STATE OIL FUND OF THE REPUBLIC OF AZERBAIJAN

ANNUAL REPORT
2018

CONTENT

ABBREVIATIONS

ACG - AZERI-CHIRAG-GUNESHLI
AIOC - AZERBAIJAN INTERNATIONAL OPERATING COMPANY
BOE - THE BANK OF ENGLAND
CBAR - THE CENTRAL BANK OF THE REPUBLIC OF AZERBAIJAN
ECB - EUROPEAN CENTRAL BANK
FED - THE FEDERAL RESERVE
GDP - GROSS DOMESTIC PRODUCT
IFSWF - THE INTERNATIONAL FORUM OF SOVEREIGN WEALTH FUNDS
IMF - THE INTERNATIONAL MONETARY FUND
OPEC - ORGANIZATION OF THE PETROLEUM EXPORTING COUNTRIES
PSA - PRODUCTION SHARING AGREEMENT
SGC - SOUTHERN GAS CORRIDOR
SOFAZ - THE STATE OIL FUND OF THE REPUBLIC OF AZERBAIJAN
SSC OF AZERBAIJAN - THE STATE STATISTICAL COMMITTEE OF THE REPUBLIC OF AZERBAIJAN
SWFI - THE SOVEREIGN WEALTH FUND INSTITUTE
VAR - VALUE AT RISK
WB - THE WORLD BANK

1. ABOUT SOFAZ

The State Oil Fund of the Republic of Azerbaijan (SOFAZ) was established in accordance with the Decree of national leader Heydar Aliyev No. 240 on December 29, 1999. SOFAZ is a mechanism whereby energy-related earnings are accumulated and efficiently managed for future generations.

SOFAZ is structured as an extra-budgetary fund and functions as the legal entity separate from the government or central bank. Statute of SOFAZ was approved in 2000.

The cornerstone of SOFAZ's philosophy is to ensure intergenerational equality with respect to the benefit from the country's oil wealth.

MISSION

SOFAZ's mission is to transform depletable hydrocarbon reserves into financial assets generating perpetual income for current and future generations.

OBJECTIVES

SOFAZ's activity is directed to the achievement of the following objectives:

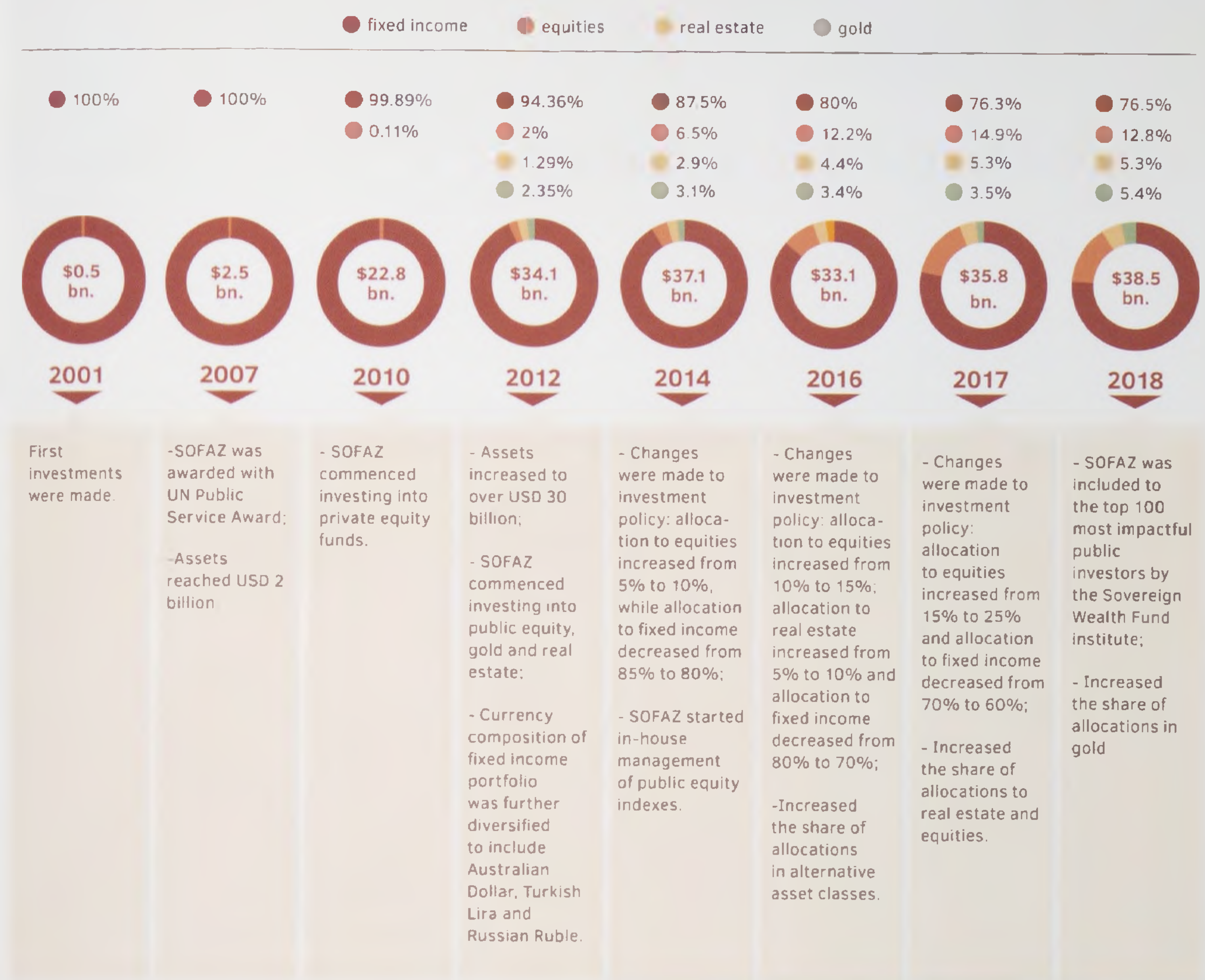
1. Supporting macroeconomic stability, participating in ensuring fiscal-tax discipline and decreasing dependence on oil revenues while stimulating development of the non-oil sector;
2. Funding major national scale projects to support socio-economic progress;
3. Ensuring intergenerational equality with regard to the country's oil wealth, accumulating and preserving oil revenues for future generations.

LEGAL FRAMEWORK

SOFAZ's operations are guided by the Constitution and laws of the Republic of Azerbaijan, Presidential decrees and resolutions, SOFAZ Statute and regulations.

SOFAZ's funding and withdrawal rules are clearly defined by the "Statute of the State Oil Fund of the Republic of Azerbaijan" and the "Rules on the preparation and execution of the annual program of revenues and expenditures (budget) of the State Oil Fund of the Republic of Azerbaijan". According to the Law "On budget system" of the Republic of Azerbaijan, all SOFAZ expenditures, except for operating expenditures, are incorporated into an annual consolidated government budget presented to the Parliament for approval. Thus, indirectly, all citizens participate in the discussions of the budget of SOFAZ. In compliance with this law, SOFAZ can only execute the expenditures envisaged by its budget.

SOFAZ's investment and risk management policies are defined by "Investment Guidelines" and "Investment Policy" approved by the President of the Republic of Azerbaijan after the review of the Supervisory Board. According to its "Investment Policy", SOFAZ's investment decisions should aim at maximizing the risk-adjusted returns. According to the "Investment Guidelines", SOFAZ makes investment decisions independently.



Note: The diagram illustrates year by year AuM and breakdowns of the investment portfolio by asset class

OUR VALUES: RESPECT, TEAMWORK, TRUST AND TRANSPARENCY

Since its very inception, SOFAZ has built a strong cooperation with a number of financial organizations and institutions in Azerbaijan and globally. SOFAZ's relations with its partners are based on the principles of mutual respect, trust, teamwork and transparency.

RESPECT

SOFAZ's relations with international organizations, financial institutions, government bodies as well as its employees are based on mutual respect. Deeply rooted into the Fund's philosophy, trust and respect are the main factors in maintaining healthy relations in workplace and cooperating fruitfully with partners.

TEAMWORK

It is through teamwork and joint efforts that SOFAZ succeeds in all of its endeavors and strengthens its prestige locally and worldwide. Building strong working relationships, praising personal, achievements and encouraging teamwork contribute to the establishment as well as further development of professional work environment.

TRUST

Since its inception, SOFAZ adheres to the highest standards of ethical behavior and honesty to gain the trust of its partners. SOFAZ expects all of its business partners to operate on the same principles of mutual trust and cooperation.

TRANSPARENCY

SOFAZ's activities are based on the principles of transparency and accountability. Internationally praised as a credible and transparent institution, SOFAZ, in line with the foremost international practices, ensures the highest level of transparency towards its counterparties, employees and external managers.

A way leading to independence

Azerbaijan, a country with great cultural and economic potential, is also abundant in natural resources. The so-called "black gold" (i.e., oil) is the main source of natural wealth of Azerbaijan. Being known as an ancient land of oil, Azerbaijan started commercial oil production in the middle of XIX century. In 1846, for the first time in the world, oil was extracted from mechanically drilled wells in Bibiheybat.

Development of oil drilling machines and technologies positively affected the structure of the oil industry. Oil production and refinery companies were established. Construction and further development of the first railway in Azerbaijan was also associated with the oil transportation. In the years 1899 - 1901, Azerbaijan was the world's largest oil producer, as it accounted for half of the global oil production. Azerbaijan attracted large amounts of foreign capital, which included some prominent names such as Rothschilds, Nobels among others. In this way, Baku became one of the industrial centers of the world.

The development of the oil industry was followed by the emergence of the Azerbaijani intelligentsia as a distinct social group. As a result, science, literature, and culture were significantly developed, and newspapers were published in our native language. This was also the period when the first national theatre was established. In 1901, the first girls' school in the Muslim world opened its doors in Baku with the support of Haji Zeynalabdin Tagiyev. 1908 was marked by another significant event in the history of musical culture of Azerbaijan. Composer Uzeyir Hajibayov composed the first opera in the Muslim East based on Nizami's poem "Leyli and Majnun". A 22-year-old composer laid the foundation of the national opera of Azerbaijan.

Since then our country has had many "firsts" which we remember with a feeling of pride. The majority of them were associated with oil. The development of the oil industry in our country has contributed to the breaking of new ground. Today, despite long years having passed since then, Azerbaijan is still known to the world as an oil country.

Source:
The official website of Visions of Azerbaijan magazine
The official website of Azerbaijan International magazine

100 YEARS of PRIDE

1918-2018

FIRST DRILLED OIL WELL | BAKU, BIBIHEYBAT, 1846

The First Democratic Republic of the Muslim East

May 28, 1918 was a turning point in the history of Azerbaijan and the opening of a new and glorious page. In February of 1917, after the fall of monarchy in Russia, Transcaucassian Seym (Parliament) was established in Tbilisi. A Muslim fraction of the Seim consisting of 44 members held a separate meeting on May 27, 1918 and decided to proclaim the independence of Azerbaijan. On May 28, 1918, the first democratic, constitutional, and secular parliamentary republic of the Muslim East – Azerbaijan Peoples Republic – was established.

During the 23-month ruling period, the laws and resolutions adopted by the Parliament were aimed at preserving the independence and territorial integrity of the country and establishing a modern and democratic state with guaranteed human rights. The development of science, education, healthcare, and national enlightenment were the focus of attention during the years of ruling of the Azerbaijan Democratic Republic. During those years the Azerbaijani language was declared as an official language, Azerbaijan State University (now Baku State University), national army, national bank were established, national currency was put into circulation. Other important achievements include national sovereignty, democratization, free elections, building diplomatic relations, international recognition, and economic reforms.

The Azerbaijan Democratic Republic, which was established 100 years ago, has left an important mark on the history of the state of Azerbaijan. The prominent date – May 28, is celebrated each year as the Day of Republic in Azerbaijan.

Source: The official website of the Presidential Library

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YEARS of PRIDE

1918-2018

THE FIRST MEETING OF THE PARLIAMENT OF THE AZERBAIJAN DEMOCRATIC REPUBLIC, DECEMBER 7, 1918

3. GOVERNANCE AND TRANSPARENCY

3.1. SOFAZ MANAGEMENT

SUPERVISORY BOARD

The Supervisory Board, consisting of representatives of the state authorities and public organisations, carries out general oversight of SOFAZ's operations. The Board reviews and evaluates SOFAZ's draft annual budget, annual report and financial statements, along with an audit report. Members of the Supervisory Board are approved by the President of the Republic of Azerbaijan. The board members act entirely on a voluntary basis.

Supervisory Board consists of the following members:

Novruz Mammadov
Prime Minister of the Republic of Azerbaijan

Valeh Alesgerov
Deputy Speaker of the Parliament (Milli Majlis) of the Republic of Azerbaijan

Natig Amirov
Advisor to the President of the Republic of Azerbaijan on Economic Policy and Industry

Samir Sharifov
Minister of Finance of the Republic of Azerbaijan

Shahin Mustafayev
Minister of Economy of the Republic of Azerbaijan

Elman Rustamov
Governor of the Central Bank of the Republic of Azerbaijan

In 2018, the Supervisory Board of SOFAZ took a number of decisions regarding the SOFAZ's activities. The decision of the Supervisory Board of SOFAZ from 06 July, 2018 approved SOFAZ's annual report for 2017 and the independent Auditor's ("Pricewaterhousecoopers Audit Azerbaijan" LLC) Report on SOFAZ's financial activities. The Supervisory Board recommended SOFAZ's 2017 budget execution project (along with the opinion of the Chamber of Accounts) for the approval by the President of the Republic of Azerbaijan.

The adoption of the Law "On changes to the Law "On the state budget of the Republic of Azerbaijan in 2018"" dated from June 29, 2018 made it necessary to review the budget of SOFAZ in accordance with the provisions made in the state and consolidated budgets. So, changes were introduced to the SOFAZ's 2018 budget upon the proposal of the SOFAZ's Supervisory Board from July 06 2018, which also made it necessary to make changes to the Presidential Decree N° 1770 "On the budget of the State Oil Fund in 2018" adopted on December 28, 2017. Hence,with the decree of the President of the Republic of Azerbaijan as of July 17, 2018, SOFAZ's revenue projection was increased from AZN 11 559 256.2 thousand to AZN 15 310 823.9 thousand, while the expenditures were revised upward from AZN 9 730 221.8 thousand to AZN 11 480 221.8 thousand. Documents pertaining to the changes to SOFAZ's budget, together with the Board's opinions, were recommended for approval by the President of the Republic of Azerbaijan.

A meeting of the Supervisory Board was held on December 18, 2018. At the meeting, the Board, having viewed the SOFAZ's 2019 budget project as well as the data on SOFAZ's management expenditures submitted by SOFAZ's Executive Director, recommended the Fund's 2019 draft budget plan, including the major directions of the use of SOFAZ's assets and investment policy and its draft operating expenditures plan for approval by the President of the Republic of Azerbaijan. At the same time, the Board reviewed and approved the changes proposed to "the Rules on the keeping, placement and management of the foreign currency-denominated assets of the State Oil Fund of the Republic of Azerbaijan". The respective documents regarding the issues discussed above (along with the opinion of the Chamber of Accounts of the Republic of Azerbaijan on SOFAZ's budget project) were recommended for approval by the President of the Republic of Azerbaijan.

EXECUTIVE DIRECTOR

SOFAZ's day-to-day activities are managed by the Executive Director appointed by the President of the Republic of Azerbaijan. The Executive Director represents the Fund, appoints and dismisses employees of SOFAZ in a manner determined by the legislation, carries out operational management of SOFAZ's activities, ensures the management and investment of SOFAZ's assets in accordance with the Guidelines approved by the President of the Republic of Azerbaijan.

DEPUTY EXECUTIVE DIRECTOR

Deputy Executive Director is appointed by the President of the Republic of Azerbaijan. Israfil Mammadov was appointed as Deputy Executive Director of SOFAZ on July 23, 2013.

ADVISOR TO SOFAZ'S EXECUTIVE DIRECTOR

Advisor to SOFAZ's CEO is appointed by the Executive Director of SOFAZ. Nargiz Nasrullayeva-Muduroglu was appointed as Advisor to SOFAZ's CEO on July 6, 2017.

SOFAZ ORGANIZATIONAL STRUCTURE

Investment activity at SOFAZ is conducted by Investment Department, Risk Management Department and Settlements Department.

Investment Department

The Investment Department is responsible for developing investment strategy, investing across eligible asset classes, including fixed income, money market instruments, equity, real estate and gold.

The department has three divisions:

- Fixed income and money market division;
- Equity and alternative investment division;
- Real estate division.

Risk Management Department

The Risk Management Department is responsible for conducting relevant research for defining risk limits and providing proposals related to investment policy updates and benchmark selection. In addition, the responsibilities of this department also include, but are not limited to, assessment and management of risks related to traditional and alternative asset class investments, measuring the absolute and relative performance of investment porfolio, monitoring of compliance of SOFAZ's investment activities and its external managers to relevant regulations/ mandates, and ensuring that the allocations of investment portfolio are in accordance with investment policy.

The department has two divisions:

- Quantitative solutions and performance measurement division;
- Alternative investments risk management division.

Settlements Department

Settlements department operates under the SOFAZ's Finance and Operations Administration. The Settlements department is responsible for verifying trades with counterparties, settling trades with the custodian and correspondent banks, reconciling cash and transactions with statements from the banks, as well as reconciling external managers' transactions and positions.

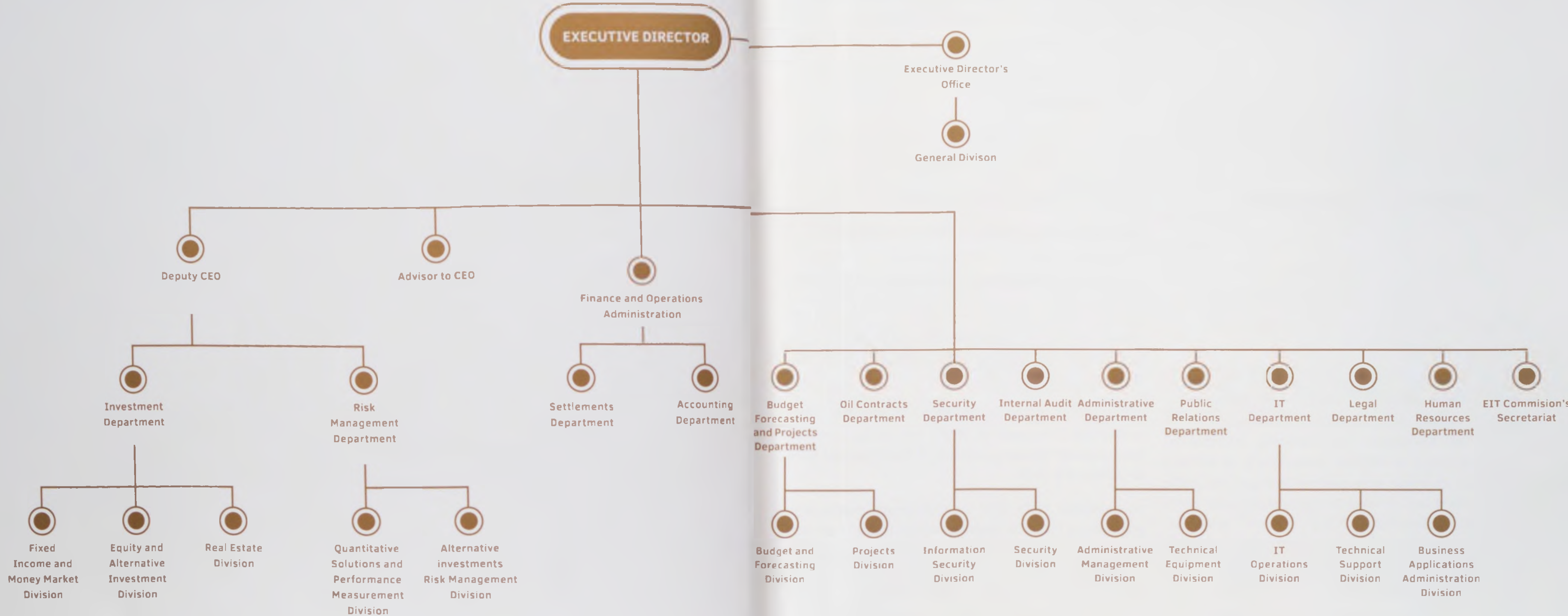
Budget Forecasting and Projects Department

The main purpose of the Department is to provide the preparation and approval of an optimal budget meeting the macroeconomic and fiscal requirements of the country and matching with the purposes of sustainable development of the Fund and to establish an effective control and monitoring system for the projects financed from the Fund's budget.

The department has two divisions:

- Budget and forecasting division;
- Projects division.

Figure 1. **SOFAZ's organizational structure**



Granting of Voting Rights to Women for the First Time in the East

During the 23-months ruling period, the Azerbaijan Democratic Republic accomplished great works and adopted many important decisions for the state system. Clause IV of the Declaration of Independence adopted by the Azerbaijan People's Republic on May 28, 1918 guaranteed equal political and citizenship rights for all citizens living on the territory of the country irrespective of their nationality, faith, class, estate, or sex. Based on this historical decision, women's voting rights within the Azerbaijan Democratic Republic have been legally endorsed. In this way, Azerbaijan became the first country in the Muslim East that introduced the right of women to vote and to be elected.

Our people have travelled a long path to reach this historic milestone. In the second half of the XIX century, a national revival process started in Azerbaijan as a result of oil industry development. Progressive community leaders of the country have made an education of women and expansion of their rights one of their priorities.

Granting equal voting rights to men and women for the first time in the Muslim world was a historic achievement. Thus, the women's right of being involved in political processes was granted in Azerbaijan even earlier than it was in some European countries and the U.S.A, which are considered to be the birthplaces of democracy.

In the beginning of the XX century, women were an embodiment of progress in Azerbaijan. This tradition is continued in the XXI century.

Source: The official website of the Presidential Library
"About Azerbaijan" website

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YEARS of PRIDE

1918-2018

FEMALE WORKERS IN PARLIAMENT OF THE AZERBAIJAN DEMOCRATIC REPUBLIC, 1918

4. NATIONAL ECONOMY AND SOFAZ

4.1. MACROECONOMIC DEVELOPMENT

Global economy. 2018 was characterized by sharp price fluctuations in the oil market. Oil prices continued to rise and the average price of Azerbaijani profit oil peaked at USD 71 per barrel. It was expected that, this positive trend to continue into the future, as a result of the alleged supply deficit and the restoration of sanctions against Iran. However, BRENT crude, benchmark that serves as a reference price for sellers and buyers of crude oil, unexpectedly slumped 40% in value after hitting the threshold of USD 80 per barrel in the early October of 2018. This phenomenon disproved the forecasts of many renowned experts and once again emphasized the particular difficulties of oil price forecasting. Though resource-rich countries as a whole demonstrated stronger economic fundamentals in 2018 than in the two years prior, their performance was still far behind the forecasts of leading global organisations. According to the World Bank's (WB) calculations, the GDP growth in the resource-rich countries group averaged 1.7% in 2018.

Overall, 2018 was characterized by positive trends for the whole global economy as the global GDP rose by 3%. This outcome, was similar to 2017's global GDP growth rate of 3.1%. To be more precise, GDP growth amounted to 2.2% in developed countries and 4.2% in the Emerging Markets and Developing Economies group (EMDEs). Nevertheless, the significant devaluation of most commodities and the substantial losses observed in most asset classes in leading financial markets in the last quarter of 2018, are suggestive of an even more turbulent period ahead for the global economy.

OIL PRICE DYNAMICS IN 2018 - 2019 AND ITS REASONS

In contrast to 2017, 2018 oil prices were characterized by instability and contradictory trends. Throughout most of the year oil was on the rise and as a result, the price per barrel of BRENT crude increased from USD 62 to USD 85 by early October of 2018. Some of the reasons provided by experts to explain this trend are: the acceleration of growth in demand for oil, the decrease in the global reserves, the significant drop in oil production in countries such as Venezuela and Libya, as well as the re-imposition of sanctions against Iran. Yet, in October of 2018 the oil price unexpectedly started to plummet and lost about 30% of its value in the following two months. Though the factors behind this phenomenon are not entirely clear, experts cite the following reasons: diminishing expectations for the 2019 global economic growth, less than expected effects of the Iranian sanctions and certain political pressures recently inflicted on Saudi Arabia, the world's largest oil exporter. Though the decision taken at the December 7th, 2018 OPEC meeting to diminish the international cartel's cumulative production by about 1% managed to halt the downfall, opinions as to its long-term effectiveness differ. Overall, the annual price of BRENT crude in 2018 averaged USD 71.

Similarly, the price forecasts for 2019 significantly differ from one another. The International Monetary Fund (IMF) took a more conservative approach and predicted the price of BRENT crude per barrel to fall by 14% and average at USD 61 in the upcoming year, while the World Bank forecasted a more optimistic price of USD 68. The price forecasts made by various big banks and investment funds range from USD 60 to USD 72 for Brent and from USD 55 to USD 66 for WTI. However, contrary to widespread expectations, the full implementation of the Iranian sanctions and intensification of the Venezuelan crisis are not likely to raise the prices significantly. OPEC predicts a much higher growth of oil supply (2.10 million barrels per day) mainly as a result of the continued expansion of the US oil sector, compared to the weaker growth of demand (1.29 million barrels per day). At the same time, the majority of price risks are now on the downside: they include the prolongation of certain exemptions for the Iranian sanction regime and a potential global economic slowdown. Possible reasons for a potential price spike may come as a result of a decrease in investment observed in the industry in the recent year which may lead to a reduction in oil production. To summarize, it is not recommended to rely on a new price hike in 2019. The IMF experts at the same time expect the oil price to remain more or less stable at the level of USD 55-60.

Price per barrel of Brent in 2018 (USD)

Source: International Energy Agency

Although uncertainties may still prevail in the oil prices, the recent analyses convincingly show that dramatic appreciations (up to USD 90 -100) anticipated still several months ago cannot be sustainable as they may increase the probability of a new global crisis. For this reason, important actors in the oil market (OPEC and non-OPEC producers alike) are themselves interested in preventing this scenario. According to the calculations made by Merrill Lynch, in case the global growth falls to 2% instead of the forecasted 3%, there will be a big risk that oil price will fall dramatically to USD 35, in the worst-case scenario.

According to the WB, global economy is set to grow by 2.9% in 2019 (2.0% for the developed countries and 4.2% for EMDEs). The IMF, taking a more optimistic approach, forecasts the growth to constitute 3.5% (2.0% in the developed countries and 4.5% in EMDEs). The World Bank predicts a robust annual economic growth of 3.6% for Azerbaijan in 2019, and 3.3% in 2020.

National economy and SOFAZ. In accordance with its purposes and responsibilities, in 2018 SOFAZ maintained accumulation and management of the revenues stemming from the execution of the oil and gas contracts and secured macroeconomic and fiscal stability. Higher than forecasted average oil prices in the reference year helped to execute the SOFAZ's budget with proficit, as well as secure an increase in the SOFAZ's assets.

The implementation of the "regulated floating regime" of the manat by the Central Bank of the Republic of Azerbaijan (CBAR), helped to preserve the stability of the exchange rate in 2018. Price of 1 USD in terms of manat equaled 1.70 and remained almost unchanged throughout 2018. Average annual inflation rate strongly moderated since 2017 and constituted a mere 2.3%, as against 12.9% in 2017. The GDP of Azerbaijan rose to AZN 79 797.3 million in nominal figures, while its growth constituted 1.4% in real terms (0.1% in 2017 and -3.1% in 2016).

In 2018, the GDP per capita constituted AZN 8 126.2, having risen by 0.5% since the previous year. At the same time, the GDP per capita adjusted to purchasing power parity (PPP), as estimated by the IMF, grew by 0.1% and amounted to USD 18 075.9.

The nominal income of the population rose by 9.2%, compared to 2017, reaching AZN 53 688.6 million. The income per capita increased by 8.2% and equaled AZN 5 467.4, whereas the average nominal monthly salary rose by 2.9%* up to AZN 540.1*.

After all mandatory and voluntary disbursements, the overall disposable income of the population amounted to AZN 49 595.5 million, or in nominal terms 9.4% higher than in 2017. The 58.5% of the country's GDP fell into the share of non-oil sector.

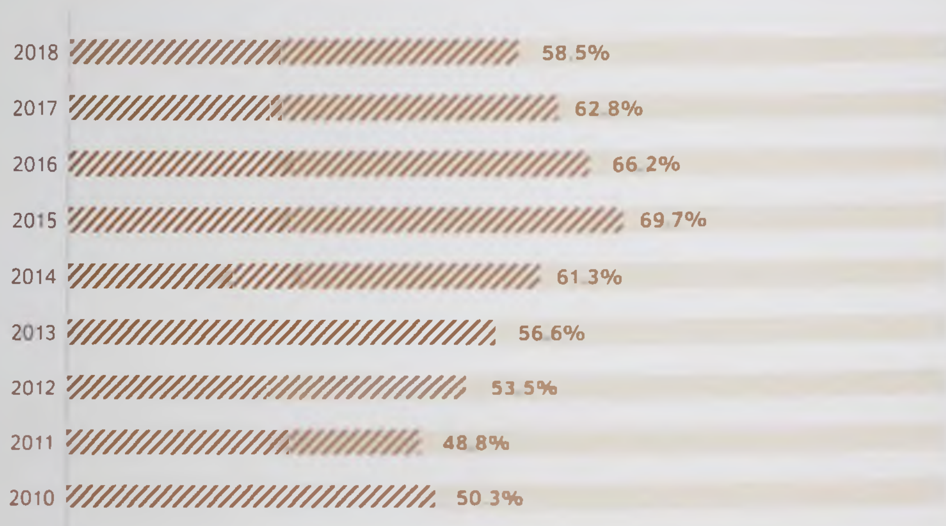
*January-November 2018

Chart 4.1.1. GDP per capita adjusted to purchasing power parity (in current international dollars)

Source: IMF

The structure of the GDP, which in 2018 totalled 79 797.3 million AZN, was as follows: 57.4% fell into the share of the production of goods, 34.8% - to services, while net taxes on goods and imports accounted for the remaining 7.8% Compared to 2017, the production of value-added in the non-oil sector increased by 1.8% in real terms, while the respective indicator for the oil sector equaled 0.6%.

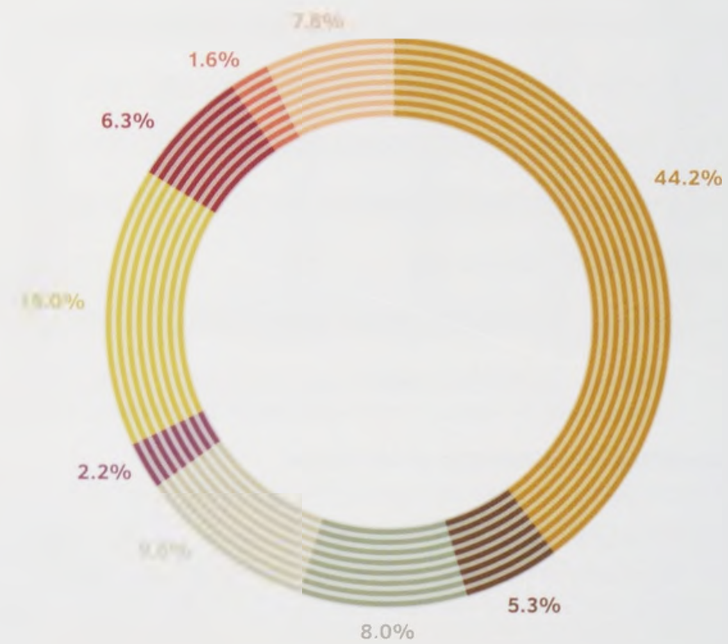
Chart 4.1.2. The share of non-oil sector in the country's GDP



Source: The State Statistical Committee of the Republic of Azerbaijan

In the reference year, industrial sector continued to play a leading in the Azerbaijani economy, its share in the GDP amounted to 44.2%. At the same time, the service sector preserved its relatively stable dynamics.

Chart 4.1.3. The GDP structure

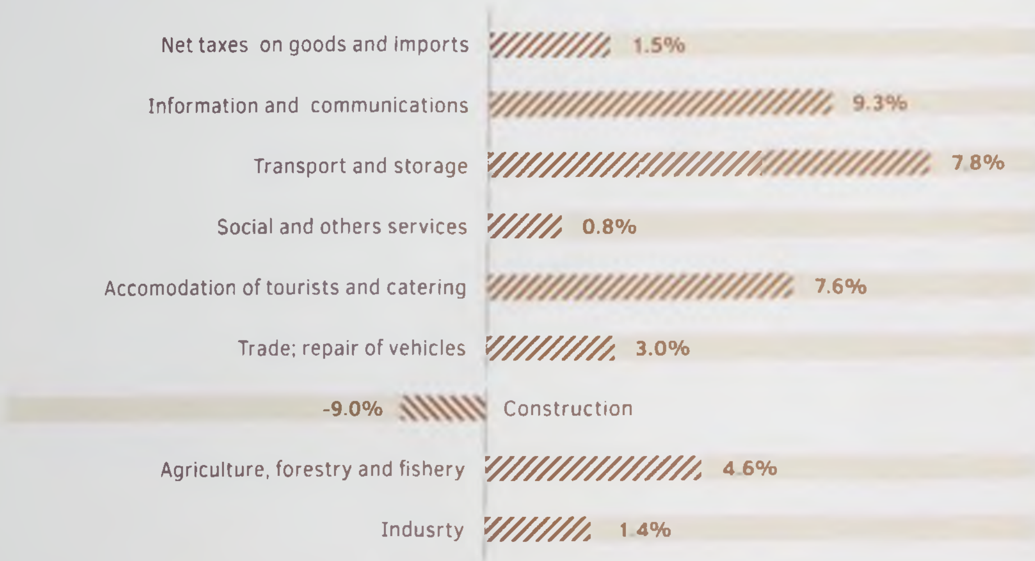


- Industry - 44.2%
- Agriculture, forestry and fishery - 5.3%
- Construction- 8.0%
- Trade; repair of vehicles - 9.6%
- Accomodation of tourists and catering - 2.2%
- Social and other services - 15.0%
- Transportation and storage - 6.3%
- Information and communications - 1.6%
- Net taxes on goods and imports - 7.8%

Source: The State Statistical Committee of the Republic of Azerbaijan

In 2018, real growth was registered in most sectors of the Azerbaijani economy. Progress in such spheres as information and communications (9.3%), tourism and catering (7.6%), and agriculture (4.6%) deserves special attention, since they were prioritized as drivers of economic development. The spectacular growth of the non-oil industry (8.5%) achieved against the backdrop of the recent years' reforms is also worth noting.

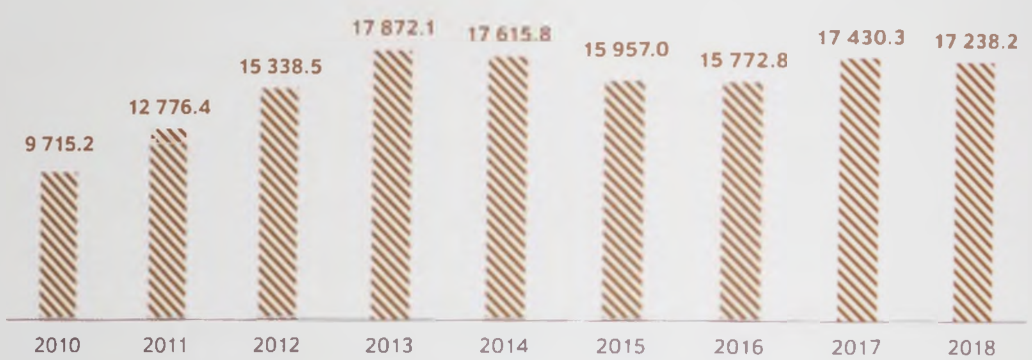
Chart 4.1.4. **Sectoral growth rates**



Source: The State Statistical Committee of the Republic of Azerbaijan

In the reference year the amount of capital investment declined by 4.4% in real terms, compared to the 2017 figures, and totalled AZN 17 238.2 million. The shares of domestic and foreign investment in this total were 69.7% and 30.3%, respectively, and 68.0% of this amount was spent on the execution of construction and installation works.

Chart 4.1.5. **Dynamics of capital investment made in Azerbaijan (million AZN)**



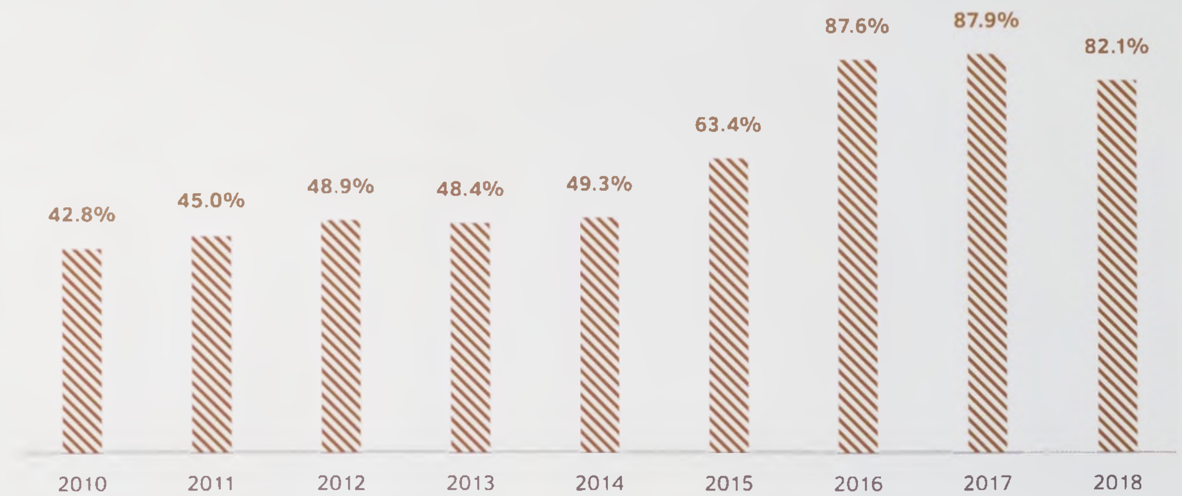
Source: The Ministry of Economy of the Republic of Azerbaijan

STRATEGIC CURRENCY RESERVES

By December 31, 2018, the country's strategic currency reserves (SOFAZ and CBAR combined) reached USD 44 140.9 million, having risen by USD 3 billion, or approximately 10%, compared to the previous year. 87.3% of these reserves fall into the share of the SOFAZ's assets.

The ratio of the SOFAZ's assets by the end-year to the GDP of Azerbaijan constituted 82.1%.

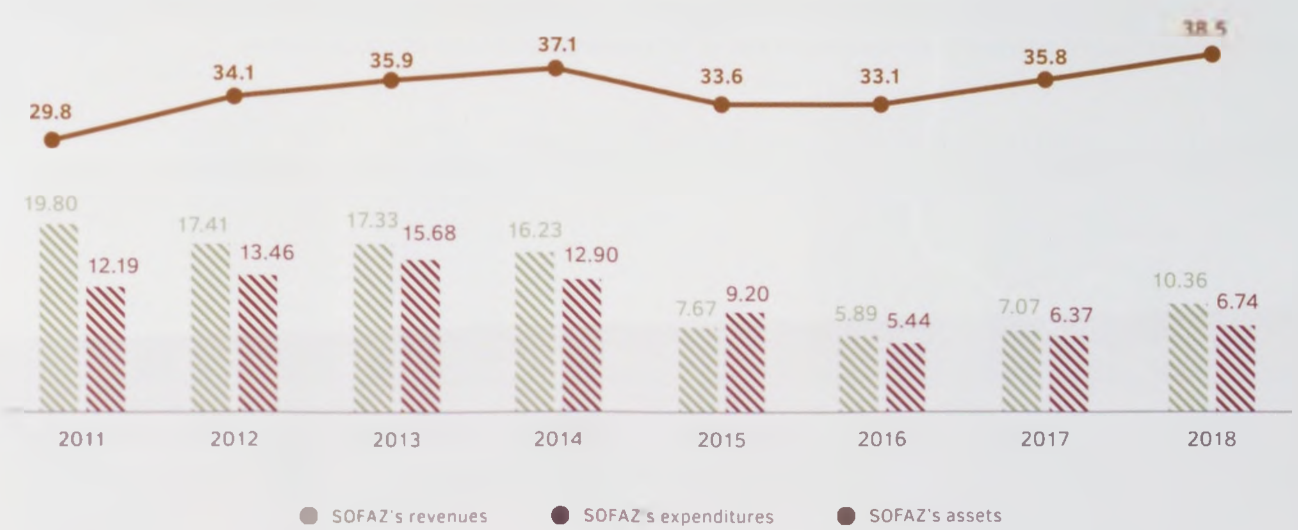
Chart 4.1.6. **SOFAZ assets-to-GDP ratio**



Sources: SOFAZ, The State Statistical Committee of the Republic of Azerbaijan

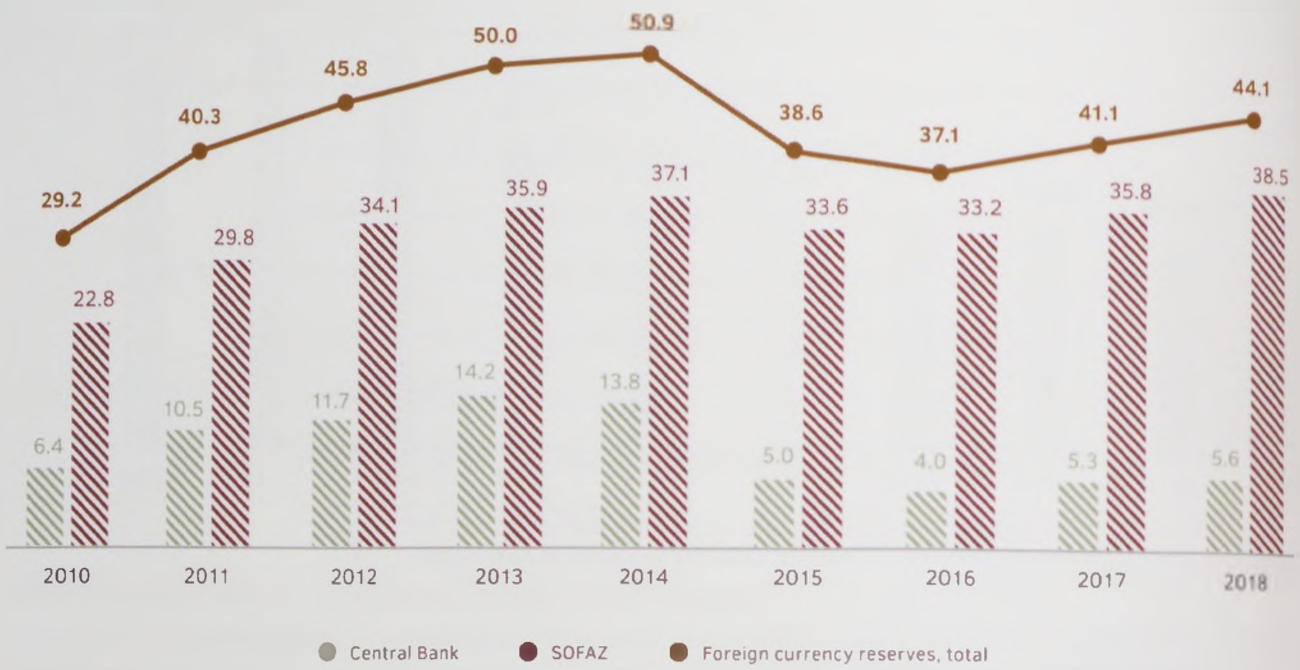
Against the background of rising oil prices, SOFAZ's assets underwent a significant growth during 2018. To put it in a context, after the dramatic decline of global oil prices SOFAZ's revenues equaled only USD 5.9 billion in 2016, as against USD 16.2 billion in 2014. This trend also resulted in the decrease of the SOFAZ's assets, which fell from the then-peak level of USD 37.10 billion at the end of 2014 to USD 33.15 billion in 2016. As the average annual price per barrel reached USD 71, SOFAZ's annual revenues equaled USD 10.36 billion, and the overall assets constituted USD 38.5 billion in 2018.

Chart 4.1.7. **SOFAZ's revenues, expenditures, and assets (USD billion)**



At the same time, official currency reserves of CBAR in 2018 rose by approximately USD 291.1 million (5.5%) to achieve the level of USD 5 625.7 million.

Chart 4.1.8. **Foreign exchange reserves of the Republic of Azerbaijan (billion USD)**



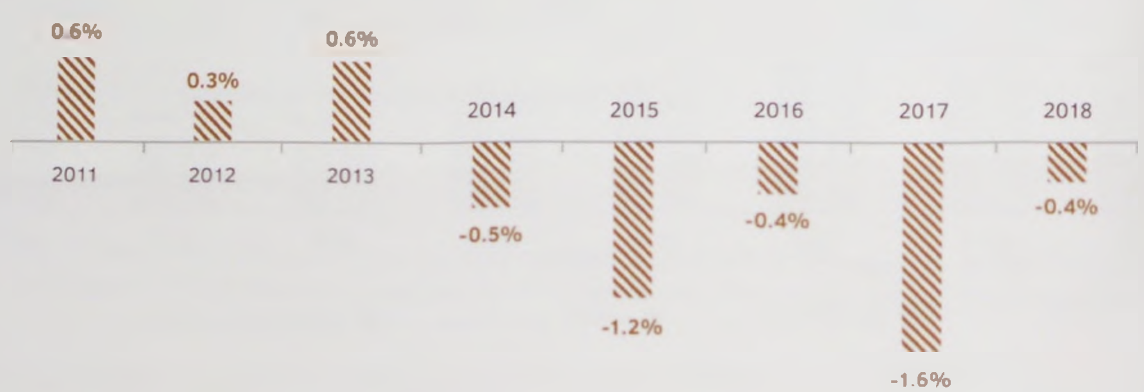
Sources: SOFAZ, CBAR

SECURING FISCAL SUSTAINABILITY

In 2018, SOFAZ played a big role in preserving fiscal balance in Azerbaijan Thus, AZN 10.9 billion, or 48.9% of the state budgetary revenues were formed out of the transfer from SOFAZ. By providing timely payments to the state budget regardless of oil prices and absorbing external economic shocks during the period of low oil prices, SOFAZ has managed to secure fiscal stability. The accumulation of reserves in SOFAZ has also positively contributed to financial stability and falling public debt levels.

Revenues and expenditures of the state budget amounted to AZN 22 411.3 million and AZN 22 718.9 million, respectively, and the state budget deficit in 2018 totalled -0.4% of the country's GDP (AZN 79 797.3 million).

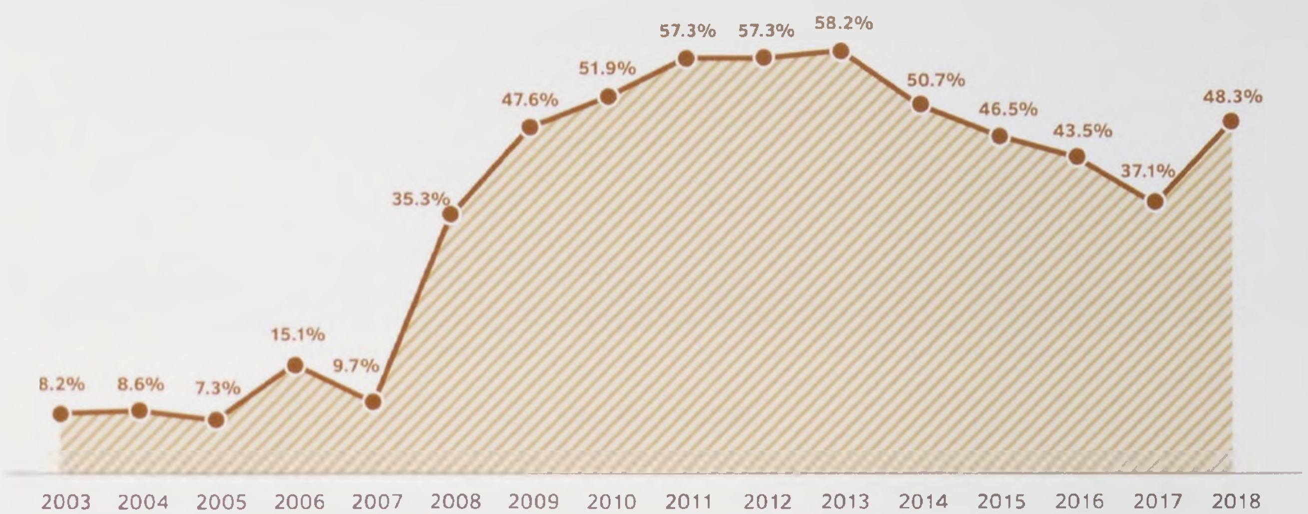
Chart 4.1.9. **State budget deficit/proficit in 2011-2018 (share of GDP)**



Source: CBAR

During the period from 2003 to 2018, the cumulative transfer from SOFAZ to the state budget has reached AZN 88.6 billion.

Chart 4.1.10. **Share of SOFAZ's transfers in the state budget revenues**

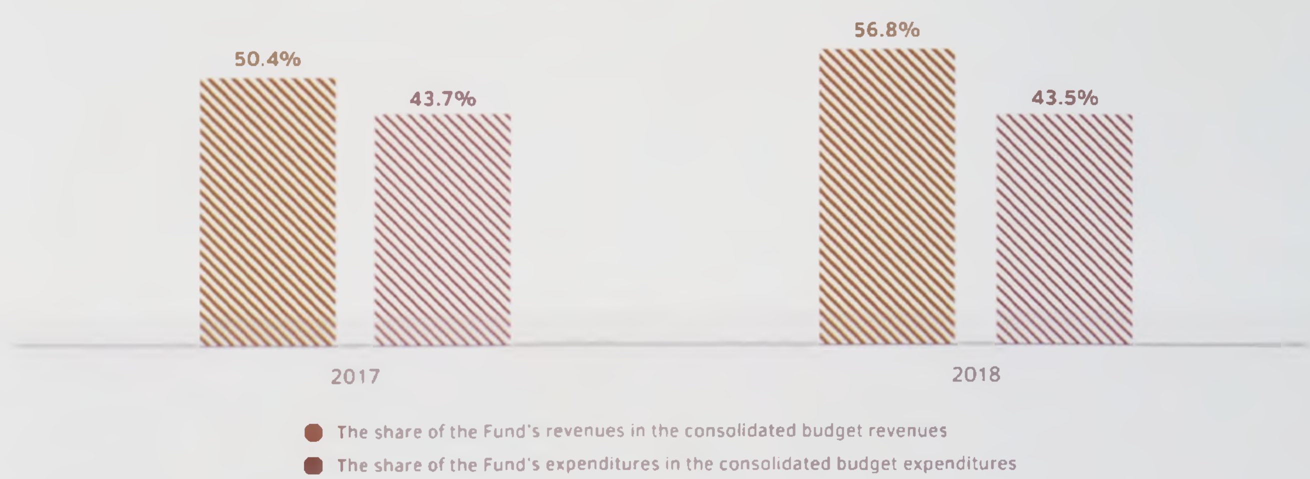


Source: SOFAZ, CBAR

The average annual price of profit oil being USD 71, contrary to the projected level of USD 55, made it possible for SOFAZ's overall revenues in 2018 to exceed the level confirmed in the budget plan by 15.0%, and for the oil revenues by 25.1%. During the years of 2001-2018, the inflows to the Fund constituted USD 148.2 billion, while approximately 38.5 billion (26%) thereof has been channeled into saving.

Consolidated budget deficit when excluding SOFAZ. Apart from the state budget, budgetary revenues and expenditures of SOFAZ comprised a considerable part of the consolidated budget revenues and expenditures in 2018. According to the Ministry of Finance of the Republic of Azerbaijan, revenues and expenditures of the consolidated budget in 2018 amounted to AZN 31 034.7 million and AZN 26 334.4 million, respectively. Out of these, 56.8% of the revenues and 43.5% of the expenditures came from SOFAZ's budget.

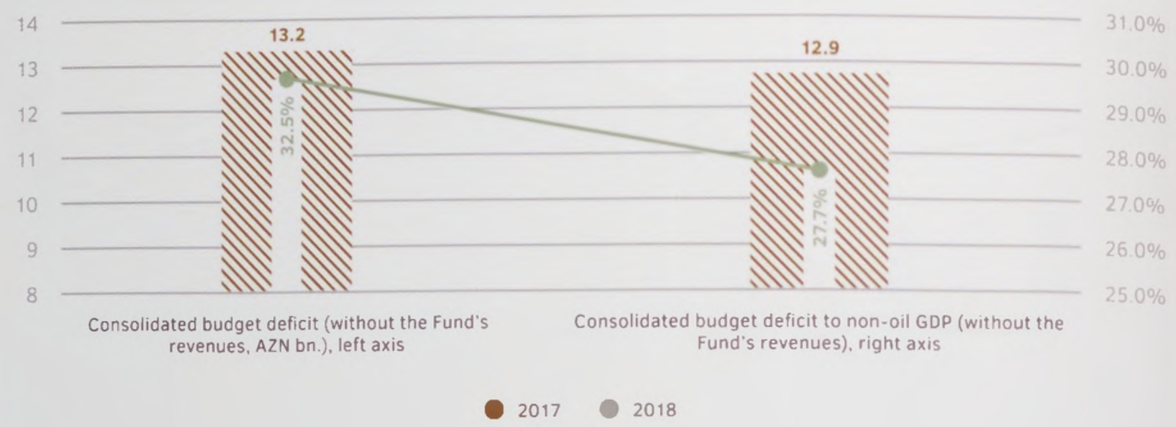
Chart 4.1.11. **The share of Oil Fund's revenues and expenditures in the consolidated budget**



Sources: SOFAZ and Ministry of Finance of the Republic of Azerbaijan

At the same time, when excluding SOFAZ's revenues, the consolidated budget deficit in the reference year equaled AZN 12.9 billion, which amounted to 16.2% of the GDP and 27.7% of the non-oil GDP.

Chart 4.1.12. Consolidated budget deficit without SOFAZ's revenues



Sources: SOFAZ, The Ministry of Finance and The State Statistical Committee of the Republic of Azerbaijan

Optimal policy frameworks for resource-rich countries

The sharp decline in the prices of oil and most other commodities that occurred between 2014 and 2015 revealed well-known fragilities and deficiencies in the structure of the economois of resource-rich countries'. Rising attention to environmental problems caused by hydrocarbons and expectations of their pending replacement by renewable energy sources brought about a notion of "stranded assets". It incentivizes extracting as much oil and gas as possible right now so as not to be left with unsellable resources in the ground. Bearing in mind that most resource-rich countries are developing ones, the goals of raising living standards and dire infrastructure needs incentivize spending without delay, instead of saving the bulk of revenues for the future. Hence, building a proper policy strategy is not an easy challenge for these countries. There are, however, several crucial principles on which most experts agree.

First of all, although the transition to renewables is not expected in the near future, it is an unescapable reality that has to be prepared for starting today. There are important signs. For example, since 2013, the World Bank has decided not to finance new coal projects "except in rare circumstances", and has also been decreasing its investment in oil and gas projects. Long-term investors, including pension funds and sovereign wealth funds, are cutting down on the shares of oil and gas assets in their portfolios. The Norges Bank, which governs the USD 1 trillion Norway Pension Fund, diverted USD 35 billion of its oil and gas assets to other sectors, while the New York Pension Fund pledged to do the same in 2018. Emissions regulation, fuel subsidy reforms, and new technologies will affect the prospects for new and prospective exporters. It is expected that oil demand will fade in the long term, and a mix of electricity, hydrogen, and biofuels could become the dominant energy sources in transportation. To prepare for these changes, most big industrial countries have already adopted energy sustainability targets: the US vowed to reduce GHG emissions 26–28% below 2005 levels by 2025, while China and India pledged to reduce carbon intensity respectively by 65% and 35% from 2005 levels, by 2030. Also, China plans to increase the share of non-fossil primary energy to 20% of its energy mix by that time. Moreover, many countries and cities are planning greater restrictions on fuel types or measures to enforce environmental performance (for example, restrictions on high-sulphur fuel, or carbon content).

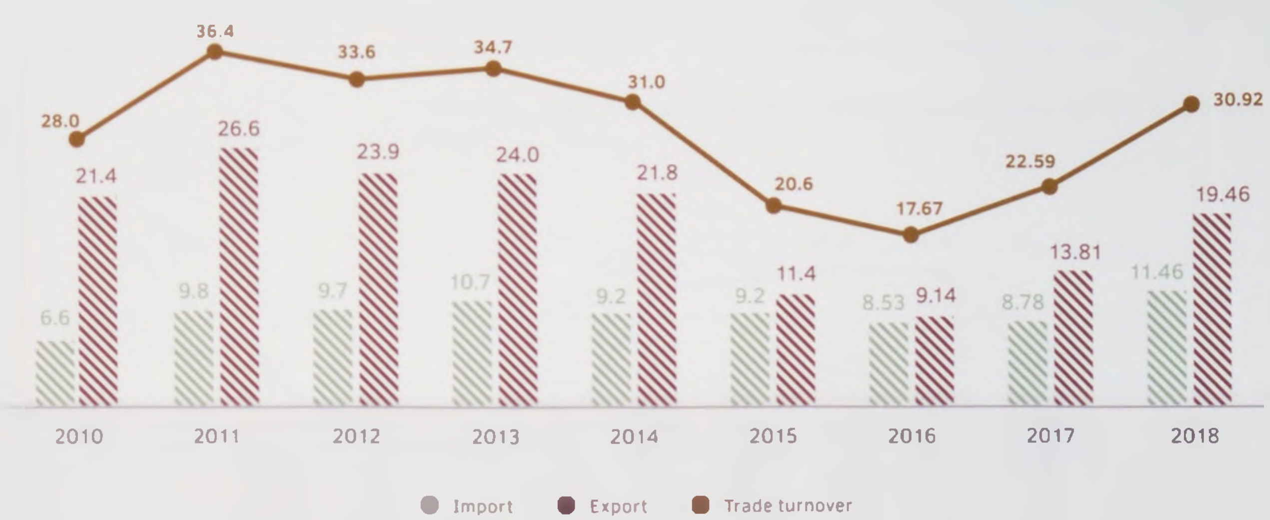
Development strategies for extractive-rich low-income countries should prioritize national goals for sustainable economic diversification, above all. In order to enable maximum benefits from the resource revenues within a limited time horizon, they should place a strong emphasis on industrial planning, investment in resilient infrastructure, and

efficient administration practices within national oil companies. The notion of "good enough governance" which is in line with the country's peculiarities, should prevail over "ideal policy recipes". According to the outcomes of different studies, the success of development policies in resource-rich countries is largely determined by the quality of governing institutions. Another significant recent trend is a focus on enhancing the accountability of public and private oil companies through regulatory processes combating corruption (e.g. the Foreign Corrupt Practices Act of the US), their accounting disclosure obligations (e.g. EU Transparency and Accounting Directives), their commitment to abide by codes of conduct and due diligence principles (e.g. OECD guidelines).

FOREIGN TRADE

According to the State Customs Committee of the Republic of Azerbaijan, the country's foreign trade turnover in the reference year amounted to USD 30.92 billion, the exports and imports constituting USD 19.46 billion and USD 11.46 billion, respectively. In 2018, an increase in the volume of foreign trade turnover by 36.9%, compared to the relevant indicator of the previous year, was observed, while exports rose by 40.9% and the imports increased by 30.5%.

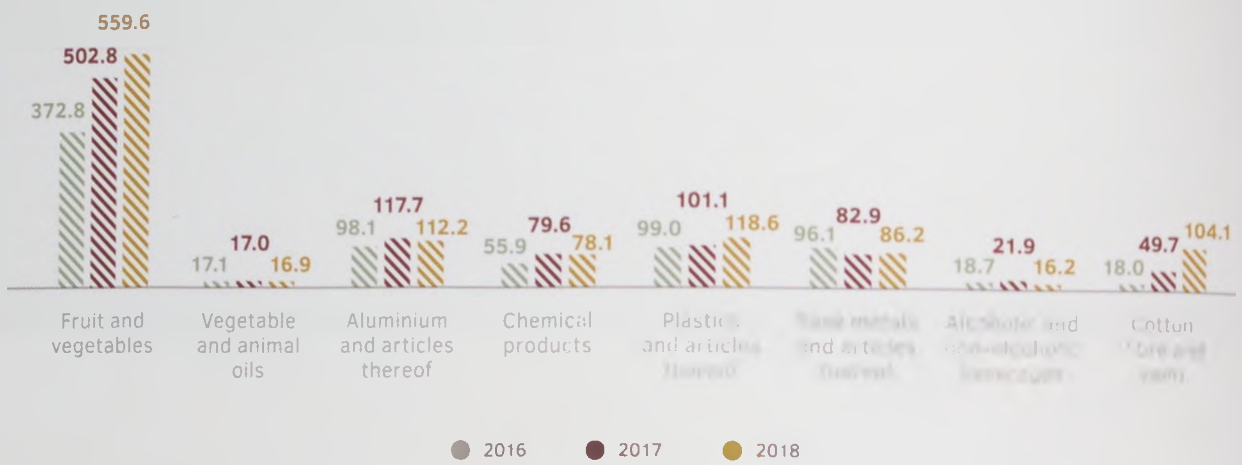
Chart 4.1.13. Foreign trade turnover (USD billion)



Source: The State Customs Committee of the Republic of Azerbaijan

Non-oil sector export. In 2018, non-oil export mainly consisted of fruit and vegetables, plastics, aluminium, base metals and items made of them, cotton, and chemical products. As the Chart 4.1.14. shows, a sufficient increase in such export items as fruit, vegetables and cotton was observed, while some other items experienced a decrease in export volumes.

Chart 4.1.14. **Major non-oil goods export (USD million)**

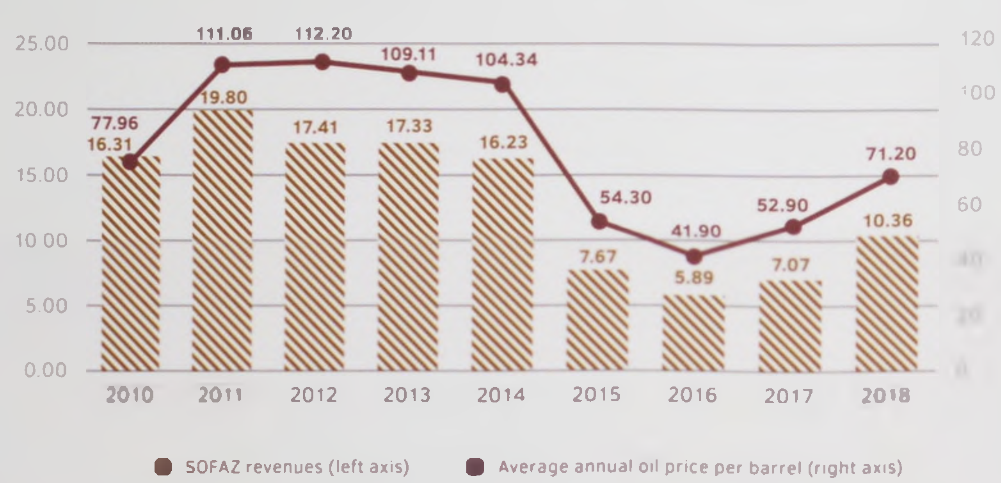


Source: The State Customs Committee of the Republic of Azerbaijan

4.2. SOFAZ'S REVENUES

In 2018, relatively higher oil prices meant SOFAZ's budget experienced higher revenues obtained from the sales of the Republic of Azerbaijan's share of hydrocarbons. Although the average annual price of a barrel of crude oil was projected at the level of USD 55 per barrel, it amounted to USD 71 per barrel in 2018. In the reference year, the sources of SOFAZ's budget revenues included proceeds from the sales of the Republic of Azerbaijan's share of hydrocarbons, bonus payments, acreage fees, the fees paid to the Republic of Azerbaijan for the transit of oil and gas through its territory, and revenues from the management of SOFAZ's assets. By the end of 2018, the overall revenues from these sources recorded a total of AZN 17 614.1 million, or USD 10 361.0 million. In 2018, SOFAZ's revenues increased by 46.6% in dollar terms, compared to the previous year's results (USD 7 065.5 million).

Chart 4.2.1. **SOFAZ revenues (in USD billion) and oil price (in USD)**



Proceeds from the sales of profit oil and gas. In 2018, the amount of AZN 16 645.6 million or USD 9 791.4 million entered SOFAZ's budget from the sales of profit oil and gas.

Chart 4.2.2. **SOFAZ's revenues in 2018 (USD million)**

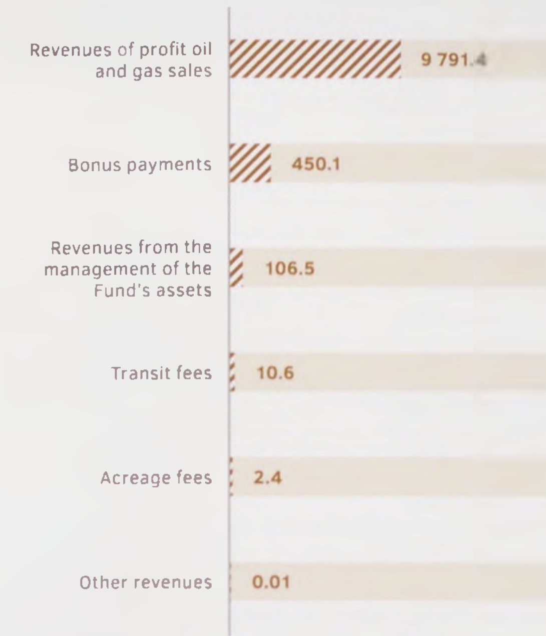
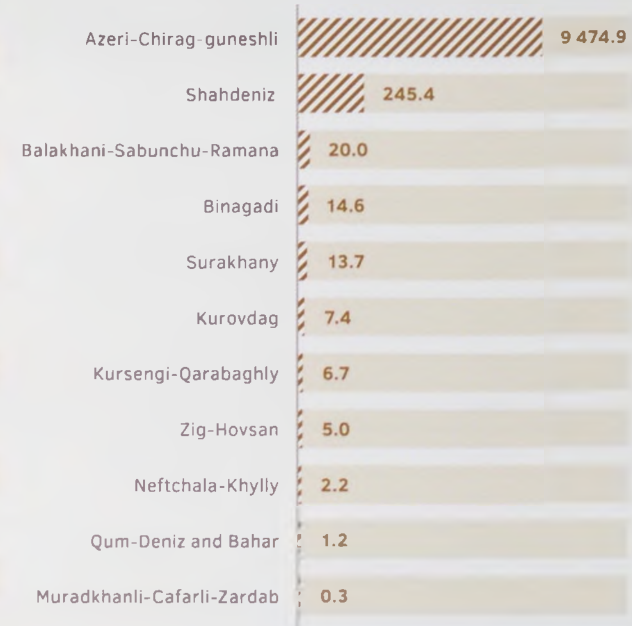


Chart 4.2.3. **Revenues from profit oil and gas sales in 2018 (USD million)**



Revenues from the asset management. In accordance with SOFAZ's investment policy for 2018, assets were invested in fixed income (debt and money market instruments), equities, real estate, and gold. SOFAZ's revenues from asset management totaled USD 106.5 million, or AZN 181.1 million. The annual rate of return from the SOFAZ's investment portfolio amounted to 0.35%.

Transit fees. In 2018, another revenue inflow was generated from the transportation of oil and gas through the territory of Azerbaijan (transit fees). The amount of transit fees transferred to the SOFAZ's budget constituted USD 10.6 million, or AZN 18.1 million. Detailed information on this revenue item is provided in the Table 4.2.1.

Table 4.2.1. **SOFAZ's proceeds from transit fees in 2018**

Transferor	Date	Amount, million	
		USD	AZN
AIOC	12.01.2018	1.031	1.75
AIOC	14.02.2018	1.035	1.76
AIOC	13.03.2018	0.934	1.59
AIOC	12.04.2018	1.045	1.77
AIOC	14.05.2018	1.045	1.78
AIOC	13.06.2018	1.086	1.84
AIOC	12.07.2018	1.030	1.75
AIOC	13.08.2018	0.369	0.63
AIOC	12.09.2018	0.754	1.28
AIOC	12.10.2018	0.651	1.11
AIOC	14.11.2018	0.623	1.06
AIOC	12.12.2018	1.045	1.78
Total		**10.65**	**18.10**

Revenues related to acreage fees. In 2018, a sum of USD 2.4 million (AZN 4.1 million) of acreage fees was transferred to SOFAZ in accordance with the offshore exploration and production sharing agreement between SOCAR and the oil company co-owned by SOCAR and BP Exploration (Caspian Sea) over the Shafag-Asiman field in the Azerbaijani sector of the Caspian. Acreage fees per company are represented in the Table 4.2.2.

Table 4.2.2. **Proceeds from acreage fees in 2018**

Transferor	Oil field	Date	Amount, million	
			USD	AZN
BP Exploration (Caspian Sea) Limited	Shallow watered area around Absheron Peninsula	25.04.2018	0.3	0.5
BP Exploration (Caspian Sea) Limited	Shafag-Asiman	05.07.2018	2.1	3.6
Total			**2.4**	**4.1**

Bonus payments. In the reference year, SOFAZ's revenues from bonuses paid by investors for signing and fulfilling oil and gas contracts amounted to AZN 765.2 million, or USD 450.1 million. Bonus payment inflows are represented in the Table 4.2.3.

Table 4.2.3. **SOFAZ's proceeds from bonus payments in 2018**

Transferor	Oil field	Date	Amount, million	
			USD	AZN
NICO	Shah Deniz	22.01.2018	0.01	0.02
BP Exploration (Caspian Sea) Limited*	Azeri-Chirag-Gunashli	29.01.2018	450.00	765.05
BP Exploration (Caspian Sea) Limited	Shah Deniz	29.01.2018	0.04	0.06
Petronas	Shah Deniz	29.01.2018	0.02	0.03
Turkish Petroleum Overseas Company Limited	Shah Deniz	30.01.2018	0.02	0.04
Lukoil Overseas Shah Deniz Limited	Shah Deniz	30.01.2018	0.01	0.02
Total			**450.1**	**765.2**

**Acting on behalf of all the contractors as an Operating Company*

Other revenues. At the same time, AZN 20 000 was transfered to SOFAZ from the sale of assets issued by investors under oil and gas agreements.

4.3. SOFAZ'S EXPENDITURES

In 2018, SOFAZ's expenditures were equal to AZN 11 455.6 million (USD 6 738.6 million). 95.7% of the total expenditures accrued to the annual transfer to the state budget, 4.1% fell into the share of the projects and state programs financed from the SOFAZ's budget, while the SOFAZ's administrative expenses constituted the remaining 0.2% of the total. The breakdown of SOFAZ's expenditures is provided in the Chart 4.3.1. and Chart 4.3.2.

Chart 4.3.1. **Structure of the SOFAZ's expenditures in 2018**

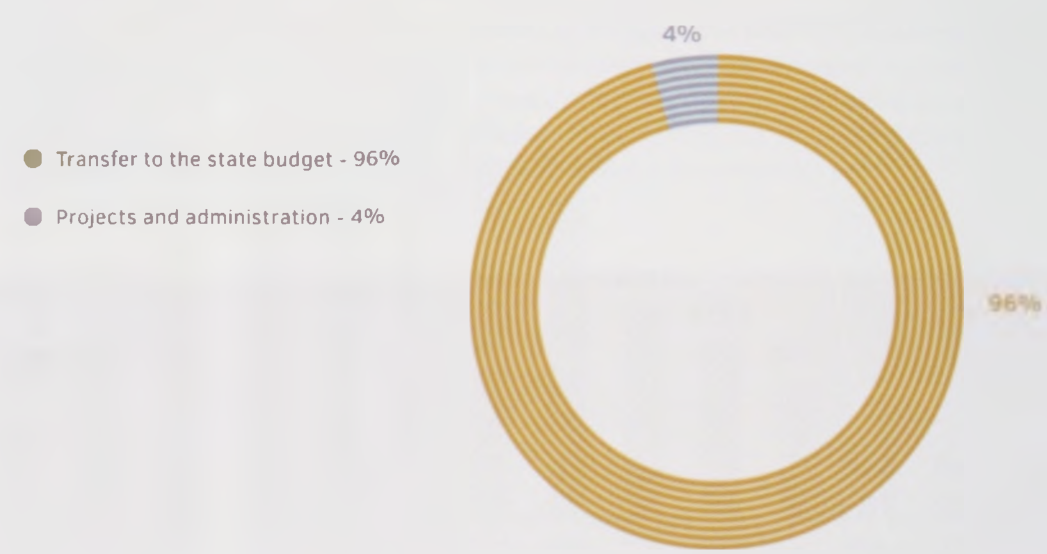
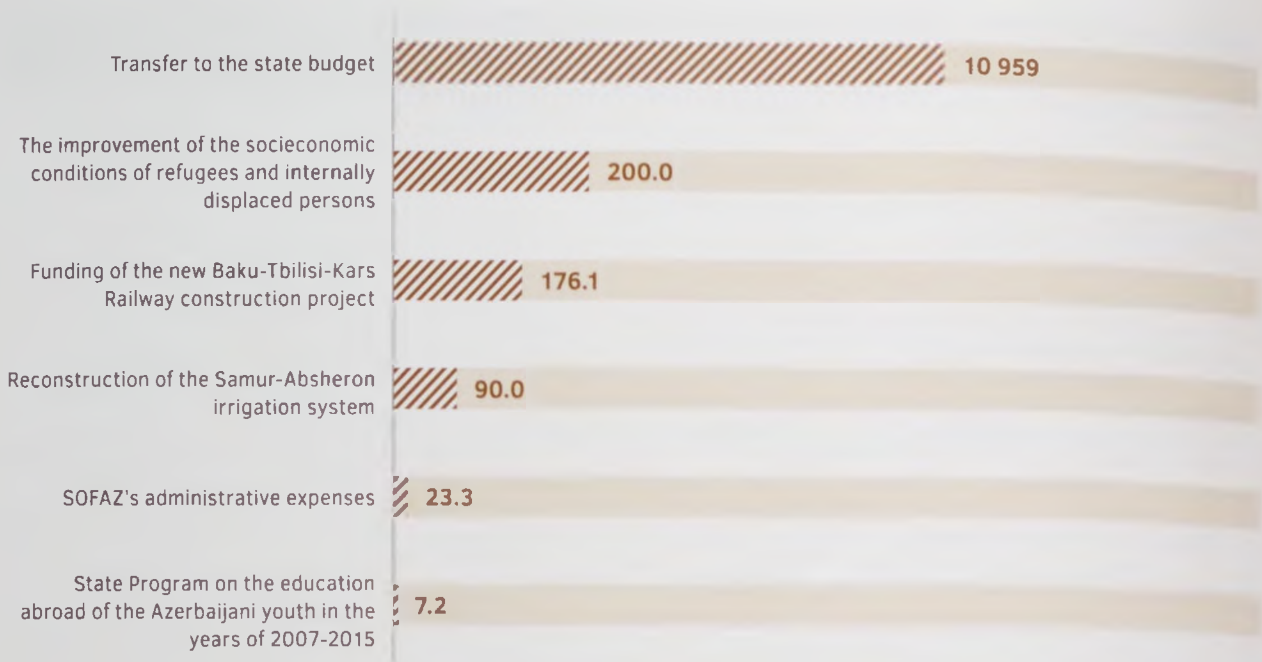


Chart 4.3.2. Structure of the SOFAZ's expenditures in 2018, AZN million



Transfer to the state budget. In the reference year, the amount of transfer to the state budget constituted AZN 10 959.0 million which amounted to 48.9% and 48.2% of the state budget revenues and expenditures, respectively.

Throughout the years 2003-2018, the overall transfer from SOFAZ to the state budget amounted to AZN 88.6 billion or USD 93 billion which is 86.9% of all SOFAZ's budgetary expenditures (AZN 102.0 billion) this far. Transfers to the state budget by years and transfers from SOFAZ as a share of the state budget revenues and expenditures in 2001-2018 are represented in the Charts 4.3.3, 4.3.4 and 4.3.5.

Chart 4.3.3. Transfer to the state budget by years (AZN million)

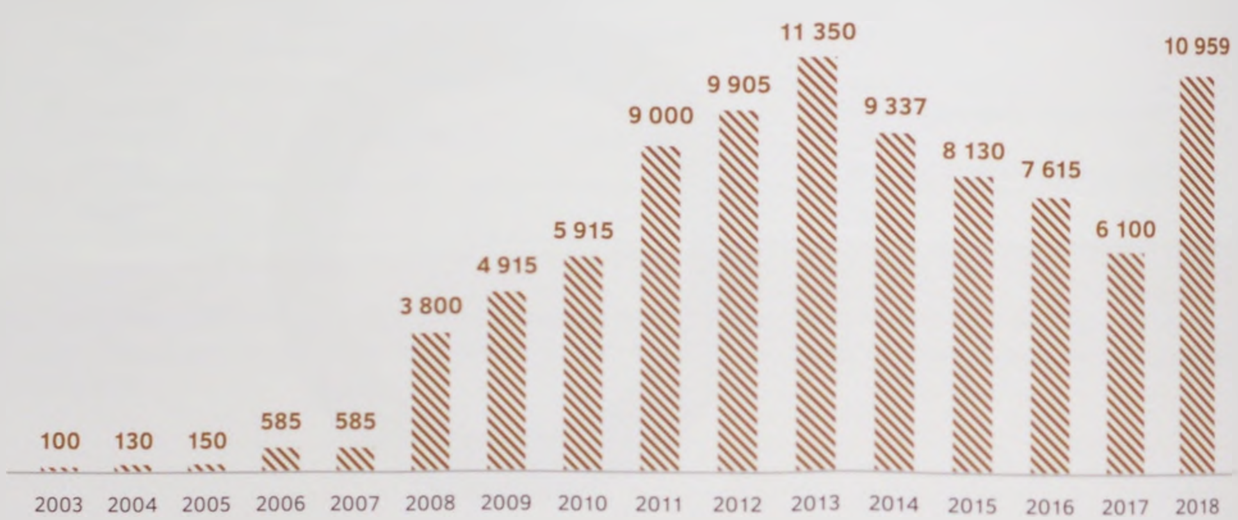


Chart 4.3.4. Transfer from SOFAZ as a share of the state budget revenues

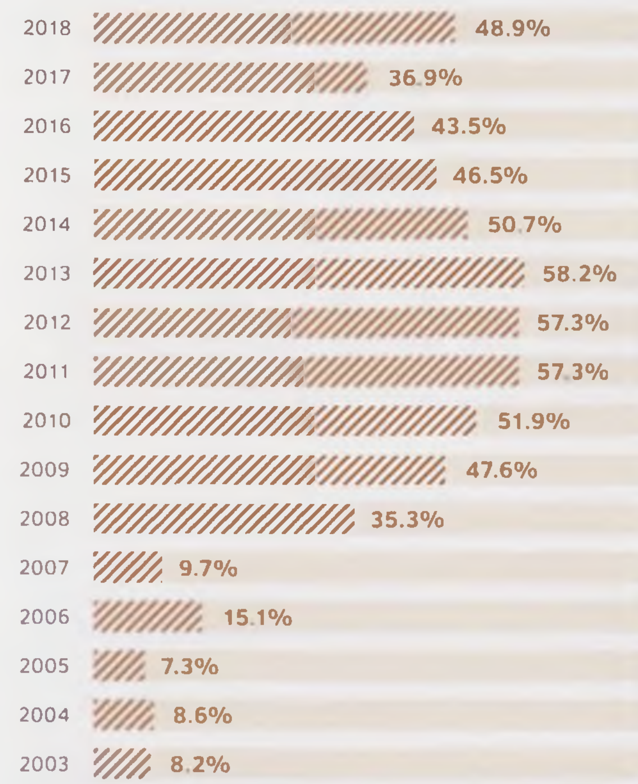
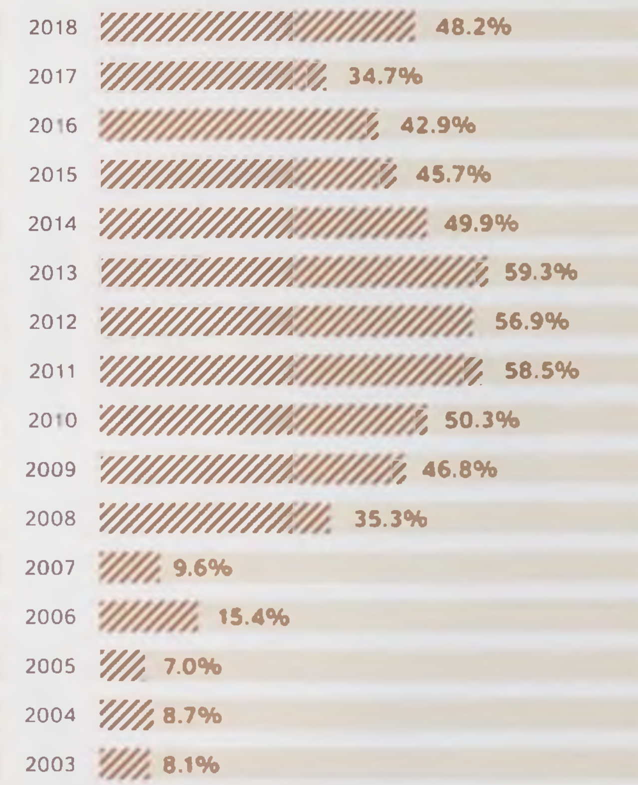


Chart 4.3.5. Transfer from SOFAZ as a share of the state budget expenditures



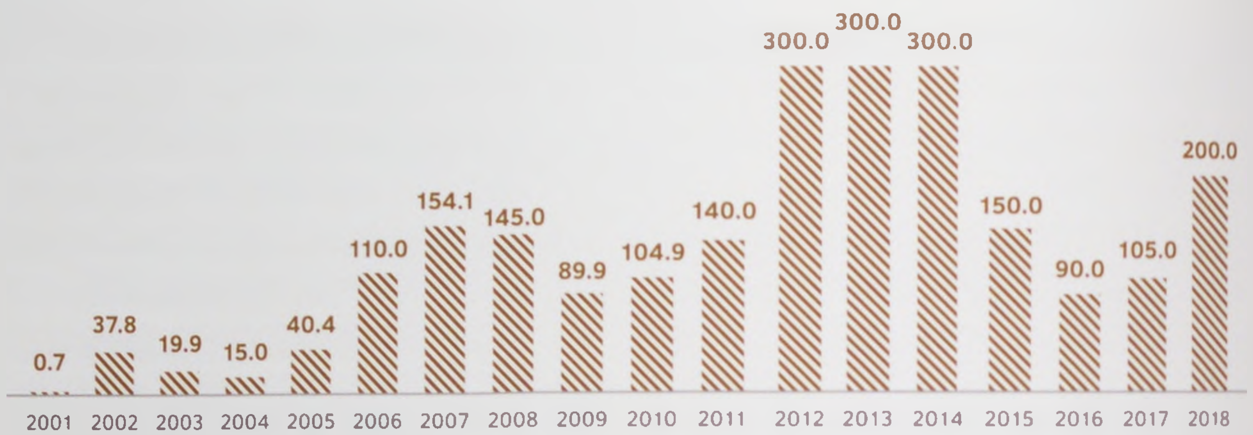
Sources: CBAR and SSC

FINANCING SOCIAL AND INFRASTRUCTURE PROJECTS

SOFAZ plays a significant role in the country's development thanks to its annual transfer to the state budget as well as financing social and infrastructural projects of strategic national importance.

The improvement of the socioeconomic conditions of refugees and internally displaced persons. The sponsoring of "The State Program on the improvement of the socioeconomic conditions of refugees and internally displaced persons" by SOFAZ continued in 2018 as well. Overall, AZN 2 302.7 million has been spent on this program since 2001 (Chart 4.3.6). More specifically, the amount allocated to the improvement of the socioeconomic conditions of refugees and internally displaced persons constituted AZN 200 million in the reference year.

Chart 4.3.6. Expenditures on the improvement fo the socio-economic conditions of refugees and internally displaced persons by year (AZN million)



The aforementioned funds were allocated for the construction of 71 residential districts of private houses, 17 residential blocks with multi-storeyed buildings that in total allow for the settlement of 33 781 families, as well as a large number of socio-infrastructural objects. In 2018, 2 residential blocks were build and 1 301 families were settled. In addition, 1 school, 2 kindergartens, 2 medical centres, 2 community centres, 2 administrative buildings, 1 communication junction, 4 water reservoirs, 4 pumping stations, 6 high voltage electric transformers, 1 electric sub-station, 6 km of highways, 15.9 km of water pipelines, 40.9 km of transmission lines, 5.1 km of gas pipelines, 9.1 km of sewerage lines were built and completed within the framework of the program in 2018.

All these measures provided opportunities for improving socio-economic conditions of the refugees and internally displaced persons and reduction of poverty rate among them from 75% in 2003 to 12% in 2017. Respective rate countrywise fell from 44.7% in 2003 to 5.9% in 2017.

DEVELOPMENT OF HUMAN CAPITAL

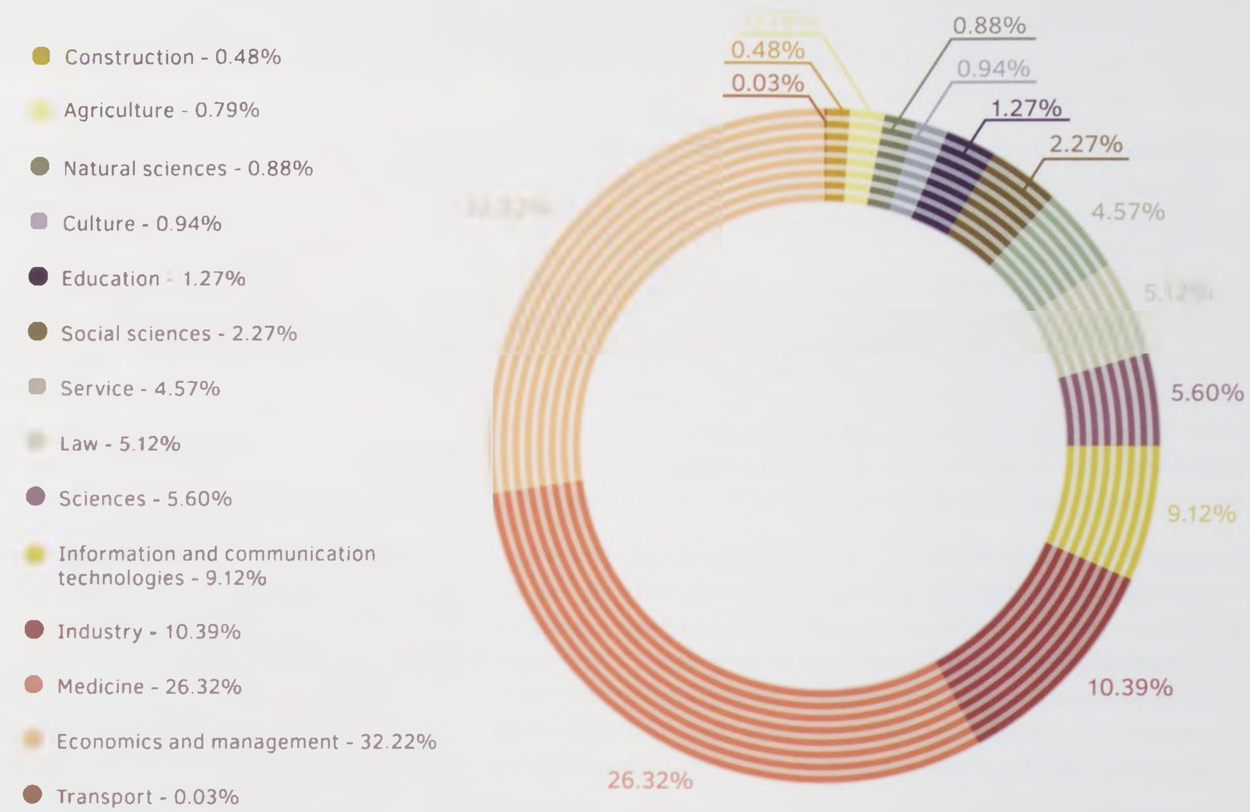
Financing the "State Program on Education of Azerbaijani Youth abroad in the years 2007-2015". SOFAZ finances the "State Program on Education of Azerbaijani Youth Abroad in the years 2007-2015" that aims at fulfilling the idea of transforming black gold into human capital. Out of AZN 7.2 million allocated by SOFAZ for the education program in 2018, AZN 3.43 million went to covering the living expenses, AZN 3.36 million to paying tuition fees, approximately AZN 266.89 thousand to paying transport expenses. AZN 100 thousand were spent on medical insurance, while AZN 73.91 thousand - on visa and registration fees and some other expenses.

By 31 December 2018, SOFAZ had financed the education of 3 454 students within the framework of the State Program, 1 913 of whom have already graduated. 79.0% of the students have been funded to study at undergraduate or graduate levels. More precisely, 1 180 studied at bachelor, 1 430 - at master's degrees. Moreover, the Program has also financed 692 students pursuing doctoral or higher medical studies. Most of the undergraduate level students studied economics and management (320 students), medicine (238 students), industry (191 students), information and communication technologies (174 students). At the graduate level, economics and management were mostly prioritized (722 people), followed by industry (138 students) and law (120 students). The majority of the program participants studied in Great Britain (29.1%), followed by Turkey (22.1%), Germany (12.4%) Canada (7.2%), Netherlands (5.2%), and Russia (3.8%). For the purposes of financing the State Program, SOFAZ has allocated AZN 212.7 million during the period of 2008-2018.

A praiseworthy fact is that 95% of the graduates are employed according to the profession they acquired, which is a sign of a correct allocation of the professions. Some of the former students teach at the leading universities of Azerbaijan or share their knowledge via various online course platforms, which enables them to further spread their knowledge gained while studying abroad and multiply the Program effects making them long-lasting and sustainable. While admission of students to the Program ended in 2016, 1 387 participants are still to graduate. The last graduates are projected to study abroad until 2021.

The division of the Program participants according to the study areas is given in the Chart 4.3.7.

Chart 4.3.7. Distribution of the students by study areas



Funding of the new Baku-Tbilisi-Kars Railway construction project. The main purpose of the project is to consolidate the Trans-European and Trans-Asian railway networks, and ensure efficient transportation of cargo and passengers between Europe and Asia by building a railway line that would pass through Azerbaijan, Georgia, and Turkey. The project envisages building a Kars-Akhalkalaki railway line, 76 km of which will pass through Turkey and 26 km through Georgia, as well as restoring and rebuilding 160 km of Georgia's Marabda-Akhalkalaki railway.

SOFAZ has been chosen to finance the reconstruction of the current Marabda-Akhalkalaki railway line and construction of new railway line from Akhalkalaki to Turkey border by the Decree № 1 974 of President of AR on 21 February 2007.

In 2018, SOFAZ allocated USD 103.6 million (AZN 176.1 million) to finance this project to the respective account of the Transport, Communication and High Technologies of AR (Lender) and was executed at the level of 100%, compared to the Fund's project budget of the same year. It should be noted that the Agreement Protocol has been signed between the Ministry of Finance of the Republic of Azerbaijan, Lender, International Bank of Azerbaijan OJSC (the Bank) and SOFAZ on the one-off payment of the unused part of the funds intended to be directed from SOFAZ to the project financing in 2018. Under the Protocol, those residuals on the project have been transferred to the respective account of the Lender by SOFAZ, and then to the specially created escrow account of the Lender at the Bank. Those transferred funds will be used from the escrow account to finance the project in the following years. Consequently, project financing is considered to be completed by SOFAZ.

Throughout the years 2007-2018, SOFAZ spent in total USD 745.9 million (AZN 748.6 million) on the project.

Reconstruction of the Samur-Absheron irrigation system. The project on the reconstruction of the Samur-Absheron irrigation system is financed by SOFAZ according to the ammendments on the Decree № 346 dated 28 December 2015 on SOFAZ's budget. In accordance with the Paragraph 5 of the Decree, the Cabinet of Ministers of the Republic of

Azerbaijan has been tasked to select an orderer organization to carry out works related to the "Reconstruction of the Samur-Absheron irrigation system" project, and thus, according to the Order of the Cabinet of Ministers №42s dated 24 February 2006, the management of the "reconstruction of the Samur-Absheron irrigation system" project and the implementation of orderer's functions were assigned to the Azerbaijan Amelioration and Waterworks Open Joint-Stock Company. The Working Group near the State Amelioration and Waterworks Agency has been set up to urgently resolve the issues emerging during the construction period related to the implementation of the "Reconstruction of the Samur-Absheron irrigation system" project in accordance with the Order № 411s of the Cabinet of Ministers of the Republic of Azerbaijan dated 23 December 2005.

Throughout the years 2006-2018, AZN 1 469.6 million (USD 1 664.6 million) has been transferred from SOFAZ with the purpose of financing the "Reconstruction of the Samur-Absheron irrigation system" project, including AZN 90.0 million (USD 52.9 million) in the reference year.

The "Reconstruction of Samur-Absheron irrigation system" project consists of two stages. Construction of facilities for the first stage, which constitutes the vast majority of the project in 2006-2014, has been completed and these facilities have been commissioned. As part of the Samur-Absheron irrigation system reconstruction project, the Takhtakorpu water reservoir with a total water capacity of 270 million m3, the Takhtakorpu hydroelectric power station with a capacity of 25 MW, the Valvalachay-Takhtakorpu channel with a length of 31.7 km, the Takhtakorpu-Ceyranbatan channel with a length of 107.9 km and the objects for the construction of roads to the Takhtakorpu water reservoir were handed over according to the Act dated 12 November 2014 by the State Acceptance Commission.

Throughout 2014-2018, works on improving water supply for the already irrigated lands and commissioning of newly irrigated lands in the Shabran, Siyazan, and Khizi districts, as well as construction of water intake facilities and water transmission channels on the northern rivers (Gusarchay, Gudyalchay, Cakachukchay, and Garachay) were completed within the framework of the second stage of the project. Thus, construction and financing works on improving water supply for the already irrigated lands and commissioning of newly irrigated lands in the Siyazan district, as well as construction of water intake facilities and water transmission channels on the northern rivers (Gusarchay, Gudyalchay, Cakachukchay and Garachay) have already been fully completed, while 5% performance guarantees were maintained.

Table 4.3.1. List of the completed and ongoing works on the Samur-Absheron project

Objects commisioned by the act of the State Comission	Objects construction of which has already been completed but which are still within the guarantee period	Ongoing objects
1. Takhtakorpu water reservoir 2. Takhtakorpus hydroelectric station (capacity of 25 MVT) 3. Objects for the construction of roads to the Takhtakorpu water reservoir as part of its construction 4. Valvalachay-Takhtakorpu channel 5. Takhtakorpu-Ceyranbatan channel 6. Improvement of water supply of existing irrigated soils in the Siyazan district and putting into operation new irrigated lands 7. Construction of waterway installations and transport channels in the northern rivers (Gusarchay, Gudyalchay, Cakachukchay) 8. Improvement of water supply of existing irrigated soils in the Khyzy region, commissioning of new irrigated lands and construction of the connecting channel to the SAK system	1. Construction of water intake facilities and water transmission channels on the northern rivers (Garachay) 2. Improvement of water supply for the lands already irrigated and commissioning of newly irrigated lands, as well as construction of a channel connecting with the SAK system in the Khizi region	1. Improvement of water supply for the lands already irrigated and commissioning of newly irrigated lands, as well as construction of a channel connecting with the SAK system, in the Shabran region *(projected to be completed in 2019)*

The First Music Conservatoire in the East

The beginning of XX century is a golden age in the history of Azerbaijan. It was characterized by a rapid development of economy, culture and other spheres. In 1921, the first higher music school in the East - conservatoire was opened in Baku. This contributed greatly to the development of art and music in Azerbaijan. It should be noted that 350 students out of 383 were Azerbaijanis in the first educational year. In 1926, Uzeyir Hajibayov was appointed the director and vice-principal of the National Conservatoire.

Many talented and prominent musicians, composers and singers of Azerbaijan, such as Fikrat Amirov, Gara Garayev, Tofig Guliyev, Soltan Hajibayov, Vagif Mustafazadeh, Muslim Magomayev, Asaf Zeynalli were graduates of the National Conservatoire. These great personalities, remembered with pride by our people, have played an important role in the propagation of the name of Azerbaijan, as well as our cultural heritage and national musical values in the world.

Source: "Musiqi dünyası" magazine
The official website of the Azerbaijan National Library

1921

100

YEARS
of
PRIDE

1918-2018

AZERBAIJAN STATE CONSERVATOIRE | CURRENT BAKU MUSIC ACADEMY, 1980

5. INVESTMENT

5.1. INVESTMENT STRATEGY

SOFAZ's investment strategy is aimed at maximizing long-term risk-adjusted returns. Broad diversification among the asset classes and across the countries along with monitoring and analysis of macroeconomic environment serves this strategic goal and assures the persistence of stable investment performance.

The government has laid down general principles and guidelines for the efficient management of the SOFAZ's assets in order to set up the legal framework for SOFAZ's investment mandate and ensure the transparency in the Fund's investment decisions. SOFAZ's investment portfolio is managed in accordance with the "Rules on managing the foreign currency assets of SOFAZ" ("Investment Guidelines"), approved by Presidential Decree No. 511 of 19 June 2001 and the Investment Policy approved by Presidential Decrees on an annual basis.

"Investment Guidelines" sets the general principles of SOFAZ's asset management framework. Along with other purposes, it outlines permissible asset classes, currencies, minimum requirements for SOFAZ's external managers, and defines the credit quality limits for SOFAZ's counterparties (custodian banks, correspondent banks, etc.). Investment Policy defines the objectives, forecasted size, currency composition, strategic asset allocation, benchmarks, and risk limits for the SOFAZ's investment portfolio.

In line with the long-term objectives, asset class composition of SOFAZ's investment portfolio is reviewed and approved annually. According to the 2018 Investment Policy, the asset allocation of the investment portfolio is defined as below:

- 60% - Debt obligations and money market instruments;
- 25% - Equities;
- 10% - Real estate;
- 5% - Gold.

As of December 2018, 76.5% of the investment portfolio comprised of fixed income and money market securities while 12.8%, 5.4%, and 5.3% were invested in equities, gold, and real estate, respectively.

Table 5.1.1. Target Asset allocation

Portfolio as of 31 December 2017	Portfolio as of 31 December 2018	Target Portfolio 31 December 2018
Fixed Income **76.3%**	Fixed Income **76.5%**	Fixed Income **60%**
Equities **14.9%**	Equities **12.8%**	Equities **25%**
Real Estate **5.3%**	Real Estate **5.3%**	Real Estate **10%**
Gold **3.5%**	Gold **5.4%**	Gold **5%**

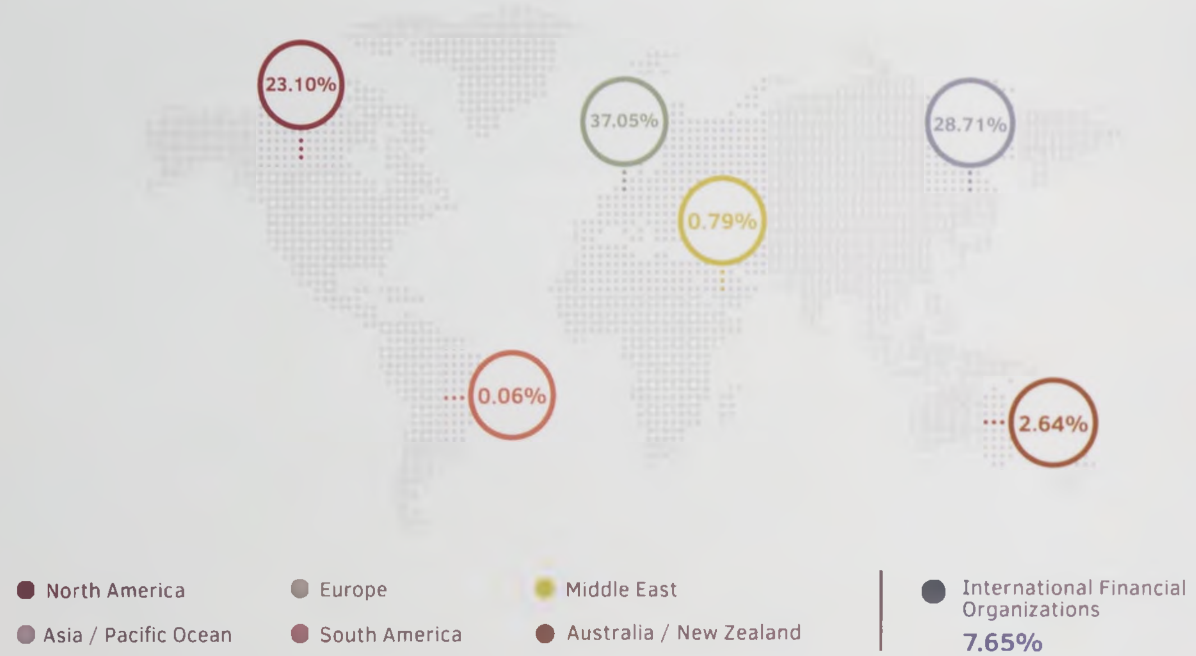
6-month LIBOR for corresponding currencies (6-month EURIBOR for assets denominated in EUR) is selected as the benchmark for the fixed income and money market instruments portfolio while the MSCI World Index is the benchmark for the equity portfolio.

Table 5.1.2. provides a summary snapshot of SOFAZ's current investment approach and its implementation to the portfolio:

Table 5.1.2. Investment Directions

	Asset classes	Strategy employed	Implementation methods
Traditional	Public Equity	Exposure to global equities	MSCI World Index, MSCI Europe ex UK index, S&P 100 index, strategic stake in VTB Bank.
	Fixed Income	Exposure through bonds and money market instruments	Sovereign, supranational, agency, and corporate investment grade bonds and money market instruments.
Alternative	Private Equity	Exposure through private equity funds	Commitments to buy-out and growth funds; Private Equity Separately Managed Mandate with Neuberger Berman; Investment in the charter capital of the Azerbaijan Rigs LLC, formed with the participation of SOFAZ (90%) and SOCAR (10%).
	Real Estate	Exposure through direct property acquisitions, co-investments, and real estate funds	Direct investments into commercial real estate located in Moscow, London, Paris, Seoul, Tokyo, and Milan; Co-investments in office and retail properties located in CBD areas in Germany, Japan, China, USA, and Singapore; Commitments to real estate funds making commercial investments in Asia Pacific, Europe and United States, as well as logistics investments in Japan.
	Gold	Exposure through physical purchase	Investments through gold bars.

Chart 5.1.1. **SOFAZ's investment portfolio breakdown by geographic regions**



External managers

As of December 2018, 9.6% of SOFAZ's investment portfolio was managed by external managers. Benefits brought by external managers include market expertise, specific industry experience, and regional presence thereby adding value to the investment portfolio.

The following external managers were responsible for managing the portion of SOFAZ assets:

For fixed income portfolio:
• World Bank – the World Bank Treasury manages USD 232 million (0.6% of investment portfolio);
• DWS International (previously named Deutsche Bank Advisors) – manages USD 106 million (0.3% of investment portfolio).

For equity portfolio:
• UBS Asset Management – manages USD 1 406 million (3.6% of investment portfolio);
• State Street Global Advisors (SSgA)* – manages USD 1 100 million (2.9% of investment portfolio);
• Mellon Investments Corporation (previously named Mellon Capital Management) - manages USD 304 million (0.8% of investment portfolio);
• BlackRock Investment Management - manages USD 289 million (0.7% of investment portfolio);
• Sumitomo Mitsui Trust International (Sumitomo)* - manages USD 270 million (0.7% of investment portfolio).

**Note: On January 10, 2018, apprx. 20% of the equity portfolio managed by SSgA was transferred to a new external manager, Sumitomo.*

Gold investments

According to the "Investment Policy" for 2018, up to 5% of the SOFAZ's assets can be invested into gold.

During 2018, SOFAZ purchased additional 20 778 kg (668 041 troy ounces) of gold bars making the total outstanding amount of gold in its investment portfolio 50 953 kg (1 638 186 troy ounces) or USD 2 093 million as of 2018 year-end. More than 99% of this gold has been transferred to the vault for storage of the valuables built in the administrative building of SOFAZ.

5.2. SOFAZ'S INVESTMENT PORTFOLIO

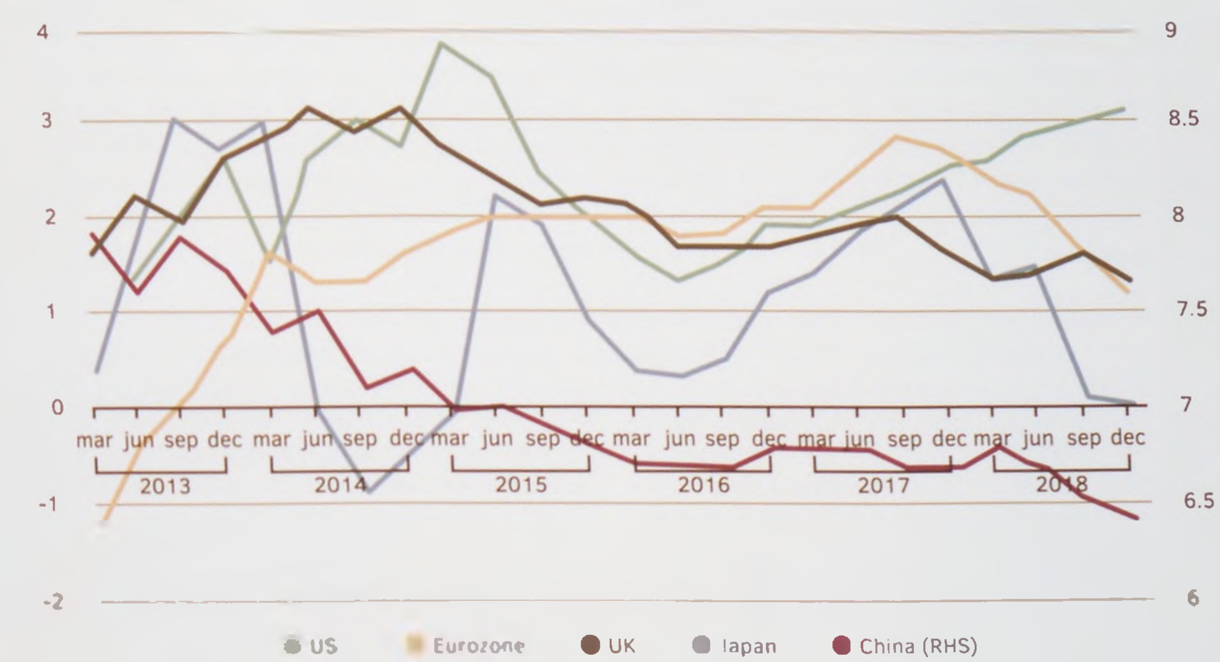
Global Economy Review

World economy grew steadily through 2018, reaching an annual growth rate of close to 4%. Continuing trade tensions affected global trade negatively causing a clear loss of steam in the euro area and China during the year. US growth on the other hand was supported by tax cuts and higher fiscal spending.

After delivering 2.2% growth in 2017, US economy grew at 2.9% in 2018, which is the strongest growth the economy had seen since 2005. Fiscal stimulus was the primary factor behind the US growth this year. Higher economic activity also accelerated wages and pushed unemployment level far into multi-decade low. Some specific factors in the euro area and Japan combined with weaker external demand brought activity down in these regions. Expansion in the British economy slowed as lower investments due to Brexit risk weighted on

growth. Slowdown in China continued in 2018 with mute consumption and weaker external environment. In Russia, GDP growth has reached 2.3% on the back of strong activity and elevated oil prices.

Chart 5.2.1. **Real GDP growth rate in major economies (2013-2018, percentages)***

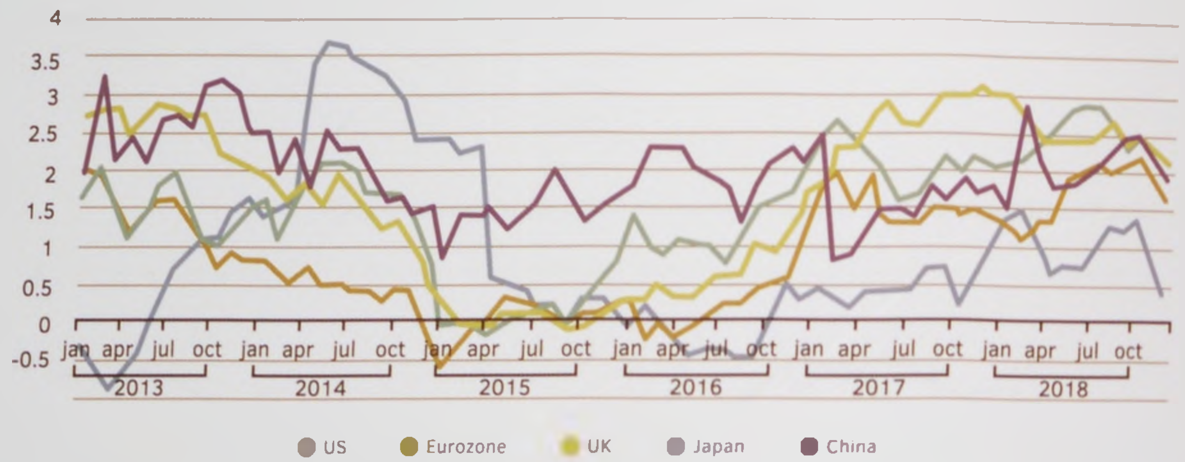


**Year-on-year rates, seasonally adjusted for the US, Eurozone and UK*

Source: Bloomberg

In 2018, headline inflation across the advanced economies increased owing largely to the recovery in oil prices. On the other hand, tight labor markets and relative increase in wages failed to create meaningful inflationary pressures and core Inflation remained subdued through the course of the year. US CPI inflation increased to 2.5%, highest level since 2011. In the euro area, the inflation figure increased further to 1.8% after settling at 1.5% in 2017. CPI inflation in Japan reached 1% in 2018 rising steadily from negative levels two years ago.

Chart 5.2.2. **Inflation rates in major economies (2013-2018, percentages)**

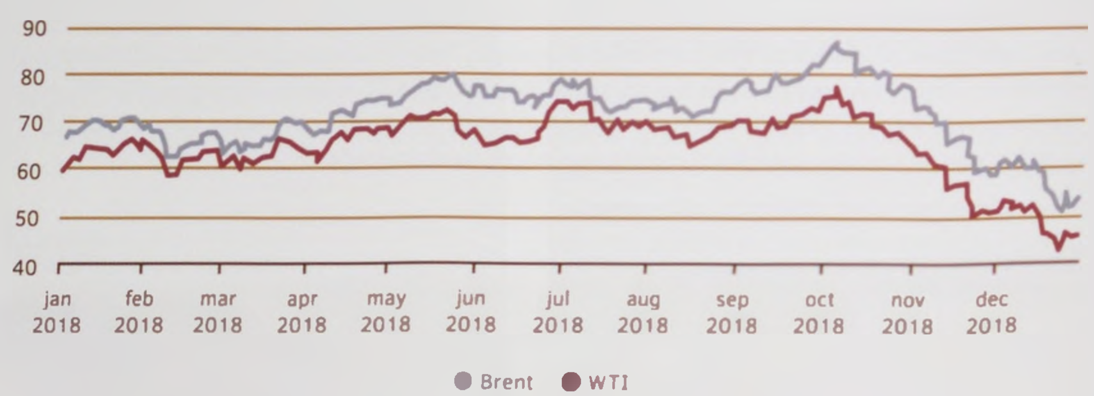


Source: Bloomberg

Oil

Through the year, oil's price trajectory was largely influenced by President Trump's policy decisions and OPEC's response. Relatively balanced entry of the market to the year was followed by a rally due to US administration proposing to leave nuclear deal with Iran. This caused a panic in the market as the investors started pricing potential supply volumes lost from Iran. However, a few weeks later OPEC announced beyond target compliance with the supply cut proposal and a plan to reduce the compliance levels down which resulted in moderation of oil prices. Later in the year, Donald Trump granted waivers to importers of US crude oil causing a downtrend in the price of oil, with Brent trading below USD 60 per barrel at the end of the year.

Chart 5.2.3. **Oil prices in 2018 (USD)**



Source: Bloomberg

Monetary Policy

Monetary policy divergence

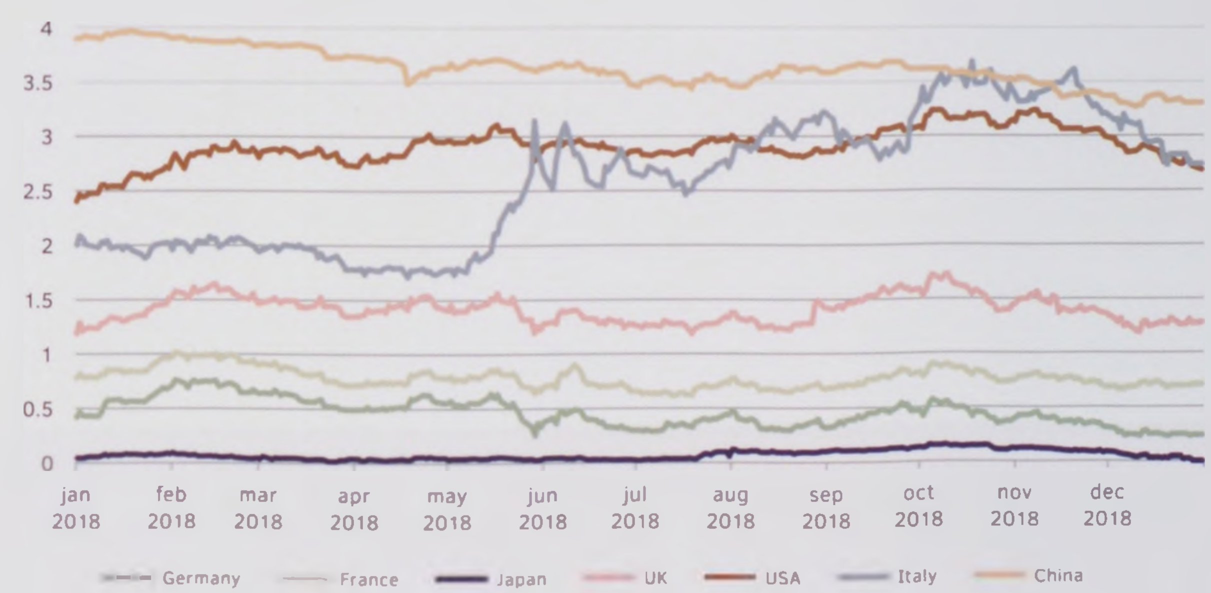
The expansion of balance sheets of major central banks has slowed over the past year, however, this normalization has not been a uniform process: the Federal Reserve (Fed) took quite a lead over the other central banks, while a monetary tightening got under way in a number of emerging countries, and the European Central Bank (ECB) confirmed the end of net purchases under its assets purchase programme.

On the back of solid growth and inflation moving back closer to 2%, the Fed decided to continue its gradual tightening cycle by hiking 1% in 2018. After the December meeting, the target range of the Fed funds rate reached 2.25-2.50%. This led to a flattening in the yield curve as the Fed tried to be more aggressive, generating market volatility.

The ECB took a first step towards exit this year by ending net purchases conducted under the APP programme. The macro-economic environment has clearly weakened since June, when the ECB first signaled an end of net purchases. In any case, the bank will continue to exert a dampening effect on euro area sovereign bond yields through re-investments of its existing holdings of government bonds of more than EUR 2 trillion.

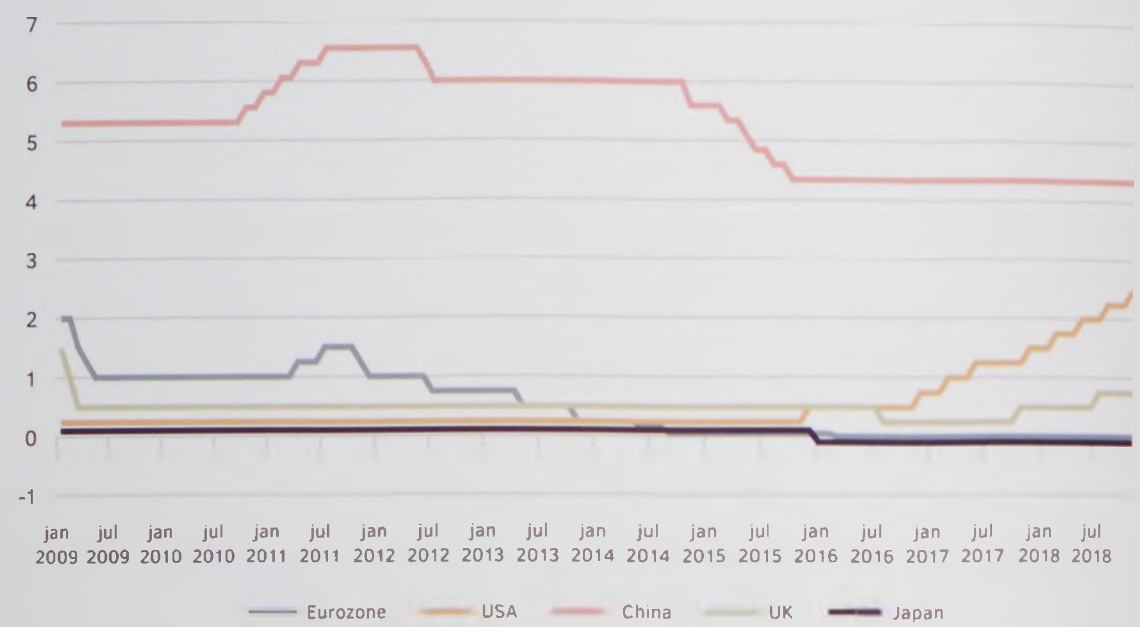
Despite a 25 bps increase in the base rate in August 2018 thereby considerably subduing the impacts of Brexit in 2018, Bank of England (BOE) kept its monetary policy accommodative. The Bank's monetary policy stance has been considerably dependent on Brexit-related developments. Therefore, the BOE has been mainly waiting for those uncertainties to unfold over the course of 2018, having proceeded to only one 25 bps rate hike in August 2018. The rate hike was necessitated due to an overshoot in inflation and a decline in unemployment.

Chart 5.2.4. **10 year generic yield (percentages)**



Source: Bloomberg

Chart 5.2.5. **Central Banks' benchmark interest rates (2009-2018, percentages)**



Source: Bloomberg

Fixed Income Markets

In 2018, short and long end of the US Treasury curve experienced different trajectories. While expectations of strong growth, T-bill issuance, and monetary tightening signaled that 10-year yields might reach 3%, the global slowdown in last quarter of the year led to 10-year bond settling within its previous range. As for the short end, Fed's determination to push ahead with rate hikes and US treasury's choice to concentrate issuance at the short end stirred the market and pushed the short end of the curve on average 100 bps up inverting 2Y-5Y segment of the curve. This was underpinned by fears of recession and slowing US economy. Fed has also gone ahead with balance sheet normalization which has led to a USD 600 billion public reduction in excess reserves.

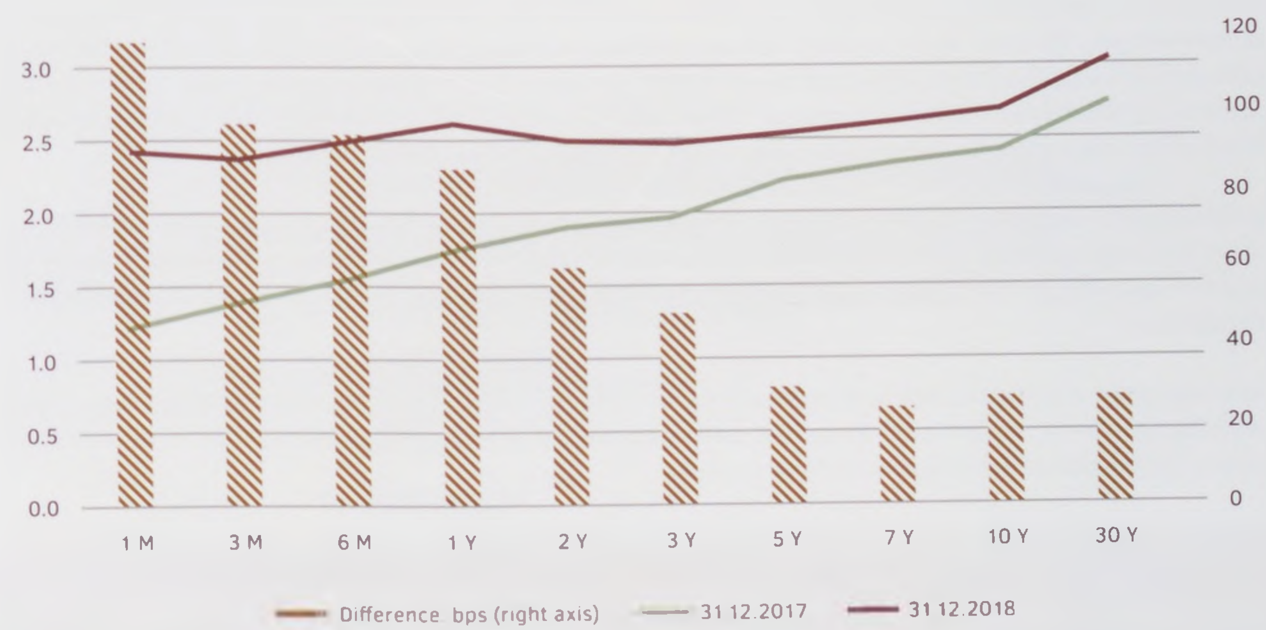
Eurozone's uptrend in risk appetite halted when coalition government by M5S and Lega was formed in Italy. As the controversies surrounding the Italy's 2019 draft budgetary plan intensified, the German 10-year bund was pushed back inside its 2017 trading range. Weak inflation data with lower global growth and tensions in France and Italy were among the factors pushing the most of the German curve down. With Fed actively shrinking its balance sheet when the ECB repeatedly pushed back the date for tightening the monetary policy, spreads between US and German curves widened to all-time highs (280 bps for the 10-year tenor) and ended the year at 245 bps. Peripheral spreads widened after the mid-year as a response to the turmoil with Italy.

The Bank of England's monetary policy is "Brexit dependent" given the uncertainty over the UK's future and impact assessments published by the BOE. The 10-year Gilt yield has traded within a wide range (1.20% and 1.70%) as a result of swings in Brexit expectations and ended the reported year at around 1.25%.

Chart 5.2.6. **Germany sovereign yield curve (percentages)**

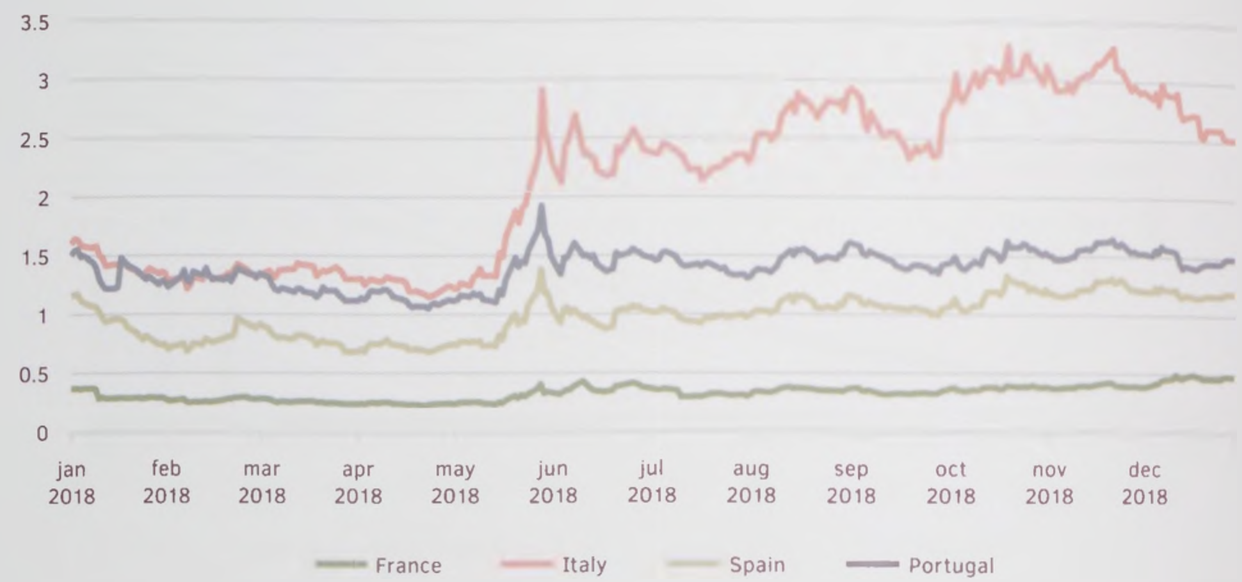
Source: Bloomberg

Chart 5.2.7. **US sovereign yield curve (percentages)**



Source: Bloomberg

Chart 5.2.8. 10-year yield spreads against Germany government bonds (percentages)



Source: Bloomberg

Foreign Exchange Markets

Underperformance of emerging currencies against G10 currencies was one of the notable movements in 2018. After the unexpected slide in 2017, the US dollar recovered and by the year-end appreciated against all currencies except the Japanese yen. The sharp appreciation of USD was fueled by increased risk aversion, trade war between the United States and China, political risks in Italy and the UK (Brexit), concerns of a slowdown in global growth, and also by solid growth in the US and Fed's continuing monetary tightening (+100 bps) leading to a further divergence in the level of the key policy rate relative to other central banks (such as the ECB, BOE and Bank of Japan).

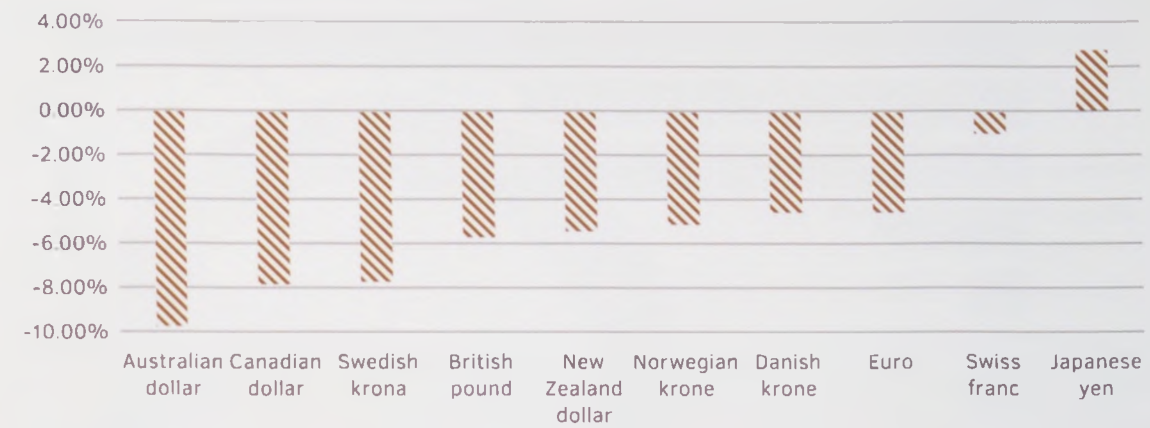
Euro declined by more than 5% against the US dollar, and finished the year at around 1.14. The Italian political crisis, a slowdown in European growth as well as weak inflation expectations and, consequently, more distant prospect of a monetary tightening by the ECB (pushed back to 2019 year-end) were all among the factors affecting the decline in EUR/USD pair.

British Pound has been significantly volatile throughout the year, especially towards the end of 2018 given the absence of visibility over Brexit. Despite one hike by BOE, GBP was penalized by the slowdown in British growth as well as the weaker inflation and increased likelihood of hard Brexit.

Chinese Yuan experienced a sharp decline in 2018, resulting in USD/CNY pair approaching psychologically important 7.0 level, with the Chinese growth and trade tensions with the US being among the significant factors.

Turkish lira dropped by more than 28% despite the rebound since September which was prompted by the sharp hike in the 1-week repo auction rate to 24%, easing of diplomatic tensions between Turkey and the United States, and the reduction in the current account deficit.

Chart 5.2.9. G10 Currency performance in 2018 against USD

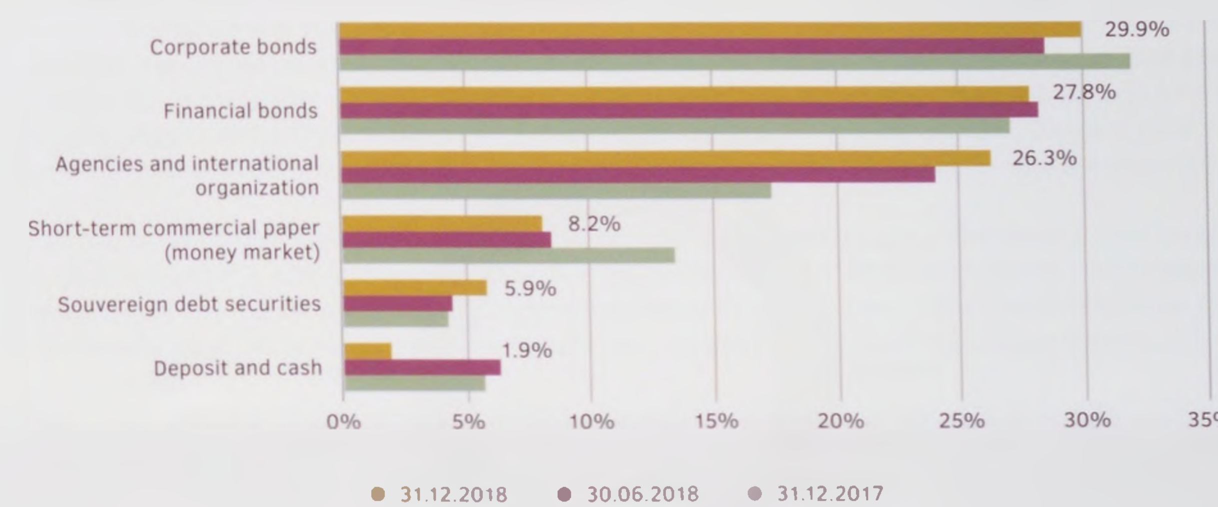


Source: Bloomberg

Fixed Income Investments

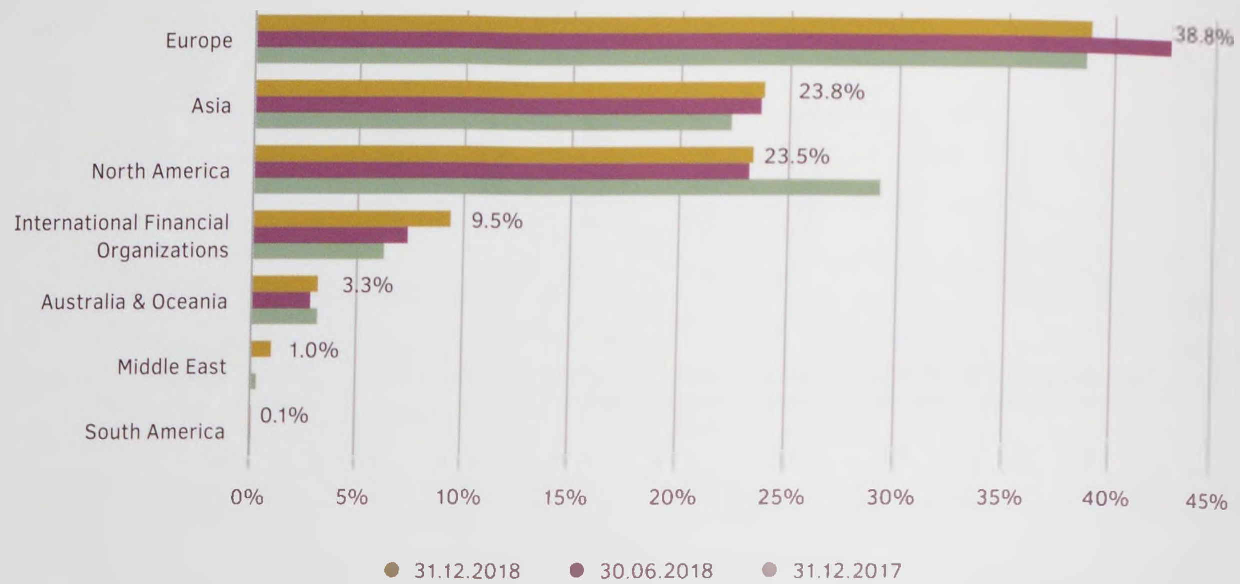
In 2018, SOFAZ's exposure to Sovereign-Supra-Agencies (SSAs) was substantially increased, and the strategy of relocating funds to securities offering lower duration and higher rating was implemented. The share of agencies and international organizations and sovereign debt securities rose by 8.9% and 1.6%, respectively, compared to the previous year. Moreover, the holding of financial bonds was largely kept equal to its level in 2017. Exposure to the short-term commercial papers was decreased due to lower money market yields and limited opportunities. Coming to the corporate bonds, slight reduction may be observed.

Chart 5.2.10. Breakdown of fixed income portfolio by product types



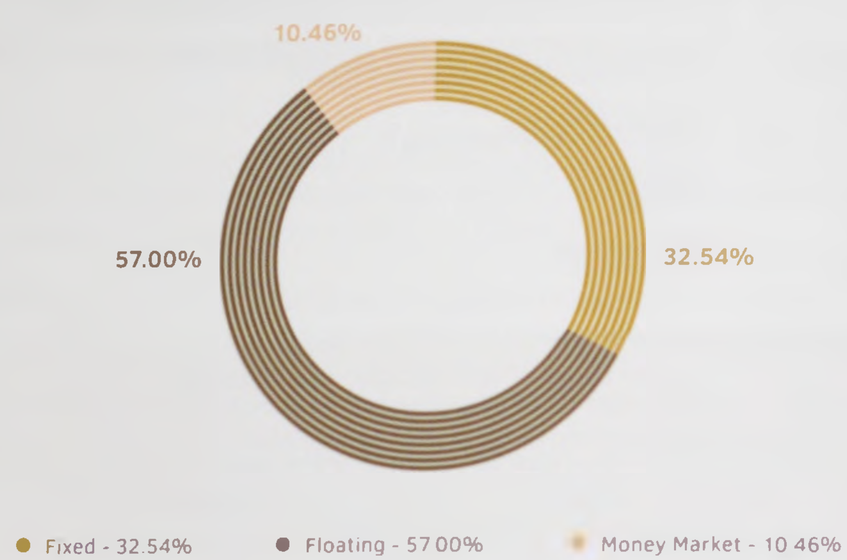
SOFAZ continued the strategy of geographical diversification of fixed income portfolio in 2018. SOFAZ underweighted its exposure to North America (23.5%) and slightly overweighed its exposure to Asia and International Financial Organizations to 23.8% and 9.5%, respectively. There was no material percentage change in holdings in other regions.

Chart 5.2.11. Breakdown of fixed income portfolio by geographical distribution



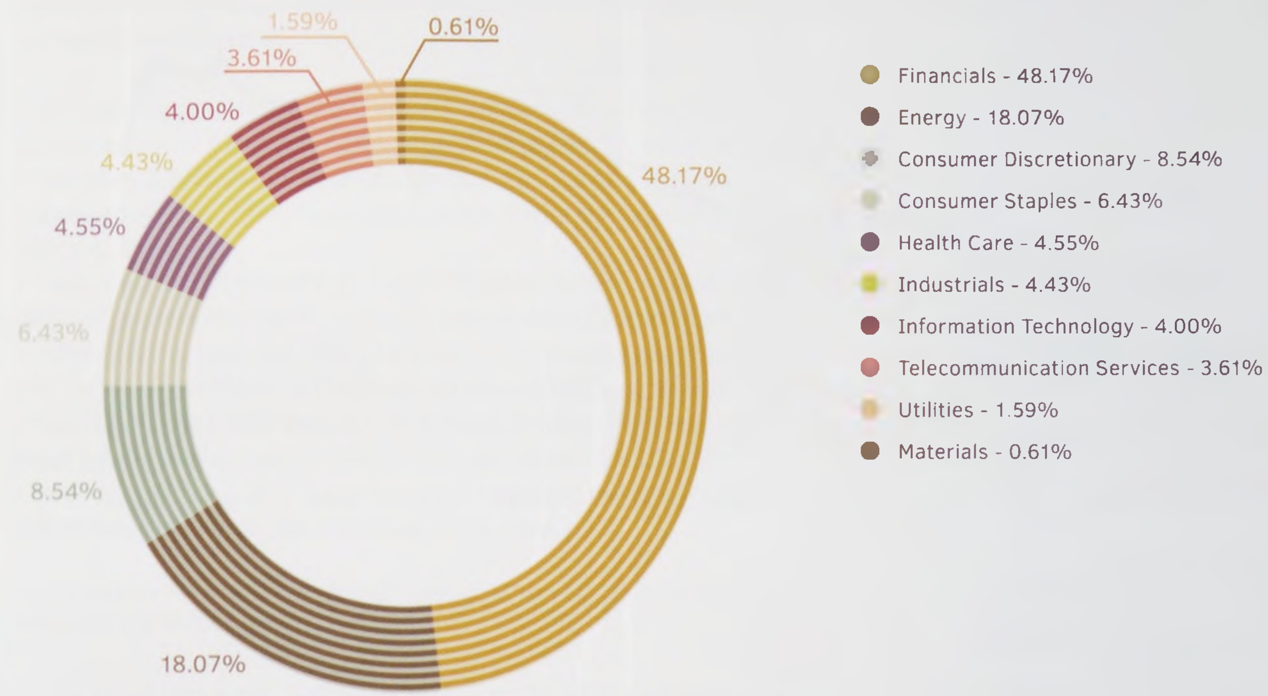
There was a significant change in the breakdown of the fixed income portfolio by security type in 2018. While there was no material change in the portion of fixed coupon securities, the holdings of floating rate notes were further increased from 49.16% to 57% and money market instruments (including deposit and cash) were significantly decreased from 19.25% to 10.46%. The increase of floating rate securities was due to rising yield environment while the decrease in the money market securities was due to the Fund's strategy of reinvesting maturing deposits in Turkish Banks into bond instruments. The aim of the strategy was to benefit from the potential rate hikes, increase in yields while eliminating major risks in emerging markets. The duration in the overall fixed income portfolio was kept short throughout the year, for the purpose of protecting it from adverse movements in the interest rates.

Chart 5.2.12. Breakdown of fixed income portfolio by security type



Additionally, the Fund's fixed income portfolio is well diversified across different industry sectors. The sectors receiving highest allocations during the reporting year were financials, energy, consumer discretionary and consumer staples.

Chart 5.2.13. Breakdown of fixed income portfolio by sectors



EQUITY INVESTMENTS

Public equity market review

2018 was not a positive year for equity markets. Despite good macroeconomic and microeconomic indicators, all country indexes and nearly all sectors recorded negative performance. Global stocks have fallen 10.44% in 2018, according to the MSCI World Index as at 31 December 2018. Gains in the first nine months of the year were erased in the final three months: global stocks reached 4.6% during the first three quarters of 2018, followed by a fall of more than 13% in the fourth quarter. The MSCI ACWI Index had its worst annual performance since 2008 with 11% loss. The broad European gauge "Euro STOXX 600" recorded eight negative months and fell 13%, the most since 2008. While the S&P 500 was up 9% during the first three quarters of 2018, it ended the year in the negative digits at 6.2%.

US president Donald Trump's tax cuts and low interest rate and loose monetary policy environment since the global financial crisis resulted in 4.2% GDP growth in the US in the second quarter of 2018, which had its positive impact on equity market. US equities declined materially in the last quarter with especially steep falls in December due to faster-than-expected pace of rising interest rates and concern over ongoing trade negotiations between China and the US.

Eurozone's economic growth slowed from a quarterly pace of 0.4% in the first quarter of 2018 to 0.2% in the fourth quarter. A slowdown in Europe has been due to a drop in car production after a change in environmental regulation, a sharp decline in the manufacturing sector's new export orders in response to a slowdown in demand from China. But domestic political factors have also been a drag. The Italian government's confrontation with the European Union over its budget, Brexit uncertainty, and protests surrounding the cost of petrol in France significantly weakened business confidence.

In terms of sector performance, utilities and health care which are referred to as "defensive" sectors and the information technology sector were the only three sectors that ended the year in a positive territory. Because of its cyclical nature, financial sector was the worst performing sector with around 16.5% loss. Materials were also among the worst performing sectors with more than 16% loss mainly due to imposed tariffs on steel and aluminum.

Chart 5.2.14. **MSCI World Index (2008-2018, index points)**

Source: Bloomberg

SOFAZ'S EQUITY PORTFOLIO

By the end of 2018, public equity portfolio decreased to 9.57% of total AUM of SOFAZ, compared to 11.7% in 2017. Throughout the year, public equity investments lost 8.74% in local terms (-11.55% in USD terms). The Fund mitigates portfolio volatility by investing the largest proportion of the equity portfolio into the well-diversified MSCI World index. The return of the portfolio tracking MSCI World accounted for -6.92% local return (-8.24% in USD terms) in 2018. SOFAZ's internally managed portfolio which is benchmarked to the S&P 100 index generated the negative return of 3.98% throughout the year. SOFAZ continues to hold an equity stake in VTB bank, a state-controlled Russian bank. In 2018, its local currency denominated return equaled -23.56% (-36.51% in USD terms). The loss of the portfolio tracking MSCI Europe ex-UK index was 10.44% in EUR and 14.14% in USD terms in 2018.

PRIVATE EQUITY

PRIVATE EQUITY MARKET REVIEW 2018

2018 was a satisfactory year for private equity markets and it was characterized with 1 175 private equity funds raising a total of USD 426 billion capital. Funds focused on North America raised USD 240 billion, while Europe and Asia focused funds secured USD 90 billion and USD 80 billion, respectively. For the first time, Asia saw more funds completing fundraising than Europe. Dry powder continued to climb through 2018, reaching USD 1.20 trillion as at December 2018 – a new record. Throughout the reference year, ten largest funds in the market gathered USD 125 billion. By the end of 2018, the average fund size reached USD 363 million surpassing the corresponding figure for 2017 (USD 339 million). The largest fund that completed fundraising in 2018 was a USD 18.5 billion "Carlyle Partners VII" and SOFAZ is one of the fund's investors.

Accumulated dry powder, high leverage and rich valuations continued to be major investor concerns in 2018. Accordingly, SOFAZ's approach was to steer clear of the funds that have generated poor returns during economic downturns, have been relying too much on leverage to deliver returns, and purchased portfolio companies at high purchase prices.

SOFAZ'S PRIVATE EQUITY PORTFOLIO

During 2018, SOFAZ has committed to five buy-out funds and one growth fund. Below are short descriptions of the mentioned investments:

• "Carlyle Europe V" is a EUR 5.5 billion fund managed by Carlyle Group. The fund aims to realize buy-out investments, predominantly in Europe. SOFAZ has committed EUR 50 million to the fund.
• "Warburg Pincus Global Growth" is a USD 13.5 billion fund managed by Warburg Pincus. The fund aims to invest in growth companies mainly in North America and to a lesser extent in Europe and Asia. SOFAZ has committed USD 50 million to the fund.
• "Vista Equity Partners VII" is a USD 15 billion fund managed by Vista Equity Partners. The fund aims to invest in technology and software in the United States. SOFAZ has committed USD 40 million to the fund.
• "Thoma Bravo XIII" is a USD 12.6 billion fund managed by Thoma Bravo. The fund is aimed to invest in technology and software companies in the United States. SOFAZ has committed USD 25 million to the fund.
• "Baring Private Equity Asia VII" is a USD 5.5 billion fund managed by Baring Private Equity Asia. The fund aims to make buyout investments in Asia. SOFAZ has committed USD 50 million to the fund.
• "PAG Asia III" is a USD 4.5 billion fund managed by PAG. The fund is aimed to make buyout investments in Asia. SOFAZ has committed USD 30 million to the fund.

Note: Fund sizes indicated above are target sizes at the time of SOFAZ's commitments and actual sizes may differ from these with some funds still raising capital in the market.

Table 5.2.1. **SOFAZ's previous PE investments**

Funds	Investment Year	Base Currency	Committed Amount, mln
"ALAC Fund"	2010	USD	100
"Global Infrastructure Fund"	2013	USD	200
"The Catalyst Fund"	2013	USD	50
"NB Caspian Fund"	2016	USD	200
"EBRD EPF"	2016	EUR	100
"Carlyle Partners VII"	2017	USD	50
"Blackstone Core Equity Partners"	2017	USD	50
"BC European Partners X"	2017	EUR	56
"Apollo Fund IX"	2017	USD	85
"FSI Mid-market Growth Fund"	2017	EUR	20

Chart 5.2.15. Breakdown of private equity funds by regions

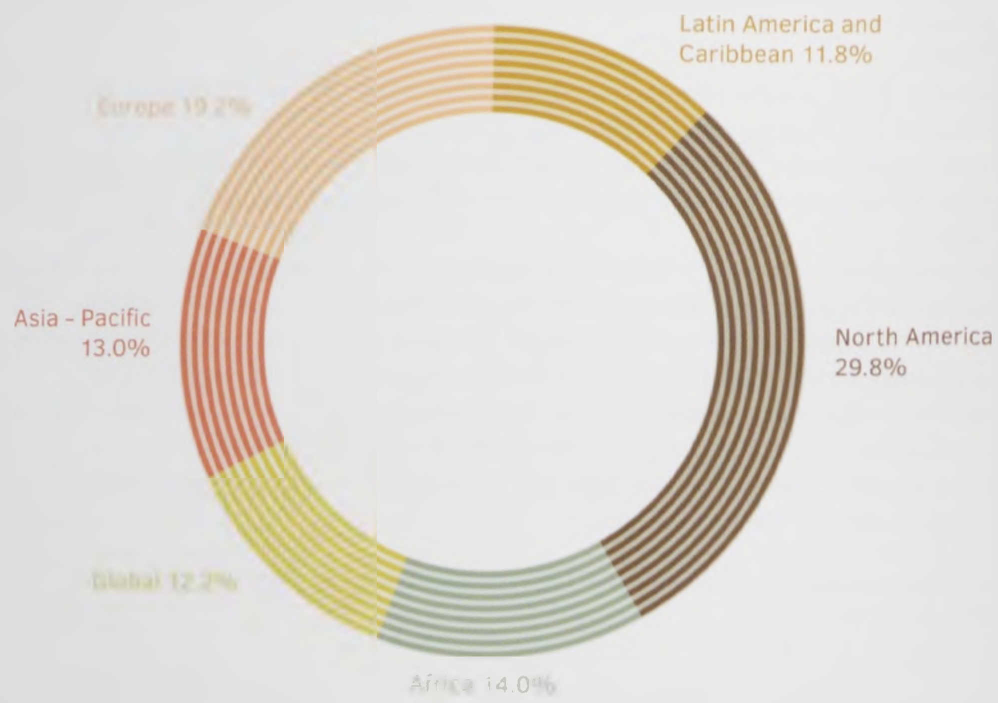
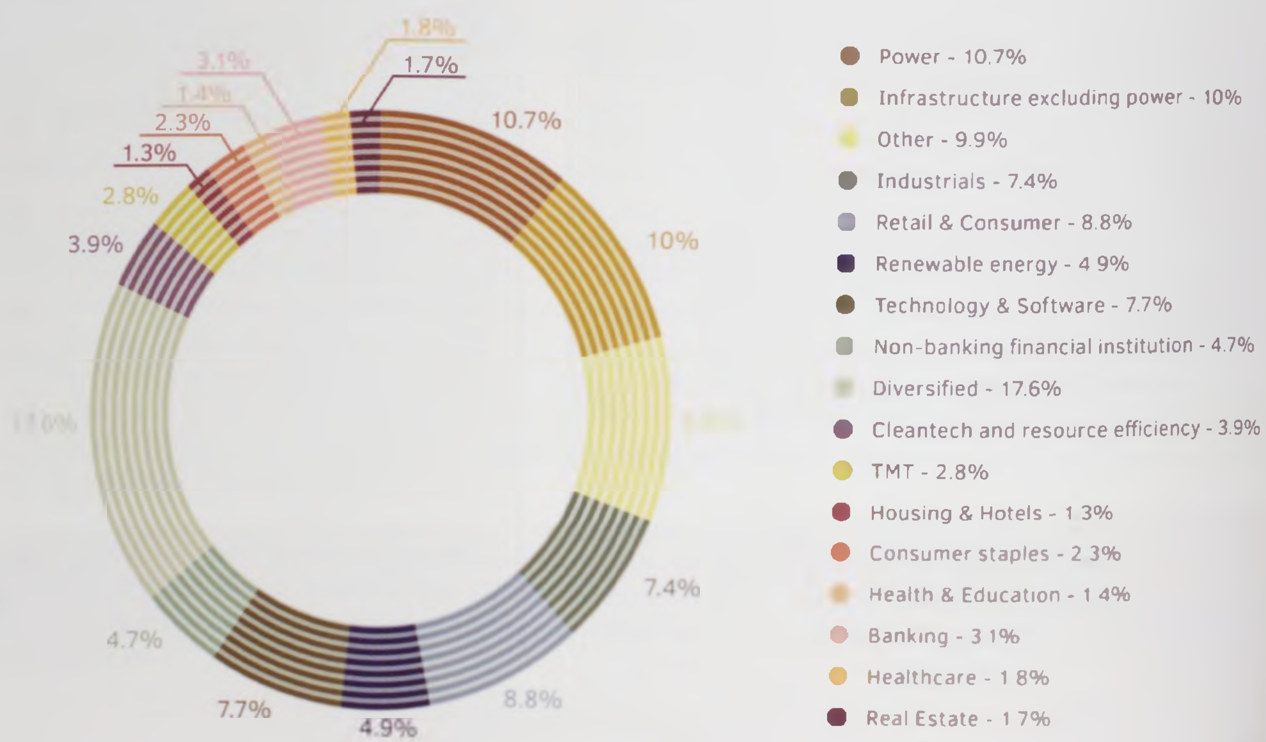


Chart 5.2.16. Breakdown of private equity funds by sectors



INVESTMENT TO THE NEW, SEMI-SUBMERSIBLE DRILLING RIG

Up to 2018, shareholders fully invested USD 1,004.7 million (AZN 1,075.0 million using exchange rates at the time of payments) in the charter capital of the Azerbaijan Rigs LLC, formed with the participation of SOFAZ (90%, USD 904.2 million) and SOCAR (10%, USD 100.5 million). The maximum budget limit of the project was USD 1 116.7 million. Payments to the contractors were fulfilled by periodic capital contributions from SOFAZ and SOCAR. According to the Engineering Procurement and Construction Contract dated 24 June 2013, Caspian Drilling Company LLC was a project contractor, which was founded by SOCAR and is the owner of existing drilling rigs in the Caspian Sea. The inauguration of "Heydar Aliyev" Semi-submersible Drilling Rig took place on 18 May 2017 with the participation of the president of the Republic of Azerbaijan. During 2018 Azerbaijan Rigs continued to establish inventory stock needed for the operations of the rig, which was delivered to the owner on 26 December 2018.

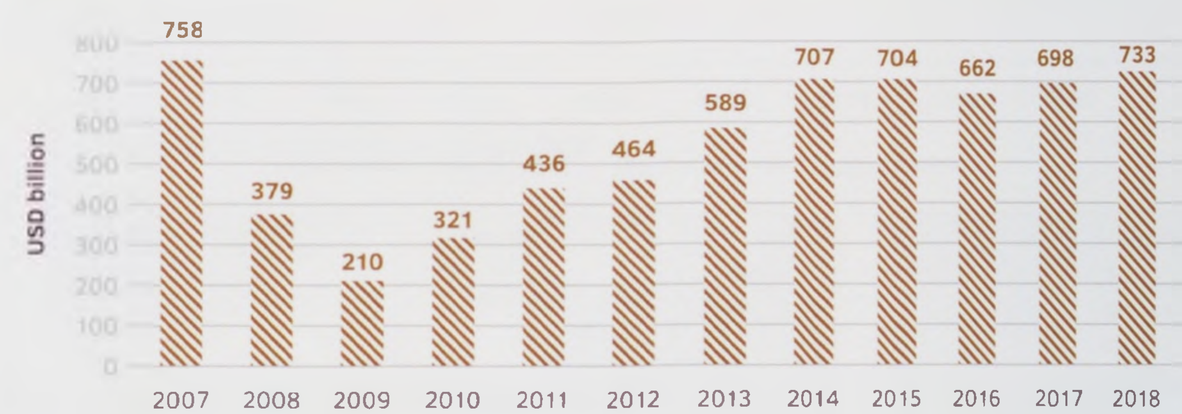
GLOBAL REAL ESTATE MARKET

In a context of rising political and economic uncertainty and volatility, global commercial real estate market performed strongly in 2018 with investment and occupier demand outpacing 2017's statistics and reaching the peak since 2007. 2018 was also characterized with robust occupier demand in office leasing markets and record demand in the logistics sector holding vacancy rates near historic lows.

INVESTMENT VOLUMES

Global commercial real estate investment volume rose by 5% making total of USD 733 billion, the best annual performance since 2007. High-quality assets, strong tenants and long leases continued to be investors' preferences as sources of stable income. Moderate rent growth was maintained even though yields were still at or below preceding year lows.

Chart 5.2.17. Global Commercial Real Estate Investment



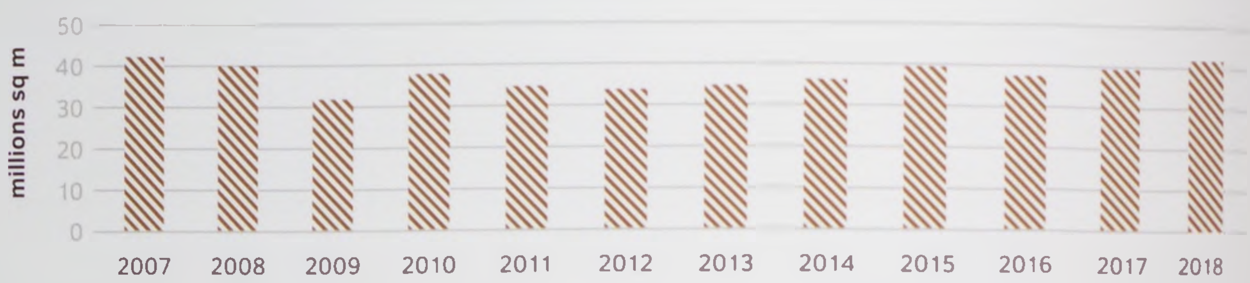
Source: JLL

OFFICE MARKET

A further decline in global office vacancy rate robustly continued in the face of a rise in new deliveries falling down to 11.3%. 2018 registered 3.8% prime office rental uplift across 30 global cities. Vacancy rates decreased in both Europe and the Americas by 20-30 bps to 6.2% and 14.7% respectively and showed no change in Asia Pacific remaining at 10.2%.

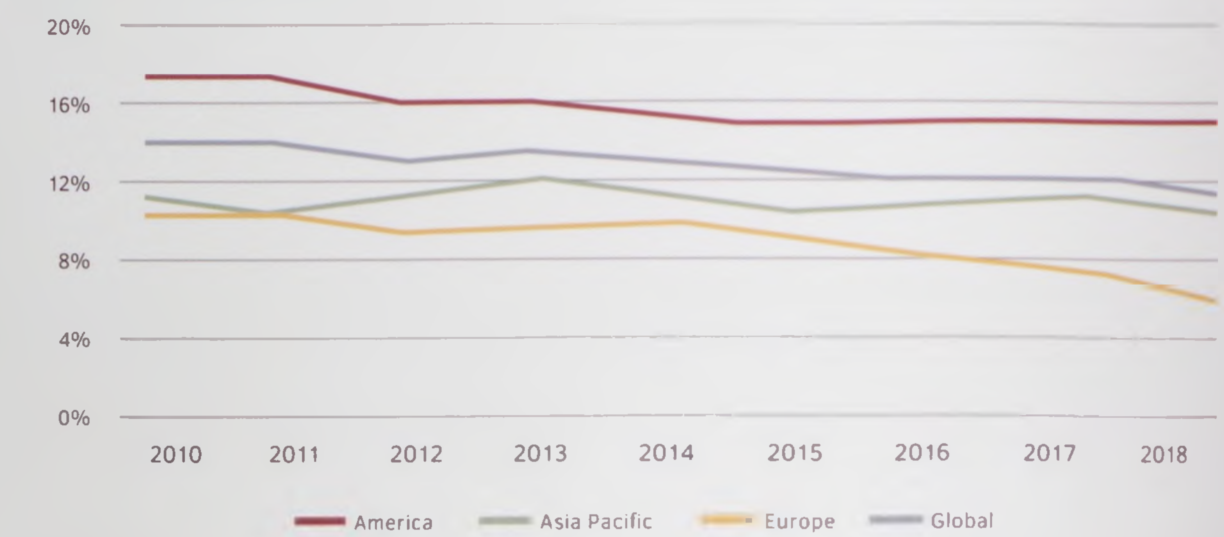
Leasing volumes reached a record level in 2018 and experienced YoY 5% increase at 43 million square meters across 96 markets. Asia Pacific continued to record an impressive increase in leasing volumes equaled to 21% in 2018, while leasing activity in the US grew moderately (up 3% in 2018). Supply shortages acted as a constraint on demand in Europe causing the year end with the same rates as in 2017.

Chart 5.2.18. Global office demand - annual gross leasing volumes



Source: JLL

Chart 5.2.19. Global and regional office vacancy rates



Source: JLL

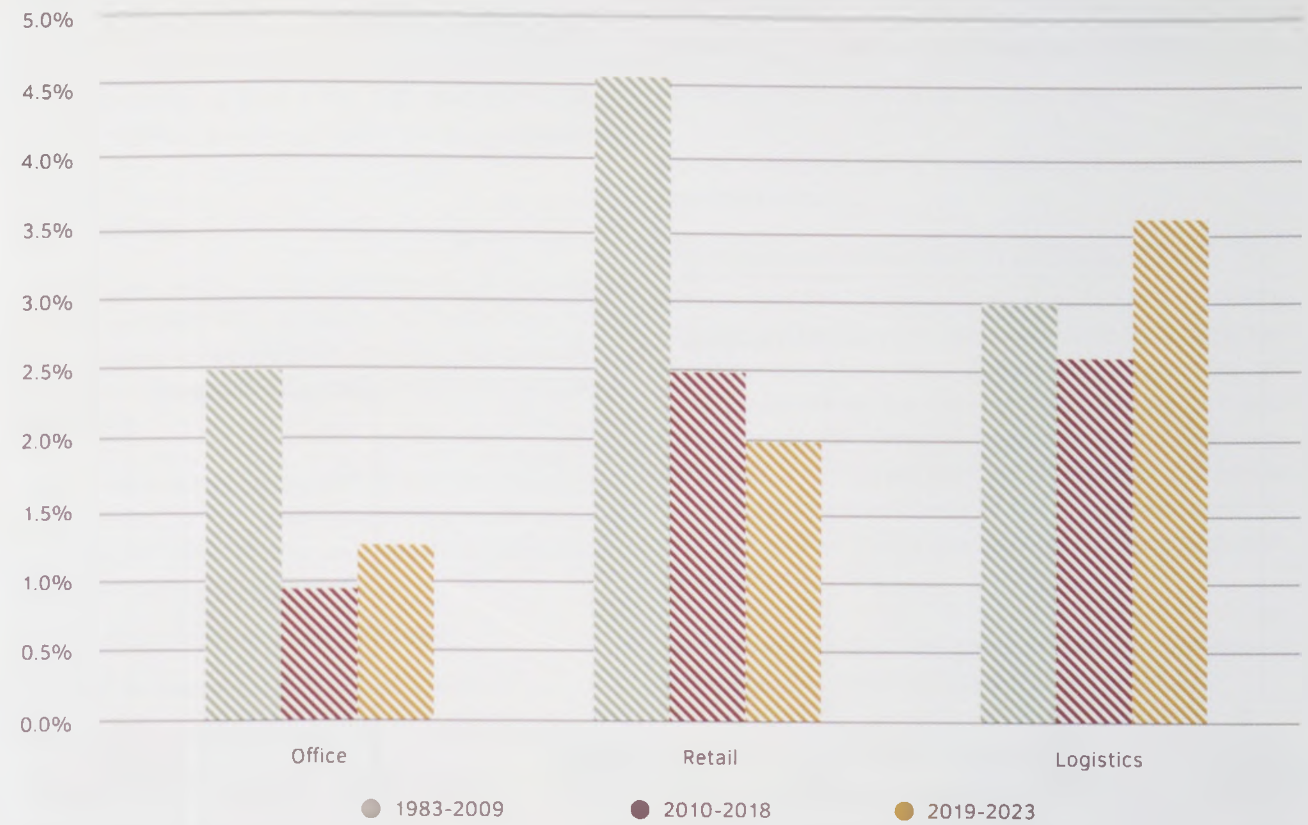
RETAIL AND LOGISTICS MARKET

In 2018 the retail market continued to face pressure as rising trend of online marketplaces remained. Absorption of retail space was weak. A shortage of new supply made retail availability relatively low, however vacancy rates approached their highest level since the depths of the global financial crisis.

In the US, deliveries of new retail centers continued to be suppressed as underperforming retailers closed and developers concentrated more on building mixed-use communities. However, demand for best-of-best retail space remains robust as tenants seek to maintain their presence in strong locations. Retailers in Europe showed mix performances. In Asia Pacific region, experience-oriented tenants constituted the largest part of demand, while rental growth was instable across the region.

In contrast, 2018 was a remarkable year for global logistics market registering record level of demand, robust pre-leasing, and historical low vacancy rates. Despite trade and tariff concerns, US industrial market kept high level of leasing and all time low vacancy rates. In Europe, the double-digit occupier growth remained at record levels and marked its sixth consecutive year of uplift in 2018. In Asia Pacific, supportive demand drivers and low vacancy resulted in rising of rents across the region.

Chart 5.2.20. Global supply growth by sector (% per annum)



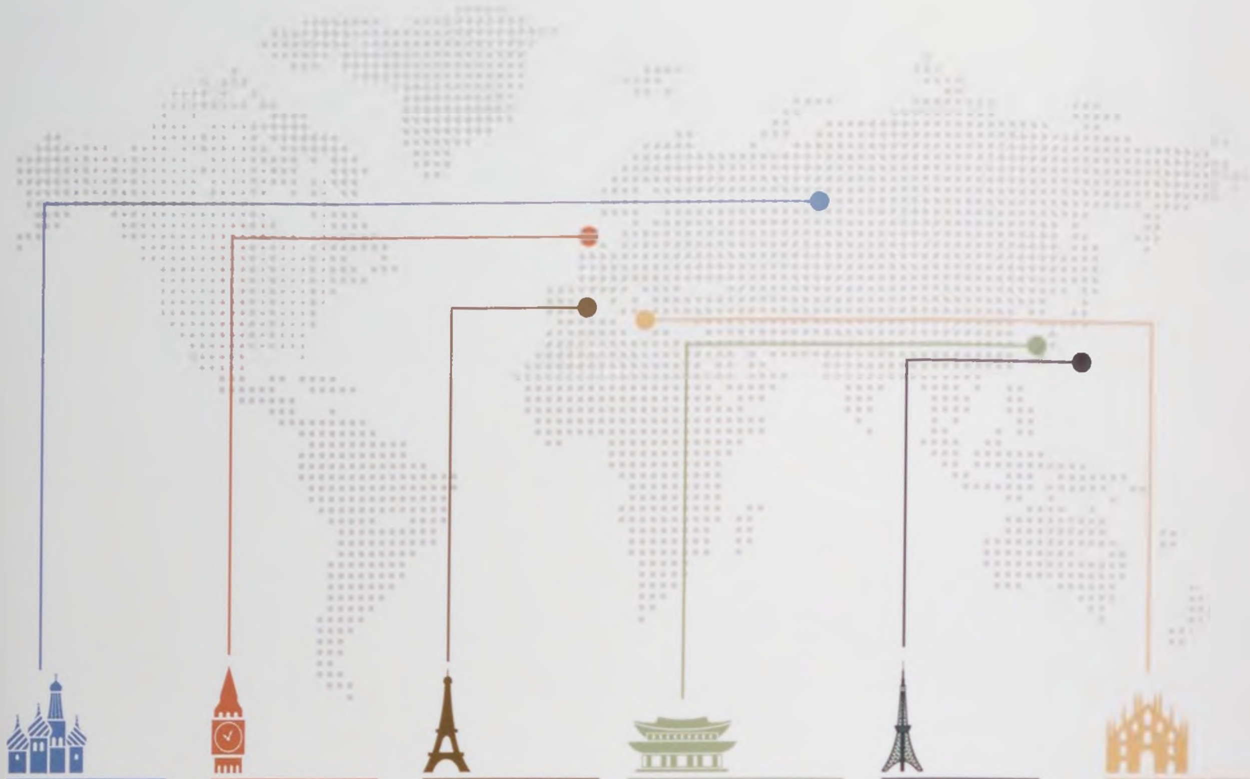
Source: PGIM Real Estate

Chart 5.2.21. Logistics rent growth by region in 2018

Source: Prologis

SOFAZ'S CURRENT REAL ESTATE PORTFOLIO

Direct investments



Name: "Gallery Actor"	**Name:** "78 St. James"	**Name:** "8 Place Vendome"	**Name:** "Pine Avenue A"	**Name:** "Kirarito Ginza"	**Name:** "Palazzo Turati"
Place: Moscow, Russia	**Place:** London, UK	**Place:** Paris, France	**Place:** Seoul, South Korea	**Place:** Tokyo, Japan	**Place:** Milan, Italy
Type: Office / Retail	**Type:** Office	**Type:** Retail / Office	**Type:** Office	**Type:** Retail	**Type:** Office
Year of acquisition: 2012	**Year of acquisition:** 2012	**Year of acquisition:** 2013	**Year of acquisition:** 2014	**Year of acquisition:** 2015	**Year of acquisition:** 2016

NEW INDIRECT INVESTMENTS IN 2018

Consistent with its real estate strategy of building a diversified risk adjusted portfolio across geographies, real estate types, and investment strategies, SOFAZ made investments to the following private real estate funds in 2018:

• Gaw Capital Partner's "Gaw US Fund III" The Fund was established in 2017 with size of USD 412 million and makes real estate investment in the US. SOFAZ's commitment in "Gaw US Fund III" is USD 63.5 million as a Limited Partner.

• GreenOak Real Estate's "GreenOak US Fund III" The Fund was established in 2017 with size of USD 1.55 billion and makes real estate investment in the US. SOFAZ's commitment in "GreenOak US Fund III" is USD 100 million as a Limited Partner.

• PAG's "PAG Real Estate Partners II" (PREP II). The Fund was established in 2018 with the target size of USD 2 billion and makes commercial real estate investments across all asset class in Asia Pacific. The fund makes investments mostly in Australia, China, Hong Kong, and Japan. SOFAZ's commitment in PREP II is USD 50 million as a Limited Partner.

• Angelo, Gordon & Co's "AG Realty Value X" The Fund was established in 2018 with the target size of USD 2.5 billion and makes real estate investment in the US. SOFAZ's commitment in "AG Realty Value X" is USD 100 million as a Limited Partner.

NEW CO-INVESTMENTS IN 2018

• SOFAZ has reached an agreement with Gaw Capital Partner's "Gateway Real Estate Fund V" to make co-investment to retail portfolio located across Hong Kong. SOFAZ's equity portion in the co-investment is USD 50 million.

• SOFAZ has reached an agreement with "Around Town" - real estate investor in Germany - to make co-investment to office property located in the CBD area of Frankfurt, Germany. SOFAZ's equity portion in the co-investment is EUR 75 million.

Annual earnings

As of the year end, direct investments in the real estate portfolio consisted of six assets located in London, Paris, Moscow, Seoul, Tokyo and Milan. During 2018, gross rents mentioned below were collected from the six respective investments:

• London, 78 St James Street, GBP 41 437 361. The amount is comprised of annual rental income (GBP 4 637 361) and surrender fee (GBP 36 873 242) received due to early termination of the lease agreement.

• Paris, 8 Place Vendome, EUR 5 332 000;

• Moscow, 16 Tverskaya, RUB 322 607 000,

• Seoul, Pine Avenue Tower A, KRW 13 520 217 383;

• Tokyo, Kirarito Ginza, JPY 1 500 380 904;

• Milan, Palazzo Turati, EUR 4 896 525.

All six assets were independently valued at the end of 2018. The valuation results and valuation companies are as below:

• 78 St James Street, JLL, GBP 120 000 000;

• 8 Place Vendome, BNP Paribas Real Estate, EUR 186 114 750;

• 16 Tverskaya, Cushman & Wakefield, RUB 3 269 000 000;

• Pine Avenue Tower A, Kyungil Appraisal, KRW 515 500 000 000;

• Kirarito Ginza, Daiwa Real Estate Appraisal, JPY 58 400 000 000;

• Palazzo Turati, CBRE, EUR 104 000 000.

5.3. RETURNS ON SOFAZ'S INVESTMENT PORTFOLIO PERFORMANCE

PERFORMANCE MEASUREMENT METHODOLOGY

Returns on SOFAZ's assets are calculated in accordance with the "Performance measurement methodology for the investment portfolio and sub-portfolios of the State Oil Fund" approved by the Internal Resolution No.31 dated November 29, 2017. In accordance with this methodology, AZN, USD, and EUR are selected as the base currencies for calculating performance of the investment portfolio with and without taking into account currency exchange fluctuations.

The following figures are based on the performance of investment portfolio measured in local currencies.

SOFAZ RATE OF RETURN IN 2018

The total rate of return on SOFAZ's investment portfolio was 0.35%. Historical returns for the period of 10 years starting from 2009 and monthly cumulative returns for 2018 are illustrated in Charts 5.3.1 and 5.3.2, respectively.

Chart 5.3.1. Rate of return of SOFAZ's investment portfolio (in local currency)

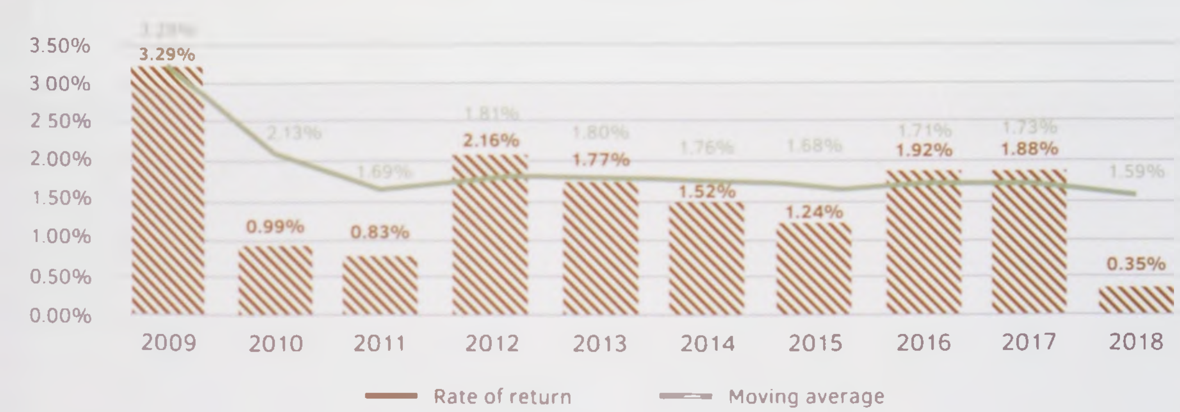
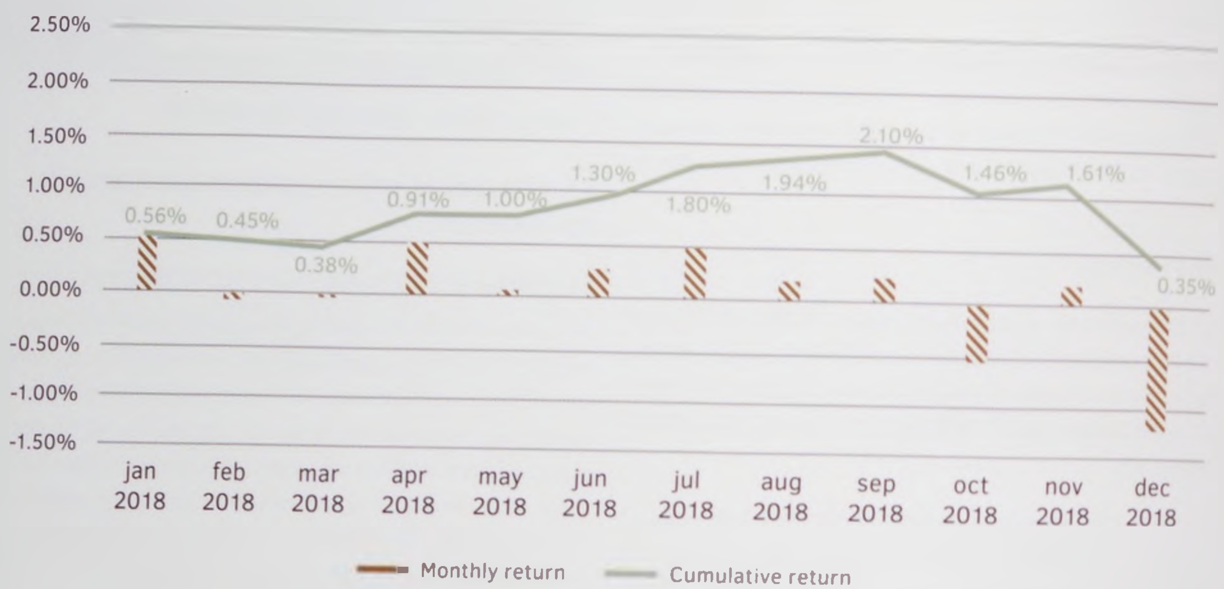
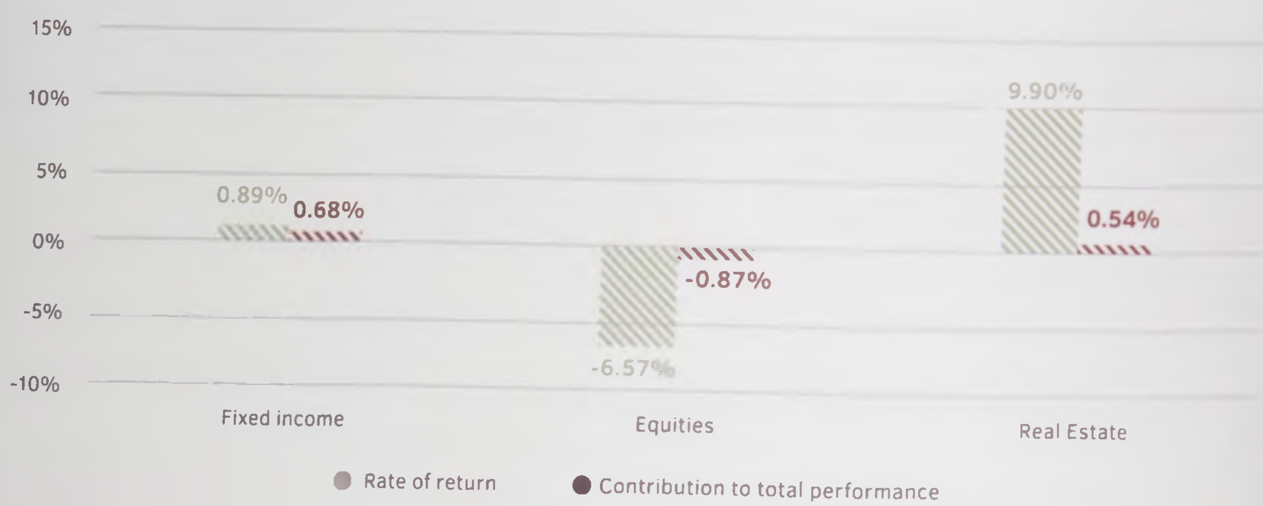


Chart 5.3.2. Cumulative monthly performance (in local currency)



In 2018, annual returns for fixed income, equity (public and private) and real estate investments were 0.89%, -6.57%, and 9.90%, respectively, while their corresponding contributions to the total performance of the investment portfolio (0.35%) accounted for 0.68%, -0.87% and 0.54% (Chart 5.3.3).

Chart 5.3.3. Performance of asset classes and their contribution to total performance (0.35%)*



*Performance of the Gold investments is not included into the total performance results because it is treated as FX effect

Chart 5.3.4. Cumulative monthly fixed income performance

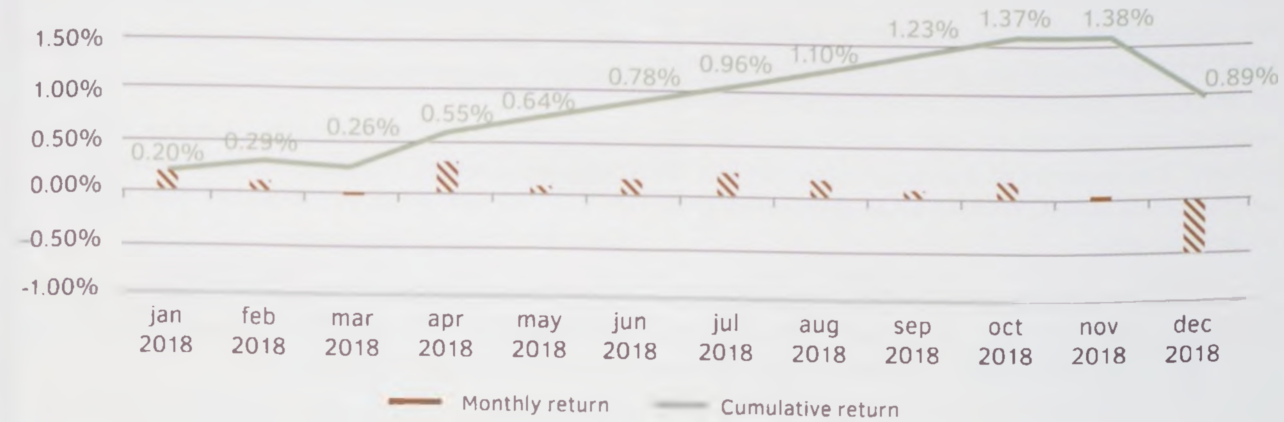


Chart 5.3.5. Cumulative monthly equity performance

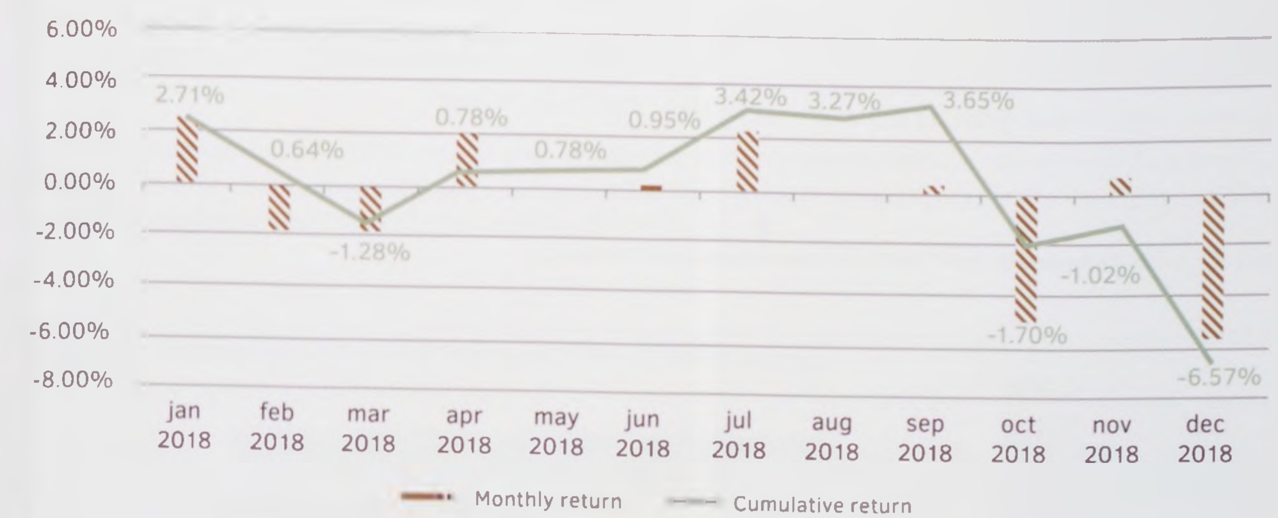
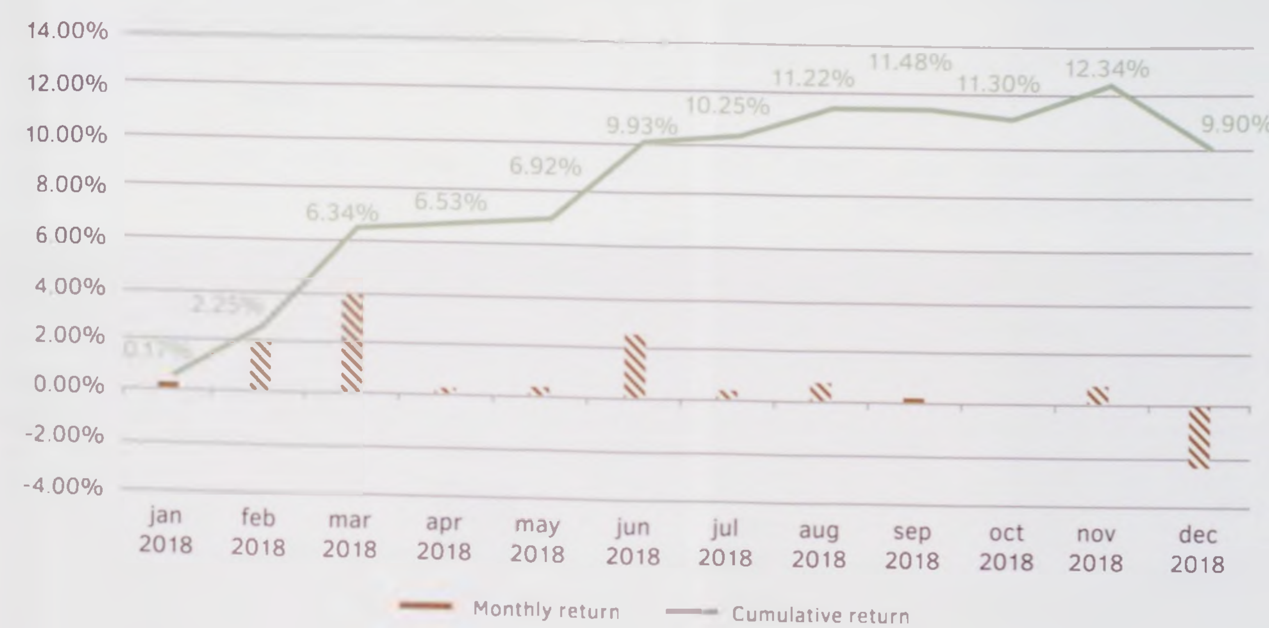


Chart 5.3.6. Cumulative monthly real estate performance



5.4. RISK MANAGEMENT

Risk management and risk monitoring procedures of SOFAZ encompass analysis across risk classes. Market risk and credit risk indicators, as well as other relevant measures, are reported for both internal and external audience. The measures of assessing market risk include duration, Value at Risk, tracking error, scenario analysis, stress tests, etc.

To monitor the risk of divergence of SOFAZ's sub-portfolio returns from their passively tracked benchmarks, tracking errors are continually observed. Ex-ante tracking error limits for the equity sub-portfolios managed by UBS Global Asset Management (UBS), State Street Global Advisors (SSgA), Mellon Investments Corporation (Mellon), BlackRock Investment Management (BlackRock), and Sumitomo Mitsui Trust International (Sumitomo) are established at the level of 30 bps on an annual basis. As of 31 December 2018, the tracking errors on an annual basis were 12 bps, 13 bps, 9 bps, 13 bps, and 7 bps for the MSCI World index mandate portfolios managed by UBS, SSgA, Mellon, BlackRock, and Sumitomo, respectively, and 21 bps for the MSCI Europe ex UK index mandate portfolio managed by UBS.

For the purpose of internal risk management, Value at Risk (VaR) is a common, well-recognized and valuable measure of total risk. We obtain VaR of the portfolio using Monte Carlo and historical simulations.

As of 31 December 2018, SOFAZ's 20 day horizon 95% VaR accounted for USD 233 million compared to USD 258 million at the end of the previous year.

The calculation of VaR and contributions to VaR of different sub-portfolios is based on local returns, since the impact of FX fluctuations might considerably skew the results, especially those of the fixed income instruments. However, due to the minor impact of FX fluctuations on the VaR of equities, FX effect is not excluded from the results of the latter.

Chart 5.4.1. Contribution to total VaR by asset classes (ex FX effect)

Chart 5.4.2. Contribution to equity VaR

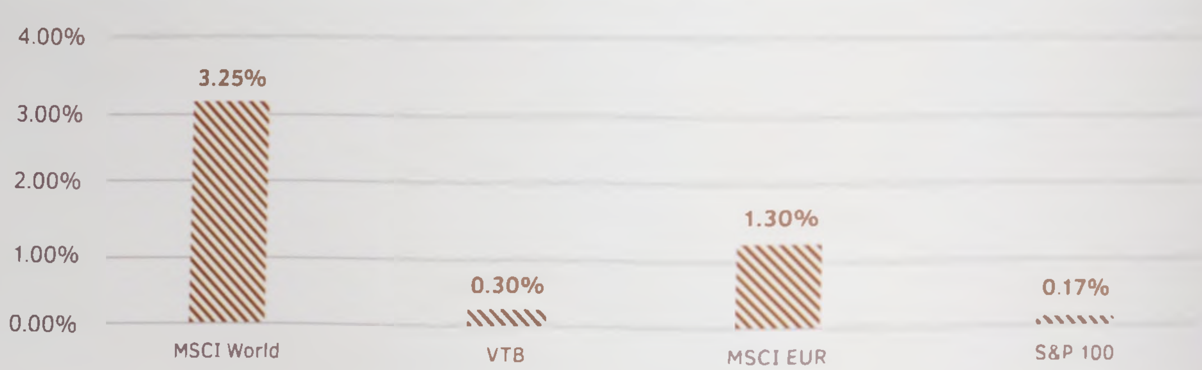
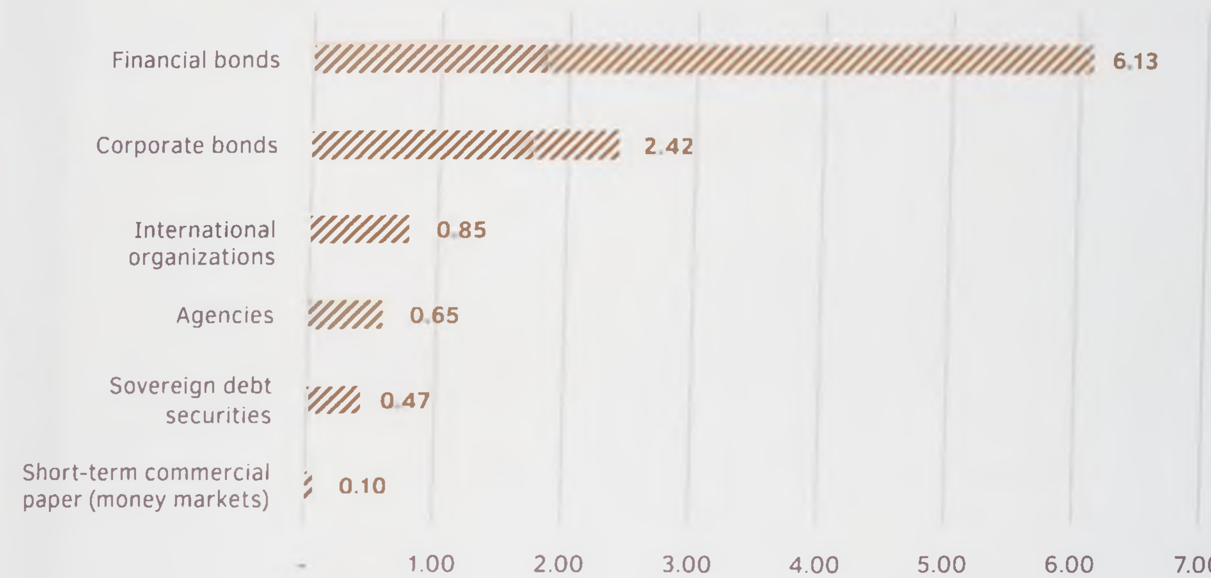
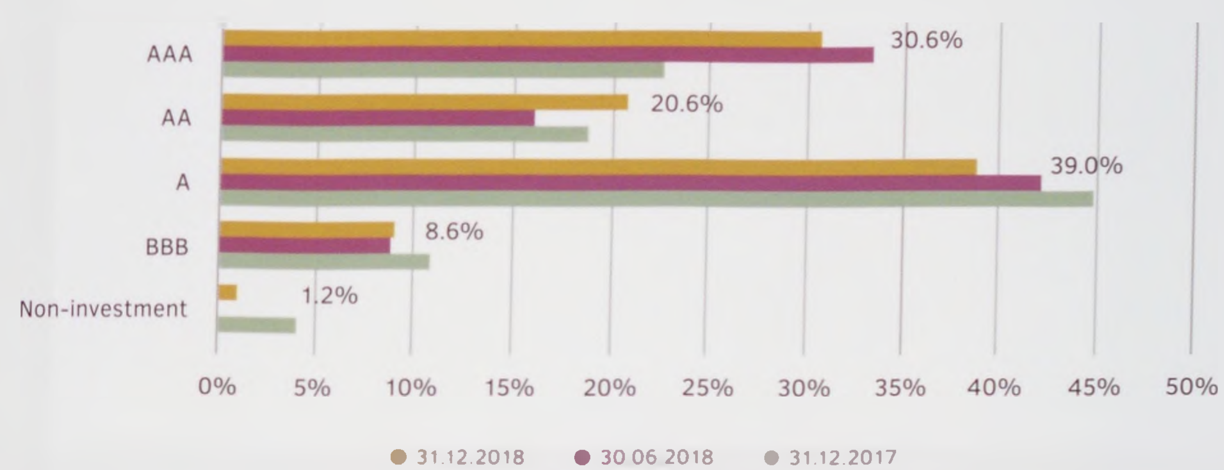


Chart 5.4.3. Contribution to fixed income VaR by product types (ex FX effect, bps)



Credit risk management is another crucial part of SOFAZ's risk procedures. SOFAZ's "Investment Guidelines" sets restrictions on the credit ratings of issuers and securities. The Chart 5.4.4 represents the change in the composition of the fixed income portfolio by credit rating from 2017 to 2018.

Chart 5.4.4. Composition of the fixed income portfolio by credit ratings



The First Offshore Oil Platform in the World

In the second half of the XX century, the process of industrialization was rapidly developing in Azerbaijan. Many unique projects were implemented in those years. One of them was "Neft Dashlari" – the Oil Stones project, i.e. the first oil platform in the world. This was an oil field built on offshore pier posts, creating a type of offshore city. Naturally, the idea of this marvel of engineering arose out of oil production.

In 1949, oil from the Caspian Sea gushed from Neft Dashlari, and this was the beginning of a new stage in oil extraction in offshore oil platform. Azerbaijan started deep-water oil extraction for the first time in the world.

Neft Dashlari infrastructure created by oilmen and builders' generations, will stay in the memory for a long time as a monument embodying the power of the human soul capable of managing nature.

Source: Wikipedia online encyclopedia
The official website of Guinness World Records book

1949

100

YEARS
of
PRIDE

1918-2018

CITY BUILT AT OIL PLATFORMS IN THE CASPIAN SEA | OIL ROCKS, 1961

6. 2018 SOFAZ'S BUDGET EXECUTION

SOFAZ's budget for 2018 was approved by the Presidential Decree № 1770 from December 28, 2017. In 2018, the Fund's budgetary revenues and expenditures were projected to constitute AZN 11 559 956.2 thousand and AZN 9 730 221.8 thousand, respectively. Moreover, the Presidential Order as of July 17, 2018 introduced certain amendments to the SOFAZ's 2018 budget. Based on these amendments that were introduced within the framework of the policy of specifying the consolidated budget, the projected revenues of the SOFAZ's budget were raised from AZN 11 559 956.2 thousand to AZN 15 310 823.9 thousand, while the expenditures increased from AZN 9 730 221.8 thousand up to AZN 11 480 221.8 thousand.

As of January 1, 2018 SOFAZ's assets amounted to AZN 60 304.3 million, or USD 35 806.5 million. Throughout the reference year, SOFAZ's assets have risen by USD 2 708.7 million, or 7.6%, eventually reaching USD 38 515.2 million. At the same time, the SOFAZ's assets as expressed in the national currency have grown by AZN 4 601.3 million (7.6%) and reached AZN 64 905.6 million by the end of the year.

In 2018, SOFAZ's budget revenues constituted AZN 17 614.1 million, or USD 10 361.0 million, meaning that the sum envisaged in the budget plan (AZN 15 310.8 million) was executed at the level of 115.0%. The overall revenues as expressed in US dollars were 46.6 % above the respective figure in 2017 (USD 7 065.5 million).

The actual budget expenditures in 2018 equaled AZN 11 455.6 million or USD 6 738.6 million, 99.8% of the estimated amount (AZN 11 480.2 million).

By the end of the year the budget was executed with a proficit of AZN 6 158.5 million, or USD 3 622.4 million, which is AZN 5 036.5 million or approximately 5 times bigger than in 2017 (AZN 1 122 million). The proficit of USD 3 622.4 million recorded in the reporting period was directed to savings.

Revenues. In 2018, the revenues accrued to SOFAZ were formed from the sales of the Republic of Azerbaijan's share of hydrocarbons, fees paid to Azerbaijan for the oil and gas transit through its territory, bonus payments, acreage fees and revenues from the management of SOFAZ's assets.

In 2018, **revenues from the sale of profit oil and gas** constituted AZN 16 645.6 million, or USD 9 791.4 million. The volume of production at the Azeri-Chirag-Guneshli field constituted 213.51 million barrels, which was 4.5% above the forecasted amount (204.4 million barrels). Since oil prices throughout the reference year were higher than projected, the respective revenue item was executed at the level of 25.1% higher than it had been projected in the budget (AZN 13 307.41 million). That is, the average sale price per barrel of oil constituted USD 71 in 2018 as against USD 55 that was forecasted in the approved budget.

During the reporting year in accordance with the agreements between SOCAR (representing the Republic of Azerbaijan) and the buyers on the sales of gas within the framework of the Shahdeniz "Stage 1" project, SOCAR purchased the excess natural gas over the agreed annual level for USD 288.4 million, instead of transferring this amount to SOFAZ. Moreover, SOFAZ did not receive the amounts of USD 134.6 million and USD 227.6 million earned from gas sales in 2016 and 2017, respectively. In total, within the framework of the Shah Deniz "Stage 1" project the sum of USD 650.6 million was not transferred to SOFAZ in 2016-2018.

Acreage fees paid by the foreign investors working in the hydrocarbons production sector made up for another source of SOFAZ's revenues in 2018. In accordance with the terms of the agreement concluded between SOCAR and a company jointly owned by SOCAR and BP Exploration Limited on oil prospecting, exploitation and production sharing at the Shafag-Asiman offshore field situated in the Azerbaijani sector of the Caspian Sea, USD 2.4 million or AZN 4.1 million of acreage fees were transferred to SOFAZ.

In the reporting year, **the bonus payments** received by SOFAZ constituted AZN 765.2 million or USD 450.1 million, having been executed at 100%, compared to the budget plan (AZN 765.2 million).

The revenues obtained from **the transit of oil and gas through the territory of Azerbaijan** in the reference year amounted to USD 10.6 million, or AZN 18.1 million. Compared to the budgetary target of AZN 17 370.0 thousand, the aforementioned item was executed at 104.2%.

The revenues accrued to SOFAZ from the **management of its investment portfolio** equaled USD 106.5 million or

AZN 181.1 million in 2018. Profitability of the investment portfolio was 0.35%, which is below the 2017 level by 1.53%. Negative profitability in global equity markets and transition from classification of "financial assets measured at the amortized cost" to classification of "fair value in profit or loss accounts" in accordance with the requirements of No.9 standart of IFRS are main reasons of low profitability.

Other revenues. Revenues from the sales of assets by investors in accordance with oil and gas contracts amounted to AZN 20 thousand.

Table 6.1. **The budget revenues of SOFAZ in 2018**

№	Revenue sources	Total revenue (AZN million)		Execution rate (%)
		Approved	Actual	
1.	Net income obtained from the sales of hydrocarbons falling into the share of Azerbaijan (excluding expenditures on transportation, customs clearance and banking services, independent surveyor services, marketing and insurance, as well as the shareholder incomes received by SOCAR in the capacity of investor, shareholder or partner in different projects it is a party to)	13 307.4	16 645.6	125.1
2.	Acreage fees paid by investors per land they use for the exploitation of hydrocarbon reserves	4.1	4.1	100.0
3.	Fees from the transit of oil and gas through the territory of the Republic of Azerbaijan	17.4	18.1	104.0
4.	Bonus payments made by investors within the framework of signing or executing oil and gas contracts	765.2	765.2	100.0
5.	Revenues obtained from the management of SOFAZ's assets	1 216.7	181.1	14.9
6.	Other revenues		0.02	
7.	**Total revenues**	**15 310.8**	**17 614.1**	**115.0**
8.	**Extrabudgetary revenues**		**32.5**	

Extrabudgetary revenues. In 2018, SOFAZ's extrabudgetary incomes stemming from the appreciation of the foreign currencies that constitute the SOFAZ's portfolio against manat amounted to AZN 32.5 million.

Expenditures. In 2018, SOFAZ's budget expenditures constituted AZN 11 455.6 million and were executed at the level of 99.8% from the projected amount. In the reference year, SOFAZ's expenditure structure was as follows:

Financing measures aimed at ameliorating social and living conditions of the refugees and internally displaced persons. In 2018, a total sum of AZN 200 million was spent on funding the aforementioned measures, this budget item having been executed at the 100% to the projected level (AZN 200 million).

Upper limit of the transfer from SOFAZ to the state budget. In 2018, a transfer of AZN 10 959 million from SOFAZ to the state budget was executed, 99.9% of the sum approved in the budget project (AZN 10 966 million).

Financing the reconstruction of the Samur-Absheron irrigation system. In 2018, AZN 90 million was spent from SOFAZ's budget for the purpose of financing the project. The project was executed at the 100% level (AZN 90.0 million).

The New Baku-Tbilisi-Gars Railway project. AZN 176.1 million, or USD 103.6 million was put by SOFAZ into the financing of the project in 2018, amounting to 100% of the initially projected sum of AZN 176.1 million.

The "State Program on the education abroad of the Azerbaijani youth in the years of 2007-2015". The State program was financed by SOFAZ at AZN 7.23 million, 44.57% of the sum initially allocated for the respective budget item (AZN 16.22 million). This sum envisages the average amount of AZN 36 000.0 per student which was calculated taking into account the probability of devaluation in the upcoming year. The projected expenditure was also intended to cover expenditures of a group of students who were admitted in the previous academic year but whose financing was temporarily frozen. However, since problems in the education of those students have not been resolved, no financing has been made for them. These were also some students whose tuition fees were paid with the use of amounts refunded to the relevant account of the Ministry in 2018, as well as those whose payments were not ordered in the last 10 days of December 2018. For the reasons mentioned above, the expenditure item for 2018 was less than what was envisaged in the budget.

SOFAZ's administrative expenses. In 2018, SOFAZ's administrative expenditures amounted to AZN 23.3 million or 73% of the respective item as approved in the budget plan (AZN 31.9 million).

Extrabudgetary expenditures. In 2018 SOFAZ's extra-budgetary expenditures related to the revaluation of foreign exchange totalled 1 589.8 million AZN.

Table 6.2. The budget expenditures of SOFAZ in 2018

№	Expenditure items	Expenditure amount (AZN million)		Execution rate (%)
		Approved	Actual	
1.	Financing measures aimed at ameliorating social and living conditions of the refugees and internally displaced persons	200.00	199.98	99.99
2.	Transfer from SOFAZ to the state budget in 2018	10 966.00	10 959.00	99.94
3.	Financing the project on the reconstruction of the Samur-Absheron irrigation system	90.00	90.00	100.00
4.	Financing the new Baku-Tbilisi-Kars railway project	176.13	176.13	100.00
5.	State Program on the education abroad of the Azerbaijani youth in the years of 2007-2015	16.22	7.23	44.57
6.	SOFAZ's administrative expenses	31.88	23.26	72.96
7.	**Total expenses**	**11 480.23**	**11 455.60**	**99.80**
8.	**Extrabudgetary expenditures**		**1 589.80**	

The World's First European Games

In 2015, the first European Games that retained in memories as one of the momentous and spectacular events were held in Baku. The decision of organizing the first ever European Games in the history was taken at the 41st General Assembly of the European Olympic Committee which took place in Rome on December 8, 2012. The Organizing Committee of the European Games was chaired by the First Vice President and First Lady of Azerbaijan, the head of Heydar Aliyev Foundation, member of the Executive Committee of the Azerbaijan Republic National Olympic Committee, and the goodwill ambassador of UNESCO and ISESCO - Ms. Mehriban Aliyeva. 6000 athletes from 49 countries competing in 30 sports had attended Baku 2015 European Games which was held in June, 2015. This grandiose sports' event aroused great interest in the world and attracted thousands of tourists to the country.

Source: The official website of European games
The official website of first European games

2015

100

YEARS
of
PRIDE

1918-2018

OPENING CEREMONY OF THE FIRST EUROPEAN GAMES | BAKU OLYMPIC STADIUM, BAKU, 2015

7. CONSOLIDATED FINANCIAL STATEMENTS OF SOFAZ

31 December 2018

International Financial Reporting Standards
Consolidated Financial Statements and
Independent Auditor's Report

CONTENT

pwc

Independent Auditor's Report

To the Supervisory Board of the State Oil Fund of the Republic of Azerbaijan:

Our opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the State Oil Fund of the Republic of Azerbaijan (the "SOFAZ") and its subsidiaries (together – the "Fund") as at 31 December 2018, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

What we have audited

The Fund's consolidated financial statements comprise:

- the consolidated statement of financial position as at 31 December 2018;
- the consolidated statement of profit and loss and other comprehensive income for the year then ended;
- the consolidated statement of changes in equity for the year ended;
- the consolidated statement of cash flows for the year then ended; and
- the notes to the consolidated financial statements, which include significant accounting policies and other explanatory information.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Fund in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code). We have fulfilled ethical responsibilities in accordance with the IESBA Code.

Responsibilities of management and those charged with governance for the consolidated financial statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Fund's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Fund or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Fund's financial reporting process

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Fund's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Fund to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Fund to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

PricewaterhouseCoopers Audit Azerbaijan LLC

11 April 2019
Baku, the Republic of Azerbaijan

PricewaterhouseCoopers Audit Azerbaijan MMC
Landmark Office Plaza III, 12th floor, Nizami 90A street
AZ 1010 Baku, Azerbaijan
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Consolidated statement of financial position

In thousands of Azerbaijani Manats	Notes	31 December 2018	31 December 2017
Assets			
Non-current assets			
Investment properties	10	2,584,684	2,763,757
Property and equipments		127,487	132,992
Intangible assets		5,407	8,204
Investments in joint ventures	11	1,167,214	979,598
Financial assets at amortised cost		-	5,199,931
Total non-current assets		**3,884,792**	**9,084,482**
Current assets			
Cash and cash equivalents	7	1,264,588	2,747,381
Financial assets at fair value through profit or loss	8	57,338,275	46,933,160
Gold bullion	9	3,558,246	2,137,212
Financial assets at amortised cost		-	137,285
Other current assets		25,821	32,888
Total current assets		**62,186,930**	**51,987,926**
TOTAL ASSETS		**66,071,722**	**61,072,408**
Equity			
Contributed capital	12	33,689,328	27,688,603
Foreign currency translation reserve		766,965	1,173,876
Retained earnings		30,592,664	31,656,494
Equity attributable to the owner		65,048,957	60,518,973
Non-controlling interest		8,436	8,020
Total equity		**65,057,393**	**60,526,993**
Liabilities			
Non-current liabilities			
Borrowings of subsidiaries		935,981	469,979
Tenancy deposits		48,414	40,087
Deffered tax liability		13,780	16,408
Other non-current liabilities		-	3,375
Total non-current liabilities	13	**998,175**	**529,849**
Current liabilities		**16,154**	**15,566**
TOTAL LIABILITIES		**1,014,329**	**545,415**
TOTAL EQUITY AND LIABILITIES		**66,071,722**	**61,072,408**

The notes set out on pages 82 to 125 form an integral part of these consolidated financial statements.

Consolidated statement of profit and loss and other comprehensive income

In thousands of Azerbaijani Manats	Notes	2018	2017
Interest income calculated using the effective interest method		86,042	295,820
Interest income from financial assets at fair value through profit or loss	14	840,516	502,314
Dividend income		266,518	178,967
Net (loss)/gain on foreign currency translation differences	15	(1,411,237)	744,033
Net (loss)/gain on financial assets at fair value through profit or loss	16	(847,509)	73,663
Net gain on gold bullions	9	32,497	168,743
Net fair value (loss)/gain on revaluation of investment properties	10	(108,674)	15,466
Rental income		167,236	92,063
Other operating income		271,253	16,426
Total operating income / (loss)		**(703,358)**	**2,087,495**
Operating expenses	17	(103,513)	(68,744)
Share of after tax results of joint venture	11	38,887	(1,491)
Profit / (loss) before income tax		**(767,984)**	**2,017,260**
Income tax	19	(455)	(17,937)
Net profit / (loss) for the year		**(768,439)**	**1,999,323**
Other comprehensive income:			
Items that may be reclassified subsequently to profit or loss			
Translation of financial information of foreign operations to presentation currency		(404,055)	224,386
Other comprehensive income / (loss) for the year		**(404,055)**	**224,386**
TOTAL COMPREHENSIVE INCOME / (LOSS) FOR THE YEAR		**(1,172,494)**	**2,223,709**
Profit / (loss) is attributable to:			
- The owner		(768,927)	1,998,045
- Non-controlling interest		488	1,278
Profit / (loss) for the year		**(768,439)**	**1,999,323**
Total comprehensive income / (loss) is attributable to:			
- The owner		(1,175,838)	2,219,681
- Non-controlling interest		3,344	4,028
TOTAL COMPREHENSIVE INCOME / (LOSS) FOR THE YEAR		**(1,172,494)**	**2,223,709**

The notes set out on pages 82 to 125 form an integral part of these consolidated financial statements.

Consolidated statement of changes in equity

In thousands of Azerbaijani Manats	Note	Attributable to the Owner				Non-controlling interest	Total Equity
		Contributed capital	Currency translation reserve	Retained earnings	Total		
At 1 January 2017		**27,632,157**	**952,240**	**29,658,449**	**58,242,846**	**7,208**	**58,250,054**
Profit for the year		-	-	1,998,045	1,998,045	1,278	1,999,323
Other comprehensive income		-	221,636	-	221,636	2,750	224,386
Total comprehensive income for 2017		**-**	**221,636**	**1,998,045**	**2,219,681**	**4,028**	**2,223,709**
Contributions received	12	11,053,917	-	-	11,053,917	-	11,053,917
Exchange translation differences		-	-	-	-	(3,216)	(3,216)
Transfers to the State Budget	18	(6,100,000)	-	-	(6,100,000)	-	(6,100,000)
Transfers for construction of "Star" oil refinery complex	18	(735,422)	-	-	(735,422)	-	(735,422)
Transfers to the State Committee for Affairs of Refugees and Internally Displaced Persons and Social Development Fund of the Internally Displaced Persons of the Republic of Azerbaijan	18	(105,000)	-	-	(105,000)	-	(105,000)
Transfers for the reconstruction of Samur Absheron Irrigation system	18	(69,997)	-	-	(69,997)	-	(69,997)
Transfers for the construction of new Baku-Tbilisi-Kars railway line	18	(20,557)	-	-	(20,557)	-	(20,557)
Transfers for the State Program on "Education of Azerbaijani youth abroad"	18	(17,010)	-	-	(17,010)	-	(17,010)
Transfers to the Central Bank of the Republic of Azerbaijan	18	(3,949,485)	-	-	(3,949,485)	-	(3,949,485)
Balance at 31 December 2017		**27,688,603**	**1,173,876**	**31,656,494**	**60,518,973**	**8,020**	**60,526,993**
Adoption of IFRS 9:							
-effect of measurement of financial assets at fair value, which previously were measured at amortised cost		-	-	(294,903)	(294,903)	-	(294,903)
Restated balance at 1 January 2018		**27,688,603**	**1,173,876**	**31,361,591**	**60,224,070**	**8,020**	**60,232,090**
Profit / (loss) for the year		-	-	(768,927)	(768,927)	488	(768,439)
Other comprehensive income / (loss)		-	(406,911)	-	(406,911)	2,856	(404,055)
Total comprehensive income / (loss) for 2018		**-**	**(406,911)**	**(768,927)**	**(1,175,838)**	**3,344**	**(1,172,494)**
Contributions received	12	17,433,067	-	-	17,433,067	-	17,433,067
Exchange translation differences		-	-	-	-	(2,928)	(2,928)
Transfers to the State Budget	18	(10,959,000)	-	-	(10,959,000)	-	(10,959,000)
Transfers to the State Committee for Affairs of Refugees and Internally Displaced Persons and Social Development Fund of the Internally Displaced Persons of the Republic of Azerbaijan	18	(199,979)	-	-	(199,979)	-	(199,979)
Transfers for the reconstruction of Samur Absheron Irrigation system	18	(89,999)	-	-	(89,999)	-	(89,999)
Transfers for the construction of new Baku-Tbilisi-Kars railway line	18	(176,128)	-	-	(176,128)	-	(176,128)
Transfers for the State Program on "Education of Azerbaijani youth abroad"	18	(7,236)	-	-	(7,236)	-	(7,236)
Balance at 31 December 2018		**33,689,328**	**766,965**	**30,592,664**	**65,048,957**	**8,436**	**65,057,393**

The notes set out on pages 82 to 125 form an integral part of these consolidated financial statements.

Consolidated Statement of Cash Flows

In thousands of Azerbaijani Manats	Notes	2018	2017
Cash flows from operating activities:			
Profit / (loss) before income tax expense		(767,984)	2,017,260
Adjustments to reconcile result to net cash used in operating activities			
Depreciation of property and equipment		5,695	5,757
Amortization of intangible assets		2,783	3,263
Unrealized (gain)/loss on change in fair value of financial assets at fair value through profit or loss	5.16	1,294,052	(75,740)
Net unrealized (gain) /loss on foreign currency translation differences		1,071,438	(874,299)
Net gain on revaluation of gold bullion	9	(32,497)	(168,743)
Fair value (gain)/loss on revaluation of investment properties	10	108,674	(15,466)
Share of after tax results of joint venture	11	(38,887)	1,491
Write-down of VAT receivables and current income tax asset		13,596	-
Interest income		(926,558)	(798,134)
Dividend income		(266,518)	(178,967)
Changes in operating assets and liabilities:			
Increase in financial assets at fair value through profit or loss	8	(7,683,782)	(4,279,839)
Purchase of gold bullions	9	(1,388,537)	-
Decrease in financial assets at amortised cost		-	74,943
Increase in investment properties	10	(6,863)	(4,412)
Increase in investment in joint venture	11	(151,646)	(193,500)
Decrease/(increase) in other assets		(6,557)	8,900
(Decrease)/increase in current liabilities		588	2,917
Net cash used in operating activities		**(8,773,003)**	**(4,474,569)**
Income tax paid		-	(1,529)
Net cash used in operating activities before income tax		**(8,773,003)**	**(4,476,098)**
Cash flows from investing activities:			
Interest received		758,490	718,264
Dividend received		266,518	178,967
Purchase of property and equipment		(176)	-
Decrease in other non-current assets		-	2,280
Net cash from investing activities		**1,024,832**	**899,511**
Cash flows from financing activities:			
Contributions received	12	17,433,067	11,053,917
Transfers to the State Budget	18	(10,959,000)	(6,100,000)
Transfers to the Central Bank of the Republic of Azerbaijan	18	-	(3,949,485)
Transfers for construction of "Star" oil refinery complex	18	-	(735,422)
Transfers for the reconstruction of Samur Absheron Irrigation system	18	(89,999)	(69,997)
Transfers to the State Committee for Affairs of Refugees and Internally Displaced Persons and Social Development Fund of the Internally Displaced Persons of the Republic of Azerbaijan	18	(199,979)	(105,000)
Transfers for the construction of new Baku-Tbilisi-Kars railway line	18	(176,128)	(20,557)
Transfers for the State Program on "Education of Azerbaijani youth abroad"	18	(7,236)	(17,010)
Proceeds from borrowings	13	456,300	-
Proceeds from other non-current liabilities		2,330	1,388
Net cash from financing activities		**6,459,355**	**57,834**
Effect of exchange rate changes on cash and cash equivalents		**(193,977)**	**48,099**
Net decrease in cash and cash equivalents		**(1,482,793)**	**(3,470,654)**
Cash and cash equivalents, beginning of the year	7	**2,747,381**	**6,218,035**
Cash and cash equivalents, end of the year	7	**1,264,588**	**2,747,381**

The notes set out on pages 82 to 125 form an integral part of these consolidated financial statements.

1. THE STATE OIL FUND OF THE REPUBLIC OF AZERBAIJAN AND ITS OPERATIONS

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards for the year ended 31 December 2018 for the State Oil Fund of the Republic of Azerbaijan ("SOFAZ") and its subsidiaries (the "Fund").

SOFAZ was incorporated and is domiciled in the Azerbaijan Republic.

Principal Activity. The State Oil Fund of the Republic of Azerbaijan was established by Decree #240 of the President of the Republic of Azerbaijan on the "Establishment of The State Oil Fund of the Republic of Azerbaijan" dated 29 December 1999 (the "Decree"). The purpose of SOFAZ is to ensure the accumulation, effective management, and use of income and other inflows generated from agreements related to oil and gas exploration and development, as well as, from SOFAZ's own activities, for the benefit of citizens and future generations of the Republic of Azerbaijan.

In accordance with the Decree and the Regulations (discussed below), SOFAZ is an extra-budget state organization, formed as a separate legal entity, which is accountable and responsible to the President of the Republic of Azerbaijan.

The consolidated financial statements include the financial statements of SOFAZ and its direct and indirect subsidiaries listed in the following table and the after tax results of it's joint venture:

Subsidiary	% interest		Country	Date of establishment	Date of acquisition	Industry
	2018	2017				
SOFAZ RE Limited	100	100	Jersey	22-May-12	-	Property management
SOFAZ RE UK L.P	100	100	Jersey	6-Aug-12	-	Property management
SOFAZ RE Min Limited	100	100	Jersey	13-Aug-12	-	Property management
78 St James`s Street Unit Trust	100	100	Jersey	2-Oct-12	-	Property management
JSC Tverskaya, 16	100	100	Russian Federation	29-Jun-93	21-Dec-12	Property management
SOFAZ RE Europe Holding S.a.r.l	100	100	Luxembourg	31-Oct-12	-	Property management
SOFAZ RE Europe S.a.r.l.	100	100	Luxembourg	31-Oct-12	-	Property management
SCI 8 Place Vendome	100	100	France	14-Nov-12	-	Property management
MAPS 21	100	100	South Korea	30-Oct-11	31-Mar-14	Property management
Godo Kaisha GK001	98	98	Japan	21-Aug-15	26-Aug-15	Property management
SOFAZ RE Fund S.a.r.l	100	100	Luxembourg	27-May-15	-	Investment management
SOFAZ PE Fund S.a.r.l	100	100	Luxembourg	28-Sep-15	-	Investment management
SOFAZ Italy Fund	100	100	Italy	19-Oct-15	-	Property management
SOFAZ Europe S.C.S.	100	100	Luxembourg	06-Dec-17	-	Investment management
SOFAZ Fund Limited	100	-	Jersey	28-Dec-18	-	Investment management

Contributions into the Fund are made in accordance with the Regulation of the Fund ("Regulation") approved by Presidential Decree #434 dated 29 December 2000 as amended by Presidential Decrees #849 and #202 on "Amending Certain Legislative Acts Regulating the Operations of The State Oil Fund of the Republic of Azerbaijan" dated 7 February 2003 and 1 March 2005, respectively, and Article 2.3 of the "Regulations on Development and Implementation of the Annual Program of Income and Expenses ("Budget") of the Fund" approved by Presidential Decree #579 dated 12 September 2001 as amended by Presidential Decrees #849 and #202 mentioned earlier. Pursuant to the Regulations of the Fund, contributions are received from the following sources:

a) Agreements on exploration, development and production sharing for oil and gas fields in the territory of the Republic of Azerbaijan including the Azerbaijan Sector of the Caspian Sea, as well as other agreements on oil and gas exploration, development and transportation entered into between the State Oil Company of the Republic of Azerbaijan ("SOCAR") or other authorized state bodies and investors, including:

i. Contributions from the sale of hydrocarbons related to the share of the Republic of Azerbaijan in oil and gas agreements (net of expenditures incurred for hydrocarbons transportation, customs clearance and bank costs, marketing, insurance, and independent surveyor fees) excluding portion related to the participating interest or investment of SOCAR in a project in which SOCAR is an investor, participant or a contracting party;

ii. Bonus payments - the fees payable by foreign oil companies to SOCAR or other relevant authorities of the Republic of Azerbaijan due to signing of an oil and gas contracts and its implementation;

iii. Acreage payments due to SOCAR and/or an authorized state body of the Republic of Azerbaijan from investors for the use of the contract area in connection with oil and gas exploration and development;

iv. Contibutions generated from oil and gas transported over the territory of the Republic of Azerbaijan with the use of the Baku-Supsa export pipeline;

v. Dividends and profit participation revenues falling on the share of the Republic of Azerbaijan in connection with oil and gas agreements implementation (excluding portion related to the participating interest or investment of SOCAR in a project in which SOCAR is an investor, participant or a contracting party).

b) Revenues generated from investment, management, sale and other disposal of the Fund's assets (including financial assets and assets contributed by investors within oil and gas agreements), other non-sale income or revaluation surplus of the Fund's assets in its reporting currency (Azerbaijani manats), etc.;

c) Grants and other free aids;

d) Other revenues and receipts in accordance with the legislation of the Republic of Azerbaijan.

Under the provisions of the Fund's Regulations approved by the President of the Republic of Azerbaijan, SOCAR or an authorized state body implements the collection of the fees listed above and transfers them to SOFAZ

The Regulations exclude the following from the list of sources of the Fund's contribution and assets:

- The rental fees from the use of state property under contracts with foreign companies;
- Contributions from the sale of hydrocarbons related to the participating interest or investment of SOCAR in any project in which SOCAR is an investor, participant or a contracting party; and
- Other proceeds generated from joint activities with foreign companies.

In 2018 and 2017, the Fund was a party to a custody agreement with the Bank of New York Mellon. Management of some portion of the financial assets of the Fund is granted to financial institutions namely DWS International GmbH, the International Bank for Reconstruction and Development (IBRD – World Bank Group), State Street Global Advisors Limited (SSGA), UBS Asset Management (UK) LTD, Sumitomo Mitsui Trust International LTD, Blackrock Investment Management (UK) LTD and Mellon Capital Management Corporation. Under the custody agreement the financial institutions hold securities purchased by the Fund, whereas in accordance with the investment management agreements the financial institutions manage the Fund's investments based on general investment policies established by the Fund.

SOFAZ's registered and actual office address is 165, Heydar Aliyev Avenue, Baku, Azerbaijan, AZ1029.

These consolidated financial statements as of and for the year ended 31 December 2018 are authorized for issue by the Fund's Management on 11 April 2019.

Presentation currency. These consolidated financial statements are presented in thousands of Azerbaijani Manats ("AZN"), unless otherwise stated.

2. OPERATING ENVIRONMENT OF THE FUND

In 2018, multi-lateral and consistent reforms were continued in our country, comprehensive stimulus measures were taken to increase non-oil exports, balanced development of regions was provided, state-entrepreneurial relations and business-investment environment were improved, non-oil sector was developed, incentives in private sector were applied, state support to the agrarian sector and, small and medium entrepreneurship were kept in the spotlight.

An analysis of the country's current socioeconomic situation shows that, implemented ongoing reforms have increased the sustainability of the economy and provided macroeconomic stability in the country.

The monetary policy carried out in 2018 is aimed at ensuring low and stable inflation. Decisions were made to mitigate the monetary policy, taking into account the significant decline in inflation and inflation expectations throughout the year. These decisions served to support economic growth without undermining macroeconomic stability. The implementation of the "regulated floating regime" of manat by the Central Bank of the Republic of Azerbaijan (CBAR), helped to preserve the stability of the exchange rate in 2018. Price of 1 USD in terms of manat equaled 1.70 and remained almost unchanged throughout 2018. Average annual inflation rate strongly moderated since 2017 and constituted a mere 2.3%. The GDP of Azerbaijan rose to AZN 79 797.3 million in nominal figures, while its growth constituted 1.4% in real terms (0.1% in 2017 and -3.1% in 2016).

In line with the new reform curriculum, reorganization of taxation principles and improvement of tax administration, work on the strategic road maps, introduction of modern innovative technologies, transparency, increasing mutual trust between taxpayers and tax authorities, etc. comprehensive measures were taken. In order to solve a number of issues arising from the demands of modern challenges, remove some gaps in tax legislations a new edition of the Tax Code has been prepared by taking into account opinions and suggestions of various government agencies and public organizations, associations, entrepreneurs.

In 2018, Standard & Poor's, international credit agency, kept Azerbaijan's long-term and short-term sovereign loan rating at 'BB+/B'. The agency linked keeping the rating unchanged with the sound fiscal position of the country, in particular due to the foreign currency reserves of SOFAZ.

The Fund's management observes these developments related to the economic environment and takes precautionary measures as it considers necessary in order to support the sustainable development of the Fund's strategy. However, the future effects of the current economic situation are difficult to predict and management's current expectations and estimates could differ from actual results.

3. SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation. These consolidated financial statements have been prepared in accordance with IFRS under the historical cost convention, as modified by the initial recognition of financial instruments based on fair value, and by the revaluation of premises and equipment, investment properties, gold bullions, and instruments categorised at fair value through profit or loss ("FVTPL"). The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. Apart from the accounting policy changes resulting from the adoption of IFRS 9 and IFRS 15 effective from 1 January 2018, these policies have been consistently applied to all the periods presented, unless otherwise stated. (refer to Notes 5 and 27). The principal accounting policies in respect of financial instruments applied untill 31 December 2017 are presented in Note 27.

The preparation of the financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Fund's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

The Fund presents its consolidated statement of financial position separating current and non-current assets and liabilities. An analysis regarding recovery or settlement within 12 months after the statement of financial position date (current) and more than 12 months after the statement of financial position date (non-current) is presented.

Consolidated financial statements. Subsidiaries are those investees, including structured entities, that the Fund controls because the Fund (i) has power to direct the relevant activities of the investees that significantly affect their returns, (ii) has exposure, or rights, to variable returns from its involvement with the investees, and (iii) has the ability to use its power over the investees to affect the amount of the investor's returns. The existence and effect of substantive rights, including substantive potential voting rights, are considered when assessing whether the Fund has power over another entity. For a right to be substantive, the holder must have a practical ability to exercise that right when decisions about the direction of the relevant activities of the investee need to be made. The Fund may have power over an investee even when it holds less than the majority of the voting power in an investee. In such a case, the Fund assesses the size of its voting rights relative to the size and dispersion of holdings of the other vote holders to determine if it has de-facto power over the investee. Protective rights of other investors, such as those that relate to fundamental changes of the investee's activities or apply only in exceptional circumstances, do not prevent the Fund from controlling an investee. Subsidiaries are consolidated from the date on which control is transferred to the Fund (acquisition date) and are deconsolidated from the date on which control ceases.

The acquisition method of accounting is used to account for the acquisition of subsidiaries. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest.

The Fund measures non-controlling interest that represents present ownership interest and entitles the holder to a proportionate share of net assets in the event of liquidation on a transaction by transaction basis, either at: (a) fair value, or (b) the non-controlling interest's proportionate share of net assets of the acquiree. Non-controlling interests that are not present ownership interests are measured at fair value.

Goodwill is measured by deducting the net assets of the acquiree from the aggregate of the consideration transferred for the acquiree, the amount of non-controlling interest in the acquiree and the fair value of an interest in the acquiree held immediately before the acquisition date. Any negative amount is recognised in profit or loss, after management reassesses whether it identified all the assets acquired and all the liabilities and contingent liabilities assumed and reviews the appropriateness of their measurement.

The consideration transferred for the acquiree is measured at the fair value of the assets given up, equity instruments issued and liabilities incurred or assumed, including the fair value of assets or liabilities from contingent consideration arrangements, but excludes acquisition related costs such as advisory, legal, valuation and similar professional services. Transaction costs related to the acquisition of and incurred for issuing equity instruments are deducted from equity; transaction costs incurred for issuing debt as part of the business combination are deducted from the carrying amount of the debt and all other transaction costs associated with the acquisition are expensed.

Intercompany transactions, balances and unrealised gains on transactions between group companies are eliminated; unrealised losses are also eliminated unless the cost cannot be recovered. SOFAZ and all of its subsidiaries use uniform accounting policies consistent with the Fund's policies. When necessary, amounts reported by subsidiaries have been adjusted to conform with the Fund's accounting policies.

Non-controlling interest is that part of the net results and of the equity of a subsidiary attributable to interests which are not owned, directly or indirectly, by SOFAZ. Non-controlling interest forms a separate component of the Fund's equity.

Purchases and sales of non-controlling interests. The Fund applies the economic entity model to account for transactions with owners of non-controlling interest in transactions that do not result in a loss of control. Any difference between the purchase consideration and the carrying amount of non-controlling interest acquired is recorded as a capital transaction directly in equity. The Fund recognises the difference between sales consideration and the carrying amount of non-controlling interest sold as a capital transaction in the statement of changes in equity.

Joint arrangements. Under IFRS 11 investments in joint arrangements are classified as either joint operations or joint ventures depending on the contractual rights and obligations of each investor. SOFAZ has assessed the nature of its joint arrangements and determined them to be joint ventures. Joint ventures are accounted for using the equity method.

Under the equity method of accounting, interests in joint ventures are initially recognised at cost and adjusted thereafter to recognise the Fund's share of the post-acquisition profits or losses and movements in other comprehensive income. When the Fund's share of losses in a joint venture equals or exceeds its interests in the joint ventures (which includes any long-term interests that, in substance, form part of the Fund's net investment in the joint ventures), the Fund does not recognise further losses, unless it has incurred obligations or made payments on behalf of the joint ventures.

Unrealised gains on transactions between the Fund and its joint ventures are eliminated to the extent of the Fund's interest in the joint ventures. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of the joint ventures have been changed where necessary to ensure consistency with the policies adopted by the Fund.

Disposals of subsidiaries, associates or joint ventures. When the Fund ceases to have control or significant influence, any retained interest in the entity is remeasured to its fair value at the date when control is lost, with the change in carrying amount recognised in profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognised in other comprehensive income in respect of that entity, are accounted for as if the Fund had directly disposed of the related assets or liabilities. This may mean that amounts previously recognised in other comprehensive income are reclassified to profit or loss.

If the ownership interest in an associate is reduced but significant influence is retained, only a proportionate share of the amounts previously recognised in other comprehensive income are reclassified to profit or loss where appropriate.

Foreign currency translation. The functional currency of each of the Fund's consolidated entities is the currency of the primary economic environment in which the entity operates. The functional currency of SOFAZ and the Fund's presentation currency, is the national currency of the Republic of Azerbaijan, Azerbaijani Manat ("AZN"). The consolidated financial statements are presented in Azerbaijani Manat ("AZN"), which is the Fund's presentation currency.

Transactions and balances. Monetary assets and liabilities are translated into each entity's functional currency at the official exchange rate of the Central Bank of the Republic of Azerbaijan ("CBAR") at the respective end of the reporting period. Foreign exchange gains and losses resulting from the settlement of the transactions and from the translation of monetary assets and liabilities into each entity's functional currency at year-end official exchange rates of the CBAR are recognised in profit or loss. Translation at year-end rates does not apply to non-monetary items that are measured at historical cost. Non-monetary items measured at fair value in a foreign currency, including equity investments, are translated using the exchange rates at the date when the fair value was determined. Effects of exchange rate changes on non-monetary items measured at fair value in a foreign currency are recorded as part of the fair value gain or loss.

Group companies. Loans between group entities and related foreign exchange gains or losses are eliminated upon consolidation. However, where the loan is between group entities that have different functional currencies, the foreign exchange gain or loss cannot be eliminated in full and is recognized in the consolidated profit or loss, unless the loan is not expected to be settled in the foreseeable future and thus forms part of the net investment in foreign operation. In such a case, the foreign exchange gain or loss is recognized in other comprehensive income.

The results and financial position of each group entity (the functional currency of none of which is a currency of a hyperinflationary economy) are translated into the presentation currency as follows:
(i) assets and liabilities for each statement of financial position are translated at the closing rate at the end of the respective reporting period;
(ii) income and expenses are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); (iii) components of equity are translated at the historic rate; and (iv) all resulting exchange differences are recognised in other comprehensive income.

When control over a foreign operation or a subsidiary with a functional currency other than the functional or presentation currency of the Fund is lost, the exchange differences recognised previously in other comprehensive income are reclassified to profit or loss for the year as part of the gain or loss on disposal. On partial disposal of a subsidiary without loss of control, the related portion of accumulated currency translation differences is reclassified to non-controlling interest within equity.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate. Exchange differences arising are recognised in other comprehensive income.

At 31 December 2018, the principal rates of exchange used for translating foreign currency balances was USD 1 = AZN 1.7000; EUR 1 = AZN 1.9468; KRW 100 = AZN 0.1521; GBP 1 = AZN 2.1529; JPY 100 = AZN 1.5366; RUB 1 = AZN 0.0245 (2017: USD 1 = AZN 1.7001; EUR 1 = AZN 2.0307; KRW 100 = AZN 0.1591; GBP 1 = AZN 2.2881; JPY 100 = AZN 1.5079; RUB 1 = AZN 0.0295). The principal average rate of exchange used for translating income and expenses was USD 1 = AZN 1.7000; EUR 1 = AZN 2.0069; KRW 100 = AZN 0.1545; GBP 1 = AZN 2.2679; JPY 100 = AZN 1.5384; RUB 1 = AZN 0.0272 (2017: USD 1 = AZN 1.7205; EUR 1 = AZN 1.9464; KRW 100 = AZN 0.1523; GBP 1 = AZN 2.2196; JPY 100 = AZN 1.5347; RUB 1 = AZN 0.0295).

Investment property. Investment property is property held by the Fund to earn rental income or for capital appreciation, or both and which is not occupied by the Fund. Investment property includes assets under construction for future use as investment property.

Investment property is initially recognised at cost, including transaction costs, and subsequently remeasured at fair value updated to reflect market conditions at the end of the reporting period. Fair value of investment property is the price that would be received from sale of the asset in an orderly transaction, without deduction of any transaction costs. The best evidence of fair value is given by current prices in an active market for similar property in the same location and condition.

In the absence of current prices in an active market, the Fund considers information from a variety of sources, including:
(a) current prices in an active market for properties of a different nature, condition or location, adjusted to reflect those differences;
(b) recent prices of similar properties on less active markets, with adjustments to reflect any changes in economic conditions since the date of the transactions that occurred at those prices; and
(c) discounted cash flow projections based on reliable estimates of future cash flows, supported by the terms of any existing lease and other contracts and (when possible) by external evidence such as current market rents for similar properties in the same location and condition, and using discount rates that reflect current market assessments of the uncertainty in the amount and timing of the cash flows.

Market value of the Fund's investment property is determined based on reports of independent appraisers, who hold recognised and relevant professional qualifications and who have recent experience in the valuation of property in the same location and category.

Earned rental income is recorded in profit or loss for the year within rental income. Gains and losses resulting from changes in the fair value of investment property are recorded in profit or loss for the year and presented separately.

Subsequent expenditure is capitalised to the asset's carrying amount only when it is probable that future economic benefits associated with the expenditure will flow to the Fund and the cost can be measured reliably. All other repairs and maintenance costs are expensed when incurred.

Financial instruments – key measurement terms. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The best evidence of fair value is the price in an active market. An active market is one in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

Fair value of financial instruments traded in an active market is measured as the product of the quoted price for the individual asset or liability and the number of instruments held by the entity. This is the case even if a market's normal daily trading volume is not sufficient to absorb the quantity held and placing orders to sell the position in a single transaction might affect the quoted price.

Valuation techniques such as discounted cash flow models or models based on recent arm's length transactions or consideration of financial data of the investees are used to measure fair value of certain financial instruments for which external market pricing information is not available. Fair value measurements are analysed by level in the fair value hierarchy as follows: (i) level one are measurements at quoted prices (unadjusted) in active markets for identical assets or liabilities, (ii) level two measurements are valuations techniques with all material inputs observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices), and (iii) level three measurements are valuations not based on solely observable market data (that is, the measurement requires significant unobservable inputs). Transfers between levels of the fair value hierarchy are deemed to have occurred at the end of the reporting period. Refer to Note 20.

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial instrument. An incremental cost is one that would not have been incurred if the transaction had not taken place. Transaction costs include fees and commissions paid to agents (including employees acting as selling agents), advisors, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs.

Amortised cost ("AC") is the amount at which the financial instrument was recognised at initial recognition less any principal repayments, plus accrued interest, and for financial assets less any allowance for expected credit losses ("ECL"). Accrued interest includes amortisation of transaction costs deferred at initial recognition and of any premium or discount to the maturity amount using the effective interest method. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discount or premium (including fees deferred at origination, if any), are not presented separately and are included in the carrying values of the related items in the consolidated statement of financial position.

The effective interest method is a method of allocating interest income or interest expense over the relevant period, so as to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the gross carrying amount of the financial instrument. The effective interest rate discounts cash flows of variable interest instruments to the next interest repricing date, except for the premium or discount which reflects the credit spread over the floating rate specified in the instrument, or other variables that are not reset to market rates. Such premiums or discounts are amortised over the whole expected life of the instrument. The present value calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate. For assets that are purchased or originated credit impaired ("POCI") at initial recognition, the effective interest rate is adjusted for credit risk, i.e. it is calculated based on the expected cash flows on initial recognition instead of contractual payments.

Financial instruments – initial recognition. Financial instruments at FVTPL are initially recorded at fair value. All other financial instruments are initially recorded at fair value adjusted for transaction costs. Fair value at initial recognition is best evidenced by the transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets. After the initial recognition, an ECL allowance is recognised for financial assets measured at AC and investments in debt instruments measured at fair value through other comprehensive income ("FVOCI"), resulting in an immediate accounting loss.

All purchases and sales of financial assets that require delivery within the time frame established by regulation or market convention ("regular way" purchases and sales) are recorded at trade date, which is the date on which the Fund commits to deliver a financial asset. All other purchases are recognised when the entity becomes a party to the contractual provisions of the instrument.

Financial assets – classification and subsequent measurement – measurement categories. The Fund classifies financial assets in the following measurement categories: FVTPL, FVOCI and AC. The classification and subsequent measurement of debt financial assets depends on: (i) the Fund's business model for managing the related assets portfolio and (ii) the cash flow characteristics of the asset.

Financial assets – classification and subsequent measurement – business model. The business model reflects how the Fund manages the assets in order to generate cash flows – whether the Fund's objective is (i) solely to collect the contractual cash flows from the assets ("hold to collect contractual cash flows",) or (ii) to collect both the contractual cash flows and the cash flows arising from the sale of assets ("hold to collect contractual cash flows and sell") or, if neither of (i) and (ii) is applicable, the financial assets are classified as part of "other" business model and measured at FVTPL.

Business model is determined for a group of assets (on a portfolio level) based on all relevant evidence about the activities that the Fund undertakes to achieve the objective set out for the portfolio available at the date of the assessment. Factors considered by the Fund in determining the business model include the purpose and composition of a portfolio, past experience on how the cash flows for the respective assets were collected, how risks are assessed and managed, how the assets' performance is assessed and how asset managers are compensated. Refer to Note 4 for critical judgements applied by the Fund in determining the business models for its financial assets.

Financial assets – classification and subsequent measurement – cash flow characteristics. Where the business model is to hold assets to collect contractual cash flows or to hold contractual cash flows and sell, the Fund assesses whether the cash flows represent solely payments of principal and interest ("SPPI"). Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are consistent with the SPPI feature. In making this assessment, the Fund considers whether the contractual cash flows are consistent with a basic lending arrangement, i.e. interest includes only consideration for credit risk, time value of money, other basic lending risks and profit margin.

Where the contractual terms introduce exposure to risk or volatility that is inconsistent with a basic lending arrangement, the financial asset is classified and measured at FVTPL. The SPPI assessment is performed on initial recognition of an asset and it is not subsequently reassessed.

Financial assets – reclassification. Financial instruments are reclassified only when the business model for managing the portfolio as a whole changes. The reclassification has a prospective effect and takes place from the beginning of the first reporting period that follows after the change in the business model.

Financial assets impairment – credit loss allowance for ECL. The Fund assesses, on a forward-looking basis, the ECL for debt instruments measured at AC and FVOCI. The Fund measures ECL and recognises net impairment losses on financial and contract assets at each reporting date. The measurement of ECL reflects: (i) an unbiased and probability weighted amount that is determined by evaluating a range of possible outcomes, (ii) time value of money and (iii) all reasonable and supportable information that is available without undue cost and effort at the end of each reporting period about past events, current conditions and forecasts of future conditions.

Debt instruments measured at AC and contract assets are presented in the consolidated statement of financial position net of the allowance for ECL. For debt instruments at FVOCI, changes in amortised cost, net of allowance for ECL, are recognised in profit or loss and other changes in carrying value are recognised in OCI as gains less losses on debt instruments at FVOCI.

The Fund applies a three stage model for impairment, based on changes in credit quality since initial recognition. A financial instrument that is not credit-impaired on initial recognition is classified in Stage 1. Financial assets in Stage 1 have their ECL measured at an amount equal to the portion of lifetime ECL that results from default events possible within the next 12 months or until contractual maturity, if shorter ("12 Months ECL"). If the Fund identifies a significant increase in credit risk ("SICR") since initial recognition, the asset is transferred to Stage 2 and its ECL is measured based on ECL on a lifetime basis, that is, up until contractual maturity but considering expected prepayments, if any ("Lifetime ECL"). If the Fund determines that a financial asset is credit-impaired, the asset is transferred to Stage 3 and its ECL is measured as a Lifetime ECL. For financial assets that are purchased or originated credit-impaired ("POCI Assets"), the ECL is always measured as a Lifetime ECL.

Financial assets – write-off. Financial assets are written-off, in whole or in part, when the Fund exhausted all practical recovery efforts and has concluded that there is no reasonable expectation of recovery. The write-off represents a derecognition event. The Fund may write-off financial assets that are still subject to enforcement activity when the Fund seeks to recover amounts that are contractually due, however, there is no reasonable expectation of recovery.

Financial assets - derecognition. The Fund derecognises financial assets when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expire or (b) the Fund has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement whilst (i) also transferring substantially all the risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all the risks and rewards of ownership but not retaining control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale.

Financial assets – modification. The Fund sometimes renegotiates or otherwise modifies the contractual terms of the financial assets. The Fund assesses whether the modification of contractual cash flows is substantial considering, among other, the following factors: any new contractual terms that substantially affect the risk profile of the asset (e.g. profit share or equity-based return), significant change in interest rate, change in the currency denomination, new collateral or credit enhancement that significantly affects the credit risk associated with the asset.

Financial liabilities – measurement categories. Financial liabilities are classified as subsequently measured at AC, except for (i) financial liabilities at FVTPL: this classification is applied to derivatives, financial liabilities held for trading (e.g. short positions in securities), contingent consideration recognised by an acquirer in a business combination and other financial liabilities designated as such at initial recognition and (ii) financial guarantee contracts and loan commitments.

Financial liabilities – derecognition. Financial liabilities are derecognised when they are extinguished (i.e. when the obligation specified in the contract is discharged, cancelled or expires).

An exchange between the Fund and its original lenders of debt instruments with substantially different terms, as well as substantial modifications of the terms and conditions of existing financial liabilities, are accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10% different from the discounted present value of the remaining cash flows of the original financial liability. If an exchange of debt instruments or modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognised as part of the gain or loss on the extinguishment. If the exchange or modification is not accounted for as an extinguishment, any costs or fees incurred adjust the carrying amount of the liability and are amortised over the remaining term of the modified liability.

Modifications of liabilities that do not result in extinguishment are accounted for as a change in estimate using a cumulative catch up method, with any gain or loss recognised in profit or loss, unless the economic substance of the difference in carrying values is attributed to a capital transaction with owners.

Offsetting financial instruments. Financial assets and liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognised amounts, and there is an intention to either settle on a net basis, or to realise the asset and settle the liability simultaneously. Such a right of set off (a) must not be contingent on a future event and (b) must be legally enforceable in all of the following circumstances: (i) in the normal course of business, (ii) in the event of default and (iii) in the event of insolvency or bankruptcy.

Cash and cash equivalents. Cash and cash equivalents include cash in hand, deposits held at call with banks, and other short-term highly liquid investments with original maturities of three months or less. Cash and cash equivalents are carried at AC because: (i) they are held for collection of contractual cash flows and those cash flows represent SPPI, and (ii) they are not designated at FVTPL. Features mandated solely by legislation, such as the bail-in legislation in certain countries, do not have an impact on the SPPI test, unless they are included in contractual terms such that the feature would apply even if the legislation is subsequently changed.

Money market funds. Investments in Money market funds are included in Cash and cash equivalents and measured at fair value. They are short-term, highly liquid investments that are readily convertible to known amounts of cash and so near their maturity they present insignificant risk of changes in value because of changes in interest rates.

Trade and other receivables. Trade and other receivables are recognised initially at fair value and are subsequently carried at AC using the effective interest method.

Trade and other payables. Trade payables are accrued when the counterparty performs its obligations under the contract and are recognised initially at fair value and subsequently carried at AC using the effective interest method.

Financial assets at fair value through profit or loss. Financial assets at fair value through profit or loss include investment in debt and equity securities. Interest from financial assets at fair value through profit or loss includes interest from debt and equity securities. Dividends are included in finance income when the Fund's right to receive the dividend payment is established and it is probable that the dividends will be collected. All other elements of the changes in the fair value and gains or losses on derecognition are recorded in profit or loss for the year as gains less losses from trading investments in the period in which they arise.

Investments in equity securities. Financial assets that meet the definition of equity from the issuer's perspective, i.e. instruments that do not contain a contractual obligation to pay cash and that evidence a residual interest in the issuer's net assets, are considered as investments in equity securities by the Fund. Investments in equity securities are measured at FVTPL, except where the Fund elects at initial recognition to irrevocably designate an equity investments at FVOCI. The Fund's policy is to designate equity investments as FVOCI when those investments are held for strategic purposes other than solely to generate investment returns. When the FVOCI election is used, fair value gains and losses are recognised in OCI and are not subsequently reclassified to profit or loss, including on disposal. Impairment losses and their reversals, if any, are not measured separately from other changes in fair value. Dividends continue to be recognised in profit or loss when the Fund's right to receive payments is established except when they represent a recovery of an investment rather than a return on such investment.

Borrowings. Borrowings are recognised initially at fair value, net of transaction costs incurred and are subsequently carried at amortised cost using the effective interest method.

Income taxes. Income taxes have been provided for in the financial statements in accordance with legislation enacted or substantively enacted by the end of the reporting period. The income tax charge comprises current tax and deferred tax and is recognised in profit or loss for the year, except if it is recognised in other comprehensive income or directly in equity because it relates to transactions that are also recognised, in the same or a different period, in other comprehensive income or directly in equity.

Current tax is the amount expected to be paid to, or recovered from, the taxation authorities in respect of taxable profits or losses for the current and prior periods. Taxable profits or losses are based on estimates if financial statements are authorised prior to filing relevant tax returns. Taxes other than on income are recorded within operating expenses.

Deferred income tax is provided using the balance sheet liability method for tax loss carry forwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit. Deferred tax balances are measured at tax rates enacted or substantively enacted at the end of the reporting period, which are expected to apply to the period when the temporary differences will reverse or the tax loss carry forwards will be utilised.

Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that the temporary difference will reverse in the future and there is sufficient future taxable profit available against which the deductions can be utilised.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis. Deferred tax assets and liabilities are netted only within the individual companies of the Fund.

The Fund controls the reversal of temporary differences relating to taxes chargeable on dividends from subsidiaries or on gains upon their disposal. The Fund does not recognise deferred tax liabilities on such temporary differences except to the extent that Management expects the temporary differences to reverse in the foreseeable future.

Business combinations. Acquisitions of businesses are accounted for using the acquisition method. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition-date fair values of the assets transferred by the Fund, liabilities incurred by the Fund to the former owners of the acquiree and the equity interests issued by the Fund in exchange for control of the acquiree. Acquisition-related costs are generally recognised in profit or loss as incurred.

Gold bullion. The Fund is involved in purchase of gold bullion for investment purposes with the intention of diversification of the investment portfolio with the ability to sell the gold in the future. The gold bullion is initially recognized and subsequently measured at fair value with gains or losses recognised in profit or loss.

Premises and equipment. The Fund's premises and equipment are tangible assets held for administrative purposes with an expected useful life of more than one accounting period. Premises and equipment are initially measured at cost and are stated at cost less accumulated depreciation and provision for impairment, where required.

Premises are subject to revaluation with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period. Increases in the carrying amount arising on revaluation are credited to other comprehensive income and increase the revaluation surplus in equity. Decreases that offset previous increases of the same asset are recognised in other comprehensive income and decrease the previously recognised revaluation surplus in equity; all other decreases are charged to profit or loss for the year. The revaluation reserve for premises included in equity is transferred directly to retained earnings when the revaluation surplus is realised on the retirement or disposal of the asset. If there is no market based evidence of fair value, fair value is estimated using an income approach.

Costs of minor repairs and day-to-day maintenance are expensed when incurred. Costs of replacing major parts or components of premises and equipment items are capitalised, and the replaced part is retired.

At the end of each reporting period management assesses whether there is any indication of impairment of premises and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's fair value less costs to sell and its value in use. The carrying amount is reduced to the recoverable amount and the impairment loss is recognised in profit or loss for the year to the extent it exceeds the previous revaluation surplus in equity. An impairment loss recognised for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's value in use or fair value less costs to sell.

Gains and losses on disposals determined by comparing proceeds with carrying amount are recognised in profit or loss for the year (within other operating income or expenses).

Depreciation. Land is not depreciated. Depreciation on other items of premises and equipment is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives:

	Years
Buildings	50
Vehicles	7
Office equipment	4
Furniture	5
Other property and equipment	3

The residual value of an asset is the estimated amount that the Fund would currently obtain from disposal of the asset less the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

Intangible assets. Intangible assets acquired separately are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortized over their useful economic lives (5 years) and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortization periods and methods for intangible assets with definite useful lives are reviewed at least at each financial year-end.

Derecognition of intangible assets. An intangible asset is derecognised on disposal, or when no future economic benefits are expected from use or disposal. Gains or losses arising from derecognition of an intangible asset, measured as the difference between the net disposal proceeds and the carrying amount of the asset, are recognised in profit or loss when the asset is derecognised.

Provisions. Provisions are recognised when the Fund has a present obligation (legal or constructive) as a result of a past event, it is probable that the Fund will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. When a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows (when the effect of the time value of money is material).

Contingencies. Contingent liabilities are not recognized in the statement of financial position but are disclosed unless the possibility of any outflow in settlement is remote. A contingent asset is not recognized in the statement of financial position but disclosed when an inflow of economic benefits is probable.

Equity reserves. The reserves recorded in equity (other comprehensive income) on the Fund's consolidated statement of financial position include:

- 'Foreign currency translation reserve' which is used to record exchange differences arising from the translation of the net investment in foreign operations;
- 'Retained earnings'

As discussed in Note 18, in accordance with the Decrees and the Regulations, the Fund is an extra-budget state organization. All decisions regarding contributions to and transfers from the Fund are made and approved by the Decrees of the President of the Republic of Azerbaijan.

Contributions/transfers received/made by the Fund represent contributions/withdrawals and, accordingly, are recognized through net equity at the fair value of the consideration received/paid.

Transfers to the State Budget, as well as state institutions, state-owned entities and companies are recognized on the date of payment. All transfers are made within the approved budget of the Fund and transferred to the State Treasury of the Republic of Azerbaijan for payments to eligible budgetary beneficiaries (state institutions, state-owned entities and companies) based on their requests for payments.

Interest income and expense recognition. Interest income and expense are recorded for financial assets at AC on an accrual basis using the effective interest method. This method defers, as part of interest income or expense, all fees paid or received between the parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts. Interest income on debt and equity instruments at FVTPL calculated at nominal interest rate is presented within "Interest income from FVTPL assets" line in profit or loss.

Fees integral to the effective interest rate include origination fees received or paid by the entity relating to the creation or acquisition of a financial asset or issuance of a financial liability, for example fees for evaluating creditworthiness, evaluating and recording guarantees or collateral, negotiating the terms of the instrument and for processing transaction documents.

For financial assets that are originated or purchased credit-impaired, the effective interest rate is the rate that discounts the expected cash flows (including the initial expected credit losses) to the fair value on initial recognition (normally represented by the purchase price). As a result, the effective interest is credit-adjusted.

Interest income is calculated by applying the effective interest rate to the gross carrying amount of financial assets, except for (i) financial assets that have become credit impaired (Stage 3), for which interest revenue is calculated by applying the effective interest rate to their AC, net of the ECL provision, and (ii) financial assets that are purchased or originated credit impaired, for which the original credit-adjusted effective interest rate is applied to the AC.

Dividend income from financial assets at fair value through profit or loss is recognized in the statement of profit or loss when the Fund's right to receive payment is established.

Other operating income including rental income is recognized on accruals basis, i.e. when these are earned.

Expenses are recognized on accrual basis, i.e. when they are incurred.

Accounting for Cash Inflows and Outflows. As described in Note 1, the Fund receives cash inflows from revenues generated from various oil and gas activities carried out in the Republic of Azerbaijan. These cash inflows are made according to certain decrees of the President of the Republic of Azerbaijan. Cash outflows for major projects and contributions to the State budget are also made according to decrees of the President of the Republic of Azerbaijan. SOFAZ believes these inflows and outflows of funds represent contributed capital and withdrawals of capital, respectively. Accordingly, SOFAZ recognises them as movements in equity in the consolidated statement of changes in equity.

Valuation of financial instruments. Financial instruments that are classified at fair value through profit or loss are stated at fair value. The fair value of such financial instruments is the estimated amount at which the instrument could be exchanged between willing parties, other than in a forced or liquidation sale. If a quoted market price is available for an instrument, the fair value is calculated based on the market price. When valuation parameters are not observable in the market or cannot be derived from observable market prices, the fair value is derived through analysis of other observable market data appropriate for each product and pricing models which use a mathematical methodology based on accepted financial theories. Pricing models take into account the contract terms of the securities as well as market-based valuation parameters, such as interest rates, volatility, exchange rates and the credit rating of the counterparty.

Where market-based valuation parameters are absent, management will make a judgment as to its best estimate of that parameter in order to determine a reasonable reflection of how the market would be expected to price the instrument. In exercising this judgment, a variety of tools are used including proxy observable data, historical data, and extrapolation techniques. The best evidence of fair value of a financial instrument at initial recognition is the transaction price unless the instrument is evidenced by comparison with data from observable markets. Any difference between the transaction price and the value based on a valuation technique is not recognized in the statement of profit or loss and other comprehensive income on initial recognition. Subsequent gains or losses are only recognized to the extent that it arises from a change in a factor that market participants would consider in setting a price.

The Fund considers that the accounting estimates related to valuation of financial instruments where quoted markets prices are not available are a key source of estimating uncertainty because: (i) they are highly susceptible to change from period to period because it requires management to make assumptions about interest rates, volatility, exchange rates, the credit rating of the counterparty, valuation adjustments and specific feature of the transactions and (ii) the impact that recognizing a change in the valuations would have on the assets reported in the statement of financial position as well as its profit/(loss) could be material.

Management uses different assumptions regarding the interest rates, volatility, exchange rates, the credit rating of the counterparty and valuation adjustments where quoted market prices are not available using their own knowledge and capabilities, as well as, data obtained from it's custodians (mainly Bank of New York Mellon) and Bloomberg. Please refer to Note 20.

Measurement of fair value of investment properties and property and equipment (building). Fair value of investment properties as well as at the property and equipment (building) is determined by independent professionally qualified appraisers. Fair value is determined using the combination of internal capitalization method (also known as discounted future cash flow method), sales comparison method and also based on the highest and best use method.

Staff costs and related contributions. Wages, salaries, contributions to the Azerbaijan State Social Insurance Fund, paid annual leave and sick leave, bonuses, and non-monetary benefits are accrued in the year in which the associated services are rendered by the employees of the Fund. The Fund has no legal or constructive obligation to make pension or similar benefit payments beyond the payments to the statutory defined contribution scheme.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Fund makes estimates and assumptions that affect the amounts recognised in the consolidated financial statements, and the carrying amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes certain judgements, apart from those involving estimations, in the process of applying the accounting policies. Judgements that have the most significant effect on the amounts recognised in the consolidated financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

Structured entities. Structured entities are designed so that voting or similar rights are not the dominant factor in deciding who controls the entity. Judgement is also required to determine whether the substance of the relationship between the Fund and a structured entity indicates that the structured entity is controlled by the Fund.

The Fund does not consolidate structured entities that it does not control. As it can sometimes be difficult to determine whether the Fund does control a structured entity, management makes judgements about its exposure to the risks and rewards, as well as about its ability to make operational decisions for the structured entity in question. In many instances, elements are present that, considered in isolation, indicate control or lack of control over a structured entity, but when considered together make it difficult to reach a clear conclusion. In cases where more arguments are in place towards existence of control, the structured entity is consolidated.

Were the Fund not to consolidate the assets, liabilities and the results of these consolidated structured entities, the net effect on the statement of financial position would be a decrease in net assets of AZN 427,795 thousand (31 December 2017: decrease in net assets of AZN 407,961 thousand) and decrease in profit by AZN 23,300 thousand (2017: decrease of AZN 63,917 thousand). Refer to Note 25 for further information about the structured entitiy.

5. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS

The following new standards and interpretations became effective for the Fund from 1 January 2018.

Adoption of IFRS 9 "Financial Instruments". The Fund adopted IFRS 9, Financial Instruments, from 1 January 2018. The Fund elected not to restate comparative figures and recognised any adjustments to the carrying amounts of financial assets and liabilities in the opening retained earnings as of the date of initial application of the standards, 1 January 2018. Consequently, the revised requirements of the IFRS 7, Financial Instruments: Disclosures, have only been applied to the current period. The comparative period disclosures repeat those disclosures made in the prior year.

The significant new accounting policies applied in the current period are described in Note 3. Accounting policies applied prior to 1 January 2018 and applicable to the comparative information are disclosed in Note 27.

The following table reconciles the carrying amounts of financial assets, from their previous measurement categories in accordance with IAS 39 into their new measurement categories upon transition to IFRS 9 on 1 January 2018:

In thousands of Azerbaijani Manats	Measurement category		Carrying value per IAS 39 (closing balance at 31 December 2017)	Effect of adopting IFRS 9		Carrying value per IFRS 9 (opening balance at 1 January 2018)
	IAS 39	IFRS 9		Reclassification	Remeasurement	
				Voluntary	Other	
Cash and cash equivalents	L&R	AC	**2,747,381**	-		**2,747,381**
Financial assets at fair value through profit or loss:						
- Agency/ Supranational bonds	FVTPL	FVTPL (mandatory)	8,056,922			8,056,922
-Corporate bonds	FVTPL	FVTPL (mandatory)	22,056,430			22,056,430
-Sovereign bonds	FVTPL	FVTPL (mandatory)	2,008,809			2,008,809
-Money Market	FVTPL	FVTPL (mandatory)	6,280,328			6,280,328
-Corporate bonds	HTM	FVTPL (mandatory)	5,337,216	5,337,216	(294,903)	5,042,313
-Corporate shares	FVTPL	FVTPL (mandatory)	7,090,424			7,090,424
-Private Equity Funds	FVTPL	FVTPL (mandatory)	441,542			441,542
-Real Estate Funds	FVTPL	FVTPL (mandatory)	998,705			998,705
Total financial assets at fair value through profit or loss:			**52,270,376**			**51,975,473**
Other financial assets						
-Trade receivables	L&R	AC	2,397	-		2,397
Total other financial assets			**2,397**			**2,397**
Total financial assets			**55,020,154**			**54,725,251**

(a) Cash and cash equivalents

All classes of cash and cash equivalents as disclosed in Note 7 were reclassified from loans and receivables ("L&R") measurement category under IAS 39 to AC measurement category under IFRS 9 at the adoption date of the standard. The ECLs for cash and cash equivalents balances were insignificant.

(b) Investments in debt securities

The main reasons for reclassifications were as follows:

• *Investments in debt securities previously designated at FVTPL.* The Fund holds some investments in a portfolio of debt securities, which had previously been designated at FVTPL as these securities were managed on a fair value basis. As part of transition to IFRS 9, these securities are now part of an 'other' business model and so are required to be classified as at FVTPL (mandatory), instead of FVTPL (designated) as such on initial recognition.

• *Investments in debt securities previously designated at HTM.* The Fund holds some investments in a portfolio of debt securities, which had previously been designated at HTM as these securities were managed on a held to maturity basis. As part of transition to IFRS 9, management decided to voluntarily classify these assets at FVTPL due to the reason that they are monitored and managed on a fair value basis. The Fund considers these assets being part of the whole debt securities portfolio and decisions on whether to buy, hold or invest further are taken purely on fair value basis.

The following table analyses the impact, net of tax, of transition to IFRS 9 on reserves and retained earnings as of 1 January 2018.

In thousands of Azerbaijani Manats	Attributable to owner				Non-controlling Interest	Total equity
	Contributed Capital	Currency translation reserve	Retained earnings	Total		
Amounts at 31 December 2017 prior to adoption of IFRS 9	27,688,603	1,173,876	31,656,494	60,518,973	8,020	60,526,993
Remeasurement to fair value for reclassified financial instruments under IFRS 9	-	-	(294,903)	(294,903)	-	(294,903)
At 1 January 2018 (under IFRS 9)	27,688,603	1,173,876	31,361,591	60,224,070	8,020	60,232,090

The following amended standards became effective for the Fund from 1 January 2018, but did not have any material impact on the Fund:

• Amendments to IFRS 2 "Share-based Payment" (issued on 20 June 2016 and effective for annual periods beginning on or after 1 January 2018).
• Amendments to IFRS 4 - "Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts" (issued on 12 September 2016 and effective, depending on the approach, for annual periods beginning on or after 1 January 2018 for entities that choose to apply temporary exemption option, or when the entity first applies IFRS 9 for entities that choose to apply the overlay approach).
• Annual Improvements to IFRSs 2014-2016 cycle - Amendments to IFRS 1 an IAS 28 (issued on 8 December 2016 and effective for annual periods beginning on or after 1 January 2018).
• IFRIC 22 "Foreign Currency Transactions and Advance Consideration" (issued on 8 December 2016 and effective for annual periods beginning on or after 1 January 2018).
• Amendments to IAS 40 – "Transfers of Investment Property" (issued on 8 December 2016 and effective for annual periods beginning on or after 1 January 2018).
• IFRS 15, Revenue from Contracts with Customers (issued on 28 May 2014 and effective for the periods beginning on or after 1 January 2018).

6. NEW ACCOUNTING PRONOUNCEMENTS

Certain new standards and interpretations have been issued that are mandatory for the annual periods beginning on or after 1 January 2019 or later, and which the Fund has not early adopted.

IFRS 16, Leases (issued on 13 January 2016 and effective for annual periods beginning on or after 1 January 2019). The new standard sets out the principles for the recognition, measurement, presentation and disclosure of leases. All leases result in the lessee obtaining the right to use an asset at the start of the lease and, if lease payments are made over time, also obtaining financing. Accordingly, IFRS 16 eliminates the classification of leases as either operating leases or finance leases as is required by IAS 17 and, instead, introduces a single lessee accounting model. Lessees will be required to recognise: (a) assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value; and (b) depreciation of lease assets separately from interest on lease liabilities in the statement of profit or loss and other comprehensive income.

IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. The Fund decided that it will apply the standard from its mandatory adoption date of 1 January 2019 using the modified retrospective method, without restatement of comparatives. Right-of-use assets for property leases are measured on transition as if the new rules had always applied. All other right-of-use assets are measured at the amount of the lease liability on adoption (adjusted for any prepaid or accrued expenses).

As IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17, the Fund does not expect any significant impact on the consolidated financial statements in respect of recognition of the Fund's activities as a lessor.

IFRS 17 "Insurance Contracts" (issued on 18 May 2017 and effective for annual periods beginning on or after 1 January 2021). IFRS 17 replaces IFRS 4, which has given companies dispensation to carry on accounting for insurance contracts using existing practices. As a consequence, it was difficult for investors to compare and contrast the financial performance of otherwise similar insurance companies. IFRS 17 is a single principle-based standard to account for all types of insurance contracts, including reinsurance contracts that an insurer holds. The standard requires recognition and measurement of groups of insurance contracts at: (i) a risk-adjusted present value of the future cash flows (the fulfilment cash flows) that incorporates all of the available information about the fulfilment cash flows in a way that is consistent with observable market information; plus (if this value is a liability) or minus (if this value is an asset) (ii) an amount representing the unearned profit in the group of contracts (the contractual service margin). Insurers will be recognising the profit from a group of insurance contracts over the period they provide insurance coverage, and as they are released from risk. If a group of contracts is or becomes loss-making, an entity will be recognising the loss immediately. The Fund is currently assessing the impact of the new standard on its consolidated financial statements.

The following other new pronouncements are not expected to have any material impact on the Fund when adopted:

• Prepayment Features with Negative Compensation – Amendments to IFRS 9 (issued on 12 October 2017 and effective for annual periods beginning on or after 1 January 2019).
• IFRIC 23 "Uncertainty over Income Tax Treatments" (issued on 7 June 2017 and effective for annual periods beginning on or after 1 January 2019).
• Sale or Contribution of Assets between an Investor and its Associate or Joint Venture – Amendments to IFRS 10 and IAS 28 (issued on 11 September 2014 and effective for annual periods beginning on or after a date to be determined by the IASB).
• *Long-term Interests in Associates and Joint Ventures* – Amendments to IAS 28 (issued on 12 October 2017 and effective for annual periods beginning on or after 1 January 2019).
• Annual Improvements to IFRSs 2015-2017 cycle - Amendments to IFRS 3, IFRS 11, IAS 12 and IAS 23 (issued on 12 December 2017 and effective for annual periods beginning on or after 1 January 2019).
• Amendments to IAS 19 "Plan Amendment, Curtailment or Settlement" (issued on 7 February 2018 and effective for annual periods beginning on or after 1 January 2019).
• Amendments to the Conceptual Framework for Financial Reporting (issued on 29 March 2018 and effective for annual periods beginning on or after 1 January 2020).
• Definition of a business – Amendments to IFRS 3 (issued on 22 October 2018 and effective for acquisitions from the beginning of annual reporting period that starts on or after 1 January 2020).
• Definition of materiality – Amendments to IAS 1 and IAS 8 (issued on 31 October 2018 and effective for annual periods beginning on or after 1 January 2020).

Unless otherwise described above, the new standards and interpretations are not expected to affect significantly the Fund's consolidated financial statements.

7. CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise:

In thousands of Azerbaijani Manats	2018	2017
Short-term deposits	4,437	2,134,556
Money market funds	553,139	198,518
Bank accounts	707,012	414,307
Total cash and cash equivalents	**1,264,588**	**2,747,381**

Money market funds

Investments in money market funds represent share ownership in funds, payable on demand. Investments in money market funds are highly liquid. Money market funds invest their assets in short-term debt and debt related instruments, such as commercial paper, certificates of deposit, bonds bearing floating interests, US treasury bonds, Eurobonds and asset-backed securities. Interest and dividends payable to the Fund are reinvested. The fair value of money market fund approximates their carrying amount.

The Fund had the following investments in the money market funds with AAA credit ratings:

In thousands of Azerbaijani Manats	2018	2017
BlackRock ICS-Institution Liquidity Funds plc	502,712	173,933
The Goldman Sachs Group, Inc	50,427	24,585
Total money market funds	**553,139**	**198,518**

BANK ACCOUNTS

Bank accounts were denominated in the following currencies:

In thousands of Azerbaijani Manats	2018	2017
AZN	895	11,332
USD	465,938	278,035
GBP	77,284	7,171
CNY	1,515	1,687
CHF	3,625	1,617
AUD	5,899	1,626
EUR	106,213	69,875
RUB	2,543	3,352
KRW	2,596	1,437
CAD	697	967
HKD	143	226
NOK	199	273
DKK	114	159
NZD	64	76
JPY	37,516	35,754
SGD	181	303
SEK	126	326
ILS	151	57
TRY	1,313	34
Total bank accounts	**707,012**	**414,307**

As at 31 December 2018, the Fund had AZN 112 thousand and AZN 820 thousand (2017: AZN 51 thousand and AZN 11,288 thousand) held at bank accounts in the International Bank of Azerbaijan and the Central Bank of the Republic of Azerbaijan, respectively.

Other accounts originated in foreign currencies were opened with non-resident banks with long-term ratings B/B2 (Standard & Poor's/ Fitch/Moody's) and above.

DEPOSITS

The Fund's investments in deposits comprise:

In thousands of Azerbaijani Manats	2018	2017
Wells Fargo	4,437	-
T.C. Ziraat Bankasi A.S.	-	472,222
Akbank T.A.S, Istanbul	-	292,613
Turkiye Is Bankasi A.S. Istanbul	-	687,892
Turkiye Garanti Bankasi AS	-	681,829
Total deposits	**4,437**	**2,134,556**

As at 31 December 2018, the Fund placed AZN 4,437 thousand (31 December 2017: AZN 2,134,556 thousand) in deposits with non-resident banks maturing in January 2019 with credit rating of A/A2 (Standard & Poor's/ Fitch/ Moody's).

The credit quality of cash and cash equivalents balances may be summarised (based on Standard and Poor's/Fitch/ Moody's ratings) as follows at 31 December 2018:

In thousands of Azerbaijani Manats	Bank Account	Short term Deposit	Money Market Funds	Total
Neither past due nor impaired				
AAA	-	-	553,139	553,139
AA	5,560	-	-	5,560
A	147,496	4,437	-	151,933
BBB*	550,050	-	-	550,050
BB*	1,661	-	-	1,661
B	1,425	-	-	1,425
Total cash and cash equivalents**	**706,192**	**4,437**	**553,139**	**1,263,768**

For the purpose of ECL measurement cash and cash equivalents balances are included in Stage 1. The ECL for these balances represents an insignificant amount, therefore the Fund did not recognise any credit loss allowance for cash and cash equivalents.

The credit quality of cash and cash equivalents balances may be summarised (based on Standard and Poor's/Fitch/ Moody's ratings) as follows at 31 December 2017:

In thousands of Azerbaijani Manats	Bank Account	Short term Deposit	Money Market Funds	Total
Neither past due nor impaired				
AAA	-	-	198,518	198,518
A	62,606	-	-	62,606
BBB	335,669	-	-	335,669
BB	4,693	2,134,556	-	2,139,249
CCC	51	-	-	51
Total cash and cash equivalents	**403,019**	**2,134,556**	**198,518**	**2,736,093**

*- AZN 4,198 thousand (2017 AZN 4,654 thousand) of this amount denotes the cash balances held by the Fund's subsidiaries, where the Fund is not directly involved in cash allocations.

**- AZN 820 (2017 AZN 11,288) thousand cash balance held by the Fund in the Central Bank of the Republic of Azerbaijan is excluded from the table as Central Banks do not have credit ratings.

Interest rate analysis of cash and cash equivalents is disclosed in Note 22. Information on related party balances is disclosed in Note 24.

8. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

Financial assets at fair value through profit or loss comprise of followings:

In thousands of Azerbaijani Manats	2018	2017
Agency/Supranational bonds	13,082,224	8,056,922
Corporate bonds	28,786,959	22,056,430
Sovereign bonds	2,915,648	2,008,809
Money Market	4,070,231	6,280,328
Private Equity Funds	641,363	441,542
Real Estate Funds	1,612,098	998,705
Equity securities	6,229,752	7,090,424
Total financial assets at fair value through profit or loss	**57,338,275**	**46,933,160**

As at 31 December 2018 the Fund held AZN 6,301,821 thousand, (2017: AZN 6,918,143 thousand) under asset management agreements with financial institutions ("external managers") including cash and cash equivalents. The management fees in 2018 to the external managers were AZN 2,887 thousand (2017: AZN 2,450 thousand).

Agency/Supranational bonds. These bonds are represented by investments in debt securities issued by international organizations of Europe, Asia and America. These securities bear fixed interest ranging from 0.125% p.a. to 5.75% p.a. and USD LIBOR, GBP LIBOR, CNY 5-day average SHIBOR with the spread ranging from -0.05% p.a. to +0.9% p.a. (2017: 0.125% p.a. to 5.75% p.a. and USD LIBOR, EURIBOR, GBP LIBOR, CNY 5-day average SHIBOR with the spread ranging from +0.01% p.a. to +0.875% p.a.) and mature during the period from January 2019 to November 2023 (2017: January 2018 to December 2022). As at 31 December 2018 total accrued interest on these securities amounted AZN 52,411 thousand (2017: AZN 27,470 thousand). These securities were held in the portfolio managed both directly by the Fund as well as the Fund's external managers, DWS International GmbH and IBRD – World Bank Group.

Corporate bonds. Corporate bonds are represented by investments in debt securities issued by corporations of Europe, Asia, Australia and America. As at 31 December 2018 these securities bear fixed interest ranging from 0.0% p.a. to 7.5% p.a. and USD LIBOR, GBP LIBOR, EURIBOR and Australian Bank Bill Short Term Rate with the spread ranging from +0.16% p.a. to +4% p.a.(2017: from 0.0% p.a. to 7.5% p.a. and USD LIBOR, GBP Libor, EURIBOR and Australian Bank Bill Short Term Rate with the spread ranging from +0.17% p.a. to +1.75% p.a.) and mature during the period from January 2019 to January 2031 (2017: January 2018 to January 2031). As at 31 December 2018 total accrued interest on these securities amounted AZN 555,575 thousand (2017: AZN 131,962 thousand). These securities were held in the portfolio managed both directly by the Fund and the Fund's external managers DWS International GmbH and IBRD – World Bank Group.

Sovereign bonds. Sovereign bonds are represented by investments in debt securities issued by various European, Asian, Australian and American institutions. As at 31 December 2018 these securities bear fixed interest ranging from 0.05% p.a. to 11.75% p.a and EURIBOR with the spread +1.20% p.a (2017: from 0.75% p.a. to 11.625% p.a and EURIBOR with the spread +1.20% p.a.) and mature during the period from January 2019 to September 2029 (2017: January 2018 to September 2029). As at 31 December 2018 total accrued interest on these securities amounted AZN 31,060 thousand (2017: AZN 19,452 thousand). These securities were held in the portfolio managed both directly by the Fund as well as the Fund's external managers, DWS International GmbH and IBRD – World Bank Group.

Private Equity Funds

The IFC Funds are comprised of three independent investment funds: IFC Global Infrastructure Fund (IFC GIF), IFC Catalyst Fund (IFC CF) and IFC African, Latin American and Caribbean Fund (IFC ALAC).

IFC GIF is formed with the purpose of identifying, acquiring, holding and disposing of a portfolio of equity or equity related infrastructure investments in emerging markets. The Fund's commitment to IFC GIF is AZN 340,000 thousand. As of 31 December 2018 the fair value of Fund's investment in IFC GIF was AZN 174,850 thousand (2017: AZN 152,690 thousand).

IFC CF was formed with the purpose of investing in a portfolio of limited partnerships or equivalent interests of investment funds or other pooled investment vehicles ("Investee Funds"), and direct co-investments primarily focused on resource efficiency and developing low-emission products and services in emerging markets. The Fund's commitment to IFC CF is AZN 85,000 thousand. As of 31 December 2018 the fair value of Fund's investment in IFC CF was AZN 53,845 thousand (2017: AZN 35,486 thousand).

IFC ALAC is formed with the purpose of identifying, acquiring, holding and disposing a portfolio of equity or equity related investments in the African, Latin American and Caribbean regions. The Fund's commitment to IFC ALAC is AZN 170,000 thousand. As of 31 December 2018 the fair value of Fund's investment in IFC ALAC was AZN 60,035 thousand (2017: AZN 67,953 thousand).

All declared dividends are reinvested in above mentioned funds by SOFAZ.

NB Caspian Partners is a separately managed Private Equity mandate formed with the purpose of investing predominantly in buy-out funds in the developed markets. The Fund's commitment to NB Caspian Partners is AZN 330,480 thousand. As of 31 December 2018 the fair value of Fund's investment in NB Caspian Partners was AZN 183,129 thousand (2017: AZN 112,950 thousand).

EBRD EPF has been formed with the purpose of providing investors with the exposure to EBRD'S equity investments in Central and Eastern Europe, Mediterranean, Central Asia etc. through Equity Return Swaps. The Fund's commitment to EBRD EPF is AZN 193,290 thousand. As of 31 December 2018 the fair value of Fund's investment in EBRD EPF was AZN 62,956 thousand (2017: AZN 22,633 thousand).

BC European Capital X is a buyout fund focused on acquiring large businesses exhibiting defensive growth characteristics mainly in Europe. The Fund's commitment to BCEC X is AZN 108,822 thousand. As of 31 December 2018 the fair value of Fund's investment in BCEC X was AZN 53,169 thousand (2017: AZN 25,745 thousand).

FSI is an independent management company based in Milan. FSI manages the FSI Mid-Market Growth Equity Fund, a private equity closed-end fund. The Fund offers to investors the possibility to combine strong investment returns and a unique access to Italian mid-market companies presenting significant growth opportunities in industrial and service sectors. The Fund's commitment to FSI is AZN 38,658 thousand. As of 31 December 2018 the fair value of Fund's investment in FSI Fund was AZN 9,002 thousand (2017: AZN 147 thousand).

Blackstone Core Equity Partners L.P. specializes in acquisitions and buyout investments mainly in North America. The Fund's commitment to Blackstone Core Equity Partners L.P. is AZN 85,000 thousand. As of 31 December 2018 the fair value of Fund's investment in Blackstone Core Equity Partners was AZN 41,436 thousand (2017: AZN 23,938 thousand).

Apollo Fund IX specializes in acquisitions and buyout investments predominantly in North America. The Fund's commitment to Apollo Fund IX is AZN 144,500 thousand. As of 31 December 2018 the fund has not drawn capital from the Fund yet.

Carlyle Partners VII is a buyout fund of Carlyle Group focused in large-to-mega cap deals in North America. The Fund's commitment to Carlyle Partners VII is AZN 85,000 thousand. As of 31 December 2018 the fair value of Fund's investment in Carlyle Partners was AZN 2,941 thousand (2017: nil).

Carlyle Europe Partners V is a buyout fund of Carlyle Group focused in Europe. The Fund's commitment to Carlyle Europe Partners V is AZN 96,645 thousand. As of 31 December 2018 the fund has not drawn capital from the Fund yet.

Vista Equity Partners VII is a tech buyout fund of Vista Equity Partners founded by Robert Smith mainly focusing in North America region. The Fund's commitment to Vista Equity Partners VII is AZN 68,000 thousand. As of 31 December 2018 the fund has not drawn capital from the Fund yet.

Warburg Pincus Global Growth is a diversified growth fund of Warburg Pincus focusing mainly in North America, Asia and Europe region. The Fund's commitment to Warburg Pincus Global Growth is AZN 85,000 thousand. As of 31 December 2018 the fund has not drawn capital from the Fund yet.

PAG Asia Capital Fund III is a buyout fund of PAG with regional focus in Asia. The Fund's commitment to PAG Asia Capital Fund III is AZN 51,000 thousand. As of 31 December 2018 the fund has not drawn capital from the Fund yet.

Thoma Bravo Fund XIII is a tech buyout fund of Thoma Bravo with regional focus in North America. The Fund's commitment to Thoma Bravo Fund XIII is AZN 42,500 thousand. As of 31 December 2018 the fund has not drawn capital from the Fund yet.

The Fund's commitment to Baring Private Equity Asia VII is AZN 85,000 thousand. As of 31 December 2018 the fund has not drawn capital from the Fund yet.

REAL ESTATE FUNDS

Real estate's indirect portfolio is comprised of real estate funds and co-investments.

The PEVAV fund was established to implement value-added real estate strategies within targeted European countries including the UK, Germany, France, Spain, Italy, Netherlands, Poland and the Nordic/Scandinavian region. The Fund's commitment to PEVAV fund is AZN 194,680 thousand. As of 31 December 2018 the fair value of Fund's investment in PEVAV was AZN 114,577 thousand (2017: AZN 129,394 thousand).

EVP is a real estate fund formed to acquire real estate assets in the Eurozone, targeting mainly France, Germany, Italy and Spain, with a value-add investment profile. The Fund's commitment to EVP fund is AZN 194,680 thousand. As of 31 December 2018 the fair value of Fund's investment in EVP was AZN 149,296 thousand (2017: AZN 65,565 thousand).

BREP EUROPE V is an opportunistic real estate fund and makes investments mostly in United Kingdom, Germany, Spain and Italy. The Fund's commitment to BREP EUROPE V fund is AZN 194,680 thousand. As of 31 December 2018 the fair value of Fund's investment in BREP EUROPE V was AZN 121,223 thousand (2017: AZN 57,946 thousand).

PREP is a value driven investment strategy fund with primary focus on Japan, China and Australia. The Fund's commitment to PREP fund is AZN 170,000 thousand. As of 31 December 2018 the fair value of Fund's investment in PREP was AZN 155,509 thousand (2017: AZN 162,271 thousand).

ASPF III is primarily focused on investing in the key markets of Australia, China, Japan, Malaysia and Singapore with value added strategy. The Fund's commitment to ASPF III fund is AZN 194,680 thousand. As of 31 December 2018 the fair value of Fund's investment in ASPF III was AZN 111,452 thousand (2017: AZN 154,357 thousand).

RJLF II is an opportunistic fund with a focus on logistics real estate investments in Japan. The Fund's commitment to RJLF II fund is AZN 170,000 thousand. As of 31 December 2018 the fair value of Fund's investment in RJLF II was AZN 103,623 thousand (2017: AZN 82,941 thousand).

EF IV Feeder is a private real estate fund with value-add strategy focused on European region. The Fund's commitment to Europe Property Fund IV Feeder is AZN 194,680 thousand. As of 31 December 2018 the fair value of Fund's investment in Europe Property Fund was AZN 132,522 thousand (2017: AZN 67,068 thousand).

GREF V is a private real estate fund with value-add strategy focused on APAC region. The Fund's commitment to Gateway Real Estate Fund V is AZN 57,970 thousand As of 31 December 2018 the fair value of Fund's investment in Gateway Real Estate Fund V was AZN 47,371 thousand (2017: AZN 13,450 thousand).

GAW US Fund III is a value-add investment fund established to invest in North American assets. The Fund's commitment to GAW US Fund III is AZN 107,950 thousand As of 31 December 2018 the fair value of Fund's investment in GAW US Fund III was AZN 8,174 thousand (2017: nil).

WSREF VIII was raised by Walton Street Capital. WSREF VIII is a private real estate fund with core-plus/value-add strategy focused on US. The Fund's commitment to Walton Street R.E Fund VIII is AZN 170,000 thousand. As of 31 December 2018 the fair value of Fund's investment in Walton Street R.E Fund VIII was AZN 110,612 thousand (2017: AZN 60,917 thousand).

CREDO invests in commercial mortgage-backed securities and other real estate debt originally rated investment grade. CREDO uses its expertise in the ownership and management of commercial real estate to invest in the real estate debt markets. The Fund's commitment to AG Commercial R.E Debt Fund is AZN 85,000 thousand. As of 31 December 2018 the fair value of Fund's investment in AG Commercial R.E Debt Fund was AZN 68,816 thousand, (2017: AZN 45,532 thousand).

The Fund's commitment to AG Realty Value Fund is AZN 170,000 thousand. As of 31 December 2018 AG Realty Value Fund has not drawn capital from the Fund yet.

The Fund has commitment agreement with Ares Real Estate Fund IX – private real estate fund with value-add strategy focused on US region. The Fund's commitment to Ares Real Estate Fund IX is AZN 170,000 thousand. As of 31 December 2018 the fair value of Fund's investment in Ares Real Estate Fund IX was AZN 33,823 thousand (2017: nil).

The Fund has commitment agreement with Gateway Real Estate Fund V for a value-add mixed-use investment in Singapore. The Fund's commitment to Gateway Real Estate Fund V fund is AZN 34,000 thousand. As of 31 December 2018 the fair value of Fund's investment in this value-add mixed-use investment was AZN 32,673 thousand (2017: nil).

SOF XI fund was established to implement opportunistic real estate strategies targeted North America and Europe. The Fund's commitment to SOF XI fund is AZN 340,000 thousand. As of 31 December 2018 the fair value of Fund's investment in SOF XI was AZN 14,408 thousand (2017: nil).

PREP II is a real estate fund formed to invest in Core-plus.value-add real estate assets in Asian Pacific region targeting mainly Japan and South Korea. The Fund's commitment to PREP II fund is AZN 85,000 thousand. As of 31 December 2018 value of Fund's investment in PREP II was 15,891 AZN thousand (2017: nil).

GreenOak US III is a value-add investment fund formed to invest in North America. The Fund's commitment to GreenOak fund is AZN 170,000 thousand. As of 31 December 2018 the fair value of Fund's investment in GreenOak US Feeder III, L.P. was AZN 19,401 thousand (2017: AZN nil).

The Fund has made a co-investment into a value-add mixed-use property with PGIM's EVP fund located in Frankfurt, Germany. The Fund's commitment with regard to this investment is AZN 71,912 thousand. As of 31 December 2018 the fair value of the Fund's share in this co-investment was AZN 96,540 thousand (2017: AZN 60,761 thousand).

The Fund has made a co-investment into a core-plus office property with Gaw Capital's GREF V fund in Yokohama, Japan. The Fund's commitment with regard to this investment is AZN 34,000 thousand. As of 31 December 2018 the fair value of Fund's share in this co-investment was AZN 66,083 (2017: AZN 30,727).

The Fund has made a co-investment into an opportunistic hotel development with PGIM's ASPF III fund in Kyoto, Japan. The Fund's commitment with regard to this investment is AZN 32,791 thousand. As of 31 December 2018 the fair value of Fund's share in this co-investment was AZN 45,762 thousand (2017:AZN 18,984 thousand).

The Fund has made a co-investment in office property with Blackrock's EFIV fund in Munich, Germany. The Fund's commitment with regard to this investment is AZN 12,330 thousand. As of 31 December 2018 the fair value of Fund's share in this co-investment was AZN 19,906 thousand (2017: AZN 12,110 thousand).

The Fund has made mixed-use co-investment with Walton Street's WSREF VIII fund in Chicago, USA. The Fund's commitment with regard to this investment is AZN 42,500 thousand. As of 31 December 2018 the fair value of Fund's share in this co-investment was AZN 37,197 thousand (2017: AZN 35,204 thousand).

The Fund has made a logistics portfolio co-investment with Gaw Capital's GREF V in China. The Fund's commitment with regard to this investment is AZN 102,000 thousand. As of 31 December 2018 the fair value of Fund's share in this co-investment was AZN 18,696 thousand (2017: AZN 1,478 thousand).

The Fund has made a core-plus retail portfolio co-investment with GAW Capital's GREF V in Hong Kong. The Fund's commitment with regard to this investment is AZN 85,000 thousand. As of 31 December 2018 the fair value of Fund's share in this co-investment was AZN 88,543 thousand (2017: nil).

Equity securities. The carrying value of equity investments consists of investments in the following sectors at 31 December 2018 and 2017:

In thousands of Azerbaijani Manats	2018	2017
Finance	1,540,246	1,988,584
Consumer	1,269,618	1,397,982
Telecommunication and information technologies	1,180,019	1,230,558
Industrial	553,239	671,072
Healthcare	805,766	797,918
Energy	333,706	376,354
Materials	324,617	416,195
Utilities	222,541	211,761
Total equity securities	**6,229,752**	**7,090,424**

These securities were held in the portfolio managed both directly by the Fund as well as the Fund's external managers, SSGA, UBS Asset Management (UK) LTD, Blackrock Investment Management, Mellon Capital Management Corporation and Sumitomo Mitsui Trust International LTD.

FVTPL assets are carried at fair value which also reflects any credit risk related write-downs. Therefore, the Fund does not analyse or monitor impairment indicators.

Analysis by credit quality of debt trading securities is as follows at 31 December 2018:

In thousands of Azerbaijani Manats	Agency/ Supranational Bonds	Corporate Bonds	Sovereign Bonds	Money Market	Total
Neither past due nor impaired (at fair value)					
AAA	8,716,172	637,696	771,830	853,296	10,978,994
AA	2,817,198	2,829,308	174,590	674,836	6,495,932
A	1,435,871	11,404,024	905,617	2,445,253	16,190,765
BBB	112,983	7,029,145	465,111	96,846	7,704,085
BB	-	5,450,817	598,500	-	6,049,317
B	-	1,432,592	-	-	1,432,592
D	-	3,377	-	-	3,377
Total neither past due nor impaired	**13,082,224**	**28,786,959**	**2,915,648**	**4,070,231**	**48,855,062**
Total debt trading securities	**13,082,224**	**28,786,959**	**2,915,648**	**4,070,231**	**48,855,062**

Analysis by credit quality of debt trading securities is as follows at 31 December 2017:

In thousands of Azerbaijani Manats	Agency/ Supranational Bonds	Corporate Bonds	Sovereign Bonds	Money Market	Total
Neither past due nor impaired (at fair value)					
AAA	4,935,999	353,303	611,850	542,369	6,443,521
AA	1,398,383	2,205,080	64,420	1,044,726	4,712,609
A	1,524,027	12,138,717	445,794	3,582,828	17,691,366
BBB	198,513	5,980,012	807,987	1,110,405	8,096,917
BB/CCC	-	1,372,418	78,758	-	1,451,176
Securities without rating	-	6,900	-	-	6,900
Total neither past due nor impaired	**8,056,922**	**22,056,430**	**2,008,809**	**6,280,328**	**38,402,489**
Total debt trading securities	**8,056,922**	**22,056,430**	**2,008,809**	**6,280,328**	**38,402,489**

The credit ratings are based on Standard & Poor's ratings where available, or Moody's or Fitch rating converted to the nearest equivalent on the Standard & Poor's rating scale. The debt securities are not collateralised.

9. GOLD BULLION

In accordance with the "Rules on Holding, Placement and Management of Foreign Assets of The State Oil Fund of the Republic of Azerbaijan" approved by Decree #511 of the President of the Republic of Azerbaijan dated 19 June 2001 as amended by Decrees #607 dated 21 December 2001, #202 dated 1 March 2005, #216 dated 10 February 2010 and #519 dated 27 October 2011, gold bars conforming to the requirements of the London Bullion Market Association may be included in the Investment Portfolio of the Fund.

Movements of gold bullion:

In thousands of Azerbaijani Manats	2018	2017
Opening balance at 1 January	**2,137,212**	**1,968,469**
Additions	1,388,537	-
Net fair value gain on gold bullions	32,497	168,743
Closing balance at 31 December	**3,558,246**	**2,137,212**

10. INVESTMENT PROPERTIES

Movement of investment properties:

In thousands of Azerbaijani Manats	2018	2017
Investment properties at fair value at 1 January	**2,763,757**	**2,619,625**
Additions	6,863	4,412
Fair value gains/(losses)	(108,674)	15,466
Effect of translation to presentation currency	(77,262)	124,254
Investment properties at fair value at 31 December	**2,584,684**	**2,763,757**

Investment properties consist of "Gallery Actor", mixed-use office and retail complex located in Moscow central business district at 16 Tverskaya Street, "78 St James's Street" an office complex in London, "8 Place Vendome" office, retail and residential building located in Paris, "Pine Avenue Tower A" office complex located in Seoul, "Kirarito Ginza" retail complex located in Tokyo and "Palazzo Turati" office complex in Milan. All properties are leased out on a commercial basis.

As at 31 December 2018 investment properties are stated at fair value, which has been determined based on valuations performed by professional valuation companies, the accredited independent appraisers. The appraisers are recognized industry specialists in valuing these types of investment properties. The fair value represents the amount at which the assets could be exchanged between a knowledgeable, willing buyer and a knowledgeable, willing seller in an arm's length transaction at the date of valuation. The fair values of the properties have been primarily derived using prices for comparable properties, market information, discounted cash flow method (income approach) and the expert opinion of independent accredited valuators who have advised on current market levels.

At 31 December 2018, investment property carried at AZN 1,681,450 thousand have been pledged to third parties as collateral with respect to borrowings. Refer to Note 13.

Where the Fund is the lessor, the future minimum lease payments receivable under non-cancellable operating leases are as follows:

In thousands of Azerbaijani Manats	2018	2017
Not later than 1 year	78,349	51,310
Later than 1 year and not later than 5 years	220,947	243,655
Later than 5 years	43,363	64,898
Total operating lease payments receivable at 31 December	**342,659**	**359,863**

Detailed disclosure on fair value change of investment properties:

Investment property	Fair value 2018	Change in fair value	Effect of translation to presentation currency	Additions	Fair value 2017
"78 St James Street", London	258,348	(162,885)	(17,635)	4,129	434,739
"Gallery Actor", Moscow	80,092	(4,026)	(16,641)	577	100,182
"SCI 8 Place Vendome", Paris	362,328	9,912	(15,481)	1,356	366,541
"Pine Avenue Tower A", Seoul	784,076	24,913	(35,339)	-	794,502
"Kirarito Ginza" , Tokyo	897,373	14,582	16,455	801	865,535
"Palazzo Turati", Milan	202,467	8,830	(8,621)	-	202,258
	2,584,684	**(108,674)**	**(77,262)**	**6,863**	**2,763,757**

Investment property	Fair value 2017	Change in fair value	Effect of translation to presentation currency	Additions	Fair value 2016
"78 St James Street", London	434,739	(699)	21,598	-	413,840
"Gallery Actor", Moscow	100,182	(49,409)	1,018	2,864	145,709
"SCI 8 Place Vendome", Paris	366,541	9,236	29,568	1,468	326,269
"Pine Avenue Tower A", Seoul	794,502	4,569	61,256	35	728,642
"Kirarito Ginza" , Tokyo	865,535	50,601	(5,700)	45	820,589
"Palazzo Turati", Milan	202,258	1,168	16,514	-	184,576
	2,763,757	**15,466**	**124,254**	**4,412**	**2,619,625**

Establishment of 78 St James's Street Unit Trust (the "Unit Trust")

The Unit Trust was established by the Fund on 22 November 2012 under the provision of the Trust Instrument. SOFAZ RE Limited in its capacity as general partner of the SOFAZ RE UK L.P. has a 99% holding of the Unit Trust. SOFAZ RE Min Limited has a 1% holding of the Unit Trust. SOFAZ RE Limited, SOFAZ RE UK L.P. and SOFAZ RE Min Limited are ultimately owned by the State Oil Fund of Azerbaijan. The Unit Trust invests in real estate located in the United Kingdom and owns the office complex "78 St James's Street". The Unit Trust is established, resident and domiciled in Jersey, Channel Islands. During 2018, the Unit Trust has contributed AZN 93,978 thousand (2017: AZN 21,419 thousand) of rental income and AZN 72,681 thousand loss (2017: AZN 17,316 thousand profit) to the net profit/(loss) before tax of the Fund (Net profit figure includes fair value decrease of AZN 162,885 thousand (2017: AZN 699 thousand decrease)).

Acquisition of JSC Tverskaya 16

On 21 December 2012, SOFAZ acquired 100% of voting shares of JSC Tverskaya 16. Its main activity is management of business and retail centre called "Gallery Actor" located in the Central Administrative District of Moscow, Russia. During 2018, JSC Tverskaya 16 contributed AZN 8,764 thousand (2017: AZN 7,800 thousand) of rental income and AZN 815 thousand profit (2017: AZN 70,582 thousand loss) to the net profit/(loss) before tax of the Fund (Net loss figure includes fair value decrease of AZN 4,027 thousand (2017: decrease AZN 49,409 thousand)).

Establishment of SCI 8 Place Vendome

On 19 March 2013, the Fund acquired via a special purpose vehicle, a mixed use office, retail and residential complex SCI 8 Place Vendome located on Place Vendome 8, Paris, France from AXA Real Estate for EUR 135,000 thousand. SCI 8 Place Vendome is an indirect subsidiary of the Fund incorporated in France as a civil partnership having its registered office in Paris, 6 place de Madeleine. SCI 8 Place Vendome is held by the Fund via two Luxembourg holding companies (the Luxcos): SOFAZ RE Fund S.a.r.l. - a private limited company with a share capital of EUR 12,500 having its registered office in Luxembourg which is 100% held by SOFAZ RE Europe Holding S.a.r.l. and holds 0.1% of SCI 8 Place Vendome and SOFAZ RE Europe S.a.r.l. - a private limited company with a share capital of EUR 12,500 having its registered office in Luxembourg which is 100% held by SOFAZ RE Europe Holding S.a.r.l. and holding 99.9% of SCI 8 Place Vendome. During 2018, SCI 8 Place Vendome has contributed AZN 10,701 thousand (2017: AZN 11,254 thousand) of rental income and AZN 14,645 thousand profit (2017: 13,932 thousand profit) to the net profit/(loss) before tax of the Fund (Net profit figure includes fair value increase of AZN 9,912 thousand (2017: AZN 9,236 thousand increase)).

Acquisition of "Pine Avenue Tower A" office complex

On 31 March 2014 SOFAZ finalised the acquisition of prime office complex, Pine Avenue Tower A in Seoul, South Korea via acquisition of 100% interest in Beneficiary Certificates ("BCs") in Real Estate Fund from Mirae Asset Management for KRW 469,007 million (AZN 346,250 thousand). During the year ended 2018, "Pine Avenue Tower A" has contributed AZN 20,886 thousand (2017: AZN 18,239 thousand) of rental income and AZN 38,775 thousand profit (2017: AZN 24,716 thousand profit) to the net profit/(loss) before tax of the Fund (Net profit figure includes fair value increase of AZN 24,913 thousand (2017: AZN 4,569 thousand increase)).

Establishment of Kirarito Ginza

SOFAZ made an investment in the amount of 51,989 million JPY (AZN 455,736 thousand) to an operator entity ("OE") under a Tokumei Kumiai ("TK") agreement on 21 August 2015. This investment formed 98% of the capital of the OE. 2% is held by the Asset Managers ("AM"), PGIM Real Estate (Japan). SOFAZ is free to sell this investment (right to cashflows) in the OE at any time. The OE invested proceeds from investors in an investment property, a retail complex in Ginza, Tokyo, for 52,434 million JPY (AZN 459,633 thousand), including investment-related acquisition costs. For detailed information, refer to the Note 25.

During the year ended 2018, "Kirarito Ginza" has contributed AZN 23,081 thousand (2017: AZN 23,872 thousand) of rental income and AZN 24,498 thousand profit (2017: AZN 63,917 thousand profit) to the net profit/(loss) before tax of the Fund (Net profit figure includes fair value increase of AZN 14,582 thousand increase (2017: AZN 50,601 thousand increase)).

Establishment of Palazzo Turati

In May 2016, the Fund has reached an agreement to acquire Palazzo Turati, an office property in Milan for EUR 97 million. For this investment the Fund established the 100% controlled Real Estate Investment Fund (REIF) that acquired the property. The Fund invested into the REIF through its Luxembourg subsidiary - SOFAZ RE Europe S.a.r.l. During 2018, Palazzo Turati contributed AZN 9,827 thousand (2017: AZN 9,479 thousand) of rental income and AZN 17,203 thousand profit (2017: AZN 9,330 thousand profit) to the net profit/(loss) before tax of the Fund (Net profit figure includes fair value increase of AZN 8,830 thousand (2017: AZN 1,168 thousand increase)).

11. INVESTMENTS IN JOINT VENTURES

The table below summarises the movements in the carrying amount of the Fund's investments in joint ventures.

In thousands of Azerbaijani Manats	2018	2017
Carrying amount at 1 January	**979,598**	**787,589**
Additions to investments in joint venture	151,646	193,500
Share of after tax results of joint venture	38,887	(1,491)
Loss from FX translation recognised in OCI	(2,917)	-
Carrying amount at 31 December	**1,167,214**	**979,598**

On 21 June 2013, Caspian Drilling Company (90% share) and SOCAR (10% share) jointly established "SOCAR Rig Assets" LLC with the share capital of AZN 1000 (100 shares, nominal value of AZN 10 for each share). The main activity of the entity is financing the construction of a new sixth generation semi-submersible drilling rig for operations in the Caspian Sea through funding from the shareholders' proportion of their respective shares. On 5 July 2013, SOFAZ

acquired all of the shares of "SOCAR Rig Assets" LLC from Caspian Drilling Company for their nominal value. "SOCAR Rig Assets" LLC did not have any operations prior to acquisition by the Fund. After acquisition "SOCAR Rig Assets" LLC was renamed "Azerbaijan Rigs" LLC. No additional paid-in capital was contributed during 2018 (2017: AZN 193,500 thousand). All strategic financial and operating decisions relating to the activity of the acquiree require the unanimous consent of both shareholding parties. The results of this joint venture are incorporated in these consolidated financial statements using the equity method of accounting.

Capitals Property S.a.r.l was established by Capitals Holding S.a.r.l on 29 January 2018 as a private limited liability company governed by the laws of the Grand Duchy of Luxembourg. When it was established, SOFAZ R.E Fund S.a.r.l and Capitals Holding S.a.r.l each held 50% of the share capital of the LLC in the amount of EUR 12,000 (12,000 shares with the nominal value of EUR 1 for each). On 21 September 2018 Capitals Holding S.a.r.l transferred 2,400 shares and SOFAZ R.E Fund S.a.r.l transferred 1,200 shares to Mainz International Holdings S.a.r.l. As a result the shareholder holdings are as follows: SOFAZ RE Fund S.a.r.l 40% ownership (4,800 shares), Capitals Holding S.a.r.l 30% ownership (3,600 shares), Mainz International Holdings S.a.r.l 30% ownership (3,600 shares). The main activity of the entity is real estate business through funding from the shareholders' proportion of their respective shares and bank loan. The Fund has contributed paid-in capital of AZN 151,646 thousand in 2018 (2017: nil) directly to the entity. All strategic financial and operating decisions relating to the activity of the acquiree require the unanimous consent of both shareholding parties. The results of this joint venture are incorporated in these consolidated financial statements using the equity method of accounting.

At 31 December 2018, the Fund's interests in its joint ventures and its summarised aggregate financial information, including total assets, liabilities, revenues and profit or loss, were as follows:

Name	Current assets	Non-current assets	Current liabilities	Non-current liabilities	Revenue	Other income	Expenses	Profit/ (loss)	% Interest held	Country of incorporation
"Azerbaijan Rigs" LLC	113,803	1,029,247	(7,514)	(7,872)	88,874	537	(50,189)	39,222	90%	Azerbaijan
"Capitals Property SARL" LLC	39,079	993,048	(4,051)	(647,287)	30,785	635	(22,453)	8,967	40%	Luxembourg

At 31 December 2017, the Fund's interests in its joint venture and its summarised aggregate financial information, including total assets, liabilities, revenues and profit or loss, were as follows:

Name	Current assets	Non-current assets	Current liabilities	Non-current liabilities	Revenue	Other income	Expenses	Profit/ (loss)	% interest held	Country of incorporation
"Azerbaijan Rigs" LLC	160,935	935,255	(7,748)	-	-	524	(2,181)	(1,657)	90%	Azerbaijan

Reconciliation of the summarised financial information presented to the carrying amount of its interest in the joint ventures is as follows:

	"Azerbaijan Rigs" LLC		"Capitals Property SARL" LLC	
	2018	2017	2018	2017
Opening net assets	**1,088,442**	**896,599**	-	-
Capital increase	-	193,500	371,822	-
Profit/(loss) for the period	39,222	(1,657)	8,967	-
Closing net assets	**1,127,664**	**1,088,442**	**380,789**	-
Fund's share in %	90%	90%	40%	-
Fund's share in amount	1,014,898	979,598	152,316	-
Carrying amount of investment	**1,014,898**	**979,598**	**152,316**	-

12. CAPITAL CONTRIBUTIONS

The movements in capital contributions to the Fund were as follows:

In thousands of Azerbaijani Manats	2018	2017
Contributions received from sales of oil and gas	16,645,569	11,029,989
Bonuses	765,228	2,408
Pipeline transit tariffs	18,103	17,915
Acreage fees	4,147	3,605
Other	20	-
Total capital contributions	**17,433,067**	**11,053,917**

13. NON-CURRENT LIABILITIES

In thousands of Azerbaijani Manats	2018	2017
Term loan (GK001 - Tokio, Japan)	479,681	469,979
Term loan (Mirae Asset Securities)	456,300	-
Tenancy deposits	48,414	40,087
Deferred tax liabilities	13,780	16,408
Other	-	3,375
Total non-current liabilities	**998,175**	**529,849**

Tenancy deposits comprise of prepayments made by tenants for Kirarito Ginza, the investment property in Tokyo with the amount of AZN 20,228 thousand (2017: AZN 15,627 thousand), Pine Avenue Tower A, the investment property in Seoul with the amount of AZN 26,434 thousand (2017: AZN 22,790 thousand) and SCI 8 Place Vendome, the investment property in Paris with the amount of AZN 1,751 thousand (2017: AZN 1,670 thousand).

The term loan comprises of borrowing by GK001 (Kirarito Ginza), denominated in Japanese Yen and borrowing by Mirae Asset Securities - Pine Avenue, denominated in Korean Won. Bank borrowings by GK001 mature by 09 September 2024 and bear coupon of 0.81% annually (2017: 0.81%). An investment property is pledged as collateral for the borrowing. Borrowings by Mirae Asset Securities mature by June 2023 and bear coupon of 3.6% annually. An investment property is pledged as collateral for the borrowing. Please refer to Note 10.

The Fund does not apply hedge accounting and has not entered into any hedging arrangements in respect of its foreign currency obligations or interest rate exposures.

The fair value of current borrowings approximates their carrying amount, as the impact of discounting is not significant. The fair values are based on cash flows discounted using a rate based on the borrowing rate of 0.81% (2017: 0.81%) for GK001 and 3.6% for Mirae Asset Securities. The fair values are within level 2 of the fair value hierarchy.

RECONCILIATION OF LIABILITIES ARISING FROM FINANCING ACTIVITIES

The table below sets out an analysis of liabilities from financing activities and the movements in the Fund's liabilities from financing activities for each of the periods presented. The items of these liabilities are those that are reported as financing in the statement of cash flows:

	Liabilities from financing activities
	Borrowing
Liabilities from financing activities at 1 January 2017	**472,007**
Foreign exchange adjustments	(2,028)
Liabilities from financing activities at 31 December 2017	**469,979**
Cash flows	456,300
Foreign exchange adjustments	9,702
Liabilities from financing activities at 31 December 2018	**935,981**

14. INTEREST INCOME FROM FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

In thousands of Azerbaijani Manats	2018	2017
Government securities	60,193	44,291
Agency securities	233,421	114,278
Corporate securities	546,902	343,745
Total interest income	**840,516**	**502,314**

15. FOREIGN CURRENCY TRANSLATION DIFFERENCES

Net foreign currency translation differences comprise of:

In thousands of Azerbaijani Manats	2018	2017
Net unrealized gain/(loss) on foreign currency translation differences	(1,375,080)	747,147
Net realized loss on foreign currency translation differences	(36,157)	(3,114)
Total net gain/(loss) on foreign currency translation differences	**(1,411,237)**	**744,033**

16. NET FAIR VALUE GAIN/(LOSS) ON FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

Net gain on financial assets at fair value through profit or loss comprises:

In thousands of Azerbaijani Manats	2018	2017
Unrealized gain/(loss) on change in fair value adjustment	(999,149)	75,740
Realized gain/(loss) on trading operations	151,640	(2,077)
Net gain/(loss) on financial assets at fair value through profit or loss	**(847,509)**	**73,663**

17. OPERATING EXPENSES

Operating expenses are comprised of:

In thousands of Azerbaijani Manats	2018	2017
Asset management fee	2,887	2,450
Operating expenses of subsidiaries	54,779	41,512
Wages, salaries and employee benefits	6,813	4,914
SSPF contributions	1,423	1,018
Bank services	2,575	2,088
Depreciation and amortization	8,478	9,020
Short-term license fee	4,735	4,122
Communication expenses	86	48
Other operating expenses	21,737	3,572
Total operating expenses	**103,513**	**68,744**

18. TRANSFERS BY THE FUND

During 2018 transfers to the State Budget, as well as to the state institutions, state-owned entities and companies were made in accordance with:

- The Decree #1770 of the President of the Republic of Azerbaijan dated 28 December 2017 on the Approval of the Budget of the State Oil Fund of the Republic of Azerbaijan for 2018.
- Decree #209 of the President of the Republic of Azerbaijan dated 17 July 2018 on making amendments to the Decree #1770 of the President of the Republic of Azerbaijan dated December 28, 2017 on "The Budget of the State Oil Fund of the Republic of Azerbaijan for 2018.

During 2017 transfers to the State Budget, as well as to the state institutions, state-owned entities and companies were made in accordance with:

- The Decree #1186 of the President of the Republic of Azerbaijan dated 10 January 2017 on the Approval of the Budget of the State Oil Fund of the Republic of Azerbaijan for 2017.
- Decree #1612 of the President of the Republic of Azerbaijan dated 04 October 2017 on making amendments to the Decree #1186 of the President of the Republic of Azerbaijan dated January 10, 2017 on "The Budget of the State Oil Fund of the Republic of Azerbaijan for 2017".

19. INCOME TAXES

The Fund provides for income taxes based on the tax accounts maintained and prepared in accordance with the tax regulations of Russian Federation, Luxembourg and France.

According to the Presidential decree №- 509-IVQD dated 21 December 2012, and law of State Parliament regarding changes to the Tax Code of Azerbaijan Republic dated 29 December 2012 starting from 1 January 2013 SOFAZ is exempted from corporate income tax. All the Jersey companies are zero corporate income tax rated by virtue of being International Service Entities. As a result there are no temporary differences in respect of SOFAZ's Azerbaijani and UK operations. According to double taxation treaty with Japan, gains from Tokumei Kumiai investments is exempt from taxation in this country. South Korea subsidiary is also exempt from taxes for the income generated from operations of its assets. It is only obliged for tax withholding when distributing earnings to unitholders.

Standard corporate income tax rates for companies operating in the Russian Federation comprised 20% for 2018 and 2017. Whereas Luxembourg and French subsidiaries are subject to income tax at a rate of 33% (2017: 33%).

Deferred taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes. Temporary differences relate mostly to different methods of income and expense recognition as well as to recorded values of certain assets.

20. FAIR VALUE DISCLOSURES

Fair value measurements are analysed by level in the fair value hierarchy as follows: (i) level one are measurements at quoted prices (unadjusted) in active markets for identical assets or liabilities, (ii) level two measurements are valuations techniques with all material inputs observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices), and (iii) level three measurements are valuations not based on observable market data (that is, unobservable inputs). Management applies judgement in categorising financial instruments using the fair value hierarchy. If a fair value measurement uses observable inputs that require significant adjustment, that measurement is a Level 3 measurement. The significance of a valuation input is assessed against the fair value measurement in its entirety.

(a) Recurring fair value measurements

Recurring fair value measurements are those that the accounting standards require or permit in the statement of financial position at the end of each reporting period. The level in the fair value hierarchy into which the recurring fair value measurements are categorised are as follows:

In thousands of Azerbaijani Manats	31-Dec-18				31-Dec-17			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Assets at fair value								
Financial Assets								
Financial assets at fair value through profit or loss	**49,633,997**	**5,450,817**	**2,253,461**	**57,338,275**	**45,486,013**	**6,900**	**1,440,247**	**46,933,160**
- Agency/ Supranational bonds	13,082,224	-	-	13,082,224	8,056,922	-	-	8,056,922
- Corporate bonds	23,336,142	5,450,817	-	28,786,959	22,049,530	6,900	-	22,056,430
- Sovereign bonds	2,915,648	-	-	2,915,648	2,008,809	-	-	2,008,809
- Private Equity Funds	-	-	641,363	641,363	-	-	441,542	441,542
- Real Estate Funds	-	-	1,612,098	1,612,098	-	-	998,705	998,705
- Equity securities	6,229,752	-	-	6,229,752	7,090,424	-	-	7,090,424
- Money Market	4,070,231	-	-	4,070,231	6,280,328	-	-	6,280,328
Non-financial Assets	**3,558,246**	-	**2,584,684**	**6,142,930**	**2,137,212**	-	**2,763,757**	**4,900,969**
- Investment properties	-	-	2,584,684	2,584,684	-	-	2,763,757	2,763,757
- Gold bullions	3,558,246	-	-	3,558,246	2,137,212	-	-	2,137,212
Total assets recurring fair value measurements	**53,192,243**	**5,450,817**	**4,838,145**	**63,481,205**	**47,623,225**	**6,900**	**4,204,004**	**51,834,129**

The description of valuation technique and description of inputs used in the fair value measurement for level 2 measurements at 31 December 2018:

In thousands of Azerbaijani Manats	Fair value	Valuation technique	Inputs used
ASSETS AT FAIR VALUE FINANCIAL ASSETS			
- Corporate bonds	5,450,817	DCF	Government bonds yield curve

The valuation technique, inputs used in the fair value measurement for level 3 measurements and related sensitivity to reasonably possible changes in those inputs are as follows at 31 December 2018:

In thousands of Azerbaijani Manats	Fair value	Valuation technique	Inputs used	Range of inputs (weighted average)	Reasonable change	Sensitivity of fair value measurement
Assets at fair value Non-financial assets						
Investment properties						
"78 St James Street", London	258,348	Residual appraisal approach	Net rental value	AZN 18,137 thousand	+/- 5%	19,604/ (18,623)
"Gallery Actor", Moscow	80,092	Discounted cash flows	Target rate of return	12-15%	+/- 1%	(2,889)/ 3,031
"SCI 8 Place Vendome", Paris	362,328	Income capitalisation method, Discounted cash flows, Direct comparison method	Market yield	3.5-4 5%	+/- 0.5%	(33,942)/49,596
"Pine Avenue Tower A", Seoul	784,076	Discounted cash flows, Comparison method	Target rate of return/ Transaction case price	5-5.3%, AZN 10,951-12,624 per sq.m	+/- 0.25%, +/- 5%	(14,213)/ 15,651, 18,764/ 18,685
"Kirarito Ginza", Tokyo	897,373	Income capitalisation method	Market yield	2.4%	+/- 0.1%	(32,351)/35,432
"Palazzo Turati", Milan	202,467	Discounted cash flows	WACC and GOCR	5.01-4.07%	+/- 0.25%	(389)/389
Total recurring fair value measurements at level 3	**2,584,684**					

For investments in equity and real estate funds, increases in the EBITDA multiple would each lead to an increase in estimated value. However, an increase in the discount for lack of marketability would lead to a decrease in value. No interrelationships between unobservable inputs used in the Fund's valuation of its Level 3 fund investments have been identified.

A reconciliation of movements in Level 3 of the fair value hierarchy by class of instruments for the year ended 31 December 2018 is as follows:

In thousands of Azerbaijani Manats	Securities at FVTPL Corporate shares
Fair value at 1 January 2018	**1,440,247**
Gains recognised in profit or loss for the year	165,375
Loss recognised in other comprehensive income	(63,077)
Purchases	710,916
Fair value at 31 December 2018	**2,253,461**

A reconciliation of movements in Level 3 of the fair value hierarchy by class of instruments for the year ended 31 December 2017 is as follows:

In thousands of Azerbaijani Manats	Securities at FVTPL Corporate shares
Fair value at 1 January 2017	**737,966**
Gains recognised in profit or loss for the year	50,686
Gains recognised in other comprehensive income	35,517
Purchases	616,078
Fair value at 31 December 2017	**1,440,247**

b) ***Assets and liabilities not measured at fair value but for which fair value is disclosed***

Fair values analysed by level in the fair value hierarchy and carrying value of assets not measured at fair value are as follows:

In thousands of Azerbaijani Manats	31-Dec-18				31-Dec-17			
	Level 1	Level 2	Level 3	Carrying value	Level 1	Level 2	Level 3	Carrying value
Assets								
Financial assets at amortised cost								
- Corporate bonds	-	-	-	-	-	5,337,216	-	5,337,216
Other financial assets								
- Trade receivables	-	4,382	-	4,382	-	2,397	-	2,397
Total Assets	-	**4,382**	-	**4,382**	-	**5,339,613**	-	**5,339,613**
Liabilities								
Other borrowed funds								
- Term loan	-	935,981	-	935,981	-	469,979	-	469,979
Other financial liabilities								
- Trade payables	-	16,154	-	16,154	-	15,566	-	15,566
Total Liabilities	-	**952,135**	-	**952,135**	-	**485,545**	-	**485,545**

The fair values in level 2 of fair value hierarchy were estimated using the discounted cash flows valuation technique. The fair value of floating rate instruments that are not quoted in an active market was estimated to be equal to their carrying amount. The fair value of unquoted fixed interest rate instruments was estimated based on estimated future cash flows expected to be received discounted at current interest rates for new instruments with similar credit risk and remaining maturity.

21. PRESENTATION OF FINANCIAL INSTRUMENTS BY MEASUREMENT CATEGORY

For the purposes of measurement, IFRS 9 "Financial Instruments" classifies financial assets into the following categories: (a) financial assets at FVTPL; (b) debt instruments at FVOCI, (c) equity instruments at FVOCI and (c) financial assets at AC. Financial assets at FVTPL have two sub-categories: (i) assets mandatorily measured at FVTPL, and (ii) assets designated as such upon initial recognition or subsequently. In addition, finance lease receivables form a separate category.

The following table provides a reconciliation of financial assets with these measurement categories as of 31 December 2018:

In thousands of Azerbaijani Manats	FVTPL (mandatory)	AC	Total
ASSETS			
Cash and cash equivalents	-	-	**1,264,588**
- Short-term deposits	-	4,437	4,437
- Money market funds	553,139	-	553,139
- Bank accounts	-	707,012	707,012
FVTPL assets	-	-	**57,338,275**
- Agency/Supranational bonds	13,082,224	-	13,082,224
- Corporate bonds	28,786,959	-	28,786,959
- Sovereign bonds	2,915,648	-	2,915,648
- Money market	4,070,231	-	4,070,231
- Private Equity Funds	641,363	-	641,363
- Real Estate Funds	1,612,098	-	1,612,098
- Equity securities	6,229,752	-	6,229,752
Other financial assets	-	-	**4,382**
-Other	-	4,382	4,382
TOTAL FINANCIAL ASSETS	**57,891,414**	**715,831**	**58,607,245**

For the purposes of measurement, IAS 39, Financial Instruments: Recognition and Measurement, classifies financial assets into the following categories: (a) loans and receivables; (b) available-for-sale financial assets; (c) financial assets held to maturity and (d) financial assets at fair value through profit or loss ("FVTPL"). Financial assets at fair value through profit or loss have two sub-categories: (i) assets designated as such upon initial recognition, and (ii) those classified as held for trading. In addition, finance lease receivables represent a separate category. The following table provides a reconciliation of financial assets with these measurement categories as of 31 December 2017:

In thousands of Azerbaijani Manats	Loans and receivables	Trading assets	Assets designated at FVTPL	Held to maturity	Total
ASSETS					
Cash and cash equivalents	-	-	-	-	**2,747,381**
- Short-term deposits	2,134,556	-	-	-	2,134,556
- Money market funds	198,518	-	-	-	198,518
- Bank accounts	414,307	-	-	-	414,307
Financial assets at fair value through profit or loss	-	-	-	-	**46,933,160**
- Agency/Supranational bonds	-	8,056,922	-	-	8,056,922
- Corporate bonds	-	22,056,430	-	-	22,056,430
- Sovereign bonds	-	2,008,809	-	-	2,008,809
- Money Market	-	6,280,328	-	-	6,280,328
- Private Equity Funds	-	-	441,542	-	441,542
- Real Estate Funds	-	-	998,705	-	998,705
- Equity securities	-	7,090,424	-	-	7,090,424
Investments held to maturity	-	-	-	-	**5,337,216**
- Corporate bonds	-	-	-	5,337,216	5,337,216
Other	2,397	-	-	-	**2,397**
TOTAL FINANCIAL ASSETS	**2,749,778**	**45,492,913**	**1,440,247**	**5,337,216**	**55,020,154**

As of 31 December 2018 and 31 December 2017, all of the Fund's financial liabilities were carried at AC.

22. FINANCIAL RISK MANAGEMENT

Management of risk is an essential element of the Fund's operations. Risks inherent to the Fund's operations are those related to credit exposures, liquidity, market and operational risks. A summary description of the Fund's risk management policies in relation to those risks is discussed below.

Credit risk. The Fund is exposed to credit risk which is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. The Fund is subject to credit risk from its portfolio of cash and cash equivalents and its investments. The Fund manages its credit risk in accordance with the "Rules on Holding, Placement and Management of Foreign Currency Assets of The State Oil Fund of the Republic of Azerbaijan" approved by Decree #511 of the President of the Republic of Azerbaijan dated 19 June 2001 as amended by Decree #607 dated 21 December 2001, Decree #202 dated 1 March 2005, Decree #216 dated 10 February 2010, Decree #519 dated 27 October 2011 (hereinafter collectively referred to as the "Rules").

Credit risk is managed and controlled through proper selection of investment assets, credit quality of investment assets and setting limits on the amount of investment per investment asset.

The following table details the credit ratings of financial instruments held by the Fund. The credit rating is issued by internationally regarded agencies Standard & Poor's, Fitch and Moody's. If the agencies have assigned different credit ratings to an asset, the lowest one was used.

2018	AAA	AA	A	BBB	BB	B	D	Total
Cash and cash equivalents*	553,139	5,560	151,933	550,050	1,661	1,425	-	**1,263,768**
Financial assets at fair value through profit or loss**	10,978,994	6,495,932	16,190,765	7,704,085	6,049,317	1,432,592	3,377	**48,855,062**

* AZN 820 thousand – bank account at Central Bank of the Republic of Azerbaijan was excluded as Central Banks do not have credit rating

** Equity securities in the amount of AZN 6,230 million and investments in Real Estate and Private Equity Funds in the amount of AZN 2,253 million are excluded from this table. The Fund has investment strategies for investments in Real Estate and Private Equity funds. The Fund performs comprehensive review process where assesses the investment experience of the funds, opinions of shareholders in the previous investments of General Partner, knowledge and experience of staff, financial facilities used in fund's organization and cash flow management and evaluates them by 10 points scale. As of 31 December 2018, the scores awarded for Real Estate and Private Equity funds are in the range of 8-9 and 7-8, respectively.

2017	AAA	AA	A	BBB	Non-investment rating	Securities without rating	Total
Cash and cash equivalents	198.518	-	62.606	335.669	2.139.300	11.288	**2,747,381**
Financial assets at fair value through profit or loss	6,443,521	4.712.609	17,691.366	8.096.917	1.451.176	8.537.571	**46,933,160**
Financial assets at amortised cost	-	-	-	-	5.337.216	-	**5,337,216**

Equity securities portfolio represent a passive replication of broad indices (MSCI World, MSCI Europe ex UK, S&P 100), where the Fund relies on Tracking Error metrics. Ex-ante tracking error limits are established at the level of 30 bps on an annual basis.

The Fund also reports on such market risk metrics as Standard deviation, Value at Risk (VaR), Beta in its internal reports.

External managers. In accordance with the "Rules", when an external manager is engaged in management of the Fund's currency assets, the external manager or its principal founder should have investment credit ratings (not lower than Baa3 (Moody's) or BBB- (Standard & Poor's, Fitch)) or have at least five years of positive history of management of assets, or be experienced in managing assets with a value not less than one billion USD.

Currency risk. Currency risk is defined as the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Fund is exposed to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. Currency risk is managed according to the currency allocation set in Investment Policy, which states firm weights for specific currencies. Apart from that according to Investment Guidelines the Fund has a discretion of using currency derivatives for hedging purposes. Currency rebalancing is implemented quarterly in line with internal procedures. Currency allocation is implemented in the multi-asset and diversified Fund investment portfolio context.

The table below summarizes the Fund's exposure to foreign currency exchange rate risk for the year ended 31 December 2018:

2018	AZN	USD	EUR	GBP	TRY	AUD	RUB	Other	Total
Financial assets									
Cash and cash equivalents	895	946.368	156.640	104.004	1,313	5,899	2,543	46,926	1,264,588
Financial Assets at Fair Value Through Profit or Loss	-	29,528,796	21,657,260	2,646,222	524,211	380,231	316,871	2,284,684	57,338,275
Other financial assets	-	-	-	1,783	-	-	1,379	1,220	4.382
Total financial assets	**895**	**30,475,164**	**21,813,900**	**2,752,009**	**525,524**	**386,130**	**320,793**	**2,332,830**	**58,607,245**
Financial liabilities									
Borrowings	-	-	-	-	-	-	-	(935,981)	(935,981)
Other financial liabilities	(1,320)	-	(2,805)	(71)	-	-	(501)	(11,457)	(16,154)
Total financial liabilities	**(1,320)**	-	**(2,805)**	**(71)**	-	-	**(501)**	**(947,438)**	**(952,135)**
Open position	**(425)**	**30,475,164**	**21,811,095**	**2,751,938**	**525,524**	**386,130**	**320,292**	**1,385,392**	**57,655,110**

The table below summarizes the Fund's exposure to foreign currency exchange rate risk for the year ended 31 December 2017:

2017	AZN	USD	EUR	GBP	TRY	AUD	RUB	Other	Total
Financial assets									
Cash and cash equivalents	11,332	358,900	1,592,489	100,240	636,561	1,626	3,352	42,881	2,747,381
Financial Assets at Fair Value Through Profit or Loss	-	21,451,624	19,573,829	2,589,744	-	423,790	532,002	2,362,171	46,933,160
Financial assets at amortised cost	-	5,337,216	-	-	-	-	-	-	5,337,216
Other financial assets	-	-	921	50	-	-	681	745	2,397
Total financial assets	**11,332**	**27,147,740**	**21,167,239**	**2,690,034**	**636,561**	**425,416**	**536,035**	**2,405,797**	**55,020,154**
Financial liabilities									
Borrowings	-	-	-	-	-	-	-	(469,979)	(469,979)
Other financial liabilities	(1,132)	-	(1,879)	(5,458)	-	-	-	(7,097)	(15,566)
Total financial liabilities	**(1,132)**	**-**	**(1,879)**	**(5,458)**	**-**	**-**	**-**	**(477,076)**	**(485,545)**
Open position	**10,200**	**27,147,740**	**21,165,360**	**2,684,576**	**636,561**	**425,416**	**536,035**	**1,928,721**	**54,534,609**

Currency risk sensitivity. The tables below indicate the currencies to which the Fund had significant exposure at 31 December 2018 and 2017 on its monetary assets and its forecast cash flows. The analysis calculates the effect of a reasonably possible movement of the currency rate against the AZN, with all other variables held constant on the statement of profit or loss and other comprehensive income.

	Impact on profit/ (loss) for the year		Impact on equity	Impact on profit/ (loss) for the year		Impact on equity
	31-Dec-18			31-Dec-17		
AZN/USD	10.00%	3,047,516	3,047,516	10.00%	2,714,774	2,714,774
	10.00%	(3,047,516)	(3,047,516)	10.00%	(2,714,774)	(2,714,774)
AZN/EUR	10.00%	2,181,110	2,430,770	10.00%	2,116,536	2,278,156
	10.00%	(2,181,110)	(2,430,770)	10.00%	(2,116,536)	(2,278,156)
AZN/GBP	10.00%	275,194	308,827	10.00%	268,458	312,014
	10.00%	(275,194)	(308,827)	10.00%	(268,458)	(312,014)
AZN/TRY	10.00%	52,552	52,552	10.00%	63,656	63,656
	10.00%	(52,552)	(52,552)	10.00%	(63,656)	(63,656)
AZN/AUD	10.00%	38,613	38,613	10.00%	42,542	42,542
	10.00%	(38,613)	(38,613)	10.00%	(42,542)	(42,542)
AZN/RUB	10.00%	32,029	39,250	10.00%	53,605	64,561
	10.00%	(32,029)	(39,250)	10.00%	(53,605)	(64,561)

Commodity price risk. The Fund is affected by the volatility of gold prices. The following table shows the effect of price changes in gold:

	31-Dec-18		31-Dec-17	
AZN/XAU	10%	-10%	10%	-10%
Impact on profit/(loss) for the year	355,825	(355,825)	213,721	(213,721)
Impact on equity	355,825	(355,825)	213,721	(213,721)

Geographical concentration. The geographical concentration of the Fund's financial assets and liabilities at 31 December 2018 is set out below:

2018	Azerbaijan	Europe	America	Asia	Australia and Oceania	International organizations	Total
Financial assets							
Cash and cash equivalents	933	785,999	436,821	40,835	-	-	1,264,588
Financial Assets at Fair Value Through Profit or Loss	6,957,699	22,405,476	14,727,172	6,512,370	1,727,172	5,008,386	57,338,275
Other financial assets	-	3,162	-	1,220	-	-	4,382
Total financial assets	**6,958,632**	**23,194,637**	**15,163,993**	**6,554,425**	**1,727,172**	**5,008,386**	**58,607,245**
Financial liabilities							
Borrowings	-	-	-	(935,981)	-	-	(935,981)
Other financial liabilities	(1,320)	(3,377)	-	(11,457)	-	-	(16,154)
Total financial liabilities	**(1,320)**	**(3,377)**	**-**	**(947,438)**	**-**	**-**	**(952,135)**
Net position	**6,957,312**	**23,191,260**	**15,163,993**	**5,606,987**	**1,727,172**	**5,008,386**	**57,655,110**

The geographical concentration of the Fund's financial assets and liabilities at 31 December 2017 is set out below:

2017	Azerbaijan	Europe	America	Asia	Australia and Oceania	International organizations	Total
Financial assets							
Cash and cash equivalents	11,339	2,459,785	273,133	3,124	-	-	2,747,381
Financial Assets at Fair Value Through Profit or Loss	1,451,176	19,865,602	16,709,896	4,321,758	1,650,949	2,933,779	46,933,160
Financial assets at amortised cost	5,337,216	-	-	-	-	-	5,337,216
Other financial assets	-	971	1,426	-	-	-	2,397
Total financial assets	**6,799,731**	**22,326,358**	**16,984,455**	**4,324,882**	**1,650,949**	**2,933,779**	**55,020,154**
Financial liabilities							
Borrowings	-	-	-	(469,979)	-	-	(469,979)
Other financial liabilities	(1,132)	(7,337)	-	(7,097)	-	-	(15,566)
Total financial liabilities	**(1,132)**	**(7,337)**	**-**	**(477,076)**	**-**	**-**	**(485,545)**
Net position	**6,798,599**	**22,319,021**	**16,984,455**	**3,847,806**	**1,650,949**	**2,933,779**	**54,534,609**

Other risk concentrations. Management monitors and discloses concentrations of credit risk by comparing reports from portfolios with investment policy of the Fund approved by the President of the Azerbaijan Republic. The Fund did not have any such significant risk concentrations at 31 December 2018 and 2017.

Interest Rate Risk. The Fund takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows as fixed income securities account for the largest portion of the investment portfolio. Interest margins may increase as a result of such changes, but may reduce or create losses in the event that unexpected movements arise. Management sets limit maximum of 48 months (duration of 4) on average for the portfolio.

Interest rate sensitivity. At 31 December 2018 and 2017 deposits and debt securities were interest-bearing and, therefore, were exposed to the interest rate risk. Depending on the market conditions the Fund is managing this risk by gradually increasing or decreasing the duration of assets in the investment portfolio. Daily risk management and monitoring is performed within above set limits by the Risk Management Department.

The following table presents a net impact of change of the fair value of securities, when market interest rate changed by 1%. Sensitivity analysis of interest rate risk has been determined based on "reasonably possible changes in the risk variable". The level of these changes is determined by management and is contained within the risk reports provided to key management personnel.

Impact on profit/(loss) before tax:

	31-Dec-18		31-Dec-17	
	Interest rate 1%	Interest rate -1%	Interest rate 1%	Interest rate -1%
Assets:				
Cash and cash equivalents	15	(15)	64	(64)
Financial assets at fair value through profit or loss	(334,166)	334,166	(352,622)	352,622
Net impact on profit/(loss) before tax	**(334,151)**	**334,151**	**(352,558)**	**352,558**
Impact on equity	**(334,151)**	**334,151**	**(352,558)**	**352,558**

Liquidity risk. Management's guiding policies are to maintain conservative levels of liquidity to ensure that the Fund has the ability to meet its obligations under all conceivable circumstances. Liquidity risk requires to hold at least of 100 million USD in cash and cash equivalents and is monitored on a daily basis. Due to budget transfers throughout the year liquidity issue is addressed in the Fund's asset class allocation (at least 60% to be invested in highly liquid Debt obligations and money market sub-portfolio), which in turn further contributes to liquidity of the Fund's investment portfolio.

The table below shows liabilities at 31 December 2018 by their remaining contractual maturity. The amounts of liabilities disclosed in the maturity table are the contractual undiscounted cash flows. Such undiscounted cash flows differ from the amount included in the statement of financial position because the amount in the statement of financial position is based on discounted cash flows.

An analysis of the liquidity risk of financial position items is presented in the following tables.

2018	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Maturity undefined	Total
Financial assets							
Cash and cash equivalents	4,437	-	-	-	-	1,260,151	1,264,588
Financial assets at fair value through profit or loss	3,093,230	2,065,143	7,886,959	28,646,098	9,417,093	6,229,752	57,338,275
Other financial assets	4,382	-	-	-	-	-	4,382
Total financial assets	**3,102,049**	**2,065,143**	**7,886,959**	**28,646,098**	**9,417,093**	**7,489,903**	**58,607,245**
Financial liabilities							
Borrowings	(327)	(4,760)	(15,261)	(1,014,750)	-	-	(1,035,098)
Other financial liabilities	(16,154)	-	-	-	-	-	(16,154)
Total financial liabilities	**(16,481)**	**(4,760)**	**(15,261)**	**(1,014,750)**	**-**	**-**	**(1,051,252)**
Liquidity gap	**3,085,568**	**2,060,383**	**7,871,698**	**27,631,348**	**9,417,093**	**7,489,903**	**57,555,993**

2017	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Maturity undefined	Total
Financial assets							
Cash and cash equivalents	1,879,422	255,134	-	-	-	612,825	2,747,381
Financial assets at fair value through profit or loss	2,972,772	3,278,077	5,915,252	24,512,958	3,163,677	7,090,424	46,933,160
Financial assets at amortised cost	64,788	-	72,497	-	5,199,931	-	5,337,216
Other financial assets	2,397	-	-	-	-	-	2,397
Total financial assets	**4,919,379**	**3,533,211**	**5,987,749**	**24,512,958**	**8,363,608**	**7,703,249**	**55,020,154**
Financial liabilities							
Borrowings	(327)	(653)	(2,940)	(506,246)	-	-	(510,166)
Other financial liabilities	(15,566)	-	-	-	-	-	(15,566)
Total financial liabilities	**(15,893)**	**(653)**	**(2,940)**	**(506,246)**	**-**	**-**	**(525,732)**
Liquidity gap	**4,903,486**	**3,532,558**	**5,984,809**	**24,006,712**	**8,363,608**	**7,703,249**	**54,494,422**

Price risk. Price risk is the risk that the value of a financial instrument will fluctuate as a result of changes in market prices whether those changes are caused by factors specific to the individual security or its issuer or factors affecting all securities traded in the market. The Fund is exposed to price risks of its products which are subject to general market and specific fluctuations.

	31-Dec-18		31-Dec-17	
	1% increase in securities price	1% decrease in securities price	1% increase in securities price	1% decrease in securities price
Impact on profit/(loss) before tax	573,383	(573,383)	469,332	(469,332)
Impact on net assets/equity	573,383	(573,383)	469,332	(469,332)

Operational risk. Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Fund cannot expect to eliminate all operational risks, but a control framework and monitoring and responding to potential risks could be effective tools to manage the risks. Controls should include effective segregation of duties, access, authorization and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

23. COMMITMENTS AND CONTINGENCIES

Off-balance sheet transactions. On 11 August 2006 the Fund signed an Asset Management Agreement on "Granting free budget (balance) Funds to trust management" with the Ministry of Finance of the Republic of Azerbaijan. According to this agreement free budget Funds of the Ministry of Finance of the Republic of Azerbaijan are to be transferred to and managed by the Fund within the asset management rules set in the agreement with the Ministry of Finance of the Republic of Azerbaijan. The Fund manages these assets free of charge, on behalf of the Ministry of Finance and in favor, at the expense and at the risks of the Ministry of Finance of the Republic of Azerbaijan. At 31 December 2018 assets received under the above agreement were AZN 577,064 thousand (31 December 2017: AZN 755,380 thousand) including accrued interest.

24. TRANSACTIONS WITH RELATED PARTIES

Parties are generally considered to be related if the parties are under common control, or one party has the ability to control the other party or can exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

Transactions between the Fund and its subsidiaries, which are related parties of the Fund, have been eliminated on consolidation and are not disclosed in this note. All government entities and their subsidiaries are considered to be entities under common control with the Fund. Transactions with such entities are disclosed below as related party transactions:

	Year	Contributions received from related parties	Carrying value of investment in joint venture	Transfers to related parties	Carrying value of bonds acquired from related parties	Interest income on bonds acquired from related parties	Bank accounts with related parties	Off-balance sheet transactions
SOCAR	2018	16,525,824						
	2017	10,973,191						
Operating Companies	2018	907,243						
	2017	80,726						
The State Budget	2018			10,959,000				
	2017			6,100,000				
Ministry of Finance of the Republic of Azerbaijan	2018				74,289	3,917		577,064
	2017				78,758	1,262		755,380
Azerbaijan melioration and water-sludge system OSC	2018			89,999				
	2017			69,997				
Ministry of Transport, Communications and High Technologies of the Republic of Azerbaijan	2018			176,128				
	2017			20,557				
State Committee for Affairs of Refugees and Internally Displaced Persons and Social Development Fund of the Internally Displaced Persons of the Republic of Azerbaijan	2018			199,979				
	2017			105,000				
Central Bank of the Republic of Azerbaijan	2018						820	
	2017			3,949,485			11,288	
Star oil refinery complex (SOCAR)	2018							
	2017			735,422				
Ministry of Education of the Republic of Azerbaijan	2018			7,236				
	2017			17,010				
International Bank of Azerbaijan	2018				1,432,593	55,571	112	
	2017				1,372,418	18,591	43	
Southern Gas Corridor CJSC	2018				4,412,344	147,997		
	2017				4,560,936	107,923		
Mercury Investments and Holdings Ltd.	2018				260,336	10,548		
	2017				299,218	8,569		
Azerbaijan (ACG) Ltd.	2018				337,452	13,150		
	2017				477,062	11,323		
SOCAR (Absheron)	2018				440,686	8,222		
	2017							
"Azerbaijan Rigs" LLC	2018		1,014,898					
	2017		979,598					
"Capitals Property S.a.r.l" LLC	2018		152,316					
	2017							

Key management personnel

The senior management group consists of the Fund's Executive Director and heads of administrations. The aggregate remuneration of members of the senior management group and the number of managers determined on a full-time equivalent basis receiving remuneration within this category are:

In thousands of Azerbaijani Manats	2018	2017
Short-term benefits:		
-Salary expense	299	126
-SSPF expense	65	28
Number of persons	3	3

25. INTERESTS IN STRUCTURED ENTITIES

Consolidated structured entities. A Tokumei Kumiai ("TK") agreement is a contractual arrangement under which one or more silent investors (the "TK investor") makes a contribution to a Japanese operating company (the "TK operator") in return for a share in the profit/loss of a specified business conducted by the TK operator (the "TK business"). To support the tax status of the TK, a Japanese resident company should have independent stake in the TK business. To comply with TK-GK rules, SOFAZ and Mitsubishi UFJ Trust and Banking ("MUTB") entered into TK arrangement to acquire Kirarito Ginza where MUTB is a Japanese resident and contributed 2% of the investment amount JPY 1,100 mln (AZN 9,643 thousand) required for TK Business, i.e. for TK Operator to acquire the property. TK-GK tax structure was chosen to obtain 0% withholding tax on distribution of TK profits to SOFAZ under Japan-former Soviet Union tax treaty. According to the agreement the total amount of SOFAZ's investment constituted JPY 51,989 mln (AZN 455,736 thousand). In return both SOFAZ and MUTB were entitled to a proportional share of profit or loss of TK Business. In 2016 MUTB was replaced by PGIM Foreign Investment Inc, who acquired MUTB's interests in the structure and took over the asset management role. The Asset Managers of PGIM Foreign Investment Inc is PGIM Real Estate (Japan).

The TK operator invested proceeds from investors in a retail complex in Ginza, Tokyo, for JPY 52,300 mln (AZN 458,462 thousand). The building met the definition of an investment property under IAS 40. SOFAZ signed an Agreement with the TK operator that contains the Strategic Plan on the development and management of the investment property. The TK operator operates the business of the company according to the Agreement and the Strategic Plan. TK agreement provides SOFAZ with limited rights with respect to the management and development of the investment property. This makes the TK operator similar to unconsolidated structured entities under IFRS 12, where a structured entity is an entity that has been designed so that voting or similar rights are not dominant factors in its management and control. Under this arrangement, voting rights relate to the administrative tasks only and relevant activities of the company are directed by means of contractual arrangements.

Based on the specific characteristics of the TK Agreement, the management concluded that a principal/agent relationship exists between SOFAZ and the TK operator. According to IFRS 10, the investor should treat decision making powers delegated to the agent as held by the investor/principal himself. The management performed analysis based on paragraph B60 of IFRS 10 and given the limited 2% investment by the Asset Managers, concluded that the TK operator is an agent of SOFAZ and hence, SOFAZ should consolidate the investee.

26. EVENTS AFTER THE REPORTING PERIOD

In accordance with the Decree of the President of the Republic of Azerbaijan on the Approval of the Budget of the State Oil Fund of the Republic of Azerbaijan for 2019" dated 28 December 2018, the Fund's budgeted contributions and distributions for the year of 2019 are estimated at AZN 15,450,150 thousand and AZN 11,595,238 thousand, respectively.

The following main types of distributions for 2019 are budgeted:

- Upper bound of transfer to the State Budget of the Republic of Azerbaijan – AZN 11,364,300 thousand;
- Financing of the measures for improvement of social conditions of refugees and internally displaced people AZN 200,000 thousand;
- Administrative expenses of the State Oil Fund of the Republic of Azerbaijan – AZN 30,938 thousand

27. ACCOUNTING POLICIES BEFORE 1 JANUARY 2018

Accounting policies applicable to the comparative period ended 31 December 2017 that were amended by IFRS 9 are as follows.

Financial instruments – key measurement terms. Depending on their classification financial instruments are carried at fair value or amortised cost.

Classification of financial assets. Financial assets have the following categories: (a) loans and receivables; (b) available-for-sale financial assets; (c) financial assets held to maturity and (d) financial assets at fair value

through profit or loss. Financial assets at fair value through profit or loss have two sub-categories: (i) assets designated as such upon initial recognition, and (ii) those classified as held for trading.

Loans and receivables are unquoted non-derivative financial assets with fixed or determinable payments other than those that the Fund intends to sell in the near term.The Fund's loans and receivables comprise of 'trade and other receivables' and 'cash and cash equivalents' in the statement of financial position.

Held-to-maturity assets include quoted non-derivative financial assets with fixed or determinable payments and fixed maturities that the Fund has both the intention and ability to hold to maturity. Management determines the classification of investment securities held to maturity at their initial recognition and reassesses the appropriateness of that classification at the end of each reporting period.

Held-for-trading investments are financial assets which are either acquired for generating a profit from short-term fluctuations in price or trader's margin, or are securities included in a portfolio in which a pattern of short-term trading exists. The Fund classifies securities into trading investments if it has an intention to sell them within a short period after purchase, i.e. within 12 months.

The Fund may choose to reclassify a non-derivative trading financial asset out of the fair value through profit or loss category if the asset is no longer held for the purpose of selling it in the near term. Financial assets other than loans and receivables are permitted to be reclassified out of the fair value through profit or loss category only in rare circumstances arising from a single event that is unusual and highly unlikely to reoccur in the near term. Financial assets that would meet the definition of loans and receivables may be reclassified if the Fund has the intention and ability to hold these financial assets for the foreseeable future or until maturity.

Other financial assets at fair value through profit or loss are financial assets designated irrevocably, at initial recognition, into this category. Management designates financial assets into this category only if (a) such classification eliminates or significantly reduces an accounting mismatch that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases; or (b) a group of financial assets, financial liabilities or both is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information on that basis is regularly provided to and reviewed by the Fund's key management personnel. Recognition and measurement of this category of financial assets is consistent with the accounting policy for trading investments.

All other financial assets are included in the *available-for-sale* category, which includes investment securities which the Fund intends to hold for an indefinite period of time and which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

Trading investments. Trading investments are carried at fair value. Interest earned on trading investments calculated using the effective interest method is presented as finance income in profit or loss for the year. Dividends are included in other income when the Fund's right to receive the dividend payment is established and it is probable that the dividends will be collected. All other elements of the changes in the fair value and gains or losses on derecognition are recorded in profit or loss for the year as gains less losses from trading investments in the period in which they arise.

Classification of financial liabilities. Financial liabilities have the following measurement categories: (a) held for trading which also includes financial derivatives and (b) other financial liabilities. Liabilities held for trading are carried at fair value with changes in value recognised in profit or loss for the year (as finance income or finance costs) in the period in which they arise. Other financial liabilities are carried at amortised cost. The Fund's other financial liabilities comprise of 'other payables' and 'borrowings' in the statement of financial position.

APPENDIX

Sovereign Wealth Funds
'Santiago Principles'
Generally Accepted Principles And Practices
Self-Assessment

April, 2019

Narration of Principles / Sub-Principles	Responses
A. Legal Framework, Objectives, and Coordination with Macroeconomic Policies.	
GAPP 1. PRINCIPLE. The legal framework for the SWF should be sound and support its effective operation and the achievement of its stated objective(s).	Legal framework of SOFAZ is clearly defined in the "Statute of the State Oil Fund of the Republic of Azerbaijan" (hereinafter "Statute of SOFAZ") approved by the decree of the President of the Republic of Azerbaijan.
GAPP 1.1. Subprinciple The legal framework for the SWF should ensure legal soundness of the SWF and its transactions.	SOFAZ is a legal entity separate from the government or central bank. The Fund's operation is guided by the Constitution and laws of the Republic of Azerbaijan, Presidential Decrees and resolutions, and the Fund's Regulations.
GAPP 1.2. Subprinciple The key features of the SWF's legal basis and structure, as well as the legal relationship between the SWF and other state bodies, should be publicly disclosed.	All relevant documents related to the legal basis and structure and the legal relationships between SOFAZ and the other government agencies are publicly disclosed and they are available on the Fund's website For further information: https://www.oilfund.az/storage/images/cotiii74r3.pdf
GAPP 2. PRINCIPLE The policy purpose of the SWF should be clearly defined and publicly disclosed.	SOFAZ was established for the purpose of accumulation and management of the revenues generated from implementation of oil and gas agreements. SOFAZ's primary objectives are to help maintain macroeconomic stability in the country (neutralize negative impact of the currency inflows) and to generate wealth for present and future generations. Above discussed purpose of establishment, as well as the primary objectives are publicly disclosed on the Funds website. For further information: https://www.oilfund.az/storage/images/rt3csc0jvm.pdf https://www.oilfund.az/en/fund/about/mission
GAPP 3. PRINCIPLE Where the SWF's activities have significant direct domestic macroeconomic implications, those activities should be closely coordinated with the domestic fiscal and monetary authorities, so as to ensure consistency with the overall macroeconomic policies.	According to its bylaws, SOFAZ is not permitted to invest domestically. Expenditures of SOFAZ constitute part of the consolidated state budget approved by the Parliament According to Budget System Law the consolidated state budget is being prepared in close consultation with all relevant government entities (Ministry of Finance, Ministry of Economy, etc.) and involvement of SOFAZ. For further information: https://www.oilfund.az/storage/images/cotiii74r3.pdf https://www.oilfund.az/storage/images/vvfbtvgrpz.pdf https://www.oilfund.az/storage/uploads/emcjtf8wiz.pdf

Narration of Principles / Sub-Principles	Responses
GAPP 4. PRINCIPLE There should be clear and publicly disclosed policies, rules, procedures, or arrangements in relation to the SWF's general approach to funding, withdrawal, and spending operations. **GAPP 4.1. Subprinciple.** The source of SWF funding should be publicly disclosed. **GAPP 4.2. Subprinciple** The general approach to withdrawals from the SWF and spending on behalf of the government should be publicly disclosed.	SOFAZ's Funding and Withdrawal rules are clearly defined by the "Statute of SOFAZ" and "Rules on the preparation and execution of the annual program of revenues and expenditures (budget) of the State Oil Fund of the Republic of Azerbaijan" (hereinafter "Rules on the budget of SOFAZ") which are publicly disclosed on the Fund's website. For further information: https://www.oilfund.az/storage/images/cotiii74r3.pdf https://www.oilfund.az/storage/images/vvfbtvgrpz.pdf https://www.oilfund az/storage/uploads/emcjtf8wiz.pdf
GAPP 5. PRINCIPLE The relevant statistical data pertaining to the SWF should be reported on a timely basis to the owner, or as otherwise required, for inclusion where appropriate in macroeconomic data sets.	SOFAZ submits monthly statistical reports to the President and Ministry of Finance, as well as quarterly and yearly reports to the State Statistical Committee. SOFAZ also reports on its revenues and expenditures to the Parliamentary Chamber of Accounts and on other relevant information to the Ministry of Taxes, State Social Protection Fund and other relevant government agencies. Additionally, SOFAZ regularly provides the relevant information on its activities to the World Bank and International Monetary Fund. All the relevant statistical data pertaining to the fund, is publicly disclosed on the Fund's website (audited annual reports, quarterly statements, etc.). For further information: https://www.oilfund.az/storage/images/cotiii74r3.pdf https://www.oilfund.az/storage/images/vvfbtvgrpz.pdf https://www.oilfund.az/storage/uploads/emcjtf8wiz.pdf https://oilfund.az/storage/uploads/emcjtf8wiz.pdf

Narration of Principles / Sub-Principles	Responses
B. Institutional Framework and Governance Structure	
GAPP 6. PRINCIPLE The governance framework for the SWF should be sound and establish a clear and effective division of roles and responsibilities in order to facilitate accountability and operational independence in the management of the SWF to pursue its objectives.	SOFAZ has a three-tier governance structure, with the President of the country being a supreme governing and reporting authority for the Fund. SOFAZ's activities are overseen by a Supervisory Board which is headed by the Prime Minister and consists of the Vice-Speaker of Parliament, Minister of Finance, Minister of Economy, Governor of the Central Bank and the Economic Advisor to the President. The operational management of SOFAZ is vested in the Executive Director. The relevant duties and responsibilities of the President of the country, Supervisory Board and Executive Director are clearly defined in the "Statute of SOFAZ". For further information: https://www.oilfund.az/storage/images/cotiii74r3.pdf
GAPP 7. PRINCIPLE The owner should set the objectives of the SWF, appoint the members of its governing body(ies) in accordance with clearly defined procedures, and exercise oversight over the SWF's operations.	The objectives of SOFAZ are clearly defined in "Statute of SOFAZ" approved by the President of the Republic of Azerbaijan. Please see also the response on GAPP 5 and 6. For further information: https://www.oilfund.az/storage/images/cotiii74r3.pdf
GAPP 8. PRINCIPLE The governing body(ies) should act in the best interests of the SWF, and have a clear mandate and adequate authority and competency to carry out its functions.	The Supervisory Board of the Fund, which is headed by the Prime Minister and consists of the Minister of Finance, Governor of the Central Bank, Minister of Economy, Vice-Speaker of Parliament and the Economic Advisor to the President, have a clear mandate and adequate authority and competency to fulfil its functions. All roles and responsibilities of the Supervisory Board are clearly defined in the relevant legislation. For further information: https://www.oilfund.az/storage/images/cotiii74r3.pdf https://oilfund.az/en/fund/management/supervisory

Narration of Principles / Sub-Principles	Responses
GAPP 9. PRINCIPLE The operational management of the SWF should implement the SWF's strategies in an independent manner and in accordance with clearly defined responsibilities.	"Statute of SOFAZ", "Rules on management of foreign currency assets of the State Oil Fund of the Republic of Azerbaijan" (hereinafter "Investment guidelines") and "Rules on the budget of SOFAZ" clearly define the role and responsibilities of the Executive Director. In accordance with these role and responsibilities Executive Director has independence in operational management. For further information: https://www.oilfund.az/storage/images/cotiii74r3.pdf https://www.oilfund.az/storage/images/daafr06kpe.pdf https://www.oilfund.az/storage/images/vvfbtvgrpz.pdf
GAPP 10. PRINCIPLE The accountability framework for the SWF's operations should be clearly defined in the relevant legislation, charter, other constitutive documents, or management agreement.	Accountability framework of SOFAZ is clearly defined in the "Statute of SOFAZ", "Investment guidelines", "Rules on the budget of SOFAZ" and Budget System Law all of which are available on the Fund's website. Fund produces and publicly discloses audited annual reports and quarterly reports. Information about Fund's activities is also disseminated through regular press conferences and published on the Fund's website. See also response on GAPP 5. For further information: https://www.oilfund.az/storage/images/cotiii74r3.pdf https://www.oilfund.az/storage/images/daafr06kpe.pdf https://www.oilfund.az/storage/images/vvfbtvgrpz.pdf https://www.oilfund.az/storage/uploads/emcjtf8wiz.pdf
GAPP 11. PRINCIPLE An annual report and accompanying financial statements on the SWF's operations and performance should be prepared in a timely fashion and in accordance with recognized international or national accounting standards in a consistent manner.	Since the start of its operations, SOFAZ has prepared annual reports and accompanying financial statements. All financial statements are prepared in accordance with International Financial Reporting Standards ("IFRS"). All annual reports and accompanying financial statements are published on the Fund's website. For further information: https://www.oilfund.az/storage/images/cotiii74r3.pdf https://www.oilfund.az/en/report-and-statistics/report-archive

Narration of Principles / Sub-Principles	Responses
GAPP 12. PRINCIPLE The SWF's operations and financial statements should be audited annually in accordance with recognized international or national auditing standards in a consistent manner.	Since the start of its operations SOFAZ has been audited by reputable international audit firms. In line with the Public Procurement Law, the Fund conducts open market tender processes to select its auditor. Price Waterhouse Coopers has been appointed to audit SOFAZ financial statements for years 2016-2018. All annual reports and accompanying financial statements are available on the Fund's website. SOFAZ also has Internal Audit department that prepares periodic internal audit reports. For further information: https://www.oilfund.az/storage/images/cotiii74r3.pdf https://www.oilfund.az/en/report-and-statistics/report-archive http://www.e-qanun.az/framework/1029
GAPP 13. PRINCIPLE Professional and ethical standards should be clearly defined and made known to the members of the SWF's governing body, management and staff.	Professional and ethical standards are clearly defined in the "Investment Guidelines". Management and staff of the Fund have to comply with ethical norms and rules of the International Financial Markets Association (ACI, Paris) and "Rules of Ethical Conduct for the Employees of SOFAZ". For further information: https://www.oilfund.az/storage/images/daafr06kpe.pdf https://oilfund.az/en/fund/management/behavior-rules

Narration of Principles / Sub-Principles	Responses
GAPP 14. PRINCIPLE Dealing with third parties for the purpose of the SWF's operational management should be based on economic and financial grounds, and follow clear rules and procedures.	Fund's activities related to third parties are based on economic and financial grounds. Fund's "Investment Guidelines" and "Investment Policy" regulate SOFAZ's dealing with third parties. All aspects of dealing with external managers are clearly defined in relevant documentation about Fund's activity. Appointment of external managers is carried out in compliance with the current legislation of Azerbaijan Republic on "State Procurement". External managers are selected on the basis of the criteria, such as credit rating of manager, assets under management, experience in the asset management industry, proposed rate of return and risk, proposed fees schedule etc. Compliance of the external managers' investments to their mandate is monitored daily. Performance of external managers' portfolios is monitored monthly. For further information: https://www.oilfund.az/storage/images/daafr06kpe.pdf https://www.oilfund.az/storage/images/6c92ernmvq.pdf
GAPP 15. PRINCIPLE SWF operations and activities in host countries should be conducted in compliance with all applicable regulatory and disclosure requirements of the countries in which they operate.	Fund conducts its operations and activities in host countries in compliance with all applicable regulatory and disclosure requirements of those host countries
GAPP 16. PRINCIPLE The governance framework and objectives, as well as the manner in which the SWF's management is operationally independent from the owner, should be publicly disclosed.	Fund's governance framework, objectives and its operational independence are clearly defined in the relevant legislation. For further information: https://www.oilfund.az/storage/images/cotiii74r3.pdf
GAPP 17. PRINCIPLE Relevant financial information regarding the SWF should be publicly disclosed to demonstrate its economic and financial orientation, so as to contribute to stability in international financial markets and enhance trust in recipient countries.	Audited financial statements are published in Fund's annual report, which is publicly available. Quarterly reports and all other relevant financial information about the Fund's activities are published on the Fund's website. Disclosed financial information includes AUM, asset allocation, benchmark, annual rates of return, etc For further information: https://www.oilfund.az/en/report-and-statistics/report-archive https://www.oilfund.az/en/investments/quarterly-investment-results

Narration of Principles / Sub-Principles	Responses
C. Investment and Risk Management Framework **GAPP 18. PRINCIPLE** The SWF's investment policy should be clear and consistent with its defined objectives, risk tolerance, and investment strategy, as set by the owner or the governing body(ies), and be based on sound portfolio management principles. **GAPP 18.1. Subprinciple** The investment policy should guide the SWF's financial risk exposures and the possible use of leverage. **GAPP 18.2. Subprinciple** The investment policy should address the extent to which internal and/or external investment managers are used, the range of their activities and authority, and the process by which they are selected and their performance monitored. **GAPP 18.3. Subprinciple** A description of the investment policy of the SWF should be publicly disclosed.	"Investment Guidelines" and "Investment Policy" set up SOFAZ's asset management framework and ensure the transparency in its investment decisions. Among the others, they define strategic asset allocation, currency composition, benchmarks, risk limits, minimum requirements for the Fund's external managers and limitations on the investment directions, as well as the credit quality limits for Fund's counterparties (custodian banks, correspondent banks, etc.). Derivatives (i.e. swaps, forwards, futures, etc.) may only be used for hedging or optimizing the currency composition and asset allocation of the Investment Portfolio. For policies and procedures related to the Fund's external managers please see our response on GAPP 14. Fund's "Investment guidelines" and "Investment Policy" are available on its website. For further information: https://www.oilfund.az/storage/images/daafr06kpe.pdf https://www.oilfund.az/storage/images/6c92ernmvq.pdf
GAPP 19. PRINCIPLE The SWF's investment decisions should aim to maximize risk-adjusted financial returns in a manner consistent with its investment policy, and based on economic and financial grounds. **GAPP 19.1. Subprinciple** If investment decisions are subject to other than economic and financial considerations, these should be clearly set out in the investment policy and be publicly disclosed. **GAPP 19.2. Subprinciple** The management of an SWF's assets should be consistent with what is generally accepted as sound asset management principles.	According to its "Investment Policy", Fund's investment decisions should aim at maximizing the risk adjusted returns. Fund's all investment decisions are made purely on an economic and financial basis according to the sound asset management principles. See also response on GAPP 18. For further information: https://www.oilfund.az/storage/images/6c92ernmvq.pdf

Narration of Principles / Sub-Principles	Responses
GAPP 20. PRINCIPLE The SWF should not seek or take advantage of privileged information or inappropriate influence by the broader government in competing with private entities.	According to its bylaws, SOFAZ is not permitted to invest domestically. In line with the "Investment guidelines", SOFAZ makes investment decisions independently of the government. Institutional and legal framework of SOFAZ has been designed in a way that the Fund cannot seek or take advantage of any privileged information. For further information: https://www.oilfund.az/storage/images/daafr06kpe.pdf https://www.oilfund.az/storage/images/cotiii74r3.pdf
GAPP 21. PRINCIPLE SWFs view shareholder ownership rights as a fundamental element of their equity investments' value. If an SWF chooses to exercise its ownership rights, it should do so in a manner that is consistent with its investment policy and protects the financial value of its investments. The SWF should publicly disclose its general approach to voting securities of listed entities, including the key factors guiding its exercise of ownership rights.	SOFAZ started to invest in equities in 2012 and has chosen not to exercise its ownership rights at this stage.
GAPP 22. PRINCIPLE The SWF should have a framework that identifies, assesses and manages the risks of its operations. **GAPP 22.1. Subprinciple** The risk management framework should include reliable information and timely reporting systems, which should enable the adequate monitoring and management of relevant risks within acceptable parameters and levels, control and incentive mechanisms, codes of conduct, business continuity planning, and an independent audit function.	Identification, assessment and management of the risks of the Fund's operations play crucial role in the Fund's overall management framework. SOFAZ's risk management system is supported with appropriate legal framework ("Investment Guidelines", "Investment Policy", etc), a specialized risk unit (Risk Management Department), internal and external audit functions and tools like RiskManager 4 by RiskMetrics and proprietary models. "Investment Guidelines" and "Investment Policy" set the main principles of risk management framework and clearly define limits on major factors for market, credit, concentration and liquidity risks. Certain pre-trade limits are set based on these factors. Furthermore, these risk factors are monitored on a daily basis via regular risk and performance reports. In addition to the factors set in the "Investment Guidelines" and "Investment Policy", a more in-depth analysis and monitoring of the market risk is performed on a regular basis through: interest rate sensitivity analysis (key rate durations, PV01, etc.), risk concentration analysis (duration by groups, VaR by groups, marginal VaR, etc.), tail events (conditional VaR, stress tests) and scenario analyses.

Narration of Principles / Sub-Principles	Responses
GAPP 22.2. Subprinciple The general approach to the SWF's risk management framework should be publicly disclosed.	Operational risk is managed in accordance with Fund's Operational Manual and business continuity planning. For further information: https://www.oilfund.az/storage/images/daafr06kpe.pdf https://www.oilfund.az/storage/images/6c92ernmvq.pdf
GAPP 23. PRINCIPLE The assets and investment performance (absolute and relative to benchmarks, if any) of the SWF should be measured and reported to the owner according to clearly defined principles or standards.	Comprehensive reports on assets of SOFAZ (including information on breakdown of investment portfolio by foreign currencies, asset class, credit ratings, maturities and geographic regions) are disseminated through the quarterly press releases. The performance of the Fund's investments is measured according to best industry standards and reported on an annual basis. Annual reports and quarterly statements are posted on the Fund's website. For further information: https://oilfund.az/en/report-and-statistics/report-archive
GAPP 24. PRINCIPLE A process of regular review of the implementation of the GAPP should be engaged in by or on behalf of the SWF.	This report was first published on SOFAZ's official website in April, 2011 and it is reviewed on an annual basis.