

AZERBAIJAN

THE GREAT GAME COMES TO BAKU

Who will tap—and transport—the Caspian's sea of oil?

Oil and the venerable Caucasian town of Baku have had a long and profitable association. In 1900, Baku, then a Russian outpost, was a cradle of the fledgling oil industry on a par with Oil City, Pa., and East Texas. At about that time, Russian writer Maxim Gorky described booming Baku's clutter of wooden derricks and huts as "a dark hell painted by an artist of genius."

Now Baku, the capital of independent Azerbaijan, is poised to open a dramatic new chapter. Foreign companies are ready to plunk down tens of billions of dollars to help open the Caspian's riches. Baku, a city of 1.5 million with an old world, Middle Eastern flavor, would be the major staging area. Azerbaijan and neighbors Kazakhstan and Turkmenistan could have well over 100 billion barrels of oil, making them comparable to Iraq or Kuwait and potentially bigger than Alaska's Prudhoe Bay or the North Sea. "We think the potential of the whole region is between 100 billion and 200 billion barrels. That is why there's such enormous interest by the industry," says Thomas M. Hamilton, president of Pennzoil Exploration & Production Co., which is in on two big Caspian projects.

Leading the pack in Azerbaijan is a 12-member consortium that is headed by British Petroleum Co. and Amoco. Pennzoil, Exxon, the Russian giant Lukoil, and Socar, the Azeri national oil company, are also partners in the Azerbaijan Independent Operating Co. (AIOC).

The first flows will be modest, about 50,000 barrels a day, but the plan is to increase them to 700,000 barrels a day. As the deal is structured, Azerbaijan will keep 80% of the revenues, meaning the nation of 8 million will receive an incredible windfall of about \$80 billion over the 30-year life of the project.

BIG PLAYERS. But before the Azeris back into high gear again, there are huge uncertainties to overcome. The big drawback about the Caspian is that it is landlocked. Proposed pipeline routes go through unstable Georgia, devastated Chechnya, or Armenia, which has been at war with Azerbaijan since 1988.

What's more, all the region's big players—Iran, Turkey, and especially Russia—want to influence the Caspian re-

CHERNOMYRDIN, AN OLD ENERGY HAND, WILL PUSH RUSSIA'S CLAIMS IN AZERBAIJAN HARD



publics and would like a slice of the oil revenues. Often through oil companies but sometimes by other means, the competing powers are playing out a latter-day version of the 19th century Great Game, in which Britain and Czarist Russia fought and intrigued for influence in this area.

Moscow has been putting the screws to Azerbaijan by covertly supporting the Armenian side in the war over the break-away enclave of Nagorno-Karabakh. "The Russians want to keep Azerbaijan in the Russian fold. There will be no exports from that region without the Russians sanctioning them," says Julia Nánay, an analyst at Petroleum Finance Co.

A new factor in Russia is the ascendancy of Prime Minister Viktor S. Chernomyrdin, a former gas industry chief who is a master at the international energy game. Chernomyrdin has been pushing long-stalled foreign oil projects in Russia. Exxon and Japan's Sodeco in late June signed a \$12.7 billion contract for a monster oil and gas project on

Sakhalin island in Russia's Far East.

The Western oil companies and the Azeris feel Chernomyrdin is a reasonable man with whom they can do business. They have cut Lukoil, which is close to Chernomyrdin, in on 10% of the AIOC and 34% of another project with Pennzoil. The thinking is that if Chernomyrdin and his oil and gas crowd prevail in the battles now raging in the Kremlin, a way will be found to get the oil out. If hard-liners regain the upper hand in Russia, all bets are off. Chernomyrdin's camp recently won a big victory when they defeated a no-confidence vote in Parliament and Yeltsin ousted several hard-liners.

PIPELINE PROBLEM. One of the optimists is Natick A. Aliyev, head of the Azeri company Socar. He holds court in a waterfront mansion on the Caspian—once owned by a pre-Soviet oil millionaire. Aliyev thinks the consortium could begin pumping about 80,000 barrels a day of "early oil" by late 1996. "The point of early oil is to show that the consortium works," Aliyev says.

By September, the consortium will choose a route for early oil that won't require new pipelines. The big decision comes later: the selection of a new pipeline that could cost \$1.5 billion and handle a much larger volume. That choice means everything to the success of the AIOC project, others like it, and the political and economic future of Azerbaijan.

The AIOC doesn't want to get into a mess similar to the Chevron Corp. ordeal in Kazakhstan. Various political and financial battles have kept Chevron from finding an export route for the oil from its \$20 billion Kazakh project.

Moscow wants the Azeri pipeline to terminate at its Black Sea port of Novorossiysk, with oil being shipped through Turkey's Bosphorus Straits. But Turkey balks at a plan that would deprive it of transport revenues and expose Istanbul to the risks of tanker spills and

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explosions in the narrow Bosphorus. The Turks are stumping for a terminus at their southern port of Ceyhan.

The pipeline game is drawing in some of the world's most brazen entrepreneurs. One is Roger Tamraz, a Cairo-born U.S. citizen who is a veteran oil wheeler-dealer. Tamraz, head of New York-based Oil Capital Inc., on June 6 announced a new plan to build a large, \$2 billion pipeline through Armenia. Says Tamraz: "The fact of the matter is that you need several pipelines. You're

going to have at least 1 million barrels a day of oil coming out of the region before long, and there's no way all that oil can go through the Bosphorus."

LOST WEAPON. Washington is also being drawn in. Under pressure from such oil heavyweights as Amoco, Mobil, Exxon, McDermott, Brown & Root, Bechtel, and Chevron, the Clinton Administration is increasingly being pushed to alter its pro-Russia policy and start backing the republics. But Washington may have thrown away a valuable weapon against Russia when it launched a campaign against Iran this spring. The companies could have pressured Russia by negotiating for a route through Iran or by swapping their oil with the Iranians for oil at the Iranian export terminals on the Persian Gulf. But by forcing the Azeri consortium to rescind the 5% share it had given the Iranians, and by ruling out a pipeline route that would go through Iran, the White House drove the one regional power with resources to match Russia's a bit closer to the Kremlin.

That's why the outcome of the battles in the Kremlin is being watched so closely in Baku and elsewhere. The key to the future of this potentially huge energy source probably lies there.

By Peter Galuszka in Baku, with John Rossant in Rome, Gary McWilliams in Houston, Russell Mitchell in San Francisco, and Stanley Reed in New York

GASPIAN PIPELINES

Companies and countries are fighting for the enormous energy riches of the troubled region. But wars and geopolitics are holding the projects up.

