

# Leveraging Regional Integration in Foreign Economic Policy: the Case of Small and Open Economies

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## Abstract

The global economic landscape has undergone dynamic transformations, leading to an interconnected and interdependent system. This evolution has prompted governments, particularly those of small and open economies, to adopt innovative instruments to bolster their competitiveness. The article explores the growing trend of utilizing participation in regional integration as a strategic tool in active foreign trade policy analysing the specific challenges and opportunities for small and open economies. For them, integration might serve as a multifaceted foreign trade policy instrument, offering avenues to reduce vulnerability to external shocks, enhance competitiveness, preserve added value, and strengthen regional resilience. This proactive approach reflects an acknowledgment that participation in integration processes is a strategic means of advancing their interests and safeguarding their economies in an increasingly interconnected world. The proposed three-dimensional evaluation framework offers a nuanced analysis of integration

processes, considering factors such as genesis, motivation, and development. This comprehensive approach provides valuable insights for policymakers, scholars, and analysts navigating the complexities of the contemporary international economic order.

**Keywords:** Regional integration, Foreign economic policy, Small economies, Open economies, National competitiveness

**JEL:** F15, F13, O19, P45

## 1. Introduction

The global economic landscape is undergoing profound structural changes, marked by key processes that redefine the dynamics of international trade and cooperation. The forces of globalization and regionalization are shaping the contours of the world economy, transcending traditional spatial and temporal constraints. In this transformative era, the interplay of market-driven changes in trade flows, the evolution of global value chains, and the increasing prominence of emerging economies are pivotal forces steering the course of economic interactions.

One salient structural change is the delicate balance between globalization and

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regionalization. While the ideal of a seamlessly integrated global economy persists, regional trade agreements and bilateral or multilateral agreements are gaining traction. The protracted negotiations within the World Trade Organization have prompted countries to explore regional alternatives, potentially leading to a paradoxical form of "closed" regionalization amid the overarching trend of globalization.

Moreover, the concept of trade liberalization occupies a central role in these structural shifts. As countries navigate the complex terrain of multilateral negotiations, regional trade agreements offer nimble forums for crafting rules and commitments tailored to the specific needs of participating countries. However, the pursuit of regional integration comes with its challenges, including the risk of trade discrimination and potential welfare losses.

Small and open economies face unique challenges and opportunities as they navigate an increasingly interconnected world. This article aims to analyse the role of regional integration as a strategic instrument in the foreign economic policy of these economies. Specifically, it tests the hypothesis that participation in regional integration initiatives can serve for small and open economies as a means to mitigate vulnerabilities, enhance competitiveness, and preserve added value in the face of global economic fluctuations.

The motivation for this study stems from the recognition that small economies are particularly susceptible to external shocks, making it imperative to explore innovative policy tools that enhance their resilience. By leveraging regional integration, these countries can advance their interests and safeguard their economies in a complex international environment.

The article contributes to the theoretical discourse on economic integration by providing a nuanced framework that highlights the multifaceted nature of regional cooperation. Through comprehensive theoretical analysis, a new conceptual typology and a novel three-dimensional approach for assessment of the participation in regional integration, the article elucidates the benefits and challenges that small economies encounter in this context.

In summary, this study finds that regional integration not only functions as a vital mechanism for reducing vulnerability to external economic pressures but also plays a crucial role in fostering long-term competitiveness and regional resilience. The findings provide valuable insights for policymakers, scholars, and analysts alike, as they navigate the complexities of contemporary international economic relations.

## **2. Major structural processes in the world economy**

In the modern global system of international economic relations, we witness a complex interplay of changes and trends influenced not only by economic factors but also by an array of social, political, and security-related ones. These trends are diverse and, in some cases, produce profound economic consequences.

Although a lot of researchers are exploring one or several of these trends and processes, almost none have tried to systematically examine their cumulative existence as major structural processes in the global economy. This analysis distinguishes itself from prior research by systematically examining the cumulative impact of key structural processes in the global economy, rather than isolating individual trends as many previous studies have done. Given the constant evolution and the multitude of interpretations in the scientific

literature, this section provides a brief and comprehensive yet not exhaustive overview of some of the various structural changes and trends in the global economic landscape, providing a foundation for understanding how these processes influence both economic integration initiatives, as well as small and open economies.

### ***Institutional changes in international trade***

In the international trade system, we observe two sets of opposing institutional changes. On one hand, there's the pervasive narrative of global trade liberalization, as exemplified by claims such as "There are no longer any major trade restrictions left to be removed. If in the 1990s the benefits of trade liberalization were huge (hundreds of billions of dollars) and liberalization brought 10% of economic growth in the world, then these benefits, although important and obvious, have already been realized" (Krugman, 2016). Simultaneously, many countries worldwide are resorting to protectionist measures, including hidden non-tariff restrictions and direct tariffs introduced after various economic crises, including for example tariffs introduced after the Global crisis by Russia, Ukraine, Ecuador, EU, Brazil, India, Turkey, Vietnam, etc.; the US-China trade "war", trade restrictions during the pandemics (including within the EU Common market), etc.

There are also a number of examples of how the new trade agreements for trade liberalization, include many "non-trade" issues (sustainable development, affirmation of democratic values, environmental norms, etc.). While these agreements may appear reciprocal in nature, they often favour developed economies. In practice, they can position developing countries as providers of

natural resources and production hubs for multinational corporations, with the capital owners primarily hailing from developed nations. This trend raises questions about the fairness and equity of these agreements, highlighting the asymmetrical distribution of benefits among participating nations and the challenges faced by developing economies in the international trade system. The international trade framework is being called into question, and uncertainty in trade relations is contributing to global economic uncertainty and dampening economic growth. (Bobeva, 2020).

### ***Globalization and regionalization:***

The process of globalization is marked by the removal of traditional spatial and temporal constraints in economic activities. It is driven by multiple factors, including significant advancements in information and communication technologies, the exploration of new energy sources, automation, biotechnology, and the increasing knowledge intensity of modern production methods. These drivers collectively contribute to a scenario where economic entities across the globe become more interconnected and interdependent, effectively binding all economic activities into a cohesive whole within the realm of the world economy.

Despite the potential for a seamlessly integrated global economy and cost-effective multilateral trade, there has been limited progress in the negotiations within the World Trade Organization (WTO). This lack of advancement in multilateral trade negotiations has led to a counterintuitive trend. Many countries, frustrated by the stalled negotiations at the global level, are turning to regional free trade initiatives and bilateral or multilateral free trade agreements as an alternative.

These regional trade pacts, often referred to as Regional Trade Agreements (RTAs), have gained prominence as they provide a means for nations to advance their trade interests outside the constraints of the WTO.

The consequence of this shift is that it has resulted in a growing gap between the Global North (industrialized and developed economies) and the Global South (emerging and developing economies). While globalization was initially seen as a force that could potentially bridge economic divides, the paradoxical outcome is a form of "closed" regionalization. In this context, countries are forming regional trade blocs and agreements that can create barriers to trade with non-participating nations. For example, for decades the EU has been criticized for the lack of coherence between its individual policies and for their contradictory effects on developing countries (Byanov and Byanova, 2018). This regionalization occurs within the broader backdrop of a globalizing economy, potentially leading to fragmentation and challenges in fostering global economic integration.

### ***Market-driven changes in world trade flows***

Market-driven changes in world trade flows reflect a rapidly evolving global landscape. In this context, emerging economies are experiencing robust development, often surpassing the growth rates of their developed counterparts. This divergence in growth dynamics has profound implications for the global trade environment.

Firstly, it underscores the contrast in commercial interests between developed and developing economies. Emerging economies are eager to secure access to markets and resources, while developed nations seek to maintain their competitive advantages. This

leads to intricate negotiations and dynamics in the world of international trade.

Secondly, this trend triggers intense competition among global economic powers to establish a significant presence in emerging, fast-growing markets. Countries vie for market share and influence in regions where economic expansion is most promising.

The concept of a "global village", characterized by information and communication connectivity, is paralleled by a "commercial connectivity." This concept encompasses the development of global value chains, wherein transnational corporations play pivotal roles in shaping world trade. Innovations in international capital flows and foreign investment are also central to this transformation.

Market-driven changes are further influenced by cyclical factors. Global demand fluctuations, volatile raw material prices, shifts in consumer behaviour (especially in China), and other economic dynamics intensify the processes of change in world trade flows. These factors collectively contribute to making these changes even more pronounced and complex, altering the traditional landscape of international trade.

### ***The changing nature of international specialization***

Last but not least, the changing nature of international specialization must also be considered. International trade is one of the main factors shaping economic growth, especially in the period after the Global economic crisis of 2008-2009 (Yotzov, Loukanova, Sariyski, Nestorov, 2020). In parallel with the growth of trade in final consumption goods, the increasing trade in intermediate and raw materials, reflecting the internationalization of production, has

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transformed international specialization. The growing purchase of intermediate raw materials from foreign countries has become integral to the supply chains of various industries, resulting in a reduction of domestic value added in exports.

Imports of intermediate raw materials account for more than 50% of trade in goods and about 70% of trade in services (Koopman et al., 2010), and in many countries a growing share of intermediate imports from abroad ends up in the production of final consumption goods for export. This results in a stronger dependence on economic conjuncture of a country's main trade partners (Tasev and Nestorov, 2020), which has implications for the role of domestic factors of production in smaller, more open economies compared to larger or resource-rich ones.

Trade can stimulate growth and increase aggregate welfare in several ways. First, it causes an optimal distribution of the factors of production among companies and industries, which leads to higher efficiency and effectiveness. At the same time, by increasing competitive pressure, trade reduces inefficiency and stimulates innovation (Aghion and Howitt, 1998). Secondly, it contributes to access to a larger international market and thus increases the opportunities to realize economies of scale and technological spillovers that support economic growth (Rivera-Batiz and Romer, 1991; Dalum et al., 1999). Thirdly, trade allows countries to specialize – both in terms of production and as human capital – in goods and services for which they have comparative advantages, and this leads to faster growing productivity through learning and scale effects (Krugman, 1980).

However, benefits of trade are not evenly distributed, both between and within countries

(Venables, 2003). Trade encourages countries to specialize, and because different goods and activities are associated with different capabilities in terms of technology and knowledge, those countries that specialize in dynamic and innovative industries are in a better position to achieve sustained economic growth (Grossman and Helpman, 1991; Hausmann et al., 2007).

### ***Trade liberalization at global and regional levels***

Trade liberalization can manifest at both the global and regional levels. Multilateral negotiations involving a large number of countries are inherently complex and time-consuming. As an alternative approach, regional trade agreements are formed among a limited group of relatively similar countries. These agreements offer flexibility in negotiating rules and commitments that may exceed the capabilities of broader forums like the WTO.

However, it's important to be aware that regional integration can introduce certain challenges. One such challenge is trade discrimination, where preferential treatment within a regional trade bloc can create disadvantages for non-participating countries. This phenomenon is known as trade diversion. It occurs when trade shifts from a more cost-effective supplier from a non-participating country to a relatively expensive intra-regional supplier. In essence, it leads to less efficient allocation of resources and can result in economic losses for some nations.

Moreover, regional integration can promote regionalism, which is the prioritization of regional trade agreements and relations over global ones. While regional integration can bring benefits, it may also act as an obstacle to trade liberalization at the global level. This

highlights the complexity of international trade dynamics and the need for balanced policies to ensure that trade liberalization efforts benefit all participants and contribute to global welfare.

### ***Digital inclusivity and digital divide***

The growth of the digital economy has led to increased digital trade and e-commerce, surpassing and bypassing national and regional borders and jurisdictions. Businesses and consumers can engage in cross-border transactions more easily, leading to the rapid expansion of online marketplaces and a shift in the way goods and services are bought and sold. Data itself has become a valuable commodity in the digital age. Companies and countries that can collect, process, and leverage data have a competitive advantage. This shift has implications for privacy, data protection, and data governance.

Free exchange and access to information lead to the development of a number of technologies such as social networks, the Internet, electronic and virtual shops, artificial intelligence, etc., which change people's way of thinking and, hence, their behaviour as consumers (Dimova, 2021). The digital economy has given rise to new business models, such as the sharing economy, platform businesses, and the gig economy. These models have disrupted established industries and created opportunities for entrepreneurship and innovation. Digitalization has redefined global value chains by enabling real-time information sharing, improving coordination between suppliers and manufacturers, and increasing efficiency. This has allowed businesses to optimize their supply chains and reduce costs.

However, the digital divide remains a pressing issue, with some countries and

communities having better access to digital technologies and online resources than others. Bridging this divide is essential for ensuring that the benefits of the digital economy are inclusive and accessible to all.

The digital economy is increasingly influencing trade, investment, innovation, and development. It raises questions about regulation, governance, and the impact on societies, making it a central consideration for policymakers and scholars in international economics.

All these factors determine the complex and interconnected dynamics at play in the world economy's key structural processes. Understanding these dynamics underscores the necessity for policymakers to design economic strategies that adapt to the evolving structures of global trade. They also offer a foundation to grasp the implications and ramifications of these developments within the context of economic integration theory and practice.

### **3. Economic integration: cause or consequence of structural transformations in the world economy?**

The term "integration" means the restoration of something in its entirety. It is used to characterize a wide variety of relations of interdependence and interweaving of social relations in a group of countries. The term 'economic integration' is used to characterise various areas of international economic relations and the process of bringing individual economies together to pursue free trade. In the narrow sense in which it will be considered here, economic integration refers to the removal of discriminatory barriers to trade between a number of countries and the establishment of elements of cooperation

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between them. Economic integration also represents an objective process of interweaving of processes in national economies as a result of the development of modern productive forces and achievements in the scientific and technical field. As a form of economic influence, it creates more favourable conditions for mastering advantageous positions in the world economy and in international relations. According to most authors, the theory of economic integration passes through two stages of development, each of them responding to political and economic issues relevant to the time of its emergence. The first stage involves the traditional theories of economic integration, which explain its possible benefits in terms of trade and are in many cases referred to as "static analysis of integration agreements". The second is the new theories of economic integration, which have evolved under changed economic conditions and trade environments and are often referred to as 'dynamic economic integration analysis'.

Research examining trade integration and explaining the theoretical aspects of preferential trade agreements is based on Jacob Viner's seminal work, *On Customs Union Questions* (Viner, 1950). His static analysis of economic integration divides its possible effects into trade creation effects and trade diversion effects. Trade creation is said to occur when, in reaching a trade agreement between two countries, trade shifts from a member country offering a good more expensively to one offering the same product more cheaply. A trade diversion occurs when imports shift from a cheaper supplier in a non-integrated third country to a more expensive supplier within the Community.

In short, Viner's theory means in practice that countries would be motivated to integrate

if integration is likely to result in more static gains than losses, or in other words, more trade creation than trade diversion. Many authors have complemented Viner's static analysis by looking at different sides of the integration effects question, adding the so-called trade expansion (Panushev, 2003). Thus, static effects generally include (1) trade creation (trade creation), (2) trade diversion (trade diversion), and (3) trade increase (trade expansion).

All studies extending Viner's analysis conclude that there is no clear answer to the question of whether or not a customs union increases world welfare. From the perspective of international trade theory, although intra-community trade is increasing, in practice static effects act as regional barriers to it, enabling a new, regional protectionism to take place, and directing the distribution of the benefits of integration towards the large, developed economies within the community at the expense of efficient resource use and global welfare gains.

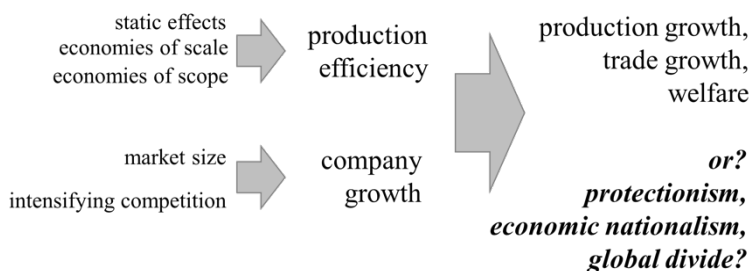
As early as the 1960s, it became clear that static analysis of trade creation and diversion was not sufficient. A central thesis in international economics is that free trade in competitive markets ensures efficiency of production and consumption across the world and in each country separately. The creation of preferential trade agreements, motivated by the ideas of static analysis, was initially seen as a shift towards free trade and was perceived as a means of increasing real incomes. However, it turns out that this is not true: this analysis does not provide simple answers and principles, and attention must therefore turn to the dynamic analysis of economic integration (Balassa, 1961).

The dynamic analysis of the effects of economic integration derives from the

characteristics of today's free economy. Because of their depth, dynamic effects of economic integration have a greater impact on economic processes than static ones. Thus, dynamic effects generally include (1) economies of scale, (2) economies of scope, (3) market size, and (4) intensifying competition.

In theory, these effects should lead to larger and more efficient production, to

increased trade flows, and hence, in the context of the neoclassical trade model, to increased welfare. However, assessed in the light of the structural transformations in global economy discussed in the previous sections, in reality are they not giving rise to a new kind of regional protectionism, economic nationalism and an intensification of the global divide (see Figure 1)?



**Figure 1.** The effects of integration

**Source:** Created by the author.

Forms of economic integration are evolutionary – each higher-ranked scheme contains the characteristics of the lower ones, but also new elements that expand it in scope and content. They can be seen as stages in a process that has as its ultimate goal (insofar as this is desired by the participating states) the achievement of full integration - unified monetary, social and economic policies and supranational institutions whose decisions are binding on the member states.

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supranational institutions whose decisions are binding on the member states.

To the extent that each successive more advanced form of integration involves the surrender of more national sovereignty by the participating states, it is they themselves who set the objectives in the integration process. "The transition from one stage to another, the higher one means the expansion of the areas of economic life - the object of integration (Marinov and Iliev, 2014). Despite the evolutionary nature of the integration process, countries that believe this is achievable and consistent with their objectives can start the process directly from one of the higher levels.

In most cases, the theories of economic integration and its benefits - both those of dynamic effects, but especially those of static effects of integration - are not applicable to underdeveloped and developing countries. Already Balassa argues that the theoretical

literature on economic integration considers a customs union only among industrialized countries (Balassa, 1961). Their problems are related to economic development and not so much to relative changes in production and consumption characteristics.

In this respect, the major problem of the distribution of the benefits of integration is also the cause of different motivations to participate in integration processes and of a serious divergence according to whether the participating countries are the same or different in terms of the size of their economy, its openness and their degree of economic development (small/large, open/closed, developed/developing). This in turn leads to different approaches, pace of development and outcomes of integration processes.

As we recognize the limitations of traditional economic integration theories, it becomes essential for policymakers to develop innovative frameworks that address the unique challenges faced by diverse economies, which can inform the subsequent exploration of the opportunities and strategies for small and open economies in utilizing integration as a proactive foreign trade policy tool in the following section.

#### **4. Economic integration and its application by small and open economies**

This part of the study attempts to identify some of the shortcomings and limitations of conventional economic integration theory in assessing integration processes in the context of contemporary changes in the world economy, especially in relation to small and open economies. Through a comprehensive literature review, theoretical synthesis and analysis of case studies and empirical evidence, the inconsistencies

between theoretical predictions and real-world integration outcomes are demonstrated. Through a critical assessment of the strengths and weaknesses of existing theories, this chapter lays the groundwork for proposing a new approach to understanding economic integration in the final chapter.

Economic integration theory attempts to answer two questions: first, what is its effect on welfare; second, what are the factors that influence countries' willingness to engage in integration processes (Abdel Jaber, 1971, p. 260). This section will examine the answers to these two questions from the perspective of small and open states.

##### **4.1. Small economies and regional integration**

Small economies face distinct challenges when participating in regional integration and trade liberalization compared to larger economies (Kurecic, 2017).

The case of Belize exemplifies the challenges faced by small economies in navigating regional integration. As a small nation with limited resources, Belize relies heavily on its agricultural exports, especially sugar, banana, and seafood. However, its integration into the Caribbean Community (CARICOM) has revealed significant hurdles, primarily stemming from its limited bargaining power in negotiations. Belize struggles to compete with larger countries within CARICOM, which possess more diversified economies and greater negotiating leverage. This asymmetry often results in trade agreements that do not favor the interests of smaller states, as they lack the capacity to implement the necessary reforms or meet the regulatory standards set by larger partners. Consequently, while regional integration aims to provide opportunities for economic growth,

it often exacerbates the vulnerabilities of small economies like Belize, leaving them reliant on a narrow range of exports and exposing them to external market fluctuations.

Limited bargaining power is a key issue, as small economies may struggle to secure favourable terms in trade negotiations. They also risk heavy dependence on a few major trading partners, making them vulnerable to economic downturns in those countries. Additionally, small economies can be more susceptible to external shocks, such as changes in global commodity prices or financial crises (Baldersheim and Keating, 2015).

Diversification can be limited due to resource constraints, which leads to an overreliance on a narrow range of industries or exports. Infrastructure and connectivity gaps may hinder their ability to engage effectively in regional and global trade. Achieving economies of scale can be challenging, making it difficult to compete with larger economies that can produce goods more cost-effectively (Katzenstein, 2016). Regulatory and administrative capacity may be insufficient to enforce trade agreements and implement reforms (Fox, 2002).

Access to international capital markets can be restricted, hindering investments in critical areas. Complying with rules of origin can be more complex and costly for small economies, and transitioning to a more open economy involves significant adjustment costs. They might also lack negotiating capacity and face currency volatility.

To address these challenges, small economies often need targeted support, capacity building, and technical assistance from regional and international organizations. This assistance can help them maximize the benefits of regional integration and

trade liberalization while mitigating potential downsides. Additionally, forming regional alliances or trade blocs with other small economies can provide them with collective bargaining power and shared resources to enhance their global competitiveness.

### **4.2. Open economies and regional integration**

Countries with greater openness to trade, participating in regional integration and trade liberalization, confront a set of distinctive challenges.

In terms of open economies, the experience of the Philippines illustrates the distinctive challenges encountered in the context of regional integration. As an open economy, the Philippines has pursued integration through various agreements, including participation in the Association of Southeast Asian Nations (ASEAN) Free Trade Area. Despite the opportunities for increased trade, the Philippines faces substantial challenges related to competition from lower-cost producers within the region. The influx of imported products from neighboring ASEAN countries has intensified price competition and put significant pressure on local industries, particularly in the agricultural sector. Furthermore, the Philippines must navigate complex regulatory frameworks and establish compliance with varying standards across member countries, which can overwhelm local businesses with the burden of adjustment. This situation highlights how an open economic stance, while beneficial for accessing broader markets, can also expose domestic industries to heightened competition and regulatory challenges, necessitating proactive policy measures to support affected sectors during integration efforts.

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Adapting to the altered economic landscape can involve substantial adjustment costs, as heightened competition within the region may disrupt certain sectors, necessitating expensive transitions to maintain competitiveness (Sampson and Woolcock, 2003). Open economies, although being beneficiaries of international trade, also grapple with intensified global competition (Vamvakidis, 1998). Regional integration can expose them to competitors from countries with lower production costs and different comparative advantages.

Furthermore, they must navigate intricate regulatory frameworks and agreements, often impacting sectors subject to rigorous oversight. Intellectual property protection is a critical concern, particularly for innovation and technology-based industries (Kharas et al., 2008). Some of these countries are exposed to currency fluctuations, influencing export competitiveness and international financial stability. Reliance on global supply chains can be vulnerable to disruptions, including geopolitical events or natural disasters in other regions. Reductions or eliminations of tariffs in trade liberalization can lead to a decrease in government revenue, necessitating alternative fiscal measures.

Balancing the interests of domestic industries, workers, and consumers poses a substantial challenge. Perceptions that trade openness harms local sectors or employment can lead to political backlash and protectionist demands, even within countries that have reaped the benefits of open trade. Additionally, non-tariff barriers, such as varying product standards and regulations in partner countries, can pose impediments to trade. Effective strategies for managing these challenges require proactively adjusting to competition, strengthening intellectual

property protection, managing currency risks, enhancing supply chain resilience, and implementing policies that harmonize the interests of diverse stakeholders. This is essential for steering through the complexities of trade liberalization while preserving national interests and ensuring equitable globalization benefits (Ng and Yeats, 1996).

In light of all these controversial issues, the equitable distribution of integration benefits poses a considerable challenge, leading to varying motivations for participation in integration processes. Moreover, disparities arise depending on whether participating countries share similar characteristics, such as the size of their economies, their degree of openness, and their level of economic development—small or large, open or closed, developed or developing. Consequently, this divergence results in diverse approaches, different development paces, and varying integration outcomes.

### 5. A new “conceptual” typology of regional integration agreements

To understand the different approaches and outcomes of different integration communities around the world, a more conceptual typology can be derived based on the different forms of economic integration discussed in the previous section (Table 1). On the basis of the policies and freedoms involved, different forms of economic integration can be distinguished:

1. Internal static integration (involving freedom of movement within the community). This category encompasses the removal of barriers to trade and economic activity between member countries, leading to greater internal economic integration.
2. External static integration (covering common external barriers). This category refers to common external barriers

**Table 1.** Conceptual typology of economic integration agreements

		Preferential Trade Agreement	Free Trade Areas	Customs Union	Common market	Economic union	Economic and monetary union	Full economic integration	Political union
<b>Internal static integration</b>	Goods (tariffs)								
	Goods (non-tariff, etc.)								
	Services								
	Capital								
	Labour								
<b>External static integration</b>	Goods (tariffs)								
	Goods (non-tariff, etc.)								
	Services								
	Capital								
	Labour								
<b>Dynamic integration</b>	Common customs tariff								
	Monetary policy								
	Economic policies								
	Sovereign policies								
Legend:		complete	partial	missing					

**Source:** Compiled by the author.

imposed collectively by participating countries on non-member countries. Such barriers, such as tariffs and trade regulations, create a different trading environment for the integrated community.

3. Dynamic integration (involving common economic and other policies) that goes beyond trade to encompass broader economic and political cooperation among member countries. It aims to create a more unified economic and political entity with shared policies and institutions.

If this conceptual typology is applied to the stages (or types) of agreements outlined in economic integration theory, it can be summarised that internal static integration

refers to free trade areas and customs unions, external static integration is inherent in the common market and economic unions, while economic and monetary unions, full economic integration and political union cover the parameters of dynamic integration.

Developing such a conceptual typology of economic integration agreements can help both policy makers and scholars to better understand different approaches to integration. It highlights different levels of economic cooperation, policy harmonization, and institutional development, offering a framework for assessing the depth and scope of integration among nations.

This expanded typology is essential for analysing and comparing different integration arrangements, identifying their specific characteristics and assessing the potential implications for the countries involved. It also highlights the evolving nature of integration, where countries can progress from one level to another, reflecting the dynamic nature of international economic relations.

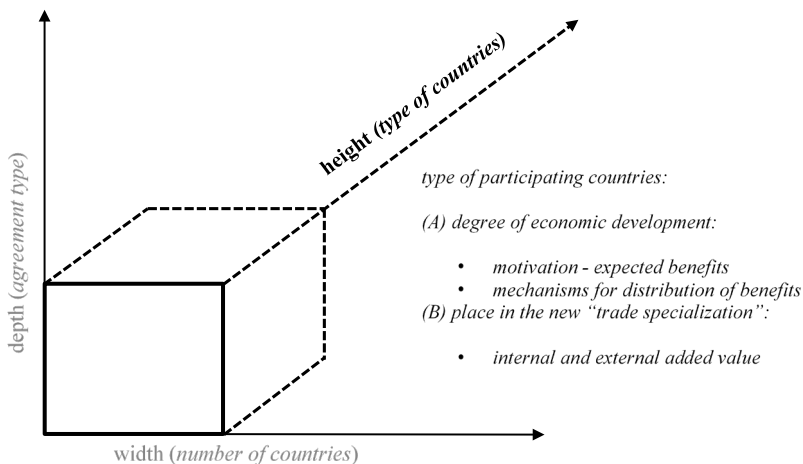
### 6. Transition to a three-dimensional evaluation of regional economic integration

In response to the multifaceted impact of integration processes (both as static and dynamic effects), particularly the distribution of benefits and motivations for participation for small and open economies, we propose a shift from a two-dimensional to a more comprehensive three-dimensional framework for assessing integration processes (Figure 2).

This expanded evaluation encompasses the following factors that influence both the participation as well as the results and benefits

of participation in integration agreements for different types of countries:

1. Genesis: examining the origins and context of integration processes. Here the focus is on understanding how and why the integration process came into being. Factors to consider include the historical, political, and economic background, as well as the motivations of participating countries. This dimension allows for an in-depth analysis of the historical and geopolitical factors influencing integration.
2. Motivation: evaluating the incentives for participation, expected benefits, and mechanisms for their distribution. This group of factors takes into account the economic and strategic interests of nations, as well as their expectations regarding the benefits of integration. This dimension allows for a better understanding of whether countries are seeking to increase trade, enhance economic development, gain geopolitical advantages, or achieve other specific goals through integration.



**Figure 2.** From two to three dimensions in evaluating integration processes

Source: Created by the author.

3. Development and results: analysing the evolution and outcomes of integration. This is the broadest and most comprehensive category, which encompasses the entire lifecycle of the integration process. It examines how integration evolves over time, the policies and mechanisms implemented, and the outcomes or results achieved. This dimension assesses the concrete impacts of integration on economic, social, and political aspects, making it possible to evaluate the extent to which the integration objectives have been met.

Based on these three groups of additional conditions and factors, when analysing a specific integration process, in addition to the number of countries (width) and the form of integration (depth), we propose a third dimension (height), which takes into account:

1. the type of participating countries, especially in terms of the size of their economies and the degree of economic development, which makes it possible to assess their motivation for participation, the expected benefits and the mechanisms for their distribution, and
2. the place of the participants in the new "trade specialization" in terms of internal and external value added of production and trade and the possibility of pursuing and defending their national or regional geo-economic interests.

The three-dimensional evaluation offers a more nuanced and comprehensive analysis of economic integration processes. It recognizes that integration is not a one-dimensional phenomenon and that various factors, from historical context to policy development and outcomes, influence the success and effectiveness of integration agreements. Each

of the three dimensions provides a deeper understanding of integration processes. By examining their genesis, motivation, and development, analysts can identify the drivers of integration, assess whether the intended objectives have been met, and understand the evolving nature of these agreements. The three-dimensional evaluation also facilitates comparative analysis of different integration processes. By considering the genesis, motivation, and development dimensions, analysts can compare agreements across regions and time periods, providing insights into the diversity of integration models.

Such a comprehensive evaluation framework is valuable for policymakers, scholars, and analysts seeking a deeper understanding of the dynamics of economic integration in a global context. Moreover, applying the three-dimensional evaluation framework can yield specific outcomes for small and open economies engaged in regional integration.

For instance, when examining the genesis of integration agreements, policymakers can identify historical precedents and contextual specificities that have either fostered or hindered cooperation. This understanding can inform the creation of tailored agreements that address particular vulnerabilities, such as those related to trade imbalances or dependency on a narrow range of exports. In terms of motivation, recognizing the diverse incentives of different economies can lead to the design of integration strategies that align more closely with the development goals of small economies. By focusing on shared objectives such as technology transfer, infrastructure development, or improved market access, small economies can negotiate terms that enhance their economic standing within the regional bloc. Finally, paying attention

to the development of integration outcomes allows for ongoing evaluation and adaptive policymaking. For example, if the integration process is found to disproportionately benefit larger economies within the group, small economies can push for policy adjustments that ensure a more equitable distribution of benefits. These proactive measures not only safeguard their interests but also enhance the overall effectiveness of integration efforts.

As a result, the comprehensive lens provided by the three-dimensional framework empowers small and open economies to navigate the complexities of regional integration more effectively, fostering sustainable economic growth and resilience in a competitive global environment.

### **7. Opportunities for small and open economies in using integration as a foreign trade policy tool**

This proposed new perspective highlights the evolving role of participation and engagement in integration processes, particularly for smaller, open, and less developed economies. The suggested new understanding of integration and its typology allows to justify the view that increasingly participation (and engagement) in integration processes is perceived as a new tool of active foreign trade policy to answer the structural changes in global trade.

For small, less developed and/or highly open economies, integration serves as a multifaceted foreign trade policy tool. It enables them to reduce vulnerability to external shocks, enhance competitiveness, preserve added value, and strengthen regional resilience. Smaller economies recognize that participation in integration processes can be a strategic means of advancing their interests and protecting their economies in

an increasingly interconnected world. This includes:

1. Integration for intra-community import substitution. Small, open economies often face challenges related to their exposure to international markets (Easterly and Kraay, 2000). These countries are susceptible to external shocks and global economic fluctuations. By actively participating in integration processes, they aim to reduce their dependence on foreign markets and foreign goods. Integration can serve as a tool for promoting intra-community import substitution, allowing these nations to replace some of their external trade with internal trade among member countries. This can help mitigate the vulnerabilities associated with global market fluctuations.
2. Stimulating regional and national competitiveness. Participating in integration processes provides an opportunity to stimulate regional and, consequently, national competitiveness (Kitson, Martin and Tyler, 2004). When smaller and less developed economies engage with their neighbours in regional integration, they can jointly invest in infrastructure development, technology transfer, and human capital. This collaboration can lead to increased efficiency, productivity, and competitiveness on a broader scale. Smaller and less developed economies can enhance their global standing by participating in integration agreements that promote cooperation and resource sharing among member countries.
3. Preserving "domestic" added value. Integration also plays a role in preserving "domestic" added value (Banga, 2014). In smaller and less developed economies, there is often a concern that a substantial portion of the value generated from

production and trade flows out to larger, more developed economies. By actively participating in integration, these nations can work toward retaining a more significant share of the value within the region. This is particularly relevant in industries where smaller economies possess unique capabilities or resources.

4. **Leveraging regional integration processes.** Regional integration processes are witnessing increased activation in various parts of the world. Smaller and less developed economies realize that they can leverage regional integration as a means to enhance their position in the global economy (Briguglio, 1995). Through regional collaboration, they can negotiate with larger and more powerful trade partners from a more advantageous position. This enables them to better protect their interests and ensure that their specific economic strengths are recognized and utilized.
5. **Fostering regional economic resilience.** Regional economic resilience is essential in the face of global economic uncertainty, especially for small, open and less developed nations (Geithner, 2007). By building stronger regional economic networks, they can create a buffer against external shocks. Through integration, these nations can work together to develop contingency plans, enhance crisis management, and collectively address challenges such as economic downturns or disruptions in global supply chains.
6. **Overcoming global trade barriers.** The intensified participation in regional integration processes is a response to the challenges and barriers posed by the global trade landscape (Baldwin, 2006). Smaller economies often find it challenging

to navigate the complexities of global trade rules and regulations. By aligning with neighbouring countries in regional agreements, they can overcome some of the hurdles associated with global trade. In essence, they use regional integration as a means to create new trade opportunities and break down global trade barriers.

To illustrate the practical implications of regional integration for small and open economies, consider the case of Costa Rica, which has successfully leveraged Central American integration efforts to boost trade and investment. By participating in regional agreements, Costa Rica has not only reduced tariffs but also established common standards that facilitate market access. Similarly, the Baltic States have benefited from their integration into the European Union, which has provided them with access to broader markets while allowing for the development of joint infrastructure projects that enhance connectivity. These examples underscore the potential for regional integration to stimulate economic growth, foster innovation, and create resilience against external shocks.

Furthermore, regional integration initiatives, such as the African Continental Free Trade Area (AfCFTA), exemplify how smaller economies can band together to enhance their collective bargaining power. Through joint negotiation efforts, member states strengthen their position against larger trading partners and create opportunities for intra-regional trade that can reduce reliance on external markets. Policymakers in small economies should consider similar strategies, ensuring that integration processes are not only viewed as opportunities for economic cooperation but also as platforms for advocating for equitable terms in global trade negotiations. This approach can lead

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to sustainable economic development and empower smaller nations to capitalize on their unique resources and strengths.

While integration fosters regional cooperation and economic strength, it also raises questions about potential regional protectionism at the global level. Smaller economies may use regional integration to advance their interests, potentially at the expense of global trade liberalization. All this, together with the intensification and proliferation of regional integration processes observed in recent decades, gives us reason to conclude that in the modern world economy, economic integration is considered, and actually used, as a means of achieving a new type of barriers to free trade - regional protectionism at the global level.

## 8. Conclusion

Economic integration has become a dominant and truly global trend in recent decades, with regional initiatives shaping diverse agreements and communities worldwide. The evolution of global trade towards greater openness, reduced discrimination, and the broadening scope of trade agreements reflects the complex dynamics of structural transformations in the world economy. As globalization, regionalization, and evolving trade dynamics continue to intertwine, a multifaceted understanding of global trade processes becomes imperative.

The deepening of regional integration, particularly in trade, has given rise to diverse agreements and communities worldwide. The shifting role of integration in foreign trade policy, coupled with the potential of regional integration as a pathway to global trade liberalization, prompts contemplation on the future of international economic relations. Small and open economies stand to gain in

various ways, from enhancing competitiveness to fostering regional economic resilience. As we look ahead, the proposed three-dimensional evaluation framework emerges as a crucial tool for understanding the genesis, motivation, and outcomes of integration processes.

The article has explored the significant role of regional integration as a strategic tool in the foreign economic policies of small and open economies. The findings indicate that regional integration not only mitigates vulnerabilities to external shocks but also enhances competitiveness and contributes to the preservation of added value within these economies. By leveraging regional partnerships, small and open economies can create a robust framework for economic resilience and sustainable growth amid the complexities of globalization.

For policymakers, the insights drawn from this study highlight the need for proactive engagement in regional integration initiatives. By fostering collaborative frameworks, countries can enhance their collective bargaining power and optimize their economic strategies. Practical measures should involve investment in regional infrastructure, capacity-building programs, and the development of tailored trade policies that cater to the unique challenges faced by smaller economies.

The article contributes to the broader discourse on economic integration by providing a nuanced framework for understanding the dynamics of regional cooperation. It calls for a revision of existing theories to take into account the diverse motivations and outcomes associated with integration processes, particularly for small and open economies. This fresh perspective prompts further investigation into the evolving nature

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of economic integration theories and their applicability across various contexts.

Despite these contributions, this study has its limitations. The analysis primarily focuses on the theoretical aspects of regional integration, and empirical case studies examining the real-world impacts on small economies were beyond the scope of this research. Additionally, the rapidly changing global landscape necessitates continuous evaluation of the integration strategies employed by different economies.

It is vital for future research to focus on empirical case studies that examine the practical effectiveness of regional integration strategies in various contexts. For instance, exploring how specific small economies have successfully navigated their integration efforts could provide valuable insights into best practices that can be replicated elsewhere. Additionally, research should address the impacts of digital transformation and technological advancements on trade dynamics, particularly how these factors can either facilitate or hinder the integration of small economies into global markets. Moreover, investigating the implications of geopolitical shifts and their effects on regional integrations will be essential in formulating adaptive strategies that ensure resilience in an evolving economic landscape. By systematically exploring these aspects, scholars can contribute to a more nuanced understanding of the intersection between regional integration and economic development. Ultimately, such research will not only enrich the academic discourse but also will equip policymakers with the evidence-based strategies needed to foster sustainable growth in small and open economies amidst the complexities of international trade.

In summary, regional integration presents a valuable pathway for small and open economies to navigate the complexities of the modern economic landscape. By acknowledging the multifaceted implications of integration, this study underscores the importance of the strategic participation in regional economic integration initiatives for achieving sustainable and inclusive economic growth.

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