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Strategic Development of Companies in Terms of Economic Integration

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CONTENTS

ABBREVIATION

ABS	Asset backed security
ASEAN	the Association of Southeast Asian Nations
CCT	the Common Customs Tariff
CET	Central European Time
CIS	Commonwealth of Independent States
CM	Common Market
CU	Customs Union
CU CC	Customs Code of the Customs Union
CUSFTA	Canada-USA Free Trade Agreement
ECO	The Economic Cooperation Organization
EDB	Export Development Board
EU	European Union
EurAsEC	the Eurasian Economic Community
FDI	Foreign Direct Investment
FTA	the Free Trade Area
FMF	Financial Market Friction model
GATT	General Agreement on Tariffs and Trade
GDP	Gross domestic product
GGD	General Government Debt
G 7	Group consisting of the finance ministers and central bank governors of the seven major advanced economies: Canada, France, Germany, Japan, Italy, the United Kingdom and the United States
GNP	Gross National Product
HDI	Human Development Index
LP	Labor Productivity
M&A	Mergers and Acquisitions
MERCOSUR	the Common Market of the South America
MRI	Mediamark research Inc.
NAFTA	the North American Free Trade Agreement
NC	National Company
PTA	Preferential Trade Agreement
R&D	Research and Development
SCO	Shanghai Cooperation Organization
SCP	the Structure-Conduct-Performance
SME	Small and medium enterprises
SWI	Social Welfare Index
SWOT	the Strengths-Weaknesses-Opportunities-Threats
UNPD	United Nations Development Program
WTO	World Trade Organization

INTRODUCTION

The Relevance of the Research. In the current business landscape affected by a variety of ongoing international integration projects, one of the main problems is the increased uncertainty, and the accelerated pace of economy change. Increasing unpredictability of markets calls for a strategic response from the companies to improve efficiency, competitiveness, and sustainability.

Commonly accepted ways to counter the negative effects of uncertainty are the formation of an effective system of strategic planning and the use of complex tools of strategic management. Problems of strategic development are particularly relevant for companies in Kazakhstan due to the fact that Kazakhstan is an active participant in economic integration processes. Ongoing reforms in trade policies lead to changes in the economic, political, and social life of the country. All of these changes are a challenge for Kazakhstan companies. Particularly companies should face complex strategic problems, such as ensuring the survival, selection and implementation of competitive strategies and the integration of the new economy, the reform of models of organization management.

Trading unions and free trading agreements are a very prominent part of our current economical landscape, and they have many important implications for all aspects of our life. This approach set the direction, goals, and the internal logic of the study, in which considerable attention is paid to the methodology of the study and evaluation of strategic development in terms of economic integration.

The modern business manager operates in a more dynamic environment. The change in the environment has been rapid and unpredictable.

The most single significant influence on organizational policy and strategy is the environment outside and inside the organization.

Our thesis satisfies for the one of the core principle of national strategy **"Kazakhstan's way – 2050: common aim, common interests, common future"** in terms of mutually beneficial openness. Kazakhstan is going to attract a wide range of foreign investments, technologies, and innovations to our economy. Country will create favorable conditions for the investors. Domestic enterprises will receive opportunity to expand business, increase capacity, find new customers. Kazakhstani companies should be ready for new challenges of economic integration and government should provide favorable policy for business environment [1].

According to the speech of the President of the Republic of Kazakhstan N.A. Nazarbayev, the current trend is the transformation of a unipolar world system in a multi-polar. Regional markets arise where most goods and services are produced and consumed. For Kazakhstan, priority is protection the national economy within the common geographical space.

The changes encourage Kazakhstan and other countries of CIS verify the correctness of the chosen strategy development, to define its place in the complex interweaving of global and regional interests in Eurasia [2].

The level of the topic scientific development.

Approaches to the management of the business is reflected in the classical theories of organization (Weber, F. Taylor, A. Fayolle, C. Henning), psycho-socially oriented theories of organization (D. McGregor, A. Maslow, E. Mayo, F. Herzberg), decision theory (I. Ansoff, E. Heinen, J. March, G. Simon). In Kazakhstan, the challenges of sustainable long-term development of enterprises through improved strategic planning system are reflected in the papers of N.K. Mamyrov, S.Y. Umirzakov, T.S. Satkalieva, K.B.Berdaliev, E.B. Zhatkanbayev, M.B. Kenzheguzin, K. O. Okaev, A.N. Sakhanova, N.T. Smagulova, S.S. Tamenova, O.A. Yanovskaya, J. Sundetov, Z.K. Davelbekova, O.M. Zaluchenova and others.

P. Druker, G. Kleyner, R. Uoterman and others discovered issues of management during the uncertainty of business environment. .

Issues of strategic management focus on the studies of D. Aaker, I. Ansoff, M. Gould, , R. Kleiner, E. Campbell, H. Mintzberg, A. Petrov, M. Porter, A Piston, S. Prahalad, A. Strickland, A. Thompson, B. Henderson, G. Hamel, K. Andrews et al.

However, it should be noted that among the numerous papers there is a shortage of studies about specific market frictions and strategic development of company.

The aim of the research.

The aim of the research is to develop theoretical - methodological aspects of strategy formation of companies in terms of participation of Kazakhstan in the international economic integration.

In accordance with this aim the following objectives were set:

- to explore the nature and theoretical content of the concept of "strategic development";
- to examine economic integration as the main factor expansionist strategy of the company;
- to analyze the structure and stages of economic integration on the example of NAFTA, MERCOSUR;
- to identify the effects of integration on companies, as well as on macroeconomic and social indicators;
- to investigate the effect of protectionist policies on local companies, taking into account the financial and information barriers;
- to investigate the effect of protectionist policy on the SME taking into account financial and informational frictions.

O**bject of study** is the activities of companies in terms of changing trade policy of the country.

Subject of study. Subject of study is organizational and economic aspects of strategy formation of companies under the influence of changes in the company's external environment.

Research methods. We used the methods of theoretical modeling, logical, systematic, and comparative analyzes of building econometric models, statistical analysis of the data using econometric analysis package Stata 9.0.

Theoretical and methodological base of the research is the papers of Kazakhstan and foreign scientists on systems analysis, the theory of strategy, information theory, general economic theory, the theory of competition, agency problem. We use formal logic (analysis and synthesis) methods in combination with the methods of systemic, qualitative, and quantitative analysis in order to achieve the objectives.

The information base for the research have constituted the decrees of the President of the Republic of Kazakhstan, laws and regulations of the Government of the Republic of Kazakhstan address of the President of the Republic of Kazakhstan “Strategy-2050”, the data of the Agency on Statistics of the Republic of Kazakhstan and periodical materials.

The scientific novelty of the results of dissertation research is the following:

First time in the literature we outline two groups of financial market frictions to study the effect of economic integration: informational frictions and financial frictions. For each group we suggest a theoretical model that looks into the cross-sectional difference of the friction effect between small and big firms.

Scientific novelty of the research is as follows:

- new approaches to strategy development companies in terms of economic integration;

- the main barriers to the two groups of financial markets (information and financial friction) to examine the impact of economic integration;

- the effect on the country's participation in the trade union on the main components of the external environment of the company, namely indicators of economic and social development;

- linear regression method and empirical tests conducted to assess the effect of a protective tariff (first used);

- recommendations on the development strategy in the context of changes in trade policy and the introduction of customs duties.

The provisions for the defense are:

- author's definition of "strategic development of companies" through the prism of the impact of environmental factors;

- recommendations for the choice of company strategies in the presence of barriers to international trade;

- the long-term effect of protectionist policies on the basis of a theoretical model of human capital accumulation. First applied the model takes into account the friction of the financial market predicts that the industry's protectionist policies have a small business can lead to a stable equilibrium;

- proposing index of social welfare (SWI), and calculations for the EurAsEC countries.

The Significance and Benefits of the Study.

With the help of three theoretical models we studied the effect of financial frictions for the effectiveness of protectionist policies, financial and informational frictions. The predictions of the models find some support in the empirical tests.

Often economic integration between some countries comes along with protectionist measures directed against other countries. Consequently the costs and benefits of economic integration and protectionist policies are intrinsically inter-twitted. When we try to study the effects of integration and/or protectionist policy, we can focus on only some aspects of the problem, for example only on benefits, or we can direct our attention to the overall effect. In this thesis we employ both approaches. In the first step we study financial and informational frictions and the effectiveness of protectionist tariff policy. That approach focuses only on the effectiveness of protective tariff policies. The second step is to investigate economic integration and social development. We consider the case of the Eurasian Economic Community. The third step is about the effect of integration on the economic growth of member countries. We estimate the net effects of the integration of the former soviet union countries into Eurasian Economic Community.

The results of our study have practical value as a guidance for policy making of the Republic of Kazakhstan. The outcome is also significant for companies that face with challenges of economic integration.

Approbation and implement of the research results.

The main propositions and results of this study were reported at international scientific and practical conferences: Международная научно-практическая конференция «Vedecky prumysl evropskeho kontinentu – 2011» (г. Прага, 2011г.) ,

Международная научно-практическая конференция «Nauka: Teoria I Praktika – 2011» (г.София, 2011г.), Международная научно-практическая конференция «ATNT 2011» (г. Коямпутур, Индия, 2011г.), Международная научно-практическая конференция “Naukowa przestrzen Europy – 2012” (г. Прага, 2012), V Всемирный конгресс инжиниринга и технологий – WCET-2012 «Наука и технологии: шаг в будущее» (г.Алматы, 2012), IV Международная научно-практической конференции «Проблемы инновационного развития нефтегазовой индустрии» (г.Алматы, 2013 г.), V International Congress on Entrepreneurship “ICE -2013” (г.Алматы, 2013 г.), Международная научно-практическая конференция “ Strategiczne Pytania Swiatiwej Nauki -2014” (г.Варшава, 2014г.)

Publications: There are 25 publications including 5 articles in journals, recommended by the Committee for Control of education, 2 in journal indexed by ISI Web of Knowledge, Scopus (Impact Factor-0,234 and 0, 165).

Thesis research structure and size. Thesis research consists of introduction, three sections, conclusion and bibliography with sources and appendices. There are 21 tables, 27 figures and 122 sources of reference in a thesis.

The dissertation outline. The remainder of this dissertation is built upon the following outline:

Chapter 1 basic theoretical and methodological principles are studied, based on which the study was conducted. Methodological approaches to the study of the strategic development of the company have been developed. On the basis of the existing theories of the nature of the concept of strategic development was disclosed. the relationship of the strategic development of the company and its external environment have been established. Economic integration is examined as one of the environmental factors as a challenge for the company. author's concept of the strategic development of the company's management was justified.

The 2 chapter is about contradictory character of integration. Analysis of world experience of economic integration on the sample NAFTA was made. Conclusions made for EurAsEC , as well as for other developing countries. Often economic integration between a number of countries comes along with protectionist measures directed against other countries. Consequently the costs and benefits of economic integration and protectionist policies are intrinsically inter-twitted.

In Chapter 3 we try to study the effects of integration and/or protectionist policy, we can focus on only some aspects of the problem, for example only on benefits, or we can direct our attention to the overall effect. In this thesis we employ both approaches. In the first step we study financial and informational frictions and the effectiveness of protectionist tariff policy. That approach focuses only on the effectiveness of protective tariff policies. The second step is to investigate economic integration and social development. We consider the case of the Eurasian Economic Community. The third step is about the effect of integration on the economic growth of member countries. Estimation of the net effects of the integration of Eurasian Economic Community into companies is one of the output of this chapter.

1 STRATEGIC MANAGEMENT AS A FIELD OF STUDY

1.1 The nature of strategic management: the outline of the subject

Companies of all types and forms today meet a wide range of challenges as risks, troubles and issues, be they strategic, operational, financial, purchasing power, marketing etc. Uncertainties are increasing due to the rapid inevitable globalization processes affecting all countries with the further regional expansion in Europe, Latin America, Arabic continent, Asia. These regions take an active part in the process of economic integration. The influence of an external environment has positive and negative effects to the companies as two sides of one coin. Company should respond to environmental changes and be ready for the challenges in order to be on the wave of success. The best way to prevent threats is coordinate strategic management process in the company.

There are plenty of literature sources about strategy, all of them mainly are about theoretical issues of subject. There is a shortage of studies with empirical evidence in strategic management. The practical issues have more significant value in the process of making a plan and decisions.

In our research, we want to make a deep analysis of the concept of the word "strategy". The term "strategy" means a plan of action in the general sense. Well-known fact that this term has a meaning as art of troop leader or office of general.

In the military "strategy" uses as the plan of war actions, creating in the beginning of the war before the battles, but the plan is constantly changing depending on the outcome of the battle. Strategic development in these conditions is the variation of the plan of actions. In the Game theory, strategy is any of the options player (in our case company) chooses where the result depends not only on his actions but the activity of bystanders from the external environment. In the dictionary the strategy is a "plan chosen to bring about a desired future, such as achievement of the purpose and objectives or solution to the problem". In the business sphere strategy is " the outcome of choices owners do, on where and how to play, to maximize profit". [3] In practice, strategy and action plans are often intertwined, and they influence each other significantly and constantly.

Analysis of "strategy" meaning shows that this term is new in the history of management and economics. Original concept based on the context of competition and military terminology. Further, under the strategy began to understand the long-term set of goals and objectives to ensure effective interaction with the external environment of the company. Next milestone is the strategy a comprehensive plan designed to ensure the implementation of the organization's mission and the achievement of its objectives. When the companies identified the necessity of strategy, the strategy was as a way of actions for managers. There is a complete systematization of data views understanding strategy by various authors as follows [4,5]:

- a way how to achieve the results;
- the coverage of all major aspects of the company;
- plan of actions;

- coverage, considered as actions aimed at winning in competition;
- procedures, plan may be unrealizable, but procedures should be provided in any case;
- the communication with its environment;
- mission and vision of company;
- the result of the SWOT analysis;

There are five determinations of strategy proposed by Mintzberg that show a multifaceted concept of strategy: plan, ploy, pattern, position, perspective. There is a famous Model of 5Ps of strategy [6]. For implementing each out the five P, company has to develop a plan for achieving purposes and objectives of the company. Thus, planning is a task for managers, and it's something that comes usual. According to his opinion strategy includes idea about competitors, especially prevent companies call on the reaction [7]. Strategy is like a scheme that shows the road how to achieve the destination in the company's development way. What kind of methods and tools are using for company results is also considered as a part of the strategy. Thus, the purpose of the strategy is to find a link between organization and environment, expand a sustainable core position of the company. Mintzberg highlights the role of culture in the cases when company makes choices about its strategy, he compares with the way of thinking that can be positive, neutral or negative [8].

We can research strategy formation in a broad descriptive context. A strategy is defined development and definition of organizational goals and objectives that have found concrete expression in the annual and long-term plans to anticipate and fix future state of the organization at the current time. Clearly developed market strategy provides flexibility in managing the organization, skill and ability to rebuild quickly, use new opportunities offered by the market, see prospects. The process of forming a financial strategy, in our view, includes the following main stages (according to Figure 1):

So, the first stage is the determination of the strategy implementation. There are several factors influencing the duration of the first stage. Factors can expand or reduce the time gap of the stage. These factors are the dynamics of macroeconomic processes and, changes occurring in the financial market, sector and specificity of the external environment of the enterprise.

The second one is analysis of environmental factors of the enterprise.

Formation of strategic goals of the company is the third one. Maximizing the market value is the main objective in this period. System of strategic business objectives must be formulated clearly, reflecting each of the objectives in specific terms, regulations.

The forth one is development of the system of measures to ensure the implementation of the strategy. In our view, this step is the most difficult, because the success of achieving goals is directly determined by the adequacy of the strategy tools.

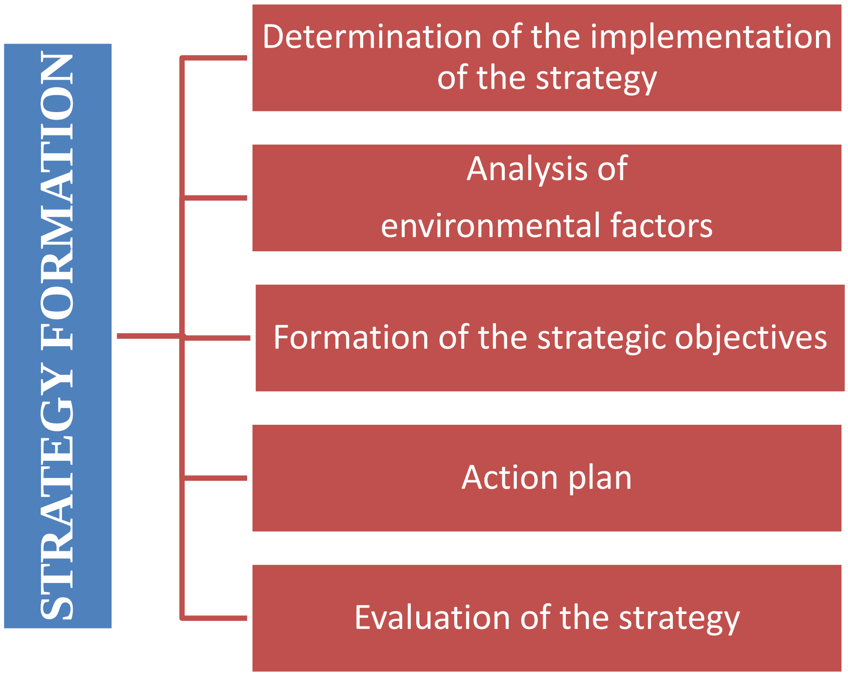


Figure 1 - Stages of Companies Strategy

Note - Compiled by the author

The final stage is evaluation developed strategy. In the practice of Kazakhstan companies questions of strategic development   are not adequately understood, the reason is   the lack of experience. At the same time, the development strategy has been hampered due to the development of inflationary processes, lack of confidence in the future.

Analysis of approaches to defining a strategy in the works of modern Russian and Kazakh scientists reveals the following judgment. Thus, A. Lotov believes that the "strategy - the definition of long-term goals of the company and the choice of the most effective ways and means of achieving them" [9]. This definition seems to us concise and succinct. At the same time, we believe that the strategy – it is part of company policy, which means that it includes not only the goals and instruments, but also events.

A. Teslinov gives the following definition: "The strategy - a set of interrelated decisions that determine the priorities of the enterprise resources and efforts to implement its mission" [10]. However, he notes that as a distinctive feature of strategy - making uses two features - the irreversibility and sustainability impacts. This means that the implementation of the strategic potential of the company making changes and return to the previous state of the control object and if possible, it requires a lot of time, resources or effort. Obviously, solutions of this kind are taken sooner or later in any enterprise, even where not used the notion of strategy.

According R. Fatkhudinov point of view, the most important thing is improvement of quality management. Implementation of competitive advantage is based on the essence of the values that are source of benefits (tangible, intangible, financial and social, etc.), and depends on its content, source of origin, dynamic manifestations scale distribution and other conditions [11].

Different approaches strategic activities of study, industries, businesses, brought to life by the ongoing development of market relations market actors of globalization. In this regard enterprise strategy - a set of objectives, actions aimed at sustainable operation with volatility factors of the environment and the efficient use of internal factors.

Fortune magazine published the results of the research about the reasons for the failures of major corporations. It turned out that only 10% of corporations successfully implement its strategy and achieve its goals. The cause of the majority of failures is not low quality strategies themselves, and numerous errors in their implementation. According to a study Harvard Business School, conducted among 937 global corporations, there are four reasons that do not allow corporations to implement their development plans [12]. The first reason is that corporate strategic plans are not coordinated with the daily activities of their employees, i.e. employees of companies do not understand the strategic objectives of the development of their enterprises. According to the survey, 93 % of employees do not link their findings with the strategic objectives of their corporations. Second, in most corporations and incentives of top managers and staff directs them not to implement the strategic plans of the company and the achievement of the current financial performance. The survey showed that only 15% of performance indicators used by corporations linked to the need to achieve strategic goals and only 24 % of managers are motivated in their work on the implementation of the strategy of the company. Third, resource allocation plans and budgets are not tied to corporate strategy. According to data obtained by researchers Harvard Business School, budget 73% of corporations associated with providing ongoing activities rather than strategic objectives. Fourth, investment projects and development programs serve to solve tactical problems and tend to ignore the strategic directions of development. The study found that only 18 % of intra- development programs aimed at implementation of the development strategy. Thus, we can formulate a number of theoretical and practical problems:

- linking strategic management action now with its development strategy;
- identification of priority facilities management (based on the monitoring of factors internal and external environment) in relation to the particular stage of development of the enterprises;
- develop clear mechanisms for implementation of the strategy to ensure the company's competitiveness.

Evolution of strategic management theory is considered as a transition from ideas of organization with its external environment to the concept of competitive advantage, then - to the priority of organizational and managerial factors of competitive advantage and understanding of the economic rents as the main result of successful strategies, afterwards to the priority of the dynamic aspects of strategies, particularly to organizational learning.

One of the Russian scientist V. S. Katkalo in his thesis "Evolution of theory of strategic management" identifies four stages in the evolution of strategic management theory:

- the first phase (1960 - first half of 1970 years) - School of Planning (A. Chandler, I. Ansoff, K. Andrews);

- the second stage (the end of 1970 - 1980 years) - School of positioning and organizational concepts strategies (M. Porter, H. Mintzberg, J. Quinn);

- the third stage (the end of 1980 - 1990 years) - resource concept of strategic management (B. Wernerfelt, J.. Barney, S. Montgomery, Prahalad, G. Hamel);

- fourth stage (the first decade of the twenty-first century) - the concept of dynamic capabilities (Teece D., G. Pisano, K. Eisenhardt, I. Nonaka, X. Takeuchi) [13].

Alfred Chandler, Igor Ansoff and Kenneth Andrews were the pioneers who developed the idea of business policy, later renamed the strategic management. The American economist Edith Penrose in her book "The Theory of the Growth of the Firm" (1959) described how companies can grow and explained the role of managerial decisions for the growth [14]. Herbert Simon, Richard Cyert and James March developed the idea of bounded rationality to study the decision-making process in firms [15]. They assumed about information uncertainty in the market and discussed role of managers in the case of vulnerability of the environment. An author of famous paper "Foundations of the Theory of Organization" (1948) Philip Selznick postulated for corrective internal factors to the external environment [16]. Selznick is the author of organizational theory, he developed the theory f strategy by placing an emphasis on the internal characteristics of a company.

Alfred Chandler was a follower of the Selznick's and Penrose's ideas. He examined American organization as General Motors, Standard Oil, Sears and du Pont de Nemours. The output of his studies is that higher productivity is possible when company has coincidence managerial organization with corporate business strategy [17].

After the expansion of the field ‘strategic management’ in the late 1970s, the focus moved towards industrial organization economics. This period is the time of the structure-conduct-performance paradigm. The basic idea of this paradigm is company’s specialization directly depends on the nature of the industry where company competes. The conduct of the company is just a reflection of the industry structure, so company decides which industry is better for the competition. Michael Porter represents this paradigm in his papers about correlation between competitive advantages and firm strategies. He developed “five forces” model that allocate different features of the industry and which determines its attractiveness and facilitates competitor analysis. He proposed the idea of generic strategies as a differentiation, cost leadership, focus, adaptation [18].

Other important studies about competitive dynamics were influenced by industrial organization economics. The basic interest of competitive dynamics is to investigate how firms are achieving competitive advantage by carrying out different types of strategic and tactical actions. Engaging in competitive dynamics can have severe implications for both incumbents and challengers. Research has shown that market leaders can only retain their strong position if they initiate more actions than their challengers, if they use a broader range of actions and if they undertake their actions quicker than rivals.

1.1.1 A consensus definition of the field

From this short historical overview we see that in the foundation of strategic management were involved scientists from different areas such as economics, sociology. Such an interdisciplinary field often suffers from a lack of clarification. However, with the clarification, a field is limited in its growth. Analysis of the literature review let us summarize the meaning of the strategic management. The nature of strategic management includes all these following issues:

1. strategy is about important initiatives;
2. strategy is a deal of managers;
3. strategy involves applying of resources;
4. strategy is for increasing the effectiveness of company;
5. strategy is not constant; it tends to be variable and must satisfy to the external challenges with consideration of internal capacity.

They, therefore, definition of basic concepts allows us to identify possible changes and perspectives in the development of theory.

1.1.2 Factors of external and internal environment

Among indirect factors that have impact on the organization's activities we can highlight following:

a) the condition of the economy. Leadership of the organization, especially when entering the international market, should take into account the economic situation in the country. The global economy affects the cost of resources and the ability of buyers to purchase goods and services. If the economy is projected to decline, it is necessary to reduce the stocks of finished products. This should be taking into consideration when we want to increase or decrease interest rates, during the possible currency fluctuations.

b) scientific and technological progress. Technical innovations enhance productivity, contribute to the improvement of product quality, as well as expand the possible applications of the goods. The appearance of high technologies has a significant impact on the development and action of companies. Technology helps to reduce the variable cost and increase the competition in the same time.

c) social and cultural factors (for example life values and traditions, customs, attitudes, organization) have a significant impact on the company's action.

d) political factors are the most unpredictable and volatile (economic policy administration, taxation system, trade policy, consumer protection laws, standardization) .

e) relations with the local population. The relationship with the local community is very important for accounting and planning in any company.

All these factors come from the external environment and requires company's reaction.

In this case, organizational capabilities play an important role to respond to unpredictable environments (Figure 2).

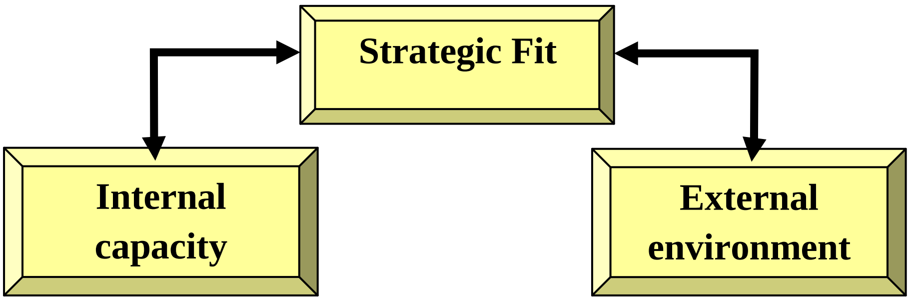


Figure 2 - The Relationship between Strategic Fit and Internal Capacity & External Environment

Note - compiled by author

According Coulter (2008) point of view environment is divided into two parts as the two sides of the same coins:

- in market conditions, there is an information friction, and the environment is a source of the uncertainty;

- the environment is a source of resources perspective [19]. We focus on the environment as sources of information to analyze how the external and internal analysis provide and influence the management in companies for planning and decision making (Figure 3).

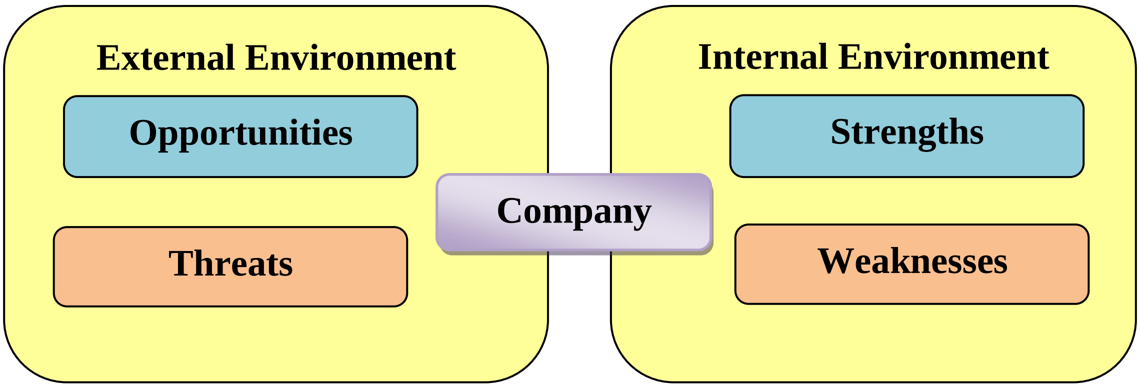


Figure 3 - The relationship between company and environment

Note-: compiled by author

As we can see from the figure 3, the internal environment of the organization is within the organization and had a continuous and direct impact on the company. The internal environment of the organization is the source of its life systems. It contains the potential that enables organizations to operate, exist and survive during the challenges. However, the internal environment can be a source of problems. It possible when company does not provide the desired operation of the organization.

In contrast the external environment is a set of active business entities, and other external conditions and factors operating in the enterprise environment and affecting different areas. External factors cause the external environment of the company.

External influences are conditions that the company can not change, but must constantly be in their work. For example, it is consumers, government, economic conditions, business political.

State of the environment is crucial for the business, as the external environment to the organization is an objective environment. It exists independently, which leads to the need to integrate it in their work. In this regard, the correctness of accounting for all aspects of the external environment depends on the effectiveness and efficiency of the company.

Typically, a company in the process of managing itself determines which factors and to what extent can affect the results of its operations in the current period and future perspective. The appropriate management decisions are making with the consideration considering the definition of the importance of each factor. So for small companies not exporting products is not a significant fact to reduce trade barriers. For export-oriented companies, this is a great opportunity to increase the market.

The link between internal and external environment is manifested in the fact that companies have to adapt to the external environment by adapting the internal environment, which determines the behavior of the organization.

It is important to provide not passive adaptation, and the desire to influence as far as possible to environmental changes. Very often company, continuing to compete or combined together to create new products that better meet consumer demands and update key market segments.

The advantages of such cooperation are to reduce the risk, sharing knowledge, resource savings, access to raw materials, technology, labor, capital, sales channels, customers. Such cooperation could lead to a merger or acquisition. But most of all organizations maintain independence and cooperate within the framework of such networks.

1.2 Strategic development as a subfield of management

The essence of strategic management is to move from a strategic choice to strategic change. The relationship of concepts “change” and “development” suggests that the problem of strategic development of the company fit into the framework of the concept of dynamic capabilities [20].

An analysis of the scientific literature concludes the complexity of the concept of "strategy", and there are certain discrepancies in its interpretation among the authors. Differences in the interpretation of the categories likely caused by a desire of the author to specify the concept of "strategy" based on isolated development trends in the internal and external environment [21].

There are two different approaches to understanding the strategy. In the first approach, the vision defines firstly. Implementation of the strategy involves the preparation of the plan with its divisions by time intervals. An example is the long-term plan for the production of certain products, which shows what and how much to produce in each period. This approach of the strategy was formed in the early stages of the strategic management theory. In this case, strategy development is the process of finding long-term goals and making a plan. Therefore, the company's strategy in a market economy should primarily focus how to gain from the changes.

The second approach considered as a long-term qualitative determination of the company. The strategy can be described as the chosen direction of the further behavior in an environment in which the company should achieve its goals. Strategies that reflect the understanding of the second approach may include:

- increased volume of sales in the market to a certain percentage without decreasing a price;
- the start production of a new product, while reducing the production of another;
- penetration to the distribution network, controlled by a competitor;
- the development of fundamentally new technology of production;
- the acquisition or enhancement of economic security, and so on;

Each stage of economic development is consistent with its view of the understanding the development strategy of the company. As the external environment changed, the concept of strategy increasingly concretized and clarified. Therefore, the external environment acts as a catalyst for change in the development of policy theory.

In our study, we are the followers of the second approach. We consider it is necessary to determine the strategy as a dynamic category rather than static. Our preference in approach we do on the basis of a literature review.

The basic concepts of strategic development of the company are:

- the theory of maximizing sales revenue;
- the theory of maximum growth;
- the theory of multiple objectives [22].

A goal of managers is to maximize sales and revenue. This assumption is basic. Managers are interested in maximizing sales, due to their direct self-interest, because of the links with their remuneration.

J. Baumol (1959) and Williamson (1963) developed first theory using the empirical evidence. Empirical data show that the desire to maximize sales is true only in the short term. There are a lot of unpredictable situations, economic fluctuations and frictions for companies in the long run [23]. R. Marris (1964) continues the approach with the possibility that the owners and professional managers share a common goal of ensuring business growth and competitiveness [24]. The crucial element is the justification of the rule of undistributed income allocated to the development of production. In each case, the owners and managers must provide the required combination of profitability and sales. We can explain internal growth and efficiency through the development of a variety of sources, including his own and borrowed funds. The second is the strategic merger. Thus, there is a replacement of the merging companies shares for new shares of a single sample. In this case there may be different types of mergers: horizontal integration, vertical integration, and conglomerate. Absorption also implies the acquisition of a controlling stake in one another firm, while the absorbed company ceases to exist as an independent entity of the market. Theory of multiple objectives based on the premise that the company has set goals, which are the subjects of staff, managers, shareholders, society. In this regard, the company can be competitive, socially -oriented, management needs to coordinate private and strategic interests, to ensure their balance. Japan's experience is instructive. Japanese companies harmonize the interests of staff, companies and community. In general, this concept is based on the use of trade-offs [25]. Strategic development of the company's strategy is changing under the influence of changes in environmental factors. In this case, the changes are measurable, using the same indicators as maximizing profits, increasing sales, attracting investment.

The process of evaluation of investment attractiveness regulated by a system of evaluation of different levels of subordination, rules and regulations [26]. Study on the strategic management and competitiveness in the modern Western economic literature associated with the development of methodological tools of evaluation the company's position in the market [26]. Thus, Boston matrix is a matrix of decision-making taking into consideration two parameters as the market share and growth rate. Boston matrix allows to make a fairly simple classification of goods and to propose a plan to work with each item [27]. Analysis of this approach allows us to draw the following conclusions regarding the features of the matrix of the Boston Consulting Group. The prospects of development of the company are possible to measure trough two indicators like the rate of growth segment of the market and a share of the segment. This ratio determines the relative competitive position of the organization in the future. Products with a high degree of market segments have enough financial return goods with the same small part of the market share of almost profitable. Matrix offers the following classification companies: “star”, “cow”, “question mark”, “dog” and suggests appropriate strategies for them. Thus, we see that the Boston Consulting Group experts link strategy companies with market. Multifactor model of competitive position, otherwise known as the market attractiveness matrix was developed by experts from the consulting company McKincey & Co [28]. Model McKincey is a pattern consisting of nine cells to display and comparative analysis of the strategic directions of economic positions of the body. BCG Matrix allows you to visualize, to see the structure of the portfolio of products, to identify sources of funding and to make decisions on the withdrawal and the development of individual products. There are four categories of the whole system showing that the strategic development is the process depending on the meaning of axes.

Issues of development strategies were presented for the first time in the papers of Peter Drucker. In his opinion, only leaders of change can survive, those companies who catch the light patterns of changes and instantly adapt to them using their benefit opportunities. Strategies need to be constantly developed, this process is endless and not predictable [29]. Drucker describes strategy in the case of companies decision-making process at present about a future that is natural uncertain. Most notably, Drucker concluded about inability of strategy to remove the risks. External environment of the company is full of uncertainties that a the sources of the risks. The companies must take a risk and manage them. In Drucker's words, the issue is that company must identify the possibilities of risks and have a solution before [30, 31].

He mentioned about four main misconceptions arising from the term strategic development:

1. Strategic development is not a bundle of techniques.
2. Strategic development is not forecasting.
3. Strategic development does not deal with future decisions. It is a current solving future problem.
4. Strategic development is not an attempt to eliminate the risk. The case is about how to have deal with uncertainties and take a risk.

Drucker’s writings contributed to the philosophical and practical foundations of the modern business corporation.

The next guru of strategic management is Henry Mintzberg. His book "The Rise and Fall of Strategic Planning" (1994) is about criticism of understanding strategic development as practices of strategic planning [32].

Later his idea was supplemented by K. Andrews and C. Christensen in their famous work the "Model Harvard Business School ". The model is based on the well-known procedure SWOT- analysis [33]. H. Mintzberg calls this as a "model school design " because it is based on the belief that the policy formulation process as based on a few basic postulates, providing “design strategy”[34]. In this case external environment comprises all factors that are outside the organization and affects it. Organization's ability to respond and cope with these changes are the essential component of success.

M.Porter describes strategic development through the two hands. The fist one is the scale of the market (two outcomes are possible either wide or narrow). , in the case of effort to minimize costs, or to produce unique products, on the other hand, that allows to charge higher prices [35].

Thompson and Strickland analyzed the development through the model of classification of financial strategies:

- cost leadership strategy (cost reduction, which attracts a lot of customers);
- broad differentiation strategy (giving goods specific features that attract a large number of customers);
- strategy optimum cost (high value for customers through a combination of lower costs with broad distinction);
- focused strategy or market niche strategy based on lower costs (lower costs and a narrow segment of buyers);
- focused strategy or market niche strategy based on product differentiation (complete customer satisfaction from the segment) [36].

The concretization of the objectives of the strategic development is achieved through the development of strategic development programs, including complex tactical and operational objectives. The most important element of strategic management development is the principles of strategic management organization.

The complexity of these principles selection is concerned with understanding how to manage the enterprise and, at the same time, self-organizing system. These general principles of strategic management must be supplemented by the following set of principles. These principals reflect the specificity of the strategic development of the company:

- accounting for initial conditions of the company in the market, that allow to improve the quality of the strategic selecting process;
- a combination of governmental and self-reflected organizational structures of management that provides strategic decision to initiate the "bottom";
- availability of innovative corporate culture, ensuring the formation of the company's commitment to the implementation of personnel changes;
- creation of the subsystem resistance to change, ensuring that the objectives to manage and control subsystems in the strategic development of the company are followed;
- a combination of control methods of direct and indirect impact on the controlled object;
- the transparency of boundaries between the enterprise and the market;
- the increasing importance of transaction costs in the development and implementation of strategic development goals of the company;
- compatibility of institutional development of integration strategies;
- hierarchy of basic competitive strategies and functional development of the enterprise;
- determination of life cycle development of company, prior strategy development and implementation;
- the absence of a strictly quantitative estimates projected in the strategic planning process;

Criterion for evaluating the strategic development of the company is its competitive position in the market. This rule is not rigid and is specified on prevailing market situation. The primary tool for achieving the target of strategic guidelines is basic competitive strategy (leadership in minimizing costs, differentiation, focused strategies, policies optimum cost). The choice of correct strategy is carried out in strategic positioning and analysis of the internal/external environment of the company, including an assessment of its resource capabilities and barriers existing in the market. The magnitude of the barriers depends on the level of competition (monopoly) on the markets. Therefore, an individual level of competition is an important step in the selection of basic strategies of enterprise development. Moreover, an important tool for the strategic development implementation of the company and study the basic competitive strategies are to develop models of its life cycle. Qualitative and quantitative characteristics of the business life cycle allow us to describe the behavior of the system and to identify the most significant moments in its development. In this regard, it is necessary to operate at the same rate the pace of organizational and technological development of the company as a condition for the sustainable development.

One of the fundamental objectives of strategic management in organization is to validate the model of business management, corresponding to the chosen development strategy. Model of strategic management structure is represented as a set of organizational structures, functions and management practices according to the specific features of its strategy. This model is based on organization of strategic management, which represents the “new school” of management. The principles of “new school” are based on three methodological approaches - the system, process and situational. One of these trend shows that the company often incorporates elements having a dual identity. Increasing the degree of enterprise openness and foreign expansion of its borders is a method to solve very specific problems relating with the issues of strategic management of the company. One of the key issues of the implementation strategy is the account of the time factor. Time factor is a certain amount of time needed by company to achieve the goal or result. Therefore, an analysis of the environment change rate and their possible correlation with the speed of adaptation is an important problem of strategic management. Data synchronization process means less time on the “recognition” of changes in the market [37].

1.2.1 Strategy of expansion to local and foreign markets

Primary task of company's management becomes maintaining equilibrium at the internal and external environment, as well as the development and use of effective mechanisms to adapt the organization to the challenges. If the external environment is relatively stable, the organization's leadership is committed to greater centralization of power, creating a rigid organizational structure of management - oriented management control over the entire process chain. Organizational structures become more decentralized, flexible, allowing quickly and react to change.

There are an evitable process of globalization resulting expansion of market boundaries and involving Western firms in a competitive environment. Direct use of this experience Kazakh entrepreneurs often difficult because of its uniqueness, the lack of universal schemes competitive behavior in the market.

One of the main ideas of the strategy is to adapt to changes in the environment, impact on its condition and at the same time to maintain a course to achieve competitiveness. According D. Aaker strategic market management is a warning and looking to the future character. The strategy should not obey the environment; it should not take it as a given. They are obliged to anticipate possible changes, impact on events inside and outside the company. So, with the help of creative, active strategies we can influence (perhaps even control) on public policy, customer needs and technological progress [38]. Many authors associate the process of adaptation to the environmental changes with the concept of adaptation.

The concept of adaptation takes leading positions in various theories and therefore requires more detailed consideration. Initially, the term “adaptation” was used in the review of biological systems, and meant a long evolutionary process of adaptation to environmental changes. The central feature of biological systems adaptation is that the process of adaptation uses only the available information about the environment. Thus, as a rule, targeted external impact on the system is absent. In socio-economic systems the development trajectory based on projections, to some extent casual and uncertain, but the lack of information is covered with the practical knowledge, the simulation results, expertise and so on. In making management decisions focused on the changes in the system, the fundamental difference is the adaptation of socio-economic systems of adaptation to biological systems.

The adaptation is “a complex concept, which includes a variety of conditions to which the system can be adapted (adaptability) and the ability of the system to detect purposeful behavior in complex environments ” [39].

The author of the well-known paper "Capacity for World Strategic Management" (1998) written in english by Russian scientist E. Markarian calls adaptation strategy as a tool to dynamic equilibrium [40]. The author notes that the adaptation of the system not only functioning, but also the development. The effect is achieved by ordering of t those parts of their environment with they interact. Adaptability always involves an individual corrective action in relation to the external environment. The source of changes can be processes that occur independently of the behavior of the system and due to own actions. In the latter case, the system must adapt to the changes brought about by itself. In this regard the adaptation is a reaction to changes in the conditions of companies internal and external environment, that has the adverse effect to the efficiency [41]. Adaptation is rather broad concept that we can divide for narrower groups. Thus, one of the criteria is the time gap (we identify short-run and long-run), one is occurs quickly and second is close to the idea of development. According the changes in structure and activity, we can define adaptation by innovation or expanding business. During the passive adaptation, the organization changes its behavior under the influence of the external environment, with active adaptation- affects its status.

In the presented definitions can be seen a common understanding of adaptation as the socio-economic tools applicable to changes in internal and external challenges. Western research studies identify the purpose of self-preservation as the adaptation of the system [42].

The adaptation obtains a favorable impact of the system and aim is the existence of an organization in a particular environment [43]. The purpose of adaptation is to counter actual or potential reduction in the efficiency of the organization. There are ongoing debates about the existence of different criteria for assessing the adaptation. Prospects in understanding the adaptation associated with early recognition and the development of new business opportunities. Therefore, a targeted strategic guideline in the adaptation process is to counter a possible decrease in efficiency of the company .

Therefore, the principal decision companies do in the case of export marketing strategy to domestic conditions. An suitable stage of adaptation is a indicator of market performance.

Adaptation is about differences between countries. These differences could be structural, consumer-based or cost-based transportation and communication costs.
Building a network of the international operation through overseas direct investment is an important aspect of the company's global strategy. Companies become

multinational through the foreign direct investment. Applying all the advantages of an exporting company may contemplate on the example of expansion strategy.

Expansion implies an increase of consumers, sales, production volumes. The strategy is active, aimed at increasing profits. However, we need an appropriate management. Expansion strategy aims for a positive results but associated with high risks and possible changes of external environment.

There are two reasons of implementing expansion strategy, one is changing in a customer type and geographic location is the second.

A.Thompson and A.Strickland discussed in their article that fast growing markets make company working harder to be in trend and drive more sales for future development of competitive advantages and capitalize the profit for saving positions on the market. At some company could want to start developing vertically to strengthen the positions [44]. M. Porter also confirms that vertical integration improves company's ability for differentiation, because this would give more possibility to add more margins on product price. For example, this could potentially expand sales channels and improve customer service. Production of some components also could be driven by differentiation strategy [45].

In the case of changes in market that make company running slower differentiation strategy can be replaced with diversification strategy. There are two types of diversifications: concentric and conglomerate. First one is about improvements of existing products through the technology or marketing. Conglomerate diversification is based on non-technological stuff. This the strategy is about high growth.

Leadership strategies to minimize costs and differentiation are quite clearly defined their scope. However, as we approached the equilibrium point in the test matrix, the differences between these policies do no longer exist, and there appears the scope of the so-called strategy of optimal costs.

The distinguishing characteristics of this strategy is the development of products better and differ than your competitor has.

In markets where consumer preferences make product differentiation as a standard and many buyers are looking at the same time both to the price and the value of the goods, the optimal strategy is preferable to the cost of pure strategies of low cost or differentiation. The reason is that the company with optimal costs can offer a product of average quality at a price lower than the average or good quality product at an average price.

The company should remember about the costs: any, even the highest margins will not lead to anything, if the company does not take on the best cost position. When company chooses differentiation, it should strive for equity or approximate equality costs relative to its rivals. , Focused strategy of differentiation depends on the consumer segment, which requires unique features and characteristics of goods [46].

The above conditions for the application strategy of focusing on differentiation are a highly controversial. Multidirectional impact of scientific and technological progress and competition in the state of the industry market is reflected in the simultaneous presence of high and low barriers to industrial output and, the presence and absence of preconditions for vertical and horizontal integration, and so on

In this case, the visible position can be summarized as a scheme to move steadily from the study of the most stable relationships that characterize the essence of management, to elementary administrative actions due to specific features of a particular object management (figure 4)

Strategy development of industry
Principles of industry management organization
Organizational forms and industry management structures
Management mechanisms of production and economic activity
Organization of management processes by different branches
Development technology and making management decisions
Realization procedures of concrete management decisions
Analysis of the results of management decisions

Figure 4 - Systematic approach scheme to the organization of the industry management

Note - compiled by author

Development of a strategy is the starting point, a basic step in the organization of management. The strategy of the company is the basis for the development of principles for governance, organizational structures and governance mechanisms. In the framework of the chosen organizational structures, using the appropriate management mechanisms, developed tactics of enterprise management, without specifying that is impossible to implement the strategy. The objective of the development of tactics is to organize management processes as a flexible interaction of successive management functions.

With the high level of information security standard-parametric technology is used widely in decision making based on the databases of the availability of financial, material, labor and other resources. However, this technique is difficult to apply in various innovations or situations involving a high degree of uncertainty, and in the absence of sufficiently developed legal framework.

In recent years the huge technological development was established, based on the use of econometric models. Models are particularly important in circumstances where it is necessary to make decisions in complex situations requiring evaluation of several alternatives. A large number of different models can use this technology in operational management and strategy development industry.

After establishing management decision, there is a problem of its effective realization. Administrative decision must be brought directly to the performers without any mistakes. For successful implementation of management solutions, special procedures that regulate the activity of each of the participants in accordance with its duties, rights and responsibilities have been developed. With the developing management realization procedures, there is an important place to communication systems, including different electronic systems, and also necessary feedback.

The final stage of the organization of control processes is to analyze the results of the implementation of management decisions. The analysis compares inherent in these management decision results of production and economic activity, and the actual data on the implementation of this decision. Analysis complete with identification of the causes of deviations from planned results and developing recommendations to eliminate distortions in the implementation of the administrative decision. A summary of the systematic approach reflects only the general features of this concept, which is more or less inherent in the theoretical development so-called "new school" of management.

Followers of this approach are R. Ackoff, I. Ansoff, Bertalanffy, R. Kalman. They consider business management as the organization of interaction of all the factors that make up the industrial and economic system.

In B. Karloff's studies different conceptual approaches to management are associated with specific countries [47]. He wrote about the Japanese three pillars (lifetime employment, seniority premiums and trade unions in enterprises). Among all varieties of models experts recommend two main models of business management, there are "growth model" and "situational model of development" (see Table 1).

There is a reflection of the main features of the organizational management, based on the mission of "natural development" in the first model. The idea is increasing production volumes for the traditional enterprise products and services, followed by access to the production of the set of products, as well as scaling production through vertical integration (merger with or acquisition). In the cease of growth model, the possible way to increase profits is to reduce production costs.

An alternative model in relation to the growth model is the concept of the situational approach, based on the principles of fast and flexible response to environment changes. Situational development model aimed at a continuous search for new and more profitable ways of capital investment, the use of the potential of high returns even with high risk of new businesses.

The ideal management is a structure that enables the company to effectively interact with the external environment, to increase productivity, meet customer needs and achieve their goals with high efficiency. There is another point of view, consists in the fact that there is no perfect, ideal organizational structure of management.

Table 1 - Main models of organization of business management

Expansion model	Situational development model
Management strategy is based on achieving long-term targets	Management is based on realization of short-term targets
The gradual development by increasing production within the existing specialization	Expanding the scope of business due to the constant search for new activities by diversifying
Maintaining a stable long-term relations with its business partners	Focusing on finding the most profitable partners, frequent changes of suppliers and intermediaries
Stable organizational management structures	Flexible organizational management structures
Formation of a stable state employees (system of "lifetime employment")	Significant fluctuations in the number of employees, the prevalence of contract system of employment
Focusing on making a profit while minimizing business risk	Focusing on higher profit even through risky business transactions
High level of centralization of management functions	Decentralization of management functions
The predominance of collective forms of management decision-making	The predominance of individual forms of management decision-making
Specialized management training	Unspecialized training or hiring management personnel generalist on a contract basis
Complex procedures of management decisions on established traditions	Simplified procedures of management decisions on established traditions
Formalized procedures for the implementation of administrative decisions	Flexible approach to the organization and implementation of management decisions
Source - Adapted from source [48]	

1.3 Economic integration as a major factor for expansionist strategy of company

Modern trends of globalization processes between the industrialized countries and the less developed and developing ideas contribute dominance of protecting national interests. One way is the creation of integration alliances based on the expansion of the region, the use of common rules and requirements for economic activity. Economic integration is a historical process occurring over many centuries. The essence lies in the integration of interstate association that has its own organizational structure. Countries - members of unions tend to deep integration division of labor intensive exchange of factors of production. The idea of a close relationship primarily for political purposes between the two countries has been characterized since ancient times. Processes of integration, cooperation, development of a broad cooperation between the countries are most common in the context of globalization. The bases of integration between countries are the processes of the international division of labor based on specialization of each country to produce products according to the presence of absolute advantage. Surplus items formed the basis of origin of barter transactions between tribes, economy and the state. The next stage of integration was overcome distances between countries to increase trade and commerce products. Means to achieve these goals were conducting world tours, organization of trade caravans and ships, is allowed to expand and strengthen the capacity of economic cooperation between the two countries. A striking example of bringing people together, to create a common market, aimed at the development of trade relations due to differences between the natural factor in the choice of economic direction is holding the silk road. “Silk Way” was held in 13-14 centuries and is a transport corridor between Europe, East and Asia [49].

Term economic integration was first proposed in the works of German and Swedish economists during the 1930s, and has been interpreted as the union of the different parts together. Economic integration is a form of internationalization of economic activity and is aimed at the relationship between the national economies and the implementation of a common economic policy. Economic integration - a process of rapprochement and interweaving the economies of several countries with similar socio-economic systems aimed at creating a single economic organism [50].

Thus, V. Baranowski meant by integration a “state of connectedness of individual differentiated parts into a whole, as well as the process leading to such a state” [51]. This definition, in essence, reflects the approach that is currently getting more popularity. For example, integration by T. Parsons includes components as the actual inter-compatibility of elements, preservation and maintenance of the specific conditions under which the integration system stands out from the external environment [52].

The initial need for analysis and theoretical understanding of the integration processes arose in the integration areas associated with the countries of Western Europe and North America. Overall, the regulations of the general theory of international economic integration created in Western Europe originally served as the methodological basis of the different concepts of interstate integration. In my opinion, it is logical that created concepts focused mainly on the condition of a highly industrialized society because at that period global practice did not have other examples. That is true, because the countries of the third world in the postwar era were still deeply divided and could not give a rise to the trend of integration.

The first attempts at theoretical understanding of the processes of regional integration were undertaken in the 1950s. by the scientists who worked in line with the neo-liberal direction (A. Predol, W. Roepke). Based on the concept of the market as the most effective regulator of the economy by integration, they saw the creation of a single geoeconomic space, which includes several countries. To achieve these goals, it was necessary to completely free foreign trade and monetary sphere of state control [53].

Followers of these views saw the integration problem mainly in the field of the integration of markets of integrable countries through liberalization of foreign trade. Thus, the efficiency of integration aspirations were reduced to the political will of states seeking to integrate their economies. To some extent, in this approach it is possible to see the origins of a particularly popular at the end of XX century concept of regionalism in international economic relations. But in the future they had to deal with a national trend of protectionism and lack of efficiency and development in the integration on a global scale.

World development trends objectively led a number of rapidly developing countries to seek an effective formula to protect national interests. The key element is the creation of conditions for the functioning of the single customs regime within the region and the development of common approaches in this regard in relation to third countries.

The concept of a customs union, in fact, has become a theoretical concept of the European Economic Community that emerged in 1957. Purely market attitude to integration that prevailed in that period in Europe was consistent with the approach to the “state as a night watchman”. This approach was extended to intra-regional relations and lead to either complete abstraction from political factors or their total disregard [54].

The subsequent course of events has made adjustments to the theory of regional integration. Establishment of free trade zones and customs union in Western Europe turned out to be not able to eliminate the uneven development and the general instability of the system. In the 1960s the reconsidering of approaches to forms of integration takes place.

The essence of the latter approach was reduced to targeted regulation of integration and significantly narrowed the scope of the neo-liberal interpretations of integration. In this regard, among scientists appeared a need to expand the definition of the integration framework.

The new direction was named “dirigiste” by several investigators. Proponents of this direction advocated the creation of a supranational political and legal institution or group of institutions to manage integration processes. In practice, this resulted in the creation of the concept of economic union. This approach has included the creation of coordinating bodies and mechanisms for a wide range of issues in the course of inter-state integration. The approach supposed corrective economic impact on the integration process. Several directions could be distinguished in the theory of economic integration. Table 2 provides a classification of these areas.

Table 2 - Classification of the theoretical directions of economic integration

Authors	Directions	Explanation
Wilhelm Roepke, Maurice Allais	Neoliberalism	
Sydney Rolf, Eugene Rostow	Corporationalism	
Gunnar Myrdal	Structuralism	
Richard Cooper	Neo-Keynesianism	The followers suggested two options for the development of international economic integration: The first is that integration with the subsequent loss of national sovereignity, but with alignment of economic goals and policies The second is that integration with the condition of preserving as much of national autonomy as possible. They believed in the necessity of combination of the two options by matching the inner and outer sides of the economic policy of integrating countries.
Jan Tinbergen	Dirigisme	The denial of the crucial role of the market mechanism in the integration process. Dirigists believe that the establishment and functioning of the international economic structures is possible through a common economic policy, harmonization of social legislation, and coordination of monetary policy.
N.P. Shmelev		Connects the origins of the integration processes with the needs of modern IDL, STP development, deepening international specialization and cooperation of economic structures of individual countries. Considers that the most important characteristics of integration are interstate regulation of economic processes, gradual formation of an integrational economic complex with common proportions and common reproduction structure, elimination of administrative and economic barriers to the free movement of goods, capital and labor within the region, and leveling of economic development integrating countries.
Y.V. Shishkov		Distinguishes «private integration» of production, national, commodity and credit markets. Believes that integration is based on market mechanisms
Source -compiled by the author according to literature sources [56]		

According to Table 2, the concepts of regional integration are formed within the well-known economic theories.

The first scientific school attempted to give a theoretical explanation of regional integration is the market school. The representatives of this trend include the consistent supporters of the basic principle of economic liberalism, Ludwig von Mises, W. Roepke, J. Rueff, etc.

According to the B. Roepke excessive government intervention, rejecting the market economy, the official pricing and limiting critical economic freedoms should lead to errors, bottlenecks, sub-optimal action and all kinds of imbalances [55]. Acceptance of the market as the best regulator of the economy, admitting the disconcerting role of government regulation of economic processes is carried by the representatives of this school to foreign trade. The main purpose of regional integration is the creation of a single market space for several countries, which shall have full freedom of competition and natural market forces for optimal regulation of the economic life of these countries.

However, this is possible only if any state intervention in the regulation of economic processes will be cancelled. That is why the main criterion for achieving integration in the view of this school is the freedom of market forces, which is determined by the level of regulatory impact from the government.

Support of regional integration leads to an understanding that the process of purposeful formation of inter-regional economic cooperation is linked. Therefore, we can assume that during the formation of inter-territorial relations the preference should be given to those forms of cross - border cooperation that are more conducive to the manifestation of market integration mechanism.

The next scientific school of regional economic integration is based on the principles of neo-liberalism, and it is a market-institutional school. Its representatives are M. Allais, B. Balassa, J. Weiler, G. Kremer, C. Meyer. They are trying to find a compromise between market mechanisms and state regulation of the economy. They are stressing the need for the market mechanism of integration, and also highlight the important role of the member states of the regional integration union - in the coordination of economic policies.

Structural integration school does not accept the liberal ideas that are the basis of the previous schools. Its representatives K.G. Myrdal, A. Marchal, F. Perroux, P. Wiles believed that the liberalization of the movement of goods and factors of production leads to the uneven economic development of regions within the integrated complex. The true integration is possible provided the structural transformation of the economies of interacting countries, contributing to the formation of a qualitatively new unified economic organism. So, according to K.G. Myrdal, the market mechanism leads to an increase rather than a decrease in inequality between regions, and the establishment of unified market by itself does not provide a more efficient allocation of resources. Therefore, in his concept the priority is given to the need of ensuring equal opportunity to all the participants of the integration process, and not to the freedom of competition. K.G. Myrdal's introduced the concept of “national integration” to the economic theory. It is associated with national political interests, which, in his opinion, have a significant impact on the allocation of resources in the world economy. A. Marchal and P. Wiles also believed that the only true integration is the one that gives equal supply of factors of production to all the components of the integrating space, which no market mechanism can give. Thus, the concepts of structural school representatives draw special attention to correcting the inequalities of integrating countries and their regions. Solving such problems is an active role for the state [57].

But the most important factor in ensuring the acceleration of economic integration, according to the structuralists, is the monopolistic capital, which has the largest mobility compared to other factors of production. In this regard, the F. Perroux's integration concept is of particular interest. He believes that at the heart of global economic management is a conscious, purposeful activity of "moving units" or "growth poles". These units, in his opinion, are the major firms, industrial complexes, whole sectors of the national economy. The interaction of active "growth poles" with the environment leads to the emergence of "poles of development", further economic interaction of which forms the "development zones" and "axis of development". They, in turn, are mutually attracted to form a "zone of integration", which is a complex mutually beneficial economic system that goes beyond national interests and covers entire regions. With the establishment and functioning of the "fields of integration", the most important tasks of economic policy are the formation of "growth poles" and the conscious control of the propagation area of their effects. Thus, representatives of the structural school of economic integration consider that the free market creates distortions that prevent unification of countries. Integration is the formation of optimally geographically, economically, and socially balanced economy, which is a kind of high-quality synergistic. Its main driving force is the private monopolistic capital, and the main task of the state is to eliminate the uneven development of the integrable part of the region [58].

In our opinion, the most important for understanding the integration interactions of national regions of the countries is the concept of F. Perroux. It complements the G. Kremer's idea of non-institutional forms of interaction is the interaction between actors of regions that refer to geographically close countries.In the 1970s, the idea of Neo-Keynesianism was widely spread. The representatives of this school were the American economist Richard Cooper and others. They believed that the central problem of international economic cooperation was the question of how to save multiple benefits of broad international economic cooperation from the limitations and at the same time to preserve the maximum freedom for each country. Neo-Keynesians have put forward two possible ways of development of international integration. The first states the integration with the subsequent loss of national freedom, and the second is the integration with maximum preservation of national autonomy. Assuming that none of these options can be presented in a pure form, they found it necessary to optimally combine them by matching domestic and foreign economic policy of integrating parties [59].

Another school of economic integration is dirigiste, which comes from the basic principle of Keynesian macroeconomic analysis of the priority concept of economic processes' direct state regulation. Its representatives are A. Philip, R. Cooper, J. Pinder, and others. They, as well as the structuralists, consider integration as a process of formation of the best international economic structure. From their point of view, the main problem of regional integration is to find a compromise between the interests of the national and integrating regional economy. Such a problem can be solved with the state's active use of institutional and legal instruments of economic regulation [60].

Thus, R. Cooper notes that the most important in the conditions of internationalization of economic life is the "increasing sensitivity of economic events in one country to what is happening in its trading partners". However, he emphasizes the prevalence of the institutional aspect of the various national interests in the common space. J. Pinder brings integration to the coordination of various measures of economic and social policy of the participating countries of the integration complex. He divides the measures of "negative" integration proposed by the representatives of market-institutional school, and "positive" integration, noting the priority of the latter [61]. According to J. Pinder, "negative and positive integration together form the economic integration, the aim of which is the economic union" [62].

Thus, the representatives of the school believe that the ultimate goal of regional economic integration is the formation of an optimal economic structure of the region, supported by the appropriate economic policy.

Significant role in the development of the theory of economic integration was done by N.P. Shmelev. He connects the origins of world integration processes to the needs of contemporary international division of labor, the development of scientific and technological progress, deepening international specialization and cooperation in the economic structures of individual countries. He considers the interstate regulation of economic processes, with the elimination of administrative and economic barriers, the leveling of economic development [63].

AY. Shishkov identifies "private integration" of production, national, commodity and credit markets in the interstate integration process. According to him, manufacturing and in the larger manner - credit and financial sphere are less amenable to the integration in the reproductive cycle. Y. Shishkov fairly believes that the integration is based on the action of market mechanisms that regulate economic relations [64].

Currently, due to the enlargement of the EU by the accession of new countries has developed a number of models for further development of European integration by way of its deepening. The basis of the first two models is the idea of the creation of the EU "core" of the most developed countries, around which the "periphery" less developed countries.

Model of "differentiated integration" comes from the fact that the geographical expansion of the EU should change the concept of integration. As well as "step integration", "differentiated integration" aims to deepen the integration process, but it eliminates the need to sign a contract and the time limit. It is also planned to create a "core" with the different composition of the participants [65].

Further resolution of the conceptual issues that justify the mechanism of integration processes is related to the institutional school. Institutionalism, based on the methods of social and political science, is of undeniable interest to the organization of integration relations management both within the regional associations and over their boundaries. The main scientific schools, formed as part of this direction, developed Western European scientists and are the theoretical basis for European Integration Studies.

Thus, representatives of the various schools of integration differently consider the mechanism of interaction of national economic systems; determine its drivers and criteria for integration of national economies. However, theories of economic integration argue about minimum intervention in the initial period to the active participation and influence in the later stages. Therefore, at the initial stage of the economic integration the focus was on the economic activity of the micro-level and later - on the various tools of government regulation. We believe that the certain provisions of the economic integration development allow us to determine the conditions necessary for the formation of the integration processes at all levels, including those involving the countries' border regions.

Thus, the process of economic and political unification of countries on the basis of development of deep, sustainable relationships, the interaction of economies at different levels and forms is called economic integration. At the micro level, this process proceeds through the interaction of neighboring countries' individual firms on the basis of the formation of various economic relations between them, including the establishment of subsidiaries abroad. At the intergovernmental level, the integration is based on the formation of economic unions and the harmonization of national policies.

Integration processes lead to the development of economic regionalism, in result of which groups of countries create among each other favorable conditions for trade and, in some cases, for inter-regional movement of production factors. Therefore, an integration union is an economic group formed to regulate the integration process between its member countries.

The global competitive environment is a space in which survive the strongest and also those countries that bring together their joint efforts to resist challenges of globalization. Here, in our opinion, lies the nature of economic integration. Regional economic integration is a factor that encourages the development of globalization. It creates the conditions for the free circulation of goods, services, capital and labor, which leads to increased interconnection and interdependence of economies, to the creation of a single world market. Regional integration provides its members preferential economic, commercial, political conditions that blur certain universal things, for example, the trade conditions set by the WTO.

Thus, the term "integration" has entered the world of science to describe quite certain, specific process in international relations. In our view, economic integration is an objective process of development of strong economic ties between the national economies that cover the sphere of production and lead to the creation of regional economic complexes. From a scientific position, integration is a contractual association of sovereign states that join their resources to improve the effectiveness of the national economy and overcome some of the difficulties and contradictions of economic globalization. Fundamentally important component of such a definition should be “unification”, “sovereignty”, “efficiency” and “contradictions”.

The presence of two - multilateral trade relations is transformed into the global integration. Create industry factors changed relations between countries on natural resources to human capital. Further development of the industry has increased the volume of production, expanded forms of intra-industry specialization and helped to create the world's productive forces, reinforcing processes international division of labor. At this stage, the distribution industry MRI happened according to the level of production costs and the existence of absolute and comparative advantages in the basic factors of production. Period of 20 - beginning of the 21st century was characterized by increased competition, both for companies and for countries that determines the need for cooperation as material, financial, and production efforts for neighboring states. The formation of such regional entities can improve and maintain a level of competitiveness in the global market in the context of globalization. We can state that form to achieve the goals of economic integration is. Term economic integration was first proposed in the works of German and Swedish economists during the 1930s, and has been interpreted as the union of the different parts together. Economic integration is a form of internationalization of economic activity and is aimed at the relationship between the national economies and the implementation of a common economic policy. Economic integration - a process of rapprochement and interweaving the economies of several countries with similar socio-economic systems, aimed at creating a single economic organism [66].

Integration processes actively began to develop during the last century. The reason was replacement of import. Among the characteristics of the integration can be identified:

- the lack of restrictions on the movement of factors of production;
- a single economic policy;
- the interdependence between members of national productions integration Union;
- the development of cooperation and specialization by progressive forms, co-financing of innovative projects;
- the establishment of common rules and standards;
- the creation of common institutions of governance of economic cooperation;
- the development of integration mainly in the regional aspect. Economic integration can be represented in the form of interaction at the level of production that will include all major international processes - trade liberalization, cooperation and specialization.

In accordance with these processes it is necessary to note some types of integration according to the spheres of influence:

- superficial integration characteristic of trade relations;
- deep integration, in which the interaction is affected by manufacture;

- management integration includes scope to manage and control both the level and national enterprises, and government regulation. It is easy to start integration through expanding the trade, a little bit harder to organize mutual production and the most difficult make financial and monetary cooperation. Factors determining the integration process are distributed in three main areas such as a global, zonal, regional relationship [67]. Each of these different levels of specialization is in the spheres of influence of integration factors. Thus, the creation of a global level is the expansion of relations of the world economy as a whole. The presence of historical background determines the relationship of political and economic factors, which is typical for the zonal level, which highlights regions that represent the third level.

The process of integration at the global level has a natural result of the internationalization of production and reflects the expansion of world economic relations in their national economies toward a single world market. Contradictory nature of integration is most pronounced at the level of the relationship these zones, which are possible in the processes of association and the sharp division into small groups.

According to Russian authors M. Maximova, I. Faminskii, M. Osmova, V. Zotov factors are based on the internationalization the joint control of supranational institutional structures [68, 69]. The highest level of cooperation in the world economy is the integration in three main areas - capital, production and labor. Definition of economic integration based on mutual understanding between the countries of economic, institutional, industrial relations in accordance with the national interests and mutual economic benefits. Integration is one of the ways of general terms and conditions of mutual economic cooperation with the outside world, to enable all participating countries further comparative advantages and the ability to lower costs to achieve rapid economic growth .

R. Dalimov understood integration as a process, based on the inherent potential of any interaction between the integrated system, which due to its synthesis acquire “new quality” [70].

A prerequisite for the development of mutually beneficial cooperation between the two countries is the international division of labor. Definition of economic efficiency relationship based on specialization and combination of factors of production based on the competitive advantages of each country. This results in the formation of global competitive area, which includes international trade, international specialization, cooperation, scientific and technical cooperation, the development of innovative strategies, joint ventures and financial institutions. Expansion trends of market relations in terms of a single economic space determine the transformation of the economies of developed countries, mainly in a single integrated system. It may be noted that the processes of market relations contribute to creating an environment for the formation of a synthetic model of development. Economic integration process consists of several stages, so that the English scientist B. Balasa identified five phases based on organizational and economic ties [71]. The first phase involves the creation of a free trade zone, which eliminated tariffs and restrictions in the trade exchange between the two countries. In the second phase, a customs union formed.

The third stage is characterized by the activity of a common market based on the free movement of factors of production. Creation of an economic union in conjunction with trade liberalization takes place on the fourth stage. The fifth phase of the highest degree of economic integration based on the unification of monetary, social and fiscal policies.

In recent decades, modern economic literature has changed the approach to the definition of inter-regional integration. According to the market-based approach, the integration process is mainly to remove obstacles that hinder the integration of national markets for goods, services, capital and labor. Thus, the elimination of customs tariffs, the creation of the European single market, free movement of capital and the European Monetary Union presented the successive stages in the process. According to the model zones "free trade", the primary role of the emerging European institutions was to ensure fair competition and price stability through macroeconomic coordination. Institutional approach defines the process of inter-regional integration, in particular, European, as the gradual transfer of legislative and administrative powers from national to supranational authorities. This model, which is often characterized by an integration strategy proposed by the European Commission, involves the redistribution of financial resources as a major tool to reduce regional disparities. Division members - participants on the "macro-regions", which corresponds to the high level of competitiveness both within the Union, both individually and in foreign markets is typical for the third approach. In which the boundary regions are separated and create artificial barriers of economic and social integration, based on the process of internationalization. Creating macro-regions based on the study of barriers to the development of bilateral and multilateral relations and examines the effectiveness of cooperation. This approach is typical for modern high-tech production period when their organizational structure is constructed under the project and become significant resource information. These approaches can not be considered as an evolution of views on the problem of interregional interactions as though they are not entirely opposed to each other, but differ significantly in the background and practical conclusions. Methodological bases of the first approach, based on the principles neoliberal theory that considers the impact of any state interference with the "natural" market process and distorting market information for economic actors. In this case addresses the international and inter-regional boundaries, where the primary production model was the mass production of standardized products, limited demand and opportunities to engage the major resources - capital and labor. The next stage is based on the inevitability and the fundamental need for an active role of government regulation in the market conditions and consistent with the policy development and implementation of national strategies. Common core of the different approaches is the definition of the integration process from the perspective of the development of relations between the regions, uniting them together. Development of integration processes is the most important characteristic of the modern world economy. Creating integration unions comes in different forms and levels, which is characterized by positive and negative effects on the economies of the member states. Country every continent involved in this integration process, some countries simultaneously participate in several integration unions that is made possible by a wide variety of types and stages of integration.

By geopolitical, economic, historical and cultural circumstances of integration for each of the countries is a priority. Foundation of world economic integration processes constitute factors characterizing the interaction of national economies at the micro - macro and international levels. In turn, the integration process includes the essential components:

- economic development;
- political issues;
- financial support;
- cultural and social police;
- scientific - educational system;
- production;
- security.

World experience of modern integration blocks shows that one of the requirements for creating them are political interests, coordination of strategic interests of the member states. Mechanism for economic development is a tariff regulation, the creation of a free trade area and customs union. Movement of labor determines the financial flows, as well as capital market, improvement of the investment environment. Consolidation of efforts of the member states aims to address common global challenges, which include the environment, territorial security and the impact of global economic fluctuations.

In the current conditions, prerequisites for the creation of integration are a political dimension, and the driving factor in the further development of economic benefits can be noted regardless of the level of integration. Examples of economic cooperation between the two countries based on the international division of labor, with the transition to the international socialization of production, the result is the formation and functioning of the integration phase. This approach was used in creating the European Economic Community of West European countries in order to improve the efficiency of the national production. Integration tools in this case were the reduction of customs duties, conditions of free movement of capital and labor [72]. Depending on the content of the integration processes are divided into levels - subnational, regional and global. Each level is characterized by the features of the economic interdependence of countries.

Degree of integration of components for each stage is different, characterized by regional and interstate associations characterized by the liberalization of the factors of production. A distinctive feature of the global integration process is to allocate transnational productive capital. Integration at the global level is represented by the participation in the WTO and the commitment to its principles - openness, non-discrimination in trade and economic relations. Current state characterized by the dominance of financial integration on economic functions, which is particularly likely when capital flows and investment.

All components are integrated economic goals, which affect the level of GDP in two ways:

- the movement of factors of production is directed to more developed countries integration bloc - labor migration, increased production, by attracting investments, development of scientific and educational spheres;
- the expansion of trade relations.

Activity of modern integration unions can be characterized by moving them to the main groups: dominance, interdependence and cooperation. The first group is characterized by the spontaneous formation of alliances, by the creation of such alliances on a global scale. And a certain one-sided benefit, lack of the legislative framework, control of compliance with agreements on the part of the country is more interested in the interaction.

Determining a second group based on the states of integration:

- the interdependence of countries - participants;
- to develop mutually beneficial terms of cooperation;
- establishment of joint bodies of control and regulation;
- long-term cooperation agreement;
- protection of national interests.

For the relationship of the third group is characterized by the integration with the following conditions:

- the prevalence of integration advantages over negative consequences;
- mobilizing efforts to solve common problems;
- the establishment of joint coordinating supranational bodies;
- the presence of a single joint strategy of integration development.

Complex interaction of integration trends in the context of globalization is based on theoretical approach to explain the relationship with countries. The modern theory of international economic integration based on the classical theory that the basis for the creation and development of specialization is based on the competitive advantages of the country. In this case, some sectors of the national economy with an opportunity for further growth, while others are shrinking.

According to one of the concepts of the theory of integration market is the principal instrument of governing the economy. In turn, state activity is considered as a source of disruption balance business environment. The impact of the state according to the followers of this concept applies not only in the domestic market but also in international politics. In their study, G. Kassel, considering protectionist policy as one of the measures of disintegration [73]. Members of this concept consider integration as complete freedom of competition and domination of the market laws, which creates equal conditions for the movement of goods, services, and capital, both internal and external economic environment. These conditions are possible in a competitive environment in which government policy creates barriers and does not conform to the rules of the market. Forms of government intervention may be export-import trade policy. In this regard, the accelerated pace of integration processes peculiar countries with the lowest proportion of protectionism. Among the signs of the integration of researchers emphasizes monetary and financial system, as applicable price levels, calculations, currency convertibility. Regulatory mechanism occurs by market forces, as well as the idea of integration is often born by the government's decision at the state level. The opposite point of view is aspects of neoliberal currents, which are outstanding representatives of J. Weiler, B. Balass, and M. Allais. Teachings of this area consist of ideas balance between market and state intervention. State regulation is a complement functioning integration unions. In order to ensure their effectiveness integration can be defined as the functioning of the common market, without discrimination or restriction of trade regulation, to meet the needs of the population. In turn K. Meyer defines integration as a way of transforming national economies into a common market, and international relations at the national [74]. According to G. Kremer international dimension of economic integration achieved in the absence of differences of nationality and when vital interests of the integration block exceed national priorities [75]. Russian researcher N. Naumova, integration analyzed as a conflict- compromise combination of processes beginning in the economic sphere and then in other areas of public life. She develops unique mechanism for making and implementing decisions, flexibly combining the principles of international cooperation [76]. She understands that the "discrimination" in the international movement of goods, labor and capital is created not only by tariffs and quantitative restrictions on imports, but also fiscal, monetary and other areas. Structuralism based on the study of integration as a way to improve social policy - improving living and working conditions, reducing poverty, achieving universal benefits. Integration processes in the different areas, because they is driven by the objective of a market economy. These processes involve a variety of aspects of the economic and political life of the integrating countries. Although the internationalization of economic life reached a global scale, now the integration processes are mainly regional. Internationalization facilitated by the requirements at the present stage of scientific and technological revolution. One of these features that deepen the internationalization of economic life. In view of this, there are, for example, individual differences in the integration of individual regions in the interaction region and the definition of the institutional arrangements. Development of integration between countries to take advantage of the single market, to ensure favorable external conditions for the development of the national economy. Through the integration, countries can attract additional resources, reduce production costs, which contributes to the effective implementation of their activities. Different levels of economic development of the integration increase productivity by introducing backward sectors and regions of the conditions that contributed to the raising of the economy in the leading industries. As for the integration processes between companies, they are carried out in different forms.

Horizontal integration involves a consortium of companies specializing in the production of the same product or operating in the same industries. Vertical integration involves pooling companies from related industries, while diversification is an association of companies “operating in different markets and technologically unrelated”. According to G. Kremer 's point of view integration should be allocated as following:

- integration, created without government assistance (inter-company agreements, the establishment of international business alliances, participation in the capital of companies in other states);

- integration, organized through unilateral state action, for example by reducing individual countries customs duties on their reasons;

- cooperative integration (international conferences, bilateral and multilateral interstate agreements or by a mere agreement between the countries concerned);

- Institutional integration [77].

With all the variety of types and kinds of integration can identify the main directions of development of software and integration, in accordance with the principles of the organization. The organization highlighted us as a parameter combining a background of the shape of the governing body and prospects. These areas are:

- a model of a typical center, at which the main integrating force acts supranational control that is not tied to territorial placement. An example is the Empire, unitary and federal states;

- a type of intergovernmental agreements requires the existence of numerous centers of power related to specific areas;

- the dominant party model in which one country is a "locomotive" and ahead of other members in terms of economic growth;

- a model of corporate investment, involves the activities of large corporate companies;

- a model of informal trade;

- a model of state law.

Despite the existing flow, the core of integration is to improve member countries, increasing competition and achieving social development. Under economic integration is considered a feature of the present stage of development of the world economy and at the same time aimed at achieving macroeconomic indicators not only one country but the entire region. Controversial issue is the achievement of regional goals to the detriment of individual countries. The solution to this problem lies in the essence of the phenomenon of economic integration, but the practical side is international experience and can be borrowed countries. This process of accretion of the economies of neighboring countries into a single economic complex is on the basis of strong economic ties between national actors. Level of integration can be determined by the following three criteria:

- the number of interested and involved in the areas of integration;

- the presence of supranational institutions;

- the number of members of the participating countries.

International economic integration is a feature of the modern type of the global economy, aimed at accelerating the development of regional economies and improve the international competitiveness of countries - members of the integration groupings. The notion of integration is not identical to the definition of the process of globalization, due to varying degrees of control allocation of factors of production. Thus, the integration basis is a recognized need of broad and comprehensive development of trade and economic cooperation, and cooperation in the future is - creating a self-sufficient and secures the overall market. By pushing the need for the support of domestic producers and creating equal conditions for business activities on a single economic space.

Summary for the first chapter

The choice of the optimal strategy is a crucial task for any private firm, and the future survival of it largely depends on how well the managerial team does their job in relation to that task. The choice of the firm's strategy is a global and multidimensional process that implies dealing with many aspects of firms activities, as well as taking into account many external factors. In this chapter, we studied the problem of the optimal strategy choice when the economy is undergoing integration process.

An analysis of the scientific literature reveals the complexity of the concept of "strategy" and there are certain discrepancies in its interpretation among the authors. Mostly they are not fundamental. Differences in the interpretation of the concept "strategy" are often caused by the author's desire to focus on isolated development trends in the internal and external environment. Numerous add-ons do not distort the philosophical basis of the strategy concept, but rather fill it with new content.

Realizing the vast variety of definitions for strategy, scientists and experts made many attempts in systematizing the content of various interpretations. As an interim step, they made the attempt to clarify the definition of the stages of evolution of strategic management theory. In this context, the main task of company's management becomes maintaining equilibrium at the internal and external environment, as well as the development and use of effective mechanisms to adapt the organization to the future challenges.

If the external environment of business is relatively stable, its organizational structure is committed to a greater centralization of control, creating a rigid structure of management-oriented management control over the entire process chain.

When the external environment of a business is unstable and there are constant changes, concealing dangers and new opportunities for the organization, the management is forced to be more concerned with the problem of survival of the organization. Then the management system is adjusted for greater flexibility. Organizational structures become more decentralized, and that feature allows it to react promptly to change.

One of the important external factors that call for strategic response is economic integration. Economic integration initiates a global restructuring of involved economies, and, no doubt, is a major factor for the business landscape of almost any firm. This factor is especially important for the firms that cling to a cross-border expansion strategy, or for the firms that operate in the industries affected by the expansion of foreign firms.

Economic integration is solely controlled by international trade barriers, such as customs tariffs, quality standards, difference in law system, and so on. By relieving or setting up trade barriers the government moderates economic integration process. Trade barriers are an important positive factor for domestic firms that have limited possibilities to compete with foreign firms, or for the firms that open international subsidiaries. For the exporting or importing firms, trade barriers are a strong negative factor.

Economic integration process involves revisiting the trade barriers: for the integrating economies, such barriers are removed, and for the other countries, trade barriers can be reinforced. Updating of trade barriers and the consequent restructuring of the affected economies is a major uncertainty factor for the affected enterprises.

Nowadays in the epoch of globalization, economic integration processes seem inevitable. Kazakhstan economy is not immune to the integration process as well. We can point out two centers of gravitation in the framework of integration economies: western economies that contribute into a competitive environment, and post soviet countries (mainly Russian Federation) that benefit from previously established technological and logistical connections. Due to the special character of this situation, the direct use of the international integration experience by Kazakhstan companies is not possible. The main factor at fault here is the lack of competition in the market, and business schemes that are not in accordance with the world standards.

The particular case of strategy that worth special attention in relation to economic integration is the expansion strategy. Economic integration, and particularly, the change in trade policy, leads to an expansion of the market, increased competition, and investment flows. These factors motivate firms for the development of strategies adequate for the new external challenges, and the opportunities for companies to expand activities.

2 ANALYSIS OF INTERNATIONAL ECONOMIC INTEGRATION: HISTORICAL AND PRACTICAL LESSONS

2.1 Analysis of world experience of economic integration

International economic integration is a feature of the modern type of the global economy development, aimed at accelerating the development of the regional economy and increasing the global competitiveness of member countries of the integration groupings.

In the international practice history, the experience of forming integration unions is often positive, but not all integration groups can cope with the problems of assessing the potential economic impact. In recent decades, the process of creating integration groups takes over countries on every continent and the positive example for all is the experience of the European Union. In 1970s, the process of integration in Europe has spurred the growth in the number of integration associations in all parts of the world. In 1980s, there were about 10 of integration associations of various types created, in 1990s - about 30.

Integrated associations formed in the time period from the year 1990 to the year 2000 differ significantly from the agreements of 1960-1980's. The differences lie in the coverage of integration measures, in the model of the external economic development, in the participation of the countries according to the level of economic development, as well as in geographical factors. Since the second half of the 1990s grows the number of inter-regional agreements on free trade areas, including the involvement of countries from different continents, as well as grow the intentions of creating a region-wide free trade zone [78].

Nevertheless, all integration associations, despite their differences, pursue similar strategic objectives: using the advantages based on the “economy of scale” theory (duplication elimination, reduction of transaction costs, etc.), creating favorable external political environment, expanding mutual trade, promoting economic restructuring, and supporting local producers.

The expanding number of regional integration unions, the diversity of their forms is justified by the increasing economic differentiation in the world and also by realizing the need of strengthening the national and state positions in the global competitive space. Integration groups in the international economy, especially in developing countries, periodically appear and disappear.

The most prevalent regional economic integration, according to many scientists, in the future will become the initial phase of global integration, which will lead to the merging of the regional unions.

In today's global economy, there are four integration development “zones” that are most pronounced. The major integration unions are established and operate in these areas:

- Europe;
- North America;
- the Asian-Pacific region;
- Africa and South America.

- In the 90s there was the establishment of organizations such as the North American Free Trade Agreement (NAFTA), the Common Market of South America (MERCOSUR) and the Free Trade Area of the Association of Southeast Asian Nations (AFTA - ASEAN Free Trade Area)

2.1.1 Structure and stages of economic integration

To be more precise, integrated unions exist in several forms or types. Figure 5 shows the forms of integration. The way how these forms are distinguished depends on the depth of the processes occurring in the integrating countries. To this moment, according to Picture 1 there are five main forms of regional integration, as follows:

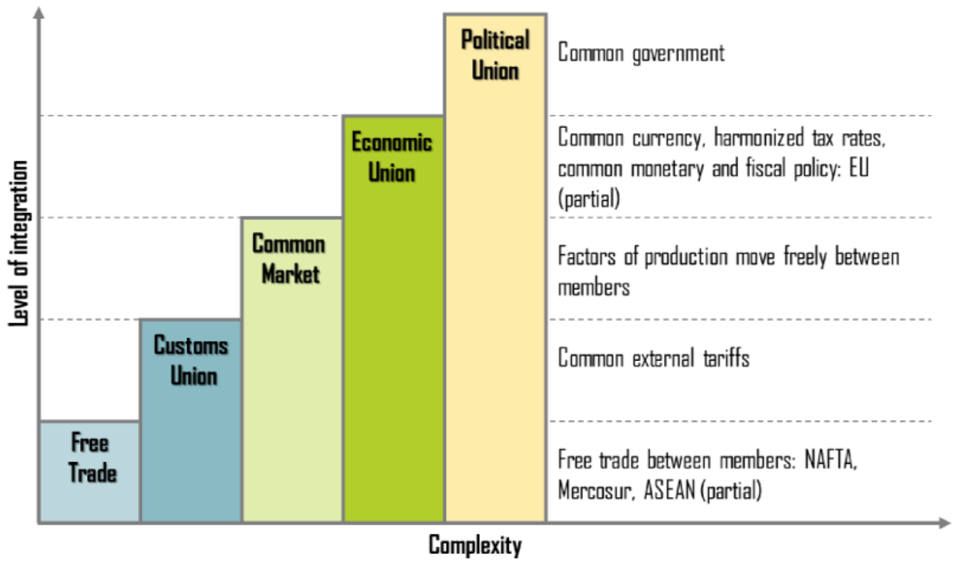


Figure 5 - Forms of regional economic integration

Note - Adapted from the literature source [79]

1.Preferential Trade Agreement.

At the first level, when the countries have yet to make the first steps to a mutual convergence they establish PTAs between themselves. Its essence is that the participating countries provide each other with mutual trade benefits. This form, as a transitional stage, existed in many integration groupings. Such agreements may be signed either on a bilateral basis between states, or between existing integration group and individual countries or groups of countries. In line with these agreements countries provide more favorable treatment to each other than they provide to third countries. [79, p. 134]

In a sense, this is a departure from the principle of most favored nation treatment, which is sanctioned by the GATT / WTO in the framework of the so-called temporary agreements that lead to the formation of a customs union. Preferential agreements, that provide preservation of national tariffs of each of the signatory countries, should not even be considered as a start, but as a preparatory stage of the integration process, which becomes such only when it takes the more advanced forms. No interstate agencies are created to control preferential agreements.

2.Free Trade Area.

A free trade area means that the barriers and quotas to mutual trade are removed. This is the preferred option for countries embarking on economic integration and for those unwilling or unable to engage in higher levels of integration. An FTA can be limited to particular sectors, thus retaining a high level of control at the national level and preventing exposure to competition for the other sectors. The authority to decide how third countries are to be treated remains unaffected (independent trade policy) in an FTA. However, rules of origin have to be agreed upon among members so as to determine which products can be transferred duty-free.

For each member country retains the right to self-determination and an independent trade regime with respect to third countries. In most cases, the conditions of a free trade apply to all products other than agricultural products. Free trade area can be coordinated by interstate small secretariat, located in one of the member countries, but usually countries do without it. The main parameters of development are usually discussed on the periodical meetings of the heads of appropriate departments. Customs and border posts among the member countries remain to control the origin of goods that cross their borders. [79, p.135]

3.Customs Union.

When two or more countries agree to remove (essentially) all restrictions on mutual trade and set up a common system of tariffs and import quotas vis-à-vis non-members, the result is referred to as a CU. The adoption of CET and joint quotas necessitates closer co-operation with respect to the sharing of customs revenues collected on non-member imports. Rules of origin are no longer necessary: when a common external tariff exists, imports into the CU–area face the same tariff in each CU-member country, hence there is no incentive for trans-shipment of imports between members. The CET effectively creates «destination-neutrality» for imports into the CU.

The agreement on the establishment of the Customs Union stipulates the following:

- removal of internal customs borders between member states;
- transfer of customs control at the outer perimeter of the union;
- elimination of customs procedures in mutual trade in goods of national production;
- standardization of forms and methods of collecting foreign trade statistics;
- approval of forms and methods of providing benefits to participants of foreign economic activity;
- introduction of a common to all member states of the Customs Union tariff and non-tariff regulation for trade with third countries;
- creation of a generalized system of preferences.

Both FTAs and CUs imply that the member countries remain nation states, yet when viewed in the historical context there are some subtle differences between the agreements.

The German Zollverein and the European Community for Coal and Steel are examples of successful CUs. The Zollverein preceded the formation of Germany in 1870 and thus holds fewer lessons for today. The European Community for Coal and Steel, a sectoral CU created in 1951, was not expected to be a precursor to eventual European political union. Nevertheless, it was recognized at the time that free trade and the consequent rationalization and specialization of production in coal and steel products would require a supranational body to regulate pricing practices and commercial policies. This historical precedent therefore suggests that a successful CU implies a common competition policy. Subsequently the European Common Market naturally adopted and extended this competition policy. [79, p.136]

4. Common Market.

A common market can be considered the first stage of deep economic integration. Free mobility of the key participants in the process of production is its characteristic. In addition to goods and services, capital and people move freely inside a common market. The benefits expected consist of further gains in efficiency through a more appropriate allocation of resources: capital moves to where skills are and people move to where opportunities beckon.

In addition to the common external tariff that defines a CU and to ensure the viability of a CM, uniform regulations have to be worked out among the members regarding the movement of people and capital. This is a major task that requires, at least over time, agreement on qualifications and certifications of workers from different member countries. [79, p.136]

For a CM to become effective, therefore, co-operation in decision-making is required in yet more areas. Non-tariff barriers have to be dismantled, structural adjustment policies have to be jointly reassessed, distribution policies will face harmonization pressures, and fiscal and monetary policies, as a dynamic consequence or by design, will show greater convergence. This convergence results from the increased economic interdependence among the members and necessitates that greater consideration be given to the effects of national policies on the welfare of CM partners.

5. Economic Union.

The next step in deep economic integration, economic union, adds to the common market harmonized fiscal, monetary and labor market policies. Tax and monetary policies affect where a business locates, and because labor market policies affect migration patterns and production costs, these will have to be streamlined among members. There will be no room for different national transportation, regional or industrial policies, as these distort competition among firms from different member countries.

To achieve such a union, it is necessary to form supranational institutions that legislate the rules of commerce for the entire area, leaving the administration to national bodies, but with recourse to supranational administrative tribunals to ensure uniform application of these rules. In an economic union supranational commercial law replaces national law.

For example, the European Union's regional adjustment policy provides infrastructure funds to regions within the EU that have 75% or less of the average EU-income level, with a budget of 0.45% of the EU's GDP. This illustrates the degree of co-operation necessitated by an economic union.

An economic union is made more effective, furthermore, by a common currency. When there is no uncertainty about exchange rates among members, location decisions and trade patterns will follow efficiency considerations, and borrowing costs will not be affected by an exchange risk premium on a particular member country's currency.

At this level of integration pressures for uniform taxation policies will increase even if agreement on such may prove elusive as shown in the case of Europe. The final outcome of economic union may well be a political confederation with unified economic policies. Economic union will stop short of political union if no supra-national bodies regarding defense and foreign policy are created.

There is also another form of integration which to this moment does not actually exist in the world, but can appear in the future. This is political union as a last and deepest form of integration. Political integration involves the strengthening of a political system, in particular the scope and capacity of its decision-making process. Besides this institutional aspect of integration, there is as well the normative dimension of creating a political community. Legal integration is closely related to political integration and involves the establishment of common legal rules and a common legal system for the citizens of the different states of a region. Sometimes political integration is interpreted as the creation of supranational institutions. However, as already indicated, supranational institutions cannot be considered as the condition par excellence to achieve an increased coherence. Treaties might well stipulate a certain degree of sovereignty transfer; however, the actual practice might sometimes diverge considerably from the stipulations of the treaty.

The success of the integration process can happen due to the presence of prerequisites that are necessary for this. Scientists have proposed classification of the motives of regional union formation, consisting of three types, namely:

- first - the common interest of states in such a form of cooperation that occurs due to geographical proximity and the presence of common economic, social and cultural interests;
- second - ideological considerations that stimulate ideas of constitutional union;
- third - the motive of rational choice in which the parties welcome the economic aspects of integration and on the basis of analyzing income and expenses from membership in such unions boost regional integration.

The motives cannot be limited to these three, as the conditions of effectiveness of regional unions may be diverse. Therefore, there are different approaches that exist in the economic theory to identify the prerequisites of integration unions, such as:

1. The proximity of the levels of economic development and degree of maturity of the integrating countries' market economy - is desirable, but not mandatory, as the experience of integration development shows that there often exists a partnership between developed or developing countries. Even in the industrialized and

developing countries the integration processes are most active between the states at about the same level of economic development. It takes a long time in order for a country that has much lower economic performance than another country to become able to participate equally in the integration process. Thus, economically stronger partners have to divert resources to these countries to pull-up their weak economies, rather than to invest resources into the development of integration processes. In this case, because of the initial incompatibility of economic mechanisms, the integration of these countries begins with a variety of transient agreements about the union, about special partnership and trade preferences. Their duration may take some time until the less developed country will create market mechanisms with maturity comparable to the mechanisms of the more developed countries.

Attempts to create unions between developed and developing countries, although happen sometime, but are only at the stage of formation, which does not allow drawing unambiguous conclusions about their effectiveness. So, as an example, the situation in the European Union, when Greece and Italy in the first phase of integration could not become members of the Euro Zone due to discrepancies with Maastricht criteria. NAFTA is also experiencing difficulties due to the different economic situation of the US and Mexico.

2. Common economic and other problems faced by the countries in areas of the development, financing, regulation, economics, political cooperation - involves the solution of specific problems faced by the integrating countries. So, the reform of the centrally planned economy has shown that all the countries of post-socialist space, having exhausted intensive methods to improve the efficiency of the national economy, had the same problems. In particular:

- all countries have experienced strong demand in all kinds of resources (investment, production, technology, innovation, intellectual, etc.) available to the global economy;
- territorial commonality conditioned the same type of complications related to the resolution of global problems, including ecological ones. All this has led to the need of combining resources for a joint solution to these problems.

Therefore, the integration is developing more successfully when the economy of the countries is booming. Countries in the stage of economic crisis integrate with each other with more difficulty, because they have to give preference to the internal situation in the country, to conduct anti-crisis measures, laws, restrictions on the export of capital, etc. (for integration characterizing feature is the freedom of movement of labor, capital, goods and services). To date, there are no stable integration unions that have appeared between the countries that are in crisis.

3. The geographical proximity of the participating countries, often the presence of the common border and the historical economic ties. Integration unions of most countries of the world began with a number of neighboring countries on the same continent, in close geographic proximity to each other, with transport links and often the same language. Indeed, for the main goals of integration, such as lower production costs and the final price for the goods it is necessary to reduce the price of all the components, including shipping costs.

Integration processes in the South America have shown that, despite the geographical proximity, the integration between the current MERCOSUR member countries did not develop until a certain time because of the lack of transport infrastructure (South America countries focused on the export of goods from the ports).

4. Political will of the integrating countries governments is essential to the creation of integration unions. Therefore, the creation of such large integration blocs like the European Union, MERCOSUR and NAFTA were the result of government initiatives of the countries concerned.

5. Creating structures to which countries should gradually transfer, delegate certain powers; tools to implement them. This should concern, for example, credentials for determining the strategy, for the creation of supranational institutions and for the development of cooperation mechanisms to harmonize national approaches to develop mutually acceptable solutions. [80]

6. Initiating the creation of the center of one or two states to combine activities of the partner countries. In connection with the (European Union) EU expansion through the accession of new countries there has been developed models for further development of European integration by its deepening. These models are:

- the model of «stepwise integration»;
- the model of a «Europe of concentric circles»;
- the model of «differentiated integration». [80, p.138]

The basis of the first two models is the idea of creation of a «center« of the most developed countries in the EU, around which will be formed the «circles« out of countries with less integration depth.

The basis of the model of «differentiated integration» is the geographical expansion of the EU that suggests the differentiation of the integration pace in different countries. The purpose of such integration is to deepen the integration process with the exception of the need to sign contracts and time constraints, as well as to create a «center» with different composition of participants.

7. Convergence of internal economic conditions in the member states of integration unions and alignment of their economic development. The purpose of entry for many integrating countries is the creation of favorable conditions for reaching high rates of economic growth over time and overcoming the negative external effects.

8. Spatial expansion opportunities for the interstate movement of goods, labor and capital within the region and the elimination of multiple administrative and economic barriers.

9. The «demonstration effect» suggests that the countries that have established integration unions usually have positive economic changes (faster economic growth, lower inflation, increasing employment, etc.) This has a psychological impact on other countries. [80, p.115]

10. After most of the countries in a region have become members of integration union, other countries that have been left out start to experience some difficulties associated with the reorientation of economic relations of these countries. That often

leads to some reduction in the trade of the countries who found themselves outside of the union. As a consequence, the «demonstration effect» leads to a «domino effect» when other countries, that have no interest in integration but are afraid of the negative aspects, start to express interest in the integration processes [81].

The accumulated experience of the integration processes in the world economy demonstrates that sometimes these conditions are not exactly fulfilled. This fact only gives a new impulse to further study of the integration processes which do not stop changing in the conditions of unsteady world economy.

2.1.2 Analysis of impact of economic integration on the companies. Cases of NAFTA

The first integration agreement of North America was CUSFTA (Canada-USA Free Trade Agreement), which entered into force on January 1, 1989.

The main purpose of forming CUSFTA was to achieve a free trade area by eliminating duties on mutual trade for 10 years, and by reducing discrimination against mutual direct investment, including the expansion of rights for the registration of companies and the application of national regime. Exceptions have been made in the field of telecommunications for the two countries and for the admission of US investment in Canada's cultural sphere [82].

On the basis of CUSFTA the North American Agreement on free trade was signed between the US, Canada and Mexico, abbreviated as NAFTA.

The premises for creating NAFTA were the following:

1. The United States, Canada and Mexico are united by the presence of geographical borders, historical economic ties and transportation links. Moreover, Canada and the United States share common cultural traditions, religion and language.

2. The United States and Canada had roughly the same level of economic development and maturity of the market economy. For Mexico, integration under NAFTA was an effective tool for a quick rise in its level of economic development.

3. There was the availability of complementary economic institutions in integrating countries.

4. Since the signing of the agreement heralded a strong economic growth, internal as well as external factors of economic development of the region were assessed as favorable.

5. The United States, Canada and Mexico were united by common economic problems, as well as by the goals set by NAFTA.

6. A certain role was played by the political desire of all three countries to form a free trade zone.

7. The other reason for forming NAFTA was the so-called “demonstration effect”. The intensification of integration processes in Europe and the Asia-Pacific region raised the issue of the creation of the NAFTA.

8. The integration of the North American countries was also caused by a “domino effect”, that occurred in the United States. Changes in the political and economic situation in the world in the late 80's, especially the termination of the Cold

War, marked the end of the bipolar world. Such treaties as the Warsaw Pact and organizations as the Council for Mutual Economic Assistance have disappeared. The strategic and economic position of Russia has weakened. In these circumstances, the countries of Western Europe and the Asia-Pacific region were increasingly trying to get rid of the US control and to concentrate resources on strengthening their economic power. Thus, the countries of Western Europe began to deepen and widen the European integration, which led to the introduction of new restrictions on third countries, and to further increase of their power and competitiveness. Japan, using the rapid growth of its economic power, began to shape the course of a new Asian common market. In this situation, the formation of a free trade zone in North America seemed a prudent and necessary step for the United States [83].

According to the Treaty, the objectives of the creation of NAFTA were the following:

- to eliminate trade barriers and to facilitate the international movement of goods and services between the territories of the parties (Canada, United States, Mexico);
- to promote conditions of fair competition in the free foreign trade;
- to increase investment capabilities of the member states;
- to ensure appropriate and effective protection of intellectual property rights in the territory of each party;
- to establish effective implementation procedures for the agreements of the joint administration and decision-making;
- to create a framework for further trilateral, regional and multilateral cooperation in order to increase and enhance the benefits of the agreement.

It should be noted that in spite of all agreements signed between the participating countries under NAFTA, Canada, USA and Mexico have maintained their own legislation of foreign trade, because the creation of the customs union was not planned. However, the content of the contract substantially exceeds the simple goal of creating a free trade area [84].

In general, the NAFTA is a comprehensive agreement that is not only aimed to gradually reduce the trade and investment barriers in most sectors of economies of participating countries for fifteen years, but also includes issues of investment, liberalization of services, intellectual property rights, environmental, labor cooperation and interstate dispute resolution mechanism.

Signed on December 17, 1992, the agreement entered into force on January 1, 1994. The central thrust of the agreement is to eliminate the vast majority of tariffs on products traded among the United States, Mexico, and Canada. The terms of the agreement to gradually phase out these tariffs and the final aspects of the deal weren't fully implemented until January 1, 2008. The deal removed export tariffs in several industries: agriculture has been a major focus, but tariffs have also been reduced on items like textiles and automobiles. NAFTA also implemented intellectual-property protections, established dispute-resolution mechanisms, and put into action regional labor and environmental safeguards, though some critics are now lobbying for stronger measures in this direction [84, p. 46].

It is important to note that all three member countries of the integration union were led by different motives to form a regional economic bloc in North America. A specific role was played by economic, political and social considerations.

Despite this, in the purely economic sphere the member states were pursuing similar objectives, namely - improving national competitiveness, taking advantage of the “economy of scale”, reducing transaction costs, encouraging foreign direct investment, helping domestic producers to obtain greater access to financial, labor, material resources, accessing a large market of neighboring countries, strengthening position on the global market, creating a favorable foreign environment, sharing the challenges of globalization, etc.

Canada's primary objective in seeking a free trade agreement with the United States was to secure access to the market that accounted for almost three-fourths of its foreign trade. The prospect of guarantees against new trade barriers through a free trade agreement was appealing. Canada also hoped to depoliticize trade disputes, particularly those involving antidumping and countervailing duties [84, p.47].

A secondary objective of Canada in seeking free trade with the United States was the rationalization of Canadian industries. Some of these industries were protected by relatively high trade barriers, and given the geographically fragmented Canadian market; they were shielded from competitive pressures and unable to realize the benefits of economies of scale. The expansion of trade with the United States would expose such industries to greater competition, and would provide opportunities to increase the production that the domestic market could not provide.

Relations with the United States have always been an important component of the economic development of Canada. Intensive exchange of goods, capital, and services suggests closer economic integration between the two countries, one manifestation of which was the conclusion of numerous trade agreements.

After signing FTA and NAFTA development of economic integration between the two countries reached a new qualitative level. The resulting economic relations of Canada and the US in terms of scope and content are unique in comparison to other partners of industrialized countries. It is important to note that Canada has received the status of a privileged economic partner of the US and gained easy access to the most capacious market in the world.

To date, the US is the largest trading partner of Canada. Thus, according to Figure 6, in 2012 the US made 57.9% of Canadian total trade.

During the period of mutual trade under NAFTA, growth was observed almost continuously. The only exception is the period from 2001 to 2002 due to the economic turmoil that occurred in the US. Figure 7 showed Canada’s main export markets in 2012. Thus, for Canada foreign economic relations with the United States are extremely important, because the main consumer of Canadian goods and services has been the US market. It accounted for 64.3% of Canadian total exports in 2012 as shown in Figure 7.

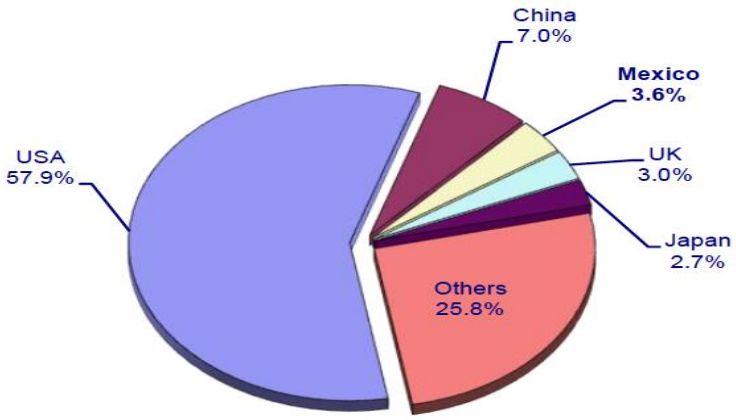


Figure 6 - Canada's main trading partners (total trade in January -August 2012: $645.8 billion of US dollars)

Note - Compiled by the author according to Canadian International Merchandise Trade Database from http://www5.statcan.gc.ca

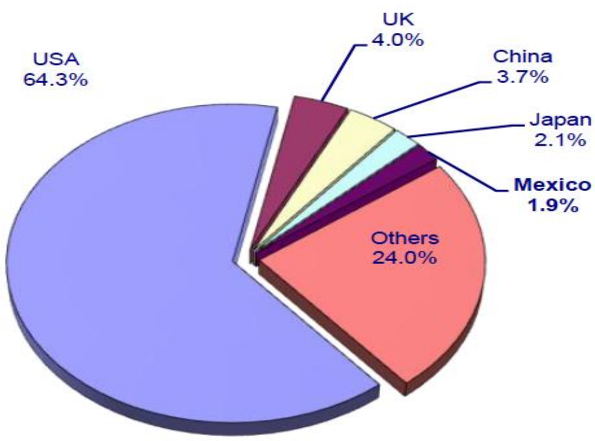


Figure 7-Canada's main export markets (total trade in January - August 2012: $337.6 billion of US dollars)

Note - Compiled by the author according to Canadian International Merchandise Trade Database from http://www5.statcan.gc.ca

In this regard, it is important to note that NAFTA has stimulated significant progress in productivity and specialization in the Canadian economy and contributed to increased economies of scale, quality of products, and price competitiveness. The result was an increase in the overall competitiveness of Canadian exports of both goods and services.

Another result is the of the ratio of exports of goods and services to the GNP Canada has been recognized as most globally integrated by all countries of the G7. It is a group of seven industrialized nations of the world.

However, until now the question of the positive or negative impact of Canada's membership in NAFTA on the development of its economy, trade and economic relations with other countries remains open and unresolved. Making a number of good opportunities for the development of foreign trade, NAFTA also created a number of factors negatively affecting Canada.

The arguments in favor of the agreement are provided in Appendix A.

Despite the positive aspects of the NAFTA, there are a number of negative consequences of the agreement for Canada.

From the point of view of Canadian international trade development, one of the problems is the fact that the agreement to some extent has limited Canada to the North American continent. Duty-free trade under NAFTA has made trade more profitable and multiplied its size within the continent. As a result, the participating countries exchange goods with each other much more readily than with third countries, although the products of third countries can be more competitive in their characteristics. Indeed, this is reflected in the commodity structure of exports and imports of member countries of NAFTA, as well as on competitiveness of exports and imports.

Canadians are also concerned that the competitiveness of domestic goods in the American market is primarily determined by the low value of the currency ratio, and not by a factor of labor productivity growth.

Additionally, the NAFTA agreement has not solved the problem of the lack of geographical diversification of Canadian foreign trade and from this point of view did not live up to expectations of many analysts. On the contrary, the dependence on one major consumer of its exports has increased markedly. To date, the degree of matching of the US and Canada economies reached a very high level. Thus, the already large proportion of the US in Canadian exports and imports has become even greater.

As a result of these circumstances, it has been argued that since the signing of NAFTA, Canada has become more vulnerable, not sustainable.

In addition, the acceleration and deepening of economic integration of Canada and the US persistently raise questions about the future of political integration, in other words - the possibility of absorption of Canada by the United States. In the foreseeable future, such an outcome of events is unlikely.

However, the problem of the dependence of Canada on the United States must be addressed, and one of its major decisions must be in favor of diversification of foreign trade.

Mexico's primary objective in requesting a free trade agreement with the United States was to attract foreign investment by sending a signal to international capital markets that the economic reforms implemented in Mexico were permanent. As a developing economy, Mexico needed both the capital and the technology that would come from increased foreign investments. Gaining improved and more secure access to the United States market was also important to Mexico, but fundamentally the free trade agreement was more about investment than trade. After all, Mexico already had relatively free access to the United States market.

From the Mexican government's perspective, expectations were very high regarding NAFTA in the case of new jobs creation, higher wages, higher economic efficiency, growth and development opportunities, increasing economic and political stability. Assessing the impact of NAFTA on the Mexican economy is much more complicated than estimating the effects of the FTA on Canada's economy. The reason is it impossible to separate out lagged and current effects of ongoing economic reform measures, as well as the effects of currency crises. Consequently, estimates can vary widely depending on methodologies, and estimation techniques employed. However, as an agreement between three countries regarding trade and investment issues, NAFTA has been relatively successful and accomplished more tasks than expected. In general terms, attractiveness of the Canadian economy has increased. It is important to analyze to what extent NAFTA directly contributed to this increase in FDI flows in Mexico. The main research findings suggest that, relative to other trading blocks, NAFTA is responsible for an increase in FDI in Mexico by approximately 70 percent [85].

The United States is the largest investor of FDI in Mexico. US companies make about 50% of investment funds investing in Mexican maquiladoras - companies that collect the finished product of the US components for export back to the United States in the free economic zone of industrial type. These firms account for almost half of Mexico exports and for more than thirty billion dollars of annual sales. Investment in the Mexican economy has helped increase the efficiency of the US production. Many manufacturing companies have cut production costs by transferring assembly of its products to enterprises - maquiladoras. This has contributed to a significant increase in production in the US manufacturing industry, which has grown by almost 60% in 1993-2006. For comparison, over the same period of thirteen years before the signing the agreement the American industrial production grew by only 42%.Figure 8 shows the dynamics of FDI in Mexico before and after NAFTA.

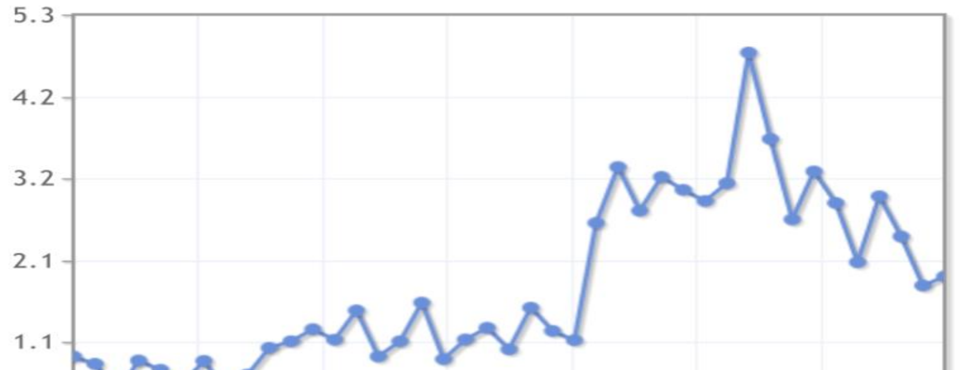


Figure 8- Foreign direct investment to Mexico, net inflows as a % of GDP

Note - Compiled by the author according to the data from the World Bank from http://data.worldbank.org

Net inflows as a percentage of Mexico's GDP increased after NAFTA has come into force and was rising steadily from 1.09% in 1993 to 4.1% in 2001. However, since 2001 the FDI was falling until reaching 1.91% in the year of 2010. Therefore, NAFTA did attract more foreign direct investment in the

Since low-skilled labor is relatively abundant in Mexico, its marginal productivity is low. An obvious expected benefit was that FDI from the United States and Canada – where capital is relatively abundant - would cause local labor employment in Mexico – because NAFTA, unlike the European Union, did not involve labor mobility. The expectation was that these capital inflows would increase wages of low-skilled workers and decrease income inequalities.

In a country like Mexico, where income disparities have been very large, creating political stability through increasing wages of low-income households was perceived as potentially beneficial for Mexico's economic growth prospects [86].

Table 3 shows Mexican wages and GDP per capita in 1998-2011. Simply put, real wages on average have grown in Mexico under NAFTA as shown in Table 3, though the increase was not steady. Wages increased from the early 1980s until the mid-1990s, after that the currency crisis hit and real wages fell by 15.5%. Wages increased after 1998 until 2002 with last percentage increase of 10.8% and then stagnated for several years. Wages fell by 3.2% in 2006 and by 5.0% in 2011.

Table 3 - Mexican Wages and Per Capita GDP, 1996-2009

Index	1998	2000	2002	2004	2006	2008	2010	2011
Average Real Wage Index (LCU, 2005=100)	79	81	90	97	99	102	102	96
Average Real Wages (% change from previous year)	-15.5	2.6	10.8	1.9	-0.1	2.3	-3.2	-5.0
GDP per Capita (in US dollars)	3,814	4,681	6,293	6,850	7,239	8,865	9,913	7,870
Source - compiled by the author based on the data from the World Bank from http://data.worldbank.org								

The increase in wages happened in the relatively higher-skilled labor in the manufacturing sector, particularly in Northern provinces in proximity to the US. This led to an increase in regional income inequalities, leaving the southern states behind.

Also, it was not entirely taken into account that prior to NAFTA the most highly protected industries in Mexico were labor intensive industries such as maize production. As the protection of these industries has been removed, large amounts of labor have been released to be absorbed in other parts of the economy. Usually, the displaced workers lack the necessary skills to find employment in other expanding sectors of the economy. Investments by US firms in Mexican manufacturing sector have been made in industries that are less skill-intensive than the average US industry, but are considered to be more skill-intensive than the average Mexican industry. The fact that most of these investments have been made in states adjacent to the US border has also widened regional wage disparities in Mexico.

Another controversial aspect of NAFTA has been its effect on the agricultural sector in Mexico and the perception that NAFTA has caused a higher amount of worker displacement in the agricultural sector than in other sectors of the economy. Mexico faced increasing import competition from the United States (that subsidies its agricultural industry); many of the changes are also attributable to Mexico's unilateral agricultural reform measures.

After NAFTA, Mexican prices of basic crops such as maize dropped and, subsequently, Mexican imports of those crops increased. However, Mexican agricultural production did not decrease after NAFTA.

In terms of trade growth, NAFTA allowed an increasing integration between Mexico and the US. Historically, the US has always been the main trading partner of Mexico. Imports and exports from Canada and the US accounted for 72% and 78% of total external trade at the beginning of the 1990s, respectively. This share increased significantly to above 92% and 75% in 2000. The integration process has been particularly relevant in the case of Mexican exports, following growing focus on the US, exports increased 6.2 times from 1993 to 2012.

In addition tariff reduction was one of the most important effects of NAFTA. In average tariffs on Mexican total exports to the US fell from 2% in 1993 to less than 0.40% in 1999. As a result of the growth of Mexican exports to the US, Mexico has achieved a substantial trade surplus with the US.

While Mexico's surplus amounted to 13 billion during 1990-1993, it increased to 42 billion between 1994 and 1998. Although Mexico continued to have significant trade deficits with the rest of the world, export growth allowed for partial stabilization of some macroeconomic variables and the exchange rate.

However, the rapid increase in Mexico's external trade has not resulted in favorable overall economic performance. Mexico's growth rate since NAFTA came into effect has been below expectations. Statistics for job creation and wage level have been disappointing.

Figure 9 showed annual GDP growth rate in Mexico in 1993-2011. According to Figure 9, annual GDP growth was very volatile during NAFTA agreement functioning. It fell substantially from 4.5% in 1993 to 6.2% in 1994. After that, the indicator fluctuated around 5% until 2001, after which it dropped to 0. In 2006, the annual growth rate returned to 5% again, but it plummeted down to -6.0% during crises in 2009 and rose again in the following years.

For the US the impact of NAFTA has been extremely beneficial. Moreover, the agreement benefited USA the most compared to Canada and Mexico. Figure 10 showed the US trade with Canada and Mexico in 1993-2011.

Table 4 reflected the total trade between US and Canada and Mexico in 1993-2011. Since NAFTA entered into force in 1994, trade with Canada and Mexico has raised three and half times, reaching 1.2 trillion as shown in Figure 10 and Table 4.

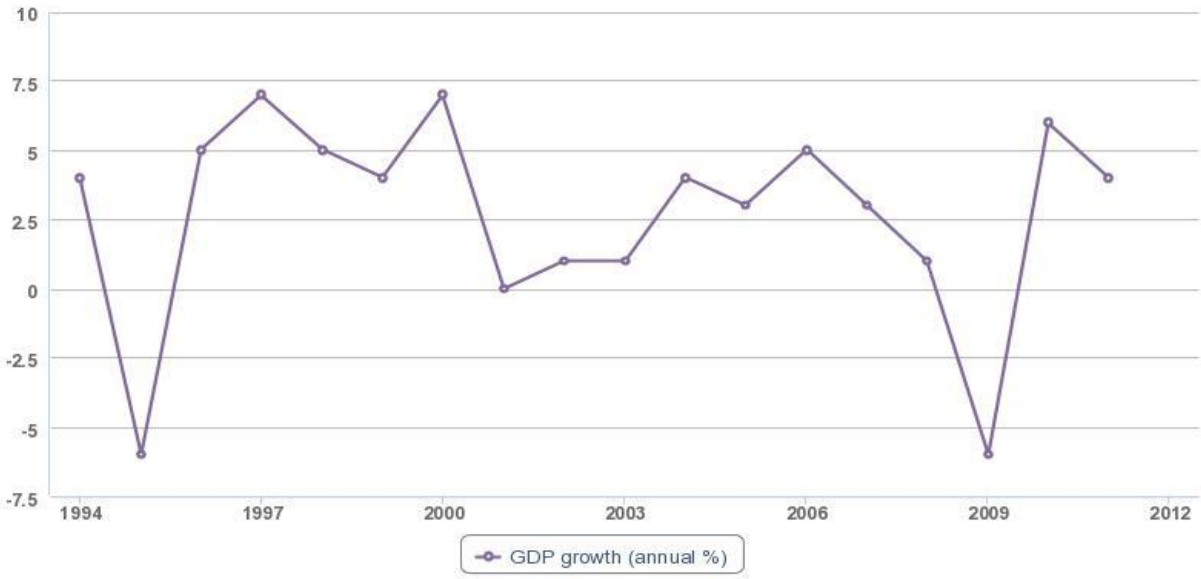


Figure 9- Mexico' annual GDP growth rate, 1993-2011

Note - Compiled by the author based on the data from the World Bank from http://data.worldbank.org

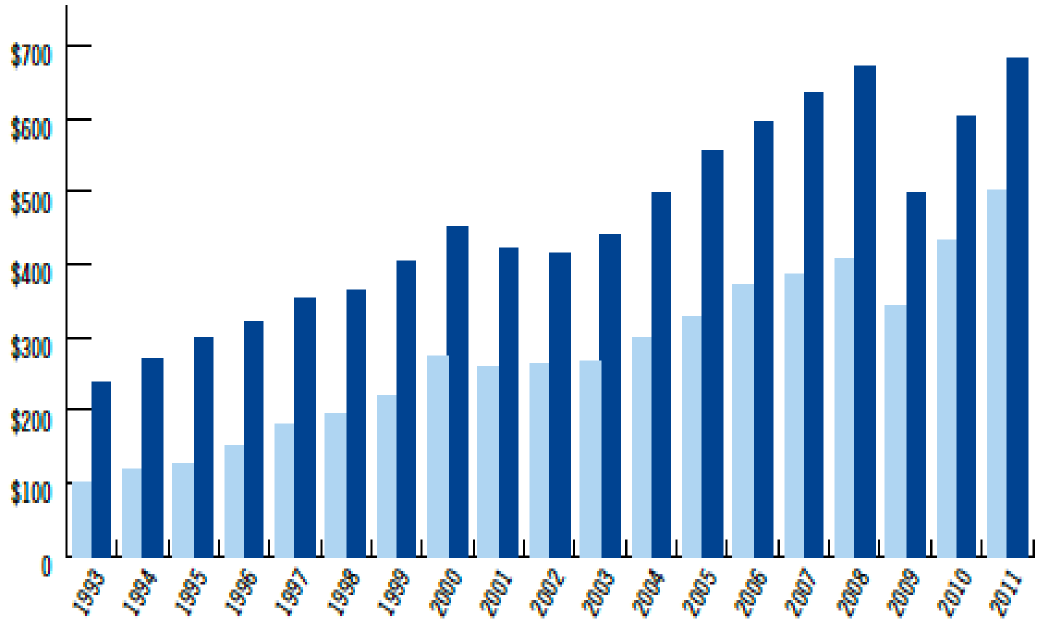


Figure 10 - US trade with Canada and Mexico since NAFTA's entry into force, 1993-2011, billions of US dollars

Note - Compiled by the author based on the data from reference http://data.worldbank.org.

Table 4 - US Total Trade with Canada and Mexico under NAFTA, 1993-2011, millions of US dollars

Total Trade	1993	2000	2011	% Change 1993-2011
With both - merchandise	293,159	657,055	1,058,051	260,9 %
With both - services	43,944	68,800	124,000	182,2 %
With Canada	237,783	452,267	681,401	186,6 %
With Mexico	99,320	273,587	500,649	404,1 %
Grand total	337,103	725,855	1,182,051	250,6 %
Source - compiled by the author based on the data from reference http://data.worldbank.org				

The two countries buy about one-third of US merchandise exports. Total US exports to Canada rose by 86.8% and to Mexico more than tripled during the period from 1993 to 2011. Table 4 shows US exports to Canada and Mexico in 1993-2011. Structure of exports to two countries differs - the US exported mostly services to Canada, and merchandise to Mexico, as reflected in Table 5.

Table 5 - US Exports to Canada and Mexico under NAFT, 1993-2011, millions of US dollars

US Exports	1993	2000	2011	% Change 1993-2011
To Canada – merchandise	100,444	178,941	280,891	179,6 %
To Canada – services	17,016	24,613	56,000	229,1 %
To Canada – total	117,460	203,554	336,891	186,8 %
To Mexico – merchandise	41,581	111,349	197,544	375,1 %
To Mexico – services	10,394	15,532	26,000	150,1 %
To Mexico – total	51,975	126,881	223,554	330,1 %
To both – merchandise	142,025	290,290	478,435	236,9 %
To both – services	27,410	40,145	82,000	199,2 %
Grand total exports	169,435	330,435	560,435	230,8 %
Source - compiled by the author based on the data from reference http://data.worldbank.org				

US imports from NAFTA partners also rose significantly. According to the Table 6, imports from Canada rose by 86, 3% and from Mexico increased almost five times. The trade in merchandise increased by 183, 5% and trade in services grew by 54%.

Trade with Canada and Mexico supports nearly 14 million US jobs, and nearly 5 million of these net jobs are as a result of trade growth generated by NAFTA.

Table 6 - US Imports from Canada and Mexico under NAFTA, 1993-2011, millions of US dollars

US Imports	1993	2000	2011	% Change 1993-2011
From Canada - merchandise	111,216	230,838	316,510	184,6 %
From Canada - services	9,106	17,875	28,000	207,5 %
From Canada - total	120,323	248,713	344,510	186,3 %
From Mexico - merchandise	39,918	135,926	263,106	559,1 %
From Mexico - services	7,428	10,780	14,000	88,5 %
From Mexico - total	47,345	146,706	277,106	485,3 %
From both - merchandise	151,134	366,765	579,616	283,5 %
From both - services	16,534	28,655	42,000	154,0 %
Grand total imports	167,688	395,420	621,616	270,7 %
Source - compiled by the author based on the data from reference http://data.worldbank.org				

NAFTA has been a boon to the competitiveness of US manufacturers, which added more than 800,000 jobs in four years after NAFTA entered into force. Canadians and Mexicans purchased $428 billion of US manufactured goods in 2011, generating $36,000 in export revenue for every American factory worker.

If to talk about the downfalls of the agreement for USA, some analysts say that the long-time growth in the US trade deficit accelerated dramatically after NAFTA became effective in 1994. According to the Bureau of Labor Statistics, the $30 billion US trade deficit in 1993 increased by 281% to an inflation-adjusted $85 billion in 2002. However, in 2011, the United States registered trade surpluses with its NAFTA partners in manufactured goods ($14.5 billion), services ($40 billion), and agricultural products ($2.6 billion). The fact that US petroleum imports from Canada and Mexico contribute to the overall US trade deficit stems from US energy policy and geology — not NAFTA.

By the end of August 2012, total trade in the NAFTA region recorded a value of $705, 6 billion USD compared to $188,5 billion in 1993.

Figure 11 shows the dynamics of trade among NAFTA partners in 1993-2012. Therefore, during 20 years of NAFTA agreement trilateral trade has more than tripled. The volumes of trade have been growing all the way except for a slowdown in 2001 and 2009 due to economic turmoil and crises during those years.

However, in spite of the significant increase in total trade in NAFTA region, the structure of trade hasn’t changed much. In 1993, 69, 3% share of total trade between Canada and the US, in 2012 the percentage has decreased to 53,5%. The share of trade between Mexico and Canada has increased slightly - from 1, 3% in 1993 to 3, 4 % in 2012. On the other hand, the share of trade between the US and Mexico has gone up from 29, 4% in 1993 to 43,1% in 2012.

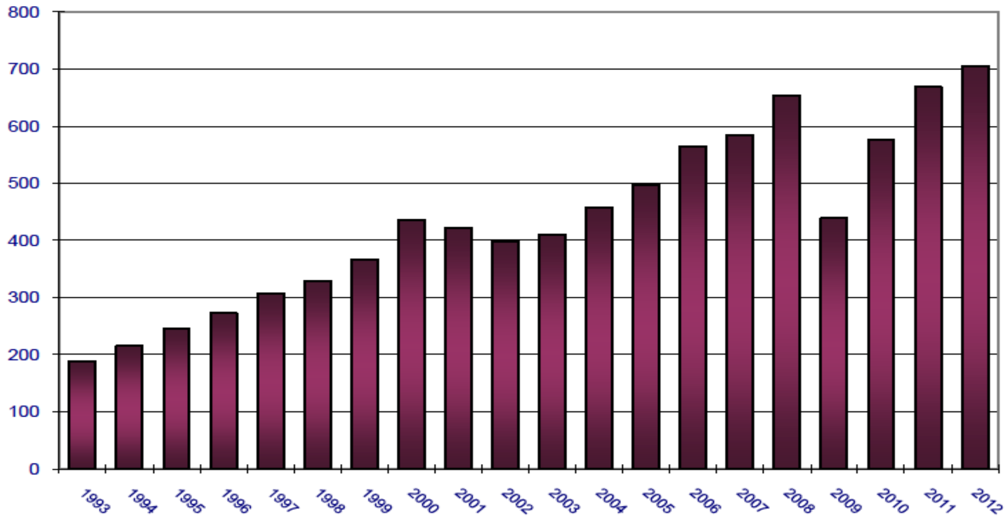


Figure 11- Trade among NAFTA Partners, 1993-2012, billions of US dollars

Note - Compiled by the author based on the data from Statistics Canada from http://statcan.gc.ca

Table 7 shows the volumes of trilateral trade among NAFTA partners in 1993-2012.

Table 7 - Trilateral Trade between the NAFTA Partners, 1993-2012, millions of US dollars

Country	Year			Growth Rate	
	1993	2011	2012	2012/1993 %	2012/2011 %
NAFTA partners					
Total trilateral trade	188,507	668,239	705,579	274.3	5.6
US imports from NAFTA partners					
Mexico	25,630	173,217	186,625	628.2	7.7
Canada	72,501	208,666	217,110	199.5	4.0
US	29,750	114,877	121,889	309.7	6.1
Canada	682	6,066	6,401	838.1	5.7
Mexico	1,766	16,567	16,755	849.0	1.1
US	58,179	148,857	156,799	169.5	5.3

Source - compiled by the author based on the data from reference http://data.worldbank.org

It can be noticed from Table 7 that Canada's imports from Mexico have grown by 849, 0%, but the nominal value increased only by about 15 billion dollars in 20 years. Mexico's imports from Canada have increased even less - by about 5, 5 billion dollars in 20 years. Trade of Canada and Mexico with the US has increased considerably more in comparison to the trade between Canada and Mexico themselves (Table 7).

Thus, this analysis suggests that NAFTA seems to be trade creating in all three member countries, but most significantly in the US. NAFTA's impact on its member countries has not been equal.

Obviously, NAFTA did boost trade and economy growth in USA and Canada, but its influence on Mexico's economy stays questionable.

As noted earlier, globalization benefits the counties with more developed economic systems, weaker countries are at risk of being absorbed by world powers. For the protection of national interests and traditions in determining their "niche" in the structure of the single market, countries are seeking to achieve accelerated growth. This becomes possible due to the participation in the integration blocks. Not every economic alliance of countries is able to develop into integration. There are many economic unions in the developing regions of the world, operating for more than 20 years, which have not led to the integration of national economies in a globalizing world. This is explained by the fact that the processes of integration are possible at a sufficiently high level of technical, economic, political and legal development of the partner countries. In turn, economic integration includes two related but distinct processes. Selecting one of them causes the character and principles of further development of the autonomous union, the overall objective of which are the formation of a single economic zone. This objective is achieved by the decisions taken which allow subdividing the processes of integration into positive and negative ones. Removal of existing economic barriers between countries - tariff, non-tariff, technical, to move the main factors of production determines the value of negative integration.

2.2 Analysis of development integration in the case of EurAsEC

Current global processes lead to a need of assessing the appropriateness of the chosen development strategy of Kazakhstan by determining its place in the global and regional processes in Eurasia.

March 1994, the President of the Republic of Kazakhstan N.A.Nazarbayev has proposed the concept of forming the Eurasian Union, which was going to be based on a voluntary, equitable integration, joint political and economic development of the post-Soviet states, and the entrance of CIS countries to a leading position in global economy [86].

That concept presents the principles, objectives and mechanism of formation of the Eurasian Union, provides the establishment of a number of coordinating supranational structures, sets out the basic directions of cooperation - the economy, science, culture, education, environment and defense.

The relevance of the theory of Eurasianism to the world community is determined by the following factors:

- intensification of Asian trends in the international economy and politics;
- development of the idea of Eurasianism as a new philosophy of regional integration in the post-Soviet space and Eurasia;
- formation of the Eurasian economy as an independent geo-economic object in an emerging multipolar world.

Participation in integration unions is foreign policy priority for the strategy of Kazakhstan. Great opportunities to expand its capabilities are available in the deepening integration of Kazakhstan in the framework of regional integration, of which a main goal is consolidation and comprehensive economic integration necessary to achieve stability, economic progress and military-political security in the region.

At the present stage of economic development Kazakhstan is a party to a number of sub-regional and regional integration unions, such as:

- Commonwealth of Independent States (CIS), formed in the disintegration of the former Soviet Union - Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Russia, Tajikistan, Turkmenistan, Uzbekistan, Ukraine (December 8, 1991);
- The Eurasian Economic Community (EurAsEC), the agreement on the establishment of which was signed on October 10, 2000 in Astana, Kazakhstan;
- CES ("CES Four") - Belarus, Kazakhstan, Russia, Ukraine (23 February 2003);
- Shanghai Cooperation Organization (SCO), whose members include China, Kazakhstan, Kyrgyzstan, Russia, Tajikistan, Uzbekistan (26 April 1996);
- The Economic Cooperation Organization (ECO), in which Kazakhstan entered on November 1992, which now comprises 10 countries, including the founding countries (Iran, Pakistan and Turkey);
- Asian Cooperation Dialogue (ACD), to which the Republic of Kazakhstan, along with Oman, Sri Lanka and Kuwait,was accepted as a member in June 2003. [102]

The Eurasian Economic Community (EurAsEC) stands out among other economic integration unions, that do not show their success in expected measure.The Eurasian Economic Community is one of the most developed regional networks in the CIS. The participation in EurAsEC is one of the priorities of foreign policy of Kazakhstan.

Institutionalization of the Eurasian Economic Community (EurAsEC) has been due to several factors, for which there are the somereasons and prerequisites. The reasons have a direct impact on the performance of a particular event, the prerequisites - indirect impact.

As for the reasons for the creation of EurAsEC, they should be considered from positive and negative aspects of the functioning of the Customs Union which was the forerunner of the Community. The name of the organization - "Customs Union", reflects rather the purpose of association, not the achieved result.

The favorable conditions for the formation of the CU appeared in 1994-1995. At the moment of signing the agreements on the Customs Union on the 6th and 20th of January, 1995, Russia, Belarus and Kazakhstan have already agreed on import duties. Level of unification was extremely high then - Russia and Belarus had their tariffs match on 95%, Kazakhstan has adopted Russian customs tariff with the exception of eight positions for nonferrous metals, which were its main export goods at that time.

However, in the following years (1996-1999) CU participants failed to keep the current level of harmonization of customs tariffs. As a result, the level of match of customs duties declined in 1998 to 47%, in 1999 it increased slightly (57%) and remained in this range until the establishment of the Eurasian Economic Community.

Among the reasons that contributed to such a significant reduction of unification should be included the following factors:

- expansion of the commodity nomenclature of CU countries by new goods (for example, highly processed products), which were not to be included in general list of goods which were subject to tariff unification;

- the presence of goods that are of a particular importance for the national economies of CU countries, and that were not included in the list for tariff unification;

- fundamental differences in the positions of Russia and Kazakhstan to the zero-rate customs duties (percentage of zero-rate customs duties in the Kazakhstani customs tariff is 27%, while in the national rates of Belarus and Russia - less than 1%); this is a serious obstacle to the formation of the Common Customs Tariff and the Customs Union in general);

- thedegree of coordination of the positions of countries on accession to the WTO.

According to Protocol on Trade Negotiations of July 3, 1997, it was decided to carry out two processes simultaneously - the creation of the Customs Union and accession to the WTO. States undertook and conducted independent negotiations with the WTO and at the same time were trying to reconcile their positions with each other. However, it is recognized that this two-step negotiation process was not very successful, resulting in November, 1998 when the Republic of Kyrgyzstan solely joined the WTO. The requirements for the entry of Kyrgyzstan into this organization automatically reduced the level of unification of the customs tariff of the republic with the CCT to 17%.

So, until the year 2000 CU participants failed to solve important problems such as the creation of a single customs territory, the formation of CCT and coordination of positions on accession to the WTO. But this does not mean that the activities of the Customs Union failed as a whole. One of the significant achievements of the Union was the creation of a free trade regime, which was later inherited by EurAsEC.

In addition to the introduction of a free trade regime at the time of conversion of CU to EurAsEC several problems have been fully or partially solved as it is shown in Table 8.

However, despite some accomplishments, it should be recognized that the main reason for the transformation of CU into EurAsEC was the failure of association to fully meet its objectives.

The treaty establishing EurAsEC was signed on October 10, 2000 in Astana and entered into force on May 30, 2001 after its ratification by all Member States. Members of the Eurasian Economic Community since its formation are the five states - Belarus, Kazakhstan, Kyrgyzstan, Russia and Tajikistan.

Table 8 - Results accomplished by CU in 1995-2000

Sphere	Result
Trade and economic sphere	Agreement on a 60% CCT for three countries (Russia, Belarus and Kazakhstan), initiating the non-tariff regulations and the establishment of common trade regime with third countries.
The area of economic policy	Agreement on the main directions for economic restructuring of the CU economies, introduction of the mutual convertibility of national currencies; agreement on the measures for ensuring the interoperability of national monetary and financial systems; initiating the creation of a common payment system; the transition to the principle of indirect taxes by "country of destination", creation of the concept of forming a common economic space.
The humanitarian field	Introduction of visa-free movement of citizens, agreement on the process for emergency medical care; simplification of the procedure of sending postal and money transfers; agreement on a simplified procedure for acquiring citizenship, creation of the legal basis for recognition and equivalence of documents on education, degrees and titles.
Legal and organizational areas	Initiation of harmonization of national legislation in trade, tax, customs, monetary and social activities; formation of 14 boards and commissions in the main areas of integration cooperation.
Source - compiled by the author according to the source [87]	

On January 25, 2006 the Protocol of Accession of Uzbekistan to the Organizationwas signed. In October 2008, Uzbekistan has suspended the participation in the work of the EurAsEC.

Since May 2002, the status of observers gained Ukraine and Moldova, in January, 2003 - Armenia. Observer rights are also held by the Interstate Aviation Committee and the Eurasian Development Bank.

The main tasks for the Community are the following:

- completion of registration in full free-trade regime, the formation of a common customs tariff and a unified system of non-tariff regulation;
- the free movement of capital;
- creation of a common financial market;
- harmonization of principles and conditions for the transition to the single currency within the Eurasian Economic Community;
- establishing common rules for trade in goods and services and their access to domestic markets;
- a common unified system of customs regulations;
- development and implementation of interstate target programs;
- creating equal conditions for production and business activities;
- establishment of a common transport market and the integrated transport system;
- formation of a common energy market;
- creating equal conditions for foreign investment in the markets of the Community;
- ensuring the free movement of citizens of the EurAsEC states within the Community;
- harmonization of social policies in order to create community welfare states, providing a common labor market, common educational space, coordinated approaches to healthcare issues, labor migration, and others;
- approximation and harmonization of national laws, ensuring interaction of legal systems in order to create a common legal space within the Community [104,].

Despite the fact that the Eurasian Economic Community was established 13 years ago, before 2006 the integration process did not develop qualitatively. The key to enhancing regional integration cooperation within the EurAsEC were the following actions:

- the establishment of the EDB in 2006;
- the creation of Customs Union of Belarus, Kazakhstan and Russia;
- the entry into the WTO as a Customs Union of three countries;
- the formation of Anti-Crisis Fund.

In February, 1999, Belarus, Kazakhstan, Kyrgyzstan, Russia, and Tajikistan signed the Agreement on the Customs Union and Common Economic Space, which defined stages of integration without specifying the dates.

The first stage - to ensure the full implementation of the free trade regime, in particular:

- non-tariff and quantitative restrictions in mutual trade;
- introduction of a unified system of indirect taxes;
- elimination of administrative, fiscal, and other impediments to free movement of goods.

The second stage is - the creation of the Customs Union, involving a single customs territory, a common customs tariff, abolition of customs controls at the internal borders and harmonization of regulatory economics and trade.

The third stage is - the formation of a Common Economic Space, providing for a common economic policy and the creation of a common market for services, labor and capital, the harmonization of national legislation and concerted social and scientific-technological policy.

Formation of the Customs Union of Belarus, Kazakhstan and the Russian Federation was exercised in accordance with the Action Plan for the Customs Union, approved by the decision № 1 of the EurAsEC Interstate Council (the supreme body of the Customs Union) at the level of Heads of State on October 6, 2007, and the stages and terms of formation of the common customs territory of the Customs Union established by the decision № 9 EurAsEC Interstate Council on June 9, 2009.

To date, the objectives set out by the above documents are mainly fulfilled.

Measures are implemented to form the legal base of the Customs Union, the Common Customs Tariff of the Customs Union (here in after - CCT TC), a unified system of foreign trade and customs regulation, sanitary, veterinary and phytosanitary control, and the institutional structure of the Customs Union.

A unified system of measures to regulate foreign trade that was established in the Customs Union, is organically integrated into the national economic management systems, while acting as a tool for the implementation of trade and economic interests of Belarus, Kazakhstan and the Russian Federation.

The final phase of the activities related to the transfer of agreed types of state border control (customs, transport, sanitary, veterinary, phytosanitary quarantine) on the external borders of the Customs Union and to the unification of trade regimes and protective measures against third world countries is being completed.

In addition, the work on the introduction of the Customs Union Customs Code (hereinafter - CU CC) is almost finished. According to the Code Commission of the Customs Union (hereinafter - the Commission) adopted more than 100 regulatory documents, prepared 20 draft international agreements, 16 of which were adopted and applied.

Of the 51 international agreements on the basic list of international treaties of the legal framework of the Customs Union, 42 entered into force and are applied. 9 international treaties are not applied, of which 7 are no longer applicable due to the entry into force of CU CC [105].

In addition to the previously indicated international agreements, more than two dozen international agreements that regulate various aspects of circulation of goods within the common customs territory and the activities of the Customs Union are adopted.

In the sphere of customs regulations the following measures are taken:

- a unified system of customs regulation in the common customs territory of the Republic of Belarus, Kazakhstan and the Russian Federation started functioning;

- national harmonization of legislation with the CU CC was conducted;

- the International Convention on the Simplification and Harmonization of Customs Procedures of 18 May, 1973 was ratified;

- by the decisions of Commission were adopted: the forms of customs documents and instructions for filling them out, the procedure of customs operations on goods for the personal use of individuals; the lists of goods temporarily imported with full exemption from payment of customs duties, the documents for the declaration and classification of goods and their customs value;

- the preparations for the transfer of customs, transport, sanitary, veterinary, phytosanitary quarantine control of the Russian-Belarusian and Russian-Kazakh border to the external border of the Customs Union are in the stage of completion;

- in the sphere of unified customs tariff and non-tariff regulation;

- the measures to create the legal framework of a unified customs tariff regulation of the Customs Union are fully implemented;

- more than 70 decisions on issues of implementation of the common measures of customs and tariff regulation were adopted.

The following protecting measures are implemented:

- the agreement on the application of special protective, antidumping and countervailing measures during the transitional period, and implementation plan for spreading protective and anti-dumping measures on a single customs territory of the Customs Union are adopted;

- the Protocol on the procedure for granting the authority that conducts the investigation, the information for the purposes of investigation, prior to the introduction of special protective, antidumping and countervailing measures in relation to third countries was adopted;

- in the sphere of technical regulations and the application of sanitary, veterinary and phytosanitary measures;

- began to operate a single legal framework for the application of sanitary, veterinary and phytosanitary measures, including the use of common lists of controlled goods; common requirements for these products; a common procedure for importing it into a common customs territory and moving it; single form registration permits, which are recognized by all members states of the Customs Union;

- in the framework of the Customs Union are canceled: the use of sanitary-epidemiological conclusions, permitting authorized body to import veterinary products (goods); certification of exporting country’s companies by the representatives of the importing country in case of mutual supply of goods;

- works are held to harmonize the test methods for the evaluation of conformity of goods to common sanitary and epidemiological and hygienic requirements;

- the unified veterinary certificates are developed and approved for goods that are imported to the customs territory of the Customs Union from third countries and that are subject to veterinary control;

- the agreement on common principles and rules of technical regulation in the Republic of Belarus, the Republic of Kazakhstan and the Russian Federation was signed [88].

Some changes were made considering the restrictive measures in mutual trade. In order to ensure the abolition of existing and prevention of new restrictive measures in mutual trade the Agreement on the free movement of goods within the common market of the Customs Union was developed, it contains the basic principles of free movement of goods in the Customs Union, excluding the legal basis to restrict their turnover compared to locally produced goods.

Gross turnover of mutual trade of member countries of the Customs Union in 2010 has increased in value by 21%, in 2011 - by 32% and continues increasing. Work within the framework of the Customs Union promotes the development and strengthening of the competitive environment for the business community. For the citizens of the Customs Union the cross-border links were greatly facilitated.

People do not have to fill a lot of customs documents, wasting time and energy on the boundary.

Table 9 describes the measures taken in the area of regulation of tax and financial relations. According to Table 15 some changes there have also taken place.

Table 9 - Measures taken in the area of regulation of tax and financial relations

Area	Accomplished result
Transfer and distribution of import duties	Agreement about the set up and the use of the order of transfer and distribution of import customs duties started functioning an in the customs union (and of other duties, taxes and charges that have an equivalent effect). The Agreement provides that import duties are transferred to a single account of the authorized body of the Party in which they are to be payable in accordance with the customs legislation of the Customs Union, and allocated to the budgets of the Parties in accordance with the standards of distribution set for the Republic of Belarus - 4.70%, the Republic of Kazakhstan - 7.33%, Russian Federation - 87.97%.
Currency regulation and currency control	In order to create a uniform procedure of movement of cash across the CU customs border a Treaty was signed. The Treaty established a threshold of mandatory written declaration for one-time export by individuals of cash and (or) traveler's checks that exceed the equivalent of 10,000 US dollars in total amount.
Taxes	The normative - legal base of the Customs Union in the field of indirect taxation is formed. It regulates the procedure for collecting indirect taxes and provides the monitoring of their payment in case of the import and export of goods.
Source - compiled by the author based on source [87, p.20]	

However, it was obvious at the beginning that the creation of the Customs Union within the Eurasian Economic Community will face a number of serious problems. In particular it covers:

1. existence of significant differences in national legislation of the Customs Union;

2. the absence of a compensation mechanism for the introduction of the Common Customs Tariff;

3. inconsistency of the parties in the use of certificates of origin;

4. strengthening the external borders of the Customs Union;

5. the lack of uniform standards in the implementation of the Customs Union trade policy.

The situation in 2013 shows, that the initial problems and related concerns about the success of the Customs Union were not groundless.

Certainly, the creation of this integration association has a positive side. With the cancellation of customs clearance procedures at the internal borders of the Customs Union on July 1, 2010 and the transfer of customs control from the internal borders of the CU to external borders opportunities to accelerate and increase the volume of trade between the three republics has expanded. Thus, in the first half of 2011 the volume of exports from Kazakhstan to the members of CU increased by 51.2% compared to the same period last year, while imports - by 39.6%.

With the transfer of customs control to the external borders, the external borders are going to be strengthened, which will reduce illegal import and defective products entrance to the Kazakhstan market. The CU creates conditions to curb smuggling, which is directly linked with increased corruption and threats to national security. Many representatives of the Kazakhstan business believe that the policy that was previously held by the government to stimulate imports led to the complete destruction of the domestic production, social and professional degradation of society. With the formation of the CU the opportunities for joint ventures has increased, that will make possible to work for a common market and will protect from the supply of Chinese goods at bargain prices.

Kazakhstan entrance into the Customs Union was an additional factor that contributes to the economic and political stability of the country. It significantly expands the potential markets for the further development of a more or less successful in the present economic sectors (fuel and power, ferrous and non-ferrous metals) and for the future revival of degraded sectors (agriculture, etc.). Thus, the foreign trade of Kazakhstan in the Customs Union and the change in the foreign trade turnover of Kazakhstan for 2007-2011 is presented below.

According to Table 10, we see that in 2007-2008 foreign trade of Kazakhstan grew at a moderate pace; it is related to the sustainable development of foreign economic activity of the country. At the same time, it should be noted that as a result of the global financial crisis, the economic situation in Kazakhstan in 2009 was quite complex. This is also evident from the figures of foreign trade of the country. Foreign trade turnover in 2009 compared to 2008 decreased by 35.5%, including exports decrease by 42.9%, imports decrease by 24.7%.

Table 10 - Foreign trade of the Republic of Kazakhstan, 2008-2011, billions of US dollars

WTO Indicators:	2008	2009	2010	2011	2012
Foreign Trade Turnover	98,3	109, 9	71,1	97,3	119,4
Export	79,8	71,2	40,7	60,2	76,8
Import	18,5	37,9	30,4	37,1	42,6
Net Export	61,3	33,3	10,3	23,1	34,2
Source - compiled by the author according to the Agency of Statistics of the Republic of Kazakhstan from http://www.stat.kz					

Foreign trade shows that Kazakhstan has a positive trade balance in 2010. The foreign trade turnover of the country at the end of 2010 amounted to $97.3 billion, a 36.9% increase over the previous year, exports increased by 48%, imports - by 22%. Thus in 2010 the trade turnover between Kazakhstan and the rest of the Customs Union was 13.5 billion dollars, of which more than 90% is with Russia. 2010 was the “turning point bridge” that led Kazakhstan on a new course of development - economic renewal and sustainable development of foreign trade of Kazakhstan.

However, there are some downfalls of the Customs Union that exist today. Statistics indicates that the formation of the CU has not led to significant increase in trade within the Common Economic Space. Specialists believe that this is due to the low competitiveness of products, the lack of uniform rules of the market and the lack of freedom of movement of goods, services and capital. It is noted that the main problem of trade between members of the CU is a small number of items that participants are willing to offer to each other to implement. In addition, increased competition, as a result of lower prices for imported goods, strikes at some industrial markets. This creates the conditions for the displacement of some domestic producers from the market and hostile takeovers.

Moreover, with the creation of the Customs Union prices in Kazakhstan has increased. Thus, according to the National Bank of Kazakhstan in January - July of 2011 inflation was 5,6% (January - July of 2010 – 4,6%). In July 2011, the annual inflation rate increased to 8,5% (in December of 2010 – 7,8%). In January - August 2011 its rates were 5,9%, on an annualized basis (August of 2011 to August of 2010) - 9%. One of the factors that triggered inflation was the introduction of the Common Customs Tariff and opening the state border. If before the accession of Kazakhstan to the Customs Union average level of import duty was 6.2%, then after the formation of the CTT average of import duties on goods from third countries was equal to 10,6%.

In addition, there is a significant increase in prices of petroleum products. Thus, regulated prices for gasoline Ai-92/93 in August 2011 increased by 29.2%compared to the beginning of 2010,prices of AI-80 increased respectively by 28.7% and diesel fuel - by 34.3%. The rise in prices of petroleum products in the Republic of Kazakhstan happened due to the opening of borders in the CU, simplification of customs formalities, the intensification of trade, and increase in the supply of Russian oil products to Kazakhstan. The presence of these trends will lead to some alignment of Kazakhstan and Russian prices for petroleum products in the domestic market of the country. Doing so may result in an outflow of domestic petroleum products outside the country.

Table 11 shows the level of fuel prices in the countries of the Customs Union in August, 2011. According to Table 17 the lowest prices for oil in Kazakhstan are presented. And in the future, as noted above, a further increase in prices of petrol and diesel is most likely to take place in the country.

Table 11 - The level of fuel prices in the countries of the Customs Union on August 21, 2011, for 1 liter, in US dollars

Belarus		Kazakhstan		Russia	
Gasoline (Ai-92)	Diesel Fuel	Gasoline (Ai-92)	Diesel Fuel	Gasoline (Ai-92)	Diesel Fuel
0.9	0.9	0.7	0.6	0.9	0.86
Source - compiled by the author based on the data from the National Statistical Service of the Customs Union.					

In this regard, the Kazakhstan government is taking measures to regulate the prices of petroleum products. Thus, the presidential decree of July 20, 2011 № 463-IV passed the law “On state regulation of production and turnover of certain types of petroleum products”. In accordance with Article 6 of the Act, the Government “said the procedure for determining the maximum price for retail sales of petroleum and petroleum products list, which established the state regulation of prices”. As noted above, in August 2011, the Government has set the following maximum retail prices for country gas stations: gasoline Ai-92/93 - 106 tenge per liter; AI-80 - 86 tenge per liter and diesel fuel - 90 tenge per liter.

However, the implementation of the law met some problems. First, the petroleum refineries in Kazakhstan limited the amount of gasoline and diesel fuel released by wholesalers (allegedly due to the need for agricultural purposes), which led to a shortage of petroleum products in the domestic market. In particular, from the gas stations of the Republic of Kazakhstan in August 2011, gasoline AI-92 has almost disappeared. Secondly, the sales of petroleum products in the border regions near Russia have increased. This is the shortage of gasoline for consumers. The current situation shows again: saving a significant difference in the prices of petroleum products in the Customs Union could lead to an imbalance of supply and demand in the oil market and increased fuel scarcity due to their export to neighboring states of CU for better prices.

The solution to these problems is possible, primarily through the creation of an adequate mechanism for the implementation of the Law “On state regulation of production and turnover of certain types of petroleum products”. It is important to gain control on the part of public authorities for the implementation of the approved plan of fuel supply in the domestic market and the misuse by some economic agents of a dominant position in the market. In addition, it is necessary to solve the issues of increasing domestic production of oil, increasing its competitiveness and refinery feedstock of the Republic . Unfortunately, these problems currently are being solved very slowly. In response, the government of Kazakhstan made a decision on the import 50 tons of gasoline A-92of the National Company “KazMunaiGas” from Russia to Kazakhstan. Imports will be at Russian prices and sales - at Kazakhstan regulated prices. Obviously, with the current difference in fuel prices in the Customs Union, NC “KazMunaiGas” will import oil from Russia “at a loss”.

In this way the government is trying to solve two main problems. First is the deficit in the domestic fuel market of the country which is to be eliminated. The second is development of inflation which is to be prevented, keeping it in the planned corridor of 6-8%. While solving the problem of fuel shortages, the government of Kazakhstan also plans to negotiate oil processing in high-octane gasoline at a tolling scheme with one of the Chinese refineries. Supply of oil to a Chinese tolling refinery will be around 1.5 million tons per year.

So, as one can infer from the analysis, it is hard to answer the question of how beneficial was the creation of CU to Kazakhstan at the current moment. For a precise answer some time should pass, only then the achieved results will tell how wise was the decision of the Heads of State to deepen the integration between Belarus, Kazakhstan and Russia.

2.3 Lessons for developing countries

Next integration Union for comparison, we chose the Eurasian Economic Community. EurAsEC as well as NAFTA is the first stage of integration in the free trade zone.

During the more ten years from 2000 to 2013 macroeconomic indicators have improved significantly in the countries of EurAsEC: stable growth of the gross domestic product, industrial and agricultural production, the volume of freight, domestic currency is stabilized, wages and pensions have increased.

Table 12 describes the growth rates of the main economic indicators of EurAsEC countries in 2012 compared to 2001. According to Table 12, compared with 2001, the average GDP among the EurAsEC member countries has grown by 56% by 2012, industrial output - by 51%, the volume of agricultural production - by 16%. Also, the volume of investment in fixed assets more than doubled. For Kazakhstan individually the changes were especially noticeable: the GDP almost doubled as did the volume of industrial production. The changes in agriculture development were not too large - the production volume increased only by 22% in ten years. Retail trade and investments in fixed assets, on the other hand, has grown three and four times respectively.

Table 12 - Growth rates of the main economic indicators of EurAsEC countries in 2010 compared to 2012, in constant prices, percent

Country	Gross Domestic Product	Industrial production	Agricultural Production	Investment in fixed assets
Belarus	194	211	152	428
Kazakhstan	195	181	122	315
Kyrgyzstan	141	110	116	184
Russia	152	143	110	204
Tajikistan	198	173	203	...
EurAsEC	156	151	116	220
Source - compiled by the author based on statistical data collected from the official website of the Eurasian Economic Community from http://evrazes.com/docs/statistics				

The indicators from the previous table are analyzed individually. If we analyze the dynamics of GDP during a period of integration from 2000 to 2009 in more details, a steady growth rate from year to year can be noticed in all countries that are members of the union as shown in Appendix B. Even in 2009, after the global economic crisis, the GDP growth was positive in all member countries except for Russia. The positive growth of GDP is reflected in Figure 12. According to Figure 12, in ten years the slowest growth was observed in Kyrgyzstan and in Russia - GDP in those countries grew only by approximately 50%.

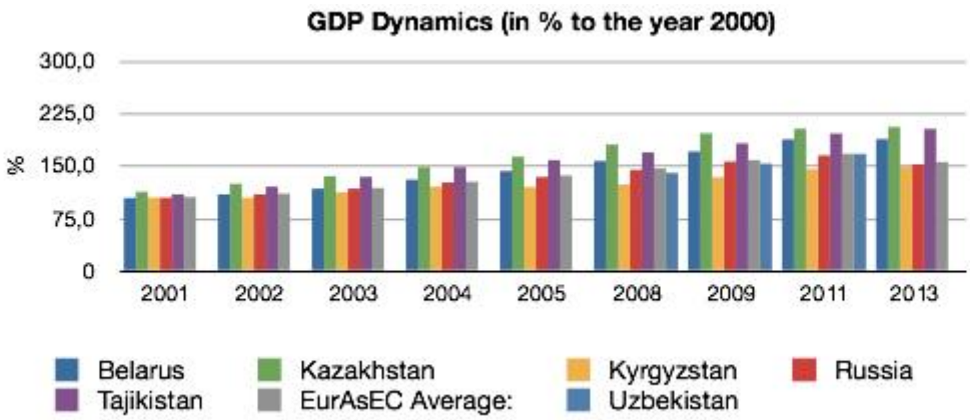


Figure 12- GDP dynamics in EurAsEC countries, 2000-2013
(in % to the year 2000)

Note - Compiled by the author based on statistical data collected from the official website of the Eurasian Economic Community from http://evrazes.com/docs/statistics

The growth in the volumes of industrial production has been not so steady as in the GDP case. Industrial production was increasing relatively evenly in Belarus, Kazakhstan, Russia and Tajikistan - the total increase in ten years totaled to 199%, 186%, 131% and 181% respectively.

The total increase totaled to 105%, which is a very small growth for a ten year period of time. The graphical representation of the volumes of industrial production dynamics is shown in Figure 13.

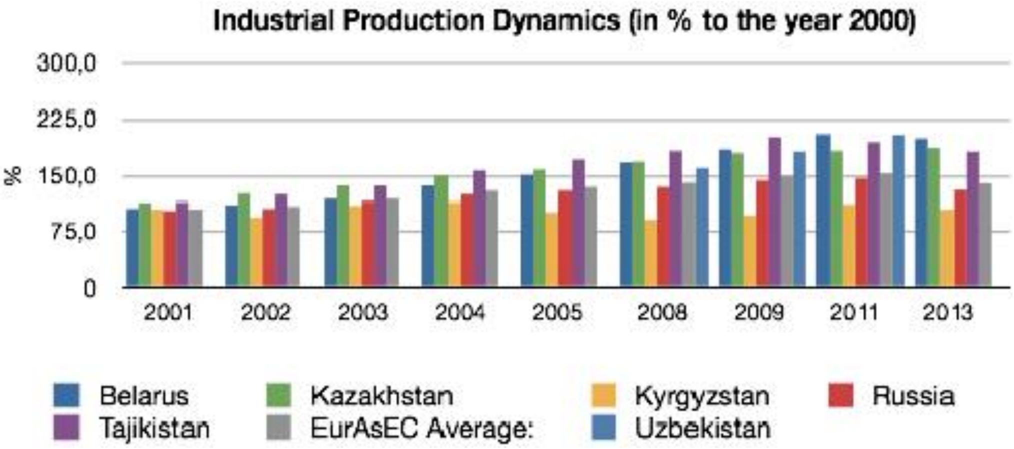


Figure 13- Industrial production dynamics in EurAsEC countries, 2000-2013 (in % to the year 2000)

Note - Compiled by the author based on statistical data collected from the of official website of the Eurasian Economic Community from http://evrazes.com/docs/statistics

The increase in the volumes of agricultural production was the most significant in Tajikistan . The production more than doubled in 10 years. In other EurAsEC countries the growth existed but was not as large. The graphical representation of the growth dynamics in agricultural sector is shown in Figure 14. According and Figure 14, in Kazakhstan agricultural production rose by 62%, in Belarus - by 52%, in Russia and Kyrgyzstan - by 34% and 28% respectively.

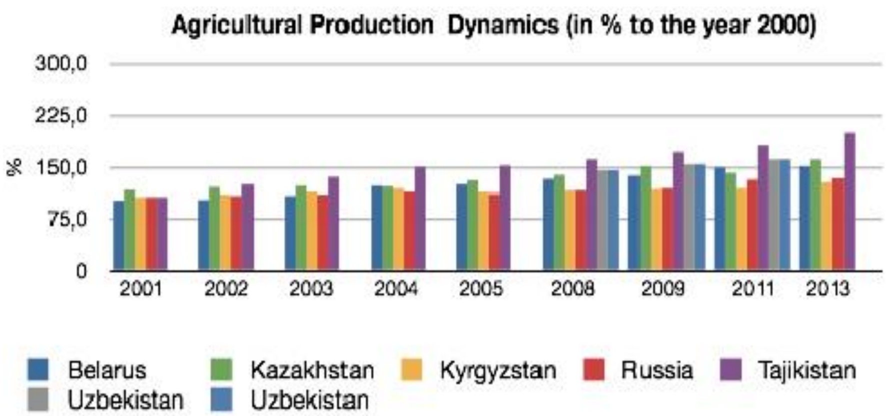


Figure 14- Agricultural production dynamics in EurAsEC countries in 2001-2013 (at fixed prices)

Note - Compiled by the author based on statistical data collected from the official website of the Eurasian Economic Community from http://evrazes.com/docs/statistics

It is interesting to observe the differences in the growth rates of investment in fixed assets in EurAsEC countries. In ten years since the agreement has entered into force, the volumes of investment increased 3,7 times in Belarus, 4,5 times in Kazakhstan, 1,6 times in Kyrgyzstan and 2 times in Russia.

However, due to the lack of information on investment volumes in Tajikistan and Uzbekistan, the average growth rate for EurAsEC equaled 134%. Figure 15 and 16 reflects the growth dynamics graphically.

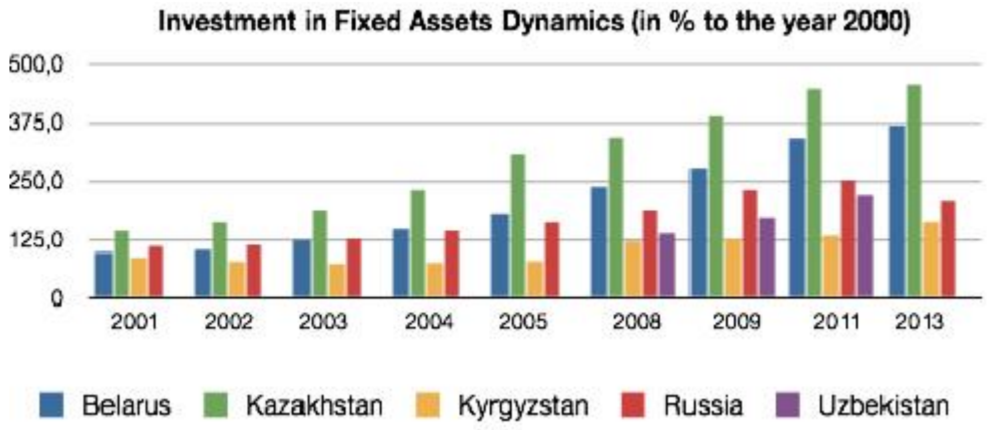


Figure 15- Investment in fixed assets dynamics in EurAsEC countries, 2001-2013 (at fixed prices)

Note - Compiled by the author based on statistical data collected from the official website of the Eurasian Economic Community http://evrazes.com/docs/statistics

Table 13 reflects the EurAsEC countries' budget deficit/proficit during 2000-2009 and Figure 12 gives a graphical representation of it. According to Table 9, the most stable growth in budget surplus was noticed in Russia. However, the budget went to deficit in 2009 after the crisis.

Table 13 - Budget deficit/proficit in EurAsEC countries in % of GDP, 2000-2012

Year	Belarus	Kazakhstan	Kyrgyzstan	Russia	Tajikistan
2000	-0,6	-0,1	-2,0	1,9	-0,6
2001	-1,6	-0,4	0,4	3,0	0,1
2002	-0,2	-0,3	-1,0	0,9	0,7
2003	-1,6	-0,9	-0,8	1,3	1,1
2004	0,04	-0,3	-0,5	4,5	-0,9
2005	-0,7	0,7	0,2	8,1	0,2
2006	1,4	0,8	-0,2	8,5	0,5
2007	0,4	-1,7	0,1	6,0	1,7
2008	1,4	-2,1	0,8	4,8	1,6
2009	-0,7	-3,1	-1,5	-6,2	-0,5
Source - compiled by the author based on statistical data collected from the official website of the Eurasian Economic Community from http://evrazes.com/docs/statistics					

In other EurAsEC member-countries the budget was fluctuating from surplus to deficit during the period of 10 years. No stable trend is observed. However, for the most of the years the budgets of the countries were in deficit, except for the Russian Federation.

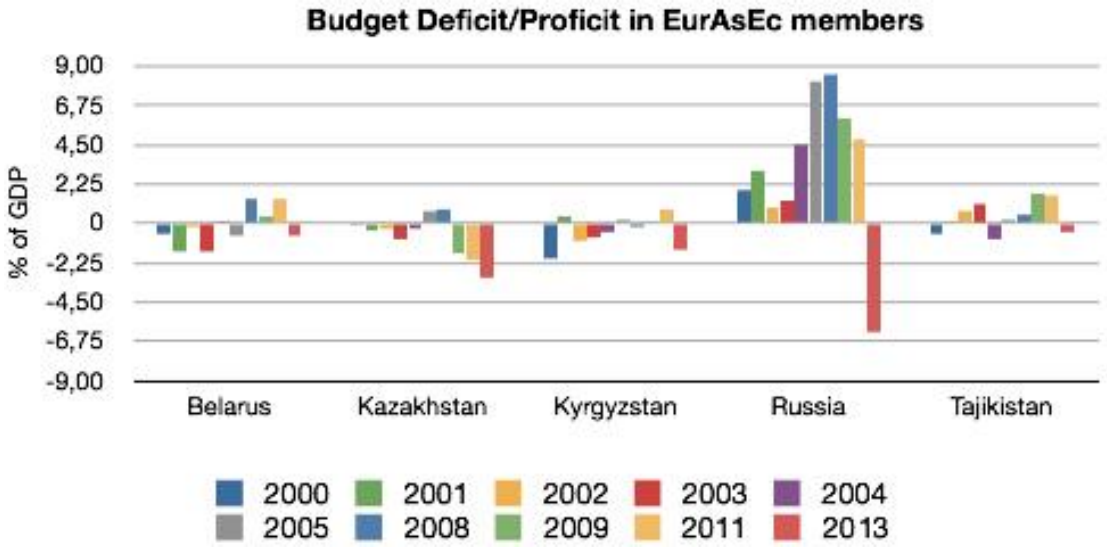


Figure 16-Budget deficit/surplus in EurAsEC countries, 2000-2013 (in % of GDP)

Note - Compiled by the author based on statistical data collected from the official website of the Eurasian Economic Community from http://evrazes.com/docs/statistics

It is essential to analyze the trade dynamics along with main economic indicators like GDP. Table 14 describes foreign trade in goods of EurAsEC countries in 2001-2013. According to Table 10, the following trend can be revealed: during the period from 2001 to 2011, before the onset of the global economic crisis, the volume of foreign trade operations increased in all countries, but after the crisis had fallen, due to difficult state of the economy of union members due after the crisis.

But, despite the decline in foreign operations due to the crisis, Table 14 shows that the mutual trade between countries of EurAsEC has grown 3 times in 10 years. According to Table 15, the highest volume of mutual trade was reached in 2008 - trade totaled to 122,6 billion of US dollars.

After the crisis in 2009 the mutual trade totaled to 79,2 billion of US dollars, but then rose to 95,2 billion in 2011.

The results of the given analysis should take into account the fact that in the outcome of main socio-economic indicators the share of participants is very different. Table 16 shows EurAsEC member countries' share in the results for the main socio-economic indicators in 2010. From Table 16 it becomes clear that in connection with the largest territory and population, the share of Russia dominates.

Table 14 - Foreign trade in goods of EurAsEC countries, 2001-2012, millions of US dollars

Country	Year	Export		Import		Foreign Trade Turnover	
		Total	with EurAsEC countries	Total	with EurAsEC countries	Total	with EurAsEC countries
Belarus	2001	7451,0	4017,0	8286,0	5472,0	15737,0	9489,0
	2008	32570,8	10992,4	39381,3	23695,4	71952,1	34687,8
	2012	25225,9	10407,2	34868,2	18475,6	60094,1	28882,8
Kazakhstan	2001	8639,0	2063,0	6446,0	3055,0	15085,0	5118,0
	2008	71183,5	7104,6	37889,0	14341,6	109072,5	21446,2
	2012	59216,6	5704,6	29760,0	11645,5	88976,6	17350,1
Kyrgyzstan	2001	476,0	161,0	467,0	241,0	943,0	402,0
	2008	1855,6	526,6	4072,4	1914,8	5928,0	2441,4
	2012	1759,8	731,7	3223,1	1525,6	4982,9	2257,3
Russia	2001	100060,0	8778,0	41884,0	6756,0	141944,0	15534,0
	2008	467580,6	38907,9	267100,7	17635,3	734681,3	56543,2
	2012	396441,7	30519,6	228953,4	14893,3	625395,1	45412,9
Tajikistan	2001	652,0	198,0	688,0	378,0	1340,0	576,0
	2008	1408,7	146,4	3272,6	1439,1	4681,3	1585,5
	2012	1195,2	135,7	2657,8	1210,9	3853,0	1346,6
EurAsEC Total	2001	117278,0	15217,0	57771,0	15902,0	175049,0	31119,0
	2008 (including Uzbekistan)	583428,0	61074,3	358016,9	61586,6	941444,9	122660,9
	2012	483839,2	47498,8	299462,5	47750,9	783301,7	95249,7
Source - compiled by the author based on statistical data collected from the official website of the Eurasian Economic Community fromhttp://evrazes.com/docs/statistics							

Another important indicator that should be analyzed is unemployment rate in EurAsEC countries, which is reflected in Table 17. As it shows, the best results are observed in Belarus and Kazakhstan, where unemployment decreased from 2,1% to 0,9% and from 3,7% to 0,6% respectively. In Kyrgyzstan unemployment rate did not show much change - it fluctuated around 3% in 2000-2007 and then decreased to 2,6% in 2009.

Table 15 - Mutual trade of EurAsEC countries, 2001-2012

Years	Billions of US dollars	in % to the previous year	in % to 2001
1	2	3	4
2001	31,1	102	100
2002	30,9	99	99

Continuation of table 15

1	2	3	4
2003	39,3	128	126
2004	56,0	142	180
2005	56,8	101	183
2006	77,1	136	248
2007	102,3	133	329
2008	122,6	120	396
2009	79,2	65	255
2010	95,2	120	306
2011			
2012			
Source - compiled by the author based on statistical data collected from the official website of the Eurasian Economic Community from http://evrazes.com/docs/statistics			

In Russia there was an increase of unemployment rate - it rose from 1,4% to 2,6% in 2004, then it showed a small decrease till rising again to 2,8% in 2009.

Table 16 - EurAsEC member countries' share in the results for the main socio-economic indicators in 2010 (value indicators at current prices as a percentage of the total for the community)

Country	Territory	Population	GDP	Industrial production	Agricultural Production	Retail trade turnover (all distribution channels)	Investment in fixed assets
Belarus	1,0	5,3	3,2	5,3	9,9	3,8	5,1
Kazakhstan	13,4	9,1	8,6	7,8	9,4	3,5	9,3
Kyrgyzstan	1,0	3,0	0,3	0,3	2,4	0,5	0,3
Russia	83,9	78,4	87,4	86,4	76,3	92,0	85,0
Tajikistan	0,7	4,2	0,2	0,2	2,0	0,2	0,3
Source - compiled by the author based on statistical data collected from the official website of the Eurasian Economic Community from http://evrazes.com/docs/statistics							

Thus, based on statistical data analysis, it can be concluded that integration within the framework of EurAsEC showed itself more effective for the more developed members of the union like Russia, Kazakhstan and Belarus. Though some positive growth was observed also in Kyrgyzstan, Tajikistan and Uzbekistan, their results in ten years were not as significant and large as in leader countries.

One of the reasons for such trend is the fact that EurAsEC member states have significant differences in the structure of national economies. So, Russia and Kazakhstan are major exporters of raw materials and at the same time producing an extensive product mix (the latter is particularly true for Russia).

Table 17 - Unemployment rate in EurAsEC countries in 2000-2009, in % on the end of the year

Country	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Belarus	2,1	2,3	3	3,1	1,9	1,5	1,2	1,9	0,8	0,9
Kazakhstan	3,7	2,8	2,6	1,8	1,5	1,2	0,9	0,7	0,6	0,6
Kyrgyzstan	3,1	3,1	3,1	2,9	2,9	3,3	3,5	3,3	2,9	2,6
Russia	1,4	1,6	2,1	2,3	2,6	2,5	2,3	2	2	2,8
Uzbekistan	...	...	...	...	...	...	0,3	0,3	0,4	...
Source - compiled by the author based on statistical data collected from the official website of the Eurasian Economic Community from http://evrazes.com/docs/statistics										

Belarus specialized in the production of finished products mainly from imported raw material, much of which comes from third countries. Uzbekistan, Kyrgyzstan and Tajikistan, lagging behind other EurAsEC member states in terms of industrial development and production are importing a large number of manufactured goods from foreign countries.

But at the same time, the functioning of EurAsEC has its drawbacks. There are factors that are harmful to the integration processes in the Eurasian Economic Community, in particular:

1. Lack of efficient mechanisms of coordination and implementation of the decision making process. To a large extent the integration is limited with the foreign trade direction, however, the situation changed with the creation of the Eurasian Development Bank, but to make a full-scale launch of project financing in its framework and their implementation will take time. Obviously, the effectiveness of the agreements implementation depends on the interest in this implementation, on the extent of how much the results of the negotiations comply with the interests of the parties.

2. The degree of coordination of EurAsEC countries' positions in the negotiations on accession to the WTO. A striking example of the lack of coordination among partners in the EurAsEC in relation to the WTO was a separate entry of Kyrgyzstan to the organization.

3. Multispeed integration. Important factor in this matter is the involvement into mutually beneficial projects that can result in a positive effect for member countries' economies. For example, the development of power industry in Kyrgyzstan and Tajikistan, the number of engineering industries in Uzbekistan, the solution of migration issues, etc.

4. Institutionalization of financial integration is facing the same problems as the integration initiatives in other areas: high-stated objectives achieved with a low level of formal interaction and weak conditions for its implementation. In respect to financial integration, these problems are even more important, because in the traditional scheme of the integration processes, it is one of the final stages of economic integration.

In order to solve problems related to the difference in the structure of the national economies of EurAsEC member states, the following actions can be taken: a joint work on aligning the priorities of developing the structures of the national economies, on holding a harmonized industrial policy, and on providing compensation from EurAsEC funds to reduce the losses of national budgets and individual producers, in the case of need to change the customs duties in industries, that are essential for the national economy development.

The past decade has clearly demonstrated the relevance and vitality of the Eurasian Economic Community, which has showed significant concrete achievements such as the establishment of the Customs Union of Belarus, Kazakhstan and Russia, the establishment of the Anti-Crisis Fund and the High Technology Center Community.

Summary for the second chapter

There are two essential features of integration processes that worth attention: 1) economic integration process that is often initiated by an abolishment of trading barriers comes along with establishing new trading barriers as a protectionist measure, and 2) integration process often unfolds between a core of relatively developed country/ or countries and usually smaller and/or relatively undeveloped periphery countries. Those two factors largely determine the character of the integration process.

We study a number of cases of past and current economic integration, namely NAFTA and EURAZES. All of them exhibit a number of common features. First of all, in an atmosphere of diverse (political, military, cultural) competition between the countries, economic integration of a number of countries almost always is a mean to compete against some other countries (There is one exception from this rule – an attempt to build a mono-polar world with a leading role of USA. More and more politicians and experts claim that this attempt failed and that we will end up in a multi-polar world.). In other words, economic integration of some countries often implies economic disintegration of some other countries: if a country establishes some new economic connections with another country, most likely it breaks some other economic connections.

The second important lesson to learn from real life integration experience is that, contrary to theoretical predictions, economic integration does not always improve the commonwealth of involved countries. Often periphery countries, such as external lands of Prussian Empire, or Mexico in NAFTA, suffer as a result of integration. The obvious culprits to blame are insufficient investments into the economies of periphery countries.

Appearance of new trading barriers or disappearance of old ones can act as a positive or negative factor for a particular firm, depending on the nature of its business, and on location of its subsidiaries and/or suppliers. For example, if exporting firm chooses to locate its producing facilities in the domestic country, protective policy in the country of its export would be a negative factor for the firm. However, if the firm places its producing facilities in the country of export, the protective tariffs are a positive factor for the firm. Consequently, when the firm has to make a strategic decision where to place its productive facilities, it should take into account the perspective of all relevant current and future integration processes.

Inequality of the integration process when we can point out the core and a periphery boils down to a situation where periphery economies have to go through much more considerable reorganization process than the core economy does. That means that periphery economies need more substantial investments into new capital, and into reorganization of the business. If on top of that periphery economies have undeveloped or sometimes even non-existing investment infrastructure, the firms of periphery economies have some considerable challenges to face. We study this question in details in the next Chapter. It focuses on the strategic challenges that stem from the frictions of the financial system: financial frictions and informational frictions.

3 STRATEGY IMPLICATIONS OF ECONOMIC INTEGRATION

3.1 Global restructuring of the economies as a part of integration process

Economic integration or globalization is a life changing process that brings considerable efficiency gains to involved economies. Those gains originate from two sources: scale economy, and specialization effect. Scale economy namely comes from the shire fact that almost all firms are bound to have some fixed costs. Mainly but not limited to, fixed costs comprise administrative costs. The definition of fixed costs naturally comes as a category that includes all costs that do not depend on the production level of the firm. Here we have to point out that there is a caveat. Strictly speaking, there are almost no costs that will not change if we increase our production level high enough. But if the increase of production level stays in some reasonable limits, a considerable group of costs do not change or change non-significantly. Let us approximately, for the sake of the model, announce such costs as fixed, and define them as F.

Alternatively, costs that depend anyhow, to a notable degree, from production level, could be defined as variable. Generally, the form of the function of variable costs with the production level as the explanatory argument could be pretty complex, but, for the sake of simplicity, we assume that the dependence has a linear form. Such an approximation could work pretty well for kind of costs like raw materials used for production of some tangible goods, for components used in an assembling process of the final goods and so on. However, even for this simple case the linear functional form is strictly speaking a simplification of the reality because of wholesale discounts. Other categories of costs could actually be far from linearity.

Nevertheless for the sake of simplicity of our model, admitting for a second that such a simplification would not lead us to any losses of generality of our approach, let as assume that all corporate costs could be categorized as fixed and variable (linear). Lets define the variable costs as V, and V=c*X, where c is the variable costs per unit of good, and X is the production level of the firm.

Then the total costs of the firm would be written as:

$$\text{Costs} = F + c*X \tag{1}$$

And total costs per unit of final good could be found if we divide Costs by X:

$$\text{Costs per unit} = c + F/X \tag{2}$$

Then for a firm with non-zero fixed costs, an increase of production level X would lead to a decrease of total costs per unit, see Figure 17:

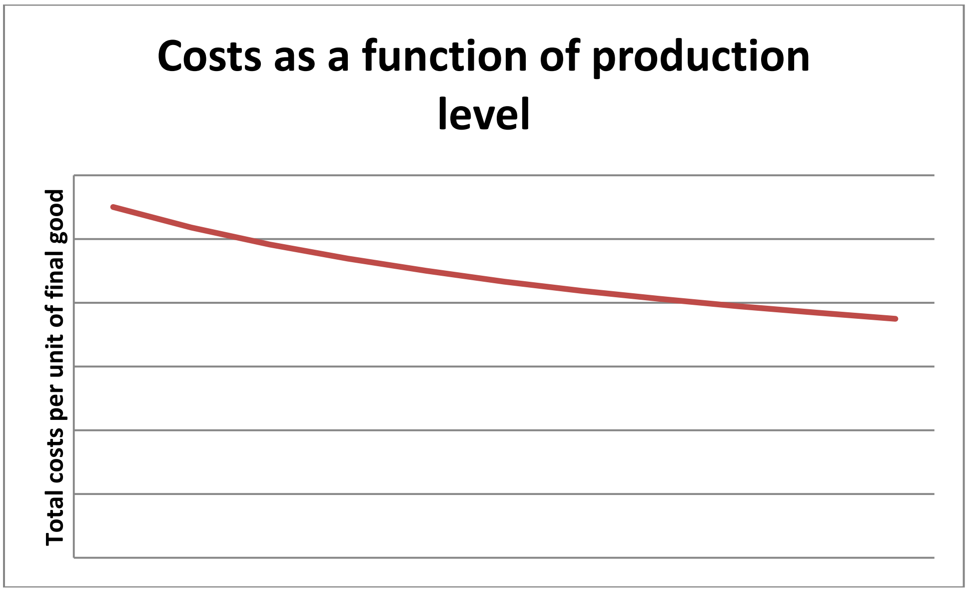


Figure 17 - Total costs per unit of final good as a function of production level

Note - the figure is developed by author

A decrease of total costs per unit of the final good would lead to an increase of firm profit per each produced unit of final good and/or a decrease of the sale price of the good. In other words, it will lead to gains of the firm and/or of the consumers, and to the achievement of a more efficient equilibrium.

One way such an increase of efficiency could be achieved is through the replacement of two (or more) small firms by a larger one. The optimizing replacement could be realized by a merger of smaller firms into a bigger one, or through a pressure of competitors and pushing out of the market inefficient firms. Different industries have different potential for a scaling up of their firms, and that potential depends on the ratio of fixed and variable costs. The higher the ratio of fixed costs to variable costs, the higher the potential for the firms to grow.

A good example of this could be the automaker market. One notable feature of this industry is that it has to do an extensive investment into research and development. Such investments come in two forms: (1) investment into new technologies, and (2) development of new models (basically combining the existing technologies inside a particular model of the car). Starting from the beginning and by 50-60-s years of the 20th century, low scale auto-producer innovators developed into a rather competitive industry with a total number of firms in the world more than ninety.

That situation was possible because the automobiles of that time were still relatively simple. Everything has changed after the oil crisis of 1973 started. High oil prices forced automakers to look for ways how to decrease the gas consumption of their cars. The solution was found with the invention of fuel injection systems. Those systems became possible after advances of microprocessor technologies.

Another important external factor that came into play around the same time was an increase of public attention to car safety. It turned out that to make a car safe, engineers had to design a protected passenger compartment, and flexible energy is absorbing zones in the front part of the car body. Such a task is a very complex one, and it usually involves a computer simulation with the help of powerful supercomputers. Those two new technologies, fuel efficiency and safety, became crucial for surviving of automakers, and their development demanded an extensive R&D investments. A continuous process of R&D investment into new technologies to stay in the business could be classified as fixed costs. A considerable increase of fixed costs in the automobile industry starting 80's years created a strong motif for scaling up of the size of corporations. As a result, carmakers started a wave of mergers.

R&D investments into new technologies were the first category of investments necessary for survival in a competitive automaker industry. The second category of vital investments was the development of actual car models. The design of the cars became more and more complex: increasing number of systems, and components, electric and electronic systems, automated controls, safety air bags, ABS and Traction control systems. All that complexity pushed the development costs of a new model up. At the same time, competition forced automakers to offer an increasing number of models, and different versions of each model, to satisfy all categories of buyers. If in 60-x carmakers offered mostly only three types of bodies – sedans, coupes, and wagons, in 70-x/80-x they introduced hatchbacks, mini-vans, and SUV-s. Increasing number of models forced carmakers to look for the ways how to decrease the model development costs. As a result, they come up with a strategy to market the essentially same model under different brands. For example, Volkswagen owns such brands as Audi, Skoda, Porsche. That strategy instigated a second wave of mergers, and by 2000s, they had only seven major car producers [90].

Along with improved efficiency, economic integration brings a variety of structural changes to the economies, and a vast literature focuses on different aspects of such changes. Economic integration contributes to differentiation of countries into industrialized core and agricultural periphery, as was demonstrated by Krugman (1991) [91]. Melitz (2007) showed that the integration affects both productivity and mark ups of companies involved into international trade [92]. Bernard, Eaton, Jensen, and Kortum (2000) apply an extension of Ricardian theory to explain basic facts about US plants [93]:

1) Productivity dispersion
2) The productivity advantage of exporters
3) The small fraction who export
4) The small fraction of revenues from exporting among those that do
5) Much larger size of exporters

They also examine the impact of various global shifts on productivity, plant entry and exit, and labor turnover in US manufacturing.

Helpman (2006) investigates the effect of international trade on organizational features, such as sourcing strategies, on trade structure, and on patterns of foreign direct investment [94].

One more of important aspects of economic integration that needs to be taken into account is custom tariffs. If we assume that markets function perfectly, then custom tariffs are just an impediment on the way of market forces. Tariffs just distort the production plans, and cause inefficiency. If we look into the concept of market efficiency, it usually comprises a number of conditions, all of which should hold, for the market to be efficient.

The concept of market efficiency dates back to 1900, the French economist Louis Bachelier formulated the ideas of the impact of past, present, and future events on the market price [95]. According to him, it was not possible to predict price changes. His work was based on the study of fluctuations of securities' prices on the stock exchange. More definitive interpretation was presented by the American economist Fama in 1965. It was expressed as "the market is effective if it adapts quickly to new information" [96].

The basic idea of the efficient market hypothesis is the rationality of investors, and the absence of information imbalance. This idea is often considered as one of the cornerstones of modern financial theory. The word "efficiency" in this case means the information, rather than operational efficiency: i.e efficient market - is a market in which prices reflects all known information. In an efficient market, it is impossible to get a real or economic profit, using available information for personal purposes [140].

In order to ensure the effectiveness of market information, it is necessary to satisfy four conditions:

1. Information made available to all market actors simultaneously, and receipt does not involve any cost.
2. There are no transaction costs, taxes, and other factors affecting the execution of the transactions.
3. Transactions made by a separate person or entity, may not affect the overall price level (market is competitive).
4. All market actors act rationally, trying to maximize the expected benefits.

Obviously, all four of these conditions are not satisfied in any real market: to obtain information requires time and money, some actors receive information earlier than others, there are transaction costs, taxes, etc. It means that free trade may not necessary promote the efficiency to the economy.

Nevertheless there are many authors who demonstrated empirically that free trade often promotes efficiency. Osang and Pereira (1996) explain the relationship between tariff structure, growth and welfare for a small, open country with endogenous growth induced by human capital accumulation [97]. Using a model with trade in consumption and two investment goods, authors consider the short- and long-run effects of a permanent unanticipated increase in the tariff rates under different replacement regimes, i.e. lump-sum transfer or investment tax credit. They show that most tariffs reduce growth, even in the short run. Also, all tariffs are welfare-reducing in the long run, but some may improve welfare in the short run. Starting from a uniform tariff structure, a revenue-neutral tariff reform may, therefore, increase growth and welfare in the long run. The structure of the optimal differential tariff varies, however, depending on the replacement regime.

If we want to study the cases when free trade is not the optimal policy choice, we should focus on the market deviations from efficiency.

The failure of the third component of the market efficiency concept, the imperfect competition, and its implications for the international trade were studied by Krugman (1979) [98].

Turkmen and Goksel (2012) study the violation of the second component for financial transactions. They show that financial constraints reduce the chance of exporting. It suggests that financial constraints are an important determinant of international trade patterns [99]. The results of research have important policy implications for countries suffering from relatively poor financial systems:

1. financial constraints act as trade barriers;
2. the largest amount of trade is between countries that have healthier financial systems in terms of access to loans;
3. financial constraints can cause zero trade.

Beladi andYabuuchi (2001) studied the failure of the first component related to the market efficiency: the free access to information [100]. They draw on the Harris–Todaro model and extend it to include an urban informal sector where the product of the informal sector is used as an industrial input in the urban formal sector [101]. They derive and contrast various welfare effects of tariff-induced capital inflow. Also, they analyze the welfare implications of employment subsidy as the policy instrument in the presence of international capital mobility.

Further we study the effect of protective tariffs in the presence of imperfect information. Rather than study the overall effect of protective tariffs, we limit the scope of our research questions to the effectiveness of protective tariffs in saving firms from bankruptcies.

3.2 Implications for management and importance of FDI

It should be noted that the activities of companies in the international division of labor is directly related to economic security and demonstrates the ability of the country with the free movement of products to produce them in accordance with the requirements of the world market. In recent decades, international competition literally took the global and world economic system, which is understood as a collection of national economies, and integrated them into the global markets, and so is becoming to be more and more clearly presented as a single geoeconomic system. This system is bonded by the feasibility communication in trade, monetary and financial regimes agreed between countries. Trends in the development of this system in the modern world are continuous processes of innovation in manufacturing, trade, finance and globalization of markets. Economic integration has become all-encompassing system that includes not only the exchange of raw materials and finished products, but also other stages of the reproductive process, such as production specialization, cooperative, and other forms of transnational linkages of national economies. Development of financial and economic relations , openness of national economies and their convergence cause strategic landmark development of Kazakhstan to be in the world economy not as a supplier of raw materials , and on the rights of economically developed countries with a high level of technological development, strong financial institutions, infrastructure and information sector . There are various theoretical mechanisms by which trade integration can provide benefits in terms of growth. Traditional trade theory emphasizes the link between trade liberalization and economic efficiency. Restriction of trade is distorting solution in consumption and production, leading to a misallocation of resources. Therefore liberalization usually leads to an increase in real income except, perhaps, when there are externalities or distortions already exist, or declining terms of trade exceed efficiency gains. For example , the authors of Anderson, Martin and van der Mensbrugghe [102] calculated that the full liberalization of trade in all countries of the world caused a rise in real incomes by about 0,5% of global GDP in 2015, about 30% of the growth in the category of developing countries. In addition, recent models of international trade and economic growth show how trade liberalization can lead to an acceleration of the dynamics. Greater openness to international trade may affect economic growth by making a wider range of products available for this country. Trade liberalization not only helps to increase the volume of existing products that are involved in the trade, it also allows the country to import and export goods new species [103]. Other channels through which trade liberalization may increase the growth rate of the country include:

- encourage the inflow of capital and labor (including FDI);
- increase the productivity of domestic enterprises by transferring new technologies;
- creation of dynamic externalities through the dissemination of knowledge.

The rationale for strengthening of regional operations is to overcome the limitations of the national organization in two ways: one, improve economies of scale and scope, thus achieving higher profits, and two, identifying and exploiting the opportunities of new market that emerged through the increased critical mass. In research on integration in the context of mergers and acquisitions (where is a similar focus on organizational configurations and changes and less attention to the managerial process of integrating), P. Haspeslagh and D. Jemison (1991) provide one of the few in-depth analysis of the integration process in mergers. They observed that an excellent execution of the integration process is crucial in achieving the potential synergies of the deal [104,105]. In the broader field of corporate strategy, there is a similar frustration with the lack of knowledge about change processes, despite the growing literature on corporate transformation broadly classifiable as restructuring, reengineering, renewal, and regeneration transformation processes.

Selection of right strategies in terms of integration depends mainly on the industry and market conditions. Regional economic integration suggests at least six implications for management (see figure 17).

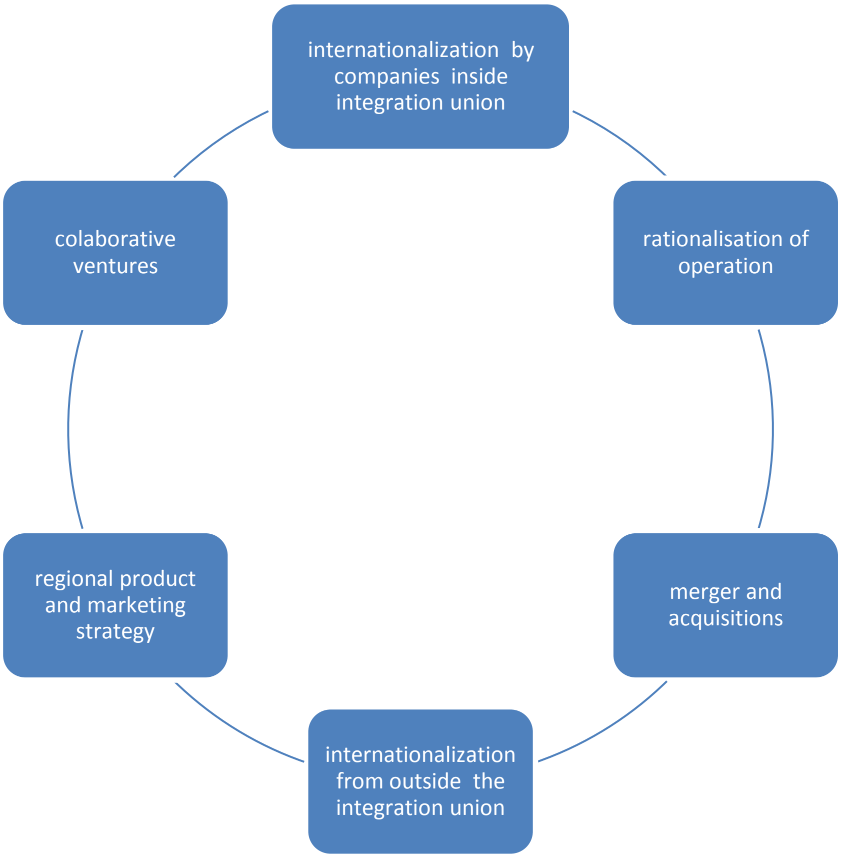


Figure 17 - Six implications for management

Note - Adapted from Saxena, "Principles of Management: A Modern Approach", 2009

Initially, regional integration presses or encourages companies to internationalize into neighboring countries within the bloc. The elimination of trade and investment barriers also presents new opportunities to source input goods from foreign suppliers within the bloc. By venturing into other countries in the bloc, the enterprise can generate new sales and increase profits. Internationalizing into neighboring, familiar countries also provide the enterprises with the skills and confidence to further internationalization to markets outside the bloc. For example, following the formation of NAFTA, many U.S. companies entered Canada and gained valuable international experience that inspired them to launch ventures into Asia and Europe.

Following the creation of an economic bloc, the importance of national boundaries will decrease. Instead of viewing the bloc as a collection of disparate countries, enterprises begin viewing the bloc as a unified whole. Managers develop strategies and value-chain activities suited to the region as a whole, rather than to individual countries. Rationalization is the process of restructuring and consolidating company operations that managers often under-take following regional integration. When an enterprise rationalizes, it reduces redundancy. The goal is to reduce costs and increase the efficiency of operations. For example, management may combine two or more factories into a single production facility that eliminates duplication and generates economies of scale.

Rationalization becomes an attractive option because, as trade and investment barriers decline, the enterprise that formerly operated factories in each of several countries reaps advantages by consolidating the factories into one or two central locations inside the economic bloc.

As an example, prior to the formation of the EU, many companies operated factories in European countries. After the EU's launch, these enterprises merged their plants into one or two European countries. Companies centralized plants in the EU locations that offered the lowest-cost operations and other competitive advantages. Thus, Caterpillar, the U.S. manufacturer of earth-moving equipment, was one of the many companies that shifted its focus from serving individual European countries to serve the EU region. Caterpillar undertook a massive program of modernization and rationalization at its EU plants to streamline production, reduce inventories, increase economies of scale, and lower operating costs. Companies can apply rationalization to other value-chain functions such as distribution, logistics, purchasing, and R&D. For example, following formation of the EU, the elimination of trade barriers, customs checkpoints, and country-specific transportation regulations allowed U.S. enterprises to restructure their EU distribution channels to make them better suited to the greatly enlarged EU marketplace. Creation of the trade union eliminated the need to devise separate distribution strategies for individual countries. Instead, the enterprises were able to employ a more global approach for the larger marketplace, generating economies of scale in distribution.

The formation of economic blocs also leads to mergers and acquisitions that is, the tendency of one enterprise to buy another, or of two or more enterprises to merge and form a larger company. Mergers and acquisitions are related to rationalization. The merger of two or more enterprises creates a new company that produces a product on a much larger scale. As an example, two giant engineering enterprises, Asea AB of Sweden and Brown, Boveri& Co. of Switzerland, merged to form Asea Brown Boveri. The merger was facilitated by regional integration of European countries in the development of the EU economic bloc.

The merger allowed the new enterprise, ABB, to increase its R&D activities and pool greater capital funding for major projects, such as construction of power plants and large-scale industrial equipment. In the pharmaceutical industry, Britain's Zeneca purchased Sweden's Astra to form AstraZeneca. The acquisition led to the development of blockbusters such as an ulcer drug Nexium and helped transform the new company into a leader in the gastrointestinal, cardiovascular, and respiratory areas.

Regional products and marketing strategy. Regional integration can also stimulate companies to standardize their products and services. Companies prefer offering relatively standardized merchandise in their various markets. The reason is that it is easier and much less costly to make and sell a few product models than dozens of models. The trade union facilitates the streamlining and standardization of products and marketing activities because in more advanced stages of regional integration the member countries tend to harmonize product standards and commercial regulations, and eliminate trade barriers and transportation bottle necks.

As conditions in the member countries become similar to each other, companies can increasingly standardize their products and marketing. For example, prior to EU unification, in order to comply with varying national regulations regarding the placement of lights, brakes, and other specifications on tractors sold in Europe, J. I. Case, a manufacturer of agricultural machinery, had produced numerous versions of its Magnum model of farm tractors. Where Case once produced 17 versions of the Magnum, the harmonization of EU product standards allowed the enterprise to standardize its tractor, allowing it to produce only a handful of models that were, nevertheless, appropriate for serving all the EU market.

Internationalization by enterprises from outside the bloc. Regional integration leads to the creation of large multicounty markets, which are attractive to enterprises from outside the bloc. Such foreign enterprises tend to avoid exporting as an entry strategy because economic blocs erect trade barriers against imports from outside the bloc. Accordingly, the most effective way for a foreign enterprise to enter the trade union is to establish a physical presence there via FDI. By building a production facility, the marketing subsidiary, or regional headquarters anywhere inside the bloc, the outsider gains access to the entire bloc and obtains advantages enjoyed by local enterprises based inside the bloc. As an example, since the formation of the EU, Britain has become the largest recipient of FDI from the United States. U.S. enterprises choose Britain as the beachhead to gain access to the massive EU market. In a similar way, European enterprises have established factories in Mexico to access countries in the NAFTA bloc.

Regional integration creates opportunities for cooperation among enterprises located inside of their own bloc. For example, following creation of the European Community, the precursor to the EU, enterprises from France, Germany, Spain, and the United Kingdom collaborated to establish Airbus Industries, a giant commercial aircraft manufacturer. The elimination of trade and investment barriers in the EU allowed Airbus to move aircraft parts, capital, and labor among the member countries from one factory to another. In a similar way, enterprises from the outside of the trade union also benefit from regional integration. Outsiders ease their entry into the bloc by entering joint ventures and other collaborative arrangements with companies based inside the bloc.

In 1990, there were approximately 50 regional economic integration agreements worldwide. Today there are some 200, in various stages of development. As the growth in world trade continues apace, nations want to be a part of emerging opportunities. Governments continue to liberalize trade policies, encourage imports, and restructure regulatory regimes, largely through regional cooperation.

Many nations belong to several free trade agreements. Economic blocs are joining with other blocs around the world. More nations are clamoring to join the EU, which has signed trade agreements with other economic blocs worldwide. Other intercontinental blocs are underway. Empirical evidence since the 1970s suggests that regional economic integration is not slowing the progress of global free trade. It is more likely that global free trade will gradually emerge as economic blocs linkup with each other over time. The evidence suggests that regional economic integration is gradually giving way to a system of worldwide free trade. During the opening of foreign trade enterprises are reoriented, i.e departure from the domestic market and international market entry. Orientation to the world market maximizes the pressure on the cost-effectiveness of local enterprises, which has a positive effect on the competitiveness and growth of the national economy. Trade openness maximizes both incentives and requirements for the reasonable trade [106].While, on the one hand, participation in foreign trade narrows the trading opportunities of governments (e.g., because of the participation in international agreements and the possibility of moving production). But, on the other hand, in the course of business, the importance of economic policy is growing. This disciplining effect of the external opening of the economy to economic policy leads to a better climate for economic growth and competitiveness in the country. A number of cross-country and panel regressions, in which attempts were made to separate the influence of various factors on the growth and find direction of causality, we found the evidence that openness to trade is closely linked to higher rates of economic growth [107]. This conclusion holds regardless of whether measured on the basis of openness of a country to trade policy (tariff and non-tariff barriers), or as the final result (the ratio of exports plus imports to GDP) . This relationship is even more pronounced when measured by GDP, and is not an absolute value and purchasing power parity, eliminating thus the impact of cross-country differences in the prices of tradable goods. However, neither the one nor the other measure of openness is sufficient. In the analysis of individual policies that restrict trade, there are serious problems. Low tariffs can mask restrictions aimed at key products. Non-tariff barriers are particularly difficult to measure. They can take many different forms: for example, discriminatory exchange policy that provides exporters with a higher exchange rate than the importers; uncertainty caused by the delay of customs clearance; contingent protection (the risk that the country will introduce restrictions on certain types of imported products in the event of a large influx of imports, for example, under the provisions of the anti-dumping and safeguard measures) . In protectionist purposes phytosanitary, sanitary and technical standards can also be used. The impact of such measures is extremely difficult to measure in quantitative terms [108]. Unfortunately, the second measure of openness - exports plus imports as a share of GDP - is equally imperfect. It reflects not only openness to trade, but also the level of economic development, geographical factors - distance from trading partners, and the possession of resources. Nevertheless, case studies support the conclusion that trade liberalization leads to faster development. Although the opening of the economy up to trade does not guarantee faster growth, all countries that have achieved significant economic progress over the past 20 years have included the liberalization of trade in their reforms. Two fundamental studies in 1978 analyzed the steps that the country experienced in the liberalization process, moving from import substitution to market-oriented trade policy (i.e. policy without anti-export bias). These studies described how the distortions caused by various protectionist measures distributed in the economy in mainly unplanned and negative consequences and showed how exports and economic growth responded to significant trade liberalization and appropriate macroeconomic policies. In this study, the World Bank analyzed the planning, implementation and the results of 36 liberalization programs in 19 countries from 1946 to 1986 showed that cases of effective and continuous liberalization are caused by rapid growth of exports and real GDP. Research carried out in 1999 showed that the number of countries with relatively closed economies that are those that have been the poorest in 1960 also had the lowest growth rate in the period from 1960 to 1985, however, a low initial income was not in correlation followed by a slower growth in open economies. In closed economies, low initial income reduces the potential economies of scale, but openness to trade, providing access to broader markets, allows us to overcome this problem [109]. Recent microeconomic studies describe a number of ways in which openness leads to higher productivity, including imports of machinery and equipment, which is usually accompanied by the transfer of know-how. Other studies have shown that import competition reduces profit margins and maximizes the levels of turnover and innovation. Empirical studies reveal a positive relationship between trade liberalization and economic growth, although with some exceptions. However, many methodological problems complicate any action to quantify the relationship between trade and growth, including the question of how best to measure the degree of openness to trade. These and other problems have led many authors, especially Rodriguez and Rodrick [110], who have questioned the reliability of empirical evidence linking trade liberalization and economic growth. As a rule, the impact of trade liberalization on economic growth depends on more general economic policy conditions. For example, trade liberalization is beneficial to the economy by reducing the price of imports. If prices in the economy cannot be freely varied, and resources (e.g., labor and capital) cannot move between industries, the economy will not use the benefits of liberalization to the fullest. Therefore, trade liberalization should be accompanied by policies that increase price flexibility and mobility of factors of production . At the same time, a significant part of the evidence of the impact of openness on growth can be criticized on the grounds that the effect of openness is not separated from the effects of a good institutional environment or other reforms, which are often carried out at the time. For example, in case studies and comparisons of "before and after" effects of trade liberalization it is difficult to disentangle from the effects of macroeconomic stabilization, liberalization of domestic prices , changes in the monetary system and the exchange rate , liberalization of the capital account , the reform of social protection systems , and many other measures . Today, the pace of development of trade, and, above all, exports in most countries outperform growth in industrial production, and GDP (see Table 18).

Table 18 - Growth rates of world industrial production and world trade, %

Indicator	1980-1990 y.	1990-2005y.	2007y.	2009y.	2010y.	2011y.	2012y.
World Industrial Production	3,1	2,3	2,5	5,0	3,5	3,0	5,0
Real GDP	3,3	2,8	3,6	4,9	4,4	5,0	4,9
World trade	6,1	5,9	5,4	10,7	7,6	9,2	6,8
Source -Compiled by the author based on data from the WTO							

According to statistical data export and import quotas are distributed unevenly in the GDP of the countries with high, middle and low-income countries. Thus, the export quota in Germany increased from 33.8 % in 2000 to 39.9 % in 2012 , in Japan - from 10.8 to 16.2 % in the U.S. decreased from 11.1 to 8.4 %, and Hong Kong (China) increased from 145.5 to 167.9 %, respectively. According to the WTO, the most open for this indicator are the economy of middle-income countries, particularly Malaysia, where the export quota in 2007 was 98.9 % (a decrease compared to 2000 by 25.5 %), while in China - 37.1 %.

In some low-and middle-income countries export-to-GDP ratio is higher than in countries with a high income. However, this is mainly due to the export of raw materials rather than manufactured products. The pace of development of foreign trade varies between different groups of countries. Growth rates of foreign trade of developing countries consistently exceeded the growth rate of trade in developed countries over the 1970-1980s. Then there is a slight lag in the pace of growth in developing countries from industrialized countries .

In the 1980-1990s the pace of development of foreign trade in both developed and developing countries has declined due to unfavorable market prices in the world market. Since 2001 the situation again is favorable for developing countries. According to the WTO in 2007, the growth rate of exports from developing countries amounted to 15.2% compared with 13.7 % in the industrialized countries of the world economy. Over the past two decades, and especially over the last few years, actively strengthen the integration of developing countries and emerging economies in the global economy. International trade in both goods manufacturing, and exchange goods became much more important to the economies of most of these countries. In general, commodity prices continue to play an important role in the economies of many developing countries, despite the fact that the current price boom brings rewards fuel exporters. However, the value of manufacturing exports to developing economies increased, especially with the sharp change in the situation in Asia, and on a smaller scale in Central and Eastern Europe and the CIS. Exporting countries, as stock and other products, expanded manufacturing exports in advanced economies, which remain the most important market for their exports, as well as in China and other Asian countries. Exports of commodities to China and other Asian countries also increased sharply, although to a lesser extent than manufacturing exports .

The modern state has a wide range of tools to solve the structural problems of economic development, problems of efficiency and balance of the national economy, trade flows of goods and they are steered in the right direction. Despite the fact that in a market economy, it would be logical to expect the prevalence of regulatory instruments economic resources (customs duties, taxes, etc.) and their automatic operation, the current trend of their application, in contrast, highlights the administrative (target, single) trade measures. This is due to, firstly, a significant decrease in the level of customs duties in the tariff negotiations in the GATT / WTO, which makes the lack of customs duties under the present instrument of protection acute monopolistic competition, and secondly, widely developed regional integration process usually begins with elimination of tariff restrictions in mutual trade . Non-tariff barriers to trade, by contrast, that have undergone a liberalization to a much lesser extent, are in the nature of direct constraints insurmountable economic way, i.e. on a competitive basis.

Numerous studies underscore the priority development of market institutions for successful economic reforms and its integration into the world economy, which should help to increase trade and attract foreign investments. Due to the liberalization of world trade value instruments open protectionist state regulation of foreign trade is reduced, but at the same time from the end of the XX century actively used tools disguised protectionism. Moreover, if the first process can be regulated at the supranational level, the second cannot .

In modern conditions of disguised protectionism, tools are more effective means of regulating foreign trade. Volumes and how to use them largely governed by national rules, which severely hampering these instruments from exporters. During its consideration of the evolution of the global trading system revealed the following modern trend: international trade is not only a liberal, but more regulated (controlled) as the interstate (supra) and at the national level. In some cases, this regulation restricts the free movement of products, in others - it promotes a certain way or organizes and arranges it. But regulated free trade as a protectionism is an intervention in the free market mechanism, free competition and in this respect is opposed to free trade in its classical sense. Therefore, at the present stage to speak not free, but the regulated (controlled) free trade, which is more relevant to the real forms of international economic relations, as in the modern world economy through foreign trade customs-tariff and non-tariff regulation in particular, relates to one of the most controlled areas of economic life.

Since the leading role in strengthening the position of national products on the world market is traditionally the export policy, one of the main objectives of improving competitiveness is to provide active support for foreign trade expansion of national producers. In recent years in most industrialized countries, the role of government regulation in the development of advanced industries, research and development activities and innovation strengthens. At the same time the government maximizes direct funding industrial R & D, expands the range of indirect methods of influence through the tax, tariff and credit system, supports the creation of new institutional structures on the basis of cooperation between government agencies, businesses and training centers. Development of the country and its regions depends on all elements of the market but primarily from the competition of enterprises. In this competitive advantage, enterprises are created and retained in close connection with the local conditions. Despite the globalization of the industry, the role of the country- and region-based company has recently increased, and the success of enterprises in competition with competitors is due primarily to the situation in the country and the region. International trade offers the great opportunities for developing countries to accelerate their economic development. First, they have to use their advantage in international competition in the production of labor-intensive goods and products that require large amounts of raw materials. However, in the process of economic growth, they also need to expand their skills in the production of capital-intensive products. Therefore, for developing countries an extensive development of the system of education is crucial. It is the only way most people can successfully participate in the development and the future to achieve international competitiveness and in the production of products with high technology content . In relation to developing countries, industrialized countries should not only promote the benefits of free trade, but also they behave accordingly. Closing their markets to agricultural and textile products from developing countries, as well as non-compliance with WTO agreements are contrary not only to their own rhetoric, but also have a negative impact on the ability of poor countries to develop.

3.3 Models of measuring the economic integration effect

3.3.1 Economic integration and social development: the case of the Eurasian Economic Community

Since Kazakhstan gained independence, the economy started developing rapidly thanks to its natural resources. Being one of the leading oil-exporting countries Kazakhstan accumulated large foreign investments. Therefore, the interest of other countries in Kazakhstan's economy has increased over recent years. The main fraction of exports deals with crude oil and minerals; however, the country now experiences a new non-resource oriented economic policy. As an emerging country Kazakhstan makes attempts to enter the modern world market and integrate to the world economy. Kazakhstan acquired huge territory situated in Central Asia, therefore, having no water roots which makes transportation costs high. Thus, Kazakhstan tries to maintain a friendly relationship with its neighbors because this made it possible to create and to enter the regional integration unions. Idea of Customs Union was realized in 2010. The Union was initiated and will be spread amount three member countries of Russia, Kazakhstan, and Belarus. Experts believe that advantages prevail and that Kazakhstan's economy, especially main economic agents, firms and households, will stand to gain.

Kazakhstan is about to enter the World Trade Organization (WTO) in the near future as some experts believe. However, whilst negotiations continue, Kazakhstan is waiting to be offered more appropriate conditions for membership. There are enormous disputes related to comparing advantages and disadvantages of entering the WTO. Policymakers, economists, experts publish reports on this issue, trying to prove that entering the organization is an integral part of becoming a globalized economy thus gaining benefits of world markets, by up-grading the technology, advancing industry, to reach high socio-economic level.

Albeit, Kazakhstan has several documents supporting economic reorientation from resource extracting to a resource processing direction, the crucial point being that Kazakhstan is still dependent on world resource prices. Therefore, the matter is to find an appropriate solution and exact suggestions for both micro and macro level. Economic integration is the process of complex transformation characterized by the intensification of the relationships between countries. Trade and economic integration remain the foundation for the majority of the existing integration schemes. During the last ten years, regional cooperation has been associated with the source of economic growth and development. From the result, the numbers of regional blocks have appeared in Commonwealth of Independent States (CIS) region. Most of them exist only on papers and are not in force in reality. Globalization is like an inevitable process that worried all nations. The reason for the arising nominal numbers of integration unions in CIS is by avoiding the dominating policies of developed countries above development. There are two faces of integration – one is to eliminate all barriers and create a common market. In this case smaller economies strengthen their competitive position with regards to large major economies. The second one is to protect the national interest and strengthen the position in the global scale. The contradictory character of integration brings misunderstanding of the meaning.

The number of integration unions as well as the world share of trade covered under them has been steadily increasing over the last ten years and this trend will be further strengthened by the many unions being proposed and those currently under negotiations. WTO data shows that Free Trade Agreements (FTA) accounted for 80% of all regional trade agreements notified and in force; Customs Unions (CU) agreements accounted 12% (Report WTO, 2006). However, most of the existing FTA gradually are transforming to CU, each fifth of FTA started to implement a common external tariff. These figures suggest that among the options available to countries today FTA became less popular and CU is the one that best reflects countries needs and objectives.

This raises the question of when an emergent, structure becomes relatively more sustainable, therefore less susceptible to disintegration. Integration processes are highly fluctuate. The choice of the right form of integration is the priority decision for cooperation between countries. Methodology of formation for economic integration includes the idea of transformation (Balassa, 1961), but there are not any guidelines about how to choose the appropriate type of integration. Thus, most of the integration unions were created by decision of the National Government.

We study the contra dictionary character of economic integration; one is as the product of Globalization and a measure to protect national boundaries. For both cases we are talking about formation of a Global competitive society. Extremely large groupings face the constant threat of losing member countries. Analysis of what constitutes a sustainable size for an integration grouping may be carried out from two angles. According to the traditional understanding, regional economic integration is the creation of an international union between several countries. In this case its sustainable size may correlate to the number of countries of an integration grouping or to the size of its population.

The second approach views an integration project as a network of agreements and accords reached by several regional countries (Libman, 2009). This approach is more flexible and to a greater extent reflects the reality of open regionalism models and tiered integration. In this case, we study integration process like a casual hypothesis between two links of Geopolitics and Economic Integration .

Geopolitics aspects include regional location of the country (size of the area, population, availability of natural resources), shorelines, and exit to other international markets. Thus, speed of Global society's formation depends on geopolitical aspect. State lands more actively participate in the integration process, whilst sea states change direction about cooperation more frequently. According to the duo pal theory (Zhan Tirarr, 1995) one of the advantages for countries is increasing land capacity. Current situation lets us conclude that each country, in terms of integration unions, is supposed to find economic welfare providing military power and political security [111].

We propose to analyze Integration like an open system. There is the presence of insiders and outsiders in each union. Insiders are members of the integration union; outsiders strongly tend to be members or countries have a strong relationship with members and sometimes have leverage on the integration processes. There are two types of the outsiders among countries:

- Potential members;
- Trade partners.

This system can be represented graphically by an internal and external elements 9see figure 18). Components of internal sub systems are country – members, initiating structure management of the community. External are potential members and trade partners. This open system cannot be stable or hold equilibrium position. At equilibrium, our system has maximum entropy and is incapable of self-organization. One of the important conditions of the system is synergetic providing development of each element.

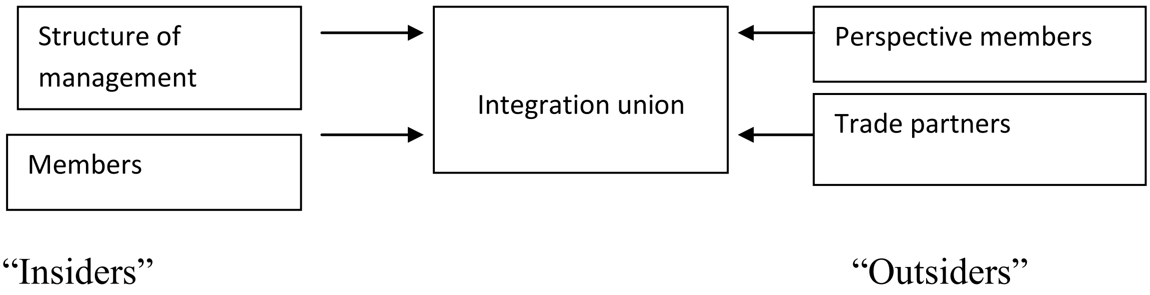


Figure 18 – System of Integration Formation

Note - compiled by author

The signs of economic integration system are:

- Number of internal and external elements;
- Dependence on environment that is not a part of the system but may change the situation inside of the union;
- Expanding era and formation of new common market.

We identify integration, as an objective process of development sustainable by economic relationship between economic agents (enterprises, firms, states).

Integration covers the sphere for production of goods and services for both the internal and the external market.

Internal integration represents cooperation of companies inside the country. External integration leads to the close interweaving of national economies with the creation of regional economic complexes. Very often external integration is a consequence of internal integration. Companies seek external markets when they have achieved success on the domestic market. There is a second way; companies tend to expand markets without horizontal integration on the domestic side. The efficiency of each policy depends on the level of companies competitiveness. The next classification focuses on the top down and bottom-up integration. The first one based on intergovernmental regulation. The second type based on FDI of TNC, existence of leading countries, high level of informal cross-border trade.

Economists have devoted their attention to the growth effects of economic integration. There are ongoing debates about criteria for successful integration and the relationships between membership in integration blocks and subsequent sustainable development.

Russian and Kazakhstani papers study integration through different criteria. Thus, effectiveness of integration is seen through the high economic growth while reducing the cost of inputs due to optimal utilization and increase the production . The intensity of the integration of relations is based on such indicators as the share of exports relative to the total volume of exports, the commodity structure of mutual exports, indicating the extent of specialization and cooperation, the absolute and relative values of the reciprocal and direct investment. Quantitative assessment of factors affecting the macroeconomic indicators of development, industry structure, investment potential and living standards. The coefficient of economic dependence on external relations reflects the change in the final production of the percentage change in the external relations at the 1%. Model of Russian economist Dvorkovich A. (2000) is based on the relationship between the level of GDP, state budget, investment flows and the state of foreign trade . Most of the Kazakhstani authors pay much attention to theoretical aspects of integration. The link between trade integration and economic growth has been emphasized by several authors as Edwards, 1993; Frenkel and Romer, 1999; Dollar and Kraay, 2001. First of all, technological change would be positively correlated with country’s openness. In fact, ”globalized” countries can either learn more quickly how to produce new inputs or can import them at lower costs increasing total factor productivity, human capital accumulation, and overall national technological capacity in papers of Grossmann and Helpmann, 1991; Romer, 1992. However, other authors do not pay much attention to the role and direction of causality between trade and growth [112]. The empirical evidence from the East Asian Newly Industrializing economies, revealed that the adoption by governments of high level of trade protection and interventionist industrial policies promoted growth through investment and technological learning. Trade protection could raise long–run growth according to the old infant industry argument if protection is accompanied by strong incentives and policies to enhance factor accumulation and investment in research and innovation.

Experts have long discussed the issue of Kazakhstan’s competitiveness in the global context, identifying that greater competitiveness leads to greater economic growth and material well-being and that growth always leads to higher incomes for all income classes, including the poor. However, emerging countries should be aware of particular socio-economic vulnerability that might appear due to global integration, particularly concerning the trade. The difficulty to drive simple empirical regularities linking trade liberalization and poverty is increased because is not easy to measure both indicators. This is not a marginal issue since results are strongly dependent on the measure of openness chosen, and the model specification used . A possible strategy is to directly identify the channels through which trade can influence development. To this aim, Winters (2000) fully explores the static effect of trade liberalization on poverty through four groups of institutions: enterprises, distribution channels, government and farm household [113]. Considering a change in the world price, tariff or exchange rate facing a single good, the effect of these shocks on poor households depends heavily on all the transmission channels and the behaviour of the agents and institutions. Winters pointes out some key points: trade shocks operate primarily via prices. If government policies prevent them the most direct effects on poverty (positive or negative) will be eliminated [114].

Another way in which trade may affect poverty is through taxes and government spending: if that trade liberalization causes falling tariff revenues, this in turn may reduce social expenditures and hurt the poor. Thus, trade liberalization may restrict the government's ability to manage spending and taxation in a way that worsens poverty.

At the same time, however, a number of other empirical papers argue that the trade was not important in the propagation of crises. Thus, Battacharya et al. (2001) show that trade linkages among East Asian countries only partially explain the propagation of crises. We try to take account of trade linkages using a slightly different approach [115].

We identified many articles related to the topic published by Montalbano (2004, 2005, 2009). The basic concept was to measure the relationship between trade liberalization and socio-economic vulnerability. The result was that the shock on trade openness directly reduced the resources available for private investment and consumption. The key point was that socio-economic well-being was worsening because of trade shocks that occurred at the beginning of the transition era, when observed countries were facing huge institutional and economic liberalization. Montalbano et al. (2004) outlined those countries with weak institutions and imperfect and incomplete internal market risk as being worse off from international competition and globalization. Federici et al (2007) noticed that the focus was to develop options and strategies to help developing countries capture benefits of trade integration minimizing the risk of negative shocks[116].

Montalbano (2009) proved that the issue of trade openness in terms of economic crises was becoming more crucial because openness raised the vulnerability to foreign shocks. The author provided several explanations to support the statement: "the notion that a weakening in a country's export performance can trigger a sudden stop in capital flows; the evidence that sudden stops in finance often extended to a loss in trade credit and that the resulting shrinkage in trade was more painful if trade represents a larger share of the economy; the empirical consideration that trade openness and financial openness go hand in hand in good and bad occurrences" (Montalbano, 2009) [116, p.12].

The IPALMO GDN Research Unit published Concept Paper (2006) titled “The Global Impact of Multilateral Trade Liberalization on Developing Countries” where authors suggested using the framework (see figure 19).

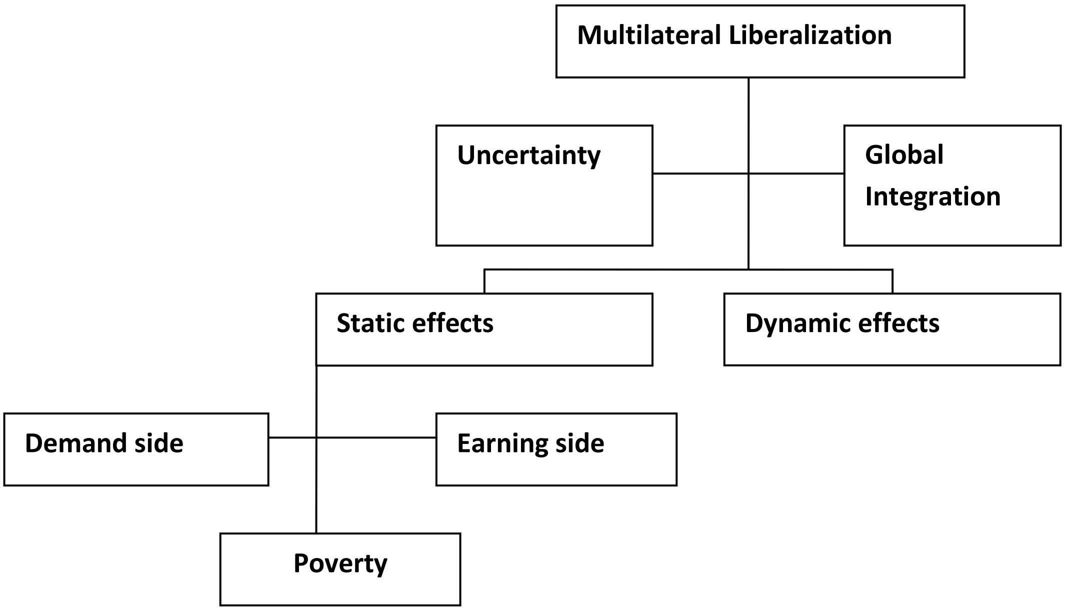


Figure 19 – The Model of Multilateral liberalization

Note - Adopted by Source: The IPALMO GDN Research Unit published Concept Paper (2006) titled “The Global Impact of Multilateral Trade Liberalization on Developing Countries”, p.4

The authors outlined that multilateral trade liberalization together with country’s global integration had the impact on income and welfare (static effects) and on total factor productivity (dynamic effects). The research stresses the methodology to use improved qualitative and quantitative data, to create empirical validation, strengthen the dynamic dimension, emphasize the role of vulnerability and uncertainty, and move towards effective integration of the macro and micro level analysis.

To carry out our social development analysis in terms of the integration union, we widened our measure of welfare, aggregating different aspects of the countries’ socioeconomic development into a single index. Idea of the single index was implemented for socioeconomic vulnerability analysis of shocks associated to trade openness by Triuzli U. and Montalbano P.

In the socio-economic context of Kazakhstan is considered as an emerging country with a transition economy. The World Economic Forum defined the stage of Kazakhstan’s development as a transition period by turning from factor oriented to productivity following. Therefore, the Global competitiveness index indicates Kazakhstan on 67-the rank; according to the Human Development Index (HDI) Kazakhstan is under a high human development ranking and acquires 82nd place in the world. The Global Peace Index which examines 23 quantitative and qualitative factors, starting from the level of military expenses to the rate of human rights respect. Besides this the index also represents the level of democracy, transparency, education, material well-being of the nation. Often the effect of economic integration is evaluated as an increase of wealth. However, utility functions of economic agents depend not only on wealth. For example it is a well known approach to define utility as a function of wealth and labor hours: U = U (w, L), where w – is wealth or wage, and L – hours of work. Another aspect that needs to be included into our consideration is the quality of life: Industrial development of countries due to integration sometimes involves personal risks related to ecology and conditions of labor. One way to improve the estimation of economic integration effect is to use an index including social development measures representing 1) working hours, and 2) the quality of life.

First time a similar aggregated index was introduced by Triuzli and Montalbano in their socioeconomic vulnerability analysis of shocks associated with trade openness. In this paper we suggest a new Social Welfare Index (SWI) that measures social development effects with 1) employment rate (as a measure of working hours) and 2) longevity and survival rate (as measures of the quality of life).

In our analysis we use the methodology of United Nations Development Program (UNDP) for Human Development Index (HDI) to de-unit and to normalize our sub-indexes [117]. Having defined the minimum and maximum values, the sub-indexes are calculated as follows:

$$x_{index} = \frac{x - min\,(x)}{max\,(x) - min\,(x)} \tag{3}$$

For the sake of simplicity, we use equal weights for each component. Our index of well being has been computed as:

$$\text{SWIti} = \text{wx1X1ti} + \text{wx2X2ti} + \text{wx3X3ti} \tag{4}$$

where SWIti is the composite index of socioeconomic development in period *t* and country *i*; *w* is the weight of each sub-index (chosen as 0.33); *Xjti* is a sub-index. Our sample includes all members of Eurasian Economic Community (EurAsEC) for the period 1995-2008 (see figure 20):

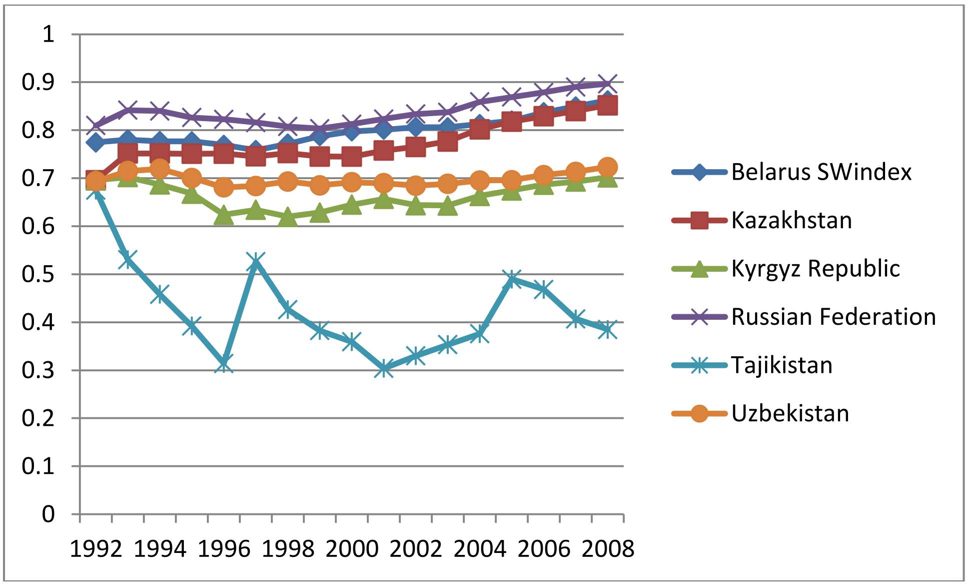


Figure 20 – EurAzEC's SWIs

Note - compiled by author

We assume the standard deviation of SWI gives us a measure of the volatility of well-being for each country in the period analyzed. While the SWI percentage rate of change of the period gives us a measure of the socioeconomic performance of each country over time and on average (see figure 21). We suppose that the comparison shows as level of volatility and worsening levels of well-being before EurAsEC and after.

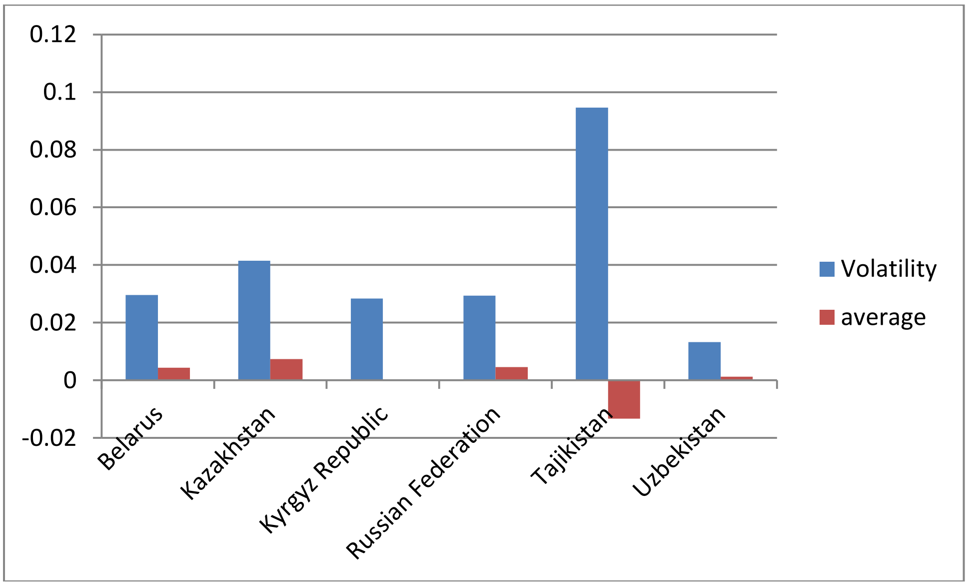


Figure 21 - A comparison between SWI volatility and average % rate of change of the EurAsEC (1992-2008)

Note -: compiled by author

The comparison supports the view that Tajikistan and Kyrgyzstan have experienced larger degrees of volatility and worsening levels of welfare during the transition period than other countries of EurAsEC.
We estimate a cross country OLS regression model in the following way:

$$SWIi = \beta 0 + \beta 1\ Tri. + \beta 2\ GGDi + \beta 3\ FDIi ++ \beta 4\ LPi\ \varepsilon i \qquad (5)$$

Where i = 1,…,N and N is the number of countries that enter the sample;
Independent Variables represent Integration.
- Tr is a trade terms ratio between Export and Import ;
- GGD – General Government Debt ;
- FDI – Foreign Direct Investment
- LP – Labor Productivity
The error terms εi are assumed to be uncorrelated with zero mean and
Var(εi) = σ2
After substantial testing using the variables, the regression results show some preferred model which are presented in table 19.

Table 19 – OLS Regression results for 6 EurAsEC for the period 1992-2008

Index	Coefficient	Std. Error	t-ratio	p-value	
const	0.611844	0.022225	27.5295	<0.00001	***
labour_producti	1.02457e-05	2.2636e-06	4.5263	0.00002	***
trade_ration	0.0236366	0.0160336	1.4742	0.14384	
ggd	-0.000297371	0.000131902	-2.2545	0.02654	**
Fdi	-0.00166177	0.000919636	-1.8070	0.07403	*

Mean dependent var	0.698938		S.D. dependent var	0.145448
Sum squared resid	0.139523		S.E. of regression	0.038943
R-squared	0.934700		Adjusted R-squared	0.928312
F(9, 92)	146.3212		P-value(F)	1.63e-50
Log-likelihood	191.5878		Akaike criterion	-363.1757
Schwarz criterion	-336.9259		Hannan-Quinn	-352.5462
rho	0.374689		Durbin-Watson	0.815283

Dependent variable: swi
Robust (HAC) standard errors
Test for differing group intercepts -
Null hypothesis: The groups have a common intercept
Test statistic: F(5, 92) = 91.6107
with p-value = P(F(5, 92) > 91.6107) = 3.52467e-034

Specification of the Model explains SWI as linear combination of the export / import ratio (trade relationship), the general government debt (public policy instrument), the foreign direct investment stock as a percentage of GDP , labor productivity . This model suggest positive correlation between labor productivity and social development, negative correlation between GGD, FDI and social welfare of the country and insignificant effect of trade openness and social welfare.

3.3.2 Effect of integration on the economic growth of member countries

A common measure of economic development of the country is a level of GDP. It is appropriate for the estimation of the current standing of the country. However, it tells nothing about the performance of the current government, and it doesn’t capture the dynamic aspect of the picture.

If we use growth of GDP . Instead, we can see the relative performance, but it is again not very indicative as a measure of government performance. Countries with low GDP level tend to show higher growth in comparison to countries with high GDP. For example, 5% growth is good for USA, and not that good for China.

S-Time measure that shows the number of years a particularly country falls behind its counterpart is similar to GDP level: it shows the relative standing of the countries. The advantage of this measure is that if we look at the change in S-times, we register the performance of the country in decreasing the distance between it and the leaders. That allows us to estimate the effect of economic integration on countries welfare.

We applied the S-time distance method as a tool of analysis. The method was developed by Pavle Sicherel (2006) [118]. The new approach offers new avenues for detecting additional information content, without replacing the existing views. If we choose to interchange in the database the roles of the level of the variable and time, a given level of the variable becomes a descriptor or identifier and time becomes a numerics in which certain distances between the compared units and time series can be expressed and measured.

B. Khusainov (2008) proposed to use this method to determine the effectiveness of integration. In his joint paper "A Study of Economic Change in the Eurasian Economic Community Using Time Distance Analysis" he tried to appreciate the difference (the time gap) between the Central Asian countries in comparison with Russia [119].

In this work, the S-time-distance analysis is used as a complementary method to analyze the effectiveness of integration in the frames of Eurasian Economic Community. The indicator that is chosen to compare the member countries of EurAsEC is GDP per capita. It represents purchasing power parity and is measured in current international dollars. As the period for comparison are taken 21 years from 1990 to 2011. First eleven years represent the indicator dynamics before the union was formed, and the rest represent either increase or decrease of GDP per capita after the agreement on EurAsEC has come into force. Time distance in general means the difference in time when two events occurred. We define a special category of time distance, which is related to the level of the analyzed variable. The suggested statistical measure S-time-distance measures the distance (proximity) in time between the points in time when the two series compared reach a specified level of the variable X. The observed distance in time (the number of years, quarters, months, etc.) is used as a temporal measure of variation between the two series in the same way that the observed difference (absolute or relative) at a given point in time is used as a static measure of variation.

We think that one rationale for using S-time distance is that it is more visual and graphic (and that part makes the work – popular oriented and political). It directly shows that e.g. Russia now is where Europe was 40 years ago.

Another rationale could be a simple model saying that all countries have the same potential GDP level H, and the speed towards that level depends on the distance to it: the far away, the faster it goes:

$$GDP(t+1) = GDP(t) + k(H\text{-}GDP(t)) + G(t) \quad (6)$$

It also depends on the government efforts G(t). If we compare growth of GDP of two countries – the growth of the one with smaller GDP would be higher – (think China and US)– and it is no the credit of Chinese government. Krugman writes about Asian miracle which is not really a miracle. From the model:

Growth (China, t+1) = GDP (China, t+1) - GDP(China, t) = k(H-GDP(China, t)) + G(China, t)

Growth (US, t+1) = GDP (US, t+1) - GDP(US, t) = k(H-GDP(US, t)) + G(US, t)

On Figure 22 there is a diagram that shows the dynamics of the GDP per capita in all EurAsEC member states. As can be inferred from the graph that all states participating in the integration can be divided into two groups - the leading countries along with the leader - Russia, and the lagging countries - Kyrgyzstan, Uzbekistan and Tajikistan. The EurAsEC average line distinctly separates these two groups of countries.

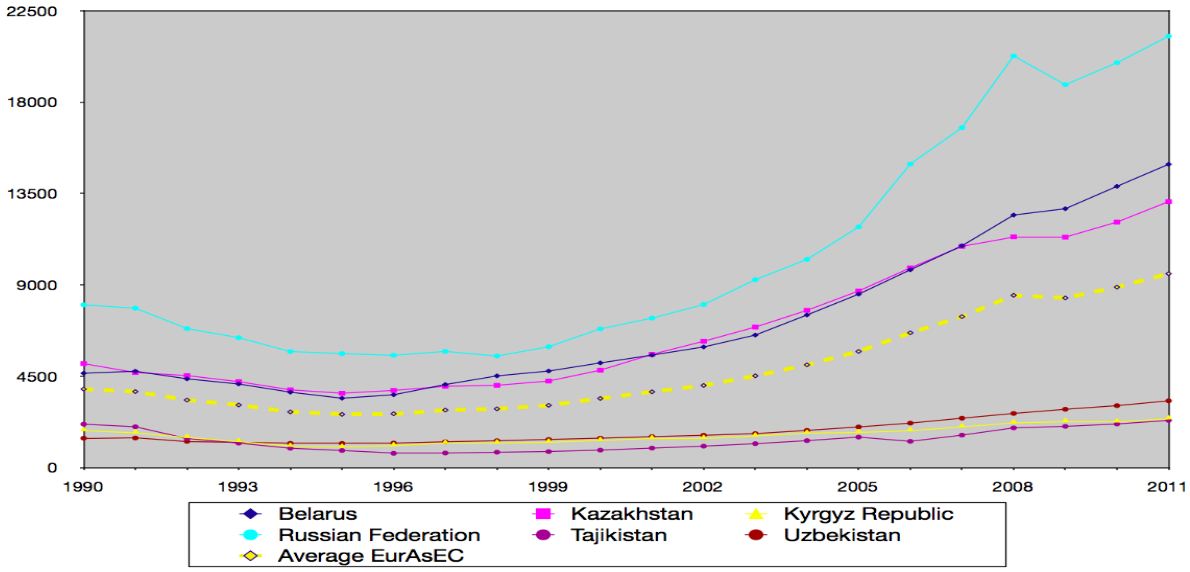
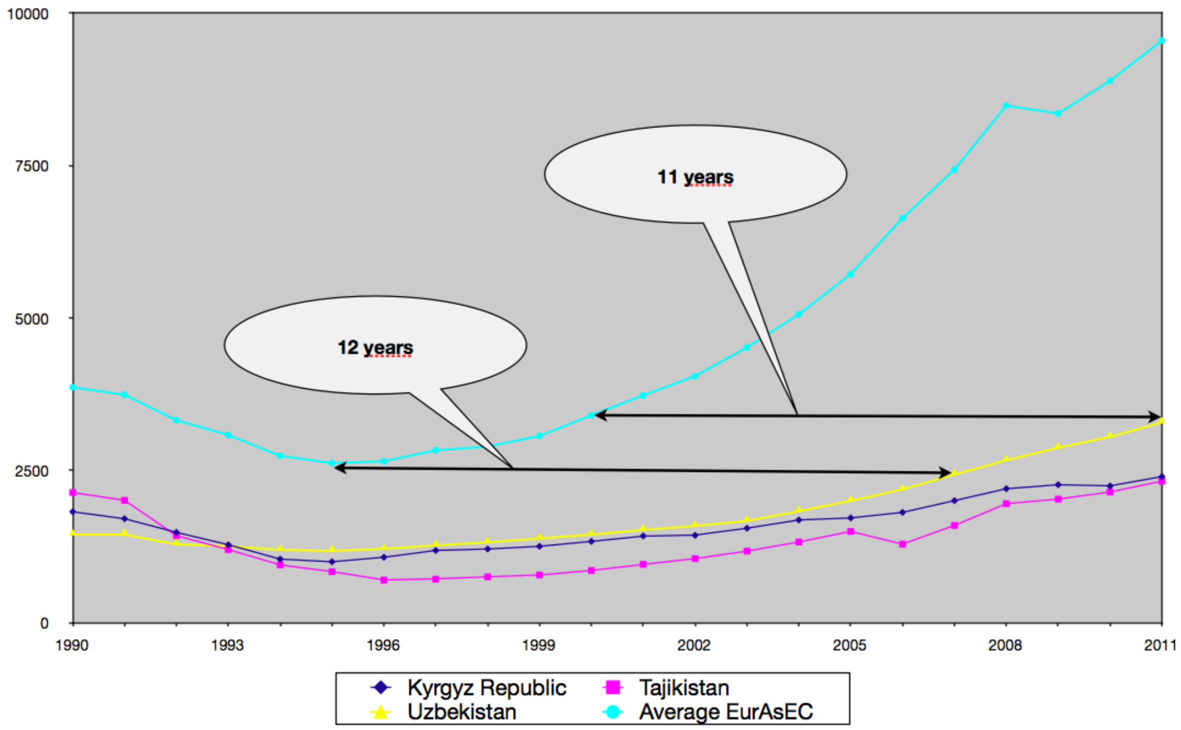


Figure 22 - EurAsEC countries' GDP per capita (PPP, current international $) in 1990-2011

Note - Compiled by the author according to the data from The World Bank from http://data.worldbank.org

Analysis for the three lagging countries and the average line. As it is represented in the graph, in 2011 the time distance that Uzbekistan is lagging behind the average has totaled to 11 years. It is just a small difference from a 2008 result, when the time distance behind the average line was 12 years. It should be noted that Uzbekistan out of three lagging states is the one that shows the most progressive GDP per capita dynamics.

However, Tajikistan and Kyrgyzstan do not show even that level of positive results. As is reflected in Figure 23, the time gap that Tajikistan is lagging behind the EurAsEC average line is exceeding 21 year. Due to the lack of data on Tajikistan's GDP per capita before 1990, it is hard to be sure if Tajikistan has ever reached closer to the average level throughout its independent history. Moreover, recently, due to the positive dynamics in the leading countries, the average line started to increase



significantly since 2003, and Tajikistan's time lag is increasing due to that fact.

Figure 23 - S-time-distance analysis of GDP per capita (PPP, current international $) in Uzbekistan

Note - Compiled by the author according to the data from The World Bank from http://data.worldbank.org

Kyrgyzstan is showing the GDP per capita growth that is much similar to the one in Tajikistan.

From the analysis it becomes clear that there is a big time gap in country development between the EurAsEC average and the lagging countries - Uzbekistan, Tajikistan and Kyrgyzstan.

For Uzbekistan this time gap is getting a little smaller, but the speed of the positive effect is not high enough. For Tajikistan and Kyrgyzstan the situation does not seem to get better over the years. In the period before and after the EurAsEC was formed the GDP per capita dynamics in these countries did not show many changes, especially not the ones for good.

In Figure 29 is represented an analysis of GDP per capita dynamics in Russia, Kazakhstan and Belarus using S-time-distance analysis. The graph shows, that while Kazakhstan's and Belarus's indicators are increasing approximately at the same level, Russia's dynamics is more lively and is increasing at a faster pace. If in 2005 Russia was 7 years ahead of EurAsEC average, in 2011 the time gap widened to 8 years.

Figure 24 represents the dynamics of GDP per capita in Kazakhstan. Right after the formation of EurAsEC in 2001, the time distance that Kazakhstan had ahead of the average GDP per capita result was 5 years. Than the gap decreased to 3 years in 2006 and widened to 5 years again in 2011. The Belarus dynamics is similar to Kazakhstan's as the two countries are fluctuating at the same level.

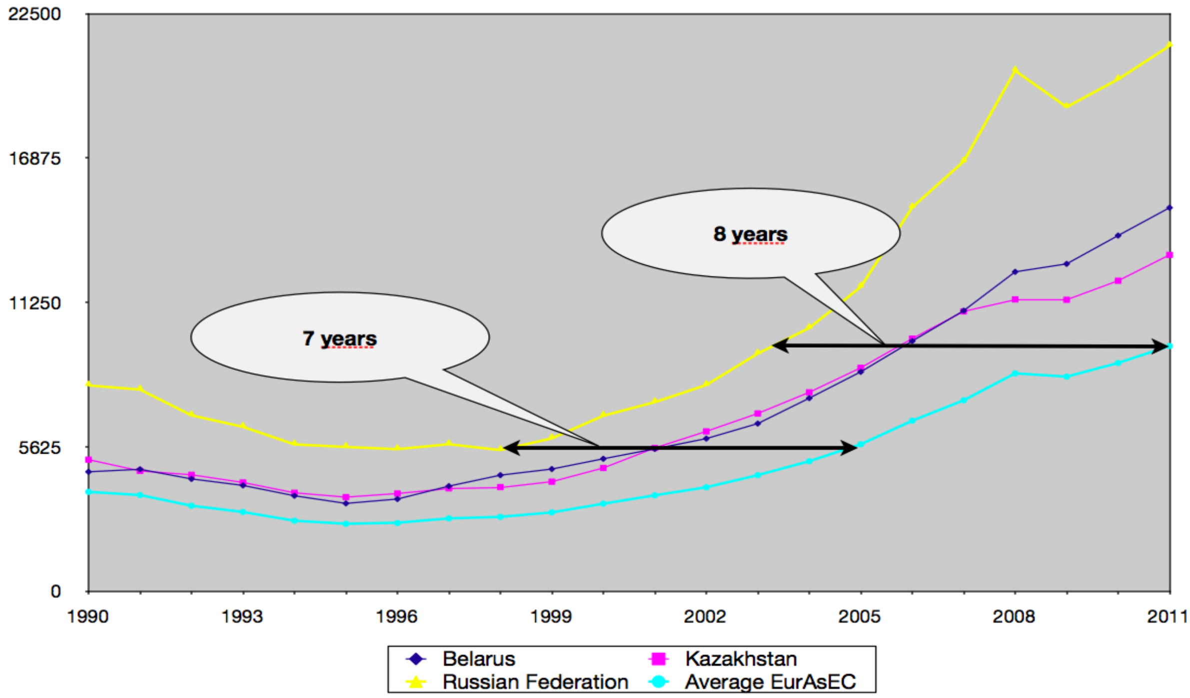


Figure 24 - S-time-distance analysis of GDP per capita
(PPP, current international $) in Russian Federation

Note - Compiled by the author according to the data from The World Bank from http://data.worldbank.org

Thus, the analysis tells that the time distance that Russia is getting ahead of the average result is getting bigger because Russia' GDP per capita is growing strongly in the last decade. By rising its GDP per capita, Russia is also rising the average level for all other member countries. Kazakhstan and Belarus are managing to fluctuate and grow above the average level, the time gaps they get ahead of the average line is fluctuating around 5 years. However, the lagging countries are not able to get anywhere close to the average level. The increase in the average level is only making the time lag wider. For Kazakhstan S-time-distance analysis of GDP per capita is shown on the figure 25.

As a result, by using S-time-distance analysis it became possible to get a new perspective on the EurAsEC integration. The carried analysis has again underlined the importance of one of the prerequisites for integration - integrating countries should have similar level of development of their economies. In EurAsEC case it becomes obvious that this prerequisite did not exist when the union was formed. This has complicated the process of integration as it has differentiated the integration effectiveness for the member countries. It can be confidently said that the integration within EurAsEC has shown itself effective for the leading countries - the results of the analysis show that. On the contrary, the effectiveness of EurAsEC for the lagging countries is still doubtful.

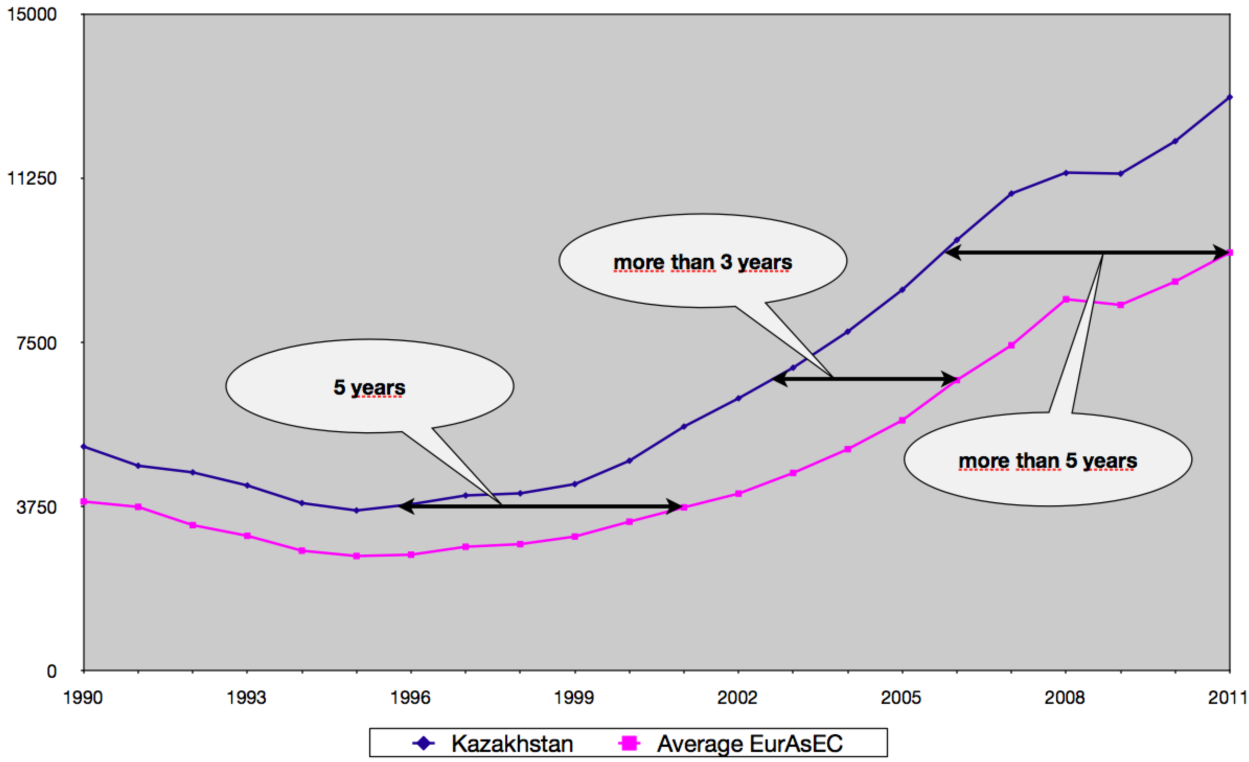


Figure 25 - S-time-distance analysis of GDP per capita
(PPP, current international $) in Kazakhstan

Note - Compiled by the author according to the data from The World Bank http://data.worldbank.org

Thus, one main conclusion that can be made from this analysis is that it was a good idea to deepen the process of integration only for three leading countries and to form the Customs Union only for Russia, Kazakhstan and Belarus. Their economic development is more or less comparable so there is a chance that their integration will prove itself effective and vital for further growth.

3.3.3 Financial and informational frictions and the effectiveness of protectionist tariff policy

In this part we study the implications of financial and informational frictions for the effectiveness of protectionist tariff policy. Even though it is a common view that free international trade brings economic efficiency, literally all countries use protectionist tariff policies as a part of government regulation. The argument of the positive role of free trade relies on the market efficiency concept (goes back to L. Bachelier, 1900, and advanced by Fama, 1965; Roberts, 1967; Malkiel, 1992) that comprises three main assumptions [120]:

1) Competitive markets;
2) No financial frictions (no fees, no taxes);
3) No informational costs and asymmetry.

Needless to say that all three of these conditions do not hold in any real economy. The effect of relaxing of the first assumption for modeling of international trade was studied by P. Krugman (1979). He focuses on the scale effect and shows that large enterprises may push smaller ones out of the market, and they gradually turn into a monopoly as a result of reliving tariff barriers. Developing a simple model of monopoly competition, P. Krugman showed the economic consequences of the phenomenon [121].

In this part we study the effects of relaxing second and third assumptions of market efficiency concept. Our first model is about the effect of information frictions. And the second one studies the effect of financial frictions.

Model 1: Informational uncertainty

The starting point of our model is that collecting of information is costly. Let us define these costs as informational frictions. The more information the firm wants to collect, the higher the costs. If we collect more and more information, at some point informational costs outweigh the value of the information. Practically it means that when informational frictions present, firms operate in an imperfect information setup.

It is natural to assume that informational frictions should have decreasing effect with the increase of the firm size due to scale effect. As a result quality of information should be lower for small firms.

Imperfect quality of information associates with direct and indirect costs for businesses. Indirect costs may come in different forms: for example, if we relate the quality of information with conservatism of accounting reports, it will affects agency costs that manifest themselves in the form of suboptimal bankruptcies, and risk shifting (Y. Loktionov, 2009) [122].

In our model we define quality of information as uncertainty about the future return of our investment, and consider costs that come from bankruptcy in the case when realized return lower than the reservation level. Let us assume that firm’s investments have a decreasing return to scale (formula 7):

$$r = r(I) \text{ s.t. } r'(I) < 0 \tag{7}$$

where I is the total investment into capital of all firms producing a particular good.

An entrepreneur doesn't know its future return to investment at the moment she initiates her business project. Instead she has an estimate of the future return which can be described as (formula 8)

$$r^* = r(I) + e \tag{8}$$

where e is a stochastic variable distributed normally (~N(0,a)) that represents a mistake of planning, and r(I) is the actual return.

The investment is fully financed by bank, so the benefit of the entrepreneur is the difference between the return generated by the business and the return that the firm pays to bank for using credit (reservation return):

Benefit = r(I) – rb

And perceived benefit is:

Perceived Benefit = r(I) + e – rb

The costs of the entrepreneur are her reputational (and maybe collateral) losses L that she bears in the case of firm's bankruptcy.

The entrepreneur tries to maximize her expected benefits net her expected losses by choosing if she invests into the project or not (formula 9):

$$\text{Max } E\{(r(I) + e - rb)dI - L\ \text{If}(\text{bankruptcy})\}$$

$$\text{or} \tag{9}$$

$$\text{Max}\{(r(I) - rb)dI - L\ \text{Prob}(\text{bankruptcy})\}$$

The first order condition for this maximization problem would look like (formula 10):

$$r(I) - rb - L \exp\frac{(-r(I) - rb)^2}{a^2} = 0$$

$$\text{or} \tag{10}$$

$$e = L \exp(-\frac{e^2}{a^2})$$

it is easy to show that the higher standard deviation of planning mistake a, the higher the equilibrium difference between average firm return and return of bank loan rb. Also the higher a, the higher the probability of bankruptcy.

Now let us consider a case when due to an external shock (like for example an introducing protective tariffs) return to investment increases from r(I) to r(I) + d.

We can show that decrease of probability of bankruptcy would be higher for firms with higher a.

It is natural to assume that a smaller firm has less precise planning in comparison to big firms. So all the above predictions based on difference of planning precision could be transferred to firms with difference in size.

If we focus on the moment of introduction of new protective tariffs then we should expect that all firms should demonstrate decrease in probabilities of bankruptcies. Our model tells us that small firms should exhibit higher decrease of bankruptcies than big ones. This effect could be tested: 1) directly through observation of bankruptcies, and 2) indirectly through profitability measures.

Hypothesis 1 would be then: an increase of the protective custom tariff reduces the number of bankruptcies among companies of the industry where the tariff was applied, and the effect is stronger for small firms.

Hypothesis 2 is: an increase in the protective tariff increases profitability of companies affected, and the effect is stronger for small firms.

Model 2: Financial Frictions

Here we study the effects of relaxing the second component of market efficiency concept: the absence of financial frictions. Following Diamond's delegated monitoring theory (1984), let us assume that a financial intermediary bears some fixed costs C associated with screening of potential borrowers. Let that cost be independent of firm size. Then the loan interest rate offered to a lender should include cost C in the following way (formula 11):

$$RL = rb + \frac{C}{I} \tag{11}$$

where the I is the size of the loan that coincides with the size of the investment, and rb is the net interest rate requested by the bank (here for simplicity we assume that the loan is risk free).

The entrepreneur initiates investment project if it's return (a function of investment) r(I) is greater than bank loan rate:

R(I) > RL or

R(I) > rb + C/I

We can show that a positive exogenous production shock (like for example introduction of protective tariffs), naturally leading to an increase of return, would cause stronger effect among small firms (formula 12):

$$\frac{dR(I)}{dI} = \frac{drb}{dI} - \frac{C}{I2} \tag{12}$$

for small firms and (formula 13):

$$\frac{dR(I)}{dI} = \frac{drb}{dI} \tag{13}$$

for big firms. Every other parameters equal, smaller firms will have a smaller sensitivity of the interest rate to investment. Consequently after an increase of custom tariffs, small firms would increase their investments more.

Hypothesis 3: an increase in the protective tariff leads to an increase in profitability, and the effect is stronger for small firms.

Model 3: Human capital effect with overlapping generation model

We extend the standard definition of market efficiency by including additional dimension of human capital. Thus, our definition includes four assumptions:

- competitive market;
- no financial friction;
- no informational asymmetry and frictions;
- and, on top of above three, no human capital frictions.

Our third model studies the effect of relaxing the fourth assumption of a frictionless human capital flow. Let us define human capital as a combination of information, know how, skills, expertise, organizational structure, and all the other elements of corporate culture which allow to exploit labor and physical capital in a more efficient way: for example, to produce a product of comparable quality but at lower costs or to produce a product of supreme quality at similar costs as competitors without human capital do. Due to the competition, the projects with higher level of human capital are the ones which will more likely succeed.

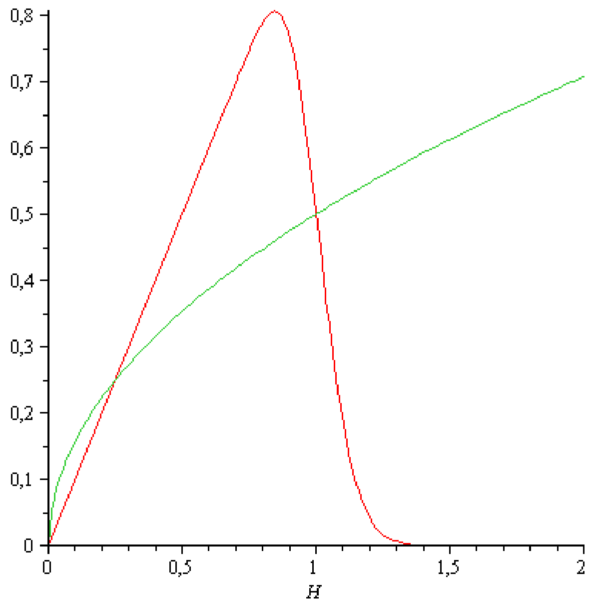


Figure 26 - Human Capital accumulation and destruction

Note - Constrain by author

As we can see from the figure 26 green color is accumulation, red is destruction. The low equilibrium is stable. When green above red human capital accumulates faster until the steady state is reached. When green below red human capital is destroyed faster until H falls back to the steady state. When exogenous shock moves the human capital stock so that H>1 the economy enters a new growth path: green always above red, i.e. human capital grows indefinitely.

We define the amount of human capital with a scalar parameter $H_{i,t}$, where i is an identificator of a project and t – is a time period, and I model the relation between the survival probability and human capital as a linear function (formula 14):

$$P(survival)_{i,t} = a + bH_{i,t}, \tag{14}$$

Where a and b are constant parameters.

Then we assume that every time period t, N entrepreneurs start one business project each, and if the business project is successful, it lasts one time period, and then the entrepreneur retires and terminates the business at time t+1. At the moment of establishment, human capital of each firm comes from two sources: random endowment of the entrepreneur, z_{it}, and spillover effect - human capital that comes from all existing firms that were established last time period (formula 15):

$$S_t = k * H_t^{\Sigma} = k \sum_{i=1}^{N} \{H_{i,t-1} * 1(if\ survives)\} \tag{15}$$

where k is the share of human capital transferred, and H_t^{Σ} is the total amount of human capital in the economy. So the human capital of a new firm is (formula 16):

$$H_{t,i} = z_{t,i} + S_t \tag{16}$$

The expected amount of total human capital in the industry at time t+1 is (formula17):

$$E(H_t^{\Sigma}) = N * E\left(H_{i,t-1} * 1(if\ survives)\right) = N * E\{H_{i,t}(a + bH_{i,t})\} =$$

$$= N * E\{(z_{t,i} + S_t)(a + b(z_{t,i} + S_t))\} \tag{17}$$

If the economy is at equilibrium, then (formula 18):

$$E(H_t^{\Sigma}) = H^* = N * E\{(z_{t,i} + kH^*)(a + b(z_{t,i} + kH^*))\} \tag{18}$$

The equation is a quadratic equation in respect to H^*, which implies that the system has two stable equilibriums: with low and with high levels of human capital H^*. If the system starts from low level of human capital it may stuck in the suboptimal equilibrium point without external help. Such help can come in a form of protective tariffs which increase the probability of business projects to succeed, and accelerate accumulation of human capital.

Empirical Tests:

Hypothesis 1

Protective tariffs decrease probability of bankruptcy. Hypothesis 1 says that this effect should be stronger for small firms. To test this formally we estimate a probit regression, where the dependent variable is a dummy DM(Bankruptcy) that equals to 1 if firm is a bankrupt, and 0 otherwise (formula 19):

$$DM(Bankruptcy) = a0 + a1\ gt\text{-}1 + a2\ controls + DM\ (b0 + b1*Size) \quad (19)$$

Explanatory variables should include dummy DM that equals to 1 if the government chooses protective tariff policy, and 0 otherwise. We are interested in the coefficient b1 for the interaction term between dummy DM and Size (Size is a proxy for size of the firm). Hypothesis 1 implies that coefficient b1 should be positive.

Hypothesis 2

Protective tariffs increase profits of the firms. Hypothesis 2 predicts that this effect should be stronger for small firms. We test hypothesis 2 with the help of OLS regression equations (formula 20):

$$Profitt = c0 + c1\ controls + DM(d0 + d1*Size) \quad (20)$$

Where DM is a dummy variable equals to 1 if the protective policy is chosen, and 0 otherwise. Hypothesis 2 tells us that the coefficient d1 for the interaction term should be negative.

Preliminary empirical results

We composed our data sample using Compustat yearly database. It contains about 3000 financial reports of firms working in or closely related to steel industry. The time span of the sample is from 1985 till 2012. The main variables of our interest are: 1) dummy that shows that firm declared bankruptcy (DM(bankruptcy)) and 2) profitability of the firm (profitability).

DM(bankruptcy) equals to 1 for the record that is the last for the firm (unless it is year 2012 – the last year of our database). Otherwise DM(bankruptcy) equals to 0.

Profitability of the firm for year t defined as a ratio of earnings before taxes and interest payments at time t to total assets at time t-1.

As control variables I use size, growth of assets, and dummy for protective tariff policy DM. Size at time t is calculated as a logarithm of total assets at time t-1. Growth of assets at time t is calculated as a logarithm of the ratio of total assets at time t to total assets at time t-1.

Our hypotheses imply the diversity of firms' behavior across the size dimension. Consequently it is important to have notable variation of firms' size in our sample. As we can see our from Figure 27, the smallest companies have total assets starting from exp(-3) and big companies go up to exp(15). I.e. our sample is quite diverse in terms of size.

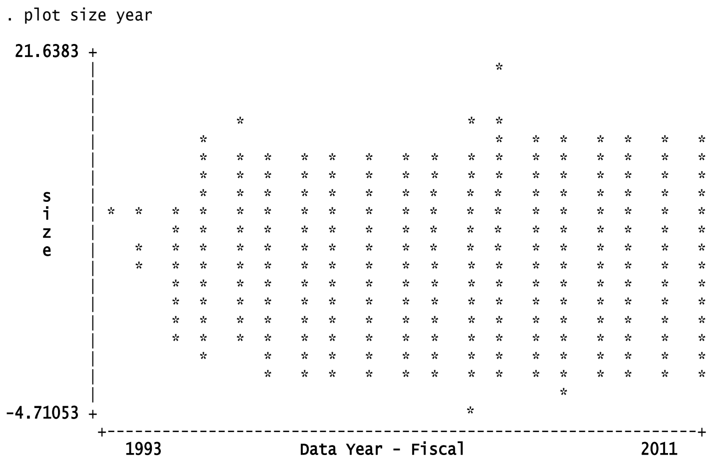


Figure 27- Distribution of companies according to size across the years

The results of the tests of hypothesis 1 (equation (1)) presented in the table 1. The regression coefficient for the Size proxy is negative, and is not significant, which implies that big companies are less likely to go bankrupt, but that result is not reliable. The loading for the interaction term DM*Size is positive and statistically significant: when companies are protected with tariffs they are safer, and this effect is stronger for small firms. It confirms the hypothesis 1.

Table 20 - Probability of bankruptcy and the size of the firm: test of the protectionist policy effect. The table demonstrates the outputs of a profit regression (coefficients, and p values)

Name of the variables	Regression coefficient and p value
Size	-0.017 (0.19)
DM*Size	0.13* (0.018)
Year Dummy	+
Constant	-5.87** (0.00)
Number of observations	4654
R2	0.064
* 5% significance level **1% significance level Note- Estimated by author	

The results of the tests of hypothesis 2 (equation (2)) are shown in the table 20 and 21. Here the regression coefficient for the size proxy is positive and statistically significant. It means that big rims have on average higher profit in relation to their total assets. The regression coefficient of the interaction term DM*Size is negative and statistically significant: when protective tariffs are introduced, the difference in profitability between big firms and small firms gets smaller. It supports the hypothesis 2 prediction.

Table 21- Profitability and the size of the firm: test of the protectionist policy effect. The table demonstrates the outputs of a profit regression (coefficients, and p values)

Name of the variables	Regression coefficient and p value
Size	0.035** (0.00)
DM*Size	-0.009* (0.02)
Year Dummy	+
Constant	-0.45 (0.1)
Number of observations	4944
R2	0.19
* 5% significance level **1% significance level	

As we can see from the results of empirical tests, both hypotheses, 1 and 2, are confirmed.

If we relax the assumption of perfect market concept about either 1) financing without frictions or 2) information without frictions, we can show theoretically that small firms would react stronger for protective tariff policy. They exhibit a stronger decrease in risk, and a stronger increase in profitability. These predictions find some empirical support.

Summary for the third chapter

Besides the increase of uncertainty, economic integration necessitates considerable capital investments. Both of two factors, the increase of uncertainty and the need of large investments, put a notable strain on financial system, and can be a reason for financial system to stop working properly. In other words, when economic integration is initiated, frictions interfering with financial markets become a major factor for the choice of firm's strategy.

This manuscript outlines two groups of frictions: informational and financial. For each group we suggest a theoretical model that looks into the cross-sectional difference of the friction effect between small and big firms. In both cases models predict that 1) frictions are a more important factor for small firms versus big firms, and, consequently, 2) small firm performance is more sensitive to the change in protectionist policy by the means of international trade barriers.

We also study the long term effect of protectionist policy by composing a theoretical model of human capital accumulation. Our model predicts that for a small firm industry in the long run protectionist policy could lead to a superior equilibrium. That result could serve as a basis for policy recommendations designed to achieve a socially desirable outcome.

To support our theoretical findings we test empirically the predictions of our "financial market friction models" (FMF). For that we investigate a natural experiment in USA steel industry. In 2001 USA government introduced protectionist tariffs to support its steel producers. I studied the response of the industry to this positive shock. Our empirical findings indicate that profitability of small firms responded stronger to the protectionist measures than profitability of big firms. Also we discovered that risk of small firms decreased to a higher degree than risk of big firms did. All findings support both of my FMF models.

Relying on both, our theoretical and supporting empirical findings, we conclude that small firms should consider the change of government protectionist policy as a major factor for their choice of strategy. Particularly they should a) reserve necessary resources to respond to the protectionist policy shock, and b) lobby the government protectionist policy (for example through establishing of industrial associations).

CONCLUSION

The results of theoretical and practical research, detected the main functions of the companies in terms of economic integration.

1. Strategic development is a long-run actions of the company to achieve its goals under the influence of external environment. To these factors we have referred such factors are financial and informational frictions and trade regime. The special case of strategy that worth special attention in relation to economic integration is the expansion strategy. Economic integration, and particularly, the change in trade policy, leads to an expansion of the market, increased competition, and investment flows. These factors motivate firms for the development of strategies adequate for the new external challenges, and the opportunities for companies to expand activities.

2. This work contributes to the development of strategic literature. Particularly we focused on the strategy decisions of the firms in integrating economies. There are two important features of the integration processes that are worth our attention: 1) economic integration process that is often initiated by the abolishment of trading barriers comes along with the establishing of new trading barriers as a protectionist measure, and 2) integration process often unfolds between a core of relatively developed countries and usually smaller and/or relatively undeveloped periphery countries. These two factors largely determine the character of the integration process.

3. Appearance of new trading barriers or disappearance of old ones can act as a positive or negative factor for a particular firm, depending on the nature of its business, and on location of its subsidiaries and/or suppliers. For example if an exporting firm chooses to locate its production facilities in the domestic country, than a protective policy in the country to within it exports would be a negative factor for the firm. However, if the firm places its production facilities in the country of export, the protective tariffs are a positive factor for the firm. Consequently, when the firm has to make a strategic decision where to place its production facilities, it should take into account the perspective of all relevant current and future integration processes.

4. Inequality of the integration process when we can point out core and a periphery countries boils down to a situation where periphery economies have to go through considerable more reorganization process than the core economy does. That means that periphery economies need substantial more investments into new capital, and into reorganization of the business that core economies. If on top of that periphery economies have undeveloped or sometimes even non-existing investment infrastructure, the firms of periphery economies have considerable challenges to face.

5. The thesis focuses on the strategic challenges that stem from the frictions of financial system. In more details, we study financial and informational frictions.

We study a number of cases of past and current economic integration, namely Prussia, NAFTA, and EurAsEC. All of them exhibit a number of common features. First of all, in an atmosphere of diverse (political, military, cultural) competition between the countries, economic integration of a number of countries almost always is a mean to compete against some other countries. In other words, economic integration of some countries often implies economic disintegration of some other countries: if a country establishes some new economic connections with another country, most likely it breaks some other economic connections.

6. The second important lesson to learn from real life integration experience is that, contrary to theoretical predictions, economic integration not always improves the common wealth of involved countries. Often periphery countries, such as external lands of Prussian Empire, or Mexico in NAFTA, suffer as a result of integration. The obvious culprits to blame are insufficient investments into the economies of periphery countries.

7. A new Social Welfare Index (SWI)was created that combines both effects of wealth and social development, measured with life longevity, survival rate and unemployment rate. We argue that SWI is a better measure of the effect of economic integration. Specification of the Model explains SWI as a linear combination of the export / import ratio (trade relationship), the general government debt (public policy instrument), the foreign direct investment stock as a percentage of GDP and labour productivity. This model suggests positive correlation between labour productivity and social development, negative correlation between GGD, FDI and social welfare of the country and insignificant effect of trade openness and social welfare.

8. The new S-Time-distance analysis is used as a complementary method to analyze the effectiveness of integration in the frames of Eurasian Economic Community. The indicator that is chosen to compare the member countries of EurAsEC is GDP per capita. It represents purchasing power parity and is measured in dollars. As a time period for comparison we took 21 years from 1990 to 2011. One main conclusion that can be made from this analysis is that it was a good idea to deepen the process of integration only for three leading countries and to form the Customs Union only for Russia, Kazakhstan and Belarus. Their economic development is more or less comparable so there is a chance that their integration will prove itself effective and vital for further growth.

9. We study the effects of relaxing specific assumptions of market efficiency concept. Our first model is about the effect of information uncertainty frictions, and the second one studies the effect of financial frictions. Assessment of the effects of the tariff is possible to produce in two stages - on the input and on the decline. In the second stage we have made impact on the level of tariff bankruptcy of companies.
The analysation of our hypothesis was marked by the result that profit fells both large and small companies. However, the decline in profits for small companies was higher than for large ones

10. We extend the standard definition of market efficiency by including an additional dimension of human capital. Our third model studies the effect of relaxing the fourth assumption of a frictionless human capital flow. If the system starts from a low level of human capital it may get stuck in the suboptimal equilibrium point without external help. Such help can come in a form of protective tariffs which increase the probability of business projects to succeed, and accelerate the accumulation of human capital.

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APPENDIX A

Table A.1 - Positive effects of NAFTA agreement on Canadian economy

Positive effect	Explanation
Strengthening position in the world market	Canada's economy has become more competitive and strong. It is accordingly reflected in the structure of foreign trade: the amount of competitive exports to other countries is increasing, as does the share of industrial goods in exports. This is driven largely by the trade with Mexico, which receives a significant amount of industrial and just finished goods. Thanks to the Mexican market Canadian firms were able to increase sales in the sectors to which access has been closed before, such as automobile industry, financial services, transportation, energy sector and fisheries.
Lowering prices for a wide range of Canadian consumer products.	Duty-free import of Canadian goods to the territory of NAFTA partners has led to a decline in prices for a wide range of Canadian consumer products. This, in turn, stimulated the demand for them and, therefore, contributed to the expansion of sales, an increase of volume of Canadian exports.
Lowering prices for Canadian import	The result of the agreement was not only cheap Canadian exports, but also imports. Part of Canadian consumers switched from local suppliers to foreign, and the result was the growth in consumption at lower prices. This was the consumer gain of the population.
Growth of national income	Despite the fact that the formation of a free trade area of NAFTA led to a loss for the Canadian budget (government revenues declined due to abolition of import duties), generally the growth of income was marked in the country. It resulted from imports of cheaper foreign goods substituting domestic goods of less efficient domestic producers.
Growth in foreign trade	The main result of the successful implementation of NAFTA agreement was the boom in foreign trade of Canada. The average annual growth of Canadian imports to the USA was 5.9% and to Mexico - above 12.5% during the period of 1993 to 2012. Moreover, it is important to note that in the mid-1990s export growth was the main driver of business activity, and with the rise in domestic demand in 1997-2000 it allowed Canada to take along with the US leader in terms of economic development in the G7.
Growth in foreign investment	Canada's participation in NAFTA has increased the attractiveness of the Canadian economy to foreign investors. Since joining NAFTA, direct foreign investment in Canada from all sources increased steadily.
Note: compiled by the author according to literature source [29]	

APPENDIX B

Table B.1 - Growth in gross domestic product in EurAsEC countries in 2000-2009 (at constant prices)

Country	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**
in % to the previous year										
Belarus	105,8	104,7	105,0	107,0	111,4	109,4	110,0	108,6	110,2	100,2
Kazakhstan	109,8	113,5	109,8	109,3	109,6	109,7	110,7	108,9	103,3	101,2
Kyrgyzstan	105,4	105,3	100,0	107,0	107,0	99,8	103,1	108,5	107,6	102,3
Russia	109,0	105,1	104,7	107,3	107,2	106,4	107,7	108,1	105,6	92,1
Tajikistan	108,3	109,6	110,8	111,0	110,3	106,7	107,0	107,8	107,9	103,4
Uzbekistan	...	...	...	...	...	...	107,3	109,5	109,0	...
EurAsEC Average:		106,0	105,0	107,0	108,0	107,0	108,0	108,0	106,0	93,0
in % to the year 2000										
Belarus	100,0	104,7	110,0	118,0	131,0	143,4	157,7	171,3	188,7	189,1
Kazakhstan	100,0	113,5	125,0	136,0	149,0	163,8	181,3	197,4	203,9	206,3
Kyrgyzstan	100,0	105,3	105,0	113,0	121,0	120,3	124,0	134,6	145,9	149,3
Russia	100,0	105,1	110,0	118,0	127,0	134,7	145,0	156,8	165,6	152,5
Tajikistan	100,0	110,0	121,0	135,0	149,0	159,0	170,0	183,0	197,0	203,7
Uzbekistan	...	...	...	...	...	...	140,6	153,9	167,8	...
EurAsEC Average:	100,0	106,0	111,0	119,0	128,0	137,0	147,0	159,0	168,0	156,2
Note: compiled by the author based on statistical data collected from the official website of the Eurasian Economic Community http://evrazes.com/docs/statistics										

APPENDIX C

Table C.1 - Growth in volume of industrial production in EurAsEC countries in 2001-2009 (in fixed prices)

Country	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
in % to the previous year										
Belarus	107,8	106,0	105,0	107,0	116,0	111,0	111,0	109,0	112,0	97,2
Kazakhstan	115,5	114,0	111,0	109,0	110,0	105,0	107,0	105,0	102,1	101,7
Kyrgyzstan	106,0	105,0	89,0	117,0	105,0	88,0	90,0	107,0	114,9	93,6
Russia	111,9	103,0	103,0	109,0	108,0	104,0	104,0	106,0	102,1	89,2
Tajikistan	109,9	115,0	108,0	110,0	115,0	110,0	106,0	110,0	97,0	93,7
Uzbekistan	...	...	...	...	...	...	111,0	112,0	113,0	...
EurAsEC Average:	113,0	104,0	104,0	109,0	109,0	104,0	105,0	106,0	103,0	91,0
in % to the year 2000										
Belarus	100,0	106,0	111,0	119,0	137,0	152,0	169,0	184,0	205,0	199,0
Kazakhstan	100,0	114,0	126,0	137,0	151,0	159,0	170,0	179,0	182,0	186,0
Kyrgyzstan	100,0	105,0	94,0	110,0	115,0	101,0	91,0	97,0	112,0	105,0
Russia	100,0	103,0	106,0	116,0	125,0	130,0	135,0	144,0	147,0	131,0
Tajikistan	100,0	115,0	125,0	137,0	158,0	173,0	182,0	201,0	194,0	181,0
Uzbekistan	...	...	...	...	...	...	161,0	181,0	204,0	...
EurAsEC Average:	100,0	105,0	109,0	119,0	130,0	135,0	141,0	150,0	154,0	140,1

Note: compiled by the author based on statistical data collected from the official website of the Eurasian Economic Community http://evrazes.com/docs/statistics

APPENDIX D

Table D.1 - Growth in volume of agricultural production in EurAsEC countries, 2001-2009 (at fixed prices)

Country	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
in % to the previous year										
Belarus	109,0	102,0	100,7	107,0	113,0	102,0	106,0	104,0	108,6	101,3
Kazakhstan	96,0	117,0	103,0	101,0	99,5	107,0	106,0	109,0	93,4	113,8
Kyrgyzstan	103,0	107,0	103,0	103,0	104,0	96,0	102,0	102,0	100,8	107,4
Russia	108,0	106,9	102,0	101,0	103,0	101,6	103,0	103,3	110,8	101,2
Tajikistan	113,0	107,0	117,0	109,0	111,0	102,0	106,0	107,0	106,1	110,1
Uzbekistan	...	...	...	...	...	...	106,7	106,1	104,5	...
EurAsEC Average:	108,0	108,0	102,0	102,0	104,0	103,0	104,0	104,0	109,0	103,0
in % to the year 2000										
Belarus	100,0	102,0	103,0	109,0	123,0	125,0	133,0	138,0	150,0	152,0
Kazakhstan	100,0	117,0	121,0	123,0	122,0	131,0	139,0	152,0	142,0	162,0
Kyrgyzstan	100,0	107,0	111,0	114,0	119,0	114,0	116,0	118,0	119,0	128,0
Russia	100,0	107,0	109,0	111,0	114,0	112,0	116,0	119,0	132,0	134,0
Tajikistan	100,0	107,0	125,0	136,0	151,0	153,0	162,0	173,0	183,0	202,0
Uzbekistan	...	...	...	...	...	...	146,0	155,0	162,0	...
EurAsEC Average:	100,0	108,0	110,0	112,0	116,0	120,0	124,0	129,0	141,0	145,0
Note: compiled by the author based on statistical data collected from the official website of the Eurasian Economic Community http://evrazes.com/docs/statistics										

APPENDIX E

Table E.1- Growth in volumes of investment in fixed assets in EurAsEC countries, 2001-2009 (at fixed prices)

Country	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
in % to the previous year										
Belarus	102,0	97,0	106,0	121,0	121,0	120,0	132,0	116,0	124,0	108,6
Kazakhstan	149,0	145,0	111,0	117,0	123,0	134,0	111,0	114,0	115,0	102,1
Kyrgyzstan	137,0	86,0	90,0	93,0	102,0	106,0	155,0	105,0	106,0	119,7
Russia	117,0	110,0	103,0	112,5	114,0	111,0	117,0	123,0	110,0	83,0
Tajikistan	...	...	...	...	150,0	112,0	170,0	215,0	141,0	84,5
Uzbekistan	...	...	...	...	...	...	109,0	123,0	128,0	...
EurAsEC Average:	119,0	112,0	103,0	113,0	114,0	113,0	117,0	121,0	111,0	87,0
in % to the year 2000										
Belarus	100,0	97,0	102,0	124,0	149,0	179,0	237,0	275,0	340,0	369,0
Kazakhstan	100,0	145,0	160,0	187,0	230,0	308,0	342,0	388,0	446,0	455,4
Kyrgyzstan	100,0	86,0	77,0	72,0	74,0	78,0	121,0	127,0	134,0	160,4
Russia	100,0	110,0	113,0	127,0	145,0	160,0	187,0	230,0	252,0	209,2
Tajikistan	...	...	...	...	...	...	...	...	...	...
Uzbekistan	...	...	...	...	...	...	139,0	170,0	218,0	...
EurAsEC Average:	100,0	112,0	116,0	130,0	130,0	135,0	141,0	150,0	154,0	134,0
Note: compiled by the author based on statistical data collected from the official website of the Eurasian Economic Community http://evrazes.com/docs/statistics										

APPENDIX F

Table F.1- EurAsEC countries GDP per capita (PPP, current international $), 1990-1996

Country Name	1990	1991	1992	1993	1994	1995	1996
Belarus	4646,85	4744,78	4370,19	4117,32	3713,97	3416,16	3585,95
Kazakhstan	5119,95	4682,26	4530,64	4231,98	3829,22	3660,59	3801,17
Kyrgyz Republic	1822,53	1708,35	1484,84	1282,44	1046,10	1002,32	1076,29
Russian Federation	8013,81	7850,38	6847,96	6398,74	5715,42	5613,43	5529,34
Tajikistan	2138,36	2010,21	1430,85	1203,03	951,82	840,85	702,50
Uzbekistan	1446,05	1456,45	1289,97	1258,99	1194,15	1189,25	1207,56
Average EurAsEC	3864,59	3742,07	3325,74	3082,08	2741,78	2620,43	2650,47
Note: compiled by the author based on the data from http://data.worldbank.org							

Table F.2 - EurAsEC countries GDP per capita (PPP, current international $), 1997-2003

Country Name	1997	1998	1999	2000	2001	2002	2003
Belarus	4089,07	4516,25	4754,33	5154,32	5539,49	5940,43	6526,33
Kazakhstan	4003,06	4051,51	4262,31	4795,67	5575,97	6221,57	6920,11
Kyrgyz Republic	1188,35	1211,88	1255,80	1336,58	1426,03	1435,69	1552,63
Russian Federation	5722,02	5492,50	5950,90	6832,78	7361,28	8029,47	9254,47
Tajikistan	717,82	756,00	785,48	859,43	959,28	1054,56	1177,07
Uzbekistan	1270,67	1322,47	1384,55	1448,08	1523,70	1590,79	1672,94
Average EurAsEC	2831,83	2891,77	3065,56	3404,48	3730,96	4045,42	4517,26
Note: compiled by the author based on the data from http://data.worldbank.org							

Table F.3 - EurAsEC countries GDP per capita (PPP, current international $), 2005-2011

Country Name	2005	2006	2007	2008	2009	2010	2011
Belarus	8540,82	9740,74	10924,10	12438,15	12748,63	13852,02	14937,97
Kazakhstan	8699,10	9835,98	10896,56	11365,73	11349,78	12091,67	13099,47
Kyrgyz Republic	1721,34	1812,42	2005,07	2200,58	2266,38	2244,68	2399,08
Russian Federation	11852,81	14949,25	16742,56	20276,16	18859,97	19940,32	21245,92
Tajikistan	1500,28	1291,82	1598,36	1955,04	2030,13	2147,21	2324,26
Uzbekistan	2000,97	2189,42	2432,05	2666,42	2871,47	3050,22	3287,36
Average EurAsEC	5719,22	6636,60	7433,12	8483,68	8354,39	8887,69	9549,01
Note: compiled by the author based on the data from http://data.worldbank.org							