

# **What went wrong with India's SEZs?: Economics, Politics or Bureaucracy**

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# Why SEZs?

- **Economic approaches ( Economic returns)**
  - Orthodox Approach
  - Dynamic orthodox approach
  - Heterodox Approach
  - New International Division of Labour (NIDL)
  - New Economic Geography (NEG)
- **Political economy approaches (Political returns)**
  - Public Choice theory: Interest group theory and rent seeking
  - Foreign Policy and the state: Soft power: Border and cross border zones and country specific zone; Qualifying zones of Egypt and Jordan);
  - SEZs to take advantage of preferential treatments.

# Success factors

## 1. Economic factors

- Orthodox approach: low labour costs, tax incentives in import substituting regime ( Macro vs micro I climate, international factors)
- Dynamic orthodox: Testing lab for reforms (Macro vs micro I climate)
- Heterodox: good investment climate within zones (Macro I, international)
- NIDL: Comparative and competitive advantages and low export costs ( Micro and Meso investment climate)
- NEG: Agglomeration economies (micro and meso investment climate, strategy and vision)

## 2. Political factors

- Short term political returns
- Development state vs inclusive development state:
- Political will, vision and strategy

### **3. Bureaucratic factors: Policy designs & Implementation**

- Poor policy designs
- Legal apparatus
- Adequate resources
- Understanding of SEZs
- Poor SEZ designs
- Lack of understanding of the implementation conditions: macro, meso and micro
- Approach towards SEZ (trust)

# Failure of SEZs

- Failure is contextual.
- Failures may be for different reasons under different contexts across countries and within the same country across different phases
- Important to analyse the performance through different lenses.

# **SEZs in India: Three broad phases**

- 1965-2000: The EPZ regime
- 2000-2005: Transition to SEZ regime
- 2005 onwards: The SEZ Regime

# Phase 1: EPZ programme was introduced as part of import substituting regime....

- India: the first Asian country to have an EPZ in 1965. Three phases
- **1965-1984: Initial phase**
  - Highly regulatory regime, poor incentive package, Poor infrastructure
- **1985-1990 : expansionary phase**
  - 5 new EPZs were set up at Noida, Madras, Cochin, Falta, Vizag
  - EOUs
- **1991-2000: Consolidating phase**
  - Devolution of powers to zone administration, sectoral coverage was expanded, private sector EPZs, only one zone at Surat came up.

# Phase I: Performance evaluation of EPZs



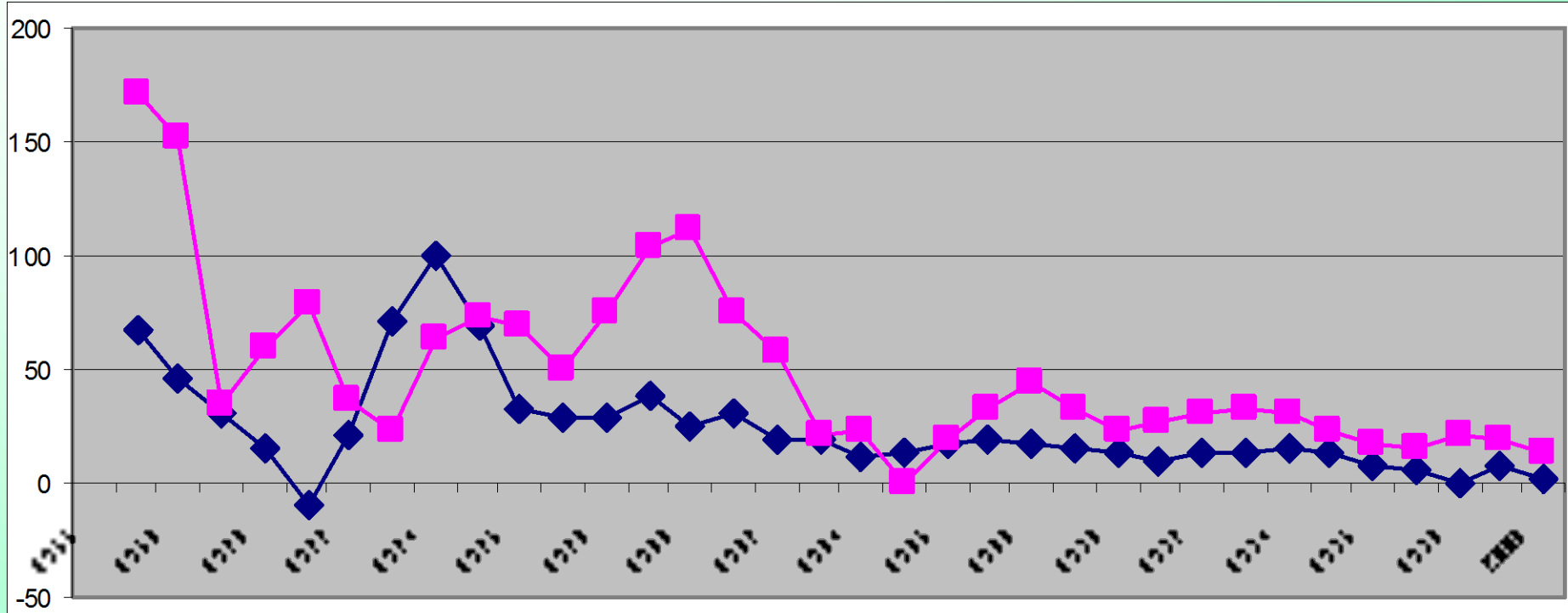
**National  
Contribution**  
to exports,  
employment

**Regional development**  
Contribution to employment,  
Income generation  
Ancilliary industrial activities  
Most notable : SEEPZ, CSEZ,  
Noida

**At the sector level** “ Selected cases of success at the industry  
level : Gems and Jewellery, Electronics, SW, rubber gloves.  
2. Development of Local entrepreneurship



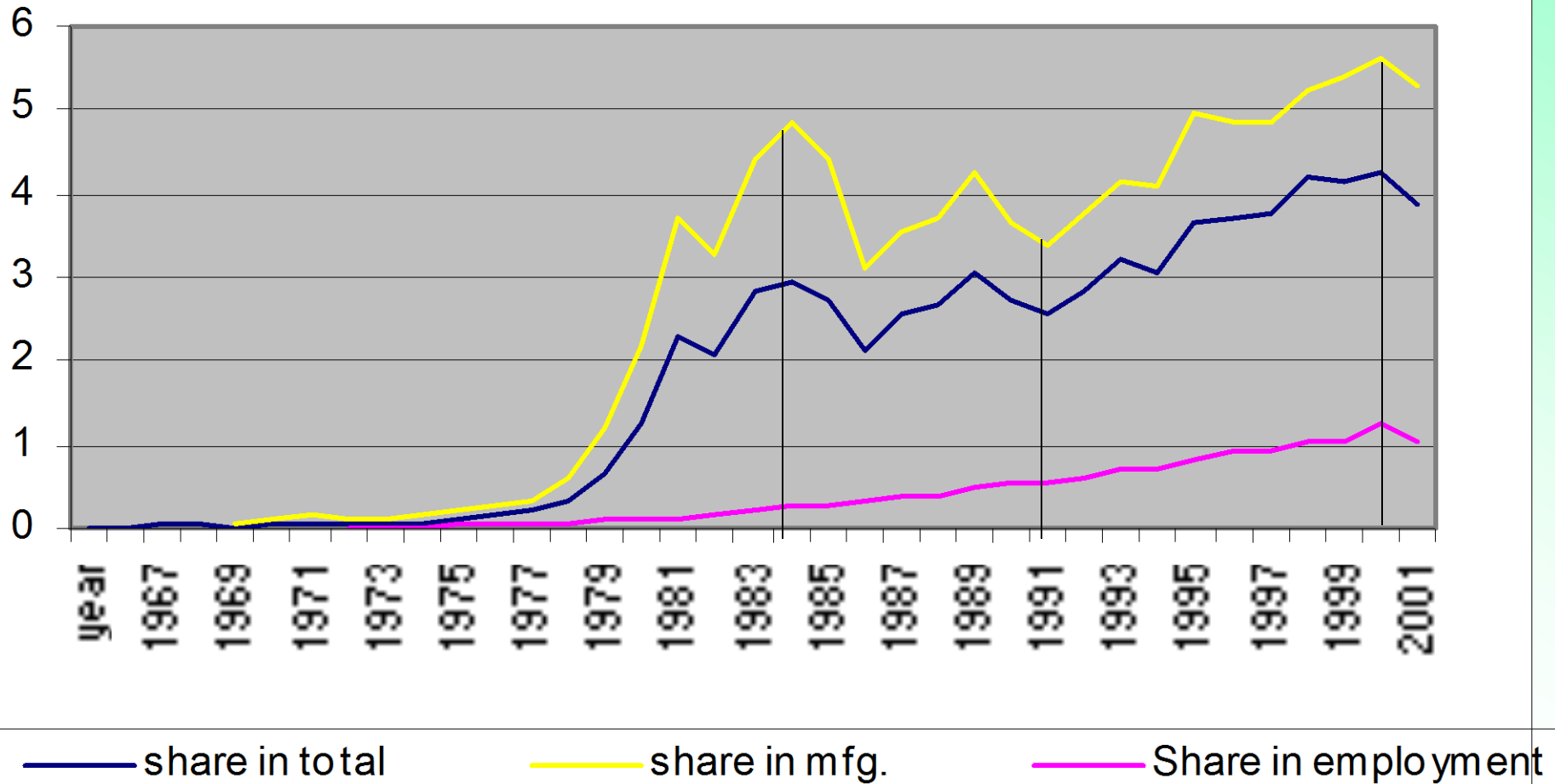
# Phase I National level performance: Employment and export growth rates across seven zones in India



—◆— Mvepmgr

—■— MVEXPGR

# Share in total and manufactured exports at the national level: Phase I



# Why could EPZs not make a substantial impact at the national and regional levels in Phase I: Was it good economics?

- India in the initial stages of growth with unemployment and low incomes
- Development strategy : A three pillared strategy
  - heavy industries with public sector assigned commanding heights (contrary to comparative advantage theory)
  - planned economy
  - Import substitution
  - Development of industrial estates
- **This means**
  - Issue of unemployment
  - Lack of industrial capacity
  - Anti export bias and foreign exchange issues
- Justification of SEZs from the perspective of all theoretical approaches: EPZs could be testing lab for market driven policies:
- **Was it a missed opportunity?**

# Was it politics or bureaucracy?

## Political factors ?

- Inclusive development state and democratic institutions
- lack of vision and strategy- Not seen as a major tool of industrialisation

## But bureaucratic failures : major bottlenecks

- Absence of legal apparatus
- Over cautious approach
- Spilling of outside economic environment into zones
- Lack of understanding
- Weak micro economic climate
- Poor meso-climatic factors
- Improvement in macro environment but relative advantages of EPZs did not improve.

- **EPZ of the first phase: Essentially, a bureaucratic failure.**

# The Transition Phase : Phase II

- Private SEZs permitted.
- The SEZ package was enhanced
- No major changes in the political or bureaucratic set up

# The SEZ regime phase III: 2005 onwards

- The SEZ act 2005 came into force in September 2005 to promote the export zones. On 10<sup>th</sup> Feb 2006, SEZ Rules also were enforced to promote SEZs in the economy.
- SEZs comprise of FTZs, EPZs, SEZs, Enterprise specific, and highly specialised zones, hybrid zones, country specific zones.
- First major effort to
  - use SEZs for large scale industrialisation in India.
  - To leverage capabilities of the private sector to drive industrialisation in the country
- Attractive incentives for private SEZ developers
- Supportive bureaucracy.

# The Rise of SEZs: Unprecedented expansion

Period	Number of zones set up	Ownership	Area (in hectare)
1995-2000	7	Central government...7	894.4
2000-2006	12	State government----5 Private sector-----7	1817.5
2006-2011	581*	State governments ...119 Private... 462	63,608.27

\*Formally approved zones between 2006 and 2011.

Source: Data compiled by the author

# Expansion in employment and Investment

Employment (Number)					Investment (Rs. Billion)				
1988	2000	February, 2006	March, 2011	March, 2012	1988	2000	Feb., 2006	March, 2011	March, 2012
<b>25625</b>	81371	129,704	676608		8.97		49.5		2018.75
						17.84		2028.05	



# A sharp increase in the share of SEZs in National Exports

Year	National	SEZ ( Rs billion)	Share (%)
2005-06	4657.48	228.4	3.17
2006-07	5828.71	346.14	3.78
2007-08	6680.00	663.38	6.43
2008-09	8580.00	996.89	7.41
2009-10	8633.00	2207.11	16.76
2010-11	11395.00	3158.68	18.11
2011-12	14825.00	3644.78	16.82

\*: Total national exports are inclusive of service exports

*Source:* Calculations based data from the Ministry of Commerce and Reserve Bank of India.

# Skill intensive and service SEZs proliferated : (Sep, 2010)

Type of SEZ	No. of notified SEZs
Pharmaceutical	18
Engineering	18
Mineral	7
Textiles	12
Multi-product	15
Chemicals	4
Multi-Services	8
Agro processing	9
Footwear	3
Others	3
<b>IT/ITES</b>	<b>206</b>
Bio-technology	18
conventional energy	6
Gems and Jewellery	6
<b>Total</b>	<b>374</b>

# But soon the descent began in terms of number and investment

	Approval (No.)	Notified (No.)	In principle approval (No.)	Operational (No.)	Land (hectare)	Units (No.)	Investment (cr)	Employment (No.)
<b>As on 17.07.2012</b>	589	389	48	153	71,502	3,400	380,284 (31.03.2012)	844,916 (31.03.2012)
<b>As on 21.01.2015</b>	491	352	32	196	56,067	3,864	201,875 (as on 30.0.2014)	1,350,071 (as on 30.9.2014)

# Was it Economics ?

- **Economics**

- Favourable macro conditions and international conditions (initially)
- Private sector capabilities, outward mobility of capital
- Heterodox approach
- New international division of labour
- Location of SEZs and agglomeration economies
  - SEZs are located in the proximity of industrial clusters
  - SEZs within industrial estates
  - Hybrid SEZs
  - Clusters of small SEZs
- Increasing share of SEZs in exports, employment and investment

# Was it a political failure? or Was it a bureaucratic failure?

- **Politics of SEZ**

- Political differences: Confusion at the top levels within the govt
- Mismatch between the ‘inclusive state philosophy’, political haste and public opinion due to issues related to land acquisition, tax revenue, inequities, rent seeking
- Astro turf or grass-root movement?
- Low political returns in the vote bank politics (lack of vision, political will power and strategy)
- Federalism ( lack of coordination between the centre and state governments)

- **Bureaucratic failures**

- Confused bureaucrats
- Sheer lack of understanding of SEZs and their potential
- Submission to the politicians’ authority in a democratic set up.

- **Politics mattered.**

# Conclusion

- SEZ success calls for
  - coordination between economics, politics and bureaucracy.
  - sound economic rationale supported by long run vision and strategy in place.
  - strong political will power and dynamic approach with favourable public opinion
  - well educated bureaucracy, and
  - A sound implementation strategy

*THANK YOU*