

High export duties for roundwood in Russia?

By Matti Palo

Increasing export duties of roundwood during 2007-2011 in Russia and its consequences have been the most frequently commented business news in Finland during 2007. About 16 million cubic metres or one fifth of the utilization of wood by the Finnish forest industries in Finland has lately originated from Russia. According to a common view the duties will become fully reflected in increasing demand for roundwood in Finland. Consequently, the respective increase in domestic supply should take place.

The timber prices in Finland have already during 2007 increased in real terms more than in 17 years. If the demand for timber in Finland would increase by the amount of the imports from Russia, it would be possible to buy this large amount only at further increased prices. The price increases would not be only restricted on the additional demand but on the total domestic demand, which definitely would make this operation non-profitable.

Therefore, the Finnish companies are considering alternative options to react on this change. The independent sawmills have only a limited number of such options. One option is to change technology to be able to saw also pulpwood-diameter logs. The four large integrated companies, especially the globalized companies, Stora Enso and UPM, have, however, more options available.

Socialistic forestry is practiced in Russia, because all forests are owned by the state. The stumpage prices (prices of standing timber) are administratively set remarkably below the market prices. These prices have recently been 4-5 euros per cubic metre, which is a tiny fraction of the respective prices in Finland. The logging contractors have hence been able to operate profitably, when at the border they have been able to sell the timber at high Finnish prices. In the official statistics, however, lately losses have been reported, which indicates low productivity in logging systems or biased reporting.

Low stumpage prices have also been a main source for huge corruption in forestry in Russia. Transparency International has assessed Corruption Perception Index in Russia as 2.5, while Finland scores 9.6. Russias rank among 163 assessed countries is 121 as counted from the least corrupted end (Finland, Iceland, New Zealand). It is one possibility that the new export duties will not be fully included in export prices but payments for corruption or profits could be somewhat decreased. In this alternative the imports of roundwood to Finland would not be totally stopped.

The rise of duties of birch pulpwood will take place not before 2011. Therefore, a change of policy may appear by the follower of President Vladimir Putin. Stora Enso and UPM are the two largest importers of roundwood from Russia to Finland. Both of them operate globally, which also have invested in fast growing tree plantations in The South. If the import prices from Russia will increase too much, the companies have two major options available.

The companies can close down some low productive mills in Finland and thus decrease the demand for domestic wood. This strategy would increase the global profitability, if the remaining mills would have higher productivity. Furthermore, the companies could avoid buying more high-priced wood in Finland, which also would improve their profitability. Both giants have already tested this strategy in Finland with highly critical public opinion due to increased unemployment. Now the increased export duties in Russia would be a reliable excuse to continue on this line.

Botnia company has this year already imported four giant shiploads of Eucalyptus chips from Uruguai to its pulp mill in Kaskinen western Finland. This outlet will be closed down still

in 2007, when the 1 million ton new pulp mill by the same company will start production. However, roundwood, chips and pulp are supplied at competitive prices in a number of other countries in the South.

The export duty in Russia is ordered by a presidential act. Therefore, it most likely that Mr Putin himself will not cancel it. If it will become fully implemented during 2009-2011, it will total to 50 euros. It is an outcome of strong lobbying by the Russian forest industries, against global efforts to liberalize international trade. If true, the markets will adjust the the future of the Finnish forest industries in various ways.

Mr Jouko Karvinen, the CEO of Stora Enso, declared last July that "The export duties are an issue of life or death for the Finnish forest industries". This view seems to be more lobbying the Finnish government than anything else. The government should not due to this publicity rumba change the tax system of forestry as suggested lately by a forest economist. The present system is clear and operational. As a policy analyst I am doubtful, if even any other instruments to support domestic wood supply will be needed.

Socialistic forestry is the predominant regime in the world, when 84 % of global forests remain owned by states. No socialistic forestry country has proven by facts its way towards Sustainable Forest Management, not even Canada. In corrupted Russia sustainable forestry is even less likely option. A first step had been to raise the stumpage prices instead of export duties. In this way the basic source of corruption within forestry had been eliminated. Neither the Russian forest industries nor the politicians wanted this effective policy instrument.

Increasing the stumpage prices had produced the same additional income to the government as the export duties. Simultaneously, it had improved the profitability of investments by the forest owner (state) in forest management intensification. Under such intensified of silviculture logging could be immediately expanded profitably within the best economic-geographic locations.

The higher stumpage prices would make logging unprofitable in the old-growth natural forests of Siberia and elsewhere in the periphery. The financial accessibility of forests for logging could even be shrunk due to rising stumpage prices. Consequently, under higher stumpage prices and values of Russian forests the markets could even be supportive for more forest conservation.

Higher stumpage prices and consequent lower corruption would also decrease the country risk for major foreign direct investments in pulp and paper in Russia. Under the present situation there exist a few announced investments from Finland in this front but the increased export duty will not decrease the country risk. Major increases in stumpage prices with its benefits are most unlikely under the prevailing socialistic forestry regime.

Ad hoc privatization or decentralization of Russian forests under heavy corruption would lead to the worse. This is the Gordian knot of Russian forestry behind the curtains of the export duties.

Russia has about 40 times the volume of the standing timber in Finland. Russia can annually log only three times more than Finland. In both countries the forests are to a large extent located in similar ecological conditions. Finland is relying primarily on the private ownership and the market system of forestry, Russia on socialistic forestry.

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