

THE PROBLEM OF REGIONAL INEQUALITY IN SOCIO-ECONOMIC DEVELOPMENT RESEARCH DOCUMENT



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**THE PROBLEM OF REGIONAL INEQUALITY
IN SOCIO-ECONOMIC DEVELOPMENT
RESEARCH DOCUMENT**

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Summary

The study leads to the conclusion that despite the implementation of three state programs for socio-economic development of the regions in Azerbaijan since 2004, as well as the expiration of the implementation period of the Development Concept “Azerbaijan 2020: Look into the Future”, there are still serious problems in bridging the gap between the socio-economic development of the regions in the country.

Summarizing the analysis of the study, it can be said that there are sharp differences in all parameters of socio-economic development of the country, both between the Baku-Absheron zone and other regions of the country and between the rest of the regions of the country themselves except Baku-Absheron.

Therefore, the study proposes to carry out reforms both in the field of management and regulation of regional development and in the field of mechanisms for stimulating the economic development of the regions to reduce inequality in the socio-economic development of the country and ensure more efficient and balanced development, and makes the following recommendations:

1. It is necessary and expedient to establish a separate central government body responsible for regional development in Azerbaijan;
2. It is necessary to develop special programs for the development of economically problematic regions and regions with unfavorable geographical conditions;
3. It is expedient to develop a special development program for each economic region in Azerbaijan;
4. It is important to strengthen the administrative and financial capacity of municipalities in order to increase their participation in solving regional socio-economic problems;
5. In regional economic development, the cluster approach should be introduced and appropriate strategies should be developed;
6. An analysis of the cluster potential of the regions should be conducted on the basis of quantitative and qualitative methods that allow assessing the competitiveness of the regions;
7. Special requirements must be set for the creation of clusters.

Introduction

Ensuring the balanced development of the regions in Azerbaijan has long been one of the important tasks facing the country. This is also one of the necessary conditions for the sustainable development of the country. Achieving a balance in the socio-economic development of the regions contains the components such as using regional resources and natural conditions efficiently, increasing agricultural production, ensuring the development of non-oil industries, including processing industry, services, other infrastructure, and tourism, increasing employment, and further improving the livelihoods of the population. Bringing the regions to a developed level in terms of socio-economic aspect is a very important factor in ensuring macroeconomic stability of the country, solving the problem of unemployment, achieving a positive balance in the country's trade turnover. However, both the legacy of the Soviet era and the economic crisis in the first years of independence of Azerbaijan led to the deepening of inequality in socio-economic development between the regions of the country. Subsequently, the country's oil strategy and the country's dependence on oil revenues led to a deepening imbalance, especially between the Baku-Absheron zone and other regions of the country. Despite the implementation of a number of state programs in the field of socio-economic development of the regions in the country since 2002, as well as the government's focus on regional development in a number of other state program documents and some progress, albeit small, in this direction, there are still sharp differences and high inequalities between the levels of socio-economic development of the country's regions. This difference is especially sharp between the Baku-Absheron zone and all other regions of the country. At the same time, even with the exception of the Baku-Absheron zone, the differences between the levels of development of other regions of the country are worrying.

This policy paper analyzes policies implemented by the government since 2002 to reduce inequality in regional socio-economic development and achieve balanced regional development and makes recommendations for improving this policy.

The first part of the study analyzes the current state of inequality in regional socio-economic development on the basis of official statistics and examines its causes. The study then examines the policy steps taken so far by the government to address this problem and presents the results of these policies and the results obtained from the study.

Then, on the basis of international experience, the directions of necessary changes needed to be made in government policy are presented in order to reduce inequality in the socio-economic development of the regions and achieve balanced development of the regions.

In the end, these directions are specified and presented in the form of recommendations.

The policy statement was developed in a desk research format.

1. The problem of regional inequality in socio-economic development: the current situation and its causes

One of the important conditions for sustainable and balanced development in the country is to ensure mainly the same level of impact of the overall social and economic development of the country on its entire population and all regions.

The territory of Azerbaijan seems to be divided into two sharply different parts according to the level of socio-economic development and economic potential: 1) about 75-80% of the country's economic potential is concentrated in Baku and the Absheron Peninsula, which cover only 7% of the country's territory and are home to up to 30% of the population; 2) only 20-25% of the country's economy is concentrated in other areas covering 93% of the country's geography and 70% of the population. At the same time, there are significant differences in the level of socio-economic development and economic potential between the individual regions in the second part.

To better see and understand these differences, let's first look at the regional territorial and population structure of Azerbaijan by economic regions (Table 1).

Table 1. The regional territorial and population structure of Azerbaijan by economic regions (as of January 1, 2019)

	Territory		Population	
	area, thousand sq. km	share in total, %	number, thousand people	share in total, %
Republic of Azerbaijan, total	86.6	100	10,067.1	100
Baku city	2.14	2.47	2,293.1	22.8
Absheron economic region	3.73	4.31	576.5	5.7
Ganja-Gazakh economic region	12.30	14.20	1,294.1	12.85
Shaki-Zagatala economic region	8.84	10.21	626.7	6.23
Lankaran economic region	6.07	7.01	946.7	9.40
Guba-Khachmaz economic region	6.96	8.04	554.7	5.51
Aran economic region	21.15	24.42	2,046.3	20.33
Upper Karabakh economic region	7.33	8.46	687.7	6.83
Kalbajar-Lachin economic region	6.42	7.41	259.5	2.58

Mountainous Shirvan economic region	6.13	7.08	322.2	3.20
Nakhchivan Autonomous Republic	5.50	6.35	459.6	4.57

(Source: State Statistical Committee)

According to the SSC, the country's **gross output** in 2019 amounted to 88.9 billion AZN. Of this, 60.9 billion AZN (or 68.9%) fell to Baku city and another 5.3 billion (5.9%) to the Absheron economic region. Thus, **75.8%** of the country's gross output was created in the Baku-Absheron zone. However, in the same year, the Aran economic region, the largest economic region in terms of territory and population, created a gross output of 7.5 billion AZN, which is 9.0% of the country's gross output. In 2019, 4.6% (4.1 billion AZN) of the country's gross output fell to the Ganja-Gazakh economic region, 2.5% (1.9 billion AZN) to the Shaki-Zagatala economic region, 2.2% (1.8 billion AZN) to the Lankaran economic region, 2.5% (2.1 billion AZN) to the Guba-Khachmaz economic region, 1.1% (1.0 billion AZN) to the Mountainous Shirvan economic region, and 4.7% (3.6 billion AZN) to the Nakhchivan Autonomous Republic (We do not include the Upper Karabakh economic region and the Kalbajar-Lachin economic region, most of which were under occupation).

Calculations based on the data of the SSC show that the annual **GDP per capita** created in the country in 2019 amounted to 3,831 AZN in Baku, 1,000 AZN in the Absheron economic region, 400 AZN in the Ganja-Gazakh economic region, 200 AZN in the Aran economic region, 190 AZN in the Shaki-Zagatala economic region, 150 AZN in the Guba-Khachmaz economic region, 90 AZN in the Lankaran economic region, 88 AZN in the Mountainous Shirvan economic region. As can be seen, the difference between the GDP per capita in Baku and the region with the lowest rate in the country is **more than 43 times**.

According to the SSC, the **total income of the population** in Azerbaijan in 2019 amounted to 56.8 billion AZN. Of this, 33.0 billion AZN or 58.1% was formed in Baku and 2.3 billion or 4.1% in Absheron: in other words, **62.2%** of the total annual income of the population fell to the Baku-Absheron zone. 12.7% (7.2 billion AZN) of the total income of the population fell to the Aran economic region, 8.2% (4.7 billion AZN) to the Ganja-Gazakh economic region, 4.5% (2.6 billion AZN) to the Lankaran economic region, 3.3% (1.9 billion AZN) to the Shaki-Zagatala economic region, 3.3% (1.9 billion AZN) to the Guba-Khachmaz economic region, 1.7% (1.0 billion AZN) to the Mountainous Shirvan economic region, and 3.3% (1.9 billion AZN) to the Nakhchivan AR.

In 2019, 39.7 billion AZN or 84.6% of the 47.0 billion-AZN **industrial output** produced in the country was produced in Baku and 2.4 billion AZN (5.0%) in Absheron. In other words, 89.6% of the total industrial output in the country was produced in the Baku-Absheron zone. Only 10% of the industrial output was produced in the rest of the country.

In 2019, 11.9 billion AZN or 80% of the 14.9 billion-AZN total **credit investment** directed to all sectors of the economy in the banking sector of the country fell to Baku.

In 2019, the total amount of **investments in fixed assets** in the country amounted to 18.5 billion AZN. Of this, 10.9 billion AZN was realized in Baku and 2.5 billion AZN in the Absheron economic region. Thus, 13.4 billion AZN or **72.4%** of the annual capital investment fell to the Baku-Absheron zone. In

other regions, the amount of investments in fixed assets during the year and their share in total investments in the country were as follows:

- Aran economic region - 1,319.4 million AZN or 7.0%,
- Ganja-Gazakh economic region - 884.0 million AZN or 4.8%,
- Shaki-Zagatala economic region - 404.2 million AZN or 2.2%,
- Lankaran economic region - 283.3 million AZN or 1.5%,
- Guba-Khachmaz economic region - 672.6 million AZN or 3.6%,
- Mountainous Shirvan economic region - 387.4 million AZN or 2.1%,
- Nakhchivan Autonomous Republic - 1,029.3 million AZN or 5.6%.

According to the SSC, the **total amount of capital investment** in the country in 2010-2019 amounted to more than **154.0 billion AZN**. Of this, 103.8 billion AZN or **67.5%** was realized in Baku, and the remaining 50.0 billion AZN was directed to the country's regions. During this period, 6.8 billion AZN (4.4%) has been invested in the Absheron economic region, 7.3 billion AZN (4.8%) in the Ganja-Gazakh economic region, 3.7 billion AZN (2.4%) in the Shaki-Zagatala economic region, 3.3 billion AZN (2.1%) in the Lankaran economic region, 4.9 billion AZN (3.2%) in the Guba-Khashmaz economic region, 11.7 billion AZN (7.6%) in the Aran economic region, 2.2 billion AZN (1.4%) in the Mountainous Shirvan economic region, and 9.3 billion AZN (6.0%) in the Nakhchivan Autonomous Republic.

At that time, almost no investment was made mainly in the occupied Upper Karabakh and Kalbajar-Lachin economic regions for obvious reasons. However, in recent years, about 1 billion AZN has been used for the settlement and landscaping of Jojug-Marjanli and some other areas in the Upper Karabakh economic region. But in 2020, as a result of the victory of our brave army, our occupied lands were liberated from occupation, and in the next 10 years, in these two regions - Upper Karabakh and Kalbajar-Lachin economic regions - large amounts of money will be required for the implementation of restoration, revitalization, and settlement works, reconstruction of all types of infrastructure (social, industrial, technological, etc.). The state budget for 2021 has already envisaged the allocation of 2.2 billion AZN for this purpose.¹

At the same time, it is planned to attract business, especially local and foreign investors, to the restoration and revitalization of these areas and to make extensive use of "public-private" cooperation mechanisms.

When we talk about the provision of social services, the first thing that comes to mind is the provision of education and health services. There are various differences between Baku and the regions in terms of pre-school education and qualified staff. The **number of doctors per 10,000 population** is 91 in Baku, 30 in the Absheron economic region, 19 in the Ganja-Gazakh economic region, 17 in the Shaki-Zagatala economic region, 10 in the Lankaran economic region, 13 in the Guba-Khachmaz economic region, 14 in the Aran economic region, 10 in the Mountainous Shirvan economic region.

¹ <https://static.president.az/media/W1siZiIsIjIwMjEzMDEvMDUvODFnenF1dzE3bF9-kb3ZsZXRFYnVkaS5wZGYiXV0?sha=06d54f2e87befc80>

The gas supply indicators of individual regions vary around 45-95%. Drinking water supply through a centralized network is very different in different regions. The lowest rate for this service is in the range of 2-10% (in Gadabay, Aghjabadi, Jalilabad, etc.). The provision of centralized sewerage services is worse in the regions. Official figures show that in 18 of the more than 60 rural districts, the level of centralized sewerage services is less than 20%, and in 32 districts, it is less than 40%.²

At present, the role of the Internet in ensuring sustainable access to information is irreplaceable. As the Internet is not profitable for the population in our country, the level of the provision of telephone lines in apartments is an important indicator.

According to official statistics, the number of landline telephones per 100 families is currently 113 in Baku, 99 in Absheron, and 30-60 in other regions. Thus, it can be said by summarizing the above analysis that there are sharp differences in almost all parameters of socio-economic development of the country, both between the Baku-Absheron zone and other regions of the country and between the rest of the regions of the country themselves except Baku-Absheron. This situation is a factor leading to increasing poverty and unemployment in the country's regions, deepening social stratification, intensification of migration processes among the population, and accelerating the flow of population to the Baku-Absheron zone. If the process of development of industrial production and other sectors of the economy in the regions is not given due attention, poverty in the country's regions will increase rapidly, social stratification will deepen, which may have very serious socio-economic consequences.

Differences in socio-economic development between the regions of the country depend on many factors. Among such factors are, first of all, the following:

- economic and geographical position;
- natural conditions and resources;
- settlement level of the population;
- sectoral and territorial structure of the region;
- historical development features.

The first State Program on Socio-Economic Development of the Regions of the Republic of Azerbaijan for 2004-2008 emphasized that along with these factors determining the socio-economic development of the regions, the role of the following in the emergence of differences between them and the poor development of most economic regions should be emphasized:³

1. The disproportionate distribution of productive forces between the regions has created a sharp difference in their level of socio-economic development. Such that the concentration of the main part of the economy, especially industry and infrastructure areas, in Baku has not only led to its faster development than the regions but also aggravated the socio-economic situation in the regions and the influx of people from the regions to Baku.
2. As a result of Armenia's war of aggression against Azerbaijan, 20 percent of the lands were occupied, the existing economic potential in the occupied regions was looted, production,

² <https://bakuresearchinstitute.org/az/paytaxt-v%20c%2099-%20c%2099yal%20c%2099tl%20c%2099r-%20c%2099sas-sosial-iqtisadi-f%20c%2099rq1%20c%2099r/>

³ <http://www.e-qanun.az/framework/4797>

technical, and infrastructure facilities were destroyed, the Azerbaijani people suffered numerous casualties, and about one million citizens lost their homes, jobs, and wealth and became refugees in their homeland.

3. Despite the fact that as a result of land and agrarian reforms in Azerbaijan, the majority of the population living in the regions became owners of land and other real estates, lack of initial capital in humans, as well as lack of conditions for the development of the agricultural sector, including machinery, services, consulting services, infrastructure, processing facilities, etc., limit the effective use of opportunities.

In addition to the above, it is important to point out the problems and gaps in governance and state regulation of the economy as other important causes of inequality and imbalance in the country's regional development.

2. Measures taken so far to solve the problem and their results

The issues of elimination of inequality and balanced development of regions, which are among the development of regions in Azerbaijan, have been reflected in many policy and strategy documents adopted by the government over the past 20 years. The country has adopted four state programs in the field of socio-economic development of the regions, the first three of which have already been implemented:

- 1) The main goals of the State Program on Socio-Economic Development of the Regions of the Republic of Azerbaijan for 2004-2008 approved by the Decree of the President of the Republic of Azerbaijan No. 24 dated February 11, 2004, are sustainable development of the non-oil sector, ensuring the balanced development of the country's regions, improving the provision of utilities and social infrastructure in the regions, increasing employment of the population as a result of the creation of new jobs and enterprises, and improving living standards of the population;
- 2) In order to accelerate the development of the non-oil sector in the country, diversify the economy, achieve balanced regional and sustainable socio-economic development, and further improve the living standards of the population, the State Program on Socio-Economic Development of the Regions of the Republic of Azerbaijan for 2009-2013 was approved by the Decree of the President of the Republic of Azerbaijan No. 80 dated April 14, 2009, in order to continue the activities started in 2004. As a result of the successful implementation of this State Program, the country has achieved high growth in the level of macroeconomic indicators, the implementation of measures in the field of socio-economic development has played an important role in further improving the living standards of the population;
- 3) As a continuation of the purposeful policy in the field of comprehensive development of the regions started in 2004, the State Program on Socio-Economic Development of the Regions of the Republic of Azerbaijan for 2014-2018 was approved by the Decree of the President of the Republic of Azerbaijan No. 118 dated February 27, 2014. The main goals of the State Program were to develop the non-oil sector in the country, diversify the economy, continue measures for the rapid development of the regions, especially to further improve the infrastructure and social services related to rural development;
- 4) The State Program on Socio-Economic Development of the Regions of the Republic of Azerbaijan for 2019-2023 was approved by the Decree of the President of the Republic of Azerbaijan No. 500 dated January 29, 2019.

Achieving balanced development of the regions was identified as one of the main goals of the Development Concept “Azerbaijan 2020: Look into the Future”. The main goals set in the Concept for the balanced development of the regions were as follows:⁴

- Coordinating business investment strategies with the state's infrastructure and investment policy in the regions by taking into account regional development priorities, prioritizing them in terms of economic efficiency based on cost-benefit analysis;

⁴ Development Concept “Azerbaijan 2020: Look into the Future” https://www.president.az/files/future_az.pdf

- Elimination of differences in living standards and quality of life, per capita product output, the volume of investments, sharp differences in the structure of trade turnover by economic regions, reduction of existing differences between economic regions of the country;
- Increasing the flexibility of local self-government bodies in making economic decisions within the framework of a modern approach;
- Stimulation of ensuring balanced socio-economic development in the regions through regional development centers, thus reducing regional inequality, slowing down the concentration of economic resources, mainly in central cities.

Another step taken in connection with the problem is the Investment Promotion Document. The main goals of the document were to expand investment activities, improve the business environment, increase industrial production, and improve the investment promotion mechanism in accordance with Paragraph 5.2 of the Action Plan for the implementation of the State Program for Industrial Development in the Republic of Azerbaijan for 2015-2020.

The State Program on Socio-Economic Development of the Regions of the Republic of Azerbaijan for 2019-2023 states: “The policy pursued by the state to build a socially oriented economy and provide decent jobs has made a positive contribution. As a result of purposeful measures taken in the field of socio-economic development of the country, more than 2 million new jobs were created during 2004-2018, of which 1.5 million were permanent, and 75% of these jobs fell to the regions.”⁵

The program emphasizes that in order to develop industrial production in the regions, by the Order of the President of the Republic of Azerbaijan No. 1077 dated February 26, 2015, Mingachevir Industrial Park, Neftchala Industrial District (9 enterprises and 1 small business workshop operate here), and Masalli Industrial District (10 enterprises operate here) has been established. Work is underway to establish Hajigabul Industrial District and Sabirabad Industrial District. For the development of the carpet business in the country, carpet production factories of Azerkhalcha OJSC have been established in 20 regions of the republic.

The private sector is supported in the regions through Azerbaijan Investment Company OJSC, Entrepreneurship Development Fund of the Republic of Azerbaijan, Agrarian Credit and Development Agency under the Ministry of Agriculture of the Republic of Azerbaijan, Agroleasing OJSC, AZPROMO, and other institutional mechanisms.

At the same time, the steps taken in recent years to improve the business environment in the country are important in terms of creating new incentives for regional development. As part of the reforms implemented for the development of entrepreneurship, as a result of comprehensive measures to regulate the system of licenses and permits and simplify administrative procedures, the number of licensed activities was reduced from 59 to 37, the number of permits from 330 to 86, newly issued and valid term licenses were established indefinitely, the amount of state fee for issuing licenses was

⁵ <http://www.e-qanun.az/framework/41320>

reduced by about 2 times, by regions by 4 times, the term of issuing licenses was reduced from 15 to 10 working days, and procedures were simplified.⁶

Within the framework of state programs, important measures have been taken to restore and develop infrastructure in the regions, provide the population with utilities, including electricity, gas, and water, build health and education facilities, and further improve the social situation of the population. Large-scale public investments have been made in this area.

“Over the past 15 years, construction, overhaul, and reconstruction works have been carried out in 2,980 schools, 360 preschools, and 477 health facilities in the regions, 34 Olympic Sports Complexes and 34 Youth Houses have been built in the regions.”⁷

Despite the implementation of three special programs, as well as other steps, it is difficult to say that much progress has been made in eliminating inequality in the country's regional development. This is confirmed by the above analysis.

Therefore, the main objectives of the State Program on Socio-Economic Development of the Regions of the Republic of Azerbaijan for 2019-2023 are as follows: “To ensure the sustainable and balanced development of the regions in the Republic of Azerbaijan, as well as to create a competitive economy based on the principles of sustainable development, social welfare that meets high standards, efficient use of natural resources, and a favorable environmental protection system.”⁸

Therefore, there is a need to clearly define the determinants of regional socio-economic development, as well as to create and apply more effective mechanisms that can ensure the balanced development of regions in the country on the basis of successful international experience.

⁶ <http://www.e-qanun.az/framework/41320>

⁷ Ibid

⁸ State Program on Socio-Economic Development of the Regions of the Republic of Azerbaijan for 2019-2023, <http://www.e-qanun.az/framework/41320>

3. Ways and mechanisms to ensure balanced socio-economic development of the regions

Development is a change related to the transition from a (old) quality condition (state) of public life to another (new) quality condition (state) of public life. That is, although there may be setbacks in this process from time to time, in the long run, development is mainly forward-looking, in the direction of positive change. The history of human development confirms this. Development in society can take place through gradual and revolutionary changes.

Social development means increasing the level of welfare and prosperity of the population of the country (as well as regions, districts, villages, etc.). Economic development, on the other hand, reflects quantitative and qualitative progress (changes) in production and consumption across a country (as well as a region, district, or city). These are closely related.

Socio-economic development is the continuous growth and qualitative improvement of the economy of a country (region, district, city, etc.) and the level of welfare of the population living there in relation to each other over a period of time.

Regional socio-economic development is the process of integrated management of changes in the economy and social sphere of the relevant regions in order to improve the welfare and quality of life of the local population.

Although "regional development" is a broad concept, in the world practice and theoretical approaches, it is primarily seen as an effort to reduce inter-regional disparities.⁹ In modern development models, the formation of quality physical infrastructure is not enough to achieve this goal. Ensuring the competitiveness of the regions and ensuring equal access to services for all people living in the regions are important conditions for the development of a balanced region.

According to the approach of the Organization for Economic Co-operation and Development (OECD), although "regional development" is a broad term, it must first be seen as an effort to reduce inter-regional disparities. Until a few years ago, "regional development" meant the creation of large-scale infrastructure, mainly through large investments. However, the old approach failed to address regional inequalities, failing to achieve targeted development in economically backward regions, although large sums of money were spent for this purpose through public funds.¹⁰

OECD experts emphasize that regional development policy should have two goals, and the developed regional development strategies should be formed directly based on these goals:

- 1) Ensuring the competitiveness of regions that play the role of geographical space for economic development;

⁹ http://edf.az/uploads/documents/regional_inkishaf.pdf

¹⁰ <http://www.oecd.org/gov/regional-policy/regionaldevelopment.htm>

- 2) Ensuring equal access of the population to basic goods and services in all regions, as well as in different areas within the regions.¹¹

According to the approach of OECD experts, in order for all regions to be able to fully contribute to the national economy, it is important to ensure the competitive advantage of the regions. Azerbaijan's regional development program for 2014-2018 emphasizes the importance of producing competitive products in the regions but does not aim to apply the necessary mechanisms to ensure the competitiveness of the region's economy as a whole, as a geographically populated area.

In international practice, a development strategy is usually developed at the national level, which defines the framework of the government's regional development policy. Based on this strategy, regional economic development plans are developed for each economic region, taking into account their specific geographical and economic development characteristics and potential. Turkey and Georgia benefit from this experience.

Management of socio-economic development of the region is a special activity of the government aimed at ensuring (regulating) the development of individual territories (regions) of the country. The purpose of such activities is to increase the social welfare of the population living there through the efficient use of all resources of the area. This can be achieved through the establishment of coordinated mechanisms for the management of all economic and social processes in the region. As there are no regional governments in Azerbaijan, the socio-economic development of all regions and administrative districts is managed directly by the central government. In Azerbaijan, this area is directly under the authority of the Ministry of Economic Development. In a number of countries, there are separate bodies responsible for regional development. For example, in Turkey, the Ministry of Economy is in charge of general economic development.¹² The development of the regions is under the direct authority of the Ministry of Development.¹³

Along with the central government, the following can be attributed to the institutions involved in the management of the socio-economic development of the regions in our country and the impact on this development at one level or another: parliament; specialized central government agencies responsible for regional development (e.g., Ministry of Regional Development, Infrastructure Development Agency, Rural Development Agency, etc.); regional and district (city) departments of central executive bodies; international organizations (through specific projects); district and city executive powers; municipalities; communities and local civil society. Each of these institutions has a more or less unique role in managing the socio-economic development of the regions. In these processes, it is necessary to effectively coordinate the activities of all agencies. However, in successful international practice, the issues of socio-economic development of the regions are mainly in the authority and responsibility of regional and local government bodies, i.e. regional and local level municipalities.

In Azerbaijan, despite the fact that it was envisaged in the Development Concept "Azerbaijan 2020: Look into the Future", no legal steps have been taken in the last 4 years to increase the role of municipalities in regional development, to increase the role of these bodies in decision-making. But the

¹¹ Governing Regional Development Policy. OECD 2009.

¹² <http://www.ekonomi.gov.tr>

¹³ <http://www.kalkinma.gov.tr/Pages/index.aspx#>

problem is not limited to the limited powers of local self-government. The financial potential of municipalities is also very limited.

The following types of policies pursued by the government in relation to the socio-economic development of the regions are distinguished:

- ***The policy of equalization of regional development*** (or elimination of disproportions in the development of regions) - the programs of socio-economic development of the regions implemented in our country and listed above are such programs;
- ***The policy of "focused development"*** (or the policy of creating "locomotives of growth" or "reference regions") - in fact, although it is unofficial, the country has recently implemented such a policy in relation to several regions. Such that in each region, more attention was paid to the development of one administrative district. For example, Gabala and Khashmaz regions are especially burdened in terms of tourism development. In recent years, steps have been taken to turn different districts into industrial centers by establishing industrial districts in these regions. For example, the establishment of industrial districts in Masalli, Sabirabad, and Neftchala;
- ***Synergy policy*** - such a policy is aimed at ensuring synchronization in the development of regions;
- ***Differentiated policy*** - such a policy involves the creation of special economic zones or clusters in different regions.

In order to eliminate inequalities in the socio-economic development of the regions and ensure balanced development, it is necessary to create more effective mechanisms that will accelerate economic development by changing the existing management mechanisms. One of such effective mechanisms in world practice is the creation of regional clusters.

According to M. Porter, a well-known economist, "Clusters are geographically close groups of interconnected companies and associated institutions in a particular field, linked by common technologies and skills. They normally exist within a geographic area where ease of communication, logistics and personal interaction is possible. Clusters are normally concentrated in regions and sometimes in a single town."¹⁴ The main difference between the cluster approach and traditional sector development is that firms that complement and support each other, rather than duplicating each other, operate within certain geographical boundaries. One of these firms is linked to another by a value chain, the service and production sectors operate under the same umbrella, and all the stages required to obtain the final product take place in one place.

Clustering can be organized by both sectors and geographical areas. In practice, mixed models are also possible. The organization of sectoral clusters, which are considered specific for each area, taking into account the characteristics of specific geographical areas, is widespread in practice. In short, a cluster is a geographical area where the activities of a group of enterprises specializing in a particular field of activity are established in a coordinated manner with other groups of enterprises and organizations

¹⁴ Competitive regional clusters. OECD Reviews of Regional Innovation.
http://artnet.unescap.org/tid/artnet/mtg/gmscb_regionalclusters.pdf

(research institutes, consulting organizations, civil society, universities, vocational education, vocational associations, etc.) in the value chain.

The main difference between regional and sectoral clusters is that sectoral clusters focus key actors around a sector to produce a specific product or service. In this case, the main goal is not to take advantage of the economic potential of the area where the sector is located, and geographical proximity is not considered an absolute criterion for the establishment of such clusters.

In the regional clusters, the geographical proximity of all actors involved in the production process, the selection of regional development as one of the main goals of clustering policy, the formation of a favorable environment for economic development in the region are at the forefront of policy.

Porter divided the regional clusters into 3 categories:

- 1) "Local industrial-based clusters". They mostly offer products and services within the region in which they operate and have limited competition with other regions in the struggle for markets. Such clusters typically specialize in the service sector.
- 2) "Source-dependent clusters". Such clusters are usually based on the natural resources (coal, oil and gas, forest resources, precious metals, etc.) of the region in which they operate. Such clusters are forced to compete in both domestic and foreign markets to sell their products.
- 3) "Net trade-oriented clusters". These clusters are formed by targeting proximity to both resources and markets and also engaged in the production of all kinds of products and services. Porter presents this model as the most competitive clustering model.

The application of the cluster approach in the management of economic processes has become one of the main tools of territorial development in the experience of various countries in recent decades. Especially in developed countries, clusters are one of the most common forms of business organization. The main argument of field researchers regarding the superiority of the cluster mechanism is that the creation of a competitive environment in an arbitrary area is possible due to the presence of both entities supporting each other and entities competing with each other within similar sectors of the economy.

When analyzing the current situation and good international practices, it is clear that the development of mechanisms for the development of regional clusters is extremely important for Azerbaijan. Special attention has been paid to the importance of the formation of clusters in strategic roadmaps on the economic development recently approved by the government. However, the study of experience shows that special attention was paid to the role of territorial clusters in regional economic development and the study of the necessary conditions for their formation. The assessment shows that the formation of the necessary legal and regulatory framework for cluster development, the creation of reliable mechanisms for assessing the competitiveness of the economy, and the development of a country model for cluster development are very important.

Results and recommendations

The study leads to the conclusion that despite the implementation of three state programs for socio-economic development of the regions in Azerbaijan since 2004, as well as the expiration of the implementation period of the Development Concept “Azerbaijan 2020: Look into the Future”, there are still serious problems in bridging the gap between the socio-economic development of the regions in the country. Summarizing the analysis of the study, it can be said that there are sharp differences in all parameters of socio-economic development of the country, both between the Baku-Absheron zone and other regions of the country and between the rest of the regions of the country themselves except Baku-Absheron. Such that in 2019, 75.8% of the country's gross output, 62.2% of the total annual income of the population in the country, 89.6% of the total industrial production in the country, 85% of the total credit investment in the country's economy, 72.4% of investments in fixed assets were concentrated in the Baku-Absheron zone, which geographically covers only 7% of the country's territory and 30% of the population. During 2010-2019, 67.5% of the capital investment of 154.0 billion AZN implemented in the country was realized in Baku. For comparison, it is enough to note that in 2019, 12.7% of the total income of the population fell to the Aran economic region, 8.2% to the Ganja-Gazakh economic region, 4.5% to the Lankaran economic region, 3.3% to the Shaki-Zagatala economic region, 3.3% to the Guba-Khachmaz economic region, 1.7% to the Mountainous Shirvan economic region, and 3.3% to the Nakhchivan AR.

This situation is a factor leading to increasing poverty and unemployment in the country's regions, deepening social stratification, intensification of migration processes among the population, and accelerating the flow of population to the Baku-Absheron zone. If the process of development of industrial production and other sectors of the economy in the regions is not given due attention, poverty in the country's regions will increase rapidly, social stratification will deepen, which may have very serious socio-economic consequences.

Therefore, we consider it expedient to implement measures in the following directions, both in the field of management and regulation of regional development and in the field of mechanisms for stimulating the economic development of the regions in order to reduce inequality in the socio-economic development of the country and ensure more efficient and balanced development:

1. ***It is important to improve the institutional capacity of regional development in Azerbaijan.*** For this, it is necessary to create a separate central government body responsible for regional development. It can also be in the form of a separate ministry or agency under the president;
2. ***The development and implementation of special programs for the development of economically problematic regions and areas with unfavorable geographical conditions should be considered a priority.*** Regional development programs may offer differential incentives, tax and investment policies in relation to these regions;
3. ***It is expedient to develop a special development program for each economic region in Azerbaijan.*** Separately developed local development programs can offer appropriate solutions by in-depth analysis of the specifics, opportunities, and challenges of each region;
4. ***It is important to strengthen the administrative and financial capacity of municipalities to increase their participation in solving regional socio-economic problems.*** In particular,

municipalities should be given exclusive powers in the construction and maintenance of road and drinking water infrastructure in rural areas, cleaning and landscaping of areas, implementation of greening measures, and organization of irrigation systems of local importance, the implementation of these powers should be provided with the necessary funding;

5. ***In regional economic development, the cluster approach should be introduced and appropriate strategies should be developed.*** This strategy can be a crucial tool in coordinating the sectoral and regional development policies of the economy and clearly defining the medium and long-term goals and priorities of regional development;
6. ***The cluster potential of the regions should be analyzed on the basis of quantitative and qualitative methods that allow assessing the competitiveness of the regions.*** On the other hand, such assessments should be openly discussed with all stakeholders, civil society, and the results should be fully publicized;
7. ***Special requirements must be set for the creation of clusters.*** For example, a minimum requirement may be set for the number of participants in a cluster and the level of representation of SMEs there, and a mandatory requirement may be set to have at least one university or research institute among the founders.

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