KAZAKHSTAN FACES A CRUCIAL SNAP ELECTORAL CYCLE

Implications of the early presidential and parliamentary elections & President Tokayev's economic reform agenda

22 September 2022

In the next few months, Kazakhstan will undergo one of the most politically tense periods in its post-USSR history, with potentially wide-reaching implications for the future of Central Asia's largest economy. Following a decision from President Kassym-Jomart Tokayev, only the second leader in 30 years, Kazakhs will head to the polls on 20th November to vote in snap presidential elections. The vote will determine whether Tokayev will continue leading the country with a fresh mandate for a non-extendable seven-year term, and will be followed by early parliamentary elections during the first half of 2023.

President Tokayev's decision to call for snap presidential and parliamentary elections caught many by surprise. Officially, Tokayev, who assumed office in 2019 and could have chosen to run for re-election in 2024, made this crucial decision to seek a strong mandate and popular support to implement major socio-economic reforms, including promoting competition and encouraging business activities, alongside other crucial implications for international investors. At the same time, the presidential decision to announce this unexpected electoral cycle comes amid multiple domestic and international challenges faced by Kazakhstan, including disputes within the country's ruling elites following the 2022 January unrest, societal tension and of course the backdrop of Russia's war against Ukraine and its impact for Central Asia.

Below, Aretera provides an analysis and overview of this landmark decision and its implications for international investors.

This memo will cover:

- an introduction into Kazakhstan and the country's political leadership,
- the reasons behind this unprecedented snap election cycle,
- domestic risks capable of impacting the upcoming election period,
- President Tokayev's economic reform agenda and its business implications,
- the international challenges facing Kazakhstan,
- a short-term outlook on the country's political future,
- recommendations for international businesses.

FROM NATIONWIDE UNREST TO SNAP ELECTIONS

On 1st September, Kazakh President Kassym-Jomart Tokayev announced early presidential elections to be held on 20th November and early parliamentary elections within the first six months of 2023. The announcement also included multiple political, economic and social reforms measures aimed at reducing the share of the state in the economy, promoting competition and encouraging private business activities.

President Tokayev assumed office in March 2019 as only the second post-USSR leader of the largest Central Asian state, succeeding his former patron Nursultan Nazarbayev, who ruled Kazakhstan for nearly 30 years.

Citing a need for a new generation of leaders following a series of protests at the time, Nazarbayev resigned the presidency in 2019, allowing his protégé, Tokayev, to assume office as Acting President. Tokayev later won a largely non-democratic snap presidential vote in June 2019. Although having resigned from the presidency, Nazarbayev has held a number of high-profile public positions to maintain his political influence, including the Chairman of the country's influential Security Council for life and a newly created title called *elbasy* (Leader of the Nation).

As his presidency progressed and he assumed a number of other influential public positions previously held by his predecessor, Tokayev's political influence and independence from Nazarbayev have steadily grown. In January, Kazakhstan was rocked by a major, two-week long violent nationwide unrest, triggered by the lifting of state-imposed price caps on liquefied natural gas but fuelled by growing dissatisfaction with Nazarbayev and his enduring influence.

As President, Tokayev imposed a state of emergency, while his security forces used deadly force to crack down on the unrest. The events resulted in Tokayev taking over the leadership of the country's Security Council and the ruling *Amanat* party from Nazarbayev, dismissing several Nazarbayev-linked government officials. The unrest was followed by a constitutional referendum in June that stripped former President Nazarbayev of all post-presidential powers in political decision-making. Additionally, the Kazakh parliament voted to rename the country's capital Nur-Sultan as Astana, as it had been known until the 2019 switch in honour of Nazarbayev.

KEY TAKEAWAYS FROM THE UPCOMING ELECTORAL CYCLE

Tokayev's move to announce presidential and parliamentary snap elections caught several observers by surprise. The President could have chosen to remain in power for two more years and run for re-election in 2024, while the country's parliament, elected in 2021, was set to continue until 2026.

Officially, Tokayev's move was spearheaded by the ongoing constitutional reforms. These include changing Kazakhstan's proportionate parliamentary election system to a mixed electoral system, with 70% of MPs to be elected through party lists and 30% from single-member electoral districts. Even more important is a proposal that would extend presidential terms from five to seven years, with no possibility of extension. The latter is a newly proposed amendment that was not part of the constitutional changes voted upon in the June referendum.

In practice, there could be a number of other reasons for calling an election. While some international observers see the decision as a potential step towards further democratization (in a country that has been generally characterized as an autocracy), it is just as likely aimed at legitimizing President Tokayev and tightening his control over the country's ruling elites. Furthermore, the country's current socio-economic situation, the regional political uncertainty caused by Russia's invasion of Ukraine and concerns over future socio-economic upheavals similar to the protests in January (intra-elite conflicts that might translate into a new unrest) could all have contributed to this landmark decision.

SNAP ELECTIONS AMID GROWING DOMESTIC RISKS

While the snap elections are a political opportunity for Tokayev, they also carry significant risks for the country, since the political and economic situation in Kazakhstan remains relatively unstable.

The 2022 January unrest resulted in large-scale socio-economic upheavals, subsequent changes in the ruling elite and the dismissal of several Nazarbayev-linked figures. However, while the former President was stripped of his political privileges, the country is yet to undergo any significant structural power reset. Kazakhstan's government was only partially renewed, with most ministers remaining in office, while others were promoted to new positions.

Furthermore, Tokayev did not trigger early elections into the lower house of the parliament (*Majilis*) and regional authorities, banking instead on a gradual transformation. To date, the clan governance system retains its influence and functionaries appointed by Nazarbayev continue to hold important offices in the public sector. Trials of organizers of the mass riots that caused the deaths of hundreds of people in January were also not concluded. Combined, these factors constitute a delicate political situation that has the potential to escalate further.

Kazakhstan's economic situation remains challenging. The country's oil-rich and export-oriented economy is visibly slowing down, while the risk of a fall in exports remains high. Most recently, global credit ratings agency S&P downgraded Kazakhstan's sovereign credit rating outlook from "stable" to "negative", explained by potential risks related to the country's oil exports through the Caspian Pipeline Consortium (CPC). Despite relatively high prices for oil, the country's main export commodity, the country's national bank expects an economic slowdown in GDP growth for this year (down to 2.5–3.5% from 2.8–3.8%).

A MASSIVE SOCIO-ECONOMIC REFORM AGENDA

In parallel with the early presidential and parliamentary elections, President Tokayev also announced a series of economic and social reforms, with wide-reaching implications for local and international businesses. These include:

- abolishing administrative price regulations on the competitive market, introducing tighter control over monopolist pricing and a transition to a "tariff-for-investment" policy;
- adopting a new Tax Code in 2023 (envisaging radical simplification of taxation management, digitalizing tax control, differentiating tax rates for various economic sectors and simplifying special tax regimes) and adopting a new Fiscal Code (transferring some tax revenues to the country's regions);
- radically simplifying enterprise regulations (cutting the number of related regulatory acts);

- transforming the Samruk-Kazyna fund (which owns the government sector's key assets) and privatizing most of its enterprises (except for strategic sectors);
- introducing a new model of public-private partnership (including a transparent procedure for concluding government contracts);
- increasing the minimum wage from KZT 60,000 to KZT 70,000 (USD 150), freezing the retirement age for women at 61 until 2028, deferring payments to children from the state budget for education and housing purchase.

The range of proposed reform measures has prompted skepticism that sufficient public resources exist to implement them all. President Tokayev is also forced to rely on some of the old elites, whose loyalty remains questionable in the country's clan governance system. Large scale reforms may run into "implementation problems" and so be delayed or sabotaged.

Low levels of trust in the announced reforms among the old elites might further complicate their implementation. In particular, the Kazakh parliament is currently considering bills that run counter to Mr. Tokayev's statements on taxation, with heavy implications for businesses.

These bills would essentially eliminate the planned simplified taxation system, expand the base for corporate taxes and complicate doing business in the country. It remains unclear how the new tax code would be implemented and whether it would fully replace the current system, adding to uncertainty when it comes to long-term business planning.

The announced reforms, especially those applying to monopolies and asset privatization, may also be primarily motivated by the aim of redistributing economic resources to the benefit of Tokayev's inner circle and reducing the influence of old elites. The attached social measures are likely intended to serve as a background for this redistribution and mitigate any related spike in social discontent.

NAVIGATING IN A CHALLENGING INTERNATIONAL ENVIRONMENT

Kazakhstan's economic challenges are in many ways connected to external factors, primarily the country's difficult relations with Russia and China. These challenges include the technical problems of the Caspian Pipeline Consortium (CPC), the company operating the Caspian Pipeline, a major Kazakh oil transit route from western Kazakhstan to the Russian Black Sea port city of Novorossiysk.

Russia controls the key link in this pipeline system, which has recently experienced major technical problems for the fourth time in a year. Critics say the interruptions of the pipeline flows may have political underpinnings, while the port of Novorossiysk serves as an important trade hub for exporting Kazakhstan's oil to foreign markets.

Aside from the Caspian Pipeline, Astana does not have any other major oil delivery routes, with up to 80% of the country's oil exported via the CPC. An additional concern is that Russia, also a key food supplier to Kazakhstan, periodically imposes restrictions on supplying Kazakhstan (and EAEU states in general) with individual types of food items, citing the need to protect its domestic market.

Russia, however, cannot openly put pressure on Kazakhstan since Astana is a member of the Eurasian Economic Union (EAEU) and the Collective Security Treaty Organization (CSTO), two regional cooperation formats that are crucially important to Moscow. Furthermore, there is virtually no alternative to Kazakhstan for large- and medium-sized Russian businesses and foreign companies looking to relocate from Moscow in order to reduce their sanctions exposure.

Despite these economic ties, however, Russia's war against Ukraine continues to exacerbate differences and increase tension between Moscow and Astana.

Kazakhstan's fears of losing its economic sovereignty stand in the way of developing China-Kazakhstan relations further, but there is no doubt that the country's dependence on its two largest neighbours remains high. As of 2021, CIS states (mostly Russia) accounted for 32.7% of Kazakhstan's foreign trade, while the share of Asian states (mostly China) stood at 32.6%. At the same time, former Soviet republics accounted for over 50% of Kazakhstan's imports (exports of food and raw materials from Russia), while China accounted for 20% (consumer goods, technologies, and equipment).

SHORT-TERM STABILITY CONCERNS

The upcoming electoral cycle in Kazakhstan, the impact of which will likely be felt beyond the snap parliamentary vote planned for the second half of 2023, carries significant medium- and long-term risks for investors in the country.

A key risk to our forecast concerns the potential resumption of protests should the economic situation deteriorate. In this regard, the date of the presidential elections (20th November) could be a turning point, while it cannot be entirely ruled out that the country's old, Nazarbayev-linked elites would use the upcoming vote as an attempt to return to the political arena.

Post-election protests could also erupt as the date of 16th December approaches. marking the anniversary of the 2011 Zhanaozen Massacre, a protest during which striking oil workers were attacked by police, leading to a number of fatalities.

Should Kazakhstan pass through this politically tense period successfully, it could mean a politically stable start for concluding the electoral cycle, with the holding of parliamentary elections during the first six months of 2023.

IMPLICATIONS FOR INVESTORS

As Kazakhstan heads towards the elections, the relatively low legitimacy of the authorities, the ongoing societal tension, demands for structural reforms, as well as exacerbating problems in the economy and external factors, ranging from the global economic downturn to Russia's war in Ukraine and its regional impact, could all increase risks associated with investment decisions in the foreseeable future.

For international businesses, the upcoming period means limited possibilities for planning operations in Kazakhstan since President Tokayev and the various branches of his government will be preoccupied with organizing (and winning) the elections.

Populist decisions, taken to gain the approval of the electorate, could also run counter to the interests of both the economy and the business sector, disrupting strategic plans and economic objectives, including those based on previously reached sectoral agreements with the private sector.

Legislative activities will likely be limited or suspended until a new parliament is elected, essentially until the end of June 2023, potentially jeopardizing Tokayev's reform agenda. Liberalization efforts in the economy could be postponed or even frozen, with a potentially negative impact on the business climate.

This period will also likely bring growing regulatory uncertainty, most specifically an increased amount of regulation from the lower levels of the Kazakh government. From the stakeholders' point of view, the overall configuration of the government and its executive bodies will remain unchanged, with the possible exception of individual reshufflings. However, personnel reshuffles at the executive level could see frequent changes in stakeholders and the disruption of business agreements.

In view of the above risks, international investors in Kazakhstan are recommended to suspend the planning of new strategic projects until the end of the snap election cycle (April-May 2023), constantly monitor and evaluate regulatory developments, actively communicate with government stakeholders and complete contracts for any business projects nearing implementation.

###

If you would like to schedule a discussion of this paper, please contact:
Daniyar Koshenov, Co-Director for Central Asia & the South Caucasus at d.koshenov@areterapa.com

Aretera

Aretera is a leading independent public affairs advisory firm operating across Central & Eastern Europe, Ukraine, Turkey, Central Asia and a growing number of global emerging markets. We advise a wide range of leading multi-national corporations, providing counsel on all aspects of public policy, public affairs and reputation management.

www.areterapa.com