A catalyst for investments: Prospects and challenges

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Special Economic Zones (SEZs) are areas within a country with special economic regulations aimed at enhancing its investments including foreign direct investment (FDI). They enable businesses to produce and trade goods at globally competitive prices by offering liberal policies, in contrast to the rest of the country, regarding investment, taxation, trading, quotas, customs, and labour regulations. SEZs have been successfully used by many emerging economies including China, India, the Philippines, Malaysia etc., as a catalyst for investment.

A typical SEZ has the following attributes: (a) geographically delimited area; (b) single management authority; (c) eligibility of benefits based upon physical location within the zone; and (d) separate customs area and streamlined regulations and procedures. Through SEZs, governments aim to develop and diversify exports while maintaining protective barriers, to create jobs, and to pilot new policies and approaches (e.g., in customs, legal, labour, and public- private partnership or PPP aspects). The other major advantage is opportunity to streamline regulatory processes and providing efficient 'one-stop' services as well as ensuring compliance with all regulatory requirements like labour, environment, building code, work place safety etc. It is important for countries with poor infrastructure and limited land access, as it provides on-site infrastructure (like fully serviced sites with purpose-built facilities for sale or lease) aimed at enhancing the competitiveness of manufacturers and service providers. SEZs are also intended to realize agglomeration benefits; i.e., the benefits that firms in related industries obtain by locating near each other or 'agglomerating'. Agglomeration benefits arise from economies of scale and network effects, resulting in lowering the costs of production of firms through competing multiple suppliers, greater

specialization and improved division of labour. OTHER COUNTRIES HAVE BENEFITTED: Special Economic Zones (SEZs) have helped many countries in overcoming business environment — and investment climate-related constraints. SEZs were established by China to serve as "demonstration areas" for policy reforms and to encourage foreign investment. The very well-known Shenzhen SEZ provides a snapshot of the impact of the SEZs on China's economic development. More than two decades of growth has transformed Shenzhen from a small fishing village to a thriving urban metropolis, and in 2003 it had an export value of $48 billion per year, $30 billion in FDI stock, and 3.0 million people directly employed. This all happened because of right policy, good business and regulatory environment. Past experiences, from countries that have successfully implemented SEZs, suggest that maximizing the benefits of such zones depends on the degree to which they are integrated with their host economies and the overall trade and investment reform agenda. In particular, when zones are designed to pilot legal and regulatory reforms within a planned policy framework, they are more likely to reach their objectives. The success of zones is also critically linked to how they are developed, managed, regulated, and where they are located. Management of zones is enhanced when they are operated on a cost-recovery rather than a subsidized basis, and are market-oriented and customer-focused. This aspect is likely to be more effective if private sector groups on a commercial basis undertake zone development and operation. Another major factor contributing to the outcome of the zone programme is the autonomy and effectiveness of the body charged with regulating zone operations. WHY SEZS FOR BANGLADESH: A key challenge for Bangladesh has been lack of adequate levels of private investments including FDI because of poor business environment as measured by different global indices. Bangladesh persistently ranks among the lowest in key performance measures, such as the World Bank's Ease of Doing Business ranking and the Global Competitiveness Index, suggesting that investors are facing serious constraints.
 Bangladesh's 'hard' infrastructure, necessary for triggering higher private investments, is also severely lacking, as exhibited by Table 1. Added to all these is the challenge of getting access to land for setting up of an industry. As a result of such a challenging investment climate, Bangladesh's average net FDI level of less than 1.0% of gross domestic product (GDP) is the lowest among the regional competitors (Figure 1).

Getting the business environment and infrastructure challenges fully corrected can be time

consuming, so setting up of economic zones can be a way to move forward. For developing countries like Bangladesh, setting up of Economic Zones (that includes SEZs, Export Processing Zones or EPZs, etc.) has both policy and infrastructure rationale. On the policy side, it includes measures meant to boost investment competitiveness and reduce business entry and operating costs, which can be a useful tool as part of an overall economic growth strategy to enhance industry competitiveness and attract investments including FDI. On the infrastructure side it can plan on providing the right type of infrastructure within a limited serviced land area, thereby also reducing challenge of access to land, thus maximizing on economies of scale. Bangladesh has quite a long experience in setting up economic zones through the EPZs in different parts of the country, exclusively to promote exports. A big part of the FDI in manufacturing sector is located in the EPZs. While Bangladesh has been successful in developing and maintaining EPZs since the 1980s under the Bangladesh Export Processing Zone Authority (BEPZA), the limitations of the EPZ model in creating spillovers to the domestic economy soon became apparent. Taking lessons from China and other successful East Asian countries, the government enacted the Bangladesh Special Economic Zones Act in 2010. Under this Act, the government has also set up a new institution, the Bangladesh Economic Zones Authority (BEZA). The expectation is that under the new SEZ paradigm, with a regulatory authority in place, there will be quick implementation of new Zones so that local firms can also harness spillover impact from FDI. To overcome many of the deficiencies of good business environment and also to make necessary infrastructure and serviced land available to potential investors, it is imperative that Bangladesh rapidly establishes the identified SEZs based on good feasibility studies. Bangladesh can use these SEZs to pilot regulatory/institutional reforms that improve business environment and reduce infrastructural bottlenecks, thereby acting as a catalyst for domestic and foreign investments to take advantage of the opportunity that the global manufacturing landscape is providing. Such zones could, thus, potentially bring in FDI that could help link Bangladesh to the global value chains and in the process diversify its export base. Nevertheless, over long term the focus should be to learn from SEZ experience and improve the investment climate and regulatory oversight throughout the country.