Soviet Breakup Stymies Foreign Firms
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Companies eager to do business in the former Soviet Union need to remember one rule: One step forward, one step back.

Ask Jack Tymann. His goal of upgrading the air traffic control system took off when the Soviet Union splintered into 15 independent republics. The Soviet general who used to control civil aviation was uncivil to foreigners with designs on Soviet airspace. But now the general has been replaced by a woman—and she'll meet with Mr. Tymann in Moscow next month.

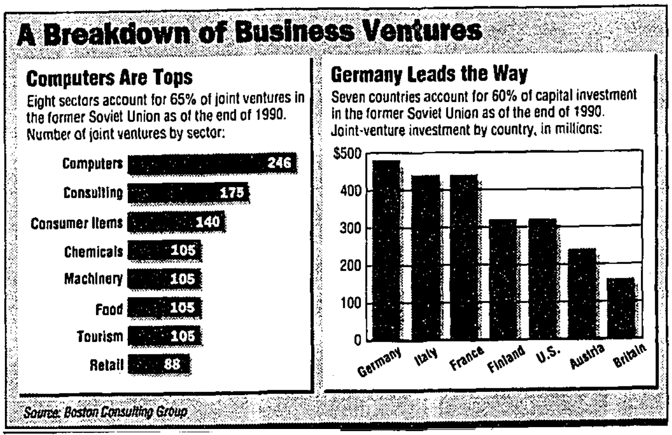
While the military interference is gone, however, money has become a big problem. Before, there was one central foreign-trade bank, Vnesheconombank, that provided all Soviet government guarantees for project financing. Now that bank is nearly bankrupt—and no replacement has emerged so far. Unless someone provides loan guarantees, the project will be dead, frets Mr. Tymann, an executive at Westinghouse Electric Corp. and the point man for a six-company international group.

'Total Chaos'

At the end of 1987, there were only 23 joint ventures between the Soviet Union and foreign interests. By last July, that figure had grown to more than 2,000. And now, as Mr. Tymann and others like him are discovering, the demise of ossified bureaucracies is enabling Western businesses to cut deals directly with local officials and managers. But American and European executives also spend much of their time figuring out just who is in charge, what laws they'll be operating under and how to circumvent a currency in ruins.

"There's total chaos. Nobody knows who's responsible for what," says Czechoslovak businessman Igor Junas, who runs **Kerametal Foreign Trade Co.**, a concern that does extensive metal trading. Kerametal used to have one procurement contract with one central authority. Now, it negotiates directly with representatives of three mines in Georgia, Russia and Ukraine, none of whom has ever before acted as an independent businessman.

The dissolution of the central government has created unprecedented unknowns. Perhaps the biggest is who owns what. One European bank says its purchase of St. Petersburg real estate has been delayed for months—because it can't get clear title to the property.



Source: Boston Consulting Group

Disappearing Partner

While new republic laws affecting privatization, joint stock companies and taxation seem compatible with those of the old union, many macroeconomic issues have been left to chance. Western concerns, for instance, face the prospect of dealing with multiple currencies as the ruble dissolves—and with multiple inflation rates. Moreover, the Commonwealth of Independent States hasn't adopted a central registration system for medicines, as Western drug makers had hoped it would.

Newmont Mining Corp. of Denver finds itself stymied in talks with officials in Uzbekistan who have never negotiated a business contract. "They have no one to tell them this is the way the law works," says James F. Hills, vice president of corporate affairs at Newmont, which wants to mine and refine the region's rich gold deposits and hopes to form a joint venture.

Some companies don't even know whether the agencies they once reported to still exist. **Polaroid Corp.**'s two-year-old joint venture has continued producing camera parts despite the political changes. But its chief partner, the Soviet Ministry of Atomic Energy and Industry, no longer exists. "We're trying to find out what that means, if anything, for our operations," says a Polaroid spokesman.

Meanwhile, Western companies that had been negotiating with the old central government are sometimes viewed suspiciously by the independent republics. Consider **Chevron Corp.**, which a year ago was close to winning a contract to develop the giant Tengiz oil field in Kazakhstan near the Caspian Sea. Since then, Kazakh officials nationalized the field. Although talks continue, "the ride's been a little bumpy," says Daniel Johnson, Chevron's manager of public and governmental affairs.

When the talks began, it was assumed the project's oil exports would generate hard currency. That currency in turn would have allowed the central government to buy goods from a consortium of companies allied with Chevron, including **Johnson & Johnson**, **Eastman Kodak Co.** and **RJR Nabisco Holdings** Inc. But with the Soviet government dead—and the fate of the ruble in question—the consortium disbanded. "Until there are some encouraging signs over there, you're not going to see substantial investment," says James H. Giffen, a founder of the consortium.

Simpler Is Better

One impediment for the consortium was its sheer complexity. Simpler ventures, involving less money and fewer parties, are less likely to get derailed.

"The more ambitious plans are on hold," says Robert Starr, head of the Central and Eastern European practice of Cole, Corette & Abrutyn, a Washington law firm. "People realize we're at a stage where things could get a lot worse before they get better, so most people are scaling down their ambitions."

That's the strategy at **Digital Equipment Corp.**, which opened a Moscow office in December, only days before the Soviet flag flew for the last time above the Kremlin. The company plans additional offices in St. Petersburg and Kiev. But Digital's investment is modest. "Our employees number in the tens, not hundreds," says a spokesman. "We're establishing modest sales offices, not manufacturing plants."

Planning Ahead

Many companies anticipated the Soviet Union's dissolution and had sought contacts in the four most populous republics, Russia, Ukraine, Belarus and Kazakhstan. One such company is **Anglo-Suisse L.P.**, a small oil outfit in Houston. The company's joint venture started drilling last summer in Siberia, and although it isn't yet profitable, exports have started to Italy. Anglo-Suisse says it signed agreements early on with city and regional officials in Siberia, as well as in Moscow.

So far, Anglo Suisse says there hasn't been any interference in its operations.

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Breakup of Soviet Union Creates Confusion for Foreign Companies

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Company officials say they are planning dozens of new wells, requiring the import of expensive Western equipment, in the next three years.

A far graver question than who is in charge is how the new governments will pay for goods and services. The removal of state price controls has sent prices skyrocketing for many goods and has made the ruble almost worthless.

Moreover, within republics, few banks have emerged that can guarantee loans the way the central trade bank used to. That gap is keeping Japanese investors on the sidelines. "A guarantee from the central bank of each republic is necessary [for Japanese companies to make investments], but these institutions aren't functioning yet," says an official at a major Japanese trading company.

The collapse of the ruble may cause **Gillette Co.** to renegotiate terms of a joint venture to make shaving products in St. Petersburg. Initially, Gillette had agreed to receive hard currency at a set exchange rate that is increasingly irrelevant in a hyperinflationary environment.

Some republics are running out of hard currency to pay for such critical goods as food and food-processing equipment. U.S. grain exporters, which shipped about 60 million bushels of wheat to the republics in December, expect to do brisk business this spring. That's largely because one old central agency—Exportkhleb, the Soviet grain importing agency—has been converted into a grain-buying company that's jointly owned by the republics.

Still, cash shortages will affect the farm sector. Western banks agreed to loan the Gorbachev government some $3 billion last year to buy U.S. food after the White House guaranteed repayment. Last week, as scheduled, the republics are said to have made their first loan payment of less than $2 million. But they face another $333 million in payments through spring—and if they default, the White House could balk at more loan guarantees.

The cash crunch is causing companies to create barter arrangements. **Tambrands Inc.**, a personal-care products concern in White Plains, N.Y., used ruble profits from a factory in Ukraine, where it makes Tampax tampons, to buy a cotton bleachery in St. Petersburg from the workers' collective that privatized it. "We'd never have been able to do that deal unless Russia had become independent," says Paul E. Konney, senior vice president of Tambrands.

American Telephone & Telegraph Co., meanwhile, will pay for its 39% stake in Ukraine's telephone authority by providing switching equipment. Under the transaction, announced last week, AT&T will get its hard-currency profits partly from long-distance calls from other countries to Ukraine. The venture marks the first time the company has moved to construct, own and operate a long-distance phone network outside the U.S.

Not all of the change has been for the worse. **Ply Gem Industries Inc.**, for example, a New York maker of home-improvement products, has a joint venture called Russian Wood Express, which can now keep as much as 50% of its export revenue, up from about just 15% under the Soviet regime.

And Kodak finds it can hire talented Russian managers and workers at a modest cost. Among the recent applicants: a Ph.D. physicist employed by a state research institute who earns just $12 a month at current exchange rates. Says Edward Hoppe, Kodak's vice president for Eastern Europe: "There are incredibly talented people who are anxious for jobs."