

Problems of Investing into the Forest Industry of Russia in the Conditions of Institutional Uncertainty

Problemas de invertir en la industria forestal de Rusia en condiciones de incertidumbre institucional

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ABSTRACT:

The authors study the problems of investing into the Russian forest complex in the conditions of certain dangers and threats. An example of organization of investment processes in the forest cluster of Finland is studied. The volumes of foreign investments into the Russian economy, Russian investment climate, investment priorities, investment processes in the forest industry, and development of laws in the sphere of investing into the forest complex are viewed. It is concluded that the attention paid to monitoring and analysis of investment processes in the Russian forest industry is insufficient.

Key words: Russia, forest industry, risks, dangers, threats, Finland, volume of investments, investment climate, priorities.

RESUMEN:

Los autores estudian los problemas de invertir en el complejo forestal ruso en las condiciones de peligro y amenazas. Se estudia un ejemplo de organización de procesos de inversión en el grupo forestal de Finlandia. Se analizan los volúmenes de las inversiones extranjeras en la economía rusa, el clima de inversión ruso, las prioridades de inversión, los procesos de inversión en la industria forestal y el desarrollo de leyes en el ámbito de la inversión en el complejo forestal. Se concluye que la atención prestada al monitoreo y análisis de los procesos de inversión en la industria forestal rusa es insuficiente. Palabras clave: Rusia, industria forestal, riesgos, peligros, amenazas, Finlandia, volumen de inversiones, clima de inversión, prioridades.

1. Introduction

At present, the tasks of attraction of investments for development of the Russian industry are very

topical.

Development of the investment mechanism in the conditions of uncertainty of economic subject has its peculiarities. These peculiarities caused by the fact that the result of investing is predetermined by not only the development of companies, which is a general form of management, but also by narrower tasks of provision of sustainability of companies to external and internal influences, threats, and dangers.

This article studies such object of investing as forest industry.

2. The example of Finland

The largest forestry companies of Finland are Stora Enso, Metsaliito, and UPM-Kymmene.

Despite the economic crisis and the negative trend in using the paper carriers of information, the basis of development of the Finnish forestry business is comprised of developments in the sphere of reduction of costs in the process of pulp cooking and paper production, as well as a range of completely new directions (Sinyavsky, 2014).

The volume of investments into the forest industry of Finland constitutes EUR 0.5 - 1.0 billion per year (Forest cluster of Finland, 2012; Decline of investments into the forest industry predicted in Finland, 2017). Approximately 40% of them support innovational projects.

As a result of private-public partnership, the organizations are formed (Forestcluster Ltd and Finnish Wood Research Oy) that finance the research in the sphere of development of forest industry for EUR 50 million annually (partially, from the state budget). Education in the forest sphere also develops (Rubanov, 2011).

Thus, innovational direction of a larger part of investments into the Finnish forest industry Finland is implemented in view of the forecasted dangers.

3. Volumes of foreign investments into the Russian economy

According to different estimates, Russia needs the investments of \$ 15-35 billion per year (Yasin, 1996; Kapkanshchikov, 2010). In 1993, the total sum of direct foreign investments in Russia constituted \$ 2.9 billion. Until the 2007-2008 crisis, the rate of investments had been growing, but began to reduce with the start of the crisis (it reduced by 14.2% in 2008, and by 21% in 2009). The capital outflow grew. As a result, net investments dropped from \$ 35.7 billion in 2008 to \$ 5.2 billion in 2009 (Delyagin, 2010).

According to the Federal State Statistics Service, direct investments into the Russian Federation constituted \$26 billion in 2013 (Federal State Statistics Service 2014). In 2014, the volume of direct foreign investments dropped to \$22 billion and reached \$4.8 billion in 2015 (Reduction of credit rankings of Russia, 2017). In 2016, the volume of direct investments reached \$19 billion (Direct foreign investments in Russia grew by 60% in 2016, 2017).

This shows that the investment flow into Russia is not stable. Back in 1990's the scholars noted that the main reason was such instability was the high level of corruption in the country (Andreev, 1998). In the following years, efforts were made for fighting corruption (Federal law, 2008; Decree of the President of the RF, 2014). However, in 2016 Russia was ranked 131st in the Transparency International ranking for corruption (Russia went down in the ranking for corruption to 131st place, 2017).

4. The investment climate in Russia

Apart from the high level of corruption, the investment rankings are influenced by the problems with the receipt of information on the investing objects, low level of economic development of the country, and low level of development of the banking system.

The agencies Standard & Poor's and Moody's reduced the sovereign rankings of Russia in 2014-2015 to the speculative level. The Russian rankings are expected to drop in the near future, as well

(Volodin et al., 2017).

The strategy of the Finnish companies in the Russian forest industry consists in increase of efficiency of the work of existing plants that are of low power. The increase of the presence in Russia is planned after accumulation of the necessary experience and analysis of possibilities of development.

It is possible to note the following risks factors of investing into the Russian forest industry (Dadalko, 2010; Troskott, 2008):

- growth of losses with growth of the volumes of financing;
 - barriers for entering the market, set by the monopolistic processors of resources;
 - lack of transparency of the investment processes;
 - underdeveloped infrastructure;
 - limitations for the weight of transported cargoes;
 - high cost of transport services and high uncertainty of their receipt;
 - complex registration procedures that accompany the process of investing.
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5. Investment priorities

At present, there are various approaches to determination of the investment priorities:

- investing into fast-payback projects (Volkov, 1998), applied for solving the current economic tasks (Andreev, 1998);
- investing into the projects for manufacture of products protected by domestic and foreign patents and import substituting products (Porter, 2001);
- investing into the objects that form the competitive advantages of the region's economy (Mosin, 1985), which suppose stage-by-stage investing into various spheres of economy;
- investing into the spheres with "growing feedback" (Golosov, 2007), based on expectation of growth in the post-crisis period.

The Federal law dated July 22, 2005 No. 116-FZ "Regarding the special economic zones in the Russian Federation" came into effect on January 1, 2006. Special economic zones of two types were to be created: industrial & production and technical & innovational (Federal law, 2005).

We think that the similar approach can be applied for development of certain spheres of industry.

6. Investing into the forest industry

A peculiar feature of the Russian forestry complex is presence and development of the monopolistic position of resources processors that form vertically integrated systems (Rozanova, 2011) [21].

Effectiveness of forestry companies depends on the consumer companies, and development of processing production stimulates development of the whole forest complex. But this does not mean that the state should help only pulp and paper plants and timber processing industry for accelerating the processes of vertical integration.

Firstly, at present, due to lack of support, most of timber industry companies ceased to exist and were replaced by smaller companies that cannot build timber roads, process waste, or export the products, do not observe the technological norms, labor code, etc.

Secondly, the help to pulp and paper plants and timber processing industry does not mean the automatic improvement of the state of timber procurers due to the monopolistic position of the former.

Thirdly, it is possible that an effective strategy of attraction of new technologies into the final production will not be formed in the near future.

Fourthly, the preferences provided to any investors stimulate the attraction into forest industry of non-profile companies that do not set the goal of its development.

We think that the companies that procure timber should be supported – in any case, before the

sphere is restored. New investment possibilities should be created for processing of timber. It is also necessary to improve the system of control over the use of preferential possibilities.

7. Legislation in the sphere of investing into the forest industry

Development of the forest legislation since 1993 didn't stimulate the progress of the forestry sector in Russia. The new Forest Code of the Russian Federation (2006) and its bylaws are especially negative (Sokolov, 2014).

"The norm according to which the companies that implement the top-priority investment projects in timber processing can rent forest without an auction and for reduced rates is also corruption" (Yashin, 2009).

At present, there's a strategy of development of the forest complex of the Russian Federation until 2020 (Decree of the Ministry of Industry and Trade of the RF and the Ministry of Agriculture, 2008). The Strategy views two scenarios – inertial and innovational.

The Strategy determines the parameters of the investment program – the need for investments for 2008-2020 will constitute RUB 673.3 billion for the variant of inertial development of forest complex, and RUB 2,768.1 billion for the variant of innovational development.

The Strategy should be realized in three stages (2007–2012, 2013–2017, and 2018–2020).

At the stage of consideration of the projects of the Strategy, the Forest Forum of the Russian Greenpeace (The Forest Forum of the Russian Greenpeace, 2008) noted that its direction at development of the forest industry in the North does not correspond to the global tendency for development in the regions where forest could be grown intensely.

The evaluations of the results of the Strategy's first stage noted that development of the forest industry goes along the inertial (negative) scenario (Sukhanov, 2012). The timber procurement activity is not profitable. The total number of profitable companies reduced, and financing of science remained at a very low level.

The specialists of the forest industry noted the following drawbacks of realization of the second stage of the Strategy (Vorontsova, 2016):

- forest restoration works (the necessity for improvement of forest policy, forest fires, illegal timber procurement, insufficient ecological education of the population, low civil activity);
 - lack of capacities for processing of semi-subsistence timber;
 - inauthenticity of information provided to investors;
 - investors' non-observation of their responsibilities for realization of the investment projects;
 - ineffectiveness of credit resources.
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8. Analysis of results

As the experience of realization of the strategy of development of the forest sector shows, it is possible to view three levels of investments (Dadalko, 2010):

- with participation of international profile corporations;
- with attraction of large non-profile Russian companies;
- with participation of regional investors.

The attempts of the leaders of the global forest business to realize large-scale projects in Russia led mostly to failures.

For example, Stora Enso planned to realize several large projects in Russia. However, only the projects on construction of sawmills and carton factories were realized.

As of 2016, the investments of the largest Finnish companies into the Russian forest industry can be characterized in the following way (Table 2)

Company name	Russian legal entity	Year of entering the RF market	Business	Volume of investments, EUR million	Key assets
Stora Enso	Stora Enso Pakajin BB LLC, Stora Enso Forest West LLC, etc.	1998	Production of paper, cardboard, and timber processing products	154	Companies for production of wrapping in Arzamas, Balabanovo, and Lukhovitsy, sawmills in Nebolchi and Impilakhti
UPM	UPM Kummene Chudovo LLC, UPM Kummene LLC	2003	Production and sales of plywood; selling paper and self-adhesive label-stock. Purchase of raw timber	200	Plywood factory in Novgorod Oblast, terminals for cutting and distribution of self-adhesive label-stock in St. Petersburg and Noginsk

Source: Compiled by the authors on the basis of the materials: Trade mission of the Russian Federation in Finland. Overview of the state of economy and main directions of foreign economic activity in Finland in 2016. URL: http://91.206.121.217/TpApi/Upload/6614696f-f244-4a7f-ac83-a1f639783939/obzor_economy_finland_2016.pdf (Accessed: 26.06.2017)

The Russian non-profile companies (e.g., metallurgical) strive only for maximum use of subsidies, but not long-term participation in development of the forest sphere.

The third level was filled by creation of small capacities for processing of plywood raw materials (200,000 m³ of yearly processing of veneer log).

The main direction of transformations in the forest sphere – redistribution of the forest fund in favor of large investors. However, realization of this direction faces certain problems. It is possible to note the following:

investors are not interested in investments, only in receipt of preferences;

most investors' documents haven't reached the government, being stuck at the regional level;

the entrepreneurs whose projects are established by the government cannot receive the preferences envisaged by the law;

the level of subsidies for investors is not sufficient.

We think that the problems that emerge in the course of implementation of the strategies of attraction of investments are not sufficiently studied. At the same time, analysis of non-correspondence of the volume and structure of investments to the ones that were expected during realization of measures for their attraction, as well as the reasons for this non-correspondence, might improve the investment climate in the country. It is necessary to form the system of attraction of investments that would react to the challenges of the modern times.

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