

Macroeconomics

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**INSTITUTIONS IN THE BROADENING
OF TECHNOLOGICAL MODERNIZATION
OF UKRAINE**

Abstract

The article expounds the need of transformational changes in Ukraine by the model «from the planned to market economy», demanding a new institutional format. It would require a transition to a new level of application of institutional factors enabling the transformation of the role of institutions as organizational structures, and relevant regulatory actions that would make it possible to raise the innovation-oriented investments to a new level. Success of transition to innovative investment model of economic growth of Ukraine is determined first of all by how well developed is institutional environment and specific institutions that promote the implementation of the projects of both macro- and microeconomic modernization. It is important at the same time to improve efficiency and to deepen market relations in the institutional environment of business with the goal of accelerated development of productive forces in Ukraine based upon capitalization of the economy. The capitalization should be the foundation of the processes of broadening of the scale of corporatization and should reach such a level of concentration of capital that can sustain the development of one of its most effective institutional forms, which is a modern corporation.

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1. Preliminary considerations

Formation of capitalist mode of production by way of transformations in Ukraine based on the «from planning to market economy» model includes, as in the other countries with the so-called transitional economies, institution of the notion of private ownership and respective rights of such ownership. Both the society and the economy have been demanding and demand in their turn the change of the format of institutional capacity that would enable the state, the business and the population to act in accordance with a new method of production, as the development of the dominating types of activities in a country signifies its respective institutional development (Reinert, 2004). Similarly, their delayed modernization, if the system of government does not provide for constant modification of norms and rules of interaction within the system «society – state – economy», impedes the progress as such for a long time. Institutional improvement in that triangle is possible when the changes occur simultaneously in all main areas of public life. The foundations for these changes are customs. As customs are one of the components of institutions, their formation and development epitomize modification of the means of production. As European experience demonstrates through its historical dimension, these developed swiftly thanks to massive inventions even in a relatively backward society of medieval Europe (Mokyr, 2014, p. 503). Later on science started to play the key role in the development of civilization (Bacon, 1971, pp. 103–116). Dependence of the formation of institutions on the progress in technological sphere that resulted from technological creativity, typical for the society, determines at the same time the need to initiate innovative transformations in institutional environment, as according to the researches, «technological creativity of Western society, since its inception in the monasteries and forests and fields washed over by rains, had two pillars – materialistic pragmatism, founded on the belief that nature can and should be manipu-

lated to increase economic wealth, and on perpetual struggle for political and economic hegemony among political actors. All that was the foundation for the institutions and structures of the stimuli without which stable technological progress was impossible» (Mokyr, 2014, p. 473). It means that there are both direct and indirect links between the development of the means of production and institutional environment. Having that in mind, we need to acknowledge that in modern conditions, when the possibilities of technological creativity and economic progress have not been exhausted under the conditions of the third industrial revolution and the fourth industrial revolution is near, the increase of economic well being will unfold on the basis of stable economic progress through the realization of new technological achievements in many types of economic activity. All this will cause growth of industrial production with increasing output. But one should not expect any changes for the better without respective changes in institutional environment, because «institutions are systemic patterns of societal expectations, self-evident prerequisites of accepted norms and habits of interaction, which impact significantly the formation of motivation and behavior of the groups of interconnected social sectors. In modern societies they as a rule take shape of governing organizations, such as a government or a firm, in which there are formal rules and rights to exercise sanctions» (Chang, 2005, p. 99). With this definition in mind, and in the course of deep transformational changes that Ukraine is undergoing, the new rules are to be continuously set and changes in organizational environment pertaining to a specific technological paradigm are to be determined. Hence the task of formation of relevant institutional changes that can have an impact on the formation and enhancement of motivation and behavior of interrelated social «agents», whose activities could make it possible to overcome, first of all, the well known dualism in the formation of institutional structure of our economy. This dualism is evident in the fact that instead of our economy's development on the basis of competition and innovations with capitalization of profits, it is oriented towards application of different schemes of enrichment, resulting from uncontrolled access to public material and financial resources, tax evasion, premeditated non-repayment of loans, abuse of administrative powers in the conditions of lack of meaningful regulatory environment and complicated administrative and licensing procedures.

To overcome this divergence between institutional environment currently existing in Ukraine and its path of economic development a wide spectrum of structural reforms should be introduced. These reforms should be able to terminate structural degradation of, first of all, the industrial sector of Ukrainian economy. There already is more than one piece of evidence of de-industrialization of the economy of Ukraine. This de-industrialization definitely leads to its backwardness, because the loss of the leading branches of industry, among which processing industries must be dominant, is a direct road not to enrichment, but to impoverishment of the country. That is why it is important that the structural reform policy, among other things mentioned earlier, institutionalize the development of industrial complex rather than its degradation. In other words, a new

level of application of institutional factors is needed, and the role of institutions as organizational structures ought to be changed along with relevant regulatory measures opening the way for raising investments in innovations to a new level.

A passage to an innovative investment model of economic growth in Ukraine that can be a basis for its modernization is determined directly by how successful its policy of improvement of investment climate is, and the results of this policy can only be deemed positive, if institutional environment and specific institutions are well developed, especially those that implement modernization projects of both micro- and macroeconomic scale. In my previous article on this topic (Gheyets, 2015, p. 4–17) a macroeconomic level of a number of key structural problems was highlighted. Relations between the business and the state are enhanced through the resolution of these problems as, on one hand, quasi-market attributes of the state are eliminated and, on the other hand, the opportunities of the state in using public savings are broadened and the processes of legalization of capitals for the investments into the economy of Ukraine are put on statutory basis. These investments can be used for economic modernization. These processes make it possible to overcome the abovementioned dualism in institutional environment of the nation. Thanks to the emergence of these institutional transformations economic growth is achieved. Utilization of knowledge – both previous and newly acquired – also takes place with this purpose in view, because the institutions promote technological modernization and accumulation of knowledge in the capital. The knowledge can be capitalized, if it is protected effectively. The latter issue is particularly topical for Ukraine, because Ukrainian jurisprudence is not yet able to protect either the owner's rights, or the copyright of new knowledge materialized in new technologies. We shall leave the legal aspect of this issue out of scope of this article. But we think that the state (and there has been a lot of examples of this in successful nations) can even under the existing conditions undertake the commitments concerning, for instance, the broadening of crediting of the economy via a specially designed entity that can in its turn initiate and to a certain degree even control credit extension of those sectors and businesses that it is primarily in charge of. In particular – and that is of utmost importance – of sustaining and developing manufacturing industries infrastructure, especially in the strategically important for the country and its economy sectors augmenting modernization processes. In practical terms it is all about the implementation of the elements of policy of economic pragmatism in a long time perspective. This implementation is first and foremost aimed at the development of infrastructure that in Ukraine is in the condition far from satisfactory. It includes a restructuring of banking system in order to prevent its disintegration, as it has not been possible so far to stop and reverse some notions of oligopoly in it. This particular issue was reviewed in the previous article to which reference was made above.

The process of emergence of capitalist economic system based on free market foundations is characterized in modern Ukrainian history by idealistic and

even romantic perceptions that capitalism has already become dominant economic system in Ukraine with market relations at its core. At the same time, Ukrainian entrepreneurial class, not having achieved tangible successes in economic modernization of Ukraine and thus not gaining authority among populace, has been herding its capitals not through the capitalization of the economy, but mostly through illegitimate privatization, direct embezzlement of public assets and funds, and has chosen the path of oligarchic control over the state building processes and many areas of public life. It was through these proceedings that Ukrainian big business has turned into an influential force of the capital, which though has been incapable of developing productive forces of Ukraine through economic and technological development that could give a positive impetus to the transformation of social relations and acceleration of social modernization of Ukraine. Reforms in Ukraine have not become «bourgeois», if we take into consideration that it was «bourgeoisie that, historically, has played a most revolutionary part... The bourgeoisie, during its rule of scarce one hundred years, has created more massive and more colossal productive forces than have all preceding generations together» (Marx, Engels, 1908, pp. 426, 429]. At the same time, an almost twenty five year period of reforms in Ukraine with the mentioned above attributes of the capitalist method of production should have been accompanied by respective agrarian reform with the surge and not decline of modern industry. But it has resulted in significant fall of production, bankruptcies of many industrial enterprises and their complete shutdowns.

Bourgeois revolution in the former Russian Empire at the dawn of the XX century that involved today's Ukraine ended in a civil war, after which this country was industrialized by means of political dictatorship and centralized planning with the known catastrophic consequences under future perspective, although it ought to undergo industrialization yet at the end of the XIX century. The main reason of the lack of success then and now might probably be related to the fact that «the bourgeois – rationalism elevated to the highest existential principle in religion» (Voieykov, 2015, p. 134) did not become one of the main attributes of the bourgeois method. This method ought to have well known requisites of bourgeois rationalism, which included:

- diligence;
- frugality;
- well being;
- honesty;
- punctuality (Sombart, 1994).

These requisites specifically have played in Ukraine their revolutionary role in the development of productive forces of both the labour and capital, and must

therefore become foundations for future upbringing of both the hired labourers and businessmen in both the short and the relatively long term perspective.

And one more substantial issue – raising the effectiveness and deepening of market relations in business institutional environment for both public and private property as a means of stabilizing the economy on its path out of economic crisis and of commencement of accelerated growth of Ukraine's productive forces grounded on capitalization of the economy. Capitalization should be the cornerstone of the broadened corporatization aimed at achieving such level of concentration of capital that can sustain the development of a modern corporation as one of its most efficient institutional forms with mergers and acquisitions being one of the forms of this broadening.

2. Corporation is the best developed organizational structure for business

Corporate form of ownership is today dominant in the developed countries, accounting for up to 90% of industrial production output. Corporatization of companies goes on dynamically in the other countries too, because, as J.K. Galbraith believed, a corporation is a very flexible institution, allowing – with various degrees of market influence dependence – to display different levels of adaptation to the requirements of the planning and of technostructure given the large size of such company and having accepted the uncertainty, typical for the market. The shape of this institution enables it to control the markets, where a corporation buys and sells. Besides, big size is absolute imperative for the sectors of the economy with costly equipment and comprehensive planning, where federal government is the only buyer (Galbraith, 2008, p.86). Such traits of a corporation as flexibility, variability and especially the size «...cannot be explained by the economies of scale. ... The proper explanation is that ... [it] is in the service not of monopoly or the economies of scale but of planning. And for this planning – control of supply, control of demand, provision of capital, minimization of risk – there is no clear upper limit to the desirable size. It could be that the bigger the better. The corporate form accommodates to this need. Quite clearly it allows the firm to be very, very large. The corporation also accommodates itself admirably to the needs of the technostructure» (Galbraith, 2008, p.88). Corporations became long ago a core of the industrial sector of economy, its activity being the source of the growing economic yield, as it is the corporations that concentrate investment resources in the prioritized sectors and locating thousands of their branches in dozens of countries, making possible cheapest access to their resources and exports of their products. The trend of the constant growth of the role of transnational corporations has become predominant in all world economy because of this form of business organization, because corporatization as a modern process

of institutionalization of economic activity allows to achieve positive transformations in industrial production worldwide through the increasing competitiveness of the exports via creation of global chains of added value. Effectiveness of the global added value chains is a result of the ability of transnational corporations (TNCs), who avail themselves of global liberalization processes, «to locate different parts of their production processes, including various service functions, across the globe, to take advantage of fine differences in costs, resources, logistics and markets. They exhibit an unending search for enhanced competitive advantage through the optimal geographic configuration of their activities» (World Investment Report, 2002, p.32).

As far as optimal geographic configuration of TNCs activities is concerned, according to the conclusions of the experts of the UN (see the report quoted above), it creates opportunities and problems for the countries with the economies in transition. The opportunities are determined by the fact that exports can be increased in those technology intensive sectors that can be developed in one country. The problems arise with the continual focus by the TNCs, especially in the recent period, on knowledge-intensive functions in value added chains. It raises the obstacles for relatively small and less competitive manufacturers in the countries with transitional economies. Because «the emerging global production system is increasingly open in terms of ownership, but with tighter coordination by lead players in each international production system» (World Investment Report, 2002, p. 38), in the countries with transitional economies, given the already existing and potential problems, an issue of transcending the ever growing technological and intellectual barriers arise. The alternative for them is to remain national suppliers of raw materials and semi-finished products in the already formed supply chains that will continue to emerge all over the globe. The countries with transitional economies will join these chains under the new conditions that were shaped out by the advances of liberalization of economic activity. In addition, as the results of research of V. Sidenco demonstrates, «... the orientation by the transnational corporations towards the establishment of strong and reliable basis for the supply of raw materials is growing, while at the same time the TNCs try to keep new technologies in both manufacturing and services in their home countries» (Sidenko, 2011, p. 106). Under these conditions any country is interested in consistent transition of its economy from exports of raw materials and low technology products towards at least mid-level technology-based and better still – technologically advanced products with high added value. These transitions do not occur though even in all the countries, where the TNCs have their affiliates. Successfulness of these countries «... depends on the strategy implemented by TNCs on the one hand, and on respective potential and policy of the host country... The model here is the success of national strategies... that combined the efforts of drawing the export-oriented operations of TNCs with development of internal potential ... it is here that the question of strategy arises along with the need to establish some room for maneuver in national policy» (World Investment Report, 2002, p. 45–47). This could only be done, where national policy, aimed at

the development of human potential is developed and implemented, first of all with regard to professional education of population, along with funding of scientific research and development of new technologies and innovations based on the results of this research. It should also include institutional support of necessary transformations that the government needs to introduce. Such policy forges the environment enabling joint activities in the territory of the country in national added value chains, especially in processing industries, engaging productive capacities of both the TNCs' affiliates and local producers oriented towards both domestic and foreign markets. In this environment their collaboration starts yet in the phase of joint innovative research and development in the interests of a host country, where a TNC's branch operates and where R&D work is done on a permanent basis.

There is an important element in the success of such work. In a country, where there are the affiliates of a TNC, national and corporate strategies are implemented in the existing and future niches of national and foreign markets. Institutional basis of these strategies are national corporations as the most successful modern institutional organization of an enterprise that can be made responsible for the implementation of the strategy of development of a country, first of all in industrial sector. It is on this basis that the affiliates of a TNC are involved in the activities beneficial for that country. The government assumes, along with mentioned above, the responsibility for the development of needed infrastructure.

Development of national institutional infrastructure through corporatization of business in the niches with good prospects in the foreign, and particularly in domestic market is a required prerequisite. Sufficient one is the notion that «... attractiveness of corporativism lies in the fact that it offers to turn the process of economic management into a «zero sum game». Here all the parties that take part in an accord (reached as a result of consensus in the settlement of controversies – *V. H.*) win, although some win less than the others... In a number of countries, where there are the organizations that protect the interests of the customers, this issue is to a large extent levelled» (Shamhalov, 2000, p. 18).

Both past and present international practices in a lot of developed and successfully developing countries has innumerable examples, when leading high technology businesses consistently institutionalized their operations, including the use of the so-called development institutes. Many of these businesses derived their successes from the long term public assistance that included creation and development of those businesses through protectionist policies, and through direct funding of both fundamental and application research and development up until now via various national programmes. Besides, among successful corporations there are those that today are under complete control of the government. In addition to that, in some countries in their today's practice of fighting the consequences of economic crisis a number of companies have been established and developed exclusively under the patronage of the state. Thanks to that the «points of growth» have been formed.

In the conditions of current economic difficulties in the European Union, when the rate of economic growth fell dramatically and the level of life of many strata of their population has been negatively affected, the rich countries can support them through social welfare. At the same time, in East European countries, where these options are limited, the solution «... has been to impose political control over strategic sectors to ensure wide access to the provision of essential goods and services... As a result, the free market is now likely to operate within tighter parameters all over the EU's eastern half... The goal is not national ownership but to avoid the risks to social welfare and stability implicit in a completely laissez-faire economy. ...when companies ignore accusations of profiteering, the government will make sure they stop making profits altogether. A revolution is stirring» (Eastern-Europe's Anti-Market Revolution, 2015). Contemporary corporate associations – depending on the situation in the economy of any specific country – are known to be able to both play a stabilizing role, and to be promoters of economic growth. It is important that they can also be used as a tool in fighting poverty, thus confirming the characteristic of corporations as rather flexible institution in economic domain despite J.K.Galbraith's statement that «... in American business world nothing is considered more illegal as the state's interference in internal affairs of the corporation» (Galbraith, 2008, p. 88). At the same time, at the far from idyllic times of crises the US corporations turned for help specifically to the government, as only the government could provide a source of needed capital. They, therefore, had to take into account the influence of the government on their decisions. The notions mentioned above bring about the proposition that protectionist policies allow establishing the new and sustaining the existing corporations that, on one hand, stimulate successful growth, including industrial one, as they become points of growth at the time, when the inroads for such growth are sought. On the other hand, they assist in sustaining the living standards at the time of crisis by applying what seem to be socialist methods, but that cannot and is not deemed sacrilegious. At the times of crisis it is considered, as a rule, quite acceptable. For instance, P.Krugman wrote that to fight the crisis that in 2008 created the threat of return of the Great Depression «It will come close to full temporary nationalization of a significant part of the financial system... finance should be re-privatized as soon as it is safe to do so. ... To save the financial system is somehow «socialism» (Krugman, 2009, p. 289).

Everything mentioned above allow us to say that corporations as economic institutes are not only reliable and flexible forms of organization of highly efficient businesses. Their organization also make possible to form the points of economic growth jointly with the state, and this is of utmost importance at the time, when the economy is searching for the ways out of crisis. This is of paramount importance for Ukrainian economy, which, having exhausted the options of renewable growth during the period of coming out transformational crisis at the beginning of 2000-ths and being drawn into modern systemic global crisis, again, having exhausted the options of the existing model of growth of global economy

through the so-called commercial expansion resulting in stagnation of external demand and manifold reduction of exports under the long-term fall of prices in commodity markets, has to look for the new variants of economic growth. These should have macroeconomic stability as their compulsory condition and structural reforms and resurgence of investment activity as their sufficient prerequisite. These reforms should take place in the new, improved institutional environment, in which corporations and hence corporatizations are among modern developed institutional forms. For this reason the author in his next article will review the practical meaning of the issue of corporatization and technological modernization of the economy of Ukraine.

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