Special Economic Zones versus Export Processing Zones

A look at how the SEZ regime will be more effective compared to EPZ regime

Introduction

"You never change things by fighting the existing reality. To change something build a new model that makes the existing model obsolete."- Buckminster Fuller.

The words of Buckminster Fuller who was an American Architect sums it all. The introduction of Special Economic Zones (SEZs) was meant to breathe new life to Kenyans economy and achieve the goals that the previous Export Processing Zone (EPZs) failed to attain.

The EPZs were introduced to boost export-oriented investment in Kenya. The regime though favourable however, overlooked various investment gaps and neglected investment directed towards boosting growth in the local market. SEZs were set up to not only boost local and Foreign Direct Investment (FDIs), but to also widen the scope in terms of investment opportunities. The article looks at the EPZ regime its successes, shortcomings and how SEZ regime is set to surpass the impact of the EPZ regime.

Performance of the EPZ Regime

The EPZ regime has seen consistent growth and investment over the years. Key performance indicators include;[1]

Indicator	2016	2017
Number of gazette zones	65	71
Number of approved projects	30	42
Number of gazette enterprises	111	131
Investment expenditure "Kes" million	88,977	95,278
Total sales "Kes" million	68,569	67,270
Direct local employment expenditure "Kes"	9.2M	10M

EPZ programs have been launched in 19 out of the 47 counties in Kenya and include investments in 15 subsectors ranging from Pharmaceuticals, agro-processing, craft and leather work, service, garment, food processing among others. Agro processing, garment sector and service business sectors being the most popular investment areas. EPZ investment has seen both local and foreign investment as outlined in the table below;[2]

Type of Investor	% ownership of EPZ entities
Wholly owned by Kenyan	36.6%
Joint Venture Arrangement	24.5%
Foreign Owned Investment	38.9%
Total	**100%**

The EPZ regime has seen equal investment in terms foreign and local investment. The investment has spanned over many counties and different business sectors. The EPZ investment and output has also seen consistent growth over the years.

Shortcomings of EPZ Regime

At face value the scheme appears to be quite successful however there are various aspects or shortcomings that the EPZ regime has had. The regime was set up at a time when Kenya's agricultural and essentially manufacturing potential was high. The export-oriented investment scheme primarily focused on the development of these two sectors. However, Kenya is seeking to diversify its output locally and globally and explore other sectors such as ICT, Infrastructure, Tourism and Service sectors. The

[1] Export Processing Zone program Annual program report 2017- accessed on 06th February 2020 on https://epzakenya.com/water-sewerage/resources/

EPZ regime would not ideally cater for these sectors.

The EPZ regime is also focused on selling for export with a restriction of sales that can be made locally. Given the global market is highly competitive and Kenya has a robust local market, EPZs would not cater for this adequately. EPZ entities also highly relied on tax incentives to create efficiency as opposed to looking into innovating their business and output.

The EPZ regime has however also faced various setbacks which have resulted in it not effectively achieving its intended purpose. The key challenges highlighted include;[3]

- Limitation of market scope as a result of market restrictions locally and in the East African Community region;
- Constant regulatory changes which are done without stakeholder consultation;
- High production and investment costs;
- High global competition which affect sales and productivity; and
- Bottleneck challenges such as trade barriers and multiple levies.

However, one key challenge that stands out is the implementation the model was not defective and what failed is the implementation of the model. From the limited scope, consistent bottlenecks, market limitations and regulation, the SEZ model would therefore have to effectively improve on the implementation in order to surpass its predecessor.

Proposed SEZ regime

As a result of these challenges, EPZ regime was set to be absorbed into the SEZ program. The SEZ program offers more fiscal and non-fiscal incentives to investors than what EPZs offered. As a result, SEZ appeared to be a more attractive alternative for investors. The incentives include fiscal incentives such as tax incentives, negotiated utility rates, work permits among others. The non-fiscal incentives include administration incentives such as One stop shop for all procedures, land and supporting infrastructure. All of which the EPZ regime could have benefited from.

SEZ program will also incorporate various schemes from business parks to Tech parks, tourism, livestock, manufacturing as well as business service center. This broadens the investment opportunities for investors and will capture many business sectors. As a result of this the SEZ program will have a greater impact and will cater to more businesses.

SEZ program will also have no restrictions in terms of market as it is open to both local and export market. The SEZ program provides incentives that not only affect SEZ entities but also protect local market. SEZ entities looking to sell locally will face no restrictions but will have to pay taxes and levies as when selling/ importing their products to the Kenyan market. There are also plans to incorporate the SEZ program within an East African Community Framework opening up more market for these entities. The implementation of the Africa Continental Free Trade Area (AFTCA) will also boost the regional marketing power of Kenya and other African countries helping with challenges associated with global competition.

SEZ entities will also benefit from reduced utility rates and improved infrastructure as such reducing both production and investment costs for the investors, a challenge that plagued the EPZ regime. The incorporation of SEZ business support hubs and incentives for SEZ entity to entity transactions will mean reduced costs and greater efficiency.

[3] EPZ Annual Program Reports https://epzakenya.com/ accessed on the 6th February 2020.

Where can SEZ improve on

One key area would be regulation as this will impact how the program is rolled out. Currently the SEZ program is regulated through the SEZ Act 2015, various Kenyan tax legislation and the 2016 SEZ regulations. The SEZ Authority (SEZA) intends to roll out supplementary SEZ regulations. As it stands there are a lot of gaps that the legislation needs to touch on including labor law provisions, investment criteria, tax regulations especially as SEZ are a separate customs territory, inter-Governmental agency interaction among other. The EPZ regime has well established provisions especially from a Customs perspective something the SEZ regime can borrow from. In our next article we look at the current SEZ legislation and what areas or gaps that need to be covered.

Conclusion

Although it is still too early to tell how effective SEZ programs will be compared to EPZs, the increased investment and gazettement of SEZ Zones is a good measure. So far 9 SEZ zones have been gazette 3 of which are Government run with the remaining being private investments. The SEZ program has a positive outlook and poses a more favourable investment option for potential investors compared to EPZs. Investors can gauge between the two and weigh which one gives them more bang for their buck.

Let's talk

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