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**ECONOMIC INERTIA AND ECONOMIC GROWTH: IS THERE  
ANY CONTRADICTION?**

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**Abstract**

The article is devoted to the phenomenon of inertia in economic development which hinders the modern economic growth. A variety of factors causing the inertia is revealed including instability of world and national economy and unfavorable geopolitical environment. The economic growth and economic inertia are shown in its dialectical unity. We also bring to light factors which exacerbate the reduction in the rate of the Russian economic growth and the risk of recession escalation. On the basis of economic forecasts which are given not only by official government bodies but also by alternative nongovernment institutions we explore the reasons of economic inertia and also show the urgent need of an effective mechanism for overcoming inertia in a recession phase of economic development. The mechanism takes into account modern challenges and threats to Russian economic resilience. The article contains the general description of the mentioned mechanism particularly on both institutional and structural policy level.

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**Keywords:** Economic inertia; economic growth; economic development; recession.

## 1. Introduction

In modern Russia, it is evident that there is an increasing need to create the basis for the economic growth, to stimulate the development of domestic industries in situation with negative external factors and stagnation trends. The aim of our research is to determine the rationale for the establishing of a mechanism to overcome the inertia of the economic downturn, aimed at creating a new concept of the



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economic growth based on the industrial development. It requires an effective institutional policy aimed at creating favourable conditions for overcoming the general economic crisis.

Currently, the Russian economy is characterized by unstable dynamics, reducing the speed of development and lack of positive structural changes. The crisis is revealed in the decline of investment and income, in an unfavourable fiscal situation and high inflation. In 2015, investments in Russia fell by 5.7%, the index of industrial production - by 3.3%, the gross domestic product - by 3.7%, the index of physical volume of production - by 5.3% (Effectiveness of Export, 2015).

In this context, the contradictory results of the anti-crisis measures undertaken by the government have not led to a change in trends in the economy and to an improvement of the socio-economic situation in the country. The crisis emerges in almost all Russian regions and in all sectors, although at different speed. The analysis shows that currently the overall trend is an escalation of economic problems and a consolidation of downturn inertia.

## **2. Methods**

### **2.1 Dialectics of Economic Growth and Economic Inertia**

In the most general terms, economic inertia is a property of the economic systems and objects to maintain or slowly change status quo. It reflects the degree of development and the stability of economic relations, as well as the ratio of the interacting socio-economic forces. Economic inertia is due to, "on the one hand, the scale of large economic units, the degree of economic "mass" and, on the other hand, the inertia of individual and organizational agents in management of economic objects and processes" (Raisberg et al., 2011). Study of the problem of stimulating the economic growth via inertia implies taking into account the whole variety of interacting forces, finding out how changes in the economy may themselves give rise to not only drivers, but also obstacles.

The inertia is one of the most obscure phenomena of the economic theory. Inertia as a characteristic of economic system implies that the system requires some time to change the state and rate of development after it has been influenced by some control actions. Inertia is a contradictory phenomenon. High inertia can be perceived as a positive feature in the case of weak sensitivity of the economic system to external perturbations (preservation of its stability during the economic crisis). It can also act as a negative feature, showing insensitivity (immunity) to external control actions. Minor inertia of the system is also characterized by positive (high control) and negative features (response to random perturbations) (Sidnina, 2003).

It is known that the mechanism of functioning of any economic system is determined by feedback, i.e. reactions to the impact intervention. The analysis of inertia allows providing insight into the structure, direction and rate of economic development, the result of which will be a variety of options for development scenarios for a certain period of time. The inertia affects both the parameters of sustainability and variability. Inertia gives stability while maintaining the existing parameters of positive development trajectory, and affects the variability preventing new relations, properties and characteristics in the given system.

The economic inertia in recession means the specific inertial mechanisms that reflect the contradictory nature of modern economic development. They are revealed in a complex interrelation and

interdependence of the whole set of constraints on local development. Due to the action of inertial mechanisms, financial resources of the federal budget which aim at the economic stabilization and regional investments do not bring the expected results. Development programs and projects also do not get the economy on a path of sustainable growth.

Disclosure of the nature and structure of the economic inertia is necessary for the development and application of effective institutional measures and solutions aimed at creating appropriate conditions and models of economic policy. The last (conditions and model) should be focused on improving the economic sustainability, stimulating the economic growth and reducing depression focal points in the economy. Specific inertial mechanism, which is inherent to the modern economy, contributes to the emergence and strengthening of major structural and institutional distortions at both the macro- and the mesolevel. It neutralizes the efforts and results in a waste of resources which are spent on economic situation changing, on the support of "risk regions" fiscal capacity and on promotion of the economic growth and socio-economic development. In the long run, such mechanism can produce and tighten the symptoms of an economic depression, consuming resources which are allocated to induce the economic growth (Afonasova, 2015).

The economic inertia is the result of a complex interaction of accelerating and decelerating factors in the economy, progressive and regressive changes happening in the country. Nowadays, the main factors of the Russian economic inertia are:

- a relatively low level of income and substantial sectoral wage disparities;
- disparities in national and regional economy;
- limited access of enterprises to financial resources;
- lack of attractive investment projects in industrial enterprises with high growth potential;
- geodistance and transport infrastructure underdevelopment of certain regions;
- a low level of inter-ethnic, inter-regional and inter-municipal cooperation (relations underdevelopment);
- insufficiently developed institutional environment which increases the transaction costs, which in turn determine the nature of contractual relationship, ownership structure, development strategies and, as a result, effectiveness of both private projects and the national economy as a whole.

The above-mentioned factors may be referred as inertial constraints that discourage the economic growth. They confront, compete with the so-called growth-accelerating factors which stimulate the economy.

Growth-accelerating factors can be the following:

- restoration and development of industrial and innovative potential of the economy, the emergence of new industries, opening of new businesses, job growth;
- reducing Russian technological underdevelopment, which results in non-competitiveness of products and services;
- high-quality human capital (high share of employees with higher education of the total number of employees);
- rich natural resources (significant reserves of oil, gas, iron ore, timber and other natural resources);
- relationship restoration and the growth of trade with the European Union, which was the main trading partner of Russia, and which accounts for half of all Russian trade;

- development of industrial, transport, investment, innovation and other types of infrastructure to ensure a congenial investment, technological and entrepreneurial climate for the development of the domestic industry;

- effective institutional reforms aimed at the foundation and development of new industrial facilities, industry funding, creating a congenial environment for the development of technological and industrial business.

The competition between these two groups of factors - accelerating and inertial - leads to different modes of functioning and development of the national economy. On the one hand, the mode of intensive growth and the economic process can be obtained if growth-accelerating factors will dominate inertial elements. On the other hand, there may be a more valuable mode which reduces the effectiveness of economic processes, if the inertial factors will be more critical than growth-accelerating ones. It is obvious that in Russia, in the last three years, inertial constraints dominate that has led to a decrease in the intensity of economic processes. According to the economic forecasts, it is almost impossible that the financial and economic situation will be improved in 2016-2017 because the inertial trend of economic slowdown has entrenched. It is supported by the negative dynamics of reproduction caused by the low level of economic security and high riskiness. That means that the emergence of risks is far ahead of the creating of instruments and mechanisms of economic security. As a result, there is low adaptive capacity of the Russian economy, predetermining its inability to block the negative factors which leads to the slowdown and to the reduction of its protective properties against, firstly, new challenges and threats, secondly, continued inertia trend, and finally, a rise of structural and other imbalances.

In order to overcome the economic inertia and to create conditions for the economic growth, a set of particular institutional arrangements are required which are aimed primarily at supporting the Russian industry, its high-tech sector, creation of new jobs, elimination of obvious structural imbalances. The institutional capacity of public authorities in modern Russian conditions should be implemented through control of re-industrialization through the production of effective institutions that govern the creation, operation and interaction of economic agents. This will help to solve such important tasks as the formation and establishing of new industrial enterprises, the development of industry financing institutions, the improvement of Russian enterprises competitiveness, and the development of domestic demand for domestic products.

### **3. Results**

#### **3.1 Influence of Economic Inertia on Modern Russian Trends and Policy**

Economic inertia can lead to serious economic problems such as rising inflation, decline in production, foreign capital drain, and lack of investments.

Over the last three years, the capital drain amounted to nearly 300 billion dollars. The state budget balance has essentially decreased, and consequently the potential for state development is being exhausted. According to official data released by the Ministry of Finance of the Russian Federation (The Deficit of the Regional Budget, 2015), the regional budget deficit in 2015 exceeded 600 billion rubles. Actually, the situation is much worse. In many regions, major energy and communication projects are

blocked. And this, in turn, is also a factor which slows down the future economic growth and fixes the inertial tendencies.

Growth-accelerating measures suggested by the Russian Government, result in two basic scenarios. The prosocial oriented policy makers in the Government propose the idea of restarting the growth model of 2011-2013 which was oriented on domestic demand, supported by rising incomes in the public sector.

An alternative to this is the scenario of the Russian Ministry of Economic Development, based on the tight monetary policy of the Central Bank of the Russian Federation, involving the decline in inflation by monetary measures to 6.5% by the end of 2016 and to 4% by the end of 2017, the continuation of reduction in real disposable income – 2.8% in 2016, and 0.3% in 2017. The reduction of real pensions should be even greater: 4.8% in 2016 and 2% in 2017, with further indexation for inflation until 2019. According to calculations of the Ministry of Economic Development, this policy will increase the number of the poor from 13.1% in 2015 to 13.7% at the end of 2017, with a peak in 2018 at 13.9%, and return the real incomes of the population and the number of poor to that of 2015 year in 2019 (The Ministry of Economic Development Proposes, 2016).

However, it is not enough to have low budget deficits and low inflation for the Russian economy to grow. The target scenario of the Ministry of Economic Development does not suggest any business environment or structural improvements or any radical changes in the structure of investments until 2019. The scenario of the Ministry of Economic Development of the Russian Federation, however, assumes the growing support of non-resource exports and localization production, as well as the rapid closing of energy non-efficient production. It is projected to provide a reduction in energy intensity of industry by 2.5% per year.

There is another scenario for the economic growth which is based on priority support of medium high-tech companies, which involves "manual control" in the economic policy and support of medium-sized companies. This scenario involves overcoming of strong resistance of the infrastructure monopolies' and the military-industrial complex' lobby. It is important that the "manual scenario" proposed by the Ministry of Economic Development, has the finite time horizons. In 2020, regardless of whether the economy of the Russian Federation will reach the GDP growth rate of 4.5% per year or not, public funds for its further stimulation will be mainly spent.

Therefore, as a basic scenario with maintaining the inertial trend for the coming years we can consider a scenario of deterioration of internal and external conditions for Russian economic development. In this scenario, one should expect low or zero growth rate due to a slowdown in domestic demand, the limited possibilities to increase productivity, continuing of economic sanctions and restrictions on access to external investment resources. At the same time, the most important task is to create conditions for the transition to a new model of the economic growth, which follows in an increase in business activity, in the labor productivity growth, in the emergence of long-term investments, and in the expansion of economic sectors, focused on the production of competitive products with high added value.

In these circumstances, it is urgent to establish specific development institutions and mechanisms to overcome the inertia of the economy, which would be aimed at the realization of the economic growth, stimulating economic activity in the Russian regions.

The mechanism of inertia overcoming is one of the economic mechanisms which includes a set of methods, forms and tools of impact on the financial, economic and social processes. In the most general

terms, it can be defined as a highly organized structure, forming a framework in which the socio-economic processes flow; different structures and institutions interact; principles, forms and methods of management are implemented; the coordination of public, group and private interests are made; and economic development is provided.

The concept of an anti-inertia and growth-accelerating mechanism, in our opinion, should be based on the principles of congruence between business entities and forms of interaction, on the reflection of interests of economic agents in the economic policy, which is organically inscribed in the context of re-industrialization strategy supported by relevant institutional changes.

Thus, the solution to the problem of inertia overcoming and the implementation of structural economic changes lie in the institutional transformation context. Another suggestion is the formation of specialized development institutions conducting the modernization program of the leading industries, first of all - engineering and metalworking.

#### **4. Conclusion**

Thus, the dynamics of national economy is determined, among other factors, by its inertial properties, its resistance to inertia, the cognitive persistence of individuals and official bodies, as well as by the time required to change one kind of inertia to another.

Since inertia is a universal property of economic systems, the variety of its expressions determines the diversity of approaches to its analysis and controlling in the context of the inertial slowdown. The points at the primary issue are the institutional arrangements needed to address the major problems of economic development.

Effective institutional arrangements, aimed at creating an appropriate environment for the economic growth and development to reduce the negative effects of economic inertia, are needed. Institutional changes should be aimed at the adjustment of the existing institutional rules and their consistency, which will help to overcome the distrust to the formal institutions, the elimination of the existing institutional traps.

Therefore, recovery and effective development of the Russian economy can only be subject to the creation of an adequate institutional framework in the form of a set of tools and mechanisms that contribute to stimulate the economic growth.

And finally, the inertia of the national economy is due to the long-existing structural problems, exacerbated by the economic crisis, the sanctions pressure on the Russian economy and the turbulent environment. In the context of the lingering crisis, it becomes more and more obvious to observe a variety of structural, institutional, and as a result - behavioral abnormalities of economic structures. As a result, the snowballing accumulation of such processes makes the economy less efficient and less competitive. The economic system loses the ability to positive strategic changes, and on the contrary, more often it reproduces and fixes in the internal environment a set of conditions and factors that are unfavorable for the future economic growth and development.

All mentioned above requires a serious analysis and identifies the causes of the economic anomalies associated with the action of inertial mechanisms in the economy that contribute to the preservation and consolidation of inefficient institutional forms. Functioning of inefficient institutions

leads to resource deficit that hinders the economic growth and thus reduces the potential for the development of the national economy.

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