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The Impact of Regime Changes on Foreign Investment: The Case of Chinese Investors in the Goldmines of Kyrgyzstan

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Key Points:

- Central Asia offers China a gateway to western markets and, as such, forms a significant part of the BRI. The region, which is rich in natural resources, has the potential to meet a substantial portion of China's demand for energy and precious metals.
- The investment climate of Central Asian states such as Kyrgyzstan has been subject to regime changes and political instabilities despite the Kyrgyzstan political elites having a friendly approach towards Chinese investors.
- Foreign direct investment in gold mines is seen as a cash cow by Kyrgyz state authorities as part of a short-term contingency plan to consolidate their power. Frequently changing the law, the government renders the investment climate of the state unpredictable. The recent case of nationalizing the Canadian operated Kum-Tor mine highlights the possibility of expropriating foreign investment through sham legislation which damages the reputation of Kyrgyzstan with investors.
- The Chinese investors are challenged by the growing anti-Chinese sentiments that result in regular local anti-mining protests.

Background of Central Asia's Political Economy

Over the last decade, Central Asia has emerged as a new region for investment with rich offshore oil and gas fields and valuable gold and uranium mines offering attractive development potential to international investors.

While the investment resources for foreign investors in Central Asia are rich, the political environment poses challenges. For Central Asian states,¹ where political considerations are more important in shaping domestic and foreign affairs than economic ones, the political regime and will of political leaders has been one of the major determinants of the investment climate.² Even though Central Asian leaders pledge to support democracy, the political regimes in all five countries have been unstable "underpinned by ethnic, sectarian, clan and regional conflicts and authoritarian regimes."³ The power transition in these states is conducted on a hereditary basis, on a clan-based principle, or to an appointed person

¹ Central Asian States comprise Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan.

² Aliya Akhmet et al., *Central Asia: Drivers, Dynamics and Prospects of Trade and Economic Cooperation*, XIII (1)

in advance. Four states (Kazakhstan, Tajikistan, Turkmenistan and Uzbekistan), which do not include Kyrgyzstan, have only their second president after 30 years of independence, only replacing leaders due to death or old age.

China and Central Asia

Sharing a 3300km long border, Central Asia offers China a gateway to western markets and, as such, forms a significant part of the Belt and Road Initiative (BRI). The region, which is rich in a variety of natural resources, has the potential to meet a substantial portion of China's demand for energy and precious metals.

Since the inception of the BRI, China has been actively investing in energy, transport, and trade sectors⁴ in Central Asia in order to diversify its markets and trade routes.

According to the China Global Investment Tracker of the American Enterprise Institute and the Heritage Foundation, between 2005 and 2020 Chinese companies invested almost US\$50 billion in four Central Asian countries (Kazakhstan, Kyrgyzstan, Tajikistan and Uzbekistan) in the above-mentioned sectors.⁵

A brief analysis of the discourses of Central Asian leaders reveals that they uniformly welcome Chinese capital to Central Asia and acknowledge

Beijing's growing role in the region.⁶ The Chinese projects that do not require political and institutional reforms are well liked by the authoritarian Central Asian elites, who struggle to meet western requirements on democratic governance and respect for human rights.⁷

Despite the willingness of the Central Asian elites to welcome Chinese economic engagement in their countries, the public reaction has been negative and has resulted in anti-Chinese protests, especially in Kyrgyzstan and Kazakhstan. According to the Central Asia Protest Tracker, there have been 97 anti-China protests in Kyrgyzstan and Kazakhstan alone in the past three years.⁸

Well-preserved cultural norms, traditions and myths in predominantly rural agrarian societies still play a role in forming the image of foreign investors. Even though Central Asian states share a common border or have close geographical proximity, China remains an 'unknown big world' with its large population and unfamiliar culture. Chinese investors mainly concentrate on building rapport with the state elites, giving little consideration to winning social license and trust, leaving the cultural gap to be filled with folk myths, propaganda remaining from Soviet times, fear and conspiracy theories.

REGIONAL SCIENCE INQUIRY, 183-200 (2021), http://www.rsijournal.eu/ARTICLES/June_2021/13.pdf.

³ Uuriintuya Batsaikhan & Marek Dabrowski, *Central Asia - twenty-five years after the breakup of the USSR*, 3 (3) RUSSIAN JOURNAL OF ECONOMICS 296-320 (2017), <https://www.sciencedirect.com/science/article/pii/S2405473917300429>.

⁴ Bhavna Dave & Yuka Kobayashi, *China's Silk Road economic belt initiative in Central Asia: economic and security implications*, 16 *ASIA EUROPE JOURNAL* 267-281 (2018). <https://doi.org/10.1007/s10308-018-0513-x>.

⁵ HARRY TALIGA, BELT AND ROAD INITIATIVE IN CENTRAL ASIA: DESK STUDY, ITUC (2021), https://www.ituc-csi.org/IMG/pdf/belt_and_road_initiative_in_central_asia.pdf.

⁶ Kemel Toktomushev, *China and Central Asia: Warm Politics, Cold Public*, CENTRAL ASIA PROGRAM (Sept. 7, 2021), <https://www.centralasiaprogram.org/china-central-asia-warm-politics-cold-public>.

⁷ Aijan Sharshenova & Gordon Crawford, *Undermining Western democracy promotion in Central Asia: China's countervailing influences, powers and impact*, 36 (4) CENTRAL ASIAN SURVEY 453-472 (2017), <https://www.tandfonline.com/doi/10.1080/02634937.2017.1372364>.

⁸ The Oxus Society for Central Asian Affairs, Central Asia Protest Tracker, <https://oxussociety.org/viz/protest-tracker/>.

Chinese Investment in Kyrgyzstan's Gold Sector

China's growing investment in the gold extraction sector of Kyrgyzstan since the inception of the BRI in 2013 has alarmed the attention of the public, especially those with negative experiences of mines.⁹ Kyrgyzstan's economy is dependent on the gold sector, which accounts for 10% of GDP and 39% of exports, so foreign investment in gold mining areas has become a battleground for Kyrgyz authorities, the opposition and the local communities. The largest Canadian-operated Kum-Tor gold mine, opened in 1997, became a focus for corruption schemes of Kyrgyz presidents starting with the first president, Askar Akaev. The scandals have formed an image of foreign direct investment in Kyrgyzstan as one of corruption, environmental damage and unfair distribution of profits.¹⁰ With each transition of power in Kyrgyzstan (three times through political unrest ousting the president), the gold mines became the target of new political debate, revenge taking and investigations. In this Research Brief, I explain how political regime changes shape the investment climate in Central Asia through the case study of Kyrgyzstan. I focus on the terms of the latest three presidents during which Chinese foreign investment came onto an agenda: Almazbek Atambayev (fourth President, 2011-2017), Sooronbay Jeenbekov (fifth President, 2017-2020) and Sadyr Zhaparov (sixth President, current).¹¹

⁹ According to OSCE analysis, as of 2019 there were nine companies operating in the gold extraction sector.

¹⁰ Beril Ocakli, *Politics of the Kyrgyz mining sector: An Interview with Beril Ocakli*, VOICES ON CENTRAL ASIA, (May 7, 2021), <https://voicesoncentralasia.org/politics-of-the-kyrgyz-mining-sector-an-interview-with-beril-ocakli/>.

¹¹ *Thirty years of Independence of Kyrgyzstan*, AZATTYK.KG, (Aug. 31, 2021), <https://rus.azattyk.org/a/tridtsat-neprostyh-let-nezavisimosti-kyrgyzstana/31436765.html>.

Changing political regimes in Kyrgyzstan and the investment climate for Chinese investors

Kyrgyzstan's political life has been turbulent compared to other Central Asian states. During 30 years of independence, the country has had 34 prime ministers and six presidents, three of whom were replaced through political protests.

Every parliamentary election, the president forms a puppet (hand) government, where the president's party holds the majority of seats, allowing the president to initiate changes in law or constitution to satisfy his wishes. Adopted in 1993, the Kyrgyz Constitution has been changed four times, widening the powers of the president.

Kyrgyzstan's fourth president, Almazbek Atambayev, started actively attracting Chinese investment. He went in search of foreign sponsors following the 2010 revolution which had resulted in inter-ethnic clashes and a weakened economy. Between 1992 and 2019, Kyrgyzstan received about US\$1.7 billion in loans and investments from China, with a sharp rise observed during his presidency.¹² For Atambayev and his government, Chinese investments primarily provided an opportunity to support the economy without any political conditions and were an alternative to existing Russian investments.¹³

During Atambayev's time, the Zhunda oil refinery, and the Datka-Kemin powerline were built, the main route of the latter coming from China through Kyrgyzstan (Torugart-Bishkek). Also,

¹² National Statistical Committee, *Foreign direct investments by countries, 2004-2020, (2021)*, <http://www.stat.kg/ru/statistics/download/dynamic/864/>.

¹³ Anar Musabeayeva, *Foreign Policy Course of President Atambayev*, CENTRAL ASIAN ANALYTICAL NETWORK (Dec. 20, 2016), <https://www.caa-network.org/archives/8139>.

several licenses for gold mining were issued.¹⁴ Among these projects, the gold mines and oil refinery became the target for protests among the public who voiced their dissatisfaction with the violation of environmental norms. When conflicts between locals and Chinese companies took place in the third largest gold mine Ishtamberdy¹⁵ and at Zhunda, President Atambayev took the stance of the Chinese investors saying that “I am ashamed that we do not fulfill our international obligations and cannot protect investors”.¹⁶ However, under pressure from the community, the government had to temporarily stop the activities of both companies until environmental inspections were conducted. However, despite calling China a ‘strategic partner’ and claiming full support of the BRI, Atambayev’s decision to enter the Eurasian Economic Union in 2015—a move which would prove challenging for Chinese investors in having to adapt to the norms of the union—shows that the country leaders lack long-term vision with respect to Chinese investments and cannot consolidate the statements they make.

Sooronbay Jeenbekov, the next President, was able to win elections in October 2017 with the open support of his old comrade Almazbek Atambayev under the promise to continue the latter’s policies. Yet, powered by his clan, he started a disagreement with Atambayev unveiling his

corruption, including in joint projects with the Chinese. This disagreement grew into a public dispute that ended with the imprisonment of Atambayev. The scandal, in 2018, involved a US\$386 million contract to reconstruct the Soviet-built Bishkek Thermal Power Station without a proper tender and contracted to the Chinese company Tebian Electric Apparatus (TBEA) and caused major concern when the capital city Bishkek went without heating during -30°C weather for three days.¹⁷ The investigation by the Jeenbekov government revealed an unjustifiably expensive reconstruction and a corrupt process. This case led to the arrest of two former prime ministers and later the ex-President himself.¹⁸ Jeenbekov’s criticism of the Chinese companies’ involvement in the previous government’s corrupt mechanisms, that they “need to observe norms and procedures ... in order to ensure the supremacy of the law of the host country,” has negatively impacted the investment inflow from China. After this scandal, the value of investments from China to Kyrgyzstan has fallen from US\$300 million in 2017 to just over US\$100 million in 2018. In 2018, it also became apparent that Kyrgyzstan did not receive US\$100 million allocated by China as a grant.¹⁹

In October 2020, Kyrgyzstan witnessed a third revolution, when protesters who were dissatisfied

¹⁴ Konstantin Syroezhkin, *Towards the end of Xi Jinping’s visit to Central Asia: Kyrgyzstan*, CARNEGIE ENDOWMENT FOR INTERNATIONAL PEACE (Sept. 23, 2013), <https://carnegieendowment.org/2013/09/23/ru-pub-53062>.

¹⁵ Kubanychbek Zholdoshev, *Ishtamberdi Scandal*, RADIO AZATTYK (June 14, 2018), <https://rus.azattyk.org/a/kyrgyzstan-gold-field-ishtamberdy/29289576.html>.

¹⁶ Zhanyl Kupesheva & A. Atambaev, *I was ashamed when the Chinese leadership spoke about the situation of Chinese investors in the Kyrgyz Republic*, FOR.KG (Sept 15, 2011), <https://www.for.kg/news-162920-ru.html>.

¹⁷ Agata Palickova & Georgi Gotev, *Scandals in Kyrgyzstan highlight dubious Chinese business practices*, EURACTIV

(Jul. 24, 2019), <https://www.euractiv.com/section/central-asia/news/scandals-in-kyrgyzstan-highlight-dubious-chinese-business-practices/>.

¹⁸ Temur Umarov, *The Failure of Atambayev’s Planned Power Transition*, CARNEGIE MOSCOW CENTRE (Aug. 23, 2019), <https://carnegiemoscow.org/2019/08/23/failure-of-atambayev-s-planned-power-transition-pub-79718>.

¹⁹ Ernest Nurmatov, *What explains the decline in investment from China to Kyrgyzstan?*, RADIO AZATTYK (Jan. 25, 2019), https://rus.azattyk.org/a/kyrgyzstan_china_reduction_investments/29730553.html.

with the election results seized the government buildings and freed some politicians from prison, including Sadyr Zhaparov who was serving a 10-year sentence for disorders and kidnapping in the Kum-Tor gold mine. Amid the political crisis, a new government was formed with Sadyr Zhaparov as the current president.²⁰ Sadyr Zhaparov has been popular for his rhetoric of nationalizing the largest gold mine, Kum-Tor, from which Kyrgyzstan did not receive much economic benefit and the Canadian investors seemingly violated environmental norms.

Anti-mining protests is not a recent phenomenon. Over the last 20 years, the local protests against foreign owned mines have become regular coupled with resource nationalism and grievances of the local population who feel deprived from the income generated by mines.²¹ Political unrest provided an opportunity for the local people to voice their demands to the companies operating gold mines and to new state authorities. Similar to two previous revolutions,²² the October 2020 unrest created a situation where by numerous attacks by the local population on the gold mines, including the Chinese operated ones such as Kichi-Chaarat and Ishtamberdy, caused production to halt for several days as they were seized by the local population. Local population's

grievances against the Chinese-operated mines were fueled by "perceived corruption, the lack of transparency, and discrimination against hiring local residents as well as environmental degradation."²³

Nationalizing the largest Canadian-operated Kum-Tor gold mine and its consequences for Chinese investors

After coming to power President Sadyr Zhaparov changed the constitution, expanding the power of the president and changing the system from a parliamentary democracy to a presidential one, with 79% support from voters. Zhaparov also passed several bills through this illegitimate Parliament whose term should have finished in October 2020 but was indefinitely extended until the new constitution was accepted.

The Parliament and President approved the changes in the Law on Joint Stock Companies and Criminal Code, according to which the government had acquired the powers²⁴ to appoint external managers to take over any company with foreign investors on a temporary basis to remedy any alleged environmental and safety violations. Shortly after the law had been approved, Kyrgyz courts found the Kum-Tor Gold Mining Company guilty of environmental violations, causing state damages worth an eye-watering US\$3 billion. Ten

²⁰ Timur Toktonaliev, *Sadyr Zhaparov's Dreams are Coming True. Will Zhaparov Make the Dreams of Kyrgyzstanis Come True?* THE INSTITUTE FOR WAR AND PEACE REPORTING (Jan. 14, 2021), <https://cabar.asia/en/sadyr-zhaparov-s-dreams-are-coming-true-will-zhaparov-make-dreams-of-kyrgyzstanis-come-true-2>.

²¹ Saipira Furstenberg & Kemel Toktomushev, *Understanding gold mining and social conflicts in Kyrgyzstan*, University of Central Asia Institute of Public Policy and Administration (IPPA) Working Paper (63), 2021, 1-22, <https://ucentralasia.org/media/ssmbkbyb/uca-ippa-wp63-understanding-gold-mining-and-social-conflicts-in-kyrgyzstan.pdf>.

²² Tulip Revolution in 2005 against the regime Askar Akaev (1st president), and April Revolution in 2010 against the regime of Kurmanbek Bakiev (2nd president).

²³ Saipira Furstenberg & Kemel Toktomushev, *Understanding gold mining and social conflicts in Kyrgyzstan*, University of Central Asia Institute of Public Policy and Administration (IPPA) Working Paper (63), 2021, 1-22, <https://ucentralasia.org/media/ssmbkbyb/uca-ippa-wp63-understanding-gold-mining-and-social-conflicts-in-kyrgyzstan.pdf>.

²⁴ Chris Rickleton, *Kyrgyzstan: Expropriation law takes Kumtor battle to the brink*, EURASIANET (May 10, 2021), <https://eurasianet.org/kyrgyzstan-expropriation-law-takes-kumtor-battle-to-the-brink>.

days later a Kyrgyz external manager was appointed, and the Canadian administration left the mine initiating an international arbitration proceeding against the Kyrgyz government²⁵ and causing the disappointment and warnings from international organizations.

Since the accession of Zhaparov, the investment and business climate in Kyrgyzstan has soured. The anti-corruption campaign initiated by the State Security Agency (led by Zhaparov's political comrade Kamchy Tashiev) resulted in a significant uptick in business investigations and detentions of business executives on criminal charges.²⁶ After the Canadians left, the potential - and only - interested investors in the development of the Kum-Tor mine were the Chinese; however even they have had difficulties in recent years in mining the deposits of Kyrgyzstan.

The Kum-Tor case did not directly impact the Chinese investors in the gold mining sector. With

45% of their debt being owed to China, the Kyrgyz authorities are less likely to violate the wishes of Chinese investors. However, the Kum-Tor case highlights the possibility of expropriating foreign investment through sham legislation which damages the reputation of Kyrgyzstan with investors.

In short, foreign direct investment is seen as a cash cow by state authorities as part of a short-term contingency plan to consolidate their power. Frequently changing the law, the government renders the investment climate of the state unpredictable. Despite the Kyrgyzstan political elites having a friendly approach towards Chinese investors, political infighting among local elites can undermine the state's economic policy.

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²⁵ *What next for Kyrgyzstan and Kumtor?* EURASIANET (May 18, 2021), <https://eurasianet.org/what-next-for-kyrgyzstan-and-kumtor>.

²⁶ Kyrgyz Republic - Country Commercial Guide: Investment Climate Statement, INTERNATIONAL TRADE ADMINISTRATION, (Oct. 5, 2021), <https://www.trade.gov/country-commercial-guides/kyrgyz-republic-investment-climate-statement>.