

# MODERN TRENDS OF INDUSTRIAL POLICY AND ITS IMPACT ON RUSSIAN ECONOMIC SYSTEM

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**Abstract.** *The article is devoted to formation of the mechanism of the territories of priority development within the framework of contemporary issues of industrial policy, which is currently faced by most countries, including Russia; the article also identifies priority areas and trends of the government to accelerate economic growth by attracting investment in the industrial sector. It discusses different approaches and scholarly positions of a number of domestic and foreign economists regarding the desirability of one or another of industrial policy and its effectiveness. The article considers the conflict of inconsistency with some theoretical and practical aspects. It introduces the concept of inclusive economic development, which implies a new quality of economic growth. The author, drawing on the results of functioning of free economic zones in the Russian Federation, justifies the strategic importance of formation and implementation mechanism of the territories of priority development for the successful modernization of the industrial sector in Russia. The author has introduced the priority point of intersection of interests of state and business which is the need of the formation of the working mechanism of return of private capital. At the end of the article there is a brief conclusion reflecting the latest trends related to the Russian economic growth in the current difficult circumstances and its impact on tourism sector.*

**Keywords:** *economic development, human resources, industry, institution, investment, policy, sanctions, strategy, economic system*

## 1. Introduction

In the scientific community, there is a series of discussions on the feasibility of a particular industrial policy to maintain the economic growth, re-industrialization, modernization of the economy. Exchange of the views in a chess style has successfully clarified some of the pros and cons of the policies to promote the industry and upgrading its structure by presenting information from all sides of the dispute, and the fact that each party upheld its own well-reasoned position.

During the extensive research, some experts note that industrial policy was not necessary. The private sector, in pursuit of profit, will be able to determine what the comparative advantages of an industry are, and will invest this direction (Forbes & Ames, 2012). Others express the view that not many markets were capable to do it (Stiglitz, 1977). For example, the foreign investors may not know how to do business in a new location. Firms, coming to the market first – no matter, if they succeed or not – create the benefits for other potential investors. These rivals and followers get the experience and do not bear the costs related to the risk management. The result can be the most effective and optimal level of doing business, unless the state intervenes to tighten it up. Another example: in countries with a large amount of seasonal unemployment, most often, it is employed in agriculture; there is the fact

that the social benefits of the industrial employment may exceed the private benefit. Therefore, there may be a need to subsidize employment or investment outside the agricultural sector to compensate this gap. Some skeptical experts still recognize that markets are not always effective, but they prefer to argue that industrial policies were not working as well. This can be explained that governments did not have full information and understand what they should do. In other words, the state does not have a peer review to detect the objects for the profitable investments, and most of the resources are spent on attractive, but actually failed projects. Or, there will be more tragic situation, the state can deliberately undermines the procedure, handing out the benefits to their industrial allies. Of course, there is a significant variation in the competence level of the governments of the various countries and influence of special interest groups, including transnational corporations. On the other hand, the passivity of the government to promote industrial policy also carries the risks (Nevskaya, 2014).

## **2. Industrial policy in the modern conditions**

A prosperous industrial sector is a key component of high economic growth, especially in the early stages (Skryl, 2013). If the economy is not able to diversify a domestic production and create jobs in the new industries, the state should seek to find a way to dramatically push the process and act as a driver of the development. However, these efforts have to obey the certain rules. Firstly, they should be temporary, because the problems are not permanent also. Secondly, the measures taken concerning the modernization are necessary to think about and quickly coordinate them if the strategy leads to a significant imbalance of the economic system. If these measures do not give a desired result, the state should have an opportunity to promptly abandon them and continue the industrial policy in a different way. An example of one of these tools is the state measures, which usage can be justified if any production without them cannot be started, also the creation of the specialized free economic zones and the territories of priority development. If the industry is not able to keep going without them, it means that the initial industrial policy was wrong and ineffective institute should be canceled (Osipov, 2015, Evseev, 2016). Third, even though such strategies will gravitate in favor of the industrial sector of the national economy, in general, they should be neutral in relation to the rest of the industry. If it is possible, they should be indifferent to a particular production, leaving a choice to the private investors. Finally, it is important to note that the inclusive development of the modern economies in parallel with the modernization of the industrial sector embrace the other key ingredients of the growth - education, technology, flexible and efficient management, etc.

### **2.1. Effects on an tourist sector**

The recent state policy changes have affected not only the industrial sector, but the service sector as well. In particular, there have been dramatic changes in the structure of the tourism business. After the tragic events connected with the two Russian aircrafts, (civilian one in Egypt and fighter jet on the border with Turkey) Russian authorities have adopted a series of restrictive measures in the part of tourism sector. Since the autumn of 2015, the tourist flow to Egypt was closed due to the

increased terrorist threat. In January 2016, sanctions against Turkey were introduced, which spelled out a series of restrictive measures, including the reduction of mutual trade between two countries and the abandonment of the sale of travel packages to Turkey. On the one hand, these measures are anti-social, as these areas were some of the most popular among the population. Turkey and Egypt are very attractive for Russian tourists because of cheap, efficient and comfortable organizing tours. Nevertheless, if you look at the data limitations in terms of macroeconomic analysis, the huge demand for overseas tours creates additional demand for foreign currency, thereby lowering the price of the national currency in the foreign exchange market. Currently, the ruble is not in the most favorable situation, rather, that since the autumn of 2015 the national Russian currency has fell almost doubled because of the collapse in the global oil market. Many experts recognize effective sanctions imposed in the tourism industry. In this situation, when the most popular tourist destinations are closed, and the remaining overseas options for recreation scare their high cost, the rejection of foreign tourist destinations creates a momentum for the development of domestic tourism in Russia.

## 2.2. Institutional restrictions in the industrial policy

In the modern Russian practice, the weakness of the institutional environment and lack of a strategic definiteness reduce the planning horizon of the most decision makers, and the state policy becomes short-term, reactive (Osipov, 2015). Actually, in these conditions, the government should be a driver to start a modernization of the industrial sector of the national economy. The modernization directly aims at developing the economic potential of the Russian Federation, ensuring the production of competitive industrial products, development of non-commodity exports. It is important to note that the current trends of the economic growth in Russia should also be inclusive. Analyzing the different options of the industrial policy, implemented earlier in Russia and abroad, the most efficient variant is that one, which focused on the removal of the various institutional barriers to doing business. Currently, in Russia such mechanism works in formation of the territories of a priority development. As noted above, the modern state policy of Russia in relation to industrial modernization is operational (Silvestrov, Zeldner, Osipov, 2015). It is important to take into account the errors of previous, not very positive experience related to the projects, concerning the creation of the free economic zones. Most of them proved to be ineffective, because of the high level of corruption and lack of institutional infrastructures. Nevertheless, the experience of the foreign countries is represented very valuable to implement the industrial policy within a formation of the territories of a priority development. The priority task of forming mechanism of the territories of priority development is a creation of a business climate and infrastructure that could compete for the investments and labor resources on a global market. Accordingly, the main problems remain the same, the solutions of which were not found by the previous mechanisms (see attached pic.1).

Picture.1 Main problems of the industrial policy in Russia

# PROBLEMS



Source: Designed by author

A new law on the territories of the priority development more clearly defines the criteria for the resident's selection, details a legal aspect, which regulate the activity of the territories of the priority development and its residents (Osipov, Skryl 2015). The main difference between a new law from the previous analog is the emphasis on the public financing of the construction and maintenance of the future infrastructure, i.e., one of the main current problems of the industrial sector. This idea clearly holds E. R. Yescombe (Yescombe, 2002).

Despite the existing criticism of many experts, including representatives of state bodies, regarding the existing sufficient financial budgets resources to build the infrastructure from scratch, the main outstanding contradiction remains in the return mechanism of the private investment. Here need to emphasize that the mechanism of the territories of a priority development is a fundamentally new institute to improve radically the investment climate. The law defines the procedure for easy access to the power grid construction. This new law legitimizes the customs, tax and administrative benefits and concessions for the future residents of the territories of the priority development. In short, all above mentioned directive measures aim at attracting investment, both domestic and foreign. However, all investors are pursuing the same goal; not only competently and safely invest their financial resources, but also to get some benefit in the future, whether it is a guaranteed profit or ownership of the infrastructure, etc. (Osipov, Skryl, Nevskaya, Shavina, 2016; Skryl, 2014)

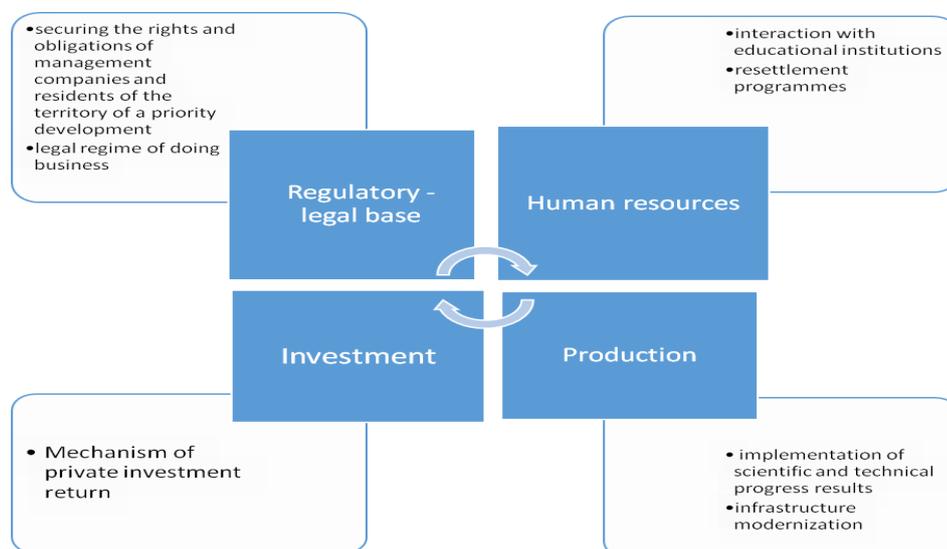
Another unresolved contradiction in the functioning of the mechanism is the human resources, acting here as a potential of the development. Firstly, we would like to emphasize the lack of the educational programs, links with educational institutions that could be directed to the training or professional reorientation of the labor force. Subsequently, the absence of a decision on this issue will lead to a shortage of Russian experts. A preparation of the professional experts takes a time, and this fact will increase the need to attract a foreign labor. Secondly, in order to improve the competitiveness of the existing work force at these territories, the state should make a local labor cheaper. The tax incentives, provision of free housing, as

well as the development of the resettlement programs and a creation of the favorable conditions for Russian citizens from regions with high unemployment can achieve it. The existing experience to motivate the labor force to move, as wage supplements, only leads to a rise in the labor cost, increase the investment costs and the main result is an unrestricted attraction of the foreign workers, especially from Asian countries, with lower wage costs. Third, during the implementation of the projects in the territories of the priority development, it is important to take into account the local specifics. It is meant a standard of living of the local population, the income and living conditions, the demographics and regional characteristics, which can have a positive effect on their correct use. In other words, any project should not be penetrate spontaneously, sharply, without an adequate training in the region and obviously not with an expectation of the instant results.

### 3. Results

There must be an institutional matrix to launch successfully the mechanism of the functioning the territories of a priority socio - economic development. Douglass North noted that institutional matrix should be as the formal rules and informal restrictions inherent in the behavior and values. Thus, using the method of formation of institutional matrix based on mentioned information, we offer the following option of the institutional. The principle of a strict interdependence of institutional-functional matrix elements does not allow the mechanism to disintegrate.

Picture 2. Institutional matrix of the creation of the territory of a priority development



Source: Designed by author

### 4. Conclusion

Nowadays the formal rules are fixed only for two elements of the matrix: legislative and industrial ones. The main issue and the actual goal of creating a territory of a priority development are remain open: how to improve the investment attractiveness of these objects. Because of this open issue, there is an informal restriction to create the territory of a priority development; there is no any mechanism

to attract a private investment to help starting the process. First, the state should develop a mechanism of returning of private investment capital. Any investor should make sure that he would not be an object of corruption schemes and the investment would bring a positive return. The next step is a need to establish the education resources and resettlement program to improve the competitiveness and reduce the labor cost.

As a result, if we compare the mechanism of the territories of priority development with the main elements of the investment attractiveness, it can be concluded that many of the provisions are consistent with each other, and above all have a common goal. The first point of interests' intersection of the state and business - it is a necessity to form of the working mechanism for the return of private capital. The private sector in the form of an individual entrepreneur or investor needs to see the transparency of the agreement, as well as from an economic point of view and from a legal as well as to be able to predict the result. The economy, which the government adheres to the current trend of economic modernization and industrial growth, should contribute to the development and implementation of the mechanism of territories of priority development, and comply with the rules defined in the institutional matrix of these territories. If the operation of territories of priority development is successful, the state receives significant savings of budget funds by attracting private investment, and business representatives are able to reduce their costs by obtaining various benefits and preferences. If we look at the implementation of the mechanism of territories of priority development in terms of economic development of Russian regions, raising their investment attractiveness and competitiveness depends on the rational use of their comparative advantages. Accordingly, the choice of development strategy issues are most relevant to contemporary regional economic policy in Russia. At the present stage the most attractive model is the mechanism of the territories of priority development, which is based on building partnerships government representatives at the federal level and the business using the market opportunities of the Russian Federation, as the possibility of generating new business opportunities for small and medium-sized businesses, as well as giving value-added products and employment in the national economy.

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