

WHAT THE SOUTH CAUCASUS COULD BE:

## EXPLORING THE ROLE OF ECONOMIC INITIATIVES AS PEACE BUILDING TOOLS IN THE NAGORNO-KARABAKH CONTEXT

EXPERT ROUNDTABLE AND POST-CONFLICT SCENARIO BUILDING WORKSHOP

### SUMMARY OF CONCLUSIONS

BERLIN, GERMANY, 7<sup>th</sup> AND 8<sup>th</sup> JULY, 2014

## COMMON HERITAGE, SHARED FUTURE?



## **Overview**

The second stakeholder consultation round in EGF's ongoing Nagorno-Karabakh (NK) research took place on 07-08 July 2014 in Berlin (Germany), including the introduction of a post-conflict scenario building workshop. More than 30 experts from Armenia, Azerbaijan, and international partner NGOs and institutions attended this event, held in a constructive atmosphere of 'exchange between gentlemen'. This meeting was the first concrete step towards exploring the idea of a roadmap leading towards an economically integrated South Caucasus, and establishment of a deeper **platform for exchange of information** between Armenian and Azerbaijani experts. During the post-conflict scenario building workshop, regional participants simulated the negotiation of a roadmap for the implementation of economic components of a peace agreement built upon the Madrid principles, encompassing joint economic measures in areas such as energy, transport, trade, rehabilitation of the territories affected by the conflict, and the return of IDPs to their homeland.

## ***Reflections on the First Consultation Round (Brussels, March 27, 2014)***

Prior to the Berlin session, an earlier consultation round was held in Brussels on 27 March 2014, which revealed a possibility for a new approach to pursuing the strategic aims of EGF's current research on Karabakh. The Brussels consultation round alluded to the creation of a platform for exchange of information between Armenian and Azerbaijani experts on energy, transport, trade issues, the rehabilitation of the territories affected by the conflict and the return of IDPs to their homeland. It was deemed at the time that such exchanges could lead to development of post-conflict scenarios for Karabakh, based on a roadmap leading towards an economically integrated South Caucasus.

The roadmap would be underpinned by a number of very broad and uncontroversial principles (also known as the Brussels Consensus on post-conflict regional integration scenarios in the South Caucasus), it was determined. These include the right of all people to live in an environment of peace and security; a shift in government strategy from preparing for war to building enduring peace and fostering economic development; good neighbourly relations as a basis for peace building; the right of all people to strive for economic prosperity; and the right of all IDPs and refugees to return to their homes and/or lands and live there in peace and security. The Berlin session was further based upon many of the positive elements that came out of the Brussels consultation round.

## ***Introductory Remarks: Berlin Session (July 7-8, 2014)***

At the commencement of the Berlin session, Dr Marat Terterov, the Principal Director and Founder of the EGF, stated that the aim of the current research is to develop an alternative narrative on Nagorno-

Karabakh through Track 2 diplomacy on conflict resolution. To that end, he pointed at developing economic incentives, as well as establishing links between economic dialogue, on the one hand, and political and security negotiations, on the other, as key priorities. He further wondered whether a different way of thinking can be instilled in the minds of decision makers on NK through highlighting the commercial and economic value of peace. This way, leaders may be offered flexibility on making the tough decisions related to NK conflict resolution, through providing them with a thorough consideration of post-conflict scenarios. From this perspective, rethinking regional cooperation in the South Caucasus (SC) may actually start with a blueprint for regional development focused on Armenia and Azerbaijan.

Ambassador Douglas Townsend, Senior Advisor, International Tax and Investment Centre, Washington DC, and former Australian Ambassador to Kazakhstan and Hungary, thought that this seminar should bring to the attention of major international investors in infrastructure projects new business opportunities in the South Caucasus. He further elaborated on his organization's support to achieving that goal.

### ***Session I: Post-conflict Regional Cooperation in the South Caucasus: A Strategic Plan for Regional Development?***

EGF's ongoing research suggests that economic incentives are unlikely to be a panacea for conflict resolution in the NK context. However, it likewise shows that expert discussion on economic issues may be highly useful in 'preparing the ground' for some level of flexibility in the current rigidity which grips the parties regarding NK. Starting a public debate amongst NK stakeholders on the advantages/disadvantages of choosing peace and regional economic development over the current state of hostility may ease some of the tension in the NK context. This view appears to be broadly supported within international peace building circles relevant to NK. The aim of this session was to explore the scope of a 'strategic plan for regional development', or a 'blueprint for economic development in the South Caucasus' as a key trigger for such a public debate. Speakers were asked to elaborate on potential 'elements of cooperation' that could lead to something far bigger and grander, if a strategic plan for regional development could be articulated by experts from Armenia, Azerbaijan and international circles working together.

Speakers' briefings and the ensuing discussion highlighted the following **key messages**:

- Although it is difficult to de-politicise the economic dialogue, we need to think 'outside the box' to break the current stalemate on NK conflict resolution. For example, a legal framework for trade is necessary to start moving from a mere economic dialogue to the practical implementation of economic incentives. The green line regulations in Cyprus may serve as a potential model. However, questions remain on how we could come up with a legal document in the absence of a political compromise on conflict resolution. How could stakeholders be motivated to adhere to/come up with a legal framework? Two possible options were proposed: 1) A leading external actor (i.e. the EU, who has already done it in the Western Balkans); 2) A combination of motivating one conflicting party via economic interests, and the other party by the prospects for joining an international organization (the China-Taiwan conflict and the role of ASEAN were evoked).

- Establishing a legal and/or political framework for economic interaction is very important for both Armenia and Azerbaijan in order to help secure public support for the peace process. However, economic interests must be genuine to drive cooperation on both sides. Otherwise, economic incentives may never work in conflict resolution. In addition, the psychology of economic cooperation should be advanced across the conflict's dividing lines.
- Azerbaijan is becoming economically stronger and able to support both post-conflict reconstruction and regional cooperation. This is an opportunity which should not be missed. Azerbaijan's extensive and effective cooperation with Georgia might be replicated in relations with Armenia in a post-conflict context. Azerbaijan may be able to invest 25 billion USD in rebuilding the territories around NK, on the basis of a post-conflict strategic plan for regional development. This could include building an urban agglomeration on the axis: Aghdam-Shusha-Khankhendi/Stepanakert, and a special economic status granted to NK (similar to the one granted by China to Hong Kong).
- The synchronization of the political and security agenda with economic cooperation is essential for successful conflict resolution in NK. From an Azerbaijani perspective, a successful application of economic incentives in conflict resolution is conditional to the implementation of two principles: 1) The return of the seven districts around NK – Baku wants to rebuild these territories where Armenia and NK have no interest to invest; 2) An interim political status for NK, within the territorial integrity of Azerbaijan, with international security and self-governance guarantees. The return of IDPs to their homes is also a vital component of the peace process.
- Armenia is looking with more interest at economic cooperation with Turkey rather than with Azerbaijan. There is lack of political will (from all sides) to solve this conflict. This is partly because there is no constituency for peace, while the economic incentives are not properly articulated yet. The biggest security threat for Armenia is insignificance (in the international context), if it does not reform its political and socio-economic structures and legislation. Confidence building is needed between Armenia and Azerbaijan. There might be at least two areas of cooperation opportunities between Armenia and Azerbaijan: countering shared threats (earthquakes, wild fires, water management, and nuclear security), and job creation and training for IDPs. Successful conflict resolution in NK requires: more local politics rather than geopolitics; broadening the constituency for peace; and fostering a new model of cooperation: to agree to disagree, but cooperate wherever it is possible.
- Azerbaijan invested in Turkey 10 times more than Turkey has invested in Azerbaijan in recent years. This fact should be also understood in Yerevan, where expectations for economic cooperation with Turkey might be overstated. Azerbaijan needs Armenia as an economic partner in the South Caucasus. For example, they may include Armenia and Armenians from NK in the new Silk Road strategy which is currently developed in Baku. Both Armenia and Azerbaijan have to recognize the benefits of doing business with each other, but these are difficult to assess when there is no business on the table.
- It is too premature to conclude that 'Armenia is doomed to economic collapse' while Azerbaijan has a 'glorious economic future in front of it'. Armenia has partially diffused the economic pressure created by the Azerbaijani-Turkish blockade, while the dynamics of the global demand for oil and gas are set to further dominate Azerbaijani economic growth prospects. In fact, the main challenge

for both countries is not so much the threat of economic collapse, but rather “to build-up a sound framework for good economic governance”.

- Transforming any form of “Armenian-Azerbaijani economic dialogue” from an instrument of information war into an incentive for future peace might be placed at the core of EGF’s research priorities on NK. Key questions which need to be addressed in conceptualizing such a transformation of the Armenian-Azerbaijani economic dialogue are: What scope for a blueprint for regional development? What are the key priorities? What other topics could be included? What regional frameworks might enable joint planning, funding, and management of economic projects? What impact might the on-going European and Eurasian integration processes have? How to inter-connect the process of resettlement of the IDPs and refugees communities of both ethnicities with the economic integration processes? Are the prospects for regional development strong enough to change the current security concerns across the South Caucasus region?
- A public debate amongst NK stakeholders on the advantages and disadvantages of choosing peace and regional economic development over the current state of hostility might facilitate political compromise. Could such a public debate support efforts to broaden the constituency for peace around the NK conflict? Could a (roadmap) Strategic Plan for Regional Development trigger such a debate?
- From an EGF perspective, a Strategic Plan for Regional Development should:
  - Be a scenario building exercise rather than a political/legal document;
  - Build upon previous attempts (i.e. Stability Pact for the Caucasus, Caucasus Stability and Cooperation Platform, etc.) without duplicating them;
  - Be underpinned by the principles of the Brussels consensus on post-conflict regional integration scenarios for the South Caucasus;
  - Adjust to the dynamics of the regional context, focus on Armenia, Azerbaijan and Nagorno-Karabakh, while maintaining an inclusive approach against other regional actors;
  - Address the dichotomy of European and Eurasian integration processes;
  - Be consistent with the political and security aspects of conflict resolution scenarios;
  - Involve to the largest extent possible interested business circles;
  - Enshrine relevant political and diplomatic feedback.
- Both Armenia and Azerbaijan recognized the need to improve the mobility of their citizens in the EU, and agreed on visa facilitation rules. However, at present, Azerbaijan seems to be happy with the status quo in relations with the EU, while Armenia has to settle its agreements with the Eurasian Customs Union before it may figure out the way ahead on relations with the EU.

### ***Session II: Considerations of Business and Investment: Reintegrating Post-conflict Karabakh within the Regional South Caucasus Economic Framework***

EGF’s research has highlighted that business people in both Armenia and Azerbaijan do not consider cooperation with one another as a viable option at the present time. However, the need to involve the business community in the discussion on post-conflict regional economic scenarios was a recurring

message from the Brussels consultation round last March. Some voices from the region call for Karabakh to become the modern day Alsace-Lorraine of the South Caucasus, implied to mean a thriving zone of regional significance, where important historical cultures intersect and economies thrive. Others, in the same spirit, call on the region to become a “free economic space”, where abundant investment from Azerbaijan will one day be welcome. At the purely commercial level, such investment may eventually come in the form of joint projects between Armenians and Azerbaijanis, as well as international partners, replacing the many missed opportunities forced on the region as a result of conflict and tension.

The aim of this session was to examine the role that business could play in regional economic development in a post-conflict scenario in the NK context. A broad range of questions were posed to the speakers in this section: Would Armenian and Azerbaijani businesses be willing to invest in this region of the Caucasus? Could region-wide investment projects ‘sweep up’ NK as part of a future regional economic boom? Are we too fixated on security questions relating to Karabakh and missing immense opportunity by seemingly ignoring scope for economic cooperation? Could Armenians and Azerbaijanis, possibly from diaspora communities, as well as Turkish, Russian and other investors see incentives in the development of joint commercial projects in the region? Can we work together towards a blueprint for regional economic development, at least in the form of a strategic policy document for decision makers and foreign investors? What is the opinion of business leaders about the overall ‘prospects for NK’, were an appropriate political climate to emerge?

The most relevant **messages drawn** from the briefings and the ensuing discussion in this section included the following:

- A global approach for the European continent, from Lisbon to Vladivostok, has major economic and energy related advantages. However, European politics are currently disruptive, and partly responsible for maintaining the protracted conflicts in the South Caucasus.
- Armenia needs open borders to optimise the conditions for its economic development. If it achieved that, it may offer alternative transit routes to Caspian energy flows to Europe. Mutual trust is essential for conflict resolution, but it could be hardly gained while Armenia seemed more dependent than ever on other regional actors. One Armenian participant thought that a “Marshall Plan for the South Caucasus” could offer the international guarantees needed by private investors to consider involvement in supporting regional infrastructure projects. Such a Plan should be prepared before the Peace Agreement was signed, and should be included in its annexes. The same Armenian speaker proposed, as a central element of a post-conflict scenario, that a DCFTA should be signed with the EU by the three South Caucasus countries together. This proposal was echoed by a couple of Azerbaijani speakers. While it is doubtful that such a step might be implemented in any circumstances, for both political and practical reasons, it may also reflect an Armenian-Azerbaijani consensus on the need to strengthen regional economic cooperation in the South Caucasus in a post-conflict context.
- Azerbaijan could become a key source of Armenian economic growth if the NK conflict would be solved. Furthermore, it may become a net contributor to the development of the whole South Caucasus region, including Armenia. Currently, even if Azerbaijani private investors were ready to invest in Armenia, they could not, since the return on investment would not outweigh the costs and

overcome the security risks. Given the huge financial burden IDPs are posing on the Azerbaijani budget, in a post-conflict context, Baku seems prepared to invest large amounts in the reconstruction and rehabilitation of the seven Azerbaijani districts around NK, and it will be looking for strong partners to associate itself with.

- One Azerbaijani speaker expected the EU institutions to take a bolder role in NK conflict resolution as a consequence of European energy interests in Azerbaijan. In his view, nothing short of NK self-government within Azerbaijan would be an acceptable solution to the NK conflict for Baku. However, this bold political statement generated negative reactions from the Armenian side. This proved once again that only a step by step approach could lead to a dialogue-based solution to the NK conflict, while the reiteration of the current disagreement on the political status of NK may counter efforts at establishing a meaningful Armenian-Azerbaijani economic dialogue.
- The security of investments is very important in any economic post-conflict scenario. Regional business communities and international organizations active in the region should set up a dialogue on this particular issue. Ideally, a Marshall Plan for the South Caucasus would supply the needed investment for making economic incentives work in a post-conflict scenario. However, there are many business-related steps to be taken before the conflict is solved. For example: monitoring to what extent the market rules (taxing regimes and the practices for protecting investors) are favourable to investments; establishing informal business communities; setting up an international body tasked to assist business communities in both countries to resolve problems related to taxation; identifying which sectors might offer a comparative advantage; or collecting information and proposing recommendations regarding the improvement of the business climate.
- Post-conflict economic scenarios should also take into account:
  - The future presence of peace-keeping forces;
  - Turkish-Armenian relations, although few Armenians were prepared to accept that they belong to a package deal on NK conflict resolution;
  - The potential disruptive role of Russia, if Moscow would perceive its geopolitical interests in the region as being threatened;
  - The prospects of Eurasian integration in the South Caucasus and its possible points of contention with the European integration process.
- Although somewhat beyond the scope of EGF's current research on NK, an ensuing idea thrived in the discussion: setting up a dialogue between Armenian and Azerbaijani communities from NK seemed to be a mutual interest. An Azerbaijani speaker proposed to use the EGF platform for dialogue on economic incentives as a springboard for organizing a meeting between the two communities in NK. A possible subject might be the restoration of Azerbaijani cultural monuments in NK, with a view to issuing a common letter of support. Another possibility for dialogue among the two communities from NK could be the joint management of the Sarsang Water Reservoir. The Armenian interlocutors seemed to agree with these proposals, and added a new possible item on the agenda of a NK communities' dialogue: establishing joint businesses in the region. However, when it came to the status of NK it appeared that no concessions would be made by the Armenian side unless firm security guarantees were in place. Furthermore, in response to an Azerbaijani proposal in the first session to grant the status of special economic zone to NK, one Armenian speaker thought that only a step by

step approach may work. Therefore, initially, Azerbaijan could grant the status of special economic zone to the seven districts around NK.

### ***Session III: Post-conflict Scenario Building Workshop and Group Simulation***

The aim of this workshop was to simulate a negotiation process in order to reflect a possible real life situation which may occur in the NK context at a future date, and to draw lessons learned during a feedback session. The given (future post-conflict) scenario was set in the year 2019. A few months had passed after a peace agreement based on the (current) Madrid Principles was reached between the imaginary Republics of Salandia and Oronia, which were engaged in years of fighting over the political status of the 'break-away territory' of Mordovia<sup>1</sup>.

Participants in the simulation were issued with instructions about engaging each other prior to commencing the simulation. The task of participants was to simulate negotiations of a bi-national Task Force (which in 2019 was) mandated with drawing up a roadmap for implementation of the economic considerations of the (2019) Peace Agreement. Furthermore, the 'Task Force' was invited to propose additional economic projects that could act as confidence building measures by addressing the restoration of war-torn energy, transport and socio-economic infrastructure in NK and the territories around it, by establishing, where possible, 'economic projects of common interest'. The end goal was to agree upon an 'official' roadmap document which could be supported by both parties.

The simulation succeeded in finding a means of enabling participants to talk to each other in a most constructive manner in the framework of hypothetical bi-national Task Force mentioned above. The discussions were mediated and assisted by international experts. The dialogue among experts highlighted the inherent interdependence of the political, economic and security agendas of the two countries, Salandia and Oronia. It eventually resulted in drafting a realistic, mostly agreed-upon action plan for implementation of the economic aspects of a Peace Agreement based on the Madrid principles, and for restoring war-torn infrastructure. This action plan was set into a timetable outlining a possible post-conflict roadmap for peace building in Karabakh.

While EGF intends to elaborate in more detail upon the conclusions of the Berlin simulation exercise in a research paper in the near future, it already appears that the action plan may result in a solid basis for developing more robust post-conflict scenarios in the context of future simulations of this nature. End game: an economically integrated South Caucasus, underpinned by the very broad and uncontroversial principles of the Brussels Consensus.

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<sup>1</sup> The country profiles of Salandia and Oronia were identical to those of Azerbaijan and Armenia, respectively, while the status of Mordovia was mirroring that of Karabakh.