

How Much Does Azerbaijan Really Earn from Higher Oil Prices?

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Fiscal revenues of carbohydrogen rich Azerbaijan is severely dependent on sales of oil, oil products and natural gas. From this point of view the change of oil prices in the global markets is considered as the main indicator for estimating the financial condition of the government. It should be noted that the price of a barrel of oil is estimated to be 45 USD when calculating the state and oil fund budget of the current year¹. Under these circumstances the net profits of the State Oil Fund of Azerbaijan (SOFAZ) from the sale of carbohydrogens is estimated to be 9,724 billion manats², while tax revenues from the oil sector to the state budget is estimated to total 1,88 billion manats. As a result, the share of oil revenues in the state budget increased compared to last year and reached 55.1%³ (the same indicator was 47.9% in 2017⁴).

According to our observations, the current conjuncture in the global oil market is changing in the favor of Azerbaijan. The price of a barrel of BRENT crude oil is changing in the interval of 70-75 USD⁵. Overall the average price for a barrel of BRENT crude oil was 66.8 USD during January – March of 2018⁶ [Note: Starting from the III quarter of 2017 SOCAR has stopped publishing the monthly average price of Azeri light, which is the only source of information]. In the meantime oil extraction of the country increased by 2.4% and reached 9,7 million tonnes, while gas extraction increased by 5,2% and attained 7,3 billion cubic meters⁷.

According to the information by the State Customs Committee, 5,438 million tonnes or 2,686 billion USD worth of oil, 938,9 thousand cubic meters or 0,168 billion USD worth of

¹ Ministry of Finance, "İcmal və Dövlət Büdcələrinin layihəsi", page: 10
<http://www.maliyye.gov.az/sites/default/files/Budce-19.10.2017.pdf>

² SOFAZ, Dövlət Neft Fondunun 2018-ci il büdcəsi təsdiq edildi, 29.12.2017
http://www.oilfund.az/az_AZ/hesabatlar-ve-statistika/buedce-melumatlari/azerbaycan-respublikasi-doevlet-neft-fondunun-2017-ci-il-buedcesi-tesdiq-edildi-29-12-2017.asp

³ Ministry of Finance, "İcmal və Dövlət Büdcələrinin layihəsi", page: 12
<http://www.maliyye.gov.az/sites/default/files/Budce-19.10.2017.pdf>

⁴ Ministry of Finance, "Information (operative) on the execution of the state budget for 2017", 12.01.2018
<http://www.maliyye.gov.az/en/node/2119>

⁵ Bloomberg Market, Brent Crude oil, 26.04.2018
<https://www.bloomberg.com/quote/CO1:COM>

⁶ World Bank, "World Bank Commodities Price Data", 06.04.2018
<http://pubdocs.worldbank.org/en/664371522786567489/CMO-Pink-Sheet-April-2018.pdf>

⁷ SOCAR, 2018-ci ilin I rübü üzrə qazma, hasilat və ixrac göstəriciləri, 16.04.2016
<http://www.socar.az/socar/az/news-and-media/news-archives/news-archives>

natural gas was exported during the first three months of the current year⁸. Compared to last year the volume and value of the exported oil has been 11,7% and 35% higher, respectively.

The above-mentioned factors show its effect on the oil revenues of Azerbaijan. During the I quarter of 2018 SOFAZ had revenues of 3,533 billion manats from sales of profit of oil and gas⁹ or in other words, 45,3% higher than the estimates, the taxes from the oil sector to the state budget has been 0,467 billion manats¹⁰.

According to the ministry of energy of the Republic of Azerbaijan, daily average oil exports have been 625 thousand barrels¹¹. If we consider the volume of daily exports [*45 USD per barrel compared to 66,8 USD per barrel*], the sale of oil has brought additional revenue of 13,62 million USD per day on average. From this point of view the actual oil revenues of the country during the first quarter have been approximately 1,23 billion more than the estimated revenues.

Keeping in mind that one of the main issues that the public is concerned about is the current increase in oil prices, we consider the following calculations appropriate. Thus, from *Table 1* you can see the volume of additional revenues from the oil sector with different average prices, given that the oil extraction remained the same.

Table 1. Forecasted increases in oil revenues given that the daily oil extratcion has remained the same (with base oil price of 45 USD per barrel).

Average yearly sale price	50 USD/barrel	55 USD/barrel	60 USD/brarel	65 USD/barrel	70 USD/barrel	75 USD/barrel
Increase in oil revenues, billion USD	1,14	2,28	3,42	4,56	5,7	6,84

Source: Author's calculations, 2018

It should be noted that due to poor accountability of the enterprises and regulatory bodies operating in the sector, serious difficulties arise when calculating the change in net income of Azerbaijan as a result of oil price fluctuations. Despite this, we have tried to obtain approximate indicators by using different methods.

⁸ State Customs Committee, "XARİCİ TİCARƏT HAQQINDA", page: 12

http://customs.gov.az/modules/pdf/pdffolder/71/FILE_ODA0B3-E08572-5D8C2E-3EF68F-82C106-6D94DB.pdf

⁹ SOFAZ, Azərbaycan Respublikası Dövlət Neft Fondunun 2018-ci ilin yanvar-mart ayları üzrə gəlir və xərclərinə dair məlumat, accessed: 25.04.2015

http://www.oilfund.az/az_AZ/hesabat-arxivi/rublukh/2018_1/2018_1_1/

¹⁰ Minsitry of Finance, 2018-ci ilin birinci rübündə dövlət büdcəsinin icrasına (operativ) dair məlumat, 10.04.2018

<http://www.maliyye.gov.az/node/2153>

¹¹ Ministry of Energy of the Republic of Azerbaijan

<http://minenergy.gov.az/52/xeberler.html>

Method 1: According to the calculations of the Ministry of Finance of the Republic of Azerbaijan, a 5 dollar decrease in the price of crude oil can cost 62.5 million USD to state budget revenues and 794 million USD to the State Oil Fund¹². Looking from this perspective the dependence of SOFAZ and tax revenues of the state budget on the price of oil can be as follows [see Table 2].

Table 2: Expected increase in revenues of SOFAZ and tax revenues of state budget depending on oil prices, billion manat

Average yearly price of oil	50 USD/barrel	55 USD/barrel	60 USD/barrel	65 USD/barrel	70 USD/barrel	75 USD/barrel
Increase in the state budget revenues	0,0625	0,125	0,1875	0,250	0,3125	0,375
Increase in SOFAZ revenues	0,794	1,588	2,382	3,176	3,970	4,764
Total increase	0,856	1,713	2,569	3,425	4,282.5	5,139

Source: Author's calculations, 2018

As seen from the calculations with this method, revenues of SOFAZ and state budget revenues from the oil sector in the form of taxes can be 5,1 billion manat or 3 billion USD higher if the average yearly price of oil stands at 75 dollars.

Method2: According to the SOFAZ report, in the first quarter of 2018, SOFAZ has profits in the sum of AZN 3,533 bln through the selling of profit oil and gas¹³. Since the daily oil export volume is 625 thsnd barrels, the net income of the Fund is AZN 62,8 per/barrel¹⁴. By taking into account the Production Sharing Agreement terms (Azerbaijan's share in AIOC's share), Azerbaijan spent USD 17.7 [including transportation costs] per barrel of oil.¹⁵ Hence, we can calculate the cost in the following manner [see: Table 3].

Table 3: Estimated revenues of SOFAZ, in case of stable oil prices and extraction volume, bln manats

¹² Ministry of Finance, "İcmal və Dövlət Büdcələrinin layihəsi", səh: 47 <http://www.maliyye.gov.az/sites/default/files/Budce-19.10.2017.pdf>

¹³ SOFAZ. Azərbaycan Respublikası Dövlət Neft Fondunun 2018-ci ilin yanvar-mart ayları üzrə gəlir və xərclərinə dair məlumat, baxış tarixi: 25.04.2015 http://www.oilfund.az/az_AZ/hesabat-arxivi/rublukh/2018_1/2018_1_1/

¹⁴ The Exchange rate was bases on the avarege Exchange weight by the Central Bank of Azerbaijan (1 USD=1.7 manat).

¹⁵ Note: According to the public statements by SOCAR's vice-president, in 2016, the production cost of Azerbaijani oil was USD 20 per barrel. "Average production cost of Azerbaijani oil \$20 a barrel, Socar says", 26.01.2016 <http://www.intellinews.com/average-production-cost-of-azerbaijani-oil-20-a-barrel-socar-says-89313/>

Average oil price	50	55	60	65	70	75
	USD/barel	USD/barel	USD/barel	USD/barel	USD/barel	USD/barel
The increase in the SOFAZ profit	0,8553	1,7106	2,5658	3,4218	4,2771	5.132

Source: The Author's Calculation, 2018

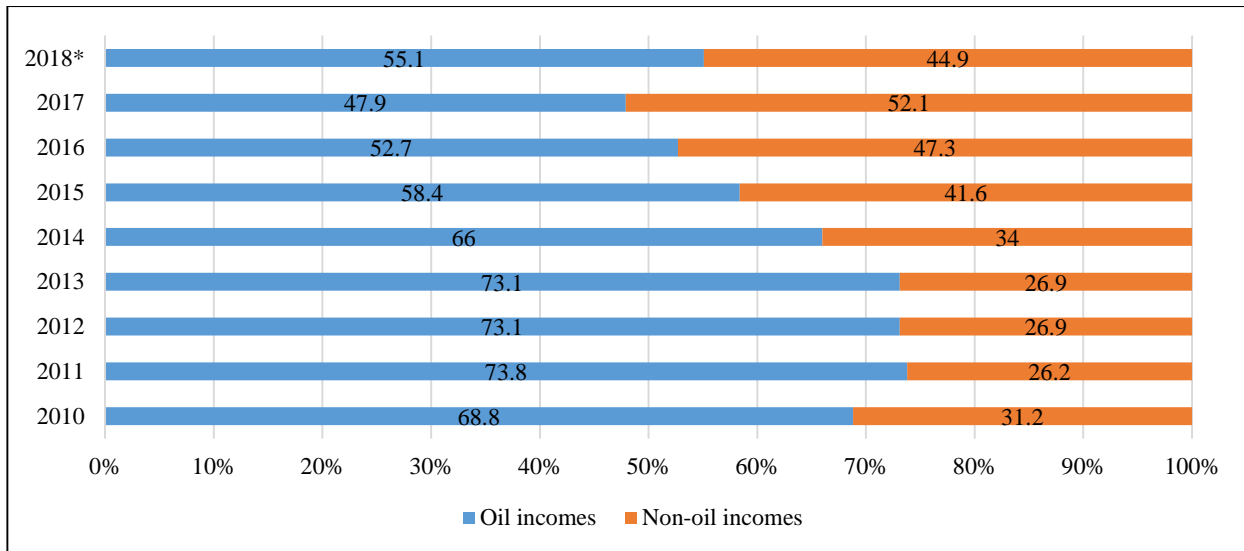
If the calculations are done using the second method, in case of a forecasted average oil price of \$ 75 per barrel, SOFAZ's revenues will gain an additional USD 5.1 billion or AZN 8.7 billion.

Although there are differences in the results of the calculations, both methods reveal that SOFAZ generates additional revenue at current energy prices in the world market. Increased oil income leads to the creation of surplus income, support of the national currency (manat), and the increase in strategic currency reserves, which positively affects major macro-economic indicators, but creates risks for the fiscal policy. Certain indicators point to an unstable future scenario. Following the economic decline in 2015, the government tried to implement fiscal consolidation, which ceased to exist; following the second quarter of 2017, there has been a trend of fiscal expansion. Following the rise in oil prices on the world market, the state budget¹⁶ and SOFAZ budget¹⁷ was changed, and expenditures increased. Additionally, oil transfers to the state budget in 2018 are going to be 51% more than in 2017: SOFAZ transfers to the state budget will increase by AZN 3.116 bln or \$ 1.83 billion. As a result, the share of the oil sector in the state budget increased again by 7.2%, which in total equals 55.1% of the state budget [see: Diagram 1].

Diagram 1: Share of the oil sector in revenues of the state budget, (%)

¹⁶ Azertag. "Azərbaycan Respublikasının 2017-ci il dövlət büdcəsi haqqında" Azərbaycan Respublikasının Qanununda dəyişikliklər edilməsi barədə Azərbaycan Respublikasının Qanunu, 30.06.2017 https://azertag.az/store/files/news/QANUN_2017-CI%20IL_%20DOVLAT_%20BUDCASI_%20HAQQINDA.pdf

¹⁷ Prezident.az, "Azərbaycan Respublikası Dövlət Neft Fondunun 2017-ci il büdcəsi haqqında" Azərbaycan Respublikası Prezidentinin 2017-ci il 10 yanvar tarixli 1186 nömrəli Fərmanında dəyişikliklər edilməsi barədə Azərbaycan Respublikası Prezidentinin Fərmanı, 04.10.2017 <https://www.president.az/articles/25422>



Source: Ministry of Finances of the Republic of Azerbaijan, 2018

The Strategic Road Maps presented a requirement for establishing a so-called “golden-rule” in 2017. Despite this requirement, this goal failed¹⁸.

Nevertheless, we think that, the increased inflow of oil money to the economy should not be an obstacle for sterilisation and fiscal consolidation policy. In case of failure to acknowledge these points, the steps taken for the sustainable development of the country’s economy are not going to have effective results and will be open to external threat.

¹⁸ Azertag. “Azərbaycan Respublikasının milli iqtisadiyyat perspektivi üzrə Strateji Yol Xəritəsi”, 06.12.2016, səh: 105

https://azertag.az/store/files/untitled%20folder/_STRATEJI%20YOL%20XERITESI_.pdf

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