

# CRITICAL ECONOMIC ISSUES

*In the latest issue of the Journal we informed our readers about the 7th International Conference “Strategy and Tactics of Socio-Economic Reforms” that was held in December 2015 in Vologda. The event was dedicated to the 25th anniversary of ISEDT RAS. Renowned Russian scientists, chief editors of social science publications and representatives of regional and local authorities delivered their reports at the plenary sessions of the conference. The report delivered by Sergei Gubanov, Doctor of Economics, Professor, Chief Editor of the journal “Economist”, was considered to be of great interest by the conference participants. Here we outline the main provisions of the report\* touching upon the key issues that would help resolve economic and social problems that Russia is facing at the current stage of its development.*

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## System Prerequisites for Economic Recovery of Russia



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*As an opening remark, Sergei Gubanov noticed that all the speakers before him had described the current events going on in Russia as a stable crisis situation. The notion that the country is plunged into a state of uncertainty is becoming a popular trend. S. Gubanov pointed out: “I would call this idea the certainty of “uncertainty”. Why is it so?*

First of all, it is due to the fact that on the background of the modern neo-industrial development paradigm the formula of “vertical integration plus neo-industrialization” applies not only to Russia but also to the world economy as a whole. We can definitely say that industrialized countries are deploying high-tech or technological industrialization

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\* The overview of Sergei Gubanov’s report “System prerequisites for economic recovery of Russia” was prepared by Ph.D. in Economics Mikhail Sychev.

and digital industrialization that are combined with vertical integration – its systemwide foundation. And today one may talk of network integration. But it would be enough, if it were possible to provide at least horizontal and vertical integration.

Russia's development formula is as follows: vertical integration plus neo-industrialization. The above formula does not include the raw materials exporting model, and it was already obvious several years ago.

For instance, our publications on the situation of 2009 pointed out: if in the post-crisis period we still adhered to the raw materials exporting model, then instead of high growth rates we end up in the situation of lingering depression. According to estimates, in 2009, the real efficiency of the raw materials exporting model did not exceed 13%. Now its efficiency is equal to the arithmetic zero. What do these 13% signify? In 2000–2008, in dollar terms, Russia's GDP increased in about six times, and the real purchasing power of the budget, citizens and enterprises increased by a maximum of 27%, i.e. it has not even reached one third. This difference is a consequence of the petrodollar inflation – a parameter, which our country does not control. But the "raw materials export" game is a zero-sum game: when we sell oil, gas and other resources at higher prices, we buy equipment and other products at higher prices. Inflation of the petrodollar does not give us any advantage whatsoever.

In 2009, based on an analysis, we made another seemingly categorical judgment that there would be no raw-materials-based growth of our GDP in the post-crisis period under any circumstances.

We published interesting findings in January 2012. Pay attention that at that time there were no Ukrainian events, there was no Maidan, oil prices were high, there were no sanctions, Russia was not isolated from global refinancing markets, the situation was favorable from the view point of external environment. We executed our research at that period and, as it usually happens, together with the chief findings we obtained quite an interesting side result proving that there would be no second wave of a global recession in the industrialized world in 2012. But quite unexpectedly, according to the calculations, we revealed the threat of autonomous recession for Russia.

The analysis of empirical and statistics data carried out in mid-2012 showed that the estimate made in January had been absolutely correct. It had forecast what we witnessed later in December 2014. And that was the time when professional economic community started talking about the anti-crisis policy.

So, what do we have to deal with: the temporary cessation of export and commodity growth rates or the death of the raw materials exporting model? What do we see? If it is a break in growth, then this is a temporary, opportunistic and non-fundamental event. If it is the end of the raw materials exporting model, then it is necessary to shift to an entirely new development model. This does not mean the end of Russia; on the contrary, it is the end of the old and the beginning of a new model.

If in 2008, we were unanimous in the opinion that the 1998 situation would not be repeated, then, unfortunately, the current situation has created prerequisites for national

default. Its latent state can be traced by the inability of the government to meet its domestic obligations, for example, to public sector employees, pensioners, etc. The current rejection of full adjustment for inflation is nothing but partial default from the point of view of financial discipline. Budget default is nothing but a result of the default of the raw materials exporting model.

Therefore, from today's perspective, we are disputing with retroliberals – those who represent the viewpoint of the past. I mention them because they started to search for the origins of the autonomous recession in our country after it had become a fact. And we knew these reasons before the onset of the recession. This raises a rhetorical question: who has the right to develop anti-crisis measures: those who know nothing of the situation, or those who proved they understood it by anticipating it three years ago?

The proposals put forward by retroliberals are as follows: to carry out the shift from demand-side economy to supply-side economy. It seems reasonable: anyway, at present the government has no funds to support demand, so let us move on to the economy of supply, reduce taxes, remove support of many expenditure items such as defense and infrastructure, reduce social spending and spending on science. Naturally, supply-side economy, as viewed by retroliberals, is nothing but a banal throwback to the situation of the 1990s, when the entire export resource rent went to the pockets of oligarchs, and they did not support domestic demand in any way. We want to pay particular attention to the fact that all the arguments of retroliberals like Alexei

Kudrin, Alexei Ulyukayev and Evsei Gurvich are based solely on the myth about the absence of demand-side economy in Russia.

Does the entire growth of GDP in the first decade of the 2000s mean the growth of the total domestic demand in the country? If there existed the economy of demand, then everything that was added to GDP turned into domestic demand. If it is not so, then the arguments concerning the economy of demand is just idle talk. But how can this be checked? It is clear that it is necessary to consider another option – the amount that is deducted from this increase, i.e. the so-called net exports. Our calculations show that net exports over the analyzed period exceeded the growth of GDP; as a result, the aggregate domestic demand did not increase in proportion to the GDP increase, and it even decreased from year to year due to the outflow of capital, reservation, placement of funds in foreign securities and also because there was the exchange of commodities for non-commodities.

But what finished off the raw materials exporting model? It is neither the sanctions, nor oil prices or other external factors; it is a phenomenon that is called new industrialization of industrialized countries.

Sometimes we hear about re-industrialization in the EU, USA, UK. Unfortunately, in Russia, there is a considerable confusion in translated terms and one does not know exactly what it is. Sometimes you can hear an absurd interpretation that re-industrialization means the increase in the share of industry in GDP. This translation is not authentic. Industrialized countries understand re-

industrialization, first of all, as the antipode of financialization, i.e. the current situation when financial capital is dominant in the economic system and commands it. Re-industrialization means striving to restore industrial capital to its dominant position. This is the authentic understanding of re-industrialization in the U.S. and the Anglo-Saxon countries. However, this still does not cover the processes of development and progress that actually take place in industrialized countries, because these countries are implementing full-fledged automation and robotization of productive forces. The increase in the quality and share of automated workplaces is the first indicator of new industrialization. Over 25% of workplaces in the U.S. are automated. In general, today the number of automated workplaces in industrialized countries reaches 60%. This is new industrialization in action. In Russia, the level of automation is only 0.2%.

How did the EU's new industrialization bury our raw materials exporting model? Primarily through increasing the share of post-oil energy sources, because the process of new industrialization is connected with the transition from thermal hydrocarbon-based energy to post-oil energy. According to our calculations made in 2009, the present-day share of post-oil energy in the power balance of the European Union was forecast to reach 33–35%. Indeed, the European Union has already reached 33% of the share of alternative sources in the total electricity supply, which in oil equivalent means annual savings of up to 160–170 million tons of oil. The demand for Russian oil and gas exports decreased by this sum. It is clear that this includes processes

such as resources recycling, energy efficiency increase, etc. They smash to bits the former idea of turning Russia into an energy superpower.

I emphasize once again that the old economic system has no prospects whatsoever. It will not promote growth, no matter what we do. But this does not mean that our country has no development opportunities. The prospect of development exists, as well as resources and development potential, but we lack an economic system aimed to boost the country's recovery. We need to make the transition to an economic system designed for socio-economic recovery. This very transition will ensure Russia's development.

In connection with the above, Sergei Gubanov puts forward the following suggestions.

1. It is necessary to develop a long-term strategy for the new industrialization of Russia until 2020, rather than some vague Strategy–2030. Russia's productive forces should be rapidly automated. From the point of view of social structure this means an increase in the share of intellectual labor in the total distribution of social labor.

2. The government must ensure equal conditions for the development of both retroliberal and neo-industrial development programs. So far, administrative and financial resources are in the hands of retroliberals, and those who uphold the new industrialization have absolutely no opportunities and proper conditions for the development of a program for Russia's new industrialization. We advocate that both programs get equal conditions for development, for attracting specialists, organizing research teams, etc.

3. Today, the entire forecast model is calculated taking into consideration the input parameter such as the price of one barrel of oil. It is necessary to create another model of forecasting and planning that takes into consideration an input parameter in the form of hourly labor productivity and wages. It is a professional issue, and we know how to solve it.

4. It is necessary to hold a national economic conference on the system issues of new industrialization. It is a form that is flexible enough for the government leadership and also in a political sense on the eve of the electoral cycle. If the government leadership finds that not all the issues have been elaborated sufficiently, it can distance itself and say that this is a debate in the scientific community. If it decides that the issues have been resolved, it can proceed to

their nationwide implementation. Therefore, I believe that this form of discussion and adoption of system changes on the eve of the electoral cycle is quite productive.

These proposals can be implemented if the scientific and industrial communities obtain support from regional and federal authorities and if the relevant orders are made by the President of the Russian Federation. The President has given the task to update the Strategy–2020 to the wrong people and teams. This is what I mean when I talk about the President' other instructions on the issues raised.

These are the alternatives of the system choice. We clearly see the prospects for Russia's development, we have specific proposals and complete understanding of how to implement them.

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