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Global Think-Tank

Baku-Tbilisi-Kars: Regional Implications and Perspectives

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CESD Press

Baku, October 2018

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Abbreviations

<i>AGT</i>	<i>Azerbaijan, Georgia, and Turkey</i>
<i>BTC</i>	<i>Baku-Tbilisi-Ceyhan</i>
<i>BTE</i>	<i>Baku-Tbilisi-Erzurum</i>
<i>BTK</i>	<i>Baku-Tbilisi-Kars</i>
<i>CJSC</i>	<i>Close Joint Stock Company</i>
<i>CTC</i>	<i>Caucasus Transit Corridor</i>
<i>EaP</i>	<i>Eastern European Partnership</i>
<i>ENP</i>	<i>European Neighborhood Policy</i>
<i>EU</i>	<i>European Union</i>
<i>GUAM</i>	<i>Georgia, Ukraine, Azerbaijan, Moldova</i>
<i>JSC</i>	<i>Joint Stock Company</i>
<i>OBOR</i>	<i>One Belt, One Road</i>
<i>OSJD</i>	<i>The Organization for Cooperation of Railways</i>
<i>OTIF</i>	<i>Organization for International Carriage by Rail</i>
<i>NK</i>	<i>Nagorno-Karabakh</i>
<i>SMGS</i>	<i>Agreement on International Goods Transport by Rail</i>
<i>SOFAZ</i>	<i>State Oil Fund of the Republic of Azerbaijan</i>
<i>TRACECA</i>	<i>Europe-Caucasus Asia Transport Corridor</i>

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Introduction

The establishment of the Eastern Partnership (EaP) policy as a part of the European Neighborhood Policy (ENP) sets new objectives for the deepening of cooperation between the EU and EaP countries, and the greater integration of the EaP based on shared norms, values and standards. Forming the eastern divide of the ENP, Armenia, Azerbaijan, Belarus, Ukraine, Moldova, and Georgia are considered official neighbors of the EU, although half of these countries (Armenia, Azerbaijan and Georgia) do not lie on the immediate borders of the EU. However, these South Caucasian countries play an important transit role by connecting the EU with Central Asia and China. Hence, the Baku-Tbilisi-Kars (BTK) railroad, crossing Azerbaijan, Georgia, and Turkey, establishes a significant link in the further development and integration of regional and global transit corridors stretching from China to Europe through Central Asia and the South Caucasus.

Crossing the AGT countries (Azerbaijan, Georgia, and Turkey), the BTK railway has been perceived as a bridge between Asia and Europe. This new stage in transportation cooperation between Europe and Asia has also been identified as a revival of the ancient Silk Road. According to Samuel Lussac, a Caucasus specialist, the previous oil and gas pipeline projects – the Baku-Tbilisi-Ceyhan (BTC) and the Baku-Tbilisi-Erzurum (BTE) – have been presented as the “New Silk Road” and, therefore, the construction of the BTK could now better be described as the “Iron Silk Road”.¹

There has been strong consensus that the development of a transport system involving EaP and EU countries may enable beneficial economic and political cooperation. Considering the importance and relevance of the topic for current academic literature and policy agendas, this paper contains analyses of different countries’ perspectives in the context of economic as well as political outcomes. The first section, the Literature Review, has been dedicated to an exploration of railway transportation in general and a discussion of different perspectives on the BTK project in particular. The second section presents a fiscal analysis of participating countries, to calculate the varying expenditures for the project, whilst the third section discusses the economic benefits of the project in a comparative way. Finally, the last part of the paper is dedicated to examining the political implications of the corridor not only for the

¹ Lussac, Samuel. 2008. "The Baku-Tbilisi-Kars Railroad and its Geopolitical Implications for the South Caucasus." *Caucasus Review of International Affairs* pp, 12.

participating members of the BTK project, but also for countries that may have interests in joining the project or have an indirect political stake, given the largescale impact of the project.

Literature Review

In this part of the study, existing literature and recommendations regarding railway transport in general and the BTK project specifically are presented. The literature contains information about the level of existing cooperation between the EU and Caucasus region, as well as the degree of cooperation of the AGT countries. Among many different assumptions about the outcome of the project, there is a debate in the literature whether the BTK project is more of an economic or political nature. In this section, therefore, different findings have been presented to show both sides' viewpoints.

There is no doubt that the initial aim of the BTK project was to create better trade cooperation between Europe and China via the AGT countries and to provide an efficient transit route. Having such a global and strategic importance, the heads of the member countries have regarded the BTK as an integral part of China's modern Silk Road Economic Belt initiative. China's ambitious economic initiative for building the 21st century's modern Silk Road has come to be known as "One Belt, One Road" (OBOR). On one hand, the Silk Road Economic Belt aims to connect Europe to China's underdeveloped hinterland through Central Asia, and on the other hand, the Maritime Silk Road connects Southeast Europe to China through ports and railways.²

Although the BTK project comprises a small portion of OBOR, yet plays a crucial role in carrying goods of China to Europe, understanding the purpose of the OBOR project will enable readers to understand the BTK project as well. There have been heated debates among Chinese scholars and experts over the geo-strategic or geo-economic nature of OBOR since the initiation of the project. According to the research of Peter Cai of the Lowy Institute for International Policy, the geo-economic dimension of the project has been incomplete while geostrategic interpretations have been overstated.³ He asserts that these goals, indeed, are not

² The President of the Republic of Azerbaijan. 2012. *Azerbaijan 2020: Look into the Future* . Baku.

³ Cai, Peter. 2017. "Understanding China's Belt and Road Initiative." *Lowy Institute for International Policy* 3-5.

contradictory and China uses OBOR as a tool for its regional leadership through economic integration.

As the BTK project is the heart of transport cooperation between the East and West, it is important to explore existing literature on the rail transport connection between the EU and EaP countries specifically. Among many analysts in this regard, Michal Beim, a transport policy expert, identifies ways of developing transportation links between countries of the EU and the EaP, as well as EaP countries themselves. According to Beim, in order to stimulate economic development, both liberalization of transport markets and the harmonization of technical regulations between different countries' transport systems should be the main starting points.⁴ Additionally, Turgut Ozkan et al. who analyzed 30 countries (mainly European and Eastern European) concluded that, apart from boosting competition, rail transportation liberalization may also attract private companies to enter the market, leading to better efficiency.⁵

According to Ozkan et al. the vertical separation between infrastructure services of railway transportation and train operations is a primary element of railway liberalization. Historically the national railways in the European railway market used to be run by the vertically-integrated model, which could not keep up with changes in the market and other developments, especially after World War Two. Therefore, market opening and privatization were prime strategies to limit the waste of public subsidies and develop the existing low-quality train services. For these reasons, several railway packages, legislation, initiatives and reforms have been adopted to create a more competitive and highly effective single European railway market. Until today, four railway packages have been adopted by the European Parliament and the Council – in 2001, 2004, 2007 and 2016.⁶ The status of the Directives' implementation across European countries can be seen in Table 1 below.⁷

In this respect, the Directorate General for International Policies of the European Parliament has provided a note, which reviewed the experiences of vertical separation (unbundling) across EU Member States. Analyzing the advantages and disadvantages for the separation of railway operations from railway infrastructure management in France, Italy, the Netherlands, Sweden and the United Kingdom, the report highlighted several findings. Great

⁴ Beim, Michal. 2017. *So Near and Yet so Far: The Challenges of Transport Cooperation between the European Union and Eastern Partnership Countries*. The Ministry of Foreign Affairs of the Republic of Poland.

⁵ Ozkan, Turgut, Gozde Yanginlar, and Salih Kalayci. 2016. "Railway Transport Liberalization: A Case Study of Various Countries in the World." *Journal of Management and Sustainability* 140-148.

⁶ https://ec.europa.eu/transport/modes/rail/packages_en

⁷ Wheat, Philip, and Chris Nash. 2006. "EU Policy and its Impact on the Rail System." *Policy Effectiveness of Rail* (European Commission and Directorate General for Energy and Transport)

benefits have been accrued due to the separation of freight operations rather than passenger operations, as the latter one is highly dependent on public funding, which is rather limited. In Sweden, with its long history of vertical separation, and the Netherlands, the introduction of a separation policy has allowed improvement in performance, elimination of delay, as well as improvements in safety, punctuality and capacity. On the other side of the spectrum, given the partial nature of separation in France, no major changes in competition, transparency or the overall increase of efficiency have been observed. Finally, the report concluded that in the UK, with the introduction of “competitive franchise bidding”, market growth has been stimulated and service innovation has been encouraged, while costs have increased at the same time.⁸

Table 1. Models of railway liberalization across Europe

Degree of separation	Degree of competition		
	Little or None	Open Access freight competition	Plus at least some competitive tendering for passenger services
<i>Vertically integrated (with separate accounting)</i>	Greece Ireland	Belgium	Austria Germany Italy
<i>Separate public sector infrastructure manager</i>	Finland France Spain		Denmark Netherlands Portugal Sweden
<i>Separate private sector infrastructure manager</i>			Great Britain

Source: Data exported from the Transport-Research.info (2006)

We have already reviewed relevant European legislation and trends in the railway sector to analyze the degree of market liberalization and financial transparency, as well as initiatives for the creation of a single European Rail area. In the following paragraphs, the study will present the elements of harmonization of European laws in the Caucasus, specifically among AGT countries. Additionally, it will review the overall degree of cooperation in the region.

⁸ Directorate General for International Policies. 2011. The Impact of Separation between Infrastructure Management and Transport Operations on the EU Railway Sector. Note, European Parliament

Regarding the facilitation of trade and transit measures in the Caucasus Transit Corridor (CTC), the Batumi Declaration plays an important role. The Summit which brought this declaration forth took place in Georgia in 2013.⁹ As a result of the Summit, participants agreed to implement measures in areas such as the simplification of customs procedures at joint border crossings, harmonization of European law, and the development of international transport law under the aegis of the Intergovernmental Organization for International Carriage by Rail (OTIF) and the Agreement on International Goods Transport by Rail (SMGS) in the framework of the Organization for Cooperation of Railways (OSJD).¹⁰ Additionally, participants agreed to promote the development of corridors among Georgia, Ukraine, Azerbaijan, Moldova (GUAM) countries, the Europe-Caucasus Asia Transport Corridor (TRACECA), the BTK and Silk Wind projects through multilateral or bilateral customs data exchange. Finally, to facilitate trade along the corridors, it has been suggested to use a single documentation system to exchange data between maritime and railway transport systems.¹¹

However, it is also important to analyze the effectiveness of the current regional integration of the AGT countries to understand the role of the BTK project and possibility for further cooperation. Among various observations on this matter, Carlo Frappi and Marco Valigi suggest a general review on the Caucasus-Caspian region and assess the effectiveness of the AGT alliance.¹² To analyze states' behavior and cooperation systems, the authors apply Theodore Caplow's "theory of coalitions in triads" to the state relations of Azerbaijan, Georgia, and Turkey. As the authors explain, the theory suggests that the cooperation of three states are built upon their mutual dependence. Hence, the application of the theory suggests that power distribution among this triad allows forecasting that any attempt of the median member to dominate the weakest one would undermine the stability of the relations and the region as a whole due to the "asymmetry of power relations" and a "clash of interests".

The reason for the relevance of the triad relationship system in the context of AGT countries can be seen upon an exploration of each country's needs. For instance, Azerbaijan is interested in mutual support to secure its external protection and political cooperation to gain influence over Armenia, as a bargaining power vis-a-vis the Nagorno-Karabakh area, as well as to protect external energy markets. Turkey, on the other hand, seeks for energy supplies and

⁹ International Rail Transport Committee. 2013. *Batumi Declaration: Conclusions of the Third Regional Conference on Trade Facilitation and Caucasus Transit Corridor Promotion*. Batumi: United Nations Economic Commission for Europe

¹⁰ International Rail Transport Committee. 2013, pp. 2

¹¹ International Rail Transport Committee. 2013, pp. 2

¹² T. Caplow, "Theory of Coalitions in the Triad", *American Sociological Review*, Vol. 21, No. 4 (1956), pp. 489-93.

aims at increased regional influence. Lastly, economic and political cooperation with Turkey and Azerbaijan in the region implies the downgrading Russian, which is of paramount interest to Georgia.¹³

On the other hand, some analysts suggest that the economic cooperation of these three regional countries may trigger further political regionalization of the countries in a form of several conflicting alliances. In this regard, Samuel Lussac argues that construction of the BTK railroad has laid down not only an economic, but also a political foundation for cooperation among Azerbaijan, Georgia, and Turkey that might result in the formation of “a geopolitical axis in the region, encompassing Russia, Iran, and Armenia against the AGT countries”.¹⁴ Hence, according to the scholar, although the countries have not set up any “formal regional organization”, the implementation of transportation infrastructure is perceived as a means for greater regional integration in the South Caucasus.

Additionally, it should also be noted that, for Azerbaijan, the development of the transportation sector was set as one of the main priorities of the development strategy on “Azerbaijan 2020: Look into the Future”, aiming to turn Azerbaijan into a regional trade hub.¹⁵ To make an effective use of the country’s strategic geographical position, the government put special emphasis on adopting a strategic approach to railway, water, air, underground and automobile transport systems. Hence, though Azerbaijan’s location next to major powers (Russia, Turkey, and Iran) and a conflicting neighbor (Armenia) creates challenging security environment, Brenda Shaffer, who has served as the Research Director of Caspian Studies at Harvard University, argues that the successful implementation of the BTK project may have positive impacts on the country’s economy and on strengthening its geopolitical position in the region.¹⁶

According to Rovshan Ibrahimov, the creation of transport corridors is important for the development of the non-oil sector in Azerbaijan.¹⁷ Given the strategic location of Azerbaijan, the existing network of transportation allows Azerbaijan to transfer both its own energy resources and oil from Central Asia to European markets. However, to achieve the further sustainable development of the economy, there is a need for the diversification of the

¹³ Frappi, Carlo , and Marco Valigi. 2015. "Patterns for Cooperation in the Southern Caucasus." *ISPI* 5

¹⁴ Lussac, Samuel. 2008. "The Baku-Tbilisi-Kars Railroad and its Geopolitical Implications for the South Caucasus." *Caucasus Review of International Affairs* 36.

¹⁵ The President of the Republic of Azerbaijan. 2012. *Azerbaijan 2020: Look into the Future* . Baku.

¹⁶ Shaffer, Brenda. 2012. "Azerbaijan's Foreign Policy." *Caucasus International* 2 (1).

¹⁷ Ibrahimov, Rovshan. 2016. "The Development of the Transport Sector in Azerbaijan: The Implementation and Challenges." *Caucasus International* 6 (1).

economy away from this single sector. Rovshan Ibrahimov argues that alternative corridors provide leverage for transit countries in the event of political and economic risks. Considering the estimated revenue from transportation of goods and passengers as an alternative to the oil sector, the author regards the West-East transport corridor would provide important contributions to the state budget of Azerbaijan outside of the oil sector. Additionally, transport routes can also trigger development of the country's regions which are able to provide logistical support and, hence, create additional revenue for the government and private entrepreneurs.

Overall, the exploration of existing literature concludes that the political aspects of the BTK project have been overstated, while a fiscal analysis has been neglected, especially in a comparative manner, for AGT countries. However, this study aims to fill this gap and presents a cost and benefit analysis for participating countries, both economic and political.

Fiscal Analysis

Starting from Baku, the capital of Azerbaijan, passing through the Georgian capital city of Tbilisi as well as the town of Akhalkalaki in Georgia, where trains move through gauge-changing facilities, the BTK railroad ends in Turkey's Kars. In total, it comprises 826 km (500 mile) of rail link. Even though, historically, these countries are linked with pre-existing railways such as the Tbilisi-Baku and Kars-Gyumri-Tbilisi railways, the latter has been abandoned due to political disputes among the nations, which will be discussed in the political implications section of this study. Hence, the aim of the BTK project was to build a Kars-Akhalkalaki railway line – 76 km passing through Turkey and a 26 km line through Georgia. Additionally, the project envisaged to restore and rebuild 160 km of Georgia's already existing Marabda-Akhalkalaki railway. To modernize the existing railway and to construct the new line the project's initial total cost was given as 400 million USD, and later increased to 1 billion USD. In addition to this rough measurement of total cost, this study provides a country-by-country analysis in order to have a more accurate cost and benefit assessment below:

Financial cost of the project for Azerbaijan:

The State Oil Fund of the Republic of Azerbaijan (SOFAZ) has provided funds for the construction of the project in accordance with the Presidential decree No. 1974 of February 21,

2007, “On implementation the Activities of the Baku-Tbilisi-Kars Project”.¹⁸ According to the statistical report of January-June months in 2018, SOFAZ has allocated 7.5 million Azerbaijani manat (AZN) for the implementation of the BTK project during this period. Throughout the years 2007-2016, SOFAZ has calculated the total amount spent on railway construction as 630,0 million USD, which is 551,9 million manat.¹⁹ Even though SOFAZ has not yet officially reported the amount including 2018 expenditure, considering annual report of 2017 and quarterly reports of 2018, the preliminary estimates suggest 579,9 million manat.²⁰

Table 2. SOFAZ expenditures on the BTK railway construction (in million manat)

2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018 (Jan-Jun)
20,7	5,3	22,1	12,4	161,9	119,0	25,7	57,1	61,5	66,2	20,5	7,5

Source: Data Exported from SOFAZ (2018)

Additionally, the construction of the BTK line in Georgia has been supported by Azerbaijani funds that were provided through two credit lines. Georgia has availed the first loan of 200 million USD at an annual interest rate of 1% for 25 years and the second loan of 575 million USD at an annual interest rate of 5% for 25 years.²¹ The credit provided by Azerbaijan has been directed to the rehabilitation of the Tetrtskaro-Akhalkalaki line, construction of a railway station in Akhalkalaki and to other railway infrastructure. According to Trend News Agency, the second line of credit is not a state debt and will be returned as the railway starts to profit.²² Hence, for the reconstruction, implementation and rehabilitation of the Marabda-Turkey border (Kartsaxi) 180 km-long line, which is located between Georgia and Azerbaijan, the total amount of credit provided by Azerbaijan made 775 million USD.

¹⁸ State Oil Fund of the Republic of Azerbaijan. 2018. *Baku-Tbilisi-Kars New Railway*. http://www.oilfund.az/en_US/layiheler/baki-tbilisi-qars-demir-yolu.asp.

¹⁹ State Oil Fund of the Republic of Azerbaijan. 2016. "2016 Annual Report." Baku, pp 44.

²⁰ State Oil Fund of the Republic of Azerbaijan. 2018

²¹ Klimas, Evaldas, and Mahir Humbatov. 2016. "Baku-Tbilisi-Kars Railroad, The Iron Ground for the Silk Road." pp, 36.

²² Trend News Agency. 2011. *Agreement on "New Credit Line for the Baku-Tbilisi Kars" railroad*. July 1. Accessed September 15, 2018.

Financial cost of the project for Georgia:

There is no doubt that the delay in the construction of the BTK line has been due to the Russia-Georgia War in 2008 and resulting political upheaval in Georgia, which led to the allocation of Georgian funds primarily to military expenditures. According to data produced by the World Bank, the highest portion of Georgian GDP during 2007-2008 was directed to the military, which coincides with the beginning of the implementation of the project.²³ Therefore, political crisis in the country caused financial difficulties which made Georgia unable to afford the construction of the line from its own budget. For this reason, the Georgian part of the BTK project has been implemented without the financial participation of the government. However, due to the joint venture established between Azerbaijan Railways Closed Joint Stock Company (CJSC) and Georgian Railway Joint Stock Company (JSC), the Georgian Railway has been granted exclusive rights to operate their part of the railway line.²⁴

Given the fact that the rehabilitation and construction of the Georgian part of line was funded through credit (200 million USD at an annual interest rate of 1 % for 25 years and 575 million USD at an annual rate of 5% for 25 years) provided by Azerbaijan, the cost of the project for Georgia is calculated as following:

- 1. $200,000,000 \times (1 + (0,01 \times 25)) = 250 \text{ million}$**
- 2. $575,000,000 \times (1 + (0,05 \times 25)) = 1,293 \text{ million}$**
- Total: $250 \text{ million} + 1,293 \text{ million} = 1,542 \text{ million}$**

Financial cost of the project for Turkey:

The Turkish State Railways' investment allocations reported that the cost of the project was assumed to be 1,623,008 thousand TL between 1999-2019; however, the total cost of construction of logistics, monitoring and construction of the 76 km line was calculated as 1,485,034 thousand TL by 2016 and 50,010 thousand TL in 2017.²⁵ Referring to the Turkish State Railway annual report, the total amount of cost till 2017 for Turkey was indeed 3,158,052 thousand TL (around 840 million USD based on 2017 exchange rate).

²³ Stockholm International Peace Research Institute (SIPRI) and The World Bank. 2017. *Military expenditure (% of GDP)*.

²⁴ Georgian Railway. 2015. "Georgian Railway Annual Report."

²⁵ Turkish State Railways. 2017. *Distribution of Public Investments by Sectors in 2017*.

Table 3. Projects to be completed in Turkey (thousand TL)

Project name	Location	Start-End year	Estimated cost of project		Costs until 2016	Investments in 2017
			Outside	Total		Total
Baku-Tbilisi Kars railway	Ardahan, Kars	1999-2019	-	1.623.008	1.485.034	50.010

Source: Data Exported from Turkish State Railways Annual Report (2017)

It is important to note that, during the visit of the Head of Azerbaijan Railways Closed Joint Stock Company (CJSC) Javid Gurbanov to the Kars Province, he signed an agreement on the construction of a logistics center in the Kars Province of Turkey, which is aimed to be commissioned in October 2018. The cost of the construction of the logistics center was estimated as 27.34 million USD (94,3 million TL).²⁶

Economic Assessment of BTK Railway Project

Despite of the existing oil and gas trade links, such as Baku-Tbilisi Ceyhan and Baku Tbilisi Erzurum lines, the new BTK railway promises to expand these limited energy relations to include all kinds of goods and services and boost the economies of the countries. There is no doubt that the purpose of initiating the BTK railway project was to shape the economic environment of the participating countries through direct and indirect economic benefits. In terms of the direct, in other words short-term benefits, the BTK railway provides transit fees to the countries it passes through (Azerbaijan, Georgia and Turkey) and increases overall economic engagement in the logistics industry.²⁷

Azerbaijan

According to the preliminary estimates of Mahir Humbatov, a co-author of two books on the railway, the BTK railway has the potential “to generate no less than 300-400 million AZN for Azerbaijan” (177-237 million USD) annually.²⁸ Examination of the income revenues

²⁶ Azer News. 2017. *Turkish Logistics Center within BTK to Open in Autumn 2018*. August 10. Accessed September 16, 2018. <https://www.azernews.az/business/117414.html>.

²⁷ Caspian Policy Center. 2017. "CPC Special Brief: An Economic Perspective for the Baku-Tbilisi-Kars Railway."

²⁸ Humbatov, Mahir. 2017. "The South Caucasus-centred Transport Hub: The Crossroads of the East-West and the North-South Corridors." *Center for Strategic Studies*, pp 62. (1 News Agency 2013)

from railway transportation in previous years suggests that rail transit services have generated increased revenues over time, as seen in Table 4 below.

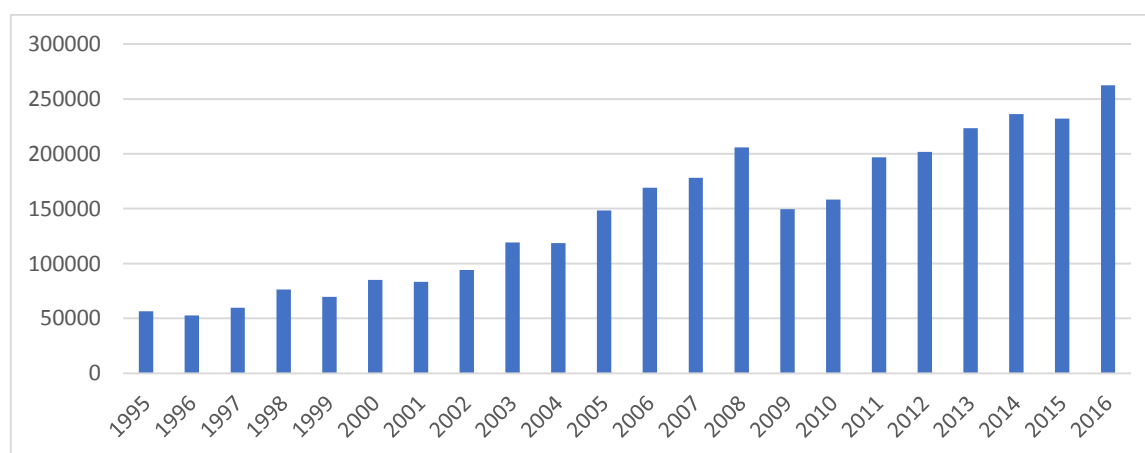
Table 4. Income from transportation per 1000 manat

	2010	2011	2012	2013	2014	2015	2016
Total	3,065,804	3,283,599	3,341,800	3,508,772	3,678,120	4,005,562	4,780,684
Railway	158,382	196,683	201,855	223,315	236,303	232,077	262,435
Sea	107,221	109,710	114,580	97,901	102,339	93,990	160,096
Air	388,870	557,911	617,870	779,843	837,820	828,058	1,053,949
Pipelines	1,712,629	1,605,901	1,535,006	1,448,865	1,439,109	1,679,770	2,047,004
oil pipes	1,563,281	1,444,549	1,359,306	1,249,234	1,195,644	1,325,903	1,515,830
gas pipes	149,348	161,352	175,700	199,631	243,465	353,867	531,174
Road	669,927	784,626	831,682	916,044	1,020,030	1,128,662	1,214,938
Tram						-	-
Trolleybus						-	-
Metro	28,775	28,768	40,807	42,804	42,519	43,005	42,262

Source: Data Exported from State Statistical Committee of Azerbaijan (2017)

As seen in Table 4 above, the findings from the State Statistical Committee of Azerbaijan suggest that even though the contribution of railroad transport was not as significant as other modes of commercial transport, it has grown along a positive trend over the years. Additionally, as seen in Table 5, overall income from transportation continues to grow, creating an important chance for increased revenues from rail transport.

Table 5. Income from Transportation (thousand manat)



Source: Data Exported from State Statistical Committee of Azerbaijan (2017)

According to Mahir Humabtov's and Evaldas Klimas's examination of these numbers, Azerbaijan needs to make considerable amount of new investments in its infrastructure to meet market needs.²⁹ Their analysis highlights some recent changes and structural reforms, along with investments and close collaborations with financial institutions on international level. However, according to the authors, to assure the successful and sustainable implementation of the BTK railroad, Azerbaijan needs to have a proper supportive infrastructure (physical, administrative, technical and digital). From that perspective, Azerbaijan has stated its readiness to provide needed condition for the smooth operation of export from Asia to the European markets during the business forum in Aktau.

As an effort in the aforementioned direction, Rovshan Ibrahimov has claimed that in 2014, the construction of a production and logistics center for Azerbaijan was initiated at Aktau port.³⁰ To achieve the expansion of transit opportunities, the development of economic partnerships and deepening of market principles through the BTK railway transportation, the heads of customs' institutions of all three countries have agreed to deepen their cooperation at the trilateral high-level meeting which was held in Baku in 2017. Within the framework of the meeting, the participating countries agreed to sign a joint declaration aiming to promote their "customs structures, cargo transportation, service modernization, and information exchange".³¹

The examination of trade turnover of Azerbaijan with Turkey and Georgia over the last decade indicated that there has been an observed increase in the numbers in 2017. This change can be understood as a successful implementation of partnership initiatives among the countries as mentioned above.

Table 6. Azerbaijan's Foreign Trade Turnover with Turkey and Georgia

Years	Turkey	Georgia
2005	588,960.9	253,934.9
2006	773,185.0	334,477.3
2007	1,680,895.5	406,750.5
2008	1,433,326.1	542,202.8
2009	1,014,604.2	454,891.4
2010	942,336.1	461,382.1

²⁹1 News Agency. 2013. *Azerbaijan is Ready to Facilitate Goods to Western markets*. June 20. Accessed September 16, 2018. <http://www.1news.az/news/azerbaydzhan-gotov-sposobstvovat-besprepyatstvennomu-vyrodu-kazahstanskih-tovarov-na-zapadnye-rynki>.

³⁰ Ibrahimov, Rovshan. 2016

³¹ Hasanli, Azad. 2017. *Azerbaijan, Turkey Creating Info Exchange System on Transit Transport*. July 19. <https://en.trend.az/business/economy/2778989.html>

2011	1,758,204.0	624,810.2
2012	2,120,430.2	700,660.2
2013	1,989,790.7	650,466.3
2014	1,789,134.2	623,437.9
2015	2,648,642.1	564,189.4
2016	2,314,398.4	394,888.6
2017	2,640,046.20	545,497.50

Source: Data Exported from State Customs Committee of Azerbaijan (2017)

Apart from the short-term benefits, Azerbaijan, like many energy-rich countries, is interested to diversify its economy to assure more sustainable growth. Therefore, although it is overly optimistic to assume that the BTK project can fulfil the targeted diversification of the Azerbaijani economy itself, it will provide a significant amount of non-oil sector revenues. It is estimated that the BTK railway will transport 6.5 million tons of cargo and a million of passengers on its initial stage and 17 million tons of cargo together with three million passengers by 2030.³²

Georgia

Georgian economists consider the BTK “the project of the century” and believe that it is worth every penny being spent on it.³³ They suppose that the scale of the project allows to strengthen Georgia’s position in the region. Eric Livni, director of the International School of Economics at Tbilisi State University, goes beyond and argues that due to the large scale of transit potential of BTK project, it is also possible to load goods from Georgia and increase the transit possibilities, though it is primarily intended to carry flows from Azerbaijan.³⁴ Additionally, Eric Livny believes that the BTK railroad will boost competition among different modalities of transport and will lead to lower transport tariffs, better services, and high volumes of transit cargo. Freight transportation is the principal source of revenue of Georgian Railway Joint Stock Company (JSC), which is the sole railway operator in Georgia. According to the

³² Railway Technology. 2013. *Baku-Tbilisi-Kars (BTK) Rail Line, Azerbaijan, Georgia, Turkey*. Accessed September 16, 2018. <https://www.railway-technology.com/projects/baku-tbilisi-kars/>.

³³ Open Democracy Russia and Beyond. 2015. *Is the Baku-Tbilisi-Kars Railway Worth the Fuss?* November 2. Accessed September 16, 2018.

³⁴ Open Democracy Russia and Beyond. 2015.

annual report of 2016, 54% of total freight transport was dry cargo , while liquid (crude oil) was 46%.³⁵

Table 7. Freight transportation volume in Georgia

Million tons

Present

	2016	2015	2014	2013	2012	2016	2015	2014	2013	2012
Liquid cargoes	5,494	6,748	7,514	9,087	9,471	46.2%	47.7%	45.1%	50%	47.2%
Oil products	3,686	5,884	5,838	5,131	4,753	31%	41.6%	35%	28.2%	23.7%
Crude oil	1,808	864	1,676	3,957	4,718	15.2%	6.1%	10.1%	21.8%	23.5%
Dry cargoes	6,388	7,395	9,159	9,098	10,605	53.8%	52.3%	54.9%	50%	52.8%
Ores	1,454	1,458	1,820	1,956	2,176	12.2%	10.3%	10.9%	10.8%	10.8%
Grain and grain products	448	716	861	952	1,424	3.8%	5.1%	5.2%	5.2%	7.1%
Ferrous metals and scrap	663	892	1,064	931	1,105	5.6%	6.3%	6.4%	5.1%	5.5%
Sugar	499	464	618	610	689	4.2%	3.3%	3.7%	3.4%	3.4%
Chemicals and fertilizers	429	507	508	481	508	3.6%	3.6%	3%	2.6%	2.5%
Construction freight	1,065	1,426	1,793	1,410	1,594	9%	10.1%	10.8%	7.8%	7.9%
Industrial freight	271	261	407	546	707	2.3%	1.8%	2.4%	3%	3.5%
Cement	62	80	380	637	672	0.5%	0.6%	2.3%	3.5%	3.3%
Other	1,496	1,590	1,709	1,574	1,730	12.6%	11.2%	10.2%	8.7%	8.6%
Total	11,882	14,143	16,673	18,185	20,076	100%	100%	100%	100%	100%

Source: Data Exported from Georgian Railway Annual Report (2017)

The Prime Minister of Georgia Giorgi Kvirikashvili, speaking at the Silk Road Forum in Tbilisi, stressed that the BTK will “open up new opportunities which will ensure economic growth and security”.³⁶ Georgian authorities have also promised that the project will provide security and job for the population of Akhalkalaki, where the gauge-changing station is located. However, the research conducted by the European Union to produce the Akhalkalaki Local Development Strategy has reported that continued unemployment is an important problem. Estimates suggest that the population has decreased by 40% due to search of employment opportunities abroad. The report also indicates that although the majority of the population is employed in agriculture and construction, they do not have vocational or higher educational qualifications in these field.³⁷ This allows to conclude that within the Georgian part of the

³⁵ Georgian Railway. 2016. "Annual Report 2016."

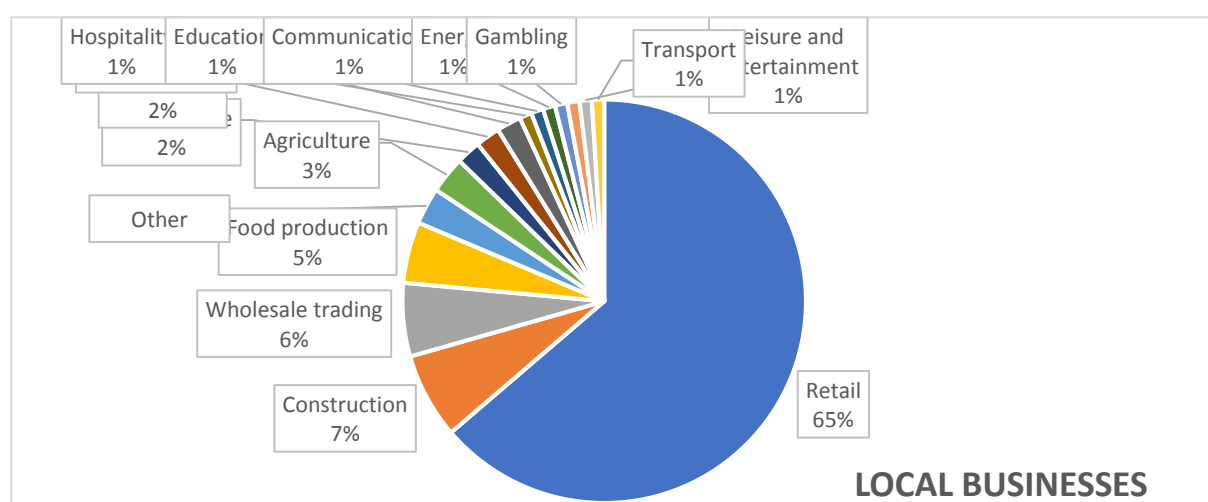
³⁶ Jardine, Bradley. 2017. *Georgia: New Europe-Asia Rail Route Slow to Produce Economic Benefits-Locals*. December 4. Accessed September 16, 2018. <https://eurasianet.org/s/georgia-new-europe-asia-rail-routeslow-to-produce-economic-benefits-locals>.

³⁷The European Union for Georgia. 2017. "Baseline Survey for Akhalkalaki LDS Development Study of the Community Problems and Needs." Tbilisi.

railway, there appears to be a scarcity of specialized workforces to work in the construction and operation of the line. Hence, to support the engagement of the Georgian population in the project as promised, the organization of trainings and workshops would be significant.

Additionally, among 523 companies registered in the region, retail (most of which are small-scale enterprises) represents 65% of the total 340 business entities, while construction and transportation are the lowest proportion (see Graph 1). Among these registered companies, however, none of the Akhalkalaki local businesses were involved in the BTK project. Indeed, these underdeveloped small-scale businesses could grow through a collaborative work in the BTK project.

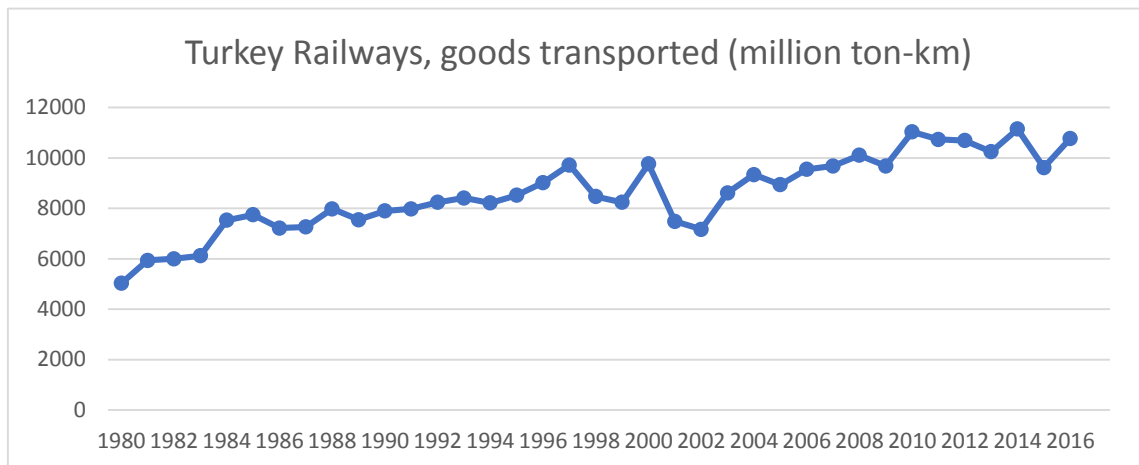
Graph 1. Baseline Survey for Akhalkalaki



Turkey

Annual estimations suggest that in 2014 and 2016, the volume of transported goods has been the highest, with 11145 million ton-km and 10773 million ton-km, respectively. Even though there have been fluctuations over the years, generally, developments in the amount of goods transportation have been positive. Especially the comparison of 2015 and 2016 shows that there has been a drastic increase, by 1155 million ton-km, which is a positive signal for further developments (see Graph 2).

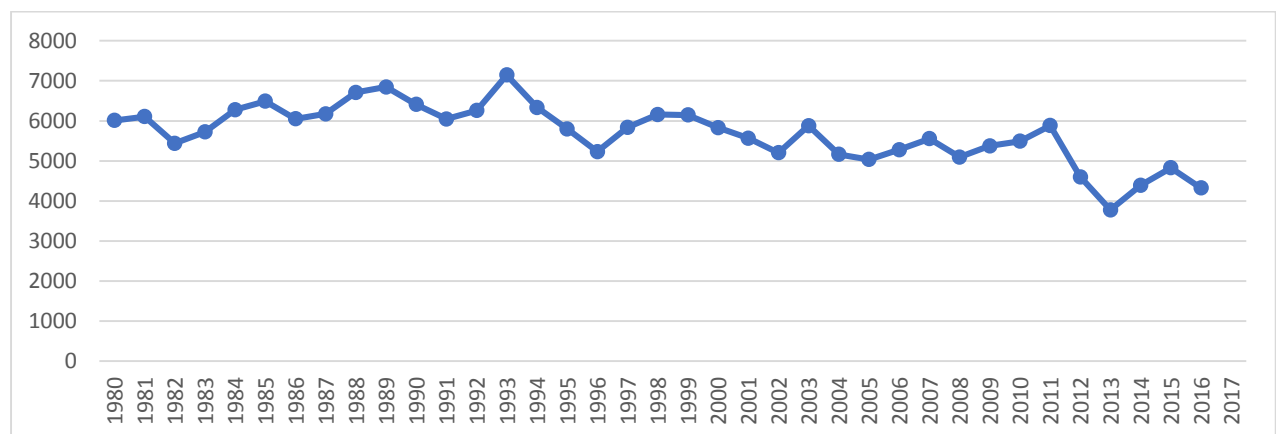
Graph 2. Railway goods transported in Turkey between 1980-2016



Source: Data exported from the World Bank, 2017

However, the number of passengers carried by railways has declined over the years, as seen in Graph 3 below. Passenger traffic declined sharply in 2014, and was at its lowest estimated number (3775 million passenger-km). Though the passenger traffic increased in 2015, it again dropped in 2016. The report by the World Bank suggests that this decline is due to the shift to air transport as a result of the special promotions of airlines and the opening up to the private sector.³⁸ Additionally, according to the Turkish railway and urban transport review, additional factors as renovated roads and highways caused the decline.³⁹ Hence, cheap and fast planes attract long-distance passengers, while renovated state roads suggest better and faster bus transportation than trains in most cases and so on.

Graph 3. Railway passengers carried in Turkey (1980-2016)



Source: Data exported from the World Bank (2017)

³⁸The World Bank. 2009. "Railway Reform in South East Europe and Turkey: On the Right Track? ."

³⁹Uysal, Onur. 2017. "Train Ridership Falls in Turkey." *Turkish Railway Journal and Review*.

Overall, the positive changes in the volume of goods transported in Turkish railways might promise benefits for the economy; however, the decline in the amount of passenger traffic would not be sufficient to bring as great profits as estimated.

Political Implications- Relevant Parties’ Viewpoints

In this section of the paper the geopolitical analysis of the construction of the BTK railroad in the Southern Caucasus region is presented. Considering the geopolitical dimension of the BTK project’s different parties, each countries’ viewpoints are discussed below:

Azerbaijan

The issue of Nagorno-Karabakh (NK) plays a major defining role for Azerbaijan in its policy toward Armenia. Azerbaijan, the main initiator of the BTK project, has a firm position against the construction of any transportation road that would involve Armenia until the comprehensive settlement of Nagorno-Karabakh conflict started. The leadership in Azerbaijan is not satisfied with the current status-quo in the conflict, and demands constructive talks.⁴⁰ This position gives Azerbaijan an important leverage in the resolution of the conflict, since, through inability to join regional cooperation, Armenia misses important economic opportunities.

However, although Azerbaijan has articulated that economic cooperation would be possible after the resolution of the Nagorno-Karabakh conflict, allowing the railway to pass through Armenia, Azerbaijan, indeed, may risk the integrity of the transportation route. Therefore, even though Azerbaijan demands Armenia to withdraw its troops from the territories surrounding Nagorno-Karabakh itself – at the initial phase of settlement – in order to be able to cooperate on an economic level, operationalizing the railway lines that would pass through Armenia would not be in the strategic interest of the government of Azerbaijan, as it would give Armenia a leverage to manipulate the project due to its emerging position as a main transit country.

⁴⁰ President Ilham Aliyev 2007

Despite its strong position against cooperation with Armenia, Azerbaijan, however, neglects the fact that the BTK railroad passes through the Georgian city of Akhalkalaki, where ethnic Armenians comprise a majority of the population (94.3%).⁴¹

Turkey

Regarding the NK conflict, the close ally of Azerbaijan, Turkey adopts the same diplomatic posture, despite of the all lobbying attempts of local Turkish entrepreneurs who consider that the reopening of the Kars-Gyumri railroad (between Armenia and Turkey) would prevent informal trade between two countries that is costly and unsafe.⁴²

Additionally, the BTK railroad is significant for creating strong ties with Eurasia for Turkey. It is often argued that the continued delays in EU membership has directed the government (AKP-led) of Turkey towards the east, which, in return, resulted in Turkey's increased economic and political engagement with Central Asia. Hence, the BTK project creates an important trading network both in Central Asia and in Europe for Turkey and reestablish country's former economic role as a bridge between East and West prior to the collapse of the antient Silk Road. As a result of the project, Turkish transportation infrastructure would be upgraded, and the economy would be diversified away from the Middle Eastern markets to more secure European and Central Asian markets.

Georgia

Samuel Lussac argues that the integration of the three countries in the region has marginalization effect on Armenia, who is mainly dependent on Russia and Georgia in its external trade.⁴³ The author regards that this policy toward Armenia in the project benefits Georgia, since the reopening of the Kars-Gyumri-Tbilisi railroad is not in the strategic interests of Georgia, who is holding a major transit country status for Armenian imports and exports.⁴⁴ According to the World Bank's "Armenia Trade Diagnostic Study" of 2002, its landlocked location due to the geography and regional political conflicts, Georgia and Iran provides the only possible transit routes to integrate into the world economy.⁴⁵ As a result of the conflict between Armenia and Azerbaijan, a closed border between Turkey and Armenia, and given the fact that Georgia has a sea port, Georgia has become the only way for the transit of economic

⁴¹Lussac, Samuel. 2008.

⁴²Lussac, Samuel. 2008.

⁴³Lussac, Samuel. 2008.

⁴⁴Lussac, Samuel. 2008.

⁴⁵The World Bank. 2002. "Armenia Trade Diagnostic Study."

activities. At the same time, in the landlocked geopolitical situation, Georgia provides the only corridor to Russia, who is one of the important trade partners of Armenia as well.⁴⁶ This provides additional leverage for Georgia over Armenia.

In, addition to the benefits gained through marginalization of Armenia, the BTK project complements Georgia's vision to act as a transit hub between East and West and is in line with Georgia's integration into Europe. According to the German Institute for International and Security Affairs, Georgia positions itself as a linking hub on China's New Silk Road, where BTK railway route constitutes an integral part. The report suggests that Georgia is primarily expanding infrastructure to establish itself as a main transit center between Eastern (China) and European markets, which makes Georgia interested in the BTK railway project.⁴⁷

Armenia

As mentioned already, the NK conflict between Azerbaijan and Armenia has resulted in Baku pushing Yerevan out of the regional projects, which has made the Armenian economy vulnerable and led to the continuing souring of relations with neighboring countries (Azerbaijan and Turkey). Due to this reason, Azerbaijan and Georgia have been the only Caucasus countries benefiting from the existing economic regional projects.

Although the government of Azerbaijan has articulated its unwillingness to involve Armenia and abandoned the already existing railroads passing through Armenia, there appears to be no law or regulation preventing Armenia from joining the project in a roundabout manner.⁴⁸ Namely, as Georgia is the sole transit country for Armenia's imports and exports, Armenia would be able to participate in the project and transport goods through the railroad by means of its existing trade to Georgia, as nothing in the agreement would be able to prohibit import or export from Georgia making use of the railway.

Russia

Perhaps the crucial political factor of the BTK project is that it would allow the regional member countries to turn their geographic position into an advantage all while bypassing Russia. As a result of leveled embargos against Russia over the Ukraine conflict, many

⁴⁶United Nations Development Programme. 2007. "Armenia and Georgia Economic Relations: Unrealised Opportunities." Yerevan.

⁴⁷Franziska, Smolnik. 2018. German Institute for International and Security Affairs.

⁴⁸ *Law of the Republic of Azerbaijan about the Agreement on "Baku-Tbilisi-Kars Railway"*. 2007. 269-IIIQ (Baku April 10).

products have been banned from entering the Russian terrain and created “bottleneck” for the European products that could have been shipped by rail to China. Even though, currently, those sanctions against the EU agricultural products have been dropped, the BTK project is still versatile and strong in providing alternative route. Indeed, it is generally perceived that in the case of healthy competition between corridors transport costs could be adjusted to lower prices and the amount of goods flowing would increase.

EU and Western Countries

Even though Asia and Europe are linked through various trade routes, BTK has added value to the overall trade benefits of Europe. Given the fact that other transit corridors are on the southern side, this new line is an important part which was missing in the puzzle. The U.S. has not developed a new tangible policy for the region after the 2008 Russian-Georgian War, however it does not imply that the U.S has abandoned the region and is willing to leave it for the Russian dominance. In fact, the BTK railway is in-line with U.S. priorities in the region, which prioritizes economic development and good governance.

China

China, on the other hand, has been searching for alternative routes to improve its connectivity across Eurasia with its “One Belt, One Road” strategy, initiated by Chinese President Xi Jinping in 2013. So far, it has been using the Russian route to reach Europe, connecting Chongqing in China to Duisburg in Germany in 16 days. The realization of London-Beijing connection in summer 2017 allowed frights to cover the route in 18 days. Should the BTK line prove able to decrease the duration even if only fractionally, it will definitely become financially viable and an attractive alternative, while decreasing Russian profits along the way.

Concluding Remarks

To conclude, the implications of the BTK project should not be generalized to all parties, as each country has distinct national interest for joining the railroad. Although the member countries share the same geographical location between East and West, their historical backgrounds and economic situations make the governments of these countries seek different purposes in terms of economic and political advantages. Having, however, an all-encompassing dimension, the BTK project allows the member countries to manifest their interests.

Analyzing the expenditure spent on the project by each member country, the study identified that Azerbaijan is a dominant country, having provided the largest amount of funding for the construction and rehabilitation of the railroad. Given this reason, Azerbaijan appears to be the most interested participant in the project, as the economy is highly dependent on the export and transportation of gas, oil and oil products and needs to be diversified. Additionally, the initiation of the project strengthens the integration of Caucasus countries, while isolating Armenia geopolitically in the region, which corresponds to the regional policy of Azerbaijan. Hence, for Azerbaijan the BTK project carries both political and economic importance. From a political perspective the project allows Azerbaijan to toughen its position towards the NK conflict and increase its regional importance. The economic benefits, however, tend to be felt in the long-run, as the government has spent a huge amount of capital now and the ability to diversify the economy away from oil-gas sector will take time.

Georgia, on the other hand, seeks rather geopolitical outcome from the project, which, in turn, would also bring economic advantages. To put it simply, the isolation of Armenia fulfils the strategic objectives of the country and positions Georgia as a main transit country not only for the Central Asian products but also for Armenia's imports and exports. Additionally, considering that the Georgian government has not participated in the financial support of the project at present, it can be concluded that the BTK project would bring economic benefits as a result of successful political strategy for Georgia.

Although Turkey has already established good diplomatic relations with member countries and Central Asia, the BTK project's objectives coincides with the broader geopolitical goals of the country. Given the fact that Turkey has long path to go to join the EU, the project provides possibilities to link with Asian countries, as in the future these two markets would complement each other.

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