



Black Sea Connectivity and the South Caucasus

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March 2021



Frontier Europe Initiative

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Black Sea Connectivity and the South Caucasus

There are growing political, security, trade, and economic interests for multiple actors in the Black Sea region. These actors include traditional Black Sea powers Russia and Turkey; Western-oriented young democracies Bulgaria, Romania, Ukraine, and Georgia; supra-national actors like the EU and NATO; the global super-power, the United States; the world's fastest growing economic power, China; resource-rich countries in Central Asia, including Afghanistan; and of course Iran, which has demonstrated limited interest in the Black Sea in the past, but may become more active, as some recent statements and diplomatic efforts suggest following the change of administration in Washington.

The United States and the EU share a common interest in enhancing Black Sea connectivity to the Caspian region via Georgia and Azerbaijan, which would enable more strategic and commercial access to Central Asia while balancing Russian, Iranian, and Chinese influence in a strategically important region. There is a need for greater coordinated efforts between key transit countries of the region to establish higher efficiency and low-cost transportation, and to enhance the interest of long-term strategic partners who have facilitated regional energy projects over last two decades. The countries of the region must understand that if the cost of coordination is too high, opportunities for the region will be lost. It is a reality that the scale of current non-energy trade and transit between Central Asia and Europe via the South Caucasus is not high enough to attract significant political-security, or business interest.

This report will explore the potential for greater trade connectivity between Europe and wider Central Asia via the Black Sea and the South Caucasus.

Security Environment in the Black Sea Region

Following the break-up of the Soviet Union, the United States, together with Turkey and other Western allies, led the process of strengthening the political and economic sovereignty of the former Soviet Bloc countries like Romania and Bulgaria, as well as newly independent countries in the South Caucasus and Central Asia. Turkey was a major anchor and channel of Western political, strategic, and economic interests in the Black Sea-Caspian region.

This collaborative effort brought about the development of vibrant energy, trade, and transit connections between the Black Sea-Caspian region and the Mediterranean, delivering huge economic and political benefits to all the producing and transit countries of the region: Kazakhstan, Turkmenistan, Azerbaijan, and Georgia. Turkey was, and continues to be, the major beneficiary of the economic, political, and security benefits of the East-West energy and transportation corridor, and of the

expanding pipeline, railway, highway, and port infrastructure linking the country to Caspian resources and markets. Further, the enlargement of NATO and the EU brought more security and economic development to the western shores of the Black Sea – to Bulgaria and Romania.

But developments of the last decade drastically changed the strategic environment in the Black Sea-Caspian region. Due to a much weaker US-Turkish alliance since the start of the war in Iraq, and the overall decline of US presence and leadership in the region, the Russian Federation has regained significant power and influence in the Black Sea region.

The prelude for Russia's increased role in the Black Sea region was the 2008 invasion of Georgia and subsequent military occupation of several areas in close proximity to major transportation links. Georgia since 2008, which is in close proximity to major transportation links connecting the Caspian region to the Black Sea, Turkey, and Eastern Mediterranean. This was followed by the annexation of Crimea in 2014, which allowed Russia to exponentially increase its military presence in the Black Sea region, and to establish a platform for power projection¹, aimed at not only the Black Sea, but the Mediterranean as well. Since 2014, Russia has moved a significant number of anti-air and anti-surface missile systems onto the Crimean Peninsula that could hit targets in most of the Black Sea region. By controlling Crimea, Russia has now almost complete strategic dominance over the Black Sea. This situation, though, re-emphasized the importance of NATO membership for Turkey, despite the deterioration of Turkey's bilateral relationships with several leading NATO member countries. The Russian-Turkish relationship is multifaceted and beyond the scope of this report, but it needs to be mentioned that Turkey tries to avoid a direct clash with Russia while trying to outsmart it in different theaters, when possible.

After the second war in Upper Karabakh, Russia increased its military presence in the South Caucasus, adding 2,000 peacekeepers in Karabakh to an already significant military presence in Armenia and in the breakaway regions of Georgia – Abkhazia and Tskhinvali region. This military presence allows Russia to establish control over the major elements of East-West transit infrastructure and communication lines on relatively short notice. After the use of military force in Georgia in 2008 and in Ukraine in 2014, this threat is not just perceived, but real. Military success in Georgia and Ukraine also emboldened Russia to move more aggressively in the Middle East, especially with its presence in Syria. The strategic significance of the weak Western response to Russian aggression in the Black Sea region has become more evident as time has passed.

¹ *Department of Defense Press Briefing by Gen. Breedlove in the Pentagon Briefing Room*, (February 25, 2015), <https://www.defense.gov/Newsroom/Transcripts/Transcript/Article/607020/department-of-defense-press-briefing-by-gen-breedlove-in-the-pentagon-briefing/>

The outcome of the military conflict in Upper Karabakh between Azerbaijan and Armenia also has significant implications beyond the regional perspective. The war demonstrated that power politics is alive and well, and that with great power consent (in this case Russia and Turkey), smaller actors - in this case Azerbaijan - can achieve their national objectives with military means more efficiently than with diplomatic means. Conflict further increased Armenia's security dependence on Russia. But Azerbaijan's success is not without cost either. Azerbaijan was forced to agree to delegate part of its sovereign rights to the Russian military over some parts of de jure Azerbaijani territory. The majority of Upper Karabakh will remain under Armenian control, secured by Russian military peacekeepers. The access road via Lachin from Armenia to Armenian controlled territories of Karabakh will also be under Russian control. In addition, one important element of the November 9 trilateral agreement between Armenia, Azerbaijan, and Russia is that border troops of the Russian security forces (FSB) will be in charge of safety of access from Azerbaijan to Nakhichevan via Armenia. The agreement does not specify size and operational modalities of those troops, however.

At the same time, Turkey now has a greater role in the Caucasus' affairs. But it is no longer necessarily seen as the channel of Western interests in the region, but rather as representing its own national interest the way President Recep Tayyip Erdogan and his domestic allies understand it. This is not news. The renewed calls for the six-party union with three South Caucasus countries, Iran, Russia, and Turkey, is a Turkish initiative, which President Erdogan first introduced as the Pact for Stability and Cooperation in the South Caucasus in the 1990s. This initiative has support from all three major regional powers - Russia, Turkey, and Iran² - because it excludes Western institutions and countries from South Caucasus affairs, which seems to be the objective here.³ There is no clarity so far on the Armenian or Azerbaijani attitude to this initiative, but Georgia affiliates itself to Western institutions, and realistic or not, desires greater Western participation in South Caucasus affairs. Obviously, Turkey is a part of NATO and supports Georgia's NATO membership as well, so participation in this new initiative doesn't necessarily mean closing doors to all Western institutions for the participant countries.

But question is what value this new grouping can bring to Georgia. Would it help to restore the territorial integrity of Georgia? Would Russia move its troops out of Georgia and reverse its decision on recognition of independence of the separatist regions of Georgia? These are highly unlikely developments, which makes Georgia's participation in this type of union impossible.

In the context of opening transportation links between Azerbaijan and Armenia, as a part of the post-conflict settlement, there may also be initiatives to consider re-opening the rail link between Russia and

² "Zarif: Iran seeking to form six-party union in the Caucasus region," *Tehran Times*, (January 26, 2021), <https://www.tehrantimes.com/news/457391/Zarif-Iran-seeking-to-form-six-party-union-in-the-Caucasus-region>

³ To many in the Caucasus, this situation resembles one hundred years ago, when Bolshevik Russia and the newly created Republic of Turkey (after the fall of the Ottoman Empire) collaborated in an effort to keep Western powers out of the Caucasus.

Georgia, crossing separatist region of Abkhazia, currently under effective Russian military control. This link is important to Armenia, and for many years Russia and Armenia have called on Georgia to allow its operations. Georgia always wanted this issue to be linked to the withdrawal of Russian troops from Georgian territory, and to the return of the displaced ethnic Georgian population of Abkhazia, who constituted a majority of the pre-conflict Abkhazian population. In the past, Azerbaijan opposed the opening this railway connection between Russia and Armenia out of fear that it could become the source of additional military supplies to Armenia. In the new geopolitical realities, when Azerbaijan itself plans to allow Russian transit to Armenia, this may become a less sensitive issue for Azerbaijan. However, Georgian pre-conditions for opening the railway will not change significantly. In addition, Russia's real appetite to open this railway was always at question. Any normalization of the relationships between Georgians and Abkhazs will be seen as a threat to Moscow's ability to manipulate the situation in the occupied regions of Georgia.

As a result of all these evolving parts in the greater Black Sea-South Caucasus puzzle, we are moving toward a new status-quo in the region – one that is still shaping up, with different actors facing different challenges as well as opportunities.

Energy Connectivity Dimension in Black Sea and Beyond

The Black Sea is a significant international waterway for energy flows. Multiple seaports specialize in oil and oil product exports, and two major natural gas pipelines cross the Black Sea, linking Russia and Turkey. In addition, significant oil and natural gas flows via land pipelines in the Black Sea region from the Caspian, via Georgia, to Turkey and onward to European markets.

Russia exports more than two million barrels a day from Black Sea outlets, mainly from Novorossiysk. In addition, a significant part of Kazakhstan's oil export goes to market via the Caspian Pipeline Consortium (CPC) pipeline to the Company's Marine Terminal in Novorossiysk. This pipeline shipped more than a million barrels a day (total of 60 million tons) in 2020 via 572 vessels.⁴ Relatively smaller volumes are also exported from Georgian ports of Supsa, Batumi, and Kulevi. Overall, more than 3 percent of the world's daily oil supply transships through the Black Sea.

Russia has traditionally dominated the Turkish natural gas market since the 1990s. In 2018, Russia sold 24 billion cubic meters (bcm) of natural gas to Turkey, making it one of the most significant markets for Russia's Gazprom. Two major pipelines directly connect Russia to Turkey via the Black Sea. The Blue Stream pipeline, with a capacity of 16 bcm, was commissioned in 2005. The TurkStream pipeline has a capacity of 31.5 bcm annually and started supplying gas to Turkey in January 2020. These two pipelines

⁴ "Oil shipments via CPC Marine Terminal in 2020 fell by 6.7% YoY," *Port News*, (January 12, 2021), <https://en.portnews.ru/news/307290/>

allow Russia to bypass Ukraine for its supplies to Turkey, Bulgaria, and other markets in Southern Europe, and serve not only commercial, but also major geopolitical objectives of Russia, aimed at increasing sales and greater dependency on Russian gas in Turkey and the Balkans. The success of Russia in this direction is obvious. From Jan. 1, 2021, Russia began supplying gas to Serbia and Bosnia and Herzegovina. Gas from Russia is transmitted by TurkStream and further across Turkey. It then flows via Bulgaria's national gas transmission system to consumers in Serbia and in Bosnia and Herzegovina.

But Turkey also made sure that alternative supplies of natural gas are available for Turkish needs. The so-called Southern Gas Corridor, connecting Azerbaijan, Georgia, and Turkey and then Greece, Albania, and Italy, has allowed Turkey to buy more Azerbaijani gas at a better price. Turkey has contracts to purchase more than 12 bcm from Azerbaijan, and transit infrastructure crossing Azerbaijan and Georgia allows Turkey to get these volumes of gas with no geopolitical strings attached. Turkey is also buying more LNG from the US and other sources, enabling major diversification from dependency on Russia. With diversification of potential sources, Turkey now has major leverage on price negotiations with Russia's Gazprom.

In terms of the oil and gas infrastructure connecting Caspian resources to European markets, there are currently several key transit energy infrastructure elements with international significance. These include two oil pipelines connecting oil-producing fields in the Azerbaijani section of the Caspian Sea to the Georgian Black Sea port of Supsa and the Turkish Mediterranean port of Ceyhan: the smaller, 100,000 barrel per day capacity Baku-Supsa pipeline, and the larger, million-barrel capacity Baku-Tbilisi-Ceyhan (BTC) pipeline. At present, around 700,000 barrels of oil flows through these two pipelines daily, supplying crude oil to Turkish, Israeli, and other Mediterranean refineries. The BTC pipeline currently carries mainly crude oil from offshore Azeri-Chirag-Gunashli (ACG) fields and Shah Deniz condensate from the Azerbaijani section of the Caspian Sea. In addition, other volumes of crude oil and condensate continue to be transported via BTC, including from Turkmenistan, Russia, and Kazakhstan.

Another infrastructure network of international significance is the so-called South Caucasus Gas Pipeline, also known as the Baku-Tbilisi-Erzurum natural gas pipeline. It began with the production of 8 bcm of natural gas annually at the Shah-Deniz field near Baku. Since 2007, it has been used to export gas to Georgia and Turkey. This pipeline, and the natural gas from the Shah-Deniz field, has provided Georgia with a much-needed alternative to Russian natural gas supplies, and has helped Turkey to diversify its supplies as well. This pipeline became the basis for the larger pipeline system crossing six countries, the Southern Gas Corridor (SGC). Projected as \$45 billion project, and completed under budget at \$33 billion⁵, was one of the largest energy projects in the world between 2014 and 2020, allowing production of an additional 16 bcm per year. The largest recipient of the gas will be Italy. The

⁵ "Rapid Response: The Southern Gas Corridor opens today," *Atlantic Council*, (December 31, 2021), <https://www.atlanticcouncil.org/blogs/energysource/rapid-response-the-southern-gas-corridor-opens-today/>

system of pipelines has linked an upgraded South Caucasus Pipeline to the Trans-Anatolian Pipeline (TANAP) in Turkey, and the Trans Adriatic Pipeline (TAP), which stretches between Greece, Albania, and Italy. Natural gas deliveries to Italy started on Dec. 31, 2020. Initially, 10 bcm of natural gas will be exported through TAP each year, but capacity can be increased to 20 bcm. For comparison, Russia, the main supplier of natural gas to the EU, exported 176 bcm to Europe in 2020.

The importance of this project is hard to overstate. This chain of infrastructure projects directly connects natural gas fields in the Caspian Sea to EU markets. And while initial volumes will cover only about 2 percent of total European needs, the project has the potential for substantial expansion based on increased volumes from other fields in Azerbaijan, as well as from Turkmenistan. Turkmenistan has the world's fourth largest deposits of natural gas and an opportunity to become an important player in the European energy market. However, political and commercial considerations prevented the development of TransCaspian energy connectivity between Turkmenistan and Azerbaijan in the past.

Skeptics of the future of the hydrocarbon economy would say that Turkmenistan has missed its chance to become a significant supplier to European markets due to EU policies oriented toward green energy etc. But the opening of the new, larger scale pipeline, connecting Azerbaijan to Europe, will create an additional incentive for Turkmenistan to send some of its gas from relatively smaller Western fields to Europe via Azerbaijan. The Convention on the Legal Status of the Caspian Sea, signed in August 2018 by leaders of the Caspian littoral states, provides a framework for Azerbaijan and Turkmenistan to arrange for joint exploration and drilling, as well as long-stalled pipeline projects.⁶ On Jan. 21, 2021, Azerbaijan and Turkmenistan reached a preliminary agreement on the joint exploration of a once-disputed section of an undersea oilfield, signaling progress in this direction. In a symbolic gesture of the spirit of partnership, parties signed a memorandum on the mutual intention to jointly explore and develop the Dostluq (Friendship) undersea field, which was previously called Kapaz by Baku and Serdar by Ashgabat.⁷

This may be a major step forward in building the TransCaspian energy partnership, allowing larger volumes of energy to flow toward the Black Sea and Mediterranean. Connecting Central Asian energy resources to Europe via the Black Sea and Turkey should remain a geopolitical priority for the regional countries and their partners in the EU and the US.

⁶ Mamuka Tsereteli, "Landmark Caspian Deal Could Pave Way for Long-Stalled Energy Projects," *World Politics Review*, (September 2018), <https://www.silkroadstudies.org/publications/joint-center-publications/item/13308-landmark-caspian-deal-could-pave-way-for-long-stalled-energy-projects.html>

⁷ "Azerbaijan, Turkmenistan Finally Reach Deal On Lucrative Caspian Sea Energy Field," *RFE/RL*, (January 21, 2021), <https://www.rferl.org/a/azerbaijan-turkmenistan-deal-caspian-energy-field-dostluq-/31061674.html>

It is important to mention that some volumes of Caspian oil are moving toward Eastern Europe via Black Sea ports as well. The oil shipments from Azerbaijan to Ukraine, for example, grew by 20 percent in 2020, shipping oil by rail to Georgian ports and then by sea to the Ukrainian ports of Odessa and Pyvdenny (Yuzhnyi). Azerbaijan became one of the key suppliers of crude oil and oil products to Ukraine in 2020.

A conversation about energy developments in the Black Sea area would be incomplete without mentioning some of the recent natural gas discoveries in Turkey. In June 2020, Turkey's state-run energy giant TPAO announced discovery of the country's largest natural gas reserves to date with an initial estimate of reserves of 320 bcm, later raised by President Erdogan to 405 bcm. This discovery may have a positive impact on the Turkish energy balance. In addition, there are new energy discoveries in Romania and Ukraine, though complicated by political, economic, or technical factors.⁸

The EU's policy to move away from a hydrocarbon economy toward green and sustainable energy will impact the decision-making of the individual members on their own energy mix. Down the road, this will have a significant impact on prioritization of regional energy projects. However, energy security of the Black Sea countries for the foreseeable future will depend on reliable sources of hydrocarbons, and improved exchange of natural gas and electricity power via interconnectors, allowing greater efficiency in utilization of regional resources.

Georgia and Turkey represent a good example of cooperation. A significant volume of electric power generated from the relatively cheaper, and definitely cleaner, hydro resources of Georgia flows to Turkey. The high voltage transmission lines between Georgia and Turkey allows larger supply of electricity to Turkey. Combining hydrocarbon resources of Azerbaijan and the vast hydro resources of Georgia may significantly increase power generation and transmission, with implications for the entire Black Sea region. Under the new geopolitical realities, Armenia can also join the operation, utilizing its nuclear power generation capacity. By receiving electricity in the East and delivering it to Western neighbors, the Turkish electricity system can allow swap energy export operations from the South Caucasus countries, contributing to the energy security of the entire Black Sea region, but also to the economic development of all three South Caucasus states.

⁸ Iulia Joja and Richard Kraemer, "Black Sea Gas Campaigning," *Middle East Institute*, (December 14, 2020), <https://www.mei.edu/publications/black-sea-gas-campaigning-2020>



Photo by Daniel Mihailescu via Getty Images

Black Sea-Caspian Connectivity

As mentioned from the beginning, the Black Sea provides an important trade and transportation linkage between the Mediterranean, Central and Eastern Europe, Russia, South Caucasus, and Central Asia. The largest Black Sea ports of the littoral states serve not only domestic markets, but also transit cargos moving in and out of the region. There is relatively well-established infrastructure connecting countries to their major ports, but there is a lack of linkages between different regions and countries, which could maximize trade and transit opportunities. The missing elements include connectivity between the countries of Eastern and Central Europe, between Eastern and Western shores of the Black Sea, and between the Caspian and Black Seas.

The Three Seas Initiative (3SI) aims to promote cooperation for the development of infrastructure in the energy, transport, and digital sectors for twelve EU member states around and between the Baltic, Black, and Adriatic Seas: Austria, Bulgaria, Croatia, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, and Slovenia. The key idea of the 3SI is to promote sustainable, innovation-based, smart connectivity between countries and to break the decades-long legacy of the post-World War II era in Central and Eastern Europe, when almost entire infrastructure development in the region was tied to Soviet infrastructure, ensuring energy and infrastructure dependency on Russia. The initiative targets new investments, economic growth, and energy security by supporting infrastructure, energy, and digital interconnectivity projects, with the ultimate goal of strengthening the countries' security and integration with the rest of Europe.

Participant countries have already agreed to multiple priority interconnectivity projects, from liquified natural gas (LNG) terminals in Krk Island, Croatia, Świnoujście, Poland, and Klaipėda, Lithuania, to new North-South highway connections, new and existing rail lines between countries in the region, a water corridor between the Danube, Oder, and Elbe rivers, and digital and various telecommunications interconnectivity projects.

Unfortunately, the initiative currently only covers EU member states, leaving out several countries from the Black Sea region with similar connectivity problems and historical pasts. Georgia, Moldova, and Ukraine in particular deserve consideration, due to their Association Agreements with the EU, and relatively higher degree of integration in EU regulatory and governance structures. But more importantly, the initiative should be looking more pro-actively to linkages between the Black Sea and Caspian, as a significant potential expansion for both resources, as well as markets for the countries involved in the initiative.

There is at least one project in the current list of 48 priority projects that involves Ukraine and Belarus and considers Moldova, Georgia, and Azerbaijan as partner countries: Viking Train. Viking Train is a joint project of the Lithuanian, Ukrainian, and Belarusian railways and stevedoring companies in ports of Klaipėda, Chornomorsk, and Odessa. The route crosses Ukraine, Belarus, and Lithuania and links the network of container lines of the Baltics and Black Seas, as well as the Mediterranean and Caspian Seas.

Other projects important for the Black Sea's connectivity with the rest of Europe include a rail and road connection between Romania's city of Constanta and Poland's port of Gdansk, as well as a rail route between Gdansk and Ukrainian ports.⁹ These lines will be competing with an alternative North-South link between Novorossiysk and St. Petersburg, promoted by Russia.

Constanta and the Ukrainian ports of Odessa, Chornomorsk and Pyvdenny will play a particularly important role in linking Black Sea traffic to European countries. These ports should help link the Black Sea with the Caspian Basin to facilitate trade, transportation, and connectivity. Key objectives in this regard will be improving Black Sea maritime and digital connectivity between Georgian ports and ports in Ukraine, Romania, and Bulgaria; improving land infrastructure connectivity between Caspian Sea ports in Azerbaijan to Georgian ports on the Black Sea; and improving Trans-Caspian maritime, pipeline, and digital connectivity. Implementation of these priorities will create much more favorable conditions for the success of the 3SI by linking it with energy and other resources, as well as markets of significant size.

The largest Black Sea ports can handle increased traffic between the Central Asian region with Europe. The most important ports include Constanta in Romania (100 million tons capacity per year), Odessa/Pyvdenny/Chornomorsk in Ukraine (around 100 million tons capacity), Varna in Bulgaria (about 10 million tons), and Georgia's Poti (about 12 million tons) and Batumi (18 million tons, of which 15 million tons is oil and oil product capacity). Constanta is the largest and deepest port of the Black Sea, servicing the largest ships allowed to enter the Black Sea due to the capacity restrictions of the Bosphorus straight, which currently stands at 10,000 containers (Twenty-foot Equivalent Unit, or TEU). This is why Istanbul is a major port of consolidation of the container traffic to and from the Black Sea. Istanbul's Port of Haydarpasa, technically outside of the Black Sea, is handling 60 percent of the Black Sea container traffic, distributed or collected mostly by 2,000 TEU feeder ships inside the Black Sea. Although vessel sizes cannot exceed 10,000 TEU, there is at least one service from Asia with ships of that size which makes weekly calls at Istanbul, Constanta, and Odessa. Ports on the Eastern Black Sea (i.e. Georgian ports) have draft restrictions and cannot take vessels of more than about 3,000 TEU. Georgia plans development of the Anaklia port with deeper draft, but prospects of this port are not clear due to disagreements between the government and the Anaklia Development Consortium, which delayed the process of development, as well as current market conditions.

One important consideration in the development of Black Sea port infrastructure is availability of cargos and market size, serviced by the ports. One significant development is the growing scale of the Ukrainian ports near Odessa, which is determined by Ukraine's greater export and import needs. Following its annexation of Crimea, Russia built a bridge over the Strait of Kerch, which now connects Russia to annexed Crimea. The height of the bridge reduced the maximum size of ships entering the Azov Sea by

⁹ "Black Sea to Baltic Trade Route," *Port Strategy*, (December 15, 2021), <https://www.portstrategy.com/news101/world/europe/black-sea-to-baltic-trade-route>

30 percent. In addition, the Russian military control of the entry to the Azov Sea determined the need for Ukraine to use other ports for its trade needs. Ukraine is planning to gradually privatize all of its ports going forward, aimed at increased efficiency of operations. Prospects of growth of Ukrainian ports are significant, based on the size of the Ukrainian economy and significant export and import needs of the country.

Ukrainian, Romanian, and Bulgarian ports can play larger role servicing not only their respective countries, but other European countries as well. Varna and Burgas in Bulgaria could be connected to Albanian Port of Vlore on the Adriatic Sea and deliver cargos from Central Asia to the Italian market, bypassing a congested Bosphorus. Constanta is capable of servicing the wider Eastern and Central Europe area, and entire Balkan region and Danube basin as well. The port has a capacity to handle one million containers (TEU) with the potential to expand to 4.5 million containers, if there is demand. The problem is that Constanta, like most ports on the Black Sea, operates below its capacity. The scale of utilization of port capacity is determined by the size of the local and transit markets serviced by the port. Increased connectivity of Constanta by rail or other transportation means may increase the cargo flow to the port. The other option to increase cargo flow is to attract larger volumes of Asian cargos via the South Caucasus transportation corridor. This would also help greater utilization of the capacity of the existing Georgian Black Sea ports, Poti and Batumi. Poti, owned and managed by the major international consortium APM Terminals, has a capacity up to 12 million tons. Poti will have an additional capacity of more than 3 million tons with the development of the new Pace Terminal, owned and operated by Georgian-American Pace Group.¹⁰ Poti is mostly servicing bulk cargos and containers and transshipped 7.4 million tons in 2020. Batumi has a capacity of up to 18 million tons, but up to 15 million tons of capacity is for liquid cargos, mostly oil products. Batumi serviced 3.5 million tons of cargos in 2020. The Batumi port is owned by Kazakhstan's KazTransOil.

Georgia also has two other ports. The first is an oil port at Supsa, with a capacity of 8 million tons, which is connected to the Baku-Supsa pipeline and currently ships about 4 million tons of Azerbaijani oil annually. The other is Kulevi, owned and operated by a subsidiary of the State Oil Company of Azerbaijani Republic (SOCAR) with a capacity of 6 million tons of mostly oil products and which shipped 1.7 million tons of oil products in 2020. It is noticeable that ownership of Georgia's port systems is diversified and balanced between different actors.

Total transshipment of all Georgian ports, both inbound and outgoing, was approximately 17 million tons in 2020, half of which was oil and oil products. Georgia's own export and import needs via ports do not exceed 4 to 5 million tons, so a great majority of the cargos serviced by Georgian ports are transit cargos. Bulk and container transshipments, servicing both Georgia's and transit needs, represent about nine million tons. One missing element in Black Sea connectivity is meaningful ferry traffic between

¹⁰ After completion in September 2021, the new Pace Terminal will handle 2.5 million tons of bulk cargo and 100,000 TEU of containers and will be equipped with the most modern and efficient equipment.

Georgian ports and the ports of Ukraine, Romania, and Bulgaria. Going forward, this element of infrastructure should be part of the transportation system, facilitating trade between Black Sea countries.

Georgian transit potential is closely linked with the needs of other countries. At this stage, the two main beneficiaries of the Georgian ports are Azerbaijan and Armenia. Both countries use Georgian ports for their export and import needs. The same is true for several Central Asian countries, namely Kazakhstan, Uzbekistan, Turkmenistan, and Tajikistan. But full utilization of the transit potential of Georgia, as well as its key transit partner country Azerbaijan, is constrained by several factors.

First, while trade between Central Asian and South Caucasus countries is growing, the volumes are still limited, and parties frequently use competitive transit routes via Russia or Iran. For example, during the summer months, despite the low draft, the Volga-Don canal is the most competitive route of transportation between the Caspian and Black Seas. In the event of a return to the Iran nuclear deal under the Biden Administration and subsequent lifting of the sanctions, Iran will again become a significant competitor to the South Caucasus transit corridor. But even before Iran is potentially opened, TransCaspian transit is limited in volumes. The newly renovated Port of Turkmenbashi in Turkmenistan, with a capacity of 17 million tons of bulk cargo and 10 million tons of liquid cargo (oil and oil products), transshipped about one million tons of bulk cargos in 2020. Meanwhile, China's trade with Europe via land transportation is growing. More than 12,000 trains transshipped an estimated one million TEU between China and Europe in 2020, leading to an increase in the cost of shipments by rail.¹¹¹² The South Caucasus Corridor must attract part of these cargos from Western China going forward by offering commercially competitive terms.

Second, there are limits of the transit infrastructure connecting Eastern and Western shores of the Caspian, and then to Black Sea ports of Georgia. New port infrastructure in Turkmenbashi, Aktau and Kurik in Kazakhstan, and the Baku International Sea Trade Port (Baku Port) in Azerbaijan allows faster and technologically more advanced transshipments of different types of cargos between Caspian ports with multi-modal transportation means. Baku Port increased its transshipments by 20 percent in 2020 and handled up to 5 million tons, of which 87 percent was a transit cargo. In 2020 Baku Port set a record for transshipments of both containers, as well as trucks (TIR). The maximum capacity of the Baku Port is

¹¹ China's overall trade in goods with Europe exceeds \$500 billion and the vast majority of shipments take place via sea lines. However, land transshipments from both the far East and Western China are growing, opening opportunities for Caspian-Black Sea transit infrastructure to attract some portion of trade in goods with relatively shorter shelf life. This is because transportation via the South Caucasus can ensure delivery of goods in about 20 days, while maritime transportation requires at least 40 days. The Indian sub-continent and wider Central Asia also enjoy significant trade with Europe, with even greater potential to grow, potentially also using the Caspian-Azerbaijan-Georgia-Black Sea transit.

¹² Greg Knowler, "Heavy demand doubles China-Europe rail rates", *JOC.com*, (January 14, 2021), https://www.joc.com/rail-intermodal/heavy-demand-doubles-china-europe-rail-rates_20210114.html

about 15 million tons, so there is a still significant room to grow, but it will take development of the supportive infrastructure of Transcaspien rail and car ferries, Ro-Ro ships, and container ferries to reach that capacity.

And finally, despite many episodic efforts, there is a lack of harmonization of the customs, border crossing, tariff, and other soft infrastructure elements, which is crucial for the competitiveness of the South Caucasus transportation corridor. Individual efforts of some countries in improving customs procedures or border crossings cannot improve the overall picture and attract cargos. More efforts are needed on the coordination and overall management of the corridor in order to fully utilize its potential. For example, a significant agreement was signed by Afghanistan, Turkmenistan, Azerbaijan, Georgia and Turkey on Nov. 17, 2017 in Ashgabat, Turkmenistan. The agreement initiated the Lapis Lazuli corridor, connecting Afghan provinces of Faryab and Herat to the Turkmenbashi port in Turkmenistan, and then through the Caspian Sea and South Caucasus Corridor to the Black Sea and Turkey, and ultimately to Europe and the Mediterranean. This route was intended to boost Afghan trade with Europe, as well as with all the countries along the Corridor, but its potential is still under-utilized. Without competitive commercial terms and conditions of smooth movement of cargos via the Black Sea-Caspian corridor, the potential for growth will not fully materialize.

All these factors mean limited cargo flow to the Black Sea ports of Georgia from the Caspian, and subsequently limited flows to ports in Ukraine or Romania. But more openness and economic growth of the wider Central Asia region will raise export and import needs. This should create a new opportunity for the South Caucasus Transportation Corridor to evolve into a major route for Asia-Europe trade. This will require a highly coordinated, systemic effort of all interested parties to ensure the successful functioning of this corridor. For all actors in the region, it is important to understand that if the cost of coordination is too high, opportunities for the region will be lost.

A potentially significant development for the region may be a re-opening of the direct railway line between Azerbaijan, Armenia, and Turkey as a part of the post-war settlement over Karabakh. Obviously, it will take time, investment, and significant political will to implement this element of the agreement. But if and when fully implemented, this route may attract Russian cargos destined for Turkey, as well as some volumes from Central Asia, which means they will by-pass Georgian Black Sea ports. Also, there may be some volumes redirected from the Baku-Tbilisi-Kars (BTK) railway toward the Baku-Nakhchivan-Turkey direction, although volumes are insignificant. The BTK railway operates below its planned capacity of 6.5 million tons. In 2020, transshipments stood at 10,500 TEU, which is a tiny fraction of the capacity of the railway.

While very important for Azerbaijan, and potentially for the normalization of the Armenia-Azerbaijani-Turkish relationships going forward, the real transit potential of the Nakhchivan corridor will be limited for the foreseeable future due to political, geographic, infrastructural and financial reasons. At the same time, this new potential significantly improves the strategic position of Azerbaijan, while opening

opportunities for Armenia as well, which found itself in a very painful position after the military defeat in Karabakh.

In terms of Russia's use of the Nakhchivan corridor, it is more realistic to expect greater utilization by Russia of Iranian infrastructure to trade with India and China via Iranian ports of Bender Abbas and Chabahar. This North-South trade route is a major competitor for the Caspian-Black Sea route, since it may also attract increased volumes of Central Asian cargos destined for Asian markets. The Nakhichevan corridor may be attractive for some volumes of specific Russian cargos going to Turkey, but Russia would prefer Iran as a transit to access Asian markets, and its own Black Sea ports to access the Eastern Mediterranean and Europe.

At the same time, a new reality cannot change Georgia's role as the critical transit country for energy resources. Caspian oil and gas will continue to flow via Georgia to markets for many years to come. The South Caucasus corridor will remain the shortest transportation link between Central Asia and the Black Sea and Eastern Europe. It will be important for Georgia and Azerbaijan, as well as other partner countries, to work together on issues of container and general cargo transit. Georgia needs to take a pro-active position in this process. Attracting cargos for European markets from wider Central Asia, including Western China, Afghanistan, and maybe the Indian subcontinent, is a realistic target, if all the transit countries can collaborate. Significant public funding, invested in Caspian ports and other infrastructure in Turkmenistan, Kazakhstan, and Azerbaijan, as well as private investments in Georgian ports, can only be justified if those volumes of cargos are attracted by lower cost and efficient movement of cargos.

This process will require major diplomatic effort and coordination, as well as political leadership. In the past, the most successful infrastructure projects in the energy sector became possible with leadership and strong diplomatic effort from the US, backed by Turkey and regional leaders. Countries of the region need to make extra efforts to re-engage with major actors. Particular attention should be paid to the EU in particular, which may be a major beneficiary of the additional access routes to markets and resources. In the absence of such support from the outside, greater regional coordination is crucial. Georgia needs to adopt a more pro-active role in the process and invite partner countries and institutions to play an active role in facilitating trade and transit between Caspian Sea and Black Sea countries. International donor institutions, like the World Bank, European Bank for Reconstruction and Development, US International Development Finance Corporation, and Asian Development Bank can play a positive role in this coordination effort, and in funding projects that will facilitate greater transportation, as well as digital and energy connectivity. These institutions, together with the EU, can also help Georgia to capitalize its Deep and Comprehensive Free Trade Agreement with the EU. The re-arrangement of global supply chains in the post-Covid world opens an opportunity for Georgia to attract some industries oriented towards European markets. The economic security of Georgia will depend on its openness and ability to attract more export-oriented industries and activities. Collaborative efforts with Georgian partners will allow regional companies to be part of this process during the post-Covid recovery.



Photo by Mladen Antonov/ AFP via Getty Images

Conclusions

Countries of the Black Sea-Caspian region need a renewed effort in facilitating connectivity between Central Asia, the South Caucasus, and wider Black Sea region in order to maximize trade and business opportunities for all involved. It will be easier for countries to manage their post-Covid recovery, and achieve significant synergy of resources and markets for years to come, if they are interconnected. But more investment is needed for infrastructure development and harmonization of tariffs and border crossing procedures, with the common aim of increasing competitiveness of the entire transit and transportation system.

The US and the EU should partner in facilitating the build-up of a Belt of Economic Cooperation, which would include countries of Central Asia, the South Caucasus, the Black Sea Region, and Central and Eastern Europe. America's strategic interests in linking with allies in the Black Sea region and wider Central Asia are clear: maintain and improve strategic access to Central Asia, bolster the economic sovereignty of all countries involved, and enable them to withstand Russia's efforts to manipulate its smaller neighbors through economic and energy levers. Closer regional economic integration will also balance China's growing economic influence in Central Asia and Eastern Europe. Finally, stronger US and EU engagement in the South Caucasus will help balance potential Iranian influence, and in the event Iranian-Western relationships evolve positively in the future, can foster collaboration with Iran in the framework of greater Europe-Asia, and specifically Black Sea-the South Caucasus-Caspian connectivity.

There is a significant number of people at highest echelons of the Biden Administration's American foreign policy team who know Black Sea region well and who understand the needs of the countries, as well as the region as a whole. This includes the Secretary of State, the National Security Adviser, the Undersecretary of State, the Senior Director for Europe at National Security Council, among many more. Time will tell whether there is enough political will to focus on this region and to develop alliances and partnerships that ensure long term stability of the region, built on common political and economic interests. The critical factor will be US-Turkey relations, due to the weight and significance of Turkey as a regional power and NATO member state, which also understands the region better, and is invested both politically and economically deeper, than Western allies. Restoring the US-Turkish strategic partnership, based on common interests and facilitated by concessions from both sides, will bring much needed energy in Black Sea-Caspian regional developments. This may also allow creation of more vibrant and dynamic regional platform for the South Caucasus, where Turkey, the EU and United States will adopt a pro-active stance.

