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A new balance of power in the South Caucasus: How can it lead to regional stability?

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Abstract

The South Caucasus, comprising Armenia, Azerbaijan, and Georgia, remains a pivotal region at the crossroads of North-South and East-West corridors. The region is rich in energy resources and communication opportunities, and it is entangled in unresolved historical conflicts and external competition. The new situation that emerged in the region after the 2020 Nagorno-Karabakh war presumes a remaking of the new balance of power as well as the re-sharing of new zones of influence. The purpose of the study is to explore the evolving balance of power in the South Caucasus, focusing on the interplay between local actors and external stakeholders, and to evaluate the implications for regional stability. Extra-regional strategic interests and influences, as well as relevant policies and current risks of regional destabilization, are also explored. The research paper emphasizes the role of the contemporary geopolitical environment in the region by taking into consideration the key developments, regional responses, and broader implications. Comparative methods and discourse analysis of official statements are widely used in the research. Some quantitative data were also collected and analyzed for the projection of the evolving balance of power in the region. It has been concluded that the upcoming years will reveal whether the region can transition from a history of conflict to a future of cooperation, or whether new tensions will emerge from the shifting power dynamics. The region's future stability will depend on the capacity of both local and external actors to prioritize dialogue and sustainable development over confrontation.

Keywords: Balance of Power, External Influence, Regional Risks, Regional Stability, South Caucasus, Strategic Interests.

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1. Introduction

The South Caucasus is a region of significant strategic importance. Over the past years, the region has been shaped by enduring conflicts, shifting alliances, and the influence of external powers such as Russia, Turkey, Western actors, etc. As of 2025, the South Caucasus is witnessing significant geopolitical transitions, driven by regional realignments, economic challenges, and declining Russian influence.

The key importance of this region lies in its crucial geographical location at the crossing point of both east-west and north-south corridors of transport and trade. For millennia, the Caucasus has been a link (or buffer) between the Black and Caspian Sea regions, and thus between Europe and Asia (including both China and India), as well as between Northern Europe, Russia, and the Middle East. Its key value lies in its location at the bottleneck of the east-west corridor connecting Europe with Central Asia and beyond, and simultaneously at the intersection of powers playing key roles in international politics [1]. The region has long been a theater of competing interests among regional and global powers due to its location, natural resources, communication routes, and prospects for economic diversification and new transits. Traditionally under Russian influence in the last centuries, the region has seen increasing competition involving near-regional actors – Russia, Turkey, Iran; and extra-regional actors – China, the European Union (EU), and the United States (U.S.). The 2020 Nagorno-Karabakh war marked a watershed moment, reshaping alliances and power dynamics in this volatile region.

Due to such developments, a strong argument can be made that the balance of power in this region has entered a new phase of evolution. From a theoretical viewpoint, the "balance of power" system is one in which the power held and exercised by states within the system is checked and balanced by the power of others. The minimum requirements for a balance of power system include the existence of at least two or more actors of roughly equal strength, states seeking to survive and preserve their autonomy, alliance flexibility, and the ability to resort to war if necessary [2]. All these theoretical databases and relevant criteria can be observed in the processes that occur in the South Caucasus region.

In addition to the theoretical definition of the "balance of power," it is important to determine its various meanings: (a) an even distribution of power; (b) the principle that power ought to be evenly distributed; (c) the existing distribution of power as a synonym for the prevailing political situation; that is, any possible distribution of power that exists at a particular time; (d) the principle of equal aggrandizement of the great powers at the expense of the weak; (e) the principle that our side ought to have a preponderance of power to prevent the danger of power becoming evenly distributed; in this view, a power "balance" is likened to a bank balance, that is, a surplus rather than equality; (f) a situation that exists when one state possesses the special role of holding the balance (called the balancer) and thereby maintains an even distribution of power between two rival sides; and (g) an inherent tendency of international politics to produce an even distribution of power [2].

As for the case of the South Caucasus region, it is obvious that the balance of power is in transformation. Competing geo-strategic arrows are crossed in this region, and this process deeply impacts the situation on the ground. Especially, eastern and western actors are becoming more resolute in enhancing and promoting their own economic and political interests by trying to corner traditional influencers of the region.

2. Research Methodology

The research is primarily based on the discourse analysis of relevant official statements, as well as on the content and comparative analysis of expert assessments regarding the ongoing processes in the South Caucasus. The theoretical materials concerning the balance of power, regionalism, political stability, security, etc., are widely considered and explored in the research. The policies of local, regional, and extra-regional actors, along with their political and economic interests and insights, are also discussed with consideration of appropriate quantitative data analysis.

3. Extra-Regional Strategic Interests and Policies in the South Caucasus

The South Caucasus, a strategic region bridging Europe and Asia, has long been an area of U.S. interest due to its role in energy transit, regional stability, and democratization efforts. As of 2025, the new U.S. administration appears to be reassessing its policies, potentially adopting a more pragmatic and transactional approach toward the region.

Most likely, the new U.S. administration may move away from a heavily ideological framework toward a strategy more closely tied to tangible national interests. This could involve prioritizing energy security, countering Russian and Chinese influence, and maintaining regional stability while possibly downplaying the promotion of democratic governance. For example, early diplomatic signals suggest the administration may streamline relationships with regional powers like Azerbaijan while balancing broader strategic objectives [3]. It should be noted that the previous U.S. administration was not actively engaged in the development of relations with Azeri state officials after the 2020 Nagorno-Karabakh war. In this regard, no bilateral relationship with countries of the Caucasus is more striking and unsettling than the downward spiral of the U.S.-Azerbaijan relationship. What was once a functioning strategic partnership is today a scene of bitter acrimony on both sides [2].

U.S. has its own country-specific implications in the region. For example: Armenia has traditionally relied on its partnership with Russia, but it is now diversifying its alliances. The U.S. could support Armenia's economic and security transitions. However, a transactional U.S. approach might reduce emphasis on democracy-building initiatives, focusing instead on areas of mutual strategic benefit [4]. Azerbaijan stands to benefit from the U.S.'s renewed focus on energy partnerships and stability in the Caspian region. Projects such as the Southern Gas Corridor align with U.S. goals to reduce European dependence on Russian energy, potentially leading to stronger bilateral ties [5]. Georgia's path toward Euro-Atlantic integration could face challenges under a more pragmatic U.S. policy. While Washington has traditionally supported Georgia's NATO aspirations, the new administration might reassess its commitments, balancing them against broader security

priorities. This recalibration could complicate Georgia's aspirations for EU and NATO membership [6]. The recalibration of U.S. policy comes amid declining Russian influence in the South Caucasus, exacerbated by Moscow's preoccupation with the war in Ukraine. This has created a power vacuum, which Turkey and the European Union are eager to fill. The U.S.'s strategic positioning in this context will play a crucial role in shaping the region's geopolitical future [7].

In the shadow of Russia's war of aggression against Ukraine, the geopolitical situation in the South Caucasus region is changing. Azerbaijan is driving much of this change. While Baku has in effect ended the conflict over Nagorno-Karabakh – leading to the displacement of the region's Karabakh Armenians – there are many remaining obstacles to peace with Armenia. The recent events have also spurred numerous geopolitical discussions in western capitals, such as the risk of regional military escalation, the implications for Russia's influence in its neighborhood, the changing dynamics of Eurasian geopolitics, and autocratic challenges to the rules-based order [8].

Obviously, the South Caucasus has historically been a key sphere of Russian influence. However, increasing U.S. engagement in the region presents significant challenges to Russia's strategic interests. The evolving U.S. approach to the region - focused on energy security, democratization, and countering Russian influence - has implications for Moscow's regional standing. This new situation engenders some heavy challenges to Russia's strategic interests, which are related to the diminution of its regional influence. Moscow's reduced engagement in the region leaves room for other external actors to play a more active role. This is the case for the EU and the U.S., for instance [9].

U.S. initiatives, such as supporting energy infrastructure that bypasses Russia, weaken Moscow's leverage [10]. For example, pipelines like the Baku-Tbilisi-Ceyhan oil pipeline and the Southern Gas Corridor reduce Europe's reliance on Russian energy, undermining one of Moscow's key tools of influence.

From the geopolitical viewpoint, the U.S. makes efforts to deepen ties with Armenia, Azerbaijan, and Georgia. Thus, this phenomenon introduces significant competition in the region, which forces Russia to adopt more aggressive postures, including increased military presence and strategic investments, to maintain its foothold [11].

Conflict mediation and management was primary Russia's regional monopoly, but now, the situation transforms also in this field. In long-standing conflicts like Nagorno-Karabakh, U.S. involvement in mediation could diminish Russia's role as the primary broker. Washington's engagement in conflict resolution challenges Moscow's ability to unilaterally shape outcomes to its benefit [12]. At the same time, Russia has a certain potential to respond by strengthening alliances. For example, Russia may deepen its ties with regional partners through economic incentives and military agreements to counterbalance U.S. efforts. Previously, Moscow has offered security guarantees to Armenia while maintaining close energy and trade ties with Azerbaijan [13]. Moscow might also review its military posturing by increasing its military presence in the region, including expanding bases or conducting joint military exercises, to project strength and signal its commitment to safeguarding its interests. Diplomatic initiatives can be implemented as another tool by highlighting Russia's historical and cultural ties to the region, presenting itself as a more reliable partner than the U.S. This approach aims to build goodwill and counter U.S. narratives about democracy and liberal governance [14].

The U.S.'s increasing engagement in the South Caucasus challenges Russia's traditional dominance in the region. While Washington's efforts to promote energy independence and regional stability align with its wider foreign policy goals, they also compel Moscow to adopt reactive measures to safeguard its strategic interests. The interplay between U.S. policies and Russia's responses will shape the geopolitical dynamics of the South Caucasus for years to come.

The new U.S. administration's policy toward the South Caucasus will likely blend continuity with recalibration. While strategic interests such as energy security and countering rival powers will remain paramount, the extent to which democracy promotion and long-term development aid feature in this strategy remains to be seen. This approach will significantly influence Armenia's, Azerbaijan's, and Georgia's regional trajectories and alignments.

Russia, traditionally a dominant player in the South Caucasus, has seen its influence wane due to its protracted conflict in Ukraine and economic sanctions. This has created a power vacuum, allowing regional actors like Turkey and global powers such as the European Union and the United States to assert greater influence.

Turkey has strengthened its partnerships with Azerbaijan through initiatives like the Trans-Anatolian Natural Gas Pipeline (TANAP) and military cooperation. Meanwhile, the European Union has increased its engagement by offering economic and political incentives to Armenia and Georgia [15].

The South Caucasus is a region in flux, shaped by the interplay of regional ambitions, global strategic interests, and the diminishing role of traditional powers like Russia. The coming years will be critical as Armenia, Azerbaijan, and Georgia navigate their paths amidst ongoing tensions and emerging opportunities. The decisions made by these nations will not only determine the region's future but also influence broader geopolitical dynamics.

The South Caucasus has also become a focal point of the European Union's (EU) strategic interests. The EU has engaged with the region primarily through the Eastern Partnership and other bilateral agreements to promote economic development, democratic governance, and conflict resolution. The EU's interests in the South Caucasus are driven by a combination of energy security, regional stability, and the promotion of European values. However, challenges such as unresolved territorial disputes, Russian influence, and internal governance issues complicate the EU's engagement.

The EU has engaged with all three South Caucasus states through Association Agreements and Deep and Comprehensive Free Trade Areas with Georgia, while Armenia has opted for a Comprehensive and Enhanced Partnership Agreement due to its membership in the Russia-led Eurasian Economic Union [16]. Azerbaijan, while maintaining close energy ties with the EU, has resisted deeper political integration.

One of the EU's primary interests in the South Caucasus is energy security. The region plays a critical role in reducing the EU's reliance on Russian energy supplies. The Southern Gas Corridor (SGC), which transports Azerbaijani gas to Europe

via Georgia and Turkey, is a key component of this strategy [17]. The EU has invested heavily in alternative energy routes to diversify its energy sources, especially after the 2022 Russian invasion of Ukraine.

Azerbaijan, particularly, has become a key energy partner, supplying natural gas to EU markets through the Trans Adriatic Pipeline (TAP) and the Trans-Anatolian Natural Gas Pipeline (TANAP) [18]. The EU's energy diversification strategy relies on stable and secure access to these resources, making stability in the region a critical concern.

The EU has also engaged in conflict resolution efforts in the South Caucasus, particularly concerning the Nagorno-Karabakh conflict between Armenia and Azerbaijan and the territorial disputes in Georgia [19]. The EU has played a mediating role in diplomatic negotiations and has provided economic and humanitarian assistance to conflict-affected areas.

Following the 2020 Nagorno-Karabakh war, the EU increased its involvement in peace-building efforts, providing financial assistance to displaced persons and supporting negotiations through the European Council's mediation [20]. However, Russia's dominant security role in the region, including its peacekeeping presence in Nagorno-Karabakh, limits the EU's direct influence.

The EU is one of the largest trading partners of the South Caucasus states, particularly Georgia and Azerbaijan. The DCFTA (Deep and Comprehensive Free Trade Areas) with Georgia has enhanced economic ties, leading to increased trade and investment [21]. Armenia, despite being part of the EAEU, has maintained strong economic relations with the EU under CEPA.

Azerbaijan's economy is heavily reliant on energy exports, with the EU being one of its primary markets. However, Azerbaijan's human rights record and democratic deficits have complicated deeper political engagement [22]. The EU has employed a pragmatic approach, balancing its energy interests with concerns over governance and human rights.

Despite its strategic interests, the EU faces significant challenges in the South Caucasus that are related to a) Russian influence: Russia maintains a strong military and political presence in Armenia and Georgia's breakaway regions (South Ossetia and Abkhazia). This limits the EU's ability to shape security dynamics [23]; b) *unresolved conflicts*: The protracted conflicts in Nagorno-Karabakh and Georgia's breakaway regions create instability and hinder regional integration with the EU; c) *democratic governance issues*: Corruption, weak institutions, and democratic backsliding in some states undermine the EU's efforts to promote good governance [24]; d) *divergent foreign policy goals*: Georgia previously aspired to EU and NATO membership, Armenia is making its first stable steps toward its European path, and Azerbaijan pursues a more countering foreign policy, complicating the EU's regional approach.

To enhance its role in the South Caucasus, the EU must adopt a more cohesive and proactive strategy that balances its geopolitical interests with the promotion of European values. Baku and Yerevan must therefore be considered, designed and implemented proactively with the view of reaching the EU's regional goals, including peace and normalization; stability and democracy; development of regional trade and transit routes; increased EU influence; and isolation and containment of Russia [8]. In this respect, Armenia's commitment to the regional peace based on mutual respect of democratic values, state sovereignty and territorial integrity is obvious. But there is no reciprocity from the Azeri side which has territorial ambitions toward Armenia.

China, as the second-largest economy with a rapidly expanding economic footprint globally and economic policies that are very distinct from those of Western countries, has become a focus of international attention. China raises admiration and high expectations from many developing countries, yet it causes concerns among countries that are critical of Chinese economic policies, suspicious of Chinese intentions, or facing strong competition from China in external markets. What is usually seen as the most alarming is China's capability and already existing practice of using economic leverage over dependent developing countries to pursue certain political goals.

Over the past two decades, trade relations between China and the South Caucasus have developed considerably [25]. Trade is the priority tool for China to advance its interests in the South Caucasus. In last two decades all three South Caucasus countries are more importing from then exporting goods to China. This fact gives China a very efficient tool of economic influence in the region. China is more restrained to get involved in apparent political issues or play a role of mediator for conflict resolution. But its economic posture has a uprising impact of the regional developments due to its geo-strategic initiative like "One Belt - one Road".

China's growing presence in the South Caucasus is driven by its strategic interests in economic expansion, energy security, and geopolitical influence. The region is a critical juncture for China's Belt and Road Initiative (BRI). China's involvement in the South Caucasus is largely pragmatic, focused on economic gains while avoiding deep political entanglements. Unlike Russia, which maintains military and political dominance in the region, and the West, which is engaged through economic and security partnerships, China has primarily pursued an economic strategy with minimal political involvement.

China's interest in the South Caucasus is largely driven by its flagship infrastructure project, the Belt and Road Initiative. The region plays a crucial role in the Middle Corridor, which connects China to Europe via Central Asia, the Caspian Sea, and the South Caucasus.

China has made significant investments in transportation and logistics infrastructure in Georgia and Azerbaijan. The Baku-Tbilisi-Kars (BTK) railway, inaugurated in 2017, has become a vital component of the Belt and Road Initiative, providing a faster alternative to traditional maritime routes [26]. Additionally, China has invested in the Port of Poti in Georgia and the Port of Baku in Azerbaijan, aiming to enhance regional connectivity [27].

China has become an important trading partner for all three South Caucasus countries. Azerbaijan's bilateral trade with China reached approximately \$2.2 billion in 2022, largely driven by energy exports [28]. China is Georgia's third-largest trading partner, and a Free Trade Agreement (FTA) between the two countries, signed in 2018, has boosted exports,

particularly wine and agricultural products [29]. While trade is relatively smaller, China has increased its investments in Armenia's mining and infrastructure sectors [30].

China's energy security strategy involves diversifying its energy imports, and the South Caucasus plays a role in this diversification. Azerbaijan, with its vast oil and gas reserves, is a particularly attractive partner. The China National Petroleum Corporation (CNPC) has participated in energy projects in Azerbaijan, and Chinese firms have explored cooperation in gas transit routes connecting Central Asia to Europe via the Caspian region [27].

China's approach to the South Caucasus differs significantly from that of Russia, the EU, and the U.S. Beijing maintains a neutral stance on regional conflicts, such as the Nagorno-Karabakh dispute between Armenia and Azerbaijan, avoiding deep political entanglements.

China carefully manages its engagement in the South Caucasus to avoid antagonizing Russia, which considers the region part of its traditional sphere of influence. While China's economic presence has grown, it does not challenge Russia's political and military dominance in the region [29]. Instead, Beijing seeks complementary engagement, focusing on trade and investment while respecting Moscow's security interests.

China has strong economic ties with Iran and Turkey, both of which are key players in the South Caucasus. The 25-year strategic partnership agreement between China and Iran (signed in 2021) includes energy and infrastructure cooperation, which indirectly affects the South Caucasus [31]. Meanwhile, China's growing trade with Turkey supports its transit ambitions through the Middle Corridor, strengthening economic links across the region.

Unlike Russia and the U.S., China has largely refrained from direct military engagement in the South Caucasus. However, Beijing has increased security cooperation through arms sales and counterterrorism initiatives.

Azerbaijan has purchased Chinese military equipment, reflecting growing defense ties [28]. China-Armenia relations include limited military cooperation, mainly in training and diplomatic exchanges. Georgia, despite its previous Western orientation, has also engaged in security dialogs with China, though at a lower level.

China faces several challenges in deepening its presence in the South Caucasus. From the viewpoint of geopolitical rivalries, the region is contested by Russia, the EU, Turkey, and Iran, making long-term Chinese expansion difficult. Another challenge for China is the ongoing tensions, particularly between Armenia and Azerbaijan, that could disrupt China's economic projects. The political instability and governance issues in the region also pose investment risks for Chinese companies.

Despite these challenges, China is likely to continue expanding its economic footprint while maintaining a neutral stance on political issues. The Middle Corridor's growth, along with China's need for energy diversification, ensures that the South Caucasus will remain an area of strategic interest for Beijing.

Therefore, China's engagement in the South Caucasus is driven by economic imperatives rather than political or military ambitions. Through the Belt and Road Initiative, trade agreements, and infrastructure investments, China has positioned itself as a key economic player in the region. However, Beijing remains cautious, avoiding direct involvement in regional conflicts and carefully managing its relations with Russia, the EU, and local actors. As global competition over connectivity routes intensifies, China's role in the South Caucasus will likely grow, shaping the region's economic and geopolitical landscape in the coming years.

Turkey, as a regional power, has demonstrated significant interest in the South Caucasus, driven by geopolitical, economic, and security considerations. Turkey's strategic interests in the region are focused on its relations with Azerbaijan, economic investments, energy corridor initiatives, and geopolitical dynamics involving Russia, Iran, and the West. The still-closed borders with neighboring Armenia are one of the key stones in the promotion of its regional interests.

Turkey's involvement in the South Caucasus is deeply rooted in its Ottoman heritage and cultural connections, particularly with Azerbaijan. The fall of the Soviet Union provided Turkey with an opportunity to expand its influence in the newly independent states [32].

Turkey's economic interests in the South Caucasus are primarily centered around energy and trade. The Baku-Tbilisi-Ceyhan (BTC) pipeline and the Baku-Tbilisi-Kars (BTK) railway are critical infrastructure projects that enhance Turkey's role as an energy transit hub [33]. These projects not only provide Turkey with economic benefits but also increase its strategic leverage over European energy security. This circumstance gives Turkey a chance to increase its regional and global ambitions.

Azerbaijan is Turkey's closest ally in the region, bound by ethnic and linguistic ties. The two countries have established strong military and economic partnerships, exemplified by joint military exercises and extensive energy cooperation [34]. The 2020 Nagorno-Karabakh conflict further solidified their alliance, with Turkey providing diplomatic and military support to Azerbaijan.

Turkey's actions in the South Caucasus are influenced by its relations with other regional powers. The rivalry with Russia, cooperation with NATO, and the complex relationship with Iran all shape Turkey's strategies in the region [35]. Turkey's active role in the Nagorno-Karabakh conflict signaled its intent to challenge Russian dominance in the region. The withdrawal of Russian peacekeeping mission from Nagorno-Karabakh in 2023 considerably fortified Turkish presence in the region.

Turkey's involvement in the South Caucasus is not without challenges. Relations with Armenia remain strained due to its denial of the Armenian Genocide and the closed border with the neighboring country. Additionally, Turkey's growing influence has raised some concerns among Western partners about the rise of its regional hegemony. After the 2020 Nagorno-Karabakh war, there is dialogue between the two countries about the restoration of diplomatic relations and the reopening of national borders. It should be noted that Armenia's government has no claims for Armenian Genocide recognition by Turkey, and it exercises soft politics toward Turkey. However, despite all these initiatives, Turkey still keeps its border closed.

This showcases that Turkey's strategic interests in the South Caucasus are driven by a combination of historical factors, economic ambitions, and geopolitical calculations. As Turkey continues to assert its influence in the region, it will play a pivotal role in shaping the future of the South Caucasus and its relations with global powers.

The South Caucasus is considered a critical region for Iran's geopolitical, economic, and security considerations as well. As a regional power sharing borders with Armenia and Azerbaijan, Iran's engagement in the South Caucasus is driven by historical ties, energy diplomacy, trade routes, and national security concerns. After the Soviet Union's dissolution in 1991, Iran navigates complex relationships with Russia, Turkey, and Western actors. Thus, Iran's strategic interests in the South Caucasus focus on economic, security, and political dimensions while also considering challenges that limit Tehran's influence.

Iran's geographical position makes it a crucial player in regional energy transportation. With significant oil and gas reserves, Iran seeks to integrate itself into South Caucasus energy networks to counterbalance Western-backed projects like the Baku-Tbilisi-Ceyhan (BTC) pipeline. However, U.S. sanctions have hindered Iran's ability to fully participate in trans-regional energy projects [36].

Iran views the South Caucasus as a key transit corridor. The International North-South Transport Corridor (INSTC), linking India, Iran, and Russia via Azerbaijan, enhances Iran's trade connectivity [37]. Georgia also plays a role in Iranian economic strategy, though Tbilisi's Western orientation had limited cooperation.

Iran maintains strong economic ties with Armenia [38] particularly as a strategic partner to bypass Western sanctions. The two countries collaborate in energy projects, including the Iran-Armenia gas pipeline, which provides Armenia with an alternative to Russian energy dependence. Conversely, Iran's trade with Azerbaijan is complicated by political tensions, although economic engagement remains significant, particularly in agriculture, construction, and non-oil sectors.

Iran has also security concerns in the South Caucasus that are related to its ethnic composition. Azerbaijan's growing nationalism and its close ties with Turkey pose a challenge to Iran, home to a large Azerbaijani minority in its northwestern provinces. Tehran fears that Baku's pan-Turkic aspirations could fuel separatist sentiments among Iranian Azerbaijanis [39].

The 2020 Nagorno-Karabakh conflict heightened Iranian concerns, as Azerbaijan's victory, backed by Turkey and Israel, altered regional power balances. Iran was particularly wary of Israeli military cooperation with Baku, fearing an increased Israeli intelligence presence near its borders [40].

Iran's engagement in the South Caucasus is also shaped by its complex relations with Russia and Turkey. While Iran and Russia share concerns over Western influence in the region, they also compete for economic and strategic influence. Turkey's growing presence in Azerbaijan challenges Iran's influence, especially given Ankara's push for a stronger regional role through military and economic agreements [41].

Iran employs a pragmatic foreign policy approach in the South Caucasus, balancing relations between Armenia and Azerbaijan. Tehran officially supports Azerbaijan's territorial integrity but also maintains close ties with Armenia to counterbalance Turkish-Azerbaijani influence. This dual-track diplomacy has allowed Iran to mediate regional tensions while securing its own interests [42].

Iran is also wary of Western engagement in the South Caucasus, particularly NATO's cooperation with Georgia and the EU's energy projects that bypass Iran. Tehran opposes any regional arrangements that could strengthen Western military or economic presence at its doorstep [43].

Despite its strategic interests, Iran faces limitations in the South Caucasus. U.S. sanctions restrict its economic outreach, reducing its role in energy projects and infrastructure development. Additionally, the strengthening of Azerbaijan-Israel ties presents a geopolitical challenge for Tehran. Iran's cautious foreign policy, driven by concerns over ethnic unrest and external pressures, limits its ability to act decisively in the region. While Tehran seeks to maintain influence through trade, energy diplomacy, and political engagement, external pressures from Turkey, Israel, and the West constrain its role. Moving forward, Iran's ability to navigate regional complexities will depend on its diplomatic maneuvering and its capacity to adapt to shifting geopolitical realities.

Foreign strategic interests and policies in the South Caucasus also include a geo-economic component, primarily based on foreign direct investments. As regards the region's developing geo-economic role, a relevant analogy is the straits/canals of Suez, Panama, Hormuz, or Malacca. The central role of these waterways is obvious. The South Caucasus is a similar corridor, albeit a land link rather than a sea link. Geography and politics combine to give it a similar role [1]. This circumstance increases the geopolitical significance of the region, taking into account the geostrategic perspectives of regional development and the growing role of the "Persian Gulf-Black Sea" corridor. In accordance with these strategies, foreign direct investments (FDI) from the U.S., EU, China, Russia, Turkey, and Iran need to be compared.

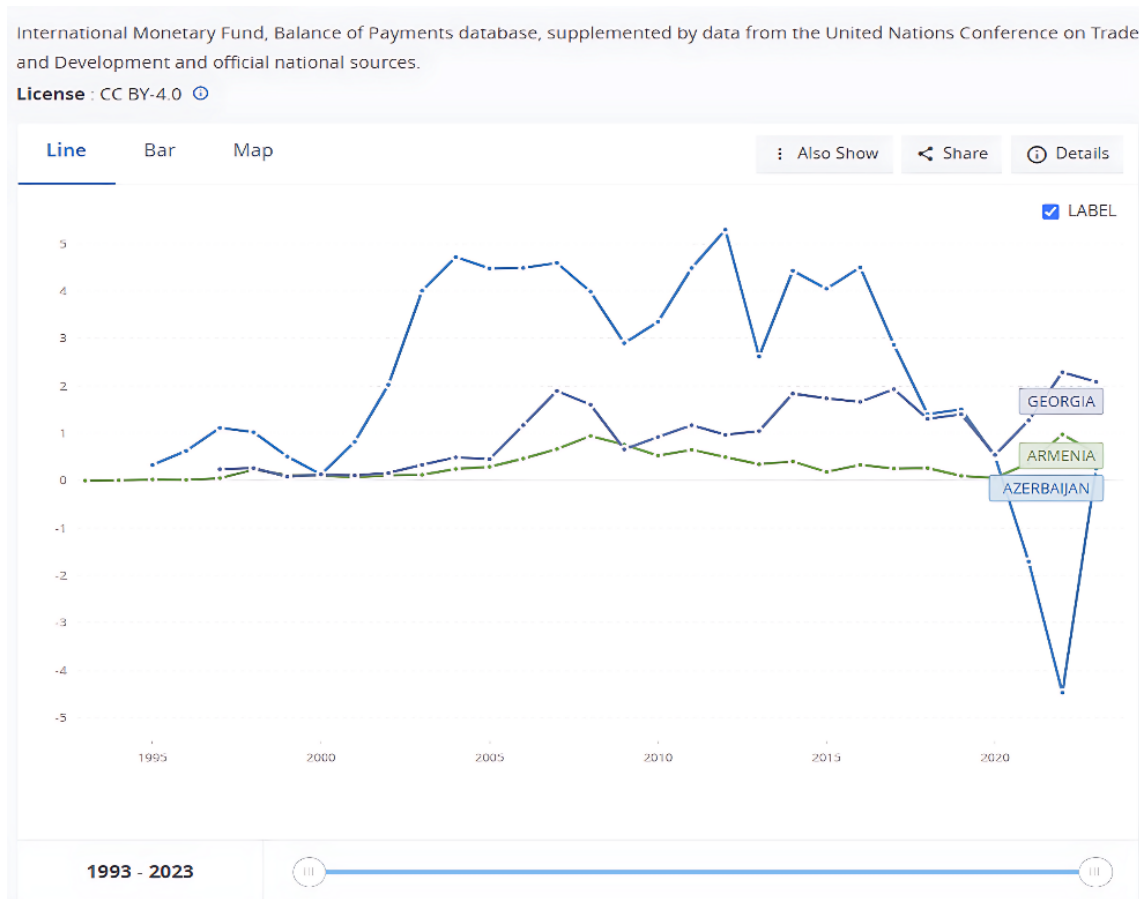


Figure 1.

Foreign direct investment, net inflows (BoP, current US\$) - Azerbaijan, Armenia, Georgia in 1993-2023.

Source: Foreign direct investment (FDI) in Armenia [44].

Figure 1 describes the FDI modulations with net inflows in the South Caucasus region from 1993 to 2023. The diagram showcases that the FDI rate is the highest in Azerbaijan; however, after the 2020 Nagorno-Karabakh war, the inflows decreased compared to the previous period. Georgia is in second place by the volume of FDI, and in this regard, it is relatively more stable compared to Azerbaijan. Armenia is the country with the lowest FDI rate in the region. However, we can notice a certain growth of inflows after the 2020 Nagorno-Karabakh war. The volume of FDI is directly related to the strategic interests and implications toward the regional countries, taking into account their capacities to be integrated into regional or even extra-regional economic projects. Most likely, Armenia's lowest FDI rate is linked to its closed borders with two neighboring countries: Turkey and Azerbaijan, which hinder its economic development opportunities.

To have a more widened picture of FDI in the South Caucasus countries, it is important to particularly focus on inflows from U.S., EU, China, Russia, Turkey, and Iran in 2022-2023.

Table 1 describes the FDI or financial support by specific foreign actors to specific regional countries. This approach helps to identify the nature of mutual relations and interests that play a significant role in the remaking of the balance of power in the region. It is important to explore the post-war period because it changed not only the situation on the ground but also the prerogatives for regional and extra-regional countries.

As for near-regional actors, despite the traditional highest rate of Russia's FDI in Armenia, a significant drop down is noticed. Compared to 2022, Russian direct inflows decreased more than twice by opposite to their growth in the case of Azerbaijan. This showcases that Russia has made strategic revision in its regional policy. As for Georgia, the Russian FDI rate dropped approximately twice.

The highest rate of Turkey's FDI is in Azerbaijan which is considered as its most reliable regional strategic ally. In the case of Georgia, Turkey has tripled its FDI in Georgia, highlighting its strategic significance in the region. No data available for Turkey's FDI in Armenia because of closed borders and the lack of diplomatic relations. Iran has also increased its FDI in Azerbaijan, but there is no data available in the case of Armenia. Iranian direct inflows in Georgia are very small. Maybe this circumstance can be determined by the absence of common borders with Georgia. Most likely Iran prefers to invest in bordering countries that can serve as transit routes for its economic implications.

As for extra-regional actors, their FDIs vary from the lowest \$4 million to the highest €588. U.S FDI in Armenia for 2022-2023 is about \$4-5 million compared to Azerbaijan's highest \$748.0 million. Despite U.S. 2022 FDI rate in Azerbaijan, a certain dropdown is noticed for the next year. Such a dropdown is seen in the case of Georgia.

Table 1.

FDI or financial support to Armenia, Azerbaijan, and Georgia from the U.S., EU, China, Russia, Turkey, and Iran in 2022-2023.

Country	U.S. Direct Investment	EU Financial Support	China Direct Investment	Russia Direct Investment	Turkey Direct Investment	Iran Direct Investment
Armenia	2022 - \$4.0 million	2022 - €130 million Enlargement and Eastern Neighbourhood [45]	2022 - \$50.0 million	2022 - \$697.0 million	2022-2023 not readily available	2022-2023 not readily available
	2023 - \$5.0 million Armenia - International Trade and Investment Country Facts [46]	2023 - €588 million EU Announces new €270 million Resilience and Growth package for Armenia [47]	2023 - approx. \$50.0 million Interesse [48]	2023 - approx. \$250.0 million Foreign direct investment (FDI) in Armenia [44]		
Azerbaijan	2022 - \$748.0 million	2022 - approx. €140 million	2022 - \$28.920 million	2022 - approx. \$518.0 million Azerbaijan - International Trade and Investment Country Facts [49]	2022 - not readily available	2022 -approx. 250.0 million Iran Foreign Direct Investment 1970-2025 [50]
	2023 - \$555.0 million Azerbaijan - International Trade and Investment Country Facts [49]	2023 - approx. €145 million Aid [51]	2023 - \$34.790 million Azerbaijan. [52]	2023 - approx. \$617.0 million Ibadoghlu [53]		
Georgia	2022 - \$49.0 million	2022 - approx. €85 million	2022 - \$43 627,3 million	2022 – approx. \$108.0 million	2022 - \$55.0 million	2022 -approx. 5.35 million 2023 FDI in Georgia at USD 1.595 Bln [55]
	2023 - \$20.0 million Georgia - International Trade and Investment Country Facts [56]	2023 - approx. €90 million Georgia to lose 121 million euros in EU funding over 'democratic backsliding' [57]	2023 - \$47 330,6 million Georgia's Investment Landscape: Comparative Analysis of Chinese and Western Investments (2018-2023) [58]	2023 – approx. \$67.0 million Georgia's Economic Dependence on Russia: Summary of 2023 [59]		
					2023 – approx. \$168.8 million 2023 FDI in Georgia at USD 1.595 Bln [55]	2023 - not readily available

As for China's FDI, the rates are quite similar balancing between \$30-50 million for all three regional countries. This showcases that China is intended to develop more balanced economic policy in the region.

The EU's financial support for Armenia considerably increased in the post-war period, reaching the highest rate compared to other regional countries. This showcases that the EU follows long-term strategic interests in the region via Armenia. The EU's growing support for Armenia has led to Azerbaijani discontent and is perceived as a geopolitical challenge to Russia's regional interests. Besides Armenia, EU financial support has fractionally increased in other regional countries.

4. South Caucasus Countries under External Influences

All foreign actors have different impacts on South Caucasus countries. After the 2020 Nagorno-Karabakh war, Armenia faced sovereignty challenges and is now amidst regional tensions. The South Caucasus security environment is mainly energy-focused. It is almost certain that Russia will continue to hinder Armenia's independence. The chance that Turkish-Armenian rapprochement will occur in the next five years is remote [60].

But now, Armenia's geopolitical strategy has undergone a significant shift as it seeks to distance itself from Russian dependence, particularly in security and border management. For the first time in 32 years, Armenian forces assumed control of a checkpoint on the Armenian-Iranian border in January 2025, symbolizing a reclamation of sovereignty. Concurrently, Armenia's border with Turkey is now jointly managed with Russian forces, though the Armenian government has actively reduced Moscow's military role in domestic matters [4]. Armenia's pivot towards the West includes economic diversification efforts, focusing on transforming Yerevan into a tech hub. By hosting the 2024 World Congress on Innovation & Technology, Armenia has attracted foreign investments from major corporations such as Amazon and Google. However, lingering tensions with Azerbaijan, particularly after the Second Nagorno-Karabakh War, and unresolved disputes over regional autonomy pose challenges to sustainable development [61].

Armenia's longstanding dependence on Russia spans critical sectors, including energy, transportation, and security. Recent developments and government initiatives highlight the potential for reducing Russian influence while pursuing regional connectivity projects.

To counter Russian dependency, Armenia has taken steps toward European integration with a considerable support from the civil society. In January 2025, the Armenian government officially endorsed a draft bill, initiating its process to joining the European Union [62]. In this way Armenia is signaling a clear intention to align more closely with Western economic partners and political frameworks.

There is a strong belief that Armenia's "de-Russification" efforts will require increased economic and political support from Western partners. Strengthened ties with Europe and the U.S. could facilitate access to new markets, reduce energy reliance on Russia, and bolster domestic reforms [63].

The unblocking of transportation and communication links is another cornerstone of Armenia's economic and geopolitical strategy. In this respect, the discussions are focused on reopening routes closed due to longstanding conflicts in the South Caucasus. Armenian Foreign Minister Ararat Mirzoyan has reiterated the government's commitment to regional integration while emphasizing the principles of sovereignty and reciprocity [64]. Prime Minister Nikol Pashinyan has expressed readiness to ensure the secure transit of goods, vehicles, and passengers through Armenian territory. Such projects could enhance regional connectivity and boost Armenia's economy [65]. However, the unblocking of communications remains fraught with challenges. Conflicting interests among regional powers, such as Turkey and Azerbaijan, could complicate negotiations. Without careful mediation, these efforts risk exacerbating existing tensions [66].

Nevertheless, Armenia is making deliberate efforts to reduce Russian influence by fostering closer ties with Western allies and pursuing economic diversification. The unblocking of regional communications holds promise for economic growth and stability but requires navigating complex geopolitical realities. With sustained international support and careful negotiation, Armenia can position itself as a more independent and integrated player in the South Caucasus.

It wasn't in Russia's interest to end the Nagorno-Karabakh conflict because it allowed Russia to maintain some control over the two former Soviet Republics through dependence (economic, military, and diplomatic) [60]. However, the developments in the region have shown that without Russia's approval, Azerbaijan couldn't launch a large-scale war in Nagorno-Karabakh in 2024. Even Russia has acknowledged that the war was a common productive operation with Turkey. The situation on the ground changed when Russian peacekeepers entered the zone of conflict. Most likely, Russia had pretended to develop new levers of pressure on both sides by locating its military forces in Nagorno-Karabakh for five years. However, after two to three years, it was obliged to leave the territory because it became unable to protect the Armenian population, which was forced to exodus from its motherland.

As for Azerbaijan, it has declared itself as a dominant actor in the South Caucasus, driven by energy wealth and strategic infrastructure projects. Baku has aggressively promoted the fake concept of "Western Azerbaijan," illegitimately claiming lands within Armenia's sovereign territories.

Infrastructure development remains central to Azerbaijan's strategy. The completion of the Rasht-Astara railway, part of the International North-South Transport Corridor (INSTC), solidifies Azerbaijan's role as a transit hub linking Russia to the Persian Gulf. This project underscores Baku's commitment to integrating itself into global trade networks while leveraging its geographic location for strategic gains [4]. However, notably, Azerbaijan's oil reserves are expected to dwindle over the next two decades. It will be challenging for the Aliyev regime to sufficiently diversify the economy in preparation for the presumed economic shock. If the economic crisis hits, the domestic political atmosphere will become tumultuous, unstable, and uncertain for the survival of the Aliyev regime [60].

As for Georgia, its internal politics and foreign policy orientation remain pivotal to the region's stability. However, previous clear pro-Western orientation at the same time was limiting Tbilisi's regional potential. Actually, it was difficult for Georgia to find its place in the region in the context of an intensified competition for influence between the Russian Federation and Turkey, as well as under the conditions of decrease of Western influence in the South Caucasus [67].

The October 2024 parliamentary elections highlighted deep societal polarization, with the ruling Georgian Dream party advocating for closer ties with Russia and a more conservative stance. Conversely, opposition parties have championed European integration and democratic reforms. The outcome of this election will shape Georgia's foreign policy trajectory and its ability to maintain a balance between Russia and the West [68].

Georgia's geographic position as a transit route for energy and trade between Europe and Asia enhances its importance. However, political instability and concerns over democratic backsliding pose challenges to its aspirations for European Union and NATO membership.

Taking into consideration Russians' migration into neighboring countries due to Russian invasion of Ukraine in 2022, it becomes important to focus on political aspect of this phenomenon that could be used as a soft tool of Russian interests' promotion in receiving countries. In this stance, Armenian and Georgian cases need to be explored. Some experts point out that there has been significantly less attention paid to the effects of the Russian migration on the receiving societies, while in many former Soviet republics where Russians have fled, a unique societal and political environment is forming, which is developing and changing very quickly [69]. The picture in Armenia and Georgia is not the same because of some distinctions among the perception of Russians. However, there were no uncomfortable feelings among Armenians regarding Russian migrants. As for Georgians, the divergent understandings of political action have led to mutual misunderstandings and a degree of alienation between Russian migrants and Georgian civil society [69]. Some kind of prudence regarding Russian migrants among Georgian society is most likely due to the consequences of 2008 war in South Ossetia and Abkhazia when Russia played a key role to strengthen and support the separatism. The fear of Russia's new probable intervention into Georgia as it was in the case of Ukraine, made Georgian civil society skeptical about Russian migrants.

Generally, the Georgian-Azerbaijani partnership in the region remains fruitful and mutually beneficial. In the conditions of the blockade of the Armenia-Azerbaijan border, Georgia remains the most important route for ensuring the export of Azerbaijan's energy resources and the development of transport links with Turkey. Relations between Tbilisi and Baku are somewhat clouded by territorial disputes over border demarcation (the situation is complicated by the presence of religious sites in these areas [67]). Meanwhile, the softened position of the Georgian authorities in relation to the Russian Federation, as well as the limited potential of Georgia in the South Caucasus, raises concerns about its prospects [67].

5. Current Risks of Regional Destabilization

Small and inherently weak states of the South Caucasus, suffering from long-standing ethnic and territorial conflicts and/or the feeling of insecurity vis-à-vis larger neighbors, seek alliances with extra-regional actors to ensure their survival and security [70]. This approach is not always functional because sometimes larger neighbors can use smaller ones for their own interests.

While regional security interactions are not fully independent of global ones, big powers enjoy significant power projection capabilities and wide agendas that often play a certain role in regional security interactions and alliance/alignment choices [70].

Membership within or orientation towards the conflicting alliances strengthens intra-regional rifts, further decreasing the chances of peaceful conflict resolution in the South Caucasus [70].

The autumn war in the Nagorno-Karabakh region in 2020 had a huge impact on the strategic balance of power in the South Caucasus region. This issue is important for regional security and power projection in the South Caucasus [71]. Enmities and amities indigenous to the South Caucasus, along with the inherent weaknesses of the regional states, pave the way for big power penetration [70]. The case of the Nagorno-Karabakh conflict proves the above-mentioned theoretical statement. After two years of the 2020 war in Nagorno-Karabakh, Russia's invasion of Ukraine and its preoccupation with the war, as well as its subsequently forced passiveness in the South Caucasus, have created a security vacuum in the region, where it had previously established a military-political hegemony. The balance of power has shifted in favor of the Azerbaijani-Turkish nexus, creating a new geopolitical reality, which comes with both opportunities and challenges [72].

Baku also tried to increase the stakes for Yerevan by challenging Armenia's own international borders and making claims on Armenian territories. By making Armenia's borders more insecure, it sought to shift Armenia's focus to concern for its own territorial integrity and force it to give up any claims on Nagorno-Karabakh. In September 2022, a major ceasefire breakdown saw Azerbaijani forces move past Armenian-held positions along their shared border into Armenia. International powers widely condemned the incursion as a violation of Armenia's territorial integrity. But Azerbaijan, backed by Turkey, rejected this [73]. In this regard, it is crucial to consider that Russia's President V. Putin, dismissing Yerevan's strong criticism of the Russian-led Collective Security Organization, insisted on Nov. 28, 2024 that Armenia has not been subjected to foreign aggression in 2022 [74]. This fact showcases that Azeri aggression over Armenia's sovereign territory was backed not only by Turkey but also by Russia which can be characterized as a smooth continuation of Russian-Turkish common operation against Armenia's legitimate interests in the region.

Recent geopolitical developments suggest a significant risk of renewed tensions and possible escalation along the Armenia-Azerbaijan border. Both Armenia and Azerbaijan have fortified their positions along the border, reflecting heightened mistrust. The lack of sustained dialogue and a growing arms race in the region increase the likelihood of localized skirmishes escalating into broader conflict. Several factors, including political rhetoric, military activities, and regional alignments, contribute to this volatile situation.

Azerbaijani President Ilham Aliyev recently escalated tensions by labeling Armenia a "fascist state," citing concerns over Armenia's ongoing military modernization and arms acquisitions from countries like France and India. In a public statement on January 7, 2025 Aliyev warned, "Fascism must be eradicated. Either the Armenian leadership will destroy it, or we will" [75]. This rhetoric is strongly reminiscent of baseless claims used by Vladimir Putin about Ukraine to justify Russia's invasion. He has claimed that Ukraine must be "denazified" [76]. By and large, Aliyev imitates Russian leader's autocratic discourse to build legitimate reasons for a new invasion into Armenia's sovereign territory.

Armenian Prime Minister Nikol Pashinyan responded by cautioning that such rhetoric could serve as a precursor to military aggression. He reiterated Armenia's commitment to peace and urged Azerbaijan to prioritize dialogue over inflammatory statements [77].

It has to be noted that Armenia's recent decision to initiate the process of joining the European Union has further strained relations. This shift toward Western integration has been perceived by Azerbaijan as a potential challenge to the regional balance of power. Armenia's EU bid could exacerbate existing tensions by introducing new political and economic dynamics unfavorable to Azerbaijan [78].

The risk of escalation between Armenia and Azerbaijan remains high, driven by political rhetoric, military developments, and shifting regional alliances. Without constructive diplomatic engagement, tensions could deteriorate further, jeopardizing regional stability.

In the eyes of the international community, Aliyev has turned into an aggressor, and his authoritarian policy of conflict resolution has been condemned by the West [72]. This circumstance does not give a legitimate ground to Azeri leader for the development of new pretexts to enhance its aggression towards Armenia by aiming to force it to an "authoritarian peace". Consequently, the West's posture for the South Caucasus stability gains more power and it reshape the balance of power in this volatile and uncertain region.

From the viewpoint of diplomatic deterrence, the EU civilian mission along the border of Armenia-Azerbaijan serves as a real and efficient tool for stabilization. It has proven its effectiveness over the last two years. Fortunately, the European Union has considered extending its monitoring mission in Armenia for an additional two years. The purpose of this mission is to enhance stability and monitor the ceasefire along the border. The mission is viewed as a means to prevent potential hostilities and ensure adherence to the ceasefire agreements that were brokered following the 2020 Nagorno-Karabakh conflict. However, Azerbaijan has strongly opposed the extension of this mission.

The EU's monitoring mission was initially deployed in Armenia in 2022, after the ceasefire was brokered by Russia following the 2020 Nagorno-Karabakh conflict. The mission is tasked with monitoring and reporting on security conditions along the border between Armenia and Azerbaijan. It plays a key role in facilitating dialogue between the two countries and discouraging further escalations. Armenian officials consider the EU's presence as crucial for ensuring regional stability and avoiding conflict [79]. Meanwhile, Azerbaijan has voiced strong objections to the extension of the EU monitoring mission, accusing it of interference in the region and suggesting that the mission might serve as a vehicle for espionage. Azerbaijani officials argue that the presence of EU monitors could challenge Azerbaijan's territorial claims and sovereignty, particularly in relation to the status of Nagorno-Karabakh and the surrounding areas. This opposition aims at raising doubts about whether the EU mission can serve as an effective deterrent against potential Azerbaijani aggression.

The success of the EU mission in preventing future aggression depends and will depend heavily on the cooperation of all parties involved. While Armenia views the EU mission as a stabilizing factor, Azerbaijan's strong opposition indicates that the mission's deterrent effect may be limited. Moreover, without the support of other regional players such as Russia, Turkey, or the United States, the EU's influence over Azerbaijan's military strategy remains uncertain [80]. The strong opposition from Azerbaijan suggests that the mission might not have the desired deterrent effect unless there is broader regional consensus and cooperation on this issue.

6. Conclusion

The South Caucasus remains a dynamic and volatile space where regional aspirations intersect with global strategic interests. The post-2020 period has underscored the complexities of navigating these dynamics, as new power configurations emerge amid enduring challenges.

The shift in the balance of power in the South Caucasus presents both opportunities and risks for regional stability. On the one hand, the decisive military outcome of the Nagorno-Karabakh conflict reduces the chances of renewed large-scale war in the immediate future. Azerbaijan has largely achieved its strategic objectives, and Armenia, despite its grievances, is in a position where it must reassess its long-term geopolitical strategy. However, the region remains fragile due to unsettled tensions and competing external influences. Still, closed borders between Armenia-Turkey and Armenia-Azerbaijan considerably hinder stabilization, integration, and peace-building in the region. Most likely, a lasting peace in this space will depend on several key factors:

a) The Armenia-Azerbaijan Peace Process – A sustainable settlement requires formal agreements on border demarcation, security guarantees, and economic cooperation. While negotiations are ongoing, deep mistrust, nationalistic and aggressive sentiments (especially on the Azeri side) could derail progress. No doubt that any failure in diplomatic talks could lead to new tensions and even clashes, particularly along the Armenia-Azerbaijan border.

b) Armenia's strained relations with Russia and its growing ties with the West introduce uncertainties. If Yerevan successfully diversifies its security and economic partnerships while maintaining pragmatism in relations with Baku and Ankara, the region could move toward stability. However, if Armenia remains isolated or becomes destabilized by internal political turmoil or external pressure from Russia, it could create preconditions for further instability.

c) While Russia's previous traditional influence has waned, it still remains a significant player in the region. If Moscow perceives its diminishing role as a strategic loss or retreat, it may take selective actions either politically or through aggressive means to reassert its control or dominant role. The Kremlin's response to Armenia's Western-leaning policies and its approach to Azerbaijan-Turkey cooperation will be crucial in shaping future regional dynamics.

d) Turkey has emerged as a dominant power alongside Azerbaijan, advocating for economic integration and regional connectivity projects. While this could bring economic benefits, Iran remains wary of geopolitical shifts near its border with Armenia (rejection of the "Zangezur Corridor" project) and may surely act to counterbalance and deter Azerbaijani-Turkish

dominance. A regional competition between three actors could either fuel tensions or encourage a new framework of diplomatic engagement.

e) The EU and the U.S. have expressed an intensified interest in promoting stability in the South Caucasus, particularly through economic initiatives and diplomatic mediation. However, their influence is limited compared to regional actors. The effectiveness of Western diplomacy will depend on its ability to offer Armenia viable alternatives while ensuring Azerbaijan remains engaged in constructive dialogue rather than military solutions. The EU civilian mission plays a crucial role in diplomatically deterring any aggression on the Armenia-Azerbaijan border and effectively monitoring the situation on the ground.

The evolving balance of power in the South Caucasus has far-reaching implications:

- *Energy Security*: The region's role as a critical energy corridor linking the Caspian Sea to Europe has gained prominence amid the global energy crisis.
- *Regional Stability*: Azerbaijan's posture after the 2020 Nagorno-Karabakh war, as well as its invasion into Armenia's sovereign territory, the development of fake and dangerous narratives (about Western Azerbaijan) toward Armenia, persists in creating tensions between the two neighboring countries. The biased involvement of some external actors risks perpetuating instability.
- *Geopolitical Competition*: The South Caucasus exemplifies the broader competition between regional and global powers, reflecting shifting alliances and strategies.

If regional actors prioritize diplomacy, economic cooperation, and confidence-building measures, the new balance of power could undoubtedly create a more stable South Caucasus. New infrastructure development, trade routes, and regional energy project initiatives could serve as stabilizing factors. However, if old enmities resurface, external actors compete aggressively for influence, or one side feels itself in a deadlock, instability could persist. Ultimately, regional stability will not be determined solely by military outcomes but by the willingness of regional leaders to pursue pragmatic policies, address historical grievances, and embrace economic interdependence. The upcoming years will reveal whether the region can transition from a history of conflict to a future of cooperation, or whether new tensions will emerge from the shifting power dynamics.

The region's future stability will depend on the capacity of both local and external actors to prioritize dialogue and sustainable development over confrontation.

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