

POLITICAL CRISIS IN KAZAKHSTAN

Changes in the balance of power in Central Asia and the risks for businesses

January 2022

On 2 January 2022, mass protests broke out in a few regions of western Kazakhstan and quickly engulfed almost the entire country. The protests were sparked by the government's decision to stop regulating prices for liquefied gas, which is widely used as automobile fuel as well as for cooking in rural areas, and quickly escalated to armed clashes. The main victims of the protests were the participants in the rallies as well as representatives of the country's security forces and civilians.

There was looting and plundering in large cities, including Almaty, Shymkent and most of the administrative centres of the southern regions of Kazakhstan. Trained fighters and adherents of radical religious movements allegedly took part in the protests. Kazakh President Kassym-Jomart Tokayev announced that other countries were involved in organizing the riots, although he did not specify the countries in question.

On 5 January, Tokayev declared a state of emergency in Almaty and the Mangistau Region (the original hotbed of the protests), which was subsequently expanded to the entire country. The state of emergency was imposed for two weeks and is set to expire on 19 January.

Also on 5 January, Tokayev dismissed the government led by Askar Mamin and announced that he would be taking over as head of the Security Council, which, according to law, was supposed to be headed by first Kazakh President (who has the title Elbasy, "Leader of the Nation"), Nursultan Nazarbayev, for life. Tokayev took over the functions of Chairman of the Security Council without amending the legislation.

Several people close to Nazarbayev were also dismissed, including National Security Committee Chairman Karim Massimov, who was then detained on charges of high treason along with his deputies. These circumstances indicate that an acute conflict has emerged between President Tokayev and at least part of the circle of former President Nazarbayev, who had sought to maintain key levers of power after ceremonially stepping down as President in 2019. In all likelihood, this conflict was one of the main causes of the current political crisis and has contributed to its rapid escalation.

On the same day, 5 January, Tokayev appealed to the leaders of the member-states of the Collective Security Treaty Organization (CSTO; the "Russian NATO" for post-Soviet countries) with a request for "help in overcoming a terrorist threat". This request was granted immediately on 6 January and a CSTO military contingent dominated by Russian troops was sent to Kazakhstan (official data indicates that the contingent consists of 2,500 people). The CSTO troops are helping to

normalize situation in Kazakhstan's capital of Nur-Sultan, Almaty, and other regions. They have also placed the country's key infrastructure facilities under protection.

On 11 January, Tokayev announced that the contingent had completed its main tasks given the end of the active phase of the anti-terrorist operation and that it would start withdrawing in two days (this information has not yet been confirmed by the CSTO Secretariat).

With the CSTO forces entering Kazakhstan, the European Union called for "observation of the sovereignty of Kazakhstan," while the United States demanded that the Kazakh authorities explain the need and ramifications of seeking help from the CSTO. The Chinese Ministry of Foreign Affairs expressed hope that the situation in Kazakhstan would stabilize as quickly as possible and also spoke out against the intervention of external forces potentially provoking violence in the country.

On 11 January, Tokayev delivered a keynote speech to members of parliament in which he outlined the main features of socioeconomic reforms to neutralize the results of the current crisis and minimize the likelihood of a similar crises recurring in the future.

At the same time, he issued a presidential decree appointing former first deputy prime minister Alikhan Smailov as Prime Minister of Kazakhstan (he already led the government in an acting capacity after PM Mamin's dismissal). Parliament approved the candidates of the new government members on the same day (see below for more details about the new government).

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WHAT LED TO THE CRISIS AND THE MAIN POLITICAL CONSEQUENCES

The protests and response by the Kazakh authorities and neighbouring countries, above all Russia, have already led to radical changes in the internal political alignment of forces in Kazakhstan and, more broadly, in the entire Central Asian region. In addition, the crisis will impact the entire post-Soviet space, including at the level of the Eurasian Economic Union (EAEU).

This situation is causing serious changes in the composition and structure of stakeholders (at the national and supranational levels) as well as political and regulatory trends in Kazakhstan and other Central Asian countries, which may require corporate departments to re-calibre their relations with government agencies in the region and approaches to working with stakeholders in order to reduce regulatory and political risks.

The specific triggers for the current crisis in Kazakhstan and its rapid escalation remain unclear. The situation is unfolding quickly and there is still a risk of new exacerbations. In this regard, the ramifications and results of the crisis (how the new political and administrative system will develop in Kazakhstan) are not completely obvious.

However, the following key factors could be the main reason for the socio-political crisis in the country:

- ✦ The dual nature of power in Kazakhstan since 2019, as evidenced by the presence of two centres of influence in the country: the formal one, represented by Tokayev, and the informal, represented by Nazarbayev and his inner circle.
- ✦ Economic problems and declining living standards in Kazakhstan in recent years. Kazakhstan's GDP decreased by 2.6% in 2020 before rising by just 3.4% in January-September 2021. Inflation is accelerating in the country: it was 7.5% in 2020 before jumping to 8.9% in 2021. Growing unemployment in major cities (primarily Almaty) was also a social factor behind the protests. The pandemic, stringent quarantine measures and falling prices for Kazakhstan's main export products in 2020 all led to a significant reduction in household incomes, which have not yet recovered.
- ✦ Major ethnic and religious differences in Kazakhstan's regions (traditional tensions between the country's north and south, as well as the confrontation of clans) combined with other factors have also contributed to a perfect storm scenario.
- ✦ Possible attempts by external players to exploit internal differences between the country's elite. Kazakhstan is traditionally a key focus of Russia and China (its main trade and economic partners with which it shares a border), Turkey (a major economic partner of Kazakhstan), the United States and United Kingdom (given the country's oil and gas assets), and the Gulf countries (investment partnership and a destination for the siphoning funds out of the country).

The events in Kazakhstan generally came as a surprise to observers and the expert community considering that over the past ten years protests were sporadic only and not particularly widespread. The current crisis can be attributed to a build-up of factors that have exacerbated internal tensions among the elite due to the transfer of power (broadly to different groups of elites associated with Nazarbayev), the country's economic problems caused by COVID-19, the slowdown of the economy and the involvement of radical religious groups.

Even though the acute phase has passed, the crisis in Kazakhstan continues to unfold, albeit with less intensity. The protests, outbreaks of street violence and actions of illegal armed groups have been stopped in most of the country, while anti-terrorist activities continue in certain regions of southern Kazakhstan.

Despite the intense dynamics of the events, certain conclusions can already be drawn about the ramifications of the crisis, which are also significant from the standpoint of revising the priorities of the government relations function of companies operating in the region:

- ✦ The end of dual power in Kazakhstan and ousting – partial, at the very least – of former President Nazarbayev's entourage from power.
 - ✦ It is safe to say that the positions of President Tokayev have strengthened within the country due to the limitation (as a first step) of the political influence of Nazarbayev's entourage on domestic political life in Kazakhstan.
 - ✦ With the dismissal of Askar Mamin's government and the arrest of National Security Committee Chairman Karim Massimov (both of whom are close to the former President), the staff purge in the special services and the stripping of Nazarbayev's title as head of the Security Council has dismantled the framework of the 'two centre' system which has been a feature of the past two years.
 - ✦ However, Tokayev's position in the power system may weaken in the long term (since seeking external assistance could be interpreted as a sign of weakness of the President).

The problem of the lack of experienced leadership loyal to Tokayev is also becoming more acute.

✚ The increasing power of the President moving forward and the revision of relations along the lines of 'government-business', 'government-civil sector/society', and 'government-international structures and external centres of influence'.

✚ Given the continued instability of Tokayev's positions among the Kazakh elite, further steps can be expected to strengthen Presidential power. The main criteria for such steps would be limiting factors that provoke social discontent and destabilize the political system (dictated by regulatory trends) and the weakening of resources among competing elite groups (dictated by political and economic changes).

✚ Tokayev outlined the basics of this policy on 11 January in a keynote speech to Parliament. The following are the most significant for businesses (and for government engagement):

1. The reform and reorganization of government agencies (limiting the political influence of the President's opponents and part of Nazarbayev's entourage):

- ◇ The replacement of the Prime Minister with a neutral figure who is far removed from the groups of influence and is loyal to Tokayev. At the same time, the new Prime Minister previously handled relations with Russia and work on the EAEU—and that is symbolic in the current situation.
- ◇ Overhaul of the Government's composition and structure. However, in most Ministries, the Ministers either retained their posts or former deputies were appointed to their posts. There also was a rotation between the Government and the Presidential Administration (in particular, former Minister of Information & Social Development Aida Balayeva was appointed deputy Head of the Presidential Administration). In addition, Ministers linked to recent failures in economic and social policy were replaced (specifically in the Ministry of Energy due to the increase in liquefied gas prices, among other things).
- ◇ At the same time, there is likely to be a serious strengthening of the positions and influence of the Presidential Administration (the strategic centre of political and economic decisions), where structural changes aimed at expanding influence may also follow.
- ◇ One of the most difficult but critically necessary steps will be to reform the law enforcement system. The most radical changes can be expected in this regard (up to the elimination and merger of individual departments and serious staff purges in their leadership).

2. Changes in the Government's role in the economy (limiting the economic resources of some of Nazarbayev's entourage):

- ◇ The elimination, change in leadership, or reorganization of business entities associated with Nazarbayev's closest circle (a proposal to close expanded producer (importer) responsibility operator with the transfer of its functions to the public sector). This could generally become a factor for strengthening the government's direct involvement and stake in the economy (an attempt to move away from the clan model of distribution and asset management to a neutral bureaucratic model).
- ◇ The reform of development institutions that are de facto controlled by certain clans (reform of the Samruk-Kazyna National Welfare Fund and Development

Bank of Kazakhstan as well as measures to inspect customs work with China and orders to the National Bank to prevent the siphoning of funds abroad during a state of emergency, among others). This would not lead to the State's diminished stake and role in the economy; on the contrary, the goal would likely be to ensure that such entities are under the control of the bureaucratic machine (direct or indirect influence of state and Presidential structures) and the transfer of their control from clan structures to the Government.

3. Changes in regulatory approaches, which for businesses would have a dual effect due to the priority of the criterion for ensuring political stability:

- ◇ The partial (targeted and, in some cases, temporary) deregulation and liberalization in areas where it could reduce risks of social discontent: this would likely include the agricultural, consumer, and healthcare sectors (the President's proposals to deregulate prices on the pharmaceutical market, introduce a 180-day moratorium on price and tariff increases, and implement previously adopted unpopular regulatory measures).
- ◇ Conversely, the tightening of regulation in sectors where 'liberalization' is perceived as a source of risk of political destabilization: this would affect the technological sector (above all IT platforms and social media networks as well as systems used to receive and process personal data) and the financial sector (e.g., the President's proposals to introduce measures to combat religious extremism).

4. A more stringent approach to the activities of the 'third sector' (primarily with respect to foreign non-governmental organizations and charitable entities). This would above all require US and EU foreign businesses to reconsider their approaches to working with NGOs in Kazakhstan:

- ◇ Given the heightened Russian factor (see below), the dividing line in relation to NGOs will take place based on geographic and religious criteria. Harsher controls will be in place with respect to entities associated with the West (the Soros Foundation, USAID projects, and EU-supported organizations) and the Gulf/Turkey (Islamic religious organizations). At the same time, there could be a more loyal attitude towards the activities of and cooperation with NGOs from numerous post-Soviet countries (with Russian and Belarusian entities).
- ◇ Overall, this could trigger a revision of the attitude towards how the interests of foreign (Western) business are represented in the country and the strong positions of such entities could be interpreted as an instrument of foreign interference and pressure (there could be moves to weaken the role of embassies of the US, Anglo-Saxon countries – the UK and Canada – and EU members, advisory bodies with foreign participation, and business associations with a dominant membership of foreign companies, such as the American Chamber of Commerce and the Association of European Businesses, among others).

➤ The first use of CSTO armed forces in the organization's existence:

- Kazakhstan's request to the CSTO for assistance and the CSTO contingent's key role in stabilizing the situation and ensuring the security of key strategic facilities in Kazakhstan will enhance Russia's influence on internal political processes in the country.

➤ The prospect of bolstering Russia's position in Kazakhstan and Central Asia as a whole:

- The situation in Kazakhstan has enabled Moscow to significantly strengthen its influence in the Central Asian region.
- Moscow's growing influence in Kazakhstan could also run counter to the interests of Turkey, to which Nur-Sultan has been actively drawing closer in recent years.
- In addition, Russia's involvement in resolving the Kazakhstan crisis strengthens its position in the context of negotiations on security guarantees with the US and NATO as a guarantor of internal political stability in key post-Soviet countries.
- Russia's greater influence in Kazakhstan could give a powerful impetus to integration within the Eurasian Economic Union (EAEU):
 - The slow levels of integration were largely due to resistance by some of the Kazakh elite, which fears competition from Russian business groups and the lack of clear positive effects of membership in the EAEU for the Kazakh economy.
 - The implementation of key Russian initiatives in economic integration (labelling of goods, regulation of the IT sector and e-commerce, lifting of domestic trade barriers, and the convergence of financial systems) at the EAEU level could pick up significantly.
 - In terms of government relations, one significant aspect could be a probable decrease in Kazakhstan's autonomy in discussing the development of supranational regulation and specific draft acts within the bodies of the Eurasian Economic Commission (there had been cases when Kazakh representatives did not support Russia's position and offered alternative options for regulation).
 - In addition, the events in Kazakhstan may affect the decision of other countries, particularly Uzbekistan, to join the EAEU. Further, Moscow could use the Kazakh crisis as an additional argument for other countries with high risks of political destabilization due to the unresolved transition of power (for example Tajikistan) in favour of joining the EAEU as well as the CSTO (Uzbekistan).
- There also is a risk of a new escalation in Kazakhstan and Russia becoming bogged down in resolving the political and economic crisis in the country:
 - In the medium and long term, Russia's involvement in settling internal conflicts among the elites in Kazakhstan could lead to resistance and irritation among the local elites. Much depends on whether the CSTO contingent is quickly withdrawn and how Russia's role is bolstered.

RAMIFICATIONS OF THE CRISIS FOR BUSINESS

President Tokayev has estimated the damage from the unrest in Kazakhstan at USD 2-3 billion. The President said that the violent actions of extremists resulted in numerous casualties among law enforcement officers and civilians (various sources put the total number of fatalities at more than 160). In addition, according to Tokayev's estimates, some 1,300 businesses were damaged, while 100 shopping centres and banks were attacked.

The damage assessments made by Tokayev, however, differ from those of the Atameken National Chamber of Entrepreneurs, which, on 14 January, [announced](#) that damages amounted to USD 217 million (1763 businesses affected in ten regions).

Regardless, the events in Kazakhstan are directly impacting business. The risks can generally be divided into short-term and long-term.

The **short-term risks** are linked to the continued state of emergency and the speed at which the government's functional capacity and infrastructure are restored:

- ✦ At present, several countries have warned their citizens that it would be unadvisable to visit Kazakhstan. The US State Department has also announced that the embassy has a limited ability to provide consular services.
- ✦ The country's largest airport in Almaty is not accepting civilian flights (only military ones), which also complicates arrivals and departures in Kazakhstan (the airport is expected to resume operations on 13 January). Internet access remain unstable throughout the country (the authorities periodically block the Internet, attributing this move to anti-terrorist measures). Mobile communications work intermittently. There have been instances of calls to and from Kazakhstan being blocked.
- ✦ A curfew has been imposed in Almaty, the centre of business in the country (from 23:00 to 7:00). The situation in the city as well as in the West (Aktau, Atyrau, Uralsk, and Aktobe) and the South of Kazakhstan (Taldykorgan, Taraz, Shymkent, and Turkestan) remains turbulent.
- ✦ As of 11 January, business activity in the country is gradually recovering. Retail facilities, primarily those selling essential goods (food and medicine), have resumed operations.
- ✦ The financial system is operating on a limited basis. People can pay for goods and services, while legal entities have limited access to their accounts.
- ✦ Customs is operating as usual, but there are delays in cargo clearance due to Internet interruptions (documents are mostly prepared in paper form).
- ✦ The accounting and registration of retail transactions is allowed on paper until 19 January. Electronic invoices or receipts are not required. There are no administrative penalties for the failure to prepare documents or for the late payment of taxes (the tax payment period for previous periods began on 5 January).
- ✦ President Tokayev has introduced a moratorium on price and tariff increases for 180 days. This decision will slow the registration of several innovations within the EAEU related to the preparation of shipping documents, the regulation of tax regimes for small entrepreneurs, and the introduction of labelling during this period.

The **long-term risks** involve the strengthening of Russia's position in Kazakhstan. The assistance provided by the CSTO (Russia) in resolving the crisis in the country may have the following ramifications, which are not immediately obvious (*they are predictive in nature and may change depending on how the political crisis is resolved*).

Regulatory risks:

- ✦ Such risks are generally associated with the 'reception' of the Russian model of interaction with foreign business and the regulatory policy that fundamentally took shape after Crimea joined Russia in 2014:
 - ✦ The import substitution policy and 'aggressive' localization, including the intensive drafting of stimulating measures.
 - ✦ Regulatory 'nationalization' – the adoption of regulation that ensures the autonomy of national and supranational economies (EAEU) in areas that are critical in terms of security:
 - ◇ The technology sector and media – strengthening control and ensuring technical autonomy.
 - ◇ Banking and finance – strengthening the National Payment System, which will include a rapid payment system for individuals and organizations, and the

- ◊ integration of payment systems with EAEU member states to ensure cross-border transactions.
- ◊ Strengthening the Government's role in the pharmaceutical sector, healthcare, and the production and sale of socially significant food.
- Increasing oversight of transactions with foreign investors, especially in sectors that are critical to the state (the technology industry, finance, and critical infrastructure):
 - ◊ Strengthening the role of the antimonopoly authorities and tightening antimonopoly regulation in transactions involving foreign investors.
 - ◊ Increasing oversight and introducing additional restrictions/filters on the activities of foreign companies and entities in areas that are important to how public opinion is formed.
- Education as well as media, expert, research, and consulting entities:
 - ◊ The weakening of infrastructure used to collectively represent the interests of foreign (Western) business – from advisory bodies (the government's Foreign Investment Advisory Council, among others) and embassies to business associations that have increasing importance as 'insurance' against the political risks posed by partnerships with local business entities that are legitimate for the authorities.
 - ◊ Restrictions on the activities of international NGOs with the possible adaptation of certain Russian legislation in this regard (legislation on 'foreign agents').

Political risks:

- Forced integration within the EAEU: the creation of common markets (energy, financial, and service markets) and the implementation of Russian integration initiatives. The possible transformation of the Eurasian Economic Union into the Eurasian Union, which would entail political integration and the creation of common authorities (following the example of the European Union).
- Possibly securing the status of the Russian language as a second state language.

Economic risks:

- Kazakhstan is one of Russia's key trade and economic partners in a number of sectors, primarily in the energy sector. Russia imports thermal coal from Kazakhstan to meet the needs of its regions (Siberia). Russia and Kazakhstan are co-owners of the Caspian Pipeline Consortium project, which is used to deliver Kazakh oil to the port of Novorossiysk.
- Russia's growing influence in the medium term may entail a revision of the terms of Kazakhstan's cooperation with companies from the US and UK, which are partners of the Kazakh Government in several major oil and gas projects in mainland Kazakhstan and the Kazakh shelf of the Caspian Sea.
- In addition, Kazakhstan is one of the top suppliers of uranium to the world market (the country produces over 40% of the global supply). External control over the state-owned company Kazatomprom could lead to major changes in the global nuclear energy sector, for example rising uranium prices or the creation of competitive advantages for Rosatom as opposed to Western companies in the nuclear energy market.

FORECAST AND RECOMMENDATIONS

On 11 January, President Tokayev appointed a new Prime Minister, and Parliament agreed on the new composition of the Government. The reformatting of the Government will lead to staff reshuffles throughout the entire vertical power structure, which will require businesses to build communications with new individuals at all levels of government.

At the same time, for now it would be impossible to say that the crisis has passed or that there is complete political stabilization in the country.

With this in mind, recommendations for government engagement can be divided into current and long-term.

Current (short-term) recommendations:

- Refrain from communications, especially public, with Nazarbayev's inner circle.
- Consider options for quietly pulling out of partnerships and cooperation (if any) with entities that are associated with or controlled by the structures of Nazarbayev's inner circle.
- Avoid any social or informational activities that could be interpreted as attempts to influence the public or political sphere, and it would also be advisable to consider the possibility of supporting initiatives that are important to stakeholders in the current crisis (such as the provision of free communication services by operators)
- Freeze any ongoing social or other kinds of non-profit projects that may raise suspicions of disloyalty among the authorities.
- Maintain only limited and targeted interaction with the "new" stakeholders after the formation of the Government in the next six months due to the continued risk of further destabilization. Build communication with the authorities under the assumption that there could be further staff reshuffling in the Government and at the level of the Presidential Administration.
- It will be crucial in the coming months to continue to follow the regulatory, political and social changes in Kazakhstan, while monitoring the ramifications for Central Asia, the EAEU and the post-Soviet space as a whole (how the CSTO forces complete their operation in Kazakhstan and the reaction from the US, EU, Turkey, and China, among other things).

Long-term recommendations:

- Gradually transform the corporate GR model from one more typical for jurisdictions strongly influenced by Western structures (such as embassies) to a model appropriate for 'protectionist' jurisdictions with extremely limited influence from Western representative structures (Russia).
- Integrate into new advisory structures that may be formed following the staff reshuffling in government agencies.
- Revise or refuse cooperation locally with international NGOs (after the situation stabilizes and depending on how the control system is established).
- Consider the possibility of cooperation and partnerships with strong local entities (also after the political situation stabilizes and an assessment of the balance of power).
- Also consider the possibility of partnerships with local business entities (localization projects). If there are similar stable partnerships in Russia, consider the value of this channel for continuing activities in Kazakhstan.

- Search for niches where joint (including non-commercial) projects with foreign business, such as the healthcare sector or small business, would be important to the authorities.

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