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UNLOCKING THE ASSETS: ENERGY AND THE FUTURE OF CENTRAL ASIA AND THE CAUCASUS

A POLITICAL, ECONOMIC, AND CULTURAL ANALYSIS

Central Asia and the Caucasus are considered by many to be the next oil and gas frontier. The region's sizable energy reserves, combined with its unique political status as eight newly independent states emerging from the break-up of the former Soviet Union, have catapulted these countries into the limelight of Western media and policy-debate. Heightened awareness has led to calls for greater public and private Western involvement in the region's development.

The hydrocarbon reserves of the region are significant. Proven oil reserves are pegged at between 15 billion and 31 billion barrels, about 2.7 percent of total world proven oil reserves. Proven natural gas reserves of 230 to 360 trillion cubic feet represent about 7 percent of total world proven gas reserves. By comparison, proven oil reserves of the Middle East represent 55 percent of world proven reserves while South America equals 8 percent. Some geologists assert that proven reserve numbers for Central Asia and the Caucasus, commonly referred to as the Caspian Basin, are misleadingly low because huge areas of the region have not been explored. The region could potentially hold between 60 billion to 140 billion barrels of oil to be confirmed by future exploration. However, this figure remains speculative and should not be compared to the 269 billion barrels of proven oil reserves already discovered in Saudi Arabia.

Oil production in Central Asia and the Caucasus will never match the Persian Gulf, where there are five major oil powers and several smaller producers. Many of the countries of the Caspian Basin have limited, if

any, oil potential. More than half of the Caspian region's proven oil reserves and 80 percent of its possible oil reserves lie in one country -- Kazakhstan. Turkmenistan holds large reserves of natural gas, but its distance from key consumer markets may mean those reserves will be commercially difficult to develop.

Were the possible reserve numbers to pan out, the region would be geologically equivalent in scale to the North Sea. Again, however, it would be unwise to draw such parallels. Once technological hurdles were tackled, the North Sea represented a huge oil province where a stable investment climate allowed maximum exploration and development of dozens of fields simultaneously over a relatively short period of time. The barriers to exploration and development in Central Asia and the Caucasus are far more numerous and burdensome than those found in other areas such as the North Sea. These barriers will make it hard for the region to move rapidly to peak output levels implied by reserve figures.

North Sea oil production ended 1997 at 6.1 million barrels a day (b/d) but is expected to peak in the coming years. Venezuelan oil production stood at 3.5 million b/d in early 1998 but is expected to rise to over 6 million b/d by the middle of the next decade. Even under the most optimistic assessments, by the year 2010, Caspian oil production will likely reach little more than 3.5 million b/d and cover only 3 percent to 4 percent of anticipated global oil use. By contrast, Venezuelan oil is expected to account for as much as 7 percent to 8 percent while Middle East

oil will still dominate with a 25 percent to 35 percent share, depending on market conditions.

In short, the Caspian Basin is not going to be the "ace in the hole" for international energy security. The region is by no means the only major oil and gas province in play that can help diversify world oil supplies and reduce reliance on the volatile Persian Gulf. Substantial reserves remain to be exploited in Africa, South America, and offshore Asia. In particular, the payoff in terms of magnitude of incremental supply to global markets would be much higher if greater efforts were applied to unlock the significant resources lying in Mexico and Russian Siberia rather than similar efforts in Central Asia and the Caucasus. Increased attention to liberalization or other means to finance expanded resource development in Mexico and Russia also meets other important U.S. foreign policy goals.

History has shown that control of energy supplies is an issue over which major powers go to war. As Desert Storm demonstrated, few would question whether access to the vast resources of the Middle East is worth a significant commitment of time and resources. The stability of the world economy continues to rely on the steady flow of moderately priced oil from the Persian Gulf. The diversification of oil supply through development of regions like Central Asia may lessen the importance of the Persian Gulf over time. But the Gulf will require a major U.S. security commitment for many years to come. Involvement in Central Asia and the Caucasus alone cannot significantly reduce the need for the U.S. to police the Persian Gulf, but such involvement could prove costly in political, military, and economic terms.

Beyond energy, Central Asia and the Caucasus's location between Russia, China, Iran, and Turkey make it a magnet for foreign powers and a flash point for potential conflict between them. In addition to neighboring countries, the U.S., Europe, and Japan have all exhibited interest in the region's economic potential. These factors raise the risk of a geopolitical competition in a region that already suffers from localized conflicts, economic distress, and environmental disasters. Such competition, if unchecked, could cause instability both there and in neighboring countries, notably Russia, and also complicate Washington's relations with Moscow.

The Economics of Exports from the Caspian Basin

The huge distance of Central Asian and Caucasus hydrocarbon reserves from the world's major energy consuming regions requires a considerable financial investment to bring them to market. The countries of the region are landlocked. Unlike competitors in other large oil-rich regions such as the Middle East, South America, and even Russia, the region's producers cannot simply ship oil by tanker from domestic ports. Instead, they must rely on expensive pipelines constructed through foreign territories as the chief means for transport.

The landlocked geography of the Caspian Basin region also creates serious logistical impediments to speedy exploration and development. The region is distant from major supply centers for exploratory equipment and faces a crippling shortage of modern drilling platforms and other material. Constraints on infrastructure, drilling equipment, and rigs are more severe in the region than in other parts of the world, and oil and gas well completions take significantly longer time. These constraints are aggravated by U.S. sanctions against Iran that deny American companies operating in the region access to Iranian transport routes and equipment.

The development of pipeline corridors from the Caspian Basin to international oil markets has been a slow and painstaking process. Many possible routes through Russia, Georgia, China, Afghanistan, Iran, and Turkey via Georgia or Armenia, have been discussed.

Numerous arguments have been advanced for favoring one route over another. Questions have arisen concerning the security of various routes given regional political uncertainties and ongoing ethnic disturbances. There are also concerns about the monopoly power that could be exerted either by privately-held pipelines or by governments of transit countries. The negotiating process has been shaped by the ambitions of various participants to capture as large a share as possible of the profits from the transport and sale of the oil from the region.

Examination of purely economic factors for export routing points to the following conclusions:

- Given reasonable expectations for economic re-

covery and growth, the littoral states of the Caspian Sea such as Ukraine, Romania, Bulgaria, and Turkey can absorb much of the projected export surplus of Caspian oil. Oil demand from these countries, combined with possible demand from refineries in Grozny, Russia, and northern Iran, could absorb as much as 900,000 b/d to 1.4 million b/d by 2010. This development will help alleviate congestion in Turkey's Bosphorus Straits but also reduces the volumes available to fill on-land pipeline routes beyond the Black Sea.

- Given the expected level of exports from the Caspian region by 2010 and the benefits of economies of scale, the use of several pipelines -- instead of one large line -- may not be the optimum solution. Multiple routes will result in substantially higher transport costs for exporting that "late" oil (that is, significant oil export volumes that will be built up via sustained exploration and development) to world markets.

- The geological and logistical difficulties in amassing large export volumes from the region argue in favor of a multiparty negotiation regime where inclusivity rather than competition is encouraged. This fact, combined with the economies of scale described above, suggest there might be a basis for reassessment of multiple routing as a key principle in the region's development.

- Proposals to construct a pipeline through Turkish Thrace to bypass the Bosphorus Straits have significant economic merit compared to other more well-known options. This route would relieve congestion in the Straits and address Turkish environmental concerns, such as the risk of an accident or oil spill.

- There is evidence that Saudi Arabia "subsidizes" prices through transport discounts for the sale of its oil to European markets. This fact has tended to lower the price of Saudi crude oil in Europe relative to Asia on balance over the last ten years. However, given the costs of transit plus shipping, the countries of Central Asia and the Caucasus will still receive a higher profit for sales to Europe than for sales to Asia via Iran. This, combined with the security concerns of adding to the already dangerously concentrated amount of world oil supply that must transit the Persian Gulf, argues against an Iranian route, regardless of the state of U.S.-Iranian relations.

- Natural gas exports to Asian consumers have more promising longer-term economic potential for

Turkmenistan and should not be abandoned due to political barriers, for example those relating to the conflict in Afghanistan.

The Geopolitical Setting

A host of complex geopolitical, social, religious, and cultural factors will influence the future of the Caspian Basin region.

The countries of Central Asia and the Caucasus, having achieved independence from the Soviet Union a mere seven years ago, are in their relative infancy. They have hardly begun the task of building post-Communist institutions or creating new national identities. Divisive ethnic tensions simmer beneath the surface in many of the countries of the region, and few, if any, boast an institutional framework for the smooth succession of leadership. Security arrangements are equally ill-defined, leaving the region prone to instability and threatening its economic development.

Finally, independence after over eighty years of direct rule by Moscow has created a strategic power vacuum in the region that has unleashed rivalries among large neighbors and distant superpowers.

A multitude of countries has shown commercial interest in the region, especially its natural resources. They include neighbors Russia, Turkey, Iran, and China; nearby Pakistan and India; and the United States, Europe, Japan, Saudi Arabia, and even Israel. Through long-term project developments and reform packages, Japanese industry leaders hope to secure a presence in Central Asia that alleviates some of Tokyo's energy import dependence on the Middle East while yielding mutually beneficial relations.

But, for the regional powers, interest extends well beyond commercial considerations. Historical factors play a role. For Russia, the region represents an area of traditional Russian dominance. For Turkey, it holds the cultural attractions of Pan-Turkism. The reemergence of Islamic practices in the region is a magnet for attention from both Saudi Arabia and Iran in their rivalry for leadership of a broader Islamic revival.

To some extent, regional powers also seek to reach into Central Asia and the Caucasus to help control ethnic movements in their own hinterlands, including Russia's southern regions, Kurdish borderlands in

Turkey, ethnic Azeri borderlands in northern Iran, and the Xinjiang province in Western China.

But geostrategic considerations also loom large. While talk of a new "great game" may be exaggerated, a number of major powers view the region, at least in part, in terms of a broader contest for spheres of influence. Though political attitudes inside Russia are often contradictory and more complex than many think, Russian leadership is sensitive to the West exploiting what it considers its temporary weakness in the Caspian Basin. China, too, will view foreign involvement in the Caspian, especially U.S. involvement, through a geopolitical prism. The Xinjiang province, which borders Kazakhstan and maintains close cultural and linguistic relations to Central Asia, is also reportedly the locale for much of China's nuclear testing. China will likely view American involvement in Kazakhstan through the prism of these security concerns.

Given budgetary constraints and the low level of support from the American public for foreign involvement lacking clearly defined, vital interests at stake, the individual countries of Central Asia and the Caucasus are unlikely to become a U.S. priority in terms of major economic assistance or security guarantees. American interest in stability in the region is likely to be case-specific and part of a broader focus related to stability in Russia, China, Turkey, and the Persian Gulf. U.S. diplomacy in the region should clearly articulate these realities.

Moscow's emerging attitudes toward the newly independent states of the Caspian Basin will have unique influences on their political and economic development. A shared interest in regional stability and economic opportunity could promote cooperation among the major powers involved in the region. But a foreign competition for influence could also feed existing ethnic, religious, and socioeconomic tensions. Conflicts, if elevated, could potentially affect international stability.

The Problem of Succession and Social Expectations

At first glance, the vigor with which any attempt at political opposition has been stamped out in Central Asia and in Azerbaijan seems to have created

a form of stability. However, the intense concentration of privilege of the existing elites makes it all but impossible for new political figures or ideas to enter the national arena save in catastrophic and revolutionary ways. By attempting to eliminate the messy ups and downs of democracy, the leaders of Central Asia and Azerbaijan have made it more likely that political change, when it finally comes, will be convulsive. The lack of predictability regarding succession is likely to breed instability.

Leadership successions are likely to occur in most of the Central Asian and Caucasus states over the coming decade, with the prospects of a younger generation of nationalists emerging to replace the old guard communist elite. Unlike the communist elite who have generally tried to hold their fragile patchwork societies together, these new nationalist leaders will likely focus increasingly on forwarding the interests of indigenous majorities and thereby are more likely to clash with large ethnic minority communities that have already exhibited separatist inclinations.

However, before they are faced with the problem of succession, the Central Asian and Caucasus governments could see the stability of their states endangered by socioeconomic problems. The leaders of the new states have generally performed poorly in keeping the social bargain that their constituents had come to expect from Soviet-style government. Living standards have slumped tremendously in the region, with each country plunging at least twenty-some rungs down the UN-calculated ladder of human development. Runaway inflation in the early 1990s drained savings accounts. The breaking of inter-republic connections has led essentially to economic collapse, which has meant an accumulation of enormous wage and pension arrears as well as the gradual deterioration of the educational, social welfare, and healthcare systems. By 1997, Central Asians spent more than 60 percent of their income on food. Human emergencies have also increased, including a rapid rise in the spread of disease, malnutrition, energy shortages, and a crisis in public education.

The Role of Religion

At present, the threat of the revival of Islamic religion to the political and economic environment

in Central Asia and Azerbaijan is remote. Muslims in the region tend to be divided by sect and degree of secularization. Political activities have been hindered by weak leadership and organization. For now, the revival of interest in Islam among the peoples of Central Asia and Azerbaijan is highly decentralized and, so far, remains distinct from the political arena.

No organized, broad-based, monolithic Islamic fundamentalist movement exists today in Central Asia or Azerbaijan, nor have charismatic Islamic politicians emerged to rally the indigenous population around a political banner. It is likely that the process of reclaiming Islam and reconstructing a viable Muslim civil society will take generations.

The rekindling of interest in Islam comes after decades of Soviet efforts to weaken its public and private influence. External manifestations of Islam's progress in the region can be seen in the increase in the number of mosques, schools, and Muslim religious organizations.

An increased awareness among Central Asian Muslims of their religious inheritance or the practice of the tenets of Islam presents no intrinsic danger to Western energy interests in the region. Islam as a faith need not hinder close economic relations between Western firms and Muslim states, as seen in long-term partnerships with many Islamic governments. But, as the population of the region becomes more educated about Islam, the utilization of Islam for political ends could become more prevalent. The danger also exists that a strengthening in Islamic identity in the region could aggravate already problematic religio-ethnic tensions.

To the extent that outward political expression and dissent are repressed by dictatorial regimes and driven underground, the growing network of mosques and religious schools will provide an efficient, alternative framework for organization of opposition movements and a forum for mobilization. While there appear to be few institutions or groups promoting the spread of political Islam at present, conditions could develop in the future that would foster the kind of underlying conditions and forces that fuel political Islamic movements. These include a high incidence of political repression and a lack of democratic processes; visible corruption among members of the ruling elite; an increasingly younger population with diminishing

employment and educational opportunities, particularly outside of urban centers; the creation of a new network of mosques and religious schools that could someday serve as an alternative network for political activity against the state; and a growing disparity between the richest and poorest segments of the population.

Corruption and Economic Disparity

A growing disparity between the wealthiest and poorest elements of the population, combined with blatant government corruption, will seriously limit the potential of increased oil and gas revenues to promote stability.

Corruption at the highest levels in several countries in the region has already widened the gap between the political elite and the rank and file of the indigenous population. As oil revenues increase dramatically, this trend could accelerate, potentially leading to internal instability that could affect the flow of oil from the region.

However, corruption in the region does not appear to be as rampant as in certain parts of Africa or the Middle East. Central Asia and the Caucasus has seen its share of resignations from government scandals. Public awareness and grassroots support for reformist programs can be tapped to aid in the implementation of new institutional systems that promote transparency. Economic reform programs can discourage wasteful spending and large-scale corruption. In Azerbaijan, for example, the International Monetary Fund ensured that oil exploration contract signing bonuses were sent into a special account at the Central Bank and fed into the national budget on a predetermined, staggered schedule.

Before energy exports begin to grow to large volumes, it would be useful for Caspian governments, local authorities, the energy industry, and international financial institutions to assess prospects for the establishment of government-sponsored social equity funds that could be directed at economic development and social services. Business partnerships could also be fostered that involve oil company-promoted projects on regional infrastructure development, transport, power generation, water management, and the environment.

Ethnic Conflicts

Inequitable distribution of oil revenues among competing ethnic groups in the region could also fuel continued or even accelerated ethnic unrest, which could similarly negatively impact the steady flow of oil exports. To the extent that oil production and transport revenues are perceived as contributing to the relative deprivation of any particular ethnic group by another, oil facilities or personnel could be targeted by indigenous ethnic groups seeking to assert their claims through acts of terrorism.

Each conflict is unique and will require case-specific approaches for resolution. The conflict between Armenia and Azerbaijan over the territories of Nagorno-Karabakh is deeply entrenched and threatens the stability of a westerly oil export route from Azerbaijan. In Azerbaijan, the large-scale refugee population lends a human face to the military occupation by Armenia of Azeri territory as a result of fighting between the two countries. The Armenian population of Nagorno-Karabakh, supported by ethnic brethren in Armenia and abroad, demand autonomy and self-rule, if not outright statehood in affiliation with Armenia, on the basis of principles of self-determination and historical claims. Multilateral mediation should continue either through the auspices of the OSCE or under the direction of the United Nations, leaving open the possibility of international peacekeeping forces if needed. Efforts should be made to accelerate regional arms control, including in the enclaves, building on the process envisioned in the 1990 Conventional Forces in Europe Treaty that is designed to reduce the number of tanks, artillery pieces, armored vehicles, and other non-nuclear weapons in Central Europe. Benefit could come from a reassessment of financial assistance to the region as part of a strategy to discourage a renewal of hostilities.

Since independence in 1991, Georgia has been struggling with numerous territorial conflicts and separatist movements that have hindered its status as an oil transit nation. One of the most serious threats to Georgia's stability has been the danger of Abkhazia's aspirations for independence. Russian military support, which played a critical role in Abkhazia's wartime gains in 1993, has waned as Russia reestablished extensive military basing rights inside Georgia. Mos-

cow now seems more interested in peaceful resolution of Abkhaz status. Other flash points in Georgia include South Ossetia, Ajaria, and the Javakheti region and, in Azerbaijan, the Lezgin provinces.

Building on progress already made, prospects for a stable, democratic, federal Georgia could be enhanced through business partnerships financed by shared transit rents. Such partnerships could broaden distribution of the benefits of development by contributing infrastructure and other development projects throughout Georgia, building on programs already underway in Ajaria.

Russia's Unique Problems

The Caspian Basin's bearing on internal Russian conditions is a very important factor and needs to be heeded by the international community. Russia must avoid political choices where its headway toward social and economic progress at home is hindered by the high costs of substantial engagement in the Caspian region. If Russia can draw anything from its experiences in the region since independence, it is that it cannot necessarily control events once they are set in motion as demonstrated during recent civil wars in Georgia and Tajikistan.

Russian military expeditions in the region have been costly in terms of internal resources, economic development, and political impact within Russian borders. Russian populations inside the federation remain wary of their regime's military involvements outside Russia's borders. The bitter experience of Afghanistan, combined with the tragedy of restoring constitutionality in the Chechen republic, contribute to a cautious mind-set. Moscow's attempts to police the Tajik-Afghan border remain unpopular with average Russians.

While conflicts in Georgia and Tajikistan appear to have reestablished the legitimacy of basing rights for the Russian military, the purpose of such bases in the post-Cold war era also remains subject to domestic debate.

In view of recent experiences in Central Asia and the Caucasus, Russia's leadership is beginning to pay more attention to the negative consequences of instability in the region. Military conflicts or ethnic separatist movements in the southern Caucasus,

for instance, could easily spill over into contiguous Russian areas, themselves patchworks of ethnicities. Moreover, related issues are increasingly entering the Russian domestic political landscape. The prominence of ethnic issues in Russian politics is mounting at the same time populations are increasingly sensitive to the heavy economic and social burden of caring for immigrant and refugee populations. There remains domestic concern for Russian populations outside Russian borders, especially in non-Christian, Islamic environments; these concerns will continue to drive external policies.

Moreover, there are other less visible problems that have direct bearing on regional stability and, thereby, Russian stability given its deep ties to the nations of the region. These include production and trafficking of narcotic substances, illegal trade in arms, disruption of communication infrastructures, spread of corruption and criminality, and ethnic violence.

Internal divisions within Russia's current political makeup and its own domestic problems are likely to create contradictions and inconsistencies in Moscow's Caspian policy for the foreseeable future. There are those inside Russia who believe the country's interests will be served through integration with the West. They argue Central Asia is irrelevant to Russia's long-term interests. But other factions believe linkages to the West will prove illusory and would like to see Moscow reassert control in its periphery.

Influential industrial groups continue to rely on Central Asian raw materials and semifinished industrial products as well as on local markets for their own goods. Communist factions would like to preserve ties to the periphery as a means to restore the Soviet legacy. Russian leadership is sensitive to the West exploiting what Moscow considers to be its temporary weakness following the breakup of the Soviet Union. For others in Russia, involvement in the region remains a sensible way of resolving the painful problem of Russian-speaking minorities in Muslim sections of the Newly Independent States. The view from inside Russia's oil sector also seems to point toward an aggressively integrationist approach. This could change over time as private Russian oil companies become more focused on garnering profits from their commercial investments in the region. Russian

corporations enjoy substantial economic and political power and may therefore be able to force changes in Moscow's future policy in the Caspian Basin.

The pluralism involved in Russian policy-making on Caspian issues complicates involvement of other international powers there. However, it will serve Western interests to pursue policies that undermine, rather than embolden, neo-imperialists in Moscow. In particular, absent real resources and guarantees, U.S. talk of containing Russia in Central Asia and the Caucasus can only be counterproductive. Instead, Russia should be supported in its efforts to refine multilateral mechanisms that may assist it in the performance of onerous duties of conflict resolution in Central Asia and the Caucasus.

Greater international attention, through organizations such as the United Nations, OSCE, and the World Bank, to the mounting Central Asian problems could be helpful in building a stable, liberal Russia. Attention should be given not only to conflict resolution in the Caucasus and Central Asia but also to social welfare issues such as poverty, environmental crises, sweeping disease epidemics, malnutrition, and power shortages. Participation of international organizations in conflict resolution, regional arms control, humanitarian assistance, and cooperation on a broad range of economic issues, including economic reform, should be the cornerstone for devising constructive, multilateral policies toward the Caspian region.

Policy Recommendations

- Geological and logistical difficulties in amassing large oil export volumes from Central Asia and the Caucasus region argue in favor of a multiparty negotiation regime where inclusivity rather than competition is encouraged.
- Expected regional oil production constraints for the next several years and economies of scale analysis suggest there might be a basis for reassessment of multiple routing as the key principle in the Caspian region's development.
- Proposals to construct an oil pipeline through Turkish Thrace to bypass the Bosphorus Straits have significant economic merit, suggesting it might be beneficial to reevaluate the relative priority being given to the longer, more expensive overland Baku -

Ceyhan route. The Turkish Thrace route would relieve congestion in the Straits and Turkish environmental concerns.

- American interest in stability in the Caspian region is likely to be case-specific and part of a broader focus related to stability in Russia, China, Turkey, and the Persian Gulf. U.S. diplomacy in the region should clearly articulate these realities and be developed in a more comprehensive fashion.
- A growing disparity between the richest and poorest segments of the population in Central Asia and the Caucasus, combined with blatant government corruption, will hinder the potential for increased oil and gas revenues to promote stability. Economic reform programs can and have discouraged wasteful spending and large-scale corruption. The International Monetary Fund and other multilateral economic advisory organizations should encourage and enforce elements in economic reform programs that promote transparency.
- Government-sponsored social equity funds should be established in the countries of the region to enhance equitable distribution of energy income. Such funds should be directed at economic development and social services. Business partnerships could also be fostered that involve oil company-promoted projects on regional infrastructure development, transport, power generation, water management, and the environment.
- Russia and the United States should encourage the countries of the region to establish arms control agreements that will prevent energy income from fostering an arms race within the Caspian Basin.
- Russia should be supported in its efforts to refine multilateral mechanisms that may assist it in the performance of onerous duties of conflict resolution in Central Asia and the Caucasus.
- Greater international attention through organizations such as the United Nations, OSCE, and World Bank to the mounting Central Asian problems could be helpful in building a stable, liberal Russia. Attention should be given not only to conflict resolution in the Caucasus and Central Asia but also to social welfare issues such as poverty, environmental crises, sweeping disease epidemics, malnutrition and power shortages. Participation of international organizations in conflict resolution, regional arms control,

humanitarian assistance, and cooperation on a broad-range of economic issues, including economic reform, should be the cornerstone for devising constructive, multilateral policies toward the Caspian region.

- Russia now faces a broad array of internal divisions within its current political makeup. While public wariness and the existence of differing political foreign policy camps seem to imply that Russia's Central Asian policy will be characterized by contradictions and inconsistencies for the foreseeable future, there exist several influential groups that would like to see Moscow reassert control in Central Asia and the Caucasus. American policy towards the region should recognize this reality. Talk of containing Russia in the region is likely to be counterproductive and, absent real financial resources and security guarantees, empty. Washington's policy toward the Caspian region should bear in mind the region's impact on Russia's internal stability and take into account parallel efforts to integrate Russia more closely with the West.
- Increased multilateral efforts to promote conflict resolution on the status of the territory of Nagorno-Karabakh should be pursued. Greater efforts should be made to implement arms control agreements in the region, and financial levers should be utilized to discourage a renewal of hostilities. The repeal of Section 907 of the U.S. Freedom Support Act, which limits U.S. assistance to Azerbaijan, should be considered as an inducement to Baku in return for cooperation in conflict resolution negotiations with Armenia. At the same time, Armenia should be encouraged to enter into meaningful negotiations with Azerbaijan to resolve the Nagorno-Karabakh issue peacefully.
- The U.S. should reassess the impact of Iranian sanctions on the timely, efficient development of Caspian energy resources as part of an overall review of U.S. policy toward Iran. Consideration should be given to the pros and cons of licensing activities of U.S. companies, including transit of drilling equipment that could help give an early boost to Caspian production.

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