

STRUCTURAL CHANGES IN EMPLOYMENT IN OLD INDUSTRIAL REGIONS OF UKRAINE

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The reforms in the former Soviet Union have been dominated by a lingering over-reliance on central institutions within the former republics. The economic character and needs of the regions within the republics are not being recognized adequately. Economic powers that are allocated to the subnational level in market economies are not present. Neither the center nor the regions have sufficient resources to restructure the regional economies. This paper proposes a system of Associations for Regional Economic Restructuring and Development. Their objective is to establish new enterprises and address the economic and social needs of the region such as employment.

Structural Adjustments on the Road to a Market

The principle of full employment is being realized in Ukraine at present. It means that everyone capable to work is ascribed to a working place. It does not mean nonetheless that he is really working. But the official statistics indicates very low rate of unemployment, about 1 or 1.5 percent, that is much below the one of Western industrial countries.

It is quite obvious that the largest number of unemployed will appear soon, and first of all in basic and mining industries. Eastern Ukraine, especially its industrial part called Donbass, is exactly the region with such an economy. More than 30 percent of population of the region work for coal mining, steel and chemical industries. There are some towns which economies are based on one industry or even one gigantic enterprise. From 70 to 90 percent of population in such towns as Artemovo, Belitskoe, Gornyak, Novogrodovka, Dimitrovo, Antratsyt and others work for coal industry. The destiny of the towns depends completely of the industry.

There is no argument that the selection of priorities for economic restructuring in the region must be made with due regard to the necessity of solving regions' major social problems and it also must lead to the creation of market economic environment in the region.

Structural changes in the economy are of a long run and capital consuming and they need their sound substantiation in advance. The first step in this line is to find out the rational directions for structural changes, to simulate an optimal structural shift and to evaluate the social consequences of changes. This work is the essential stage for the elaboration of concept for structural changes in the regions' economy.

There are many pitfalls on the road to the solution of the problem. The transition to a market in Ukraine and other CIS countries is being conducted under the economic crisis with virtually complete absence of any influence of market incentives and tools on the processes. To estimate in such conditions whether the directions selected for the restructuring are right one has to make a clear picture of ultimate consequences of the shifts in "a true market economy".

In fact the main question is like this: What would be the behavior of the region's economy if it were in real market environment? and as a result of that, What would happen with the region's economic structure in case the region was put in such environment for quite a long time.

The idea of the study was to simulate structural changes in the region's economy, that is in the Donbass' economy, being plunged into the developed market. Being surrounded by the competitive developed market the region would have to undergo through changes in its structure that would reflect without those distortions inherited by the Ukrainian economy from the Soviet economy actual demand of the world market. This forecasted structure and its dynamic might be taken for the essential point in estimation of the employment dynamic and would serve as a basis for elaborating a policy in this issue.

For getting an answer to these questions the quasi experimental approach developed at the Regional Research Institute of West Virginia University by A. Isserman has been used. The approach is based on the comparison of the behavior of the selected region with "the ones in the past". Those "regions from the past" are chosen by some criteria. Economy of the selected region and those "from the past" must be identical in other words. The advantage of the method is that it gives the direct access to the major regions' social indicator, that is employment, and breaks it down by sectors. Mathematically the method is quite simple.

The search of the region which is similar to the Donbass has brought to West Virginia. Location Quotients (Table 1) for both regions have shown great identity.

Table 1: PRELIMINARY COMPARISON OF ECONOMIC STRUCTURE

	LOCATION Donetsk Region	QUOTIENTS Compared to WV
More Specialized		
Machinery & Computer Services + Pub.Ed. + Sciences	3.04	3.82
Transportation	2.57	2.59
Farming and Forestry	2.38	2.14
Ferrous, Non-ferrous metals	3.20	3.54
Electric Power & Public Utilities	1.97	1.77
Coal Mining	2.81	3.03
Construction	1.35	1.85
Construction Materials + Glass, Clay & Porcelain	1.13	1.86
Less Specialized		
Arts, Culture, Health, Phys. Culture, Soc. Welfare	0.92	0.71
Communication Services	0.74	0.78
Retail Trade	0.43	0.39
Other Sectors of Material Production	0.33	0.24
Wholesale Trade	0.27	0.18
Lumber, Wood, Paper, and Allied Prod.	0.22	0.28
Govt Credit and Security + Pub. Admin.	0.08	0.05

Actual employment in the Donetsk region has not undergone through any changes for ten years (1985-1995). But being in the market economy similar to American one it would go through really deep structural changes over the same period (Table 2).

Table 2: A NUMBER EXERCISE: DONETSK REGION WITH WEST VIRGINIA'S GROWTH RATES, 1985-95

	Donetsk		Donetsk as WV	
	1985	1995	1995	+ or -
TOTAL EMPLOYMENT	2,554,300	2,460,200	2,452,982	7,218
Coal Mining	360,000	355,500	176,470	179,030
Machinery, Equipment, and Metal MFG	267,700	270,500	214,178	56,322
Construction	227,900	235,600	171,169	64,431
Farming and Forestry	225,200	203,000	224,753	(21,753)
Info&Computer	222,800	220,700	401,649	(180,947)
Serv.+Pub.Ed.+Science				
Transportation	220,800	176,600	174,723	1,877
Ferrous, Non-Ferrous Metals	198,900	167,300	98,184	69,116
Retail Trade	174,900	180,300	198,062	(17,762)
Arts, Culture, Health, Phys. Culture, Soc. Welfare	157,600	174,400	224,454	(50,054)
Electric Power & Public Utilities	135,800	131,500	140,933	(9,433)
Const. Materials + Glass, Clay & Porcelan	70,800	62,000	37,462	24,538
Consumer Goods	56,300	63,700	43,778	19,922
Chemicals and Petrochemicals+others	49,500	50,100	36,961	13,139
Govt Credit and Insurance + Public Administration	46,000	33,300	46,337	(13,037)
Manufactured Food and Kindred Prod.	43,500	50,200	28,190	22,010
Other Sectors of Material Production	34,500	33,000	44,342	(11,342)
Wholesale Trade	31,000	20,000	29,308	(9,308)
Communication Services	23,600	22,100	20,889	1,211
Lumber, Wood, Paper, and Allied Prod.	7,500	10,400	7,947	2,453

But, and that is a remarkable result of the simulation, the overall employment would not be reduced. New sectors of the economy would grow fast. The falls of employment in some sectors would be compensated by the growth of others. That is, by the way, the case of West Virginia development in the 1970s where unemployment rate drooped from 7 to 3 percent. The study has shown that the most rapidly growing sectors of American economy have not experienced any significant increase in the

Donbass economy and on the contrary the American declining industries remained stable in the Donbass.

One major conclusion which might be drawn from the study is as follows: the Donbass is not in such a hopeless situation that it would not be able to cope with deep structural changes in its economy. The fear of big rate of unemployment in the region has a solid ground and is quite realistic. But the unemployment might be overcome through drastic economic reforms. The progress in economic reforms in Ukraine is far behind of those needed to create economic environment similar to the one in the model. So, we have to speed up our reforms to reduce enormous unemployment which we will face in the near future. The simulation has shown those specific sectors of the economy which can provide fast absorption of unemployment in basic industries. It also provide the scope of such absorption within a 10-year period.

But now another critical issue arises: What is the role of the regional bodies in implementing of the restructuring? Who organizes and conducts structural economic policy in old industrial regions?

Organizing the Region for Economic Restructuring

Most of the distortions in the economies of the former Soviet Union are thought to result from poor decisions by central planning institutions. These distortions are considered so serious that no one particular region will be able to overcome them by itself. All the regions of the former Soviet Union are equal in that sense. Appalling defects in the structure of the economy have been deliberately formed more or less evenly all over the former Soviet territory.

Partnership must be accepted as the organizational basis for economic restructuring of the regions. Being overburdened with present economic problems, the regions do not have the resources for any sufficient solution to their problems. Perhaps the way out of such a mass of contradictions within the regions should be sought in the experiences of other countries. For instance, 12 regional corporations were organized in Alaska in the 1970s (University of Alaska 1985). They covered the whole territory of the state. The corporations were set up as capitalist firms. They were to make their livelihood by setting up businesses to use those state lands and natural resources that had been allocated to them. As one leader of a regional corporation explained, the corporation combined both capitalist and socialist aspects. The capitalist origin of the

corporation displays itself in the production sphere. The corporation tries to earn as much profit as possible and is no different from any other firm in this sense. The socialist origin manifests itself in the distribution of the corporation's net income. One of the main principles of this distribution is to achieve maximum social justice for the entire population of the region (University of Alaska 1985). The search for new institutions to promote social and economic development under the current conditions in the former Soviet Union should follow similar directions. The regional administrative boundaries should coincide with actual economic regions.

A key issue in restructuring economic activity is generating investment in urgently needed and costly projects in the region. At present the national government cannot provide investments, as it did within the planned economy. The system of central allocation of investments through ministries and their structures is no longer in place. Ministries no longer collect funds from the enterprises, which they could then invest. State budget allocations to the ministries have also been reduced dramatically. Yet, neither has the previous system been replaced with any territorially organized system of central allocation of investment. Given the dismantling of the centrally planned mechanism of investment, new organizational structures must be invented to provide the necessary investment in regions during the transition to a market economy.

The current regional budget system of Ukraine entails dependence on the central budget with substantial flows of funds between the regions and the republic. The regions get only one third of the taxes collected on their territory. In the Donetsk region, for example, 85 percent of the two major revenue sources (value added tax and income tax) go to the central budget. As a result, the revenues remaining for the region are barely enough for the current social programs. Very little is available for capital investments. As the economic situation in Ukraine gets worse, the regions' budgets are shrinking faster than the central one. The central budget itself only suffices for current basic needs of the nation. Nothing remains for investments in the regions. There is at present no serious redistribution of money from the center to the regions.

In countries with developed market economies, the share of the regions' budgets in all governmental budgets ranges from one-half to two-thirds. Because of the general transition to a market economy in Ukraine, even more substantial financial support of regions is needed to enable them to carry out their socio-economic responsibilities. The practice of tax distribution must be changed to make regions more financially strong than they are now.

No bureaucratic superstructure of the central government is needed for regional economic restructuring programs. It also is unrealistic under market conditions to set up an organization for carrying out economic restructuring and development programs without evident economic benefits for all participants. An organization dealing with economic restructuring in a region should be profitable. Furthermore, any regional restructuring organization must work on social issues of the territory. Goals, such as creating employment opportunities, maintaining income, protecting the environment, and ensuring public health, must determine the main directions of future development of the region's economy. Profitability of restructuring measures should not be the only criterion. At the same time, the scale, rate, and trends of the restructuring should be within the resources available to the regional organization.

Associations for Regional Economic Restructuring and Development

One way to implement these principles is to try to generate money for investments within the region by forming a network of regional associations of businesses. They would combine the funds of different enterprises to create sufficient revenues for sound investment projects. At present, enterprises have their bank accounts in branches of the State Bank. The money of the enterprises, until it is involved in transactions, is under complete control of the State Bank and does not generate any substantial revenues for the enterprises. The State Bank usually uses the money for investment projects, not necessarily in the territory that generated the funds. In short, neither the state, the ministries, nor individual enterprises have the necessary funds for the big investment projects so urgently needed in the regions. Furthermore, an enterprise, using the system of state banks, cannot generate even average commercial returns. Temporally unused, the enterprise's money is just idle.

Regional unions of enterprises and local governments could have the combined resources needed for the radical restructuring of the regional economy. These unions might be called Associations for Regional Economic Restructuring and Development. A few large enterprises in a region could found their region's Association. They would pay fees big enough (millions of roubles) to set up a Commercial Bank of the Association. Enterprises and organizations not able to pay the fees would pay membership dues. Membership dues along with part of the fees would be used to form and maintain the administrative bodies of the Association.

The supreme managing board of the organization could be the Council of Overseers of the Association. It would include managers of all leading enterprises, organizations, and local government representatives with equal rights. The main obligation of the Council of Overseers would be to select major investment projects for economic restructuring, as well as social programs for raising the standard of living in the region. The set of these projects and programs need not include those planned by individual enterprises. Only projects most likely to make major contributions to the economic restructuring process within the region are evaluated and implemented by the Association. The Council determines what percentage of the Commercial Bank's investments will be obligated to the selected industrial projects for regional restructuring. It also organizes studies of effective directions for the economic development of the region and nominates the Board of Directors of the Association and the Board of Administration for the Socio-Economic Development Fund of the Association.

To be able to put the strategy into practice, the Council of Overseers creates the Board of Directors. The Council provides the Board with authority to deal on behalf of the Association, to undertake financial transactions, to sign contracts with different state and private companies, and to provide material and technical supplies to enterprises of the Association. In all its activity, the Board of Directors is accountable to the Council of Overseers and regularly reports to the Council about its activity.

The Commercial Bank of the Association is formed in the region to provide an investment source for different business and social projects. It is set up as a joint-stock company with firms and individuals from the region taking part in its creation. The controlling interest in the hands of the Council of Overseers guarantees that the recommendations on priority investments for restructuring the region are followed by the Bank. Everything constructed using the loans granted to the Association by the Commercial Bank becomes the property of the Association, which can sell the properties to other companies or individuals.

Firms and individuals from other regions can become shareholders of the Bank. Except for the investments designated by the Council of Overseers for restructuring projects, all bank loans are made on a commercial basis at the highest possible interest to generate maximum revenues. Thus, the Bank raises revenues and creates more resources for selected restructuring projects. The Bank can use its money for profitable projects all over the republic.

Administratively, the Bank does not depend on the Council of Overseers or the Board of Directors. The Bank is an independent financial institution operating on a commercial basis under the control of its shareholders. The shareholding founders (the entities that contributed the initial fees) hold the controlling interest and therefore control the activity of the Bank. This mechanism is the main guarantee that the loan policy will support restructuring projects.

Freed of direct administrative control by the Association, the bank need not spend money on loans for unprofitable projects and can concentrate its resources on those with the highest returns. This independence stimulates the Bank and the Association to look not just for employment producing projects, but also for truly profitable ones. At the same time, it eliminates from direct influence those politically powerful Association members that did not contribute fees to set up this financial structure.

To solve the most acute social problems in the region, the Association creates its Socio-Economic Development Fund. The Fund makes investments in social and cultural projects in the region and forms new, separate enterprises. The social projects of the Association will not duplicate those of the local government or any enterprises. They are aimed at overcoming extremely severe social problems related to the transition to a market economy. The resources for the Development Fund might stem from regular deductions from the income of enterprises that own the Association, voluntary payments of the Association's members, deductions from the Commercial Bank returns, and contributions and donations by other organizations and individuals. The social infrastructure projects would be selected by the Association through the Development Fund on a competitive basis just as it funds production investments.

The Council of Overseers, as the supreme administrative organ of the Development Fund, makes decisions on priorities for different social programs. The Council creates the Board of Administration of the Development Fund to conduct its current management. To work out a strategy and to elaborate a set of specific projects for economic restructuring in the region, the Council establishes the Regional Scientific Board of Economic Development. The Board consists of prominent scholars and practitioners from different sectors of the economy who elaborate a number of alternative economic restructuring strategies for the long-run and the near future. The set of alternatives proposed by the Scientific Board is a primary source of the projects to be financed by the Commercial Bank after they have been adopted by the Council of Overseers.

To guarantee maximum social justice in using resources of the Development Fund and to achieve the highest responsiveness of public opinion in the region when selecting social projects, a Committee of Working People ought to be established. The Committee has the mission to rank, in accordance with the priorities of the majority of the population, alternative projects in the social sphere of life. Being master of the Development Fund, the Council of Overseers selects the specific set of projects to be financed from those proposed by the Committee. Although the Fund is not meant to be profitable, the Council of Overseers prefers to finance projects which are able to repay at least part of the money. The projects should have a maximum effect on the social development goals.

Conclusion

Associations, similar to the one described above, have recently been created in the Donbass region of Ukraine (Shachtersk, Donetsk, and other places) to provide economic restructuring of the region in its transition to a market system. The Association as a regional restructuring organization has the advantages of a self-financing enterprise. It does not interfere in the economic independence of firms and companies already existing in the region. It purposefully creates a new economic structure and builds enterprises in new industries with advanced technologies that are competitive in the world market. It responds to market demand and permanently coordinates the region's productive activity. The Association also meets some social and productive needs of the region that have not been satisfied by the existing management institutions of the republic. The Association is a private commercial organization, working on the basis of market laws. Its principles of management, financial rules, and relations among its subdivisions and with other firms and companies follow the private capitalist approach to business.