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## SPECIALIZATION PRIORITIES OF KHABAROVSKY KRAI ECONOMY

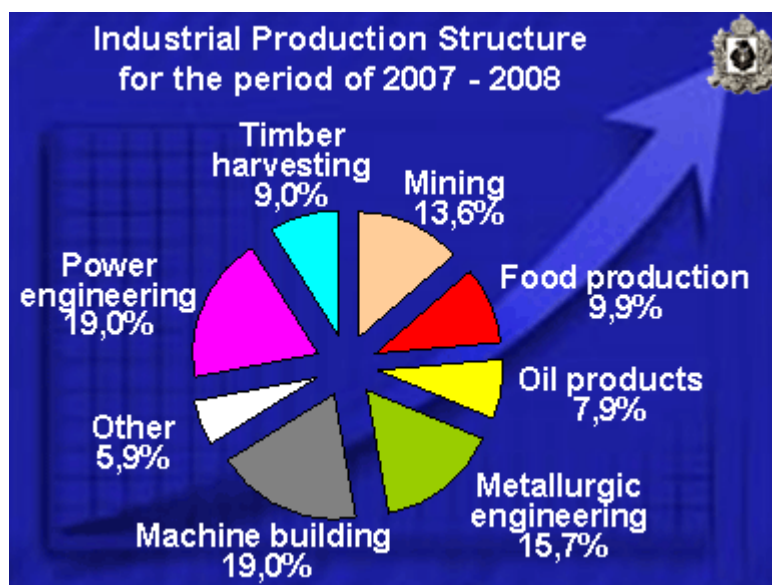
Distinguished Forum participants and guests!

It is a particular pleasure to warmly welcome you to hospitable land of Khabarovsk Krai.

The economy of Khabarovsk Krai is a multi-industry one; it is based on developed and diversified industrial production and services provided to long-haul transport traffic; unlike the resource based economy of the Far Eastern Federal District.

In my report, I would like to dwell upon the key priority sectors of economy, the sectors of high growth potential. Global financial crisis exercises influence upon the implementation of the prospective plans, however it does not modify the ranking of strategic priorities of the Krai economic policy.

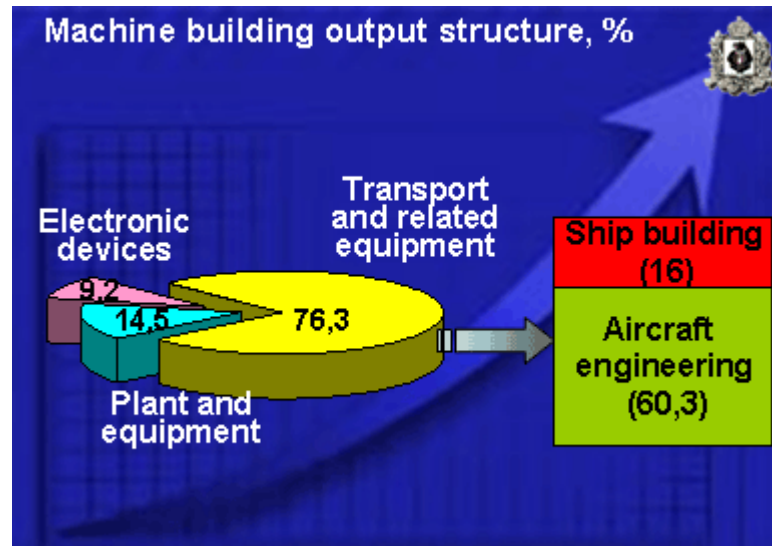
Slide 2



We consider machine building as a backbone of industrial and innovation development of the Krai; this sector of industry generates high-quality labor and competitive high-tech products. Machine building accounts for about 20 per cent of Krai industrial output. However, in period of time between 2000 and 2003 it accounted for more than 45 per cent of Krai industrial output.

Khabarovsk Krai machine building is a multi-industry one, one can point out that aircraft and ship building industries are the biggest by the volume output and development potential.

## Slide 3



Aircraft-building industry development in Khabarovsk Krai envisages the domestic and global market entry with the highly competitive civil aircraft; capacity building for military aircraft engineering.

## Slide 4



Komsomolsk-on-Amur Aircraft Production Association named after Yuri Gagarin is the largest aircraft manufacturing facility in the Krai.

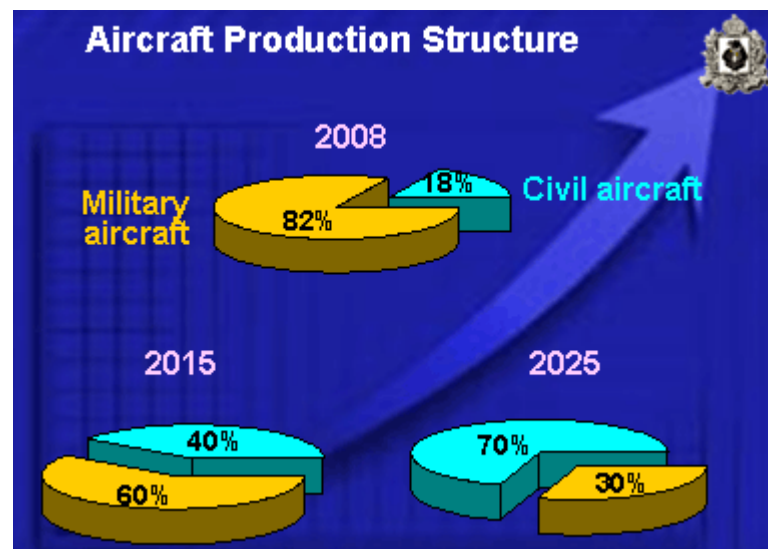
Recently, KNAAPO has been undergoing a comprehensive upgrade of its production facilities. The digital aircraft design and technological production process preparation will increase company's efficiency and competitiveness of its products. Medium-haul aircraft «Sukhoi Superjet 100» will be commissioned shortly. The company won contracts for more than 100 jets. KNAAPO will eventually produce about 70 aircraft per annum.

## Slide 5



Military aircraft production plays an important role in company's activities. Russian Federation Defense Ministry placed orders for a large number of the state-of-the art SU-35 FLANKER-E multirole fighters. 5<sup>th</sup> generation fighter will be finalized and mass manufactured at a later stage.

## Slide 6



After implementation of the programs targeted at production of new aircraft, the production rate will grow a great deal and its production structure will be modified considerably. At this stage military aircraft production accounts for 80% of all output. By the year 2015 civil aircraft production will grow up to 40%. By the year 2025 civil aircraft production will be as high as 70% of total aircraft output. As the result the company will become more competitive and stable in a highly volatile military aircraft market.

## Slide 7



Apart from that Khabarovsk Krai strategy on development of machine-building complex is based on shipbuilding development, including military, dual-purpose and civil shipbuilding.

## Slide 8



We have formulated the following market development objective: fishing vessels, tanker fleet, dry-cargo freighters, and offshore service vessels. We believe that one of the promising development avenues is the cooperation in manufacturing of offshore oil and gas drilling rigs, given the fact that we have already gained positive experience of that kind.

Military shipbuilding definitely remains as an industrial specialization of Khabarovsk Krai. At the same time, the current complicated state of affairs in the shipbuilding industry persists. There is underutilization of the existing capacities due to shortage of defense and

civil contracts. Technical and engineering capabilities of shipbuilding industry, as contrasted with aircraft manufacturing one, have not been upgraded in recent years.

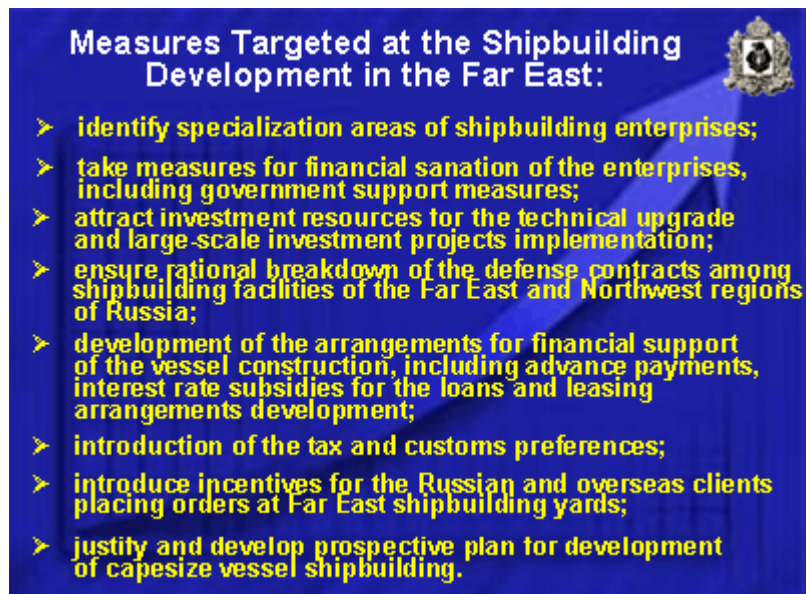
Civil and defense capability of shipbuilding industry in the Far East could be implemented with proviso that a comprehensive set of measures targeted at the upgrade of the national and regional shipbuilding industry will be adopted and implemented.

Slide 9



It is necessary to finalize the formation of the Far East Shipbuilding and Ship Repair Center and its policy.

Slide 10

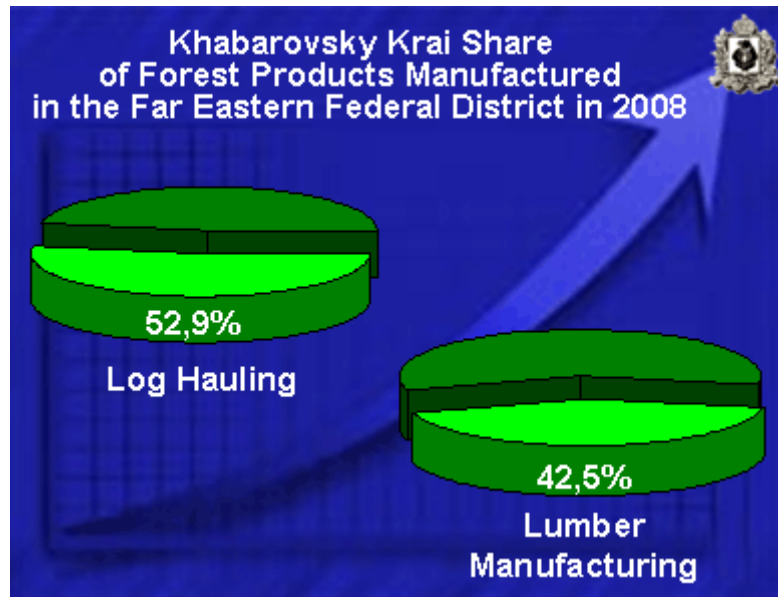


From our point of view, it should contain such measures as development of financial support arrangements for vessel construction, attract investments for the industry retrofit, provide incentives to the Russian and overseas clients, rational breakdown of the defense contracts, specialization of the shipbuilding facilities and long-term plan development.

Implementation of the measures demonstrated at the slide will make the industry more competitive, implement potential opportunities for the industry development, develop a powerful shipbuilding center in the Far East.

Khabarovsk Krai is rich in woodlands and timber resources. More than a quarter of the Far East timber resources are in Khabarovsk Krai. Available cutting area is more than 15 mln. cubic meters.

Slide 11

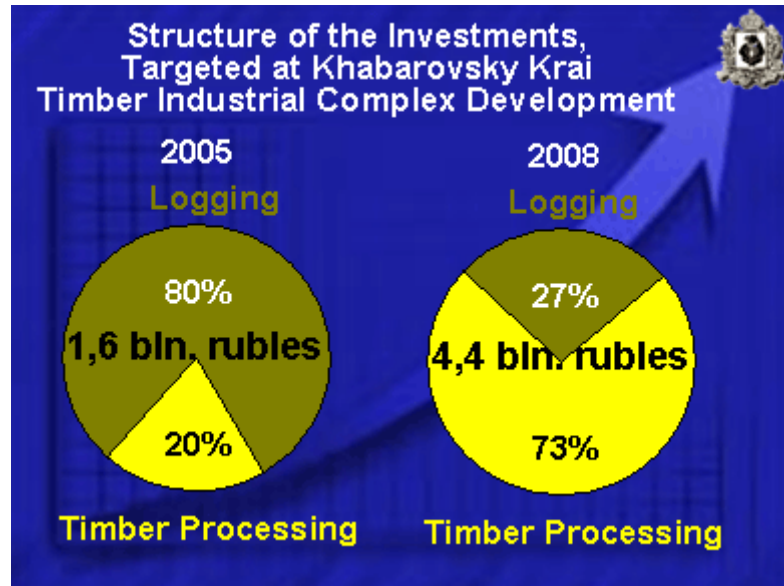


Khabarovsk Krai is the largest producer of major types of timber products in the Far East region.

Khabarovsk Krai, as well as other regions of the Far East, majors in logging with the subsequent exports of logs overseas. There is a shortage of timber processing capacities. In connection with this, we have assigned a task to dramatically increase the timber industrial complex efficiency, ensure comprehensive utilization of timber resources by introducing new technologies of sustainable forest management.

A strategy of upgrading timber industrial complex has been elaborated and utilized in Khabarovsk Krai focused on modern timber processing facilities development, forest protection and rehabilitation.

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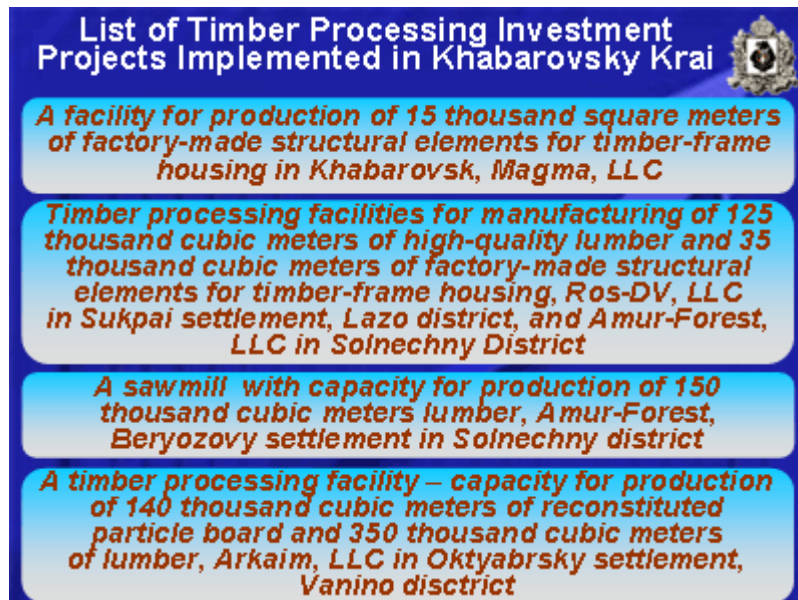


During last three years the investment structure of monies targeted at the timber industry has changed dramatically.

73 per cent of investments were channeled to timber processing projects in 2008; however the share of investments in timber processing had not exceeded 20 per cent in 2005.

Currently a number of large scale timber processing projects have been implemented.

## Slide 13

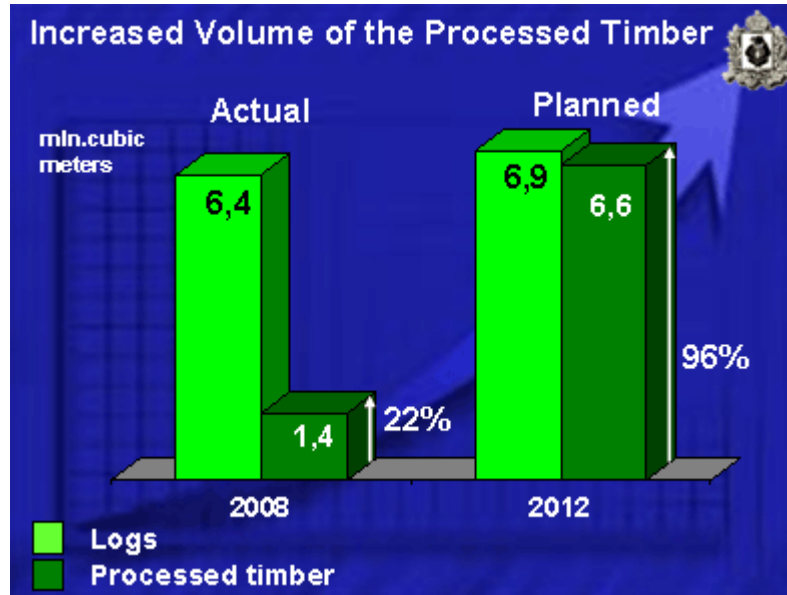


July saw the completion of the construction of the first stage of the timber processing complex for reconstituted particle board manufacturing and high-quality lumber by joint venture Arkaim, LLC. Construction of the MDF manufacturing facility by Rimbunan Hijau

MDF, Ltd is under way; DalEvroles Co., Ltd is in the process of construction of the veneer plant. Dalleprom, JSC has started the construction of the facility for veneer production in the city of Amursk and chip production facility in Vanino settlement.

Implementation of the planned investment projects will considerably decrease exports of logs.

Slide 14



However, the implementation of the timber industry upgrade strategy requires the streamlining of the timber export policy.

In order to increase resilience of the regional timber products market, provide incentives for development of timber processing, we propose to introduce prohibitive export duties for log exports for three years, at the same time reduce duties (down to zero) for the companies involved in the implementation of the large scale timber processing projects.

Streamlining of the timber companies export policy is issue of the day. About 30 per cent of the export revenue is lost as the result of the piecemeal activities of Khabarovsk timber exporting companies. The price on Russian timber in overseas markets, as a rule, is considerably lower compared to our major competitors' prices, given the fact that the quality of the timber is the same. We should seriously analyze the successes of the overseas timber exporting and importing associations; revise forgotten Russian successful approaches and finalize an efficient timber export system.

Despite favorable commercial prospects, preparation and implementation efficiency of timber investment projects is restrained by infrastructure limitations, high transport and energy costs.

There are no pulp-processing facilities in the Far East; pulp-processing plants are major users of low quality timber, as the result about three million cubic meters of low quality timber is not utilized according expert estimates.

A construction of the pulp-processing plant is envisaged in the city of Amursk. The plant capacity is up to 500 tones per annum. The cost of the project is more than 30 billion rubles. Investments in infrastructure are about five billion rubles. We consider that Russian Federation Government should consider its participation in the project on conditions of public private partnership and utilize Investment Fund financial resources to this end.

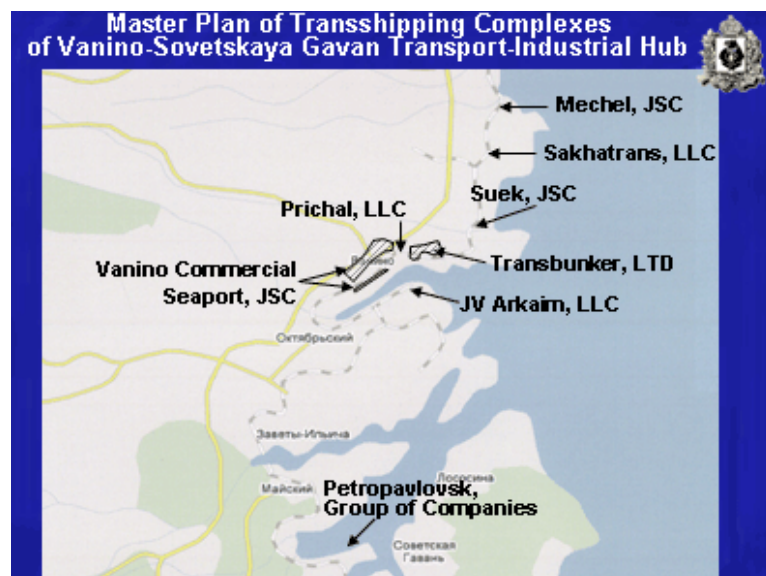
I would like to draw your attention to the third issue – transport infrastructure development.

Development of a powerful transportation framework in Eastern Russia is one of the critical elements for the successful implementation of the Development Strategy of Far East and Baikal region till 2025.

A number of large scale transport projects are in the process of preparation and/or implementation, targeted at strengthening of the transit functions of the region, removal of the infrastructure limitations and contribute to the development of the economy, create favorable conditions for habitation of people and contribute to improvement of Krai investment appeal.

I would like to draw your attention to the most critical issues.

Slide 15

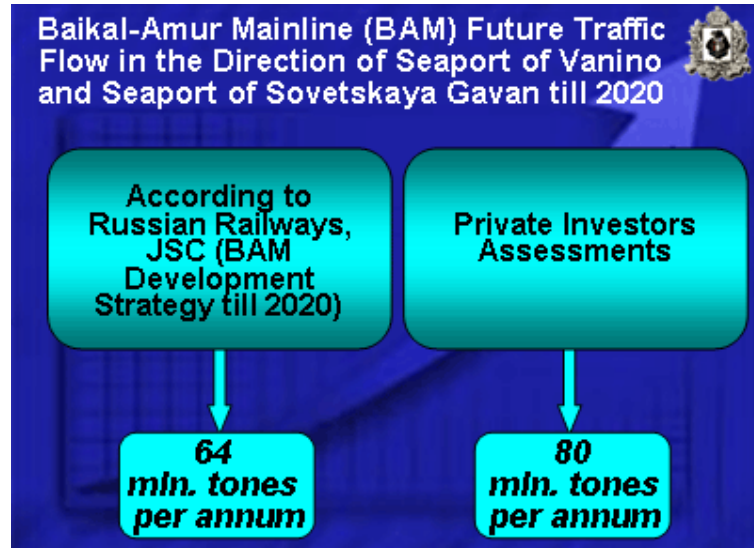


A new Vanino-Sovetskaya Gavan Transport - Industrial Hub is being built in the Vanino and Muchke bays of the Sovetskaya Gavan gulf. The cargo handling capacity of the hub will grow from current 10 million tones up to 80 million tones in 2020. The work is under way for establishing the first sea port special economic zone in Sovetskaya Gavan port

following the federal tender results. The existing transport network does not meet future demand.

The topical issue is the endorsement of the Russian Railways, JSC plans for expansion of the Baikal - Amur Mainline (BAM) throughput in the direction of the seaport of Vanino and the seaport of Sovetskaya Gavan.

Slide16



We have not yet agreed upon this issue. This ambiguity negatively impacts private business decisions on developing port cargo terminals and time of their completion.

As the above projects are highly capitalized, the government support is required for Russian Railways, JSC, including public-private partnership arrangement.

Unfortunately, the Russian Federation Government decree has not yet been endorsed on the Sovetskaya Gavan sea port special economic zone development as the result Vanino–Sovetskaya Gavan Transport Industrial Hub development has been slowed down.

Slide 17



Another critical transport infrastructure development project is the construction of the Far Eastern Air Logistics Hub in the Novy international airport, city of Khabarovsk. The completion of this project will not only streamline air transport system but it will allow the Hub to become an integrated part of the Asia Pacific Region international air transportation network.

Motorway network development is definitely of paramount importance for Eastern Russia. The motorway density of Far Eastern Federal district is the lowest among all Federal Districts. Khabarovsky Krai motorway density is lower 6 times than an average indicator in Russia. We believe that funding for motorway construction should not be cut down; moreover motorway construction provides employment and contracts for the construction industry enterprises.

Construction of the federal highway "Amur" (Chita – Khabarovsk) is going to be finalized in 2010. The highway commissioning will be instrumental for more active truck transportation in the Far East. At the same time, the combined two lane bridge across the Amur River can become a bottleneck, as there is a four lane highway approach to combined bridge. We have raised several times an issue for construction of the second phase of the motorway bridge and the railway bridge in the Russian Federation government and Ministry of Transport of Russia. However, the positive decision has not been made till now.

I strongly believe that endorsement of the development Strategy for the Far East and Baikal region will facilitate the implementation of the long-term development plans of each territory.

Thank you for your attention.