

POLICY BRIEFING

# Kazakhstan:

## Selected trade and economic issues

### Abstract

In a number of ways, Kazakhstan has performed best among the former Soviet republics in Central Asia. Benefitting from rich natural resources, the country recovered from the collapse of the Soviet plan economy and posted very good results for most of the last decade. With a relatively open and market-oriented economy, Kazakhstan has increasingly integrated into the world trading system, although with some serious distortions, particularly in key economic sectors such as mining and oil.

Kazakhstan is currently an upper-medium income country, and one viewed – thanks to its hydrocarbon reserves – as a strategic economic (and often political) partner by most of its neighbours, the EU and the US. Trade with Europe is on the rise, and the EU is the country's first trading partner.

Increased revenues have helped improve infrastructure and social services, and the country has experienced significant progress in terms of human development and the fight against poverty. Social and regional disparities have not been entirely erased, however, and the country still faces serious economic, environmental and social challenges.

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## 1. Introduction: A commodity-driven transition

The dissolution of Soviet Union severely impacted Kazakhstan.

The dissolution of the USSR had a severe negative economic and social impact on Kazakhstan. Demand and supply networks based on free transport quickly collapsed in the early 1990s. While the shift to market prices for natural resources was theoretically beneficial to Kazakhstan and other energy exporters, the country was unable to benefit immediately from changed economic circumstances as a result of its heavy dependence on Russian pipelines. In fact, Russia exploited its monopoly by regulating flows and levying high tariffs on Kazakh exports. Routes for Kazakh oil and gas did not substantially change in the first decade following independence, with only small quantities of oil shipped across the Caspian Sea; most continued to be exported through Russia<sup>1</sup>.

Like other Central Asian republics, Kazakhstan suffered from disrupted supply chains and higher prices for imports. An imminent economic collapse was suggested in 1991 by falling output and rising prices, but the situation became dramatic after the dissolution of the USSR wiped out the remaining centralised bodies that had governed the Soviet economic space.

More than 1.5 million highly skilled people left the country after independence.

After independence, Kazakhstan experienced a serious brain drain that also impacted its economic performance. Highly qualified minorities, including Germans and many educated Russians, chose to leave the country<sup>2</sup>. By the end of the 1990s, almost 1.5 million people had left Kazakhstan – more than 10 % of its population during Soviet times.

Economic performance in the first years of independence was hampered by 'bottlenecks' limiting oil exports.

Macroeconomic performance in the first decade after independence was disappointing. After rapidly transforming to a market economy, Kazakhstan experienced deep recessions in the first half of the 1990s. The country then recovered slightly in 1995-97, before being hit again by the 1998 Russian crisis. Since 2000, Kazakhstan's economy has grown rapidly, led by exports and stimulated by currency depreciation. Oil and other commodities revenues have boomed.

The process of reform in Kazakhstan was initially rather promising but slowed in the mid-1990s. Large-scale privatisations generally benefitted insiders and other well-connected people, who gained the lion's share of the most valuable assets and – as in Russia – distorted the privatisation process.

The early 2000s were extremely positive for Kazakhstan; the economy

In sharp contrast, the first decade of the 21st century has brought rapid GDP growth, driven by oil and commodity exports. Kazakhstan's government has promoted an ambitious plan to use budgetary surplus to

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<sup>1</sup> Richard Pomfret (OECD working paper No. 212), Central Asia since 1991: the experience of the new independent states (July 2003).

<sup>2</sup> François-Olivier Seys: [Les dynamiques démographiques au Kazakhstan, un modèle spécifique depuis l'indépendance](#) (2009).

grew at sustained rates.

promote economic diversification and avoid excessive dependence on oil exports. Kazakhstan has heavily invested in its integration in the global economy, including through the adoption of international standards in key productive, financial and administrative sectors.

GDP per capita has significantly increased in the past decade, and Kazakhstan achieved a significant reduction in poverty and remarkable improvements in social development indicators between 2000 and 2010<sup>3</sup>. Among those indices registering improvements, the gender inequality index (GII) was a notable forerunner, gaining more than 30 % over the course of the decade. Kazakhstan has already attained the first three out of eight Millennium Development Goals and has made good progress on the remaining goals. In 2010, the UN Development Programme (UNDP) ranked Kazakhstan 69<sup>th</sup> of 187 countries in its Human Development Index (HDI)<sup>4</sup>.

Yet the country remains in a transitional phase, and serious issues – including widespread corruption, murky government practises and social and regional disparities – have still to be rectified. The Kazakh government launched new employment programmes and increased social spending in 2012 following labour-related violence in the south-eastern town of Zhanaozen.

## 2. Economic indicators

Despite efforts to diversify, the Kazakh economy is still largely driven by oil and minerals.

The country is highly dependent on mining industries and in particular on the oil sector, which accounts for 60 % of total exports and more than 25 % of GDP. Kazakhstan has huge fossil fuel reserves and large stocks of other minerals and metals, such as uranium, copper and zinc. Oil production is expected to double in less than ten years, as soon as the Kashagan oil field becomes fully operational.

Industry, however, suffers from low productivity and competitiveness, as well as from the appreciation of the national currency, the 'Tenge'<sup>5</sup>. The country remains vulnerable to commodity price fluctuations. The government has invested significant efforts and created a fund to modernise the country's industrial base.

Services are gaining a stronger role in Kazakhstan, but the sector is still fragile and underdeveloped.

The service sector, once rather neglected, is also developing steadily thanks to high local demand. In 2002 Kazakhstan became the first country in the former Soviet Union to receive an investment-grade credit rating. The banking sector, after a brilliant phase in the early 2000s, experienced major problems during the global economic downturn of 2008-2009 and continues to constitute one of Kazakhstan's major weaknesses<sup>6</sup>.

<sup>3</sup> Islamic Development Bank, Country Programs Department, Country Economic Work: '[Enhancing Competitiveness and Diversification of the Kazakhstan Economy](#)' (2011)

<sup>4</sup> UNDP, 2013 Human Development Report: [Kazakhstan](#).

<sup>5</sup> 1 Euro = 203 KZT as of 28 August 2013.

<sup>6</sup> Rabobank, Country note on Kazakhstan (May 2011)

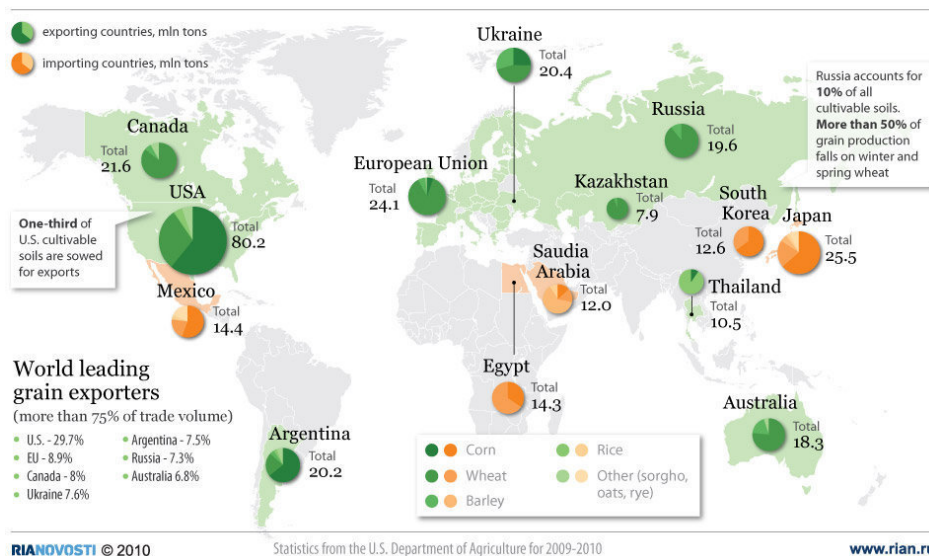
The country's 'Virgin Lands' programme in the late 1950s and 1960 led Kazakhstan – traditionally a pastoral economy with a cotton sector concentrated in the south – to become a major grain producer. After independence, the agricultural sector experienced a severe decline. This has been reversed in the past decade, when crop production (with the exception of cotton) substantially increased. Like cotton, the growth of livestock has been more modest<sup>7</sup>.

Agriculture is still an important source of employment and revenues but requires further modernisation.

For all other Central Asian countries, imports of Kazakh wheat are crucial.

Today the agricultural sector's contribution to GDP is relatively small – less than 5 % of GDP. In terms of employment, however, the sector is important, occupying nearly 30 % of the labour force. The country's production is concentrated on grains and livestock; Kazakhstan is among the major exporters of wheat in the world, and its wheat is of a high quality. For all other Central Asian countries, imports of Kazakh wheat are crucially important<sup>8</sup>. Due to the persistent drought affecting the country's 'northern grain belt', the 2012 crop yielded significantly less than in previous years. However, carryover stocks (mostly from 2009, a record year) and high cereal prices enabled Kazakhstan to reduce its drought-related losses and maintain its position among the ten leading world grain exporters in 2012<sup>9</sup>. The 2013 output is likely to be slightly higher than that of 2012, but still far below the 2011 crop.

**Figure 1:**  
Map of world grain exporters and importers



Industry, including mining, contributes a relatively large 39 % to GDP. The service sector accounts for the remaining 57 %.

<sup>7</sup> Richard Pomfret, [Using Energy Resources to Diversify the Economy: Agricultural Price Distortions in Kazakhstan](#) (2008)

<sup>8</sup> Oxford Analytica: Central Asia's Food Security Hinges on Kazakh Wheat, (26 April 2011).

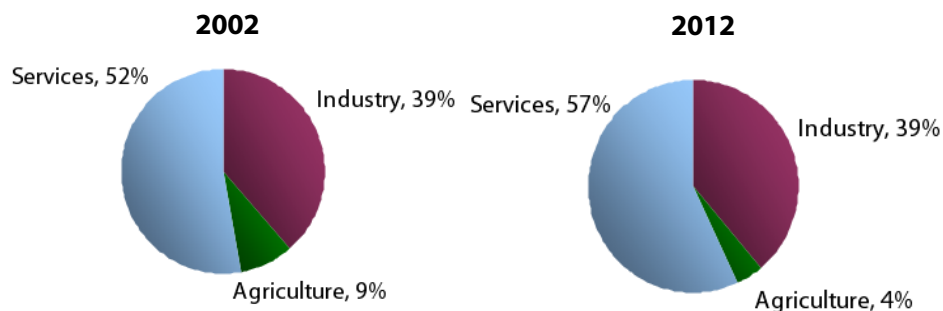
<sup>9</sup> International Maize and Wheat Improvement Center, Water-saving techniques salvage wheat in drought-stricken Kazakhstan (March 2013).

**Table 1:**  
Change in economic sectors, 1992-2012

	1992	2002	2012
Industry	44 %	39 %	39 %
Agriculture	27 %	9 %	4 %
Services	29 %	52 %	57 %

Source: World Bank

**Figure 2:**  
Kazakhstan's economic sectors

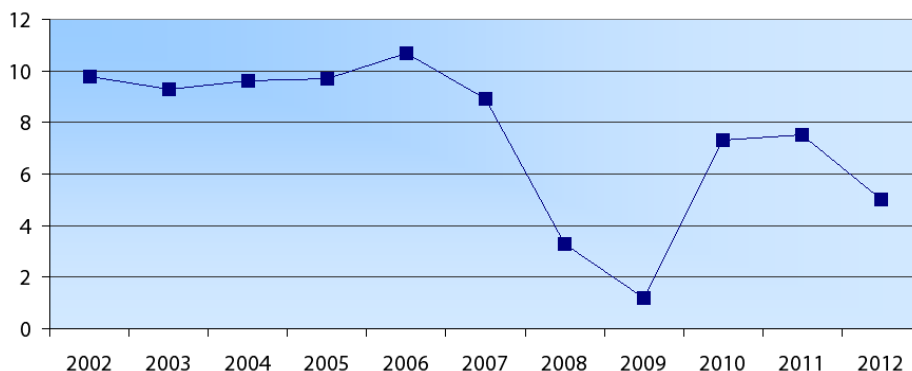


Source: World Bank

Economic growth today is good, if less sustained than in the early 2000s.

Kazakhstan rapidly recovered from the economic recession that affected the country in 2009. Due to a fall in oil and commodity prices, the entire country faced a serious, albeit short, economic slowdown. The rise in commodity prices that followed the (partial) recovery in 2010 and 2011 returned the country's growth to stronger levels – 5 % in 2012 – although they remained lower than before the-crisis.

**Figure 3:**  
Kazakhstan GDP annual growth rate



Source: World Bank

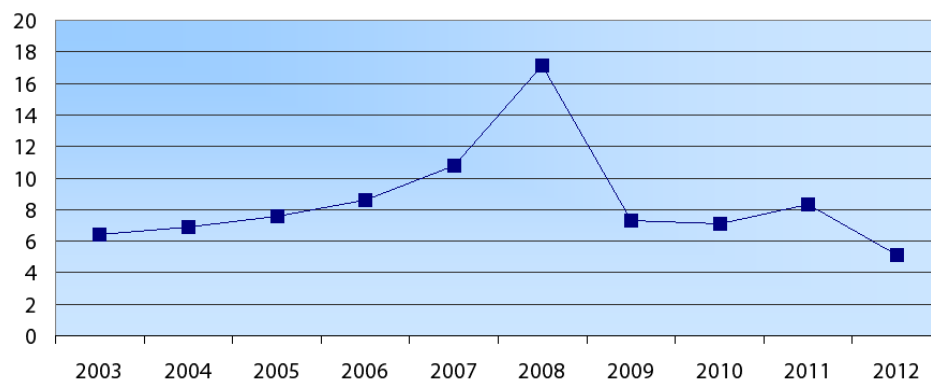
Astana is making a serious effort to diversify the national economy by moving away from a concentration on the energy and mining sectors and towards the growth of a domestic high technology industry. However, the results have been only moderately positive so far. The relative strength of the local currency, coupled with an underperforming industrial sector, has

slowed down the country's industrial development. Some analysts have even evoked 'Dutch disease'<sup>10</sup> to describe the potential danger facing the Kazakh economy if no adjustment is adopted<sup>11</sup>.

Inflation and public debt indicators are very good.

Inflation for 2012 grew by 5.5 % – a slightly better result than in the two previous years, when it reached 7.1% and 8.3% – and is due to remain at similar levels in 2013.

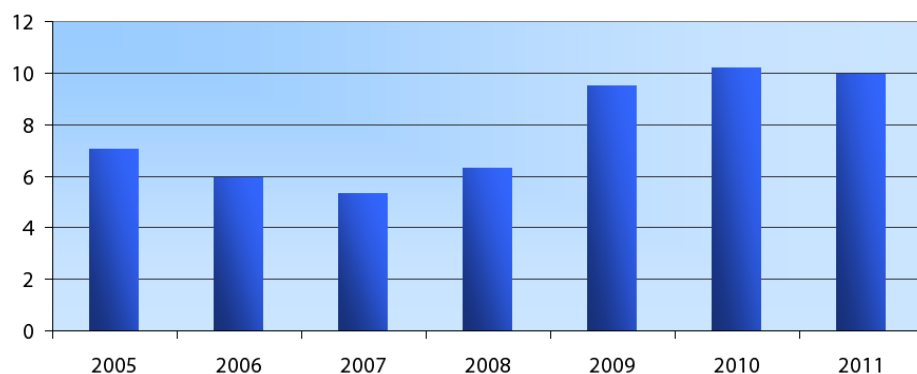
**Figure 4:**  
Inflation



Source: World Bank

Public debt has risen slightly, essentially in response to the government's expansionary policies. Yet even at 10 %, the level of debt remains one of the lowest in the world.

**Figure 5:**  
Public debt



Source: World Bank

The World Bank's 'Doing Business Index' is rather positive about Kazakhstan, particularly relative to the other countries in the Commonwealth of Independent States (CIS). Thanks to the country's relative stability and the government's efforts to cut red tape, the country was ranked 49<sup>th</sup> of 185 countries in 2013 – a position that marked an improvement of 10 places from 2011<sup>12</sup>.

<sup>10</sup> The term 'Dutch disease' originates from a crisis in the Netherlands in the 1960s that resulted from discoveries of vast natural gas deposits in the North Sea. The newfound wealth caused the Dutch guilder to rise, making exports of all non-oil products less competitive on the world market.

<sup>11</sup> University of Michigan, [Dutch Disease Scare in Kazakhstan: Is It Real?](#) (2007)

<sup>12</sup> World Bank, ['Doing business report'](#) (Kazakhstan, 2013)

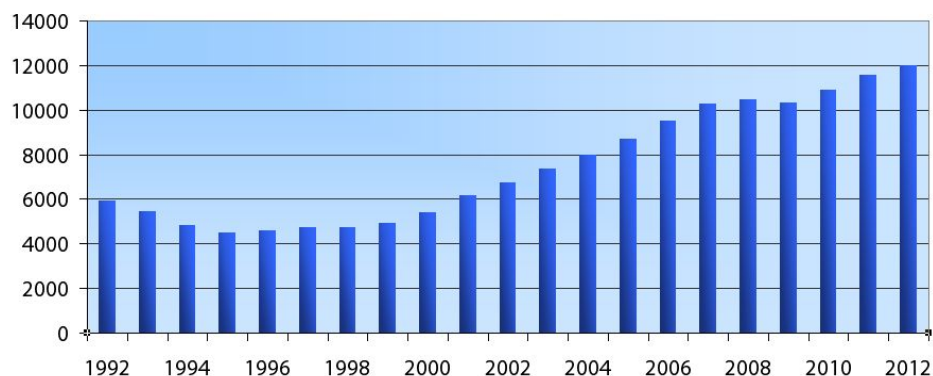


### 3. Social and environmental issues

Social and environmental issues are high on the government's agenda.

Thanks to its oil resources, Kazakhstan is the richest of the former Soviet Central Asian republics. The World Bank classifies Kazakhstan as an 'upper-middle-income country', with a per capita GDP just below USD 12 000 (EUR 9 000) in 2012<sup>13</sup>.

**Figure 6:**  
GDP per capita, PPP  
(constant international  
2005 USD)



Source: World Bank

In the past decade, there has been a significant decrease in poverty rates, which fell from 46.7 % in 2001 to 5.3 % in 2011. The gap between urban and rural living standards, however, is still high: the poverty rate is less than 5 % in towns, while about 10 % in rural areas. Overall, about 30 % of the population receives some sort of social assistance.

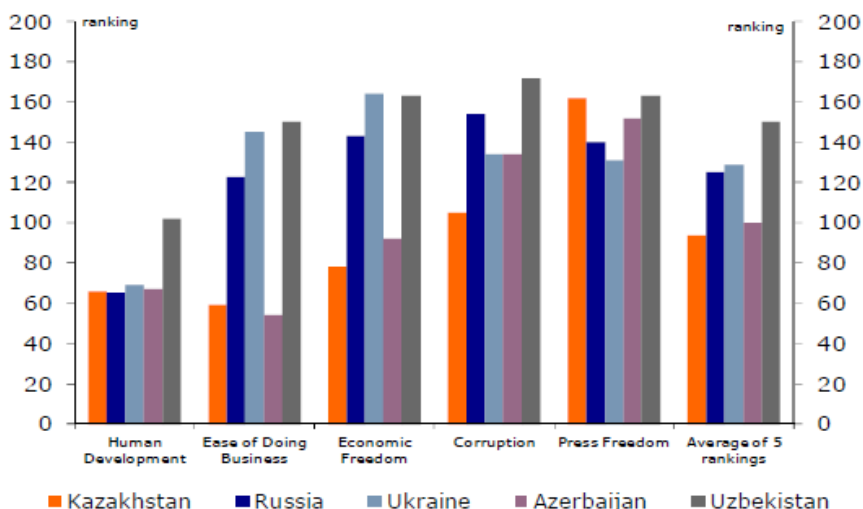
Kazakhstan's economy is largely a functioning market economy, but interference by the state is not completely excluded. As a result of the 2008 crisis, the state presence in the economy increased by 5 %, from 30 % to 35 %<sup>14</sup>. Of particular note is the state-owned holding Samruk-Kazyna, which controls a number of industrial and financial undertakings in the country and whose role is central in national development plans.

As shown by the chart below, Kazakhstan is performing well in terms of social indicators in comparison to Russia and other former Soviet republics. The notable exception to this success is the country's 'freedom of press'.

<sup>13</sup> The World Bank, Kazakhstan overview (August 2012).

<sup>14</sup> Oxford Analytica, Samruk-Kazyna remains key to Kazakhstan development (8 April 2012)

**Figure 7:**  
Social Indicators (2010)



Source: Rabobank (higher ranking implies worse performance)

### 3.1. Education

Kazakhstan is generously investing in education, with positive results.

In its pre-independence years, Kazakhstan played an important role in the Soviet scientific research community. Higher education suffered in the years after the declaration of independence, but since 2000 the government has given this sector increasing attention. Efforts to expand pre-school access and offer make secondary education free and compulsory have been successful. Kazakhstan now has high levels of literacy (97 %) and has achieved near universal primary education. Currently there are 177 universities in Kazakhstan – 68 public and 109 private, with five branches of Russian universities. In 2005 approximately 750 000 students (in a population of over 15 million) enrolled in higher education.

In 2009 Kazakhstan ranked first in UNESCO's 'Education for All Development Index', with particularly positive results for its near-universal levels of primary education, high adult literacy and full gender parity<sup>15</sup>.

For the coming years, Kazakhstan is due to undertake further major reforms across all education levels and to strongly invest in universities. The Kazakh government would like to transform the University of Astana into a state-of-the-art institution able to compete on equal footing with the most prestigious world universities<sup>16</sup>.

### 3.2. Healthcare system

Kazakhstan faces challenges in restructuring its healthcare system<sup>17</sup>. The country's health outcomes lag behind its rapidly increasing income, and the national healthcare system is in need of major improvements. The main causes of adult mortality are non-communicable diseases, such as cancer, cardiovascular disease, other tobacco and alcohol-related diseases and

<sup>15</sup> UNESCO, Report on ['The Education For All Development Index'](#) (2009)

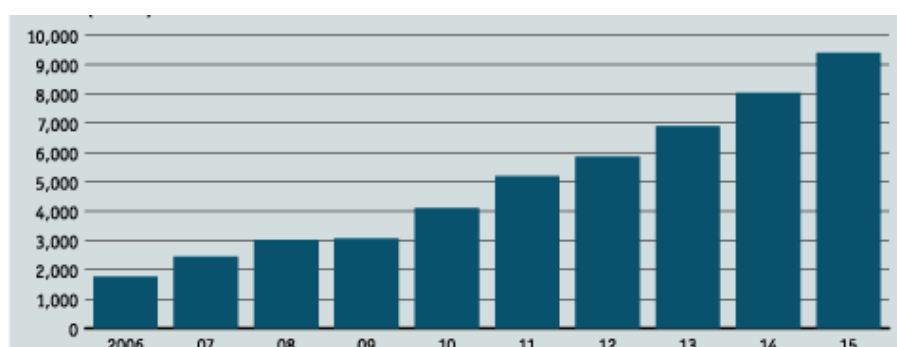
<sup>16</sup> The World Bank, [Kazakhstan-World Bank Joint Economic Research Program](#) (2012)

<sup>17</sup> WHO (World Health Organisation) [Health Systems Review: Kazakhstan](#) (2012)

injuries.

Despite significant financial efforts (see table below), the population's health has not improve substantially in recent years. Private, out-of-pocket expenditure is still very high (36 % of total health expenditure in 2007) and exposes poorer layers of the population to potentially unbearable costs. According to the Kazakh National Statistical Agency, more than 7 % of the population did not use health services in 2008 because of the high costs.

**Figure 8:**  
Healthcare spending  
(USD million)



Sources: *Epicom, Economist Intelligence Unit*

Kazakhstan is reforming its healthcare system, which still lags behind Western standards.

The new State Health Care Development Programme recognises health as one of the country's major priorities and a pre-requisite for sustainable socio-economic development. Low life expectancy, high infant and maternal mortality, high rates of tuberculosis and non-communicable diseases are among the major challenges the Kazakh government will have to face in the coming years. The government is also working to reduce regional inequalities and increase the number of qualified healthcare operators in the countryside.

### 3.3. Environment

The environment is a matter of serious concern.

Kazakhstan has inherited significant environmental problems from its past military nuclear testing programmes and industrial and mining activities. The country also faces land deterioration, desertification and water scarcity.

Between 1949 and 1991, the Soviet government conducted about 70 % of all of its nuclear testing in Kazakhstan, mostly in the north-east, near the city of Semipalatinsk (now known as Semey). Nearly 500 nuclear explosions occurred above and below ground there, and more than 40 nuclear detonations occurred at other testing grounds in western Kazakhstan and in the Qyzylqum desert. More than one million of Kazakhstan's inhabitants have been exposed to dangerous levels of radiation because the Soviet government decided not to evacuate or even warn populations living close to the nuclear test sites. In the late 1980s, large demonstrations were held in Kazakhstan calling for an end to the nuclear testing, and in 1991 the Kazakh government put a stop to the practice. However, the testing grounds, and

<sup>18</sup> Naturvernforbundet, [Environmental issues in Kazakhstan](#) (2012)

most probably the underground aquifers, remain highly contaminated<sup>18</sup>.

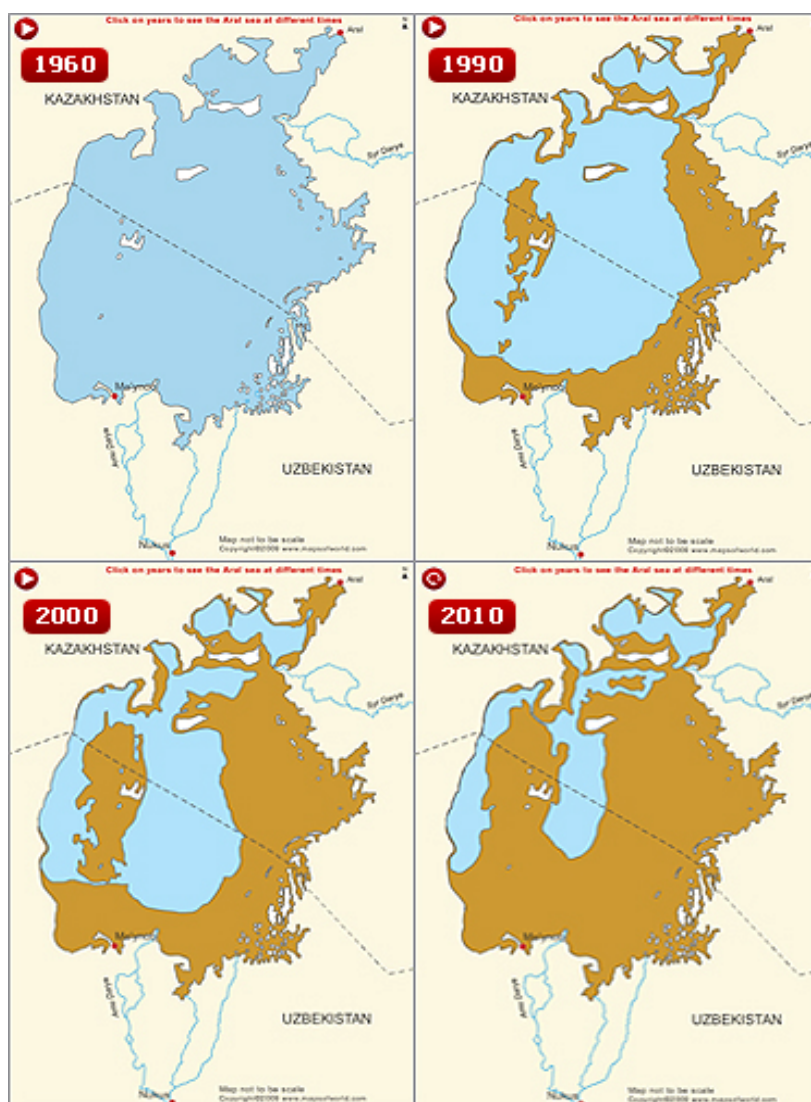
**Figure 9:**  
Map of radioactive, chemical and biological hazards in Central Asia



Kazakhstan is actively trying to stem the progressive disappearance of the Aral sea.

Another major ecological issue in Kazakhstan concerns the Aral Sea, the retreating water basin that Kazakhstan shares with Uzbekistan. In the early 1960s, the Soviet government promoted intensive cotton culture in Central Asia, with a view to developing self-sufficiency and possibly creating a surplus to export to friendly countries. Excessive irrigation and high evaporation rates substantially decreased the flow of water to the Aral sea, which resulted in a rapid diminution of the basin's surface (see map below). The original coastline of the sea receded by several dozens of kilometres, exposing large surfaces that had once been covered by waters and contaminating them with salt and other hazardous substances. This completely destroyed the wildlife habitat and caused severe health problems, including respiratory infections and parasitic diseases, for people living nearby. Local economies, which had largely depended on agriculture and fisheries, collapsed, and some inhabitants were forced to migrate elsewhere. Efforts to address the crisis, focused on preventing further shrinkage of the Aral Sea, have so far produced mixed results.

**Figure 10:**  
Maps showing the  
disappearance of the Aral  
Sea



Kazakhstan also faces the problem of urban pollution, particularly in its major cities, which are exposed to harmful emissions from lead and zinc smelters, a uranium-processing mill and other heavy industries. In recent years, environmental activist groups in Kazakhstan have begun lobbying for tighter emission controls.

Other environmental issues in Kazakhstan include soil pollution resulting from the overuse of pesticides in agriculture, and the increasingly polluted waters of the Caspian Sea.

National environmental monitoring systems are inadequate and require greater funding to become fully operational. The government has made progress in environmental management, but the environmental situation of the country requires further action.

#### 4. Foreign trade and investment

Foreign direct investments in oil and mining are pouring into Kazakhstan.

The strong increase in the price of hydrocarbons and minerals has boosted Kazakhstan's foreign trade sector. Exports have grown manyfold, with the trade surplus reaching the unprecedented level of USD 14 billion in 2011

and only slightly declining in 2012.

**Figure 11:**  
 Merchandise  
 export/import  
 (in EUR million)



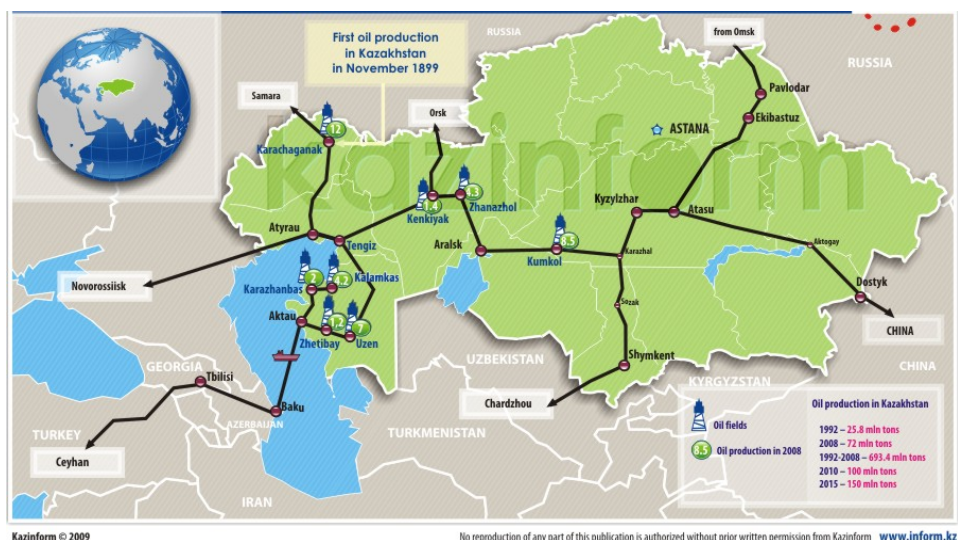
Source: World Bank

The country requires infrastructure to bring its oil and gas to markets abroad.

The EU, Russia and China are Kazakhstan's three largest trading partners. Beijing is particularly interested in deepening its economic and trade relations with the country. The Kazakh economy is, in fact largely, complementary to the Chinese, and an expected increase in the production of oil and gas is likely to be exported to satisfy the growing Chinese consumption.

The geographical proximity of China and Kazakhstan also plays an important role in the two countries' relations. Kazakh infrastructure is still being developed, and further investments are needed to best exploit the country's natural resources<sup>19</sup>. The first pipeline serving China was opened in 2006. Its current – 10 million tonnes per year – is likely to be expanded for the opening of the Kashagan oil fields, located on the north shore of the Caspian Sea. A second pipeline (the 'Central Asia pipeline') was inaugurated in 2009 to bring oil from Turkmenistan and Uzbekistan (and to a lesser extent Kazakhstan) to the Chinese province of Xinjiang. Supply to western countries is usually done via Russia or Turkey (see map below).

**Figure 12:**  
 Map of Kazakhstan's oil  
 fields and supply routes



Kazakhstan would, however, prefer that Beijing not fully control local oil and gas facilities. Astana has tried to redirect Chinese capital into economic

<sup>19</sup> Oxford Analytica, Kazakhstan-China commercial ties are likely to deepen (7 May 2012)

sectors other than mining and oil as it copes with popular fears that the Chinese constitute a major threat for the domestic economy. Turkey, the United States, Canada and Ukraine are also among Kazakhstan's top trading partners. (For trade relations with Russia, please refer to the chapter on the customs area below.)

**Table 2:**  
Kazakhstan's top five trading partners, 2012

Origin of imports				Destination of exports				Trade partners				
#	Origin	€ million	%	#	Destination	€ million	%	#	Partner	€ million	balance	%
1	Russia	11,182	31.4	1	EU27	20,123	39.9	1	EU27	27,193	+13,052	31.6
2	China	9,438	26.5	2	China	10,342	20.5	2	China	19,780	+904	23.0
3	EU27	7,071	19.9	3	Russia	4,883	9.7	3	Russia	16,065	-6,299	18.7
4	Ukraine	1,568	4.4	4	Canada	2,397	4.8	4	Ukraine	3,887	+750	4.5
5	Turkey	917	2.6	5	Ukraine	2,318	4.6	5	Canada	2,484	+2,310	2.9
<b>All imports:</b>		<b>35,604</b>		<b>All exports:</b>		<b>50,428</b>		<b>Balance of trade:</b>		<b>+14,824</b>		

Source: DG Trade

[Kazakhstan's negotiations to join the World Trade Organisation are underway and may be concluded shortly.](#)

Kazakhstan is not a Member of the World Trade Organisation (WTO). Negotiations for accession started in 1996 and have progressed slowly, having been delayed by, *inter alia*, Astana's decision to enter the Belarus-Russia-Kazakhstan Customs Union in 2009.

More recently, Kazakhstan has intensified its efforts to complete bilateral market access negotiations, signing a number of bilateral goods and services agreements in 2010 and 2011. While the country has yet to conclude WTO bilateral market access agreements with a limited number of WTO members, Kazakhstan signalled its intention to complete work on an accession package in 2013. This goal is probably over-ambitious, since some key multilateral issues have still to be cleared by the accession working party. Major issues that remain the subject of negotiations include:

- (a) Kazakhstan's localisation policies in procurement by state-owned and state-controlled enterprises;
- (b) trade-related investment measures that Kazakhstan enforces in the oil, gas and mining industries; and

Kazakhstan's agricultural policies, including domestic support, export subsidies, value-added taxes on imports, and tariff-rate quotas (TRQs).

#### 4.1. Trade and economic relations with the EU

The EU is the country's first EU-Kazakhstan bilateral trade and economic relations have developed significantly since 2000. The EU has progressively become Kazakhstan's first

trading partner.

trade partner, accounting for a roughly 32 % share in Kazakh external trade. Kazakhstan's exports to the EU were principally oil and gas, which accounted generally for more than 80 % of the country's total exports in 2010. Kazakh imports are largely machinery, chemical products and manufactured goods<sup>20</sup>.

**Table 3:**

Kazakhstan's trade in goods with the EU

	Exports to EU:	Imports from EU:
Value 2012:	EUR 20,123 million	EUR 7,071 million
EU's rank (for Kazakhstan), 2012:	1	3
Kazakhstan 's rank (for EU), 2012:	37	16
% total, 2012:	39.9 %	19.9 %
% EU total, 2012:	0.4 %	1.4 %

In 2012 Kazakhstan was the 26<sup>th</sup> trading partner of the EU and the third in the CIS area, after Russia and Ukraine.

**Table 4:**

EU-27 trade with the CIS countries (EUR million)

	2000		2005		2009		2010		AAGR* 2000-2010		Change 2009-2010 (%)	
	Imports	Exports	Imports	Exports	Imports	Exports	Imports	Exports	Imports	Exports	Imports	Exports
Armenia	131	271	514	419	161	534	257	557	7.0	7.5	60	4
Azerbaijan	994	362	2 506	1 495	7 333	1 612	9 763	2 347	25.7	20.6	33	46
Belarus	1 330	1 694	3 422	3 234	2 590	4 962	2 627	6 716	7.0	14.6	2	35
Kazakhstan	3 821	1 427	10 276	3 576	10 752	5 313	15 841	5 231	15.3	13.9	47	-2
Kyrgyz Rep.	140	71	17	110	29	186	199	210	3.5	11.5	575	13
Moldova	270	610	435	1 080	516	1 227	582	1 529	8.0	9.6	13	25
Russia	63 777	22 738	112 591	56 696	117 254	65 614	158 394	86 505	9.5	14.3	35	32
Tajikistan	100	42	106	88	75	101	57	144	-5.5	13.2	-24	43
Turkmenistan	258	201	903	331	591	825	366	719	3.6	13.6	-38	-13
Ukraine	4 807	5 454	8 655	13 281	7 896	13 922	11 396	17 334	9.0	12.3	44	25
Uzbekistan	653	584	529	590	318	972	415	1 243	-4.4	7.9	31	28
<b>Total CIS</b>	<b>76 280</b>	<b>33 453</b>	<b>139 957</b>	<b>80 901</b>	<b>147 505</b>	<b>95 289</b>	<b>199 897</b>	<b>122 534</b>	<b>10.1</b>	<b>13.9</b>	<b>36</b>	<b>29</b>

\* AAGR: Average Annual Growth Rate

Source: Eurostat

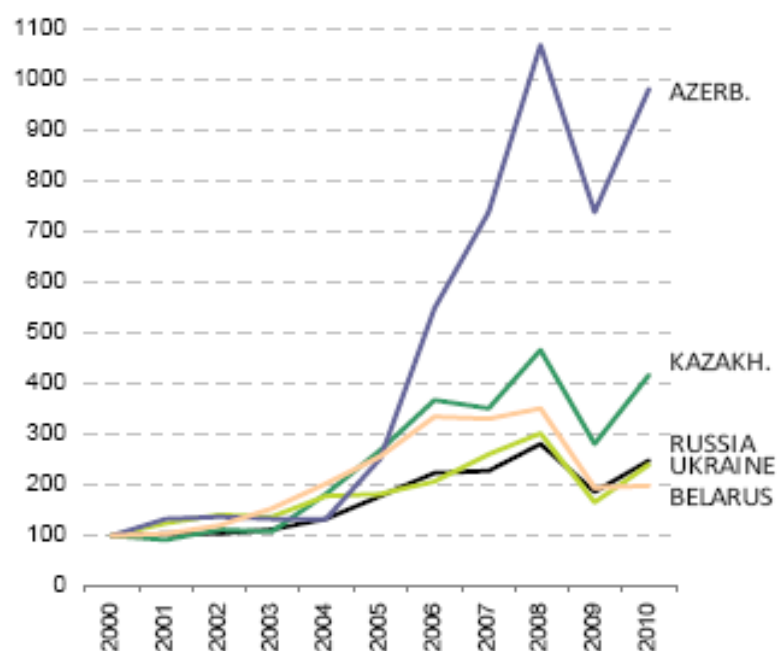
Bilateral trade increased four times in the 2000-2010 decade, with Kazakhstan consistently ranking second after Azerbaijan among the EU's Central Asian partners since 2005 (see table below)<sup>21</sup>.

<sup>20</sup> DG trade, [Statistics on Kazakhstan](#) (2012)

<sup>21</sup> Eurostat, [CIS-EU - Trade in goods](#) (2012)



**Figure 13:**  
Bilateral EU-Kazakhstan  
trade



Source: Eurostat

The EU is also Kazakhstan's largest investment partner, with more than 60 % of foreign direct investment in Kazakhstan coming from European companies. European investments concentrate in the oil and mining industry. Trade in services is relatively small but steadily increasing in response to a growing demand for high quality services in Kazakhstan<sup>22</sup>.

Trade and economic relations between the EU and Kazakhstan are governed by the Partnership and Cooperation Agreement (PCA) signed in 1999. Trade in specific sectors is still managed under bilateral agreements or autonomous measures. Since the expiry of the EU-Kazakhstan steel agreement in 2006, the bilateral trade in steel has been based on autonomous measures. Following the expiry of the EU-Kazakhstan textiles agreement in 2004, the two parties signed an additional protocol in 2006 to extend the old agreement's provisions on trade in textiles; however, this protocol never entered into force.

Negotiations for an enhanced Partnership and Cooperation Agreement (PCA) between the country and the EU started in 2011.

Negotiations for an enhanced trade and investment agreement started in 2011. The new PCA is intended to improve political and economic relations with the Central Asia country, and to reinforce political dialogue, enhance cooperation in home and justice affairs and promote mutual trade and investments. Three rounds of negotiation have taken place so far. The last meeting was held in Astana on 10 July 2012, and the next round is due to

<sup>22</sup> The EU business is represented in Astana by a [EU-Kazakhstan Chamber of Commerce](#).

<sup>23</sup> EEAS, [The EU and Kazakhstan continue negotiations on a new enhanced PCA in Astana](#) (10 July 2012). See also DG Trade: [Overview of FTA and other trade negotiations](#) (Updated 1 August 2013)

take place in Brussels in October 2013<sup>23</sup>.

In June 2013, the EU announced that it had reached agreement with Kazakhstan on bilateral conditions for the Central Asian country's admission to the WTO<sup>24</sup>.

## 4.2. Barriers to trade and investment

Barriers to trade and investment are significant in the country.

Because Kazakhstan is not a member of the WTO, the country is not bound by WTO rules. Astana therefore exercises a certain discretion in its application of customs and trade measures, with a potentially protectionist effect. The European Commission, in its 2012 'Trade and Investment Barriers Report', focused on the negative impact of the newly created customs area with Russia and Belarus (*see below*)<sup>25</sup>. A more detailed analysis on potential trade barriers – largely applicable to EU businesses – has been prepared by the United States Trade Representative (USTR)<sup>26</sup>. Astana's restrictions on investments, notably in the banking system and the mining industry, are rather strong. The government's strategy, which aims to increase the use of local content in public procurement, adversely impacts foreign suppliers and is a subject of intense discussions in Kazakhstan's WTO accession process.

## 4.3. Economic integration with Russia and its impact on the EU

Further economic integration with Russia may damage relations with EU.

The Customs Union between Russia, Kazakhstan and Belarus was formally set up in January 2010. As is common, the three countries agreed on a common external tariff regime (CET), with new tariffs based the highest tariff levels – Russia's – including its 'anti-crisis' tariffs. Consequently, the overall impact of the new Customs Union was to substantially increase import tariffs, especially in Kazakhstan (the most 'liberal' of the three countries). A harmonised customs code came into force on July 2010, while internal borders between the three countries were removed in July 2011.

On 1 January 2012 the Customs Union was transformed into a more ambitious 'Single Economic Space', largely inspired by the EU Single Market and its 'four freedoms' – i.e. free movement of goods, capital, services and people.

On 18 November 2011, the Presidents of Russia, Kazakhstan and Belarus committed themselves to create a Eurasian Economic Union (EEU), which would represent the 'third stage' of this regional integration process. The EEU process should be completed by 2015 and include defence, space and military cooperation, as well as other policies on research and development, environmental protection, and natural resource management. In part to stem China's economic penetration in Central Asia, Russia has asked Kyrgyzstan and Tajikistan to join the EEU.

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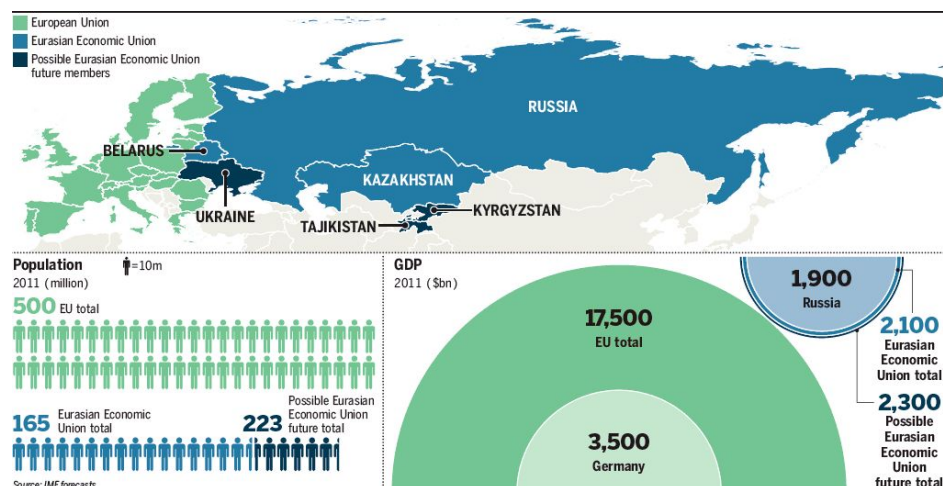
<sup>24</sup> Interfax, Kazakhstan, EU determine conditions for Kazakhstan's accession to WTO (5 June 2013)

<sup>25</sup> European Commission, [Trade and investment barriers report](#) (2012)

<sup>26</sup> USTR, [National Trade Estimate Report on Foreign Trade Barriers](#) (2013)

**Figure 14:**

Comparison of EU, European Economic Union and possible Eurasian Economic Union



Moscow has also promoted the launch of a 'CIS FTA' (free trade agreement) that is supposed to replace the existing network of bilateral FTAs between CIS members. On 19 October 2011, Armenia, Belarus, Kazakhstan, Kyrgyzstan, Moldova, Russia, Tajikistan and Ukraine signed the draft treaty. In fact, the treaty's significance is more political than economic, since there is little new content in the new CIS FTA compared to earlier initiatives from the 1990s.

The EU expressed its deep concern about the creation of the new Customs Union. As a result of the new Customs Union and the noticeable increase of import duties, access to the Russian and Kazakhstan markets has worsened. Kazakhstan has increased the tariff rate on some 5 400 tariff lines, and its average import tariff in 2010 increased from 6.7 % to 9.2 %. Kazakhstan also established tariff-rate quotas on imports of poultry, beef and pork as part of its Customs Union obligations. It should be noted that customs unions negotiated by WTO members usually result in a decrease (not an increase) in common external tariffs.

Another negative effect of the new customs area on relations with the EU is a likely delay in the conclusion of a new PCA with Kazakhstan. EU negotiators will have to choose either to remove key elements of the new treaty (technical barriers to trade, sanitary and phytosanitary, customs and trade facilitation, important parts of trade in goods, trade defence instruments) because they are now a full competence of the Customs Union, or to open negotiations to the Customs Union as a whole. This second scenario is politically and technically difficult: other members of the Customs Union may not be able to fully implement an enhanced WTO agreement when they still have to comply with basic WTO rules; the Russian position on negotiating a new PCA is rather stiff and the EU does not intend to enter a deal with Belarus under the current political framework.

## 5. Conclusions

In a number of ways, Kazakhstan has performed best among the former Soviet republics in Central Asia. Benefitting from rich natural resources, the country recovered from the collapse of the Soviet plan economy and posted very good results for most of the last decade. With a relatively open and market-oriented economy, Kazakhstan has increasingly integrated into the world trading system, although with some serious distortions, particularly in key economic sectors such as mining and oil.

Kazakhstan is currently an upper-medium income country, and one viewed – thanks to its hydrocarbon reserves – as a strategic economic (and often political) partner by most of its neighbours, the EU and the US. Trade with Europe is on the rise, and the EU is the country's first trading partner.

Increased revenues have helped improve infrastructure and social services, and the country has experienced significant progress in terms of human development and the fight against poverty. Social and regional disparities have not been entirely erased, however, and the country still faces serious economic, environmental and social challenges.