The Donbass Economy: State, Development Trends, and Forecasts

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Abstract—The article, which is a continuation of the study of the problems of economic development in conditions of limited opportunities, published in the journal for 2018, offers an interpretation of predictive scenarios for the development of the autonomous Donbass. An assessment of the general state of economic development of the DPR in the period 2014–2021 is given, the expected trends in the development of the economy are identified, the main internal and external problems of economic development are identified, growth prospects are outlined in key manufacturing industries that have the potential to contribute to the achievement of structural optimality of the economy.

Keywords: state regulation of the economy, territories with limited economic opportunities, trends, development scenarios, forecasts

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State formations with limited economic opportunities have different aggregate economic potential, on which the effectiveness of their functioning directly depends. They are faced with issues of insufficient economic resources, restrictions on the import of raw materials and other materials, export of finished products, etc. because of the existing problems of a political, economic, social and even global nature that impede development processes. The tendencies of the emergence of new state formations, which, in fact, are territories with problem sovereignty, generate scientific interest in the study of problems associated with the management of their economy [1–10], including, in particular, geopolitical, conflictological, and legal aspects. Taking into account the undeniable importance of these aspects, it should be noted that there is insufficient work on the economy of such territories. The available studies in this area indicate the prevalence of their economic development on the basis of external, humanitarian aid, with all the multivariance of subsequent scenarios. Solving the economic problems of such territories, which include the Donetsk People’s Republic (DPR), requires expanding their economic opportunities, full access to the resources at the disposal of the territory, and their effective use in order to improve the quality of life of the population.

The DPR, despite the systemic crisis in the economy, remains an industrial region. In 2020, the processing industry accounted for half of all manufactured products. In the structure of the processing industry, about 20% is accounted for by metallurgy, 18% by the food industry (the growth rate for the year was 11%), and coke production, 6%. In 2020, significant growth took place in the pharmaceutical and light industries (by 2 and 1.7 times, respectively). Production in the chemical industry increased by 25%. In general, the general structure of the volume of sold industrial products by type of activity did not undergo significant changes in comparison with previous years.

The DPR economy, like the world economy, has felt the impact of COVID-19, which forces us to think about the role of government regulation in a crisis caused by a prolonged pandemic [11–13]. In 2020, compared to 2019, the volume of industrial products sold by enterprises of the Republic decreased by 22.4%, which was due to a decrease in metallurgical production (1.6 times), extraction of other minerals and quarrying (by 48.4%), production of coke and petroleum products (30.4%). In the light and pharmaceutical industries, as noted above, the volume of sales increased by 1.7 and 2 times, respectively. The volume of retail trade in 2020 compared to 2019 increased in comparable prices by 20.6%, and the volume of wholesale trade by 15.3%.

The foreign trade balance in 2020 remained negative and amounted to 72.4 billion rubles, which is 1.5 times more than in 2019. At the same time, almost 90% of foreign trade turnover falls on Russia.

The situation on the labor market in 2020 is characterized by unfavorable trends. The decrease in the average number of full-time employees (1.7%) and the number of hours worked, along with a decrease in the volume of industrial products sold (22.4%), became the reasons for the decline in labor productivity in 2020 by 19.8%.
The average monthly wage of a full-time employee in 2020 increased by 21% and amounted to 15.48 thousand rubles, the real wage index for January–December 2020 to January–December 2019, 110.8%.

As of 2021, 932 industrial enterprises operate in the DPR.

Assessment of the current state of social and economic development of the DPR based on the dynamics of data on the volumes of sold products of industrial enterprises of the DPR over seven years (2013 Donetsk region) [14] allows us to speak about an extremely moderate economic recovery, insufficient to produce sustainable economic growth. At the same time, such an assessment makes it possible to carry out predictive calculations of the options for the development of the economy of the republic for 2020–2025 (Fig. 1).

Forecast calculations for 2020–2025 were carried out on the basis of official data on the volume of products sold by industrial enterprises in the DPR for 2013–2019 (in connection with the current restrictions on the provision and dissemination of generalized statistical information in the interests of information security of the DPR) and analysis of significant patterns in the development of the economy of the Republic.

The inertial forecast assumes the preservation of the current level of sales of industrial products.

The optimistic forecast is calculated on the basis of the hypothesis of an annual growth of 2.5% (the minimum conditional estimated estimate of the economic growth rate necessary to reach the minimum growth rate of welfare).

A forecast with a negative economic growth (−3%) is presented based on a preliminary assessment by Rosstat of the state of the Russian economy at the end of 2020, i.e., −3.1% [15]. The forecast takes into account the prerequisites for a decrease in the growth of the world, as well as the Russian economy, to which the DPR economy is affiliated. The projection of these circumstances onto the current situation in the Republic suggests that the decline in economic growth may be an order of magnitude greater.

The republic continues to restore the ruined economic system, eliminating problems of its functioning. But at the same time, it is necessary to recognize the inevitability of a decrease in the economic growth rate of the DPR, at least in the short term, which is due to the following objective reasons of an internal and external nature [16].

Firstly, the peculiarity of the current economic system of the DPR is “manual control,” which, on the one hand, is necessary in the current conditions as a way to effectively control an emergency situation in order to stabilize it and eliminate negative consequences. At the same time, the duration of manual control in any economic system testifies to the manifestation of an institutional crisis and its deformation.

Secondly, the powerful influence of the geopolitical factor on the uncertainty of the economic development of the DPR creates a high degree of risk for the stable development of the Republic’s economy; at the same time, the formally undefined prospects of political and economic cooperation and economic cooperation with the Russian Federation cannot yet be considered sufficient for increasing the rate of economic growth. The geopolitical factor to a certain extent limits the possibilities of the DPR as a state and as an operating economy in implementing the development policy of the Republic. This means that the DNR’s economy should function, taking into account the risks of uncertainty about development prospects, and will be forced to eliminate real and calculate potential economic threats in order to mitigate them in a timely manner.

Possible scenarios for economic development trends are calculated based on data on the volume of sales of industrial products in the DPR in 2016–2020 (Fig. 2).

Prerequisites and assumptions in determining the expected development trends are the following provisions.

Not all possible scenarios are considered, but the classical forecast trends of possible economic development, which have precedents/analogies in other countries and are used in a scientific and expert environment. To identify such scenarios, the method of scenario factors is used, which makes it possible to identify “forks” – key development alternatives. What

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1 Ministry of Economic Development of the DPR on economic development and investment climate in the Republic. 08/02/2021. DNR LIVE. http://dnr-live.ru/mer-o-razvitiyi-ekonomiki-i-inves-titsionnom-kliamte-v- respublike/. Cited August 2, 2021.
these vectors of development will actually be depends on the actual trajectory of the DPR’s economic development, on the economic and political situation in the states bordering on the DPR and on other interest groups in terms of the situation in Donbass.

When making forecasts based on changes in the volume of sales of industrial products, the impact of its dynamics, reflected by the cumulative total, on the economy of the DPR is taken into account.

It is conventionally assumed that the DPR budget revenues are equal to the actual budget expenditures.

A hypothesis is put forward about the beginning of the recovery/revival of the DPR economy in the period from 2021.

The objects of the forecast are the available official data on the dynamics of changes in the total sales of industrial products in the DPR, as well as on the key sectors of the economy: metallurgy, machine-building, and coal mining.

At present, the factor of uncertainty in the economic development of the DPR directly affects the variants of possible trends in the development of the Republic’s economy and determines significantly different assumed trajectories of socioeconomic dynamics:

— A negative development trend reflects development with insufficient financial and human resources.
— The inertial trend shows the preservation of the current rates of economic development.
— A positive trend is characterized by a rather high dynamic of economic development and is likely when solving political issues about the status of the region and the forced inclusion of the DPR in international economic relations, formal legalization of the integration of the economies of the DPR and the Russian Federation, which will help to attract investments, technologies, and labor resources.

Note that in order to make strategically important management decisions at the state level, the level of individual corporations and other levels of economic management, it is necessary to take into account the entire range of possible options for the future development of the DPR economy.

The least desirable trend, of course, is the negative trend in the development of the DPR economy, which is formed as a result of chronic insufficiency of financial, production, human and other resources.

The inertial scenario of economic development in the DPR, which is distinguished by a combination of high cost parameters and minimum values of target indicators, should also be considered ineffective.

The variant of a positive trend in the economic development of the DPR is undoubtedly the most attractive, and if at least some institutional transformations are carried out, it can lead to some growth in economic indicators, but at the same time, there will be no fundamental improvement in economic development without structural reforms.

In the DPR, there is a need to change the structure of the economy and achieve a significant increase in labor productivity based on modern technologies. Diversifying the economy in favor of the manufacturing industry allows for high growth rates, longer periods of growth, and a decrease in its volatility, which supports growth in the long term. The processes of economic changes taking place in the DPR, caused by a decrease in economic activity in heavy industry and industrial production, suppress the potential for economic development, limiting the possibilities of using new technologies in production and leading to low labor productivity. It is necessary to understand which industries provide the process of economic growth and how technologies can be modernized in these industries. Innovation in manufacturing processes affects productivity in different ways across industries, altering the structure of output, employment and exports.

The metallurgical industry in the DPR potentially has the greatest positive development trends, provided that stable production is ensured, the development and modernization of production capacities of industrial metallurgical enterprises2 (Fig. 3).

The principle of the general strategy for the development of the DPR’s economy can be the priority development of high-tech industries in the economy of the Republic, including the sectors of mining, processing, and transportation of coal (Fig. 4).

The coal industry needs to be restructured, maintained and developed to ensure energy security3. The growth of coal production and the efficiency of its use, 2 Joint statement of the Heads of the DPR and LPR on the transfer of branches of CJSC Vneshtorgservice under the management of a new investor. https://dan-news.info/official/sovmestnoe-zajavljenie-glav-dnr-i-lnr-o-vneshtorgservis-pod-upravlenie-novogo-investora.html. Cited December 6, 2021.
3 Poloyyan A. The lion’s share of the mines in the DPR will remain in service. http://ways-novorossia.ru/index.php?id=18025&show=news&newsid=901. Cited January 15, 2021.
the strengthening of the coal sector based on the development of processing enterprises, high-tech mechanical engineering and the service sector (geological exploration, engineering, equipment maintenance, R&D, etc.) can become a powerful stimulus for the development of the DPR economy.

The development of the machine-building industry (Fig. 5) has great potential for the development of the DPR economy, and it must be stimulated by the state.

Promising areas should also be recognized: the development of mechanical engineering for maintenance, production of equipment and modernization of the energy complex of the DPR; municipal transport engineering, railway transport engineering; creation of a new type of mining machine building. The development of these areas requires a high quality of institutions, business environment, and public administration in the DPR. Since the evolution of institutions and governance does not occur quickly, it can be argued that in the coming years, the innovative machine-building sector will not be able to become the main source of economic growth in the DPR.

From a strategic perspective, the sectors of the DPR economy that have the opportunity to search for new efficient technologies include energy, heavy engineering, metallurgical and chemical industries, the agro-industrial complex, and the military-industrial complex. At the same time, economic growth in the DPR (as a territory with limited economic opportunities, where there are objectively barriers to business development) is impossible without high entrepreneurial activity. It should also be noted that there are currently no financial resources to provide subsidies to support enterprises in the DPR.

In general, the quality of economic growth in the DPR, taking into account the constructed development trends, can be determined by the limiting development options:

— A positive development trend: the structural and technological modernization of the DPR economy will take place in stages, the formation of a more complex and diversified structure of the economy, including the coal mining industry, deep processing, sectors of high-tech metallurgy and mechanical engineering industries; the formation of high-tech platforms based on the interaction of science, technology, production; creation of production facilities of high technological orders; elimination of infrastructure and institutional problems.  

— A negative development trend: maintaining the existing low growth rates or alternating periods of insignificant economic growth and periods of its decline; preservation of the parameters of the sectoral structure of the DPR economy; wear and tear without the necessary renovation of production, transport and social infrastructure. Theoretically, if structural problems are resolved in the medium term, the DPR economy will be able to show an annual growth of 2.5%. To mobilize the existing development potential of the Republic, it is necessary to intensify activities at the state level to draw up indicative plans with a clear definition of priorities,

4 The authorities of the DPR established the Almaz State Corporation to ensure the implementation of policy in the military-industrial sphere. The corresponding Decree no. 203 of the Head of the DPR was published on the official website of the country's leader on July 19, 2021, Donetsk News Agency. https://glavadnr.ru/doc/ukazy/ukaz_N203_19072021.pdf. Cited July 30, 2021.

5 Ministry of Economic Development of the DPR on the economic development and the investment climate in the Republic on February 8, 2021. DNR LIVE. http://dnr-live.ru/mer-oorazvitii-ekonomiki-i-investitissiennom-klimate-v-respublike/. Cited August 3, 2021.
goals, means and possible vectors of economic development of the DPR [17]. One of the conditions for the effectiveness of economic policy aimed at ensuring economic growth is a clear choice of priorities, the main of which should be reaching the highest rates of balanced economic growth [18]. The preservation of the current state of the DPR economy and weak economic growth create conditions for its stagnation, form potential risks that will not allow maintaining the social stability of the region in the medium term.

The economic policy in the DPR should be based on the realities of the resource economy, when, due to the targeted decisions of the authorities, decisions will be made regarding the adoption of the necessary measures and the sequence of steps in the field of economic development. In 2021, the Republican program was approved to stimulate the domestic production of the DPR for 2021–2022, within the framework of which it is planned⁶ to provide state support to manufacturers by resuming the activities of industrial enterprises, if necessary, their reprofiling, improving customs and tariff regulation, reducing the dependence of enterprises on imported components.

The regulatory capacity of the state is significant. It is proposed in the existing programs for the development of cities in the DPR to systematize the implemented measures, to give them a coordinated and comprehensive character, because practice shows that not all the tasks outlined in the submitted and approved program documents can be provided with the required investments, appropriate management mechanisms and implementation of the development policy. As an application of the state’s efforts at the initial stage, there can be export, customs and especially tax incentives and preferences for budget-forming industries in the DPR.

The potential for economic growth in the DPR is determined by both positive factors (availability of raw materials, relatively high quality of human capital, availability of production potential) and negative (weak institutions, lack of investment to modernize production, limited opportunities for structural maneuver in order to renew and develop the economy). In the DPR, an economic policy is being implemented without designated goals for the formation of the structure of the economy, i.e., passive structural policy [19].

A policy aimed at creating conditions for sustainable economic growth in the DPR should be aimed at reducing the influence of negative factors and maximizing the effect of the territory’s advantages. For this, a higher-order managerial resource must be involved, which must function within the framework of such exceptional target priorities as ensuring economic and social development and the welfare of the citizens of the Republic. It is necessary to set and solve practical tasks to include the production of the Republic in the production chains of Russia, to remove customs barriers, facilitate the transit procedure, carry out activities to counteract bureaucracy and corruption based on digitalization, expand the scope of electronic payments and constantly revise the regulatory framework to reduce the number of duplicate regulatory documents, etc. [20].

It should be noted that any analysis of probable economic processes in the DPR can only be approximate due to the uncertainty of the future borders and political status of the Republic and, accordingly, the amount of available natural and industrial resources. Therefore, it is important to have scientifically substantiated forecasts of such development in order to assess and formulate the development strategy of the Republic. The long-term strategy for the development of the DPR’s economy cannot be limited to short-term forecasts. It should focus on the economy of the future, take into account the trends that determine the optimistic forecast of development. Without a practical orientation to the trend of accelerated development, presented in the article as conditional, the DPR economy will only demonstrate an imitation of development. The Republic needs to move from a policy of moderate economic recovery to defining a long-term development strategy and its phased implementation.

Based on the development trends of the Donbass economy in the period 2014–2021, it can be assumed that, as a baseline scenario for the development of the DPR economy in the medium term, there is a likelihood of an inertial scenario of uneven growth. This scenario assumes, while maintaining the invariance of

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⁶ The DPR government adopted the documents developed by the Ministry of Economic Development. 21.07.2021. Access mode: https://mer.govdnr.ru/index.php?option=com_content&view=article&id=9289:pravitelstvo-prinyalo-razrabotannye-mine-konomrazvitiya-dokumenty&catid=8&Itemid=141 (accessed 07.22.2021).
the influence of a powerful geopolitical factor on the development of the DPR economy, the continuation of the current economic policy, which will produce a decline in economic growth rates due to a slowdown in demand growth and limited opportunities to increase its productivity.

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