A natural gas pipeline crossing the Caspian Sea basin – which factors contribute to its advancement or impediment?

What are the main challenges for Turkey with respect to promoting the attempt to realize the trans-Caspian gas pipeline project?

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I Executive Summary

Concerns about energy security have been on the rise lately. The concerns do not end with the European Union or with an importing country for that matter. Energy security also concerns the exporting countries and the oil and gas corporations among others. With the increasing concerns, energy security (policy) has increasingly come to play a vital part in a state’s foreign policy strategy. In this respect, the trans-Caspian gas pipeline project is a pipeline project aimed at bringing East Caspian gas to the West. The Caspian region, however, is a complex area to do business in. The competition for hydrocarbon reserves in the Caspian region is also named the ‘New Great Game’, pertaining to the ‘Great Game’ which was fought between the Russian and British Empire in the 19th century. The main difference, however, is that now it encompasses far more players (global, regional powers, transnational oil corporations, intergovernmental organizations and so forth) with various conflicting interests making it more complex. A first attempt to realize this gas pipeline project was undertaken at the end of the nineties, but it failed due to several factors. With the growing concerns about energy security a second attempt is started, which is still ongoing. In this respect, what are the main factors that shall contribute to the advancement or impediment of the trans-Caspian gas pipeline project in the future and to which extent and under which conditions shall this occur? In order to answer this question the Case Study Protocol, specifically designed to analyze with hindsight which predetermined factors had the largest effect on the realization or failure of a large gas infrastructure project, will be used. The Case Study Protocol focuses on four explanatory factors, namely the investment climate, transit risk, offtake risk and geopolitical relationship. Nevertheless, this Protocol had to be altered as regards the content and also with respect to its application in order to make it fitting to analyze this particular ongoing gas pipeline project.

In short, it is decided to determine the factors that have led to the failure of the first attempt and use these results as a starting point from where it is determined whether the explanatory value of these factors have evolved over time till the present. One of the main factors that have led to the failure of the first attempt was the bad leadership of the then Turkmen president Niyazov. President Niyazov’s régime was characterized as erratic and suppressive offering little protection to ensure the sanctity of contracts making it undoubtedly an unreliable partner. Furthermore, Russia is identified as a large stumbling block opposing firmly to the realization of the trans-Caspian gas pipeline project. In the first attempt, it actions to lock-in the Central Asian gas and to saturate the intended offtake market for the East Caspian gas by implementing its own gas pipeline project (Blue Stream gas pipeline project) were a severe blow. In the second attempt, a new factor has emerged; the interconnected gas pipeline project. The Nabucco gas pipeline project is bound to deliver the East Caspian gas to the European markets. It is argued that given the increasing concerns about energy security, more of these mutually dependent large gas pipeline projects will emerge in the future connecting regions over vast distances. Therefore, it is asserted that this new factor must be included in the original Case Study Protocol. Naturally, this factor’s influence is relevant to the extent that such an interconnected gas project exists. In addition, in the second attempt, Turkey has thrown up a demand that they want to buy relatively cheaper gas from the interconnected Nabucco gas pipeline project endangering the realization of the former and the trans-Caspian gas pipeline project. Furthermore, China has entered the ‘New Great Game’ in the second attempt in view of its growing concerns about energy security. In the nineties, China did not play any role of importance in the ‘New Great Game’ in the Caspian region. It made up leeway in the 21st century and became a formidable competitor in the ‘New Great Game’ and a potentially strong impediment to the trans-Caspian gas pipeline project. They are an impediment, however, to the extent that it is vied for the same gas resources. Moreover, the
former Turkmen president Niyazov deceased making way for president Berdymuhammedov, a reform minded person, which has been sending auspicious signals with respect to its participation to the trans-Caspian gas pipeline project. Subsequently, in the ongoing second attempt, the driving forces that are responsible for the change in the explanatory value of these factors are uncovered, which is used to help determine the possible future development of the factors. In addition, future international political and economic systems (worlds) are outlined in order to examine what its consequences are for the development of the identified factors.

In addition to this, Turkey is identified as the problem in this dissertation. As a result, parallel to the attempts, the role and influence of Turkey from the first attempt till now is analyzed. In the end, all these Turkey specific insights and the insights regarding the prospected development of the factors in all the various future worlds will provide the opportunity to identify what the main fields of interest are for Turkey in order to effectively promote its realization. It is argued that although it does not seem possible that Turkey can join the competition between the great powers for the hydrocarbon resources in the Caspian region, it still has a potential of affecting the future of the region. In this respect, Turkey’s unique ties with the Turkic countries combined with its growing economic capacity, its regional and international prestige and developing economic and political relations with Russia do provide Turkey with an opportunity to play a greater role in the ‘New Great Game’. Nevertheless, the main challenge for Turkey in this regard is that it needs to show political willingness to prioritize its ambitions towards this region and design a realistic and pragmatic foreign policy strategy towards Central Asia. Furthermore, Turkey’s main challenge regarding its firm disagreement over the pricing mechanism regarding the Nabucco gas project is not to loose sight of the bigger picture; its objective to increase the security of its gas supply and to augment its (geo)strategic importance for the European Union.
II List of Acronyms in Text

BCM: billion cubic meters
BSP: Blue Stream gas pipeline
BSEC: Black Sea Economic Cooperation
BTC oil pipeline: Baku-Tbilisi-Ceyhan oil pipeline
CIS: Commonwealth of Independent States
ECT: Energy Charter Treaty
IOC: international oil corporations
IGO: intergovernmental organizations
IFI: international financial institution
NOC: national oil corporation
OSCE: Organization for Security and Co-operation
SCP: South Caucasus gas pipeline (also called: Baku-Tbilisi-Erzurum pipeline)
TCGP: trans-Caspian gas pipeline
TOE: ton(s) of oil equivalent
TNOC: transnational oil corporations
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1 Introduction

Natural gas has seen an unprecedented growth in the European Union over the last decades. The natural gas consumption of the EU-30 is expected to rise from 510 million toe in 2010 to 660 million toe in 2030 (EU 2000). Moreover, the consensus is that the share of imports as a percentage of European gas demand (import dependence) is expected to rise from one-third in 1998 to reach around two-thirds by 2030 (EU 2000, pp. 117). Thus it is not remarkable that the issue of energy security (security of supply) has seen a renewed interest within the European Union. These concerns were reinforced by the Russian-Ukrainian gas crises (gas cut-off) in January 2006 (Stern 2006), in 2008 (BBC 2008) and 2009 (Reuters 2009). However, energy security concerns has not only found its revival in the European Union, it has risen to the top of the political agenda globally. In the light of a state’s national interests (a state wants to survive and be secure), energy security (policy) unmistakably deserves a prominent place.

In fact, when it comes to the world’s current and future energy security, the Caspian region has a significant bearing. In this respect, the European Union, the United States and Turkey are attempting to realize the westbound trans-Caspian gas pipeline project (TCGP). It is a pipeline project originating from the Central Asian countries that is bound to deliver to the European markets with the main characteristic that it does not cross Russian or Iranian soil. Russia and Iran are therefore strongly opposed to this pipeline project. A first attempt to realize this project has been undertaken in the period between 1997 and 2001, but eventually failed due to several factors. Currently, the proponents are again engaged in an ongoing second attempt to realize the TCGP. To this end, the main research question of this dissertation is dual; What are the main factors that shall contribute to the advancement or impediment of the attempt to realize the trans-Caspian gas pipeline in the future and as far as this is concerned what are the main fields of interest for Turkey in order to effectively promote its realization? Turkey plays a central role in this dissertation given their advantageous geostrategic position as it could become the fourth main artery of delivering natural gas to the European Union after Russia, Algeria and Norway (Roberts 2004). However, this depends heavily on the completion of the TCGP among other projects.

The Caspian region, however, is a complex area to do business in. The Central Asian and Caucasian countries have just recently in 1991 became independent from the former Soviet Union. These countries to a lesser or higher extent are characterized by autocratic rule, potential instability and a bad investment climate. Nevertheless, these states are more than willing to offer their natural gas to the lucrative European markets. The figures about the amount of energy reserves available are adjusted regularly since new reserves are being discovered continuously. One of the latest estimations is that the countries adjacent to the Caspian Sea possess over 10% of the proven natural gas reserves (BP 2002) intensifying the competition in the region. The competition for hydrocarbon reserves in the Caspian region is also named the ‘New Great Game’, referring to the ‘Great Game’ which was fought between the Russian and British Empire in the 19th century (Hopkirk 1992). The main differences, however, are that the ‘New Great Game’ encompasses far more players with various conflicting interests (various states, transnational oil corporations, intergovernmental organizations2) and also the geostrategic importance of the region has increased significantly (abundant hydrocarbon reserves, combating drug trafficking, a bulwark against Islamic fundamentalism) as a result of which its overall complexity is much greater.

1 The current EU-27 members including the candidate members Croatia, Turkey and Macedonia
2 An intergovernmental organization is an organization comprised primarily of sovereign states (referred to as member states) to facilitate cooperation. It can be divided into international, regional, ethnic, (cultural, historical and religious) and economic organizations.
1.1 Problem description

Turkey is taken as the problem owner in this research considering that it has an advantageous geostrategic position as it can facilitate a natural corridor through which natural gas from a wide variety of suppliers from the Caspian Sea region, the Middle East and the Gulf can access the growing European market by pipeline. These actualities shape the goal of Turkey of aspiring to become the fourth main artery for delivering natural gas to the EU, next to Russia, Algeria and Norway. The primary objective of Turkey, though, is to find diversified, reliable and cost-effective supplies for its rapidly expanding energy need. The realization of the trans-Caspian gas pipeline (TCGP) project has the potential of contributing largely to these objectives. The failed first attempt concerns a 1600 km pipeline system that would run from the Shatlyk and Dowletabad fields in eastern Turkmenistan going across the Caspian Sea to Azerbaijan, Baku, onward through Georgia to Erzurum, Turkey as then it would be linked to the principal Turkish gas transportation grid (see figure 5). The immediate offtake market was meant to be Turkey, but Europe was considered as well, though in the long-term. Exports to the European Union is considered again in the second attempt by means of the Nabucco gas pipeline project\(^3\), though this time it is regarded as the main offtake market. However, the realization of the TCGP project is not clear-cut. Its realization is not solely dependent on its economic and technical potential, but also on other factors such as (geo)politics. In this respect, conflicting interests of the involved actors are one of the main causes for the experienced impediment. The main actors opposing the TCGP are Russia and Iran. Russia considers the Caspian region as its legacy after the break up of the Soviet Union and does not want any rivals to enter the Caspian region and undermine its sphere of influence. Furthermore, Russia still is an important trading partner and a geographical connection to the outside world for these states. Turkmenistan and Kazakhstan are still entirely dependent on the Russian network of gas pipelines for exporting its natural gas to foreign markets. Although the price of natural gas that is sold to Russia has increased over the years, it is still relatively low compared to the price that Russia’s Gazprom charges to the European markets. The Russian state-owned energy monopoly, Gazprom, re-sells this gas to Europe making a high profit (Roberts 2004, pp. 9). Russia uses its strong political and economic ties with these states to prevent them from diversifying their export routes. Any route under or across the Caspian Sea would diminish Russia’s control over Turkmenistan’s and Kazakhstan’s gas exports, along with the strategic influence over the country’s domestic and foreign policies that such control brings (Sahgal 2004). However, these states, which have centuries-old political, commercial and cultural legacies with Russia, have been pursuing to establish a balance between their new orientation with the USA, Europe and regional powers like Turkey and Iran.

Another important aspect with respect to Turkey is that its goal cannot be viewed separately from its EU candidacy. Turkey is focussing on energy transit issues as a way of increasing its leverage with Brussels, especially now with its EU negotiations in a dip (Schleifer 2007). Bulent Aras, a professor of international relations at Istanbul’s Isik University and an expert on energy issues, has said that Turkey is changing its attitude. He asserts that Turkey in the first place was following the line of going along with bilateral agreements with the EU on energy projects, but now, however, Turkey is using its position as a potential significant transit country as a bargaining chip regarding EU accession (Schleifer 2007). However, the consequences of the realization of the TCGP as such on the EU accession negotiations are not

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\(^3\) The Nabucco gas pipeline is designed to connect the Caspian region and the Middle East with the European Union. The pipeline will start in Turkey and passes Bulgaria, Romania, Hungary and ends in the Baumgarten hub in Austria. From Austria it is further transported to the Central and Western European countries. The pipeline will have a total length of 3,300 kilometers.
a part of this dissertation as it falls outside the scope. It is merely mentioned to indicate that Turkey’s aspiration of becoming an important energy artery has multiple dimensions. All in all, Turkey’s objectives of becoming one of the main energy arteries of the European Union and to find secure, diversified and cost-effective gas supplies is not uncontested. In this context, the trans-Caspian gas pipeline project has the potential of contributing significantly to these objectives, yet the realization of this gas pipeline project is considered troublesome and subject to a variety of (conflicting) strategic interests of various countries that all have their own reasons to realize or obstruct this project.

1.2 Research objective

The main objective is to identify what the main factors are and to which extent they shall contribute to the advancement or impediment of the trans-Caspian gas pipeline project. As regards this it will be determined what the main fields of interest are for Turkey in order to effectively promote the realization of the TCGP project. This objective will be met by using the Case Study Protocol provided in Hayes (2004, pp. 22-28), which is in fact a guideline for identifying to which extent the predetermined factors have been an influence on the attempt to implement a gas pipeline project. The Case Study Protocol focuses on four explanatory factors, namely the investment climate, transit risk, offtake risk and geopolitical relationship. However, adjustments need to be made to this Protocol in order to make it fitting to this particular gas pipeline project. In addition to this, parallel to the phases, the development of the role and influence of Turkey from the first attempt till now will be analyzed. In the end, all these Turkey specific insights and the insights regarding the prospected development of the factors in the various future worlds will provide the opportunity to identify what the main fields of interests are for Turkey with respect to promoting the TCGP project. It is believed that it will provide Turkey with valuable information regarding what the future may have in store for the attempt to realize the TCGP on the basis of which Turkey can construct its energy strategies to promote the realization of this project.

1.3 Structure

In Chapter 2, Research Questions and Methodology, the research questions that need to be answered are outlined and additionally the analytical framework for answering these research questions and thereby analyzing the trans-Caspian gas pipeline project is explicated. In Chapter 3, Operationalization of the Case Study Protocol, the Case Study Protocol as provided in Hayes (2004) is adjusted and supplemented according to the characteristics of the trans-Caspian gas pipeline project and by using insights gained from various sources. In Chapter 4, Analysis of the first phase, the first failed attempt to realize the trans-Caspian gas pipeline project, which occurred between 1997-2001, is analyzed as to determine which factors to which degree have influenced the project. This will be done on the basis of the adjusted Case Study Protocol. In Chapter 5, Analysis of the second phase, which is still ongoing, (2001 till present) is analyzed to determine how the identified factors in the first attempt have developed in terms of explanatory value and also new (sub) factors will be analyzed. The Case Study Protocol will be adjusted if necessary to make it suitable for the ongoing second attempt.
In Chapter 6, *Analysis of the third phase*, the possible future development of the identified main factors will be determined. To this end, future worlds (international political and economic system) are constructed.

In Chapter 7, *Conclusions*, a summary of the main findings are given with respect to the failed first and the ongoing second attempt. Furthermore, Turkey’s main challenges in the various possible future contexts for effectively promoting the TCGP project will be stated. The chapter is finalized with an overview of the main limitations of this dissertation and recommendations are given for further research.

Below in figure 1, an overview is provided of how the dissertation is structured. The connection between the chapters is explicated in an orderly manner.
Figure 1: An overview of the structure of the dissertation
2. Research questions and methodology

In this chapter, the research objective will be translated into concrete research questions that need to be answered in order to meet that objective. Subsequently, a schematic overview and description of the analytical framework is given, which provides a structure on the basis of which this dissertation examines the research questions at hand. Next, the type of data gathering used in this research is outlined. The chapter is finalized with a general demarcation in order to exemplify the scope of this dissertation.

2.1 Research Questions

The main research question is the following:

What are the main factors and to which extent and under which conditions shall they contribute to the advancement or impediment of the attempt to realize the trans-Caspian gas pipeline in the future and as far as this is concerned what are the main fields of interest for Turkey in order to effectively promote its realization?

The sub research questions are the following:

- How should the Case Study Protocol as presented in Hayes (2004) be operationalized according to this specific case in such a way that it gains in analytical strength and in which analytical framework should it be casted?
- To what extent and under which conditions contributed the four ‘explanatory factors’ to the advancement and especially impediment of the failed first attempt to realize the TCGP in the period 1997-2001?
- What are the main alterations of the explanatory factors taking into account their development over time from the first attempt till now and how do they contribute to the advancement or impediment of the ongoing second attempt to realize the TCGP?
- What is the possible future development of the explanatory factors and how will they contribute to the advancement or impediment of the attempt to realize the TCGP?
- What was the role and influence of Turkey during the first attempt and how has it developed over time till now and what are the main challenges for Turkey with respect to the factors’ possible development into the future within the context of the ‘New Great Game’?

2.2 The Case Study Protocol’s characteristics

In this section, the choice for the Case Study Protocol as provided in Hayes (2004) will be explained. In addition to this, light will be shed upon its main advantages and disadvantages.

The Case Study Protocol’s main advantage and the main reason why it is used in this dissertation lies in the fact that it provides a structure/framework, which allows one to conduct a straightforward analysis. Moreover, the Protocol has predetermined the major explanatory

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4 These explanatory factors are determined in Hayes (2004) by means of interviews with various experts and literature research.
factors (investment climate, transit risk, offtake risk and geopolitical relationship) as supplemental to the techno-economic factors, which provides a sound starting-point for this dissertation. In addition, the Protocol provides the opportunity to conduct comparative analyses between the various case studies (gas pipeline projects) and thus allows one to draw aggregated conclusions from the insights obtained in every case study. Nevertheless, it has major drawbacks, one of them being that 'geopolitical relationship' as a factor is defined narrowly, not utilizing the full explanation power of the study 'geopolitics'. Another drawback is that it is static in the sense that it solely focuses on analyzing a case study with hindsight. It does not allow for an analysis that incorporates a case study’s development over time, while a dynamic approach is exactly what this particular gas pipeline project (TCGP) demands. Therefore a new analytical framework needs to be constructed incorporating the dynamic characteristic of this specific gas pipeline project, stated in the following section. Moreover, as regards the adjustments and supplements to the Case Study Protocol, an additional research question ought to be included, namely:

*How should the Case Study Protocol as portrayed in Hayes (2004) be operationalized to analyze an ongoing (dynamic) gas infrastructure project?*

### 2.3 Conventional vs. unconventional factors

The factors identified in Hayes (2004) will be compared to the more conventional techno-economic and environmental factors. This is done in order to discuss its explanatory power in a relative manner and to explain why the unconventional factors are also important apart from the conventional ones.

It is believed that the realization process of a large gas infrastructural project can roughly be divided into 4 stages:

0. Availability of and demand for natural gas
1. Techno-economic and environmental\(^5\) feasibility studies
2. Forming a consortium and designing a financial scheme
3. Implementation of the large gas infrastructure project

In the null stage, before any study is financed there needs to be somewhat\(^6\) reliable data about the gas supply projections (based on the availability of gas and domestic demand) of the host country. The concerned gas source can be one which has been extracted for some time increasing the reliability of the remaining estimated amount of gas or it can be a new gas field which has not been extracted yet but somewhat reliable data exists about the amount of gas it contains. On the other hand, to make the picture complete, there needs to be reliable data/forecasts about the absorption capabilities (demand projections) of the concerned offtake markets.

Subsequently, funds are allocated for the techno-economic and environmental feasibility studies. The techno-economic factors as used in a feasibility study entail technical, financial and economic analysis of a gas pipeline project. The technical and engineering considerations used to determine the techno-economic feasibility of a gas pipeline route are pipeline length and diameter, geological, topographic and geographical (land use) conditions (Fereydoon

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\(^5\) This happens predominantly in the Western backed gas projects

\(^6\) The term ‘somewhat’ is used consciously because it is never sure until you have extracted the gas field for some time
For example it is not desirable to route pipelines through urban and industrial areas and in large bodies of water and roads; the highest construction costs are assigned to these type of terrains. The lowest costs are assigned to areas with bare ground, dry grass, less dense vegetation and agriculture. Concerning the geological characteristics, a distinction can be made in the hardness of the rocks. Obviously the costs decrease as the rock gets softer. These data but less detailed are used to draw up a financial estimation of the capital investment costs. Moreover, the technological state of laying pipelines in various terrains is an important factor, such as constructing pipelines on subsea terrains. (e.g. Blue Stream pipeline).

Furthermore, also the economics of the gas pipeline project are estimated taking into account the demand profiles of the offtake countries, fluctuating gas prices etcetera. Obviously this is crucial information for private investors and the producing countries alike.

Apart from the techno-economic feasibility study, the environmental factor has become important as well over the years. Therefore in this current context the gas pipeline projects also require an environmental impact assessment.

If the project is commercially\(^7\), technically and environmentally feasible and the concerned actors (host, transit and offtake countries) concur with these results and showing willingness to go through with it, the next step is to form a consortium and design a financial scheme for the project.

The next stage is to form a consortium of transnational oil and gas corporations. This may include the NOCs of the concerned actors and/or IOCs who are able to build and operate the gas infrastructure project. Considering the change to a ‘new gas world’, the consortium needs to assess the (commercial) risks of the project and as a result decide whether they are willing to finance the entire capital investment costs. If not, which with a high likelihood can be explained by the factors as provided in Hayes (2004), namely a bad investment climate in the host countries, transit and offtake market risks, (external) financiers can be approached to design a mechanism for the financing of the project. These financiers are (inter)national financial institutions such as the World Bank, EIB, national and private banks etcetera. In addition, also the states themselves can be approached for funding. As a result, these factors should be seen as supplemental to the techno-economic and environmental factors, which come into play in the second stage of the realization process. Moreover, considering the high costs and the perceived risks associated with large gas infrastructural projects, designing a financial scheme can be a complex undertaking to say the least.

After having designed a financial scheme accepted by all the concerned actors, the next phase is to implement the gas infrastructure project. The implementation entails the construction of the pipeline transportation network at the least, but it could also include the drilling and production of the natural gas.

\textit{Natural gas and geopolitics}^8

Whereas the factors identified in Hayes (2004) and the associated risks (see chapter 3 for a detailed explication) mostly come forward in the second stage of the realization process, geopolitics can occur in every stage of the project. Nevertheless, it does not arise in every gas infrastructure project to the same degree. This very much depends on the geographic location of the project and the international political and economic system in which the project takes place (Correlje 2006). In addition, the degree to which geopolitics plays a role also depends on a Western point of view as China for example aggressively pursues to secure their gas supply paying little attention to the commercial feasibility of the pipeline project.

\(^7\) ‘geopolitics’ is in this research defined as the influence of geographic, demographic, economic and technological factors on political outcomes and vice-versa.

\(^8\) This is true from a Western point of view as China for example aggressively pursues to secure their gas supply paying little attention to the commercial feasibility of the pipeline project.
on the involvement of the external actors as the involved actors can be classified into two groups:

- Directly involved actors (host, transit and offtake countries);
- The external actors (USA, Russia and China).

Geopolitics as an influencing factor will reach its determinative influence when the external actors are involved as well. Because of these external actors, geopolitics is regarded as a latent factor, lying in wait to strike at any time. In this respect, it needs to be mentioned that the USA as a global power is the biggest player in the global energy system. Even so, Russia’s and especially China’s position is changing fast in this respect as the latter is aggressively pursuing to secure its oil and gas supply. As far as this is concerned, China is seen as the new major player in the global energy system (IEA 2000).

Moreover, the Caspian region where the ‘New Great Game’ takes place is considered a geographic location where geopolitics flourishes. It is a location with strategic importance for the foreign and security policy making (energy security and the war on terror) of the external actors. This makes geopolitics a factor with a potentially high explanatory value especially with respect to the trans-Caspian gas pipeline project and should be analyzed accordingly.

All in all, a feasible gas infrastructure project in techno-economic and environmental terms does not necessarily imply a guarantee that it will be realized. At the most, it constitutes a framework on the basis of which negotiations can occur among the directly involved actors. Next is to secure financial support, which may be a daunting task given the large investment capital required for gas infrastructure projects and the perceived risks associated with the factors as identified in Hayes (2004). These factors should be regarded as supplemental to the techno-economic and environmental factors and come into play in the second stage of the realization process of a gas pipeline project. In the end, however, geopolitics as an explaining factor possesses the potential influence to determine the direction of a gas route to the expense of another.

2.4 The analytical framework

The trans-Caspian gas pipeline project must be rendered into an analytical framework such that it endorses and uses its dynamic characteristic to determine the main explanatory factors and the development in their explanatory values by using the past and the time period till the present. Hence, it is rendered into an analytical framework such that the failed first attempt (1997-2001) and the time period till the present (2001-present), ongoing second attempt, are viewed as two separate, but connected phases succeeding and feeding each other with the necessary input. The development of the explanatory factors over time from 1997 till the present functions as the connection between these phases and thus plays a central role. A schematic overview of the analytical framework is given in figure 2. It needs to be mentioned that the explication of the analytical framework partly answers the first sub research question.
The thread that connects the phases with one another is ‘the major explanatory factors’ as identified in Hayes (2004, pp. 2-3). In order to make this dissertation more valid and applicable to this specific gas project and the research objective of this dissertation (Turkey as problem owner), the original Case Study Protocol by means of which the first and the second phase will be analyzed ought to be operationalized. More about this in chapter 3.

The aim in the first phase of the analysis is to identify which of these factors, to which degree have contributed to the advancement and especially impediment of the failed first attempt to realize the TCGP in the period between 1997-2001. The outcome of the first phase is a discussion of which factors to which extent and under which conditions have impeded the first attempt.

From that point on in the second phase, the evolution of these factors from the first attempt till the present day will be the point of focus. To this end, the outcome of the first phase will be used as input for the second phase. It will be determined what the driving forces are behind the development of these factors and subsequently what the current influence is of these factors on the ongoing second attempt. The driving forces will be probed as it provides necessary information for the attempt to derive the development of these factors in the various future worlds (3rd phase). The outcome of this phase is a discussion on what the current influence is of the main factors from the first attempt, having considered their development over time. Furthermore, also new (sub) factors may emerge, which must be taken into consideration as well.

In the third phase, the objective is to determine how the identified factors may develop into the future. To this end, first of all a comparative analysis will be carried out between the first two phases in order to make a distinction between the more or less constant (long term, non-changing) factors, the changing and the non-assignable factors over time (see figure 2). The underlying reason is that the categorization of the factors provides one with indications to some extent of how they might develop into the future. Secondly, various future worlds (international political and economic systems) will be constructed within which the possible
future development of the factors will be derived. The third phase ought to be considered, though, as merely a reflection on how the factors could develop into the future. Moreover, it needs to be cited that the second part of the research objective is to identify the main fields of interest for Turkey with respect to the attempt to realize the TCGP as Turkey is taken as the main actor/problem owner in this dissertation. To his end, Turkey’s developing role and influence within the context of the ‘New Great Game’ will be analyzed in the first two phases. Subsequently, in the third phase the results obtained from determining the possible development of the factors in the future worlds combined with the gathered information about Turkey will contribute greatly to achieving that objective.

2.5 Defining energy security and the use of the constructivist approach

In this section, it will be explained what the constructivist approach entails, why this approach is selected over rational choice and how it will be used within the analytical framework of this dissertation. Moreover, energy security will be defined and so will its place within the constructivist approach.

Constructivism can be regarded as an approach to international politics (Barnett 2001). It is about social action and about the relationship between structures and agents (actors) (Jackson 2006). Constructivism focuses on human awareness and its place in world affairs and as such provides a framework to understand the relationship between agents and structures. It encompasses the understanding that normative and ideational structures (non-material structures) are just as important as material structures. Constructivists believe that the non-material structures shape the social identities of actors which inform the interests and, in turn, the actions of the actors (Reus-Smit 2005). According to (Wendt 1999), idealism and holism are the core commitments of Constructivism. The former refers to the claim that the most fundamental feature of society is social awareness. It claims that the world is defined by material and ideational forces and that these ideas are social as such that the meanings and consequences of these forces are not given by nature but rather driven by human interpretations and understandings. In other words, it claims that the social and political world, including the world of international relations, is not a physical entity or material object that is outside of human consciousness. It claims that it exists only as an intersubjective awareness among people (Jackson 2006). It acknowledges that the meaning and construction of the material reality is dependent on ideas and interpretation. Ideas shape how we see ourselves and our interests, the knowledge that we use to categorize and understand the world, the beliefs that we have of others and the possible and impossible solutions to challenges and threats (Jackson 2006). Holism is the view that claims that structures cannot be decomposed to the individual units and their interactions because structures are more than the sum of its parts and are irreducibly social (Barnett 2001). Moreover, the effects of structures go beyond merely constraining the actors but also construct them.

Moreover, power in the traditional sense is interpreted as the ability of one state to compel another state to do what it otherwise would not. However, it needs to be mentioned that the forces of power, from the perspective of constructivism, are not only material (political, economic, military) but also ideational (soft) power. Soft power can be defined as getting the outcomes you want without tangible threats or payoffs. A state may obtain the outcomes it desires in world politics because other countries - looking up to their values in terms of an exemplary model, aspiring to for example its level of openness and prosperity – want to
Constructivism is not the only meta-theoretical perspective as rational choice is another. Rational choice offers a framework for understanding the relationship between actors and their environment. One of the main differences is, however, that rational choice believes that actors operate with fixed preferences and that they attempt to maximize those preferences under a set of constraints. These constraints are believed to be induced by the environment whereas constructivism sees the environment as constituting the actors’ identities and interests. Moreover, rational choice treats interests as fixed, constructivism on the other hand treats interests as constructed by the environment and interactions. Moreover, constructivism does not exclude the explanatory value of material forces. On the contrary, it merely states that the meaning that is given to material forces is through human interpretation (ideas). As a result, it believes that if the thoughts and ideas that constitute the international system change, then the system itself will change as well. The latter entails the underlying reason why this approach is chosen over other meta-theoretical approaches as constructivism claims that there is no such thing as fixed preferences but treats actors’ interests as constructed by the environment and human interactions (Reus-Smit 2005) and thus is subject to change.

Application of this approach, which inherently takes into account a dynamic and changing environment, to this particular gas infrastructure project (TCGP) that is ongoing (dynamic), provides an effective framework to analyze and explain the changes in the factors’ explanatory value over time (the time span of the three phases) and/or the emergence of new factors for that matter. In other words, constructivism endorses the dynamic character of interest (trans)formation and enables to identify the driving forces of the changing interests providing a solid basis on which the possible future development of the factors can be determined. Moreover, providing yet another sound argument for using constructivism, it is worthy of being able to explain the development of the normative and ideational structures of the present international system as well as the social identities they have brought about (Reus-Smit 2005, pp. 201). This is significant in the sense that it endorses the construction of future worlds (see section 2.4).

In conclusion, the constructivist approach will be used as a tool to analyze and explain the factors’ changing explanatory value over time brought about by the changing environment and through interactions between actors. In the end, the constructivist approach ought to be incorporated into the Case Study Protocol in order to make it suitable to analyze a dynamic gas infrastructure project as it is believed that it is the best meta-theoretical approach for this purpose.

Defining energy security and its use within the constructivist approach

Obviously, energy security plays an important role in the state’s ultimate desire to survive and be secure (national interest). When it comes to defining energy security, it is asserted that it is an umbrella term that covers many concerns linking energy, economic growth and political power (see figure 2). The energy security point of view varies depending upon one’s position in the value chain. For example, consumer countries and energy-intensive industries want reasonably-priced energy on demand and have concerns about supply disruptions. Major oil producing countries consider security of revenue and of demand

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9 Exemplary are the human rights activists’ ‘name and shame’ activities to force the concerned states to adopt the widely accepted codes of conduct and existing legal norms

10 The underlying assumption is that the actors’ interests and thus strategic behaviour partly explain the degree of importance of the explanatory factors.

11 It concerns holistic constructivism in particular
integral parts of any energy security discussion. Oil and gas companies on the other side consider access to new reserves, ability to develop new infrastructure and stable investment regimes to be critical to ensuring energy security (WEF 2006). Moreover, the change in the urgency or prioritization of energy security over the time period taken in this research may provide an explanation for the change in the explanatory value of the factors over time endorsing the use of the constructivist approach. To this end, the potential change/evolution in the prioritization of energy security by the concerned actors over the time period taken in this dissertation and its potential effect on its strategic behaviour (energy policy) will be determined.

![Energy Security: An Umbrella Term](image)

Figure 3: Energy security: an umbrella term

### 2.6 Data gathering & Information sources

The information used in this dissertation is gathered by desk research (literature review) and also semi-constructed interviews. Semi-constructed interviews provide more flexibility than standardised methods such as the structured interview or survey. Although the interviewer in this technique will have some established general topics for examination, this particular method allows for the exploration for emergent themes and ideas during the interview rather than solely relying on questions defined in advance of the interview (ESDS 2009). Hence, it provides the scope to pursue and probe emergent ideas making this particular method best suitable to gather relevant information. The respondents that are approached range from academics, energy experts and former ambassadors to the former project coordinator of the Nabucco gas pipeline project. For an overview of the interview questions it is referred to appendix A.
2.7 General Demarcation

First of all, the actors will be stated that are involved in the attempt to realize the trans-Caspian gas pipeline or prevent it from becoming reality. The involved state and non-state actors that will be taken into account in this dissertation are: USA, Russia, China, the EU (the European Commission and relevant member countries), Turkey, Iran, Turkmenistan, Kazakhstan, Azerbaijan, Georgia, transnational oil corporations and relevant intergovernmental institutions. All of these actors have a certain role and influence within the ‘New Great Game’ in the Caspian region. The Caspian region encompasses Central Asia and the Caucasus (see figure 4). It will be elaborated upon in detail in the following chapters.

Subsequently, it needs to be cited that Uzbekistan – a gas rich Central Asian country - is not seen as a supplying country for the TCGP. In the future, the lion’s share of the Caspian natural gas export potential will come from Turkmenistan and Kazakhstan (see figure 5 and 6). Uzbekistan’s production share will decline rapidly in the next decade as shown in figure 7. Although Uzbekistan will still be a major regional producer of natural gas for some time, its export potential will become insignificant because of its high levels of domestic consumption, as the most populous state in the region. Moreover, since Uzbekistan is landlocked and since its natural gas competes with Russian, Turkmen, Kazakh and Azeri natural gas, Uzbekistan is limited in its ability to export. Instead, Uzbekistan has concentrated on supplying the Central Asian natural gas market. The fact that in the short term Uzbekistan’s export potential will decline at such a pace that no significant role can be played in the global energy market, led to the decision to leave Uzbekistan out of this research as a potential supplier. In conclusion, from this point on only Turkmenistan and Kazakhstan will be regarded as potential Central Asian suppliers for the trans-Caspian gas pipeline.

Moreover, time plays a central role in this research as such that a distinction has to be made between, short, medium and long term. By short term a timeframe is meant between zero to 5 years. By medium term it is referred to a timeframe between 5 to 10 years. By long term it is meant 10 years and longer.

Figure 4: A political map showing the nations situated in Central Asia and the Caucasus (CIA 2000)
Figure 5: Turkmenistan’s natural gas supply projections (CIEP 2009)

Figure 6: Kazakhstan’s natural gas supply projections (CIEP 2009)
Figure 7: Uzbekistan’s Natural Gas Export Potential Forecasts (RAND 2003)
3 Operationalization of the Case Study Protocol

In this chapter, the Case Study Protocol as provided in Hayes (2004, pp. 22-28) will be made suitable for this specific gas pipeline project, namely the attempt to realize the trans-Caspian gas pipeline project. Moreover, in Hayes (2006, pp. 28) the task was to uncover the factors that have the largest effect on whether a gas infrastructure project is built. In this research, however, the goal is to determine which of these factors have the largest effect on the trans-Caspian gas pipeline project. Taking this into account and the assumption that every case is unique, all the factors will be applied to this specific gas project.

To this end, the following sub research question will be answered in this chapter:

*How should the Case Study Protocol as portrayed in Hayes (2004) be operationalized to analyze an ongoing (dynamic) gas infrastructure project?*

The outcome of this chapter will be the operationalized Case Study Protocol, stated in section 3.7.

3.1 Explanatory factors

In Hayes (2004), four major explanatory factors are identified - beyond simply technological and economic potential – after consulting experts and surveying vast amounts of literature, which could prove to be strong explanations for why certain large-scale gas projects are built and others are not. These factors explain decisions by investors to put money into gas infrastructure projects. These are the following factors: *general investment climate, transit risk, offtake market risk and geopolitical relationship.*

A short but thorough description will be given of each explanatory factor:

There is a shift going on in the *investment context*, from an “old world”, in which state enterprises dominated, to a “new world” where private firms increasingly bear the burden of making investments (Hayes 2006, pp. 28). In this supposedly new world, the investment decisions are increasingly guided by the relative risks across countries rather than by direct state involvement. Private investors find the sunk cost nature of the capital investment in these fixed infrastructure very important. These investments require a long period of predictable operation to recover the original investment and to yield acceptable returns. An effective means to secure the demand and thus the revenue is a long-term contract, which often plays a central role in such projects. However, the balance of bargaining power at the time of contract negotiations shifts to favour the regulators of offtakers when the infrastructure is built (Vernon 1971). Hence, investors have a large interest in the enforceability of contracts, the stability of the business environment and tax codes as well as in the factors that are particular to individual deals, such as repatriation of profits etc.

Second of all, the existence of *transit countries* could mean a significant obstacle to creating viable cross-border gas pipelines. One of the underlying reasons is the fact that transit countries have fundamentally other interests than exporting or importing countries. Transit countries have only their transit fees to lose when actively interfering with a deal, although such behaviour could damage their international standing (Stevens 2003).
Third of all, the project investors could have special concerns about the *offtake market risks.* These risks regard the price and quantity of the gas that can be sold from a given pipeline. Risks arise around the introduction of large quantities of gas in immature offtake markets, which can be averted through large complementary investments in gas-using technologies by potential customers. Furthermore, gas suppliers (and buyers) are threatened by variations in price, depending on the particular contractual and regulatory arrangements. Preliminary evidence suggested that a poorly developed gas infrastructure downstream entails uncertainty and risks for a new gas project. In such a situation, there is considerable uncertainty about whether the necessary investments will be made in the gas-using technology and how gas prices will be regulated. Another uncertainty concerns the rate of growth in end-use gas demand relative to the volumes delivered from the proposed project and other new supplies.

Lastly, another point of concern is the *geopolitical relationship* between supply, transit and offtake countries or better said the lack of it. When the concerned countries have not developed a broader relationship, through for example trade and cross investment, this could lead to a situation in which governments could use their market power to drive up prices or cut off supplies for political purposes. As a result of this possible ‘gas weapon’, private investors and governments may not be eager to see their interests attended by unpredictable neighbours. With respect to this subject, in Hayes (2006) it is explored whether international institutions could help ease problems of international coordination by reducing transaction costs and building confidence. The lack of these institutions could very well both be symptom and cause of the inability to make investments in collective infrastructures.

### 3.2 Overview of insights

In this section an overview is given of the insights obtained in Hayes (2005), the insights obtained in the gas case study review meeting (House 2003) and other sources. At the same time it is pointed out how these insights will be incorporated into the original Case Study Protocol.

#### 3.2.1 Role of the state in Gas trade

An “old world” of gas trade is one in which the state dominates the economy, including the provision of gas and international gas trade is backed by state-to-state agreements. In contrast, the “new world” is defined as one where the role for the state shifts to provider of market institutions that create the context for private firms to take risks and attain rewards from investment in costly infrastructure projects. Although these are ideal types and neither project operates solely in one of these “worlds”, it is useful to expose the underlying forces at work, especially considering the shift to a greater role for private investment in new gas projects. With respect to this topic, first, the insights relating to supply and then to the demand for gas are outlined.

*Role of the State in Gas Supply*

While there is a shift to a greater role for private investment in new gas export projects, geography and (geo)politics have slowed the exit of the state (Hayes 2005, pp. 322-325). It simply reflects the desire of governments to preserve control over the rents that accrue from gas projects. Russia, Algeria and China are good examples with respect to maintaining powerful state-owned companies that dominate gas production and ascribing revenues to the state and its favoured partners. Turkmenistan’s and Kazakhstan’s situation should be probed as to find out to what extent their government plays a role in this context. It needs to be cited
that regardless of the industrial structure, host country governments generally preserve their sovereign controls over taxation, royalty treatment and access to gas resources.

It is important to note that even if the direct role of host country governments in gas export projects might weaken, states still play a critical role in securing an uninterrupted gas flow within the borders and in setting the institutional and legal context within which these multi-billion dollar investments can operate.

Role of the State in “Creating” Gas Demand

The findings in Hayes (2005, pp. 225-230) point out that governments play a critical role in “virgin markets” by creating the necessary demand for new volumes of gas. A virgin market is defined as a market of which gas makes up less than 10% of its total primary energy utilization.

It is not claimed that this role for the state is economically efficient or the only way to create a market, but the historical case studies have shown that this role for the state accounts for a large amount of the observed variation in the timing and completion of first-of-a-kind gas projects. This valuable insight should be incorporated in the Case Study Protocol by researching the actual role of the state in creating gas demand and particularly the role of building gas grids in the offtake markets on the condition that the markets are considered a virgin market. This addition should not only be apparent in the first phase of the analysis but also in the succeeding second phase as the Nabucco gas pipeline is considered a first-of-a-kind gas project connecting the Central and East European markets, which may or may not be virgin markets as it should be analyzed accordingly, to the natural gas resources in the Caspian basin.

3.2.2 Credibility of long-term commitments and Security of Supply

In the “old world” the concerns of gas trade are centered around assuring firm deliveries of contracted volumes. In this context, the long-term contract for guaranteed deliveries was designed to mitigate these concerns. A take-or-pay clause was specifically drafted, committing the buyer to pay for a specified volume of gas, whether or not he actually takes delivery, usually over a period of 20-30 years. The pricing formulas included provisions for renegotiation and were linked to prices of oil products it replaced in the end-user market. This is the so-called “netback” pricing scheme. Then there is the rise of the share of the LNG trade and the dimension in the spot market in the total gas trade as it could enable a shift to a more global market (Constantini 2005). However, the bulk of the gas trade now and for the foreseeable future it is expected that it will still be supplied by gas pipelines connecting regional markets (IEA 2002) and thus long-term contracts are expected to remain the prevailing way of contracting.

“Obsolescing bargain”

Important to note is the concept of “obsolescing bargain”, which gains its significance in a world where the investments in gas infrastructure projects are increasingly being made by corporations. Before the project is built, potential investors are in power, having scarce capital and technologies required for the project. After a deal is struck between investors, gas buyers and host countries, the capital has ‘sunk’ into developing gas fields and constructing export infrastructures. After the realization, the constructed pipeline or LNG facility has no alternative use as a result of which the leverage switches from the investors to the gas buyers, the host country government and the transit countries (Vernon 1971). Below the insights

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12 A first-of-a-kind gas projects is one that differs from another project in terms of geographical location, technological application etcetera.
obtained related to ‘obsolescing bargain’ will be explicated as it is subdivided into gas suppliers, transit countries and gas buyers.

A supplier’s ‘gas weapon’

The findings suggest that based on the seven case studies there was only one case that strategically made efforts to drive up gas prices i.e. Algeria in the early 1980s (Hayes 2005, pp. 333). All the other cases reflect more complicated issues and are the by-product of other factors such as internal conflicts that spill over to disrupt exports. All in all, it is concluded that the gas weapon is rarely used due to the fact that all major gas markets are fundamentally replaceable over the long term by alternative suppliers or alternative fuel sources. The harm it does to the reputation of a country can result in being locked out of lucrative markets for a generation or longer. In short, the lesson that should be taken into consideration stems from the case of Algeria; the shifts in political regimes and the limited time-horizons of leaders who aim to upset existing orders may pose a continued threats to stable gas exports. This is especially true for Turkmenistan where the power is centralized in the hands of one person, namely the President, making it an unreliable partner. Both potential host countries should be examined as to determine the risk of irrational strategic manoeuvres due to regime change and limited time horizon of the leaders.

A transit country’s ‘gas weapon’

Moreover, the findings suggest that interruptions due to opportunistic behaviour in transit countries are few and occur mainly as unintended by-products of broader disputes (Hayes 2005, pp. 333). However, based on the dissertation that every case is unique, it is decided to take this specific factor into account anyway. To this end, the various transit countries in this dissertation will be examined; it will be examined whether they have shown opportunistic behaviour in the past and whether this behaviour have contributed to the failure of the first attempt to realize the trans-Caspian gas pipeline.

A buyer’s gas weapon?

The case studies involve more examples of interruptions and renegotiations of contracts urged by users than suppliers and transit countries. The findings point out that if a gas buyer has suitable energy supply alternatives and they are the sole buyer (as in a pipeline project), they are in the position that they can renegotiate prices and volumes. This monopsony power particularly lies in wait as the operating costs of any project are a small fraction of the already sunk capital cost. This implies that gas suppliers are willing to sell for a fraction of the cost required to fully require their investment. The buyers in this specific case should be examined as to find out whether or not they possess a monopsonist position and if they have used it in the past. To this end, its implications on the realization of the TCGP will be explored.

Upholding terms of agreement over the life time of the project

Typical gas export projects require allocating more than half of the capital investment in the export country itself in field development, pipelines and processing equipment. In this respect, most of the world’s gas reserves are in countries where institutions for enforcing commitments are weak, politicized or nonexistent. Investors in gas pipeline projects are ardently aware of the motivations and opportunities for host country governments to shirk contracts. All else equal, investors prefer to operate in states that can most credibly signal their commitment to uphold original bargains. In this respect, the reputation of the host countries will be examined as the most obvious way for a government to indicate its ability to
sustain a commitment is through its past actions. It will be determined if and if so to which extent this aspect has played a role in impeding the first attempt to realize the TCGP.

**Energy Charter Treaty**

With respect to adherence to international legal norms and the adherence to international arbitration, the Energy Charter Treaty (ECT) could play a role of significance. The launch of the Energy Charter Treaty, which strengthens the rule of law on energy issues by creating a level playing field of rules adhered to by all participating governments, could prove to be a powerful instrument to create investors confidence\(^\text{13}\). For that reason it will be examined whether the ECT has played or is playing a role in the attempts to realize the TCGP and if so to which extent.

### 3.2.3 Insights on the four major explanatory factors

It is found on the basis of the historical case studies in Hayes (2006) that the investment climate is very important, especially considering the shift to a “new world” in which a greater role is reserved for private investors and competitive gas markets. The influence of this factor will be thoroughly investigated regarding the failed first attempt to realize the TCGP and also in the succeeding phases. Moreover, the findings suggest that the time horizon of the leaders should be probed. This is reinforced by the existent autocratic rule in these former Soviet Union countries.

With respect to transit countries there was not any broad evidence found that they were likely to act to “hold up” shipments for political or economic gain. However, on the basis of the argument that every case is unique this factor will be treated for this specific project. Moreover, there are sound examples such as the Russia-Ukraine gas crisis (Pirani 2007) and Russia-Belarus oil crisis (BBC 2007) demonstrating that it can occur.

The initial hypothesis regarding offtake markets was that projects that served well-developed markets would entail lower financial risks and would allow a rapid construction due to the fact that a robust market allows easier absorption of new volumes. However, the findings in Hayes (2006) point into another direction; the risks in the offtake market are mainly a function of government energy policy. The role of the state is considered critical in virgin markets\(^\text{14}\). Therefore the following question should be added: *Are the offtake markets considered ‘virgin markets’ and is the importing country government willing to spend the political or economic resources needed to advance gas use?* There are uncertainties about the fact if the private investors will jump in to fulfil this role. This entails a thorough investigation of the offtake markets as the extent of its (possible) influence on the realization of the TCGP should be probed.

Furthermore, the international institutions (intergovernmental organizations) did not play much of a role in the development of these gas trade projects. Rather, these massive projects operate outside pre-existing treaties and the imperative for energy trade can operate on its own logic. This will be examined nonetheless based on the view that every case is unique. Moreover, the case studies did show, however, that international financial institutions

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\(^\text{13\url{http://www.encharter.org/index.php?id=7}}\)

\(^\text{14\ It entails that a state depends on natural gas for less than 10 percent of its primary energy supply}\)
(multilateral lending agencies) such as the World Bank\textsuperscript{15} or other private banks have had a profound impact on projects in cases that they have financed a substantial amount of the project costs, which otherwise would not be able to attract capital. These multi-lateral lending agencies often also provided other loans or support to the host-country government as the banks used the threat of curtailment of these other services to sustain the agreed framework for the oil and gas project. Comparably, investors may engage private banks to supply capital. Even the investors with deep pockets could be drawn to that option because the host country may be reluctant to stiff banks with which they want to sustain broader lending relationships.

### 3.2.4 Insights from the Case Study Review Meeting

Mentioned briefly in Hayes (2006) and further emphasized in the case study review meeting (House 2003), convened to review these case studies, was the emergence of the factor “resource curse”. The question whether or not the resource curse applies to natural gas was raised. A particularization of the resource curse is the notion that the presence of petroleum and mineral wealth generally delays or even blocks the politico-economic development. Specifically it entails that a state and economy, which is dependent on these sources for its wealth has an increased chance to experience difficulties in developing both a democratic government and a market-based economy (Goorha 2006). This phenomenon could lead to civil unrest and thus result in the inability to assure local security. However, there are projects in Nigeria and Venezuela that have fully developed plans to supply local communities with water, power and health care. This fact may suggest that gas projects may be less likely to have the ills of the “resource curse”. Without proving whether or not the resource curse is applicable to natural gas, it will be probed what the possible implications of the resource curse may be on the domestic governance and thus on the already fragile domestic stability of Turkmenistan and to a lesser extent Kazakhstan. This will be incorporated into the Case Study Protocol in terms of adding concrete research questions.

### 3.3 Overview of the concerned actors

Moreover, also the specific features of this particular gas pipeline project need to be considered when operationalizing the Case Study Protocol. In table 1, as a result of a preliminary investigation, an overview is given of the actors that were and are involved in the first and current second attempt to realize the trans-Caspian gas pipeline project. In the following sections, this overview will be explicated in terms of the actors’ actual role and involvement in the project. For a more detailed analysis of the actors’ interests and strategic behaviour it is referred to chapter 4 and 5.

<table>
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<tr>
<th>Host countries</th>
<th>Transit countries</th>
<th>Offtake countries</th>
<th>Other involved countries</th>
<th>TNOCs</th>
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<td>Turkmenistan</td>
<td>Azerbaijan</td>
<td>Georgia</td>
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<td>International Consortium</td>
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<tr>
<td>Kazakhstan</td>
<td>Georgia</td>
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<td>United States of America, Iran, European Union, China</td>
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Table 1: The concerned actors in the attempt to realize the trans-Caspian gas pipeline project

\textsuperscript{15} In the Gasbol project, for example, the World Bank chose to provide financing as part of its broader agenda focused on Bolivian development and regional integration. The strong position of the World Bank in these two countries, particularly Bolivia, provides a strong incentive for the governments to uphold the terms of the Gasbol contract.
3.4.1 Host countries

In the first attempt to realize the trans-Caspian gas pipeline (TCGP) project, Turkmenistan was the primary potential supplier for this pipeline (CEE 2001). For that reason Turkmenistan alone is considered in the first phase. Kazakhstan on the other hand, has just recently in 2005 become a net exporting country of natural gas and has the prospects of exporting 15 bcm of natural gas in 2010 (Ögütçü 2006, pp. 1). Hence, Kazakhstan is added as a potential host country for the TCGP in the second attempt together with Turkmenistan. Moreover, gas suppliers (and buyers) are threatened by variations in price, depending on the particular contractual arrangements and for regulating the prices. In this respect, the potential influence of the liberalisation of the EU gas market on the first attempt to realize the TCGP ought to be researched.

3.4.2 Transit countries

In the first attempt, only the countries Azerbaijan and Georgia were considered as transit countries (CEE 2001). Although delivery to the European markets was considered, it was merely a future prospect and no concrete plans were made yet to build a gas pipeline connecting Turkey with Europe. These concrete plans to connect the Caspian and the Middle East region with Europe were made after the first attempt in the time period of the second phase through the possible construction of the Nabucco gas pipeline (Nabucco 2008). Hence, the central and east EU countries Bulgaria, Romania and Hungary together with Turkey are taken into account as a transit country in the second phase of the analysis (see chapter 5). Also in the second phase, with the addition of Kazakhstan as a potential supplier to the TCGP, Turkmenistan will have to function as a transit country as well, considering that the pipeline may originate from Kazakhstan and run through Turkmen soil before crossing the Caspian Sea over to Baku, Azerbaijan. These transit countries will be analyzed according to the transit risk section stated in the Case Study Protocol. Moreover, the transit country’s reputation is investigated and whether they have engendered any impediment using their position during the negotiations in the first attempt.

3.4.3 Offtake countries

In the first attempt, Turkey was regarded the main offtake market at least in the short term (Açikalin 2001). During the first attempt delivery of Turkmen gas to the European markets was considered but it was merely a future prospect. In the second attempt, however, also the European Union member countries Bulgaria, Romania, Hungary and Austria including Turkey are regarded as offtake markets, connected through the potential implementation of the Nabucco gas pipeline project. These offtake countries will be included into the Case Study Protocol in the second phase of the analysis (see chapter 5).

3.4.4 Global and regional power(s)

In the first attempt, USA and Russia were respectively the main global and regional powers engaged in respectively stimulating and blocking the realization of the trans-Caspian gas pipeline. Furthermore, also Turkey and Iran played their part as a regional power as the latter was opposing the project. In the second attempt, however, the list of powers competing for hydrocarbon resources in the Caspian region has increased. It has witnessed the entrance of the European Union and of China into the ‘New Great Game’ (see chapter 5).
3.4.5 Transnational oil corporations

Considering the switch from the “old world” in which state enterprises dominated to a “new world” where private firms increasingly bear the burden of making investments, the role of transnational oil corporations (TNOCs) cannot be ignored. In the first attempt, an international consortium was formed constituted by transnational oil corporations to implement the trans-Caspian gas pipeline project (Cutler 2003, pp. 25). Its role and influence should be taken into account in the Case Study Protocol in the section ‘geopolitics’.

3.4.6 International financial institutions

In the first attempt, the involvement of international financial institutions and its influence ought to be examined as it can provide some protection for the project investment in the resource-rich but institution-poor host countries. More importantly, they can play a key role in providing finances for a project where the TNOCs are reluctant to take the financial risk because it is haunted by many uncertainties such as controversies about the economic viability, a bad investment climate, unknown gas reserves etcetera.

3.5 Problem owner: Turkey

Furthermore, since Turkey is the problem owner in this research, its role and influence within the context of the ‘New Great Game’ will be analyzed thoroughly. To this end, Turkey’s relations with the other involved actors will be analyzed as to find out to what extent Turkey’s interests and foreign and energy policy objectives compete or coincide with the rest of the actors. Moreover, the role and potential influence of the cultural, linguistic and ethnic connection of Turkey with Turkmenistan on the first attempt to realize the TCGP shall be determined as well. Turkey as a problem owner will be the focus point in all of the three phases of the analysis.

3.6 Geopolitics of gas

The scope of geopolitics as it is applied in Hayes (2006), namely as geopolitical relationship, is not suffice to explain the exact influence of this explanatory factor. Especially considering the geographic location from where the gas has to originate (the Caspian region) where geopolitics notably flourishes as the competition in this region is dubbed into ‘The New Great Game’. Therefore it is stated that the scope of the section ‘geopolitical relationship’ in the original Case Study Protocol (see appendix B) must be widened to include the study of ‘geopolitics’. The meaning that is given to ‘geopolitics’ in this research is the influence of geographic, demographic, economic and technological factors on political outcomes and vice-versa (Hayes 2005, pp. 6-7). In this rather broad definition, relative gains matter, however, also substantial gains matter from possible cooperation. Since technology, geography and political choices direct gas trade along one route to the expense of another, so are investment and revenues diverted as well, with considerable political and economic consequences. States that have committed themselves to importing large quantities of natural gas place their security partly in the hands of others. In turn, this gives both suppliers and users a stake in the political and domestic stability of one another. This is what is meant by
“geopolitics of gas”, not just the zero-sum jockeying for global position\textsuperscript{16}, but also the extremely political actions of states and non-state actors (TNOC’s) who determine which gas infrastructure projects will be built and how the gains will be allocated (Hayes 2005, pp. 7). Furthermore, geopolitics is applied within the context of the “New Great Game” in the Caspian region. The conditions for the “New Great Game” were laid after the dissolution of the Soviet Union as a result of which various states in Central Asia and the Caucasus have proclaimed their independence. This has brought a new struggle for influence as this time it focuses in particular on the struggle for the hydrocarbon resources between the global and regional powers. This will be discussed thoroughly both in the first phase of the analysis as well as in the second phase.

Moreover, it is asserted that additional project specific and regional/country specific sub factors with a profound impact on this project are explained by geopolitics, which will be taken into account as well. Furthermore, it needs to be mentioned that by widening the scope of the geopolitics factor, the portrayal of a certain level of entanglement with the other factors is unavoidable and needs to be taken into consideration. Furthermore, the extent to which the involved states are in favor or against this project is identified and explained as to find out the driving forces behind their strategic behavior.

3.7 The Case Study Protocol operationalized

In this section, the Case Study Protocol (Hayes 2004) will be adjusted and supplemented in conformance with the insights in the aforementioned sections. It needs to be pointed out that this adjusted Case Study Protocol solely applies to the first phase as for the second phase it will be further adjusted and supplemented.

First of all, some general information about the trans-Caspian gas pipeline project ought to be given in order to get a sufficient notion of the project. Therefore the following questions will have to be answered:

1. When was the trans-Caspian gas pipeline project first proposed? What was the scope of this project?
2. Who were the motivating actors (e.g. supply country government, receiving country government, domestic private investor, foreign investor, or international financial institution)? Which actors were “active” supporters vs. passive supporters. Who were the involved countries in this project (host countries, offtake countries and transit countries)?
3. What was the length, diameter, projected construction time and projected cost of the TCGP project? What was the projected route of the trans-Caspian gas pipeline?
4. How would the TCGP project be financed (European Investment Bank, World Bank, private investors, governments or a combination of these)?

In this section only the adjusted and supplemented part of the Case Study Protocol as provided in Hayes (2004) will be outlined. The remaining part (the original Case Study Protocol) as taken from the aforementioned source can be found in Appendix B.

\textsuperscript{16} In this view of international politics, prevalent especially during the Cold War, countries are primarily concerned about gains from trade, investment, and military action relative to other national competitors. Greater territory and resources for one party necessarily create a loss for others.
- Investment climate of Turkmenistan in particular in the first attempt (1997-2001)

The case study regarding the TCGP should provide an overview of the broader investment climate of the host country Turkmenistan in particular. This should include a description of political, security, economic, and legal contexts during the period in which the project was attempted to be realized and also relevant historical information should be provided.

Domestic Security and Political Context
The level of political and constitutional stability within the host country should be described.

The domestic security context should entail the discussion about the general state of mind of the population with regards to their own everyday life and the way the country is being led by their leaders. It should be examined to what extent the constitutional rights of the people are safeguarded and also whether there is risk of widespread civil unrest under the population and fear of revolution that could result in expropriation. As a result the following question should be answered: Are there any organized separatist groups in the host countries endangering the ability of the government to assure local security and how have they manifested themselves in the past? Moreover, the possible impact of the ‘resource curse’ should be examined as well; what are the possible implications of the ‘resource curse’ on the already fragile domestic stability of the host countries? Furthermore, it should be examined what its effect is on fuelling the discontent under the separatist groups or on fuelling the civil unrest? Moreover, it should be researched whether the oil and gas companies are privatized or whether they are state-owned companies. To this end, the following questions ought to be answered: to what extent are the interests of the host country government intertwined with the interests of the incumbent oil and gas companies and what is its influence on the functioning of the incumbent company regarding attracting foreign investment in the energy sector?

One should also describe the energy security issue and the risk of the political electorate to use its supplier position as a “gas weapon”. In this context the past of these countries should be probed: what is the reputation of these countries with respect to upholding contracts concerning large-scale projects that are capital intensive and have a long pay-back time and what is the time horizon of the leaders?

Domestic Macro-Economic Context
One should describe the macroeconomic situation in the host countries as the following questions should be answered: what were the projected growth rates of the overall economies; what were the economic risks (exchange rate, uncertain growth prospects, etc.) and the projected needs for energy services in the offtake countries that would be served by the projects; how did the projects fit into the strategic energy plans of the governments?

“Rule of Law”
The case should discuss the development of the “rule of law” in the upstream countries (Turkmenistan) with respect to upholding contracts and its credibility to long-term commitments17. In this respect, the following ought to be answered: has the host country in the past used its position after the project was realized (obsolescing bargain) to renegotiate contracts and if so did it have an impact on the failed first attempt?

17 The downstream and transit markets obsolescing bargain’ will be treated respectively in the offtake market risk and the transit risk section.
One should also describe the historical track record on upholding contractual agreements and the role and independence of the judiciary in deciding disputes. The adherence to international legal norms and international arbitration ought to be explicated where utilized prior to the proposal of this infrastructure project.

**Regulatory**

Each case should analyze the *ex ante* and status of regulation in upstream, downstream\(^{18}\) and transit markets (where relevant). In this respect, gas suppliers and buyers alike are threatened by variations in price, depending on the particular contractual arrangements and for regulating price. Relevant information would include any laws governing the price and quantity of gas sales outside of the project in question. In this respect, the following question ought to be answered: *did the liberalisation of the EU gas market, a market open to private and foreign ownership and investment with prices flexible for any particular project, have an impeding effect on the first attempt to realize the TCGP?*

Environmental legislation and laws concerning indigenous peoples and protected lands are also critical issues for siting, constructing, and operating a gas pipeline. The case study should especially explore the environmental and ecological problems that were deemed potential obstacles in the construction and operation of the TCGP considering that it will cross the Caspian Sea. Furthermore, any particular social problems should also be explored.

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**- Transit countries (Azerbaijan and Georgia)**

Regarding this factor, it ought to be explained how the number and type of transit countries affected the outcomes. In this respect, the following needs to be answered: *have they used their position as a leverage to increase their transit revenues or for other purposes and have they been involved in a gas project as a transit country before and if so what is their reputation?*

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**- Offtake market risk (Azerbaijan, Georgia and Turkey)**

Each case study should explain evolution of the off-take country’s gas market and examine the risk that the off-take market would be unable to absorb the quantity of gas supplied by the project. In this respect, one should examine whether take-or-pay clauses would be included in the contract or other arrangements used to reduce these risks and with what effect.

Moreover, one should also examine what *the role of the state is in the off-take countries in creating gas demand and particularly in building gas grids*. In this respect, it should be determined *whether the offtake markets are considered ‘virgin markets’*. The role of the state is considered critical in virgin markets. There are uncertainties about the fact if the private investors will jump in to fulfil this role (Hayes 2005).

Furthermore, the risk that the offtake countries could use their position as a monopsonist power to renegotiate supply volumes or prices should also be explored (obsolescing bargain). A buyer is most likely going to use its ‘gas weapon’ to renegotiate prices if it has suitable energy supply alternatives and is the sole buyer of this gas (monopsonist position). As regards this, the following question needs to be answered: *has the outlook for this possible*

\(^{18}\) Its regulatory environment is treated in the offtake market risk section
monopsonist behaviour played a role of importance during the first attempt and if so what was its influence?

- **Geopolitics of gas**
  "Geopolitics’ is the influence of geographic, demographic, economic and technological factors on political outcomes and vice-versa. In this broader definition, relative gains matter, but so do the substantial gains from possible cooperation.

**Geopolitics within the context of the ‘New Great Game’ in the Caspian region**

This factor investigates the geopolitics of natural gas within the context of the ‘New Great Game’, with key roles for the littoral states to the Caspian Sea basin which are Russia, the Central Asian states Kazakhstan and Turkmenistan, Azerbaijan and Iran. Furthermore Turkey, the European Union, the USA and China are actively involved participants in the struggle for Caspian natural gas. Nevertheless, the EU and China come into the picture in the second phase of the analysis.

Since Turkey is the main actor in this research, its role and influence during the first attempt of implementing the TCGP should be determined and explained. To this end, the driving forces (interests and identity) behind its foreign and energy policy will be determined (as those are inextricably linked to one another) and so will its influence in relation to the involved actors in terms of economic, political (diplomatic) and ideational power (Nye 2004). It will be started from the break-up of the Soviet Union that resulted in the unavoidable stance for Turkey to redefine its role in the region and reshape its foreign policy. This analysis will contribute to understanding Turkey’s role and influence in the region within the context of the ‘New Great Game’ and in specific the attempt to realize the TCGP. In the time period taken in this research Turkey’s energy security policy and foreign policy objectives together with its role and influence in the ‘New Great Game’ might have changed. This will be researched accordingly in the second phase of the analysis. Furthermore the following questions will be treated in the first phase: did Turkey during the first attempt have an active or a rather passive role and why? What was Turkey’s relations with all the involved actors? To what extent did Turkey’s interests compete or conflict with the interests of the other involved actors? Which actors were considered allies and why? What kind of measures did Turkey undertake to influence the first attempt to implement the TCGP? To what extent did Turkey’s cultural, ethnic and linguistic relations with Kazakhstan and Turkmenistan influence the first attempt to realize the TCGP?

Moreover, it is necessary to identify and explain the extent to which the involved states are in favor or against this project and thus find out the driving forces behind their strategic behavior. To this end, the following question should be answered: how will the realization of the TCGP influence the ability of the relevant actors to achieve their primary objectives given the context of the “New Great Game”? Furthermore, energy security (policy) plays an important role in the state’s ultimate desire to survive and be secure (national interest) and thus plays a prominent role in explaining the actors’ interests and strategic behaviour. Therefore, in the first phase of the analysis the influence of a state’s energy security objectives on its interests and strategic behaviour (energy policy) will be analyzed.

Moreover, the additional project specific and regional/country specific (sub) factors with a potentially profound impact on this project will be analyzed as well in the geopolitics section, since it is believed that it can be explained by geopolitics as such.
**Institutions and their influence**

The ability to complete investments in cross-border infrastructures may also depend on how well host countries engaged in a particular project are able to cooperate on and manage collective issues and conflicts. To this end, bilateral and multilateral agreements ought to be probed and its effectiveness should be assessed.

The following questions need to be answered: *How well are the host countries’ economies integrated with the transit and the offtake countries? Have they cooperated on or managed collective issues and conflicts before? Which bilateral or multilateral agreements or treaties have been signed and for which purpose? What was the influence of this on the first attempt to realize the TCGP?* The operation and effectiveness of the Energy Charter Treaty (ECT) during the first attempt should be probed: *has this treaty or other treaties have played a role in creating investors confidence?* It may be useful to detail the history of cross-border conflicts or collective action by the host countries and to explore the roles of institutions in resolving the conflicts. One should be mindful that effective cooperation might not take place entirely through formal institutions. It is also important to review the expectations about the likely futures for cooperation with host countries, especially in the aftermath of the declaration of independence of both host countries in 1991 having detached themselves from the Soviet Union. As regards this the following question needs to be answered: *how, if at all, did those expectations influence or reflect the official foreign policy, security and social goals of the host country governments?*
4 Analysis of the failed first attempt (1st phase)

4.1 Introduction

The central aim in this chapter is to determine which factors, to what extent and under which conditions have contributed to the advancement and especially impediment of the failed first attempt of the TCGP in the period of 1997-2001. This will be done by means of the operationalized Case Study Protocol (see section 3.7). Moreover, the results of this first phase will be taken as a reference point for the subsequent phases (see figure 2). Along the way, whether it is in the first or in the subsequent phase, there is a high likelihood that also explanatory project/regional specific or other additional (sub) factors will emerge. These (sub) factors will also be analyzed in terms of influence. Moreover, since Turkey is the main actor in this research, its role and influence during the first attempt to realize the TCGP will also be investigated according to the operationalized Case Study Protocol.

This phase in essence provides the answers for the following sub questions:

*To what extent and under which conditions contributed the four ‘explanatory factors’ to the advancement and especially impediment of the failed first attempt of realizing the TCGP in the period of 1997-2001?*

*What was the role and influence of Turkey during the first attempt to realize the TCGP?*

The outcome of the first phase is a discussion about which factors to which extent and under which conditions have advanced and especially impeded the first attempt. In addition, it will also provide the results from the Turkey specific analysis. These results (output) will be the input of the second phase of the analysis (see figure 1).

4.2 General information about the TCGP project

The trans-Caspian gas pipeline (TCGP) project was initiated in 1997. It is a 1600 km pipeline system that would run from the Shatlyk and Dowletabad fields in eastern Turkmenistan and could possibly extend to other supplying fields as well. The pipeline would go across the Caspian Sea to Azerbaijan, Baku, onward through Georgia to Erzurum, Turkey (Ögütçü 2001) (see figure 8). Then it would be linked to the principal Turkish gas transportation grid. Both fields have been exploited for very long and could have a sustainable production for the TCGP for many years. Exports from these fields were more than 50 billion cubic meters of gas per year to Russia and Ukraine since the early 1980s. The immediate offtake market was meant to be Turkey, but Europe was considered as well, though in the long-term. It was planned to be developed by an international consortium of Amoco and a new pipeline joint venture owned by affiliates of GE Capital and Bechtel Enterprises (PSG) and later joined by Shell. Working with Botaş, the Turkish national pipeline company, Bechtel had completed the technical and economic feasibility studies for the project. The costs of the pipeline were estimated at around $2.4 billion and the term of construction was set at 3 years. The planned capacity in the final stage was to be 30 billion cubic meters a year with the prospect that 16 bcm per year would be delivered to the Turkish market and 14 bcm would be re-exported to Europe for hard currency to be remitted to Turkmenistan (Ögütçü 2001). The legal grounds for the project were laid down by a Framework Declaration signed by the presidents of Turkmenistan, Azerbaijan, Georgia and Turkey in mid-November 1999 at
the OSCE summit in Istanbul. This declaration was also signed by U.S. President Bill Clinton to show the U.S. commitment that it supported the construction of the gas pipeline (CEE 2001).

Figure 8: Map showing the route of the trans-Caspian gas pipeline (Stratfor 2006)
4.3 Investment climate

In this section, the factor investment climate and its influence on the first attempt to realize the TCGP will be examined according to the operationalized Case Study Protocol. The assessment of the investment climate is made by taking into account several (sub) factors. This section will be focused on Turkmenistan in particular, since it was the only host country during the first attempt. First of all, Turkmenistan’s political and economic life will be analyzed. Secondly, the potential implications of the ‘resource curse’ on the domestic governance will be looked upon in detail. Then, the legal regime of the energy sector in Turkmenistan is analyzed as to determine its influence on the first attempt. Lastly, the potential influence of the liberalisation of the EU gas market on the first attempt is analyzed.

4.3.1 Turkmenistan’s political and economic situation

Political stability

Following the dissolution of the Soviet Union, Turkmenistan became an independent country on December 25, 1991 (Olcott 2004). It is governed by a constitution that was adopted in May 1992, which concentrates all the political power in the office of the President. There is no post for a vice president or a prime minister. The first President of Turkmenistan was Niyazov, which was in office during the first attempt. The President can best be described as highly authoritarian and very unpredictable and opaque in its behaviour. The President nominates all the candidates for the People’s Council, he chooses the members of the Cabinet of Ministers, the country’s leading judges and the heads of the provincial, municipal and local administrations. Politically speaking, it is a highly authoritarian state. The Kalkh Maslakhaty (The People’s Council) and the Mejles (Parlement) are not permanent legislative bodies. Instead they are summoned annually or at the wish of the President. There is virtually no free press. In 2002, the Special Representative of the Organization for Security and Cooperation in Europe (OSCE) recapped the situation in Turkmenistan by saying there existed an “absolute lack of any freedom of expression… unseen in the OSCE region since the establishment of the organization” (EIU 2003). It has been described as a “sultanistic regime”, a category of regimes first named by Max Weber and characterized by personal rule, large-scale corruption and manipulation of fear and rewards (Sabonis-Shelf 2005).

When probing the past of Turkmenistan in order to find out what its reputation is with respect to upholding contracts, it can be concluded that no substantial evidence is found that endorses a bad reputation on this issue. Nevertheless, this might have changed over time as it should be taken into account in the second phase of the analysis. Moreover, the concentration of power in the office of the President (political structure of Turkmenistan) combined with the opaque and capricious nature of Niyazov caused major stalemates in the first attempt. For example, President Niyazov put out an unreasonable condition as he demanded that the international consortium had to pay $500 million upfront, which created frustrations to the parties in the project (Cutler 2003). Furthermore, Niyazov during the first attempt in May 2000, in the climax of the negotiations, committed to supply vast volumes of gas to Russia. As a result, Turkmenistan would be unable to supply the TCGP while at the same time pumping a substantial amount of gas to Russia, at least not from the same gas reserve. The data about the actual amount of gas available in the concerned and other gas reserves was uncertain. This had severely hurt the TCGP and frustrated the involved actors even more. For this and other examples of highly opaque and unambiguous behaviour from the side of President Niyazov see Appendix D.
Moreover, President Niyazov had a reputation of being a ruthless dictator, who did not tolerate any political opposition and violated the freedom of assembly (Sunder-Plassmann 2002). A case (one of many) illustrative to this statement and the discontent under the population is the crushing of a peaceful demonstration of hundreds of people on the morning of 12 July 1995 (Sunder-Plassmann 2002). In addition, although there were indeed organized separatist groups, such as the National Democratic Movement of Turkmenistan and the Republican Party of Turkmenistan (CIA 2008), they were exiled and operating from abroad. These groups have had no effect whatsoever on endangering the ability of the government to assure local security. All in all, during the period of the first attempt to realize the TCGP, the risk of having a widespread civil unrest resulting in revolution and eventually expropriation was considered improbable at the least. The domestic arena was under tight control of President Niyazov and thus there was no fear of domestic instability in the country.

Another aspect that deserves attention in the short to medium term, which would be a key threat to Turkmenistan’s domestic governance and political stability, was the sudden death of the President Niyazov since Turkmenistan does not have a sufficiently developed level of institutionalization. This regime does not have institutions of succession to rely on when the current leader passes away, underlining the Turkmen president’s limited time horizon. Therefore a succession may become a catalyst for unrest and civil strife endangering the investment climate and since Russia and Iran both have interests in the stability and security of Turkmenistan, a period of chaos could leave both Russia and Iran tempted to intervene. Although the risk of sudden death was not an issue in the first attempt, it could very well be an issue in the second phase.

**Economic stability**

Turkmenistan has a static, highly indebted economy. Its currency remains unconvertible and hence the legal and black-market exchange rates have a great discrepancy. By Turkmen reporting, real GDP has exceeded 1989 levels since 2001, due to increased gas exports through Russia, although the economic data coming from the republic should be viewed with suspicion (Shiells 2003). The country’s gross domestic product (GDP) is export driven, with the principal commodities (gas, oil and cotton), which are still largely state controlled. Inward FDI flows into Turkmenistan during 1997–2001 averaged around $110 million per year and it were mainly in the form of production sharing arrangements\(^{19}\) (PSAs) in the oil sector and joint ventures\(^{20}\) in the non–oil sector, although the latter were very modest mainly due to non–supportive government policies (Shiells 2003). In the oil sector, FDI inflows were well below the amount needed to achieve the government’s annual production targets. Apparently this was due to disappointing results of recent Caspian Sea oil exploration efforts and the ongoing territorial disputes between Turkmenistan and Azerbaijan concerning the legal division of the Caspian Sea (see section 4.6.7).

Its private sector accounts for less than a third of the country’s GDP. Furthermore the participation of ordinary Turkmen in the private sector is severely hampered by sharp

\(^{19}\) In a PSA, the oil (and gas) is legally in hands of the state giving it ultimate control over it, while a private company or consortium of companies extracts it under contract. In practice, however, the actions of the state are severely constrained by stipulations in the contract. The private company provides the capital investment in exploration drilling and the construction of infrastructure. The first proportion of oil (and gas) extracted is allocated to the company, which uses the sales to recoup its costs and capital investment. Once costs have been recovered, the remaining ‘profit oil’ is divided between state and company in agreed proportions. The company is usually taxed on its ‘profit oil’. There may also be a royalty payable on all natural resources produced.

\(^{20}\) Joint Venture is defined as an activity carried out by an aggregation of persons, without constitution of a new legal entity, jointly participating in the supply of technical and financial resources for implementation of the contract entered into between the competent body and such aggregation.
restrictions on access to foreign exchange. Its banking sector is weak and state dominated (Olcott 2004). The Turkmen government is committed to both privatization and land reform and the government has announced to implement a series of laws designed to encourage private investment in the country. However, Turkmenistan’s legal system provides little protection of private property. This has stifled foreign direct investment, even in the oil and natural gas sectors. Some 90% of all FDI is in the oil and gas sector (Shiells 2003).

One potential problem for the trans-Caspian gas pipeline is Turkmenistan’s economic health. During the first attempt the country’s financial troubles had the ability to make matters more difficult. It needs to be said that Turkmenistan’s grip on fiscal health has been slipping since March 1997, when it lost access to its traditional gas export pipelines after a pricing dispute with Russia. In this respect, officials of the U.S. Export-Import Bank have raised doubts about Turkmenistan’s ability to service its debts (Lelyveld 1999). Under its charter, the bank could not provide financing or loan guarantees unless it had a reasonable assurance of being repaid.

Impact on first attempt

The political structure of Turkmenistan, which enables a concentration of the power in the office of the President, is a source of trouble for the domestic, political and economic stability of this country. This is especially risk full when it is combined with a President who is highly authoritarian, opaque and non-pragmatic in his behaviour as was the case with President Niyazov. Niyazov was reluctant to distance himself from the power he enjoyed and to implement democratic reforms.

President Niyazov has created obstacles and put unreasonable conditions impediment the realization of the trans-Caspian gas pipeline project. Furthermore, although Turkmenistan has a history of violating human rights, this did not have any effect on the internal stability, at least not in the period of the first attempt. This does not mean, however, that this will remain the same in the future. Hence, it must be taken into account in the subsequent phase. In addition to this, another aspect needs mentioning is the underdeveloped state of institutionalization, which could be the cause of civil unrest and strife when its President dies a sudden death. Though this is not relevant for the first phase, it is a factor that could prove to be highly influential in the second phase and thus needs to be taken into account.

Turkmenistan’s private sector is small, its legal system provides little protection for private property and its banking sector is weak and state dominated. During the fist attempt one of their most important sources of income had been cut due to gas pricing disputes with Russia. As a result, Turkmenistan’s fiscal health was a growing concern. The U.S. Export-Import Bank was worried about Turkmenistan’s ability to service its debts. Under its charter, they are not allowed to provide loans if there is not a reasonable assurance of being repaid, while the participation of these lending agencies are seen as crucial both for financing and the commitment of political will.

4.3.2 Legal regime of the energy sector and its governance in Turkmenistan

By means of this section, the legal regime of the energy sector in Turkmenistan and its influence on the first attempt will be investigated.

First of all, it needs to be mentioned that the incumbent energy company of Turkmenistan, Turkmenengaz21, is a state-run company. Therefore the interests of the state (read President of

21 Turkmenengaz is the main gas producer of Turkmenistan
Turkmenistan) are inextricably linked to the interests of the company. Concretely this means that all the new energy projects will have to be communicated with and reviewed by the state, making it a complex undertaking for any foreign company attempting to enter the Turkmen energy market, especially considering the political system of Turkmenistan, which puts all the political power in the hands of the President.

The Turkmen government has endeavoured to develop a legal regime that would attract sufficient foreign investment in its oil and gas sector in both the development and exploitation of fields as well as in the transport sector. The existing legislation includes a Law on Foreign investment. This law guarantees that foreign investments are not subject to nationalization or requisition. Concessions are granted to foreign firms between 5 and 40 years for onshore and offshore areas containing natural resources for the investment in enterprises that explore, develop, extract and use natural resources.\(^{22}\) Foreign investors are guaranteed the right of international arbitration as article 55 of the Petroleum Law provides the contractors protections that are “in accordance with international law” including the protections that are stated in the license and agreements that relevant parties negotiate about. Article 56 grants the right for parties to seek for international arbitration for resolution of any disputes “associated with issuance, refusal to issue, suspension of effect and/or annulment of a license, as well as associated with performance of a contract.” However, subsequent Turkmen legislation sharply limits the applicability of these rights, which is an enormous blow to the country’s adherence to international legal norms and its adherence to international arbitration.

Moreover, the country has adopted the Law on Hydrocarbon Resources, internationally known as the Petroleum Law, the Oil and Gas Rules and Regulations and Model Production Sharing (PSA) and Joint Venture Agreements (JVA) (Hines 2001). However, the implementation of this legislation remains a concern. The decision making process remains highly non transparent, with the President having the final word in all deals. The government also has the reputation of not keeping to terms of contracts. Although suggested otherwise, Turkmenistan does not fully relinquish its control over resources and operations and in even in the operation under PSAs and JVAs, companies meet resistance in separation of decision making and control (CEE 2001). In most of the cases the Turkmen government insists on maintaining a majority interest in any joint venture. Foreign investors have been reluctant to enter JVs extensively controlled by the government, as a result of competing business cultures, conflicting management styles and even discriminatory actions (Hines 2001). Hence, traditional remedies as entering a joint venture with the Turkmen government or with a local firm with political connections do not provide a clear cut remedy to unevenly enforced and unclear laws. Foreign investors may only sell shares or abandon with government permission, though there is no exact regulation on this. Furthermore, Turkmen legislation also sets the tax structure for projects, but leaves a lot of room for negotiation. The size of royalties is also to be determined in each agreement, and has ranged from 3 to 15 percent. The taxation system is not clear and is discriminatory (Olcott 2004). In addition, there is widespread corruption. Turkmenistan is assigned a Transparency International’s Corruption Index indicator (TI-CPI) of 2.0 (TI 2005).\(^{23}\)

Both the Rules and Regulations as well as the Petroleum Law fail to provide a specific provision that holds Turkmenistan to the enforcement of awards rendered in the arbitration of disputes (Hines 2001). Lawyers working in the Caspian oil sector are also pointing the initial weak track record of the Turkmen government, which has been threatened with international

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\(^{23}\) 0 is highly corrupted, and 10 is highly clean.
arbitration in a number of its early contracts. All in all, although the government has introduced many laws, it provided no real protection for investments.

**Impact on first attempt**

After having outlined the legal regime in Turkmenistan with regard to the energy sector one might not be surprised to hear that transnational oil corporations were reluctant to make substantial investments in the energy sector as in the case of the trans-Caspian gas pipeline project. They were threatened by the opaque nature of doing business in Turkmenistan where their investments enjoyed little assurances and protection as its legal and regulatory framework is capricious, unclear and discriminatory. The TCGP would have definitely stalled on the issue of financing was it not for the intervention of the United States. More about this in the geopolitics section.

**4.3.3 Potential petro-states and its implications on domestic governance**

In this section the implications of the ‘resource curse’ on the domestic governance and thus on the domestic stability of Turkmenistan is discussed. As it is already mentioned the question to what extent the ‘resource curse’ is applicable to natural gas or on Turkmenistan will not be researched as it falls outside the scope of this research. Instead it will be taken as given and it will be researched what the implications of the ‘resource curse’ may be on the domestic governance and thus the domestic stability of Turkmenistan. An overview is given of the classic problems of the petro-state in Appendix C.

**Potential impact of the ‘resource curse’ on Turkmenistan**

The strategy of governance in Turkmenistan is not unfamiliar to many OPEC states, namely the “no taxation, no representation” model (Sabonis-Shelf 2005). As a result the state is neglecting to establish competence and experience in taxing or budgeting. A complete lack of transparency from this country has had the consequence that even the most basic statistics published, such as population figures, are viewed with disbelief. However, based on the promise of hydrocarbons, the international community keeps on lending money where it is unwilling to invest. President Niyazov has relied heavily upon actual and prospected gas export revenues to support a high level of public spending in order to prevent his citizens from experiencing a decline in their Soviet-era living standard. However, there will come a time that the international community is not prepared to lend money any more and is expecting to see some structural changes instead. A possible result could be the curtailment of large-scale subsidies, which could fuel the public’s anger and discontent even more about the way the state is being run. Moreover, as a result of large-scale subsidies, prestige projects, and state mismanagement of the economy, Turkmenistan qualifies as a highly indebted country under World Bank classifications (EIU 2002). See table 2 for an overview of the external debt as percentage of GDP.

<table>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Turkmenistan</td>
<td>50.6</td>
<td>64.6</td>
<td>NA</td>
<td>NA</td>
</tr>
<tr>
<td>Kazakhstan</td>
<td>19.2</td>
<td>27.3</td>
<td>36.2</td>
<td>36.4</td>
</tr>
<tr>
<td>Russia</td>
<td>31.5</td>
<td>65.6</td>
<td>89.0</td>
<td>61.7</td>
</tr>
</tbody>
</table>
Moreover, the increasing reliance on gas export revenues, see table 3, is fuelling the desire to substitute it for much needed economic reform (investing in modernization and diversification of the economy). Turkmenistan’s dependence on gas export revenues has another dimension to it as it is also increasingly becoming dependent on Russia, since Russian soil still remains the only route for the landlocked Turkmenistan to export its gas through. This increases the insecurity of revenue even more. A continuingly increasing indebtedness of this country, to a high extent consolidated by the increasing dependence on gas export revenues, may in the long term result in further economic destabilization. In addition to this, the increasing dependence on gas export revenues brings along the threat that at times of decreasing oil prices (gas prices are linked to oil prices), there would be no compensation by other income-earning sectors (Wälde 2008). This will result in lending more money from the international community just to keep their economy afloat, increasing their indebtedness even more.

<table>
<thead>
<tr>
<th>Country</th>
<th>1998</th>
<th>1999</th>
<th>2000</th>
<th>2001</th>
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<tbody>
<tr>
<td>Turkmenistan</td>
<td>54.7</td>
<td>63.7</td>
<td>79.8</td>
<td>82.9</td>
</tr>
<tr>
<td>Kazakhstan</td>
<td>34.9</td>
<td>38.0</td>
<td>50.2</td>
<td>58.1</td>
</tr>
<tr>
<td>Russia</td>
<td>36.7</td>
<td>38.9</td>
<td>62.9</td>
<td>61.0</td>
</tr>
</tbody>
</table>

Table 3: Energy as a percentage of exports

Turkmenistan’s grip on fiscal health has been slipping since March 1997, when it lost access to its traditional gas export pipelines after a pricing dispute with Russia (Haghayeghi 2001; Olcott 2004). Its increasing indebtedness had caused an important U.S. lending agency, Exim bank, to cast doubt about their readiness to lend money (Lelyveld 1999), while their participation in the first attempt was seen as crucial, both for financing and the commitment of political will (see 4.6.8). In the first attempt, Turkmenistan’s increasing indebtedness was considered more a threat to the financing of the TCGP, then that it was a threat to its domestic stability. Nevertheless, this might have changed in the medium to long term. Turkmenistan’s indebtedness and the state of the oil prices (increasing dependence on gas exports) should be taken into account in the second phase of the analysis. These key threats in the long run may prove to be the main bottlenecks in assuring the country’s domestic stability.

4.3.4 Price and volume risks as a result of liberalisation of the EU gas market

The liberalisation of the gas market in the European Union was hardly a matter of relevance during the period in which the first attempt to realize the TCGP took place. Nevertheless, one could investigate whether the outlook of liberalisation of the EU gas market had influenced the first attempt. However, it is believed to be suffice to discuss Turkmenistan’s energy strategy to diversify its gas exports. For Turkmenistan this project would mean an entrance to the lucrative European markets. A large majority of gas from Turkmenistan is being sold to Russia for a much lower price, since Russia had a monopoly

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24 Data from EIU Turkmenistan, and The Economist Intelligence Unit, Kazakhstan Country Profile 2003, and Russia Country Profile 2003, The Economist Intelligence Unit Limited, (Henceforth EIU Kazakhstan, EIU Russia), London: 2003

25 Estimated from tables in (EIU Russia), including mineral products and chemicals. Data from EIU Turkmenistan, and The Economist Intelligence Unit, Kazakhstan Country Profile 2003, and Russia Country Profile 2003, The Economist Intelligence Unit Limited, (Henceforth EIU Kazakhstan, EIU Russia), London: 2003

26 Liberalisation of the EU gas market was a gradual process. The launch was in 1998 and the full opening of the gas market was planned for 2007.
position in the export of Turkmen gas, than could be earned by selling it to the European markets. Therefore Turkmenistan views this project both as a way to diversify their gas exports and as a means to upset the pricing policy of Russia (Alexander 1998). In addition to this, Turkmenistan had experienced a fall in the gas exports after its independence. After the collapse of the Soviet Union in late 1991, Gazprom stopped Turkmen gas reaching the European markets which Gazprom wanted for themselves. Instead, Turkmenistan was given Russian access to the CIS markets, mainly Ukraine, the Caucasian countries, Kazakhstan and Uzbekistan (APS 1998). However, these countries have failed to pay their gas bills on time and some have failed to pay for years. They also had reduced purchases since 1992, with the country still heavily dependent on the old Soviet pipeline system for export. Moreover, the dramatic fall in Turkmen gas production and exports in the years 1997-1998 was caused by the Russian gas monopoly Gazprom, which cut access to its pipeline system for Turkmen gas due to disputes over transit fees and the choice of markets (APS 2006). Hence, it does not seem surprising at all that during the period of the first attempt the price or volume risks in the long term as a result of liberalisation of the EU gas market did not play a role at all in impeding the trans-Caspian gas pipeline. Moreover, delivery to the European markets was indeed planned for the long-term as the immediate offtake for the TCGP was Turkey. Nevertheless, the impact of the liberalisation may have changed over the years, since the liberalisation of the EU gas market has advanced and then there is the fact that in the second attempt the immediate offtake market for the TCGP is considered to be the European Union. Hence, this will be taken into account in the second phase.

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27 The 1998 Directive, transposed into national laws, had only limited effect on competition. In this respect a new Directive was laied down and accepted on March 16, 2002, which imposed two principles on all countries: maximal opening of their end market, legal separation of the network and regulated access.
4.4 Transit risk

In this section, the transit risk and its potential influence on the failed first attempt will be discussed. In the first attempt in the period between 1997-2001, the main transit countries were Azerbaijan and Georgia, with final deliveries to Turkey. Although it had the prospect to deliver to European markets as well, this was at that time subordinate to actually constructing the first section of the gas pipeline, namely the trans-Caspian gas pipeline, since no concrete plans were on the table at that time to connect Turkey to the European markets. The main question that needs to be answered is whether or not the transit countries have created obstacles that have impeded the realization of the TCGP and if so, to what extent and under which conditions this has occurred.

4.4.1 Transit country risk

Azerbaijan and Georgia were no different from Turkmenistan and Kazakhstan in the sense that they had also just recently declared their independence from the Soviet Union in 1991. These countries were left with a weak economic structure as it once was a central planned economy directed from Moscow. In addition, Georgia and Azerbaijan were quite heavily dependent on Russia for energy imports, but also in terms of bilateral economic relations. In this respect, the trans-Caspian gas pipeline was seen as a possibility to consolidate their state independence by limiting their energy dependence on Russia.

Having underlined the aforementioned, the next step is to determine whether or not the transit countries have used their position in the first attempt to negotiate for higher transit fees or other economic and political gains and to determine if this particular aspect had an impediment effect on the failed first attempt. Georgia, in the first attempt, firmly demanded the right to be allowed to receive energy supplies from the TCGP against favourable terms (Cutler 2003). This was not surprising at all, taking into account that the country suffers, since the fall of the USSR, from the pricing policy applied by the Russian giant Gazprom (Gremy 2006). However, this firm demand of Georgia was satisfied by the discovery of the huge Shah-Deniz gas field in offshore Azerbaijan in 1999 (Rigzone 1999).

Azerbaijan’s situation though is quite different as an important event occurred that increased the complexity of the factor transit risk and the TCGP negotiations in particular. As a pure transit country in accordance with the Case Study Protocol, Azerbaijan was not a risk to the project. Nevertheless, this changed as Azerbaijan’s impact on the project did become substantial when they discovered a huge offshore gas field transforming it also into a host (exporting) country. In other words, its role as a transit country was supplemented by a host country role. As a result, its energy security interests got a refurbishment as its energy security perception changed due to an alteration in its position in the value chain or better said it attained an extra position in the value chain. Consequently, this had also changed its strategic behaviour. It attained a strong bargaining position, since the gas field discovered was huge enough to deliver on its own and the fact that it lies further down the line. Azerbaijan as a result, relying on its strong bargaining position, demanded nearly 50% of the throughput capacity of the trans-Caspian gas pipeline project (Ögütçü 2001). Turkmenistan was firmly against Azerbaijan’s demand and tough negotiations commenced as a result. The process and the outcome of the negotiations are for a large part dependent on the extent to which these countries have developed a broader relationship, through for example trade and cross investment. When this is taken into account it falls under the factor geopolitics. But on the other hand, its role as a transit country gave it the strong bargaining position as a result of which it can be assigned to both factors. For a clear understanding of the implications of this
sudden change in the bargaining position and its energy security interests, the tough negotiations will be explicated in the geopolitics section.

4.4.2 Theft of gas

There are no indications that potential theft of gas during transit has caused an impediment for the realization of the TCGP. Moreover, the trans-Caspian gas pipeline in its simplicity is not comparable to the Ukrainian gas network, which is one of the largest in the world, featuring 37,800 km of pipelines with an annual nameplate input capacity of 280 bcm and output capacity of 175 bcm (Pirani 2007). In addition, the latter in combination with the fact that this gas is transported through an integrated network, complicates the ability to track actual flows of gas to specific customers. Since, this is not the case regarding the trans-Caspian gas pipeline, potential theft of gas during transit being considered as a potential impediment to this project is highly unlikely.
4.5 Offtake market risk

Firstly, the offtake risk concerning Turkey and its influence on the failed first attempt will be outlined. Then it is examined whether Turkey was a virgin market and if so what the role of the government was in creating gas demand. Subsequently, it is researched whether the buyer (Turkey) used its gas weapon and if so what its influence was on the first attempt.

4.5.1 Offtake price risk

The natural gas import, transportation, distribution and sales and pricing in Turkey was governed by the state-owned Petroleum Pipeline Corporation BOTAS. Moreover, the bulk of the gas imports in Europe were and still are backed by traditional long-term contracts where the price clauses are indexed to oil prices and the gas prices are revised periodically between states or the concerned (trans)national oil corporations. This would not have been different for Turkmenistan and Turkey with respect to the trans-Caspian gas pipeline project. All in all, no offtake price risk existed in the failed first attempt.

4.5.2 Offtake quantity risk

Turkey, during the first attempt to realize the TCGP, was the major intended off taker, as in the mid-1990s BOTAS estimated that Turkey’s demand for gas would rise rapidly from 9 bcm 1997 to 52 bcm in 2010 to over 80 bcm in 2020 (Coe 2000). As a result, Ankara was excessively anxious to lock in future natural gas supplies. However, there were serious concerns about the validity of the demand estimates made by BOTAS, as it was believed that the growth of the gas demand of Turkey was overestimated28. Even if its demand did reach those figures, Turkey had signed “take or pay agreements”29 with among others Russia, Iran and Turkmenistan to purchase gas at volumes that would exceed even those optimistic demand projections. Consequently, the two giant gas projects, Blue Stream30 and the trans-Caspian gas pipeline project (plus the Azeri line) were racing to get to the Turkish market first, knowing that the loser will probably be shut out for some time.

Despite claims to the contrary made by Turkish officials, in testimony to the U.S. Senate in 1999, Ed Smith, the president of Pipeline Solutions Group, openly confirmed the abovementioned assertion by saying:

“Both the Blue Stream and the trans-Caspian gas pipeline will bring gas to Turkey, but only one will be developed at a time because of the size of the market in Turkey. Turkey’s demand for natural gas is very great and would seem to be big enough to support the development of both projects. But it is not. The enormous cost and risks involved in developing projects of this size require a high level of confidence that the market will be there when the gas arrives . . . We are therefore convinced that, once one of the

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28 These demand estimates are heavily criticized by local and international institutions and experts for several reasons. There is no serious planning and coordination to justify the demand estimate studies and the methodology and programs used are incompetent. There are many factors suggesting that the official figures are overestimated.

29 A “Take-or-pay agreement” is a common type of long-term gas contract. The goal is to guarantee compensation against the failure of both the supplier and the consumer countries, since such long-term (25 years or more) agreements need billions of dollars investment (both for gas exploration/production and for transportation/distribution projects). Thus, if the consumer country fails to complete its commitments, it still must pay the cost of the gas, whether it consumes it or not. Similarly, if the supplier fails to supply the volume of gas agreed upon in the contract, it must compensate for the losses of the consuming party.

30 The Blue-Stream pipeline, an agreement signed in December 1997 between Turkey and Russia, had the aim of transporting 16 bcm of natural gas annually from Russia to Turkey, through an underwater pipeline crossing the Black Sea for a period of fifteen years.
The competition between these two projects had become part of the strategic competition over the future of the region. With Russia identifying the Blue Stream project as a top priority, the fate of this project would certainly help to determine the direction of Turkish-Russian relations as well as that of the Caspian basin. The Russians were well aware of the fact that the loser of this race would probably have to delay the implementation of its pipeline for some time. Hence, the implementation of the Blue Stream gas pipeline should be viewed as an integral part of Russia’s strategic manoeuvres to hinder the realization of the TCGP. Being dubbed as a top priority, the Blue Stream gas pipeline steamed ahead of its competitor, the trans-Caspian gas pipeline. With financing arrangements basically completed for the $3.2 billion dollars costing Blue Stream gas pipeline, 10 February 2000 witnessed the groundbreaking ceremony (Ögütçü 2001). This has unquestionably been a great blow to the trans-Caspian gas pipeline project and thus is considered an important impediment to this project. Striking is the fact that Turkey was accessory to this particular impediment as Turkey’s offtake market was just not big enough to absorb gas from both pipeline projects.

4.5.3 Virgin gas market

Before the end of the first half of the nineties Turkey’s gas market was considered a virgin market, entailing that it depended on natural gas for less than 10 percent of its primary energy supply (Goliath 2004). It is mentioned in the Case Study Protocol that especially in virgin gas market the role of the government in creating gas demand is considered crucial. This role was performed by the state-owned Petroleum Pipeline Corporation BOTAS. In 1997 BOTAS had estimated a significant increase in gas demand and they were acting accordingly to facilitate this increase. BOTAS still continues to see it as its responsibility to create gas demand and in particular to expand the Turkish gas market by building main pipelines for imported gas to reach various parts of Turkey. The total length of these high pressure pipelines in 2004 was 4,700 km and has reached 8000 km in 2007 and is expanding (Goliath 2006). Considering the significant role of BOTAS in expanding the gas grids in Turkey during the nineties and beyond in order to satisfy and influence the growing demand, it can be said that this specific aspect did not negatively effect the offtake potential of the country.

4.5.4 A buyer’s weapon

Literature has been explored to find out if Turkey has used its ‘gas weapon’ to renegotiate supply volumes or prices before and whether this has played an impediment role in the failure of the first attempt. As a result, it is concluded that it has not played an impeding role in the first attempt. As a matter of fact, Turkey before or during the first attempt did not have the opportunity to exploit its ‘gas weapon’. It did not have a monopsonist position and the necessary alternative gas supplies in order to execute their ‘gas weapon’. Although it did not play a role of impediment in the first attempt to realize the TCGP, this could be somewhat different when analyzing the second phase. This is because of the fact that during the period of the second phase, in April 2003, Turkey has shut down the flow of gas from Russia demanding a price and supply revision. Turkey forced renegotiation of the Blue Stream contracts when the expected bullish gas market in Turkey failed to meet expectations.

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as a result of a severe economic crisis in 2001\textsuperscript{32}. Whether the use of its monopsonist position had an impeding effect on the second attempt will be discussed in the following chapter.

\textsuperscript{32} Turkey’s extraordinary financial crisis of 2001, followed by a severe recession, sharply decreased its gas requirements calculated in the 1990s. Facing a free fall of its economy in 2001, it neither needed nor could afford huge amounts of gas imports.
4.6 Geopolitics in the “New Great Game”

First of all, background information on the “New Great Game” will be outlined in order to facilitate a more comprehensive understanding on this newly surged geopolitical game after the dissolution of the Soviet Union, before touching upon the actual content and purpose of this section. Subsequently, the objectives, interests and the strategic behaviour of every relevant actor will be identified and explained taking into account that the actor’s interests are subject to dynamism (constructivist approach). This will form the basis for further analysis. Then, the analysis of Turkey will be conducted. Its role and influence in the first attempt to realize the TCGP will be determined and also sub factors which are geopolitically induced will be dealt with. Furthermore, regional and project specific (sub) factors’ influence on the TCGP project will be analyzed. Last but not least, the role and influence of international institutions in the first attempt will be analyzed.

4.6.1 The “New Great Game” unleashed in the Caspian region

The Caspian Sea is at the border of the Middle East. It divides Europe from Asia and the Caucasus (Azerbaijan and Georgia) from Central Asia (Kazakhstan, Uzbekistan, Turkmenistan, Kyrgyzstan, Tajikistan and Afghanistan, and Xinjiang in China) (see figure 3). Historically, this region has sometimes controlled the Middle East. It is a historic zone of struggle between great powers: Greeks and Persians, Chinese and Arabs, Russians and Turks, and all of the above and modern Iran. Since the dissolution of the Soviet Union and thus the emergence of the new independent republics in Central Asia and South Caucasus, the conditions for a ‘New Great Game’ have been created among the forces interested in creating access to the region’s vast oil and gas resources (Amineh 2003). Whereas in the Soviet era, Central Asia and the Caucasus were largely cut off from the political, economic and cultural influences of the West, since 1991, a wide array of Western states, inter-governmental and non-state organisations have expanded into the region. The Western penetration is reflected in growing diplomatic links, bilateral political, military relations, trade and investment ties, and other exchanges. This preoccupation with the region partly indicates a growing interest in its energy resources, a recognition of its geo-political significance, a desire to balance Russian influence, to stem the growth of drug trafficking and also to help a region that could be a bulwark against Islamic fundamentalism. On the other hand, in addition to the economic gains expected to be earned from natural resource exploitation, many former Soviet republics view the engagement of the West as one way to balance the otherwise overpowering Russian and Chinese influence in their affairs. This section effectively touches upon the geopolitical importance of this region as a result of its undeniable significance as a supplier of oil and natural gas. According to the Statistical Review of World Energy (BP 2002), the proven total gas reserves of the five Caspian countries (Azerbaijan, Iran, Kazakhstan, Russia and Turkmenistan) are estimated at 76 trillion cubic meters, which is almost 50 % of the world’s total proven gas reserves. Nonetheless, the proven oil reserves are estimated at 153.8 billion barrels, 14.6 percent of the world’s total proven oil reserves. These figures blatantly indicate the importance of this region. Its vast oil and gas resources have transformed it into an area of huge competition as well as cooperation between both state and non-state actors for the control of these resources. This competition makes the Caspian region one of the most important geopolitical areas in terms of exacerbating existing instability in the post-Cold war world. In this respect, it needs to be cited that the energy security interests (policy) of the involved actors are closely intertwined with its foreign policy towards the region. This ought to be taken into account when analyzing...
geopolitics as a potential explaining factor in the attempt to realize the trans-Caspian gas pipeline.

The geo-strategic importance of the Caspian region to the West and to the European Union in particular will increase substantially in the coming decades. Since the end of the Cold War, both states and non-state actors have assigned more significance to economic and resource concerns. An increased probability that conflicts could arise are pertinent as global oil and gas consumption rises, environmental conditions deteriorate, availability of oil and gas resources decreases and prices for these commodities rise. Internal conflicts over oil and gas could arise in countries where these are the main source of income. Oil and gas resources in the Caspian region bring forth both cooperation and conflict between states and non-state actors of the immediate and highly interested regional powers (China, Iran, Russia and Turkey), the Western countries, the United States of America (USA), the European Union (EU), and their respective transnational corporations (TNOCs).

Russia still remains the most influential regional power in the Caspian region. This is most apparent as Russia tries to reincorporate the region into its security system by establishing a unified air defence system in the context of the Commonwealth of Independent States (CIS) (CNS 2007). For Russia the CIS plays a pivotal role in reviving the former security, political and economic Soviet order within a new political construction. Russia sees its decline in power as a result of its own economic problems, the wish of CEA countries to distance themselves from Russia and an increasing US involvement (military, political and economic) in the region.

China, another immediate power, has the potential to become a powerful force not only in the region but also globally in the coming years. Like Russia, it fears that the USA will dominate the region and thus obtain control over the Caspian oil and gas resources. Hence, there exists common interests between China and Russia. However, in contrast to Russia, China has a booming economy and thus an immense yearning for energy resources. It has a great interest in the import of oil and gas resources from the Caspian region. As a possible counterbalancing act to the US, China and Russia have established the Shanghai Cooperation Organisation (SCO), which also includes Kazakhstan, Kyrgyzstan, Tajikistan and Uzbekistan as member countries. China, however, did not play any role of significance during the first attempt, but it will be taken into account in the second phase of the analysis in order to get a comprehensive understanding of the power struggle in the “New Great Game”.

Iran, although economically less powerful than Russia and China, is considered an important regional player and attractive for cooperation for the countries in the Caspian region. Iran controls about 8.5 percent of oil and 15.5 percent of global gas resources (Atieh 2002). Moreover, it is geographically adjacent to Turkmenistan, providing the latter the possibility to lay a pipeline through Iran in order to reach Turkey and further on to the European markets. However, this was eventually thwarted by the US-Iranian policy since the mid-1990s to isolate Iran (U.S. 2006) and even escalated further as a consequence of Iran’s nuclear standoff (Gollust 2008).

Turkey, also less powerful in terms of economic influence, is considered an important regional player and attractive for Caspian countries to do business with. Turkey’s gas demand is increasing with a high pace, which makes it an attractive market for gas exports from this region. In addition to this, Turkey offers the geographical opportunity to link the Caspian markets with the European continent. Also worth mentioning is the cultural, ethnic and linguistic connection that Turkey enjoys with Kazakhstan and Turkmenistan as its potential
influence during the first attempt will be analyzed. While both Iran and Turkey are members of the Economic Cooperation Organisation (ECO) Turkey has also initiated the establishment of the Black Sea Economic cooperation (BSEC) that includes Russia but excludes Iran as a member country.

The United States of America has acknowledged the great energy potential of the Caspian region. It realizes the role that the Caspian region can play in providing a temporary alternative supply in case of political instability in the Persian Gulf region. This is firmly embedded in its wider Eurasian and Middle Eastern strategic priorities as its objective is to re-enforce the independence and ensure the prosperity of Central Asian and the Caucasian countries (Aras 1998). Important to note is the polarization that comes along with the involvement of the United States in the competition for Caspian hydrocarbon resources. Russia perceives the involvement of the United States as a way to diminish the Russian influence throughout the region and enhance its (geo)political and economic clout. Therefore the US takes their steps with sheer prudence, not eager to unleash another Cold War.

The European Union as such needs to be distinguished into the European Commission and the member-state political level. The European Union has its own rationales to get involved in the ‘New Great Game’. Due to the geographical proximity it fears that instability in that region could also affect Europe. In addition, because of the declining energy sources in the North Sea, the rapidly rising energy demand and the need to diversify in order to become less dependent on especially Russia, the EU is searching for alternative sources as it realizes that the Caspian region is a viable option (ICG 2006). Although striving to exert influence in the Caspian region and the surrounding countries, a unified European strategy did not yet exist during the first attempt. This is partly due to the fact that the EU member states, in particular the main actors (Britain, France and Germany), each have different priorities. The lack of a unified stance towards the Caspian region is considered a weak spot in trying to exert its influence in that region. During the first attempt, the EU has played a subordinate role. Only the European transnational corporation Royal Dutch Shell participated in this process. Though, its role and influence of the EU increased substantially during the second attempt as the need to diversify its gas supply from Russia became a top priority on the EU agenda (ICG 2006).

4.6.2 The involved actors’ interests and objectives

In this section, the relevant actors’ interest (trans)formation and objectives will be analyzed and explained from a constructivist approach within the context of the ‘New Great Game’ and the role of the trans-Caspian gas pipeline project therein. Needless to say that energy security claims an important part herein. This will form the basis for analysis in the succeeding phases. In this respect, it is necessary to identify and explain the extent to which the involved actors are in favor or against this project and thus find out the driving forces behind their strategic behavior.

Therefore, the following research question will have to be answered:

*How will the realization of the TCGP influence the ability of the relevant actors to achieve their objectives given the context of the “New Great Game”?*

The relevant actors constitute the state and non-state actors that have played a role of importance during the first attempt. These are the following: Russia, Iran, Turkmenistan,
Azerbaijan, Georgia, Turkey, the United States, the transnational corporations (TNOC’s) and the international financial institutions.

**The Republic of Turkey**

The primary objective of Turkey with respect to its energy security policy is to find diversified, reliable and cost-effective supplies for its expanding energy needs (security of supply). Turkey as an off-taker/consumer of energy desires reasonably-priced energy on demand and has concerns about the security of supply (disruptions). The trans-Caspian gas pipeline project is in this respect an answer to its prayers as it would secure its demand for gas on the one hand and diversify its gas sources – it is for 65% dependent on Russian gas (Kaplangil 2008) - on the other. Moreover, its geostrategic advantageous position partly explains its political interests as well. In this respect, the TCGP would also contribute greatly to Turkey’s aspirations to become one of the main energy arteries of natural gas for the European markets while at the same time augmenting their leverage vis-à-vis the European Union. It would help increase its strategic significance for the EU. Therefore Turkey’s energy (security) policy is closely intertwined with its foreign policy. Although this objective has been more prevalent in the second attempt and accordingly will be discussed in detail in chapter 5. Moreover, it would create a milestone in the Turkmen-Turkey bilateral relations, strengthening it to a great extent and paving the way for greater involvement in Turkmenistan and the rest of the Turkic-speaking countries. Turkey therefore strongly supported the implementation of the trans-Caspian gas pipeline project.

**The Russian federation**

With the dissolution of the Soviet Union, Russia had to reconsider its novel forms of statehood and national identity at home as well as come up with new approaches for its foreign relations. The approach that was adopted was Eurasianism (Amineh 2003). The concept of Eurasianism is solely based on the notion of Russia as superpower and its goal is to reinstate Russia’s dominance in the Eurasian region. It adheres to a nationalist-patriotic course, believing that due to geographical, psychological, historical and cultural particularity, Russia can neither be classified as East nor West. It states that Russia is a strong state, communitarianist\(^{33}\) and a dominant Eurasian power. President Putin, after he became President of Russia in March 2000, continues and intensifies the main efforts of Russian foreign policy since 1992-1993: first to preserve Russia’s integrity, then to restore Russian primacy in political, economic and military terms (Blank 2002). To this end, Vladimir Putin chose energy (security) as the means to become a regional and then a global power again (objective). In this respect, he is seeking to re-integrate the Caspian region into its energy system (Correlje 2006). Actually, it had to choose energy. As Vladimir Putin stated on December 22, 2005 at the Russian Security Council meeting, the only area in which Russia can become the leader of the world in the short and medium term seems to be energy (Yasmann 2006). The difference of President Putin is that he has a more pragmatic approach towards Central Eurasia (also called near-abroad) and he recognizes Russia’s limited economic and political capabilities and the necessity to make concessions (Smith 2000).

The value and the meaning that Putin’s Russia gives to their energy reserves is in the sense that it defines and reinforces at the same time its identity as a re-emerging regional and global power. Russia’s energy (security\(^{34}\)) policy should be viewed as a powerful tool to achieve

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\(^{33}\) Communitarianism emerged in the 1980s as a response to the limits of liberal theory and practice. Its dominant themes are that individual rights need to be balanced with social responsibilities, and that autonomous selves do not exist in isolation, but are shaped by the values and culture of communities.

\(^{34}\) From Russia’s perspective it means securing and raising demand and revenues.
their objective to re-emerge as a regional and then a global power. In this respect, Russia uses its natural resources to increase its prestige and (economic and political) power. For that reason, its energy policy is closely intertwined and has a reciprocal relationship with its foreign policy. Moreover, control of transport infrastructure is a key point of geopolitical significance for Russia for all their relations with the “near abroad”.

Having mentioned the former, a possible realization of the trans-Caspian gas pipeline would put an end to the Russian monopsonist position and on the monopoly that it holds as the only transit country for the gas exports from Turkmenistan through the Central-Asia-Center gas pipeline. This would be a blow to Russia’s goals as it would undermine her endeavours to restore Russian primacy in the near-abroad. Additionally, it is believed that the realization might even start a chain reaction in the defying spirit of the other states, decreasing Russia’s leverage even further. The other states would become encouraged to face up to Russia’s strong arm.

Moreover, the realization of the trans-Caspian gas pipeline project would also effectively mean that Turkmenistan would redirect its gas to other offtake markets, leaving less relatively cheap gas for Russia, which they need in order to save or to postpone the development of difficult and expensive gas fields that lay beyond the Arctic Circle as it faces declining yields at core domestic fields (Ögütçü 2006). For the development of these expensive gas fields foreign investment is necessary in terms of financing and technology, but President Putin is persistent in its aggressive pursuit of expansion and acquisition. Unless Moscow is able to secure additional gas supplies from gas fields in Central Asia, it may struggle to meet its commitments to Europe in the long term, which would be devastating for their reputation as a reliable supplier, and also the rising domestic demand (Thomson 2008). Central Asian gas has gained an additional value for Russia in the second phase of the analysis parallel to the growing domestic and external demand. Above all, they would miss out an major source of gas revenues. Turkmen gas is a huge income source for Russia, since they purchase it for a relatively low price and resell it for European prices (security of revenue). This is why maintaining full control over Central Asia’s export routes is so critical for Kremlin. This indicates an increasing strategic role for the supply of Turkmen gas (and Kazakhstan in the second phase). In this respect, despite Russia’s abundant gas resources, it is relying increasingly on the security of gas supply from Central Asia (RT 2007). This fact makes Russia also an importing country and in turn constitutes another perception of energy security, namely finding reliable and cost-effective gas supplies.

The economic and political leverage that comes with the monopoly on Turkmen gas exports is considerably high, since Turkmenistan is highly dependent on its energy revenues due to its low diversified economy (see section 5.3.1). For Russia the energy dependency bears even more meaning considering the fact that Turkmenistan has remained aloof from cooperating with the CIS and Russia in many policy areas (Smith 2000). It is basically the only string of relations that Russia has with Turkmenistan.

Breaking the Russian monopoly would reinforce Turkmenistan’s negotiation power when bargaining over the price of its natural gas. The delivery of Turkmen gas to the lucrative European markets would give Turkmenistan a strong impetus to bargain for higher prices for the natural gas that it sells to Russia.

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35 Russia is the world leading producer and exporter of natural gas: in 2006, it produced 656 bcm of natural and exported 201 bcm. The country is also the second largest producer and exporter of oil with 480 Mt of oil in 2006. About half of the production is exported (250 Mt).

36 The nationalization of the Russian gas company Gazprom in 2005 (50% +1 shares) and also the oil company Transneft
All in all, the trans-Caspian gas pipeline would level out Russia’s strong economic and political leverage on Turkmenistan over more players as it would give other actors such as Turkey and the European Union a bigger stake in the security and stability of Turkmenistan. In addition, the Turkmen gas is increasing in strategic importance for Russia as it is used to save or postpone the development of expensive gas fields and satisfy the increasing external and internal demand. Therefore Russia is very keen on its monopoly on Turkmen gas exports and opposes the realization of the trans-Caspian gas pipeline in a strong and adamant manner.

The Islamic republic of Iran

Iran’s main objective is to give its own economy a new impetus through economic cooperation with the Central Asian and Caucasus countries by relying on their common historic links (Amineh 2003). To his end, providing gas and oil to the landlocked countries in Central Asia was the goal of its assertive policy. As a major energy producing country, whose economy for a substantial part is dependent on energy exports, it endeavours to secure and increase its revenue and demand and thus its economic growth by expanding its off takers at the expense of its competitors (economic interests).

The main aim of its foreign policy has been to prevent the US and its Turkish ally to fill the vacuum left after the fall of the Soviet Union (Roy 1999) (geopolitical interests). Knowing that they themselves cannot fill up this vacuum, Iran teamed up with its Russian neighbour (strategic behaviour), creating a North-South strategic axis (Russia-Yerevan-Tehran) to oppose the East-West axis (Washington-Ankara-Baku-Tbilisi). The competition between the different pipelines reflects this strategic double axis: East-West for the US, Turkey (and the EU) (TCGP), North-East for Moscow and Tehran (Baku-Novorossiysk and CPC for Russia, connection with the Iranian networks to the Oman Gulf for Iran).

During the first attempt of the TCGP, Iran pursued to build a Turkmenistan-Iran-Turkey gas pipeline. Although being the most economically sound option, U.S. sanctions against Iran for its ideological and political anti-Western Islamism and alleged support of international terrorism have prevented this pipeline from becoming a reality. In general, these sanctions have crippled Iran’s capabilities to turn its economic resources into power and influence, which explains for a major part the failure of Iran’s strategic overtures in Central Asia and the Caucasus. These sanctions ensure that Iran continues to see the United States as a hostile power and its activities as potentially threatening to Iran’s interests. Strongly supported by the U.S., the trans-Caspian gas pipeline is deployed as a means to by pass Iran, which Iran would rather like to see it passing through its own territory. The realization of a trans-Caspian gas pipeline would further isolate Iran from the Central Asian region seriously challenging its regional ambitions. Unmistakably, it would be a major setback to its strategic goal to reap the fruits of the energy rich Turkmenistan. Hence, Iran strongly opposes the U.S. backed trans-Caspian gas pipeline.

The republics of Turkmenistan and Kazakhstan

The primary objective of Turkmenistan and Kazakhstan is to obtain diversified export routes for their oil and gas resources and at the same time to secure and raise demand and revenues. To this end, any route is sufficient. Secondly, these countries desire a route that will maximize their political independence 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. Each possible route brings

37 Kazakhstan became a potential candidate to provide natural gas to the TCGP in the second attempt. Nevertheless it is treated here as its interests with regards to the export of energy sources to a large extent coincides with the interests of Turkmenistan.
along their own advantages and disadvantages in light of Kazakhstan’s and Turkmenistan’s important objectives, namely economic growth and political independence. In this regard, Russia is a dominant force and a potential obstacle for their goals.

The realization of the TCGP would open up a lucrative market for both Turkmenistan and Kazakhstan providing the possibility to sell natural gas directly to the European markets. Furthermore, it would mean that Russia’s monopoly on its gas exports would be penetrated, alleviating Turkmenistan’s and Kazakhstan’s economic and political dependency on Russia. It would also mean that Turkmenistan and Kazakhstan can demand higher prices for the natural gas that is sold to Russia as the realization would have a direct impact on their bargaining position. Hence, during the first attempt Turkmenistan strongly favoured the trans-Caspian gas pipeline.

Although their goals are the same, their ties with Russia are not. With respect to Kazakhstan there are two factors that make a close relationship with Russia necessary, which explains the strategic behaviour and stance of Kazakhstan towards the TCGP (see 5.7.4); the first is the common economic and security ties as they share a long border. The second is the presence of a minority of six million ethnic Russians in Northern Kazakhstan. Both of these lead to a high level of Russian influence and overtures that can only be increased by Russian control of pipeline routes. Russia uses these strong economic, security and ethnic ties to exert leverage over Kazakhstan.

**United States of America**

The United States has since the appointment of Bill Clinton as President pursued the approach of Econocentrism (Klare 2002) to ensure national security. National security is inextricably linked with energy and the concerns for energy security (Deutch 2004). In this respect, the US economy is increasingly relying more and more on imported energy resources - especially oil -, which are not distributed uniformly around the globe. The protection of global energy has become an important feature of US security policy. There has been a growing emphasis on military operations but also in oil-field protection, the defence of maritime trade routes and other aspects of resource security. Central to this policy shift is the view that from the end of the Cold War national power no longer depends solely on the possession of a huge military arsenal and an extended alliance system but on economic dynamism and the cultivation of technological innovation. In this respect, the United States places high priority on the security of supply of oil and gas as it sees economy and security as interrelated. The role for the military in this respect is to protect the resource supplies. Therefore the US government is eager to expand its military presence in the Persian Gulf as well as in the Caspian Sea.

The United States strongly supports the western pipeline route through Turkey, bypassing Iran and Russia. This is firmly embedded in its wider Eurasian and Middle Eastern strategic priorities as its objective is to re-enforce the independence and ensure the prosperity of Central Asian and the Caucasian countries. Hence, its support for “the concept of multiple pipelines and multiple pipeline routes through the region as oil and gas are extracted” (Aras 1998). Its policy attaches great importance to market reforms in CEA countries, in part to strengthen the positions of US transnational corporations in the region. In Russian view, however, the central motivation for this policy is to diminish the Russian influence throughout the region. It believes that the US aims to ensure access to the Caspian region and the Persian Gulf in order to enhance its geopolitical and economic importance. Therefore the US takes their steps with sheer prudence, not eager to unleash another Cold War.
The U.S. proactively supported the first attempt to realize the TCGP, appointing a special representative for Eurasian matters, John Wolf, who had the difficult task to coordinate the realization of the pipeline project. In this respect, Washington lobbied to Azerbaijani President Aliyev and the Turkmen President Niyazov to consider the Turkish route. Yet Washington also wisely encouraged Aliyev to consider the northern oil pipeline route through Russia as well in addition to the Turkish route, a move which was well calculated to avoid the appearance that Washington stands in opposition to Russian interests. Nevertheless, this did not prevent Russia to view the U.S. as a geopolitical rival and act accordingly augmenting its decisiveness to block the trans-Caspian gas pipeline. Moreover, the United States, Azerbaijan and Turkey as a result of Niyazov’s stance in the negotiations redirected their time and effort to the South-Caucasus gas pipeline in order to keep at least some portion of the Eurasian energy corridor alive.

The realization of the TCGP would, besides counterbalancing Russia’s influence, function as a catalyst for more extensive Western involvement in Turkmenistan. Its realization would send a strong signal to the other Central Asian states that it is possible to break through the Russian dominance in the region. This would consolidate the influence of the United States within the Caspian region paving the way for further involvement in the exploitation and export of the region’s energy resources in order to decrease their dependence on the Gulf region. The latter is the main motivation for the U.S. to remain involved in the Caspian region. Its aim is to control the exploitation and export of the Caspian region’s energy resources (Forsythe 1996). The US regards the Caspian region as vitally important especially due to its energy resources that could form a balance to US reliance on Persian Gulf oil. To this end, the US government and the U.S. transnational corporations act in union in most cases.

In addition, another strategic goal and at the same time a reason for actively supporting the TCGP is to exclude Iran from participating in the production of oil and gas in the Caspian region and to prevent the development of transportation routes or pipelines that would lead from the Caspian region to the Gulf via Iran. On the one hand this is closely related to the containment policy of the US against Iran and on the other it is linked to the fundamental US strategy in the Middle East of preventing the rise of any dominant regional power who are capable of influencing the oil markets in the Gulf (Aydin 2000).

**Georgia and Azerbaijan**

The primary objective for both Georgia and Azerbaijan is to become sovereign independent powers integrated within the West, given their West-oriented outlook after gaining independence from the Soviet Union in 1991. One of Azerbaijan’s main foreign policy priorities is integration into European and Euro-Atlantic political, security and economic institutions such as the North Atlantic Treaty Organization (NATO) (Bakinsky 2007). For Georgia integration and eventually joining the NATO is one of their main foreign and security policy objectives (Kishkovsky 2008). Georgia attaches great importance to the role that NATO can play in maintaining and reinforcing their stability and security. Moreover, these countries desire a decrease of economic and especially political dependence on Russia. In this respect, the TCGP would generate a great amount of transit fees and contribute substantially to their economies. In addition, given the fact that Russia still has a big share in the delivery of gas supplies to Georgia in particular, the TCGP would also mean a diversification of gas supplies against cost-effective prices consolidating their independence from Russia. Furthermore, the discovery of the huge Shah-deniz gas field enhanced Azerbaijan’s chances to become less dependent from Russia. This resulted into a prioritization of its potential as a host (exporting) country with the aim to secure demand and revenues as it claimed a substantial portion of the throughput capacity of the TCGP. Above all, the
extension of this pipeline to the European markets would mean that the European Union would have a big stake in the security and stability of these countries reinforcing their integration with the West. Therefore both countries were very favourable towards the realization of the TCGP.

**Transnational Oil Corporations**

For these huge oil and gas companies the primary objective is continuation. Hence, the translation of their investments into profits is vitally important. Concretely this means that before constructing long oil and gas pipelines, they must get a ‘throughput guarantee’ i.e. the host country should guarantee that oil or gas will flow through these pipelines (Udum 2002). First there needs to be the focus on getting access to the gas fields and then on the pipeline to get it out as was the case with the BTC oil pipeline (Kucera 2008). Moreover, since these firms take decisions according to economic parameters, they are interested in the technical details of the pipelines in terms of cost-benefit analysis, rather than political considerations. In this respect, stable investment regimes are deemed critical for an energy company to ensure its energy security. Furthermore, access to new reserves and the ability to develop new infrastructure are also critical to ensuring energy security.

After the dissolution of the Soviet Union, the TNOC’s were all eager to get hold of exploration rights in the newly independent post-Soviet littoral states given their potentially enormous energy reserves. The companies were all striving to get a piece of the huge profit cake. It needs to be mentioned that the TCGP was just one of the many pipeline projects that were proposed during the period of the first attempt. The trans-Caspian gas pipeline was not any different from the other pipelines viewed from a commercial point of view. Any successful implementation of these pipelines might generate subsequent deals for the concerned TNOC’s. The difference with the other pipeline projects were that the US transnational corporations were fervently supported by the United States government for the attempt to realize the TCGP, both in financial and political terms through the US lending agencies. Above all, the United States government is regarded as an extension of the US transnational corporations and the promoter for these corporations in areas where they can do business (Amineh 2003).

**National financial institutions**

Needless to say that the participation of (inter)national financial institutions are considered crucial for the financing of the trans-Caspian gas pipeline project given the many uncertainties that TNOCs are up against in Turkmenistan (see section 4.3). International financial institutions (IFIs) refers to financial institutions that have been established by more than one country and hence are subject to international law. Some relevant examples are the World Bank, the European Investment Bank (EIB) and the European Bank for Reconstruction and Development (EBRD). Relevant in the sense that the former have either provided funds earlier for the realization of large energy infrastructure projects or given the potential role that the European financial institutions might play in the future in terms of providing funds for the TCGP. Some examples of national financial institutions are the U.S. Ex-Im bank and the Overseas Private Investment Corporation (OPIC), which have proved their value in the first

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38 In June 1998 the PSG international consortium was established to construct the trans-Caspian gas pipeline. The PSG’s obligations included finding suitable partners to the consortium and developing a finance model, which would ensure smooth progress in the TCGP project. It was comprised of the companies GE Capital and Bechtel Enterprise, which was later joined by Shell. The latter is an European based TNOC as the first two are both American companies.

39 Other examples were the Trans-Afghan pipeline and the Turkmenistan-Iran-Turkey gas pipeline.

40 The World Bank provided funding for the Bolivia-Brazil gas pipeline project among others and the EIB has provided funding for the Chad-Cameroon oil pipeline project.
attempt. They were mobilized by Washington to come with a mechanism to fund the realization of the trans-Caspian gas pipeline project (see Appendix D).

4.6.3 Turkey’s efforts to reclaim its (geo)strategic importance (1)

Since Turkey is the main actor in this research, its role and influence during the first attempt of implementing the TCGP should be researched thoroughly. In this respect, also Turkey’s relations with the global and regional power(s) are looked upon in detail. In addition, it is examined whether Turkey’s ethnic and cultural ties played a role during the first attempt. First of all, though, Turkey’s identity and the driving forces behind its foreign policy will be analyzed by putting it into historical perspective for the purpose of understanding its interests and strategic behaviour.

Moreover, the sub research questions that will be dealt with respectively in this section are the following:

What kind of measures did Turkey undertake to influence the first attempt to implement the TCGP and how can the role of Turkey be classified and why?

Did Turkey’s cultural, ethnic and linguistic ties with Turkmenistan play a role of significance in the first attempt to realize the TCGP and if so to which extent?

What was Turkey’s relations with the global and regional power(s) and to what extent did Turkey’s interests match or compete with their interests?

Turkey’s national identity and its foreign policy after dissolution of the Soviet Union

Traditionally, Turkey’s foreign policy in the post-1923 republican era, introduced and reinforced by Mustafa Kemal Atatürk, was based upon two guiding principles; the first principle was its unambiguous orientation towards the West, which translated into its endeavour to join the European Union. It has defined itself as a state that is part of Europe and the West, a secular and democratic country. This has constituted its identity from that period onwards and it has remained this way up till now. The second principle concerned its conservative and defensive strategy regarding the avoidance of extra-territorial and imperialist interests extending beyond the borders of the country (MOFA 2002). It was based on the concept “peace at home, peace in the world”. To this end, Turkey became a founding member of the UN in 1945 and joined the Council of Europe in 1949. As a result of the growing threats to security in Europe, it joined the NATO alliance in 1952. In 1963, Turkey and the EU (then the European Economic Community) signed an association agreement (EU 2005). In addition to this, Turkey is a member of the Organization for Security and Cooperation in Europe (OSCE), the Organization for Economic Co-operation and Development (OECD), the Black Sea Economic Cooperation (BSEC), the Organization of the Islamic Conference (OIC) and the Economic Cooperation Organization (ECO).

The groundwork of its foreign policy was seriously challenged in the 1990’s, turning into an assertive policy towards the Middle East, Balkans, Caucasus and the Central Asian republics. The initiator of this shift was the key political figure Turgut Özal, which was the president of Turkey during the early nineties. He emerged as the key architect for Turkey’s neo-liberal economic reforms. The first striking evidence of the shift in foreign policy became evident during the 1990-1991 Gulf crisis as Turkey took an active role in the U.S.-led coalition against Iraq, following the invasion of Kuwait. Turkish President Turgut Özal declared at a 1991 post-Gulf War press conference that Turkey "should leave its former passive and
hesitant policies and engage in an active foreign policy" (Makovsky 1999). The newfound assertiveness also expressed itself in a proactive rapprochement towards the former Soviet republics in the Caucasus and Central Asia, which Turkey was first to recognize in 1991. The underlying forces that contributed to the shift in Turkey’s foreign policy are several. During the Cold War era of superpower rivalry in which the world was divided into two camps, Turkey enjoyed a geostrategic position in the Western alliance and NATO, embodying an apprehensive barrier against further expansion of the Soviet Union towards the South. The end of the Cold War, however, marked a change in how the West viewed Turkey in terms of (geo)strategic importance. Its strategic relevance was no longer clear-cut as it had been before. Furthermore, the rejection of Turkey’s bid in 1989 to become a full member of the European Union was widely interpreted in Turkey in both the policy circles and the public as a rejection on cultural (ethnic and religious) grounds (Onis 1999). A deep sense of isolation and insecurity was a direct and natural consequence of these developments, which encouraged a more active role. Also the support of the USA in the involvement of Turkey in the Middle East, the Balkans, Caucasus and Central Asia, played an important role in this change. Turkey's embrace of the "Turkic Republics" also had an important psychological dimension (Onis 2001). Closer ties with people of common historical descent was a means of overcoming Turkey's traditional fear of isolation and insecurity. Feelings that were induced by the negative attitude on the part of Europe and the Arab Middle East as well as several ongoing conflicts around the country's own borders. This sense of isolation is crucial in order to comprehend the initial euphoria regarding the Turkic republics in the Caucasus and Central Asia. It was regarded as a means to strengthen the Turkic cultural and ethnic identity. In the early nineties establishing closer ties with the Turkic states based on identity was considered a top priority. Significant changes in Turkey's domestic politics also contributed to that trend, particularly in relation to the former Soviet republics.

All in all, the breakdown of the Soviet Union and the emergence of the new independent states of Central Asia and the Caucasus was seen by Turkey as an unique opportunity to explore a potential new role as an influential regional power. Turkey’s ethnic, cultural and linguistic ties with Azerbaijan, Kazakhstan, Uzbekistan, Kyrgyzstan, and Turkmenistan provided the foundation on which Turkey could build upon in order to regain its (geo)strategic importance. It is considered that the main aim of Turkey was not to create an alternative for the West, but reinforcing its political position against it by forging new brother nations in Central Asia and the Caucasus (Laçiner 2005). Through these means, Turkey would have created a more influential position in Western structures. Therefore, Turkey presented its status as a modern democratic, secular and market-oriented state as an alternative model for these states in a post-Communist world. In other words, the Turkish foreign policymakers had the aspiration that such leadership could revive its strategic importance to the West and thereby enhance its own economic and security interests at a time in which its old role in the context of the Cold War period had perished (Onis 2001). This strategic vision was supported by the European Union and the USA, but explicitly promoted by the latter. This support was justified by the need of preventing the rise of another Iranian Islamist model (RAND 2003).

**Failure of the “Turkic World” model**

Following the collapse of the Soviet Union, the new independent Turkic states in Central Asia and the Caucasus became the focal point of Turkey’s diplomatic efforts peaking in the early nineties. Turkey tried to build upon the strong cultural, linguistic and ethnic bonds with the new republics as it tried to be an alternative model with its status as a secular, democratic and market-oriented state for these newly independent Turkic nations. Moreover, Turkey tried to apply a combination of material (mainly economic) and above all ideational
(soft) power (Nye 2004) based upon alleged similar identities. However as constructivism states, identities are social and are produced through interactions, hence the deduction that identities can change (Barnett 2001).

With hindsight, it can be concluded that in the first decade of their independence Turkey’s successes as an influential power in the Caspian region was rather limited. The active engagement of Turkey has helped to orient the region towards Europe. Through their cultural and economic interactions with Turkey, these Turkic states came to realize that they wanted to be a part of Europe and not the Muslim world or the Middle East. Turkey’s attempt to play a leadership role was encountered with many harsh setbacks, which resulted into the fact that Turkey had to scale back many of its grandiose plans. The early euphoria about the Turkic states was replaced in the mid-1990s by a more sober and pragmatic approach based on mutual economic benefits. Several factors have contributed to the relative decline of Turkey’s regional influence and its attractiveness as a model. One of those factors regards the long dominion that these Turkic republics had to endure from the Soviet Union. It had made their ideational structures more in line with the communist structure of the former Soviet Union and given the assertion that identities are social and produced through interactions, Turkey was not able to play a successful ethnic identity card in the beginning of the nineties. This was just one of the many aspects why the Turkic World model had failed. Another was Turkey’s inability to financially assist these states in a grand scale due to its poor macro-economic situation. Furthermore, although the Soviet Union’s direct control was over, the Russian influence was still immanent. Inheriting the Soviet-created division of labour, the republics continued to be economically dependent on Moscow and also lived in the shadow of Russia's military power and cultural influence. Having been under the rule of the Soviet Union for decades had definitely left a huge mark on the Turkic countries, underlining that identity is indeed subject to change. This made it harder for Turkey to penetrate the Turkic society. Moreover, Turkey positioned itself as a ‘big brother’ for these Turkic countries. This was not appreciated as they just became independent from the Soviet Union and were not at all receptive to come under Turkey’s big brother dominion (Torbakov 2002).

Turkey has given up its traditional approach towards the Turkic states. After the mid nineties Turkey has adopted a Central Asian foreign policy based on ‘equality’, leaving behind its aspirations to become a ‘big brother’ for these states. Turkey still promoted the concept of Turkic brotherhood, but as a reasoning to enhance cooperation and dialogue between the Turkic states on an equal basis. In the beginning this primarily expressed itself in the strengthening of the economic ties and is gradually developing to other fields of cooperation. Moreover, Turkey’s interest in the region’s vast oil and gas resources as well as in the exploration and production goes without saying. On the other side, for obvious reasons the Caspian region in turn has an interest in Turkey as a potential off taker of gas and as a transit route for delivering gas to the lucrative European markets.

The role of Turkey’s ethnic and cultural ties with Turkmenistan

Having stressed the failure of the “Turkic World” model, it comes as no surprise that Turkey’s cultural and linguistic ties with Turkmenistan was not an important factor whatsoever in the first attempt. It was more the reputation of Turkey’s erstwhile President Süleyman Demirel that had made some difference as he was highly esteemed in the Turkic

41 This is emphasized by the former President of Turkey Süleyman Demirel as he said in 1996: “We see this rich region of oil and gas reserves, not just as a source of energy, but as an element of stability. Just as the founders of the European Community saw coal as a source of peace and stability for Europe, so we see oil and gas in our region serving the same role. Stability and prosperity in the region will mean also increased trading and investment opportunities for Turkey”
world, who as a consequence booked some success with the Turkmen leader (Cutler 2003). Furthermore, Turkey did not blatantly use this specific card in the bilateral talks with Turkmenistan to actively promote the TCGP. There were other instruments more prevalent to promote this pipeline, such as the potential economic benefits that could be gained from this project. Although Turkey’s cultural and linguistic ties with Turkmenistan may not have played an important role during the first attempt, her developing ties with the Turkic states in a redefined framework is very well worth analyzing in the following phase.

**Turkey’s energy policy in general**

Turkey’s new foreign policy is closely intertwined with its energy politics that considers energy security as a top national interest that informs its actions (Ögütçü 2001). To this end, the Caspian basin’s vast energy resources play a vital part. In addition, politics cannot be separated from the means to exercise it and energy is perhaps one of the most effective means in the field of international politics and thus an integral part of a country’s foreign policy. Although other energy resources such as hydropower and nuclear power also have an effect on the ties between two countries, it is oil and increasingly natural gas that are considered the paramount political energy sources that have a profound effect on international relations (Iskit 1996).

One of the key elements that determines Turkey’s overall energy policy is its widening gap in its energy supply and demand. Turkey has been pursuing policies in order to meet its expanding energy need based on diversified, reliable and cost-effective supply sources. Another key element determining Turkey’s energy policy regarding the Caspian region in particular is its striving to become a participant in the Caspian production of energy in order to profit from its lucrative business (Bardakç 2003). Though perhaps the most important element is that its geographical position offers unique possibilities to transit the region’s vast oil and especially gas resources to the Western markets. This was a direct cause of the EU commission’s publishing of the Green paper titled “Working towards a European strategy for the security of energy supply”, which emphasized uninterrupted flows of gas through secured and diversified external energy. In this respect, the EU acknowledged Turkey as a key transit country, transporting Middle Eastern and Caspian gas to the European markets, attaining a key role in ensuring European energy security (see section 5.7.3).

Turkey, which is one of the biggest investors in the Caspian region, acts not only due to its commercial interests but also feels responsible for supporting the Caspian nations in their social and economic development. The efforts of the trans-Caspian nations to bypass Russia when transporting hydrocarbons, has led to the rise of Turkey as an important player in the export of Caspian oil and gas. As Turkey's grander ambitions in the region began to fade and the Caspian oil boom picked up steam, the Baku-Tbilisi-Ceyhan (BTC) oil pipeline project as the first component of the Eurasian energy corridor increasingly became the core of Turkish energy policy towards the Caspian region and indeed an important priority of Turkish foreign policy overall in which Russia is bypassed in favour of Georgia to get Azerbaijani oil to the Mediterranean Sea. The second component of the Eurasian energy corridor was the South Caucasus gas pipeline running parallel to the BTC oil pipeline, which is considered to be the first leg of the trans-Caspian gas pipeline. The possible support for the BTC oil pipeline, however, was implicitly linked to the success of the South Caucasus gas pipeline, since the

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42 As a country with an emerging and rapidly growing economy, Turkey is facing a rising growth of its demand for energy by 8 percent per annum whereas the world average is 1.8 percent.

43 British Petroleum was leading both the BTC oil pipeline and the South Caucasus gas pipeline project consortium.
laying of both of these pipelines would effectively increase the cost effectiveness (Ögütçü 2001, pp. 10).

**Turkey’s energy policy towards TCGP and alternative projects**

Turkey, in May 1999, signed an intergovernmental agreement with Turkmenistan to supply 16 billion cubic meters of natural gas per year beginning from 2002 with the prospect of delivering an extra 14 bcm per year onwards to the European markets (Ismailova 2001). Furthermore, although the discovery of the Shah Deniz field in late 1999 in offshore Azerbaijan had increased the already complex negotiations on the trans-Caspian gas pipeline (see section 4.6.7), Turkey was cooperating with the United States to try to bridge the differences between Azerbaijan and Turkmenistan and to keep the TCGP project on track 44. Although, Turkey did allocate time and effort to the realization of the TCGP, it needs to be said that it was more actively involved in supporting alternative projects, the Iranian and especially the Blue Stream gas pipeline project which weakened support to the TCGP deal (Ersoy 2000). This project envisioned to bring 16 bcm of additional Russian gas directly (no transit country involved) to Turkey, saturating the Turkish offtake market and not leaving enough offtake capacity for the TCGP (see section 4.5.2). In the end, Turkey intensively supported the implementation of the Blue Stream pipeline (BSP), which steamed ahead of the TCGP, afflicting a major blow to the latter 45.

Turkey’s active support for the Blue Stream pipeline in particular is hard to explain at first sight, considering that it would make it even more dependent on Russian gas. On the other hand, however, it would mean a diversification of its gas routes, thereby making its supply more reliable. Another explanation as Necdet Pamir 46, a renowned energy expert in Turkey, pointed out is that there were powerful corporations pressing the Turkish government to implement the BSP. The corporations would gain substantial deals from this transaction. In addition to this, the realization of this pipeline project had a strategic significance for the bilateral relations. This was underlined by the then Prime Minister Chernomyrdin’s declaration after the signing: "No more Chechen and no more PKK problems" 47. All in all, despite the fact that Turkey did support the attempt to realize the TCGP, it was at the same time pursuing a multi-vector approach. However, Turkey dedicated more time and effort to the realization of the BSP, which diminished the chances of the TCGP.

**Iran and Russia: standing between Turkey and the TCGP**

In this section, first some background information is given about Russia’s and Iran’s development as a regional power in the ‘New Great Game’ in the Caspian region. Then the relations of Turkey with Iran and Russia will be examined with regards to the ‘New Great Game’ and the TCGP in particular.

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44 President Süleyman Demirel of Turkey brought a two-day visit to Turkmenistan in the beginning of April 2000 in order to sort out the differences between the latter and Azerbaijan. As a result of President Demirel’s mediation efforts, President Niyazov accepted to add 5 billion cubic meters of Azeri natural gas to the 30 billion cubic meters already agreed. Moreover, Demirel’s visit resulted in a withdrawal of Niyazov’s demand of an upfront payment, only to be dismissed not long after.

45 The groundbreaking ceremony of the Blue Stream gas pipeline on the 10th of February in 2000. The pipeline project was put into operation in 2003.

46 (Interview with author, Ankara, 29-10-2008)

47 He was referring to Russia's belief that Turkey aided the Chechens during the 1994-1996 war and to Turkey's own suspicions that Russia supported the terrorist PKK group. Prior to his arrest in February 1999, the PKK leader Abdullah Ocalan sought shelter in Russia to the dismay of Turkey. Blue Stream advocates have argued that certain Russian circles could revitalize the PKK unless there was strong commercial co-operation, with Blue Stream at the heart of the strategic partnership.
Iran: a pragmatic radical

In the early years of the “New Great Game”, Iran has been less of a player due to several reasons, though it has taken a lift from the mid nineties. Among the factors that have prevented Iranian influence to expand in the region are its overwhelming Shi’ite population, while the majority of the Muslims in Central Asia and the Caucasus are Sunnis; its openly theocratic character, which is incompatible to the region’s secular leaders; and its policy of confrontation with the West, while the newly independent states were rightly focusing their attention to the West appealing for aid and assistance.

In the second half of the nineties Iran has had some success in projecting a more positive image in the region. The most important factor contributing to this positive image was the utilization of a more moderate policy than originally anticipated. It has been quite diligent and careful at the same time not to give out signals of trying to destabilise the region with its revolutionary rhetoric. In this respect, Iran's alliance with Russia and the mutual understanding regarding preservation of stability in the Caspian region has played an important part. Though once viewing each other as enemies, after 1991 it became clear that Russia and Iran shared similar interests in the region. The Russian-Iranian alliance can be regarded as the most remarkable and important geopolitical episodes of the post-Cold War era (Amineh 2003).

Historically speaking, Iran has close links with the Caspian region. It has the aspiration to use these links to secure its own economic interests in the region. As a matter of fact Iran’s main aim is to enhance its own economy through economic cooperation with the Caspian region. In this respect Iran aspires a gas pipeline running from Turkmenistan via Iran to Turkey and then on to the European markets, considering the TCGP as the undisputed rival for the realization of its own gas pipeline. However, Iran has failed to develop a regional foreign policy. In general, Iran's internal economic problems give it little to offer Central Asia and the Caucasus in terms of finances and technology. In addition to this, U.S. opposition to any major Iranian involvement in Caspian oil and gas development and transportation crippled its capabilities, also with respect to the Turkmenistan-Iran-Turkey gas pipeline (Olcott 2004).

Turkish-Iranian relations: cooperation and conflict

Iran naturally opposes Turkey’s foreign policy towards the Caspian region as they consider Turkey as a competitor and a threat to their own regional foreign policy goals. They have become rivals in attempting to create spheres of influence in the Caspian region. Turkey was concerned that Iran may attempt to turn Muslim nationalities toward theocratic rule, while Iran was worried that Turkey's active role in the region is aimed at forging Pan-Turkic hegemony on Iran's northern and western frontiers. Thus, for a while both countries vied for the hearts and minds of the Turkic-Muslim states in the region. In spite of their initial enthusiasm in approaching these republics, however, it has become increasingly apparent that both Turkey and Iran lacked the economic resources that would enable either of them to exercise a dominating influence in the region. Moreover, Iran is against the laying of the trans-Caspian gas pipeline as they want to see this pipeline go through their own territory. Iran is keen to transport together with the Turkmen gas also Iranian gas to the European markets, however, this is countered with substantial U.S. force.

Besides viewing each other as rivals in the quest for regional dominance in the Caspian region, there has even been significant cooperation between the two countries as they in 1996 signed a US 23 billion dollars deal on gas delivery for a period of 23 years connecting Tabriz, Iran with Konya, an Anatolian province in Turkey. The signatories to this accord also indicate
that eventually Turkmen gas can be routed through this conduit to Europe, which would of
course increase the transit fees collected by these states. Turkey stayed on the course despite
strong US opposition because of the fact that Turkey viewed this deal as an opportunity to
secure and diversify its energy supplies.

Russia: determined to remain a hegemonic player in the Caspian region

Although Russia had no coherent policy toward its former colonies on its southern
borders for about a year or so after the break-up of the Soviet Union, suddenly from late 1992
onwards and especially after the ultra-nationalist bloc had won the elections in 1993, started
to exhibit a keen interest in the region, redefining it as the "Near Abroad" (Amineh 2003). By
1994, the power vacuum created by the collapse of the USSR had proved to be a temporary
phenomenon. Since then the Russian main political groups and elite have agreed that Russia is
a great power with a keen interest in the near-abroad and that Russia’s own interests has to be
stressed before pro-Western policy. To this end, Russia only supports pipelines that crosses its
own territory. In addition to this, the extensive political, historical and economic ties forged
over the years between Russia and the former Soviet republics in Central Asia and the
Caucasus should not be overlooked. In this respect, Russia is enjoying a prominent and
powerful position.

Russian-Turkish relations: cooperation and conflict

Russia is considered a significant obstacle to the achievement of the ambitions of
Turkey regarding the Caspian region. Turkey’s cooperation with the West adds to the
hostilities between these two countries. Russia views Turkey as a traditional geopolitical rival
in the Caspian region. However, the extent to which Turkey can be a threat to Russia’s clout
in Central Asia is disputable at the least. Although Russia at first welcomed Turkey’s
engagement in Caspian geopolitics, offering it an alternative to the Islamist based Iranian
model, it soon made Russia question whether Turkey was aiming at regional hegemony
and/or a revival of pan-Turkic unions. Moreover, the energy politics of both Turkey and
Russia towards the Caspian region are an obstacle to friendly relations with each other. Russia
objects to any pipeline towards the West including the TCGP and Turkey opposes to a
pipeline towards the north passing through Russia. What is at stake here is not only oil and
gas transit revenues from pipelines passing through their own territories, but more
importantly, this pipeline network is one of the key factors in securing and maintaining
influence throughout Central Asia and the Caucasus.

Turkish-Russian ties can also be characterized by significant cooperation. Turkey’s main
partner in the economic arena in the nineties was Russia. The intense interaction was due to
major diplomatic efforts on both sides. A major step into this direction was the inclusion of
Russia in the Black Sea Economic Cooperation Project (BSCE) 48. BSCE came into effect in
1992, orchestrated by Turkey, including all countries adjacent to the Black Sea plus Greece.
The extent of economic cooperation greatly exceeded those with Central Asia and Azerbaijan
as it peaked in 1997. The overall bilateral trade volume, including non-registered trade by
tourists, reached around $10 billion in 1997, making Russia the second largest trading partner
of Turkey. Moreover, the Turkish construction did $8.5 billion of business in Russia in 1997.
These economic relations are not any different in the second phase as it grew only stronger
(see section 5.7.3). Worth noting in this respect, is off course the Blue Stream gas pipeline
project of which the realization period ran parallel to the TCGP. With Russia, recognizing the

48 http://www.bsec-organization.org/Pages/homepage.aspx
Blue Stream as a top priority, this project would most definitely consolidate and determine the direction of Turco-Russian relations.

**USA: a strategic ally of Turkey**

The United States strongly supports the western pipeline route through Turkey, bypassing Iran and Russia. As Turkey’s and the United States’ interests in the region overlap, the United States from the start supported Turkey's rapprochement towards the region. However, as it became increasingly clear that Turkey's financial resources and political weight would not be enough to counterbalance Russia's neo-hegemonic resurgence in its near abroad and given the substantial investments of American transnational corporations in the region, the United States moved with more determination to disrupt and even replace Russian influence. Though, this is done with sheer prudence, not eager to unleash another Cold War. The US has opted for the Baku-Tbilisi-Ceyhan oil route and the trans-Caspian gas pipeline in tune with the Eurasian Energy Corridor. Such advocacy of the Turkish position is a prudent one for Washington, as the route westward is not only likely to prove viable and secure, but should bring significant revenues to Turkey to finance future development projects. This is in the interests of American foreign policy, because of the fact that a strong Turkey represents a positive, secular model for the newly independent Turkic republics of the region who are always being challenged by fundamentalist Iran. Turkey, which is geographically located within a region that is characterized by dictatorial regimes and prone to fundamentalism, represents a beacon of stability and a textbook example of a secular, democratic but Muslim country. These features are most appealing for the United States, which explains why Turkey is a strong strategic ally of the United States. In terms of cooperation during the first attempt, Turkey and the U.S. have struggled side by side to break through the impasse of negotiations between Turkmenistan and Azerbaijan regarding the allocation of gas into the TCGP (Gültasli 2000). Hence, the relations between Turkey and the USA can be classified as cooperative as their interests with regards to the realization of the TCGP matches.

Turkey has been and still is attempting to perform a delicate balancing act between USA on the one hand and Russia on the other. Leaning too much to one side could cause harm to the relations with the other. Although, the United States is viewed by Turkey as the more traditional strategic partner, it is, however, aware of Russia’s importance as a trading partner and that it is a neighbour with significant regional power with which one has to reckon with.

**4.6.4 TCGP: in between the ‘old’ and the ‘new’ world of gas trade?**

Naturally, the PSG international consortium, established to construct the TCGP in the first attempt, would only be interested in investing if there is a reasonable rate of return over the lifespan of the project. In view of the available alternatives, the issue of the economics of the TCGP was controversial. Some found the route quite unattractive due to potential inability of Turkmenistan to offer competitive gas prices as the financial costs of the pipeline would be too high. Moreover, also because the Turkish market was not large enough given that Turkey would be the only potential buyer at lease in the short term and given that the Blue Stream pipeline was advancing fast. On the other hand, there were also sounds, that considered demand profiles for Azerbaijan, Georgia and Turkey, and looked at factors influencing the economics of the TCGP, claiming that under most of the future worlds the TCGP could yield positive returns and could be beneficial for all parties involved (Turkmenistan, transit countries and Turkey) (Gülen 1999). Having said the latter, in a purely ‘new world’ of gas trade the state would not interfere in the financing of a gas pipeline project. However, that is not the case here as there are uncertainties about the commercial viability of the TCGP, the
existence of a bad investment climate in Turkmenistan and the understanding by the U.S. in particular that there is more at stake than only the construction of some pipeline. The United States, being aware of the potential significant geopolitical implications of the trans-Caspian gas pipeline project and considering their own strategic goals and interests (see 4.6.2) does not disrelish making ‘political investments’. To this end, during the first attempt the United States had encouraged US financial institutions (lending agencies) to come up with a mechanism to fund the project. All in all, the aforementioned is a sound illustration of the fact that the trans-Caspian gas pipeline project was definitely operating in between an ‘old’ and a ‘new world’ of gas trade. This will also be researched in the second phase of the analysis.

4.6.5 Genuine environmental concerns or ‘geopolitics of gas’?

It can be concluded that Russia’s and Iran’s environmentally based objection is poorly substantiated. As a result of the analysis (see Appendix E), it can be asserted that mainly geopolitics of gas plays a significant part in explaining this strategic stance taken by Russia and Iran. Although it could not be assigned a big impeding role in the first attempt due to its poor substantiation, it was, however, an impeding (sub) factor in the margins. Moreover, when combined with other marginally impeding factors in the course of which the timing of deployment is essential, the impediment power might become substantial.

4.6.6 Legal status of the Caspian Sea: deliberate postponement?

The Caspian Sea is the world’s largest inland body of water. It covers approximately 275,000 square miles (around 700 miles long and 170 miles wide), and is relatively shallow, with an average depth of only 86 feet (25 metres) below sea level. The only outlet to the outside world is through the Don River and the Volga canal through Russia to the Gulf of Finland in the Baltic Sea.

It goes without saying that disputes over the legal status of the Caspian Sea bed’s subsoil oil and gas deposits bear directly on the political risks facing both states and oil corporations, both local and international, who desire to exploit these resources. The purpose of this section is to determine to what extent the unresolved legal status of the Caspian Sea has impeded the first attempt. To this end, Russia’s and Iran’s stance towards the legal status of the Caspian Sea will be researched, with the aim of uncovering the driving forces behind their strategic behaviour. This analysis can be found in Appendix F.

Impact on the first attempt

Iran and Russia’s stance on the legal status of the Caspian Sea is based upon their geopolitical and economic interests. Russia and Iran used this non resolved issue concerning the legal status of the Caspian Sea to oppose and hinder the realization of the TCGP, which obviously is a threat to their own interests in the Caspian region (see section 4.6.2). When it comes to assessing the impeding level of this particular (sub) factor, it can be said that, although the impediment power of this sub factor was not displayed in the first attempt, it did have the power to seriously delay the realization of the TCGP at the very least. Considering that this issue has legal enforceability, it is likely to be more effective than the objection on environmental grounds. However, it extracts most of its impeding power from the bilateral issues between Azerbaijan and Turkmenistan and in particular regarding the delineation of the of their adjacent Caspian Sea borders. In this respect, Azerbaijan’s stance that it is a matter of the countries across whose zones the pipeline crosses should not to be taken lightly. It is believed that, since the trans-Caspian gas pipeline will only cross the adjacent maritime
borders of Turkmenistan and Azerbaijan, the consent of both countries would be suffice. However, then it will be a question whether Turkmenistan is willing and able to resist Russian (economic and political) pressure. In addition to this, according to Jozias van Aartsen\textsuperscript{49}, the former coordinator of the Nabucco project, there are currently so many pipelines that are constructed in the Azerbaijani section of the Caspian Sea that it is claimed that a connection to the Turkmen coastline is relatively short in terms of distance.

4.6.7 Disputes between Niyazov and Aliyev and its ramifications

In this section the disputes between Azerbaijan and Turkmenistan and its impact will be assessed. In this respect, the implications of the discovery of the huge Shah-Deniz field will be analyzed, since it is believed that Azerbaijan’s altered interests has started a chain reaction which lead to a fierce impediment of the first attempt to implement the TCGP. The analysis can be found in Appendix G. The main purpose of this section is to find out to what extent these disputes between Niyazov and Aliyev have impeded the first attempt to implement the TCGP.

\textit{Impact on the first attempt}

The discovery in late 1999 of the large gas-and-condensate field at Shah-Deniz changed the overall equation. The Azeri president Aliyev made claims on almost 50\% of the volume of the TCGP. The discovery of this gas field gave rise to the revival of deep rooted tensions, also on personal level and initiated a chain reaction. Niyazov firmly disagreed and as a result he reacted by reiterating the first Turkmen claims to some major Azerbaijani offshore oilfields. The latter bilateral issue is the direct cause of the sharp differences regarding the exact delimitation of both country’s adjacent maritime borders. This event complicated the negotiations even further. When it comes to analyzing to what end Niyazov chose to revive this problem at this particular moment in time, one can think of the reason that Niyazov by reiterating claims to these oil fields tried to attain a bargaining chip by holding the outcome of the negotiations about the allocation volume hostage to the outcome of the Serdar/Kyapaz oil field. However, this was considered foolish since Azerbaijan had a better bargaining position. Furthermore, also Azerbaijani debts arising from unpaid electricity bills supplied by Turkmenistan added more fuel to the fire. It is claimed by unofficial sources at SOCAR (Huseynova 2001), the State Oil Company of Azerbaijan Republic, that the termination of the negotiations between these two countries and thus the cancellation of the pipeline project in October 2001 was the result of these ongoing bilateral issues and not so much the result of the announcement to construct the BTE gas pipeline. Considering the toughness of the events this assertion seems plausible. Hence, the ongoing bilateral issues between Turkmenistan and Azerbaijan should be regarded as one of the most decisive impeding (sub) factors that blocked the first attempt of the TCGP. Moreover, the bilateral issues should be seen as a \textit{precondition} that needs to be handled with in order for a future attempt to have the chance to become successful. Although, the realization of the trans-Caspian section of the TCGP was cancelled, the construction of the South Caucasus gas pipeline could make a prospected connection with Turkmenistan even more viable in the near future (see section 6.3). This will be explicated in the second phase.

\textsuperscript{49} (Interview with author, 28-2-2008, The Hague)
4.6.8 The role and influence of international institutions

The Energy Charter Treaty is an intergovernmental agreement that provides a legal framework to protect investment and secure trade and transit in the energy sector, entered into force in April 1998. The ECT adds a significant new tool in the arsenal of anybody facing an investment dispute in the energy sector. The treaty currently has 46 fully ratified members, under which Turkmenistan and Kazakhstan, plus an additional five signatories and 19 observer states. From that point on till the cancellation of the TCGP in 2001, the ECT has not played a substantial role of importance in creating investors’ confidence in general and with respect to the TCGP in particular. The first years of its commencement, the ECT enjoyed very little attention and authority within its member states (Victor 2004). Nevertheless, this might have changed over time as it will be looked upon in detail in the second phase of the analysis.

The Organization for Security and Co-operation is the largest regional security organization in the world. It conducts a wide range of activities related to all three dimensions of security — the human, the politico-military and the economic-environmental. It has a total of 56 participating members, including the offtake and transit countries and the host government Turkmenistan. During this summit in Istanbul, Turkey, Turkmenistan, Georgia and Azerbaijan signed the “Intergovernmental Declaration on the Principles for Implementing the trans-Caspian gas pipeline”. In tune with the declaration, a joint committee was established to negotiate the intergovernmental agreement and host government agreements for the project (CSIS 2000). Turkey has also signed a “Memorandum of Understanding” with Azerbaijan and Georgia at this summit. It supports mutual cooperation regarding the sale and purchase of Azeri natural gas by Turkey. A possible cooperation between Azerbaijan and Turkmenistan for the transportation of natural gas to Turkey and further on to Europe will increase the benefits for both countries. The most valuable part of this OSCE summit in Istanbul with respect to the TCGP was supposed to be the settlement of the dispute between Azerbaijan and Turkmenistan regarding the Turkmen claims on some Azerbaijani offshore oil fields in the Caspian Sea. It was ostensibly settled at this summit as Niyazov initialled the concerning documents. However, this had proven to be premature as Niyazov reiterated its claims during negotiations with Azerbaijan about the division of the allocation of the volumes (see section 4.6.7). Nevertheless, the abovementioned indicates that such an institutional platform did prove to be of added value, since several bilateral and multilateral agreements were signed with respect to the TCGP.

The participation of U.S. financial institutions (lending agencies), namely the Export-Import Bank and the Overseas Private Investment Corporation (OPIC), were considered crucial, both for financing of the trans-Caspian gas pipeline and the commitment of political will. This is especially apparent considering the reluctance transnational oil corporations had shown in making substantial investments in the Turkmen energy sector as their investments enjoyed little assurances and protection from the legal and regulatory framework (see section 4.3.2). The actual participation of these financial institutions was due to the strong support of the US government for the TCGP as Washington mobilized them to come up with a mechanism for financing the trans-Caspian gas pipeline project (Newsbase 2000).

After Heydar Aliyev came to power in 1993, relations between Turkmenistan and Azerbaijan changed. Azerbaijan’s membership in the Commonwealth of Independent States helped to improve bilateral economic and political relations. In 1995, Azerbaijan became a major trading partner of Turkmenistan. Their relations climaxed at a visit by Niyazov to Azerbaijan in March 1996. During the visit, both presidents declared that there were no serious contradictions in the relations between two brother nations, and signed a dozen...
intergovernmental agreements. However, the time of the dispute with Turkmenistan around the fields and determinations of the fixup value for the middle line between the sectors of both countries in the Caspian Sea started in February 1997 (Ogli 2000). Niyazov claimed that the “Azeri” oil field was situated in the Turkmen sector of the Caspian Sea and that Azerbaijan exploited it illegally. This was the start of the deterioration of the relations between the two countries, followed by more Turkmen claims on other oil fields located in the Caspian. Although the CIS platform initially played a pivotal role in improving bilateral economic and political ties in middle of the nineties, eventually the clashing economic interests in the Caspian Sea and other bilateral issues would prove to be more influential in shaping their relation.
4.7 Conclusions

In this section, an answer is provided to the sub research questions stated in the beginning of this chapter. The answer is based upon the conducted analyses in this chapter. As such, first an answer will be given to the following sub research question:

*To what extent and under which conditions contributed the four ‘explanatory factors’ to the advancement and especially impediment of the failed first attempt to realize the TCGP in the period of 1997-2001?*

Below in table 4 an overview is given of the relevant (sub) factors.

<table>
<thead>
<tr>
<th>Actors/Agents</th>
<th>Investment climate</th>
<th>Transit risk</th>
<th>Offtake market risk</th>
<th>Geopolitics</th>
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<tbody>
<tr>
<td>States</td>
<td>- Political structure of Turkmenistan</td>
<td>- tough Azeri-Turkmen negotiations - ongoing bilateral issues</td>
<td>- Turkey’s adherence to Blue Stream Pipeline - Turkey’s overestimation of its gas demand</td>
<td>- Implementation Blue Stream Pipeline project - Environmental objection - illegal without littoral pact on division Caspian Sea - President Niyazov’s irrational and non-pragmatic behaviour - Turkey’s ambiguous stance by betting on two mutually exclusive pipeline projects - US (financial and political) support</td>
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<tr>
<td>Non-states (TNOC’s)</td>
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<td></td>
<td>- International consortium led by US companies</td>
<td></td>
</tr>
<tr>
<td>Institutions</td>
<td></td>
<td>- U.S. lending agencies’ financial commitment and political will</td>
<td>- OSCE in 1999, platform for signing agreements</td>
<td></td>
</tr>
</tbody>
</table>

Table 4: Overview of the relevant (sub) factors in the failed first attempt

The main impeding (sub) factor related to the *investment climate* regards the political structure of Turkmenistan, which allows a highly autocratic and totalitarian rule of the President. All the political power is concentrated in the office of the President, which takes all the important decisions. In such a country, the risk of detrimental reign and political instability is much higher, which was the case with Turkmenistan during the first attempt. This fact combined with the erratic and non-pragmatic behaviour of Niyazov has severely impeded the first attempt to realize the trans-Caspian gas pipeline project.

With regards to the factor *transit risk*, it can be stated that the problems started when Azerbaijan’s role changed from being merely a transit country to also becoming a host country changing its energy security and economic interests and reinforcing its bargaining
position. Azerbaijan demanded nearly 50% of the throughput capacity of the trans-Caspian gas pipeline after the discovery of the Shah-Deniz gas field. This had initiated a chain reaction in which the mutual understanding between president Niyazov and Aliyev went from bad to worse as the former reiterated its claims over the disputed oil fields in the Caspian Sea. It is even asserted that these ongoing bilateral issues between the countries have eventually led to the decision to terminate the negotiations and thus should be considered as the most decisive (death blow) impeding (sub) factor and a precondition that needs to be resolved before future attempts are undertaken.

Regarding the factor offtake market risk, Turkey, as the most immediate market in the short term for the first attempt, overestimated its future gas demand. This became a problem when Turkey in conjunction with Russia decided to construct their own direct gas pipeline to the Turkish mainland, namely the Blue Stream gas pipeline. Consequently, these two giant gas projects were vying for the Turkish gas market, knowing that the loser probably would be shut out for some time as the Turkish offtake market was just not big enough to absorb both. The Blue Stream gas pipeline was winning the race to the Turkish market and this severely hurt the economic viability and attractiveness of the pipeline project.

Last but not least, there is the factor geopolitics. From the actors that strongly opposed the trans-Caspian gas pipeline project (Russia and Iran), it can be said that Russia was the one that had the most to lose in terms of economic and political leverage over Turkmenistan and in terms of strategic importance for supplying large amounts of gas to Russia. In addition, Russia was also considered the most powerful opponent that the actors in favour of the pipeline would have to face up against in attempting to realize the TCGP. To this end, Russia pulled quite a few strings to hinder the progress of this pipeline project; first of all, it steamed ahead with the Blue Stream pipeline saturating the Turkish gas market and handing out a severe blow to the TCGP project. Furthermore Russia also entered into talks with Turkmenistan amidst the TCGP negotiations to further open up the northern connection. This hurt the negotiations, since such an agreement would not leave enough gas for the TCGP. In addition, Russia joined with Iran to press the case that the trans-Caspian gas pipeline project is environmentally risky and illegal without a littoral pact on dividing the Caspian Sea. Moreover, the latter’s future impeding level should be assessed on the basis of whether Turkmenistan is willing to adopt the stance of Azerbaijan, namely that it is a matter of the countries across whose zones the pipeline crosses. If adopted, this would diminish the impeding level of the (sub) factor in question.

Although Turkmenistan had much to gain from the trans-Caspian gas pipeline project, its actions were considered counterproductive and have been hindering the progress in the first attempt. This is predominantly because of President Niyazov’s non-pragmatic and irrational behaviour during the negotiations. His behaviour had frustrated the involved parties to the extent that it even caused the withdraw of two out of three companies from the PSG international consortium. Considering the close entanglement between Washington and the U.S. companies, the latter’s withdraw from the consortium was a sign of a fundamental shift in U.S. policy toward Turkmenistan. It should be viewed as a decline of U.S. support for the trans-Caspian gas pipeline, which is crucial for the implementation of this project, particularly with regards to the financing. Moreover, the United States, Azerbaijan and Turkey as a result of Niyazov’s stance in the negotiations redirected their time and effort to the South-Caucasus gas pipeline in order to keep at least some portion of the Eurasian energy corridor alive.
Furthermore, the participation of the U.S. national financial institutions (lending agencies) and thus the support of the United States have been crucial to the TCGP project in terms of financing and the commitment of political will. It is believed that otherwise the trans-Caspian gas pipeline project would have definitely stalled on this particular issue, considering the unhealthy and risky investment climate of Turkmenistan and the contentious economic feasibility studies about the TCGP project. In addition, the Organization for Security and Co-operation (OSCE) as an institutional platform have provided to be of high added value, since several bilateral and multilateral agreements were signed with respect to the TCGP. Moreover, the United States’ participation into the ‘New Great Game’ has created a tense situation in the Caspian region increasing the polarization and geopolitical rivalry with Russia. The strong U.S. support for the TCGP has without a doubt played a role in augmenting Russia’s decisiveness to block it.

The second sub research question that needs to be answered is the following:

*What was the role and influence of Turkey during the first attempt?*

First of all, Turkey’s role was that of the sole offtaker of Turkmen gas and have acted as one by signing a bilateral agreement with Turkmenistan for the delivery of 16 bcm per year to Turkey and 14 bcm per year onwards to the European markets. With respect to the TCGP, Turkey’s interests coincided with those of the United States, leading to cooperation on attempting to bridge the differences between Azerbaijan and Turkmenistan during the tough negotiations. But it was the United States that was leading the project and pulling the strings. Turkey had just a minimal role in this respect.

The fact remains that Turkey was the intended off take market for the Turkmen gas in the first attempt, which brought along a certain degree of influence as it could ‘break’ the project. In this respect, Turkey’s influence was particularly visible when it lifted its condition that it would only receive Azerbaijani gas if the trans-Caspian gas pipeline was realized. By doing this, Turkey opened the door for negotiations on the South-Caucasus gas pipeline, redirecting the concerned actors’ time and effort to this project. Furthermore, although Turkey was backing the TCGP project, it was also pursuing alternative projects, such as the Iran-Turkey gas pipeline and the BSP project in particular while its gas market was not big enough to absorb the gas from both the BSP and the TCGP projects. Turkey’s active support for the Blue Stream project in particular is hard to explain at first sight, considering that it would make it even more dependent on Russian gas. On the other hand, it would mean a diversification of its gas routes eliminating any transit risk by connecting directly to the source and thereby making its supply more reliable. Another explanation, however, is that there were powerful domestic corporations pressing the Turkish government to implement the BSP as the corporations would gain substantial deals from this transaction.

In conclusion, although on the one hand Turkey was indeed supporting the trans-Caspian gas pipeline project in view of its energy security interests, it was its discriminative allocation of time and effort to the Blue Stream gas pipeline project in particular, which steamed ahead of the trans-Caspian gas pipeline project and saturated its gas market, that resulted into becoming accessory to impeding the first attempt.
5 Analysis of the ongoing second attempt (2nd phase)

5.1 Introduction

In this chapter, the second phase with respect to the attempt to realize the trans-Caspian gas pipeline project will be analyzed (see figure 2). The timeline of the second phase commences from the moment that it was announced by Azerbaijan that the TCGP will not be built, which was in October 2001 and runs until the present. The main purpose of this chapter is to ascertain the actual development of the main (sub) factors determined in the first phase of the analysis (failed first attempt). It will be determined what the driving forces are behind the development of these factors and subsequently what the current influence is of these factors on the ongoing second attempt to realize the TCGP project. In addition also new (sub) factors may emerge, which must be taken into consideration as well. Furthermore, since Turkey is the main actor in this research, its role and influence in the ongoing second attempt to realize the TCGP will be investigated as well.

In this second phase, the following sub research questions will be answered:

What are the main alterations to the operationalized Case Study Protocol in the ongoing second attempt to realize the trans-Caspian gas pipeline?

What are the main alterations to the explanatory factors taking into account their development over time from the first attempt till now and to which extent do they contribute to the advancement or impediment of the ongoing second attempt to realize the TCGP?

Are there any new (sub) factors that have emerged in the second phase and what is their influence on the ongoing second attempt to the extent that it is possible to determine it in this stadium?

What is the role and influence of Turkey in the ongoing second attempt to realize the trans-Caspian gas pipeline?

The outcome of this chapter is a discussion on what the current influence is of the main (sub) factors from the first attempt, taking into account their development over time. Furthermore, also the influence of newly emerged (sub) factors in the second attempt will be discussed.

5.2 Adjusting the operationalized Case Study Protocol

Naturally, changes have occurred in relation to the previous phase that needs to be taken into consideration when analyzing the ongoing second attempt. This means concretely that modifications will have to be made to the operationalized Case Study Protocol answering the following sub question:

What are the alterations to the operationalized Case Study Protocol in the ongoing second attempt to realize the trans-Caspian gas pipeline project?

One of the most important characteristics of the second phase that ought to be taken into account is that the second attempt is ongoing and cannot be analyzed with hindsight in a manner similar to the analysis of the failed first attempt. The first attempt has a clear end
whereas the second attempt is still in its first stage (see section 2.3). In addition, the original Case Study Protocol was designed for gas infrastructure projects that have already finished (built or not) to which it thanks its static characteristic. However, the results of the analysis of the first attempt provide sufficient grounds on which the second phase can be analyzed (see section 2.4). The operationalized Case Study Protocol should be adapted nonetheless as this is elucidated below.

First of all, besides focusing on the development of the main (sub) factors identified in the first phase, the second phase should also take into account the identification of potential new (sub) factors and their influence on the ongoing second attempt. In this respect, the Nabucco pipeline project is bound to deliver the Turkmen and/or Kazakh gas to the European markets as a result of which a mutual dependency is apparent with the TCGP. It is believed that more of these mutually dependent large gas pipeline projects will emerge in the future connecting various regions, which brings along the identification of a new factor: ‘the interconnected gas pipeline project’. It will be researched how the interdependency between the TCGP and the Nabucco gas pipeline project is constructed. However, it is not the idea to identify and analyze the factors that influence the attempt to realize the Nabucco project. This is considered outside the scope of this study. Moreover, it is believed that it should be included in the original Case Study Protocol to increase its completeness and therefore its analytical strength.

With regards to the investment climate section in the Case Study Protocol the most important modification is the addition of another host country, namely Kazakhstan. As Kazakhstan is increasing its potential to become a major gas exporter in the near future (Ögütçü 2006, pp. 1-2), it became a potential host country in the second attempt to feed the trans-Caspian gas pipeline. Noteworthy is that adding new actors might mean that new explaining sub factors (aspects) will come into play.

Regarding the section transit risk in the Case Study Protocol a number of new transit countries are introduced in the second phase, since the trans-Caspian gas pipeline project was revived with the purpose of feeding the Nabucco gas pipeline. The newly added transit countries are Bulgaria, Romania, Hungary and Austria. In addition also Turkey’s role has changed. As a consequence of the Nabucco project, Turkey’s main role with respect to the TCGP is that of a transit country. Moreover, also Turkmenistan is added as a transit country, since the prospected TCGP is supposed to originate in Kazakhstan and then be routed into Turkmenistan where it will be supplemented with Turkmen gas (see section 5.3).

With respect to the offtake market risk section of the Case Study Protocol the main alteration concerns the fact that all the abovementioned newly added transit countries with the exception of Turkmenistan are also considered offtake markets for the Turkmen and/or Kazakh gas. These countries will need to be taken into account as well when analyzing this particular factor.

The main change with regards to geopolitics is the proactive involvement of the European Union and China in the ‘New Great Game’, increasing the competition. As a result, the dynamics of the struggle for Caspian gas is intensified. The impact of this change on the ongoing second attempt to realize the trans-Caspian gas pipeline ought to be examined. Furthermore, the 9/11 terrorist attacks in 2001 and the war on terror as a result also had geopolitical implications regarding the Caspian region. The aim is to find out how these events have had an impact on the struggle for Caspian gas in the ‘New Great Game’ and the
trans-Caspian gas pipeline project in particular. Furthermore, Turkey’s stance and strategic behaviour will be researched with respect to the Nabucco pipeline project and also what this project entails for Turkey in strategic sense since it is the problem owner of this dissertation. Moreover, access to and an independent assessment of the size of the gas fields was not considered an important issue during the first attempt. In the ongoing second attempt this might be more of an issue. For that reason, access to gas fields and independently acquired data about the size of the gas fields will have to be included from the perspective of the transnational corporations.

5.3 General information on the trans-Caspian gas pipeline project

The realization of the South Caucasus gas pipeline (SCP), running from Baku, Azerbaijan through Georgia to Turkey, has changed the prospects for the trans-Caspian gas pipeline. Since it would only be necessary to construct an underwater pipeline from Turkmenistan (and probably some new pipelines in the country from the eastern areas) to connect with the SCP in Azerbaijan, such a connection could effectively reduce the length of the TCGP from 1,600 km to 1,000 km. This would significantly reduce the costs of the project. Previously, the total costs were estimated at $2.4 billion, including the costs of construction in Azerbaijan, Georgia and Turkey. The reduction in length, cost and construction period makes the TCGP a viable and attractive project. Furthermore, Kazakhstan’s huge potential as a future gas supplier has attracted Western interests as it is proposed by the United States and the European Union to connect Kazakhstan with the trans-Caspian gas pipeline. Kazakhstan is planning to produce 60-80 bcm of associated gas50 by 2015 as proclaimed by the Kazakh President Nazarbayev (Interfax 2006). The proposed trans-Caspian gas pipeline would originate near the Tengiz field in western Kazakhstan and be routed south to Turkmenbashi, on Turkmenistan’s Caspian coast, supplemented by Turkmen gas before heading offshore to Baku, Azerbaijan. The actual second attempt is believed to have been reinvigorated after the events in early 2006. After Europe had enjoyed four decades of unbroken flow of Russian gas, a brief cut off of deliveries in January 2006 by Gazprom, the Russian gas monopoly, raised serious questions about Russia’s reliability as a supplier. Western support for the high cost sub sea gas pipeline reflects growing anxiety about energy security concerns worldwide, particularly in the European Union, since its dependency on gas imports is expected to grow substantially in the future (EU 2000, pp. 117). To this end, the European Union has financed a feasibility study of 1.7 million euro’s– looking at business, engineering and environmental issues – and was due to present initial findings in December 2007 with a final report by December 200851. The EU sponsored study off course gives a strong political signal, hoping that it will open doors and speed up procedures. This second attempt is not as advanced in its development as the previous attempt to construct the TCGP. The various parties (transnational oil corporations, Turkmenistan, Kazakhstan, EU etc.) are awaiting the results of the feasibility study before concrete steps are taken (establishing an international consortium etc.) to realize the project.

50 Associated Gas is natural gas which is found in association with crude oil either dissolved in the oil or as a cap of free gas above the oil.
51 No publications have been made on this issue at the time of the publication of this dissertation, namely May 2009.
5.4 Investment climate

In this section, Kazakhstan’s investment climate is researched according to the guidelines stated in the operationalized Case Study Protocol in order to find out if there are any investment climate related (sub) factors that are influencing or may influence the ongoing second attempt. Moreover, also the development of Turkmenistan’s main (sub) factor(s) specified in the previous phase will be analyzed. Lastly, the potential influence of the liberalisation of the EU gas market on the ongoing second attempt will be analyzed.

5.4.1 Kazakhstan’s political life

Following the August 1991 abortive coup attempt in Moscow and the subsequent dissolution of the Soviet Union, Kazakhstan declared independence on December 16, 1991. It was the last of the Soviet republics to declare independence. Kazakhstan is a constitutional republic. The president is the head of the state. He is also the commander in chief of the armed forces and may veto legislation that has been passed by the parliament. Nominally speaking, Kazakhstan is democratic, however, in reality it is a highly authoritarian and autocratic state in which the power is concentrated around President Nazarbayev and its inner circle. Nevertheless it is much more open and pluralist than Turkmenistan. The Senate (upper house) and the Majilis (lower house) are permanent legislative bodies, although they typically rely on leadership from the Ministries and Presidential apparatus. The key opposition leaders are in exile and political parties other than those supportive of the President do not tend to withstand. Members of President Nursultan Nazarbayev’s extended family own substantial stakes in promising private and parastatal industries (Sabonis-Shelf 2005).

President Nazarbayev’s re-election

Nazarbayev was re-elected as the President of Kazakhstan to another seven-year term in December 2005 in a landslide victory. Results have shown that he received more than 90 percent of the votes while his main opposition received only 6.6 percent (Saidazimova 2005). Although the OSCE evaluated the elections as not being coherent to international democratic standards (Saidazimova 2005), according to Peter van Leeuwen52, former ambassador for the Netherlands in Kazakhstan, the overwhelming majority as well as the high turnout of 77 percent send out a strong signal by voting on Nazarbayev. The people of Kazakhstan are content with the path the President has set out to run the country, suggesting that the population of Kazakhstan is satisfied with the country’s development and their own personal situation. Much of Nazarbayev’s popularity rests on years of uninterrupted economic growth, which has transformed Kazakhstan into a modern economy with a growing middle class.

President Nazarbayev’s growing power

A meaningful event is that the Kazakh President Nursultan Nazarbayev in May 2007 implemented into law constitutional changes permitting him to stand for office indefinitely. This event is interpreted as an extension of Nazarbayev’s pervasive influence over Kazakh life (RFERL 2007). Moreover, according to Peter van Leeuwen53, the ruling elite was also very keen to see him remain at his post as a President because they are content with the situation as it is right now. Opposition parties accused him of striving to establish a personality cult (Golovnina 2007). In the upcoming years to this event, Kazakhstan has seen Nazarbayev’s political and economic power grow substantially thanks to the soaring oil

52 (Interview with Author, 7-03-2008, The Hague)
53 (Interview with Author, 7-03-2008, The Hague)
prices. A highlight concerns the appointment of Timur Kulibaev, Nazarbayev’s son-in-law, to chair KazMunaiGaz’s new board of directors. KazMunaiGaz is one of Kazakhstan’s biggest state oil and gas companies. From that point on the oil sector came under the direct control of Nazarbayev and its family. This appointment is just the tip of the iceberg as several of Nazarbayev's children and their spouses have prominent positions in Kazakhstan's heavily intertwined public and private sectors. It is believed, though, that the reinforcement of Nazarbayev’s political and economic power will not seriously affect Kazakhstan’s standing in the world for a very practical reason; the Western interests in the abundant Kazakh mineral resources may overtake this concern.\(^5^4\)

**Lack of institution building**

A serious threat to Kazakhstan’s political and domestic stability in the short to medium term arises from the insufficient level of institutionalization that is supposed to guide and support a democratic change (Sabonis-Shelf 2005). According to Peter van Leeuwen\(^5^5\), Nazarbayev is doing little to ensure a smooth succession of his presidency. A development that consolidates President Nazarbayev’s negligence to establish a high level of institutionalization is that he was granted by Parliament to stand for office indefinitely (Golovnina 2007). This allowed him to put an end to speculation about the presidential succession among his advisors and his family members, strengthening his hand. The succession crisis may well bring to the surface a wide range of economic, political, ethnic and religious grievances that autocracy and comparative economic health had kept from submerging (RAND 2003).

Moreover, the long-term contracts prevalent in energy industries are particularly susceptible to subsequent action by new governments (Wälde 2008). There is even a higher risk if the country in question has a dictatorial, non-democratic rule. It would be a case of the new government against the old government where the private investors will simply be a victim. The investment disputes could entail expropriation, altering the terms of the contracts, altering tax laws etcetera. Hence, Kazakhstan with its insufficient level of institutionalization entails a political risk for private investors (TNOCs) who are especially active in the energy industries where long-term contracts are the rule.

**5.4.2 Kazakhstan’s Economic life**

With an average growth of 9.8% in real GDP in the first seven years of the twenty-first century, it can be stated that Kazakhstan is one of the fastest growing economies in the former Soviet republics. The main factor behind this development is a good external environment in which oil prices were sky high. This had not only an impact in terms of encouraging oil output but it also encouraged investments into the sector as the profits to be earned were very high. The growth of the FDI and real GDP is for a large part based on the growth in the oil and gas sector. In 2004 46% of all FDI went to the oil and gas sector and only 0.03% to agriculture. Moreover, its oil and fuel products accounted for 63% of the country’s exports (Shiells 2003). In addition to oil and gas resources, which have emerged as the number one attraction for foreign direct investment, Kazakhstan also has world class natural resources as coal, uranium, gold, aluminium, lead, copper, zinc etc. Furthermore, Kazakhstan has a great potential to become a major transit route for the transit of goods between Russia, Central Asian countries and China. Transit flows include oil and gas, connecting Turkmenistan and

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\(^{5^4}\) In sharp contrast to the opposition's criticism, the United States welcomed the amendments, which also included giving additional responsibilities to parliament, as a "good step forward for democracy in Kazakhstan".

\(^{5^5}\) (Interview with Author, 7-03-2008, The Hague)
Uzbekistan with Russia through existing pipelines. Its location is relatively close to the emerging markets of Russia, Central Asia and China, which presents opportunities to serve as a hub for transport and other services.

It has to be mentioned though that the economy of Kazakhstan has a low degree of diversification. Being dependent on natural resources and world prices makes a national economy vulnerable. Therefore, Kazakhstan's leadership had announced that other -- non-oil sectors of the economy should be developed, too. Among them are the production of machinery for the energy sector, metallurgy, textiles, and telecommunications. However, it is stated (Saidazimova 2006) that implementation of these reforms is the biggest problem in Kazakhstan. Corruption is widespread, which makes investment quite difficult. In addition, because of the fact that the Nazarbayev family is so entrenched, you ought to have the right connections to invest in Kazakhstan (Umurzakov 2003). Moreover, the state interference in the private sector is experienced as an obstacle to further economic development. All these aspects provide obstacles to diversify the economy, which implies that the degree of dependency on oil prices and revenues will probably continue in the future.

5.4.3 Legal regime of the energy sector and its governance in Kazakhstan

Since having acquired independence in 1991 from the Soviet Union, the Central Asian republic of Kazakhstan has been the most successful country in attracting foreign investors compared to the other former Soviet Union blocs. This is mainly due to the fact that the energy resources in Kazakhstan were not immediately available for exploitation as it was in for example Turkmenistan (Buiter 2001). This was done through a policy of opening up to foreign investment and privatization of most of the economy including the energy sector. The international investors had to be convinced of the business-friendly intentions of the government – a key aspect of their risk calculations. As a result, during much of the 1990s the Kazakh government was reform minded. In 1994 several laws concerning foreign investment were adopted, including taxation and petroleum laws, as well as a law on the European Union energy charter that will pave the way for Kazakhstan to bring its energy policies more closely in line with the West (Dorian 1994).

The Kazakh government has worked actively towards establishing an effective legislation framework to attract the much needed foreign investment. Its basic investment law, the Petroleum Law, was promulgated in January 1991 and provides tax breaks and guarantees against expropriation. Joint ventures and concessions are established on a tender basis. This Law has been revised many times as the Kazakh government was seeking a balance between investors and the Kazakh people. The taxes collected on oil projects in Kazakhstan were determined on a case to case basis, which allowed the government the space of flexibility, but dampening the interest of some foreign companies (Dorian 1994). The government preferred and stimulated the concept of equity joint venture arrangements, with particular emphasis on the exploration for oil deposits. Other types of arrangements are concessions56 and production sharing contracts. Foreign partners currently prefer the stability of production sharing agreements in Kazakhstan, given the concerns they have over political instability. It gives the private companies political advantages as it relieves nationalist pressures within the country.

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56 In the concession model, the government grants a private company a license to extract oil (and gas), which becomes the company’s property once extracted and who in return pays the government taxes and royalties for the oil.
However, the pace of economic reforms has slowed down gradually in this decade. It is even asserted that structural reforms have stopped now (Saidazimova 2006). Major economic sectors are controlled by family members and cronies of Nazarbayev. Moreover, with hindsight the rush to privatize is sometimes regretted by the Kazakh government. As the state enjoys more success in oil exports, the government on several occasions has expressed a desire to renegotiate its contracts with foreign investors, many of which it now feels were not designed sufficiently in its favour. A good illustration of this is that the state owned oil company KazMunaiGaz recently raised its shares in the giant Kashagan oil field paying just $1.78 billion and stripping Italy's ENI of its leading role in the project. This project will further be delayed to 2013 (Trend 2008). Analysts have interpreted the tougher stance of Kazakhstan as part of the growing trend of resource nationalism in other countries, such as Venezuela and Bolivia, instigated by soaring prices for oil (Stevens 2008). This will likely further tighten the control of Nazarbayev and its inner circle over economic resources, which in combination with a cease on structural reforms potentially poses a threat to the country’s investment climate.

5.4.4 Potential impact of the ‘resource curse’ on Kazakhstan

Kazakhstan also appears to follow the governance strategy of “no taxation, no representation” model familiar to OPEC states. It has failed to establish competence in taxation or budgeting. Transparency and high level of corruption remain problematic. In contrast to Turkmenistan, energy resources were not immediately available for exploitation and had to be developed first. To this end, Kazakhstan has opened up to foreign investment and rapid privatization followed. However, the one-time influx of revenues did not solve the deeper rooted problems. In order to protect the weak state, without making efforts to strengthen its competence, Kazakhstan has apparently relied on a strategy of privatization and using that to shuttle blame for government deficiencies to foreign investors (Sabonis-Shelf 2005).

The state has not enhanced its state capacity or bureaucratic competence. Instead, the state appears to be capturing oil rents without accepting obligations to its people. This may be the first of the anticipated “pernicious effects,” which will lead to economic decline and destabilization of the regime, but it is too early to say. As for now, Kazakhstan watchers are more concerned that, as Luong notes (Luong 2000):

“If current trends continue, Kazakhstan will emerge as a quasi-state – that is, one with international legitimacy but without the domestic capacity to generate sufficient revenue, address basic social problems, and promote even minimum levels of economic growth”.

As Kazakhstan is continuing to increase its reliance on oil and gas export revenues - in 2005 its oil and gas sector accounted for some 70 percent of the country’s exports (Pannier 2008) - and continues to omit to develop bureaucratic competence, one troubling trend is that as a state with significant oil and gas reserves, it can continue to borrow money in the international community. This grants them the opportunity to avoid structural changes and basically ensures that future generations will inherit substantial debt as well as incoherent political and bureaucratic structures. This will especially pose a threat at a time when oil prices decline and remain low for a substantial period of time, leaving the state incapable of paying back the required debt obligations and plummeting further into an economic crisis.
(see next section). This may fuel the civil unrest in the country, which could result into domestic instability endangering its investment climate.

5.4.5 Potential impact of the global financial crisis on the host countries

The main outcome of the analysis about Kazakhstan revealed that a sharp decline of oil prices is one of the main threats to its political and domestic stability and thus its investment climate. In this respect, the picture of economic growth averaging around 10% a year in the past seven years may be changing as in the second half of 2008 a global financial crisis has set in causing the oil prices to drop significantly. It is forecasted by the International Monetary Fund (IMF) that its economy will grow with a mere 1 percent in 2009 (SRI 2009). Burdened with large, quickly maturing debt by its banking sector and a large share of retail loans and mortgages issued in foreign currencies, the Kazakh government has pledged USD10 billion from the National fund57, which represents more than a third of its total value, to help recapitalize the country’s banks and to support real activity. However, the potential impact of the global economic slowdown on Kazakhstan has already raised concern among international creditors and rating agencies. According to the latest report by Fitch, a credit rating agency, Kazakhstan’s economic situation, while manageable at this point, could deteriorate if the global financial crisis continues for a long time (SRI 2009). This would put even more pressure on the nation’s government for financial support, which could overextend the National Fund, already under significant pressure.

When it comes to Turkmenistan, the global financial crisis will have a much lesser effect. The underlying reason is that its financial sector is much less developed than in other states of the former Soviet Union and as such global currents are less applicable (Tynan 2008). The simple reason for this is that the country hasn’t integrated with the global economy. It has not borrowed heavily and it has used its external rents gained from gas exports to finance development. Moreover, the rising prices of natural gas and oil and oil products, which together account for some 80 percent of Turkmenistan’s merchandise exports in 2007 (WB 2009), had brought along substantial export revenues. With these revenues its external public debt has been steadily reduced. By 2005, external debt stock was less than 60 percent of the 2000 level (WB 2009) making it even more immune to the financial crisis. Moreover, gas prices, although usually being linked to oil prices, is altered and adjusted periodically as agreed upon in the contract implying that it might take some time before the decline of oil prices shows its influence. In addition, inherent to the aforementioned argument the price clauses indexed to oil prices are revisable (flexible), reducing the actual effect of declining oil prices on gas exporting countries. Furthermore, it is expected that China and Turkmenistan, considering the China-Turkmenistan gas pipeline project (GI 2007) (see 5.7.4), will not index the gas prices to oil prices but that they will agree on a start price and on that the price is periodically revisable. It is believed that the actual price that Turkmenistan will receive in the future for its gas exports will mainly depend on the competitive pricing policy by Russia and China and perhaps Europe as well.

All in all, if the global financial crisis continues for a long time and with it the oil prices remain low, Kazakhstan faces the risk to be exposed to a deep economic crisis and dire social consequences. This might fuel the public’s anger and unrest plunging it into a long period of domestic and political instability. Therefore this uncertain period ahead cannot be overlooked.

57 The Kazakh National Fund is founded in August 2000 and is modeled after the Norwegian Government Petroleum Fund, and its main objectives are to accumulate savings for future generations and to reduce the dependence of the budget on world oil prices.
as it should be taken into account given that it has the potential to endanger the country’s investment climate and therefore Kazakhstan’s participation into the trans-Caspian gas pipeline project.

5.4.6 Turkmenistan’s autocratic leadership

It was concluded in the first phase that the political structure of Turkmenistan, which allows a concentration of all power in the office of the President, combined with President Niyazov’s fickle and unpredictable behaviour had formed a strong impediment to the failure of the first attempt to realize the trans-Caspian gas pipeline. For that reason this impeding (sub) factor is also taken into account in the second phase. It will be researched how this impediment has developed. In addition, its current influence on the ongoing second attempt will be researched in the section geopolitics.

The most defining event with regards to this (sub) factor is the sudden death of the former President Niyazov in late December 2006. Despite of the fact that no clear successor had been appointed and expectations of political turmoil and even a ‘catastrophe’ were drawn in case of the sudden death of Niyazov (Eurasianet 2004), the succession process occurred without any noteworthy tensions. Hence, the speculations drawn about the possible implications of this occurrence turned out to be incorrect. Berdymukhammedov was named acting president in late December after Niyazov’s death and as of February 2007, he was elected to president in what has been called an unfair election that fell short of international standards. On November 4, 2007, Berdymukhammedov have held talks in Ashgabat with Chinese Prime Minister Wen Jiabao (Blank 2007). The energy topic was at the top of the agenda in the discussions as the Turkmen leader expressed eagerness to proceed with the construction of a gas pipeline delivering of up to 30 bcm per year for 30 years starting in 2009. In addition, Turkmenistan granted licenses to Chinese entities to explore and develop natural resources on the right side of the Amudarya River (see figure 6). In his open-door stance, Berdymukhammedov continues to remain interested in a possible Turkmen participation in a trans-Caspian gas pipeline project. These actions indicate that the Turkmen president is not in a hurry to align itself with one of Central Asia’s major energy players, namely Russia, United States, China or the European Union. Instead Berdymukhammedov is determined to keep all the energy options open underlining its multi-vector energy policy.

In conclusion, although the political structure of Turkmenistan has not changed considerably, the appointment of the new Turkmen President Berdymukhamedov has brought a refreshing wind regarding the second attempt to realize the TCGP. He appears to be more realistic and pragmatic than the former Turkmen president. In this respect, neither the objectives nor the interests of Turkmenistan have altered but it is more the determination and pragmatism with which the new President Berdymukhamedov is proceeding to realize its multi-vector foreign policy that provides an opportunity for the concerned actors. In short, President Berdymukhammedov’s depicted actions promise a more sound and reasonable approach towards realizing this gas pipeline project than his predecessor.
5.4.7 Liberalisation of the EU gas market and its possible implications

Liberalisation of the EU’s gas market has the aim of creating internal and external competition based on a competitive unified gas market by integrating traditional and new suppliers (Libya, Nigeria, Qatar, Caspian countries) and by development of spot markets around gas ‘hubs’ as in Baumgarten, Austria. The objective is to secure lower-price supplies for all categories of consumers (Locatelli 2002). To this end, the traditional long-term contracts applied by Russia and Algeria are considered to hamper efficient competition as foreseen by the liberalisation of the gas markets. The overall character is not criticized as the ‘Take or Pay’ clauses of existing long-term contracts are relatively flexible and price clauses indexed to oil prices are revisable. However, it is the Final Destination clause in these contracts that is controversial, because it prevents competition between big intermediaries by preventing resale on other markets. Russia (Gazprom) and Algeria strongly oppose the abolition of this clause, partly because they want to maintain certain control over their end markets, but mainly because they want to prevent initial buyers finding extra value by reselling gas on other markets where prices are higher. Furthermore, the liberalisation also entails the gradual modification of certain contractual clauses concerning indexation of prices and multiple aspects of the pricing formulae and it may also result in a modification of exported volumes by increased flexibility of Take or Pay clauses. Overall, the liberalisation will probably increase exposure of traditional suppliers to ‘price risk’ and ‘volume risk’ (Locatelli 2002). In the longer term, adaptation of these contractual clauses (Take or Pay, indexation of prices and Final Destination clause) are strong constraints for Gazprom (and Algeria) since long-term contracts are the basis of the company’s investment financing in production and transport (Locatelli 2002). For Gazprom, as for other EU suppliers (such as Algeria), the Take or Pay clause and the clause on indexation to oil prices grant financial stability, which is necessary for large-scale investments.
Having said the latter, the same can be asserted for Kazakhstan and Turkmenistan as well as they also seek financial stability for the large-scale investments that is needed for the trans-Caspian gas pipeline. Although Turkmenistan and to a lesser extent Kazakhstan is lacking the capital needed to invest in the pipeline, they are not eager to endure price and volume risks since it is usual that producing countries would have to wait until the investors have earned back the investments they made before they can get their share. The higher the volume and price risks are, the higher the risk is that a delay will occur in which Turkmenistan and Kazakhstan can earn hard currency. Hence, it is expected that Kazakhstan and Turkmenistan will oppose a modification of the clauses in the traditional long-term contracts. From a practical point of view, according to analysts, the EU is facing a serious supply gap that will be complicated to fill (CIEP 2004). In addition to this, given the increased urgency of security of supply, again underlined in the 2009 Ukraine-Russia gas crisis (Reuters 2009), it would be more pragmatic from the EU’s point of view to create the best conditions for encouraging the development of new supplies (CIEP 2008). Moreover, since it can be expected that in the future the majority of gas will come from only a few large producer countries who are guided by long-term views and interests (CIEP 2008, pp. 19), the European Union might just not have another option than to comply with their interests. Hence, based on the analyses, it is believed that this particular (sub) factor will not play a substantial impeding role in the attempt to realize the TCGP and thus it is not taken into consideration.
5.5 Transit risk

Basically, there are 7 transit countries through which the natural gas from either Turkmenistan, Kazakhstan or both will flow before being connected to the Baumgarten in Austria and further on distributed to Central and West European markets. These are Turkmenistan, Azerbaijan, Georgia, Turkey, Bulgaria, Romania and Hungary. Although the abovementioned European transit countries are a part of a different gas pipeline project, namely the Nabucco gas pipeline, the latter is the only outlet for Trans-Caspian gas entailing a strong dependency. For that reason the Nabucco and the trans-Caspian gas pipeline should be viewed as one project with respect to this particular factor.

5.5.1 Transit countries’ reputation

The transit risk concerns holding up negotiations in the second attempt to realize the TCGP project. This will be assessed by looking at their reputation on holding up negotiations as a transit country. Moreover, the likelihood that a transit country may hold up negotiations will be assessed taking into account their interests and energy security objectives.

Technically, the first transit country that would be crossed is Turkmenistan, assuming that the trans-Caspian gas pipeline starts in Kazakhstan. If the former President was still in office, he would have casted doubt on Turkmenistan’s probable behavior as a transit country. However, the situation is different now, since the appointment of the new President Berdymukhamedov in the beginning of 2007. He has showed a remarkable willingness in comparison to the former President to cooperate with various international actors with regards to the energy sector. Moreover, the Kazakh gas crossing Turkmen soil would entail transit fees, meaning hard currency, which Turkmenistan badly needs. In addition, holding up negotiations would only mean a delay of the construction, meaning a delay of cash flow for Turkmenistan both in transit fees but more importantly for diversifying and increasing the export of their natural gas as it is regarded as a vital objective for Turkmenistan (see section 4.6.2). Hence, it is believed that if the TCGP will indeed start in Kazakhstan, Turkmenistan will pose no serious impediments to the second ongoing attempt by holding up negotiations about transit fees and/or other issues.

The second transit country that will be crossed is Azerbaijan. The only times that they have been part of a large-scale energy project was when they acted as the host country in the Baku-Supsa oil pipeline, the Baku-Novorossiysk oil pipeline and the South Caucasus gas pipeline. Hence, nothing can be said about their reputation, since they have never been involved in a large-scale energy project as a transit country. Nonetheless, it can be said that Azerbaijan has adopted a new role for itself in its energy policy. Azerbaijan is touting their potential as an energy conduit linking Central Asia and Europe. Aliyev, the President of Azerbaijan, made that pitch directly to European leaders at the World Economic Forum in Davos, Switzerland in late January of 2007 (Ismayilov 2007). Azerbaijan President Ilham Aliyev stepped up its ongoing campaign at an energy summit in Kyiv in May 2008 to promote Azerbaijan as the key to Europe’s energy security (Ismayilov 2008). This is in line with their main foreign policy and security objectives as Azerbaijan is endeavoring to join the European and Euro-Atlantic political, security and economic institutions. But this is a role in which Baku needs a supporting actor, namely Turkmenistan. The goodwill campaign that Azerbaijan has started towards Turkmenistan to improve their bilateral ties after President Niayzov’s passing should be viewed in this respect (see section 5.7.4). Taking into account these new developments, it
is believed that most likely Azerbaijan will not use its transit leverage to hold up negotiations about transit fees and other issues.

The third country to be crossed is Georgia. Georgia does have a record of holding up negotiations over transit fees and over the quantity and price of natural gas to be supplied by the crossing pipeline. This regards the Baku-Supsa oil pipeline, TCGP’s first attempt and the South Caucasus gas pipeline (Cutler 2003). However, it was not considered an impediment of importance during the first attempt and also the other energy projects, the BTC oil pipeline (Delay 2000) and the South Caucasus gas pipeline (Newsbase 2001) did proceed, albeit with a minor delay. On the one hand, Georgia has as with the other energy projects much to gain from this deal as it will provide much needed hard currency, but more importantly it will provide an additional source of gas supply safeguarding the country’s independence from Russia and strengthen its security and stability. Hence, although Georgia could somewhat delay the negotiations of the second attempt, it is not expected (considering its political, economic and energy security interests) that its actions will form a significant threat to the second attempt to realize the trans-Caspian gas pipeline.

The next country to be crossed is Turkey. Turkey is seeking –far more than in the first attempt- to become one of the main energy corridors for delivering gas to the European Union. Its role within this project has shifted from an essential offtake country in the first attempt to a transit conduit in the second attempt. Turkey views this project as a top priority enhancing their leverage with the European Union, strengthening its regional power status and a way to secure its gas supplies. However, as the negotiations on the Nabucco gas pipeline are proceeding, Turkey has come up with a demand perceived as non-negotiable by the European Union and the concerned member states. Turkey seeks to extract 15% from the Nabucco gas pipeline against relatively cheap prices, thereby implying that it should get an exceptional treatment due to its geographical location. Turkey’s desire to maximize its profits by suggesting an uncompromising pricing mechanism is proving to become a serious disagreement as it not only angers the importing countries but also Azerbaijan, the source (Templethorp 2008). Rationally speaking, Turkey will loose more than it can gain with this attitude underlining the presumption that they will most likely not go as far as allowing it to evolve into a serious threat.

The European markets that the Nabucco gas pipeline will cross are respectively Bulgaria, Romania and Hungary. With respect to Bulgaria, it can be said that it has been involved as a transit country in the Progress gas pipeline, through which the majority of Russian natural gas moves on to other markets such as Turkey. Though, it has not been found that Bulgaria has held up negotiations. The same can be said about Romania too, through which the Progress gas pipeline also passes. Nothing has been found about Romania holding up negotiations over transit fees or other issues. For both Bulgaria and Romania no historical indicators are found suggesting that it is likely that they will hold up negotiations in the future projects. Lastly, with respect to Hungary it needs to be said that they have never been involved in a large energy project acting as a transit country. Hence, nothing can be said about their reputation. Moreover, it needs to be asserted that these EU member countries consider the Nabucco gas pipeline as an important means to enhance their strategic role within the European Union and also as a source of income. This reinforces the presumption that they will most likely not hinder the Nabucco pipeline in a substantive manner.
5.6 Offtake market risk

In this section, the off-take market risk of each concerned country is assessed. This entails researching the risk that an off-take market would be unable to absorb the amount of gas supplied. Subsequently, every offtake country’s past is explored to find out whether it has used its position as a monopsonist power to renegotiate supply volumes or prices.

5.6.1 Offtake risk

First of all, it needs to be said with respect to the Nabucco pipeline and the markets it is serving that it will reach its maximum transmission volume of 31 bcm annually around 2020, taking into account the stepwise increase of the gas demand in the offtake markets en-route and the markets in Central and Western Europe. In other words, the increase in transmission volume of the Nabucco gas pipeline is adjusted to the increase in gas demand in these offtake markets over the years. In the first phase of the project in 2013 the pipeline will have a capacity of 8 bcm. The second phase will consist of installation of further compression stations at key points of the pipeline in order to continuously increase the pipeline capacity up to 31 bcm/y. Hence, the Nabucco gas pipeline project is one that must be regarded over the medium to long term. This should be taken into account when analyzing the offtake risk of the various countries. Furthermore, with regards to the Nabucco gas pipeline only the offtake markets that make up the physical part of this project will be considered. Hence, Central and Western European markets are left out of the analysis.

Azerbaijan’s gas demand is 10 to 11 bcm annually. Azerbaijan is regarded to be self-sufficient for a large part mainly as a result of the discovery of the giant Shah-Deniz gas field. The commercial production of this field and the delivery of gas started in December 2006 (BP 2006). For the remaining part Russian gas is imported. In the near future with the start of the second phase of the Shah-Deniz field in 2015, Azerbaijan is expected to become totally self-sufficient (EIA 2007). Hence, Azerbaijan’s role in the near future would be purely limited to the transit of the Turkmen and/or Kazakh natural gas from the trans-Caspian gas pipeline.

A large part of Georgia’s gas demand in 2007 has been met by Azerbaijani gas. The gas from Azerbaijan covered two-thirds of Georgia’s gas requirements in 2006, entailing approximately 1.1 billion cubic meters (Kramer 2006). For the remaining part Georgia received its gas from Russia. The lion’s share of Georgia’s gas demand will continue to be supplied by Azerbaijan, leaving a small portion of its demand that could be fed through the trans-Caspian gas pipeline, entailing a small and thus negligible offtake risk.

In the second attempt, the role of Turkey has changed drastically from being the primary offtake market to being one of the many offtake markets but primarily to being a main transit corridor, transiting the Kazakh and Turkmen gas onwards to the European markets. Hence, the aspect that induced Turkey’s offtake market risk as encountered in the first attempt has lost its most of its relevance in the second attempt. Moreover, Turkey’s gas demand is expected to grow to 56 bcm in 2015 and 66 bcm in 2020 up from 35 bcm in 2007 according to Botas’ adjusted forecasts (Reuters 2008). Therefore there is little doubt about that Turkey will be able to absorb the gas from the TCGP.

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58 Monopsonist means that it is the only buyer of in this case an energy source
Bulgaria has a relatively low demand of natural gas. However, plans have been made to gasify urban areas and to supply gas to the commercial and residential sector. In this respect, in August 2004 the Bulgarian natural gas company Overgas, Dor Gas Elran Infrastructures and Africa-Israel Investments signed an agreement to build a larger gas transportation network in Bulgaria. Construction on a main natural gas pipeline and smaller distribution pipelines to supply half of Central Bulgarian households will take approximately four years (Gegov 2002). It is expected that the natural gas demand will reach 8-9 bcm in 2010, with the prospect that it will steadily increase in the years thereafter (UNECE 2002). In addition to this, Bulgaria is not considered a virgin market as natural gas accounts for more than 13% of its energy supply (EC 2007). Hence, considering the steady growth in gas demand and the fact that the Nabucco gas pipeline will reach its maximum transmission volume around 2020, no off-take risk is expected from Bulgaria.

Romania has the highest natural gas demand and is the largest gas market of Central and Eastern Europe. From 2001 till now Romania has seen a slight but relatively constant increase in the demand for natural gas, which is supported by continuously high growth rates in GDP of between 4-6 % over the last few years and is expected to grow steadily in the coming years (Stephan 2001). Romania also is not considered a virgin market as natural gas accounts for more than 30% of its primary energy supply. In conclusion, no off-take risk is expected from Romania as the same line of reasoning asserted for Bulgaria also applies for this country.

In 2001, natural gas represented almost 41% of Hungary’s primary energy supply. In absolute terms this corresponds with 12.85 bcm (IEA 2003). In 2005 the gas consumption rose to 14 bcm and its gas market is expected to grow steadily (Shell 2006). The major drivers behind the growth are the increase usage of gas in the residential and commercial sectors. Considering the aforementioned and the gradual increase of the transmission volume of the Nabucco gas pipeline, it is not expected that Hungary will have trouble off taking the gas from the trans-Caspian gas pipeline in the medium to long term.

As for Austria, its energy consumption has been rising for decades. It is likely that this trend will continue in the next years. Its energy consumption grew approximately with 9.8% in the period from 2002 till 2005. Fossil energy sources contributed about 79% of total energy consumption in 2005 of which 18% was represented by natural gas (Umwelt 2006). No offtake risk is expected for the same reasons as underlined in the aforementioned European offtake countries.

5.6.2 A buyer’s weapon

The only noteworthy case is the one in which Turkey demanded a price revision and lower supplies with respect to Russian gas supplied through the Blue Stream gas pipeline using its monopsonist position. Gas deliveries to Turkey stopped in April 2003, less than a month after commercial supplies had started (Victor 2004). Turkey, which overestimated its future demands, was seeking to re-negotiate its agreement with Gazprom, insisting it could receive the gas at cheaper prices from suppliers such as Iran. In July 2003, Turkish and Russian officials, had reached an agreement behind closed doors, apparently keen to reach an out of court settlement. However, the conditions are different with respect to the TCGP since Turkey is not the only offtake market anymore as it was in the first phase. In this respect, the trans-Caspian gas pipeline will be connected to the Nabucco gas pipeline through which a number of Central, East and West European countries will be supplied. In conclusion, Turkey
in the second attempt does not have an absolute monopsonist position as a result of which the risk of the “buyer’s weapon” with Turkey as the buyer is reduced substantially.
5.7 Geopolitics

In this chapter, the development of the geopolitical (sub) factors identified in the first phase are researched in order to assess their impeding or contributing level in the second attempt. Also the driving forces behind the development of these factors will be determined in order to make a distinction between changing, constant and non-assignable sub factors, which will be determined in the third phase. In addition to this, the most defining events/developments influencing the course of the second attempt will be identified and assessed. Moreover, the potential change in the prioritization of energy security by the concerned actors over the time period taken in this dissertation and its potential effect on the actor’s strategic behaviour (energy policy) will be analyzed and determined. Furthermore, regarding Turkey it will be assessed how their role and influence has changed over the years within the context of the ‘New Great Game’. In this respect, also Turkey’s own domestic development and its influence on its foreign and energy policy will be determined. Lastly, the development of the role and influence of the relevant institutions identified in the first phase will be researched.

5.7.1 Developments in the ‘New Great Game’

In the second phase, two powerful actors have entered the ‘New Great Game’, namely China and the European Union, apart from the already active global and regional powers (Russia, USA, Turkey, and Iran), increasing the competition for Caspian hydrocarbon resources (natural gas) and its dynamic environment. In addition to this, the skyrocketing of energy prices (Mortished 2008) has increased it even further. The starting year of the second attempt is 2006 in which the EU experienced a harsh wake up call with respect to their vulnerability of being dependent on Russian gas (Stern 2006). Moreover, Turkmenistan witnessed an increased interest from the West when former President Niyazov unexpectedly died at the end of 2006.

An important event with global implications regards the terrorist attacks on 11 September 2001 on New York and Washington. This resulted into a military intervention of the U.S. and the NATO into Afghanistan. From this perspective, the new Central Asian states have aligned themselves economically, politically and militarily with diverse partners in an environment largely established by the contest of these powers (Ferguson 2005). In concrete terms, this means that the United States had gained access to the use of military bases in Kyrgyzstan and Uzbekistan to support military operations in Afghanistan (Tully 2005). As a counterbalancing effect, Russia reacted by establishing military bases in Tajikistan and Kyrgyzstan, evidently afraid of the U.S. overtures in Central Asia. Russia (and China) fears that the USA is determined to stimulate regime change parallel to the ones occurred in Ukraine, Georgia and Kyrgyzstan (Kimmage 2005).

When it comes to determining the influence of the ‘post-September 11’ events on the ‘New Great Game’, it is suffice to assert that it added an extra dimension to the struggle for influence in Central Asia. It provided the opportunity for the United States and the NATO to strengthen bilateral relations with the Central Asian countries, which particularly occurred in the military and security dimension with Uzbekistan, Tajikistan and Kyrgyzstan and Kazakhstan (Garcia 2003). Turkmenistan, on the other hand, mainly due to its isolationist behaviour during the rule of former President Niyazov, provided no incentives for the West to consolidate bilateral relations in the military and security field. All in all, the ‘post-September 11’ events have intensified and consolidated the struggle for influence in the Central Asian region in general of which the struggle for hydrocarbon resources is an integral part.
5.7.2 The evolution of energy security

When analyzing this section one has to take into account that the perspective of energy security depends upon one’s position in the value chain. In this section, the potential change/evolution in the prioritization of energy security by the concerned actors over the time period taken in this dissertation and its potential effect on the actor’s strategic behaviour (energy security policy) will be analyzed and determined. This change will be explained by distinguishing it into internal and external drivers. It will be done for the concerned actors insofar as the prioritization of energy security has actually evolved. This can provide an explanation for the change in the explanatory value of the factors over time endorsing the use of the constructivist approach.

Accordingly, the following sub research question will guide this analysis into the right direction:

How does the potential evolution in the prioritization of energy security by the concerned actors in the time period between 1997 till the present influences the ongoing second attempt to realize the trans-Caspian gas pipeline project?

The Republic of Turkey

An important internal driver that increased the urgency of security of supply in the second phase of the analysis is that the economy picked up steam and started growing again after the financial crisis in 2001. It has grown in average 7% a year for 6 years from 2002. Concretely, Turkey’s gas demand is expected to grow to 56 bcm in 2015 and 66 bcm in 2020 up from 35 bcm in 2007 according to Botas’ adjusted forecasts (Reuters 2008) explaining its need to secure future gas supplies.

Moreover, the external driver is Russia’s strategic behavior as it is not reluctant, to say the least, to use its position (‘gas weapon’) for coercing price revisions or the payment of debt obligations (for example the Ukraine gas cut-offs). In addition to this, Iran has not proven to be a very reliable supplier as the gas supply to Turkey was turned off in the winter of 2007 (Haber7 2007) and 2008(Zaman 2008). These developments have resulted into growing concerns about the security of its energy supply and increased understanding that the country’s economic growth needs to be protected from potential future gas cut offs whether it is politically driven or not. To this end, Turkey seeks for diversification of its gas supplies in order to reduce the risk that they will be out of gas.

In addition to this, Turkey’s position in the value chain is not limited to being an importing country but its geostrategic position grants it the opportunity to become a main artery for transiting natural gas from the Caspian region and the Middle East to the European markets. This has become more prevalent in the second phase, which as a result has shaped its energy policy.

The abovementioned drivers explain Turkey’s strong support for and participation in the Nabucco gas pipeline project perfectly. On the one hand it is a way to secure and diversify its gas supplies and to achieve its objective to become one of the main arteries for delivering natural gas to the EU, while on the other hand it is a way to significantly increase its (geo)strategic importance both for the Caspian region but more importantly vis-à-vis the European Union.

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60 The meaning of energy security for a transit country is to secure an uninterrupted flow
The European Union

Internally, steadily rising energy prices, decreasing European gas production and increasing gas demand have contributed to concerns about the European Union’s ability to meet future gas demand. Externally, concerns about the global climate change, the threat of terrorist strikes against energy infrastructure and last but most definitely not least Russia’s apparent willingness to use its energy power for political ends has compelled the EU to prioritize how to address external influences that may effect future energy requirements (Gennip 2006). Moreover, its concerns about its energy security culminated in 2006 following the Russia-Ukraine gas dispute (Stern 2006).

These actualities have put energy security on the forefront of the EU agenda shaping its energy policy. It has put the emphasis on diversifying its gas sources among other things in order to secure supply. It has recognized the Caspian region as vital for the diversification of its gas supplies (EU 2000). This has translated itself into the strong support for the realization of the Nabucco gas pipeline project and also the trans-Caspian gas pipeline project. Moreover, in the light of its energy policy it has agreed to expand political partnerships with and increasing pipeline and energy infrastructure investment in producer and transit countries situated in the Caspian region and Central Asia. In this respect, members of the European Commission have made numerous visits to Turkmenistan to stress the significance of its participation and to obtain a concrete commitment with regards to the TCGP (see section 5.7.4).

The Republic of China

Energy security for China found its meaning and importance in the second phase under the growing concerns about securing their energy supply as a result of the growing need for foreign sources. China has come to view the necessity to protect its economic growth and the security of its energy supply as a top priority. In addition, China has prioritized to expand the use of natural gas in its energy strategy as access to Caspian gas is an increasingly important element in achieving that aim. This is done by means of a resolute but subtle foreign (political dimension) and energy security policy (economic dimension) (IEA 2000), which have become more intertwined which as a result of the growing concerns of energy have become more intertwined.

It has influenced the second attempt to realize the TCGP in the sense that an additional competitor has entered the “New Great Game”. It is not a competitor that can be ignored very easily as it possesses substantial economic power while at the same time it is a consumer country with vital energy security interests. In addition, it is geographically advantageous since it borders the Central Asian countries. Its competitive strength will become apparent if rivalry erupts over gas fields in the Caspian region. To this end, they are prepared to bear the entire costs for the realization of energy pipeline projects originating from the Caspian region, making it a formidable competitor to be reckoned with and a potential impediment to the TCGP project.

The Russian federation

An internal driver that increased the urgency of energy security for Russia and which made it an integral part of its foreign policy was without any doubt the election of Vladimir Putin as president in the year 2000. Securing and raising demand and revenues came to the forefront of the Russian agenda, but this time it was part of a bigger objective as Putin saw the opportunity to restore Russia’s regional and then global power status by means of the one
natural resource that it has in abundance, namely natural gas. Hence, it has come to view energy security as a top priority not only in order to sustain and protect its economic growth but also to safeguard their only means to restore its hegemony in the region and then in the world. It is seeking to secure its demand and revenues by means of a proactive and aggressive foreign policy.

An external driver is no doubt the increasing demand for gas from the European Union, its largest and most profitable market. Furthermore, the engagement of the West (EU and in particular the USA) into Russia’s near-abroad also played a role, which is seen as a threat to its energy security and thus its objective to restore its supremacy in the region. Moreover, it is believed that instead of relying on significant foreign investment in its energy infrastructure, Russia is seeking to satisfy its long-term gas contracts with the EU member states through its near monopoly on importing and transiting gas from Central Asia (Makarychev 2006) (Kazakhstan, Turkmenistan and Uzbekistan). In other words, the Caspian region has developed into a region with substantial (geo)strategic importance as the Central Asian gas supplies enables them to postpone large investments in their own energy infrastructure. In this respect, it seeks to re-integrate the Caspian region into its energy system. The gas supply from the Caspian region has become an important means to secure and raise its revenues and demand. This explains that it views the Western energy interests in the Caspian region as a threat.

Having mentioned the drivers, it is no surprise that Russia firmly opposes any pipeline project that is headed to the West and bypasses its soil. Its economic power, defined as its near monopoly as an outlet for gas from the Caspian region and its extensive trade relations, supplemented with its substantial historical and linguistic ties with the Caspian region as well as its restored confidence as a regional power makes it a strong competitor in the ‘New Great Game’.

The Islamic republic of Iran

Energy security as such has always been a priority for Iran as it sits on one of the largest oil reserves and as it is one of the largest exporters of oil (EIA 2006). But the level of prioritization of natural gas within their energy policy has undergone a significant transformation.

The internal drivers for the change in how Iran has come to view energy security with respect to natural gas is the government’s 20-year strategic plan to increase gas production substantially (Gould 2008) given the increasing internal gas demand (7% annually) and the aspirations to improve regional ties by exporting gas. It views gas pipelines as an extension of its regional strategy and thus a strategic element in regional relations (Khanjehpour 2009). Iran has come to view energy security as a priority.

The external drivers are the growing importance of natural gas, hence the increase in gas demand from the EU and China, and the growing security of supply concerns. Its influence on the TCGP is multidimensional as it entails a conflict of interests; on the one hand it is considered a potential supplier to the Nabucco gas pipeline project, which the project badly needs considering that there are growing concerns about finding sufficient sources of supply (see section 5.8). Therefore, the participation of Iran may become crucial to implement the Nabucco and thus also influence the realization of the TCGP. But on the other hand, Iran still opposes the trans-Caspian gas pipeline. Nevertheless, Iran’s role in the Nabucco project will be known in the short term taking into account the presidential elections

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61 Russia has the largest gas reserves in the world,
in Iran in June 2009 (Dahl 2008), which will determine the course of Iran’s nuclear stand-off.62

**The Republic of Kazakhstan**

The internal driver is Kazakhstan’s growing demand for natural gas. Above all, the external drivers explaining Kazakhstan’s objective to become a net exporter of natural gas of 60-80 bcm annually by 2015 are the growing share of natural gas in the primary energy supply of the EU and China and their increasing security of supply concerns. This has led to a proactive and multi-dimensional foreign and energy policy seeking to find outlets for their gas, which explains their interest in joining the trans-Caspian gas pipeline project and its emergence as a potential host country in the second phase.

### 5.7.3 Turkey’s efforts to reclaim its (geo)strategic importance (2)

As previously stated, Turkey’s role in the ongoing second attempt is revised as now they are no longer considered the main offtaker for the Turkmen and/or Kazakh gas, but a corridor for transiting Caspian natural gas to the European markets. This is also stated as one of the pillars of Turkey’s energy strategy; to become an energy corridor funnelling oil and predominantly gas from the energy rich countries in the Caspian region, Central Asia and the Middle East regions to the European markets. Turkey has the desire to become the fourth main artery of Europe’s gas supply security after Russia, Algeria and Norway (Roberts 2004), which is considered an effective means to regain its (geo)strategic importance. Turkey’s newfound energy strategy followed the EU’s publication of the Green Paper on Energy Security on November 2000 (EU 2000). In the paper the emphasis is put on an uninterrupted flow of gas by means of secure and diversified energy supplies as Turkey is recognized as geographically advantageous to become a natural corridor for energy supplies from the energy rich regions.

In this section, the following sub research questions will be treated:

**How has the role and influence of Turkey developed over time from 2001 till now regarding the struggle for Caspian gas in the ‘New Great Game’?**

**How has the relations between Turkey and the involved actors changed and how has that impacted their role and influence in the Caspian region?**

**Turkey’s economic and political development**

Try to imagine an economy with an ever-rising domestic debt and record level interest rates, a high and constant inflation, an extremely weak banking sector, political instability and geographical location with constant turmoil in neighbouring countries. This reached its peak in 2000, resulting in a financial crisis (Özatay 2002). These developments had severely hurt the foreign and domestic economic circles’ confidence in Turkey’s authorities, leaving the in November 2001 elected AK party (Justice and Development party) with a daunting task to turn around the odds. However, against all the odds, facing serious difficulties, the AKP displayed strong determination to carry out the political and economic reforms to stabilize its economy and to start the EU accession process. The AKP enthusiastically worked to implement the National Programme drawn up by the previous government in 2001. The Programme required Turkey to comply with EU’s Copenhagen Criteria, namely, the rule of

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62 This is the primary reason that the EU is against Iran’s participation in the Nabucco project in the first place.
law, respect for human rights and advocacy of a free market economy. Major packages of reforms were passed through parliament in an effort to bring the present legal system in line with the EU policy. This resulted in the start of the EU accession negotiations in October 2005. From that point on, the road to full membership have been one with many bumps and hurdles. Furthermore, thanks to the Economic stability program, AKP’s efforts and an appropriate global economic climate, the Turkish economy achieved big progress between 2002 and 2007. Besides strong economic growth, averaging at around 7% per year, big advancements have been made to solve chronic economic problems like high borrowing costs and big budget deficit. Also high volatility of financial markets and currency fluctuations have been resolved accordingly and consequently economic stability was provided. These developments had a positive influence on Turkey’s ties with the concerned actors in the ‘New Great Game’. The substantially grown economic and political relations with Russia need particular attention. Nevertheless, Turkey still has a volatile political and domestic stability underlined by the domestic events aimed at overthrowing the AKP government (CNNTürk 2008).

All in all, throughout the years from 2002 onwards Turkey has recovered its self-confidence and is endeavouring a more assertive foreign policy strategy as to play an important role in the region and in the world. This is expressed in playing a mediator role between Syria and Israel (Zaman 2008). Moreover, Turkey was one of the main contributors to convincing Hamas to acquiesce to a cease-fire in the war with Israel (Zaman 2009), it was the initiator of the Caucasus Stability platform (Kanbolat 2008) and its admittance to the Security Council of the United Nations for the period of 2009-2010 (Hürriyet 2008).

**Turkey’s maturing foreign policy**

After the failure of the “Turkic World” model in the first half of the nineties, Turkey turned into itself in the second half, which emerged as years of loss in the country’s foreign policy. Central Asia, a meaningful zone of security in the minds of Turkish foreign policy makers ended up as a region getting farther from Turkey. In addition, the economic crises in the country in the 1990s and in 2001 prevented Turkey from deepening its economic ties in the region. From the end of the second half of the nineties, though, both the rhetoric and practices in Turkish foreign policy have changed and as a result a self-confident, proactive, dynamic and multi-dimensional (well balanced) foreign policy line emerged. The new Turkish foreign policy line can be viewed in a wide framework of following balanced relations with regional countries like Russia, Iran, Pakistan, India and China and maintaining good relations with the U.S. and the European Union.

**The new foreign policy towards Central Asia**

As Turkey is making progression on the EU road to full membership, its ties with other regions gain strategic depth and influence. While moving towards the West, it is creating a sphere of influence in the East. Turkey has started to follow a foreign policy that validates regional and international legitimacy and aims to reconcile ethical principles with strategic interests (Aras 2008). In this respect, Turkey maintains good relations with regional and international actors in order to gain strategic depth in Central Asia through bilateral relations with the countries in the region. It is also attempting to become a key political and economic partner in the region. Within the context of its new foreign policy, Turkey views the Caspian region and Central Asia as a potential sphere of influence in which it seeks an active role.
Within the context of Turkey’s new foreign policy, Abdullah Gül, the newly appointed President of Turkey in 2008\(^{63}\), has paid high level visits to the Turkic countries. Although the intention of the visits was good, the question remains, however, whether these Presidential visits are sufficient to bring the economic, political and strategic relations to the ‘desired’ level in accordance with their foreign policy objectives. In this respect, the executive power is not in the hands of the President of Turkey, but in the hands of the Prime minister and its Cabinet. The President’s influence is such that it can only suggest the government to reinforce bilateral relations with these countries. These symbolic visits are a show of goodwill, but if it is not substantially backed by the executive government these visits will loose its momentum. Furthermore, Iran’s systematic natural gas cuts in the winter periods, as in the winter of 2007 and 2008, have triggered Turkey to take an active role in getting Turkmen gas to Turkey. In this respect, turkey announced that if necessary it is willing to play a mediator role to help solve a deep-seated dispute between Azerbaijan and Turkmenistan on the status of the Caspian Sea (Sariibrahimoglu 2008). Turkmenistan and Azerbaijan has welcomed the proposal.

The share of energy security in its new foreign policy

On the one hand, there are the increasing concerns about energy security, while on the other there has been a review of how it can increase its (geo)strategic importance; to become an energy corridor funneling oil and predominantly gas from the energy rich countries in the Caspian region, Central Asia and the Middle East to the European markets. This also explains the change in the explanatory value of the Turkey related (sub) factors as in this phase, on top of that it is the only viable route for the trans-Caspian gas pipeline project, they also function as the vital link to secure the European Union’s energy supply via the Nabucco project (see section 5.8 for the interdependency between the Nabucco and the TCGP project). Considering the aforementioned, Turkey’s energy policy has been inextricably connected to and makes up a big share of its foreign policy especially with regards to the energy rich Caspian region, Central Asia and the European Union.

All in all, Turkey has set its eyes on the Central Asian region once again. Though this time, pragmatism and rationalism prevails in its foreign policy over shared ethnic and linguistic ties. However, Presidential visits are not sufficient to improve bilateral relations in a substantial manner considering Turkey’s objective to become a key economic and political partner in the region. Nevertheless, its unique ties with the Turkic countries combined with its increasing economic clout, its growing regional influence and international prestige and the improving relations with the West do provide Turkey with an opportunity to become a key player in the Central Asian region.

Post-September 11 period and its influence on Turkey’s role and influence in the Caspian region

The post-September 11 developments have consolidated Turkey’s strategic importance and thus has helped to reshape its relations with the EU and the USA, as well as with the countries in its neighbourhood (Bagci 2003). In this respect, from a practical point of view, only the extent of the influence that these events had on Turkey’s role in the Central Asian region will be discussed further.

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63 Gül was the former Minister of Foreign affairs, known for his outstanding efforts in Turkey’s EU accession bid and reinforcing bilateral ties with the Turkic countries
The war with the Taliban in Afghanistan and on terrorism brought the Central Asian region and the Caucasus once again into the locus of interest. Most countries in the region are ruled by former communist leaders in an authoritarian manner, but they were under pressure from domestic opposition. Since, this opposition was mixed with some elements of Islamic radicalism, particularly in the case of Uzbekistan, they became proactive supporters of the international coalition against the Taliban and al-Qaeda. Moreover, allowing the United States in their region was also seen as a good chance to balance Russian dominance by assuring American backing. The United States did not counter any opposition from these countries and gained access to air space and military bases in Uzbekistan and Kyrgyzstan (Kimmage 2005). In developing U.S. relationship with the Central Asian region, Turkey’s special ties with the region again appeared to be an important asset for U.S. foreign policy. Turkey had a lot to offer; not only did Turkey have strong political, cultural and economic connections to the region, but it had also accumulated a significant intelligence capability in the region. Besides that, Turkey’s experience in fighting terrorism would be made available in expanding the global war on terrorism in this region. In sum, it was thought that, due to its geographical position allowing easy access to the region and its strong ties with the countries there, Turkey could play a pivotal role in the conduct of U.S. military operations in Afghanistan and reshaping the politics in Central Asia. Hence, Turkey strongly believed that it had acquired a new opportunity to enhance its influence in Central Asia and to regain its (geo)strategic importance and acted accordingly (Aras 2001).

In the first half of the nineties, Turkey was presented as a model for the economic, social and political transformation of the Central Asian countries. This time, however, the role expected from Turkey was limited to the military and strategic field. Turkey’s role was limited to playing a mere “subcontractor” role in the region and thus facilitates the U.S. presence in that region in the light of the global war on terror. For that reason, Turkey’s ambitions and manoeuvrability space are very much limited by international interests in the region. Moreover, a policy based solely on limited military contribution would not be successful as long as the economic dimension is lacking. It is destined to remain temporary and once the conditions have altered and the region returns to normal, the underlying realities might resurface and this policy might leave Turkey at a disadvantaged position in political and economic terms (Bagci 2003). Furthermore, the post-September 11 developments provided Turkey also with an impetus to increased engagement with the Caucasus region. This resulted into increased military cooperation with Georgia (TDN 2005), especially after the U.S. decision to establish military presence in this Caucasian country.

All in all, the post-September 11 events left Turkey with a hangover, overestimating the potential influence of their newfound role in the Central Asian region. As the immediate threat of international terrorism is gradually decreasing, Turkey’s actual influence in the Central Asian states as a result of the September 11 events can be assessed as minimal at most. Moreover, the U.S. military establishment in Georgia gave the BTC oil pipeline and the South Caucasus gas pipeline project a new chance as it increased the security of these projects in the volatile Caucasus region (TDN 2002). The most noteworthy event that followed the September 11 attacks was that the U.S. threw its weight behind Turkey in supporting the construction of the BTC oil pipeline (Babali 2005). This intensified U.S. support changed it in favour of Turkey. In short, although the post-September 11 terrorist events did not provide Turkey with structural influence in the Central Asian region which it so much hoped for, it did, however, have a positive effect on the realization of the BTC oil pipeline and the South Caucasus gas pipeline project.
Developing Russia-Turkey relations

The development in their relations mainly occurred in the economic field. Where in 2004 the trade relations were worth $11 billion, in 2007 this has reached $38 billion. In addition, Turkish investment in Russia surpassed $6 billion, while Russian investment in Turkey amounted to $4 billion (Ogan 2009). Moreover, approximately 3 million Russian people visited Turkey in 2008. Its relations have also been developing in the political and diplomatic field as Turkey’s President has been received on the occasion of a ‘state’ visit instead upgraded from an ‘official’ visit, indicating the value that Russia ascribes to their mutual relations (Ogan 2009). In addition, there have been recent developments underlining the increasing mutual trust. Whereas Russia in the nineties viewed Turkey as a potential threat to its domestic stability due to its pan-Turkism stance, the relations have developed to such an extent that Russia does not view Turkey’s desire to develop relations with Tatarstan (Niyazbayev 2009) and other by ethnic Turkic people inhibited federations within Russia with suspicion any more.

When it comes to analyzing the impact of these developing relations on Turkey’s influence in the Caspian region, one has to conclude that for the time being this is limited, which is partly explained by Turkey’s own ‘passive’ foreign policy towards this region (see previous section on its foreign policy). Nevertheless, the developing Russia-Turkey relations ought to be taken into account in the third phase when constructing the future worlds. It may eventually lead to a change in Russia’s current perception about Turkey as a geopolitical rival in the ‘New Great Game’.

Turkey returns to the energy chess game (Turkey – Iran relations)

Turkey made an important move in the ‘New Great Game’ when it signed a Memorandum of Understanding (MoU) with Iran in July 2007 that could make both Russia and the USA rethink their energy policies (Sariibrahimoglu 2007). The objective of this section is to find out what the effect of Turkey’s strategic behaviour may be on the second attempt to realize the trans-Caspian gas pipeline.

In Ankara on July 14, 2007, Iran's visiting Minister of Petroleum Seyyed Kazem Vaziri-Hamaneh and Turkish Energy and Natural Resources Minister Hilmi Güler signed a gas deal, agreeing on Iranian gas export to Europe via Turkey and Turkmen gas export to Europe via Iran. Both countries also agreed to develop the giant South Pars gas field in the Persian Gulf on a buyback basis (Sariibrahimoglu 2007). This move is faced with strong opposition by the United States.

The United States strongly urged Turkey to cancel the deal with Iran, reminding Turkey of the existing sanctions against Iran (Kreyenbühl 2007). Under the Iran sanctions act, the U.S.A. can impose sanctions to international firms doing business with the oil and gas sector of Iran. Turkey’s stance on this issue is that it will continue with this energy deal, since Iran is an important supplier of natural gas for Turkey and vital for Turkey’s energy security (Sariibrahimoglu 2008). This move of Turkey should also be viewed from the standpoint that it is endeavouuring to increase its (geo)strategic importance provided that the gas is send to the European markets. In addition, it also considers this gas deal as a good opportunity to reinforce relations with a vital neighbour. However, according to Necdet Pamir64, a renowned energy expert in Turkey, the Iranian side put forth unreasonable conditions; it will sell the gas to Turkey at international prices and Iran demands to be the operator of the gas fields despite

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64 (Interview with author, Ankara, 29-10-2008)
the fact that Turkey is the investor. This and other investment terms have delayed the finalization of the gas deal between the two countries (Uslu 2008).

A possible implementation of this gas deal with Iran would make the trans-Caspian gas pipeline project redundant. A precondition, however, to the realization of this Turkmen-Iran-Turkey gas pipeline is that the European Union must accept Iranian gas as a potential source to supply the Nabucco gas pipeline. However, this does not seem very likely in the short term considering Iran’s nuclear stand-off (Khanjehpour 2009).

There have even been claims that the recent deal that Turkey made with Iran may be a bargaining chip to persuade the U.S. authorities to ensure the completion of the Iraqi natural gas project. Indeed not long after signing a Memorandum of Understanding in November 2008, the Turkish Petroleum Corporation (TPAO), the state-owned Turkish Pipeline Corporation (BOTAS) and Shell Energy Europe B.V. signed a preliminary contract to explore, manage, transport and market natural gas in Iraq after the United States pressured the Iraqi authorities to include Turkey in exploring Iraqi oil and gas reserves (Zaman 2008).

In conclusion, the effect of Turkey’s gas deal with Iran on the attempt to realize the trans-Caspian gas pipeline project has been non existent. The one positive development that it brought forth so far are some concrete steps to realize the Iraqi natural gas project with the aim of forwarding it to Turkey. However, the much needed stability in Iraq is a far fetched concept, strongly impeding the realization of any pipeline project in that country. It is believed that considering the strong US pressure on the one hand, the importance that is ascribed to the strategic partnership with the U.S. and unrealistic demands from Iran to Turkey on the other, the likelihood that Turkey will go through with their gas deal with Iran is low.

**Profit maximization at the cost of Nabucco?**

Turkey’s desire to regain its (geo)strategic importance by becoming one of the main arteries for delivering gas to the EU might be in danger. It has put forth a demand that may prove to be a serious bottleneck for the realization of the Nabucco gas pipeline project. Turkey is determined to extract cheap gas from the Nabucco pipeline, demanding a preferential treatment over the other actors involved in the project. This view is strongly rejected by not only the EU but also angered Azerbaijan, which is one of the sources, who has already been looking northwards to Russia as an alternative outlet (VOA 2009). As a result, Turkey is entangled in a dispute with the 27-nation bloc over the pricing mechanism and its role in the multinational natural gas project. Turkey is taking a rigid stance on this issue as so it seems.

It is believed that Turkey’s ambitions of maximizing profits from energy pipelines might overshadow its aspirations of becoming a gas artery. The attitude that Turkey is entitled to get a premium, just because the oil and gas go via turkey, is not justifiable. As a consequence Turkey is gaining enemies for a small amount of money. The expectation that the rest of the actors in this multinational project will accept this condition without strong objection is naïve and counterproductive. To think that every transit country, like Georgia, Bulgaria, Romania and Hungary, would want exactly the same thing with exactly the same justification is no less than rational.
The structure of Turkey’s (T)NOC’s and its implications

In the eighties, Turkey needed to fragment its state oil firm as a result of a series of demands of the World Bank (Turkce 2007). This was a huge drawback especially in the nineties with the dissolution of the Soviet Union and new republics were created in Central Asia and the Caucasus. Turkey with their disintegrated structure of their energy corporations was unprepared for this as a result of which it was not able to exert more leverage towards this region in general and in the first attempt to realize the TCGP. A vertical integration of its national energy corporations, meaning a merger between TPAO, the state-run Turkish petroleum corporation, and BOTAS, the state-run petroleum pipeline corporation, will bring about an opportunity for Turkey in the form of a strong player with substantial economic power and know how about the entire supply chain (exploration, production, refinery, transportation, distribution and marketing) in order to gain a greater foothold in the ‘New Great Game’. According to Necdet Pamir, a renowned energy expert in Turkey, Turkey misses this powerful instrument to gain more ground in the struggle for the Caspian hydrocarbon resources in the ‘New Great Game’.

5.7.4 The actors’ development and its implications in the “New Great Game”

In this section, the new states’ as well as the traditional states’ (who were involved in the first attempt) position and influence within the “New Great Game” will be researched to the extent that its influence has changed considerably making it relevant for the ongoing second attempt to realize the TCGP.

*What are the main alterations to the explanatory factors taking into account their development over time from the first attempt till now and to which extent do they contribute to the advancement or impediment of the ongoing second attempt to realize the TCGP?*

*Are there any new (sub) factors that have emerged in the second phase and what is their influence on the ongoing second attempt to the extent that it is possible to determine it in this stadium?*

The implications of EU’s entrance to the “New Great Game”

Ideational structure

One of the European Union’s basic foundations and its raison d’être entails the liberalisation of markets (competition) and in essence the concept of free trade within the borders of the EU. Therefore the EU believes that any project should be commercially viable, which in turn influences her actions. As a result, the EU has an aversion to making ‘political investments’, which has the potential to harm the attempt to realize the TCGP and the Nabucco project (see section 5.8).

The European Union, its member states and the Central Asian region

EU strategy towards Central Asia has until 2007 remained in the shadows of the US and major TNOCs policies. As a result, US policy in the region has often mistakenly been perceived as a common Western strategy. This is partly due to the fact that the member

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65 Besides the increase in capital as a direct influence of vertical integration (increase in revenue), it is also believed that such a vertically integrated firm is able to create a greater amount of funds in the international market than the energy corporations in the current structure.
66 (Interview with author, Ankara, 29-10-2008)
countries of the EU each have different priorities (Aminne 2003). France is traditionally more oriented towards North-Africa, Germany towards Eastern Europe and Britain towards the Baltic states. Individual member states’ interests have been the main stimulus to enter into cooperation with the Central Asian countries. The lack of a coherent EU strategy on Central Asia had prevented the European Union to develop a strong influence in the region. Nevertheless, this has changed due to a disturbing wake-up call.

A disturbing wake-up call

An event of significant meaning is the rude awakening the Russia-Ukraine gas dispute in 2006 had caused within the European Union (Stern 2006). A dispute over gas prices had exposed the European Union’s energy security vulnerability catapulting concerns over security of supply to the forefront of the EU agenda. Above all, this crisis raised the questioning of Russia as a reliable supplier and Moscow’s willingness to use its energy power as a political weapon. Thus in March 2007, in the face of increasing concern about Europe’s reliance on Russian gas and growing public pressure to address global climate change, EU member states agreed to forge an “Energy Policy for Europe” (Belkin 2007). To this end, EU member states have agreed to cooperate to form an external energy policy centered on expanding political partnerships with and increasing pipeline and energy infrastructure investment in producer and transit countries. The EU member states have specifically selected Central Asia, the Caspian and Black Sea areas as focal points for such activities as these regions have the strong potential to contribute to the diversification of oil and gas supplies to the European Union. In this respect, the EU has funded a feasibility study to investigate the economic, technical and environmental feasibility of a trans-Caspian gas pipeline. Preliminary results were planned to be published at the end of 2007, however, no results have been published as yet. At the same time, however, the European Union is cautious about entering into anti-Russian alliances in the Central Asian region. To the contrary, it is of the opinion that interests will only be able to be pursued in the region through close cooperation and partnership with Russia (Belkin 2007). In addition, it is promoting the TCGP, not as a competitor to Russian pipeline projects but as a complementary project attempting to ease the geopolitical rivalry and increase its chances of realization.

The growing concerns about security of supply have triggered the EU to become more assertive and proactive as a union to secure its supply explaining its entrance into the ‘New Great Game’ and the change in its explanatory value as a (sub) factor influencing the ongoing second attempt to realize the trans-Caspian gas pipeline project. This is a good example of how the constructivist approach is used in this dissertation.

EU-Turkmen gas agreement promising?

An auspicious agreement was reached during the talks held between EU officials and President Berdymukhammedov on April 9-10 in the Turkmen capital Ashgabat. Turkmenistan has confirmed that it will directly supply the European Union with 10 billion cubic metres annually by 2009 (Berdyeva 2008). This gas would have to come from the gas fields that are already in operation and not from the alleged huge gas fields in south east Turkmenistan. Although a relatively minor commitment, it is a very important first step, which may lead to a major revision of the Caspian Basin energy equation, breaking Russia’s dominance of export routes. It might very well turn out to be a building block for greater energy cooperation between the EU and Turkmenistan. In addition, although it would only be enough to fill one-third of the Nabucco pipeline’s projected capacity, it could still be enough to get the project off the ground. However, how the gas will be transported to the EU countries remains to be
worked out\textsuperscript{67}. In the end, however, these and other uncertainties remain making the commitment dubious to say the least such as whether the Turkmen President will follow through with this deal (Turkmenistan’s credibility issue).

**EU’s Central Asia strategy reviewed concisely**

In spite of the danger of inaction, many countries in the EU are indecisive about engaging in energy deals with Turkmenistan and Kazakhstan due to the reason that they have a poor record on human rights or rule of law. The sheer reluctance of the EU to incorporate their energy sector when engaging with the Central Asian region comes with a price. The EU therefore lacks the means (material power) to exert proper leverage to encourage these states to change (Belkin 2007). The perception of the EU is of such a nature that they are viewed as reprimanding its neighbours, calling for too much political and social reform without offering much in return. The Central Asian states are aware that untimely implementation of political reforms without the necessary improvements in economic, political and physical infrastructure, the governmental control would collapse leaving behind a region susceptible for terrorism, extremism and drug trafficking.

Moreover, although the EU is not willing to make investments without seeing substantial political and economic reforms in Central Asia, this does not bother China and Russia whatsoever. Brussels says it will not underwrite the investments, insisting on the fact that the projects must be commercially viable. Many analysts have warned that the EU’s aversion of “political investments” makes its strategic interests vulnerable to meddling by Russia and China (see next section). Especially given the long time frame associated with oil and gas projects, Russia and also China would be able to lock the states of the region with a single substantial commercial victory, leaving the West with severely limited options with which to press reforms.

Furthermore, although the rude wake-up call did start a discussion about ceding national sovereignty to EU institutions in the field of energy policy, the EU member states remain reluctant to hand it over and it remains primarily the responsibility of the member states. Decisions concerning long-term oil or gas purchases, the development and improvement of energy-related infrastructure and the use of particular fuels continue to be made at the national level by individual member states, seriously undercutting the EU’s chances to play a more influential role in the region.

All things considered, the European Union as an institution has a long way to go before it can be viewed as a player with substantial influence equal to Russia, China and the USA in the ‘New Great Game’. Nevertheless, it does have a great opportunity in its hands as strong financial support for the Nabucco project will increase the chances of the ongoing second attempt to realize the trans-Caspian gas pipeline project (see section 5.8).

**The implications of China’s entrance to the “New Great Game”**

**China and the Central Asian region**

China’s policy towards the CA region is based upon two guiding principals (Amineh 2003): to safeguard stability at home against outside threats i.e. Islamic radical movements that could stir up the Turkic-Muslim Uighur population in the strategically important Xinjiang region\textsuperscript{68} and of more relevance to this dissertation to satisfy partly its growing oil and gas

\textsuperscript{67} There are 3 possible routes; two of which involves construction of a pipeline across the Caspian Sea and the other involves liquefaction of the gas and shipping it aboard tankers across the sea. Turkmen officials have remained silent on this issue.

\textsuperscript{68} It contains vast amounts of oil and gas reserves.
demand with imports from the CA region. Within the context of its energy security strategy, China has politically mandated its national oil corporations to acquire security of supply at whatever cost (Wälde 2008).

Just a decade ago China played almost no role in the Central Asian region. However, its strategy towards this region changed dramatically, induced mainly by the booming growth in their economy and thus the increasing need for energy supplies (security of supply). Since then China has been tirelessly nurturing its ties with the Central Asian region. In the 1990’s, China had relatively little trade with Kazakhstan, Central Asia’s economic engine. But by 2006, China ranked third behind Germany and Russia in Kazakhstan’s $35.6 billion export market and second after Russia in the nation's $22 billion import market (Birch 2007).

Beijing, in contrary to Russia and USA, is playing a subtler game. It is a customer, not a competitor for Central Asia’s natural resources. China is implementing a successful strategy by using “soft power” - judiciously apportioned aid, aggressive diplomacy and massive investments – to shove Russia aside from being the most influential player in the region.

Chinese state companies have poured in piles of money into Kazakhstan to help built the pipelines that are or will bring oil and gas to the country to help drive the country's economic growth, indicating China’s determination to attain access to Central Asia’s natural resources. Illustrative to this is the $700 million oil pipeline in December 2005 linking Atasu in central Kazakhstan to Alashankou on the Chinese border. In addition, China and Kazakhstan on 8 November 2007, signed an agreement in Astana outlining the principles for building and operating the China-Kazakhstan natural gas pipeline (Xinhua 2007). Also noteworthy is the signing of two key gas deals by the new Turkmen president Berdymukhammedov on 17 July 2007 during a two day visit to China, which might help him realize his aim of diversifying Turkmenistan’s gas export options (GI 2007). The pipeline, roughly 7000 km in length (2000 km to the Chinese border) will cross the territory of Uzbekistan and Kazakhstan and is destined to deliver of up to 40 bcm of natural gas per year for a period of 30 years to Kazakhstan and the Chinese markets (Reuters 2008). The gas pipeline’s costs are estimated at $14 billion (Gould 2008). However, China’s growing economy is devouring energy at such a rate that Beijing is keen to get access to Turkmen gas. This is best expressed in their willingness to finance the entire project from exploration and production to the pipeline construction and transportation saving no expense.

China’s aggressive pursuit for foreign energy resources is an illustrative example of how its explanatory value has changed over the years due to its growing concerns about energy security (constructivist approach). In the nineties, China did not play any role of importance in the ‘New Great Game’ in the Caspian region. It made up leeway in the 21st century and became a formidable competitor in the second phase. The driving force behind it is that China has come to view the necessity to protect its economic growth and the security of its energy supply as a top priority. China has come to view energy security as an integral part of its national interests, namely to survive and be secure as a nation.

**China: a threat to the TCGP?**

China is considered a threat to the trans-Caspian gas pipeline project to the extent that it is vying for the same gas reserves. China’s national petroleum corporation has received a mandate from the Turkmen government to explore and extract for gas reserves on the right bank of the Amu Darya river (see figure 4) in the far east of Turkmenistan as the source for the Turkmenistan-China gas pipeline would have to come from this area (Gould 2008). Having mentioned that, the source for the TCGP is not supposed to come from the same area. Instead Turkmenistan’s offshore section or the allegedly large onshore gas reserves in south-
east Turkmenistan (such as Yoloten and Osman gas fields) are depicted as potential sources of gas supply for the TCGP.

All in all, China has developed into a formidable player in the ‘New Great Game’ as such that it is has gained an influential position both in economic and political terms. Moreover, China is not a threat for the TCGP as long as the sources to fill these pipelines originate from different gas fields. Nonetheless, China needs to be reckoned with in the ‘New Great Game’, since they are an end consumer and are neither sceptical about the commercial viability of the pipeline nor are concerned with the poor human rights record or rule of law in the CA region. It is prepared to do whatever it takes in terms of financing to get the pipeline up and running. In addition, their proximity to the Central Asian countries gives them a substantial advantage over the European Union.

**Russia’s manoeuvres within the ‘New Great Game’**

**Russia’s unprecedented revival**

With the appointment of Vladimir Putin as President in March 2000, Russia as a former superpower entered a new phase. This is best described in the dissertation that President Putin ostensibly wrote about rebuilding Russia’s domestic and international power and the role of energy herein (Putin 1999). He argued that energy should not be a wholly independent sphere, but tied to the state. In this respect, energy’s political importance is evident in the fact that the two major Russian energy giants, Gazprom and Rosneft, became to have close ties to the Kremlin in view of its nationalisation (Pappe 2007). Moreover, he claimed that Russia needs to leverage its mineral resources to promote growth and Moscow’s international status (Times 2006). And this is exactly what he did in the 8 years that he was acting President of Russia. Putin restored Russia’s international status as now it is considered a strong regional power that needs to be reckoned with.

**Russia’s alarming gas balance**

Russia on the other hand has a pressing problem maintaining its gas balance. It has even got more important in the second phase due to rising internal and external demands and declining domestic production. The domestic demand have been steadily increasing in step with the rise in GDP, up from 258 bcm in 2004 to 325 bcm in 2005 (Kimmage 2006). This domestically used gas, which is sold on a reduced price, has an important catalytic feature, since they preserve social stability and subsidize the Russian economy. In addition to this, substantial exports to the European markets, which account for the bulk of Gazprom’s profits, are also increasing as it is foreseen that exports in 2008 has reached 163 bcm in 2008 up from 151 bcm in 2006 (Kimmage 2006). According to calculations made by the Institute of the Problems of Natural Monopolies (IPEM), Russia’s annual gas deficit may reach 120 billion cubic meters by 2010 and 343 billion cubic metres by 2020. (Other studies put the deficit at 100 billion cubic meters by 2010.) Faced with declining yields at home and rising domestic and external demand, Gazprom is looking south to make up the difference as a result of which the strategic importance of Central Asian gas is increasing.

**Russia’s actions to bind Central Asian gas**

Whereas Russia in the largest part of the failed first attempt was somewhat passive with respect to binding Central Asian gas, this all changed after the appointment of Putin as President of the Russian federation. Driven by its personal vision and the growing concerns about not being able to secure and raise its gas demand and revenues in the light of the prospected increasing gas demand from the EU, Russia entered a new era by means of an
aggressive foreign (energy) policy explaining the change in the explanatory value of this particular (sub) factor.

In order to secure gas supplies from this region, Russian President Putin together with the leaders of Turkmenistan and Kazakhstan agreed on May 12 in 2007 to a large expansion of an existing gas pipeline (Prikaspiisky gas pipeline), running along the coast of the Caspian Sea crossing Turkmenistan and Kazakhstan into Russia. The pipeline would initially carry 10 billion cubic meters a year and a parallel new pipeline would be laid alongside it to boost overall capacity. This has been hailed by the international media as a Russian victory over the West, claiming that it handed out a severe blow to the trans-Caspian gas pipeline project leaving no gas for the TCGP (Konyrova 2007).

However, several analysts are downplaying the new agreement. They believe that the chances for the TCGP to be built are not more or less than prior to this announcement. For example, John Roberts, an energy security specialist with Platts Energy Services, has explained that the gas transported via this pipeline is unlikely to come from the major fields in southeast Turkmenistan that all the big players are fighting for (Abdujalil 2007). Furthermore, the initial capacity of the reconstructed line will only be 10 billion cubic meters a year, not much compared with the 50 billion cubic meters per year the Turkmen now sell to Russia and the 30 billion cubic meters per year promised to China. In addition, the Turkmen authorities have indicated that the construction of alternative routes including the trans-Caspian gas pipeline remains feasible. Although this Prikaspiisky gas pipeline deal is an important development, it does not signal the end of other proposed pipelines. It does, however, entail a considerable symbolic meaning in the sense that it shows that Russia is still the closest ally of the energy-rich Central Asian states considering the swiftness of the course of the negotiations.

Another noteworthy measure to secure gas supplies from this region, undertaken by the Russian state-controlled conglomerate Gazprom is that, starting in 2009, it would pay European market prices for Central Asian gas (Lillis 2008). Although not specifying a concrete price, given the current market conditions, the Central Asian gas producers can expect to receive somewhere in the range of $200-$300 per 1,000 cubic meters (tcm) of gas next year. In 2008 Gazprom has payed $180/tcm for Central Asian gas. This strategic behaviour helps to solidify Moscow’s position as the gatekeeper for Central Asian energy exports to Western European markets at a time in which competition over Central Asian resources has intensified. Although it seems that Russia now may be feeling more confident that it will stay on top of the ‘New Great Game’, initial indicators suggest that the “European price” that Turkmenistan will receive from Gazprom for natural gas exports in 2009 may only be a fraction of what the European Union pays for imports from Russia (Eurasianet 2008). There are speculations that Turkmenistan will be offered $210/tcm. Until there is a deal, however, nothing is set. And even then, the export price is still subject to upward revision. Fluctuations in supply and demand are only part of the cause. For the TCGP, if the price spike turns out to be higher than speculated, it might cause a dent in the EU’s leverage regarding the struggle for Caspian resources. However, Russia is not planning to absorb all the shock of the higher costs, since it plans to add the expense to its own consumers based on the announcements made by Gazprom CEO Alexei Miller (Lillis 2008), on March 14, that the gas price for European customers could reach $400/tcm by the end of 2008, compensating the aforementioned decrease in the European Union’s leverage.

All in all, it is believed that the price spike will not turn out to be a disaster for the trans-Caspian gas pipeline. Not only because of the downward speculations made about the price spike but mainly due to the fact that the Central Asian countries have more important goals, besides getting a better offer for their natural gas, to stay involved with the EU-U.S. backed
pipeline plans; political and economic independence, securing their demand and revenues by diversification and a strengthening of the relations with the West (see section 5.6.5). From EU’s perspective, the pipeline plans will not be affected in the sense that the EU is not so much desiring to gain cheaper gas as it is to diversify their gas supplies from Russia’s growing clout as a natural gas provider. Nevertheless, it remains to be seen how high the price increase will get, entailing an uncertainty with regards to this specific topic.

**The aftermath of the Russian-Georgian war**

The first week of August 2008 had seen a devastating development as Russian military forces had invaded South Ossetia, as a response to the Georgian military advancement into the breakaway region. Russia’s response could be interpreted as such that it has displayed that it is still a superpower in its immediate region, and it is prepared to act upon it, militarily if provoked.

More importantly, the implications that such an attack may have on future energy projects is of vital relevance for this research. It is believed that the war in Georgia has made the countries in the surrounding area think twice before implementing a giant energy project. Although Russia did not bomb the existing pipelines in Georgia\(^{69}\), the war reinforced the volatility of the region and thus the risk factor for making huge investments. Increased political risk makes it more difficult and more expensive (higher risk premiums) to finance new energy infrastructure projects in the region. The increasing perceptions of risk in the South Caucasus and the perceived cost of disagreement with Russia, may affect the direction of future oil and gas exports (Gould 2008). Nevertheless, it should be kept in mind that the TCGP will be connected to an existing gas pipeline, the South Caucasus pipeline. This entails that it does not encounter the same level of risks as perceived with the construction of new energy infrastructures in this region making the threshold to invest not as steep.

All in all, the perceived risk of disagreement with Russia has become higher and from the perspective of the host countries for the TCGP, it would require a compelling commercial and political case to make the risk worthwhile. The EU need to examine what they are prepared to offer to implement the TCGP, including possibilities to mitigate and/or underwrite the investment, transit and supply risks along the southern corridor.

**The United States’ ‘passive’ support**

In the second phase, the United States have been somewhat in the background with respect to promoting the trans-Caspian gas pipeline. Nevertheless, they still endorse their objective to reinforce the independence and ensure the prosperity of the Central Asian and the Caucasus countries of which promoting multiple pipeline projects and routes is an integral part. Its passiveness can partly be explained by the fact that the EU as a powerful actor (in economic terms) took over the role as a strong supporter of the pipeline project. As a result, this has somewhat eased the geopolitical rivalry in the ‘New Great Game’ concerning the struggle for Caspian gas. Nevertheless, this may change in the future as Washington could re-enter the struggle for Caspian gas with the same vigour as in the first attempt and thus must be taken into account.

**Iran’s all the more isolation causing behaviour**

Iran’s domestic and especially foreign politics took on a new start after the presidential elections in June 2005, electing Mahmoud Ahmadinejad as the new President. The new President was the initiator of a new wave of anti-West sentiments. The West in particular got

\(^{69}\) The bombings, however, occurred very close on both sides of the actual route of the pipelines
to know him for his hard-line approach. His comments that Israel should be “wiped off the map” and that the Holocaust was a “myth” drew widespread condemnation from the West. Furthermore, once in power, he strongly persists to continue with his country’s nuclear programme, repeatedly defying the West. He sticks to his opinion that it is the sovereign right of every country to develop peaceful nuclear energy, even after having faced UN imposed sanctions (BBC 2006). The nuclear sanctions continue to prevent Iran from being incorporated in the Nabucco gas pipeline project and also from being seen as a potential transit corridor for transiting Turkmen gas into the European markets (Reuters 2008). In addition, the U.S. is continuing to exclude Iran from any major pipeline projects in the Caspian Sea and is pressuring transnational corporations and states to decline from investing in the energy sector in Iran through the Iran sanctions act (ISA).

All in all, the hard-line approach of president Ahmadinejad only augmented Iran’s incapability to play a role of significance in the ‘New Great Game’ and blocked its potential participation to the Nabucco gas pipeline project, at least in the short term. Moreover, its new objective to improve regional ties by the export of gas has not been fulfilled either.

Kazakhstan’s emergence as a potential host country to the TCGP

From their independence in 1991 till now, Kazakhstan has successfully balanced its foreign policy with Russia, China, and the United States. After the alarming event in January 2006 (see EU section), the EU undertook a hot pursuit to secure diversified gas supplies in the Caspian region, entering the “New Great Game’. To this end, the trans-Caspian gas pipeline was reconsidered as an option, however, this time by redefining Kazakhstan as a potential supply country. Kazakhstan fits this picture entirely, since they are planning to produce 60-80 billion cubic meters of gas in 2015 (Ögütçü 2006). This has led to a proactive and multi dimensional foreign and energy policy seeking to find outlets for their gas. This explains their interest in joining the trans-Caspian gas pipeline project and its emergence as a potential host country in the second phase.

The EU and the U.S. in their official visits to Kazakhstan in May 2006 (Asianews 2006; RFERL 2006), strongly urged Kazakhstan to construct a gas pipeline across the Caspian Sea in order to create a gas outlet for Central Asian supplies to Europe through the Caucasus and Turkey, whilst offering a grant to help fund the feasibility of the project. For Kazakhstan this would mean a diversification of its export routes and a possibility to break Russian monopoly over export routes from the landlocked Central Asia. Kazakhstan’s stance is that they consider the TCGP as an important interest and even adopted the position that trans-Caspian pipelines should be an issue of the countries whose seabed is crossed. However, it awaits for a resolution on the Caspian Sea’s legal status as Kazakhstan remains cautious given that Russia is Kazakhstan’s main strategic partner as the latter takes into account Russia’s opinion. This strongly indicates Russia’s leverage in the relations with Kazakhstan.

All in all, the Russian leverage should be regarded as an important hurdle to the West’s endeavours to involve Kazakhstan in supplying the trans-Caspian gas pipeline. Kazakhstan’s moderate stance caused the European Union to refrain from its proactive efforts to include Kazakhstan - without excluding the option - and turned their attention to Turkmenistan. For now, with respect to the trans-Caspian gas pipeline project, Kazakhstan is awaiting the results from the feasibility study as only then the possibility will emerge to discuss it in more detail (Itar-Tass 2007).
The new Turkmen President offers hope

The death of President Niyazov followed by the appointment of the new President Berdymukhammedov and his proclaimed multi-vector foreign policy has sparked renewed hope that gas-rich Turkmenistan will open up fully to international investment. Turkmenistan, however, is still careful before signing on the dotted line with new private partners. It is believed that the Turkmen strategy to remain cautious is because this way they can use pipelines as bargaining chips to maximise interest in its resources. Moreover, diplomats in Ashgabat believe the first important step needed before a trans-Caspian gas pipeline can be built is the discovery of more gas by outside firms in the offshore Turkmen section (WGI 2007). They claim that only then Turkmenistan will be willing to export gas to Europe. This announcement should be viewed in the context of the longstanding prohibition of foreign companies to gain a stake in the onshore section, which unlike the offshore is guarded for national interests. In this respect, it is believed that the discovery of an offshore gas field will probably be the most convenient for the TCGP in terms of costs and transparency, since lesser pipeline will have to be laid as opposed to connecting it to the fields in southeast Turkmenistan. In addition, permission is granted for foreign corporations to explore, drill and produce natural gas in the off shore sector. However, it is argued that in the end foreign investment is necessary in terms of financing and technological expertise to develop the resources onshore (Pannier 2008). Especially, since Berdymukhammedov’s ambitious plan for the country is to increase its gas production to 125 bcm annually by 2015 and 250 bcm by 2030 compared to 70 bcm in 2007 (APS 2008).

Furthermore, President Berdymukhammedov announced in January 2008 to allow an international auditing firm to assess its alleged vast gas reserves, suggesting that Turkmenistan is serious in its strategy to open up to the outside world (WGI 2008). In this respect, preliminary results of the audit have shown that the Yoloten-Osman gas field has a low estimate of 4 trillion cubic meters, a best estimate of 6 trillion cubic meters and a high estimate of 14 trillion cubic meters (Pannier 2008). This would make the Yoloten-Osman gas field approximately the fourth or the fifth largest gas field in the world. Nevertheless, gas (and oil) reserves information is considered inherently imprecise making the estimation highly uncertain (SPE 2007). Adding to that uncertainty is the fact that the acquired reserves information is assessed by just one company. For the time being, the availability of sufficient natural gas in Turkmenistan is uncertain and ought to be taken into account as an important impeding (sub) factor.

If the results are affirmed, though, it remains to be seen how quick the West will react. For Turkmenistan it means that they need to decide about whether they can afford to defy Russia. In this regard, the benefits must be sufficiently high as such that the gas deal is able to provide a significant part of their future revenues. Just then it might be worthwhile for Turkmenistan to irritate their powerful neighbour.

All in all, President Berdymukhammedov’s actions do promise a more sound and pragmatic strategy with respect to the realization of multi-vectored pipeline projects. However, Turkmenistan is remaining cautious with making substantial commitments as it is believed that not knowing what kind of cards Turkmenistan is holding might give President Berdymukhammedov the best bargaining position with Russia, China and the West. In this respect, Turkmenistan’s decision to have an independent audit of their gas reserves is a first step in exposing their cards and may be a possible forerunner for opening up to foreign investment in the onshore section.
5.7.4 Rapprochement between Azerbaijan and Turkmenistan

Another notable development regards the recent rapprochement between Azerbaijan and Turkmenistan. The death of Niyazov in December 2006 provided Baku with an opportunity to revive the ties and make a fresh diplomatic start. Renewed bilateral talks between the two countries have found its highlights in 2008 in which representatives of both countries have met three times to talk about the long-lasting issues that were tormenting bilateral ties. In the last meeting even a breakthrough was achieved on a 16-years old debt dispute, indicating a glimpse of hope to advocates of the trans-Caspian gas pipeline. Moreover, the delineation of the maritime border has been a major point of contention between the two countries for years and the frosty ties between the two former leaders only aggravated the issue. It is this issue more than others that have caused more than a decade long chill in the relations of the two countries. As identified in the first phase, bilateral issues was the main impediment that had caused the negotiations between Turkmenistan and Azerbaijan to fail. A resolution on this particular issue is a must before the countries can enter into talks about the implementation of the trans-Caspian gas pipeline.

With regards to the delineation of their maritime borders, the presidents were optimistic but noncommittal. Representatives of both countries did discuss that issue and noted progress, but they declined to give any specifics, such as whether they were closer to agreeing on jointly developing the fields. Instead Berdymukhammedov pointed out that the legal status of the Caspian Sea must be decided soon. But Aliyev added that if his country and Turkmenistan could resolve their differences over the disputed fields, then that could also lead to a final decision on the Caspian’s status (Pannier 2008), suggesting that they are willing to be proactive with regards to resolving the legal status issue pursuant to their own interests. One should keep in mind that President Berdymukhammedov especially would not want to anger Russia, hence the cautious approach. If this trend of pragmatism and goodwill continue on both sides, it is argued that an agreement on the delineation of their territorial lines may be forthcoming in the near future.

5.7.5 The legal status of the Caspian Sea

The latest summit of the Caspian heads of state was held in Tehran, capital of Iran, on October 16th, 2007, hosting the leaders of Russia, Iran, Azerbaijan, Turkmenistan and Kazakhstan. Hopes were high on finally resolving the longstanding issue – sea or lake? - over the definition of the world’s largest inland body of water. Instead, the leaders dodged the key issue and left it for the next Caspian summit. Moreover, on the Caspian summit, Putin found himself in disagreement with the Presidents of Azerbaijan, Kazakhstan and Turkmenistan on the issue of pipeline construction in the Caspian Sea. Putin reaffirmed his position, which is shared by Iran, that all five riparian countries should approve the construction of any trans-Caspian pipeline project. This would give Russia a veto for blocking any trans-Caspian pipeline projects that would connect Kazakhstan and Turkmenistan, via Azerbaijan, directly to Europe. While Azerbaijan has all along supported the right of littoral states to lay trans-Caspian pipelines in their respective sectors and to link such pipelines if needed, Kazakhstan supported it intermittently. However, on the summit in Tehran, Kazakhstan unambiguously proclaimed that the laying of a trans-Caspian pipeline should only be conditional to an agreement between countries whose seabed would be used, signalling a consistent stance on this issue from now on. Turkmenistan on the other hand, deferred to the Russian and Iranian position on this issue during the former President Niyazov’s rule (1992-2006). But on the

70 Under the deal, Turkmenistan will reportedly receive by the end of the year nearly $45 million of the $56 million it claims it has been owed for gas supplies since 1991-92. Baku had claimed the debt was just $18 million.
Tehran summit the Turkmen President Berdymukhammedov did not endorse the position of Putin on this issue, clearly displaying his pragmatic and rational nature in tune with Turkmenistan’s interests (nCa 2007). However, he did not assume a clear and assertive position on the issue either. The Russian and Iranian view failed to be included in the Summit’s declaration signed by the five Presidents. During the summit President Nazarbayev as well as President Aliyev, necessitated the freedom of transit in the Caspian basin by all means of transportation, including pipelines. They argued that this should be included in any convention on the Caspian Sea’s legal status.

All in all, the legal status of the Caspian Sea remains unresolved, continuing to be an impediment to any trans-Caspian pipeline projects. However, the refusal of the Turkmen President to endorse Putin’s position on the construction of trans-Caspian pipelines seems promising, although he still has to adopt a clear and proclaimed position on this issue. Nevertheless, the promising rapprochement between Azerbaijan and Turkmenistan might make a resolution on the legal status of the Caspian Sea unnecessary, since it is considered an issue concerning only the maritime borders of these countries, at least from a technical point of view. But the willingness and determination of in particular Turkmenistan to go through with the implementation of the TCGP, despite the lack of an agreement of the legal status, remains to be seen.

5.7.6 The status of the environmental objection

On the Caspian summit in Tehran, Russia and Iran reiterated their argument that no trans-Caspian pipelines can be built due to its ecological risks. In addition, the littoral Caspian countries have agreed that each of them has the right to demand an environmental evaluation of any pipeline project crossing the Caspian basin, which is regarded as an obstacle that could delay or even kill a project. This part of the declaration and the speeches of the Russian president can be seen as Russia desiring to emulate the attempts of Estonia and Finland to freeze construction of the Nord Stream gas pipeline (running from Russia to Germany under the Baltic Sea) (Brower 2008). It is believed that Moscow may be using the same tactic; if a pipeline in the Baltic can be delayed for ecological reasons, than why not in the Caspian as well (Globe 2007). This is an interesting development with respect to this issue, which must be taken into account.

5.7.7 Transnational corporations and their striving to minimize project risks

In the second attempt no consortium of transnational corporations is established as yet, since first and foremost the results of the feasibility study funded by the European Union is awaited, before any concrete steps will be taken in this regard. Furthermore, another point that deserves attention from the point of view of investors is the access to energy fields. The decision to make an investment in the field of energy is usually made after balancing the expected financial rewards with the attendant perceived geological, commercial and political risks (Seck 1996). In this respect, it is not clear how much the TCGP project will cost, how much natural gas Turkmenistan possesses and how much of it would be left after Turkmenistan fulfils its obligations to China and Russia making it a commercially risky undertaking. The physical access to energy fields is an important catalyst in this regard, especially in a country such as Turkmenistan in which ambiguity and opacity has been more a rule than an exception. The direct access to the gas energy fields in terms of exploration and production has the potential of levelling out at least some of the commercial risks that the TNOC’s face. For example, the acquired access to the energy fields is what made the
implementation of the BTC oil pipeline and the South Caucasus gas pipeline successful. The key to success back then was to focus first on getting access to the energy fields and only than concentrating on the pipeline to get it out, rather than on building the pipeline first (Kucera 2008). The physical access to energy fields was less of an issue for the transnational corporations in the first attempt as the United States and their lending agencies were financially and politically committed to support the TCGP. This took away the commercial risks the corporations faced for not having access to the energy fields in Turkmenistan. However, whether the same commitments will be made in the second attempt remains to be seen. This depends partly on President Berdymukhammedov’s willingness to open up the onshore section for foreign investors or on a discovery of a gas field in the offshore section of Turkmenistan. On the other hand, it also depends on whether the EU and/or the USA is prepared to make strong financial commitments. Nevertheless, this uncertainty needs to be incorporated and therefore physical access to gas fields is seen as an important (sub) factor in the second attempt. Moreover, it is regarded as a precondition for the TNOC’s, unless financing is guaranteed by a third party.

5.7.8 The role and influence of international institutions

As it was in the first phase, the participation of (inter)national financial institutions may also be crucial in the ongoing second attempt, both for the financing of the trans-Caspian gas pipeline and the commitment of political will. Turkmenistan especially does not have a legal structure in place that provides the same level of protection in Azerbaijan and Kazakhstan. Above all, the access to gas fields is not guaranteed and as long as that fact remains the same combined with the low level of legal protection, transnational corporations will not be eager to invest billions of dollars as the risk assessment would tell them to decline. There has been no confirmation as yet of financial support for the TCGP in this stadium. The European Union on the other hand is wary on politically motivated investments as they strongly believe that the project should be commercially viable.

Regarding the overall effect of the Energy Charter Treaty, it can be stated that the number of publicly reported cases under the ECT have been relatively limited to date but are slowly on the rise (Beeley 2007). However, whether this Treaty will be successful in the general sense and in the Central Asian countries in particular is doubtful to say the least. The value of the Energy Charter Treaty (ECT), from the perspective of the foreign investor lies in its ability to decrease the level of political risk in the concerned transition economies, including Central and Eastern Europe and the Commonwealth of Independent States (CIS). However, the (foreseen) political instability in parts of the CIS, including Turkmenistan and Kazakhstan, raises the fear of major upheavals in government. A change of government in itself should not release a State from its Treaty obligations (Brazell 1996); however, in practice, radically different administrations are not likely to accord international investment treaties with much respect (Sornarajah 1996). In the event that a new State is created by secession, it may not consider itself to be bound by the Energy Charter Treaty. Furthermore, it is asserted that due to formidable institutional and internal weaknesses, some countries are not in a position to implement the investment provisions of the Energy Charter Treaty (Andrews-Speed 1996). It is believed that this also holds for Kazakhstan and Turkmenistan in particular, since they are characterised by institutional weaknesses (see section 5.4.3 and 4.3 respectively). Also the recent trend of resource nationalism in Kazakhstan (see section 5.4.3) only adds to this assertion. Therefore it is believed that the direct and immediate impact of the Energy Charter Treaty in Turkmenistan and Kazakhstan with respect to providing a favourable investment climate is likely to be modest and is therefore left out of the analysis.
5.8 The interconnected gas pipeline project

In the current climate of the need for diversification of gas supplies and routes more attention goes to securing gas over larger distances connecting various regions through different gas pipeline projects. This is explained by the constructivist approach as the increased prioritization/urgency of energy security is a direct result of how some importing countries have increasingly come to view dependency on some gas exporting countries as a threat to its energy security (e.g. Russia-Ukraine gas crises) among other aspects (see section 5.7.2). Therefore a new factor is identified, namely the ‘interconnected gas pipeline project’. In this respect, the Turkmen and Kazakh gas will be connected to the European gas markets by means of the Nabucco gas pipeline project (see figure 8). It is researched if the Nabucco project has alternative interconnected gas projects meant to feed the pipeline and the same is done for the TCGP project as well in order to determine the degree of interdependency between the two projects. Investigating which specific factors influence the realization of the Nabucco project falls outside the scope of this study though, since it would entail writing a dissertation similar to this one.

For the time being, the Nabucco project is the only outlet for the East Caspian countries to send their gas to the European markets, which makes its realization vital for the ongoing second attempt to realize the TCGP. Nevertheless, some level of depth is required in the analysis as to find out how the host countries view the interdependency between the two projects. Moreover, EU’s point of view in relation to Russia’s view will be touched upon as well.

Needless to say that both Kazakhstan and Turkmenistan have significant ties with Russia who adamantly opposes both the Nabucco and the trans-Caspian gas pipeline project. In this respect, the host countries are not prepared to damage these ties for loose promises. It is believed that until Nabucco can show visible progress on construction, it is unlikely that any of the two countries would risk damaging their ties with Russia by committing to the European project. In other words, these countries will seriously consider committing themselves to the project if they have the guarantee that they can transport their gas to the European gas markets. Moreover, the ongoing second attempt differs from the first in a critical point; the fact that the European Union is actively portraying the Nabucco gas pipeline and the TCGP as complementary to Russian gas projects rather than as rivals. In the first attempt, the USA was aggressively encouraging the realization of the TCGP and thereby polarizing the competition for Caspian region’s natural resources. In the ongoing second attempt, however, Jozias van Aartsen, the former Nabucco project coordinator, underlined and propagated this view of the EU as he grabbed every opportunity in the talks that he had with his Russian counterparts to declare that Nabucco is not a rival but rather a complementary project, attempting to change Russia’s perception.

Although it seems that the TCGP project is more dependent on the successful implementation of the Nabucco pipeline than vice versa, due to the fact that the Nabucco pipeline project has more alternatives besides the TCGP, this is not entirely true. These alternative sources all have their own set of problems complicating the viability of these interconnected pipeline projects. As the TCGP depends on the green light for the implementation of the Nabucco, the Nabucco in his turn also depends on the TCGP’s realization due to a lack of sufficient supplies. In this respect, the only supply guarantee, albeit a gentleman’s commitment, the

71 South Stream gas project; an additional gas pipeline project aimed to provide Eastern and South Europe with Russian gas.
72 (Interview with author, 28-2-2008, The Hague)
Nabucco has obtained is from Azerbaijan, but Azeri gas alone is not sufficient to fill it as announced by Azeri officials (HDN 2008). Azeri export capacity in general and to the Nabucco in particular remains unclear. Nevertheless the Azeri gas is crucial to bring Nabucco on line in 2013 as planned. In addition, the latest developments show that Azerbaijan is dithering between competing Russian and EU bids for its gas exports (VOA 2009). Iran is no option since the EU has announced that it does not need or desire Iranian gas which has to do with the latter’s disputed nuclear stand-off. Iraq has pledged to supply the Nabucco with 5 bcm per year, but the country has been tormented the past years with fierce instability as a result of which potential gas supply from that region is doubtful at the least. The Arab Gas Pipeline project is destined to be online by early 2010, linking Aleppo, northern Syria, with the Turkish border. Officials have announced that this pipeline will supply the Nabucco gas pipeline with 2 bcm annually (Lobjakas 2006). Simple mathematics tell us that even with the prospected deliveries from Azerbaijan73, Egypt and Iraq, it will not be enough to fill the Nabucco gas pipeline which has a capacity of 31 bcm annually.

All in all, the Nabucco project has no serious alternative interconnected gas projects that could replace the trans-Caspian gas pipeline project. The TCGP project in turn also has no serious interconnected gas projects at least in the near future. This underlines the strong interdependency between the gas pipeline projects. In conclusion, this new factor must be incorporated into the original Case Study Protocol to increase its completeness and therefore its analytical strength. In the medium to long term, however, the TCGP’s odds of becoming reality could gain in value since Turkey may become the sole offtaker in the future given their increasing demand projections for gas eliminating this particular factor all together. In addition, the Turkey-Greece gas interconnector with the prospected extension to Italy could become a viable outlet as well. This will be touched upon in the third phase.

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73 Prospected deliveries of 11,5 bcm annually to Turkey-Greece-Italy interconnector
5.9 Conclusions

The main purpose of this section is to provide an answer to the research questions stated in the beginning of this chapter based upon the conducted analyses in this chapter. As such, first an answer will be given to the following research questions:

*What are the main alterations of the explanatory factors taking into account their development over time from the first attempt till now and how do they contribute to the advancement or impediment of the ongoing second attempt to realize the TCGP?*

*Are there any new (sub) factors that have emerged in the second phase and what is their influence on the ongoing second attempt to the extent that it is possible to determine it in this stadium?*

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Table 5: Overview of the (sub) factors in the ongoing second attempt

With respect to the *investment climate* of Kazakhstan, it is concluded that a serious threat in the short to medium term to its domestic and political stability arises from the insufficient level of institutionalization that is supposed to guide and support a democratic change. In this respect, President Nazarbayev is doing little to ensure a smooth succession of his presidency. Hence, a sudden death of Kazakhstan’s leader is a threat needed to be reckoned with endangering the investment climate of the country and in turn decreasing the implementation chances of the TCGP, at least the section from Kazakhstan.
In addition, the current global financial crisis brings along a serious threat for Kazakhstan as it faces the potential risk to be exposed to a deep economic crisis and dire social consequences endangering its political and domestic stability. Furthermore, although the political structure of Turkmenistan has not changed considerably and still is an impediment to its investment climate, the change in autocratic leadership, however, has brought opportunities for the concerned actors regarding the second attempt to realize the TCGP. It was not the interests of Turkmenistan that have changed but more the determination and pragmatism with which the new President Berdymukhammedov is acting to pursue his multi-vector foreign policy.

With respect to the transit risk, the main impediment in the first attempt, the Azeri-Turkmen bilateral issues, is still an issue in the ongoing second attempt as well. It is regarded as a precondition that needs to be resolved beforehand. Nevertheless, after the appointment of the new President Berdymukhammedov motions have been set in place between the two states that has brought a solution of this particular issue a step closer.

The fourth factor concerns geopolitics. Also in the second phase, Russia and Iran oppose the TCGP on environmental grounds. In addition, an important development of this (sub) factor occurred on the Caspian summit in Tehran in 2007 where the littoral countries have agreed that each of them has the right to demand an ecological evaluation of any pipeline project crossing the Caspian Sea. This is an agreement that could delay or even kill the trans-Caspian gas pipeline project and any other pipeline project crossing the Caspian Sea. Furthermore, also the issue of the legal status of the Caspian Sea lingers as one of the main impediments. However, the refusal of the Turkmen President to endorse Putin’s position that no trans-Caspian pipelines can be built without the consent of all riparian states seems promising, despite the fact that he still has to adopt a clear position on this issue. On the other hand, the promising rapprochement between Azerbaijan and Turkmenistan might make a resolution on the legal status of the Caspian Sea redundant, since it is considered an issue concerning only the maritime borders of these countries, at least from a technical point of view. But the willingness and determination of in particular Turkmenistan to go through with the implementation of the TCGP, despite the lack of an agreement of the legal status, remains to be seen.

Russia, as it was in the first attempt, is working persistently to secure the much needed gas from Central Asia and to prevent the gas from being sent directly to the European markets. In this respect, Russian President Putin agreed on May 2007 with the leaders of Turkmenistan and Kazakhstan to expand an existing gas pipeline running along the shore of the Caspian Sea, namely the Prikaspiisky pipeline. Experts claim, however, that the impact of this Russian move on the trans-Caspian gas pipeline will be limited, as some explicate that the gas transported via this pipeline is unlikely to come from the Turkmen reserves that all the big players are fighting for in southeast Turkmenistan. It is asserted that the gas will come from the mainstream gas fields, which are already in operation. In the meantime there is no doubt that the agreement has a considerable symbolic meaning in the sense that it underlines that Russia is still the closest ally of the Central Asian states.

China is considered a serious competitor to the trans-Caspian gas pipeline project to the extent that they are vying for the same gas reserves. In light of the announced preliminary audit results, which were better than anyone ever imagined, China is to be reckoned with in the “New Great Game” as fierce competition is expected for these huge gas fields in southeast Turkmenistan if proved accurate. A competence to which China is not unfamiliar to say the least since they are an end consumer and are not sceptical about the commercial viability of the pipeline but do whatever it takes in terms of financing to get the pipeline up and running.
With respect to the United States, it remains to be seen to which extent they will get involved now that the European Union is the actor that has the strongest interest in the project. The EU is a relative latecomer to the ‘New Great Game’, facing up against the strong relations that Russia enjoys in the Caspian region and China’s rising power. A pressing problem, however, is to find investors for the trans-Caspian gas pipeline project. Brussels says it will not underwrite the investments, insisting on the fact that the projects must be commercially viable. The EU’s aversion of “political investments” makes its strategic interests vulnerable to meddling by Russia, which controls the huge national gas company Gazprom and China, who also owns their oil and gas companies.

In the second phase, the United States have been somewhat in the background with respect to promoting the trans-Caspian gas pipeline. As a result, this has somewhat eased the geopolitical rivalry in the ‘New Great Game’ concerning the struggle for Caspian gas. Nevertheless, this may change in the future as Washington could re-enter the struggle for Caspian gas with the same vigour as in the first attempt and thus must be taken into account.

Turkmenistan’s pragmatic approach is further underlined by President Berdymukhammedov’s permission to allow an independent international auditing firm to assess the country’s alleged vast natural gas resources. Although the preliminary audit results of the southern Yoloten-Osman gas field indicated that there is enough gas for Turkmenistan to comply with its existing gas contract commitments and more, the accuracy is highly uncertain in this stadium. To this end, the uncertainty with regards to the availability of sufficient natural gas in Turkmenistan remains an important impeding (sub) factor. Furthermore, it needs to be mentioned that a discovery of a gas field in the offshore section will probably be more attractive for the TCGP in terms of costs and competitiveness, considering the proximity to the South Caucasus gas pipeline.

Kazakhstan’s stance towards the realization of the TCGP is that they consider the TCGP as an interest, however, it believes that the project cannot be put into effect without a binding agreement on the legal status of the Caspian Sea. The economic and political might of Russia is mostly felt in this country as Russia is her main strategic partner due to common economic and security ties and the presence of 6 million Russians living in Kazakhstan explaining its cautious approach when it comes to Russia. It did, however, take a defying stance in the Caspian summit in Tehran in 2007 that the construction of the trans-Caspian gas pipeline is up to the countries whose seabed it crosses. For now it is awaiting the results of the feasibility study because only then the possibility will emerge to discuss it in more detail.

The transnational corporations consider getting physical access to gas fields as an important issue, especially in volatile regions such as Central Asia and the Caucasus. When access is denied transnational corporations are reluctant to take the commercial risk. In this case a strong financial and political commitment from the West and their (inter)national financial institutions may be required.

No affirmed commitments have been done by neither the U.S. or the European Union and their respective (inter)national financial institutions to come up with a mechanism to fund the project. This was crucial in the first attempt to induce the international consortium to make investments under risky market conditions and other commercial uncertainties. In the ongoing second attempt, both the financial and political commitment may prove to be equally significant.

Another additional factor that needs to be taken into account is that the trans-Caspian gas pipeline is interconnected to another gas pipeline project, namely the Nabucco pipeline. For the time being, the Nabucco project is the only outlet for the East Caspian countries to send their gas to the European markets, which makes its realization vital for the ongoing second attempt to realize the TCGP. Moreover, it is believed that until Nabucco can show visible
progress on construction, it is unlikely that neither Kazakhstan nor Turkmenistan would risk damaging their ties with Russia by committing to the European project. Furthermore, the Nabucco project has no alternative interconnected gas projects capable of replacing the TCGP underlining the strong interdependency between the two projects.

The third research question that needs to be answered is the following:

*How has the role and influence of Turkey developed in the second phase within the context of the ‘New Great Game’?*

Turkey has set its eyes on the Central Asian region once again. Though this time, pragmatism and rationalism prevails in its foreign policy over shared ethnic and linguistic ties. Although attempts have been made in this respect on the Presidential level, these are not considered sufficient as the involvement of the executive power is necessary to reinforce the bilateral ties substantially, considering Turkey’s objective to become a key economic and political partner in the region. Nevertheless, its unique ties with the Turkic countries combined with its increasing economic clout, its growing regional influence and international prestige and the improving relations with the West do provide Turkey with an opportunity to become a key player in Caspian region.

Moreover, in the light of its growing importance as a mediator Turkey has suggested to mediate between Azerbaijan and Turkmenistan as both countries welcomed this proposal. Furthermore, Turkey has seen its economic and political ties develop with Russia in the second phase. Perhaps more importantly, recent developments indicate that Russia does not view Turkey as a threat to its domestic stability as it did before in the nineties. It may eventually lead to a change in Russia’s perception that Turkey is a geopolitical rival in the ‘New Great Game’. To this end, the developing Russia-Turkey relations ought to be taken into account in the third phase when constructing the future worlds. Moreover, Turkey demands to extract fifteen percent (15%) of gas from the Nabucco gas pipeline against relatively cheap prices, thereby implying that it should get an exceptional treatment due to its geographical location. This has resulted into a dispute with the European Commission and the member countries involved in the project. An adamant stance of Turkey may endanger the Nabucco gas pipeline project and thereby the TCGP. Turkey may not only loose the chance of increasing its security of gas supply but also risk losing an opportunity to regain its (geo)strategic importance.
6. Reflection on the factors’ possible future development (3rd phase)

6.1 Introduction

In this chapter, the potential future development of the identified main (sub) factors will be determined (see figure 2). It is argued that countries respond to the evolving situation in the energy market, adopting reflexive strategies and have regard for each other. Moreover, it is asserted that energy relations in the world will take shape along the lines of the future international political and economic system (Correlje 2006). To this end, future worlds will be constructed along these lines of the future international political and economic system as it will be examined what its implications are for the development of the identified (sub) factors. Nevertheless, the third phase is considered as merely a means to reflect on how the factors could develop within certain international political and economic contexts. In this respect, mainly contrasting (extreme) future contexts will be constructed along which the world may develop.

In this chapter, an answer will be provided to the first part of the main research question:

To which extent and under which conditions shall the main (sub) factors contribute to the advancement or impediment of the attempt to realize the trans-Caspian gas pipeline project in the future?

6.2 The constant, changing and non-assignable factors

In this section, before determining the future development of the (sub) factors, a comparative analysis will be conducted between the first and second phase in order to make a distinction between the more or less constant (long-term, non-changing), the changing and the non-assignable (sub) factors (see figure 1). The underlying reason is that the categorization of the (sub) factors provides one with indications of how they may develop into the future. In other words, it helps determine the future development of the (sub) factors. The (sub) factors will be categorized by using the collected knowledge about the driving forces behind the factors’ development from the first phase till the second phase (constructivist approach). Also uncertainties that have manifested in the first phase and its actual development in the second phase will be taken into consideration. Furthermore, the newly emerged (sub) factors in the second phase will also be considered. However, since no conclusions can be drawn based upon their development over time, their assessment will occur by mere reasoning.

A (sub) factor is constant (non-changing) when in the period between the first and the ongoing second attempt, 1997 till present, the factor still manifestly plays a role of importance in an unchanged manner. In other words, this means that the (sub) factor’s driving forces must be unchanged, but the extent of influence or explanatory power of this (sub) factor can be very much altered. In addition to this, in case that a (sub) factor arises in the second attempt and one cannot derive much from its development over time, one can also employ plausible reasoning to label it as constant. This also applies to the subsequent factor. A (sub) factor is labelled as changing when in the period between the first and the ongoing second attempt a development in its driving forces has occurred, which caused it to change in terms of explanatory power and/or outlook. In addition, there is also a third label, namely non-
assignable (sub) factors. Factors will be assigned to this label when its influence/effect is unsure and/or cannot be backed by plausible reasoning as to whether a (sub) factor is either constant or changing.

The (sub) factors that are considered constant are the unresolved legal status of the Caspian Sea, ecological objections by Russia and Iran, Turkmenistan’s political structure, Kazakhstan’s political structure, Russia’s actions to bind Central Asian gas, China’s struggle for Central Asian natural resources, physical access to energy fields and the participation of (inter)national financial institutions.

The changing sub factors are new leadership in Turkmenistan, Turkey’s mediator role and the bilateral relations between Azerbaijan and Turkmenistan.

The non-assignable sub factors are Turkey’s demand to import cheap gas from Nabucco, succession of Kazakhstan’s Presidency and EU’s aversion to political investments degree of dependency on the interconnected gas project and sharp decline of oil prices (global financial crisis).

6.2.1 Constant factors

The legal status of the Caspian Sea still remains unresolved in the ongoing second attempt. In this respect, Russia and Iran are fervent advocates of the status quo. Although, each have their own idea of how the Caspian Sea should be divided coherent with their economic and geopolitical interests, Russia’s and Iran’s common point, however, is that the status quo will hinder Western influence in the Caspian Sea and the littoral Turkic countries. In this respect, it provides them with the means to hinder the realization of the western bound trans-Caspian gas pipeline project. By and large, the driving forces behind the Russian and Iranian stance have not changed as a result of which this issue has seen no noteworthy developments in the second phase and therefore is considered a constant sub factor.

The driving forces behind the ecological objections by Russia and Iran to trans-Caspian pipelines have not changed as it is still used as a means to hinder the trans-Caspian gas pipeline project. It has, however, undergone a change in its impact/influence. The littoral states of the Caspian Sea have agreed that each of them has the right to demand an ecological evaluation of any pipeline project crossing the Caspian Sea. This has the power to delay or even kill the project augmenting the impediment power of this particular sub factor.

Russia’s actions to hinder the realization of the TCGP is as prevalent in the second attempt as it was in the first as it is attempting to bind Central Asian gas with various actions. Furthermore, these actions of Moscow to bind the Central Asian gas is a natural consequence of its prioritization of energy security (interests) and what it means for their objective to restore Russian supremacy in the region and in the world (see 5.7.2), implying that it will remain a constant impeding (sub) factor.

Turkmenistan’s political structure has not changed as all the political power is still concentrated in the office of the President. In such a country, the risk of detrimental reign and political instability is high, hence making it a constant impeding (sub) factor.
Kazakhstan’s political structure in essence has not changed either. On the contrary, there have been developments which indicate that President Nazarbayev’s political and economic power has increased, augmenting the (sub) factor’s potential impeding power.

Although the U.S. have remained in the background in the second phase, their foreign and (energy) security policy towards the Central Asian and Caucasus countries has not changed as it is therefore viewed as a constant (sub) factor. It is a global power who in the future could decide to again proactively support (in financial and political terms) the TCGP increasing the geopolitical rivalry in the ‘New Great Game’. This may generate different results depending on the future context of the world (future worlds).

China’s entrance in the ‘New Great Game’ added another rival to Russia and the West regarding the competition for the Central Asian gas reserves. Although introduced in the second phase, China’s presence in the ‘New Great Game’ is expected to be long-lasting given its prospected economic growth and increasing need for foreign energy resources (see 5.7.2).

In the ongoing second attempt no financial commitments have been made or willingness to that end is shown as yet by neither the USA nor the EU. As a result of which physical access to the energy fields should be regarded as a precondition for the transnational oil corporations before they will commit themselves financially.

The participation of the (inter)national financial institutions is unsure in this stage of the project as the feasibility study’s results are still awaited for. Moreover, an important potential driving force behind their participation, which are the EU and USA since they have the power to mobilize the financial institutions, is unsure as well. But it is believed, considering the bad investment climate of especially Turkmenistan and the commercial risks of the project (availability of gas in Turkmenistan), that the participation of the international financial institutions would be necessary in the ongoing second attempt, making it a constant (sub) factor.

6.2.2 Changing factors

The leadership of Turkmenistan underwent a significant change in the sense that the former President Niyazov was succeeded by a relatively reform minded person, especially on the energy dimension. President Berdymukhammedov, in contrast to the former President, has a far more pragmatic approach towards finding export outlets for its natural gas, laid out in his multi-vector foreign policy. This factor has undergone a significant development in its driving force (new President) as it is not considered one of the main impediments any more, but an opportunity and therefore is considered a changing (sub) factor.

Turkey has announced, given its new multi-dimensional foreign policy strategy (see 5.7.3), that it is willing to play a mediator role between Turkmenistan and Azerbaijan, indicating a proactive stance in the ongoing second attempt and a potential contributing factor to realize the TCGP. This should be seen in the light of Turkey’s developing diplomatic status, which has been obtained in the second phase (2001 - present) making it a changing (sub) factor.

The bilateral issues between Azerbaijan and Turkmenistan, which was deemed as the death blow in the first attempt, are unchanged in the ongoing second attempt and is regarded as a precondition that needs to be resolved before the TCGP can be realized. Nevertheless, one of the main driving forces behind this (sub) factor has changed as new leaders in both Azerbaijan
and Turkmenistan have assumed Presidency as a result of which positive developments have occurred. For that reason, this (sub) factor is categorized as changing.

### 6.2.3 Non-assignable factors

Unlike the United States, the European Union is apparently against ‘political’ investments, since they believe that the project should be commercially viable. This is regarded by some experts as the Achilles heel of the European Union compared to the energy security strategy laid out by Russia and China. EU’s presence in the Central Asian region will be long-lasting, taking into account their interests laid out in a long-term strategy towards this region and in particular with respect to their energy security interests. However, if the competition in the ‘New Great Game’ gets fiercer while assuming that Russia and China will continue to disregard the liberal market attitude that a gas infrastructure project should be commercially viable, the EU may be compelled to change their stance. Therefore this particular (sub) factor is defined as non-assignable.

The Kazakh President Nazarbayev is not undertaking significant efforts to guarantee a sufficient level of institutionalization that is supposed to guide and support a democratic change. The low sense of urgency will stay the same or even be reinforced after his enactment to stay President for life. Therefore its political and domestic stability is under potential danger, considering that a sudden death of the residing President Nazarbayev may create a power vacuum in the country. However, the same was said about Turkmenistan and its former President’s death, but the succession had occurred smoothly and without any complications. The extent to which Turkmenistan and Kazakhstan are comparable in this respect is outside the scope of the study, but the Turkmen case leads to the fact that this particular (sub) factor is labelled as non-assignable.

Turkey’s demand to import cheaper gas from Nabucco to use it for domestic use has been stalling the project among other factors\(^\text{74}\). The EU is starkly against Turkey’s stance on this issue as they cannot give Turkey a preferential treatment over the other participating countries. Nevertheless, the project’s significance for Turkey is far bigger than just a means to maximize its profits as its realization would augment Turkey’s (geo)strategic importance in the region and to the EU and at the same time increase its energy security. The project also cannot be seen separately from Turkey’s candidacy to join the European Union. Hence, when considered from a long term strategy one would think rationally that Turkey will cave in to EU’s demands and certainly will not bring the Nabucco project into danger. However, the perseverance that Turkey has shown till now combined with its reputation that it is not reluctant to use its position to renegotiate prices and volumes (see 5.6.2) has earned this sub factor to be labelled as non-assignable.

The interconnected gas pipeline project’s influence is undeniable as it the only outlet in the foreseeable future for Turkmen and Kazakh gas with respect to the TCGP whether or not it is in the form of the Nabucco project or an alternative interconnected gas project. But there is also the possibility in the medium to long term that Turkey could function as the sole offtake market for Turkmen and Kazakh gas given its prospected growth in the demand for imported gas. This would eliminate this particular factor as the South Caucasus gas pipeline is already built. Therefore, this particular factor is labelled as non-assignable.

\(^{74}\) Financing and finding sufficient supplies
One of the main threats to Kazakhstan’s investment climate is a sharp decline in oil prices causing a substantial decrease in its export revenues as the diversification of its economy is poor. Given the cyclical nature of oil prices (Stevens 2008), surpassing the time period taken in this research, this (sub) factor is categorized as non-assignable. Moreover, the current global financial crisis may have a highly damaging effect on its investment climate provided that it persists for a long time.

6.3 Constructing future worlds

The main objective of this section is to write different and contrasting future contexts. In the next section, it will be examined what the consequences of these contexts are for the (sub) factors’ development. When writing these future worlds one has to take into account that the state of the world does matter for what is and will be happening in the world of oil and gas industry as the history of the energy market clearly shows (Clarke 1990). In order to capture this influence, the future of the oil and gas industry is considered within the context of the international (geo)political and economic system (Correlje 2005).

6.3.1 Arena, scope, period and issue

The next step is to identify the basic principles for writing future worlds (Schwartz 1991; Oettinger 2003). The arena, scope, the period and the issue are stated in table 6.

<table>
<thead>
<tr>
<th>Arena</th>
<th>Scope</th>
<th>Period</th>
<th>Issue</th>
</tr>
</thead>
<tbody>
<tr>
<td>International political and economic system (Oil and gas industry)</td>
<td>‘New Great Game’: Struggle for Central Asian hydrocarbon resources</td>
<td>10 to 15 years</td>
<td>The attempt to realize the TCGP</td>
</tr>
<tr>
<td></td>
<td>The West, China, and Russia and Iran, host countries, TNOC’s, international institutions and its interests and behavior</td>
<td></td>
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</table>

Table 6: Framework for constructing future worlds

**Arena**
The arena in which the future worlds will operate in is the international (geo)political and economic system with particular emphasis on the oil and natural gas trade.

**Scope**
The scope encompasses the ‘New Great Game’: the struggle for hydrocarbon resources (natural gas) in the Caspian region. It comprises all the concerned actors and their interests and objectives.

**Period**
The plausibility of long-term speculations is small, so somewhere between ten to twenty years will likely to be sensible in most cases. For this particular case, the chosen period is 10 to 15 years.
**Issue**

The central issue is the attempt to realize the trans-Caspian gas pipeline project. The issue divides the concerned actors in two blocks: the West is in favor of the pipeline project including Turkey whereas Russia and Iran are against it. Kazakhstan and Turkmenistan are in the centre of this struggle, since they are the potential host countries. China, though, cannot be firmly allocated in these blocks as they are neither in favor nor against the project. Nevertheless, China is a formidable competitor and a fervent potential opponent and threat in case that it is vied for the same gas reserves.

**6.3.2 Axes of uncertainties**

The next step is to identify a bundle of uncertainties taking into account the international (geo)political and economic context of the conducted analyses, that have some commonality to a single spectrum, an axis of uncertainty. In this respect, the ‘old’ world of gas trade vs. the ‘new’ world of gas trade is taken as the reference point (see section 3.2), which is an integral part of this research. This refers to the notion that the ‘old’ world of gas trade is defined as that the state dominates the economy and the provision of gas and that international gas trade is backed by state-to-state agreements, such as bilateral investment treaties (BITs). The inverse of this notion is defined as a world in which the markets dominate the economy obviously and the role of the state has shifted to a provider and guarantor of the market institutions crucial for private companies to take risks and attain rewards from investing in rather costly gas infrastructure projects.

Taking the abovementioned into account, two axes of uncertainty are identified:

*Markets vs. States;* will the future bring about a world in which markets (private companies, IOCs) dominate the economy and secure states’ gas supply or demand? A world in which the state’s role is confined to providing the market institutions needed to create the context for private firms to take risk and invest in costly infrastructure projects. Or will the future’s economy and the provision of gas be dominated by the state through its NOCs (state-run national oil companies). A world in which domestic energy resources are viewed as a top national interest inducing the behavior to protect it from (foreign) IOCs. In this world, a state’s behavior ensued from geopolitical interests is more a rule than an exception.

*Unilateralism vs. Multilateralism;* will the future bring about an intensification of the multilateral approach in which multiple states cooperate through intergovernmental organizations (IGOs) on a given issue? Or will the world be a place where cooperation on given issues is secluded and is dominated by a doctrine which supports one sided action and bilateral agreements?

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75 Bilateral investment treaty is an agreement establishing the terms and conditions for private investment by nationals and companies of one state in the state of the other.

76 Natural gas pipeline projects are characterized by high capital costs

77 An IGO is an organization comprised primarily of sovereign states (referred to as member states). It can be divided into international, regional, ethnic, (cultural, historical and religious) and economic organizations.
Figure 11: Matrix of four different quadrants of uncertainty

The two axes of uncertainty are crossed as a result of which a matrix is constructed that allows one to define four different quadrants of uncertainty (see figure 11). It needs to be mentioned that other bundles of uncertainties that are expressed in a similar fashion are not excluded. Of course, hundreds of possible future worlds can be spun from combinations of the forces, but this will consume much time as fewer are better. It is also believed that these two axes represent the context of the international and (geo)political system in which the attempt to realize the trans-Caspian gas pipeline project is operating in eminently.

6.3.3 Future worlds

The next step is to outline the four future worlds. This will be done for each quadrant of the matrix (see figure 11).

However, before commencing with the future worlds, the expectation of the future gas trade in continental Europe deserves elaboration. First of all, it is expected that gas pipelines will remain the main transportation means in the future (IEA 2002). The market and corporations may take over the role from the state of investing capital in new gas projects within the ‘markets’ context, but the trade agreements will still be made on the basis of long-term contracts (bilateral agreements) with the producing countries. This assertion is based on the characteristics of natural gas, namely its physical properties. Its lower energy density (than oil) results in high capital costs for transport and storage. And where specificity of investment is high, long-term contracts will continue to remain the prevailing instrument (Dickel 2007). In addition, the expectation is that a few big suppliers will remain in the future (CIEP 2008) who fall outside of the EU’s direct leverage, namely Russia and Algeria (as opposed to Norway78). They will continue to view long-term contracts as the best instrument to secure their demand and thereby their capital-intensive investment.

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78 Although Norway is not a member of the European Union, it nevertheless has chosen to adopt much of the EU legislation due to its participation into the European Economic Area (EEA). It allows Norway to participate in the European single market without joining the EU. Additionally, it has chosen to opt into many of the Union's programmes, institutions and activities. In this respect, Norway already is and is expected to cooperate even more intensively with the European Union in the field of energy and security of energy supply in particular.
Hence, the four future worlds are the following:

1. A multilateral state dominated world
   It defines a world in which markets are subordinate to the states as the latter dominate the economy. It is a world that is increasingly polarizing and in which states do not refrain from executing a foreign policy with the aim of gaining political and ideological influence in other countries in order to protect their interests. In this respect, geopolitics has become an integral part of the international political system inducing the states’ strategic behaviour. Nevertheless, in this future world, states also do consider the effectiveness of cooperation through intergovernmental organizations (IGOs), but it is mainly a means through which an increasingly polarized world is pursuing and protecting their own strategic (geo)political and economic interests. In this respect, increasingly more intergovernmental organizations are established, but they are more regionally based in order to increase regional cooperation and to protect their strategic interests underlining the polarization of the world.
   As regards to the oil and gas industry, in this increasingly polarizing world in which geopolitical events are regularly occurring, the competition for the Caspian region’s natural resources is fierce partly brought about by the increasing concerns about energy security. The national oil corporations (NOCs) are the predominant type of transnational oil corporations, reflecting the state’s strategic (geo)political and economic interests. The NOCs, as is the case with the intergovernmental organizations, are a means of the state to pursue their own strategic interests. The NOCs provide the funding for the investment in gas projects. Nevertheless, the IGOs are called upon if needed to realize transnational gas projects (such as international financial institutions) and to secure supply or demand (international courts to settle disputes).

2. A unilateral state dominated world79
   In this future world, states dominate the economy and firms will become less international, but operate from a national perspective. The main difference with a multilateral state-dominated world though, is that the international political and economic system is in an advanced stadium with respect to polarization as the world is divided into ‘regions’ and ‘rival blocks of states’ on the basis of ideology, religion and (geo)political arguments. Political and military strategy and unilateralism (and bilateralism) divide the world up into EU, USA, Chinese, and Russian spheres of influence, which will increase the regional competition over goods and resources. National and international security concerns and conflicts are fuelling the distrust and the polarization between states and also hinder the international economic integration through the control over the flows of goods, persons and capital.
   With respect to the oil and gas industry, the competition for gas resources is culminating in this polarized world and so are the concerns for energy security. In this future world, it is relatively hard to secure supply and demand. To this end, states will have to forge strong bilateral partnerships and strict agreements (BITs and long-term contracts) in order to realize transnational gas projects. The state’s are wary of one another (distrustful) as such that the flexibility of the long-term contracts are adjusted downwards. Moreover, the NOCs are the predominant type of transnational oil corporations. The financing will be done by states and their NOCs and national/regional financial institutions.

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79 This is similar to Regions and Empires in Correlje (2006)
3. A multilateral market dominated world

A world in which the international economic system is characterized by integration of markets and increased support for liberalization. It assumes that there is an intensification of the social, cultural and economic globalization of markets. The states do not interfere in the market to the extent that they are facilitators for the market mechanisms as their task is to maintain good market conditions (regulation). There is a continuing and intensified cooperation in the international economic and political institutions. There is persisting support for the development of the multilateral system that governs international relations. Ideological, religious and political conflicts are to a large extent dealt with through the multilateral system of IGOs (such as the UN and NATO). Further liberalization creates the conditions to make the international flow of goods, persons and capital grow.

In this future world, IOCs will be the predominant type of transnational oil corporations. The markets and institutions context provide the IOCs and the concerned IGOs the suffice incentives to mobilize capital to invest in the expansion of gas production, transportation and distribution facilities. Moreover, under the growing concerns of energy security, it would be relatively easy to secure gas supply and demand.

4. A unilateral market dominated world

In this future world, markets dominate the economy but only in terms of an intensified regionalisation of markets. There has been a fierce return to ones roots and identity (cultural) preservation is prevalent. This has triggered states to adopt a more isolationist stance and to initiate bilateral non-economic cooperation based on (political) ideology, religion, and ethnic (linguistic and historical) ties as well. In addition, there has been an increase in the competition over these regional markets in the Caspian region, however, the states that have extensive non-economic ties have a head start. The increasingly xenophobic stance of the states has resulted into a diminishing of the cooperation in the political institutions. In this future world, it is limited to cooperation in the regionally based economic institutions alone.

Furthermore, the states do not interfere in the market to the extent that they are facilitators for the market mechanisms as their task is to maintain good market conditions.

With respect to the gas industry, the market and the national/regional financial institutions are providing incentives to invest in the expansion of gas production, transportation and distribution facilities. Both the IOCs as well as NOCs are operating in the regionally based markets. In awarding rights to transnational corporations (TNOCs) for exploration, production and construction of transportation and distribution pipelines, the states’ selection criteria is mainly identity based (nationality of the companies). Moreover, it would be easier to secure gas supply and demand (energy security) if there are common religious, ideological or ethnic ties between the states. Furthermore, competition for the Central Asian and Caucasus market(s) is fierce and more difficult for the West to obtain a foothold.

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80 This is similar to the Markets and Institutions context in Correlje (2006)
**6.4 Possible development of the factors in the future worlds**

In this section, the identified (sub) factors’ development will be determined in each of the four future worlds. In this respect, the obtained knowledge as a consequence of the categorization of the (sub) factors and the context of the future worlds allows one to derive the factors’ development into the future. In addition, also the obtained knowledge about how the evolution in the prioritization of energy security may influence the actors’ strategic behaviour will be taken into account when determining the factors’ possible future development.

The factor *degree of dependence on the interconnected gas project* brings about an interesting opportunity to dwell on alternative interconnected gas pipeline projects or offtake markets that could be put forth in the future and its possible influence on the trans-Caspian gas pipeline project. For example, one can consider that Turkey’s offtake market could become large enough in the future to absorb the amount of gas through the Caspian gas pipeline project. In addition, also the existing Turkey-Greece interconnector, with the inclusion of the future extension to Italy, could be a viable outlet for the TCGP. Nevertheless, this falls outside the scope of this study and is recommended for further research. This and other possibilities are discussed in section 7.5.

**1. A multilateral state dominated world**

The main characteristic of this future world is that it is increasingly polarizing in which the states are pursuing their strategic (geo)political and economic interests albeit through intergovernmental institutions and through their NOCs.

- **Investment climate**

  Regarding the investment climate, there is the impediment level of *Turkmenistan’s political structure*, which needs to be taken into account. In such an increasingly polarizing world, the main powers (China, EU, USA and Russia) would want to integrate the Caspian Sea region with their abundant energy resources into their energy system as much as possible through intergovernmental institutions and the realization of transnational energy projects. The increasing difficulty of securing energy supply will prevail over an unhealthy investment climate as the NOCs will be prepared to finance the gas project throughout the entire supply chain. In addition, the fiercer the competition, the more likely that the political structure’s impediment level will decline even further. Hence, given the abovementioned, it is believed that this particular (sub) factor will lose its impediment level in this particular future world. Nevertheless, in such a country where the President enjoys absolute power the fact remains that the country’s leader can *make or break* the project as this applies to every future world. Moreover, how *Turkmenistan* will develop under its new leader is hard to predict. First and foremost, it depends on the capabilities of the President himself. Furthermore, it also depends on the extent to which the future world allows the President to execute its multi-vector foreign policy approach. This will be very challenging in the ‘state dominated’ future worlds and in the ‘unilateral state dominated’ future world in particular.

In the ‘state dominated future worlds’, it will be very difficult for Kazakhstan to cut themselves somewhat looser from Russia’s influence (see section 4.6.3 for the extensive ties between the countries), which will make it hard for the West to include Kazakhstan into the trans-Caspian gas pipeline project.

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81 The fierceness of the competition will increase when more reliable information is released about the capacity of the Turkmen Yoloten and Osman gas fields.
Kazakhstan’s succession of its leader concerns an internal issue which is independent of the future world it operates in. The only meaningful assertion, nevertheless, is that internal turmoil was expected after Turkmen president Niyazov’s death as well, but this has not occurred. Naturally, nothing conclusive can be said before figuring out the extent to which the two counties are comparable (falls outside the scope of the study), but it does raise questions about the widely expected development in Kazakhstan in case a succession of its leader occurs. The same reasoning as asserted for Turkmenistan applies to Kazakhstan’s political structure as well. The difference is that Kazakhstan has already established a somewhat better investment climate. Assuming that the diversification of Kazakhstan’s economy will remain poor as there are strong signals that it will (see section 5.4.3 and 5.4.4), the state of the oil prices (cyclical phenomenon) can have a detrimental effect on its political and domestic stability and thus on its investment climate. However, in this increasingly polarizing world, energy security has become a priority and a healthy investment climate of the host country is becoming less important for the investors (states and their NOCs). Hence, a sharp decline of oil prices, although being a threat to the investment climate of the host countries, may lose a substantial part of its impediment level in the ‘state dominated’ future worlds.

- Transit risk

In the ‘state dominated’ future worlds where the competition for natural resources is getting fiercer and securing the supply of gas is getting more difficult, Turkey is not expected to pose demands (to import cheaper gas) which could delay the construction of the TCGP project.

That Turkmenistan aims to exploit its natural resources by diversifying its gas exports and that Azerbaijan aims to increase its value to the West by becoming a transit conduit is beyond dispute. The question is whether this will be sustained in this particular future world. Progress in the bilateral relations with Azerbaijan and Turkmenistan depends on the political willingness of the concerned countries and their leaders as well as on the context of the world. In the ‘state dominated’ future worlds, improving bilateral relations may be difficult depending on the extent to which both countries have sided itself to the developing spheres of influence. The ‘multilateral state dominated’ context provides some maneuvering room for the concerned countries though. It is believed that Turkmenistan in particular in comparison to Azerbaijan will have difficulties to sustain its multi-vector approach. This is explained by the expectation that Russia’s strategic appetite for Central Asian gas and its goal to retain its supremacy in the near-abroad will be sustained and even instigated in this particular future world (see geopolitics below) making it hard for Turkmenistan to resist Russia’s increasing economic and political power. Azerbaijan on the other hand, given its current close associations with the West and the expectation that this will be sustained at the least, is expected to have a higher endurance level against Russian advances.

- Geopolitics

With respect to Russia, it is asserted that all the future worlds allow for re-integration of Central Asia into the Russian energy system (Amineh 2003). Nevertheless, this is conditioned by its economic recovery and its ability to retain its supremacy in the world. Russia’s actions to bind Central Asian gas will reside in both the ‘state dominated’ future worlds as well as the ‘market dominated’ worlds. This assertion is based on Russia’s Eurasianism approach shaping its national identity and generating its main objective; to retain its supremacy in the region (near-abroad) and in the world by means of their hydrocarbon energy resources. In the ‘state dominated’ future worlds, however, geopolitically induced interests play a far greater role taking into account the increasingly polarizing world.
Moreover, in the second phase the Central Asian gas has gained in strategic importance for Russia as it is increasingly being used to compensate the decreasing domestic production while at the same time the demand is growing. It is expected that Russia, especially in the state dominated world will continue to resist opening up their domestic energy market for foreign investors. The *unresolved legal status of the Caspian Sea* in this context will most likely stay unresolved - as the categorization of the factors has shown - given the fact that the underlying economic and especially (geo)political arguments for Russia’s stance would be sustained and nurtured in this future world. This also applies for the *ecological objections* shown by Russia as it is believed that this will persist in this context.

As long as the U.S. sanctions against Iran continue, crippling Iran’s capabilities to turn its economic resources into power, and the TCGP is regarded as a pipeline to by pass Iran - depending upon its relations with the West - it will continue to oppose it. In an increasingly polarizing world, there is a high probability that the relations with the West will stay the same. Hence, the *ecological objections* shown by Iran is likely to continue in this future world. Furthermore, in a world where the economic and geopolitical interests determine the actor’s strategic behaviour, the *legal status of the Caspian Sea* from the perspective of Iran will stay unresolved.

*China’s* growing economic (and political) power (Shenkar 2004) needs to be taken into account in every future world. Its obsession with security of supply and the strategy being implemented to achieve it makes it a formidable competitor for the other actors vying for the Caspian region’s resources. Its growing economic and political power combined with its geographic advantageous position in the light of the objective of the host countries to diversify their export sources will make it a formidable competitor in the “New Great Game” in every future world. Moreover, its main advantage in relation to the West in the light of the relations with Russia is that its participation in the ‘New Great Game’ is tolerated by the latter. China is therefore considered as one of the main impeding and robust (sub) factors in the future.

With respect to Turkey, it can be asserted that as long as its quest for securing its gas supplies proceeds and the pursuit to become one of the main gas arteries for the European Union keeps up, Turkey will continue to support the TCGP. Moreover, Turkey’s multi-dimensional foreign policy strategy may become difficult to sustain in both the increasingly polarizing ‘state dominated’ worlds. This would endanger its *neutral, diplomatic* status. In addition, there are uncertainties regarding Turkey’s future development given its volatile political and domestic stability. Nevertheless, if Turkey’s internal development and its road to full membership of the EU proceeds positively, it is expected that Turkey will continue to develop its multi-dimensional foreign policy strategy.

In both the ‘state dominated’ future worlds, in the light of the increasingly polarizing world and the increasing concerns about energy security, it is expected that the *United States* will proactively re-enter the struggle for the Caspian hydrocarbon resources making use of its determining power in (energy) security policy to attempt to realize the TCGP. Its participation will only increase the fierceness of the competition and augment the determining influence of geopolitics as a factor. In this particular future world, though, it will choose cooperation and a multilateral approach (with EU, Turkey etc. and through IGOs) when engaging the ‘New Great Game’.
With respect to *EU’s aversion to ‘political investments’*, it can be asserted that in this particular future world the EU is strongly compelled to re-examine its stance on this issue. Nevertheless, there exists some doubt about whether the EU shall internalize these practices, given the *multilateral* characteristic of the future world and because it opposes its ideational structure. Therefore, EU’s aversion to political investments can turn out to be one of the main bottlenecks in this future world. In this future world the predominant source of financing comes from the NOCs and the IGO’s. The latter’s participation depends to a large extent on the political willingness of the EU member states (European parliament) and if that is not the case the realization of the TCGP could come into danger.

*Physical access to gas fields* will become less important in this future world, considering the fierceness in the competition over gas resources and the increasing concerns over energy security.

It can be said that this future world encompasses a proactive use of intergovernmental organizations including the *participation of (inter)national financial institutions*. Hence, the TCGP will not fail on account of this particular (sub) factor.

2. A unilateral state dominated world

The main difference with the previous future world is that this world is in an advanced stadium concerning the polarization as it is divided into regions and rivals of blocks in which one-sided action and bilateral agreements are the order of the day. In this respect, only the noteworthy differences with the previous future world will be described in order to prevent repetition as for the rest the (sub) factors’ development can be expected to occur in the same fashion but within an intensified polarized world.

- **Investment climate**
  See ‘multilateral state dominated’ world.

- **Transit risk**
  External encouragement of the bilateral relations between Azerbaijan and Turkmenistan is less effective given the sharp division of the world. Both Azerbaijan and Turkmenistan will be forced to choose a side. Considering the current orientation of the countries (Azerbaijan is West oriented and Turkmenistan is very much isolated) this would mean that there is a possibility that both countries may choose for different sides, diminishing the chances that the TCGP will be realized. In addition, in such a world, unilateral action by Azerbaijan and Turkmenistan to implement the TCGP ignoring the unresolved legal status of the Caspian Sea will be less likely considering the harsh unilateral retaliation it may induce from the other concerned actors/blocks (Russia in particular). Moreover, this polarized world leaves no maneuver room for the President implement a well balanced multi-vector foreign policy approach.

- **Geopolitics**
  In this particular future world, in case of conflict in the Persian Gulf, *Russia* would want to secure the stability of its borders and adjacent states by integrating the area (Correlje 2005). The Russian induced impediments will continue and most likely grow even stronger considering that Russia will relatively easily adapt to this world given its experience as a former empire. Furthermore, its historically grown strong ties with the Caspian region provides it with a big lead start. However, again this depends on its ability to retain its
supremacy in the world as a re-emerging global power. Hence, neutralizing Russia’s growing power in the Caspian region will become a fierce challenge for the proponents of the TCGP.

In this particular future world, China is one of the spheres of influence making it a strong competitor and a potential strong impediment to the TCGP. Competing against China for the Caspian resources will be a daunting challenge in this future world.

Turkey’s mediator role’s effectiveness is highly challenged in this future world. Its multi-dimensional foreign policy strategy is even more difficult to sustain as Turkey will be compelled to choose a side thereby losing its neutral status. Turkey’s choice could very well be the cause for one of the concerned actors to withdraw its support for Turkey’s mediation effort.

In this particular context, the U.S. will unilaterally (or bilaterally) attempt to realize the trans-Caspian gas pipeline project underlining the culminating geopolitical rivalry in this future world.

The little doubt that existed in the first future world about that the EU would come to terms with doing political investments, is taken away in this future world. The EU has no choice than to internalize the international political and economic system, but the adaptation process will not be easy, given that the EU is firmly embedded in the multilateral, liberal approach (Correlje 2005).

Physical access to gas fields will become irrelevant in this future world, considering the culminating fierceness in the competition over gas resources as well as the concerns over energy security.

The national or regional financial institutions could play an important role in providing funds for the large gas infrastructure projects in this future world but if they are weakened and they are not able to assume the role properly, it is up to the states and their NOC’s to provide funds.

3. A multilateral market dominated world

This future world is characterized by an integration of markets and increased support for liberalization. There is an intensification of the social, cultural and economic globalization of markets in which there is an intensified cooperation in the intergovernmental organizations.

- Investment climate

As free trade and the role of markets (IOCs) increase in significance, so will the investment climate of a producer country. Hence, Turkmenistan’s (and Kazakhstan’s) political structure’s impact on their investment climate is highly relevant in this context. In the ‘market dominated’ future worlds, there is a higher probability that Turkmenistan will integrate more in the global or regional markets as it provides the right context to implement a successful multi-vector foreign policy approach. This would result into efforts to improve their investment climate. Nevertheless, this depends highly on the President himself as he controls the direction to which Turkmenistan is heading.

Considering that this context provides the ideal context to implement a multi-vector foreign policy approach, the potential contributing influence of Turkmenistan’s new leader will be sustained and may even increase in this future world.
In this particular future world, Kazakhstan will have more manoeuvre room when it comes to Russia’s influence considering that it is believed that Kazakhstan will integrate deeper in the global economy as well as the international economic and political institutions. The political structure of Kazakhstan in the future is hard to predict, but given its integration into the global economy and the international institutions, it is believed that this will diminish the risks of the political structure’s (President’s autocratic power) impact on the investment climate. The state of the oil prices is considered a risk to its investment climate and given the priority that is given to a healthy market conditions in this future world it could form an important impediment to the inclusion of Kazakhstan into the TCGP project.

- Transit risk

In a world where it would be easier to secure the supply of gas, Turkey would have a weaker negotiation position since alternative gas pipeline routes would be deployed, at least in theory. The fact remains, however, that Turkey is the most commercially viable route for transporting Central Asian gas to the European markets (CI 2005). Nevertheless, it is expected that in this future world Turkey will become deeper integrated with the European Union especially in ideological and institutional terms, in the light of its pursuit to join it, which would restrain Turkey from throwing up such a demand to import cheaper gas.

The normalization of the relationship between Azerbaijan and Turkmenistan will gain momentum in the ‘market dominated’ future worlds apart from the political willingness of the respective leaders of the countries. These two countries are not subdued to external (geo)political pressure and harsh retaliation as it is the case in a ‘state dominated’ world. Therefore the bilateral implementation of the TCGP without taking into account the legal status of the Caspian Sea is more likely than in the ‘state dominated’ future worlds.

- Geopolitics

Also this future world allows the re-integration of the Caspian Sea region into the Russian energy system (Amineh 2003). In this world, Russia’s efforts to re-integrate the Caspian region depends on its emancipation and economic recovery (Correlje 2005). Furthermore, in this context Russia will become broader and deeper integrated in the EU market and probably more open towards cooperation in the economic field. In this context, a clear-cut resolution on the issue of the legal status of the Caspian Sea will largely depend on finding a compromise based on the economic interests of the littoral states as opposed to geopolitically induced arguments in the ‘state dominated’ future worlds. Hence, the likelihood that the legal status of the Caspian Sea will be resolved increases in this future world, but it will nevertheless remain complicated given the economic interests of the Caspian littoral states and especially Iran (see section 4.6.6). The ecological objections would lose its driving force in this future world given that strategic behaviour is predominantly induced by economic interests as opposed to geopolitics. In this respect, it would probably lose its most powerful proponent as well, namely Russia. Russia’s actions to bind Central Asian gas will continue as it is, but based upon economic arguments in the light of the increasing strategic importance of this region’s natural gas for Russia.

In this future world, depending upon the relations with the West, it is expected that Iran bears the highest risk to become the most impeding actor in finding a resolution on the legal status of the Caspian Sea given its economic interests. Furthermore, the ecological objections by
Iran will continue also depending on its relations with the West. Nevertheless, its impeding power with respect to these (sub) factors is conditional upon Russia’s backing. With respect to the legal status, Iran would be the only actor in disagreement as it would be under great pressure from the other littoral states and especially Russia to change its position. Furthermore, the ecological objection will lose its impeding influence when Russia would stop supporting it.

*China* will continue to integrate the Caspian region into their energy system. Although their current security of supply policy fits the ‘state dominated’ future worlds and the ‘unilateral state dominated’ one in particular better, it is believed that the ability to effectively secure their energy supply will be even larger in this particular context. This way they can invest without fully participating in the competitively strained international system through locally specific investments (Horsnell 2000).

Turkey’s multi-dimensional foreign policy strategy will be thriving in this future world. Hence, *Turkey’s initiative to mediate* has no limitations and its contributing effect may be decisive in normalizing the relations between Turkmenistan and Azerbaijan.

In this future world, the United States of America would stimulate the Central Asian and Caucasus countries to establish stable political and economic institutions with the aim of reinforcing their investment climate in the light of its energy security policy. In general, it would be instrumental in creating and maintaining open markets in which various actors would be willing to invest (Correlje 2005). This would pave the way for their IOCs to invest in the Caspian region’s hydrocarbon sector. It is believed that especially in this future world the U.S. engagement in the Caspian region has a higher probability to pay off.

EU’s aversion of political investments may lose its impeding influence in this context, since the markets and institutions (multilateral and liberal) context would provide the IOCs with funding to invest in the trans-Caspian gas pipeline project. Moreover, the EU is not unfamiliar with this context as it will not have a difficult time adapting to it. Therefore, it is believed that this future world provides the right conditions for the EU to become a strong competitor in the ‘New Great Game’.

Physical access to gas fields is regarded a precondition in such a context as the energy market is dominated by IOCs and as it is an effective way for this actor to decrease the risks of financing a major infrastructural project.

This future world entails a shift to a world in which the financing is increasingly done by private investors (IOCs) making the actual participation of (inter)national financial institutions less likely, while its participation may prove to be necessary in this future world given the potentially bad investment climate of the host countries (Turkmenistan in particular) and uncertainty about access to gas fields.

4. A unilateral market dominated world

This future world is characterized by a market dominated economy, but in which institutionalization and globalization of markets have resulted into a fierce return to the roots and identity preservation by states. Non-economic bilateral cooperation occurs only between states when there exists common ideological, religious, ethnic and political ties. Again, only the differences with the multilateral market dominated future world will be described in order
to prevent repetition as for the rest the (sub) factors’ development can be expected to occur in the same fashion.

- Investment climate

It is believed that the ‘market dominated’ world will provide incentives for Turkmenistan to improve its investment climate. If this translates into changing its political structure is hard to predict given the identity based characteristic of this future world. However, considering the disadvantageous position of the West in relation to Russia in particular, the investment climate will come to play a less important role in this future world as compared to the ‘multilateral market dominated’ world. This applies to Kazakhstan’s political structure as well.

The regionalization of markets and the lack of international political and economic institutions in this future world does make Russia’s leverage over Kazakhstan an issue to consider compared to the ‘multilateral market dominated’ world.

The potential impact of the fluctuation of oil prices on Kazakhstan’s investment climate will remain the same. Nevertheless, considering that in this future world the West will have it more difficult to gain a foothold in the Central Asian gas market compared to the multilateral market dominated world, the investment climate’s impeding power may become less important.

- Transit risk

Turkey’s geostrategic importance would gain a boost in this future world, which may instigate the desire to pose a demand to import relatively cheaper gas. Nevertheless, when taking into account its deepening integration with the European Union this would not be without any resistance.

The normalization of the relations between Azerbaijan and Turkmenistan gains a boost in this future world apart from the strengthening economic ties as both countries are also ethnically, culturally and linguistically related.

- Geopolitics

In this world, Russia will become broader and deeper integrated in the EU market, however, this relationship is limited to the economic field. Russia’s advantageous geographic position and its historical (and linguistic) relations with the Central Asian countries provide it with an important vantage to re-integrate the Caspian region into its energy system in relation to the EU and the other actors. Therefore, Russia’s actions to bind Central Asian gas, will in this future world be more effective taking into account the world’s identity based preference when selecting corporations.

In this future world, Iran will be broader and deeper integrated economically with their neighbours in the Middle East, Central Asia and the Caucasus as well as Turkey. As for the legal status of the Caspian Sea, it is expected that Iran bears the highest risk to become the most impeding actor in finding a resolution given its economic interests but this is asserted to be limited since it would come under great pressure from the other littoral states and especially Russia’s influence with which it has strategically important relations.

China’s energy security policy to integrate the Caspian region into its energy system will effectively continue in this context. Its growing economic and political power will not be resisted so easily. In addition, its geographic advantageous position adjacent to Central Asia in the light of the regionalisation of markets and the objective of the host countries to
diversify their export sources will continue to make it a formidable competitor in the “New Great Game”.

This future world provides the right conditions for Turkey’s multi-dimensional foreign policy strategy to be effective considering on the one hand its common religious, historical and ethnic ties with the Middle East and Central Asia and the Caucasus and on the other the deep political and institutional integration in the European Union in the light of its pursuit to join the EU. Turkey’s role as a mediator gains in effectiveness, considering their ethnic, linguistic and religious ties with the host countries. In this future world, Turkey would even become the key player for the West to bind the Turkmen and Kazakh gas to deliver to the European markets.

In this context, the U.S. will have it very difficult to gain a foothold in the Central Asian and Caucasus energy markets given its identity based characteristic of rising regional markets. As a result, the U.S. and their IOCs increasingly will have to rely on their economic power and competitive technological advancements to enter into these energy markets.

The EU would have to reconsider its stance with respect to ‘doing political investments’ considering their disadvantageous position in relation to Russia and China in the competition over the Central Asian regional market. In other words, there is a high possibility that this (sub) factor will turn out to be a crucial impediment in this future world.

Physical access to gas fields may loose some of its influence in such a context as the West and their TNOCs have a disadvantageous position in this future world in relation to China and Russia.

In this future world, the participation of national or regional financial institutions is more likely. Given the potentially unhealthy investment climate of the host countries, its participation could even be classified as potentially necessary.
6.5 Conclusions

The moment has come to ponder about the results. One has to conclude that the ‘market dominated’ future worlds provide the best conditions for the trans-Caspian gas pipeline to become reality. Although the competition in the ‘New Great Game’ will reside in both the ‘market’ and the ‘state dominated’ future worlds, the driving force and the means with which the competition for the Central Asian energy resources is pursued is different. In the ‘state dominated’ worlds where regionalization and rivals of blocks are the state of the world and energy security concerns are culminating, nations are wary of each other as a result of which the nations employ (geo)political, ideological and military strategy to pursue their energy security interests. The ‘market dominated’ worlds, on the other hand, provide a breath of fresh air as competition for the Central Asian resources and the pursuit to secure energy supply or demand is based upon a more or less level playing field and liberalization of markets, particularly in the ‘multilateral market dominated’ world.

The ‘market dominated’ future worlds provide sufficient manoeuvre room for Azerbaijan and Turkmenistan to normalize their bilateral ties (precondition) on the basis of economic interests as they are not subject to geopolitically induced pressure by Russia. The same also applies to Kazakhstan’s situation with respect to Russia’s influence. Kazakhstan will have more manoeuvre room when it comes to decreasing Russia’s influence considering that will have a higher chance to integrate more in the global economy as well as in the international economic and political institutions. Moreover, in the ‘multilateral market dominated’ world the United States’ participation in the ‘New Great Game’ would occur on the basis of a multilateral approach with the aim of reinforcing the region’s investment climate. It is believed that especially in this future world the U.S. engagement in the Caspian region has a higher probability to pay off with respect to the TCGP project. On the other hand, it is believed that China’s ability to effectively secure their energy supply is even larger in the ‘multilateral market dominated’ world, since then they can invest without fully participating in the competitively strained international system via locally specific investments. Nevertheless, the competition occurs in such a context to which the European Union is not unfamiliar with increasing the chances that it will stand a good chance against China. Although the West would be experiencing difficulties to gain a foothold in the Central Asian market in the ‘unilateral market dominated’ world, it might have a trump card which they can employ, namely Turkey. Considering its common religious, historical and ethnic ties with the Middle East, Central Asia and the Caucasus and on the other side its potentially intensifying political and institutional integration in the European Union in the light of its pursuit to join the EU, Turkey might become the key player for the West to bind the Turkmen and Kazakh gas to deliver to the European markets.
7. Conclusions

This dissertation has sought to explain what the main factors are that may contribute to the advancement or impediment of the ongoing second attempt to realize the trans-Caspian gas pipeline project. To this end, it has utilized the Case Study Protocol as provided in Hayes (2004). Nevertheless, it is detected that this Protocol requires modifications as regards its content but also with respect to the way it is applied in order to make it suitable to research this particular gas pipeline project.

The first chapter of this dissertation introduces the various issues that surround this particular project such as the various involved actors and the geopolitical characteristics that the Caspian region brings along. It seeks to provide sufficient information about the main characteristics of the TCGP project. Turkey is introduced as the problem owner for which a detailed analysis needs to be conducted in order to find out what its main challenges are with respect to promoting the project’s realization.

Chapter 2 explicates the choice for the Case Study Protocol and its determined factors in relation to the more conventional techno-economic (and environmental) factors. The original Case Study Protocol lacks to take into account time and the evolution it brings along in the explanatory value of the factors as a result of which an adequate analytical framework is constructed. Moreover, the constructivist approach is selected as the most suitable approach within this framework to analyze the change in the explanatory value of the factors.

Chapter 3 encompasses a detailed outline of how the Case Study Protocol should be operationalized on the basis of literature research and plausible assumptions such as the characteristics about the geographic location from where the gas originates.

Consequently, the analysis of the failed first attempt is conducted in chapter 4 as a result of which the main factors are identified. Moreover, in this chapter assertions were made about the potential domestic and political instability that might arise in case of a sudden death of former Turkmen President Niyazov. But in chapter 5, which constitutes the second phase of the analysis (2001-present), it was identified that these assertions had not occurred as the succession developed smoothly. This development has changed the way in how the similar Kazakhstan case was viewed in the third phase. Moreover chapter 5 sought to use the identified factors in the previous chapter to investigate if and if so how and to which extent they have changed in terms of explanatory value. It also encompasses the identification of another factor, namely the interconnected gas pipeline project provided that the gas project in question has such a connection. Chapter 6, the third phase of the analysis, focuses on exploring various future worlds, which are expressed in various international political and economic systems by means of which it is reflected on the possible future development of the identified factors.

7.1 Summary of the main findings

In the analysis of the failed first attempt to realize the TCGP, it became clear that Turkmenistan’s bad investment climate and in particular the opaque and erratic behaviour of former president Niyazov (bad leadership) formed a severe impediment.

One of the severe blows to the first attempt was when Russia in cooperation with Turkey decided to implement the Blue Stream gas pipeline project (geopolitical factor). Given Turkey’s overestimation of its gas demand, the offtake capability of Turkey’s gas market to absorb the gas from both pipeline projects was intensely questioned endangering the commercial feasibility of the TCGP project. Turkey’s motives are hard to understand given the fact that the pipeline project would make it even more dependent on Russian gas. Nevertheless, it does mean a diversification of its gas routes especially considering that it
provides a direct connection to the source eliminating any transit risk and thereby increasing its security of supply. Above all, it is believed that pressure from domestic powerful corporations were the main cause of Turkey’s consent to the BSP.

Moreover, worth mentioning is that during the negotiations between the U.S., the international consortium and Turkmen president Niyazov an unforeseen discovery occurred; Azerbaijan found a huge gas field in their section of the Caspian Sea making it capable to deliver to Turkey on its own. Its original role as merely a transit country was supplemented all of a sudden by a host country role. Its energy security interests changed as a result, changing also its strategic behaviour. Consequently, taking into account that Azerbaijan is also further down the line, the Azeri President Aliyev demanded nearly 50% of the throughput of the pipeline capacity (transit risk and geopolitics). This paved the way for tough negotiations and harsh rhetoric deteriorating the bilateral relations.

Moreover, during these failing negotiations, Turkmen president Niyazov’s susceptibility to Russia’s overtures (investment climate / bad leadership) to further open up the northern connection made the proponents of the TCGP very anxious and was considered another severe blow to the attempt. It was believed that it would not leave enough gas for the TCGP in the light of the insecure and opaque data about the amount of gas available in the Turkmen gas wells. Although the U.S. was financially and politically supporting the TCGP in the beginning, the tough negotiations and Niyazov’s opaque behaviour therein was increasingly alienating Washington to the point of no return. This point came when the leading U.S. transnational oil corporation pulled back from the international consortium, which can be viewed as a decline of U.S. support. As a result, the U.S. redirected its time and effort to the South Caucasus gas pipeline project in order to at least some portion of the Eurasian energy corridor alive.

On top of these highly impeding events (factors), the issues such as the unresolved legal status of the Caspian Sea and the environmental objection by Russia and Iran (geopolitics) were just the right marginal impediments to give the attempt to realize the TCGP project a push towards failure.

Above all, it is believed that the death blow to the TCGP was the deteriorated bilateral relations between president Niyazov and Aliyev making this issue a precondition, which needs to be resolved before efforts to realize the TCGP can be restarted.

The second attempt to realize the TCGP is still ongoing and it cannot be analyzed with hindsight in a manner similar to the analysis of the failed first attempt. This is because the latter has a clear end whereas the second attempt is still in its early stages. In this respect, the proponents (host, transit and offtake countries) are awaiting the results of the techno-economic feasibility study before concrete steps can be taken with regard to forming a consortium and designing a financial scheme for the project. Nevertheless, some interesting developments have occurred as regards the identified factors in the failed first attempt. Berdymukhammedov have assumed the Presidency in Turkmenistan, signalling reforms in the field of energy exports in particular. He has announced a multi-vector foreign policy aiming to diversify Turkmen gas exports. In addition, the new Turkmen and Azeri President have been making good progress to restore their bilateral relations. In this respect, it is asserted that if these countries make sufficient progress in the delineation of their maritime borders, it would make the resolution on the legal issue of the Caspian Sea unnecessary. However, this is true to the extent that these countries are capable of ignoring Russia’s strong arm. For this to happen, Turkmenistan and Azerbaijan would need the support of another powerful actor, namely the United States of America.

The ongoing second attempt and the ‘New Great Game’ have also witnessed the entrance of new actors: the European Union and China. The former is the intended offtake market of the
TCGP whereas the latter is a strong competitor in the ‘New Great Game’. Whereas the EU has an aversion of doing political investments, China is pursuing an aggressive energy security and foreign policy to secure its oil and gas supplies. EU’s refraining attitude could very well become the cause for the failure of the TCGP or to be more precise for its outlet, the Nabucco gas project with which a strong interdependency exists. Moreover, also Turkey has thrown up the demand to import relatively cheaper gas with which the involved actors in the Nabucco project are having troubles with to say the least. China on the other hand, has no problem whatsoever with providing state funding to finance the entire capital investment needed to realize the oil and gas pipeline projects gaining a competitive edge over the rest of the actors in the ‘New Great Game’. Furthermore, Kazakhstan is included into the ongoing second attempt as a potential host country. Nevertheless, Kazakhstan’s extensive relations with Russia (historical, economic, political, ethnic and security ties) has made it wary of giving green light for joining the TCGP project at least for the time being. For now, it is awaiting the results of the techno-economic feasibility study.

Russia’s actions to bind Central Asian gas has persisted in the second phase and even intensified with the appointment of former president Putin, which is the current Prime Minister. The Central Asian gas even increased in strategic importance for Russia given the higher increase in domestic and external demand for Russian gas in relation to its supply capacity. Russia is seeking to compensate the discrepancy in its supply and demand levels with relatively cheap Central Asian gas. It aims to postpone the development of expensive domestic gas fields. Furthermore, its traditional instruments to block any trans-Caspian pipelines also persist in the ongoing second attempt; the legal status of the Caspian Sea and the environmental objection.

The United States has assumed a latent position so far with respect to the ongoing second attempt to realize the TCGP project. Nevertheless, this may change in the course of the attempt whereas this would increase the polarization and intensify the competition in the ‘New Great Game’. Moreover, a new independent factor is identified, namely the interconnected gas pipeline project. For the TCGP it means that it will be linked to the Nabucco gas project, connecting minor Asia with the European mainland. The idea is to research the degree of interdependency between the two large gas infrastructure projects. To this end, it needs to be examined whether these gas projects have alternative interconnected gas pipeline projects. This factor is also relevant in the sense that alternative outlets could be put forward in the medium to long term, provided that the Nabucco project fails to materialize, which could be taken into account when determining the possible future development of this particular factor. In fact, it can be asserted that with respect to the TCGP for the time being (geo)political interests have prevailed over purely economic interests and the main transport routes have become instruments of political pressure.

All in all, for the time being it can be asserted that geopolitical factors and the bad investment climate of Turkmenistan in particular have prevailed over pure economic interests in the attempt to realize the trans-Caspian gas pipeline project. Nevertheless, there have been some positive developments such as the rapprochement between Azerbaijan and Turkmenistan and the positive preliminary results of the independent audit of the huge Yoloten and Osman gas fields in Turkmenistan that appears to be promising for the future to come.
7.2 The main challenges for Turkey

It will be explicated which factors Turkey should focus on when constructing its energy strategy regarding the attempt to realize the TCGP and why and what the main challenges are for Turkey in this respect. This will be done by means of the (Turkey specific) results in the first and second phase, the results of the third phase (possible future development of the factors) as well as the results of the interviews that are conducted with various scholars and energy experts will be used. To be more precise, the obtained Turkey specific results encompasses its advantageous ties, its competencies and weaknesses, its strategic position in the ‘New Great Game’ in relation to the other actors and its developing bilateral economic, political and diplomatic ties with the concerned actors.

In this respect, an answer will be provided to the second part of the main research question:

*As far as the main factors are concerned what are the main fields of interest for Turkey in order to effectively promote its realization?*

**Turkey’s multi-dimensional foreign strategy with emphasis on Central Asia**

Turkey’s multi-dimensional foreign strategy’s effectiveness differs per future world. In a ‘multilateral state dominated’ world its strategy may become difficult to sustain considering its increasingly polarizing context. In a ‘unilateral state dominated’ world this becomes even harder to say the least as Turkey will be compelled to choose a side thereby diminishing its neutral status and its efforts to effectively pursue a multi-dimensional, balanced foreign policy strategy. In a ‘multilateral market dominated’ future world on the other hand, its foreign policy strategy would be thriving as the context entails an intensification of the social, cultural and economic globalization of markets. A context in which polarization and aggressive protection of a state’s own strategic interests are non existent as Turkey can execute its strategy unhindered. In a ‘unilateral market dominated’ world, Turkey’s multi-dimensional foreign policy strategy would be effective as well considering on the one hand its common religious, historical and ethnic ties with the Middle East, Central Asia and the Caucasus and on the other potentially intensifying economic and institutional integration in the European Union in the light of its pursuit to join it in the future. In fact, in this world Turkey might become the key player for the West to bind the Turkmen and Kazakh gas to the European markets.

Moreover, Turkey’s main advantage regarding Central Asia is its existing cultural, linguistic and ethnic ties with the Turkic countries including Kazakhstan and Turkmenistan. Independent of whichever international political and economic system will exist in the future, Turkey should utilize these existing advantageous ties to augment its economic, political and cultural ties with the Turkic countries while at the same time continue to perceive these countries as states equal to Turkey. In addition, Turkey ought to stop walking down the path chosen from the time that these republics have proclaimed independence from the Soviet Union. According to Mete Göknel, a highly placed energy expert at the Eurasian Strategic Research Institute (ASAM) in Turkey, Turkey has been and still is sending its Presidents to these countries, which holds a more symbolic meaning. Although this is beneficial in terms of maintaining personal relations with the Turkic country’s Presidents and especially with Turkmenistan and Kazakhstan considering their autocratic system, this should be part of a more comprehensive and well designed strategy. To this end, the executive power of Turkey (the government and Prime Minister) ought to be actively involved as its participation is vital to reinforce tangible bilateral relations with other countries.

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82 (Interview with author, Ankara, 29-10-2008)
All in all, although it does not seem possible that Turkey can join the competition between the great powers for the hydrocarbon resources in the Caspian region, it still has a potential of affecting the future of the region. Turkey’s unique ties with the Turkic countries combined with its growing economic capacity, its regional and international prestige and developing economic and political relations with Russia do provide Turkey with an opportunity to play a greater role in the ‘New Great Game’. Nevertheless, the main challenge for Turkey in this regard is that it needs to show political willingness to prioritize its ambitions towards this region and design a realistic and pragmatic foreign policy strategy towards Central Asia.

Identity or market based foreign policy strategy

In the ‘state dominated’ future worlds an identity based foreign policy would be more effective given the polarization of the world on the basis of ideology, religion and political arguments. In a ‘multilateral market dominated’ world, however, the market based foreign policy strategy would be more effective given the globalization and integration of markets. Its main task and challenge is to be a provider of market institutions that create the context for private firms to take risks and attain awards from capital intensive investments in gas infrastructure projects. In a ‘unilateral market dominated’ world, the main challenge, however, is to design a foreign policy strategy, which combines both an identity and a market based strategy. This is due to the fact that in this future world the economy is market dominated, albeit regionalisation of markets is the norm and states select other states with which they want to cooperate on the basis of common religious, identity and ethnic ties.

Turkey’s NOCs and vertical integration

Turkey’s energy corporations suffer from a big weakness, namely the lack of vertical integrated energy firms. Turkey unmistakably misses this powerful instrument to gain more ground in the struggle for the Caspian hydrocarbon resources in the ‘New Great Game’ as Necdet Pamir83, a renowned energy expert in Turkey, has pointed out. Nevertheless, its effectiveness does differ per future world. In the ‘state dominated’ future worlds, the increasingly polarizing world in which securing energy supply and demand has become very hard has led the states to take their destiny in their own hands and pursue their energy security by means of their national oil corporations (NOCs). Hence, these future worlds would provide the NOCs with the ideal context to thrive in. In the ‘multilateral market dominated’ future world, however, the context encourages the international oil corporations (IOCs). In this context, the main challenge for NOCs in order to survive would be to maintain the competitive edge with IOCs. Not so much in terms of technology as this is increasingly being provided by service companies, but more in terms of managing large projects and combining the various technologies and managing risk (Stevens 2008). In the ‘unilateral market dominated’ future world, Turkey’s NOC would have a head start over the other IOCs and NOCs, considering its common ties with the Central Asian countries, but this very much depends on its ability to develop into a global player.

All things considered, it is needless to say that Turkey should encourage the merger between TPAO, the state-run Turkish petroleum corporation, and BOTAS, the state-run petroleum pipeline corporation, in order to play a more influential role through its NOCs.

Turkey’s demand to import relatively cheaper gas

In the ‘state dominated’ future worlds where the competition for natural resources is getting fiercer and securing the supply of gas is getting increasingly difficult, it would not be wise for Turkey’s energy security to pose demands that can endanger the realization of a gas

83 (Interview with author, Ankara, 29-10-2008)
infrastructure project running through its soil. In the ‘multilateral market dominated’ future world, it would be relatively easy to secure gas supply as a result of which Turkey’s negotiation position would be weaker as alternative gas infrastructure projects would be deployed, at least theoretically speaking. The fact remains, however, that Turkey is the most commercially viable route for transporting Central Asian gas to the European markets. Nevertheless, it is believed that in the light of Turkey’s pursuit to join the EU, Turkey will become deeper integrated in its institutions and political system, which would restrain Turkey from throwing up such a demand. In the ‘unilateral market dominated’ future world, Turkey’s geopolitical importance would gain value, which may encourage Turkey to pose this demand. However, considering Turkey’s deeper integration in the EU, this would not occur without any resistance.

Although the main problem of the Nabucco project is that it cannot find sufficient resources to fill the pipeline, Turkey’s firm disagreement over the pricing mechanism should not be taken lightly. The main challenge for Turkey in this respect is not to lose sight of the bigger picture, namely its objective to increase the security of its gas supply and to increase its strategic importance for the EU by becoming its fourth main natural gas artery.

Turkey’s mediator status

Recent efforts of Turkey regarding peacekeeping and mediation between nations have brought it regional and international prestige and augmented its neutral, diplomatic status. Turkey’s strategy to act as a potential mediator for solving bilateral issues between Azerbaijan and Turkmenistan and its endorsement by the concerned countries is viewed as an opportunity to help solve this issue. This issue is regarded a precondition for the realization of the TCGP project.

In the ‘state-dominated’ future worlds, the main challenge for Turkey is to continue its multi-dimensional foreign policy and sustain its neutral status in an increasingly polarizing world. In the ‘unilateral state-dominated’ future world in particular, this will be very difficult as the world, divided in regions and rivals of blocks, leaves little to no room whatsoever to maneuver as Turkey is forced to choose a side. As a result, it will have a difficult time to sustain its neutral, diplomatic status diminishing its chances in successfully mediating between the concerned actors. In the ‘market dominated’ future worlds, however, Turkey’s multi-dimensional foreign policy strategy will be thriving and thereby its diplomatic status. Especially in the ‘unilateral market dominated’ future world in which states prefer other states with common religious, ideological and ethnic ties, its mediator role gains in potential effectiveness considering its advantageous ties with the host countries.

In the meantime, Turkey should work on reinforcing relations with the Turkic countries, which will increase the effectiveness of its mediation efforts when the time comes. In the end, however, the normalization of the bilateral relations between Azerbaijan and Turkmenistan depends on their political willingness.

Neutralizing Russia’s perception about Turkey

Russia’s influence is clearly omnipresent in the ‘New Great Game’ as the failed first attempt has unmistakably shown. In the ongoing second attempt, the strategic importance of Central Asian gas for Russia has even grown as it is increasingly being used to replace the declining domestic production as the domestic and foreign demand has been rising. Russia can easily be classified as one of the main obstacles to the realization of the trans-Caspian gas pipeline project.

Russia’s impeding influence is the largest in the ‘state dominated’ future worlds where the fierceness of the competition for Caspian hydrocarbon resources and concerns over energy security will culminate. The main challenge for Turkey as regards this is to persuade Russia
that it is *not* a geopolitical rival. Turkey has an opportunity to reinforce and supplement EU’s strategy by attempting to change Russia’s image about Turkey, which is more psychological than it is realistic as Mustafa Kibaroglu 84, a professor of international relations at Bilkent University in Ankara, pointed out. The currently developing economic, political and diplomatic relations with Russia create a sound opportunity for Turkey in this respect. There have even been signals pointing out that its perception of Turkey is changing. According to Mustafa Kibaroglu, Turkey first of all needs to prove (quantitatively as much as possible) that it is simply not capable of becoming a rival to Russia as it does not posses the necessary (geo)political and economic power to diminish Russia’s leverage in general and with respect to the Turkic countries in particular. Secondly, the Turkish government including the President should put effort into changing the view in the highest Russian bureaucratic levels about Turkey. This comprehension should eventually seep to the lower bureaucratic levels in Russia which otherwise would never be realized 85. Above all, Russia also has to be ready to be convinced, which is a *precondition* in this regard.

### 7.3 The Case Study Protocol reviewed

This section entails providing a clear overview of both the main adjustments and supplements to the content of the Case Study Protocol as well as to the way it is applied to a dynamic gas infrastructure project. To this end, on the basis of the insights obtained in this dissertation the following research question ought to be answered:

*How should the Case Study Protocol as portrayed in Hayes (2004) be operationalized to analyze an ongoing (dynamic) gas infrastructure project?*

*A dynamic approach: analytical framework and constructivism*

The Case Study Protocol in its original static state is only suitable to research gas infrastructures that have already occurred, such as the failed first attempt (1997-2001). However, the continuation of the TCGP attempt on a later point in time necessitates a dynamic approach. At first, the analytical framework is outlined, which takes into account time and the evolution that it may bring about in the explanatory value of the factors (see figure 2). It views the first failed attempt as the first phase of which the results are used as input for the second phase (2001 till the present). In addition, also a third phase is included in which various future worlds are constructed on the basis of which it can be reflected on how these identified factors may develop into the future. Furthermore, also the obtained knowledge from the first two phases is used to help determine the possible future development of the factors.

Nevertheless, this is just a framework outlining the borders within which the gas project ought to be analyzed. The actual tool that is used to analyze the dynamic characteristics (evolution of the explanatory value of the factors over time) of such an ongoing project is the *constructivist* approach. Moreover, it endorses the construction of future international political and economic contexts as it is able to explain the development of the normative and ideational structures of the present international system as well as the social identities they have brought about (Reus-Smit 2005, pp. 201). An illustrative example that endorses the use of the constructivist approach is the case of the ‘Turkic World model’ or better said the failure of it. Turkey in the beginning of the nineties tried to build upon the strong cultural, linguistic and

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84 (Interview with author, Ankara, 30-10-2008)

85 For example Turkish trucks kept on hold on the Russian borders, even after the Russian foreign ministry’s proclamations of lifting the restrictions up as a result of Turkey’s decision to let through the US military ships into the Black Sea to medically assist Georgia in its conflict with Russia.
ethnic bonds with the new independent Turkic republics in the former Soviet Union. Turkey tried to apply a combination of material (mainly economic) and above all ideational (soft) power based upon alleged similar ethnic identities. Nevertheless, the long dominion that these republics had to endure from the Soviet Union had made their ideational structures more in line with the communist structure of the former Soviet Union and given the assertion that identities are social and produced through interactions (Barnett 2001), Turkey was not able to play a successful ethnic identity card in the beginning of the nineties. This was just one of the many aspects why the Turkic World model had failed. Furthermore, China and its growing concerns about energy security is another illustrative example. In the nineties, China did not play any role of importance in the ‘New Great Game’ in the Caspian region. It made up leeway in the 21st century and became a formidable competitor in the second phase. The driving force behind it is that China has come to view the necessity to protect its economic growth and the security of its energy supply as a top priority. China has come to view energy security as an integral part of its national interests, namely to survive and be secure as a nation. This is done by means of a resolute but subtle foreign (political dimension) and energy security policy (economic dimension).

Additionally, in the second phase of analyzing the trans-Caspian gas pipeline project, the Nabucco gas pipeline project is bound to deliver the Caspian gas to the European gas markets. As a result, the Nabucco and the trans-Caspian gas pipeline project are mutually dependent. Given the increasing concerns about energy security (see section 5.7.2), it is believed that more of these mutually dependent large gas pipeline projects will emerge in the future connecting various regions over vast distances, which brings along the identification of a new factor, namely ‘the interconnected gas pipeline project’. This is explained by the constructivist approach as the increasing concerns about energy security are a direct result of how some importing states (such as the European Union) have increasingly come to view dependency on some gas exporting countries as a threat among other aspects. Moreover, identifying the factors that influence the attempt to realize the concerned interconnected gas project ought to be considered outside the scope of the study since it would entail writing a dissertation. The idea is to research how the interdependency between the two large gas infrastructure projects is constructed. To this end, it needs to be researched whether these gas projects have alternative interconnected gas pipeline projects. In conclusion, this new factor must be incorporated into the original Case Study Protocol to increase its completeness and therefore its analytical strength.

**Adjustments to the Case Study Protocol**

First of all, it needs to be mentioned that as time elapses in the attempt to realize a gas infrastructure project, the number and type of involved actors may change as for example new ones can be added. This pertains to the direct actors, namely the host, transit, offtake countries and the transnational corporations but also the inclusion or exclusion of indirect actors (states), namely the global and regional powers. These actors and their interests ought to be considered when operationalizing the Case Study Protocol for a particular gas infrastructure project.

Regarding the factor investment climate, the notion that gas suppliers and buyers are threatened by variations in price have resulted into including the investigation of the potential influence of the liberalisation of the EU gas market on European bound gas pipeline projects. Furthermore, it ought to be investigated what the potential influence of the ‘resource curse’ – brought up during the Case Study Review Meeting (House 2003) - may be on the domestic governance (stability) of the host countries. In this respect, the question whether or not it applies to natural gas falls beyond the scope of the research. Nevertheless, considering that it
might have a substantial impact on a gas infrastructure project, it is suggested to analyze the host country’s potential vulnerability to the ‘resource curse’ accordingly over the time frame taken in the research. In addition, this argument is especially true for gas exporting countries whose primary energy export is oil, such as Kazakhstan.

Additionally, the expectation that existed about the Turkmen leader’s succession that it would bring about political and domestic instability is proven wrong in the second phase of the analysis. The succession has occurred smoothly and without any noteworthy complications. Although the extent to which other autocratically ruled country’s, such as Kazakhstan, are comparable to Turkmenistan falls outside the scope of this study, this development must be taken into account in the Case Study Protocol nevertheless when determining the possible future development of this particular (sub) factor.

Furthermore, it is noticed that in autocratically ruled countries, such as Turkmenistan and Kazakhstan, the leadership qualities of the person in question could be determinant for the success or failure of a gas infrastructure project. Consequently, this ought to be researched accordingly in the Case Study Protocol.

With respect to the **transit risk**, it ought to be kept in mind that even if the country did not use its transit position as a leverage to pursue its (economic or political) interests in the first attempt it does not necessarily mean that it will continue to refrain from using it. This might change depending on the ‘state’ of the world (international political and economic system) and the country’s internal situation (political structure). At the least the reputation of the transit country should be probed as to find out whether they have been involved in a gas project before and how they have acted. The driving forces behind their behaviour ought to be probed in order to assert about the future development.

Furthermore, the analysis of the first attempt to realize the TCGP has shown that unexpected developments can influence its course. As such, Azerbaijan discovered a huge gas field in their segment of the Caspian Sea as a result of which the attempt was greatly endangered. As the field was big enough to supply Turkey and since it was further down the line, Azerbaijan demanded a bold portion of the trans-Caspian gas pipeline paving the way for tough negotiations. As unexpected developments like these would normally be ignored, it is believed that given the long lead time of a dynamic gas infrastructure project and depending on the energy abundance ratio of the region in question, a transit country finding a gas field and its potential implications ought to be probed. Naturally, the implications are to a large extent dependent on the developed (economic, political and institutional) relations between the host and the transit country (geopolitical ties) but also on the state of the world. Therefore, the potential implications should be probed in the various future worlds.

Furthermore, regarding the **offtake market risk**, the role of the state in the offtake countries in creating gas demand and particularly in constructing gas grids ought to be considered (Hayes 2005). This becomes especially urgent when the offtake markets are considered ‘virgin markets’86 since the role of the state in creating gas demand and constructing gas grids is considered critical in these markets. Therefore it should be analyzed whether the concerned offtake market is a virgin market and if so what the role of the state is in order to asses the risk that the offtake country would not be able to absorb the gas.

Moreover, ‘**geopolitical relationship**’ ought to be incorporated into the Case Study Protocol as the study ‘**geopolitics**’. The analysis of the abovementioned *indirect* actors takes place in the geopolitics section of the Case Study Protocol. In this respect, in order to find out the actors’

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86 It is a market of which less than 10% of its primary energy supply is constituted of natural gas.
stance toward a gas project and explain their strategic behaviour the following question is asked: how will the realization of the ‘gas infrastructure project’ influence the ability of the relevant actors to achieve their objectives given the geopolitical context in which the project operates? As such energy security plays a prominent role in explaining the involved actors’ strategic behaviour and should be analyzed accordingly in this section.

Moreover, additional project specific and regional/country specific (sub) factors with a potentially relevant impact on this project should be analyzed in this section as well, since it is believed that it can be explained by geopolitics.

Furthermore, the ability to complete investments in cross-border infrastructures might also depend on the degree of cooperation between states. As regards this, bilateral and multilateral agreements should be probed and its effectiveness should be assessed. To this end, the effectiveness of the Energy Charter Treaty and its potential influence on creating investors’ confidence regarding the gas infrastructure project should be probed.

Moreover, in the time frame of the attempt to realize the gas infrastructure project, important events may have taken place (such as terrorist attacks on 9-11, regional wars) that might have influenced the geopolitical situation and the security and stability in the concerned region. This ought to be incorporated in the Case Study Protocol and investigated accordingly.

The historical case studies have shown that international institutions (intergovernmental organizations) did not play much of a role in the development of the gas infrastructure projects (Hayes 2005). This ought to be researched, nonetheless, considering that every case study is unique. However, it has been shown that international financial institutions (multilateral lending agencies) such as the World Bank or other private banks have had a profound impact on projects in cases that they have financed a substantial amount of the project costs, which otherwise would not be able to attract capital. This should be incorporated into the Case Study Protocol.

All things considered, the elapsed time and its influence is of absolute essence when analyzing a gas infrastructure project that is ongoing (dynamic) and should be incorporated accordingly. The development/changes in the explanatory value of the factors over time and its explanations ought to be determined by means of the constructed analytical framework and the constructivist approach. This approach and the framework in which the Case Study Protocol is casted is highly suitable for explaining the change in the actors’ interests and strategic behaviour and its influence on the explanatory value of the factors as well as the emergence of new (sub) factors. One of the main adjustments concerns broadening the original factor ‘geopolitical relationship’ to ‘geopolitics’ as a result of which a wide range of potential explanatory sub factors (regional/project specific factors, important events, actor analysis) can be researched in detail enhancing the completeness of the Protocol. In addition, also the emerged new factor ‘interconnected gas infrastructure project’ ought to be included as a fifth explaining factor in the Case Study Protocol. Off course, this factor’s influence is relevant to the extent that such an interconnected gas project exists. And last but certainly not least, the constructed analytical framework and the operationalized Case Study Protocol allows one to select any actor as a problem owner. For the problem owner, a specific analysis can be conducted in order to find out how it can effectively contribute to the advancement or impediment of the concerned ongoing gas infrastructure project.

7.4 Limitations and further research

Like all studies, this study has a number of limitations. These limitations are primarily related to the scope of the research. Although these limitations do not necessarily invalidate
the findings, it may inspire further research that could overcome it and bring forth further explanations about which (sub) factors to which extent influence the realization of gas infrastructure projects.

One of the main limitations of this study is that the operationalized Case Study Protocol and the constructed analytical framework was applied to only one specific gas project. As a result, nothing much can be said about the framework’s validity as it needs further testing by applying it to other dynamic gas infrastructure projects.

Another limitation of the operationalized Case Study Protocol is that due to scope restraints, no effort was undertaken to investigate whether the ‘resource curse’ also applies to natural gas. This ought to be investigated accordingly and included into the Protocol if relevant.

Moreover, it was decided not to include the Energy Charter Treaty as a potential main (sub) factor in the third phase of the analysis (see section 5.7.8). Nevertheless, it might be interesting to examine its possible contribution to creating a favourable investment climate in the various future worlds based on the assumption that the ECT will become successful in the future.

Additionally, it ought to be researched how the succession of the Turkmen leader occurred without any noteworthy complications against all the odds. As a result, these insights can be used to compare the Turkmen case with other autocratically ruled country’s, such as Kazakhstan, in order to assert with more validity about the potential influence of their leader’s succession.

Another important aspect regards the exclusion of the factor interconnected gas project (Nabucco gas project) in the 3rd phase of the analysis. This opens up interesting possibilities to speculate about future alternative outlets and its possible influence on Turkey and the trans-Caspian gas pipeline project. One of them being that Turkey can be assumed as the main offtake market in the future for the TCGP project given its projected gas demand excluding the necessity to connect it with the European markets and thereby reducing the associated transit and geopolitical risks. In addition, also the existing Turkey-Greece interconnector with the prospected extension to Italy could be a viable outlet for the TCGP. Furthermore, this could result into an acceleration of Turkey’s accession to the European Union in order to exclude Turkey as a potential transit risk. This particular aspect, the possible consequences that the realization of the TCGP may have on Turkey’s EU accession negotiations, was excluded from the scope of this study. But it could be interesting to take it into account in further research embroidering away on the conducted analyses and obtained results in this study.
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Interviews

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Peter van Leeuwen, 7-03-2008, The Hague (Netherlands)

Necdet Pamir, 28-10-2008, Ankara (Turkey)

Mete Göknel, 28-10-2008, Ankara (Turkey)

Mustafa Kibaroglu, 29-10-2008, Ankara (Turkey)
Glossary

Caspian region: all the littoral countries to the Caspian basin, which are Azerbaijan, Russia, Kazakhstan, Turkmenistan and Iran. Except for Iran and Russia, these countries are situated in both Central Asia and the Caucasus.

Turkic countries: these are, Turkey, Turkmenistan, Kazakhstan, Azerbaijan, Uzbekistan and Kyrgyzstan. These independent states are linked with each other by a common Turkic ethnic identity.

Intergovernmental Organization: An organization comprised primarily of sovereign states (referred to as member states). It can be divided into international, regional, ethnic (cultural, historical and religious) and economic organizations.

Bilateral Investment Treaty: is an agreement establishing the terms and conditions for private investment by nationals and companies of one state in the state of the other.
Appendix A Interview questions

- What is your opinion on Turkey’s stance/energy policy regarding the Trans-Caspian gas pipeline project? Idem for the Nabucco gas pipeline project? To what degree is the TCGP and the Nabucco part of Turkey’s energy policy on the one hand and Turkey’s wider (geo)political interests and objectives on the other? What is the role of Nabucco and TCGP in Turkey’s energy policy? In this respect, what is the connection between the two projects and how do you see that back in the energy policy of Turkey? How do you fit in Turkey’s tough stance on the pricing mechanism regarding the Nabucco gas pipeline? What is Turkey’s energy policy regarding becoming an energy hub for the EU (main energy transit country or a main energy trade hub)? How do you foresee it developing in the future?

- How do you assess Turkey’s foreign policy towards Central Asia and how do you foresee Turkey’s influence in the region developing in the future? What are the main obstacles for Turkey with respect to playing an influential role in the Central Asian region and if possible how could Turkey overcome this? Which strings does Turkey have at its disposal to increase their influence in the Central Asian region?

- What is needed to convince Turkmenistan and Kazakhstan to go into business with Turkey in the field of the TCGP? Idem for the West (EU and US)?

- What are according to you the main factors influencing (in an a positive and negative sense) the attempt to realize the TCGP?

Specific questions

- What is your view on the possible implications of the audit results of Turkmenistan’s gas reserves for the competition in the “New Great Game”? How should Turkey use this momentum to promote the realization of the TCGP? What are other opportunities for Turkey to promote the realization of the TCGP?

- How do you explain Turkey’s engagement with Iran to develop the South Pars gas fields in terms of their energy policy and strategic behaviour?

- How do you explain Turkey’s stance when it simultaneously supported the Blue Stream gas pipeline and the TCGP causing an impediment to the latter’s realization?
Appendix B The original Case Study Protocol

1. General Investment Climate within each Proposed Host Country and offtake and transit countries if relevant

Each case study should provide an overview of the broader investment climate of each of the host countries. This should include a description of political, security, economic, and legal contexts at time the project was proposed, as it changed during the construction of the project, and also relevant historical information.

Domestic Security and Political Context

The case study should first describe the level of political and constitutional stability within each of the host countries. Is there a fear of revolution or dramatic change in government that could result in expropriation? The discussion of the political context should also describe the form of government (e.g., totalitarian, democratic), the level of centralization of powers (e.g., centralized state, federal system), and the distribution of power in the political system (e.g., authority of the executive to make credible long-term decisions, shared powers between executive and legislative, role of judicial review).

Domestic Macro-Economic Context

A description of broader economic issues should first describe the macroeconomic situation in the host countries. What were the projected growth rates of the overall economies? What were the economic risks (exchange rate, uncertain growth prospects, etc.)? What were the projected needs for energy services in countries that would be served by the projects? How did the projects fit into the strategic energy plans of the governments, and to what degree were the governments actually able to conceive and implement strategic energy infrastructure plans?

“Rule of Law”

The case should discuss the development of the “rule of law” in the upstream, downstream, and transit countries (where relevant). Were commercial laws clear and evenly enforced; if not, how effective were traditional remedies for poor rule of law (e.g., corruption, joint ventures with politically connected local firms, joint ventures with politically powerful foreign entities)? Describe the historical track record on upholding contractual agreements and the role and independence of the judiciary in deciding disputes. Describe the adherence to international legal norms and the adherence to international arbitration where utilized prior to the proposal of this infrastructure project. Was corruption a significant problem at the time that the projects were proposed? The case should also discuss any regulations or policies concerning foreign investment—generally as well as particular rules governing investments in energy and infrastructure. What was the prior experience with private and foreign investment? What were the tax regimes for energy products and how were tax laws enforced? We ask these questions so that each case study examines the risks and opportunities for investors prior to undertaking of the projects and to uncover the interactions between government policies and various investors (non-governmental and governmental). These infrastructure investments are costly and “lumpy”—especially the first such project is risky and often entails (for the importing country) a substantial shift in the energy system, which is hard for entities other than the government to engineer. The factors related to “rule of law,” such as enforceability of contracts and the abilities of governments to implement long-term strategies, are important because costly infrastructures are prone to suffer the problem of the
“obsolescing bargain.” Once the capital is deployed the investor is in a poor position to assure that the contractual terms are met for the decades required to recoup the initial investment and secure a profit.

**Regulatory**

Each case should analyze the *ex ante* and status of regulation in upstream, downstream and transit markets (where relevant). Where did the market segments stand on the continuum from state run monopolies with allocation determined politically to a market open to private and foreign ownership and investment, with prices flexible for any particular project. Relevant information would include any laws governing the price and quantity of gas sales outside of the project in question. In India, for example, gas allocation is politically determined and the retail price of gas is capped by regulation, posing a challenging obstacle to any new gas import projects. Thus, *ceteris paribus*, an investor is likely to consider a project to India much differently than an export project to a country gas pricing is determined freely in the market.

The cases should also discuss proposed regulatory reforms, and historical and prospective progress in carrying out these reforms, as viewed from the investor at the time the projects were being proposed.

Right-of-way legislation in a host country is another important issue for infrastructure projects. Many countries do not have laws of eminent domain that facilitate the acquisition of land for project construction. Georgia, for example, changed its constitution to make the Baku-Tbilisi-Ceyhan oil and gas pipelines a project of “national interest,” thus making it feasible to acquire the local lands needed for the pipeline routes. Similarly, a proposed natural gas pipeline from Sakhalin to Japan has been stalled in part due to difficulties in acquiring land to build the spurs that would transport gas landed in Northern Japan to other points in the country.

Environmental legislation and laws concerning indigenous peoples and protected lands are also critical issues for siting, constructing, and operating a gas pipeline. The case should detail laws such as limitations on liability for infrastructure projects or specially protected local populations or lands. The case studies should explore any particular social and environmental problems that were deemed potential obstacles in the construction and operation of the projects. Where relevant, the case should describe the means proposed or actually employed to resolve these disputes. In some cases legislative changes may be required, as in the right-of-way issues discussed above. In other instances, negotiations with native groups or non-governmental organizations may be able to produce non-regulatory solutions to social and environmental conflicts.

2 **Transit Countries**

It ought to be explained how the number and type of transit countries affected the outcomes and whether particular routes were chosen to avoid certain transit countries or regions.

What were the expectations about transit fees for the pipeline? Do precedent transactions exist to benchmark costs and rents for the transit country? Is theft of gas during transit a concern? Theft may be a significant problem where gas is transported through an integrated network, complicating the ability to track actual flows of gas to specific customers. Such is the case in transit countries like Ukraine creating constant tensions between Moscow and Kiev.
3 Off-take market risk

Each case study should explain evolution of the off-take country’s gas market and examine the risk that the off-take market would be unable to absorb the quantity of gas supplied by the project. Were take-or-pay contracts or other arrangements used to reduce these risks, and with what effect?

In the market where the gas was to be sold: Who are the intended off-takers? What were the prices (level and volatility) of competing energy supplies, and what infrastructures already existed (or were expected) to deliver the gas? What were the growth prospects for gas demand and related infrastructures? Were there special factors (e.g., environmental, security) that caused decision makers or off-takers to favor or disfavor gas?

To some degree, price risk is merely the mirror of quantity risk, but in markets where the price of gas is regulated there are special risks associated with the system for regulating price. Where did the market segments stand on the continuum from state run monopolies with allocation determined politically to a market open to private and foreign ownership and investment, with prices flexible for any particular project and how did it effect the project?

4 Inter-governmental/Institutional Relationships between Proposed Host Countries

The ability to complete investments in cross-border infrastructures may also depend on how well host countries engaged in a particular project are able to cooperate on and manage collective issues. Thus this protocol seeks information in each project on the degree of integration of the host countries’ economies as well as institutions that may have been established to facilitate or manage trans-border issues—in particular, trans-border capital investments and trade.

Each study should probe the operation and effectiveness of these institutional relationships. It may be useful to detail the history of cross-border conflicts or collective action by the host countries and to explore the roles of institutions in resolving the conflicts. Measures of such activities include the number of joint-governmental working groups, commissions or inter-governmental treaties. The case study authors should be mindful that effective cooperation might not take place entirely through formal institutions. It is also important to review the expectations about the likely futures for cooperation by host countries. How, if at all, did those expectations influence or reflect the official foreign policy, security and social goals of the host country governments?

We ask these questions because the existence of effective institutions for collective action—and the expectation that such institutions will become more effective over time—should encourage investors (government and non-government) to build infrastructures that can yield benefits only if they are managed on a collective basis over a long period of time.
Appendix C The problem of the petro-state

The future prospects for Turkmenistan (and Kazakhstan) are expected to be more promising than the expectations for most of the post-Soviet states, due to the abundance of oil and gas reserves in these countries. Hydrocarbons have indeed claimed the bulk of the foreign and domestic investment. The investments and the returns are even expected to rise in the upcoming years. However, although Turkmenistan (and Kazakhstan) are starting to thrive from the success in the international oil arena, their domestic economies and political structures are beginning to show some of the classic negative side effects of becoming “petro-states” (Sabonis-Shelf 2005). A petro-state is defined as a nation that to an increasing extent is structured by their role as oil/gas exporters.

Most of the experts in the political economy of energy accept that the phenomenon of being an oil exporting state is inherently associated with certain pathological development tendencies, such as the lack of transparency, lack of separation of powers within the government, a remarkable lack of equitable distribution of wealth and power, high levels of state debt and a “permanent tendency toward rent seeking by state officials (Karl 1997).

In her book, The Paradox of Plenty: Oil Booms and Petro-States, Terry Lynn Karl notes that the capital deficient oil exporting states of Algeria, Indonesia, Iran, Nigeria and Venezuela evolved along the same lines after the oil booms of the 1970s. She shows that these nations have followed a common trajectory in which the policy environment first became “petrolized”, serving the interests of the oil industry, but not the larger state. These nations have increasingly relied upon the substitution of public spending for statecraft that caused the state capacity to become even weaker. In the final stage, oil booms actually had “pernicious effects”, resulting in economic decline and destabilization of the regimes. This image suggests that oil is a hidden curse rather than a blessing for a developing state.

The underlying reasons for this effect is widely discussed in the abovementioned book. Firstly, Karl notes that all her case states are “late developing” states, that were on the outside of the already established global trading system. These nations have experienced oil booms before having strong national identities or administrative structures. More important, these nations were dependent on revenues from export rather than from taxation. By taxing a commodity, rather than their people, the government fails to create a accountability link as the government spending tends not to become an issue for public consideration (Karl 1997). As a result, the state is largely free to construct a “no taxation, no representation” system of governance. The tendency exists that no coherent budgetary system is developed and the increasing dependence on oil revenues makes the state vulnerable for fluctuations in the oil price. Instead of constructing a coherent public bureaucracy (the origins of most government bureaucracies are in taxation), the petro-states tend to engage in uncontrolled public spending.

In times that the oil revenues are less than expected, the prospected oil revenues enables them to borrow. On the other hand in times of high revenues, the public perception that the high revenues should be beneficial for all often results to an extension of subsidies or taking on expensive projects which cannot be stopped when oil prices fall. In addition to this, as a result of the oil boom hyperinflation can occur, causing the state to go further into debt even when revenues are at their highest.

The limited capacity of an immature or weak state makes it vulnerable to the strongest interests in the state, namely the energy interests. With absent transparent democratic institutions, the oil interests become the only actors that are invited and listened to by the government to develop business policies and hence becomes the only non-state voice that the
government takes seriously. Over time, politicization of the industry is inevitable. With no strong policy measures in place to diversify the economy, oil has the tendency to outshine and surpass other industries and thus other sources of national revenue, pushing the oil exporting revenue further along the trajectory Karl described.
Appendix D Most defining events in the failed first attempt

Figure 12: Overview of the most defining events in the failed first attempt
The conclusion of this first phase, which covers the first attempt from 1997 till 2001, is drawn by stating and elaborating on the most defining events in a chronological order. It is believed that explaining the connection between the most defining events will effectively decrease complexity for a better comprehension of the impediment power of these factors. For an overview of these events see figure 5. In this figure, one can see that the events are separated in 4 sections or groups of actors. The first section on the outer left concerns Russia and Iran. They are placed together, since they both opposed the trans-Caspian gas pipeline project. The second section refers to Turkmenistan, Azerbaijan, Georgia, and Turkey as they are the countries that are directly involved in this project either as a host, transit or an offtake country respectively. The third section concerns only the United States, since they were the only global player actively promoting the trans-Caspian gas pipeline project. The fourth section on the outer right of the figure refers to the Transnational corporations (PSG international consortium) as they have the important task to draw a financial plan for this project.

The trans-Caspian gas pipeline project was conceived initially in 1997 by Bechtel Enterprises. Following this event, the first noteworthy event occurred in April 1998, when the U.S. Trade Development Agency (TDA) had awarded a $ 750,000 grant to Turkmenistan to prepare a feasibility study for piping Turkmen natural gas under the Caspian Sea to Baku and then on to Turkey (Alexander 1998). This states that the United States was involved in the trans-Caspian gas pipeline project from the very beginning. The granting of this sum of money coincides with the first visit of the Turkmen President Niyazov to the United States and follows several energy deals that the Turkmen government already had made with U.S. companies. The Clinton administration had been urging Turkmenistan to consider a different pipeline route other than the one that would pass Iran for transporting natural gas to Turkey. The subsequent noteworthy event occurred in June 1998, when the international consortium consisting of Amoco and a new pipeline joint venture owned by affiliates of General Electric Capital and Bechtel Enterprises, was established (Alexander 1998), marking serious progress in the first attempt to implement the gas pipeline. This consortium took charge of the engineering, design, procurement and construction of the TCGP.

Worth mentioning is the commencement of the border dispute between Azerbaijan and Turkmenistan. This occurred in February 1997 as they disagreed about the determinations of the fixup value for the middle line between the sectors of both countries in the Caspian Sea (Ogli 2000). Although Turkmenistan recognized the sectoral delimitation principle in the Caspian Sea, it insisted that the ‘Azeri’ and ‘Chirag’ fields belonged to Turkmenistan. This was the beginning of the deteriorations in the relations between the two states.

In May 1999, Turkey signed an intergovernmental agreement with Turkmenistan to supply 16 billion cubic meters of natural gas per year beginning from 2002 with the prospect of delivering an extra 14 bcm per year onwards to the European markets. This is marked as an event indicating that both countries are committed to implement this gas pipeline project. In August 1999, it became known that the U.S. Ex-Im Bank and the U.S. Overseas Private Investment Corporation (OPIC) will take an active part in the creation of a mechanism for financing the trans-Caspian gas pipeline project (Newsbase 2000). The announcement was made by the special advisor to the U.S. president for energy diplomacy, John Wolf, after his meeting with Turkmen President Niyazov. Wolf went to Turkmenistan to take part in the signing of three documents designed to implement and accelerate the project. To this end, the participation of the U.S. Ex-Im Bank and the U.S. OPIC can be ascribed to the strong U.S.

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87 The TDA is an independent agency that helps U.S. companies establish business in emerging markets.
government backing of this project. Subsequently, in November 1999, at the sidelines of the OSCE summit in Istanbul, the leaders of Turkey, Azerbaijan, Turkmenistan, Kazakhstan and Georgia signed a landmark deal on the transportation of the Central Asian and Caucasian oil and gas to western markets. This platform also provided the opportunity to deal with the border dispute between Turkmenistan and Azerbaijan. They jointly stated that the dispute on the fixup value of the middle line between the Caspian sectors of both states would not pose a hinder to the realization of the trans-Caspian gas pipeline.

In late November 1999, short after the OSCE summit in Istanbul, Russia and Iran jointly stated that they were against the U.S. backed plan for a trans-Caspian gas pipeline before all five littoral states have agreed on dividing the waterway. Azerbaijan in reply said that that it was up to the countries through which borders it will cross. Turkmenistan chose to remain silent as it is believed that they did not want to upset Russia, since they were still dependent on Russia for their only export route of natural gas and because a potential future gas deal with Russia was at stake. It is clear that both Russia and Iran would rather see a gas pipeline through their own territory in favour of their own geopolitical and economic interests. It is believed that this specific impediment factor has the potential to become one of the main bottlenecks if only this issue was to remain that needed to be resolved. It is believed that if necessary both countries would at least exert high diplomatic pressure with strong judicial backing of their statement to prevent the project from being implemented. Moreover, it needs to be mentioned that Iran in the past have threatened with their military gunboats leading to a withdraw of the Azerbaijani exploitation crew in a disputed area in the Caspian.

Almost a month after the OSCE summit in Istanbul, another controversy erupted over the trans-Caspian gas pipeline deal in December 1999. Aliyev, the President of Azerbaijan, after discovering a huge offshore gas field, demanded access to the TCGP, stating that it could no longer be considered only as a transit country. Aliyev demanded for half the capacity of the line, which dramatically changed the economics of the plan for Turkmenistan. A result, this paved the way for intense negotiations regarding the allocation of the volumes and effectively hampered progress on the TCGP. As the negotiations were failing, Niyazov in reply reiterated its claims over the concerned oil fields about which everyone was surprised, since they thought that this issue was solved during the OSCE summit in Istanbul. It did not stop here as after the mid-February 2000 stalemate, Niyazov turned to Russia as a way to pressure the U.S. developers to come up with new terms. Niyazov entered into talks with Russia’s Gazprom about raising its deliveries from 20 billion cubic meters to 50 billion cubic meters (see next passage). At the same time, Turkmenistan was also negotiating with Iran on an increase in sales from the Korpedze-Kurt-Kui gas pipeline to 13 billion cubic meters from about 2 billion a year. The Azerbaijani side countered as it declared that it was perfectly capable of proceeding on it’s own on the basis of the Shah-Deniz field discovery.

Another impediment to the TCGP project by the side of Russia and surprisingly also Turkey concerned the groundbreaking ceremony of the Blue Stream gas pipeline on the 10th of February 2000, which would transport Russian gas through a pipeline crossing the Black Sea to the Turkish market (Ögütçü 2001). It had steamed ahead if its competitor, the trans-Caspian gas pipeline. Given the prospected growth of the Turkish market, it was not able to absorb all the gas from both giant gas projects. This was just one of the many actions undertaken by Moscow to frustrate the construction of the TCGP. As abovementioned, Russia also seized the opportunity during failing negotiations between Azerbaijan and Turkmenistan by further opening the northern connection, arguing that a new Turkmen outlet is unnecessary. As a result of President Niyazov’s frustration at the lack of progress in this U.S.-backed plan to pump Turkmen natural gas to Turkey and its needs for urgent cash to improve its faltering
economy, Russia signed a deal with Niyazov in May 2000 by agreeing to supply vast volumes of gas to Russia over 30 years with supplies that could reach 50 bcm per year. Moreover, he had already pledged to supply the Turkish line with an eventual 30 bcm a year. Turkmenistan would be unable to meet that demand while at the same time pumping 50 bcm to Russia annually, since its production in 1999 was just 23 billion cubic meters. This severely hurt the trans-Caspian gas pipeline project in the sense that it negatively influenced the support and determination that the concerned actors had for the TCGP project. The concerned actors frankly were frustrated about the behaviour of Niyazov, who was not showing determination and commitment for the TCGP.

After the mid-February 2000 stalemate in Ashgabat in the negotiations between Azerbaijan and Turkmenistan regarding allocation of the volumes, the Turkmen side assumed the obligation to fine-tune the TCGP deal. It was anticipated that President Niyazov would undertake to work out those conditions with President Aliyev. To this end, Niyazov, who had visited Baku a few years before, now invited Aliyev to be his own guest in Ashgabat for a signature ceremony. Aliyev responded publicly that he would accept the invitation to Ashgabat for late April, only if the conditions of the deal were agreed before then. The Turkic summit in April 11-12 was to be the time for discussion on the allocation of the volumes. However, Niyazov did not show up making Aliyev furious, because such an attempt to pressure Azerbaijani side, without agreeing on the conditions of the contract before Aliyev’s trip to Turkmenistan later in April, would have put Aliyev in the role of supplicant going to Niyazov (Cutler 2003). This resulted in cancelling its visit to the signature ceremony in Turkmenistan in late April. Furthermore, Turkey abandoned its condition that it would require delivery of Azerbaijani gas through the TCGP only if Turkmen gas passes through it. It is believed that an element in Turkey’s decision was Niyazov’s reiteration of a large up-front payment, from which he earlier desisted at the Turkish President Demirel’s personal request during its visit in Turkmenistan in late March (Gültasli 2000). This meant that Azerbaijan now had the opportunity to realize its own project, namely the South Caucasus gas pipeline (SCP).

Meanwhile, the United States agreed to submit detailed financial proposals for the TCGP by the end of March 2000 in order to boost the troubled project’s viability. In late March of 2000, the PSG international consortium made a “last and final” offer as they had a dispute with Niyazov regarding the splitting of profits from the pipeline. The U.S.-led PSG International consortium offered improved financial terms in order to advance the project. However, Niyazov reiterated its demand of 500 million dollars upfront, which created frustration to the parties in the project (CEE 2001). Moreover, Niyazov failed to respond to the final offer and did not renew the consortium’s mandate (Lelyveld 2000). These events eventually caused Bechtel and General Electric companies to withdraw from the international consortium in June 2000. Shell, however, remained committed and took over the lead of the international consortium.

Meanwhile, Azerbaijan proceeded independently to realize the South Caucasus gas pipeline, is believed to be a retaliation on Turkmenistan’s refusal to give ground on the disputed oil fields. To this end, Azerbaijan secured a gas deal with Turkey in March 2001 (EIA 2002). Turkey signed a 15-year agreement with Azerbaijan to buy gas from the Shah-Deniz field from 2004. In March 2001, Russia and Iran jointly stated to be opposed to the trans-Caspian gas pipeline project on environmental grounds. Obviously this should be seen as a strategic manoeuvre as to undermine the progress on the project in view of their own geopolitical and economic interests. This manoeuvre came at an interesting moment, since Azerbaijan was making good
progress on the realization of its own project with the full support of all the directly concerned actors and the United States, while at the same time the trans-Caspian gas pipeline project was nearing its end.

In August 2001, Turkmenistan stepped up its claim on Caspian oil fields operated by Azerbaijan, following an unprecedented step taken by Turkmenistan to close its embassy in Baku, Azerbaijan. Turkmenistan flexed its military muscle to pressure Azerbaijan into handing over the two disputed oil fields. It has issued dark threats of 'unexpected consequences' if the Azeri leadership refused to agree to its demands, marking further deterioration of bilateral relations.

In September 2001, the presidents of Georgia and Azerbaijan signed a key agreement on transit rates for a planned natural gas pipeline from the Caspian Sea to Turkey. Negotiations on the rates lasted longer than planned, one of several delays on the proposed 1,000 km (625-mile) pipeline from the Shah-Deniz gas field through the Azerbaijani capital Baku and the Georgian capital Tbilisi to Erzurum in Turkey (APW 2001).

In October 2001, Azerbaijan declares that the TCGP will not be build. Officials at SOCAR, the Azerbaijani oil company, point out that the root cause of cancelling the TCGP is the ongoing bilateral issues between Azerbaijan and Turkmenistan and not so much the progress regarding the BTE gas pipeline project.
Appendix E Russia’s and Iran’s environmental objection examined

Russia and Iran both object to the trans-Caspian gas pipeline on environmental grounds (nCa 2007). Their joint position is that no pipelines should be built across the Caspian, ostensibly due to the fact that it would inflict serious environmental damage to the Caspian Seabed. They further declared that it cannot be implemented without prior discussion by all five Caspian nations (IHS 2007). This environmental damage includes smothering or siltation of habitat/unique species; changes in sedimentation rates and reduction in light and/or patterns caused by alteration of terrain; and destruction of habitat/species during pipeline installation via blasting trenching as well as other construction related issues (Santini 2000). Another often mentioned objection is the active tectonic activity in the Caspian Sea. However, their arguments do not stand up to criticism. Firstly, this active tectonic zones are mainly limited to the southern Caspian and the pipeline route can easily avoid these problem areas. The minor seismic activity prevalent in the trans-Caspian gas pipeline route could be resolved easily by taking them into account in the design features of the pipeline (Cutler 2007). Furthermore, the design features of the pipeline could easily resolve the issue of potential ecological damage due to pipeline construction and operation (Cutler 2007). Moreover, no one is able to prove that sea pipelines are a greater threat than the shipping of oil by tankers which is excessively being done already. In addition, sea pipelines have existed for many decades, since Soviet times and link the shore with the fields Bahar and Neftyaniye Kamni. Besides, Russia’s newfound desire to protect the ecological nature of the Caspian Sea is ironic, since it is the “most ecologically devastated area in the world” due to severe air and water pollution incurred during Soviet rule (CIA 1993). Moreover, Russia has transformed the Volga river into a sewage from which hundreds of thousands of tonnes of oil products, chemicals, industrial and agricultural waste, sewerage etc, flows into the sea every year (Aminmansour 1996). At the same time Russia was pushing through a sea pipeline on the bed of the Black Sea, namely the Blue Stream gas pipeline. Moscow has not found it necessary to agree its plans with any of the littoral states, while the ecological risks stemming from the greater length, depth, inhospitable environment are unmistakably higher here. Having provided counterarguments for the grounds on which Russia and Iran object to laying pipelines across the Caspian and taking into account their interests and objectives (see 4.6.2), which places them on the opposite side rallying firmly against the trans-Caspian gas pipeline project, one has to conclude that these environmental objections are just a cover up for their geopolitically motivated strategic behaviour.
Appendix F Unresolved legal status of the Caspian Sea

The legal status of the Caspian Sea at the end of the nineties

The current legal status of the Caspian Sea bed dates back to the Treaty of Friendship of 1921 and the Treaty of Commerce and Navigation of 25 March 1940 between the former Soviet Union and Iran. Not surprisingly, these agreements are outdated but still very much valid for lack of a comprehensive agreement on the legal division of the Caspian Sea. The instruments only deal with the issues of navigation and fishing rights. No maritime boundary between the former Soviet Union and Iran was ever established. The treaty further declared that the "parties hold the Caspian to belong to Iran and to the Soviet Union." Since the collapse of the Soviet Union in 1991, the legal issues are on the rise because the 1982 U.N. Convention on the Law of the Sea (UNCLOS) defines it as "a special inner sea."

Russia: The Strategic Chess Player

Beginning in the fall of 1994, Russia put forth the argument that the Caspian Sea, as an enclosed body of water with no outlet to the ocean, is really an inland lake and thus has attached a "special rights" status to the development of its natural resources (Faraz 2007). Given this argument, Russia uttered that the UNCLOS was not applicable. Legally, Russia uphold its position in two ways. Firstly, it based its argument on the assertion that the Soviet-Iranian treaties of 1921 and 1940 are still valid. Secondly, all decisions regarding development of the Sea's resources would have to be agreed upon by all five littoral countries (Blum 1996). Russia opted for a regime of shared sovereignty, in international relations also called a condominium system, allowing equal access to all littoral states. This would effectively stop implementation of oil contracts signed by Azerbaijan, Kazakhstan, and Turkmenistan and nullify their ability to make independent decisions on the exploitation of their Caspian energy reserves. It is argued that the official argument of Russia [and Iran] being in favour of joint sovereignty of the Caspian is that the latter is necessary to protect the Sea’s ecosystem from the rapid development of offshore oil and gas deposits (Frank 2001). The real reasons, however, are geopolitical and economic of nature. Joint dominion over the Caspian Sea would empower the dominant regional actor, Russia, with the strongest card in the exploitation of the Sea’s energy resources and undermine the independent decision-making ability of the other newly independent littoral states. Not been able to develop its resources and thus to draw its own path to economic and political independence, the Former Soviet states adjacent to the Caspian Sea would again become a virtual client of Moscow.

Iran: The Legal Veto

Iran’s legal position is tempered by several geopolitical and economic realities. First of all, there is the reality that based on the Modified Median Line (MML) principle, Iran due to its relatively small Caspian coastline would get only a small piece of the pie, nearly 13 percent of its seabed. Second is the fact that Iran’s shores do not appear to hold significant hydrocarbon reserves (Diba 2006). Furthermore, even if significant profitable amounts would have been discovered, Iran lacks the funds to allocate significant resources away from its Persian Gulf production agenda. Last but certainly not least, Iran has good reason to prevent the Caspian from becoming another Persian Gulf. It fears that an open door policy will especially attract American corporations, thereby instigating the involvement of the USA in Caspian affairs (Lelyveld 1999). In Tehran’s eyes this is a direct challenge to Iran’s sovereignty in the region (Lelyveld 1999). Based on these realities the Foreign Ministry of Iran has generally followed the Russians in using a “legal veto” strategy regarding Caspian development.
Both Russia and Iran condemned Turkmenistan’s decision to construct the trans-Caspian gas pipeline among others on the ground of the unresolved legal status of the Caspian Sea. In late November 1999, the two countries joined in a statement opposing a U.S.-backed plan for a trans-Caspian gas pipeline to Turkey before all five shoreline states have agreed on dividing the waterway (Lelyveld 1999). The Iranian Foreign Ministry spokesman named the move unacceptable and said that it was against the principles of countries bordering the Caspian Sea. Furthermore, it was added that Turkmenistan’s decision violated both multilateral and bilateral agreements given the current legal status of the Caspian Sea and that such a project requires approval from all five littoral countries (BBC 1999). Azerbaijan was of the opinion that this is a matter for the countries across whose zones it is proposed to build them.
Appendix G Bilateral issues Niyazov and Aliyev examined

Discovery of Shah-Deniz Field in offshore Azerbaijan and its implications

The discovery in June 1999, of the large gas-and-condensate field at Shah-Deniz, offshore from Azerbaijan changed the overall power balance. Surveys pointed out that these discovered volume was between 700 and 1000 bcm of natural gas. The trans-Caspian pipeline must cross Azerbaijan, but now Baku may be able to supply Turkey with gas that is closer and cheaper than Turkmenistan's reserves. In May 1999, Turkey signed a purchase and sales contract with Turkmenistan, but it included flexible pricing that may be reviewed every six months. This deal could be vulnerable if Azerbaijan undercut Turkmenistan's price. Moreover, this had the consequence that Azerbaijan’s interests changed as it was no longer solely a transit country but also a potential host country. As a result, Azerbaijan demanded a portion of the volume of the TCGP for itself. Niyazov firmly disagreed with Aliyev’s proposition because Turkmenistan was in need for hard currency as their economy was plagued with debt, which paved the way for a tough dispute in which Niyazov in reply reiterated the first Turkmen claims to a major offshore oil field, namely Serdar/Kyapaz oil field (Kurbanov 2007). This was odd because during the November 1999 OSCE summit in Istanbul, documents were signed by Turkmenistan and Azerbaijan agreeing not to allow the dispute over the oil fields to stand in the way of cooperation on the TCGP (Cutler 2001). The tough negotiations was due in part of the poor personal ties between the two Presidents. “Both men could not stand each other” says John MacLeod, a senior editor at the London-based Institute for War and Peace Reporting (IWPR). "Aliyev was a very strong character, and Niyazov was...an eccentric, to say the least”. This personal animosity made the difficult negotiations indeed go from bad to worse. It went even so far to the point that there was no diplomatic relationship between the two countries (see appendix D). This manoeuvre by Niyazov, which basically is like ‘scratching an old wound open’ complicated the negotiations even further and can be regarded as fuel to the fire. Hence, a dispute began with Turkmenistan over the volumes to be allocated between the two countries. Of the TCGP's 30 bcm per year, originally all was to have come from Turkmenistan. Turkey had contracted for 16 bcm per year for its domestic market, with the other 14 bcm in the long term being re-exported to Europe for hard-currency earnings. Now Azerbaijan wanted those 14 bcm of the TCGP's annual volume for the Shah-Deniz gas. Azerbaijan's negotiating position over TCGP volume allocation was based upon its assessment of its own export capacity needs. Its demand of 14 bcm per year was a maximum throughout quota that would not be reached in the first year of production. BP-Amoco, which leads and operates the Shah-Deniz consortium, estimated it would take only two years to ramp up to maximum volume. The prospects of the construction of the trans-Caspian gas pipeline could provide Turkmenistan with the much needed loans just to keep the economy afloat (Lelyveld 1999). Niyazov insisted that it would take at least five years and he firmly refused to accept Baku’s demand of nearly half the TCGP volume. This inflexible stance of Niyazov was not understood by the involved actors, since Azerbaijan was further down the line and by discovering the Shah-Deniz field it had a substantially better bargaining position. Azerbaijan wanted to agree in advance on a quota that would not block future development, even if that quota was not fulfilled in the first year. So Baku kept on persisting for a figure of 14 bcm annually from the start.

In reply to the stalemate in the negotiations, Niyazov turned to Russia to work out a deal with respect to further opening up the northern connection. The Azerbaijani side countered, on the basis of the Shah-Deniz find, that it was perfectly capable to proceed on its own, with construction of a gas pipeline through Georgia to Turkey. With the Shah-Deniz field, it did
not need Turkmen participation or the TCGP. Since Azerbaijan would be able to limit the volume of gas from Turkmenistan to be allowed into the TCGP across its territory, it could have killed the project by making the financial parameters uninteresting to investors. On the other hand, if Turkmenistan did not show irrevocable interest, then Azerbaijan and the Shah-Deniz consortium were ready to construct their own pipeline to Turkey. In the meanwhile Niyazov’s irrational behaviour had frustrated the involved actors so much that two out of the three transnational corporations (U.S. companies) had withdrawn from the international consortium (see Appendix A). Taking into account the close entanglement between Washington and the U.S. companies, the latter’s withdraw from the consortium was a sign of a fundamental shift in U.S. policy toward Turkmenistan. It should be regarded as a decline of U.S. support for the trans-Caspian gas pipeline, which is crucial for the implementation of this project, particularly with regards to the financing. As the TCGP talks were failing in Ashgabat, BP-Amoco was indeed making it clear that it did not intend to wait to move on exploiting the Shah-Deniz deposit. It announced plans to take Shah-Deniz gas to Turkey following a timetable similar to that projected for the TCGP. However, the prices would be better than those Turkmenistan could offer. As a result of the continuing stalemate, the package of agreements concerning the Baku-Tbilisi-Erzurum (BTE) gas pipeline project were signed between Turkey and Azerbaijan on 12 March 2001 during the official visit of the President of Azerbaijan to Turkey and between Georgia and Azerbaijan on 29 September 2001. In October 2001 (EIA 2002), Azerbaijan announced that the planned trans-Caspian gas pipeline would not be realized. A reference is made to appendix D for a more detailed overview of the most defining events. Although, the realization of the Trans-Caspian section of the TCGP was cancelled, the construction of the South Caucasus gas pipeline could make a prospected connection with Turkmenistan even more viable in the near future (see section 6.3).