

INTERNATIONAL ALERT

ECONOMY AND CONFLICT RESEARCH GROUP  
OF THE SOUTH CAUCASUS

# FROM WAR ECONOMIES TO PEACE ECONOMIES IN THE SOUTH CAUCASUS



EXECUTIVE SUMMARY

# INTRODUCTION

---

## Context

It has been more than a decade since the collapse of the Soviet Union and the transition process that it triggered in the South Caucasus. Its population has experienced war for nearly half this time. Poverty is widespread, and the rise of patronage politics continues. The region is struggling to attract foreign investment and, despite hopes for continued investment in oil and gas extraction, remains isolated from the global economy.

However, there are signs of change. The new Georgian government has pledged to combat corruption. If managed well and considered in the context of the overall political economy of the region, oil in Azerbaijan could be used as a resource to support development. The half-constructed Baku-Tbilisi-Ceyhan (BTC) oil pipeline could be a lever for building confidence throughout the region. Ongoing talks between Armenia and Turkey over the opening of the border between Kars and Gyumri suggest both a step towards improved relations between the two countries and the possibility of a more integrated economic system in the South Caucasus region that cuts across traditional geopolitical faultlines.

## The Economy and Conflict Research Group project

New political forces and international dynamics mean that prospects for peace in the South Caucasus remain unpredictable. However, it is clear that there cannot be a sustainable peace without economic opportunity for its people. *From War Economies to Peace Economies in the South Caucasus* is the product of a 18 month period of research and analysis that aimed to explore how a better understanding of the region's current economic dynamics might contribute to the resolution of its conflicts. It is the first book to examine this topic from the perspectives of those living in the region - the authors are members of the Economy and Conflict Research Group; a pool of experts from throughout the South Caucasus, covering Armenia, Azerbaijan, Georgia, Turkey and including Abkhazia, Nagorno-Karabakh and South Ossetia.

The research project, facilitated by the conflict transformation NGO International Alert, aimed both to examine the nature of economies in the region with a view to exploring economy-related peacebuilding opportunities and to promote dialogue and cooperation between the researchers themselves. Working relationships between ECRG members fostered by the project were an important component as they all hail from different sides of the conflict divides and have different perspectives on the issues.

# CONTENTS

---

Research topics were chosen by the group and fit into three categories:

## 1. Regional perspectives

- Cross-border cooperation between Turkey and South Caucasus: prospects for sub-regional integration
- The role of economic cooperation in the settlement of conflicts in the South Caucasus: an Armenian perspective

## 2. International business development

- The role of international organisations in the development of small businesses and the peaceful settlement of the Nagorno-Karabakh conflict
- Georgia: conflict regions and economies
- Economic development prospects in Abkhazia and the concept of regional cooperation

## 3. The informal economy

- Economy and conflict in South Ossetia
- The potential impact of Sadakhly market on the settlement of the Armenian-Azerbaijani conflict

Specific approaches to the research varied according to topic but were also framed via a number of questions relating to the broader issue of war economies:

- To what extent is conflict determined by inequalities in wealth distribution?
- Who determines how economic benefits are distributed?
- Does trade reduce or fuel conflict?
- Which economic sectors are most vulnerable to conflict? Which are most resistant?
- What role does the private sector play in conflict?
- If economic issues are to be brought further up the conflict transformation agenda, what alliances will be required?

The resulting essays were edited through a consultative process between the members of the ECRG. The project did not set out to achieve consensus between the individual researchers on the links between economics and conflict and what those links imply about possible solutions – the situation is too complex for such an ambition. However, there are a number of common threads around the current regional economic climate, challenges that need to be addressed and recommendations for future action.

# THE REGIONAL ECONOMIC SITUATION

---

- The physical, cultural and economic blockades brought about by conflicts in the South Caucasus have led to a particular pattern of trading in the region, sustained by entrepreneurial energy plus the need to trade in order to survive and to exploit the limited opportunities that remain.
- People need to trade – and will do so, no matter what the political situation. Unregulated, informal economic relations are important coping mechanisms for those caught up in conflict zones.

However:

- As in other ‘war/shadow economies’, individuals or groups seek to control the situation. Unregulated trading patterns provide space for those seeking to exploit the context to make huge profits – and an unregulated economic system tends to generate revenue for the pockets of the few. If those few also hold political power, then, as the research shows, ‘the deeper the (unregulated) economic and business relations between the conflicting sides, the less interest there is in a political solution to the conflicts’ – one of the main obstacles to peace in the region.
- Despite the strong entrepreneurial dynamism in the region, the fact that political control is held by so few creates a sense of being blockaded, denied opportunity and of psychological and economic suffering caused by the conflict. Efforts towards sustainable peace in the region will need to counter this sense of isolation and suspicion.

The combination of economic stagnation, entrepreneurial coping mechanisms, competition and control represents both a challenge and an opportunity for conflict transformation in the region.

## CHALLENGES

---

These are some of the specific challenges drawn from the common findings of the individual research papers.

**1) How can legal frameworks be established for trade while the political status of non-recognised entities remains unresolved?** Although the Georgian researchers conclude that strengthening unregulated economic links between Georgia and South Ossetia merely serves to sustain those who benefit from the frozen context and thereby prevents the resolution of the conflict, the South Ossetian researchers point out that Ergneti market is the main source of revenue for their economy and should therefore be strengthened. Without Ergneti market, they argue, South Ossetia would suffer financially and conflict would be more likely to reignite. But the dilemma persists of how Ergneti market can be legitimised while South Ossetia’s legitimacy as a recognised entity is still contested.

**2) How can the ‘internal’ development needs of the people in non-recognised entities be addressed without alienating those in recognised states?** The Nagorno-Karabakh researchers propose that, in the current context, international aid should be redirected from large infrastructure projects towards the development of small and medium enterprises, because large businesses will always have political constraints (as they have to be backed by political power), thus hindering their motivation towards addressing the conflict status quo. Their research suggests that those with secure jobs have attitudes more aligned to peaceful approaches to conflict resolution, as opposed to those still supported by humanitarian aid. However, business development in Nagorno-Karabakh may have an opposite effect on the attitudes of Azerbaijanis towards a resolution of the conflict since they view their own economic problems as inextricably linked with the loss of the region. The research on Abkhazia explores the potential for restoring agricultural production in the east of the region. However, it is unclear what Georgia’s reaction would be to assistance and development, which raises the question of how economic development in non-recognised entities can be fostered without antagonising the ‘other side.’

**3) How can an economic dynamic based on competition and cooperation be compatible with a political dynamic based on confrontation and domination?** This dilemma is illustrated by the dual political (or security) and economic roles that Turkey plays in relation to Armenia and Azerbaijan. Turkey has, in some ways, sacrificed its economic role for a political and security role by supporting Azerbaijan over the Nagorno-Karabakh dispute. The sealed Turkish/Armenian border contributes to the fragmentation of the region and has increased security concerns: its opening has the potential to foster economic integration in the South Caucasus and facilitate a restart to the deadlocked peace process. Recent lobbying for the border to be opened by the Turkish-Armenian Business Development Council (TABDC) may well prove that the solution to this blockage lies with the private sector.

**4) How can the needs of small-scale traders be brought to the attention of those in positions to influence the political context within which they operate?** This issue touches on arguments for more democratic political processes that can create the space for different needs to be heard and for the legitimisation of the informal economy. This dilemma is most clearly illustrated in the research from Azerbaijan. People from conflicting sides come together to trade at Sadakhly market. It may be the case that the market's unique socio-psychological atmosphere and the demonstrable pragmatism of its participants is worthy of serving as a model of possible coexistence and deserving of further study. However, there remains the issue of how to connect such pragmatic people with those seeking a political solution to the conflict: space needs to be found to bring their influence to bear on those engaged in track one and track two negotiations.

**5) How is it possible to engage the gatekeepers of the current economic system as stakeholders in future alternatives?** In an unregulated economic system it is difficult both to identify exactly who holds economic power and to find openings for dialogue with them. There is an additional dilemma of legitimising such actors through the process of engagement. However, if, as the research suggests, trade links across the conflict divides already exist, then there are opportunities on which to build. Business people can be at the forefront of such efforts, given their interest in stability and open markets.

## CONCLUSIONS AND RECOMMENDATIONS

---

The project's main conclusion was that if there is to be a successful process of long-term peacebuilding in the region, further discussion, dialogue and analysis is needed - both around the links between the economy and conflict identified during this research and the potential for economics and business to play a positive role for peace. Bearing in the mind the challenges noted above, there are a number of further conclusions that can be drawn:

- Although international perspectives on the region tend to be dominated by a focus on oil exploitation, a broader exploration of the dynamics between economic factors and conflict in the South Caucasus would be beneficial to conflict transformation efforts.
- The ideas generated by the research process need to be translated into practical projects. ECRG researchers are well placed to play a continuing role in this – making connections between their own constituencies, in particular within the business community.
- Support from the private sector (both local and foreign) is required in order to translate the ideas in this book into action. Foreign investors can contribute to economic development, job creation and transfer of business standards – but need to be sensitive to the interaction between their investments and the dynamics of local conflicts.
- Efforts can and should be made to develop geopolitical alliances that cut across the north/south and east/west axes that dominate confrontational politics.
- The donor community should develop economic strategies that contribute more directly to conflict transformation through projects that help to integrate the region economically and protect livelihoods.
- Development interventions need to be aware of the existing linkages between legal and shadow economies – and balance recognition of territorial integrity with the development needs of the non-recognised entities. At the same time, they need to take pre-existing structures such as informal markets into account and try to incorporate them into development efforts where they provide vital economic support to local populations. Otherwise the creation or consolidation of 'formal' structures like transport and infrastructure links may unwittingly undermine less visible survival economies.
- Economic opportunity for the region's people requires a sustainable strategy for economic development that involves a thriving business sector operating within a legal framework that meets international norms and results from democratic decision-making.

## FOR MORE INFORMATION

---

For more information about the ECRG, International Alert, and their future work in the South Caucasus region, or to obtain a copy of *From War Economies to Peace Economies in the South Caucasus* (English or Russian version) please contact Diana Klein [dklein@international-alert.org](mailto:dklein@international-alert.org) or + 44 (0)20 7627 6859.

International Alert is an international NGO that works to build sustainable peace in countries and communities affected or threatened by violent conflict. This project is part of a wider programme of work by International Alert aimed at promoting a positive link between business and peacebuilding. For more information see [www.international-alert.org/policy/business.htm](http://www.international-alert.org/policy/business.htm)

The Economy and Conflict Research Group of the South Caucasus is a group of researchers from Tbilisi, Sukhum/i, Tskhinval/i, Yerevan, Stepanakert/Khankendi, Baku and Istanbul that seeks to explore economy-related peacebuilding opportunities in the region.