

**CASPIAN ENERGY AND THE POLITICS OF CASPIAN STATES:  
KAZAKHSTAN AND TURKMENISTAN**

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## **EXECUTIVE SUMMARY**

The two littoral countries located on the east of the Caspian, Kazakhstan and Turkmenistan, desire oil and gas export routes that will maximize their political and economic strength at a crucial time in their history. Whatever the exact route, corruption, governmental control, centralization, and authoritarianism—all well in place in both Kazakhstan and Turkmenistan—will plague oil and gas development and transport. Unique obstacles face each country. For Kazakhstan, the obstacle is a possible civil war between north and south if economic prosperity does not come soon enough. For Turkmenistan, the obstacle is its corrupt, authoritarian, but nonetheless entrepreneurial leader—how he decides to appropriate oil and gas money will determine the future of the country. Despite its potential consequences, however, rapid construction of pipeline routes is in both Kazakhstan's and Turkmenistan's interest—without them, both countries are economically stagnant. Until oil and gas transport is underway, Kazakhstan and Turkmenistan will neglect developing themselves in other ways—the focus of both countries will be primarily on the politics and economics surrounding pipeline construction.

There are several export routes to be considered. Kazakhstan is naturally drawn toward a pipeline route through Russia with whom it shares a border and history, and also

by virtue of the six million ethnic Russians living in northern Kazakhstan. Turkmenistan is naturally drawn to a pipeline into Iran with whom it shares a border and a mutual interest in establishing a pragmatic, profitable relationship. For Kazakhstan, the main challenge is to find a pipeline route bypassing Russia in addition to the route through Russia currently being built. The additional export route would mitigate the unhealthy level of control Russia already has over economics and internal politics. For Turkmenistan, the main challenge is to find any export route to get its gas to Europe's markets—currently gas is being exported to delinquent customers such as Ukraine and Armenia.

## **CASPIAN ENERGY AND THE POLITICS OF CASPIAN STATES: KAZAKHSTAN AND TURKMENISTAN**

How Kazakhstan and Turkmenistan go about securing export routes for their oil and gas is a gamble of geopolitics and time. Their primary goal is to obtain an export route for their oil and gas reserves--in this sense, any export route is a good one. Second to that, the newly independent republics desire a route that will maximize their political and economic strength at a crucial time in their history. Which route is chosen will depend on the strategic interests of Russia, Iran, China, the United States, and Turkey—all pushing for one or another pipeline route.

Kazakhstan's and Turkmenistan's troubles, however do not end with the construction of pipeline routes. History has shown that "oil booms" can cause insurrection and a total collapse of the economy in countries without a progressive government and stable economy in place. The first part of this paper will delineate potential drawbacks to oil and gas development and why it should, nonetheless, continue. The second part of this paper will outline which pipeline routes are being considered and, from Kazakhstan and Turkmenistan's perspectives, the advantages and disadvantages to each.

## **Country Background**

Turkmenistan and Kazakhstan are located on the arid eastern shores of the Caspian. Kazakhstan, with a population of 16.9 million and size of 1,049,200 square miles (slightly less than four times the size of Texas), is bordered by Russia, Turkmenistan, Uzbekistan, Kyrgyzstan, and China. Turkmenistan, with a population of 4.7 million and a size of 188,455 square miles (slightly larger than California), is bordered by Iran and Kazakhstan. In Kazakhstan, Kazakhs make up only 37% of the population, the rest being primarily Russian.<sup>1</sup> For the most part, the Kazakh half is Muslim, while the Russian half is Russian Orthodox. In Turkmenistan, however, the population is primarily homogeneous—70% are Muslim Turkmen.<sup>2</sup>

Both countries' governments and economies have been largely shaped by their Soviet legacy. President Nazarbayev and President Niyazov were both Communist Party officials before they assumed the presidencies of Kazakhstan and Turkmenistan, respectively. Following the footsteps of the past, Nazarbayev has largely governed by decree and has extended his presidential term by referendum to the year 2000. Niyazov has created something of a "cult of personality" and has also extended his term by referendum to the year 2002. As with all of the former Soviet states, rampant inflation rates show that the economic situation of both countries deteriorated rapidly after independence. The International Monetary Fund (IMF) helped Kazakhstan reduce

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<sup>1</sup> Energy Information Administration, <http://www.eia.doe.gov/emeu/cabs/kazak.html>

<sup>2</sup> Energy Information Administration, <http://www.eia.doe.gov/emeu/cabs/turkmen.html>

inflation rates from over 2,000% in 1994 to 29% in 1996.<sup>3</sup> Turkmenistan, on the other hand, was much worse off. Inflation declined to 84% in 1997 from 10,000% in 1993.<sup>4</sup>

The Soviet legacy also left the newly independent states with a lack of adequate infrastructure. Prior to independence, their electricity, gas, and oil infrastructure was organized to serve the entire Soviet Union rather than the individual republics. The problem is especially apparent in Kazakhstan. Domestic electrical networks are linked to a Russian network in the north and a Central Asian one in the South. Gas producing areas in the west are unconnected to consuming areas in the populous southeast.<sup>5</sup>

Agriculture and energy are the two most important industries in the economies of both Kazakhstan and Turkmenistan. In Kazakhstan, the economy is regionally skewed—with virtually all heavy industry in the north, and agriculture predominating in the South. Mining (primarily of metals and coal) and oil production are the two most important industries. Important agricultural exports include grain, livestock, and wool. In Turkmenistan, the primary energy resource is gas. Apart from the gas industry, much of the economy is cotton-related.

Given that most of the land area is desert, both countries suffer from a lack of water. In Turkmenistan, water is only available at night and usually unfit for drinking.<sup>6</sup> The water crisis is furthered by the drying up of the Aral Sea due to a history of

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<sup>3</sup> Energy Information Administration, <http://www.eia.doe.gov/emeu/cabs/kazak.html>

<sup>4</sup> Energy Information Administration, <http://www.eia.doe.gov/emeu/cabs/turkmen.html>

<sup>5</sup> Energy Information Administration, <http://www.eia.doe.gov/emeu/cabs/kazak.html>

<sup>6</sup> Robert Ebel, *Energy Choices in the Near Abroad: the Haves and the Have-Nots* (Washington D.C.: CSIS, 1997), section on Turkmenistan.

ecologically unsound Soviet policies. Damage to the Aral Sea especially effects Kazakhstan's agricultural sector.<sup>7</sup>

The main challenge facing Kazakhstan and Turkmenistan today is to recover from the dire economic situations they found themselves in after independence. Both countries have turned to their oil and gas resources. Kazakhstan's primary hope is its oil resources, which come from three large onshore fields—Tengiz, Uzen, and Karachaganak. Turkmenistan's primary hope comes from its two largest gas basins—Amu-Dar'ya and Murbab.

### **Oil and Gas Development: Why it is Needed Despite the Consequences**

Oil and gas development does not come without its consequences. Venezuela, Trinidad and Tobago, Nigeria, and Mexico are just a few of the many countries that have undergone enormous strain--at times leading to the near collapse of the economy--at the hands of a much anticipated "oil boom." Only Norway can be cited as an example of a country where oil money has lead to long-term prosperity and stability. Unfortunately, the situations in Kazakhstan and Turkmenistan resemble the "failures" more closely than the "successes."

Whether or not oil and gas development qualifies as a "boom" depends on how fast the resources are developed. Given Kazakhstan and Turkemistan's unfettered focus on their energy industries and the willingness of foreign investors, the speed with which

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<sup>7</sup> Robert Ebel, *Energy Choices in the Near Abroad: the Haves and the Have-Nots* (Washington D.C.: CSIS, 1997), section on Kazakhstan.



pipelines are built will be the limiting factor determining the rate of oil and gas development. One has to consider, then, effects of both rapid and delayed construction of pipelines on Kazakhstan and Turkmenistan. Rapid development of the oil industry is unfavorable because it would increase already strong trends of corruption, centralization, and authoritarianism. At the same time, delayed construction is also unfavorable because economic hardship is a reality. Moreover, until oil and gas transport is underway, both countries will focus entirely on the politics and economics surrounding pipeline construction and neglect the development of other areas of their economies.

### **Rapid Development of the Oil and Gas Industry**

The Nitze School of Advanced International Studies (SAIS) is currently studying "shock therapy"--the effect that sudden wealth generated by one sector of the economy has on the development of a country. In a paper entitled "Being Rich Will Not be Enough," Fredrick Starr of SAIS notes among other factors, four ways in which Kazakhstan and Turkmenistan are not ready for oil and gas development:<sup>8</sup>

- \*Corruption within the structure of government and society
- \*Lack of progress in privatization and de-centralization
- \*Authoritarianism in government
- \*A tendency toward extravagant public projects

Oil and gas development intensify the negative effects of these four trends on government, economy, and society. Unless these trends are at least in the process of being

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<sup>8</sup> Fredrick Starr, "Being rich will not be enough: oil and policy in Central Asia and the Caucasus," *Central Asia Institute Briefing Paper*

addressed before oil and gas development is underway, Kazakhstan and Turkmenistan will face many challenges in the future.

### Corruption

Development of the oil and gas industries will increase corruption by increasing the flow of revenue into Kazakhstan and Turkmenistan. Those with power and special connections will profit off of greater revenues, while little will trickle down to the rest of the population. This would create even greater dichotomies between the rich and poor. Because of its inherent dishonesty and secretiveness, increased corruption would also increase disorder in society and government.

Corruption has two facets: 1) methods by which those in power stay in power and 2) ways for individuals to profit through contacts with the right people. In both senses, corruption is a fact of life in the post-Soviet states. Azerbaijan, Kazakhstan, and Russia were ranked among the most corrupt of post-Soviet states in a recent study.<sup>9</sup> Turkmenistan was probably left out only by default--the vice-like hold that Niyazov exercises on the country thwarts freewheeling corruption.

In Kazakhstan, both types of corruption are already evident in the energy industry. The first type of corruption is evident in the way new employment opportunities created by oil development are distributed. Chevron admits, "There are no employment agencies.

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<sup>9</sup> Elshan Alekbreov, "Despite political obstacles, energy work progresses around Caspian Sea," *Oil and Gas Journal*, June 15, 1998, pg.38.

The major way we identify potential new employees is word-of-mouth.”<sup>10</sup> Consequently, the communist old guard effectively chooses whom benefits by oil industry development. The second type of corruption is also evident. Individuals out to make a profit and oil companies looking to claim a stake have made secret deals. The British Trans-World Corporation was able to take temporary control of some of Kazakhstan's largest metal plants because of the company's "special relationship" with former Kazakhstan minister and then Russian first deputy Prime Minister, Oleg Soskovets.<sup>11</sup>

Under the leadership of Nazarbayev, Kazakhstan has taken measures to stem corruption. Nazarbayev has reportedly stated that "anyone taking bribes is considered an opponent of the president's policy." Moreover, a draft anti-corruption law being discussed in Parliament is expected to become law by this spring.<sup>12</sup> The nature of reform, however, is slow and will probably not be able to keep pace with the development of the oil industry. When they come, the pipelines will present an incentive to halt the process of reform too glittering to refuse.

Corruption in Turkmenistan is not as evident as in Kazakhstan primarily because of Niyazov's strong hold on society. Niyazov himself, however, clearly maintains power through corrupt means. The other style of corruption--based on individual profit--probably occurred frequently in the early period of energy development. Around 1991, Turkmenistan auctioned off oil and gas fields for as little as \$100,000 to customers such as

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<sup>10</sup> Frank Viviano, "Fuel for Discontent," *San Francisco Chronicle*, pg.A1.

<sup>11</sup> Martha Brill Olcott, "The Caspian's False Promise," *Foreign Policy*, Summer 1998, pg.98.

<sup>12</sup> Elshan Alekbreov, "Despite political obstacles, energy work progresses around Caspian Sea," *Oil and Gas Journal*, June 15, 1998, pg.38.

a Dubai car salesman, Swedish real-estate magnate, and a Lebanese American entrepreneur.<sup>13</sup>

### Governmental Control and Centralization

According to Starr, oil and gas development leads to increased governmental control because it involves primarily foreign trade; it leads to centralization because the production and transport of oil and gas are large-scale operations. Traditions of governmental control and centralization are already strong in Kazakhstan and Turkmenistan--oil and gas money will further stifle their societies and economies. High levels of governmental control and centralization push away much-needed foreign investors who wish to oversee operations in which they have a stake.

One measure of how ready Kazakhstan and Turkmenistan are to accept the governmental control and centralization that oil and gas development bring is their dedication to privatizing the economy, especially in regards to the energy sector. Unfortunately, they are both far from a well-developed program.

In Kazakhstan, attempts have been made to privatize the oil and gas industry. In February of 1998, however, they were temporarily put on hold in order to choose a "strategic partner" for the national oil and gas company, Kazakhoil, which holds state-owned shares in all joint ventures the government has signed.<sup>14</sup> Significant steps towards

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<sup>13</sup> David B. Ottaway and Dan Morgan, "In Drawing a Route, Bad Blood Flows: Varying agendas bear on routes," *Washington Post*, October 11, 1998.

<sup>14</sup> Sharon Behn, "Kazakhstan halts oil-sector privatizations, choosing to wait for Kazakhoil partner," *Platt's Oilgram News*, February 13, 1998, Vol.76, No.30, pg.3.

privatization, however, may have already taken place. According to Vice-President Balgimbayev, many of the country's main oil interests have already been privatized. Yet, the statement should be weighed carefully as Balgimbayev is reportedly "not a fan of privatization."<sup>15</sup>

In Turkmenistan, prospects for privatizing the oil and gas sector are non-existent. Every cent of oil and gas revenues will go into a state fund controlled by Niyazov and his advisers. According to one government official, "As the president pointed out, at the present time, it's most important that all the earnings from the industry should be concentrated in one place."<sup>16</sup> The government also reserves the right to interfere in oil and gas projects whenever it chooses, creating major conflicts for gas companies willing to invest. Currently, Argentina Bidas has three claims against the Turkmen government in international arbitration. One claims government interference with a gas field joint venture and another claims that the government owes the company \$50-mil for oil delivered to a state-owned refinery.<sup>17</sup> Evidently, governmental control and centralization will hamper foreign investment in Turkmenistan.

There is, however, one way in which further oil and gas development will lead to more progressive policies in the region--through the infusion of market-oriented thought into the government. In order to attract oil companies, both Nazarbayev and Niyazov have appointed younger, English-speaking businessmen to government. In Kazakhstan,

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<sup>15</sup> Ibid.

<sup>16</sup> Frank Viviano, "Black Gold, Iron Rule: Caspian nations bank on autocratic regimes to ride out oil boom," *San Francisco Chronicle*, August 13, 1998, pg.A1.

<sup>17</sup> Jane Upperton, "Bigger turnout, but still wariness, in Turkmenistan," *Platt's Oilgram News*, March 13, 1998, Vol. 76, no.49, pg.1.

Nazarbayev fired the head of Kazakoil and the Minister of Energy, Industry and Trade, replacing them with "New Kazakhs"—Kazakhs who grew up with visions of transforming Kazakhstan into another Kuwait.<sup>18</sup> In Turkmenistan, Kurbanov, who holds five senior government posts, is said to be a "breath of fresh-air" by oil and gas company executives because of his attempts to reach out to their needs. He makes the executives more confident that their incentives to invest will not be crushed under the weight of governmental control. One observer claims that "if he keeps Niyazov's support, it really could mean changes are on the way."<sup>19</sup>

### Authoritarianism

Oil and gas development cause increased governmental control and centralization. In turn, these increase the tendency towards authoritarianism, already well in place in Turkmenistan, and to some extent, Kazakhstan. Niyazov's "cult of personality" approaches that of medieval kings--his preferred name, "Turkmenbashi" (the leader of all Turkmen), is on everything from the airport to yogurt in a grocery store.<sup>20</sup> Nazarbäev, although he has paid attention to privatization and begun corruption reform, shows

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<sup>18</sup>Elshan Alekbrev, "Despite political obstacles, energy work progresses around Caspian Sea," *Oil and Gas Journal*, June 15, 1998, pg.38.

<sup>19</sup> Jane Upperton, "Russia and the Republics," *Platt's Oilgram News*, March 16, 1998, Vol.76, No.50, pg.3.

<sup>20</sup>Elshan Alekbrev, "Despite political obstacles, energy work progresses around Caspian Sea," *Oil and Gas Journal*, June 15, 1998, pg.38.

ambivalence to democratic institutions--he extended his presidential term through referendum and dissolved parliament after the 1994 parliamentary elections.<sup>21</sup>

### Tendency for Extravagant Projects

Oil and gas development could increase the government's tendency to spend money on extravagant projects. According to Starr, "It is human nature for a government that has benefited from windfall profits to want to celebrate its new prosperity with public works projects that impress and delight the domestic public as well as visitors from abroad." In the case of Kazakhstan and Turkmenistan, the fear is that such glamorous projects will have little to do with bettering the situation of its citizens. Niyazov is more concerned with how the Academy of Sciences looks like than with what it teaches.<sup>22</sup> Nazarbayev is spending billions of dollars to turn the provincial town of Akmola into a "model twenty-first century" capital.<sup>23</sup>

### **Delaying Oil and Gas Development**

While the pace of oil development in the Caucasus poses risks, it cannot happen too slowly because of the realities of economic hardship. In Turkmenistan, the average monthly wage in 1996 was thirteen dollars.<sup>24</sup> In Kazakhstan, 75% of those surveyed in

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<sup>21</sup>Martha Brill Olcott, *Central Asia's New States: Independence, Foreign Policy, and Regional Security*, (Washington, D.C.: United States Institute of Peace Press, 1996), p.84.

<sup>22</sup> Martha Brill Olcott, "The Caspian's False Promise," *Foreign Policy*, Summer 1998, pg.106.

<sup>23</sup> Ibid.

<sup>24</sup> Frank Viviano, "Black Gold, Iron Rule: Caspian nations bank on autocratic regimes to ride out oil boom," *San Francisco Chronicle*, August 13, 1998, pg.A1.

1995 purchased no consumer goods at all the previous year.<sup>25</sup> If economic hardship were the only factor, an argument can be made for expediting the process of finding and building export routes. Economic hardship, however, takes an especially severe form when considering the psychology of expectation—the anticipation of riches to come make the realities of the present day that much harder to bear. Another dimension is present in Kazakhstan, where ethnic tensions already exist and could escalate if prosperity does not come soon.

In many respects, the situations of Kazakhstan and Turkmenistan are dire. As evident from rampant inflation rates, the disintegration of the Soviet military-industrial complex has had "severe economic consequences."<sup>26</sup> The prideful, extensive public education system of Soviet times is breaking down. The cost of living is rising while pensions go unpaid. Health care is rapidly deteriorating--previously well serviced urban areas are fighting water contamination and other unsanitary conditions helping to spread cholera, hepatitis, and typhus. Ironically, energy shortages have become worse--Turkmenistan has regular power outages.<sup>27</sup> A telling statistic is that half of all emigrants from Kazakhstan go to Russia, where prices are two to three times lower and salaries at least twice as high.<sup>28</sup> One fear is that, under this kind of pressure to keep afloat, the countries of the Caspian may turn more and more towards drug trafficking. Currently,

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<sup>25</sup> Martha Brill Olcott, *Central Asia's New States: Independence, Foreign Policy, and Regional Security*, (Washington, D.C.: United States Institute of Peace Press, 1996), p.68.

<sup>26</sup> Martha Brill Olcott, "The Caspian's False Promise," *Foreign Policy*, Summer 1998, pg. 104.

<sup>27</sup> Ibid.

<sup>28</sup> Nurlan Amrekulov, "Inter-ethnic conflict and resolution in Kazakhstan," in Roald Z. Sagdeev and Susan Eisenhower, eds. *Central Asia: Conflict, Resolution, and Change* (Chevy Chase, Maryland: CPSS Press, 1995).



opium and heroin from Afghanistan are entering Turkmenistan, while illegal opium production is increasing in Kazakhstan.<sup>29</sup>

By the dreariness of the statistics, it may seem that the people of Kazakhstan and Turkmenistan have little hope for the future. However, for those that are not the "poorest of the poor," the disintegration of the Soviet structure has opened up new avenues for building careers. Moreover, the nascence of the countries leads the young to speculate how their lives will be different from their parents. Compounded with the prospect of oil and gas development, their visions of the future have become quite hopeful. According to a young student at the private Western University in Baku, "Our generation believes we will all be rich eventually. Look at Kuwait: Nothing but oil, no other product in their economy, and everyone has big cars and villas."<sup>30</sup> The fact that Niyazov also promises "another Kuwait" only increases expectations. Once the oil boom has come, these expectations may lead to increased social unrest, with people grabbing at whatever they can get their hands on. However, according to the author of the Anatomy of a Revolution, "Social firestorms are more often ignited by rising--but frustrated--expectations."<sup>31</sup>

In the case of Kazakhstan, firestorms between Kazakhs and the large minority of Russians are brewing and await only a threshold level of dissatisfaction to ignite them. Several nationalist groups already exist. One example is the group Unity, formed by

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<sup>29</sup> Martha Brill Olcott, "The Caspian's False Promise," *Foreign Policy*, Summer 1998, pg. 110.

<sup>30</sup> Frank Viviano, "Fuel For Discontent: Oil bonanza primes pump for social upheaval," *San Francisco Chronicle*, August 12, 1998.

<sup>31</sup> Ibid.

Russian members of the local government in Almaty (the former capital). Others include the legally sanctioned LAD and Slava Russian nationalist groups.<sup>32</sup> Existing grievances of the Russians are the state policy on citizenship, privatization, and language—they desire dual citizenship with Russia, a privatization policy that does not favor Kazakhs, and that the official state language be Russian.<sup>33</sup> When President Nazarbayev moved the capitol from Almaty to Akmola, further north, Russians there reacted negatively, perceiving the move as a spread of Kazakh influence.<sup>34</sup>

When Nazarbayev asked parliament to address the grievances of the Russian north, the Kazakh nomenklatura in parliament refused.<sup>35</sup> This suggests that whoever takes over after President Nazarbayev will probably be either pro-Russian or pro-Kazakh.<sup>36</sup> The only way, then, to guarantee the long-term political stability of Kazakhstan is through economic prosperity high enough to preserve the status quo. Therefore, the future of Kazakhstan, to some extent, depends on how much Nazarbayev manages to accomplish in the realm of pipelines while in power.

Social upheaval between Kazakhs and Russians could result in one or another, almost equally disastrous, outcomes. Either there is a civil war and the north secedes or Russians emigrate en masse out of Northern Kazakhstan. In the first case, Kazakhstan

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<sup>32</sup> Martha Brill Olcott, *Central Asia's New States: Independence, Foreign Policy, and Regional Security*, (Washington, D.C.: United States Institute of Peace Press, 1996), p.68.

<sup>33</sup> Nurlan Amrelkulov, "Inter-ethnic conflict and resolution in Kazakhstan," in Roald Z. Sagdeev and Susan Eisenhower, eds. *Central Asia's New States: Independence, Foreign Policy, and Regional Security*, (Chevy Chase, Maryland: CPSS Press, 1995), pg. 167.

<sup>34</sup> Richard R. Dion, "How oil, gas investment prospects compare for Azerbaijan, Kazakhstan," *Oil and Gas Journal*, July 28, 1997, pg.25.

<sup>35</sup> Ibid, pg. 168.

loses a part of its territory, inclusive of a large number of oil and gas producing factories. In the second, Kazakhstan loses a large portion of its skilled and professional workers. Even today, Kazakhstan is facing a dilemma as Russians leave, selling their talent in more receptive markets.<sup>37</sup>

In regards to the Russian minority, there is one way in which slower development of the oil and gas industry is favourable. Currently, Russians constitute a majority in cities, while Kazakhs constitute a majority in villages.<sup>38</sup> An oil boom would create opportunities for Kazakh farmers to work in city factories. A delay in the development of oil would allow for a more natural, slower integration.

Taken all together, there are strong arguments for proceeding with pipelines as fast as possible despite the consequences. All point to the fact that Kazakhstan and Turkmenistan's economic and political outlook depends on how and when pipelines become operational. According to Julia Nanay, "Without these pipelines, the countries of this region are economically stagnant.... Rapid construction of pipelines is the most critical element for the Caspian's economic and political development."<sup>39</sup> While everybody else involved in Caspian energy--Iran, Russia, Turkey, China, the United States, and the oil companies--can afford the luxury of waiting until a route that serves their interests surfaces, Kazakhstan and Turkmenistan cannot. Both countries have major challenges to

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<sup>36</sup> Martha Brill Olcott, *Central Asia's New States: Independence, Foreign Policy, and Regional Security*, (Washington, D.C.: United States Institute of Peace Press, 1996), p.85.

<sup>37</sup> Ibid, pg.62.

<sup>38</sup> Nurlan Amrelkulov, "Inter-ethnic conflict and resolution in Kazakhstan," in Roald Z. Sagdeev and Susan Eisenhower, eds. *Central Asia's New States: Independence, Foreign Policy, and Regional Security*, (Chevy Chase, Maryland: CPSS Press, 1995), pg. 164.

face once the pipelines are built. In many ways, they are not ready to meet them.

However, the state of limbo they are in right now is not helping to prepare them.

Overriding trends of corruption, centralization, authoritarianism, and extravagance plague oil development. At the same time, economic hardship is a reality--the money that oil and gas development brings is much anticipated. Kazakhstan and Turkmenistan, then, are both confronted by the same challenge—to find a way to integrate oil and gas money while ensuring their future economic and political stability. However, the obstacles to meeting that challenge differ. For Kazakhstan, possible division between North and South is the most pressing concern. President Nazarbayev's position is much like Tito's was in Yugoslavia after WWII--he has the task of introducing economic progress before ethnic tensions become too great. For Turkmenistan, the most pressing concern is its corrupt, authoritarian, but nonetheless entrepreneurial leader. How he decides to appropriate oil and gas money will determine the future of the country.

### **Pipeline Politics**

Kazakhstan and Turkmenistan are different from countries such as Venezuela, Trinidad and Tobago, Mexico, and Nigeria in that their political outlook, as well as their economic outlook, is intricately intertwined with oil and gas development. Russia, Iran, Turkey, the United States, and China all have their own strategic interests in one or

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<sup>39</sup> Julia Nanay, "Prepared Statement on Caspian Oil Basin and Gas Developments," *The Petroleum Finance Company*, May 6, 1998, pg. 8.

another pipeline route. For Russia, Iran, and Turkey, securing transit routes through their territory means revenue from tariffs and control over much vied for commodities. For the United States and China, easy access to gas and oil reserves depends on securing the appropriate export route. The politics of pipelines, then, will determine Kazakhstan's and Turkmenistan's future allies.

Each of the possible routes have their own disadvantages and advantages in light of Kazakhstan's and Turkmenistan's two primary goals: economic growth and political independence. For both countries, Russia is a dominant force and a potential obstacle to obtaining their goals. In Kazakhstan's case, strong ties to Russia will mean that at least one route must go through Russian territory. In order to assert its political and economic independence, Kazakhstan will have to look for additional routes through Iran and Turkey. In Turkmenistan's case, recent differences with Russia leave the country with no available export routes. Turkmenistan, then, is looking for any possible outlet for its gas.

### **Kazakhstan**

To date, most of Kazakhstan's oil exports have been delivered to the Near Abroad, with imports to Russia by far the largest share. Exports to Russia are dedicated to a swap agreement. Since two of Kazakhstan's oil refineries on the east are far removed from the centers of oil production, they import oil from Russia in exchange for Kazakh oil delivered at Smyrna.<sup>40</sup> In the near abroad, major importers of Kazakh oil are the Ukraine, the Baltics, and Azerbaijan. The pipeline from Atqau, Kazakhstan to a refining facility in

Samara, Russia is the primary method of transport—as of 1996, it moved forty percent of Tengiz crude oil.<sup>41</sup>

The drawbacks to Russian export routes are the limited capacity of Russia's Glavtransneft (pipeline network in Russia) and Russia's total control over deliveries and tariffs. Kazakhstan's quota for access to pipelines leading to the port of Novorossisk on the Black Sea is just 76,000 barrels per day (b/d).<sup>42</sup> Tengiz oil using the Samara line competes with oil brought in from Siberia and is subject to intermittent cut-off.<sup>43</sup>

Fortunately, Chevron, who manages transport from the Tengiz fields, has found export routes that bypass Russia. Today, oil is being barged from Atqau, Kazakhstan to Baku, Azerbaijan and then sent by rail to the Black Sea terminal Batumi, Georgia. Rail shipments to China were begun in November 1997. Together, exports to Russia and the Baltics, Batumi, and China, exceed 170,000 b/d.<sup>44</sup>

Kazakhstan has also been the first to venture in oil swaps with Iran, an indication of its desire to explore export routes outside of Russia. The swap contract currently in place allows for 120,000 b/d via this southern route.<sup>45</sup>

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<sup>40</sup> Robert Ebel, *Energy Choices in the Near Abroad: the Haves and the Have-Nots* (Washington D.C.: CSIS, 1997), pg. 75.

<sup>41</sup> Robert Ebel, *Energy Choices in the Near Abroad: the Haves and the Have-Nots* (Washington D.C.: CSIS, 1997), pg. 73.

<sup>42</sup> Ibid.

<sup>43</sup> Interview with Ms. Epinger at the Caspian Policy Division of the State Department, November 2, 1998.

<sup>44</sup> Julia Nanay, "Prepared Statement on Caspian Oil Basin and Gas Developments," *The Petroleum Finance Company*, May 6, 1998, pg. 2.

<sup>45</sup> Ibid., pg.3.

### Caspian Pipeline Consortium

The Caspian Pipeline Consortium (CPC) represents the one route from Kazakhstan that would go through Russia. Begun by Russia, Kazakhstan, and Oman and later joined by Chevron, it is scheduled to complete a 940 mile pipeline with an initial capacity of 560,000 b/d running from the Tengiz field to Russia's Black Sea terminal at Novorossiisk by 2001.<sup>46</sup> The primary obstacle to pipeline construction has been securing rights-of-way—legal documents allowing pipeline construction through Russian territory. Recently, the consortium has secured local permits, and is currently waiting for a federal permit from the Russian Government.<sup>47</sup>

Kazakhstan's chief concern with the CPC pipeline to Novorossiysk is maintaining a balanced relationship with Russia. There are two factors that necessitate a relationship with Russia: 1) common economic and security ties and 2) a minority of six million ethnic Russians in Northern Kazakhstan. Both of these lead to an unhealthy level of Russian influence that can only be increased by Russian control of pipeline routes. At the same time, they give Russia the power to hurt Kazakhstan if Russian interests in transit routes are not satisfied.

The economic and security ties created by a 4,500 mile shared border are enhanced by the fact that Kazakhstan was part of the Soviet Union. Prior to independence, Russia accounted for approximately seventy percent of Kazakhstan's total trade.<sup>48</sup> Today, eighty

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<sup>46</sup> Ibid.

<sup>47</sup> Interview with Mr. Morningstar, Assistant Secretary, Coordinator for Caspian Policy, Room 7524, State Department, November 2, 1998.

<sup>48</sup> Martha Brill Olcott, *Central Asia's New States: Independence, Foreign Policy, and Regional Security*, (Washington, D.C.: United States Institute of Peace Press, 1996), p.57.

percent of all Kazakhstan's exports to the CIS states go to Russia.<sup>49</sup> In Soviet times, Kazakhstan, bordering China, housed several nuclear plants and a significant amount of Russian military. At independence, much of this arsenal was returned to Russia and the nuclear power plants closed. However, many factories still exist and are heavily invested in by Russia.

Russia uses these strong economic and security ties to exert leverage over Kazakhstan. Industrial factories in northern Kazakhstan are especially prone to Russian pressure. As punishment for state debts, Russia regularly cuts off their power. Those factories geared towards military production, however, are protected by military agreements between Kazakhstan and Russia. Consequently, when Kazakhstan is "punished," only these factories are left with power.<sup>50</sup>

The large minority of ethnic Russians in Northern Kazakhstan are the second factor necessitating strong relations with Russia. According to one journalist, "Many decisions that Kazakhstan makes virtually have to be cleared with Russia, or at least made in consideration of Russia's reaction because of its large minority there."<sup>51</sup> If Russian interests are not met, Russia could fuel a secessionist movement much like it did to cajole newly independent states to join the CIS.<sup>52</sup>

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<sup>49</sup> Richard R. Dion, "How oil, gas investment prospects compare for Azerbaijan, Kazakhstan," *Oil and Gas Journal*, July 28, 1997, pg. 25.

<sup>50</sup> Martha Brill Olcott, *Central Asia's New States: Independence, Foreign Policy, and Regional Security*, (Washington, D.C.: United States Institute of Peace Press, 1996), p.66.

<sup>51</sup> Richard R. Dion, "How oil, gas investment prospects compare for Azerbaijan, Kazakhstan," *Oil and Gas Journal*, July 28, 1997, pg. 25.

<sup>52</sup> Martha Brill Olcott, "The Caspian's False Promise," *Foreign Policy*, Summer 1998, pg.100.



On the other hand, Epinger's assertion that "a shared border" carries more weight than does the large Russian minority relies on significant evidence that Russia would not aid in a secessionist movement even if there were significant discontent. After Chechnya, Russia is unlikely to engage itself in a war with a newly independent state. Russia also does not have the capacity or the will to accept a large amount of expatriates and would rather see the Russians in Kazakhstan satisfied with their situation.<sup>53</sup>

The two factors necessitating a close relations with Russia--strong economic and security ties and the large minority of Russians—could and have resulted in Russian leverage. With the construction of pipeline routes, Russia's power to exert leverage promises only to increase. Russia has invested much time, energy, and money in the CPC line, expecting to realize two separate goals. The first is to secure a means to profit off of Kazakhstan's future oil wealth. Today, the Russian government and Russian oil companies have secured forty-four percent in the Caspian Pipeline Consortium.<sup>54</sup> Russia's second goal is to secure a strong measure of control over future oil transport from Kazakhstan. This second goal is also likely to be reached--Glavtransneft has been designated as operator of the Tengiz-Novorossisk pipeline.<sup>55</sup>

The one mitigating factor presently guiding Kazakhstan's relations with Russia is President Nazarbayev's friendly relationship with President Yeltsin. Both are adroit and pragmatic leaders confronted by similar problems. At times, they have considered

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<sup>53</sup> Martha Brill Olcott, *Central Asia's New States: Independence, Foreign Policy, and Regional Security*, (Washington, D.C.: United States Institute of Peace Press, 1996), p.62.

<sup>54</sup> Richard R. Dion, "How oil, gas investment prospects compare for Azerbaijan, Kazakhstan," *Oil and Gas Journal*, July 28, 1997, pg. 25.

formulating a Eurasian Union, though this idea has yet to materialize into anything substantial.<sup>56</sup>

In summary, Russia wants export routes through its territory in order to secure profits from Kazakh oil and control over a much vied-for commodity. Given the strong economic and security ties with Kazakhstan, Russia expects a route from Tengiz to go through its territory. The six million Russians living in northern Kazakhstan can only further the leverage Russia has. The seriousness of Russian involvement has led to the formation of the Caspian Pipeline Consortium, the longest lasting and most highly invested in consortium in the Caspian. If not appeased, Russia has the power to hurt Kazakhstan and slow export routes that avoid Russia. Therefore, at least one export route must go through Russia. Kazakhstan, then, must look for additional routes that will reduce its reliance on Russia and secure its political and economic independence. The question becomes where to find another export route and among those available, which has the greatest potential of coming to fruition.

### Route Through Iran

One alternative is to build a pipeline from Kazakhstan to Iran. A route from Turkmenbashi, Turkmenistan to Kharg Island, Iran is already being investigated by Shell. It could be extended to include Kazakh oil.

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<sup>55</sup> Robert Ebel, *Energy Choices in the Near Abroad: the Haves and the Have-Nots* (Washington D.C.: CSIS, 1997), pg. 107.

<sup>56</sup> Nurlan Amrelkulov, "Inter-ethnic conflict and resolution in Kazakhstan," in Roald Z. Sagdeev and Susan Eisenhower, eds. *Central Asia's New States: Independence, Foreign Policy, and Regional Security*, (Chevy Chase, Maryland: CPSS Press, 1995), pg. 167.

There are two overriding reasons why an Iranian route is attractive. Although Iran, like Russia, is a powerful and populous neighbor of Kazakhstan, it cannot exert similar leverage over Kazakhstan. Secondly, an Iran route would be quick and valuable--a southern route is by far the cheapest route available to countries on the Caspian's eastern shores.

There is one drawback to a route through Iran. It is also an additional drawback to relying solely on Russia for an export route. Both Russia and Iran have their own oil and gas reserves to consider. Reliance on export routes through either could present risks flowing out of a conflict of interest between Russia or Iran and Kazakhstan for access to markets.<sup>57</sup>

Primarily the United States has argued against an Iranian route. Based on its own politics with Iran, the United States pushes the idea that a conflict of interest, compounded by the inefficiency and corruption of the Iranian government, would make a southern route less favorable.<sup>58</sup>

The Iran route, however, remains attractive notwithstanding US hostility. President Nazarbayev insisted that if the US government doesn't come up with financial

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<sup>57</sup> There is a crucial distinction to be made concerning problems surrounding a "conflict of interest". The main difference between the problems concerning tariffs and deliveries Russia's Glavtransneft poses and those that a CPC line or a line through Iran pose is that the former is entirely under the control of one country while the latter two are joint ventures. Control of tariffs, deliveries, and access to markets is a matter of the contract in question—of degree—in the latter two cases.

<sup>58</sup> Interview with S. Frederick Starr, Chairman, Central Asia Institute, Nitze School of Advanced International Studies, Johns Hopkins University, November 3, 1998.

support for a non-Iranian route soon, Kazakhstan will decide its pipeline routes according to its own national interests.<sup>59</sup>

### China

The Chinese National Petroleum Company (CNPC) is looking into funding the extension to the Turkmenistan-Iran pipeline discussed above.<sup>60</sup> China has become intricately involved in the transportation and production of Kazakh oil because it wants to secure oil imports independent of US carriers, who currently ship oil to China from the Gulf States. The government of Kazakhstan and the CNPC are also discussing a route from Uzen, Kazakhstan to Xinjiang, China. The proposed route would cost \$7 billion, more than two times the expense of any other route.<sup>61</sup> The fact that such a route is even being considered testifies to Chinese resolve in securing oil exports from Kazakhstan.

Chinese involvement, on the one hand, is welcome because it would add a serious and capable investor to pipeline projects. On the other hand, it could result in China exerting leverage similar to Russia's over Kazakhstan today. China could buy out a significant portion of Kazakhstan's oil reserves or means of oil transport and thereby insure that its interests are met. At one point, Kazakhstan sold a sixty-percent share in one of its large oil fields to a Chinese State oil company.<sup>62</sup>

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<sup>59</sup> Elshan Alekbreov, "Despite political obstacles, energy work progresses around Caspian Sea," *Oil and Gas Journal*, June 15, 1998, pg.38.

<sup>60</sup> Julia Nanay, "Prepared Statement on Caspian Oil Basin and Gas Developments," *The Petroleum Finance Company*, May 6, 1998, pg. 3.

<sup>61</sup> Martha Brill Olcott, "The Caspian's False Promise," *Foreign Policy*, Summer 1998, pg.103.

### Baku-Ceyhan Route

Another route for Kazakh oil that would bypass Russia is the Baku-Ceyhan route. A relatively low-capacity pipeline from Baku, Azerbaijan to Supsa on the Black Sea is in the process of being built. The United States and Turkey would like to see that pipeline continued through Turkey to the port of Ceyhan on the Mediterranean. While the line to Subsa would not have the capacity to export oil from Kazakhstan in addition to Azeri oil, the line to Ceyhan would.

There are two possible ways to get the oil from Kazakhstan to Baku: building a pipeline south from the CPC line or an east-west line underneath the Caspian (Trans-Caspian), starting at Atqau, Kazakhstan and ending at Baku. If any, Russia would prefer the first alternative. However, since it does necessitate going through Russia, the first alternative would undermine the benefits of a Turkish route as a bypass to Russia.

The Baku-Ceyhan route offers Kazakhstan a truly “independent” alternative primarily because Turkey cannot exert leverage similar to Russia’s over Kazakhstan and does not have reserves of its own as do both Russia and Iran. Unburdened by a closeness of interests and situation, Turkey and Kazakhstan are free to be allies on a variety of issues. Celebrating the anniversary of Kazakhstan’s independence (first recognized by Turkey), Demirel states, “As president of the Turkish Republic, I want to say the following to the Kazakh people and to honourable President Nazarbayev: Under all

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<sup>62</sup> Ibid., pg.100.

conditions, and on every issue, Turkey will be on the side of Kazakhstan.”<sup>63</sup> The sweeping quality of his declaration indicates the strength of one overriding issue binding Turkey to Kazakhstan—oil. Later in the statement, Demirel stresses that Kazakhstan is the oil country of the future and that the Baku-Ceyhan pipeline must be built with a capacity of 100m tons per year.<sup>64</sup> Clearly, wherever the export routes end up being built, pipeline politics will determine Kazakhstan’s future allies.

## **Turkmenistan**

Turkmenistan has the same primary goal as Kazakhstan: to secure an export route or routes that will strengthen the country economically and politically. The means to achieve that goal, however, differ—primarily because Turkmenistan has weaker relations with Russia and stronger relations with Iran.

Turkmenistan has the fourth largest gas reserves in the world. In addition to national companies, two foreign companies—Bridas of Argentina and Unocal of the United States—are prominently involved in developing the reserves. Currently, Turkmen gas is being piped to Iran, consumed domestically, and sent to the Ukraine. Only the gas being piped to Iran is making a profit—the Ukraine has little ability to pay. Unfortunately, only seven percent of annual production capacity can be sent to Iran through the current pipeline.<sup>65</sup> Clearly, the export routes available for Turkmen gas are inadequate.

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<sup>63</sup> “President Stresses Country’s Firm support for Kazakhstan,” *BBC Summary of World Broadcasts*, December 18, 1996, Part 2 Central Europe—the Balkans, Turkey.

<sup>64</sup> Ibid.

<sup>65</sup> Jane Upperton, “Bigger turnout, but still wariness, in Turkmenistan,” *Platt’s Oilgram News*, January 17, 1995, Vol. 73, No.11, pg.4.

### Russia and Gazprom

For a time, both Kazakhstan and Turkmenistan piped gas through Russia under the auspices of Gazprom. However, Gazprom, in competition for European markets, only sells Russian gas to Europe while distributing Kazakh gas within Russia and Turkmen gas to delinquent customers such as Armenia and Ukraine. Consequently, Kazakhstan and Turkmenistan only received a portion of what their gas is worth. To this date, Kazakh gas is sent through Russia. Turkmenistan, on the other hand, quickly got fed up with the desperate situation Gasprom created. By the spring of 1997, Ukraine owed Turkmenistan 450 million dollars for its gas shipments.<sup>66</sup> Given this state of affairs, President Niyazov of Turkmenistan cut deliveries to Gazprom in the same year.<sup>67</sup> Although when Russia decided not to sell Turkmen gas on European markets, the Gazprom chief said he would promise to do what he could to keep the Turkmenistan population from “starving to death,” in dealings with Gasprom, Niyazov commented that he “smelled old Soviet ambitions.”<sup>68</sup> Turkmenistan has yet to find another viable pipeline route for its gas.

Today, Turkmenistan and Gasprom are discussing the possibility of another contract, although Turkmenistan would much rather find an alternate export route. Currently, Gazprom is asking for 25 cents more than Turkmenistan previously paid in

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<sup>66</sup> “Turkmen pipeline meeting is underway—President says Turkey route is acceptable,” *Platt’s Oilgram News*, January 17, 1995, Vol.73, No.11, pg.4.

<sup>67</sup> David B. Ottaway and Dan Morgan, “In Drawing a Route, Bad Blood Flows: Varying agendas bear on routes,” *Washington Post*, October 11, 1998.

<sup>68</sup> Ibid.

tariffs and wants to take the gas via a much longer route than necessary.<sup>69</sup> Fortunately, Turkmenistan can distance itself from Russia far more easily than can Kazakhstan. Turkmenistan does not share a border with Russia, and it does not have a significant Russian minority. Equally important, Turkmenistan has a potentially close relationship with Iran.

#### Turkmenistan-Iran-Turkey Route

By contrast, a common border, shared interest in pipelines, and large Turk minority in Iran, all draw Turkmenistan toward Iran. A relationship based on pragmatism materialized in the low-capacity gas pipeline from Turkmenistan to Iran—for all the talk, the first Russian bypass to be built in the Caspian.<sup>70</sup> Turkmenistan and Iran have come to agreement in other areas besides pipelines—Iran has promised to treat the Turk minority well in exchange for Turkmenistan's promise not to stir up revolts.<sup>71</sup> In some ways, Iran and Turkmenistan have a similar relationship as Turkey and Kazakhstan—unburdened by the history of the Soviet Union and open to compromises.

Recognizing Turkey's need for gas and Turkmenistan's special relationship with Iran, President Niyazov proposed a pipeline from Turkmenistan through Iran and to Turkey. One problem, however, is that Iran, with its own abundant gas reserves, could have a conflict of interest in dealing with gas from Turkmenistan. Although Iran has yet

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<sup>69</sup> Jane Upperton, "Bigger turnout, but still wariness, in Turkmenistan," *Platt's Oilgram News*, January 17, 1995, Vol. 73, No.11.

<sup>70</sup> Ibid.

<sup>71</sup> Ibid.



to develop its gas reserves, future development could make Iranian control over access to markets undesirable.

Another problem is that Russia may again involve itself in the transport of Turkmen gas. Last November, Shell, who is evaluating the Iranian route, and Russia's Gazprom formed a strategic alliance with plans to jointly handle a range of oil and gas projects.<sup>72</sup> Although Turkmenistan has been determined to distance itself from Russia, it is clearly not entirely free of Russian leverage.

#### Trans-Caspian Gas line

Another way to get to the gas markets in Turkey is through a pipeline underneath the Caspian, from Turkmenbashi to Baku and then to Turkish markets. Already considered in 1991, this alternative has run into several hurdles. For one, the dispute between Azerbaijan and Turkmenistan over an offshore oil field (called Serdar by Turkmen and Kyapaz by Azeris) will have to be resolved if a pipeline route is to be agreed upon.<sup>73</sup> Moreover, this route would preclude the one through Iran and is thus opposed by Iran.

Turkmenistan's position on the trans-Caspian pipeline has taken Iran's interests into consideration. Recently, Kazakhstan, Turkey, and the United States, among others, signed a declaration in Ankara in favor of a Trans-Caspian pipeline. Conspicuously,

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<sup>72</sup> "Standing up to Russia," *Petroleum Economist*, February 20, 1998, pg.41.

<sup>73</sup> Patrick Crow, "Pipeline Politics"

Turkmenistan was not one of the signatories.<sup>74</sup> Unwilling to upset Iran by coming to an agreement with the United States, but nonetheless desiring to keep as many options open as possible, Turkmenistan opted for a bilateral agreement with Turkey instead.

### Eastern Routes

The final option that Turkmenistan has to consider is routes to the east. One possible route is from Turkmenistan through Afghanistan and to Pakistan. UNOCAL, Saudia Arabia's Delta, and Argentine Bidas have considered this route. The major obstacle is the political instability of the Taliban in Afghanistan. Currently, the project is delayed indefinitely. The other possible route is from Turkmenistan to China, considered by the CNPC. At an estimated 13 billion dollars, the major obstacle to this route is cost.<sup>75</sup>

Routes to the east are advantageous for a couple of reasons. The markets there are starving for oil and gas, unlike the saturated European market. Secondly, they bypass Iran's conflicting interest for access to gas markets. The route to China represents a clear alternative. The route to Pakistan, however, may have to go through Iran.

### Legal Issues

Legal issues regarding the Caspian Sea reflect Caspian politics. They are also a "wild card" that each country uses to enhance its position. They arise because the Caspian is not technically a "sea" as defined by the 1982 UN Convention on the Law of the Sea,

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<sup>74</sup> Interview with Mr. Morningstar, Assistant Secretary, Coordinator for Caspian Policy, Room 7524, State Department, November 2, 1998.

but rather "a special inner sea." Up until the end of the Soviet Union, the sea was joint Soviet-Iranian property by the Protocol of 1940.<sup>76</sup> With the breakup of the Soviet Union, conflict between the littoral states--Azerbaijan, Turkmenistan, Kazakhstan, Iran, and Russia--for ownership of the Caspian began.

Both Russia and Iran want to see the five states share the resources since their immediate offshore waters do not contain significant reserves. At first, Russia took a hard line, opposing any division of the Caspian among the five states.<sup>77</sup> At the time (1994-95), there was a fear that the issue would cause regional conflict between Russia and the newly independent republics and between the republics themselves. An eight billion dollar contract that Azerbaijan signed for oil production resulted in a dispute with Russia and then also with Kazakhstan, Turkmenistan, and Uzbekistan for failing to lend enough support.<sup>78</sup>

Since then, Russia has proposed a condominium approach whereby the seabed would be divided into five sections, but the water above shared. This means that to start an oil project, all five littoral states would still have to vote on it beforehand. Motivated by a feeling that oil and gas development will go on regardless of legal issues and a desire to share in Kazakhstan's success, Russia came to an agreement with Kazakhstan on

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<sup>75</sup> Martha Brill Olcott, "The Caspian's False Promise," *Foreign Policy*, Summer 1998, pg.103.

<sup>76</sup> Geoffrey Kemp, *Energy Superbowl: Strategic Politics and the Persian Gulf and the Caspian Basin*, (Washington, D.C.: Nixon Center for Peace and Freedom, 1997), pg. 28.

<sup>77</sup> Margaret McQuaile, "Question looming above all: who is Caspian's owner?", *Platt's Oilgram News*, February 24, 1995, Vol. 73, No.38., pg.1.

<sup>78</sup> Amberin Zaman, "No resolution to Caspian legal status: Turkic meeting fails to agree on several issues," *Platt's Oilgram News*, Vol. 52, No.205, pg.4

demarcation lines in August 1998.<sup>79</sup> Iran, on the other hand, is still arguing for a shared seabed—either that or a redrawing of demarcation lines that would give Iran a substantial increase in offshore reserves. Turkmenistan is reluctant to agree to dividing the seabed for three reasons: a dispute with Azerbaijan over an offshore oil field, close ties to Iran, and a lack of its own offshore reserves.<sup>80</sup>

Azerbaijan, on the other hand, wants to see the agreement go further and divide the "water-column".<sup>81</sup> Kazakhstan and Turkmenistan, since the beginning, have not been supportive of the Azeri stance, jealous of Azerbaijan's far greater offshore oil reserves. In the future, however, Kazakhstan will want freedom to explore its own offshore oil reserves.

Legal issues concerning the Caspian Sea really come down to economics and politics. The issue surfaces whenever there is something to be gained or lost. Today, Russia and Iran use the legal issue to oppose "Trans-Caspian" pipelines.

The external politics of pipelines as a whole can be understood in terms of geopolitics. Kazakhstan is drawn closer to Russia and Turkmenistan to Iran primarily because of shared borders. For Kazakhstan, there is a stronger tie based on a shared history and large minority of Russians in northern Kazakhstan. In both cases, it is instructive to look at the consequences of having only one major export route--through Russia for

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<sup>79</sup> *Petroleum Economist*, August 12, 1998, pg.45.

<sup>80</sup> Elshan Alekbreov, "Despite political obstacles, energy work progresses around Caspian Sea," *Oil and Gas Journal*, June 15, 1998, pg.38.

<sup>81</sup> *Ibid.*

Kazakhstan and through Iran for Turkmenistan. For Kazakhstan, dependence on Russia introduces an increase in the already unhealthy level of Russian control over economics and internal politics. In addition, Russia presents a conflict of interest that could result in higher transit fees and problems with deliveries. For Turkmenistan, Iran also presents a conflict of interest. Niyazov's history with Gazprom makes him especially weary of such a clash.

The primary dilemma facing Kazakhstan is to find an export route in addition to one through Russia before it becomes too late and the inertia of the CPC line has already set in. There are two options available: a route south through Iran and a route under the Caspian and west to Ceyhan, Turkey. The Iranian route, again, presents a conflict of interest, but is attractive because of its low cost. The Turkish route, on the other hand, bypasses all conflicts of interests and strengthens relations between Turkey and Kazakhstan.

Turkmenistan's primary dilemma, on the other hand, is finding any realistic alternative to get its gas out. If the economic incentives of a route through Iran overcome current political obstacles, Turkmenistan will send its gas via Iran to Turkey. If, instead, the wishes of Turkey and the United States prevail regarding the trans-Caspian pipeline, Turkmenistan will send its gas across the Caspian. Routes to the East—either to China or Pakistan—are an attractive option in the long-term.

## **Conclusion**

Kazakhstan and Turkmenistan are at a turning point in their history. As with any newly independent republics, the actions they take now will set up their relations with neighboring countries and their situation in the global geopolitical world. The one aspect that sets them apart is an abundance of oil and gas reserves. They face the challenge of finding an export route that suits their interests best. In both cases, multiple routes are desirable so that no one route has "veto power." For Kazakhstan, a route through Russia along with one through either Iran, Turkey, or China--each with its own disadvantages and advantages--would take into consideration Kazakhstan's close ties to Russia and need to assert its independence. For Turkmenistan, a route through Iran to Turkey along with one to the East would build upon Turkmenistan's current ties to Iran and provide a way to bypass the conflict of interest Iran presents. A "trans-caspian" could, however, end up taking the place of a route through Iran.

Currently, both countries are forestalled—they cannot develop themselves because their economic and political outlook is almost entirely determined by how and when their oil and gas will get to market. Therefore, even though the perennial dilemmas of oil and gas development face both Kazakhstan and Turkmenistan, rapid construction of pipelines is in their interest. One journalist summarizes what we might expect from oil and gas development in Kazakhstan and Turkmenistan:

"The oil boom in the Caspian basin promises to alter everything in its path--to erect a new El Dorado in desert wastes, fuel the economies of US and Europe, and re-order the global economy. It will also imperil thousands of years of tradition,

setting its defenders against the tide of a glittering but deeply uncertain future."<sup>82</sup>

Indeed, oil and gas development will bring in much needed revenues to jump-start the economies of Kazakhstan and Turkmenistan. It will also define their future allies and the economic and political stability with which they will face the next several decades.

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<sup>82</sup> Frank Viviano, "Black Gold, Iron Rule: Caspian nations bank on autocratic regimes to ride out oil boom," *San Francisco Chronicle*, August 13, 1998, pg.A1.

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