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Stages of the Economic Integration and the Level of International Competitiveness. Optimization Methods. The EU Case

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Abstract. The paper highlights and discusses the concept of integration optimum. For this reason, there are analyzed aspects related to the stages of integration and the level of international competitiveness as well as the relationship competitiveness - integration – second-best optimum. The integration's benefits and costs are outlined in various stages of the EU enlargement, emphasizing the importance of combining national resources, performances towards competitiveness and the dynamics of dimension efficiency. The paper also includes an analysis of integration in different areas (Latin America, Northern America, Asia and Africa) and the degree of institutionalization in relation to competitiveness.

Keywords Integration, optimum, competitiveness, institutionalization, costs, benefits

1. The Process Of Integration and EU's Level Of International Competitiveness

"By its size – the largest in the world – the single market with no frontiers represents an invaluable value for the revitalization of our business and for making them more competitive. It is one of the main engines of the European Union"

Jacques Delors, July 1987

1.1. Market Dimension and Economies of Scale

"European countries are too small – as Jean Monnet wrote in 1943 – to give their citizens prosperity that is now possible and therefore necessary. They need larger markets".

Therefore, the market size matters. Since its inception in the 50s, an important premise backing the European economic integration was the belief that the unification of the economies of the European countries, by allowing access to a larger market for European companies, will make European firms become more efficient and thus lead towards lower prices, increased quality and toward gaining competitiveness on foreign markets.

Competitiveness remains an ambiguous concept in the literature in the field, firstly because of the manifold ways to define and measure it, and secondly because of insufficient theoretical substantiation, being taken from the business environment and showing a pregnant applicative character. From a macroeconomic point of view, competitiveness is analyzed at national level and describes the "economic capacity of a nation to produce a rapid and sustained improvement of living conditions". (Global Competitiveness Report, 1996).

This conceptualization of competitiveness represents a shared vision of the World Economic Forum and the European Commission (2000-2004), but still adds the wording according to which competitiveness is the „ability of economies to ensure a high standard of living of the population and an employment rate on sustainable basis".

As it results from the definitions of competitiveness listed below, the objective of competitiveness lies in maintaining or increasing the population's standard of living (particularly through increased income and employment), while simultaneously increasing the participation of a country's share in international markets.

- *"competitiveness represents the degree to which a nation can produce, under the conditions of the free market and fair competition, goods and services able to pass the test of international markets, being able to simultaneously maintain or increase the real income of citizens"*[1]
- *„...a country's ability to achieve its core objectives of economic policy, especially the growth regarding income and employment, without putting out the balance of payments"*[2]
- *"competitiveness represents a country's ability to maintain and increase the market share which it has on international markets, while improving the population's standard of living"*[3]
- *„....the ability of companies, branches, regions, nations and supranational associations facing competition to ensure a high relative cost of production factors and high relative levels of employment on a sustainable basis"*[4]
- *from the macroeconomic perspective, the essence of international competitiveness resides in price-based factors, the microeconomic perspective considering individual performances regarding the competitiveness of companies or branches of an economy (business strategy, behavior towards competitors, differentiation, specialization, innovation, technology, etc..). According to the first perspective, competitiveness translates into ensuring internal and external balance at national level and focuses on the effect of factors on competition. It highlights the links between changes in the balance of payments, the real exchange rate developments, reallocating resources among different economic activities and changes in competitiveness and its ultimate purpose is to increase the real income of citizens. The level of macroeconomic competitiveness can be seen as an aggregate export performance of the companies of a nation.*

The European idea of competitiveness translates into the ability of economies to sustain high rates of productivity growth. Since the Lisbon Strategy, set out to make Europe the most competitive and dynamic world economy, competitiveness has become one of the priorities of EU policy. The need for a competitive European industry and of a competitive market generally comes from the desire to achieve the economic, social and environmental objectives, and ensuring an increasing level of social

[1] President s Commission on Industrial Competitiveness, Global Competition: The New Reality, Wahington DC, Government Printing Office, 1985.
[2] J. Fagerberg, International Competitiveness, The Economic Journal, 98/1988.
[3] F. Fajnzylber, International Competitiveness: Agreed, Hard Task, CEPAL Review, 36/1998.
[4] European Commision, EU Sectorial Competitiveness Indicators, 2005.

welfare. The need of the European economy to adapt to structural changes,, the redistribution of resources and jobs towards new industries, the relocation of the industrial activity towards emerging economies and the risk of the de-industrialization process can be addressed by promoting competitiveness at EU level. Competitiveness in the European Union's vision means to excel in terms of research and innovation,, information and communication technologies, entrepreneurship, competition, education and training, and depends on the capacity, the outlook and behavior of the "branches of economic activity of European countries to achieve structural adjustment towards achieving performance in those areas".

Each country or region sets priorities according to what can mostly contribute to increasing competitiveness and productivity in the stage where they are. To put activities / elements inconsistent with the country's economic conditions could mean that the first one failed in reaching that goal (more competitive), and secondly a waste of resources. Obviously, there is a logical sequence of these stages, and logical links between competitive conditions. What must be present in all cases and at all stages is to maintain economic macro-stability. The need for a competitive European industry and of a competitive market generally comes from the desire to achieve the economic, social and environmental objectives and to ensure an increasing level of social welfare. The need of the European economy to adapt to structural changes, the redistribution of resources and jobs towards new industries, the relocation of the industrial activity by emerging economies and the risk of the de-industrialization process can be addressed through the promotion of competitiveness at the level of the European Union[1].

Regarding *the European integration in terms of the economic equilibrium theory, we can say that it fits better the details of economic equilibrium in a dynamic vision*, according to which the economic balance is a stage of the economic change (if the integration is intended as a step registering positive effects in the long run), changes caused by some disturbance factors/elements (international environment), state to which the system may return after having been adopted and implemented appropriate adjustment measures (European policy response). We can even talk about achieving *a high or low "economic integration", and hence the problem of establishing the optimal level of "economic integration".* However, the idea of degree or factor of integration makes us think of the possibility of its quantification, measurement or estimation, which is still very difficult. The theory of Second Optimum or the Optimum of Second Range is characteristic to suboptimal situations. Suboptimal cases are explained by the effect of not meeting some conditions in the sense of the paretan optimum. A sub-optimal situation which meets all the paretan requirements with one exception only is not better than another situation that also satisfies all conditions except one. Also, *the rule of Second Optimum, if applied to forms of integration, allows drawing conclusions according to which, if all steps of integration are sub-optimal, in terms of competitiveness, they lead to the same results.*

The rule of paretan optimum applied to integration formulas allows drawing the following *conclusions*:

- the Customs Union falls within the criterion of Second Optimum, compared to the global free trade;
- the optimal situation should not be reduced to static effects.

The European experience in particular, but also that of other regional unions, highlights *the dynamic effects*, such as:

- Economies of scale are achieved as a result of market growth;

[1] Wziątek-Kubiak, A., On Essence and Measurement of Changes in Competitiveness of the Accession Countries. Critical Review of Literature, Studies & Analyses No. 321, CASE – Center for Social and Economic Research, Varşovia, Polonia, March 2006)

- Renewal of the structure and quality of supply, following competitive challenge of the opening of markets;
- Increased domestic and foreign growth of firms in the integrated space.

The presence of dynamic effects and especially the economies of scale put forward the creation of regional unions (free trade areas, customs unions, common markets), especially between countries with similar specialized structures.

Since the accession in the period 2004 - 2007 there has been great progress in the fields of justice, freedom and security. Recently, the focus of attention is on economic competitiveness. Certainly the way the EU works can always be improved. Internal reforms must be driven and it is also necessary to intensify the efforts towards peace and welfare, as they serve the basic interests of the EU and its inhabitants.

Also, special attention should be given to the significant link between the available national resources, national performance and achieved competitiveness, as shown in Figure 1.

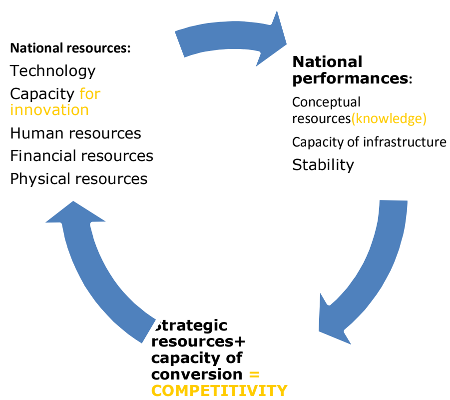

Figure 1. The method of combining the national resources and performance for competitiveness

The national internal environment contains all the elements on which the industry or the sector has a decisive influence on and, theoretically, has full control over. The study of the internal environment should establish which are the resources available for different sectors and if it would be able to follow the chosen strategy. Understanding the internal environment is the first necessary step in formulating a strategy. Studies on resources generated a conceptual framework of analysis - the study on the industry sector based on resources, used to explain the elements that create competitive advantages. The performance of an industry or sector is associated with a configuration of its resources whose value is fixed by comparison in a foreign context.

In the literature in the field, the term resource is associated with other concepts: skills or capabilities. Thus, the essential basic skills and collective experience of the industry are manifested particularly in combining the various skills associated with the production and integration of multiple technology streams.

Any *management of a strategy* requires two sub-systems:

1. *Strategy Formulation*:

- Strategic planning;

- Long-term plans;

2. *Implementation and strategy assessment*:

- Operational annual budgets;

- Periodic reports and statistics;

- Performance assessment;

- Policies and procedures.

From the implementation process of the strategy the double loop control should not miss, as shown schematically in Figure 2.

But there are barriers that may prevent the control strategy:

1. *Systemic barriers* - deficiencies in the design and management control system;

2. *Behavioral barriers* - conventional thinking, organizational culture, cognitive limitations, resistance to change;

3. *Other barriers* - inability to agree upon a strategy and to allocate resources, its lack of acceptance by those involved or affected by it, the hiding of inappropriate results.

The strategy will lead to increasing the competitive advantage of EU Member States:

a) Economy of scale -> lower costs and thus lower prices;

b) Economy of learning -> same good solution can be extended;

c) The effective use of existing capacity;

d) Management and organizational efficiency;

e) Increase of solidarity by the construction of a more transparent society, bringing citizens closer to the public services and their elected representatives, by developing new educational tools, by facilitating the finding of jobs and dissemination of administrative initiatives.

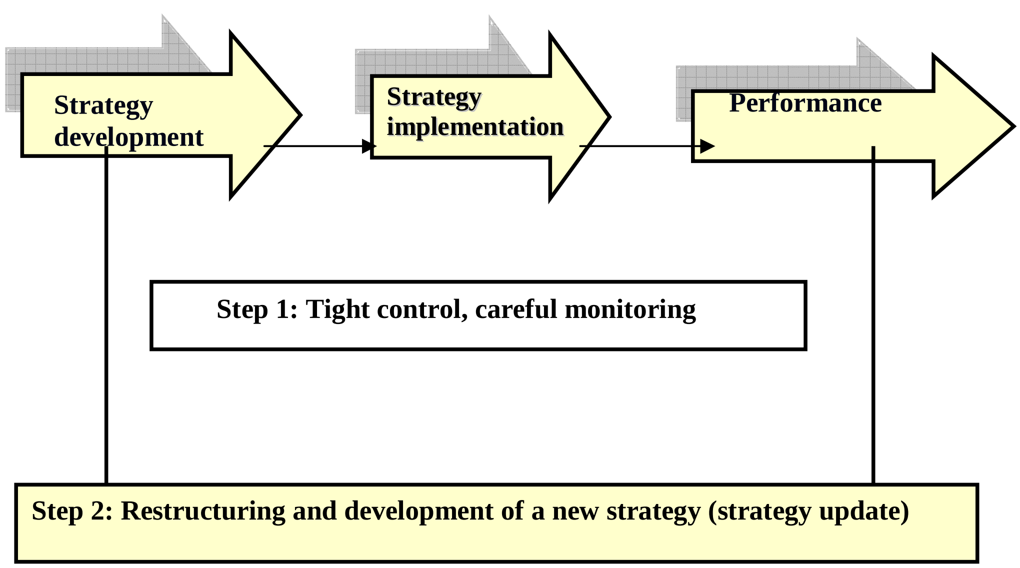

Figure 2. Steps of control process for the strategy of sustainable economic development in the context of country competitiveness

It is considered that, from a certain stage, the scale's performances are exhausted. Thus, if the quantity of factors continues to grow and the amount of products increases less than proportionately with that quantity of factors of scale, it is estimated that performances are decreasing. Given these conditions of production, unit costs begin to rise. From now on the phenomenon called diseconomies of scale will occur. The economic theory explains this phenomenon based on the combination of a fixed factor and a variable factor which necessarily leads to decreasing performances.

Graphically, the cost curve, called the *long-term cost curve*, reflects the evolution of unit costs of production depending on the quantities of factors used. The „U" shape of the curve shows the successive emergence of economies and diseconomies of scale in relation to the evolution of the performance (ascending or descending). The „G" point represents the optimal level of activity, separating the advantages and the disadvantages as a result of the dimension of the activities/work.

Each activity is represented by companies whose size can be considered optimal.

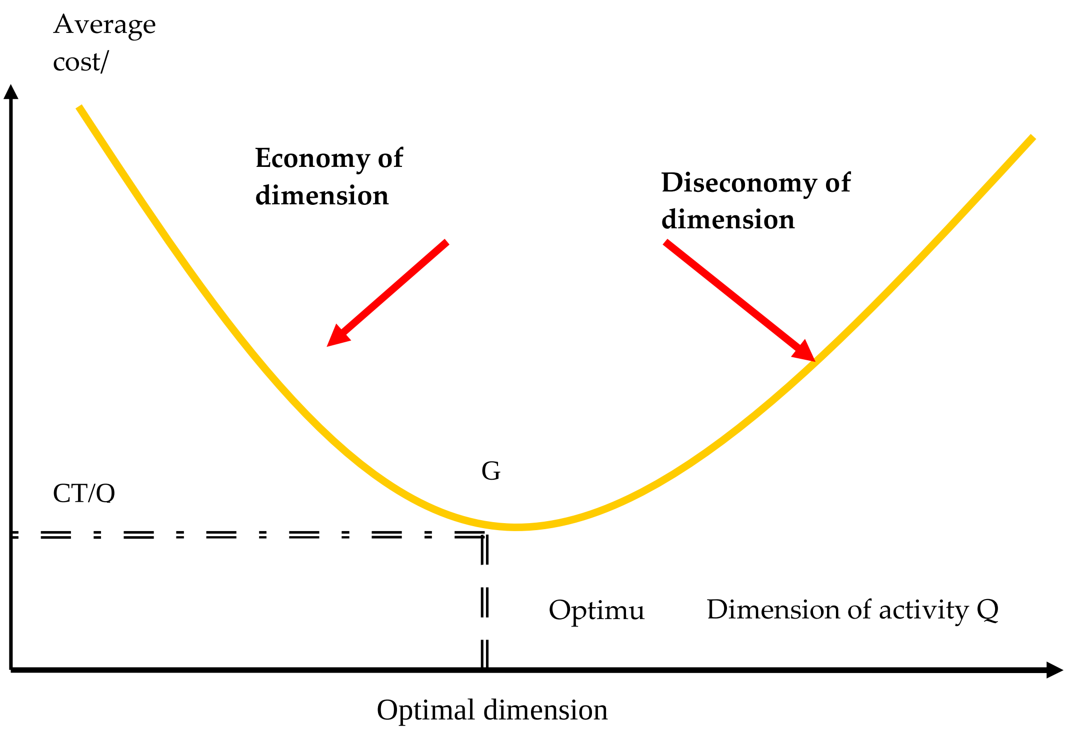

Figure 3. The „rule of the cup" or the long-term cost curve and the optimal dimension of activities

1.2. The Stages of Economic Integration. The Benefits and Costs of the EU Enlargement and their implications on European Compared to other Integrationist Structures

Economists agreed that economic integration is both a process and a state of fact determined through a concatenation of transformations. The consensus regards at least three aspects:

- "economic integration", in particular, refers to the division of labor and intra- and international specialization;
- "economic integration" implies freedom and mobility, the movement of goods, services and factors of production, or of all;

- it is in close correlation with differential or discriminatory trade treatment regarding the origin or destination of goods, services and production factors. This consensus does not mean that one unit integrates views about the definition of the concept.

The phenomenon of integration is a complex phenomenon that involves:

- The establishment of free trade areas in order to optimize the resource's allocation, increasing the efficiency of the productive mechanism and boosting the economic life;
- Formation of a new competitive space, large and favorable for the economy of scale and specialization according to comparative costs theory.

The stages of the economic integration can be grouped as follows:

a) free trade zone - established by eliminating tariff and non-tariff barriers between members, each member country maintaining a set of restrictions; the agreement may be limited to a few sectors, or may cover all aspects of international trade (e.g. NAFTA);

b) the customs union - including a free trade zone, and representing an agreement between the participating nations in order to eliminate all tariff and non-tariff barriers; the basic purpose of perfecting a customs union is to increase economic efficiency, namely the creation of political and cultural relations between member countries (e.g. the Benelux);

c) the Common Market – the Single Market - is a major step towards economic integration by removing all trade barriers between the Member States, namely the adoption of a common external tariff, permitting, in addition, the free movement of goods and services within the established market; the major benefit is represented by the free movement of production factors between the Member States, respectively their more efficient allocation, followed by additional growth in productivity (e.g. EU, since 1992);

d) economic and monetary union – representing a union in which the national, social and tax policies are harmonized and administered by a supranational institution – so that an agreement regarding the transfer of economic sovereignty towards a supranational authority becomes necessary; the final degree of economic union will be represented by the unification of the national monetary policies and the acceptance of the single currency.

Full economic integration is the final stage of the economic integration; political integration is a prerequisite in this respect, and in order to become truly effective all areas should be in the same stage of the economic cycle. Also, to reach this stage of economic harmonization, it is necessary to increase the degree of central control in order to implement a policy to control inflation and promote economic stability throughout the delineated area.

As noticed, originally the integration covered only the product markets, the markets for production factors, then extending to various areas of the economic policy. However, the complexity of forms of achieved integration brought forward the need of institutional redefinition. At the same time, the transition from one form of integration to the next and from one state to another is extremely flexible and can't usually be well defined. The first integrationist stages - free trade area and customs union - seem to relate solely to market integration, according to the classic laissez-faire theories, while more advanced stages - economic union, monetary union and economic and monetary union - involve a greater macroeconomic coordination.

The stages of integration have two common characteristics. They remove discrimination between economic agents within partner countries (the domestic purpose). Furthermore, in various forms, they maintain or introduce certain forms of discrimination on economic agents in third countries (the external purpose).

In economic terms, the process of extending brings benefits for both new and old member states and to the Union as a whole. Trade between the old and new Member States have nearly tripled in less than 10 years (from € 175 billion in 1999 to around € 500 billion in 2007). These aspects are shown more clearly by the five-time increase in the volume of merchandise trade between the new Member States, from less than € 15 billion to € 77 billion in the same period.

This was a key factor that contributed to a steady annual increase of 1.5% in employment in the new Member States in the period between their accession in 2004 and the start of the financial crisis.

The economic crisis has shown that the expansion is not a problem; it is the solution that can revitalize the economy. We have a common destiny.

Regarding the influence upon the citizens it should be underlined that higher stability and peaceful development, to which successive EU enlargements contributed over the years, is a benefit for all Europeans, and not only. By including in the European internal market of over 100 million consumers with growing purchasing power, the demand for products from companies in the old Member States has intensified. This has led both to preserve and create jobs in the home country. As German citizens take advantage of each machine produced and sold by a German company in Poland, so each transaction of a Dutch bank in the new Member States intends benefit for the entire Dutch economy. Conversely it is equally valid.

The most important points in the last accession negotiations were food safety and animal health. EU has taken strict measures to bring new members to EU standards. Food processing plants, dairies and slaughterhouses that do not meet the standards were closed before accession, and only those meeting the established conditions were able to sell their products on the European internal market.

Implementation of specific directives on water led to improved drinking water quality and of water in general.

Also, nuclear safety has improved as a result of enlargement. Within the obligations of states imposed by membership, more nuclear power stations that pose a security risk were closed. The European nuclear safety has improved through the initiative of the new Member States to integrate into the European rapid exchange of information provided in case of radiological emergency situations.

Following enlargement, more countries joined the Schengen Treaty, which provides facilities regarding free movement to all citizens. Integration of new Member States in domestic air traffic in the EU has resulted in safer flight services and better service value. EU citizens can benefit from expansion by improving business opportunities and the possibilities regarding the study and work abroad.

Regarding *the costs of EU enlargement*, it should be stressed that EU financial assistance for new Member States is about 0.2% of the gross domestic product of the old Member States and it will grow by 2013 to 0.3%. The economic benefits for EU outweigh this expense by far. Money from these percentages is used so that the entire EU should take advantage. Construction of roads and other infrastructure projects in new Member States is often taken over by companies from the old Member States. The stability of the laws guaranteed by the state, reducing corruption and improving infrastructure are beneficial to companies throughout the Union. The funds used for the development of national economies in the new Member States also create business opportunities for both the old Member States and for new ones.

However, it should be emphasized that the EU includes two internal spaces: the space of internal "periphery" and the internal "central" space; among the most prosperous regions and the least favored regions in the EU the gap is between 57% and 278% of the average GDP and GDP/capita established on regions are between 33 and 278% of the communitarian average.

Considered in terms of eligibility regarding structural funds, 60 EU regions are below the threshold of 75% of the Community average, of which 24 are located in the old Member States (Greece, Italy, France, Germany, Portugal and Spain) and 36 in the new Member States, without Slovenia and Cyprus.

All 36 regions represent almost entirely the 8 new Member States, except for three capital regions (Prague, Budapest and Bratislava). The internal "periphery" of the economic integrated space has increased in terms of enlargement in the period 2004-2007:

a) In the case of the EU-15, the peripheral regions occupy 57% -75% of the communitarian average
b) In case of the EU-25:
   • 6 of the poorest regions of the EU-25 are between 33-37% of the average (Poland, a Slovak region and 3 regions of eastern Hungary are included in this category). The regions in Romania and Hungary are between 31-34% of the EU-25.
   • The "Internal periphery" of the EU is to be divided into 2 areas: a "traditional" area characterized by a GDP/capita between 50-75% of the EU average, and another new area characterized by a GDP/capita between 30% and 50% of the communitarian average. The latter is characterized by a particularly low level of payment, infrastructure, investment and employment.
c) In the case of EU-27:
   • 11 regions are located in the category 50-77% of the EU average
   • 25 regions (the majority) are in a new area, between 30-50%. (these areas represent a level of development that the EU did not know until the expansion in 2004-2007).

The integration theory shows that an integrated system works effectively if there is uniformity of structure. EU does not fall into such a system if we consider structural segmentation, respectively the two segments: „internal periphery” and „national center”.

2. The Integration Optimum. Methods of Optimization

Before revealing the scientific aspects we consider it useful to present some considerations on the word “optimum”. The notion of “optimum” cannot equate “the best”, “the cheapest”, “the most ...” but can rather be considered as “the most convenient according to certain criteria in certain restricted conditions”. Hence the conclusion that the optimum is not necessarily an absolute maximum, but more a partial extreme determined under certain conditions (restrictions) and for previously set objectives. The issue of optimization can be treated as a separate entity or integrated into a systemic approach. The systemic approach should better reflect the frame and conditions of optimization integrating the inputs and outputs and the feed-back.

European expansion is a unitary and irreversible process which has no reason to being blocked by countries of the basic matrix; from an economic and social point of view the expansion process involves costs (both for the integrated and the integrator), but also benefits; the integration process should not be mistaken for the time of accession, a political act based on reason, analysis and well-negotiated agreements (at least regarding principle and public image), by both sides (the integrator and the integrated one); the process of integration includes accession, there being a before and an after stage of the integration, i.e. pre-, post accession. The activities included in the process of European integration are activities that involve the circulation of large quantities of various types of resources: human, financial, raw materials, strategic positions, key intangible assets, etc.

Therefore, the concern for continuous optimization of processes in this field is justified.

The microeconomics of the European integration shows that, after integration, there are three types of economic effects: a) the allocation effects, sometimes also called “static effects”, b) accumulation effects, also known as “growth effects”, they determining the impact of integration on the accumulation of economic resources, particularly of capital, and c) effects of localization, at European level, these representing geographical reallocation of resources, but in terms of the regional perspective they appear as effects of accumulating.

Once the benefits of future integration exceed costs, a higher level of integration (coordination or unification) will be released. Each successive stage of autonomy loss will make it more difficult for a state to adopt that economic strategy which should target specific objectives. Progress towards future integration depends on how rapidly gains appear and are perceived by as many interest groups and losses will be minimized. Gains derive from a common better allocation of production factors, from the stabilization policies of the economic growth and also from the equitable redistribution of income.

Costs will arise from the impossibility of granting national preferences to certain strategies, following a decrease in decision-making autonomy. Thus, by decision coordination or unification there will diminish:

- The ability to balance the revenue against budget expenditures, according to domestic spending;
- The possibility of budget deficit inflationary financing;
- The possibility of using monetary devaluation as a means of stimulating exports and decreasing imports;
- The possibility to use a consumer sequential protection, of some national health policies, the redistribution of income and the foreign policy.

As changes occur from one stage of integration to another, more national powers will be transferred to group level. The first will be those in the economic field, followed by the non-economic ones (cultural, social, foreign policy, defense).

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