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Export of Timber from Slovakia to China

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Declaration:

I hereby declare that I am the sole author of the thesis entitled “Export of Timber from Slovakia to China“. I duly marked out all quotations. The used literature and sources are stated in the attached list of references.

In Prague on

Lukáš Benda

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List of Abbreviations:

CCPIT - China Council for the Promotion of International Trade

CPI – Consumer Price Index

CSKC - Czech – Slovak – Chinese Chamber

EAD – Export Accompanying Document

ECB – European Central Bank

EUR – Euro

FSC – Forest Stewardship Council

FMPRC – Ministry of Foreign Affairs of the People’s Republic of China

GDP – Gross domestic product

GFW – Global Forest Watch

HS – Harmonized System

ICC - Institute of London Underwriters

MFN – Most Favoured Nation

MOFCOM – Ministry of Commerce People’s Republic of China

NBSC - National Bureau of Statistics of China

NFC – National Forest Centre

PTA – Preferential Trade Arrangements

RMB - Renminbi

RTA – Regional Trade Agreement

SARIO – Slovak Investment and Trade Development Agency

SCJBC – Slovak-Chinese business council

SFA – The State Forestry Administration (China)

SOPK – Slovak Chamber of Commerce

USD – U.S. Dollar

WFOE – Wholly Foreign Owned Enterprise

WTO – World Trade Organization

Introduction:

Continuous strengthening of globalisation undoubtedly carries many new opportunities for international trade and business. The overall trend of globalisation decreases the barriers between countries which causes easing of trade regulations, and thus increases exponentially the pace and level of trade of goods and the flow of capital between countries. Although historically international trade was conducted to act as a source of goods which were scarce to specific geographical areas, nowadays it is used, in many cases, as an instrument to increase profitability of a firm. Decrease in transportation costs happened to cause countries to specialize in production according to classical economic theories, where countries focus on production of goods for which they have the lower cost. Given this upper hand, they then trade it. The biggest boom in international trade was seen during the 19th century, with exception of the war periods, and was caused by technological developments in transportation.

During the past couple of decades trade expanded from traditional; bordering or close bordering countries, to trade with partners from across the ocean. One of the greatest expansions on the international market in the last couple of decades can be seen in Asian countries, such as China. This country has been in trade surplus consecutively for many years, meaning that the country exports more goods than it imports. Taken into consideration the late Chinese trend of purchasing raw material from all over the world, I became to wonder if one cannot export wood into China from Slovakia, as not only the current market with timber in Slovakia, but the whole European market of timber is overheated for many years. The issue with prices of wood started with countries joining the European Union, which resulted in free-trade zone with no customs.

This work is therefore further focus on potential export of Slovak wood to China, as I see a potential to fill the market in China by Slovakian timber. This Bachelor thesis will namely focus on description of the markets of the previously mentioned countries and factors determining the mode of entry to the market. Furthermore, detailed description of several options of market penetration will be discussed and practical application of the researched information and recommendation to Lesprodukt s.r.o., a wood logging company operating in Slovak market since 2008.

The research question of this work is therefore, to what extent is it viable for Lesprodukt to export timber from Slovakia to China, and what is the most suitable way of conducting international trade with China for company of such a size. Given the assumptions, that the company is aware of basic risks in international business, and assuming that both countries are politically stable. However, the practical application will be not only for Lesprodukt, but for all companies seeking conducting such operation in any raw material exportation.

Methodology of this research will be primarily by using and investigating secondary sources, such as governmental organization supporting trade, statistical reports of the two economies, and reports from other relevant world organizations (WTO, OECD, OEC, UN, and others). Further, as a primary source an interview, conducted by the researcher, with the director of Lesprodukt is going to be used. These sources are going to be used to support the research question in order to: assess whether Slovakia is a potential long-term partner for business with China; and to discover whether there is a spare capacity in China for timber.

First two chapters will be focused on description of the global market of the countries, their international trade policies, outline of specific regulations for export and import, and most importantly regulations by China and Slovak Republic for timber logging in case of the exporting countries. Furthermore, target will be placed on the situation on the wood market; prices of the wood and specifics of the markets. In the second chapter, Chinese market will be investigated in a similar way, however focus will be placed on investigation of the import quotas limitations, and outline the system of Chinese customs for wood market.

Process of exporting wood into China will be the main topic of the third chapter, where description of several ways of penetration to the market will be mentioned but the main target will be placed on partnership and setting up our own branch in China. In this case, theoretical process of creating a new company from scratch will be discussed. Further, in the third chapter, contractual, logistics, pricing, and brief recommendations on how to negotiate on the Chinese market will be described. However, the aim of this work is not to deeply describe the cultural dimensions and differences, but to create a summary of differences which I believe are the most important for understanding the Chinese culture, and by this try to avoid possible cultural clashes when it comes to negotiations.

Fourth, being the final chapter of this thesis, will be the summary of the research conducted and recommendations to the company Lesprodukt s.r.o, on how to penetrate to the Chinese market, will be given. Brief description of the process, which I believe, is going to be the best choice for them, and practical evaluation of the opportunities will be given. However, risks in the international business will not be specifically investigated, as they are depended on many different factors, and can be partially avoided through choosing the right contractual conditions, which will be mentioned. Risks will be mentioned in related topics, and few most important factors on tackling some of them will be covered.

Aim of this work is therefore to outline the global market in People's Republic of China and Slovak Republic; in order to gain insight into the economic situation of the countries, and further to place focus on timber market in the countries; to outline the process of exporting wood into China with focus on specifics and regulations; and most importantly to give recommendations to Lesprodukt s.r.o., a company suggestive to conducting international business operation with China on the most appropriate way of penetration and an investigation on whether there is an opportunity for such a company on the market.

1. Market of Slovak Republic

The aim of this Chapter is to provide information about the current situation on Slovak market as a whole, with focus on economic indicators connected to the specific market. Furthermore, focus on basic description of wood market to understand the basic concepts and processes will be given. Prices and current trends of the market will be described in more detail later in this chapter. Key international organizations promoting trade relations with China will be briefly described.

1.1 Overview of Slovak Market

Slovak Republic is a European mid-size country geographically located in the hearth of Europe, bordering important trade partners: Czech Republic, Austria, Poland, Ukraine, and Hungary. The country itself was established on 1st January 1993 after the dissolution of Czechoslovakia, and has a population around 5.44 million as of 30. September 2017.¹ Which makes it one of the smaller markets in Europe in terms of capita. As international trade is conducted between China and Slovakia, there is a need to describe conditions not only of China in terms of economy, but also for Slovakia in order to provide an overview for Chinese investors as stability of partner in business is essential for long-term ongoing relationship.

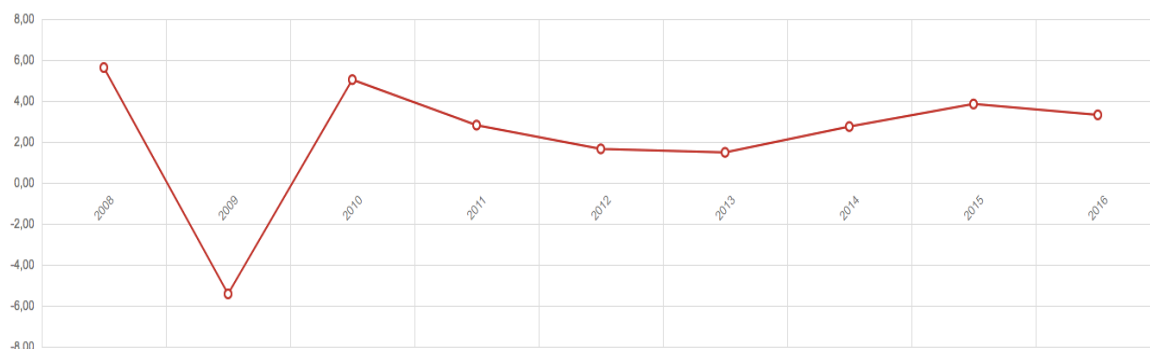
1.1.1 Gross Domestic Product

In terms of gross domestic product, the GDP of the country follows an overall growing trend since 2009, see Graph 1 on the next page, and the latest available data for 2016 shows that GDP was EUR 81.1 billion. Graph 1 shows that in period of last 3 years, the average growth is kept around 3.3%, which also corresponds to the predictions of World Bank in next couple of years, thus the economy has a stable growth and can prosper in the future.²

¹Štatistický úrad Slovenskej republiky, “*Stav obyvateľstva v SR k 30. septembru 2017*“, [accessed online on 05.01.2018 at: <https://slovak.statistics.sk/>]

²Národná banka Slovenska, “*Makroekonomická databáza*“, [accessed online on 05.01.2018 at: www.nbs.sk/sk/menova-politika/makroekonomicka-databaza]

Graph 1: GDP growth of Slovakia (2008-2016)



Source: Národná banka Slovenska, www.nbs.sk

Graph 1, further shows a fairly stable GDP growth, which provides Chinese partners with a solid prove about the performance of the economy, and a conclusion that further growth of the economy, in case no unexpected events would occur, can be made.

1.1.2 Unemployment Rate

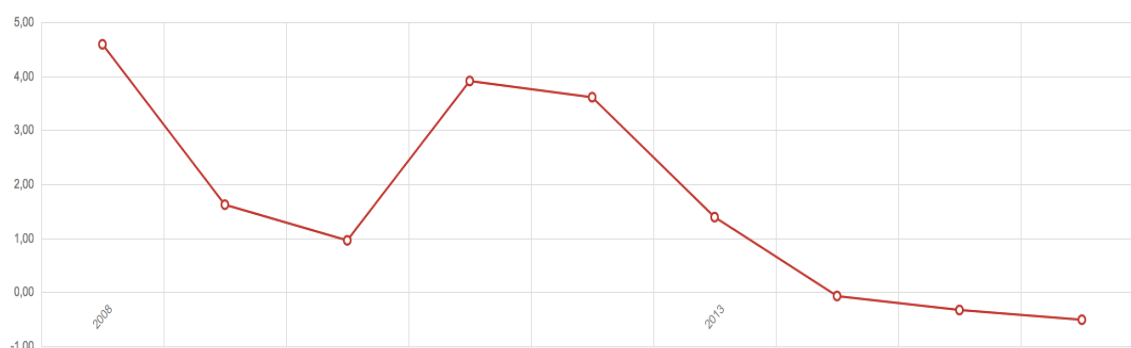
Mentioning unemployment rate is crucial for evaluation of the country's potential and performance. Even though Slovakia suffers from a high level of unemployment which has decreased in November 2017 to level of 5.95%, there was an impressive decrease from 7.5% in August 2017, and decrease from annual reported unemployment rate of 9.7% in 2016.³ This can be perceived as an indicator of improving situation on the Slovak market. The indication of an improving market is important for assessing the risk while considering a trade partnership with a company from another country.

³Ústradie práce, sociálnych vecí a rodiny, "MESAČNÁ ŠTATISTIKA o počte a štruktúre uchádzačov o zamestnanie za mesiac November 2017", [accessed online on 05.01.2018 at: <http://www.upsvar.sk/>]

1.1.3 Inflation Rate

Investigating economic situation of a country, consideration of the inflation rate is necessary, to be able to have a rough foresight of the possible price level changes of the goods exported / imported. As when the inflation rises, according to classical economists, wage, cost of production, and transportation cost increases accordingly, therefore it will affect the price in the short-run. Looking at Graph 2, major differences in inflation rate is seen, that is measured by “CPI index of all goods without seasonality”, as specified on website of Slovak National Bank.⁴

Graph 2: Inflation in Slovakia during (2010-2016)



Source: Národná banka Slovenska, www.nbs.sk

CPI measures the prices of selected basket on the market. Red dots on the graph represent years accordingly, starting from 2008 ending 2016. The major increase for year 2010, might be caused by the acceptance of euro as a national currency in Slovakia on 1st January 2009. The inflation shock could have been postponed by the difficulties of accepting new currency. On the other hand, inflation levels after 2012, follow a massive decrease from 3.61% to 1.39% in 2013. This decreasing trend continues until 2016, when there was deflation of 0.51%. Interestingly, when the country's currency is appreciating, one would expect the domestic investors to withhold their investments into the company, which further decreases the deflation, as consumers and investors are expecting the prices to drop even further. This phenomenon is explained by IS-LM model.⁵

⁴ Národná banka Slovenska, “*Makroekonomická databáza*“, [accessed online on 05.01.2018 at: www.nbs.sk/sk/menova-politika/makroekonomicka-databaza]

⁵ Mankiw, N. G., “*Principles of macroeconomics*“, Sixth. Mason: South-Western Cengage Learning, 2012. ISBN 0538453060;9780538453066

However, partial lack, or only a slight effect, of this phenomenon may be once again explained by the acceptance of euro in 2009, which came together with allowance of ECB (European Central Bank) to regulate largely the monetary and fiscal policies of the country. Slovak Republic entered European Union in 2004, which created a free-trade and no custom zone for the goods, and therefore acceptance of euro as a currency further eased obstacles in trade, this boosted imports and mainly exports of the country.⁶

1.1.4 International Trade

Following the previous paragraph, international trade of the country is another factor which needs to be considered when looking at the overall situation of the economy.

In 2016 Slovakia exported goods in total value of EUR 79.1 billion⁷, and the distribution by segments were made out of: 33% Machinery (video displays, broadcasting technology), 29% Transportation (cars, vehicle parts) 9.4% of metals (hot-rolled iron, coated hot-rolled iron), and only 1.1% of wood, and wood products were exported.⁸ Trends of the timber market will be discussed further in the work, in subchapter 1.2. Slovakia mostly exports to Germany, Czech Republic, and Poland. These three export partners make up around 41.2% of the total export.

Imports of goods and services into Slovakia were conducted in 2016 for total of EUR 73.5 billion⁹. This shows that Slovak Republic has a positive net trade of EUR 5.6 billion. The economy has a positive trade balance since first quarter 2015 when exports exceeded, for the first time after 1995, imports of the country. The biggest import category is machines with, same percentage as for export, comprising of 33% of the incoming goods. As the country has many car production factories, there is no surprise that vehicle parts make up to 11% of the imported goods, out of the 16% in transportation category. Third and fourth biggest categories of imported goods are metals and minerals products, namely then crude petroleum and petroleum gas.

⁷Národná banka Slovenska, “*Makroekonomická databáza*“, [accessed online on 05.01.2018 at: www.nbs.sk/sk/menova-politika/makroekonomicka-databaza]

⁸ *OECD - Slovakia (SVK)*, “*Exports, Imports, and Trade Partners*“, Observatory of Economic Complexity, [accessed online on 05.01.2018 at: atlas.media.mit.edu/en/profile/country/svk/]

⁹Národná banka Slovenska, “*Makroekonomická databáza*“, [accessed online on 05.01.2018 at: www.nbs.sk/sk/menova-politika/makroekonomicka-databaza]

1.1.5 Organizations Promoting International Trade with China

China and Slovakia has governmental institutions that aim to help with entering new markets, and are run by professionals from each segment of the market, who are willing to co-operate and advise on entering to a new market. For Slovakia, there is SARIO (Slovak Investment and Trade Development Agency) which focuses on supporting Slovakian entrepreneurs while expanding to new markets. On websites of SARIO, you can find all the basic information connected to export from Slovakia into different regions, these specifics will be discussed later on.¹⁰

Another state organization for supporting business relations with China is SCJBC (Slovensko-Čínská podnikateľská rada), which operates under the Slovak Chamber of Commerce since 2013. The main goal of SCJBC is to support Slovak exporters into expanding to China, and to help Chinese investors with investments on Slovak market.¹¹

However, also non-governmental organization such as CSMC (Czech – Slovak – Chinese Chamber) exists to support local Czech and Slovak businessman and aims to connect parties from these regions in order to help them in establishment of fundamental relations for conducting future transactions. CSMC consist of more than thirteen professionals who have great experience with conducting business in China, among others Ing. Libor Táborský, a director of Chinese branch of PPF Investments is one of the board members of the organization.¹²

1.2 Timber Market and Export

This subchapter focuses on explanation of wood market, effect of different categories of the commodity on price, what is the current market with wood in Slovakia and its trends, and last but not least on the export regulations of timber.

¹⁰ Slovenská agentúra pre rozvoj investícií a obchodu, “*Exportujte do zahraničia*“, [accessed online on 5.01.2018 at: www.sario.sk]

¹¹ Slovensko-Čínská podnikateľská rada [accessed online on 05.01.2018 at: www.scjbc.eu]

¹² Czech-Slovak-Chinese Chamber, [accessed online on 06.01.2018 at: www.czc.eu]

1.2.1 Timber Market Introduction

Wood market is a market with commodity specific in long taking reoccurrence of the logging process, this is why the importance of long-term stability and sustainability is the key of the business. There are many false beliefs that private owners tend to log as much wood as possible, due to their greed for profit. These accusations are in majority false, as the essential part of the business is sustainability of forest, as the land has only minor part on the value.

Description of what economy of forestry management, according to Mr. Kupčák, is that it is expansion of forest done by people in order to economically benefit from managing it with main aim of the process being production of wood for sale.¹³ However, as mentioned earlier, to maintain logging as a stable business, and therefore income of profit, need to sustain the forest at its natural level is necessary. As Moravčík, Konopka et al. propose almost half of the wood processed comes from damaged or rotting trees. This shows us the importance of appropriate management. Talking about the sustainability of the forest five principles of long term development must be provided.

- 1) *Principle of sustainable development* – focuses on tendency to maintain all the characteristics and principles of forest, and secure continuous expansion of forest
- 2) *Principle of optimal production and of non-production functions of forest*
- 3) *Principle of stability* – explains the need to help the maintain the forest healthy
- 4) *Principle of ecology* – pays focus on maintaining the eco system of the forest
- 5) *Principle of forest management*¹⁴

These principles need to be maintained in order to sustain a long-lasting business in forestry, and logging. Principles described above do not focus only on logging of wood, but also on the ecosystem in the forests. It is important to keep in mind that forestry business must be conducted with ethics and morals and not to forget that it is a home to many different species. This is also why the latest strategies concerning logging and forestry focuses more on the protection of environment, than on the profit making.

¹³ Kupčák V., „*Ekonomika lesního hospodářství*“, 2. vyd. Brno: Mendelova zemědělská a lesnická univerzita v Brně, 2006. ISBN 80-7157-998-X..

¹⁴ Moravčík M., Konopka J. et al., „*Strategy of forestry development in Slovakia*“ Lesn. Čas. – Forestry Journal, 55(1): 65 – 84, 2009, ref. 7. Discussion paper. ISSN 0323–10468

At the beginning of 2017, there was an interesting medial clash between public and government, when according to GFW (Global Forest Watch), forests decreased in volume by 6% between 2001 and 2014. However governmental organizations, being NFC (National Forest Centre) and Forestry Chamber, argued that this research is based on satellite pictures, which does not include up-to-date information and most importantly newly plant trees cannot be seen on these pictures.¹⁵

Contradict to GFW, the NFC reported that in last ten years, the area of forests increased by 0.46% and the available wood resources increased by 14.7%.¹⁶ These media campaigns might be effecting the timber market in Slovakia in year 2017 and further, as there is a pressure from public on logging companies, however at this moment, most recent data available are for year 2016.

1.2.2 Overview of the Timber Market

When evaluating or reviewing the market, the need of data provided from trustworthy sources is necessary. Data provided in this work are obtained from Slovak governmental organization only, to exclude any potential misunderstandings, due to different criteria for data obtaining. Slovakia is 10th most forested county of the European Union, with approximately 41% of the overall land covered with forest. Since 1950s lands covered by forest increased by 10% to current 2 million hectares.¹⁷

Table: 1 : Logging and Deliveries in Slovka (2009-2016)

in thousands m ³	2009	2010	2011	2012	2013	2014	2015	2016
Logging of coniferous wood	6 183	6 235	5 512	4 592	4 132	5 269	4 811	5 144
Logging of non-coniferous" wood	3 065	3 625	3 955	3 640	3 705	4 149	4 332	4 177
Sum of logged wood	9 248	9 860	9 467	8 232	7 837	9 417	9 143	9 321
Deliveries of coniferous wood	6 276	6 383	5 449	4 427	4 053	5 149	4 662	5 194
Deliveries of non-coniferous wood	2 811	3 216	3 764	3 775	4 010	4 019	4 332	4 073
Sum of deliveries	9 087	9 599	9 213	8 202	8 063	9 168	8 995	9 267

Source: Author's interpretation of data obtained from Slovenský Štatistický Úrad

¹⁵ Hančinský D., „Nepravdivé informácie o úbytku lesov na Slovensku“, Slovenská Lesnícká Komora [accessed online on 06.01.2018 at: www.slsk.sk]

¹⁶ Tiskova agentura Slovenské Republiky, „ANALÝZA: Lesov na Slovensku podľa satelitných záberov ubúda.“ TERAZ.sk, 10 Jan 2017, [accessed online on 06.01.2018 at: www.teraz.sk/ekonomika/iep-lesov-na-slovensku-statistika/237437-clanok.html.]

¹⁷ Slovenská agentura pre rozvoj investícií a obchodu, 2012 „Lesy a Drevospracujúci Priemysel“, [accessed online at 06.01.2018 on: <http://www.sario.sk/>]

As per data provided in Table 1, total of logged wood and deliveries with division to two basic categories of wood can be seen. Logging represents the raw real outcome of the logging process and deliveries represent the actual amount of wood ready for further processing in any form. Government organizations logged 52.4% of the processed amount, and private organizations were responsible for the remaining 47.6% of the timber in year 2016.

The division of these categories as for their sector in biodiversity of the Slovak forest is around 38.6% for coniferous wood and 61.4% for non-coniferous wood. Assumption that supply of non-coniferous trees to the market will be stronger may be made, however due to the possible use and the price of non-coniferous wood, there is a larger supply of coniferous wood to the market.¹⁸

Interesting point to make is that the amount of logged wood during years which were highly affected by the World's financial crisis, after the collapse of US financial market in 2008, no remarkable differences in cubic meters logged in years 2009 and 2010 can be seen. Further on, difference in market price levels are to be discussed. This might be also caused by the long taking time before wood perishes, and specifics of the market, as for example in construction businesses there is a demand for dried wood, this process can take up to a year. Another possible explanation may be the calamity logging which will be explained further in this chapter.

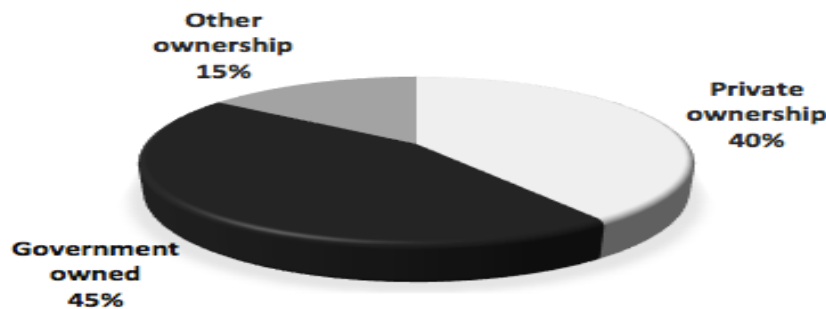
For year 2016, the overall natural recovery of forests made up 7,133 ha, and the recovery done by people through forestry management plans equalled to 10,972 ha of newly planted forest. Total amount of recovered forest is 4% higher than in 2015. Increasing trend in forest recovery since year 2014, when the forest was damaged by a natural disaster in form of gale "Alžbeta" and "Žofie", can be observed.¹⁹

¹⁸ Národná sústava povolaní, "*Sektorová rada lesné hospodárstvo a drevospracujúci priemysel*", [accessed online at 6.01.2018 on: https://www.sustavapovolani.sk/sektorova_rada-9]

¹⁹ Ministerstvo Pôdohospodárstva a rozvoja vidieka Slovenskej Republiky, „Správa o lesnom hospodárstve v Slovenskej Republike za rok 2016“, Národné lesnícke centrum, Bratislava 2017

Financial results of timber market in Slovakia for year 2016 slightly decreased from preceding year and the revenue in timber industry was EUR 433.15 million, and the gross profit reached in the industry resulted in EUR 44.76 million.²⁰ As in 2015 the gross profit for the period was EUR 44.80 million. The decline of the gross profit as shown on Table 1, is caused not due to reduction of logging or the number of transactions, however it is caused by collapsing price levels which are occurring since 2012.

Chart 1: Structural ownership of forest in Slovakia (2013)



Source: Author's interpretation of data obtained from Národná sústava povolaní www.sustavapovolani.sk

If we take a look at the structure of the ownership, we must specify categories on Chart 1, in order to fully understand the division of ownership. “Private ownership” comprises of companies and physical subjects, but also of ecclesiastic, agricultural cooperatives and general cooperatives. On the other hand, “Other ownership” is composed of private owners who gave the right to dispose of the property to governmental organizations.

Numbers shown on Chart 1 are rounded up as a percentage of the total area, which makes exactly 2,013,419 ha for year 2013 (latest official data).²¹ The proportions of logging conducted by governmental and private organizations, fact that private ownership obtains proportionally more timber for their area can be seen.

To fully understand the basics of the timber market we need to address the issue with so called “Calamity logging” which stand for wood from fallen trees due to environmental causes and for other issues caused by them, for example due to underground insects brought

²⁰Národná banka Slovenska, *Makroekonomická databáza*, [accessed online on 5.01.2018 at: www.nbs.sk/sk/menova-politika/makroekonomicka-databaza]

²¹Slovenský Štatistický Úrad, *Výmera pôdy, prírastky a úbytky pôdy*, [accessed online at 6.01.2018 on: www.datacube.statistics.sk]

to the trees as a result of strong wind. The proportion of calamity logging makes around 42 – 65% of all the logging in Slovakia.²² In year 2005, the amount of calamity logging caused the forest management plan to exceed by 50%, and in year 2010 by 25%. Logging occurring due to natural causes makes the process of forest management difficult, as there is no possibility of predicting the climate conditions.

Important issue related to timber market, not only in Slovakia, but globally. The issue being an illegal logging of wood, which is said to cover 10 to 30% of all supplied wood on the market. Issue with stealing wood is that it can never be accurately estimated, due to the nature of the logging business.

1.2.3 Regulations and Grading Categories

Wood is traded and sold on the market according to many factors separating the categories. There are few categories of timber divided according to the use, and there is a further division based on the quality category of the wood. Transactions on the market are mostly conducted in a pulp wood (timber which is usually damaged or rotten, that is not fit for further processing), which is used mostly in paper industry, and in wood of III. category (lumber).

These categories are described by in national system STN 48 0055 from 1. 4. 2007, by European norms EN, and by norms still valid from time of Czechoslovakia.

Norms of the wood described by European Union with identification of EN are further division of STN categories according to quality of the specific timber. This classification of quality is similar to food quality divided into A, B, C, D.²³ These depends on the weight, shape, health, appearance and size of the wood. I believe there is no requirement for further explanation of these quality categories, in order to gain a basic insight into the market.

²² Tiskova agentura Slovenské Republiky, „Z lesov miznú miliózn kubíkov dreva ročne. Za posledné desaťročia sa plánovaná ťažba takmer zdvojnásobila“, FinWeb 17.07.2017 [accessed online at 6.01.2018 at: <https://finweb.hnonline.sk/ekonomika/996731-z-lesov-miznu-miliony-kubikov-dreva-rocne-za-posledne-desatrocia-sa-planovana-tazba-takmer-zdvojnasoila>]

²³ Greppel E., Paluž H. et al., „*Zhodnotenie drevnej hmoty a marketingové riadenie 2009*, Národné lesnícké centrum, Zvolen 2009, ISBN 978-80-8093-094-3

Here is a summary of STN categories, which serve as a basic division:

- I. Category – used for musical instruments and technical instruments
- II. Category –used for fire matches, and special lumber
- III. Category – round logs for lumber
- IV. Category – timber used for production of pillars, blanks, and sticks
- V. Category – pulp wood
- VI. Category – used for energy production²⁴

European Union stated in 2011 that it aims to create a common forest management and regulations plan for forestry industry by 2020.²⁵ At current moment forestry management is proposed by the specialist in forestry management who is appointed by the owner of the forest, and further reviewed and accepted or declined by the Ministry of Environment. This plan is called “LHP (Lesný Hopodársky Plán)“, which can be translated as Forest management plan. These plans are specific according to the age and bonity structure of each specific area. Additional to a planned logging, country expects, as described earlier, around 40-50% of wood extracted from the forest to be due to calamity logging.²⁶

²⁴ Greppel E., Paluš H. et al., „*Kvalita dreva a obchod s drevom*“, Národné lesnícké centrum, Zvolen 2007, ISBN 978-80-8093-028-8

²⁵ European Commission, KOM (2011) 244, [accessed online on 8.01.2018 at: [http://www.europarl.europa.eu/RegData/docs_autres_institutions/commission_europeenne/com/2011/0244/COM_COM\(2011\)0244_CS.pdf](http://www.europarl.europa.eu/RegData/docs_autres_institutions/commission_europeenne/com/2011/0244/COM_COM(2011)0244_CS.pdf)]

²⁶ Interview with Ing. Dušan Vatraľ, director of Lesprodukt s.r.o. [conducted on 18.12.2017]

1.2.4 Role of the European Union

European Union set its goals and priorities for horizon of next few years in Directive 2009/28/EC which shows large trend of shifting our sources of energy from traditional sources such as coal and nuclear power to renewable energy. EU aims to achieve percentage of energy coming from renewable sources up to 20% by 2020, and further increase to 27% in 2030.²⁷

These targets, set by the EU, are supported by incentives to governments and business subjects, which aims to increase the production of biomass and establishing power plants based on biomass. These trends might have an effect on the diversity on the market and where the future of the market is heading, as with the incentives from European Union, it might be better to start planting fast growing trees, such as different species of bamboo, in order to gain profit, rather than planting traditional trees. As Ing. Dušan Vatraľ suggested, these trends are arising in his region.²⁸

European Union further established funds which aims to provide supports to recover forests damaged by environmental disasters, in order to increase the diversity of the eco systems, and to support forest industry as such. Some of these supports are either delegated by national governments and have strict requirements for obtain them, or by EU programmes such as LIFE+.²⁹

²⁷ Ragonnaud G., *The European Union and Forests*, European Parliament, June 2016[accessed online on 08.01.2018 at: http://www.europarl.europa.eu/RegData/etudes/fiches_techniques/]

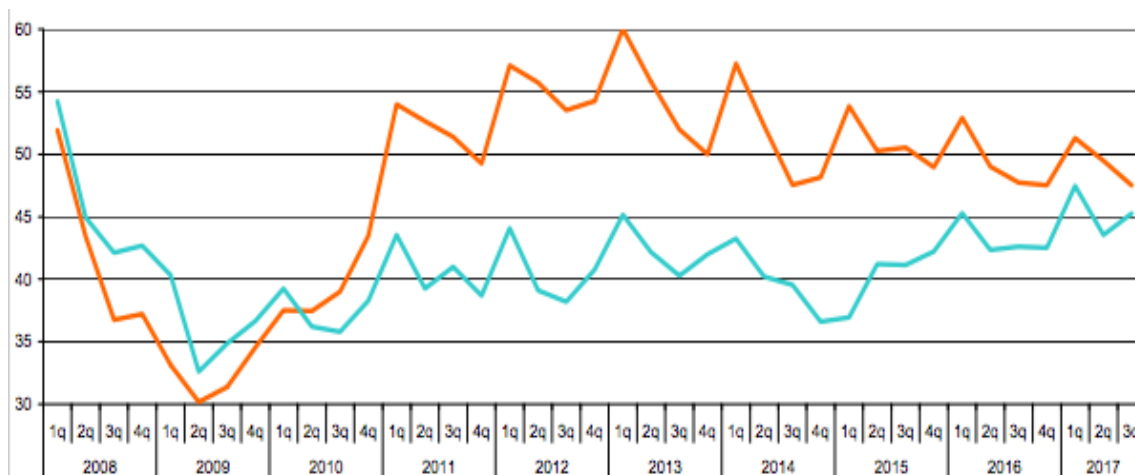
²⁸ Interview with Ing. Dušan Vatraľ, director of Lesprodukt s.r.o. [conducted on 18.12.2017]

²⁹ Ministerstvo pôdohospodárstva a rozvoja vidieka SR, accessed online on 08.01.2018 at: www.mpsr.sk

1.2.5 Prices and Export of Timber

Subject of price levels and export are intentionally kept together, even though they might seem distant from each other. The sensitive issue with price levels on Slovakian market is discussed by businesses in the domestic timber industry. This attention is caused by the continuous collapse of the average price level per 1 m³ since the beginning of 2013.³⁰ Trends of the wood market prices are shown on Graph 3.

Graph 3: Average prices of timber from non-governmental organizations on domestic market (2009 – 3Q 2017)



Source: Spravodajca Národného Lesníckého Centra, www.nlcsk.sk

Looking at Graph 3, decreasing trend of price levels on timber market can be observed. Orange line represents coniferous wood, and blue line represent non-coniferous wood. The rapid decrease of price levels observed in 2008 was due to the world financial crisis in 2008 that was initially caused by the US subprime mortgage crisis.

The current prices of wood are in on average for coniferous and non-coniferous wood in range of EUR 45-48/m³. Specific prices on domestic and export market, for each timber category and quality differs significantly, and even further prices on domestic and foreign markets can be said to be incomparable, as on domestic market they are significantly lower.

³⁰ Ministerstvo Pôdohospodárstva a rozvoja vidieka Slovenskej Republiky, „Správa o lesnom hospodárstve v Slovenskej Republike za rok 2016“, Národné lesnícké centrum, Bratislava 2017

As per Table 2 provided above, the largest export partner of Slovakia was Czech Republic. Important note to rise is that Trade Value stands does not stand for the profit conducted from the international business, however it stands for the overall amount of the transaction. Summing up the numbers of top 7 exports of Slovakia value representing 28% of the total revenue from Slovak Republic will be shown. Data obtained from UN Comtrade Database shows that Slovakia exports wood in total of 5.7 million cubic meters to top 7 partners, and imports 1.6m cubic meters from their top import partners.³¹

Table 2: Export trade partners for Slovakia (2016)

Fx. 0.940	Trade Value (USD)	Trade Value (EUR)	Quantity (m³)	Average trade value (EUR)
Czech Republic	55 261 476	51 945 787	3 063 176	16,96
Austria	34 872 194	32 779 862	1 554 176	21,09
Poland	26 266 757	24 690 752	890 239	27,73
Hungary	5 798 187	5 450 296	143 440	38,00
China	3 715 885	3 492 932	20 435	170,93
Romania	3 439 092	3 232 746	34 458	93,82
Germany	1 926 060	1 810 496	17 623	102,73

Source: Author's interpretation of data obtained from Un Comtrade Databse, www.comtrade.un.org

Price level differences between domestic and average export market prices shows a major difference. The biggest difference can be seen on coniferous wood of I. category, when domestic price in 2016 was EUR 62.25/m³ and EUR 202.22/m³, and on non-coniferous wood of I. category when price level on domestic market is EUR 265.93/m³ and average price on export market is EUR 365.70/m³.

³¹ UN Comtrade Database [accessed online on 9.01.2018 at: www.comtrade.un.org]

2. Market of People's Republic of China

Main economic factors related to the global Chinese market, and specifically timber market is covered within this chapter. Further, brief overview of the country's history and its current role in international trade will be covered. State organizations promoting and related to foreign trade will also mentioned, however their role will be covered later in the work. Trend on timber markets and important news are going to be discussed so as trade limitations for conducting business with wood.

2.1 Overview of Chinese Market

People's Republic of China is the 3rd biggest country in terms of area, and the second largest consumers market in the world in terms of value of consumption. China is the largest East Asian country with estimated population of 1.38 billion as of July 2017.³² China is a country often connected to many discussable topics, rules, laws, and regulations. In this economical overview of the country, focus will be placed on the most important indicators of the current expanding economy. China has been improving its international position since 1970's when its economy went through transition from closed economy into more open-market economy, which resulted in creating a solid position of the biggest exporter in the world since then. Currently China is the biggest holder of currency reserves in the world. Last thing to mention about Chinese economy and conducting business in China is that it can be very misleading, confusing, and not easy to establish a business in China due to its many regulations and specific laws to different areas.

2.1.1 Gross Domestic Product

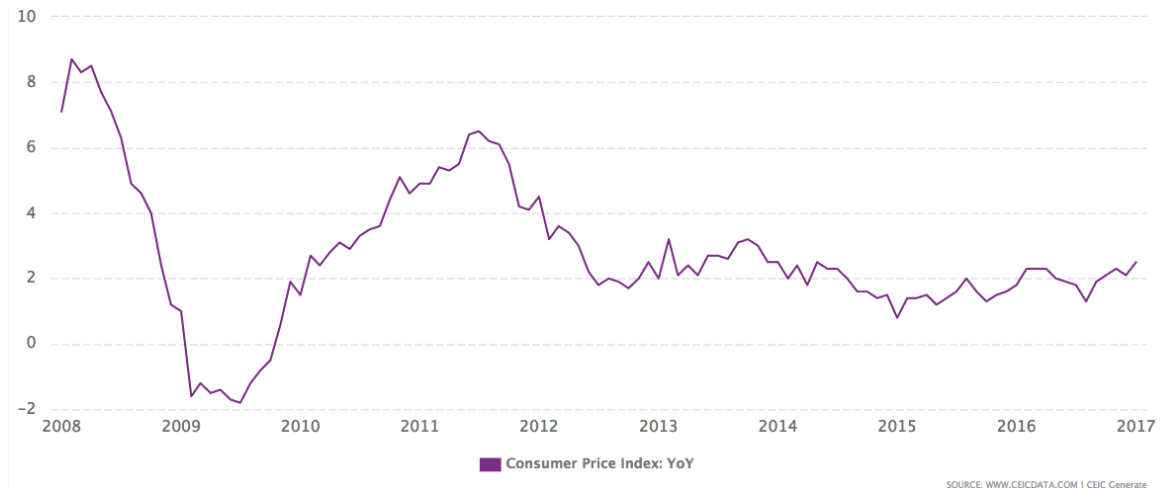
China has been showing incredible growth in GDP since 1970's when the market was liberalised and opened to other international trade. Since then Chinese GDP grew on average around 10% annually, due to this many consider economy of China as one of the most successful economies in the world, even though it currently faces many problems which might affect the future GDP growth.³³

³² Central Intelligence Agency, The World Factbook China [accessed online at 8.01.2018 on: <https://www.cia.gov/library/publications/the-world-factbook/geos/ch.html>]

³³ Wayne M. Morrison, *China's Economic Rise: History, Trends, Challenges, and Implications of the United States*, Congressional Research Service, [accessed online at 09.01.2018 on: <https://fas.org/sgp/crs/row/RL33534.pdf>]

The total gross domestic product for year 2016 was USD 11.2 trillion, which put it right behind the world largest economy of USA with USD 18.6 trillion.³⁴

Graph 4: GDP Growth in China (2008-2017)



Source: Ministry of Human Resources and Social Security, www.ceicdata.com

Graph 4, shows the GDP growth in China over the period of last nine years. The GDP has been growing in the last five years in a range between 1-3%, which is considered as a healthy pace of growth. As for 2017, the GDP has been at about 2.5%, thus indicating a well developing economy with stable growth. Firms should find this economy therefore stable for conducting international business from this point of view.

Chinese GDP PPP per capita scored at 70th place (USD 15,535) out of 175 countries, while Slovakia scored at 34th place (USD 30,632). From this indicator, the huge social situation differences in the countries may be observed, as the GDP PPP per capita in Slovakia is almost double the Chinese one, even though sizes of the markets are incomparable.³⁵ This economic indicator provides us with a basic presumption of high poverty level in China. GDP PPP is calculated as sum of all goods and services produced in the country divided by population. This indicator is based on purchasing power parity which is the ration between exchange rates, GDP PPP takes into consideration then the price differences on markets. However, the indicator is largely affected by fluctuation of exchange rates.³⁶

³⁴ World Bank, *Gross domestic product 2016*, [accessed online at 9.01.2018 on: <http://databank.worldbank.org/data/download/GDP.pdf>]

³⁵ Ibid

³⁶ Mankiw, N. G. *Principles of macroeconomics*. Sixth. Mason: South-Western Cengage Learning, 2012. ISBN 0538453060;9780538453066.

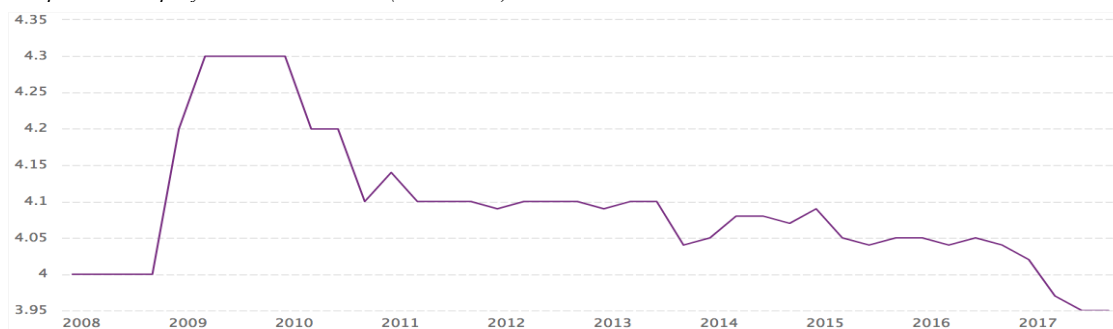
2.1.2 Unemployment Rate

Measurement of unemployment in China is a key of discussion for many economists, as they believe that Chinese government intentionally provides either modified, or strangely calculated data. For example, talking about unemployment rate, it is to notice that according to NBSC (National Bureau of Statistics of China) the values from year 2007-2016 were in range from 4.0 – 4.3%.

The lack of objectivity of this data is given by the specification of the obtained data. NBSC calculated unemployment rate as a registered unemployment exclusively in urban areas, including foreign employees, and re-employed retirees, less the employed in rural labour force. Therefore, in the calculation of unemployment is no consideration of unemployment in the rural areas of China.³⁷

Economists argue, that shown level of unemployment is unrealistic, due to the fact that even external factors such as Financial Crisis in 2008, as shown on Graph 4, did not affect the unemployment rate and was kept in the narrow boundary described earlier. Economists from Chinese universities were conducting a national research on unemployment rate based on official housing survey and found out that the average real unemployment rate between 2002 and 2009 was 10.9%.³⁸

Graph 5: Unemployment rate in China (2008-2017)



Source: Ministry of Human Resources and Social Security, www.ceicdata.com

³⁷ National Bureau of Statistics of China, *National Data*, [accessed online at 09.01.2018 on: www.data.stats.gov.cn/english]

³⁸ "The Economist, The Economist Newspaper "Trying to count China's jobless, 19 Aug. 2015, [accessed online at 9.01.2018 at: www.economist.com/blogs/freeexchange/2015/08/unemployment-china]

Important note to make is that research analysed by the economists are coming from NBSC research. I believe this points out a very straightforward interest of Chinese government to alter officially provided data.

There are many disputes in misinterpretation or belief of data alternation, as the GDP and GDP PPP per capita growth had increasing potential over the period of many years, which might not be expected while having such a high unemployment rate as 10.9% provided by the researchers. On the other hand, this GDP growth might have been, to some extent, caused by foreign workers, and most importantly by foreign companies registering in China in order to participate on the market. These companies might be “empty” companies managed from outside of China, and therefore the employees won’t be included in the household research by NBSC.

2.1.3 Inflation Rate

For the macroeconomic indicator of inflation, the CPI index of all goods without seasonality, for the purposes of comparability with Slovak Republic. When focusing on Chinese CPI major drop from approx. 8.5% in mid-2008 to negative inflation can be noticed, resulting in deflation of almost 2%. This drop resulting in deflation resulted in decrease exports over the period of deflation, due to appreciation of the currency, however China was still ranked among the top exporters in the World, and GDP growth remained at slighter, but continuous growth. The increase of inflation in the period post-financial crisis, was a result of economic stimulus imposed by the government, in order to counter the economic slowdown caused by the 2008 crisis.³⁹

Increased inflation resulted in major problems, which China was facing in period until 2012. These problems included severe real estate bubble, when prices of assets grew between 5 – 10 times the original price; and increase in consumer prices.

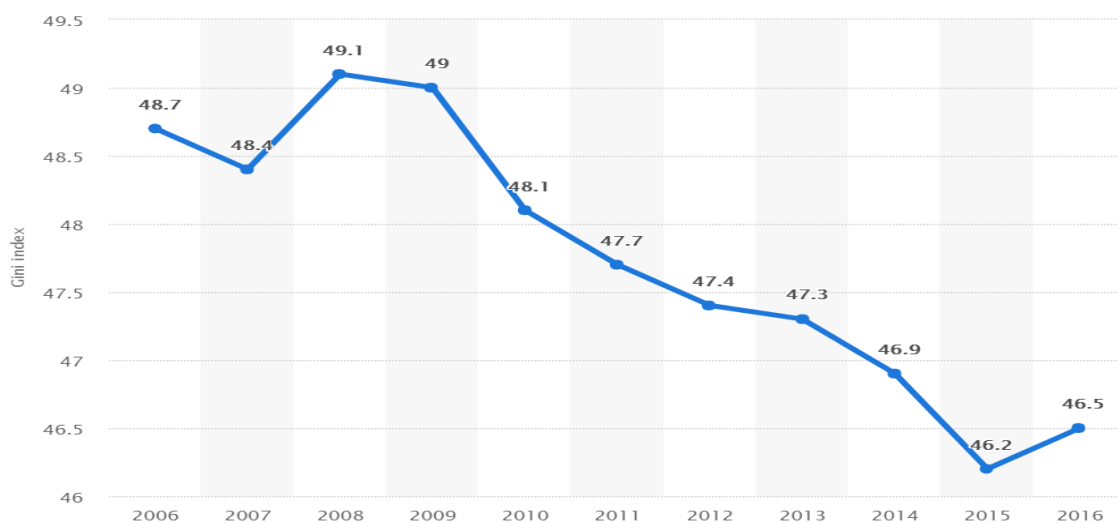
In the last couple of years China is trying to keep the inflation at so called “healthy” rates between 1.5-3% of inflation, which complements with the export strategy of the country.

³⁹ Linyue Li, Thomas D. Willett, and Nan Zhang, “The Effects of the Global Financial Crisis on China's Financial Market and Macroeconomy,” *Economics Research International*, vol. 2012, Article ID 961694, 6 pages, 2012. doi:10.1155/2012/961694

2.1.4 Poverty Level

Issue of poverty is a major topic for Chinese economy. This issue is being addressed by the general secretary of China Xi Jinping, who aims to reduce poverty over the next few years. According to the government, there is about 43.55 million people suffering from poverty in China as of 2016.⁴⁰ According to the new 5-year plan, China aims to lift 10 million people from poverty per year. (Poverty line in China is set to be 2,300 Yuan per year, which equals approximately to 363 USD). As mentioned prior to this subchapter, the GDP PPP per capital in China is ranked on 70/175 place with USD 15,535. Indicator of poverty is important for the timber market due to a likely increase in consumption and therefore demand, especially for lumber, as with decreasing poverty an increase in real estate development is connected in which lumber plays elementary role. Decrease poverty will also likely result in higher purchase power of the country.

Graph 6: Gini coefficient of China (2005-2016)



Source: Statista 2018, www.statista.com

Poverty is measured by Gini Coefficient, which shows the spread in distribution among the population. From Graph 6, a decreasing trend in poverty until 2015 can be observed. As for Gini Coefficient, the closer the value is to a 100, the greater is the inequality. Value of 40 is said by the UN to be the warning level. This clearly shows us, that there is a space for improvement in China.

⁴⁰ Glenn E. Thomas N., „China steps up war on poverty, though some still left behind“ Reuters [accessed online at: <https://www.reuters.com/article/us-china-congress-poverty/china-steps-up-war-on-poverty-though-some-still-left-behind-idUSKBN1CK053> on 17.3.2018]

2.1.5 International Trade Balance

International trade of China has been export based since 1970s', when the country started to increase its importance on the international market, as discussed in the market overview. China became the World largest exporter in 2010, when it took the position of the World leader from Germany.⁴¹

Chinese export based strategy can be seen on their positive Balance of Trade in value of USD 736 billion in 2016, and the fact that the country stays in surplus of net trade since 1993.⁴² The Chinese export is composed out of computers (6.6%), broadcasting equipment (5.6%), and telephones (4.1%), concerning wood products the export of the country are in value of USD 14.8 billion.

Comparing the structure of export with other countries, a major difference in percentages of different categories can be observed as China does not specialize in specific production, like for example Slovakia. China exports in value of USD 29.4 million with its largest partner being Vietnam with 96% of exports as of 2016.⁴³

Imports of the country are structured narrower than the exports. The largest group of products being integrated circuits (9.7%), crude petroleum (8.8%), gold (4.7%), and iron ore (4.4%). The amount of imports conducted in 2016 was USD 1.3 trillion. Timber represented USD 19.6 billion of imports into the country. This is discussed in more depth later in this research.

⁴¹ Linyue Li, Thomas D. Willett, and Nan Zhang, "The Effects of the Global Financial Crisis on China's Financial Market and Macroeconomy," *Economics Research International*, vol. 2012, Article ID 961694, 6 pages, 2012. doi:10.1155/2012/961694

⁴² National Bureau of Statistics of China, *National Data*, [accessed online at 17.03.2018 on: www.data.stats.gov.cn/english]

⁴³ *OECD - China Exports, Imports, and Trade Partners*, Observatory of Economic Complexity, [accessed online on 17.03.2018 at: <https://atlas.media.mit.edu/en/profile/country/chn/>]

2.1.6 Organizations Supporting International Trade

Chinese government does not promote imports into the country through local government, on the contrary the international trade promotion is focusing on setting up cooperation with third parties, which then aim to help with exportation. However, China do have two major organization aiming to promote trade, one of them being China council for the Promotion of International Trade (CCPIT). This organization was established in 1952 and aims to help with organization of many fairs and trades. Among other functions, this organization sets out delegations for Chinese companies to foreign trade fairs and expositions. Most importantly this governmental organization issues certificates of origin of the product, trade mark registration, and helps with intellectual property rights.⁴⁴ The CCPIT has established, since the beginning, 18 overseas offices and has worked with 10 international organization, in order to promote trade.

The second important mode of promotion of international trade is through China Import and Export Fair, also known as the Canton Fair, which is organized by the China Foreign Trade Centre. The fair took place for the first time in 1957, and on the last 122nd fair, 191,950 overseas buyers and 25,049 exhibitors were present. The Canton Fair is currently the biggest promotion of international trade in China.⁴⁵

2.2 Timber Market

These subchapters are focused on a brief description of timber market, on the regulations of importation, market trends, and outline the process of importation with focus on governmental organizations involved.

2.2.1 Introduction to the Market

Since 1980's China has been a major World player on the timber market, due to their high demand and supply of timber and wood products, as a result of changes in the production processes. System of timber market has been monopolised by the Chinese government prior to 1980's, when the country started with liberalization of the timber trade.

⁴⁴ China council for the Promotion of International Trade (CCPIT) [accessed online at: <http://en.ccpit.org/>, on 17.03.18]

⁴⁵ China Export and Import Trade [accessed online on 17.03.2018 at: <http://www.cantonfair.org.cn/>]

However, until now, the harvest and transportation of the wood remains under governmental supervision. This means that producers are required to have permits, which are issued by the government in order to log or transport wood.

Chinese market with timber operates under very specific criteria in a developed system. Wood in China can come either from privately owned forests, collectively owned forests, and forest farms. Prior to year 1998, Chinese government was obtaining most of the timber from state owned forests (see further in the chapter).

There are three main ways of obtaining wood in China; timber directly from the logging companies; from timber markets - number of different markets with wood exists in China, where prices are set differently simply according to supply and demand as opposite to the last medium of distribution; state-owned timber companies. The last medium of distribution is regulated by the government, and prices are set exactly for each category of wood. These firms used to be one of the largest distributor of wood in China, however after year 2002, when the country accepted the Natural Forest Protection Program, these companies decreased their market share due to ban of logging in natural forests.⁴⁶

Timber markets, which are operated by privately owned companies or by individual traders are existing on regional, country, and city areas. It is said that there are around 990 different markets operating in the country, however only about 10% of these are said to be well established entities.

Considering Chinese forestry planning, The State Forestry Administration (SFA) is the central state organization responsible for management of forest national resources. Currently China is trying to increase its coverage by forests from 21% of the country to 21.66%. However according to the National Forest Protection Program, almost 40% of the existing forests are protected, and 56% of the forests are fit for timber production (note: these are logged according to plans, and not all of the share is available for immediate processing).

⁴⁶ Xiufang Sun, Liqun Wang, Zhenbin Gu, „A brief overview of China’s timber market system“, International Forestry Review Vol. 6(3-4), 2004

The SFA in cooperation with Ministry of Commerce (MOFCOM) and Ministry of Foreign Affairs and Customs (FMPRC) launched a campaign against illegal timber, which is believed to represent up to 10% of Chinese imports in 2011. Illegal timber is said to be coming mostly from countries such as Russia, Mozambique, and Papua New Guinea. China has been requiring as secure information as possible about the origin of the imported timber since they have started the campaign against illegal wood.⁴⁷ This campaign may increase Chinese demand of wood from official sources, stabilize the market price levels, and increase the price predictability for suppliers.

2.2.2 Market Trends

Timber on Chinese markets is obtained from importation or from domestic production. The largest importer of wood into China is Russia. However, due to recent events, it is believed that Russia will decrease its export to China, as they have increased the duties on exportation of timber as a way of promoting the domestic production of wooden goods.⁴⁸

From the latest available data for year 2016, China has been the largest world importer of industrial round wood where the country imported 39% of all traded timber in the category and 23% of sawn wood traded in the World. China has been also on top of the ranking as for recovered paper (50%) and pulp for paper (33%).⁴⁹

The number of categories in sawn wood imported into the country and its percentage changes over the last decades, shows a correlation among the Chinese acceptance of National Forest Protection Program in 1998 and the imported sawn wood. With the logging ban on the national forests, China was running out of sawn timber, and many saw mills (which used to be prior to the ban mostly governmentally owned) had to be closed, or are currently operating under their production. This however, gave a birth to several small sawn mills located in close proximity to the markets who are benefiting from the imported timber.⁵⁰

⁴⁷ Timber Trade Federation „*Country Guide to Timber Legality China*“ [accessed online on 20.03.2018 at: http://www.tft-earth.org/wp-content/uploads/2013/03/China_Guide_to_legality_EN.pdf]

⁴⁸ GWMI, „*Russia to gradually increase log export duties in order to promote domestic wood processing*, February 2018, [Accessed online on 20.03.2018 at: <https://www.globalwoodmarketsinfo.com/russia-gradually-increase-log-export-duties-order-promote-domestic-wood-processing/>]

⁴⁹ Food and Agriculture Organization of the United Nations [accessed online on 20.03.2018 at <http://www.fao.org/forestry/>]

⁵⁰ Xiufang Sun, Liqun Wang, Zhenbin Gu, „A brief overview of China’s timber market system“, *International Forestry Review* Vol. 6(3-4), 2004

The lack of available domestic sawn timber in the countries, resulted in promotion of facilities for production and processing of alternatives. Government started heavily supporting production of plywood mills, which resulted in China to be the largest wood-based panel (16% of trade) and plywood exporter in the World as of 2016, and the largest plywood producer since 2013, when the production exceeded the US outputs.⁵¹

The export strategy with timber its related products of the country is as follows. China has exported timber and timber related products in amount of USD 14.8 billion, out of which plywood contributed by 35%, other wood articles by 16%, and the third largest contributor to the export total value was fibreboard with 8.3%. China is the largest contributor to international trade, among other products, also in “Other wood products” which description is to be found in harmonized system codes under codes 4421, and the breakdown of these products is to be found under codes 4415-4420. These are for e.g. wooden tools, boxes, wooden frames for paintings and many others.⁵²

From these data, the importance of plywood in China be seen, and potentially one of the reason behind the shift of the market trends from the previous sawn wood production. However, in the near future, we might observe another interesting change in the domestic market, as the USA, the largest plywood importer from the country, has imposed an anti-dumping measures on importation of such goods from China.

This decision has come to force recently, when the U.S. International Trade Commission voted in favour of 4-0 of imposing such measures on January 10th 2018, and supported the claim that Plywood has been supplied to the U.S. market on lower value than a fair value and with subsidies from the Chinese government. Some of these tariffs results in almost 200% increase of the price.⁵³ As China is the World largest producer and exporter of plywood, these changes might shape the future Chinese market with Timber, so might the Russian duties on exportation of timber.

⁵¹ Food and Agriculture Organization of the United Nations [accessed online on 20.03.2018 at <http://www.fao.org/forestry/>]

⁵² World Customs Organization, “*Harmonized System Database*” [accessed online on 20.03.2018 at: www.wcoomd.org]

⁵³ U.S. International Trade Commission, „*Hardwood Plywood from China*“, Investigation Nos. 701-TA-565 and 731-TA-1431 (Final), Publication 4747, December 2017

Paper products exported in the World, where China has been placed second behind Germany in USD value of exported paper to the market, must be mentioned while discussing wood market. Timber imported into China is also used for the purposes of paper production, these will be described later.

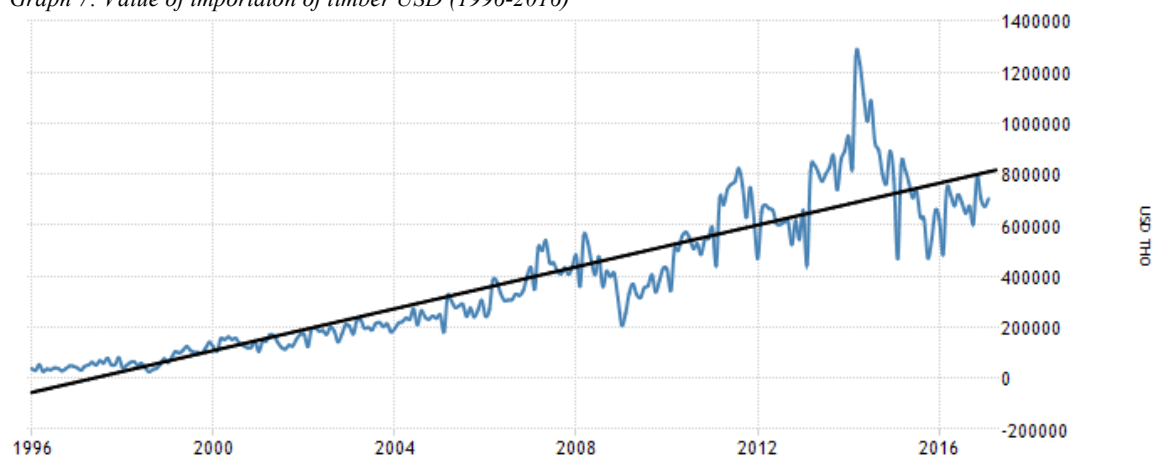
Last, but not least, to mention about the trends on the Chinese market with timber, is the fact that the country is the World largest producer and supplier of furniture on World's market. Where China supplies 36% of the internationally trade furniture, and the U.S imports 34% of it. The overall exportation was done in amount of USD 72 billion as of 2016.⁵⁴

2.2.3 Import Regulations and Customs

As of today, China's dependence on imports is growing, partially due to reasons mentioned earlier in the work. In 1980's during the period of liberalisation of the market, China has started with easing of import regulations. Prior to 1980's Chinese government had complicated system for approval of importation, especially commodities.

At the beginning of 2000's China has abolished permits for importation of timber, and as of today every company which is registered at the Ministry of Commerce (formerly Ministry of Foreign Trade and Economic Co-operation) or any other authorized offices according to Foreign Trade Law for international trade is allowed for any importation of products to China, and therefore including timber.

Graph 7: Value of importation of timber USD (1996-2016)



Source: Trading economics & Chinese customs, (www.tradingeconomics.com)

⁵⁴ OEC - China Exports, Imports, and Trade Partners, Observatory of Economic Complexity, [accessed online on 17.03.2018 at: <https://atlas.media.mit.edu/en/profile/country/chn/>]

Graph 7, provides support for the increasing trend of importation since abolishment of permits for importation of this commodity. The graph follows increasing trend over the period of twenty years with an anomaly growth in 2014. There has been an increase of 9% since 2015, which indicates increasing demand for timber.

Chinese importation is based on restrictions, products are either permitted, restricted or prohibited. As in European Union, some products are completely forbidden from importation into the country, other products are restricted by quotas or licenses.

Chinese customs require an HS code of the product to calculate the tariff duties and taxes for products. These codes can be found on World Customs Organization website. According to these codes you can find customs for each country on each product on WTO websites and further you can find tariffs for MFN and other benefited countries.

MFN stands for Most Favoured Nation, and it includes all members of WTO, and the MFN tariffs applies therefore on all importation from these countries. However, in case any WTO member has a preferential trade arrangements (PTA) or regional trade agreement (RTA), their tariffs might differ according to these agreements. As of today, European Union, and therefore Slovak Republic, does not have any RTA nor PTA with China concerning these goods.⁵⁵

Chinese customs generally require for most products an import license, and might require additional licenses to meet the Chinese standards. These products are divided into three categories according to the license they require; permitted goods; restricted goods, and prohibited goods. Most products falling under permitted goods require only automatic import license, however some of these products, such as for e.g. wine, are subjects to monitoring and require additional licenses. Restricted goods are generally goods who are under quotas and therefore acquisition of non-automatic license is required. The last category of goods cannot be imported into the country whatsoever.

⁵⁵World Trade Organization, „Regional Trade Agreement Database“ [accessed online on 17.03.2018 on: <http://rtais.wto.org/UI/PublicMaintainRTAHome.aspx>]

The process of acquiring licenses can take up to two weeks and the state organization in charge of issuing them is Ministry of Commerce People's Republic of China (MOFCOM).⁵⁶ Step-by-step process of registration a company will be described further in this research, with focus on required licenses and exportation possibilities of Lesprodukt s.r.o, depending on chosen recommendation of penetration to the Chinese market. Goods usually require a CCC mark registration and license in order to enter the Chinese market, however timber does not require any CCC mark, and therefore this process is not required.

2.2.4 Prices of Wood in China

Market price levels of timber in China are never to be assessed accurately, due to the system of domestic market with the commodity. As described earlier, there are many markets operating in China, which have no fixed price, as usual per markets with commodities. Due to lack of statistics for timber categories a table with researchable specific wood types existing in Slovakia is provided.

Table 3: Overview of Market prices & Import value of timber (2016)

	Avg. Market	Avg. Market		Import unit	Import unit
Fx. 0.129	price (RMB/m³)	price (EUR/m³)	Fx. 0.808	value (USD/m³)	value (EUR/m³)
Beech	5200	670.80	Coniferous sawn wood	121.17	97.91
Oak	5450	703.05	Non-Conif. sawn wood	377.24	304.81
Douglas fir	2100	270.90	Coniferous logs	99.26	80.20
Larch	1700	219.30	Non-Conif. logs	259.24	209.47
Cherry	9500	1225.50			
Walnut	13750	1773.75			

Source: Author's interpretation of data obtained from IHB, ITTO and Global wood (www.ihb.de, www.itto.int, www.globalwatch.com)

The market prices shown in Table 3 are coming from approximates of prices on Guangzhou Yuzhu, Zhangjiagang, and Shanghai Furen markets. Total amount of importation for these has been as follows: from hardwood beech 600,000 m³, oak 849,000 m³; and from softwood douglas fir 1,870,000 m³, larch 2,41,000 m³.⁵⁷ The average customs value of sawn wood imported into the country was EUR 153.71, and for logs it was EUR 114.60.⁵⁸

⁵⁶ Ministry of Commerce People's Republic of China, [accessed online on 20.03.2018 on: <http://english.mofcom.gov.cn/>]

⁵⁷ Global Wood, „China Wood Products Prices“ [accessed online on 21.03.2018 on http://www.globalwood.org/market/timber_prices_2017/aaw20170402d.htm]

⁵⁸

3. Exportation of Wood from Slovakia into China

Third Chapter of this work will be focusing on the modes of entry to the market, based on the previous explanation of external and some of the internal factors determining the penetration. The factors which must be taken into consideration while desiring expansion to foreign markets are trade policy conditions, economy of the country, political environment (international relationship among the countries), legal environment, and characteristics of the partner and product.⁵⁹

3.1 Ways of Penetrating the Market

There are generally two most considerable options, which will be evaluated upon further in this chapter, being; setting up own company in China for product distribution, with an option of either selling timber to the local markets, or straight to the manufacturers; or concluding this operation straight through export/import operations with partnership on the Chinese market. These two basic approaches will be explained and elaborated upon them later in Chapter 4 in consideration to the desirable expansion of Lesprodukt s.r.o. to the Chinese market. Therefore, two basic options for the company will be discussed, either by way of equity mode of entry (first option) or business operations (second option), as the third option of penetration to the market, non-equity mode of entry, is not suitable for such company.

3.1.1 Partnership and Business Operations in China

Business Operations and Partnerships are one of the simplest form of exportation of products, due to their relative low requirement of investments. This kind of penetration to the market is mostly suitable for all kind of companies, as some of their benefits are relative low requirement of workforce for the exporting company, the simplicity of the process once all the relationships has been established, and the process has been automatized. It is to be noted, that these factors might change according to the contractual conditions, and services provided by the exporter.

⁵⁹ Sato A., Halík J., Hinčica V., International Business Operations. Prague: Oeconomica Publishing House, 2017. 168 s. ISBN 978-80-245-2205-0.

While choosing the most suitable way of establishing partnership or conducting any business operation activities it is important to decide upon the business strategy of the exporting company. One of the basic decisions are placed around the customer is the way of distributing the goods or products. For example, in case of Lesprodukt s.r.o., among many options you could choose to distribute the wood through wholesalers and retailers, in case of a saw wood (which has already been processed in the country of origin), through a direct exportation in case of rough timber, or through partnership based on some agreements with representatives of the company.

Penetration to the market through wholesaler and retailers is used by companies whose size or product portfolio is not sufficient enough to create their own facilities on the target market, but large enough to partially or fully supply the demand of the wholesaler. These companies work on principles of mark-ups and margins, meaning they earn money on the difference between purchase prices and selling price. Just for clarification, the difference between retailers and wholesalers is in the quantity of the sold products, when wholesalers tend to sell products in higher quantity, by which they are able to sell for cheaper prices.⁶⁰ In case of wood and timber industry, there are not many retailers on the European market, as the rough timber is being sold straight to the manufacturers and in case of saw wood, they are usually being sold to the wholesalers. In Slovak Republic these wholesalers being OBI, Bauhaus, and other do-it-yourself store or wholesalers focusing on supplying construction companies.⁶¹ In other words, retailers work as a bridge between producer and wholesaler.

Commercial Representative is a form of partnership between the exporter and, exclusively company, operating at the target market, in which the representative operates under long-term contract with the exporter (principal). The representative acts on behalf of the and on account of the exporting company in conducting transactions as specified in their contract. The commercial representative works on commission basis, meaning he earns percentage from the business he has conducted. The benefit of such partnership lies in the simplicity and may work as a financially not demanding way of testing a new market. However, the problem with commercial representatives lies in the risk of causing a reputational harm to the exporter as he acts on behalf and on account of the exporter.

⁶⁰ Sato A., Halík J., Hinčica V., International Business Operations. Prague: Oeconomica Publishing House, 2017. 168 s. ISBN 978-80-245-2205-0.

⁶¹ Interview with Ing. Dušan Vatraľ, director of Lesprodukt s.r.o. [conducted on 18.12.2017]

This way of penetration can be done through contracting player on one of the domestic markets in China, and exporting wood straight to the manufacturers based on businesses conducted by the commercial representative.

Another way of penetrating to the Chinese market through partnership with players operating on the target market is through commission agents' contract also known as commission sales agreement. This contract is similar to commercial representative, with the difference being that the agent work on his behalf in account of the exporting company. This principle works on the basis of commission, same as the one mentioned earlier. The potential disadvantage of such an agreement lies in the fact that the exporter does not build up his brand on the market, as the commission agent operates under his name.

Last option of partnership in exportation, which could be applicable for our company, is through Association of Small Exporters, also known as export alliances. This way of exportation is beneficial for companies looking for expansion to markets abroad, who do not possess knowledge, human or capital resources to conduct such operation themselves. These associations are usually created within producers in similar industries. Using such a way of penetration to a foreign market increases the potential market share in the target country, and increase the negotiation power, among many other financial benefits.

3.1.2 Capital Intensive Penetration

Penetrating market through establishment of Limited Liability Company is another possible way of supplying the market with goods. Chinese limited liability Company with the most similar legal rights and obligations to Czech and Slovak s.r.o. is called Wholly Foreign-Owned Enterprise (WFOE). This form of penetration to the market is more capital and time demanding, however in case the company seeks a long-term cooperation with the local buyers, and it could be beneficial for the company to have a strong base on the target market.⁶² This company can be used not only as a medium for selling timber in Chinese market, but can also work as a bridge on the way back to the Slovak, or European market with wood products. Such an operation would be called Refining Operation or Production Cooperation.

⁶² Hebnar J., Kocourková B., Marková L., *Export do Číny, Manuál pro Exportéry*, Zastupitelský úřad ČR v Pekingu, [accessed online on 1.04.2018 at: https://www.mzv.cz/file/832898/export_do_Ciny.pdf]

In such operations, the domestic producer would export wood for production in China and sold the products of such a company back on the EU market. This can be established through cooperation with Chinese manufacturers, and can result in major cost reduction, as the transportation costs could be divided among the interested parties.

Considering establishment of WFOE, description of such a legal entity needs to be included. WFOE is a company wholly owned by another foreign subject, and has similar rights to the local limited liability companies. There are different approaches of establishment of WFOE with different purposes, below outline of foundation of trading WFOE is to be described. The process is divided into two main parts, first one being prior to obtaining license, and the second one post obtaining.

First key of establishment of any company operating in China is the approval of name. This phase of the process is fairly new, and requires some additional information for the government in order to get approval. This new limitation is said to be done due to misleading names which might confuse the customers. The availability of a name can be found on <http://www.chinatrade-markoffice.com>.⁶³

After the name is approved, the proposed company must have a registered address in China. In case the premises are not owned by the investor, there must be at least 12 months lease contract signed which states that those premises are legally leased for business purposes.

Once these steps are done, application for the company must be send to MOFCOM with information about the investors and their representatives, business license, power of attorney for the representatives and ID documents of involved people. This can be all done through the internet, with no need of physical presence. Last step of establishment of the company prior the license obtaining, is to send the approved documents from MOFCOM. These steps involve social security registration, business license, organization code, tax registration and statistical registration certificates. After this the organization legally exists, and only requires license in order to be fully operational.⁶⁴

⁶³ China Trade Mark Office, [accessed at: <http://www.chinatrade-markoffice.com>]

⁶⁴ Dezan S. & Associates,, “*Setting Up a WFOE in China: a Step-by-Step Guide*”, June 22,2017 China Briefing [accessed online on 04.04.2018 at: <http://www.china-briefing.com/news/2017/06/22/setting-wfoe-china-step-step-guide.html>]

Due to the difference between Chinese and European companies in sense of authority and legal representation of the company, the newly established company needs to create its own official seal, which has the power to validate all contracts, and agreements with no relationships of who uses it. This seal can be obtained from The Ministry of Public Security of the People's Republic of China.

Furthermore, WFOE trading company must acquire import / export registration, this registration as discussed earlier in the text, is done at MOFCOM. This registration allows you to exchange money and to refund VATs. Talking about finance, Chinese WFOE requires minimum of two accounts, one being domestic account in Renminbi (Chinese currency) and another one for currency exchange operations but most importantly for being able to send and receive money from abroad.⁶⁵

Provided information above, conclusion, that the process of establishment of the company is demanding, and not the most suitable option for all companies wishing to enter the Chinese market, can be made.

3.2. Contractual Conditions

Contractual conditions are important for closing successful deal with your partner. It is important to closely specify all the required specifics of the business. Here is a list of the most important ones from which some will be evaluated upon further; logistics (with specified places and time), incoterms, price mechanism, method of payment and insurance.

3.2.1 Mode of Transportation - Logistics

Logistics is an important part in process of international trade, since it is all down to the transportation of the goods from country A to country B, in case of this research countries being Slovakia and China. There are generally four ways of transportation of goods, from which only three of them are applicable in our case. These being either rail, road or marine transportation.

⁶⁵Redman K. „*How to form a wholly foreign owned enterprise (WFOE) in China*“ Cogency Global Inc. [Accessed online on 04.04.2018 at: <https://www.cogencyglobal.com/blog/how-to-form-a-wholly-foreign-owned-enterprise-wfoe-in-china>

Due to the location and process of wood logging, there is always a combination of these modes of logistics, as the wood needs to be firstly transported from the forest either to saw, warehouse or to the carrier depending on the cargo.

It is important to agree with the buyer upon specific conditions of logistics, or in case of payment of the freight to choose the most appropriate mode of transportation according to the specifics of the goods taken into consideration the time taken for the transportation and cost.

As prove of conducted agreement between the transporter and the transporting party is in case of marine time transportation Bill of landing (B/L) is issued, and works as a receipt from the transportation company. This document states nature and quantity of goods, residence of shipper, information about the vessel, place of loading and final destination, and other freight stipulations. Due to the fact that the holder of B/L has the right of possession to the carriage and the consignee is not able to take over the goods without the appropriate document a new way of waybill has been used, where the receiver does not need to possess any physical documents in order to take over the goods.

In case of transportation using multiple mode of movements a Thorough B/L or Multimodal Transport B/L FIATA is used.⁶⁶

Train journey from Bratislava, capital of Slovakia, to Chinese Dalian is 11,000km long and takes up to 17 days. This route goes through Ukraine and Russia and is expected to become more frequent. According to the latest news the first trial shipment was conducted recently in November 2017 on the opposite direction, meaning from Dalian to Bratislava. However, during the first half of 2018 it is expected to send train from Bratislava once a week and increase the frequency of the transportation to twice a week in the second half of 2018.⁶⁷ The containers are being reloaded on Slovak-Ukrainian borders in region of Kosice, where Lesprodukt s.r.o. operates, therefore it might be an interesting mode of transportation for the company in the proposed operation, depending on cost of the freight.

⁶⁶ Pavelka L, Jamborova E.M., Ruzenkova V., „*Manual Slovenskeho Exportera*“, Eximbanka SK [accessed on 8.4.2018 at: https://www.eximbanka.sk/buxus/docs/dokumenty/Manual_slovenskeho_exportera.pdf]

⁶⁷ The Slovak Spectator, *First trial freight train from China arrives in Bratislava*, 13 November 2017 [Accessed on 08.04.2018 at: <https://spectator.sme.sk/c/20695576/first-trial-freight-train-from-china-arrives-in-bratislava.html>]

Another mode of transportation used to transport the goods from Slovakia to China is through marine time transportation. The port used for this transportation depends on the contractual conditions and agreements in case of partnership, in case of own exportation it is always recommended to contact the local carrier for appropriate way of transportation. In case of marine time transportation, it is much slower than using rails. However, the clear benefits are lower cost, as marine time transportation is the cheapest of all, and possibility of transporting large volume of goods at the same time. The average time taken to transport goods from Slovakia to China by marine time is approximately 6-8 weeks.⁶⁸ The importance of marine time transportation can be seen on the fact that almost 80% of European international shipping is done by vessels.⁶⁹

Last but not least, an on-road transportation must be used in timber industry. This transportation is done by trucks and serves as a basic mode of movement of the goods from the place of logging. In case the cargo goes straight to the buyer, the transportation costs are usually carried by the buyer.⁷⁰

3.2.2 Financing and Insurance

Financing banks and insurance companies are key for conduction export and import operations. Insurance and short-term export letter of credit works as a risk management for the exporting company. On Slovakian market EXIMBANK, export import oriented bank provides financial and insurance services to companies seeking to conduct business in these branches⁷¹. Involvement of such entity greatly reduces risks. Insurance works as management of risk in case of failure of the transaction, accidents during the shipment, intentional damage done by a third party and may other risks.

⁶⁸ Slovenská agentura pre rozvoj investícií a obchodu, *Exportujte do zahraničia*, [accessed online on 5.04.2018 at: www.sario.sk]

⁶⁹ Sato A., Halík J., Hinčica V., *International Business Operations*. Prague: Oeconomica Publishing House, 2017. 168 s. ISBN 978-80-245-2205-0.

⁷⁰ I Interview with Ing. Dušan Vatraľ, director of Lesprodukt s.r.o. [conducted on 18.12.2017]

⁷¹ Exportna Importna Banka SK, [Accessed online on 08.04.2018 at: <https://www.eximbanka.sk/>]

To achieve insurance or any other financial service, it is important to calculate the value of goods for customs. This value is calculated by value of the timber with all connected costs related to packing, commissions, and transportation. Sum of all these costs are called the transaction value, and is required not only by domestic financial and insurance institution, but also by the customs in the country of import for calculation of related taxes and costs.

Recommendation on which way of financing, and the principle of these financing will be discussed later in fourth chapter. Due to the variety of the possible financing and insurance services, only one of each will be discussed later with acknowledgment of Lesprodukt.

Investigating insurance conditions more thoroughly, three basic definitions described by Institute of London Underwriters (ICC), must be mentioned. The three-basic division of ICC are as stated below:

ICC–A (All Risks) – Undertakes all possible risks without any exception

ICC–B (Limited Coverage) –Transportation risks incl. environmental risks

ICC–C (Named Risks) – Transportation risks⁷²

3.2.3 Incoterms

International Commercial Terms (INCOTERMS) written by the International Chamber of Commerce, were created in order to clarify and make internationally acceptable rules and obligations of parties involved in international transactions. These terms specify who is responsible for cost of risks like insurance, customs, duties and freights. It is important to note, that Incoterms do not substitute the purchase / sale contract of the goods, they just work as a clarification for them. The latest terms used are Incoterms®2010, and they compose out of 11 rules. The most appropriate ones for transportation are going to be outlined below.⁷³

FCA – Free Carrier, this operation represents a delivery on an agreed place to the carrier. At this moment, all the risks and costs associated with the transportations are passed to the buyer. Therefore, the seller is not responsible for any customs or other importation costs.

⁷²L. Pavelka, E.M. Jamborova, V. Ruzenkova, „*Manual Slovenskeho Exportera*“, Eximbanka SK [accessed on 8.4.2018 at: https://www.eximbanka.sk/buxus/docs/dokumenty/Manual_slovenskeho_exportera.pdf]

⁷³ International Chamber of Commerce [accessed on 05.04.2018 at: www.iccwbo.org]

CIP – Carriage and Insurance Paid To, the seller is obliged to pay the cost of the transportation and the related cost of insurance up to the point where he delivers the goods to a carrier. The insurance shall cover minimum of 110% of the contractual price.

FAS - Free Alongside Ship, this term represents an operation in which the seller transports the goods up to the port, and the obligations and costs are moved along to the buyer for example at the point when the carriage is next to the ship on a quay.

FOB Free on Board, operation similar to FAS, with the difference that the obligations are passed to the buyer at a point when the goods are successfully boarded on the ship. Therefore, in case the goods will be damaged or lost during the process of boarding, the costs are carried by the seller.

CFR – Cost and Freight, the selling party delivers the goods to the vessel, specified by the buyer, and the risks are passed at the point when the carriage is on board. The difference in FOB and CFR, is that in CFR the seller is carrying the freight costs.

CPT – The seller is required to carry costs of transportation only to the point of the point when the goods are delivered to the nominated carrier.

CIF Cost, Insurance and Freight, is similar to CFR with a difference of Insurance cost up to the point when the carriage is on the vessel.⁷⁴

⁷⁴Sato A., Halík J. Hinčica V., International Business Operations. Prague: Oeconomica Publishing House, 2017. 168 s. ISBN 978-80-245-2205-0..

3.2.4 Payments

There are many modes of payments available on the market. However, only description of letter of credit and bill of exchange will be provided below, due to the extent of this work.

Bill of exchange is a commonly used method of payment, which has the benefit in simplicity and an option of selling the note to a third party. In order for bill of exchange to be acceptable, it must fulfil certain conditions; in the body of the text must be explicitly state that this is a bill of exchange, specified amount of money, name of the drawee and the name of the drawer, and maturity time. The payments of bill of exchange differ and can be paid either at sight, fixed day, in a period, and at period after sight. Large benefit of bill of exchange lies in the fact that the drawer may sell the bill of exchange for example to an exporting bank such as EXIMBANKA SR prior to time when the payment of the drawee is due. The issue with bill of exchanges is that many confusions and disputes might arise from transferring them among the beneficiaries, as there is no obligation of the drawer to notify the drawee, when the drawer changes. Another issue is the credibility of the drawee, there is a possibility to have a third party who guarantees for the payment, however payment disputes might be long-lasting and for smaller exporters result in financial distress over.

Another way of payment method is letter of credit (L/C). This method of payment is one of the most secure, as the guarantee is bank of the importer. The applicant requests a payment order at his domestic bank (issuing bank) and sets out requirement for all necessary documents in order for the transaction to take place. Once the importing bank receives all the necessary information it notifies the advising bank of the exporter. Once the importer and exporter agrees upon all the conditions on the L/C the advising bank send documents to issuing bank after receiving the payment. These documents are passed on the importer in order to be able to obtain the goods from the transportation company. L/C is one of the safest payments due to the cooperation of banks who works as guarantors for the transaction.⁷⁵

⁷⁵ L. Pavelka, E.M. Jamborova, V. Ruzenkova, „*Manual Slovenskeho Exportera*“, Eximbanka SK [accessed on 8.4.2018 at: https://www.eximbanka.sk/buxus/docs/dokumenty/Manual_slovenskeho_exportera.pdf]

3.4 Cultural differences Related to Business Practices

Culture describes specific social groups with similar traits of characteristics, geographical location, religion, values, and beliefs. Culture has been investigated through so called cultural dimension, which were described by many scientists over the years, however one of the most significant ones are Geert Hofstede and Fons Trompenaars. G. Hofstede sees culture mostly as a set of values and beliefs whereas F. Trompenaars was discovering culture as a way in which specific groups solve problems. Focus is only placed on one factor determining the difference in culture among Slovakia and China from each scientist, as these are the most important ones.⁷⁶

China is a highly collectivist country in comparison to Slovakia, this specific of the culture was described by Mr. Hofstede, and it focuses on the relationships within the society. Collectivist cultures, on a contradictory to individualist cultures, pays focus on acting in accordance with the social group. This difference between these countries is essential for understanding the business negotiation and process of decision making. Collectivist cultures make their decision according to other members of their in-groups, and tend to sacrifice their own benefit for the benefit of the group. From this a difference in the pace of the negotiation arises, as the time taken to come to a decision in collectivist cultures tend to take much longer, due to the compliance of the whole group.⁷⁷

Another major difference to be evaluated upon is considering the way collectivist cultures value relationship as a whole, not only in business environment. Collectivist cultures takes largely into consideration the relationship on workplace, unlike individualistic countries. This factor will be further described in next subchapter of negotiation ethics, as these cultural differences pays capital role in negotiation processes and especially in conflict management.⁷⁸

⁷⁶ Hofstede, G. (2011). *Dimensionalizing cultures: The Hofstede model in context*. Online readings in psychology and culture, 2(1), 8. [accessed online 28.03.2018 at: <http://scholarworks.gvsu.edu/cgi/viewcontent.cgi?article=1014&context=orpc>]

⁷⁷ Triandis, H. C., Bontempo, R., Villareal, M. J., Asai, M., & Lucca, N. (1988). *Individualism and collectivism: Cross-cultural perspectives on self-in-group relationships*. Journal of personality and Social Psychology, 54(2), 323.

⁷⁸ Triandis, H. C. (2001). *Individualism- collectivism and personality*. Journal of personality, 69(6), 907-924. Chicago

Mr. Trompenaars came with an idea of describing cultures in a specific and diffuse way, when specific cultures have a strong distinction between personal and social life, whereas in diffuse cultures the border between these two is closely connected.⁷⁹ China is a diffuse culture, in which it is very usual to have a strong and honest relationships with others. This is key for understanding the mentality of Chinese people in communication with other people, and importantly for understanding of decision making process.

Lastly, China is so called face-saving culture, meaning that for them it is unacceptable to be humiliated or confronted publicly. Face-saving cultures tend to hide their true feelings, as they believe it is unacceptable to show their personal feeling publicly. This greatly affects business negotiations.

The difference in hiding emotions as a non-verbal communication is also to be described. China is one of the implicit culture. Implicit cultures require a lot of content in order to understand the true message. This can be largely seen in differences among business contracts, implicit cultures lack detailed descriptions of future and current operations in the contract, whereas in explicit cultures, such as Germany, everything is clearly specified. In case of dispute, unlike explicit cultures, both parties are trying to find a mutually beneficial solution.⁸⁰

⁷⁹ Trompenaars F., Hampden-Turner C.. *Riding the waves of culture: Understanding diversity in global business*. Nicholas Brealey Publishing, 2011. ISBN: 857881761

⁸⁰ Bočánková M. a kol. *Intercultural communication: typical features of the Czech, British, American, Japanese, Chinese and Arab cultures*. 2. přeprac. vyd. Praha: Oeconomica, 2010. 152 s. ISBN 978-80-245-1648-6

4. Practical Process & Recommendations for Lesprodukt s.r.o.

Aim of this chapter is to describe the company of Lesprodukt s.r.o. in order to gain insight into their production capacity and variety of timber supplied to the market. This is important in order to investigate whether there is an opportunity on Chinese market for such company. Further, recommendation on the preferable way of penetration, taken into consideration experience in international trade and size of the company, description of steps required in order to conduct such operation, and other recommendations such as most appropriate use of mode of payment will be given. It is to note, that this work is not focused on the profitability of such operation and should not be perceived as a business plan. This work, and namely chapter, should be perceived as an investigation on whether there is a demand for products of Lesprodukt on the Chinese market, and as description and recommendation on the chosen most appropriate international operation. The financial models are for Lesprodukt to conduct and based on them to decide the profitability of the suggested expansion, and therefore are not part of this work.

4.1 Lesprodukt s.r.o.

Lesprodukt s.r.o. (“Lesprodukt”, “Company” or “Firm”) is a company operating on Slovak market since it was established in year 2008. The company has operations in timber logging, timber purchasing and re-selling, consulting, hunting, short distance transportation, and function as a professional forest manager for third parties.⁸¹ It has a registered office at Hunkovce, near city of Svidnik.

Company conducts its activities in eastern part of Slovakia, close to Polish and Ukrainian borders, in region of Dukla. Due to this strategic location, it is able to conduct international trade on European market as of now, from my understanding it has been active in longer trade relationship only in Poland and Slovakia. This region of Slovakia is also known for environmentally protected area of Východné Karpaty, which is surrounding the operational area the Company.

⁸¹ Official website of Lesprodukt s.r.o., [accessed on 08.04.2018 at: <http://www.lesprodukt.sk>]

4.1.1 Forest Stewardship Council (FSC) Certificate

The Company pays attention to long-term sustainability of the ecosystem in the forest and the sustainability of the forest itself, due to which it has received Forest Stewardship Council (FSC) certificate. Forest Stewardship Council is a world-wide non-profit organization. This certificate is given to forest managers who are focused on environmentally beneficial, socially beneficial and economical prosperous management of the forests, and goods coming from companies owning this certificate are branded with FSC logo, which ensures the legality of the product for all companies included in the process of supply chain management.

This certificate has been introduced in 1993 and is said to be one of the most difficult and most reliable certification, which can be obtained for an operator on a timber market. FSC members are also automatically granted membership in ISEAL alliance, which includes Fairtrade, The Marine Stewardship Council and Rainforest Alliance. This certificate is also supported by all environmental groups such as Greenpeace, Sierra Club, National Wildlife Federation, and WWF.⁸² As discussed earlier, the issue of trade with illegally logged wood has become a large problem on the timber market and is assumed to make up to 10-30% of all the supplied wood on the market.⁸³

4.1.2 Production Overview

Prediction for logging in year of 2018 is in amount of 8,500 m³, taken into consideration of the current market trends in Slovakia, as mentioned previously in first chapter the Slovak market is facing a continuous decrease in price levels which leads to production to be under its maximum potential. The maximum capacity on the held forests with 1,950 ha of land is higher than the planned value by one thousand cubic meters. It is important to note, that the planned production is excluding calamity logging that makes up to 42 - 65% of logging on the market.⁸⁴

⁸² Forest Stewardship Council official website [accessed on 09.04.2018 at: <https://us.fsc.org/en-us/what-we-do/mission-and-vision>]

⁸³ Hlaváček J., *Management lesních ekosystému*, amo.cz, November 2017 [accessed online at 7.01.2018 on: https://www.amo.cz/wpcontent/uploads/2016/11/UNEA_lesy_final.pdf]

⁸⁴ Tisková agentúra Slovenskej Republiky, „Z lesov miznú milióny kubíkov dreva ročne. Za posledné desaťročia sa plánovaná ťažba takmer zdvojnásobila“, FinWeb 17.07.2017 [accessed online at 6.01.2018 at: <https://finweb.hnonline.sk/ekonomika/996731-z-lesov-miznu-miliony-kubikov-dreva-rocne-za-posledne-desatrocia-sa-planovana-tazba-takmer-zdvojnasoila>]

When roughly comparing Lesprodukt to the competition on the private ownership of timber, note, that the portion of the production is a small percentage out of the whole production, must be made. Taken into consideration the amount of deliveries of the whole market in year 2016 of circa 9,267,000 m³, with 40% of privately owned forests, which are to be taken as a competition Lesprodukt creates around 2.5% of the market share. It is to note that this information is to be a high-level approximate as to fully discover the market share it would require conducting in depth market research logging companies on privately owned forests.

Lesprodukt plans to expand its area of operation by additional acquisition of 2,100 ha of forest, which is planned to be conducted in period of 3 years. This acquisition would increase the potential maximum logging capacity by 5,000 ha resulting in overall production capacity of 14,500 m³. The acquisition would dramatically increase the market share of the company and further results in cut of costs per one logged cubic meter.⁸⁵

Due to the forest diversity and market prices, the firm is focused on planning forest growth in beech wood, which as of now makes 95% of logging. The reason for the high portion of beech wood in production is also due to the current market strategy of the company which are influenced by recent price growth on non-coniferous market, as seen in Chapter 1 on Graph 3. Beech is a most commonly used hardwood non-coniferous tree for furniture production in Europe, due to its natural flexibility and endurance. However, there are many other uses of beech for example for production of modal (textile fibre), barrels for alcohol production of wine and spirits, paper products, and is also heavily used construction.

Elaborating on the use of the logged wood in manufacturing discovery, that 65% of the logged wood is fibre, which can be used for production of paper, cardboards, and tissues, is to be found. Processed wood fibre can be also used for construction purposes, when pressed into hard panels. These panels are used as an alternative to more expensive plywood, in case the material does not require strength. Furthermore, 25% of the timber is a sawn wood production, which is appropriate for construction and furniture production purposes (lumber). Rest of the production is high quality and usually serves for wood veneer purposes. Wood veneer are slim slices of wood used mostly in furniture production.

⁸⁵ Interview with Ing. Dušan Vatraľ, director of Lesprodukt s.r.o. [conducted on 18.12.2017]

Lesprodukt mostly conducts trade with these STN categories of wood at these average market prices. As mentioned in Subchapter 1.2.3 *Regulations and Bonity Categories*, wood of BK II. category is used in special lumber (saw wood), and BK III. A, BK III.B, and BK III. C category is round logs for lumber. Where BK stands for Beech wood.⁸⁶ Furthermore, Lesprodukt is largely active, as described earlier, in BK Wood fibre.

4.2 Practical Process of the Findings

Looking at trends on Slovak and Chinese market, a rise in demand for wood products, compared to stagnating market in the whole European Union, can be seen. From these trends, and mostly from the occurring changes on the importation from Russia, due to the export quotas on timber, an increased demand of timber in China, due to the lack of wood imports from Russia are creating a gap on domestic market, is observed. Furthermore, China's economy has been stably increasing and its market share has been rapidly growing over the period of last decade. With the poverty fighting policy of the general secretary Xi Jinping, an increased investment into real estate development can be expected, which is closely connected with demand for wood, as lumber is used in construction. Due to the realities mentioned above evaluation that China is a market where a gap for products of Lesprodukt are to be found, can be made.

4.2.1 Recommended Ways of Penetration

Focusing on the most suitable and sustainable way of penetration it is necessary to mention once again that Lesprodukt lacks experience with international trade outside of European Union. Furthermore, looking at current production capacities and taking into consideration ongoing contracts on Slovak market ending in period of two years as of now a capital-intensive way of penetrating the Chinese market might not be the most appropriate way. Due to these factors focus will be placed on recommendations in boundaries of partnership.

However, it is recommended for the company to open up a WFOE in future in case the company will wish to engage on the market more intensively.

⁸⁶ Greppel E., Paluš H. et al., „*Kvalita dreva a obchod s drevom*“, Národné lesnícké centrum, Zvolen 2007, ISBN 978-80-8093-028-8

This must also be taken into consideration once the company will have higher production capacity in order to decrease relatively large costs for establishment and operation of such a company.⁸⁷ The complex process of establishment of WFOE has been described previously in Chapter 3.

The considered ways of partnership were decided previously in Chapter 3, out of these possibilities resale and wholesale relations can be eliminated, due to the relatively small production capacity. Further on, focus will be placed at commercial representative, commission agent, and associate of small exporters, and evaluate their compliance with the characteristics of the company.

Association of small exporters is a very secure way of penetration, who would be a great fit for Lesprodukt s.r.o. due to their lack of experience in conducting such operations. However, entering an association brings obligations to the participating company, as they share contracts with other involved organizations in the alliance. This way of penetration might possibly result in cost reduction in comparison to conducting the whole process of exportation within the company, however the price policy of such organization might not cooperate with the market strategy of Lesprodukt and due to the obligations arising from such alliance the costs and time taken to break from any unfavorable deal within the association might in the end result in lower profitability or loss for the company. Considering these realities, I would not suggest for the company to enter in such an alliance.

The recommended partnerships ways for the company are through Commercial representative and Commission agent. These are one of the capital least intensive ways of penetration, and can be conducted in any amount of production. These ways of penetration are also recommended as due to the size of the company, the reputational risk on Chinese market is not such a significant as the brand image of such small companies is usually not taken into consideration on the markets. However, in case the company would like to secure the reputational risk, commission agent is the better choice for them.

⁸⁷ Interview with Ing. Dušan Vatraľ, director of Lesprodukt s.r.o. [conducted on 18.12.2017]

Such contracts work on commission bases or fixed salaries, when it is important for the company to secure a fixed amount of commission or salary in the contract. It is strongly recommended for the company to work with the agent on commission bases in order to decrease the potential financial risk arising from fixed salary in case the Agent would not satisfy the expectations and would not be able to deliver any orders.⁸⁸

4.2.2 Establishment of Partnership

Once the most appropriate method of penetration for the company has been picked, recommendation on a way of choosing the right partner is to follow. In order to choose the right partner for establishing partnership in China in form of previously discussed Commission Agent's contract or Commercial representative, it is highly recommended for the company to visit business expositions and fairs in order to communicate with the partners and most importantly to create a benchmark on behavior of local businessman. Furthermore, involvement of domestic authorities might be of a help in recommendation for already tested partners in China. This is why contacting organizations promoting trade with China such as SARIO, CSKS or SCJBC, as mentioned in Chapter 1 is a great start on getting information about already established cooperation with agents in China.⁸⁹ Another way to get information about the market is to connect directly with CCPIT, which is promoting international trade.⁹⁰

It is strongly recommended, among other suggestions, to ask for the import license of the agent or distributor, list of products the partner is currently offering, seek recommendation letters of companies the agent is already cooperating with, and from the financial point of view to agree upon commission fee in percentage from sold goods rather than fixed amount. As mentioned before, fairs are a great way on how to see what the agents are asking for in terms of commissions and conditions. Fair to recommend to the company is definitely the China Import and Export Fair, which is the largest event taking place in Canton since 1957.

⁸⁸ Sato A., Halík J., Hinčica V., International Business Operations. Prague: Oeconomica Publishing House, 2017. 168 s. ISBN 978-80-245-2205-0..

⁸⁹ Slovenská agentúra pre rozvoj investícií a obchodu, *Exportujte do zahraničia*, [accessed online on 05.04.2018 at: www.sario.sk]

⁸⁹ Slovensko-Čínská podnikateľská rada [accessed online on 05.04.2018 at: www.scjbc.eu]

⁸⁹ Czech-Slovak-Chinese Chamber, [accessed online on 05.04.2018 at: www.czc.cn]

⁹⁰ China council for the Promotion of Intranational Trade (CCPIT) [accessed online at: <http://en.ccpit.org/>, on 06.04.2018]

The fair happens to be the biggest promotion of international trade on the domestic market with exhibitors and buyers from all branches of businesses.⁹¹ It is important to note, that Chinese commission agents usually work as importing partners too, meaning that the whole administrative process of importation can be conducted by them. This levies lot of work from the exporting company, as the procedures and most of the websites necessary for successful importation process are in Mandarin.

When approaching Agents through different ways, such as looking them up at the internet. It is not recommended to communicate with Chinese Agents by email, as the usual habit is to send messages by fax. When an email is required, translation into Mandarin is advised, as many people do not speak English.⁹²

4.2.3 INCOTERMS, Law & Delivery

Once the Agent is chosen and the commission contract is signed, an offer for purchase should be received in time. This offer should include all the necessary information about type of wood, amount, price and time taken for delivery. Once agreement upon the offer has been made, the firm will send an approval to the Agent for signing the sale contract with the interested party.

The contract should include the supplementary description of INCOTERMS in order to clarify all required transportation, freight and insurance costs. However most importantly the contract needs to state according to which law the contract and any possible disputes will be settled. Here recommendation for using Slovak law, in case the importer will agree, is given. Another recommendation is to use law in which the company is able to find an appropriate support in. In case of any dispute arising from the business avoiding court by mediation or outside of court settlement is recommended, as the costs are usually lower.

⁹¹ China Export and Import Trade [accessed online on 06.04.2018 at: <http://www.cantonfair.org.cn/>]

⁹² International Trade Administration [accessed online on 08.04.2018 at <https://www.export.gov/article?id=China-Market-Overview>]

Lesprodukt's most appropriate and secure INCOTERMS to use are FAS, CPT, and FCA, depending on the chosen way of transportation. The decision upon transportation is left on Lesprodukt, as for the correct evaluation a place of shipment (according to the agent), convenience and mostly the cost of freight transportation. It is important to state exact delivery conditions (Just-in-time, accurate date, fixed, according to demand etc.), as for our company the most practically used delivery terms are going to be on accurate date or period of time, due to the nature of business.

Such terms do not require the seller to carry transportation costs of the goods and further he is not required to procure insurance, and therefore, compared to other INCOTERMS requires least capital. Exception being CPT, where the seller carries cost of transportation until the goods reach the agreed carrier. Insurance is strongly recommended in order to proceed customs in China and Slovakia, and an obligation in case of financing the process using export/import banks. Therefore, one party is required to carry such cost of insurance. The most secure way is to insure the goods from both sides, sellers & buyers.

Both of these obligations require the seller to clear the goods for exportation, therefore Lesprodukt will have to prepare all the necessary documentation for customs. Such a process and all the required documentation will be mentioned later in this chapter.

4.2.4 Most Suitable Payment Method

The most secure ways of payments are advance payments in full or partially, however in reality not many importers or buyers wish to pay fully for goods which they do not have. In case of advance payments, the buyer trusts the seller to deliver goods, with a difficult way of getting the money back in case the goods would not be delivered. This will be theoretically the most recommended way of payment, however in real life situations, buyers do not want to under come such a risk and at the same time from the business perspective, it is not beneficial to pay for the goods from their own money. This is the reason why most buyers wish to purchase goods on invoiced with postpone payments, such as 30 or 60 days, as through this way, they have an option to sell the goods prior the payment to the producer.⁹³

⁹³ Sato A., Halík J. Hinčica V., International Business Operations. Prague: Oeconomica Publishing House, 2017. 168 s. ISBN 978-80-245-2205-0..

In consideration of the practical use and benefit for both, the seller and the buyer, using payment method called Letter of Credit (L/C) is the most appropriate fit. Letter of Credit is very secure and therefore almost risk free; only in case the importers bank is trustworthy. In situation when issuing bank is not considered as a reliable, exporter may request a confirmed L/C, this means that there will be a second guarantor who assures the payment.

When considering using Letter of Credit as a method of payment, it is important to mention that this payment method will be used in purchase or sale contract. After this step, the importer asks his domestic bank to issue a letter of credit in favor of the exporter. The issuing bank approaches Slovak bank, in this case use of previously mentioned EXIMBANK SK or any other commercial provider of such operation can be of a fit, to provide them with the issued L/C in favor of the exporter. Lesprodukt will be then asked to verify all the provided conditions in the issued letter of credit, namely the terms of export transaction (incl. method of payment, insurance, quality of goods, quantity and other important information). Furthermore, an agreed trigger of payment needs to be specified in the conditions, as according to this the banks are able to assess their risk in such transaction and know when to conduct transfer of capital. This payment trigger can be for example a specific date or transfer of documents relating to owning rights for the goods.

When all the terms are met and confirmed involved banks will then require Lesprodukt to provide all the export / import documentation, as specified in per the purchase contract, in order to conduct the operation and most importantly to check whether all conditions for the successful shipping are met. The exporting bank then moves these documents to the issuing bank in the moment specified in the L/C and purchase contract. These documents will be outline in the next subchapter.

Once these documents are obtained and checked by the importer's bank, the bank informs the buyer that all the required conditions were met, and will transfer money to the exporting bank, and upon confirmation on the bank will transfer all required documents to the importer.

It is important to focus a little bit more in depth on the currency and invoice time issues. In case of letter of credit or bill of exchange, mentioned bellow, a specification of currency plays an important factor. For Lesprodukt, as a Slovak company, issuing invoiced in Euros is the most preferable option, however the importer might face difficulties with exchange

of currency, due to the regulated foreign currency market operating in China. In this case, recommendation on alternative acceptance of USD is preferable, however payments in RMB are not advised. In case of future establishment of WFOE, the company needs to have two bank accounts, one for domestic payments and the second one for foreign currency payments. This issue of currency is becoming more complex when creating WFOE, and should be investigated by Lesprodukt in case of establishment of such entity.

In case Lesprodukt's management would not want to undergo such a process, a bill of exchange might be used as an alternative to L/C. This alternative is less secure as there is usually no bank to guarantee the payment, however the benefit of such method is the option to sell the obligation of payment to a third party prior to the due day.

4.2.5 Insurance & Financing

In case the INCOTERMS would result in cost bearing options, the exporter can use services of exporting banks to ask for financing obligations carried by the exporter. These might be for example be freight and insurance costs, depending upon the agreed terms. As mentioned prior to this, financial profitability and conditions will be mentioned only theoretically, and therefore there this work would not include specific numbers. In consideration of benefiting from financial services of banks, such as EXIMBANK SK, arranging meeting with banker who is able to provide information about all services including L/C fee and insurances is strongly advised. Due to the diversity of this topic, only outline of the basic conditions used in insurance will be provided.

Basic insurance divides into KARGO and KASCO, where the first one mentioned covers the transportation medium, and the second one take coverage of the goods only. KARGO insurance for Lesprodukt can be also applicable, as the company owns trucks which are currently used solely for short-distance transportation. Considering ICC terms, the most secure one is of course ICC-A, however considering the transportation route and frequency of shipments through such a route, in case Lesprodukt would have to be responsible for bearing insurance ICC-C should be sufficient enough in consideration of cost – benefit analysis.⁹⁴

⁹⁴ Hebnar J., Kocourková B., Marková L., *Export do Číny, Manuál pro Exportéry*, Zastupitelský úřad ČR v Pekingu, [accessed online on 1.04.2018 at: https://www.mzv.cz/file/832898/export_do_Ciny.pdf]

Furthermore, in consideration of using Bill of Exchange as a payment method, insurance against non-payment of a client is also available on the market and might be of a consideration when conducting business with new buyers.

4.3 Process of Export & Import

This subchapter will focus on the main steps in order to successfully import and export goods. Detail will be paid to all necessary documentations and organizations involved.

4.3.1 Export Obligations

The role of exporter is to prepare all the required documents as stated in the purchase / sale contract signed with the buyer. First element, which works as a base for all other documents involved is the invoice. Invoice needs to include all the elementary information as a usual business invoice and further needs to have HS code of the product stated, currency of the invoice, INCOTERMS, and commission in case of agent's contract.

Next step of invoice is so called customs invoice, which serves as a base for calculation of all the required tariffs and taxes in the importing country. This document, in comparison with the business invoice includes: invoiced amount, mode of transportation and its costs, insurance costs, packaging costs, EORI code, and method of payment. EORI code is a unique sequence of digits used for communication with all customs in European Union, and therefore required even for communication with domestic Slovakian customs. Lesprodukt has been already registered with EORI, and therefore registration process will not be described.⁹⁵ The customs invoice is being checked and approved by the Slovakian customs.

Depending on the agreement among Lesprodukt and the buyer, additional documents such as shipping and insurance materials must be prepared by the company and delivered to the customs in order to successfully proceed.

⁹⁵ Finanční Správa, EORI [accessed online at 10.04.2018 on: <https://www.financnasprava.sk/sk/podnikatelia/clo-obchodny-tovar/EORI>]

However, as discussed earlier, if the company is to use most suitable INCOTERMS, these documents will be prepared by the importer. In consideration of shipping, as discussed earlier combination shipment of Transport B/L FIATA would be used.

As stated above, the invoice needs to have HS code stated. When looking at current products of Lesprodukt all of them are in HS category 44 “Wood and articles of wood; wood charcoal”, and more specifically in non-coniferous wood in rough HS 44039400 and HS 44079940, HS 44079990, and HS 44079200 into which beech saw wood falls with difference on their thickness.⁹⁶ As of now, there is only a requirement for Lesprodukt to have an exporting license for such goods, which it already has obtained for their previously conducted trades, but there are no export regulations for such products.⁹⁷

Another document to mention in this chapter is the Origin of Goods declaration. This is another document required to be delivered by the exporter. As for timber, it is a much easier process due to the fact that this good is wholly originated in one country. Origin of Goods is prepared upon request by the SOPK and this document is called FORM A.

Lesprodukt is a registered payer of VAT, due to this, a documentation providing valid VAT register is required to proceed to the final requirement in order to successfully apply for exportation of goods from Slovakia.⁹⁸

All these documents stated above are required in order to file for Export Accompanying Document (EAD). This documentation is required in case of exportation of documents goods in value above 1000 EUR, which in case of Lesprodukt will be the case.

⁹⁶ European Customs Portal [accessed online on 10.04.2018 at <https://www.tariffnumber.com/>]

⁹⁷ Finančni Sprava, TARIC [accessed online on 10.04.2018 at: <https://ekrcis.financnasprava.sk/isstinet/Tools/HomePage.aspx>]

⁹⁸ Finančni Sprava [accessed online on 10.04.2019 at <https://www.financnasprava.sk/sk/podnikatelia/clo-obchodny-tovar/vyvoz>]

4.3.2 Import Obligations

Based on the recommendation given to Lesprodukt, no obligations for importation should arise, as all of these should be covered by the agent or buying company. In case the Chinese agent would not be able to conduct the importation process, hereby brief outline of the process and most importantly all the organizations involved is provided. The main issue with Chinese importation is that you have to find a partner who already has established company with importation license issued by MOFCOM, or start your own WFOE or Join-Venture company and ask for such license.

As of today, all companies who are registered at MOFCOM or any other authorized office in compliance with Foreign Trade Law is allowed for importation after obtaining license from MOFCOM. Brief outline of such a process is described in Chapter 3.

Once the company is registered and obtained license for importation, it must approach CCCPIT in order to provide them with all the necessary information for approval of the importation. These documents are the same ones as stated above in the exportation part, where a stress is given to origin of goods, especially in timber industry, as China, namely SFA with cooperation of MOFCOM and FMPRA, has started a campaign against illegally logged wood. Here comes the benefit of Lesprodukt as a holder of FSC license, which proves not only the origin of the timber but also the sustainability of the forests. This license provides to a Lesprodukt a higher demand of the wood, especially in current trend markets where sustainability plays a major role. Furthermore, CCCPIT provides trademarks, and CCC licenses for approval that goods imported into the country meet the domestic standards. However, as for all timber products, there is no requirement of CCC mark.

Considering exportation, HS code is very important in communication with all state organizations concerning importation, and mostly duties and tariffs. As of now, China does not have any tariff quotas on importation on HS products starting with 44, meaning any timber products. Considering tariffs, China does not impose any tariffs on any raw wood (excl. bamboo) and its forms (wood pallets etc.) from members of World Trade Organization, which Slovakia is.

As for the whole HS 44 group “Wood and articles of wood; wood charcoal” the simple average of MFN tariff rate is around 3.31% and is applied ad valorem, however these tariffs do not apply on anything but charcoal, that could be possibly imported with country of origin being Slovak Republic.⁹⁹

For the calculation of tariffs, duties and taxes, it is necessary to provide the customs with customs invoice, which has been described earlier in this chapter. According to this the amount of duties is calculated and VAT if applicable of 17% is taken into consideration.

4.4 Negotiation Ethics

Negotiations and cultural differences, as mentioned in Chapter 3, are closely linked to international business and play an important role in any business operation on the market. I believe that it is important to give an insight to Lesprodukt on the main cultural clashes in order to understand their potential business partner in more depth, and potentially to avoid any possible disputes in future arising from such differences.

When engaging in negotiations in China, it is very important to keep in mind the Chinese way of introduction and cultural differences. When talking about introduction, it is recommended in China to come with a team and preferably with older or senior member of the company, it is not usual for Chinese negotiations to be taken between four eyes. Once reaching the point of introduction, it is important to have business card written in Chinese and English, and most importantly to respect the custom of giving and receiving the business card. It is important to give / receive the card with both hands and closely observe the obtained card. This card should never be put into your pocket or briefcase, it is a custom to keep the business card on the table.

It is also important to note, and be prepared, for the difference in talking distance. Chinese tend to stand closer than Europeans, while engaging in conversation. It is important to keep this in mind, to avoid any awkward moments which could arise from Chinese partner keep coming closer, and the Slovakian partner to keep stepping back.

⁹⁹ World Trade Organization, „*Tariff Averages*“, [accessed online on 17.03.2018 on: <http://tao.wto.org/report/TariffAverages.aspx>]

Giving small gift to the partner works as a nice gesture. Gifts work as a great way to establish stronger relationship with your partner. It must be kept on mind that it is against Chinese culture to accept gift on the first time, so it is necessary to gently insist on acceptance of the gift. As a recommendation for a gift, a fine bottle of wine or some other alcoholic beverage is a preferable choice of gift.

Another specific of the Chinese way of negotiation is the length of these negotiations, unlike in European countries, they can be very long taking and exhausting. This negotiation strategy is frequently used by Chinese partners. Europeans are generally used to going straight to the main key issues of the deal and get over with the meeting as soon as possible.

Chinese, on the other hand, feel the stress and pressure put on the European partners during these long negotiations, and therefore uses the length of negotiations as a pressure creating strategy in which they expect their partner to give up and accept their conditions. Moreover, this pressure is supported by the gap between their answer to a question, or any response, which feels very unnatural to Europeans (with exception of Scandinavians). Therefore, it is recommended to take these habits into consideration, and to be frustrated nor been put under pressure from the time taken.

As already previously mentioned in the text, China is a high context country, which means that they rather avoid saying the message straight away, but they incline on the complexity of the situation in which the message has been said. Recommendation to avoid having issues of being perceived as rude or impolite is in trying to respect Chinese way of communication in comparison to Slovakia. It would be absolutely unacceptable, in case a member of your or the opposite party would cause a dispute to directly blame the person for the issue which has arose.¹⁰⁰

Dispute settlement for negotiations in Chinese culture is to be covered next. Firstly, it is essential to understand that word “no” is impolite to use in China. It is very common that Chinese people use variety phrases to avoid saying no for example, saying “I need to think about it”, “possibly”, or “maybe”.

¹⁰⁰ Bočánková M., a kol. *Intercultural communication: typical features of the Czech, British, American, Japanese, Chinese and Arab cultures*. 2. přeprac. vyd. Praha: Oeconomica, 2010. 152 s. ISBN 978-80-245-1648-6

Understanding this principle give us knowledge base in to be able to avoid the initial cause of a dispute. However, when the conflict arises, collectivist cultures are less prominent and keen on targeting the problem directly.¹⁰¹ It was discovered that collectivist countries, such as China, tend to seek for advices and approval of the solution from their surroundings.

As mentioned earlier, it is unacceptable to make a decision based on one's approach, as collectivist cultures seeks the most beneficial solution for the whole group, rather than an individual. With this bearing in mind, accepting the culture and their way of settlement dispute system, rather than be pushing others into executing fast decision.

This fact can be used in favour of Slovakian partners, as once they understand the importance of relationships, rather than goal orientation of Chinese people, possibility to establish a strong relationship with target partners arises. Expectation them to make decisions based on benefit of the whole partnership, rather than their personal profit should be kept while dealing with Chinese culture.

¹⁰¹ Ohbuchi, K. I., Fukushima, O., & Tedeschi, J. T. (1999). *Cultural values in conflict management goal orientation, goal attainment, and tactical decision*. Journal of Cross-Cultural Psychology, 30(1), 51-71.

Conclusion

The aim of this work was to determine to what extent is it viable for Lesprodukt to export timber from Slovakia to China, where focus was placed not only on the Slovakian partner, but the viability of Slovak economy in terms of long-term sustainability was discussed through macro-economic indicators. Major part of this work, was the basic description of timber market, which was described from view of logging company, where description of regulations and key principle of the market were provided, and from a more of a business view later in the thesis.

Stability of the domestic (Slovak) market was proven by stable GDP growth over period of six years, where the GDP growth was kept in boundaries between 1.80 – 4.00%. Further, the viability of the exporting partner was proven through Graph 2, showing the recently stabilised inflation rate, which resulted in deflation. As for Chinese partners, deflation is beneficial as exports becomes more profitable, due to the comparatively cheaper price of products on foreign markets.

Furthermore, the strong support of governmental and non-governmental organizations, promoting international trade not only with China, was described. Surprisingly Chinese market has been promoted heavily on the market, and organization cooperating with Czech Republic in order to increase the competitiveness of these economies, was established (CSKS). These organizations play a major role in establishing partnership, in support of perfecting the business plan, and most importantly in obtaining information about the Chinese market, which are not easily accessible, compared to information about European and US market.

From all information stated above, conclusion that Slovakia is a viable partner for long-term relationship can be drawn. However, as mentioned earlier, this conclusion is made based on an assumption that political situation is stable in the country.

Timber industry was investigated from the viewpoint of a logging company in the first Chapter, where the explanation of grading categories and basic overview of types of wood was given. A brief introduction to the importance of sustainability in the forestry market was given, so as the basic principles of forestry management, from which realities that the business is not aimed only at profitability, but also at the importance of the ecosystems were raised. The most shocking finding was the assumption that 10-30% of the lumber traded in the World is coming from illegal logging. Importance of so called calamity loggings and issues arising from them explained problematics of logging planning. Surprisingly, Slovak and the whole European market with wood is facing a decline in market prices, this might be caused by the Role of European union as described earlier. The support given by EU to promote forestry industry in order to produce more biomass for the newly planned power plants for renewable energy sources, may be the reason of oversupply on the market, which may have caused the decrease in prices.

Second chapter was focused on stability of Chinese market, its future potential, and current relationship among these two economies. As described in overview of the economy, GDP of the country has been on a rise with a stable growth, which suggests a stable economy. The interesting points to conclude about general market of China are that the country has a decreasing unemployment, which is however measured in a non-trustful way and new policies by the general secretary of the country on tackling issue of poverty. As said earlier, timber market is correlated to the real estate development, and due to this decrease of poverty may result in further increase of currently high demand of timber in China.

Continuing to elaborate on the point of the conclusion in previous paragraph, the demand might be even increased due to the new Russian regulation of exports of timber. Russia has been the largest exporter of wood to China and therefore the new regulation will cause a distress on supply side of the timber market. China's dependency on timber lies in the fact that it is the largest exporter of furniture and plywood in the World, and the insufficiency of the forest production domestically is not cause only due to acceptance of Natural Forest Protection Program, but also due to the natural conditions for growing trees. This demand of wood causes a large market price on all of the 18 largest markets with timber in China, as seen on the table provided in Chapter 2, there is a large difference among prices in Slovakia, as shown on Graph 3.

The following chapter was considering the theory and some of the practical applications of key factors in international business operations such as: ways of penetration, where potentially applicable ways for small to mid-size companies such as Lesprodukt were discussed; payment methods for most secure transaction; and other important contractual conditions, were discussed. Furthermore, the cultural differences in terms of individualism and collectivism were explained. This chapter was aimed mostly as a theoretical part in order to be able to fully understand the following chapter with recommendations for Lesprodukt, and to research the most suitable methods for the company.

Last chapter was focused on specific process and recommendations tailored for Lesprodukt, however this research and advises can be used for any small to mid-size company seeking to conduct such a business. An overview of the company was provided, and future evaluation on production capacity of the firm was given. Important information about the company regarding the FSC certificate was discovered, which further improves the demand for wood coming from Lesprodukt, as this certification provides proof of legality of the wood. As mentioned earlier, China has started a campaign against illegal timber, which may cause a decrease of the overall supply of timber on the market as 10-30% of traded timber is assumed to be logged illegally.

The conclusion on creation of partnership, including outsourcing most of the obligations through partnership was stated, as the obligation with such a relationship, especially when the agent or representative is also a licensed importer, are much lower than when the small to mid-size company such as Lesprodukt would be able to cover.

The description of all the necessary actions required in order to be successful in exportation of timber from Slovakia were researched and described. Usage of letter of credit was recommended to the company, due to the high level of security as there is a major involvement of banks in the process. As an alternative, bill of exchange, was suggested due to the simplicity of such method and the option of reselling the receivable prior to the payment due day to a bank, or any third party without noticing the drawee.

Furthermore, practical business negotiation recommendations were given and the topic of local customs connected to gifts was briefly described.

Final conclusion, based on the factors researched in this work and the discovered realities that it is viable for Lesprodukt to enter into Chinese market. This conclusion is supported by factors such as newly applied exportation quotas of Russian exports for timber, by the ongoing large demand for timber due to the Chinese production of many products from wood, not only furniture, and due to lack of domestic wood and its variety in China. Thorough research and investigation of the most suitable way of conducting international business operation with China was provided. This researched suggested that establishment of partnership is most suitable, due to the size of the company, and due to the long-taking process of establishing entity in the target market. Moreover, recommendations on finding the most reliable partner were given, with consideration of contractual conditions.

On the other hand, this thesis has not spoken about financial models and factors in exportation of timber into China, and it is for every company seeking to conduct such an operation to conduct them themselves, due to many confidential internal factors affecting the profitability and other external factors such as amount of exportation and others.

This research has shown that there is a possibility and capacity for Slovak companies to expand into Chinese market, and should provide such companies with a basic overview of the processes required in order to conduct a successful international business operation.

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