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The CESD Exclusive Assessment: Causes and Consequences of Rising Utility Prices in Azerbaijan

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The regular meeting of the Tariff (Price) Council of the Republic of Azerbaijan held on November 28, 2016 re-examined the sale prices of natural gas, electricity, heating oil, jet fuel. According to the appeal made by the State Oil Company to the Tariff (Price) Council, during recent years large-scale investments have been undertaken to ensure the sustainability of natural gas supply and the quality of service has been improved.

Additionally, it was stated that, following the agreements on production sharing, some part of natural gas sold in the country is purchased from the operating companies in USD. This results in a loss, since the cost exceeds the regulated prices in the country. In order to ensure sustainability and quality alongside decreasing financial burden, it was proposed by SOCAR to raise the natural gas tariff to 180 manat per 1000m³ for all consumers.

Based on the appeal made by the Azerenerji JSC and Azerishig JSC, in order to increase production capacity, to maintain power stations in normal condition, to meet the demand for electricity, to decrease the potential loss and to ensure the sustainability of power supply, an increase to the wholesale price of electricity per kWh by 1.6 copeck and to the retail price by 2.8 copeck to be applied.

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It was stated that, the new price regulation takes into consideration the social policy objectives, including social protection of low-income families and thereby, a differential tariff regulation will be applied.

That is to say, a retail price of natural gas for population is not to be changed i.e. 0.1 manat per m³, if the amount of annual consumption is up to 1500 m³ and an increased price of 0.2 manat per m³ will be applied to the amount exceeding 1500 m³. According to SOCAR, 62% of subscribers use less than 1500 m³ per year and in accordance with the differential price regulation, low-income families won't face higher tariffs. These new tariff regulations on natural gas consumption for population will be applied starting from January 1, 2017. Based on the decision of the Tariff Council, the price of natural gas for electric power companies will be 120 manat per 1000m³, and 200 manat for other companies starting from January, 2017

The regulations on the price of natural gas made it necessary to also reconsider electricity tariffs. Based on regulations, the wholesale price of electric power per kWh is to be 5.7 copeck, while retail price is not to be changed i.e. 0.7 manat per kWh, if the amount of monthly electric power consumption is up to 250 kWh and an increased price of 0.11 manat per kWh will be applied to the amount exceeding 250 kWh. Azerishig states that, 72% of subscribers use less than 250 kWh monthly, and thereby they are not expected to be affected new tariffs. These new tariff regulations on electric power consumption for population will be applied starting from January 1, 2017. Based on the decision of the Tariff Council, the price of electric power will be 9 copeck for companies starting from January, 2017.

Before discussing the impact of new price regulations, it should be stated that, international financial organizations have made some recommendations on the

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optimization of pricing. That is to say, in most cases, these organizations are reported to experience a loss. The main purpose of this step is to decrease the burden of state budget and increase the creditability of these organizations. On the other hand, if these organizations operated effectively, then the cost of these products could have been decreased without undertaking radical steps.

The application of differential approach and optimal pricing can be considered a positive step. However, the actual prices approved by the Tariff Council and the threshold amount is disputed. That is to say, in determining the threshold amount for increased price for subscribers both of natural gas and electricity, the family size has not been taken into consideration.

Based on the regulation of the Republic of Azerbaijan on the composition of consumer price basket and international practice, both electricity and natural gas are calculated in per capita terms. Thus, family size is one of the main factors affecting the amount of consumption. In other words, if calculated by per capita terms the share of population using less than threshold amount is not as high as 62% or 72%.

2-person household (250 kWh/125 m³) = 7-person household (250 kWh/125 m³)

Observations show that, in most cases, multi-person households are usually the households with low income due to various reasons and social difficulties. Hence, the social impact of new tariff implementation must be accurately specified and employed criteria must be reconsidered.

On the other hand, ceiling levels of natural gas and electricity utilization which are determined for subscribers and for which the price changes are applied are carried

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out disregarding urban and rural factors. Such that, the application of equal limits for urban and rural population groups may lead to unjust evaluation.

The third problem is the absence of differentiated criteria for households not provided with natural gas. Such that, the majority of new buildings in Absheron peninsula are not supplied with natural gas where the largest share of population resides. Moreover, there are still residence areas not supplied with natural gas. This will result in fact that, those families will only consume electricity and exceed the specified quota ((250 kilowatt-hour monthly); hence, those will pay 57% more for the electricity consumed in comparison with other families.

As seen, the protection of interests of various social groups must be considered during the implementation of optimal price and differential tariff policy.

The price increase for non-residential consumption groups will adversely affect the profit rates and the economic activity of business entities. Prices of several consumption goods and services will rise. Hence, even if families will not incur financial loss for tariff increase, those will suffer from the increase in consumption prices.

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