ENERGY RESOURCES AND ENERGY POLICY

CASPIAN OIL IN THE REGIONAL ECONOMIC AND WORLD POLITICAL CONTEXTS

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In May 2005, a fairly pompous ceremony in Baku marked the filling of the Azeri stretch of the Baku-Tbilisi-Ceyhan pipeline (BTC) with oil. A lot of high flowing words were said as the oil reached Georgia and Turkey. In November, the wave approached the shores of the Mediterranean. Those who spoke at the final celebrations in Ceyhan were convinced that the pipeline would radically improve the economic and political situation of all the local countries, primarily Azerbaijan, Georgia, and Turkey, and would make them more stable and secure. After a while, however, the emotions aroused by the inflated expectations subsided under the pressure of more rational assessments of the geopolitical and regional changes brought about by the "project of the century."

Local Oil and Globalization American Style

The continued prosperity of America and the states of the "golden billion" depends on raw materials supplied by other countries, their own resources being fairly limited. This explains the zeal with which the United States and its allies are trying to gain access to the natural riches of others. The methods are well known: liberal reforms and privatization of state enterprises. This started back in the 1990s when the downfall of the Soviet Union triggered a re-division of the world. The struggle for non-renewable energy sources was rekindled, while its center shifted from the Middle East to the former Soviet republics on the Caspian shores.

The United States, however, has not abandoned its attempts to punish those Mid-Eastern oil producers who ignored the orders of the only superpower. In 2003, under flimsy pretexts, Britain and America declared a war on Iraq, one of the OPEC founders with a key role to play in price formation on the oil market. It was at the same time that the U.S. branded the Islamic Republic of Iran first a "rogue country" and then part of the "axis of evil" to toughen up American sanctions. In the 1990s, American oil companies gained access to Caspian oil as an alternative to Mid-Eastern oil and the oil produced by the OPEC countries.

The Caspian countries are no rivals of the Middle East when it comes to the amount of oil reserves: the Middle East is literally floating in oil. In the last decade of the 20th century, when Western firms first betrayed their interest in the oil of Azerbaijan, Kazakhstan, and Turkmenistan, the local media spoke of the great future of Caspian oil. Americans were talking about 10 billions tonnes of oil reserves (later, in 2000, they cited a figure of 30 billion). According to OPEC's estimates, the reserves were not more than 23 billion tonnes, while Russian experts agreed on a figure of 15 to 20 billion. Only 10 percent of the total oil reserves are concentrated in the Caspian; over 60 percent of the world's total oil riches are found in the Middle East. The Caspian stands no chance of becoming "another Persian Gulf."[1]

In fact, the United States and its NATO allies cherish the idea of opposing the Middle East with eventual additional amounts of oil to push down world oil prices. There are other no less attractive opportunities: while Mid-Eastern oil producers rely on state companies, the newly independent countries deprived of Moscow's support found themselves in dire straits. They all were only too glad to invite the oil giants to their oil markets and were seeking foreign investments in their oil and gas industries. The United States hastened to exploit the chance to declare the Caspian area and the Caucasus a sphere of its strategic interests; American companies, as well as companies of other imperialist states struck root in the local economies. More than that: the West and its companies did their best to squeeze out "imperialist Russia" from the Caspian, the Caucasus, and Central Asia.

The results were fairly modest: contrary to what Western ideologists and their Russian supporters were saying, the Soviet Union was not an empire. It never exploited the republics at its fringes; in fact, it supported them in all spheres—political, social, and economic—and supplied their economies with trained specialists. This explains why they did not hasten to sever trade, political, and cultural ties with Russia and turn to the West.

Still, for two reasons, those who wanted Russia out of these areas stood a good chance.

- First, ruined by the IMF-imposed liberal reforms, Russia could no longer support the former republics or maintain the active economic cooperation of the Soviet period.
- Second, neither the Yeltsin nor the Putin cabinets arrived at a clear and rational policy regarding the former Caucasian and Central Asian republics; the same was true of other post-Soviet states. Abandoned by Moscow, they followed the road of economic and political reorientation.

[1] See: *Azia i Afrika segodnia,* No. 12, 2001, p. 19; *Central Asia and the Caucasus,* No. 1 (25), 2004, p. 90.

Successes of Azerbaijan's Oil Sector

After declaring its independence in 1991, Azerbaijan aimed to develop its oil industry to earn money for other economic sectors. To achieve this, its president, Heydar Aliev, used the State Oil Company of the Azerbaijan Republic (SOCAR). Its obviously inadequate financial resources forced the country to adopt laws designed to attract transnational companies willing to invest in Azeri oil.

Soon after that, SOCAR announced the discovery of three promising oil fields in the Caspian (Azeri, Gunashli, and Chirag). In 1994, Azerbaijan signed the "contract of the century" with an international consortium of four American, one British, one Turkish, SOCAR, and some other firms[2] to develop the newly discovered oil fields. Still later, albeit smaller fields were discovered and transferred to foreign firms for development. In 2005, there were over 30 foreign companies working in the republic.

Gradually expert assessments of Azerbaijan's oil riches increased to reach, according to Russian experts, the figure of 3.5 to 5.6 billion tonnes.[3] Americans supplied an even higher figure of 10 billion tonnes.[4] In any case, the republic was rich in oil to be extracted by SOCAR and foreign firms. While in the first half of the 1990s oil production was declining, after a while it stabilized and began to grow: in 1980, Azerbaijan extracted 14.7 million tonnes of oil; in 1990, 12.5 million; in 1996, 9.1 million, in 1998, 11.4 million; and in 2003, 15.4 million. SOCAR produces over 50 percent of the total amount.[5]

After a while, in 2003, more oil fields were discovered; optimistic information appeared, both in Azerbaijan and abroad, that even more oil could be extracted, mainly on the Caspian shelf. In anticipation, American and other companies insisted on building an oil pipeline to the Mediterranean.

The Bottlenecks of the Azeri Oil Route

More oil meant more transportation options. At first small quantities of oil were moved by rail or by road to Batumi on the Black Sea coast of Georgia where oil was pumped to tankers and shipped to Turkey, or further on through the Black Sea straits. In 1993, a 926-km-long oil pipeline between Baku and Supsa (not far from Batumi) via Tbilisi made the task easier, yet the western route could move only relatively small quantities of oil. The problem called for a radical solution.

At first, Azerbaijan used the Russian 1,411-km-long pipeline between Baku and Novorossiisk via Grozny; after a while, in the mid-1990s, this became harder because Chechnia tried to appropriate the transit payments. Russia hastily replaced the stretch that crossed Chechnia with another pipeline outside the unstable republic to move the agreed amounts of oil along the Baku-Tikhoretsk-Novorossiisk route.[6] Azerbaijan exported about one-third of the total amount of the extracted 15-16 million tonnes of oil. The world, however, needed more—the country could meet these requirements.

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[2] See: I.S. Zonn, *Kaspiyskaia entsiklopedia,* Moscow, 2004, p. 233.
[3] See: Ibid., p. 24.
[4] See: *Neft Rossii,* No. 4, 2005, p. 39.
[5] See: *Bulletin OPEC,* Vienna, IX, 1997, p. 7; *Azia i Afrika segodnia,* No. 2, 1995, pp. 45-46.
[6] See: I.S. Zonn, op. cit., p. 273; *Azia i Afrika segodnia,* No. 2, 2005, p. 46.

The Baku-Tbilisi-Ceyhan pipeline is a brainchild of the United States and Turkey, which signed an agreement with Azerbaijan on its construction in 1993 in Ankara. In 1998, the presidents of Azerbaijan, Georgia, Kazakhstan, Turkey, and Uzbekistan signed a Declaration on Caspian Oil Supplies to the World Market. The U.S. Secretary of Energy put his signature under the document as well. The project, 1,730 km long with an annual capacity of 50 million tonnes of oil, was expected to cost $2.9 billion. The money was supplied by a consortium of eight of the largest oil companies eager to obtain an alternative oil transportation route. BP of Britain was the operator, while UNOCAL of the U.S., Statoil of Norway, Turkish Petroleum of Turkey, ENI of Italy, Total Finna Elf of France, Itochi Oil of Japan, Delta Hess of Saudi Arabia, and SOCAR were involved as participants. The project was launched in September 2002 at the Sangachal terminal to the south of Baku; it was expected to be completed by 2005.[7]

None of the oil companies of Russia, Kazakhstan, Turkmenistan, Georgia, or Uzbekistan, the countries interested in the new oil route, were among the participants. They refused to participate for different reasons: first, the shocking cost; second, some of the companies doubted there would be enough oil to move it along the new pipeline, which made the project a money-losing enterprise. Third, the pipeline was expected to cross fairly volatile regions: Azerbaijan and Georgia were resolved to use force to restore their territorial integrity; and Turkey was plagued by terrorist acts organized by the Kurdistan Workers' Party. (In the summer of 2005, Premier of Turkey Erdogan said to President George W. Bush that "in recent months his country has lost more soldiers killed by Kurds than America in Iraq."[8]) Russia expected its transit revenue to drop once the pipeline was commissioned.

Today, despite the celebrations in Ceyhan about the consortium, participants and experts from other countries are offering much more sober assessments of the project.

Winners and Losers

Russian and foreign experts believed that Azerbaijan would be the main winner and Russia would be left out in the cold as the main loser. A more detailed investigation, however, casts doubt on this. The users of Caspian oil are the main winners: the American, British, and other oil companies gained direct access to another source of oil and greatly increased their influence in the region.

As the supplier and transit country, Azerbaijan is totally satisfied: the high oil prices bring more money into the republic's coffers, yet the new pipeline is fractionally responsible for this. It will do nothing to improve living standards: oil transit will generate no more than $130 million a year, or $0.16 per capita per month.[9] The country expects to become the pipeline's only owner by the year 2025 by buying up the shares of all the other shareholders. It should be said that the pipeline's future depends on the three oil fields mentioned above (Azeri, Gunashli, and Chirag), which will yield 700 million tonnes of oil in the next 20 years (there will be about 200 million tonnes left). To become the pipeline's only owner, Azerbaijan will have to buy 75 percent of the shares of the consortium's participants, the real cost of which is about $3 billion; together with the credit interest, the figure will be $3.6 billion. Transit revenue will be negligible. This shows that the citizens of Azerbaijan are unlikely to enjoy the promised prosperity in 20 years' time.

In the first five years of the pipeline's functioning at its full capacity, Georgia will receive $0.12 per barrel; in the next 15 years, this figure will rise to $0.17; on average the country can count

[7] See: I.S. Zonn, op. cit., pp. 72-73.
[8] *Hurriyet,* 10 July, 2005.
[9] See: *Neft Rossii,* No. 7, 2005, p. 18 (the quoted calculations for the three countries have been made by Vl. Mishin).

on an annual income of $60-65 million (1.2 percent of its GDP for 2004, or about $1 per capita per month). This did not prevent Georgian President Mikhail Saakashvili from delivering an enthusiastic speech in Baku, in which he promised that BTC and the Baku-Tbilisi-Erzerum pipeline will create prosperity for all the countries of the region.[10]

Seen from Turkey, the prospects are not bright either: in the first five years the local tariffs will be $0.2 per barrel and will gradually increase to the $0.37 level, that is, $130 million a year. This will comprise 0.07 percent of the country's GDP for 2004, or $0.16 per capita per month, which is even lower than in Georgia.

These fairly modest incomes may become jeopardized if smooth transportation is disrupted. Experts do not exclude this, therefore the problem of guarding the pipeline has come to the fore. The choice is between the local security services and special units of the United States and its allies. In fact, there have been American troops stationed in Turkey for more than 50 years now; they have been present in Georgia for the last four years and may come to Azerbaijan (it should be said that the American army failed to reliably protect the Kirkuk-Ceyhan oil pipeline in Iraq). In this case, the United States would have strengthened its position in the Southern Caucasus and the Caspian area.

Georgia and Turkey will be hardly allowed to buy Azeri oil for prices lower than the world prices. In fact, the prices increased from $31 per barrel in 2003, when the project started, to $60 or even $70 in 2005, when the project was commissioned.[11] In any case, the price issue is not a monopoly of SOCAR—it belongs to all the companies involved.

I have already written that Azerbaijan produces over 15 million tonnes of oil, 33 percent of which it exports. To be profitable, the BTC pipeline should move at least 35 million tonnes, or 70 percent of its capacity. Being aware of this, the consortium is counting on oil from Kazakhstan and, to a much lesser extent, on Russian and Turkmenian oil.

Oil from Kazakhstan— A Chance of Survival

In 1990, under Soviet power, the republic produced 25.8 million tonnes of oil; at the dawn of its independence, in 1996, the country produced 22.9 million tonnes. It reached the old level of oil production (25.9 million tonnes) in 1998.[12] In 1993, when an international consortium was set up to develop the hydrocarbon potential of the republic's Caspian sector, geological prospecting and oil production were intensified. In 1997, a production sharing agreement was signed in the United States; some time later a consortium called Offshore Kazakhstan International Operating Company (OKIOC) was set up with the participation of Ajip (Italy), ExxonMobil (the U.S.), Shell (Dutch-British), Total Finna Elf (France), and others, which received certain economic privileges as investors.[13] The republic started developing shelf oil even before the Caspian states divided the sea. It turned out that Russia and Kazakhstan claimed the same two oil fields as their own and agreed to use them together on the 50:50 principle. Kazakhstan owned several large oil fields (Tengiz, Karachaganak, and Kulkol); in 2000, another large oil field was discovered in Eastern Kashagan (7 billion tonnes of oil of estimated reserves). Over 200 oil fields contained 4 billion tonnes of oil (on land) and 15 billion tonnes off-

[10] See: Ibid., p. 102.
[11] See: *Nezavisimaia gazeta,* 15 August, 2005.
[12] See: *Bulletin OPEC,* IX, 1999, p. 7.
[13] See: I.S. Zonn, op. cit., pp. 100-101.

shore. In terms of its proven reserves Kazakhstan is one of the first five oil-rich countries in the world (its reserves are larger than those of Azerbaijan).[14]

Foreign money helped Kazakhstan to bring up oil production to 58 million tonnes in 2004. According to national forecasts, by 2015 the country could increase oil production to 150-170 million tonnes by moving offshore. This will allow the country to become one of the ten largest oil producers[15] and to push aside most of the OPEC members.

To export its oil, the country used pipelines inherited from the Soviet Union: Atyrau-Orsk, Uzen-Aktau, and Uzen-Samara. In 1992, an international structure—the Caspian Pipeline Consortium (CPC)—was set up to build an oil pipeline from Tengiz to Novorossiisk (1,580 km long with a capacity of 67 million tonnes of oil a year. It will cost $2.3-2.4 billion). It was completed in 2001 and brought oil from Kazakhstan to the Black Sea. As soon as the oil terminal in Primorsk was completed, Moscow allowed Astana to use its pipeline which crosses the Baltic Sea.[16] Russia rented its tankers to Kazakhstan so that it could bring its oil to the Russian port in Makhachkala and in Enzeli in Iran. Later, Russia built more tankers, the first of which was transferred to Kazakhstan in 2004.[17] It was at the same time that Astana and Tehran agreed on the deliveries of Kazakh oil to Iran in exchange for an equal amount of south Iranian oil. The United States hastened to remind Kazakhstan that it considered Iran to be an "axis of evil" country and insisted on an economic blockade. The oil barter idea was dropped.

Simultaneously, the United States spared no effort to convince President Nazarbaev and his government to support the BTC project. Washington and Ankara forwarded the idea of an oil pipeline along the seabed from Atyrau to Baku. Russia and Iran actively objected to this. Moscow insisted that any leak might irretrievably damage the sea's biological resources (90 percent of the world's acipenserids live in the Caspian). Tehran pointed out that the Caspian states had not yet agreed on sea delimitation.[18] The project was shelved.

Even though Astana supports the idea of multivectoral transportation routes, it stayed away from funding the BTC project; later, it might reach an agreement on moving its oil along it and will send more of its oil by tankers to Baku. In view of the already achieved agreements and possibilities, however, Kazakhstan will have not enough oil for the BTC. The republic intends to sell part of its oil to China and even to Japan.

What the Other Caspian States Think of the BTC Pipeline

The members of the consortium want to know what Turkmenistan, Russia, and Iran think of the new pipeline: they count on Turkmenian oil.

Turkmenistan is rich in raw materials, primarily in hydrocarbon resources; according to Ashghabad, the Turkmenian part of the Caspian Sea contains from 3 to 12 billion tonnes of oil; and the reserves of natural gas are even greater.[19] These figures naturally attract foreign companies which have already started geological prospecting to specify the figures.

[14] See: I.S. Zonn, op. cit., p. 317; *Neft Rossii,* No. 3, 2005, p. 40.
[15] See: *Azia i Afrika segodnia,* No. 2, 2005, p. 48.
[16] See: I.S. Zonn, op. cit., pp. 2, 16, 217, 273.
[17] See: *Izvestia,* 14 December, 2004.
[18] See: *NG Sodruzhestvo,* 31 May, 2000.
[19] See: I.S. Zonn, op. cit., p. 368.

In the past, the republic relied on its railways to send oil to the central regions of the Soviet Union; President of independent Turkmenistan Niyazov is planning a single railway network to connect the country with Iran, Uzbekistan, Kyrgyzstan, Kazakhstan, and China. Late in the 1990s, the country acquired a railway stretch between Tejen and Mashhad in Iran, the larger part of it running across Iran.[20]

Sea transport is coming to the fore: the country first chartered and then bought tankers (the first of them was named after the president's father[21]) to move its oil to Makhachkala, from which oil is moved by pipeline to Novorossiisk. After a long interval caused by the conflict between Ashghabad and Baku over three offshore oilfields, the sea ferry resumed its functioning—it moves railway cars from Turkmenbashi (formerly Krasnovodsk) to Baku.

In fact, Ashghabad can send more oil to the BTC pipeline, yet President Niyazov concentrated on gas production and gas pipelines going to the west, to Europe via Iran and Turkey; to the south, to Pakistan and India via Afghanistan, and to the east, to China and Japan via the Turkic republics of Central Asia. This explains why oil-related projects are put on the back burner.

According to different estimates, Russia accounts for 6 to 10 percent of world oil production; its main oilfields are found in Eastern Siberia, and smaller ones are found in the Northern Caucasus and the Caspian area which use the pipeline leading to Novorossiisk. It was at the turn of the current millennium that Russia started developing its part of the Caspian shelf.

A multipurpose North Caspian Sea Steamship Line based on the oil tanker line Reydtanker founded in 1938 is operating in Astrakhan. It brings cargoes to the river ports of the Russian Federation and to the ports of the Caspian, Azov, and Black seas. Oil goes to the Novorossiisk pipeline.

Experts in Russia pointed out many times that the BTC project was too expensive, that it would require special protection, and that there would be not enough oil to load it to its capacity. These experts believed that the pipeline was unlikely to be profitable and maintained that it was built for political rather than economic purposes. The consortium examined the arguments and found them unconvincing.

Today the consortium and other interested companies are looking for more oil suppliers for their already commissioned pipeline. Naturally enough, they turned to Russia: there are plans to reverse the Baku-Tikhoretsk-Novorossiisk oil pipeline to move some of Russia's oil to Ceyhan. At the same time, groups of experts are trying to establish whether Kazakhstan would find it more profitable to use the Caspian stretch of the CPC to move its oil to Baku. So far, the Russian Transneft Company is ignoring these efforts, yet if enough oil is discovered in the Russian part of the Caspian shelf, the reverse variant might prove viable.

Iran has several hundred kilometers of the Caspian shore; in the post-Soviet period it suggested that the sea should be divided into equal parts (20 percent of the sea to each of the coastal states). Most of the newly sovereign states rejected the idea. Iran's uncompromising position does not allow the coastal states to divide the sea. Iran discovered large oil fields and even larger reserves of natural gas; every year it extracts over 200 million tones, according to OPEC quotas. Its main oil fields are found in the southern and central parts, therefore the country's north suffers from a lack of oil and oil products. (This explains why the country tried to realize the barter idea with Turkmenistan and Kazakhstan.) At the same time, the country has just started geological prospecting of its Caspian coast and shelf. When Azerbaijan announced a tender for developing the oilfields in the contested zone, Iran sent its military aircraft and warships there to scare the foreign companies away. Today, neither side dares to move close to the contested fields.

[20] See: *Persia* (Moscow), No. 1, 2000, p. 33.
[21] See: I.S. Zonn, op. cit., p. 340.

Iran would like to see Caspian and Central Asian oil moved across its territory to the Persian Gulf and to the Southeast Asian states, the most promising users of energy fuels, yet the American sanctions and warnings are keeping the pragmatically-minded countries away. In this way, Iran is deprived of the opportunity to use its geostrategic advantages to move oil along a vertical route. Iran will not use the BTC pipeline; this may happen, however, if large oil reserves are discovered in the south of the Caspian.

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The BTC pipeline serves the interests of most of the Caspian oil exporters, as well as of oil users in the West and Turkey. Azerbaijan, Georgia, and Turkey, the transit countries, may count on additional, albeit modest revenues.

This will happen if the pipeline is used to its maximum capacity—so far there is not enough Caspian oil to achieve this, therefore we can conclude that the pipeline serves political rather than economic aims. This is true primarily of the United States, which is resolved to build up its political, economic, and military control over the oil-rich areas in the Middle East, the Caucasus, and Central Asia.