AZERBAIJAN

By Interfax-M&CN

Although Azerbaijan has reserves of iron, lead, zinc, molybdenum, alunite, gold, silver and industrial minerals (in particular zeolite), it is only a minor ore and metal producer. A few metal deposits were exploited in Soviet times but, since the beginning of the 1990s, ore and concentrate production in Azerbaijan, as well as metal output, has dramatically declined. Many of Azerbaijan’s mines and metallurgical plants have stood idle in recent years. Oil and gas are the main resources which play decisive role in the economy.

Azerbaijan has pulled through a recession and achieved steady economic growth starting in 1996 as the military phase of the Nagorno-Karabakh conflict with Armenia ended, the political situation stabilised, and foreign investment poured into the oil and gas industry. Azerbaijan's GDP grew by 11.4% in 2000. Industrial production last year rose by 6.9%. Agricultural production grew by 12.1% and capital investment was up 2.4%.

The IMF is expected to provide Azerbaijan with US$100-150 million for the implementation of a three-year investment programme, designed to support the country's macro economy, improve the system of public administration, reform the country's fuel and energy organisations, and also modernise the tax and customs bodies. The programme envisages the financing of projects aimed at developing agriculture and other sectors of the economy, which are not connected to oil production and refining. The programme also includes measures aimed at overcoming poverty in the country. Since 1992, the IMF has given Azerbaijan loans totalling SDR308 million.

In January 2001, the European Bank for Reconstruction and Development confirmed a new two-year strategy for Azerbaijan aimed at developing the private sector. The EBRD will expand its activity in the country in the mid-term by lending more to the private sector. The bank will also support Azerbaijan's policy to increase investment in the oil and gas sector. EBRD will focus on supporting small business, developing the financial sector, assisting authorities in creating a market infrastructure, speeding up the privatisation of small and medium-size enterprises, and eliminating obstacles to the development of the private sector.

In March 2001, Azerbaijan’s leader, President Heydar Aliyev, signed a directive on privatising the country's chemical, engineering and fuel-energy industry plants. According to the documents, up for privatization are 17 plants within the state company Azerkhimiya, 16 engineering plants, 67 plants part of the state oil company of Azerbaijan, 8 Azerigaz units, and 3 Azerenerzhi plants. In terms of the fuel and energy sector, the privatisation will focus mainly on small research institutions, plants for servicing petroleum extraction, district oil bases, and construction and repair plants. Privatisation will not affect enterprises that explore for, extract and transport oil and gas. Pursuant to the directive, chemicals and engineering sector plants are to be privatised through investment tenders or other legal methods. The State Property Ministry has been tasked with determining the way fuel and energy sector plants will be privatised. Azerbaijani companies, as well as foreign firms will be allowed to take part in the privatisation process.

Aluminium

In April 2001, President Aliyev gave his seal of approval to a contract between the Azerbaijani Ministry of State Property and Fondel Metals International BV of the Netherlands for the transfer to the latter of Azerbaijan Aluminium for 25 years. Azerbaijan Aluminum, or Azeraluminii, was set up in April 2000. It controls Sumgaittsvetmetall, Glinozem alumina works (Ganja), the Dashkesan Mining Combine and the Zeilik alunite mine. A statement by President Aliyev says the Dutch company has 25 years to pay the aluminium company's debts, except for wage arrears and similar indebtedness.

A tender was awarded to Fondel Metals to manage the aluminium complex in October 2000. The company pledged to invest US$1 billion, US$300 million of it in the first three years of the 25-year contract. The rules stated that Azerbaijan Aluminum must be producing annually 29,000 t of aluminium, 450,000 t of aluminium oxide and 850,000-1.25 Mt of alunite ore within three years of the contract being signed. Fondel Metals said it was prepared to raise aluminium production in Azerbaijan to 100,000-120,000 t/mth.

Oil and Gas

Azerbaijan has significant oil and gas reserves. Prior to the conclusion of the production-sharing agreements with foreign companies on the oil exploration and development projects, Azerbaijan’s reserves at offshore fields in the Caspian Sea were estimated at 4,000 Mt of oil. Moreover, that figure has risen thanks to geological studies being conducted by foreign oil companies. Offshore reserves are mostly contained in three fields (Azeri, Chirag and the deep water Guneshli). The potential resources in the Azerbaijani section of the Caspian Sea have been estimated at 4,000-10,000 Mt of oil equivalent. Azerbaijan also has onshore reserves, and proven recoverable onshore reserves are estimated at around 160 Mt of oil and around 50,000 million m^3 of gas. Total potential gas reserves in Azerbaijan, according to some reports, exceed 3,000 billion m^3, with predicted reserves of over 1,000 billion m^3 and proven reserves of 400 billion m^3.

Production of oil and gas condensate in 2000 amounted to 14.86 Mt, up 2% year-on- year. At the same time, production of gas in the reporting period fell 5.9% to 5.64 billion m^3.

There are two major oil-producing companies in Azerbaijan: The State Oil Co. of the Azerbaijani Republic (SOCAR) and Azerbaijan International Operating Co. (AIOC). SOCAR produced 9.01 Mt of oil in 2000, 0.1% over target and 21,200 t less than in 1999. SOCAR produced 5.02 billion m^3 of gas, which was 2.2% below target and 341.3 million m^3 less than in 1999. AIOC produced 5.1 Mt of oil in 2000 (4.81 Mt in 1999).

SOCAR plans to produce 8.9 Mt of oil in 2001. AIOC will remain the only operating company producing in the Azerbaijani section of the Caspian Sea in 2001. AIOC plans to finish modernising the Chirag-1 stationary platform in the second quarter of this year. The AIOC, which is developing the Azeri, Chirag and Gunashli oil fields on the Caspian Sea shelf, plans to bring Chirag's oil output to 5.75 Mt this year. Its 2002 target is 6.5 Mt. The Azeri oil field is expected to yield 5 Mt in 2005 and 17 Mt in 2006 under the Phase 1 project. Phase 2 will be launched around the same time, to bring the annual output to between 10 Mt and 12 Mt by 2008. The three fields will reach the peak of their capacity by 2010, yielding an annual 40 Mt. Their output will stay at this level until 2016 or 2017 and will fall after that. The AIOC's contract will expire in 2024.

Annual investment in Azerbaijan's oil industry starting this year will be US$2-2.5 billion. Investment for 21 agreements that have been signed with 33 oil companies from 15 countries will be US$60 billion, and US$3.4 billion has already been invested in the oil industry since 1996.

Russian oil major Lukoil is among the most active foreign companies in Azerbaijan's oil industry. Lukoil plans to start exploration drilling at the D222 structure in the Azerbaijani sector of the Caspian this year. In mid-2000, LUKArco Operating Co. Ltd decided on a drilling point for an exploratory well at D222. According to the conditions of the contract the depth of the well should not be less than 4,200 m. Lukoil (60%) and SOCAR (40%) signed an agreement on joint exploration and development of the D222 block in the Caspian in 1997, calling for investment of US$2.5 billion. Lukoil consequently transferred 46% of its share to its strategic partner US Arco and the shares of the partners in the project were as follows: SOCAR - 40%, Lukoil - 32.4%, Arco - 27.6%. After a merger between Arco and British Petroleum and the merged company's refusal to participate in the project, Lukoil's share rose to 60% again.

SOCAR and Lukoil also signed an agreement on the rehabilitation, exploration and development of the Zyk and Govsany oil deposits in Azerbaijan and on the distribution of production at these deposits, which are located in the south-east of the Apsheron peninsula. The first stage of work on this project involves the rehabilitation of the existing well fund and the modernization of infrastructure at the deposits. After the drilling of two assessment wells, a programme will be drawn up for the rehabilitation and future development of the deposits. Total investment in the initial phase will amount to over US$200 million.

Investment in the exploration area will be confirmed after a minimum programme of exploration work has been implemented. The main potential to increase recoverable reserves and production is tied to the development of new areas, including the offshore section of the Govsany deposit. The Zyk/Govsany project is oriented towards the Azerbaijani domestic market: Lukoil will process crude from the project at Baku refineries and the oil products produced will be sold through its filling stations, which will increase from five at present to 20. Residual recoverable reserves at the deposits amount to 25 Mt. The total contract area covers 128 km^2, including the rehabilitation area of 52 km^2. Productive oil horizons lie at a depth of 3,700-4,300 m. At the moment there are 15 wells in operation at the deposits, producing about 250 t/day of oil.

Given future growth in Azerbaijan's oil production, the country needs additional oil transport capacity to sell oil on foreign markets. Until recently, the AIOC's crude was shipped only via the Baku-Novorossiisk pipeline connecting the Azerbaijani capital Baku with the Russian Black Sea port of Novorossiisk. In late 1998, AIOC completed construction of the Baku-Supsa pipeline which links Baku with the Georgian Black Sea port of Supsa. AIOC shareholders financed construction of what is called Western Route Export Pipeline. This is 812 km long and has an annual capacity of 5 Mt of oil, as much as that of the Baku-Novorossiisk pipeline. The AIOC plans to increase the capacity of the Baku-Supsa pipeline by 20% within months by refurbishing pump stations. This will enable the company to put 6 Mt through the pipeline this year, compared with 5 Mt in 2000.

Meanwhile, implementation of the Baku-Tbilisi-Ceyhan project should give a boost to Azerbaijan's oil industry. The pipeline will have capacity to ship 50 Mt/y of oil. The sponsor group for the engineering efforts in the Baku-Tbilisi-Ceyhan project was formed last October and includes SOCAR with a 50% share, BP (25.41%), Ramco (1.55%), Unocal (7.48%), Statoil (6.37%), Turkey's TPAO (5.02%), Itochu (2.92%), and Saudi-American Delta-Hess (1.25%). Earlier the cost of the project was estimated at US$2.4 billion but the costs can be reduced by US$150-170 million if eight pumping stations are build and not 11, as planned earlier.