

The Development of Energy Resources in Central Asia

**House Foreign Affairs Committee
Wednesday May 21, 2014
2200 Rayburn HOB
Washington, D.C.**

**David A. Merkel
Senior Fellow, Atlantic Council
Dinu Patriciu Eurasia Center
Former Deputy Assistant Secretary of State for European
and Eurasian Affairs and Director for South and Central
Asian Affairs at the National Security Council**

Introduction

I would like to thank Chairman Rohrabacher, Ranking Member Keating and the Members of the House Foreign Affairs Subcommittee on Europe, Eurasia, and Emerging Threats for the opportunity to testify today. Further, I would like to commend the Committee for exploring this topic today. Too often, the issue of energy security, or Eurasia more broadly, tends to be discussed in reaction to steps planned and carried out by Moscow or Beijing. Events in Ukraine, as was the case with events in Georgia in 2008, require a well considered proactive approach.

In the time I have with you today, I would like to make an assertion, a couple of historical points and a few recommendations.

Russia as Gas Station to Europe

When I talk with our European allies about the leverage Moscow has because of Europe's dependence on Gazprom to keep their showers warm, they are often reluctant to pursue policies that result in the diversification of their hydrocarbon imports because they - notably Berlin - fear that Moscow would react negatively and their supply and other considerable business relationships would be interrupted. Europe receives more than 30 percent of its gas from Russia. While they see clearly the leverage that Russia has over the European Union as a supplier of energy, they often undervalue the fact that both suppliers and customers of energy have leverage. Even European Union documents, that my Russian interlocutors love to reference, conclude that Russia is more important to the European Union than the EU is to Moscow.

In Moscow any suggestion of competition of supply or transit would be characterized as anti-Russian or

reminiscent of a cold war mentality. These assertions would be made with quite a bit of verve as Putin relies on oil and gas as a political weapon in Europe, and among the countries of its former soviet empire.

Putin has determined that if the disillusionment of "Upper Volta with Nuclear weapons", as the USSR was often called, was the "greatest geopolitical catastrophe of the century", then he can regain at least regional greatness with a passive US Administration and an inward looking EU by being the gas station to Europe.

In order to maintain Russia's energy leverage over Europe, which as we have seen frustrates the likelihood of the EU implementing meaningful sanctions on Russia as a result of invading Ukraine, Moscow must control Central Asian gas and it's route to market. While it is clear that multiple sources and transit routes of hydrocarbons to market are preferable, this will not just happen. It requires a solution that is commercially viable; enjoys political leadership and vision as well as a corporate champion.

I should also point out here that there are other factors preventing European support for sectoral sanctions on Moscow. President Obama does not have the personal authority or relationships to gain Europe's consent to sectoral sanctions and Putin knows it. British Prime Minister David Cameron's concern for the City of London has him rejecting financial sanctions. French President Hollande's interest in the delivery of two war ships built for the Russian Navy, one remarkably named Sevastopol, call into question France's agreement to military sanctions along with Berlin's objection to Energy sanctions.

Baku-Tbilisi-Ceyhan Success

The Baku-Tbilisi-Ceyhan pipeline, transports one million barrels of oil per day from the capitol of Azerbaijan on the Caspian through the Republic of Georgia to the Turkish port of Ceyhan on the Mediterranean. Today, it is a commercial success that is contributing to one of the fastest growing economies, the most significant link between Europe and the Caspian Sea region and a most valuable tool in diversifying global sources of energy. This important link that assists Europe's energy needs and enhances the sovereignty of former Soviet Republics is the result of American leadership by two Administrations. Through a proactive policy developed and implemented by both the Administration of Bill Clinton and George W. Bush with significant input by both Houses of Congress and the political courage and leadership of the President of Azerbaijan, we see clearly what we are able to achieve when we have a strategic vision and see Russia as it is rather than as we wish it.

Central Asian Gas

Today the issue is more about gas than oil but again Central Asia and the Caspian region will play an important role. For Moscow to maintain its leverage over Europe, it must maintain or enlarge its share of the European gas market. It might have done so by restructuring its domestic gas market allowing for greater efficiencies resulting in increased volumes available for export or investing more in new - more challenging - domestic fields. As neither of these were pursued, choosing instead to spend its billions on corruption and a vanity project in Sochi, it must maintain a strangle hold on Central Asian gas and its transport to keep its European market share.

Kazakhstan, Uzbekistan and Turkmenistan are the three Central Asian Republics with significant hydrocarbon reserves. According to the International Energy Agency (IEA), Central Asia has five billion tons of recoverable reserves. While Kazakhstan has significant foreign investments developing its gas fields, the same cannot be said for Turkmenistan or Uzbekistan. This has been the result of a number of factors but most significantly because of the reluctance of the host governments to engage with foreign companies as a result of pressure from Moscow as well as corporate concerns about the investment climate.

Providing insulation to pursue our strategic interests

The Russian invasion of Ukraine and the annexation of Crimea despite international law, accepted norms of territorial integrity and even Russia's own signature on the 1994 Bucharest Memorandum, has brought to the front of the minds of decision makers the reality of Moscow's aggressive revanchist foreign policy. Countries in what Moscow calls its, "privileged sphere of influence" are concerned and looking to the United States for reassurance.

Despite previous U.S. Administration's National Security Strategy calling Central Asia an "abiding foreign policy priority" it is natural, given the retrenchment of the Obama Administration, for these countries in Central Asia to question if they have any other options. Yet, Putin showing his true colors along with his bare chest, provides an important opportunity in Central Asia and Europe. It would be wrong in the face of a successful Russian military invasion for the U.S. to ask countries in the region to do what is most difficult in their relationship with Moscow. However, if we articulate and pursue a clear policy that provides Central Asia and Europe benefits

that their leaders and citizens value, then we can be successful.

Prompt action is required

In 2008, following the invasion of Georgia, there was a similar moment. While the trigger for the conflict was less clear in the minds of many in Europe, the global financial picture was more dire and the Bush Administration, in which I served, was in its final months. Despite what CNN's Fareed Zakaria incorrectly asserts, the Bush Administration took significant steps to show Russia that the international community would not allow these actions and to discourage him from going on to Crimea - the principle concern at the time for Putin's next step - if Russia paid no price for its invasion of Georgia.

Regrettably, the lack of resolve and preparedness by President Sarkozy delivered a less than sound cease-fire agreement. What isolation and costs Russia would have incurred from the Georgian invasion were wiped clean as a result of the Obama Administration's "Russia reset." Europe was not going to implement something it did not have Washington's support for and Putin, seeing that he paid no price for Georgia, saw no reason not to move on to Crimea when he judged it in his interest.

Recommendations

Cross the Caspian: Link the hydrocarbon rich nations of Kazakhstan, Turkmenistan and Uzbekistan with Azerbaijan including support for a Trans-Caspian gas pipeline system.

If we are to decouple Central Asia from Russian dominance, we need to enhance its connection with Azerbaijan. Azerbaijan is the most dynamic country

with a growing economy in a region of great importance. The majority of the supplies exiting Afghanistan as a result of the U.S. drawdown transit Azerbaijan along the Northern Distribution Network. Baku has demonstrated itself as a valuable, stable and reliable partner in a difficult region addressing threats emanating from the Middle East and Central Asia.

Azerbaijan, Kazakhstan and Turkmenistan, along with Russia and Iran make up the littoral states of the Caspian Sea. Greater cooperation between Baku, Astana and Ashgabat, with the support of the U.S., would enhance the ability to exploit the resources of the Caspian sea and counter efforts by Moscow and Tehran to prevent a transit pipeline for gas from the west coast of the Caspian Sea from linking up with Baku's Southern Gas Corridor.

Despite pressure from President Putin, Azerbaijan President Ilham Aliyev has already demonstrated the vision, courage and leadership to resolutely state that Azerbaijan's gas is for European markets and pursue the Southern Gas Corridor. All that is needed for Central Asian gas to find markets in Europe is the ability to cross the Caspian sea.

This is preferable to the TAPI (Turkmenistan Afghanistan Pakistan India) Pipeline which, while it would have the benefit of bringing Afghanistan needed transit revenue, has several seemingly insurmountable obstacles. India, for its part, is focused on importing LNG - hopefully from the United States - to meet its growing energy needs.

Appoint a Special Envoy for Nagorno-Karabakh: Yesterday Georgia, today Ukraine, tomorrow Azerbaijan?

Putin's goal is to destabilize those former Soviet Republics that reject Moscow's claim of a "privileged sphere of influence" and choose to determine their own future. This is why Moscow is supporting separatists in Transnistria, recognized as independent the Georgian regions of South Ossetia and Abkhazia, annexed Crimea, are working to destabilize Ukraine's east and why they support Armenia's occupation of approximately 20 percent of Azerbaijan. We need to recognize that if what we once called the "frozen conflicts" left to us after the breakup of the Soviet Union are to be peacefully resolved, it will not be by following Moscow but by providing active diplomatic leadership. A peaceful resolution of the conflict in Nagorno-Karabakh is in the interest of Baku and Yerevan. It would return territory to Azerbaijan separated for over twenty years and provide Armenia an opportunity to climb out from under Moscow's stifling protection. It is only Russia that is the status quo actor.

The Obama Administration needs to be shaken out of their complacency and recognize that action is required to prevent an ever increasing possibility of armed conflict in Nagorno-Karabakh. Bloodying Azerbaijan - Putin's greatest vulnerability in controlling Caspian oil and gas - perhaps by claiming to come to Armenia's assistance, which is a member of Moscow's Customs Union and is under Russia's security umbrella, is all too possible.

As Secretary Kerry has demonstrated that Iran, Syria and North Korea will fill his calendar, what is required is a Special Envoy who has the respect of those in the region and is able to push Moscow for greater cooperation. It is my view that former Secretary of State Rice would be an ideal candidate. If not, the Obama Administration should pick someone of

similar gravitas, energy, established relationships and intellect.

Engage, uphold principles and moderate expectations:

OPIC

Putin's recent actions show that while the United States and the European Union want to do business in Central Asia, Moscow wants to own it. Now is the time to actively engage to develop Central Asian energy. The Overseas Private Investment Corporation's (OPIC) Central Asian activity should be reviewed with a view to supporting US exploration and production activities in Uzbekistan and Turkmenistan.

Elevate Engagement

No sitting US President has ever visited the region. This compared to Russian and Chinese leaders who, through regional and bilateral meetings, see the Presidents of Central Asia several times a year. We cannot compete with the amount of attention that Russia or China pay to the Central Asian leaders nor do we need to in order to demonstrate our interest. President Obama should travel to Baku, Azerbaijan to meet with President Ilham Aliyev and the Presidents of Kazakhstan, Turkmenistan and Uzbekistan to demonstrate our resolve to see energy supplies from the east coast of the Caspian joining with those on the west destined for markets in Europe.

Uphold Principles

The United States must always stand by our values, we never go wrong when we are an example to the world of the values that are at the very core of the formation of our country. When advancing these values internationally we do ourselves, our national interests, or our effectiveness no favors if we make proclamations without an understanding of the realities of the country, region and process within which the

recipient lives. In the case of Central Asia and the Caspian region, this includes neighbors such as Russia, China and Iran.

Realistic Expectations

Our policy should also be influenced by our own experience. We do not have the carrots for Central Asia and the Caspian region that we did for former eastern block countries. We need to come to terms with the fact that advancing free market principles, democratic principles or human rights advancement in Central Asia will not follow as quickly as was the case in Central Europe. Unlike in Central Europe, we do not have the incentive of NATO membership, EU candidacy, or debt forgiveness to leverage greater reform. Nor are they hearing only from the the US or Europe on the benefits of democracy. While Central Asia lacks a regional organization that includes the appropriate countries and promotes values and security, the European Union or NATO membership is not a possibility.

China Tilt: Russia-China tension in Central Asia.

It was the Great Game between the British Empire and Imperial Russia in the late 1800s that brought the Khanates of Khiva and Bukhara and British soldiers Connelly and Stoddard's experiences in the bug pit that defines this historic term. The Great Game for Central Asia in the future will be one between reactionary Russia and Mercantilist China. Russia has many advantages. Beginning with its history, not just the seventy years of the Soviet Union that linked Central Asia to Moscow but also earlier gains of Czarist Russia. Leaders, bureaucrats, academics and common people throughout Central Asia have had a link with Russia. Education, language, business, diaspora remittances and the ubiquitous Russian language television, point to the connections between Russia and the former Soviet Central Asian Republics. However,

the demographic reality of Russia demonstrates that in the future Moscow will not be the magnet it has been. Compare this with China. China, through the Shanghai Cooperation Organization (SCO) and directly, is investing large sums of money throughout Central Asia on huge road projects, rail projects, hydropower projects and other building projects. They are active in concessions on hydrocarbon projects including China's CNP acquisition of ConocoPhillips share of Kazakhstan's Kashagan oil field in the north Caspian.

China has demonstrated that its interests in Central Asia are economic, energy and to promote stability. It recognizes that it wants to have a common cause with the Central Asian Republics, principally Kazakhstan, to stifle separatist sentiments of the ethnic Uyghur in Xinjiang in its west. This is not to say that China's vast population superiority does not raise concerns of excessive demands following investment from Beijing among the leaders of Central Asia.

During the last decade in Central Asia, the only reason for Russia and China to work together in Central Asia, where they should be competitors, has been to counter what they see as US hegemony extending to military bases along their periphery.

We need not put ourselves in a position of having our interests in Central Asia characterized as countering Russia's historic role or China's growing role in the region. Nor, do we want to be seen as joining a compact deciding with other powers what is best for the government and people of Central Asia. We must have direct bilateral relationships to advance our national interest.

However, we need to be realistic. The Obama Administration is being questioned for pulling back from the strategically important Middle East, questions remain about what - if any - residual force will remain

in Afghanistan and President Obama's "Asia Pivot" has largely failed to materialize. There are real doubts in Central Asia about our future role.

We need to provide insulation for these countries when another power moves to serve its interest by bullying. When there are three powers, as Otto von Bismarck said, it is better to be in a group of two than to be the one facing the two.

Therefore, not in a way that could be described as a condominium, We should explore tilting towards China. China's foreign policy in Central Asia is much more benign as compared to Moscow who wants to and does meddle in their domestic elections and dictates with whom they can sign military and diplomatic alliances. In addition to moderating Moscow's appetite for influence in Central Asia, it may also have the benefit of not confronting China in Central Asia on its western border as the United States strengthens alliances - commercial, diplomatic and defense - to China's east and south.

Conclusion

I have lived, worked and traveled to this region for over two decades. I meet with the Presidents and Ministers in Central Asia. They are not looking to complicate their relationship with Russia, nor do they see themselves as Belarus or Armenia where their options are dictated by Moscow. They need to see that while our interests may be more limited, we will exercise leadership in pursuit of policy goals.

Hydrocarbon deposits in Central Asia and the Caspian region will be developed. The question is: will they be developed as an independent source adding to the options customers in Europe and Asia have or will they be exploited by Moscow enhancing Putin's ability to use energy as a political weapon.

It is wrong to suggest that Gazprom will not be a factor in Europe's energy mix into the future and we should not set as a goal this unachievable ambition. However, what is needed is for more market forces, more options to exist so when Putin picks up his energy tool for political purposes again, as he surely will, a proper exploitation of the Caspian resources along with US LNG and greater renewables will prevent it from being a useful weapon.