SÉRIE “Ekonomika”

https://doi.org/10.52058/2695-1592-2024-2(33)-10-25

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LESSONS OF ECONOMIC MODERNIZATION IN THE SOUTHEAST OF UKRAINE (END OF THE 19th CENTURY – BEGINNING OF THE 20th CENTURY)

Abstract. In the second half of the 19th century, processes of economic modernization associated with the development of industrial capitalism began in many countries. Some countries were guided by the British model of modernization, in which the state intervened little in the economy and did not restrict free enterprise. Some countries (Germany, Japan) followed their own path, when the state became the initiator of modernization. The most typical example of modernization was the new industrial region in southeastern Ukraine. Large coal mining and metallurgical enterprises were created through foreign investments, mainly French and Belgian. Although this created dependence on foreign capital, there was no other way for rapid industrialization at that time – there was not enough domestic capital. The products of the new enterprises were used mainly to create an extensive railway network, and foreign investors made good profits from this. The main securities market for these enterprises was on the Brussels Stock Exchange (and partly on the Paris Stock Exchange). The processes of economic modernization were interrupted with the outbreak of the First World War in 1914 and the revolution in 1917. However, already at the beginning of the twentieth century it became clear that modernization was not entirely successful. Contemporaries liked to compare the new industrial region in the southeast of Ukraine with America of those years. However, the only similarity was in the pace of industrialization, and that was where it ended. Both the methods of economic management and the societies themselves were completely different. Full-fledged inclusive institutions were never created, and without them economic modernization could not be effective.
Keywords: economic modernization, southeast of Ukraine at the turn of the 19th – 20th centuries, foreign investment, inclusive institutions

Main problem. Economists are familiar with the phenomenon of path dependence. Institutional inertia, the strength of tradition, really resembles a deep rut on a dirt road, from which it can be so difficult to get out. Our past creates a viscous and at the same time familiar environment that we often don’t want to leave. The «rut effect» is like a chronic disease that is not immediately noticeable to others. This disease manifests itself in the fact that the system tends to change even those people who would like to change the system. Such a disease occurs due to a combination of several reasons and is often passed on from generation to generation, and it can be difficult to find the moment when exactly it began. So, path dependence arises from a confluence of historical circumstances. A good example is two neighboring countries, the USA and Mexico, where you can see completely different worlds and living conditions.

By the end of the 19th century, many countries, trying to get out of the well-trodden rut of tradition, adopted the British model of capitalist development, where the free market came first, and a very strong state existed for the sake of the economy, and not vice versa. However, there was another way, where the interests of the state initially prevailed over the economy. Germany followed it during the time of Bismarck and Japan during the Meiji era. Here, the development of capitalism took place at the initiative of the state, combining state regulation of the economy and the free market. The results turned out to be quite good – these countries also won the race against time. However, it was not they who became the world leader who replaced England, but the United States.

Capitalism developed mainly at the initiative of the state (albeit with less results) at the end of the 19th century in Ukraine, divided between two empires. In Western Ukraine, part of Austria-Hungary, economic modernization began in the second half of the 19th century under the long-ruling Emperor Franz Joseph. And although Austria-Hungary was difficult to compare with England, France, or Prussia in terms of economic growth rates, the policy of moderate reforms yielded results. Central and Eastern Ukraine also required economic modernization. Here the main proponent of rapid industrialization was the Minister of Finance Sergei Witte. Thanks to his policies, accelerated modernization began here, affecting not only the economy, but also many aspects of life. Factories and railways were built, coal was mined, and steel was smelted.

The object of the study is the features of economic modernization and the factors that ensure full modernization. The subject of the study is the industrialization of the late 19th – early 20th centuries in eastern Ukraine.

Literature analysis. Numerous works by authors of that time (including publications in the economic and financial press) are devoted to the processes of
industrialization in the east of Ukraine, from which all statistical data are mainly taken, as well as the works of researchers published in Ukraine (Baranovs'ka I. V., Brover I. M., Golobuc'kyj V. O., Gurzhij O., Derev’jankin T. I., Dovzhuk I. V., Donik O. M., Nebrat V. V., Shherbinina O. V.) [1—9] and in other countries. The main research method is a systematic analysis of the processes of economic modernization based on statistical data on industrialization in eastern Ukraine and the role of foreign investment, as well as the works of various authors on this topic.

**Target of research.** The purpose of the study is to conduct a systematic analysis of the processes of economic modernization in the east of Ukraine (late 19th – early 20th centuries) and identify factors that ensure full-fledged modernization, as well as factors inhibiting it.

**Research results.** The processes of economic modernization manifested themselves most clearly in the southeast of Ukraine, whereby the end of the 19th century a new industrial region emerged, mainly due to foreign investment. Belgian and French capital played the main role in the industrial revolution here. Therefore, this region ironically began to be called «White Congo», hinting that it was turning into a Belgian colony, like the African Congo. And some people jokingly called the Luhansk region «the Liege of the Donetsk basin» [10, с. 14].

In fact, industrialization had nothing to do with colonization – it was an imitation of developed countries. And an attempt to move at the same feverish pace of technological progress with the rest of the world. According to Nikolai Mikhnovsky, a lawyer and publicist of the early twentieth century, who visited Lugansk in 1899, «capital rules here, industry is developed, and new forms of life are being created» [11, с. 95].

Of course, Donbass and Krivoy Rog did not become colonies of Belgium or France, but there was also some truth in this irony. At the end of the 19th and beginning of the 20th centuries, indeed, almost everything here belonged to foreigners, mainly Belgians and French – factories and mines, railways and real estate.

At first, in the 1870s, the creation of the metallurgical industry proceeded rather slowly, both due to the novelty of the business and due to the reduction in railway construction, so the demand for coal and steel could not be so great. After all, the main consumer of coal and metal was the railways. The real boom – a whole industrial revolution in our steppes – began in the 1890s. It was a consequence of the greatly expanded railway construction which created a massive demand for the products of the metallurgical industry.

There was another reason for the boom – the accumulation of free capital in the developed countries of Western Europe, due to which the flows of foreign investment (mainly French and Belgian) in the southeast of Ukraine became truly massive. The total amount of direct investment of French capital in the industry of the tsarist empire from 1888 to 1914 increased from 219.8 million francs to 2245 million francs [12, p. 85].
It was thanks to them that the industrial revolution took place there. You can argue as much as you like that dependence on foreign capital is bad. But if the country is not rich in its own capital, and industry needs it, then there is no other way out of this situation than attracting capital from abroad. The only truly real (and not fantastic) way to finance the rapid creation of a network of industrial enterprises could only be foreign investment in those years. Therefore, the very posing of the question «why they didn’t want to grow it naturally» makes no sense.

And investors were interested in the most profitable business – mining and metallurgical enterprises in the southeast of Ukraine. And buyers of their shares were attracted by the fact that in companies with foreign capital, dividends in most cases were no less than 5–10%, and sometimes even 15% and 20%. Foreign investment in the mining and metals industries in the southeast has increased rapidly. From 1890 to 1900, its increase in the mining industry was 525%, in the metallurgical industry – 938% [13, с. 83]. By the beginning of the twentieth century, almost 90% of the capital there belonged to investors from Western Europe. Belgian and French capital predominated, followed by German capital. Investments from other countries (including England) were significantly less significant.

The motives of investors here were the same as in other countries – the discovery of new rich deposits of raw materials (coal and iron ore), together with cheap labor, made it possible to obtain a much greater return on the capital invested than if it had been invested in their own country. At first glance, it may seem that this was outsourcing – the transfer of metallurgical production from France and Belgium to Krivoy Rog, Yekaterinoslav or Donbass. Actually, this is not true. Outsourcing at that time can be seen in England, which transferred textile production to India and imported the finished products of these factories from there. But the products of metallurgical plants in the southeast were not transported to Western Europe, and they did not reduce their own metal production either in Belgium or in France. The cost of local metallurgical products turned out to be higher than in Belgium. So, the main consumer of metal became the railways of the tsarist empire, and foreign investors took out only profits.

Although the construction and development of new enterprises was largely financed through the securities market (their shares were in good demand on the Paris and especially Brussels stock exchanges), most of these factories would not have appeared without the support of the State Bank and personal contacts with influential people from the Ministry of Finance. And the main promoter of industrial capitalism was, of course, Sergei Witte, the influential Minister of Finance. After all, new metallurgical plants worked primarily with government orders related to planned railway construction.

The doors were hospitably opened to French and Belgian investors for a reason – there was a lot of politics involved. This has probably always been the case everywhere – rarely did massive foreign investment, especially in countries with
catching-up development, begin only on the initiative of the «invisible hand of the market». Support from the government has always been required to create incentives for investors.

French «came to the rescue» not out of kindness. They were attracted by markets favorable to the export of capital. And especially the opportunity to build coal mining and metallurgical enterprises in the southeast of Ukraine, located near the richest deposits of coal and iron ore. Moreover, there was a steady demand for the products of these factories in the domestic market – a large construction of the railway network was underway.

In the 1880s, the share of French investment reached 32%, ahead of English (31%). In 1901, almost 47% of investments were Belgian, 25% were French, 20.5% were English, 6.6% were German. In 1917, 27.9% of capital was French, 27.4% was English, 21.6% was Belgian, 10.8% was American, and 7.2% was German [14, с. 14].

When the Ekaterininskaya Railway began operating in 1884, connecting Donbass with Ekaterinoslav, the city began to develop rapidly. It turned out to be the center of the Krivoy Rog iron ore region, where ore production almost doubled from 1890 to 1908, from 129 million poods to 225.5 million poods [15, с. 77–128; 16,c. 49–83]. At the end of the 19th century, the speed of development of the Ekaterinoslav district, where several large factories are located, is barely imaginable.

Soon, many other industrial enterprises appeared (at the beginning of the twentieth century, their number in the city reached 70), forming the core of another new industrial region that arose around the richest reserves of iron ore. In 1895, a telephone network appeared in the city (initially with 60 subscribers); in 1897, the Franco-Belgian tramway society began building city tram lines.

In terms of the volume of capital invested in this region, French investors took first place. In July 1912, the shares of six mining and metallurgical companies in the southeast of Ukraine were quoted on the Paris Exchange. However, the main market for industrial securities was not the Paris Exchange, but the Brussels Exchange.

The influx of Belgian capital became especially noticeable during the «iron fever» of the late 19th century. Belgium created several enterprises in Europe, Asia and Africa that were reminiscent of the prosperous Belgian colonies». It was then that Ekaterinoslav with its factories and the entire Krivoy Rog iron ore region began to sometimes be called the «white Congo», hinting that it already resembled a Belgian colony.

Belgian investors began to appear as early as the 1870s, initially specializing in tram companies, which they had already founded in many countries. In Belgium, this business was controlled by the Otlet Group (Union de Tramways) and the Urbana Group (Societe generale Chemins de fer economique). Founded in 1880 by the Urbana Group, the Odessa Trams company was the first, then similar companies were created in Kyiv, Warsaw, Kharkov and other cities. Trams in Odessa, Warsaw and Kharkov in 1897 gave an average return of 15% on fixed capital.
Then, from creating «horse-drawn railways» (as they were then called) in several cities, the Belgians moved on to larger mining and metallurgical enterprises. Belgian companies built factories similar to their own and thus benefited from a huge market in a country just beginning to create its own industry. The «characteristic impudence of the Belgians» helped them achieve their goals, and in the industries in which they invested their capital, they felt like complete masters.

Belgian investment volumes increased rapidly. Investments in metallurgical and other companies turned out to be very profitable, and advertising in Western European newspapers ensured high quotations of securities of mining and metallurgical enterprises on the Brussels Stock Exchange. Shares of new enterprises brought huge dividends, which foreign capitalists had long been unaccustomed to, and it was enough to add the word «Dnieper» or «Donetsk» to the name of the company to count on the easy sale of shares on European stock exchanges – primarily on Brussels and Paris.

The Belgians invested their capital not only in Yekaterinoslav and Krivoy Rog, but also in the Donbass. The influential Belgian company Societe Generale founded the Metallurgical Society in 1895. The company acquired 4,600 hectares of land with coal deposits, and Oscar Bie (formerly the general director of Saint-Leonard Societe) moved to the Donbass to manage the construction of the plant, which began producing products in 1898. The co-founder of the society and the author of its charter was Fyodor Enakiev (1852–1915), another engineer who became an industrialist.

In the 1890s, among foreign investments in the new industrial region (in 1900 reaching 888 million Belgian francs), it was Belgian capital that prevailed (550 million), significantly surpassing French capital (275 million). British (34 million) and German (29 million) investments were fundamentally smaller [17, p. 111]. Although the bulk of the invested capital was Franco-Belgian, the distinction between French and Belgian capital turned out to be very conditional. Due to the economic connection between France and Belgium, a significant part of the capital that was formally considered Belgian was of French origin.

During the decade of the 1890s, foreign capital invested in the coal industry alone increased almost sixfold, with the Belgians leading the way. So, it was no coincidence that Donbass, Krivoy Rog, and Yekaterinoslav were called the tenth province of Belgium, and there was a lot of talk in the press about the invasion of foreign capital, especially Belgian. The maximum presence of Belgian capital was in 1900 (60 companies, of which 20 metallurgical, 13 mining, 10 tram, etc.; after the crisis of 1900–1902 it decreased to 31 in 1910). Belgian capital, in addition to the mining and metallurgical industries, was then invested in a significant number of various enterprises. In most industrial enterprises founded by Belgians, the shares had a small denomination, usually no higher than 100–250 francs (37–92 rubles), sometimes 50 or even 25 francs. This means that they were intended for small individual investors. True, for the Belgians.
The industrial boom in the new industrial region from Krivoy Rog and Yekaterinoslav to Donbass and Kharkov was based on large government orders for rails and other railway equipment. Since the export of metallurgical plant products to Belgium and other Western European countries was not expected, only the profits of metallurgical plants were exported. And their products were used mainly in the construction of railways.

The interest of foreign investors arose after railways appeared in the Donetsk steppes, and telegraphs, telephones and banks appeared in the cities. One of the first to start its activities in 1883 was the Society of Rock Salts and Natural. It was not engaged in coal, but in salt mining in the vicinity of Bakhmut. This society has been involved in coal since 1895 [18, р. 120–159].

In addition, on June 11, 1891 adopted a new protectionist customs tariff to increase the cost of imports and stimulate the development of its own industry, including coal mining and metallurgy. This goal, in general, was achieved, albeit at a high price – foreign investors exported profits abroad, and manufactured products could only be sold on the domestic market, since their price turned out to be too high. In the 1890s, a real boom began among foreign investors – «intoxicated by the success of the first factories, blinded by the experience of operations throughout Europe», they, according to Arthur Rafałovich (official agent of the Ministry of Finance in Paris, author of many works on economics), looked at everything «with rose-colored glasses», not noticing the growing problems that ended in a crisis at the turn of the 19th and XX centuries [19, р. 717–718].

Before the crisis, industrial growth was faster than in Western Europe, and the abundance of free capital, together with easily accessible short-term loans, caused, as always, another shareholder boom. From 1894 to 1899, many new companies appeared with capital more than a billion rubles, not counting railway, banking and foreign companies.

The same thing as always – a market collapse. The first sign of an approaching crisis was a decrease in the profitability of capital in trade in the southeast of Ukraine from 6% in 1896 to 3.29% in 1898. In industry during these same years, the decrease in profitability was still insignificant – from 10.5% to 10.25% in 1898 [20, с. 86]. However, a global economic crisis soon began, which became especially severe in our area due to crop failures in 1897–1899.

If we recall the history of the creation of the railway network in the USA, Argentina, and other countries, then there is nothing unusual in the crisis at the turn of the two centuries. The approach of the crisis was primarily reflected in the stock exchanges, where in September 1899, stock prices began to fall, and then panic began.

In 1899, the market value of securities of industrial enterprises fell by 40%, after which their owners suffered large losses. We can say that it was the stock exchange that was playing bearishly, but the beginning of the crisis was noted then
in many countries. The difficulties of industrial enterprises, when their shares and
bonds fell significantly in price, caused concern among Belgian and French investors
who invested huge amounts of money in these enterprises.

Many people wrote about the causes of the crisis of 1899–1902. Most often
they mentioned things that are already well known today, first, the availability of
cheap loans, which pushed entrepreneurs to risky projects. The crisis was intensified
by speculators, swindlers and brokers who offered gullible foreigners to buy all sorts
of dubious enterprises.

Cheap, easily accessible credit, coupled with government orders for products
at inflated prices, is a characteristic feature of many speculative bubbles, especially
those created due to the influx of foreign investment. Entrepreneurs and joint-stock
companies counted on huge profits that turned their heads, and the game for
increasing shares, thanks to which everyone got rich, fueled the thirst for enrichment
even more. But since joint-stock companies often did not sell their shares, but
pledged them to commercial banks, equity financing was replaced by short-term
loans.

It has long been known that the more mobile foreign financial capital is, the
easier it can not only enter the country, but also withdraw from it at the slightest sign
of approaching problems. It is not surprising that the financial crisis is rapidly
spreading across borders thanks to the growing connections between national markets.

In Western Europe, financial markets began to experience severe constraint
back in 1899, under the influence of the outflow of capital to the Far East and other
places in Asia which manifested itself in a fall in the prices of most interest-bearing
securities. And the rapid growth of joint stock companies, covering various
industries, and intensive railway construction led at the end of 1898 to an overflow
of the market with securities.

In our area, many entrepreneurs took on large businesses with too little capital,
pinning all their hopes on the fact that they would be able to take advantage of a
cheap short-term loan. However, due to increasing tensions in the financial markets
in 1899, obtaining foreign investment became problematic and many projects proved
unfeasible. From September 1899 to March 1900, 18 Belgian enterprises stopped
payments, and the decline in demand for products created great problems for
metallurgical plants, which were forced to reduce production. The competition
between entrepreneurs began to intensify, mainly for obtaining government orders
for coal and metal – the only salvation in a crisis.

In 1899, the metallurgical plant of the Belgian «Upper Dnieper Society»
suspended its work, in 1900 – the Kramatorsk plant, in 1902 – the Kerch plant. A
year earlier, in 1901, one of the largest Donetsk-Yuryevsky Plant (DUMO), founded
by A.K. Alchevsky, stopped. The Donetsk-Yuryevsky Metallurgical Plant was one
of the best and grandest in all of Europe, but it turned out to be too large and
disproportionate to the real demand for its products.
The government's plans to develop the railway network had to be postponed for a while, and government orders for rails were cancelled. When shareholders found out about this, panic began among them, after which the prices of industrial securities fell even further. Their total value for 98 French and Belgian companies decreased from 1316 million francs to 536 million – by 59%. First of all, the price of shares fell, the prices of which far exceeded the real profitability of the enterprises. Stock prices dropped significantly, including bank stock prices – almost twofold. «In this state of affairs, complacency... began to give way to stormy meetings», at which «the public, which had been pinched quite a bit in recent years by bank and stock exchange manipulation», openly expressed its indignation. Thanks to the dissatisfaction of shareholders, «the behind the scenes side of the activities exhibited by our joint-stock banks during the period of financial and industrial revival began to be revealed to the eyes of society» [21, с. 137].

Nobody wanted to invest capital in enterprises in Donbass or Krivoy Rog – industrial growth stopped for a while. The French and Belgian press blamed government for everything – the idea of a natural alternation of cyclical ups and downs was, as always, too inconvenient for the majority to understand. Every time the rise began, the majority of the public naively believed that it would last indefinitely. Meanwhile, factories in southeastern Ukraine continued to operate during the crisis, accumulating production. However, from 1900 to 1903, the demand for coal, iron ore and steel decreased by 50%, which made the further operation of many enterprises economically unprofitable and even unprofitable. And the collapse of the banks of A.K. Alchevsky and several Belgian banks that financed the industry of the region (including Banque de Liege) further aggravated the situation. In mid-1901, the rates of even the most popular dividend securities before the crisis fell so much that the shares of the Aleksandrovsky Steel Plant and the Donetsk-Yuryevsky Metallurgical Plant were given 20% of the par value (50 rubles per share with a par value of 250 rubles). At the beginning of 1899, the shares of the Hartmann Locomotive Plant were paid 154 rubles instead of 245 rub. By 1902, the shares of the Dnieper Society fell in price by 65%, and its subsidiaries – the Almaznaya mine and the Nikolaev Shipyard – by 90%. Even worse was the situation of the Providence company, which invested too much capital in eastern Ukraine before the crisis [22, с. 33, 48–49].

The State Bank provided financial assistance to large metallurgical enterprises to save them from collapse (from 1900 to 1902, loans to these enterprises doubled, to 280 million rubles). However, despite the loans issued to clearly problematic factories, it was not possible to save them from bankruptcy. And the support of the State Bank and the Ministry of Finance for enterprises with no prospects only slowed down the natural development of the crisis – it did not make anyone better. Inept government intervention has led to even greater problems than if the government had done nothing at all.
As a result, during the crisis, about a third of the industrial enterprises of the new industrial region had to be liquidated. They were either swallowed up by larger market participants, or they went bankrupt and became the property of competitors. Belgian factories were especially affected by the crisis. While the government created the Prodamet and Produgol syndicates in 1902 to set supply quotas and thus maintain production during the crisis, there was practically no coordination among Belgian enterprises (and other foreign companies). On the contrary, the competition has only intensified. One of the attempts to cooperate and coordinate the actions of Belgian investors was the proposal of engineer Jules Gernaert to create an industrial federation in 1902 to coordinate the actions of Belgian enterprises in Donbass. There was interest in the idea – many industrialists came to the first meeting of the federation. However, they were unable to agree on joint actions – the Belgian syndicate of Donbass enterprises was never created. In the same year, Edouard Despres, head of the Societe generale, again proposed creating a similar syndicate of large Belgian and French metallurgical enterprises, but they could not do this either, although there was nothing unrealistic in this proposal – in those years such creation of syndicates became common practice. The competition between the four main Belgian metallurgical enterprises of Donbass was too strong, reflecting the struggle for marketplace among the parent companies in Belgium, and it undermined all common sense.

The decline in the newly industrialized region between 1899 and 1902 was short-lived and, for most, not very dramatic. True, several enterprises had to be closed. But the Belgians, until recently leaders in the metallurgical industry in the south-east of Ukraine, confidently considered this region the «tenth province of Belgium» and the «white Congo», were unable to maintain their influence after the crisis. Some of their enterprises passed into the hands of French investors, and until 1917 they dominated the new industrial region.

And although in 1910 there were 31 Belgian enterprises operating in the south-east of Ukraine, the Belgians no longer focused on metallurgy, but on their usual business, in which they were considered recognized leaders – tram companies in Kyiv, Kharkov, Odessa and other cities. And in society, the attitude towards the Belgians changed – the press increasingly accused them of trying to monopolize first the metallurgical industry, then – urban transport. Belgian tram companies were often called purely speculative, although they built tram lines (many examples of this are known, at least in Kyiv).

This rise was most noticeable in the industrial southeast, which experienced its heyday in the 1910s. And the pace of joint-stock founding has reached its maximum. At large enterprises in the Donbass and Krivoy Rog region, the financial results of the activities of these companies in 1911–1912. turned out to be downright brilliant. In 1913, the products of the new industrial region in eastern Ukraine accounted for more than 20% of the total imperial production volume, including 78% of coal
production, 67% of iron production, 57% of steel, 18% of mechanical engineering products [23, c. 230].

After the start of the new rise of 1907–1913, the Belgians tried to regain their former influence, but they were never able to regain leadership. However, the Brussels Exchange remained the main market for securities of enterprises in the new industrial region in 1913. At the Paris Bourse in 1912–1913, 6 types of securities of mining and metallurgical enterprises were quoted, and on the Brussels – 19 types [24, c. 22; 25, c. 6].

All this irrevocably ended in 1914 – Belgium was occupied by Germany, after which Belgian companies in Donbass were under the threat of confiscation and nationalization. And after two revolutions in 1917, the Belgians lost everything – according to rumors, the total amount of their losses was 2.5 billion francs in gold.

However, during the boom years, foreign investors brought not only capital to the new industrial region in southeastern Ukraine, but also advanced technologies – especially in the metallurgical industry. At that time, these innovations (without which mass industrialization would not have been possible) had a strong influence on the development of capitalism. At the end of the 19th century, there was probably no part of the world where advanced technology had not penetrated, although the results varied.

Developing economic systems usually lack their own capital, so any investment for the host country is perceived as a positive phenomenon. However, when everything is owned by foreigners, and everything is created only by them, domestic entrepreneurs find themselves in difficult conditions, and it is not easy for their enterprises to survive. In countries that achieved success and initially depended on foreign direct investment, their share was very clearly controlled by the state. And they avoided the situation where everything belongs to foreigners, and everything was created only by them (remember the history of the formation of the economy in the USA or Japan). The authorities tried to prevent foreign investors from gaining complete control over the enterprises being created.

In this case, foreign direct investment turns out to be very productive indeed. They have a demonstration effect, showing the benefits of new production technologies and new management methods, and bring not only information about world markets, but also important connections to them. It is clear that the effect of spatial distribution does not always occur – the greater the share of ownership of foreign investors, the more they are tempted to use local raw materials and labor, exporting profits and especially not caring about the future of the country and its economic growth. Then the host country really begins to resemble a colony – «White Congo».

The situation with investments was not much different in the western part of Ukraine, which was part of a completely different state – Austria-Hungary. Oil production, and industrialization in general, took place there too, mainly at the
expense of foreign capital. This is the fate of many peripheral economies in different countries and on different continents.

How could this be avoided to protect local businesses and stimulate the growth of our own industry? One of the ways is to set optimal customs tariffs and duties in a timely manner, which was done, and do not forget to remove them on time. After all, protectionism in itself does not guarantee economic success, and excessive state protection leads to the fact that domestic producers find themselves in hothouse conditions. And then it is not possible to create a competitive industry, enter world markets and take advantage of free trade.

The economy was included in global markets through foreign investment and new technologies, but included unilaterally. There was only an incoming flow, but we also needed an outgoing and export flow. And not raw materials or grain, but products that create economic complexity. And this just did not happen.

The economy remained focused on the export of raw materials – the state budget was based on income from grain exports. The budget covered inflated costs to produce rails and other products of the metallurgical industry, and everything was based on government orders. And although favorable conditions developed at the end of the 19th and beginning of the 20th centuries (demand for grain, global economic growth, and financial globalization), it was not possible to go beyond the commodity economy. To produce competitive products, a completely different level of economic complexity was needed. But this complexity did not exist, and there was nowhere for it to appear in those conditions – after all, this is a long process that requires a combination of many factors.

And yet, with the help of foreign direct investment and the policies of Sergei Witte, he managed to create a huge industry. It seemed to many then that these changes were so radical that this growth would be long-term, and the era of general prosperity would soon begin. However, this attempt at modernization (like all previous ones in this problematic empire) inevitably reached a dead end and ended in social cataclysms – bloody revolutions.

There was something unbearable for society in such a development. And for the mentality of contemporaries. It seemed that money and technology had become easily accessible, and that building a large plant with foreign capital was not at all difficult. Because of this apparent ease and simplicity, contemporaries missed the opportunity to adopt not only money and technology, but also something more valuable – social institutions.

In the advanced countries of that time, the path to creating these institutions was long and difficult. It is clear that it was unrealistic to repeat this path – and it was not necessary. And care had to be taken to not simply imitate (at best) Western European institutions, but to adopt them in such a way that they would become viable. This is more important than money. We need to care about the chance for a better future, and not just about attracting capital.
The main problem of the economy of the tsarist empire was authoritarian capitalism. But the issue is not about authoritarian capitalism itself. In those years, such authoritarianism could be seen in both the German and Japanese economies, and there it did not create such problems. So, it was not authoritarianism that was the problem, but the general archaic inertia of the state in which Witte tried to carry out his reforms.

Officials, out of a centuries-old habit, stuck their noses into the economy, where it was not needed, to receive more bribes when distributing budget orders. And where needed it was necessary to support domestic entrepreneurs and stimulate domestic innovative production; too much systematic, painstaking work was required, but officials did not want to get involved with this. It was much easier to feed on the generous cash flow of foreign investment that arose and not think about the future of local business. Moreover, a lot was determined by government orders at inflated prices for railway construction, which did not create opportunities for the export of competitive products and effective market relations.

And they did not realize the consequences of the unregulated powerful flow of foreign capital. There was only one task – to build as many industrial enterprises as possible, which the tsarist empire itself could not have done. However, there was a more ambitious task – to grow our own large business, a leader in advanced industries. But on the whole, it was not possible to do this.

Full modernization is impossible without transforming political institutions – the economic system is inseparable from the political one. However, repeating the development trajectory of successful countries, in principle, were not satisfied with the tsarist authorities. They wanted to create an industry without changing anything in the political system. Not to mention the ideology of «Orthodox autocracy» that is so important to them.

The state that began to industrialize needed to create a system capable of creating modern and viable institutions that could eventually become accessible to everyone, not just a select few. As long as there is a small group of selected industrialists who sell products to the state at inflated prices and export the profits abroad, the formation of institutions that reflect the interests of large groups is unlikely. And without such institutions, it was difficult to combine adaptability and stability, which is much more difficult than accelerating economic growth in the short term.

The system of institutions develops simultaneously with the formation of the structure of the economy; there is no primary or secondary, although sometimes the formation of institutions may lag behind. In those countries where the authorities sought to increase the industrial potential of the state, the quality of institutions inevitably increased over time, even if their creation was not part of the government's plans. It is possible to launch economic growth without inclusive institutions (besides, what are inclusive institutions for China are not considered such anywhere
in Germany). The main thing is that existing institutions prove to be viable and not created for appearances. Otherwise, it will turn out that institutions are on their own, and real life is on its own. Because formal borrowing of institutions very often turns out to be useless.

Industrialization, like other economic and social changes of the early twentieth century, awakened in people enthusiasm, innovative energy and a desire for experimentation, a desire for something new. This mood affected not only the intelligentsia (especially the new layer of well-educated engineers), but even some of the workers – after all, they also wanted a better life. If the authorities had supported the increased accessibility of political and civil institutions, history might have turned out differently. But in the tsarist empire, the authorities could not support this in principle. In addition, people wanted to see direct economic benefits for themselves from all these economic changes. If benefits never materialize or take too long to arrive, faith in institutions is lost.

Theoretically, there were ways to solve problems, but in practice it turned out that the idea of «creative destruction» did not work here, and during the years of the revolution and civil war, «creative destruction» became not very creative. True, the Bolsheviks later created a whole world of planned industrial socialism here, but that was later. The communists promised in 1917 to create new, «people's» inclusive institutions. And the people supported them. As a result, the organizations they created led to the fact that the promised inclusive institutions in a totalitarian society were reduced to insignificant meetings «for appearances». And the very idea of civil society turned out to be devalued for a long time – if not forever.

Conclusions. Foreign capital, together with technology, caused transformations on a state scale, but they were more quantitative than qualitative. The specific bureaucratic structure of society, excessive corruption, business culture, work culture, weak institutions and much more hidden in the depths of the collective unconscious – this was difficult to change. Technology and capital by themselves were not enough to launch the mechanism of long-term economic growth.

Institutions that promote long-term economic growth could not develop normally in a frozen political system. Often, they were created formally, for appearances, were alien to society and were not filled with new content. And societies with weak institutions tended to end up in a vicious cycle of poverty and violence. The low quality of institutions creates the risk of falling into a trap and being stuck forever in the developing economy stage.

History shows that many so-called «developing» economies remain «developing» for decades. Time goes by and it doesn't look like they are getting anywhere near developed. And the disappearance of the gap between rich and poor countries is not happening, despite all the optimistic forecasts of economists. At first, it seems that developing countries, borrowing capital, technology, and other innovations from developed countries, are beginning to quickly catch up with them.
But soon there comes a time when everything that could be borrowed has already been borrowed, and your own innovations are needed. And developing economies usually cannot cope with this task.

Sustainable and long-term economic growth is available to only a few countries. And, strictly speaking, it would be naive to expect that industrialization and new technologies would completely transform the country, mired in centuries-old inertia, as a tsarist empire. However, if you do not set such obviously unrealistic goals, then the result of industrialization in the east of Ukraine looked very good at the beginning of the twentieth century.

We know examples when economic systems became successful not in the most liberal societies with an increased importance of the state in the economy and the general cohesion characteristic of these countries (first Japan, then South Korea, Taiwan, and especially China). However, their rapid rise also did not come without the emergence of economic freedoms and the expansion of personal freedoms, as well as the creation of an institutional culture.

Regardless of the characteristics of the country and the existing model of capitalism in it, the main secret of success is the ability to awaken creative entrepreneurship, inseparable from the personal freedom of people, which creates entrepreneurial excitement and drive in them. Another condition is an effective humane state. It is such a state that makes the very existence of a full-fledged market economy possible. Each of these factors can easily become toxic – poorly regulated entrepreneurship, free business devoid of social responsibility, and an interfering government. The secret lies in the correct proportions and mixing technology.

And this turned out to be possible only in some countries where effective interaction between people, society and the state was ensured. Then everyone could not only be part of the economic system, but also to pursue their own goals, which contributes to long-term economic growth.

A promising direction for further research by the author is the study of the processes of economic modernization in modern Ukraine, considering the experience of successes and failures of industrialization of the late 19th – early 20th centuries.

References:


