

AMERICAN UNIVERSITY OF ARMENIA

**A STUDY OF THE CONTROVERSY OVER THE OIL FACTOR
IN THE CASPIAN BASIN AND ITS IMPLICATIONS
FOR ARMENIAN FOREIGN POLICY-MAKING**

**AN INTERNSHIP POLICY PAPER SUBMITTED TO
THE FACULTY OF THE GRADUATE SCHOOL OF
POLITICAL SCIENCE AND INTERNATIONAL AFFAIRS
FOR PARTIAL FULFILLMENT OF THE DEGREE OF
MASTER OF ARTS**

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DECEMBER 2000

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ACKNOWLEDGMENTS

I would like to express my thankfulness to Dr. Ashot Galoyan, my faculty advisor, for his help and support while writing my Internship Paper. His advice has been very useful to my writing process.

I would like to say special words of gratitude to Ms. Dziunik Aghajanyan, my supervisor at the Department of Political Planning and Analysis of the MFA, and to express my genuine appreciation of her personal and professional attitude; the support I have got on her behalf and information provided by her.

My gratitude also goes to the faculty members of the Graduate School of Political Science and International Affairs for providing me with appropriate knowledge and skills to do this study.

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List of Abbreviations

AIOC	Azerbaijan International Operating Company
BP	British Petroleum
BSEC	Black Sea Economic Cooperation
CIPCO	Caspian International Petroleum Company
CIS	Commonwealth of independent Staes
CiO	Chairman-in-Office
CPC	Caspian Pipeline Consortium
EU	European Union
GUAM	Georgia, Ukraine, Uzbekistan, Azerbaijan, Moldova
INOGATE	Interstate Oil and Gas Transport to Europe
MEP	Main Export Pipeline
MG	Minsk Group
NAOC	North Absheron Operating Company
NGO	non-governmental organization
NK	Nagorno-Karabagh
OPEC	Organization of Petroleum Exporting Countries
OPIC	Overseas Private Investment Corporation
OSCE	Organization for Security and Cooperation in Europe
SOCAR	State Oil Company of the Azerbaijan Republic
TDA	Trade and Development Agency
TRACECA	Transport Corridor Europe-Caucasus-Asia
USA	United States of America
USSR	Union of Soviet Socialist Republics

ABSTRACT

This Policy Internship Paper is an attempt to discover the shifts in foreign policy orientations of the Caspian states, particularly those related to oil (Azerbaijan, Kazakhstan, Turkmenistan, and Georgia) during first years of their independence, and reveal its reflections on Armenian foreign policy-making. The Department of Political Planning and Analysis of Ministry of Foreign Affairs has provided immediate help and supported with the necessary information in the process of work on the paper.

The South Caucasus, a region full of tensions and conflicts, is a center of confrontation of great power interests (Russia, the U.S., and regional powers). They all try to enlarge the zones of their influence by taking oil exploitation processes under their control. In a region where the economy is mixed with politics, it's hard to expect predictability in foreign policies. In addition, the question of pipelines for Caspian oil has proven particularly susceptible to politicization. In fact, this is a zero-sum game, which especially restrains competition around the oil.

Armenia, as a non-oil state, however, is a pivotal country in the Caucasus, and developments in the region are directly reflected on Armenian foreign policy. being a landlocked country and because of the threat of being isolated from the regional cooperation, pipeline projects, Armenia should make maximum efforts to be fully involved in regional economic programs and exercise a foreign policy allowing to act equally with others and bringing utmost benefits to the Republic of Armenia.

I. INTRODUCTION

“It will be sad to see how the magnet of oil draws great armies to the Caucasus; it will be fascinating to examine how the oil companies mobilize their forces of diplomacy to fight their battles across green tables and behind the scenes...; it should be enlightening to study how far the foreign policies of nations, in the matter of recognition, of credits, etc., are influenced by that universal lubricant and irritant – oil...”

Louis Fischer (1926)

Within the last several years, the Caspian Sea basin has become the focus of attention for the world oil industry. The next “Persian Gulf” was supposed to have enormous and virtually untapped energy resources. It opened important new avenues for multinational investment and the fulfillment of consumer demand. “As at the turn of the century, global powers once again vie for market share in an area of the world exotic and remote” (Bremmer, 1998, p.1).

Five nations border on the Caspian Sea – Russia, Kazakhstan, Turkmenistan, Iran, and Azerbaijan. Because their national interests do not always coincide and because of the power conferred by oil, development of the Caspian cannot be separated from politics. This becomes more evident if we take into consideration that oil has been attracting some of the world’s major powers – the U.S.A., Russia, Turkey, and Iran into the region.

As Robert E. Ebel (1998, p.16) once pointed out, “ the scent of oil is very intoxicating. It is intoxicating to the private sector and to governments alike. Caspian and Central Asian oil and natural gas have caught the attention of a broad array of nations and entrepreneurs, for reasons which mix politics and economics. It is, in sum, the power of oil”.

In the beginning of the 20th century, Russian Empire produced 50 percent of the world’s oil from Baku, now in Azerbaijan, on the west side of the Caspian Sea (International Finance Corporation, 1998). Prior to the Soviet period, the Caucasus had been rather freely connected to the world, long functioning as a central transit point between Mediterranean Europe and Central and East Asia. In fact, the Silk Road passed right through this region (Hooson, 1998).

The rapid growth of the oil production in Baku occurred however after the establishment of the Soviet regime in Azerbaijan in 1920, and in 1940 the oil industry of Azerbaijan was responsible for 70 percent of all oil production in the Soviet Union. During World War II Baku oil was even piped to the Black Sea to aid allies. The region was targeted also by Nazi Germany, which repeatedly tried to capture Transcaucasia and cut-off the Soviet Union's oil lifeline.

Since the independence of the new republics in 1991, the geopolitical significance of the Caspian Sea drastically altered as a result of high-intensity campaign about the discovery of huge, previously unrecognized deposits of oil and natural gas, estimated to be the second largest in the world after the Persian Gulf. This campaign, aimed to entice flow of Western investments, bore fruit only in September of 1994, in Baku. Then the Azerbaijan International Operating Company (AIOC), a consortium of the world's major oil companies led by the British Petroleum Company (BP), signed an \$8 billion production-sharing contract with the SOCAR (State Oil Company of the Azerbaijan Republic)¹. The 30-year contract called for production of 80 000 barrels per day (b/d) by 1997; output was expected to reach an eventual peak of 700 000 b/d. The contract provided for the development of the Azeri, Chirag, and Guneshli offshore oil fields in the Caspian Sea, which were estimated to contain reserves of 3.8 billion barrels (Bolukbasi, 1998). Kazakhstan had already begun to see significant foreign investment in its oil sector as early as 1993.

There were, however, contradicting opinions and data about real oil resource capacity of the Caspian. Many independent experts have several times noted that Caspian oil reserves compose no more than 7-10 billion tons against the data (approximately 25 billion tons)

¹ In 1994 the stakes among the holders of the consortium (AIOC) were shared in the following way: US-based Amoco (17 %), Unocal (9.5%), Pennzoil (4.8%) and Exxon (5%), Russia's LUKoil (10%), Norway's Statoil (8.5%), Turkey's state-owned TPAO (6.75%), Japanese Itochu (7.45%), Britain's Ramco (2%), Saudi Arabia's Delta Nimir (1.6%), and Azerbaijan's SOCAR (10%) (Bolukbasi, 1998).

advertised by the high officials of the republics of Azerbaijan and Kazakhstan, and the US Energy Ministry (MFA, Political Bulletin #29, 09.10.1998).

While according to Hooson (1998), “after the war, the Soviets shifted their emphasis in oil extraction to the reserves of West Siberia, and the Caspian oil industry grew at a much slower pace. It aimed to marginalize the region geopolitically as the Southern periphery of the Soviet empire” (p.10).

However, the question why should have the Soviet government left rich and developed Azeri fields and drilled low-quality oil reserves in cold Siberia, which was far more expensive, than in the Caspian, was overlooked by the oil analysts. Obviously, the Soviet geologists did not find enough oil resources in the seabed of the Caspian to continue to produce. This speculation became more evident when some international consortia, such as NAOC (North Abseron Operating Company) of BP Amoco, and CIPCO (Caspian International Petroleum Company) of Pennzoil, which had contracts on the early drilling of Azeri oil fields, dissolved. This proved the rightness of people who were sure that there was more politics in the Caspian than oil (Naumov, 1999). In fact, 150 years of intensive oil production in Azeri Caspian has resulted in the consumption of 80% of initially proven reserves. Even Kazakhstan, which is the richest state with its hydrocarbon deposits among other littoral states, counts approximately 3 billion explored and proven reserves. The amount of course is not small, but the comparison of the Caspian would be more appropriate to the North Sea rather than to the Persian Gulf, which today has more than 90 000 billion tons of proven reserves (MFA, Political Bulletin #13, 26.04.1999).

Anyway, numerous plans were on the agenda for developing deposits through multinational consortia and transporting energy to world markets. *All these endeavors by the new states were directed to the achievement of balance against Russian dominance, which was accompanied by flourishing the relations with Turkey and Iran, and directing the*

transport of oil and gas away from Russian soil. In addition, such strategy was aimed at implementing unilateral projects in the Caspian basin. As an alternative, the emphasized pro-Western political line was obvious in the foreign policies of Kazakhstan, Turkmenistan, and Azerbaijan in the early years of their independence.

II. RESEARCH DESIGN

The purpose of this Policy Internship Paper is to study the political developments in Central Asia and Caucasus, and the shifts in foreign policy orientations in these regions under the influence of the oil factor. Armenia, not being an oil state, cannot, however, avoid to be involved in the regional political developments and should consider its foreign policy in the regional context, where the oil has a decisive role and an immense geopolitical importance. In this respect, this issue is seen as a significant one for Armenian foreign policy and demands special attention and study.

Research Questions

1. What interests did Great powers follow in the region?
2. What tendencies were noticed in the political orientations of the Caucasian and Central Asian countries since their independence until 1998?
3. What is the picture of foreign policy orientations of those countries from 1998 to mid 2000?
4. Do the oil price and the transportation routes play decisive role in the choice of foreign policy in Caucasian and Central Asian countries?
5. What is the possible implication of regional developments on the Armenian foreign policy making?

Methodology

In this Policy Internship Paper the historical and comparative method will be applied to analyze the existing data on the issue from 1998 to mid 2000. The data under consideration include official documents, reports, as well as materials covered by media.

Sociologists, political scientists, and other social scientists largely use historical and comparative method of research. It involves studies in finding out the development of different phenomena, in this case, political developments over time and/or across nations. The comparison of those findings allows to draw the pattern of political developments and reveal the purpose of the policies carried out by decision-makers of the respective nations (Babbie, 1995).

III. Interests of Major Players

The West/USA

Since the breakup of the Soviet Union, the West, and the U.S. in particular, have envisioned to prevent either a return to Russian dominance of the Caucasus and Central Asia or the rise of the Iranian one in the region. The one issue that US had to face in its regional policy has been the attempted development of the Caspian oil reserves. The Caspian became one of the highly restrained areas in the world, in which Russia and the US were competing actively and openly.

Initially, Washington was not too assertive on its efforts to gain influence in the Caucasus, acknowledging it as Russia's sphere of influence. It mostly supported Turkey's "petition" for influence there, taking into account also the cultural similarities of these new states in Central Asia and Caucasus with Turkey. However, by 1994-95, there was noticeable change in US policy toward the Caspian region.

Starting in 1995, the US specifically advocated the establishment of multiple energy export pipelines, traveling along an “east-west” axis from the Caspian region. The second half of 1996 marked a major shift in U.S. policy, as it announced that it considers the Caucasus and the Caspian a region of “vital US interests”. Georgia and Azerbaijan, started demonstrating explicit pro-Western/pro-US stance, and later on openly spoke about their firm intention to become NATO members (Cornell, 1999). Officially US policy on the Caspian region aimed to seek the following goals:

- Promote multiple pipelines and ensure the diversification of oil supply sources for the USA: energy dependence is the most powerful type of political-economic dependence. Understanding this very well, the U.S. tries to diversify its energy sources as much as possible (Sullivan, 1999).
- Support the realization of a new Trans-Eurasian trade corridor running through Georgia.
- Encourage the building of a large diameter pipeline from Baku to Turkish port of Ceyhan on the Mediterranean.
- Reinforce American sanctions against Iran by preventing Iran from serving as a transit route (Ebel, 1998).

Russia

The demise of the Soviet Union led to a tremendous reversal of Russia’s role both in Europe and Asia. The weakened economy, crisis in social sphere, and paralyzed state infrastructure forced Russia to be a mere witness of political developments for a while. It became a passive player in the struggle for the establishment of dominance in Central Asia and the Caucasus. Despite the above-mentioned factors, Russia still retained its influence and remained somewhat welcome, which served as a basis for trying to reassert its influence over former dominions.

For the past, the central goal of Russian Caspian policy has been to restrict outside players, namely, Turkey and the U.S. in this part of Russia's southern flank. The consequent policy objectives have been:

- first, to get involved in the biggest oil projects in the Caspian;
- second, to have the main oil routes pass through its territory.

The 1994 contract with AIOC Azerbaijani government expected to sign yet in September 1993, which did not include Russian oil companies. However, in June 1993, that is, two months before the signing of "the contract of the century", a military uprising that led to the ousting of pro-Turkish Azeri President Abulfaz Elchibei, made possible for Heydar Aliyev to become the next Azeri President, who, in fact, organized the allocation of 10% of AIOC to Russian LUKoil. Thus, Aliyev tried to change the strictness of Azeri pro-Western predisposition. He proved that once again by transferring 5% out of SOCAR's initial 20% share in the AIOC to the Iran's Overseas Industries and Engineering Company. However, AIOC, under the pressure of the U.S. administration, annulled the agreement (Sampson, 1999).

Currently Russia is more actively involved in the Caspian, and considers it as a priority. This is mostly due to Russia's new President Vladimir Putin,. He places special attention on the Russian Caspian policy and personally makes efforts to activate Russia-Caspian states relations.

Iran

The other crucial player in this game is Iran. Like Russia Iran also pursued a policy to avoid Turkish and Western presence in the region. As a result, Tehran initiated numerous cooperation plans with Kazakhstan, Turkmenistan, and Azerbaijan regarding the extraction of Caspian oil and gas resources, in order to extend its influence in the region. "Yet the US

opposition to most of the projects Iran promoted has eventually led Tehran to side increasingly with Moscow...” (Bolukbasi, 1998, p.398). In addition, Iran shared Russia’s position on legal status of the Caspian. Therefore, it has more positively related to the return of Russian hegemony in the region, than to the possible Turkish influence. “As a result of this, Russia and Iran have become increasingly aligned into ... a virtual alliance. Both states share an aversion to US and Turkish influence in their neighborhood and work together to minimize it. In this context Armenia has become a logical part of the alliance, and in fact a virtual Moscow-Yerevan-Tehran axis has emerged, whose main function is to counteract Turkish influence” (Cornell, 1999, p.8). Iran, in its turn, insisted the main pipelines to cross Iranian soil, claiming that it was the cheapest way to carry the Caspian oil to the world markets.

Turkey

Turkey is strongly Western-oriented country with close military ties to the US. Moreover, “it is sometimes seen as the prolonged arm of the US in Central Asia and the Caucasus” (Cornell, 1999, p.7). Turkey as the only NATO ally in the region serves as a means for the U.S. to excise Iran and limit Russian influence. This strong desire for the political influence, however, comes from Turkey’s being the primary transit point for petroleum in the region (Sampson, 1999). Turkey’s main ally in the region remains Azerbaijan. Turkey openly supported Azerbaijan in its conflict with Armenia. It supports Azerbaijan till now and has noticeable economic and political influence there (Cornell, 1999).

Turkey’s Baku-Ceyhan pipeline, strongly backed by the US, expresses the strategic interests of both countries in the region and excludes Russia from having important role in the Caspian, a goal to which they direct their immense economic leverage in the form of different programs carried out in Azerbaijan. They also continue the process of campaign to

convince international oil companies to opt the Baku-Ceyhan line. The implementation of the project still remains uncertain, as its financing is under suspicion.

IV. Tendencies in Foreign Policy Orientations

To consider major shifts in foreign policy orientations of the Caucasian and Central Asian republics two phases can be viewed; ***first***, since the independence to 1997, with emphasized pro-Western foreign policy disposition, and ***second***, starting from 1997 up to the present with noticeable shifts in orientation toward Russia, at times with balanced expressions.

The loosening ties between the republics and the central authority in Moscow, and the complete dissolution of the Soviet Union in 1991, have brought up the question on how different republics would relate to their immediate neighbors and to the broader international community. The chance for regional cooperation increased as the newly independent and economically weak republics were seeking to replace Russia with new economic partners. The West, and particularly the U.S. wanted to see Turkey's position as a Western NATO ally enhanced in the Caucasus and in Central Asia, and that of Iran contained. Therefore, the foreign policies demonstrated by the Caucasian and Central Asian republics right after the independence were extremely pro-Western especially those of related to oil. Oil was highly manipulated in their purpose to restrict Russian influence on their economies. Two important factors explained that tendency: first, eagerness to preserve newly acquired sovereignty; and second, to gain active Western backing.

Such predisposition predominated in the foreign policies of those countries especially during the Oil Boom (1994-1997).

Azerbaijan

During the first years of its independence Azerbaijan acquired an image of a newly sovereign state not only welcoming the West very warmly, but also denying any kind of Russian presence and influence there. Abulfaz Elchibey, coming to power in 1992 moved to cut ties with the CIS. Though being called “anti-Russian” leader, Elchibey several times tried to show that he signifies the relations with Russia, while rejecting the Russian dominance in the CIS.

However, there were also tensions between Russian minority in Azerbaijan and the representatives of the titular nationality, which came out into the open at times over language issues, and then definitely with the struggle over Nagorno-Karabagh when Russians, as Azeris argued, tended to support Armenians.

As a result of 1993 coup, Heydar Aliyev succeeded Elchibey, who was expected to be a leader with more pro-Russian disposition. However, Aliyev’s return did not mean a restoration of Russian dominance. Indeed, Aliyev seemed to be more enthusiastic in his prompt acceptance of CIS membership, but he never permitted the return of Russian troops to Azerbaijani soil (Sampson, 1999). Moreover, he widely encouraged international oil companies to come to Azerbaijan and invest considerable amount of money, convincing the world community that there are huge, undiscovered oil reserves in the southern Caspian.

Georgia

Independent Georgia also tried to refuse the participation in the CIS, and was inclined to cooperate with bordering Turkey, and to embrace the West rather than to continue with the Russian dominance. However, de facto dissolution of Georgian state, that is, Abkhazian and South Ossetian de facto secessions, compelled Georgia to accept Russian troops on its land and CIS membership.

Georgia's interests are principally similar to that of Azerbaijan's, since both struggle for territorial integrity: Azerbaijan still is in conflict with neighboring Armenia over Nagorno-Karabagh and faced the issue of refugees and occupied territories; Georgia is a more explosive republic in terms of the number of internal conflicts and the danger to dissolve eventually, such as the possibility of territorial claims of Javakhetian Armenians or Agarians. So, both hope to have Western support in their territorial issues. The commonality of interests resulted in more close relations between these two Caucasian states. However, to get stability in the country, Georgia had tried to keep possible neutrality in its relations with the neighbors, while not concealing its strong desire to become NATO member. Furthermore, in order for this desire to become more realistic, Georgia has pursued a proactive rather than reactive foreign policy, the evidence of which became the creation of GUAM² (Cornell, 1999). In addition, Georgia is widely involved in oil deals of the Caspian in terms of transportation – Baku-Supsa pipeline currently is in use, and Baku-Ceyhan, if to be constructed, will cross Georgian land. Georgia gets and hopes to get in the future considerable revenues from transit fees, which carry great importance for the strained Georgian economy.

Kazakhstan

Kazakhstan is a state whose titular nationality represents only roughly half of its population and includes substantial Russian-speaking community (out of 17 million only 8 million are Kazakh). The overall inclination of Kazakhstan's foreign policy throughout its independence can be characterized as pro-Russian at times with some fluctuations. Kazakhstan is a CIS member and is a part of the Treaty on Collective Security signed in May 1992. Also it is in bilateral security agreement with Russia signed in May 1992, too.

² GUAM will be discussed below in detail (p.39).

In the course of the dispute over the legal status of the Caspian, Kazakhstan also, like other Caspian countries, opposed Russian argument, trying to control its oil industry the way it wanted and without Russian interference. This strategy toward Russia was evident even in the speeches of high officials, like Kazakhstan's former Prime Minister; who in his radio speech specifically noted that "as soon as we are no longer dependent on Russia in oil matters, it will talk differently with us" (Blum, 1998, p.141). This strategy had an obvious purpose to keep Russia away from being involved in Kazakh oil production as well as transportation issues.

Turkmenistan

If Kazakhstan sometimes demonstrated controversial foreign policy toward Russia and the West, Turkmenistan pursued clearly more independent policy in the beginning. However, its small size and economic dependence on Russia, did not allow it to occupy hard positions, especially when it faced the problem of transporting its natural gas (Cornell, 1999). The only pipelines available for the realization of this task of vital significance for Turkmenistan, cross Russian territory. Turkmenistan has no other choice since Iranian version for getting world markets is limited by the 1996 Iran-Lybya Sanctions Act³, and Afghanistan is extremely risky zone for oil companies.

V. The Controversies in the Caspian

1. Legal Status

The exploitation of the Caspian oil reserves has been held up by the disagreement of the five countries bordering the sea regarding the division of the Caspian basin, where the issue

³ The Iran-Lybya Sanctions Act (ILSA), passed by Congress in 1996, provides that foreign companies that invest more than \$20 (later it was raised up to \$40 million) million in Iran's energy sector are liable to sanctions.

of legal status of the Caspian Sea was largely debated. Throughout the Soviet period international regulation involved only the USSR and Iran, and from 1921 until 1991 the legal status of the sea remained essentially stable. Since 1991, however, the Caspian's status has become increasingly debatable among Russia and the other states bordering the Sea, with sharp disagreements over access to, and maintenance of, natural resources. The key legal dispute over the Caspian has centered on the permissibility of dividing the Sea into exclusive zones to be used by each sovereign state. This involves the issue whether the Caspian should be defined as a sea or a lake. If the Caspian is defined as a sea, the international law implies certain distributional arrangements. On the other hand, if defined as a lake, it as such requires mutual consent for the establishment of zones, and for division of the resources (Blum, 1998).

Russia, trying to take part in all Azeri, Turkmen, and Kazakh agreements somehow became more patient toward the Western involvement, at the same time continued to argue that there should be a treaty between Caspian littoral states determining the issue of the legal status of the Caspian. In this way Russia hoped to keep Western companies away from investing in the region claiming that those contracts would have no binding effect. Iran, after its exclusion from AIOC, defended Russian stance on the legal status of the Caspian. They viewed the Caspian as an international lake, and insisted treatment of the Caspian be derived from established custom and usage in the region (Horton, 1998). Russia continued to demonstrate coercive stance: until 1997 it systematically denied Azeri ships access to the Volga-Don. However, Azerbaijan was resistant. Kazakhstan and later Turkmenistan sided with Azerbaijan in resisting Russia's legal claims by calling for division of the Sea into exclusive zones (Finansovoye Izvestiya, November 25, 1997).

2. Pipeline Routes

The other issue dividing the five littoral states concerns the routing of pipelines to transport oil out of the region. Moscow wants the pipelines to be routed through Russia; the US favors a route under the Caspian, through Azerbaijan and Georgia, to Turkey; and Tehran wants the pipelines to be routed through Iran.

Robert E. Ebel (1998), the Director of Energy and National Security at the Center for Strategic and International Studies (CSIS), brings three reasons asserting why countries seek the construction of pipelines across their territories: first, transit fees, which can be considerable over time; second, anticipated economic stimulus to the regions; and third, the political and economic leverage a pipeline confers. The US-backed Baku-Ceyhan, however, is the most expensive alternative, but the political rewards, that is, reduced Iranian and Russian influence in the region, are highly expected. In contrary, “the cheapest pipelines face the greatest diplomatic obstacles. The most attractive economically is a pipeline running due south from Baku to Iran. But American sanctions have kept this southern route off the table” (Bremmer, 1998, p. 2).

Unlike other major oil producing regions, Caspian Basin is landlocked with few good options to reach the outside world and, therefore, needs pipelines crossing several borders to get to world markets. International oil companies before investing huge amount of money in the region want to be sure in the safety of the oil transportation routes.

Soviet-era infrastructure, combined with geopolitical instability resulting from ethnic tensions and conflicts in the region, means that there is no easy link between Caspian resources and consumers. To have political objectives fulfilled and to have oil flow to the world markets avoiding Russia, new pipelines needed to be built. Many proposals of pipelines for moving Caspian crude oil to world markets were considered and are still under deliberation. The players of this “great game”, as many analysts like to call, have presented

their pipeline options, which would enable Azerbaijan and Kazakhstan to export their oil. The main competitors over the route selection then, in 1994, were Moscow and Ankara, and each promoted its own version.

Russians, in fact, proposed expansion of their pipeline route. It consists of two branches. One requires construction of 1500-kilometre \$1.8 billion pipeline from the Kazakh Tengiz fields through Tihoretsk (120 km East of Novorosiisk) to the Russian Black Sea port of Novorosiisk. This pipeline, which would have a 600 000 b/d capacity, would join the existing 1400-kilometre Baku-Tihoretsk pipeline which could carry the Azeri oil from the Caspian Sea (Bolukbasi, 1998).

If the Russian route was the only way to move Azeri and Kazakh oil, Ankara would have become a loser in this game of taking the dominance over the region. After the collapse of the Soviet Union the U.S. expected Turkey to play a key role in the region by providing strong ties with the newly independent Turkic states. Accordingly, Turkey proposed its own pipeline option, Baku-Ceyhan, which would carry the oil through Georgia to Turkish Mediterranean Sea port of Ceyhan. This export pipeline is estimated to cost \$2.5 billion but could run as high as \$4.5 billion (Lelyveld, 1998). The US-backed Baku-Ceyhan, however, is the most expensive alternative, but promised significant political rewards. The Clinton administration hoped that it would serve the US policy of preventing Iran from participating in the development of Caspian energy resources. Therefore, since September 1994, Turkey began intensively to convince AIOC to choose Baku-Ceyhan as the main export pipeline claiming that it was the most commercially sound option. Despite numerous delays on the selection of route, the agreement on Baku-Ceyhan was eventually signed in November 1999, yet the construction has not yet begun due to various political, economic and legal differences among the signatories.

The other target of the US multiple pipelines policy is the construction of the Trans-Caspian gas pipeline as a component of the east-west corridor. It is projected to compliment Baku-Ceyhan, and is aimed at weakening Turkmenistan's dependence on Russian pipeline network and the possibility to seek Iranian cooperation. While the pipeline is not yet constructed, Turkmen gas continue to run through Russian routes.

However, before the AIOC's decision on the MEP (main pipeline route), it had to resolve the problem of transportation of the so-called "early-oil" – the preliminary and relatively low-level Caspian production.

Because of commercial, logistical, and geostrategic reasons, many oil companies as well as political players, preferred to avoid altogether both the existing Russian pipeline network, and proposed routes passing through Russian territory.

In this respect Russia had enormous leverage. Soviet central planning meant that roads, rails, electricity, and pipelines ran from Russia to the outlying republics. Nearly this entire infrastructure is still in place. The Soviet large pipeline network was the most extensive in the world, with a design capacity of 12 million barrels per day, of which 2 million was designated for export. After the dissolution of the USSR, eighty percent of the system is still under the control of the Russian Federation, where Transneft has monopoly position over the Caspian oil transportation (Marashian, 1998). This helps to understand why despite the overall unwillingness of oil producers, they could not avoid the usage of Russian pipeline network for their purposes.

Having these considerations in mind and also under the pressure of Russian and Turkish campaigns, and for pure commercial reasons, AIOC, eventually, made a decision on 9 October 1995, that "early oil" from Azerbaijan would be transported to the Black Sea through two pipelines. One was the northern functioning route through Russia, crossing Chechnya, to the port of Novorosiisk on the Russian Black Sea. The other was the so-called western route

that ran from Baku to the Georgian Black Sea port of Supsa (Partridge, 1998). This was the compromise approach in order not to restrain already antagonized relations between Moscow and Ankara on this issue. Anyway, Turkey announced this achievement as a victory against Russia's attempts to fully dominate the region politically and economically (Bolukbasi, 1998).

Kazakh "early oil" also was transferred to the world markets, through Russian pipelines. However, the main target of Russian efforts was to achieve dominant position in the transportation of Kazakh "big oil". Eventually Russian government's long struggle, begun yet in 1994, gave positive results. In November 24, 1998 US-based Chevron-led Caspian Pipeline Consortium (CPC), with 20 billion investment, including Russia and Kazakhstan and other oil companies signed a pact to build a pipeline connecting Kazakh Tengiz oil field to a Russian port on the Black Sea. The Tengiz oil field is one of the largest oil fields in the world with proven high-quality oil reserves of 6-9 billion barrels. "The Caspian Pipeline Consortium's 1,200 km, \$2 billion pipeline – half new, half refurbished – will carry crude from its Tengiz and nearby fields on the Eastern shores of the Caspian, to the Black Sea port of Novorosiisk. It will be built along the route of an older Russian network. The pipeline will be the first major oil route through Russia controlled independently of the monopoly operator Transneft. Shipments may start in three years (2001), with supplies going through the Bosphorus Straits and to markets in the Balkans. Initial capacity of the 42-inch line is set at 560 000 barrels per day; ultimate capacity may reach 1.5 million barrels per day" (Marashian, 1998, p. 36).

Under this agreement Russia acquired a 24% share of the consortium, Kazakhstan, 19%, and Oman, 7%. Other shares were held by oil companies: Chevron took 15%, venture of LUKoil and ARCO, 12.5%; Royal Dutch/Shell Group and Russian RAO Rosneft, 7.5%; ENI of Italy, 2%; BG PLC of Britain, 2%; and Oryx Energy Company of Dallas, 1.75%.

This agreement as a next Russian achievement came to prove that Russian power to influence had not yet been consumed (Gordon, 1998).

And while CPC or the Turkish pipelines are not available, Kazakhstan will continue to rely on the Tengiz-Novorosiisk pipeline not only for exporting Tengiz oil, but also for Kazakh offshore Caspian oil, once being extracted. Even the efforts of Tansu Ciller, the then Turkish Prime Minister, to convince Nursultan Nazarbaev of Kazakhstan to choose Turkish pipeline, became vain in August 1995. Moreover, Nursultan Nazarbaev insisted that Kazakh oil should initially be transported to Russia's Black Sea terminals. Later, even accepting Turkish variant, Nazarbaev at the same time emphasized the importance of a diversion of pipelines from the main line to Turkey having in mind the CPC. In addition, Nazarbaev suggested Russia also take part in Turkish pipeline project (Bolukbasi, 1998).

The failure of a big international pipeline project contributed to the Russian advancement in the region was. The project which included US-based companies and also Turkey, Iran, Turkmenistan, and Russia, would cost \$6-7 billion, foresaw a 3500-kilometre export pipeline for Turkmen gas through Iran and Turkey with the aim of eventually reaching European markets. However, the US' position toward Iran's participation was strict, that is, it pursued Tehran's permission on foreign ownership of the 1450-kilometre Iranian section of the line. Tehran remained resistant. As a result, in February 1996 the Russian company Gazprom and the Turkmenistan Ministry of Oil and Gas established a joint venture, Turkmenrosgas, which gained the right to extract hydrocarbon deposits, and to make agreements with CIS countries on the export of Turkmen natural gas (Bolukbasi, 1998).

This period was manifested by noticeable shift toward Russian orientation of foreign policies of these countries. The failure of the Western countries to implement big oil projects left the oil countries with no other choice but to turn back to Russia.

Nevertheless, the key question how the “big oil” would reach world markets, continued to remain open, as AIOC did not hurry to eventually make such an expected decision. Moreover, AIOC’s preferred option was to expand the capacity of both Novorosiisk and Georgian pipelines. Especially after the merger of British Petroleum and the American company Amoco, which held at the time (August, 1998) one-third of the shares in the AIOC, the tide turned completely against the Turkish proposal. Moreover, the former AIOC President John Leggate said that Baku-Supsa was opted as a clear expression of AIOC’s rejection of the project, as the latter is twice as expensive and longer than Baku-Supsa (Saadet, 1998). On the other hand, Kazakhstan complained that the selection of MEP was up to Azerbaijan, and not to Kazakhstan which is the main oil supplier of the Caspian, and declared that Kazakhstan itself will determine the routes through which its hydrocarbon export would reach to the world markets (Baku News Summary, 08.07.1998). This position adopted by Kazakhstan was an obvious rejection of Baku-Ceyhan. Indeed, the analysts predicted that “the choice of the route for the main export pipeline, which will be developed by the world’s big oil companies and the participating states, will decide the winner of the biggest game” (U.S. News and World Report. May 10, 1999).

VI. Caspian States and Oil Companies

Apart from the producing states in the Caspian, international oil and gas companies are the most important players. Without their desire to contribute risk capital and management competence, nothing can go ahead. They are primarily guided by the logic of the market place: commercial assessment of projects in order to achieve required rates of return. In the past oil companies (BP, ENI, American companies) were mostly identified with their home state politics. However, such closeness now sometimes disappears under the global market pressures. “If association with politics helps to develop the competitive position of the

company, markets will reward it – but if it is a sacrifice of the commercial objectives of the company, markets will penalize it” (Waelde, 2000, p. 12).

This corresponds to the situation of continuing delays of Baku-Ceyhan project, which despite its prohibitive expense and questionable security would have number of political goals. However, this route will be established only if somebody will finance the cost excess, and it is clear that neither the US, nor the Turkish government is ready to take this burden. So, they exercise considerable pressure on the companies as it is uncompetitive by itself. Therefore it can be assumed that “the higher the political pressure, the greater is the deficit of such projects” (Waelde, 2000, p. 10). The commerciality of the Baku-Ceyhan even according to American oil companies will be provided by exporting 60 million tons per year, which can be realistic if Kazakh oil also will run through the same route. Based on the most optimistic estimates Azerbaijan can provide only 30-40 million tons of oil per year (MFA, Political Bulletin, #29, 09.10.1998).

On different levels, however, US/Turkish efforts were put together to keep the project on the agenda. Suleyman Demirel in 1999 in Washington declared that Baku-Ceyhan would start in the year 2000, while all experts had expressed their belief that that was an impossible goal (Kazaz, 1999). Therefore, it is unlikely that oil companies will pay for a purely political pipeline accompanied, in addition, with uncertain factors (volatility of oil price; high political risk in producer countries) and security risk (ethnic conflicts in the region and possible Kurdish attacks). Hence, Waelde (2000) maintains that

Turkish insistence on this route does not look good considered from its own interest; the geopolitical advantage gained from providing the highest-cost pipeline which is also hostage to internal [external]insecurity is therefore highly debatable as well. It is therefore hard to see how this pipeline can materialize except if Turkey (or the US, or both) explicitly and formally assume both the high cost and the political risk. Such risk assumption might not be in Turkey’s interest (p.17).

Analysts say that despite numerous agreements, there have been few real signs of progress for the other US-backed plan – Trans-Caspian natural gas pipeline from

Turkmenistan to Turkey. This one also aimed at neutralizing Russian and Iranian influence in the region. This project also confronts many obstacles. From the point of view of geologists it is highly risky to construct a pipeline crossing the Caspian Sea, argued that the Caspian seabed is active and unstable, which would create additional difficulties and uncertainties for the investors. In addition, there is a problem of financing: the US Export-Import Bank officials have raised doubts about Turkmenistan's ability to service its debt, as under its charter, the bank may not provide financing or loan guarantees unless it has a reasonable assurance of being repaid (Lelyveld, 1999).

As time passes this project also would probably become uncompetitive and its realization questionable. Such conclusion becomes possible especially when there is increasing disagreements between Saparmurat Niyazov (Turkmenistan) and Heydar Aliyev (Azerbaijan) after the latter's suggestion, supported by the U.S., to split pipeline capacity evenly with Azerbaijan. Turkmenistan argues that Azerbaijan and also Georgia as transit countries can demand only the transit fees (one-sixth of planned volumes), but never a 50:50 split of quotas. Niyazov blamed John Wolf, U.S. special adviser on Caspian energy, for the exacerbating relations between former Soviet republics trying to dictate them what are their political interests in the region. Oil analysts say that Turkmenbashi's strictness is explained by the renewed agreement between Turkmenistan and Gazprom in 2000 (Gazprom buys Turkmen gas since 1996), according to which 50 billion cubic meters (bcm) of Turkmen gas will be pumped to Russia annually. The Turkmen economy is in a state, that time is not on Niyazov's hands, they maintain. It suffers from huge debts, high inflation rate, and wages are very low. Indeed, for Turkmenistan the outcome matters more than the pipelines through which its gas will reach world markets. So, under such conditions, it is probable that Turkmenistan will end with the project, preferring Russian routes and immediate revenues (Turkistan Newsletter, 2 March, 2000).

Trans-Caspian project's accomplishment became doubtful also after Russia's proposal of the "Blue Stream" project, which is already under construction, as this project, unlike others, does not face financing problems (Mediamax, Bulletin "Energonositeli", 22.02.2000). "Blue Stream" natural gas pipeline will cross Black Sea from Russia to Turkey through which each year 16 bcm of Russian gas will reach Turkish market. Russia and Turkey signed this intergovernmental agreement and contract in December 1997 (Mediamax, "Energonositeli", 01.03.2000). In fact, this project compared to other proposals is economically more acceptable for Turkey, and also politically for Russia, as it makes both Baku-Ceyhan and Trans-Caspian projects less attractive for Turkey and international oil companies in terms of economic costs and political risks. The important advantage of this project is that no third transit country is involved: the gas reaches to the consumers immediately from the supplier to the buyer.

In this respect it is more logical and therefore natural that international oil companies involved in the Caspian oil deals prefer to expand the existing pipelines and to pursue the inclusion of Iran in Caspian oil projects either by using Iranian soil for pipelines or by applying oil-swap program. The latter is more likely to be utilized by Iran in order to avoid US sanctions. Iran would export the same volume of its own Persian Gulf oil as it imported from Central Asia, but do so in the name of the Central Asian provider (Stratfor, 26 January, 2000). In addition, the southern route through Iran is seen by oil companies and European governments as the most practical export route for Caspian oil and gas for markets in the West.

The producing countries such as Kazakhstan and Turkmenistan also have not ruled out Iran. Iranian route for Kazakh oil would cost on \$600 million to \$800 million in contrast to \$2.8 billion of a pipeline crossing the Caspian Sea to Azerbaijan. Even the AIOC, with 40% American participation, proposed the option of a \$2 billion pipeline from its offshore fields to

the Persian Gulf, arguing that there could be big differences in the project costs and oil prices due to the turns of international politics (Marashian, 1998). High officials in Iran, such as Mehdi Hosseini, Deputy Minister for International Affairs, is sure that sooner or later regional countries will eventually turn to Iran in their oil and gas transfers to international markets and Iran will play its appropriate role (Turkistan Newsletter, 2 March, 2000).

All in all, in this phase Russia turns to be the winner in pipeline routes competition, as the proposals, promoted by the U.S. and Turkey with the aim to restrict Russian influence in the Caspian are still in the state of infancy with little chances to be completed in the future. In this respect Waelde (2000) makes a warning that “if a major pipeline project goes definitely sour for reasons of politics and insecurity then new project investment is unlikely to become available for quite some time again” (p.21). The evidence of politicization of pipelines was the opening of the Baku-Supsa route, which followed the military maneuvers training to defend the line by Ukrainian, Georgian and Azeri troops, acting as part of GUAM, and under the framework of NATO’s Partnership for Peace (Stratfor, June 15, 2000).

Russia counts achievements also in the legal status debate. In 1999 Russian President Vladimir Putin proposed a formula according to which the Caspian states would own the Caspian shores within their boundaries and the water and seabed resources would be owned by the littorals evenly. Kazakhstan sided with Russia in this issue, and in October 10, 2000 Nazarbayev and Putin confirmed their united position regarding the legal status of the Caspian Sea. Russia continues also negotiations with other littorals in order to come to agreement in the forthcoming Caspian Summit (Turkistan Newsletter, 14 October, 2000).

Oil Price

The other important factor determining the political arrangements and the behavior of international oil companies in the region is oil price. In fact, in the recent years there is instability in oil price in the global markets. There was recorded serious collapse of oil price in late 1998 and early 1999, when the oil price moved to very low levels (\$10 per barrel), with a subsequent upwards movement (to over \$15) (Waelde, 2000). According to specialists the cost structure for Caspian fundamentally differs from the North Sea and Persian Gulf. Two kinds of costs are taken into account in Caspian barrel, transportation (\$6.50/bl) and development drilling (\$3/bl), and fully built up Caspian Development Cost is estimated \$12/bl. For example, North Sea region is more favorable in terms of transportation (Adams, 2000). In the period of oil price slump there a decline was noticed in both flow of investments and interestedness of international oil companies to make new deals with regional governments. On one hand, energy companies were concerned about the high costs, on the other hand, low oil prices that had a major impact on all parts of their businesses, made their presence in the region unjustified. The withdrawal or paring down of operations of many oil companies partly was due to slumping prices in addition to the fact that Caspian oil reserve capacity was overestimated, which had already made questionable the necessity of MEP or any other new pipeline. In addition, the revenues that Caspian states collected was sufficient only to cover production costs (Lelyveld, 1998).

The calls for cuts of oil production by many oil producing countries to recover prices bore fruit. In March 1999 OPEC (Organization of Petroleum Exporting Countries) and four non-OPEC nations (Mexico, Russia, Norway, and Oman) agreed to cut output by 1.7 million and 400 000 barrels a day respectively. As a result of this consensus oil and gas prices run up roughly from \$10 to \$30 a barrel creating panic in the oil markets of the world (Samuelson, 2000). However, the stability in oil prices and at the same time the maintenance of high

prices toward which OPEC and other oil countries were seeking was hardly to be achieved especially when many oil countries such as Saudi Arabia and Mexico insisted that there is a need to reduce the prices. Some oil producers also agreed that high prices might result in the loss of consuming countries, as the latter would suffer from overcharging. So, the interests of consumers also should be accounted. Of course, high oil prices are in hand of oil companies and producing countries as their gains and revenues increase. However, oil economists think that the market is so tight that prices could rise from \$30 a barrel. The reason is that two thirds of the world's known oil reserves are in the Middle East, in a region with highly restrained and unpredictable politics. For example, Saddam Hussein could demand the end of economic sanctions against Iraq "because the world will need Iraq's oil to maintain price stability" (Samuelson, 2000, p.1). This is, of course, not in the interests of world oil majors, who seek stability in all parts of oil business.

In addition, high oil prices would make investors forget and put down high political and transit risk. This factor especially is important in the Caspian. On one hand high oil prices may again effect in new oil deals between oil companies and Caspian governments. On the other, the fluctuating oil prices do not allow for those projects with long-term construction phase to become feasible. The oil companies would rather utilize the existing routes to gain more profit from the high prices of oil without giving much attention to political aspects. In addition, the exporting of oil from politically unstable and dangerous region may face many obstacles, which would raise the costs the companies would pay. This makes Caspian very vulnerable in terms of confidence necessary for oil companies. Also the probability of restarting of regional conflicts especially in transit countries may question the continuation of projects in the Caspian despite high prices.

The high prices of oil resulted also in the strengthening of Russia's stance in the region. The first time after its independence, Russia was able to cut the budget deficit due to the

revenues from oil exports, and substantially reduce its dependence from outside powers and international financial organizations.

Although it is hard to predict the future of price development, OPEC foresees that in mid-2001 there is expected an abrupt fall in oil prices as it was in 1998. In this respect it is planning to cut off the volumes of oil production in order to avoid such a future. However, the oil-importing countries alert that the shortening of production volumes may result in international economic crisis (Radio Azatutyun, November 13, 2000). Yet in February, 2000, Oil Ministers of Gulf states declared about their intention to enlarge the oil production, if the increasing oil prices would threaten the world economic growth (Mediamax, 26.02.2000). In this case, if the prices would fall even not equal to 1998 standards the Caspian oil would become less competitive, as Caspian crude is not commercially competitive if oil price is below from \$15 per barrel (Adams, 2000).

VII. CONCLUSIONS: Implications to Armenia

For the last years Armenia has been advocating for complementary foreign policy in the Caucasus. Having this in mind the following thesis can be put forward: when there are no dividing lines of influence zones in the Caucasus and power relations are more balanced in the region, a more stable, peaceful, and secure political environment is created, which allows for a more efficient economic development. In addition, it should be stated that a balanced region is more conducive for cooperation among the Caucasus countries.

Based on the analysis of foreign policy development in the region, we see the noticeable changes in political environment for Armenia connected with the oil factor activeness. When the oil factor is active, political and economic developments for Armenia are unfavorable, and just the opposite, when the oil factor is passive Armenia more freely maneuvers in both regional and international political arena.

To study foreign policy developments of the Republic of Armenia two phases must be distinguished: 1. 1994-1997 – Oil Boom – flow of international oil companies to the region and large investments in Azerbaijan, and relative isolation or attempts to keep Armenia away from regional developments; and 2. 1997 - present times – Oil Boom Decline – characterized as a period of delayed investments and continuing withdrawal of especially American oil companies from non-economic pipeline projects, weakened Azerbaijani influence in NK conflict negotiations and diminished international significance. In this phase, Armenia, in contrast, more actively gets involved in the regional developments, is released from high political pressure from the West and the US in particular, on the Karabagh issue.

Armenia in TRACECA

Many cooperation programs have been initiated in the Caucasus during last decade by international organizations such as European Union. TRACECA and INOGATE are EU initiatives in the region for the restoration of the Historic Silk Road⁴. These projects envisage the establishment of multi-dimensional and multi-functional communications system with a purpose to support the newly independent countries of the Caucasus and Central Asia by helping them to upgrade and link their infrastructures. By funding new road, rail and ferry links in the region, the EU hopes to increase local trade, and, just as importantly, open an alternative transportation system to the existing Russian one. The perspective political goal of these programs is to weaken the dependence of Caucasian and Central Asian countries from Russia. The overall price of TRACECA is approximately 50 million ECU (MFA, Political Guide #1, 25.07.1998).

⁴ The abbreviation for TRACECA stands for Transport Corridor-Europe-Caucasus-Asia, and for INOGATE – Interstate Oil and Gas Transport to Europe. Both programs are implemented within the framework of TACIS (Technical Assistance to the Commonwealth of Independent States).

From the beginning Armenia has participated in projects within TRACECA⁵. However, Armenia considers that the main road bypasses Armenia, which creates isolated situation for Armenia in the region. The evidence of excluding Armenia from the processes was the decision to change the place of 1998 TRACECA Conference from Tbilisi to Baku. Moreover, initially, Armenia didn't receive an invitation. There was a noticeable intention to keep Armenia away from TRACECA projects as during the Baku Summit on September 9 1998, Azerbaijan and Turkey ensured that Armenia despite its formal membership would be excluded from most of the TRACECA projects. In addition, Azerbaijan signed TRACECA Basic Multilateral Agreement⁶ with provision according to which Azerbaijan will not participate in those initiatives within TRACECA where Armenia has a direct participation. Obviously, this provision contradicted to the principle of even participation of the project and to the international law⁷, and deepened Armenian isolation depriving the latter to participate on the maximum level (MFA, RA Foreign Policy Guide, June 2000).

Armenia participated in Baku conference of 1998 on a very high, Prime Minister's level, thus showing that the implementation of TRACECA is of great importance for Armenia. However, it believed that it is not the ideal system for the inclusion of regional states. "Armenia would like to see Iran as a party to the project, in the belief that this would convert Armenia from a "dead-end" into a transit state and thus promote solution of many economic problems" (Azer-press, 3 January, 2000). In addition, in the opinion of Vardan Oskanyan, the Minister of Foreign Affairs of Armenia, the involvement of Iran in TRACECA will provide the political balance in the region and would guarantee the setting up of the regional security

⁵ 1. The restoration of Karmir Blur terminal is accomplished within the TRACECA-Intermodal Terminal Equipment program, 2. Program for the provision of Tbilisi-Yerevan fibroptic link

⁶ The participant states of TRACECA Basic Multilateral Agreement are – Armenia, Azerbaijn, Georgia, Bulgaria, Kazakhstan, Kyrgyzstan, Moldova, Romania, Tajikistan, Turkey, Ukraine, and Uzbekistan. The agreement has already been approved by Azerbaijan, Georgia, Uzbekistan, Tajikistan, and Armenia (December 29, 1999).

⁷ Article 19-c of 1969 Convention on the Status of International Treaties prohibits to make a provision that contradicts the main purpose of the given treaty.

system which will enhance the role of Armenia as an axis state influencing such processes (ibid). In this connection, Armenia has several times raised the issue of developing not only an east-west transport corridor but also a north-south one, which cannot be done without including Russia and Iran in the project. Indeed, Armenia keeps working on this seeing the engagement policy as the only way for achieving balance and stability in the region. During the visit of the President of Bulgaria to Armenia, two Presidents discussed the possibility of establishing a transport connection from Iran through Armenia and Georgia to Bulgaria (Drumeva, 1999). Armenia seeks maximum participation in TRACECA and other programs, which would create more favorable ground for Nagorno-Karabagh conflict resolution.

Undoubtedly, the full participation in TRACECA has political and economic importance for the Republic of Armenia based on the following considerations:

- the full participation in TRACECA would stimulate the improvement of Armenian transportation and infrastructure system, and, thus, economic growth;
- the full participation in TRACECA would assist to the maintenance of long-term stability in the region and will exclude political and economic isolation of Armenia.

For this purpose Armenia proposes the restoration of Kars-Giumri-Tbilisi railroad⁸ within the framework of TRACECA. This project compared to the Turkish proposal about the construction of Kars-Tbilisi railroad, is economically more viable option. Moreover, Armenia should actively work in order to avoid the implementation of the Turkish proposal. Otherwise, Armenia will appear in isolation from transportation routes. For the long-term political stability efforts should be made to include Iran in EU projects implemented in the region, which would enhance the role of Armenia in the Caucasus.

The Importance of Section 907 for Armenian Foreign Policy-making

Since 1994, the US has also been interested in the reviving of the Historic Silk Road. The US as the promoter of multiplicity of energy sources strived to establish Eurasian energy and trade corridor thus keeping Russia and Iran out of regional influence (Baku-Ceyhan, Trans-Caspian pipelines). Within this policy objective, many attempts were made to repeal Section 907.

Section 907 is a part of Freedom Support Act passed by the US Congress on 1992⁹. It bans direct assistance from US government to the Azeri government until Azerbaijan ceases “all blockades and other offensive uses of force against Armenia and Nagorno Karabagh” (Freedom Support Act 1992). This achievement was due to the efforts of Armenian lobby in the US.

The significance of 907 is not only the fact that U.S. assistance to the Azerbaijan was restricted, but it also provided Armenia with a good card in NK conflict negotiations. However, parallel to the oil boom and more actively since 1996 great efforts were made in the Congress to abolish or at least mitigate Section 907. As a result, in 1996 a provision was passed which allowed the U.S. President to allocate humanitarian assistance to Azerbaijan. This permitted the U.S. government to partly bypass 907 and through non-governmental organizations support Azerbaijan. While Armenia and NK continued to remain in blockade, Azerbaijan received more than \$130mln of humanitarian assistance via NGOs (Save the Children, US World Food Program) and oil companies (Amoco, Unocal) (MFA, Political Guide #1, 22.06.98). The US, in fact, was committed to defend the interests of its oil companies in the Caspian rather than to oversee whether Azerbaijan continues economic blockade against Armenia and NK or not. So, the US President Administration applied much

⁸ Armenia proposed this project during TRACECA Intergovernmental Committee first meeting in Tbilisi held in March 10-11, 2000.

⁹ Full name: Freedom for Russia and Emerging Eurasian Democracies and Open Markets Support Act

pressure on the Congress regarding to Section 907. In 1998 on one hand the Administration's pressure, and on the other hand the efforts of strong oil lobby have resulted in the passage of additional provisions that more and more weakened Section 907. They allowed assistance to Azerbaijan if it would be directed to the activities supporting democratic reforms, arms non-proliferation programs. In addition, oil lobby achieved also the passage of provisions to allow for some government aid through the Overseas Private Investment Corporation (OPIC) and Trade and Development Agency (TDA), aimed at helping American companies doing business in Azerbaijan. The former insures oil companies against the risk they hold in the Caspian (Lacey, 2000).

Another attempt to repeal 907 was through the introduction of Silk Road Strategic Act in 1997 by Senator Sam Brownback. The third article of the Act stated about the necessity to abolish Section 907 of Freedom Support Act based on argument that its maintenance endangers the US Caspian policy implementation. Armenia announced about its disagreement on this Act. The then Armenian ambassador in the U.S. Rouben Shougarian in his meeting with Senator Brownback in March 19, 1999, stressed that in the absence of any progress toward lifting the blockade to waive 907 is unacceptable for Armenia. Armenia claimed that it would reward Azerbaijan for its intransigence by threatening NK negotiation process. Also, it would serve Azerbaijani policy to isolate Armenia from regional economic projects, such as TRACECA and BSEC (Black Sea Economic Cooperation) (Embassy of Armenia in the U.S., Political Document, March 24, 1998).

Facing tight position from both official Armenia and Armenian lobbyist organizations, 1999 Silk Road Bill was proposed by Congressman Doug Bereuter, who dropped the provision to repeal Section 907. On 2 August, 1999, the Bill was accepted by the House without any difficulty (Embassy of Armenia in the U.S., Political Document, 4 August, 1999). It is worth to mention that the discussions for a given year are held in previous year.

That is, 1999 Bill was discussed in 1998, and its results show the political tendencies of the year 1998.

So, despite these efforts from the strong American oil lobby and the U.S. Administration on behalf of Azerbaijan, the restrictions on aid remained in place and are still there. In addition, House-passed Foreign Operations Bill and increased the amount of monetary assistance allotted for Armenia during Fiscal year 2000 to approximately \$90 mln in contrast to \$48 mln for 1999. This is especially important if to take into account that overall funding for the Independent States account was reduced by \$66 mln from the previous year (Armenian Assembly of America, November 18, 1999).

To sum up, it is obvious that the maintenance of 907 is significant for the Republic of Armenia, as this achievement is due to the efforts of not only Armenian lobbyists, but also Armenian foreign policy-makers.

The retention of 907 must continue to remain on the agenda of Armenian foreign policy priorities, as it

- still is an important lever during Minsk process;
- strengthens Armenian positions during negotiations;
- does not favor to U.S.-Azerbaijani relations.

Due to the provisions allowing different kinds of assistance to Azerbaijan, the overall amount received is quite significant. But activities made by the pro-Azei powers against 907, prompts that the abolishment of 907 for Azerbaijan has political importance. Azerbaijan realizes that 907 will continue to be a serious obstacle if negotiations on NK will restart.

Armenia-GUAM Relations

In October 1998, in Strasbourg the Presidents of Georgia, Ukraine, Azerbaijan, and Moldova agreed upon the creation of an economic union (GUAM). These four states share common interests: first, they all have problem of territorial integrity. Abkhazia and South Ossetia in Georgia, NK in Azerbaijan, and Transdnestria in Moldova are de facto seceded autonomies, although the issue of Crimea in Ukraine is not sharp and is more narrowly expressed, no one can be sure about the future developments; second, they all resist any further strengthening of the CIS as Russia would naturally play a leading role in it, and seek their security and sovereignty problems solution through western security mechanisms – mainly NATO. In fact, GUAM acted as a counter mechanism to the CIS within the framework of the CIS. Some political analysts were sure that the creation of GUAM was pushed by the West, and particularly by the U.S. It had a purpose to split the CIS – by itself loose – unity, and perhaps more importantly, thus having weakened Russian influence to make easy the implementation of the U.S. pipeline policy¹⁰.

Naturally, the further development of GUAM was toward military cooperation, and in January, 1999, the Ministers of Defense of these states decided to form common peace-keeping forces for pipeline protection. At the same time they refused to participate in the CIS Treaty on Collective Security, then expanded to include Uzbekistan, and demonstrated strong will to embrace NATO in their territories¹¹. In this respect, “GUAM is attempting to act as a single entity in its relations with NATO in a so called ‘19+4’ formula” (Cornell, 1999, p.6). With the same enthusiasm they promote TRACECA and US backed oil and gas pipelines.

¹⁰ U.S. pipeline policy envisaged the construction of Baku-Ceyhan and Trans-Caspian strategically important pipelines, which totally cuts Russian presence in the Caspian.

¹¹ During the NATO anniversary summit in April, 1999, in Washington DC, the GUAM expanded to include Uzbekistan (GUUAM). GUUAM established a charter about military cooperation within the group and with NATO. Uzbekistan also refused to participate in the CIS Collective Security Treaty (Stratfor, June 15, 1999).

Armenia, as the only Russian ally in its southern flank, firstly, because of its unchanged pro-Russian predisposition, and secondly, because of the NK conflict automatically is excluded from GUAM's cooperation projects. The development of this bloc, actually, is not in favor of Armenia and threatens the implementation main objectives of the Armenian foreign policy in the region. However, some analysts think that the creation of GUAM was a primitive political "blackmail", which usually is used by those states or group of states, who realize some weakness of their position and through such "improvisation" try to get political dividends (Golts, 1999). The same source further maintains that NATO itself will not place its military bases in countries, which have not yet solved their territorial disputes with their neighbors (Georgia, Azerbaijan). At the same time NATO continues to be indifferent toward such speculations, as strengthening of GUUAM is in NATO's hand and may potentially play a role of counterbalance to Russia.

Anyway, Azeri officials do not reject their intention to use GUUAM for the regional isolation of Armenia. In its turn, Yerevan does not deny the possible threat to Armenia's security from the bloc. For this reason Armenia should

- pay special attention on its relations with GUUAM states and make maximum efforts to strengthen cooperation with them in order to neutralize Azerbaijan's influence and to prevent the possibility of Azerbaijan using the bloc against Armenia.

Many positive moves are already accomplished toward this goal on the level of bilateral cooperation with Ukraine, Moldova, and Georgia (MFA, Political Bulletin #25, 01.07. 1999).

- activate its involvement in other regional projects, such as BSEC, which would marginalize GUUAM's influence.

Call for Stability

One of the priorities of the Armenian foreign policy agenda is the creation of regional stability and security system. Armenia put forward this idea at the OSCE Summit in Istanbul, in 1999. Armenia proposes application of 3+3+2 formula, which involves three regional states (Armenia, Azerbaijan, Georgia), three neighbors (Russia, Iran, Turkey), and two outside major players (USA and EU). The concept behind the armenian proposal is that there is no regional organization which includes all the regional players in it and could bare thus served as a forum for the discussion and solution of political issues in the Caucasus.

To come up with the idea about the necessity to create such a pact several factors have been taken into account:

- first, based on the past experience of being pushed out from almost all the regional projects, Armenia considers such a system as an arena where it can behave evenly with other players;
- second, this comprehensive system may provide with more favorable conditions for solving regional conflicts and prevent the escalation of possible conflicts (Kurdish issue, North Caucasus);
- third, the region is explosive, as the continuous confrontation of interests among the regional actors can more and more deepen dividing lines and cause long-lasting instability.

At the Istanbul Summit other proposals on regional stability and security system were made as well: one by Azerbaijan, and other by Turkey. The latter supposed the establishment of security system under the aegis of OSCE, which automatically left Iran out. While Azerbaijan and Georgia backed the Turkish proposal, Armenia spoke against it. Additionally, in that case any system created will not be comprehensive as Iran has been and remains one

of its main strategic partners in the region. Moreover, Armenia excludes the possibility to achieve the above mentioned goals if any of these countries is not included.

All in all, the idea of creation of such a system was positively accepted by the participants of Istanbul Summit, as the necessity of regional stability and security system has already been mature. So, despite the differences in the approaches to such a forum between the countries on the issue, they all were ready to discuss the possibility of establishment of the system.

In recent months positive moves were made in this sphere. On the one hand, there is noticeable improvement in Americo-Iranian relations, on the other hand, Turkey and Azerbaijan manifest about the changes they have made in their approaches regarding Iran's participation in the pact.

EU, as an initiator of many programs in the region, also is interested in the establishment of regional stability and security system. Certain attempts were already undertaken to push the process forward. Under the EU sponsorship, a Task Force for the Caucasus created a document, A Stability Pact for the Caucasus, which is an attempt to introduce special approach on the regional security system. Despite all the shortcomings of the paper it is worth considering as it includes all eight countries proposed by Armenia.

All this positive moves make possible to promote Armenian version of Stability Pact, and, which is more important, to create favorable environment for dialogues between Armenia and Azerbaijan.

Implications to the Nagorno-Karabagh Conflict

The most stable in its foreign policy orientation after the breakup of the USSR was Armenia. Armenia considers Russia as its natural geopolitically strategic partner and signifies

the close ties established with Russia, and confirmed by strong military cooperation between two countries¹².

Although the pro-Russian line of Armenian foreign policy in political and security issues was clearly identified, Armenia saw the path of its economic development in European integration. In 1992, immediately after its independence, Armenia, together with the other CIS countries, became a member of the CSCE, later OSCE. Mr. Levon Ter-Petrossian, the first Armenian President, undertook the first steps to integrate the country more strongly into European structures, by starting the accession process into the Council of Europe. Moreover, 1996-1997 Ter-Petrossian foreign policy was dominated by the desire for Armenia to have the blockade lifted out and participate in the international transit for Azerbaijani oil export (Boulerian, 1999). To achieve the goal certain concessions should have been made, and particularly regarding the issue of NK. The illustration of the external political pressure by the Western countries and oil companies was the OSCE Chairman-in-Office (CiO) statement in Lisbon in 1996, which envisaged the phased resolution of the NK conflict, reiterating the territorial integrity of the Azerbaijan Republic, and conferring on NK high degree of self-rule (autonomy) within Azerbaijan. Armenia vetoed this statement. However, in September 1997 Ter-Petrossian announced about his readiness to accept the proposal presented with some amendments. This announcement conditioned the further internal developments within Armenia and resulted in the resignation of the President. “On February 3, 1998, at the highpoint of the pipeline negotiations, Ter-Petrossian was forced out of office for his lenient attitude in the Karabagh conflict” (Boulerian, 1999).

Although this historical turn threatened with growing isolation of Armenia, the international community eventually accepted that the winner in the war, Armenia, would not

¹² In 1997, August 29, a contract was signed between the RA and the RF about friendship, cooperation, and mutual assistance. The third article states that the parties should take all the means, including military, to fight

agree upon Azeri conditions. The loosening of the oil interest in the region contributed to substantial de-politicization of the whole process and creation of more balanced approach from the western countries to the resolution of the NK conflict. In the beginning Azeri tight position on NK issue was explained by the importance it gained in the international arena due to the oil boom. However, the following developments brought clarity in the real state of oil deposits in the Caspian, which steadily diminished Azerbaijan's significance in the world and mitigated its positions in the negotiation processes.

At present, the peace process is still in deadlock, yet the external pressure on Armenia has significantly weakened which was clearly demonstrated at the Istanbul Summit of the OSCE heads of states and governments. The declaration adopted at the summit called for the resumption of negotiation without putting preconditions unlike Lisbon.

The last proposal of the Minsk Group, presented in 1998, was on the "Common State." It has not been replaced with a new one despite Azerbaijan's rejection. In comparison to the previous proposal on phased resolution of the conflict, this one marked a significant change in the approaches of both the international community and the Minsk Group Co-Chair: the notion of autonomy to serve as the basis for the discussion of the political status for NK has been taken out from the proposal. Firstly, that meant that the international community has finally realized the unacceptability of the principles of the CiO statement at Lisbon for the resolution of the NK conflict, and, secondly, the international community firmly understood that no document signed on the resolution of the NK conflict could be fulfilled if it did not take into consideration the opinion of the Armenian people both in Armenia and Nagorno Karabagh and did not have their approval (MFA, RA Foreign Policy Guide, June, 2000).

In 1998 the Azerbaijani side continued to reject any discussion with the participation of the NK representatives and refused to take part in the hearings at the Parliamentary Assembly

against aggressions and threats endangering the peace of both countries.

of the Council of Europe on Nagorno Karabagh. Despite its efforts to stop the hearings, it took place in Paris in December 1998 with the participation of the Armenian and Karabagh delegations. Those hearings were very important as they provided an opportunity to present the Nagorno Karabagh issue in its entirety and the position and approaches of the Armenian side directly to the European community. As a result, the European Parliament adopted a resolution in March of 1999 in which it specifically stressed that Nagorno Karabagh had declared its independence in conformity with the existing legislation of the time and expressed its support for the MG last proposal (MFA, RA Foreign Policy Guide, June, 2000).

Overall the last two years registered some advancement in the NK peace process. It was the first time that Azerbaijan accepted the need for the resolution of the NK conflict on the basis of compromise. Also, the international community realized the importance of the resumption of negotiations without any preconditions. The Istanbul Summit declaration accepted this reality and by effacing the situation created after the Lisbon Summit opened the way for the resumption of negotiations.

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