Strategy of Import Substitution in the Rostov Region: Results, Problems, Prospects

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Abstract: In 2014 appeared the most important for Russia, challenges that required the mobilization potential of its economy, particularly in 2014, according to the results of the all-Crimean referendum was the accession of the Republic of Crimea to Russia (Based on the Agreement between the Russian Federation and the Republic of Crimea about acceptance to the Russian Federation Republic of Crimea and education in the Russian Federation new constituent entities). In this regard, a number of countries and international organizations have imposed sanctions against Russia in the form of restrictive political and economic measures that impede collaboration and cooperation in key areas. The initiator of introduction of sanctions was the leadership of the United States and the European Union, which also joined a number of other developed countries. For a long time in Russia there were so-called “recovery model” of economic development based on involvement in the production of spare capacity and labour, and growing external demand for Russian commodities (Medvedev, 2016). Taken together, this resulted in the raw material orientation of Russian exports, high import dependence, technological backwardness and other problematic aspects of socio-economic development of the country. This situation causes a high degree of relevance of a study on the analysis of trends in the external environment for the economy of the Rostov region, to identify factors that can affect the development of the region and identification of possible threats and opportunities for the sustainable development of the Rostov region. The aim of this work is to identify the main external challenges for the Rostov region in the policy of import substitution, as well as threats and opportunities generated by these challenges in the context of the development of the region.

Keywords: policy of import substitution, sanctions, import substitution, import substitution strategy, competitiveness of the region

JEL Classification: F10, P33, P45, R19
INTRODUCTION

External challenges geo-economic and geopolitical nature seriously affect the specificity of economic activities of enterprises. At the same time, the escalation of geo-economic competition and geopolitical conflicts can significantly transform the economic activity of enterprises of the Rostov region, severely reduce the scope of foreign economic cooperation with many countries.

Moreover, for the region as a whole as the object of attraction of foreign investments, the subject of economic policy aimed at increasing the competitiveness of enterprises, knowledge-intensity and technological effectiveness of products external challenges are significant and outside of the immediate context of export activities on global markets.

Thus, the study of import substitution policy in the context of regional economic, social and spatial imperatives of development is characterized by considerable relevance in the context of global uncertainty and makes use of different methods of assessment of the situation and prospects for the region, its competitiveness and sustainable development.

MATERIALS AND METHODS

In conditions of high sanctions pressure experienced by the Russian Federation, the President of Russia Vladimir Putin one of the main economic interests of the state designated “smart” import substitution (Government of the Rostov region. Interdepartmental Working Group on Enhancing the International Competitiveness of the Rostov Region Economy. “Implementation of the policy of import substitution in the Rostov region”), which implies state policy aimed at the creation, the development of domestic enterprises of production, replacing imports, the economic security of the country due to the rapid development of priority sectors of economy through realising the potential of domestic demand.

According to Vladimir Putin “Reasonable import substitution is a long – term priority, regardless of external circumstances. The import substitution program should work on the creation in Russia of a large group of industrial companies that can be competitive not only domestically but also in international markets”.

What the policy of import substitution? It is a policy by which they try to reduce the external dependence of the economy at the expense of local food production and industrial goods. According to the author’s interpretation of “import Substitution – organizational and technical-economic phenomenon, consisting in the possibility of domestic production of a particular final or intermediate items (semi-finished products, raw materials) products and substitution in their imports in domestic consumption. It is this type of economic strategy and industrial policy, which aims to substitute imports of industrial goods that are in demand in the domestic market, goods of national production”.

The main reason for the policy of import substitution in Russia is to ensure economic security and sustainable development of the country on such key areas as high-tech manufacturing, food, Finance (Rogachev, 2015). For Russia, the problem of economic security of the country due to imbalances in the structure of the economy and, consequently, unsatisfactory structure of the foreign trade. Thus, the Russian export is mainly due to commodities (Askerov, Novichkov, Novichkov, Nosova & Rabadano, 2016). At the same time, the import consists mostly of the final product, and the volumes are growing at a faster pace compared to the production of finished products of domestic producers. As a result, domestic demand is
realized at the expense of imported products and not transformed in the growth of production in the country. State interference in the market relations will lead to the degradation of the scientific and production potential until the complete disappearance of entire sectors of the economy and, consequently, critical dependence on imports of the product concerned. Import substitution of domestic products should contribute to growth of competitiveness of domestic producers (Gusev, 2016). The competitiveness of products formed through market mechanisms, through the creation of globally competitive “economic environment” of business functioning with minimal use of protectionist measures, justified solely by the need to create equal conditions for Russian and foreign manufacturers in terms of government support.

Classical mechanisms for implementation of the strategy of import substitution in Russia are the protection of domestic producers through tariff and non-tariff regulation, and promote domestic production through direct or indirect subsidies.

The effectiveness of the policy of import substitution in Russia at the moment is determined by several factors:

First, it is the depreciation of the national currency, ensuring price competitiveness of domestic products compared to imported analogues.

Second, it sanctions restricting foreign trade, which directly reduces the offer of imported products in the domestic market and may be filled by either Russian producers in case of successful implementation of the policy of import substitution or import from countries not participating in sanctions.

In the short-term implementation opportunities of the Russian producers can only be implemented by downloading the available capacity and increase production without significant changes in its quality characteristics (Ivanova, Mackay, Platonova & Elagina, 2017; Tyaglov, Kushnarenko, Khokhlov & Qeropyan, 2017).

Figure 1: Objectives of import substitution

Ensuring national and state security of the Russian Federation
Achievement of technological independence in critical areas
Facilitating the formation of a positive trade balance
Cultivation of national leaders to conquer the global market
An important role at this stage is played by the stimulation of demand for relevant products from the state.

In the long-term effect of both factors will be offset, therefore, effective long-term policy of import substitution can only be realized by investing in the creation of globally competitive industries.

The main factors that prevent the implementation of the policy of import substitution in the long term, are significant technological gap between key industries and restrictions of a financial nature (Government of the Rostov region. Interdepartmental Working Group on Enhancing the International Competitiveness of the Rostov Region Economy. “Implementation of the policy of import substitution in the Rostov region”).

Foreign trade parameters characterize the result of a competitive struggle for the markets and the degree of implementation of export potential. These indicators reflect the level of involvement of regional economy in the foreign trade relations, the ability to produce and supply the world market with competitive products, the degree of self-sufficiency, foreign trade and industry export specialization (Goncharova & Gudenitsa, 2016).

When you implement a policy of efficient import substitution, it is important to take into account the high degree of integration of Russia into the world economy, due to the participation in the international division of labor.

To minimize the negative consequences of the import substitution policy should be implemented consistently.
The potential for increasing production in the framework of the implementation of the import substitution policy has two fundamental limitations - the volume of the market of imported products and resource constraints of the economy.

This determines the unreasonableness of the consideration of import substitution as the main source of economic growth in the long term and the inability to implement appropriate economic policies in all sectors of the economy, which requires the definition of priority industries, producing the most critical from the point of view of economic security products.

Research methodology the current state of import substitution in the Rostov region includes the key activities in accordance with the action Plan (road map) “support of the enterprises of the Rostov region, producing import-substituting products” (Plan of measures (“road map”) “Support of enterprises in the Rostov region that produce import-substituting products” (approved by the Governor of the Rostov Region on September 25, 2014)), which is presented in Figure 3.

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Figure 3: Direction of a study of the implementation of the strategy of import substitution in the Rostov region
The implementation of the import substitution policy today is a key factor in ensuring stable development of national economy in general and in particular the Rostov region. Its effectiveness is determined by successful implementation in each region of Russia and right choice of regional priorities. Improving the competitiveness of the region is one of the main strategic objectives of economic policy of the Government of the Rostov region. For its implementation, the region has developed an extensive system of business support and investment attraction in all areas of highly mineralized economy of the Rostov region (Goncharova & Gudenitsa, 2016).

For efficient import substitution in the Rostov region is the accelerated development of certain industries identified on the basis of national priorities (based on the criteria of criticality for the economic security of the country and the level of import dependence) as well as specialization and resource potential of the regional economy, namely (table 1):

1. Industry critical to the economic security (in terms of final product):
   1.1. Machine tools;
   1.2. Agricultural engineering;
   1.3. Helicopter construction;
   1.4. Power engineering;
   1.5. Metallurgy.

2. Industry, is not critical from a position of economic security that provides economic and scientific-technical development:
   2.1. Radio-electronic industry;
   2.2. Light industry;
   2.3. Chemical industry.

A promising area of development for the Rostov region is agrarian-industrial complex, where priority directions of import substitution are:

1. Animal breeding:
   1.1. Dairy cattle;
   1.2. Pig breeding;
   1.3. Poultry;
   1.4. Beef cattle.

2. The vegetable open and protected ground.

3. Processing and storage:
   3.1. Processing of milk;
   3.2. Processing of vegetables;
3.3. Processing of fruits and berries;
3.4. Deep processing of grain;
3.5. The construction and modernization of vegetable stores.

### Table 1

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<th>Priority sector</th>
<th>Ministry of Industry and Trade of the Russian Federation</th>
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<td>Subsector</td>
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<td><strong>Industries of specialization</strong></td>
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<tr>
<td>Manufacture of machinery and equipment</td>
<td>agricultural machinery industry*</td>
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<td></td>
<td>machine-tool construction*</td>
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<td>power engineering*</td>
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<td>oil and gas engineering*</td>
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<tr>
<td>Manufacture of vehicles and equipment</td>
<td>transport engineering*</td>
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<tr>
<td>Textile and clothing industry</td>
<td>helicopter industry*</td>
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<tr>
<td>High-tech</td>
<td>light industry (in general)</td>
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<tr>
<td>Manufacture of electrical equipment, electronic optical equipment</td>
<td>radioelectronic industry*</td>
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<tr>
<td>Chemical production</td>
<td>chemical industry (in general)*</td>
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* Subsectors that are critical for economic security (in terms of final products).

The foreign trade turnover of the Rostov region in the first half of 2016 amounted to 3 billion 448 million US dollars, including exports worth 2 billion 450 million US dollars, imports - 998 million US dollars. Foreign trade turnover increased by 15.2% or by $ 457 million compared to the same period last year (hereinafter - APPG).
In the first half of 2016, there was a surplus in the trade balance in the amount of 1 billion 452 million dollars (2015 - 1 billion 51 million US dollars).

The dynamics of the main indicators of foreign trade is presented in the diagram:

The most demanded import-substituting groups of goods in the context of the Rostov Region and the Russian Federation (Foreign economic activity of enterprises of the Rostov region in the first half of 2016).

In the first half of 2016, the import of the Rostov region amounted to 998 million US dollars, which is 2.8% or 28 million US dollars more than the same period of 2015. The physical volume of imports for the same period increased by 2.5%.

The cost of imports from non-CIS countries was $726 million (6 months of 2015 - $ 676.3 million), from the CIS countries - $272 million (6 months 2015 - $294 million).

The largest trading partners in the import of the Rostov region in the first half of 2016 are (in descending order of value): China (18.8%), Ukraine (17.5%), Germany (8.6%), Italy (5.8%), Belarus (5.1%), Turkey (4.7%).

Commodity structure of imports of the Rostov region:
- machine-building products - 37% (369.2 million US dollars);
- food products - 16.1% (161.1 million US dollars);
- textiles and footwear - 13.2% (132.1 million US dollars);
- ferrous and non-ferrous metals - 11.4% (114.1 million US dollars);
- chemical products - 11.4% (114.1 million US dollars);
- mineral products - 10.9% (108.8 million US dollars).

![Figure 5: Commodity structure of imports of the Rostov region](image-url)
In the first half of 2016, the value of imports of engineering products amounted to 369.2 million US dollars, or 106.1% of the volume of APPG. At the base of imports of engineering products are various equipment and mechanical devices ($262.1 million), electrical machinery and equipment ($51.5 million), land transport ($19.4 million), boats ($18.3 million). The main trading partners (in descending order of cost): China, Germany, Ukraine, Italy, Belarus, Turkey, USA, Denmark.

In the first half of 2016, the value of imports of food products and agricultural products for their production amounted to 161.1 million US dollars, which is 19.6% more than in APPG. The basis of this category of products was oilseeds and fruits ($46.7 million), tobacco and tobacco products ($41.3 million), cereals ($32.5 million), vegetables ($10.1 million), fruits ($4.6 million), meat and edible meat by-products, and ready-made meat and fish products ($3.9 million each). The main trading partners (in descending order of value): Brazil, Ukraine, USA, Romania, France, Azerbaijan, Belarus, Italy.

In the first half of 2016, the value of imports of textiles, textiles and footwear amounted to 132.1 million US dollars, which is 28.9% more than the volume of APPG. The imports of this category of goods include knitted garments ($38.7 million), garments other than knitted garments ($27.9 million), cotton ($15.2 million), chemical threads ($14.5 million), knitted fabrics ($8.3 million), cotton wool, felt, and chemical fibers ($7.8 million each). The main trading partners (in descending order of cost): China, Vietnam, Bangladesh, Ukraine, Taiwan, USA, Uzbekistan.

In the first half of 2016, the value of imports of metals and products from them amounted to $114.1 million, or 77.6% of the volume of APPG. The imports of this category of goods are based on ferrous metals ($48.1 million), ferrous metals ($42.8 million), tools, cutlery and hand tools ($6.8 million, ($6.7 million)), aluminum and products from it ($6.6 million). The main trading partners (in descending order of cost): Ukraine, China, Kazakhstan, Belarus, Germany, Italy, Turkey.

In the first half of 2016, the value of imports of chemical products amounted to $114.1 million, or 97.9% of the volume of APPG. Plastics and their products ($45.5 million), tanning or dye extracts ($18.1 million), rubber, rubber and articles made of them (13.9 million US dollars), million US dollars), essential oils, perfumes, cosmetics ($8.5 million), soap, detergents ($8.1 million). The main trading partners (in descending order of value): Germany, China, Italy, Turkey, Spain, Ukraine, Poland.

**DISCUSSION**

In order to systematize the implementation of the import substitution policy in the region, the following have been approved:

1. Action plan (“road map”) “Support of enterprises of the Rostov region, producing import-substituting products” of September 25, 2014, which includes a number of key areas such as:
   - Organizational measures, that is, the definition of the most demanded import-substituting groups of goods, analysis of existing production capacities.
   - Increasing the competitiveness of goods and services of the region’s enterprises includes activities to organize the work of scientific and technical and public councils, as well as working groups under the relevant ministries with the purpose of analyzing problematic issues and prospects for the development of import substitution.
– Measures of financial support, which include the compilation of existing support measures and attraction of additional funds for enterprises producing import-substituting products.


The purpose of implementing the regional plan for import substitution in the Rostov region (hereinafter - the regional plan) is the formation by the Government of the Rostov Region of the conditions for outstripping development of certain types of industries, determined on the basis of national priorities, as well as the specialization and resource potential of the regional economy.

In accordance with the need to take into account the specifics of the implementation of the regional plan for import substitution in the short and long term, the tasks of effective import substitution in the Rostov region are:

– Increasing the production of competitive products within existing enterprises;
– attraction of investments in creation of new import-substituting productions.

The main prerequisites for determining the priorities of import substitution in the Rostov region are:

– referring industries and selected types of products to the priorities of the policy of import substitution of the Russian Federation, as defined by the Doctrine of Food Security of the Russian Federation, plans to promote import substitution in industry and agriculture;
– sectoral specialization and resource potential of the region, the availability of competitive enterprises that issue priority or critical, in terms of import substitution, products;
– specific import dependence of the regional market of final and intermediate products of the Rostov region.

The Ministry of Industry and Trade of the Russian Federation, based on criteria of criticality for the economic security of the country and the level of import dependence, selected and prioritized for the implementation of the policy of import substitution of the Russian Federation for the industry. Based on this information, and also based on the industry specialization of the Rostov region, the priority in the industry of the region is:

– machine-tool construction;
– radio electronic industry;
– light industry;
– oil and gas engineering;
– agricultural machinery;
– transport engineering;
– aviation industry (helicopter industry);
– power engineering;
– chemical industry.
Based on the priority directions of import substitution, determined by the Ministry of Agriculture of the Russian Federation, as well as the specialization and resource potential of the Rostov Region, the priorities of the regional policy of import substitution in the agro-industrial complex are:

- livestock (dairy cattle, pig, poultry, beef cattle);
- vegetable growing of open and protected soil;
- processing and storage of milk, fruit and vegetable products, deep processing of grain, construction and modernization of vegetable stores.

Stimulating the expansion of production of existing enterprises and support of investment projects in these priority areas will contribute not only to the implementation of the regional import substitution plan, but will also give an additional impetus to the development of the economy of the Rostov region. The implementation of the regional import substitution plan will allow producing and supplying competitive products not only for consumers of domestic but also for foreign markets.

Figure 6: The set of measures of the regional plan for import substitution in the Rostov Region
An effective tool of implementing policy of import substitution in industry is the creation and development of regional industry clusters. The competitiveness of a region determined the necessity of formation of a set of recommendations, in which a special place is cluster development, including the prospects for formation of inter-industry clusters (chemical, textile industries as providing the engineering and chemical industries as providing), are able through internal synergetic effect to increase the innovativeness of products and increase the share of high-tech industries in the regional economy (Abazieva, Goncharova, Stratan, Gudenitsa & Voronina, 2016).

In the Rostov region successfully develop 10 clusters and cluster initiatives.

The resolution of the Government of the Rostov region from 18.02.2016 No. 104 approved development strategy, six priority clusters - marine engineering “Marine system”, machine tool industry, biotechnology, “the Don dairy products”, information and communication technologies as well as innovative-technological cluster “southern constellation”. Approved by the resolution of the roadmap for the development of clusters, contain measures aimed at the creation of import substituting industries (the production of aviation equipment, optical-electronic and radio equipment, integrated systems and control, robotics systems, scientific hydro acoustic and fishing equipment, processing systems, tool manufacture and machine bases).

On the basis of an industrial complex in Azov Group of MTE in the framework of the signed basic agreements with the Government of the Rostov region and KOVOSVIT MAS is implementing the project on creation and development of a regional cluster of machine technology. The total volume of planned investments in the project amount to 4 billion rubles, including in the implementation of the project invested more than 1.5 billion rubles. Systematic work on increase of production localization. Together with the company OOO NPP “Mechatronics” implemented the project on development and introduction of Russian system of CNC machine tools OOO “MTE KOVOSVIT MAS”. Investor at the end of 2015 submitted to the Ministry of industry and trade of the Russian Federation on the signing of a Special investment contract with the Russian Federation. The contract is planned for the first half of 2016, which will create the most favorable investment climate for the development of high-tech industries and will facilitate access of machine tool companies to the instruments of state support. As a result of full implementation of the project will be established machine-tool production of a full cycle, design offices and engineering center.

In Mines of the holding company light industry “BTK group” is implemented two investment projects. The project on creation of manufacture of hi-tech fabrics from synthetic fibers. Running garment manufacturing, in 2015, implemented the technological launch of production of textiles and hi-tech fabrics from synthetic fibers, which provide a solid Foundation for the creation of the holding of a regional cluster of light industry. Created production will be able to qualitatively compete with world analogues. The volume of investments in these projects amounted to more than 3 billion, created more than 1,500 jobs.

In the framework of 10-th International exhibition and scientific conference on hydro aviation “Gidroaviasalon-2014” signed a Memorandum of cooperation on creation of helicopter-building cluster in the territory of the Rostov region. The parent company is JSC “Rostvertol”. The cluster is formed based on the 6 components:
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- flight test facility;
- Assembly production of helicopters Mi-28, Mi-35 and Mi-26;
- Assembly production of the medium helicopters;
- competence center for the production of composite blades and other products made of composite materials;
- center, operational support for helicopters of the Ministry of defense in the southern military district;

branch helicopter Academy for training and retraining of specialists for the Ministry of defense of the Russian Federation and in the framework of military-technical cooperation.

Among the most promising and rapidly-developing projects of the Rostov region can be attributed to the creation and development of wine territorial cluster “Valley of the Don”.

In the framework of the Concept of cluster development in Rostov region in 2015 – 2020, approved by decree of the Government of the Rostov region from 12.03.2015 No. 164, Union of winegrowers and winemakers of don in cooperation with the Department of consumer market of Rostov region has initiated the creation of a wine territorial cluster “Valley of the don”.

It is planned that the wine cluster will unite the leading scientific, educational, production, engineering and innovation-innovation organizations and enterprises of the Rostov region operating in industries in the following areas: viticulture, viniculture, development of wine tourism, research and educational programs, development of trade infrastructure, the production of components for the wineries.

Meanwhile, members of the cluster, with the direct participation of Department of consumer market of Rostov region, work continues on the expansion of the cluster, and the intermediate result of this work will be enable soon such participants as:

Hotel complex Is;
- “Gidroremservis” LLC (manufacturer of equipment for viticulture);
- “Avrora”, LLC (typography, manufacturer of self-adhesive labels).

At the final stage of the preparation of the strategy of development of the wine cluster “Valley of the don”, which will include the main tasks facing the members of the cluster and possible ways of their solution.

It is planned that the key projects of the cluster will be:
- the creation in Russia of a network of firm shops don wineries of the “Wine of the valley of the don” under the brand “Made on don”;  
- educational activities;
- the development of the wine tourism route.

Each project cluster has already been successfully developed.

So, in the project on creation of network of firm shops “Wines of the valley of the don” under the brand “Made on the don” is currently has 5 stores. The plans of the Union of winegrowers and winemakers of don extension chain stores don wines throughout the Russian Federation in the cities.
Wine cluster can provide good economic results, but also enhance the level of tourist attractiveness of the region, which will favour the development of interest in our region at the Federal and international level.

Despite the fact that economic efficiency and competitiveness are traditionally addressed at the level of individual enterprises, the current dynamics of economic development, characteristic of all national economies in the global economy, demonstrates the growing role of the state (at both national and regional level) in the processes of economic interactions, improve and strengthen support of economic entities (Goncharova & Gudenitsa, 2016).

In the region “work” in almost all forms of state support: subsidizing interest rates on loans, tax incentives, co-financing of costs for technological connection to networks of engineering infrastructure.

Between 2010 and 2015 for this purpose sent to 4.9 billion of the regional budget. 60% (2,926 billion) of these funds are aimed to support enterprises of an industrial complex on realisation of measures on import substitution. The most of import substitution in the region is conducted in areas such as the production of meat, milk, cheese and butter, vegetables in greenhouses and of fruits. In this regard, we defined a list of import-substituting projects. At various stages of implementation are 7 projects in animal husbandry, 7 – in crop and 8 – in the food processing industry. The long-term policy of import substitution can only be realized by investing in the creation of production and the current level. And here, of course, a key tool for the implementation of the import substitution policy remains state support. Another effective measure for the development of import substitution may be a ban state and municipal customers for the purchase of imported products with domestic counterparts that correspond to a specific quality.

CONCLUSION

The substitution in modern conditions is defined as the type of economic strategy of the state aimed at protecting national priorities of socio-economic development and their implementation based on the support of their own products on the domestic market or its separate segments. The growth of domestic production is the major stimulus for the strengthening of the national production. In other words, import substitution should be given the managed nature, which primarily consists in the choice of the most priority directions in accordance with the national economic strategy.

The government of Russia, in the case of the deliberate policy of import substitution by 2020 you can expect to reduce dependence on imports of different industries with the level of 70-90% to the level of 50-60%. And in some industries, can result in the lower.

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