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Introduction

Background

Special economic zones (SEZs) have a long economic pedigree in the context of India as well as other countries. From a global perspective, in today's context, SEZs are a modified version of the conventional export processing zones (EPZs), which again are a combination of two older instruments, viz., industrial estate/industrial park and free zone/free trade zone (FTZ) (World Bank, 1992). 'Industrial estate' refers to a geographical area allotted for industrial development. This concept emerged in the industrialized countries towards the end of the nineteenth century.¹ However, FTZs were set up near airports or seaports areas, which were free from customs duties. These facilities were used for storing transaction goods. The fusion of two ideas, that is, industrial estate and FTZ, provided a basic framework for the emergence of EPZs, which were customized for the promotion of non-traditional exports. The world's first and full-fledged EPZ came up in Ireland in 1959 (World Bank, 1992), and thereafter, within a short span of time, the concept of EPZs spread all over the world, particularly the developing economies. India and Puerto Rico were at the forefront in popularizing EPZs as an instrument of trade. In India, the first attempt in this direction was made in 1964, as part of an inward looking trade strategy, followed by other developing countries such as Taiwan, Philippines, the Dominican Republic, Mexico, Panama and Brazil during the period between 1966–70 (Wong and Chu, 1985).

It is undeniable that neither India nor China invented or pioneered the SEZ concept; rather, it is fair to believe that it evolved over the centuries

¹ The world's first full-fledged industrial estate was set up in 1896 as a private commercial venture at Trafford Park in Manchester, England (World Bank, 1992).

through permutations and combinations of different practices prevailing in many parts of the world. In fact, the number of EPZs increased sharply from 79 (spread over 25 countries) in 1975 to 6,000 (spread over 130 countries) by the end of 2006. The initial stimulus and growth of these zones could be attributed to the failure of the inward looking trade strategy that was in vogue in most of these economies. This was true particularly in the case of developing countries throughout Asia. The success of EPZs in later years was due to demonstration effect of the successful experience of the earlier zones, i.e., those established in the 1960s and 1970s.

Further, a look at the spread of EPZs across major geographical zones of the world reveals that Central American countries and Mexican, followed by Asian countries, were at the forefront in the promotion of EPZs (Table 1.1). The Asian zones, however, hold the record for having generated more employment opportunities as compared to the Central and Latin American countries. This could be due to the sectoral composition and type of investment attracted by these zones and the comparative advantage they enjoy in respect of producing labour-intensive products in the Asian region. However, different terminologies are being used across countries to define the concept of SEZs (Table 1.2). Diversity in its terminology reflects its evolutionary nature and the distinct purposes behind the establishment of zones across countries (Armas and Sadni-Lallab, 2002). These zones can be categorized into manufacturing, trading and service zones. Further, the terms used also speak of the physical characteristics of zones, type of activities involved, incentives and permission given for domestic or overseas sales, etc.

Table 1.1: Size and Employment in EPZs/SEZs across the World

Geographical regions	Number of zones	Employment (million)
Asia <ul style="list-style-type: none">• of which China• of which BGMEA* factories in Bangladesh	749	37 (30) (0.20)
Central America and Mexico	3300	0.22
Middle East	37	0.7
North Africa	23	0.4
Sub-Saharan Africa	64	0.4
North America	713	0.3

Geographical regions	Number of zones	Employment (million)
South America	39	0.3
Transition economies	90	0.2
Caribbean	87	0.22
Indian Ocean	3	0.1
Europe	55	0.051
Pacific	14	0.014
Total	5,174	42

Note: *BGMEA refers Bangladesh Garments Manufacturer Exporters Association.
Source: ILO (2006).

Table 1.2: Different Terminologies used for EPZs/SEZs

Synonyms	Studies, countries and date of first use
Free Trade Zone	Traditional term since the nineteenth century
Foreign Trade Zone	Individual authors (R. S. Toman, 1956; W. Dymsha, 1964), India (1983)
Industrial Free Zone	Ireland (pre-1970), UNIDO (1971), Liberia (1975)
Free Zone	UNCTAD (1973), USAID (1982), United Arab Emirates (1983)
Maquiladoras (in-bond) Enterprises	Mexico (early 1970s), Costa Rica, Honduras, Ireland, Trinidad and Tobago, Turkey, United Arab Emirates, Uruguay, Venezuela
Export Free Zone	Ireland (1975), UNIDO (1976)
Duty Free Export Processing Zone	Republic of Korea (1975)
Export Processing Free Zone	UNIDO (1976), UNCTAD (1983)
Free Production Zone	Sternberg Institute (1977)
Export Processing Zone	Philippines (1977), Harvard University (1977), APO (1977), WEPZA (1978), UNIDO (1979), Malaysia (1980), Pakistan (1980), Singapore (1982), UNCTC (1982), ILO (1983)

Synonyms	Studies, countries and date of first use
Tax Free Trade Zone	Individual author (D. B. Diamond, 1980)
Investment Promotion Zone	Sri Lanka (1981)
Free Economic Zone	Individual author (H. Grubel, 1982)
Free Export Zone	Republic of Korea (1983)
Free Export Processing Zone	OECD (1984)
Special Economic Zone	China (1979), India (2000)
Industrial Estates	Thailand
‘Points francs’ (Special Industrial Free Zones)	Cameroon
Bonded Zone	Indonesia
Tax Free Factories	Fiji
Industrial Free Zones for Goods and Services	Colombia

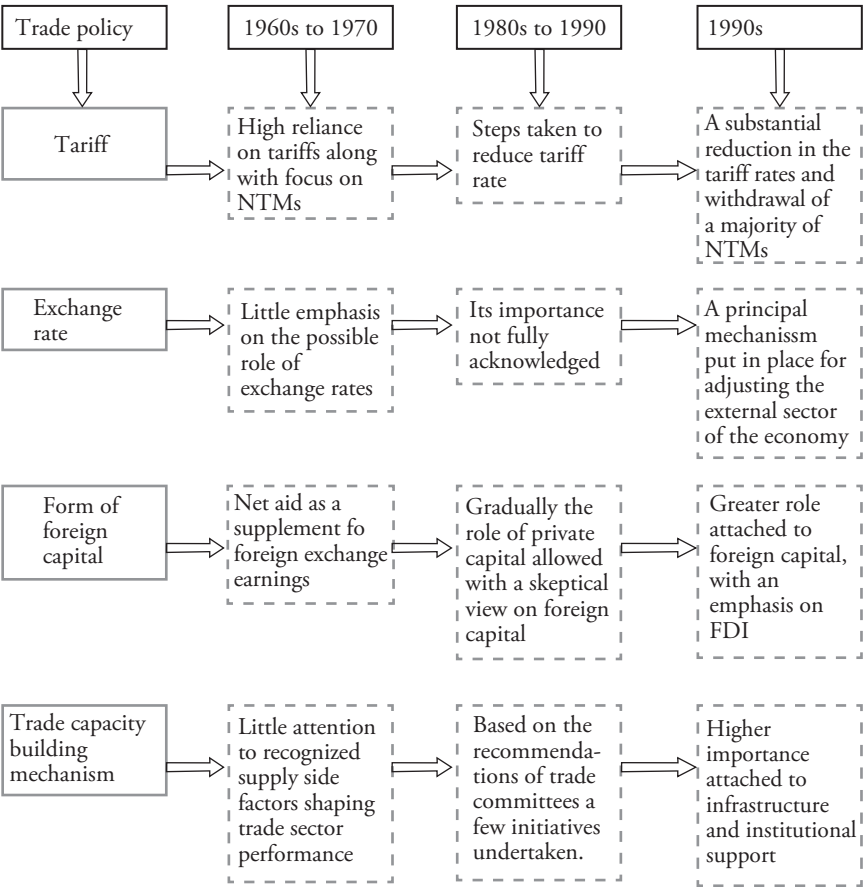
Source: Armas and Sadni - Lallab (2002), Kusago, and Tzannatos (1998), Government of India (1997).

In India, SEZs concept *per se* was introduced in the EXIM policy statement of 1997–2002, almost a decade after the introduction of India’s reform process, and in response to challenges emerging out of the economic liberalization initiated the world over. In fact, SEZs represent a typical case of reform strategy with a number of adjustments made to the existing policy instrument along with a set of new instruments.² Nevertheless, India had done the required groundwork through the creation of FTZs/EPZs at Kandla in the early 1960s, as part of the government’s efforts to have an alternative port set up in the western coast of India. This was later followed by the establishment of other zones in different parts of the country with different objectives underlying their promotion. Thus, the present SEZ policy came to be executed in two different stages in India. Initially, all the existing EPZs, that is, Kandla, Santacruz, Noida, Chennai, Cochin, Falta, Vizag and Surat were brought under the SEZs scheme. We refer to these as the conventional SEZs of the country. This was later followed by the approval of fresh SEZs

2 Details of major differences between the pre-reform and post-reform periods have been outlined in flow chart 1.1.

in the country, and these are referred to as new SEZs in this study.³ Currently, SEZs have completed more than a decade since their introduction in the country and during this period they have received both bouquets and brickbats from different quarters on a wide range of issues pertaining to their establishment.

Chart 1.1: The Evolution of Trade Policy through the Pre-reform and Post-reform Periods



Source: Author.

Focus of the study

A survey of literature pertaining to India's SEZs (see for instance, Kundra, 2000; Aggarwal, 2004, 2005, 2007, 2010 and 2012; Mukhopadhyay, 2007;

3 A detailed analysis of the SEZ policy has been carried out in Chapter 2.

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Rao, 2007; Bhaduri, 2007; Sharma, 2007; Gill, 2007; Patnaik, 2007; Gopalakrishnan, 2007; Banerjee *et al.*, 2007; Palit and Bhattacharjee, 2007; Kasturi, 2008; Sampat, 2008; Shah, 2009; Mukhopodyay, 2009; Menon and Mitra, 2009; Laxmanan, 2009; Gupta, 2008 and 2009; Carter, 2010; Levien, 2011; Sundarapandian, 2012; Cook *et al.*, 2013), against the backdrop of such growing academic interests, reveals that most of these studies are kind of piecemeal effort and what is missing is a holistic appraisal of SEZs expansion in India. In fact, studies pertaining to India's EPZs/SEZs could be categorized into two broad groups. The first category covers studies that evaluated the performance of these enclaves based on different parameters. Within this, a few studies attempt time-series analyses, cross-country comparisons and contextual analyses specifically in terms of assessing the capacity of emerging SEZs in meeting different expectations of the policymakers. The second set of studies consists largely of debates over current SEZ policy of the country from land, resettlement, rehabilitation to environmental considerations. Undoubtedly, these studies fail to address a few pertinent issues such as before introducing SEZs in India based on China's experience whether we had a sufficient understanding of the factors that boosted their performance and whether China's SEZs were really as promising as hypothesized by Indian policymakers? Whether the current SEZ policy merely represents old wine in a new bottle or whether there are any new functionalities? Whether there exists any basic loopholes not addressed by the current SEZ policy? How far operational SEZs have been able to meet the expectations of policy makers? To what extent are the conventional indicators of performance parameters appropriate? If not, what are the other appropriate techniques for evaluating their performance? With this background in view, this book attempts to provide certain critical insights into various pertinent issues surrounding the expansion of SEZs in India. Specifically, the SEZ policy has been evaluated in terms of: (a) Exploring the very relevance of the idea underlying promotion of the present SEZs policy, i.e., did we have a clear idea of expected benefits and associated negative impacts of the intended policy; did we know the experience of a similar policy sufficiently well, if any, in respect of other countries – were they successful ventures or a flawed attempts and what factors would explain such outcomes? (b) Looking into the SEZ policy structure and its implementation process, does the SEZ policy represent old wine in a new bottle or whether there are any new functionalities and also whether there are any fundamental problems left unattended? (c) It evaluates

the performance levels of SEZs in terms of both conventional indicators and a new set of frameworks.

Canvas of the study area and methodology

To explore whether there was logical clarity behind the promotion of SEZ policy, we have analysed the policy and performance experience of SEZs in China since India's SEZ policy has been modelled after China's SEZs. In particular, for an in-depth study, among the five full-fledged SEZs and 14 ETDZs of China, we have chosen Shenzhen SEZ for two reasons: (a) given its size, Shenzhen SEZ represents a classic case of an industrial township; and (b) its commanding performance according to the stated objectives relative to other SEZs and its transformation from a small fishing community into a full-fledged industrial township. The reference period of the study spans three decades from 1980 (post-SEZs) to 2012–13. The analysis is based on various policy documents related to China's SEZs, secondary data (*Chinese Statistical Year Book*, 2012 and *Shenzhen Statistical Year Book*, 2013) and the author's perception during an extended fieldwork in China.⁴ However, it is to be noted that our aim here is not to draw any comparison between China's and India's SEZs; rather, the attempt is to understand China's SEZ policy and its experience from India's perspective, and to draw appropriate lessons so as to make India's SEZs more effective as a policy instrument.

Besides outlining China's SEZ policy and experience, the focus of the study is to analyse the dynamics underlying the promotion of SEZs in India and in particular, to trace the effectiveness of SEZ policy over EPZs of the country both in terms of policy document and performance. For this purpose, only those SEZs that were operating at least five years prior to the introduction of the SEZ policy (2000) in the country have been covered by this study, the reason being that new SEZs might not help locate the effectiveness of SEZs *vis-à-vis* EPZs. Accordingly, this study has covered seven conventional⁵ SEZs operating across seven states. Thereby, it includes, Kandla SEZ (KSEZ) in

4 The fieldwork was carried out in 2007 (across two cities of China namely, Beijing and Shenzhen) and 2013 (across three cities of China namely, Beijing, Chengdu, Shanghai)

5 The currently operating SEZs in the country could be categorized under two major types – conventional SEZs and modern/new SEZs. Conventional SEZs are those which were operating under the EPZ structure of the country, currently brought under the SEZs scheme. Modern SEZs, however, are those which were approved after the enactment of the SEZs policy in the country.

Gujarat, Santacruz SEZ (SSEZ) in Maharashtra, Noida SEZ (NSEZ) of Uttar Pradesh, Chennai SEZ (MSEZ) in Tamil Nadu, Cochin SEZ (CSEZ) in Kerala, Falta SEZ (FSEZ) in West Bengal and Vizag SEZ (VSEZ) in Andhra Pradesh.⁶ Excepting Santacruz, which has been promoted exclusively for the promotion of gems and jewellery and electronics industries, all other zones offer a multiproduct base to investors. An analysis of India’s SEZ policy and performance is based on both secondary data published in various reports and documents and primary data collected through a survey. Information on policy changes and related information on India’s SEZs has been gathered from SEZs Act 2005, SEZs Rule 2006, subsequent amendments, various reports and documents published by the Ministry of Commerce and Industry, respective state government gazettes, RBI annual reports on the Indian economy, economic survey of India, whereas the secondary data on India’s SEZs from the respective Development Commissioner’s office located in each zone, Ministry of Commerce and Industry, Export Promotion Council for SEZs and EOUs, and Export Promotion Council for Gems and Jewellery. Primary data⁷ on India’s SEZs was collected at two levels: at the first level, information was collected from officers in charge of different sections of Development Commissioner’ office, Export Promotion Council for SEZs and EOUs, and zone associations; and at the second level, information was obtained from exporting units in each zone.

Table 1.3: SEZs Notified before the Enactment of SEZs Act, 2005 in India

Sl. No	Zone	Notified
Government SEZs (converted from EPZs)		
1	Kandla, Gujarat SEZ (FTZ)	1964
2	Santacruz, Maharashtra SEZ (EPZ)	1973–74
3	Noida, Uttar Pradesh SEZ (EPZ)	1984–85
4	Chennai, Tamil Nadu SEZ (EPZ)	1984–85
5	Cochin, Kerala SEZ (EPZ)	1984–85
6	Falta, West Bengal SEZ (EPZ)	1985–86
7	Vizag, Andhra Pradesh SEZ (EPZ)	1986–87

6 Refer table 4.1 for brief description of seven SEZs covered by the study.
7 Primary data are based on fieldwork carried out between 2007 and 2014.

Sl. No	Zone	Notified
SEZs Notified before Enactment of SEZs Act, 2005		
8	Surat, Gujarat SEZ	1 November 2002
9	Manikanchan, West Bengal SEZ	12 June 2003
10	Jaipur, Rajasthan SEZ	1 July 2003
11	Indore SEZ	1 August 2003
12	Jodhapur, Rajasthan SEZ	8 September 2003
13	Salt Lake Electronics city – WIPRO, West Bengal	12 August 2005
14	Mahindra City SEZ (IT), Tamil Nadu	26 October 2004
15	Mahindra City SEZ (auto ancillary), Tamil Nadu	
16	Mahindra City SEZ (textiles), Tamil Nadu	26 October 2004
17	Nokia, Tamil Nadu	7 December 2005
18	Moradabad SEZ	30 September 2003
19	Surat Apparel Park, Gujarat	31 January 2005

Source: www.sezindia.nic.in.

Organization of the book

The book is organized into seven chapters including of an introduction. The second chapter traces the evolution of India’s SEZ policy. In particular, this chapter attempts a programmatic historical survey of EPZs/SEZs followed in India over the last five decades (1960 to till date), focusing especially on the possible reasons leading to the realization on the part of policymakers and the government that the existing EPZs required a radical overhauling both in terms of their objectives and the arms provided to bring this objectives to fruition, which in turn led to the transformation of EPZ into SEZs; to what extent has the transformation of EPZs into SEZs been effective at the construction and implementation levels; what are the problems and prospect of the current SEZ policy. Underpinnings of Chinese SEZ policy and its growth trajectories are outlined in chapter 3. In this chapter, in particular, we explore issues such as (a) factors contributing to the success of China’s SEZ

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policy, as also various supportive mechanisms, both internal and external that have played an important role in scripting this success story; (b) inadequacies of India's policymakers in understanding the demands underlying such a policy shift and its implementation, and also the institutional and infrastructural requirements that should have been provided for its emulation; (c) the lessons that India can imbibe in its attempt to redefine the SEZ policy, which, doubtless, has become a necessity now.

How far have been the operational SEZs been able to meet the expectations of policymakers both at aggregate and disaggregate levels is an issue that has been discussed in the fourth chapter. While questioning the conventional parameters of performance, chapters 5 and 6 provide alternative techniques for evaluating the performance of SEZs. In particular, chapter 5 deals with the issue of fiscal implications of SEZs expansion in India. The issue of efficiency of SEZs as a trade policy as well as factors contributing to it are probed in the chapter 6. Chapter 7 summarizes the major findings along with suggestions for policy revision.