can also be used to avoid the negative effects of customs tariffs and quotas imposed by the host country. Thus, in cases where tariffs are based on value (ad valorem) or customs quotas are set on value, the amount of tax to be paid can be reduced by lowering the prices of parts imported from other departments and the parent center.

- - Taking advantage of expected exchange rate fluctuations for speculative purposes. This method can be used as a means of protecting or benefiting from the negative effects of expected changes in exchange rates. This is especially useful in fixed exchange rate systems and foreign exchange control practices. For example, if the national currency of one country is expected to be devalued and the currency of another country is expected to be revalued, the funds will be withdrawn from the country where money is expected to depreciate and transferred to the country where value is expected to be revalued.

- Global companies can transfer their after-tax net profits to their home country just as they can transform them into new investments. In the second case, as a result of the transfer, the host country may face a shortage of foreign currency. This situation has a negative impact on the balance of payments. For example, in 1993 alone, global companies transferred $ 27 billion to the United States, $ 11 billion to the United Kingdom, and $ 4 billion to Germany by transferring part of their profits to a central country. To prevent this, the host country is resorting to practices that limit profit transfers and encourage new investment.

- Finally, when global companies choose domestic production instead of export, the host country will be deprived of potential foreign exchange earnings.

As we have seen above, foreign direct investment can bring significant economic benefits to the country's economy. In addition, it can bring negative effects. In this regard methods of attracting foreign investment and coordinating it in the country in an efficient way if very important for the wealth of the economy.

CHAPTER II. EXPERIENCED METHODS OF ATTRACTING FOREIGN INVESTMENT

2.1. Factors that affect investment environment

The state of the business and investment climate in any country is a key factor in determining a country's ability to attract foreign investment and develop small and medium enterprises. Transnational enterprises prefer to invest in countries with a healthy business environment, ie where costs, delays and risks are minimal. In addition, the chances of small and medium enterprises developing are higher in an environment that is not burdened with various taxes and regulations. In one of its reports The World Bank states an effective investment climate as necessary pillar of each country's strategy to boost its economic development. In turn, this strategy creates opportunities for more productive labor and higher incomes for the poor (Saurav, Abhishek; Kusek, Peter; Albertson, Mark (World Bank), 2021).

Investors, financial institutions, as well as companies are trying to choose a place and area to invest that will bring them the greatest possible benefit , taking into account many factors. There are a number of things to consider when making a decision in this process. These factors are studied and classified by a lot of state agencies for the purpose of attracting foreign investment. For example, we can check classification disclosed on International Foreign Direct Investment Strategy for 2021-2023 of Turkey (Investment Office of Turkey, 2021):

Political and Institutional Conditions: Political system; Balance between socio-economic groups; Government attitude to foreign capital; Public administration; Legal infrastructure; Justice system and conflict resolution.

Macroeconomic conditions: Long-term strategy – Stabilization, local market, export, promotion of foreign investment; Economic freedom – Public-private sector, privatization programs, tariffs and barriers, currency mode, taxation; Performance – GDP growth, inflation, public openness, domestic and foreign debts.

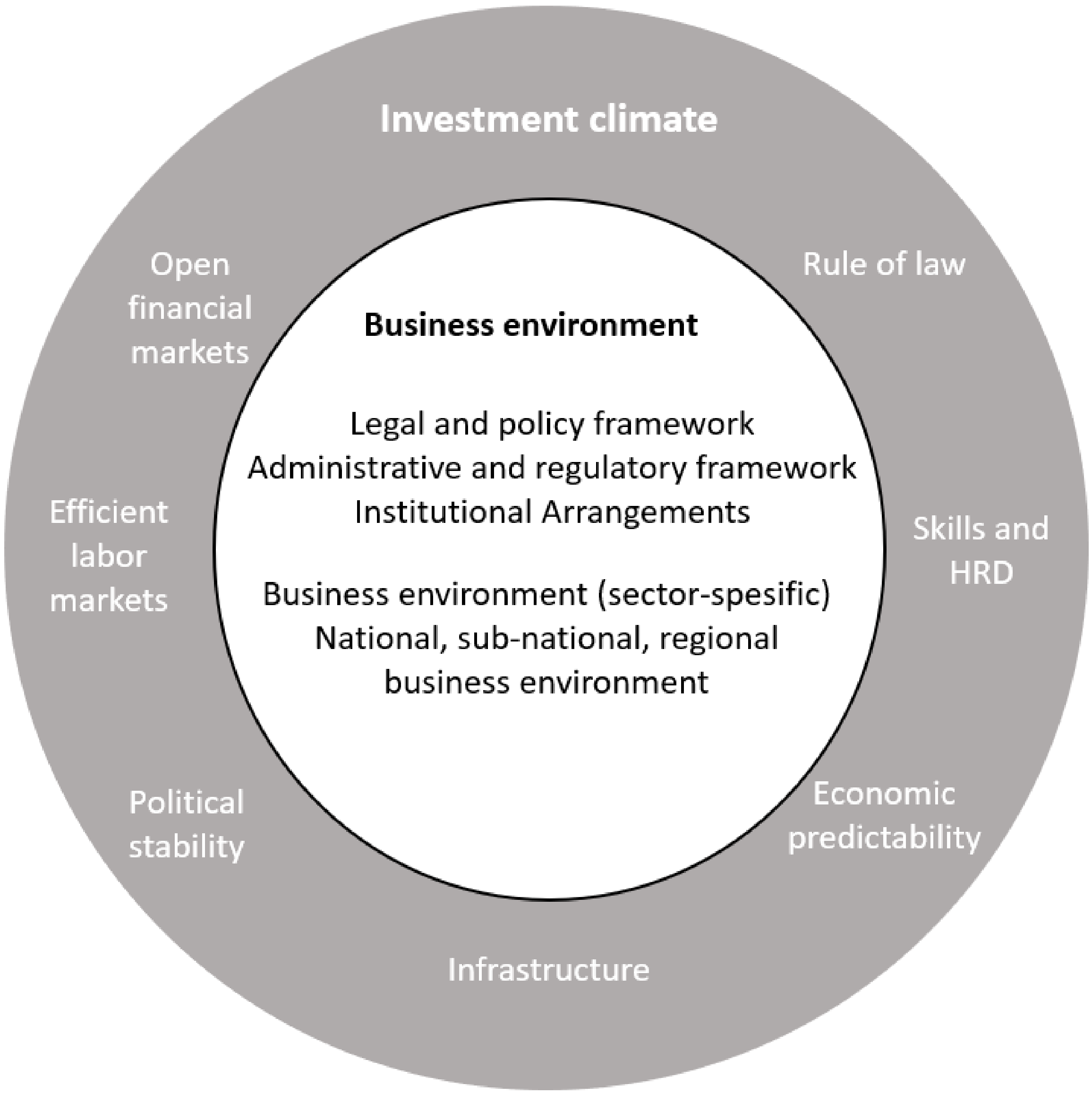
Industrial Conditions: Industrial structure – Sectoral distribution, firm size, R&D and technology, working conditions, forward-back links, non-formal sector; Communication – Telecommunications, transport network; Competition – competition mode, access barriers.

Investment Place Advantages: Market size – Internal, regional, international; Labor market – Salaries, workforce quality, industrial relations and labor legislation; Place of investment – Area prices and office rents, industrial areas; investment incentives, post-investment services; Energy – Cost, compatibility; Transportation – Cost, intensity; Financial – interest rates and credit opportunities, banking system, financial markets; Taxation – Tax system, investment incentives, effective tax rate.

When we talk about the investment environment, we can think of the climate created by these factors in a complex way. It includes a wide range of components from different spheres (not only economy, but also social, political etc.). In this regard, it is important to classify and evaluate all these components in a comprehensive manner in order to make a reliable decision.

We can divide investment environment into two levels: investment climate and business environment. World Bank gives definition of the business environment as "a complex of legal, policy, regulatory and institutional conditions which govern business activities" (Donor Committee for Enterprise Development, 2021). As Picture 1 shows, business environment can be considered as a sub-category of the broader investment climate with a smaller focus on regulation, administration, and legislation that is in relationship to establishing and managing a business than the larger country(region)-specific and exogenic factors shaping investment climate.

Picture 1: Investment climate and business environment

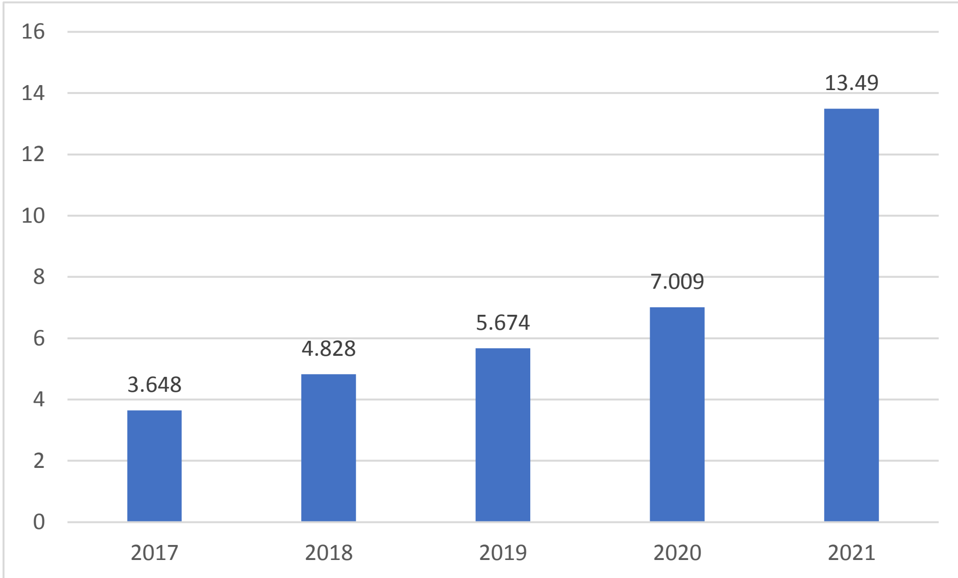


Source: based on The Report of Donor Committee for Enterprise Development (2021)

The investment climate may be affected by variety of indirect conditions like level of poverty, workforce participation, crime rate, national security, infrastructure, stability and liquidity of financial markets, political stability, tax rates, rule of law, democracy, property rights, legal environment, transparency of government etc (Hartwell C., B.Michael, 2015). So the main focus of an investor would be the business environment in the country, but on the background of that all the components of investment climate has to be considered adequately. Each of these components includes a lot of points that determine future return on investment, business sustainability and security. In order to attract foreign investment in country/region every part of the investment climate must be tailored to be proper for economic development. In this paragraph in order to understand relation between those factors and flow of foreign investment statistical correlations are used and assessed.

One of the main factors that foreign investors analyze in the country is conditions of financial markets and whole monetary system. It doesn't mean that financial markets have to be highly developed but should be as open and free as possible without decisive intervention of government. Especially in the countries where government directs the decisions of central bank, e.g. interest rates, this makes financial system vulnerable and unreliable. In such countries, foreign investors lose confidence in the country's financial system and are reluctant to invest here. This is exacerbated by government interference in central bank policy in particular. As a result, large investors are withdrawing foreign capital from the country. At first glance, this may seem like a limited loss of capital, but in fact it is the disappearance of components of the economic network in the country, and the consequences can be quite serious, such as devaluation of national currency, economic recession, market shrinkage, bankruptcy of small and medium businesses etc. These situations can lead to a chain reaction, cause the withdrawal of the remaining investments in the country and ultimately catastrophic consequences. In recent years, in Turkey suspicions about government's intervention in central bank decreased FDI flow to country and made foreign investors withdraw their capital from country. Because of that, as we can on the Figure 1 below, the national currency lost its value rapidly, worsened the real purchasing power and forced economy to be under pressure.

Figure 1: Average Turkish lira equivalent of 1 US Dollar (2017-2021)



Source: Exchange rates, OECD (2000-2021)
(https://data.oecd.org/conversion/exchange-rates.htm)

In this context, ensuring transparency in the market is also an important component. Transparency allows shareholders to identify abuses and access information that may be important to protect their interests. Transparent systems provide access to a wide range of information, clear decision-making procedures, public participation and open channels of communication between shareholders and officials.

> *For local and foreign investors, the development of rules and regulations related to investment, as well as the provision of transparent information on how they can be changed, is a necessary decisive factor in making investment decisions. Transparency and foresight are important, especially for foreign investors who need to operate in conditions that are very different from their regulatory systems, cultures and administrative frameworks. A transparent and predictable regulatory system for investments helps businesses more accurately and timely assess potential investment opportunities and thus accelerate the return on investment.* (OECD, Policy Framework for Investment, 2015 Edition (https://doi.org/10.1787/9789264208667-en.))

Factors of production

Naturally, investment needs factors of production in order to be realized. Thus, abundance and cheapness of them is quiet attractive for the foreign investors. Conventionally factors of production are classified as following:

- Land (including natural resources)
- Labor
- Capital
- Entrepreneurship

Natural resources are the components in the nature which can be used and processed in production or the conditions that make proper environment for production. They exist without any acts by mankind. These include

  - Minerals (Hydrocarbons, metals, rocks, ores and gems)
  - Climate (atmosphere, land, water, sunlight)
  - Vegetation
  - Animal life etc.

The more country has these resources, the more foreign investment will flow into it.

Labor is another vital factor. Foreign investors analyze in detail the state of the labor market in different countries, the volume and potential of the workforce, labor legislation, the availability of highly qualified personnel. Countries with high unemployment and poverty, but rich natural resources, attract investment in the extractive industries. On the other hand, foreign investors are investing in knowledge-based technologies in countries where there are enough highly educated personnel.

The availability of satisfactory infrastructure in the country is very important in terms of investment attractiveness. This includes the condition of the road transport network, the density of roads and railways, the level of sea and air transport, the availability of cargo terminals, electricity and water supply, the availability of basic goods and materials plants, access to services, etc. The availability of opportunities that are important for business and economic activity is very important for investors.

The remaining two factors (labor and entrepreneurship) are what a country would want to attract from other countries. In order to achieve that, besides natural resources and human capital, the country should present incentives like investment discounts, exemption from customs duties or late payment, cheap loans etc. Investors attentively analyze these components when they make investment decisions in order to minimize spending and maximize output. These incentives can be differentiated in order to make specific regions more attractive for foreign investment.

Besides above, special economic zones which are free from custom or other fees and presents a lot of discounts are very good initiatives to improve investment climate and attract FDI. These zones apply exclusive conditions that in favour of decision makers – investors. As we can see on Table 2 the countries with most SEZs in the world include those which have huge amounts of FDI.

Table 2: Top 10 countries with most SEZs and their net FDI inflow in 2019

	Number of SEZs	FDI (Billions USD)
China	2543	187.2
Philippines	528	8.6
India	373	50.6
Turkey	102	9.1
Thailand	74	4.8
Republic of Korea	47	9.6
United Arab Amirates	47	3.6
Malaysia	45	9.2
Bangladesh	39	1.9
Cambodia	31	3.7
World average FDI		1.5

Source: SEZs Report, UNCTAD (2019); Net FDI inflows, World Bank (2019)

The most important issue for a foreign direct investor is the economic and political stability of the country in which he will invest. For example, fear that can emerge about foreign capital investment is nationalization of a foreign initiative without compensation. Generally, if a country's political situation makes a project risky for a long time, such as a potential war, aggression, insurgency, insurrection, collapse of the state, fear of abandoning a foreign capital company with (expropriation) or without (confiscation) payment, foreign firms will be extremely reluctant to invest.

Besides political stability, it is important to consider general political climate and level of democracy in the country. Investing in a country in which authoritarian government has leadership would result in sudden, forced secession of the investment into ruling people or their relatives. Because of that, democratic factors like government transparency, voting rights, human rights and freedom of the country in which investment is planned to be made needs to be analyzed. Rule of law and freedom of the judiciary are very important. As lack of transparency of the courts causes a risk of being sued illegally or losing a case unfairly for a company, there is a lot of examples about non-democratic countries' failure on attracting FDI.

That does not only affect the decisions of investors, but also encourages other states to sanction the country which further worsen the investment climate. For example, The United States imposed sanctions on nine Belarusian companies in 2006 and 2021 for human rights abuses and weak democracy (US Bureau of Economic and Business Affairs).

Social and psychological factors have a significant impact on foreign capital investment. These factors can lead to pessimistic outcomes in the future, with some fears from the past.

The negative campaigns of ideological currents about foreign capital also concern foreign capital. These companies have reduced or abandoned some of their projects for fear of public backlash in the countries in which they will invest. It can be said that anti-foreign capitalism in most developing countries increases the risk of new investments and hinders the integration of those who work in fear and anxiety with the country's economy. When we look at countries such as Ireland, Hungary, Greece and Belgium, which have well-benefited from foreign capital, it is clear that these countries do not have prejudices about foreign capital. The positive impact of psychologically relaxed foreign capital on the economies of these countries has been enormous.

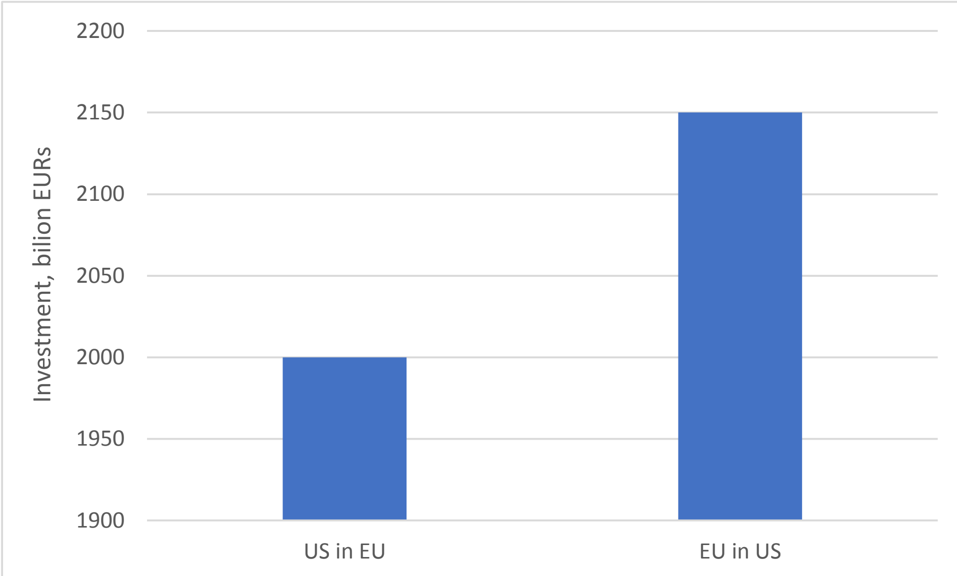
One of the most important social factors directly affecting foreign capital investment is labor market regulations and the effectiveness of trade unions (Niyungeko A., 2003).

The country's social structure, traditional characteristics, moral and ethical values should not have a negative impact on foreign capital investment.

Although economic theory states that moral values do not influence investment decisions and that economic rationality must be decisive, in practice it is known that foreign investors will prefer to work in conditions that do not make them feel like foreigners. It would be more expedient to carry out production and sales activities in a country where they know their people, are familiar with their culture, know their habits and predict their reactions.

In short, while trade considerations and profitability are the first and foremost preferences, we can assume that differences in social and moral values affect foreign investment decisions. Thus, investors tend to set up businesses in societies where they are aware of their social and cultural values and structure and feel more native. It's kind of their comfortable economic choice. Among other important factors, this is one of the reasons why Western European and American capital are increasingly investing in each other which can be seen on Figure 2 below. It has to be noted that in 2019 investment of EU in US was eight times the amount of investment of EU in China and India together.

Figure 2: Investment between European Union and United States, 2019



Source. European Comission Trade Report (2019)
(https://ec.europa.eu/trade/policy/countries-and-regions/countries/united-states/)

As mentioned above, the business environment is inside part of the the investment climate, also the most important module for the investors. It's mainly shaped by legal, policy, administrative, regulatory framework and market environment in the region or whole country.

Here we can examine process of establishing a business, legal procedure, registration, accounting, environmental, social and other requirements of a country. The less favorable those steps and requirements are, the more time-consuming and costly founding a business will be, thus averting FDI. That's the reason why states work on programs to ease doing business as complex of the factors above.

Important part of the business environment is market. The phrase of "market environment" refers to the variables and forces that influence a company's capacity to develop and sustain effective customer connections. "The entirety of physical and social elements which are taken into consideration in the behavior of the decision makers in the organization" is how the business environment is described (Duncan, 1972)

The environment is divided into three levels:

Internal environment – the parts of an organization that are utilized to produce, convey, and deliver market goods.

External microenvironment – Small external influences that impact a company's capacity to service its consumers.

External macro environment — variables related to the society that have an impact on the organization's ability to survive.

2.2. World experience on foreign investment attraction in similar regions

Karabakh economic region was liberated from occupation in the last quarter of 2020. Undoubtedly, there are wide market opportunities for new investments. However, the fact that the area has emerged from a long-term conflict also presents risks and dangers. Taking this into account, analyzing the work done to attract foreign investment in post-conflict areas with similar characteristics to Karabakh, it will be useful to learn a fairly useful experience.

Most post-conflict zones ironically provide ample opportunities for business as they weren't used, occupied and industrialized by any company for many years. On the other hand, there may be problems in terms of security and political stability in such areas. For this reason, it is necessary to take into account each point when making comparisons and come to a rational conclusion. When selecting cases for comparison, it is possible to obtain a detailed insight by preserving geographical and social diversity by selecting zones with variable cultural characteristics from different continents.

FDI can help to bring about peace, while violence is not conducive to recruiting FDI. As a result, official development aid (ODA) is likely to be a more conspicuous source of foreign financial and technical support in war and post-conflict settings than private investment, at least at initially. Its contributions are intended to aid in the achievement of specified recovery goals including as primary humanitarian relief, the restoration of public services, and infrastructure reconstruction.

Croatia would be a very good example as the country was included in socialist world in Eastern Europe and suffered deadly war against separatist subjects in 1990s, just like Azerbaijan. The conflict in the Southern Slavic states emerged in the early 1990s as these countries declared independence from Yugoslavia, spurred on by discontent with the Yugoslav government, ethnic concerns, and independence movements and democratic developments in Eastern and Central Europe. As a result, ethnic Serbs in the country's central and eastern areas founded the Serb Krajina, Autonomous Region, which was backed by the Serbian government and the Yugoslav army which is mostly Serb-dominated. The battles stopped in 1995 by United Nations-backed cease-fire and Croatia could regain control in occupied territories (Cigar, Norman, 1996).

Croatia joined a group of economies, particularly in Central and Eastern Europe, that were transitioning to a capitalist, market-based economic system after independence from the formerly communist Yugoslavia. Croatia's 1990 Constitution set forth the goals and broad principles that have guided economic development in the country since then. The Constitution's economic goals include promoting "social welfare and economic advancement" as well as caring "for the economic development of all its zones and sectors" (article 49). The new Constitution also repealed previous Yugoslav economic regulations and endorsed activities necessary to establish a new system, including the privatization of state-owned enterprises (SOEs). It recasts economic model of Croatia, declaring that " market and entrepreneurial freedom should be the foundation of the Republic of Croatia's economic system."

The Constitution grants international investors the identical legal rights as local investors (national law, article 48) as well as other protections ("foreign investors must be guaranteed repatriation and free transfer of earnings and cash invested," article 49). All the invested capital, including FDI, can be expropriated, but only for a (specified) public purpose, such as national security, the environment, or public health, and only after full recompense based on fair value of the investment (article 50).

In the 1990s and 2000s, the Croatian Constitution was accompanied by a succession of investment-related rules and international conventions aimed at increasing the country's investment attractiveness. In general, these policies aimed to create a favorable legal environment for investment by providing them with national treatment, anti-expropriation protections, and simplified dispute resolution and tax procedures. Early in the post-conflict period, the country also established IPAs (investment promotion agencies). Croatia's present IPA, on the other hand, was just re-established in 2002 that became fully active in 2005.

Croatia did not enact a distinct foreign investment law since the Constitution guarantees the rights of both domestic and international investors. The rights guaranteed by the Constitution, on the other hand, have been reaffirmed and/or expanded upon via particular legislative actions. The Company Law (1995), the Law on Privatization (1996), The Law on Free Zones (1996), The Law on Stock Company Takeovers (1997), The Investment Promotion Law (2000) are all noteworthy legislation.

Croatia engaged in extensive privatization of public assets and firms as part of their overall economic reforms. Croatia began privatization SOEs well before the conflict ended, typically selling them to international investors who might compete around an equal level with local investors. Croatia began a privatization initiative as part of its economic liberalization, which is still ongoing.

Foreign investors were eligible to partake in privatizations from the start, thanks to the Constitution's provision of national treatment. As per the World Bank's privatization database, a cement factory was the first to be sold to a foreign investor in 1992, following by the transfer of two chemical facilities the following year. The private sector's proportion of GDP rose substantially during the early years of Croatia's existence, rising from a 25% in 1991 to 55% in 1997. Major privatizations in the telecommunications and financial sectors happened in the late 1990s, while other vital infrastructure was generally avoided (UNCTAD, 2009).

Croatia has not made a concerted effort to entice international investors with its overall tax structure. The corporate income tax rate of 20% was much higher than that of its Eastern European neighbors, such as Northern Macedonia (15%), Hungary (10-16%), and Serbia (10-16%). (10 %). Only in 2005 was the dividend withholding tax repealed. Croatia, on the other hand, has signed 48 dual treaties in minimize foreign investors' possible tax liability (UNCTAD, 2008).

As the result of FDI-dedicated policy Croatia got just $76 million in average yearly FDI inflows throughout the war period (1991–1995). Following the conclusion of the conflict, FDI into Croatia skyrocketed, expanding by a factor of 10 on an annually. Inflows averaged $907 million per year from 1996 to 2000, and $1.5 billion from 2001 to 2005. From 1990 to 2007, Croatia's foreign investment stock (i.e. cumulative inflows) topped 40% of GDP, compared to 46% in Hungary, 35% in Bosnia and Herzegovina, 31% in Serbia and Montenegro, and 16% in Slovenia. Croatia sustained her greater level of foreign investment inflows in 2008, obtaining $4.4 billion in total (World Bank datas, 1990-2007).

Mozambique's civil conflict impacted the entire country. Until the mid-1980s, violent attacks against population were mostly concentrated in the country's south and center, particularly in the border regions of Tete and Manica. Fighting stretched from the border areas to the sea during the second, more vicious phase of the conflict, and grew more intense in the southern, while also expanding to the north.

The United Nations oversaw a successful demilitarisation and demobilization operation following the approval of the civil conflict peace treaty between Renamo and Frelimo in October 1992 in Rome (Manning, Carrie L., 2002). In 1994, democratic elections were held, resulting in the return of one million refugees and the start of a fragile process of national recovery and peace-building.

The Reconstruction And development Programme of 1987–1991, which included a number of fundamental adjustments backed by the International Monetary Fund (IMF) and the World Bank, and the initiation of a new Constitution in 1990 that was more liberal in political and economic terms than before, were two major improvements. Mozambique's Constitution, in addition to declaring the country's economic growth and scientific and technical progress objectives (article 6), recognized the significance of a free market in accomplishing them.

Article 41 citations "market forces" and "proposals of economic agents" among many other cornerstones of the new "economic order," though these are to also be substantiated by a predominant role for the state, including legislation for social and economic reasons, as well as the potential of full as well as joint state shareholdings. Article 45 addresses foreign investment explicitly, allowing "foreign initiatives... in all sectors of the economy, except those expressly allocated for Nationalisation or development by the State."

Mozambique had implemented the fundamentals of reforms in areas where FDI would otherwise be hindered. These improvements were not always of "international standard," and considerable impediments to regular corporate operations persisted. They did, however, convey a friendly attitude toward FDI and were significant steps toward facilitating its introduction.

The Investment Law (1993), which was established in concert with the Code of Fiscal Benefits (1993) and the Foreign Exchange Control (1996) Regulation Law were the first important pieces of post-conflict investment regulation. In contrast to Croatian legislation, the Investment Law addressed the rights and duties of foreign investors openly, expressly opening the market to Foreign Direct Investment in every field not designated for the state and giving all international investors special protection (UNCTAD, 2009).

Mozambique signed and approved a number of Bilateral Investment Treaties (BITs), the first of which was with Portugal in 1996 and entered into force in 1998. Republic of South Africa (1997), the The US (1998), Holland (2001), China (2001), France, Germany, and the Great Britain (2002) are among the major accords (2004). The Mozambique–United States Bilateral Investment Treaty, based on the United

States model BIT, includes the usual assurances of national and most preferred nation treatment, and also expropriation limits, transferability of investment-related resources, performance parameters, access to foreign managers, and the use of arbitral tribunal.

The privatization effort in Mozambique began in the late 1980s and accelerated after the signature of the peace agreement in 1992. (Pitcher, 1996). In 1987, the government applied for World Bank financing, which included a structural adjustment package that included the privatization of SOEs. This ecommendation was backed up by government studies in Mozambique, which revealed the terrible status of these businesses, employed in the agricultural sector. Reduce the government's budgetary burden, promote the private sector, increase economic efficiency, reduce administrative costs, establish financial system, and gain access to markets, resources, and technology were all goals of the privatization initiative. In comparison to commercialization efforts of other countries of Africa, the initiative is widely regarded as a success.

The privatized SOEs were divided into two groups based on their size. Small and Medium businesses were sold to local investors through the appropriate parental ministry. Large corporations were open to both foreign and local investors through an open tender procedure that relied on a global advertising effort to market the opportunity.

Tax incentives were implemented early in Mozambique, and they tended to be tailored by size of project and sector. Non-tax business costs are still substantial in, although efforts are being made to lower them.

On the surface, Mozambique's tax system appears to be uncompetitive, however it is mitigated by a number of exclusions and incentives. Even though the statutory corporate tax rate is greater than that of Mozambique's peers, it has decreased from 35% between 1999 and 2002 and 32% between 2003 and 2007. Mozambique was not as active in the field of double tax agreement as Croatia, thus exposing foreign companies to significant tax responsibilities (KPMG Global, corporate tax rates). However, agreements were signed with key FDI source nations such as Portugal in 1991, Mauritius in 1997, and South Africa in 2007.

Early on, Mozambique took advantage of both general and specialized tax benefits. These tax breaks have widened the gap between the normal and real tax rates that investors face. The Code of Fiscal Benefits (1993), which applies to qualifying investments under the Investment Law, was the first to set tax incentives of Mozambique. The Code of Fiscal Benefits offered tax exempt status, reduction, and deduction to international investors, allowing them to avoid most of the non - competitive and complicated general tax system on business (box III.2). These incentives are frequently related to government goals such as technical advancement, skill diffusion, economic growth, and infrastructure rebuilding. For example, the Code's working capital tax credit is now quadrupled, if not treble, for investments made there.

Mozambique's FDI attractiveness has also improved dramatically after the conflict ended. Mozambique received barely $9 million in FDI each year on average in the five years leading up to the 1992 peace pact. The prior five years' average yearly FDI inflows were $215 million a decade later. FDI increased consistently until 1997, when it exploded to a considerably greater pace. After 1997, there was a significant increase in FDI in two "megaprojects": the Mozal aluminum mill and the Tamane energy project. By 2007, these two projects had accounted for 60% of Mozambique's total FDI inflows. They frequently dominate discussions of Mozambique's FDI attractiveness performance, and it is commonly considered that they account for all of Mozambique's FDI attraction success (World Bank datas, 1990-2007 (https://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD)).

In Table 3 below, we can see the general results of actions taken by governments of Croatia and Mozambique in order to attract foreign investment.

Table 3: FDI inflows of Croatia and Mozambique

during post-conflict years ($ million, average of previous five years)

Years	**Croatia**	**Mozambique**
1990	-	5
1995	95	32
2000	907	179
2005	1520	258
2008	4383	587

Source: : UNCTAD, FDI/TNC database, UNCTAD GlobStat Database, World Bank (https://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD)

Conclusion of above experiences

Conflict-torn countries or regions are not the best places for international investors to launch ventures. Conflict exacerbates the risks of investing since it is often linked with insecure governments, damaged or destroyed infrastructure, and severe interruptions in economic operations, all of which result in lower output, GDP, and high rate of inflation, all of which discourage or hinder FDI. Foreign investors are frequently in a poorer position than local compaines to appraise developments in a post-war zone, thus uncertainty about the likelihood for enduring peace continues after the fighting ends. As a result, domestic investment and official help or loans often account for the majority of investment. Post-conflict nations can, however, take efforts to actively pursue FDI and gain from its possible benefits to investment, employment, government finances, stable macroeconomy, infrastructure, company development, and overall economic growth, all of which can contribute to long-term peace. To achieve these goals, a balance must be struck between providing a competitive legislative framework to compensate for the heightened risks that investors face in post-conflict nations, on the one side, and increasing FDI's beneficial influence on the country's economy, on the other.

Post-conflict economies are barely normal economies, owing to the lingering effects of violence, the possibility of security breakdowns, major market failures, and poor infrastructure. It is no easy feat to change them into dynamic, competitive, and self-managing systems. Development assistance alone will not be able to repair damaged economies, hence FDI can be a useful instrument for economic restoration. This study has proven that post-conflict economies may attract and use FDI to assist realize long-term economic development and stability, which can aid in the peace-building process, by looking at the successful models of Mozambique and Croatia.

It is not pure fantasy to hope for Foreign Direct Investment in the immediate aftermath of a war. FDI may respond fast under the appropriate circumstances, such as credible stability and a strong government dedication to economic transformation. Following a conflict, post-conflict countries should focus on building the required preconditions, such as economic stability and fundamental foreign investment regulations. In post-conflict contexts, FDI recruitment strategies such as investment supports and privatization might help to mitigate the risks faced by international investors.

International technical and financial aid plays an important role not only in the restructuring, but also in the restoration and creation of facilities, which is critical for attracting FDI. The presence of FDI at the outset might give good indications towards other foreign investors, resulting in an exponential increase in flows over time. More complicated kinds of FDI, like as infrastructure, and the accompanying legal framework, might be addressed after the post-conflict era.

Strategic policy is required to use FDI for economic growth. Foreign direct investment may have a significant and positive influence on conflict-affected nations by delivering well private cash, innovation, talents, and government income, as well as encouraging local sectors and exports. These advantages from foreign investment, however, are not inevitable. FDI is unlikely to build the required amount of development ties with the domestic economy if left to its own tools. Well-tailored guidelines, such as the implementation of megaprojects to maintain FDI in infrastructure, SMEs' linkage and capacity-building programs, competitive and open privatization to restructure SOEs, the promotion of capital-based FDI in depressed regions, and some other policies discussed in this report, could really achieve maximum FDI's potential contributions. Foreign organizations can help with the finance and design of these programs once again.

Coordinated efforts for attracting foreign direct investment, as well as safeguarding and amplifying prospective advantages, are part of a good policy agenda. Taking all of this into account, it is evident that there is no "one-size-fits-all" policy option for attracting and profiting from post-conflict investing. The creation of a post-conflict private capital system must be customized to the degree of development and unique features of each country.

2.3. Analysis of the current situation in the Karabakh Economic Region in terms of attracting foreign investment

The main step to be taken in order to identify ways to attract investment to a region or country is to conduct an in-depth analysis of the current situation in the region. In this way, it is possible to study the region's profitable economic opportunities, see the points that discourage investors, identify the necessary infrastructure, personnel and security, have the basic information for strategic planning and achieve other important issues.

This study uses SWOT analysis, one of the most successful and useful methods to study the current investment climate in the Karabakh economic region. Thus, the region's strengths, weaknesses, opportunities and threats are identified, and the necessary information is formed to make strategic investment decisions.

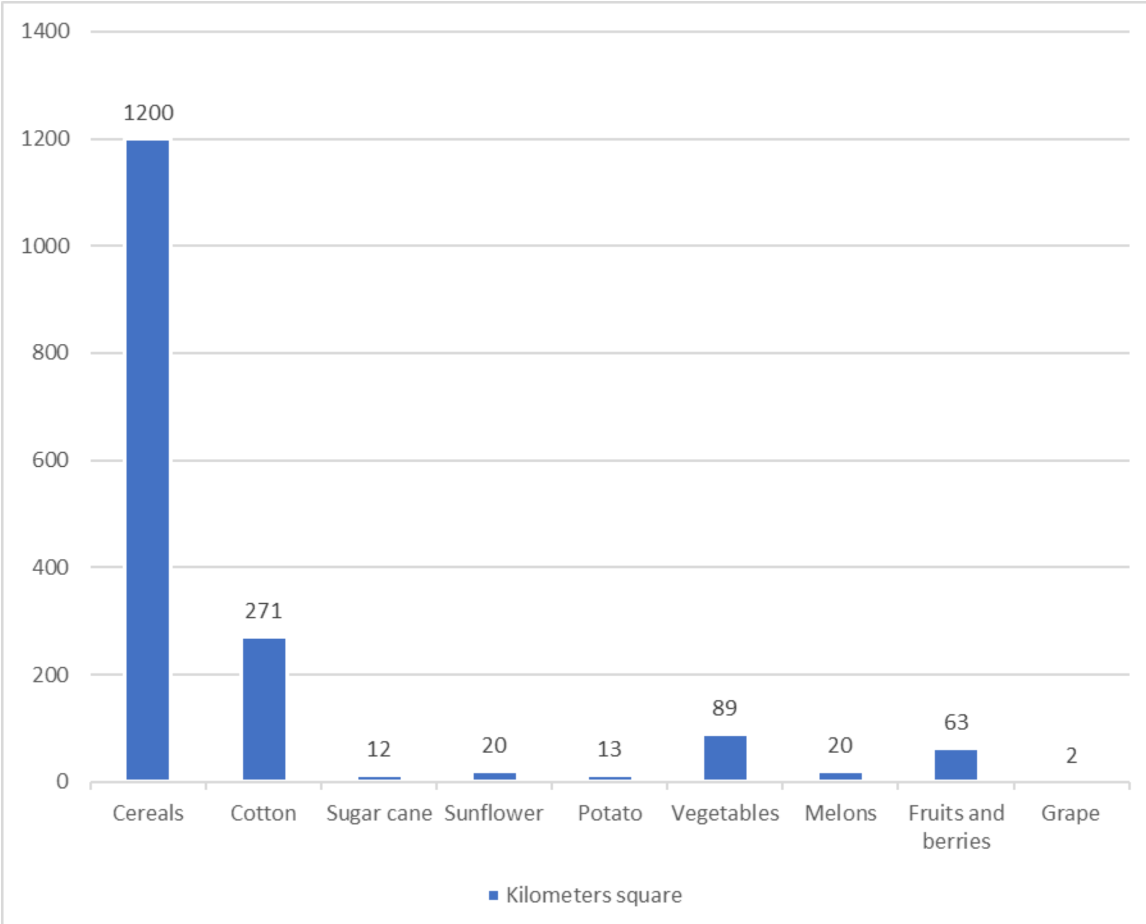
First of all, it is necessary to determine the geographical boundaries of the Karabakh Economic Region. Until 2021, there was the Upper Karabakh Economic

Region, which is approximately the same area as this region. According to the Decree of the President of the Republic of Azerbaijan on the new division of economic regions in the Republic of Azerbaijan, the Upper Karabakh region was abolished.

The newly created Karabakh Economic Region consists of Agjabadi, Barda, Tartar, Agdam, Fuzuli, Khojavend, Khojaly, Shusha districts and the city of Khankendi (https://president.az/az/articles/view/52389). It has area of 8990 km² (https://www.economy.gov.az/article/qarabag-iqtisadi-rayonu/31889#), stretch from Murovdag mountain range in the North to Araz river in south and covers both high mountains and wide plains.

At first, it would be expedient to emphasize the strengths of the region in terms of investment attractiveness. The natural resources of the area should be mentioned in this regard. The region is rich with significant natural resources which can boost economy when realized. The cultivated are in the region are 1690 square kilometers in total (https://www.stat.gov.az/source/regions/?lang=en). The diagram below shows the distribution of sown areas.

Figure 3: Cultivated area for plants in Karabakh Economic Region, 2020-2021

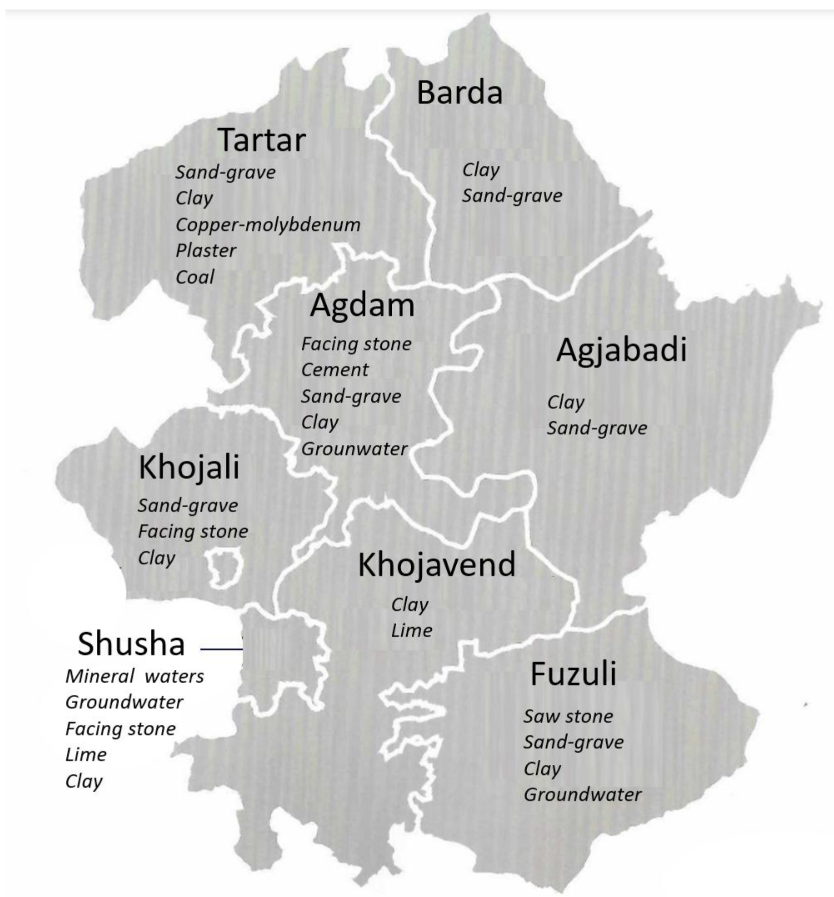


Source: State Statistical Committee (2021)
(https://www.stat.gov.az/source/regions/?lang=en)

As we have seen above, a large part of agriculture is covered by grain and cotton, which are currently in great demand on the world market and in the local market. In his speech on December 1, 2020, The President of Azerbaijan Ilham Aliyev noted that Armenia grew wheat on thousands of hectares of land in Agdam, Fuzuli (these two are inside Karabakh ER), Jebrayil, and Zengilan districts. Armenia harvested up to 90 thousand tons of wheat per year in the formerly occupied territories; little more wheat is produced in territory of Armenia itself, just 100 thousand tons per year (https://president.az/az/articles/view/48205). We can assume that half of these amount are produced in two noted districts of Karabakh Economic Region. Considering all of the above, investments in this area of agriculture can be economically successful, as well as have a positive impact on solving the food problem.

As for minerals, the region is especially rich in building materials. It is possible to see the relevant mineral resources on the map regions. This, in turn, will benefit in two ways. First, there are ample investment opportunities for companies engaged in the production and processing of construction materials. Second, due to the proximity of the materials needed for construction, the building of any industrial, agricultural and service enterprises, as well as residential buildings and public facilities is accelerating, and the region's economy is developing rapidly.

Picture 2: Mineral resources in Karabakh Economic Region



Source: Əlizadə E.K., Tarixazər S.Ə (2015), Azərbaycan respublikasının coğrafiyası. III cild "Regional coğrafiya"

From the point of view of human resources, it is possible to say that the region is a suitable place for investment. According to the relevant report of the State Committee, the population density registered in the region last year was 102 people per square kilometer, and the natural increase was positive - 4130 people. The number of labor force is 418,200 and the employed population is 392,000 (https://www.stat.gov.az/source/regions/?lang=en). Given that the majority of the registered population is IDPs and will need new jobs when they return to their lands, it is not difficult to predict that there will be a large labor market for entrepreneurs in the region.

As mentioned in the previous paragraph, transport and logistics infrastructure – airports, railways, roads etc. play an important role in attracting investors to the region. In this regard, it is necessary to emphasize the projects implemented in Karabakh after the liberation.

In October 2021, with the participation of the Presidents of the Republics of Azerbaijan and Turkey, an international airport was opened in Fuzuli. Currently, the airport regularly serves cargo and passenger aircraft. The runway is 3,000 meters long and 60 meters wide. Equipped with state-of-the-art infrastructure, the airport's terminal allows for at least 200 passengers per hour. All the work done here was carried out in accordance with international norms and standards. An Air Traffic Control Tower equipped with automated systems has been built here. This makes it possible to start flights at Fuzuli International Airport in accordance with ICAO and IATA standards (https://president.az/en/articles/view/53734).

Another sector to be talked about is the railway. Currently, two major projects in this area are being implemented in the Karabakh Economic Region. These are related to the restoration of the Barda-Agdam and Horadiz-Agband railways. Most of the work on both projects has already been completed. Freight trains have started running on the Horadiz-Agband railway passing through the Jabrayil region (https://corp.ady.az/infrastruktur/yeni-xetlerin-tikintisi).

Along with all this, the construction of roads should be noted as the most important part of daily transport. After the liberation, the road infrastructure in Karabakh was of poor quality. For this reason, the government is taking consistent measures to build new roads. At present, Victory Road (101 km), Ahmadbeyli-Fuzuli-Shusha (81.6 km), Ahmadbeyli-Horadiz-Minjivan-Agband (123.8 km), Talish-Tapgaragoyunlu-Gashalti (22 km), The construction of Khudaferin-Gubadli-Lachin (83 km), Shukurbayli-Jabrayil-Hadrut (43 km), Fuzuli-Hadrut (13 km), Barda-Agdam (45 km) highways is underway and most of the work has been completed. The roads are planned to be commissioned during 2022 ((http://www.aayda.gov.az/az/news/3180).

Thus, we can say that the transport infrastructure of Karabakh is being rapidly restored and developed, and in a short time it will be ready for large-scale economic activity. Of course, these projects are not only related to the territory of Karabakh. The geographical location of the region makes it an important point for international transport routes. The airport, railways and highways under construction will help the region to take its place in the transport chain and the economy to flourish.

Undoubtedly, one of the most important factors for the revival of economic and household activities in an area is energy. Relevant infrastructure projects are being implemented in Karabakh in this area as well. In 2021, immediately after the demining operations in the liberated areas, Azerenergy started operating in parallel in some places, built new digital substations with a capacity of 600 MV / A, laid more than 400 km of 110 kV transmission lines to Shusha. The city supplied electricity to Fuzuli, Jabrayil, Zangilan, Gubadli, Kalbajar and Aghdam regions. At the next stage, Sugovushan-1 and Sugovushan-2 HPPs with a total capacity of 7.8 MW, destroyed as a result of combat operations, were reconstructed and put into operation. In general, Sugovushan has an invaluable role in Karabakh's energy network. In 2022, 110/35/10 kilovolt “Ağcəbədi” electrical substation, “Ağdam-1”, “Ağdam-2” substations and “Qarabağ” digital control center were constructed (http://www.azerenerji.gov.az/news).

At the same time, there is a potential for solar energy in the Economic Region. According to the amount of solar radiation falling on the earth's surface, the Fuzuli district in the south of Karabakh is in second place after the territory of Nakhchivan AR. Here, one square meter of solar radiation falling on a horizontal surface is 1600-1700 kWh per year. The total solar energy potential of these areas is 3000-4000 megawatts (https://minenergy.gov.az/en/xeberler-arxivi/dagliq-qarabag-ve-etraf-regionlarin-enerji-potentiali).

The rich tourism potential of Karabakh is also one of the issues to be emphasized. Mountain and forest areas in Khojaly, Khojavend and Tartar regions attract special attention in terms of natural recreational resources. There is a great potential for the development of nature and ecological tourism. Relevant work has already begun in this direction. The foundation of a tourism complex to be established on March 20, 2022 in Sugovushan settlement of Tartar region on the basis of the Tourism Development Concept has been laid ((https://azertag.az/xeber/Prezident_Ilham_Aliyev_Suqovusanda_turizm_kompleksinin_temelini_qoyub_VIDEO-2062319).

Fuzuli, Aghdam and Khojavend districts host rich historical and cultural monuments, which opens them up to a wide range of tourism potential. The city of Shusha, which combines elements of both nature and historical and cultural recreation, is the most important point of Karabakh in terms of tourism. It is no coincidence that last year Shusha was declared the cultural capital of Azerbaijan (https://president.az/en/articles/view/51394). The organization of colorful events, festivals, presentation of tourism products, holding international exhibitions and other cultural events in the city is already of great interest (Salmanlı R., 2022 (https://www.azerbaijan-news.az/en/posts/detail/qarabagin-zengin-turizm-potentiali-var-1644093605)).

The attractiveness of investing in Karabakh is not limited to the factors directly related to the region itself. Positive aspects of the country's investment climate in general are also encouraging factors. The following are examples of this:

- Favorable trade conditioins under an Europeand Union Cooperation and Partnership Agreement
- Growing well-trained and qualified workforce
- Developed transregional transport infrastructure
- Political and economic stability
- Easy registration and operation processes – “One Stop Shop (Bir pəncərə)” system (PwC, 2022).

In addition to these strengths, the Karabakh economic region also has its weaknesses. Most of them are related to the past of the occupation. It is clear that over the past 30 years, the economy in the region has been completely destroyed and almost never developed. For this reason, the economy must be restored and the economic activities to be established must be formed almost from scratch which will take long time. Water, gas and energy supply has to be rebuilt too.

The main driving force of any economy is the population. The population is both a human resource and a consumer. For this reason, the more developed a society is in a given region, the more complex the social and economic relations, the more prosperous the economy can be. From this point of view, the current situation in Karabakh is clearly not heartening. In order to build the region's economy, IDPs must return home and adopt the norms of daily life. The government is taking operative measures in this direction. These include the restoration of infrastructure in the region, the planning and construction of settlements on the basis of “smart city” and “smart village” principles. For example, enough work has already been done in this direction in Agali village of Zangilan region (https://president.az/en/articles/view/53631).

However, the process of returning the population to Karabakh has not yet begun, and we can say that it will take a long time for a number of objective reasons. Thus, this is definitely one of the weakest factor in Karabakh Economic Region in the view of investment.

Another issue is the former militarization of the area. Most areas of the economic zone, especially the former contact line, are heavily mined. This situation is delaying activities in the area, as well as endangering human life. From November 10, 2020 to February 28, 2022, 10,600 anti-personnel mines, 4,865 anti-tank mines and 14,045 unexploded ordnance were found (https://azertag.az/xeber/2037368). The head of the press service of the Interior Ministry said that 85 civilians were hit by landmines in the liberated areas after the war (https://report.az/hadise/isgaldan-azad-edilmis-erazilerde-minaya-dusen-sexslerin-sayi-aciqlanib/). Unfortunately, mines are not the only problem. At the same time, other military defense facilities and unexploded ordnance built in the area over the years have a negative impact on the situation. Special attention should be paid to this issue for the rapid recovery of the region and the improvement of the investment climate.

We can add the following to the mentioned problems:

- Degradation of natural conditions in some parts of the region as a result of environmental terrorism committed during the occupation
- Investors' possible psychological reluctance as the region is post-conflict/war zone
- The issue of integration of ethnic Armenians, citizens of Azerbaijan in Karabakh, into the socio-political life of our country

When talking about opportunities, we must first look at the trilateral statement signed by the presidents of Azerbaijan, Armenia and Russia. The ninth paragraph of the statement envisages the opening of all transport and economic ties in the region, as well as the restoration of land links between the western regions of Azerbaijan and the territory of the Nakhchivan Autonomous Republic (http://kremlin.ru/events/president/news/64384). The realization of this corridor will first of all provide more flexible access to the world market by increasing the transport capacity of the Karabakh region, as well as increase the transit importance of the region, and perhaps turn it into a transportation hub. Although the work in this direction has been delayed by the Armenian side, appropriate solutions continue to be taken. Based on the terms of the Moscow Declaration of January 11, 2021, a working group has been set up to work on the issue (https://president.az/ru/articles/view/50070).

Another noteworthy agreement is the Memorandum of Understanding signed between the Deputy Prime Minister of Azerbaijan and the Minister of Roads and Urban Development of the Islamic Republic of Iran on the establishment of new communication links between the East Zangazur economic region and the Nakhchivan Autonomous Republic. In fact, it can be considered as an alternative to the corridor through Armenia. Thus, the diversification of transport routes saves the region and the country from dependence on political games (https://www.bbc.com/azeri/azerbaijan-60770645).

In the previous sections, it was written about the construction of Karabakh's energy infrastructure. As an important element of this sector, the liberated territories have been declared green energy zones by the President's decree. In order to appoint an specialized international consulting company on the development of the relevant concept and master plan, it was decided to allocate AZN 1,391,040.0 from the reserve fund of the President of the Republic of Azerbaijan envisaged in the 2021 state budget of the Republic of Azerbaijan to the Ministry of Energy (http://e-qanun.az/framework/47397). It will help the region to have a sustainable energy network, to ensure the use of clean energy by the enterprises operating there, and to conduct environmentally friendly production. Given that the world's sensitivity to climate change is growing and companies are constantly focusing on this issue to protect their reputations, Karabakh could open up promising opportunities for foreign investors.

The post-war period also posed specific threats to Karabakh. These are mainly related to the war and the current state of affairs. For example, despite the tripartite statement, illegal armed groups have not yet been expelled from Karabakh. This threatens the establishment of stability and socio-economic prosperity in the region. These armed groups regularly commit provocations in Karabakh. An example of this is the recent incident committed by Armenian armed groups in Khojaly region at March, 2022 (https://mod.gov.az/az/news/mudafie-nazirliyinin-melumati-39654.html).

In addition, a final peace agreement with Armenia has not yet been signed. Our western neighbor is still delaying the agreement as much as possible and is trying to maintain tensions in the region. For this reason, during the demarcation and delimitation of the state border, even armed conflicts occur. In May, July, September and November 2021, there were battles on the border (https://mod.gov.az/az/xeberler-arxivi-141/). These noted issues also increase the likelihood of heavy fighting in the future, which hinders the region's goal of becoming a safe and secure place for foreign investment.

Armenia's disregard for international agreements does not only lead to military problems. At the same time, economic and transport relations are stagnant. The other side may continue to prevent the resumption of communications, especially in the Zangazur corridor. Such behavior invalidates Armenia's obligations under other agreements reached.

CHAPTER III. EXPERIENCED METHODS OF ATTRACTING FOREIGN INVESTMENT

3.1. Independence era government efforts on bringing foreign investments

In the first years of independence, Azerbaijan had to deal with both the difficulties of the transition from a planned economy to a market economy, as well as the hardships of a large-scale war and its aftermath. Against this background, the political turmoil in the country did not even allow us to think about a few foreign investments. All the resources of the economy were concentrated on the Karabakh front, and the country's economic leadership became chaotic due to political disputes. Only after the signing of a ceasefire agreement and ensuring political stability it was possible to focus on this issue.

The history of foreign investment in Azerbaijan dates back to 1995. Thus, the signing of the Production Sharing Agreement (PSA) on the Azeri-Chirag-Guneshli oil field (located in Azerbaijani part of the Caspian sea), the country's first international oil agreement, was the beginning of foreign direct investment in the country (Mehtiyev A., 2018).

As mentioned in the previous paragraphs, the main factor for the formation, development and attractiveness of the investment climate in the country is the creation of an appropriate legislative framework in this area. In this way, the boundaries of investments are determined, their protections, as well as restrictions are selected, and their rights and obligations are clarified. So the state forms the appropriate legal and regulatory framework, creates institutions and supports a competitive business environment.

The law of the Republic of Azerbaijan on protection of foreign investments was first adopted in our country in 1992. The law is aimed at attracting foreign material and financial resources, advanced foreign equipment and technology, management practices in the national economy, their effective use and guarantees the protection of the rights of foreign investors. Forms of foreign investment, types of activities, taxes, customs, accounting, etc. points are reflected here. According to this law, all types of property and property rights that foreign investors invest in entrepreneurial and other activities for profit, including rights to the results of intellectual activity and other rights not related to property rights, are foreign investments.

The next important legislative act is the Law of the Republic of Azerbaijan on Investment Activity, signed in 1995. This determines investment activity's (investment) general economic, social, legal conditions in territory of the Republic of Azerbaijan and defines investment concepts. The law is aimed at intensive investment in the economy of the Republic of Azerbaijan, its effective use for the development of the country's socio-economic base, as well as international economic cooperation and integration, and guarantees equal protection of the rights of all investors, regardless of ownership. We can consider these two laws as a initial national legal basis for foreign investment in Azerbaijan.

Legal framework on foreign innvesments in the Republic of Azerbaijan are regulated not only by national legislation, but also by multilateral agreements ratified by our country. Bilateral agreements on mutual protection and promotion signed with foreign countries also provide additional protection for foreign investors. At present, about 30 such agreements have been signed between the Republic of Azerbaijan and various countries of the world, and a joint or intergovernmental state commission has been established between the Government of the Republic of Azerbaijan and the governments of 53 countries (http://economy.gov.az/index.php?option=com_content&view=article&id=272&Itemid=162&lang=az).

In addition, in order to increase and stimulate investment in the country's economy, the Republic of Azerbaijan cooperates with international organizations and financial institutions such as United Nations, World Trade Organization, European Union, Commonwealth of Independent States, GUAM, Economic Cooperation

Organization, Black Sea Economic Cooperation Organization, World Bank, International Monetary Fund, European Bank for Reconstruction and Development, Asian Development Bank, Islamic Development Bank, Black Sea Trade and Development Bank and International Finance Corporation.

As you know, one of the most important conditions of the business environment is the tax regime. Tax relations in relation to the investor are regulated by the "Tax Code of the Republic of Azerbaijan" approved by the Law of the Republic of Azerbaijan No. 905IQ on July 11, 2000. It should be noted that in recent years, certain steps have been taken to reduce taxes and social insurance payments. Since 1998, tax rates in the country have been gradually reduced. Thus, the corporate income tax rate is from 35% to 20%, as well as the VAT rate is from 28% to 18%, the maximum rate of personal income tax is from 55% to 35%, social reduction of insurance deductions from 40% to 22% , reduction of the number of state taxes from 15 to 9 as a result of abolition of some taxes, exemption of entrepreneurs engaged in agricultural production from other taxes except land tax, etc (https://www.taxes.gov.az/az/page/ar-vergi-mecellesi). Measures to reduce the tax burden on such investors have been implemented in recent years. In addition, tax administration has been improved and agreements have been signed with a number of foreign countries on the elimination of double taxation, as well as the promotion and mutual protection of investments (https://www.taxes.gov.az/az/page/ikiqat-vergitutmanin-aradan-qaldirilmasi-haqqinda-beynelxalq-muqavilelerin-inzibatciligi-qaydalari).

In order to bring the activities of the customs authorities in line with international standards, to further simplify and make the procedures more transparent, the Customs Code was adopted, approved by the Law of the Republic of Azerbaijan No. 164-IVQ of June 24, 2011 (https://e-qanun.az/framework/22248). The presidential decree "On some measures for the development of entrepreneurship in the Republic of Azerbaijan" envisages the simplification of procedures for launching multi-stage economic activity, the elimination of existing bureaucratic obstacles in this area. According to the decree, the relevant government agencies apply a single coding system, while the activities of business entities are organized on the principle of "one stop shop (bir pəncərə)". This decree is of fundamental importance for the removal of obstacles to the development of entrepreneurship in the country. At the same time, in order to develop a competitive environment in the domestic market, to regulate the tariffs for products and services of natural monopolies, the President of the Republic of Azerbaijan signed a decree No.341 on December 26, 2005 to approve the the Regulation of the Tariff Council of the Republic of Azerbaijan (https://president.az/az/articles/view/18138).

Accordingly, the Ministry of Economy and Industry has a relevant Secretariat and 12 working groups covering various areas. A number of measures have been taken to simplify the licensing system in the country. Thus, the existing licensing system in the country has changed radically, the number of licensed activities has been reduced from 240 to 30, and the term of the license has been extended from 2 to 5 years (Ibadoğlu Q., 2020).

The Azerbaijan Export and Investment Promotion Agency is the main entity in charge of investment promotion for country (AzPromo). AzPromo is a public-private partnership launched in 2003 by the Ministry of Economy and Industry to promote the economic growth and diversifying by attracting international investment and increasing non-oil industries. Azerbaijani President Ilham Aliyev issued a proclamation in January 2018 calling for new legislation, which has yet to be implemented, to guarantee that the country complies with international norms to defend international investment rights.

Since the beginning of 2016, the government has implemented investment and tax incentives for corporations and business entities in sectors that are not directly related to oil and gas as part of the overall macroecomic divesification and reform initiatives. Certain temporary partial exemptions from property and income taxes; favorable tax conditions for manufacturing plants and purchasing of manufacturing equipment; financial aids for special exports are included. Holders of the investment certificate don’t have to pay 100% of customs payments on importing equiptment, material, machinery, devices, 50% of the corporate tax; 100% of the land tax; and. Certificates are valid for 7 years in the entreprenurs on non-oil business.

In March 2016, a government decision formed the Alat Free Economic Zone (AFEZ) near to the Port of Alat, some 50 miles south of Baku. In June 2018, President approved legislation outlining the AFEZ's incentives and rules. The legislation excludes all AFEZ firms from taxation and custom duties; requires the AFEZ authority to establish its own personnel, relocation, conflict resolution, and arbitration policies; protects against nationalization; and ensures the free movement of capital into or out of the zone. The AFEZ is almost completely functioning, the legal structure is in effect and early development has commenced.

The Ministry of Transportation, Communications, and High Technologies (now, The Ministry of Digital Development and Transport) has explored proposals to establish more special economic zones, including as a petro - chemical complexes and regional technology zones, to help the telecoms sector grow. Until 2023, private corporations and people engaged in entrepreneurial activity in one of 5 government industrial or technology parks are free from paying corporate tax, property tax, land tax, or Value-added tax on importing machineries (Bureau of Economic and Business Affairs, 2020).

To get an overview of the results of the steps taken, we can take a look at the inflow of FDI to Azerbaijan for different years:

Table 4: FDI inflows of Azerbaijan during independence era ($ millions)

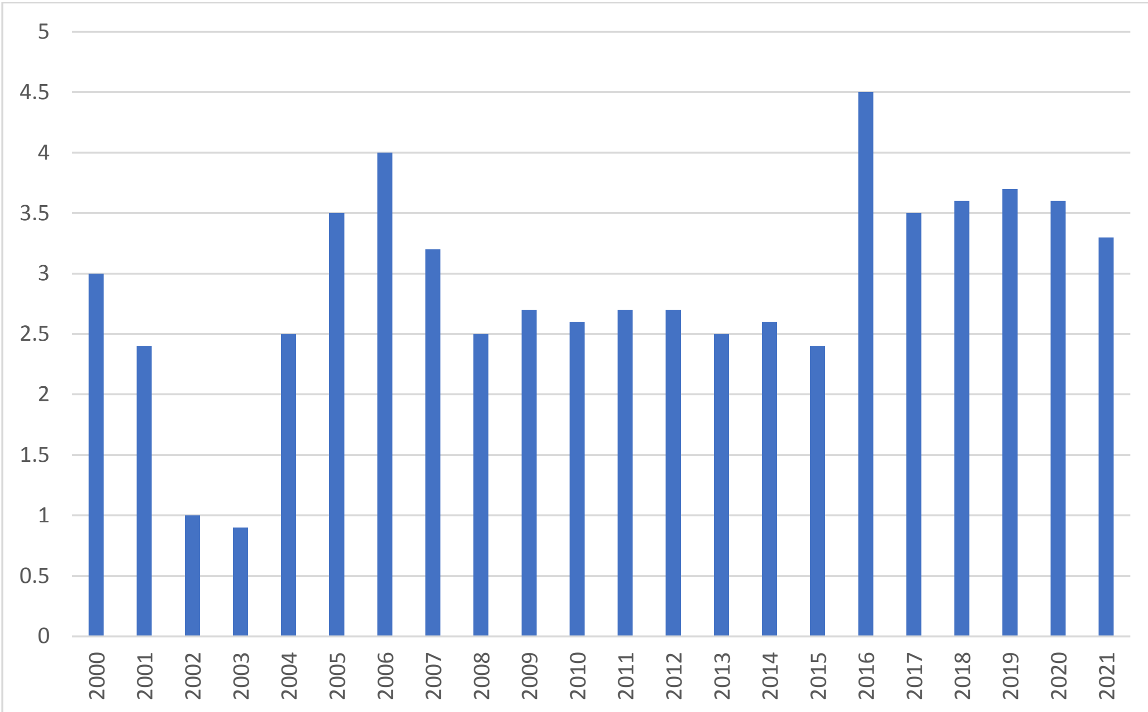
Years	FDI inflow
2001	813
2006	4469
2011	4444
2016	7323
2017	5713
2018	4109
2019	4275
2020	4528
2021	4795

Source: Central Bank of Azerbaijan (https://www.cbar.az/page-43/external-sector-statistics)

As can be seen from the above figures, the volume of foreign direct investment in Azerbaijan has been generally stable in the first 10 years of the 21st century. It peaked only in 2016, and although it declined the following years, it rose again slowly towards 2021.

The most unpleasant thing about foreign investment in Azerbaijan is that most of them belong only to the oil and gas sector. If we analyse figures from State Statistical Comitee, we can see the low rate of FDI on non-oil industries and sercives:

Figure 4. Non-oil FDI ratio to non-oil GDP in Azerbaijan, 2000-2021 (percent)



Source: Prepared on the basis of data from State Statistical Committee

It is significantly important for Azerbaijan, which is attempting to diversify its exports to take foreign direct investment to non-oil industries, notably the processing industry, in order to lessen its dependency on oil and gas income. As a result, it's quite suitable that one of the four primary indicators listed in the government's Strategic Roadmap of the National Economy Prospects is to achieve a 4% proportion of non-oil foreign investments in GDP by 2025. (compared to 2.6 per cent in 2015) (https://president.az/az/articles/view/29589).

3.2. Suggestions to attract foreign investments in Karabakh Economic Region

The previous paragraphs provided a detailed analysis of the current investment climate in Karabakh, the work done by the Azerbaijani government to attract foreign investment, as well as experiences from two different regions of the world that share a similar fate with Karabakh. The steps to be taken to increase the attractiveness of Karabakh's foreign investment can be determined on this basis. As we studied in the previous chapter, Karabakh has a wide range of economic opportunities. At the same time, there are some weaknesses and threats in the region, without which it will be very difficult to attract foreign investment. On the other hand, the steps taken by the government and the study of the created investment climate give us a basis for the next decisions to be made. In this way, successful decisions can be improved and undesirable steps can be replaced in different ways.

The investment potential of a region depends not only on its own conditions, but also on the general business environment of the country within which it is located. For this reason, first of all, it is necessary to identify steps that can be taken to improve the investment climate in Azerbaijan and make the country a sustainable place for foreign investment. Based on the analysis and experience in the previous paragraphs, we can say that these steps include:

- Developing and implementing an unified government strategy to attract foreign investment. In this case, the main goal is to develop and implement a constructive policy by comprehensively and coherently assessing investment opportunities in the country and regions, so inviting investment more complex and reliably. It will also eliminate sharp differences between regions in terms of investment and help to efficiently utilize the resources of all regions;
- Improving government oversight accountability, transparency, and the elimination of corruption. Undoubtedly, the transparency of the government in the destination country is very important for foreign investors. Only in this case, entrepreneurs can confidently invest in the country and expect a reliable income;
- Improving investment legislation in the country and bringing it in line with the latest standards. Attracting investments is a matter of competition between the countries of the world, and in order to be successful in this area, it is necessary to have a favorable legal framework for investors. It is clear that entrepreneurs demand the highest conditions of protection for themselves, and the country that wants to attract them must meet these requirements within its interests. In this regard, the legislative

framework of Azerbaijan has developed quite positively, but there is still a need for additions;

- Fully activating Alat Free Economic Zone and creation of new special economic zones. SEZs are one of the most attractive points for foreign investors and also contribute to the development of the economy by improving the overall market relations of the country;
- Introduction of new incentives for foreign investors, simplification and further transparency of registration, customs and tax procedures;
- Establishment of a new “coordination office” to investigate foreign companies interested in large-scale investment projects and appoint strategic key account managers who will work directly with them;
- Increasing investment cooperation with different countries and reaching new agreements, offering special discounts to entrepreneurs of relevant countries;
- Making the distribution of investments more equal across sectors, increasing the economic potential of non-oil sector to attract investment. Azerbaijan's rich hydrocarbon resources have helped attract large amounts of foreign investment to the sector. However, other industries and services need investment to build a more sustainable economy. Therefore, steps must be taken to make these areas more attractive for foreign entrepreneurs. An example of this is the application of extra incentives, discounts or protections for entrepreneurs who invest in relevant areas;
- Raising the level of digitalization of transportation in the country, automation of operations in transport entities - ports and terminals in order to increase the efficiency of logistics processes;
- Development of education. Education is a tool for progress and creativity. The hiring of some specialized advisers to guide pupils relating to professional abilities could boost their value. Because foreign investors have a high demand for students to perform internships in various firms, there is a need to expand the number of students who can attend those internships and meet the eligibility conditions.

In addition to these, there are issues that need to be addressed directly related to the region itself. The work that needs to be done in this direction is to address the vulnerabilities and threats highlighted in the previous sections of the study. Thus, based on the results of the study, the following proposals can be implemented to increase the investment attractiveness of the Karabakh economic region

- Accelerating the restoration of transport and economic infrastructure in the region. Large-scale infrastructure projects are currently being implemented in Karabakh. The completion of these projects in the near future and the provision of the entire zone with a comprehensive transport network will prepare the area for investment;
- Providing the region with energy from its own resources. As noted in the previous paragraphs, Karabakh has extensive natural energy resources (especially solar and water). Meeting the region's energy needs through local resources will help make energy prices more economical and increase supply efficiency. At present, preliminary ideas have been put forward in this direction;
- Starting of the return of IDPs to the region and build modern settlements in the region. The main driving force of economic revival in Karabakh will be the people who will live there, ie the consumer, the labor force and the society that will sustain the economy. For this reason, the return of residents to the region should be carried out as soon as possible;
- Establish cooperation with foreign countries that have antimining experince and invitation of their specialists to accelerate the clearance of areas from mines and unarmed weapons, as well as the provision of new special equipment for this work;
- Elimination of the ecological crisis created in the region during the occupation and restoring the nature;

- Implementation of awareness-raising activities and social campaigns in the direction of integration of the ethnic Armenian population of the region into the Azerbaijani society and economy;
- Taking decisive steps in the political arena to implement the Zangazur corridor, as well as to restore other transport and communication links. Although the Zangazur corridor is valuable for Azerbaijan's transport opportunities in general, it is of special importance for Karabakh. The opening of this corridor will help Karabakh to become part of international transport corridors and develop rapidly;
- Ensuring the complete withdrawal of illegal armed groups from Karabakh. This is one of the conditions of the tripartite statement, and is a very important requirement for the the security of the region, revival of the economy and society.
- Signing of a final peace agreement with Armenia recognizing Azerbaijan's territorial integrity and ending territorial claims once and for all, as well as normalizing economic and transport relations. Ongoing armed tensions on the border, problems with the delimitation of borders, and the complete isolation of the two countries' economies and communications are major threats to the region. In order to make the region a suitable place for investors, it is necessary to sign a peace agreement that will eliminate these issues.

CONCLUSIONS AND RECOMMENDATIONS

Based on the work performed, the following conclusions can be drawn:

- The Karabakh economic region has a rich economic potential. However, the region's economy and infrastructure have been completely destroyed and need to be rebuilt. On the other hand, security issues remain a serious problem and must be addressed soon.

- Currently, the lack of residents in the economic zone limits its investment attractiveness and in the current situation makes only infrastructure projects suitable for foreign investors. Also, the level of integration of the local ethnic Armenian population of the region into the Azerbaijani society is low;

- The steps taken by the Azerbaijani government’s investment attractiveness policy have been successful both in terms of the legal framework and in terms of technicality, and have facilitated the arrival of FDI in the country. However, there is still a need for improvement, especially to increase investment in the non-oil sector;

- The steps to be taken to increase the investment attractiveness of the Karabakh economic region should be aimed at overcoming the weaknesses and threats to the region and the country itself. These include military-security and political issues, as well as economic and social issues.

The study provided a detailed analysis of the current investment climate in Karabakh, the work done by the Azerbaijani government to attract foreign investment, as well as experiences from two different regions of the world that share a similar fate with Karabakh. The steps to be taken to increase the attractiveness of Karabakh's foreign investment can be determined on this basis. As we studied in the previous chapter, Karabakh has a wide range of economic opportunities. At the same time, there are some weaknesses and threats in the region, without which it will be very difficult to attract foreign investment. On the other hand, the steps taken by the government and the study of the created investment climate give us a basis for the next decisions to be made. In this way, successful decisions can be improved and undesirable steps can be replaced in different ways.

The investment potential of a region depends not only on its own conditions, but also on the general business environment of the country within which it is located. For this reason, first of all, it is necessary to identify steps that can be taken to improve the investment climate in Azerbaijan and make the country a sustainable place for foreign investment. Based on the analysis and experience in the previous paragraphs, we can say that these steps include:

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- Fully activating Alat Free Economic Zone and creation of new special economic zones. SEZs are one of the most attractive points for foreign investors and also contribute to the development of the economy by improving the overall market relations of the country;
- Introduction of new incentives for foreign investors, simplification and further transparency of registration, customs and tax procedures;
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In addition to these, there are issues that need to be addressed directly related to the region itself. The work that needs to be done in this direction is to address the vulnerabilities and threats highlighted in the previous sections of the study. Thus, based on the results of the study, the following proposals can be implemented to increase the investment attractiveness of the Karabakh economic region

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