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PRESENT CONDITION AND OUTLOOK

FOR POTASH DELIVERIES FROM RUSSIA AND BELARUS :

PRODUCTION, LOGISTICS, MARKETS

by

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Good afternoon, Ladies and Gentlemen,

First of all I would like to thank the organizers of the IFA Production and International Trade Conference for inviting me to address you. I am very pleased and honored to be here today (Chart 1).

I. Introduction.

Potash ore is a rare natural resource. Potash production is highly concentrated in a few countries of North America, Europe and Middle East. Canada and the Former Soviet Union (FSU), namely Russia and Belarus, presently have 85% of known economic reserves. These regions also account for two-thirds of world potash production capacities.

II. Development of potash industry in the USSR.

Two potash ore deposits are exploited presently in the FSU: Verkhnekamskoye in the Urals in Russia and Starobinskoye in Belarus. These deposits combined are the second-biggest reserves of potash ore in the world.

The primary potash production in the FSU countries is carried out by JSC “Uralkali” and JSC “Silvinit” in Russia, PA “Belaruskali” in Belarus. Together the enterprises account nowadays for 12 million tonnes K_2O or 33% of total world potash capacities (Chart 2).

Initially potash industry of the FSU was developed to cover the demand on the internal market and supply the members of the COMECON (Chart 3). In 1988, when consumption in the former Socialist bloc countries reached its peak, it exceeded 10 million tonnes K_2O amounting to 33% of the world total.

The share of the FSU producers in the potash market of the East Europe amounted in 1988 to 62% or almost 2 million tonnes K_2O (Chart 4). The rest of volume was supplied by former German Democratic Republic. Export played a very minor role in the combined output of the 3 potash enterprises in the FSU - slightly more than 1.5 million tonnes K_2O were delivered to offshore markets (Chart 5).

III. Influence of transition period on the potash industry of Russia and Belarus.

Dissolution of the socialist system and later of the Soviet Union, economic changes in the countries of Eastern Europe and the FSU due to transition from state plan to market economy led to profound changes in the consumption of fertilizers, including potash. In a very short period of time consumption on the domestic market and in East Europe declined drastically by 5 times (Chart 6).

Capacity utilization dropped below 40%. Potash enterprises with 50,000 employees were on the edge of survival. The only possible solution to keep production on stream was export. But to replace the volumes lost in the domestic market with offshore deliveries both Russian and Byelorussian enterprises were obliged to overcome a lot of obstacles and resolve numerous problems to increase their competitiveness in the world potash market.

The most logical and natural solution was to increase sales in geographically close and mature market of West Europe.

Here the suppliers from Russia and Belarus encountered a competitor represented by the united German potash industry. Unfortunately, due to numerous trading channels, we failed to find any appropriate solutions. As a result, one of the biggest and most profitable markets was closed for the Russian and Byelorussian potash fertilizers by anti-dumping barriers.

We came across the same problem in the USA. But there we managed to find a solution without the introduction of protectionist measures.

IV. Main targets of potash enterprises after the USSR.

In order to work efficiently in the offshore markets of Asia, Africa and Latin America the enterprises had to resolve problems inherited from the USSR:

1. Undeveloped logistical infrastructure;
2. Narrow range of products;
3. Insufficient quality of goods.

1. There was only one specialized potash terminal in the port of Ventspils in the Soviet times. Small lots of product were delivered through the terminal in the port of Nakhodka, which was destroyed by a natural disaster.

During the past years the logistical situation has considerably improved.

a) Port of Ventspils (Baltic Sea). The annual transit shipments capacity of the “Kalija Parks” terminal at Ventspils totals 7.5 million tonnes of product. Current covered storage capacity has increased up to 140,000 tonnes of product.

b) Two terminals for transit shipments of potash fertilizers have been constructed in the seaport of Nikolaev (Black Sea). New storage facilities are being constructed nowadays.

c) Port of Vostochny (Far East). A terminal with a transit shipments capacity of more than 2 million tonnes of potash and other fertilizers was inaugurated in 2001 (Chart 7).

d) Port of St. Petersburg (Chart 8). The Baltic Bulk Marine Terminal (BBT) was put in operation in December 2001, and the second terminal line was inaugurated in February 2002. The annual transit shipments capacity of the terminal amounts to about 6 million tonnes of product; its storage capacity exceeds 250,000 tonnes of product.

e) Port of Klaipeda (Baltic Sea) is also being developed. Nowadays its storage capacity amounts to 120,000 tonnes of product. Construction of additional storage facilities is being carried out.

It is worth to note that our smart potash producers have developed port infrastructure not only for their products but also for other types of fertilizers.

The logistical facilities were being developed in correlation with the growth of exports. A lack of rolling stock impeded stable deliveries of volumes required. The distance from the Russian enterprises to the ports of the Baltic and Black Sea amounts to 2000 km, and to the port of Vostochny – 7000 km. The distance from PA “Belaruskali” to the ports of the Baltic Sea amounts to 1000 km, and to the ports of the Black Sea – 2000 km.

Due to the shortage of the rolling stock of the state railways of Russia and Belarus the enterprises were obliged to acquire or lease specialized railcars to carry out potash transportation. All the enterprises have made considerable investments in the purchase of the specialized hoppers as well as in the leasing of additional railcars when necessary. Nowadays the potash enterprises have their own rolling stock for potash transportation. The product is delivered to ports in specialized railcars, which return back empty, guarantying that the quality of the product does not deteriorate during transportation due to foreign material left over from previous trip.

The enterprises have invested in the production of a new advanced mineral hopper car to increase their rolling stock.

2. Quality. The main principle of the socialist economy was fulfillment of quantities stipulated by the planning order frequently at the expense of quality. When we started to develop our exports, we understood that the quality of goods was requiring a continuous improvement. Unlike deliveries in the domestic market of the USSR, numerous transit shipments and storages during the transportation as well as climatic conditions of importing countries put additional requirements on the quality of product.

3. It was necessary to take into account that our numerous customers worldwide have their preferences in respect of color of product, its granularity and other quality characteristics. Today the enterprises produce 11 grades of potash fertilizers including chemically pure and reactive potassium chloride. JSC “Uralkali” has initiated the production of SOP and potassium magnesium sulphate.

V. Current condition of potash industry in Russia and Belarus.

Summarizing the above-mentioned points, we can affirm that today potash enterprises of Russia and Belarus have developed logistical schemes and their products that correspond to the world quality standards. The range of goods meets the requirements of customers.

We believe that our export volumes of 6.5 million K_2O in 2002, which provide an average capacity utilization rate of 70%, are optimal (Chart 9).

Potash exports from Russia and Belarus were increasing gradually in correlation with the world consumption trend, and sometimes, maybe moving a little faster, but we have always sought to keep stability in the market (Chart 10).

The geographical structure of our sales reveals current trends of the world potash market. A higher increase of demand is registered in Asia and Latin America. In North America and Europe the consumption is stable or even decreases slightly. We deliver our product in more than 60 countries worldwide (Chart 11).

As we have mentioned above our export volumes depend on the world potash demand. A gradual growth of potash exports from Russia and Belarus registered for the last 10 years was mainly due to a continuous increase of deliveries to the countries of Asia, Latin America and East Europe (Chart 12). These regions are constantly increasing potash consumption in order to improve volume of agricultural production and feed the growing population.

World potash consumption increased by 4% in 2002 compared with 2001. However, the growth rate in many countries of Asia and Latin America exceeded considerably this rate. Both Russian and Byelorussian enterprises have consolidated their position as major suppliers to the world potash market. Diagram 13 shows the share of our exports to the biggest developing markets in 2002 (Chart 13).

A slight decrease in deliveries to West Europe and Africa was more than offset with the growth of exports to Asia, Latin America and East Europe. These volumes increased by 6%, 7% and 5% respectively in 2002 when compared with 2001. If we take a look at the geographical structure of the FSU deliveries we can see that the bulk of exports goes to the markets of Asia, Latin America and Eastern Europe. These regions accounted, respectively, for 57%, 15% and 12% of the total potash volumes sold from Russia and Belarus in 2001 (Chart 14).

Markets in Africa, North America and West Europe consume relatively low volumes of FSU potash due to different reasons. For example, as concerns the EC countries the product is delivered only for inward processing due to the anti-dumping measures against the FSU producers, unfortunately still in force since 1992.

We believe that FSU producers have achieved optimal sales volume in accordance with the market requirements and economic condition of the enterprises. Now the main challenge is increasing the sales efficiency of the potash industry of Russia and Belarus.

Russian enterprises are privatized. The enterprises are joint stock companies, they do not get subsidies or any support from the State. PA “Belaruskali” is a state enterprise, but the terms of its functioning are similar in many aspects to the Russian enterprises. All enterprises use export revenues for energy payments, which are growing permanently. We can say the same about railway transportation as well as sea transportation. The enterprises invest their money into the modernization of production, maintenance of ore base and laying of shaft cavities. Considerable part of the revenues is spent for the development of the transportation infrastructure: purchase of carriages, terminals’ arrangement, etc.

VI. Problems and aims of potash enterprises of Russia and Belarus.

We may conclude that in the present situation our major goal is to maintain profitability of the enterprises for production’s renovation and to continue working on improvement of servicing our clients by increasing quality of the goods and enlarging range of products.

However, the situation may change. Very soon we'll be faced with another problem. From May 01, 2004 a number of countries of East Europe and Baltic States will enter the EU. Now sales volumes of Russian and Belarus product in this market amount to 800,000 tonnes of K_2O or 87% of total consumption volumes.

From the moment of accession of these countries to the EU, the EU regulations and directives in force, including anti-dumping measures, will be fully implemented in these countries. The level of anti-dumping measures imposed makes impossible for the enterprises of Russia and Belarus to continue supplying the goods to these countries.

Thus, we see a dilemma: to loose these volumes or to substitute them with deliveries to other markets. Decrease of export volumes by nearly 1.3 million tonnes of product is a huge financial loss for the enterprises. Deliveries to other markets, more distant geographically, will increase transportation costs on the one hand; on the other hand, these volumes are not supported by corresponding growth of demand, which may cause destabilization of the world market. Of course, the optimal solution is a repeal of the anti-dumping measures. Anti-dumping duties have been in force for an unprecedented long period of time - 11 years. In our opinion, there is no economic justification to keep these measures in force. At the time of their introduction the reason for imposing anti-dumping duties was due to chaotic and uncontrolled deliveries of the Russian and Byelorussian product, but nowadays sales are regulated and predictable.

Production in the EU countries at the functioning enterprises is not growing and production capacities have been reduced. Next year the following situation could emerge: there would be a shortage of product in the enlarged EU and in the other regions of the world there would be a surplus of the product. It could lead to destabilization of situation in the world market in general. To my strong conviction destabilization is profitable neither for producers nor for consumers who are interested in stable supplies and predictable expenses as well.

What can be an alternative if the anti-dumping measures in the EU are not cancelled? In our opinion, there is no alternative.

We hope that the IFA and its members understand our position, share our anxiety and will render assistance in our efforts to eliminate anti-dumping measures in the EU.

Thank you for your attention.