

Energy Diplomacy In Azerbaijan's Foreign Policy

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Abstract

In the 21st century, the relations between states are being shaped by factors deriving from the national interest and the national security agenda. Many countries have shifted their foreign policies towards an economization strategy, i.e. assigning a particular importance to the economic priorities and instruments in foreign policy, as in the case of the small state of Azerbaijan, bordered by large neighbors and influenced by yet larger powers. Before Azerbaijan's independence, Regional powers such as Russia, Turkey and Iran were active and after the independence, the US and EU, added to the competition over the rich oil and natural gas resources of the Caspian region. All of these countries created an external pressure and influence in Azerbaijan, turning the Caucasus region into a new playing field of the Great Power Game. Thus, the geopolitical ambiguity combined with oil and gas resources and further with geographical imperatives will shape and pose challenge to the country's foreign policy.

Keywords: Energy diplomacy, Foreign policy, Caspian Sea, Economic Security.

1. Introduction

After the collapse of the Soviet Union, Azerbaijan declared independence on October 18, 1991 and signed some major reforms to bring her economy on the path of liberalization for free access of market. Plethora of natural resource availability in the Caspian Sea basin especially oil and

natural gas provided Azerbaijan a platform and to set its economic objective accordingly. Therefore, to achieve economic target set by the newborn country it was necessary to use Caspian Sea energy resources in a most logistic, judicious and effective way. The year 1994 can be called as a great and most important year in the history of Azerbaijan for its economy as Azerbaijan signed contract with the world's leading Oil Company which played an important role in ensuring energy security both at regional and international scale (Bagirov 2007).

Sudden independence gained by the coastal countries of Caspian Sea basin left them totally on their own fate as new problems started emerging in front of these countries related with the unclear division of Caspian Sea ownership rights and pre existing oil and gas pipelines. Russian control over the export route limited access to these newly independent countries for expanding their economy. To cope up with these problems, these nations invited foreign multinational oil companies for the extraction and investment of undiscovered energy resources in the region.

During the last decade of 20th century, Azerbaijan signed major oil contracts with different companies of the world. These oil contracts were very important for Azerbaijan's economic and political development. Azerbaijan also started the strategic course and plan for pursuing its national interests for the export of oil and gas resource to the international energy market. While carving out its future national interests Azerbaijan's main objective was to diversify its energy, transport route for not making it dependent on any single route. Diversified energy resources and export routes in the region, fulfill the interests of the major purchasers of gas and oil of Azerbaijan, as well the goals of the Energy importer nations.

2. Azerbaijan's Oil and Gas production and reserves

Azerbaijan holds an important position in the Caspian Sea basin in terms of oil and gas production and reserves, which give her an important tag of world major oil and gas producing country. Traditionally it is an oil producing country, but in future as infrastructure will develop and advance, natural gas will gain importance in Azerbaijan's economy. Natural gas accounted for nearly 67% of Azerbaijan's energy consumption in the year 2012 while oil contributed about 30% of its total energy used. Oil and gas production and its export are a key element in Azerbaijan's economy as the country's economy which is heavily dependent on its energy

export. It is vital to note that more than 90% of its total export volume was contributed by oil and gas sector (IMF 2012).

2.1 Oil: production and reserve

Azerbaijan has a strong economic and scientific caliber, suitable special location and its rich oil and gas deposits have given an important place in the region's political environment. Oil plays an important role in Azerbaijan's overall development. As the result of the global wide scale and comprehensive policy conducted by the national leader Heydar Aliyev, Azerbaijan aims to ensure the economic prosperity, political independence and welfare of the people. The oil industry of Azerbaijan is almost 150 years old. But the people of Azerbaijan were able to begin a wide scale utilization of these reserves in the late 20th century. Heydar Aliyev was the one who made that come true. Azerbaijan which is famous as the oil country in the entire world initiated the industrial production of oil in the middle of the 19th century. "The oil fountain in the Bibiheybat field of Baku in 1848 laid the foundation for the first industrial production of the black gold in Azerbaijan. Azerbaijan took first position in the production and processing of oil in 1899 and accounted for 50% of the global oil production" (Babayev 2002). In the beginning of 2012, Azerbaijan had a 7 billion barrels oil reserves while in 2013 it produced 881,000bbl oil per day and during this period it consumed about 85,000bbl oil per day. ACG oil field holds an important position in Azerbaijan's total oil production as it produces almost 75% of total oil production and, 70% of total country's oil reserves which was almost 5 billion barrels (OGJ 2013).

The collapse of the Soviet Union led Azerbaijan to face numerous challenges, especially in the field of economy. Azerbaijan is traditionally an oil producing country so major infrastructure related to the production, processing and refining of oil was left with Russia, which created a major setback to the country's economy as it was dependent on oil for their growth and development, and, came under the monopoly of Russia. From (fig.1) it is clear that in the beginning, year of independence, the production of oil was recorded very low which was about 222.24 barrel per day in 1992. So in order to promote and crystallize the production of oil Azerbaijan framed its policy accordingly.

Year 1994 saw a major shift in the policy of Azerbaijan as Azerbaijan signed many oil projects with foreign multinational companies. In 1994 Azerbaijan signed a joint agreement to develop Azeri Chirag Gunashli (ACG) oil field with twelve companies latter known as “contract of the century”. After the construction of Azerbaijan International Operation Company (AIOC) in 1995, production of oil gained a boom. There was a significant increase in the production of oil in Azerbaijan from 2002 to 2010 except in 2008 because of international economic slowdown. However, production started declining since 2010 till present from 932,000 bbl/d (2012) to 880,000 bbl/d (2013) due to the recent fall in oil prices and political instability in the region. Till date, Azerbaijan has signed more than 25 field agreement with more than 35 companies of different nations (EIA 2013).

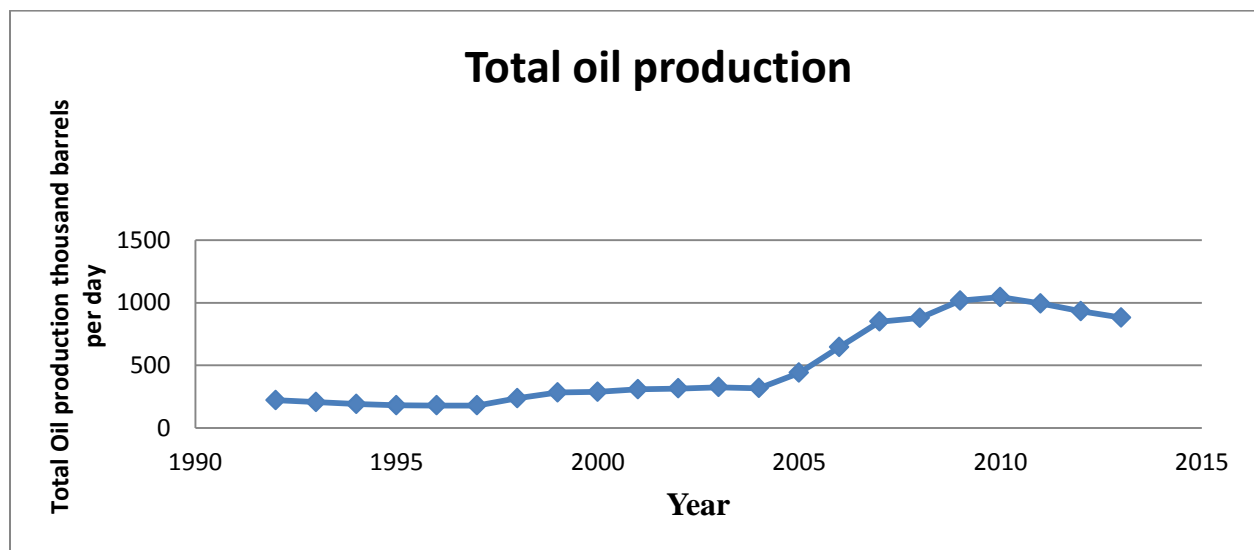


Fig.1

2.2 Natural Gas: production and reserve

According to Oil and Gas Journal, Azerbaijan’s proven natural gas was 35 trillion cubic feet (Tcf) at the end of 2013. Shah Deniz field have largest reserves of natural gas. After the discovery of Absheron and Umid field, a total proven reserve was expected to rise to 15 trillion cubic feet. However it is not clear how much of natural gas is technically feasible to extract. It is

important to note that, traditionally Azerbaijan is oil producing country but natural gas production and export is growing rapidly.

ACG and Shah Deniz fields play an important role in the production of natural gas in Azerbaijan. These two fields are offshore in nature. In 1999, Azerbaijan passed a law which required planning for associated gas exploitation to deal with each oil project. According to Energy Information Administration report 2013 “SOCAR and TDA signed a \$425,000 agreement in 1999 to fund a comprehensive natural gas study”. Shah-Deniz gas field has reserves of 29 trillion cubic feet to 40 tcf of gas (EIA 2013). The yearly production rate from Shah-Deniz gas field is estimated by 286 billion cubic feet (Bcf). Nakhchivan gas field contains 900bcf reserves is also important centre of Azerbaijan for gas production. Offshore fields contribute almost 95% of Azerbaijan’s total gas production. The offshore gas field i.e. Bakhar alone makes 40 % of country’s total gas production. Discovery of Shah Deniz field led to the increase of Azerbaijan’s natural gas production that started production in 2006. It is clear from the fig.6 that till the discovery of Deniz field, production of gas was stagnant but after 2006 there was a significant increase in the production of gas (British Petroleum Report 2013).

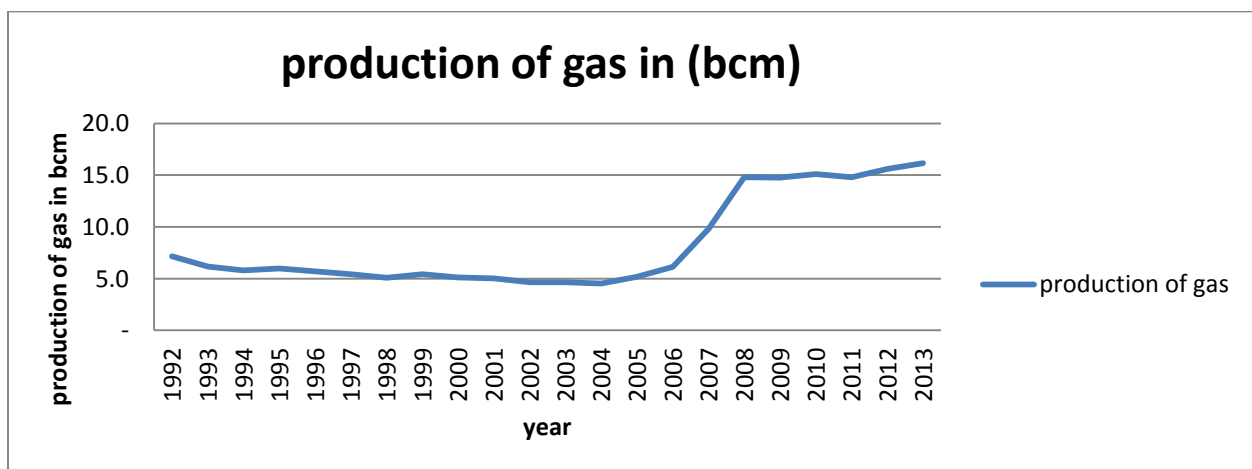


Fig.2

3. Impact of oil and natural gas on Azerbaijan's economy

The sudden imposed independence of Azerbaijan shattered its economy in a large manner. Early days of independence was occupied with the “problems such as war between Azerbaijan and Armenia, Russian restriction on transportation and stopping the use of two major oil pipelines due to the war in Chechnya, administrative weakness disruption in the legal layout and ethnic minorities. All these problems led to the economic crisis in the country” (Guner 2008).

The GDP was reduced to 30% in 1994 as compared to 1990 GDP. The inflation reached its highest level that is 1764% in 1994. All the macro economic variables got affected during this time period because of the war situation and Nagorna-Karabach conflicts. When Haider Aliyev came on power he transformed Azerbaijan's unstable and sluggish economy into stable and rising economy. He has taken critical decisions related to the Country's long-term interests. (Samuel 2010).

Oil and gas reserves and production are the major source for Azerbaijan's economic development. After independence Azerbaijan got foreign attention due to its energy resources, due to these resources a number of projects installed within the Country's political boundary. Under the strong leadership of Haider Aliyev, Azerbaijan got a stable environment which promoted major international energy companies to invest in the country's economy. ACG, BTC, BTE, and Shah-Deniz oil fields work as a “backbone” for Azerbaijan overall development (Suleymanov, Nuri and Huseynov 2013).

The Azerbaijan economic situation improved with the passage of time and it leads to controlled rate of inflation stable currency, external debt ratio and the budget deficit becoming low. GDP rate reached at desired level and is increasing till present. “After the production and export of Caspian deposits since 2006, Azerbaijan has begun to reboots its economy and maintained the increasing trend in GDP. Economic growth from 2003 to 2011 was 80%. During 1994-2011, a total investment volume in the country was approximately 80 billion dollars” (Azerbaijan Statistical Report 2014). The poverty level was also reduced to 7% in 2011 that is all time low after the collapse of Soviet Union and republic's independence, which was 49% in 2003.

Azerbaijan's energy resources contribute to its economy to a large extent. The role of oil and gas extraction is growing in Azerbaijan which leads to its economic growth. In spite of major contribution of economic resources to its economy, there is huge mismanagement of profit and lack of development strategy for other sector which create imbalances in the country's economy. According to the ministry of finance of Baku, the energy sector inculcates about 75% of the Republic's tax revenue. Natural gas and oil makes up to 95% of Azerbaijan's export.

4. Oil and Gas resources in Shaping Azerbaijan's foreign policy

After Azerbaijan emerged as an independent country and integrated her with the world economy. It signed the "Contract of century" in the year 1994; this agreement played an important role in the Azerbaijan's export and production of oil. This agreement was very important for the development and reconstruction of Azerbaijan's economy as it played a key role in the international economic and political relation of Azerbaijan. After the signing of major oil contracts during the last decade of 20th century, Azerbaijan faced numerous challenges i.e. problem related to the legal status of Caspian sea, politics related with the pipelines and managing its oil revenues. In order to solve these problems Azerbaijan launched a careful and strong policy.

Azerbaijan's late president Heydar Aliyev was the architect and guiding source of country's energy policy. In his opening speech in the International Oil-Gas Production in the Caspian Sea Exhibition which was held in Baku on 24 May 1994 president Aliyev quoted that "cooperation with the western oil companies would ensure further development of the Azerbaijan's oil industry and would lead to mutual partnership with the western countries. Steps taken by Azerbaijan towards cooperation with western oil companies have both economic and political substance".

Since 1994 Azerbaijan made significant progress in the world economic and political sphere. It is important to note that with the all prevailed problems such as Caspian legal status, obstacles in creating new oil pipeline routes, BTC oil pipeline and BTE gas pipeline constructed and emerged as world major oil and gas supply routes. Due to this advancement Azerbaijan turned into world

hydrocarbon provider and tries to further expand its supply. In 2011, Azerbaijan has established trade relations with more than 150 nations.

Before independence, Azerbaijan's foreign policy was shaped by USSR. All its oil has been diverted to the Russian oil companies, and during that time there was no way for it to influence its foreign policy agenda. After the sudden independence in 1991, the foreign policy shifts were quite hasty and unstable. It took some time to establish its foreign policy relations by establishing its energy resources. With the production of oil and gas more and more foreign investment took place in the country for oil and gas which raised economy of Azerbaijan at an amazing rate, and till 2008 the oil revenues contributed to a doubling of the GDP and also 75% of the state budget coming from the energy sector. In order to get the most out of its resources, Azerbaijan has tried to play a balanced foreign policy game with the regional powers and the global ones. Contrary to its neighbors Armenia, which is Russian-oriented, and Georgia, showing a great sympathy towards the west, Azerbaijan has tried to shift its policy towards both the areas. The reason for this is that it wanted to open ways for economic benefits from all sides, and keeping options open is the only way out for a small country of Azerbaijan, on which the major powers are relied hugely to fulfill their energy needs.

The Baku-Tbilisi-Ceyhan pipeline has aided Azerbaijan to bypass Russia in providing Europe with oil, and as a result has lifted the pro-western spirit within the country itself. It is important to note that Azerbaijan politically seeks integration within NATO structures, and, therefore, its legislation has started to be harmonized with the Council of Europe standards (Mamedyarov & Olcott 2005). These measures are as usually taken from the western countries to build democracies wherever there is a national interest because democracies are peaceful and friendly, and controlling Azerbaijan's oil and gas production seems a lot easier in this way.

The growth in economy due to the oil revenues has also boosted confidence on the foreign policy towards Armenia and the internal problem that the country has in Nagorno-Karabakh. The president, had threatened Armenia that with this kind of economic growth in a few years, the both countries will be at great par, and Azerbaijan will use its wealth to strengthen its army and be ready for getting back the occupied territory (Allnut 2010).

The country's long term plans are to exploit its geostrategic location in addition to its own energy resources, which may turn to be an imperative to the regional transport and energy-transport projects. Some of these include Turkmenistan and Kazakhstan, the other two oil-rich ex-Soviet countries whose oil is largely being controlled by Moscow. Azerbaijan could use its geographical position to open new routes for these countries and also to show that it has a balanced foreign policy, Azerbaijan's president has visited both Washington and Moscow, and has clearly expressed its neutrality, foreign-policy-wise, due to its ties with both countries in different levels.

Though the BTC pipeline was thought to be solving Europe's problem with oil but the recent tensions in Georgia have shown that the route is not all that stable. The BTC pipeline confirmed the assumption that a long-term political project realized on the wishes of politicians to isolate neighboring countries, for e.g. Armenia, can never be profitable. As a result, it decided to reduce the shipments of oil to EU through the only BTC pipeline connecting EU with the oil-rich Caspian region, and instead increased its exports to Russia and Iran. It is important to note that the country has made some smart moves after the Georgian conflict, after which all the attention was directed towards Azerbaijan and its natural resources. The international society was seen as a medium not only to sell, but also for conflict resolution of Azerbaijan's separatist region, Nagorno-Karabakh. Azerbaijan strategic location i.e. it connects Asia to Europe and works as crossroads between the two continents of the world. An 800 km extent, from Caspian to Black Sea helps Azerbaijan to retain its significance role in the world's Cultural and economic links.

5. Conclusion

Azerbaijan oil and gas sector plays a key role in its economic development. After the Soviet breakup, Azerbaijan tries to maintain close relation with the western countries in order to step up into the world energy market. In order to reduce its reliance on any single power, Azerbaijan tried to diversify its energy routes through Georgia, Armenia, and Iran. Western states were the part of Azerbaijan's long term strategic plan for bringing together global and regional players to check Russia and Iran. The construction of BTC oil and BTE gas pipelines worked as a major tool for Azerbaijan's economic development and to strengthening its regional cooperation. Azerbaijan is the starting point of major strategically and economically oil and gas export

terminal such as: Baku-Tbilisi-Erzurum gas pipeline, Baku-Novorossiysk and Baku-Tbilisi-Ceyhan oil pipeline. With these pipelines Azerbaijan worked as the energy export corridor which helped it to gain a strong and strategic position in the Caspian Sea region.

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