

New Forest Code comes into force

The Russian president has a rather direct way of talking. “If we continue chewing snot from one year to another we change nothing,” he said on a meeting with the Government Ministers on the 27th of March, 2006. “We must take all steps to stimulate wood processing in Russia and stop simply sending logs abroad. They hustle here and there in great numbers, and nothing’s been done. I understand why this is happening,” he paused, “and you understand,” he paused again, “these lobbyists... They think of their own interests. But you must think of the people’s interests. Since 1999 various projects are being considered, and not a damn thing’s been done. I know these blathers, and every year we have the same.” It sounds rough. But if you think of peculiarities of the Russian timber business you may feel that this is the right language to use.

How much forest is in Russia?

Russia houses up to a quarter of the world’s total forest and a half of the world’s coniferous wood. Forest land area in Russia is estimated at 774 mln hectares. Potential wood resources are 82 billion cubic metres (including 35 billion cubic metres of coniferous wood) of which 44 billion cubic metres is mature forest ready for exploitation.

Not all forest, of course, can be felled. Allowable felling is determined by forestry authorities each year and is normally in the range 500 – 600 mln cubic metres. These are theoretical figures which have never been reached. Maximum of 380 mln cubic metres were logged in 1988, which is subject to some scepticism due to the widely practiced system in Soviet wood industry when registered figures were higher than the actual felling. These days according to official data Russia is felling around 130-140 mln cubic metres a year. These figures do not take into account several factors. First, these figures

represent the amount of forest as stated in documents authorising felling in a particular area and, therefore, are somewhat speculative. Real figures can be higher. Secondly, they do not include substantial illegal logging which can be as high as 25% of the official felling. Thirdly, these figures do not take into account forests owned by towns and the Ministry of Defence, which to some extent remain outside of the jurisdiction of the state forestry authorities. Total annual felling therefore can be estimated in the range of 170 - 200 mln cubic metres.

Opportunities vs. Challenges.

It appears that the potential of the timber business may well be comparable to the oil or gas industries. Fabulous opportunities, however, may well get drowned under rapidly developing challenges.

Today Russia is exporting mostly logs, timber products with added value comprise a tiny fraction of the exported wood. Logging is a difficult and, perhaps, the least economically effective stage in the production chain. However, as it can be seen from the table export of roundwood is growing very rapidly. Russia has every chance of failing developing own timber industry and become a resource base for neighbouring countries. Russian – Chinese timber trade is a good illustration to the trend.

The border between China and Russia extends nearly 4,000 kilometres, from the south western Primorski Region in the Russian Far East to Chita and Altai Regions in eastern Siberia. In 10 years timber import from Russia to China has increased by nearly 50 times and now reached 17 mln cubic metres a year. It seems that China plans not only to import Russian wood for its own needs but also to modernize its huge sawmill industry in Northeast China and export sawn timber to other countries. China's Heilongjiang Province has seen an increase in new timber processing enterprises, including Nacha Wood, Lancian Wood, Mudanjiang Forest Wood, San Gan Ling and Xin Yang Wood together with others representing more than 600,000 cubic metres of annual processing capacity. According to Bureau for Outreach Campaigns (BROC), Friends of the Siberian Forests (FSF), and Forests Monitor by 2025 China could face a deficit of 200 million cubic metres of wood per year and to satisfy the demand China will continue to look northward to Russia.

Another challenge for the Russian timber business is ineffective work of the state forestry authorities. The state clearly fails to implement the policy that could provide sustainable and environmentally friendly forestry, tackle forest fires and enormous illegal logging. Timber business remains perhaps the least transparent and one of the most criminalised sectors of economy.

Looking at the British landscapes today it is difficult to believe that in the mediaeval times a squirrel could travel from Edinburgh to London from tree to tree without ever touching the ground. It is likewise hard to believe that Russia may face deficit of wood in some near future. However, nearly 70% of the wood is logged in the European part of Russia and the

Urals, at the same time these regions house only 30% of the total resources. In fact most of potentially exploitable forest is far from roads and can not be felled without enormous investments in infrastructure.

New Forest Code.

New Forest Code becomes the law on the 1st of January 2007. It has been debated in parliament for nearly 2 years and was enacted despite vigorous criticism expressed by many non-state organisations and local communities.

According to the Russian constitution forest legislation is in mutual competence of the Federation and the regions. The Forest Code has supreme power over the regional laws and regulations and is in force on the whole territory of Russia. The local regulations must be in compliance with the federal legislation.

Under the new law forest, generally speaking, can not be privately owned. All forests will remain in the state ownership. Forest can be privatised if it is on the land which is categorised as i.e. the land of towns or agricultural land. This is, however, a very small fraction of forest.

A significant feature of the new law is a clear intention to avoid excessive participation of the state in the routine management of forests. The state will continue fulfilling regulatory functions but emphasis will be made on delegation to private companies which hopefully will be more effective than the state. Forest management can be assigned to any private company which wins the business on a tender.

Powers of regional authorities will be limited. They will be controlling the management of forests but relevant regulations will be set up at the federal level.

A contract, most commonly used for commercial exploitation of forest, is the contract of lease of forest. The leaseholder obtains no ownership rights over the land but owns logged timber. The new law eliminated prohibition of sub-lease existed under the old law allowing greater flexibility to the business.

After a contract for usage of forest is concluded no additional formal permission, a logging ticket, is needed. Instead, the forest user has to submit a forest declaration. This change aims to reduce the administration burden on business.

The Forest Code lifts the minimal period for the lease contract. The contract of forest lease can now be concluded for a period between 10 and 49 years.

Another novelty of the law is that the contracts can only be concluded at auctions where those who offer higher lease payments win. Under the old law the contracts were concluded at tenders. Criteria to determine who won a tender were not established by the federal legislation

and were invented locally on ad hoc basis. Business, therefore, saw benevolence of the local authorities as an important asset.

Trends and forecasts.

Today more than 90% of domestic timber companies are small enterprises. At the same time only 10% of the companies make 60% of sales. Russian timber companies owned or controlled by foreign enterprises comprise less than 1% of all Russian timber companies but produce 25% of total amount of timber and paper products. Today there are 9 timber / paper companies with total sales around 2 billion dollars among 200 largest Russian corporations (according to the rating of 'Expert-200'): «Ilim Pulp Enterprise», Syktyvkarskiy LPK, Arkhangelsk CPC, JSC 'Volga', Continentalinvest, Kondopoga, Svetogorsk, Solikamskumprom, Segezhskiy CPC. The new Forest Code is designed to support large companies and it is expected that enlargement of the industry will continue very rapidly.

January, 2007