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Turkmenistan's Quest for Energy Market Stability: Navigating Export Route Diversification

*Ms. Akanksha Meena**

Abstract

Turkmenistan is one of the leading resource-abundant nations in the world. Despite the vast reserves, the country faces the market challenges of exporting gas and the difficulty of doing business in the republic. Turkmenistan was heavily dependent on Russia for selling its gas for a long time despite the long-lasting neutrality strategy. It depended on the Soviet pipeline network, which connected the country only to European Russia through the Central Asia-Center (CAC) pipeline. Today, Turkmenistan's government is focused on developing new export routes as an essential element in its energy strategy, which boosts its national energy budget with high energy revenues. 2009-10 proved to be a turning point in Turkmenistan's energy when Russia reduced its purchases from Turkmenistan due to oversupply caused by the recession. This marked the beginning of the diversification strategy of Turkmenistan's energy policy. This paper looks into Turkmenistan efforts to diversify its export routes. It attempts to explore the strategies employed by Turkmenistan to expand its energy market, reduce dependency on a single export route, and enhance market stability. The paper analyses the shifts in Turkmenistan's energy relations with both major players, such as Russia and China, and with regional players, like Turkey and Iran.

Keywords: *Natural gas, Geo politics, Energy security, China, Export diversification*

Introduction

Turkmenistan is an important player in the global energy system, bestowed with abundant natural resources strategically located in Eurasia. Turkmenistan is characterized by an energy-intensive economy with a sizeable hydrocarbon reserve, primarily natural gas. It has gained prominence in the global energy market. It is covered around 80 % with a flat desert with slight elevation along with the bordering areas of Afghanistan and Iran. Due to its enormous potential for natural gas deposits and petroleum, Turkmenistan is known as a 'gas republic'. The primary energy shares of gas accounts to 72.4% and 27.6% of oil. The energy sector, comprising gas and oil, is the key driver of Turkmenistan's economy, which amounted to 31 percent of the GDP. The government had to cut down on

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the subsidies, spending on the social sector and public infrastructure due to the loss of revenue from the hydrocarbon resources. According to the report of the Asian Development Bank (ADB), Turkmenistan's GDP growth witnessed a steep fall from 14.7 percent in 2011 to 10.3 percent in 2014 and 6.5 percent in 2015. However, in the case of Turkmenistan, due to the unavailability of specific data, an exact picture cannot be given (Stronski, 2017).

Since 1991, Turkmenistan has faced the issue of a limited level of foreign investment in its hydrocarbon sector. The huge amount of energy resources and the potential of high export value of Turkmenistan could not be translated to substantial state revenues from the hydrocarbon sector. The geopolitical rivalry in the region on the Caspian Sea's status, instability in Iran and Afghanistan, a poor track record in terms of the rule of law, and the absence of accurate data on oil and gas reserves exacerbate the unfavorable investment climate of the country. Access to global energy markets is also limited due to the country's geopolitical location, which also results in the isolation of Turkmenistan's energy market from the international market happenings (Dzardanova, 2010).

Turkmenistan adopted the old Soviet model of a 'national way of development' based on a state-led economy. The country's economy was based on the structures created during the Soviet era. The trade and transport networks were created in such a manner that isolated the countries connected with the outside world. It did not reorient its economy towards a market-oriented direction like Kyrgyzstan and Kazakhstan. For example, post-independence Kazakhstan initiated the transition towards a free and open market economy based on the Russian model of radical reforms implemented under Yeltsin. In the early 1990s, Kazakhstan launched the privatization program targeting most medium and small enterprises. Similarly, the Kyrgyz government introduced a new legislative framework to govern the liberalized economy of the newly independent country. On the other hand, economic liberalization was never a priority of the regime, and the country was the least developed in the region (Spechler, 2008).

President Gurbanguly Berdimuhamedov has initiated domestic reforms in the country's energy sector. The President initiated a series of structural reforms to boost the oil and gas industry. The resolution passed by the President was renamed (The Ministry of Oil and Gas Mineral Resources) in the Ministry of Oil and Gas of Turkmenistan. Despite these reform measures, the hydrocarbon sector of Turkmenistan faces the problem of low levels of foreign investment. The dominating presence of the energy sector in the energy sector has posed a significant challenge to the private sector's development. The segment of the private sector in the economy has largely been limited due to the strict administrative structure ("Commercial Laws of Turkmenistan", 2010).

The domestic dynamics impact the country's foreign and energy policies. President Gurbanguly Berdimuhamedov opened up some scope for foreign investors in this aspect. He has underlined the need for foreign investment in the energy industry of Turkmenistan. Turkmenistan became reliant on Russia's existing gas and export infrastructure to get its gas to the market when it gained independence. Russia continues to have a considerable presence in the energy landscape of Turkmenistan (Milov, 2011).

Under the leadership of President Gurbanguly Berdimuhamedov, Turkmenistan is strengthening its partnership with other countries to develop energy resources. The diversification of sources and gas supply routes has become a concern for Turkmenistan. The Turkmenistan government has been in pursuit of attracting international investment in its hydrocarbon market. In the present scenario of diversifying its export routes, Turkey offers a significant route for Turkmenistan to get its gas to the European market. Turkey's Foreign Minister Mevlut Cavusoglu noted:

Having perfect political relations is not enough. There is potential for cooperation between the two countries and the other countries in the region on other important issues such as energy, economic relations, transport, and logistics. We will work harder to actualize this potential cooperation (as cited in Shlykov, 2014).

Evolution of Turkmenistan's Energy Relations with Russia

Soon after independence, Turkmenistan faced the challenge of taking over control of the industrial sector that the Soviet Union left behind. The former Soviet Union's state-planned economies relied on a barter system in which one country bartered with another



Fig.1: Showing Central Asian Centre (CAC) pipeline spans from Kazakhstan, Uzbekistan, and Russia, transports Turkmen gas to the European side of the Soviet Union. Source: Stefan Hedlund, 'Turkmenistan Comes into Focus,' Geopolitical Intelligence Services, 25 March 2019.

based on Moscow-controlled demand and supply. Turkmenistan relied on the existing gas and export infrastructure to supply gas to the market while becoming self-sufficient to meet its energy needs. Thus, Turkmenistan depended on Russia's energy plans and infrastructure (Milov, 2011). Turkmenistan exported gas to Ukraine via the Central Asia Centre (CAC) pipeline on a shared income basis during the Soviet Union reign.

Turkmenistan was a significant gas provider to other republics through a system known as the 'Steel Umbilical Cord,' a network of pipelines that spanned the Soviet Union's entire territory. The CAC pipeline, which spanned Kazakhstan, Uzbekistan, and Russia, transported Turkmen gas to the European side of the Soviet Union (Anceschi, 2017). This system was practiced in the initial years of transition, but Ukrainian non payment became a cause of worry for Turkmenistan. Until 1994, Russia operated a nominal quota system and eventually ceased allowing Turkmen gas to flow through its territory. In September 1993 and November 1994, Ukrainian enterprises and organizations illegally diverted Russian natural gas shipments from transit pipes due to a dispute over non payment by Ukraine. As a result, Russia temporarily halted natural gas deliveries three times between 1992 and 1994, adversely impacting Turkmenistan's exports (Kanapiyanova, 2020).

Following the dissolution of the Soviet Union, Itera, an international organization of corporations, acted as an interim mediator for gas transit conflicts in the former Soviet republics. It became a source of natural gas from Turkmenistan to former Soviet Union nations. By the early 2000s, Gazprom, the Russian gas company, had replaced Itera with a new intermediary company bearing the same name. The Turkmen export to Ukraine has significantly benefited from this substitution. With the signing of a deal with Naftogaz, the Ukrainian gas company, and Eural Transgas as arbitrators, it quickly became a crucial player in the Russian gas business. Turkmenistan agreed to deliver 36 billion cubic meters of gas to Ukraine between 2003 and 2006, using the existing pipeline infrastructure (Garibov, 2019).

The East-West pipeline was proposed in 2007–2008 as an expansion route of the Central Asia Centre gas pipeline system to ensure the planned Caspian Coastal pipeline supply. Initially, it was planned to be built with the help of Russian gas giant Gazprom. However, tensions between Russia and Turkmenistan in 2009 prompted Turkmenistan to seek international bidding for the pipeline. The building process began in 2012 and ended in 2015. The East-West pipeline will increase the country's export capability by linking Turkmenistan's largest gas resources with the Caspian coast's pipeline network. The route is an essential first step toward Turkmenistan's westbound export plan. However, numerous political and financial issues must be solved before establishing a stable export route from Turkmenistan to the West (Konarzewska, 2016).

Gas pricing has traditionally been a source of contention between Turkmenistan and Russia. During the initial phase, the gas trade followed the existing pricing mechanism, and Turkmenistan could not renegotiate the fixed price. Although Russia raised the amount of gas it purchased from Turkmenistan, it had the advantage of establishing its own price compared to former Soviet Union republics. Russia adopted the strategy of purchasing Turkmen gas at a lower price and reselling it to Europe at a much higher price.

However, in 2004, things changed due to a boom in demand for oil and gas in Europe, which resulted in a sharp increase in gas prices. Turkmenistan took advantage of the changing market conditions to renegotiate gas rates with Russia.

Turkmen gas shipments to Russia, previously the primary market, drastically decreased in 2009. When demand in Europe and Russia fell, Gazprom reduced imports to 10–12 Bcm annually and sought Turkmengaz, Turkmenistan's national gas company, to alter the 2008 oil-linked price formula. Turkmengaz has traditionally been a secondary gas source for Russia, used to supplement the country's domestic supply. In 2010–14, exports were about 10–11 billion cubic meters yearly. Turkmengaz and Gazprom's relationship deteriorated in 2014 and 2015 due to a payment and supply volume disagreement. In June 2015, Gazprom filed a complaint with the Stockholm arbitration court. However, the case was placed on hold the following year 'to reach a mutually acceptable agreement on continued collaboration outside the scope of the arbitration' (Elliott, 2019).

The gas ties between Turkmenistan and Russia shifted again in 2015, when Russia reduced its purchases from Turkmenistan owing to a significant decline in oil prices. Meanwhile, Russian gas giant Gazprom filed a complaint against Turkmenistan in Sweden's arbitrary court over gas prices. Serious breaches of the bilateral agreement were placed on the Turkmen administration. In January 2016, it was announced that Gazprom's contract with Turkmengaz State Concern had been terminated (Fredholm, 2005). In 2019, Gazprom signed a five-year contract with Turkmengaz to acquire natural gas. Turkmenistan would provide Gazprom with up to 5.5 billion cubic meters (bcm) of natural gas per year, according to the firm. The agreed-upon figure is much less than Turkmenistan's supply to Russia in the decades before the halt when yearly exports to Russia might approach 50 billion cubic meters. Most Turkmen gas presently flows to China (approximately 40 bcm out of 70 bcm), and the Ashgabat administration is constructing a pipeline from Afghanistan to India via Pakistan (Konarzewska, 2016).

Joint Projects and Initiatives Between Iran and Turkmenistan

The opening of the Bafq-Bandar Abbas and Mashhad-Sarakhs–Tajan railroads in

1994 and 1996 marked a turning point in Turkmenistan-Iran connectivity and commercial possibilities. The Bafq–Bandar Abbas track connected Turkmenistan's railway system to Iran, while the Mashhad–Sarakhs–Tajan route linked it to Bandar Abbas, Iran's Persian Gulf port city. Iran has invested in many technological projects in Turkmenistan, in addition to several border markets. It is a \$1.5 billion investment in Turkmenistan that was made in 2008. The Kazakhstan–Turkmenistan–Iran project (KTI) pipeline was also proposed. This 1,500-kilometer pipeline, with a daily capacity of one million barrels, would transport Kazakh and Turkmen oil to worldwide markets through Kharg Island in the Persian Gulf. Even though the pipeline's construction circumstances were favorable, the project was hampered by the United States' continuous resistance (Atai & Azizi, 2012).



Fig.2: Shows the Trans-Caspian Gas Pipeline is proposed subsea pipeline between Türkmenbaşy, and Baku in Azerbaijan. Source: Caspian Policy Center, 'Kazakhstan and Azerbaijan plan an undersea trans-Caspian oil pipeline', 2016.

The National Iranian Gas Company (NIGC) and Turkmenistan signed a 25-year Korpje–Kurt Kuy gas export agreement for Turkmen gas to Iran in 1995. Western Turkmenistan's gas deposits are connected to northern Iran through a 200-kilometer pipeline. The pipeline cost \$190 million to construct. The pipeline, which opened in 1997 and has a capacity of 8 billion cubic meters per year, is significantly less than the planned Turkmenistan–Iran–Turkey pipeline. Building a gas pipeline with Iran was

Turkmenistan's first successful attempt at export diversification in 1997. Its objective was to reduce dependency on Russia by not passing through any other countries (Chufrin, 1999).

Due to the government's stringent restrictions, major international corporations avoided investing in the country, especially in the oil industry. In early 2002, firms such as ExxonMobil and Shell lost interest in Turkmenistan's oil prospects. Despite this, Iran has only made a few investments in Turkmenistan. One such project was the installation at a Turkmenbashi refinery's gasoline-producing unit, which cost \$47 million. An energy swap deal exists between Turkmenistan and Iran. Iran fulfills its northern areas' energy requirements from neighboring nations (Turkmenistan, Kazakhstan, and Azerbaijan) and distributes an equivalent amount of energy in the Persian Gulf on their behalf (Bayulgen, 2005). This Turkmenistan-Iran pipeline is of strategic and political significance for Turkmenistan. It surmounted both the US and Russia's challenges. The two countries' collaboration has continued. On January 6th, 2010, the Turkmenistan–Iran gas pipeline was completed. It was a 1,024-kilometer pipeline that connected the two countries' gas networks. It delivered gas to Iran's northeastern areas, had the option of gas swapping, and could trade in natural gas with East Asia and Europe. Turkmenistan's energy industry has reformed since President Gurbanguly Berdymu-khamedov took office in December 2006. The private sector's involvement in the economy has grown, while subsidies have decreased.

Both countries have the potential to cooperate in the energy sector. They have successfully cooperated in oil swaps and pipeline networks. At the same time, they face the problem of the adverse investment climate in Turkmenistan along with the Iran–U.S. confrontation. The geopolitical rivalry in the region also shapes Turkmenistan and Iran's energy relations. Turkmenistan and Iran disagreed about natural gas payments. Turkmenistan accused Iran of defaulting on payments due in exchange for Turkmenistan's natural gas. As a result, Turkmenistan chose to relocate to Iran. Both nations have agreed to take the case to an arbitration court to settle the dispute. The gas conflict between Turkmenistan and Iran is more than a bilateral issue between two neighbors; it has far-reaching implications for future global energy commerce. Both countries must agree on a solution. Turkmenistan wants to diversify its gas exports to other parts of the globe, and Iran has shown to be an excellent export partner (Nova, 2018).

Energy Cooperation Between Turkmenistan and Turkey

Turkmenistan's government has been striving to make its oil and gas markets more appealing to foreign investors. Turkmenistan and Turkey have been working hard to expand their commercial, economic, and political ties. The amount of bilateral commerce

is increasing at a rate of 30-40 percent every year. Turkmenistan-Turkey energy cooperation will bolster Turkmenistan's resource-based economy while also providing lucrative new contracts for Turkish construction firms. The agreements between Turkmen company 'Türkmengaz' and Turkish company 'Atagaz Dogalgaz A.S.,' which were inked during Erdogan's visit to Ashgabat, point to Turkmenistan and Turkey strengthening their relations (Shlykov, 2014). A trilateral framework on energy cooperation between Azerbaijan, Turkey, and Turkmenistan was established in early 2015 to highlight energy cooperation with Turkey. It planned to expand the Southern Gas Corridor and build the Trans-Caspian gas pipeline, bypassing Russia and supplying Turkmen natural gas to Turkey via Azerbaijan and Georgia. It extends for around 300 kilometers and can carry up to 30 billion cubic meters (bcm) of Turkmen gas per year to the Southern Gas Corridor. South Caucasus Gas Pipeline (SCPX), Trans Adriatic Pipeline (TAP), and Trans Anatolian Pipeline (TANAP) are the three pipelines that make up the project (Morrison, 2017).



Fig.3: Shows the TANAP pipeline forms the central part of the Southern Gas Corridor (SGC) and is 1,841 meters long, passing through 20 Turkish provinces. Source: Aksam Gazetesi, Design & Translation: Necdet Pamir

The Trans-Caspian Gas Pipeline (TCP) would give significant potential for the Caspian to sell natural gas to European markets, expanding its export destinations. It would be fed by the existing inland East-West Gas Pipeline, which connects the Galkynysh Gas to Turkmenistan's Caspian Shore. The creation of new export markets for Turkmenistan's natural gas would enhance the country's natural gas output and provide another element for economic development. Russia is opposed to the pipeline. However, Turkmen President Gurbanguly Berdimuhamedov maintains that constructing a pipeline is a sovereign prerogative of the state whose territory the pipeline will pass through.

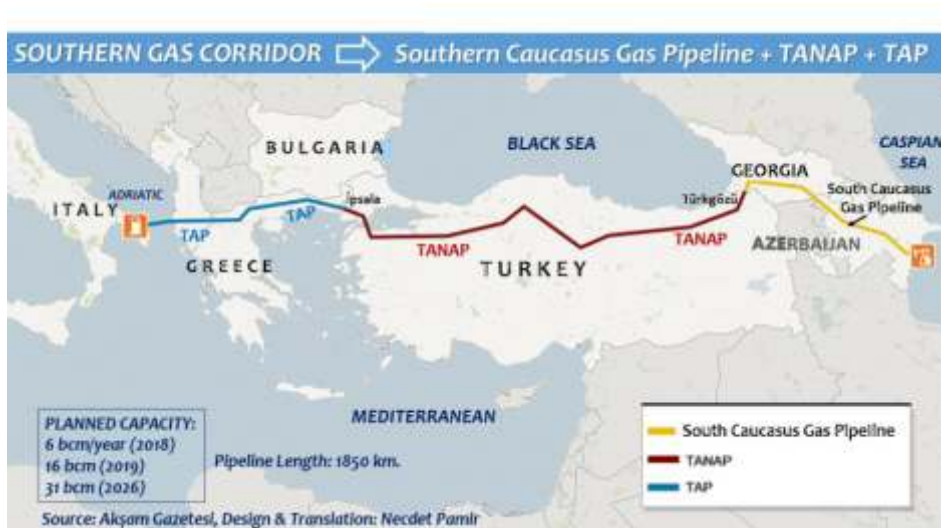


Fig.4: Shows that the Central Asia– Center gas pipeline system is a Gazprom controlled system of natural gas pipelines, which run from Turkmenistan via Uzbekistan and Kazakhstan to Russia. Source: Stefan Hedlund, 'Turkmenistan Comes into Focus', *Geopolitical Intelligence Services*, 25 March 2019.

Russia and Iran oppose the Trans-Caspian pipeline, claiming that it cannot be considered until the geographical split of national sectors in the southern Caspian is resolved. The European Union has been working to get Turkmen gas to European markets and concentrating on accelerating TCP usage. On the other hand, the fall in natural gas prices may prove to be an impediment in making costly infrastructure investments like TCP unprofitable in the short run. TCP also has to deal with an unresolved Caspian Basin issue (Konarzewska, 2016).

Another project connecting Turkmenistan and Turkey is the Trans-Anatolian Natural Gas Pipeline (TANAP), which intends to replace Russian gas in the European market with natural gas from Azerbaijan and Turkmenistan. This initiative has received assistance from Georgia, Ukraine, the EU, and the US. The TANAP may transport Turkmenistan's resources to Southern and Eastern Europe.

While the construction of an export route between the two countries is still ongoing, Turkey and Turkmenistan signed a memorandum of understanding in 2014 under which Turkmenistan agreed to sell gas to Turkey in order to supply gas to the TANAP project and lessen European reliance on Russian gas supplies. With its vast and readily exploited gas reserves, Turkmenistan might supply global markets by establishing a transit link with Turkey. This would promote Turkmenistan's economic growth by extending and increasing Turkmenistan's involvement in a corridor connecting its gas resources in Turkey to Europe, benefiting all parties involved (Mostajabi, 2017).

Turkmenistan's Energy Relations with China

China has emerged as a crucial ally in Turkmenistan's diversification policy, which aims to lessen the country's reliance on Russia. The General Agreement on Gas Cooperation between China and Turkmenistan in 2006 solidified their commercial relations in the post-Niyazov period. This gas transaction led to the development of the Central Asia-China pipeline and paved the way for China National Petroleum Company (CNPC), China's main national oil and gas corporation, to develop reserves in eastern Turkmenistan. The completion of the Central Asia-China Gas Pipeline in 2009 enabled Turkmenistan to break Russia's monopoly on Turkmen exports (Durdiyeva, 2010). The President of Turkmenistan, Gurbanguly, hailed the construction of the gas export as the 'pipeline of the century'. The new pipeline was a respite during the critical times when the country suffered the loss from a gas export restriction after the April 2009 explosion in the Central Asia-Center-4 pipeline carrying gas from Turkmenistan to Russia, which led to a nine-month dispute over gas prices between Ashgabat and Moscow (Vakulenko, 2023).

China's decision to obtain gas from Turkmenistan was based on its industrial strategy, which included providing Turkmenistan with a large-scale credit program. In its pursuit of boosting the gas market, China has made upstream investments and built pipelines with the help of CNPC and state banks. The National Development and Reform Commission (NDRC) has adopted a reform plan that is the first significant step toward shifting away from the conventional regulated cost-plus pricing system to an oil-linked netback pricing system, which has been tested since November 2011. The key objective of NDRC is to replace a large number of regulated pricing systems in each province with a single city-gate price and 'liberalize well-head prices and allow the market to decide the prices' (Cheon & Urpelainen, 2014).

While Turkmenistan is China's largest gas supplier, supplying more than 40% of its total gas imports, Beijing has continuously diversified its export networks. Turkmenistan owes China billions of dollars in loans to construct gas pipes to transport gas from Turkmen's fields to China. Due to its debt trap, Ashgabat cannot fulfil China's demand to supply more gas through the pipelines (Putz, 2016). Turkmenistan has become more exposed to Chinese price pressures due to China's 2014 agreement with Russia, which has significantly influenced the country's economy. China's insistence on paying substantially below European prices for Turkmen goods, with the possibility of even lower prices in the future, has signaled the rising reliance of Turkmenistan on China (Dadwal, 2017).

Other Projects in Turkmenistan

Turkmenistan's export policy toward the European Union is geared at attempting to overcome legal and political barriers to the establishment of a TCP, as well as the



Fig.5: Shows that the TAPI pipeline that originates from Turkmenistan will transport natural gas from Galkynysh Gas Field passing through Afghanistan and Pakistan will reach India. Source: Oil and Gas Journal, 'TAPI pipeline progresses, but future uncertain', 2016

European Union's proposal in 2009 to establish the Caspian Development Corporation, which was envisaged as a single commercial vehicle capable of aggregating Turkmen gas purchases. Turkmenistan and the European Commission signed a legally binding contract in 2011 ("The EU energy policy", 2011). Turkmenistan's insistence on selling gas outside its borders and market uncertainty caused by the recession can be blamed for the failure of the Turkmen-European route. The Commission believed that single-buyer models were required to negotiate with Turkmenistan, even though they violated EU competition regulations. The necessity for a coordinated strategy to Turkmenistan and EU competition rules contrasts significantly with Turkmenistan's approach to China, where CNPC, China's state-owned business, financed a significant share of the Turkmen upstream investments required to finish the project.

The launch of the 33 billion cubic meters (bcm) TAPI (Turkmenistan-Afghanistan-Pakistan-India) pipeline in South Asian markets has been delayed due to the involvement of other nations' national segment construction (only Turkmenistan finished its own), and the difficulty in securing financing, demands have been postponed numerous times—Afghanistan's government declared in February 2018 that TAPI will begin gas supplies in 2022. TAPI pipeline faces delays in construction and security issues affecting its realization (Pannier, 2010). During 2011, diplomats continued to discuss the pipeline, but no definitive decisions were taken. According to sources, Pakistan was seeking 14 billion cubic meters of gas per year in Multan at 70% of Brent oil per unit of energy. In late

2011, oil prices of approximately \$100 per barrel would indicate a gas price of roughly \$11/mmbtu. Other reports estimated a landing price of \$13/mmbtu in India, including transportation, based on oil prices of around \$100 per barrel, or almost three times what ONGC, India's state-owned oil and gas company, pays for gas produced locally (“Investment climate statement”, 2012).

Conclusion

Since its independence, Turkmenistan's export policy has been consistent with its ‘multi-vector’ foreign policy. Though it has made no political or strategic distinctions between potential buyers, it has procedures to sell gas solely on its border, with the buyer bearing all transportation and other hazards from there. Turkmen energy exports remain the backbone of the country's economy. However, unlike other emerging countries with abundant energy resources, the money generated by this industry has not resulted in a significant increase in the country's population's standard of life. The country's small population (5.1 million) and weak government have made it vulnerable to great power politics. Other Caspian oil producers, such as Kazakhstan and Azerbaijan, benefit from more robust export alternatives or a more open economy, giving them the power to overcome the oil price drop, at least partially. Despite having vast hydrocarbon reserves, Turkmenistan lacks all of these. Turkmenistan's predicament is challenging because it relies only on China for oil money. As a result, new gas export alternatives are required, as well as the allocation of a substantial portion of its declining earnings to finance infrastructure projects to strengthen the country's economy. In such conditions Gazprom's gas purchases in Turkmenistan provide Ashgabat with much-needed foreign money and the opportunity to further collaborate with Russia on new projects that might help Turkmenistan diversify its export portfolio. It also opens up many possibilities for counteracting the country's chronic over-dependence on China. Turkmenistan seeks to diversify its energy relations in this environment of great power politics in the energy sector. Geopolitical and security concerns complicate Turkmenistan's efforts to adopt a diversification plan of export channels. In the current scenario, creating new export channels has become one of the top objectives in Turkmen's energy policy.

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