



The effects on international road freight transportation of the protectionist policies concerning the truck manufacturing industry in Belarus

Summary

This paper discusses the protectionist policies concerning the truck manufacturing industry in Belarus and its effects on international road freight transportation. The major impediments to furthering the national road carrier network are discussed and recommendations are given on how to increase competitiveness.

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1. Introduction

Geographically and historically, Belarus is a key transit country between Asian countries, Russia and Europe. The export of transportation services thus plays an important role in the Belarusian economy. This is proven by statistical data: the share of transportation services amounts to 55% of total service exports (2005).

The major part of the revenues derives from delivering products via pipelines (oil and gas), railways and roads. It should be noted that Belarusian road carriers cover not only the domestic market - their transit capacities supply outside markets as well to deliver services to customers, such as between European countries or within the Russian Federation. This sector is almost totally privately owned and started to develop just 15 years ago achieving capacities it had never had before. International road freight transportation has proven to be a very promising export sector where Belarusian firms can have a clear competitive advantage over foreign firms.

Yet the state's policies since 2003 have been leading to decrease in competitive advantage of the Belarusian road carriers and to a deterioration of the sector. The further development of the sector depends strongly on the government understanding of its specificity and its problems as well as on appropriate regulatory policy.

The statistical data throughout this paper covers only international road carriers using TIR procedures (Transports Internationaux Routiers), which constitute about 90% of the overall revenues from international transportation. Hence, the actual overall numbers should not be very different.

This paper reviews the introduction of duties and its effects on the national trucking industry (part 2), analyses the effects of the protectionist measures on road freight transportation (part 3), discusses the importance of international road transportation for the Belarusian economy and certain other impediments to its further development (part 4 and 5). Final remarks and policy recommendations can be found in part 6.

2. Protection of the Belarusian truck manufacturing industry

2.1. The protectionist measures

Nearly 40% of all trucks used by Belarusian transport companies are leased from foreign companies. The old laws did not levy any customs duties on imported trucks and semi-trailers as long as they were used for international transportation. These vehicles were imported under a so-called "temporary import regime". Since May 2003, after the Council of Ministers adopted Resolutions of №406 and №677, companies have to pay VAT and duties, which are prohibitively high, especially for used vehicles. The duty rates are 5 to 10% for trucks not older than 3 years, but 50% if the vehicle is older. Moreover, the amount of the duty cannot be less than EUR 3 per cm³ of the engine's cylinder capacity. With an average engine capacity of 12,000 cm³ the average duty amounts to EUR 36,000, which is more than the price of a used truck. Almost no heavy trucks were imported into the country after this regulation came into effect, even though the duty can be paid in monthly installments of 3%. The same resolution makes it illegal for Belarusian firms to operate trucks registered in other countries.

Between 2004 and 2006 a number of legislative acts were adopted to prolong the validity of the 2003 Resolutions (see Table 1). Resolution # 1364 (19.10.2004) of the Council of Ministers lowered the duty to EUR 2.2 per cm³ but the resulting duty still exceeds the average cost of a used truck. Presidential Edict # 211 (04.05.2004) exempts non-residents from paying import duties for the first month of a vehicle's presence on the territory of Belarus, and also exempted Belarusian semi-trailers registered in other countries from paying duties. All this had no positive effect on the sector, however, as the number of international freight transportation carriers shrank by 13% and the number of vehicles used was reduced by 15% in 2004.

Table 1. The most important legislative acts regarding the import of heavy trucks to Belarus, 2003 to 2006

Document	Date	Major outcomes
Resolution of the Council of Ministers №406	26.03.2003	Import duty for trucks introduced (50% of the cost but not less than EUR 3 per cm ³)
Resolution of the Council of Ministers №677	22.05.2003	The "temporary import" regime is canceled
Resolution of the Council of Ministers №117	03.02.2004	Prolongs the Resolution of the Council of Ministers №406
Presidential Edict № 211	04.05.2004	Non-residents do not pay duties for one month; Belarusian firms can use semi-trailers registered in other countries
Resolution of the Council of Ministers №1364	29.10.2004	Minimal import duty decreased from EUR 3 to EUR 2.2 per cm ³
Resolution of the Council of Ministers №846	01.08.2005	Prolongs the Resolution of the Council of Ministers №1364
Presidential Edict №349	25.05.2006	Introduces 5% tariffs for imported Euro 3 trucks 3-7 years old, all other tariffs stay the same

2.2. The effect of the new import tariffs on the national truck manufacturing industry

The main justification for introducing high import tariffs on trucks was to support the national truck manufacturers, mainly Minsk Automobile Plant (MAZ). Obviously, this is both an important economic and social goal: the plant itself employs about 30,000 people. Yet the strategy to fill the domestic market with locally produced trucks failed completely: national road carriers bought only 260 MAZ trucks in 2004 and 75 in 2005. The reason is that operating an MAZ truck is more costly than a western European analog: MAZ trucks are less reliable, weigh more and consume more fuel. The cost of an average trip from Belarus to Western Europe with an MAZ truck may cost 100 Euro more than using a western-made unit. Moreover, European customers prefer to work with reliable transportation firms. Reliability is hard to achieve for any firm using MAZ trucks since service support is extremely underdeveloped for these trucks in Western Europe (unlike in the Russian Federation).

The national truck industry is export oriented: most of the trucks are exported to Russia and to Arab countries. The exports increased from USD 121 m in 2002 to USD 194 m in 2004. In 2005 export fell to USD 180 m (from 6863 to 5963 trucks in physical terms). Yet, during the first half of 2006 exports grew again by 30%. Compared to this large volume of exports, truck sales within Belarus have little impact on the national industry. Introducing the prohibitive import duties on trucks in 2003 have not had a measurable impact on the national truck manufacturing industry. The initial goal of the protectionist policy has not been achieved: sales of domestically produced trucks did not increase.

At the same time, the protectionist policy had immense effects on other branches of the economy such as road freight transportation. The effects of the policy on this branch will be discussed in the next chapter.

3. The effect of the protectionist measures on road freight transport

The measures taken by the government since 2003 to protect truck manufacturers have led to a substantial deterioration in the road freight transportation sector.

- The number of international road carriers in Belarus decreased by 850 between 2003 and 2006;
- The Belarusian cargo fleet for international transportation decreased by 40% (5500 vehicles). These vehicles were brought to neighboring countries (mainly Russia), Belarusian firms thus invested at least USD 150 to 200 m in the economies of these countries;
- The branch lost about 6000 work places.

- The share of vehicles more than 7 years old rose from 59% in 2002 to 72% in 2005. This tends to increase the costs borne by Belarusian road carriers and decreases their competitiveness.
- The quality of the vehicles is also a problem – only 31.5% of them pass the Euro 2 and Euro 3 standard. Since 2006 only Euro 4 trucks could be registered within the European Union. To compare, the share of Euro 2 and 3 trucks in Russia is 65%, in Ukraine 58%, in Lithuania 66%.

The Belarusian Association of International Road Carriers (BAIRC) estimates that Belarusian road carriers need to replace 1000 to 1500 trucks annually. But due to the unfavorable regulations only 490 trucks were bought in 2004 and 151 in 2005. During the same time, the Lithuanian and Latvian cargo fleets grew by more than 1500 vehicles each in 2005.

At first sight this hasn't led to a dramatic decrease in the revenues and service export inflows into the country. The unfavorable regulations did not lead to a decrease in the volume of service provided by private carriers. The volume of road freight transport service exports continued to grow in 2004/2005, though not as rapidly as in previous years (11 to 13% in 2004/2005 compared to 23 to 30% in 2000/2003). By comparison, the growth rate for railway freight transport service exports is 2 to 3 times lower. The taxes and fees payable by road carriers have grown too: their growth rate in 2004 was as much as 21%. This is surprising considering the drastic decrease of the production capacity (number of vehicles) of road carriers. The number of trips and the volume of goods carried dropped as well. The revenue increase was achieved by raising tariffs and by a nearly 50% improvement of operational efficiency: an average truck made 1 roundtrip a month in 2000 and 1.42 in 2005. Yet this reserve has come to an end already: during the first half of 2006, for the first time since 1999, the revenues from international freight transportation decreased by 1.1% yoy.

Belarusian firms have been losing not only markets in Western Europe and Russia but within Belarus as well. The share of international firms in the overall volume of goods carried to/from Belarusian customers was just 27% in 2002. In 2004 it was already 38% and in 2005 – 41%. The transit of Belarusian road carriers through Belarus decreased as well: from 185,000 trips in 2000 to just 95,000 in 2004.

With the drastic reduction in the number of imported vehicles the government lost a considerable amount of registration fees.¹ The reduced number of trips led to losses of tolls on the M1/E30 road, sales taxes on fuel etc.

Thus introducing high tariffs amounted to a net loss for the economy: the potential revenues lost by the road carriers and the state did not transfer to the domestic manufacturers. Without the negative effect of the government regulations, revenues and exports of transportation firms would have been much higher.

4. The importance of international road transportation for the Belarusian economy

The Belarusian government has declared export promotion to be a strategic goal. One advantage of transportation as compared to industrial and agricultural production is that it does not require large imports of raw materials and energy. A sound system of international transportation is essential for Belarusian producers since they use many imported materials and export a major portion of the goods they produce.

Road freight transportation services are provided by competing state-owned and private enterprises. The share of international transportation in the overall amount of services provided by cargo carriers is approximately 75%. The share of state-owned

¹ There is a registration fee for all vehicles in commercial use that amounts to 5% of the vehicle's cost.

firms in the overall volume of international freight transportation services is quite tiny - not more than 2%. State-owned firms are mostly engaged in in-country while private firms in international transportation. Small firms and individual entrepreneurs constitute the core of the business, operating up to 70% of cargo fleet.

The branch has been developing rapidly every year since the 90s: the total service exports rose from USD 26 m in 1993 to USD 288 m in 2005. During the period of maximum development in 2001/2002 there were 2500 firms and entrepreneurs on the market operating about 14,000 vehicles. What makes international road transportation so important for the Belarusian economy? There are at several reasons.

Promoting export

The branch is export oriented: only a small fraction of revenues comes from delivering goods to/from Belarusian firms. The biggest part derives from providing service between European countries and Russia. The share of road freight transportation in the total transport service exports of Belarus amounted to 24.4% in 2005 (13.3% of total services exports). In 2004 this share surpassed the one for railway freight transportation, which is provided by large state holdings that employ more than 100,000 people.

Developing small business

Small business development is of extreme importance for transforming a country like Belarus since it does not require large investments and absorbs some of the excess labor force. 43% of the firms operating in the international freight transportation market are individually owned. Almost 70% of these firms possess up to 5 trucks, and another 17% up to 10 trucks. Since the number of persons allowed to be employed by individual entrepreneurs is limited to two, half of the firms operate only 3 vehicles. The branch provides roughly 57,000 work places, many of them in the medium-sized and small towns, where unemployment and low salaries are common.

Attracting investment to the country

Small businesses like road freight transportation are easy to invest in, especially when a leasing scheme is used. Before 2003, 40% of the trucks were leased from foreign companies, using foreign bank credits. This is particularly important for Belarus, where private sector investment funds are in short supply. The trucking branch has developed without any state investment, contrary to such sectors as heavy industry, agriculture or railways.

Increasing government revenues

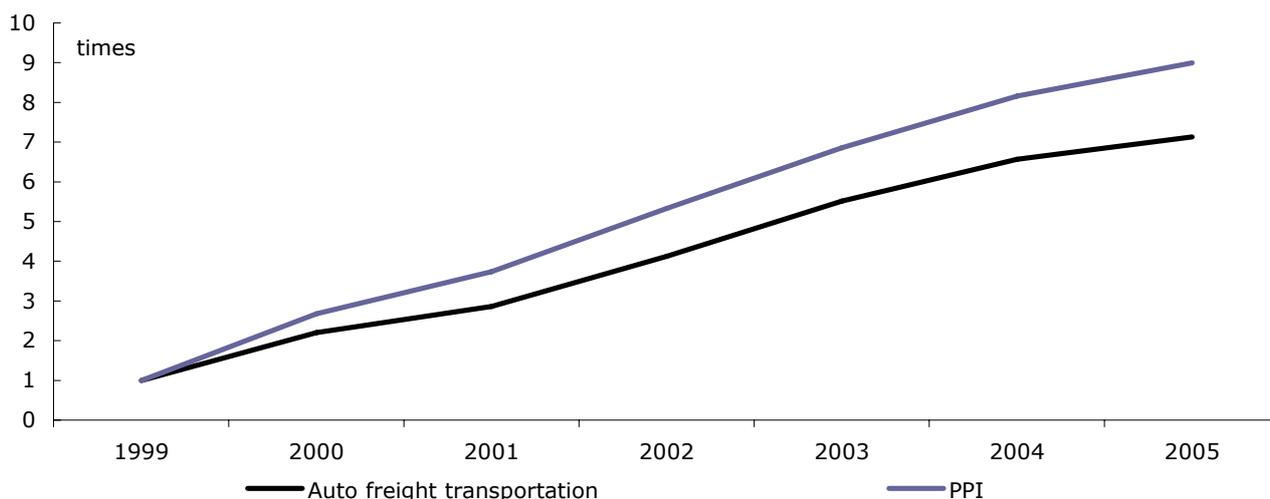
The average revenue for one roundtrip by a truck is USD 2800 to 3000, for which about USD 350 and 370 in taxes and fees are payable. International road carriers contributed BYR 78.7 bn (USD 36.5 m) to government revenues in 2005 in the form of taxes and fees (BYR 61.3 bn in 2004). These taxes and fees paid by the road carriers have grown from year to year.

Low fares due to high competitiveness

The high level of competition between the numerous private road carriers has led to low tariffs. As Figure 1 shows, the PPI index for the last 6 years exceeds the tariff index. This greatly benefits local exporters and importers that use road transport. Over the same time, railway transportation tariffs grew much faster than the PPI.²

² See Belarus Infrastructure Monitoring, 2004-2006.

Figure 1. Index of tariffs for road freight transportation and PPI



5. Other impediments to developing international road transportation in Belarus

Prohibitive import duties on trucks are the most serious obstacle to developing road freight transportation in Belarus. Yet, there are some other impediments that decrease the competitiveness of Belarusian road carriers as compared to firms in neighboring countries.

Complicated and expensive leasing schemes

Up to 75% of the Belarusian cargo fleet should be replaced during next 4 to 5 years. If not, Belarusian road carriers will lose competitiveness vis-à-vis firms from Russia and the new EU member states. Belarusian firms should acquire at least 1000 trucks annually. There are three major schemes to renovate vehicles: Purchase using the firm's own funds, obtaining a credit or leasing. Leasing seems to be the most acceptable way since it doesn't require spending one's own funds; also, additional collateral and lease payments can be included in the costs. Before 2003 up to 40% of the vehicles used in international transportation were leased. At present this figure is about 10%.

Leasing schemes in Belarus are still underdeveloped. The company "Mazcontractleasing" provides leasing for short periods only, Belarusian banks charge very high interest rates (12 to 16%) and they require collateral for 60 to 70% of the credit. The financial status requirements, which a firm has to meet are very high, and the procedures for obtaining credit are complicated and lengthy. For the majority of firms these conditions are unacceptable. In contrast foreign companies provide leasing for periods of 3 to 5 years, charging 7 to 10% annual interest and require no further guaranties.

High taxes

The tax burden in Belarus is generally heavier than in neighboring countries. For international road transportation, taxes amount to 9.2% of revenues, compared to 2.8/5.4% in Russia³, 4.2% in Lithuania, and 5% in Poland. High taxes make it harder for Belarusian firms to compete on the international transport market. The profitability rate⁴ of road carriers has decreased rapidly: from 5.1% in 2003 to 4.1% in 2004 and 2.2% in 2005. Excessive taxation also motivates people to hide revenues by engaging

³ Depending on the taxation system a firm is subject to.

⁴ The profitability rate is the standard indicator used in Belarusian statistics of the ability of a firm to generate profits. It is defined as the ratio of revenues to costs.

in all kinds of gray schemes. The most acceptable form of taxation for most road carriers would be monthly flat tax. The tax rate is easy to calculate on the basis of the average revenue per round-trip and costs. Most experts agree that it should be 180 to 200 Euros per month, which would represent about 5 to 6% of revenues. Moreover, firms and individual entrepreneurs would be treated equally.

6. Conclusions and policy recommendations

The protectionist policies to benefit the national truck manufacturers, which were implemented by the Belarusian government between 2003 and 2006 did not have any significant impact on truck production and sales, while the prohibitive import duties that were introduced as a part of these policies lowered the competitiveness of Belarusian road carriers providing service on the international market.

The competitiveness of the Belarusian road carriers depends on the ability of the government to create a favorable regulatory framework. High truck import duties give an advantage to the main competitor of road carriers: railway transportation. Firms residing in countries with lower duties (Russia and the new EU member countries) also benefit. The introduction of prohibitive import duties on trucks led to a net loss for the Belarusian economy. It seriously harmed the national road carriers and decreased government revenues without benefiting the national truck manufacturers.

It is recommended that the government take the following steps to make Belarusian road carriers more competitive:

- Restore the “temporary import” regime for Euro 2 and higher trucks and semi-trailers used exclusively in international transportation;
- Lower the import duties on trucks, up to 10 years old, to 0.5 EUR per cm³ of engine displacement;
- Introduce a flat tax for international freight transportation services replacing the present taxation system. The tax should amount to EUR 180 to 200 per month per truck registered for international transportation;
- Develop a sound leasing scheme for Minsk Automobile Plant (MAZ) trucks.

At the same time, steps should be taken to restructure the Minsk Automobile Plant to make MAZ trucks and buses more competitive on both the national and international markets. The quality and reliability of the vehicles needs to be improved and a network of service centers created. Privatizing the plant and selling part of the shares to strategic Western investors could achieve this.

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