

KARELIA UNIVERSITY OF APPLIED SCIENCES  
Degree Programme in International Business

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ENTRY PLAN FOR FINNISH PRESSURE TREATED TIMBER TO  
RUSSIA- CASE COMPANY: PRIMATIMBER

Thesis  
May 2018



**THESIS**  
**May 2018**  
**Degree Programme in International Business**  
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Commissioned by PRIMATIMBER OY

Abstract

The main goals of the thesis are: to explore the opportunities in Russia for pressure treated timber produced by PrimaTimber in Finland, to assess Russia's suitability for entry, and to design an entry strategy. Moscow and Saint Petersburg are the first cities planned for entry. The research is based on the collection and analysis of primary data obtained from interviews with industry experts, and secondary data gathered from various sources.

The business environment of the timber market in Russia is analyzed. The specifics of Moscow and Saint Petersburg and issues related to customs are also analyzed. Market trends are investigated. Competition in the impregnated timber market is viewed in terms of domestic production, imported impregnated timber, and the role that substitutes play.

The research led to the conclusion that the competition is quite tough and substitutes pose a substantial threat. The future competitive situation seems to only get worse for PrimaTimber on Russian market. Poor economic situation in Russia is slowly improving, but unfavorably weak Russian ruble and fluctuations in its value are challenging.

The designed entry strategy covers the selection of an entry mode, marketing mix, terms of contract and other issues arising when doing business internationally. A summary in the end summarizes the key points of the thesis.

Language  
English

Pages 38  
Appendices 0  
Pages of Appendices 0

Keywords

Russia, market research, entry strategy, timber

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# 1 INTRODUCTION

## 1.1 Background

Timber is a popular construction material, especially for building outdoors. Unfortunately, it is susceptible to rotting and diseases when it gets into contact with water and the ground. The diseases greatly reduce timber's lifespan. Various wood preservation methods have been developed, including pressure treatment, which allows increasing timber's lifespan by 30-60 years, depending on usage conditions. (Sudoma Sawmill 2018a.)

Fir and pine are widely available and relatively cheap wood species that are most often pressure treated. The process itself is not expensive when carried out industrially. All of these factors make the resulting product affordable to most users. (Sudoma Sawmill 2018a.) Around the world the method is fairly known and popular nowadays, but the Russian market is only beginning to realize the benefits of pressure treated timber (Sales manager of Voodoodrev 2018).

## 1.2 Company and product description

PrimaTimber is the case company of this study. PrimaTimber is a producer of pressure treated timber. It was established in 2003 in Joensuu, Finland and it is a part of the Iivari Mononen Group (PrimaTimber 2018).

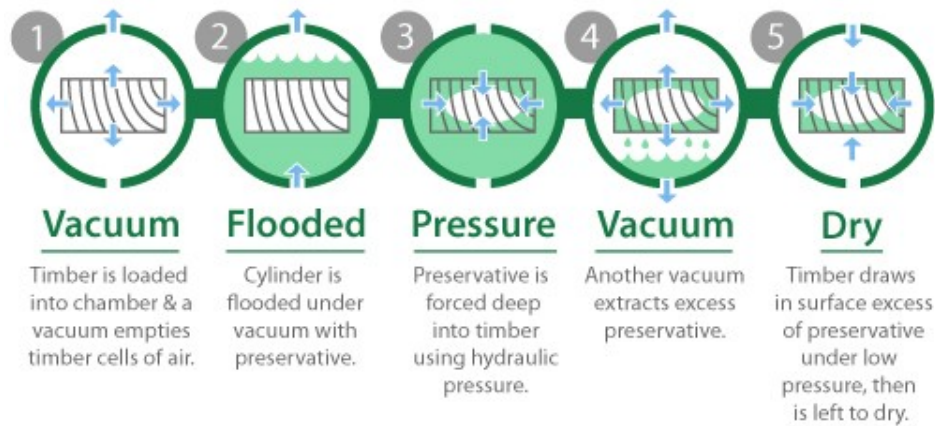
Iivari Mononen Group's history started in the middle of the twentieth century as a timber pole business. Nowadays, the group consists of three companies – Scanpole, Exsane and PrimaTimber. Scanpole produces poles that have various applications, ranging from telecommunications to electricity poles. It is one of the leading players in Europe. Exsane provides various services for

infrastructure networks for telecommunications, electricity and street lightning. (Iivari Mononen Group 2018.)

PrimaTimber uses Nordic pines to produce pressure treated timber of different types, such as sawn, planed and round timber. Pressure treated timber is also known as impregnated timber. That timber is well-protected against insects or fungus, high humidity, water and rotting, and can withstand harsh weather conditions, ensuring long lifespan and safety required for building outdoors. Impregnated timber has various applications, such as docks, fences, decks and other structures found in courtyards and gardens. PrimaTimber's impregnated timber can be brown, green or gray. (PrimaTimber 2018.)

PrimaTimber uses a copper based wood preservative, which is the most commonly utilized preservative in the impregnated timber market all over the world (Nousiainen 2018). The Tanalith E wood preservative (which is produced in England) is most commonly used for the impregnation of timber. It is safe for human and animals, and it does not smell. Further painting or other protection of impregnated timber is not needed. After impregnation, timber's mechanical qualities remain the same. (Sudoma Sawmill 2018a.)

The process of pressure treatment can be seen in Picture 1. Depending on the class of treatment, the preservative can penetrate timber from millimeters to centimeters deep (Sudoma Sawmill 2018a). PrimaTimber's products are impregnated either in class A or class AB, depending on purposes of the timber. Class A impregnated products are suitable for applications with direct ground or water contact (e.g. fence posts), while class AB products are used above ground (e.g. decking). (Nousiainen 2018.)



Picture 1. Timber pressure treatment process (Source: Shedstore 2018).

In Finland, PrimaTimber sells its products B2B to wholesalers, retailers, construction companies, and directly to house builders. Retailers normally are various hardware stores (also known as DIY stores) from where consumers and businesses can purchase the timber. About 95% of PrimaTimber's products are sold in Finland, and the rest is exported to Spain and China. (Nousiainen 2018.)

### 1.3 Goals

As PrimaTimber is successful on the local market, it is turning its views to other countries to expand its business. Neighboring Russia has always attracted the company's attention, but so far no business has been conducted there. Currently, the company considers Russia as one of its options for further growth.

The main goal of this thesis is to explore opportunities in Russia for pressure treated timber produced by PrimaTimber in Finland, to assess Russia's suitability for entry, and to design an entry strategy. The focus of the paper is on Russia's biggest cities – Moscow and Saint Petersburg.

## **1.4 Methodology**

This practice-based thesis utilizes research and the analysis of primary data from interviews with industry experts as well as secondary data from various sources. Some information covers Russia as a whole, and some focuses specifically on the markets in Moscow or Saint Petersburg.

Three interviews were conducted with experts from Russia, one by personal meeting and the remaining two over the phone. The personal meeting took place with a sales manager of a hardware store in Karelia (the LCK hardware store chain). The phone interviewees were the sales managers of companies producing impregnated timber, Pinopreg in Moscow and Voodoodrev in Saint Petersburg. In addition, the Business Director (COO) of PrimaTimber, Joni Nousiainen, was also interviewed. The information regarding customs issues was received from Inga Kairo, a consultant on the customs issues of the Finnish-Russian Chamber of Commerce.

Secondary data was gathered from official statistics, industrial research agencies, as well as news agencies and impregnated timber producers' websites.

In this thesis paper, all ruble numbers were converted to the euro based on the official exchange rate of the Bank of Russia (2018a) valid as of 14 April 2018, when one euro was set at 75.7507 Russian rubles.

## **1.5 Outline of the thesis**

The thesis contains four major parts. The first part analyses the business environment of the timber market in Russia. The market trends are then analyzed along with the competitive situation on the market. Based on the research done, an entry strategy is designed.

The business environment is analyzed in terms of political, legal and economic environments. The specifics of Moscow and Saint Petersburg and issues related to customs are also presented.

The market trends covered are those found on the market of impregnated timber, also on DIY market, and trends in substitutes. Other market trends relevant to the case are also considered.

Competition in the impregnated timber market is viewed in terms of domestic production, imported impregnated timber, and the role that substitutes play. Based on that, competition in the market is analyzed using Porter's Five Forces framework. Then competitive position of PrimaTimber's products on the Russian market is analyzed.

The entry strategy covers the selection of entry mode, marketing mix, terms of contract and other issues arising when doing business internationally.

## **2 BUSINESS ENVIRONMENT OF THE TIMBER MARKET IN RUSSIA**

This chapter deals with the political and legal issues of the pressure treated timber market in Russia, as well as economic developments in the country. A brief economic overview of Moscow and Saint Petersburg is presented. In the end, issues related to customs regulations of impregnated timber are covered.

### **2.1 Political and legal environment**

In 2012 the Russian Federation became a member of WTO, which framed the trade relations of Russia and the European Union according to WTO rules, aimed at easing international trade, and having lower import duties as one of



the outcomes. However, there are still some disputes due to violations of the agreements. (European Commission 2018.)

In the World Bank's Doing Business rating, Russia has shown great improvement, having climbed from 120<sup>th</sup> place in 2012 to 35<sup>th</sup> in 2017 (TASS 2017). Out of all indicators of the rating, the most relevant improvement is found on the indicator of Trading across Borders, in which Russia has climbed to 100<sup>th</sup> position in 2017 from 140<sup>th</sup> in 2016 (Ministry of Economic Development of the Russian Federation 2018).

In 2014, after economic sanctions from the US, EU and other countries, Russia intensified its efforts on import substitution. That was organized by introducing programs and projects with governmental support to local businesses in many ways, such as funding and subsidies and such. (PIA Новости 2015a.) Import substitution efforts are taken not only to substitute import products with locally produced ones, but also to increase the export potential of Russian products, with competitiveness based on both price and quality (МИА «Россия сегодня» 2017).

The EU sanctions on exports to Russia include many types of products but not pressure treated timber (European Union 2018). The Russian response to the sanctions in form of food embargoes on certain product categories is also irrelevant to the case (РОСБИЗНЕСКОНСАЛТИНГ 2014). It is projected that Western sanctions will stay and tensions will remain at least during the forecasted period, from now all the way to 2022 (Economist Intelligence Unit 2018).

## **2.2 Economic environment**

The recent economic decline in Russia is related to low oil prices and Western sanctions. The drop of oil prices in 2014 majorly impacted the Russian economy, as it is highly dependent on oil. The situation, together with the general decline of commodity prices, made the Russian government implement measures to shift from a natural-resource-based economy to an innovation-

driven model. (PricewaterhouseCoopers 2017.) The economic situation is still quite poor, and last year household consumption began to recover while still staying at the level of year 2012 (Bank of Finland 2018a).

In 2017, Russia experienced GDP growth of 1.5 percent, which was preceded by two years of recession (The World Bank Group 2018). It is forecasted that the Russian economy growth rate will stay weak, at a rate between 1-2 percent GDP over next two years (Deloitte CIS Research Centre 2017). DT Global Business Consulting GmbH estimates a growth rate of around 2 percent in its longer term five-year GDP forecast, providing oil would stay at about 57-64 USD, no structural reforms would be implemented, and Western sanctions remain (DT Global Business Consulting GmbH 2018).

In March 2018 the inflation rate was 2.4 percent (Bank of Russia 2018b). Overall, inflation has declined over the last few years (BBC 2017). Inflation is expected to be as low as 4 percent all the way through 2020, which is the lowest in last 10 years (Deloitte CIS Research Centre 2017).

The Russian ruble has faced vast fluctuations against the euro over the past few years, when the value of the euro roughly doubled in comparison to the same period during the preceding year 2014 (Figure 1). The spikes in the exchange rate tend to fall back, but still the overall trend is the weakening of ruble (European Central Bank 2018). The lower external value of the ruble makes products imported from Finland more expensive and hence less competitive on the Russian market. The fluctuations and weakening of the ruble also pose a risk, which in turn may force companies operating in Russia to consider various measures, such as localizing production or even leaving the Russian market.

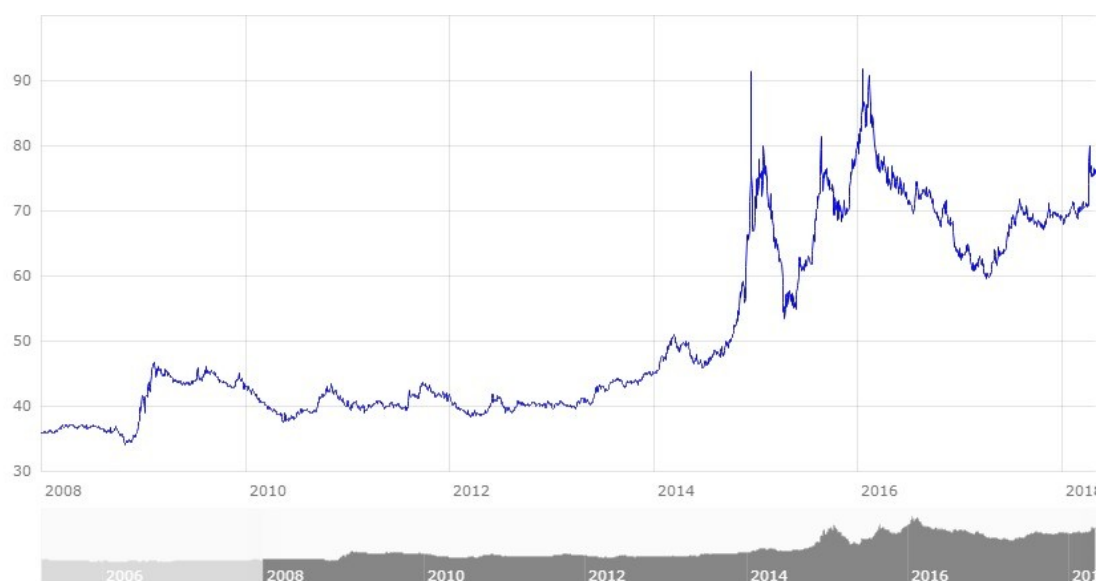


Figure 1. Ruble to euro exchange rate from 1 January 2008 to 1 May 2018 (Source: European Central Bank 2018).

The recent loss of the external ruble value is attributed to new sanctions by the United States that happened on 6 April 2018 when some Russian businessmen, public officials and Russian companies were placed on the sanctions list (Bank of Finland 2018b). There is a consensus that the weak ruble will stay (Deloitte CIS Research Centre 2017). Table 1 shows the forecasted exchange rate by two respected institutions –Economist Intelligence Unit and IEF RAS.

Table 1. Ruble to euro exchange rate forecasts (average per year) (Source: Deloitte CIS Research Centre 2017).

Source	2018	2019	2020
IEF RAS	RUB 68.4	RUB 68.6	RUB 70.7
Economist Intelligence Unit	RUB 73.1	RUB 70.9	RUB 74.3

It is a positive sign that Finnish-Russian trade grew in 2017. Still, exports from Finland were lower than imports and grew at slower pace. The total value of exports from Finland to Russia was 3.4 billion euros, which is a growth of 15 percent in comparison to 2016, and the total value of imports from Russia was 8.2 billion euros (growth of 33 percent). Most of the imported products to Finland were energy products with a share of the total imports of 61.7 percent. (Tulli 2018.)

### **2.3 Moscow and Saint Petersburg**

The population of Moscow as of 1 January 2018 was about 12.5 million people, which is somewhat close to being one-tenth of all of Russia's population. In Saint Petersburg the number was 5.4 million people. (Federal State Statistics Service 2018a.)

Moscow's Gross regional product (GRP) in 2016 was 14.3 trillion rubles (189 billion euros), which is much more compared to 3.7 trillion rubles (49 billion euros) that Saint Petersburg had. The GRP has been growing for the past ten years in both cities. Moscow contributed 15.5 percent to Russian GDP in 2016 (Federal State Statistics Service 2018b). In 2015 GRP per capita in Moscow was about twice that of Saint Petersburg, and more than twice the average number for Russia (Moscow investment portal 2018a).

Moscow's inhabitants have high personal incomes, with per capita income in 2016 around 59,100 rubles/month (780 euros). That was almost double the national average of about 30,700 rubles (405 euros). (Moscow investment portal 2018b.)

### **2.4 Customs issues**

Phytosanitary certification is needed for each shipment of products, it should be obtained from relevant authorities in Finland. It is most likely that there are no export fees or permits required in Finland, but it is better to check by contacting the Finnish customs directly (website: <http://tulli.fi>). For PrimaTimber's products, the customs duty is 10 percent and the VAT is 18 percent, which should be collected when goods are imported. There is no excise duty or other duties. Further information on certification can be obtained from the following companies: SGS Finland Oy (<http://www.sgs.fi>), РосГост (<http://rosgost.com>), Серконс (<http://www.serconsrus.ru>). (Kairo 2018.)

Exporting goods from Finland to Russia requires a customs code (commodity code) for each product. The code covers categories, so some products could

have the same code. It should be noted that Finnish and Russian commodity codes differ to some extent. (Kairo 2018.)

Russia is a part of Eurasian Economic Union (EAEU), whose other members are Armenia, Belarus, Kazakhstan, Kyrgyzstan. A single tariff level is applied in customs union which comprises all EAEU member countries, and goods can move between the countries freely. (Федеральная служба по ветеринарному и фитосанитарному надзору (Россельхознадзор) 2018.) For products in the customs union the EAC (Eurasian Conformity) mark is necessary. It is much easier for a Russian party to take care of importing to Russia than it is for a Finnish party. It is best to make who is responsible for obtaining all needed certificates clear in the contract. (Kairo 2018.)

### **3 MARKET TRENDS**

This chapter covers trends on the market of impregnated timber, as well as developments in other areas that are relevant to the case. Trends are presented from the DIY market, from the market of substitutes of impregnated timber, and from other markets.

#### **3.1 Trends in market of impregnated timber**

Nowadays, Russian customers are becoming more and more familiar with impregnated timber as it is quite a new product on the Russian market. The product is not widely known, and usually some explanations and promotion to potential clients are needed to prove the benefits of the product. The production of and demand for impregnated timber in Russia is growing currently, as is the export of impregnated timber. The quality of impregnated wood that is made in Russia is comparable to foreign analogues, due to the usage of imported equipment. The prices of local products are lower. (Sales manager of Voodoodrev 2018; Sales manager of Pinopreg 2018.)

Approximately ten years ago Russian companies launched the production of impregnated timber. Finnish impregnated deck board was introduced back then when there was no Russian alternative. Nowadays, the demand is satisfied with local production. (Sales manager of Voodoodrev 2018.) Overall, deep wood processing is increasing in Russia nowadays. The weak ruble has allowed exporters to rip huge revenues, even though the exporting has mainly consisted of raw materials. The Russian government's stimulation plays a big role, as it provides subsidies for capital investment credits for deep wood processing plants, and removed import fees for deep wood processing equipment and export fees for deep processed wood products. The competition on the Russian market is increasing. (Григорьев 2017.)

### **3.2 DIY market trends**

As seen from Figure 2, the Russian market for DIY products has been shrinking for two years since 2015, but in year 2017 a little growth of 1.8 percent was achieved. The growth was due to the sales of finishing products (Soft DIY), while construction materials (Hard DIY) continued to sink. (INFOLine 2018a.) However, DIY and household retail stores are not primary channels for their biggest suppliers. In 2017 only 14 percent of them received more than half of the turnover from retail stores, and most (70 percent) of the suppliers had no more than 30 percent of turnover from the stores. Most suppliers (over 80 percent) do not plan to sell more through DIY and household retail stores. (INFOLine 2018b.) The DIY market has entered a consolidation phase, and the 10 biggest retailers showed increases in market share last year, from 33 percent to 37 percent (INFOLine 2018c).

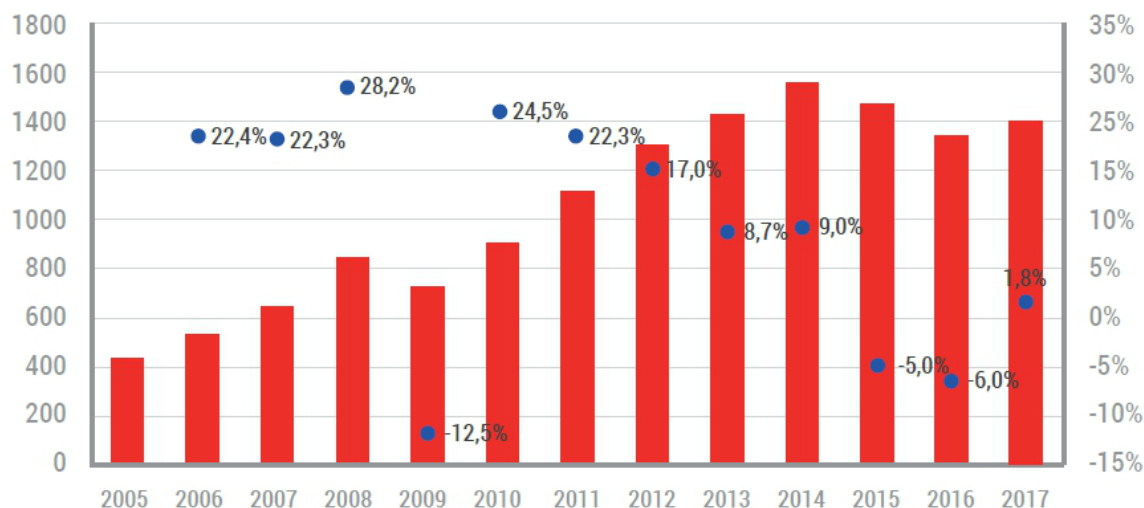


Figure 2. DIY market of Russia, billion rubles (red for turnover, blue for growth rate percentage) (Source: INFOLine 2018a).

For the most part, the market of Moscow and Saint Petersburg could be pretty similar to that of Petrozavodsk, which is the biggest town and capital of the Republic of Karelia. The biggest retail hardware store in Karelia is ЦСК (CSK), a local chain of DIY shops operating since 1999 in Petrozavodsk (ЦСК 2018).

Currently in ЦСК, Russian timber makes up about 95 percent of the timber sales. The company is not seeking to substitute locally produced timber for imported timber and is ready to purchase timber from abroad when it is economically reasonable. Since 2014 the company saw an increase in sales of timber until 2017 when sales started to decline. Lately there has been a drop in demand mainly caused by a 10 to 15 percent price increase in timber products in 2018. The reasons for this are less material available and the tightening of government regulations. (Dubrivniy 2018.)

ЦСК started selling impregnated timber only in 2018, sourcing it from a local producer. Nowadays, the sales volume is growing, and the growth is expected to continue. It is just the beginning of the product life cycle on Petrozavodsk's market, and most customers are not aware of it and its benefits. At the same time, ЦСК will not anymore sell timber which is antiseptically treated by dip treating, as it has weak protection and the price difference is relatively minor to impregnated timber, especially considering the superior qualities of latter one.

(Dubrivniy 2018.) Some consumers also show a bad attitude or mistrust towards impregnated timber. They still confuse it with dip treated timber, often after a bad experience with dip treated timber or a fake product – dip treated instead of impregnated timber (Dubrivniy 2018; Sales manager of Voodoodrev 2018).

### **3.3 Trends in substitutes**

On the Russian market, there are several types of wooden products, either domestic or imported, that can be utilized instead of pressure treated timber in many applications. These are thermally modified wood and wood-plastic composites. In addition, there are products made with types of wood resistant to rotting such as larch, abachi, alder, aspen and others. Larch is of Russian origin and it is the main substitute to impregnated timber. More expensive types of wood are primarily used for saunas, at about 90 percent of those wood types' sales volumes in ЦСК. (Dubrivniy 2018.)

Impregnated timber is by far the most versatile product on the market, for various applications. Some applications of wood-plastic composite (WPC) are similar to impregnated timber, and in ЦСК the sales volume of WPC made in Russia has been growing since 2014. WPC is most often used by businesses, where it is a popular material for building decks and terraces for restaurants and cafes. The sales increased recently because of new color options - from two to five colors. Compared to impregnated timber, the color options of the WPC play a major influence on choice in affluent buyers and businesses, while the green color is often not considered appealing. The company expects further increase in demand for WPC. (Dubrivniy 2018.)

A low end substitute is antiseptically treated timber by dip treating, which is processed industrially. This type of timber nowadays has fallen out of favor for most users. (Dubrivniy 2018.)

Just using dried timber or unseasoned timber (undried timber) is also practiced, with its short outdoor lifespan. It also poses safety hazard because of quickly



diminishing mechanical properties. In some structures such as fence posts, metal or reinforced concrete are also often used.

Timber also could be manually treated with antiseptics but that protection is less reliable than dip treating. Some users turn to painting wood with paints or varnishes, giving some degree of superficial protection. Painting is needed to be renewed rather often, sometimes even annually, which increases costs of maintenance.

### **3.4 Other market trends relevant to the case**

In 2017 logging in Russia dropped for the first time in the last five years, although the drop was minor, only 0.65 percent. Totally the 212.4 million m<sup>3</sup> of wood was logged. Government-supported priority investment projects have been the main source of growth, although they still do not cover for the decline in other areas of logging. (WhatWood 2018.)

There is a lot of wood in Russia, most of which used to be cut and exported as a commodity. Currently, the situation is changing. Due to the higher exchange rate and the import substitution efforts of the Russian government, domestic producers are growing production of deep processed timber products at a higher added value. (Григорьев 2017.) Still, the needed equipment is mostly purchased abroad (Sales manager of Voodoodrev 2018).

One example of a large government-supported project is the Sudoma sawmill, located in Pskov Oblast, which borders with Leningrad Oblast. It is a deep wood processing plant specializing in wooden finish materials. The factory is a part of the Dedovichi production facility complex, which operates full cycle, from growing trees and logging to manufacturing, aiming at waste-free production. Apart from sawn wood, it produces impregnated timber and thermally modified timber (Sudoma Sawmill 2018b). During the construction of the factory its price increased about one and a half times, with final cost being estimated at 1,842 billion rubles (24 million euros), and the cause is mainly attributed to the growth

in prices of equipment due to changes in the Russian ruble exchange rate (Костринский 2015).

One factor that affects the sales of impregnated wood for building outdoors is the decreasing demand for private houses and *dachas* (in Russian this means summer houses outside of city). This trend is observed especially in Moscow Oblast (area around Moscow), and the stagnation seem to continue. (PIA Новости 2018b.) Besides, the costs of ownership of those have recently increased due to new taxes and requirements of building registration (Информационное агентство "Znak" 2018).

## **4 COMPETITION IN IMPREGNATED TIMBER MARKET**

This chapter deals with the competitive situation on Russian market of impregnated timber. It covers domestic production and imported impregnated timber, as well the role of substitutes. Porter's Five Forces framework was utilized to understand the situation in the impregnated timber industry. Finally, the overall analysis of the competitive situation on the Russian market is presented.

### **4.1 Domestic production**

In Russia there are many producers of impregnated timber, and new players may come as it is becoming more popular product. Often plants are located in towns which are rich in raw materials and have good logistics.

Producers reach customers in many ways, by selling directly to end users or through hardware stores or dealers, and some have own shops or storages in the cities. Various types of wood preservatives are used for impregnation, of

both Russian and foreign origin. Some popular brands are TanalithE and Celcure C4 among others. (Sales manager of Voodoodrev 2018.)

Table 2 displays information compiled on the retail prices of impregnated timber producing companies in Moscow and Saint Petersburg or in the nearby area. To simplify the comparison, size and price are provided for profiled deck boards made with Russian pine, and green as the default (and cheapest) color. Unfortunately the sizes vary, and only the thickness and width are put into the table. The length is omitted. Prices are in rubles per square meter, including VAT, and euro prices are calculated with the reference exchange rate (one euro at 75.7507 rubles). In cases where there was no price per square meter but only price per piece instead, simple calculations were made to find the price out. Most producers do not mention the timber impregnation class, but most probably for deck board it is class AB or the equivalent. Factory prices are presented, meaning that buying from a hardware store is more expensive, but prices do not include the cost of delivery. Most local producers sell directly to customers as the main distribution channel.

Table 2. Retail prices of impregnated timber by local companies in Moscow and Saint Petersburg.

Company name	Size (cm)	Price (per m <sup>2</sup> ) RUB	Price (per m <sup>2</sup> ) EUR	Sales area	Location of production	Source
<b>Moscow</b>						
Мечтаево (Mechtaevo)	32x140	900	11.9	Moscow and Moscow Oblast	Moscow or nearby	Мечтаево 2018
VoodooDrev	32x140	900	11.9	Moscow and Moscow Oblast	30 km	VoodooDrev 2018
Стандарт Вуд (Standartwood)	28x120	900	11.9	Moscow and Moscow Oblast	80 km	Стандарт Вуд 2018а
ЭкоТехВуд (EcoTechWood)	30x96	900	11.9	Moscow and Moscow Oblast	80 km	ЭкоТехВуд 2018
<b>Saint Petersburg</b>						
"Торговый дом "ПДЗ" (Torgoviy dom "PDZ" ) (Pinopreg brand)	35x145	823	10.9	All Russia	100 km	Торговый дом "ПДЗ" 2018
РэдВуд (RedWood)	34x95	795	10.5	Saint Petersburg	20 km	РэдВуд 2018
Арелан (Arelan)	30x150	856	11.3	Moscow, Saint Petersburg, Yoshkar-Ola; sells in six hardware store chains	150 km	Арелан 2018

#### 4.1.1 Production in Moscow and Moscow Oblast

In the Moscow Oblast (also known as Podmoskovye), which surrounds Moscow, there four following producers are found.

Мечтаево (<https://www.mechtaevo.ru>) is a construction company specializing in private houses. It produces impregnated timber for use in construction of its

houses, and also sells it separately. It also uses a special landing page on the internet for selling impregnated timber (<http://www.imdrev.ru>). In addition, it offers timber impregnation service.

VoodooDrev (<http://voodoodrev.ru>) is an impregnated timber producer.

Стандарт Вуд (<http://standartwood.ru>) – is an impregnated timber producer.

ЭкоТехВуд (<http://ecotechwood.ru>) – is an impregnated timber producer which also uses it to make garden furniture, garden houses, fences and piers. It also offers timber impregnation service.

#### **4.1.2 Production in Saint Petersburg and Leningrad Oblast**

In the Leningrad Oblast surrounding Saint Petersburg there are three producers of impregnated timber.

"Торговый дом "ПДЗ" (<http://www.pdz.spb.ru>) – is a producer of Pinopreg brand timber (<http://pinopreg.ru>). The company sells throughout Russia and also exports its products. It impregnates timber in green and brown colors, with brown being slightly more expensive. It offers timber impregnation service. It does not sell through stores or intermediaries. All customers can find the company through the internet (Sales manager of Pinopreg 2018).

«Арелан» (<http://arelan.ru>) – is an impregnated timber producer. It owns a hardware store "Пилометр"(Pilometr) which also has an online shop (<https://pilometr.ru>). The company owns a sawmill and sells untreated sawn timber products as well. It is also an exporter.

"РэдВуд" (<https://redwood.tiu.ru>) – is an impregnated timber producer.

## 4.2 Imported impregnated timber

Some importing of impregnated timber from Finland is also taking place. Table 3 shows the price comparisons for profiled deck boards. Sales volumes are probably low. Unfortunately, a direct price comparison cannot be made because of the different sizes and types of profiling that Russian and Finnish companies use. Imported Finnish impregnated timber is much more expensive compared to Russian impregnated timber.

Table 3. Retail prices of Finnish imported impregnated timber

Company name	Size (mm)	Price (per m <sup>2</sup> ) RUB	Price (per m <sup>2</sup> ) EUR	Sales area	Source
Тимбер Про (Timber Pro)	32x100	1360	18.0	Saint Petersburg	Тимбер Про 2018
ФинСтрой (Finstroy)	28x95	2337	30.9	Moscow and Saint Petersburg	ФинСтрой 2018
Стим (Stim)	28x95	1590	21.0	Saint Petersburg	Стим 2018

Тимбер Про (<http://timberspb.ru>) is a distributor of impregnated timber produced by the Finnish company Tammiston Puu and its various constructions, such as prefabricated garden houses. It also offers assembly services.

The ФинСтрой company group is a distributor of imported timber products – impregnated timber, thermally modified timber and other timber products, as well as Russian timber products. ФинСтрой has offices and warehouses in both Moscow and Saint Petersburg (<http://fin-sm.ru>).

The construction company Стим distributes impregnated timber produced by the Finnish companies KUUSISTO GROUP and UPM (<http://thermo-wood.ru>).

### 4.3 Role of substitutes

There are several substitutes for impregnated timber. Table 4 presents the prices of profiled deck boards made with impregnated timber substitutes, except for dried timber and unseasoned timber, which are just planed boards. All the products in the table are of Russian origin, and are available in both Moscow and Saint Petersburg. Again, size and price are provided, and the most similar sizes of products are presented.

Table 4. Retail prices of substitutes to impregnated timber.

Company name	Size (mm)	Price (per m <sup>2</sup> ) RUB	Price (per m <sup>2</sup> ) EUR	Source
<b>Thermally modified wood</b>				
Лестермо (Lestermo)	23x130	1450	19.1	Лестермо 2018
TWOOD	20x130	1360	18.0	TWOOD 2018
ТЕРМОВУД (Theromwood)	23x136	1350	17.8	ТЕРМОВУД 2018
Magic Wood	130x20	1100	14.5	Magic Wood 2018
ТермоЛес (Thermoles)	25x115	1850	24.4	ТермоЛес 2018
Фореста Дизайн (Foresta Design)	20x92	2200	29.0	Foresta 2018
<b>Wood-plastic composite</b>				
Леруа Мерлен (Leroy Merlin)	162x26	1715	22.6	Леруа Мерлен 2018a
Петрович (Petrovich)	150x25	2542	33.6	Петрович 2018a
SAVEWOOD	163x25	1398	18.5	SAVEWOOD 2018
ЭКОДЭК	140x22	1794	23.7	ЭКОДЭК 2018
<b>Larch</b>				
Леруа Мерлен (Leroy Merlin)	27x142	981	13.0	Леруа Мерлен 2018b
Петрович (Petrovich)	27x143	1429	18.9	Петрович 2018b
Атланта	34x140	1000	13.2	Атланта 2018
<b>Dried timber</b>				
Петрович (Petrovich)	20x120	481	6.3	Петрович 2018c
<b>Unseasoned timber</b>				
Петрович (Petrovich)	25x125	329	4.3	Петрович 2018d

The prices vary considerably. Wood-plastic composite is the most expensive substitute type, while thermally modified wood is a little cheaper, and larch is the cheapest. All of them are more expensive than Russian impregnated timber (Table 2). On the opposite side of price and rot resistance, unseasoned timber (pine) is cheaper than dried timber, but they both are unprotected and structures made with them naturally have shorter lifespans.

#### **4.4 Competitive situation on Russian market**

Competition in the market is analyzed with Porter's Five Forces framework, which is a powerful and recognized tool for analyzing an industry's profitability and overall attractiveness for entry. The forces that reduce profitability in the industry are rivalry among existing competitors, power of suppliers, power of customers, the threat of substitutes and the threat of new entrants. A company should try to defend itself against the forces or try to use them in its favor. To do that, learning about an industry's environment is necessary, along with delving deeply into reasons for all the features. Finally, a company can design an appropriate strategy. (Porter 1979.)

##### **4.4.1 Threat of new entrants**

Many Russian companies are willing to enter the market. There are low barriers to entry and favorable government policies. The required investments are not too big, although the economies of scale are not so favorable, because the main piece of equipment for the impregnation process is an autoclave, which is one separate unit (Picture 2). Buying a second unit would double capacity but require doubling timber and sales volume to achieve maximum profitability. Equipment is usually of foreign origin, and the ruble is weak nowadays. Prices of autoclaves vary, and for example Chinese autoclaves made by Henan Taiguo Boiler Manufacture Co., Ltd. cost from 8 to 50 thousand USD, depending on options and the sizes of the autoclave (Alibaba.com 2018).





Picture 2. An autoclave at timber impregnation plant (Source: Стандарт Вуд 2018b).

New entrants cannot differentiate their products considerably, but it is attractive that profitability is higher than in selling untreated wood. Timber market players will need to reduce their share of other timber business to utilize their timber for impregnation, or increase the supplies of raw material. Good logistics is vital. Taking all features into account, the threat of new entrants is on a medium level.

#### **4.4.2 Threat of substitutes**

Thermally modified wood and wood-plastic composites are rising on the Russian market, and classic solutions which are rot resistant wood species have always been substitutes. Those options are more expensive though. It is easy for consumers to switch products. The color of substitutes may play a role, especially for decking. Some customers might have preferences for more natural products, or they may be afraid of chemicals in pressure treated timber. So, overall the threat of substitutes is high.

#### **4.4.3 Bargaining power of customers**

Products are not much differentiated. Buyer switching costs are low, because timber is considered rather as a commodity, and there are many suppliers. Substitutes are materials that are similar in their mechanical properties so it is easy to switch to them. Substitutes are becoming more numerous. It is easy to

find out all the options and information. Buyers are numerous and less concentrated, which makes them less powerful. Backward integration is unlikely but it also may happen. The bargaining power of customers is therefore on a medium level.

#### **4.4.4 Bargaining power of suppliers**

Suppliers can always easily sell their timber as a commodity or even export it. It is also easy for companies to switch suppliers, although logistics plays a role. It is relatively easy for a supplier to vertically integrate and start producing impregnated timber. This all creates high bargaining power for suppliers.

#### **4.4.5 Industry rivalry**

There is competition on the market. The products are quite similar, and it is hard to differentiate or innovate. The more expensive alternative woods are less affordable to Russian customer in a period of hard economic situation. At their expense, impregnated timber sales are set to grow, winning the market of cheap construction material. The impregnated timber market is growing nowadays. Both Russian and imported products are presented on the market. The result is a high degree of rivalry in the industry.

### **4.5 Analysis of case company's competitive position**

Given the variety of options for deck board available in Russia, it can be concluded that PrimaTimber's impregnated timber is not a product that is unique and hard to replace on the Russian market. The competitive situation on the Russian market is rather tough.

For comparison, PrimaTimber's profiled deck board of brown color of size 28x120 mm sold in Finnish hardware store K-Rauta at a price of 1.99 euro per meter (K-Rauta 2018). That price is 1,256 rubles (16.6 euro) per square meter. The price is more expensive than Russian impregnated timber (Table 2) but cheaper than imported Finnish impregnated timber (Table 3). The domestic

product costs less than 12 euros in Russia, while PrimaTimber's product costs almost fifty percent more without the additional costs related to import that it would incur if sold in Russia. Apparently the final price of imported Finnish timber includes customs duty, Russian VAT and delivery costs. For that product type, Russian VAT is 18 percent (Kairo 2018), but Finnish VAT is 24 percent (Tax Administration 2018). Coping with competition could prove hard, and finding a niche could be the best option.

When PrimaTimber's price is compared to substitutes of impregnated timber, thermally modified wood and wood-plastic composite are more expensive, but larch is a cheaper substitute (Table 4). There is a variety of applications of impregnated timber, and in some areas substitutes might be preferable because of color or other features. Since PrimaTimber's products are more expensive than Russian impregnated timber, expensive substitutes pose a higher threat to PrimaTimber than they do to Russian impregnated timber.

Not all impregnated timber is similar. There are differences in impregnation class, wood preservative used, species of the wood impregnated, the wood quality itself, profiling and color. Apparently affluent customers would prefer to pay more to get a more natural brown color, as opposed to the cheaper normal green color of impregnated timber. Profiling makes the price higher but it is a normal feature of deck board used outdoors. If it is true that the quality is the same for Finnish and for Russian impregnated timber, then the resulting construction made with the timber would look same and have a long lifespan. It is likely that no one would know that a deck is made with Finnish timber unless they are told so. This is in comparison to other products such as car and smartphones, where the producers are easily recognizable. So there is no real reason to pay more if a customer does not really get more for buying Finnish impregnated timber.

The final Russian consumer price for PrimaTimber's timber depends on delivery cost, VAT, customs fees, the profit margin of hardware store or any intermediary. Joensuu, where PrimaTimber's timber impregnation plant is located, is distant from Russian customers. The distance from Joensuu to Saint Petersburg is about 400 kilometers, and from Joensuu to Moscow it is about

1100 kilometers. Joensuu itself is located around 100 kilometers from the border with Russia, and around 200 km from the border crossing point leading to Saint Petersburg. The transport company that PrimaTimber is using in Finland does transport to Russia, so another company is needed to take care of transportation (Nousiainen 2018).

As discussed in Chapter 2, the ruble will stay weak at least in short term. That gives a price advantage to Russian companies. If the ruble continues to stay weak, and competition keeps growing, PrimaTimber's impregnated timber is not going to be competitive pricewise with Russian impregnated timber and substitutes.

## **5 ENTRY STRATEGY**

This chapter proposes an entry strategy into the Russian market. Areas are covered such as selecting entry option, customer segmentation, marketing mix, terms of contract and others.

### **5.1 Entry option selection**

When venturing into a new country, there are some options to choose from. Considering the higher price of PrimaTimber's products and the current economic downturn in Russia, along with all the other risks, the best option to minimize risks would be indirect export. Direct export is the second best option, but the risks are much higher. A local Russian distributor is an easy option but it also increases the price as the distributor takes their own margin. Other demanding options are more risky, especially with the company's lack of prior experience of doing business in Russia. Therefore, the distributor or hardware store is the option that is used in this entry strategy.

## **5.2 Segmentation, targeting, differentiating and positioning**

With a quality product that is not competitive in price, it is better to target a less price-sensitive segment, such as rich Russians and companies. Finnish origin, trust and its long company history differentiates PrimaTimber in a good way, as Russians value Finnish products (Fontanka.fi 2016). The product is to be positioned same way as Finnish products are positioned normally on Russian markets, as being trustworthy, reliable and safe, durable, and of high quality.

There are many more segments, such as selling directly to consumers and businesses as well as orders from governments and NGOs and others that can become end users for impregnated timber. A lot of people purchase timber and similar products for their private houses and *dachas*.

## **5.3 Marketing mix**

A marketing mix is a set of marketing tools that should allow producing a desirable outcome on the market. The marketing mix includes four tools (four Ps) – product, price, place and promotion. (Kotler & Armstrong 2014.)

### **5.3.1 Product**

The best product to export would be luxurious, expensive and with a higher added value, namely a profiled deck board. PrimaTimber's deck board comes in several profile types and many dimensions. Brown and gray are the best colors, while green is less valuable for consumers. A deck board is visible and it is a product that affects user experience the most. There are other types of boards that are used outside constructions, such as plain boards, planks, battens and fence posts. These are much simpler products, and there is no reason for Russian customers to purchase them from abroad at a higher price if local substitutes are readily available. At same time, there are a lot of substitutes in the deck board market, and it is very competitive.

Other types of impregnated timber used as frame materials are often hidden from sight. These are sawn planks, barks, glulam timber (glued laminated timber). Since they are not a part of the user experience, they are also easily substituted with local alternatives. Only a question of quality and trust in a producer could be an issue there.

PrimaTimber's profiled deck board is used as a product for export in this entry strategy.

### **5.3.2 Price**

PrimaTimber's higher price is justified with such benefits as Finnish quality and confidence in the product, brand value and color options. It is reasonable to set a price higher than market average. The price level of Russian thermally modified wood and composite deck board would be reasonable.

The weak ruble and fluctuations of its external value compared to the euro pose a great threat. To illustrate the impact of ruble exchange rate fluctuations, Table 5 presents calculations made for changes in price of PrimaTimber's deck board if sold at a retail price of 17 euros per square meter. A one-hundred percent exchange rate is the one used in this thesis as a reference (one euro at 75.7507 rubles). Nine-hundred rubles is used as a price per square meter of Russian deck board being compared.

The first column of Table 5 shows the possible scenarios of changes in the exchange rate. The last column shows how much more expensive or cheaper PrimaTimber's ruble price (if sold at 17 euro) becomes compared to generic Russian deck boards at a price of 900 rubles, following an increase or decrease in the exchange rate. So, if the initial price is already 1.4 times higher, it is going to be twice that already if the exchange rate grows by 40 percent. When it doubles, PrimaTimber's deck board price almost triples compared to Russian deck board. That is a high risk, which is unfavorable for distributors. On the other hand, PrimaTimber's price becomes equal to Russian price in case of a 30 percent decrease in the exchange rate.

Table 5. Exchange rate influence on PrimaTimber's deck board at a price of 17 euros to a Russian deck board at a price of 900 rubles.

Exchange rate %	Exchange rate	Ruble price	Price comparison (times)
100 % (reference)	76	1288	1.4
5% increase	80	1352	1.5
10% increase	83	1417	1.6
30% increase	98	1674	1.9
40% increase	106	1803	2.0
50% increase	114	1932	2.1
100% increase	152	2576	2.9
5% decrease	72	1223	1.4
10% decrease	68	1159	1.3
30% decrease	53	901	1.0
50% decrease	38	644	0.7

PrimaTimber can employ various strategies in response to changes in the exchange rate. If the company expects that after a decline in the external value of the ruble it is going to eventually get stronger, it may want to keep its end user prices unchanged to keep its market share by selling at lower price to the distributor. That strategy would however not work considering the long term ruble prospect. In case the ruble strengthens, PrimaTimber could reduce the price to increase the market share. Whether that is a viable strategy or not is a question of price elasticity of demand.

### 5.3.3 Distribution channels

Same companies that are importers of impregnated timber (ФинСтрой and Стим) could be potential distributors for PrimaTimber. At the same time, this would create competition among the products that a distributor sells. The financial situation of the potential partner companies should be found out in advance.

Selling in hardware stores might be harder because of their stricter supplier policies and the possible orientation of localizing business to allow for cheaper products. It is good that hardware stores also often operate as wholesale suppliers.

Since distributors or hardware stores takes the titles (ownership) of goods, it is supposed to have warehouses to keep stock. From there they can deliver impregnated timber to clients. PrimaTimber's main concern in that case is delivery to a given warehouse. The company may try to find a transport company, or the Russian party could organize it, especially if it is already engaged or has had experience with importing goods from Finland. Shipping by truck or train are the only viable options. It is easier if a Russian party takes care of the transportation and legal issues on the Russian side.

To find a proper partner and get other types of support, it is a good idea to become a member of Finnish-Russian Chamber of Commerce. The organization offers various benefits to its members, and a basic package of 400 euro would be reasonable (Finnish-Russian Chamber of Commerce 2018).

#### **5.3.4 Promotion & communication channels**

Online presence is crucial nowadays, and it is reasonable to implement a Russian version of the company's website. Penetration on the internet is high in Russia, and in 2017 74.1 percent of the Russians actively used the internet, while the share of internet users was 76 percent of population (Federal State Statistics Service 2018c). Search engine optimization also is a must.

Online advertising can be utilized. This should be focused on high-income individuals. It is possible to order advertising or articles in some magazines, for example ЛесПромИнформ magazine (<http://lesprominform.ru>). As PrimaTimber already has a profile on Facebook, it is reasonable to make a Russian language profile on Facebook, and also a profile on the biggest Russian social network V Kontakte (<https://vk.com>). Promotional activities which are in Russian language are to be handled by the distributor. Outsourcing could be utilized as the distributor may use the services of a local digital marketing agency.

There are tradeshows in Russia where it is possible to participate in order to increase the awareness of the product and the company. The list of upcoming events is available on the website of ЛесПромИнформ magazine –



<http://lesprominform.ru/exhibits> (ЛесПромИнформ 2018). The most suitable event is «Загородный дом» / Holzhaus, which is organized by the international company group ITE (ITE 2018a). The event is organized biannually in Moscow and it focuses on private house construction technologies and materials (website: <http://www.zagoroddom.com>) (ITE 2018b). PrimaTimber's sales agent or the COO could attend in person and present products, together with a distribution representative.

#### **5.4 Terms of contract**

Formal contract should be used between PrimaTimber and a Russian party. It is best to provide distributor rights of exclusive representative in the area of Moscow and/or Saint Petersburg, but for a limited time, for example two years. For delivery terms, using Incoterms 2010 terms, FCA Joensuu or EXW Joensuu are relevant options for the company. For payment, using Open Account with a credit period of 30 days is the simplest but also a dangerous option. It is best to start negotiations from Advance payment as the safest option. The Russian party should take care of customs clearance and obtaining certificates.

#### **5.5 Other considerations**

Any Russian partner is unlikely to speak Finnish and even English, so a language barrier poses an obstacle and even a risk. During negotiations and for translating documents, hiring Russian-speaking staff or using translator service are possible options. Cultural differences can affect how business goes. A visa is needed for Finnish citizens travelling to Russia.

## 6 SUMMARY

Despite the current harsh economic situation in Russia, it still could be seen as a promising market. First of all, it is a question of if the company really wants to enter the Russian market, given all the difficulties involved and the unfavorably weak ruble. In the long run, the competitive situation seems likely to only get worse for PrimaTimber on Russian market.

The legal environment has been framed by WTO regulations, and the Russian government is currently working on easing international operations. At the same time, international tensions seemingly are staying, and the risks of economic sanctions are quite unpredictable. They could affect the exchange rate even further, potentially making PrimaTimber's already costly product even more expensive and less competitive in Russia.

The competition on the Russian market of impregnated timber is tough and growing, and substitutes are available. The price of PrimaTimber's product puts it into the high price segment. A strong point of the company that it is a Finnish company. Affluent customers make up the target market for PrimaTimber in Russia.

Deck board is best product to export to Russia, as it is a luxury product itself and is most visible and noticeable during use, which is important for conspicuous consumption. It can allow also the highest profit margin.

A partner in Russia is necessary, such as a distributor or hardware store. Stock should be kept at a partner's warehouse in Russia. Changes in the exchange rate are to be monitored, and strategies to compensate those may to be utilized. Promotion both online and offline should be done in Russian language. Language barrier is an issue.

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