

ЭКОНОМИКА

A SHORT LOOK AT THEORIES ON INTERNATIONAL ECONOMICS, AND GROWTH SCENARIO FOR KAZAKHSTAN UNDER MODERN THEO- RIES

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¹Under capitalism, man exploits man. Under socialism, it is just the reverse.

-Anonymous-

Economists traditionally divide the subject matter of international economics into two parts: international trade theory, which extends microeconomic analysis to international questions, and international finance, primarily the theory of balance of payments, or open-economy macroeconomics, which applies macroeconomic analysis to international problems at the aggregate level. In the first part, quantities of various goods produced, consumed and traded, and related decisions are concerned. Major concerns included in the second part are level of employment and output in each economy as well as changes in the general price level, balance of payments and exchange rates. This implies that international trade and finance must be understood in a much broader sense than simply the intercountry flow of goods and financial resources.

The study of international economics has always been an especially lively and controversial part of economics. Many of the key insights of modern economic analysis first emerged in 18 and 19th centuries over international trade and finance. However, there was never a time when the study of international economics was as important as it is today because many socialist countries are opening themselves into international economic relations. Keeping this in mind, one may simply claim that to best analyze the transition, we should know where they started from and where they are going. To this end, it is desirable to first remind ourselves of basics of international economic relations of a socialist economy or how ex-socialist countries planned and implemented their external economic activities and then how they are determined in market economies. This short analysis is considered necessary to explore how transition might have affected Kazakhstan's international economic relations afterwards.

International Economic Relations under Socialism

Every society has to organize its both domestic and external economic activities through a network of institutions, which are supposed to make the most possible efficient allocation of its scarce resources. Socialism tried to accomplish it for over seventy years via commands in plan form from the center. Socialism, sometimes called command economy, is actually more than state regulation of the market. Rather, it is the effort to replace the market with centralized economic order as Marx criticized the market for creating anarchy. To him, planning was the best alternative. The nature and extent of the international economic relations of socialist countries, especially those in the USSR, with other countries is important to know

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for varied purposes. For the purpose of this thesis, we examine these relations from two different points of view. First, we consider the USSR as one big country as it was. To begin with, we must realize that the USSR was not a closed economy in its strict sense because it was trading with other socialist countries as well as with non-socialist countries. Second, socialist countries in fact were making up a block and they, as many claimed, enjoyed 'bloc autarky'.

Socialist economies are generally thought as 'trade averse' economies.² The reason that lies behind this idea is that foreign trade was integrated into the overall planning. In fact, it is not only foreign trade but also all kinds of other economic relationships were part of the central plan, meaning that, all external economic activities were state monopoly and were planned and conducted through some state institutions. What are those institutions? All trading activities were conducted through Foreign Trade Organizations (FTO) attached to the Ministry of Foreign Trade (MFT) or to the industrial ministries. The Vneshtorgbank or Bank for Foreign Trade (BFT) was also partly accounted for this kind of institutions. Bank for Foreign Trade together with State Bank (Gosbank) used to prepare a balance of payments account for the payment of foreign trade transactions. Besides, there was another organization in the USSR namely State Committee for Foreign Relations, which was responsible for managing Soviet foreign aid program. In summary, the state planning commission, the state bank, the bank for foreign trade, and foreign trade organizations made up a foreign trade monopoly. State committee for foreign relations was primarily a political rather than an economic institution. Table 1 exhibits shares of Soviet type economies in world GDP and world trade and enhances our understanding of the socialist economies as well as their participation in the world economy.

Table 1. Shares of Economies in World GDP and Trade, 1.

Shares in World GDP		Shares in World Trade
Industrialized West	63%	65%
Socialist Countries including China	24%	10%
Other	13%	26%

Source: Gregory and Stuart (1); pp. 1.

Although socialist countries' share of GDP in world GDP is 24%, their share in world trade is only 10% compared to those of industrialized west's 63% and 65% in world GDP and trade, respectively.

Socialist countries were planning every economic activity in standard material balance. As such, they were also planning foreign economic activities in it. In the standard material balance, imports used to be on the resources side and exports on the uses side. Foreign trade, in fact, acted to fill deficits in the material balance. When planned resources seemed to be insufficient and if it was impossible to increase the

² The socialist economy avoids heavy reliance on foreign suppliers, even if a product may be available more economically from abroad (Gregory and Stuart (1989), pp. 363). In 1920s and 1930s, Soviet trade ratios declined, but expanded later on after 1950s. In the seven year period of 1959-1965, its trade with developed capitalist countries more than doubled to a total of 3.1 billion dollars in 1965 while its total trade with close to 100 countries was \$16.6 in the same year (Potolichev 1967).

growth or savings, imports were necessary. In case imports were necessary, then ways had to be found to increase exports in order to accomplish trade balance and thereby to avoid a balance of payment problem. From this characteristic of foreign trade, we can draw two conclusions: First, foreign trade was a secondary activity to domestic trade. Second, imports had priority over exports for a socialist country. Exports were to pay for imports.

Succinctly, the essence of the plan formulation is the material balance technique. A balance is in fact a table that identifies sources (supply) and uses (demand) of both intermediate and final products. This table, on the supply side, shows (i) domestic production, (ii) stocks on the hand and (iii) imports during planning period. On the uses (demand) side, they show (i) inputs used for production (interindustry demand), (ii) investment, (iii) consumption, and (iv) exports. An example of material balance is represented in Table 2 below.

Table 2. Material Balance of a Plan

Resources (Supply)	Uses (Demand)		
1. Domestic production	1500	1. Inputs for production	600
2. Imports	300	2. Investment	300
3. Stocks	200	3. Consumption	300
		4. Exports	800
TOTAL	2000	TOTAL	2000

Source: Lavigne (1995); pp.

Normally, both sides in the balance must be equal. Discrepancies are reconciled through adjustment of certain items of the balance.

Shortcomings of International Economic Relations in Socialism

Deficiencies of any economic system directly influence its relations with other nations. Since the Soviet type economies are argued to be characterized by the existence of certain type of deficiencies, was it able to sustain its foreign economic relations easily? Of course not. There were problems, especially with pricing, convertibility of ruble-Russian currency-and balance of payments. Trade among socialist countries was mainly on a barter basis. In trading with non-socialist countries, they had to use world market prices because they could not influence them on their own. Similarly, because ruble was not convertible, countries first had to export in order to have enough stock of foreign currency to pay for imports.

Prices in socialist countries used to be established by state agencies rather than by sellers and buyers, as is the case in a market economy. It implies from it that prices were not equalizing supply and demand. Prices in those countries remained fixed over long periods of time³. This would let government save revision cost and evaluate the enterprise performance easily across time. At official prices, overall demand for both consumer and producer goods exceeded their supply. Socialist prices generally did not reflect the scarcity values and real cost of production ignoring opportunity cost so it was difficult to price realistically both imported and

³ Prices used to be engraved on the products already during the production, so that these products would sell for the same price in a big geography.

domestic goods.⁴ On the other hand, western goods did reflect scarcity values as opportunity cost of their production. Thus, their costs were minimized. Since comparison of domestic and import prices could result in an unrealistic picture of socialist economies, they could not establish an import-export basket (trade pattern). Similarly, since official prices were not rational guides to production, their economic development was not demand oriented. Excess demand gave the planners some power to overrule the market in allocating resources, so that the state could implement its growth priorities industry by industry and region by region. Fulfilling the plan targets was important and this led the firms to choose quality and assortment to make plan targets easier to realize than matching users' preferences or requirements in the best possible way. The net result was the reduced use value of what was produced.

It is also of interest to know that the currencies of the socialist countries were not convertible into currencies of capitalist countries. What this means is they could not be sold or purchased in the world open market for purposes for which they reflected real exchange rate.⁵ Of course, there were exceptions when people could convert their money into the domestic currency. For example, tourists were allowed to change their money in order to do shopping inside these countries. As could have been expected, inconvertibility of socialist currencies created black market for foreign currencies. This became much evident especially after 1s as depicted in Table 3.

Table 3. Official and Black Market Exchange Rates for Soviet Union and Eastern European Countries Currencies, 1989

	Official Rate	Black-Market Rate
Soviet Union (ruble)	\$1.63	\$0.10
East Germany (ost mark)	0.54	0.04
Poland (zloty)	0.0003	0.0001
Hungary (forint)	0.17	0.13
Czechoslovakia (koruna)	0.17	0.03

Source: Business Week, November 27, 1989, in Yarbrough and Yarbrough (1997); pp. 889.

The other result of inconvertibility was barter-oriented trade. Sales between socialist countries were negotiated on barter basis. As such, the value of commodities traded used to balance. In the case of East-West trade, on the other hand, barter trade was required by the Eastern partner but this rarely occurred. Trade among them was pursued on a multilateral basis, which required the clearance of the transactions in a convertible western currency or, trade was financed by credit arrangements. Consequently, the intra-bloc trade did not reach its maximum level because of efforts to achieve the planning purposes, the need to balance imports and exports and bilateral trade agreements. The other problem that prevented the

⁴ Even it was difficult to minimize cost because factor movement to profitable sectors or places was not permitted due to inexistence of property rights.

⁵ There was an official exchange rate, which was a statistical unit of account.

foreign economic relations of the socialist countries from developing to attainable level was the problem of the balance of payments.

Normally, the planned economies were not expected to run into balance of payments problem because their imports and exports were planned for the occurrence of no such problem. If either export or import exceeded, necessary adjustments were made to balance the other. As for intra-bloc trade is concerned, there was usually no balance of payments problem because it occurred, if at all, under bilateral agreements based on the principle of barter. The balance of payments problems are a matter of the demand for and the supply of convertible western currencies. It may as such be realized that sustainable maximum mutually beneficial foreign trade under such conditions was not possible. Because of those aforementioned reasons, share of socialist countries in world trade was much lower than the developed countries as could be seen from Table 4. For example, the USSR suffered balance of payments problem, especially in 1960's due to these very reasons. Recurrent gold sales serves as a sufficient indication of the USSR suffering from hard currency deficit.⁶ However, this might partly be the result of loans and credits extended to LDC. The non-trade components must also have contributed to the Soviet balance of payments problem. However, since the reliable data to this effect are not available, their exact counter function to the problem is difficult to ascertain.

Table 4. Trends in World Exports, 1970-1994

	Official Rate	Black-Market Rate
Soviet Union (ruble)	\$1.63	\$0.10
East Germany (ost mark)	0.54	0.04
Poland (zloty)	0.0003	0.0001
Hungary (forint)	0.17	0.13
Czechoslovakia (koruna)	0.17	0.03

Source: Todaro Michael, "Economic Development", 1, pp. 1.

Lastly, institutional weaknesses may have also caused insufficient development of international economic relations. Institutional weakness considered here refers to the continuous lack of effective communication —upward, downward, horizontal-between government institutions such as planning agencies, ministries, political leaders, etc. Another aspect of institutional weakness that beset countries other than Russia was inappropriate international transfer of planning practices into local conditions. We will discuss this topic (institutional change/reform) in later chapters.

International Trade Theories of Market Economy

Adam Smith who has been considered as the father of free market economy advocated free trade among countries as means of enlarging a country's wealth. He developed theory of *absolute advantage*, which suggests that a country should export those goods and services for which it is more productive than other countries are and import those goods and services for which other countries are more pro-

⁶ See Weiss (1966): pp. 577.

ductive than it is. However, this theory suggests that no trade would occur between two countries if one country has absolute advantage in the products traded between them. David Ricardo solved this problem by developing the theory of *comparative advantage*. This theory states that a country should produce and export those goods and services for which it is relatively more productive than are other countries and import those goods and services for which other countries are relatively more productive than it is. This theory also has a question: What determines the products for which a country will have a comparative advantage? To answer this question, two Swedish economists, Eli Heckscher and Bertil Ohlin, developed their theory of relative factor endowments. Their theory is now referred to as the *Heckscher-Ohlin model*. They developed their theory based on two observations. First, factors (or types of resources) vary among countries. Second, goods differ according to the factors that are used to produce them. Based on these observations, they conceptualized that a country will have a comparative advantage in producing products that intensively use resources (factors of production), which it has in abundance. For example, Ukraine has comparative advantage in wheat growing because of its abundance of land.

Those above-mentioned trade theories were later referred to as classical country-based trade theories. These theories can well explain *interindustry trade*, which is the exchange of goods produced by one industry in one country for goods produced by a different industry in a different country, such as exchange of Kazakh wheat for Japanese type players. However, much international trade consists of *intraindustry trade*, which is between two countries of goods produced by the same industry. For example, Kodak sells film made in US factories to Japan while Fuji sells film made in Japanese factories to US. While Japan exports Toyotas to Germany, Germany sells BMWs to Japan. Intraindustry trade accounted for approximately 40% of world trade in 1980s (Griffin and Pustay, 1996) and it is not predicted by country-based theories. This necessitated development of firm-based international trade theories. Additionally, it was recognized that labor is not a major factor of production and capital is absolutely mobile.

In 1961, Swedish economist Steffan Linder sought to explain the phenomenon of intraindustry trade. He hypothesized that international trade in manufactured goods results from similarities of preferences among consumers in countries, which are at the same stage of economic development. In his view, firms initially manufacture goods in order to serve their domestic market. As they look for exporting opportunities, they discover that the most promising foreign markets are in countries in which consumers' preferences resemble those of their own domestic market. For example, Sony sold its first Walkman radio domestically. Observing the product's success in the country, it quickly expanded its distribution to Canada, USA and Europe because consumers in these countries are greatly similar in incomes and preferences to those in Japan. Linder's theory is called *country similarity theory*. It is especially useful in explaining trade in differentiated goods such as automobiles, expensive electronics equipment, etc. for which brand names and product reputations play an important role in consumer decision-making.

Another firm-based theory is *product life cycle theory*, which originated in marketing field to describe the evolution of marketing strategies as a product matures. The theory, which was developed by Raymond Vernon from Harvard Business

School in Is, traces the roles of innovation, market expansion, comparative advantage, and strategic responses of global rivals in international production, trade and investment decisions.

Most recent explanations of pattern of international trade, developed in 1980s by Paul Krugman and Kelvin Lancaster. They examine the impact on trade flows of *global strategic rivalry* between multinational companies. According to this view, firms struggle to develop some sustainable competitive advantage, which they can then exploit to dominate the global marketplace. Like Linder's approach, global strategic rivalry theory predicts that intraindustry trade will be commonplace. However, it focuses on strategic decisions, which firms adopt as they compete internationally. These decisions affect both international trade and international investment.

The most recent contribution to international trade theory has come from Michael Porter, Harvard Business School professor. His theory has been named as the *theory of national competitive advantage*, which states that success in international trade comes from the four country and firm specific elements: factor conditions, demand conditions, related and supporting industries and finally, firm strategy, structure and rivalry. In fact, Porter's theory is a hybrid: It blends the traditional country-based theories that emphasize factor endowments with the firm-based theories that focus on the actions of individual firms. Countries (governments) play a critical role in creating an environment that can aid or harm firms' ability to compete internationally, but firms are the actors that actually participate in international trade.

In summary, no single theory of international trade explains all trade flows among countries. The classical, country-based theories are useful in explaining interindustry trade of homogeneous, undifferentiated products such as agricultural goods, raw material, and processed goods like steel and aluminum. The firm-based theories are more helpful in understanding intraindustry trade of heterogeneous, differentiated goods like televisions, cars, many of which are sold on the basis of their brand names and reputations. And, in many ways, Porter's theory synthesizes the features of the existing country-based and firm-based theories.

International Investment Theories

Although trade theories can explain both interindustry and intraindustry international trade, they are not sufficient to explain international investment. Why do firms invest in other countries? One may simply answer it "Because average rates of return are higher in foreign markets". However, given the pattern of FDI between countries, this answer is not satisfactory: Canada and UK are both major sources of FDI in US and important destinations for FDI from US (Griffin and Pustay, 1). Average rates of return in one of these countries cannot be simultaneously below the others. This requires search for another explanation for FDI. More powerful explanations for FDI focus on the role of the firm. Initially, researchers explored how firm-specific ownership (or monopolistic) advantages affected FDI. The *ownership advantage theory* suggests that a firm owning a valuable asset that creates a monopolistic advantage domestically can use that advantage to penetrate foreign markets through FDI. The asset could be a superior technology, a well-known brand name, etc. This theory is consistent with the observed patterns of interna-

tional and intraindustry FDI in the world. For example, Caterpillar, a bulldozer producer, built factories in Asia, Europe, Australia, South America, and North America in order to exploit proprietary technologies and its brand name. Its chief rival, Komatsu, has constructed plants in Asia, Europe, and the United States for the same reasons.

The ownership advantage theory only partly explains why FDI occurs. It does not explain why a firm would choose to enter a foreign market via FDI rather than exploit its ownership advantages through other means like exporting its products, franchising a brand name, or licensing technology to foreign firms. For example McDonald's has successfully internationalized by franchising its fast-food operations outside US while Boeing has relied on exporting in order to serve its foreign customers. Internationalization theory addresses this question. This theory heavily relies on transactions costs, which are the costs of entering a transaction, that is, those connected to negotiating, monitoring, and enforcing a contract. A firm must decide whether it is better to own and operate its own factory overseas or to contract with a foreign firm to do this through a franchise, licensing, or supply agreement. *Internationalization theory* suggests that FDI is more likely to occur when the costs of negotiating monitoring and enforcing a contract with a second firm are high. This way, indeed, international production will be internalized within the firm. For example, Toyota's primary competitive advantages are its reputation for high quality and its sophisticated manufacturing techniques, neither of which are easily conveyed by a contract.

Although internationalization theory addresses why firms choose FDI as the mode for entering international markets, it ignores the question of why production, either by the company or a contractor, should be located abroad. That is, is there a location advantage to producing abroad? This issue was incorporated by John Dunning in his eclectic theory, which combines location advantage, ownership advantage and internationalization advantage to form a unified theory of FDI. This theory recognizes that FDI reflects both international business activity and business activity internal to the firm. According to Dunning, FDI will occur when three conditions are satisfied: Location advantage, which is when the business activity is more profitable in a foreign location; ownership advantage, which is when the firm owns some unique competitive advantage to overcome the disadvantages of competing with foreign firms on their territory; internationalization advantage, when the firm benefits more from controlling the foreign business activity than from hiring an independent local company to provide the service.

Factors Influencing FDI

There are numerous factors that may influence firms' decisions to undertake FDI. They can be classified as supply factors, demand factors, and political factors.

Supply factors are affected by a firm's costs. Some most important supply factors, which may impact a firm's decision to undertake FDI, are production costs, logistics, availability of natural resources and access to key technology. Firms may also engage in FDI in order to expand the market for their products (demand factors). The demand factors include customer access, marketing advantages, and preservation

tion of competitive advantages. Political factors may also enter into a firm's decision to make FDI. Firms may invest in a foreign country in order to avoid its trade barriers or to take advantage of its economic development incentives.

On the other hand, many critics believe that FDI is a Trojan horse; it looks good on the outside but carries the seeds of national devastation. FDI critics generally raise four objections. First, they argue that FDI may result in foreign control of the national economy: Foreigners' ownership of natural resources like oil, gas, mineral deposits may mean that these nonrenewable assets are exploited for the short term gain of the foreigners, not for the long term benefit of host country and its citizens. Second, some claim that FDI may be used to seize a country's advanced technologies: foreign companies are often able to buy struggling high technology firms thereby acquire emerging technologies cheaply. Third, some believe that FDI may lead to a reduction in R&D efforts in a country: when a foreign company buys a domestic firm, it consolidates R&D activities back at its headquarters, drying up research opportunities and jobs for domestic scientists. Finally, FDI may also lead to a reduction in the development of human capital in the host country: foreign companies generally reserve the best jobs in their foreign affiliates for home-country managers, reducing opportunities for host-country citizens to acquire high-level training and experience, and improve their skills.

Growth Scenario For Kazakhstan Under Modern Theories

It is considered instructive to discuss certain natural characteristics of Kazakhstan in order to better understand the potential direction of its economic relations with other countries. It is established that Kazakhstan is moving away from its socialist past to become increasingly integrated with world trade. Kazakhstan can be cited as a land-abundant, natural resource-rich and labor-scarce economy. According to the theory of international trade, Kazakhstan is expected to increasingly specialize in areas of its comparative advantage, which appear to include, as important components, natural resource exploitation and processing activities, agriculture, and mineral extraction. Specifically, Kazakhstan is richly endowed with oil resources, deposits of coal, aluminum, copper, zinc, etc. Its terrain, soils and climate have encouraged in its certain territories broad-acre agriculture, and sheep and cattle grazing. Kazakhstan, as well-endowed with all manners of natural resources, is expected to take the maximum advantage of opportunities. Better still, it can embark upon a long-term development path on which it enjoys a growth rate higher than it can achieve with another growth policy. To the extent that factor endowments govern the structure of comparative advantage, one would expect Kazakhstan to export natural resources, processed or raw, and land-intensive goods and import technological and labor-intensive goods. Also, given the fact that its production almost stopped during transition, it is certainly expected to import all kinds of labor and technology-intensive goods.

As for the link between production factors and growth is concerned, Kazakhstan should accumulate capital and technology to take advantage of its natural resources. In Kazakhstan, which is a relatively labor-scarce economy, capital is likely to be substituted for labor so capital accumulation in form of labor-saving technology is crucial for its growth. We think that it can accumulate the required technology and

capital through international trade and FDI and utilize it via well-educated human capital. The accumulation is particularly crucial for the development of the sectors like oil and gas and agriculture in which Kazakhstan has comparative advantage. It may be argued that as technology and capital are accumulated, the production frontier of the country will move outward, more of everything can be produced.

We may consider natural resources abundance of Kazakhstan in a way that it affects its growth thereby the shape of its foreign economic relations. To assess the effects of the abundant natural resources on its foreign relations, a review of related literature is made. Sachs and Warner (1995), on review of a vast literature and empirical analysis of 97 developing countries between 1970 and 1989, find that resource-poor economies often vastly outperform resource-rich economies in growth. However, economic theory does not provide a convincing explanation as to why resource abundance should be inherently disadvantageous from the point of economic growth of a country. In fact, the additional rents and foreign exchange obtained from commodity exports should permit higher levels of investment and greater capacity to import capital goods with which to accelerate economic growth (Auty, 2000). Sachs and Warner (1995) argue that the oddity of resource-poor economies outperforming resource-rich economies has been a constant motif of economic history. In the 17th century, resource-poor Netherlands eclipsed Spain despite the overflow into it of gold and silver from its colonies. In the 19th and the 20th centuries, resource-poor countries such as Switzerland and Japan surged ahead of resource-abundant economies such as Russia. In the past thirty years, the fast-growing countries of South Korea, Taiwan, Hong Kong and Singapore of East Asia have been the resource-poor countries while many other resource-rich especially oil-rich countries of Mexico, Nigeria, Venezuela have gone bankrupt. Indeed, this is puzzling because natural resources raise the wealth and the purchasing power over imports, so that resource abundance might be expected to raise an economy's investment and growth rates. Many oil-rich economies have aimed to use their vast oil revenues to finance diversified investments for them to serve as basis of a 'big push' in industrial development.

Auty (2000) also argues that variations in economic performance are caused by differences in the quality of governance that are linked through the type of political state and pattern of structural change to the natural resource endowment. According to him, resource-rich countries are likely to distort their economies severely and thereby compound the inherited problems of the shift from resource-driven growth to skill-driven growth. What has happened to resource-rich countries may also happen to Kazakhstan as well. In this sense, one may ask whether resource-abundance of Kazakhstan may help it accelerate growth in all industries and overall development in the country: with an intelligent public policy, "Yes". But, resource abundance of Kazakhstan may have adverse affect especially on its manufacturing sector. Because when an economy experiences a resource boom, such as discovery of a new oil reserve, the manufacturing sector tends to shrink. Oil production uses very little labor, so it does not directly draw labor from manufacturing. From this point of view, and considering already collapsed manufacturing sector in Kazakhstan, one may argue that even if Kazakhstan is able to revive its natural resources sectors, this will not be a solution to certain problems like unemployment. This takes us to the conclusion that it primarily has to revive its manufacturing and ser-

vices sectors. For this, Kazakhstan either has to wait for vast oil revenue to finance especially its manufacturing sector or it has to encourage FDI into manufacturing sector. The former can be accomplished in the medium term at the earliest. The latter, however, can be achieved sooner than the former if a sound FDI environment is created in the country. on the other hand, Matsuyama (1992) shows that trade liberalization in a land-intensive economy could actually slow economic growth by inducing the economy to shift resources away from manufacturing and towards agriculture.⁷ In this regard, we may expect that development of oil sector in Kazakhstan will not employ much labor. In contrast, it may push labor into other sectors like trade since trade liberalization is also expected to shift labor from manufacturing. This puzzle may be expected to force a particular shape of Kazakhstan's economic relations with other countries.

Kazakhstan may also be classified as a landlocked country since it is far from West, South and South-East Asian countries and has no coastal area except its Caspian coast. In fact, any model of development, which stresses outward-looking orientation or the productivity-enhancing effects of exports for production would identify being landlocked as an impediment to growth. MacKellar, Wörtgötter and Wörz (2000) through empirical data find that landlockedness reduces average growth by about 1.5% per year.

On the other hand, its historical links with certain countries like Turkey seem to play a dominant role in the development of some kind of relations. For example, schools opened by Turkish private organizations so far have reflected Turkish private sector's interest in this nation.⁸ Further, some countries consider Turkey as a gateway to Central Asia. They form joint ventures with Turkish companies before entering Kazakhstan and they employ mostly Turkish directors (Bingol, 1998). This opinion has contributed not only to the development of Kazak-Turkish economic relations but also to overall development of Kazakhstan's economic relations with other countries. It seems that Kazakhstan will acquire, to some extent, the knowledge and technology it needs either from Turkey or from other countries through Turkey.

In sum, Kazakhstan has some advantages like its rich natural resources as well as disadvantages like its landlocked geographical position. But, what are sure of may be cited as knowledge and technology transfer into the country. It may be interesting to know that 96% of the research and development (R&D) is carried out in a handful of industrial countries, the remaining 4% takes place in a large number of developing countries, with only 15 of them doing significant R&D (Helpman, 1997). Industrial countries spend only between 1.5 to 3 percent of their GDP on R&D. But, rate of return on R&D is so high that this investment has a significant impact on output growth. In fact, R&D raises productivity, which in turn stimulates capital accumulation. Is R&D so important for economic growth? In our view, considerable evidence exists on inventive activities to have played a key role in modern economic growth. For example, the steam engine, which provided a reliable source of energy, and the dynamo, which enabled flexible use of electricity in manufacturing plants triggered economic growth and industrialization of today's developed

⁷ Quoted by Sachs and Warner (1995), pp. 5.

⁸ Since education shapes future generations of a nation, permitting those schools may show Kazakhstan's trust in Turkey and Turkish people because Kazakh governmental officials in the earlier years must have asked themselves again and again whether these schools would be beneficial to the country.

nations. However, it may take many years for the full impact of the new technology to work itself out. For example, forty years had passed from the invention of dynamo until electrification substantially raised total factor productivity in US manufacturing sector (Helpman, 1997). The message that the detailed historical studies give to us is that over the last two-three hundred years, inventions and innovations played a crucial role in raising our welfare. Not every country can invent or innovate. Some countries have to import technology from other countries.

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REVIEW OF EURASIA FOUNDATION GRANTS IN MICRO FINANCE

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The Eurasia Foundation (the Foundation), its Almaty Regional Office (ARO) supported the following micro finance projects in the Republic of Kazakhstan:

- Kazakhstan Community Loan Fund in Taldykorgan;
 - Public Fund for Assistance to Farmers in Almaty oblast;
 - Public Fund Akmola Rural Advisory Center in Akmola oblast;
 - Public Fund for Assistance to Farmers of West Kazakhstan oblast; and going to support
 - Mercy Corps International. Development and Growth of Women's Micro Enterprises in Talas oblast, the Kyrgyz Republic.
- Both, the Republic of Kazakhstan and the Kyrgyz Republic, had the primary