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The political economy of mineral resource use: The case of Kyrgyzstan

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ABSTRACT

Effective and sustainable management of mineral resources is one of the key public policy objectives of developing countries. Kyrgyzstan, one of ex-Soviet Central Asian countries, is a perfect example which struggles forming reliable policies as well as a mining industry after shocking political and social movements. In the shadow of several coup d'état attempts, international pressures from regional powers, and ethnic clashes, the government has developed vast administration reforms regulating social and economic changes besides resource management. Policy making in mineral resource management depends upon interim governmental establishments, prior use of the locals, and attributes of the resource. Mineral-rich Kyrgyzstan's initial and current problems' impact on public policies and legislations of resource management provides a case study explaining the emergence of such tools. Utilizing institutional theory as the theoretical background, the study offers perspectives from other Central Asian countries, which contributes to comparative policy analysis literature.

1. Introduction

Mineral resources play an important role in the state development plan of Kyrgyzstan as in other developing countries with mineral resources (Sachs, 2008; Madykov and Ten, 2009; Kyrgyz Ministry of Economy, 2014). Despite being a small country of 5 million, Kyrgyzstan has struggled to establish efficient and effective regulations and norms to manage its mineral resources industry. After its independence from the Soviet Union in 1991, Kyrgyzstan emerged with an underdeveloped and underinvested mineral industry. In 1990s Kyrgyzstan tried to attract international aid and investments to resolve the fiscal crisis it found itself in, as intergovernmental financial transfers from Moscow halted suddenly. Having to deal with several constitutional crises and two regime changes in 2000s due to mass social discontent, Kyrgyzstan has missed the opportunity to benefit from the recent world commodity price increases in copper, gold, silver, uranium, mercury and other rare metals (Rickleton, 2011). However, it is not too late for Kyrgyzstan to improve its mineral resource management policy and practice.

After transition to a parliamentary system in 2010, national leaders in Kyrgyzstan have been focusing precisely on this issue—development of the mineral resources industry. The mining industry accounts for more than 40% of Kyrgyzstan's exports and 10% of its GDP (Khamidov, 2011). In 2012 Kyrgyzstan was a major producer of mercury and uranium in the world and gold was the primary mineral resource in terms of its value for the Kyrgyz economy (Safirova, 2014). In 2013, Kyrgyzstan exported raw gold worth $749 M (10.4% of GDP) and radioactive chemicals worth $56.1 M (0.8% of GDP) (Observatory of Economic Complexity, 2013). On average, Kyrgyzstan produced 16,600 kg of gold every year during 2008–2012 (Brown et al., 2014).

Given the importance of mineral resources for economic development in Kyrgyzstan, it is important for policymakers and the public to understand the political economy of property institutions that would aid effective utilization of mineral resources. When managed poorly, rich resources are not benefited by the governments and people of Kyrgyzstan, if not wasted all the way. On the other hand, successful utilization of mineral resources depends on many factors including the nature of resources, relative fluctuations in world market prices, domestic and international political interests, and types of governance institutions (Libecap, 1989; Collier, 2010).

Hence, this study attempts to answer the following questions: what are the factors affecting the emergence of institutional rules and political norms for management of mineral resources in Kyrgyzstan? Can Kyrgyzstan change these institutions to develop policies and practices for more efficient and sustainable use of resources? Exploring answers to these questions has a potential to yield useful insights for scholars and policymakers in Kyrgyzstan and beyond.

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2. Theoretical approach

This study applies the institutional theory to understand the case of Kyrgyzstan. Institutions are formal rules and informal norms that enable and constrain human cooperation (North, 1990). Depending on the quality of institutions that govern cooperation among individuals and groups, mineral resources can be either put to efficient use or be dissipated. Libecap (2007) and Ostrom (1990, 2005) argue that institutions that are based on prior use and local conditions serve best for efficient and sustainable exploitation of a mineral resource because private owners and local community members have an incentive to ensure the long-run sustainability and profitability of the resource. In other words, both of the authors argue against the allocation of property rights by the central government. Libecap's (2007) institutional theory is influenced by the case of the United States, where historically prior use and local conditions has meant private ownership and use before the reach of the central government. Ostrom's (2005) institutional theory is derived by studies in most of the developing countries in Africa and Asia, where prior use in modern history has typically meant community ownership and use in which a group or a community of individuals in a local setting were owners, until colonial governments instituted private ownership. In post-Soviet Kyrgyzstan, however, prior use means state ownership and use guided by the policies of the Communist Party of the Soviet Union. Once some means of rules and norms regarding property ownership are established, they are hard to change (Libecap 1989), as Kyrgyzstan has experienced in its attempts of institutional reform after independence in 1991 (Honkonen, 2013).

Ostrom (2005) sets out four steps for the emergence of policies and institutions. First, natural characteristics of the mineral resource partly determine the rules and norms governing the exploitation of the resource. Some minerals are more easily exploitable than others; happen to exist in inhabited or uninhabited areas and in near or remote regions; and some resources are more lootable than others. The natural characteristics of the resource are also linked to the technology for exploration and exploitation of the resource. For instance, open-pit and high elevation gold mining requires more intensive technology than close-pit, low elevation gold mining does. Information about mineral resource endowment and use can depend on the characteristics of the resource, as it is hard to know if the mines are located in remote areas that are hard to reach or away from public purview. Challenges in obtaining, processing, and exporting gold can thus have different developmental effects than those of coal and other heavy earth minerals (Libecap, 1989; Collier, 2010).

Second, relative changes in world commodity prices affect the evolution of property rights over resource ownership and utilization (Libecap, 1989). Higher world market prices can bring strategic importance to a specific mineral resource which can lead to stricter state control or even nationalization of the exploitation and production procedures. If the state does not have access to capital and technology, then it might be required to adopt market friendly policies and institutions to attract private investors and firms that are capable of exploiting the resource. For instance, as will be discussed later, gold prices have increased for most of 2000s and attracted much attention from investors and politicians alike.

Third, ethnic homogeneity and/or ideological congruity can lead to more effective rights and norms, since property rights are valid only if they are respected by the people who agree on it and protected by the state. High level of heterogeneity of the community in terms of language, culture, and beliefs can create tensions over the creation and enforcement of property rights for resources. If communities cannot agree on policies due to ethnic or cultural differences, then it might also create disputes with respect to who owns and what policies should govern the use of the resource. Individualistic versus collectivist values can also lead to private versus common property rights (Libecap, 1989, 2007).

Finally, rules and norms governing mineral resource use are also affected by vested interests of economic, political, and bureaucratic nature (Libecap, 1989). If economic interests such as investment companies and mining firms are powerful in a country or region, then their preferences as to what kind of property rights should be instituted could be reflected in national mining policy. In contrast to business interests, politicians respond to issues of mineral rights differently depending on the relative power of each constituency. For example, constituencies in mining communities of one region of Kyrgyzstan might be more or less powerful than constituencies in mining communities of another region of the country, and such relative balance of power change over time (Tiainen et al., 2014). With their expertize and experience in the long run, civil servants can also affect property institutions, especially in technical areas such as mining policy, according to the interests of their own bureaus and administrators. It is thus interesting how mining policy and implementation responsibilities were shifted back and forth between the State Agency for Geological and Mineral Resources (SAGMR) and the Ministry of Natural Resources (MNR) in Kyrgyzstan in 2009–2011 in order to change the influence of political, business and bureaucratic interests with respect to the mining industry (Honkonen, 2013).

Although Libecap (1989) provides a general explanation for economic rationale and merits of market mechanisms in mineral resource, private property rights are not a *sine qua non* for efficient and sustainable resource management. There are many countries throughout the world where prior use and local conditions resulted in either community or state ownership. So, it requires a special comparative attention to understand why prior and local conditions differ in concluding settlements. Comparison of Norway and Botswana to Nigeria and Angola tells us that whereas the former had more honest and accountable governance institutions at the outset of resource development and exploitation, the latter had weak and unaccountable governments bringing out conflicts over the control of resource rent (Collier, 2010; Steimann, 2012).

In post-Soviet countries such as Kyrgyzstan where prior use and local conditions signify state ownership and management of mineral resources, governments can take several actions to improve efficiency and sustainability of mineral resource use. Typically, policymakers in such countries might not have enough information and knowledge about the technologies of foreign firms who bring in technology and capital (Baxter and McMillan, 2013). The leaders may fail to negotiate a deal that is viewed as fair by the public. Such leaders are also pressed for revenue in the short run and thus negotiate less profitable deals when the long run is considered. Adopting more transparent Production Sharing Agreements (PSAs) and more equitable tax structures with international companies as well as stronger domestic governance institutions can maximize returns on foreign investments, domestic human capital, and technology transfer. In countries where resources are being squandered because of local hostilities and weak institutions, it is difficult to establish transparent licensing, taxing, and spending mechanisms. Civil society organizations can help creating self-enforcing mechanisms and social norms that foster more social responsibility on the part of corporations and demand for more information and transparency on the part of citizens (Collier, 2010; Tiainen et al., 2014; Kotilainen et al., 2015).

Other factors such as geography of the country, transportation infrastructure, and characteristics of overall economy also have an unavoidable impact on the rules and norms managing mineral resources. While a land-locked country has an apparent disadvantage, it is not necessarily a curse; a rail-road system can be built to facilitate the transportation of goods and people. An