Special Economic Zones (SEZs) in India and China: A Study On Strategy of Export led Growth

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Introduction

Export led growth finds a great significance in all period of history both at the level of growth experience and in economic literature. In the twentieth century, Japan, South Korea, Taiwan, Malaysia, Indonesia and Singapore achieved faster economic growth through export led policies. Developing countries of Asia, after political independence attempted to have growth based on domestic market by protecting their domestic industries from foreign competition. But the strategy of growth and industrialization through protected domestic market was not successful in most cases. These economies experienced slow growth and in the latter half of the last century most of them adopting the policy of export led growth.

India after economic reforms in1991, has shifted its policy towards export oriented growth and has been liberalizing export sector. Apart from providing financial and fiscal incentives to export sector, India has been opening up various key sectors such as software, automobile and consumer electronic goods, banking and insurance for foreign investments. In an attempt to give further boost to the export sector, India started Special Economic Zones in 2000 and passed SEZ Act in 2005. Concept of Special Economic Zones is being used by many emerging economies who now want to have faster economic growth propelled by export sector.

This paper attempts to evaluate Indian SEZ policy, its impact on the society and public opinions on the policy. Then a comparison is made with Chinese SEZs which have been successful in export promotion and transformation of recent industrial growth in China. Lastly conclusions will be drawn whether the strategy of SEZs is plausible for Indian democratic set up committed to have socialistic pattern of society or an alternative strategy of growth is more compatible in Indian socio-economic situations.

SEZs in India:

India's shift to export oriented growth policy has transformed the export sector from stagnant agricultural exports towards exports of industrial goods. Now India's share in light manufacturing goods such as textile, handicrafts, readymade garments, leather and leather goods, light engineering goods, processed foods have been rising and the share of traditional exports such as tea, jute and other agricultural and allied products have been declining over years. India has now emerged as a major software exporting country while BPO industry is exporting services to global companies all over the world. Liberalization of FDI policy for Indian economy has attracted global companies not only to the export oriented software industries but to automobile industries, consumer electronic industries, service industries such as banking insurance and BPOs. India's vibrant service sector's contributions to the growth of GDP (its share is 51 per cent), to export earnings have increased substantially. This sector also has

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created employment for skilled labour. Now India's exports have increased at the rate of 18- 20 per cent, (Economic Surveys 2006-7) while according to 2008 Economic survey, exports have grown at the rate of 21.6 per cent in dollar and 7. 7 per cent in Rupee terms (due to appreciation of Rupees), yet a comparison of India's export performance and FDI flows with emerging economies of East Asia and China shows that India's export sector has not been as dynamic. Though India started export promotion (1967) earlier than China through creation of Special Processing Zones (SPZs), free port facilities and providing fiscal as well as financial concessions to export oriented units(EOU), India's share in the world trade was only 0.9 per cent in 2005. India received much less FDI compared to China. China received $42.4 billions FDI in 2006 and India only got $7 billion which is many times lower than china's. In recent years FDI inflows are playing an important role in expansion of trade, capital formation and growth of world GDP(UNCTAD, 2006).

In this scenario, the govt of India recognised that faster economic growth, can be achieved only through export promotions and FDI compliant business environment. Consequently, in 2000 the govt of India changed the exim policy to convert SPZ into SEZs and establishment of new SEZs. Then the Special Economic Zone Act was passed in 2005 and was implemented from 2006. As on 2006 announcement, 439 SEZs are given approval, 138 are approved in principle and 195 are notified.(Ministry of Commerce, GOI)

The concept of Special Economic Zone is based on the promotion of free market mechanism allowing competition among firms and industries so that they can operate at the most efficient level by using the best technology and managerial practices. SEZs require large stretch of land for industries free from any economic regulations of national govts. SEZs also need to have multi product larger scale production units so that interdependence among industries is created to get economies of industrial conglomeration while free market would improve competitive environment and growth of industries. SEZs are provided better infrastructure, fiscal incentives and good governance. This environment in SEZs is expected to attract global companies and enable India to shift to hi-tech, high value products so that her share of exports increases to 1.25 per cent of world exports as well as employment opportunities are created for high skilled labour. In order to improve the quality of governance, measures are taken for single window approval for establishing units in SEZs. Large number of non-fiscal and fiscal incentives is announced for the developers and production units. This will cost the treasury the revenue loss of 4-6 per cent of GDP in 5 to 10 years. SEZs can be started under private sector, state govt or as a joint venture.

Indian SEZ policy from the inception, has been attracting public debates, criticisms, protests to such extent that the central Govt announced postponement of any further actions towards implementation in 2007 and a review committee at the Ministerial level has been set up to reformulate the SEZ Act. Though this step has temporarily pacified the agitating public and affected farmers but big business houses are dissatisfied and think that delay in implementation of the act will hurt business confidence. The policy has created divisions within the political parties, among the public of different strata from intellectuals to grass root level affected by the policy. Opinions are expressed that the policy has been formulated without research and hence it suffers from basic inadequacies. Others think that since the policy will benefit big business houses at the cost of the weaker sections, this is not a plausible policy in our democracy based on socialistic pattern of society.

Next part will analyse problems and debates on 2005 SEZ Act regarding (a) land development (b) land acquisition (c) labour law and employment (d) other inadequacies of the act.

Land Development for SEZs: State Govts were empowered to acquire land which would be transferred to private developers to develop appropriate infrastructure for SEZs. The Act announced the size of the SEZs to be between 10 to 1000 hectares depending on the type of product units to be started. Private developers are provided the incentives of 100 per cent tax exemptions for initial five years and 50 per cent for another five years. They are allowed the ownership right on the land they develop for SEZs. The govt has not given any specific guide lines for land use of SEZs while developers have decided to put 35 per cent of land for processing units and rest would be used as non processing zones. Apart from processing units, SEZs can have residential complexes, entertainment sections and amusement parks.

Now question arises whether or not so much of liberty of land usages to the private developers with ownership rights on land would bring efficient use of land which is the absolute necessity in a situation of over all scarcity of land. A look at the trends of approval and notification patterns of SEZs does not support that. Table 1 shows that, of the approvals given to the private sector for which data are available, 61 per cent has been given to the real estate developers and 12 per cent to the IT companies. Again, of total approvals to the real estate developers (Table 2), IT companies have the major share. From these two tables it can be gathered that approval for production units for SEZs are given to those which have the proven track records of export performances. Do they really need SEZs facilities when they have been performing well otherwise. It could be an indication that these units are relocating their productions in order to take advantage of SEZs. Also real estate developers may be attempting to reduce risk by choosing successful export ventures rather than going for new and unknown ones. Approval list of companies do not have any manufacturing units though notification (up to 2006) list contains some multi-product SEZs. These trends, even at start can be alarming that SEZs may not fulfill the promises of attracting domestic and foreign investment for industrial production.

Table 1

Pattern of Sector wise approvals of private SEZ Developers

Sector	No. of approval	Percentage
Real Estate Developers	167	60.95
Information Technology	34	12.41
Drug	17	6.20
Investment/holding/ finance	14	5.11
Industrial	9	3.28
Engineering	7	2.55
Logistic	5	1.82
Textile/ Footwear/apparel	5	1.82
Mining /Metals	4	1.46
Gems	3	1.09
other	8	2.92

Source: Ministry of Commerce, Government of India

Table 2
Sector wise Disaggregation of Real Estate Companies applications

Sector	Approval	percentage
IT	87	52.10
Multi product	32	19.16
Textile/ apparel	15	8.98
Engineering	8	4.79
Drug/Chemical/ Biotech	8	4.79
Service	6	3.59
Gems	3	1.80
Electronic	2	1.20
Food processing	2	1.20
FTWZ	2	1.20
Other	1	0.60
petrol	1	0.60

Source: Ministry of Commerce, Government of India

Unregulated land development policy by the private sector may also lead to further problems such as developers are likely to charge high price from the production units or final land users in a situation of scarcity of well developed space. This opens the door of rampant speculative activities on land discouraging both domestic and foreign companies to come to SEZs and defeating the purpose of the policy. Private land developers may also choose to keep a large stretch of land unused. Even China had to face such problems in course of development of SEZs.

Problems of Land acquisition:

State govts are allowed to acquire any land for the purpose of SEZs. Even though land acquisition act was amended in 1960 making consent of the farmer compulsory for any acquisition, state govts in overenthusiastic zeal ignored the above law and used 1864 draconian land acquisition act of colonial period which permits acquisition without consents of owners. Using this method, total of 1.25 lakhs hectres of prime agricultural land are being acquired in the first phase and in the second phase too almost equal area will be acquired(Feb 14 2007, South Asia). This resulted into a number of disputes between farmers and the concerned state Govt. Table 3 gives some details of the nature of protests in order to understand rootedness of land acquisition problem.

Table 3

Local Level Protests against Land acquisition in India

State	Location	Protest by against	Type of Land
Punjab	Barnala	Farmers against Triedent	Agro Land
Punjab	Amritsar	Farmers	Fertile agro Land
Haryana	Jhajjar	Farmers	10.000 hectres of double cropped land
Mumbai	Near Mumbai	Farmers	14000 hectres of double cropped area
Mumbai	Uttar-Goria Belt	Bt fishermen and sultpan workers	2 km metre in width and 18 Km in length
Orissa	Kashipur	Against Birlas (Utkal Aluminum Ltd.)	for 13 years
Orissa	Earasama near paradeep	Against South Korean MNC	Posco for 2 years
U.P.	Dadri	Against Anil Ambani's Reliance Group Power plant	
Chattishgarh	Baster	Against state Govt.	
Goa	Goa	Protests by Citizens	Govt. ordered cancellation of notification
WB	Singur	By local people and farmers against state govt. acquisition of land for Tatas	20 acres of fertile Agro land at a nominal price
WB	Nandigram	Local protest group against the state govt's acquisition for Indonesian Salim group	Repression of protesters and killings described as worse than Jallianawalla Bag

Apart from grass root level resistances, various political formations and NGOs (Citizens' Research Collective and Left Parties)have been campaigning against SEZ land acquisition policy particularly on the question of displacements. They point out that present SEZ policy is business friendly rather than market friendly. They describe that the present policy is formulated only for satisfying the preference of the big business houses for land close to urban areas with strong agricultural economies and powerful farming interests. They suggested that land should be paid at the market rate and proper compensation package should be provided to all the stakeholders. In response to these criticism, the Govt of India will be bringing two amendment bills to the parliament one on land acquisition and other on rehabilitation and resettlement of displaced persons. But the provisions of bills are not enough to protect the interest of more than sixty per cent of population dependent on agriculture directly or indirectly be affected by the policy. Also an implication of land acquisition needs to be understood in the broader context of food security. Acquisition of prime agro land by the private developers may lead to disinvestment on land as happened in China. This will worsen already distressed conditions of Indian agriculture.

SEZs and Labour Laws and employment prospect

In terms of employment creation, proposed Indian SEZs do not look to be promising. SEZs will create 7 lakh jobs for urban skilled labour while 1.14 lakhs farm families having five members per family will be displaced along with 82 thousand farm workers.

According to a study by A. Aggarwal (2007) in 2006 in the existing SEZs, 170, 000 workers were employed while in China 20 million people were employed in SEZs in 1998(UNIDO report). Research studies mention that Indian SEZs are not favourite destination for both domestic and international investors because of stringent labour laws and industrial disputes. In countries such as Bangladesh Sri Lanka and China, casualisation of workers has taken place enabling the entrepreneur to reduce labour cost to improve their competitiveness in the world market.

Other inadequacies

Among othe the inadequacies of SEZs in India, the policy has not worked out appropriate legal framework between Domestic tariff Area and SEZs. Since these two systems will have two different sets of economic rules, the possibility of pilferage and corrupt practices in movements of goods between two areas can not be ignored. Moreover the policy does not mention anything about export obligation neither it specifies any minimum value addition for SEZ units. These inadequacies could prove to be serious and defeat the purpose of SEZs altogether even when the nation pays such high cost for SEZs.

SEZs in China and India: A Comparison

The success of Chinese SEZs was due to some economic and socio- political conditions specially existing there. China introduced free market economy in the political set up of one party dictatorship. Therefore any policy change was not confronted with political repercussion. In India there is a fear of loss of power if the govt displeases vulnerable sections. "A proudly democratic India that grows at 6 per cent a year, should be congratulated for succeeding better than an "anti-democratic China which grows at 10 per cent a year" (Economist March 5, 2005). China also has other favourable conditions such as close connectivity with Hong Kong and Taiwan which served as the gateway for Chinese exports and inflows of FDI. Non Resident Chinese invested FDI in the industrial sectors and capital formation while in NRI brought financial capital through remittance which did not go for physical capital formation. Yet Chinese miraculous growth experience was not without costs. Recent studies have brought out negative sides of SEZs in China and how she was compelled to stop any further expansion of SEZs in 1998 due to large scale protests by the workers and farmers.

Table - 4

	China	India
Number	At present only 7 though at one stage there were several thousand. Many of them were closed after 1998.	Ultimately 600 or more
When started	1980	Mostly after 1991, especially after 2005
Democratic decision-making?	Lot of discussion and debate (within policy-making circles) preceded setting up of SEZs	No discussion. Parliament passed the law easily. Most discussion has followed protests.
Land legislation used	Initially land was under the state ownership. Law for agricultural land conservation passed in 1998 after concern over loss of cultivable land and natural resource base because of SEZs. No SEZs after 1998.	'Public purpose' clause in Land Acquisition Act of 1894 still used to acquire land for SEZ, though recent policy announcements promise State withdrawal from land transactions
Size	Very large (Shenzhen: 32,700 hectares) These are all multi product SEZs	Small (3 – 14,000 hectares). Mostly small and single product. Only few multi product sezs are notified till 2006.
Ownership	State.	Private corporations
On what kind of land	Mostly coastal wasteland	Mostly fertile cultivated land close to urban hinterlands
Exports	Very good 12 per cent of Chinese GDP was contributed by SEZS in 2006	Poor so far SEZs contributed 4.2 per cent of export growth in 2007
Employment	Several million low-paid jobs with poor working conditions	Very limited so far: 180,000 in all the SEZs till March 2007.
Tax revenue collections	tax incentives provided to production units , workers and foreigners interest earnings. Workers are provided free housing.	Across-the-board tax holiday given to companies both for production units and to the developers but no incentive for the workers and no promise of free housing facilities.
Overall economic success	Shenzhen very successful, but most SEZs have failed	Largely unsuccessful so far
Ease of land acquisition	Land battles in some areas still	Bloody, bitter resistance
Macroeconomic Environment	More favourable for industrial growth especially exit policy and competitive laws and incentives for small industries to grow into large scale	Industrial dispute, exit policy, competitive law are not favourable in India. It takes ten years for an industry to declare bankruptcy here. Incentive to small scale industries discourage big business growth.

Source: Table has been adapted from *Citizens' Research Collective*'s booklet *SEZs and Land Acquisition: Factsheet for an Unconstitutional Economic Policy* and Shankar Gopalakrishnan, 'Negative Aspects of SEZs in China', EPW, April 28, 2007 and other writings referred at the end. The data and facts are drawn from various government documents

Conclusion:

1. **SEZ policy not compatible with Democracy:**

This paper brings out apprehensions that SEZ policy will break fabric of the socialist pattern of the society. According to Front Line (2007) " SEZs would lead to concentration of wealth, uneven development, jobless growth and anti-democratic atmosphere". In Indian democratic set up, any change in economic policy will have some losers and gainers. This is bound to create conflict of interests and instability in the society. Especially SEZ policy will hurt more than 60 per cent of rural population depending directly or indirectly on agricultural land. India can not take the risk of such policy that will deprive majority of people. In this case no package of compensation to the losers will be sufficient.

2 **Growth through expansion of domestic market - a socially harmonious and equitable strategy**

Alternative for India is to have growth through expansion and integration of domestic market. This looks to be plausible with rise in per capita income at the rate of 7.2 per cent (Economic Survey 2008) and high propensity to spend by Indians as Economic Survey (2008) indicates 5.1 per cent growth of private final consumption expenditure.

3. **Development of Infrastructure for the entire economy through public sector is the pre condition**

Development of infrastructure for the economy is the pre condition for this pattern of growth. This will open up opportunities of growth for the entire economy rather than selected areas through SEZ policy thus reducing the possibility of regional imbalances of growth. This also ensures more equitable growth. The paper suggests that even if Public Private Partnership (PPP) needs to be forged, the Govt should refrain from transfer of ownerships of land to the private developers.

4. **Increase in the reserve of skilled labour through expansion of Education is another requirement**

Faster economic growth will increase demand for skilled manpower. Scarcity of highly skilled human resources may tend to increase wages for them disproportionately. In that case these jobs would be exported to other economies around the world having low wages. Only way to prevent this tendency is to invest in skill formation. In that case large labour force can become advantage for Indian economy. Moreover a large pool of skilled labour will help to have quick spill over effects of the growth propelled by exports and FDI inflows.

5. **SEZs for agro-based industries in the prosperous farming areas**

Lastly, SEZ or similar policy can be adopted to develop agro-based processing industries for creating employment for the rural economy. This will reduce burden on land. This policy will incorporate more inclusive, participatory and harmonious growth. These zones can absorb low skilled rural labour with some basic training compatible to their educational levels. This strategy will be less costly compared to paying huge compensation to displaced persons through SEZ land acquisition policy

References

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Detailed references are provided in the main report.