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Federal Government Special Economic Zones (SEZs) Policy: Issues for Legislative Action

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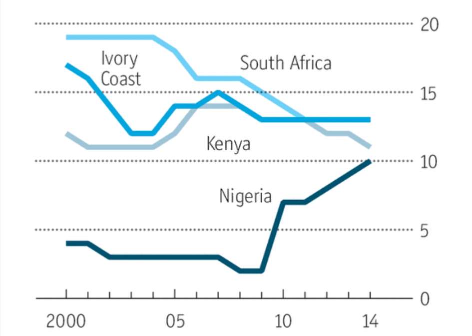
Overview

As part of its effort to drive its diversification agenda, the Federal Government of Nigeria announced its plan to set up 6 Special Economic Zones (SEZs) across the country. The Ministry of Industry, Trade and Investment is mandated to facilitate the setup of the zones. The specific goals include to help overcome the infrastructure disadvantages faced by local manufacturers, and promote the cluster effects gained by locating similar manufacturing businesses together. Special economic zones, referred to as SEZs, have become increasingly common as countries have shifted from import substitution policies to export-led growth policies. They are used by governments all over the world to promote trade and FDI in the host countries. While the Federal Government have indicated its desire to establish six (6) SEZs across the geopolitical zones in Nigeria, evidence from developing and emerging countries shows that several factors are considered by countries that have used SEZs to drive their diversification process. This brief examines these issues and highlights possible ways forward for Nigeria. While it is observed that countries like India and Philippines have success stories with SEZs, enacting legislation for SEZs played a significant role in the successful establishment and operation of SEZs in these countries. Nevertheless, the downsides associated with SEZs include loss of initial revenue to government through high incentives and environmental degradation in the geographical location of the SEZ. Nonetheless, the benefits of SEZs in creating jobs remains outstanding.

I. Background and Conceptual Clarification

1. One of the major problems facing Nigeria today is her weak industrial base. Relative to South Africa and Egypt, the contribution of manufacturing to the Nigerian economy, places Nigeria far behind the Newly Industrializing Countries (NICs) of the South East Asia[1]. Manufacturing in Nigeria has largely been dominated by a valorisation of raw materials and import-substitution type that are capital intensive rather than labour intensive. The rapid decay of industries that once flourished in the 80s such as textile and assembling plants, is also regrettable. The general low level of inter-industry linkages-failure have only helped to worsen the situation as industries cannot benefit from vertical and horizontal integration processes. As such, many have argued that Special Economic Zones (SEZs) can be used to salvage the situation in Nigeria.

Figure 1: Manufacturing as a Share of GDP: 2000 – 2014 in Selected Countries



Source: World Bank/ The Economist, 2016

2. A Special Economic Zone is a geographical region that has economic laws that are more liberal than a country's prevailing economic laws. In India, SEZs are specifically delineated, duty-free enclaves that can be deemed as foreign territory for the purposes of trade operations, duties and tariffs. They can be set up by any private or public, joint or exclusively State-owned, or even foreign-owned company. SEZs constitute a mechanism by which export-oriented industry can, with government assistance, achieve exemption from a large range of tax obligations. Common features of SEZs include: (a) A geographically defined area, and (b) Streamlined procedures – such as for customs, special regulations, tax holidays – which are often governed by a single administrative authority.

Table 1: Conceptual Analysis of SEZs Types

Types	Definition/ Characteristics	Comments
Free Trade Zones (FTZ)	Characterised as being a geographically fenced-in, tax-free area that provides warehousing, storage and distribution facilities for trade, shipping and import/export operations in a reduced regulatory environment. Have less stringent customs controls and sometimes fewer labour and environmental controls.	Other countries may benefit at the detriment of Nigeria.
Export Processing Zones (EPZ)	Similar to FTZs in that they encompass land estates that focus on foreign exports, but they differ in that they do not provide the same degree of tax benefits or regulatory leniency.	Other countries may benefit at the detriment of Nigeria.
Enterprise Zones	They provide the benefits of local, centralised development efforts; are generally created by national or	Would require government funding hence, not sustainable

[1] Ajayi, D.D (2011), 'Nigeria's Industrial Development: Issues and Challenges in the New Millennium' https://www.witpress.com/Secure/elibrary/papers/SDP11/SDP11059FU1.pdf

	local governments to revitalise or gentrify a distressed urban area.	
Single factories	Are not geographically delineated; do not have to be located within a designated zone to receive trade incentives.	Has the political advantage of not being located in geo-political zone but not effective in achieving its goals.
Freeports	Freeports are typically expansive zones that encompass many different goods and service-related trade activities such as travel, tourism and retail sales.	Other countries may benefit at the detriment of Nigeria; leads to revenue loss and could discourage the budding local enterprises.
Specialised Zones	Established to promote highly technical products and services unique to an industry.	The various GSM/ Computer villages in the country could benefit from this kind of arrangement. However, other countries may benefit at the detriment of Nigeria.
Industrial Parks	These are facilities (buildings) that are set aside for production and business services in order to attract new businesses by providing integrated infrastructure in one location and localised environmental controls that are specific to the needs of an industrial area.	Seems best suited for Nigeria and has the advantage of creating jobs, promoting business start-ups.
Spatial Development Corridors	Spatial development corridors connect two or more economic nodes by means of transportation networks, and accommodate various economic activities along the corridors.	Would benefit two zones linked through transport e.g. Lagos and Kano via rail. Has the advantage of promoting business growth in the connected states.
Industrial Development Zone	An industrial development zone is a purpose-built industrial estate linked to an airport or sea port that leverages domestic and foreign fixed direct investments in value-added and export-oriented manufacturing industries and services.	

Source: UNIDO Report on Economic Zones in the ASEAN, 2015 & Authors Comments

II. Cross Country Experience

3. Special economic zones (SEZ), are being increasingly used in the economic development strategies of many countries in Asia. Most member states opt for special economic zones (SEZs) to attract investors, create jobs and increase export earnings. Examples with the implementation of SEZs in some countries are discussed.

4. India established SEZs to accelerate the economic growth of the country through increasing export and to attract foreign investment. The Government also provide extensive range of incentives and tax exemptions for all those who invest in these Zones. The Special Economic Zone Act 2005, was passed to provide a legal framework for SEZs in India. Cambodia also have a legal framework for its SEZs. Like India, its Act was passed in 2005. The country has started with about 35 SEZs. Only 14, however, are currently operational according to available data.

5. Unlike India and Cambodia, countries like Vietnam and Lao Peoples Democratic Republic (PDR), have a master plan to spell out the rules to govern the operation of SEZs. A master plan was approved in 2015 for the creation of 400 industrial parks and 18 economic zones by 2020 in

Vietnam with the aim of attracting FDI to the manufacturing sector. There are about 295 industrial parks, 3 technology parks and 15 economic zones in Vietnam all of which are under government control. According to reports by the UNIDO in 2015, all 58 provinces in Vietnam have at least one economic zone. These SEZs in Vietnam account for about 40% of its GDP and 45% of export value. Also, SEZs in Vietnam are under the responsibility of provinces, with the central government only having a coordinating role.

6. Though SEZs were established in the early 2000s, the operation of SEZs in Lao PDR have remained relatively shallow. The aim of SEZs in the country is to attract investors from a broader range of economic sectors, thereby contributing to the diversification of the economy, which is strongly driven by investment in natural resource. As such, though 10 zones were initially developed, only 2 are fully operational in Lao PDR. The focus of SEZs in Lao PDR to develop natural resource rather than invest in manufacturing and other non-natural resource aspects of the country's industrialization has been blamed for this woeful experience.

7. The Philippines is another country whose SEZs are well established by an Act of Parliament. The country hosts well over 300 economic zones administered by the 18 different investment promotion agencies which have contributed significantly both to FDI inflows and to exports. The Philippines Economic Zone Authority (PEZA) alone owns three eco-zones and administers the incentives for over 300 privately-managed zones. These include 21 agro-industrial economic zones, 216 IT parks and centres, 64 manufacturing economic zones, 19 tourism economic zones, and two medical tourism zones (as of May 2015). PEZA also have a good reputation among investors for its one-stop, non-stop service. Other major zones in the Philippines include Subic Bay Metropolitan Authority (SBMA). The SBMA was the overall winner for Asia in 2015 of the FDI Global Free Zones Award, owing in part to its performance in encouraging reinvestment. An Act of Parliament facilitated the SBMA. On March 13, 1992, the Philippine Congress passed Republic Act (RA) 7227, known as the Bases Conversion and Development Act of 1992. Section 13 of RA 7227 created the Subic Bay Metropolitan Authority (SBMA) to develop and manage the Freeport which provides tax and duty-free privileges and incentives to business locators in the special economic zone. The SBMA plays a significant part in promoting the industrial, commercial, investment, and financial areas of trade in the Philippines.

III. Lessons from Other countries

i. SEZs play a key role in the government's FDI attraction strategy. As such, it is important to ensure coherence between SEZs and the overall investment policy framework of the country;
ii. Countries where an Act of parliament was used to drive SEZs (such Philippine, India and Cambodia) have more success stories than those without (such as Vietnam and Lao PDR). It would be important therefore, for Nigeria

to toe the line of considering a legislation to drive its SEZs.

iii. Engaging anchor investors and other stakeholders in the preparatory phase, will be crucial. This is to ensure that the legislation covers all relevant aspects including the establishment of necessary institutions and regulations.

IV. The Downside of Special Economic Zones

i. The development of SEZs has not come without significant costs. Although SEZs bring about employment and job creation for citizens, the location of SEZs is often associated with environmental degradation.

ii. Also, one of the reasons for investor success in some SEZs is that they avoid many of the costs of taxation, labour standards, human rights oversight, and safety and environmental regulations to which other sectors must adhere when doing business.

V. Conclusion and Recommendation

8. Another benefit of SEZs in Nigeria is that it will reposition Nigeria to contribute significantly to intra-Africa trade. Africa is experiencing exceptionally low levels of intra-Africa trade. This low level is restricting the potential development of the African continent. Currently, Africa's entire share of world trade is less than 3% (according to UNIDO report in 2015). This situation is attributed to Africa's narrow range of exports and over-dependence on primary products. One such policy instrument used to address such one sidedness is the implementation of special economic zones (SEZs). Some countries have established SEZs to increase foreign exchange earnings while others have aimed to stimulate production of non-traditional exports such as electronics and automobiles. SEZs have also been located in disadvantaged regions or cities to tackle unemployment.

9. As part of its effort to drive its diversification agenda, the Federal Government of Nigeria announced its plan to set up 6 Special Economic Zones (SEZs) across the country. This brief examines these issues and highlights the possible way forward for Nigeria. While it is observed that countries like India and Philippines have success stories with SEZs, enacting a legislation for SEZs was found to play a significant role in the success establishment and operation of SEZs in these countries. Nevertheless, the downsides associated with SEZs include loss of initial revenue to government through high incentives and environmental degradation in the geographical location of the SEZ. Nonetheless, the benefits of SEZs in creating jobs remains outstanding.

The views expressed in this Research Issue Brief are those of the author(s) and do not necessarily represent the views of the Institute and its Management.

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