

Special Economic Zones: A Comparison of the Economic Policies of China and Pakistan

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Abstract

China established Special Economic Zones (SEZs) in the late seventies and eighties which later became major drivers of their economic development. Now China is replicating the same phenomenon in Pakistan under CPEC. China, through the China Pakistan Economic Corridor (CPEC), the flagship project of One Belt One Road, has pledged to invest sixty-two (62) billion US dollars in Pakistan. The development of SEZs in Pakistan is divided into two phases. Phase one started in 2012, and the main focus in this phase was on Dhabeji, Rashakai Faisalabad. In phase two nine SEZs will be developed. If Pakistan successfully manages the SEZs it will shift the country towards industrialization in the long run and stabilize the Pakistani economy in the short run. However, many inconsistencies have originated due to Pakistan's weak economic policies. This paper will provide a comparison between the SEZs in Pakistan and China, and how Pakistan can capitalize on the SEZs and pave the way for industrialization.

Key Words:

Poverty, Protoindustrialization, Trade Deficit, Foreign Direct Investment, Import, Export, Economy,

JEL Classification: R58, O11, M21.

Vol. III, No. II (Fall 2018)

Page: 12 – 19

p-ISSN: 2521-2974

L-ISSN: 2521-2974

e-ISSN: 2707-0093

DOI: 10.31703/ger.2018(III-II).02

Special Economic Zones (SEZs)

Special economic zones can be explained as, a specific area of land in a country that is used for increasing industrial growth and its full potential can be achieved by giving them relaxations in economic and tax policies, but these relaxations are only limited to that specified region. The term special economic zones were first coined by the Chinese. SEZs were created in China in 1980, and these economic zones played a pivotal role in alleviating seven hundred million from poverty. Massive success witnessed by many countries alongside China, other countries followed suit.

Objectives of SEZ's

The objectives of these zones are simple. Foremost is to attract foreign direct investment

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(FDI). FDI is essential for any state's economy. With this kind of investment, the flow of technology increases which in turn will create prosperity in the region. The second aim of the special economic zone (SEZs) is to generate employment. More jobs translate to more employment opportunities for the youth, which constitutes more than sixty percent of Pakistan's population. With more jobs, the wages will also increase and as a consequence, the living standard of many people will improve. The third objective is to experiment with the economic reforms which can be achieved by implementing Zone-exclusive trade policies. Relaxation in tariffs among other measures is a common practice in order to attract investment. It is a well-known policy that if governments desire enhanced foreign investment and gain maximum profit from foreign projects, they introduce relaxations in trade laws like lowering tariff rates and providing land on lease.

China's Economic Policies

After 1949 socialism prevailed all over China. Socialism in simple words is a theory in which the working class, which earns a living from working in factories, offices, etc, owns the means through which they earn. The concept of private ownership does not exist in socialism, and according to socialists, the right of ownership belongs to the community. So, after implementing socialism, the next step was to encourage entrepreneurship, which means people start their own businesses by investing everything they own, taking risks in hope of profit. When the practice of entrepreneurship became common the other thing policymakers introduced was "open door diplomacy", and through this policy other countries were invited to do businesses and invest in China. All countries were treated equally in the sense that trade laws were the same for every investor. The other sectors where China focused were the production of steel, iron, chemical fertilizers, farms tools, and hydroelectric power, for this purpose, they launched a network of township village enterprises. Rural industrialization was realized because of this project. The next thing that China included in its economic policies was "Proto-Industrialization" (ge 1999). This phase comes before industrialization; before industries, there used to be a factory system. In proto-industrialization, production was controlled by merchants, and goods were produced by vast numbers of small fabricators, which were in different places; this was the decentralized method of production. This helped China transform its agrarian economy by peasant farmers to a modern economy (Zhou 2018). After the success of previous policies, when China introduced special economic zones it introduced new policies for the Chinese in it. First, in SEZs the right to property was given to Chinese people. Second, tax incentives up to 100% were given to the investor, and this was the new strategy adopted by the Chinese government to attract investors. Other benefits of these incentives include an increase in employment opportunities; when employment increases the flow of capital also increases, along with advancement in technology which results in the development of the underdeveloped areas. Thirdly, the taxes were reduced up to 20%, this relief was given to lower the burden on people in order to build capacity so that they can open new businesses. Fourth, a land policy was introduced, according to which the owner of the land can lend his land to someone else and can make money from it. Along with the above-mentioned policy reforms, the Chinese government introduced labour laws for Chinese as well as foreign manpower. According to this law, a foreign investor can hire or fire Chinese employees anytime they want. Wages were set for the workers which were higher in

comparison to the other parts of the country, and it was done so that more labour can be attracted.

OBOR and Chinese Interests

The other interest of China under the OBOR is to introduce the Renminbi, the main trading and investment currency with the countries involved, as it will strengthen the Chinese currency against the US dollar. The other motives are the creation of OBOR banks which will give loans to the countries involved in the project. It will help China expand its monetary business and become as strong and reputable as the IMF. China wants to expand its satellite and navigation systems. According to China, they will launch 30 more Beidou satellite navigation systems. These will be launched in the period of the next five years (Jiadong Sun 2008). China wants to expand the China-controlled telecommunications networks. It is an imperative feature of the “ONE BELT ONE ROAD” (OBOR) initiative. CITIC Telecom CPC and newly assimilated Linx Telecommunications have facilities in Kazakhstan and the ‘Stan’ region, Russia, Eastern Europe and the Baltic Sea (Wade n.d.). This will provide China with telecommunications services across much of its targeted ‘Belt’ region.

China Pakistan Cordial Relations

China Pakistan ties have survived the test of time and a new age of this relationship has begun, which is not only focused on military along with economic ties but on economic dependency as well. The new dimension of this relationship is due to China’s tremendous investment in Pakistan under CPEC. Eventually, with completion of all CPEC projects in 2030, it is likely that China and Pakistan will achieve “complex interdependence” (S. Ahmed 2018). In the longer run Pakistan’s economy would flourish and China would get road access to resource-rich CARs (Minhas Majeed Khan 2016).

China initiated the OBOR “One Belt One Road” and OPEC is a smaller project under this grand scheme. Under CPEC, China will build a network of railway lines, roads, and pipelines to connect different parts of Pakistan with each other and with China, alongside providing road access to other countries, especially the Central Asian countries. In total under OBOR 65 countries will be linked together. This network of rail and road along with other advantages provides China with uninterrupted and secure access to energy resources. The networks built by the Chinese would not be exclusive to the Chinese alone; all countries which are part of OBOR can trade among themselves and will reap the benefits of this mega project. CPEC has played a role in enhancing social and cultural exchange among the Pakistani and Chinese masses. China helped many Pakistani students to study in China on scholarships in an action reciprocated by Pakistan whereby a large number of Chinese now live in Pakistan and receive education in Pakistani institutes.

SEZs in Pakistan

The development of SEZs in Pakistan will be accomplished in phases. The first phase was all about access to high-quality infrastructure, uninterruptible power supply, public facilities, and support services. The fiscal benefits given under the SEZ laws included a one-time exclusion from custom duties and taxes for all capital goods imported into Pakistan for the development purposes, and operations and maintenance of SEZs (Khan

2017). There is a ten years' exemption on income tax for all inventors as well as for the zone enterprise. The first special economic zone was developed on 14 February 2014, in Khairpur district, Khairpur Export Processing Zone. The other economic zone is Rashakai economic zone, Mardan, M1 KP; Raisalpur Export Processing Zone, Raisalpur; Gadoon Economic Zone GadoonAmazai, Swabi KPK; Gujranwala Export Processing Zone, Gujranwala, Punjab; Hathar Economic Zone Hathar Haripur KPK; Hathar Economic Zone Hathar Haripur KPK.

In phase two the focus of the SEZs will be on the revival of the industrial revolution in Pakistan. Industry which was once thriving is now in a critical condition. This downfall in the industrial sector has resulted in financial crises for Pakistan. Currently, Pakistan is going through a severe balance of payment crises mainly due to our limited exports. The revival of the industries will help Pakistan in increasing its exports and attract foreign direct investment; its economy will improve systematically under the SEZs and eventually jobs opportunities for Pakistani youth will be created. This all will ultimately assist Pakistan's economy towards an uphill trend and its image will improve as well. In phase two nine special economic zones will be developed. These are Rasakhai economic zone, M-1, Nowshera, Allam Iqbal industrial city (M3), Faisalabad, Boston industrial zone, Mohammad marble city, Moqquadass SEZ Gilgit-Baltistan, ICT Model Industrial zone, Islamabad, China special economic zone Dhabeji, Pakistan Steel Mills Land at Port Qasim near Karachi, and Special Economic Zone Mirpur, AJK. These SEZs will be completed by 2035 (Ministry of Planning, Development & Reform 2018).

Failure of Industrialization efforts in Pakistan and its causes

Previously many efforts were made for industrialization, but all the efforts failed because of the following reasons; the negative role played by the international financial institutions as the structural adjustment program is not compatible with the local financial system, thus devaluing of the currency which has always severely affected the economy. The growing and ever-persistent trade deficit is a major hurdle when it comes to the Pakistani government's investment in the industrialization sector, and even attempts of revival are hampered due to the balance of payments crises. There is active resistance from the elite and bureaucratic structure, which hampers the formulation and implementation of any genuine policy reforms that will assist the industrial revolution in Pakistan. Corrupt procedures and practices are designed by the bureaucratic administration in issuing licenses and demanding high money for it, which has an adverse effect on the small export businesses. Another factor behind failure is the rising competition in the overseas market which has affected Pakistan's domestic market severely. However, some local businesses and small textiles are thriving in the domestic market, so they can enjoy access to the foreign markets as well. The size of the Pakistan domestic market is reducing day by day which is a major driver of the economic downfall (Jamal 2016). Bad governance is another hurdle in the industrial revolution. The tussle between political parties to change the policies according to their wishes and interests by exerting influence on the government institutions and machinery is a major obstruction towards beginning an industrial revolution. Another reason for the failure is the rent-seeking behavior of already failed or failing industries.

Underutilized Potential of the Existing Economic Zones in Pakistan.

Work on SEZs in Pakistan began in 2014, some SEZs have become functional but unfortunately, these are not working up to their full potential due to a variety of reasons. Pakistan has failed in the creation of “proto industrializations”, that would have provided a basic foundation for the industrial revolution. Pakistani exports have fallen considerably and the Pakistani government is trying earnestly to address the balance of payment issues. The blows suffered by the economy are huge and the government has failed in establishing a sound foundation for the success of existing SEZs. With government change in Pakistan, the new administration tried to address financial issues with a temporary solution, i.e. to approach the IMF and to attract direct foreign investment FDI. However, to attract Foreign Direct Investment, Pakistan allowed many relaxations to potential investors in terms of tariffs and land reforms. In the case of SEZs, Pakistan’s monitoring policies were not up to the mark. There was a conflict on the ratio of Chinese and Pakistani labour which created disagreements. The Pakistani public wanted more domestic labour to be employed in these special economic zones rather than be imported from China. Another shortcoming identified by the workers was the lack of any incentives for them. No reforms for rural industrialization were introduced as it could have helped the rural community to develop and play their role in the industrial revolution.

How to Realize the Full Potential of Economic Zones in Pakistan

To yield the full potential of a special economic zone in phase 1 and to get the maximum benefit from phase 2 of SEZs, the government will have to bring major structural reforms in Pakistan. Starting with Proto industrialization in two phases, in the first phase, Pakistan will have to do the capacity building of rural manufacturing units. State machinery will have to facilitate the rural manufacturing units so that they can become the pulse of national and international markets. Secondly, rural industrialization should become so widespread socially and economically that it becomes the reason for propelling economies. It is the fastest means of alleviating poverty (Hussain 1994). Pakistan needs to make a conducive environment that will attract maximum foreign direct investment, and this can be achieved through sound policymaking. The goods produced under the special economic zones of Pakistan should secure duty-free status in China and this can be achieved only when Pakistan receives the most favoured nation (MFN) status by China. The government needs to discourage the rent-seeking behaviour of the industries, the special incentives that are given to them won’t help those industries to flourish; instead, it will affect Pakistan badly (Thomas Farole 2011). Pakistan’s economic policies have failed to achieve the desired results in the past, now it’s time to get rid of those faulty economic policies. By generating more energy resources and providing unending power supply to the industrial sector industries can perform exceptionally, but for this Pakistan would need to build hydropower reserves, indigenous coal plants, and electricity can be produced by the solar systems and wind turbines as well (Ahmed 2018). Pakistan needs to bring transparency to the projects and address the reservations raised by the political parties and other stakeholders. Lack of transparency and corruption allegations would only hinder the development of special economic zones. All the ministries must ensure speedy and effective implementation of various special economic zones. The issues of Pakistani labour should be solved quickly; it should be the number one priority of the Pakistani government. If not solved, the discontent among the workers would grow and the chances of strikes by workers would

be amplified which would consequently affect the progress of the economic zones. Pakistan is facing a major crisis in the form of its massive population under the age of thirty which is largely unemployed. SEZs if effectively run, will counter the menace of unemployment. Pakistan has taken effective measures in order to address terrorism concerns. Insurgency in Balochistan is also a major threat to the security of SEZs, Chinese personnel and foreign investment. Any terrorist attack on CPEC related projects could derail the trust of foreign investors. It would project a message to the international community that Pakistan is not a suitable place for investment. After that, it will become difficult for Pakistan to attract foreign direct investments. Most importantly Pakistan needs to mend its relationship with its neighbours Afghanistan, Iran and India and work towards their inclusion in CPEC, and especially with India since its inclusion in CPEC would multiply the benefits in terms of bilateral trade. Pakistan needs to improve ties with Afghanistan because stable relations with it would translate to stability in Pakistan. Relations with Iran are crucial as well since a cold relation with Iran will affect the development process. Good relationships with these countries are necessary as these would pave the way for Pakistani exports to reach deep into South and Central Asia (Bhola 1986).

Conclusion

The 219 special economic zones established by the Chinese contributed to the growth in GDP and helped China's economy to take off. Many claim that with the help of these SEZs China introduced the culture of entrepreneurship. China successfully implemented the structural reforms and the rest of the world followed suit. China conveyed the message that open-door diplomacy can bring back life to a crippled economy. Chinese investment under CPEC and OBOR has reached one trillion. Now China is willing to invest in Pakistan, and Pakistan is in desperate need of foreign investment. The question is whether Pakistan can reap advantages from such investment despite the prevailing flaws in the governance policies, a flawed monitoring system, huge trade deficit, huge circular debt, terrorism and the differences between the political parties. Other than this, it seems that Pakistani leadership lacks vision and insight in order to make a decision that is beneficial for the people of Pakistan. The main reason is that the feudal and elite of Pakistan do not want the government to make policies that are not favorable to them. They want an unchecked hold on the domestic market. The biggest question that the Pakistani government faces nowadays is when will structural reforms take place. A lot of time has been wasted with ineffective policies. If Pakistani policymakers didn't design any sound and comprehensive policy until 2019- 2020, then Pakistan might never be able to benefit from the investment under CPEC and the economy's take-off might become even more challenging. An elaborate study of the Pakistani economy and its financial policies will reveal major shortcomings. Pakistan has failed to create a culture of proto industrialization. More imports, very few exports, lack of foreign exchange modernization and many other things were reasons discussed in this paper. Pakistan needs to create rural industrialization and proto industrialization alongside establishing a market at home and abroad, by creating a resilient 'textile industry' and eventually becoming part of global Chinese multinational chains. This will help in improving Pakistan's exports, which will consequently pave the way for the modernization process and help in sustainable industrial development. Pakistan needs to add new players to the market every now and then, and the market must be protected from inefficient producers and monopolies who are not ready to bring change

because it is not in their interest or they are unable to compete.. The wise move by China was to replace the Maoist cultural revolution with a new era of permanent revolutions. The hurdles in the path of SEZs must be addressed by the Pakistani government. Changes and innovation need to be brought in the sectors of agriculture, industry, taxation, energy, environment, health, land, water, labour and many others. CPEC can help Pakistan in numerous ways, though in order to achieve that, Pakistan has to bring economic reforms at the domestic level.

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