

# *Developing labour skills through local content policy*

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## DEVELOPING LABOUR SKILLS THROUGH LOCAL CONTENT POLICY

Over the last decade the Kazakhstani government is adopting strict policy of local content rules. The use of local content may of course develop naturally, but when it does not develop governments may substitute for the actions of private actors. This paper analyses the development of labour skills through local content policy.

**Key words:** *Local content, labour skills, Kazakhstan*

### Introduction

The shift in Kazakhstan towards more assertive market regulation took place in the last decade. It highlighted the common concern of the Kazakhstani government to improve the capabilities of local companies involved in supply and services. This concept of local content is not a new one. «It emerged in the United States in the 1900s, and in the 1920s it spread to the United Kingdom industry» [5. – P. 136].

«Local content» could be defined as the amount of local or indigenous inputs employed or utilised in carrying out all the operations of exploration, development and production of oil and gas<sup>1</sup>. In this paper we will concentrate on expertise, in terms of human resources. Local content builds up the locally owned and adapted knowledge of a community. «It is thus an expression of a community's capacity to appropriate knowledge, and technical and managerial skills, from external sources, and to transmit this on to others in the locality and the broader economy» [5. – P. 136].

There are several strong arguments why governments should be concerned to develop local content in the host country, one of the most important is broadening the knowledge base of local capabilities. For the last decade, in Kazakhstan it has become a fact of life for companies working in the country. In the literature local content policy was analysed extensively by the number of authors Corden [1], Grossman [3], Vousden [9], Hollander [4], Davidson, et.al. [2], Richardson [7], etc. Based on the experience of the other resource-rich countries it is evident that governments can seek to maximise value from the hy-

drocarbon sector through non-fiscal instruments, which include local content and local participation. For example, in «the UK content of orders place by the petroleum industry has increased dramatically since the early 1970s (when it was under 40%) to over 80% in the later 1980s» [6. – P. 600].

The immediate priority of Kazakhstan is to foster stronger local output and employment related to the energy industry itself, and the ultimate challenge is to reduce natural resource dependency. The Kazakhstani government is pursuing the policy of economic diversification, meaning the development of competitive industries of the Kazakhstani economy outside of the hydrocarbon and related sectors. They consider the local content policy as one of the crucial mechanism in the implementation of the diversification strategy. Developing local content could be seen as a step towards building the skills and business networks of the local economy in areas outside the hydrocarbon industry.

As Kalyuzhnova [5] pointed out the general trend in Kazakhstan is to create an environment, which involves local business wherever possible, and to train the indigenous population. Since 1990s in industrial and service sectors of the hydrocarbon industry it was a prevalence of foreign over local companies. The basis of their operations was built on an «expatriate» principle – in terms of human resources. This situation pushed the Kazakhstani government to seek the new avenues of increasing local content. The authorities make all possible to maximise the usage of local labour force, businesses, goods and services, etc.

The crucial question underlying such strategies concerns the level of local capability development and absorption capacity. How rapidly can

<sup>1</sup> «Value creation in the country» is the definition used in Norway and the UK.

the professional skills be transferred to deepen and broaden capability and international competitiveness of local business and labour forces? And how can government policies help foster a spillover to other sectors of the economy?

So far, Kazakhstan is the only case in the CIS countries in which serious attempts have been declared to ensure competitive cost levels in the non-hydrocarbon sector, to reduce the share of hydrocarbon sector in the total national income, and to develop a broad non-oil economy. There is a number of policy measures, including the Programme on Industrial Development (2004), 2010–2014 National Program of forced industrial and innovative development of the Republic of Kazakhstan, etc.

#### **Establishment of legal frameworks**

By designing local content regulations the authorities are hoping to foster a more favourable environment for a «trickle down» of skills and output to host country economies. However, if ill-designed, however, they can lead to significant economic and commercial problems [5]. It could create a less predictable environment for investors as well as increasing their costs; and that there are risks of creating a climate of permanent protection, inferior industry development and infrastructure, etc. All this could lead to the decline of economic growth by consuming the wealth rather than creating value.

Although, it is logical from one hand to seek to capture and extend local value from the hydrocarbon sector by building local capabilities that support the sector's growth, but from the other hand this could become a debatable area between the local governments and operating companies [5].

Since 2001, the Kazakhstani government has been pressing local content requirements (through laws, degrees, labour quotas), as well as obliging companies to invest in social projects around the areas of operations. This has had major implications for the industry in terms of increased participation of the National Oil Company, increased attention to the use and development of local content and local labour.

The companies cannot expect to ignore the local content concerns of the Kazakhstani government, although they tend to adopt a cautious ap-

proach. It is obvious that the companies are profit driven, and therefore, they are often reluctant to invest time and resources in training their local staff for semi-professional and professional jobs, and preferred entry level jobs, skilled jobs, apprenticeship jobs, technical and office jobs. In some cases the scale and the time of the projects/contracts might not be sufficient to make the training viable.

#### ***Case study: Levels of jobs in the oil and gas industry***

There are eight levels of jobs in the oil and gas industry, which required different skills and time scale in training. Supply vessel workers, offshore workers, cooks' helpers, seismic driller's helper, electrician's helpers, survey helpers, equipment operators are required little or no previous experience. This type – *entry level jobs* – is easy to fulfil and it will not cost the companies much resources. Similar situation is with *skilled jobs*. Derrick hand, power tong operator, motor hand, welder, driver, gas utility operator, compressor operator, control room operator are expected to have some training, but not much.

The situation is changing on the third level – *apprenticeship jobs* level. Here, it is expected that the person will be a certified trades person. It is usually four year training programme, where a person is taking a short course and usually gets paid to train on job. It is already quite a demanding task on an employer and required a certain firm commitment over a period of time. The examples from the oil and gas industry are the following: pipe fitter, cook, mechanic, welder, electronics, plumber, carpenter, and electrician.

The next level – *technical jobs* is required a technical college certificate or diploma and the length of the programme required from an employer is one or two years. The jobs of this level expect a quite sophisticated set of the skills and competences, e. g., seismic recording technician, survey technician, petroleum technician, mechanical technician, geophysical technician, instrument technician, etc.

Accounts clerk, secretary, purchasing agent, materials clerk are examples of *office jobs*. These jobs are required at least completed secondary education as well as some training experience.

*Semi-professional jobs* such as warehouse manager, catering manager, safety officer, environmental monitor or drilling foreman are already required at least a college diploma, although it is possible to get these positions through work experience and on – the job-training.

The most of time and resource-consuming are the professional jobs. The prerequisites here are university degrees, which obviously cannot be obtain in a short – run, The examples of such jobs in oil and gas sector are geologist, engineer, research analyst, land surveyor, accountant, nurse, land agent, general manager, human resources, etc.

As it was possible to see from the examples above, the implementation of training programmes would vary, putting different pressures on companies to facilitate them. The role of the governments in this situation is monitoring company training programmes and make sure that the local content element will be sufficient there.

In order to find the optimal balance for the interests of the companies and the governments it is important to have an appropriate legal framework in place, which would be able to reinforce the economic opportunities and incentives facing companies and at the same time to meet up the government's expectations. This is particularly important in the situation when the expatriate employment market in Kazakhstan reached the saturation.

Since the collapse of the Soviet Union Kazakhstan became one of the attractive destination for the specialists in oil and gas: challenging engineering environment, opportunities for young engineers, developing of new technologies. This is relevant for both expats community as well as Kazakhstani nationals.

However, the scope and speed of training local staff should be realistic, it is important to realise that there are significant limitations in this respect. For many locals who came from auls [rural areas] is incredibly difficult to adapt to the new style of life with the working hours from 8 a.m. to 5 p.m. «They could leave work earlier. They cannot tolerate the noise or achieve a quick speed of work. ... To people who are accustomed to livestock-like activities, such «science» is very

difficult. However, some people are adapting to the new conditions, starting to earn good money and became more accustomed to the good life». [8. – P. 26].

Another interesting aspect of local content development in some resource rich countries (and Kazakhstan is not an exception in this respect) is a governmental requirement of companies involvement in social projects, which the governments consider as a form of local content. «That is a debatable area, which is very germane to the issue of defining realistic boundaries for local content and corporate and social responsibility» [5. – P. 142].

One could ask how the involvement into social projects could influence the development of labour skills in the country.

It is clear that supporting local content can only be achieved realistically through an overall integration with corporate and social responsibility and here are the elements of education and training which are in the core of developing labour skills. The practical examples include the creation of Kazakh British Technical University (KBTU) Graduate School by BG Group in Almaty; Zhas Dauren Orphanage programmes, mini MBA training for small and medium-sized enterprises, etc.

BG Group is always invested in personal development programmes in Kazakhstan with an aim to build technical competencies and behavioural skills, and at the same time the company undertook a project of supporting formal education programmes, since this is key to attracting and retaining the best local talent. Therefore, BG Kazakhstan, together with its joint sponsor, Shell, launched a new graduate school at the Kazakh British Technical University (KBTU) in Almaty in 2004. KBTU has partnered with three British universities to deliver a number of postgraduate masters programmes including Human Resource Management and Petroleum Engineering. Since 2006 (the first graduation year) a number of the graduates are working in the Karachaganak venture. From the company point of view such initiatives support the transfer of skills and demonstrate a commitment to broader corporate responsibilities, while also helping to build a pool of

skilled labour from which it can attract future employees.

Another example of the developing of the labour skills is a BG Kazakhstan – the IBC Group Ltd range of development programmes for students at the Zhan Dauren Ophanage in Uralsk, a neighbouring community to the Karachaganak facility in the West Kazakhstan Oblast (WKO). This project includes investment to educational and career development programmes; awards of scholarships to graduates for further study at WKO universities as well as a job placement programme. The latter is in form of internships within the BG Group. That work experience no doubt has enabled young professionals to apply their skills in a real working environment and has assisted in helping them to secure employment.

Mini-MBA trainings for small and medium size entrepreneurs cover information technology, language skills training, book keeping, motivational training and business. Such a programme is enabling young professionals to develop small and medium size businesses within West Kazakhstan Oblast. It is, no doubt, enhance their business skills. BG Group once again employed a practical approach to the demand of the particular skills.

To conclude, the demand and supply of skills provides some economic reinforcement to the development priorities set by governments in terms of training programmes and recruitment, although there are some limitations in this field.

#### ***Goals and the realities of local content implementation***

Different countries are accessing and measuring LC in its own way (at present time we have Brazilian, Kazakh, Nigerian methodologies, etc). Overall, a comprehensive Local Content Indicator (LCI) should include ownership, local content of materials, % of local labour, % of locals in professional and management positions, services (contracts) and local taxes. Depending on the policies and pursuits of the government's LCI is varied focusing on one or another component. One striking fact which is relevant to all resource-rich countries: LC always begins from the governmental demands to increase share of local labour. The operating companies are directed to maximise spending with local suppliers. In Kazakhstan,

the current trend is «to increase nationalisation of the workforce with international suppliers to meet PSA targets as well as to assess demand for specialist financing solutions for SMEs, i. e. innovative investment projects to provide transparent sources of finance» [5. – P. 147].

Basically the governments are trying to create an environment for the enterprise development and training opportunities for local suppliers. A sound enterprise policy should rest on the twin pillars of FDI and domestic SME development. Central to a well designed policy is the notion that vertical linkages should tie local SMEs into the supply chain of foreign enterprises. In Kazakhstan, hydrocarbon-based FDI has been strong, but attracting non-oil FDI is still remaining a challenge. A comparative advantage of Kazakhstan is that the high level of oil and gas-based FDI offers a solid platform for SME development and consequently to develop labour skills.

During the last decade the evolution of developing labour skills within the Kazakhstani LC policy has undergone through several stages. Initially it was a concern with making sure that the true substance of local content is connected to value creation within Kazakhstan. It is a full utilization of oil and gas wealth, together with the capacities established in the service sector, to create a local manufacturing sector (in other words achieving diversification of the economy) – with employment opportunities and with other multiplier effects on the local economy.

Throughout recent years, the industry was experiencing, and in some cases developing itself, a range of different approaches. Some ideas and approaches are emerging on both sides that may contain the seeds of a new partnership between companies and governments in the area of developing new labour skills within LC policy. This was related to developing a new common working culture which should overcome the Soviet legacy. The promotion of Code of Conduct and understanding fundamentally new way of conducting operations and business and indeed treating this as standard contractual terms that all led to the transformation of the perception of the role of labour forces in Kazakhstan. The most common types of breaches are related to inappro-

priate safety behaviour, misuse of company assets, fraud, theft, etc. Therefore, it was important to establish a mechanism in place which would guarantee of monitoring and enforcing of the main aspects of the code of conduct.

So, the new policies were introduced like the Compliance Assurance Policy. It is important that the employees are able exercise their rights to express concern, and are able to identify areas which require attention. That was of course not a case in the culture of the Soviet enterprises. Therefore, it takes some time to adjust and understand full grasp of such possible areas of concerns (safety, conflict of interests, harassment and discrimination, workplace violence, improper use of company assets, etc) which include quite crucial aspects of the day-to-day operations such as government contracts, employment law, international business issues, etc.

For some companies the inclusion of educational elements in their local content programmes was the next step in developing labour skills of their employees. These are mainly related to postgraduate programmes, short courses, training programmes in house, as well as creation of specialised training centres in the regions.

There are no doubts that for the local employees some of these programmes represent big challenges, namely new techniques and methods of work, a weak knowledge of English. The perception of the international staff was that since the companies are hoping to compete internationally, the knowledge of English by local staff is essential (Author's various of interviews in Kazakhstan in 2001–2008). In 2011 Nursultan Nazarbayev, the president of the country stated that by 2020, 20 percent of the population should speak English. It is a very noble desire but would it be implemented or not time will tell.

In addition the local staff is in need to have more time to switch to Western practices in business, including a pro-active approach. It is still the old custom of not questioning a process, and this passivity still remains an obstacle today.

It would be wrong to state that the Kazakhstani nationals do not posses any experience. They do have skills, but what they lack is reaching a level which allow them to meet project

needs and standards. This is where the training is essential and important. This also allows the contractor to increase productivity with the utilization of the Kazakh labour market at minimal cost and time and at the same time reviewing the competence of the workers for future training and future development of the national labour force.

To date the oil and gas companies developed and maintained a standardized training process in partnership with the construction, maintenance and pipeline industries operating in Kazakhstan. The training process itself is portable, meaning that the knowledge and skills learned by students and workers are taken from project to project, from company to company. As industries compete more intensively for fewer qualified worker, a professional, accredited training program that offer industry-recognized credential and a clearly defined career path will attract and retain high-calibre workers. This is how hopefully in the near future Kazakhstan would develop a competitive advantage in labour specialisation and technologies which will be used outside Kazakhstan (similar to the UK competitive advantage-expertise and technologies transfers from the North Sea experience to the Caspian region).

It is obvious that standardized training will create a national pool of construction, maintenance and pipeline workers with documented, portable skills.

In advocating standardized training there are several facts which are important to highlight. Training improves productivity, which increases profitability – that is in a great interest of any management of the company. It shapes the industry as an industry with credible career opportunities rather than just jobs and ultimately career paths defined through standardized training will improve the image of the industry. Corporate commitment to improving craft workforce skills and professionalism increases employee loyalty and motivation while reducing absenteeism and turnover. That would clearly demonstrate a commitment to quality management, providing a critical competitive edge. All this is a first step in developing innovative atmosphere since well-trained workers are more capable of identifying

potential problems and making innovative, cost-reducing solution.

To conclude, a direct benefit of the local content development would be an impact of the training process which should increase productivity, reduced accidents and, in turn, achieve more cost-effective construction, maintenance, and pipeline operations. However, often the benefit of training cannot be seen immediately, and it is only the cost. Companies pay this cost, but it is they who ultimately benefit from the training.

### **Developing sustainable frameworks**

At a broad policy level, governments may seek and industrial spin-offs from oil and gas production, while failing to take key flanking measures on the business environment. Specifically on local content, the Kazakhstani government had already set aggressive targets in the past, however, it was quickly realised that pursuing this approach will raise costs and risks, deterring investors. So the importance of achieving acceptable levels of local content in major hydrocarbon projects is became increasingly evident in Kazakhstan.

The last decade significantly changed the attitudes and perceptions of both parties: companies and government, recognising that LC is a core element in economic development of Kazakhstan and should be approached carefully without hastiness and with realism. The developing of the local skills cannot be happening overnight, and therefore defined strategies and set targets should be realistic and consistent.

In this respect the government should assess carefully the impact of mechanisms to maximize local value-added in the short term, in order to build capability for increased value capture over the longer run. LC requirements influence project design and are certain to influence contracting strategy, which in turn may impact on project costs and schedule.

«For both governments and companies, it is important to realise that increased local content takes time (sometimes longer than is anticipated) and be prepared for risk mitigation and cost sharing incentives» [5. – P. 165]. At the beginning of 2000s when the Kazakhstani authorities tried to force the multinationals to introduce local content elements everywhere, even when it was practical-

ly impossible it proves that this strategy was unsustainable. (Author's interviews in Kazakhstan, 2001, 2003, 2005–2012).

The efficiency of the governmental involvement in promoting a high level of LC with the oil and gas companies operating in Kazakhstan will be defined by the ability of the government to set up a framework that enable the growth of national content via a transparent, self regulating process, which does not deter companies from expanding their operations. The Kazakhstani government has a reciprocal responsibility to understand the contractor. The contractor is looking for leadership from Kazakhstan and the client. LC development requires a collaborative approach between all parties involved in managing resources in today's marketplace.

There are particular questions which might help us to understand the modalities of the development of the LC, namely, how far can the oil and gas industry support the global demand for local content (in particular developing labour skills)? And how are these demands to be balanced against project requirements of budget, safety, quality and increasingly shorter schedules? It would be misleading to answer these questions with Too often these questions are answered with the dry run of the statistics. There are several factors (based on Kalyuzhnova, 2008 methodology) which would be important to take into account in order to provide the answers on the questions above.

First, set of criteria to evaluate LC impact, which takes into account the specifics of project life-cycles in the industry, should be established. Second, the maximisation of LC should be based on identifying opportunities to capture local value added through the selection of specific local staff. Third, a clear strategy is needed to deliver maximum local value by increasing participation of local nationals in appropriate functions, backed by specific training programmes. Fourth, approaches to sub-contracting are needed that increase the scope, over time, to raise the participation of local firms, on a competitive basis. Fifth, there needs to be a definition of possible additional modalities, including aspects of social responsibility.

Kazakhstan already had a deep learning curve in defining LC goals and setting up the rule for competitive advantage and its stimulation. At the stage of awarding companies with contracts, the government is now giving preferences to companies with higher levels of LC and a substantial content on labour skills development, although that must still result in a competitive industry.

A clear and mutually-understood between government and companies will help lay the basis for realistic solutions to «local content» in technical terms. To be effective, such a framework should be based on the following underlying assumptions: «the need for competent contractors, for a competitive process, for real and sustainable national content...» [5. – P. 167].

### Conclusion

Designing a comprehensive programme for local content development which will include a substantial element of developing labour skills by companies in Kazakhstan proves the point that it depends on the willingness, adaptive and flexible attitude of the business to be involved in the economic development of the country of their operation in ways that offer an overall synergy with business goals. These initiatives in Kazakhstan are encouraging signs of creativity in trying to craft realistic but substantive approaches.

At the present time Kazakhstan is undergoing socio-economic transformations, there are changes in the attitudes and perceptions of the population, their view to work, knowledge and code of conduct. Developing the common companies' culture will require time and the commitment of Kazakhstani employees and management. This desire for a common culture and the associated development of the human resources, can be considered as a very particular aspect of the development of LC.

It is important for LC goals to be realistic, but also to ensure that the effects from it would be beneficial for the whole economy. Kazakhstan is attempting to set up environment that is favourable to local manufacturing, and the availability of finance, raw materials and provision for local R&D facilities. This process needs to take place against a background that is investment-friendly and well-disposed towards developing and using competent local suppliers and staff. Here, a proactive role by companies is clearly crucial. Companies need to work with government to focus on changes that make the development of LC a powerful element in the country's strategy over the long run.

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