

Energy storage policy azerbaijan

Oil and gas exports continue to dominate Azerbaijan's economy and provide the majority of government revenue. Although they are plentiful, the long-term outlook for fossil fuel resources (and therefore for government revenue) is becoming uncertain in light of recent commitments by major importing countries to achieve net-zero greenhouse gas (GHG) emissions by 2050.

Oil and natural gas bring in around 90% of Azerbaijan's export revenues, and they finance around 60% of the government budget. They also supply 98% of primary energy and more than 90% of the country's electricity. Oil and, more recently, gas have been largely responsible for the remarkable rise in living standards in Azerbaijan since the late 1990s.

The government has recognised the need to reduce economic dependence on oil and gas exports. Efforts to modernise and increase oil refining and petrochemical production have been successful and continue to produce improvements. SOFAZ, the State Oil Fund of the Republic of Azerbaijan, could stimulate further diversification.

It is critical to increase efficiency, attract new entrants and investments, and diversify the energy supply in Azerbaijan's current energy system in which gas, electricity and heat are supplied by financially burdened monopolies at strongly subsidised prices. Policy responses should therefore include energy tariff reform, electricity and gas market reform, greater renewable energy use and higher energy efficiency.

The level of energy prices is central to attract investment and encourage citizens to use energy efficiently. As part of the country's social policy, the government sets domestic end-user prices for electricity, natural gas and oil very low, often below the full cost of supply. The IEA estimates that in 2019, Azerbaijan's implied subsidies for oil, natural gas and decline.

Subsidised tariffs do not encourage residential and industrial consumers to use energy more efficiently, even though it would make economic sense for the country as a whole. Tariff reform should therefore be central to Azerbaijan's energy sector reform efforts. The oil and gas saved through improved efficiency or through substitution by renewable energy could be exported at much higher prices or turned into higher-value-added petrochemicals. Furthermore, the GHG emissions avoided would help the country meet its Paris Agreement climate target (see below).

To reduce subsidies in the longer term, more emphasis should be placed on explaining to the public that blanket energy subsidies are a highly regressive measure that benefits mainly the well-off. These subsidies should be phased out gradually and replaced by support mechanisms that protect vulnerable groups.

Azerbaijan's 2016 Strategic Roadmap recognised the need for electricity reform, and several reform proposals

have been drafted. These include the draft laws on electricity, on the role of the regulator in energy and public utilities, and on the use of renewable energy in electricity generation. The IEA urges the government to adopt the pending legislation and proceed to implement an ambitious electricity market reform for the benefit of the country and its economy.

The establishment of the regulator in 2017 was a major step in electricity market reform. Since the Azerbaijan Energy Regulatory Agency (AERA) remains closely overseen by the Ministry of Energy, just like the electricity sector monopolies Azerenergy and Azerishiq, it will be essential to grant it the legal right to take binding decisions and issue recommendations. This also applies to its work in natural gas and district heating.

Instead of subsidising energy use for everyone, the government should focus social policy measures on those in real need while gradually switching to more efficient energy use. As part of its targeted support measures, it could, for example, launch programmes to replace the least efficient household appliances (refrigerators, washing machines, etc.) with new, highly energy-efficient models, offering subsidies for the least well-off.

As renovations to improve the energy efficiency of the existing building stock, especially residential and public buildings, would also save energy while benefitting citizen health, the case for introducing financing mechanisms for energy-efficient housing is strong. The government should also ensure that residential buildings comply with energy efficiency regulations. In many IEA countries, compliance is verified by public sector building inspectors, which is an approach Azerbaijan's government should consider.

Experience in IEA member countries shows that minimum energy performance standards are among the most effective and cost-efficient energy efficiency policy instruments. The government should therefore introduce stringent standards across all sectors to cover buildings, vehicles, appliances and equipment. These standards should be underpinned by an effective energy efficiency audit mechanism. It should also update the standards regularly and, when applicable, accompany them with energy labelling.

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Web: <https://www.hollanddutch tours.nl/contact-us/>

Email: energystorage2000@gmail.com

WhatsApp: 8613816583346

