



RSC MONTHLY CLOSED BRIEFING

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The Regional Studies Center (RSC) held the latest in our monthly series of closed briefings on Wednesday, 20 January, featuring a comprehensive analysis consisting of three main areas:

- (1) assessing recent political developments in Armenia, related to the implications of the December passage of the constitutional referendum, and a review of the negative economic impact on Armenia from the Russian crisis;
- (2) an overview of regional developments, including the recent Russian military buildup in Armenia, the deepening economic crisis in Azerbaijan, and the outlook for Armenia-Turkey “normalization,” especially given the recent Turkish-Russian crisis;
- (3) an assessment of the broader military situation, in light of the recent escalation of clashes over Nagorno-Karabakh and with an added focus on the outlook for the diplomatic mediation of the Karabakh conflict following the December meeting of the Armenian and Azerbaijani presidents in Switzerland.

In accordance with our standard format, this briefing also featured an informal “off-the-record” closed discussion.

As an independent “think tank,” the Regional Studies Center (RSC) offers this series of briefings in order to serve as more of a resource for the representatives of the diplomatic community and international organizations in Armenia. More specifically, our aim is to provide an alternative source of objective analysis and information on a regular basis.



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SUMMARY NOTES

I. Political & Economic Developments

Aftermath of passage of constitutional referendum

In the wake of the December passage of the Armenian constitutional referendum, there are five key developments, comprised of three serious concerns and two notable observations:

1. Serious concern over the authorities' half-hearted follow-up on the litany of voting irregularities and violations, with insufficient investigation and inadequate prosecution;
2. Concern over the government's questionable commitment to the electoral reforms now necessitated by the transformation to a parliamentary form of government;
3. Serious concerns from the authorities' over-reaction and crackdown on even the most radical fringe opposition groups and more marginal cases of discontent;
4. The stark reality of the even more discredited, less popular and largely isolated traditional opposition parties, emptying the political playing field for the emergence of new political parties like the "Civil Contract" and "Bright Armenia" parties;
5. The opening of talks to broker a new political coalition, driven by the authorities' ability to co-opt and entice the nominal opposition Armenian Revolutionary Federation (ARF or "Dashnak" party), and the government's plan for a minor cabinet reshuffle, with the ministers of culture and economy most likely to be replaced.

Positive trends

From a broader perspective, there are three positive trends now underway, offering a degree of opportunity for Armenia and with wider implications for the South Caucasus region:

1. **Armenia-EU relations.** In a rare second chance, Armenia is now able to restore relations, regain confidence and rebuild trust with the European Union (EU). After formal negotiations over a new "legal framework" opened on 7 December 2015, the Armenian foreign minister led a delegation to the January 18 meeting of the Cooperation Council in Brussels to further deepen Armenia-EU relations. And for its part, the EU is providing a new 30 million Euro aid and assistance package, with an emphasis on jobs and public finance policy, as well as support for civil society, through the European Neighbourhood Instrument (ENI);

2. ***Re-Engaging Iran.*** Despite a likely challenge from Russia in some areas (energy and transport, most notably), as the only stable neighbor of Iran, Armenia is uniquely positioned to expand relations with Iran in the wake of the recent easing of sanctions. Yet the Armenian government seems neither prepared nor positioned to take full advantage of this opportunity, and must move quickly to formulate a strategy for engagement;
3. ***Armenia-Russia: A More Assertive Armenia.*** In an uncharacteristically strong defense of Armenian interests at the 21 December Moscow CSTO summit, the Armenian president forcefully criticized Russian indifference and timidity regarding the recent escalation of Azerbaijani military attacks against Nagorno-Karabakh and Armenia proper. This is matched by a broader shift in Armenian policy that more directly challenges the unequal and asymmetric terms of the Armenian-Russian security alliance, reflecting a more assertive and self-confident Armenia.

Economic fallout from Russian crisis

The Armenian economy continued to suffer from the negative economic fallout from the Russian crisis, including a serious decline in remittances, exacerbated by the decline in the value of the ruble, and the loss of jobs for many Armenian migrant and seasonal laborers working in the Russian construction sector.

Armenian economy: meager growth & lack of sustainability

Bolstered by the combination of a surprisingly strong performance in the agricultural sector and a significant investment in the country's mining sector in 2015, the Armenian economy was largely able to weather the larger economic downturn and maintain a degree of positive, yet limited growth. But there are three serious concerns over the medium- to long-term, including:

1. A lack of sustainability for future growth stemming from the fragility of the agricultural sector (which accounts for roughly 20 percent of GDP) due to limited credit for farmers, their mounting level of debt, and the inherent vulnerability of agriculture production to unpredictable seasonal weather conditions, as well as the stagnant state of the construction sector, which was a previous driver of GDP growth. Moreover, the growth of the agricultural sector was also due to a one-time advantage for Armenian farmers from the Russian ban on products from the EU and Turkey;
2. The dependence on the mining sector for growth is limited by increasing volatility in global commodity prices, as well as by costly environmental damage from mining operations, and the finite amount of minerals, ore and precious metals;
3. Even more challenging structural deficiencies that include a lack of competition, rooted in the inordinate market share of imports and exports of key raw materials by so-called "oligarchs," or commodity-based cartels, and serious shortfalls and inefficient tax and revenue collection, as well as shortcomings in economic reform.

II. Regional Analysis

Russian military buildup in Armenia

On 9 December, Russia moved to bolster its forces in the South Caucasus by deploying more combat and transport helicopters to Armenia. The deployment consisted of seven modernized Mi-24 attack and Mi-8 transport helicopters, stationed at a military airfield outside of the Armenian capital Yerevan. That Erebuni airfield, along with the 102nd Russian military base in the city of Gyumri, constitutes the sole Russian military presence in the region. In addition to hosting a full Russian helicopter squadron, there are also more than a dozen Russian MiG-29 fighter jets and Armenian military aircraft stationed at the airfield, many of which were fully modernized last year.

The move was the first in a series of steps aimed at bolstering Russian forces in Armenia and was followed by a second deployment of additional rotary wing aircraft last month. Similarly, the Russian base in Gyumri, home to some 5000 military personnel has also undergone a sweeping upgrade of infrastructure and installations. Taken together, the strengthening and expansion of Russian military forces in Armenia is also seen as a response to the November shutdown of a Russian military warplane by Turkey, and as a response to an incursion of Armenian airspace by Turkish army helicopters on two separate occasions in early October. More recently, after that significant upgrade and expansion of Russian air power in Armenia, a new delivery of Russian-made “Takhion” unmanned aerial vehicles (UAVs or “drones”) has further bolstered Russian surveillance capabilities in Armenia.

Azerbaijani economic crisis & unrest

Both the severity and significance of the economic crisis in Azerbaijan continues to deepen. Since the 21 December decision to “float” the manat, the value of the Azerbaijani currency, the manat, has fallen by roughly 50 percent compared to the dollar. That sudden depreciation has also prompted the Azerbaijani authorities to spend some \$640 in repeated currency market interventions aimed at bolstering the manat, spending almost half of its hard currency reserves.

Overall, the Azerbaijani government has been rather slow to respond, and when it has acted, has opted for questionable measures, including the imposition of currency controls, the forcible closure of currency exchanges, and the enforcement of a new 20 percent tax on “currency exports,” targeting outward investment and purchases, with suggestions of further controls targeting capital flight. Subsequent moves included a temporary freeze on enforcing some taxes, the imposition of pay cuts for some military officers, as well as a sudden halt to planned defense spending, and moves to limit price rises for bread and flour.

The responses to date, however, have done little to address the underlying problems of widening inequality, as seen by mounting disparities in wealth and income, entrenched corruption and high unemployment, sharp urban-rural divisions between the capital and the regions, and the structural lack of diversification of the energy-dependent economy.

Moreover, Azerbaijan has been especially hard hit by the decline in oil prices, as the economy relies on oil and gas for 90 percent of exports and 70 percent of total revenue. The crisis has also triggered an unprecedented wave of unrest, with demonstrations and protests spanning some eight regions across the country.

The outlook for Armenia-Turkey

In light of both the pressing security challenges from escalating violence in eastern Turkey and terror-related threats emanating from the war in Syria, as well as the crisis in Turkish-Russian relations, the short-term outlook for any possible Turkey-Armenia “normalization” appears bleak at this point.

Moreover, in response to the recent expansion of Russian airpower in Armenia, Turkey may perceive this latest move to strengthen Russian surveillance on the Armenian side of the closed border as a provocative and possibly aggressive move. From a military perspective, such a view is also related to the wider context of Russian power projection on several fronts, ranging from the Black Sea to the Syrian theater. Turkish military planners may, therefore, reinforce their own forces along the closed border with Armenia. Such a move by Turkey may be logical, reflecting a more assertive force posture also related to the escalation of military operations against the Kurdish PKK insurgency in eastern Turkey. At the same time, however, the Turkish military will likely be more cautious in refraining from any direct confrontation, avoiding any repeat of its October 2015 incursions into Armenian airspace.

III. Military Security

Nagorno-Karabakh military escalation

As reported in our December 2015 report: “RSC Nagorno-Karabakh Situational Assessment,”¹ the recent escalation, in which at least half of dozen deaths were reported from all sides, a military UAV was shot down and a tank unit was used for the first time since the signing of the 1994 ceasefire, raises serious concerns.



¹ “RSC Nagorno-Karabakh Situational Assessment,” Regional Studies Center (RSC), Yerevan, Armenia, 14 December 2015. www.regional-studies.org/en/publications/analytical/467-141215

Moreover, there are several factors underlying the significance of this latest escalation. Beyond the notable deployment of an armored unit, for example, this recent escalation follows a similar upward trend last year, as clashes claimed some 72 lives in 2014, representing the highest level of deaths over the past twenty years. And more specifically, this escalation is dangerously defined by four underlying components:

- ***greater operational intensity***, whereby recent ceasefire violations have included the use of mortars and grenade launchers, well beyond more routine sniper fire, and evident in the November 2014 downing of a Karabakh Mi-24 army helicopter, as well as the ***first use of armor*** since the May 1994 ceasefire;
- ***increased operational tempo***, with much more frequent attacks that also include more advanced reconnaissance missions and probes of defensive positions involving better trained Azerbaijani units brought in from Baku and endowed with greater operational autonomy and authority than standard front-line units;
- less deterrence and ***more willingness to use force***, as Azerbaijan's force posture has become significantly more assertive, reflecting its frustration over the peace process;
- ***expanded battlespace***, with Azerbaijani attacks on Armenia proper, targeting largely civilian population centers in the southern and north-eastern regions along the Armenian-Azerbaijani border.

The Nagorno-Karabakh peace process

Against that backdrop of escalation, the Karabakh peace process also looks bleak. The presidents of Armenia and Azerbaijan met in Switzerland in December and although the meeting was in itself important, the sides remain too far apart on core issues, with little likelihood for any resumption of substantial negotiations. Yet one important suggestion may be to take into account Turkey's role. Turkey has never fully embraced or expressed the positive role of the OSCE Minsk group format. But a positive statement by Turkey, in support of the mediators, may help to bolster the stalled peace process and could encourage more of a discussion of confidence-building measures (CBMs).