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State intervention in Kazakhstan's energy sector: Nationalisation or participation?

Serik Orazgaliyev

Graduate School of Public Policy, Nazarbayev University, Cambridge Central Asia Forum

A R T I C L E I N F O

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A B S T R A C T

This paper explores the dynamics of state intervention policies in Kazakhstan's petroleum sector between 2001 and 2012. Although the government in this period had become more assertive in relations with multinational enterprises (MNEs), a full-scale nationalisation had not occurred as the state strengthened control over the industry without forcing out oil multinationals. The findings suggest that the increased state intervention in Kazakhstan's petroleum sector was motivated by a rationale of indigenous capacity-building rather than by an exclusively economic rationale of maximising rents. It is often overlooked that the government endeavoured to achieve a greater participation of Kazmunaigas national oil company (NOC) in the domestic energy sector. Contrary to nationalisation, participation doctrine does not prioritise asset expropriation and/or displacing foreign investors. In Kazakhstan, participation strategy facilitated a partnership between the NOC and MNEs with the aim of strengthening local expertise.

1. Introduction

The relationships between resource-rich host countries and foreign investors have always been complicated. There have been periods of the foreign direct investment (FDI)-friendly environment when multinational enterprises (MNEs) were mainly seen as drivers of economic growth, and there have been periods of the spread of 'economic nationalism', characterised by general hostility towards multinationals. The beginning of the twenty-first century was a period of unprecedented rise in global oil prices but also the period of return of resource nationalisation in many oil and gas exporting countries. It was documented that in the last few decades the global energy industry has witnessed the largest number of expropriations (Click & Weiner, 2010).

Resource nationalisation represents a threat to investments, and it is one of the most significant political risk factors for oil multinationals. For example, assets of international oil companies (IOCs) were the first target of nationalisation decree after the 1917 Bolshevik revolution in Russia (Kobrin, 1985). This paper reviews the period between 2001 and 2012, which was not only a period of unprecedented rise in global oil prices but also the time of resource nationalisations in many countries. Governments of Bolivia, Russia, Venezuela, Ecuador and Chad all engaged in resource nationalisation at different levels. Due to the considerable effect that these events had on the global energy market, studies of motivations behind nationalisations have generated renewed interest (Guriev, Kolotilin, & Sonin, 2011; Vivoda, 2009). Understanding the exogenous and endogenous aspects of this

Corresponding author. Graduate School of Public Policy, Nazarbayev University, Astana, Kazakhstan

E-mail address: serik.orazgaliyev@nu.edu.kz.

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phenomenon is equally important for scholars, policymakers and businesses.

Studies on nationalisation policies in Kazakhstan's energy sector focused on economic goals that the government pursued in renegotiating contracts with foreign investors (Domjan & Stone, 2010; Sarsenbayev, 2011). Without rejecting the economic rationale argument, this paper argues that the desire to extract larger rents during the high oil prices is an incomplete explanation for the greater state involvement. Through amendments in the fiscal regulation of petroleum sector, Kazakhstan introduced more advanced taxation system, which substantially increased budget revenues. However, most of the studies overlook that in parallel with this, the government pursued a developmental mission for Kazmunaigas NOC, achieving much visible state participation in energy projects. Thus, developing local expertise was another imperative motivation for state intervention policies in Kazakhstan.

The doctrine of participation, which was first introduced in the Middle Eastern countries in the 1960s (Jaffe & Elass, 2007; Stevens, 2008), aimed at gradual increasing of the involvement of domestic companies and workers to achieve indigenous capacity-building. Similarly, in Kazakhstan, key agreements with foreign investors remained unchanged, and the expropriation of assets did not take place. Instead, the government amended the regulatory regime to tighten the control over the industry and strived to increase the NOC participation as a partner for MNEs in major energy projects. At the same time, changes to the legislation ensured redistribution of rents according to higher oil prices. These policies proved to be less radical compared to what happened in other oil-rich countries.

Competition for energy resources in Kazakhstan, and more broadly in the Caspian region and Central Asia, received adequate attention in the scholarly literature (Akiner, 2004; Dorian, 2006; Ebel & Menon, 2000; Heinrich & Pleines, 2012). However, most of the studies focused on geopolitical competition between the external powers and adopted realist framework of 'the new great game' (Blank, 2012; Stegen & Kusznir, 2015; Zabortseva, 2012), where China, Russia and the U.S. are seen as the main players (Kubicek, 2013; Orazgaliyev, 2017). In particular, China's increased activity in securing energy supplies from the region was well documented (O'Neill, 2014; Swanström, 2005). At the same time, the role of domestic politics and its influence on interactions between governments and foreign investors remain underexplored. Triggers and driving factors behind the increased state intervention deserve closer attention and a broader study of historical events will be helpful to shed light on factors that influenced government policies.

This paper is structured as follows. After reviewing the literature and history of nationalisation in the petroleum industry, this paper examines the events that preceded the switch of the relative bargaining powers in favour of the host government in Kazakhstan. It then focuses on legislative changes and cases illustrating, how and with what purpose, the government exerted greater influence in the petroleum sector. Finally, following the analysis of the expansion of Kazmunaigas in the country's energy sector, the paper draws implications and conclusions.

2. Nationalisation as a major political risk factor for foreign investment

2.1. Nationalisation in the global petroleum industry: Theory

In contrast to the resource-based view (Barney, 1991), industrial organisation scholars emphasise industry-level and country-level risk factors in determining bargaining power variables in MNE–host country relationships (Caves, 1996; Kobrin, 1982). Research on political risk also employed bargaining model for their analysis (Fagre & Wells, 1982; Lecraw, 1984; Vernon, 1971), although, this was mostly limited to studying expropriation risk (Ghadar, 1982; Kobrin, 1980) and the effect of instability on MNE strategies and investment decisions (Brewer & Rivoli, 1990; Kobrin, 1984). These studies asserted that companies might not be able to eliminate risk in their operations, but they can mitigate it by influencing factors that pose risk.

Nationalisation is often defined as one of the categories of political risk. Most of the studies directly link political risk and nationalisation or other interventionist actions by host governments (Brink, 2004; Friedman, 2012; Riches, 2003). For example, Riches (2003, p. 161) presented political risk from the MNE-centred point of view defining it as 'the possibility that stakeholders' politically motivated actions could cause an investment to make less money than had been expected when that investment was made'. However, Neil (1974) adopted a broader view of political risk, linking it to the possibility of production interruptions or loss of MNE's property as a result of host government intervention (expropriation, contract violation, change in regulatory regime) or as a consequence of external factors such as war, civil unrest or economic crisis.

Nationalisation and resource nationalism are related but inherently different concepts. Nationalisation is a process, which manifests itself in the transfer of ownership from private companies (foreign or domestic) to state entities. Resource nationalism is a determination of governments to increase or maintain state control over the exploitation of its natural resources. Resource nationalism often drives nationalisation process although it may not express itself in expropriation as it can refer to efforts to prevent or limit foreign participation (Domjan & Stone, 2010, p. 38). By the way of illustration, Mexico and Turkmenistan are examples of states with limited foreign participation in their respective energy sectors.

The phenomenon of 'resource nationalism' emerged during the second half of the twentieth century. In the developing world, this coincided with the beginning of decolonisation process, where the movement for independence and obtaining greater control over national resources became an ideology. Newly independent states were keen to end their 'colonial relationship' with multinationals, which were usually of the same nationality as the former colonising countries (Kennedy & Tiede, 2011, p. 14). Notably, resource nationalism phenomenon is not only found in developing countries – Australia and Canada, are often mentioned as 'resource-nationalist' countries (Stevens, 2008; Uslaner, 1996).