

# WHAT DRIVES THE EMPLOYMENT OF PUBLIC-PRIVATE PARTNERSHIPS IN KAZAKHSTAN AND RUSSIA: VALUE FOR MONEY?

Nikolai Mouraviev\*,

Department of Public Administration, KIMEP University, Kazakhstan

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**Abstract:** Public-private partnerships (PPPs) are employed in many countries as an alternative method of public service provision in which partners from the public and private sectors share their resources, responsibilities, and risks. Some well-justified factors that drive the partnership development are value for money and lack of budget funding. As PPP drivers may be unique, the paper surveys the reasons for PPP expansion in two transitional countries, Kazakhstan and Russia. Based on detailed discussion of the commonly employed reasons for partnering (such as greater value for money, or lower total social cost associated with a PPP as opposed to contracting out a service), internal and external PPP drivers in Kazakhstan and Russia have been categorized and examined. Among internal drivers, the need to attract private initiative and funding for upgrading the utilities and housing infrastructure is most influential because of enormity of the task for which governments lack resources. The countries' intention to align themselves with the requirements of perceived international best practices is yet additional influential driver of external nature. The paper concludes that public policy in the two countries is the major driving force for PPP development although the value for money concept and transaction cost economics appear to be neglected. The emerging PPP policy paradigm in Kazakhstan and Russia has facilitated PPP development in recent years, since 2005. However, lack of reliable solutions and instruments for PPP formation and implementation significantly slows down PPP expansion.

**Key words:** public-private partnership (PPP), value for money, PPP drivers, concession

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## Introduction

Governments in many countries increasingly turn to public-private partnerships (PPPs) as an alternative method of delivering public services as opposed to traditional public procurement contracts or in-house government provision. Partnership projects are implemented in many sectors including transport infrastructure (such as construction and management of automobile roads, railroads, sea ports, and airports), utilities

\* Department of Public Administration, KIMEP University, Almaty, Kazakhstan.  
Mailing address: 4 Abay Ave, #306, Almaty, Republic of Kazakhstan 050010.  
E-mail: nmouraviev@yahoo.com, mnikolai@kimep.kz Tel: +7 701 756 41 40

infrastructure (such as water treatment and provision), health care (such as hospital management), energy (construction of power generating facilities and power transmission), and others.

While the U.K., France, Spain, the U.S., Australia, New Zealand and other countries have already accumulated extensive experience in PPPs (Bult-Spiering & Dewulf, 2006; Hood et al., 2006; Reeves, 2003; Vining et al., 2006), other countries such as Bulgaria, Croatia, Kazakhstan and Russia are in the very beginning of using partnerships as a method of delivering public services (Vnesheconombank, 2010). What drives the expansion of PPP usage in transitional countries compared to industrialized nations? This paper critically examines PPP drivers in Kazakhstan and Russia and compares approaches in the two nations with traditional approaches to PPP formation used in OECD countries.

The paper begins with a brief overview of the meaning of a PPP and its essential features. This will allow, in subsequent sections, to highlight the differences between the commonly accepted understanding of a partnership and that in the Russian language literature. The paper moves on to the review of reasons for PPP formation as stated in the Western literature, mainly from the value for money perspective and using the transaction cost economics theory. To ensure a balanced approach to PPP formation issues, the paper identifies not only the arguments in favor of partnerships, but also their shortfalls.

Then the highlights of PPP operations in Kazakhstan and Russia are provided in order to set contextual background for the discussion of PPP drivers in these countries. This discussion follows in the next section in which drivers are categorized as internal and external, and specific factors in each category are identified and explained in detail.

The next section gives a critical assessment of what the Russian language literature claims to be PPP drivers in Kazakhstan and Russia. The comparisons with OECD approaches and relevant literature are made and the differences are noted.

Section 7 provides an assessment of influence that drivers identified earlier have on PPP expansion. This assessment allows to indicate priority factors and also the factors that have lesser importance. This section further discusses the role that governments play in defining behavior of actors in the public and private sectors. In addition, contextual factors surrounding most influential PPP drivers are described. Finally, the question of why the progress with PPPs in Kazakhstan and Russia appeared to be slow is addressed, followed by insights regarding how PPP expansion can be facilitated.

The paper concludes that criteria for PPP formation in the two countries are largely vague and inconsistent, whilst PPP advantages are often inflated. It remains unclear what role the value for money concept and transaction cost economics play in decisions regarding whether to form a partnership. In practice, the major driving force for partnership expansion is the public policy as a comprehensive factor that strengthens and pushes all other drivers in the direction of PPP development. This paper adds to and broadens knowledge and understanding of why and how governments in Kazakhstan

and Russia address PPP expansion within the context of the acute needs of these transitional economies. In addition, this paper critically appraises the rationale of policy makers in Kazakhstan and Russia regarding why they push for PPP proliferation, and why, despite multiple drivers and the public policy in place, PPP expansion appears to be slow.

In reference to why the reasons behind partnerships in Kazakhstan and Russia are examined together and compared, it can be argued that the two nations possess a large number of commonalities in their economies and public policies. Both countries are transitional economies and share many economic, political, business, social, educational and cultural realities that stem from a common Soviet legacy. Although the two economies are different in size, the ways in which governments have shaped their PPP policies, created a legal and regulatory framework and selected sectors for partnership projects show considerable similarities that allow meaningful comparisons between the two countries. An empirical examination of the PPP drivers in Kazakhstan and Russia may thus contribute to a deeper understanding of what the actual reasons for the broader employment of partnerships are, and how they are different from justification commonly used in OECD countries.

## **1. Essential Features of a Partnership**

A brief overview of the meaning of a PPP may be useful for highlighting the properties of a partnership that make it different from traditional forms of collaboration between the public and private sectors such as public procurement contracts or when government sub-contracts a private company for implementation of a specific task. A PPP arrangement exists when a government agency assigns a traditionally public responsibility to a private company in an attempt to improve delivery efficiency, lower costs, increase customer satisfaction and attract private funding (Hofmeister & Borchert, 2004).

A comprehensive understanding of a partnership is offered by Grimsey & Lewis who describe a PPP as an “agreement where the public sector enters into long-term contractual agreements with private sector entities for the construction or management of public sector infrastructure facilities by the private sector entity, or the provision of services (using infrastructure facilities) by the private sector entity to the community on behalf of a public sector entity” (Grimsey & Lewis, 2002, p. 108).

Yet another approach argues that a PPP is an institutionalized arrangement between public and private actors in which they share a responsibility for a product, risk, costs, and benefits (Klijn & Teisman, 2003). Although this definition lacks explanation of what exactly a PPP is going to provide and how, it includes key elements that partners have to share. In other words, it is sharing that transforms collaboration into a partnership. Perhaps, this is most evident in reference to costs: if public and private parties do not contribute jointly to the costs of a project, then one partner’s involvement becomes considerably reduced (which also is likely to result in a reduction of risks). In that case, cooperation may be managed by a contract, i.e., by hiring a private party to do a job

for the government. In other words, the absence of one or more shared elements in a partnership may change the nature of public-private collaboration significantly – normally from a partnership-type interaction to contracting public services out to a private firm. From the perspective of shared responsibilities, this definition accurately captures the collaborative nature of a PPP as opposed to hiring a private company for implementation of a public sector task.

Having discussed the understanding of a PPP, it is useful to identify the reasons of why partnerships are formed. This will allow to capture the difference between the approach described in the Western literature and employed in OECD countries with approaches employed in Kazakhstan and Russia.

## 2. Reasons for Partnering

As PPPs are often associated with a number of advantages, it is worth discussing what benefits partnerships may bring. PPPs also have shortfalls that will be discussed in the next section.

There are three major options for infrastructure delivery (although each has many variations): direct public provision, contracting-out, or public–private partnerships (Vining & Boardman, 2008).

The literature thoroughly explores numerous reasons for partnering. Hofmeister & Borchert (2004) point out that in most cases economic efficiency and effectiveness are the only criteria. Although the discussion of some specific benefits related to PPPs takes place in the literature, the majority of scholars commonly embrace the “value for money” perspective when they discuss advantages and disadvantages of PPPs (Kakabadse et al., 2007).

Value for money (VfM), when applied to a PPP, means that a PPP is supposed to bring larger value for the money that the public sector spends, compared to when services are provided ‘in-house’ (by public agencies) or when services are contracted out to a private company. The underlying logic is that using a PPP will make sense, in the opinion of many, only if a PPP can deliver public sector services cheaper and better, meaning with smaller costs as opposed to other options, and with improved quality (and other enhanced output features) as opposed to other options. If value for money is not there, for example, when government costs of the PPP project are higher than costs involved in the direct public service provision, a PPP should not be employed.

The same notion is supported in a different way: whilst government considers whether to employ a PPP, the overarching aim should be to get a good deal for the taxpayer (Colman, 2000). If it is not, two serious risks to value for money can arise: that government attention will be focused on executing the process rather than achieving a good outcome; and that government attention will focus on reaching agreement on a deal and not on getting a good deal (Colman, 2000, p. 73).

The comprehensive definition of value for money is available in the U.K.’s Her Majesty’s Treasury *Value for Money Assessment Guide*: “Value for money is defined as

the optimum combination of whole-of-life costs and quality (or fitness for purpose) of the good or service to meet the user's requirement. The term whole-of-life is used to refer to the lifecycle of the good or service. VfM is not the choice of goods and services based on the lowest cost bid" (Her Majesty's Treasury, 2006, p. 7).

The VfM concept allows public agencies to compare the costs of a planned PPP project with the cost of the same project, if it is going to be accomplished through traditional procurement. The definition above puts emphasis on the need to take into account the lifetime project costs, and also the quality of a good or service, making the output specification (which is a PPP property discussed earlier in this literature review) an important partnership feature. A trade-off between lifetime PPP project costs and service quality is in the core of the VfM concept.

Having discussed the VfM assessment methodology and its application, Morillos & Amekudzi argue that, despite its usefulness, the government should look at the broader picture. "Although the VfM assessment can be used to determine whether to pursue a PPP, public agencies must be aware of the complexities of the overall PPP process and the limitations of the VfM methodology. It is important for agencies to realize that VfM cannot be the only factor in the decision to pursue a project as a PPP; they must evaluate their own capacity to manage such large, complex, and long-term projects aside from what the final value might say" (Morillos & Amekudzi, 2008, p. 125).

In the conclusion above, the authors acknowledge the limitations of the VfM assessment methodology. Additionally, two other implications can be drawn from their observation. The first is that authors do not imply in any way that other factors noted by many (such as an ability of a PPP to innovate, or superior management and technological expertise that a private company brings to a PPP, or the possibility for government to faster meet the needs of infrastructure development) can take precedence over value for money. Although VfM is not the only basis for making a decision to employ a PPP, VfM remains the most important factor. The second implication is that the lack of government own capabilities to manage large scale long-term projects may be a limiting factor. Even if value for money is identified in a prospective PPP, a public agency may opt to not pursue the project in the PPP form and may look for other ways of how to accomplish a public sector task.

In addition to value for money, there are other reasons for employment of partnerships. Synergy that PPPs create as a result of mobilization of public and private resources is often noted (Brinkerhoff & Brinkerhoff, 2004; Sedjari, 2004). Other reasons for PPPs include the use of comparative advantages and rational division of labor; multi-actor, integrated solutions (which means that few public agencies, few private firms and few financial institutions can join forces for the implementation of a specific task); and engagement in open decision-making processes to promote a broader operationalization of a public good (Brinkerhoff & Brinkerhoff, 2004). The latter can be described as follows: as the partnership ability to deliver a specified output (goods or services) becomes a strong factor in deciding on the PPP value for money, involving final users in the discussion regarding what public goods they need and what

the service requirements are will be useful for the enhanced transparency and greater efficiency of the public sector.

Other advantages of PPPs include: the use of private funds and know-how for the implementation of public tasks; insourcing private expertise in various fields including advancements in business as well as technology; and improvement of management capabilities of the public sector (Hofmeister & Borchert, 2004). Regarding the latter feature, the government, whilst employing PPP, can learn from its own experience and use the knowledge and skills of the private sector partner for the better service provision in the future and/or in other regions, and/or in other sectors, thus improving the public sector management. Partnerships, through involvement of the private sector, may accelerate the implementation of projects and innovation in service delivery and technology used (Morallos & Amekudzi, 2008).

Among other driving factors for partnerships, there is an argument that PPPs enable public agencies to transfer a substantial amount of costs to the private sector. PPP advocates endorse the persuasive argument that people will either obtain some public services with the use of private partners and private funds, or not. "The ability to shift the government's financial burden of providing and maintaining facilities and services is a major driving force especially for nations and states facing funding strains on their infrastructure budgets" (Morallos & Amekudzi, 2008, p. 114). This note applies to transition countries including Russia and Kazakhstan as their infrastructure is in great need for upgrading and development.

This argument in favor of PPPs – the increased use of private funds – has yet another side: it allows the government to greatly reduce its own borrowing and move some projects off the public sector books. Sadka argues that PPPs can be seen as a means to disguise conventional contracting undertakings that are subject to standard budgeting processes as some new undertakings that are carried out off budget (Sadka, 2007, p. 2).

Thus, when PPPs are employed, the cost of capital-intensive projects such as those in infrastructure will be borne by the private sector, and will not be counted as public spending. In many countries, especially in the European Union that restricts the size of its member-states' public debt, this is a strong incentive, from the government perspective, for the use of partnerships. In February 2004, a ruling by Eurostat, the Statistical Office of the European Commission, stated that the assets involved in a PPP should be classified as non-government assets (Hall, 2008, p. 5).

Another concept that focuses on the benefits of public service provision through a PPP is derived from transaction cost economics (TCE). TCE uses total social costs and their minimization as a criterion regarding which option for the public service provision to choose (Vining & Boardman, 2008).

Total social costs are defined as production costs incurred in service provision (including construction costs and payments to third parties), plus transaction costs (such as bidding costs and interest payments on loans), plus (net) negative externalities (such as cost of pollution less value of positive externalities such as reduced waiting time), holding quality constant (Vining & Boardman, 2008, p. 149).

The TCE perspective argues that, if the employment of a PPP as opposed to the traditional public service delivery (via direct government provision or contracting out) minimizes the sum of total social costs, a PPP should be preferred. Vining & Boardman emphasize that in assessment one should include all government transaction costs over the whole period of project time that derive from the project even if they do not appear in the project's budget. Also one should include all externalities and account for quality differences although these costs rarely show up in any budget.

The concept of using a PPP if and when it minimizes total social cost has some similarities with looking at a PPP from the value for money concept: both perspectives intend to compare the cost (or value) of a PPP project with some benchmark which is the cost (or value) of a traditional way of the public service provision. Also, in both perspectives not only the use of quantitative methods may be required, but also the application of qualitative methods, for example, for assessment of value of externalities in TCE, or for assessment of effect of a PPP on wider access to public services in the VfM concept.

Concluding the section about the PPP advantages and benefits, it is worth noting that some of them may or may not be realized in a specific PPP project. For example, the PPP ability to innovate for the purpose of larger profit may be not used or used unsuccessfully in a way that will, in fact, raise costs.

Many advantages are potential; they may be achieved or may not. Whether some advantages and benefits will be received or not depends on how a particular PPP project was designed, and under which terms a partnership has been formed. It also depends on how effective a partner interaction is in the course of the PPP project. However, claiming that government should employ PPPs because they possess a number of advantages seems unjustified as advantages are in no way guaranteed.

An objective investigation of PPPs requires a discussion of not only their benefits, but also their disadvantages that follows in the next section. As Russia and Kazakhstan have limited experience with partnerships, some PPP disadvantages may not be observed yet. For these countries it would be beneficial to learn not only from the successful examples in other economies, but also from the PPP failures, and try to avoid mistakes in the future.

### **3. PPP Shortfalls**

Although PPPs may have strong advantages, they may also have some shortcomings. In the literature there is a tendency to stress mainly positive sides of PPPs (Haque, 2004). This section focuses on identification of principal disadvantages associated with partnerships.

One significant disadvantage is that a PPP often costs government more than direct provision of services by a public agency. One of the reasons is that private firms normally are facing higher, than the government, interest rates on loans that they need for financing of the PPP project. Partnerships may be an expensive way of solving the public sector problems because private sector borrowing normally is more expensive,

and in the case of PPP failure, government should bear the full cost of the project (Bovaird, 2004; Kakabadse et al., 2007). In line with the above, Hall argues that “in almost every country in the world, governments can borrow money more cheaply, at lower rates of interest, than the private sector” (Hall, 2008, p. 7).

Sadka explains why financial institutions are willing to lend money to the government at a lower rate (i.e., a “risk-free” rate) than they are willing to lend money to the private sector. This is because banks correctly perceive that the government will not default on its loan, whereas the private sector may (Sadka, 2007, p. 17).

This means that, although it seems that PPP project financing is done by a private company and should not concern the government, eventually all partnership costs will be paid for by the government and/or user charges. Thus, attracting a private sector party in a PPP normally costs the government more than when it opts to provide a service itself. In the case when a private company gets paid by final users, the outcome is the same: end users will have to pay more than what they would have been required to pay if a service is provided by the government.

Higher costs associated with PPPs are a significant shortcoming as they may outweigh value for money, which is the major argument in favor of PPPs.

Additionally, PPPs may lead to erosion of government own obligations for provision of public services (Haque, 2004). This may happen, for example, if quality of service deteriorates over time, and the government fails to correct a problem in a timely fashion. Though later on the government may discipline the private sector partner, the monitoring and control on a daily basis are hardly possible. In addition, customers, when they do not see government involvement in the service provision, may form a perception of the government that it distances itself from the traditional responsibilities.

Other PPP shortfalls include personal and organizational differences between public and private partners that reduce overall efficiency and effectiveness of PPPs, commitment problems (Acar & Robertson, 2004), absence of methods to analyze risks and opportunities, a lack of clearly defined objectives, inadequate control and evaluation mechanisms (Hofmeister & Borchert, 2004), and contract alterations and difficulties in working relationships (Kakabadse et al., 2007).

For example, a public agency assigns a high priority to the quality of customer service and reduction of waiting time for service, whilst a private partner may be more interested in purchasing the equipment that makes the collection of fees easier. A public sector partner may be interested in keeping a user fee stable, whilst a private company may be pushing for raising fees and tariffs for the variety of reasons. Private partner’s commitment to a project may be fading rapidly when a project gets closer to completion, and may transform in unwillingness to properly maintain or upgrade equipment and other physical assets that soon will have to be transferred to the public agency.

PPP drawbacks deserve further elaboration in the Russia and Kazakhstani context, given relatively new and limited experience that both countries have with partnerships, to make sure that policy makers in the two countries can draw useful insights and avoid mistakes.



#### 4. Areas of PPP Operations in Kazakhstan and Russia

PPP operations in Kazakhstan include the transportation sector (railroads and an airport), the energy sector (electrical power generation and transmission), and social infrastructure (city kindergartens). There is a plan to convert in the near future a road from Astana, the capital, to the northern resort area of Borovoye, into the toll road, and give its operation and maintenance to a private company in the form of a concession. Also, there are a few planned projects involving the construction and operation of toll roads. Additionally, there are PPP projects targeting railroad construction, with the goal of establishing a private company to manage, maintain and operate these projects in the form of a concession for 25-30 years. Those include a segment of railroad between Eraliyev and Kuryk, and a segment of railroad between Korgas and Zhetigen (Kazakhstan Public-Private Partnership Centre, 2012). Another PPP project in Kazakhstan is the construction and operation of an international airport passenger terminal in Aktau, also as a long-term concession (Mouraviev et al., 2012, p. 412).

There are three further concessions in Kazakhstan in the field of power supply. One project involves the construction of power lines, power transmission and generation as well as maintenance of a railroad power system for a segment between the Makat and Kandyagash stations in the Aktobe region. The second project includes the construction and operation of an inter-regional electrical grid between Northern Kazakhstan and the Aktobe region. The third PPP project includes the construction and operation of a power station that will use natural gas for power generation in the town of Kandyagash in Aktobe oblast.

Table 1 summarizes available information about concessions that have been approved in Kazakhstan although some of them have yet to become operational.

Table 1 shows that some projects initially approved by the Kazakhstani government have been subsequently put on hold and are being reconsidered. While the exact reasons were never disclosed, this leaves just three PPPs active (number 1, number 2 and number 7 in the table) out of seven that were designed and planned for implementation.

In Russia, PPP operations are broader, compared to Kazakhstan, and include transportation (both railroads and toll roads, airport construction and management, sea ports, for example, construction of a toll highway from Moscow to St Petersburg, reconstruction and operation of Pulkovo airport in St Petersburg); urban and regional infrastructure (such as reconstruction of a water supply system in Perm (i.e., Permskaya oblast); construction of water purification facilities in Petrozavodsk and the Republic of Karelia; construction of a refuse recycling plant in Yanino in Leningradskaya oblast; and housing construction such as “Simbirskoe Koltso” in Ulyanovskaya oblast and a similar project in Krasnoyarskaya oblast (Public-Private Partnerships in Russia, 2012; Northern Capital Gateway, 2010; Mouraviev et al., 2012). This paper focuses only on the drivers for contractual partnerships, although the PPP lists at the Federal, regional, and municipal levels also include the large number of projects that may be categorized as institutional PPPs or may even lack PPP features such as special economic zones for technological development (Public-Private Partnerships in Russia, 2012).

TABLE 1. PPP projects in Kazakhstan as of March 2012

No	Project title	Project cost (U.S. dollars)	Concession term	Project status
1	Construction and operation of interregional electrical grid from Northern Kazakhstan to Aktobe region	\$165.82 M	17 years, from 2005	Concession contract signed 28 December 2005. Construction phase has been completed; services are being provided
2	Construction and operation of the passenger terminal of international airport in the city of Aktau	\$65.5 M	30 years, from 2008	Concession contract signed 3 December 2007. Construction phase has been completed; services are being provided
3	Construction and operation of a railroad segment between Yeraliyevo station and Kuryk station	\$63.06 M	23 years	Concession contract signed 14 December 2007. Construction has been postponed
4	Construction and operation of the power system for the railroad segment between Makat and Kandyagash stations in Aktobe region	\$350 M	23 years	Concession contract signed 14 December 2007. Project is on hold
5	Construction and operation of natural gas power-generating plant in the town of Kandyagash in Aktobe region	\$146.52 M	20 years	Concession contract signed 7 April 2008. Construction has been postponed
6	Construction and operation of a new railroad between Korgas station and Zhetigen station in South-East of Kazakhstan	\$775.4 M	28 years	Concession contract signed 18 April 2008. Project is on hold
7	Construction and operation of 11 kindergartens in the city of Karaganda	\$40.5 M	14 years	Concession contract signed 16 November 2011. Construction has started

Source: adapted from Tilebaldinov, 2008; Kazakhstan Public-Private Partnership Centre, 2012; Regional Centre for Public-Private Partnership of Karagandinskaya Oblast, 2012.

In 2011, a number of concessions at the municipal level in Russia exceeded 200; in addition, there are two concessions at the regional level, and two at the federal level (Bazhenov, 2011, p. 6). The rapid growth in the number of concessions is summarized in Table 2.

The dramatic increase in the number of concessions over just two years, as Table 2 shows, is indicative of the direction of the public policy

TABLE 2. Number of Concessions in Russia, 2009–2011

	January 2009	January 2011
Federal level	0	2
Regional level	0	2
Municipal level	23	200

Source: compiled by author from Varnavskiy et al., 2010, p. 47; Bazhenov, 2011, p. 6.

aimed at enhanced employment of partnerships, particularly at the municipal and regional levels, although the latter is clearly lagging behind the former. One reason is that regional projects are likely to be larger and more expensive than municipal. Difficulties with finding investors and obtaining financing explain, in part, the slower growth in the number of regional partnerships in Russia. Other reasons will be discussed in section 7 later in this article.

## **5. Internal and External PPP Drivers in Kazakhstan and Russia**

In this section, principal PPP drivers are categorized and examined in detail.

The discussion of background for PPPs, from the philosophical perspective, is normally lacking in the Russian language literature. Instead, three items are usually pointed out, namely, that partnerships are broadly used in many Western as well as transitional countries; PPPs are associated with perceived benefits (which will be discussed below, in the section regarding reasons for partnering emphasized in the Russian language literature); and governments in Russia and Kazakhstan have already approved PPPs as a policy tool for the long run. These three arguments are used in the Russian language literature as a typical justification for partnerships.

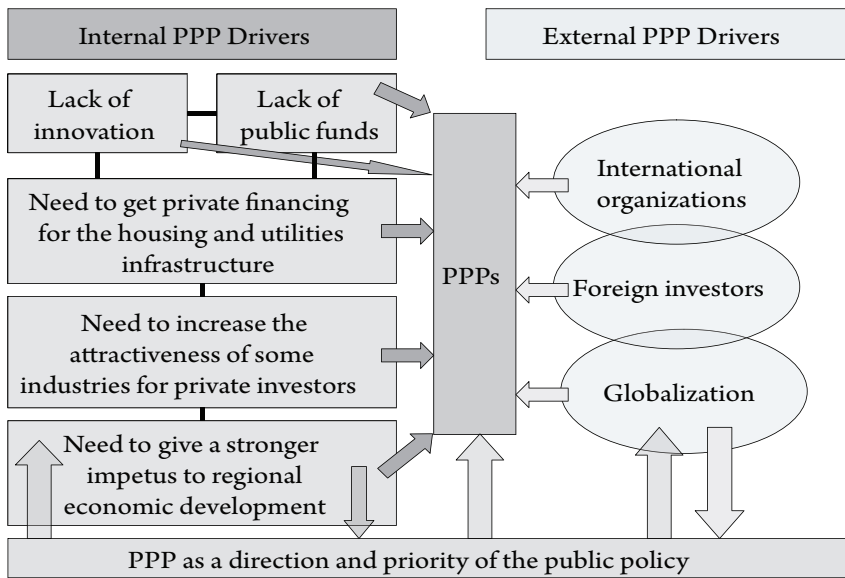
However, some insights regarding the background for PPPs are available: it is argued that effective cooperation between government, business and civic groups in Russia is lagging behind that of industrialized nations, and is likely to be at the very beginning stage (Alpatov et al., 2010, p. 17). The same applies to Kazakhstan, perhaps to the higher extent, due to authoritarian trends in government and underdevelopment of the civil society.

Many authors claim that there is general lack of trust between the business community and government (Kabashkin, 2010; Pankratov, 2010, p. 86; Varnavskiy et al., 2010), which means that private companies often are not interested in getting engaged in the long term cooperation with the public sector. Thus, lack of trust between businesses and government can be considered the background for PPPs. To reverse this situation, partnerships are viewed by government and academics as a policy tool that would ensure closer collaboration between the public sector and the private sector.

However, it is insufficient to explain PPP development in Russia and Kazakhstan just with the government approval of partnerships as a policy tool. In order to understand what factors contribute to the enhanced employment of partnerships, it would be useful to identify principal internal and external PPP drivers, which is the purpose of this section.

In Figure 1, PPP drivers are summarized and divided in two groups – internal and external. There are five internal, and three main external drivers. PPPs as a priority tool in government development policy are pictured in Figure 1 as a background factor that supports and enhances other drivers, both internal and external.

Figure 1 shows interrelations between all the factors that drive the PPP development. For example, there is a certain pressure on governments in Russia and Kazakhstan from



Source: compiled by the author.

FIGURE 1. Internal and External PPP Drivers in Russia and Kazakhstan

foreign investors supported by international organizations. In turn, this enhances the influence of globalization processes on the public policy in the direction of broader employment of partnerships. At the same time some public policy actions (such as selection of a concession as a preferred PPP form) are supposed to align Russia and Kazakhstan with perceived globalization processes.

All drivers pictured in Figure 1 are discussed in detail below.

### 5.1. Internal PPP Drivers

The discussion of internal factors that act as stimuli to the enhanced employment of partnerships in the Russian language literature is normally brief and does not involve any serious justification of either factor. In other words, driving factors for PPPs are considered to be given, obvious, and not subject for much debate. This can be explained with the notion that, perhaps, the strongest internal PPP driver in both Russia and Kazakhstan is the public policy that includes statements that the PPP employment is the government priority in collaboration between the public and private sectors for the long run.

In particular, in the Conception for the Long-Term Social and Economic Development of the Russian Federation to 2020, which was approved by the Russian government in 2008, development of institutions and tools of public-private partnerships has been determined as a strategic direction (Alpatov et al., 2010, p. 7). In 2008, the Kazakhstani government approved the Conception for Development of Public-Private Partnerships for 2009-2015. This policy document has assigned a priority to the expansion of sectors for PPP employment as well as to the need for expanded use of various

partnership tools and mechanisms (Conception for Development of Public-Private Partnerships in the Republic of Kazakhstan for 2009-2015, 2008, pp. 18-19). In addition to railroads and the energy sector, the document calls for the use of PPPs in such sectors as water supply, education, health care, penitentiary system, utilities and housing infrastructure, and urban transport infrastructure.

In turn, public policy as an internal driver of a comprehensive nature is grounded in other, more specific drivers. Among these drivers two are most traditional and can be applied to most countries in the world. They include lack of public funding and the intention to get greater access to private funds; and lack of new technology and anticipation that private firms will bring along technological, management, and other kinds of innovation (Alpatov et al., 2010, pp. 16-17; Kabashkin, 2010, pp. 9-11, 18-19, 30; Pankratov, 2010, p. 32; Varnavskiy et al., 2010, pp. 29-30).

Three other drivers are more relevant to the Russia and Kazakhstan context. They include the need to get private financing specifically for the housing and utilities infrastructure; the need to increase investment attractiveness of selected industries; and the need to give stronger impetus to regional economic development.

#### *A Need to Get Private Financing for Utilities and Housing Infrastructure*

As Figure 1 shows, one internal factor is a commonly shared assumption that PPPs may improve conditions in the housing sector which includes housing itself and housing and utilities infrastructure, such as water and energy supply, sewerage, supply of natural gas, and heating systems (Kabashkin, 2010, pp. 14, 17). This requires additional comments as follows.

As most people in both countries live in apartments, not individual homes, during the Soviet time all these systems were designed as centralized, meaning that delivery of services is done from some central source historically owned and managed by a government agency. A typical illustration of the centralized service delivery is apartment heating. Aside from water for household needs, a family in its apartment receives, from the centralized water heating service, hot water that goes in heating units in each room; for this service a family normally pays a public agency a flat fee per month. As these facilities were built in Russia and Kazakhstan 50-60 or more years ago, they have become outdated and require extensive renovation and upgrading. As a result, the need to get private investment in housing and utilities infrastructure is often named as a major driving factor in favor of PPPs (Kabashkin, 2010, pp. 29-30).

#### *A Need to Increase Attractiveness of Selected Industries for Private Investors*

One more internal PPP driver that also has country-specific nature and applies to both nations is that governments, with the help of PPPs, aim to increase the attractiveness of some industries for private investors. Naturally, this driver is closely connected with the first one as housing and utilities infrastructure is the sector that needs private investment most.

However, the range of industries that would significantly benefit from private investment is broader and includes railroads, automobile roads, regional and local airports, health care, child care, sports and recreation, and education.

To raise financial attractiveness of a project in a selected industry means, according to the Russian language literature, that the government should pay a part of the project cost (Pankratov, 2010, p. 88). In a view of some authors, government support of a PPP project should be, as a rule, extensive and may take many forms such as a subsidy to a private partner's capital expenditure, periodic payments to an operator, tariff subsidization (i.e., part of the tariff is paid by citizens, whilst another part is paid by the government), and the government guarantees for private partner loans and bonds. Pankratov (2010, p. 80) suggests that the government should play the role of a guarantor in a PPP.

Similarly, it is argued that extensive government financial involvement in a partnership is one of the principles of PPP formation and operation (Varnavskiy et al., 2010, p. 26). Although calling the government financial support to a private partner 'a principle' seems to be lacking justification as this significantly increases public sector risks and costs and may undermine partnership's value for money, this approach is indicative of the typical understanding of the role that the government is supposed to play in a PPP, specifically from the financial point of view.

#### *A Need to Give a Stronger Impetus to Regional Economic Development*

Yet additional country-specific PPP driver is the need to give – with the use of partnerships – the greater impetus to the development of regions (as opposed to projects aimed at improvements in major cities, such as renovation of airports, or construction of bridges and tunnels). This task is common for both Russia and Kazakhstan (Alpatov et al., 2010, p. 26; Pankratov, 2010, p. 96; Varnavskiy et al., 2010, pp. 180-194).

The policy response to this need is that both countries currently are pushing for the formation of regional government-owned PPP centers that would provide institutional structure for project selection, preparation, and implementation monitoring. As of January 2011, in 15 regions in Russia (out of 83 regions total) PPP centers have been formed (Bazhenov, 2011, p. 11), although only one has been formed in Kazakhstan – Regional PPP Center of Karagandinskaya oblast (Regional Center for Public-Private Partnerships of Karagandinskaya Oblast, 2012). It is expected that regional PPP centers would integrate with regional governments in order to ensure more effective and faster project selection. Overall, PPP centers have been assigned the facilitator role for regional partnerships and are supposed to guide participants through the preparation and project approval process and help them to arrange proper financing.

There are three external factors that spur employment of partnerships including influence of international organizations, pressure from foreign investors and, in a more general way, globalizations impulses.

## **5.2. External PPP Drivers**

### *Impact of International Organizations*

In Russia the impact of international organizations has concentrated in the joint project of the United Nations Development Program (UNDP) together with the Russian government-owned Vnesheconombank. One of the departments of the latter is the national PPP Center which is charged with responsibility to serve as a government financing and coordinating vehicle for partnership development. The joint UNDP-Vnesheconombank project has been designed for five years from 2010 to 2014. Its major aim is development of Russia's potential for PPP projects, and its activities include training of staff, consulting and assistance to regional PPP centers, and preparation of the model projects in water supply, refuse management, energy supply, transport infrastructure, and social infrastructure. In addition, the project is aimed at providing recommendations for drafting regional laws and regulations that would allow extensive employment of PPPs (United Nations Development Program, 2009, pp. 3-4). Although it is premature to evaluate the project's impact, its goals clearly address a few core impediments to development of partnerships in Russia, i.e., virtual absence of regional legislation governing PPPs, lack of qualified staff, and lack of pilot projects the experience of which would allow to employ some typical financing and management solutions, relevant to a particular sector such as water supply.

The same core impediments exist in Kazakhstan as well, although no international organization has come up yet with a similar PPP development project. It is worth noting that the UNDP project in Russia has yet additional goal of contributing to the formation of the Regional PPP Center for the Countries of the Commonwealth of Independent States (CIS). The project has acknowledged Russia's growing role in the CIS and intends to use the Russian experience for the promotion of PPPs in other CIS countries including Kazakhstan (United Nations Development Program, 2009, p. 5).

Kazakhstan has been included in a technical assistance project (2010-2012) of the Asian Development Bank (ADB) aimed at preparation of road maps for Central and West Asia in three sectors including energy, transport, and urban services (Asian Development Bank, 2010). A road map is defined as a strategic plan for both ADB and government which will enable better decisions to provide innovative solutions to sector challenges.

Describing these challenges and the need for technical assistance, the ADB report states that "reforms are needed to improve the efficiency of service provision and to allow the private sector to participate" (Asian Development Bank, 2010, p. 1). Among its goals ADB has declared the improvement in "delivery of infrastructure services that will create an enabling environment for public-private partnerships and private sector engagement" (Asian Development Bank, 2010, p. 3). As ADB works in tight collaboration with national governments and, in addition, Kazakhstani government is co-financing this project, it is fair to argue that the ADB goals are synchronized with those of Kazakhstani public policy. Thus, this international financial institution is likely to impact Kazakhstan in the direction of increased employment of partnerships.

### *Pressure from Foreign Investors*

Among other external PPP drivers there is pressure that comes from foreign investors who are interested in using new business opportunities in transitional countries. The use of foreign investors in Russia and Kazakhstan possesses a number of advantages: foreign firms may bring along the expertise that domestic companies lack, and financing can be arranged easier through foreign banks and access to foreign capital markets.

An example of foreign investment in PPPs in Russia is Northern Capital Gateway – an international consortium that includes Fraport AG Company (Germany), a leading worldwide operator of airports, Greek investment group Copelouzos, and the Russian bank VTB Capital (Northern Capital Gateway, 2010). The consortium won a contract for re-construction and operation of the Pulkovo airport in St Petersburg, Russia, and the project commenced in April 2010.

In 2007, a Turkish company, ATM Grup Uluslararası Havalimanı Yapım Yatırım ve İşletme Ltd Şti, won a contract for one of the first PPP projects in Kazakhstan – a concession for 28 years that includes the construction and operation of a passenger terminal of an international airport in the city of Aktau (Kazakhstan Today, 2009). Also, in November 2012 the Turkish company called *The 7 Piramit Company* has won the PPP contract for construction and operation of eleven kindergartens in the city of Karaganda in Northern Kazakhstan, in the form of a concession for 14 years (Regional Center for Public-Private Partnerships of Karagandinskaya Oblast, 2012).

These examples show the interest of foreign investors in using the newly opened opportunities in Russia and Kazakhstan.

### *Integration with Globalization Processes*

Finally, a major role in sending external impulses to the PPP development in Russia and Kazakhstan can be attributed to globalization processes. This can be described as a general intention in those countries to align their policies, processes and tools in both the public and private sectors with international trends. The growing employment of PPPs in many countries around the world is deemed as one of those trends. Alpatov et al. (2010, p. 26) indicate that Russia's integration with the world economy is one of the main goals of PPPs. It is argued that the connections between PPPs and globalization are developing in two directions: globalization calls for the enhanced employment of partnerships, especially in transitional countries such as Russia and Kazakhstan because PPPs are viewed as an internationally recognized tool; and partnerships serve as an impetus for further development of globalization processes. The latter, in turn, is explained with the two factors: participation and increased use of foreign investment in domestic PPP projects is considered a sign of openness and internationalization, and the same impact is attributed to the government support of domestic private companies that seek participation in PPPs in other countries (Pankratov, 2010, pp. 30-32).

This becomes more evident in reference to the use of concessions: not only PPPs are deemed a global worldwide trend; moreover, a prevailing use of concessions, as opposed to other PPP forms, is deemed to be an international trend as well.



In summary, in Russia and Kazakhstan there are both external and internal PPP drivers, they possess similar characteristics without any major discrepancies between the two countries, and many drivers are intertwined with and supported by a respective country's public policy which has set PPPs as a long-term priority tool for development of collaboration between government and business.

## **6. Why Partnerships? A Critical Assessment of Claims in the Russian Language Literature**

Disregarding the set of internal and external PPP drivers, the Russian language literature often emphasizes drivers of a different nature, namely (1) intrinsic, in their view, advantages of a partnership, and (2) social significance of a PPP project as a single criterion for whether to form a partnership or not.

The PPP management literature in Kazakhstan and Russia includes claims that a PPP is instantly associated with at least two advantages that are considered intrinsic to partnerships. One is that partnerships are viewed as a tool that brings along technological innovation. The second is that a PPP inherently carries greater efficiency due to the synergy effect.

The link between PPPs and innovation is described in the Russian language literature as a claim that PPPs should be employed because they bring along technological innovation (Varnavskiy, 2004; Pankratov, 2010; Varnavskiy et al., 2010; Firsova, 2011). However, this claim remains unjustified as innovations are in no way guaranteed; moreover, it has to be proven that a certain partnership will produce innovation, and whether the technology that a PPP is going to use is truly innovative, rather than an upgrade. In addition, the criteria of what constitutes technological innovation should be identified. For example, if highly efficient technology is employed at the beginning of the project, and after 20 years it becomes obsolete, although remains in a usable condition for another 10 years, are there enough arguments to claim that a PPP has brought along innovation?

Moreover, the literature is silent that technological innovation may be costly and this may lead to an increase in total PPP costs, and, consequently, rising risks for both government and a private partner.

PPPs are associated with yet additional advantage, namely, greater efficiency due to the synergy effect that stems from partner collaboration. Although the notion regarding combining government resources with the private partner initiative driven by the profit motive, as well as with the private sector funds and business management expertise, is broadly shared in the Russian literature (Zusman, 2008; Pankratov, 2010; Varnavskiy et al., 2010; Firsova, 2011), the explanation of why a specific PPP project may have greater efficiency (compared to when the government implements a project 'in-house' or contracts it out) is often lacking.

At the same time, the literature is silent about overall PPP costs, i.e., aggregate costs of both the public sector and the private sector. As in the Russian language literature the

overall PPP costs normally are not viewed as a concern, this presents an issue, namely, that participation in a partnership is likely to cost all parties more. Some reasons are as follows. For example, a private partner normally gets a loan at a higher interest rate than government because a bank associates a private firm with greater risk; government extends a subsidy that pays part of the project cost; or customers may face higher tariffs because they may be raised to ensure that revenue covers private partner expenses. In either case overall PPP costs go up. Greater PPP efficiency due to the synergy effect, therefore, becomes debatable.

Considering PPPs from the perspective of public policy and public management, it is worth noting that the Russian language literature is silent regarding concerns that the government, by getting engaged in a partnership, is likely to pay more as opposed to the cost of direct government provision or cost of contracting out.

Lack of concerns in Kazakhstan and Russia about overall PPP costs and efficiency is linked to yet another issue, namely, regarding criteria in these two countries for PPP project formation, i.e., criteria to judge whether formation of a partnership is well justified.

The Russian language literature is silent about transaction cost economics, and this theory is not used as a basis for making a decision whether to form a PPP or not. Although overall PPP costs may be higher due to extensive government financial support to a partnership, expensive technology, and higher cost of private partner borrowing, nevertheless, the literature claims that a PPP is a preferred form for collaboration between the public sector and the private sector in both Russia and Kazakhstan (Tilebaldinov, 2008; Kabashkin, 2010; Pankratov, 2010; Varnavskiy et al., 2010; Bazhenov, 2011). This means that in the literature in Russia and Kazakhstan there is general acceptance of a notion that PPPs are associated with higher, not lower, total costs of a project, although the Western literature argues the opposite. According to the KPMG report, government financial support in Russia reaches 20 to 40% of the total PPP project cost, which is significantly higher than in many other countries (10 to 20%). The KPMG report also argues that the cost of contracting out in Russia is about 6% less than the PPP cost (Shabashevich, 2011, p. 3-4).

This suggests that the reasons for PPP employment in the two nations significantly differ from those in OECD countries. In other words, the traditional reasons in the Western countries for PPP employment in Kazakhstan and Russia have been replaced with other considerations. In addition to perceived partnership advantages, the 'social significance' of a project has become a commonly emphasized principal criterion for the formation of a PPP.

Labeling a potential PPP project as 'socially significant' is directly linked to how much administrative and financial support government intends to provide to a partnership. The Russian language literature claims that the nature of government involvement in PPPs is determined by the 'social significance' of a project (Zusman, 2008; Azizov, 2009; Varnavskiy et al., 2010). The government is not supposed to be involved in any PPP project, according to the Russian language literature; in order to justify government

participation in a partnership, a project has to be deemed 'socially significant'. The latter means, in their view, that a project should be implemented in a field or an industry that is significant for population, such as health care or water provision, and the project results are supposed to have positive influence on the standard of living delivering some improvements for people. However, the literature is silent regarding how exactly this significance can be assessed and why one PPP project may be more significant than another, and how improvements for population can be measured.

In addition, project's 'social significance' is not tied specifically to public services; in other words, improvements that a PPP project is supposed to bring along are understood in a broad way and are not focused on anything particular. The following example can be used to highlight this controversy. In the city of Karaganda, Kazakhstan, one approved PPP project targets construction of 11 kindergartens, whilst another proposed project is aimed at reconstruction of water purification facilities (Regional Center for Public-Private Partnerships of Karagandinskaya Oblast, 2012). At the same time, the purpose of yet another, ongoing PPP project in Northern Kazakhstan is construction of power lines and transmission of electrical power across the region (Kazakhstan Public-Private Partnership Centre, 2012). It remains unexplained in the literature (including government reports and policy documents) whether either of the three above mentioned projects has social significance equal or similar to that of another project, and how their social significance differs from that of a PPP project that includes, for example, operation of a toll road.

The principal questions in this theme are as follows. What are criteria for PPP project selection in Russia and Kazakhstan? Are these criteria used consistently across different sectors and regions? Shall PPP project's social importance be employed as a major criterion? If so, how to measure it? Shall technological innovation be used as one of the criteria? Shall various criteria be assigned different weights or ranks? Shall greater importance be assigned to selected criteria such as larger volume and better delivery of public services? In a broader way, what are the implications of including some criteria and excluding others? So far, these questions remain unanswered by the public policy as well as academics in both countries.

## **7. Why is the PPP progress slow?**

This section provides a critical assessment of PPP drivers from the perspective of their influence on the progress with partnership development in the two countries, which allows to prioritize drivers. It also discusses the nature of the government policy regarding partnerships and the role that public policy plays in PPP proliferation. This discussion is complemented by highlighting the contextual factors defining the public policy influence. Finally, this section identifies reasons due to which the PPP expansion appears to be slow at the present time and suggests how development of partnerships can be facilitated.

Among three internal PPP drivers, the need to get private financing for upgrading housing and utilities infrastructure is by far the most pressing. This need is grounded in deeply outdated housing the vast majority of which is the Soviet legacy and in utility infrastructure that was also built often before World War II and requires massive replacement. The contextual factor that explains the burning need for getting the private financing in this field is the colossal size of utility infrastructure overhaul. The enormity of the task, in terms of the dollar amount required for the overhaul, forces governments in Kazakhstan and Russia to argue that getting PPPs with private financing in this field is the only feasible solution. Delays in upgrades are likely to result in more frequent breakages of power lines, or pipeline systems that supply water or natural gas, in high repair costs, as well as disruption of public service delivery to customers. Thus, PPPs become a feasible solution that permits combining the interests of all stakeholders: citizens who need better housing and utilities infrastructure, governments that look for ways of financing the infrastructure renovation, and private firms seeking profitable investments.

The need to increase financial attractiveness of selected sectors to private investors also carries significant value that can be described as complementary to the need for financing the housing and utilities infrastructure overhaul. This is because private investors are needed exactly in this field, and also for other infrastructure projects such as construction and operation of railroads, automobile roads, airports, sea ports, and in the energy sector. What is common in all these sectors is the high cost of capital assets that governments in Kazakhstan and Russia hope to construct or renovate with the help of private investors. Thus, one PPP driver reinforces the other, and their enhanced combined influence pushes governments to seek solutions in the formation and implementation of partnership projects for the purpose of massive infrastructure upgrade.

As opposed to the two internal PPP drivers discussed above, yet another internal PPP driver, namely, the need to create an additional stimulus for economic development in the regions, is associated with much lower influence on partnership proliferation. This is due to the fact that by its nature the responsibility for regional economic development is shared between national government and regional governments in both Kazakhstan and Russia.

Although Kazakhstan is a unitary state, regional governments have their budgets (approved by national government) and are responsible fully or in part for the provision of services such as school education, health care, regional transportation services, water supply, road construction and many others. In reality national government has assigned the bulk of responsibilities to regional governments through the budgetary allocations and intergovernmental transfers. In Russia, a highly centralized federation, sharing responsibilities between federal government and regional governments is also observed and regional governments are funded in a similar way. This means that whilst national governments in Kazakhstan and Russia may push for some pilot projects in selected regions, the principal responsibility for economic development in a region

remains with a regional government because of its close proximity to citizens and its ability to better understand local needs.

In summary, PPPs as an impetus to regional economic development may come into play only after the national government has exhausted its possibilities to form partnerships according to its own, national agenda. However, if and when a region can form a PPP without asking for funds and other resources (such as land) from the national government, the latter is likely to welcome this kind of a partnership. This can be illuminated by an example from the city of Karaganda, Kazakhstan, in which a PPP project that involves construction and operation of 11 city kindergartens was approved in November 2011 much faster and easier than other partnership projects, approved earlier, in which national public sector agencies were involved (Regional Center for Public-Private Partnerships of Karagandinskaya Oblast, 2012). Additionally, the large number of concessions in Russia at the local level summarized in Table 2 (200 in 2011 compared to 23 in 2009) also suggests that local governments are able to form partnerships faster and easier as long as bureaucracy related to national regulations and national agencies is not involved.

Moving on to the assessment of external PPP drivers, it can be argued that Kazakhstan and Russia's intentions to align themselves with perceived globalization trends and international best practices is the most influential factor that facilitates partnership development. Both countries have become highly receptive, in a positive way, to impulses from the rest of the world, particularly to those that would allow Kazakhstan and Russia to claim that they are fully fledged members of the international community. These positive responses to multiple external challenges have become a reality – and an essential part – of government policies.

In turn, the principal reason for these policies is the government's intention to share values with industrialized countries in as many fields as possible because shared values, ultimately, would allow to judge whether a certain country is part of the international community. Whilst in politics or human rights shared values between Kazakhstan and Russia, on the one hand, and industrialized nations, on the other hand, are just emerging, in other fields, such as economy or education, formation of shared values is quite possible, and the two countries are eager to seize each available opportunity including PPP development.

The intention of Kazakhstan and Russia to get aligned with PPPs as an international trend also explains why these countries are receptive to pressure that comes from foreign investors and international organizations. It can be argued that the two countries are interested in getting experience and expertise from foreign firms, which is likely to be true. In addition, the international involvement in PPP projects is by itself an influential factor that legitimizes and facilitates PPP employment in both nations.

However, the effects of internal and external PPP drivers could be substantially smaller if there was no public policy in place. The PPP public policy is the major driving force that furthers partnership development in Kazakhstan and Russia. The two countries started to form their policies at approximately the same time (2004-2005)

and have shaped them in a similar way. The principal commonality is the nature of the PPP policy in Kazakhstan and Russia that focuses on reversing the historical trend of the government political and economic dominance which stems from the Soviet legacy. It is also aimed at overcoming lack of trust in government and corresponding lack of willingness among private businesses to cooperate with public agencies. Whilst Kazakhstan and Russia continue to build a market oriented economy, these goals are deemed useful as they may result in expansion of the sectors in which private firms can successfully operate and use their own, not government, funding. In summary, PPPs are viewed as a strategic tool of collaboration of the public and private sectors for the long run.

The notable feature of the PPP public policy in both countries is that governments are swiftly transforming the PPP debate into the evolving policy paradigm. Although overall PPP costs may be higher due to extensive government financial support and higher cost of private borrowing, nevertheless, the literature claims that PPPs are a preferred form of collaboration between the public and private sectors in Kazakhstan and Russia (Kabashkin, 2010). Thus, the value for money concept appears to be neglected, and it gives place to the PPP policy paradigm.

The elements of this paradigm include the following: the broad government understanding of the meaning of a partnership that includes almost any form of collaboration of the public and private sectors (this applies particularly to Russia); PPP approval process that lacks consistency across regions in a country; unbalanced government approach to perceived PPP benefits in which excessive emphasis is being put on positive PPP externalities, whilst negative externalities are discounted; unjustifiably extensive government financial support to PPPs; unwarranted approach to risk allocation in which government tends to accept excessive and/or unnecessary risks; and strong emphasis on a concession regardless of availability of other PPP forms and the nature of an industry.

The emerging PPP policy paradigm can be viewed as a tool using which governments in Kazakhstan and Russia facilitate the expansion of partnerships. A paradigm assigns selected features to a partnership (noted above), and disregards others. Once the paradigm is in place, the discussion of whether a PPP is a useful form for implementation of the public sector task is largely replaced by accepted approaches and instruments that are deemed undisputed and that provide vast opportunities for employment of partnerships.

However, the progress with the paradigm formation appeared to be quite slow in a sense that governments themselves are undecided how to define certain aspects essential for PPP development. Specifically, governments are lacking typical solutions regarding risk allocation between partners, i.e., who has to bear a certain risk, such as exchange rate risk, land acquisition risk, demand risk, or public acceptance risk (for example, if car drivers are not willing to use a toll road as it was anticipated in a project). In addition, despite government extensive financial support to partnerships, it is still difficult to find private investors who possess required funds and are willing to borrow

significant amounts in order to undertake a project. Also, private banks are reluctant to lend money for a long term such as 15-20 years or longer due to multiple risks including political risk and risk of changes in regulatory environment.

The quick emergence of the PPP policy paradigm has now stalled to a large extent and this backfires the government and its own policy. Unless governments are able to identify typical financial, organizational and risk allocation solutions, the progress with PPP development is likely to be slow. One opportunity to pursue is to let local (and perhaps regional) governments experiment with PPP formation, as long as national funds and other resources are not employed. This may permit to find managerial arrangements and financial solutions, on a smaller scale of a municipality, that national governments are currently lacking. Also, the experience of local governments may suggest what changes in PPP legislation are necessary to facilitate partnership expansion in Kazakhstan and Russia.

## **Conclusion**

This article critically evaluates factors that drive PPP expansion in Kazakhstan and Russia. Among internal drivers, two are of the general nature – lack of innovation and lack of budget financing - and can be applied to almost any country, although Russia puts an unusually (and unjustifiably) high importance on technological innovation that partnerships may bring along.

Three other PPP drivers in the same category of internal factors are contextual and apply specifically to Kazakhstan and Russia as both countries are heavily influenced by the Soviet legacy. These drivers include a need to use private funds for massive upgrading the utilities and housing infrastructure; a need to increase attractiveness of selected industries for private investors; and a need to give a stronger impetus to economic development in the regions. An assessment has shown that the most influential driver among them is the need to get private financing for the massive overhaul of the housing and utilities infrastructure due to the enormity of this task for which governments in Kazakhstan and Russia are unable to raise sufficient funds in the foreseen future.

The paper has identified and discussed the three external factors that foster an accelerated proliferation of partnerships in Kazakhstan and Russia. Among them, the governments' intention to align themselves with perceived international best practices is most influential as it allows the two countries to claim their full fledged membership in the world community because of values shared with industrialized nations. This intention drives many policy actions in the two countries and the PPP proliferation is yet additional example.

The noted PPP drivers have been contrasted to what the policy documents and the scholarly Russian language literature claim to be factors of PPP expansion. These claims include often unjustified association of partnerships with selected advantages that are deemed intrinsic to PPPs such as technological superiority and greater efficiency.

The paper finds that neither the value for money concept, nor transaction cost economics play any significant role as theoretical underpinnings for PPP formation in Kazakhstan and Russia as opposed to OECD countries.

The major driving force for partnership expansion is the public policy that governments in the two countries tend to develop in a similar way and that evolves as a policy paradigm. In this emerging paradigm, instruments and solutions for PPP financing, governance, and risk mitigation are supposed to be readily available, and if so, they may replace any policy debate regarding why and how partnerships may be employed. However, typical solutions and tools for partnership financing and implementation in both Kazakhstan and Russia are lacking at this time, and this is the principal reason due to which the progress with PPP development appears to be slow.

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