New Silk Road: Inside Kazakhstan's Incredible Economic Transformation

By Wade Shepherd
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Suitably, the headquarters of National Welfare Fund Samruk-Kazyna is located in a pair of opulent gold-mirrored towers that rise up from the heart of Astana, the 19-year-old planned capital of Kazakhstan. Standing out stark and meaningfully from the menagerie of futuristic, contorted, anachronistic, and otherwise mismatching architecture of the business district, the choice of color for these towers was no accident, as they house the beating heart of Kazakhstan's economy.

I sat in the reception area of an office of a nearby tower while waiting to do my interview, trying to make sense of a massive chart that hung upon the wall that showed the hierarchy of all of the companies that are under the wealth fund's control. It was a mass of color-coded bubbles that had company names written in them that were connected by lines shooting in all directions to other similarly labeled bubbles, although it probably could have been simplified with a single sentence: "Samruk-Kazyna owns everything."

The business district of Astana. Note the gold towers of Samruk-Kazyna. Image: Ken and Nyetta via Wikimedia Commons

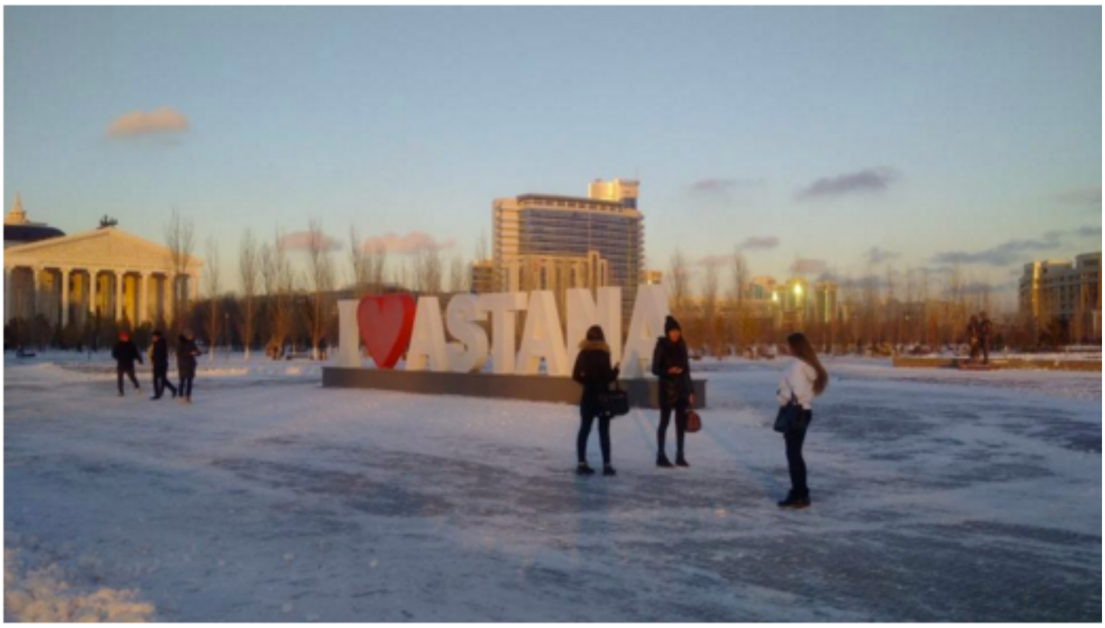
From Kazakhstan's national railway to the state oil and gas company, the state uranium company, Air Astana, multiple banks and financial groups, the national electricity company, the national telecom company, a big energy company, at least three airports, the United Chemical Company, the National Mining Company, the postal service, all the way down to Astana's bicycle sharing system, Wealth Fund Samruk-Kazyna is a majority owner. Samruk-

Kazyna has so many assets, in fact, that it took an all out study to even find out the full extent of what it owned — spiderwebs inside of spiderwebs of subsidies amounting to nearly 600 companies in all.

But one thing that is for certain is who owns Samruk-Kazyna: the Kazakhstan government. However, Samruk-Kazyna isn't really a testament to autocratic communist ethics, but is rather a symptom of such. The fact that the Kazakh government still owns and essentially operates huge swaths of the country's business entities is not viewed as a good thing. Kazakhstan is attempting to fundamentally change the way it operates and does business, and the $100 billion wealth fund was put together in 2008 to better organize the country's assets, increase their profitability, and ultimately manage systemic reform.

Around three or four years ago Kazakhstan saw the writing on the wall: economically speaking, they were simply not competitive in global markets, and continuing to rely on oil and gas for sustenance was a fool's gamble. Kazakhstan understood clearly that Kazakhstan needed to change.

Adamas Illkevicius is in the business of change. He was brought into Kazakhstan as an adviser to Samruk-Kazyna eight years ago. Originally from Lithuania, he refers to himself as an east/west hybrid, having grown up on the cusp of the post-Soviet upheaval and experiencing the inter-generational changes of mentality and culture first hand.



Downtown Astana. Image: Wade Shepard.

"Most of my life was in different types of projects that involved one or another type of change. Taking something and making it different from what it was," he told me. “So delivering change is my specialty. I’ve done it in the West, I’ve done it in the East, and Kazakhstan is one of the countries that wants to have both.”

To these ends, Kazakhstan set itself on an ambitious trajectory. Under the auspices of an initiative called Kazakhstan 2050 the country aims to be among the top 30 developed countries in the world by, you guessed it, 2050. This plan consists of reforming state-owned companies, diversifying the economy away from resource dependency, attracting foreign investment, building world-class transportation infrastructure, sparking vibrant commercial and manufacturing enterprises, and applying international standards throughout.

Kazakhstan doesn’t really have much of a choice but to transform. 62.3% of the country’s economy currently comes from oil, so when prices for the commodity began its free fall in 2014 so too did Kazakhstan. This decline in oil prices combined with low prices in many of Kazakhstan’s other major exports, like aluminum, iron, and copper. Topping this off, economic downturns in Russia and China, Kazakhstan’s two biggest trading partners, meant even less buyers for what the country was selling. This all resulted in a currency collapse that saw the tenge drop from 120 to the dollar at the end of 2013 to 386 in January of 2016, topping off a perfect storm of economic calamities.

While Kazakhstan lived to see another day, its drive to reinvent itself became that much more vital. According to Illkevicius, there are three main objectives to this transformation.

The first is in governance — in devising a new framework upon which decisions are made and how processes are carried out. Kazakhstan is a former Soviet country, and the mentality of a Soviet-style command economy is still very much alive. The lines between ministries and companies remain perilously blurred, often making regulator and the regulated one and the same.

“It’s like a dance,” said Illkevicius, “you chose whether you play the music or you dance for this music. . . Now we are changing this so there is a more consensus and more dialog type of approach, bringing in professional boards, bringing independent directors who can give another opinion, who can challenge decisions, and so on.”

The second objective of Kazakhstan’s economic transition is to evaluate, restructure, and upgrade the country’s business portfolio — i.e. reforming that mess of bubbles and lines on the chart that hung above us. In 2013 Samruk-Kazyna conducted a global study on economic efficiency and discovered that other countries were getting far more out of their companies with the same level of invested capital than they were.

“Because we have more than 600 companies the management is like chemical elements. When you combine some of them they do nothing, others just explode,” Illkevicius said. “So we’re looking where the pieces of our companies can have synergies.”

This endeavor is resulting in similar-sector companies being merged, under-performing companies being liquidated, and the entire economic system being optimized from top to bottom in the pursuit of competitiveness and profitability.

“How many layers of management do we have?” Illkevicius asked rhetorically referring to the diagram of Samruk-Kazyna’s subsidies. We counted them. “So nine levels, which is far too deep. It is like going into deep water, the deeper you go the less you see. So if you are acting out of transparency, for the sake of transparency we need to cut these layers. So that means a massive restructuring of the portfolio.”

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The third objective is to increase operating efficiency, enhance value added, and basically get the most out of the country’s economic ecosystem. This involves cutting off the post-Soviet fat, making assets more commercially oriented — in some cases privatized — with less cronyism in the works and more exposure to market vulnerabilities.

“We’re actively working to change. Change the philosophy of these assets,” Illkevicius said. “Objectives in Soviet times were absolutely different. Nobody thought about profit. It was more like employ as many people as you can, be as powerful as you can, we need to conquer all the world and you have to contribute to this. That was the mantra and everybody was full of it. Now when you look at the economic side of it. Is it profitable? Is it beneficial? Not necessarily. . . We are not squeezing them or sweating them to the levels that normally commercial companies or private companies would do.”

In addition to reforming state-owned companies and the fundamentals of the economy is managed, Kazakhstan has also been taking monumental strides towards developing its non-oil sector. In 2014, Kazakhstan announced its “Nurly Zhol” plan to develop its transportation infrastructure, and new highways, sea and dry ports, and 10 tax-free special economic zones began popping up around the country. The idea is to transform Kazakhstan into a linchpin which physically connects the markets of China, Russia, South Asia, and Europe together — the preeminent crossroads of a New Silk Road. This is an ambition that runs flush with China’s Belt and Road initiative, which seeks to develop an enhanced network of economic corridors spanning across Eurasia from China to Europe.

But in Kazakhstan this large-scale transformation runs deeper than merely cleansing some business practices, reforming a few ministries, and developing a logistics economy. The change that Kazakhstan is going through is systemic; not only impacting the government and business sectors but the culture as well. In many ways it's a generational transformation; a younger generation is coming of age who do not have the hangovers of the Soviet era.

"I think why it is changing is because a new generation has come in, a new generation [who has] less seen this style of Soviet control and kind of military discipline," Illkevicius said. "Many people have been sent to be educated in the West they are returning back and, one by one, they are adding to the workforce, they are adding to the elite that manages the country, that manages businesses in this country. They have already different views. Through internet, they are part of the global thinking machine. For them it's easier when they see a mismatch of how the world generally thinks and how we locally think. If they notice the gap they challenge why there is a gap."

Kazakhstan is a country that is fully aware of what's broken, what's not working well enough, and what needs to be changed. The question moving forward is if the country truly has the capabilities and political will necessary to take its hands off the controls a little and allow the economic transformation to truly seed itself and grow.

Up to here, a large amount of progress has been made. Forbes contributor Kenneth Rapoza called Kazakhstan, "one of the best and more reliable of the frontier markets." And the numbers back this up. In 2012, Kazakhstan was #72 in the World Economic Forum's Global Competitiveness report. In 2015, it was at #42 — a jump of 30 positions in a mere three years. This year, Kazakhstan is slotted at #41 in the World Bank's Doing Business rankings, which is higher than both Belgium and Italy. In terms of on the ground impacts, Kazakhstan's poverty rate has fallen from 47% in 2001 to just 3% in 2013. The Organization for Economic Cooperation and Development claimed that Kazakhstan is currently "well-placed" to catch up with OECD income levels by 2050.

Something is working.

Kazakhstan's economic recession now appears to be on its way out. The tenge has stabilized, commodity prices have risen, the stock market is up, and, after showing stagnant growth this year, Kazakhstan's GDP is expected to start rising again in 2017. A Chevron-led consortium of oil companies recently signed a $36.8 billion deal to develop the Tengiz oil field and the giant Kashagan oil field re-launched in October, as Kazakhstan attempts to enter the top ten oil producing countries in the world.

Kazakhstan is a wonderland where colossal, almost unbelievable transformations can really happen. The view from the window of the tower that I was sitting in confirmed this. The entire city that sprawled out below me — the strange green twisty skyscrapers, the 60 meter tall pyramid, the presidential palace that is an unabashed replica of the White House, the five star shopping mall that was built inside of the world's largest tent, the apartment blocks that house 800,000 people — didn't exist 20 years ago.

On to 2050.

I'm the author of Ghost Cities of China. I'm currently traveling the New Silk Road doing research for a new book. Follow by RSS.