

**D. E. Sorokin**<sup>a)</sup><sup>a)</sup> Financial University under the Government of the Russian Federation

## ECONOMIC THEORY, ECONOMIC REALITY AND ECONOMIC POLICY<sup>1</sup>

*This paper analyzes the opposition between the «liberals» and «statists» in the Russian political and economic thought. It demonstrates that the economic liberalization is an absolute prerequisite for the transition to sustainable socio-economic development. Such development must rely on investment activities of the state, which in the current circumstances is a necessary but not sufficient measure for reversing the negative trends. The negative developments can be prevented only through implementation, along with the institutional changes in the economic area that form a strata of economically independent entrepreneurs-innovators, of no less profound transformation in political institutions aimed at democratization of public life.*

**Keywords:** economic theory, economic policy, social and economic development

«... the ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood. Indeed the world is ruled by little else. ...Madmen in authority, who hear voices in the air, are distilling their frenzy from some academic scribbler of a few years back».

*John Keynes* [1, p. 383-384].

A powerful constraining factor in the development of economic science is the indifference of government authorities to it, to its recommendations on strategy. Confident in their own competence, the authorities do not need advisers.

*Leonid Abalkin* [2, p. 37].

Today, there is no more urgent task for the Russian economic science than to develop the concept of overcoming the existing trend of fading economic growth and moving towards a sustainable socio-economic development (see. Table 1).

Table 1

**GDP growth, % to previous year**

Indicator	2008	2009	2010	2011	2012	2013	2014
Growth rate	5.2	-7.8	4.5	4.3	3.4	1.3	0.5*

\* According to the forecast prepared by the Ministry of Economic Development of Russia (September 2014).

Sources: hereinafter, unless otherwise specified, the statistics are based on publications of the Russian Federal State Statistics Service and forecasts prepared by the Ministry of Economic Development of Russia for the relevant years.

The data shown above demonstrate that the economic slowdown became apparent since 2010, when the pace of recovery in GDP was lower than its growth in 2008, even though, in the last quarter of 2008, the GDP has decreased (relative to Q4 2007) as a result of economic crisis. In absolute terms, the GDP growth in 2010 and 2011 decreased, respectively, by 74 % and 16 % compared to 2008. This trend continued in the following years. As a result, the average annual GDP growth in the post-crisis (2009) period (2010–2013) was more than twice lower than in the comparable pre-crisis period (2005–2008).

However, given the current state of resource base in the economy, a 2-3 % growth is the minimum that allows only the simple reproduction [3, p. 34]. That is why the Main Areas of Activities of the Government of the Russian Federation for the Period until 2018<sup>2</sup> indicate that: «In the forthcoming mid-term period, it is necessary to ensure the transition to the path of sustainable economic growth of at least 5 %.... 2-3 % annually ... (would be) critically low. Such dynamics of gross domestic product will not be allowed to balance economic and social components of national development». The problem of dynamics of economic growth becomes particularly acute amid the current aggravation of political and

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<sup>2</sup> The Main Areas of Activities of the Government of the Russian Federation for the Period until 2018 (approved by the Chairman of the Government of the Russian Federation on January 31, 2013). URL: <http://base.garant.ru/70309020/#ixzz3HP6At700>.

economic standoff between Russia, on the one hand, and the US and the EU, on the other, which may be of a relatively long-term nature.

However, the economic authorities have apparently resigned themselves to the negative trend of economic growth. In September 2013, for the first time in the history of preparing such documents, the Ministry of Economic Development of Russia proposed to select as the base scenario for its forecast an inertial, and in fact, pessimistic scenario providing for the «preservation of inertial trends prevailing in the last period». According to this scenario, the average annual GDP growth in 2013–2016 should be 2.8 %, which actually puts the economy in the «red line» indicated by the Main Areas. The forecasts made in May and September 2014 make it a «tradition» to opt for inertia scenario as the base scenario by consistently reducing the average annual growth rates for the period of 2013–2017 to 1.9 and 1.7 %, respectively. In essence, this is taking the economy under the «red line»<sup>3</sup>. Speaking in the State Duma of the Federal Assembly of the Russian Federation (October 8, 2014), the Russian Minister of Economic Development said that the annual rate of 3 %, which is projected to be achieved only by 2017, «is, apparently, an acceptable level in the present circumstances». It remains unclear how this is consistent with the Main Areas where this rate is recognized as critically low, since in this case «it will not be possible to balance the economic and social components of the national development».

Meanwhile, the development of a concept to reverse the existing development vector is accentuated by the current split in the economic science community. In essence, the standoff of the Soviet period between the proponents of «market-oriented» and «planned» economy is reproduced today as the opposition between the «liberals» and «statists». In this case, we are talking about the split and not about a scientific discussion between representatives of various political and economic schools, since each of these groups holds separate forums, congresses, conferences, etc., publishes its «own» magazines by preferring to criticize their opponents at a distance in a circle of like-minded people, and forms its future adepts in their «own» educational institutions. As a result, the one «party» that suffers a real harm is Russia's political and economic thought.

Nevertheless, there are grounds for overcoming this existing split.

Despite all the opposing views on the economic policy for the country, the representatives of both schools are united in their understanding of causes behind the current slowdown in growth rates and material conditions for overcoming it.

First, both the expert community and economic authorities agree that the high growth rates experienced before the current situation (in 1999–2008, 6.9 % on an annualized basis) have been, to a large extent, ensured by external economic environment for the energy and raw materials which form the bulk of Russian exports.<sup>4</sup> Could the economic growth based on such a source be sustainable? The answer came at the end of 2008, when the recovery vector of the Russian economy has changed towards a deep fall. And although this is often explained by the effects of global financial and economic crisis that has been under way in that period, this is only an apparent reason. The political and economic nature of the global financial crisis in 2008–2009 and the one of the Russian crisis are fundamentally different. In both cases, the trigger was the collapse of financial base for the economic growth. However, in industrially developed countries, where the global crisis has originated, the underlying

<sup>3</sup> Even in a moderately optimistic scenario of the forecast made in September 2014 for the period of 2014–2017 the average annual GDP growth is assumed at the level of 2.5 %, i.e. in the «red line».

<sup>4</sup> The share of mineral products in the commodity structure of Russian exports has increased from 53.8 % in 2000 to 71.6 % in 2013.

«The high growth rates achieved in recent years were almost by half based on leading growth in physical export volumes and higher oil prices» (Updated Forecast of Socio-Economic Development of the Russian Federation for 2006 and Main Parameters of the Forecast until 2008, the Ministry of Economic development of Russia, 2005 [electronic resource, in Russian]. URL: <http://www.lsn.ru/1269.html>). «In 2004–2007, the external economic conjuncture provided 42–50 % of the growth» (Forecast of Socio-Economic Development of the Russian Federation for 2010 and for the Planning Period of 2011 and 2012, the Ministry of Economic Development of Russia, 2009 [electronic resource, in Russian]. URL: <http://economy.gov.ru/minec/activity/sections/macro/prognoz/doc1254407742765>). «The external economic factor (higher oil prices and demand for commodity exports) was up to 50 % determining the economic growth» (Explanatory Note of the Ministry of Economic development of Russia on Scenario Conditions for Preparing the Scenarios for the Forecast of Socio-Economic Development in 2013–2015, the Ministry of Economic Development of Russia, 2012 [electronic resource, in Russian]. URL: <http://sakha.gov.ru/node/70777>). In 2000s, the dynamic growth of the Russian economy with an average annual rate of about 7 % has been for more than its half determined by the effect of improved external economic conjuncture, growth in production and exports of hydrocarbons and raw materials, as well as by implementing the general advantages of catch-up growth (about 4 % of GDP growth annually) (Forecast of Socio-Economic Development of the Russian Federation for 2014 and for the Planning Period of 2015 and 2016, the Ministry of Economic Development of Russia, 2013, [electronic resource, in Russian]. Access from Garant, a reference and legal information system. <http://base.garant.ru/70458344/>). «More than a quarter of Russian GDP comes from the sale of gas, oil, metals, wood, other raw products or first-processed products in the global market [4].

factor of the financial base was the credit expansion that gave rise to a «debt pyramid», which, like all similar pyramids, was bound to collapse, sooner or later. The financial base for the growth of the Russian economy was provided by the conjuncture of export markets for energy and raw materials. This conjuncture has deteriorated dramatically under the impact of the global economic crisis (reduced demand led to lower exports and prices). The result was the above-mentioned fall in GDP.<sup>5</sup> However, such change in the conjuncture may also occur without global economic crisis, as it has been in the 1980s and much of the 1990s. After all, the scientific and technological progress will sooner or later solve the problem of access to alternative sources of energy. What will then happen to the prices of energy and raw materials which traditionally make up the bulk of Russian exports? In this case, the source of economic crisis hitting the Russian economy will not be the global economic crisis but the global scientific and technological progress. This is why the expert community has fully shared the point, made by the Russian president when setting the task of developing the concept of long-term socio-economic development, that a scenario based on energy and raw materials «inevitably leads to an increase in Russia's dependence on imports of goods and technology, assigning to us the role raw material appendage of the world economy and, in the future, may result in a lag behind the world's leading economies and displacement of our country from among the world's leaders. By following this scenario, we will not achieve the necessary progress in improving the quality of life of Russian citizens. Moreover, we will be able to ensure neither the security of the country, nor its normal development, and will endanger its very existence, I'm saying this without any exaggeration».<sup>6</sup>

Secondly, the expert community and economic authorities agree that the material basis for sustainable national economic growth (socio-economic development) is not the production of raw materials but that of the final consumption goods. Such growth implies the existence of developed processing sector which, in turn, requires a modern technological base. However, this sector of real economy suffered the greatest collapse during the crisis of 1990s. By 2000, the production of machines and equipment was less than a third from the level of 1991. Moreover, the production of metal-cutting machines fell almost 9 times, including a 125-fold drop in the production of computerized and numerically controlled (CNC) machines, a 19-fold drop in the production of forge-and-press machines (77-fold drop for CNC forge-and-press machines), a 16-fold drop in the production of automatic and semi-automatic assembly lines for machine building and metal processing. This was accompanied by the qualitative deterioration of technological base. As pointed out in the economic literature, the 1990s have been marked by a 2-fold decline in the share of high-tech sector in the total industrial production [5] along with the loss of more than 40 % of technology stock and up to 90 % of design organizations [6]. That is why the task of creating such base was set by the government programs from the very beginning of transition to restorative growth.<sup>7</sup>

Thirdly, the representatives of different schools and trends of the Russian political and economic thought see the cause of this negative tendency in the current system of economic relations and agree that significant institutional changes are needed in order to overcome it. Therefore, today, all economic schools are united in understanding the need for an active role of state in the economic life.

However, there are apparently irreconcilable differences on where exactly the state should play its more active role.

<sup>5</sup> «In the most acute phase of the crisis (Q4 2008 — H1 2009) — noted the Forecast of Socio-Economic Development of the Russian Federation for 2010 and for the Planning Period of 2011 and 2012 (Moscow, the Ministry of Economic development of Russia, September, 2009, in Russian) — the decline in export earnings and, as a result, the contraction of domestic demand have caused the drop of GDP by 4.6 -5 %, or almost 50 % of such drop (Forecast of Socio-Economic Development of the Russian Federation for 2010 and for the Planning Period of 2011 and 2012, the Ministry of Economic Development of Russia, 2009 [electronic resource, in Russian]. URL: <http://economy.gov.ru/minec/activity/sections/macro/prognoz/doc1254407742765>).

<sup>6</sup> V. Putin. On Russia's Development Strategy until 2020. Speech at the enlarged meeting of the State Council held on February 8, 2008 [electronic resource, in Russian]. URL: <http://archive.kremlin.ru/text/appears/2008/02/159528>

<sup>7</sup> Earlier, in the draft Main Areas of Socio-Economic Development for the Long-Term Perspective (until 2010) prepared in accordance with the directive of the Russian Government No. 2021-p of December 1, 1999, the second section was devoted to objectives of modernizing the economy, while the innovation scenario has been recognized as having no alternative. This document also defined the period for implementing such scenario (2007–2010), which will see «the creation of scientific, technological and production prerequisites for radical technological re-equipment of major economically important sectors of production and increasing the share of modern products competitive at the global level» (Main Areas of Socio-Economic Development for the Long-Term Perspective (until 2010)), draft, [electronic resource, in Russian]. URL: <http://www.pro-roo.ru/images/files/direct2010.pdf>).

Those who are referred to the «liberal» school see the market forces as the main engine of economic growth. Hence, the bet on private investment activity and, consequently, on institutional measures aimed at providing greater freedom to entrepreneurs for such activity, including:

- Lowering the administrative barriers for market entry;
- Eliminating unnecessary regulation of business activities;
- Strengthening the institutions for protection of property rights;
- Eliminating corruption;
- Eliminating the monopolization of markets;
- Lowering inflation through a tight fiscal policy aimed at zero deficit (and even better a surplus) of the budget by sterilizing the «excessive» money supply formed by oil and gas revenues and limiting public spending;
- Restricting the investment activity of the state, including through privatization of state assets.

Those who represent the «statism» school believe that the investment activity of the state should become the driver of economic growth and, consequently, give priority to institutional measures aimed at expanding such activity:

- Establishing the institutions of state-sponsored investing;
- Identifying priority areas for state-sponsored investing;
- Mobilizing financial resources available to the state for investing.

In turn, the implementation of such approach implies the refusal to protect such «sacred cows» of economic liberalism as:

- Priority of monetary methods in suppressing inflation through tight budgetary constraints and inadmissibility of budget deficit;
- Large-scale privatization of state-owned assets, instead of which they propose to establish an effective state control over the assets that are absolutely required for achieving the objectives of structural and technological transformation.

Without going into the theoretical foundation of the above views, let's mention only the fact that, until recently, the official economic policy in Russia was based exactly on the «liberal» concept. It was this concept that served as the theoretical foundation for «shock» liberalization of prices, «runaway» privatization, etc., carried out in the 1990s.

At the same time, when assessing the economic effects of this policy, it does not seem methodologically justified to base the conclusions on economic results of 1990s. During this period, the main political objective of new government authorities was to prevent the restoration of the old political system and the economic policy has been, above all, subordinated to achieving that goal. One can still debate for a long time whether these were exactly the actions necessary to produce the desired political effect, but it wouldn't be correct to consider the economic dynamics of that period as a result of transition from economic dominance of the state to reliance on market forces.

Meanwhile, it was this period that saw the formation of institutional framework for the market economy, such as the emergence of economic agents independent of state, capital market, relevant regulatory framework, etc. Therefore, when at the junction of 1990s and 2000s the issue of political power was resolved, the economic policy could be subordinated to properly economic objectives by relying, on the one hand, on stabilization of economic situation and favorable foreign economic conjuncture achieved at the end of 1998 — beginning of 1999 by the government of Evgeny Primakov and, on the other hand, on the institutional framework that, overall, was in line with the theoretical premises of market liberalism.

The Program of Socio-Economic Development of the Russian Federation for the Medium-Term Perspective (until 2004) adopted at the beginning of the first decade of 2000s stated that: «The deregulation of economy, guarantees of property rights and equal conditions of competition should be the main motives of economic policy. ...In the Russian economy, the non-market signals play a substantial role. This problem must be solved by further privatization combined with consistent application of anti-monopoly laws». In later documents of this kind, such provisions have become a cliché repeated as a sort of «mantra». Thus, the Forecasts of Socio-Economic Development of the Russian Federation for 2011–2013, 2012–2014, 2013–2016 include, literally, the following sentences:

- «The pace of privatization will be significantly increased for progressive reduction of the public sector in the economy»;

- «Developing the mechanisms aimed at protecting the property rights of shareholders and investors»;
- «Improving the regulatory legal acts in the area of legislation on insolvency (bankruptcy)»;
- «Improving the competitive environment»;
- «Improving the anti-monopoly regulation»;
- «Improving the regulation of natural monopolies».

The same forecasts have consistently stated the need to tighten the fiscal policy by reducing public spending in order to ensure a balanced budget.

Accordingly, the dynamics of economic development of Russia in 2000s can indeed be used to assess how efficient was the policy of «reliance on market forces».

Unfortunately, we have to observe that there were no positive results achieved in creating a modern technological base of the economy (Table 2).

Table 2  
Production Dynamics of Machinery and Equipment, % as compared to 1991

Indicator	FACT				FORECAST
	2000	2008	2009	2013	2017
Production of machinery and equipment	32.3	63.3	42.3	53.7	55.6

During the recovery growth of 2000s, the production of machinery and equipment was increasing in an extremely uneven way and, by 2008, was by more than a third below the level of 1991. This includes the production of metal-cutting machines (increase by more than 7 %), CNC metal-cutting machines (+3.4 %), forging machines (+11.5 %), CNC forging machines (+15.5 %), automatic and semi-automatic lines for machine building and metal processing (+1.3 % compared to 1991). After the crisis in 2009 had thrown the mechanical engineering back to 1990s, even this low level has not been restored. Moreover, the sharp drop of the growth rates in production of machinery and equipment in

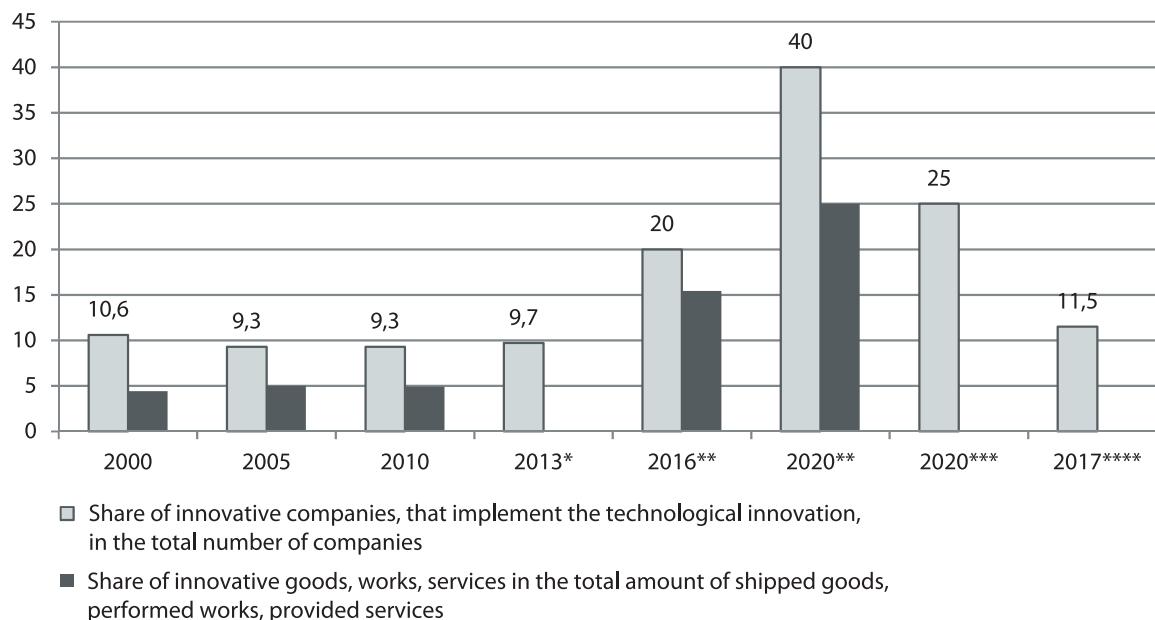


Fig. The Dynamics of Innovation Activities in the Industry

2012 to 2.7 % compared to 11.1 % in 2011 escalated in 2013 into the fall of their production by 3.4 %. The forecast of the Ministry of Economic Development of Russia made in September 2014 implies that in 2014 the rate of this decline will more than double and will reach 7.1 % compared to 2013. Even though 2015 is expected to bring back the growth of production, the Table 2 shows that the low levels of 2008 will not be restored even in 2017.

Despite all organizational and resource-related efforts, the share of innovative companies in the industry and the share of innovative goods (works, services) remained at an unacceptably low level of 2000, which required more than substantial reduction of targets set by the Strategy of Innovation

Development of the Russian Federation for the Period until 2020 in the State Program «Economic Development and Innovation Economy» adopted only two years later (Fig.).

As it was rightly pointed out in the Strategy of Innovation Development, a key reason for this «was the overall low demand for innovation in the Russian economy ... Neither private nor the public sector show sufficient interest in implementing innovations».

These trends result in the physical and moral aging of technological base of the economy. According to the Ministry of Economic Development of Russia, some 80 % of the technological equipment in the real sector of the economy is 16–35 years old and, in mechanical engineering, more than 50 % is more than 25 years old. It is clear that the manufacturing of competitive products on such technological base is, at the very least, complicated.

The result has been the lagging of processing industries and industry as a whole (in 2013, their production volumes were 88.7 % and 90.5 %, respectively, compared to 1991), which, according to the forecast of the Ministry of Economic Development of Russia (September 2014) will continue up until 2017 (according to the base scenario – 97.9 % and 97.1 %, respectively). Thus, the infamous imbalance of the Russian economy towards raw materials is not determined by «overdevelopment» of raw material industries (their growth reflects the natural competitive advantages of Russia), but by underdevelopment of processing sector and, above all, its technological base.<sup>8</sup> As a result, today, we see the «stage productions» that are thirty years old.<sup>9</sup>

The most dangerous thing in this situation is that the economic authorities, apparently, already do not believe themselves in the possibility of reversing these trends. Otherwise, how can one explain that in the forecast for 2014–2016 (September, 2013), the Ministry of Economic Development of Russia predicts that: «The specific structure of investments in 2013 will probably see the decline in the share of investment in machinery and equipment, which corresponds to a decrease in demand for mechanical engineering products... In 2014–2016, the projected low demand for machinery and equipment will further reduce the share of this group in the structure of investment», while the scenario for the period until 2017 (prepared in May 2014) suggests conservative investment policies of private companies in the upcoming period? It appears that we will have here a case self-fulfilling prophecy: how should behave the investors after reading such passages coming from a governmental authority?

This situation has led not only to more aggressive campaigning by proponents of active state-sponsored investing, but also to new emphasis in the formulation of economic policy. Thus, the Forecast of Socio-Economic Development of the Russian Federation for 2012 and for the Planning Period of 2013–2014 (September 2011) stated that: «The development of Russian economy in the period of reforms shows the liberal, purely market-based mechanisms do not lead to the rapid development of high-tech industries. ... This situation requires increased state intervention in the national economy and a comprehensive policy of modernization.» Speaking in the State Duma on April 11, 2012, Vladimir Putin said: «The state will directly invest its funds in technology development and support to critically important industries. First of all, this is the machine-tool building (italics added by D. S.)» Accordingly, the State Program «Developing the Industry and Increasing its Competitiveness»<sup>10</sup> indicates that even «in the early 2000s, it became clear that, without the participation of the state in addressing the key challenges of infrastructure, investment and innovative nature, the industry will not be able to reach the required level of competitiveness».

The September (2014) forecast of the Ministry of Economic Development of Russia, in its Institutional Transformation section, puts in the first position the measures aimed at developing the institutions and mechanisms of governance related to strategic government planning.

<sup>8</sup> In fact, the practice has once again confirmed a well-known theoretical conclusion that market mechanisms ensure the priority direction of investment resources to those industries where the country has natural competitive advantages.

<sup>9</sup> The Main Areas of Activities of the Government of the Russian Federation for the Period until 2018 indicate that: «The overall number of existing challenges and conditions for economic development determine, as a primary goal, the improvement of competitiveness of the Russian economy based on the intensive growth of labor productivity». Compare it with the following: «In order to successfully solve diverse economic and political tasks faced by the country, there is no other way than the rapid growth of labor productivity, steep increase in the efficiency of entire public production» (Report of the Central Committee of the Communist Party of the Soviet Union and the Party's immediate tasks in the areas of domestic and foreign policy of the Party // Proceedings of the 25th Congress of the CPSU, Moscow, Politizdat, 1976, p. 43-44, in Russian).

<sup>10</sup> Developing the Industry and Increasing its Competitiveness, State Program, approved by the Directive of the Government of the Russian Federation No. 91-r of January 30, 2013) [Electronic resource, in Russian]. Access from Consultant Plus, a reference and legal information system.

The state began to implement a number of measures (establishing direct and indirect state control over the largest corporations and banks, preparing the laws on strategic planning and industrial policy, adopting decisions on using the money from National Welfare Fund (NWF) and Russian Direct Investment Fund to finance the largest investment projects, such as Baikal-Amur Mainline, Trans-Siberian Railway, Central Ring Road, Tyvinsky, Smart Grids, and eliminating digital divide, directing up to 10 % of funds from NWF to projects involving the Rosatom State Atomic Energy Corporation), which in aggregate forced the proponents of the «liberal» school to start talking about the dangers of state capitalism.

However, so far, as shown by the above economic results of the last 2-3 years, no reversal can be observed in the economic dynamics and it is not even predicted in the next mid-term period. Moreover, the investment «impulse» of the state has not been picked up by the business sector.

How to explain this situation? By erroneous theoretical constructions or lack of professionalism on the part of those who implement them?

Representatives of the «liberal» school see the reason in inconsistent policies of the state to develop the entrepreneurial freedoms suppressed by the economic activity of the state which, therefore, is preventing the creation of a good «investment climate». The «statists», on the contrary, explain the absence of positive results by inconsistent course to increase the economic activity of the state while preserving the line to liberalize the economy. This debate resembles the one that was going on after the defeat of the first Russian revolution of 1905, when the question has been whether it was necessary to take up arms? The thesis that «there was no need to pursue the course of liberalization» («state investment activity» — underline as appropriate) is opposed by a counter argument that «yes, it was necessary to pursue, but only more resolutely and vigorously».

We will leave the issue of professionalism demonstrated by those who implement the policy as being outside the subject matter of political and economic analysis and turn our attention to economic theory.

The science of political economy has long ago come to conclusion that, in a market economy, the driver of real economic growth is business competition. This is what has been written already by Karl Marx: «...A capitalist, who applies the improved method of production, appropriates as the surplus labor a larger part of the working day than the rest of capitalists in the same industry. ...This very law, acting as the enforcement law of competition, forces the rivals of our capitalist to adopt the new method of production» [7]. This implies that not every entrepreneur is a subject of real economic growth, but only the one whom Joseph Schumpeter would later call the entrepreneur-innovator that «pulls over» the financial resources to create new and more efficient technology. Therefore, the main task is to not create a favorable investment climate in general, but to create it for entrepreneurs-innovators. It is unlikely that any proponent of relying on state investment activity will object to the need for consistent prioritized elimination of excessive administrative barriers for such entrepreneurs, effective protection of their property rights, reducing the costs and simplifying their access to financial resources and other preferences, as demanded by the adepts of economic liberalization. From theoretical point of view, such policy should bring the desired results and, therefore, the economic liberalization in this area is an absolute prerequisite for the transition to sustainable socio-economic development.

But is such liberalization a sufficient condition for transition of the country to sustainable socio-economic development in a specific context of today's Russia?

In this regard, one need to remember that theoretical concepts in any science use the abstract notions and the laws formulated in such abstract terms manifest themselves in pure form only «under otherwise equal conditions». In real life, such «equal conditions», usually, do not exist.<sup>11</sup> To turn the theoretical constructions into applied tools of economic policy, they must relate both to external and internal political and economic realities of a country.<sup>12</sup> It is well-known what negative consequences for Russia had the struggle for the «purity of theory» in the period of the so-called «socialist (communist) construction» that ignored the economic reality. Is it necessary to repeat today, basically, the same

<sup>11</sup> This point applies not only to social but also to natural sciences. It was already Vladimir Vernadsky who wrote: «The organism removed from the biosphere is not real, (it) is an abstract logical construction, which by its properties is as distant from reality as it is distant from the real air, i.e. the troposphere, the air of physics [8, p. 193].

<sup>12</sup> «That a fact is described as economic is already an abstraction... A fact is never, if we take into account its deep causes, exclusively or «purely» economic; it has always other, often more important sides» [9, p. 57].

error with inevitability of the same consequences while fighting, this time, for the «purity of market-based principles»?

The thesis on the need to relate the theoretical constructions to realities of specific country is not new for the science of political economy.<sup>13</sup>

Today, at least on the verbal level, it is accepted by the state authorities.<sup>14</sup>

Of course, this is not about a «special path for Russia» but about the need to take into account its economic, as well as social and geopolitical reality. When addressing this reality, it would be not out of place to ask the following questions:

1. Do the Russian entrepreneurs and non-state financial institutions have today the resources to meet the large-scale challenges for radical technological re-equipment of the national economy?

The aforementioned Forecast of Socio-Economic Development of the Russian Federation for 2012 and for the Planning Period of 2013–2014 indicated that a more active «state intervention in the national economy» was required exactly because the «deficit of financial and technological resources, insufficient development of transport and energy infrastructure, as well as the lack of qualified personnel, prevent the large-scale transition to innovative, socially oriented type of development».

2. How real are the prospects of obtaining the resources from foreign sources for developing a competitive technology base?

In the light of recent geopolitical events around the Ukrainian crisis, the answer to this question is all the more obvious.

3. Does the Russian economy have today the critical mass of entrepreneurs-innovators ready to ensure the appropriate redirection of financial flows?

The latter makes us to remind that the leaders of modern Russian business have grown not out of competition for markets through organizational and technological innovation, but out of competition for division and the redistribution of property, which requires a whole different set of skills. Given these objective circumstances, one can hardly expect them to behave as Schumpeterian entrepreneurs-innovators.

Of course, the appropriate changes in the institutional environment will encourage the emergence of entrepreneurs whose talent will be directed towards the necessary transformations. However, such changes require more than the adoption of laws and other regulatory acts that are perfect in terms of

<sup>13</sup> It was already Karl Marx who believed that «the same economic basis, the same in terms of main conditions — with the infinite variety of empirical circumstances, natural conditions..., external historical influences, etc. — can reveal in its manifestation the infinite number of variations and gradations that can be understood only by analyzing the empirical data of these circumstances» [10, p. 354]. It was exactly this methodological principle that served as the basis for his reply in 1881 to the request made by Vera Zasulich to explain his «views ... on the theory that, by virtue of historical inevitability, all countries of the world must go through all phases of capitalist production» [11, p. 576]: «In analyzing the origin of capitalist production, I am saying that... the «historical inevitability» of this process is limited precisely to the countries of Western Europe» [11, p. 250]. It is interesting to note that Karl Marx quotes here the French edition of the first volume of «Capital» (1875). The authentic text is not included in the 2nd Edition of the Works of Karl Marx and Friedrich Engels in Russian [7, p. 726-728], because the Russian translation was made from the 4th German Edition (1890) [11, p. 561].

This point of view was also actively supported in the Russian political and economic thought. Alexander Butovsky, the author of the first textbook on political economy, believed that: «If you apply a theory to explain the various aspects of life in England, this will still shred little light on the same issues about France or Russia, and even less with regard to Egypt or China. ...The people's activities in each of these states are under the influence of totally dissimilar circumstances, climate, location, state order, customs and education in general. It is not surprising that in all its manifestations, with all similarity of motives and means, there is a great dissimilarity, especially in the direction and results [12, p. XXX-XXXI].

The same view was shared by Sergei Witte, who observed, in particular, that the forms, in which the law of supply and demand manifests itself, would inevitably mutate «according to different characteristics of social organization» [13, p. 134] and, therefore, «as long as the Russian life does not elaborate its own national economy based on individual characteristics of Russian soil, we will remain in the process of vacillating between various fashionable teachings while being alternatively carried away first by one of them, and then by the other; ...and it is clear that until then we will not be living the right economic life but will be towed along by foreign influences and all kind of speculations about public welfare»[13, p. 162].

The same methodological views were held by Leonid Abalkin, who once observed that «the nature of property, the market institutions, the motives of behavior cannot, for all their generality, be without differences in Anglo-Saxon and Romance countries, in South-East Asia and the Muslim world, in India, China, and Russia [14, p. 214].

<sup>14</sup> For example, during the meeting of the Russian government held on August 1, 2013, to discuss the State Program «Economic Development and Innovation Economy», the point made by Vladimir Fortov, the President of RAS, who said that «today, in the world, there is no universal model for building an innovation economy. Each country builds these economies in its own way: the French, in their own way, and Koreans, in their own», was backed by the Prime Minister, who noted that: «It is absolutely fair (to say) that this system cannot be international. Of course, it should be based on the achievements of all mankind... But it still must be tailored for the Russian Federation: we have specific conditions, in the same way, incidentally, as America has its specific conditions, and France, too. It will always have a specifically national character».

meeting the needs of effective market mechanisms. It was already Douglass North who mentioned the fallacy of views «that the life and economic processes are subordinated to written laws and property rights. However, even in the most developed economies, the formal rules represent a small (albeit very important) fraction in the set of constraints which shape the choices that we face... Our behavior, to a great extent, is determined by the unwritten codes, rules and conventions [15]. This results in a phenomenon which the lawyers call the gap between the law and its enforcement practice.

Of course, the development of market relations based on consistent institutional changes, in theory, should lead to appropriate shifts in social consciousness and the emergence of a critical mass of entrepreneurs-innovators. However, it should be borne in mind, first, that this process will be rather long. Secondly, for Russia, this length may be particularly substantial given the historical characteristics of Russian entrepreneurs.

The whole economic history of Russia indicates the low propensity of Russian entrepreneurs to innovative behavior.

Back in 1663, Juraj Križanić wrote while addressing the Russian leaders of that period: «It would be good to establish firmly, and to punish those who disobey, not to sent abroad any raw material, such as raw leather, hemp and flax, but to make sure that our people make all kind of wares at home, as much as possible, and sell the ready-made things abroad» [16, p. 75].

60 years later (in 1724), Ivan T. Pososhkov, the first Russian political economist, sent his manuscript to Peter the Great, where essentially he repeated the same idea: «And instead of taking to us the fabrics made of our materials, it will be better that we take to them the ready-made fabrics» [17, p. 25]. By the way, this proposal was submitted when Peter the Great had implemented the first industrialization (i. e. in fact, an innovative renewal) of the Russian economy. However, once the state-led modernization momentum has weakened, everything came «back to square one», as it was tellingly demonstrated by the history of developing the universal steam engine, the use of which gave rise to first industrial revolution.

In April 1763, Ivan Polzunov submitted a design of the universal steam engine to the head of Kolyvano-Voskresensky plants (Altai, Russia). In December of the same year, a courier from Saint Petersburg delivered to Altai the Decree issued by Catherine the Great, which rewarded Ivan Polzunov with a cash prize and praise, and invited him to Saint Petersburg in order to join the Russian Academy of Sciences. At the same time, his superiors were ordered to begin the construction of the machine based on his design. The machine has been commissioned on May 23, 1766. In less than 6 months, the machine, which was operating at less than a third of its capacity, did not only fully repay its costs (7,200 rubles), but also brought more than 12 thousand rubles of profit. However, on November 10, 1766, the engine stopped following the leakage from the boiler. There was no one to repair it, and the engine was sent to the dump.

The first patent for the universal steam engine was issued 20 years later in England to James Watt. In 15 years (1800), there were almost 500 machines operating in England, in 1810 – 5,000, and in 1825 – 15,000. To Russia, the first industrial revolution arrived much later.

At the end of 19th century (1893), the Program for the Development of Industry and Trade in Russia mentioned the same trend and set the same objectives as in the 17th century: «Our exports still focus primarily on raw materials, i. e. the least profitable product in international trade. (We need) to gradually prepare the transition to a relatively greater exports of processed products, so that the people's work can draw greater benefits from exports to pay for mainly our people's riches».

Despite its well-known significant scientific and technological breakthroughs, the Soviet economic system also was unable to ensure the transition of the economy to the path of innovation development following the political directive to «shift from extensive to intensive type of economic growth based on scientific and technological progress» backed by the establishment of mandatory indicators in the plans of enterprises for implementing the technological innovation.<sup>15</sup>

<sup>15</sup> Thus, the share of products manufactured by eleven ministries of civil mechanical engineering for more than 10 years, i.e. morally obsolete, has increased by early 1980s to 30.6 % as compared to 16.2 % in 1967 (Planovoye Khozyaystvo magazine, 1985, No. 4, p. 92, in Russian), which translated into the reduction of share of exported machines, equipment and vehicles in the total exports of USSR (including re-export) from 21.5 % in 1970 to 13.6 % in 1985.

Current Russian leaders continue to repeat almost literally all these arguments made more than a century ago.<sup>16</sup>

The above allows to make a legitimate assumption about a certain, historically developed mechanism that reproduces the non-innovative character of Russian economic system. But if this is so, then the use of traditional mechanisms (tax incentives or other preferences) is unlikely to be sufficient in the elaboration of required institutional changes. As we know, these mechanisms have been actively tried in the past. However, the above statistics show that it did not lead to any significant results. Therefore, we need a science-based search for fundamentally new solutions allowing to reverse this historical trend.

Anyway, inevitably, there is the most important question: Does Russia have the time resource to wait for the results of institutional reforms in the form of the emergence of a critical mass of Schumpeterian entrepreneurs-innovators?

The currently established vector of economic dynamics and geopolitical situation clearly give a negative answer.<sup>17</sup>

Therefore, when consistently and persistently carrying out the science-based search and implementation of institutional measures facilitating the emergence and accumulation of a critical mass of entrepreneurs-innovators,<sup>18</sup> we must understand that, in the current Russian socio-economic reality, these measures, while being undoubtedly necessary, are insufficient for transition to the path of sustainable economic growth within the time interval available to Russia for such transition. They should be complemented by a comprehensive set of measures that can «fill the time gap» between the need for immediate reversal in stagnation trends and time when this function can be assumed by a new generation of Russian entrepreneurs. Is it possible, in the present circumstances, to implement these measures without using the investment potential of the state?

Of course, the investment activity of the state carries certain risks. The opponents of these measures rightly point out that, first, under otherwise equal conditions, the state is a «bad entrepreneur» compared to the private one. Secondly, there is a danger of incorrectly defining the priorities of structural reforms which can lead to the waste of resources. Thirdly, the investment activity of the state is fraught with an outburst of inflationary trends. Fourthly, in Russia, we have an «ineffective state».

While agreeing, in principle, with the above arguments, it is necessary to mention the following.

First, in the current Russian reality, the point about the state as a «bad entrepreneur» is confronted with a situation when there is no critical mass of «good» entrepreneurs, at least in the area associated with technological transformation<sup>19</sup> («For the lack of letter headed paper, we have to write on a plain sheet»).

Secondly, the modern science knows how to minimize the risks arising when defining the priorities of scientific and technological development. The remaining risks of errors are substantially lower than the risks arising from the refusal to make such definition.

Thirdly, while agreeing with the point about inflationary risks, we should bear in mind that there are well-known mechanisms to minimize these risks, and the latter, at least, do not exceed the risks arising from the shortage of investment resources generated by limiting the government spending. Apparently, the economic authorities are beginning to realize this, at least, in words. Thus, just recently, the forecasts for 2012–2015 (September 2012) and 2014–2016 (September 2013) stated the need to «maintain stability of the budget system through the introduction of fiscal rule and restricting within its limits the expenditures of federal budget». Moreover, the forecast for 2014–2016 (October 2013) established that «the monetary policy focuses on the transition to inflation targeting in 2015».

<sup>16</sup> «We need to create incentives not to send the raw materials abroad but process them here in Russia, and manufacture, on our own, the ready-made, highly-demanded products for domestic market and to supply them abroad with a high level of processing and added value» (Vladimir Putin, «We need to create incentives not to send raw materials abroad», a speech at the commissioning of Tobolsk-Polymer plant, October 15, 2013 //Russian People's Line, an information and analysis service [electronic resource, in Russian]. URL: [http://ruskline.ru/news\\_rl/2013/10/15/vladimir\\_putin\\_nado\\_sozdat\\_stimuly\\_dlya\\_togo\\_chtoby\\_ne\\_gnat\\_syryo\\_za\\_rubezh/](http://ruskline.ru/news_rl/2013/10/15/vladimir_putin_nado_sozdat_stimuly_dlya_togo_chtoby_ne_gnat_syryo_za_rubezh/)). «We sell raw materials and, mostly, buy abroad the ready-made products which are very often made from our own raw materials» (Dmitry Medvedev, Strategies for Development of Chemical Industry, a speech at the meeting on measures for developing the chemical and petrochemical complex in Russia, July 3, 2013//the Government of Russia, [electronic resource, in Russian]. URL: <http://government.ru/news/2771/>).

<sup>17</sup> In a way, the present situation can be described by a point made by Joseph Stalin more than 80 years ago: «We are 50–100 years behind advanced countries. We must make good this distance in 10 years. Either we do it, or we shall be crushed» [18, p. 39].

<sup>18</sup> One can and should debate the content and sequencing of such measures, and their matching to a specific situation.

<sup>19</sup> The story of È-Mobile car is an example of evidence to support this point.

However, the next forecast of the Ministry of Economic Development of Russia for 2014–2017 (May 2014) acknowledged the fact that «one of the major internal risks ... is a rather strict inflation target projected by the Bank of Russia» and «a moderately optimistic scenario of economic development implies the modernization of the fiscal rule... by increasing the federal budget deficit».

Fourthly, by accepting the point on the «inefficiency of the state» as our starting position, we condemn ourselves to inaction. This is because the «inefficient state» will fail to demonstrate not only the appropriate investment activity, but also, for sure, any institutional activity, including in the area of developing the freedoms for private entrepreneurship.

One should also bear in mind that the investment activity of the state does not contradict, in itself, the objectives of developing the private entrepreneurship activity. Moreover, the experience of countries that have successfully built modern high-tech structures shows that this process was happening and still happens with the large-scale investment support from the state. While setting the task of reviving the American manufacturing in his State of the Union address (February 2, 2013), the US President invited the Congress to support his initiative for one-time investment of 1 billion dollars to create a national network of 15 institutions of innovation for manufacturing industry and expressed his intention to use the resources of the executive branch for creating three new institutions which, in partnership with business, universities, colleges and government, will create and develop the manufacturing technology that will help businesses within the United States to create attractive jobs.

However, the economic reality of Russia demonstrates that the reliance on investment activity of the state, while being necessary in the present circumstances, nevertheless will be insufficient to reverse the negative trends and, under certain conditions, may act as a factor which is aggravating the current negative trends.

First of all, one must remember that the state investments, by virtue of limits that are objectively inherent to large systems (and the national economy is just such a system) can ensure only isolated breakthroughs rather than a comprehensive socio-economic development of the country. This point is confirmed by our own historical experience of economic modernization (modernization under Peter the Great, industrialization in 1930s, a failed attempt to «ride» the scientific and technological revolution in 1970s).

And most importantly, we should not forget the substantial risk of the policy aimed at increasing the investment activity of the state that follows from the Russian historical past. It is the established belief in the omnipotence of the state. The genetic memory of state paternalism may lead to a situation where the authorities will carry out their investment activities exclusively through the so-called «mobilization mechanism» relying on the priority of government enforcement. The inevitable consequence of this approach would be the more extensive use of «manual controls» which, despite allowing to solve some individual problems, are fundamentally unable to move the economy to a balanced sustainable development, suppress private business initiative and lead to excessive state presence in economic areas where it should be kept to a minimum and the definite lack of state participation in the areas where it is really needed. Our historical experience shows what negative socio-economic and political consequences for society can have this scenario, even if it is initially introduced as a temporary measure.

Such a development can be prevented only by conducting, along with the institutional changes in the economic area that form a strata of economically independent entrepreneurs-innovators, a no less profound transformation of political institutions aimed at democratizing the public life that can, on the one hand, prevent the emergence of «Big Brother» and, on the other, exclude the inclination of entrepreneurial class towards the privatization of the state.

The need to create a theoretical rationale for the scenario that seamlessly links the economic liberalization with a more active economic role of the state is dictated by today's economic reality in Russia. The reliance of theoretical studies on this reality is the condition for overcoming the existing split in the Russian political and economic thought and ensuring its real impact on economic policy. While overcoming this split, one should remember the lesson taught by the history of science — with the monopolized right to have the «only true scientific theory» ends the science and begins competition for access to the «ruler's ear», which is, in essence, the fight for the access to financial resources. The logic of this fight inevitably leads from slogans such as «Those Who Do Not Sing with Us Are Against Us» to labeling the opponents as «red-browns», «national traitors», «fifth column», etc., with all the consequences that this might have not only for science but for the nation as a whole.

Also, it is necessary to emphasize that the formation of the concept for transition to sustainable socio-economic development of the country cannot be reserved only to political and economic thought. Its theoretical base should be not only the discovered economic laws and knowledge of the real state of national economy, but also the knowledge of the condition and trends of social consciousness, the balance of different political forces, foreign policy trends and many other objective non-economic factors, which are the subject matter of other branches of social science. Therefore, the scientific status can be given only to a concept, the creation of which implies going outside the limits dictated by narrow economic thinking and reliance on integrated social science knowledge.

However, no matter to what economic school belong the representatives of economic science engaged in studying the laws of national economy's growth, as a rule, they are united in their critical attitude towards the current economic policy. Russian political economists are not the exception. «Complaints» that those in power «do not listen to scientists» (or, at least, «are not enough listening») can be heard from representatives of all kind of schools and trends of economic thought (though, it would be fair to observe that the «complainers» often consider as scientists only those colleagues who profess similar views).

But how justified are such claims?

The function of science is augmenting the knowledge about the objective laws of nature and society (fundamental science) and elaborating on the basis of this knowledge the ideas (proposals) on the possibilities of using these laws to achieve specific results (applied science). For a political economist, this is the knowledge of objective laws governing the economic life of the society in its integrity and building the concept of economic policy which implies the use of these laws in the interest of sustainable socio-economic development.

Implementing this function is a special area of professional human activity, which can be described by certain performance criteria and, like any professional activity, requires from its carriers certain abilities, knowledge and skills.

The state policy is the activity aimed at governing the state and society. The economic (social and economic) policy is the governance of economic (social and economic) life of the society. It is clear that this type of activity also requires a special kind of abilities, knowledge and skills. A politician is someone who uses these abilities, knowledge and skills to exercise such governance or seeks to achieve that goal. Therefore, the principal criterion for the effectiveness of politician is his/her ability to retain the place at the helm of government or (for the opposition) the ability to take this place. Everything else (including the social and economic policy) will inevitably be seen by a politician (consciously or unconsciously) as the means (tools) to achieve this goal. In this sense, the politics will always «have precedence over the economy».

Is it possible in these conditions to expect from politicians any strict implementation of the so-called «science-based concept of socio-economic development»? Of course, the sustainable socio-economic development is the most important financial condition for allowing a politician to retain his/her place at the helm of government. But for all its importance, it is not the only one. Can we demand a politician to put aside his/her thoughts about the date of next elections when adopting the decisions dictated by a particular theoretical concept? The difference of scientific and political performance criteria will inevitably lead to the situation where the real economic policy will always be different from any of its science-based scenarios and, thus, give a pretext for criticism from the scientific community. Therefore, the theorists of economic science should not assume the functions of economic policy-makers and keep in mind that this is a different area of professional activity with other criteria of expediency and efficiency.

The aptitude to augmenting the objective knowledge of the world and the ability use this knowledge for building a theoretically consistent ideas (concepts) for their possible application describes the professionalism of a scientist.

The professionalism of a politician is expressed in his/her ability to combine the activities aimed at retaining the state power in the hands of political force that he/she is representing (gaining access to such power when the politician is in opposition) with the strategic goals dictated by the objective laws of social evolution. This is where lies the art of economic policy — not a dogmatic adherence to theoretical concepts but in the ability to carry out specific activities that, at any given moment, may not coincide with the theoretical premises and can even, apparently, «contradict» them, while maintaining the science-based strategic vector of motion. This is what would be the policy that can

claim the status of being scientifically sound. Otherwise, we will witness the implementation of a well-known argument «With an iron hand we shall drive mankind to happiness» which will inevitably lead to consequences that are well-known, too.

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## Information about the author

**Sorokin Dmitry Evgenievich** (Moscow, Russia) — Doctor of Economic Sciences, Professor, Corresponding Member of the Russian Academy of Sciences (RAS), Vice Rector for Research, Financial University under the Government of the Russian Federation (49 Leningradsky Avenue, Moscow, 125993 Russian Federation, e-mail: dsorokin@fa.ru).