VERTICAL INTEGRATION AS A DIRECTION OF THE STRATEGIC DEVELOPMENT OF A HOLDING COMPANY

M. O. Orlov
Head of the staff of the Federation Council Committee on agrarian and food policy and environmental management, Moscow, Russia

Zh. N. Dibrova
K.G. Razumovsky Moscow State University of technologies and management (The First Cossack University), Moscow, Russia

S. Dimitrieva
K.G. Razumovsky Moscow State University of technologies and management (The First Cossack University), Moscow, Russia

A. O. Khmeleva
K.G. Razumovsky Moscow State University of technologies and management (The First Cossack University), Moscow, Russia

ABSTRACT

The most common form of organization of activities of domestic integrated structures are holding companies. In modern conditions, the successful development of a production company is inextricably linked with strategic management. The article discusses vertical integration as a direction for the strategic development of a holding company.

Keyword: vertical integration, strategic development, holding company, integration, enterprises, economy.

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1. INTRODUCTION
At present, in most modern models of the market economy of Russia and foreign countries, integrated corporate economic structures are being created, functioning and successfully developing.

Integration - interconnectedness, system connection into a single whole and, accordingly, the process of establishing such relations, rapprochement, association of organizations, industries, etc. There are different types of integration (Figure 1.).

![Types of Integration Diagram](image)

**Types of Integration**

- **Vertical integration**
- **Quasi-integration**
- **Conglomerate Integration**
- **Horizontal integration**

**Figure 1.** - Types of integration

According to the degree of homogeneity of the assets of the integrated enterprises, horizontal and vertical integration is distinguished. Horizontal integration contributes to the unification of enterprises of the same industry, the production of which is characterized by technological community and homogeneity of products. With this integration, enterprises are trying to resist competition from strong partners. At the same time, the strategy of horizontal integration can be aimed at expanding the geography or expanding the product range.

2. METHODOLOGY
Vertical integration implies the unification of enterprises operating in the same or different industries, connected by a single value chain. The essence of vertical integration lies in the fact that enterprises prefer to create the necessary elements of the production cycle independently, within an integrated structure, rather than buying them on the free market [2]. Vertical integration can be carried out in two directions: towards the suppliers (integration down), or towards the final consumers of the finished product (integration up) [2]. In order to gain control over distribution channels, expand market share and conquer new markets, an enterprise that is an integration core creates its own output stages of the technological chain (direct integration). Integration in the direction of sources of raw materials (reverse) is to join functions that were previously performed by suppliers, acquiring ownership and establishing control over sources of raw materials.

The strategy of vertical integration can be aimed at the full integration of production activities with participation in all links of the industry value chain or incomplete (partial) integration, which includes only some links of the value chain [4]. Conglomerate integration is a combination of companies in different areas of production, leading to an increase in the number of markets in which the company operates, as well as the unification of various unrelated organizations (groups of enterprises and organizations) at different stages of production and operating in various industries economy.
The practical manifestation of vertical restrictions can be attributed to the activities of network companies, or network companies. The attractiveness of the network form of interrelationships between enterprises is due to the fact that as a result of joint activities, sufficiently high economic indicators are achieved that are not available in stand-alone production. Most contracts are regional firms with certain suppliers and consumers. Such constancy spontaneously forms a certain circle of interdependent enterprises - partners working in local chains. The key element in creating a network is the presence of a sufficient level of trust between its members, an example is the Japanese model of network organizations, the so-called keiretsu, characterized by a high level of mutual moral obligations. In this version, the network organization does not have a single source of power, and disagreements on economic issues are resolved by the group members [3].

Within the company integration can be carried out in three main ways [8]:

1) Expansion of activities within one company by organizing its own production of raw materials

2) Expansion of activities in the framework of a single company through the organization of its own processing production.

3) Complete merger of enterprises into one legal entity.

In the first and second cases, the expansion of production is due to the consolidation of the company, but with the preservation of all parts of the industry market. Here the sphere of inter-company relations is expanding due to an increase in the scale of business. In the third case, the integration processes are accompanied by a reduction in the number of participants in the sectoral market, here the production organization, control over property, control over the management of the previously independent division change somewhat and the scope of intra-company interactions also expands. Other scientists assign a special role to the association of enterprises with or without property rights, when enterprises belonging to the association do not lose their legal independence [5]. The attitude of scientists and practitioners to the phenomenon of "vertical integration" is generally ambiguous. In the economic literature there are quite convincing considerations against integration. AND I. Butyrkin believes that they are of a general nature, and with respect to them there is a rare unanimity among researchers [2].

We give some of them. First, vertical integration increases the company's investment in the industry or related industries, thereby increasing business risk and not allowing the company to direct financial resources to other more profitable areas of business.

Secondly, the integration of both “forward” and “backward” imposes restrictions on the choice of suppliers, orienting the company to domestic sources of supplies of raw materials and components. Compared to competitors within the company, delivery conditions may be more costly. Thirdly, vertical integration is accompanied by the problem of imbalance of production capacity at each stage of the value chain. The optimal volume of production for one link in the process chain may not correspond to the needs of the other link associated with it. Fourth, the integrated “forward” and “backward” businesses differ from each other and require different business abilities and skills. Fifth, vertical integration in the direction of manufacturers of components can reduce the adaptive capabilities and production flexibility of the company [2]. Sixth, vertical integration contributes to creating the foundations of monopoly power and strategic barriers to entry of potential competitors.

3. RESULTS

According to most scholars, there are quite a few motivations to explain the reasons for integrating enterprises. One of the most important incentives for vertical integration is the
expectation of obtaining savings on transaction costs associated with the preparation and conclusion of contracts. This is a direct savings, as in a vertically integrated structure, the costs associated with obtaining information about prices, suppliers, negotiating and preparing contracts are reduced.

The second existing incentive for vertical integration is the ability to realize the market power of a vertically integrated structure. This is possible by eliminating the so-called “double margin” or “double premium” effect, as a result of which a vertically integrated structure can reduce intermediate costs and increase profits. A significant motive for vertical integration can also serve as the possibility of diversification of production. Under the diversification of the enterprise is the expansion of economic activity to new areas, as a rule, not having a direct production or functional dependence on its main activity. Diversification, as an investment strategy aimed at reducing the risk and growth of the company, contributes to the fact that: - a vertically integrated company allows you to switch to new activities; - gets the opportunity to expand markets; - allows more efficient use of modern technology;

Modern economic theory explains vertical integration from at least three basic positions: neoclassical, institutional, and transactional.

Within the framework of the neoclassical theory, vertical integration was investigated as an important component of the sectoral market structure. Neoclassicists explained vertical integration from a position of economic efficiency primarily due to the elimination of the “double premium”.

In the framework of the institutional approach, representatives of the transactional direction attempted to give their own interpretation of the origin of the vertical integration trend. The reason they saw in saving transaction costs. However, opponents point out that “saving on transaction costs” is not the main and main thing, but only a related phenomenon of integration. You can save on the main cost elements included in the cost of [6]. Vertical integration can be implemented through various forms of organization of economic activity. Our country has considerable experience in the field of enterprise integration for joint economic activities. Thus, the development of social production relations in Russia in the early twentieth century led to the emergence of such forms of business associations such as trusts and syndicates.

The trust represented a form of association of state enterprises with the rights of a legal entity. Each trust was a single enterprise, which included several production units. These associations were financed from the state budget. The trust could own, use and dispose of state property and was responsible within the limits of this property. Trusts were allowed to make long-term loans in the form of issuing bonds, and the state did not respond on these bonds [7].

The creation of syndicates in the mid-20s was associated with the need to strengthen control over the activities of the trusts. During the period of planned economy, syndicates became one of the elements of the system of planned management. Later, when merging the glavkov and syndicates into a single system based on the principles of cost accounting, the trusts were liquidated. Further development of the industry was associated with the redistribution of management functions towards the decentralization of operational management with rigid centralized management [9; 11-12].

Further, as a result of the reorganization, industry-specific industrial associations, whose functioning was based on cooperative ties, replaced the syndicates. By “cooperation” is meant an intra-industry association of organizations (groups of organizations) operating within a single technological process. In the Soviet period, in the conditions of a planned economy, close attention was paid to the issues of co-operation. Under socialism, a planning system was introduced that determined the general directions in the planned distribution of products and was expressed in attaching buyers to suppliers.
The further development and improvement of the specialization and cooperation of production was facilitated by the creation in the USSR in the early 60s of production associations, which are a single production and economic complex, which included plants, research, technological, design and other organizations that have production communication. This kind of production associations became an important economic unit of industry, whose activities were based on a combination of centralized management with the economic independence of the association. The production units that are part of the production association were not legal entities and acted in accordance with the Regulations on the Production Association (Combine), approved by a decree of the USSR Council of Ministers of March 27, 1974. At the same time, concerns, consortia, associations, and unions began to form [1].

Within the framework of the concern several independent enterprises were united in order to carry out joint activities. At the same time, managerial functions were strictly centralized. Merging companies into consortia was temporary. The duration of cooperation of enterprises that had the status of a legal entity was determined by the scale of joint activities. The jointly selected management exercised the management of the consortium. Associations and unions can be called a special form of association of enterprises. These types of associations were included in the company, which, despite being united to achieve common goals, did not lose their strategic, legal and economic autonomy.

In the period of transition from administrative economy to the market, there was a change in the system of social relations, the redistribution of property, the rupture of economic relations, which led to a recession and inefficiency of production. Evaluating the depth of the decline in production as a result of the reforms, it should be noted that in the last quarter of 1991 industrial production in the USSR had already fallen by 21% compared with the corresponding period of 1990 and a quarter relative to the highest point reached in 1989. These circumstances necessitated the formation of efficient industrial production on the basis of vertical integration, ensuring business consolidation and its concentration. This led to the widespread use of such forms of business organization as holding companies or holding companies. Their contribution to the real economy becomes significant: since the share of holdings in the number of enterprises is 39%, in the number of employees - 64%.

E.O. Kutin offers the term “holding” to mean a structured association of interrelated organizations that does not have the status of a legal entity, but has partial legal capacity and acts in various markets for goods and services as a single, consolidated entity. In our opinion, this definition does not reflect the distinctive features of the holding form of organization. A more precise definition is given by V.V. Minaev and I.N. Mikheeva, highlighting the main characteristics of the holding: the presence in its composition of industrial enterprises and the ability to have a significant impact on the activities of subsidiaries and affiliates. Thus, they understand an industrial holding as an association of legal entities with the participation of an industrial organization (industrial organizations) in which the parent (parent) company has the ability, directly or indirectly (through a third party), to have a significant impact on the decisions made by the management bodies of its subsidiaries. and dependent societies.

4. CONCLUSION
The main modern trends in the development of Russian industrial holdings are: high dynamism of development and an increasing role in the development of the country's economy; expansion of the number of companies included in the holding and the formation of subholdings; strengthening inter-company and intra-company cooperation; increasing the concentration of production resources; increased innovation activity; activization of foreign economic activity.
In our opinion, the benefits of vertical integration in the metallurgical industry can be fully realized on the basis of the holding form of organization of activities, since a combination of centralized and decentralized management is possible within the holding. Centralization allows for additional effects, and decentralization facilitates rapid adaptation to changing conditions.

So, despite numerous researches of scientists, both in foreign, and in the domestic theory and practice, the unified attitude to the “integration” phenomenon has not been fully formed. In our country, the advantages of vertical integration have been studied and gained widespread adoption in the period of a planned economy. However, the use of domestic experience does not fully allow changes in business conditions. In this regard, we believe that in modern conditions integration issues require additional research on the mechanisms of interaction between holding companies' participants, taking into account, on the one hand, accumulated theoretical and practical experience, and on the other hand, modern realities and industry-specific enterprises.

REFERENCES


