

Kazakhstan-Kyrgyz Republic: SEZ Framework in Two Landlocked Countries

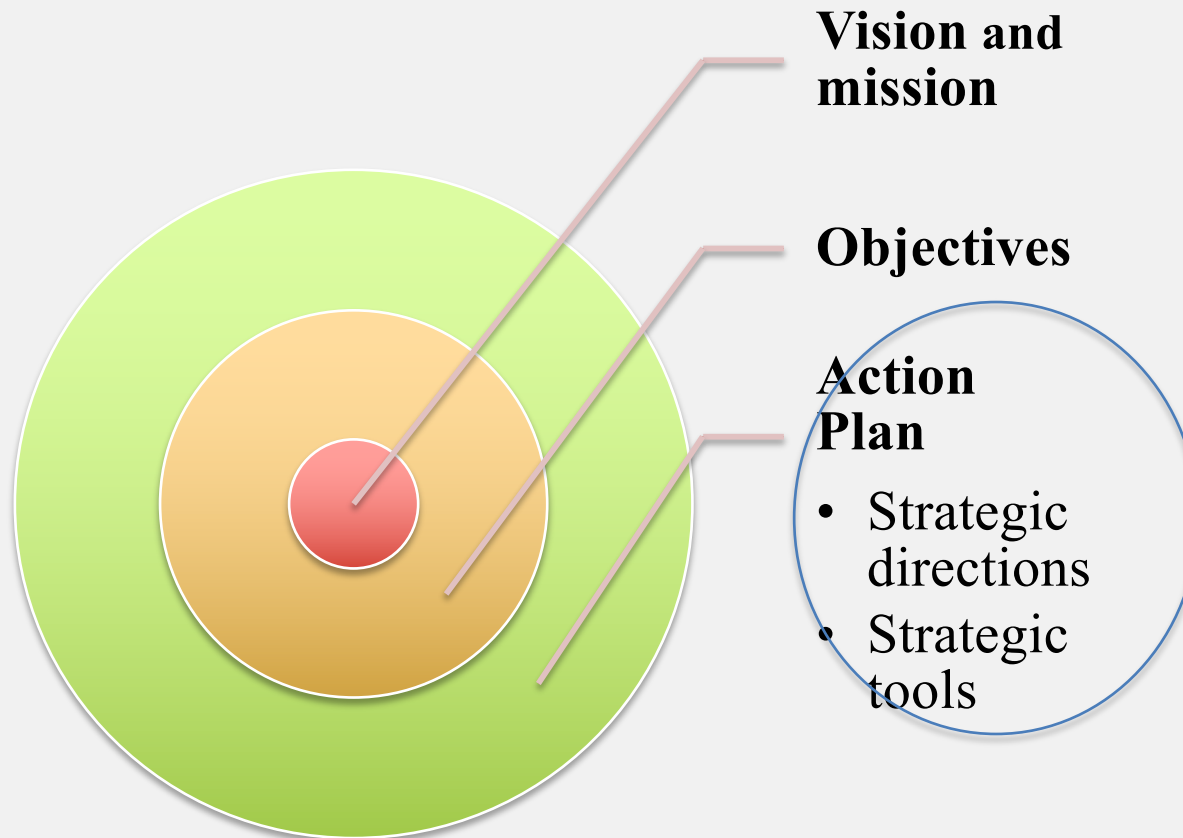
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What is the Strategic Framework



- **Given the objectives of SEZs as specified in the SEZ policy of Kazakhstan, this report focuses on**
 - The strategic positioning of the SEZs and IZs in the development strategy
 - The key approaches and instruments that can be used and adapted when promoting zones in Kazakhstan;
 - The best practices that can be adapted to Kazakhstan's context; and
 - the critical factors for effective implementation of zone policy as well as monitoring and evaluation (M&E).

The Framework for SF



Planning for SEZs

Understanding development challenges

Historical Features

At the time of independence: little productive capacity of its own

Fully integrated in the USSR internal chains

Serious disruptions following the dissolution of the Soviet Union.



Fast catch up required

Geographical features

Land Lock: Source of poverty trap

Natural resource abundance: Resource curse

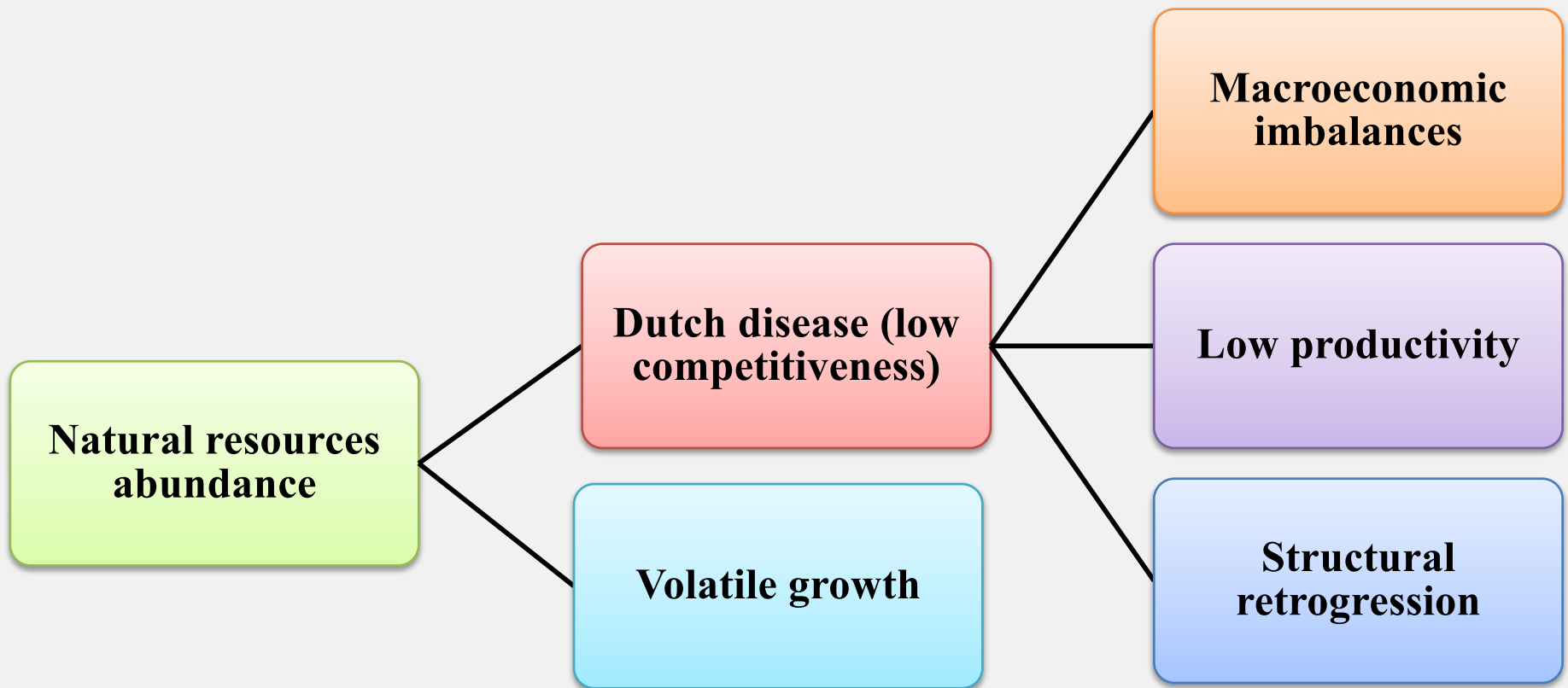


Low productivity and competitiveness

A successful strategy was adopted to avoid land lock induced poverty trap

- Envisioned to become a transport channel of global significance
 - Exploiting a unique geographical location, with potential of making Kazakhstan one of the most important transport and transit hubs for global trade.
- Infrastructure as a priority area in the early stages of development.
- Over time, major initiatives have been taken to implement a transport strategy at the national level.

However, resource abundance induced resource curse could not be avoided



The macroeconomic analysis shows...

- **Highly volatile growth rate concomitant with export commodity prices**
- **Low competitiveness manifested in**
 - High consumption rates with high balance of trade deficit
 - Low productivity: both TFP and labor
 - Inter-sectorial productivity gaps: Labor productivity in mining in 2013 was more than 6 times greater than the average of the other sectors.
 - Diminishing productivity growth between 2001 and 2015
 - Declining share of industry in particular manufacturing in GDP
 - Employment absorbed in agriculture, internal trade and hotels, and other services (i.e., administrative, health, education, defense, and recreation) with little structural bonus

- **Low competitiveness in international markets**

- **Exports:**

- The share of “manufactures” in total goods and services trade declined sharply from 40% in 1995 to around 20% in 2014.
 - At the two-digit level, three products dominate total exports.
 - Early 2000s: crude petroleum and natural gas, manufacturing of basic metals, and agricultural products.
 - Since 2004, coke and refined petroleum products entered the top three, displacing agriculture.
 - The number of products at the four-digit level in which Kazakhstan has a revealed comparative advantage declined continuously from 2004 to 2012

- **FDI:**

- is concentrated in mining and quarrying, geological exploration, and prospecting activities.

- **Regional inequalities** are large.

The major development challenge is to

- overcome the resource curse, and
- Improve productivity and competitiveness to promote manufacturing and bring about industrial diversification which is at the core of the development strategy of Kazakhstan.

What are the key competitiveness challenges

Cost-competitiveness

- High wages
- Volatile exchange rate
- High tariffs

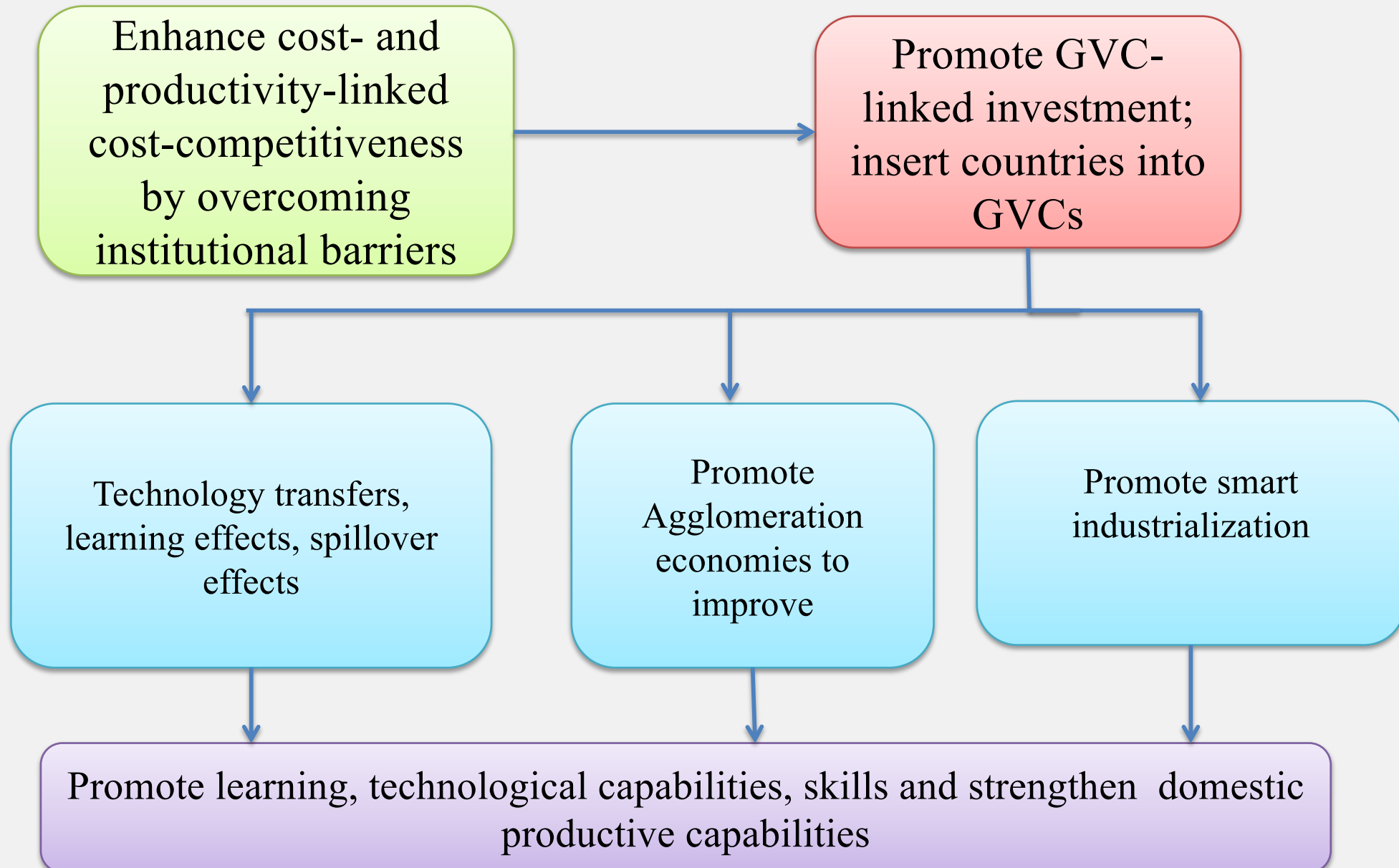
Productivity-linked cost-competitiveness

- Low governance: Corruption, bribery, lack of voice and accountability
- Energy and roads
- Custom clearances
- Business rules and regulations

Productivity-based competitiveness

- Talent and skills: low-quality education system
- Underdeveloped finance systems
- Lack of technological capabilities and low efficiency of research and development infrastructure

How can SEZs and IZs address competitiveness issues?



Limited Success of SEZs and IZs in Kazakhstan

- **Major reasons**
 - Disconnect between Objectives and Approaches
 - Disconnect between the Development Strategy and Approach toward Economic Zones
 - disconnect between the policy and the changing global trade and investment landscape, today, where the rise of GVCs has reshaped global production and trade systems
- There is a need for a strategic framework that addresses these key gaps.

SIX PILLARS

Pillar 1: Integrating the cluster development program with economic zones

Pillar 2: Promoting investment climate in economic zones

Pillar 3 : Promotion of spillovers from global value chain-linked investment

Pillar 4: Augmenting regional value chains and cross-border chains

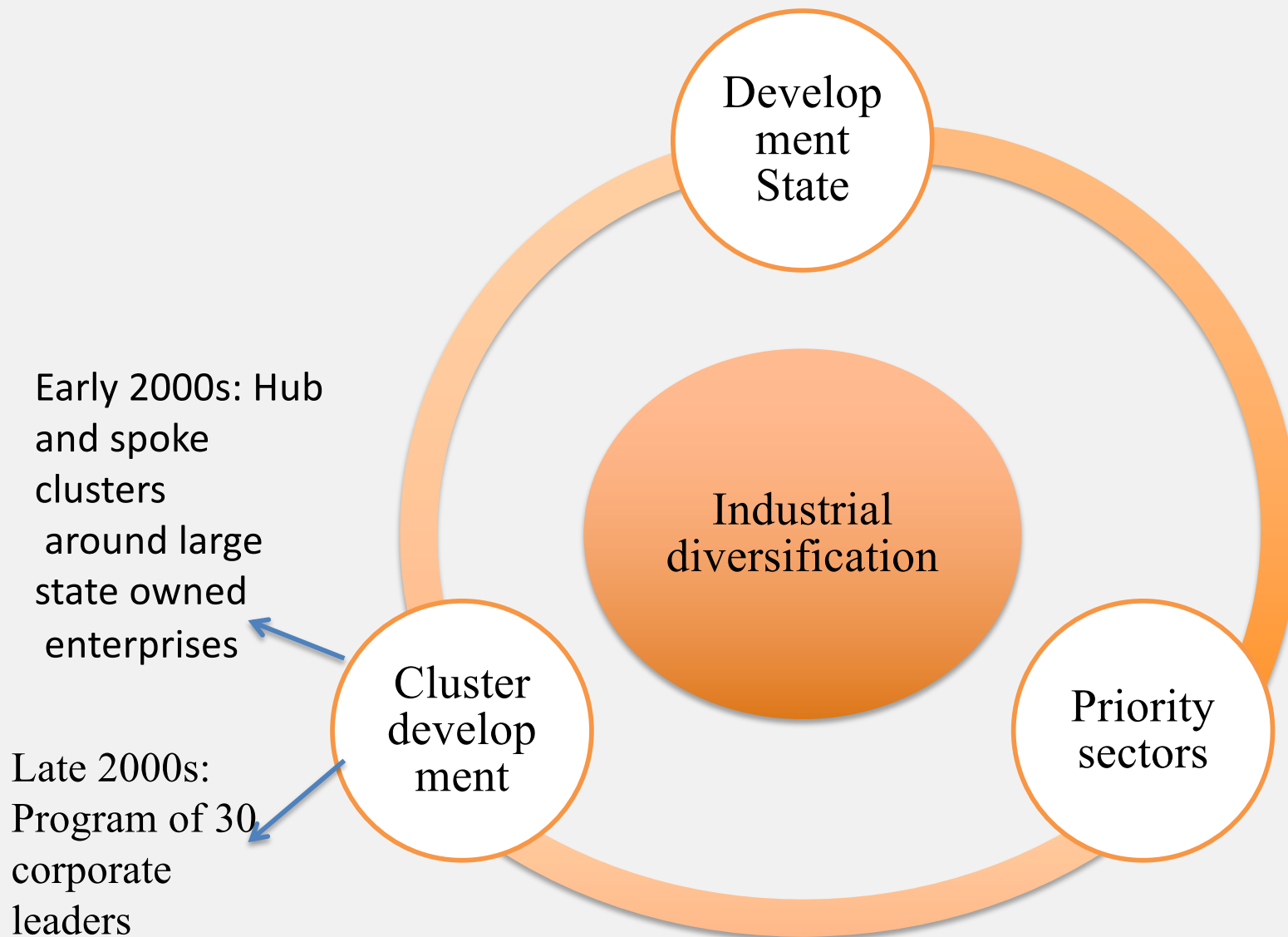
Pillar 5 : Implementing the zone strategy

Pillar 6: Establish a sound M&E framework

Pillar 1: Integrate SEZs and IZs with development strategy of industrialization

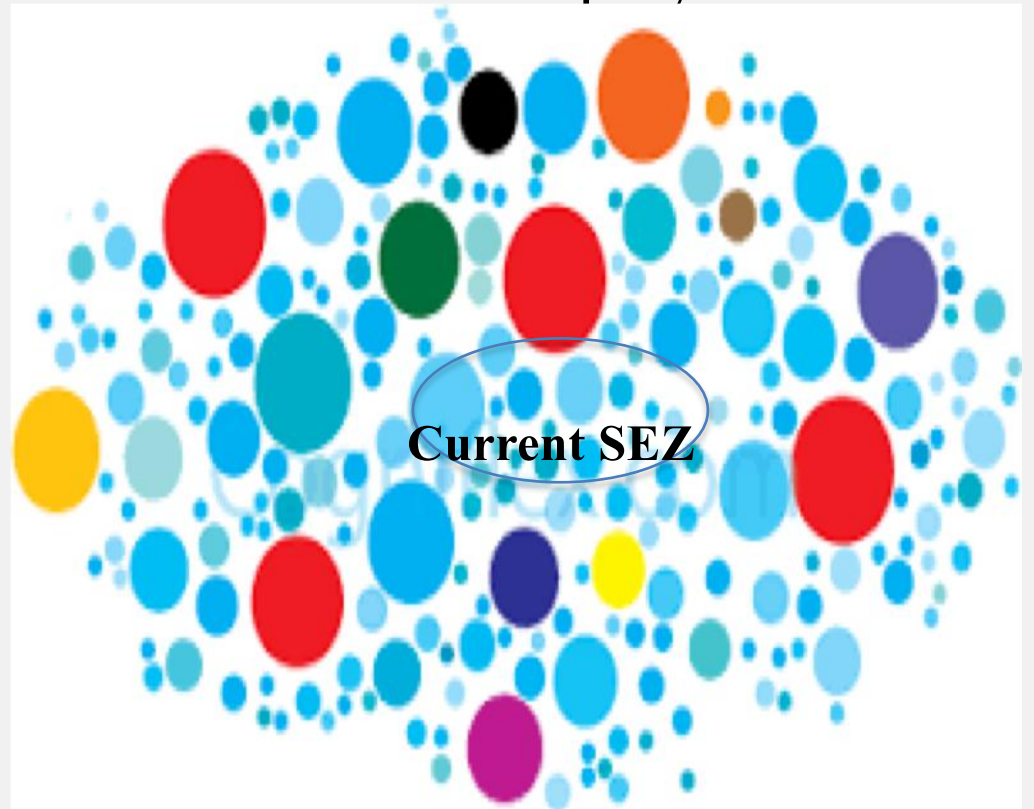
- SEZs and IZs need to be positioned within the development strategy to overcome the institutional constraints that can impede the development process.

The development strategy of Kazakhstan: The Framework



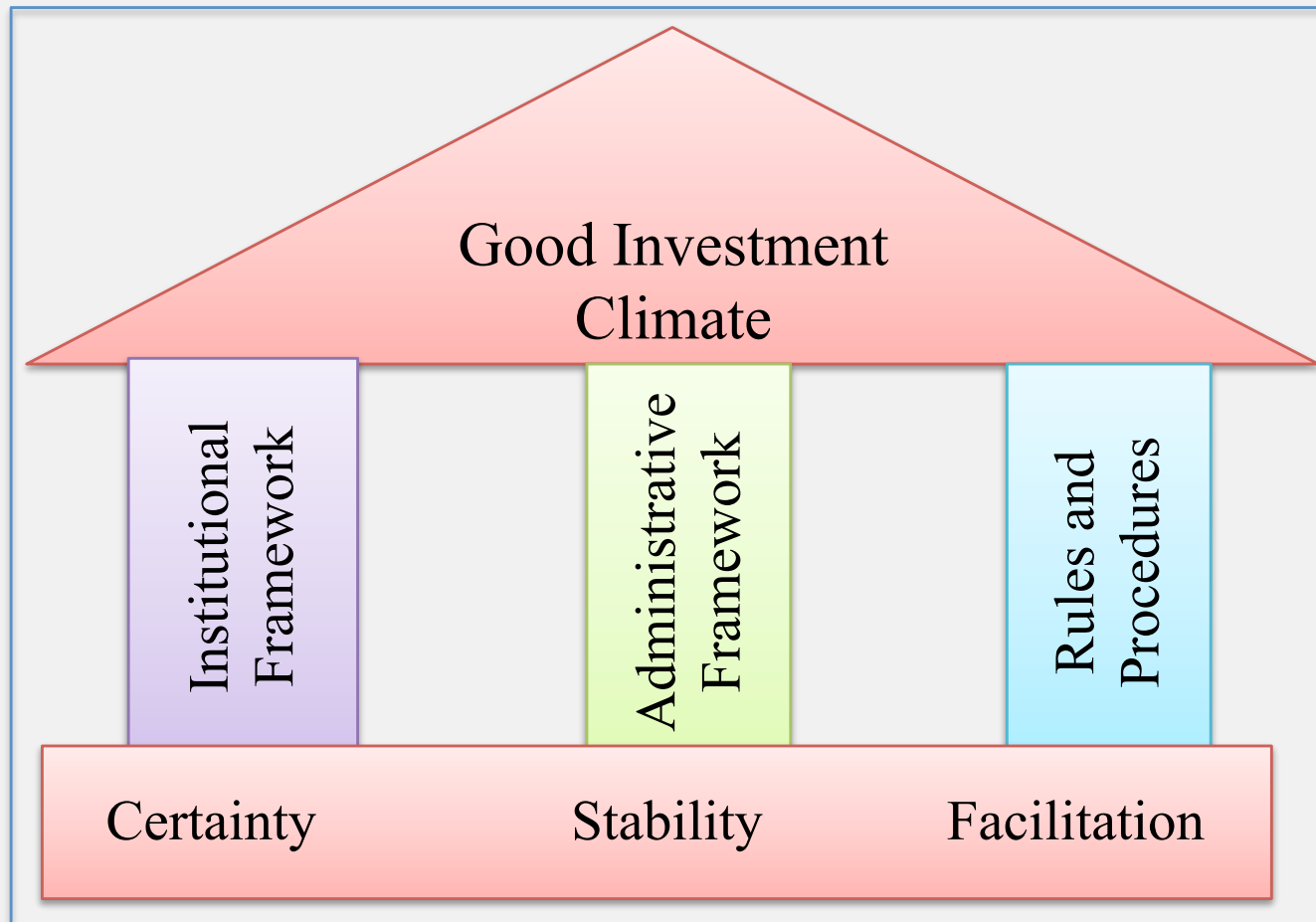
Pillar 1: Position SEZs and IZs to promote industrial clustering and insertion into GVCs

- **Transform Satellites of Economic Zones into Dynamic Clusters Rejuvenating Regional Economies**
 - Promote SEZ –centred clusters by developing hybrid zones with
 - Draw on the SEZs of Poland and China to develop hybrid economic zones with SEZs and IZs.



- **Ensure complementarity between SEZs with IZs** by promoting priority industries in IZs and light industries where Kazakhstan enjoys competitive advantages in SEZs
- **Adopt a System-based approach while defining priority industries.** In this system, sectors are defined across value chains to promote integrated industrial parks to localize value chains
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- **Target GVCs:** basic metals, electrical machinery, other transport equipment, construction, and food industries
- **Target investors**
- **Promote country specific parks**

Pillar 2: Promoting investment climate in Economic Zones : The Framework

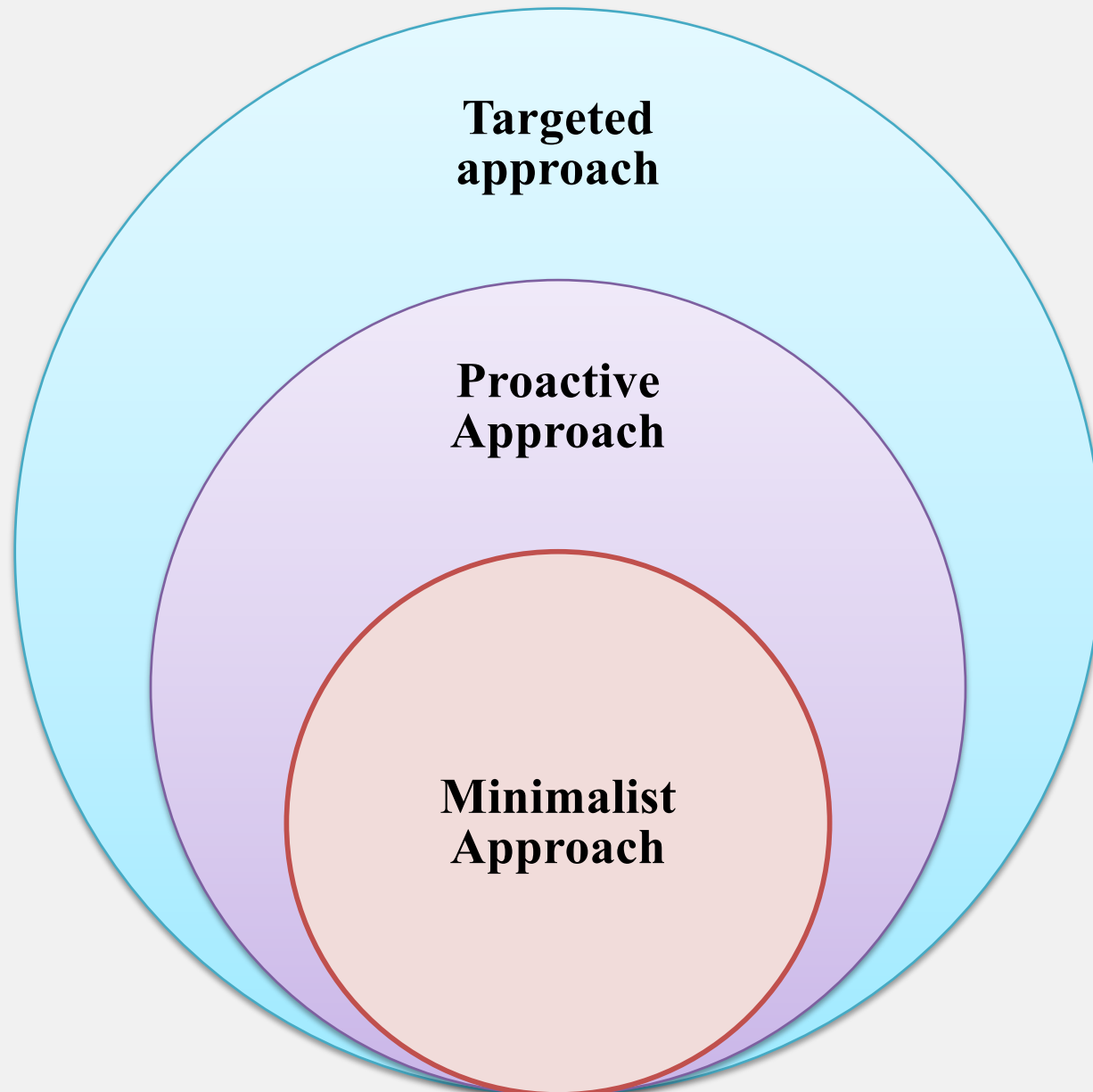


Source: Author

Action plan

- **A sound legal framework** with overriding rule or grandfather clause for certainty in rules.
- **Administrative Framework with**
 - A clear division of responsibilities between regulator, developer and managing bodies.
 - Effective regulatory body
 - Representation to private sector
- **Best international practices in**
 - One stop shop
 - Infrastructure development: Onsite, offsite, industrial, social
 - Incentives
 - Facilities
 - Labor, land, finance
 - Marketing

Pillar 3 : Promotion of spillovers from global value chain-linked investment: The Framework

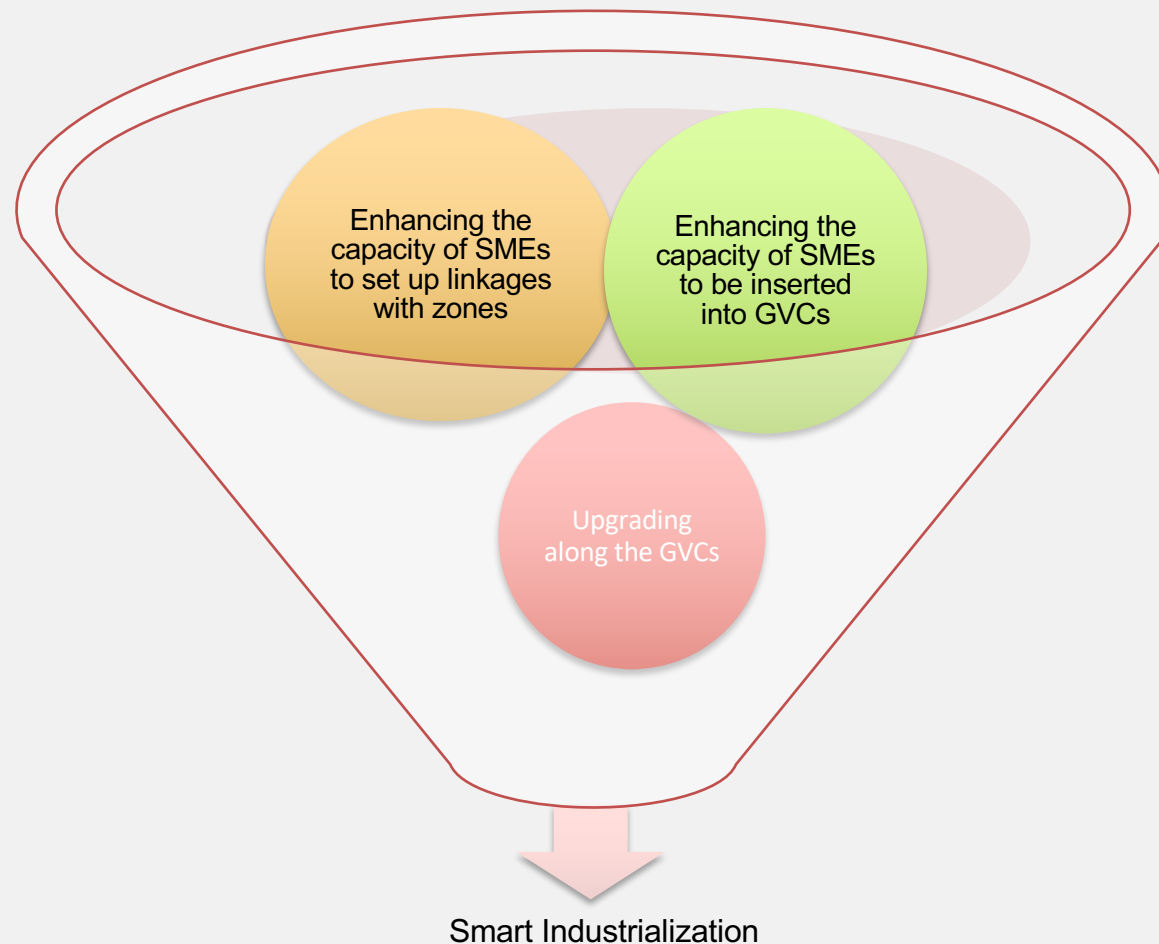


Action Plan

- *Minimalist approach*
 - Lowering Policy Barriers on transactions between SEZs and the domestic mainland
- *Proactive approach*
 - Using horizontal industrial policies to strengthen domestic capabilities alongside GVC-linked investment: Macro economic policies, improvement in business rules, human capital development, financial development, infrastructure development

- *Focused approach*

- Vertically-specialized industrialization with GVC investment at the core of industrial policy.



Pillar 4: Developing Regional Value Chains and Cross-Border Chains

- RVCs are organized at the regional, rather than the global level for consumption that may take place regionally or globally.
- **Relevance**
 - RVCs as the pathway to GVCs.
 - RVCs for decoupling of growth from that of advanced countries and promoting regional industries
 - RVCs for leveraging both RTAs and SEZs.
- **Facilitators**
 - Deep regional integration
 - Regional connectivity
 - Economic diversity with Russia as a leading goose

Strategic action plan

- **Step 1: Identify Growth Sectors**
 - Automotive sector
 - Machinery and equipment.
 - Chemical industries including petrochemicals
 - Retail chains
- **Step 2: Harmonize SEZ rules, and technical and safety standards in the region**
- **Step 3: Initiate programs and projects for SME promotion**

Managing Cross Border Value chains : Khorgos–East Gate Special Economic Zone

- **The vision (present)**
 - transform the location into a modern transport and logistics hub to be developed by Dubai Port World, and call it the ‘New Dubai’.
- **Economic benefits**
 - Specialisation in transport and logistics.
 - Promotion of cross border bazaar trade.

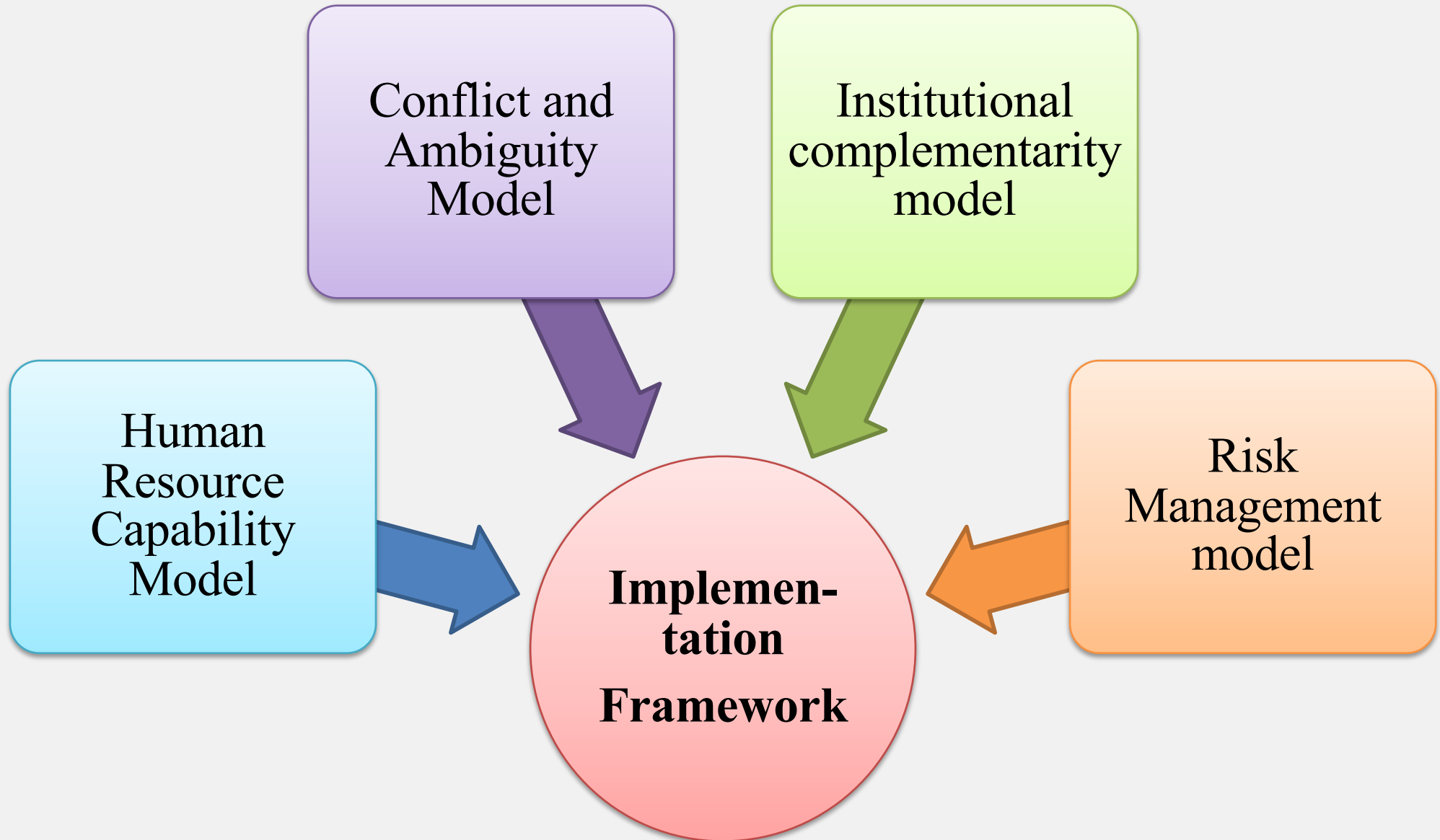
Strategic proposal: Promote cross border VCs

- Set up a hybrid zone with the expectation of attracting FDI particularly from China forming cross border value chains
- The PRC has established the 'Horgos Economic Development Zone' (HEDZ) on 30 September 2011 on the PRC side of the border.
 - It is now being positioned to become the Shenzhen of the Western PRC. It is being promoted as a prime robot manufacturing and export hub
- Kazakhstan needs to promote its side of manufacturing zone to form cross-border value chains with its PRC counterpart.

Action plan

- **Identify the possibility of cross border value chains**
 - High-tech machinery and equipments
 - Agriculture and light industries
- **High level agreements for developing regional institutions to promote the proposed border economic zone.**

Pillar 5 : Implementing the zone strategy : The Framework



ACTION PLAN

- ***Stakeholder management***

- Identify stakeholders, assess their roles and responsibilities, commitment, and resistance, .plan a communication strategy and dialogue for feedback and input, engage them in decision making and prosperity sharing, and limit the extent of change.
- Keep policy goals clear and consistent, and communicate to the implementing agencies. Too much ambiguity in the policy imposes both discretion and confusion in agencies that administer policies, leading to different interpretations by different officials, and also corruption and rent seeking.

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- ***Human resource management***

- Train implementing personnel, set up mechanisms to ensure accountability; and offer incentives.

- *Management of complementary institutions.*
 - Conduct macro-management of the economy to create an environment in which trade and investment can grow exponentially
 - Collaborations, bilateral and multilateral agreements
- *Risk management:*
 - **Macroeconomic risks:** Anticipate, assess, and manage risks in implementing the policy effectively
 - **SEZ related risks :** Adopt best practices regarding SEZ-related risks, such as fraud and money laundering, noncompliance, and change in the government attitude toward SEZs.

Pillar 6: Establish a sound M&E framework

- *Key Strategic proposals*
 - Develop a Monitoring and Evaluation Framework, including a schedule for evaluations;
 - Develop performance indicators covering the measures of inputs, processes, outputs, outcomes, and impacts of the policy.
 - For each evaluation, prepare an initial evaluation plan; identify the indicators; select an appropriate methodology; recruit and train a team to conduct the evaluation.

- *Key lessons*

- Disseminate findings to make them publicly known.
- Do not over engineer an M&E system, particularly through multiple monitoring systems or with an excessive number of performance indicators.
- Develop an action plan for follow-up; M&E is worthwhile only to the extent that it is actually used to improve government performance

Kyrgyz Republic: Another
landlocked country

Economic Challenges

- Low and highly volatile growth rate
- Consumption as the main driver of growth
- Resource curse like situation due to
 - Gold mine in particular Kumtor and other minerals
 - Remittances
 - Foreign aid

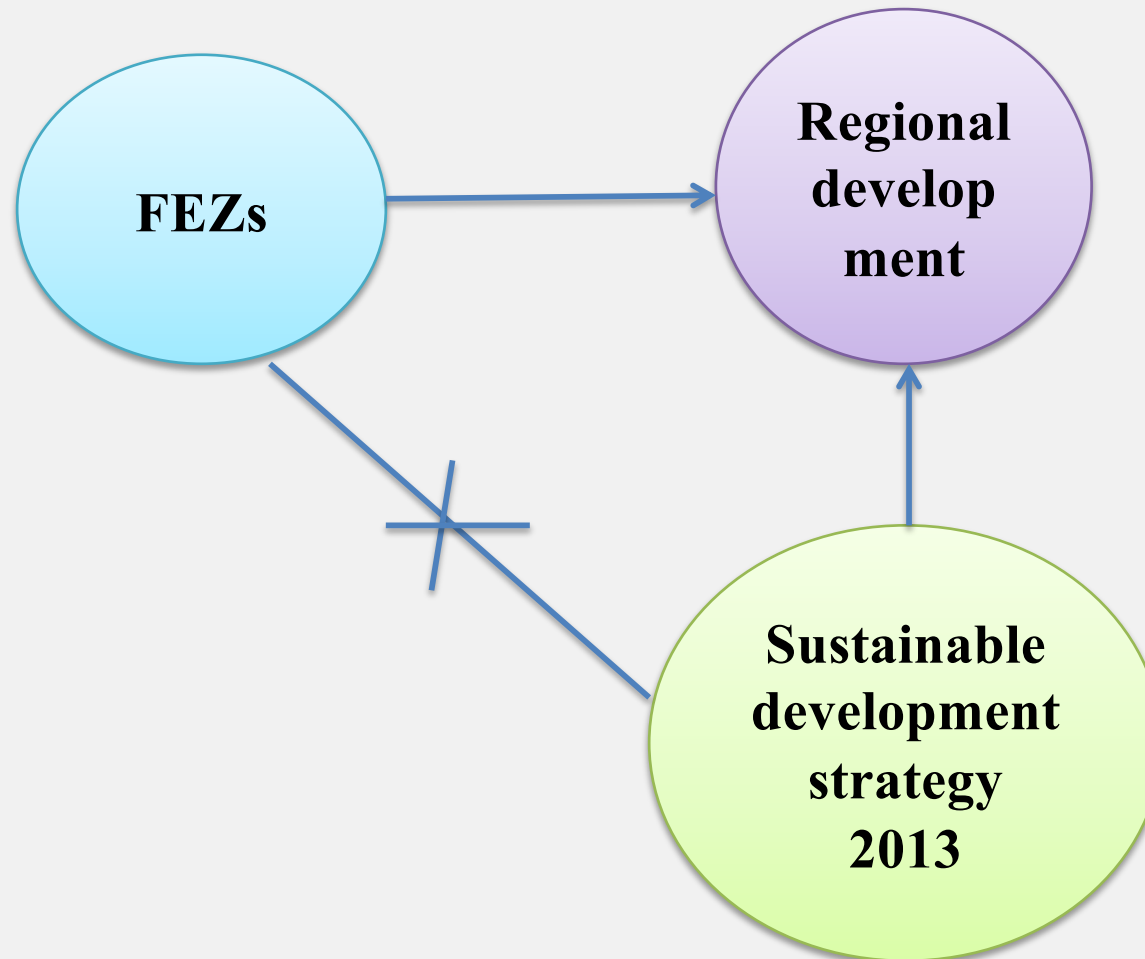
Socio political challenges

- Multi ethnicity and north-south divide
 - Internal political and socioeconomic instability, ethnic tensions, a north–south divide, rising fundamentalism, and growing criminalization of the society
- High poverty rates
 - Although the Kyrgyz Republic has been successful in reducing its rate of extreme poverty (\$1.90/day) to less than 5%, the national poverty rate based on the national poverty line was as high as 32% in 2014
- Regional inequalities:
 - Bishkek and Issy-Kul oblast increasing their share in regional GRP and widening gaps with others.
 - The gap is not confined to North-South Gap

Major policy challenge is to achieve sustainable development

- with three pillars: Economic, Social and environmental
- **This in turn requires improvement in productivity and competitiveness**
- It is critical for achieving sustainable development :
 - Rapid economic growth
 - Productive employment and hence decline in poverty rates and inequalities
 - Efficient use of resources protecting environment.

The development strategy of the Kyrgyz Republic



But limited Success of SEZs and IZs in Kyrgyz Republic

- **In addition to,**
 - **International conditions**
 - **Macroeconomic environment**
 - **Regional capabilities**
- **Major reasons**
 - Disconnect between the policy and its implementation (Unattractive SEZs)
 - Disconnect between the Development Strategy and Economic Zones
 - disconnect between the policy and the changing global trade and investment landscape. Today, where the rise of GVCs has reshaped global production and trade systems

SIX PILLARS

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The key policy messages for the Kyrgyz Republic

- FEZs and IPs should be positioned within the development strategy as an important tool of regional development and should be used to
 - insert the regional economy into GVCs
 - Create good investment climate to attract GVC linked investment.
 - Upgrade along the chains
 - Promote RVCs and cross border chains with effective implementation and monitoring
 - Learn from Laos PDR

Finally....

- SEZ and IZ success calls for
- knowledge of the necessary and sufficient conditions for SEZ-induced growth,
- belief in the strategy adopted for growth and commitment, and
- the spirit of experimentation with imaginative policymaking informed by a strategic framework

THANK YOU