

# Preface

The efforts to tap and oil and gas resources of the Caspian Sea and its vicinity have begun to draw much attention as a new focus in the international energy markets. The purpose of this book is to analyze the potential impacts of these efforts on regional and international politics. For years, Japan's contacts with Central Asia and the Caucasus have been extremely limited. Given the fact, however, that several of the countries which gained independence following the disintegration of the Soviet Union have been pursuing independent political and economic development strategies, the region has become too important to ignore when predicting where the ongoing realignment of the Eurasian continent is headed. This book is written with the basic perception that the development of the oil and gas resources of the Caspian Sea will be a crucial factor in this realignment process.

The background underlying the arguments presented in the book can be summarized as follows:

## ***Security Issues and the Development of the Caspian Sea Oil Resources***

Since the middle of 1997, the Caucasus and Central Asia have become the focus of international attention in connection with the launching of projects to develop the enormous oil and gas resource deposits in the Caspian Sea and its vicinity, mainly those of the Tengiz oil field and the oil field off the coast of Baku, Azerbaijan. The international oil majors, led by U.S.-based firms, have begun to take part in the exploration and exploitation of the region's oil fields, which have estimated deposits of 200 billion barrels of oil, or 20 percent of the world's total, as they are among the world's few with low development risks. U.S. oil interests have a 40 percent stake in the Azerbaijan International Oil Corporation (AIOC), which was established to exploit the undersea oil field off the coast of Baku, with a target production of 700,000 barrels a day in 2002. Especially noteworthy is the fact that during 1997 the United States made explicit its intention to involve itself in handling the security issues of the Caspian Sea and Central Asia. Thus a major process of regional realignment has begun to unfold, a realignment that not only pivots around the development of the Caspian oil and gas resources, but also involves the region's security.

## ***Adjustment of Interests among the Concerned Countries***

Five countries of the region — Azerbaijan, Kazakhstan, Turkmenistan, Russia and Iran — are directly involved in the development of the Caspian oil and gas resources. Before the collapse of the Soviet Union, all issues concerning the Caspian Sea were solved simply through bilateral agreements

between the USSR and Iran, but today the solution of such issues has to involve a balancing of the interests of these five countries. A tussle has been waged in the form of a legalistic debate over the rights to develop the oil resources. On one side of the argument are Azerbaijan and Kazakhstan, which insist that these rights should be handled in accordance with maritime laws on territorial waters and continental shelves. Russia and Iran, however, claim that the Caspian Sea is a lake, and that its resources should be developed jointly by the shoreline countries. Turkmenistan, which is sandwiched between the two camps, has taken a complex attitude toward the debate. Given the fact, however, that some projects such as the offshore Baku oil field have already been launched even in the absence of developments in this debate, the question of how to resolve the conflicts of interests among the five countries will remain a serious task.

### ***Changes over Time in the Region's Status: From Strategic Way-station in the East-West Trade, to an Outlying Region, and toward a Revived Trade Route***

For centuries the Caucasus and Central Asia had been characterized as a strategically important way-station in east-west trade. During the reign of the Soviet Union, however, it was relegated to the status of an outlying region within the Soviet federation. Its traditional links with neighboring countries were artificially severed, and it was rendered unable to perform its traditional role as a way-station for commercial trade. Now that the countries of the region have regained their independence, there are expectations that they will again perform the role of important way-stations for the east-west trade, and will also take on a new role as a way-station for north-south trade. However, the region's transportation infrastructure is insufficient for these roles, and it is to be hoped that improvements in this respect will be forthcoming in the future.

### ***Economic Difficulties Afflicting the Newly Independent Countries***

This region is blessed with rich endowments of oil, natural gas, and other natural resources. Yet the region consists of newly independent countries, all of which, since gaining independence, have been afflicted by ethnic rivalries and economic difficulties resulting from the transformation to market economies. The region is replete with a number of factors that make the political situation very volatile. It has been shaken, for instance, by the war between Azerbaijan and Armenian ethnic and territorial claims for Nagorno-Karabakh, which has displaced more than one million Azeri refugees, secessionist movements in Abkhazia and South Ossetia, both in Georgia, and a civil war in Tajikistan. Beside these strifes, the region is certain to experience a growing disparity between rich and poor, which may nurture deep social discontent. In the medium- to long-term, the region's countries may become able to use their oil exports to finance economic development, but they will have to steer their economic policies carefully and overcome the economic difficulties which they will likely face between now and then.

## ***National Security Questions for the United States, Russia, and the Individual Republics Concerned***

Most of the republics in the region would like to become more independent from Russia, in substance as well as in name, but Russia for its part is anxious to maintain or recover its influence over the region, and is strongly wary of the possibility that the Caucasus and Central Asia will stray from its sphere of influence following the eastward expansion of NATO. The U.S. policy toward the region has also taken a new turn. In the Caucasus, the United States has begun to side more with Azerbaijan despite its strong connection with Armenia, and has taken the initiative in mediating a peace between the two. In Central Asia, on the other hand, the United States has moved to reinforce its strategic tie-ups with Uzbekistan. Moreover, Azerbaijan and Georgia have established a de facto economic alliance. Armenia, for its part, signed a treaty for stronger military cooperation with Russia in May 1996, amidst a deepening economic crisis. With military units posted in Armenia, Georgia, and Tajikistan, Russia is capable of exerting influence on the region's ethnic conflicts, and thus on the political situation as a whole. The development of the oil and gas resources in the Caspian Sea and its vicinity is being constrained by the region's security issues, in the sense that a success of the former is conditional upon proper handling of the latter.

### ***Problems Concerning the Choice of Pipeline Routes***

Another problem involved in the tapping of the Caspian oil and gas resources, and one that completely differentiates the region from the Persian Gulf, is that the oil and gas produced in or in the vicinity of the lake called the Caspian Sea must be transported through a third country or countries in order to reach ocean ports and major consumption markets. Pipelines are deemed to be the most efficient means of inland transportation, and the choice of routes can be very important. If, for instance, a proposed pipeline route is very long, or if it passes through areas where construction is very difficult, then the construction costs can become an important constraint. Moreover, the construction of such pipelines takes on a strategic implication with close bearing upon the intra-regional relationships. Thus, the construction of pipelines for the development of the Caspian oil and gas resources has also acquired deep political implications.

### ***The Russian Route and Its Implications***

The central issues that have emerged in choosing pipeline routes are related to Russia and Iran. In linking Baku and the Black Sea, a choice had to be made between two alternative routes: the preexisting Russian route, and the newly proposed Georgian route. A compromise was made whereby the crude oil produced by the first phase of the development project, beginning in late 1987, would be transported via the Russian route, while the products of the latter phase would be shipped via the Georgian route, which would be operated in parallel with the Russian route. At first Azerbaijan was unwilling

to use the Russian route, and thereby subject itself to Russian influence, but it made a compromise to partially accept the Russian route, in order not to strain its relationship with Russia. It should also be pointed out that the Russian route passes through the Republic of Chechnya, which fought a war with Russia for independence, and that Russia was forced to make a concession to Chechnya on the question of the passage fee.

### ***The American Containment Policy Toward Iran***

The possible choice of Iranian routes will be complicated by unique factors. A pillar of the United States' strategic goals in the Middle East is a policy of containment toward Iran and Iraq, and it is trying hard to prevent Iran from gaining benefits from the development of the Caspian oil resources. Thus, it supports the development of alternative pipeline routes that will not pass through Iranian territory. Yet, the proposed Iranian route is attractive because it offers a short route to the Persian Gulf coasts or the Indian Ocean, and passes through areas which are politically stable. Iran has eagerly touted its geographical advantages to the oil producing countries in an attempt to change their minds. Already, Turkmenistan, which has declared neutrality and begun to act on its own to improve its relationship with Iran, is prying open a way to export its natural gas through Iran.

The American policy of containing Iran is an integral part of its world strategy, but, at the same time partly reflects the fact that Israel, which has considerable influence on American foreign policy, has identified Iran as its major enemy. There are, however, forces within the United States, including oil interests, who question the wisdom of continuing this policy. Spearheading these criticisms, former National Security Advisor Zbigniew Brzezinski has insisted that the United States should try to induce Iran into cooperating with the United States. Meanwhile, new developments seem to be brewing, as the new regime of President Khatami which took office in July 1997 has made approaches to the United States which might lead to a rapprochement between the two countries. Although it is quite possible that the Clinton administration has begun to look into ways of readjusting American policy toward Iran, rapprochement does not automatically mean that the U.S. will change its pipeline policy toward Iran.

### ***Alternatives to the Iranian Route***

One of the pipeline routes that has been proposed to bypass Iran is the one that starts from Baku, Azerbaijan, enters Georgia, and leads through Turkey to Cehan on the Mediterranean Sea. The U.S. government is openly endorsing this route because it believes that Turkey, which is a member of the NATO committed to secularism, can serve as an effective counterbalance to Iran's Islamic fundamentalism. For Turkmenistan's natural gas, a route that leads to Pakistan through the southern part of Afghanistan has been proposed. The drawback to this plan, however, is that the political situation in Afghanistan remains unstable because of the violent civil war which has been going on ever since the withdrawal of the Soviet troops. Following the

capture of the capital by the Islamic fundamentalist force Taliban in September 1996, Unocal Corporation, an American oil interest, approached the new regime to negotiate on the pipeline route, and the U.S. government, which does not officially recognize the regime, is indirectly condoning the negotiations. Iran, for its part, is taking a strongly alarmist view of Taliban, as it regards it as part of the wider international movement hostile to Iran.

### ***The Rearrangement of International Relations within the Commonwealth of Independent States***

A tendency toward dispersion is gathering momentum within the Commonwealth of Independent States (CIS), with the question concerning the procurement of energy resources being an important catalyst. Ukraine, the CIS' second largest country after Russia, is eagerly seeking ways to reduce its dependence on Russia for its oil and natural gas supplies; on one hand, it is trying to cultivate closer ties with Azerbaijan and Kazakhstan, and on the other, it is trying to ease its conflicts with Russia. The development of the Caspian hydrocarbon resources is working as a leverage for a rearrangement of the international relationships within the CIS.

### ***Asian Countries Are Also Taking Growing Interest in the Development of the Caspian Oil Resources***

China is reported to have decided to invest a total of 8 billion dollars into projects to develop oil in Kazakhstan and to construct a pipeline to transport the oil to China. Other countries outside the Caspian region, including Malaysia, Oman, and Japan, are planning to take part in the exploitation of the region's oil and gas deposits. To be sure, tapping the Caspian oil and gas resources entails greater difficulties, especially in connection with transportation, than those of the Persian Gulf. However, given the quantities of oil and gas which will be needed in Asia in the years to come, it is certain that Asian countries will show increasingly keen interest in the projects for developing the oil and gas resources of the Caspian Sea region once the oil and gas wells there prove to be productive. At the same time, there is no denying that, to make the development of the region's oil and gas resources more attractive to Asian countries, greater efforts are needed to solve the outstanding disputes in the Caspian Sea and its vicinity to ensure that their supply is stable.

This book is a joint product of Professor Valentine Yakushik, University of Kiev-Mohyla Academy in Kiev, Ukraine, the author of Chapters 2 and 3, and the editor, which is responsible for Chapters 1, 4, 5, and 6. I would like to express my gratitude to Professor Yakushik for sparing his precious time to contribute to this volume. To give the reader a few words of warning, there is some overlap between Professor Yakushik's papers and my own, but I have decided not to make changes in order to preserve as much as possible our differences of tone. I am afraid that this book may fail to satisfactorily explore many of the issues, partially because it was compiled in a limited time, and

partially because the state of affairs in the Caucasus and Central Asian region remains in flux. Nonetheless, we very much hope that it will be of some assistance to the reader in placing the development of the region's natural resources into a proper perspective.

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Manabu Shimizu  
Professor, Utsunomiya University

The views expressed in this paper are those of the authors and do not necessarily coincide with those of the Institute of Developing Economies.