

# Kazakhstan's Energy in Foreign Policy

## *Oil and Gas in the Multi-vector Policy*

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Master Thesis in European and American Studies  
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Kazakhstan's Energy in Foreign Policy: Oil and Gas in the Multi-vector Policy

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# Abstract

This thesis examines the relationship between Kazakhstan's oil and gas resources and its multi-vector foreign policy. The relationship is explored by studying how oil and gas resources have been used in the multi-vector policy. The aim is to uncover general patterns of investment decisions and to see if political and foreign policy considerations have influenced energy development. This is done by studying decisions made by Kazakhstan regarding investments and development of its resources through selling rights to companies and export routes. In light of the data analyzed, the role of energy in the multi-vector policy is explored as a possible tool or as a driver. The thesis is based on a large pool of written accounts and interviews with practitioners in Kazakhstan's oil and gas sector and foreign policy.

In this thesis it is argued that Kazakhstan has developed its oil and gas resources and export routes in accordance with its multi-vector foreign policy. The United States, Russia and China are the most important vectors and partners in Kazakhstan's foreign policy, which is mirrored in Kazakhstan's energy development. From the year 2000 Kazakhstan has moved from being fully dependent on Russia for oil export toward more diversification and mutual dependence in its energy relationships. However, transit through Russia is still Kazakhstan's main export route. For Kazakhstan both economic and political considerations have played a part in decisions on energy development. Political considerations seem to have been important for investment and development decisions and appear to have hindered development of certain export routes. It is argued that energy has been used as a tool by Kazakhstan in relation to its multi-vector policy. In addition, there is some support for the view that energy can have a role as a driver for Kazakhstan's foreign policy.



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# List of Abbreviations

BGR-TBA	Bukhara Gas Region–Tashkent-Bishkek–Almaty pipeline
BTC	Baku-Tbilisi-Ceyhan pipeline
CAC	Central Asia Centre pipeline
CNOOC	China National Offshore Oil Company
CNPC	China National Petroleum Company
CPC	Caspian Pipeline Consortium
CSTO	Collective Security Treaty Organization
EIA	Energy Information Administration
GDP	Gross domestic product
IEA	International Energy Agency
IOC	International Oil Company
KCP	Kazakhstan-China Pipeline LLP
KCTS	Kazakhstan Caspian Transport System
KMG	KazMunaiGaz
KMG EP	KazMunaiGaz Exploration Production
KNOC	Korea National Oil Company
KPO	Karachaganak Petroleum Operating B. V.
LPG	Liquefied petroleum gas
NATO	North Atlantic Treaty Organization
NOC	National Oil Company
OPEC	Organization of the Petroleum Exporting Countries
OSCE	Organization for Security and Co-operation in Europe
PSA	Production sharing agreement
RFE/RL	Radio Free Europe/Radio Liberty
SCO	Shanghai Cooperation Organization
TCO	Tengizchevroil
UAE	United Arab Emirates
UK	United Kingdom
US	United States of America

# Units of Measure

Bbl	Barrel
Bbl/d	Barrels per day
Bcf	Billion cubic feet
Bcm	Billion cubic meters
Bn	Billion
Mcm	Million cubic meters
Mmcf	Million cubic feet
Tcf	Trillion cubic feet
Tcm	Trillion cubic meters

Map 1: Kazakhstan, Caucasus and Central Asia



Source: University of Texas Library, at:  
[http://www.lib.utexas.edu/maps/commonwealth/caucasus\\_cntrl\\_asia\\_pol\\_2003.jpg](http://www.lib.utexas.edu/maps/commonwealth/caucasus_cntrl_asia_pol_2003.jpg)

# 1 Introduction

## 1.1 Topic of this Thesis

After Kazakhstan proclaimed its independence 1991, it found itself landlocked and located between the major powers of China and Russia. Kazakhstan has enormous energy resources of oil and natural gas, but Kazakhstan lies far from the world's energy markets. The young state continues to face challenges regarding how to export its energy resources and to secure its independence from foreign energy interests. For Kazakhstan the route of pipelines exporting oil and gas is a major interest, and both a source of prosperity and potential political dependence. Economic and political developments since the 1990s have increased the competition and interests for Kazakhstan's energy<sup>1</sup> resources. For both the United States (US) and the growing giant China, Kazakhstan and Central Asia represent an alternative source of stable oil and gas supply and help to limit their oil dependence on the Middle East and OPEC. Several commentators, authors and scholars have described the competition for energy resources in Central Asia between the world's major powers as a new "Great Game" (Edwards 2003; Kleveman 2003; Yergin 2011, 44). The foreign policy and energy policy of Kazakhstan is vital for how the state meets its political situation in the international state system. This study explores the situation from Kazakhstan's point of view.

The relationship between Russia and Kazakhstan has historically been close, with their economies and infrastructure interconnected and interdependent since Soviet times (Olcott 1996). The interdependence relationship is asymmetrical however, with Russia as the stronger part and Kazakhstan relatively more dependent on Russia. This relationship is problematic for Kazakhstan because it makes Kazakhstan vulnerable to pressure. Russia, led by Yeltsin in the 1990s, did not seem that interested in Kazakhstan and Central Asia, but after Putin came to power Russia has found new interest in its neighbor and its energy resources. Russia, led by Putin, seems determined to promote its position as a major energy actor, and to secure control over energy transport from Kazakhstan and Central Asia.

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<sup>1</sup> Energy in this thesis refers to oil and natural gas extracted from hydrocarbons.

Since the independence of Kazakhstan, President Nazarbaev has described his foreign policy as multi-vector<sup>2</sup>. This policy is based on Kazakhstan's need to build relations and partnerships in multiple directions. Kazakhstan's foreign policy situation in Central Asia with powerful neighbors and a landlocked position, demands Kazakhstan to cooperate with others to secure export routes for their resources and its interests more broadly. The country's large reserves, growing production and export of oil and gas gives Kazakhstan an opportunity to use energy resources as a tool, to promote and achieve foreign policy interests and objectives. Energy resources can potentially help Kazakhstan overcome its difficult foreign policy position, and avoid too much dependence on any one state, especially Russia. Has Kazakhstan used its energy resources as part of its multi-vector policy?

## 1.2 Research Question

The purpose of this thesis is to analyze and explore the relationship between the oil and gas resources<sup>3</sup> of Kazakhstan and its multi-vector foreign policy in the timeframe of 1992 to 2012. The main emphasis is on the years from 2000, with the 1990s as a background. After 20 years of independence and conducting foreign policy, it is now possible to look back and explore developments. As a young state with substantial oil and gas resources and challenges in regard to foreign policy, Kazakhstan has been in a position where energy assets could be used for dealing with foreign policy challenges. Will not a state use every natural asset in pursuit of its goals and interests? If that is the case, how would Kazakhstan use its resources? The research question is: *How are the oil and gas resources being used by Kazakhstan in the country's multi-vector foreign policy?* In this relationship oil and gas resources are viewed as a means to an end for the state. This implies that Kazakhstan's oil and gas resources are used as a tool, meaning an instrument to achieve a goal. The nature of a tool is that it can be used once in multiple and separate processes as a dependent variable, such as making decisions, while the effect or outcome of the tool might be lasting.

The goal pursued with the tool is in this case the aims of the multi-vector policy, which is the independent variable with this perspective. A vector in this sense is a direction for foreign policy with a magnitude, for example, relations with Russia can be one vector. An important assumption of the research question is that there is a close relationship between Kazakhstan's

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<sup>2</sup> In this thesis the terms "multi-vector foreign policy" and "multi-vector policy" are used interchangeably to describe the same phenomenon.

<sup>3</sup> In this thesis oil and gas resources are also called energy resources, with no reference to other energy sources.



oil and gas resources and foreign policy. Because of oil being more significant than gas in terms of export and production, the main focus of the study is oil.

However, if it is possible that energy resources are a tool for the state's foreign policy, it could mean that the role of energy is more than a tool, given a close relationship with foreign policy. Oil and gas resources may perhaps influence foreign policy decisions in one direction or another thus having a role as a driver. In contrast to a tool, a driver has lasting influence over time as an independent variable, which can result in specific outcomes. It is therefore important to explore if oil and gas resources are a tool or a driver for the foreign policy of Kazakhstan. This study explores the direction of causality, but the research design of this thesis prevents a clear conclusion on the strengths of the causality direction because of the different direction of tool and driver.

Given that Kazakhstan has oil and gas resources, how can they be used as a tool for the government? For a producer and exporter, such as Kazakhstan, the main decisions related to the oil and gas business are how to develop production and transportation. If Kazakhstan has used its oil and gas resources as a tool, one would expect to observe this in decisions on production licenses and export routes. Decisions on transport are of vital importance in Kazakhstan's landlocked situation since the energy resources would have no value without development of costly and politically significant export routes. Consequently, it is relevant here to study how Kazakhstan has chosen to develop its oil and gas resources and how to develop export routes to foreign markets.

The research question is studied in two parts to uncover general patterns of investment decisions. First, the ownership structure of major oil and gas<sup>4</sup> fields and projects are examined. The aim of this is to uncover if Kazakhstan has followed a pattern when selling these rights to oil and gas companies with origin from foreign countries. This study examines if there are differences between foreign countries or vectors regarding involvement in energy projects and if economical or political considerations can have influenced decisions. Only the largest projects are included here. This is done because these cover nearly all of Kazakhstan's production and reserves. Second, the research question is studied by looking at Kazakhstan's choices regarding development of export routes for oil and gas. Here it is relevant to discuss existing pipelines and possibilities to expand them, the development of new pipelines, export

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<sup>4</sup> In this thesis gas and natural gas refer to gas extracted from hydrocarbon gas used as fuel.

routes by rail and sea, and potential routes that have not been developed by Kazakhstan. The aim is to look for a pattern of the direction and magnitude of the development of export routes, as well as study if decisions have been influenced by political or economical considerations. Is it possible see any influence from foreign policy and political considerations on choices in energy development?

In this thesis it is argued that oil and gas resources are important tools for Kazakhstan's multi-vector foreign policy. It is explored how energy resources have been used to promote important aspects and goals of the multi-vector policy, such as economic and political independence and sovereignty, maintaining a balance between great powers and developing mutually dependent partnerships. Further it is argued that political considerations have been important for development of its energy resources and in Kazakhstan's decisions on development of export routes. It is found evidence in support of the view that energy in Kazakhstan can have the role as a tool, and some evidence of a role as a driver. The analysis is based on a large pool of different sources, such as official documents and academic literature in addition to interviews with practitioners in field.

### **1.3 Contributions of this Thesis**

The main contribution of this thesis is to generate more knowledge of the relationship between the energy resources of oil and gas, and the multi-vector foreign policy of Kazakhstan. An additional aim is to contribute to a broader understanding of the role of energy in foreign policy as a possible tool and as a possible driver. An analysis of Kazakhstan can serve as an investigation of how energy exporters use their resource advantage to their benefit in foreign policy, without resorting to aggression through the use of oil and gas as a weapon. Even if the findings from Kazakhstan are not universally transferable, they may become a starting point for further research. Later in this thesis it is argued that the dynamics between politics, foreign policy and energy resources are not yet fully explored or understood.

### **1.4 Outline of this Thesis**

This thesis consists of six chapters. Chapter Two provides a theoretical and methodological framework for this study. First, the main topics of the study are outlined and findings in the literature are presented. Second, the methodical approach used in this thesis is discussed.

Chapter Three gives an overview of Kazakhstan's oil and gas sector, and presents empirical knowledge and data. In Chapter Four a discussion of the background for Kazakhstan's multi-vector foreign policy is provided. Furthermore an examination is given of topics in the multi-vector policy and how the policy has been carried out in practice. Chapter Five discusses Kazakhstan's oil and gas resources in relation to its multi-vector policy in three sections. The first section deals with Kazakhstan's decisions on development of energy projects. In the second section Kazakhstan's development of export routes are discussed. The final section discusses the findings presented earlier in Chapter Five in relation to how Kazakhstan has used its energy resources. The role of energy as a tool or a driver in relation to the multi-vector policy is discussed. In Chapter Six, the main broad findings are summed up with concluding remarks and points toward future research.

# 2 Theoretical and Methodological Framework

## 2.1 Introduction

The purpose of the first part of this chapter is to present an overview of the main topics of study and findings in the literature, which form a theoretical and analytical framework for this thesis. Terms and theory outlined in this chapter will be used in the analysis to draw lines between the literature and empirical findings. The second part of the chapter outlines the method used in this study and the considerations behind choices affecting the research process.

Section 2.2 presents an overview of literature on the relationship between energy, politics and foreign policy. Furthermore, a discussion is provided of a few subjects, such as energy as a tool of foreign policy, “pipeline politics” and the “energy weapon”. Section 2.3 starts with an outline of what the multi-vector policy is and its main components. Views and studies on the multi-vector foreign policy of Kazakhstan are discussed. Lastly, in section 2.3, a study on the role of energy in Kazakhstan’s the multi-vector policy is presented. This forms a starting point for exploring the field in this thesis. Section 2.4 gives a presentation and discussion of the mixed method design used in this study. Then strength and weaknesses of this design are discussed. Data sources are outlined, with regard to types of sources, language and transliteration. Lastly, the approach to conducting interviews and issues relating to the interviews are discussed.

## 2.2 Energy and Politics - The Close Relationship

Much is written in newspapers and by commentators in addition to academic literature on the subject of the relation and connection between energy and foreign policy (Sorbelli 2011, 26). In the literature there is foundation for the claim that energy and politics are closely connected (Shaffer 2009; Ostrowski 2010; Yergin 2011). One of the most thorough reviews on energy and foreign policy is the work of Linda B. Miller (1977), written in the context of the oil crisis in the 1970’s. One of the main volumes that Miller discusses is *Energy and World Politics* by Mason Willrich (1975). Willrich looked on the role of energy in world politics from a global

viewpoint, and emphasized the political dimension of energy problems. Willrich (1975, ix) stated that “the most fundamental energy issues are political in nature and international in scope”. He makes an analytical distinction between importers and exporters of energy, which has merit to it. Furthermore, Willrich (1975) argues that importers and exporters face problems regarding energy. The main problems identified are access to supply and price for exporters, and sovereignty and foreign markets for importers.

However, the distinction between different problems for energy importers and exporters can be too strict. Price is a major issue and problem for both sides of the table, not just importers. Importers want to pay the lowest price possible while exporters want the highest price achievable. In modern societies energy exporting states are often dependent on revenue from their exports to finance public budgets. Rick Strange (2009, 6-7) argues that energy price and stability are in the interest of both importers and exporters, and should be promoted to increase security. Energy is vital for a state’s security, and energy security is “closely and directly linked to general economic security” (Willrich 1975, 68). The need to secure the supply and access to energy links together a state’s energy resources, economy, energy policy and foreign policy. Consequentially, energy policy is an important part of a state’s foreign policy. Foreign policy can be used to make supply of energy more stable and avoid market shocks, by reducing political risk and conflict in energy producing regions and along trade routes (Strange 2009, 7). An example is for Kazakhstan to promote lasting peace and stability in Central Asia, to secure its energy production and secure export of oil through transit countries. Coordination of foreign policy and energy policy should, according to Strange (2009, 7), be used by both importers and exporters to promote energy price stability. They should do this because exporters are dependent on revenue from exports and importers are dependent on supply of energy. However, he does not discuss or explore how this coordination should be done. For prospective producers who need investments to develop production, foreign policy can help attract needed finance. The relation between energy and foreign policy is shown to be close and complex.

Brenda Shaffer (2009, 3), in her book, *Energy Politics*, states that “energy and politics are inseparable”. Energy is surely important to the state and an important issue in politics, however to claim that they are inseparable is quite strong. Her book gives a broad overview of the relationship between the two concepts, and highlights the links between importers and exporters in support of the views of Strange (2009). Shaffer (2009, 28) maintains that “state

of the world market affects broader international relations and vice versa.” The argument is built on the realities of oil dependence and the international character of the oil market, since changes in supply and demand around the world affects the world price for oil. For Shaffer energy is a tool that states can use in their foreign policy similar to any other means, she states that “States are no more likely to refrain from using energy to promote their policy goals than to ignore economic or military means of doing so” (Shaffer 2009, 1). A tool refers to an instrument of policy, where energy is a means to achieve policy aims. This argument has merit on the basis that states are rational. A tool can be used directly or indirectly to pursue a goal. If energy is to be used as a tool, it is required that a given state has the ability to use it. This implies that the state has to control production, export or transport of energy. The argument may therefore apply to Kazakhstan as an energy exporter, but not necessarily energy importing states.

Energy resources have been used as a tool in foreign policy by energy producers and transit countries in the past. One example is to enforce an embargo. The Arabic states launched an embargo in 1973-74 against the US due to the Yom Kippur war. Another example of energy resources as a tool is Hugo Chavez’s offering of oil and oil revenues to other states in Latin America to gain influence and support (The Economist 2005). In addition, in relation to the plans of a giant pipeline supplying South America with gas from Venezuela, the political goals were seen as more important than economics (New York Times 2006). This example shows that political considerations in development of energy export routes may be important for a government’s decisions. Energy can also be used as a weapon to pressure another actor or state that is dependent on supply or transit routes. A recent example from the 2000s is the gas disputes between Russia and Ukraine over natural gas supply, prices and debt. Shaffer (2009, 33) argues further that energy is more important and a more prominent tool in a state’s foreign policy during tight market conditions<sup>5</sup>. A tight energy market will be more sensitive to disruptions in supply and states become more vulnerable. In such a situation, the energy weapon can be more effective, and the incentive to use it may be strengthened as the potential reward is greater. The energy weapon is discussed below. The question that remains is how energy as a tool for foreign policy applies to Kazakhstan.

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<sup>5</sup> A tight market refers to a situation when there is little space between supply and demand, and is associated with high prices. An example is when there is barely enough oil to cover demand.

Energy can also influence foreign policy outcomes (Shaffer 2009, 28). For example, a state can be driven and influenced by energy needs to develop close cooperation and political agreements with another state, because of a need to secure transit or import of energy. While Shaffer (2009) argues in general that energy can influence and drive foreign policy, Paulo Sorbello (2011, 116) argues specifically that energy is one of the main drivers of Russian foreign policy under Putin. Energy can therefore possibly have two roles, as a driver of policy through influencing decisions, or as a tool for policy. A driver and a tool are opposed to each other in principle, since an instrument is opposed to the aim or driving force of using the tool. On the other hand they could be complementary in practice in that energy may influence and drive foreign policy, and simultaneously the state can use energy as one of several tools to achieve the aims set for foreign policy. Nevertheless, it might be possible that energy can change between the roles over time, and across different policy issues.

### **2.2.1 Energy and Foreign Policy**

Some scholars have linked “energy dependence” and “energy security” in relation to foreign policy (Mitchell, Beck and Grubb 1996; Massari 2007, 9). The link is as follows, when a country is dependent on another for energy it is vulnerable regarding its energy security, since it has to rely on foreign markets. Higher degree of energy independence will enhance a country’s energy security. In a dependent relationship there is potential for states supplying energy to use energy as a tool, by use of the energy weapon to enhance its foreign policy situation, since states can use energy as leverage to pressure others. In relation to Kazakhstan this would mean stopping energy supply by Kazakhstan or by one of its transit countries, such as Russia.

Shaffer discusses the energy weapon and differentiates between oil and gas because of their different nature (Shaffer 2009, 33-35). Stopping energy supply is difficult regarding oil, because of the global market characteristics of oil with most of the transportation of oil made by independent tankers. The connection is therefore often indirect between supplier and customer. For gas there is a much more direct relationship, since transport is mainly done through pipelines. However, if a state is landlocked, such as Kazakhstan, it may be more vulnerable to the energy weapon than other states, since it is as a producer is dependent on transit countries to access markets. The energy weapon is an example of energy being used as a tool directly. According to Shaffer (2009, 38-39), an important aspect regarding the

vulnerability to the energy weapon is the degree of dependence or interdependence between the actors involved with supply and consumption. Mutual dependence can reduce the risk of the energy weapon being used, because it will hurt both parties if supplies are disrupted. This argument has merit considering that if the supplier is dependent on revenue from sales of energy and the consumer or transit country is dependent on supply of energy to run its economy, then it is unlikely that the actors will use the energy weapon. This argument applies well to Kazakhstan as a producer with limited export options since it has a relative mutual dependence relationship with its transit countries. If there is a high degree of independence in the relationship, for example where the supplying country is not dependent on sales to a specific country, then the supplier is in a relatively stronger position and can use the energy weapon with less financial costs and less harm to its own economy. According to Jérôme Gulliet (2011, 59), gas can only be used as a weapon in “highly asymmetrical relationships”. Kazakhstan’s neighbor Russia has been accused of using the energy weapon against its neighbors, but the reality and effectiveness of this weapon is still disputed (Smith 2006, 1-2; Goldthau 2008, 54; Rutland 2008, 207-208). Kazakhstan runs the risk of being targeted by the energy weapon by its transit countries, especially Russia, since the export and transit is more important economically to Kazakhstan than to its transit partners. If Russia in this situation threatens to close its borders and pipelines regarding energy transport, then Kazakhstan would be forced to comply with the demands or suffer major damage to its economy. If Kazakhstan chose to do the same action, then it would just hurt itself more than its transit countries, since Kazakhstan is unable to export its energy elsewhere. Kazakhstan’s oil and gas resources are not worth much without access to markets to be sold. This makes it in Kazakhstan’s interest to have full access to markets and not stop the supply. Economically a more effective export network with more export routes enhances economic interests and development. Kazakhstan can thereby benefit from a more secure export situation. In addition, using this weapon would hurt foreign relations and credibility. It is therefore difficult for Kazakhstan to use this weapon. The energy weapon is nonetheless a factor to consider in the dynamic between energy producers and their transit countries, which is relevant for Kazakhstan.

According to Sorbello (2011, 25), many studies that analyze energy and politics refer to price as a key variable that can change the balance of power between actors. Examples of such studies are by Daniel Yergin (2006) and by David Deese (1979). This point can be seen in light of the energy weapon, since price affects the vulnerability and strength of the actors. In opposition to studies such as Deese (1979) and Yergin (2006), are Shaffer (2009) and



Sorbello (2011, 25), who holds that the emphasis on prices and by that a tight market, in relation to the case of Russia, is exaggerated. Prices can influence states' behavior in foreign affairs, following Yelena Kalyuzhnova (2002), but Sorbello (2011, 25) argues that a country such as Russia is not a price-setter in the world market that can dictate price. Therefore importers and exporters can take advantage of their situation when the price is in their favor. This point should also be the case for Kazakhstan, which is not in a position to dictate price. However, the Organization of Petroleum Exporting Countries (OPEC) has the power to influence the price of oil and use that to their advantage (Kaufmann, Dees, Karadeloglou and Sánchez 2004). Higher oil prices can strengthen Kazakhstan financially and make its resources more attractive to foreign investors. At the same time revenue from high prices is a powerful incentive to take more control over the oil sector<sup>6</sup> to maximize value from energy rents, which gives rise to resource nationalism and national oil companies (NOCs) (Shaffer 2009, 23, 30-32). More than 75 percent of world oil and gas reserves are controlled by national oil and gas companies (Shaffer 2009, 29). This is a sign of states' desires to control energy and maximize energy rents.

The literature on the connection between the terms "energy" and "foreign policy" can however be criticized, following Sorbello (2011, 26), for lacking empirical studies that show scientific correlation between energy and foreign policy. This is a result of the lack of statistical academic studies of the relationship. However, the relationship can be difficult to describe and explore in a statistical study because the complexity of the relationship makes it difficult to quantify and reduce it to numbers. Furthermore, most of the research on the relationship between energy and foreign policy is only given limited space, as a chapter or a small part in a larger work or edited book (Kalyuzhnova, Jaffe, Lynch and Sickles 2002; Øverland, Kjærnet and Kendall-Taylor 2009). One exception is the study by Sorbello (2011). One should note here that most of the studies of energy and foreign policy have come in times with tight market conditions or energy crises, when energy problems are high on the public agenda and receiving attention from the media (Sorbello 2011, 26). The fact that a great deal of the literature on the subject have a journalistic background as opposed to academic, can be seen in relation with the greater focus on these issues during and after energy crises (Sorbello 2011, 26).

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<sup>6</sup> In thesis the oil and gas sector refers to oil and gas production, transportation and refineries.

Regarding energy, and Kazakhstan more specifically, issues concerning transportation are vitally important because production is usually located far from markets and consumers. Pipelines are the main way to transport oil and gas in large volumes from Kazakhstan because of its landlocked position (one alternative is by rail), and is an important issue in relation to Kazakhstan's foreign policy. Pipelines only happen when there is a need for new capacity for transport and there is agreement and benefit for everyone involved (Gulliet 2011, 59, 60 and 63). The route of the pipeline is important regarding which marked and transit country Kazakhstan commits to export. In addition to economic considerations, politics often limit alternative transit routes for pipelines (Stevens 2009, 17). A reason for this is that some transit countries may not be stable or trustworthy enough to qualify. This point refers to considerations done by the energy producer as well as investors financing the project with loans and credit for 20 years or more. This is a long-term commitment so the relationship and understanding between the actors involved has to be good and stable. "Pipeline politics" is a term for the political struggle regarding the building of and routes for pipelines (Sorbello 2011, 44). Political agreement is vital for construction of pipelines, especially pipelines that cross international borders (transit pipelines), since this major piece of infrastructure relies of support of local government (Gulliet 2011, 70). Transit pipelines, involving a third party and sovereign state, also have the problem of lacking a legal jurisdiction (Stevens 2009, 2). Political pressure can therefore make or break the prospects for a pipeline. However, politicians cannot build a pipeline without commitments from a supplier, a purchaser, transfer fees and an agreed price (Stevens 2009, 15; Gulliet 2011, 68,69,70). Paul Stevens (2009) and Gulliet (2011) make a distinction between political and economical considerations regarding development of pipelines. The need for transit pipelines through neighboring countries makes this an important issue for a state's foreign policy. It is important both to develop relations and decide on new projects and to secure stable relations after the pipeline is built. As a consequence, pipelines are a central issue for both Kazakhstan's government and other actors with a stake in the development and export of oil and gas in Kazakhstan.

## **2.3 Kazakhstan and the Multi-vector Foreign Policy**

The term "multi-vector" has been the label on Kazakhstan's foreign policy since President Nursultan Nazarbaev established it in his article "A Strategy for Formation and Development of Kazakhstan as a Sovereign State" published in 1992 (Nazarbaev 1992; Hanks 2009, 257).

Not only has President Nazarbaev laid the foundation of Kazakhstan's foreign policy, he has also controlled it as president of Kazakhstan for over 20 years. Since 1992 the multi-vector approach has been fairly constant and affirmed as Kazakhstan's approach to foreign policy and foreign relations (Hanks 2009, 257). Kazakhstan has followed Nazarbaev's strategy and multi-vector approach in several areas, discussed in Chapter Four.

What is the multi-vector foreign policy? The term "multi-vector" comes from the term vector used in mathematics and physics. A vector is generally a geometric object with a magnitude and a direction. One central feature of the multi-vector policy is pragmatism. According to Reuel Hanks (2009, 259), "the term multi-vectorism refers to a policy that develops foreign relations through a framework based on a pragmatic, non-ideological foundation." This pragmatism means that Kazakhstan has been following a cost-benefit analysis in foreign policy as an inter-state actor. This can be related to the realist model on state behavior, where self-interest is a primary motivation. Kazakhstan's landlocked status points to pragmatism as a necessity to come to agreement with its neighbors (Cummings 2003a, 142). If Kazakhstan had an ideological approach to foreign policy, it would limit options and make Kazakhstan more vulnerable. For example, if Kazakhstan followed a principle to not develop close relations and not do business with China because of its communist party, then Kazakhstan would ignore a potential partner as well as becoming more dependent on Russia. With powerful neighbors such as Russia and China, with an asymmetric relationship toward Kazakhstan, it is expected that Kazakhstan acts with flexibility and adapts to developments to maximize benefit and autonomy for Kazakhstan. It is therefore reasonable that pragmatism is an important part of the Kazakh<sup>7</sup> multi-vector policy considering Kazakhstan's actions over the years and the foreign policy situation.

In addition to pragmatism, a central component in the multi-vector policy is to develop good relations with all important foreign actors, especially neighbors, and to balance between foreign powers (Sultanov and Muzaparova 2003, 187). Multi-vector also implies relations in every direction. President Nazarbaev outlined this feature in his strategy from 1992, which stated that Kazakhstan should develop close ties with the states of the Commonwealth of Independent States, Europe, Asia, North America and the Pacific Basin, with Russia and Central Asia as top priorities (Nazarbaev 1992; Hanks 2009, 260). This balancing game is

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<sup>7</sup> The term "Kazakh" refers to the state of Kazakhstan in this thesis, not to the ethnic group.

important for small states to keep their autonomy, especially those states that are neighbors to a great power that can dominate the small state in an asymmetrical relationship (Nexon 2009).

The main contributions for understanding of the multi-vector foreign policy have come from Kazakhstan. President Nazarbaev and the ministers of foreign affairs and top officials in the Kazakhstani government, such as diplomat Tair Mansurov, Kasym-Zhomart Tokaev (former foreign minister) and Oumirserik Kasenov (former director of the Kazakh Institute of Strategic Studies), have outlined the multi-vector foreign policy with priorities on strengthening state sovereignty, integrity and inviolability of borders, and protecting economic interests (Kasenov 1995; Sorbello 2011, 29). Kasenov (1995) maintained that securing good relations with neighbors continues to be the only alternative for Kazakhstan to gain security. This demands balancing between the neighboring states. Both Kasenov (1995) and Tair Mansurov (1997) have underscored the special importance of relations with Russia and the need for strategic partnership. Furthermore, Mansurov (1997) identified three main directions by which Kazakhstan's foreign policy toward Russia was to be based: integration, sovereignty and strategic partnership.

Scholars in the United States and Europe who study Kazakhstan have mostly concentrated on state-building, society and geopolitics of Central Asia. Among the most important scholars on Kazakhstan are Sally Cummings (2000; 2003c; 2005) and Martha Brill Olcott (1996; 2002; 2005) who have written several extensive studies in the post-Soviet era. However, works on the multi-vector foreign policy are not many and the subject is often referred to in just one chapter of a larger study, but this leaves room for more research. Some works have nonetheless studied the foreign relations between Russia and Kazakhstan (Alexandrov 1999; Mansurov 2001). Robert Legvold (2003a) and his contributors present analysis of the perspective, foreign policy and interests of Russia, the United States, China, Japan and Europe toward Kazakhstan. The chapter by Bulat Sultanov and Leila Muzaparova (2003) analyze Kazakh views on the major external powers foreign policies toward Kazakhstan. They touch upon the multi-vector policy. They do not discuss the foreign policy of Kazakhstan itself. Seen from abroad the multi-vector policy may only be viewed as another phrase for a pragmatic foreign policy. Nonetheless, in this thesis the multi-vector policy is studied from Kazakhstan's point of view. The study of role of energy in foreign politics, especially in relation to Kazakhstan, has attracted less attention in the literature. There are some works dealing with the economics and politics regarding the oil sector, how it is

organized and implications for Kazakhstan and the Caspian region's economy and regime (Kalyuzhnova 2008; Najman, Pomfret and Raballand 2008; Ostrowski 2010).

According to Wojciech Ostrowski (2010, 8), "oil plays a key role in the political and economic life of post-Soviet Kazakhstan." By following Ostrowski (2010), it can be argued that the oil and gas industry plays a role in regime stability and regime survival in Kazakhstan. The government can use oil revenue, by granting positions and work to both the elite and the masses to counter dissent and opposition. The importance of Kazakhstan's resources to western international oil companies made them support President Nazarbaev and the current regime, and plays a role in stabilize the country (Ostrowski 2010, 149-153). Another political perspective is that Kazakhstan's oil and gas resources enhance the state's standing and importance to other states, especially relative to those countries which are dependent on oil and gas imports, thus gives Kazakhstan a better bargaining position in foreign affairs. This argument strengthens the view of energy as a tool for foreign policy as presented by Shaffer (2009). In this case to have energy means one more tool available for enhancement of the state's status and situation.

Cummings (2003a) has explored national identity and ideas in relation to Kazakhstan's foreign policy. She argues that the foreign policy, termed "multi-vector", is pragmatic and not built on ideology. In addition, Cummings (2003a) argues the leadership of Kazakhstan has used foreign policy to legitimize its rule and reshape national identity. Cummings (2003a) agrees with Kasenov (1995) on the matter that pragmatism in the pursuit of good relations with neighboring states and the priority of the relation with Russia is the only solution for Kazakhstan. According to Cummings (2005, 3), one of the main underlying reasons for the multi-vector policy was the need to secure multiple pipeline routes for export of energy and to attract a differentiated group of foreign investors to become less dependent on Russia.

Hanks (2009) fill some of the void in the literature by giving an assessment of the multi-vector policy and its evolution. Hanks (2009) has some good points and views that are useful and relevant to build on for this thesis. Comparable to Cummings (2003a), Hanks (2009) argues that the base for multi-vector foreign policy is pragmatism. In addition, Hanks (2009, 259) links this pragmatism with the states' interests as a basis for policy, where a cost-benefit analysis is central to foreign policy actions. This relates to a realist rational model view on the foreign policy of Kazakhstan. Nonetheless Hanks does not see the factors behind foreign policy as exclusively external, but also open to a domestic dynamic. For Hanks (2009, 260)

the two main foreign policy goals that guide multi-vectorism are state security and economic development. He agrees with Cummings (2005) that the main driver behind the policy was the need to develop production and export routes with multiple partners (Hanks 2009, 264). This last point relates to the pragmatic nature and economic priorities of the multi-vector foreign policy. Here Hanks (2009) and Cummings (2005) both point out economical and political considerations as part of the relationship between Kazakhstan's energy resources and multi-vector. The weight on political considerations can point to energy being a tool to pursue foreign policy goals, such as reducing Kazakhstan's dependence on Russia. In comparison with the other states in Central Asia, Kazakhstan's importance in regional and world affairs is magnified by possessing energy resources and its geopolitical position (Hanks 2009, 257-258). Furthermore he points out that, in addition to Kazakhstan, other states such as Armenia and Kyrgyzstan in the post-Soviet space also have developed a foreign policy that can be termed "multi-vector" (Hanks 2009, 259). However, Kazakhstan has been the most consistent and skillful in their development and execution of the multi-vector policy among the former Soviet states.

Paolo Sorbello (2011) has studied the role of energy in foreign policy, with his research on the Russian – Kazakhstan relation from the Russian perspective. Sorbello (2011) does have a different perspective on energy than other scholars who view energy as a tool such as Shaffer (2009), or as a part of and related to economic development such as Deese (1979). However, as Sorbello (2011, 117) points out, no one variable (energy) is sufficient to explain the direction taken by government officials. This point was considered in this thesis by choosing to study energy and foreign policy in a relevant and influencing context, such as the geographical situation of Kazakhstan. According to Sorbello (2011, 117), energy has the unique characteristic of being both a tool and a *trigger* for foreign policy decisions. Here Sorbello is quite radical in arguing that energy is a trigger and thus more than a driver. He goes further than Shaffer (2009, 28), who argues that energy influence foreign policy outcomes. From one point of view energy can be a tool or instrument for foreign policy through control over and use of pipelines as leverage to influence others and promote dependence. From the alternative view energy can possibly trigger foreign policy decisions by the interest of energy companies such as Gazprom and Lukoil (Russia), which are integrated with the state and part of the formulation and execution of national interests. The position of energy is also apparent when you consider that energy is on top of the agenda for Russian foreign policy, and in meetings between Russian and Kazakh leaders (Sorbello 2011, 117).

This points to that energy is central in the relations between Russia and Kazakhstan. Compared with Sorbello (2011), this thesis is more broadly based by not being limited to just Russia- Kazakhstan interaction, and by having a perspective more from Kazakhstan's viewpoint and of the situation in relation to multiple partners. However, it is beyond the scope of this thesis to study the subject with all the variables and depth as Sorbello (2011) does.

One scholar to study the relationship between energy and the multi-vector foreign policy of Kazakhstan is Pinar İpek (2007). İpek (2007) argues that Kazakhstan has followed a multi-vector foreign policy in relation to the geopolitics of energy exports and development of the country's oil resources. The argument is that development and export of energy resources and significant geopolitical considerations is a determinant of the foreign policy, with only a limited role for national identity and internal political dynamics. Here there is a difference to Hanks (2009), who is open to domestic dynamics. Furthermore, İpek (2007) highlights the importance of Kazakhstan's relationship with Russia and its geopolitical position, for how the energy resources has been developed and exported. Kazakhstan's dependence on Russia for pipelines and their economic integration means that pragmatism is and was the only alternative for foreign policy. Here she agree with Cummings (2003a). By bringing in American, European and Chinese companies in the energy sector, developing new export pipelines and keeping good relation with every major power and neighbor, Kazakhstan gradually weakened its dependence on Russia and balanced the major powers. Nonetheless according to İpek (2007, 1183,1187) Kazakhstan followed a strategy of inclusion toward Russia and made concessions because of their landlocked position and the need to keep good relations with Russia. Strategic partnerships with Russia, China and United States are all viewed as necessary for Kazakhstan to balance the three great powers. İpek's study shows that energy can play an important role in foreign policy by balance between foreign states, and that political considerations play a part in decisions on investments and development of energy resources in Kazakhstan. These points will be explored more in this thesis.

The literature points to a close relationship between energy and foreign policy. There are several studies on the multi-vector foreign policy of Kazakhstan. The views of the scholars seem to have reached a consensus on what the multi-vector is and that it is conducted by Kazakhstan. Conflicting viewpoints in regard to Kazakhstan have therefore been difficult to highlight in this chapter. There are few studies on Kazakhstan's multi-vector policy and its relation to energy. The study of İpek (2007) suggests that Kazakhstan's energy resources and

export routes have been developed in accordance with the multi-vector policy. Ípek's view will be explored further in this study, by using it as a starting point to determine if there is support for this argument. The lack of specific studies on the topic of this thesis means that there is room for more studies and gives an opportunity to develop knowledge on the relation between energy and foreign policy in Kazakhstan. The works of Shaffer (2009) and Sorbello (2011) suggests that energy can be a tool and a driver for foreign policy. What are a tool and a driver in this case? The nature of a tool is that it is applied once in a process to produce an outcome that lasts over some time. In this case energy can be used in a decision to achieve a policy aim. Both Shaffer (2009) and Sorbello (2011) argue that energy can be an instrument or a tool for foreign policy. A driver operates over time and has lasting influence over outcomes. As a driver energy can influence foreign policy decisions. Shaffer (2009) is more moderate by claiming that energy can influence foreign policy outcomes, however Sorbello (2011) claims more strongly that energy is a trigger of foreign policy decisions. The perspectives on energy as a tool and driver have different causality directions. As a tool energy is the dependent variable being influenced by foreign policy the independent variable. As a driver, energy is the independent variable influencing foreign policy. Because of this difference in causality it is explored here if energy is a tool or a driver. The research design of this thesis limits the study from uncovering the strengths in causality of this relationship. However, this thesis explores the relationship in regard to Kazakhstan.

How this relates to Kazakhstan is explored by studying if economical consideration or political considerations has played a part in investment decisions made by Kazakhstan regarding development of energy resources and export routes. If considerations were mainly political and played an important part in decisions, it then points towards energy having a role as a tool. This is because it implies that political state aims are the driving force for energy. If considerations were mainly economic, it then points towards energy's role as a driver, since economic gains from energy revenues may be the driver behind decisions. However, the fact that economic development is a key goal for Kazakhstan complicates the issue, and makes it also possible that energy development on economic considerations is a tool in pursuit of a state's political goal.



## **2.4 A Mixed Method Study**

The scope of the research question suggests mainly using qualitative data and thus using a qualitative method. Qualitative data is better suited for analytical descriptions. A qualitative approach is well suited to study a phenomenon in depth, as is the aim here (Grønmo 1996, 80; Johannessen, Tufte and Christoffersen 2010, 32). However, a mixture of methods in collecting data was chosen to explore the research question. “Mixed methods design refers to the use of two (or more) research methods in a single study, when one (or more) of the methods is not complete in itself” (Morse and Niehaus 2009, 9). For example, when collecting information on Kazakhstan’s energy sector, much of it is available as statistics and other quantitative data. This promotes a degree of method triangulation, by seeing a phenomenon from more than one perspective (Johannessen et al. 2010, 367). Data base for the analysis is strengthened by using more than one method.

The main approach here is text analysis of a large pool of relevant written sources on the research field. Quantitative data on Kazakhstan’s energy production and reserves is used to better understand its importance and related dynamics. As support to the written sources interviews were conducted of informants with knowledge of or experience from Kazakhstan’s energy industry and its foreign policy. These interviews were conducted in Norway and during a fieldwork in January 2013 to Astana and Almaty in Kazakhstan. The aim of these interviews is to get better insight in the issues, relationships and problems most important for the study. Interviews are also used to get a deeper and broader understanding of the research field, and thus better be able to analyze the research question. The reasoning behind this is that traveling to Kazakhstan and receiving input from informants with great knowledge of the research field gives a better foundation for fruitful analysis.

### **2.4.1 Strengths and Weaknesses of this Design**

Regarding strengths, qualitative data from text analysis and semi-structured interviews give the flexibility of changing focus and aim during the data collection and pursuing relevant information (Grønmo 1996, 81-83). Qualitative interviews imply a close relationship with the sources. Combined with the flexibility of a semi-structured design it gives prospects for relevant interpretation and analysis of the collected data. Too much flexibility in data collection in the quest for relevance may lead to limited validity because of fragmented data

(Grønmo 1996, 83). Use of qualitative method and data also has the strength of exploring a phenomenon in depth. By using a mix of qualitative and quantitative data the confidence in the results of the analysis is strengthened, and can give a better overall picture of the phenomenon studied (Grønmo 1996, 99). The research design can consequently offer a holistic view of the phenomenon in its relevant context.

An important test for judging quality of a research design is construct validity (Yin 1994, 32-33). This validity refers to “establishing correct operational measures for the concepts being studied” (Yin 1994, 32-33). To ensure construct validity, multiple sources of evidence have been used and to build up a chain of evidence in the data collection. A series of interviews of informants were conducted to strengthen validity of data collected. Because of the subjective nature of qualitative method and data collection the study may be weakened by the researcher’s potential biases. I have been aware of this threat to validity and reliability, and have therefore sought to be as objective as possible in the role as researcher. To strengthen reliability an outline of the approach to interviews, a list of informants and documentation of data sources are provided in the study.

One major weakness of this research design is that it is difficult or maybe impossible to generalize the findings in this study to the energy and foreign policies of other states. Since only Kazakhstan is studied here there is no way of knowing if the phenomenon studied is unique or not. The low extent of generalization of research results means that external validity of the study is weak (Edmonds and Kennedy 2013, 4-5). A quantitative study with extensive use of quantitative data across many cases is best suited when the aim is to make broad generalizations (Ragin and Amoroso 2011, 37, 54).

## **2.4.2 Data Sources**

This study has been based on a large collection of different primary and secondary data sources. Scholarly literature from books, journal articles and reports have been drawn upon and utilized. Newspaper articles from the internet have been used to study unfolding events. The internet can be problematic regarding reliability because of its volatile nature, but was necessary and invaluable to be up-to-date on relatively new events and developments as well as to get access to sources not available elsewhere. Use of public documents, statements and speeches, mainly from Kazakhstan, were important sources to get better insight to public

policy. Interviews of informants provided a supplement to written sources and a better understanding of the research field.

In this thesis it is used sources in Norwegian, English and Russian originated from Kazakhstan, the Caspian Region, China, Russia and Western countries. Sources in Russian were crucial for data material and analysis, as well as sources in English. A command of the Russian language has been invaluable to be able to study relevant sources on the research field. This thesis is not based on any sources in Kazakh, since I do not know the language, but this has not been a major problem. Most newspapers and public information from Kazakhstan are published in English, Russian and Kazakh.

Many of the sources used in this study are secondary sources. This means that data is interpreted by other authors and news reporters. This problem of reliability was limited by conducting cross-checking of these sources. I have been aware of possible bias in these sources, and have endeavored for objectivity.

Different sources give different estimates of oil and gas production. In this study data from BP (2012) is used, to be able to compare over time. The data from BP is widely used by researchers. Conversion between different measurements is done by using the conversion factors in BP (2013b).

For transliteration of names and literature in Russian, this thesis uses a simplified version of the American Library Association - Library of Congress system (ALA-LC) (Library of Congress 2012). Exceptions to this practice are names that have an accepted norm for transliteration, or where an author has made a particular choice of transliteration.

### **2.4.3 Approach to Qualitative Interviews**

The selection of informants was strategic by recruiting persons with relevant background, knowledge and experience. The “snowball method” was used to find relevant informants willing to be interviewed. The snowball method works by asking experts on the field to recommend others that the researcher should contact to interview and then repeat the process (Johannessen et al. 2010, 109). I approached potential informants directly and received recommendations for new candidates. Some informants were difficult to contact directly and there was also the challenge of locating relevant individual informants in a corporation or

institution. Recommendations helped overcome these issues. This resulted in ten interviews completed in Norway, Astana and Almaty in Kazakhstan. Time and resource constraints limited the number of informants to ten. Semi-structured interviews were used with key questions and topics prepared in advance. This gave flexibility to ask follow up questions and create a relaxed and more informal setting than would have been the case with a structured questionnaire. The interviewed informants are representatives of the oil and gas community in Kazakhstan, representatives of international oil companies (IOCs) operating in Kazakhstan, journalists and researchers<sup>8</sup>. Unfortunately, I was not able to get interviews with public officials and representatives of Kazakhstan's government and national energy companies as this proved very difficult. The fact that their perspectives are not represented is problematic for the reliability of the study. However, use of written sources such as public statements and public documents issued by the government and national energy companies may limit this disadvantage.

Anonymity was offered to informants and was important to encourage an open discussion. The problem with anonymity is that it limits the possibility for others to verify the accounts in question (Ragin and Amoroso 2011, 103-104). Even if full real names and citations may give better evidence, it is still better to have the interview take place than to have the issue of anonymity limit the sample. This was also an important consideration in relation to recruitment of informants. Written notes were taken down during the conversation but without a tape recorder. This approach was chosen to encourage a more relaxed interview setting and to assure the informants that they would not be quoted against their will. Some of the informants have read through the thesis before they approved their name being attributed to the list of informants. This was done according to their request to ensure that there were no misunderstandings and errors regarding material from the interviews. This fact may increase reliability. The conclusions done in the study have not been changed after this process.

Several of the interviewees did not want to be quoted or be attributed to "on record". To respect these wishes written published sources have been found to confirm facts and to represent views presented by informants. Even without direct citation the interviews have been invaluable to this study. This can be seen in relation to the point of anonymity, since

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<sup>8</sup> A full list of informants is provided in the reference list.

some persons and their views were anonymized to reduce the likelihood of their having problems their employer.

Interviews challenge the researcher to reflect on his/her role as a researcher. Interviews that are not fully structured carry the risk that information given by the informant may be affected by the relationship between researcher and informant (Johannessen et al. 2010, 138). The fact that I am a “western outsider” interviewing informants in Kazakhstan, may have resulted in different results and information gained than if the interviews were, for example, carried out by a local researcher from Kazakhstan. Cultural difference may play a part in interpretations of the researcher. This challenge to reliability has been met by being aware of the danger and by conducting more interviews to lessen risk of bias. As a Norwegian I had some advantages as a researcher in the quest to recruit informants because there was an opportunity to enlist help from Norwegian diplomats, businesses and nongovernmental organizations based in Kazakhstan.

# 3 Oil and Gas Resources in Kazakhstan

## 3.1 Introduction

The importance of oil and natural gas to the prosperity and security of states is difficult to overstate. According to the International Energy Agency (2012) (IEA), in 2010 oil amounted to 41.2 percent and natural gas to 15.2 percent of total world energy consumption. Combined these fossil fuels accounted for 56.4 percent of world energy consumption with oil having a dominating share of energy used for transportation. In addition, to oil and gas importance to the world in broad terms, these resources are also central to Kazakhstan's economy.

The aim of this chapter is to present an overview of the oil and gas sector in Kazakhstan. First the difference between oil and gas is briefly presented. Then the oil and gas sector in Kazakhstan is outlined including production, importance to Kazakhstan, major projects, pipelines and other transportation and refineries.

## 3.2 Difference between Oil and Natural Gas

Oil and gas have important differences that need to be considered to understand their impact on policy. Both oil and gas can be used to generate electricity, provide heat, but oil is much more widely used for transportation (Shaffer 2009, 11-13). Oil is liquid and can be stored easily. It can be transported by trucks, rail or pipeline. Oil has more energy per unit than gas, and is a global commodity with a world price. Characteristics of oil affect the price for a barrel (Shaffer 2009, 12). This relates to if the oil is "sweet" or "sour"<sup>9</sup>, and if it is "light" or "heavy". The characteristics "heavy" or "light" oil refer to the density of the oil, with light oil giving a higher yield of petroleum products than heavy oil (Shaffer 2009, 12). The cost of production of oil and gas differs different from location to location. Difficult extraction processes and remote extraction locations far from markets drives the price higher.

Natural gas is more challenging to store and transport. Natural gas production and transmission is more complex and expensive than for oil (Kandiyoti 2008a, 14). In contrast to

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<sup>9</sup> Sweet and sour refers to the amount of sulfur in the oil, which need to be cleansed at the refinery. A raw product with more sulfur or sour oil is more expensive to refine, and therefore are given a lower price.

oil, gas is transported mostly by pipeline directly from the producer to customer with a price being negotiated on long term contracts. Pipelines' long term horizon and then political connection relates to the fact that pipelines cannot be moved when they are built. Rail and trucks are not practical for large scale gas transportation. Gas can be transported by liquefied natural gas tankers. This is not possible for landlocked countries. Natural gas has an advantage over oil in that it releases lower emissions that contribute to pollution. Even so, legislation that forces environmental concerns is needed for this to directly affect price. These differences of the long term commitment, reliance on pipelines and need for political support combined with aspects relating to pipelines discussed in Chapter Two, means that generally gas is more closely connected to politics than oil. However, since Kazakhstan is landlocked it is more reliant on pipelines than other countries. It could be interpreted that oil and its transportation is more connected to politics in Kazakhstan.

## **3.3 Oil and Gas in Kazakhstan**

### **3.3.1 Overview**

Discoveries, extraction and production of oil and gas have been developing in Kazakhstan since Soviet times. However, because of technological difficulties of developing petroleum fields and lack of investments, most fields and the whole industry in Kazakhstan were underdeveloped before 1990s. This evolution happened because the Soviet government preferred to develop the fields in Siberia (Ostrowski 2010, 30; Yergin 2011, 65). Kazakhstan has been faced with four great challenges in developing its petroleum resources since the 1990s. First, development in the Caspian basin was slowed and hindered by disagreement over delimitation of national territories (Najman et al. 2008, 1). Second, there was the issue of high costs and how to transport all the oil and gas over huge distances to foreign markets. Third, the old pipelines running through Russia were and still are controlled by the Russian state-controlled company, Transneft, which has discriminated against non-Russian oil and by demanding higher prices (Najman et al. 2008, 1, 4). Lastly, much of Kazakhstan's resources are located in northern Caspian Sea offshore and in remote areas in the country inland where there are harsh weather conditions and poorly developed infrastructure and communications. The consequence of these major challenges is that development of Kazakh oil and gas has

been hampered and delayed by relative high costs, long development time and technical difficulties.

To overcome these challenges and to get access to finance and technology, western IOCs were invited to Kazakhstan from the early 1990s to develop the oil and gas resources. Most of the existing oil and gas industry was privatized in the 1990s by selling to foreigners to get foreign investments and technology (Tompson 2011, 46-47). In the 2000s Kazakhstan has moved toward more resource nationalism, in which KazMunaiGaz (KMG) played an important part (Domjan and Stone 2009; Sarsenbayev 2011, 369). Resource nationalism refers to the state taking control over and taking ownership of natural resources in its territory. In 2002, the national oil company (NOC) KMG was founded. The Kazakh state became more directly involved in production and development of the oil and gas resources. KMG has several subsidiaries such as KazTransGaz, KazTransOil and KazMunaiGaz Exploration Production (KMG EP)<sup>10</sup>. Through KazTransOil and KazTransGaz KMG controls a state monopoly on energy transport pipelines except the Caspian Pipeline Consortium (CPC) pipeline. This shift was also marked with new regulations favoring the state and KMG on the expense of IOCs. One of the new regulations from 2002 required that 50 percent of all new strategic oil and gas projects must be owned by Kazakhstan through a Kazakh firm in a joint venture<sup>11</sup> or KMG (Ostrowski 2010, 57; Olcott 2011, 115-116). This means that the state is represented in all new major energy deals and projects since energy companies have to come to agreement with KMG. From 2004 KMG's rights was further increased when KMG was given the right to participate in all oil and gas projects (Kaiser and Pulsipher 2007, 1311). Later in the 2000s the Kazakh government made even more laws and regulations to strengthen the supervision and control of the industry.

Even if Kazakhstan has set the stage for KMG to play a major role in its oil and gas industry, Kazakhstan is still dependent on foreign companies to be able to develop many fields under difficult technical and climatic conditions (Yenikeyeff 2008, 6). However, in the last few years several IOCs have or are in the process of reducing their activity or have withdrawn from Kazakhstan (Washington Post 2013). The reason behind this development is speculated to be loss of business attractiveness in Kazakhstan to IOCs and resource nationalism (Respublika 2013).

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<sup>10</sup> For a full study on KazMunaiGaz see Olcott (2007).

<sup>11</sup> Joint venture is a common contractual agreement between two or more parties to execute a business undertaking together.



### 3.3.2 Importance of Oil and Gas to Kazakhstan

The oil sector dominates the Kazakh economy, by accounting for 25 percent of gross domestic product (GDP), 65 percent of total exports and 40 percent of total budget revenue by 2011 (Cummings 2012, 128). This claim is supported by economic data from the World Bank seen in Table 1. Kazakhstan has experienced substantial economic growth since independence and especially in the 2000s after the economic hardships of the early 1990s (Raballand, Najman, Pomfret and Sourdin 2008, 111-113). Kazakhstan's economy has grown faster than the other Central Asian countries to become the leading economy in the region (Cummings 2012, 128). This growth has been fueled by large foreign investments, mainly in the oil and gas sector, export of oil, high oil prices and export of other natural resources, as seen in Table 1. The oil and gas sector have a great impact on the rest of the economy and on social and economic development, and can be described as the driving force in the Kazakh economy (Ministerstvo nefti i gaza Respubliki Kazakhstan 2011, 3).

**Table 1: Economic Data on Kazakhstan by Year**

Economic variable	Year											
	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
GDP growth (annual %)	9,8	13,5	9,8	9,3	9,6	9,7	10,7	8,9	3,3	1,2	7,3	7,5
Oil rents (% of GDP)	29,6	23,8	25,5	26,1	28,2	31,0	28,3	24,5	28,1	20,8	22,4	-
Total natural resources rents (% of GDP)	37,5	29,3	30,3	33	35,9	41,1	38,4	32,9	36,8	26,4	27,6	-
Foreign direct investment, net inflows (% of GDP)	7,0	12,8	10,5	6,8	9,6	3,5	7,8	10,6	10,7	11,5	7,3	6,9

Source: World Bank (2012).

### 3.3.3 Production and Reserves

In the 1990s there were overly optimistic estimates on the potential resources located both in Kazakhstan and in the Caspian region. The region was presented as a new *El Dorado* (Raballand and Genté 2008, 9). However, the estimates and hopes of oil wealth have in recent years gone down and become more realistic, since it seems that the Caspian does not have the same amount of reserves as the Middle East. Nonetheless, Kazakhstan still has major deposits of oil and, to a lesser degree, gas. The Kashagan field, found in 2000 and one of the most substantial oil discoveries in the last 20 years, shows that Kazakhstan and the Caspian basin have great potential (Cummings 2012, 128).

Kazakhstan has the second largest reserves and the second largest production of oil among the former Soviet republics (EIA 2012). According to BP, Kazakhstan had at the end of 2011 proven oil reserves of 30 billion barrels (bbl), which is up from 5.4 billion bbl at the end of 2001 (BP 2012). In 2011 this amounted for 1.8 percent of the world's total reserves.

Kazakhstan has according to BP (2012) the twelfth largest deposits of oil in the World and the second largest in Europe and the Eurasian region after Russia. Kazakhstan's reserves are relatively smaller regarding natural gas. Proven reserves of natural gas were at the end of 2011 at 1.8 trillion cubic meters (tcm) or 0.9 percent of World's total reserves. This is far behind both their neighbors Russia and Turkmenistan, who have some of the largest gas reserves in the world.

**Table 2: Proven Oil and Gas Reserves and Production in and around the Caspian Region**

Country	Oil reserves, billion bbl	Oil production, million bbl/d	Gas reserves, tcm	Gas production bcm
Azerbaijan	7.0	0.93	1.3	14.8
Kazakhstan	30.0	1.84	1.9	19.3
Russia	88.2	10.28	44.6	607.0
Turkmenistan	0.6	0.21	24.3	59.5
Uzbekistan	0.6	0.08	1.6	57.0

Note: Numbers are from the end of 2011. Numbers on Russia are total. The reserves and production located in the Caspian are just a small portion.

Source: (BP 2012).

Production of both oil and gas has increased steadily since the mid 1990s. Production of oil in 2011 was 1.84 million bbl a day (bbl/d), and is up from 869 000 bbl/d in 2001 and 569 000 bbl/d in 1992 (BP 2012)<sup>12</sup>. Consumption of oil is relatively low in Kazakhstan compared with production. Only 212 000 bbl/d in 2011 of produced oil went to domestic consumption. This means that most of the country's production is exported. Kazakhstan has ambitious goals regarding development and increasing oil production and export. By 2015 the Kazakh oil and gas ministry plans to export 84 million tons of oil, up from 68.1 million tons in 2009 (Ministerstvo nefi i gaza Respubliki Kazakhstan 2011, 21). KMG expects that Kazakhstan's production will rise to 90 million tons of crude oil a year in 2015, and to 130 million tons a

<sup>12</sup> The lowest oil production since independence was in 1994 with 446 000 bbl/d.

year in 2020 (Oil & Gas Journal 2012). This is a large increase from 82.4 million tons of oil produced in 2011, as estimated by BP (2012)<sup>13</sup>.

Kazakhstan produced 19.3 billion cubic meters (bcm) of natural gas in 2011, or only 0.6 percent of World total production (BP 2012). As much as 9.2 bcm was used for domestic consumption in 2011. In the last ten years consumption has been relatively stable, but production has increased from 9.2 bcm in 2001. Kazakhstan has been a net exporter of gas from 2004 (Kaiser and Pulsipher 2007, 1306). It should be noted here that the numbers from BP are different from official numbers. This can be explained by different method of calculation, by taking gas reinjection, flaring, technical use and import-export into account (Yenikeyeff 2008, 41). Even if Kazakhstan produces enough gas for domestic consumption, it relies on imports to its eastern part because of insufficient infrastructure. Importing gas in the east is offset by exporting gas in the western part of the country. An important feature of Kazakhstan's gas is that it is closely connected with oil production. This comes from the fact that most of Kazakhstan's gas is associated gas and condensate produced from the same fields as crude oil (Campaner and Yenikeyeff 2008).

In Kazakhstan's case natural gas is produced and exported to a much lesser degree than oil. However, gas can become more important over time as production rise. Estimates by Shamil Yenikeyeff (2008, 75-76) suggest that production of natural gas can increase strongly by 2015. This is also affirmed by The Kazakh Oil and Gas ministry, which plans to increase the volume of produced gas by 58.6 percent from 2010 to 2015 (Ministerstvo nefiti i gaza Respubliki Kazakhstan 2011, 9). Large investments are needed to achieve this increase in production. The prospects for future exports of gas from Kazakhstan are weakened by the ambitions of the government's policy on gas utilization and gasification of the country, combined with ambitions to increase domestic consumption of gas and build gas pipelines to supply the country (Nazarbaev 2012a; Pirani 2012, 3, 7). Domestic consumption is targeted at 24 bcm a year in 2020, but it is uncertain if this aim will be met (Pirani 2012, 3). To meet production aims for gas there is also a trade-off related to Kazakhstan's associated gas. Since this gas is difficult to separate from oil and to use, the gas can be re-injected to keep up the physical pressure for oil production or it can be sold. If this reinjection is reduced to increase gas production, it may lower oil production (Crandall 2006, 80). This fact combined with Kazakhstan's relatively low reserves of natural gas and government policy suggest that

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<sup>13</sup> Equivalent to 1.84 million bbl/d.

Kazakhstan may not export great amounts of gas in the not so distant future. If Kazakhstan is to become independent in regard to gas supply, but not able to export large amounts, this can make gas less important for Kazakh foreign policy than it is today.

### 3.3.4 Oil and Gas Fields and Projects

The most important part or about 90 percent of Kazakhstan's proven oil reserves are concentrated in 15 large fields: Tengiz, Kashagan, Karachaganak, Uzen, Zhetybai, Zhanazhol, Kalamkas, Kenkiyak, Karazhanbas, Kumkol, North Buzachi, Alibekmola, Prorva Central and East, Kenbai and Royal (Ministerstvo nefi i gaza Respubliki Kazakhstan 2011, 2). Most of the reserves are located in the western part of the country or in the Caspian Sea. According to EIA (2012) about 80 percent of gas reserves are located in the four fields of Kashagan, Tengiz, Karachaganak and Imashevskoe. Below in Tables 3 and 4 is an overview of major oil and gas projects in Kazakhstan.

#### Major Oil and Natural Gas Projects

Table 3: Onshore Projects

Name of field/project	Project Partners	Estimated Reserves	Project Status
<b>Aktobe:</b> <b>Zhanazhol</b> <b>Kenkiyak</b>	-CNPC Aktobemunaigaz - 85 %.  In the block ADA: -KNOC (South Korea) -LGIC -Vertom	1.17 billion barrels of oil (2007).	Produced 116 660 bbl/d of oil, and 69.6 bcf a year of gas (1.948 bcm) in 2005.
<b>Alibekmola and Kozhasai</b>	-KMG – 50 % -Caspian Investments Resources – 50 %	Proven reserves of 102 million barrels of oil (2011).	Produced 1.14 million tons of oil (22 891 bbl/d) in 2011.
<b>Amangeldy</b>	-Amangeldy Gas (KazTransGaz <sup>14</sup> subsidiary)	22-25 bcm of gas (2008).	Produced 0.32 bcm of gas in 2007.
<b>Arman</b>	-Caspian Investments Resources – 50 % -Shell – 50 % <sup>15</sup>	Proven reserves of 2.8 million barrels of oil (2011).	Produced 76 500 tons (1 536 bbl/d) of oil in 2011.
<b>Emba</b>	-KMG – 51 % -MOL Rt. Vegypsyzer (Hungary) – 49 %	500 million barrels of oil (2007).	Produced 57 700 bbl/d of oil in 2004, 3.1 bcf of gas (0.086 bcm) in 2004.

<sup>14</sup>KazTransGaz is a KMG subsidiary.

<sup>15</sup> Shell's share in Arman appears to have been sold to Lukoil in 2012.

<b>Karachaganak</b>	-BG Group (UK) (joint operator) - 29,25 %, -ENI (joint operator) – 29,25 % -Chevron – 18 %, -Lukoil – 13,5 %, -KMG – 10 %	Gross reserves of 2.4 billion barrels of condensate <sup>16</sup> , 16 Tcf of gas (2013).	Producing 202 900 bbl/d, 1.1 mmcf/d natural gas (2005). 244 000 bbl/d of condensate in first half of 2012. 70 % of oil is exported through CPC pipeline.
<b>Karakuduk</b>	Caspian Investments Resources: -Lukoil (Russia) – 50 % -Sinopec (China) – 50 %	Proven reserves of 56.6 million barrels of oil, 22.7 bcf of gas (0.635 bcm) (2011).	Produced 1.4 million tons of oil (28 112 bbl/d) and 120 mcm of gas in 2011.
<b>Karazhanbas</b>	Karazhanbasmunai: -Citic Resources Holdings (China)– 50 % -KMG – 50 %	286 million barrels of oil (2011).	Produced 36 200 bbl/d in 2011.
<b>Kazgermunai</b>	-KMG – 50 % -PetroKazakhstan <sup>17</sup> (China) – 50 %	100 million barrels of oil (2007).	Produced 3.0 million tons of oil (60 240 bbl/d) in 2011.
<b>Kumkol North</b>	Turgai Petroleum: -Lukoil - 50 % -PetroKazakhstan – 50 %	Proved reserves of 86 million barrels of oil, 29.7 bcf of gas (0.83 bcm) (2011).	Producing 2.5 million tons of oil (50 200 bbl/d) in 2011.
<b>Kumkol South</b>	-PetroKazakhstan (China)	116 million barrels of oil (2007).	Produced 3.2 million tons of oil (64 257 bbl/d) in 2011.
<b>Mangistau</b>	Mangistaumunaigaz: -KMG – 50 % -CNPC – 50 %	1.4 billion barrels of oil (2007).	Produced 117 000 bbl/d of oil from Jan- June 2012, and 33.3 mmcf/d of gas in 2005.
<b>North Buzachi</b>	-CNPC- 50 % -Caspian Investments Resources (Russia/China) – 50 %	Proved reserves of 134 million barrels of oil (2011).	Produced 1.97 million tons of oil (39 558 bbl/d) in 2011.
<b>Tengiz</b>	TengizChevroil: -Chevron (US) – 50 % -ExxonMobil (US) – 25 % -KMG – 20 % -LukArco <sup>18</sup> (Russia) – 5 %	6-9 billion barrels of oil (2013).	Produced 25.8 mill tons of oil (579 000 bbl/d), 1.3 million tons of LPG and 6.9 bcm in 2011. The majority of oil is exported through CPC.
<b>Uzen</b>	Uzenmunaigaz (KMG subsidiary) – 100 %	Proved and probable reserves of 166 million tons of oil (1.2 billion barrels) (2011).	Produced 5.1 million tons of oil (102 409 bbl/d) in 2011.

Note: Some of the projects include multiple fields. The table is as of 31. December 2012. Numbers in brackets are converted to with BP's conversion factors (BP 2013b).

Modified from the following sources: (Olcott 2007; Yenikeyeff 2008, 32, 78-80; Ekspert Kazakhstan 2010; CITIC Resources Holdings 2011; KazMunaiGaz 2011a; KazMunaiGaz 2011c; EIA 2012; Lukoil 2012; PetroKazakhstan 2012a; PetroKazakhstan 2012b; BG Group 2013; CNPC 2013; KMG EP 2013; KPO 2013; Lukoil 2013; TCO 2013).

<sup>16</sup> Is a mixture of liquid hydrocarbons.

<sup>17</sup> PetroKazakhstan is owned by KMG (33 %) and CNPC (67 %), see (PetroKazakhstan 2012).

<sup>18</sup> LukArco is a subsidiary of the Russian company Lukoil.

**Table 4: Caspian Sea Projects**

Name of field/project	Project Partners	Estimated Reserves	Project Status
<b>Kashagan:</b> <b>Kashagan E</b> <b>Kashagan W</b> <b>Kairan</b> <b>Aktoty</b> <b>Kalamkas</b>	North Caspian Operating Company (NCOC): ENI (Italy) – 16.81 % KMG – 16.81 % Total (France) – 16.81 % Shell (UK/Nederland) – 16.81 % ExxonMobil (US) – 16.81 % ConocoPhillips (US) – 8.40 % <sup>19</sup> Inpex (Japan) – 7.56 %	9 to 13 billion bbl of oil recoverable (2007).	PSA. <sup>20</sup> Production is estimated to start in the first half of 2013. Initial production of 75 000 bbl/d, and max of 1.2 million bbl/d.
<b>Kurmangazy</b>	KMG – 50 % Rosneft (Russia) – 50 %	550 to 1800 million tons of oil recoverable (4 to 13 billion barrels) (2013).	PSA. Exploration.
<b>Tyub-Karagan</b>	KMG – 50 % Lukoil (Russia) – 50 %	N/A	PSA. Exploration. Lukoil financing 100 % of the exploration.
<b>Atash</b>	KMG – 50 % Lukoil (Russia) – 50 %	N/A	Exploration contract. Exploration. Lukoil financing 100 % of the exploration.
<b>Zhemchuzhiny (“Pearls Block”)</b>	Shell (UK and Nederland) – 55 % KMG – 25 % Oman Oil Company (Oman) – 20 %	N/A	PSA. Exploration. Shell and Oman Oil Company financing 100 % of the exploration.
<b>Makhambet</b>	Ayraumunaigaz. (KMG subsidiary)	N/A	PSA. Exploration.
<b>Bobek</b>	Ayraumunaigaz. (KMG subsidiary)	N/A	PSA.
<b>Imashevskoe</b>	-KMG -Gazprom (Russia)	Over 100 bcm of gas (2011).	Joint Russian-Kazakh agreement on exploration.
<b>Khvalynskoe</b>	-Lukoil – 50 % -KMG - 25 % -Total (France) – 17 % -GDF Suez (France) – 8 %	N/A	Negotiations. Russia’s jurisdiction.
<b>Tsentralnoe</b>	-KMG – 50 % -TsentrCaspNeftegas (Gazprom/Lukoil) – 50 %	N/A	Negotiations. Russia’s jurisdiction.
<b>Abai</b>	-KMG -Statoil (Norway) <sup>21</sup>	N/A	Negotiations.
<b>Isatai</b>	-KMG -ENI (Italy)	N/A	Negotiations.
<b>Darkhan</b>	-KMG -Chinese consortium headed by CNOOC.	N/A	Negotiations.

<sup>19</sup> ConocoPhillips is in a process to sell its share by 2013.

<sup>20</sup> A PSA or production sharing agreement is a common contract between a government and energy companies on how to share revenue from the resources.

<sup>21</sup> Statoil have withdrawn from the project in 2013, see Trend (2013).

<b>N-block</b>	-KMG – 51 % -ConocoPhillips (US) – 24.5 % <sup>22</sup> - Mubadala Development Company (UAE) – 24.5 %	270 million tons of oil (1.98 billion barrels) (2013).	PSA. Exploration.
<b>Satpayev</b>	-KMG – 75 % -ONGC (India) – 25 %	N/A	Exploration and production contract.
<b>Zhambai South</b> – <b>Zaburunie South</b>	-KMG – 50 % -Repsol (Spain) – 25 % -Caspian Investments Resources <sup>23</sup> (Russia/China) – 25 %	N/A	PSA. Exploration.
<b>Zhambyl</b>	-KMG -Korean consortium lead by KNOC.	N/A	Negotiations.

Note: Updated as of 31. December 2012. Some projects include several fields. Numbers in brackets are converted to with BP's conversion factors (BP 2013b).

Modified from the following sources: (Olcott 2007; Oil & Gas Journal 2009a; Ekspert Kazakhstan 2010; KazMunaiGaz 2011a; KazMunaiGaz 2011c; Tengri News 2011; EIA 2012; Kazenergy 2013; Lukoil 2013; Tengri News 2013d; Washington Post 2013).

### 3.3.5 Pipelines, Transportation and Export of Energy

The lack of access to the sea and huge transit distances are important differences between Kazakhstan and other petroleum producers and exporters. Kazakhstan is reliant on pipelines to export large volumes of oil and gas because of its landlocked position. Exporting through pipelines requires large investments and long term planning. This is because pipelines cannot be moved after they are built and operational. After independence in the 1990s pipelines for export of oil all transited through Russia. The policy of Kazakhstan has since been to diversify export routes. The country has made progress in this regard in the 2000s with the new pipeline to China, oil swaps with Iran and export with tankers through Azerbaijan. Still most of Kazakhstan's oil is exported through Russian territory. In 2010 the share was estimated to around 75 percent (Jarosiewicz 2010). As of 2010 the export capacity is estimated to a little over 1.5 million bbl/d, while the export volume in 2009 was around 1.3 million bbl/d and about 1.4 million bbl/d in 2011 (International Energy Agency 2010, 512; EIA 2012). Kazakhstan needs to increase its export capacity because of the large planned increase in oil and gas production. When the Caspian Pipeline Consortium (CPC) pipeline became operational in 2001 Kazakhstan's ability to export oil was increased. Since this pipeline is going through Russia it does not weaken the dependence on Russia. However,

<sup>22</sup> ConocoPhillips sold its share in 2013 to KMG.

<sup>23</sup> Caspian Investments Resources is owned by Lukoil (50 %) and Sinopec (50 %), after the Chinese company acquired their share from Mittal Investments in 2010 (Ekspert Kazakhstan 2010).

because this pipeline is private owned, it is more difficult for Russia to use CPC to pressure Kazakhstan than the other pipelines owned by the state company Transneft. Even so, Transneft has a significant share in CPC. In addition to the pipelines and the current export capacity available, there is several new transport projects proposed and planned expansions of the existing pipelines such as CPC and the Kazakh-China oil pipeline. The process of building CPC in the 1990s, and negotiations regarding expansion until 2008, have been delayed by Transneft and Russia for several years (Dellecker 2008; Olcott 2010, 260).

Most of Kazakhstan's oil is exported through three main pipelines (see Table 5), where the largest part goes through the Russian pipelines. Oil is also exported by tanker from the maritime terminal at Aktau to Makhachkala in Russia, Baku in Azerbaijan and Neka in Iran. In 2011, the sea export was 9.3 million tons of oil (KazMunaiGaz 2012). Iran and Kazakhstan conducts oil swaps. This means that Kazakh oil is exported to northern Iran, where Iran consumes it, then Iran export an equivalent oil amount from the Persian Gulf to the World market for Kazakhstan. To fulfill their obligations to export oil through the BTC pipeline from their agreement with Azerbaijan in 2006, Kazakhstan is developing the Kazakhstan Caspian Transportation System (KCTS) to increase export through Baku by making a link across the Caspian Sea (Socor 2006; KazMunaiGaz 2011b). This system includes pipelines, increased terminal capacity in Kuryk and tanker capacity. This system has been put on hold until 2018 at least because of insufficient oil production resulting from the delays developing Kashagan (Central Asia Newswire 2010). When oil is exported to Baku, it can be exported to the world market by pipeline or rail to Batumi in Georgia, in addition to the BTC pipeline. Kazakh oil from Tengiz was exported through BTC in 2008 and 2009, but was stopped in 2010 because of disagreement on tariff (Trend 2011). In 2009, France and Kazakhstan agreed to develop a trans-Caspian oil pipeline, so that Kazakh oil can link up with the BTC pipeline (Oil & Gas Journal 2009a) In addition, some oil is exported by rail to Russia and China. In 2010, exports by rail amounted to 6 million tons of oil (Ministerstvo nefti i gaza Respubliki Kazakhstan 2011, 7).



**Table 5: Oil Export Pipelines**

Pipeline	Ownership	Length/Capacity	Notes
<b>CPC pipeline: (Tengiz-Novorossiisk pipeline)</b>	Caspian Pipeline Consortium (CPC): -Russia/Transneft – 31 % <sup>24</sup> -KMG – 19 % -Chevron (US) – 15 % -LUKARCO B.V. (Russia) – 12.5 % -ExxonMobil (US) – 7.5 % -Rosneft-Shell (Russia/UK/Nederland) – 7.5 % -BG Group (UK)– 2 % -ENI (Italy)– 2 % -Kazakhstan Pipeline Ventures (Kazakh)– 1.75 % <sup>25</sup> -Oryx – 1.75 %	1511 km from Tengiz field to the port of Novorossiisk in Russia, Black Sea. Phase I capacity of 565 000 bbl/d; Phase II capacity of 1.3 million bbl/d (2015).	First tanker loaded in 2001. Transported about 670 000 bbl/d in 2012.
<b>UAS pipeline (Atyrau, Samara; Connecting With Russian pipeline system)</b>	KazTransOil (KMG Subsidiary) – 100 % on Kazakh side of the border	From Uzen via Atyrau to Samara in Russia and linking up with the Russian pipeline system. Capacity of about 300 000 bbl/d.	Old pipeline built in 1970s. Upgraded in 2002 to about 300 000 bbl/d, and are in discussions to expand further. Transported 15.4 million tons (309 000 bbl/d) of oil in 2011.
<b>China pipeline (Atasu-Alashankou or KCP)</b>	KMG/KazTransOil - 50 % CNPC (China) - 50 %	Initially 7 million tons of oil, then upgraded to 10 million from 2008. From 2011, a capacity of 12 million tons a year (240 000 bbl/d).	First oil reached China in 2006. Plan to expand capacity to 20 million tons a year (400 000 bbl/d) in 2013.
<b>BTC (Baku-Tbilisi-Ceyhan pipeline)</b>	The Baku-Tbilisi-Ceyhan Pipeline Company: BP (UK) – 30.1 % SOCAR (Azerbaijan) – 25 % Chevron – 8.9 % Statoil (Norway)– 8.7 % TAPO (Turkey) – 6.5 % ENI – 5 % Total (France) – 5 % Itochu (Japan) – 3.4 % Inpex (Japan) – 2.5 % ConocoPhillips – 2.5 % Hess Corp. (US) - 2.4 %	1768 km long route from Baku in Azerbaijan via Georgia to the Turkish Mediterranean port Ceyhan. Capacity of 1 million bbl/d.	First shipment of oil in 2006 from Ceyhan. Exported 1.9 million tons of Kazakh oil from Tengiz in 2009, but stopped in 2010 over disagreement on tariff.

Note: Numbers in brackets are converted to with BP's conversion factors (BP 2013b).

Sources: (Olcott 2007; Upstream 2008; Babali 2009; International Energy Agency 2010; Trend 2011; EIA 2012; KazMunaiGaz 2012; BP 2013a; CPC 2013a; KazTransOil 2013a).

<sup>24</sup> Transneft bought Oman's share in 2008 (Upstream 2008).

<sup>25</sup> KMG own 49.9 % after buying BP's share in 2009 (BP 2009).

Map 2: Proposed and Existing Oil Pipelines



Source: [http://www.eia.gov/countries/analysisbriefs/China/images/oil\\_map.png](http://www.eia.gov/countries/analysisbriefs/China/images/oil_map.png)

## Gas Pipelines

Kazakhstan has four main gas pipelines: the Central Asia Center pipeline, the Bukhara – Ural pipeline, Bukhara-Tashkent-Bishkek-Almaty pipeline and the Turkmenistan-China pipeline (EIA 2012). The pipeline system is operated and control by KazTransGaz, which is a KMG subsidiary. However, this infrastructure is not interlinked, a legacy from Soviet times. Producing regions in the west have not been connected with the major population and industry centers in the east and south.

Kazakhstan has to import gas from Russia and Uzbekistan to satisfy demand in the eastern part of the country because of a lack of pipelines connecting the western and eastern parts of the country (Pirani 2012, 8, 72-73). Kazakhstan is an important transit country for gas from Turkmenistan and Uzbekistan to Russia and China. The total export of gas in 2009 was only 7.0 bcm, while the amount of gas transited through Kazakhstan was 73.3 bcm (Ministerstvo nefti i gaza Respubliki Kazakhstan 2010, 14). It is fair to state that Kazakhstan is much more important as a transit country than as an exporter of gas.

**Table 6: Main Gas Pipelines**

Pipeline	Direction/Capacity	Notes
<b>Central Asia Centre (CAC)</b>	The eastern part origins from southeastern Turkmenistan (2.2 tcf), western part from Turkmen Caspian coast (120 bcf). They link up at Beineu in Kazakhstan and go to Alexandrov Gai in Russia.	Two branches controlled by Gazprom. Exports gas from Central Asia to the Russian gas system.
<b>Bukhara – Ural</b>	Uzbekistan via Kazakhstan to Russia. Capacity of 706 bcf.	Transit pipeline through Kazakhstan.
<b>Bukhara Gas Region- Tashkent-Bishkek-Almaty (BGR-TBA)</b>	From the Bukhara area in Uzbekistan to Kazakhstan with a link to Kirgizstan. Capacity of 160 bcf.	Supply southern Kazakhstan with gas.
<b>Kazakhstan-China (also known as Turkmenistan-China gas pipeline)</b>	From Turkmenistan, along BGR-TBA to Almaty and China. Export capacity of 30 bcm to China, 10 bcm for domestic use.	First line commissioned in 2009. Supply China with Turkmen gas, and can supply China with Kazakh. Expansion is planned. Section two, Beineu-Shymkent is expected finished in 2015, with a capacity of 10 bcm. Development financed by China.

Sources: (Yenikeyeff 2008, 33-36; KazMunaiGaz 2011e; EIA 2012; Pirani 2012; KazTransGaz 2013b; KazTransGaz 2013a).

Kazakhstan has been working on modernizing the pipeline system and expanding it with more pipelines to more effectively supply the country with gas. This development could remove the need to import gas from Uzbekistan in the future (EIA 2012). Central to this development is the building of the Beineu-Shymkent gas pipeline, which will connect to the Turkmenistan-China pipeline and will supply southern Kazakhstan with gas. This pipeline has been supported by China, and the project started in 2011. The project, a joint effort between Kazakhstan and China, is financed on a 50/50 basis with \$500 million each (KazTransGaz 2013b). This pipeline also opens for export of gas from western Kazakhstan to China. In 2007, Russia, Kazakhstan and Turkmenistan agreed to build a new gas pipeline (KazMunaiGaz 2011e). It would be built onshore going from Turkmenistan to Russia. This pipeline allows for export of Turkmen and Kazakh gas to Russia. This new gas pipeline to Russia has however been postponed (Reuters 2010). Regarding the Kazakhstan-China gas pipeline, China has financed the construction of the Kazakh section by giving a loan of \$7.5 billion (KazTransGaz 2013a). These developments in gas pipelines are discussed more in Chapter Five.

### 3.3.6 Refineries

Kazakhstan currently has three major oil refineries: Atyrau, Pavlodar and Shymkent. These refineries are from the Soviet era, and are being upgraded and modernized until 2014 (KazMunaiGaz 2011d). These refineries supply most of Kazakhstan's domestic fuel (Olcott 2007, 18). Most of Kazakhstan's oil and gas production facilities are located far away from these refineries, which can be problematic for Kazakhstan. The Pavlodar refinery, in the eastern part of the country, receives oil supplies from Russia, while Kazakh oil is being exported in the western part. The refinery still depends on the old soviet pipeline system for supplies, since the pipeline infrastructure is not fully developed. This fact of being dependent on Russian supplies can be seen as a risk, which the Kazakh government recognizes (Ministerstvo nefti i gaza Respubliki Kazakhstan 2011, 8). In addition, the Karachaganak field, close to the Russian border, is dependent on the Russian refinery in Orenburg for processing and to keep up production (Gazeta.kz 2001). Kazakhstan is planning to build a refinery to handle production from the Karachaganak field, as a response to this situation (Bloomberg 2012; Nazarbaev 2012a).

# 4 Kazakhstan's Foreign Policy in Practice— the Multi-vector Policy

## 4.1 Introduction

This chapter provides a presentation and discussion of the background of Kazakhstan's foreign policy, and how its multi-vector foreign policy has been carried out. After a presentation and theoretical framework of the policy in Chapter Two, it is necessary to explore the multi-vector foreign policy in practice and in more depth. First, a presentation is provided of the background of Kazakhstan's foreign policy with reference to geography, landlocked status and demography. The purpose is to understand the context and the background of the multi-vector foreign policy as well as its constraints, possibilities and limits. Furthermore, the Soviet heritage influence on Kazakhstan in foreign policy terms is taken into account. Second, Kazakhstan's multi-vector foreign policy is discussed. This policy can be said to be an answer to Kazakhstan's situation and interests. Topics of the policy reviewed here are balancing, aims of the policy, international organizations, security cooperation, the Caspian Sea and its development over time. Lastly, the multi-vector policy in practice is discussed with weight on Kazakhstan's relations with its main partners: United States, Russia and China. The relation to the energy resources is touched upon, but is explored more in Chapter Five.

## 4.2 Background of Kazakhstan's Foreign Policy

Kazakhstan and President Nursultan Nazarbaev was hesitant to declare independence from the Soviet Union, and was the last of the republics to leave the union on December 16<sup>th</sup> 1991 (Olcott 1996, 4). This reluctance to be independent is understandable when seen in light of the unique, but also vulnerable foreign policy situation of Kazakhstan at that time. Kazakhstan's foreign policy situation is less vulnerable in 2012 than it was in early 1990s.

Kazakhstan is geographically situated in Central Asia, and borders Russia, China, Uzbekistan, Kyrgyzstan and Turkmenistan. It also has access to the Caspian Sea. The country's large land mass makes it the ninth largest country in the world with borders over 12 000 km long (Agentstvo Respubliki Kazakhstan po statistike 2012, 4). These borders date back to the

Soviet Constitution of 1936, and were generally accepted after the breakup of Soviet Union (Sorbello 2011, 34). Kazakhstan has since its independence signed several border treaties with its neighbors to clarify their borders and settle disputes (Golunov and McDermott 2005). Kazakhstan has had a dispute with China regarding their common border, but the parties came to a final agreement in 1998 after previous agreements in 1994 and 1997 (Guangcheng 2003, 118). With only 16.67 million inhabitants, the country is sparsely populated and mostly wilderness. This means that Kazakhstan has a security problem of how to effectively control, protect and supervise its long land borders. The border with Russia is the longest continuous international land border in the world. It has no natural boundaries. Kazakhstan and Russia's long open border means that both countries are tied to one another from the point of view of security (Torjesen 2009, 8). Kazakhstan's security cannot be defended by military means against its powerful neighbors, Russia and China, so it has to rely on building alliances, political relations and economic interaction (Kasenov 1995, 263-264). By sharing a border with the great powers Russia and China, Kazakhstan needs to take their interests into account when conducting foreign policy.

A central feature of Kazakhstan's geography and foreign political landscape is that the country is landlocked. This can have a major constraint on a country's foreign policy options (Idan and Shaffer 2011, 263-264). This means that Kazakhstan's trade, import and export has to transit a least one of its neighboring countries for the goods reach the world market. In foreign policy terms this situation demands that Kazakhstan needs to keep good relations with its neighbors to keep the borders open to trade, especially to be able to export its oil and gas through transit pipelines.

The demographic composition of the country makes the situation more complicated. The census from 2009 claims that Kazakhs are a majority with 63.1 percent and the Russian minority constitutes about 23.7 percent (The Agency on Statistics of the Republic of Kazakhstan 2011, 20). The Russian minority is concentrated in northern Kazakhstan by the Russian border and in major cities. Just after independence the Kazakh elite feared that this Russian minority would secede and join the Russian Federation. The Russian state's assumed role as protector of Russians living in the former Soviet Union makes this situation even more problematic for Kazakhstan (Olcott 1996, 58). The fear of secession is probably lower today than in the early 1990s, but the threat still remains. This demographic situation requires the

government of Kazakhstan to keep these two large ethnic groups content, and to keep good relations with Russia to ensure the country's unity.

The heritage from the time of the Soviet Union ties Kazakhstan to Russia and its neighbors in Central Asia, such as Turkmenistan, Kyrgyzstan, Tajikistan and Uzbekistan. Kazakhstan has a shared history and common use of the Russian language with these countries, which make up a cultural connection between them. Kazakhstan also inherited infrastructure, nuclear weapons, pipelines, military facilities, economic interdependency with Russia and the Baikonur Cosmodrome. These large investments, weapons and structures built in the Soviet era could both be assets or liabilities for foreign policy. Kazakhstan chose to dismantle their nuclear arsenal in the 1990s after talks with the United States and Russia, which will be discussed more below (Olcott 1996, 70-71). Baikonur Cosmodrome represents a special case for Kazakhstan foreign policy since both Kazakhstan and Russia claimed ownership to the site in the early 1990s (Olcott 1996, 71-73). Russia is therefore currently dependent on working with Kazakhstan to effectively run its space program. The lease agreement from 1994 was extended to 2050 in 2004 (RIA Novosti 2010a). This arrangement is important for Russia since Baikonur is the main site it can use for space launch until the Vostochny Cosmodrome is fully operational from 2020 (Vzgliad Delovaia Gazeta 2012).

Transport infrastructure with railways and pipelines was in the Soviet time built in the north-south direction with goods traveling between the Central Asian republics and Russia. The infrastructure was built to connect the republics, not necessarily to connect various parts of Kazakhstan with each other. Kazakhstan has connecting links with Russia in the west and east of the country, but the infrastructure going west to east inside Kazakhstan was and still is poorly developed. Kazakhstan therefore has to import energy in the east and export it in the west. Export routes for Kazakh goods and products transit Russia, to a large extent. Sharing infrastructure contributes to Russia and Kazakhstan's interdependent relationship.

The interdependent economic relationship with Russia was strong just after the fall of the Soviet Union. According to Olcott (1996, 65), Kazakhstan sent "about 70 percent of its industrial production and mined products to Russia, as well as just over one-fourth of its agricultural production." In return, Kazakhstan received other raw materials, equipment and manufactured goods. Northern Kazakhstan was fully dependent on Russia for oil and electricity (Olcott 2005, 31). Since the early 1990s this interdependence has been reduced, but Russia is still among Kazakhstan's main trade partners together with China and the European

Union (Coronel, Rozhkov and Al-Eyd 2010, 19). Even if Russia's share of Kazakhstan's exports has declined drastically since the demise of the Soviet Union, Russia is still a key transit country for exports because of the existing infrastructure. One example is the export of oil through pipelines crossing Russia.

As can be seen the background of Kazakhstan's foreign policy influencing and limits the policy today and has done it for the last 20 years. Now the multi-vector foreign policy will be discussed in light of the foreign policy situation described above.

## **4.3 Topics of the Multi-vector Foreign Policy**

### **4.3.1 Balancing and Aims of the Policy**

Kazakhstan can be seen as an example of a relatively small state between the comparably larger neighbors Russia and China, and functioning as a classic buffer state. To keep its autonomy Kazakhstan needs to balance China and Russia to hinder being dominated, in accordance with Daniel Nexon (2009). For Kazakhstan good relations with the United States and states in the European Union, are important to balance Russian and Chinese influence to achieve autonomy. China, the United States and Russia were selected as vital partners, which reflect that these states were more important than others to Kazakhstan. This approach was again made clear and reaffirmed in President Nazarbaev's *Kazakhstan 2030* statement (Nazarbaev 1997). Since independence Kazakhstan has developed relations with these powers, so that each power has interest in Kazakhstan, but no actor dominates. Kazakhstan's middle ground in foreign policy relates to its orientation as Eurasian, neither East or West, but as a bridge between them (Cummings 2003a, 140-141). The balancing middle ground component of Kazakhstan's multi-vector policy works in close relation to its pragmatism as they are strengthening each other by being complimentary.

Kazakhstan has since independence worked for a differentiation of export routes to make Kazakhstan less dependent on Russian pipelines for export to the world market (Hanks 2009, 264). This goal has been repeated by President Nazarbaev and ministers over the years. It has been an important priority. This is related to Kazakhstan's aim to bring in as many partners as possible to invest in Kazakhstan and to develop oil and gas resources. Several scholars see the differentiation of export routes with multiple pipelines as an important driver for the multi-



vector policy (Cummings 2005, 3; Hanks 2009, 264). The quest for multiple export routes can be a driver by pushing Kazakhstan to develop relations in multiple directions to secure long term commitments to the development of transit pipelines. However, this implies that the development of energy resources and its export is a key state interest. Whether this is a goal or a driver for the multi-vector policy will be explored in more depth in Chapter Five. State security, sovereignty, and economic development and economic interest can be seen as the main goals of the multi-vector policy (Mansurov 1997; Hanks 2009, 260). These goals are linked with aims to attract foreign investment and equalize the influence of foreign actors (Sultanov and Muzaparova 2003, 187). This means that multi-vector has a political and an economic dimension. The issue of export routes relates to these main goals and aims. Politically it can be a threat to national security to be dependent on Russia for export of energy, due to fear that Russian will use of the energy weapon. Kazakhstan has come a long way toward these goals since independence, by having a more robust economy and less fragile foreign policy position than in the 1990s. Now a discussion is provided of the main developments from 1992 in relation to Kazakhstan's multi-vector foreign policy.

Since the early 1990s Kazakhstan's multi-vector policy has been influenced by issues relating to its foreign policy situation and background. Kazakhstan's economic dependence on Russia and its pipelines for oil export pushed Kazakhstan to try to weaken Russia's leverage over its economy and their shared infrastructure. However, Kazakhstan could not break the ties with Russia because of their interdependent relationship. This meant that good relations with Russia had to be developed. The large Russian minority and security issues such as the long common border and infrastructure meant that Kazakhstan needed to cooperate with Russia to gain autonomy. Russia could easily extract concessions in this favorable position if it wanted to (Olcott 2002, 43). According to Olcott (1996, 63), President Nazarbaev's goal in Kazakhstan's relation with Russia has been to achieve integration without subordination of sovereignty. Olcott's view appears to be a fair assessment. This is an example of Kazakhstan's balancing pragmatism in its multi-vector policy and shows the importance of Russia as presented by Cummings (2003a).

The fact that Kazakhstan inherited nuclear weapons after the fall of the Soviet Union, gave Kazakhstan an opportunity to gain an ally and support from United States and to balance against Russian influence. Kazakhstan started to negotiate the dismantlement of its nuclear arsenal shortly after independence (Olcott 2002, 44). Instead of asking Russia for help to

dismantle the weapons, Kazakhstan turned to the superpower, the United States. In 1995, all nuclear weapons had been dismantled or returned to Russia (Olcott 1996, 70-71). Kazakhstan also signed the Nuclear Non-Proliferation Treaty. As a consequence Kazakhstan's security situation became improved as Russia was assured that Kazakh nuclear weapons were no threat. It also brought the United States into Kazakhstan as a partner. The United States filled a power vacuum, since Russia was weaker economically and had to partly withdraw from Central Asia in the 1990s. The relationship and support of US was also deepened by American companies investing in Kazakhstan, such as the IOC Chevron who signed a final development contract in 1993 on the oil field Tengiz (Olcott 2002, 145-146). American companies were joined by European, Asian and Middle eastern companies to fuel foreign investments, so that Kazakhstan attracted more foreign direct investments per capita than other post-Soviet states (Olcott 2002, 129). This development increased economic development and secured that more and more countries gained stakes and interests in Kazakhstan, in accordance with the multi-vector policy. This point will be explored more in Chapter Five in relation to IOCs and energy resources in Kazakhstan.

### **4.3.2 International Organizations**

The multi-vectorism is also reflected through the willingness of Kazakhstan to join and participate in international organizations and international relationships. According to Olcott (2007, 54), Kazakhstan has sought membership in virtually every European and Asian multilateral organization which was open to membership for Kazakhstan. These organizations are led by different foreign powers who may be opposing each other and have contradicting orientation, such as the United States, China and Russia (Idan and Shaffer 2011, 250). By doing this Kazakhstan balances different interests and receives international recognition and legitimization. Kazakhstan has worked for closer integration among the former Soviet republics and in Central Asia, such as the Eurasian Economic Community created in 2000, the Customs Union together with Russia and Belarus and Nazarbaev's efforts to found and to strengthen the Commonwealth of Independent States (Olcott 2002, 36-42; Cummings 2003a, 43; Idan and Shaffer 2011, 251). This can be seen in light of Kazakhstan's reluctance to declare independence from the Soviet Union and the strategy of working closely with many partners, especially those states of the former Soviet Union. One of the highest profiled events relating to international organizations was when Kazakhstan succeeded in being awarded the chairmanship of the Organization for Security and Co-operation in Europe (OSCE) for 2010.

Kazakhstan gained a diplomatic victory on this issue by being the first former Soviet republic to lead the multinational organization (RFE/RL 2007; Eurasianet 2011). The OSCE chairmanship was relatively successful for Kazakhstan. However, it is questionable if Kazakhstan gained much politically from focusing resources and goodwill on this chairmanship other than national prestige (Hanks 2009, 267). Still, it provided a diplomatic learning experience for the government.

### **4.3.3 Security Cooperation**

Kazakhstan's multi-vectorism can be seen in the country's security co-operation with others. Kazakhstan was one of the founders of the Shanghai Cooperation Organization (SCO) (Hanks 2009, 260). The SCO provides a forum for cooperation with Russia and China on security issues. Kazakhstan joined the Collective Security Treaty Organization (CSTO) in 2002 (Oliker 2007, 67). CSTO is a military alliance of former Soviet States with Russia as the strongest member Russia has been and continues to be Kazakhstan's closest partner in security cooperation (McDermott 2009, V). Kazakhstan buys and uses Russian military hardware for its armed forces. This gives Russia opportunity to pressure politically, and help to keep the two countries close in security issues (Sharip 2009). As a sign of this close security relationship is the fact that Russia and Kazakhstan has cooperated with joint exercises since the early 1990s (Laruelle 2010, 165). In contrast to the relationship with Russia and China, Kazakhstan is involved with NATO through the Partnership for Peace program. Kazakhstan has also conducted joint exercises with the United States, with a sharp increase since 2002 and 50 military events in 2005 alone (Hanks 2009, 260). This relates to the United States' increased military interest in Central Asia after 2001 and the war in Afghanistan. Kazakhstan followed up this relationship with the United States by sending a small unit of non-combat troops to operate in Iraq until their withdrawal in 2008 (Daly 2008). Just after the war in Afghanistan started in 2001 Kazakhstan offered the right of overflight to the United States and did so again in 2010 (Oliker 2007, 67; Washington Post 2010). According to Cummings (2003a, 152), when Russia, the United States and France all had different position regarding the war in Iraq in 2003, all three of them saw Kazakhstan as an ally to their own position. This situation was quite remarkable considering the heated discussions in the United Nations Security Council prior to invasion lead by the United States. This example is a clear sign of Kazakhstan's pragmatic and balancing multi-vector policy to make good relations with everyone. It also appears to have been successful in this case.

### **4.3.4 The Caspian Sea**

The Caspian Sea represents both a challenge and an opportunity for Kazakhstan's foreign policy. The Caspian Sea is the largest landlocked body of water in the world, and holds major deposits of oil and gas (Sorbello 2011, 37). The littoral states of Kazakhstan, Russia, Azerbaijan, Turkmenistan and Iran however have not agreed on a legal common agreement on borders, national territory and natural resources regarding the Caspian Sea (Sorbello 2011, 37-38, 48-51). The states quarreled over the delimitation issue after the breakup of the Soviet Union, and seemed not to come to an agreement. In 1998, Russia and Kazakhstan signed a bilateral agreement dividing what they consider as "their part" of the Caspian Sea. This agreement is based on the median line concept. In 2002, Putin and Nazarbaev followed up with an agreement on joint development and determination of jurisdiction of the border fields Kurmangazy, Tsentralnoe and Khvalynskoe in offshore Caspian (Kazakhstanskaia Pravda 2002). Azerbaijan came to an agreement with Kazakhstan dividing the Caspian Sea into their national sectors in 2001 and 2003 (Trend 2012). In 2003, Kazakhstan, Russia and Azerbaijan signed a joint agreement for adjacent sectors in the Caspian Sea. Even if the legal status is still not settled regarding the Caspian Sea, it is now divided into de facto national sectors (Olcott 2011, 117). This development is a consequence of the agreements between Kazakhstan, Azerbaijan and Russia. Iran has opposed these agreements. It would probably not have been possible for Kazakhstan to develop its oil and gas resources in the Caspian Sea without an agreement with Russia. For Kazakhstan it was very important to gain access to develop their offshore oil and gas resources in the Caspian Sea, such as the huge Kashagan field. Kazakhstan was therefore willing to make some concessions to Russia. For example, giving Russia full jurisdiction over the oil and gas fields Khvalynskoe and Tsentralnoe, to get an agreement signed. This act from Kazakhstan can be seen in the light of constraints by being landlocked and dependent on Russian goodwill (Idan and Shaffer 2011, 263-264).

## **4.4 Multi-vector and the Great Powers**

After 2000, several important developments influenced Kazakhstan's foreign policy and its relationships with the major powers. The war in Afghanistan made the United States more interested in the region as a whole regarding security, but Kazakhstan took a back seat regarding security because of its distance to the conflict, with the United States' bases in Uzbekistan and Kyrgyzstan (Olcott 2005, 1-2, 182-183). From the other perspective, the

United States was still interested in Kazakh energy resources as an alternative source of oil to the Middle East and its problematic political situation with Islamic extremism. From the 1990s United States' interests in terms of energy in relation to Kazakhstan can be termed as enhancing energy security (Legvold 2003b, 83-84). This meant that the Clinton administration wanted to promote multiple pipelines from the Caspian region, reduce dependency of Russia, cooperate regionally and achieve economic development by energy exports (Legvold 2003b, 84). When President George W. Bush became president in 2001 there was little change to this, but energy issues came second to security after September 11, 2001 (Legvold 2003b, 87-88). The United States has supported efforts to get oil from the Caspian Sea to the world markets by promoting the BTC and the CPC pipeline. When Kazakhstan agreed to support the BTC pipeline, in contrast to Russian opposition, it showed that Kazakhstan are committed to the multi-vector approach and can confront Russian energy interests (Torjesen 2009, 7). When other Central Asian states became more important to the United States after 2001, with Kazakhstan-US relations more distanced, Kazakhstan turned more toward Russia and China (Sultanov and Muzaparova 2003, 188; Cummings 2005, 3, 35). This process might have been accelerated by Kazakhstan becoming more nervous about American pressure for political reforms after the "color revolutions" in Georgia 2003, Ukraine in 2004 and Kyrgyzstan in 2005 (Fumagalli 2010, 188). The worry from Kazakhstan's perspective might be that an opposition fueled on American support and demanding political reforms will destabilize the country and the government. However, when the planned withdrawal, by the United States from Afghanistan, occurs in 2014, its interest in Central Asia as a whole and Kazakhstan as part of it may be lessened, at least in regard to security issues.

Kazakhstan has developed more close relations with Russia and China from the early 2000s (Sultanov and Muzaparova 2003). This comes as China's influence and economic power has grown, with increasing economic presence in Kazakhstan. This also relates to China's increasing need to import oil to cover its oil deficit, with the oil deficit becoming negative from 1993 (Guangcheng 2003, 126). Central Asia and Kazakhstan has oil and gas that China needs to achieve a secure supply of energy to continue its economic growth. Energy is therefore a major part of Chinese policy toward Kazakhstan and as a strategic issue for the Chinese state (Guangcheng 2003, 117, 126). Energy security is therefore closely linked with foreign policy for China. Kazakhstan represents an opportunity for China to secure its interest in stability of energy supply and a land route which lessens dependency on seaways for import of energy to China (Shaffer 2009, 51). China is also interested in stability in

Kazakhstan and in Central Asia in fear of separatism in its western province of Xinjiang (Guangcheng 2003, 109, 111). These interests can be seen in relation with China's "going out" policy. The Chinese state has through this policy encouraged Chinese companies and NOCs to invest abroad and become multinational (Paik 2012, 280-285). Chinese NOCs have pursued a strategy to globally buy energy assets to secure oil and gas supplies (Ziegler 2006, 8). Even if China has invested abroad from the early 1990s and in Kazakhstan from 1997, it has intensified in the 2000s (Paik 2012, 280, 282-283, 286-297). Results of major Chinese investments and acquisitions in Kazakhstan can be seen in Tables 3, 4, 5 and 6.

Kazakhstan's shift to focusing building relations with Russia and China, with the United States and Europe as balancing actors, can be seen as a sign of Kazakhstan's stronger economic position with higher oil prizes. Furthermore, it may also be connected with Russia and China being more interested and capable of involvement in Central Asia and Kazakhstan. China also moved closer to Kazakhstan after offering Kazakhstan financial help during the global financial crises (BBC News 2010). Help came through loans-for-oil agreements in 2009 worth US\$10 billion, where China's NOC CNPC bought half of the oil company Mangistaumunaigaz as part of the deal (Bloomberg 2009). In total, in 2009 the financial help amounted to nearly US\$13 billion according to BBC News (2010). However, the Kazakhstan's government has to balance Chinese economic involvement in Kazakhstan to not upset public opinion. Kazakh public opinion is deeply skeptical of China. An example of this is when the Kazakh government reconsidered leasing agricultural land to China after public resistance (BBC News 2010).

An important shift since Kazakh independence is Putin's presidency and rise to power in Russia from 2000. During Yeltsin's reign Russia had a more distant relationship with Kazakhstan with Russia's policy toward Central Asia being more inconsistent, contradictory and uncertain (Kavalski 2010, 9-10; Laruelle 2010, 156). This uncertainty can be described as "one document-signing after another, most of which were soon forgotten or greatly encumbered if implemented" (Naumkin 2003, 58). In the late 1990s, Russian foreign policy became more coordinated (Naumkin 2003, 59). Russia had largely neglected Central Asia in the 1990s to prioritize developing relations with Europe. This lasted until December 1999 when the "Near Abroad"<sup>26</sup>, including Kazakhstan, became a new priority in Russian foreign policy (Sultanov and Muzaparova 2003, 190). From 2000 Russia returned as the most

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<sup>26</sup> It refers to the former Soviet republics.

important partner from being in the background in the 1990s for Kazakhstan and the other Central Asian countries (Laruelle 2010, 160). Russia had strengthened its position and was more active in developing relations from 2000. Even so it is important to note that Russia never left Kazakhstan and Central Asia in the 1990s. Putin brought new energy and prioritized the Russian-Kazakh relationship by more meetings at top levels, new agreements and support for Kazakh initiatives for integration (Naumkin 2003, 59-60). Since then Putin and Nazarbaev and other top officials have urged that Russia and Kazakhstan have a special and close relationship as well as a strategic partnership (Kazinform 2010; Trend 2012).

The energy sector and issues of oil and gas have been closely linked with the foreign policy of Russia in general and, more specifically, in relation to Kazakhstan under both Yeltsin and Putin (Nygren 2007, 177; Oldberg 2011, 49-50). President Putin and President Nazarbaev met 15 times in Kazakhstan during Putin's first and second term as president from 2000-2008, with topic of the meetings having a great emphasis on energy issues (Sorbello 2011, 113). In 2005 alone, the number of summits between the two presidents were as many as ten (Nygren 2007, 176). An important aim and interest for Russia is to control transport routes for energy and lessen its dependency on transit countries (Oldberg 2011, 51-52). Control of transport from Kazakhstan and Central Asia gives both economic gains of revenue and political power to pressure. In practice, this means Russia is working to gain as much from Kazakhstan's oil and gas resources as possible.

In the latest strategy for *Kazakhstan 2050* President Nazarbaev reaffirms Kazakhstan's priority of developing partnerships with Russia, China, USA, Central Asian, European and Asian countries (Nazarbaev 2012b). This is consistent with the multi-vector approach. The closer relationship between Kazakhstan and both Russia and China after the year 2000 can be related to energy agreements and development of energy resources. These are explored more in Chapter Five.

To summarize briefly, since 1992 until 2012 the multi-vector approach has been consistent in Kazakh foreign policy. The fragile situation for the Kazakh state in the 1990s and the foreign policy situation of Kazakhstan show the need for the multi-vector approach, based on pragmatism, building good relations with everyone, multiple partnerships and balancing. Both political and economic aims seem important for Kazakh foreign policy. The foreign policy situation and background show how important the relation with Russia is for Kazakhstan. This is reflected by Kazakh priority regarding this relationship and its policies toward Russia.

# **5 Energy and the Multi-vector Policy**

## **5.1 Introduction**

In this chapter the oil and gas resources of Kazakhstan are discussed in relation to the multi-vector policy. This is done by analyzing how Kazakhstan has chosen to develop its energy resources, and Kazakhstan's choices in developing export routes. General trends and the big picture are explored to see if political considerations in relation to foreign policy play a role in Kazakhstan's decisions. Are there general patterns of investment decisions?

In the first part data presented in Chapter Three, Tables 3 and 4 are used as a base for analysis. The aim is to find if there are trends and patterns in Kazakhstan's oil and gas industry after 2000 regarding energy companies, the companies' size and countries that are involved. Change from 1992 will be taken into account. The change connected with the rise of KazMunaiGaz (KMG) and its implications are then discussed. In addition, the major projects of Tengiz, Karachaganak and Kashagan are explored to see the development in practice. In the second part, Kazakhstan's choices regarding development of export routes are analyzed. This is done by looking into the development from 1992 and exploring the different existing export routes. In addition, some alternative export routes that have only been partly developed or totally undeveloped are presented and discussed. In the third part, the relationship between energy resources and the multi-vector foreign policy is discussed in light of the findings made from analyzing the data in part one and two of the chapter. Furthermore, there is a discussion if and how Kazakhstan has used its energy resources, seeing it as part of a larger foreign policy picture. The chapter ends with a discussion of whether Kazakhstan's energy resources are a possible tool or driver for foreign policy and the multi-vector policy.

## **5.2 Energy Projects and Presence of Foreign Companies in Relation to Multi-vector**

### **5.2.1 Development of Oil and Gas Resources in the 1990s**

Since 1992 the Kazakh government has been faced with the issue of how to best develop its oil and gas resources. The size of the reserves compared with the population meant that the



potential for revenue was great and represented a source of prosperity. However, the resources could also help the state achieve its aims of state sovereignty, state security and economic development.

As discussed earlier, Kazakhstan was in a vulnerable situation of the 1990s. Kazakhstan needed to secure its independence from Russia, to develop the country economically and to develop its energy resources. It was important for Kazakhstan to reduce its dependence on imports of energy from Russia and on Russian pipelines for energy transport. Logically, the government used what means it had at its disposal to reach its goals, following the argument of Shaffer (2009, 1). Kazakhstan's petroleum wealth gave the government an opportunity to through energy development to achieve real independence, autonomy and economic growth.

Since Kazakhstan in the early 1990s did not have the capacity to finance, or the technology to develop its oil and gas resources on its own, the natural move for Kazakhstan was to invite foreign states and companies to provide assistance. Kazakhstan could decide who and how many actors it wanted to sign development contracts with. Russia had its own problems in the early 1990s and did not have the sufficient technology and finances to develop the large fields in difficult conditions in Kazakhstan (Olcott 2011, 111). More involvement from Russia at this early stage would also not help Kazakhstan diversify its partners and make it less dependent on Russia. Kazakhstan chose to bring in capable companies from Western Europe<sup>27</sup>, the United States and Canada with the expertise and finance to develop its oil and gas resources. Major international oil companies (IOCs) became partners in Kazakhstan, such as the Italian Agip (now ENI) and British Gas (now BG Group) on Karachaganak field and American Chevron on the Tengiz field (Olcott 1996, 79). Another important company was Hurricane Hydrocarbons (now PetroKazakhstan), then a Canadian company operating in Kazakhstan from 1991 (PetroKazakhstan 2012a). However, Russian companies and interest were not absent. In 1995, Lukoil signed an agreement with the Kazakh government to develop the Kumkol field and to supply oil to Kazakh refineries in Pavlodar and Shymkent (Olcott 1996, 79). The IOCs got contracts and PSAs on favorable terms with Kazakhstan in the 1990s, at a time when oil prices was low and the Kazakh state was not strong financially (Yenikeyeff 2008, 4-5).

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<sup>27</sup> Referring to non post-communist countries in Europe.

This development led by the Kazakh government in the 1990s can be seen both from an economic perspective and a political perspective connected with the multi-vector foreign policy. The Kazakh policy seems sound from an economic point of view. It is possible to attract more investments and to achieve better deals by bringing in many different companies competing for contracts than cooperating with only a few selected partners. Kazakhstan's beginning cooperation provided a win-win situation where both the Kazakh government and IOCs could get a share of the profits. The IOCs, represented by Chevron (US), also committed to support social programs, help develop local communities and use local content<sup>28</sup> through Kazakh workers, goods and services (Tengri News 2013c). This helped to develop the Kazakh economy. This also served the Kazakh state and is an important goal of the multi-vector policy. In this way economic development by development of energy resources can be linked to the multi-vector policy.

The result from the policy of inviting foreign companies was that Kazakhstan had many different companies operating on its territory associated with many foreign states by the end of the 1990s (Kolchin 1997). This era in Kazakhstan can be characterized as an era of oil majors with entry of the largest energy companies (Chevron, Mobil, Shell, BP, BG, Eni, Exxon, Texaco) (Kalyuzhnova 2008, 73). By bringing in foreign companies and IOCs, the Kazakh government got much needed foreign investments, finance and expertise to develop its energy resources. The government's aim of bringing in foreign investments was remarkably successful. According to Cummings (2003b, 31), "Kazakhstan had by 1997 attracted the second largest amount of per capita foreign direct investment of all post-communist states (after Hungary)." Most of these investments went to the oil and gas sector.

The presence of Russian companies such as Lukoil in the 1990s shows that Kazakhstan did not want to keep Russian interests out of the country. There are several reasons why Russian companies may have been favored. It may be of habit and familiarity that Kazakhstan chose to work with Russian companies. It could also be that Kazakhstan was interested to give Russia a stake in its energy resources, both to get investments and bring in Russian influence. Kazakhstan might be seeing it as an advantage to have Russian energy interest represented. If Kazakhstan were to exclude Russian companies from its energy sector to try to weaken Russian influence, it may be counterproductive. Russia would probably not be pleased and

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<sup>28</sup> Local content refers to the use of local recruitment, training, purchasing of services and goods in a country that host oil and gas projects.

relations would suffer as a result. Since Kazakhstan has a closely interdependent relationship with Russia, it would be dangerous economically and for security to alienate its large neighbor (especially in the early 1990s). However, the favoring of signing contracts with Western IOCs over Russian companies can be seen in relation to the political climate of the period. Considering the 1990s, this was when Kazakhstan tried to develop good relations with Europe and the United States, while Russia had a more withdrawn approach to Kazakhstan and Central Asia.

After being in the background for years China evolved to a more important player in Kazakhstan's energy development. China entered the Kazakhs oil and gas sector for the first time in 1997 when China National Petroleum Corporation's (CNPC) purchased 60 percent of Kazakhstan's Aktyubinsk Oil Company for \$4.3bn (Jaffe and Lewis 2002, 125). This was followed up by several contracts, such as the Chinese investments in Uzen field from 1997 and the planning of the Kazakhstan-China oil pipeline (Ziegler 2006, 12). This sudden change in China's interest in Kazakhstan's energy can be seen in relation with a new government directive that pushed Chinese state companies, such as CNPC, to acquire energy production internationally (Jaffe and Lewis 2002, 122). This "going out" policy can be seen as a clear move to strengthen energy security for China after the country became a net importer of oil in 1993, as discussed in Chapter Four.

From a political perspective, the Kazakh government's choices in energy development in the 1990s can be seen as a way to increase security and achieve foreign policy aims, and reflects the multi-vector policy. From Astana's point of view, foreign IOCs represent their country of origin and their presence is a part of the foreign state's national interest. However, it is important to note that most IOCs are independent private companies. NOCs on the other hand are more directly linked to its government. After Kazakhstan's decision to dismantle its nuclear arsenal, President Nazarbaev, declared "Our main security will be a powerful Western business presence in Kazakhstan" (Associated Press 1994). The importance of American companies involvement in Kazakhstan related to Kazakhstan's national security was confirmed by foreign minister Tokaev in 2002 (BBC News 2002). The thinking behind this is that Kazakhstan needed, and continues to need, to balance Russian influence to not be vulnerable to pressure. The presence of American and European energy companies can be a tool to this end. Kazakhstan gave each actor a stake in its energy resources by bringing in different companies from different western states. This implies that they also have a stake in

the future and stability of Kazakhstan. An important reason for the Kazakh government to diversify in this way is that large Western energy companies bring with them important diplomatic support (Olcott 2002, 215). The entry of large American companies is especially important in this regard. Support from the world's superpower can enhance Kazakhstan's security and be a powerful counterweight to Russia's strong position in relation to Kazakhstan.

### **5.2.2 Development of Oil and Gas Resources from 2000**

After 2000 Kazakhstan still seem committed to a multi-vector approach in relation to development and ownership of its oil and gas fields. The data presented in Chapter Three is used here to explore and to analyze developments in development rights of resources and presence of foreign IOCs after 2000. By examining Tables 3 and 4 it is possible to get an overview of the situation in 2012 on the large energy projects. There are four important changes from 2000 that should be highlighted in light of the situation in 2012.

Firstly, after the agreement on national sectors in the Caspian Sea with Russia and Azerbaijan, several offshore fields have been opened for exploration and production in the Caspian Sea, which were not available in the 1990s. These fields have made less progress in their development than onshore fields, with no production offshore as of 2012. Offshore fields generally need more time to be developed than onshore because of more difficult conditions. The consequences of this political agreement show the key importance of politics and foreign policy to energy development. This is also an example of how energy can drive and influence foreign policy, as suggested by Shaffer (2009). The prospects for development of energy resources in the Caspian basin were a powerful incentive for Russia and Kazakhstan to come to an agreement.

Secondly, there is now a substantial Russian presence, both onshore and offshore. Of the 15 onshore projects in Table 3, Russian energy companies have stakes in seven. Russian companies have stakes in seven of 15 offshore projects, as seen in Table 4. Russia's relative strong presence offshore can be linked to cooperation agreements signed with Kazakhstan in 2002 as discussed earlier, and to the opening of the Caspian for petroleum exploration. This can also be seen in relation to an agreement in principle from President Nazarbaev in 1996. This agreement pledged Lukoil operation on 20 percent of Kazakhstan's part of the Caspian Sea (Kommersant 1996). Onshore increased Russian presence is directly attributed to

acquisitions of stakes made by the Russian company Lukoil when they bought Caspian Investment Resources from Nelson Resources for \$2 billion in 2005. Half of the company was later sold on to Mittal Investment in 2006, and then Mittal resold to Chinese Sinopec in 2010 (Kommersant 2006; Ekspert Kazakhstan 2010). Lukoil also bought BP's share of LukArco in 2009, and by that increased its stake in Tengiz and the CPC pipeline (BP 2009). Even if Russian companies share of current Kazakh oil and gas production is relatively low compared with Chinese and American companies, the sheer number of developing projects by the Russians shows Russia's importance in energy for Kazakhstan.

Thirdly, large Chinese NOCs have gained a firm presence in energy projects in Kazakhstan. Of the 15 onshore projects, Chinese companies own shares in ten. However, Chinese stakes are only two of 17 offshore projects. This development can be seen as an increasing need to secure access to energy resources for China's energy needs, in line with China's interest as discussed earlier. According to Olcott (2010, 265), China is becoming a dominating presence in onshore projects in Kazakhstan, in both major and smaller fields. The findings presented here give some support to Olcott's view of the Chinese presence. Even if China has a strong and increasing position onshore, to call it dominant may be too strong of a statement. One has to consider the strong Russian presence, KMG's large share and European and American IOCs' dominance on major fields such as Tengiz and Karachaganak. The increased Chinese presence after 2000 in major projects has come through mainly three acquisitions. In 2003, CNPC purchased stakes in North Buzachi from the IOCs Texaco and Nimir (CNPC 2013). Canadian PetroKazakhstan was bought in 2005 by CNPC, and then shared with Kazakhstan and KMG the year after. In addition, there is Sinopec's acquisition of Caspian Investment Resources in 2010 as mentioned above. When buying stakes in both small and large projects, the Chinese NOCs with Chinese government support have often offered higher prices in bidding on tenders to secure energy assets in Kazakhstan (Oil & Gas Eurasia 2012). This is important evidence to the claim that Kazakhstan is central in China's bid to achieve energy security. As a result China has gained a large share of Kazakh oil production. How large the share is not certain. One estimate is that Chinese NOCs control 25 to 30 percent in 2012 (Oil & Gas Eurasia 2012). Some have even claimed that China will control over 40 percent of Kazakh oil production in 2013, through direct and indirect ownership (Tengri News 2013a). The latter estimate seems a bit high. It is difficult to make a precise estimate because of intermediary foreign companies owning shares in projects which increase uncertainty of ownership. However, Chinese companies do not currently have the oil reserves to sustain its

current large share of Kazakh oil production. Chinese companies are not represented in the major projects such as Kashagan, Tengiz and Karachaganak. This is where most of Kazakhstan's reserves are located and the origin of most of future increase in oil production.

It is interesting that Chinese companies are so heavily involved in energy projects in Kazakhstan, but have not been able to buy into the largest projects of Tengiz, Karachaganak and Kashagan. As discussed later in this chapter, Kazakhstan may be wary of China getting too large a share of its oil and gas resources and therefore block attempts to buy stakes in the large strategic projects such as Kashagan. Furthermore, this could be a balancing multi-vector move to hinder that the Chinese vector does not become too strong and dominant. A key difference between the large Chinese companies (CNPC, Sinopec and CNOOC) and most of the IOCs operating in Kazakhstan is that the Chinese companies are NOCs and owned by the Chinese state. This means that the political connection between Chinese companies and their government is relatively stronger regarding these companies compared with other foreign energy companies in Kazakhstan. This point might contribute to Kazakhstan's opposition against giving the Chinese too much access to its energy resources.

The fourth main development in the 2000s is the rise of Kazakhstan's NOC KMG from 2002 and its presence in Kazakhstan's energy sector. As can be seen in Tables 3 and 4, KMG has grown to become a significant player in Kazakhstan's oil and gas projects. In 2012, KMG had a stake in every major offshore project. Onshore, KMG had stake in eleven of 15 projects. The result is that KMG is involved in nearly all oil and gas projects of significance in Kazakhstan (Olcott 2011, 116). This find is evidence of increasing resource nationalism in Kazakhstan from 2002. The Kazakh state has increased its presence in the oil and gas sector since 2000 both by reserving the right for KMG to get 50 percent of new projects, as discussed earlier, but also by negotiating the entry of KMG into established PSAs on older projects. However, KMG acts as sole operator on only a few major projects. One reason for this is that KMG still lacks sufficient financial and technological strength to develop fields in difficult conditions (Yenikeyeff 2008, 6).

The choices by Kazakhstan to develop a strong NOC and to have a greater state role in the oil and gas sector can be seen in light of increasing oil prizes and a stronger government from 2000. In other words, the Kazakh state's ability and economic benefits of having a NOC were pulling in the direction of developing a strong KMG. Establishing a NOC is not uncommon for countries with significant oil and gas reserves, but rather the norm internationally. By

having KMG operating directly in the oil and gas projects, the Kazakh state can increase its revenue. Increased revenue comes from dividends from KMG to the state and a domestic workforce paying taxes from oil and gas related work in addition to the regular taxes on oil and gas operations. This view is in line with the argument that energy exporting states want to get the highest price or value possible from its resources based on economic motivations, as discussed in Chapter Two. In this regard KMG can be seen as a tool to maximize economic value and economic development. This is central to Kazakhstan's interests and one of the aims of the multi-vector policy. This view is support to an argument by Olcott (2007) on KMG's relation to foreign policy: "While NC KMG has often been the voice through which the Kazakhs speak, their leadership has not been the source of these foreign policy decisions; it simply has become the vehicle for executing them" (Olcott 2007, 56-57).

Apart from the natural implication of higher revenue and economic gains for Kazakhstan, there are other important implications of KMG's increased role in the oil and gas sector. First, when the Kazakh state increases its share in oil and gas projects through resource nationalism, the share available for everyone else decreases. This means that there is less profit and opportunities for foreign investors, IOCs and NOCs. This could lead to less plurality of energy companies and a fall in the magnitude of foreign stakes in the Kazakh oil and gas sector over time. As a consequence of this, Kazakhstan's ability to use the energy resources as a tool to balance foreign powers in a multi-vector framework may be compromised. Secondly, by developing KMG to become a solid and competent energy company that can operate on its own, means that the need for foreign IOCs will decrease in Kazakhstan. This is important because it gives Kazakhstan a better bargaining position and reduces the relative dependence vis-à-vis foreign IOCs.

### **5.2.3 Continuity in Development of Oil and Gas Resources**

Apart from the four major changes from 2000 outlined above there are also some factors that have been more stable in Kazakhstan's oil and gas sector. The three most important projects: Kashagan, Tengiz and Karachaganak are still dominated by large IOCs with American and European origin. There are still many IOCs involved from different countries, more so offshore than onshore, relating to the Russian and Chinese acquisitions in the 2000s as discussed earlier. In Kazakhstan in 2012 companies from 15 foreign countries have a stake in

one or more major oil and gas projects<sup>29</sup>. If one does a study of smaller fields as well, the number of foreign countries associated through IOCs increase even more (Olcott 2010). On the other hand there seems to be a trend of IOCs from Europe and the United States are moving toward being relatively less involved in Kazakhstan's major oil and gas projects (Respublika 2013). This has happened both by exit and by takeovers by other companies. Examples are the sale of BP's assets in Kazakhstan in 2009, Statoil and ConocoPhillips exits scheduled for 2013, in addition to the buying of IOCs such as PetroKazakhstan and Caspian Investment Resources by Russian companies, Chinese NOCs and KMG as earlier mentioned (BP 2009; Washington Post 2013). Reasons behind the exit made by IOCs from Europe and the US have been speculated to be resource nationalism and loss of investment attractiveness (Respublika 2013). This point is discussed more below. I will now move on to explore the three most important energy projects Tengiz, Karachaganak and Kashagan in more detail to see the development in practice and their role in the bigger picture.

#### **5.2.4 Development of Tengiz, Karachaganak and Kashagan**

The three giant fields of Tengiz, Karachaganak and Kashagan represent Kazakhstan's greatest reserves and most of the potential for growth in production (Kaiser and Pulsipher 2007, 1303). At the same time developing these projects account for a large part of foreign investment in Kazakhstan. To get a better understanding of the dynamic between the energy resources and the multi-vector foreign policy it is beneficial to look more closely at the three largest energy projects.

##### **Tengiz**

The Tengiz field was discovered in 1979. It is one of the largest fields in Kazakhstan with reserves of 6 to 9 billion barrels (TCO 2013). The field is located in western Kazakhstan, just by the northeastern shore of the Caspian Sea. Tengiz is important because it is currently the largest producing field in Kazakhstan with a little under one third of total oil production (EIA 2012). Tengiz is also important because it was the first major oil project in Kazakhstan in the 1990s to be developed by foreign investors. The negotiations regarding development of

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<sup>29</sup> The companies involved in major energy projects in 2012 are from the following countries: US, Italy, France, UK, Nederland, Japan, Russia, Oman, China, India, South-Korea, Spain, UAE, Norway and Hungary. See Tables 3 and 4.



Tengiz started in 1988, and went on until 1993 when the final agreement was signed. The contract spans 40 years. Foreign interest in this field was significant because of the large revenue potential. The major IOC Chevron (US) won the rights to lead the development of the field, in competition with Russian companies (Sorbello 2011, 71). Originally, Chevron joined Kazakhstan in a 50-50 joint venture by founding Tengizchevroil (TCO), but the Kazakh government soon reduced its share. After Mobil bought a 25 percent share from Kazakhstan in 1996, the joint share of the American companies Chevron and ExxonMobil in TCO is now 75 percent (TCO 2013)<sup>30</sup>. From 2001 Tengiz started to export most of its oil through the CPC pipeline. Before that most of the oil was transported through Samara and the Russian pipeline system and by rail (Kaiser and Pulsipher 2007, 1303). The CPC pipeline was a key to gain export capacity from Tengiz and to be able to increase production at the field. By awarding the rights to develop Tengiz to American companies the Kazakh government could bring in and secure American long term interest in Kazakhstan, as well as secure future oil production and finance for development. The sale of stakes in the field also provided needed funds for the state treasury. Tengiz was central in the US vector of Kazakh foreign relations by bringing in a long term large American business presence in Kazakhstan. This was especially important for Kazakhstan in the 1990s when Kazakhstan greatly needed investments and to develop good relations with the United States as a balance to Russia. Tengiz can be seen as an asset to be sold and a bargaining chip for the Kazakh government to pursue economic and foreign policy goals, which supports the views of İpek (2007).

## **Karachaganak**

Discovered in 1979, and is one of the largest oil and gas condensate fields in the world (KPO 2013). Karachaganak is located in the north-west, very close to the Russian border and the Russian Orenburg refinery. In 1997, Kazakhstan signed a 40 year final production sharing agreement with Eni (Italy), BG Group (UK), Chevron (US) and Lukoil (Russia) creating the Karachaganak Petroleum Operating B. V. (KPO). KPO started a large development of the field to increase production. In 2007, Karachaganak contributed with 49 percent of Kazakhstan's total gas production and 18 percent of oil production (Yenikeyeff 2008, 23). In 2012, KMG joined the project with a share of 10 percent after the government and the IOCs in KPO had a dispute about environmental and tax issues at Karachaganak (Sarsenbayev 2011; Natural Gas Europe 2012; Tengri News 2012b). Allegedly the deal meant that by

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<sup>30</sup> Chevron owns 50 %, ExxonMobil owns 25 %, KMG 20 % and LukArco 5 %. See Table 3.

giving KMG a share in KPO, the Kazakh government would drop export duty claims. Prior to this event, Karachaganak was the only major energy project without government representation by KMG. This pressure of IOCs by the government can be seen to be driven by economic motivations since it will bring an estimated \$3.3 to 5 billion in revenues to KMG by 2037. By KMG representing the government in the consortium the Kazakh state can also be able to influence decisions more directly if it wants. An important part of the agreement was that KPO would receive an additional two million tons of oil capacity in the CPC pipeline (Reuters 2012).

The Karachaganak field represents an interesting case both because of its size and importance to Kazakhstan, but also because of the close connection to the Russian pipeline system and the Russian Orenburg refinery. Before the CPC pipeline became operational, and linked with Karachaganak in 2002, the oil and gas condensate from Karachaganak went north through Russian pipelines (Kaiser and Pulsipher 2007, 1304). This arrangement of transport through the Russian pipeline system has been highly unfavorable for Kazakhstan and the companies operating on Karachaganak. There have been high tariffs and estimated sale prices down to as low as 30 percent of world level (Hines and Shyngyssov 2005, cited by; Kaiser and Pulsipher 2007, 1304). When oil from Karachaganak had no real alternative to export through the Russian pipeline system, Transneft could easily give unfavorable terms to the Karachaganak Venture. Low prices and high tariffs did not only apply to oil, but gas condensate as well. Understandably Kazakhstan and the IOCs involved at Karachaganak wanted to solve this unfavorable economic and political situation.

This situation can also be understood in the context of Karachaganak's dependence on the Orenburg refinery for processing of gas condensate and to continue its level of production. In effect, this put Russia in a position to pressure Karachaganak regarding price of deliveries to Orenburg. As a consequence of low price and lack of access to other markets, as much as 6.6 bcm of gas has been re-injected into the field a year, according to Upstream (2005). Potentially this is a security and economic risk for Kazakhstan and for the IOCs involved. If the Orenburg refinery breaks down or the Russian government decides to stop import from Kazakhstan to Orenburg (for one reason or another), then Karachaganak would have to reduce production and Kazakhstan and the IOCs involved would suffer accordingly.

Despite of these problems Kazakhstan tries pragmatically to make the best out of the asymmetric situation with its strategic partner Russia. On July 17<sup>th</sup>, 2006, Presidents

Nazarbaev and Putin signed a joint declaration on cooperation on gas processing of gas from Karachaganak at Orenburg (KazRosGas 2013). Cooperating on gas processing was concretized by Kazakhstan and Russia when they started a joint venture to expand the Orenburg refinery to a capacity of 15 bcm a year. According to RFE/RL (2006a) President Nazarbaev said, "First of all, it saves billions of dollars that would have been spent on building a new plant..." Economic considerations in this matter seem to have been important for Kazakhstan, at least in public. As a result of this KazRosGas<sup>31</sup> signed a 15 year agreement with KPO in 2007 to process gas at Orenburg and export it. In accordance with the agreement KPO increased its supply of gas from 7.5 bcm a year to 16 bcm a year to Orenburg (Yenikeyeff 2008, 25). Then some of the gas is sent back to Kazakhstan for domestic use, while the rest is exported through Russian pipelines. This agreement was important for Kazakhstan since to be able to increase production at Karachaganak it must have transport and processing capacity available.

The oil portion of the dependence on Orenburg and Russia's pipeline system was largely dealt with when an oil pipeline was built from Karachaganak and linked with the CPC pipeline in 2002, with the first Karachaganak oil shipped from Novorossiisk in 2004 (KPO 2013). Because of this Karachaganak gained diversified export routes, and since 2004 70 percent of its oil is transported through CPC (Upstream 2005; BG Group 2013). The gas portion of the dependence remains a challenge to Kazakhstan since export of gas currently has no real alternatives to Russia. However, President Nazarbaev announced plans in 2012 to build a new gas processing plant with a capacity of 5 bcm a year to handle the production from Karachaganak (Nazarbaev 2012a). President Nazarbaev also stated that this was part of the effort to gasify Kazakhstan by supplying domestic markets and becoming more energy self-sufficient. This move by Kazakhstan would make Karachaganak less dependent on Orenburg refinery and, in turn, KPO may be able to be offered better price and tariff for its gas. However, since the capacity of the new plant is only 5 bcm a year it will be in addition to Orenburg not replacing it. Phase I of the new plant is scheduled to be online in 2019 and phase II in 2023 (Tengri News 2012e). This means that the plant will be fully operational when the 15 year agreement on gas processing at Orenburg is complete. If Russia and Kazakhstan cannot agree on a price for gas, Kazakhstan may after the Beineu-Bozoi-

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<sup>31</sup> KazRosGas is a joint venture between Kazakhstan and Russia created in 2002, as a result of the agreement between the Government of Kazakhstan and the Government of Russia regarding cooperation in gas industry on November, 28th, 2001 (KazRosGas 2013).

Shymkent pipeline is operational in 2015, send gas from Western Kazakhstan and Karachaganak to the southern part of the country or to China instead (Tengri News 2013b).

Developments on the Karachaganak project show the close relationship between energy, politics and foreign policy in Kazakhstan. This find on this relationship is in line with views of Sorbello (2011) and Shaffer (2009). Regarding Karachaganak, Kazakhstan brought in British, Italian, American and Russian interests, and thereby created a balance between influences from foreign states. This is an example of the multi-vector approach in the development of energy resources. Kazakh-Russian interaction shows the dependence relationship in the energy sector, where Kazakhstan must work together with Russia to be able to develop its oil and gas resources at Karachaganak. These findings support the views of İpek (2007) regarding Kazakhstan's multi-vector approach to development of energy resources, and the importance of its relationship with Russia.

Gas seems to be more difficult than oil for Kazakhstan to export via other routes than Russia. The reason for this seems to be the lack of gas pipelines outside Gazprom (Russian) control, compared with several alternatives for oil. To open alternative export routes for gas is both expensive and difficult, especially if the volume is limited (Pirani 2012, 43). Consequently it seems to be a good economic option for Kazakhstan to continue cooperation on Orenburg and export through Russia from Karachaganak, even if the terms are not favorable. In addition, it is in Russia's interest to pressure Kazakhstan regarding gas to get them to export as much as possible at a low price through Russian pipeline to maximize Russian value from the trade. Before 2008 it may also have been important to keep Gazprom's export obligations to Europe and China (RFE/RL 2006b). However, Gazprom's market share and export volumes in Europe has declined from 2008 (Korchemkin 2010; The Economist 2013). This means that this point less relevant as an explanation after 2008. Kazakhstan's actions make sense in a multi-vector perspective by them cooperating with several IOCs, at the same time the pragmatism is clear in the way Russia's strong position is not ignored or openly challenged. Kazakhstan tries to get as much value as possible from its position at Karachaganak, and simultaneously to balance Russian interests with European and American companies. The connection of Karachaganak to the CPC pipeline, and the plan to open up for gas to China, are examples of how Kazakhstan differentiates its export routes in correspondence with its multi-vector policy.

## **Kashagan**

Kashagan is Kazakhstan's largest oil field and is located offshore in the north-eastern part of the Caspian Sea. The field was identified in the 1970s, but was not drilled or explored further because of challenging environmental and geological conditions which meant that development would demand high cost and be technically difficult (Kaiser and Pulsipher 2007, 1304-1305). One challenge is that this area of the Caspian freezes in winter. The discovery of the field was made official in 2000 and declared commercial in 2002 (Campaner and Yenikeeff 2008, 5). Kazakhstan's moves regarding ownership of this project are interesting. In 1997, the North Caspian Production Sharing Agreement was signed between Kazakhstan and Offshore Kazakhstan International Operating Company (Campaner and Yenikeeff 2008, 8). In 1998, Kazakhstan government sold its development rights in the project to Phillips (US) and Inpex (Japan) for \$500 million (Campaner and Yenikeeff 2008, 13). In 1998, this consortium consisted of nine IOCs: ENI's subsidiary Agip (Italy), BG (UK), BP Amoco (UK), ExxonMobil (US), Shell (UK/Nederland), Total FinaElf (France), Phillips Petroleum Co. (US), Statoil (Norway), and Inpex (Japan) (Campaner and Yenikeeff 2008, 8). However the composition of the consortium and its name has changed several times. Because of the difficulties and costs of developing this field it was necessary for Kazakhstan to invite large IOCs with expertise and finance. Estimates of the costs of developing so far are different and range from \$46 billion to \$116 billion (as of 2012), if the latter is the case it would make the project the most expensive in the world (BBC News 2012; Tengri News 2012a).

In 2003, BG Group (UK) wanted to sell its share in the project to Chinese companies CNOOC and Sinopec, but the deal did not go through because the consortium partners exercised their pre-emption rights (Campaner and Yenikeeff 2008, 8, 13). Finally, in 2004, the Kazakh government bought half of BG's share with the other half going to the IOCs in the consortium. This blocked the Chinese from entering the Kashagan project. The Kazakh government represented by KMG increased its share further in 2008 when they signed an agreement with the consortium to get compensation for delays in development of the field (Campaner and Yenikeeff 2008, 13; Babali 2009, 1299). As a result of this agreement the consortium changed its current name to North Caspian Operating Company (NCOC).

Kazakhstan's decisions regarding buying back a stake in Kashagan can be seen in relation to developments toward resource nationalism and the increasing role of KMG in the Kazakh oil and gas industry. At the same time the context of rising oil price in the 2000s and a more

secure economic and financial position for Kazakhstan in the 2000s meant that Kazakhstan was better able to take a more active role and secure a stake in Kashagan.

The composition of the consortium starting from 1998 to 2012 shows Kazakhstan's commitment to and practice of the multi-vector foreign policy. Large IOCs from several important countries including the United States, Japan, France, UK and Italy were given a stake. The long term development of Kashagan implies that Kazakhstan can secure these countries interests for decades and by that balance these countries with Russian and Chinese interests. The fact that no Russian and Chinese companies have been accepted by the government as stake holders in Kashagan appear to be a sign that Kazakhstan wants to limit these countries influence on its oil and gas sector. This argument is strengthened by the rejection of the sale of shares in Kashagan to Chinese companies CNOOC and Sinopec in 2003 as mention above. However, the technological and financial resources required to develop this field is an important reason for favoring the major western IOCs over Russian and Chinese companies, especially in the 1990s. Kazakhstan has a reason to limit Chinese and Russian companies' involvement in Kashagan because they are largely involved in many other energy projects in Kazakhstan, and thus to make sure that Russian and Chinese companies does not get too large share of Kazakh oil and gas (See Tables 3 and 4). This multi-vector balancing act by Kazakhstan is clear in the case of Kashagan. This gives support to the views of İpek (2007). The political considerations in Kazakhstan's decisions must be seen in a close dynamic with economic considerations of gaining the most value from the field, by preferring KMG as a partner before Chinese companies.

### **5.2.5 Thoughts on Development of the Kazakh Oil and Gas Sector**

In this part of the chapter it has been shown that there has been an evolving dynamic in the composition of energy companies operating in the development of Kazakhstan's oil and gas resources from 1992 to 2012. Kazakhstan has invited companies from Europe, North America and Asia to get as much foreign investment as possible. Most of the large projects are developed directly or indirectly through ownership by large IOCs or NOCs<sup>32</sup>. One explanation for this is that large companies have more resources to develop the challenging energy projects in Kazakhstan. There seems to be a pattern that Kazakhstan has secured many

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<sup>32</sup> Here it is referred to major IOCs and NOCs, for example Chevron, ExxonMobil, Lukoil, CNPC, Total, Shell and Eni.

different countries represented through IOCs and NOCs, especially the major powers and Kazakhstan's partners the United States, Russia and China. By doing this Kazakhstan avoids being dependent on any actor. However, some vectors in energy and foreign policy in Kazakhstan are more important than others. Considering the significant presence of Chinese and Russian companies in energy projects, with American companies having fewer but bigger stakes in the largest projects, show these actors importance to Kazakhstan. Foreign IOCs and NOCs from different countries can be seen as vectors mirroring the multi-vector policy in the energy sector. Kazakhstan's development of its energy resources of oil and gas using foreign companies may therefore play a role in how the Kazakh government balances between different foreign interests and influence. The foreign policy goal of balancing foreign actors to gain autonomy seems to work together with the broad aim of economic development and development of Kazakhstan's energy resources. This finding regarding the relationship between energy resources and the multi-vector policy supports the arguments of İpek (2007), as discussed earlier.

European and American IOCs had a strong position in the 1990s. They still have a strong presence even if their relative presence in relation to Russia and China is reduced from 2000 to 2012 compared with the 1990s. From the year 2000 Chinese and Russian companies became more involved in Kazakhstan having developed a presence on most oil fields. This development can be seen in the evolving political landscape that occurred in Kazakhstan's relations with Russia, the United States and China. The increasing Chinese and Russian presence in Kazakh oil and gas projects happened simultaneously as Kazakhstan's relations with its two powerful neighbors improved and became closer than before. Russian companies have gained access to the Caspian Sea and several larger oil and gas fields such as Tengiz and Karachaganak, while China has been limited to onshore and smaller fields. This fact means that China's current high share of oil production will fall significantly when Kashagan starts production. Kazakhstan seems to want to limit China's stake in its oil and gas industry from becoming too large, considering that China's share of Kazakh oil production is over 20 or even over 30 percent, as discussed earlier. The statement by Olcott (2011, 118) seems to have merit: "Astana shows no signs of giving Chinese national oil companies the same access to its energy assets that it gives the Russians." This favoring of Russian companies and not Chinese can be an example of foreign policy considerations affecting energy issues. The argument is based on the notion that Kazakhstan is more dependent on Russia than China, and the Kazakh government is therefore trying harder to keep good relations and make concessions to Russia

than with China. At the same time China's presence functions as a powerful balance to Russian influence.

Relations with the United States on the other hand have become relatively more distanced than in the 1990s and early 2000s, compared with Russia and China. The rise and favoring of KMG and beginning resource nationalism by Kazakhstan may also have contributed to the relative weakening presence of European and American IOCs and a relatively more distanced relationship with the respective countries. With fewer resources available to investment for IOCs, combined with higher taxes, might have lead to relatively lower investment attractiveness and thus the exit of IOCs from Kazakhstan.

Even if the composition of foreign companies has changed and Kazakhstan's priority of some vectors over others has changed, there seems to be stability in the overall framework to diversify sources of investments. The underlying approach of multi-vector in relation to oil and gas field ownership rights and presence of foreign IOCs did not change significantly in the period studied from 1992 to 2012. Furthermore, foreign policy considerations linked with multi-vector appears to be mixed with economic considerations in this area for Kazakhstan. Kazakhstan can in effect pursue the aims of developing its economy simultaneously as it balance foreign influence. This may point to energy as both a tool and a driver in relation to foreign policy.

### **5.3 Choice of Export Routes by the Kazakh Government**

Kazakhstan has from 1992 to 2012 been faced with the challenge of how to best export its energy resources given its substantial oil reserves. This challenge continues as according to International Energy Agency (2010, 512) Kazakhstan needs an additional 2 million bbl/d of capacity to be able to export estimated future production. Gas export was not an important issue for Kazakhstan until 2004 when Kazakhstan had become a net exporter of gas. The inherited situation at the beginning of the 1990s was that export routes and capacity by rail and pipelines was limited and directed mainly through Russia. The situation was not favorable in economic or political terms for Kazakhstan. It was faced with high transport costs of rail transport and Russia's near monopolistic position where Russia could dictate terms. The Kazakh government needed a solution for exporting increasing amounts of oil to fair or good



prices, while decreasing its dependence on the Russian controlled export routes (75 % of oil exports in 2010), and at the same time keeping good relations with its powerful Russian neighbor. It is a difficult balancing act for Kazakhstan, with both economic and foreign policy considerations. Kazakhstan had to decide if they wanted to develop one large export route to handle future oil production or the more expensive option of developing multiple export routes. One export pipeline will be much cheaper to build than several, but it provides less security than multiple pipelines. With one export route or pipeline Kazakhstan would be more dependent on the transit country and is more vulnerable to disruptions from technical problems and terrorism (Soligo and Jaffe 2002, 114). This is a clear tradeoff between costs on the one hand and security on the other. For Kazakhstan it made sense to develop multiple export routes with pipelines to export its oil.

The Kazakh government has made its policy clear, Kazakhstan wants to develop multiple pipelines in multiple directions (The White House 2001; İpek 2007, 1188). This policy has been supported by the US, who shares interest in this development. In 2003, then foreign minister Tokaev (2003, 4) stated that, “Our view is quite simple. The more pipelines we will have, the better this will be for Kazakhstan... We have no political prejudices.” This statement shows quite clearly the pragmatic stance of the Kazakh government, which supports the view of Cummings (2003a) and Hanks (2009) on the pragmatic nature of Kazakhstan’s foreign policy. The goal of multiple pipeline routes is also linked to the multi-vector policy, as discussed earlier. By developing multiple pipeline routes Kazakhstan can balance different interests and secure long term partnerships with multiple states and actors. As a result of this policy Kazakhstan has developed several export routes in the time up to 2012. However, they all have their problems and limitations from a Kazakh perspective.

I will now explore the current export routes as of 2012 and see the context of their development. Aspects and considerations related to why Kazakhstan chose to develop as they did and relevant implications will be taken into account. The discussion of the export routes starts with the export routes that have been open from Soviet times and the 1990s. Then moving on to the routes and pipelines developed in the period up to 2012. See Chapter Three, for an outline and data on the pipelines and export routes. Lastly, some alternative export routes that have not been developed by Kazakhstan are discussed.

### 5.3.1 Exports by Rail

Kazakhstan has an extensive rail network which can be used for exporting energy and to transport it domestically for consumption (EIA 2012). The capacity is limited however at around 300 000 bbl/d (about 15 million tons a year) and exports amount for only a part of this capacity with four million tons in 2009 and six million tons of oil in 2010 (International Energy Agency 2010, 513; Ministerstvo nefti i gaza Respubliki Kazakhstan 2010, 14; Ministerstvo nefti i gaza Respubliki Kazakhstan 2011, 7; EIA 2012). Nevertheless, exports of crude oil by rail have increased from the late 2000s to a volume of seven million tons a year by 2012 (Tengri News 2012d).

Kazakhstan has used rail as an export route to both Russia<sup>33</sup> and China since the 1990s. The route to China was opened in the 1990s, transporting about one million tons a year and did so to the oil pipeline to China became operational (Kandiyoti 2008b, 79). Since 2000 exports by rail has been steadily increasing and are projected by International Energy Agency (2010, 513) to increase in the time up to 2035. The rail option has gone from being an important route in the 1990s and early 2000s to become a small part of Kazakhstan's diversification solution to export routes, as the new export routes have come online. The problem with these rail export routes is that they have become the most expensive alternative after increases in costs from the 1990s (EIA 2012). This is shown in low utilization of the rail capacity. The inefficiency of rail explains to a degree the shift toward more pipelines to transport large volumes. From a political perspective rail can be a flexible tool and can be used to shift export between different countries if needed. For example, Kazakhstan can use rail to export more through Russia on the expense of China or vice versa depending on which is most favorable.

### 5.3.2 Atyrau - Samara Pipeline

Atyrau-Samara pipeline was built in Soviet times during the 1970s and connects Kazakhstan oil production with the Russian pipeline system controlled by Transneft<sup>34</sup> (International Energy Agency 2010, 514). This pipeline was Kazakhstan's main export route in the 1990s, before the Caspian Pipeline Consortium (CPC) pipeline became operational in 2001 (EIA 2012). Expansion of this pipeline was done in 1999-2001 (to about 300 000 bbl/d) which increased exports, and from 2009 KazTransOil and Transneft discussed the possibility of

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<sup>33</sup> Oil can be exported through Russia by rail to European markets.

<sup>34</sup> From here Russia can export the oil to markets in North-Western, Central and Eastern Europe.

increasing capacity to 25 million tons (about 500 000bbl/d) (Babali 2009, 1300; International Energy Agency 2010, 514; KazTransOil 2013b). The capacity continues to be limited in 2012, and the pipeline operates at practically full capacity. Atyrau-Samara represents one of the important links in the close energy relationship between Russia and Kazakhstan. In 2002, Kazakhstan signed an agreement with Russia pledging to export no less than 15 million tons of oil for 15 years through the Russian pipeline system (Kremlin 2002; Nygren 2007, 178). Even so, Kazakhstan's export through the Russian pipeline system is limited by its oil export quota (Oil & Gas Journal 2009b). According to Vitaly Naumkin (2003, 51-52) Russia had a difficult decision increasing the quota because Russian companies feared it would harm their interests. This quota has been increased in steps in the late 1990s and early 2000s (Naumkin 2003, 51-52). According to Tengri News (2012d) the Kazakh Oil and Gas minister stated in 2012 that "This pipe is a key route; so far we don't plan to expand it." However, this route is not as important to Kazakhstan as it might seem and have not been subject to large scale commitment, contrary to the impression in light of expansion and the export agreement. Even if total export through this pipeline has increased since the 1990s, its relative importance as an export route has fallen with the development of other options, especially the CPC pipeline. Kazakhstan's decision regarding the limited development of this export route seems to be influenced by both economic and political considerations.

Atyrau-Samara has some important problems as an export route for Kazakhstan which can be seen in relation with why this export route has diminished in relative importance. The problems can also be seen as reasons for why Kazakhstan has chosen to rather develop other routes. First, Kazakh oil is mixed with heavy Russian oil from Urals and the oil exported as one blend (Lee 2008; International Energy Agency 2010, 514). With no quality bank to adjust the price received according to the quality of oil input, Kazakhstan's high quality oil from Tengiz and Karachaganak receives a lower price when it is exported to markets through Atyrau-Samara. However, most of the oil from Tengiz and Karachaganak are exported through the CPC pipeline. The Atyrau-Samara pipeline therefore relies on supplies from KMG and several smaller producers. Consequently, this is a major economic drawback of this export route.

Secondly, for Kazakhstan this route is problematic since it is controlled by Russia through the Russian state company Transneft. Russia therefore can set the transit price for Kazakh oil exported through this route. This makes Kazakhstan vulnerable to Russian pressure

considering that around 75 percent (2010) of Kazakh oil is exported through Russia, which show that Kazakhstan still depends on transporting its oil through Russia. If the objective for Kazakhstan is to become less dependent on Russia in regard to export routes then the point is to diversify and not increase capacity of Atyrau-Samara or sales to the Russian pipeline system. It is uncertain if Kazakhstan's main reason for not committing more oil through this route is because of political considerations of not wanting to increase export dependence on Russia, or if it is just a matter of poor terms offered by the Russians. Obviously it can be a combination of both.

Nevertheless, this pipeline is important for Kazakhstan. If Kazakhstan is going to be able to export increasing production in the future, then it will need capacity from all routes to have enough. In accordance with the Kazakh government's policy of as many export routes as possible, it makes sense to keep this pipeline operational. At the same time it seems wise for Kazakhstan to cooperating with Russia on energy transport to keep good relations. Even so, it may not be in the interest of Kazakhstan to develop this route beyond its current capacity, without a guarantee to an increased oil export quota, especially considering that Russia and Transneft would probably not prioritize Kazakh oil over Russian, if the capacity on the Russian side is full.

### **5.3.3 Trans-Caspian**

The maritime terminal at Aktau on the shore of the Caspian Sea is one of Kazakhstan's main export hubs, and exports most of the seaborne oil on the Caspian. According to International Energy Agency (2010, 515) 17 percent or about 220 000 bbl/d of Kazakhstan's oil exports in 2009 were transported from Aktau with tankers to Baku in Azerbaijan, Neka in Iran and Makhachkala in Russia. In 2011 this export was 9.3 million tons in total (about 187 000 bbl/d) (KazMunaiGaz 2012). The exports to Russia by tanker are just a small part compared with the Russian pipelines. They do not play a part of differentiation. However, the export to Iran and Azerbaijan plays an interesting part as alternative export routes worth exploring further.

### **Oil swaps with Iran**

In the 1990s Kazakhstan had trouble gaining access to export capacity and was pressured by Russia over export quotas (Kandiyoti 2008a, 186-187). Kazakhstan entered swap agreements with Iran as a solution to gain another export route and more capacity. The volume of this

trade is not large however, at around six to seven million tons of oil a year since the start. The arrangement is beneficial for both countries. Iran gets oil to its northern region and Teheran without having to build new pipelines from the oil fields in the south, thus saving transport costs. At the same time Iran charged a swap fee to sell an equal amount of oil on the world market from the Persian Gulf. Kazakhstan gains one more export route and increases its diversification, and can export for a relatively low cost and gain access to world market prices.

This deal was initiated by Kazakhstan despite pressure from the United States to avoid transport via Iran. American sanctions on Iran are a major problem for this route and lessen the potential for the route to develop into a major export route. The US sanctions on Iran hinder American companies such as Chevron and ExxonMobil who control a large part of Kazakh oil production in selling their oil to Iran (Kandiyoti 2008b, 87). Still, other companies can sell to Iran. Another problem is lack of capacity. This hinders this route to truly help Kazakhstan diversify export routes. In Iran the terminal in Neka has had a capacity of 200 000 bbl/d before 2013, and the maximum amount practical for swap due to refinery capacity is around 500 000 bbl/d (Soligo and Jaffe 2002, 115; Kandiyoti 2008b, 86-87; Azernews 2013). However, Iran is in the process of expanding its capacity. According to International Energy Agency (2010, 513) the capacity currently for Trans Caspian export is 300 000 bbl/d. Kazakhstan's export capacity by sea will increase greatly to 56 million tons (about 1.1 million bbl/d) when the Kazakhstan Caspian Transportation System (KCTS) becomes operational in the future (KazMunaiGaz 2011b). Since KCTS are directed towards Azerbaijan and not Iran this may imply that the oil swaps with Iran will continue to be a small supporting export route. The political and foreign policy gains of diversifying for Kazakhstan through oil swaps are not significant.

### **Kazakhstan Caspian Transport System and BTC Pipeline**

The Kazakhstan Caspian Transport System (KCTS) is a major project to increase export of oil from the port of Kuryk to Baku in Azerbaijan and connect to the Baku-Tbilisi-Ceyhan (BTC) pipeline (KazMunaiGaz 2011b). KCTS is planned to be a system for transport and includes a pipeline from Eskene to Kuryk, maritime terminals at Kuryk and in Azerbaijan and a fleet of tankers transporting the oil across the Caspian. The main oil supply for the pipeline is meant to be future Kashagan production. The initial terminal at Kuryk is going to have a capacity of

760 000 bbl/d, and the KCTS will expand until 2025 to have a estimated capacity of 1.1 million bbl/d (International Energy Agency 2010, 513,517; EIA 2012). To understand this development a perspective looking on the big picture is warranted, and to see it in relation to the BTC pipeline.

When the US supported BTC pipeline became operational in 2005 and the first oil shipped in 2006, Kazakhstan gained a new potential export route (Soligo and Jaffe 2002, 110-112; BP 2013a). The fact that the pipeline has a capacity of one million bbl/d, is privately operated by major IOCs and is designed to bypass Russia makes BTC an important competitor to the Russian pipelines CPC and Atyrau-Samara.

In 2005, Kazakhstan laid official plans to develop a trans-Caspian export route westwards (Socor 2005). The following year Kazakhstan signed a framework agreement with Azerbaijan committing oil supplies to the BTC pipeline (Eurasianet 2006). Kazakhstan then pledged to transport 25 million tons of oil through BTC. However, the plan to export through BTC was not without problems. After a new agreement in 2008, Kazakhstan began to export oil with tankers through BTC in 2008, but broke down in 2010 on tariff disagreements (Trend 2011). The disagreement appears to have been founded on economic considerations. Kazakhstan's oil minister stated in 2012 that this export may start again, "...in case it offers some spare capacities and if the conditions are economically acceptable for Kazakhstan" (Tengri News 2012d). The prospect of exporting large volumes through BTC was also slowed by the delays developing the Kashagan field. These delays spilled over to delay the KCTS at least until 2018 since Kazakhstan does not have enough oil to export large amounts via BTC in addition to other current export routes without Kashagan production (Central Asia Newswire 2010). In the early and mid 2000s BTC probably needed Kazakh oil to fill up capacity and make the project profitable since there was a lack of available oil to the pipeline in Azerbaijan (Soligo and Jaffe 2002, 111-112; Eurasianet 2006). However, from 2005 to 2009 Azerbaijan over doubled its oil production, so this point might be less applicable from 2009 (Ciarreta and Nasirov 2012, 284-285). This development can be seen in relation to the tariff disagreements since increased oil production gave Azerbaijan a stronger position with lesser need for Kazakh oil to fill BTC. Still, in the long term, Azerbaijan will probably need Kazakh oil to operate the BTC pipeline because of much lower reserves compared to Kazakhstan, as seen in Table 2.

From a political and foreign policy perspective Kazakhstan's commitment to the BTC, and the development of KCTS, is strengthening Kazakhstan's multi-vector foreign policy. By developing a large export route westwards and bypassing Russian control and influence, Kazakhstan gains a real diversification of export routes if the KCTS's full potential is realized. A result of this would be that the high share of exports transit from Kazakhstan through Russia will decline from 75 percent (2010), and thus reduce transport dependence on Russian export routes. The view of Torjesen (2009, 7), that Kazakhstan with these actions have gone against Russia's wishes and interests, seems to be a fair assessment. Kazakhstan has followed its own interests and at the same time accommodated the United States, Japan and European countries interest in the BTC pipeline which is represented by their respective IOCs. An important part of this is that the IOCs of Eni (Italy), Total (France), ConocoPhillips (US) and Inpex (Japan) who are operating on Kashagan also own a stake in BTC, and therefore have an interest in exporting Kashagan oil through this route<sup>35</sup>. These developments and findings shows that Kazakhstan is not fully in Moscow's influence, but has room for maneuvering and balancing Russia with the United States and European countries. A key point here is that this shows that Kazakhstan not only talks about conducting a multi-vector policy, but also is able to implement it in practice. The issue of trans-Caspian transport will be further discussed under alternative export routes regarding the proposed pipeline crossing the sea.

### **5.3.4 Caspian Pipeline Consortium**

When the Caspian Pipeline Consortium (CPC) started pumping oil in 2001 it was a major change in the oil export situation of Kazakhstan. It was the first new export pipeline built from post-Soviet Kazakhstan and unlocked the potential for export of Kazakh oil to the world market. The project was developed in cooperation between the governments of Russia, Kazakhstan, Oman and a consortium of IOCs<sup>36</sup>. From 2001 CPC gave much needed export capacity for Kazakh oil. Already from 2004 CPC was at full capacity at 28.2 million tons a year, and from 2005 it increased by improving flow to 35 million tons a year (CPC 2013b). Most of the oil transported comes from Tengiz and Karachaganak.

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<sup>35</sup> See Tables 4 and 5 for full information.

<sup>36</sup> See current ownership structure and data in Table 5.

For Kazakhstan both economical and political considerations were central concerning development of CPC. The building of CPC can be seen as a practical solution for the need of expanded capacity related to increased production from oil fields in Kazakhstan. At the same time it can be seen as a pragmatic compromise between the interests of Kazakhstan, the United States and Russia. Kazakhstan wanted more pipelines for capacity and diversification of export routes. The United States supported these goals to get more oil to the world market and to reduce Russian control over the export routes. However, Russia wanted transport through Russia and to gain economic gains from transit. The CPC pipeline realize Russian ambitions by transporting oil through Russian territory, having overall control with the project and receive transit and port fees (Kandiyoti 2008a, 188). In this context CPC can also be viewed as a concession made by Kazakhstan to Russia (Kandiyoti 2008a, 189). The point being that Kazakhstan accepted that it had to develop one pipeline through Russia while they searched for other export route options.

Being the only partly privately owned oil pipeline on Russian soil, CPC represents a diversification for Kazakhstan and foreign IOCs from the state run Transneft Russian pipeline system. Regarding ownership in the consortium, by making the pipeline private Russia has then less control over it, compared with the state monopoly. Even so Transneft and the Russian state still have a major share of 31 percent in the CPC pipeline and have influence over it. Russia increased its share from 24 percent to 31 percent by acquiring Oman's share in CPC in 2008 (Upstream 2008). In 2009, BP sold out of CPC as well by selling its share in LukArco to Lukoil and BP's share in Kazakhstan Pipeline Ventures to KazMunaiGaz (BP 2009). Consequently, the consortium has moved toward more ownership by the Russian and Kazakh governments. Even if Russian and Kazakh ownership has increased in CPC, it does not necessarily result in more political control of the pipeline. An increased share will only have economic returns as long as the CPC is operated by consensus. Nevertheless, Russia has been moving for a change in the structure of CPC from consensus to majority vote, where larger ownership gives more power (Dellecker 2008, 17). If Russia succeeds to promote this change in management, they could potentially gain more control over CPC in the future and consequently reduce CPC's effect as a diversification to the Russian state controlled Atyrau-Samara route for Kazakhstan.

Kazakhstan's choice of developing CPC can be seen in relation to problems with Transneft in the mid and late 1990s in a context of low oil prices, when Transneft granted only limited



access to Tengiz oil through the Atyrau – Samara pipeline (Cuk and Feiveson 1998 cited by Kandiyoti 2008b, 79). This problem with export capacity can also be linked with development of production. Because of the low available export capacity before 2001, Chevron<sup>37</sup> (US) had to scale back on its investments in Kazakhstan (Kandiyoti 2008b, 79). Delays in the CPC capacity can therefore have slowed development of oil production in Kazakhstan because of lack of export capacity (Dellecker 2008, 14; Kandiyoti 2008b, 80).

Events regarding development of CPC point to the difficulty of Kazakhstan and IOCs in being dependent on transit through Russia. Early on in the process to develop the pipeline there was problems with coming to terms with Russia. The negotiations with Russia lasted from 1992 to 1996, then a technical evaluation received final approve from Moscow in 1998 (Olcott 2010, 260). The slow process and Russian interference in developing this private pipeline may have strengthened the interest of the United States and Kazakhstan in the BTC pipeline (Olcott 2010, 260).

According to Olcott (2011, 111) Transneft stalled the construction of the CPC pipeline in the early 1990s so that construction did not begin before 1993. Again in the late 1990s Russian authorities slowed the project delaying of permits and rights (Cuk and Feiveson 1998 referred to in Kandiyoti 2008b, 80). These actions can be seen in the context of low oil price on the world market and the Russian interest to protect other Russian ventures (Olcott 2011, 111). It is difficult to understand the actions of Transneft and Russia from an economic perspective (Dellecker 2008, 15-21). Russia loses transit revenue by delaying CPC therefore it must be seen in a bigger political picture. CPC transports Kazakh oil, not Russian, so for Russia the goal of gaining stronger control over CPC could increase their influence and control over Kazakhstan and production projects in Kazakhstan. Russia's actions in this matter seem opportunistic in the way they promote national interests. The delay related with the construction is not the only stalling by Russia and Transneft.

Phase II of the project was envisioned in 1998, but the shareholders in consortium did not agree on the expansion until 2008 (CPC 2013c; CPC 2013b). The expansion meant a capacity of 65 million tons a year by 2015. Several factors contributed to the slow process of reaching agreement on building and expanding the pipeline. CPC operates by consensus. In practice this means that one actor may pressure the others to give in to demands before consensus is

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<sup>37</sup> Chevron has a stake in Tengiz (50%) and Karachaganak (18 %), see Table 3.

reached. Regarding the expansion Russia demanded change in tariff, lower interest rate for the consortium from operating companies, change in management and financial issues (Dellecker 2008, 13-14). Russia was in a good position to pressure Kazakhstan and the IOCs on the CPC project because Russia had time to wait while Kazakhstan and the IOCs, with plans to increase production of oil in Kazakhstan, had to get access to capacity relatively fast. Russia's opposition to the expansion officially came also from concerns about low return on investment and adding too much volume to pass through the Bosphorus (Upstream 2008). The problem is that the Bosphorus is very narrow and Turkey have set limits on shipping do to environmental concerns and fear of accidents (Kandiyoti 2008a, 140-141). The strait is as a result a real bottleneck and delays transport. The process of expansion of CPC was slowed by the consortium waiting for a clarification on the prospect of the Burgas- Alexandroupolis pipeline<sup>38</sup>, which was meant to bypass the Bosphorus and hinder increased pressure on the strait (Babali 2009, 1301). Russia decided to withdraw their claims in the negotiation in the summer of 2008 after the consortium came to agreement on raising tariff and halving interest rate on loans to CPC (Upstream 2008). The final decision to expand also came after Russia, Greece and Bulgaria signed an agreement in 2007 regarding the Burgas- Alexandroupolis pipeline and thereby reduced the worry of troubles relating to the Bosphorus (RIA Novosti 2007). However, Bulgaria stopped construction of the project in 2010 because of ecological reasons, and withdrew from the project in 2011 (RIA Novosti 2010b; RIA Novosti 2011b). Nevertheless, the CPC expansion went forward from 2008.

### **5.3.5 Kazakhstan-China Oil Pipeline**

The Kazakhstan-China pipeline (KCP) represents a major development in Kazakhstan's pursuit of diversification of export routes in accordance with its multi-vector approach. With a pipeline operational Kazakhstan could increase their exports of oil to China from smaller amounts of about one million tons a year by rail to the far more significant 10 million tons a year from 2006 (Kandiyoti 2008b, 79).

The project started with an agreement between Kazakhstan and China on September 24 1997 regarding cooperation on oil and gas and the building of a pipeline from western Kazakhstan to the Xinjiang province in western China (China View 2006; KCP 2013). Later in 2004 China National Petroleum Corporation (CNPC) and KMG signed an agreement on the main

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<sup>38</sup>This is a project to build a pipeline from Burgas in Bulgaria to Alexandroupolis in Greece to bypass Turkey.

principles of the construction of the Atasu-Alashankou pipeline<sup>39</sup> (KCP 2013). Construction was done in phases and with CNPC having the responsibility of construction and finance the project (International Energy Agency 2010, 517-518)<sup>40</sup>. The first phase (the most western part of the pipeline) was complete in 2004, bringing oil from Aktobe and CNPC controlled fields westward to Atyrau. However, for this pipeline to be able to supply China its direction of flow needed to be reversed. The second phase from Atasu in eastern Kazakhstan to Alashankou in western China was completed in December 2005 and fully operational in 2006 (EIA 2012; KCP 2013). According to President Nazarbaev's speech at the opening ceremony the cost of the pipeline was US \$800 million (KCP 2013). From 2006 this part of the pipeline exported oil to China mainly from the Kumkol fields, in which CNPC has shares, and Russian oil via the Omsk-Pavlodar pipeline<sup>41</sup>. The third phase of the KCP connects the two first parts between Kenkiyak and Kumkol and was completed in 2009. The final pipeline can export Kazakh oil to the Chinese market and is currently being upgraded to a capacity of 20 million tons a year<sup>42</sup>, which is its designed capacity (China View 2006; KazTransOil 2013a). The refineries at Pavlodar and Shymkent in eastern Kazakhstan can potentially be supplied with oil pumped through the Kazakhstan-China pipeline.

During the development and planning of KCP there were problems with securing enough Kazakh oil for export through the pipeline to make maximize the benefit (Paik 2012, 290-293). The solution had two parts. First, Chinese companies such as CNPC bought several Kazakh energy assets and fields during the 2000s, and then used this production to export to China. Second, Russian oil also became necessary to fill the pipeline. This was solved with an agreement of export of Russian oil signed in 2007 (Paik 2012, 293-294). The large Chinese presence in the Kazakh oil and gas projects and fields, as discussed earlier, can therefore be seen in relation with the development of the Kazakhstan-China oil pipeline.

The fact that the KCP can supply the refineries of Pavlodar and Shymkent with Kazakh oil instead of being reliant on Russian imports can potentially make Kazakhstan more independent regarding energy supply. This demands that there is enough Kazakh oil for both the refineries and export to China, which is not certain. In 2011, Pavlodar received Kazakh oil for the first time, but is still reliant on Russian oil to operate (Tengri News 2012c).

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<sup>39</sup>It is also called the Kazakhstan-China oil pipeline since this is the export part of the final pipeline.

<sup>40</sup> See Table 5 for data on the pipeline.

<sup>41</sup> The two pipelines meet at Atasu, see Map 2.

<sup>42</sup> Equals about 400 000 bbl/d.

For Kazakhstan the choice of developing this export route has both economic and political considerations. The Kazakhstan-China pipeline provides Kazakhstan with more export capacity for its oil, and simultaneously provides China with a steady supply which is important for its western region. Strictly economically speaking, it is not attractive to transport oil over 2200 km from western Kazakhstan to China because of transport costs (International Energy Agency 2010, 518; KazTransOil 2013a). That said, since China took responsibility for financing and constructing the pipeline, the costs of this export route for Kazakhstan are reduced. China is willing to invest in an expensive transport infrastructure to transport oil directly to its border, and thereby secure supply of oil. The difference between this export route and the other pipelines is that this one exports directly to China and is not a part of the world market. Since Kazakhstan through this pipeline is committed to sell oil to China, it may be in a more vulnerable position in possible future negotiations on price. From the other perspective this vulnerability is reduced by Kazakhstan's development of multiple export routes, as long as Kazakhstan has spare capacity to shift oil away from China in the case of being offered poor terms and price.

Both countries clearly have political motivations for developing this pipeline. For China a direct oil pipeline from Kazakhstan serves its energy policy and enhances its energy security by gaining direct transport over land and lessens their dependence on international seaways (Shaffer 2009, 50-51). This security of supplies is enhanced by the fact that the oil supplies for the pipeline comes from fields controlled by Chinese companies such as CNPC. For Kazakhstan a new export route directly to China helped diversify its export routes and thereby lessens dependence on Russia. Kazakhstan through this pipeline has also been part of trying to develop a mutual dependency relationship with China. In the asymmetric relationship of Kazakhstan-China relations a move toward mutual dependency of oil exports and oil supplies favor the smaller Kazakh state. Kazakhstan also has political motivations for developing the KCP regarding balancing foreign influence. By giving China a major stake in Kazakhstan's export infrastructure, China will be more interested in the stability and future of its neighbor. For Kazakhstan the Chinese can be counterweight to the Russian interest in export through CPC and Samara pipelines. This pipeline is a key development by Kazakhstan in pursuit of the goals of the multi-vector policy. It has also contributed to moving toward a mutual dependence relationship between Kazakhstan and China.

### **5.3.6 Alternative Export Routes – Why not these?**

These alternative routes have not been chosen by Kazakhstan to be developed in the period up to 2012. Reasons for this seem logical as these export routes have major obstacles to be solved before they can be fully developed. Each route and its problems are discussed in turn.

#### **Kazakhstan – Turkmenistan - Iran**

An oil pipeline from Kazakhstan to Iran via Turkmenistan has been discussed but has not yet been developed, and probably will not for some time because of American sanctions (RFE/RL 2008). Kazakhstan has been positive about building this pipeline, which makes sense since this is the shortest and cheapest route (New York Times 2001; Babali 2009, 1302). In 2003, foreign minister Tokaev stated that “We do not exclude the possibility of constructing the pipeline which will go to Iran”(Tokaev 2003, 4). There is also the issue that Kazakhstan had not enough oil to supply Europe through Russia and China at the same time as Iran, at least up until late 2000s. However, this could change if the estimated production increases for 2015 and later are realized (RFE/RL 2008).

If relations between the United States and Iran improve and the sanctions are lifted this route is still problematic from the perspective of the United States and other oil importing countries such as Japan, France and Britain. If Kazakhstan increases export through Iran with a pipeline, more oil will flow through the Strait of Hormuz, as discussed above. Such a development would go against efforts to increase diversification and energy security for the United States, China and Europe making the Strait of Hormuz even more important for oil transport than it already is (Yergin 2011, 59). With its pragmatic multi-vector foreign policy Kazakhstan is probably cautious to not alienate American and European energy interests by developing this export route. These points can also be valid for the oil swaps, if it reaches larger volumes. Political considerations seem to have been important to the outcome, and may have overshadowed economic considerations to Kazakhstan’s decision in this case. This finding supports the view of Stevens (2009) and Gulliet (2011) on the importance of politics in relation to development of pipelines. Still, this needs to be researched further to be more certain.

## **Kazakhstan – Turkmenistan – Afghanistan- Pakistan - India**

This oil pipeline route has been considered and proposed as an alternative to Iran by reaching the Indian Ocean and south Asia from western Kazakhstan, with access to the world market by tankers (RFE/RL 2002). Insignificant progress has been made in regard to develop this route because it has major political problems. First, the political stability and security in Afghanistan are far from what is required of this long term and expensive project. The second problem is related to economics. Since the route will be very long approximately 4000 km, it will be expensive to develop (RFE/RL 2002). Considering the importance of political stability argued by Stevens (2009, 17), as long as Afghanistan remains politically unstable both investors and Kazakhstan will probably not commit to develop this route. Political considerations seem to have clearly influenced the decision to not develop this route.

## **Pipeline Crossing the Caspian to Azerbaijan**

A trans-Caspian oil pipeline from Kazakhstan to Azerbaijan and connecting to the BTC pipeline would be a big step to diversify export routes and increase export capacity. Kazakhstan has worked to be able to develop this pipeline. In 2009, Kazakhstan signed an agreement with France to build a pipeline crossing the Caspian Sea to Baku (Oil & Gas Journal 2009a). France's interest and push forward in this matter can be seen in relation to security of supply through more export routes for Kazakh oil and with the French IOC Total's stake in BTC, Kashagan and other fields.

This pipeline is an alternative to the Kazakhstan Caspian Transport System (KCTS), but the pipeline has major obstacles ahead that hinder its development and its chance for being built. The unclear legal status of the Caspian Sea makes it very difficult to develop this pipeline because Russia and Iran are strongly opposed to this pipeline and have stated that all five littoral states must agree on such a pipeline (International Energy Agency 2010, 516-517). Iran's and Russia's view is consistent with their interest in securing transport of energy through their own territory, and are opposed to being bypassed. A pipeline would be economically more cost-effective than tankers as the planned part of KCTS (Socor 2006). Even if economic considerations push for this development, the political considerations for Kazakhstan have been strong against, which makes the prospects for this pipeline uncertain as long as the legal issues of the Caspian Sea are not resolved. It seems more likely that Kazakhstan will continue developing KCTS as planned, since tankers gives no legal problems

and are harder for Russia and Iran to hinder, even if Russia and Iran do not subscribe to this solution either.

### **5.3.7 Gas Export and Gas Pipelines**

Export and export routes for gas are less central than oil regarding Kazakhstan's multi-vector foreign policy. With relatively low production and reserves of gas combined with government ambitions for gasification and increased domestic consumption. This makes gas less important and effective to be used politically through choice of export routes. This does not imply that gas is insignificant. The case of Karachaganak shows that gas is a significant part of the development of energy projects and export, and has foreign policy considerations.

Kazakhstan's role as a transit country for Uzbek and Turkmen gas is interesting to see in light of multi-vector. Kazakhstan is connected to its neighbors through pipelines transporting gas from Uzbekistan and Turkmenistan to Russia and China. The agreement with Russia and Turkmenistan from 2007 to build a new gas pipeline along the coast of the Caspian to Russia can be an example of Kazakhstan's pragmatism and balancing. This pipeline can be seen as supporting Russia's interest in controlling transport and export of gas, but also giving Kazakhstan revenue from transit fees. Just the year before Russia had been bypassed by two major oil projects by Kazakhstan, after Kazakhstan's commitment to BTC oil pipeline and the Kazakhstan-China oil pipeline becoming operational. Playing along with Russia on the issue of gas was probably important for Kazakhstan to balance and not challenge its strategic partner regarding energy. However, the postponement of the project brings uncertainty to when it will be developed.

The building of a more extensive domestic gas transport system to gasify Kazakhstan can play a role in pursuing multi-vector goals of state security and autonomy. The Kazakhstan-China gas pipeline and the Beineu-Shymkent pipeline are important developments by Kazakhstan and crucial for the goals of gasification and diversification of export routes. Through this system Kazakhstan will be able to increase supply to domestic markets and create an alternative export route to China in addition to the old gas export route through Russia. By making Kazakhstan less dependent on gas imports from Russia and Uzbekistan to the south and east, Kazakhstan will be less vulnerable to pressure. The substantial Chinese investments in these gas pipelines are evidence of China's important role as a partner for Kazakhstan in developing and exporting its resources.

### 5.3.8 Thoughts on Development of Export Routes

Kazakhstan's situation has gone from full dependence on Russian export routes in the 1990s to become more diversified in 2012 through development of multiple pipelines and export routes. After exploring the individual export routes available to Kazakhstan there are several findings regarding choices in development of export routes in relation to the multi-vector policy.

The development of new major export routes was mainly done in the 2000s, with the first being CPC in 2001. This can be understood in relation to the economic sense of building new capacity to meet increased production that came online and was planned in the 2000s. In addition, the transit troubles with Russia in the 1990s showed the need for Kazakhstan to develop alternatives to Russia.

Kazakhstan's choices in development and investments appear to have been based on both economical and political considerations. The economic need for expanded export capacity and revenue has been compromised with political balancing between foreign states, the quest for multiple pipelines and mutual dependence relationships. The choice of the expensive options of developing multiple routes in different directions is a testimony of how important foreign policy and political considerations are in the process. Furthermore, the economic and political considerations go hand in hand on this issue since multiple routes will protect Kazakhstan against artificial low prices on its commodities. Kazakhstan has moved from Russian dependence towards mutual dependence, which reduces the danger of the energy weapon used against it by a near monopoly trade partner. This find is in line with the argument of Shaffer (2009) as discussed in Chapter Two, which applies to Kazakhstan. This is especially relevant for Kazakhstan considering its landlocked position and asymmetric power relationships with Russia and China. A choice of only developing the Russian route, for example, would have given lower short term cost of building and development, but would be exposed to the longer term costs and insecurities. The choices of Kazakhstan seem rational given its landlocked situation, which demand that Kazakhstan cooperates with its neighbors on energy transportation.

Kazakhstan's balancing and multi-vector approach to foreign policy is mirrored in development of export routes. In the new important export projects in the 2000s Kazakhstan has given each of its three main strategic partners the United States, Russia and China a stake



in its exports and not overlooked their interests. First, Kazakhstan's commitment to BTC, the KCTS and private ownership of CPC accommodated US interest. Second, Russia gained some by partial control and transport through Russia with CPC, oil export agreements and agreement with Kazakhstan on the new transit gas pipeline from Turkmenistan. Lastly, China was favored with both an oil pipeline and a gas pipeline from Kazakhstan. The increasing export to and investments from China moves Kazakhstan's and China's relationship towards mutual dependence. Kazakhstan needs access to China's market and investments, while China needs a reliable energy supply. A move towards mutual dependence can also be valid for Kazakhstan's energy relationship with Russia. Developments in the Kazakh-Russian energy relationship point in this direction. Kazakhstan has become less dependent on Russian transport for energy. The two countries have shown that they can cooperate for mutual benefit through cooperation on energy issues as production from fields in Kazakhstan and refineries.

Pipeline politics, political issues and considerations seem to have triumphed over economical consideration in alternative routes that were only partly developed or not at all. This finding gives support to the views of Stevens (2009) and Gulliet (2011) on the importance of political agreement for development of pipelines and of the limits of alternatives imposed by politics, as discussed in Chapter Two. The best example is the lack of a pipeline to Iran which would have made great economic sense. This also applies to the trans-Caspian oil pipeline to Baku. Political considerations may have influenced Kazakhstan's decision to develop an export route.

However, Kazakhstan's effort to diversify its export routes of energy is not fully achieved. Transport through Russia is still the dominant export route for oil and gas, and was 75 percent in 2010 (RIA Novosti 2011a). This situation may be further secured when phase II of the CPC pipeline becomes operational in 2015<sup>43</sup>. On the surface it may seem as Kazakhstan has chosen Russia as its dominant export route. However, this situation may be just a transitional phase for Kazakhstan. A major reason why Kazakhstan has not been able to diversify more of its exports is a lack of sufficient oil supplies to export significant amounts in multiple directions. With a production of 1.84 million bbl/d in 2011 there is little volume available for the trans-Caspian route and other alternatives considering that CPC, Atyrau-Samara and KCP are at near full capacity and does not have enough capacity to cover Kashagan (Campaner and Yenikeyeff 2008, 9). Since it is more economically efficient to transport at full capacity from

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<sup>43</sup> See Table 5.

some routes than disperse the same volume on more routes, Kazakhstan has to wait for the delayed Kashagan project to become operational before exports bypassing Russia can rise. With Kashagan's maximum future production of 1.2 million bbl/d, Kazakhstan can more effectively diversify its exports of oil. This is linked to the planned development of the KCTS transporting oil to Baku in Azerbaijan and BTC. The delay of Kashagan may have weakened Kazakhstan's degree of diversification of export routes in the period examined. Nevertheless, Kazakhstan need all available export capacity developed if it wants to transport future increased production.

## **5.4 The Role of Energy in Multi-vector**

It is notable that the Kazakh government has communicated so openly its strategy in conducting its multi-vector foreign policy and regarding energy policy of development of export routes. This openness has been followed up with actions and development in line with public policy, as highlighted in this thesis. This fact makes it very clear to see that Kazakhstan has followed a multi-vector foreign policy and it is difficult to conclude otherwise. It also explains the consensus on this issue in the literature.

After having explored the energy sector in Kazakhstan empirically there are clear signs of a close and interlinked relationship between energy resources, politics and foreign policy in the case of Kazakhstan. It is not only that the state institutions make decisions regarding its natural energy resources, but also that these decisions appear clearly influenced by political and foreign policy considerations. Political considerations seem to have been important for Kazakhstan's choices in how to develop its oil and gas resources and in the development of pipelines and export routes. Examples are the diversification of IOCs and NOCs partners in developing oil and gas projects and development of oil and gas pipelines to China. These findings support the views of Shaffer (2009) and Ostrowski (2010) on the close relation between energy and politics.

By developing the energy resources by inviting companies from many different countries, with the majority from the United States, Russia and China, Kazakhstan has managed to balance foreign influence, hinder dependence on any one actor and thus gain autonomy. European IOCs also play an important part here as intermediaries, by decreasing the substantial Russian and Chinese share of the oil and gas sector. The balancing act between the

three major powers is reflected in how Kazakhstan has developed export routes for energy as well. As discussed earlier, Kazakhstan has developed or is in the process of developing three main export routes which each have support from the United States, Russia and China. Kazakhstan can balance between the big three foreign powers by having one pipeline or export route which each supports their interests. These three are: CPC, Kazakhstan-China pipelines and KCTS with links to BTC. This development is a sign of Kazakhstan's multi-vector approach in regards to energy resources.

The data point in the direction that Kazakhstan has developed its oil and gas resources by building partnerships with multiple partners and export routes in multiple directions. Kazakhstan has developed its energy resources with a multi-vector approach which mirrors and can be seen in relation to the country's multi-vector foreign policy. This supports the findings of İpek (2007) as presented in Chapter Two. This also points to the direction that oil and gas resources have played a role as a tool for Kazakhstan, to be used to achieve the goals of the multi-vector policy. The findings point towards three main vectors which are more important than the others to Kazakhstan in energy development, energy export, and the multi-vector foreign policy.

The first and most important vector is Russia with its presence in field development, but foremost in its strong position as Kazakhstan's most important export route and for refinery capacity. Kazakhstan's continuing dependence on Russian pipelines for transport and export, for example, in relation to Karachaganak and the CPC pipeline, show that Russia is still Kazakhstan's most important vector and partner in energy and foreign policy. Russia and Kazakhstan's energy relationship seems to have moved toward mutual dependence, as Kazakh dependence has been reduced and cooperation between the two has increased. Kazakhstan has played along with Russia for the most part in energy issues, but has taken important steps and decisions against Russian interest and Russian pressure on several occasions from 2000. Notable decisions against Russian interests are: to commit to oil export through the BTC pipeline in 2006, the building of oil and gas pipelines to China, through no Russian energy companies involved on the major project Kashagan and giving just a small share of five percent of Tengiz. Russian interest in Kazakhstan exporting as much as possible through Russia have only partly been accommodated by Kazakhstan from the mid to late 2000s when export to China and through Azerbaijan increased. The evidence examined give

support to the view of İpek (2007), for Kazakhstan the relationship with Russia is important for the development of the energy resources.

The second vector is China. China's strong presence in field development and production of oil, with both oil and a gas pipeline to China, show that Kazakhstan's large eastern neighbor has developed from 1997 to become a crucial partner in addition to Russia. Development of energy export pipelines to China contributed toward a mutual dependence relationship between the two states. This is favorable to Kazakhstan since it gives an opportunity to balance between China and Russia in foreign policy as well as differentiation of export routes and more export capacity. However, there is some evidence pointing in the direction of China's companies being excluded from the major oil projects, such as Kashagan. Kazakhstan seems to be wary of China gaining too much influence over its energy resources. However, this needs to be researched further to gain more evidence.

The United States is the third vector, and is important to Kazakhstan. The crucial American involvement in the development of oil and gas resources in Kazakhstan is reflected in their sizeable presence in Kazakhstan's largest fields of Tengiz, Karachaganak and Kashagan. In addition, there are American IOCs present in the consortiums operating the pipelines CPC and BTC transporting oil west. The importance of American companies to national security, as stated by President Nazarbaev and foreign minister Tokaev, is a clear evidence of Kazakhstan having political considerations behind how to develop its energy resources and the importance of keeping American interests present. Kazakhstan has managed in its first 20 years as a state to give each of the three great powers a stake in Kazakhstan's oil and gas sector, and thus balanced between them. Kazakhstan's aim to develop strategic partnerships as part of its multi-vector foreign policy is clear in relation to oil and gas with the strong involvement of China, Russia and the United States from 2000. The connection to multi-vector in the 1990s is still valid. However, the United States, Canada and European countries were more favored in the 1990s than China and partly Russia.

There are objections about viewing Kazakhstan's energy resources as a tool for its multi-vector foreign policy. Firstly, if Kazakhstan is to be able to use its energy resources by diversifying partners in development and by diversifying export routes, it then demands that there are energy assets and projects not yet developed to be distributed between partners. The situation in 2012 is that Kazakhstan has sold the rights to develop most of its oil and gas resources and at the same time the state control an increasing share through KMG. This

evolution has developed through the 2000s, and has led to Kazakhstan having fewer projects to attract foreign investments with in 2012. This is a clear sign that Kazakhstan is becoming a more mature petroleum producing country.

The same analysis applies to pipelines with their long term commitments. Kazakhstan has as of 2012 already developed several export routes, and consequently has less to offer in future negotiations since the need for additional export pipelines is reduced. One reason for this is that existing pipelines such as CPC and Kazakhstan-China will be expanded, and thus reduce the need for new pipelines. However, the effect of Kazakhstan's past decisions remains since the partnerships with foreign oil companies and the partnership with transit states for its export pipelines is long term. The prospect of inviting new partners using energy resources is however reduced. Energy as a tool in multi-vector may seem to be best suited for the 1990s and first half of 2000s, from the perspective that the energy assets as a bargaining chip have been exhausted. From this perspective Kazakhstan has sold away or is consuming its strategic assets of energy, as it used the nuclear arsenal dismantlement in the 1990s to start a partnership with the United States. From the perspective of energy playing a long term role in multi-vector also after it has been developed suggest that energy's role as a tool is relevant in the whole period to 2012, and still may be in the future. While both perspectives have some merit, a middle ground is more fruitful to follow. Resource nationalism and KMG have reduced the potential for using the energy resources as a tool in the multi-vector policy, but only to a degree. Regarding energy as a tool, at first decisions on projects and investments are done once while the effects are lasting. However, as the case of Chinese interest in buying rights to Kashagan show, when contracts and rights are sold and rewritten it opens up more separate government decisions and possibilities to use energy as a tool.

Secondly, the nature of energy as a tool in Kazakhstan's case is indirect. When Kazakhstan uses energy resources as a tool to balance foreign influence it works indirectly and gives an indirect effect by gaining autonomy and security for Kazakhstan. Hypothetically, Kazakhstan could use its energy resources directly as an energy weapon by choosing to stop oil export to one transit country and favor another. However, in practice this is not possible. Three reasons are: Kazakhstan's vulnerable landlocked position, the lack of export options and reliability. Kazakhstan is dependent on revenues from energy export, and does not have enough spare capacity to close operating pipelines. Since Kazakhstan needs to cooperate with its neighbors to transport its energy, it cannot be seen as an unreliable partner. Using the energy weapon

only once or twice will hurt Kazakhstan's reliability in the eyes of investors and foreign partners, which may lead to Kazakhstan losing its partners. Russia is in a much stronger position, as a key transit country for Kazakhstan, and could close its pipelines to Kazakhstan if it wanted to. However, this is unlikely since both countries have a strategic partnership and mutual interest in keeping the oil and gas flowing. Since Kazakhstan's use of its energy is indirect in relation to multi-vector and foreign policy, options for how to use energy is limited. Nevertheless, Kazakhstan's indirect use is an example of a state tool that is not aggressive, and stands in contrast to the energy weapon. This difference is important to keep in mind.

Thirdly, the relationship of energy resources as a tool for Kazakhstan's multi-vector policy has some uncertainty tied to it. Even if there is a close relationship between energy and multi-vector as argued by Shaffer (2009), a timely question is if the roles can be the other way around, meaning that foreign policy and multi-vector is a tool to help develop Kazakhstan's economy and its energy resources. This perspective follows the argument by Hanks (2009, 264), that the need to develop production and export routes has driven the multi-vector policy. This perspective has some merit since Kazakhstan's foreign policy has played an indispensable part in development its energy resources and to secure export routes. Foreign policy negotiations have been required to secure long term agreements and understanding with transit countries which is necessary to be able to develop export routes from a landlocked position. Diplomacy was therefore important to secure the development of the CPC pipeline, the trans-Caspian route and the pipelines to China. Foreign policy has also helped Kazakhstan unlock new energy resources for development, such as the agreement with Russia in 2002 on delimitation of the Caspian Sea which opened up Kazakhstan's Caspian oil and gas potential. Foreign policy and energy can therefore possibly be a tool for the state in the pursuit of national interests and the goals of the multi-vector policy.

The implication of the flexible relationship between energy and foreign policy of Kazakhstan is that energy may be a driver for its multi-vector foreign policy, following Cummings (2005), Hanks (2009) and Sorbello (2011). This view is based on that the needs of energy development and diversification of export routes drove Kazakhstan's multi-vector policy. Energy as a driver perspective runs in to a problem of finding the most significant independent variable driving multi-vector. There are two main possibilities. Is it the state's goals of state security and autonomy that drives multi-vector to secure the state and through it

development of energy resources? Or is it the goal of economic development and development of energy resources that are the main driver? The former have an overweight of political considerations. The latter have more economic considerations in how to develop Kazakhstan's energy resources. Since Kazakhstan seem to follow both economic and political considerations in the development of its energy resources, it may be a sign that the relationship behind multi-vector is complex and possibly driven by all state interests, not only energy and economic development. More research and more evidence are needed to explore this further. However, the findings presented here suggest that political considerations have been important and in some cases crucial in relation to development of export routes. Economic considerations have given the need for export capacity, while political considerations have been important for Kazakhstan in choosing which export routes to develop. Based on the empirical findings presented it seems necessary to research if energy has a stronger role as a tool than a driver for Kazakhstan's multi-vector policy, or if the strength of the relationship is vice versa.

Furthermore, there is not clear evidence in this study of energy being a trigger for foreign policy in Kazakhstan's case which does not give support to the argument by Sorbello (2011), as discussed in Chapter Two. This point derives from the logic that energy has to be a driver with decisive influence to be a trigger. Even if energy may have influenced foreign policy, such as in the negotiations regarding delimitations, it seems too strong to call energy a trigger without further evidence. This is an interesting perspective worth exploring further. However, the data and time needed to study this in depth is beyond the scope of this thesis.

# 6 Concluding Remarks

## 6.1 Main Findings and Conclusions

This thesis has explored both the relationship between Kazakhstan's oil and gas resources and its multi-vector foreign policy, and how energy resources of Kazakhstan have been used as part of the multi-vector policy.

As I have shown in this thesis, there is a close relationship between Kazakhstan's energy resources and its foreign policy. They mirror each other through general patterns in Kazakhstan's development of energy projects, and through the development of multiple export routes in different directions. The mirroring approach is also clear by looking on Kazakhstan's strategic partnerships with Russia, the United States and China in the multi-vector foreign policy which are the same three main vectors and partners in development of its oil and gas resources. Kazakhstan has balanced between the three great powers both in development of oil and gas, as well in export routes by favoring development of three pipelines that supports their interest. Kazakhstan has developed its resources in accordance with its pragmatic multi-vector policy. Kazakhstan's status as landlocked seems to be an important consideration for understanding Kazakhstan's decisions regarding energy and foreign policy. This status makes Kazakhstan reliant on pipelines for energy export and makes pipelines a vital issue in regard to energy development.

Here it is found support for the view that oil and gas resources have been used as a tool in the multi-vector policy in two main ways, in diversifying foreign interests and companies in development of the resources and through the development of multiple export routes for energy. Through use of these two approaches regarding investment decisions Kazakhstan has progressed toward reaching the goals of the multi-vector policy, and limit foreign influence by balancing against Russia, the United States and China. It is important to be aware that these goals have been pursued in a closely connected manner in regards to both economics and politics. Kazakhstan has moved from being fully dependent on Russia for exports toward more diversified export routes, and toward an energy relationship of mutual dependence with both Russia and China. However, Russia still has a strong position as Kazakhstan's main export route for energy.



There is evidence that support that Kazakhstan's energy resources can play a role as a potential tool that can be used for promoting national interests. At the same time there is also some support for the view of energy as a driver for Kazakhstan's foreign policy by influencing foreign policy decisions. Kazakhstan's development and investment decisions appear to have been based on both economic and political considerations which point toward that energy may have a role both as a tool and a driver. Political considerations seem however to have played an important role in hindering development of several export route options, and seem to have been important regarding decisions to sell development rights to foreign companies. The empirical findings presented here point in the direction that the role of oil and gas resources as a tool seems stronger in relation to Kazakhstan, than the role as a driver. Still, there is uncertainty on the relative strength of these roles in comparison to each other for Kazakhstan and in general. Because of the limits of the research design I cannot however state the strength of this relationship with certainty. However, the evidence on energy's role suggests that the relationship between energy and foreign policy might be interdependent, as energy can influence and be a tool for foreign policy. These findings, relationships and issues needs to be explored further by researchers and scholars. Given the close relationship between energy and foreign policy in Kazakhstan, it should be explored further if foreign policy and the multi-vector policy can be a tool for development of Kazakhstan's economy and its energy resources.

Findings from this study on Kazakhstan show that by balancing foreign interests indirectly through energy projects and export routes, energy can be used as a tool without utilizing aggression. Kazakhstan's indirect use of its energy resources as a tool stands in contrast to the direct and aggressive energy weapon.

## **6.2 Implications for new Research and the Road ahead**

In the whole period of study of Kazakhstan, President Nazarbaev has been the leader of the country and the country's foreign policy. The Kazakh government's openness about conducting the multi-vector foreign policy and its policy on development of multiple pipelines has set the framework for how researchers shall understand this relationship. After Nazarbaev's presidency comes to an end, will the current relationship between energy and multi-vector continue? This question for study would also be interesting if Kazakhstan

decides to adopt a different foreign policy in the future. Even if real change comes slowly, a move away from openness by Kazakhstan about its policy approach may open up for more plurality of analysis in the research literature.

The importance of political considerations to development of energy resources and export routes deserves to be explored in more depth. The decision process behind Kazakhstan's choices should be studied with data from informants directly involved. Countries in a similar position as Kazakhstan can also be studied to see if findings from Kazakhstan have some external validity. Are political considerations regarding energy development more important for landlocked countries than other countries?

Regarding the role of energy as a possible tool or a driver for foreign policy, this relationship is far from fully understood or fully explored. There is a need to study this relationship in depth, as suggested above. One interesting path to explore is if the findings in this study have relevance to other cases besides Kazakhstan. It would be especially interesting to study the relationship between energy and foreign policy in other landlocked countries, and other countries with a stated multi-vector policy. Unfortunately, this possibility is limited by the small number of states which share these commonalities with Kazakhstan. Even so the question whether Kazakhstan is unique or not, in relation to the relationship between energy and foreign policy, deserves to be answered.

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