

DEVELOPING REGIONAL COOPERATION AMONG TURKEY, GEORGIA AND AZERBAIJAN: IMPORTANCE OF REGIONAL PROJECTS

Mehmet DİKKAYA* - Deniz ÖZYAKIŞIR**

Abstract

Since the collapse of the former Soviet Union, the leaders of the Caucasian countries and the economists interested in the region have always spoken favorably about the prospects of a regional cooperation among the Caucasian countries. Their rhetoric and joint declarations call attention to their common historical background and the Soviet experience. However, the war in Nagorno-Karabakh between Armenia and Azerbaijan dramatically weakened the viability of such cooperation projects; Turkey's contribution accelerated regional integration among countries in the mid-1990s, except Armenia. This paper presents the major dynamics of this emerging regional economic cooperation among these three countries by focusing on infrastructural cooperation (such as transportation, telecommunication, and pipeline projects) and factor movements (such as trade in goods and services, labor and capital flows) among these countries.

Key Words

Regionalism, Caucasus, BTC Oil Pipeline, Kars-Tbilisi-Baku Railway Project, Nabucco, South Caucasus Pipeline, Turkey, Georgia, Azerbaijan

Regional Cooperation with Respect to the Theoretical and Historical Base

Regionalism is a process in which people and countries with different economic and political conditions form a common area. Regionalism can have many forms; however, the most common form is economic integration that is initiated by foreign trade and investment flows. As a result, a transnational economic entity without a formal regional organization is created. Sub-regionalism, on the other hand, refers to sub-regions in the same geography, such as CEFTA (Central European Free Trade Agreement), which was a part of the European integration after the Cold War; and in our case,

* Assoc. Prof., Kafkas University, Department of Economics / Turkey, e-mail: mdikkaya@yahoo.com

** Research Assistant, Kafkas University, Department of Economics / Turkey, e-mail: dozyakisir@gmail.com

cooperation between Turkey, Georgia, and Azerbaijan, members of Black Sea Economic Cooperation (BSEC) project. BSEC project was proposed by the Turkish political leader Turgut Ozal as a multilateral organization that is instrumental in encouraging trade and investment among regional countries. In the following years, on 25 June 1992, eleven countries including Albania, Armenia, Azerbaijan, Bulgaria, Georgia, Greece, Moldova, Romania, Russia, Turkey, and Ukraine signed the Summit Declaration and the Bosphorus Statement giving birth to the BSEC in Istanbul.

Since the failure of the former USSR, many attempts of regional cooperation have been realized in the new Eurasia. Although some of them concentrate on security issues, the rest are particularly interested in the economic development among the regional countries. Russia, Turkey, and Ukraine are the main powers in these organizations. The most important activities of these regional groups focus on economic cooperation, infrastructural development, environmental problems, natural and human resource management in tourism, culture, and management.¹

In the literature of economics, economic cooperation necessitates countries sharing common borders influence each others markets. Excessive red tape, weak telecommunication and transportation networks can decrease economic growth.² These factors affect the prospects of a regional cooperation in becoming a successful initiative.

Transportation costs may negatively affects the success of a regional cooperation and a close attention should be paid to communication networks especially for developing regions. According to Balassa,³ the US integration had prolonged almost a hundred years. The relations between trade and transportation network are not a simple connection in this case.

The regional cooperation among Turkey, Georgia, and Azerbaijan, which has its roots in the post Soviet period, have been very important aspects with respect to the infrastructure. However, yet trade flows among these three states have not been of satisfactory level, although recent developments have showed good prospects. Three countries have obtained unequal political advantages in both regional and global trade via common projects.

¹ Ian Bremmer & Alyson Bailes, "Sub-Regionalism in the Newly Independent States", *International Affairs* 74, I, 1998, pp. 131-32.

² F. Kahnert & P. Richards at all. *Economic Integration among Developing Countries*, Paris: Development Centre of the OECD, 1969, p. 35.

³ Bela Balassa, *Economic Development and Integration*, Mexico: Centro De Estudios Monetarios Latinoamericanos, 1965, pp. 31-32.

As suggested by Robson,⁴ investment strategies of multinational companies mainly depend on scale economies and transportation costs. Furthermore, there are direct connections between foreign direct investments and conditions for investment in any country. This region in our case has lucrative opportunities in transport and telecommunication for further cooperation. Azerbaijan, which has rich hydrocarbon reserves, and increasing oil revenues, does not have so much chance to bring its products to the Turkish market and to the world's oil consumers. On the other hand, Turkey has long coastlines connecting to the world markets. Georgia has not great resources in hydrocarbons compared to Azerbaijan, but it is strongly in need of hard currencies which will result from transportation lines. Moreover, Turkey and Georgia have developed a very close relationship after the Cold War because of the difficulties of the transitional period in Georgia, and the Russian threat on the unity of this newly independent country. Turkey has provided Georgia its free market experiences, offered consumer products, and balanced the Russian threat on the country to some extent.

In this paper, we first examine the emergent regional cooperation among Turkey, Georgia, and Azerbaijan by focusing on the economic and political importance of these countries. In the second part of the study, we will analyze the regional projects in relation to this sub-area. The last part of the study is going to express the future prospects and the crucial role of Turkey in such cooperation. Our main concern will especially be the economic and geo-strategic ties between the three countries; ignoring other prospects of partnerships in the trilateral connections.

Regional Countries and Their Economic Potentials

Azerbaijan, Georgia, and Turkey as sub-regional countries could be divided into two parts in terms of their economic backgrounds. First of all, Turkey has had experiences of the market economy for long years. On the other side, Georgia and Azerbaijan, which were parts of the former USSR, had long had centrally planned economies. After the collapse of the Soviet Union, these two states became independent, and since then their economies have been transforming to the market economies. The general economic situations and the recent economic developments of these countries will now be discussed.

⁴ Peter Robson, *The Economics of International Integration*, London&New York: George Allen&Unwin, 1998, p. 279.

Azerbaijan

After independence in 1991, Azerbaijan became a member of almost all international organizations and has showed considerable economic growth especially with the end of the war in Karabakh. As domestic demand and industrialization have increased, Azerbaijan has faced instability in prices, especially in non-oil industry stimulated inflation. As the energy sector grows very rapidly, partly causing the Dutch disease, Azerbaijan will probably face some controversies in its economy. Despite such controversies, two thirds of Azerbaijan has rich oil and natural gas reserves in addition to gold, silver, iron, copper, and titanium.

The State Oil Company of Azerbaijan (SOCAR) and 13 leading oil companies of the world signed a contract to exploit hydrocarbon reserves in 1994. After the production-sharing agreements were realized, Azerbaijan needed more transmission networks as oil production increased. The Baku-Tbilisi-Ceyhan crude oil pipeline (BTC), which is one of alternative routes for oil export, became active in May 2006 and stretches over 1,774 kilometers through the territory of Azerbaijan (440 km), Georgia (260 km) and Turkey (1114 km). This line is designed to transport up to 50 million tons annually and carries oil from the Caspian Sea oilfields to global markets. The South Caucasus Pipeline, also stretching through the territory of Azerbaijan, Georgia and Turkey, became operational at the end of 2006 and offers additional gas supply to the European market from the Shah Deniz of Azerbaijan. It is expected to produce natural gas up to 296 billion cubic meters annually. Azerbaijan also plays a major role in the EU-sponsored Silk Road Project.

As a result of heavy investments in oil and gas sectors, economic growth averaged 13.7% annually between 2001 and 2005. Steady inflows of FDIs (Foreign Direct Investment) attracted by the country's oil and gas sectors will be the basis for sustained healthy expansion during the five-year period, with real GDP growth nearing 30% in 2006, and averaging 17.8% annually through 2011. Export revenues more than doubled in 2005, largely reflecting the impact of high prices and increased production in oil revenues. Despite the continued strong demand for capital imports, the trade surplus widened to \$3.25 billion and the current account balance recorded a first-ever surplus. The current account surplus is expected to expand to \$2.4 billion in 2006, and the external surpluses will continue to widen to an average of \$4.1 billion per year over the five-year forecast period, as the completion of major oil and gas projects reduces demand for capital imports and project-related

services, while the volume of oil and gas exports continues to increase.⁵ Indeed, in 2007 the country's total exports to the world markets amounted to about 6 billion dollars and this trend reflected a trade surplus again.⁶

According to Table 1, the country demonstrated relatively high performance in economic growth, FDI movements (except year 2006), industrial value added as percentage of GDP, and GNI (Gross National Income) per capita figures in purchasing power parity between the years of 2001 and 2006. Azerbaijan seems to have obtained economic and political stability and is more eager to increase its export revenues by developing regional and global economic ties encouraging regional economic infrastructure.

Table 1. Azerbaijan: Main Macro Economic Trends (2001-2006)

	2001	2002	2003	2004	2005	2006
<i>FDI.net inflows (BoP, million US\$)</i>	226.5	1392.4	3285.0	3556.0	1680.0	-584.0
<i>GDP (current US\$)</i>	5707	6236	7276	8680	13245	19851
<i>GDP growth (annual %)</i>	10	11	11	10	26	35
<i>GNI per capita, PPP (current int, \$)</i>	2370	2630	2970	3270	4010	5430
<i>Agriculture, value added (% of GDP)</i>	16	15	13	12	10	7
<i>Industry, value added (% of GDP)</i>	47	50	53	55	64	70
<i>Services, etc., value added (% of GDP)</i>	37	35	34	33	27	22
<i>Inflation, GDP deflator (annual %)</i>	3	3	6	8	16	5
<i>Population, total</i>	8.1	8.2	8.2	8.3	8.4	8.5

Source: <http://www.worldbank.org> (30.07.2008).

Georgia

Georgian real GDP growth in 2003 of 11.1 percent is a figure that dipped to 8.4 percent in 2004 due to a poor agricultural harvest, but is expected to rebound to around 10 percent for both 2005 and 2006. In the following years, this country's growth rate was 9.4 percent for 2006, and 12.4 percent for 2007.⁷ Consumer price inflation (CPI) was 4.8 percent and 5.6 percent in 2003 and 2004, respectively. Estimates for the next two years were around 6.8 percent, but there are some indications that it might exceed

⁵ Azerbaijan Country Forecast, in Political Risk Yearbook of PRS Group Inc., 2007, p. 19.

⁶ UN Commodity Trade Statistics Database, <http://comtrade.un.org> (06.05.2008).

⁷ International Monetary Fund, *World Economic Outlook*, April 2008, p. 93.

that, which is a cause of growing concern. According to the data for 2006 and 2007, CPI increased to 9.2 percent in both years. The country's total exports have increased from \$831 million in 2003 to an estimated \$1.225 billion in 2006, and imports have increased from \$1.467 billion to an estimated \$2.6 billion. The deterioration in the trade balance is considered to be temporary and is mainly attributable to the construction of the BTC pipeline in an economy that was not sufficiently developed to supply the needs of such a major construction effort. Turning to the issues of economic policy, there has been strong growth in revenue collection since the Rose Revolution. In fact, initial targets for tax revenues had to be revised upward twice in 2004 because of the surge in tax collection. During that year, tax revenues doubled what they were in 2003.⁸

Despite rapid economic growth in recent years in Georgia, the GDP fell by 72 percent between 1989–94; in Azerbaijan, GDP in 1996 was 42 percent of the 1990 level; and the economy of Armenia was in serious condition up until 1994, with GDP in 1993 at one-third of the 1989 level. Starting in 1994–95, a trend toward stabilization and economic recovery has been seen in the states of the South Caucasus, thanks to an aggressive reform policy, but the consequences of the crisis were so profound that it may take years to overcome them. This cannot be done without pursuing radical and constructive domestic economic policies, along with an optimal combination of the interests of all states in the region and the active attraction of foreign investments.⁹

Table 2 shows general macro economic data on the Georgian economy which reflects a stable panorama. Unlike Azerbaijan's glorious macro data, Georgia's figures are relatively poor in relation to the GDP growth rate and net FDI inflows.

⁸ James V. Wertsch, "Georgia as a Laboratory for Democracy", *Demokratizatsiya*, vol. 13 no: 4, Fall 2005, p. 522.

⁹ Vladimer Papava, "Georgia's Economic Role in the South Caucasus", *Problems of Economic Transition*, vol. 48, no. 4, August 2005, p. 86.

Table 2. Georgia: Main Macro Economic Indicators (2001-2006)

	2001	2002	2003	2004	2005	2006
<i>FDI.net inflows (BoP, million US\$)</i>	109.8	160.2	334.6	492.3	452.7	1059.7
<i>GDP (current US\$)</i>	3219.5	3395.7	3991.4	5125.7	6412.2	7743.7
<i>GDP growth (annual %)</i>	5	6	11	6	10	9
<i>GNI per capita, PPP (current int, \$)</i>	2280	2480	2830	3120	3490	3880
<i>Agriculture, value added (% of GDP)</i>	22	21	21	18	17	13
<i>Industry, value added (% of GDP)</i>	22	24	26	26	27	25
<i>Services, etc., value added (% of GDP)</i>	56	55	54	56	56	62
<i>Inflation, GDP deflator (annual %)</i>	5	6	3	8	8	8
<i>Population, total</i>	4.6	4.6	4.6	4.5	4.5	4.4

Source: <http://www.worldbank.org> (30.07.2008).

In recent years, although steady economic growth has been observed in the country, the Georgian small-sized economy has affected regional and global fluctuations. Lack of hydrocarbons and political disturbances have negatively influenced country's economic performance. Especially separatist movements over South Ossetia and Abkhazia, which are autonomous regions in Georgia, as well as Russian support behind them, have directly and negatively affected the country's economic and political stability.

Turkey

The Turkish economy has faced a relatively higher inflationary period until 2002, although it never reached hyperinflationary levels. Instability in prices was the main problem of the Turkish economy in parallel with the fluctuations in national production.

The export-oriented growth strategy was quite successful in the early 1980s. The annual GDP growth rate was 5.8 percent between 1981 and 1988 and the economy did not experience any recession. The real increase in industrial production was above GDP growth during this period which averaged 8.1 percent. The economy of the 1980s transformed to "boom-bust" growth performance with lower average growth rate and a high macroeconomic volatility in the 1990s.¹⁰

¹⁰ Ahmet Ertugrul & Faruk Selçuk, "A Brief Account of the Turkish Economy, 1980–2000", *Russian and East European Finance and Trade*, vol. 37, no. 6, November–December 2001, pp. 6–30.

Political instabilities have accelerated fluctuations in the economy during 1990s. Some regional crises (such as the first Gulf War) and the world economy's negative growth also contributed to this instability. On the other hand, some regional opportunities (such as after the failure of the USSR, economic transition of the newly independent states to the free market economies) emerged at the same time.

From the extraordinary elections in 2002 to date, Turkey experienced relatively important economic benefits and showed substantial economic growth performance.¹¹ Furthermore, in the years of crises in which the economy fluctuated four times between 1994 and 2001, Turkey was not successful in becoming a regional power. Since the elections in November 2002, the country's economy has been stabilized, the inflation rate has steadily been decreasing, and the process of EU integration has been accelerated by the starting of accession negotiations on 3 October 2005.¹² With the help of economic recovery and regional projects (especially via energy routes), Turkey has emerged as an absolute regional power in Eurasia in five years.

Table 3. Turkey: Main Economic Indicators (2001-2006)

	2001	2002	2003	2004	2005	2006
<i>FDI.net inflows (BoP, million US\$)</i>	3352	1137	1752	2883	9801	20070
<i>GDP (current US\$)</i>	145594	184331	240955	302678	363369	402710
<i>GDP growth (annual %)</i>	-7	8	6	9	7	6
<i>GNI per capita, PPP (current int, \$)</i>	5510	5960	6350	7100	7770	8410
<i>Agriculture, value added (% of GDP)</i>	13	12	12	12	11	10
<i>Industry, value added (% of GDP)</i>	27	26	26	26	27	27
<i>Services, etc., value added (% of GDP)</i>	61	62	62	62	63	63
<i>Inflation, GDP deflator (annual %)</i>	55	44	23	10	5	11
<i>Population, total</i>	4.6	4.6	4.6	4.5	4.5	4.4

Source: <http://www.worldbank.org> (30.07.2008).

Macroeconomic data on Turkey's economic performance has demonstrated stable and hopeful results for the whole economy (excluding the year 2001 which was the biggest macroeconomic crises in Turkish economic

¹¹ Korkmaz Ilkorur, "AKP Ekonomide Başarılı Oldu mu?", *Radikal* (22.05.2007).

¹² Menderes Cinar, "Turkey's Transformation under the AKP Rule", *The Muslim World*, vol. 96, July 2006, p. 470.

history). Since the beginning of 2002, the economy has obtained positive growth rates, inflation has mostly been controlled, and GNI per capita has increased substantially (see table 3).

Regional Projects

Turkey's new position after the Cold War, and Georgian and Azerbaijani political attitudes against Russia, urged these three states to extend cooperation in the South Caucasus. As a result of their occupation in the Nagorno-Karabakh region of Azerbaijan¹³ and their claims over genocide thesis against Turkey, Armenia has been excluded in becoming part of regional projects. The contradictions between Turkey and Armenia, between Armenia and Azerbaijan, and between Georgia and Russia, fostered close relations among these three states. Finally, many common projects have been debated, and some of them have been implemented without Russia's contribution. This is also absolutely a fact for Armenia and its possible contribution on regional projects. According to Balat,¹⁴ among regional projects, "BTC is one of the very good demonstrations of how governments could come together for the same purpose and could promote the realization of the specific project". If we take other projects into consideration, regional self-reliance has substantially developed between three countries.

These plans can be divided into three parts; Baku-Tbilisi-Ceyhan Crude Oil Pipeline, Natural Gas Project from Shakh Deniz of Azerbaijan to the EU through Turkey's existing pipelines, and Proposed Kars-Tbilisi-Baku Railway Connection. In addition, some regional defense projects were realized among these states.

Baku-Tbilisi-Ceyhan (BTC) Crude Oil Pipeline

BTC is an oil pipeline to connect Baku in Azerbaijan, through Georgia and Turkey to Turkey's Mediterranean port of Ceyhan. Several agreements over the BTC oil pipeline were signed by the presidents of Azerbaijan, Georgia and Turkey at the Organization for Security and Cooperation in Europe summit in Istanbul in November 1999. These three countries, and Kazakhstan and Turkmenistan, signed additional agreements concerning the shipping of the latter two states' oil via the Baku-Ceyhan pipeline. The Azeri,

¹³ Armenian troops occupied not only Nagorno-Karabakh but also about 20 percent of Azerbaijani territory.

¹⁴ Mustafa Balat, "The Case of Baku-Tbilisi-Ceyhan Oil Pipeline System: A Review", *Energy Sources*, Part B, 2006, 1, p. 119.

Georgian, Turkmen, Turkish, and US presidents signed additional agreements on the Trans-Caspian Gas Pipeline. These pipeline routes were intended to provide a way for oil and gas to flow from the Caspian Sea to the Western countries, without having to go through either Russia or Iran.

In September 2002, the construction of a massive, multi-billion-dollar pipeline commenced. The pipeline would carry Caspian oil from Azerbaijan to Turkey via Georgia. In mid-2005, the long-awaited opening of the Baku-Tbilisi-Ceyhan pipeline resulted in political confrontations between protestors and the authorities.¹⁵

As an early result of this route, 275 millions of barrels of Azeri crude oil have reached the world oil markets via Turkey's Ceyhan port, as of January 2008. Additionally, Azeri officials said that their country plans to construct a crude oil refinery in Turkey at a cost of 10 billion dollars.¹⁶ Furthermore, the contribution of Kazakh oil would be advantageous for the BTC and would directly affect the commercial viability of the project. By establishing a connection between Aktau (a port city in Kazakhstan's Caspian coastline) and Baku, the BTC would be renamed the Aktau-Baku-Tbilisi-Ceyhan (ABTC) pipeline. The necessary measures will be taken to add Kazakhstan to BTC, and bring Turkmen and possibly Uzbek natural gas to the Baku-Tbilisi-Erzurum natural gas pipeline.

The BTC is the first direct pipeline link between the landlocked Caspian Sea and the Mediterranean, and this project will clearly bring economic advantages to the regional states (especially to Georgia and Turkey which are not so rich in hydrocarbons) and avoid increasing oil traffic through the vulnerable Turkish Straits. This pipeline developed by a group of eleven national and international oil companies and the BTC Pipeline Company was formed for this purpose in August 2002 as a separately incorporated company.

Regional projects will also give substantial economic benefits to transit countries. The construction of the BTC pipeline, along with plans for the South Caucasus Gas Pipeline Project (SCP), has provided an important engine of economic growth for Georgia. With the completion of both of these projects, however, the country will no longer be able to rely on major new

¹⁵ Azerbaijan Review, p.57; <http://www.countrywatch.com> (20.04.2008).

¹⁶ Osman Balcı & Ali Akçoban, "BTC ile Akdeniz'e inen petrolü Haydar Aliyev tankeri taşıyacak", *Zaman*, (10.01.2008).

infusions of construction funds to maintain its economic development. The BTC pipeline will be providing approximately \$50 million US per annum in transit fees, but it will become increasingly important to foster growth in SMEs (Small and Medium-Sized Enterprises), especially the agriculture and tourism sectors. Tourism especially had been an important sector of the Georgian economy during the Soviet years when several million tourists came to the republic each year, compared to a mere ten thousand in 2004. In this context, Georgia can easily develop this untapped potential.¹⁷

Proposed Kars-Tbilisi-Baku Railway Connection

Many academic studies demonstrate that the railroad connection should be developed for a possible intra-regional trade in post-Soviet geography.¹⁸ Because the regional infrastructural environment is relatively poor, trade relations among the countries have been underdeveloped. Although railroad connections are relatively developed in Turkey, they are not as sophisticated as those in Europe. Azerbaijani and Georgian railroad lines which are a heritage of the former USSR also necessitate financial help for modernization.

The Kars-Tbilisi-Baku (KTB) railway project bypassing Armenian borders will be a crucial step to foster regional cooperation. Armenian political leaders lessened their so-called genocide thesis against Turkey, because Armenia excluded from KTB (in addition to the BTC oil pipeline project). Furthermore, they strongly argued that the Kars-Gumru railway project will be realized again and emphasized that the KTB is currently a time-consuming effort. Armenia, which has preferred to be a closed economy, has begun to follow more rational regional policies, especially against Turkey.¹⁹

After long opposition to this project, Armenia has announced that it is ready to participate if Turkey opens its border with the Southern Caucasus state. The border was closed in 1993 following Armenia's support for the breakaway Azerbaijani region of Nagorno-Karabakh. Armenian Deputy-Minister for Foreign Affairs Gegam Garibjanian said on 18 January 2007 that his country could join the project by reopening a section of railway that runs from the Turkish town of Kars to Akhalkalaki in Georgia via Armenia "the day after the border between Armenia and Turkey is opened." Such a

¹⁷ Wertsch, *ibid.*, p. 522.

¹⁸ For example, see Richard Pomfret, *Central Asia Turns South? Trade Relations in Transition*, London: The Royal Institute of International Affairs, 1999, pp.12-14.

¹⁹ Mehmet Dikkaya, "Kafkasya'da Ulaşımında Bölgesel İşbirliği ve Kars-Tiflis-Bakü Demiryolu Projesi" [http://www.usakundem.com/uayazar.php?id=607\(10.09.2007\)](http://www.usakundem.com/uayazar.php?id=607(10.09.2007)).

section could significantly reduce transportation costs. But, Azerbaijan has its conditions too: Azerbaijani President I. Aliyev stated that Armenia's participation in the project "is not possible" until the country ends its support for the ethnic Armenian leadership of the self-declared Republic of Nagorno-Karabakh, a breakaway region of Azerbaijan. The US and the EU, the influential backers of such regional projects as the BTC crude oil pipeline and the South Caucasus gas pipeline, have declined to support the rail link since it excludes Armenia. Therefore, in many ways, the project can reflect a case study in regional self-reliance.²⁰

Data on the importance of the project show that five million tons of freight capacity in the first year, and 30 million tons of freight capacity after 20 years of the project's implementation, will be realized for the participant countries. These figures will be very high when compared data on all freight capacity of the year 2004 as shown the Table 4. In parallel with the construction of the KTB railroad, the historical Silk Road will be transformed to "Iron Silk Road."

Table 4. Transport Data for Azerbaijan, Georgia, and Turkey (2004)

Countries	Roads			Railways				Ports		Air	
	Ro1	Ro2	Ro3	Rw1	Rw2	Rw3	Rw4	Po	Ai1	Ai2	Ai3
Azerbaijan	27.016	47	9.862	53738	2.122	584	6.98	-	11	1.007	34
Georgia	20.247	39	4.987	22.5	1.565	401	5.065	-	4	203	3
Turkey	354.42	42	163.33	152.16	8.697	5.237	9.332	2.942	110	12.516	369
Total	401.68	128	178.18	228.4	12.38	990.24	21.38	2.942	125	216.52	406

Sources: World Development Indicators 2006; http://devdata.worldbank.org/wdi2006/contents/Table5_8.htm, 24.01.2007.

Explanations: Ro1: Total road network km (1999–2003); Ro2: Paved roads (%) (1999–2003); Ro3: Passengers carried million passengers (1999–2003). Rw1: Goods hauled million ton-km (1999–2003); Rw2: Rail lines total route-km 2000–2004); Rw3: Passengers carried million passenger- km (2000–2004); Rw4: Goods hauled million ton-km (2000–2004). Po: Port container traffic thousand. Ai1: Registered carrier departures worldwide thousands; Ai2: Passengers carried thousands; Ai3: Air freight million ton-km

²⁰ Rovshan Ismayilov, "Azerbaijan, Georgia and Turkey: Building a Transportation Triumvirate?" <http://www.eurasianet.org/departments/insight/articles/eav020707.shtml> (02.07.2007).

Construction of the Kars-Tbilisi-Baku railroad began with a ceremony in Tbilisi on 20 September 2007. Turkey, Georgia, and Azerbaijan have signed the necessary agreements for the project, which will connect Turkey to Azerbaijan and Central Asia. The railway, expected to cost US\$ 420 million, is seen as a major step in linking the ex-Soviet Caucasus region south of Russia to the West. Azerbaijan is providing a US\$ 220 million loan to Georgian railway builder Marabda-Kartsakhi Railways, of which the first installment of US\$ 40 million has already been transferred for the construction in Turkey. Railroad construction will be completed in late 2008. Azerbaijan expects the railways freight capacity to be 3 million tons per year in 2008, reaching 15 million tons by 2015.²¹

The proposed railway project would have an important spillover effect for Northeastern Anatolia. For instance, mayor of Kars, Naif Alibeyoglu, considers the new railway as a crucial lifeline for the city which is one of the poorest towns in Turkey. He also thinks that this line confirms Kars' position as a natural bridge between two geographical zones, Turkey and the Caucasus. Similar opinions could be considered for other cities located along the line.

Natural Gas Connections

Since the BTC main oil pipeline project has already progressed, reaching an agreement was not difficult. Azerbaijan, Georgia, and Turkey have agreed to build a second pipeline parallel to the BTC line (the route would be exactly the same up to the eastern Turkish city of Erzurum, where the gas pipeline would connect to the Turkish gas pipeline system), which would reduce costs.²²

Azerbaijan could also begin exports to the fast-growing Turkish natural gas market under a \$600–\$700 million proposal to extend existing pipelines to Georgia 174 miles to Erzurum, Turkey. A feasibility study on utilizing existing pipelines for exports is being developed under the EU's International Oil and Gas Transport to Europe (INOGATE) program. Turkey and the US have been pressing for a "Western route" pipeline that would carry oil from Azerbaijan's port of Baku through Azerbaijan and Georgia and then across Turkey to Ceyhan, at an estimated cost of \$1.8–\$4 billion. This

²¹ International Construction, "Iron silk road", September 2007, p. 10.

²² Tuncay Babalı, "Implications of the Baku-Tbilisi-Ceyhan Main Oil Pipeline Project", *Perceptions*, Winter 2005, p. 50.

would be a major part of the proposed “Eurasian Corridor” to bring Caspian oil and gas to international markets via Turkey, and to bypass Russia and Iran. Russia, on the other hand, was promoting a “Northern route” across the Caucasus to the Russian Black Sea port of Novorossiysk, but it has given up its insistence after having realized US pressure on BTC.

Azerbaijan Shah Deniz project aims at meeting some parts of gas demand of Turkey by Azeri gas. The negotiations, which started in October 2000, for the supply of natural gas from Shah Deniz of Azerbaijan were finalized in March 2001, and a gas sales and purchase contract was signed by BOTAS and SOCAR on 12 March 2001. According to the contract; natural gas delivery for 15 years is going to start in 2004 with 2 Bcma and reach 6.6 Bcma on the plateau period in 2007. The natural gas would be transported by pipelines to be constructed within the territories of Azerbaijan and Georgia. The Turkish section of the pipeline from Georgian border of Turkey to Erzurum/Pasinler is going to be approximately 250 km long, and it will be connected to the Eastern Anatolia Natural Gas Main Transmission Line at Erzurum/Pasinler.

Despite previous statements by the Turkish government stating that a gas pipeline from Turkmenistan was a top priority, this now seems highly unlikely as it would compete against the proposed Blue Stream project, as well as against possible gas supplies from Iran and especially Azerbaijan. Gas deliveries from Azerbaijan’s Shah Deniz field could begin in 2004, with Turkey and Azerbaijan having signed a 15 year deal to this effect in March 2001. Turkey claimed that its gas demand growth will be fast enough to support multiple pipelines, but many analysts believe Turkey’s forecasts are unrealistic, and that only one of the main options (i.e., Blue Stream, TCP, and Shah Deniz) can be supported for some time.

A meeting of the “Trilateral Working Group” of the EU, Turkey, and Greece was held in Brussels on 7 July 2000 under the EU Commission INOGATE Program. According to the “Concluding Statement” issued at the end of the meeting; a technical working group would be established to conduct studies on the bilateral pipeline between the two countries and the realization of the Southern Europe Gas Ring for the purpose of transportation of the NG produced in the Caspian Basin, Russia, Middle East, Southern Mediterranean countries and other sources via Turkey and Greece to European markets. On 18 January 2001, a Memorandum of Cooperation regarding the project was signed by BOTAS and The Public Gas Corporation of Greece (DEPA).

For the realization of the Southern Europe Gas Ring; the first step will be the connection of NG networks of Turkey and Greece by a pipeline to be constructed. The NG linkage Tsohatzopoulos is perhaps the most concrete example of that relationship. The first phase of the project, to be completed by 2004, will result in a NG pipeline from Ankara that can transport 1.5 Bcm of Iranian gas to Komotini, Greece. The proposed Greek-Turkish link, which would run from Ankara to Komotini, Greece, would diversify the European Union's gas imports and firm up its infrastructure links to Greece and Turkey. A Turkey-Greece-Italy connection would finally lash Greece, which is essentially an EU island at the far tip of the Balkan Peninsula, into the developing Southern European NG Ring, a key aspect of EU efforts to establish a common energy infrastructure. Both the Ankara-Komotini and Greece-Italy sections will likely receive substantial EU funding as a result. The project's beginnings are in an on-again, off-again deal that allows Turkey to import NG from Iran. Political complications, U.S. opposition and Turkey's economic problems have repeatedly delayed the project, but now the Tabriz-Ankara line is finally operational. Deliveries this year should total about 4 Bcm and eventually be ramped up to 13 Bcm. It is unclear whether Turkey, only now recovering from a deep recession, can consume all of that gas—raising the possibility of the country re-exporting at least some of it to Europe.²³

With this project, the main aim of the partners is to carry natural gas produced in Azerbaijan to Turkey. An agreement to last 15 years was signed between Turkey's BOTAS and Azerbaijan's SOCAR on 12 March 2001. Natural gas delivery started in July 2007 in connection to this Project. When the project is finalized, 750 million cubic meters natural gas would be delivered to Greek and Italy markets.²⁴

The 692km South Caucasus Pipeline (SCP) has been designed to transport natural gas from the Shah Deniz field in the Azerbaijan sector of the Caspian Sea, through Georgia and onto the Georgian-Turkish border. At full capacity, and after additional stages of development, it is envisaged that the pipeline will export up to 16 billion cubic meters a year. At the border, the pipeline links up the Turkish-built extension joining SCP to the domestic supply grid at Erzurum. The first deliveries of gas to Turkey are scheduled to commence on 30 September 2006. As of December 2005, over 95% of SCP

²³ Harun Kemal Ozturk & Hepbasli, Arif, "Natural Gas Implementation in Turkey. Part 2: Natural Gas Pipeline Projects", *Energy Sources*, vol. 26, no: 3, 2004, pp. 293-94.

²⁴ BOTAS (Petroleum Pipeline Corporation), <http://www.botas.gov.tr/projeler/projeler.asp#02> (18.01.2008).

had been constructed, with good progress being made in completing hydro testing of the line throughout the high mountainous sections of Georgia. This has been a critical item of work to finish prior to the onset of wintry conditions. Facilities for the off-take of gas were 98% complete in Turkey and 95% complete in Georgia. Georgia itself has rights to take 5% of the annual gas flow through the SCP in lieu of tariff and can purchase a further 0.5 billion cubic meters of gas a year at a discounted price. The SCP is being constructed in the same corridor as the BTC pipeline in order to minimize the environmental and social impact, using the same integrated project team. At a peak during the construction phase of the combined projects some 22,000 people were employed.²⁵

Georgian dependence on Russian gas supply has also faced this country important problems. In another words, together with the harmful effects of the security issues on country's future, by realization of such projects Georgia will be more independent from Russian policies.

On the other hand, under the Nabucco Gas Pipeline International Company, an almost 3300 kilometers gas pipeline project started. Participant countries (Turkey, Bulgaria, Romania, Hungary, and Austria) intend this Project to bring 25,5–31 billion cubic meters of Caspian and Iranian natural gas to their countries.²⁶ As seen in table 5, almost two-thirds of the project will be operational in Turkish borders under Nabucco. With the implementation of the project, Azerbaijan will enjoy export revenues from natural gas production and Georgia will gain additional transit fees. In addition to the difficulties of becoming a net energy importer²⁷ this project will bring additional benefits for Georgia. With this project, Turkey will also get an alternative gas supplier other than Russia and Iran.

²⁵ BP Caspian, <http://www.bp.com> (29.01.2008).

²⁶ BOTAS, *ibid.*

²⁷ There are seven countries in post Soviet geography, which are net energy importers, including Armenia, Belarus, Georgia, Kyrgyz Republic, Moldova, Tajikistan, and Ukraine.

Table 5. Turkey's Crucial Role in Nabucco Project

Main Route for Nabucco	Participant Countries	Line's length
	Turkey	1558 kilometers.
	Bulgaria	392 kilometers.
	Romania	457 kilometers.
	Hungary	388 kilometers.
	Austria	46 kilometers
Length of feedback lines in Turkey	Georgian border-Horasan	226 kilometers.
	Iranian border-Horasan	214 kilometers.
Total length of lines in the Turkish borders		1998 kilometers.

Source: Petroleum Pipeline Corporation (BOTAS), 18.01.2008

According to the energy experts, Nabucco would be a key factor in the upcoming energy strategies. Most recent plans say that tenders for the project's infrastructure developments should be put out no later than the end of this year. Recent estimates demonstrate that total investment needed for the project will exceed \$150bn. The financial requirements the project needs will partly come from the European Union itself via its European Investment Bank, but the involvement of other financial contribution will also be necessary. The US has said it will not apply any veto because of Iran's possible involvement in the project. According to the latest plans, a key contributor to the Nabucco pipeline would be Azerbaijan, with at least 1.2 trillion cubic meters of natural gas resources.²⁸

Developing Regional Cooperation and Turkey's Strategic Role

The failure of the USSR and the emergence of the new 15 independent states have brought Turkey both opportunities and risks to its northern and eastern borders. So far, Turkish influence in the post-Soviet Eurasia has provided substantial benefits to the Turkish economy and its geo-political importance has significantly increased.²⁹ Because of sharing common borders, common cultural ties (especially true for Azerbaijan), and their landlocked geographical position (especially important for Armenia and Azerbaijan),

²⁸ *The Budapest Sun*, September 20-26, 2007, p. 4.

²⁹ Laurent Ruseckas, "Turkey and Eurasia: Opportunities and Risks in the Caspian Pipeline Derby", *Journal of International Affairs*, vol. 54, no: 1, Fall 2000, pp. 217.

newly independent Caucasian states are relatively more important for Turkey. At the beginning of their independence, Georgia and Armenia had the same political importance for Turkey. After the Armenian claims in favor of so-called genocide in 1915 and Nagorno Karabakh's occupation by Armenian troops, Turkey closed its borders, declared them not to open until the Armenians withdraw from occupied land, and concentrated its regional effort towards Azerbaijan and Georgia.

After Armenian policies negatively affected the region's common initiatives, as strongly expressed by Balat,³⁰ the BTC oil pipeline project became one of the very good examples of how governments could come together for the same purpose and could promote the realization of a specific project. The BTC project, being the first leg of the East-West Energy Corridor and once treated as a "dream" by some experts, has turned into a physical entity. Many academics emphasized Turkey's unique geographical position regarding such projects.³¹ For instance, Turkey first proposed the KTB railway project in 1993 as it looked for ways to increase its influence in the South Caucasus. However, a protocol on the project was only signed between Turkey, Georgia, and Azerbaijan in 2004. Feasibility studies began that same year. In May 2005, the presidents of the three countries reaffirmed their support for the railway with a formal declaration in Baku.³² From this starting point, this project will nearly be realized in late 2009.

Regional cooperation attempts in Caucasus show that a country can assume the initiator role. Turkey may become such a country. As a result of its activities, Turkey is largely influential in Azerbaijan and Georgia.³³ According to Aydin, Turkey has also been more than willing to extend its friendship, economic, political, and military support to the region.³⁴ In this context, Turkey's interests towards Azerbaijan and Georgia could be easily understood by three types of factor movements which are: direct trade flows, capital movements to the region, and training human capital. One can easily argue that such kinds of cooperation among the states encouraged the regional integration process.

³⁰ Balat, *ibid.*, p. 117.

³¹ Gareth M. Winrow, "Turkey and the East-West Gas Transportation Corridor", *Turkish Studies*, vol. 5, no. 2, Summer 2004, pp. 25-27.

³² Ismayilov, *ibid.*

³³ Shireen Hunter, "Turkey, Central Asia, and the Caucasus: Ten Years after Independence", *Southeast European and Black Sea Studies*, vol. 1, no: 2, May 2001, p. 14.

³⁴ Mustafa Aydin, "Foucault's Pendulum: Turkey in Central Asia and the Caucasus", *Turkish Studies*, vol. 5, no: 2, Summer 2004, p. 12.

Trade Flows between Turkey, Georgia, and Azerbaijan

The Southern Caucasus Republics, once a part of the former USSR and independent since 1991, have started to seek new trading partners and new markets. However, the first years of their independence have been very hard mainly due to the economic problems they have had. There have been infrastructure problems and not enough investment capital or experienced entrepreneurs, which means that these countries are less able to be competitive in international markets.

The infrastructure in the Caucasus is so important in shaping the trade and development in the region. As Pomfret points out,³⁵ the infrastructure of transportation and telecommunication between the former USSR republics and their southern neighbors is generally poor. From this point of view, Caucasian states also have weak transport network limiting regional trade relations.

On the other hand, Turkish economic policies inhibit developing economic ties towards the region. Some policies make it harder for large companies operating in Turkey to become involved in the Caucasus. According to Aras who is an expert on Eurasian affairs, Turkish policy should be enlarged to fully utilizing the BSEC project as an international forum to address regional problems from a broader geopolitical perspective. The BSEC region is in the process of becoming a sub-region.³⁶

Turkish trade relations have substantially increased, especially after the regional projects have been implemented. Between 2000 and 2006, trade data show that Turkish exports to Azerbaijan and Georgian markets increased three times. On the other hand, Turkish imports from these countries ascended steadily (See Table 6). Although trade figures do not reflect a large share in view of total Turkish foreign trade, Turkey seems to have become the largest trading partners for Azerbaijan and Georgia.

³⁵ Pomfret, *ibid.*

³⁶ Bulent Aras, "Turkey's Policy in the Former Soviet South: Assets and Options" *Turkish Studies*, vol. 1, no. 1, Spring 2000, pp. 52-54.

Table 6. Turkish Trade Flows towards Azerbaijan and Georgia, 2000-2006, in million dollars

Years		AZ	(1)	GEO	(2)	(3)
2000	Ex	230	19.6	131	18.5	1.3
	Im	96	5.5	155	48.0	0.5
2001	Ex	225	15.7	144	19.1	1.2
	Im	78	3.4	127	39.9	0.5
2002	Ex	227	13.6	103	12.9	0.9
	Im	63	2.9	138	39.9	0.4
2003	Ex	316	12.0	155	13.6	1.0
	Im	123	4.7	274	59.4	0.6
2004	Ex	404	11.5	200	10.8	1.0
	Im	136	3.8	307	47.4	0.5
2005	Ex	528	10.0	272	10.9	1.1
	Im	272	6.3	303	35.0	0.5
2006	Ex	695	13.2	408	11.1	1.3
	Im	333	5.2	342	34.4	0.5

Source: <http://stat.wto.org>, 24.01.2008; <http://comtrade.un.org> 28.01.2008

Explanations: AZ: Azerbaijan, GEO: Georgia, Ex: Exports, Im: Imports;

(1): Share in total Azerbaijani exports or imports as percentage (2) Share in total Georgian exports or imports as percentage (3) Share in total Turkish exports or imports as percentage, including both countries

Turkish Capital Movements towards the other Countries

After the collapse of the USSR, Turkish manufacturers started to seek new markets and new trade partners in the Caucasus and Azerbaijan; Georgia and Armenia became early trading partners for Turkey.

Turkish companies became important investors in Azerbaijan, together with American and British firms. By 2000, there were 1300 Turkish firms in Azerbaijan operating in many sectors and in non-oil sectors; Turkish investments have the largest share in total foreign direct investments in Azerbaijan.³⁷ In Georgia, as of 2000, Turkish investments have the second

³⁷ TİKA (The Turkish International Cooperation and Development Agency) Azerbaijan Cumhuriyeti, p. 25, <http://www.tika.gov.tr> (29.01.2008).

largest share after American firms. In addition, Turkish Eximbank credits were almost 40 million dollars in the same year.³⁸ TPOA (The Turkish Petroleum Company), which is the state oil company of Turkey, has also invested in Azerbaijan and Kazakhstan. As of December 2006, total oil production by TPAO reached 43.5 millions of barrels in Azerbaijan.³⁹

Another business area in which Turkish investments were concentrated in the region since the early 1990s was the construction sector. Turkish contracting companies have undertaken important projects in the South Caucasus together with Russia, Ukraine, and Central Asia. According to the Turkish Contractors Association (TCA), the total volume of investments undertaken by Turkish contractors has reached 621 million dollars in Azerbaijan.⁴⁰ After 2000, total contracts undertaken by Turkish construction companies increased 2.96% in Azerbaijan.⁴¹

In addition, the bilateral visa facilitation policy enabled both Georgian and Turkish people to increase their international visits. This policy indicated that common political efforts can easily accelerate regional collaboration. Another important point in favor of developing regional cooperation suggests that the Eurasian railway corridor project will force further railway modernization projects in the region. It is expected that Turkish construction companies will have additional contracts in Georgia and Azerbaijan through this project.

Actually, Turkish entrepreneurs have been active in both in Azerbaijan and Georgia since 1990s. In addition to investments of Turkcell, one of the biggest Turkish telecommunication companies, Turkish investors have large shares in foreign investment both in Azerbaijan and Georgia. Turkish companies are the second largest FDI group in Georgia. Now, we emphasize the main characteristics of Turkish influence towards the region.

³⁸ TİKA (The Turkish International Cooperation and Development Agency) Gürcistan Ülke Profili., pp. 26-27, <http://www.tika.gov.tr> (29.01.2008).

³⁹ TPOA (The Turkish Petroleum Company), http://www.tpao.gov.tr/v1.4/index.php?option=com_section&task=view&id=3&itemid=15 (06.02.2008).

⁴⁰ Nurel Kılıç "Yurtdışı Müteahhitlik Hizmetlerinin Sorunları ve Çözüm Önerileri", Araştırma ve Meslekleri Geliştirme Müdürlüğü, Haziran 2004, p. 18, <http://www.izto.org.tr> (29.01.2008).

⁴¹ TCA (Turkish Contractors Association), <http://www.tmb.org.tr/genel.php?ID=10> (29.01.2008).

Regional Cooperation in Human Capital Development

Turkey's successful experiences for developing human capital in the region have been very important since the independence of Azerbaijan and Georgia. The activities of Turkish entrepreneurs and educators have been important parameters for bilateral economic relations in the region. These educational institutions have supported human capital in order to compete with the globalizing world. If all of the educational institutions are taken into account, we can say that Turkish influence in the region will be higher than expected in the future. Turkish firms operating in Azerbaijan and Georgia also employ many native citizens who have been educated in Turkish-led institutions and contribute substantially to decreasing unemployment in the region.

Turkish influence towards the Turkic states of the former USSR includes Azerbaijan and covered nearly 1800 Azerbaijani students by 1997. In addition, eleven high schools and two universities were opened in Azerbaijan by Turkish entrepreneurs.⁴² In Georgia, a few high schools and one private university supported by Turkish businessmen are also active. Furthermore, these educational institutions have been supported by native administrative elites and they are considered by political leaders as opening the windows of their countries to the contemporary world.

Conclusion

Transportation of goods and services is a crucial and contentious issue in the post-Soviet regions. The landlocked nature of some oil-rich countries with negative economic growth has urged them to seek alternative transport means. This is especially valid for Azerbaijan which is rich in oil and natural gas reserves and for Georgia having a small-sized economy.

Armenian policies against Azerbaijan and Turkey have made Georgia an important transit country. In fact, Turkey has kept its border with Armenia closed since 1993. This closure was associated with Turkey's embargo designed to stimulate Armenia's withdrawal from Azerbaijani territory occupied during the conflict in Nagorno-Karabakh in the early 1990s. Apart from relations with Armenia, the other three states have not got any disputes on their borders and their policy implementations. This favorable political

⁴² Aras, *ibid.* p. 45.

environment has accelerated regional cooperation among them. Trade and capital flows have dramatically increased in the region thanks to the oil and natural gas pipelines and a proposed railway connection.

Turkey's geo-political importance is continuing with its geo-economic importance in the new millennium. Turkey's growth and industry-oriented policies have shifted from the realm of public policy to a market-driven domain since 1980s. With the end of the Cold War, the "Iron Curtain" around Turkey has been removed. These two developments provided Turkey with a great chance with her historical, cultural and economic ties to form a geo-economic space and to become an engine for regional development.

Moreover, Turkey's policy on developing regional cooperation in the Southern Caucasus has been the leading stimulant for regional economic developments. Regional cooperation has long been considered as Turkey has experienced economic and political stability since 2002, Georgia constructed close relations (especially after the Rose Revolution of this country) with Turkey and Azerbaijan, and there are improvements in domestic political institutions in Azerbaijan.

Regional plans, which have been both implemented and proposed, are fostering further regional integration. When we take historical experiences into account, infrastructural cooperation in a close region has accelerated economic growth. Increasing trade relations, growing capital flows, and further cooperation in human capital shows how common initiatives could be important in the same region. In this context, when all regional projects are completed, a new sub-region covering Turkey, Georgia, and Azerbaijan will come to exist. In other words, as indicated by Aydin,⁴³ when regional projects are completed, the Caucasian states will be less dependent on Russia. Because of the Soviet heritage and its remaining roots, the region has suffered, as seen in many examples. Trilateral cooperation among the mentioned countries can develop relations at least on an equivalent level at the beginning of the millennium.

⁴³ Aydin, *ibid.* p. 16.

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