Book

2020 state budget of Azerbaijan : brief independent review

Provided in Cooperation with:
Center for Economic & Social Development (CESD), Baku

Reference: (2019). 2020 state budget of Azerbaijan : brief independent review. Baku, Azerbaijan : Center for Economic and Social Development (CESD).

Better research, better policy, better reform

CESD | CENTER FOR ECONOMIC & SOCIAL DEVELOPMENT

Global Think-Tank

2020 State Budget of Azerbaijan: Brief Independent Review

CESD Fiscal Research Team

CESD Press

Caspian Plaza, 3rd Block, 13th floor
J.Jabbarli str. 44,
Baku, Azerbaijan
Phone: (99412) 5943665
Fax: (99412) 5943665
Email: info@cesd.az
URL: www.cesd.az

Baku, September 16, 2019

2020 State Budget of Azerbaijan: Brief Independent Review

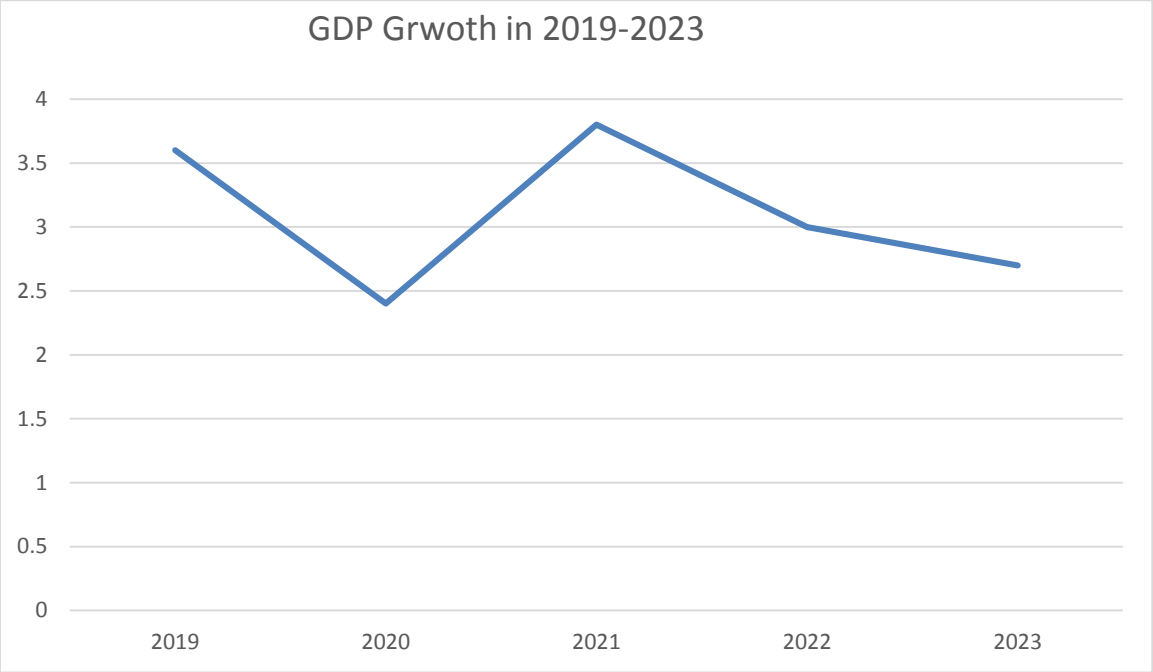
The Ministry of Finance of the Republic of Azerbaijan presented the draft of the 2020 State Budget. According to the document, the growth rate of the Gross Domestic Product (GDP) in Azerbaijan is expected to decline by 2020. Thus, if GDP is projected to grow by 3.2% in 2019, then it is projected to grow by 2.4% in the following year. GDP is forecasted at 82.7 billion manat in 2020 (US $48.64 billion at the current rate). The Ministry of Finance predicts a 3.3% rise in non-oil GDP, which means it will generate 54.2 billion manat (US $31.88 billion at the current rate) in the non-oil sector next year.

According to the government's forecast, the inflation rate will reach 4.6% by 2020. It is worth mentioning that in 2019 the Central Bank predicted 3.7%. According to CESD forecast, real inflation in 2019 will be 8.2%. One of the most discussed topics is whether the inflation rate declared by the State Statistical Committee reflects reality.

The draft State Budget takes the expected cost per barrel in 2020 as US $55. Despite the fact that it is US $5 less than the previous year's price, it doesn't fully ensure related risks. Thus, CESD suggests to take US $50 per barrel for the state budget next year. Aside from minimizing risks, it would also be important in terms of expanding accessibility.

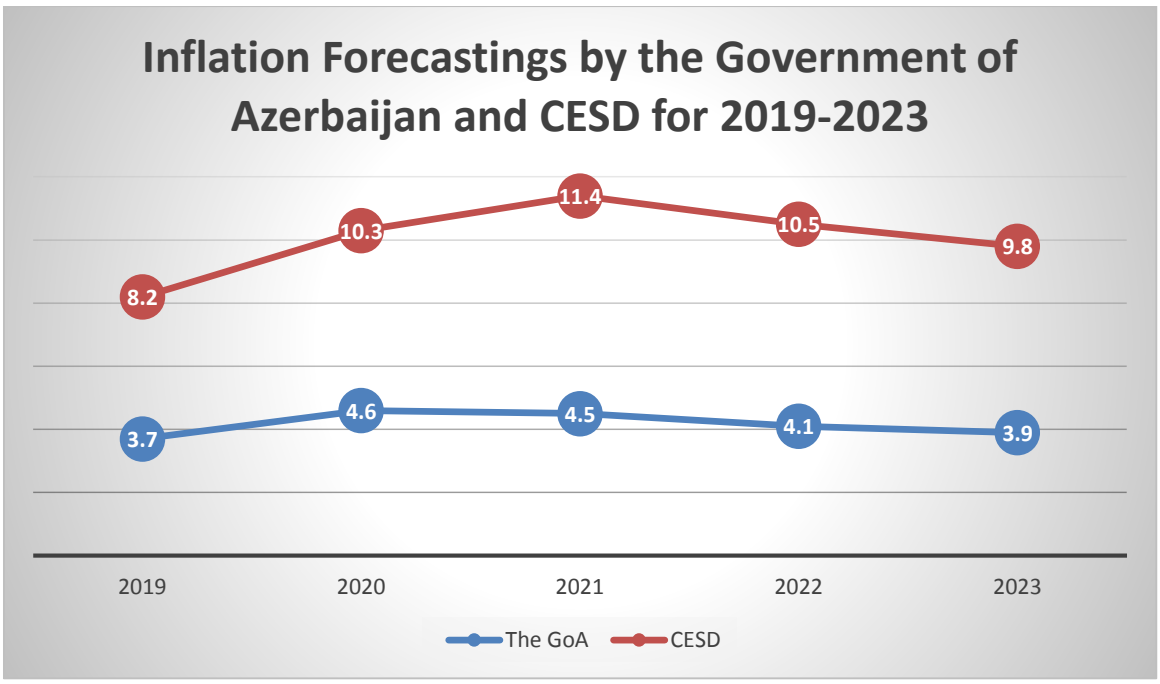
The 2020 Consolidated Budget is expected to be 28.19 billion manat (US $16.58 at the current exchange rate), while revenues are projected as 27.60 billion manat (US $16.23 at the current exchange rate). The Consolidated Budget deficit is projected at 586 million manat (US $344.70 at the current exchange rate). The State Budget expenditures are expected to be 25.62 billion manat (US $15.07 billion at the current exchange rate), which means an increase of 427.7 million manat (US $251.58 million at the current exchange rate) by 2020. Despite the strategy of

budget expenditures' optimization, the Ministry of Finance continues to keep its pace of spending, which means that oil-based growth in budget spending will be maintained.



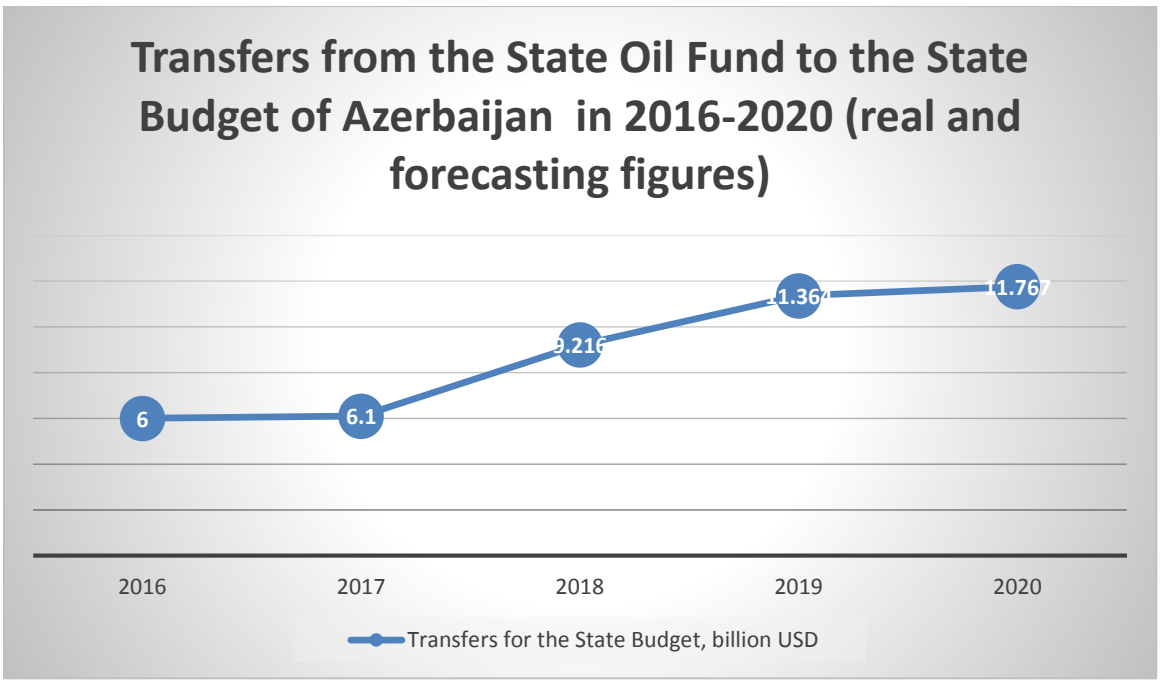
Source: The Ministry of Finance of Azerbaijan Republic, 2019

As it becomes clear, Azerbaijan's GDP growth rate will be reduced per next year in comparison with 2019. The decline will be related to the projected downturn in oil production and the current volatility in world oil prices. Thus, although the non-oil sector has a significant share in GDP, oil prices remain crucial for macroeconomic indicators.



Source: The Ministry of Finance of Azerbaijan Republic and CESD calculations, 2019

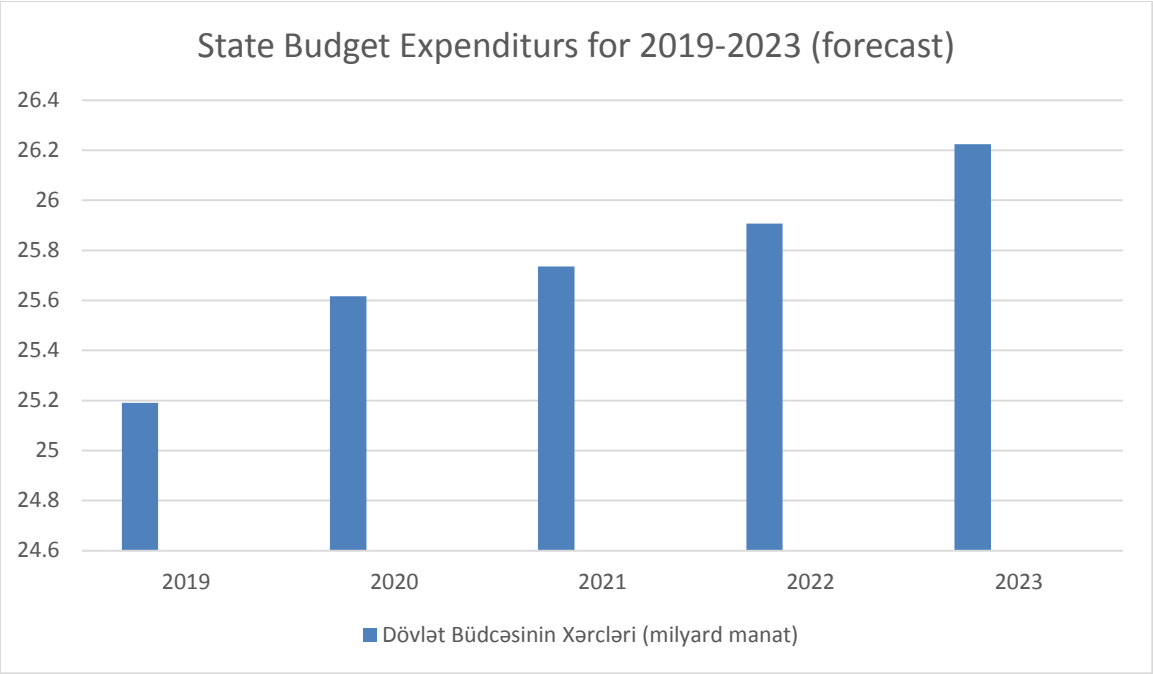
As it may be observed, amid rising budget spending, there will be some changes in the inflation rate as well. Although the government of Azerbaijan predicts higher inflation next year, the official inflation rate is still a single digit. At the same time, according to CESD inflation forecasts, Azerbaijan expects double digit inflation in 2020-2022. Amid growing budget spending and expanding the social package, the demand for more resources to the consumer market will increase as well. At the same time, import dependence will continue to protect the import inflation effects in the coming years.



Source: The State Oil Fund of Azerbaijan, 2019

Budget revenues are projected at 25 billion 484 million manat for the next year. Thus, 57% of revenues will be addressed to the oil sector. 11 billion 767 million manat will be transferred to the State Budget from the State Oil Fund. It should be noted that this year the State Oil Fund should pay 11 billion 363 million manat to the State Budget. In fact, the Ministry of Finance should focus on reducing the Fund's transfers, not on increasing them, because the budget's dependence on oil and, in particular, on the oil market, remains a main priority. The non-oil sector's share in budget revenues will grow by 11.3% compared to 2019. Although this developed may be seen as a positive trend, the government should still strive to generate at least half of its budget revenues through the non-oil sector.

As it may be observed, even after the oil shock there has been an increase in transfers from the State Oil Fund to the State Budget. This doesn't allow the budget to cope with the oil surplus. As a result an increased dependence on the Oil Fund will be observed. It is projected that SOFAZ will become a decisive source in the formation of budget revenues in the coming years.



Source: The Ministry of Finance of Azerbaijan Republic, 2019

The Ministry of Finance forecasts that the growth in budget spending will continue in the following years. However, it is not considered desirable from the budget spending optimization point of view. As it becomes clear, the burden of budget revenues falls on the oil sector, thus, this means that the oil market will have a leading influence on the cost of the expenses.

According to the data provided by the Ministry of Finance, the highest point of the consolidated budget's expenditures will be determined in accordance with budgetary rules. Hence, according to the law of the Republic of Azerbaijan on the budgetary system dated August 24, 2018, new budget rules for medium- and long-term management of budget expenditures will be introduced starting from the 2019 budget year. According to the budget regulations, the consolidated budget expenditure is based on the forecast of non-oil and other receipts of in oil revenues, although the limit of consolidated budget expenditures should not be more that 103% of the approved budget expenditures for the current year. As in 2019, the highest point of consolidated budget expenditures in 2020 and in the medium-term will be determined with regard to the given law.

As it becomes clear, the fiscal rules proposed by the Ministry of Finance will be approved from the next year. This means that the fiscal rules were not implemented during the preparation of the 2020 state budget.

Conclusion

The Ministry of Finance presented a summary of next year's State Budget draft to the public. An analysis of the draft Azerbaijan State Budget for 2020 shows that the budget will still be dependent on oil next year. 57% of budget revenues will be gained by the oil sector, which will be driven mainly by transfers from the Oil Fund. According to the document, the estimated price per barrel in the national budget is US $55. Although it was US $5 less in comparison with 2019, it was advisable to lower the price considering the volatility in the oil market. The Center for Economic and Social Development (CESD) suggested US $50 per barrel. On the other hand, the increase in budget spending by 2020 will increase pressure on the consumer market, which is reflected in both official and independent inflation forecasts. Thus, according to official and independent inflation forecasts, more price increases are expected. The draft budget illustrates that fiscal rules are not yet implemented in Azerbaijan and that budget allocations will increase over the following years. The Ministry of Finance forecasts that the rate of manat against the dollar will not change next year. However, in spite of positive tendencies, how the manat's exchange rate will change in 2020 will largely depend on world market prices for oil and the exchange rate of national currencies of our non-oil trading partners.

References

Azərbaycan Respublikasının 2020-ci ilin dövlət və icmal büdcələrinin ilkin göstəricilərinə dair açıqlama (http://finance.gov.az/news/5377/azerbaycan-respublikasinin-2020-ci-ilin-dovlet-ve-icmal-budcelerinin-ilkin-gostericilerine-dair-aciqlama-)

State Oil Fund of Azerbaijan's repots, https://oilfund.az/en/report-and-statistics/recent-figures

Foreign debt of Azerbaijan in 2018: realities and perspectives, http://cesd.az/new/wp-content/uploads/2018/02/Azerbaijan_Foreign_Debt_2018.pdf

Foreign debt in Azerbaijan in 2016: realities and perspectives, http://cesd.az/new/wp-content/uploads/2017/02/Azerbaijan_Foreign_Debt_January_2017.pdf

The 2018 State Budget Project of Azerbaijan: From Consolidation to High Spending?, http://cesd.az/new/wp-content/uploads/2017/11/CESD-Research-2018-Budget-Projections.pdf

Changes to the Oil Fund's Budget: the impact of increased revenues on government spending, http://cesd.az/new/wp-content/uploads/2017/10/CESD-Article_SOFAZ_Budget-Eng.pdf

The CESD Assessment on the 2017 State Budget Project, http://cesd.az/new/wp-content/uploads/2016/11/CESD-Assessment_Azerbaijani_State-Budget-2017.pdf

Azerbaijani Oil Fund: Fiscal Consolidation, Volatility and Oil Wealth, http://cesd.az/new/wp-content/uploads/2017/05/CESD_Paper_SOFAZ_Budget.pdf

Azerbaijani State Budget in 2016: Perspectives and Challenges, http://cesd.az/new/wp-content/uploads/2015/09/CESD_Paper_Budget_Azerbaijan_2016.pdf

The Azerbaijani economy in the first half of 2018: Brief Overview, http://cesd.az/new/wp-content/uploads/2018/07/Azerbaijan_Economy_in_the_first_half_2018

The Economy of Azerbaijan in 2017 -Brief Overview, http://cesd.az/new/wp-content/uploads/2018/01/CESD_Research_Paper_Azerbaijan_Economy_2017.pdf

Macroeconomic Forecasts for Azerbaijan in 2017: Independent View, http://cesd.az/new/wp-content/uploads/2017/01/2017-forecast-for-the-economy_Azerbaijan.pdf

The Azerbaijani economy in the first half of 2019: Brief Overview, http://cesd.az/new/wp-content/uploads/2019/08/Azerbaijan_Economy_the_first_half_2019.pdf