

# Chapter IV

## Pipeline Projects and the Present Situation of the Caucasus

One peculiar feature of the development of the Caspian oil resources is the fact that the question of how the oil and natural gas should be transported to the consumption markets, especially those in Europe and Asia, has emerged as an independent issue which needs to be dealt with separately from those concerning production. The transportation question manifests itself in, or gives rise to, a set of questions: 1) How will transportation costs affect the prices at which the Caspian oil and gas can be marketed? 2) Who will undertake the large-scale pipeline projects? 3) Who will finance the projects? 4) Which route will be politically safest and strategically most advantageous? and 5) Where should future markets for the Caspian oil and gas be sought?

This chapter will be devoted mainly to a discussion of the political and strategic conditions in the Caspian region. It is important to examine these conditions, because the actual problems of the region involve factors that cannot be judged in terms of economic costs alone. We must examine factors that are closely interlocked with Russian policy toward the Caucasus and Central Asia, and the Eurasian strategy of the United States since the breakup of the Soviet Union.

Russia is keenly interested in retaining, or recovering, its political influence over this region, and in acquiring some leverage over the international oil and gas market. On the other hand, the United States is pursuing a new strategy in the region, and with ever growing impacts. One important strategic goal of the United States is to safeguard the "independence" of the newly independent countries of the region against the influence of Russia, or for itself to become a primary political influence in the region, replacing Russia. Another strategic goal is to exclude Iran from participation in the production of Caspian oil and gas, and to prevent the development of transportation routes or pipelines that would lead from the Caspian region to either the Persian Gulf or the Indian Ocean via Iran. This second objective is not based on short-term economic considerations, but rather is closely linked to the United States' world strategy, especially its Middle East strategy. It is related to the

ongoing dual containment policy of the United States against Iran and Iraq, and to the fact that Iran is to some extent opposed to the American-led Middle East peace process, but it is also anchored more deeply in the fundamental U.S. strategy in the Middle East, namely, the strategy of not permitting the emergence of any dominant regional power capable of influencing the oil market in the Persian Gulf. Therefore this "doctrine" may remain unchanged whether U.S.-Iranian relations are tense or not at any particular point in time.

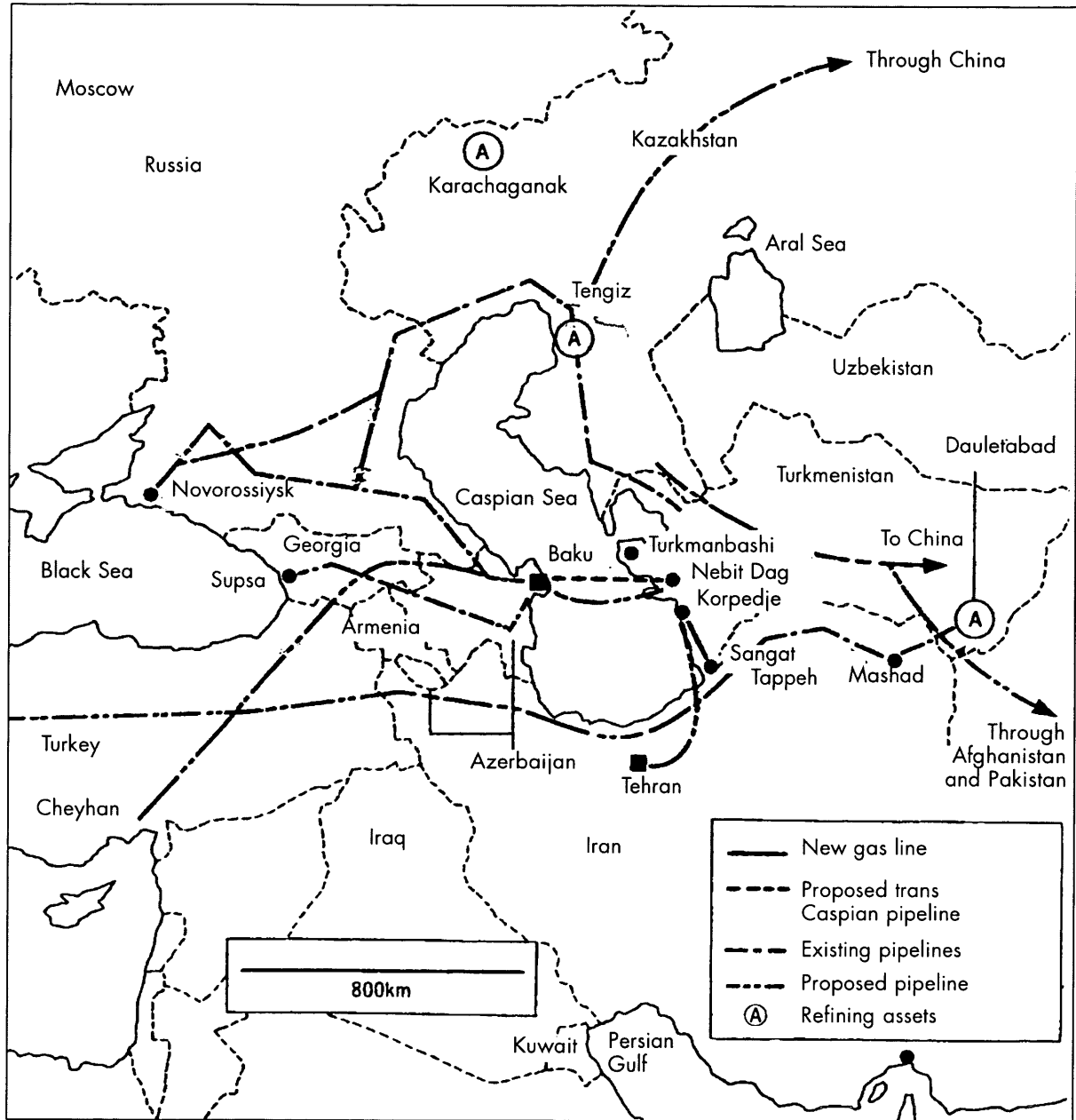
As is mentioned in the previous chapter, there are today pipelines connecting Baku, Azerbaijan, through the northern Caucasus in Russia, with Novorosiisk on the Black Sea. Russia has been insistent that this route should be the transit for future oil from Azerbaijan's Caspian offshore fields. However, there are competing projects or proposals for pipelines running through Georgia, through Turkey to Ceyhan on the Mediterranean Sea, or through Iran. Countries can gain leverage for economic and strategic power from having pipelines run through their territories. For this reason, we must pay special attention to Russian intentions, because the loss of its current monopoly on oil routes will inevitably lessen its leverage on the Newly Independent Republics in Caucasus and Central Asia.

Let us begin by focusing on the Caucasian countries, which will have direct bearing upon the oil route through Azerbaijan, and examine the political and strategic conditions of these countries, especially as seen in terms of their relationships with Russia.

### *1. The Transcaucasus*

The Transcaucasus (a region in the south of Russia, across the Caucasus mountains), which was once part of the Soviet Union, consists of three Republics, Azerbaijan, Armenia, and Georgia, which have populations of 7.5 million, 3.8 million, and 5.5 million, respectively, as of 1995, or a total of 17 million. Each country has a dominant, titular nation.<sup>1</sup> Azeris make up 83 percent of the population of Azerbaijan, Armenians occupy 93 percent of the

**Caspian Sea: possible oil and gas pipeline routes**



Source: *Financial Times*, Jan. 8, 1998

population of Armenia, and Georgians hold a 70 percent share in the population of Georgia. The percentage of population held by the titular nations in the Transcaucasus are considerably higher than in the Central Asian republics. Some Armenians have migrated to Georgia and Azerbaijan because they are engaged in trade and commerce. On the other hand, the Azeris of Azerbaijan have a large number

of compatriots living in Iran's northwestern province of Azerbaijan, so that the Azeris have a sense of being artificially divided into two states.

The Azeris belong to the Turkic race, and a majority are Shiite Moslems, while a majority of the Armenians and Georgians are believers of two branches of the Eastern Orthodox Church (the Armenian Orthodox Church and the Georgian Orthodox

Church). Thus, in each country, religion is closely related to the national/ethnic identity. The state languages of the three countries are Azeri, Armenian, and Georgian, all of which are quite different from each other. The Armenian and Georgian languages alone were allowed to retain their unique scripts even during the reign of the Soviet Union. In contrast, the script of Azeri, a Central Asian language, which was originally based on the Arabic letters, was Latinized and subsequently replaced by the Cyrillic script, which is used in Russian.

Until its absorption by Russia as a result of the latter's southward expansion in the nineteenth century, the Caucasus was an area of confrontation between Turkey and Iran. Thereafter, the period of unrestrained colonial control under the Russian empire saw repeated revolts against its rule. Immediately after the 1917 Russian Revolution, movements for the independence of the Caucasians erupted, and they maintained their independence until the Bolsheviks gained power in early 1920. As evident from this history, the region had a strong nationalist tradition of resistance against Russian domination. The rift that took place between Stalin and Lenin during the process of the formation of the Soviet Union over the "Georgian question" had a far-reaching effect on the relationship between the Soviet Union and its member Republics. In his conflict with Lenin over the question of how much leeway Georgia should be given to act independently, Stalin insisted upon concentrating power in the hands of the Union government.

Yet, the areas both to the north and the south of the Caucasus mountains (including areas belonging to the Russian Federation today), have a very complex intermingling of various nationalities believing in divergent religious creeds, and they were characterized, even during the reign of the Soviet Union, by extremely complicated manifestations of ethnic problems. Because of its rich underground oil deposits, and its strategically important geographical position between the Caspian and Black Seas (important in the sense that it served historically as an important route for East-West trade, and in modern history as a route of southward expansion from Europe or the Black Sea region into Iran and Turkey), the region attracted keen interest from not only local powers such as Turkey, Iran, and Russia, but also of external powers such as Britain and Germany.

During the Soviet period, however, the Cauca-

sus was artificially cut away from its traditional ties with the neighboring countries to the south, was forcibly incorporated into an economic and transportation system centered in Moscow, characterized as a geographically "marginal region" within the Soviet Union. Since it was dubbed as a marginal, outlying region, its transportation infrastructure was developed in a very unbalanced and lopsided manner. An exclusive emphasis was placed on making the region a better end point for transportation routes stretching centripetally out of Moscow, and little consideration was paid to reinforcing the more appropriate role of being a historically important commercial route. With the arrival of independence in 1991, the region found itself able again to restore its trade and commercial relations with the neighboring countries, thereby reasserting its status as an international commercial route in the southern part of the Eurasian Continent, or to move from being an "outlying" region to an "international center." The question of how to restore or improve transportation routes with neighboring countries such as Iran, Afghanistan, and Turkey became a pressing concern for the region. The challenge needs to be tackled in coordination with Central Asian countries, but it is safe to say that the process of reorganizing the movements of people and goods within the Eurasian Continent is already underway. Immediately after the dissolution of the Soviet Union, Azerbaijan (along with the five Republics of Central Asia and Afghanistan) joined the Economic Cooperation Organization (ECO), which was established in 1985 by Turkey, Iran, and Pakistan. The expanded ECO has great potential as a regional economic organization, depending on whether political conditions can be improved through better infrastructure for transportation and communication. In order to improve their relationships with Turkey and Iran, which will entail a resolution to the conflict in Nagorno-Karabakh and the Kurdish question, the countries of the region are facing the new task of intra-regional coordination, something that was unnecessary during the Soviet period. In 1996, Uzbekistan, Turkmenistan, Georgia, and Azerbaijan concluded a four-party agreement, with a pledge that they would work jointly toward trade liberalization and the abolition of tariffs among the four. Kazakhstan and the Ukraine have also expressed their desire to join this regional agreement, and this expression, even if it takes some time before it is materialized, underlines

the potential importance of the Caucasus as a commercial route.

The Caucasus has a very delicate ethnic and political balance. Azerbaijan contains within its borders the Nagorno-Karabakh Autonomous Region, with a population of approximately 150,000 mostly Armenians, while the country's Nakhichevan Autonomous Republic, which consists mostly of Azeris, has a detached enclave sandwiched between Armenia and Iran. Incidentally, President Heidar Aliyev himself is from the Nakhichevan Autonomous Republic. Georgia for its part includes the Abkhazia Autonomous Republic, the Adzharia Autonomous Republic, and the South Ossetian Autonomous Region. During the Soviet period, when Moscow exerted strong control over the region through Communist Party channels, ethnic conflicts in the Caucasus were somehow held in check.

The situation began to change following Gorbachev's election to Secretary General of the Communist Party of the Soviet Union (CPSU) in 1985. His policy of "Perestroika," or reconstruction, which was aimed at revitalizing the country's stagnant economy, proved unsuccessful, but the principle of "Glasnost," or freedom of information, which he called the pillar of economic reconstruction, had the effect of fueling the secessionist tendencies and nationalism in the Soviet Republics. The Caucasus was one of the first regions to experience violent outbursts involving ethnic minority problems. In 1987, when the country was still part of the Soviet Union, a movement in Nagorno-Karabakh demanding secession from Azerbaijan and incorporation into Armenia began to gain momentum. A head-on collision that took place in Sumgait, Azerbaijan, between Azeris and Armenians, led to a sudden deterioration of the relations between the two republics. Gorbachev's inconsistent policy on ethnic problems added fuel to the fire, accelerating the process of the collapse of the Soviet Union. In May 1992, the corridor of Lachin, connecting Armenia and Nagorno-Karabakh was occupied by Armenian forces.

The three Republics of the Caucasus declared independence amid this growing confusion caused by ethnic conflicts, with Georgia declaring its independence on April 9, 1991, Armenia on August 23, 1991, and Azerbaijan a week later on August 30, all in advance of the dissolution of the Soviet Union. Unlike the Central Asian Republics, whose independence was attained not through strong pressures

from popular, nationalist movements, but primarily by the judgments of their political leaders at that time (many are still in power), the independence of the Caucasian Republics was underpinned by violent nationalist sentiments, as evident from the Nagorno-Karabakh dispute. Thus, unlike Armenia, which maintained a close relationship with Russia, Azerbaijan and Georgia did not join the Commonwealth of Independent States upon its establishment, at the time of the dissolution of the Soviet Union in December 1991, but did so only later (in September 1993 and March 1994, respectively). And after their independence, all the three Republics have been living in the shadow of Russia, regarding their diplomatic relations with it as their most nerve-straining question. Even today, Russia maintains military units in Armenia and Georgia. As we shall see in greater details later, the Caucasus finds itself vulnerable to external pressure, especially from Russia.

The oil deposits of the Caspian Sea can be seen as both a powerful vehicle for the Caucasian Republics' economic development, and a weapon which can change the balance of power in the region. Armenia has deep concern about the future course of oil development in Azerbaijan, while Azerbaijan is intent on turning the region's situation into one more favorable to itself.

## 2. Azerbaijan

As has been pointed out already, Azerbaijan is one of the major players in the development of the Caspian oil deposits, and in particular the offshore deposits. Azerbaijan is bounded in the north by the Caucasus range and the Dagestan Republic, which is part of the Russian Federation, in the west by Georgia and Armenia, and in the south by Iran. It faces the Caspian Sea in the east. The Azeris are the majority people, and the Republic is named after them. Because of historical circumstances they have a group of compatriots living inside the Iranian Province of Azerbaijan, constituting a sizable ethnic group in Iran. This complicates the country's relationship with Iran, which is deeply concerned about the possible rise of a movement for greater-Azerbaijanism. Especially given the historical fact that the short-lived People's Republic of Azerbaijan was established after World War II, with the support of the Soviet Union, Iran has been on a constant

lookout for any signs of separatist actions by the Azeris. This explains why, in the Azerbaijan-Armenia dispute over Nagorno-Karabakh, the "Islamic fundamentalist" state of Iran has taken the apparently contradictory policy of supporting Christian Armenia rather than Islamic Azerbaijan. Religiously, the majority of the Azeris are Shiite Moslems, but they feel closer to Turkey than to Iran because of their linguistic and ethnic similarity with the Turks. Partly because of the lingering effects of the anti-Islamic policy and secularism of the Soviet reign, Islam's political influence extends only to a limited pocket of Muslims in Azerbaijan. On the other hand, Azerbaijan is on good terms with Israel, which has been trying to deepen its relations with Azerbaijan as part of a policy of antagonism toward Iran. It should be kept in mind, however, that the sense of belonging to the Islamic world has certainly restrained Azerbaijan from affiliating too closely with Israel.

The challenges confronting the government of President Aliyev (formerly a member of the Politburo of the Soviet Communist Party), which took office in June 1993, are to secure the legal right to develop the offshore oil field of the Caspian Sea, to finance the sustained economic growth of his country through oil export revenues, and to negotiate a settlement to the dispute with Armenia, on terms favorable to his country, by capitalizing on the country's enhanced international status as an oil exporter. In other words, Azerbaijan sees its oil deposits as an important strategic weapon for solving its outstanding problems with the neighbors. To meet this challenge, President Aliyev believes it is imperative both to improve his country's negotiating position vis-à-vis Russia by strengthening its ties with the United States, and to minimize conflicts with Russia while eliminating Russian interference. When Azerbaijan's relations with Russia became tense immediately after it signed a contract with AIOC in September 1994, President Aliyev put the capital of Baku under martial law, ousted then-prime minister Suret Husseynov and other government leaders on charges of having attempted a coup d'état, and thereby reinforced his own political power base. Although the economic hardship remains, the progress he had made toward the development of the Caspian oil fields has turned the political environment greatly in his favor. In the process of decision-making on the pipeline routes, Azerbaijan and Georgia have come to form a virtual community of common interests. With the passage

of time, and with further progress in the development of the oil resources, the situation vis-à-vis is growing increasingly in Azerbaijan's favor.

### 3. *The Azerbaijan-Armenia Feud*

In September 1991, the Republic of Nagorno-Karabakh proclaimed independence, but two months later in November, then-president Mutalibov of Azerbaijan declared the autonomous republic under his direct control. Subsequently, Armenian military forces advanced into the enclave, capturing 20 percent of Azerbaijan's territory, and establishing a corridor from Armenia to Nagorno-Karabakh. After many turns and twists, an armistice was reached between Azerbaijan and Armenia in May 1994. During the armed conflict, Armenia had held 20% of Azerbaijan's territory, and more than one million Azeris fled the occupied enclave of Nagorno-Karabakh and other areas into Azerbaijan proper and Iran. Following the signing of the armistice, the two parties began to exchange prisoners of war through Russia's mediation, and in June 1996 a trans-Caucasian summit was convened with participation of the leaders of Azerbaijan, Armenia, Georgia, and Russia. They agreed on the principles of respect for territorial integrity, non-aggression across borders, and respect for the rights of ethnic minorities.

However, even today, approximately one decade after the outbreak of the feud in 1988, the problems have yet to see a fundamental solution. One major obstacle that has frustrated a number of international initiatives taken during the last decade has been Russia's support for and the United States' leaning toward Armenia. Azerbaijan has a deep distrust of Russia, which, it was revealed, supplied Armenia with more than one billion dollars in weapons during the period up until 1995, even after the cease-fire. As for the American involvement, the existence of a powerful Armenian lobby within the United States pushed Armenia into second position, after Israel, in terms of per capita receipts of American aid.

It is important to note that at present, the prospect of the development and exploitation of the oil and gas deposits of the Caspian Sea is beginning to change the context of the feud. As the Caspian oil resources gain in importance, and as American oil interests come to attach greater impor-

tance to their stakes in Azerbaijan, the American policy toward the Caucasus is shifting, and putting the Armenian lobby increasingly on the defensive. The Armenian lobbies are especially powerful in the United States and in France, among other Western countries. In 1992, the United States imposed economic sanctions against Azerbaijan in protest of its cut-off of the oil supply to Armenia; but in October 1995, former National Security Advisor Zbigniew Brzezinski visited Baku, tilting the U.S. stance closer to Azerbaijan. This was followed in June 1997 by a visit to Baku by Deputy Secretary of State Talbott, with a proposal for arbitration which called, among other things, for Armenian withdrawal from the occupied territory. European Union and Turkey are also reported to have offered to act as mediators. Azerbaijan is proposing to give Nagorno-Karabakh the status of an autonomous province, but is opposed to the idea of forming a federation with it.

An oil pipeline route extending to Turkey via Armenia is one of the possibilities Azerbaijan is contemplating, and President Aliyev is reported to have made a proposal to offer the pipeline transport fees to Armenia in exchange for Armenia's withdrawal from the occupied territory. However, the conflict makes this a purely theoretical option. Nonetheless, a solution will eventually become necessary, as the pipeline from Baku to Georgia passes just north of the Nagorno-Karabakh area.

#### 4. *Armenia*

Armenia has borders with Georgia in the north, with Azerbaijan in the east and south, with Iran in the south, and with Turkey in the west. Though it prevailed militarily over Azerbaijan in the conflict over Nagorno-Karabakh, Armenia has suffered from an energy crisis as well as a serious economic crisis due in part to the economic blockade imposed by Azerbaijan. Now with the arrival just around the corner of an oil development boom in Azerbaijan, it feels all the more threatened and frustrated by the prospect of being put at a further disadvantage vis-à-vis its neighbor. Armenia is virtually blockaded by Turkey, an ally of Azerbaijan, and all its direct trade routes are closed, with the exception of the one with Russia, which passes through Iran and Georgia. Compared with the two other Caucasian countries, Armenia has cultivated deep

relations with Russia, and, as pointed out earlier, has permitted the latter to maintain military units within its borders. Toward the end of 1997, however, staunch nationalists began to gain the upper hand in a power struggle against forces favoring reconciliation with Azerbaijan, and as a result of this, a proposal made by the OSCE in December 1997 to settle the dispute in phases proved unsuccessful. In his compromise settlement plan, former President Ter-Petrossian envisaged a scenario where both the Nagorno-Karabakh and Armenian forces would withdraw from six areas of the Azerbaijani territory under their control, the Azeris refugees would be allowed to return to these areas, which would be placed under the control of international peace-keeping forces, and the final status of Nagorno-Karabakh would be determined subsequently. The proposed settlement plan reflected a sense of urgency existing in Armenia that the country needed to rehabilitate its economy and lift itself out of the state of isolation as promptly as possible. Nonetheless, the proposed settlement, upon which Armenia and Azerbaijan were reportedly close to agreement, was aborted after strong objections from the president of Nagorno-Karabakh to the proposed treatment of his region. Amidst the state of confusion following the breakdown of the settlement scenario, the Republican Bloc, Ter-Petrossian's support base, split in half, with the majority including Foreign Minister Alexander Arzumanyan and Central Bank President Bagrat Asatorian defecting to the staunchly anti-Azerbaijani nationalist faction headed by Ministry of Defense Gobazgen Sakishian, who is well known for his hawkish view that "The best way to maintain peace is to prepare for war." Ter-Petrossian, who had been President since independence in 1991, and had been reelected to a second term in 1996, was forced to resign, on February 3, 1998. Robert Kocharian, president of Nagorno-Karabakh from 1993 to 1997, was elected the new president of Armenia at the end of March 1998.

The momentum that had once built up toward the settlement of the dispute over Nagorno-Karabakh was dealt a set-back by this change of government. President Aliyev of Azerbaijan stated that he would honor the cease-fire agreement, but also noted that he was watching the developments in Armenia with deep concern. Armenia's actions present the most serious destabilizing factor for the future of the Caucasus, and an early settlement of

the conflict over Nagorno-Karabakh is needed all the more urgently. And Russia still holds the key to the improvement of the situation.

### 5. *Georgia and Ethnic Minority Questions*

Georgia is bordered in the north by Russia across the Greater Caucasus Range, in the east by Azerbaijan, and in the south by Armenia and Turkey across the Minor Caucasus Range.

For Georgia, a small Republic with a population of 5.5 million, allowing crude oil pipelines from Azerbaijan to pass through its territory would be an extremely desirable option for boosting economic development. The most serious problem faced by Georgia in pursuing this option is its concern about suspected Russian support for the secessionist ethnic minority movements within its borders. The pipeline route now under consideration is scheduled to pass at several places near Abkhazia (in the northwestern part of the country), South Ossetia (central-northern part), and Adzharia (southwestern part), where fighting with separatist forces is still going on. The armed confrontation with the Abkhazian Muslims has been suspended since 1994, but has not yet been resolved fully, as there are still temporary outbursts. On the other hand, the South Ossetians, the majority of whom are Georgian Orthodox, are demanding union with North Ossetia, which is part of the Russian Federation. These separatist forces have essentially won their civil wars with the central government of Georgia, and are now pressing the central government into acknowledging their victories as established facts. With respect to the civil war with Abkhazia, Georgia has expressed a readiness to give the secessionist forces there a degree of autonomy, but a final solution is still pending. Moreover, in an area near Abkhazia, an opposition force led by former President Zviad Gamsakhurdia remains influential, posing another challenge to be dealt with by Eduard Shevardnadze's government.

It should also be pointed out that Russia, even as of early March 1998, maintains four military bases and 15,000 soldiers in Georgia. Shevardnadze had to rely on the Russian army to suppress the internal revolts, and in March 1995 concluded an agreement on military cooperation. One of Georgia's most urgent agendas as an independent Republic, both

economically and politically, is to regain administrative rights over its shoreline borders with Turkey and to regain its right of defense over the Black Sea. In accordance with an agreement signed with Russia in 1994, approximately 2,500 Russian soldiers have been put in charge of controlling Georgia's borders, but the tedious procedures for crossing the border to Turkey, the country's major trade partner, are seriously hampering cross-border land transport, mainly by trucks, between the two countries. In 1997 a military base near the capital city Tbilisi was handed over from Russia to the Georgian military, but the base, it is reported, had been poorly maintained and was in a dilapidated condition when the transfer was completed.<sup>2</sup> How to withdraw the Russian forces, and how to eliminate Russian influence within the country, are burning tasks facing the country. Georgia's decisions in early 1998 to hold a joint military drill with Turkey and to give Turkish warships permission to make port calls in Georgia were clearly aimed at building a counterbalance to Russian influence.

On February 9, 1998, there was an assassination attempt on President Shevardnadze, who had been in office since 1992. A car parked close to his car exploded, killing his bodyguard, and injuring the President himself. Formerly Foreign Minister of the Soviet Union in the Gorbachev government, Shevardnadze had won the first election held under the new Constitution in 1995, and in August of the same year, shortly after the election, had also the target of a terrorist attack, in which hand grenades were tossed at his car, killing three people and wounding six. This meant that the attack in early 1998 was the second attempt on his life in three years. One of the President's aide announced that the attempted assassination was made by ultra nationalists and communists from Russia.<sup>3</sup> In fact, no evidence of the identities of the assailants was found, except for the fact that one was carrying a Russian passport. President Shevardnadze stated that the attempted assassination was meant to create confusion in Georgia in order to prevent the construction of new pipelines extending from the Caspian Sea through Georgia. Without pinning the blame on to the Russian government, Shevardnadze stated nevertheless that "a third group of Russian international terrorists" seemed to be responsible for the attempt. He also revealed his view that there lurked "behind the scenes extremely powerful forces who aim at a solution different from the

pipeline running through Georgia.” In 1995, after the AIOC, the Azerbaijani consortium announced a plan to build a pipeline that would pass through Georgia, with a capacity of 800,000 barrels a day. Russia opposed the Georgian route, insisting that the pipeline route should pass through its territory and its territory alone. Subsequently an agreement was reached on the parallel adoption of the Russian and the Georgian routes, but Georgia remains distrustful of Russian intentions. Both the Russian and the Georgian routes would involve transporting crude oil to the Black Sea via pipelines, and then carrying the oil aboard tankers from the Black Sea to the Mediterranean via the Bosphorus Straits. There are strong suspicions in the Caucasus that certain forces inside Russia, who are still displeased with the independence of the three Caucasian Republics, may be planning to reassert Russian control

over the region. There is also a strong belief in Georgia that Russia is trying to shake Georgia by supporting the secessionist movements in Abkhazia and South Ossetia, and the nexus between the ethnic minority problems within the country and the country’s diplomatic relations with Russia is an unwavering focus of attention.

Under these circumstances, it is clearly desirable that the construction of the oil routes, and especially the pipelines, be implemented in ways conducive to mitigating, rather than escalating, the region’s conflicts.

#### Notes

1. Refers to ethnic groups that have given their name to countries.
2. *Financial Times*, March 5, 1998
3. *Financial Times*, February 11, 1998