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PRESS RELEASE

Implications of dramatic reductions to the Russian log export tax rattle many log and lumber exporters and suggest new supply opportunities for importers

Reduced duties or the elimination of the Russian Log Export Tax has many exporters wondering what this means, especially in the roaring China market

December 6, 2010 — Vancouver, BC.

Russia's surprise move to reduce or eliminate log export duties has caught many industry players and traders by surprise and off guard. Most industry observers were more focused on when the log export tax on softwood logs would be increased towards 80% and not reduced from its current 25% level. The news has created nervousness for some companies that might have something to lose and, conversely, some optimism for those that might gain from an increased supply of lower priced Russian logs.

Various news reports have caused a flurry of questions to be raised, as no official details have been released. However, some of the recent press releases have attempted to outline different aspects of the possible agreement, but all seem to have some conflicting details. WOOD MARKETS has been fielding an unprecedented number of inquiries on this topic, given the ongoing wood products consulting work that it conducts in both Russia and China (in addition to our other global coverage). Ironically, Company President Russ Taylor returned from China on the day of the first announcements and Vice-President Gerry Van Leeuwen returned from Russia a few weeks earlier from his second trip in two months.

Until more clarifications are provided (expected as early as **December 7** from one meeting), WOOD MARKETS will start providing some perspectives on an interim basis to assess some of the key questions about "what does all this mean" for log and lumber exporters to China or to those regions in Europe that might benefit from lower cost, higher volume Russian log exports. "Clearly," said Russell Taylor, President, "the Russian log export tax, if reduced or removed, will cause some market dislocations. However, it is the pace and timing of increased Russian log exports that is more the key question right now."

Based solely on new reports and feedback from some of our global contacts, here are the latest developments that have been received by WOOD MARKETS. Following this summary, **WOOD MARKETS has provided its perspectives at the end of this release (Page 3).**

(continue reading below or go to our website to review the full press release [HERE](http://www.woodmarkets.com/pressreleases.html)
<http://www.woodmarkets.com/pressreleases.html>).

Background:

- Russia's initial decision to impose high and prohibitive Russian log export tariffs of up to 80% was tied to the objective of attracting foreign investors in Russia's timber processing industry.
- Russia started increasing roundwood timber export duties in 2007, when the rate grew from Euro 4/m³ (6.5%) to Euro 10/m³ (20%). The tariffs were further raised to Euro 15/m³ (25%) on April 1, 2008. The softwood tax was scheduled to be raised to a minimum of Euro 50/m³ (80%) on January 1, 2009, but this has been postponed each year and was postponed again to January 1, 2012 in November 2010.

- On paper, Russia has been trying to get into the World Trade Organization (WTO) since 1993. In practice, it has stalled and delayed moves toward membership. The reason is that WTO membership could lead Russia to lose more than it gains: Oil and gas, which make up the bulk of Russian exports, aren't covered by WTO rules. Joining the WTO would force Moscow to cut import tariffs on almost all goods, exposing its still-considerable uncompetitive manufacturing base to foreign competition.
- Russia is the only major economy that doesn't belong to the WTO. Joining requires consent from all 153 members of the Geneva-based body.
- The proposed increase from the current 25% export tax to 80% on most species caused a diplomatic row with Finland starting in 2008. This also raised concerns within the European Union's (EU) 27 country bloc, who said the increase would contradict the free trade rules of the WTO, which Russia wants to join. For Russia to be accepted in the WTO, it must eliminate any disputes with other WTO members, such as the CIS state of Georgia and, potentially, China, if the proposed log export tax reductions in the EU are not also applied to China.

November 2010 announcement to reduce Russian log export tax:

- The Finnish Ministry of Foreign Affairs was the first to initially announce in late November that Russia and the European Commission (EC) have reached a deal on Russia's roundwood export duties.
- The new agreement between Russia and the EU, if finalized, would smooth Russia's entry into the WTO but would be subject to Russian softwood log export duties being substantially reduced or eliminated.
- **To be clear, the Russian government has not officially confirmed any decision to lower log export duties.** According to Russian press reports, a formal announcement is expected during the EC-Russia Summit scheduled for **December 7** in Brussels. As the Russian government realizes that entry into the WTO is an important objective, Russia is now working quickly to try to find a compromise solution that meets the needs of those who have already invested in the forest industry and to not impose or impair timber enterprises operating in EU countries.

Prior to acceptance in WTO, Russia may reduce log export duties:

- Various media reports indicated that the current Russian log export tariffs of 25% on softwood logs could be reduced to various rates, ranging from 15%, 12.5% or 2% prior to Russia being accepted in the WTO. The proposed date of implementation for reductions in log export duties also varies, as some reports suggest as early as January 2011, others mid-year 2011, and others suggest no change until entry in WTO - clearly no logic to any of these rates or timetables at this time.
- Hardwood log export duties could be cut even more sharply from the current 40% (Euro 100/m³) on sawlogs – one report suggests to 10% and others suggest even lower.

If accepted into the WTO, Russia log export duties could be further reduced as of the date of ascension into the WTO:

- Some experts, however, believe that after Russia joins the WTO, the country will minimize export tariffs rather than cancel them altogether. The lowest duties would be set for hardwood (birch), while softwood (pine) duties would remain higher.
- However, another report says that it appears that Russia could cancel log export duties altogether if the country is accepted to the WTO before December 31, 2011. Although there is no official information available yet, it would appear that Russia may keep the current tariffs in 2011 and might cancel all roundwood export duties in 2012 if accepted in WTO.
- And another report mentions "phasing out" log export duties, so yet another option.

Further Developments or Wildcards:

- EU officials concede that Russia's admission could be delayed by the long list of WTO rules with which it must comply, including canceling state-aid programs, unfair health rules for farm imports and weak enforcement of intellectual property rights.

WOOD MARKETS' Perspectives on the Implications to Exporters to China:

- The initial concern of the proposed Russian log export tax reductions is related to the China market supply of logs as well as imported softwood lumber. **WOOD MARKETS believes that, based on the initial information received, that there would be little to no impact for most of 2011.** This is tied to the heavy log harvest that occurs mainly in the Russian winter and to weakened logging infrastructure in Russia since the global economic recession.
- The implications for 2012 would be more pronounced, as new investment in Russian harvesting and logistical equipment would be expected, but it would also depend on the timing of when Russia would gain entry into the WTO. **However, given China's soaring demand for imported logs and lumber, the initial impact is still expected to be minor with perhaps some pressure on prices but not necessarily on volume.**
- The pace of Russian investments in timber harvesting will be one of the keys to watch, as this could be a key indicator of how fast Russian log exports could be expanded for shipments into Scandinavia, the Baltic States, China and even Japan and South Korea.

WOOD MARKETS' Initiatives Going Forward:

- WOOD MARKETS is now developing a strategy to formally assess the implications of changes to the Russian log export tax schedule as new or official information is released.
- WOOD MARKETS is considering an update to its previous forecast reports that covered the implications of the Russian log export tax. Previous subscribers that ordered one or more copies of two WOOD MARKETS' strategic reports will be contacted:
 - *The China Book: Wood Products Industry and Market Review – Outlook to 2015* (June 2010)
 - *The Russian Log Export Tax – Global Implications* (January 2009)
- WOOD MARKETS is also looking for any further sources of information on these topics and plans to release periodic updates to interested parties. Please contact us if you see any new information or if you want to be placed on our mailing list for updates.

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