

Using petroleum wealth to diversify the Kazakh economy



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What is the investment strategy of Samruk-Kazyna?

In the investment portfolio of our national holding company, we have 138 projects worth a total of US\$139.4 billion, with the aim of creating more than 124,000 jobs during the construction period and more than 43,000 jobs during the operational phase. To date, 25 of the 138 projects have been implemented. Our goal is to diversify our economy, moving away from dependency on raw materials and towards high-tech industries. The projects include railways, factories, plants, production, technology and housing. As examples, Kazakhstan Temir Zholy has built in Ekibastuz a plant for the production of cable cars, with 3,340 built so far, and Kazakhtelecom is building a network of fibre-optic subscriber access in Astana, Almaty, and many regional cities.

At the same time, we are developing new industries. One such is the chemical industry. We are creating special economic zones in Atyrau and Taraz to attract partners and investors in chemical production, with natural gas supply laid on, and we have a United Chemical Company, which is implementing a project to produce petrochemical products. Another aim is to build a stable, balanced electricity supply through our company Samruk-Energy, and we have also begun developing alternative energy, such as wind and solar stations. A third area is mining, through our company Tau-Ken Samruk. Its task is to bring in modern technology for exploration, production and processing in mining metallurgy. One of our priorities is final processing, especially for gold because all our gold has been, until recently, exported in half-finished form. A fourth direction of new investment is real estate development. We recently initiated construction of the Zelyoniy Kvartal (Green Quarter) for "EXPO -2017". Finally, we are thinking about how to develop civilian engineering through our company Kazakhstan Engineering, which hitherto has been confined to the defence sector.

Is the sale to the population of minority interests in subsidiaries and the sale of non-core assets intended to free up funds for new investments?

The privatisation programme aims to restructure companies and make them more business like. Ownership of non-core assets distracts the managers

of our companies, as well as ourselves, from our core business, where we need to make money. This is the ultimate priority for us. It is also important in attracting technology and capital, and in improving corporate governance, which also increases efficiency and transparency at these companies.

What are the State's main objectives in this regard?

Primarily, the development of our share of small and medium-sized businesses, to increase their contribution to the economy and also develop the stock market. In our opinion, the participation of Samruk-Kazyna's portfolio companies will achieve these goals.

Of the 599 companies included in the structure of the Fund, 122 companies will be introduced into a competitive environment – of these 16 consist of non-core assets and 106 of core assets. We are going to sell at auction businesses considered unattractive to the market, such as holiday houses and hunting lodges, while those which have a good dividend base and have generated profits in the past few years are going to be transferred to the stock exchange. In order to improve the prospects for attracting investment into electricity generation (Samruk-Energy) and transmission (Kegoc), the government is working to improve the system of tariff formation. A new policy will be approved by the middle of this year. This will enable an upgrading of the relevant infrastructure.

In our privatisation programme, we are very conservative in estimating risks. We also plan to carry the programme out with maximum transparency and we intend to publish the data on the sale of assets to the private sector.

How has the corporate governance of Samruk-Kazyna changed as a result of this process?

First, we need to understand what is meant by corporate governance. As interpreted in the West, it is the 'art of management'. Since the establishment of our national holding company in 2006, a great deal of work has been carried out to form boards of directors, to set up the Institute of Independent Directors, and to build up external and internal audit systems.

All our documents are based on OECD standards. In 2009 the Organisation developed its methodology of corporate governance diagnostics, which we



have put into practice. We evaluate our level of compliance in line with these standards and calculate our so-called corporate governance rating on an annual basis. Today, a number of major companies, such as KMG, KTZh, Kazpost, Kazatomprom and Kazakhtelecom, have achieved the level of 70 per cent in terms of compliance with OECD standards. The leader is Kazakhtelecom at 80 per cent, a listed company with several major shareholders. This once again confirms that the placing of shares with the public, and privatisation, increases management efficiency. We aim to raise the average corporate governance rating for major companies to 75 per cent by 2015. Raising the corporate governance rating for a company will effectively lower its cost of capital, and attract investors. For any person or company willing to invest it is important to know that their funds will be recovered and will work for them. The corporate governance rating is a litmus test by which to evaluate potential risks.

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But you cannot rely solely on ratings. Shareholders should monitor the results of corporate activities, revenue, market conditions, and assume responsibility for the selection of the board of directors and, in general, pay attention to the transparency of the company. Transparency is not just a disclosure of information, but the authenticity of financial statements, and the absence of corruption and fraud. And the board of directors should ensure the protection of the interests of the shareholders, creditors and ordinary employees.

Accordingly, the professional composition of the boards of directors is important for us. We have conducted international benchmarking and determined that, in the leading companies of the world, boards consist of at least 10 people, and that most of them are high-class professionals with rich managerial experience, some of them ex-CEOs or partners of leading audit firms. But at the moment, our companies' boards consist of six people on average. This is why, in the medium term, we will increase the number of people on our boards and change their composition.

What are the reasons for the delay in resuming oil production at the Kashagan field?

The delay is related to the problems with the integrity of the pipeline system intended for the transportation of oil and gas from the seaport of "D Island" to the "Bolashak" land installation of the oil and gas processing complex. Oil production started in September 2013, but was halted in October after repeated gas leaks from the pipeline, due to sulfide stress cracking caused by localised excessive metal hardness. At present the operator of the North Caspian Project is developing a plan of repair and renewal operations which should be completed by mid-2014.

When Kashagan production resumes, will Kazakhstan require a new infrastructure to export the oil, or are the trunk pipelines to Russia and China sufficient?

In the short-term perspective of increasing oil production volume in Kazakhstan, including the planned production from Kashagan, no additional infrastructure for oil export will be required. This is because capacity in the Caspian Pipeline Consortium is being increased to 67 million tonnes per year, of which the capacity of the Kazakhstan region is being increased to 52.5 million tonnes per year, and because the capacity of the Kazakhstan-China oil transportation system is being increased to 20 million tonnes per year.

Is Kazakhstan, an exporter of crude oil but an importer of petroleum products, planning to increase its refining capacity?

Kazakh oil processing is currently strained to capacity. The growth of our dependence on imports of oil products is related to the growth of internal consumption, which is rising at approximately five to six per cent a year. Moreover, Kazakh refineries are not at present configured for full production of high-octane gasoline, of which 30-35 per cent has to come from Russia. But the aim is to meet all domestic demand with domestic refined products by 2017. The modernisation programme includes the construction of complexes for production of aromatic hydrocarbons and deep oil processing, and the modernisation of Pavlodar CPC, ensuring the possibility of processing up to 5.2 million tonnes a year of Kazakh crude and of PetroKazakhstan Oil Products, including production of Euro 4.5 environmental standards from 2016. ■