

U.S. Caspian Policy Faces Fresh Challenges

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Brief Analysis

Turkmenistan president Saparmurad Niyazov today signed an agreement with Turkey's energy and natural resources minister, Ziya Aktash, to supply Turkmen natural gas to Turkey via a trans-Caspian pipeline. Later this month, work will begin on a much-delayed oil pipeline to carry oil from fields operated by a Chevron-led consortium in Kazakstan, a Caspian littoral state, across Russia, to a loading terminal on the Black Sea. And last month, during a visit to Washington by President Haidar Aliyev of Azerbaijan, Exxon and Mobil signed long-awaited agreements to look for oil in the waters of the Caspian Sea.

U.S. policy toward the Caucasus and Central Asia is predicated on the need to develop the large oil and natural gas reserves in the former Soviet republics -- and now independent states -- of Azerbaijan, Kazakstan, and Turkmenistan. (Azerbaijan has about as much proven oil as Canada, Kazakstan slightly more; Turkmenistan's strength is in gas -- it has almost as much as Algeria.) Washington wants to create, where possible, new export routes westward, to reduce dependence on Russia and to avoid alternative routes proposed through Iran. The goal is that a stream of revenues from oil and gas will further establish the independence of the new states of the Caucasus and Central Asian region.

But America's Caspian policy, which aims also to help neighboring Turkey and Georgia, could face serious challenges. Iranian and Russian opposition are smaller problems; the main difficulties are that the commercial basis of U.S. policy now seems ill-founded, nascent political institutions are weak, there are tensions about the Caspian boundaries, and Turkey has not yet clarified its energy policy.

Unclear Commercial Prospects. The recent months' activity may overstate the interest in the oil and gas reserves of the region. In fact, local geological challenges and the uncertain price of oil, combined with the need for long and therefore expensive pipeline routes, make the profitability of the region's hydrocarbons, in the minds of many industry experts, marginal at best. This year, two consortia of oil companies gave up their concession areas in Azeri waters in the Caspian because of a lack of commercially exploitable reserves.

Weak Political Institutions. The leaders of the three nominally Muslim countries each spent decades as communist apparatchiks during the Soviet era. To promote oil and gas deals in these countries, Washington has had to tolerate local limits on political participation and civil rights that in many other parts of the world it would deem

unacceptable. Perhaps the weakest political institutions are in Azerbaijan. After Aliyev's visit to Washington, the Azerbaijani leader made a surprise detour to Cleveland, Ohio, where he underwent quadruple heart bypass surgery. The operation on seventy-five year old Aliyev appears to have been successful, although it strains credulity to believe the remarks of his health minister that the Azeri leader's heart is now good for another fifty years. Back home in Azerbaijan, behind a faade of political stability, there is speculation about who might be Aliyev's successor. His son, Ilham, the senior vice president of the state oil company, is one apparent contender, but it is uncertain whether he wants the role. Haidar Aliyev's five years in office have witnessed the development of new oil fields, which replaced declining fields from Soviet-era exploitation, and the creation of a new oil route, through Georgia to the Black Sea, which supplemented an existing line running through the unstable Chechen region into Russia. But real oil wealth -- "a wall of money" -- still remains elusive. It is at least three years off and might never happen.

Caspian Territorial Tension. Turkmenistan contests Azeri notions of where their territorial waters meet. In March, President Niyazov, the self-styled Turkmenbashi (father of the Turkmens), made formal diplomatic complaints to the United States, Britain, and Turkey about their perceived support for the Azeri point of view. In April, two Turkmen helicopters buzzed an Azeri oil production platform. And Iran is pressing two European oil companies, Shell and Lasmco, to announce oil exploration deals next month, in waters that Azerbaijan considers belong to it -- potentially compounding the problem. U.S. cartographic experts are scheduled to arrive in the region soon to try to resolve differences over rival claims -- at least between Azerbaijan and Turkmenistan. A further awkward dimension is the legacy of the war in the early 1990s between Azerbaijan and Armenia. During the North Atlantic Treaty Organization (NATO) summit in Washington in April, Secretary of State Madeleine Albright brokered a public handshake between President Aliyev and his Armenian counterpart, Robert Kocharian. U.S. assistance to Azerbaijan is still limited by Congress because of the Azeri blockade on Armenia and the enclave of Nagorno-Karabakh. Perversely, Armenia has become dependent on Russian and Iranian aid. Earlier this year, Moscow heightened the tension by delivering S-300 long-range anti-aircraft missiles and MiG-29 fighters.

Turkey's Unclear Energy Policy. If enough oil is found in Azerbaijan, then a new route into Turkey will become a credible option. Ankara wants the oil to be directed through to the port of Ceyhan, on the Mediterranean coast close to Syria. The United States strongly supports the project, fearing that an alternative route would be via Iran, providing Tehran with another stream of hard currency revenue. But Turkish and Azeri teams negotiating on the details of the proposed oil pipeline are only making slow progress, even though the route would benefit both countries politically. Turkey is determined to avoid an increase of oil via the Black Sea that would then have to exit through the narrow Bosphorus Strait. There is no financial benefit from this traffic to Ankara -- the 1936 Montreux convention on the waterway allows free passage -- but there is a risk that a tanker accident would jeopardize Istanbul, which lies on the waterway. Experts say a traffic management system would considerably reduce the risk, but in the meantime Turkish officials doggedly push for the Ceyhan option.

The main problem with the Ceyhan route is expense -- it is the longest option. And whereas many parties seem to want it, nobody wants to pay for it. At the recent low level of oil prices, the high transit fees and production costs would result in little net revenues to the producing countries. The oil companies say the pipeline would not be commercial unless one million barrels a day of crude could flow through it -- and it remains debatable whether this level will ever be reached. Current Azeri exports are greater than 100,000 barrels a day, but these exports are adequately covered by one line through Georgia to the Black Sea coast and another northward into Russia -- although this passes through Chechnya and has been plagued by sabotage.

Ankara's arguments for the oil pipeline are based on avoiding the Bosphorus and building up Ceyhan as a Mediterranean entrepot for oil and refined products, but Turkey's main attraction for Caspian energy producers is as a consumer of natural gas. The Turkish economy seems to have an insatiable appetite for gas, both for domestic use

and industry. Two years ago, to the annoyance of Washington, Ankara announced plans to buy gas from Iran. Earlier this year, Turkey announced plans to buy Russian gas to be delivered via the planned "Blue Stream" pipeline under the Black Sea. (The seabed is so contaminated with Soviet-era environmental sludge, however, that the pipeline will have to be made of stainless steel. Cynics have thus dubbed the project "Blue Dream.") A further option under consideration is for Turkey to buy gas from fields in the Egyptian Nile delta. It already buys liquid natural gas from several sources. The fact that all of these different proposals are being seriously considered makes unclear the status of the deal signed today with Turkmenistan. Under that deal, a technically difficult pipeline would carry gas from fields in the eastern part of Turkmenistan under the Caspian, then via Azerbaijan and Georgia to Turkey.

Conclusions. During the past two months a film crew has been in Azerbaijan shooting scenes for a new James Bond movie. The plot, reportedly, involves a group of international villains seeking to destroy a Caspian oil pipeline on which the future of the world depends. Currently, the world does not depend on Caspian oil -- and it is never likely to, given that more than 97 percent lies elsewhere.

But the future of Caspian states does depend on energy exports. If oil discoveries continue to lag, dogged U.S. persistence on developing a new oil pipeline rather than on developing existing routes could saddle the nascent regimes with a crippling debt. Any sign of instability may be exploited by Russia from the north and Iran from the south. Perhaps more pressing than the future of the oil pipelines is the issue of the gas pipeline, as Turkey has not made clear how serious it is about the different primary supply sources from which it has pledged to purchase gas.

Simon Henderson, a former Washington Institute visiting fellow, writes about Middle Eastern energy issues from London.

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