

# CRS Report for Congress

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## Azerbaijan: Current Developments and U.S. Interests

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### Summary

This report discusses political, economic, and security challenges facing Azerbaijan, including faltering democratization, poverty, crime and corruption, and the unsettled conflict in Azerbaijan's breakaway Nagorno Karabakh region. Oil and natural gas resources and pipelines are briefly examined. A table provides basic facts and biographical information. This report may be updated. Related products include CRS Issue Brief IB95024, *Armenia, Azerbaijan, and Georgia*, updated regularly.

### U.S. Policy<sup>1</sup>

U.S. national interests in Azerbaijan include "strongly cooperating" on security and counter-terrorism, advancing U.S. energy security, supporting Azerbaijan's democratization and economic reforms, and mediating the conflict over Azerbaijan's breakaway Nagorno Karabakh (NK) region. Azerbaijan's stability is important because it borders Iran, Armenia, and the "strategic" Caspian Sea, and is a "vital link" in a trans-Caspian energy export corridor. The involvement of U.S. firms in exploiting Azerbaijani oil is "key" to the Administration's objectives of diversifying world oil supplies, boosting the regional economy, and promoting U.S. energy security and U.S. exports (*Congressional Budget Justification for Foreign Operations, FY2005*). Cumulative U.S. aid budgeted for Azerbaijan from FY1992 through FY2003 was \$435.21 million (FREEDOM Support Act and other program funds), reportedly about the same as



Source: Map Resources. Adapted by CRS. (08/02 M.Chin)

<sup>1</sup> Sources include Foreign Broadcast Information Service, *Daily Report: Central Eurasia*; Radio Free Europe/Radio Liberty, *Newsline*; *Eurasia Insight*; Economist Intelligence Unit; State Department and U.N. information; and Reuters and Associated Press wire service reports.

donated by the European Union. In FY2004, estimated U.S. aid was \$49.06 million, and the Administration has requested \$51.24 million for FY2005 (excluding Defense and Energy Department funds), focusing on reforming agriculture, the financial sector, the energy sector, the judiciary, and law enforcement, and on strengthening private business, export controls, and border security. Law enforcement initiatives include counter-narcotics training, support for combating corruption and trafficking in persons, advice on anti-terrorism and money laundering legislation, and help in implementing a criminal code. Azerbaijan signed an agreement in late 2003 to implement funding for some Comprehensive Threat Reduction (CTR) programs. Azerbaijan was designated as a candidate country for enhanced U.S. development aid from the newly established Millennium Challenge Corporation (but in May 2004 was not selected for FY2004 funds).

Congressional interests in Azerbaijan and the Caspian regions have been reflected in hearings, visits, and legislation. Congressional concerns about the ongoing NK conflict led in 1992 to Section 907 of the FREEDOM Support Act (P.L. 102-511) that prohibited most U.S. government-to-government assistance to Azerbaijan until the President determined that Azerbaijan had made “demonstrable steps to cease all blockades and other offensive uses of force against Armenia and Nagorno-Karabakh.” Congress eased many Section 907 restrictions on a year-by-year basis until the terrorist attacks on the United States in September 2001, after which it approved an annually-renewable presidential waiver (P.L.107-115). The conference managers stated that the waiver was conditional on Azerbaijan’s cooperation with the United States in combating international terrorism, and that they intended to “review and reserve the right to amend the waiver language.” Among other Congressional initiatives, beginning with FY1998 appropriations, Congress created a South Caucasus funding category to encourage conflict resolution in NK, provide for reconstruction assistance, and facilitate regional economic integration. Congress passed “The Silk Road Strategy Act” in FY2000 (as part of consolidated appropriations, P.L. 106-113) calling for enhanced policy and aid to support conflict amelioration, humanitarian needs, democracy, economic development, transport and communications, and border controls in the South Caucasus and Central Asia. In August 2003, Congress and the Milli Mejlis (legislature) signed an inter-parliamentary agreement envisaging discussions on security, energy, fiscal policy, and human rights.

#### Basic Facts

**Area and Population:** Land area is 33,774 sq. mi.; about the size of Maine. The population is 8.3 million (*Economist Intelligence Unit*; 2003 estimate), about 40% of whom live in the capital, Baku. Up to 2 million may live and work abroad. Administrative subdivisions include the Nakhichevan Autonomous Republic (NAR) and the Nagorno (“Mountainous”) Karabakh Autonomous Region (NK). NK’s autonomy was dissolved in 1991.

**Ethnicity:** 90% are Azerbaijani, 2.5% Russian, 2.0% Armenian, 3.5% Lezgins, Talysh, or Tats, and others (CIA, *World Factbook*, 1998 est.). About 13 million Azerbaijanis reside in Iran.

**Gross Domestic Product:** \$7.1 billion; per capita GDP is about \$860 (*EIU*; 2003 est., current prices).

**Leaders:** *President:* Ilkham Aliyev; *Chairman of the Milli Mejlis (legislature):* Murtuz Aleskerov; *Prime Minister:* Artur Rasizade; *Foreign Minister:* Elmar Mamedyarov; *Defense Minister:* Safar Abiyev.

**Biography:** Ilkham Aliyev, born in 1961, graduated with a kandidata (advanced) degree from the Moscow State Institute of International Relations in 1985 and then taught history. In 1991-1994, he was in business in Moscow and Baku, then became head of the State Oil Company (SOCAR). He was elected to the legislature in 1995 and 2000. In 1997, he became head of the National Olympic Committee. In 1999, he became deputy, then first deputy chairman, of the ruling New Azerbaijan Party. In August 2003, he was appointed prime minister, and was elected president on October 15, 2003.

## Contributions to the Campaign Against Terrorism

After the terrorist attacks on the United States on September 11, 2001, Azerbaijan quickly granted blanket overflight rights and intelligence support and offered the use of its bases. The State Department's *Patterns of Global Terrorism 2003* reported that Azerbaijan also stepped up its interdiction efforts against terrorists and equipment transiting its territory and moved against indigenous terrorists and terrorist financing. Azerbaijan was among the "coalition of the willing" countries that openly supported the U.S.-led Operation Iraqi Freedom (OIF). It offered the use of its airbases and assistance in re-building Iraq. In mid-August 2003, Azerbaijan contributed 150 troops to the coalition stabilization force for Iraq. NK Armenians and U.S. diplomats have censured some statements by Azerbaijani officials calling for international "counter-terrorism" actions against NK.

## Foreign Policy and Defense

President Ilkham Aliyev has emphasized good relations with the neighboring states of Georgia and Turkey, but relations with foreign states have often been guided by their stance regarding the NK conflict. Relations with neighboring Russia have been poor until recently (see below) and remain cool with Iran. In July 2001, Iranian fighter aircraft and a warship forced to shore an Azerbaijani oil research vessel in the Caspian Sea due to differences over sea boundaries. Azerbaijan views Turkey as a major ally against Russian and Iranian influence, and as a balance to Armenia's ties with Russia. Ethnic consciousness among some "Southern Azerbaijanis" in Iran has grown, which Iran has countered by limiting trans-Azerbaijani contacts. Azerbaijani elites fear Iranian-supported Islamic fundamentalism and question the degree of Iran's support for an independent Azerbaijan. Azerbaijan is a founding member of the GUUAM cooperation group (formed by the first initials of the members — Georgia, Ukraine, Uzbekistan, Azerbaijan, and Moldova). Most of the members have territorial disputes involving Russia. GUUAM has discussed energy and transport cooperation and pipeline security. Azerbaijan takes part in the European Union's Transport Corridor Europe-Caucasus-Asia (TRACECA) program, and is a member of the Black Sea Economic Cooperation group, the Council of Europe, the Economic Cooperation Organization, and the Organization of the Islamic Conference. Tensions with fellow member Iran have been displayed during meetings of the latter two organizations, and with Armenia during meetings of the former three.

Giving in to Russian pressure, Azerbaijan joined the Commonwealth of Independent States (CIS) in September 1993, but it never ratified the CIS Collective Security Treaty and in 1999 refused to re-sign it. Frictions in Azerbaijani-Russian relations include Azerbaijan's rejection of Russia's proposals for a predominantly Russian peacekeeping force in NK, its allegations of a Russian "tilt" toward Armenia in NK peace talks, and its refusal to permit Russian troops to patrol its borders. In 1997, Russia admitted that large amounts of Russian weaponry had been quietly transferred to Armenia, and in late 2000, Russia transferred heavy weaponry from Georgia to Armenia, fueling Azerbaijan's view that Russia supports Armenia in the NK conflict. Russia long raised objections to Azerbaijan's efforts to build oil export pipelines bypassing Russia. In late 1999, Russia accused Azerbaijan of failing to halt the transit of arms and mercenaries to Russia's breakaway Chechnya region. Azerbaijani-Russian relations appeared to improve in 2002 when the two states agreed on a Russian lease for the Soviet-era Gabala early warning

radar station in Azerbaijan and they reached accord on delineating Caspian Sea borders. Perhaps seeking Russian support for his rule, Ilkham Aliyev in March 2004 reaffirmed the 1997 Azerbaijani-Russian Friendship Treaty.

According to *The Military Balance 2003-2004*, Azerbaijani armed forces consist of 66,490 army, air force, and navy troops. There are about 5,000 border guards and more than 10,000 Interior (police) Ministry troops. To address chronic underfunding of the military and improve its offensive capabilities, defense spending has been increasing in recent years, to \$144.6 million in 2004, about 10.1% of the budget. Under a 10-year lease agreement, about 1,400 Russian troops maintain the Gabala radar station. Azerbaijan reportedly received foreign-made weapons of uncertain origin and armed volunteers from various Islamic nations to assist its early 1990s struggle to retain NK. Azerbaijan ratified the Conventional Armed Forces in Europe (CFE) Treaty, but is not in compliance. In 1994, Azerbaijan joined NATO's Partnership for Peace (PFP) to "bring Azerbaijan closer to the Western world," increase aid possibilities, and contribute to ending the NK conflict. Some Azerbaijani troops have participated in NATO peacekeeping in Kosovo since 1997, in coalition peacekeeping in Afghanistan beginning in late 2002, and rebuilding in Iraq since August 2003. Within PFP, there are tensions between Armenia and Azerbaijan.

**The NK Conflict.** In 1988, NK petitioned to become part of Armenia. This sparked ethnic conflict creating Armenian refugee problems and atrocities. In December 1991, an NK referendum (boycotted by local Azerbaijanis) approved NK's independence and a Supreme Soviet was elected, which in January 1992 declared NK's independence and futilely appealed for world recognition. The conflict over the status of NK resulted in about 15,000 casualties on both sides and over 840,000 Azerbaijani refugees and displaced persons (plus over 300,000 Armenians). NK Armenians control about 15% of Azerbaijan's territory (NK and adjacent areas) behind strong military fortifications. A formal ceasefire agreement was signed in July 1994 and the sides pledged to work toward a peace agreement. The 1994 cease-fire has been upheld while negotiations continue, including those held under the auspices of the Organization for Security and Cooperation's "Minsk Group" countries. In April 2001, Secretary of State Powell hosted the presidents of Armenia and Azerbaijan at Minsk Group talks in Key West, Florida, and the two later met with President Bush, indicating the new Administration's interest in a settlement. In May 2004, Ilkham Aliyev repeated the stance that "the occupied territories must be liberated, [and] the refugees must return to their native places, after which negotiations over the status of Nagorny Karabakh can be held." Azerbaijan also resurrected an earlier proposal that NK relinquish control over territories around NK in return for the reopening of railways transiting Azerbaijan to Armenia. NK "President" Arkadiy Gukasyan repeated the stance that the status of NK first needed to be settled.

## Political and Economic Developments

The Azerbaijani constitution, approved by a popular referendum in November 1995, strengthened presidential power and established an 125-member unicameral legislature (Milli Mejlis) with a five-year term for deputies. The president appoints and removes cabinet ministers (the Milli Mejlis consents to his choice of prime minister), submits budgetary and other legislation that cannot be amended but only approved or rejected within 56 days, and appoints local officials. It is extremely difficult for the Milli Mejlis to impeach the president. The U.S. State Department viewed an August 2002 constitutional referendum as flawed and as doing "very little to advance democratization."

Some opposition party leaders objected to one constitutional change designating the prime minister as the next in line in the case of presidential incapacity, death, or resignation, which they predicted would facilitate a succession from Heydar to his son, Ilkham.

In June 2000, the Parliamentary Assembly of the Council of Europe (COE) approved Azerbaijan's membership, conditioned on its compliance with commitments it made to the COE, including holding a free and fair November 2000 legislative election. Following U.S., COE, OSCE, and other criticism regarding the exclusion of some opposition parties, Azerbaijan's Central Electoral Commission allowed thirteen additional parties to take part in the party list voting. Final results of the vote on the party list ballot resulted in four parties surmounting a hurdle of 6% of the votes to receive seats: the NAP (16 seats); Popular Front (Reform) (4); Civic Solidarity (3); and the Communist Party (2). In single constituency races, NAP or independent candidates won most seats. Prominent opposition parties National Independence, Democratic, and Musavat (Equality) did not win seats in the party list vote (though some members were elected in single constituencies). All six opposition party members of the Central Electoral Commission denounced the election as fraudulent, and several protests were reported across the country. OSCE and COE observers judged the race "seriously flawed," though they said it showed some reform progress. Although international observers also judged January 2001 legislative run-off elections as seriously flawed, PACE admitted both Azerbaijan and Armenia as members later in the month.

Marking the closing of an era, Heydar Aliyev suffered serious cardiac problems in April 2003 and was mostly in hospital up through the expiration of his term in October. In what some critics termed a move to ensure a dynastic succession, Ilkham in July proffered his candidacy for the scheduled October 15, 2003 presidential election, but demurred that he was running only to buttress his father's candidacy. On August 4, the legislature hurriedly convened to confirm Ilkham as prime minister, a post permitting him to rule as interim head of state in case his father resigned or died. In early October, the ailing Heydar Aliyev withdrew from the race in favor of his son. Ilkham Aliyev handily won the election, beating seven other candidates with about 77% of the vote.

Protests alleging a rigged vote resulted in violence, and spurred reported government detentions of more than 700 alleged opposition party "instigators" of the violence. Trials reportedly have resulted in convictions for over 100 and prison sentences for about 40. On October 21, 2003, the State Department expressed "deep disappointment" with "serious deficiencies" in the election. It also expressed "extreme concern" about post-election violence by both police and civilians and about "politically-motivated arrests." Pointing to these problems, in December 2003 the NGO Freedom House downgraded Azerbaijan from "partly free" to "not free." In May 2004, trials reportedly will begin for prominent oppositionists arrested after the election, including People's Party leader Panah Huseynov, Hope Party Chairman Iqbal Agazada, Democratic Party secretary-general Sardar Calaloglu, Musavat Party deputy chairmen Arif Hacili and Ibrahim Ibrahimli, and Yeni Musavat newspaper editor Rauf Arifoglu. Defense Secretary Donald Rumsfeld's visit to Azerbaijan in December 2003 was widely viewed in Azerbaijan as signaling U.S. support for the newly elected Ilkham Aliyev.

According to the U.S. State Department's *Report on Human Rights Practices for 2003*, the Azerbaijan government's human rights record remained poor in 2003. The government restricted freedom of assembly and association. Numerous cases of arbitrary

arrest, beatings, unwarranted searches and seizures, and other human rights abuses were reported. The judiciary was corrupt and subject to government influence. The government harassed and jailed many political opponents. Freedom of speech and of the press were limited and media harassment increased. The conflict between NK Armenians and Azerbaijan has contributed to widespread human rights abuses by both sides. The State Department's *International Religious Freedom Report 2003* concluded that there was some slight improvement in religious freedom in recent months, with several churches that previous suffered from harassment able to successfully register, import religious literature, and meet. However, local authorities sometimes harassed nontraditional and non-favored religious groups and some groups continued to be denied registration.

The collapse of the Soviet Union and the NK conflict in the early 1990s contributed to the decline of Azerbaijan's GDP by over 60% by 1995. The economy began to turn around in 1996-1997, and the *Economist Intelligence Unit* estimated that GDP grew 11.2% and that consumer inflation was 2.1% during 2003. Continued GDP growth is dependent on further development of the oil sector and oil prices. A State Oil Fund provides some accountability for revenues. Most small and some medium-sized enterprises have been privatized, but most large-scale firms remain state-owned. Private sector agriculture and industry are the largest contributors to GDP, although much of the labor force is employed in the state sector. Foreign investment doubled 2002-2003 to over \$2 billion. To boost privatization and investment, an Entrepreneurs Council (including foreign investors) was created in 2002 that reports to the president. The *World Bank* and the non-governmental organization *Transparency International* have viewed Azerbaijan's government as among the most corrupt worldwide. The World Bank reports that poverty rates in Azerbaijan are among the highest in Europe and Eurasia. Azerbaijani officials in 2004 reported that over 40% of the population lives on less than \$1 per day.

**Energy.** The U.S. Energy Department in June 2003 reported estimates of 7-13 billion barrels of proven oil reserves and 30 trillion cubic feet of natural gas reserves in Azerbaijan. U.S. companies are shareholders in three international production-sharing consortiums that have been formed to exploit Azerbaijan's Caspian Sea oil and gas fields, including the Azerbaijan International Operating Company or AIOC, led by British Petroleum (developing the Azeri, Chirag, and Gunashli fields). In 1995, Azerbaijan and the AIOC announced a decision to transport "early oil" (the initial volume of oil from the AIOC fields, along with other Azerbaijani oil) through two Soviet-era pipelines in Georgia and Russia to Black Sea ports. The trans-Russia "early oil" pipeline began delivering oil to the port of Novorossiisk in late 1997. The trans-Georgian pipeline began delivering oil to Black Sea tankers in early 1999. The United States also has backed the construction of a large (one million barrels per day) oil pipeline from Azerbaijan through Georgia to Turkey's Ceyhan seaport on the Mediterranean (the Baku-Tbilisi-Ceyhan or BTC pipeline) as part of Azerbaijan's economic development, and because this route neither allows Russia to gain undue control over Azerbaijan's resources nor forces Azerbaijan to seek export routes through Iran. In August 2002, the BTC Company was formed to construct, own, and operate the oil pipeline. Construction began in 2003. Tankers may begin receiving the oil at Ceyhan in mid-2005. A gas pipeline from Azerbaijan's offshore Shah Deniz field to Turkey is also proposed.