INVESTMENT CLIMATE AND ITS INFLUENCE ON THE DEVELOPMENT OF ENTREPRENEURSHIP: PRACTICE OF THE REPUBLIC OF KAZAKHSTAN

Arslan Kulanov ¹, Saltanat Tamenova ², Kamilya Amenova ³, Alma Karshalova ⁴, Leila Tussupova ⁵

¹,²,⁵ Turan University, Satpaeva Street, 16a, Almaty, 050000, Kazakhstan
³,⁴ Narxoz University, Zhandosova Street, 55, Almaty, 050035, Kazakhstan

Received 20 December 2019; accepted 26 August 2020; published 30 December 2020

Abstract. The purpose of this study is to identify problems that impede the investment activities of small and medium-sized enterprises (SMEs) in the Republic of Kazakhstan, as well as to study the recommendations of the leading representatives in the business community regarding the activities of the authorities in creating a favorable investment climate. Expert interviews with the Kazakhstan’s entrepreneurs, representatives of Akimats, and representatives of the scientific community have been conducted during the study. The results of the expert survey allow to conclude that the Republic of Kazakhstan has developed a rather favorable investment climate in general, and the authorities have done significant work to create conditions for business development. However, according to the expert review, some problems in the implementation of investment projects by SMEs still remain. According to the experts, the most significant problems include the underdeveloped transport and logistics infrastructure, the lack of available production and office space, and difficulties with registering land, attracting foreign labor, as well as obtaining various permits required for doing business. As a result of the study, the recommendations have been made for eliminating the barriers that hinder the creation of a favorable investment climate and the successful development of SMEs in the Republic of Kazakhstan. According to the experts, the attention should be focused on creating and developing ready-made platforms for doing business for investors, improving transport and logistics infrastructure, speeding up the state property privatization, etc.

Keywords: investment climate; business environment; entrepreneurship; business climate; investment activities


JEL Codes: M13, M14

1. Introduction

Integration with global markets and the increasing competitiveness of the private sector have contributed to the unprecedented growth of many economies – especially those of Asian countries, such as China, Vietnam, etc. (World bank, n.d.; Siddique et al., 2020; Adeniran et al., 2020).
The development of entrepreneurship in the Republic of Kazakhstan is the most important factor in influencing the welfare of the country's economy (Serikbaeva, Bektanov, Bekturganova, 2019). More than 1.2 mln SMEs operated in the country and over 3.3 mln people were employed in the sector at the beginning of 2019 (Statistics Committee of the Ministry of National Economy of the Republic of Kazakhstan, n.d.).

At the same time, the economic potential of SMEs in the Republic of Kazakhstan is not fully utilized. The number of people currently employed in SMEs in the Republic of Kazakhstan is 21.6 %. In most advanced economies, this indicator is in the range of 45 – 75 %. For example, the number of people employed in SMEs is 44.9 % of the total employment in Germany, 50 % - in France, 56.1 % - in the UK, 73.3 % - in Italy, and 72.9 % - in Korea (OECD.stat, n.d.).

The SMEs’ contribution of the value added to the GDP in the Republic of Kazakhstan is 28.4 % (Statistics Committee of the Ministry of National Economy of the Republic of Kazakhstan, n.d.). For comparison, this indicator is 76.6 % in Korea, 63.4 % - in Italy, 45.6% - in the UK, and 43.4 % - in France (OECD.stat, n.d.).

Foreign direct investment (FDI) is one of the main catalysts for the development and encouragement of the economic activities of SMEs. It is generally recognized that the importance of FDI for the country’s economic prospects is growing amid the increasingly globalized business environment. Attracting investment in economic development is especially important for the Republic of Kazakhstan, which has positive prospects for the growth of consumer markets and unrealized natural resource potential.

For the Kazakhstan’s SMEs, the potential benefits of attracting investments are related to expanding market opportunities and internationalizing their business, improving managerial skills, using new technologies, and facilitating access to capital (Dyussembekova et al., 2019).

The Republic of Kazakhstan observes the positive dynamics in the development of investments: the inflow of FDI in the country’s economy increased by almost 58 % over four years, from 15.4 bln USD in 2014 to 24.3 bln USD in 2018 (Statistics of direct investment by the direction of investments, n.d.).

A favorable investment climate is one of the main reasons for the observed growth in investment activities in the Republic of Kazakhstan. While huge reserves of Kazakhstan’s hydrocarbons and mineral resources remain the basis of the economy, the government of the Republic of Kazakhstan creates the proper conditions: the investment law is enforced, the relevant regulations are adopted, preferences for certain types of production are put in effect, the money is raised to invest in free economic zones (FEZs), and an appropriate program of industrial and innovation-driven growth is adopted.

Kazakhstan adopted the OECD Declaration and Decisions on International Investment and Multinational Enterprises and became an associate member of the OECD Investment Committee in June 2017 (Madiyev et al., 2018).

In August, 2017 the government of Kazakhstan adopted a new National Investment Strategy for 2018 – 2022, developed together with the World Bank, which outlined new coordination measures to improve the investment climate, privatization plans, and a policy of economic diversification. The strategy aims to increase the total FDI inflow by 25 % by 2022 (Decree of the Government of the Republic of Kazakhstan No. 498, 2017).
The efforts of Kazakhstan to remove bureaucratic barriers, in particular through a “single-window” program for investors, were moderately successful, and Kazakhstan ranked 28th out of 190 in the World Bank’s ranking on the ease of doing business in 2019 (World Bank, 2020).

Despite ongoing institutional and legal reforms, such problems as corruption, bureaucracy, and limited access to skilled labor remain relevant in some regions of Kazakhstan.

2. Literature review

Many scientific works are devoted to the problems of the SMEs development. Many authors agree that entrepreneurship is a powerful economic force that creates the majority of new jobs and contributes to economic growth, which determines the interest of the state in this phenomenon (Burov, 2013; Dethier, Hirn, Straub, 2011; Aterido, Hallward-Driemeier, Pages, 2007; Dollar, Hallward-Driemeier, Mengistae, 2005; Merzlova, Sharkova, 2013; Rubio-Mozos, García-Muiña, Fuentes-Moraleda, 2019; Kowo, Adenuga, Sabitu, 2019).

The steady growth of SMEs reflects the stability of the economy (Rubio-Mozos, García-Muiña, Fuentes-Moraleda, 2019). Although the concept of entrepreneurship has not been yet completely formed, the interest of researchers in it is growing (Wiklund et al., 2011).

Researchers note that creating a favorable environment for the dynamic development of the entrepreneurship sector is directly dependent on government policies aimed at creating a transparent, stable, and predictable investment climate (Dethier, Hirn, Straub, 2011; Novolodskaya et al., 2019; Savitz, Dan Gavriletea, 2019).

The investment climate is the economic, financial, and sociopolitical conditions in the country that influence the willingness of individuals, banks, and institutions to issue loans and to acquire shares (to invest) in the enterprises operating in that country (Ongbwa, 2017).

The investment climate in a given country or region can be defined by a wide range of factors that determine whether domestic and foreign investments occur: the soundness of macroeconomic policies, the strength of economic and political institutions, the regulatory framework, the quality of infrastructure and other services, etc. (Vijayalakshmi et al., 2019).

As a rule, factors contributing to the development of the investment climate are selected during surveys of company managers and owners, as well as during interviewing potential investors.

Much of the research literature is devoted to the study of the relationship between the characteristics of the business regulatory environment and enterprise performance, as well as macroeconomic results (Rose, Mamabolo, 2019; Lynch-Wood, Williamson, 2014; Asim et al., 2019; Avan, Kraslawski, Huiskonen, 2017). However, the studies in general do not give final results regarding the direction of causal relationships. A hypothesis is usually made that better regulation encourages better economic outcomes (Graafland, Bovenberg, 2019).

Many aspects influence the quality of the country's investment climate and overall competitiveness. A number of global benchmarking initiatives have been developed by now, which can be useful in understanding the investment climate of business in countries (Borkova et al., 2019).
Most of these initiatives are built around five topics (Golaido, Soboleva, 2015): 1) competitiveness and investment climate; 2) prospective restrictions on the part of enterprises; 3) business and investment barriers; 4) risk and uncertainty of the policy; and 5) the cost of operations.

With regard to competitiveness and investment climate, the data on prospective restrictions on entrepreneurship are provided in the World Bank Group's enterprise surveys. The World Bank Group’s Doing Business indicators measure regulatory concerns for enterprises based on a combination of statistics, regulatory information, and enterprise surveys (World Bank, 2020). These surveys and indicators are complementary, but have different approaches to benchmarking of the business environment quality in different countries.

The World Economic Forum's Global Competitiveness Index (World Economic Forum, 2019) is another source of information, which combines the results of opinion polls of managers and quantitative data in an attempt to measure the economy competitiveness based on a set of elements covering broad socioeconomic aspects, such as institutions, infrastructure, macroeconomic stability, financial system, dynamism of entrepreneurial activities, innovative potential, etc.

The United Nations Industrial Development Organization (UNIDO, 2018) evaluates more than 100 countries in terms of their industrial competitiveness and their production and export potential, in particular.

The policies of the Organization for Economic Cooperation and Development (OECD) address a range of areas that influence investment. The OECD uses such indicators as the volume of external flows and inflow of FDI, external and internal positions of FDI, as well as income from the export and inflow of FDI in order to assess the investment climate. The index of regulatory restrictions on FDI is one of the most important indicators that determine the factor of the country's attractiveness for foreign investment (Kalinova, Palerm, Thomsen, 2010).

As such, a rather extensive methodological base for assessing the state of the investment climate is presented in the scientific literature at the moment. However, the leading global indicators of various aspects of the investment climate are not sufficient to get a complete picture of the problems of investment competitiveness of small and medium enterprises in countries with developing economies.

The hypothesis of the study is the assumption that a favorable investment climate helps raise capital and increase the competitiveness of SMEs.

3. Methods

The main method of research was a representative sociological survey of experts. The experts were selected according to a preplanned list sample. Three hundred and eleven people were invited as experts from among the heads and deputy heads of SMEs in the Republic of Kazakhstan, 32 representatives of Akimats with the economic profile, and 27 representatives of the scientific community competent in the subject of the study. If an expert did not want or could not participate in the interview, then other people competent in the subject of the study, i.e., their deputies, assistants, and colleagues, were allowed to participate in the survey.

The main objectives of the survey were to obtain data describing the state of the investment climate, including problems and prospects for the development of SMEs, and to prepare recommendations for improving the investment climate in the Republic of Kazakhstan.
The survey was conducted using the approved questionnaire with formalized questions. A personal interview with an expert was used as the interview method. If a personal interview with the expert was impossible, the survey was carried out by phone or by email. The interview was recorded using a voice recorder (after that, the audio was transcribed into Word).

Based on the results of the survey, a general list of factors that have both positive and negative impact on the investment climate of the country has been compiled. By the nature of the impact on the innovation climate, all factors are divided into several groups:

• Factors of the country's natural resource potential - mineral reserves, availability of own fuel and energy resources, level of environmental pollution;

• Factors of the institutional environment and socio-political stability - the level of the regulatory framework for the protection of property rights and regulation of small and medium-sized businesses, the development of competition mechanisms and market institutions, the tax environment, government support measures for small and medium-sized enterprises, measures to ensure the execution of contracts;

• Infrastructural factors - the quality of financial infrastructure, transport accessibility, the state of energy infrastructure, the level of ICT development, the provision of housing for the population;

• Factors of economic development - macroeconomic stability of the country, GDP per capita, inflation, openness of the economy to international trade, annual growth in value added of industrial sectors, gross capital formation, final consumption expenditures.

• Labor market development factors - unemployment rate, labor productivity in industry, agriculture, services sector.

The distribution of the survey participants by the beginning of their activities was uniform: 18% carried out their activities for no more than three years, every fifth entrepreneur began to carry out their activities no earlier than one year ago – 22%, or six months ago – 22%. Only 18% of the entrepreneurs had been working for more than three years.

4. Results

The results of the survey reveal that most experts positively assess the measures of the authorities of the Republic of Kazakhstan aimed at the development of SMEs. For more convenient presentation, the experts' responses were divided into three groups: high ratings (positive), average ratings (neutral), and low ratings (negative).

Translating into a five-point rating scale, most entrepreneurs usually give these measures four points. At the same time, all representatives of government bodies that took part in the survey rated the existing support measures as high (Figure 1).
At the same time, it can be noted that there is a high proportion of the experts in the overall distribution who assess the measures of government bodies aimed at developing SMEs in the Republic of Kazakhstan at an average level, noting that the shortcomings are still present (28.1 % of the respondents), and who rate these measures as low (7.6 %). In addition, 18 experts from among entrepreneurs indicated that they found it difficult to assess these measures because they had never noticed or encountered them. The respondents consider these measures to be insufficient because the authorities do not always want to “hear” entrepreneurs and are not always open.

The experts assess the measures aimed at creating a favorable investment climate in the Republic of Kazakhstan as lower than the measures to develop entrepreneurship in the country.

The share of the experts who took part in the survey and found it difficult to assess these measures, since they had never encountered or heard anything about them, was almost 15 % (Figure 2)
At the same time, 31.1% of the business, government, and the scientific community representatives in the Republic of Kazakhstan highly rate the measures aimed at creating an investment climate.

At the same time, the shares of the experts who rated the measures to create an investment climate in Kazakhstan at an average and low level were approximately equal. For example, 27.6% of the experts highly appreciate the measures aimed at creating an investment climate. At the same time, 26.5% of the experts, on the contrary, rate these measures very low. Most experts (84.3%) believe that Kazakhstan is already an attractive and promising field for raising investment. The level of satisfaction with the business conditions existing today in the Republic of Kazakhstan among the experts is rather at the average level (Figure 3).
The survey results indicated that entrepreneurs were generally not critical in assessing the conditions for doing business, but they did not provide high ratings either, noting that there were still some problems in this area. At the same time, almost 5% of the business representatives found it difficult to answer this question.

The experts note that despite the fact that much work has been done in the Republic of Kazakhstan in terms of the measures aimed at developing SMEs in general, there are big problems with the implementation of investment projects of SMEs. According to the experts, the largest share of serious problems in the implementation of investment projects is noted in infrastructure and logistics (51.1%) and the lack of available production and office space (48.9%) (Figure 4).

In the course of the survey, the experts were invited to identify factors that encouraged the investment activities of SMEs. The experts noted the availability of significant reserves of fossil fuels and other minerals and metals, the laws in force in the Republic of Kazakhstan on the protection of property rights, a fairly favorable tax environment, and a range of government support measures for SMEs as the main encouraging factors that influenced the investment climate (Figure 5).
More than 40% of the respondents named the development of competition mechanisms and market institutions, macroeconomic stability, established rules for enforcing contracts, legislation on the SMEs regulation, and the quality of infrastructure as the main encouraging factors.

In general, the experts believe that these factors should ensure and encourage the development of SMEs and the stability of the investment climate. It must be noted that the experts who took part in the survey mentioned that the factors influencing the state of the investment climate and the development of SMEs were interconnected and usually did not differ.

5. Discussion

In conclusion, the experts were asked to give their recommendations for the creation of a favorable investment climate and the successful development of SMEs in the Republic of Kazakhstan.

The most popular recommendations on the creation of a favorable investment climate and the successful development of SMEs in the Republic of Kazakhstan mentioned by the experts include the creation and development of ready-made platforms for doing business for investors, improvement of infrastructure, speeding up the privatization process, etc. (Figure 6).
Almost two-thirds of the experts (65.9%) believe that providing investors with ready-made platforms for doing business is an effective tool to attract investments in the country's economy. Such platforms include special economic and industrial zones (SEZ and IZ) and investment contracts.

It must be noted that 12 SEZs have already been created and are operating in the Republic of Kazakhstan. They have already proved their effectiveness. According to the Ministry of Industry and Infrastructure Development of the Republic of Kazakhstan, the budgetary costs for the construction of the infrastructure of all SEZs amounted to 314.3 bln tenge, while the volume of the raised investment amounted to approximately 910 bln tenge. This means that one tenge from the budget invested in the SEZ infrastructure allowed to raise 2.8 tenge of private investment.
investments. At the same time, 85.9 bln tenge were invested in the IZ infrastructure. As such, 2.1 tenge of
investments were attracted per each tenge invested from the budget. In total, 183 projects were launched in the
territories of SEZs, of which 46 projects were with foreign participation, 15.5 thousand jobs were created, and
about 150 bln tenge were repaid to the budget as taxes.

At the same time, 38.9 % of the experts noted that the SEZs in the Republic of Kazakhstan were not working
efficiently enough, despite the significant level of budget investments in the development of zonal facilities. This
requires timely diagnosis of the factors that impede the success of SEZs and targeted actions to address them.
The experts name the following main reasons for the low efficiency of some SEZs: weak management structures
or too many institutions involved in the management of SEZs, poor location of facilities requiring large capital
costs or situated far from the infrastructure centers; poor design of areas with inappropriate equipment or
maintenance, etc. (Figure 7).

![Fig. 7. Key problems for SEZs (% of the respondents)](source: Compiled by Authors)

Regular monitoring and evaluation mechanisms should become a key aspect of the institutional and
managerial structure of the SEZ. There is no systematic evaluation of the performance of the zones in
the Republic of Kazakhstan today, and no mechanisms have been created to solve the problems of
insufficient performance of SEZs.

It seems appropriate to draw attention to international practice in the formation of a system for
monitoring the performance of SEZs. For example, China regularly evaluates the performance of high-
tech development zones (HTDZs), as well as economic and technological development zones (ETDZs).
The 1996 Administrative Decree of the Ministry of Science and Technology requires regular evaluation
of HTDZs. The 2013 rating index system includes four categories and 40 indicators, such as:
Knowledge creation and technological innovation: the level of employees’ education, R&D expenses, the number of research institutes and incubators, etc.

Capabilities for industrial modernization and structural optimization: the number of high-tech enterprises, ratio of enterprises in the service sector, registration of intellectual property, the number of registered companies, etc.

Internationalization and participation in global competition: the ratio of employees who have graduated abroad, the ratio of foreign personnel, the number of foreign branches, registration of intellectual property abroad, etc.

Sustainable development potential: the ratio of employees with Master's and Doctor’s degrees, growth rate of the number of companies or tax revenues, volume of new investments, energy consumption, etc.

Evaluation of the innovative potential of HTDZs has been used as an additional performance criterion since 2016.

The Ministry of Commerce of China has been conducting an annual ETDZ assessment since 2016. The exit system applies to the lowest rated ETDZs for two consecutive years. Evaluation of ETDZs is based on five criteria, namely industrial potential, technological innovation, regional integration, environmental protection, and administrative efficiency. The Ministry of Commerce publishes a list of top 30 zones and the names of top 10 zones in the categories of industrial potential, innovation, FDI, and foreign trade, respectively.

The Russian Federation has developed a comprehensive method for monitoring and evaluating the performance of its SEZs in a similar manner (Nikitina et al., 2018; Levkina, Sakharova, Edelev, 2020). The government monitors and evaluates several SEZ types in the Russian Federation: industrial production, technological innovation, tourism and recreation, and ports. The legislation of the Russian Federation establishes six indicators of the SEZ performance: investment attractiveness, business environment, infrastructural support, access to land resources, investment activity of the SEZ residents, and information transparency of the SEZ website. The evaluation is carried out annually, and zones are ranked according to certain criteria. This process mainly served to create equal pressure on the ineffective zones and regional authorities of the area in which they operate. Unscrupulous performers are excluded from the SEZ list and shut down.

In addition to the SEZs, the creation of SME parks is also a promising tool for creating a favorable investment climate in the Republic of Kazakhstan.

The SME parks are autonomous geographical areas with high-quality infrastructure facilities that host industrial enterprises. The main goal of the SME parks is to create SMEs that produce high value-added products but lack the necessary funds to invest in the development of their own basic infrastructure facilities, though they are able to pay for the services provided to them.
The government secures infrastructure facilities and, therefore, creates favorable conditions for attracting SMEs. The general goals of the SME parks are to take advantage of local and international investment opportunities by creating processing parks in strategic areas rich in raw materials.

In the course of the survey, the experts identified a number of priority areas for the development of the SME parks and industrial zones in the Republic of Kazakhstan: reimbursement of investor costs for building and assembly works on infrastructure construction (47.8 %), infrastructure construction by providing a preferential rate (30.3 %), and optimization and automation of land allocation (27.3 %).

More than half of the surveyed experts (52.2 %) highlighted the availability of high-quality infrastructure as a recommendation on creating a favorable investment climate and successful development of SMEs in the Republic of Kazakhstan. Almost all regions of Kazakhstan need additional investments in the logistics infrastructure. According to the ESCAP, the annual need for investments in the infrastructure of the Republic of Kazakhstan is 2.1 % of the GDP, of which 0.7 % of the GDP is for the transport infrastructure, 0.9 % is for the energy infrastructure, 0.3 % is for the water supply and sanitation infrastructure, and 0.2 % is for the ICT (Branchoux, Fang, Tateno, 2017). Improving infrastructure is especially important in the regions in order to attract foreign investors and FDI.

More than half of the experts (51.4 %) believe that the privatization process should be sped up in order to create a favorable investment climate. A large share of state participation strengthens monopolistic trends and limits the development and growth of enterprises and their market orientation.

The privatization process should be sped up to make the development of enterprises more efficient. To speed up the privatization process, an inventory of state property and assets should be compiled, and their market value should be determined with the involvement of an independent appraiser. One of the prerequisites for the privatization process is its transparency and openness. State property may be sold through an open electronic auction rather than through direct sales.

In addition to those mentioned above, the expert recommendations include the need to simplify procedures related to the attraction and hiring of foreign labor, promoting the country's investment image abroad, raising SMEs awareness of the existing measures of state support, removing barriers to the participation of SMEs in public procurement, etc.

Therefore, it is recommended for authorities and competent authorities to pay an increased attention to the measures proposed by the experts and consider the possibility of their implementation in the future.
Conclusions

The results obtained in the course of the study confirm the hypothesis that a favorable investment climate helps raise investment in the development of the country's economy and increase the investment activities of SMEs of the Republic of Kazakhstan.

According to the experts, the main problematic issues that arise during the investment activities of SMEs include the underdeveloped transport and logistics infrastructure, the lack of available production and office space, as well as difficulties with registering land.

In general, the experts have identified the following factors encouraging the investment activities of SMEs: availability of significant reserves of fossil fuels and other minerals and metals, the current legislation in the Republic of Kazakhstan on the protection of property rights, a rather favorable tax environment, and a range of the state support measures for SMEs.

The Kazakhstan’s experts have made suggestions to improve the investment climate in the course of the survey. The most numerous expert recommendations relate to the creation and development of ready-made platforms for doing business for investors, improving transport and logistics infrastructure, and speeding up the privatization of state property.

References


Statistics of direct investments by the directions of investment. Gross inflow of direct investment in Kazakhstan from foreign direct investors. The official Internet resource of the National Bank of Kazakhstan. Retrieved from: https://nationalbank.kz/cont%D0%98%D0%9F%D0%98%20q19%20%D1%81%20%D0%BE%D1%82%20%D1%85%20%D1%80%20%D1%85%20%D1%83%20%D1%81%20%D3%20%D5%20%D3%20%D1%80%20%D1%83%20%D1%81%20%D1%81.xlsx


Make your research more visible, join the Twitter account of ENTREPRENEURSHIP AND SUSTAINABILITY ISSUES: @Entrepr69728810

Arslan KULANOV  
ORCID ID: https://orcid.org/0000-0002-8148-5411

Saltanat TAMENOVA  
ORCID ID: https://orcid.org/0000-0002-2656-6040

Kamilya AMENOVA  
ORCID ID: https://orcid.org/0000-0001-9561-5494

Alma KARSHALOVA  
ORCID ID: https://orcid.org/0000-0002-0065-8369

Leila TUSSUPOVA  
ORCID ID: https://orcid.org/0000-0001-7511-1889