USDA Foreign Agricultural Service

GAIN Report

Global Agriculture Information Network

Template Version 2.09

Voluntary Report - public distribution

Date: 11/2/2005

GAIN Report Number: RS5075

Russian Federation

Solid Wood Products

Forestry Sector Continues to Struggle

2005

Approved by:
Allan Mustard
American Embassy, Moscow

Prepared by:
Erik Hansen and Marina Muran

Report Highlights:
Inefficient utilization of forest resources, lack of down-stream wood processing, and a dysfunctional export structure continue to constrain Russia's forestry sector from fulfilling its growth potential. Currently the forestry sector contributes only three percent to total GDP. Although efforts are being made by the Russian government to develop reliable and transparent regulations and a sound tariff policy, to combat illegal logging and to attract foreign capital to the sector, there is still a long way to go.

Includes PSD Changes: No
Includes Trade Matrix: No
Unscheduled Report
Moscow [RS1]
[RS]

Table of Contents

Executive Summary 3
Forest Production 3
Exports 4
Table 1. Major Russian Wood Exports Destination in 2004, m^3 4
Trade Policy 4
Consumption 5
Table 2. World Harvest and Timber Consumption of Coniferous Wood, Million, m^3 6

Executive Summary

The International Forestry Forum held in St. Petersburg, October 4-7, 2005 brought together an array of federal and local governments as well as industry and business leaders to address the following issues that are considered important for the sustainable development of forestry in Russia: transparent government policy and regulations, changes in tariff policy and export structure for wood products, and mechanisms for fighting timber poaching and illegal trade.

Russia's forest industry remains as fragmented as it was a decade ago. There are over 20,000 operating enterprises, of which half are independent exporters. The majority are small low-capacity enterprises unable to meet obligations of long-term leases, develop infrastructure, process wood, and have no forest management knowledge at all.

In the last few years, the Russian government has passed a number of resolutions lowering export duties of several value-added forestry products. However, export duties are still higher (for some areas are twice as higher) for many downstream wood-processing products than for coniferous and deciduous timber.

World prices for coniferous wood increased by an average of five percent in 2005 due to growing world consumption of coniferous wood, which currently outpaces production. It is forecast that the European Union and North America will likely supply one-third of total world demand, of which China and other South East Asia countries will continue to demand larger volumes.

Forest Production

In his opening remarks, Valeriy Roshchupkin, Head of the Russian Federal Forestry Agency (FFA), stated that the total forest output in Russia reached 180 million cubic meters in 2004, including 160 million cubic meters from forests under the authorization of the FFA. He went on to say that the use of forest leases now make up the majority of land usage. As of July 2005, the total area of forests leased for wood harvesting reached 90 million hectares. In addition, total standing timber volume of forests is estimated at 129 million cubic meters.

Although the allowable forest cut increased to 559 million cubic meters, logging output is estimated to have declined by an average of 1.5 percent with 52 percent of logging enterprises working at a loss. During the first half of 2005, 12 logging enterprises in Russia went bankrupt. Most of them had poor equipment and machinery, no harvesting infrastructure and the bulk of accessible forest resources had been already exhausted. The most profitable logging enterprises are those that operate under vertically integrated entities. This integration enables these loggers to achieve a better financial performance by gaining access to improved and modern machinery and technology.

In 2005, the woodworking sector grew by 7.5 percent compared to the previous year. At the same time, the pulp and paper industry's growth rate dropped considerably. The higher growth rates of woodworking are attributed to new investments and new production capacities.

According to Roshchupkin, the fact that the forestry sector contributes only three percent of Russia's GDP can be explained the inefficient utilization of forest resources, the lack of down-stream wood processing, and a dysfunctional export structure. Trade sources stated that there are several other reasons including:

a) Wide-scale illegal logging, which is estimated between 25 and 50 percent of total log exports from the country. In addition, illegal logging hinders investment and sustainable forest management.
b) Inefficient and outdated processing facilities.
c) Lack of reliable and transparent government regulations and policies. The new Forestry Code has still not been adopted due to disagreements and on-going disputes between policy-makers, producers and representatives of environmental groups.
d) Low levels of foreign investment even after Roshchupkin's optimistic estimate that beginning in 2005 foreign investments in the sector would reach $ 2 billion a year.

Exports

Export earnings from forest products reached $5.4 billion in 2004, while exports for the first half of 2005 have already reached $3 billion. Round wood remains the dominant product among forest exports, but there is also a growing increase in revenues from plywood and sawn wood exports. The bulk of Russia's wood product exports are destined for China, Finland and Japan. In the first half of 2005 exports of Russian softwood logs to China increased by 26 percent compared to the same time period in 2004. China now accounts for nearly half of all softwood logs exported from Russia.

Russia's forest industry remains as fragmented as it was a decade ago. There are over 20,000 operating enterprises, of which half are independent exporters. The majority are small, low-capacity enterprises unable to meet obligations of long-term leases, develop infrastructure, process wood, and which have no forest management knowledge at all.

Table 1. Major Russian Wood Exports Destination in 2004, m^3

HTS	Export (m^3)	Destinations
Coniferous wood, not treated, not stripped HTS 440320	13,251,958	China
	5,678,044	Japan
	5,522,991	Finland
	Total: 24,452,993	
Non coniferous wood, not treated (excluding oak and beech) HTS 440399	6,250,522	Finland
	1,744,010	China
	1,078,679	Sweden
	Total: 9,073,211	
Coniferous lumber HTS 440710	1,199,154	Egypt
	936,880	Japan
	707,188	Great Britain
	Total: 2,843,222	

Source: Customs Statistics of the Russian Federation

Trade Policy

In the last few years, the Russian government has passed a number of resolutions lowering export duties of several value-added forestry products. However, export duties are still higher (for some areas are twice as higher) for many downstream wood-processing products than for coniferous and deciduous timber. The government is working to introduce a program of increasing export tariffs for logs by the end of autumn 2005. According to the Minister of Economic Development and Trade (MEDT) German Gref, export tariff increases for these types of products is crucial for the effective distribution of forestry resources. On the other hand, the Ministry is concerned about increasing these tariffs too quickly because it could hurt the forestry enterprises and thus, increase unemployment.

According to MEDT and the Russian Chamber of Commerce, the current level of export tariffs of forestry products and the existence of other historical problems in Russia's forestry sector are causing round-wood and downstream products to be sold at a price that is considerably lower than the international market price. Although Russia is the world's largest exporter of round wood, it is not on the list of top 20 exporters of high-value forestry products. The problem of "progressive dumping" is also attributed to new requirements imposed by most importers on wood products.

Sources from MEDT, Ministry of Natural Resources, and State Duma, are also opposed to sharp increases of export tariffs for logs. According to the representatives of these organizations, lack of high-tech equipment, inaccessibility of forestry roads and inflexible transport tariffs, and the high cost of "official" timber exports all stimulate unregistered exports. As a consequence, there are serious implications for the raw base of the forestry sector. In addition, export tariffs are inconsistent with World Trade Organization (WTO) requirements, which is important because Russia is currently working towards accession.

The Government Commission on Foreign Trade Protection and Customs Tariff Regulations agreed to a zero tariff on the export of sulphate-bleaching cellulose from coniferous species. The commission is also considering the application of a single export tariff for wood fuel as well as unprocessed forestry products at the rate of 6.5 percent of their custom value, but not less than 4 Euro per cubic meter beginning January 1, 2006. Starting 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.

Consumption

Although trade sources estimate that at least one-third of total Russian production of coniferous wood in 2005 will be exported, there are some new promising areas for timber consumption being developed in Russia. According to Roshchupkin, these two new areas for wood utilization in Russia are: a) construction, modern wood-based materials are increasingly being used in panel and frame wooden house building; and b) energy production, as more consumers demand pelletized fuel in the context of local and municipal energy sector development.

These new areas provide opportunities to accelerate the growth of domestic wood processing as well as additional national housing programs. It offers also an opportunity for public-private partnership, which already has already sparked the interests of large forest industry companies and major banks.

Trade sources also discussed total world consumption of coniferous wood, which currently outpaces production. As a result, prices increased by an average five percent in 2005. The European Union and North America will likely supply one-third of total world demand, of which China and other South East Asia countries will continue to demand larger volumes.

Table 2. World Harvest and Timber Consumption of Coniferous Wood, Million, m^3

Countries	Production			Consumption		
	2003	**2004**	**2005**	**2003**	**2004**	**2005**
World, total	1,004.4	1,013.8	1,016.0	1,008.0	1,014.7	1,017.0
Asia	84.9	85.4	85.0	119.6	118.2	120.0
China	59.7	60.0	60.5	75.7	78.4	80.0
Japan	12.4	12.6	12.5	22.7	26.3	26.0
Europe, total	363.4	366.9	365.0	347.5	354.7	354.0
Great Britain	7.0	7.2	7.2	7.4	7.7	7.7
Germany	30.0	28.1	28.5	29.4	27.5	28.0
Russia	89.1	90.2	93.0	61.3	63.7	67.0
Finland	43.1	45.1	45.0	48.7	50.9	50.5
France	22.7	22.9	23.0	21.7	22.1	22.0
Sweden	57.6	59.3	58.0	61.1	63.2	62.0
North America	433.0	432.7	434.0	427.4	427.7	428.0
Canada	157.5	156.7	157.0	157.3	157.2	157.0
USA	275.5	276.0	277.0	270.1	270.5	271.0

Source: *Rossiyskaya Gazeta*, August 9, 2005. Estimates by the European Economic Commission.