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Prospects for Urban-centric Industrial Development of Pakistan under CPEC

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INTRODUCTION:

Industrial sector plays a vital role in the long run economic growth of an economy. From early-nineteen century, many economies have taken up the export-led economic development policies. For the purpose they constituted the hard and soft infrastructure development policies, with an objective to strengthen industrialization in the economy, modernize export base, enhance innovations and value addition via attracting foreign direct investment (FDI) and technological transformation. These hard and soft infrastructural provisions were provided globally for industrial development, but in the late 1980s with the inception and success of China's Special Economic Zones (SEZs) policy, the concept of SEZs become popular.

Special Economic Zones are a global phenomenon and share some common characteristics. Generally, SEZ is a geographically delimited area, usually physically secured, it has a single management or administration, offers benefits for investors physically within the zone, has a separate customs area (duty-free benefits) and streamlined procedures⁴. In addition, an SEZ normally functions under more liberal economic regimes than those typically prevailing in the economy. SEZs contribute to

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⁴ Farole, T. (2011). Special economic zones in Africa: comparing performance and learning from global experiences. World Bank Publications.

two main kinds of paybacks and advantages to the economy. These benefits are the core objective of setting up of SEZs and their use as a key policy tool for industrialization around the world. The benefits can be broadly divided into two main categories. First kind is known as “static” economic benefits. These include employment generation, export boost-up, government tax incomes, and foreign exchange earnings; and the second is the “dynamic” economic benefits such as skill up gradation, technology flow, knowledge spill overs, innovation, value addition, economic diversification, enhancement in total factor productivity of local firms, and so on.

Special Economic Zones (SEZs) have also been used as a prominent policy tool for sustainability and long run economic growth all over the world. Various countries have developed, modernized their existing SEZs, and established new SEZs to rapidly attract the FDI, promote trade through liberalization, and boost up their economies. The number of SEZs have increased from 79 across 29 countries in 1975 to 3,500 across 130 countries in 2006 and 5000 SEZs in 135 countries till date. During this time the employment in SEZs also almost tripled, from 22.5 million to 66 million⁵. To date, China has built around 1750 SEZs at state and provincial levels⁶. By the outset of these SEZs more than 30 million jobs have been added into the labour market of China. National statistics from China portray a positive picture of SEZs to the Chinese economic growth, as they contribute 60% to exports, 46% to FDI, and 22% to that characterize them as SEZ⁷.

⁵Aggarwal, A. (2005). Performance of export processing zones: a comparative analysis of India, Sri Lanka and Bangladesh. *Indian Council for Research on International Economic Relations*, 155, 10-13.

⁶Khan, K., & Anwar, S. (2016). Special Economic Zones (SEZs) and CPEC: Background, Challenges and Strategies.

⁷World Bank (2008). Special Economic Zones: Performance, Lessons Learned, and Implications for Zone Development.

Why does Pakistan need SEZs? The basic reason remains that Pakistan aims to use SEZ development as a tool to fulfil infrastructure requirements, which once improved, will further attract foreign direct investment (FDI). The need for SEZ development has been strongly realized in the China-Pakistan Economic Corridor (CPEC). CPEC portfolio includes projects for regional connectivity, power generation for economic activities and industrial cooperation for infrastructure development and re-building of Pakistani manufacturing sector via the development of nine prioritized Special Economic Zones (SEZs). These SEZs are located in different regions all over the country, including Punjab, Sindh, Balochistan, Khyber Pakhtunkhwa (KPK), Azad Jammu and Kashmir (AJK), Federal Administrative Tribal Area (FATA) and Gilgit Baltistan (GB). SEZ development in Pakistan is under the domain of Board of Investment (BOI). To attract the investor and particularly the private sector and FDI, the BOI offers a package of financial incentive to the investors from across the world. Besides the financial modalities and industrial benefits of SEZ development, the implications of SEZ development on the urban development also need to be considered. The experience in the last 70 years with the industrial clusters in Pakistan have shown that large slums are generally formed in the neighborhood of these industrial clusters/zones. Moreover, the assisting population creates pressure on the municipal service delivery system as well. The SEZ model in Pakistan should recognize concerns associated to the urbanization and focus on developing the self-sustaining industrial settlements, so that the augmented economic activity does not create burden on the existing setting, and the municipal service delivery remains efficient and effective as well. This policy paper briefly reviews the international best practices for urban development in the existing SEZs all over the world, with a special focus on the Shenzhen Special Economic Zone (SSEZ) of China and provides brief policy recommendations for the proposed SEZs under CPEC framework in Pakistan.

The review of literature regarding worldwide successful SEZs suggests that one of the important components of a SEZ success and fruitfulness is its “location”. Indeed,

a SEZ located next to an urban center and population dense area (well developed hard and soft infrastructure) will constitute a competitive labour market, have easier access to firms, capital, and skilled labor and thus can better integrate itself with local firms⁸. One of the key factors in Shenzhen as a successful SEZ was its “location”. Shenzhen a coastal city located nearby Hong Kong-became a well-established industrial state with the passage of time. Hence, Shenzhen being a coastal city and nearby to a well-established urban place developed itself as a successful SEZ with-in a short span of time. Another element that exists in almost all successful SEZs of the world is the “planned conversion of a particular area from rural community to the urban community”. Such up-graded area (as evident in the history of Shenzhen SEZ) did not just consist of geographic expansion rather it included widened scope, increased urban facilities, environmental protection, and densification of the area to attract people as employees as well as investors⁹.

Secondly, for successful operation of a SEZ, it is also vital that management of the SEZ and the industries maintain bondage of trust and mutual understanding with each other. The participation of local community in the SEZ development process at the planning stage is also important to avoid clashes, create consensus and share responsibilities for ongoing development and building trust and attaining support from community. Past experience of Indian SEZs also depicts a sound regional planning as an essential element for the success of SEZs¹⁰. Regional planning by state-level and local level authorities includes how to improve public services and delivery of services. In the above-mentioned countries (China & India) SEZs development also focused on the establishment of modern transportation networks to facilitate the local population around SEZs.

⁸ White, J. (2011). Fostering innovation in developing economies through SEZs. *Special Economic Zones*, 183.

⁹ Wong, K. Y. (1987). China's special economic zone experiment: an appraisal. *Geografiska Annaler. Series B. Human Geography*, 27-40.

¹⁰ Shah, S. (2008). Special economic zones in South Asia: A comparative analysis of Bangladesh, Sri Lanka, and India. John F. Kennedy School of Government.

Thirdly, as Aggarwal (2005) states, that better plans for urbanization, electricity supply, commercialization and recreational opportunities also help expedite the urbanization in the existing surroundings through the channel of SEZs development. Moreover, the role of government (federal, state, and local) is important in the field of environmental licensing, disseminating the SEZs concept and principles, and providing the necessary legal support. Government incentives can help industries to continuously improve their environmental and social performances. Lastly, the most common and significant success factor found in the existing SEZs of China and India is “urban governance”. This particular aspect included how plans were executed and government policies are implemented within and around the SEZs. Moreover, management capacity of the government was also found as one of the important aspects to connect SEZs, with other regions.

POLICY RECOMMENDATIONS:

Based on review of literature and best urban-specific practices for development of SEZs, some of the policy recommendations for CPEC SEZs are as follows:

- One of the key elements of successful SEZs development is the selection of the “location” of the SEZs. A SEZ should be located within the reach of a large market where the necessary infrastructure such as highways/roads have already been developed or are easier to be developed. Moreover, foreign investors generally invest in SEZs that have the “abundant” and “low-cost work force” available. Hence, future SEZs under CPEC framework should be located where they have maximum “latent competitive advantage (LCA)” and “labour at low cost”. These factors must be considered in future before the selection of location of any SEZ.

- The SEZs linked with the economic corridors will lead to agglomeration economies. One of the learning example for development of SEZ's under CPEC is the Delhi-Mumbai industrial corridor - the corridor links together industrial towns, logistics hubs, and urban nodes. Each hub carries the world class infrastructure, business centers, transport facilities, and good urban connectivity. SEZs are thus a part of the agglomeration. They are expected to be benefited from these industrial nodes and are expected to reinforce themselves further and thus contribute to economic growth. Therefore, it is imperative for Pakistan to choose the location of SEZs that are cost saving. Development of a detailed master plan for each SEZ including its adjacent areas is also needed. On the basis of location and LCA of each SEZ, value proposition for each SEZ may also be suggested in the detailed master plan.
- Urban connectivity holds pristine role in the success of any SEZ. Countries like China and India made significant changes in their infrastructure for regional connectivity and local integration of the SEZs regions with other territories. In both countries, networks for the metropolitan transport systems were designed and implemented for linking the regions with each other. SEZs in Pakistan cannot survive in isolation. They should be planned and well connected to the nearest merchant cities. SEZs in Pakistan will be strengthened if they are integrated with the networks of logistic hubs as well as established both by the public and private sectors.
- Traditional SEZs in china have been found as the “port SEZs”; however, due to the updated infrastructure, urbanization strategies and improved regional connectivity, the modern SEZs can be located anywhere. Nevertheless, geographical clustering of firms in any SEZs should be encouraged as it results in technological spill overs, knowledge sharing, and agglomeration economies. For successful running of SEZs and clustering of firms, Pakistan

may explore the possibilities of availability of land at discounted rates or provision of concessional long term land financing may also be an option for investors.

- A comprehensive rural to urban transformation plan should be formed for the SEZ development with a definite timelines that should be visible to the investors as well. This will lead to investor's long term investment compositions and risk-factor adjustment for the investment. Similarly, policies for densification and inner city redevelopment should be formulated. Moreover, SEZs that are situated near the existing urban centre such as "M-3 SEZ" of Punjab, should be developed under a carefully articulated modern urban development strategies that include development of public transport, advance waste management systems and provision of other allied services.
- The concerned authorities of SEZs also hold a vital role. They should implement policies related to the development of linkage of SEZ with the nearest locality, provision of the basic services (housing, water, health, sanitation), and creation of entertainment and commercial enclaves. They should not only limit themselves to the maintenance of the urban facilities, but also play a dynamic role promoting the services among local entrepreneurs, suppliers, and companies in order to create backward linkages that can potentially yield urban innovations.
- In case of Pakistan, as per SEZs Act 2012, a federal SEZ's regulatory authority is required, which would not only act as an approval body but also oversee and manage all SEZs and industrial zones consistently at all levels. The said act also states that at provincial/state levels SEZs authorities may also be established, A development and management board for each SEZ, having representations from federal and provincial SEZ authorities, investors, both

local and Chinese and successful entrepreneurs need also to be constituted. The establishment of authorities at federal and provincial levels, coupled with establishment of special courts arbitration bodies for legal assistance and engagement of accounting firms may promote more peaceful, globally competitive and conducive environment for development, management and operation of SEZs under CPEC in Pakistan.

In conclusion, SEZs under CPEC can serve as an effective tool for inserting domestic economy into the global economy, if planned, developed, and managed carefully by recognising concerns associated with the urbanization. They can be homes to urban knowledge spill-overs if elements of the urbanization are carefully identified and managed accordingly. The successful operation of SEZs under CPEC can boost the economic growth in Pakistan, solve the issue of low competitiveness, and create innovation. However, the benefits can only be reaped when Pakistan couples the operation of CPEC SEZs with industrial transformation and also examines the potential for urban services, logistics, information technology, and other business services. In a nutshell, SEZs under CPEC can act as a key tool for growth and development provided they are developed on the basis of best urban practices and lessons learnt from national and international experiences.