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## EURASIA DAILY MONITOR Volume 1 Issue 103 (October 12, 2004)

### RUSSIAN COMPANIES PROPOSE DEBT-EQUITY SWAPS IN CENTRAL ASIA

By [Gregory Gleason](#)

Recent Russian proposals for debt-equity swaps in Central Asia and the Caucasus represent a bold new strategy for extending Russia's influence in the southern tier. Debt-for-equity swaps involve trading debt for ownership shares in enterprises. For more than a decade Russian financial officials have been reluctantly negotiating such debt-for-equity trades with Western bankers who were anxious to collect Soviet-era debts to the West. Russian officials have now turned the same logic on the creditor states in the former Soviet Union. Under Kremlin guidance, Unified Energy Systems (UES), Russia's large electric power public utility, has aligned with Gazprom, the world's largest natural gas producer and marketer. Gazprom Director Alexei Miller announced last week that, following the recent merger with Rosneft, Gazprom would further diversify into electric power (Kommersant, October 5). The Rosneft merger also left the Russian government with a controlling interest in Gazprom (RBC.ru, October 4).

Debt-for-equity swaps emerged in the 1980s as a palliative to the consequences of heavy sovereign indebtedness in Latin American countries. The practice represents an alternative to default or debt rescheduling. Trading debt for equity typically involves a substantial risk because creditors take an equity position in what are typically loss-producing enterprises. In debt-for-equity swaps, as in all barter transactions, the true terms of exchange are often distorted because it is so difficult to objectively assess the worth of assets traded. In such cases, political considerations often dominate economic concerns. Political considerations have clearly taken the upper hand in Russia's efforts to transform debt into strategic positions along Russia's Asian perimeter from China in the east to Turkey in the west.

Russia has sought to reintegrate the Soviet-era electric grid in order to establish UES as the dominant player in the region's power market. In order to capture market position, UES has negotiated power-supply agreements with Armenia, Azerbaijan, Georgia, and Kazakhstan on terms attractive to

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## PUBLICATION DETAILS

Previously known as the Monitor, the Eurasia Daily Monitor addresses the new strategic realities emerging in Eurasia. Analysts include Vladimir Socor, Rutland and many others based in Eurasia. Focusing on the evolving political and economic landscape, the Eurasia Daily Monitor covers key issues affecting conflict and instability in Eurasia.

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the countries. UES also took over responsibility for running Armenia's Medzamor power plant in 2003. In September 2004 UES concluded a deal to take a 50% equity share in Kazakhstan's large Ekibastuz power plant (Zakon.kz, October 9). In October 2004, Russia negotiated an agreement giving UES responsibility for maintaining Georgia's main power plants (Regnum.ru, October 10).

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Russia's power strategists are now developing an integrated power strategy linking Russia's vast natural gas reserves with Central Asia's largely untapped hydroelectric potential. Hydroelectric power is typically less expensive than coal, oil, or gas, but it is subject to seasonal demands as irrigation users and heat users compete for control of the generating regime. Linking gas and hydroelectric power makes economic and environmental sense, as small gas-fired plants can be situated close to urban populations with little risk or environmental impact. The first step is to gain controlling shares in existing hydroelectric plants in Kyrgyzstan and Tajikistan.

UES chief Anatoly Chubais headed a delegation to Kyrgyzstan this past August to negotiate investment in Kyrgyz hydroelectric stations. Power plants originally planned for exploitation during the Soviet period were abandoned during the early 1990s due to lack of funds. Russia is now returning to these facilities. The completion of Kyrgyzstan's Kambar-Ata stations # 1 and # 2 were the focus of the August discussions. Kambar-Ata # 2 will require \$350 million to complete, while Kambar-Ata # 1 will require much more. The Russians are proposing to trade Kyrgyz debt for a stake in the facilities and offering to bring Kambar-Ata on line by 2007 (Gazeta.kg, August 21).

Tajikistan's domestic electric demand is now met from the large Rogun dam high on the Vakhsh cascade. The construction of dams lower along the Vakhsh was interrupted by the Soviet collapse and the Tajik civil war, which also left Tajikistan heavily indebted to Russia. This summer UES took the step of forming a consortium to finance the completion of the Sangtuda power station. Russia's proposal is to take over a controlling share in the Sangtuda station in exchange for writing off some \$50 million of Tajikistan's debt and bringing \$50 million of new investment to the deal (Avesta.tj, August 26). Kazakhstan has announced an interest in joining the deal (RFE/RL, September 13). The final details of the agreement are awaiting a visit by Russian President Vladimir Putin to Dushanbe, now scheduled for mid-October (Asia-Plus, September 30).

If Gazprom and UES succeed in winning controlling interests in Central Asia's hydroelectric plants, it will open Russia's energy vistas far beyond Central Asia. As demand for electric

power rises in response to the reconstruction of Afghanistan and population growth in western China, Pakistan, and Iran, UES and Gazprom will be positioned to reintegrate the Soviet-era electric grid throughout the Caucasus and Central Asia in a way that enhances Russia's strategic influence throughout the entire region.

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