

# OPINIONS, JUDGEMENTS, COMMENTS

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## «Postindustrial» illusions or systemic «neoidustrialization»: modern Russia choice \*



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Discussions on the problems of structural and institutional modernization of the Russian economy and the role of business and the government in this process appeared to be at second place in the face of harsh realities of the global financial and economic crisis, deeply affecting our country.

Of course, the problems associated with the support of the real sector and banking system strengthening, tensions reduction on the labor market require complex solutions, and coordinated action by the government and business. However, as evidenced by the history of world and domestic economy, the crisis comes to its end sooner or later, a new wave of economic growth begins, and as a rule, on a new industrial and technological basis.

The fundamental question is what this framework would be like in Russia, and what structural and institutional changes it will cause. Will the new industrial recovery become gradual stabilization of the result, whether the transition to a fundamentally different way delineated as “neo-industrialization” in the article by S. Gubanov happen, (“Economist”. № 9. 2008)?

According to the author of the article, system reconstruction of the Russian economy can not and should not be based on reckless of the plants of Western theory, which persistently and consistently insisted on the “post-” myth as alleged is clear, and the fait accompli. Besides scientific arguments are often replaced by adepts of western “post” Civilization by peremptory assurance of the inviolability of the current unipolar world economic system.

Statistical data analysis and conclusions in the article by S. Gubanov, indicate in favor of the fact that the global process of industrialization of the economy is still far from complete, despite the favorite argument of the “post-” mythology adherents that the share of services in the XX century became the dominant and almost determines the main vector of the modern civilization evolution. In fact, as amply demonstrated in the article, check reveals a completely different, really genuine fact: *the development of the major powers of today is moving through the production of capital goods rather than services.*

Moreover, the imperative of the modern stage of industrial development is an organic unity of science, innovative production and

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vertical integration of the corporate sector of the economy. That is, according to S. Gubanov, one of the objective economic laws in force in the highly developed economies which have reached a high level of socialization and concentration of production and capital.

This law, if you bear in mind the specific modalities of its practical implementation requires that the current profitability of the production of intermediate remained zero, a final economic effect obtained at the outlet of the corporation, would serve as a criterion for evaluating the quality of corporate governance in general. This is possible only if the re-based plants transfer pricing and contractual relationships transfer their products to each other in the chain not in order to maximize profit, but for the sake of common vertically integrated corporations end result – updated product range, improve its quality and competitiveness, building capacity for innovation, developing new markets and the accumulation of a corporate capital.

Just remember that the economic development of Russia was carried out because of the adoption of the model of privatization in the opposite direction. In the transition period, based on large and major industrial enterprises there appeared a lot of smaller private entities that have chosen the daily survival tactics at the expense of existing resource and production base, pulling apart liquid assets and extract the highest possible current income.

It is our conviction that the established adaptation economic model has been in the integral mainly only for small and medium-sized businesses, but only in those few industries where there were conditions in order to achieve short-term profitability and which are not urgently required to attract significant investment (trade, catering, personal services, municipal transport and communication, in part, housing). But this model has been contraindicated for big business.

*Focusing on the benefits of private capital and market-based mechanism for self-knowledge-and capital-intensive industries is clearly a failure.*

Since the beginning of reforms the state is largely lost the real levers of influence on technology and capital intensive production, and corporate behavior of the new property owners was basically a profit through the use of monopolistic market situation. And in the most advantaged position were those that received control over the most lucrative export commodity of the economy, producing intermediate rather than final products. Politics of spontaneous «adaptation» to the emerging markets, presented by ideologists of radical reform as a panacea for stagnating, went bankrupt, giving the race for a false purpose.

Domestic machinery, including electric locomotive building lost not only two decades, but much of the potential, which it had before the start of large-scale change.

The outcome of irrational, largely destructive economic rate of 1990's are very sad: it is not only a partial de-industrialization and the disintegration of the country's economy, the loss of many traditional markets of high-tech products but also managers' staff degradation who are not seeking to assume responsibility for the implementation of major investment projects.

As a result of such tactics of the Directorate industrial, financial and social activities of many enterprises and companies are deformed. In order to achieve the particular interests the companies are deliberately stocked to bankruptcy. Corporate Codes of Conduct adopted by many companies, are only to create an attractive image of the company in the eyes of the controlling authorities, while maintaining the resources pulling apart policy and hiding information. To this end, the leadership of the companies creates "friendly" companies, with which they conclude unprofitable contracts on behalf of society, on favorable terms production facilities are provided, equipment, electricity and raw materials, assets and profits are "pumped" to the accountable companies, money laundering and capital flight abroad are organized.

To act in this way is possible because of a lack of checks and balances subsystem in the corporate governance mechanism. Only responsible active industrial policy of state-based partnership with the business community can stop this catastrophic trend. S. Gubanov expressed its main core in the formula: “neo-industrialization plus vertical integration”. It is, as we see it, not so much in the theoretical component of the proposed paradigm, but in its sound practical sense, based on real experience of painful search for the way out of domestic firms from crisis deadlock.

In 1990s the giants of Russian industry, which traditionally have been developed on the basis of guaranteed state orders and stable sources of funding for R&D and mass production were in the most difficult situation.

Thus, the abolition of state orders has brought many factories, the giants of Rostov Region (Rostselmash, NEVZ, Taganrog, Krasnosulinsk, Belokalitvinsk metallurgical plants, etc.) to the brink of bankruptcy, creating a wave of layoffs a significant number of employees. A similar situation is repeated in these and other companies in the current crisis.

*The traditional self-supporting regime, inherited from the previous system, and indicating our businesses to maximize profits, drives skill- and capital-intensive production to a standstill:* companies are forced to curtail production of technologically complex products due to continuing growth in prices for all types of components, raw materials, electricity, fuel transport fares, etc. They are pushed to it by steadily declining demand for the ultimate machine-building products in the domestic and foreign markets.

The natural reaction at the situation where there is nobody to pay for a new, technically sophisticated and competitive products is re-production in favor of a more simple and inexpensive to manufacture products and, consequently, regressive institutional and financial restructuring of companies. As a result of this reorganization of joint stock companies,

focusing exclusively on the removal of current income, wins, of course, neither the state nor the majority of the population.

In this context, it is relevant and valid idea put forward by S. Gubanov of the need to reorient the strategy of the national economy in the course of overcoming the current crisis on a different vector of development. *Russia should not withdraw out of the crisis with the old archaic (export commodity) economy structure.* The country must come to the best stage of growth, with different priorities, different dominant values, and other strategic installations and institutions, other mechanisms for their achievement.

Russia really is on the threshold of neo-industrial development phase, which is characterized by the following features:

- ◆ accelerating restructuring of the economy, the transition from a predominantly commodity production to the production of high-tech, competitive end-use product;
- ◆ formation and expansion of modern innovation and industrial sectors with the subsequent release of their products to international standards of quality and reliability;
- ◆ decriminalization and debureaucracy of government, regional, municipal and corporate governance, training and promotion of management-based skills relevant to the terms and conditions of neo-industrial economy.

Which of the available or required in the future economic structures are capable of providing such a development? The answer to the question suggests the corporate practice of most developed countries, where rapid growth and progressive development of the economy are determined by the most significant scientific and industrial company profiles, i.e., the leading industrial corporations. In the United States, for example, there are more than three million of these corporations, which constitute 20% of the total number of American firms. They cover 90% of total sales of goods and services. However, not they, but only one hun-

dred largest corporations determine the status and international influence of the American economy. They account for 45% of the workforce and 60% of national investment.

Skeptics may argue that this structure did not save the U.S. economy of unprecedented crisis. However, in our opinion, the reason for the current crisis lies in the strains of modern financial and monetary system, as the crisis itself is not a kind of cyclical crisis of capital overaccumulation.

When the heads of the major nations of the world in which different models of a competitive market economy are long-established and entrenched, say with alarm that responsibility is more important than profit, one has to talk about the possibility of transformation, enabling radically alter the fundamental framework and modalities of the world economy. With respect to our country, we are less likely to threaten the foreseeable future crises overproduction of goods, if our industries will be able to develop import-substituting domestic production of mass demand, for which there is an enormous and far from saturated the market. Besides its size, no doubt, will rapidly increase in parallel with the process of neo-industrialization based on vertical integration of corporate structures.

Objective process of production and capital on the basis of the vertical integration of corporate relations for many industries is characteristic for the industrialized countries. Integrated corporations demonstrate unquestionable advantages over other forms of modern knowledge production. They are, at least in the following points:

- greater efficiency of production and economic activity through the increase in scale and impact on market sales;
- opportunities of complex scientific and technical developments, effective innovation and attracting highly qualified staff and use of modern marketing tools and instruments;
- a significant resource potential, its effective use and development.

Therefore, referring to the railway engineering branch, on the analogy there should be a powerful integrated electric center in our country that meets the requirements of today and tomorrow, that can successfully compete with the best European and Asian manufacturers of electric locomotives.

As you know, Novochoerkassk Scientific-Industrial Complex (VELNII and NEVZ) had and now has a unique position in the domestic market as the only country in the developer and producer of electric locomotives to thrust and has the status of our country's largest electric power. Creating at its base a vertically integrated corporation, the concentration of the state's and private companies' investments provide in the shortest possible time significantly (several times) to increase the production of electric locomotives, update equipment and technology, create electric rolling stock of the new generation and more efficient use of financial resources.

Leadership of industrialized countries in the material production is ensured not by mythical predominance of services in gross national product (GNP) and not by technothrone-specificity of the information structure of modern production *but by the increasing role of the powerful vertically integrated corporate structures*, covering all levels of reproduction cycle and capable of efficiently meeting the challenges of sustainable financing for R&D, design, development, mass production of the series, sales and postproduction service of products of new generation.

That does not detract from the role in the reproductive processes of modern means of searching, storing, processing, analysis and information transfer. These means of information and technologies may serve as a catalyst, accelerating the transition to the new stage of industrial development, but do not give an idea about the entire specifics of modern stage transformation of the global economy.

The mechanism of vertically integrated corporations functioning, based on a rational combination of the capacity of corporate strategic planning, market self-regulation and partnerships with the state, has, we believe, a particular importance for our country.

First, the tactics of survival alone has not lived up, it resulted in a number of cases to the disintegration of large research and production associations, with strategic importance for the country, and secondly, the development of the vertically integrated structure provides effective interaction with the country's external environment, starting from the markets of States abroad to integrate into the world market.

And this is understandable as foreign trade integration is not based on narrow-profile corporate commodity type. In essence, these companies have nothing to offer foreign partners in terms of long-term joint activities and strengthening of market positioning. They are interested in TNK and FIG solely as external partners, suppliers of cheap raw materials and hydrocarbons.

A new formula for the development of Russia, put forward by S. Gubanov in applications means the need for the development and implementation of the federal target program of the formation of vertically integrated public-private and public corporate structures, aimed at the creation, development, mass production and implementation of innovation products. Today's crisis gives us a certain time period for taking appropriate policy decisions and action in this direction.

Of course, vertically integrated corporations have not only the advantage. Like any complex institutional foundation, they are able to generate in the process of its functioning and the negative side effects.

The biggest fear in this regard is the traditional and possible tilt of integrated corporate structures to limit competition and reinforce monopolistic tendencies. However, one can not help but notice, the other side. Large vertically integrated corporations at the expense of profitability in the regulated regime about intermediate levels reduce transaction costs throughout the processing chain and thus increase the efficiency of the ultimate innovative products.

Innovation-based companies are well positioned to focus the scientific, industrial, natural resources, financial and human capital,

increasing the speed and scope of its expanded reproduction. As part of such corporations new opportunities to optimize the costs of intermediate products, improve quality and competitiveness of products of final consumption appear, which is essential for all companies seeking to acquire transnational status.

In other words, on the basis of vertically integrated corporations development economy may get the most advanced modern forms of management of the national economy.

It is also apparent that large vertically integrated companies do not arise without active state support. Our State which lost ability to influence the private business effectively and be responsible for macro-economic processes during the period of liberal romanticism is now trying to use all the traditional regulators. Given the strategic challenges, the state has no right to limit by the urgent measures of financial recovery of the corporate sector, aimed at maintaining the liquidity of banks and companies, curbing inflation, preventing massive bankruptcies and rising unemployment, social support for disadvantaged groups.

It is necessary to make substantial adjustments to the recently adopted (October 2008), but because of the racing events already outdated Concept of long-term socio-economic development of the Russian Federation until 2020 as soon as possible, set for the near term several priority technologies and industries, which can develop rapidly in the private-public and public vertically integrated corporations.

Breakthrough technology can be a versatile nanotechnology, biotechnology, life extension technologies, new medical technologies and other innovations that would be beneficial for investment, as catalysts for the transition to neo-industrial economy can be industries such as aviation, space technology, shipbuilding, transportation engineering, nuclear energy, etc.

This is a time of consolidation, time for responsible decisions able to bring the corporate sector of the Russian economy to a new neo-industrial development level.