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FREE TRADE ZONES: ARGUMENTS AGAINST AND IN FAVOR BASED ON EXPERIENCE OF FOREIGN PORTS

By many, a FTZ is seen as an instrument for expanding and modernising an economy through the attraction of foreign investment, the transfer of technology and employment generation. The actual impact of FTZs on national economic development has been studied frequently. However, many of these

studies are out-of-date, and country-specific. What may not be classified a success today may be different tomorrow and vice versa. Some FTZs have been real engines of outward-oriented economic growth and have had a considerable impact on industrial development. (Maria Kottari, 'The new integrated European Maritime Policy. The challenges of the maritime governance in the Mediterranean', p. 1.)

Some arguments used against FTZs

- The impact of the FTZs on the local economy is limited.
- FTZ cannot compensate for failed economic reform.
- FTZs account for only a small share of the host country's investment.
- A FTZs is only a second-best policy to develop the economy of a region.

A first-best policy would be to provide an optimum enabling environment. (Maria Kottari, 'The new integrated European Maritime Policy. The challenges of the maritime governance in the Mediterranean', p. 1.)

The Dakar EPZ established in 1974 is an example of an unsuccessful zone. The Dakar zone became operational in 1976 but did not achieve its goals in creating employment, foreign exchange. Employment reached a high of 1,200 in 1986 to drop back down to 600 in 1990. Some 10 firms exported a meagre 4 million FCFA51 (approx. US\$14.7m) out of the zone despite a relatively stable political environment and advantageous financial promotions.

There are several reasons for the zone's failure:

- red tape;
- minimum employment and investment floors;
- government mandated labour market rigidities;
- low productivity of the labour force;
- no standard rental factory space available
- high utilities and transportation costs.

But still there are a lot of arguments in favour of FTZs:

Job creation is probably the first and foremost goal of a FTZ. FTZs have created jobs and, in some cases, a remarkably high number of them. Mauritius: in 1971, the first nine EPZ firms employed 600 people, growing to a maximum of 91,000 in 1991. This represented approximately one third of total employment and 80 per cent of all jobs in industry. In Malaysia, where seven zones were created between 1972 and 1990, jobs grew from 21,000 in 1973 to some 123,000 in

1994, while the workforce in Sri Lanka's three zones multiplied eight-fold over the period 1980-1994. (United Nations publication, 'Free Trade Zone and Port Hinterland Development')

Export performance: Taiwan Province of China and the Republic of Korea: almost 100 per cent of manufactured exports; Mauritius: 95 per cent manufactured exports are produced in FTZs; Kenya: 75 per cent of manufactured exports, with the vast majority depending on the duty exemption system.

Foreign exchange. For many countries, especially low income countries, foreign exchange earnings are a prime target as they serve to finance import and the development of the local economy. For example, Mauritius: saw FTZ gross exports earnings grow from 3 per cent of total export earnings in 1971 to 52.6 per cent in 1986 and 68.7 per cent in 1994. (United Nations publication, 'Free Trade Zone and Port Hinterland Development')

Tax revenue versus tax losses. Tax incentives are a prime characteristic of FTZs. When establishing a FTZ, governments hope that the potential tax revenue losses – as a result of offer tax incentives – are outweighed by gains accrued in terms of employment creation and provision of foreign exchange earnings. In this calculation, the cost of establishing the FTZ must be included as well since it requires substantial investment in real estate, transportation infrastructure, utilities, communications facilities and administrative support.

Backward linkages. Businesses that operate from FTZs can create linkages between themselves and the rest of the economy. Linkages can take two forms: FTZ firms sourcing domestic raw material inputs or subcontracting supplies with domestic firms. An example of a successful FTZ is the situation at the Masan Zone in the Republic of Korea in 1988. A total of 56 of the 73 zone firms had engaged 525 domestic firms for outsourcing processes. These 525 employed 16,686 workers, equivalent to half of the entire Masan zone work force.

Upgrading of physical capital. FTZs may lead to upgrading of physical capital. Successful zones are those for which governments have created an efficient and competitive industrial transport and logistics infrastructure. Among the most advanced of the new kinds of zones is the one in Kaohsiung, Taiwan Province of China. It began with simple sewing in 1967, expanded to fashion garments, then to electronics assembly and then to electronic design, testing and R&D, and is now moving into the business of hosting corporate headquarters and global logistics centres.

Contribution of Logistics FTZs. The contribution of specialized logistics zones or logistics oriented FTZs is similar to traditional or manufacturing oriented FTZs. Logistics zones originally are aimed at promoting efficient logistics system by establishing or integrating logistics cluster around port or inland area. Logistics zones around port areas contribute to develop efficient domestic logistics activities resulting in logistics cost and time savings at a national level.