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TELNO U/N

OF 100557Z AUGUST 90

INFO IMMEDIATE UKDEL IMF/IBRD, PARIS, BONN, WASHINGTON

INFO IMMEDIATE ROME, UKREP BRUSSELS

*If this is to keep our
own businesses going then
at this time it would be wise
to consider it.
On the other hand there would be a
suffer from large sanctions not*

YOUR TELNOS 1399 AND 1400: SOVIET REQUEST FOR BRITISH FINANCIAL ASSISTANCE

GORBACHEV/ELTSIN

1. THE GORBACHEV/ELTSIN REFORM AGREEMENT FURTHER INCREASES THE CHANCES THAT THE SOVIET UNION OVER THE NEXT TWO YEARS WILL UNDERTAKE REAL MARKET REFORMS BASED ON ELTSIN'S '500 DAYS' PROGRAMME. IT ALSO INCREASES THE CHANCES THAT AT LEAST A MAJORITY OF THE 15 REPUBLICS WILL FOLLOW THE SAME REFORM PROGRAMME. BUT THERE IS STILL A LONG WAY TO GO. RELATIONS BETWEEN THE REPUBLICS AND THE CENTRE WILL COME UNDER RENEWED PRESSURE IN THE AUTUMN WHEN THE QUESTION OF THEIR CONTRIBUTION TO NEXT YEAR'S UNION BUDGET COMES UP FOR DISCUSSION. IT MAY WELL PROVE DIFFICULT TO GET SOME OF THE NECESSARY LEGISLATIVE UNDERPINNING FOR THE REFORM PROGRAMME THROUGH THE USSR SUPREME SOVIET. THE PICTURE WILL BE CLEARER BY OCTOBER WHEN THE EC COMMISSION TEAM ARE DUE TO REPORT. BUT A COMPREHENSIVE ASSESSMENT OF THE CHANCES FOR SUCCESS MAY NOT BE POSSIBLE UNTIL THE END OF THE YEAR. THE AUTUMN SESSION OF THE SUPREME SOVIET WILL ALSO HAVE TO GRAPPLE WITH THE COMPLEX AND HIGHLY CONTROVERSIAL ISSUE OF THE NEW UNION TREATY: MUCH OF THE REFORM LEGISLATION THEREFORE MAY NOT GET THROUGH THE SUPREME SOVIET UNTIL NOVEMBER/DECEMBER.

2. DETAILS OF THE '500 DAYS' PROGRAMME - WHICH IS NOW LIKELY TO FORM THE BASIS OF REFORM PLANS - WERE SET OUT IN OUR TELNOS 1276 AND 1277 OF 12 JULY. THE LIKELY TIMETABLE IS FOR A START TO BE MADE WITH PRIVATISATION AND DISMANTLING MINISTERIAL MONOPOLIES THIS YEAR, WITH THE REALLY PAINFUL PARTS OF THE REFORM PROCESS - CLOSING OF INEFFICIENT ENTERPRISES, PRICE REFORM, ETC - BEGINNING IN EARNEST FROM MID-1991. FINANCIAL ASSISTANCE DESIGNED TO ASSIST THE ACTUAL PROCESS OF REFORM THEREFORE IS LIKELY TO BE PREMATURE IF OFFERED MUCH BEFORE THIS DATE. THE POSITION NOW REMAINS AS IT WAS IN THE RUN UP TO THE DUBLIN AND HOUSTON SUMMITS: IE THAT THE SOVIET ECONOMY IS NOT YET IN A POSITION EFFICIENTLY TO ABSORB WESTERN ASSISTANCE. A SOVIET TRADE OFFICIAL TOLD US RECENTLY THAT THE USSR HAD OVER POUNDS 1.5 BILLION WORTH OF UNINSTALLED FOREIGN EQUIPMENT IN THE CHEMICAL SECTOR

ALONE. IF ANYTHING INCREASED REPUBLIC ASSERTIVENESS IS MAKING THE SITUATION EVEN MORE UNCERTAIN : VIZ THE RECENT DISPUTE OVER CONTROL OF BANKS.

3. WE APPRECIATE THAT THERE IS AN IMPORTANT DISTINCTION BETWEEN THE HOUSTON DISCUSSION/IMF AND EC EXERCISES AND RZYHKOV'S REQUEST FOR IMMEDIATE FINANCIAL ASSISTANCE. AS SEEN FROM HERE, THE CASE FOR A POSITIVE RESPONSE TO THE LATTER RESTS ON:

- (A) THE ASSUMPTION THAT, WITHOUT IT, THE SOVIET UNION WILL NOT HAVE SUFFICIENT BREATHING SPACE TO PREPARE THE REFORMS:
- (B) THAT WITHOUT ASSISTANCE THE USSR WILL BE FORCED TO REQUEST FORMAL TALKS ON DEBT RESCHEDULING: (THERE WAS SOME SPECULATION IN THE WESTERN PRESS RECENTLY ON THIS SUBJECT FOLLOWING SOME HINTS IN A GORBACHEV SPEECH):
- (C) THE BILATERAL CASE FOR INCREASING TRADE AND BALING OUT UK COMPANIES.

4. YOU WILL HAVE BEEN LOOKING AT THE ARGUMENTS FOR AND AGAINST THESE PROPOSITIONS IN THE RUN-UP TO DUBLIN AND HOUSTON. OUR CONTACTS SUGGEST THAT MANY SOVIET ECONOMISTS OPPOSE THE IDEA OF UNITED FINANCIAL ASSISTANCE. THEY ARE AWARE OF THE POLISH PRECEDENT AND BELIEVE THAT SUCH ASSISTANCE WOULD INCREASE THE DEBT BURDEN BUT DO NOTHING TO RESTORE THE COUNTRY'S DEEP SEATED ECONOMIC PROBLEMS.

5. WE FIND IT DIFFICULT TO JUDGE THE REAL SERIOUSNESS OF THE SOVIET SHORT-TERM BALANCE OF PAYMENTS PROBLEM. IN THE PAST FEW WEEKS THEIR PUBLIC STATEMENTS SUGGEST INCREASING ANXIETY. GORBACHEV, RYZHKOV AND OTHERS HAVE ON MORE THAN ONE OCCASION, SAID, A PROPOS OF THIS YEAR'S HARVEST, THAT THE SOVIET UNION HAS NO MONEY FOR ANY ADDITIONAL GRAIN PURCHASES. SITARYAN, A DEPUTY CHAIRMAN OF THE USSR COUNCIL OF MINISTERS, SAID TWO WEEKS AGO THAT THE SOVIET UNION'S HARD CURRENCY DEBT TOTALLED 36 BILLION HARD ROUBLES (IE APPROXIMATELY POUNDS 36 MILLION). THE PREVIOUS HIGHEST FIGURE WE HAD SEEN A FEW MONTHS EARLIER WAS 34 BILLION ROUBLES. GERASHENKO, HEAD OF THE USSR STATE BANK, SAID AT A SEPARATE PRESS CONFERENCE THAT THE DEBT-SERVICE RATIO WAS WORSENING - HE DECLINED TO GIVE PRECISE FIGURES.

REACTIONS OF OTHER WESTERN COUNTRIES

6. APART FROM THE FRG'S DM5 BILLION LOAN AND REPORTED OFFERS FROM THE ITALIANS (WHICH INDICATIONS SUGGEST ARE ALSO TO BE TIED TO BILATERAL BUSINESS) WE HAVE BEEN TOLD BY A DANISH BUSINESSMAN THAT HIS GOVERNMENT IS CONSIDERING GUARANTEEING A POUNDS 60 MILLION LOAN TO ENABLE THE SOVIET GOVERNMENT TO SETTLE DEBTS WITH DANISH

COMPANIES. (THIS INFORMATION MAY OR MAY NOT BE ACCURATE IN DETAIL.)

LATEST POSITION ON INDEBTEDNESS TO THE UK

7. WE ARE IN TOUCH WITH OVER 30 COMPANIES WITH DEBT PROBLEMS TOTALLING APPROXIMATELY POUNDS 50 MILLION. ECGD IS IN TOUCH WITH A FURTHER GROUP OF COMPANIES. TOTAL UK DEBT MAY BE AROUND POUNDS 80 - 100 MILLION.

8. THESE DEBTS ARE CURRENTLY BEING PAID OFF AT A VERY SLOW RATE AND SEVERAL COMPANIES ARE FACING IMMINENT BANKRUPTCY. THE RYZHKOV PROPOSAL COULD BE SEEN AS A REQUEST TO CONVERT THESE PRIVATE OUTSTANDINGS TO STATE DEBT AND, IN A SENSE, THEREFORE, TO RESCHEDULE IT.

KNOW-HOW FUND

9. IF THE SUBSTANTIVE RESPONSE TO RYZHKOV IS TO BE NEGATIVE, WE ASSUME THAT EVERYTHING POSSIBLE WILL BE DONE TO COUCH THIS IN AS SUPPORTIVE LANGUAGE AS POSSIBLE. THIS COULD DRAW ON IDEAS FROM THE PARTNERSHIP PROGRAMME WORKED UP IN PREPARATION FOR THE PRIME MINISTER'S VISIT BUT NOT PURSUED AT THE TIME BECAUSE OF DOUBTS ABOUT THE FUTURE OF THE SOVIET UNION REFORM PROGRAMME. THIS COULD INCLUDE THE SORT OF IDEAS INCLUDED IN THE NON-PAPER LISTING AREAS IN WHICH THE US WOULD BE PREPARED TO OFFER TECHNICAL CO-OPERATION WHICH BAKER GAVE SHEVARDNADZE IN PARIS. THIS WOULD HAVE TO AVOID THE RISK OF PREEMPTING THE EVENTUAL UK RESPONSE TO THE RECOMMENDATIONS OF THE COMMISSION AND THE IMF.

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