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## Russian Federation

### Solid Wood Products

### Annual

### 2006

**Approved by:**

Allan Mustard  
American Embassy, Moscow

**Prepared by:**

Erik Hansen and Marina Muran

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**Report Highlights:**

The production of solid wood products is forecast to increase in 2006-07 due to growing international demand. Exports of softwood logs, lumber, and hardwood plywood are increasing, with China, Japan, and Finland as the major destinations. The continued growth of the Russian economy is leading to an expansion in domestic demand for wood and wood products, primarily from the furniture, construction, and paper/pulp sectors. The Russian government has prioritized combating illegal logging. However, little progress has been made due to rampant corruption and the lack of coordination between government agencies. In 2006, a new Forestry Code is expected to be approved by the State Duma.

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## Executive Summary

The production of solid wood products in Russia is forecast to continue expanding in 2006 and 2007, boosted by increased domestic demand and exports of softwood logs, lumber, and hardwood plywood. The main driving force behind higher production is the expectation of increasing exports to China and other Asian markets as well as stable demand from European markets. The continued growth of the Russian economy, albeit at a slower pace, is also boosting demand for wood and wood products from the domestic furniture, paper and pulp, and construction sectors along with the development of new areas of wood utilization. Overall exports of forest products are forecast to increase in most categories in 2006 and 2007. Important changes in forest policy, such as the new Forest Code and a tariff reform, are likely to be approved by the Duma this year. Government initiatives to combat illegal logging will not be effective until the problem of corruption in the sector and transparent coordination between ministers and agencies are resolved.

## Forest Situation/Outlook

Russia is endowed with abundant forest resources, comprising one-fifth of the world's forested area and one quarter of the world's timber stock. Russian forests also provide the largest land-based carbon sink in the world and one of the most biodiverse ecosystems.

Total forested area is estimated at 850 million hectares. Boreal forests are predominant in Russia and most forest resources are located in remote areas, of which 40 percent is considered not accessible. It is conventional wisdom that nearly 70 percent of Russia's total forested area is in Siberia (43 percent) and the Far East (27 percent), whereas 70 percent of the population and more than half of wood demand are in the western part of the country. Russian forests hold all three main categories of trees: coniferous (pine, cedar, spruce, silver fir, and larch), which account for about 70 percent of total area; softwoods (birch, asp, poplar, willow, and alder) - 17 percent of total area; and hardwoods (oak, beech, ash, maple, elm, and locust). The timber stock is estimated at nearly 73 billion m<sup>3</sup>. Coniferous trees account for 58 billion m<sup>3</sup> (80 percent), softwood species for 13 billion m<sup>3</sup> (18 percent), and hardwood species for two billion m<sup>3</sup> (two percent) of the total timber volume. Planted forest is estimated at 20 million hectares. The total volume of logging is estimated at 183 million m<sup>3</sup>, including 129 million m<sup>3</sup> of forests administered by Federal Forestry Agency (FFA). This amount is still well below the total allowable cut estimated at 559 million m<sup>3</sup>.

Russia's role in world trade of forest products does not correspond to the potential of its forest resources base. Russia's market share of the world market for all wood products is still low and consists mostly of unprocessed wood products. The Russian government is trying to pursue long-term policies that improve the sector's efficiency by: 1) increasing the share of processed and higher-value wood and wood products; 2) curbing illegal export and trade of logs; 3) applying tariffs and other government measures to promote the export of processed products versus logs; and 4) attracting of foreign investment; and 5) adopting a long awaited legislative base, Forestry Code and unified national forestry policy.

## Solid Wood Products Situation/Outlook

According to the State Statistics Service (RosStat), Russian economic growth slowed for a second year in 2005 as the pace of growth in oil production eased and manufacturing faltered. GDP growth in 2005 is estimated at 6.4 percent, down from 7.2 in the previous year. Industrial production growth in 2005 reached 4 percent compared to 7.3 percent in

2004, but the construction sector grew at nearly 7 percent. The forest sector's share of Russia's economy is estimated at 2.5 percent of the GDP.

Softwood logs and softwood lumber constitute the largest category of solid wood production and trade in Russia. Production is expected to maintain an average of five to six percent annual increase in 2006-07. The increase in production is supported by strong demand from the export market, mostly China and Finland, and by the rapid expansion of domestic demand, as income and wage growth continue to outstrip GDP expansion, and retail sales remain strong.

Growth in the domestic wood-processing sector is also estimated to increase by more than seven percent annually in 2006-07, boosted mostly by an expected increase of ten percent in the production of panel products (particleboard and medium density fiberboard), and a 13-percent increase in veneer production. This sector is attracting foreign investment and growth is mostly derived from large and vertically integrated enterprises. Higher returns on investments in wood processing facilities, along with a new tariff policy implemented by the government will likely maintain expansion at high levels compared to other categories of the forest sector.

However, according to trade sources, a high number of small and medium-sized logging enterprises went bankrupt in 2005 due to outdated equipment and machinery, lack of harvesting infrastructure to access new forest resources since the bulk of accessible forest resources have been already exhausted, higher transportation tariffs, higher energy prices, and lack of financing mechanisms to allow new investments in equipment and technology.

## Trade

Total exports of forest products (Chapter 44 HTS) in 2006 are forecast at a record of \$5.7 billion (up 26 percent from 2005), while imports of all forest products are forecast at \$335 million (up 11 percent from 2005). The increase in total value of exports of forest products in 2006 can be attributed to the following factors: a) continued increase in exports mostly to China and Finland, and to a lower extent to Japan; b) increase in exports to other markets such as Egypt, Estonia, the United States and the European Union. On the import side, the European Union is the largest supplier of wood products to Russia, followed by Poland, China, Ukraine, Finland and the United States.

## Policy

### Forestry Code

Russia's new Forestry Code is finally under consideration by the Duma and according to the Chairman of the Natural Resources Committee at the State Duma, the forestry code will pass the second reading in March 2006 and will likely be enacted in July-August 2006. The new code seeks a balance between the various aspects of forest management, such as economic, environmental and social aspects. It also provides opportunities for private ownership of forestland in the future, which is likely to attract foreign investment into the sector.

Since 1997, Government Resolutions amended the Forestry Code eleven times. The most recent government resolution signed by President Putin on December 31, 2005, establishes that beginning in 2006 all subjects of the Russian Federation will be responsible for the management and usage of forest resources. However, there is a list of forests, including natural reserves that will remain under the Federal Government supervision. According to

Greenpeace, this resolution will result in the downgrade of the Federal Forestry Agency (FFA) and lead to the collapse of national forests (leskhoz).

The government also took some progressive initiatives in launching the program of forest road construction. Poor transportation infrastructure is considered one of the key reasons for harvesting only 22 percent of the total allowable cut (TAC) annually. According to FFA, 500 million rubles (\$17.7 million) will be allocated for road construction in 2006 and funds will come from the federal budget, federal subject budgets, and bank credits.

### **Certification**

Forest Certification is another challenging issue for the Russian government. It was introduced five years ago. The key advantage of certified wood product is the guaranteed origin of products to meet an increasing ecologically sensitive and price-competitive world market.

Currently, there are three forest certification systems that are competing in Russia:

- 1) Russian System of Voluntary Forest Certification (RSFC). This system was initiated by the Russian Union of Timber Merchants and Exporters and governed by the National Voluntary Forest Certification Council.
- 2) National Forest Certification System. This system was introduced by the Ministry of Natural Resources of the Russian Federation in 2004 and developed under the World Bank Sustainable Pilot Forestry Project. It is competitive with PEFC and FSC, as well as other systems.
- 3) Forest Stewardship Council (FSC) is run by non-government organizations, primarily the World Wildlife Federation (WWF). According to WWF representatives, currently 6.1 million hectares of forests are certified with this system in Russia. According to their forecast, 10 million hectares will be certified by FSC system in 2007.

According to Dmitriy Chuyko, Director for Development of Ilim Pulp Enterprise, certification provides a considerable competitive edge in the market. Currently, there is no substantial price difference for certified and non-certified products in the world wood market, but this situation is changing as profitability improves. The other concern is the cost of certification. The process is very costly, especially for small-sized companies.

### **Tariff**

The Russian Government continues to work on a proposal to apply a selective tariff policy that gives preferential rates to exports of value-added forestry products. In the past several years, the government has approved a number of resolutions lowering export duties for several categories of value-added forestry products.

Beginning January 1, 2006, a single export duty for unprocessed forestry products was established at the rate of 6.5 percent, but not less 4 Euro per cubic meter. The Government Commission on Foreign Trade Protection and Customs Tariff Regulations is working to adjust the remaining export duties for unprocessed wood and finished products. Beginning January 2007, export tariff rates for unprocessed wood, except for coniferous species, will be set at 10 percent of the custom value, but not less than 6 Euro per cubic meter. According to Government Resolution # 789 dated December 21, 2005, export duty for sulphate cellulose (HTS 4703 29 000 0) beginning January 21, 2006 will be zero.

Another breakthrough in the Russian Government Tariff Policy was the temporary lowering import duties to zero for some types of forestry processing equipment designed for MDF processing that Russia does not produce domestically (Government Resolution # 680 dated November 14, 2005).

### **Illegal Logging**

Illegal logging continues to pose a significant threat to sustainable development of the forest sector and poses a challenge for the Russian government. In addition to the obvious negative impact on the Russian economy in terms of tax evasion and lost revenues, illegal logging also affects trade for competing exporters. Illegal businesses do not pay taxes or customs duties, do not conduct mandatory replanting and environmental conservation activities, and do not comply with social obligations and community development.

According to the latest official data announced by the Ministry of Natural Resources, since 1992 annual volume of illegal logging has surpassed of 700,000 m<sup>3</sup>, with estimated financial losses to the forestry sector of five billion rubles (\$176 million) annually. According to the data provided by the Ministry of Natural Resources, it appears that the share of illegal logging is only 0.5 percent of total official logging in Russia, which is 160 million m<sup>3</sup>. However, many environmental organizations consider the volume of timber poaching more likely between 20-50 percent with losses generated by illegal trade of \$1 billion.

Official sources report that from 1992 to 2004, illegal logging incidents have increased. According to the Forestry Agency, the situation with timber poaching is most critical in the Far East due to its proximity to the Chinese borders. According to World Wildlife Fund data, the share of unregistered wood to total volume of timber consumption reaches 53 percent in Chita region, 34 percent in Primorskiy kray, 33 percent in Khabarovsk kray, 17 percent in Vologda region, and 10 percent in Krasnoyarsk kray.

Since 2004, the Federal Forestry Agency introduced a system of space monitoring and aerial photography. The system is expected to improve effectiveness of forest management and enforce violations of the forest legislation. This new technology is also expected to monitor forest fires and other adverse ecological situations.

Currently the monitoring activities are being conducted in Arkhangel'sk and Irkutsk oblasts, Krasnoyarsk kray, Khabarovsk Kray, Primorskiy Kray and Komi Republic covering mostly harvested areas and totaling 49.1 million hectares. According to the FFA, by 2007, space monitoring will cover all 140 million hectares of timber harvesting estimated.

Russia is now a member of Europe and North Asia Forest Law Enforcement and Governance process (ENA FLEG). In November 2005, Russia hosted a Ministerial Conference in St. Petersburg. It was aimed at elaborating the inter-governmental cooperation program between 52 FLEG members whose major concern is the development of legal procedures for eliminating illegal logging and further illegal timber trading for processing. This objective is to be reached through standard market regulation, forest management certification, and the marking of round wood.

Trade sources report that government initiatives to combat illegal logging will not be effective until the problem of corruption in the sector is resolved, and transparent coordination between ministries and services is established.

For more detailed information on illegal logging refer to GAIN RS4043.

## PS&amp;D Tables

Table 1. Production, Supply, and Distribution of Softwood Logs

| PSD Table<br>Country<br>Commodity | Russian Federation<br>Softwood Logs<br>1000 CUBIC METERS |                                  |                                   |                                   |                                   |                                   |
|-----------------------------------|--|----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|
|                                   | 2005<br>USDA Official<br>[Old]                           | Revised<br>Post<br>Estimate[New] | 2006<br>USDA<br>Official<br>[Old] | Estimate<br>Post<br>Estimate[New] | 2007<br>USDA<br>Official<br>[Old] | Forecast<br>Post<br>Estimate[New] |
| Market Year Begin                 |  | 01/2005                          |                                   | 01/2006                           |                                   | 01/2007                           |
| Production                        | 74875  | 77360                            | 77345                             | 81755                             | 0                                 | 86524                             |
| Imports                           | 0  | 0                                | 0                                 | 0                                 | 0                                 | 0                                 |
| TOTAL SUPPLY                      | 74875  | 77360                            | 77345                             | 81755                             | 0                                 | 86524                             |
| Exports                           | 32245  | 35610                            | 33860                             | 39170                             | 0                                 | 43087                             |
| Domestic Consumption              | 42630  | 41750                            | 43485                             | 42585                             | 0                                 | 43437                             |
| TOTAL DISTRIBUTION                | 74875  | 77360                            | 77345                             | 81755                             | 0                                 | 86524                             |

Table 2. Production, Supply, and Distribution of Temperate Hardwood Logs

| PSD Table<br>Country<br>Commodity | Russian Federation<br>Temperate Hardwood Logs<br>1000 CUBIC METERS |                                  |                                   |                                   |                                   |                                   |
|-----------------------------------|--|----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|
|                                   | 2005<br>USDA<br>Official<br>[Old]                                  | Revised<br>Post<br>Estimate[New] | 2006<br>USDA<br>Official<br>[Old] | Estimate<br>Post<br>Estimate[New] | 2007<br>USDA<br>Official<br>[Old] | Forecast<br>Post<br>Estimate[New] |
| Market Year Begin                 |  | 01/2005                          |                                   | 01/2006                           |                                   | 01/2007                           |
| Production                        | 26625  | 29025                            | 27820                             | 31690                             | 0                                 | 34782                             |
| Imports                           | 0  | 0                                | 0                                 | 0                                 | 0                                 | 0                                 |
| TOTAL SUPPLY                      | 26625  | 29025                            | 27820                             | 31690                             | 0                                 | 34782                             |
| Exports                           | 10975  | 13022                            | 15965                             | 15365                             | 0                                 | 18130                             |
| Domestic Consumption              | 15650  | 16003                            | 11855                             | 16325                             | 0                                 | 16652                             |
| TOTAL DISTRIBUTION                | 26625  | 29025                            | 27820                             | 31690                             | 0                                 | 34782                             |

Table 3. Production, Supply, and Distribution of Softwood Lumber

**PSD Table**  
**Country**  
**Commodity**

|                           | <b>Russian Federation</b> |               |          |               |          |               |
|---------------------------|---------------------------|---------------|----------|---------------|----------|---------------|
|                           | <b>Softwood Lumber</b>    |               |          |               |          |               |
|                           | 1000 CUBIC METERS         |               |          |               |          |               |
|                           | 2005                      | Revised       | 2006     | Estimate      | 2007     | Forecast      |
|                           | USDA Official             | Post          | USDA     | Post          | USDA     | Post          |
|                           | [Old]                     | Estimate[New] | Official | Estimate[New] | Official | Estimate[New] |
|                           |                           |               | [Old]    |               | [Old]    |               |
| <b>Market Year Begin</b>  |                           | 01/2005       |          | 01/2006       |          | 01/2007       |
| Production                | 17160                     | 17980         | 18645    | 20795         | 0        | 24128         |
| Imports                   | 0                         | 0             | 0        | 0             | 0        | 0             |
| <b>TOTAL SUPPLY</b>       | 17160                     | 17980         | 18645    | 20795         | 0        | 24128         |
| Exports                   | 13285                     | 14210         | 14615    | 16910         | 0        | 20123         |
| Domestic Consumption      | 3875                      | 3770          | 4030     | 3885          | 0        | 4005          |
| <b>TOTAL DISTRIBUTION</b> | 17160                     | 17980         | 18645    | 20795         | 0        | 24128         |

Table 4. Production, Supply, and Distribution of Temperate Hardwood Lumber

**PSD Table**  
**Country**  
**Commodity**

|                           | <b>Russian Federation</b>        |               |          |               |          |               |
|---------------------------|----------------------------------|---------------|----------|---------------|----------|---------------|
|                           | <b>Temperate Hardwood Lumber</b> |               |          |               |          |               |
|                           | 1000 CUBIC METERS                |               |          |               |          |               |
|                           | 2005                             | Revised       | 2006     | Estimate      | 2007     | Forecast      |
|                           | USDA Official                    | Post          | USDA     | Post          | USDA     | Post          |
|                           | [Old]                            | Estimate[New] | Official | Estimate[New] | Official | Estimate[New] |
|                           |                                  |               | [Old]    |               | [Old]    |               |
| <b>Market Year Begin</b>  |                                  | 01/2005       |          | 01/2006       |          | 01/2007       |
| Production                | 5040                             | 5040          | 5190     | 5170          | 0        | 5275          |
| Imports                   | 0                                | 0             | 0        | 0             | 0        | 0             |
| <b>TOTAL SUPPLY</b>       | 5040                             | 5040          | 5190     | 5170          | 0        | 5275          |
| Exports                   | 360                              | 392           | 380      | 430           | 0        | 440           |
| Domestic Consumption      | 4680                             | 4648          | 4810     | 4740          | 0        | 4835          |
| <b>TOTAL DISTRIBUTION</b> | 5040                             | 5040          | 5190     | 5170          | 0        | 5275          |



Table 5. Production, Supply, and Distribution of Softwood Plywood

| PSD Table<br>Country<br>Commodity | Russian Federation<br>Softwood Plywood |                                  |                                   |                                   |                                   |                                   |
|-----------------------------------|--|----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|
|                                   | 1000 CUBIC METERS                      |                                  |                                   |                                   |                                   |                                   |
|                                   | 2005<br>USDA<br>Official<br>[Old]      | Revised<br>Post<br>Estimate[New] | 2006<br>USDA<br>Official<br>[Old] | Estimate<br>Post<br>Estimate[New] | 2007<br>USDA<br>Official<br>[Old] | Forecast<br>Post<br>Estimate[New] |
| <b>Market Year Begin</b>          |  | 01/2005                          |                                   | 01/2006                           |                                   | 01/2007                           |
| Production                        | 283                                    | 265                              | 291                               | 271                               | 0                                 | 280                               |
| Imports                           | 2                                      | 0                                | 2                                 | 0                                 | 0                                 | 0                                 |
| TOTAL SUPPLY                      | 285                                    | 265                              | 293                               | 271                               | 0                                 | 280                               |
| Exports                           | 190                                    | 175                              | 193                               | 180                               | 0                                 | 187                               |
| Domestic Consumption              | 95                                     | 90                               | 100                               | 91                                | 0                                 | 93                                |
| TOTAL DISTRIBUTION                | 285                                    | 265                              | 293                               | 271                               | 0                                 | 280                               |

Table 6. Production, Supply, and Distribution of Hardwood Plywood

| PSD Table<br>Country<br>Commodity | Russian Federation<br>Hardwood Plywood |                                  |                                   |                                   |                                   |                                   |
|-----------------------------------|--|----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|
|                                   | 1000 CUBIC METERS                      |                                  |                                   |                                   |                                   |                                   |
|                                   | 2005<br>USDA<br>Official<br>[Old]      | Revised<br>Post<br>Estimate[New] | 2006<br>USDA<br>Official<br>[Old] | Estimate<br>Post<br>Estimate[New] | 2007<br>USDA<br>Official<br>[Old] | Forecast<br>Post<br>Estimate[New] |
| <b>Market Year Begin</b>          |  | 01/2005                          |                                   | 01/2006                           |                                   | 01/2007                           |
| Production                        | 1940                                   | 1910                             | 2095                              | 2085                              | 0                                 | 2280                              |
| Imports                           | 0                                      | 0                                | 0                                 | 0                                 | 0                                 | 0                                 |
| TOTAL SUPPLY                      | 1940                                   | 1910                             | 2095                              | 2085                              | 0                                 | 2280                              |
| Exports                           | 1353                                   | 1340                             | 1490                              | 1500                              | 0                                 | 1680                              |
| Domestic Consumption              | 587                                    | 570                              | 605                               | 585                               | 0                                 | 600                               |
| TOTAL DISTRIBUTION                | 1940                                   | 1910                             | 2095                              | 2085                              | 0                                 | 2280                              |