

Analysis of main problems facing Azerbaijan's non-oil exports

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While the history of Azerbaijan's gaining extensive resource revenues is relatively short (less than 10 years), this timeframe was sufficient for the economy to face 'resource curse': the share of the resource economy in the budget jumped to 70%, and its specific weight to 90%. The economic share of Baku agglomeration, where more than 98% of the natural resources are concentrated, exceeded 80%.

However, the sharp drop in oil prices in the world markets since the end of 2014, that caused a 3-4 time loss of Azerbaijan's revenues in 2015-2016, compared to the previous five years, could be a historic chance to take lessons from the crisis. There well may be some truth in the proverb, saying 'Better to see something once than to hear about it a thousand times.' Over the past 50 years, countless academic investigations on 'resource curse' have been carried out in the world, with live examples shared about its consequences. However, no governments were reluctant to see the fact that they were on the wrong track until this threat is just around the corner. From this point of view, what is really significant for Azerbaijan is the diversification of its exports and an increase in non-resource currency revenues. In 2015, the devaluation of Azerbaijan manat by more than 2 times in a short period showed that the long-term sustainable development in the economy, as well as macroeconomic stability would not be possible unless the national currency is moved away from dependence on natural resource revenues. What changes have been made in Azerbaijan's export potential for the last 3 years after the crisis? What are the main trends observed in the volume and structure of non-resource products?

This analysis tries to uncover answers to these questions.

Problem: Limited product coverage

Looking at foreign trade statistics, the quantity of export products is very noticeable at first glance. In 2017, Azerbaijan exported 1180 items of products worth \$ 13.812 billion (the calculation included only products with a value of more than \$ 1,000). Moreover, 96.5% of total exports, or \$13.334 billion, fell to the share of 30.5 items, of which 5 are related to oil sector, and 25 to, non-oil sector. In other words, the 2.6% product included in the export basket provides almost 97% of all exports. Namely, 2.6% of the export products cover 97% of the total exports.

Azerbaijan's main export products

Description	Code	Export value, ths USD
Potatoes, fresh or chilled	070190	25822
Tomatoes, fresh or chilled	070200	151595
Turnip-like onions	070310	15672
Cucumbers and gherkins, fresh or chilled	070700	10716
Shelled hazelnuts	080222	114532
Apples, fresh	080810	30873
Cherries and wild cherries, fresh, other	080929	23155
Persimmons, fresh	081070	90981
Cane or beet sugar and chemically pure sucrose	170199	39443
Spirits obtained by distilling grape wine or grape marc (cognac, grappa, brandy, other)	220820	14058

Copper ores and concentrates	260300	19494
Oils and other products of the distillation of high temperature coal tar	270799	34596
Crude oil	270900	10706818
Jet fuels	271051	82187
Heavy distillates or gas oil for other distillate range products	271061	241872
Natural gas in gaseous state	271121	1193712.4
Petroleum coke, not dehydrated	271311	15468.47
Electrical energy	271600	50569
Methanol (methyl alcohol)	290511	42779
Polyethylene – specific gravity <0.94 in primary form	390110	75353
Other substances in primary form obtained by polymerization	391190	21596
One thread cotton yarn	520512	32548
Gold (not used for coin-minting and other raw forms); Gold (used for coin-minting)	710812,710820	139015.7
Semi-finished products of iron or non-alloy steel containing, by weight, $\geq 0,25\%$ of carbon	720720	22733
Tubes and pipes, having circular cross-sections and an external diameter of $> 406,4$ mm, of flat-rolled products of iron or steel	730539	9543
Refined copper cathodes and sections of cathodes	740311	12003
Aluminium, not alloyed, unwrought	760110	22666
Unwrought aluminum alloys	760120	28563

Plates, sheets and strip, of non-doped aluminum, of a thickness of > 0,2 mm	760611	22616
Plates, sheets and strip, of aluminum alloys, of a thickness of > 0,2 mm	760612	42889
Total value of export products	13334000.0	

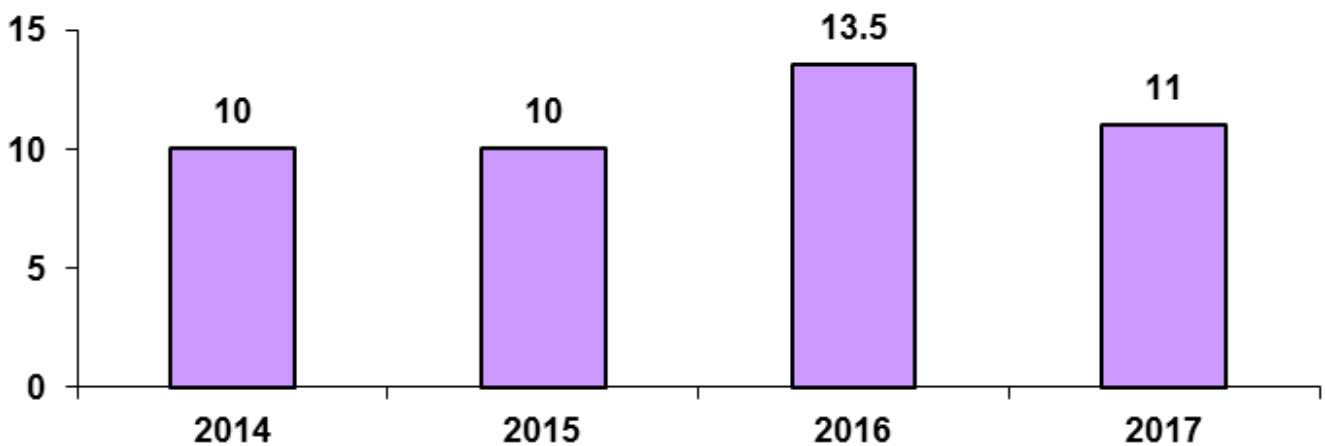
Just by looking at the product types in the table above, it can easily be concluded that out of the main 31 export products, top ten with the highest share in the export are related to metallurgy, 8 agriculture, 5 oil, 3 chemical and 2 food industries.

The above facts maintain that Azerbaijan has a very low capacity to secure the export product diversification.

Problem 2: the low level of non-oil exports in the country's overall export

In 2017, Azerbaijan's non-oil exports stood at \$ 1.538 billion, accounting for 11% of the country's total export value.

The dynamics of non-oil exports in the total country exports, relative to total exports in %



Share of non-oil exports in total country exports, %

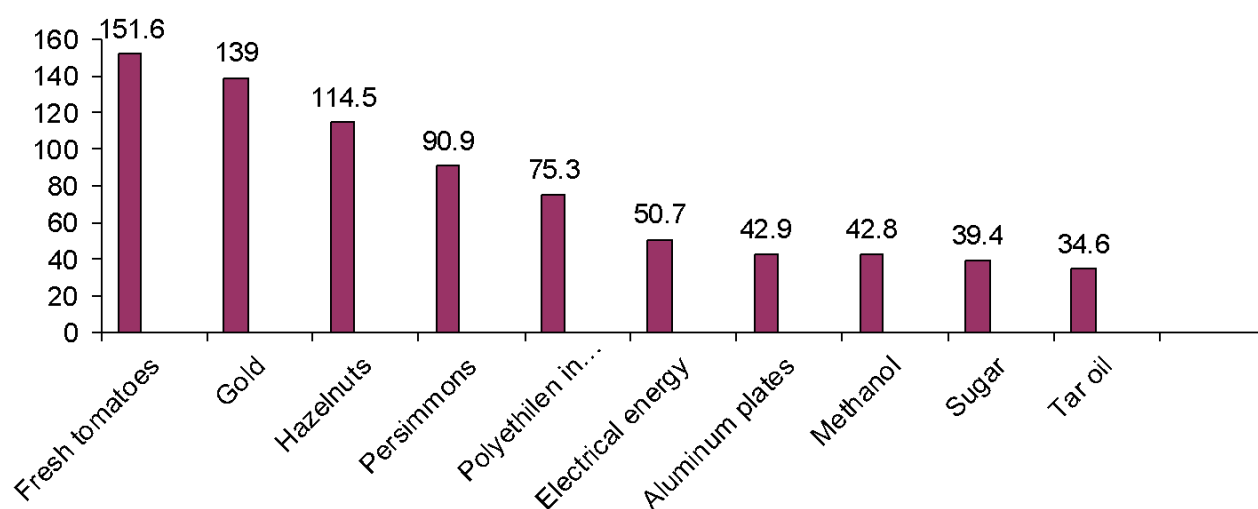
As can be seen from the chart, there were no significant

changes of the non-oil exports in the share of overall country exports from 2014 to 2017. The share of non-oil export products in the country's overall export was 10% and 11%, respectively, in 2014 and 2017.

Even though the volume of non-oil exports surged by \$ 150 million (+11%) in 2017 compared to 2015 and by \$ 300 million (+22%) compared to 2016, it was \$170 million less (-10%) compared to 2014. The interesting point is that in parallel to the decrease in oil and gas export revenues as a result of falling oil prices in global markets, there was decrease in the total volume of non-oil export revenues and it is quite challenging to find a sound answer to this phenomenon in economic terms.

Another interesting point is that on the one hand, the low level of export diversification appears in the concentration of main export volume (about 90%) in one sector alone – oil and gas, on the other hand, even though there were more than 1,150 product types in non-oil exports, in 2017 more than 71% of total non-oil exports (\$1.094 billion) was secured through 25 (non-oil) export products.

Export value of the top 10 non-oil exports in 2017, in \$ million



Furthermore, the top 10 non-oil exports with the highest share

(fresh tomatoes, gold, hazelnuts, persimmons, unprocessed polymer, electrical energy, methyl alcohol, sugar, tar oil, and aluminum plates) accounted for 51% of the sector's total export value (\$781.7 million).

As obvious from the chart if we exclude the first five export products, the total value of the remaining export products would not be that much. The highest indicator of the non-oil sector's export dependency on one product was 10% (fresh tomatoes with the export value of \$151.6 million).

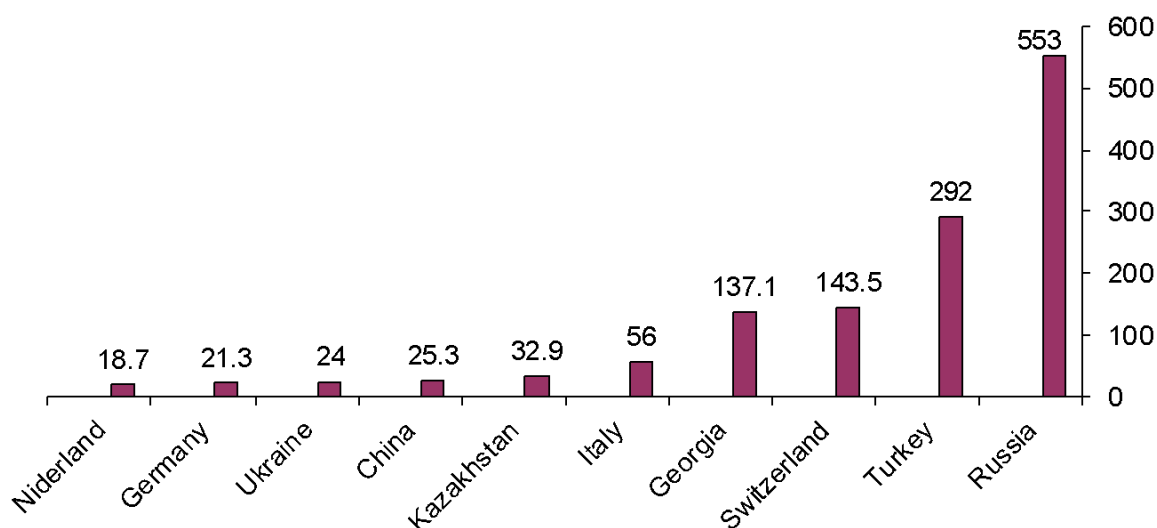
The average export value for the products (more than 1,100) accounting for nearly 95% of non-oil exports was \$ 500 thousand or less.

Problem 3: the low level of diversifying the geography of today's export

Not only the increase in the share of non-resource products in overall export is vital for Azerbaijan, but also the diversification of the export's geography is of strategic importance. No single country in the world is insured against crises and catastrophes. In this respect, the wider geography of the export exposes the exporting country to more risks, in case the importing country faces potential risks and threats.

Azerbaijan had foreign trade relations with 187 countries in 2017. However, about 77% of the country's non-oil exports fell to the share of five countries alone: Russia, Turkey, Georgia, Switzerland and Italy.

Top 10 countries with the highest share in Azerbaijan's non-oil exports in 2017 (in \$ million)



Top 10 countries with the highest share in the export of Azerbaijan in 2017 had provided 85% of overall exports from the country, pointing to the low level of the geography of Azerbaijan's export.

There are even some non-oil export products that Azerbaijan only exports to one or two countries, which are included in the top 10 non-oil export destination countries. For example, in 2017, 99.7% of fresh tomatoes was exported to Russia, gold export went entirely to Switzerland, 73% of hazelnuts was exported to Italy and Russia, 94% of permissions was exported to Russia, 89% of electrical energy was exported to Russia and Georgia.

The dependency level of Azerbaijan's non-oil export on one country (Russia) is 35%, on three countries (Russia, Turkey and Switzerland) is 65% and this is quite high indicators (in terms of country with the high risk export geography diversification indicator).

Problem 4: low technological capacity

Considering the classification of export products (low, medium low, medium high and high technological level) applied in international practice based on their technological level and complexity, almost all export products from Azerbaijan (including oil and gas) are included in the third and fourth

classification groups (low and medium low technological level). According to the classification, the export products with low technological level considered any raw materials produced which do not go through the processing stage, such as food products (including beverages), tobacco, textile, clothes, leather, leather products, paper, paper products, furniture, etc. According to our assessments based on foreign trade statistical data as of 2017, about 94-95% of Azerbaijan's overall exports and 50-55% of non-oil exports were classified under "low technological" products. Medium technological level products include refined oil products, rubber and plastic products and metallurgy products. The share of this technological level export products is not higher than 4-5% in the country's overall exports and 35-40% in its non-oil exports.

Medium high and high technological level products include the production of chemical industry products, equipment, medical and dental equipment, vehicles, electrical appliances, arms and other military products, equipment and devices related to the space industry, air transport and pharmaceutical industry products. If considering some scale of chemical industry and military products, the share of this group of export products in country's total exports in the best case is fluctuating between 1-2%.

Problem 5: the scarcity of export

According to official data, thousands of business entities are involved in the foreign trade process. However, a close look at the official statistical data indicates that 54% of all non-oil export (\$822 billion) was formed by 20 companies in 2017. Moreover, more than 30% of the total non-oil export of the country belongs to 10 companies with the highest share in export.

This situation shows that very few local businesses benefited from the export profits and the export profits itself is not

equally distributed among the export entrepreneurs.

Problem 6: low capacity of the private sector

It is no secret that Azerbaijan's oil and gas export revenues are under the state monopoly. Moreover, the share of the state in non-oil exports, which are much smaller than oil and gas exports, is quite big as well. For example, in 2017, the state sector constituted about one-third of the country's total non-oil exports (around \$500 million), with the share of the private sector in total exports, standing at about 65% (slightly higher than \$1 billion). Furthermore, 33% of the non-oil export turnover of the private sector (\$353 million) fell to the share of top 10 companies.