CENTRAL BANK
OF THE REPUBLIC OF AZERBAIJAN

MONETARY POLICY REVIEW

AUGUST 2026

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ACRONYMS

AEs	Advanced economies
APPI	Agricultural Producer Price Index
BCI	Business Confidence Index
CBA	Central Bank of the Republic of Azerbaijan
CCI	Consumer Confidence Index
CPI	Consumer Price Index
EME	Emerging Market Economies
FAO	Food and Agriculture Organization of the United Nations
FDI	Foreign direct investment
FED	Federal Reserve System
FX	Foreign exchange
GDP	Gross Domestic Product
ILO	International Labor Organization
IMF	International Monetary Fund
IPPI	Industrial Producer Price Index
NDA	Net Domestic Assets
NFA	Net Foreign Assets
NEER	Nominal Effective Exchange Rate
OECD	Organization for Economic Co-operation and Development
OPEC	Organization of the Petroleum Exporting Countries
PMI	Purchasing Managers' Index
REER	Real Effective Exchange Rate
RSM	Real Sector Monitoring
SCC	State Customs Committee
SSC	State Statistics Committee
WTO	World Trade Organization
Y.o.y.	Year-over-year

EXECUTIVE SUMMARY

The Central Bank concentrated its efforts on its primary mandate – price stability in accordance with the 'Statement of the Central Bank of the Republic of Azerbaijan on main directions of monetary policy for 2026' in the first half of 2026.

During the reporting period, Azerbaijan's external sector indicators remained favorable on the backdrop of a complex global economic environment and its strategic foreign exchange reserves continued to exceed internationally accepted adequacy norms. Supply exceeded demand considerably in both cash and non-cash segments of the FX market.

In June 2026 annual inflation stood at 5.8%. Under the July baseline scenario annual inflation is expected to shift to the target starting from the second half of 2027.

The Central Bank's monetary policy decisions were guided by macroeconomic forecasts and shifts in the balance of risks stemming from demand and supply-side factors of inflation. Monetary policy tools were implemented by considering interbank money market developments and liquidity position of the banking system. Banking system liquidity elevated over the reporting period. Both secured and unsecured segments of the interbank money market remained active.

RECENT MONETARY POLICY DECISIONS

Date	Floor of the interest rate corridor	Refinancing rate	Ceiling of the interest rate corridor
22 January, 2025	*6.25%*	**7.25%**	*8.25%*
12 March, 2025	*6.25%*	**7.25%**	*8.25%*
23 April, 2025	*6.25%*	**7.25%**	*8.25%*
11 June, 2025	*6.25%*	**7.25%**	*8.25%*
23 July, 2025	*6.25% → 6.00%*	**7.25% → 7.00%**	*8.25% → 8.00%*
10 September, 2025	*6.00%*	**7.00%**	*8.00%*
22 October, 2025	*6.00%*	**7.00%**	*8.00%*
10 December, 2025	*6.00% → 5.75%*	**7.00% → 6.75%**	*8.00% → 7.75%*
4 February, 2026	*5.75% → 5.50%*	**6.75% → 6.50%**	*7.75% → 7.50%*
2 April, 2026	*5.50%*	**6.50%**	*7.50%*
6 May, 2026	*5.50%*	**6.50%**	*7.50%*
24 June, 2026	*5.50%*	**6.50%**	*7.50%*
31 July, 2026	*5.50%*	**6.50%**	*7.50%*

1

GLOBAL ECONOMIC TRENDS

1.1 GLOBAL ECONOMIC ACTIVITY AND INFLATION

Despite uncertainties and geopolitical shocks, global economy continued to grow in the first half of 2026. However, the intensification of the conflict in the Middle East and trade barriers drove down global growth. Against this backdrop, inflationary pressures increased, while economic activity showed signs of weakening.

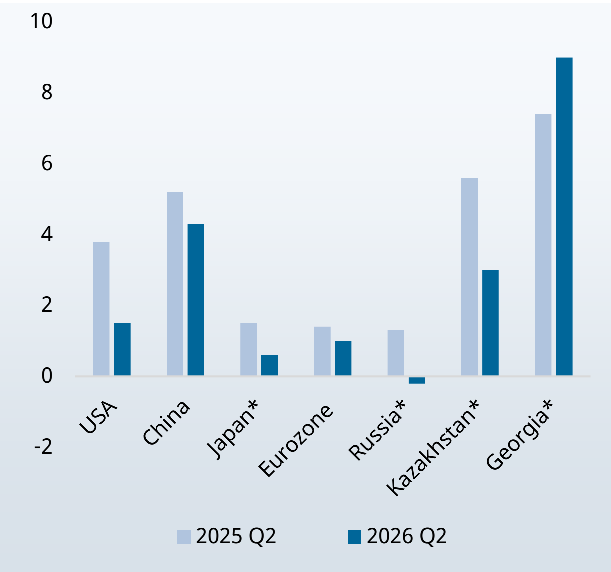
1.1.1 Global economic activity indicators

Whereas global economic activity continued in H1 2026, indicators varied across countries.

GDP increased by 1.5% annually in the United States in Q2 2026. Recovery in government spending, capital investments in AI-related sectors and growth in export and consumer spending supported economic growth.

Chart 1. Economic growth by countries, %

Source: National Statistics Offices



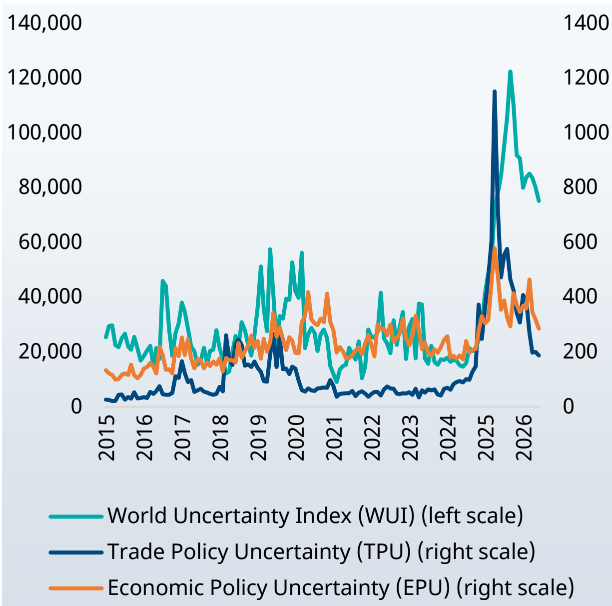
* Indicators cover Q1.

Economic growth in the euro area was 1% in Q2 2026, exceeding market expectations significantly. AI-related strong investments, sustained government spending and a number of temporary factors helped neutralize the adverse effects of the conflict in the Middle East and high energy prices.

The Chinese economy grew by 4.3% y.o.y. in Q2 2026, lower than expectations. Weak domestic demand, subdued private investment, and the prolonged property sector crisis outweighed the positive contribution from sustained growth in AI-related exports. However, foreign trade accelerated significantly. The oil price shock and a more challenging global economic environment could place additional pressure on growth in the periods ahead.

Chart 2. Global uncertainty indices[1]

Source: IMF



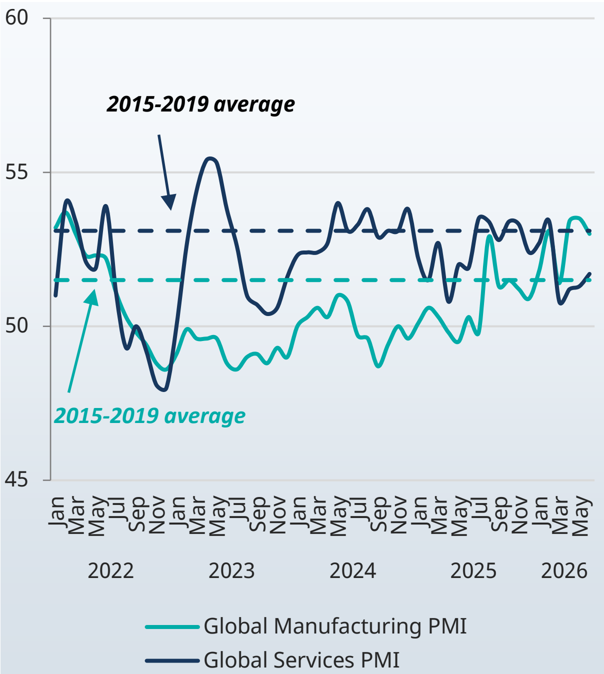
Against this backdrop, the level of uncertainty is lower than the peaks of 2025. However, it remains elevated by historical standards. The World Uncertainty Index (WUI) declined both from the levels of the

[1] Uncertainty indices are based on news and media sources and measure the attention of the media to news related to global uncertainty (WUI), economic policy uncertainty (EPU), and trade policy uncertainty (TPU).

last two months of the previous quarter and from the corresponding period in 2025. The Trade Policy Uncertainty Index (TPU) continued its downward trend following the sharp increase in January. Geopolitical developments in the Middle East continue to pose risks to the persistence of elevated uncertainty in the periods ahead.

The Global Purchasing Managers' Index (PMI) edged up (0.2) in June from the previous month to 52.0, the highest level in the past four months. Remaining above the neutral threshold (50.0) the index indicated a continued expansion in economic activity.

Chart 3. Purchasing Managers' Index (for manufacturing and service sectors)
Source: S&P Global



The manufacturing PMI stood at a higher level in Q2 2026 year-over-year. Following a decline in Q1 amid the effects of the US–Iran conflict begun in March, the index returned to its pre-conflict level in June.

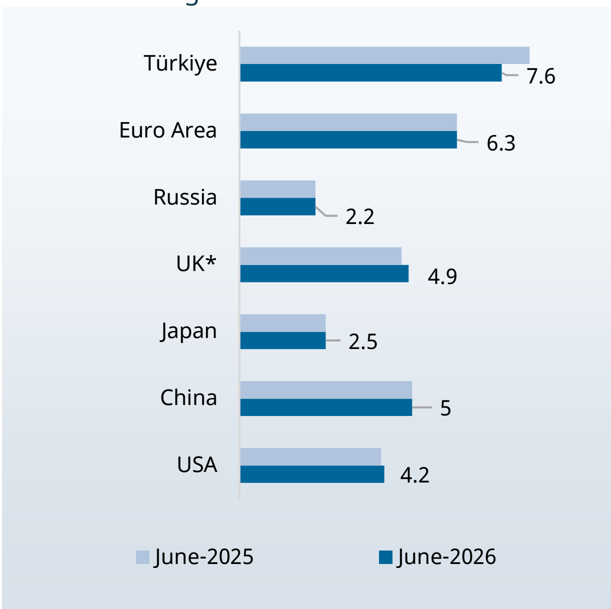
The services PMI stood at 51.7 in June 2026.

India, Ireland, and China recorded the highest, while France, Canada, and Russia the lowest PMI levels.

1.1.2 Global unemployment

Unemployment rates have diverged across countries in the reporting period. In H1 2026, rates declined in Türkiye, remained unchanged in China, the euro area, Russia, and Japan, while edged up slightly in the United Kingdom and the United States year-over-year.

Chart 4. Unemployment rate, %
Source: Trading Economics



* Indicators cover May.

According to the OECD's June 2026 Economic Outlook report, labor market conditions remained broadly unchanged compared to the previous period. Labor markets remained generally stable across most OECD economies. However, the slowdown in global trade, continued uncertainty over trade policy, and geopolitical tensions in the Middle East are emerging as key sources of additional risks to labor markets, potentially constraining job creation, which contribute to a gradual weakening of the labor market condition.

1.1.3 Global inflation

Although global inflationary pressures generally moderated in H1 2026, they varied across countries. The escalation of geopolitical tensions in the Middle East led to increases in energy and commodity prices. However, the subsequent easing of tensions toward mid-year helped alleviate price pressures.

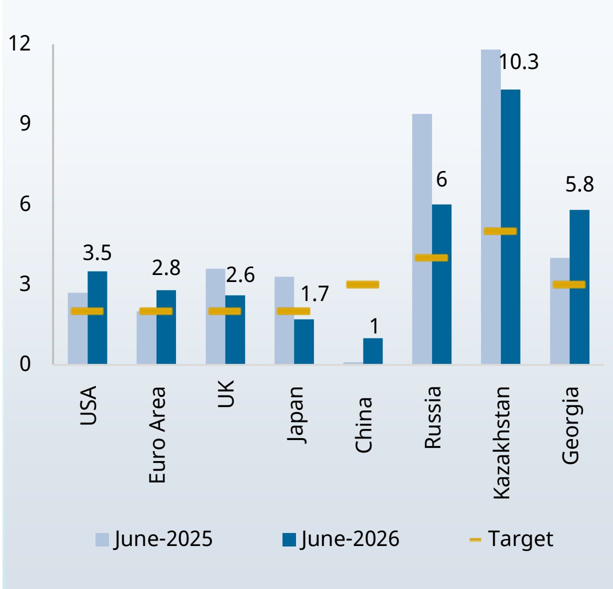
In the United States, annual inflation declined from 4.2% in May to 3.5% in June 2026, the first decline during the year. In the euro area, annual inflation stood at 2.8% in June, 0.4 pp lower than the 3.2% in May. Despite the decline in inflation, headline inflation remained above the ECB's inflation target. Core inflation, which excludes energy and food prices, declined from 2.6% to 2.4 %.

Inflation in China remained subdued, declining to 1.0% in June, driven by three consecutive months of lower food prices and a slowdown in the growth of transportation costs following the government's reduction in fuel prices. Core inflation declined from 1.2% in May to 1.0% in June, attributable to the fact that domestic demand remained weak and the pass-through of higher global commodity prices to domestic prices remained limited.

In Japan, annual inflation rose to 1.7% in June 2026 from the previous month, driven by a moderation in the decline in electricity and gas prices following the expiration of government subsidies, as well as accelerated price growth for transportation, household goods, clothing, and recreational services.

In Russia, annual inflation increased by 0.7 pp to 6.0% in June 2026 from the previous month, driven by a surge in fuel prices and continued strong price growth in the services sector. Amid supply shortages in the fuel market, petrol prices increased by 19.9% y.o.y., while services inflation stood at 10.6%. Food inflation remained relatively subdued at 3.4%.

Chart 5. Annual inflation, %
Source: National Statistics Offices



In Türkiye, inflation continues to decrease. Annual inflation declined to 32.1% in June 2026, driven by slower price growth in housing, transportation, education, and household goods. By contrast, inflation for food and non-alcoholic beverages, as well as restaurant and accommodation services continued to increase.

In Kazakhstan, annual inflation declined slightly from 10.4% in May to 10.3% in June 2026, the lowest rate since April 2025, driven by slower food price growth. Meanwhile, inflation in paid services increased amid higher rental costs, while non-food inflation remained unchanged from the previous month.

In Georgia, annual inflation increased from 5.7% in May to 5.8% in June 2026, driven by higher inflation for food and non-alcoholic beverages, housing and utilities, and transportation. Meanwhile, price growth moderated for alcoholic beverages and tobacco, clothing and footwear, and healthcare.

1.2 GLOBAL COMMODITY PRICES

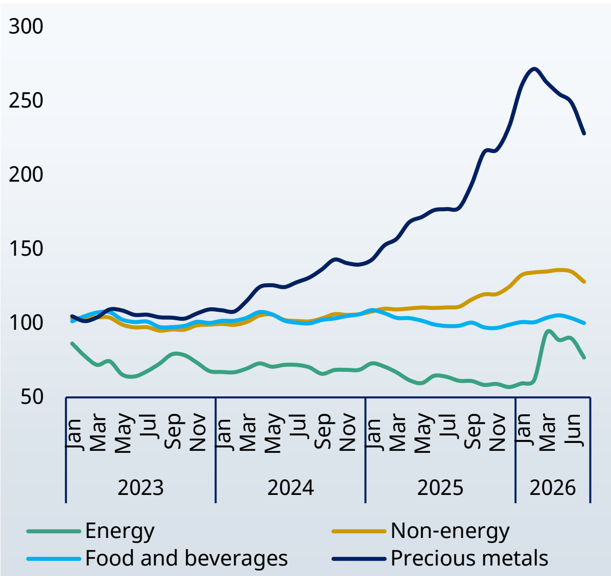
In the first half of 2026, commodity prices responded to the intensification of geopolitical conflicts. Energy prices increased sharply during the reporting period, with the effects passing through to other prices. While commodity prices remained elevated, a temporary ceasefire and the memorandum of understanding between Iran and the United States contributed to a partial reversal of the price increases from their peak levels in April 2026.

1.2.1 General trends of global commodity prices

According to the IMF, the global commodity price index increased by 14.1% in H1 2026, stemming from the surge in energy prices. Prices of several non-energy commodities also increased.

Chart 6. Dynamics of global commodity price indices (2022 December=100)

Source: IMF



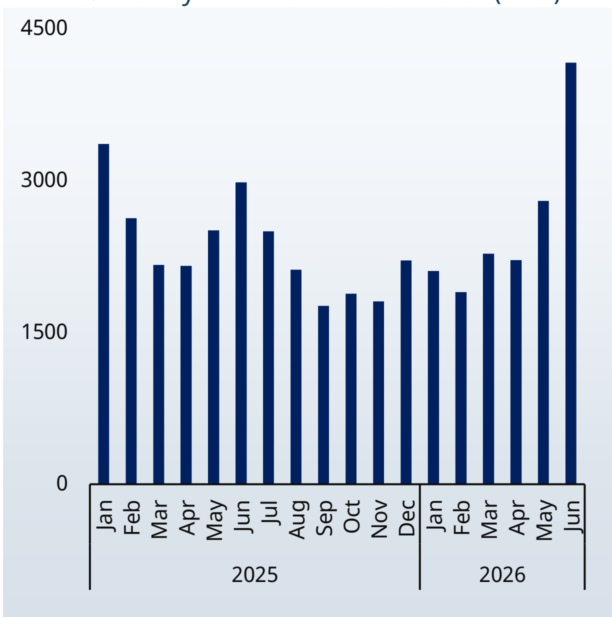
The increase in energy prices was primarily driven by supply shortages and supply chain disruptions amid heightened geopolitical tensions.

The IMF's non-energy price index increased by 2.8% in H1 2026, attributable to higher food and base metal prices. The IMF's base metals price index increased by 9.4% during the reporting period.

Higher transportation costs also contributed to upward pressure on prices in 2026. The cost of shipping a 40-foot container by sea increased by 88% by the end of June 2026 compared to the end of the previous year.

Chart 7. International transportation costs, US dollar/40ft

Source: Drewry World Container Index (WCI)[2]



The Middle East conflict remains a key source of risks to price volatility. A protracted conflict could further disrupt supply chains and adversely affect financial conditions.

1.2.2 Dynamics of global energy prices

Amid geopolitical conflicts, global energy prices remained elevated in H1 2026. According to the IMF, the energy price index increased by 7.2% in June from the end of the

[2] The World Container Index measures the average price of container shipments and indicates the overall level of trade costs by sea.

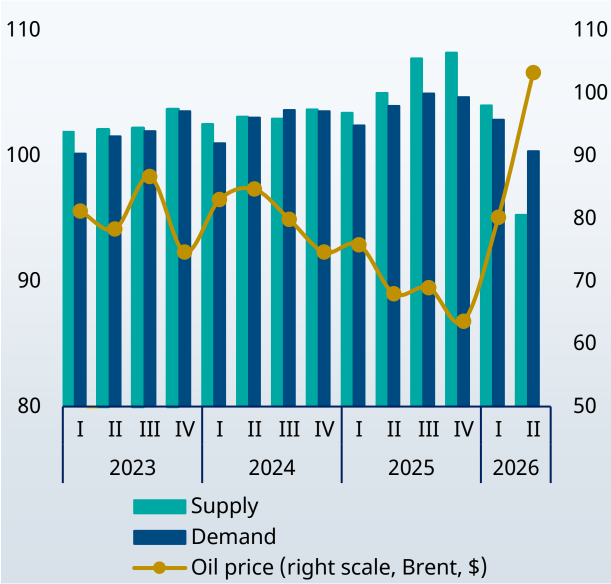
previous year. The average spot price of Brent crude oil stood at $85/barrel in June, $22/barrel higher than at early year.

The closure of the Strait of Hormuz, a strategic chokepoint for global oil transit, severely disrupted global oil flows and contributed to increased oil price volatility. On June 18, the United States and Iran signed a memorandum of understanding on a temporary ceasefire and the reopening of the Strait of Hormuz. Following the signing of the agreement, reports indicated a significant increase in tanker activity through the region for the transportation of crude oil and petroleum products. High oil flows through the Strait of Hormuz were a key factor driving oil prices lower in the final weeks of June.

The conflict in the Middle East rapidly altered market dynamics, forcing producers in the region to significantly reduce oil extraction. Consequently, average daily demand exceeded supply. With the restoration of oil flows, disruptions to crude oil production in the Middle East are expected to ease. Even if oil production and exports from the region increase in the coming months, it will take time to replenish significantly depleted global oil inventories and fully restore production capacity in the region.

Chart 8. Supply and demand in the world oil market, in million barrels (daily)

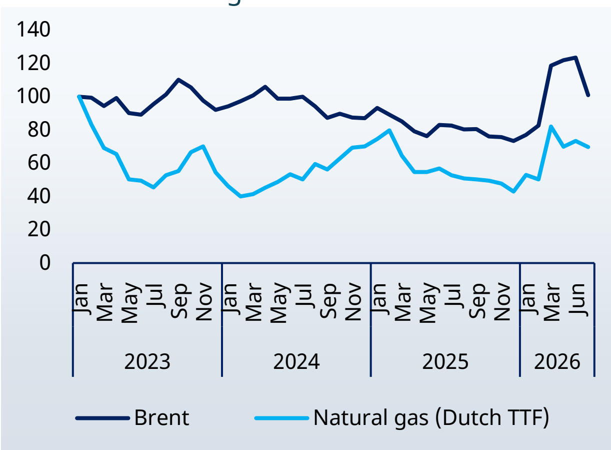
Source: The U.S. EIA



The crisis in the Middle East triggered a significant supply shock in global natural gas markets. The conflict placed pressure on the global gas balance, which had been gradually stabilizing, while damage to LNG export facilities in the region altered the medium-term outlook. Although LNG cargo flows through the Strait of Hormuz have increased since the temporary ceasefire agreement between the United States and Iran was reached in June, they remain well below pre-conflict levels. The timing of a full restoration of traffic through the Strait of Hormuz remains uncertain.

Chart 9. Monthly price index of Brent oil and natural gas (January 2023=100)

Source: Bloomberg



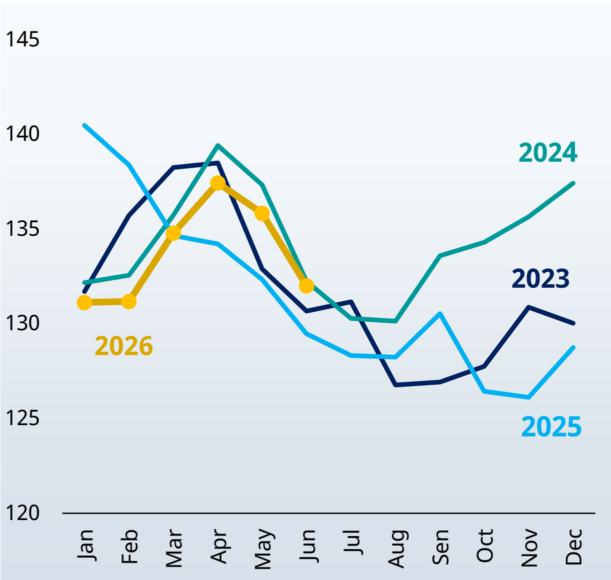
Spot prices in Asia and Europe responded immediately to supply disruption caused by the effective closure of the Strait of Hormuz. Prices reached their highest monthly levels in March since January 2023. Although prices declined somewhat in Q2 2026, they remained well above 2025 levels. Amid elevated spot prices, global gas demand declined in H1 2026, reflecting lower consumption in major LNG import markets.

1.2.3 Dynamics of global food prices

Global food prices generally rose in H1 2026. The agriculture price index released by the IMF[3] increased by 2.5% during the first six months of the year. Due to the increase in energy prices during the reporting period, manufacturing and transportation costs of food products increased, which had an upward impact on overall prices.

Chart 10. The Agriculture Price Index (2016=100)

Source: IMF



The FAO reports the Cereal Price Index rose by 2.8% in the first half of the year. Stronger demand for Indica rice in Asia, as well as weather-related concerns and elevated production, transportation, and marketing costs pushed up prices across rice varieties. The Vegetable Oil Price Index increased by 16.2%, largely owing to higher palm oil prices. By contrast, sunflower oil prices remained broadly stable in global markets.

The Meat Price Index increased by 5.0% over the six-month period, driven primarily by higher international poultry and ovine meat prices. Poultry and ovine meat prices rose amid stronger global demand and limited exportable supplies. The Dairy Price Index, meanwhile, declined by 8.4% in June compared with the end of the previous year. While prices declined across all dairy products, market conditions varied across products. Butter and cheese prices fell amid improved milk supplies in the European Union and the United States, as well as increased butter and cheese production. The Sugar Price Index declined by 1.1% in the first half of the year. In June, greater allocation of sugarcane to sugar production in Brazil contributed to lower international sugar prices. In addition, stronger exports, supported by the depreciation of the Brazilian real against the US dollar, exerted further downward pressure on prices.

Overall, the FAO Food Price Index was 4.7% higher in June than at the end of 2025.

[3] The agriculture price index summarizes the price indices of food, beverages, and agricultural raw materials.

1.3 GLOBAL FINANCIAL SYSTEM TRENDS

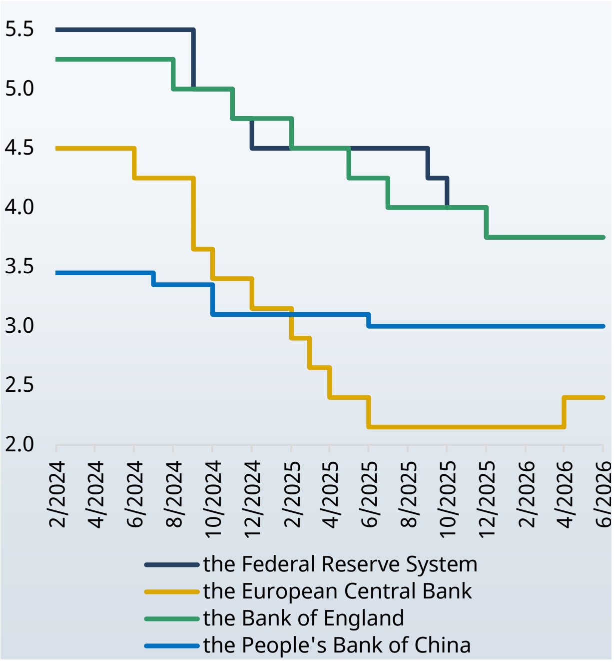
In the first half of 2026, heightened geopolitical tensions contributed to greater uncertainty and volatility in global financial markets. Rising inflationary pressures led to a pause in monetary policy easing, while some countries tightened policy. The global financial system remained resilient.

1.3.1 Monetary policy decisions of central banks

In H1 2026, geopolitical tensions and inflationary pressures amid the conflict in the Middle East forced most central banks to adopt a cautious stance, pausing monetary policy easing and keeping policy rates unchanged. However, some central banks tightened monetary policy to curb mounting inflationary pressures.

Chart 11. Key policy rates of major central banks

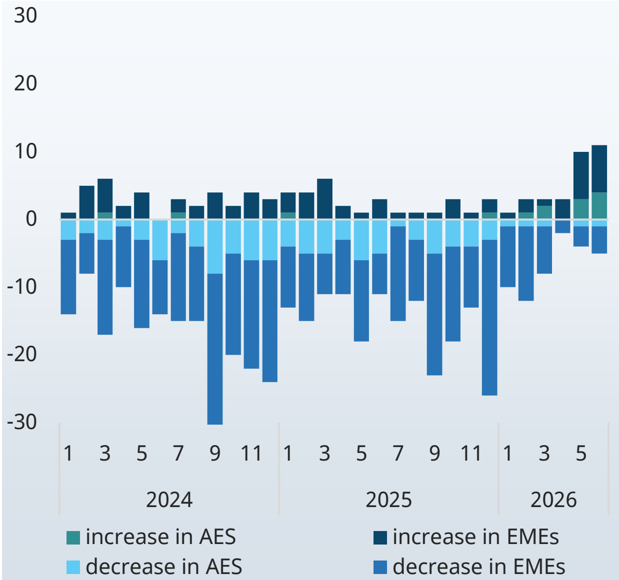
Source: tradingeconomics



Amid persistent inflation-related uncertainty and tensions in the Middle East, the central banks of major economies largely kept policy rates unchanged during the period, while some raised rates. The FED maintained the federal funds target range at 3.50–3.75%, while the Bank of England kept Bank Rate unchanged at 3.75%. The ECB, however, raised its policy rate from 2.15% to 2.40% amid a pickup in headline inflation and intensifying inflationary pressures.

Chart 12. Change in key policy rates across 83 central banks

Source: centralbanknews, cbrates



The People's Bank of China maintained the easy monetary policy stance, keeping its policy rate unchanged to support economic growth and alleviate deflationary pressures. The Bank of Japan raised its policy rate from 0.75% to 1% in response to the risk that elevated energy prices could pass through to other prices and cause inflation to move above target.

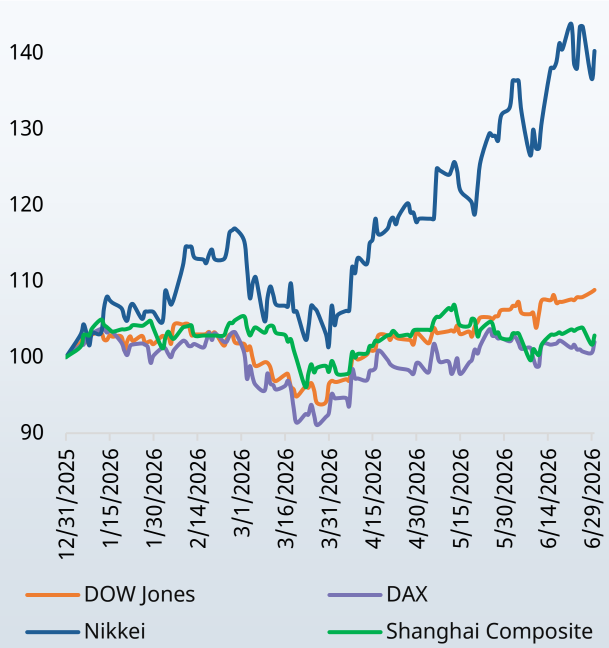
The Bank of Russia, meanwhile, cut its policy rate to 14.25% as the economy moved toward a more balanced growth trajectory and price pressures eased. Despite this modest easing, monetary conditions remained tight.

1.3.2 Financial market trends

In H1 2026, global financial markets underwent elevated volatility and uncertainty. Rising geopolitical tensions and surge in energy prices affected financial asset prices adversely in the first quarter. However, markets staged a partial recovery toward the end of the first half of the year.

Chart 13. Dynamics in stock exchanges (31 December 2025=100)

Source: Bloomberg

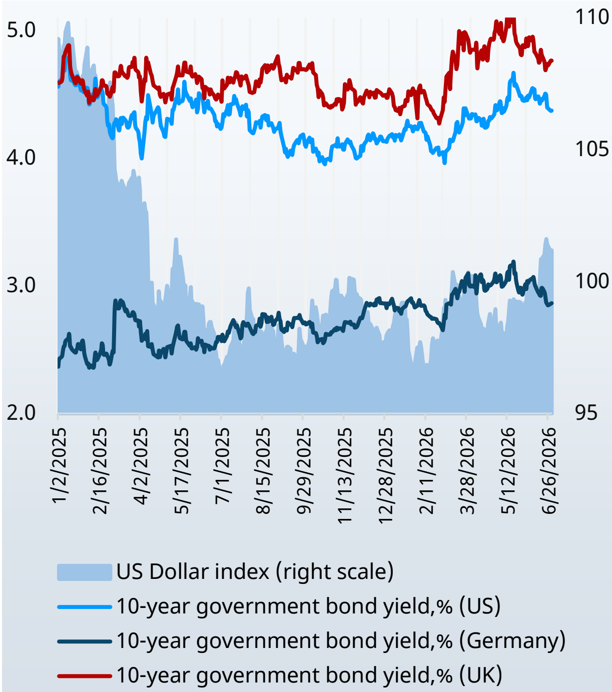


In H1 2026, the Dow Jones, FTSE Eurotop, and MSCI World indices rose by 9% each, while the DAX and Shanghai Composite gained 2% and 3%, respectively. The Nikkei recorded a notable 40% increase, supported by stronger semiconductor exports and corporate earnings amid robust global demand for AI, substantial dividend payouts, and progress in structural reforms. By contrast, the RTSI index lost 15%.

Although the U.S. dollar index declined somewhat at the beginning of the year, it increased toward the end of the period and fluctuated around the 100 level. This indicates that the U.S. dollar index strengthened to some extent compared with the first months of the year.

Chart 14. U.S. dollar index and 10-year government bond yields

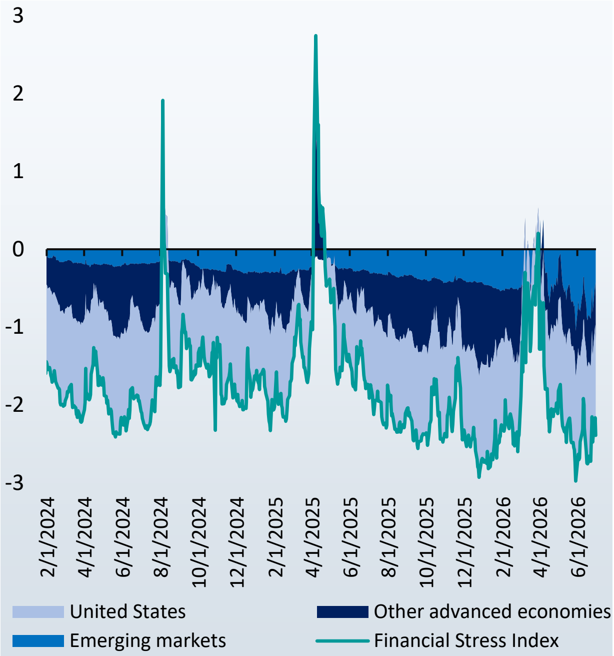
Source: investing.com



Amid heightened geopolitical tensions and intensifying inflationary pressures, 10-year government bond yields in the United States, Germany, and the United Kingdom rose in the first quarter, but subsequently declined toward the end of the first half of the year.

According to the U.S. Office of Financial Research, the Global Financial Stress Index fluctuated during the first half of 2026, rising in the first quarter before declining in the second quarter and returning to negative territory. This pattern indicates that financial stress intensified following a sharp escalation in geopolitical tensions but subsequently eased as global financial markets stabilized toward the end of the first half of the year.

Chart 15. Global Financial Stress Index[4]
Source: The U.S. Office of Financial Research



According to the IMF's WEO July 2026 Update, the global financial system remained resilient. High corporate earnings and a resilient global economy helped shield the financial system from the adverse effects of the Middle East conflict. Although crude oil prices eased somewhat toward the end of the first half of the year, higher energy prices are expected to intensify inflation risks. Accordingly, the expected trajectory of policy rates for 2026 was revised upward. In Asian net oil importer EMEs deteriorating terms of trade increased inflation and exchange rate pressures, while currency appreciation in energy-exporting economies outside the Middle East helped anchor inflation expectations.

[4] The Financial Stress Index (FSI) is a daily market-based indicator of stress in global financial markets, incorporating 33 financial market variables, such as income margins, valuation metrics, and interest rates. The FSI is positive when market stress levels are above average and negative when they are below average. The FSI reflects the contributions to financial stress from three regions: the United States, AEs, and EMEs.

2

DOMESTIC MACROECONOMIC DEVELPMENTS

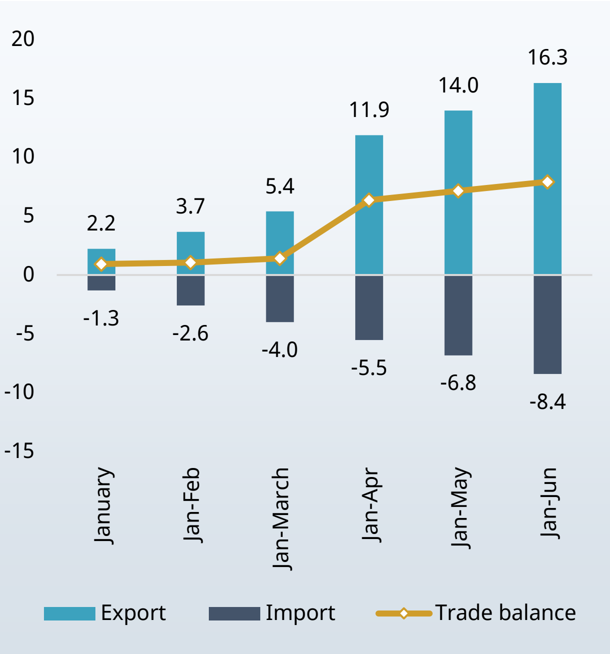
2.1 EXTERNAL SECTOR OF AZERBAIJAN

In the first half of 2026, the external trade balance, one of the key components of the balance of payments, recorded a surplus. Non-oil and gas exports increased year-over-year, while the economy remained attractive to foreign investment. Foreign exchange reserves continued to exceed the internationally accepted adequacy norms.

2.1.1 Foreign trade turnover

According to the SCC, the country's foreign trade turnover from January to June of 2026 amounted to $24.7B. Of this total, exports amounted to $16.3B (66.2%), while imports amounted to $8.4B (33.8%). Foreign trade surplus stood at $8B.

Chart 16. Foreign trade balance in H1 2026, in billion U.S. dollars
Source: SCC

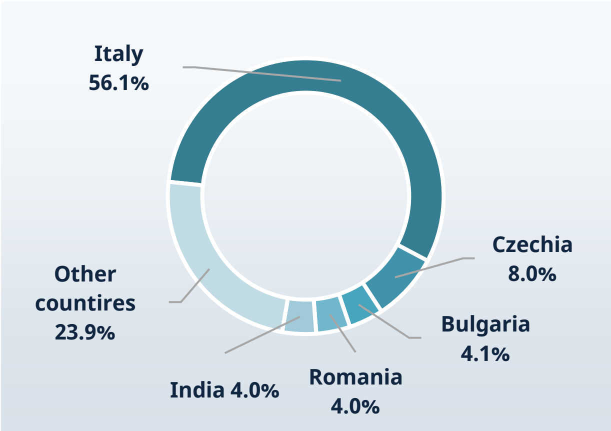


The EU accounted for 37.8%, the CIS for 11%, and other countries for 51.2% of total foreign trade turnover. Italy, Great Britain, Türkiye, China, Russia, Georgia, Germany, the Czech Republic, Bulgaria and Greece accounted for over half of trade turnover.

Main partners in export included Italy (33.7%), Great Britain (21.3%), Türkiye (10.3%), Russia (3.7%) and Georgia (3.1%). The share of other countries was 27.9%.

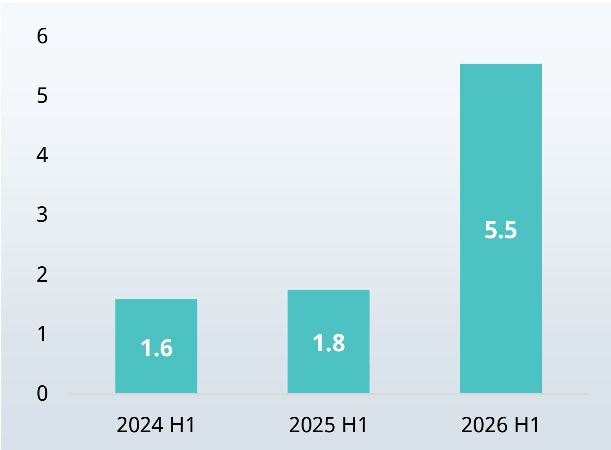
The total value of oil and gas exports amounted to $10.8B, comprising $6.7B from crude oil and other manufactured oil products, and $4.1B from natural gas.

Chart 17. Crude oil exports by country in H1 2026, in %
Source: SCC



Non-oil-gas exports increased by 3.2 times to $5.5B year-over-year.

Chart 18. Non-oil-gas exports, in billion U.S. dollars
Source: SCC



The main contributors to the growth of non-oil-gas exports were gold, sugar, cotton, oils, aluminum and related products, ferrous metals and related products, tea, fruit, vegetables and their processing products, alcoholic and non-alcoholic beverages.

The main non-oil and gas export destinations were Great Britain (62.6%), Russia (10.7%), Türkiye (6.3%), Georgia (5%) and Switzerland (3.9%). The share of other countries was 11.5%.

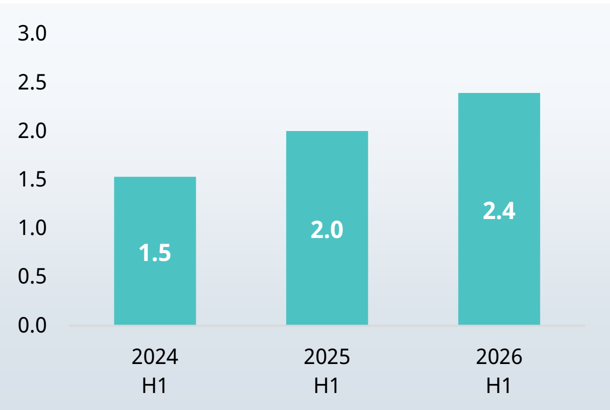
Commodity imports amounted to $8.4B – the public sector accounted for 7.7%, legal entities for 83.6%, and individuals for 8.7% of total commodity import. Imports of machinery and equipment (24.2%), food products (16.4%) and vehicles (13.4%) prevailed in total imports.

China accounted for 26%, Türkiye for 13.6%, Russia for 13.4%, the United States for 4.9%, Germany for 4.1%, Iran for 3.6%, Italy for 3.1%, Belarus for 2.5%, Japan for 1.8%, Great Britain for 1.8% and other countries for 25.2% of total imported products.

2.1.2 Foreign investments

FDI inflows continued during the period under review in 2026. According to the SSC, total investments from external financial sources y.o.y. increased by 18.2% to AZN2.4B (25.8% of total investments).

Chart 19. Investment in fixed capital from foreign sources, in billion U.S. dollars
Source: SSC



Investor funds from the UK, Türkiye, Russia, the UAE, the United States, Switzerland, Japan, Iran, Hungary, France and India accounted for 96.9% of total foreign investments. The continued inflow of foreign investment reflects the depth of the country's integration into the global economy and the sustained interest of global investors in the country.

2.1.3 Tourism services

The conflict in the Middle East also affected tourist flows. During January–June 2026, 1.1 million visitors from 189 countries traveled to Azerbaijan, y.o.y. down by 10.3%. Visitors from Russia accounted for 28.1%, Türkiye for 21%, Iran for 8.2%, Georgia for 4.9%, Kazakhstan for 4.6%, Uzbekistan for 3.2%, Pakistan for 2.9%, India for 2.8%, Israel for 2.6%, China for 2.4%, Saudi Arabia for 1.8%, Ukraine for 1.6%, Turkmenistan for 1.3%, Germany and Great Britain each for 1.1% and other countries for 12.4% of total arrivals.

Chart 20. Number of inbound and outbound tourists, in millions of people
Source: SSC

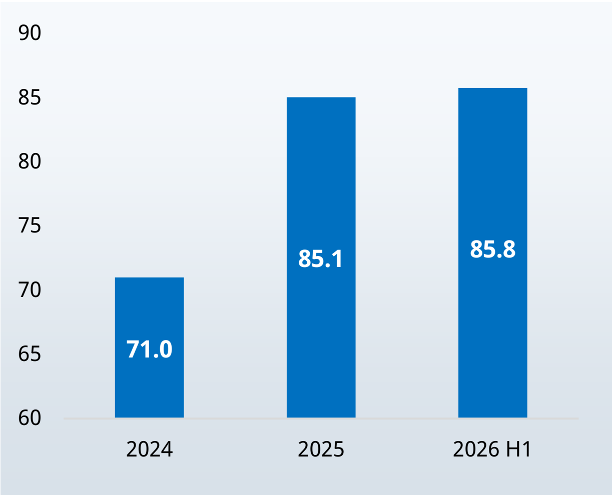
The number of residents travelling abroad for tourism purposes amounted to 0.9 million persons (y.o.y. down by 5.1%). Those travelling abroad for tourism visited Türkiye (41.5%), Russia (17.1%), Georgia (11.7%), Iran (6.2%), and other countries (23.5%).

2.1.4 Foreign exchange reserves

By the end of June 2026, strategic foreign exchange reserves increased by $703.2M (0.8%) compared to the beginning of the year to $85.8B. CBA's foreign exchange reserves increased by 14.3% or $1.6B to $13.2B by the end of June.

Chart 21. Strategic reserves, in billion U.S. dollars

Source: CBA



Strategic foreign exchange reserves continued to exceed international reserve adequacy benchmarks during the reporting period. As of the end of June 2026, strategic reserves were sufficient to cover 40 months import of goods and services (considering the import of goods and services for Q1 2026) and surpassed the broad money supply in manat (M2) by 3.4 times (based on the M2 money aggregate as of 1 July 2026).

These indicators demonstrate the country's resilience to external and internal economic shocks and confirm that debt risks remain at a fully manageable level.

2.2 AGGREGATE DEMAND

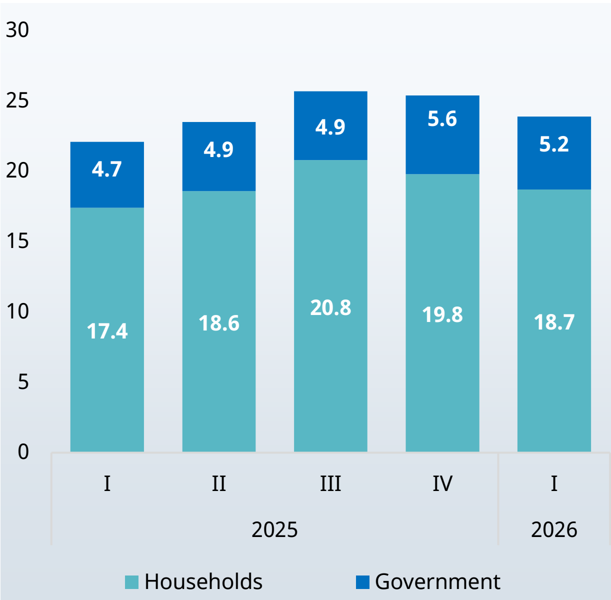
In the first half of 2026, growth in aggregate domestic demand supported economic growth. Rising household incomes contributed to stronger consumption demand, which in turn supported overall aggregate demand.

2.2.1 Final consumption expenditures

In H1 2026, growth in domestic consumption remained the main driver of aggregate demand.

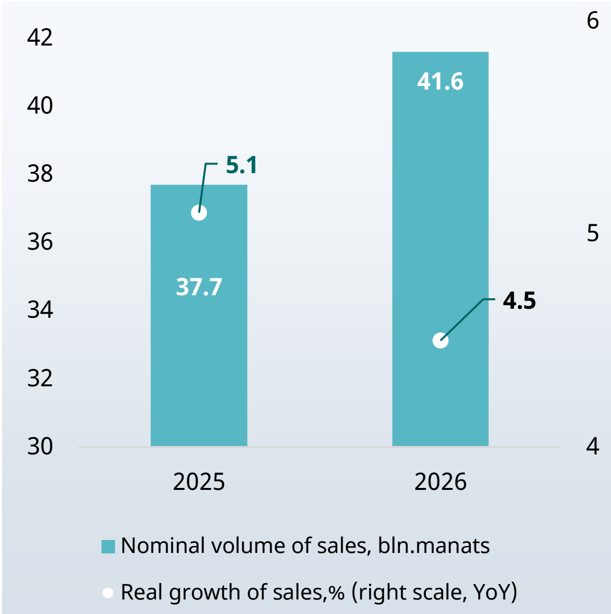
In Q1 2026, households' final consumption expenditures stood at 62.9% (y.o.y. up by 4.7 pp) of nominal GDP, while public institutions accounted for 15.7% (y.o.y. up by 1.7 pp). Households' final consumption expenditures increased by 7.4%, and those of public institutions increased by 10.3% in nominal terms.[5]

Chart 22. Consumption and its sources, in billion AZN
Source: SSC



In H1 2026, the value of goods sold and services provided to the population y.o.y. increased by 4.5% to AZN41.6B. In the consumer market, 77.8% of the total value was generated by retail trade turnover, 18.8% by paid services, and 3.4% by public catering turnover.

Chart 23. Dynamics of total value of goods sold in the consumer market, in billion AZN
Source: SSC



Retail trade turnover increased by 3.7% y.o.y. in real terms, including an increase of 1.5% for food, beverages, and tobacco products and 6.5% for non-food products. The average monthly retail trade turnover per capita amounted to AZN525.7, which was AZN42.9 higher than y.o.y.

The increase in public catering and paid services to the population indicates active consumer demand. Public catering turnover increased by 5.9% y.o.y. in real terms, while services provided to the population increased by 7.6%. During the period, residents of the country spent y.o.y. AZN89.8 more than the average monthly income on paid services.

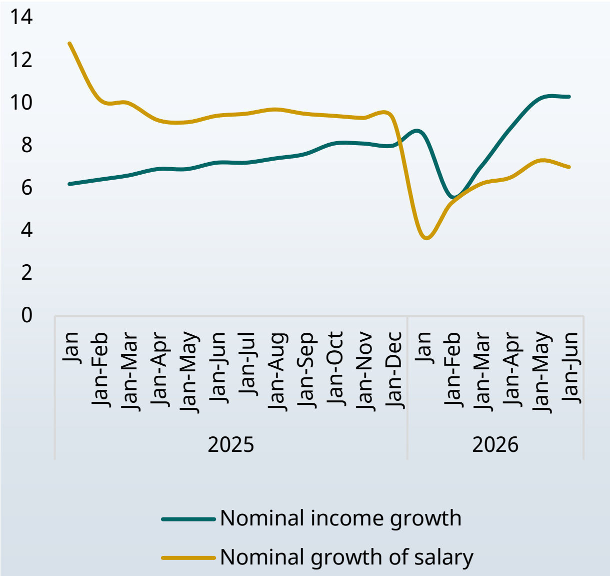
Consumer demand was driven by the growth of income of the population in nominal terms. According to the SSC, during the first six months of the year, nominal

[5] Source: The SSC's 'Use of GDP' table and CBA's calculations.

income of the population y.o.y. increased by 10.3% to AZN47.3B. Disposable income of the population increased by 10.5% to AZN41.8B. The average monthly nominal salary of hired labor increased by 7% to AZN1174.4 y.o.y.

Chart 24. Growth dynamics of nominal incomes and salaries of the population, year-over-year, %

Source: SSC



One of the main factors driving the increase in consumer demand was the growth of consumer loans. Consumer loans issued by banks increased by 11.7% y.o.y. in June[6].

Government spending was one of the funding sources of aggregate demand in the reporting period. Based on the latest available data, state budget expenditures reached AZN16.8B in January-June. Within this, current expenditure rose by 10.1% to AZN11.6B. Spending on social protection and social security increased by 12.1% y.o.y. to AZN8.8B[7].

2.2.2 Investment expenses

In H1 2026, total investment to the economy from all funding sources y.o.y. increased by 13.8% to AZN9.3B. AZN5.04B (54.2%) was directed to production. Investments in the oil and gas sector increased by 34.3%, while in the non-oil-and-gas sector increased by 5.5%. y.o.y. Of the investment in the non-oil and gas sectors amounted to AZN2.5B, AZN0.3B was utilized in the non-oil industrial sector.

41.8% of investments were made by public and 58.2% by non-public investors. Investments channeled into the economy from domestic sources accounted for 74.2% of total investments.

Industry (46%), transportation and warehouse (23.1%) and construction (20.9%) accounted for the main share in the structure of investments. Investments in industrial sector increased by 21% y.o.y. This growth was mainly driven by investment in the mining industry.

[6] Source: CBA
[7] Source: Ministry of Finance

2.3 AGGREGATE SUPPLY AND LABOR MARKET

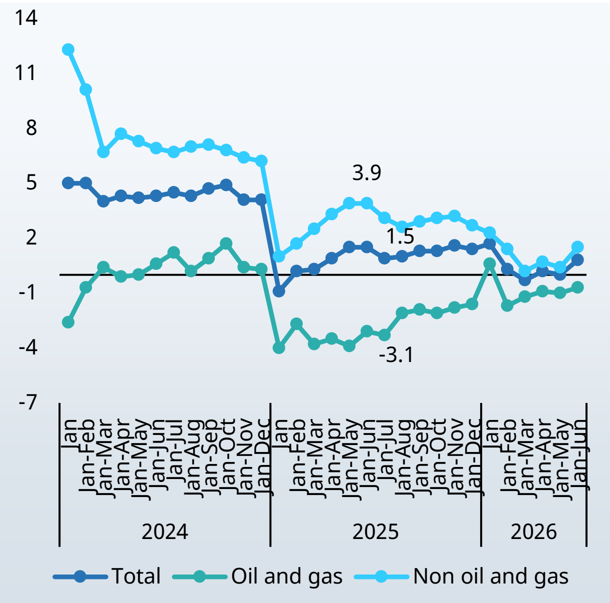
Economic growth continued in the first half of 2026, with the non-oil and gas sector remaining the main driver of growth. Labor market indicators also improved, with increases recorded in the economically active population and the number of hired employees

2.3.1 Economic growth

According to the SSC, in January-June 2026, GDP increased by 0.8% y.o.y. in real terms and amounted to AZN65.2B in nominal terms. Non-oil and gas GDP accounted for 69.9% in the nominal GDP structure.

Nominal oil and gas GDP decreased by 0.7% to AZN19.6B. Crude oil production y.o.y. decreased by 3.1%, while natural gas extraction increased by 1.1%.

Chart 25. Economic growth, year-over-year, %
Source: SSC



Non-oil and gas GDP y.o.y. increased by 1.5% in real terms to AZN45.6B. Production in the non-oil and gas industry increased by 4.1%.

Agricultural output increased by 2.2% in the reporting period. Livestock products increased by 2.5%, and plant products increased by 1.8%.

Growth continued in services sector. Transport and warehousing grew by 8%, freight and passenger transport increased by 2.5% and 8.3%, respectively. Freight transportation by road, with the largest share in cargo transportation, increased by 6.6% y.o.y. The value added in the information and communication sector grew by 7.5%, while tourism and public catering increased by 2.4% y.o.y.

CBA's RSM results are broadly consistent with official statistics. In H1 2026, the BCI demonstrated mixed dynamics across sectors. It was in positive territory in the industrial and services sectors.

Table 1. Dynamics of economic growth by sectors of the economy, year-over-year, %
Source: SSC

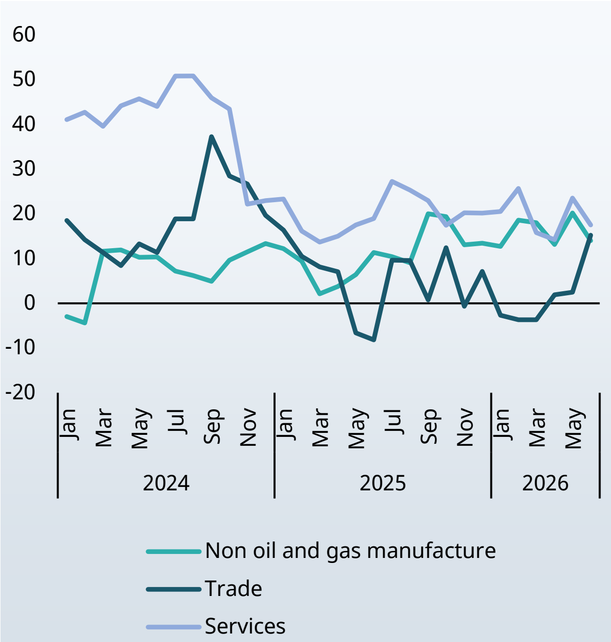
Sectors	Jan-June 2025	Jan-June 2026
Industry	-2.9	0.3
Construction	8.5	-13.0
Agriculture, forestry, and fishery	1.4	2.2
Trade, repair of vehicles	3.0	3.7
Transport and warehousing	2.7	8.0
Tourism and public catering	10.2	2.4
Information and communication	8.4	7.5
Other	2.0	0.9
Net taxes on products and import	3.7	0.5

The BCI for non-oil-and-gas industrial enterprises was higher, particularly in the chemical, food and beverages, machinery and equipment manufacturing subsectors. BCI in the trade sector was in negative territory for the automotive segment in June, while it remained in positive territory for household goods and electrical appliances.

The BCI was high and positively zoned in healthcare, hotel management, communication and transportation subsectors.

Chart 26. Business Confidence Index across sectors

Source: CBA calculations based on RSM results [8]



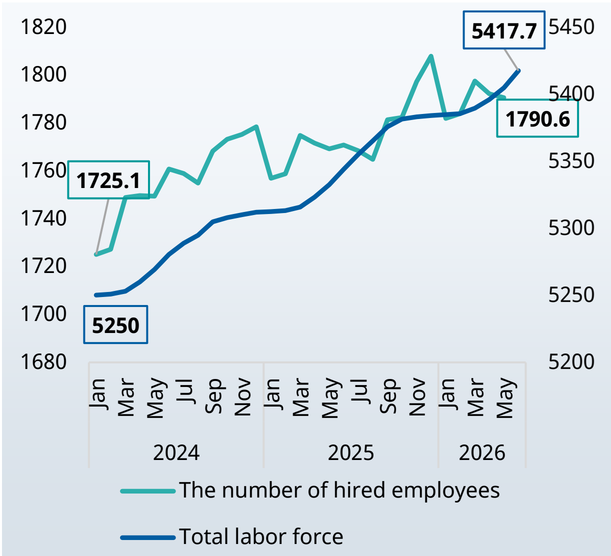
The increase in the number of commercial organizations engaged in the economy also confirms that economic growth continues at a moderate pace. According to the SSC, as of 1 July 2026, commercial organizations registered in the country numbered 215.4 thousand (y.o.y. up by 6.7%).

2.3.2 Employment

As of 1 July 2026, total labor force was 5417.7 thousand people (y.o.y. up by 1.4%), employed population numbered 5137.1 thousand people (y.o.y. up by 1.5%). As of June 1,2026, the number of hired employees was 1769.2 thousand persons (y.o.y. up by 1.2%) – 859.9 thousand persons were engaged in the public sector, while 930.7 thousand persons were employed in the non-public sector. The number of those employed in the non-public sector y.o.y. increased by 3.8%. The oil and gas sector employs 30.5 thousand people, while the non-oil and gas sector employs 1760.1 thousand people. In terms of structure, the largest share of wage earners falls in the sectors of trade and transport repair (18.6%) and education (18.1%). Other relatively large employment sectors were health and social services (8.6%), construction (6.6%), and public administration (6.1%).

Chart 27. Total labor force, in thousands of people

Source: SSC



As of 1 July 2026, the number of registered unemployed people increased by 3.6% from the early year to 248.5 thousand people.

According to the results of the survey conducted as part of RSM, employment expectations in June were particularly strong in non-oil-and-gas manufacturing subsectors, including the production of plastic products, metallurgy, and construction materials.

[8] Industrial BCI = (output – final goods inventory + production expectations)/3
Services BCI = (business condition + actual demand + demand expectation)/3
Trade BCI = (actual sale – changes in goods inventory + sale expectations)/3

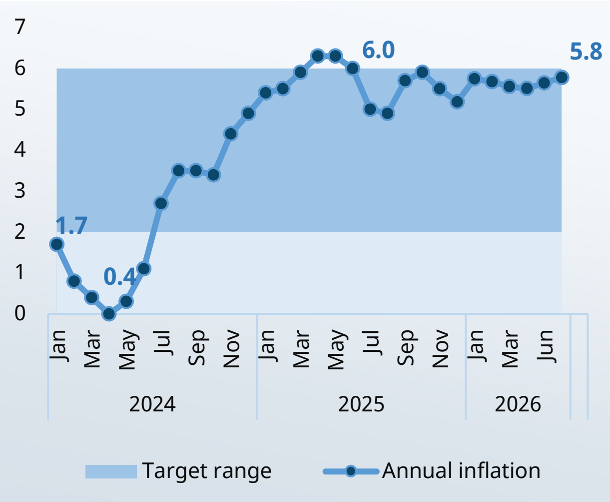
2.4 INFLATION

In the first half of 2026, annual inflation moved within the target range. Inflation was driven primarily by cost-side factors.

2.4.1 Consumer price index

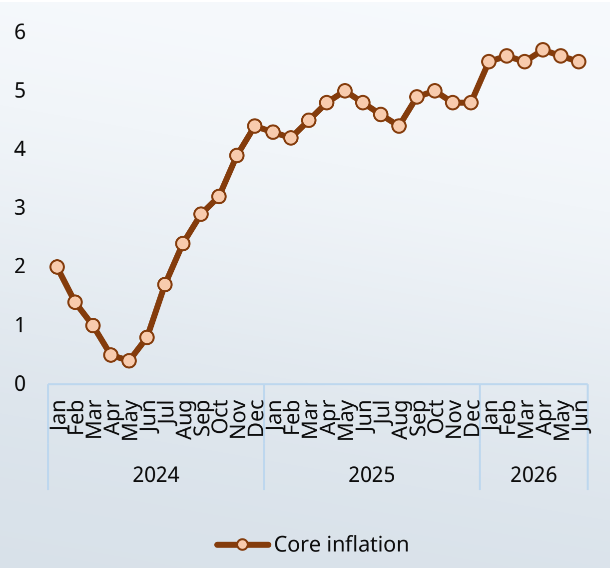
In June 2026, the CPI increased by annual 5.8% on total products and services.

Chart 28. Annual inflation, %
Source: SSC



Annual core inflation, calculated excluding changes in prices regulated by the state as well as prices of seasonal products and services, stood at annual 5.5% in June 2026.

Chart 29. Annual change in core inflation, %
Source: SSC

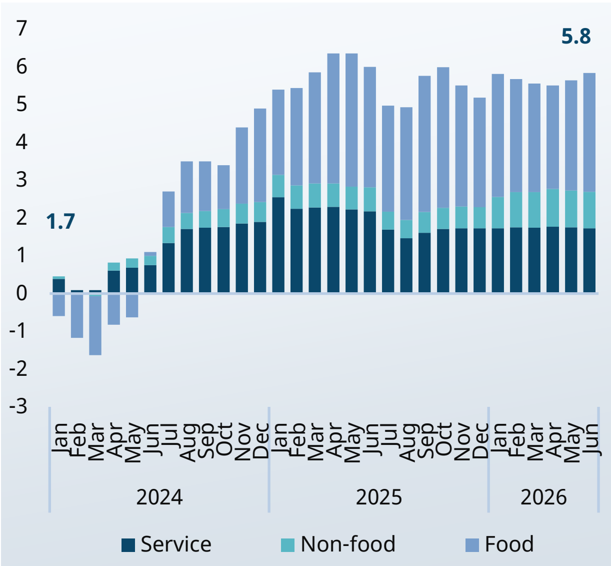


In June, annual inflation on food products, alcoholic beverages and tobacco products stood at 7.1%. The contribution of food prices to inflation increased to 3.1%. Food inflation was mainly driven by milk and dairy products and fruits, with annual price increases of 9.5% and 10.7%, respectively.

Annual non-food prices increased by 3.8%. The highest annual price hike among non-food products was in jewelry products (21.7%). The contribution of non-food products to inflation increased from 0.7 pp to 0.9 pp.

The service inflation stood at annual 5.6% in June 2026. Out of paid services to the population, the highest annual price hike was in housing and household services (6.8%), dental services (7.7%), passenger transport by air (12.8%), passenger transport by metro (20.0%) and central heating (50%). Contribution of services to annual inflation decreased from 2.2 pp to 1.7 pp y.o.y. in June.

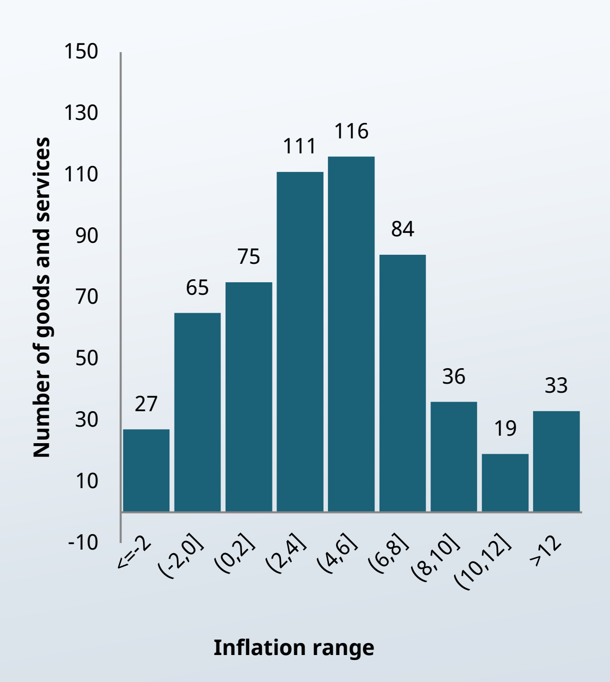
Chart 30. Contribution of CPI components, %
Source: Calculations of the SSC and the CBA



In June 2026, of the 566 goods and services included in the consumer basket, prices of 172 items increased more than 6% annually. For 64% of the items with rising prices, the increase remained below 6%. Prices declined by 16% of the goods and services in the basket.

Chart 31. Distribution of annual inflation across goods and services in the consumer basket

Source: Calculations of the SSC and the CBA



Overall, a number of developments in the global and domestic environment affected the formation of inflation. The CBA's assessments indicate that, government and household consumption together contributed 2.01 pp to annual inflation, while APPI contributed 1.60 pp, inflation in trading partners 2.84 pp, and NEER 0.02 pp. Other factors (inflation expectations and others) exerted a downward contribution of 0.67 pp.

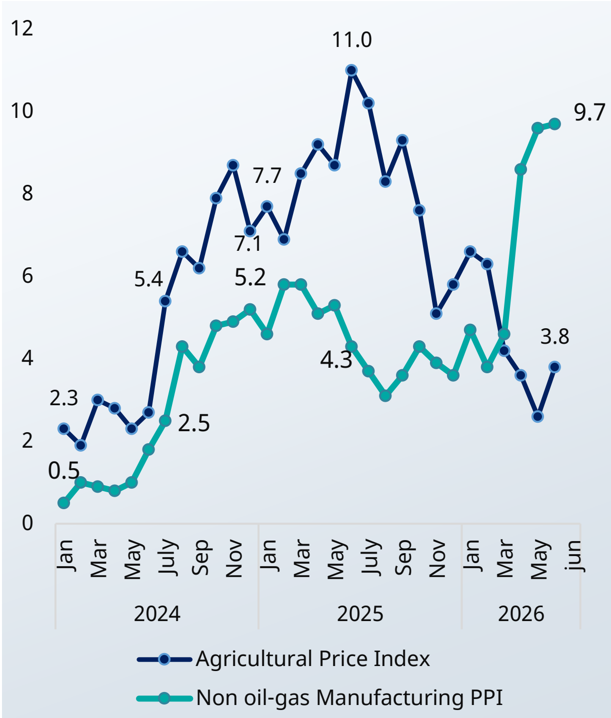
2.4.2 Producer Price Index

According to the SSC, in June the APPI y.o.y. increased by 3.8%, prices for plant growing products by 2.1%, and prices for livestock products by 5.3%.

In June 2026, the production PPI increased by 26.8% y.o.y. The PPI increased by 31.2% y.o.y. on the oil and gas products and 9.7% y.o.y. on non-oil and gas products. The PPI in processing increased by 15% y.o.y.

Chart 32. Annual change in PPI, %

Source: SSC

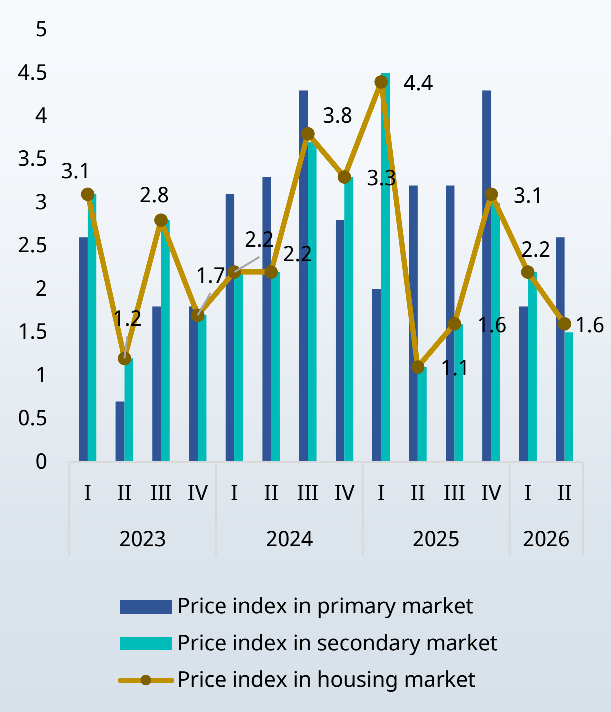


In June 2026, prices increased by 5.8% for transport and warehousing, by 3.9% for freight transportation services, by 2.1% for postal and courier services, by 2.1% for advertising services and decreased by 4.5% for software development-related services.

2.4.3 Housing Price Index

According to the SSC, in Q2 2026, the housing price index increased by 8.6% y.o.y. Prices in the primary housing market rose by 12.4% and in the secondary market by 8.6%.

Chart 33. Housing price index, quarter-over-quarter, %
Source: SSC



In June 2026, rents paid by tenants increased by 7.4% annually and 0.3% monthly.

3

MONETARY AND EXCHANGE RATE POLICY

3.1 MONETARY POLICY DECISIONS, TOOLS, MONEY MARKET AND EXCHANGE RATE

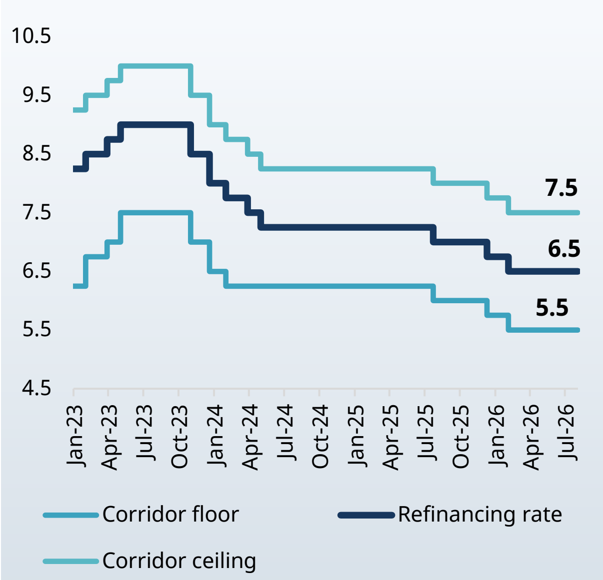
During the reporting period, the CBA's monetary policy was aimed at keeping inflation within the target range influencing monetary conditions. Monetary policy tools were employed taking into account developments in the financial market and the liquidity position of the banking system. Over the period, the AZIR index moved close to the refinancing rate. Both the secured and unsecured segments of the interbank money market remained active.

3.1.1 Monetary policy decisions

The CBA's Management Board discussed the interest rate corridor parameters five times during the past period of 2026. In the first monetary policy meeting, the refinancing rate was lowered from 6.75% to 6.5%, the ceiling of the interest rate corridor from 7.75% to 7.5%, and the floor 5.75% to 5.5%. In subsequent meetings, a decision was made to keep all interest rate parameters unchanged. Monetary policy decisions were made considering the consistency of actual inflation with the forecasted range, regional geopolitical stance, global financial market developments, domestic macroeconomic environment, and monetary policy transmission. Decisions on the interest rate corridor were communicated to the public under the preannounced schedule with analytical commentaries.

Chart 34. Interest rate corridor parameters, %

Source: CBA



The reference interest rate formed in the interbank unsecured money market - AZIR continued to move on a trajectory close to the refinancing rate. While the average spread between the AZIR index and the refinancing rate stood at 0.21 pp in 2025, it declined to 0.05 pp during H1 2026. The shrinkage of the spread suggests a high transmission of the refinancing rate to the interest rates established in the interbank market.

Chart 35. Dynamics of the refinancing rate and the AZIR index
Source: CBA

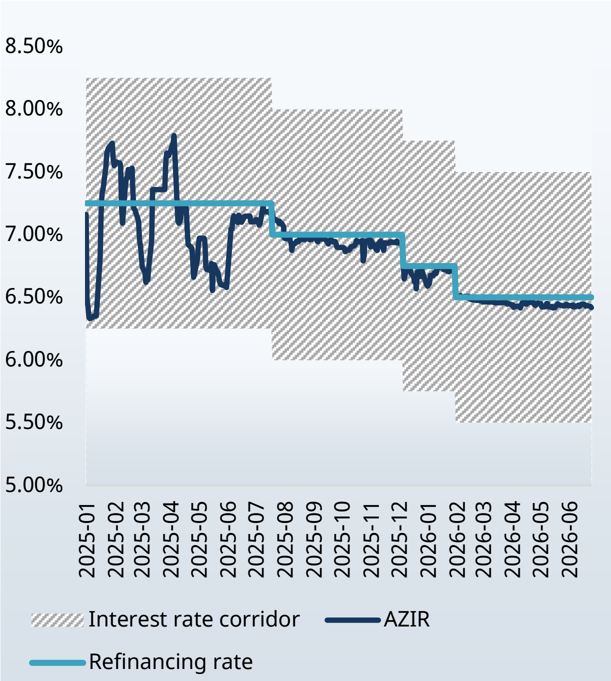
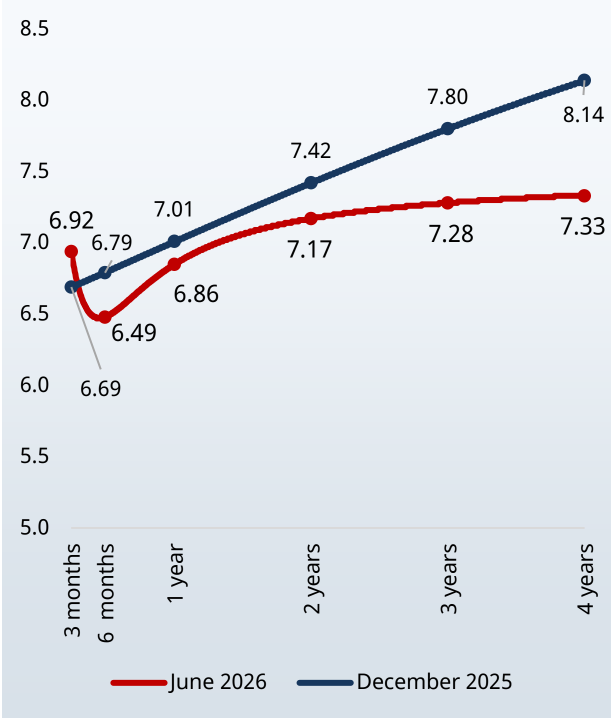


Chart 36. Yield curve, %
Source: CBA



The CBA's refinancing rate-related decisions also affected the dynamics of yields in the government securities market. Yields across most segments of the yield curve declined by end-June 2026 compared with end-December of the previous year. The yield on 6-month government bonds decreased from 6.79% in December to 6.48% at end-June, while yields on 1-year, 3-year, and 4-year bonds declined from 7.01% to 6.85%, from 7.80% to 7.28%, and from 8.14% to 7.33%, respectively.

3.1.2 Monetary policy tools

In H1 2026, monetary policy tools were applied, considering trends observed in the financial markets and the banking system's liquidity position. Various term monetary operations were used to manage liquidity during the period. Standing facility tools were used actively, and the quantitative parameters of open market operations were determined based on liquidity forecasts. The effective use of monetary policy tools ensured that short-term interest rates in the interbank money market were formed within the interest rate corridor.

In the reporting period, banks used CBA's both liquidity absorbing and liquidity providing standing facilities. Banks accessed the overnight deposit standing facility on 100% of business days, while the overnight reverse repo facility was used on 3% of business days. 112 overnight deposit operations and four overnight reverse repo operations were carried out during the period.

Chart 37. Amounts placed by banks with the CBA (overnight deposits) and absorbed from banks through overnight reverse repos under the CBA's standing facilities, in million AZN
Source: CBA

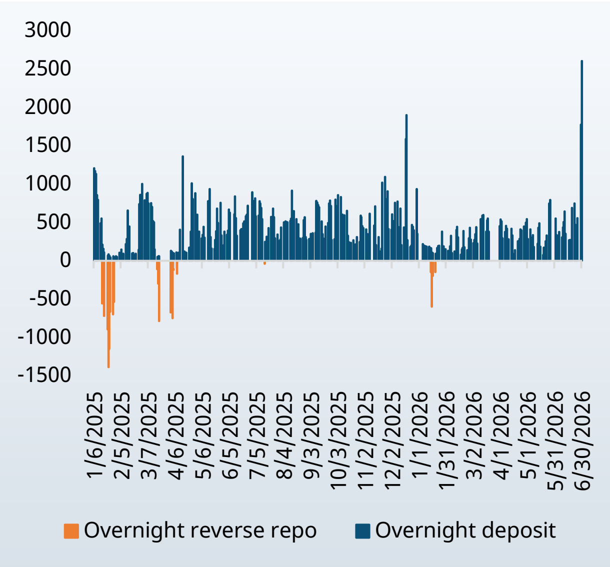
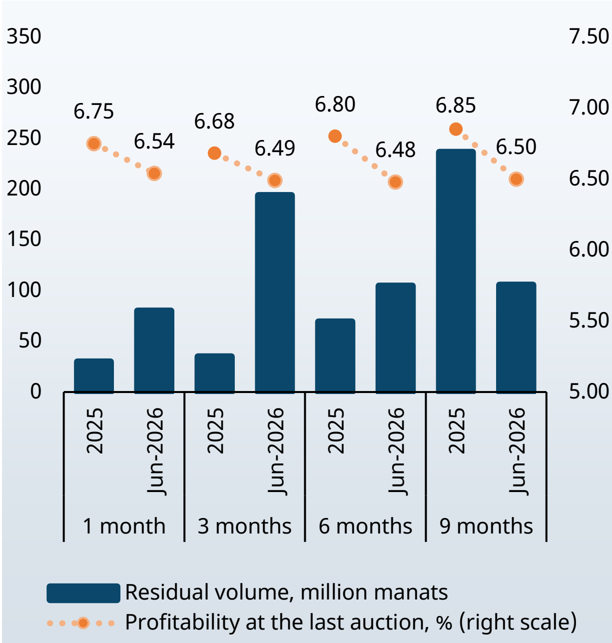


Chart 38. Amount and yield on CBA's short-term notes in circulation
Source: CBA



In the reporting period, the CBA mainly relied on 7-day deposit operations to minimize the impact of autonomous factors on monetary conditions and steer AZIR closer to the policy rate. In January-June 2026, the CBA held 48 deposit auctions. The average transaction volume for those auctions was AZN1423M.

Auctions for the placement of 28-day (1 month), 84-day (3 months), 168-day (6 months), and 252-day (9 months) CBA notes continued to be conducted. In total, 92 note auctions of various maturities were organized by the CBA over the period, 23 auctions for each maturity. The total amount of the CBA's note portfolio made up AZN484M, y.o.y. up by AZN113M.

Yield on short-term notes declined. Yields recorded at the final auctions held in June 2026 declined across all maturities compared with end-December of the previous year. Thus, yields on 28-day notes declined from 6.75% to 6.54%, yields on 84-day notes from 6.68% to 6.49%, yields on 168-day notes from 6.80% to 6.48%, and yields on 252-day notes from 6.85% to 6.50%.

Ongoing implementation of reserve requirements under the averaging regime continued to support banks' flexible management of liquidity. According to the results of monitoring conducted, the average balances of banks' correspondent accounts with the CBA in both national and foreign currencies exceeded the amount of funds required to be maintained as mandatory reserves throughout the reporting period. These indicators suggest that the banking sector possessed sufficient liquidity.

The banking sector operated under conditions of excess liquidity. Excluding funds to be held as required reserves, the sector's structural liquidity surplus (the difference between the CBA's liabilities to the banking system and its claims on banks) reached AZN6B at the end of the first half of the year, increasing by 2.1 times compared with December of the previous year. This indicates that banks' lending capacity remained sufficiently high.

Overall, in H1 2026, CBA's monetary operations ensured effective liquidity management in the banking system and supported the achievement of operational targets of monetary policy. During the remainder of the year, the use of monetary policy tools will continue to be guided by liquidity conditions in the banking system, the macroeconomic environment, and financial market developments.

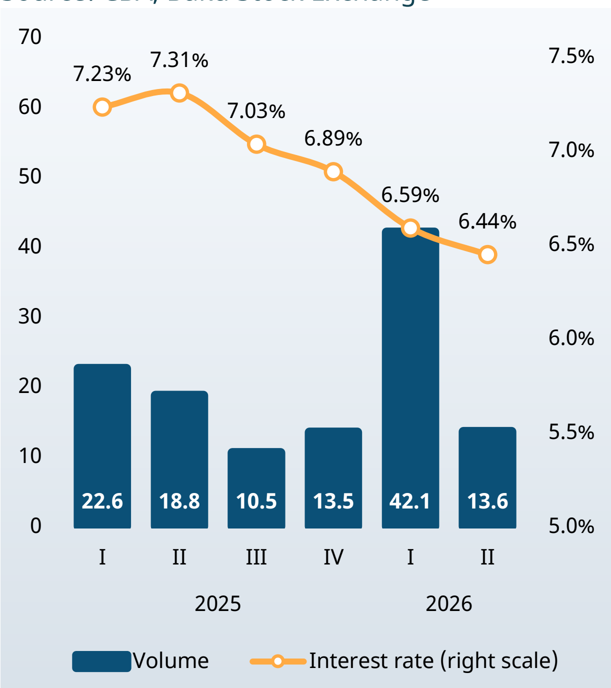
3.1.3 Money market

During the first six months of 2026, activity in the money market remained high. Continued demand for short-term funding supported activity in the interbank market. At the same time, interest rates declined in certain segments of the money market.

AZN55.7B worth 1530 transactions were concluded in the Bloomberg trading system in the unsecured market (y.o.y. up by 35%). In volume terms, 96% of the concluded transactions consisted of 1–3-day operations.

Chart 39. Transactions in the interbank money market, in billion AZN

Source: CBA, Baku Stock Exchange



Interest rates in the unsecured interbank market declined during the reporting period. The average interest rate on transactions in the unsecured interbank money market decreased from 6.58% in Q1 2026 to 6.44% in Q2 2026. Overall, the average interest rate in the unsecured market stood at 6.55% in the first half of the year, 0.71 pp lower than a year earlier.

In addition to the unsecured interbank market, high operational activity was maintained in the repo market. In particular, the second quarter of 2026 recorded the highest transaction volume in recent periods. During the first six months of the year, 3,015 repo transactions with a total volume of AZN 20.6 billion were concluded in the repo market, Of the total transaction volume, 87% was generated through transactions involving banks. Transactions with maturities of 6–8 days accounted for 90% of total repo transactions.

Chart 40. Repo market operations, in billion AZN

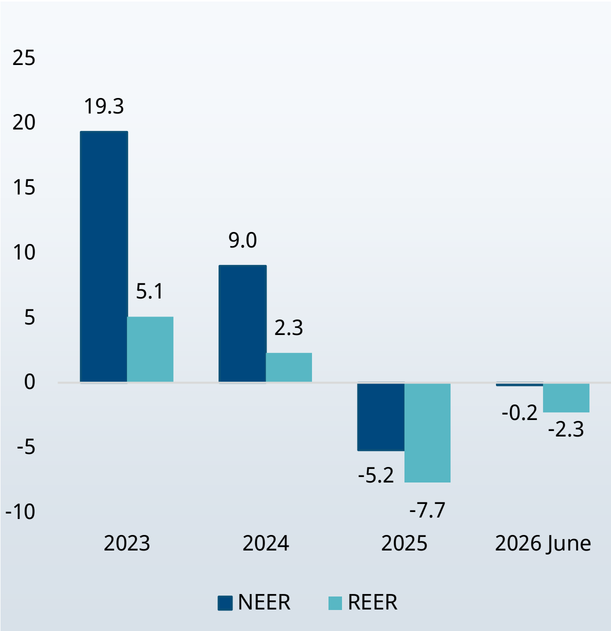
Source: CBA, Baku Stock Exchange

The downward trend in the weighted average interest rate on repo transactions continued across the quarters. The weighted average interest rate declined from 6% in Q1 to 5.68% in Q2. Overall, the average interest rate on repo transactions stood at 5.83% in H1 2026, 1.08 pp lower than a year earlier.

3.1.4 Bilateral and multilateral exchange rates

The official USD/AZN exchange rate was determined based on the average exchange rate of interbank transactions (both auction and over-the-counter transactions conducted through Bloomberg trading system). In the reporting period, the average daily official USD/AZN exchange rate was AZN1.7. The effective exchange rate indices of the manat evolved broadly in line with the exchange rates of the currencies of Azerbaijan's trading partner countries.

Chart 41. Effective exchange rate indices (compared with end-2025)
Source: CBA



Compared with last December, the non-oil trade-weighted NEER of the manat depreciated by 0.2% in June 2026, while the REER depreciated by 2.3%. Inflation in Azerbaijan was lower than the weighted average inflation in trading partners and had a downward effect on the REER. Compared to last December, Azerbaijan's 6-month inflation rate was 2.7%, while the weighted average inflation rate across trading partners was 4.7% in June 2026.

3.2 MONEY SUPPLY, DEPOSIT AND CREDIT MARKET

In the first half of 2026, money supply, deposits, and credit to the economy increased, alongside continued de-dollarization.

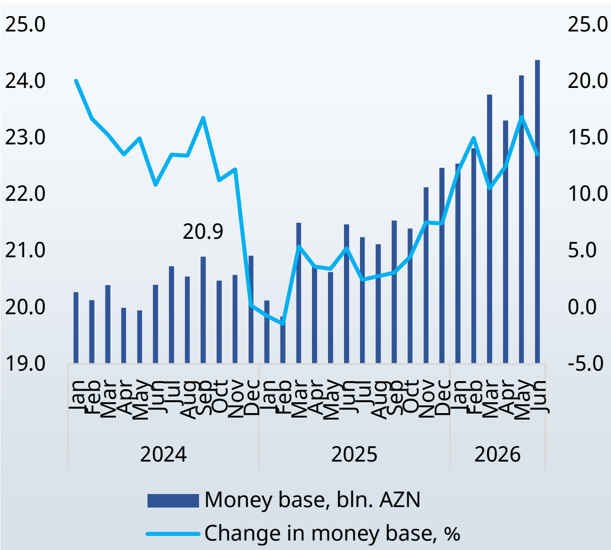
3.2.1 Base money and money supply

In H1 2026, the base money in manat increased by 8.5% to AZN24.4B, primarily driven by the changes in government account balances and CBA's foreign currency purchases. Cash in circulation[9], a structural element of base money in manat, increased by 4.7%, while the balance of correspondent accounts in manat increased by 34.4%.

The manat money multiplier, which reflects the banking sector's money creating capacity (the ratio of broad money in manat to the money base in manat), stood at 1.77.

Chart 42. Amount of base money and its year-over-year change

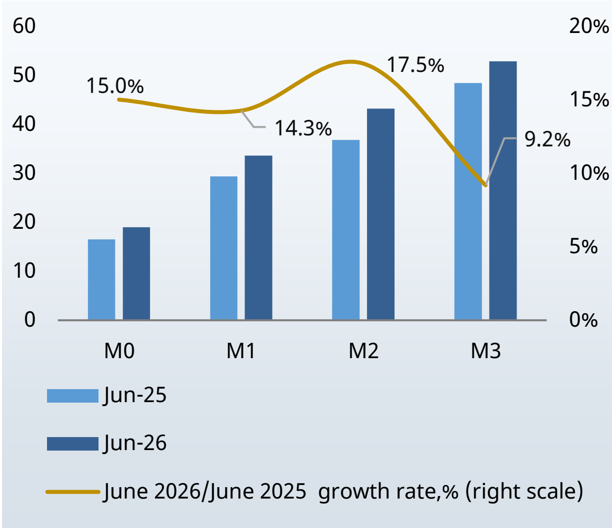
Source: CBA



In H1 2026, broad money supply (M3) increased by 6.1% to AZN52.9B. Broad money supply in manat (M2) increased by 7.1% to AZN43.3B as of the end of the reporting period.

Chart 43. Money aggregates, in billion AZN

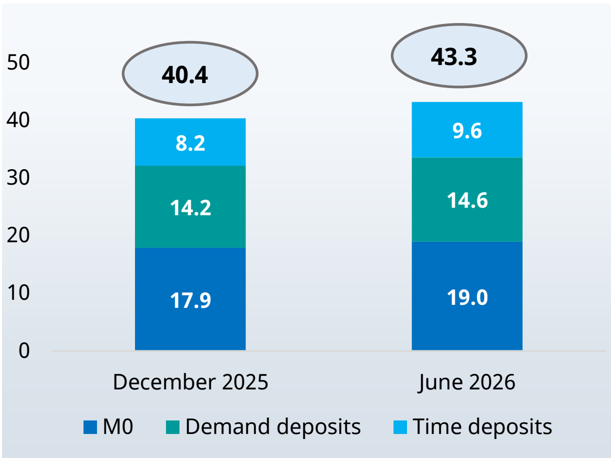
Source: CBA



In January-June 2026 all structural elements of M2 money aggregate grew. Cash in circulation (M0) increased by 5.8%, term savings and deposits by 17.2%, and demand savings and deposits by 2.8%. The share of demand deposits in M2 decreased by 1.4 pp to 33.8%, and that of term deposits increased by 1.9 pp to 22.2% by end-June.

Chart 44. Composition of broad money supply in manat, in billion AZN

Source: CBA



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[9] Cash money outside the banking system, cash in bank ATMs and cash offices

The share of cash (M0) in broad money supply in manat (M2) decreased by 0.5pp to 43.9%.

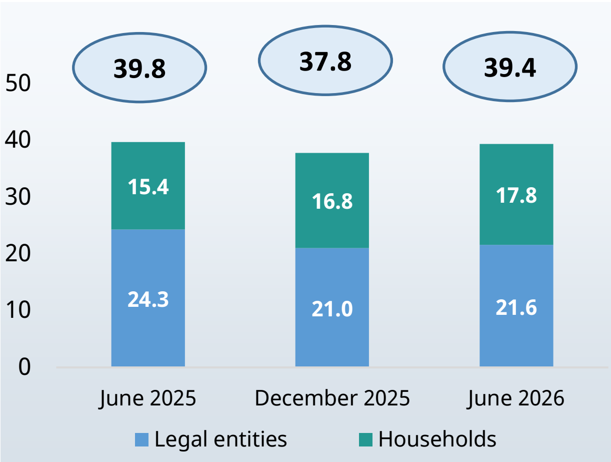
De-dollarization continued. In June the share of foreign currency denominated savings and deposits in total savings and deposits stood at 28.5% (29.7% early year), and in M3 money aggregate stood at 18.3% (19% early year).

3.2.2 Deposit market

In H1 2026, the deposit portfolio (excluding the financial sector) increased by 4.2% to AZN39.4B. Term deposits increased by 8.5% to AZN17.4B, while current deposits increased by 1.1% to AZN22.1B.

As of end-June, total deposits of legal entities increased by 2.6% to AZN21.6B since early year. During the period, current accounts accounted for 72.2% of deposits held by legal entities, while term deposits accounted for 27.8%.

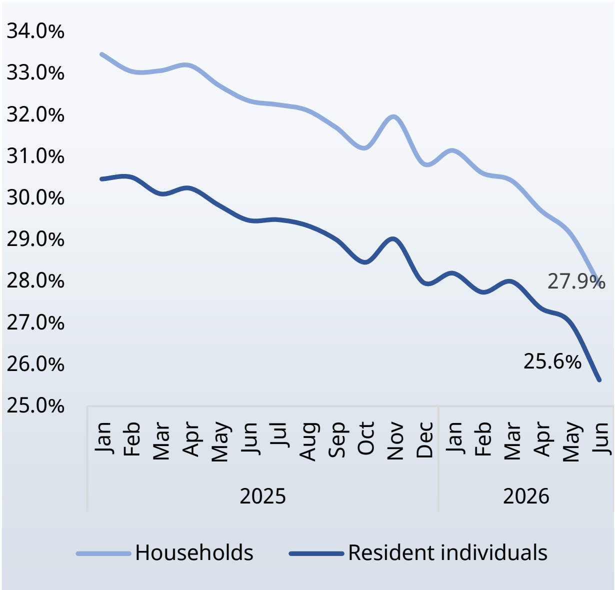
Chart 45. Deposits, in billion AZN
Source: CBA



At end-June 2026 deposits in manat amounted to AZN26.2B, while foreign currency denominated deposits amounted to AZN13.2B equivalent.

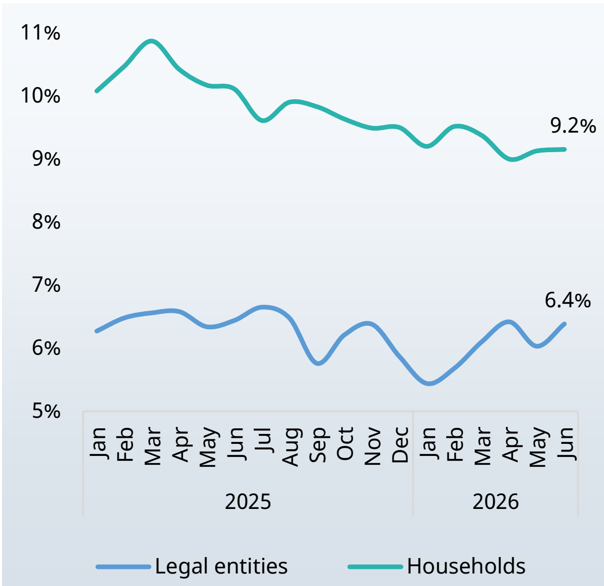
Dollarization of individuals' savings decreased by 2.9pp to 27.9% and that of resident individuals' savings decreased by 2.3% to 25.6%.

Chart 46. Dollarization of deposits, %
Source: CBA



Interest rates on newly attracted manat deposits on individuals decreased by 0.3 pp. As of the end of June, interest rates on newly attracted deposits for legal entities was 6.4%. Interest rates on newly attracted foreign currency deposits decreased by 0.1 pp on individuals and stood at 3.3% on legal entities as of end-June.

Chart 47. Average weighted interest rates on newly attracted manat deposits and savings
Source: CBA



3.2.3 Credit market

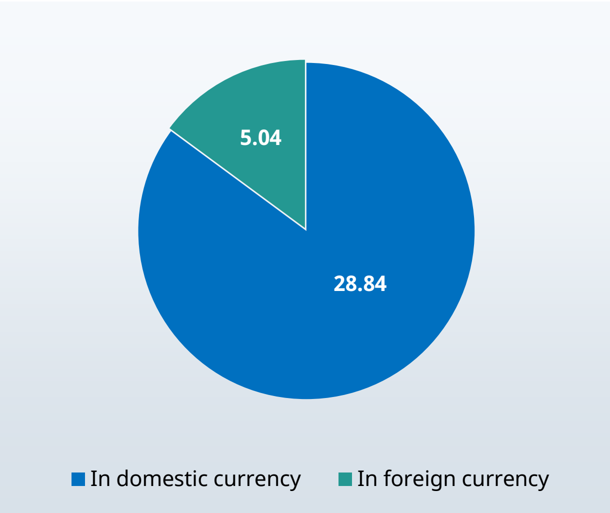
Credit investment in the economy continued to grow in January-June 2026. The loan portfolio (banks and nonbanks) increased by 6.1% to AZN33.9B in June compared with the early year. Long-term loans dominated and stood at 82.5% as of the end of the period. Long-term loans increased by 6.8% to AZN27.9B. Short-term loans have increased by 2.6% since the early year to AZN5.9B.

Business loans increased by 6.7% to AZN17.2B as of end-June. The highest growth in business loans was in transport (36%). Consumer and mortgage loans increased by 6% and 2.7% to AZN9.9B and AZN4.7B respectively.

Foreign currency denominated loans accounted for 14.9% of total loans as of the end period.

Chart 48. Currency structure of the loan portfolio, in billon AZN

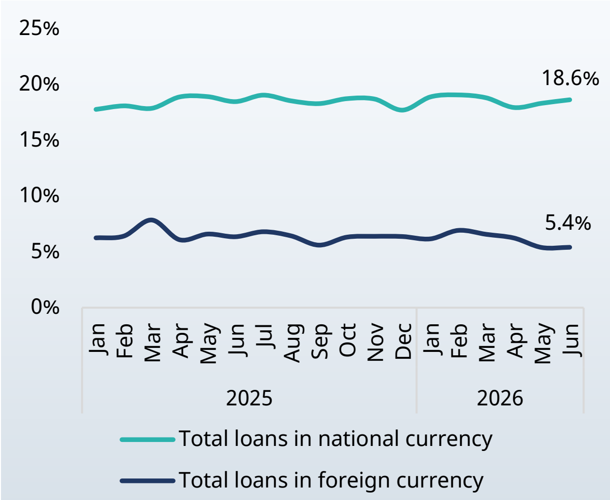
Source: CBA



In June 2026, average weighted interest rates on newly issued loans in manat stood at 18.6%, those in foreign currency stood at 5.4%.

Chart 49. Average interest rates on newly issued loans (banking sector)

Source: CBA



Over the past year, interest rates on manat-denominated loans have remained broadly stable, while those on foreign-currency-denominated loans have declined.

4

ECONOMIC OUTLOOK

4.1 GLOBAL ECONOMIC FORECASTS AND RISKS

Revised projections indicate that global economic growth continues this year, albeit at a somewhat slower pace. The outlook for global growth remains broadly unchanged, while global inflation is expected to rise initially before gradual moderation.

4.1.1 Global economic growth and inflation forecasts

According to the IMF's WEO July 2026, global economic growth is projected at 3.0% in 2026 and 3.4% in 2027. The revised projections indicate that global growth will be slower in 2026 than both the growth in 2024–2025 and the pre-pandemic historical average of 3.7%. The 2026 growth projection was revised down by 0.1 pp from the previous forecast, while the 2027 projection was revised up by 0.2 pp. The slowdown in growth this year is mainly attributable to the effects of the conflict in the Middle East. However, stronger demand in the global technology sector, driven by advances in and adoption of AI, partly offsets these adverse effects.

In the latest report, growth projections for AEs were revised down by 0.1 pp for the current year and up by 0.1 pp for the following year compared to the previous forecast. Growth in this group is projected at 1.7% in 2026 and 1.8% in 2027. However, these projections remain below the 1.9% growth of the past two years.

In the United States, economic growth is projected at 2.3% in 2026 and 2.2% in 2027. The growth projection for the current year is unchanged from the previous forecast, while the projection for the following year was revised up by 0.1 pp. Economic activity is supported by favorable financial conditions, fiscal policy, and investment in technology-related sectors.

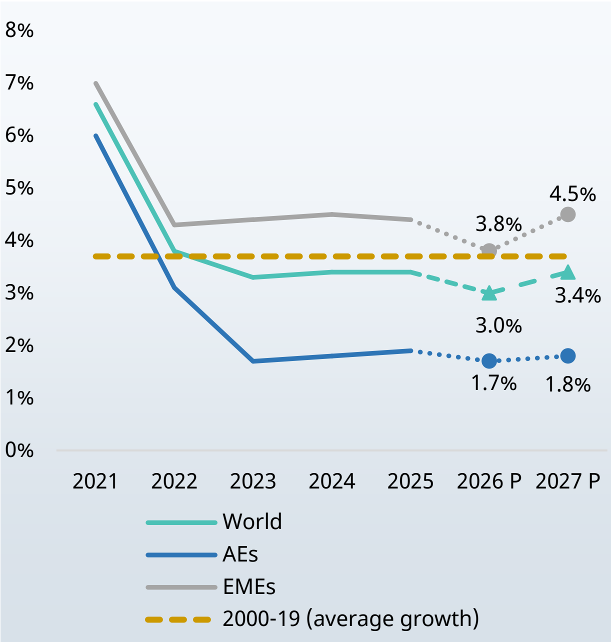
Economic growth in the euro area is projected at 0.9% in 2026 and 1.2% in 2027, both below the 1.4% growth in 2025. The growth projection for the current year was revised down by 0.2 pp, while the projection for the following year remains unchanged. Higher energy prices and weaker consumer confidence are weighing on the growth outlook.

In Japan, economic growth is projected at 0.6% in 2026 and 0.7% in 2027, down by 0.1 pp for 2026 and up by 0.1 pp for 2027 relative the previous report. Fiscal policy measures are mitigating the adverse effects of higher energy prices.

In the United Kingdom, economic growth is also projected to remain weaker than in 2025. Growth is projected at 1% in 2026 and 1.3% in 2027 with the fading effects of the energy shock in 2027. For 2026 it is up by 0.2pp compared with the previous forecast, while the projection for 2027 remains unchanged.

For EMEs, growth is projected at 3.8% in 2026 and 4.5% in 2027, down by 0.1pp for 2026 and up by 0.3pp for 2007 compared with the April forecast. Revisions to the growth outlook reflect factors including countries' geographic location, remittances, tourism revenues, sensitivity to financial conditions, and their position in global technology value chains.

Chart 50. Global economic growth forecasts
Source: The IMF WEO

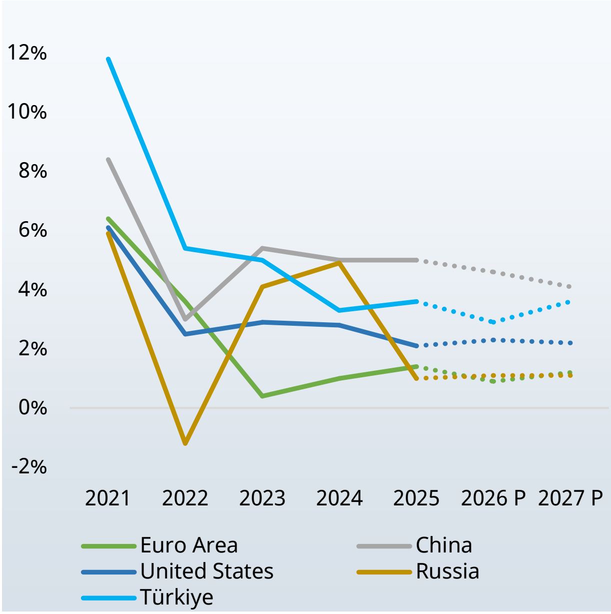


In China, economic growth is projected at 4.6% in 2026 and 4.1% in 2027, up by 0.2 pp for 2026 and by 0.1 pp for 2027 compared with the April forecast.

Higher commodity prices, in part, are supporting export revenues and thereby contributing to economic growth in Russia. Growth is projected to be 1.1% in both 2026 and 2027, unchanged from the April forecast.

Türkiye's growth projection for the current year was revised down. Economic growth is projected at 2.9% in 2026 and 3.6% in 2027, down by 0.5 pp for 2026 and up by 0.1 pp for 2027 vs the April forecast.

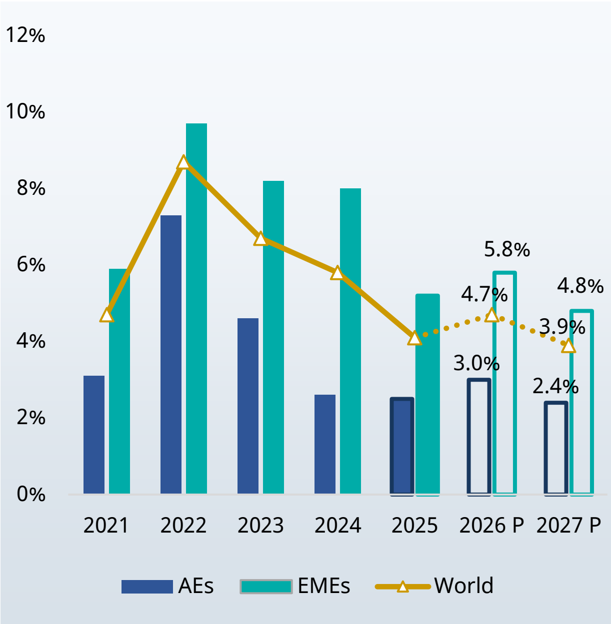
Chart 51. Growth projections across certain countries
Source: The IMF WEO



According to the IMF's updated July forecast, the upward trajectory of global inflation is expected to continue this year, before moderating again in 2027. Inflation rates are expected to remain uneven across countries, attributable to differences in exchange rate pass-through, persistent services inflation, labor market conditions, and other country-specific economic factors. Global inflation is projected to rise to 4.7% in 2026, from 4.1% in 2025, before declining to 3.9% in 2027, up by 0.3 pp for 2026 and by 0.2 pp for 2027 vs the previous forecast.

Overall, inflation projections for both AEs and EMEs were revised upward for 2026 and 2027. Inflation in AEs is projected at 3.0% in 2026 and 2.4% in 2027, while inflation in EMEs is projected at 5.8% and 4.8%, respectively. For 2026, inflation projections were revised up by 0.2pp for AEs and by 0.3 pp for EMEs.

Chart 52. Global inflation forecasts
Source: The IMF WEO



4.1.2 Global risks

According to the IMF's WEO July 2026, risks to the global economy became more balanced compared with the April forecast but remain tilted to the downside amid geopolitical tensions. A renewed escalation of geopolitical tensions in the Middle East could weaken global growth and intensify inflationary pressures. The conflict is contributing to volatility in commodity prices, raising inflation expectations, and weighing on the global economy through tighter financial conditions.

Further increases in commodity prices, supply shortages, and exchange rate pressures amid geopolitical conflicts also pose downside risks.

The limited increase in oil prices and the fading impact of higher oil prices on economic activity reflect the release of strategic reserves. The reserves are currently approaching multi-year lows and could reach critical levels if supply disruptions persist.

Higher food and energy prices could increase the risk of social unrest and domestic political instability, particularly in some fragile economies in Africa. At the same time, growing disruptions to international financial flows could accelerate capital outflows from EMEs with weak macroeconomic fundamentals.

AI-related risks are characterized by both upside and downside scenarios. If AI-related capital expenditure remains elevated or financial conditions ease further, this could offset some of the adverse effects stemming from geopolitical tensions, trade disruptions, and limited policy buffers. Conversely, an AI wave and excessive optimism in financial markets could contribute to macro-financial instability. Under a scenario of weaker-than-expected productivity gains from AI, a decline in investment in technology sectors could undermine confidence and amplify risks.

A reduction in geopolitical tensions would support global economic growth. Peace agreements could accelerate the restoration of global trade routes and supply chains. Trade agreements could lower tariffs and revive investment that has been deferred due to an uncertain external environment.

4.2 MACROECONOMIC OUTLOOK FOR AZERBAIJAN

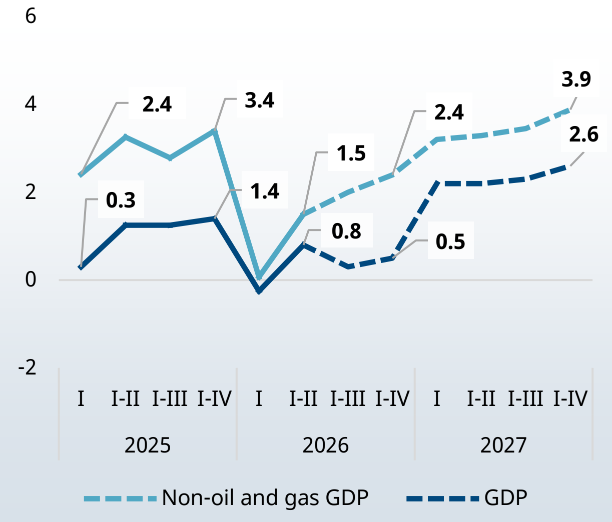
According to the CBA's July 2026 projections, annual inflation is expected to gradually decline and remain within the target range over the medium term. At the same time, the non-oil and gas sector is expected to remain the main driver of economic growth.

4.2.1 Economic growth forecast

Despite downward revision of economic growth projections for 2026, the overall outlook remains positive. According to the CBA's July 2026 projections, real GDP growth is expected to be 0.5% in 2026, while non-oil and gas GDP is projected to grow by 2.4%. In 2026, the oil and gas sector is expected to weigh on overall GDP growth, while the non-oil and gas sector is projected to make a positive contribution. Growth in the non-oil and gas sector is expected to be driven by household final consumption expenditure, net exports of goods and services, and gross fixed capital formation.

Chart 53. July forecast for real GDP and non-oil and gas GDP growth

Source: SSC, CBA AzIM[10] model



In 2027, real GDP growth is projected at 2.6%, while non-oil and gas GDP is expected to grow by 3.9%. The oil and gas sector is projected to make a neutral contribution to overall GDP growth in 2027, while the non-oil and gas sector is expected to make a positive contribution. Growth in the non-oil and gas sector is expected to be driven by household final consumption expenditure and net exports of goods and services.

The projections for the oil and gas sector are based on government's official forecasts. In the first six months of the current year, oil and gas GDP declined by 0.7%. Taking this trend into account, if oil and gas GDP growth in 2026 is assumed to range between -1% and -2%, rather than the projected -3.3%, overall GDP growth in 2026 could be range 1.0–1.3%.

The realization of the projected growth in the non-oil and gas sector in 2026 and 2027 will largely depend on developments in domestic and external aggregate demand.

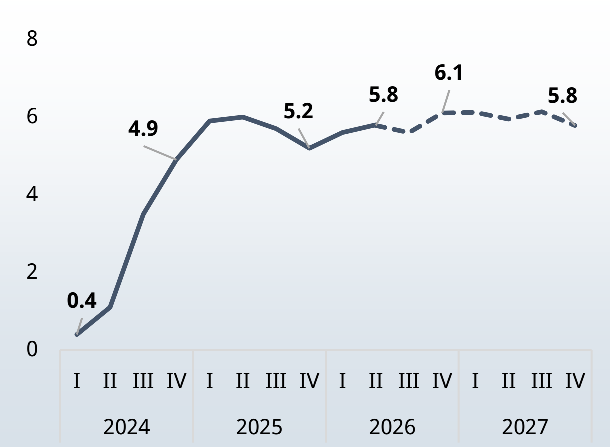
4.2.2 Inflation forecast

According to the CBA's July projections, annual inflation is expected to remain within the target range over the medium term. Annual inflation is projected at 6.1% at end-2026, 6% 12 months ahead (i.e., in June 2027), and 5.8% at end-2027. Accordingly, annual inflation is expected to return to the target range from the second half of 2027. For 2026, weighted inflation in trading partners, agricultural producer prices, household consumption, and government consumption are expected to

[10] The Azerbaijan quarterly macroeconomic forecasting model (AzIM) is a New Keynesian model of a small open economy. It is also referred to as a gap model, as it captures trend movements and explains deviations from trends. Variables respond actively to shocks in the short run and converge toward their steady-state levels over the long run. AzIM comprises four core equations: aggregate demand, the Phillips curve, a monetary policy rule, and interest rate parity. The model parameters have been calibrated, and the model has undergone standard econometric tests, including impulse response analysis, decomposition analysis, and in-sample simulations

contribute 2.81, 2.60, 1.06, and 0.24 pp, respectively, to annual inflation. In contrast, the NEER and other factors are projected to have downward effects of 0.53 and 0.08 pp, respectively.

Chart 54. July forecast for annual inflation, %
Source: CBA AzIM model



According to the estimates, APPI is expected to contribute 2.45 pp to the projected annual inflation rate of 5.8% in 2027, while inflation in trading partners, household consumption, government consumption, and other factors are expected to contribute 1.88, 1.33, 0.27, and 1.22 pp, respectively. In contrast, the NEER is projected to have a downward effect of 1.34 pp.

The realization of the projections will depend on developments in both external and domestic factors. Amid uncertainty in the global environment, inflation in trading partners represents an external risk factor, associated with elevated volatility in global commodity and financial markets. In particular, the continuation of conflicts in the Middle East is exacerbating price volatility in energy markets. The persistence of this trend over the remainder of the year could affect inflation dynamics in trading partners.

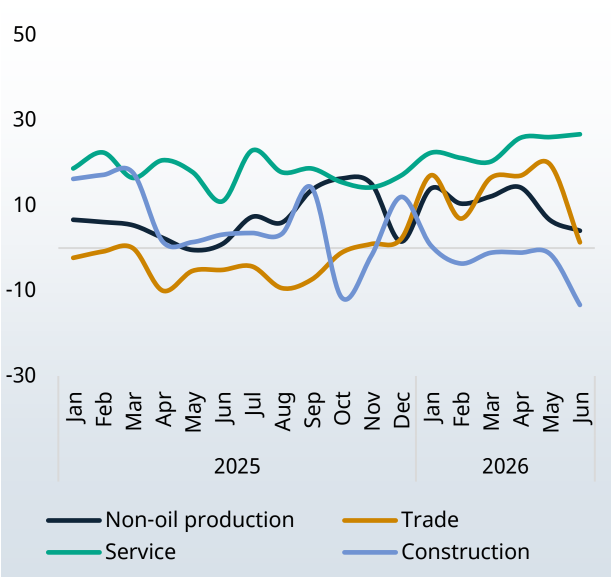
In addition, a weakening of the NEER could accelerate the pass-through of import price pressures to domestic prices. Another important risk factor relates to climate change. Adverse weather conditions could constrain agricultural production and put upward pressure on global food prices.

As for domestic factors, under the current fiscal and monetary policy framework, the likelihood of aggregate demand rising to a level that would generate significant inflationary pressures is low.

4.2.3 Inflation expectations

In June 2026, inflation expectations evolved differently across sectors. According to the CBA's RSM results, inflation expectations in the non-oil and gas manufacturing and trade sectors were higher than year-over-year, although they have declined in recent months. In the services sector, inflation expectations have remained broadly stable in recent months. In the construction sector, price expectations for the next three months have declined significantly both year-over-year and in recent months.

Chart 55. Price expectations for upcoming three months across the real sector[11]
Source: Surveys among entities



[11] The index shown in the chart is calculated as the difference, in percentage, between the share of positive and negative responses. Ranging from -100 to +100, the index indicates the direction of price expectations over the next three months.

CHARTS AND TABLES

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