

Interim Report

IR-99-054

On the Establishment of Trust in the Russian Forest Sector

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Approved by

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11 October 1999

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Abstract

The present situation in the Russian forest sector, with a harvest less than one fifth of the annual allowable cut, cannot be attributed to the physical world. The country has an abundant resource, which is poorly utilized. This paper seeks an explanation for this tendency by sampling the experiences of individual actors within the sector. These are compared with a similar sample from the Swedish forest sector. It can be established that there is a major lack of trust between the actors involved in the Russian forest sector. Violation of selling agreements leads to a demand by actors for advance payments in order to safeguard their interests. Based upon a verified hypothesis, it is argued that, although partially a historical residue, trust can be established between actors with diverging self-interests. Conclusively, it is assumed that the actors of the industry themselves must participate in the establishment of trust, while the role of political institutions, such as the state, should be to provide the legal instruments necessary to protect the individual actor's own right to pursue his self-interest, in brief, to provide the constituents of a democratic system that can promote economic development.

Key words: Russia, forest industry, trust, self-interest, collective action, Wood Measuring Societies.

Acknowledgments

I would like to express my gratitude to those who, in various ways, contributed to the completion of this paper. Firstly, to those professionally involved in IIASA's Sustainable Boreal Forest Resources Project. These are the project leader, Sten Nilsson, and the assigned supervisors, Lars Carlsson, Nils-Gustav Lundgren, and Mats-Olov Olsson. Secondly, I would like to express my appreciation to those not formally involved in the project, but who still provided their support. Here I owe gratitude to my colleague, Carina Lundmark, for giving valuable comments on my work, to my fellow participant of the YSSP, Piotr Nowak, for aiding me whenever my computer caused distress. Lastly, to my husband and colleague, Terence Fell, for enduring readings of numerous versions of this paper and for everything else.

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1. INTRODUCTION

As is well known, forested areas cover a large part of the Russian Federation and those forests are of crucial importance to all life sources. The vastness of the Russian forests makes a well functioning forest industry an important economic issue in a nation going through economic transition. The ownership and management of the forest areas of Russia have varied throughout history (The World Bank, 1997). At the end of the 18th century Russian forests were the private property of the few. In the middle of the 19th century, forests showed signs of overuse. This problem was recognized and subsequently led to the introduction of The Principles of Forest Conservation, which was an attempt to manage and conserve the forest in a more sustainable way. After the revolution of 1917, the people were declared owners of the forests that were to be managed for the common good of the nation by filling centrally planned production quotas at prices that were fixed through political decision-making rather than through the relation between supply and demand.

After the collapse of the Soviet Union the situation changed. Since 1991, the price level in the Russian forest sector has, to a large extent, been made sensitive to supply and demand (Backman, 1998). This has led to an increase of tariffs on transport while, at the same time, the prices of timber has dropped, which has affected some parts of Russia harder than others. Today, people in Russia make use of these forest-covered areas, not only by enjoying oxygen while breathing, but also as a well from which they draw resources such as game, fruits, berries, mushrooms, nuts, and medicinal raw materials (Nilsson and Shvidenko, 1997). This can, of course, be of major economic value for the individual, but for the Russian economy this exploitation of the forest-covered areas of the country is of negligible importance. The fact that the use of non-wood forest products is unevenly distributed among the population, but in fact plays a major part in the livelihood of some of the Russian indigenous peoples, is by far insignificant in the ongoing discussion about the future use of forest resources. The development of the Russian forest industry is, however, not regarded here as contradictory to the needs of these minorities. On the contrary, a decline in employment and income for those

formerly engaged in the forest industry has brought about a situation where the indigenous peoples have to compete for food and firewood (The World Bank, 1997).

Previous research (Nilsson and Shvidenko, 1997; Carlsson and Olsson, 1998; Carlsson *et al.*, 1999) has noted that the Russian forest industry has nearly reached deadlock. In spite of the abundance of forested areas Russian harvests have declined from almost 350 million m³ in 1985 to 125 million m³ in 1996, or by 64 % over an 11 year period (Nilsson and Shvidenko, 1997:11). In 1997, the actual harvest in Russia went below 100 million m³, or one fifth of the annual allowable cut of 500 million m³ (Palo and Uusivuori, 1999:345). Russia is today losing its share of the international timber market, while at the same time, suffering from a decline in national consumption of forest products (Backman, 1998). It should be noted that a decline in harvesting might not be the environmental advantage it initially appeared. Conversely, the forest industry of the former Soviet Union left parts of the woodlands ravaged by severe over-harvesting, while at the same time, due to logistical difficulties, other parts were left untouched (Nilsson and Shvidenko, 1997). In these remote areas you will today find problems with high mortality, due to forest fires and damage caused by insect outbreaks. These problems could be eased by thinning and sanitary felling.

The transition of the formerly planned economy of Russia has been described as a "... redesign of the institutional framework" (Raiser, 1997:2). The problems that face the Russian forest industry today cannot be attributed to the physical world or the forest resource itself, but rather to the institutions of Russian society. Institutions should be understood in accordance with Douglass North's (1990:3) definition, as "... the rules of the game in a society or, more formally, [institutions] are the humanly devised constraints that shape human interaction. In consequence they structure incentives in human exchange, whether political, social or economic." These institutions are of both formal and informal character and have a "... joint role in reducing transaction costs and facilitating economic exchange" (Raiser, 1997:2). The institutions that are to be examined here are the informal ones that partly shape the economic interaction in the Russian forest industry and could be described as "... the collection of social norms,

conventions, and moral values that constrain individuals and organisations in pursuit of their goals” (Raiser, 1997:2).

One factor of great importance in human relations of all kinds is the degree to which people are ready to trust each other. As the following quotation suggests, one could not overestimate the importance of trust; on the contrary “...one of the most important lessons we can learn from an examination of economic life is that a nation’s well-being, as well as its ability to compete, is conditioned by a single, pervasive cultural characteristic: the level of trust inherent in society” (Fukuyama, 1995:7). As this quotation suggests, the level of trust between actors strongly affects their performance. If this assumption is right the situation in the Russian forest sector with its decreasing harvests might be possible to explain in relation to the notion of trust.

The aim of this paper is twofold, firstly it aims to estimate and discuss the importance of trust between actors in the Russian forest sector. And, secondly, it aims to indicate what might be done if the situation one finds today in the Russian forest industry is affected by a lack of trust between actors.

In order to find the informal rules that shape the incentives governing the actors, this study will be carried out, not by examining the written laws of the country but by taking part of the actors’ own description of their business behavior. By evaluating these incentives it should be possible to determine whether or not the situation we see in the Russian forest sector is, in fact, affected negatively by a lack of trust between actors. To get a reference, to which one can compare the business behavior in the Russian forest sector, a parallel study of behavior in the Swedish forest sector will be conducted. The hypothesis that is to be tested here is the following: It is possible to establish trust between actors with divergent self-interests in order to contribute to solving the problems affecting their interaction.

1.1 Approaching the Problem

This paper is based on the assumption that people active within any industry are those who can give the most accurate description of their field of work. The comparison of business activities in the two countries is therefore based upon a series of interviews with forest owners and forest companies in Russia and Sweden (see the Appendix). In these interviews people describe their relationship to their business associates and to the banking system by sharing their experiences of the institutions that shape their behavior. The level of trust between actors is, in this analysis of business behavior, not seen as something exactly measurable. If this was so, one could produce a specific measure of trust. Then one could say that the level of trust the respondents in country A are ready to bestow in their customers reaches the level of 5 while the level in B is 6. It will, however, give us an indicator of the level of trust between the actors in question so one can assess the level as being high or low.

It should be emphasized that the analysis is not based on the assumption that Sweden and the other countries in the western world are flawless utopias, but rather that the market economy, together with the political democratization, has created societies with strong positive features, such as general welfare, etc.

This analysis is based on a view of business behavior as possible to understand through teleological explanations. Such explanations are based on the assumption of man as rational and capable of choosing the course of action that he assumes most likely will lead to the goal he is trying to reach. The chosen path of action may, of course, lead him astray but what should be remembered is that, from his point of view, it seemed the best alternative action at that given time and place, even if the outcome of his action subsequently turned out to be less than optimal. An outcome below the optimal can be due to the lack of knowledge about factors that might appear along the path. To have the complete picture of factors affecting the outcome may probably be impossible, but our man is assumed to lessen the amount of costly uncertainties he has to face by accessing useful information. One factor that can affect the availability of information is, of

course, the cost of accessing it. Here, it will be argued that cooperation will reduce the cost for obtaining useful information.

If one considers man capable of this kind of rationality and if you think of him as pursuing his self-interest you will, according to Fukuyama (1995), in eighty percent of all cases be able to explain his way of action. The fact that you might be wrong in your explanation is due to the different social settings in which man acts. The interviews used in this paper will aggregate a picture of the social setting, or the incentives, facing the actors in question, people active within the Swedish and the Russian forest industry. If man were regarded as acting irrationally, perhaps because he landed far from where he aimed or because the path he chose, in retrospect, could be considered somewhat strange, it would, of course, be impossible to explain business behavior from this approach.

The individual interest, or self-interest, of human beings has played an important part in political philosophy for quite some time. By quoting a famous passage by Adam Smith, Huemer puts the self-interest of human beings in an economic context, "It is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner, but from their regard to their own interest" (Smith 1776 in Huemer, 1998:43). In other words, the utility-maximizing baker should be regarded as working for his own benefit. Another concept that has undergone careful examination is that of the dilemma of collective action. This paper is about the problems that occur when individual actors find themselves in a situation where they would benefit from taking actions collectively in order to better utilize their right to pursue their self-interest. An early writer on this topic is David Hume (Hume in Putnam, 1993:163), who describes it as follows:

Your corn is ripe to-day; mine will be so to-morrow. 'Tis profitable for us both, that I shou'd labour with you to-day, and that you shou'd aid me to-morrow. I have no kindness for you, and know you have as little for me. I will not therefore, take any pains upon your account; and should I labour with you upon my own account, in expectation of a return, I know I shou'd be disappointed, and that I shou'd in vain depend upon your gratitude. Here then I leave you to labour alone; You treat me in the same manner. The seasons change; and both of us lose our harvest for want of mutual confidence and security.

What the farmers here cannot take for granted is that his neighbor will return a friendly act. Fukuyama finds one source to the problem of collective action; it occurs simply because we are not angels but human beings. An obvious solution to this problem is to establish institutions in society, such as clear rules that promote collective action but also allow actors to pursue their self-interests.

What the future will look like in Russia is of course — to the extent it is actually a matter within reach of the Russian political system — a matter for the Russian people to decide. It is, however, neither taken for granted that Russia could, in detail, copy the development of the Western world, nor that Russia is so different that its future development by necessity must be completely different from that of other European countries. Fukuyama (1995:4) describes countries' alternative paths of development as follows "... the world's advanced countries have no alternative model of political and economic organization other than democratic capitalism to which they can aspire." Anyone can, of course, dispute Fukuyama's conclusion since there might be a rich variety of alternative models of economic and political organization towards which Russia might, in fact, come to aspire. But it is, nevertheless, not possible to conduct a comparative study of the incentives facing actors in the Russian forest industry without relating these incentives to "something". The incentives facing the actors in the forest industry of Sweden, a country regarded by most as both capitalistic and democratic, are in this case used to allow a comparison.

1.2 The Structure of the Report

The second chapter deals with the notion of trust in order to explain how the concept will be conceived in this report. The aim is to locate the sources of trust and to discuss its importance in a market economy.

The third chapter consists of a description and an analysis of business behavior in Russia and Sweden. The aim of this chapter is to establish whether or not the present situation in the Russian forest sector can be attributed to a lack of trust between actors. The 221 interviews in Russia and 24 in Sweden, was conducted following a

questionnaire designed at IIASA (see the Appendix). Interviews have been carried out in the following regions of Russia; Arkhangelsk, Irkutsk, Karelia, Khabarovsk, Krasnoyarsk, Moscow, Murmansk and Tomsk. In Sweden, all of the companies interviewed are located in the most northern part of the country, Norrbotten. In order to get a picture of both new and more established actors, the companies in both countries varied in the number of employees as well as in the year of establishment. To illustrate the different stages, from the forest to the market, the selection of companies was carried out in a fashion that made sure that all possible actors, such as forest owners, sawmills, harvesting companies, etc., were asked to share their experiences of market behavior.

The fourth chapter presents an example from the Swedish forest sector, the establishment of Wood Measuring Societies. The aim of this chapter is twofold, firstly to test the hypothesis that trust can be established between actors with diverging self-interests and, secondly, to analyze the process in relation to what has been stated in chapter 2 as the sources of trust. This will provide some understanding of the driving forces of the process itself.

The final chapter discusses how one might benefit from past experiences in order to improve the situation in the Russian forest industry for the future. The discussion will focus on the division of labor between actors who can, presumably, bring about a change. Can one, from what has been presented in previous chapters, conclude what private actors can achieve themselves and what ought to be the responsibilities of the state?

2. ON THE NOTION OF TRUST

As is often the case with abstract notions such as trust, much time has been spent trying to formulate a definition that would win world-wide acceptance (on this quest see Huemer, 1998). That is not the goal here. This exploration of one of the many definitions of the concept of trust has a somewhat less philosophical purpose, namely to introduce a definition of the concept that will be used while analyzing a series of

interviews with Swedish and Russian forest companies. Trust will be interpreted as nothing more complicated than, in Huemer's words (1998:94) "...the optimistic expectations of a single individual relative to a prospective outcome of an uncertain event." This definition will be used while discussing its importance in business relations, the sources from which trust evolves and to ascertain whether or not trust has been established.

2.1 The Importance of Trust

Fukuyama (1995) describes trust as essential in the economic sphere of human life, a sphere that by no means should be regarded as equipped with, or dominated by, norms and rules that widely differ from other aspects of human activity. There is always some level of risk involved in transactions. Fukuyama presents everyday cases. The manager of a restaurant will let the guest finish the meal before asking for payment and the calculating customer evaluates the utility of a single free meal in relation to the economic and social costs if caught running from the bill. Whatever steps taken by the manager to reduce the risk of being cheated by customers will be an economic burden, a transaction cost that might be possible to measure.

The way we make decisions in our private life and how we do it in business transactions is basically the same. We evaluate the expected utility in relation to whatever moral bond we might transgress. Then we act according to our calculations. When we have to estimate the trustworthiness of our business associates we reach a more complicated stage. In non-personal relations trust consists of the positive expectation on the other party's willingness to comply with legal norms, such as contracts. Compliance with the legal norms of business transactions is the fulfillment of agreements and contracts. If our business associates fail to do so it is, of course, important that we can trust society's institutions to be equipped with both the legal rights and the capabilities to take sanctions against them. In order to sustain legal norms and promote rule compliance the effectiveness of society's law enforcement becomes essential. As Hendley *et al.*, (1997:19) put it, for actors to engage in impersonal relations it might be especially important that an economy in transition is equipped with institutions that enhances trust, such as, "(1) generally accepted rules that help to structure economic relationships; (2)

mechanisms for enforcing agreements; and (3) procedure for dispute resolution.” Based upon the experiences expressed in the interviews, the willingness to comply with legal norms among actors in the Russian and the Swedish forest sectors will be revealed.

2.2 The Sources of Trust

If, as Fukuyama (1995) suggests, trust is the lubricant of the market economy strongly effecting the economic performance of countries, one might suspect that the Russian forest industry is affected by a lack of trust between actors. Locating the sources of trust matters since, as stated in the introduction, the hypothesis that is to be tested here is that a heightened or increased level of trust can be a solution to problems with collective action, even between actors with diverging self-interests. But there are (Mishler and Rose, 1998:4), other convincing arguments for this pursuit

Distinguishing the sources of trust in institutions is important not only for testing competing theories, it also has significant implications for public policy. If political trust (or distrust) is culturally conditioned and rooted in long standing patterns of interpersonal relations, then there is little the new democracies can do to cultivate trust in political institutions.

In other words, if the outcome one can see today in the Russian forest industry can be associated to a lack of trust between actors and if one finds the sources of trust to be solely historical, what can policy makers possibly do to affect the future of the industry but nothing?

According to Fukuyama (1995), the foundation from which trust can emanate is shared norms and values that sometimes has a religious source. These norms and values do partly depend on the historical development of society and they will affect the way you act towards the society around you. However, in their study of the sources of trust Mishler and Rose (1998), find reason to question if trust has purely historical roots as it is sometimes postulated. Political trust can also be described as partly a result of the socialization process where we learn to trust first of all the ones closest to us, the family, and later people we interact with in civil society or “...all non-governmental organizations, such as the press, leisure clubs, churches, neighborhood associations and so on” (Raiser, 1997:11). Here, in order to separate them from other ways of explaining

the sources of trust, theories that finds the roots of trust to be partly historical and partly based upon our interaction with the civil society will be called *cultural theories* of political trust.

According to other theorists, political trust is a response to, or an evaluation of, how well various institutions, such as governments, fulfill their objectives. Distinguishing established democracies from new ones Mishler and Rose (1998) make the following observation of these theorists' way of explaining the importance of policy outcome, such as economic prosperity, as a basis for public trust. It is primarily in established democracies that public trust in political institutions depends upon the policy outcome, while in new democracies, such as the post-communist countries, the character of the political institutions may be just as important as policy outcome. In these countries, the political institutions were ill famed for a long time for their characteristic subjugating of individual interests in favor of those of the state and for their oppression of individual liberties. This way of describing the sources of trust will be called here *institutionalist theories* of political trust.

These two ways of explaining trust do not necessarily have to be mutually exclusive, but may in fact be complimentary. Both cultural and institutional theory appears to find trust to be based on experience. The difference between them can, according to Mishler and Rose, be defined by how long the human learning process is assumed to be. Cultural theories (Putnam, 1993; Fukuyama, 1995) put much emphasis on things learned during the early stages of life, "The basic cultural hypothesis is that national political institutions will be trusted in direct proportion to the extent of interpersonal trust" (Mishler and Rose, 1998:6). Institutional theories, on the other hand (North, 1990), stress the importance of the individual experiences of adults. It is as rational adults that we respond to the performance of political institutions. If one, as the institutional theorists do, accepts history and culture as perhaps hampering but not entirely decisive for the future and if one, furthermore, assumes human beings to be rational in their choices, it follows that the political institutions will acquire a design that will win public trust. So, in order to win the trust of the people the political institutions of the new democracies face a change in character that is equally essential as

economic performance. “Specifically, higher growth, less corruption and more freedom should produce greater trust in political institutions” (Mishler and Rose, 1998:10).

Are these sources of trust — presented here by cultural and institutionalist theories — also producing certain relations of trust, or distrust, between actors in the forest industry of the countries in question, Sweden and Russia? Or are there other forces at work here? There seems to be no logical explanation to why not trust, or distrust, between actors in the forest market could evolve and be established through institutional change in the same fashion as in society as a whole. Thus, the rational seller of timber will respond to the performance of his customers and other actors who will influence the outcome. If the rules of the game do not allow the actors to interact to their own liking, they will, according to institutionalist theories, change the rules. The new rules, or institutions, could be considered as trust-establishing if they, through a new design, win the trust of the actors on the timber market.

In conclusion, one might add that the existence of trust between actors in a market economy is crucial. Without an acceptable level of trust, the cost of protecting one’s own interests from being ravaged by other actors becomes economically unbearable. And, furthermore, trust can partly be conceived of as determined by the historical development of societies, but also as a property that can be enhanced by institutional change, given, of course, the possibility for people to cooperate and take part in the process of evaluating and changing the institutions of society.

3. BUSINESS BEHAVIOR

In this chapter, the business behavior of a sample of actors within the Russian and Swedish forest industries will be illustrated. By analyzing the answers from the interviews a picture of the incentives facing the actors should emerge. What is of interest here, is to discuss whether or not one can explain the situation in the Russian forest industry with the decline in harvest from this sample of forest companies in relation to the notion of trust. The focal point will be on factors and institutional arrangements on the societal level that Huemer (1998) describes as formal substitutes

for trust, such as, sanctioning capabilities. The actors here are not only sellers and buyers of timber, but also banks and other institutions in society, such as the Russian Arbitration (arbitrazh) Courts, the judicial body in Russia dealing with disputes between companies. In Russia, 221 forest companies have been asked to share their experiences, while the interviewed companies in Sweden reached 24.

3.1 Violation of Selling Agreements

In *Table 1*, answers to the following question are presented: Do you regard violations of selling agreements as a problem? As one can see, nearly 53% in the Russian sample consider this to be a big problem, while 20.4% of them found it to be a small problem. In Sweden, none of the interviewed companies described this a large problem, but 12.5% considered violation of selling agreements to be a small problem.

In other words, out of all the interviewed companies in Russia, 73.3% had experienced problems with this type of violation. One form of violation of selling agreements that causes a problem in the Russian economy is the renegotiating of contracts (Hendley *et al.*, 1997), not only the time for delivery but also the quantity and prices of goods may be altered. These violations of agreements might affect the level of trust between companies. In other words, experiences of previous violations of selling agreements will partly shape the incentives facing every single actor about to engage in a second round of business contacts.

Table 1: Violation of selling agreements

	Russia	Sweden
Big problem	52.9	0
Small problem	20.4	12.5
No problem	15.8	87.5
No answer	10.9	0
Total	100	100

Source: The IIASA Institutional Framework Database.

In percent: Russian sample N= 221, Swedish sample N=24

3.2 Enforcement of Selling Agreements

Table 2 shows the answers to the following question: What will happen if either part breaks the agreement? The interviewed actors in the two countries show similar behavior when their counterparts do not fulfill agreements. It seems that the first step taken is to negotiate and, in some cases, to abstain from further contacts with the defaulting party. In the Russian forest industry, the Arbitrazh Courts deals with 20.4% of the disputes between parties. The Arbitrazh Courts' law enforcement capabilities have been questioned in previous research (Hendley *et al.*, 1997). Out of the interviewed Russian forest companies, 20.4% of the cases will, however, put their hope or faith, in this way of solving problems with violations of agreements. This supports the conclusion that the Arbitrazh Courts, even if not working to perfection, have some potential usefulness (Hendley *et al.*, 1997).

Table 2: Enforcement of selling agreements

	Russia	Sweden
Negotiation	10.9	12.5
Sanctions financial/other	13.1	16.7
No more business	9.5	4.2
Negotiation/non formal	1.4	0
Negotiation/arbitration	20.4	12.5
Nothing happens	10.4	8.3
No problem	14.9	45.8
No answer	19.5	0
Total	100	100

Source: The IIASA Institutional Framework Database.

In percent: Russian sample N= 221, Swedish sample N=24

3.3 Arrangement of Selling Payments

How, then, can this business behavior be analyzed according to what has been stated earlier, assuming that the actors are pursuing their self-interest, and that the level of trust they are ready to bestow in others is based upon experience and their evaluation of the institutions, or rules in use? How will our actors respond to violated or renegotiated selling agreements?

Table 3 summarizes the answers to the following question: When is timber or wood paid for? In answering this question, the interviewed companies reveal the level of trust

they are ready to bestow in their customers by stating at what time they demand to get payment for products from their customers; the alternatives being before, on, or after delivery.

One difference in business behavior between the interviewed companies that becomes obvious is the different habits of arranging payments between sellers and buyers of forest products. While in the Swedish sample, the seller of a product seldom demands payment in advance, this is a far from a rare request made by companies in the Russian sample.

Among the Swedish respondents, the most common payment arrangement, used in 66.7% of all cases, is cash payment after delivery. In the Russian sample, on the other hand, only 3.2% of the companies would accept an arrangement where the entire sum was paid after delivery.

According to what has been stated earlier, this is a rational response to the incentives facing the interviewed actors. The level of trust that the Russian respondents of sellers are ready to bestow in their customers has been revealed and found to be low.

Another apparent difference between Russian and Swedish actors concerning payment arrangements is the use of non-monetary payment. While none of the Swedish respondents do so, more than 30% of the interviewed companies in Russia will accept, or demand, non-monetary payment, or barter. Along with an increase in violations of selling agreements barter is also becoming more common (Commander and Mumssen, 1998). Some of the problems connected to barter can be illustrated by the following example “You send the goods to an enterprise and they send you motorcycles. You don’t need motorcycles so you send them back and they send you wheat. Then you have to process the wheat. By the time this is done it is three months” (Hendley *et al.*, 1997:34). Still, this is the way an increasing number of Russian companies are transferring payments. Of the interviewed companies in Russia, 20% will accept, or demand, non-monetary payment, partly or to the full value of the products both as

sellers and in the role of buyer (The IIASA Institutional Framework Database). The question is, to what incentives facing the companies is this a rational response?

Table 3: Arrangement of selling payments

	Russia	Sweden
Cash before delivery	8.1	0
Cash and barter before/on delivery	35.3	0
Cash and barter on delivery	33.9	0
Cash on/after delivery	0.5	33.3
Cash after delivery	3.2	66.7
Other arrangements	19	0
Total	100	100

Source: The IIASA Institutional Framework Database.

In percent: Russian sample N= 221, Swedish sample N=24

3.4 Transferring Selling Payments

When asked to describe the arrangement of selling payments no less than 95.8% of the interviewed companies in Sweden accept, or demand, that money is transferred via the banking system only, while out of the Russian respondents, only 36.2% do so (see *Table 4*). How do the companies explain this behavior? Out of the 221 interviewed Russian companies more than 165 will not make use of the banking system. In this sample, as many as 10% make no use of the services provided by the banking system neither when selling nor when buying products (The IIASA Institutional Framework Database). What are their arguments for not doing so? Previous research (Commander and Mumssen, 1998) finds that Russian companies have financial incentives to avoid the banking system. Using the banking system could be costly because of the time it takes to transfer money. But, avoiding the banking system can also be interpreted as a measure taken to avoid taxation. Any money found on a bank account is likely to be used by the bank as payment of debts to the bank, or by the tax authorities as payment of tax.

Table 4: Transferring of selling payments

	Russia	Sweden
Via bank	36.2	95.8
Bank and company	44.8	4.2
Company self: cash/barter	10.0	0
Other arrangements	0.9	0
No answer	8.1	0
Total	100	100

Source: The IIASA Institutional Framework Database.

In percent: Russian sample N= 221, Swedish sample N=24

3.5 The Social Responsibilities of Forest Enterprises

In both countries, interviewed companies take on responsibilities that are not immediately connected to production. Through the interviews it became obvious that the social responsibilities of the Swedish sample are quite wide (The IIASA Institutional Framework Database). This is a notable since one would imagine that the adaptation to a market economy would entail a decrease of the social responsibilities of companies. In the former economic system of Russia, the forest companies often provided housing for their employees, schools for their children, medical care and subsidized transportation to make life in remote villages easier. This is changing (The World Bank, 1997). Today, the social responsibilities are being transferred to local governments who, due to a shrinking tax base, cannot provide sufficient services. This is why the standard of these services has deteriorated. Still, the forest companies in Russia are willing to take on social responsibilities far from the extent that is the habit of companies in the west. Some forest companies that have experienced a total stop in production still keep their former employees on the payroll to make it possible for them to continue to benefit from the services provided by the company (The World Bank, 1997). This may be taken as a sign that some properties of the old economic system are still surviving.

The social responsibilities that the interviewed companies in Sweden take on are different from those in Russia (The IIASA Institutional Framework Database). In the Swedish sample the most common form of social responsibility is to sponsor sports and leisure activities in local communities. These responsibilities vary from giving cash

support to local sports clubs to providing timber for the building of huts used by skiers and people driving snow mobile in the woods. No less than 45.8% of the interviewed companies in Sweden provide this. And, 12.5% of the interviewed companies, are providing opportunities for young teenagers to get a glimpse of the companies activities by inviting them to spend a few weeks as trainees (The IIASA Institutional Framework Database). By providing these facilities, these Swedish forest companies get a connection, not only to their own employees, but also to other people in the community. This is of course of importance, since forest companies are conducting their business in forested areas that are used by people for leisure.

3.6 Membership in Branch Organizations

Yet another difference between the companies in the sample that became obvious is their experience of membership in branch organizations. To the question: “Is the enterprise a member of any branch organizations?” the answers differ strongly between respondents in Russia and Sweden. In Sweden, a majority of the respondents are a member of branch organizations in order to access information, to regulate the relation between themselves and their employees, and to cooperate to strengthen the position of each individual company in regard to other actors. The Russian respondents, on the other hand, did not have this experience. The answers provided showed that the cooperation in branch organizations is something unfamiliar to the Russian respondents. Of course, one might cooperate but not in official branch organizations. How can one explain this difference in relation to the notion of trust? Mishler and Rose (1995:5) provides the following explanation

Trust also is a necessary condition for individuals to participate voluntarily in collective institutions, whether directly political institutions such as political parties or institutions of civil society such as labour unions, economic associations, and churches.

It became obvious that the present situation in the Russian forest sector can be explained in relation to the level of trust between the actors. The decrease in harvest can partly be explained by a widely spread reluctance among sellers to accept payment after delivery. The reason for this reluctance can be sought in their experiences of violations of selling agreements.

4. THE ESTABLISHMENT OF TRUST

The analysis of the interviews shows that there is an almost paralyzing lack of trust between actors in the Russian forest industry. Assuming that there always is a potential risk involved in business transactions, would it then be possible to reduce this risk by establishing trust between the parties involved? The purpose with the following short example from the Swedish forest sector is to answer that question. In other words, to test the hypothesis that trust can be established as a solution to some specific problems with collective action between actors with diverging self-interests. This will be done firstly by elucidating one part of the chain of interactions that is a result of the actors trying to solve problems connected with the Swedish forest industry, namely the establishment of an objective wood measuring procedure and secondly, to analyze this in reference to what was stated in chapter 2, where it was claimed that history and the actors' rational response to the function of the institutions, or rules of the game, affect the level of trust. Can the establishment of Wood Measurement Societies in Sweden be used as an argument in favor of the assumption that cultural and institutional theories of the origins of trust are not mutually excluding but, in fact complimentary? If so, the following example could be used to indicate how the level of trust might, hypothetically, be enhanced in the Russian forest sector through institutional change.

4.1 The Swedish Wood Measurement Societies

As sawmills became a more common sight in the Swedish landscape in the middle of the 19th century competition increased among buyers of timber. Buyers were competing not only by offering the highest possible price but also by using different standards when measuring the timber. This was possible since no law stipulated otherwise. In 1892, the buyers of timber in Ådalen, a district located in the central part of Sweden, reached the conclusion that this would be to their disadvantage in the long run. This led buyers to organize their interests in Wood Measurement Societies, which ensured that all timber would be measured according to set rules and that the same price for wood would be offered by all potential buyers. Although this stabilized the timber market, it

proved to be a far from ideal situation for sellers of forest products since the buyers exclusively ran the Wood Measurement Societies to their own advantage (Skogsstyrelsen, 1965; Falk, 1992).

Therefore, the sellers of timber put pressure on the political institutions to bring about change. The question became a matter for the Swedish Parliament in 1932. It would last until 1935 before Sweden passed the first law that would also promote the interest of sellers by making way for them, and suggesting that equal influence should be granted them in existing Wood Measurement Societies. The Act of 1935 was only conclusive in those parts of the country where Wood Measurement Societies had previously been formed. Consequently, in some parts of Sweden, the relationship between sellers and buyers was still unregulated by law. In these parts, it was still common that buyers were competing by placing more generous bids on timber and offering more generous measuring procedures in order to be able to buy from sellers at attractive nearby locations (Skogsstyrelsen, 1965; Falk, 1992). The forming of Wood Measurement Societies in the late 19th century had, as its objective, to reduce the transaction costs of the individual buyers of timber. This situation, where buyers no longer had to send a representative to felling sites to bargain on prices, led to a substantial reduction of these costs (Falk, 1992:79). Today, the four existing Wood Measurement Societies to a great extent conduct the actual measuring of timber in Sweden (Skogsstyrelsen, 1998). The wood measurers are employed by, but independent of, sellers as well as buyers. Both sellers and buyers perceive this as a successful solution to the obvious problem posed by the diverging self-interests of the two parties.

This concludes one of three aims of this chapter. It seems clear that measures may indeed be taken that can establish trust between actors with diverging self-interests. Can one also determine from what source trust emanated in this case? In other words, can this example give support to either cultural theories or to institutional theories of political trust? The suggested answer is both. It seems clear that the establishment of Wood Measurement Societies in Sweden can be used as an argument for the claim that cultural and institutional theories of the origins of trust are not mutually excluding but, in fact, highly complimentary. The fact that the two sides, sellers and buyers of timber,

in this case acted as two different parties representing, respectively, the aggregated self-interest of individual forest owners and sawmill owners supports the definition of the sources of trust made by cultural theories. The fact that the sellers united their interests as a response to the creation of a buyer's organization can, just as well, give support to how institutionalist theories define the sources of trust. According to this, trust can be established through a change of the rules, or institutions, that form the incentives facing actors.

4.2 On Cooperation and Trust

This Swedish example also elucidates the advantage of individuals cooperating to promote their self-interest. As Fukuyama (1995) states, a high level of trust will have a reducing effect on transaction costs. It seems clear that the buyers of timber in Sweden could cooperate, in spite of the fact that they were in a competitive situation while pursuing their self-interest.

Even if Swedish buyers of wood, just as Smith's baker mentioned earlier, should be considered to be pursuing their self-interest they somehow overcame the threshold that Hume's farmers could not conquer, namely the misconception that cooperation favouring individual self-interest is impossible. The fact that the transaction costs were reduced (Falk, 1992:79) shows that the establishment of trust had the effect for which the actors strived. The aggregate self-interest of buyers of wood was later confronted with that of the sellers. In the institutionalist theorists' terms, this shows how sellers responded in a rational way to the performance of the buyers in order to bring about a change of the rules of the game. The result was the establishment of trust in the shape of an objective third party that could reduce the uncertainty and vulnerability of the actors.

Finally, what can be said about the division of labor between those involved in the establishment of wood measuring societies in Sweden? The role of the state could, in this case, be described with the following quotation, "The state can effect the net wealth of a community by redefining the structure of property rights, and by providing public goods, such as standardized weights and measures, which reduce the cost of

transacting” (Eggertsson, 1990:247). It only stands to reason to conclude that, if you assume the presented theories of the sources of trust to be accurate, institutional theories can, in this case, find support for their postulate that the level of trust the actors are willing to bestow in a system depends on the adaptability of the system. If people do not approve of the rules they should have the power to change them, or the rules will lose whatever legitimacy they might once have had. In this case the legislative body did respond to the demand from the actors in the forest industry and provided the legal instrument that increased the level of trust between sellers and buyers in order to reduce transaction costs. As was stated before by Hendley *et al.*, (1997), it is especially important for actors within an economy in transition that the rules that give structure to the relationship between actors are widely accepted.

5. CONCLUSION AND RECOMMENDATIONS

Fukuyama’s (1995) assumption that there is a growing adherence to liberal democracy and free markets in the world could prove to be right with regard to the future for Russia as well for other countries of the former Soviet Union. Global cultural unification is not regarded as a prerequisite for this development. But neither should the cultural differences automatically be regarded as obstacles impossible to overcome. Interaction across cultural borders can bring about the economic development of countries, without the eradication of cultural differences. To illustrate this, Fukuyama points to the western world’s influence over Japan that brought about the industrialization of the country. Of course, no one would today claim that the effects of industrialization in these countries have only been welcome blessings. The negative impact on the environment should not be ignored, but most people would say that industrialization has brought prosperity to the countries in question.

The fact that Japan has developed democracy and capitalism within its own cultural norms and rules is, by Fukuyama (1995), taken as a sign of the compatibility between democratic capitalism and a variety of cultural settings. And this, then, should be the strength of democratic capitalism; it promotes economic development if the cultural setting fulfills certain prerequisites. It does so, both in the form of institutions

guaranteed by the political system, such as well-defined property rights, but also informal rules, such as a sense of moral obligation to the society and trust.

5.1 Towards Democratic Capitalism?

To talk about the transition in Russia is to say that the country is going from one specific way of organizing political and economic life to a different system. The question is: towards what system is Russia heading? Can the business behavior observed among the enterprises in the Russian sample of interviews be the based upon which one concludes whether or not Russia is aiming towards the democratic capitalistic ways of the western world of organizing economic activities?

To answer this question one has to pinpoint what the driving forces of the economic system of the present day Russia are, and compare these with the driving forces of an established democratic capitalist economy. Even if one cannot tell for certain what the future will look like in Russia, one might, based on what has been stated earlier, conclude that some of the properties of the former economic and political system of Russia are still very prominent while others have successfully been quenched. One of the latter properties was the total subjugation of individual self-interest. The interviews conducted in Russia and Sweden give evidence of similarities, the driving forces are the same. As was stated in the introduction the respondents in both countries are assumed to be rational and pursuing their self-interest. The fact that the outcome in the Russian forest sector has proved to be far from optimal of the decline in harvests indicates that the actors cannot utilize their rights attained in the new economic system.

The respondents also provide an explanation for the poor economic performance in the sector. It has been made clear that the Russian forest sector is severely affected by the lack of trust between its actors. The problem, as it has been dealt with here, is that if Russia is aiming for a democratic capitalist system, its political sphere ought to guarantee the possibilities for actors to utilize their property rights by providing a functioning way to solve problems with, for instance, violations of business agreements and contracts. This is, as was stated in the introduction, not the place to dwell at any

length upon what property rights system Russia ought to construct in order to better utilize its forest resources, but the following should be noted, property rights are not equivalent to private ownership. Property rights define how people distribute the right to utilize different goods or resource units among themselves (Ostrom, 1996). Private property entails a specific property right, the right of alienation. This property right, the right to sell or to lease, distinguishes private property from other forms of ownership. “Property rights systems that do not contain the right of alienation are to be considered ill-defined” (Ostrom, 1996:8).

No matter how ill- or well-defined property rights are, to utilize their rights as actors people active within the Russian forest industry depend on society’s rule enforcing capabilities. Improving these capabilities is one of the tasks that the political system of Russia ought to deal with in order to prevent private enforcement from becoming part of the solution to the problem of lack of trust between actors. Private rule or law enforcement might, of course, be highly effective, but if Russia is aiming for a democratic capitalist system, the rule enforcement body of society ought to be made accountable in elections.

Returning to the notion of trust explained by cultural and institutional theories as partly a historical residue but partly possible to establish through institutional change, also suggests a responsibility for other actors than the state. To better utilize their right to pursue their self-interests, the actors in the Russian forest sector ought to consider the potential benefits of taking collective action through branch organizations. The example of the founding of Wood Measuring Societies in Sweden can be used as an argument that the actors themselves have to be part of the establishment of trust in the Russian forest sector.

One argument in favor of the involvement of private actors, such as owners of forest enterprises, in the process of establishing trust is the same as the reason for conducting the interviews; it is the actors themselves who can best describe and locate the problems of the sector. Another argument for the involvement of the individual actor in the process of changing the “rules of the game” is, of course, that this is now their privilege.

The transformation of the economic and political system in Russia is providing the individual actor with possibilities and rights that for a long time was denied the Russian people.

It has also been argued here that, for actors in an economy in transition as those in the Russian forest sector, a high level of trust is especially important. An assumed precondition for the establishment of trust being possible in the new democracies is that the character of the former political system has been altered. One property of the old economic system that, by the interviews, has proven still to be surviving is the Russian forest companies' social responsibilities. An adaptation to a market economy does not necessarily include a total separation between forest companies and the communities within which they are active. It should, however, not be the responsibility of forest companies to provide social services, such as medical care, to former employees.

Conclusively, a word or two about the interaction across borders as a way to spread economic prosperity. As was stated earlier, the countries of the western world are not perfect societies that can serve as a blueprint for Russia to copy in detail, but the market economy is here since long established as a way to organize economic life. In the process of further developing the society, Russia ought to make the best possible use of the experiences collected in the west to better utilize its forest resources, not necessarily to be forthcoming towards foreign investors, but to the benefit of the Russian people today and of posterity.

5.2 Further Research

This paper has focused only on a small part of the realities facing the actors in the Russian forest sector, as revealed by those same actors. The conducted interviews contain material that could be used much more extensively than here. This paper has dealt with a general picture of the Russian forest sector. The perspective could, however, be narrowed. The fact that interviews have been conducted in several different regions in Russia allows a search for differences and similarities in business behavior between these regions. By doing so, one might be able to detect regional differences in

the level of trust between actors. Revealed regional differences could supply the empirical foundation for more detailed policy recommendations.

Yet another possible aspect to explore is if experiences of violations of business agreements are more common among newly established enterprises than among older ones. The interviews also contain information about the professional experiences of the leaders of the enterprises. It might be of value to know how differences in education and professional experiences affect business behavior. Such information could also be the base upon which more detailed policy recommendations could be formulated.

Lastly, it could be of value to focus on the accessibility of information. If, as one might suspect, the former political and economic system in Russia were characterized by a total state control of information in society, it would be interesting to analyze the Russian interviews and focus on how private actors access and share information in the new open society. The level of information available to the actor will enhance the probability of avoiding uncertainties that can prove themselves to be costly. By studying this, one might be able to locate traces of the, presumed, old closed network of actors sharing information between themselves, or new emerging networks where the information is shared more openly. To develop the latter would, of course, be the policy recommendation from this study.

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Appendix

Questions used in the interviews with the Russian and Swedish forest sector enterprises.

Interview no.

Interview conducted by:

Date:

Name and address of enterprise:

Respondent:

SECTION A: GENERAL DESCRIPTION OF THE ENTERPRISE

1. Name of the enterprise?

2. What year was the enterprise established?

3. Give a short description of the enterprise.

4. Type of enterprise?

Forest owner/possessor/forest service

Harvesting enterprise

Processing industry

Consultant

Other type, describe

5. What are your main products?

Today:

One year ago:

5 years ago:

10 years ago:

6. What is the actual production volume of the enterprise?

Today:

One year ago:

5 years ago:

10 years ago:

7. Who is the legal owner of this enterprise?

The state, specify:

Private person/persons, namely:

The enterprise is a corporation

owned by other companies, namely:

Other, namely:

8. Number of employees? (Counted as full time personnel)

Workers, today:

Workers, 5 years ago:

Workers, 10 years ago:

Administration, now:

Administration, 5 years ago:
Administration, 10 years ago:

9. Do you have any engagements and responsibilities related to activities other than “production”?

Housing.
Provision of consumer goods:
Schools:
Health care:
Child care:
Other:

10. Do you currently make any investments in your enterprise?

No
Yes, describe content and scale

11. How are your relations to the “banking system” – can you borrow money, from whom and on what terms? Describe:

SECTION B: INPUT SIDE OF THE ENTERPRISE

12. From whom do you acquire timber/wood?

Provider: _____ % of total volume:
Provider 1:
Provider 2:
etc.

13. On what terms is the timber/wood normally acquired?

FOR CONSULTANCY FIRMS:

12 b. From whom do you get your orders/tasks/assignments?

Client: _____ % of total volume:
Client 1:
Client 2:
etc.

13b. On what terms do you get your orders/tasks/assignments? Describe:

14. Do you have any alternative supplier(s)?

Yes
No

15. Can you acquire a sufficient amount?

Yes
No, what is the explanation?

16. How is the timber/wood paid for?

Payment upon delivery:

Payment before delivery:

Other arrangement, namely:

17. How are payments arranged?

Via bank; name of bank:

Payments are done by the enterprise itself:

Other construction, namely:

18. What will happen if either part breaks the agreement or does not fulfil its duties?

19. Do you regard violations of agreements as a problem?

Yes, a big problem

Yes, but a small problem

Not really a problem

20. Describe how a typical purchase transaction is performed.

SECTION C: OUTPUT SIDE OF THE ENTERPRISE

21. To whom do you sell your 'products'? Name and type of customers in order of importance (as a percentage of total volume), name all.

Customer: _____ % of total volume:

Customer 1:

Type:

Customer 2:

Type:

etc.

22. Can you describe how a typical sales transaction is performed?

23. What will happen if either part breaks the agreement or does not fulfil its duties?

Describe

24. Do you regard violations of agreements as a problem?

Yes, a big problem

Yes, but a small problem

Not really a problem

25. How do you get paid for your products?

Cash or equivalent upon delivery

Cash or equivalent paid before delivery

Other arrangement, namely:

26. How are payments arranged?

Via bank; name of this bank:

Payments are done by the enterprise itself

Other construction, namely:

SECTION D: INSTITUTIONAL ASPECTS

27. Is this enterprise member of any branch organization or equivalent?

No

Yes, namely:

What are the arguments for this construction?

28. Are there rules or regulations that apply to your enterprise which you regard as an obstacle for your activities?

No

Yes, describe:

29. Are there other problems which you regard as obstacles for a successful business?

Describe

No, only minor:

machinery/technology:

equipment/supply/maintenance:

personnel/skill/competence:

other:

30. What is the single most binding “restriction” on the activity of your enterprise? Describe.

31. Generally speaking, do you find the formal legislation regulating Russian/Swedish forest enterprises adequate and efficient?

Yes

No, explain why.

32. If it would be possible to change anything related to the Russian/Swedish forest sector, what would you change?

33. Other comments of relevance?