Economic Factor of Resource Nationalism Policy in Kazakhstan

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Abstract: Such energy resources as oil and gas play a significant role in the socio-economic sphere of a country, especially in the country producing these resources as Kazakhstan. Hydrocarbons can be the reason for people’s prosperity (for instance, such countries as Kuwait, Qatar, Saudi Arabia) and, at the same time, they can cause the so-called “Dutch Disease” (or other negative manifestations of the “Resource Curse”) which paralyzes all other spheres of economy, making the country completely dependent on the export of oil and gas. However, the energy resources affect not only economies; first of all, they have a dramatic impact on politics. Disputes over the oil fields and desire for the possession of energy resources can result in the worsening of relations among the states and sometimes can even be the reason for starting a war (for instance, the Iraq-Kuwait War of 1990, which is also known as the first oil war; and the US invasion to Iraq in 2003).

Key words: National Oil Company (NOC) • International Oil Company (NOC) • Oil strategy • Resource Curse • Resource Nationalism • KazMunaiGaz

INTRODUCTION

Today, the issue of resource nationalism has become significant as in recent years we have been witnessing an increase of such cases all over the world. Kazakhstan is one more example of such policy. Despite the fact that the country has constantly denied that it is following this global trend, the assessment of its recent steps suggests that this is precisely where the country is headed [1]. The case of Kazakhstan is relevant as today the state is becoming a major oil producer. According to the official data Kazakhstan has 5 billion tonnes of proven oil reserves; while expected recoverable reserves are calculated at 15-17 billion tonnes [2]. Today the oil production in Kazakhstan exceeds the level of 67 million tonnes per year (the top fourth producer outside the OPEC). However, it is expected that by 2015 the production will reach 80 million tonnes a year which makes Kazakhstan an emerging energy power in Central Asia. It also should be indicated that the country is one of a few producers which are not expected to reach their peak of crude oil production for at least the next two decades [3]. Thus, the republic owns large reserves of energy resources, that is why it is important what policy Kazakhstan will follow as its political line can affect the world’s overall energy supply as well as the formation of global prices on hydrocarbons.

This paper does not intend to explore whether it is right or wrong to adopt resource nationalism measures and whether it is justifiable for the government to switch to such policy. This paper examines the economic factor of the policy of resource nationalism in general and particularly the economic factor which had impact in the case of Kazakhstan.

Oil as a Strategic Resource: As the World Bank reports indicate, the Republic of Kazakhstan is blessed with significant oil reserves and its substantial progress in the economic transition was reached thanks to its oil wealth [4]. During the 1990s petroleum became a strategic resource for the Kazakhstani economy. This is not due the consumption of a big amount of oil by Kazakhstan, but due to the fact that petroleum constitutes approximately 30 percent of the country’s GDP and makes up for over half of the country’s overall export revenues [5]. An independent analyst Aset Abdualiyev, who holds LLM in Natural Resources Law and Policy and has worked for a number of state bodies including the
Administration of President of the Republic of Kazakhstan and Joint-Stock Company “National Welfare Fund” Samruk-Kazyna in Kazakhstan notices that “out of 67 million tonnes extracted in Kazakhstan last year 7 billion were consumed by the Republic, while 60 million went abroad.” [6]. Thus, Kazakhstan consumes approximately 10 percent of the extracted oil and exports 90 percent. And as the consumption of oil in the country has been more or less stable in recent years, as long as the extraction is growing considerably, the percentage of the exporting oil will definitely increase.

Therefore, one of the factors which encouraged Kazakhstan to appeal to the policy of resource nationalism could be its substantial reliance on the oil reserves. Patrice Dreiski, Special Adviser to the Co-ordinator of the OSCE Economic and Environmental Activities, emphasizes that "oil and gas are the national assets for Kazakhstan, another fact that oil and gas are non-renewable resources and one day they are going to be over” [7]. The head of energy programme at NUPI (Norwegian Institute of International Affairs) Indra Overland also notes that "oil is a strategic and at the same time limited and exhaustible resource, so it (its economic importance) could be one of the factors” [8]. This importance prompted the republic in its attempts to strengthen its position in the energy sector, particularly through the increase of its shares in different oil fields. From the interviews with the experts I have distinguished two main reasons (in the framework of the factor of oil as a strategic resource) which explain why Kazakhstan decided to increase the role of KazMunaiGaz (Kazakhstan National Oil and Gas Company) in the Kashagan oil-field: to develop competitive advantage and capacities of KMG and to establish national supervision over the largest oil-field discovered in the last 30 years.

Aset Abdualiyev notes that "foreign oil companies pursue only one objective to gain a profit; they do not care about other things, while national companies are created for securing national interests” [9]. Of course, such national oil companies as KMG also gain profit, but making profits is not their only and possibly even primary goal. National companies can invest money in unprofitable social projects or projects profitable in a long-term outlook. This distinguishes them from foreign oil companies. Mr. Abdualiyev makes an example of a recent plan of the Kazakhstani government to construct a pipeline which will connect Southern regions of Kazakhstan (which at the moment are dependent on the import of gas from Uzbekistan) to its Western gas-bearing region. The estimates of the total cost of this project range from $ 2.5 to 4 billion; at the same time, its payback period is 30 years; and, because of this long term period "none of the foreign oil companies will agree to this project, as nobody can guarantee them that they will be working in Kazakhstan in 30 years” [10]. However, KMG as a national company, which will not quit Kazakhstan at any circumstances, is easily investing in this “strategic object.” Thus, by participating in such oil-field projects as Kashagan and making profits KMG develops its capacity for investing in various projects inside the country, which would be unprofitable for foreign companies. At the same time, by working in partnership with such oil giants as Exxon, Eni, Total, Chevron, Shell and other oil companies, KMG is learning and improving its managerial and technical capacities.

Another role of the national company is the implementation of supervision over oilfields. For instance, Kashagan is both a large oil and gas field. Often foreign companies, trying to develop oil-fields as quickly as possible, do not pay much attention to the ecological problems and to such issues as extraction of the associated gas. The role of KMG, in this case, is to be in charge of environmental protection and to control the full utilization of the field, so that the associated gas will be also used and its waste will not harm the environment.

Moreover, KMG is called to supervise the expenditure of the consortium and, as far as possible, optimize its expenses. Kashagan is developed in accordance with the Production Sharing Agreement (PSA) signed by the government of Kazakhstan and a group of companies in 1997 (initially comprised of Exxon, Eni, Total, Shell, BG, ConocoPhillips and Inpex) which created a special consortium Agip KCO. The nature of the Production Sharing Agreements is granting the execution of exploration and production activities to a company of the group of oil companies (which is the case with Kashagan) on a compensated basis, [11] which means that after the start of oil extraction the companies are permitted to use the money from produced oil to recover their capital expenditures (CAPEX). Initial CAPEX of the Agip KCO in the Kashagan project constituted 57 USD billion; however, in 2012 Eni (the operator of the project) announced the increase of the CAPEX to $ 136 billion. In one day the cost of the project was increased by 79 USD billion which is more than a double of its initial cost. Aset Abdualiyev notices that there could be the case of so-called “gold-plating” - unjustified expenditures or intentional overstating of costs, "Eni knew that all capital expenditures will be compensated, so it did not care much about these expenditures or even could
artificially overstate them,” that is why, Kazakhstan needed to introduce KMG into the project, which could supervise the consortium and exclude any cases of “gold-plating.” Indra Overland also notes that “the issue of controlling the costs is a very big problem for any oil company” and that such a big increase of CAPEX in the Kashagan project “was a legitimate concern for the government.”

Thus, petroleum is the source of great importance for Kazakhstan. It is the main reason for the relative prosperity of the state and the main drive of its rapid economic development in recent years. Patrice Dreiski notices that because of oil’s importance and its non-renewable nature "the government wanted to establish control and this wish to control is something normal” [12]. Therefore, the strategic role of petroleum in general and willingness to establish control and supervise the adequate use of the oil-fields in particular were (among the others) the factors which encouraged the government of Kazakhstan to adopt resource nationalism.

**High Oil Prices:** From 2003 up until last year we could witness an enormous increase in oil prices from 25 USD per barrel to the historical maximum of 147.3 USD [13]. Toughening of the conditions for foreign oil companies, generally, coincides with the period of unprecedented raise of prices for petroleum. This striking coincidence suggests interconnection of both phenomena.

The reports of International Energy Agency note that all the governments tend to use high oil prices as an instrument to shift the income flows in their favour [14]. My interviewees generally share this point of view. According to Indra Overland, high oil prices had a direct impact on the policy of Kazakhstani government, "they (the authorities) saw that there was a lot of money coming, more than it was expected when the contracts were signed and they felt that they should have a larger share of profits” [15]. Mr. Abdualiyev considers the increase in oil prices to be the most crucial and decisive factor which encouraged Kazakhstan to adopt resource nationalism, "when the government was signing the agreements on Tengiz, Kashagan and Karachaganak the oil prices were much lower. At the same time the cost of oil extraction in Kazakhstan is relatively high (in comparison with the Middle East); and with the price of 20 USD per barrel the companies developing Tengiz oil-field were making profit of only $ 3 from each barrel” [16]. The profit of the companies was not very high, that is why the government did not pay great attention to the conditions of the agreements; however, with the increase of oil prices to 147 USD the companies started to make $ 127 from each barrel, which was the increase of more than 4000 percent of their initial revenues. At the same time, as the analyst Abdualiyev notes, "the oil giants, while setting up the agreements with the government, lobbied the inclusion of a so-called "Stability Clause;” that is to say in the invariability of the Tax Regime which was in action at the time of concluding the agreements” [17]. The Tax Code of the 1990s could not take into account the high oil prices of 2000s and had very low VAT and even if the Code was amended, it would not have affected all the major foreign oil companies operating in Kazakhstan as “the Stability Clause was included into the Concession Agreement on Tengiz and into the Product Sharing Agreements on Karachaganak and Kashagan” [18]. Therefore, while being a major oil producer, the Republic of Kazakhstan was not benefiting from the enormous increase in the petroleum prices. That is why such circumstances encouraged Kazakhstan to appeal to the policy of resource nationalism. Many analysts note that the switch to the policy of resource nationalism in Kazakhstan took place against the background of unprecedented rises in world oil prices and, generally, this switch was aimed at the maximization of benefits. For instance, Joseph A. Stanislaw in his paper Power Play: Resource Nationalism, the Global Scramble for Energy and the Need for Mutual Interdependence notes “with oil passing 120 USD per barrel, producer nations everywhere—from Russia to Venezuela to Algeria to Libya to Bolivia to Ecuador to Nigeria to Kazakhstan—are rethinking their arrangements with oil companies and other partners, seeking to maximize their share of today’s high oil prices” [19]. Although, Patrice Dreiski does not think that high prices promoted the rise of resource nationalism in Kazakhstan as, according to him, “the price is important only for the investors” and “it is the capacity to consider the level of investments,” [20] other interviewed experts believe that there was a connection. I myself share the view of the latter and think that such an increase in petroleum prices definitely had a direct impact on the decision of Kazakhstani government to appeal to the resource nationalism policy. Thus, high oil prices were another factor which prompted the country to take steps towards maximization of the benefits coming from the energy sector. However, as economic diversification of the Republic of Kazakhstan is becoming so essential for the past five years, economic factor of Resource Nationalism is on the way of becoming agenda today.
REFERENCES

10. Ibid.
17. Ibid.
18. Ibid.