

*This is the original draft of the telegram which I sent on the IMF and economic policy. The computer in my office could not link to our communications equipment, so after I drafted it on my word processor, Jackie or Karen had to type it again into comms. While they were doing this, inspiration struck and I went down and added to the end of the telegram by hand.*

Craig Murray  
May 2006.

Subject: IMF/Uzbekistan: A fake reform programme

## Summary

1. IMF mission in town to assess progress on SMP following two month extension. The reform process is a sham. Crash Uzbek measures immediately before IMF arrival designed to impress not to stick. FDI has dried up and investors are voting with their feet. Gap between black market and official exchange rates not closing. US push for politically motivated IMF approval could have disastrous long term consequences for development and the region.

## Detail

2. The IMF are currently visiting to assess Uzbek progress in the two months since they were given a second chance to meet the requirements of the SMP. They will find no progress at all on the key issue of currency convertibility. On the target of narrowing the gap between the black and official exchange rates to 20%, it had remained between 40 and 50% throughout the two month period until falling to around 25% in the last week due to a series of quite extraordinary measures.
3. Notoriously before the June IMF visit the Uzbeks flooded the bazaars with cash dollars to cause a temporary exchange rate blip. This time they have hit on the cheaper expedient of physically closing down the bazaars. On 1 September the largest bazaar and main source of imported goods, the Hippodrome, was summarily closed for "repairs". In the last week all the main bazaars selling imports have been shut down and hundreds of traders raided by the police to check documentation. If this is not in order (ie nearly all the time) the goods are confiscated plus the trader is fined in hard currency the value of the goods again.
4. Simultaneously an emergency import tax of an additional 30% was introduced on all except medical items, on top of existing tariffs of 50% on food and 90% on non-food goods. Not surprisingly these extreme measures to halt imports have reduced dollar demand short term and led to a fall in the black market rate; but no one doubts that they are unsustainable and highly temporary measures designed again to produce a temporary blip for the IMF visit. Uzbekistan's unreformed post-Soviet economy does not produce consumer goods for import substitution and a long term solution needs a devaluation and early abolition of the official rate, not an artificial strengthening of the Som on the black market.
5. The government claims to be moving towards currency convertibility by the end of this year, but it is unclear that it understands the concept. Certainly nobody in the dwindling business and financial community believes that you will be able to walk into a bank with som and walk out with dollars. Lack of convertibility and consequent inability to repatriate profits, together with bureaucracy stifling every transaction and pervasive corruption, have led to most smaller foreign investors giving up and quitting. Every single one of the Ambassadors on who I have paid courtesy calls has concurred that their resident business community has reduced in

the last five years, usually by well over 50%, with smaller investors bearing the brunt.

6. British American Tobacco are a good example of what can go wrong. Our 300 million euro showpiece investment, they have received negligible currency allocation to allow them to remit profits. In desperation they purchased a locally built Ilyushin 76 aircraft for some to literally fly some of their profits out – they planned to sell it outside the country, only to discover that no-one wants to buy an Uzbek Ilyushin for hard currency. They have also been let down by the Uzbek government which has broken promises on tax and prevention of smuggling.
7. Another 45 million euro British project, Sergily Building Materials, which included 10 million euro of EBRD financing, failed when the Uzbek government reneged on a contract to purchase much of the product. It reneged by the simple expedient of dissolving the parastatal which had signed the contract and reconstituting it with a new name. The EBRD is currently negotiating to let the Uzbek government have the 10 million euros of equipment supplied for a great deal less than it cost, on the grounds that the British venture having been bankrupted this is the only way for the EBRD to recoup some of its loan. This is, frankly, appalling. I hope it gets a mention at the EBRD Conference in Tashkent next spring.
8. Both BAT and Sergily suffer from not making corrupt payments, and not in particular involving members of President Karimov's family. Coca-Cola and Case New Holland, for example, are closely associated with the President's daughters and featured prominently on the list of those who had no difficulty getting and remitting dollars at the official rate, along with the trading companies connected with the Karimov oligarchy. Coca-Cola have recently fallen spectacularly from grace after the MD of the Uzbek franchisee divorced the President's daughter. In a deposition to an US custody court on 12 September the MD claimed that Coca-Cola and his other business interests in Uzbekistan were subsequently subject to constant government harassment – in fact they just joined the ordinary foreign investor in that position.
9. When I met the British Business Community it is fair to say that many regretted their investment. FDI has all but dried up except where there is offshore hard currency income (Oxus). The EBRD, for example, cannot find viable private sector partners and in 2001 92% of its lending was into the public sector. 48% of its overall portfolio is public sector, and the two largest schemes in its private sector portfolio have failed spectacularly.
10. One of the raft of reforms just passed for the IMF is the abolition of the list of companies who get priority foreign exchange allocation. But with a false exchange rate rationing will still happen – it will now be done by the commercial banks not the government, but the “commercial” banks are of course state-owned. EBRD who have had terrible problems using them as a conduit for SME finance because their lending decisions are corrupt and political, not commercial, so they will simply favour the oligarch firms who were on the “abolished” list. It is a pretence at reform.

11. The same is true of cotton. In another IMF prescribed measure President Karimov has announced that farmers may sell half their cotton privately and need only sell half to the state. But how meaningful is this when the farms themselves have not been privatised and the farmers are, in effect, serfs? I have been told by member firms of the Liverpool Cotton Association that the state purchasing body is preparing forms for farmers to sign "voluntarily" selling the other half of their cotton to the government.
12. The list of sham reform goes on. Import licensing will be abolished, but the correct import documentation has to be submitted and approved in advance. Not import licensing, of course.
13. In 20 years in power, 11 of it in charge of an independent country, Karimov has overseen extraordinarily little economic liberalisation and I see no reason to believe that he has changed his views now. The only two people I have met in three weeks who profess to believe that Karimov really intends to introduce genuine market reforms are the US Ambassador and the MFA press spokesman. I do not see how, with even the slightest scrap of integrity, the IMF can approve this so-called reform programme. I have worked on economic affairs in post-communist transition economies and in developing countries. This country is not in transition and is not developing.
14. I have asked the views of my diplomatic colleagues as I paid my courtesy calls. Let me be very plain about this next point. I have been told separately by the World Bank and EBRD resident representatives, and by the French, German, Italian, Slovak, Czech, Polish, Indian, Pakistani and Russian Ambassadors that a political deal has been reached in Washington, post September 11, that in return for American use of Uzbek air facilities the IMF would approve the Uzbek economic programme (after pulling out in disgust two years ago). The World Bank rep and the Russian Ambassador (both angrily), plus the French, Italian, and Pakistani Ambassadors (cynically) and the German and Czech Ambassadors (sadly) made explicit their view that this meant approval would be given whether the Uzbeks deserved it or not.

## COMMENT

15. The German Ambassador pointed to a painting on his wall named "Illusion". He said that if you went to the theatre to see an illusionist you all enjoyed the spectacle of seeing a man walk on air. You knew it was really impossible, but to remove the curtain would spoil the show. When the IMF came we would all be at the theatre marvelling at the reforms and agree not to look behind the curtain.
16. Which is a good analogy but a stupid idea. This is not an entertainment but affects real lives – especially the poor of Uzbekistan, who have African levels of poverty in this terribly unequal and appallingly governed society. Without real economic reform soon poverty will worsen still further. And that will breed more Islamic fundamentalism (see MIFT). You do not encourage real reform by
  - applauding fake reform. The poor of Uzbekistan should not become more victims of September 11.

17. The integrity of the IMF (although we all doubt it sometimes) should not be sacrificed. Its purpose must be to promote development, not be a tool of regional politics. The diplomatic world of Tashkent is a hothouse, and while the diplomatic corps here may have convinced themselves that there is an understanding that the IMF will not criticise Uzbekistan, ~~it seems to me inherently unlikely that British ministers are party to such a deal.~~ <sup>for non-economic reasons</sup> But I do believe that US Ministers may be. The very good BBC Correspondent here, Katherine Davies, has been told by her sources that this was the primary outcome of O'Neill's visit here in [June.] She asked the question at the O'Neill/Karimov press conference "Will the IMF make a genuine judgement on reform here or will it be content with more sham". Karimov refused to answer the "impertinent" question - in which he was backed by O'Neill.

18. We have no institutional memory of a working visit by a government economist from any department. One would be very welcome.

See MIFT

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there is an explicit understanding ~~and~~ between Uzbekistan and the US on economic support for Karimov in return for the US bases. This encompasses both the IMF approval and \$140 million per year of US aid. To justify the US bases (see MIFT)

~~This to justify this requires a programme of both economic and human rights reforms~~ <sup>the appearance of</sup>

Karimov's visit to Washington followed by

I do not believe we are party to any such understanding.