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Purchasing Power: The Effects of Foreign Investment on Political Development in Kazakhstan

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PURCHASING POWER: THE EFFECTS OF FOREIGN INVESTMENT ON POLITICAL DEVELOPMENT IN
KAZAKHSTAN

PURCHASING POWER: THE EFFECTS OF FOREIGN INVESTMENT ON POLITICAL DEVELOPMENT IN
KAZAKHSTAN

A thesis submitted in partial fulfillment
of the requirements for the degree of
Master of Arts in Political Science

By

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Harding University
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ABSTRACT

This thesis examines the effects of foreign direct investment on Kazakhstan's political growth. Kazakhstan's transition to a market economy was plagued by corruption, and heavy investment in the oil industry generated resource dependency concerns. The regime later began to exert control over the oil industry through renegotiated contracts and legislative changes. This enriched and empowered the regime. As a result, Kazakhstani president, Nursultan Nazarbayev, was able to consolidate control over the state by employing "soft authoritarian" tactics and by rewarding political supporters. The regime was able to employ these tactics because of the wealth that foreign investment created. Thus, control over the investment-friendly oil industry allowed the regime to strengthen its hold over Kazakhstan, limiting opportunities for meaningful political reform.

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to the Graduate Council.

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DEDICATION

This thesis is dedicated to my family for browbeating and supporting me throughout this endeavor. Now you don't have to ask me when I'll be finished.

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Chapter 1: Introduction

Kazakhstan achieved astonishing levels of growth following independence. In spite of poor conditions that existed after the collapse of the Soviet Union, the state would become Central Asia's "most stable" economy.¹ Economic reforms created conditions helped draw foreign investment, which encouraged growth. For example, privatization enabled to state to draw over USD 2 Billion in foreign direct investment, FDI, by 2001. The majority of this investment was used to develop the state's oil reserves. This investment, in addition to higher oil prices, was the primary cause of the state's economic growth.² This growth helped Kazakhstan prosper, yet resource revenues also affected political development. The governing regime now actively participates in the oil industry. Political elites were empowered during this process and have used this clout to consolidate their hold over political life. Thus, oil revenues have contributed to autocratic behaviors among political leaders in Kazakhstan, which has limited political development.

The regime earned revenues through participation in the oil industry and was able to use this participation to expand its control over the state. Interaction with the oil sector allowed the regime to control the state's most lucrative industry and to manage foreign entry into the state. Such developments strengthened the regime's control over this vital industrial sector. Important steps in this process were the creation of a national oil company, NOC, and regulatory reforms that enhanced state oversight of the oil industry. Creation of a NOC allowed the regime to create a role for itself within the oil industry, while modified laws and tax codes allowed the regime to extract revenues from

¹ Levent Koch and M. Ali Chaudary, "Economic Transformation of Kazakhstan: Evidence from Liberalization Reforms," *Journal of Academic Studies* (2002): 145.

² Richard Pomfret, "Kazakhstan's Economy since Independence: Does the Oil Boom Offer a Second Chance for Sustainable Development," *Europe-Asia Studies* 57 (September 2005): 867; Koch and Chaudary, 143.

participating MNCs.³ This participation enabled the regime to enrich itself and strengthen its control over the national oil industry. Such developments have also influenced political development in Kazakhstan.

The regime was able to use increased revenues to expand its control over political life in Kazakhstan. The regime had already displayed authoritarian instincts, yet resource wealth allowed government officials to forego traditionally repressive tactics. Accordingly, scholars suggested that governments that were able to attract FDI were able to strengthen their political position, although investment only contributed to autocratic behavior in regimes that already displayed such leanings.⁴ It is also significant that the regime began to adopt means of persuasion and image-making to control the public sphere instead of resorting to overt repression. Others speculated that increased revenues enabled the regime to deploy more subtle tactics of control.⁵ Such findings indicate that prosperity enabled the regime to find more effective means of maintaining control over political life in Kazakhstan.

The regime's increased participation in the oil industry also contributed to corruption in Kazakhstan. For example, observers noted that nearly USD 500,000 in "privatization bonuses from foreign companies," who were in negotiations to enter the state, had completely vanished. Likewise, journalists have suggested that as much as twenty percent of the "country's wealth is believed to have ended up in Swiss bank accounts."⁶ Such accusations of embezzlement imply that Kazakhstan features a non-transparent government. These tendencies were likely to have been exacerbated by oil revenues.

³ Rudiger Ahrend and William Tompson, "Caspian Oil in a Global Context," *Transitional Study Review* 14 (2007): 172; Political Risk Services, "Kazakhstan: Country Conditions, Investment Climate," *Political Risk Services Group* (May 2005), 3.

⁴ Oksan Bayulgen, "Foreign capital in Central Asia and the Caucasus: Curse or blessing," *Communist and Post-Communist Studies* 38 (2005): 52.

⁵ Edward Schatz, "Transitional image making and Soft Authoritarian Kazakhstan," *Slavic Review* 67 (Spring 2008): 50-52; Bayulgen, "Foreign capital in Central Asia and the Caucasus," 50.

⁶ Wojciech Ostrowski, *Politics and Oil in Kazakhstan* (New York: Routledge, 2010), 86; Lutz Kleveman, *The New Great Game: Blood and Oil in Central Asia* (New York: Grove Press, 2003), 81.

Scholars found that access to revenues often gave autocratic rulers incentive to retain their position.⁷

Kazakhstan is unlikely to achieve significant political development until these issues have been resolved.

Background

It must be noted that the regime's ability to influence political development, as described above, slowly developed after the state achieved independence. Pomfret observed that Kazakhstan was mired in a recession, in which the national GDP declined by 40 percent between 1991 and 1995. Indeed, the national economy did not begin to recover until 1999.⁸ The regime was willing to offer substantial concessions in order to attract investment during this period. For example, during negotiations with MNCs, the regime provided substantial contractual guarantees that it would later attempt to nullify, claiming MNCs had defrauded Kazakhstan.⁹ While the state would later be able to establish control over these corporations, the state was initially required to offer incentives to attract capital. The regime's ability to overcome these setbacks allowed the regime to justify its future consolidation. Understanding the conditions that Kazakhstan faced following independence is crucial to explaining its subsequent actions against this industry.

As previously noted, Kazakhstan faced a variety of challenges after it achieved independence. Use and construction of pipelines that carried Kazakhstani oil illustrate the nature of these problems. Examination of pipeline policies is indicative of the issues that plagued the regime. Kazakhstan does not border an externally accessible body of water and export arrangements were only viable if Kazakhstan remained on good terms with its neighbors. Scholars thus observed that the regime encouraged "regional integration" and accommodated the policies of critical foreign allies who were active in the

⁷ Oksan Bayulgen, "Facing the dilemma of capitalism: the case of Azerbaijan," *Central Asian Survey* 22 (June/September 2003), 216.

⁸ Pomfret, 860, 862.

⁹ Ahrend and Tompson, 170, 172; the state would later implement policies "it had previously been too weak or inexperienced to uphold."

region.¹⁰ Export arrangements reflected a similar spirit of cooperation. For instance, the Caspian Pipeline Consortium's pipeline, CPC, connects to the Tengiz field, crosses Russian territory and also connects Chinese fields, providing multinational access to the state's oil.¹¹ The state's need to accommodate multiple interests in developing export lines demonstrated that Kazakhstan's economic viability was dependent on maintaining positive relationships with its neighbors.

Kazakhstan's desire to maintain positive relationships with its neighbors was also designed to help the state avoid dependence on Russia. The CPC pipeline was intended to reduce the state's reliance on the Russian-made Transneft pipeline that is owned by Transneft, itself owned by Russia. This company engaged in "monopsonistic practices," including inequitable "route allocations," and random pricing measures.¹² Kazakhstan also utilizes the Baku-Ceyhan pipeline, BTC, which crosses the Caucasus to Turkey. American and some Kazakhstani officials favor this pipeline as it does not cross Russian territory. Others favored a pipeline that crossed the Caspian into Iran. Kazakhstani officials viewed this as fiscally and "economically sensible," yet American political concerns prevent this from becoming a viable alternative.¹³ These projects and the geopolitical interests they entail demonstrated that the regime intended to develop positive relationships with the international community, while avoiding dependence on Russia.¹⁴ Yet the constraints of developing relationships also highlighted the challenges that Kazakhstan faced after achieving independence.

Foreign direct investment

Such conditions shaped Kazakhstan's ability to export its oil. Yet the state required a considerable amount of investment in order to access these resources. Kazakhstan was not guaranteed

¹⁰Fiona Hill, "Whither Kazakhstan," *the National Interest* (October 2005): 6; page numbers correspond to a PDF printout.

¹¹Pomfret, 868.

¹²Pomfret, 868, 867.

¹³Lutz Kleveman, *The New Great Game: Blood and Oil in Central Asia*, (New York: Grove Press, 2003), 76, 90-92.

¹⁴Hill, 6.

such investment and made concessions in order to attract the necessary funding. These compromises helped Kazakhstan, yet other factors also enabled the state to recruit investors. A review of the conditions that draw investment can explain Kazakhstan's success. Some, citing Dunning's *"International production and the multinational enterprise,"* observed that a multinational corporation, MNC, will invest in a state based on advantages of entering that state. A corporation that encountered favorable conditions would be more likely to invest. For example, an "ownership advantage" refers to a production model or resource that allows an international corporation to operate more efficiently than others in that state. Such advantages allow an MNC to capture benefits or capitalize on "firm-specific motivations" that make investment advantageous.¹⁵

Li and Resnick made similar observations and extended Dunning's hypotheses. They observed that Dunning's "location-specific" advantages helped developing states attract investment. Commodities including raw materials, a large supply of labor, and appropriate economic policies helped states recruit investors.¹⁶ Natural resources or other contextual features also enable a state to attract foreign investment. Firms also invest abroad when doing so allows them to capture a greater share of a market. Thus, the natural features of a state represent a major factor in drawing investment.

A state's investment climate may also shape a corporation's decision by mitigating foreign concerns over domestic behavior. Firms encounter "political risks" created by the potential for host regimes to appropriate corporate property. This led scholars to conclude that governments capable of mitigating such risks draw investment by reducing "costs of internalizing production."¹⁷ Li and Resnick observed that a state which could guarantee "favorable regulation, preferential treatment...and sound

¹⁵ Nathan M. Jensen, "Democratic Governance and Multinational Corporations: Political Regimes and Inflows of Foreign Direct Investment," *International Organization* 57 (Summer 2003): 591; favorable conditions included an "ownership advantage," "locational advantage," and an "international advantage."

¹⁶ Quan Li and Adam Resnick, "Reversal of Fortunes: Democratic Institutions and Foreign Direct Investment Inflows to Developing Countries," *International Resources* 57 (Winter 2003): 179.

¹⁷ Jensen, 592.

property rights protections” would be an ideal location for investment.¹⁸ Governments willing to offer such assurances were more likely to attract foreign investment.

Effects of FDI on political development

The effect of FDI often varies according to the sector receiving investment. Scholars found that changes in bargaining strength between a host-state and an MNC could be analyzed according to the industrial sector receiving investment. They found that investment in extractive industries often led to a shift in negotiating leverage in favor of host-states. After a multinational had financed infrastructural development, host-states were able to gain project management capabilities within the industry, allowing the state to maintain production without assistance from the MNC.¹⁹ These conditions would suggest that investment in extractive industries can enable governments to develop the capacity to operate autonomously within the sector. This would also imply that states with extractive industries can develop the capacity to demand concessions from an MNC as a result of extractive sector development.

Others who examined the impact of investment suggested that financial growth may contribute to corruption in states that featured traditional patronage systems. It was also observed that FDI may lead to corruption when investment rapidly enters or exits a state.²⁰ Ross noted that resource revenues enabled a state to placate social groups through generous spending policies and reduced taxation, which helped isolate a government from criticism.²¹ It is equally significant that discovery of oil in Chad contributed to the deterioration of that state’s political climate, and that the state’s president utilized authoritarian means to capture the states’ resource revenues.²² Such conditions indicate that

¹⁸ Li and Resnick, “Reversal of Fortunes,” 180.

¹⁹ Stephan Haggard, *Pathways from the Periphery: The politics and growth of newly industrializing countries* (Ithaca NY: Cornell University Press, 1990), 220-21.

²⁰ Bryan W. Husted, “Wealth, Culture, and Corruption,” *Journal of International Business Studies* 30 (Second Quarter, 1999): 343; Robertson and Watson, 387-89.

²¹ Michael L. Ross, “Does Oil Hinder Democracy,” *World Politics* 53 (April 2001): 332-35.

²² Matthew S. Winters and John Gould, “Betting on Oil: The World Bank’s Attempt to Promote Accountability in Chad,” *Global Governance* 17 (2011): 235-37, 239.

investment, in addition to the revenues investment generates, may lead non-democratic governments to exploit their position in order to pursue personal or political gains.

Conditions in Kazakhstan indicate that FDI had a negative impact on the state's political climate. Scholars who examined the Kazakhstani economy found state institutions to be non-transparent. Others who examined the privatization process, in which the state's "largest factories" were privatized through "individually negotiated" agreements, found the process to be incredibly corrupt.²³ It was also observed that after the oil sector began to develop, political leaders utilized techniques of undermining opposition figures without resorting to overtly oppressive measures.²⁴ Such conditions confirm that the institutional quality of the Kazakhstani government has declined. These developments can be attributed to FDI, and may indicate that FDI, and the revenues it generated, had a negative impact on Kazakhstan.

Corporate interaction with a host regime

The relationship between investors and the host government is also a crucial factor in promoting economic development. For example, security against nationalization is a primary concern for investors. Bayulgen observed that, having invested in a state, corporations actively petition a regime to address their concerns, especially those regarding consistent regulation and protection of property. Indeed, demand for these conditions is such that investors may be unconcerned with the state's broader political climate.²⁵ Investors also sought protection against tax code revision and similar forms of regulation. Thus, for investors in Kazakhstan, the "crucial factor" was the regime's willingness to make these guarantees.²⁶ The government's ability to provide this type of legal protection represented a vital component of the regime's ability to attract investment.

Corporate interest in political development is generally limited. Gulbrandsen and Moe observed that collaborative organizations in Kazakhstan, which featured investing corporations and members of

²³ Olcott, 139.

²⁴ Schatz, 50-52.

²⁵ Bayulgen, "Foreign capital in Central Asia and the Caucasus," 54.

²⁶ Ahrend and Tompson, 170.

the regime, were only willing to challenge the government when issues that threatened investment-related operations arose.²⁷ International organizations sought to pressure oil corporations into playing a larger role in promoting transparency in Kazakhstan, yet corporations have resisted such activities. Indeed, Gulbrandsen and Moe found that corporations did not consider it to be their responsibility to critique government use of resource revenues. This led the authors to categorize joint corporate efforts as “the ‘law of the least ambitious,’” in which the most inactive organization shapes the scope of government pressure.²⁸ Such conditions suggest that concern over investments can limit corporate willingness to call for reforms.

Gulbrandsen and Moe also observed that, while corporations may face international calls to promote transparency, such efforts may be met with hostility by the host state, suggesting that contract termination and other repercussions may reduce calls for transparency.²⁹ Bayulgen observed that investors may favor a degree of plurality, as it allows them to utilize the political process to petition the state, yet such requests are likely to be confined areas affecting their investment.³⁰ Corporate inattention to broader political issues may have shaped the regime’s decision-making process, allowing it to expand its control over the state.

Such actions can reinforce authoritarian tendencies. Bayulgen noted that authoritarian regimes provided security that allowed select economic sectors to prosper, yet also contributed to authoritarian persistence by enriching state leaders. For example, revenues provide autocrats with motivation to retain their office, which provides further access to resource revenues.³¹ Baylugen also suggested the ability to attract investment helped legitimize state leaders. Continued investment may imply approval

²⁷ Lars H. Gulbrandsen and Arild Moe, “Oil Company CSR Collaboration in ‘New’ Petro-States,” *Journal of Corporate Citizenship* 20 (Winter 2005): 60.

²⁸ Gulbrandsen and Moe, 55, 62.

²⁹ Gulbrandsen and Moe, 60.

³⁰ Bayulgen, “Foreign capital in Central Asia and the Caucasus,” 54.

³¹ Oksan Bayulgen, “Facing the dilemma of capitalism: the case of Azerbaijan,” *Central Asian Survey* 22 (June/September 2003), 216.

from the international community and can improve a leader's public image.³² Such conditions suggest that investment influenced political development in Kazakhstan by indicating foreign support for President Nazarbayev and by creating incentive to retain political power.

Effects of oil revenues on political development

Scholars characterized a state whose natural resources attract high levels of revenue as a "rentier state." Such states accumulate revenue that is supplied by international investors. Revenue under these conditions is created by a minority; most citizens are only involved in the consumption of rents. Such wealth also allows governments to downplay calls for political reform. For example, greater resources may allow a government to reduce taxes, which may also reduce demands for inclusion in the political process.³³ Revenues generated by natural resources may therefore enable a government to placate and control the public. This type of influence may also limit calls for political reform.

The political context of Kazakhstan fits this description. OECD reports indicated that Kazakhstan collected "the lowest general government revenue and expenditure as a share of GDP...on 2001 returns." In addition, natural resources attracted nearly USD 30 Billion in 2004.³⁴ This suggested that Kazakhstan featured some of the characteristics of a rentier state. Such conditions also indicate political decision making was influenced by resource revenues. Thus, the abundance of resource revenues may have also influenced the regime's political behavior, which effected political development.³⁵

The regime was also able to extract rents through manipulation of its relationships with foreign oil companies. This was achieved through legal modifications and enforcement of unrealistic laws. Analysts found that MNCs found it necessary to guard their investments against perpetual legal and

³² Bayulgen, "Foreign capital in Central Asia and the Caucasus," 52; quoting Armijo, "Financial Globalization and Democracy in Emerging Markets," 2001.

³³ Ross, 329, 332.

³⁴ Kaser, 466, 465; Political Risk Services, 1.

³⁵ Ross, 330.

regulatory reforms.³⁶ The regime also passed legislation in 2003 that made contractual agreements retroactively susceptible to revision, including additional requirements that forced onto corporations. Additional changes included multinational agreements which effected the development of “goods subject to excise duties.”³⁷The ability of the regime to enforce these developments may have assisted the regime’s efforts to develop control over the national oil industry.

The regime’s ability to develop control over the state’s most important economic sector suggests that the regime had consolidated its hold over important political institutions. Collection of resource revenues enabled the regime to establish this level of control. Ross observed that the link between resource-generated revenues and political reform was negative, suggesting that governmental control increased as resource revenues increased. Bayulgen also suggested that resource revenues had a tendency to “make states less democratic.”³⁸Thus, exploitation of Kazakhstan’s natural resources could enable autocratic behavior among national leaders. Such effects are possible in any state with natural resources, yet Pomfret observed that the impact of revenues on political development was often shaped by institutional context: Oil revenues that enriched states without a democratic background contributed to abuse of political power.³⁹ Political conditions as Pomfret described exist in Kazakhstan. The state’s ability to collect resource revenues helped empower Kazakhstan’s political elite.

Oil drove Kazakhstan’s economic development.⁴⁰Yet these resources are also finite, and depletion will have serious ramifications on the state’s economy. Continued dependency on oil reserves will also magnify potential consequences. Pomfret observed the state was unsuccessful in its attempts to diversify the national economy following independence. He claimed economic sectors unconnected

³⁶ Political Risk Services, 4.

³⁷ Ahrend and Tompson, 174; the authors observed that such changes were also designed to prevent overdevelopment.

³⁸ Ross, 328; Bayulgen, “Foreign capital in Central Asia and the Caucasus,” 67.

³⁹ Pomfret, 872.

⁴⁰ Pomfret, 860; “the oil and minerals sector” drove economic growth after the 2000 economic “boom.”

to the oil industry were unsuccessful in transitioning to an open economy.⁴¹ Failure to achieve diverse economic growth will have a devastating effect on Kazakhstan after its resources are depleted.

Connection to theory and organization of research

This thesis expounds upon the complex relationship between foreign investment and political development. Scholars who examined this connection noted investment shapes the “political fortunes” of national leaders and, in Central Asia, contributed to autocratic consolidation through neglect of non-government industries and by creating incentive to maintain status-quo relationships.⁴² Others who examined the impact of foreign investment on corruption have found that the pace with which investment enters the country strongly contributes to an uptick in instances of corruption. As corruption involves misuse of public means to advance a private or personal goal, it is considered to have a negative impact on political development.⁴³ This thesis contributes to these studies by highlighting the mechanisms which allowed the Nazarbayev regime to consolidate power. It is significant that, while the president had displayed authoritarian leanings, his control over state institutions increased after MNCs began to invest in Kazakhstan.

This thesis also examines the impact of oil revenues on political development. The link between resource wealth and political development has been well documented. Ross suggested that “oil inhibits democracy even exports are fairly small, particularly in poor states.” This development is manifested through a “rentier effect,” which allows oil-wealthy governments to avoid extensive taxation and to reward political support, which reduces demand for political liability.⁴⁴ Kazakhstan has been able to extract these rents. Yet it should be noted that foreign investment may also have the same impact as oil revenues, with regards to political development. Ross also noted that a “rentier state” collected

⁴¹ Pomfret, 869.

⁴² Bayulgen, “Foreign capital in Central Asia and the Caucasus,” 50.

⁴³ C.J. Robertson and Andrew Watson, “Corruption and Change: The Impact of Foreign Direct Investment,” *Strategic Management Journal* 25 (April 2004): 387-89, 386.

⁴⁴ Ross, 356, 327-28.

revenues paid by international contributors and are only captured by the minority of a population, the majority participating in “distribution or utilization of” rents.⁴⁵ This description can also describe the state’s ability to attract foreign investment. This thesis will demonstrate that foreign investment in Kazakhstan has influenced political development in a manner similar to oil revenues.

The chapters of this thesis have been segmented in order to demonstrate how oil revenues influenced political development in Kazakhstan. Chapter two addresses Kazakhstan’s economic development following independence. The regime implemented structural reforms during this period that helped attract FDI and played a major role in promoting growth. The regime’s ability to overcome various socio-political challenges also provided a foundation for the state’s growth. Yet these reforms only encouraged investment in the oil industry. Kazakhstan can thus be characterized as a resource dependent state. The chapter will conclude with the observation that reforms primarily benefitted the oil industry, and that this industry was primarily responsible for the state’s economic success.

Chapter three will examine the regime’s interaction with the oil industry. Kazakhstan implemented several reforms and made initial concessions in order to attract investment. However, the regime would later take steps to regain control over the sector through changes to legal and regulatory provisions. The regime also created a national oil company to assist in this process, which was intended to facilitate state participation in the oil industry.⁴⁶ This participation also influenced political life in Kazakhstan by empowering national leaders and bureaucrats overseeing the oil industry and encouraging corruption. The chapter demonstrates that oil revenues enabled the regime to reward supporters while preventing the development of opposition groups. This enhanced the regime’s autocratic tendencies.

⁴⁵ Ross, 329.

⁴⁶ Ahrend and Tompson, 172.

Finally, chapter four will examine the regime's ability to consolidate political power over the state. Oil revenues facilitated autocratic tendencies that the regime had already begun to display. Specifically, revenues enabled the regime to use non-repressive tactics to establish control over the state. Scholars found that the regime had learned to cultivate public opinion against opposition figures.⁴⁷ Corruption among elites also limited opportunities for political development. Members of the president's family have been granted influential posts in important sectors of the national economy.⁴⁸ This concentration of political power can be considered corruption and may have prevented opposition groups from developing in business sectors. The chapter thus demonstrates that oil revenues allowed the regime to control important facets of political life in Kazakhstan, further cementing its rule.

Such conditions indicate that oil revenues had a significant impact on political development. Resource revenues led to modification of autocratic behaviors and contributed to corruption. Policies designed to expand Kazakhstani control over the oil industry also enriched the regime and ensured that its supporters occupied influential posts within the national economy.⁴⁹ It is unlikely that, under these conditions, any domestic opposition group will emerge to challenge the Nazarbayev regime.

⁴⁷ Schatz, 50-52.

⁴⁸ Andersen, 146; Ostrowski, 49.

⁴⁹ Franke, et. al., 114-15.

Chapter 2: Economic Development in Kazakhstan

Introduction

Kazakhstan achieved a remarkable level of economic growth since gaining independence. Having emerged under difficult conditions, the state's development as a market economy is a considerable achievement.⁵⁰ The regime used this growth to assume control over development projects in the oil industry. The regime achieved this control through legislative changes, such as a law that granted the government rights to shares in development projects before the shares are marketed. This law helped the regime undermine foreign investors.⁵¹ Although these changes empowered the government, such behavior may discourage future investors from entering the state and could damage Kazakhstan's long term economic viability.

The state achieved a remarkable level of growth in spite of major problems following independence. Indeed, Kazakhstan has been described as being more developed than other Soviet republics. Much of Kazakhstan's subsequent success can be explained by the state's oil resources. Scholars claim that oil and gas industries are responsible for almost "80 percent of [Kazakhstan's] industrial output."⁵² Yet such resources did not guarantee a smooth transition from Soviet rule. The state experienced major shortcomings after the collapse of the Soviet Union and these issues have affected the pace of Kazakhstan's economic growth.⁵³

The state achieved this growth through a combination of legislative reforms, privatization, and accompanying foreign direct investment, or FDI. For example, a 1995 law intended to develop the banking industry gave the government oversight and allowed the state to move assets away from

⁵⁰ Pradeep Agrawal, "Economic Growth and Poverty Reduction: Evidence from Kazakhstan," *Asian Development Review* 24 (2007): 91; Levent Koch and M. Ali Chaudary, "Economic Transformation of Kazakhstan: Evidence from Liberalization Reforms," *Journal of Academic Studies* (2002): 145.

⁵¹ Wojciech Ostrowski, *Politics and Oil in Kazakhstan* (New York: Routledge, 2010): 146-47.

⁵² Fiona Hill, "Whither Kazakhstan," *the National Interest* (October 2005): 6, 8; page numbers correspond to PDF printout.

⁵³ Yerbol Orynbaev, "Kazakhstan's Greater Competitiveness as a Prerequisite of Development and a New Quality of Life," *American Foreign Policy Interests* 28 (October 2006): 393.

problematic areas.⁵⁴ This reform was crucial to the development of a viable banking sector. Likewise, privatizations attracted nearly USD 7 Billion in the mid-1990's and helped the state modernize its economy.⁵⁵ These policy components were essential to Kazakhstan's economic development.

Explanations of the state's success must consider how these elements helped the regime create growth.

Kazakhstan's natural resources were also essential to its economic growth. Interest in these resources began before the Soviet Union collapsed: Chevron and others agreed to invest almost USD 20 Billion to develop these fields.⁵⁶ New fields were also discovered after independence. The Kashgan field is estimated to contain several billion barrels worth of oil and may eventually increase the state's export capacity.⁵⁷ Kazakhstan's development cannot be explained apart from these resources, and such assets fueled the state's economic growth.

This development was not without consequences. The government has begun to enact tougher polices that limit corporate earnings. For instance, the regime passed legislation that granted it the right to purchase shares in a project before it is marketed for sale.⁵⁸ Domestic participation in resource development is not inherently troubling; however, this behavior is problematic because control of these industries was granted to privileged citizens with ties to the regime.⁵⁹ This raised concerns of about corruption. Government treatment of foreign investors was also uneven. Scholars observed the

⁵⁴ Alexandr Akimov and Brian Dollery, "Financial System Reform in Kazakhstan from 1993 to 2006 and its Socioeconomic Effects," *Emerging Markets Finance and Trade* 44 (May-June 2008): 83.

⁵⁵ Agrawal, 92; Richard Pomfret, "Kazakhstan's Economy since Independence: Does the Oil Boom Offer a Second Chance for Sustainable Development," *Europe-Asia Studies* 57 (September 2005): 864.

⁵⁶ Political Risk Services, "Kazakhstan: Country Conditions, Investment Climate," *Political Risk Services Group* (May 2005): 8.

⁵⁷ Lutz Kleveman, *The New Great Game: Blood and Oil in Central Asia* (New York: Grove Press, 2003), 75.

⁵⁸ Ostrowski, 146.

⁵⁹ Anne E. Peck, "Industrial Privatization in Kazakhstan: The Results of government Sales of Principal Enterprises to Foreign Investors," *Russia and East European Finance and Trade* 38 (New York: Grove Press 2003), 86.

government had inconsistently applied tax laws and was “blatantly unfair” to foreign corporations in other instances.⁶⁰ Such conditions could easily prevent future investors from entering Kazakhstan.

Such “government intervention” may further damage the state’s ability to attract investment.⁶¹ Other factors may also hamper economic growth: the state is in danger of becoming resource dependent. Scholars have speculated that the state may be vulnerable to Dutch disease, which could limit growth in other economic sectors.⁶² Thus, the growth that Kazakhstan achieved is not a guarantor of stability. The state has reached impressive levels of development, but deliberate alteration of investment conditions and resource dependency may undermine these achievements.

Independence and initial setbacks

The collapse of the USSR imposed several challenges on Kazakhstan and contributed to the state’s initial economic difficulties. As with most Soviet republics, the Kazakhstani economy became stagnant during the 1980’s and shrank in the 1990’s.⁶³ Kazakhstan was also a component of the larger Soviet economy and some sectors produced a small number of value-added products, while others manufactured goods “in excess of local needs.” Other scholars observed that Soviet collapse damaged Kazakhstan’s trade patterns, which “had accounted for more than 90 percent of the country’s trading volume.”⁶⁴ This crippled the national economy. Such conditions forced Kazakhstani leaders to reorganize the national economy while simultaneously undergoing political transitions. Such challenges posed serious challenges to economic growth.

Kazakhstan was poorly equipped to exploit its resources. The national economy had been based on agriculture rather than natural resources. Indeed, agriculture accounted for 42 percent of Kazakhstan’s economy while other sectors, including extractive industries only accounted for 21 percent

⁶⁰ Political Risk Services, 3.

⁶¹ Political Risk Services, 1.

⁶² Pomfret, 871; Kleveman, 89.

⁶³ Akimov and Dollery, 82.

⁶⁴ Agrawal, 91; Orynbaev, 393.

of the national economy.⁶⁵ Moreover, Soviet integration required Kazakhstani oil refineries to process Siberian crude, while refineries in Russia processed Kazakhstani oil.⁶⁶ Thus, the collapse of the USSR had diminished Kazakhstan's ability to process its own resources. Overcoming the setbacks caused by Soviet integration was a significant accomplishment for the Kazakhstani government.

The collapse of the Soviet Union also carried major social ramifications. Crime and corruption were rampant during this period, yet the most pressing issue was the flight of non-ethnic citizens.⁶⁷ Russian minorities in Kazakhstan became a politically sensitive issue for the regime. Russian citizens were among the "educated and technologically skilled [members of the] population." Their status was a point of contention between the state and Russia. The regime could not neglect these citizens, yet the president also needed the support of ethnic Kazakhs in order to bolster his political authority. This situation was partially resolved by Russian emigration and through easily converted citizenship between Kazakhstan and Russia. Yet this also resulted in a loss of skilled workers among national elite.⁶⁸ The collapse of this human infrastructure also presented an early challenge to the state.

Investment in Kazakhstan was not guaranteed. The state lacked infrastructure that other former Soviet republics possessed. Production deficiencies were also exposed as the state began to encourage investment, and Kazakhstani industries required a significantly larger financial commitment in order to maintain operations. Scholars writing at the outset of this process observed that "the quality of finished products was poor..." and that machinery in Kazakhstani factories was rarely functional. These

⁶⁵ Akimov and Dollery, 82; "mining and energy sectors" accounted for 21 percent of the national economy.

⁶⁶ Pomfret, 861.

⁶⁷ Orynbaev, 393.

⁶⁸ Martha Brill Olcott, *Kazakhstan: unfulfilled promise*, (Washington DC: Carnegie Endowment for International Peace, 2002), 53, 43, 57; Pomfret, 861; ethnic Germans were also part of this emigration.

shortcomings also led government officials to compromise over the terms of investment agreements.⁶⁹

Indeed, Olcott claimed the state of Kazakhstani infrastructure was so dilapidated that government officials were unaware of “how technologically obsolete” national industries were.⁷⁰ Kazakhstan’s ability to achieve economic growth becomes increasingly impressive in light of these structural deficits.

Market Reforms

Kazakhstan eventually matured into an economically viable state. This development was partially created by successful legislative changes. These efforts oriented the national economy towards global markets and helped the government manage the transition to a market economy. These reforms also created the conditions that encouraged foreign investment. Yet such growth also improved the lives of Kazakhstani citizens. According to scholars, the effectiveness of legislative reforms was evident in “the fact that the ratio of financial assets...held by the public to GDP has increased.”⁷¹ A review of these legislative changes helps illuminate the mechanisms of Kazakhstan’s growth.

Financial sector reforms were a major component of Kazakhstani success. A 1995 program included initiatives that applied greater oversight to national banks and allowed the government to foreclose on “non-viable banks.” The law also permitted the regime to move “non-performing loans” away from problematic banks. Reforms included regulations against lending practices, insider trading, and “reserve requirements,” among other efforts.⁷² Such reforms were important because they created a financial sector that met international standards. Scholars claim that such reforms were a crucial step in developing “a well-functioning banking system.”⁷³ Such reforms were also an important step in cultivating an image of Kazakhstan as having a stable investment climate.

⁶⁹ Douglas Bartley and Michael Minor, “Pitfalls of Privatization in Kazakhstan,” *Business Forum* (Winter/Spring 1994), 32-33; the 1995 law was the “Program for the Reform of the Banking Sector.”

⁷⁰ Olcott, 144.

⁷¹ Peck, 49-50; Bartley and Minor, 33.

⁷² Akimov and Dollery, 83.

⁷³ Political Risk Services, 6; Agrawal, 92.

Liberalization continued throughout 1995 and the government eliminated “export quotas and licensing requirement[s].” The state also introduced anti-trust measures and a modified tax code in the same year. The regime then passed a “Deepening of Reforms” program in 1996 that addressed “macro-economic stabilization, structural-institutional transformations,” and sought to cultivate crucial economic areas.⁷⁴ These reforms were important factors in liberalizing the economy. Drafting a new constitution was also an important step in this process. Scholars claim the new constitution served as a legal foundation for the reforms that created open markets. The document helped initiate the privatization process and theoretically created “property owners and [laid] the foundation for the middle class.” Thus, the new constitution represented an effort to institutionalize market reforms and provide a foundation for future growth.⁷⁵ These reforms helped the state attract foreign investment and spurred the transition of the national economy.

The Privatization Process

Privatization was essential to Kazakhstan’s economic growth. Allowing national assets to be developed by foreign investors generated revenue for the government and helped the state capitalize on its resources. The state’s ability to attract investors was especially impressive when one considers the lack of organization that initially plagued the state. Analysis of this process also explains how the state achieved economic growth.

Privatization occurred in three stages, primarily between 1991 and 1998, although some companies were sold in 1999.⁷⁶ The first phase of this process was home privatization. The process was carried out using a voucher system. Pomfret claimed that citizens received enough shares to purchase their own homes. However, non-Kazakh minorities unevenly benefitted from this process. Russians and

⁷⁴ Koch and Chaudhary, 139-40; the program also addressed non-economic issues, including security concerns.

⁷⁵ Orynbaev, 393-95.

⁷⁶ Olcott, 136-37.

Uzbeks possessed nicer apartments in the capital because they also held higher paying employment, and therefore received a “better housing allocation.”⁷⁷

The second stage of privatization involved moderately sized factories and industries employing more than 200 workers.⁷⁸ This stage was also based on a voucher format and allowed citizens to purchase shares of enterprises. Kazakhstanis received vouchers which could be used to buy into an Investment Privatization Fund, or an IPF. This system was designed to prevent “excessive fragmentation of ownership.” Yet voucher distribution skewed towards non-urban citizens and tended to favor ethnic Kazakhs. Pomfret claimed the regime intentionally distributed vouchers in this fashion to remedy inequalities that emerged during the first stage. This stage also marked the beginning of efforts to sell portions of state industries to foreign companies. In 1993, the government sold shares of factories producing tobacco, margarine, and other confectionary goods. This generated almost USD 450 million in revenue for the government.⁷⁹ However, investment fund managers unevenly benefitted from this system and became “Kazakhstan’s new economic elite.” This made most citizens skeptical about the privatization process.⁸⁰ Citizens also became skeptical about the privatization process, as the wealthy began to accrue greater resources. Partial privatization later slowed down, and by 1998 was replaced by the sale of entire corporations.⁸¹

The third stage marked the acceleration of the privatization process. Olcott observed that industries “were sold in part or whole” to foreign investors.⁸² Peck found the speed of the privatization process remarkable and claimed the sale of state industries was accomplished in an astonishingly small

⁷⁷ Pomfret, 864.

⁷⁸ Olcott, 137.

⁷⁹ Pomfret, 864; see endnote #3 on p. 873.

⁸⁰ Olcott, 138.

⁸¹ Pomfret, 859, 864.

⁸² Olcott, 139.

window.⁸³ As part of this stage, the government sold operational agreements to foreign investors who were expected to improve production facilities and “market the enterprise’s assets without fully assuming its debt.” The investor was then offered the chance to purchase stock in the plant. Most factories maintained non-productive areas, including child care centers, living complexes and infirmaries. It was assumed plants would generate profits once stripped of these obligations. These agreements enabled the government to modernize industries, and it was hoped these renovated facilities would enable the state to entice further investment.⁸⁴

However, this stage of the process was stained by corruption. Peck expressed concern over the lack of transparency associated with this stage of privatization.⁸⁵ Olcott also expressed reservations over this stage of privatization, characterizing this period of the privatization process as “the most corrupt stage of investment.”⁸⁶ Dealings between investors and the government were closed and details of transactions were not publicized. This led Peck to conclude “bribery and other forms of payment were the norm” during these negotiations.⁸⁷ Such rumors suggest the privatization process was not entirely transparent and provided a troubling insight into the regime’s behavior.

Several contracts were granted to mineral exploitation and processing companies during privatization. Corporations purchased iron ore mines, aluminum, and chromite processing plants. Trans World Group and the Kazakhstan Mineral Resources Corporation, or KMRC, purchased shares in these resource mines and plants, as well as in Bauxite and Coal mines. Oversight conflicts with KMRC later forced Trans World Group to withdraw from the state. These industries were then controlled by KMRC. It was significant the corporation is owned by a bank manager who had business connections to President Nazarbayev. Olcott also suggested Trans World Group fell out of favor with the regime before

⁸³ Peck, 53.

⁸⁴ Olcott, 139.

⁸⁵ Peck, 54.

⁸⁶ Olcott, 139.

⁸⁷ Peck, 54.

it pulled out of Kazakhstan. This led her to claim that maintaining positive relations with the government was crucial to corporate entry into Kazakhstan.⁸⁸ It would also appear that associates of the regime were enriched through their connections, and were rewarded with lucrative opportunities. Such conditions confirm charges of a corrupt during the privatization process.

Interestingly, the privatization process did not meet the government's expectations. Privatization drew nearly USD 7 Billion from late 1995 to late 1996, but many enterprises that were marketed were not purchased. Moreover firms sold between 1996 and 1999 became less productive than industries under state control.⁸⁹ Olcott attributed this problem to these industries being overvalued by the government. Indeed, "less than 5 percent of...large scale industries" had been sold by 1998, although a majority of smaller industries had been privatized by the fall of that year.⁹⁰ Such figures suggest the privatization process attracted investment, but fell short of the government's intentions.

Foreign Direct Investment

Attracting the business of international investors was crucial to the development of the Kazakhstani economy. This was a major objective of the state's privatization process. Olcott claimed "foreign investment goes hand in hand with privatization."⁹¹ Kazakhstan's privatization process can be considered successful because it captured this investment. Between 1995 and 1997, foreign investment in Kazakhstan grew by 37 percent. By 2003, FDI accounted for almost 12 percent of the national economy.⁹² FDI clearly played a role in Kazakhstan's growth. The regime's ability to attract this investment is a crucial explanation of the state's economic success.

Attracting investment forced the state to meet conditions for corporate entry. Corporations were concerned with the size of the national labor market, "physical infrastructure, supplier base,

⁸⁸ Peck, 34-5; Olcott, 140.

⁸⁹ Pomfret, 864; Peck 54.

⁹⁰ Olcott, 140-41.

⁹¹ Olcott, 144.

⁹² Vildan Serin and Elif Yuksel, "Foreign Direct Investment Flows in Kazakhstan: The Role of the Energy Sector," *Journal of Academic Studies* 7 (May-July 2005): 10.

technology support,” and other contextual details within a state. Scholars observed that investment is most likely in states that are politically stable, and with an independent legal system.⁹³ Thus, corporations invest in locations that provide a suitable climate for the development of their investment. States hoping to attract investment must be able to meet these conditions.

Kazakhstan enacted legislative reforms as a way to encourage FDI and was successful in this endeavor. Earlier reforms had allowed the state to attract investment at an accelerated rate. Data from the Kazakhstan National Bank indicated the state garnered as much investment in the first six months of 2001 as it had throughout 2000.⁹⁴ Between 1991 and 2006, rising levels of investment increased the GDP per capita PPP by 166 percent. Unemployment across the country had also declined by 2007.⁹⁵ Such improvement suggests that reforms successfully drew investment. Kazakhstan attracted USD 30 billion in foreign investment in 2005, two-thirds of which was invested by the US.⁹⁶ “Investment in main production assets” also topped USD 16 Billion in 2005, and was a substantial increase over 2004 investment levels.⁹⁷ Such investment significantly enhanced Kazakhstan’s economy.

The state’s non-oil mineral resources also drew investment. The government offered incentives to corporations that invested in such “priority economic sectors.”⁹⁸ During this process, the previously mentioned Trans World Metals group purchased shares in a chromium mine as well as the accompanying processing plant. The firm also purchased shares in an “aluminum smelter in Pavlodar and a ferro-alloy smelter in Aksu.”⁹⁹ The British firm, ISPAT international purchased “Kazakhstan’s only integrated steel mill.” Samsung assumed management of a national copper plant and later bought a

⁹³ Serin and Yuksel, 11.

⁹⁴ Koch and Chaudary, 141.

⁹⁵ Akimov and Dollery, 91; unemployment was “less than 8 percent,” using ERBD data from 2007.

⁹⁶ Michael Rywkin, “Stability in Central Asia: Engaging Kazakhstan,” *American Foreign Policy Interests* 27 (2005): 441.

⁹⁷ Orynbaev, 396.

⁹⁸ Olcott, 147.

⁹⁹ Political Risk Services 10; Olcott, 139.

substantial stake in the same plant.¹⁰⁰ Kazakhstan's mineral resources outside of the oil sector drew investment in their own right.

Other sectors of the national economy attracted investment. In 1993, US tobacco company Philip Morris began investment in Kazakhstan, worth USD 350 Million over five years. The company also produced domestically sold cigarettes, and by 2000 the company had constructed a USD 200 million plant in Southern Kazakhstan. American electrical corporations also invested in Kazakhstan. Between 1996 and 1997, AES purchased several power generating plants in Eastern Kazakhstan. The state also awarded the corporation with "management control of regional electric distribution companies" for the next decade and a half.¹⁰¹ Kazakhstan's gold deposits also generated investment, although these resources did not produce significant yields and created tensions between investing corporations and the state.¹⁰² Thus, Kazakhstan's was able to encourage investment in sectors outside of the oil industry.

Yet many have expressed concern regarding negative ramifications of foreign investment. For example, scholars fear that Kazakhstan has become resource dependent. Pomfret noted that the state's agricultural sector was not profitable throughout the 1990's. He also noted that by 2003, the regime was not able to decide "how the farm sector should be organized" in a free market economy. Likewise, "services sectors" saw their percentage of the national GDP decline "between 1998 and 2002," and observed that "coalmining and metallurgy" also experienced a downturn prior to 1998. Thus, sectors of Kazakhstan's economy declined while the national oil industry continued to develop. Pomfret attributed many of these problems to institutional deficiencies and noted that these problems, in addition to an inefficient "restructuring of existing enterprises," limited opportunities for growth.¹⁰³ Such descriptions

¹⁰⁰ Peck, 35; Samsung bought 40 percent of the plant.

¹⁰¹ Political Risk Services, 9.

¹⁰² Olcott, 166.

¹⁰³ Pomfret, 869-70; the metallurgy sector "stabilized after 1998."

indicate that Kazakhstan's non-oil economy failed to match the oil sector's growth. These conditions expose the state to problems of resource dependency.

The investment process also resulted in ownership consolidation. As foreign investors failed to meet the terms of their contract, the regime sold rights to favored investors. As a result, the state's "minerals sector" is largely dominated by four corporations. For example, Samsung initially controlled a single copper processing plant, yet would later be permitted to purchase failed enterprises across the copper industry.¹⁰⁴ Business deals were also dependent on political patronage. The dealings of Trans World Group became increasingly difficult once a supportive Prime Minister was dismissed from office. The company that assumed management of Trans World's contracts also had connections to President Nazarbayev.¹⁰⁵ This type of business climate can undermine the state's investor-friendly image and raise concerns about corruption. Such conditions may discourage investors from entering the state and has the potential to threaten Kazakhstan's economic growth.

Scholars have expressed concern that the regime may damage its reputation as a positive investment climate, with regards to protections guaranteed by Kazakhstan's legal code. Legislative changes exposed investors to increased taxation. For example, the regime originally passed legislation designed to protect investors from government appropriation of corporate property.¹⁰⁶ Yet others noted current legal codes did not guarantee security against future modifications. Some corporations also faced changes that incorporated current development projects into new tax regimes. This led analysts to characterize development negotiations as non-transparent, noting that investors faced corruption at multiple points within the government.¹⁰⁷ Such problems have the potential to prevent future investment in Kazakhstan. Investors may avoid the state if it continues to modify its legal codes.

¹⁰⁴ Peck, 35-39.

¹⁰⁵ Olcott, 162-63.

¹⁰⁶ Serin and Yuksel, 12.

¹⁰⁷ Political Risk Services, 4-5.

Oil Industry Development

Other sectors contributed to Kazakhstan's growth, yet Kazakhstan's oil resources were the indispensable element in this process. Even President Nazarbayev observed "the oil sector's development became the locomotive of [Kazakhstan's] economic growth." Scholars also claimed that the national economy was defined by resource exploitation.¹⁰⁸ Others observed that Kazakhstan's development was attributable to a rise in the cost of oil, beginning in 1999.¹⁰⁹ Thus, Kazakhstan's economic success is primarily attributable to its sizable oil reserves and the investment they drew.

Foreign direct investment was also crucial to the oil industry's development, and the regime's efforts to attract this funding were equally important. A major step in this process was a 1994 law that established "legal and economic principles" that governed investment and included measures addressing asset securities and conflict resolution. Scholars viewed this as a signal of Kazakhstan's intention to create a stable investment climate. The law was designed to shield investment from state intercession, including "expropriation, changes in legislation," and other interventionist policies.¹¹⁰ It should be noted that such concessions were granted because of the state's pressing need of investment, specifically to repair outdated infrastructure. Yet these policies were successful. As of 2005, nearly 60 percent of the annual FDI that entered Kazakhstan was invested in extractive industrial sectors.¹¹¹

Negotiations for Kazakhstani oil began before the state achieved independence. Olcott observed that Chevron began negotiating a deal to expand production at the "Tengiz oil field in 1990..." The Tengiz field was estimated to contain between six and nine billion barrels of extractable oil, and at the time was

¹⁰⁸ Nursultan Nazarbayev, "Kazakhstan: Economic Force on the Global Frontier," *Foreign Affairs* 86 (January/February, 2007): 114; K. Arystanbekov, "Quality of Kazakhstan's Economic Policy and Balance of Payments," *Problems of Economic Transition* 51 (February 2009): 64.

¹⁰⁹ Hill, 3.

¹¹⁰ Pamela Blackmon, "Divergent paths, divergent outcomes: linking differences in economic reform to levels of US foreign direct investment and business in Kazakhstan and Uzbekistan," *Central Asian Survey* 26 (September 2007): 361; Serin and Yuksel, 12.

¹¹¹ Blackmon, 362; Koch and Chaudhary, 144; Blackmon also observed that this investment was used to develop export pipelines.

Kazakhstan's most productive oil field.¹¹² Chevron later partnered with the Kazakhstani government and other corporations to create TengizChevrOil and signed a forty year agreement to invest roughly USD 20 Billion into these fields. The conglomeration also procured a stake in the Caspian Pipeline Consortium, or CPC, a major pipeline that transports this oil to the Black Sea.¹¹³ The size of such resources helped draw investors and drove economic development.

Tengiz was not the only major oil field in Kazakhstan's portion of the Caspian Sea. The Kashgan field was also estimated to hold nearly "30 billion barrels" of oil and proved significant enough to provoke estimates of export levels comparable to Saudi Arabia. Yet negotiations over this field proved contentious. Questions regarding the destination of this oil prevented American corporations from developing the field, as the oil might have been shipped to Iran. Development only commenced when the Italian company Agip was chosen to oversee development.¹¹⁴ Yet field prospecting at Kashgan also generated revenue. According to LeVine, the mayor of the port nearest to the Kashgan field was able to extract millions from oil MNCs to improve local infrastructure.¹¹⁵ Thus, interest in Kazakhstani oil generated investment by itself, although geopolitical concerns presented challenges that hampered the speed of field development.

Investment was not limited to Western corporations. The government sold the Chinese government rights to the Uzen oil fields in 1997, which was the state's second largest field at the time. In return, Beijing promised to finance a pipeline to the Chinese border which would cost almost USD 10 billion over eight years. The Chinese also agreed to construct a pipeline to Iran. As of 2005, the pipeline to the border was under construction and the Chinese national oil company, or CNPC, purchased the

¹¹² Olcott, 144-46; this deal was not completed until 1993; Pomfret, 867.

¹¹³ Political Risk Services, 8.

¹¹⁴ Kleveman, 75-76.

¹¹⁵ Steve LeVine, *The Oil and the Glory: The Pursuit of Empire and Fortune on the Caspian Sea*, (New York: Random House, 2007), 339; LeVine described these improvements as the mayor's "pet projects."

remainder of the shares in the Uzen field conglomeration.¹¹⁶ Yet as of 1999, Beijing only deployed “about 60 percent of the planned investment...” This prompted Olcott to speculate the Chinese wanted access to Kazakhstani resources, but did not consider cultivation of these fields a major necessity.¹¹⁷ Yet China may become an important market for Kazakhstani oil, and relations between these states may expand.

Not every corporation that invested in Kazakhstan was successful. In 1996, Hurricane Hydrocarbons, or HHL, purchased fields that had previously been owned by the state. Yet by 1998 HHL was involved in a dispute with its main refinery at Shymkent, which was owned by the Kazakh Central Asian Industrial Investments group.¹¹⁸ By 1999, the firm faced commercial failure; in part because HHL had not anticipated the extent of “community obligations” it had accepted. Such conditions required HHL to approve a Kazakhstani bank as an investment partner.¹¹⁹ This suggested that investors still faced a variety of challenges following entry into the country, including pressure to include local firms in development projects.

The shortcomings of Hurricane Hydrocarbons illustrated several problems that characterized investment conditions in Kazakhstan. As previously noted, most factories in the state maintained nonproducing facilities, including “hospitals and apartment buildings” for employees. The fields HHL purchased included such assets. When HHL attempted to reorganize these areas into integrated decision-making processes, disenfranchised plant directors exploited connections with local police and government officials to force to HHL to subcontract jobs to local companies.¹²⁰ This illustrated that investing corporations faced numerous structural problems in Kazakhstan that had the capacity to derail investment.

¹¹⁶ Olcott, 154; Political Risk Services, 10; this purchase cost roughly USD 150 Million

¹¹⁷ Olcott, 154.

¹¹⁸ Political Risk Services, 10; Peck 40.

¹¹⁹ Ostrowski, 106; a global dip in the price of oil also hurt HHL.

¹²⁰ Olcott, 139; Ostrowski, 106.

Corruption and resource dependency

These developments did not impede economic growth in Kazakhstan. Olcott observed that the state possessed an estimated “16.4 billion barrels of oil reserves,” making investment in Kazakhstan a virtual certainty.¹²¹ Yet the effects of the regime’s political agenda may damage long-term prospects for growth. Prominent politicians have been accused of corruption and improper actions. For example, President Nazarbayev acknowledged holding USD one billion in an undisclosed Swiss bank in 2002. The president claimed these actions were intended to protect the national economy from the negative effects of the hurried infusion of this capital.¹²² Such issues will be addressed further in later chapters. Yet such actions are likely to undermine the credibility of the Kazakhstani government and may limit the state’s ability to attract further investment.

The government’s tendency to enact legislation that affects foreign corporations may have ramifications on future investment. The laws that the regime enacted gave the regime the ability to take corporate assets, and may limit investment. Peck observed that, as of 2002, the national government was drafting legislation which would facilitate seizure of corporate assets. Peck also noted that the regime stopped courting potential investors, instead preferring to redistribute national properties to “those close to the ruling elites.”¹²³ These circumstances created a business climate in which investors cannot guarantee the security of their investment. Such conditions have the potential to damage the state’s reputation and may damage Kazakhstan’s ability to cultivate future investment.

The regime also began to legislate a greater role for itself in the oil industry. The regime has passed regulations which gave the state the right to procure shares in resource development plans before they could be marketed for sale. Experts also observed that corporations are unlikely to enter a

¹²¹ Olcott, 148.

¹²² Kleveman, 82.

¹²³ Peck, 55.

state in which leaders can alter laws with “astonishing ease.”¹²⁴ The regime’s ability to inject itself as a developmental corporation into the oil industry is likely to damage the state’s reputation abroad, and may damage the state’s ability to attract further investment and maintain economic growth.

Indeed, scholars believe such behavior will ultimately impede the country’s economic growth. Peck speculated that economic development in Kazakhstan has faltered because of the influence of local financial groups. Others also observed that the state’s ability to draw investment became increasingly subverted due to trends of state intrusion into foreign projects.¹²⁵ The oil industry was responsible for the state’s economic development, yet the government’s tendency to interfere with foreign corporations may threaten the state’s ability to exploit these resources.

The importance of oil cannot be overstated. The resource was almost entirely responsible for the growth that Kazakhstan achieved. Yet such dependency may ultimately have negative effects. One of such effect is Dutch disease, or an increase in the value of a national currency due to a single resource, which also decreases state capacity to develop other tradable projects. Such conditions limit development of a diverse economic infrastructure, leading to a decline when resources are depleted. Kazakhstan was unable to capitalize on its resources and experienced a severe economic downturn following independence.¹²⁶ The state must avoid a return to such conditions by mitigating the possibility of resource dependency.

Yet Kazakhstan may already be exposed to the effects of Dutch Disease. Scholars described the national economy as being “characterized by an extractive orientation,” while the mining industry was responsible for almost 54 percent of Kazakhstan’s industrial output in 2007.¹²⁷ Others shared this concern. Observers noted a reliance on natural resources represented a major challenge to the national

¹²⁴ Ostrowski, 146-47.

¹²⁵ Peck, 55; Political Risk Services, 1.

¹²⁶ Pomfret, 871, 859-60.

¹²⁷ Arystanbekov, 64.

economy, which could threaten continued development. Indeed, apart from its mineral resources, the state was “a net importer of consumable goods.”¹²⁸ Any number of issues could prevent the state from successfully marketing its resources. The regime does not appear to have made a serious effort to diversify its economy and to prevent this scenario from developing.¹²⁹ Such conditions may not inherently lead to economic collapse, yet this form of dependency certainly raises concerns over the effects of resource depletion in Kazakhstan.

The state’s growth may also be threatened by changes in the international price of oil. Pomfret claimed that pricing of natural resources was somewhat unpredictable, raising concerns over the impact of declining international demand and poor returns on domestic investments.¹³⁰ It should be noted that Kazakhstan has benefitted from higher prices. Indeed, the state economy began to take off in 2007 and 2008 due to higher levels of extraction and the rising cost of oil.¹³¹ Thus, the national economy benefitted from increased international demand; however, these prices may fluctuate and make it difficult for Kazakhstan to maintain its current rate of growth. The state still maintains “the most stable economy in Central Asia due to proper management.”¹³² Yet the conditions which created this prosperity were neither permanent nor irreversible. The regime’s ability to effectively manage the revenues generated by oil may jeopardize the state’s economic success.

Conclusion

The level of economic development Kazakhstan achieved is impressive. The state’s evolution from a single economic component of the Soviet Union into Central Asia’s best established economy is remarkable.¹³³ The reforms that the Nazarbayev regime enacted helped make this growth possible by encouraging foreign investment in Kazakhstan’s natural resources. These reforms were successful; the

¹²⁸ Koch and Chaudhary, 145.

¹²⁹ Kleveman, 89.

¹³⁰ Pomfret, 871.

¹³¹ Arystanbekov, 64.

¹³² Koch and Chaudary, 145.

¹³³ Agrawal, 91; Koch and Chaudhary, 145.

state was able to attract nearly USD 30 Billion in foreign investment in 2005.¹³⁴ This level of investment demonstrated the regime had successfully created a business climate that was capable of attracting FDI from the international community. Such legislative changes helped Kazakhstan achieve growth following independence and represented an important component of the state's development.

However, Kazakhstan's economic growth was primarily driven by natural resources. Scholars observed that serious economic growth only occurred after development projects became active and international prices rose.¹³⁵ Pomfret claimed that resolutions to transport disputes and the discovery of new fields were expected to guarantee the stable production rates well into the 21st Century. Such benefits were also enhanced by a fivefold increase in the cost of oil over a six year period. Indeed, the IMF anticipated that Kazakhstan's natural resources would generate nearly USD 165 billion in revenues by 2050.¹³⁶ The state's ability to exploit these conditions was connected to the reforms passed following independence, yet revenues generated by the state's oil reserves was the primary factor in Kazakhstan's economic development.

However, mismanagement of resource revenues may threaten these accomplishments. As Pomfret previously observed, the state appears to be overly reliant on natural resources.¹³⁷ Moreover, the regime's pattern of incursion into the oil industry may also damage the positive investment climate that Kazakhstan cultivated.¹³⁸ The regime has also displayed a willingness to rewrite laws and to establish parameters for state entry into the oil sector. Such patterns are unlikely to encourage further investment, and may have serious repercussions on Kazakhstan's economic future.¹³⁹ The level of growth that the state achieved is still remarkable, yet these conditions are tenuous. The Nazarbayev

¹³⁴ Orynbaev, 396.

¹³⁵ Arystanbekov, 64.

¹³⁶ Pomfret, 862, 868; oil rose from "less than \$10 a barrel in 1998 to over \$50 in late 2004..."

¹³⁷ Pomfret, 871.

¹³⁸ Political Risk Services, 1.

¹³⁹ Ostrowski, 146-47; Political Risk Services, 1.

regime must take both political and economic steps to maintain the investment climate that was developed after the state gained independence. The state must also make efforts to diversify the national economy, or risk economic collapse when resources are depleted.

Chapter III: Regime Expansion into the Oil Industry

Introduction

Multinational corporations sought to invest in Kazakhstan for a variety of reasons. Yet this interest carried political ramifications. The capital that foreign corporations pumped into the state strengthened the autocratic tendencies of President Nazarbayev's administration. The regime was able to leverage this newfound clout to assert its control over Kazakhstan's oil industry. The regime achieved this through steps that forced foreign oil companies to include domestic corporations and through modification of oil contracts. Foreign investment itself also aided the regime's efforts to control the oil sector. Enrichment empowered the regime and enabled it to expand its control over other elements of political life, leading to a reduction of political freedoms in Kazakhstan.

The Nazarbayev regime was initially obligated to make concessions to attract investment following independence.¹⁴⁰ Peter Riches considered this a common trend among states attempting to attract investment. When signing a production sharing agreement, a government may postpone collection of its dividend for a length of time, encouraging oil corporations to finance early development expenses and allowing the corporation to capture early returns from the venture.¹⁴¹ Conditions surrounding Kazakhstan's independence prompted the regime to offer such incentives. However, Kazakhstan also required a significant level of economic aid following independence. According to Ahrend and Tompson, this contributed to a "weak bargaining position" that forced the regime to offer additional concessions that it would have not been made in better conditions. Yet once the state's oil resources were developed, the regime began to insist upon a larger role in the oil industry.¹⁴² Conditions

¹⁴⁰ Rudiger Ahrend and William Tompson, "Caspian Oil in a Global Context," *Transitional Study Review* 14 (2007): 170.

¹⁴¹ Peter Riches, "Perspectives on the political risk system for western multinational oil company investment in Central Asia," in *Oil Transition, and Security in Central Asia*, ed. Sally N. Cummings. (New York: Routledge Curzon, 2003): 168.

¹⁴² Ahrend and Tompson, 178.

that Kazakhstan faced initially constrained the options available to the regime, yet it became increasingly active as the oil sector matured.

Attempts by the regime to participate in the national oil industry may also be part of a natural evolution between an investing corporation and a host government. This relationship alters as resources develop. Riches found that, having invested in a state, an oil firm could expect to lose negotiating leverage over the state as the investment developed.¹⁴³ Evidence of such change is observable in Kazakhstan. The state has adopted a more assertive stance against oil companies. For example, disputes over taxation levels between investing corporations and the regime also centered on the understanding of agreements that had previously been negotiated.¹⁴⁴ Such events suggest that Riche's analysis of declining leverage over an investment period is accurate. These developments help explain how the regime was capable of creating a greater role for itself in the national oil industry.

Conditions surrounding Kazakhstan's independence also indicate that foreign multinationals initially held negotiating leverage over the state.¹⁴⁵ Given the regime's expansion into the oil sector, these changes imply that the relationship between investors and the state has changed over to the length of the agreement. Riches defined this as an "obsolescing bargains" trend, in which state leaders are likely to readdress earlier concessions regarding extraction of a state's natural resources. A government may develop the capacity to use its expanded leverage to renegotiate agreements.¹⁴⁶ This also suggests that the effects of foreign investment may allow political leaders to reverse earlier decisions. It is therefore necessary to consider various effects of foreign investment on the political development of a state.

¹⁴³ Riches, 170, 169; "The end of substantial short-term financial gains...may well generate forces that will exacerbate the obsolescing bargain problem over the next few years."

¹⁴⁴ Ahrend and Tompson, 172.

¹⁴⁵ Ahrend and Tompson, 178.

¹⁴⁶ Riches, 168-69.

Foreign Investment and Political Development

Li suggested that investment in a democracy would lead to resistance to “incentive policies” among political opposition figures, which may lead a state to limit corporate tax breaks. Such interaction implies that FDI can influence political decision-making. If such effects occur in democratic states, it is likely that autocratic regimes are also influenced by FDI. Li observed that politicians courting foreign investors may provide financial breaks to foreign corporations as a way to gain personal corporate sponsorship, rather than courting investment “for the sake of maximizing social welfare.” Li also feared that providing tax incentives to corporations would trigger a “race to the bottom,” by reducing a state’s fiscal assets and ultimately damaging the state over an extended period of time.¹⁴⁷ Thus, attempts to attract investment in non-democratic states may enable officials to rank personal motivations over state objectives. Such action is likely to have a negative effect on political development within a state, and would hamper political development.

Yet scholars disagree over the exact impact of FDI on development. Some scholars expressed concern that investment may contribute to authoritarian behaviors among national leaders. Haggard noted that the bargaining strength of investing corporations often depended on the sector receiving investment. He suggested that relations between the corporation and a state would progress based on the type of investment a state received. Likewise, Ross observed that revenues generated by natural resources could have a negative impact on transparency and democratic development.¹⁴⁸ This may, as implied above, indicate that certain types of investment carry the same consequences as improperly used oil revenues, suggesting that improper forms of investment may also contribute to autocratic tendencies. Therefore, the effects of investment must be examined in order to illustrate the link

¹⁴⁷ Quan Li “Democracy, Autocracy, and Tax Incentives to Foreign Direct Investors: A Cross-National Analysis,” *Journal of Politics* 68 (February 2008): 66, 72.

¹⁴⁸ Stephan Haggard, *Pathways from the Periphery: The politics and growth of newly industrializing countries* (Ithaca NY: Cornell University Press, 1990), 220; Michael Ross, “Does Oil Hinder Democracy,” *World Politics* 53 (April 2001): 328.

between political development and investment. Within this framework, natural resource investment must also be reviewed to determine how such revenues can affect government behavior.

Wibbels observed that integration into the global economy influenced the social spending patterns of developing states. He hypothesized that integration led to lower levels of social welfare spending by governments, as integration into the global economy would lead actors in “tradable sectors” to oppose proactive government spending during recessions. Natural resource reliance, in addition to “real exchange rate volatility,” would force developing states to reorganize social welfare programs to avoid deficits. Wibbels believed such policies would severely impact impoverished citizens in developing states. He concluded that policy decisions in developing states were heavily influenced by “internationally inspired economic circumstances.”¹⁴⁹ These conditions indicate that decision-making in the developing world is shaped by external factors. Such conditions also influence the ability of a state to attract investment, and may reorganize political priorities in a way that places investment attraction over social aid for citizens. Such decision-making in a non-democratic state may have the potential to empower leaders without providing citizens a forum to express discontent.

Yet implications as described above may differ between the sectors attracting investment. As previously observed, the effect of investment may depend on the industry being developed. Haggard suggested the effect of FDI on regime assertiveness during negotiations would vary across economic sectors. According to Haggard, extractive corporations generally held a stronger negotiating position than state governments prior to investment. Such industries required a considerable amount of capital be implemented over an extended time table. This initially gave these MNCs leverage. Yet “once investment was sunk,” states developed expertise that allowed them to take stronger negotiating positions against the MNCs. However, “import substituting industries” gave the state the ability to

¹⁴⁹ Erik Wibbels, “Dependency Revisited: International Markets, Business Cycles, and Social Spending in the Developing World,” *International Organization* 60 (Spring 2006): 435-36, 438, 458, 462.

restrict access prior to investment. These sectors lacked a supportive consumer base and potentially faced domestic competition, leading Haggard to conclude that “the point of entry” represented the weak negotiating point for these corporations.¹⁵⁰ Thus, the impact of investment on the pace of political development may vary according to economic sector. Extractive industries initially hold most negotiating leverage, suggesting that governments must maintain positive relationships with these MNCs during early investment stages. Yet successive regimes would be able to unilaterally revise these relationships, in favor of the state.

Tugwell observed aspects of this relationship in Venezuela. He observed that political leaders often lacked information about multinational interests, and that corporate decisions often affected domestic welfare, which was also by determined “externally based [decision-makers.]” He suggested these conditions would lead states to call for a larger role in resource development as a way to reduce such risks. As the state controls access to resources, MNC’s were likely to meet these demands. Tugwell assumed that relations between extractive MNCs and a state would be intrinsically unstable as a result.¹⁵¹ This suggests that investment in extractive industries may also encourage mistrust between a state and an MNC. A state under these conditions could be more likely to adopt proactive measures against corporations that reduce corporate influence on policy making.

Tugwell also analyzed relations between oil MNCs and Venezuela. He claimed the ideology driving oil policy in this state had been articulated by Perez Alfonso. Alfonso believed oil had “a high intrinsic value” not reflected on international markets. Governments should therefore control these resources to capitalize on their potential. Crucial components of this agenda were conservation and

¹⁵⁰ Haggard, 220-21.

¹⁵¹ Franklin Tugwell, *The Politics of Oil in Venezuela* (Stanford: Stanford University Press, 1975), 9, 13, 14-16.

extensive taxation of MNCs.¹⁵² Successive governments implemented such policies and allowed the state to assume control over increasing levels of revenue that investment had created. Yet relations between governments and oil MNCs were not overly antagonistic. The state adopted a “conciliatory attitude” towards the oil MNCs that made provocative measures more palatable. Other national issues also spurred Venezuelan entry into its oil industry. Fiscal concerns forced the state to occasionally adopt an agenda that favored “short-term consequences.”¹⁵³ Thus, the state adopted a broad strategy designed to maximize influence over the oil industry. This illustrates that obtaining shares of oil revenues was an important objective for Venezuela. This further implies that the possibility of attaining these revenues may influence governmental behavior.

Investment may affect government behavior in multiple ways. Rising levels of corruption would have an adverse effect on a state’s political growth. Husted found corruption was significantly related to higher levels of financial growth. He suggested dynamic economic growth was a strong predictor of corruption in states that featured either a “collectivistic,” or paternalistic culture.¹⁵⁴ Financial growth may not contribute to corruption and growth may originate from sources aside from FDI, yet a state without institutions or historical experiences that ensure transparency would be likely to witness an increase in corruption. Thus, in some developing states, prosperity could lead to a decline in transparency. Nontransparent institutions would have a negative impact on the political development of a state.

Robertson and Watson explored the connection between FDI and corruption, hypothesizing that FDI represented an opportunity to benefit from state resources. They observed that a rapid prosperity

¹⁵² Tugwell, 34, 36-37; Alfonso also believed revenue accumulation should be limited by the state’s ability to absorb the wealth.

¹⁵³ Tugwell, 150-51, 155-57.

¹⁵⁴ Bryan W. Husted, “Wealth, Culture, and Corruption,” *Journal of International Business* 30 (Second Quarter, 1999): 353-54, 343; Husted measured economic growth using the GNP per capita PPP of observed states.

rise could be attributed to FDI, which could prompt leaders to “resort to corruption.” This led the authors to suggest corruption levels could be connected to the speed with which investment entered or exited a state.¹⁵⁵ The authors empirically examined aspects of the relationship between FDI and corruption and found them all to be significant. They suggested the connection between FDI and corruption may be “bidirectional...with FDI flows affecting corruption.”¹⁵⁶ Such findings imply that a credible link between investment and deteriorating transparency is possible. This would further suggest that investment can negatively affect political development.

Ross also made significant contributions to this theory. He suggested natural resource revenues could be used to reduce pressure on governments for transparency. Such revenues enabled a regime to reduce or eliminate political institutions that provide citizens an opportunity to critique their government. For example, significant oil revenues may reduce a government’s need for tax revenues. This may reduce citizen demands for transparency from the ruling regime. He also found that such revenues could be exploited by autocrats as a way to reduce calls for political openness through reduced taxation and generous social policies. This led Ross to conclude that increases in resource revenues could have a negative impact on political development.¹⁵⁷ Although oil revenues are not supplied by the same actors who supply investment, the effects of oil revenues and investment appear to be similar. As observed above, investment can lead to corruption, hampering political growth. A similar effect is created by oil revenues. This would imply that, in appropriate contexts, the effects of oil revenues and foreign investment are equally negative.

Winters and Gould examined the impact of foreign investment on political development in Chad, which had gained significant revenues from natural resources. The authors observed that oil

¹⁵⁵ C.J. Robertson and Andrew Watson, “Corruption and Change: The Impact of Foreign Direct Investment,” *Strategic Management Journal* 25 (April 2004): 387-89.

¹⁵⁶ Robertson and Watson, 392-93.

¹⁵⁷ Ross, 332-35, 357.

revenues had a deleterious effect on political development, despite efforts by the World Bank to promote transparency. Chad was governed by an autocratic president who limited World Bank efforts to promote transparency and the responsible use of oil revenues. The president was able largely to remove such restrictions by undermining political and civil society institutions.¹⁵⁸ In this context, Winters and Gould observed that natural resources made politics a “zero-sum contest” for the resource-generated revenues. The authors predicted that such funds would only “intensify domestic institutional stress.” Indeed, after observing political developments in Chad, the authors claimed oil revenues had actually contributed to the Chadian president’s autocratic consolidation.¹⁵⁹ Such findings confirm that revenues generated by extractive industries had a negative impact on political development in Chad.

The preceding examples suggest that investment generated revenues can have a negative impact on political development in developing states. FDI may lead government officials to engage in corrupt actions, yet the effect of FDI may also be more extreme than that. Ross claimed the revenues that investment helped generate could empower a government to side step democratic constraints. Examples from Chad appear to confirm Ross’ hypothesis.¹⁶⁰ This indicates that oil revenues have the potential to promote autocratic tendencies of states that are dependent on natural resources. Robertson and Watson’s research suggested that FDI could contribute to corruption.¹⁶¹ This indicates the effects of investment and resource revenues can have an equally negative effect on political development.

However, such effects depend on the political conditions that predate investment. Bayulgen observed that levels and types of FDI helped determine “regime trajectory.” She observed that investment provided autocratic regime with an international “vote of confidence” through economic

¹⁵⁸ Matthew S. Winters and John Gould, “Betting on Oil: The World Bank’s Attempt to Promote Accountability in Chad,” *Global Governance* 17 (2011): 230, 229, 235-37.

¹⁵⁹ Winters and Gould, 232, 235, 240.

¹⁶⁰ Ross, 332-35; Winters and Gould, 240.

¹⁶¹ Robertson and Watson, 392-93.

development. Others also found that oil-rich states receiving FDI were able to maintain autocratic practices and subvert political reforms by promising returns from “oil boom prosperity.”¹⁶² This appears to have happened in Kazakhstan. Pomfret noted that privatization had a negative impact on “the institutional quality of the economy,” noting that the state scored poorly in measurements of transparency and openness.¹⁶³ These findings indicate that investment in Kazakhstan carried negative repercussions. This also suggests that foreign investment has supplemented the regime’s ability to consolidate power.

Initial investment conditions in Kazakhstan

Kazakhstan possessed elements that enable a state to attract investment. A crucial factor was the structural reforms that were designed to attract FDI. A 1994 law shielded international investment from “nationalization [and] expropriation, changes in legislation, and illegal action by state agencies or officials.”¹⁶⁴ Likewise, financial reorganization helped the state achieve stability and garnered nearly USD 1.5 billion in foreign investment in 1999 and in 2000. Natural resources also played a major role in attracting investment. Between 1993 and 1997, several large oil MNCs signed agreements to develop fields in Kazakhstan.¹⁶⁵ Bayulgen claimed that such changes enhanced the stature of the regime. She observed that the regime was “dominant in the oversight of contracts with foreign companies,” noting that prominent officials were responsible for reviewing investment agreements while deciding the regime’s stake. Economic and political reforms, as well as natural resources, helped create economic

¹⁶² Oksan Bayulgen, “Foreign Direct Investment in Central Asia and the Caucasus: Curse or Blessing,” *Communist and Post-Communist Studies* 38 (2005): 52, 63; Alec Rasizade, “The great game of Caspian Energy: ambitions and realities,” *Journal of Southern Europe and the Balkans* 7 (April 2005): 4.

¹⁶³ Richard Pomfret, “Kazakhstan’s Economy since Independence: Does the Oil Boom Offer a Second Chance for Sustainable Development,” *Europe-Asia Studies* 57 (September 2005): 867.

¹⁶⁴ Vildan Serin and Elif Yuksel, “Foreign Direct Investment Flows in Kazakhstan: The Role of the Energy Sector,” *Journal of Academic Studies* 7 (May-July 2005): 12.

¹⁶⁵ Levent Koch and M. Ali Chaudhary, “Economic Transformation of Kazakhstan: Evidence from Liberalization Reforms,” *Journal of Academic Studies* 4 (May-July 2002): 141; Pomfret, 864-66.

growth. Yet such developments also boosted the standing of the regime. This enhanced standing is likely to have helped President Nazarbayev consolidate power.

Early negotiations allowed foreign oil companies to extract favorable terms from the regime. The terms of a deal between Chevron and the Soviet Union, who initiated the negotiations, gave Chevron over 25 percent of revenues generated by the Tengiz field. Kazakhstani negotiators later learned that “not a single lawyer [was part of] the Soviet delegation” during initial conferences. President Nazarbayev initially faced criticism during this era. This was based on the perception that the president was selling the state’s most valuable assets to international corporations. Indeed, pressure was strong enough to force the president to promise “not to approve any deal that was disadvantageous to Kazakhstan.”¹⁶⁶ The president was also a minor figure during initial Tengiz development negotiations. Talks began during the final years of the Soviet Union and Nazarbayev’s position as president limited his importance. Yet Nazarbayev rose to prominence after Soviet rule collapsed and he was able to call for new negotiations as an independent state. However, financial needs forced the president to offer significant concessions in order to attract foreign investment, which allowed oil MNCs to enter the state under favorable terms.¹⁶⁷

Indeed, the state’s financial needs drove the regime to offer such incentives in order to draw investment. According to Pomfret, the state endured a financial downturn in the early 1990’s. Likewise, Kazakhstan’s GDP fell again in 1998 as a result of the “Russian [financial] crisis.”¹⁶⁸ Oil MNCs frequently offered some form of payment in recognition of these problems and as a prelude to negotiations. For instance, early interactions with Omani representatives included the transfer of USD 100 million to help feed livestock and prevent famine. When Mobil sought rights to develop a portion of the Tengiz field,

¹⁶⁶ Steve LeVine, *The Oil and the Glory: The Pursuit of Empire and Fortune on the Caspian Sea*, (New York: Random House, 2007), 137, 139; Chevron eventually agreed to 20 percent of Tengiz profits.

¹⁶⁷ LeVine, 120, 125; Ahrend and Tompson, 170, 178.

¹⁶⁸ Pomfret, 861.

the regime extracted a USD 145 million payment from the company before granting access to the field.¹⁶⁹ Such pressing needs illustrate why the regime chose to grant such concessions to oil companies.

The regime's need for cash influenced its decision to offer favorable terms to foreign investors. For example, the regime was willing to negotiate contracts "on a case-by-case basis" and offered contractual inviolability as further incentives. Ahrend and Tompson considered this a crucial component of the regime's effort to attract investment.¹⁷⁰ Initial agreements with Chevron included a clause that allowed the company to avoid paying most of a USD 450 million signing bonus to Kazakhstan, should the state failed to construct a pipeline to a coastal outlet. According to LeVine, these terms gave Chevron a major stake in "the world's sixth largest oil field..." for which the company paid "a paltry USD 30 million."¹⁷¹

These terms gave foreign oil corporations significant influence over Kazakhstan's oil industry. Yet the regime eventually began to emphasize its control over this sector. The extensive allowances the state offered help explain the changes the regime has implemented in contract negotiations. Ahrend and Tompson have claimed the regime has begun to interpret contractual "provisions in favor of the state..." They also claimed that this explained the regime's assertion it was only reclaiming its rightful stake in state resources.¹⁷² The regime was attempting to recoup some of the control over the oil industry that it had lost as a result of concessions it had granted during the years following independence.

Disputes over pipeline financing also constrained the regime. The state only held "one third of the votes" in the CPC pipeline coalition, which made Kazakhstan the least influential actor in negotiations over pipeline development. Disagreements also raised tensions between investing

¹⁶⁹ LeVine, 130-31, 277.

¹⁷⁰ Ahrend and Tompson, 170.

¹⁷¹ LeVine, 140.

¹⁷² Ahrend and Tompson, 172.

corporations and the regime, and threatened to shut construction down.¹⁷³ The CPC pipeline was only completed after a coalition of four companies, as well as Russia, Kazakhstan, and Oman agreed on financing terms. As a result, the CPC pipeline “opened in October 2001, after at least 5 postponements...”¹⁷⁴ It is also significant that the pipeline was only completed because an agreement between CPC members, and the partnership of Arco and Lukoil, was reached. This compromise incorporated a Russian firm, which was a political necessity. Indeed, LeVine reported that pipeline development had experienced setbacks due to “insufficient Russian involvement.” As a result of these negotiations, Kazakhstan only retained control of about 25 percent of the Tengiz field after these conferences were completed.¹⁷⁵ These conditions explain the regime’s subsequent efforts to establish control over the oil industry.

Regime expansion into the oil industry

The Nazarbayev regime was able to gain control over the oil industry in Kazakhstan using two specific policies. First, the regime made changes to its contractual relationships with oil MNCs by altering legislative agreements. Second, the regime used its political influence to expand the role of domestic companies within the oil industry. These developments allowed the regime to gain leverage over foreign corporations, which allowed it to influence development in the oil sector and to prosper through participation. Creation of a national oil company, or NOC, also represented an initial step in this process. The NOC was created by combining state companies that managed development projects and “trunk pipelines.” This merger allowed the regime to develop and implement a consistent agenda regarding national resources. Indeed, Ahrend and Tompson observed that the regime specifically intended for the

¹⁷³ LeVine, 252.

¹⁷⁴ LeVine, 284; John Roberts, “Caspian oil and gas: how far have we come and where are we going,” in *Oil Transition and Security in Central Asia*, ed. Sally N. Cummings. (New York: Routledge Curzon, 2003): 152.

¹⁷⁵ LeVine, 282, 288; the agreement gave Arco-Lukoil a 5 percent stake in the Tengiz field at a cost of USD 200 Million. LeVine considered this “eye-popping,” as Chevron had paid USD 800 Million for a 50 percent stake. LeVine believed this underscored the “bargain” that Chevron received when entering Kazakhstan.

NOC to be part of an increase in governmental participation in the oil industry.¹⁷⁶ However, these changes contributed to non-democratic tendencies within the regime. As was previously noted, revenues accrued by non-democratic leaders often enabled them to deflect criticism of their political performance.¹⁷⁷ This would allow the Nazarbayev regime to conduct its affairs with greater autonomy.

The policies the regime created for the NOC were consistent with its objective to actively participate in the oil industry. A law issued in 2003 specified that agreements reached following ratification were “subject to changes in legislation,” in addition to changes in global markets. The regime also drafted legislation that required the NOC to automatically receive half of the available stakes in potential projects.¹⁷⁸ Domjan and Stone claimed this represented an attempt to generate greater returns by expanding state participation through the NOC. This enabled the NOC to develop expertise and the managerial experience necessary to operate on Caspian Sea fields.¹⁷⁹ Creation of the NOC and development of its technical capacities thus enabled the state to actively participate in Kazakhstan’s oil industry. This participation expanded government involvement and helped the government gain control over Kazakhstan’s oil sector.

The regime also used legislative changes and corporate shortcomings to expand its control over the oil industry. Scholars considered implementation of a modified tax code to be an example of the regime’s ability to control the oil industry. The regime approved an amendment that increased export tax rates based on changes in the international price of oil. Yet the same scholar also observed that these changes circumvented protections that were previously guaranteed, namely those that ensured a fixed level of corporate taxation over the length of a contract. These provisions allowed the regime to

¹⁷⁶ Ahrend and Tompson, 172.

¹⁷⁷ Ross, 332-34.

¹⁷⁸ Ahrend and Tompson, 174; Global Agenda, “Kazakhstan turns the screw,” August 4, 2007.

¹⁷⁹ Paul Domjan and Matt Stone, “A Comparative Study of Resource Nationalism in Russia and Kazakhstan 2004-2008,” *Europe-Asia Studies* 62 (January 2010): 51-53.

capture between 65 and 85 percent of oil industry revenues.¹⁸⁰ The regime also used corporate shortcomings to expand control. The regime began to assert that oil corporations had not provided a higher level of “management expertise” in field development, and began to hold multi-national firms responsible for postponements. The regime accomplished this by forcing corporations to bear the financial consequences of developmental delays.¹⁸¹ Thus, changes in taxation and assertions of ineffectiveness enabled the regime to extract further concessions from oil companies and helped the regime expand its leverage over the oil industry.

The regime also grew more assertive with oil MNCs regarding the speed of field development, specifically over the pace of development at the Kashgan field. Initial projections suggested the field would become operational in 2005, yet production had not begun in 2007 and was estimated to be delayed until 2010. Development costs were also expected to double during this period. In early 2008, estimates suggested that production would commence in 2011.¹⁸² These delays led the regime to audit “subsoil contracts” with the intention of determining if agreements were breached. Scholars also implied that these reviews were also intended to help the regime “maintain leverage over foreign investors.”¹⁸³ This suggested that production delays placed the regime in a position to exert influence over oil MNCs operating in Kazakhstan.

Implementation of such policies as described above was designed to put “the burden of cost overruns” on MNCs, which forced these corporations to accept the demands of the regime.¹⁸⁴ These actions also allowed the regime to force MNCs to comply with state demands and gave the regime leverage over these corporations. For example, after a developmental delay at the Kashgan field in

¹⁸⁰ Pinar Ipek, “The Role of Oil and Gas in Kazakhstan’s Foreign Policy: Looking East or West,” *Europe Asia Studies* 59 (November 2007): 1190; see footnote #27.

¹⁸¹ Domjan and Stone, 51-52.

¹⁸² Domjan and Stone, 51; Global Agenda, August 4, 2007.

¹⁸³ Global Agenda, August 4, 2007.

¹⁸⁴ Domjan and Stone, 51.

2007, the Prime Minister announced that the regime considered these delays to violate the operating consortiums contractual agreements. The regime stated that it intended to counter violations with “adequate measures.” Analysts also suggested that state agencies intentionally failed to meet their contractual obligation, helping to create these developmental delays.¹⁸⁵ Such conditions suggest the regime adroitly utilized technical delays to renegotiate agreements. These developments also enabled the regime to expand its bargaining control over foreign corporations.

Domjan and Stone observed that the regime also sought to expand participation beyond development and into other areas of the oil industry. For instance, the regime signaled its desire for Kazakhstani companies, particularly the NOC, to have an expanded role beyond field development as a way of gaining management experience. To this end, the NOC purchased a Romanian oil refinery in the mid-2000s. Scholars identified this as an attempt to expand the NOC’s assets to areas outside of field development.¹⁸⁶ Such actions indicate that the regime expects the NOC and other national firms to participate in multiple areas within the oil industry. This expansion of domestic companies is likely to give the state greater influence and the ability to extract greater revenues from the oil industry.

Investors encountering such conditions may consider withdrawal from a state. However, the constraints that oil companies face make such actions difficult to consider. Ahrend and Tompson observed that the significant monetary investment needed for oil field development created financial deterrents that prevent corporations from leaving. Put simply, MNCs lose the ability to develop their product if they leave the state. These disincentives also create an advantage for host states. Ahrend and Tompson also observed that “once investments were initially made, and costs were sunk, it was relatively easy for states to revise the terms of their interaction.” They also found the Nazarbayev regime’s plan to increase its participation in the Kazakhstani oil industry were successful, in part,

¹⁸⁵ Global Agenda, August 4, 2007; Political Risk Services, “Kazakhstan: Country Conditions, Investment Climate,” *Political Risk Services Group* (May 2005): 4.

¹⁸⁶ Domjan and Stone, 53.

because of corporate hesitancy to abandon their investment. Thus, the regime was able to become more assertive because of the prohibitive costs associated with a pullout of Kazakhstan.¹⁸⁷ These limited options allowed the regime to establish leverage over oil MNCs and gain greater control over the national oil industry.

Evolution of the relationship between the regime and investors

The regime's desire to regain revenue sources that were given as concessions following independence partially explains the state's interactions with the national oil industry. Yet the evolving relationship between a resource rich state and investors can also explain such developments. Riches observed that negotiating leverage between an oil supplier and a shipment corporation favors the supplier prior to the completion of a transit route. A similar assessment can be made regarding oil field development. A state that cannot finance the infrastructure necessary to capitalize on resources will initially be dependent on foreign assistance. Yet as an "oil company sinks its money into a country, its bargaining power with the state progressively declines over the length of the field."¹⁸⁸ Haggard made similar observations regarding the bargaining power of an investing corporation vis-à-vis the host-state, finding that initial conditions favored investors, yet shifted to the host state as the industry developed.¹⁸⁹ Thus, the negotiating leverage that the regime gained can also explain its recent ability to extract concessions from investing multinationals.

These conditions contributed to the changes in negotiating leverage in Kazakhstan. Riches also claimed that evidence of this transition could be observed in taxation clauses and "delays in the definition of recoverable costs under the contract."¹⁹⁰ This shift in bargaining power coincided with increased international demand for oil. One scholar observed that development of the state's oil field, in

¹⁸⁷ Ahrend and Tompson, 177-78.

¹⁸⁸ Riches, 164, 168.

¹⁸⁹ Haggard, 220

¹⁹⁰ Riches, 168-69.

addition to the increasing price of oil enabled the regime to establish control over oil MNCs “between 2004 and 2007.”¹⁹¹

Domjan and Stone categorized the state’s efforts to control the oil industry as “resource nationalism.” They considered such policies to be profit motivated: “The aim [of the regime] has been to improve the economic terms and long-term economic [benefits] of the country.” The regime pursued these objectives in a variety of ways; however, a critical component of this process was the regime’s tendency to expand government oversight of a project using the NOC, Kazmunaigaz. Others also observed this trend. A key component of the regime’s strategy was legislation that mandated the compulsory inclusion of the NOC in half of any development plan.¹⁹² Moreover, in the midst of a dispute over development rights, the regime approved a provision that granted it “the right of first refusal” of any plot for sale in currently developed fields. The provision even stipulated that the law “trumped the terms of the contract itself.”¹⁹³ Such provisions clearly indicate the regime was has established control over Kazakhstan’s oil industry.

Domestic inclusion in the oil industry

Natural shifts in bargaining strength helped the regime establish control over the oil industry; however, the regime soon developed the capabilities necessary to enter this sector. Kazakhstanis who were employed by the oil industry gained technical experience during the early years of investment. This empowered the state and also enabled the regime to establish negotiating leverage over oil MNCs. Expertise also enabled the regime to develop state resources without investor assistance. Discontent over the pace of development at the Kashgan field allowed the regime to review contractual agreements with MNCs as a method of gaining control over these companies. Yet scholars also suggested that such reviews were intended to steer “sub-contracting work” at multinational sites to

¹⁹¹ Ipek, 1188.

¹⁹² Domjan and Stone, 51-52; Global Agenda, August 4, 2007.

¹⁹³ Ahrend and Tompson, 173.

domestic businesses, while also improving the “conditions for local workers.”¹⁹⁴ This suggests the regime utilized the improved skills of domestic workers to help the state operate independently of oil MNCs. This ability also helped the regime create a larger role for itself within the oil industry.

The limited number of production sharing agreements, or PSAs, that the regime had recently signed led Domjan and Stone to suggest that the regime is evaluating the NOC’s capacity to oversee a project without foreign assistance.¹⁹⁵ Ahrend and Tompson also observed that the regime took steps to ensure that the NOC and other domestic firms had a role in subsequent exploration and development efforts.¹⁹⁶ Thus the regime appeared to have capitalized on the improved technical capacity of domestic companies as a way to promote national involvement in the oil industry. Such efforts are likely to help the regime maximize control over the oil industry.

Inclusion of domestic businesses was also enhanced by “learning within the state administration,” and by foreign investors who granted the regime expanded oversight of projects. Ahrend and Tompson observed that domestic companies were professionalized by exposure to the advanced development methods that Western corporations employed. The regime utilized this improvement to expand the role of domestic firms. Domjan and Stone observed that the regime captured large amounts of revenue from the oil industry by enabling government-owned corporations to occupy a large role in oil industry.¹⁹⁷ This level of domestic participation is also likely to give the state greater leverage in negotiations and may allow the regime to establish control over multiple areas within the oil industry.

¹⁹⁴ Global Agenda, August 4, 2007; it was also suggested that “revenue raising figured prominently” into the regime’s contractual review.

¹⁹⁵ Domjan and Stone, 53-54; the government did sign a PSA with Rosneft in 2005.

¹⁹⁶ Ahrend and Tompson, 179.

¹⁹⁷ Ahrend and Tompson, 177; Domjan and Stone, 51.

As previously noted, scholars observed that the regime made efforts to “improve conditions for local workers.”¹⁹⁸ This appeared to have been a legitimate concern for the regime. For instance, contractual agreements with major corporations included requirements to meet monetary needs, donate to social causes, and to make up for local depression by compensating for “back wages, [and rebuilding] factories and plants” in the area. Likewise, Domjan and Stone claimed that President Nazarbayev paid deliberate attention to improving “standards of living, economic competitiveness,” and structural upgrades. The president listed these as explicit policies that were implemented in his “*Kazakhstan 2030* economic plan.”¹⁹⁹ The regime also used contract negotiations to create jobs. Beginning in the 1990’s, employment of domestic workers became a “de facto performance requirement.” By 2001, the regime had changed its proportioning structure regarding international workers, which forced MNCs to hire more native laborers.²⁰⁰ These requirements enabled domestic workers to gain the previously mentioned experience. Such steps may also have helped the regime maintain its control over political life by deflecting criticism of the state’s economic performance.

Impact of expanded participation on political development

There were political ramifications to foreign investment in Kazakhstan. The regime’s expansion into the oil industry altered the structure of political power and allowed the regime to consolidate its control over the state. Indeed, scholars observed that investment is “the link between politics and economics [and] is...the main factor for consolidating power” in contexts similar to Kazakhstan.²⁰¹ This connection embowered President Nazarbayev. Pomfret observed that the regime’s distribution of development permits during the privatization process was considered a “corrupt process” that helped create “a form of crony capitalism.” This indicated that the regime was able to use the investment

¹⁹⁸ Global Agenda, August 4, 2007.

¹⁹⁹ Political Risk Services, 12; Domjan and Stone, 52-53.

²⁰⁰ Political Risk Services, 20.

²⁰¹ Anja Franke, Andrea Gawrich, and Gurban Alakbarov, “Kazakhstan and Azerbaijan as Post-Soviet Rentier States: Resource incomes and Autocracy as a Double ‘Curse’ in Post-Soviet Regimes,” *Europe-Asia Studies* 61 (January 2009): 120; the authors were referring to “the post-Soviet context.”

process to enrich and empower itself. Pomfret also argued the long-term effects of the state's resource wealth would depend on its level of democratic development, "which does not augur well for Kazakhstan."²⁰²

Pomfret's assessment of Kazakhstan's potential was shared by others. Scholars have expressed concerns based on observations of decision-making arrangements, which were decidedly non-transparent. They observed that investment deals were directly negotiated by the president and that the regime did not even maintain the appearance of democratic accountability. For example, revenue intended for the national resource fund was obscured by non-transparent policies. Indeed, nonexistent "mechanisms of good governance" even prevented scholars from identifying the amount of revenue collected by the national oil fund.²⁰³ Such assessments further indicate that the investment process allowed the Nazarbayev regime to develop non-transparent tendencies. It is possible a lack of democratic accountability promoted autocratic tendencies within the regime.

Yet international oil corporations have not displayed great concern over the effects of this investment. Gulbrandsen and Moe examined oil MNC's commitment to promoting good governance by reviewing forums that promoted communication with the regime. These forums theoretically had the capacity to influence policy, yet the authors observed that corporations did not criticize the regime's behavior. Rather, they only challenged the government on issues regarding these MNC's primary concerns.²⁰⁴ Indifference to broader political concerns may have also enabled autocratic tendencies within the regime. Bayulgen observed that corporate concern over political conditions was confined to the stabilization of the national "regulatory environment." She also observed that investing companies

²⁰² Pomfret, 872; although Pomfret was hopeful of a "Mexican-style revival."

²⁰³ Franke, et. al., 124, 131.

²⁰⁴ Lars Gulbrandsen and Arild Moe, "Oil Company CSR Collaboration in 'New' Petro-States," *Journal of Corporate Citizenship* (Winter 2005): 60.

“did little to promote democracy across the region.”²⁰⁵ In this context, foreign investment appears to have negatively influenced political development in Kazakhstan. The wealth FDI generated seems to have enriched the regime, allowing these rulers to establish control over political life in Kazakhstan.

Conclusion

The conditions that Kazakhstan faced following independence led the regime to seek out Western corporate investment in order to develop their natural resources. These efforts enabled the state to develop the infrastructure necessary to exploit its natural resources. Yet Western inclusion also left the state with diminished control over its own natural resources. According to analysts, such arrangements grew “ever less palatable” with the continued rise in prices of oil.²⁰⁶ Such conditions explain the regime’s subsequent attempts to emphasize its control over the oil industry. They also lend credibility to the regime’s claim that “it is now merely reasserting its legitimate interests...that it had previously been too weak to enforce.”²⁰⁷

The regime took steps to expand its role in the oil industry. A key factor in this process was the development of the NOC, Kazmunaigaz. While the NOC has “limited capabilities,” the regime requires its inclusion in half of any development venture.²⁰⁸ The regime also began to reconsider agreements with foreign investors. One factor that helped the regime establish this control was a 2004 law that granted the regime “the right of first refusal” on any share exchange in joint production arrangements. It is significant that the law applies equally to extant and impending contracts. This will give the NOC, and the regime, the ability to participate in any development project across the state. It is also significant that the regime has interpreted this law as overriding any “rights [that] consortium owners might have negotiated in the original contracts.”²⁰⁹ The regime also made efforts to include domestic corporations

²⁰⁵ Oksan Bayulgen, “Foreign Direct Investment in Central Asia and the Caucasus,” 50-52.

²⁰⁶ Political Risk Services, 8.

²⁰⁷ Ahrend and Tompson, 178, 172.

²⁰⁸ Global Agenda, August 4, 2007.

²⁰⁹ Political Risk Services, 2.

in development of the oil industry. Domjan and Stone claimed that this allowed domestic companies to develop management experience.²¹⁰ This will allow these companies to operate independently of MNCs and will give the regime a greater capacity to develop its own resources. Such efforts created a greater role for the regime within the oil industry and enabled it to control the oil sector in Kazakhstan.

These actions may be calculated steps taken by the Nazarbayev regime that are intended to expand state control over the oil industry. Yet such developments also represent the natural evolution in a relationship between an investor and the state. Riches observed an investor will gradually lose negotiating leverage over a state as the field develops. He claimed a state will “almost predictably” attempt to increase its share of natural resource control based on the decreasing leverage of an investor.²¹¹ Other modifications the regime has made confirm this hypothesis. This suggests the regime managed to cultivate control over investors as a way to gain control over the state’s natural resources.

The regime’s expanded participation in the oil industry carried political ramifications. According to Bayulgen, investment like Kazakhstan received has the potential to produce “regime persistence” if a government already displayed autocratic tendencies.²¹² Pomfret observed that the distribution of oil field contracts was part of a “corrupt process” that affected Kazakhstan’s economy and had the potential to influence the state’s political system.²¹³ Foreign investors displayed little interest in the political development of the state. Gulbrandsen and Moe observed interactions between the state and oil companies and found that firms only challenged the regime when important issues were threatened.²¹⁴ This suggests that FDI impeded political development in Kazakhstan. FDI may have enabled the regime to consolidate its control over the oil industry, enriching elites and severely constraining political development as a result.

²¹⁰ Domjan and Stone, 53.

²¹¹ Riches, 168.

²¹² Bayulgen, “Foreign Direct Investment in Central Asia and the Caucasus,” 52.

²¹³ Pomfret, 872.

²¹⁴ Gulbrandsen and Moe, 60.

Chapter IV: Political Development in Kazakhstan

Introduction

Kazakhstan achieved a striking level of economic development, yet this progress permitted President Nazarbayev and his regime to consolidate power and stifle political development. Observers noted that, although elections in Kazakhstan met the most basic criteria for a democracy, outcomes were typically suspect. In 2007 legislative elections, the president's party was the only organization that won seats in the national assembly.²¹⁵ Several factors allowed the president to strengthen his authority, yet a key factor was corruption among figures in his administration. This reinforced the regime's control over the national economy and limited opportunities for further political growth.

The regime did not initially dominate political life. However, the president took steps soon after independence to control the public sphere using decrees and legislative acts. For instance, the government punished association "with the political parties and professional unions of foreign states." The government was also restructured to ensure that political power was highly centralized, and the regime has hesitated to implement reforms which would empower regional officials."²¹⁶ Such behavior limited avenues for political opponents to openly criticize the regime. Such measures have strengthened the president's control over the state.

Yet the regime also employed indirect methods of power consolidation. This was achieved through the corrupt actions of the president and his associates. Hill observed that the president's immediate family has become progressively more connected to vital business sectors, and that his family "always tries to get a piece of the action." Others echoed this concern. Opposition figures have

²¹⁵ Oskar Lehner, "Respecting Human Rights in Central Asia: Will this stabilize or destabilize the region," *Security and Human Rights* 20 (March 2009): 50.

²¹⁶ Evgeny A. Zhovtis, "Freedom of Association and the question of its realization in Kazakhstan," trans. Maria Kozhvenikova in *Civil Society in Central Asia*, ed. M. Holt Ruffin and Daniel Clarke Waugh (Seattle: University of Washington Press, 1999): 62; Martha Brill Olcott, *Kazakhstan: unfulfilled promise*, (Washington DC: Carnegie Endowment for International Peace, 2002), 96-97.

claimed “the structure of power is totally corrupt.”²¹⁷ Scholars also observed that actual political power is concentrated around the president, his relatives and a few elites.²¹⁸ The fact that power is concentrated in such a tight circle also indicates an uneven distribution of authority, which also constrains political development.

Revenues generated by oil boosted the regime’s control over Kazakhstan. Bayulgen claimed that regimes who collect significant revenues can utilize tactics that are less repressive as a way to consolidate power.²¹⁹ This suggests that oil revenues allowed the regime to avoid blatantly autocratic methods to control the state. Oil revenues also allowed the regime to manipulate its relationship with foreign oil companies. Analysts observed that corporations must guard their investments from continuous pronouncements and regulatory modifications.²²⁰ The ability to collect revenues appears to have empowered the regime and has allowed it to extend its control over the political life.

Corruption among government officials also empowered the regime. Legal modifications enabled the president to initially control the public sphere, yet the government’s interaction with both foreign corporations and Kazakhstani society has been defined by corruption, which empowered the regime. For instance, the regime occasionally neglected to announce changes to guidelines regarding “customs exemptions...in the Law on Foreign Investment,” which allowed the regime to deal with corporations individually, leading to uneven legal treatment. Such actions can be regarded as corruption. Scholars defined corruption as an act that disregards the official government responsibilities

²¹⁷ Fiona Hill, “Whither Kazakhstan,” *the National Interest* (October 2005): 12; Paul Starobin, “Sultan of the Steppes,” *Atlantic Monthly* (December 2005): 100.

²¹⁸ Anja Franke, Andrea Gawrich, and Gurban Alakbarov, “Kazakhstan and Azerbaijan as Post-Soviet Rentier States: Resource Incomes and Autocracy as a Double ‘Curse’ in Post-Soviet Regimes,” *Europe-Asia Studies* 61 (January 2009): 114.

²¹⁹ Oksan Bayulgen, “Foreign Capital in Central Asia and the Caucasus: Curse or Blessing,” *Communist and Post-Communist Studies* 38 (2005): 50.

²²⁰ Political Risk Services, “Kazakhstan: Country Conditions, Investment Climate,” *Political Risk Services Group* (May 2005): 4.

in favor of financial advancement or prestige.²²¹ Such behavior has allowed the regime to strengthen its control over the oil industry and over the country. Control over this resource has helped the regime consolidate power and may have prevented political development.

Historical Influences on Political Development

Multiple factors can explain the prevalence of such behaviors in Kazakhstan. The lack of political development can partially be explained by the state's Soviet heritage. Scholars claimed that Central Asian states maintain Soviet-style policies following independence. National leaders were simply "party bosses, who changed their communist lapel pins for nationalist ones..."²²² Others observed that members of Kazakhstan's communist party retained their position and responsibilities following independence.²²³ In 2001, 86 percent of Kazakhstani elites had been members of the state's communist party. Murphy also observed almost no noteworthy alterations to national elite or among "intra-elite relationships" as of 2002, except that the office of the president had been empowered.²²⁴ This indicated that Kazakhstan maintained several elements of communist rule following independence. The persistence of Soviet holdovers may explain the state's lack of political growth.

Political power in Kazakhstan is concentrated around the President and a close circle of relations. Such behavior may be connected to the state's cultural identity. Scholars note that power consolidation in Kazakhstan created a "neo-patrimonial system based on trust and kinship."²²⁵ Others noted that leaders are dependent on unofficial associations that are based on Kazakhstan's social

²²¹ Chuck CY Kwok and Solomon Tadesse, "The MNC as an agent of change in host-country institutions: FDI and corruption," *Journal of International Business* 37 (2006): 767.

²²² Wayne E. Merry, "The Politics of Central Asia: National in Form, Soviet in Content" in *In the Tracks of Tamerlane: Central Asia's Path to the 21st Century* ed. Daniel Burghart and Theresa Sabonis-Helf (Washington DC: National Defense University Center for Technology and National Security Policy, 2004), 31.

²²³ Franke, et. al., 113.

²²⁴ Jonathan Murphy, "Illusory Transition? Elite Reconstruction in Kazakhstan, 1989-2002," *Europe-Asia Studies* (June 2006): 537, 539, 547.

²²⁵ Franke, et. al., 114-15.

structure.²²⁶ The social importance of these groups may have inadvertently hampered political development. Collins claimed these clans played an important role in social identification. Groups were organized around familial relations and location. Such relationships also served as a support system for citizens, leading Collins to observe that “kin-based patronage and reciprocity” sustained citizens during economic downturns. Clan membership provided material goods and social support during periods of Soviet neglect. This led scholars to suggest the president may have exploited these relationships to consolidate political authority.²²⁷ Such actions also explain the state’s lack of political development. Indeed, Collins believed clan identification was detrimental to Kazakhstani’s reliance on national institutions.²²⁸

Yet the precise role of clans following independence remains unclear. Clan-based relationships have played an important role in Kazakhstani society and this type of relationship had the potential to undermine development and growth of official institutions.²²⁹ However, these problems do not sufficiently explain the state’s shortcomings. Murphy suggested that the political clout of national elite and “plain nepotism” explained the Kazakhstan’s political development.²³⁰ Regardless of the source, political leaders have been able to maintain their office while curbing political freedoms. Such behaviors have strongly contributed to the state’s current political climate and may have cultivated a culture of corruption among elites.

Early Power Consolidation

These conditions slowly developed after the state gained independence. The legislative efforts that the regime used illustrate how the regime was able to consolidate its political authority. Kazakhstan initially featured elements of an open civil society. Zhovtis observed that the national media was

²²⁶ Wojciech Ostrowski, *Politics and Oil in Kazakhstan* (New York: Routledge, 2010), 18.

²²⁷ Kathleen Collins, “The Political Role of Clans in Central Asia,” *Comparative Politics* 35 (January 2003): 176; Ostrowski, 18-19.

²²⁸ Collins, 178.

²²⁹ Ibid.

²³⁰ Murphy, 526; citing Edward Schatz.

essentially free of government control for the several years following independence. She also claimed that a degree of tolerance for public associations and independent organizations also existed during this period.²³¹ Olcott also observed that the state had developed a dynamic media and that the national parliament had acted as an effective check on presidential authority during this period.²³² Political growth may have occurred in Kazakhstan, had these institutions continued to develop.

These institutions were soon subjected to government control. In 1997, the government required media outlets to buy “rights to certain frequencies,” and charged exorbitant fees for these licenses. Zhovtis believed such actions shut down non-government media outlets across the country. The regime employed similar tactics to gain control over private groups. A 1998 law forced organizations to pay an enrollment tax in order to gain legal recognition.²³³ The meetings of public associations were also supervised by governmental representatives to ensure their legality. This body of laws had multiple facets which limited the actions and influence of private organizations. For example, it became illegal for a public association to interfere “with the activities of state agencies.” Other provisions penalized coordination with international political organizations.²³⁴ These laws helped the government cement its control over private organizations in Kazakhstan, and restricted organizations that were capable of criticism. Such developments also helped the president establish control over the state.

The regime also manipulated the structure of the national government. The state’s first constitution created a strong central government. As a result, regional officials had little unilateral powers. The regime also chose not to empower regional governors. According to Olcott, a strong central government guaranteed that regions were reliant on the national government to respond to local concerns. This prevented regions with different ethnic compositions from developing an independent

²³¹ Zhovtis, 58.

²³² Olcott, 104.

²³³ Zhovtis, 59, 62.

²³⁴ Zhovtis, 64-65.

power base.²³⁵ This system also allowed the regime to organize the federal government in a way that empowered the national government and enabled the president to control the governing process.

Constitutional reforms in 1995 further expanded the president's control over the state. The 1995 Constitution granted more authority to the Office of the President. Executive orders also became equivalent to law, while the national and regional assemblies lost several political powers.²³⁶ The national Parliament was redesigned to receive legal proposals submitted directly by the president. The regime also ensured supremacy in the national legislature by altering its composition. The new constitution still allotted two senators per oblast; however, the president gained the ability to appoint additional senators to the legislature. The president also gained authority to dismiss the national assembly and to fill important offices. Indeed, the only limitation on presidential authority was illness or treason, which required a majority vote in both legislative houses.²³⁷ Such changes clearly enhanced the scope of presidential authority and further limited opportunities for political opponents to challenge the regime.

Indirect means of consolidation

While the regime used legislative acts to control the state, other factors also enabled the regime to consolidate power. Such factors are distinct because they have strengthened the authority of the regime, without damaging its public image. For example, Bayulgen suggested that foreign investment assisted the regime's efforts to consolidate power. She speculated that international investment in state-owned business can provide a regime with international support, helping ensure the viability of that government. She also speculated that foreign revenues helped such governments survive by influencing "the distribution of power among political actors..." This would imply that investment in

²³⁵ Olcott, 96-97; the decision to establish a unitary state was also intended to prevent Kazakhstan from fracturing along ethnic lines.

²³⁶ Ostrowski, 46; citing Zhovtis, "Freedom of Association and the Question of its realization in Kazakhstan," 1999.

²³⁷ Olcott, 112; Ostrowski, 46; these offices included that of the Prime Minister.

Kazakhstan's oil industry helped President Nazarbayev strengthen his control over the state. However, Bayulgen also observed that the effect of such revenues "depends significantly on the nature of the existing regime."²³⁸ Such revenues appear to have strengthened the autocratic tendencies of the regime.

Revenue generation helped explain the president's ability to consolidate political authority. Bayulgen also noted that foreign capital provided to state-owned businesses or to corporations that rely on government support can create common interests between international investors and political elite, which can undermine calls for political reforms. Moreover, FDI does not necessarily cause investors to advocate for domestic reforms. Rather, corporate concern is likely to be restricted to portions of the legal code that directly affect investment. This led Bayulgen to claim that regimes which receive such investment can employ a "milder version of authoritarian rule" as a means of consolidation.²³⁹

The president was also able to maintain a more tolerant style of autocratic rule by appointing supporters to privileged positions in the government. The president had altered the process of nominating akims, or regional governors, in order to consolidate his authority. The president initially appointed officials who were politically supported by a region, yet when these officials began to act autonomously, the president replaced them with personal supporters who were politically indebted to the president. This enabled the regime to fill political positions with candidates who were less likely to become political opponents.²⁴⁰ Such actions allowed the regime to strengthen its control over regional governments and limited opportunities for political rivals to develop.

Other scholars have observed that the regime was able to utilize subtle tactics to consolidate power. Schatz claimed that "soft-authoritarian regimes" were more likely to employ methods that were designed to win public support rather than resort to overt repression. Such regimes used manipulation

²³⁸ Bayulgen, 53, 52.

²³⁹ Bayulgen, 53-54, 50; MNCs were concerned with "a stable regulatory environment" and "strong property rights."

²⁴⁰ Ostrowski, 51; these 'lieutenants' were also replaced frequently to prevent them from becoming political rivals.

and constructed “images of state and society” to gain public support. This behavior allowed the regime to avoid traditional means of control. Instead, the regime could limit the development of opposing narratives instead of having to confront them. Schatz claimed the Nazarbayev regime was adept at this type of narrative construction.²⁴¹ Such conditions suggest that indirect methods and even investment enabled the regime to establish control over political life in Kazakhstan.

The regime was able to deploy these indirect means to influence public opinion in Kazakhstani society. Nurbulat Masanov, a prominent political opponent, was belittled as a puppet for foreign governments and for his alleged support “of the west’s agenda.” This allowed the regime to cast doubt on Masanov’s intentions and to undermine his political arguments. Schatz also observed that the national parliament would casually, with presidential backing, propose stringent legislative acts which the president could veto in order to present himself as a “champion of moderation.” Schatz believed this behavior weakened the legitimacy of political challengers and enabled the regime to avoid direct means of repression.²⁴²

The regime also employed indirect means to influence the outcome of national elections. Elections conducted in 1999 were considered impartial, “but not without irregularities.” For instance, Akehezan Kazhegelden, a former Prime Minister who joined an opposition group, was arrested after declaring himself a candidate for the national assembly. These actions led Western delegates of the OSCE to describe the election as extremely unfair.²⁴³ The speed with which these elections were conducted was also problematic. Elections that were scheduled for January 1999 were actually held in early October of the preceding year. Olcott claimed this was intentionally designed leave opposition figures with an insufficient amount of time to mount an effective challenge. The regime also added

²⁴¹ Edward Schatz, “Transnational image making and Soft Authoritarian Kazakhstan,” *Slavic Review* 67 (Spring 2008): 50-52.

²⁴² Schatz, 53-54.

²⁴³ Olcott, 122-23.

prohibitive qualifications to candidate requirements. A candidate was expected to gather 120 thousand signatures, pass a language test, and provide a USD 3000 registration fee.²⁴⁴ These additional qualifications helped the regime manipulate the electoral process to their advantage.

Yet it should be noted that President Nazarbayev maintains a degree of legitimacy and even popularity in Kazakhstan. According to scholars, the president's term was legally extended through "a referendum and a series of parliamentary votes."²⁴⁵ Many Kazakhstani view the president as well intentioned. A journalist reported that citizens considered the president a preferable alternative to the Soviet Union, even if he was a corrupt leader. Others were not concerned by rumors of corruption, claiming the president "cares about the people and does things for the country." Likewise, many assume that if the state is rich with natural resources, then the president should be equally wealthy.²⁴⁶ Such statements suggest that international criticisms of the regime are not relevant in Kazakhstan, as average citizens appear to be content with the regime's leadership.

It is possible that the regime's ability to avoid use of repressive tactics has mitigated public criticisms of the regime. Nevertheless, freedoms for opposition figures are curtailed. Olcott observed that Kazakhstan featured an empowered presidency, while political dissidents face stringent restrictions on their activities.²⁴⁷ Yet such conditions do not appear to concern average citizens. If the regime's only interaction with society was repression of political opponents, it could not maintain popularity. These conditions indicate that the regime has found ways to generate political support among Kazakhstani citizens. Such efforts also provided the Nazarbayev regime with legitimacy.

Corruption

Corruption presents a serious challenge to political development around the world. A definition of corruption is necessary to explain the actions that members of the president's family have taken, and

²⁴⁴ Olcott, 119, 120.

²⁴⁵ Hill, 2.

²⁴⁶ Starobin, 102.

²⁴⁷ Olcott, 123.

how they qualify as corruption. A brief examination of corruption will also explain how this problem affects political development. Transparency International defined corruption as the misuse of authority to accrue personal advances.²⁴⁸ Other scholars defined corruption as a relationship amongst parties in which one seeks to “influence the allocation of resources” and as the abuse of shared responsibility for individual means. Such behavior has repercussions on political development because it establishes an informal alternative to official channels and undermines official institutions.²⁴⁹ Thus, while details vary, it is evident that corruption involves the misuse of government authority to benefit one’s self. Moreover, corrupt actions appear to empower individuals at the expense of the state. This can generate mistrust and cynicism towards a government and may ultimately undermine the legitimacy of the state.

Elements of corruption are present in Kazakhstan. For instance, journalists have expressed concern over the management of the national oil fund, which is currently supervised by associates of the president and whose expenditures are not clearly earmarked.²⁵⁰ Likewise, the ERBD ranked Kazakhstan 22nd of 27 “transition economies” that suffer from corruption. Other surveys found that as much as five percent of business returns were used for bribery. Other scholars characterized Kazakhstan as being one of “the world’s most corrupt and ineffective states.”²⁵¹ Corruption clearly represents a serious problem in Kazakhstan. The lack of transparency and misuse of authority that corruption entails poses serious political challenges to affected states.

²⁴⁸ Transparency International, “Introducing Corruption in the Private Sector,” in *Global Corruption Report 2009, Corruption and the Private Sector* ed. Dieter Zinnbauer, Rebecca Dobson and Krina Despota (New York: Cambridge University Press, 2009), 7.

²⁴⁹ Kwok and Tadesse, 767; Transparency International, “The International Dimension: corruption in a globalizing and diverse economy,” in *Global Corruption Report 2009, Corruption and the Private Sector* ed. Dieter Zinnbauer, Rebecca Dobson and Krina Despota (New York: Cambridge University Press, 2009), 47.

²⁵⁰ Lutz Klevevan, *The New Great Game: Blood and Oil in Central Asia*, (New York: Grove Press, 2003), 89.

²⁵¹ Michael Kaser, “The Economic and Social Impact of Systemic Transition in Central Asia and Azerbaijan,” *Perspectives on Global Development and Technology* 2 (2003): 464-65. Maureen Crandall, “Low Grades For Petro-States in the former Soviet Union,” *Journal of Third World Studies* 24 (2007): 196-97.

The regime was able to consolidate political power through corrupt actions. This consolidation was manifested in two ways. The first method involved the sale of state assets to foreign investors. The second method of power consolidation developed through the control that president's family as able to assert over sectors of the national economy, especially the oil sector. This suggested that the regime and other members of the national elite engaged in corrupt actions, which allowed them to amass a personal fortune. The regime's ability to directly affect the national economy in this fashion also influenced political development.

The privatization process was heavily criticized as corrupt. Analysts observed that most business deals were made without public scrutiny. Scholars observed that negotiations over foreign business contracts are primarily conducted by the president, whose decision is considered legally valid.²⁵² Olcott observed that the president and his entourage enjoyed an extravagant lifestyle as a result of foreign investment. She recorded an episode in which they spent roughly USD 250,000 while shopping. Likewise, a steel plant with a projected billion dollar "replacement fee" was sold for a significantly lower amount. Rumors suggested President Nazarbayev, who had worked at this plant, also profited from the transaction.²⁵³ Such conditions indicate that the president, his family, and political supporters became wealthy as a result of privatization. Such behaviors would qualify as corruption.

The regime was also slow to issue operating licenses to oil companies. According to scholars, this made corporations susceptible to state inspections, which had the capacity to halt production for those corporations without a license. Yet as of 2005, the legal requirements of these permits had not been ratified by the government, which renders these licenses "impossible to legally obtain." Neither did the government provide guidelines on the application of laws regarding "customs exceptions" and

²⁵² Political Risk Services, 5; Franke, et. al., 124.

²⁵³ Olcott, 139, 160, 140.

foreign investment. This led to an arbitrary enforcement of these laws.²⁵⁴ This behavior allowed the regime to assert control over the oil industry through seemingly legal implementation of vague laws. These tendencies have allowed the regime to further assert control over the oil industry, enriching the state in the process.

Such actions qualify as corruption. Scholars have also defined corruption as actions taken by government representatives that are inconsistent with relevant normative assumptions.²⁵⁵ For example, foreign oil companies in Kazakhstan sought contractual guarantees upon entering the state. Yet as of 2003, investments no longer enjoyed “the degree of protection and contract stability that had been available hitherto...”²⁵⁶ It should be noted that Kazakhstani officials have defined such behavior as a reassertion of state interests that had been unenforceable, yet such behavior would also “violate established norms” of the international community.²⁵⁷ Such actions were likely to empower the regime, by allowing it to further cement its control over the state and over the oil industry. Yet international observers would also be likely to consider the regime’s behavior non-transparent and corrupt.

Corruption among government officials

Corruption among the national elite may also limit opportunities for political reform. Some have observed that members of the national elite exercise a significant level of control over business deals, many of which are made in a non-transparent fashion.²⁵⁸ Scholars also observed that the president occupies a central role in the negotiation of “international business contracts on oil and gas exploration.” The ability of public officials to conduct such negotiations presented several opportunities for corruption. The same scholars also claimed that the government no longer bothers to maintain the appearance of a transparent regime, noting that agreements negotiated by President Nazarbayev

²⁵⁴ Political Risk Services, 5.

²⁵⁵ Wayne Sandholtz and William Koetzle, “Accounting for Corruption: Economic Structure, Democracy, and Trade,” *International Studies Quarterly* 44 (2000): 35.

²⁵⁶ Ahrend and Tompson, 170, 174.

²⁵⁷ Ahrend and Tompson, 172; Sandholtz and Koetzle, 35.

²⁵⁸ Political Risk Services, 5.

“effectively serve as a contract.”²⁵⁹ Business dealings in Kazakhstan are clearly non-transparent, which creates the possibility for corruption among government officials. Such behavior has the potential to limit economic growth. Ahrend and Tompson observed that erratic application of “customs regulations and tax laws” may limit trade opportunities. Such actions are also likely to empower officials who oversee the oil industry.²⁶⁰ Moreover, the ability of officials to behave in this fashion also reinforces government control over the oil industry and allows the regime to assert its political authority.

The government was able to extract concessions by requiring foreign corporations to maintain political connections to the regime. Analysts observed that “a joint venture with a well-connected local partner” is a crucial precondition to entering the state.²⁶¹ Such requirements also created opportunities for corruption. Pomfret noted that many of the regime’s negotiations with US companies involved instances of corruption. For example, officials of major US oil companies were party to legal cases that involved several million dollars that were deposited “through a US intermediary into offshore accounts of senior Kazakh officials.”²⁶² This implied that bribery was essential to establishing a relationship with political elites and that some form of payoff played a role in corporate entry into Kazakhstan. As previously noted the ability of the regime to extract such concessions helped it regulate entry and allowed them to exercise control over the oil industry.

The regime was also prepared to intimidate non-compliant corporations. Scholars noted that low level officials were able to make “life impossible for those without the right connections or unwilling to pay a necessary bribe.” The same scholar observed that smaller “oil-extracting companies were taken over by people from the [center] of the country.”²⁶³ Others observed that such conditions also created

²⁵⁹ Franke, et. al., 125.

²⁶⁰ Ahrend and Tompson, 183.

²⁶¹ Political Risk Services, 12.

²⁶² Pomfret, 866.

²⁶³ Ostrowski, 50-51.

“new opportunities for patronage” by giving national elites the ability provide followers opportunities for financial windfalls and further allowed the regime to establish control over the oil industry.²⁶⁴

Corruption among the president’s family

This behavior empowered the regime and allowed the president’s family to gain influence over areas of the national economy. Dariga Nazarbayeva, one of the president’s daughters, was head of a national media outlet and was active in national politics. Nazarbayeva established “her own political party” in 2005 and led experts to speculate that she was poised to succeed the president if he ever left office.²⁶⁵ Such connections indicate that segments of Kazakhstani society outside of the executive branch are controlled by parties loyal to the president. If Nazarbayeva was able to gain her positions as a result of her father, such conditions may qualify as corruption.

Other members of the president’s family used their political connections to accrue a personal fortune. The president’s son-in-law, Timur Kulibayev, exploited his position in the government for personal gain. Kulibayev was appointed as a vice president of the national oil company after the turn of the century. Shortly thereafter, Nelson Resources, a Canada-based company, purchased a majority stake in several oil fields around Kazakhstan. This caused the “market capitalization” of the company to grow to roughly USD One billion. This growth was significant because the “financial and political forces behind Nelson resources were Kulibayev and his associates.” Such actions certainly qualified as corruption and would be considered an abuse of “collective responsibility for private ends.”²⁶⁶ This behavior also empowered the president’s family and others connected to his regime and enabled them to further expand their control over the state’s natural resources.

This behavior had a wider effect on political development in Kazakhstan. According to scholars, the empowerment of relatives ensured that “power and wealth [stayed] in the family,” which also

²⁶⁴ Franke, et. al., 120; Ostrowski, 51.

²⁶⁵ Michael Andersen, “Dynasties and Dictators,” *Index on Censorship* 34 (February 2005): 146.

²⁶⁶ Ostrowski, 49, 58; Kwok and Tadesse, 767.

empowered the president.²⁶⁷ The president's ability to enrich his associates also allowed the president to create a patronage system with important figures in the oil industry. The regime pursued a similar strategy with appointees to political office. These figures also allowed the regime to establish control over distant regions in Kazakhstan. Such behavior was significant because it allowed the president to use his influence to place supporters in office. Such behavior allowed the president to control institutions which may have produced a political opponent.²⁶⁸

These actions are also considered forms of corruption. As previously noted, corruption can be defined as "the abuse of entrusted power for private gain..."²⁶⁹ The wealth generated by the president's family and associates has originated from a misuse of authority. For example, regarding the regime's interest in smaller oil corporations, government officials realized "that their signature [meant] money, making life impossible for those without the right connections, or unwilling to pay the necessary bribes."²⁷⁰ These actions suggest that members of the president's administration benefitted through improper use of their position. This behavior thus empowered the regime and strengthened its control over the oil industry and over the state.

Yet it is important to note that the regime had already established control over government institutions by the time officials began to act in this manner. Interaction with oil corporations only allowed the president to solidify his position. The regime had moved against independent media groups and oppressed opposition figures throughout the 1990's, effectively limiting political growth in Kazakhstan. Yet the oil industry did not generate significant revenues until 2000.²⁷¹ Thus, oil revenues empowered the regime, but the regime had already begun to display autocratic tendencies. Yet oil revenues assisted the regime in their efforts to limit political opposition by giving it the ability to place

²⁶⁷ Andersen, 146.

²⁶⁸ Ostrowski, 59-60.

²⁶⁹ Transparency International, "Introducing Corruption in the Private Sector," 7.

²⁷⁰ Ostrowski, 50-51.

²⁷¹ Zhovtis, 59-60; Pomfret, 867.

supporters in positions of power. This ability to influence the shape of the government was also a crucial component of the consolidation process. These behaviors further enabled the regime to establish control over the state.

Such behavior is also likely to perpetuate corruption. Scholars observed that rent-seeking led to continued “abuse of revenue from resources for the personal gain of elites.”²⁷² Others observed that regional governors spent their administrative terms primarily accruing personal wealth instead of working to improve the well-being of their provinces.²⁷³ Scholars considered this an indication that “political elites” were isolated from public opinion and from any consequences, as corruption of this magnitude isolated the regime from average citizens. This hindered the state’s political development. Elite control of natural resources allowed the regime to purchase support and undermine opponents. These actions helped the regime maintain control over the state. Such manipulation has limited political development and suggests that further political reforms are “unlikely.”²⁷⁴

Oil Revenues and Democratic Development

These developments indicate that democratic development is improbable in the foreseeable future. The regime’s ability to utilize its wealth to stifle opposition movements has limited the potential for the emergence of a representative government. Yet the broader relationship between oil revenues and political development remains a point of debate among scholars. Ross observed that oil wealthy governments can evolve into “rentier states,” in which revenue from international sources flows to the national government. Such conditions are problematic if the state’s citizens solely take part in spending these rents. Thus, oil revenues can reduce demand for political reform. Revenues enable a regime to spend greater amounts on political support, “which, in turn, dampens latent pressure for

²⁷² Franke, et. al., 126.

²⁷³ Ostrowski, 52.

²⁷⁴ Franke, et. al., 127, 133.

democratization.”²⁷⁵ Others do not consider resource-generated wealth to be harmful. Michael Herb found that revenue rents can be used to develop a “middle class, increase GDP per capita, and drive of other measures of development,” all of which are associated with democratic governments. This led him to suggest that resource-driven growth did not necessarily prevent democratic development.²⁷⁶ Such findings indicate that the impact of such resources may depend on how revenues are spent.

Okruhlik made similar arguments. She noted that, while international groups help finance rentier states, such a definition overlooks the role of politics in economic development. More specifically: “Money does not spend itself. Those acting in the name of the state make decisions and the nature of the regime influences them.” Okruhlik concluded that rentierism theories required elaboration based domestic institutions, which influenced the decision-making process.²⁷⁷ Such findings are consistent with previous observations about the effects of FDI. Bayulgen observed that the effects of this investment were highly dependent on the behavior of the sitting governments. These findings have negative implications for the state, given the regime’s tendency for autocratic rule.²⁷⁸ Such conditions suggest that resource rents and FDI alike have enabled the regime to consolidate power and to limit political reforms in Kazakhstan.

Rentierism in Kazakhstan

Kazakhstan has encountered such problems. As previously observed, the government was successful in attracting investment from abroad. Scholars observed that the state, in addition to other Central Asian republics, attracted the largest levels of rents among CIS states.²⁷⁹ Observers also noted that, as of 2004, roughly USD 29.5 billion was invested in natural resources in Kazakhstan. However, this

²⁷⁵ Michael L. Ross, “Does Oil Hinder Democracy,” *World Politics* 53 (April 2001): 329, 331, 333, 328.

²⁷⁶ Michael Herb, “No Representation without Taxation? Rents, Development, and Democracy,” *Comparative Politics* 37 (April 2005): 297, 300.

²⁷⁷ Gwenn Okruhlik, “Rentier Wealth, Unruly Law, and the Rise of Opposition: The Political Economy of Oil States,” *Comparative Politics* 31 (April 1999): 297, 308; Zhovtis, 62, 64-65.

²⁷⁸ Bayulgen, “Foreign Capital in Central Asia and the Caucasus,” 52.

²⁷⁹ Ross, 331, 333; Ross cited studies by Entielis, Kessler and Levy, and Bazdresch.

investment led to a decline in transparency. Others observed that the state only initiated political reforms that would enable it to draw foreign investment.²⁸⁰ Thus, the state was able to draw investment, however; the reforms that drew FDI did not include efforts to promote political openness. This further suggests the regime used investment as a means of power consolidation.

Rentier characteristics can also be illustrated through taxation levels. Reports by the OECD suggested the state collected “the lowest general government revenue and expenditure as a share of GDP...on 2001 returns.” As Ross observed, oil revenues can offset low levels of tax revenues. This can lead to a situation in which citizens become unlikely to demand governmental reforms.²⁸¹ It is possible that oil revenues have enabled the regime to avoid taxation of citizens. Yet oil rich regimes must find ways to “legitimize their power.” The Nazarbayev regime accomplished this through expanded provisions for retirees and increased social spending.²⁸² Moreover, in speeches made in 2005, the president detailed several policies that were intended to raise incomes and construct new housing complexes, among other objectives.²⁸³ Such programs may be a part of a broader development plan. Yet such conditions may help explain the regime’s popularity and lack of demand for political reform.²⁸⁴

Ross observed that leaders of oil-rich states were able to employ revenues to blunt calls for political reform.²⁸⁵ Others have also expressed concern over the connection between oil revenues and the lack of political development. Scholars observed that political parties in Kazakhstan were weak organizations, unsupported by the general public. Political power was instead based around “former Soviet economic structures and new business groups,” manifested as parties devoted to an individual or

²⁸⁰Political Risk Services, 1; Franke et. al., 120.

²⁸¹ Kaser, 466, 465; these figures were also caused by “an extensive shadow economy;” Ross, 332.

²⁸² Franke, et.al, 127.

²⁸³ Hill 7.

²⁸⁴ Starobin, 102.

²⁸⁵ Ross, 333.

as oligarchs, all of whom were devoted to the president.²⁸⁶ Perhaps as a result, there were few connections between parties and average citizens. Olcott also observed that few elements in the state appeared capable of creating independent parties. Moreover, opposition parties that are formed are created by the regime and are used to distribute services, but do not function as training grounds for potential leaders.²⁸⁷ Such conditions further establish that the regime is able to control several elements within Kazakhstan's political system, limiting competition as well as opportunities for political reform.

Such problems are intensified by corruption. Pomfret observed that "rent-seeking of the late 1990's" and the actions of national figures rendered political reforms improbable.²⁸⁸ Others have observed that leaders in Kazakhstan are considered to be "among the worlds most corrupt...using bribes, abuse and repression to retain power." They also noted that such behavior disregarded calls for political reforms and had the potential to threaten commerce.²⁸⁹ Pomfret also speculated that resource revenues would either encourage development "with equity or they will enrich a self-perpetuating elite" with the capacities to undermine reforms. It is evident that resource revenues were used to make political leaders wealthy. Such problems will continue to plague Kazakhstan so long as current elites remain in power.

Conclusion

Kazakhstan weathered several challenges following independence, yet the state continues to suffer from problems stemming from its corrupt government. Several international organizations have categorized the state as plagued by corruption. Freedom House Index categorically ranked the state as "not free."²⁹⁰ Such conditions have unquestionably had an impact on the state's political development. Scholars observed corruption in the state has enabled leaders to isolate themselves from the public

²⁸⁶ Franke, et. al., 115-16; see footnote #12.

²⁸⁷ Olcott, 94-95.

²⁸⁸ Pomfret, 872.

²⁸⁹ Crandall, 197; the author applied this description to leaders of all oil-producing states in Central Asia.

²⁹⁰ Lehner, 51.

opinion of citizens.²⁹¹ Such behavior has reduced the probability of political reform. The ability of leaders to enrich themselves through non-transparent means limited the opportunity for a meaningful opposition to the regime to develop.

Yet Kazakhstan's political climate was not exclusively created through corruption. The regime took steps to limit the influence of political opponents almost immediately after the state achieved independence. Legislation passed in the 1990's prohibited citizens from association with "political parties and professional organizations of foreign states."²⁹² Such mechanisms and others allowed the regime to limit opportunities for opposition groups to take part in the political process. Using legislative methods to control opposition groups also allowed the regime to consolidate power and limit the emergence of political challengers.

Oil revenues and FDI further enhanced the regime's control over the state. This occurred in several ways. The investment that natural resources drew lent the regime credibility and helped undermine calls for political reform. Investment also gave the regime the ability empower political allies and enter important sectors of the national economy, most notably the oil sector. Bayulgen observed that regimes receiving investment were able to impose "a milder version of authoritarian rule" without resorting to outright repression.²⁹³ This suggested that revenues allowed the regime to enhance its authority without resorting to force. Such conditions also ensured that foreign corporations would be forced to cooperate with regime and further allowed the president to consolidate power.

Kazakhstan was also categorized as a "rentier state," or one in which wealth that is generated by natural resources is collected and distributed by the government.²⁹⁴ Scholars suggest Kazakhstan has developed into such a state. The national economy improved due to oil revenues, which allowed the

²⁹¹ Franke, et. al., 127.

²⁹² Zhovtis, 65.

²⁹³ Bayulgen, 50.

²⁹⁴ Ross, 329-30.

state to collect a high level of rents.²⁹⁵ Multiple indicators confirm this assessment: tax returns in 2001 were among the lowest levels of government revenue received in former Soviet states.²⁹⁶ As Ross observed, oil wealth states were able to avoid heavily taxing citizens, which in turn, reduced calls for transparency. Likewise, the resource revenues that the Nazarbayev regime collected were used to fund social benefits.²⁹⁷ These conditions suggest that Kazakhstan is developing as a rentier state. Such conditions helped the regime avoid criticism and limited opportunities for further political development.

The Nazarbayev regime displayed autocratic tendencies since coming to power. The regime also managed to prevent political challenges from arising through oppressive, indirect, and subtle means. The regime initially limited political freedoms, through legislation, later appointing political allies to office as a way to maintain control over regional provinces.²⁹⁸ Corruption also allowed the regime to expand its control over political life. Such conditions created a political system which Olcott described as an empowered presidency and opposition groups with strict limitations on their activities.²⁹⁹ Political reforms will not take root until the state has eliminated corrupt practices and reformed its autocratic government. However, such reforms are unlikely. Scholars, in reference to Azerbaijan, noted that “there is no sustainable and democratic alternative to the ruling elites...” Such conditions also exist in Kazakhstan.³⁰⁰

²⁹⁵ Franke, et. al., 122, 119.

²⁹⁶ Kaser, 466.

²⁹⁷ Ross, 332; Hill 7.

²⁹⁸ Zhovtis, 62, 64-65; Ostrowski, 51.

²⁹⁹ Olcott, 123.

³⁰⁰ Franke, et. al., 119.

Chapter V: Conclusion

Effects of foreign investment on Kazakhstan

Kazakhstan's economic growth was astonishing. A state that had been deeply incorporated into the Soviet economy was able to attract nearly USD 30 billion by 2005.³⁰¹ It is also impressive that the state was able draft the necessary legislative reforms that attracted this investment. These reforms helped draw over USD two billion per year to develop Kazakhstan's natural resources after 2001. The state's resources were primarily responsible for the state's growth and helped the state recover from initial setbacks.³⁰² However, there were also negative consequences to resource-driven development. For instance, World Bank officials observed that corrupt behavior has disproportionately benefitted Kazakhstani elite, expanding the gap between the wealthy and impoverished.³⁰³ Effectively, Kazakhstan's mineral resources helped President Nazarbayev and his regime expand their control over the state, distorting political development in Kazakhstan.

Unfortunately, the investment that helped the state achieve this growth may have also contributed to Kazakhstan's political dilemmas. Indeed, the state's political climate encouraged misuse of oil revenues. Bayulgen observed that authoritarian states were particularly suited to draw foreign investment, and were able to bolster their regime as a result. She claimed autocratic states can guarantee limited opposition to corporate entry, and can help foster a stable setting for their investment.³⁰⁴ Moreover, corporations investing in an autocratic state are unlikely to press for democratic reforms within host-states. Bayulgen also observed that investors are likely to only lobby the government on issues related to their investment, particularly guarantees of property protection and

³⁰¹ Akimov and Dollery, 82; Michael Rywkin, "Stability in Central Asia: Engaging Kazakhstan," *American Foreign Policy Interests* 27 (2005): 441.

³⁰² Richard Pomfret, "Kazakhstan's Economy since Independence: Does the Oil Boom Offer a Second Chance for Sustainable Development," *Europe-Asia Studies* (September 2005): 867, 862.

³⁰³ Lutz Kleveman, *The New Great Game: Blood and Oil in Central Asia* (New York: Grove Press, 2003), 86.

³⁰⁴ Oksan Bayulgen, "Facing the dilemma of global capitalism; the case of Azerbaijan," *Central Asian Survey* (June/September 2003): 215-16.

consistent regulations.³⁰⁵ Others even have observed that corporations take care to not challenge an autocratic regime for fear of retaliation.³⁰⁶ Thus, autocratic states can provide an investment context suitable to corporations, who appear to be unwilling to confront this government over broader political issues. Such conditions allow authoritarian regimes to enhance their control over state institutions, limiting political development.

Autocratic states benefit from the structure of foreign investment, particularly FDI. Bayulgen found that FDI helped empower autocratic regimes by providing them with implicit support and by effectively allowing elites to outspend political rivals, which further enabled such governments to maintain their authority.³⁰⁷ Others noted that FDI affected political development. Referring to Kazakhstan, scholars found investment negatively shaped the national economy and the political system, suggesting the “link between politics and economics” was the crucial feature of the regime’s ability to consolidate power. This led the authors to claim oil revenues enabled the regime to establish control over the state and to limit reform.³⁰⁸ Thus, while FDI clearly helped Kazakhstan achieve economic growth, it also enabled the regime to manipulate the political process for its own advantage.

FDI also led to instances of corruption, which further enhanced the regime’s control over Kazakhstan. A key feature of these efforts was the regime’s interaction with the oil industry. Scholars observed that constantly modified regulations, in addition to arbitrary application allowed the regime to extract concessions from the oil industry. The addition of a domestic investor to an international investment group was a necessity in order to enter the state. The regime also appeared to demand

³⁰⁵ Oksan Bayulgen, “Foreign Capital in Central Asia and the Caucasus; Curse or blessing,” *Communist and post-Communist Studies* 38 (2005): 54.

³⁰⁶ Lars H. Gulbrandsen and Arild Moe, “Oil Company CSR Collaboration in ‘New’ Petro-States,” *Journal of Corporate Citizenship* (Winter 2005): 56.

³⁰⁷ Bayulgen, “Foreign capital in Central Asia and the Caucasus,” 52, 67.

³⁰⁸ Anja Franke, Andrea Gawrich, and Gurban Alakbarov, “Kazakhstan and Azerbaijan as Post-Soviet Rentier States: Resource incomes and Autocracy as a Double ‘Curse’ in Post-Soviet Regimes,” *Europe-Asia Studies* 61 (January 2009): 120; the author was also referring to Azerbaijan.

bribes before allowing investors to develop state resources.³⁰⁹ The regime's efforts to extract concessions are indicative of its attempts to gain control over the oil industry. The ability to draw such revenues has also helped the regime establish control over the state.

Scholars have also recorded multiple episodes in which members of the regime were able to assert control over the state itself by using corrupt practices. For instance, the president directly selected regional governors and chose from supporters that were indebted to the president. These administrators usually spent their terms fleecing the region instead of serving public interest. Such conditions qualify as corruption. Scholars have defined corruption as activities that determine distribution of state resources in addition to the "abuse of public or collective responsibility for private ends."³¹⁰ Moreover, these officials allowed the president to limit the emergence of political figures who could challenge the regime by ensuring appointees were loyal to the president.³¹¹ Thus, the regime's ability to appoint these ministers was the result of a corrupt process and allowed it to further establish control over the state.

Such conditions confirm that oil revenues had a strong influence on political development in Kazakhstan. Resource development has a profound effect on political systems. Development contributed to "illegal rent-seeking behavior," while permitting these states to project an image of perpetual growth, which reduced calls for political reforms. Thus, scholars claimed that a "rent-seeking orientated policy" allowed the president and the regime to provide political allies with lucrative opportunities.³¹² Oil revenues effectively allowed the regime to reward supporters while simultaneously disenfranchising

³⁰⁹ Political Risk Services, "Kazakhstan: Country Conditions, Investment Climate," *Political Risk Services Group* (May 2005): 12; Pomfret, 866-67.

³¹⁰ Chuck CY Kwok and Solomon Tadesse, "The MNC as an agent of change for host-country institutions: FDI and corruption," *Journal of International Business* 37 (2006): 767.

³¹¹ Wojciech Ostrowski, *Oil and Politics in Kazakhstan* (New York: Routledge, 2010), 51, 50.

³¹² Franke, et. al., 123, 120.

opposition. These revenues also contributed to the state's culture of corruption and have allowed the regime to delay political development.

These conditions indicate that Kazakhstan has become a rentier state, or one in which revenues are collected from international groups by state governments. According to Ross, such states collect enough revenue from natural resources that they can avoid high taxation levels, and reduce calls for accountability. Observing Middle Eastern states, Ross noted that oil rich governments can develop budgets that are not constrained by the domestic tax base, which enhanced their ability to reduce oppositional threats.³¹³ Others observed that such conditions tend to dampen democratic development. Traditionally, "independent middle and labour classes" are necessary components of democratic reforms. Yet in a rentier state, these groups are replaced by recipients of rentier wealth and are dependent on "rent opportunities" as a result.³¹⁴ Such patterns are prevalent in Kazakhstan.

The state had collected a minimal amount of revenue from 2001 tax returns and, as previously observed, by 2004 the state collected almost USD 30 billion in foreign investment.³¹⁵ Such conditions certainly indicate that the state was able to draw significant levels of investment, which are likely to influence political development. Moreover, the regime also implemented social policies which provided citizens with expanded services. For example, President Nazarbayev referenced government programs in a 2005 speech that were designed to raise government salaries and to create "new housing programs..."³¹⁶ It is probable that economic rents expanded the regime's ability to carry out such policies. Ross categorized such activities as a "spending effect" of rentierism, or one that allowed the regime to spend greater amounts on political supporters, which reduces calls for democratic

³¹³ Michael L. Ross, "Does Oil Hinder Democracy," *World Politics* 53 (2001): 329, 332, 334.

³¹⁴ Franke, et. al., 112.

³¹⁵ Michael Kaser, "The Economic and Social Impact of Systemic Transition in Central Asia and Azerbaijan," *Perspectives on Global Development and Technology* 2 (2003): 466, 465; Political Risk Services, 1.

³¹⁶ Fiona Hill, "Whither Kazakhstan," *the National Interest* (October 2005): 7.

transitions.³¹⁷ Such conditions indicate that Kazakhstan has become a rentier state, whose government is able to subvert calls for political reform.

Effects of resource-driven economic growth on political life

However, it must be observed that the regime had already displayed autocratic tendencies prior to the oil industry takeoff. Scholars observed that the regime took steps during the 1990's to establish control over independent social groups and over the media itself. The oil industry did not generate significant revenues until 2000, at the earliest.³¹⁸ This indicated that the regime had already begun to consolidate power prior to oil industry growth. The oil boom also allowed the regime to alter power consolidation methods; resource revenues can enable a government to lower taxes and reduce calls for political participation.³¹⁹ Thus, resource-generated revenues may allow a regime to increasingly control a pacified public. Scholars have connected this trend to foreign investment. Bayulgen suggested that FDI had the capacity to shape power distribution, which, in turn, had the potential to empower autocratic leaders. This led her to conclude that the effect of such investment depended on the behavior of the regime receiving investment.³²⁰ Such effects indicate that foreign investment allowed the Nazarbayev regime to enhance previous efforts of power consolidation.

These conditions also enabled the regime to maintain a degree of popularity among Kazakhstanis. Reporters found that, the president is assumed to act in the state's best interest, and citizens are unconcerned by charges of corruption, assuming that if the state possessed wealth, then "the head of state must be rich, too." Citizens also claimed that alternatives to Nazarbayev were more likely to be corrupt and that conditions in neighboring states were noticeably worse.³²¹ Such claims may

³¹⁷ Ross, 333.

³¹⁸ Zhovtis, 59, 62; Pomfret, 862.

³¹⁹ Ross, 329, 332; this was a characteristic of a rentier state.

³²⁰ Bayulgen, "Foreign Capital in Central Asia and the Caucasus," 50, 52.

³²¹ Paul Starobin, "Sultan of the Steppes," *Atlantic Monthly* (December 2005): 102; these claims were made by citizens living near Uzbekistan.

indicate that the regime's use of non-repressive tactics created a degree of tolerance among citizens. Likewise, the regime's ability to spend revenues on development projects may have also generated popularity among Kazakhstanis. This context would seem to suggest that the regime successfully placated citizens, potentially reducing public critique of the regime's performance.

Effects of resource dependency on long-term growth

Such conditions exist because oil revenues led to rapid economic growth. Yet this type of growth is not sustainable. Pomfret observed that development spurred by natural resources tended to have negative ramifications on long-term economic growth. He suggested that resource-generated growth was vulnerable to Dutch disease, price swings on global markets, and "rent seeking and distortion of institutions." Pomfret did not consider Dutch disease to be a major threat to the national economy as of 2005; nevertheless, he suggested the corresponding increase in currency value may prohibit growth in non-resource sectors that could have developed otherwise.³²² For instance, US Company, Philip Morris' investment in a Kazakhstani tobacco company was the only significant investment that was not intended to develop the state's natural resources.³²³ Such investment patterns indicate that investors are primarily interested in the state's natural resources. When these resources are depleted, there is no guarantee that the state will be able to maintain economic growth.

Likewise, oil traded on the international market is appraised by a plethora of concerns, any of which may impact prices. Such fluctuations can have a significant impact on domestic policy. Price changes may enrich a state, yet rapid devaluation would also damage that state's economy. Given these conditions, it is significant that Kazakhstan's national economy began to improve following a price uptick in 2000 and expanded further in 2007 and 2008 following another increase in the cost of

³²² Pomfret, 863, 871.

³²³ Political Risk Services, 8-10, metallurgical resources did attract moderate amounts of investment.

oil.³²⁴ Kazakhstan benefitted from a rising cost of oil, yet such resource dependency can be precarious. Pomfret claimed reliance on revenues generated by high prices can negatively impact a state if it is not prepared to properly invest such gains.³²⁵ The volatility of such revenues can pose serious problems for states that are resource dependent. Kazakhstan's reliance on such revenues could lead to a crippling downturn if oil markets collapsed.

Rent-seeking among elites also poses serious problems to the state, and has the potential to impact economic growth. Scholars have identified several rentier mechanisms which influenced development factors. They expressed concern that rent-seeking would cause a state to delay diversification of the national economy and were also concerned that the level of revenue generated by natural resources would allow a state to maintain a false impression of economic viability.³²⁶ Dependency on a single resource would lead to an economic crisis if the oil market were to collapse. In this context, it is significant that other economic sectors in Kazakhstan had not performed as well as the oil industry and, in spite of government efforts to encourage investment; non-oil sectors only attracted a small amount of investment in 2005.³²⁷ Such conditions demonstrate that Kazakhstan is heavily reliant on its oil industry. A negative shock to this sector would have serious consequences for the Kazakhstani economy.

Effects of resource dependency on political development

Scholars also expressed concern was that wealth generated through investment would contribute to "illegal rent-seeking behavior." More specifically, scholars worried that the state's ability to attract rents would reduce the need for taxation, isolating leaders from the population and enabling them to pursue "individualistic, rent-seeking" policies.³²⁸ Bayulgen made similar observations about

³²⁴ Pomfret, 867; Arystanbekov, 64.

³²⁵ Pomfret, 871.

³²⁶ Franke, et. al., 123.

³²⁷ Pomfret, 870.

³²⁸ Franke, et. al., 123, 125.

politics in potential rentier states. She noted that leaders of states which used resources to attract rents were more likely to develop methods of autocratic governing, as rents also helped the state draw revenue from an active oil industry.³²⁹ Given these concerns, it is significant that agreements between the regime and foreign oil corporations were largely conducted by the president, whose unilateral decisions were considered legally valid. This was considered to be a defining feature of rentier states.³³⁰ These conditions indicate that Kazakhstan developed features of a rentier state. Such conditions were likely to enhance the regime's ability to control political life in Kazakhstan. Restricting the regime's ability to collect rents will be a crucial step towards establishing a representative government.

Pomfret also observed instances of corruption, in which investing corporations made discrete payments to members of the regime. For example, an executive for Mobil was imprisoned in 2003 because of "tax evasion" for payments he received from the sale of his stake in the Tengiz oil field.³³¹ Others have defined this as a primary form rentierism, in which state revenue is specifically generated by resources. They observed that such states had a greater chance of becoming autocracies, as only a minority of citizens was involved in collection and dispersal of rents. Scholars also expressed concern that the ability to attract such rents contributed to corruption, as it encouraged the misuse of rents for private profit.³³² Such conditions have allowed the Nazarbayev regime to profit from oil industry development. This empowered the regime and enabled President Nazarbayev to consolidate power and prevent political development.

Conclusion

To conclude, Kazakhstan was able to achieve an astounding level of development after gaining independence. The state's oil resources helped the state attract investors, and it was the development of Kazakhstan's natural resources that propelled economic growth. However, the effects of this

³²⁹ Bayulgen, "Facing the dilemma of global capitalism: the case of Azerbaijan," 216.

³³⁰ Franke, et. al., 124

³³¹ Pomfret, 866.

³³² Franke, et. al., 111-12.

development have had a profound impact on the state. Kazakhstan's dependency on oil has the potential to undermine the state's economic success. For instance, the effects of Dutch disease may also decrease the productivity of non-oil sectors, which may also require substantial state assistance to encourage growth.³³³ Thus, despite the growth that the oil industry created, over-reliance on these resources may ultimately damage the Kazakhstani economy.

There were also political ramifications to this development. The state's ability to attract investment empowered elites to pursue rents and created a culture of corruption.³³⁴ As a result, President Nazarbayev and his regime, which had already passed autocratic measures, were able to consolidate their hold over political life and effectively stifle political development. Foreign investment and oil revenues also contributed to these developments. According to Bayulgen, this investment enriched state leaders and provided them with legitimacy they might not have otherwise attained.³³⁵ Kazakhstan developed features of a rentier state and its political leaders succeeded in undercutting opposition and further ensconcing itself in a position of power.³³⁶ Such conditions are likely to persist until Kazakhstan's resource-driven growth is threatened. This may finally lead Kazakhstanis to demand political reforms from their traditionally non-responsive government.

³³³ Pomfret, 860, 863, 871.

³³⁴ Franke, et. al., 125; the authors applied this description to all "post-Soviet rentier states."

³³⁵ Bayulgen, "Foreign Capital in Central Asia and the Caucasus," 50, 52.

³³⁶ Franke, et. al., 125; the authors describe the ability of the president's family to influence business and political development.

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