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Effective Ways to Inject Oil Revenues into the Economy in Oil Countries

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ABSTRACT

The main objective of the study is to explore how to achieve economic growth and the role of oil in the oil countries' economy. The practical necessity of the article is to learn how to effectively integrate oil revenues into the country's economy. At the same time, it is justified by the evidence that non-oil sector development and ultimately sustainable economic development can be achieved by injecting oil revenues into the economy efficiently and reasonably. Besides, at result of the study found that oil-rich countries for reaching long-term economic growth and sustainable economic development should be able to develop the non-oil sector and obtain economic diversification. Research work has been carried out on the basis of systematic analysis and methods. Scientific novelty of the research-modern features of oil revenues management and ways of its effective use were identified and in the result of research proposals were made.

Keywords: Diversification of the Economy, Non-oil Sector Development, Oil Revenues

JEL Classifications: E31, Q41, O11

1. INTRODUCTION

Modern oil market is featured in developing dynamics and it is related to the increase of consumption and world production. During 2005-2015, oil consumption and production increased 12.1% and 11.9% respectively. Besides, there are instability oil prices in the world oil market. This case was observed seriously in 2008 and 2014-2016 (Francois and Velerie, 2008).

The system of income tax and borrowing is considered the main instruments in the world. But in oil-rich countries, oil revenues at various stages of economic development, especially in transition economies are the basis of budget revenues. However, the persistence of this trend is considered risky to the country's economy. From this point of view, social and economic development must be achieved through oil revenues in the long term, economic diversification should be carried

out and budget revenues should be largely funded by taxes via the development of the non-oil sector. These tools have an impact on the economy at both the macro and micro levels. For this reason, decisions related on them should be taken into account for avoiding a negative impact on the country's economy (Vugar, 2011).

Implementation of these measures will reduce the dependence of the state budget revenues on the dynamics of oil prices on the world market and in the long run fiscal stability will be ensured.

The experience of advanced oil countries shows that state budget burden should be gradually transferred to the non-oil sector by injecting oil revenues into the economy in accordance market conditions. This process will ensure fair distribution of oil revenues between the generations (Francois and Velerie, 2008, Hamilton, 2010).

2. THE CURRENT SITUATION

National economies of oil-rich countries depend mainly on crude oil exports. Some of this revenue is saved in sovereign wealth funds (for future generations and to preserve macroeconomic stability during recessions associated with negative oil price shocks) and the remaining revenue is transferred to the state budget to stimulate economic diversification and growth (Ghalayini, 2011, Jimenez and Sanchez 2005).

However, possibly due to structural sluggishness caused by misallocation and inefficient use of resources, and non-tradable sector and the booming oil industry, production (or tradable) sector shrinks and a low level of economic diversification is followed. This in turn also hinders diversification and makes the economy vulnerable to oil price shocks.

At the same time, it is estimated that oil demand will not decrease over the next 20 years. This can be seen in the following research:

The rapid development and spread of information and communication technologies during the first 10-20 years of the 21st century, and regarding the processes of globalization have a significant impact on the socio-economic life of the countries. In this sense, oil countries (including Azerbaijan) are no exception. Global, planetary factors influence almost all areas of the country's life - economic, social, political, humanitarian and cultural fields (Humbatova et al., 2019). However, as in each country, oil countries also have regional (region-specific) or inter-country factors depending on their origin and influence, so that they can be considered in the management of different areas of public life in terms of effective policy formulation. In this regard, oil economies need to make economic reforms, these economies must realize that oil revenues are depleted, and have to ensure sustainable economic development by effectively injecting oil revenues into the economy (Table 1).

At the same time, we can say that efficient use of oil revenues should increase the production of competitive products with high export share. It is necessary to create a network of social, production and market infrastructure, to use modern forms of management and management, which will lead to the expansion of the non-oil sector and respond to modern challenges. The development of the non-oil industry can be achieved through the efficient use of economic and natural resources and the involvement of these resources in economic turnover (Alonso, 2006).

It was discovered that most of the state budget revenues (about 70%) are formed in the oil sector, which is risky in terms of oil prices in the world market. To do so, the efficient management

of oil revenues to the economy should be a key component of a cost-effective budget policy. The main issue for oil countries is that they should not remain behind the developed countries of the world and to produce competitive products by effectively injecting oil revenues into the economy. The main challenge of the modern era is the development of human capital. This can be seen in the Norwegian experience, which has rich natural resources (Mukhtarov et al., 2019, Alonso, 2006).

In general, the Norwegian model is the most successful model of oil revenues management. The country has developed oil industry - oil extraction, petrochemicals, petrochemical industry, on the one hand, significant investments in human capital. Today Norwegian prosperity has been thanks to the educated people. Almost human capital is the most important factor behind Norway's economic growth (Norwegian Petroleum Directorate).

Norway currently has a high standard of living. Infrastructure is fully built in any area. How did Norway succeed? For this, a democratic society was established, an economic model based on science, knowledge and the welfare of the population was created.

Under these conditions, the main challenge facing oil countries is to avoid retardation as compared to the pace of development in the world. This firstly requires eliminating the existing dependence on the hydrocarbon resources export in the economy and constantly focus on such an important issue as preventing the global economy from turning into a raw supplement and a technological outsider. While oil exports have been a major driver of economic growth over the past decade, the main challenge at this stage is to accelerate the development of the non-oil sector, at the same time to increase the efficiency and competitiveness of the economy and to provide its innovative development. In other words, the transition from the traditional economy to the "knowledge economy" should be laid, and the development of human capital which is crucial to this, must be put to the forefront. This is in addition to making appropriate requirements for the formation of an economic model, but also leads to a radical change in the education system - the importance of such components as additional education and lifelong education, it also envisages increasing the role of virtual learning and computer-networking knowledge. At the same time, the importance of intellectual property will also increase which its core mission is to support creativity, stimulate innovation and market regulation.

3. EFFECTIVE WAYS OF USING FROM OIL REVENUES

The above facts shows the current state and current prospects in oil countries. It can be concluded that oil revenues have already

Table 1: Long-term oil demand (from 2017 to 2040) (mb/d)

Name of organizations and regions	2017	2020	2025	2030	2035	2040	Growth 2017-2040
OECD	47.3	48.3	46.8	44.2	41.5	38.7	-8.7
Developing countries and OPEC	44.4	47.8	53.1	58.1	62.6	66.6	22.2
Eurasia	5.4	5.8	6.1	6.3	6.4	6.4	1.0
World (total)	97.2	101.9	106.0	108.6	110.5	111.7	14.5

OPEC: Organization of the Petroleum Exporting Countries, OECD: Organisation for Economic Co-operation and Development. https://www.opec.org/opec_web/en/publications/340.htm

begun to enter the economy in such a way that the challenges of managing it gradually become apparent. It can be evaluated as follows:

- Spending most of the oil revenues (mainly for consumption purposes) puts the economy of oil countries now and in the future in a critical situation;
- Now spending large portions of oil revenues distracts from the importance of economic reforms, leading to a certainty in fiscal, tax and exchange rate policies. This undermines oil countries' intention to build a competitive economy in the world;
- To spend most of the oil revenues now, would not be fair in terms of intergenerational justice - only will be left with a ruined environment and an unnecessary, rusty infrastructure to the future generations (the current state of the oil industry is an example of this).
- Negative effects of The Harrod-Blassa-Samuelson can seriously damage non-oil industries in the medium and long term (due to the rapid increase in the overall price level and prices of production factors).
- Efforts should be made to create new businesses that meet modern requirements and create value chains in the manufacturing sector.
- Specialized and general-purpose industrial campuses should be established, and industrial enterprises should be encouraged to use innovative technologies.

At the same time, it should be noted that currently, the Republic of Azerbaijan has done a great deal in connection with the above measures. Thus, the World Bank's Doing Business 2019 report published on October 31, 2018, included Azerbaijan in the list of the 10 most reformed countries in the world and was declared the most reforming country in the world. Azerbaijan's position ranks 25th out of 190 countries by 32 steps compared to 2017 (Doing Business, 2019).

However, the economic environment and infrastructure should be developed by the government, and direct participation in business projects using state oil money should not be allowed.

Economic policy should be built in such a way that oil revenues should be perceived as never before. Only in this case, oil revenues could contribute to the overall economic development (Odhiambo and Nyasha, 2019).

Oil revenues would be better if the government spent mainly on three purposes:

1. For the development of human capital
2. For large infrastructure projects
3. For ensuring of favorable microfinance environment in the country.

Let us explain in detail the following scheme:

It is necessary to accelerate the establishment of an industrial campus to develop specific areas, in particular, it is necessary to accelerate the work on establishment of the Free Economic Zones. The United Arab Emirates is an example for this process.

Although this country is oil-rich, but it has achieved sustainable economic growth by diversifying its economy and establishing Free Economic Zones. Taking advantage of this experience, the establishment of Free Economic Zones in the territory of the Republic of Azerbaijan will expand the economic relations of the country and at the same time strengthen the political and economic position of Azerbaijan in the region (Graph 1).

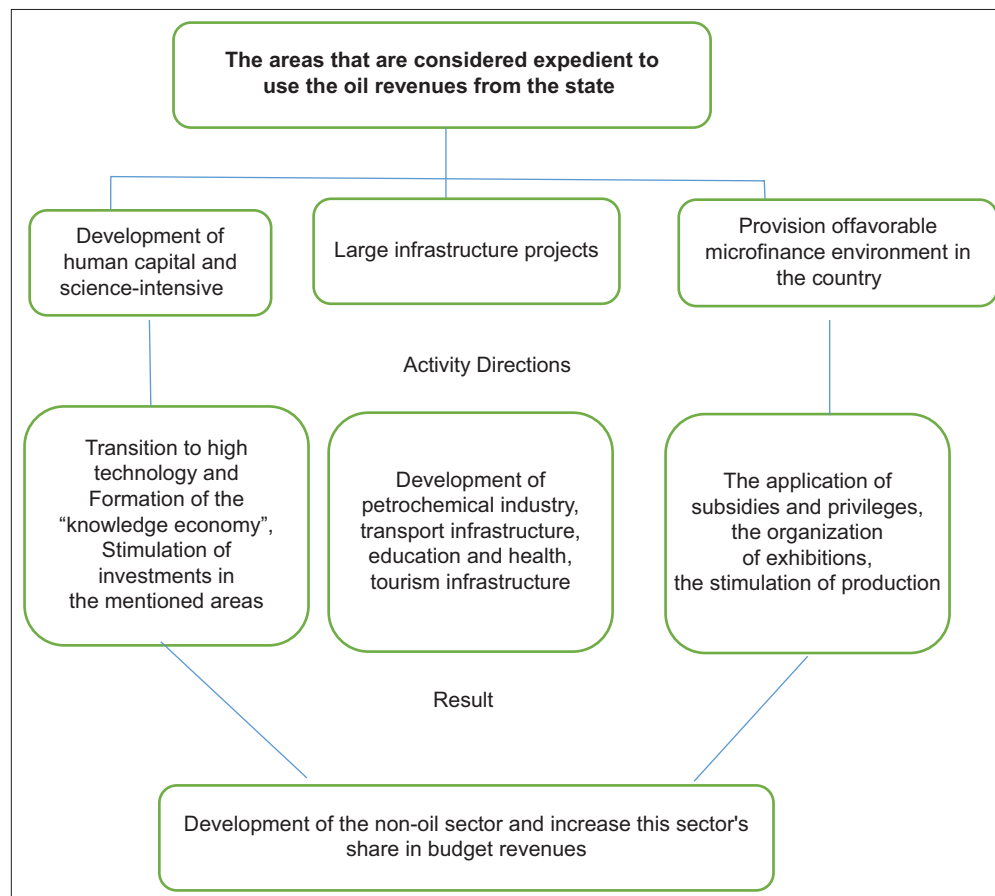
Oil countries that have the potential to develop the agrarian sector which is one of the key sectors of the non-oil sector, will need to create new industrial centers for the processing of agricultural products to develop and improve its sectoral structure.

Many oil countries have all the opportunities for large-scale development of medical and leisure and tourism facilities. This includes both natural and geographical conditions and economic factors. Azerbaijan is one of these countries (Daniel, 2002).

The economic benefits can be achieved by directing oil revenues in this area after all these factors are considered.

In addition to those mentioned, regarding given the level of economic development of oil countries, the situation in the social sphere, and the current level of economic, political and social institutions, it would be advisable to use oil revenues in the following areas:

1. For the development of the petrochemical industry: preparing highly qualified management and technical management personnel, modernization of scientific and technical base of petrochemical industry, technological modernization of the petrochemical industry of the oil countries, modernization of the oil machine-building industry and increasing its export capacity;
2. Education: training of highly qualified specialists in the leading educational institutions of the world in the areas of the future economic development of oil countries (including Azerbaijan), training of engineers and technicians in accordance with modern requirements of educational institutions in oil countries, creation of specialized vocational education institutions that train highly qualified specialists for various industries, repair of educational institutions and strengthening of material and technical base, creation of educational credit system;
3. Health: From the health care system to struggle the disease, transition to health care system aimed at prevention of diseases;
4. The development of future technologies in oil countries and close integration of oil countries into the global business services market;
5. Development of oil Electronic industry, development of biotechnology industry, Establishment of Information and Communication Technology Production Centers, preparing of the necessary specialists, creation of appropriate infrastructure;
6. For the development of transport infrastructure: infrastructure projects that strengthen the role of oil countries in regional oil and gas transit, besides, the creation of infrastructure that could turn these countries into regional centers for goods, services and transportation, creation and development of the business services sector (Humbatova et al., 2019).

Graph 1: The main directions in which oil revenues should be directed through the state budget

At the same time, there are great opportunities for the creation and development of logistics facilities in the economic sectors.

Other significant effects of the transfer of a portion of oil revenues to the economy through the budget channel have manifested itself as “Dutch disease” symptoms. Real appreciation of the national currency and rising labor costs negatively affected the competitiveness of the non-oil economy, and the rapid growth of the above-mentioned sectors contributed to the financial and partial labor outflow to the non-commercial sectors.

4. CONCLUSION

The above measures can be summarized as follows:

- Adoption of state programs on education of young people from oil-rich countries in developed countries and their financing by the Oil Funds;
- Achieving sustainable economic growth, primarily through the expansion of the non-oil sector, including the non-oil industry;
- Taking into account the dynamics of growth of revenues from the placement and management of foreign currency assets in the structure of the Oil Fund’s revenues in recent years and expansion of activities in this area;
- Development of non-oil sector of economy, regions, small and medium business;
- Large-scale development of infrastructure fields (Anis, 2019);

- Ensuring the application of innovative production methods in the non-oil sector and achieving fundamental structural changes in the economy (Khayati, 2019);
- Implementation of poverty reduction measures and solution of other social problems;
- Stimulating the intellectual and technological base of the economy;
- Development of “human capital” (preparing of highly qualified personnel, professional development of personnel);
- Creation of new production areas and introduction of new technologies in the industrial sector (Graph 1).

It is assumed that the results obtained in the research process will be successful for oil countries.

The study has also explored the experience of countries such as Norway, which have efficiently used oil revenues and currently have more than \$200 trillion in oil revenues, including those that have achieved economic growth through economic diversification. In the end, it should be noted that Venezuela is probably the largest oil field in the world. However, the lack of democracy in the country and the lack of proper economic system have caused poor living conditions and hyperinflation. Therefore, oil countries should aim to effectively inject oil revenues into the economy and develop the non-oil sector and ensure sustainable economic growth, independent of oil revenues (Norwegian Petroleum Directorate, Odhiambo and Nyasha, 2019).

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