



J. Henry Schroder Wagg & Co. Limited
120 Cheapside, London EC2V 6DS

Chris Duffy

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To: Nick Brookes - Director
BAT Industries plc

Fax tel: 071 233 1792

From: William Wells

Direct tel: 071 382 6175

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PROJECT UMPIRE

Notes from visit to Tashkent, Tuesday 11th to Friday 14th January, 1994

KEY POINTS.

1. **ATF/PMI:** are offering to make TTF an important satellite to ATF with US\$20-US\$30 million of "investment" in return for leaf.
2. **TTF:** Mahmudov is now more receptive to BAT's PCI as long as it is part of a wider proposal for the re-construction of TTF. He does not object to re-furbished equipment. UPP wish him to visit CME to view re-furbished equipment.
3. **Excise:** the excise authorities appear very receptive to excise proposals. BAT estimate in very general terms that the government could raise a further US\$135 million from the proper implementation of excise + import duties + VAT
4. **GKI re-assurance:** that the radio interview given by Mrs. Mahmudova was not an invitation to tender and that BAT was still the preferred partner.
5. **March proposal:** a full proposal was expected in early March by UPP and the GKI.

ACTION POINTS.

1. **Intelligence on the ground:** in addition to leaf and production visits in January and February, ask B&W to authorise Farhad (?) to keep NBD inform of events in the market place.
2. **Papirossi case:** BAT to provide TTF with case against the continued production of papirossi, including evidence of lack of profitability.
3. **Trading:** BAT to answer TTF requests for IFB imports, if appropriate.
4. **Spare parts list:** assess with a view to ordering.
5. **Raw materials list:** assess with a view to seeing how TTF could be helped.
6. **Brand packing mock-ups:** prepare mock-ups to illustrate new local brand, if appropriate.
7. **Visit to London/CME for UPP/TTF:** to agree terms and conditions of PCI and visit CME as soon as possible (early February?).
8. **Social policy/personnel issues:** given the GKI's emphasis on this, arrange for visit to TTF, SFP and UFP by David Johns.

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9. **Fixed asset valuation:** review possible discussion with UPP/GKI on C&L work in February.
10. **TTF production plan:** consider production plan beyond PCI.
11. **Excise report:** receive excise report by Wednesday 19th January and consider excise proposal for inclusion in March proposal.

A. Briefing from Hopkins/Lioutyl on discussions at TTF on 10th and 11th January, 1994

Present: Rowlands-Rees, Hopkins, Lioutyl (BAT); Wells (Schroders)

1. ATF/PMI proposal. It was understood that the principal components of the ATF/PMI proposal were:

- US\$20-US\$30 million would be available in exchange for fermented leaf supply. It was not stated if this was cash or capital value. It was understood that this might only be the initial offer.
- the manufacturing equipment would be new and not refurbished; refurbished equipment would be used for training;
- TTF would produce up to an aggregate of 10 billion cigarettes per annum comprising low cost local brands and Marlboro SC;
- Mahmudov would have an employment guarantee as general manager for 5 years. It was understood that Mahmudov was impressed by the ATF director's views on management incentives provided by PMI;
- ATF laid considerable emphasis on any investment being one between regional brothers; and
- ATF/PMI arrived with a 'contract' to sign and left details of the proposal and contract with UPP.

2. Progress with TTF. Discussions with TTF had progressed so that Mahmudov now seemed prepared to accept re-conditioned equipment; still arguing that Papirossi cannot be phased out as there was a core market for it (agricultural, elderly).

3. UPP comments: all UPP's enterprises were currently producing 'privatisation' plans to be submitted to UPP within a month or so as part of the process of turning UPP into a form of holding company. Usmanov claimed that he had managed to convince Khamidov to remove the tobacco industry from this programme for the time being. Usmanov advised not to await privatisation as BAT would then be dealing with 'closed' joint stock companies which he thought would be more difficult.

4. Fiscal/excise: the impression was that BAT could have almost any exemption it wanted. David Bishop was reasonably convinced (on the basis of a number of assumptions) that the Uzbek government could increase its excise income by some US\$135 million without too much effort. The tax authorities were being very co-operative and informative.

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B. Meeting with UPP at 1020hrs on Thursday 14th January, 1994

Present: Rowlands-Rees, Hopkins, Liouryl (BAT); Wells (Schroders)

1. **Customs Union:** few details had been released about the Union. However, UPP thought that such was the shortage of cigarettes in Uzbekistan that the government was unlikely to make any defensive moves to protect the tobacco industry.
2. **UPP plan for TTF:** UPP want to re-construct the whole plant in stages (by this they seemed to mean the total replacement of all the equipment, not necessarily work on the buildings). UPP would wish to use equipment from BAT to produce high quality, international standard cigarettes as soon as possible. UPP noted that BAT should treat TTF as their own, proposing the installation of a deputy to Mahmudov and sending Mahmudov on a course for a year or two.
3. **PCI discussion document:** UPP were taken through the discussion document. UPP had no major difficulty in accepting the discussion document so long as the future handling of raw materials was addressed.
4. **ATF/PMI:** BAT took the opportunity to stress that ATF's interest had to be driven by PMI, that TTF would only ever be treated as a satellite manufacturing site and that ATF/PMI could not, given the level of their investment at ATF, contemplate the level of investment being considered by BAT.

C. Meeting at TTF on Thursday 13th January, 1994 at 1600hrs.

Present: Mahmudov, Rybakov, Usmanov (TTF); Usmanov (UPP); Rowlands-Rees, Hopkins, Liouryl (BAT); Wells (Schroders).

1. **General position:** Mahmudov was fairly hostile noting that he had yet to receive either a production proposal or a proposal for the trading of imported cigarettes, the latter he had wanted by 5th January. He felt that the Uzbek tobacco industry's immediate problem was the raising of TTF's production, not developments elsewhere in the industry which were all medium term issues, and that BAT should work with him to address the immediate problem. Moreover, since the "recent radio programme" [the interview by Mrs. Mahmudova?] he had received telephone calls from two of BAT's competitors.
2. **Discussion document:**
 - (a) **Technical components:** TTF were concerned to keep the papirossi operation because of their perception of demand for the product. In addition, as the papirossi machines were over 60 years old it was thought that the equipment would fall apart if moved. Mahmudov wanted to see BAT's economic case against papirossi as soon as possible.
 - (b) **Spare parts:** Mahmudov asserted that he had already provided BAT with a list. He doubted that a budget of US\$1 million would be adequate as his main need was electronic rather than mechanical parts; he suggested that all or some of this money might be better spent buying new machines.
 - (c) **Raw materials:** Mahmudov asserted that he had provided BAT with a list already. His most pressing needs were for acetate filters, wrappers, polypropylene and cellophane - the rest he could obtain for himself.
 - (d) **Impact on capacity:** Mahmudov wanted to know to what levels the equipment set out in

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the discussion document would raise capacity - 10 billion by the end of 1995 but to what by the end of 1994?

(e) *Brands:* Mahmudov was particularly concerned about the lack of proposals for brands in the discussion document. He was less interested in the production of *Uzbekistan SC* and more interested in the development of a new local brand, suggesting that BAT could benefit from the work already done by TTF on this a few years ago (*Amur Tmor; Tashkent*). BAT undertook to consider some further packaging mock-ups.

3. *Usmanov's covering protocol:* Usmanov presented a draft protocol to cover the discussion document in which it was emphasized that the information in the discussion document was an inalienable part of an overall plan for the reconstruction of TTF and that agreement on the supply of the equipment - principally, that Mahmudov would need to come to the UK to inspect the equipment.

4. *BAT's position:* BAT stressed that in the interests of speed the goal was to keep the PCI proposal as simple as possible so that its obligations under the MoU could be fulfilled as quickly as possible. It was agreed that Hopkins should return on Friday morning to: review the equipment list in more detail; collect the spare parts request; collect the raw materials request; and disclose the capacity forecasts. BAT would review the Usmanov protocol.

D. Meeting with Mrs. Gulnora Mahmudova at the GKI on Friday 14th January at 1100hrs.

Present: Mahmudova (GKI); Rowlands-Rees, Yablonskaya (BAT); Wells (Schroders)

1. *Radio interview:* Mahmudova offered us her re-assurance that the interview was not an announcement of any form of tender but merely a speculation about privatisation policy. It had been intended for broadcast solely on local Uzbek radio and had been broadcast from Moscow without her knowledge. The GKI was aware of the commitments under the MoU and the Protocol signed by Mr. Djurambekov. Moreover, she was aware of the amount of work and resources which BAT were devoting to Uzbekistan. In her view, BAT were the favoured partner for investment.

2. *Social policy:* the importance of social policy to the GKI was reviewed - in particular, the maintenance of the volume of jobs if not an increase in the number. Mahmudova noted that in many parts of the country the population was growing rapidly and unemployment was rising, especially in some of the less populated provinces. In addition, the GKI would pay attention to salary increases, pensions, health and safety and other support services for employees.

3. *Samarkand Region:* Mahmudova noted that the GKI office in Samarkand worked closely with the Governor's office and were aware of BAT's interests. She stressed that in her view, the GKI would be in control of any work in relation to Samarkand Region.

4. *Fixed asset valuation:* it was explained that BAT were conducting a valuation of the fixed assets involved in the Uzbek tobacco industry as promised in the MoU. It was explained that BAT had been informed by UPP that a commission from UPP was reviewing the valuation of assets but that the GKI had firm views on valuation which were not limited to fixed assets. It was stressed that BAT's work arose under the MoU and was for discussion purposes only; it was also recognised that there were other ways of valuing the industry but nonetheless it might be deemed appropriate to discuss the fixed asset valuation work undertaken to date.

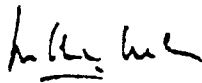
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E. Meeting with Dr. Khamidov at UPP on Friday 14th January at 1400hrs

Present: Khamidov, Usmanov (UPP); Rowlands-Rees (BAT); Wells (Schroders); Tatiana Olkhovskaya.

The meeting was held to secure Khamidov's signature to the Usmanov Protocol. In the course of the brief meeting, Khamidov noted that:

- he saw no future for the production of Papirossi; and
- he felt it was inappropriate for cigarettes to be manufactured at Urgut.



William Wells
17th January, 1994

Distribution:

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