

Export Processing Zone Development in Ethiopia: Law and Policy Review

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Abstract

Export processing zones [EPZs] have been used for over a century to attract investors who are interested in manufacturing and exporting. Despite long usage, the role and benefits of EPZs remain one of the most controversial areas both in practice and theory. However, the fact that countries from South East Asia and Latin America have obtained several benefits from EPZs encouraged countries such as Ethiopia to adopt them. Even though Ethiopia began its EPZs programme recently, the number of zones being built is increasing dramatically. Experience shows that the success or failure of industrial parks depends upon the host country's condition. Most sub-Saharan African countries' programmes of EPZs failed due to inappropriate domestic policies, regulatory systems and administration. The aim of this article was to scrutinize the impact, role, and status of Ethiopia's export processing zones and to investigate the factors behind the success or failure of EPZs. To investigate the status of Ethiopian EPZs, the author has investigated the legal and policy frameworks of Ethiopia. Moreover, the EPZs of successful South East Asian countries and of those African countries who failed are also consulted to learn both from the success and failure stories. Using the teleological approach of comparing the realized goals against the targeted objectives, the author of this article finds that Ethiopian EPZs are not living up to their expectations. Since various factors are responsible for their underperformance, the government is advised to take numerous policy and regulatory improvements so as to reap the aspired benefits.

Keywords: Export processing zones, Ethiopia, law, policy

Introduction

Low income countries in their efforts to come out of the poverty trap have been trying various mechanisms to stimulate their economic growth. The most important way commonly used to bring economic growth has been the

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attraction of foreign direct investment (FDI) from developed nations. Sometimes FDI is praised as the only curative drug and the only way out from the vicious circle of deep-rooted poverty for developing countries¹. The commonly agreed view in our today's world is that FDI might have both positive and negative contributions depending upon the conditions, laws and policies of the host state and the way investment flow is regulated.² Developing countries including Ethiopia continue to compete to attract FDI through various mechanisms even though both the practice and the theory showed a mixed result.

One of the commonly used mechanisms used to attract FDI is the construction of export processing zones.³ The creation of specific locations in cities in its rudimentary form to promote foreign trade had existed for many centuries⁴. The first export processing zone was believed to be established in 1896 in Manchester, England.⁵ Some scholars argued that the first modern export processing zone was the Shannon export free zone of Ireland which was established in Ireland in 1959.⁶ The initial success of this experiment led the organizations such as the United Nations Industrial Development Organization (UNIDO) to promote it as a model to be reproduced by developing countries.⁷ It goes without saying that the number of countries establishing EPZs increased dramatically within a short period of time. By 1990, the number of EPZs built worldwide reached well over 200 with total employment exceeding 2.5 million people.⁸ Sixteen years later, the number of EPZs reached well over 3,500 and the total number of

¹ Imad A. Moosa, *Foreign Direct Investment; Theory, Evidence and Practice*, Palgrave, (2002), P. 72: [Herein after Imad A Moosa, Foreign Direct Investment Theory, Evidence and Practice]

² Guangzhe Chen, Michael Geiger, Minghui Fu, Manufacturing FDI in Sub-Saharan Africa; Trends, Determinants and Impacts, World Bank group, (2015), P. 7: Theodore H. Moran, FDI and Development, A New Policy Agenda for Developing Countries and Economies in Transition, Institute for International Economics, Washington DC, (1998), P. 25

³ Jarmila Vidova, Industrial Parks, History, Their Present and Influence on Employment (2010), *Review of Economic Perspectives*, Vol. 10(1), P. 36

⁴ Sean Wulfrey, Special Economic Zones and Regional Integration in Africa, Tralac Working Paper, (2013), p. 6

⁵ Petter Gibbon, et al, An Assessment of the Impact of Export Processing Zones and an Identification of Appropriate Measures to Support Their Development, Danish Institute for International Studies, (2008), P. 13

⁶ Akbar Noman et al, *Africa, Industrial Policy, and Export Processing Zones: Lessons from Asia*, Oxford Scholarship Online, (2011), PP.2-28

⁷ Ibid.

⁸ UNCTAD, Export Processing Zones, Role of Foreign Direct Investment and Developmental Impact, United Nations Publication, (1993), pp. 6-13

workers employed in them worldwide reached 66 million according to the 2006 census.⁹ Despite the dramatic increase in the number of EPZs, the theoretical discourse as well as practical reality remains controversial.¹⁰ Despite the controversies, experience shows that there are countries which have enormously benefited from EPZs whereas others have lost much because of regulatory defects.¹¹ Hence, it is agreed that whether EPZs help the economic progress of a given state depends upon the domestic conditions of each country.¹² If we see the EPZs performance and impact in Africa, most sub-Saharan African countries began implementing EPZs development programmes only recently, except Senegal, Mauritius and Kenya.¹³ The findings from previous studies show that sub-Saharan African export processing zones have by and large underperformed, with the significant exception of Mauritius and the partial exception of Kenya and Madagascar.¹⁴ The EPZs of many African countries have been put up with lack of attention to labor and displacement issues, and poor economic management skills have made it impossible for governments to tackle the numerous challenges of providing high-quality infrastructure, government services, and human capital.¹⁵ It is on the backdrop of this understanding that the Ethiopian government spent billions of dollars for a massive EPZ construction. So far, Ethiopia has within ten years finished the construction of EPZs in Addis Ababa Bole Lemi and Kilinto, Hawassa, Dire Dawa, Mekelle, Kombolcha, Adama, Jimma, Bahir Dar, and Debe Berhan, while extra more zones are also under construction in different towns.¹⁶ Moreover, these multi-purpose zones which are specific agro-processing zones were also built in the regions of Tigray, Amhara, Oromya and Southern Nations Nationalities region. The

⁹ Ibid.

¹⁰ Keijiro Otsuka & Tetsush Sonobe, *A Cluster- Based Industrial Development Policy for Low-Income Countries*, GRIPS Policy Research Center, Tokyo Japan,(2011), p. 4

¹¹ Hye young Cho, *Industrial Park Development Strategy and Management Practices*, Korean Ministry of Knowledge and Economics, (2012), p. 4; Hyeyoung Chu tells us that Korea is the most successful country in getting benefit from EPZs. He reckons that Korea prospered because it managed to properly regulate the EPZ business and applied them in areas which are in Koreas comparative advantages. Most Sub-Saharan African countries are the looser from EPZs due to lack of proper regulation and lack of political will and commitment.

¹² Bayisa Tesfaye, *Prospects and Challenges of Industrial Zones Development*, ACJTB,(2016), 2(1), PP. 1-64

¹³ Zeng, *Global Experience with Special Economic Zones, with a Focus on China and Africa*, The World Bank Trade and Competitiveness Global Practice, Conference Paper,(2015), p. 7

¹⁴ Ibid.

¹⁵ Ibid.

¹⁶ Ethiopian Industrial Parks Development Corporation website (June,2015) ; Available at; <http://www.ipdc.gov.et/images/downloads/New/IPDCBrouchure.pdf> last accessed on 08/01/2020

government has the plan to add 13 more agro-processing zones.¹⁷ Just like any developing country, the government of Ethiopia aspires to reap the benefits of export diversification, foreign currency earning, employment creation, economic growth, forward and backward linkage and technology spillovers and transformation of the economy from EPZs expansion.¹⁸ However, even though EPZs' transformational role in Ethiopia's industrialization process is believed to be enormous, efficient and feasible policies and institutional arrangements are yet to be developed in the Ethiopian regulatory system. Moreover, the Ethiopian EPZ development program suffers from lack of comprehensive regulatory framework (such as the absence of comprehensive legal, policy and organizational frameworks).¹⁹ Some scholars argue that it is too early to say that the EPZs are successful or unsuccessful until they serve 5 to 10 years.²⁰ Nevertheless, the initial conditions seen within the first five years can give us sufficient information to predict their fate in the near future. The early result of Ethiopian EPZs that has been observed within the past five years of EPZs revolution time shows us that Ethiopia is not in the right track regarding its EPZs development programmes since the aspired advantages are not materializing despite nearly a decade is over since the EPZs development programme. Furthermore, the success of EPZs is not solely dependent on factors relating to EPZs, rather there are additional factors which might determine the failure or success of EPZs, such as ease of doing business, absence of risks, political stability which includes sound macroeconomic and exchange rate policies and so on.²¹

This article is divided into six sections. While the first section is devoted to the general concept and definition of EPZs, the second section tries to address the theoretical perspectives on the impacts of EPZs. The third section covers the status of EPZs in sub-Saharan Africa. The fourth section

¹⁷ UNIDO, Integrated Agro-Industrial Parks in Ethiopia, (2018), p. 11 available at <https://www.unido.org/sites/default/files/files/2018-08/Integrated-Agro-Industrial-Parks-in-Ethiopia-Overview-document.pdf> last accessed on 08/01/2020

¹⁸ Federal Plan Commission, Ethiopian Growth and Transformation Plan II, (2017),p. 138 see also Industrial Parks Development Corporation Website available at: <http://www.ipdc.gov.et/images/downloads/New/IPDCBrouchure.pdf>

¹⁹ Bayisa Tesfaye, Prospects and Challenges of Industrial Zones Development, *supra* note 12 pp. 1-64

²⁰ Farole Thomas, Export Processing Zones of Sub Saharan Africa, Learning from the Global Experience, World Bank Publisher, (2011), p. 161

²¹ Dorsati Madani, A Review of The Role and Impact of Export Processing Zones, World Bank, (1999), p. 52

of the article is devoted to models of success or failure of EPZs. The fifth and the sixth sections of this article deal with the status of EPZ in Ethiopia and the policy and legal recommendation for their success.

1. Concept and Definitions of Export Processing Zones

EPZ refers to a geographically limited and specially administered area within a country that is established to attract local investment and FDI, trade, employment and industrial development.²² They refer to the land well prepared for industries based on the comprehensive plans.²³ EPZs are also defined as geographically delimited areas, commonly physically secured, that are usually, outside the customs territory of the host country.²⁴

Different countries have been using diverse names to refer to EPZs, and analysts have varying definitions of what constitutes an EPZ.²⁵ Some of the lists of terms include, “Export Free Zone” in Ireland, “Maquiladora” in Mexico, “Duty Free Export Processing Zone” and “Free Export Zone” in South Korea, “Export Processing Zone” in the Philippines, “Special Economic Zone” in China, “Industrial Parks” in Ethiopia, “Foreign Trade Zone” in India and “Free Zone” in the United Arab Emirates.²⁶ World Bank defines them as geographically defined places within a country offering a free trade environment, a liberal regulatory regime, and/or tax and other incentives oriented to attracting FDI and with an expectation that firms operating within it focus on export oriented manufacturing.²⁷ UNIDO defines EPZs as:

A tract of land developed and subdivided into plots according to a comprehensive plan with or without built-up (advance)

²² UNCTAD, Enhancing the Contribution of Export Processing Zones to the Sustainable Development Goals, United Nations, New York Geneva, (2015), p. 3

²³ Hyeyoung Cho, Industrial Park Development Strategy and Management Practices, *supra* note at 11, P.28

²⁴ *Ibid.*

²⁵ Jessie Adala, A Case Study of the Performance of Export Processing Zones Garment Firms in Mauritius and Kenya in the Dawn of Agoa Phase IV, Unpublished Theses, (2008), P.13

²⁶ Engman, M., Onodera, O. & Pinali, E., Export Processing Zones: Past and Future Role in Trade and Development. OECD Trade Policy Working Paper, (2007), P. 53.

²⁷ World Bank, EPZs, Washington, D.C, World Bank Industry and Development Division, (1992), P.

*factories, sometimes with common facilities and sometimes without them, for the use of a group of industrialist.*²⁸

The requirements needed to qualify as export processing zones include prior master planning, follow-up management through management organizations and facilities supporting production of resident enterprises.²⁹

The Ethiopian industrial park proclamation used a term “Industrial Park” instead of EPZs and defined it as:

*An area with distinct boundary designated by the appropriate organ to develop comprehensive, integrated, multiple or selected functions of industries, based on a planned fulfillment of infrastructure and various services such as road, electric power and water, one stop shop and have special incentive schemes, with a broad view to achieving planned and systematic development of industries, mitigation of impacts of pollution on environment and human beings and development of urban centers, and includes special economic zones, technology parks, export processing zones, agro-processing zone, free trade zones and the like designated by the Investment Board;*³⁰

Based on this definition the term Industrial Park is used as a generic term that represents all the kinds of industrial estates with various degrees and kinds. Here, in the definition, EPZs are listed as one type of industrial parks among many. Nevertheless, the proclamation failed to define and explain the similarity, difference and purposes of the various industrial estates it listed.

For Nicolas Papadopoulos and Shavin Malhotra, Special Economic Zones [SEZ], and EPZs are similar since they focus on manufacturing for export whereas the difference between the two is that EPZs are geographically

²⁸ UNIDO, Industrial Estates Principles and Practice. Technical Report. United Nations Industrial Development Organization, (1997), P.8 also available at: <https://www.unido.org/resources/publications/flagship-publications/industrial-development-report-series> last accessed on 23/08/2019

²⁹ Imad A. Moosa, Foreign Direct Investment, Theory, Evidence and Practice, *supra* note 1, P. 72

³⁰ Industrial Parks Proclamation, (2015), Art.2 (1), Proc.No.886/2015, Fed. Neg. Gaz., year 21,no.39

restricted, and often fenced-in, enclave, whereas SEZs cover a large area extending to the territory of an entire city, province, or region.³¹

In the same fashion, UNIDO holds that EPZs can come in a variety of forms such as industrial zones, industrial estates, cities and districts; technology or innovation areas; science parks or cities; cyber parks; high-tech (industrial) parks; research and technology parks; science and technology parks; technology incubators; and eco-industrial parks.³² These different forms can be situated in special economic zones, export processing zones and free trade zones, which can also be a part of a larger geographic and economic area, involving multiple countries along the transport corridors and forming the industrial and economic corridors.³³ Douglas Zhihua puts the various nomenclatures of EPZs as follows:

Table 1. Common types of EPZs

<i>Name</i>	<i>Meaning</i>
<i>Free Trade Zones</i>	Are fenced-in, duty-free areas, offering warehousing, storage, and distribution facilities for trade, transshipment, and re-export operations.
<i>Export Processing Zones</i>	Are industrial estates aimed primarily at foreign markets. They offer firms free-trade conditions and a liberal regulatory environment. There are in general two types of EPZs: one is a comprehensive type, open to all industries; another is a specialized type, only open for certain specialized sectors/products.
<i>Comprehensive Special Economic Zones</i>	Are zones of a large size that are a mix of different industrial service and urban-amenity operations. In some cases these zones can encompass a whole city or jurisdiction, such as Shenzhen (city) and Hainan (province) in China.
<i>Industrial Parks</i>	Bonded Areas (also known as “Bonded Warehouses”) are specific buildings or other secured areas in which goods may be stored, manipulated, or may undergo manufacturing operations without payment of duties that would ordinarily be imposed. To some extent, a “bonded area” is similar to a “free trade zone” or “free port.” However, the major difference is that a “bonded area” is subject to customs laws and regulations, while a “free trade zone” is exempt from these provisions.

³¹ Nicolas Papadopoulos and Shavin Malhotra, *The Role of Export Processing Zones in Development and International Marketing Strategy*, Carleton University, (2005) P.3 available at; <https://journals.sagepub.com/doi/10.1177/0276146707300070> last accessed on 23/08/2019

³² Olga Memedovich UNIDO, *Leveraging a New Generation of Industrial Parks and Zones for Inclusive and Sustainable Development*, Vienna, (2018), P. 1

³³ *Ibid.*

Specialized Zones	Specialized Zones include science/technology parks, petrochemical zones, logistics parks and airport-based zones.
Eco-Industrial Zones or Parks	Eco-industrial zones or parks focus on ecological improvements in terms of reducing waste and improving the environmental performance of firms. They often use an “Industrial symbiosis” concept and green technologies to achieve energy and resource efficiency. Due to environmental challenges, increasing number of countries are embracing this new type of zone.

Source: Zeng (2012)

Although different nomenclatures are used in different countries with some variation in purpose and size, there are similar elements shared by these entities. Broadly, four characteristics describe the concepts of EPZs in various names: (1) they are geographically delineated area, usually physically secured; (2) they have single management or administration; (3) they offer benefits for investors physically within the zone; and (4) they have a separate customs area (duty-free benefits) and streamlined procedures.³⁴

Terms such as Industrial Parks, Export Processing Zones (EPZ), Free Trade Zones (FTZ), Special Economic Zones (SEZ) and Export Processing Factories (EPF) refer to similar concepts with variations determined by policy prescriptions and objectives.³⁵ Given the fact that the phrase “EPZ” is the most commonly used terminology in most countries and in the literature, the author of this article uses EPZ for the purpose of this article to represent other nomenclatures. EPZs are entities or estates which allow for the creation of an 'enclave', isolated from the domestic economy, within which export-oriented manufacturing activities can freely operate without state intervention.³⁶ Hence, EPZ shall be used to refer to any fenced-in industrial entities in different variants and naming typically established with the aim of achieving one or more of the policy objectives of attracting foreign direct investment and promoting exports and industrialization; serving as “pressure valves” to create large-scale employment opportunity; increasing the foreign currency reserves to support a wider economic reform strategy; and acting as experimental laboratories for the application of new policies and

³⁴ FIAS. Special Economic Zones: Performance, Lessons Learned, and Implications for Zone Development.” Washington, DC: World Bank,(2008), P.13

³⁵ Madani, D., A Review of the Role and Impact of Export Processing Zones, The World Bank, (1999), P. 12: Available at; ([http:// www.worldbank.org](http://www.worldbank.org).)

³⁶ Kankesu Jayanthakumaran, An Overview of Export Processing Zones: Selected Asian Countries, Bangkok, Thailand, (2002), P. 13

approaches.³⁷ The common benefits provided in EPZs include preferential tax or duty treatment or exemptions from restrictions on the repatriation of profits, direct financial subsidies and improved physical infrastructure as well as expedited permission and related services.³⁸

2. Theoretical Perspectives on the Impact of Export Processing Zones

Export processing zones are as popular as they are controversial.³⁹ The experience with EPZs shows a mixed picture. There has been a lot of intense polarized argument over the years as to the significance of EPZs as a policy instrument.⁴⁰ Most traditional economic analysis, including major analytical tools from the World Bank, view zones as a second-best policy, preferring economy-wide liberalization. The World Bank and several economists have expressed their worry about the possible distortion effects that zones bring because of subsidies and by allowing countries to delay general liberalization of the economy as a whole.⁴¹ However, other researchers have noted the dynamic, long-run economic impacts of successful zone programs.⁴² The extraordinary success stories in South East Asia coupled with serious disappointments in sub-Saharan Africa have intensified the debate on the rationale and justification for using EPZs as an instrument for economic development.⁴³ The gain that they could bring is a subject of much debate. For many, EPZs are a contrivance to develop a more general form of industrial organization through the creation of industrial “clusters”, i.e. a concentration of interconnected firms in a particular field of activity. The

³⁷ Douglas Zhihua Zeng, *Special Economic Zones: Lessons From the Global Experience*, Center for Economic Policy Research, PEDL Synthesis Series, (2010), p.3 available at: https://assets.publishing.service.gov.uk/media/586f9727e5274a130700012d/PEDL_Synthesis_Paper_Piece_No_1.pdf last accessed on 23/08/2019

³⁸ UNCTAD, *Enhancing the Contribution of Export Processing Zones to the Sustainable Development Goals*, United Nations, (2015), P. 3

³⁹ Yannick Saleman and Luke Simon Jordan, *The Implementation of Industrial parks; Some Lessons Learned in India*, World Bank, Washington, DC, (2013) P.99[Here in after Y. Saleman & L.S.Jordan *The Implementation of Industrial Parks; Some Lessons Learned in India*]

⁴⁰ Farole, Thomas, *Special Economic Zones in Africa, Comparing Performances and Learning from Global experience*,(2011), p.8 [Here in After Farole *Special Economic Zones in Africa, Comparing Performances and Learning from Global Experience*]

⁴¹ Farole, Thomas; Moberg, Lotta, *It Worked in China, So Why Not in Africa? The Political Economy Challenge of Special Economic Zones*, Working Paper, No. 2014/152, ISBN 978-92-9230-873-5, WIDER, Helsinki (2014),p. 2,

⁴² Vastveit, *Export Processing Zones in Sub-Saharan Africa – Kenya and Lesotho*, unpublished, (2013),P. 9 [Herein after Vastveit, *Export Processing Zones in Sub-Saharan Africa – Kenya and Lesotho*,]

⁴³ Douglas Zhihua Zeng, *Special Economic Zones, Lessons From the Global Experience*, Center for Economic Policy Research, (2011), P. 4

concentration of EPZs had been justified by two reasons. The first justification is easiness in providing infrastructure for a geographically limited space.⁴⁴ The second rationale is the concentration of firms within a certain space can generate considerable spillover effects both inside and outside the zones.⁴⁵ EPZs are praised to improve and diversify exports, create employment opportunity and increase foreign exchange earnings by attracting foreign capital, yield positive externalities such as technology and knowledge spillovers that may contribute to improving the host countries' competitiveness, establish links to global value chains through participating in international competition, and making full use of comparative advantages to promote the upgrading of industrial structure and persistently improve the country's position in the international division of labor.⁴⁶

The theory for the development of EPZs hinges on the premise that governments must provide public goods such as infrastructure so as to make firms competitive.⁴⁷ If the firms are not there yet, the provision of infrastructure will encourage them to choose the parks. If the zones are built, but the general economic environment is difficult to do business, exemptions and incentives should be made to further attract firms and create competitiveness.⁴⁸

One of the benefits said to be reaped from EPZs is agglomeration economic effects which could result from hub development around city centers and transportation centers.⁴⁹ According to Carol Newman and John Page, agglomeration economies are the firm-level productivity gains that result from spatial concentration of economic activity.⁵⁰ Marshall points out that there are three main justifications why firms should be situated closer to each other; namely, to reduce cost of transportation, to pool relevant workers

⁴⁴ Marshall, A., *Principles of Economics*. London: Macmillan, (1920), p. 2

⁴⁵ Sonobe, Tetushi, & Otsuka, K., *Cluster-Based Industrial Development: An East Asian Model*, Palgrave, Macmillan, (2006), p 3

⁴⁶ Vastveit, *Export Processing Zones in Sub-Sahara Africa Lesotho and Kenya*, *supra* note at 42,P. 2: See also Ziaodi Zhang et al, *Industrial Park Development in Ethiopia, Case Study Development*, UNIDO,(2018), p.2

⁴⁷ Y. Saleman & L.S.Jordan, *The Implementation of Industrial Parks; Some Lessons Learned in India*, *supra* note.39 P. 1

⁴⁸ *Ibid.*

⁴⁹ *Ibid.*

⁵⁰ Carol Newman and John Page, *Industrial Clusters, The Case for Special Economic Zones in Africa*, UNU-WIDER, (2017), p. 2

in areas where there is high employment and to exchange knowledge spillovers among firms, which could be high.⁵¹

Nevertheless, EPZ development policies are strongly criticized for the large scale land grabs and speculation issues particularly if the parks built remain vacant or little occupied by investors for long periods of time, for the huge government money spent for the construction of parks, for the loss of revenue from the exemption policy to the parks, and for the insufficiency of wages paid for labor.⁵²

There have been strong opposition and criticisms against the issues of large tracts of land allocated for their construction, particularly when zones are long delayed or not occupied, which may imply land speculation. It has also proven difficult to demonstrate additionality, i.e. the activities in zones would not have happened without their construction and the public money that has been spent to support it.⁵³ The disappointment with EPZs becomes stronger against policies that not only provide public money for zone construction but forego revenues in the forms of taxes or resort to specific regulations such as lax environmental laws. Although those zones can create jobs, promote investment, and catalyze regional development, they could be the sources of labor abuse, limited social and economic upgrading, low levels of investment, and excessive establishment costs.⁵⁴ Labor activists campaigned against restrictions on freedom of association, collective bargaining, and other basic rights in EPZs. Farmers who are dispossessed their lands due to EPZ expansion without appropriate compensation protest frequently.⁵⁵

⁵¹ Marshall, A., *Principles of Economics*, *supra* note, 44 p. 3

⁵² Peter Gibbon, *An Assessment of the Impact of Export Processing Zones and an Identification of Appropriate Measures to Support their Development*, Danish Institute for International Studies, (2008), p. 11 [Herein after *An Assessment of the Impact of Export Processing Zones and an Identification of Appropriate Measures to Support Their Development*]

⁵³ Mester Liana-Eugenia, Bugnar Nicoleta-Georgeta: *The Role of Industrial Parks in Economic Development*, *Annals of Faculty of Economics, University of Oradea*, Vol. 1 no.1, (2013), pp.123-130,

⁵⁴ Nel, Etienne L. and Christian M. Rogerson. , *Special Economic Zones in South Africa: Reflections from International Debates*. *Urban Forum*, (2013), Vol. 24: no. 2 pp. 205–217

⁵⁵ Peter Gibbon, *An assessment of the Impact of Export Processing Zones and an Identification of Appropriate Measures to Support their Development*, *Supra* note 52, P. 11

Nonetheless, successfully managed EPZs will continue to play an important role in increasing competitiveness.⁵⁶ Carefully planned EPZs could provide an environment conducive to the growth of foreign investment, generate employment opportunities, foreign exchange, backward, forward and demand linkages, self-generating capital accumulation, training and technological spillovers and significant local spin-offs and co-ownership opportunities.⁵⁷ The notable examples who have benefited from the development of EPZs are the East Asian Tigers or alternatively known as the Newly Industrialized Nations such as the Republic of Korea, Hong Kong, Singapore, China and Taiwan.⁵⁸ These countries have achieved a remarkable success from EPZs programs by reaping the full benefits from the zones such as employment creation, export diversification, backward linkages, foreign currency earnings, and overall economic growth of the countries.⁵⁹

Those EPZs which are not appropriately planned and managed, however, may not yield the aspired benefits. Many EPZs operate in an unsustainable way due to the social and environmental problems caused by poor management.⁶⁰ It is not the presence of EPZs or a sufficient infrastructure that makes the difference in attracting FDI, icreating jobs, and generating spillovers to the host country. Rather, it is the relevance of the EPZ programs in the specific context in which they are introduced, and the effectiveness with which they are designed, implemented, and managed on an ongoing basis, that will determine success.⁶¹ EPZs, under current conditions, may well be effective only if there is a generally helpful macroeconomic and business atmosphere in place and the expected impacts from EPZs as such are diminishing from time to time.⁶² The world's most successful zones have been established in East Asian countries and their achievements have not

⁵⁶ Thomas Farole and Gokhan Akinici, *Special Economic Zones: Progress, Emerging Challenges and Future Directions*; the International Bank for Reconstruction and Development 1818 H street NW Washington DC, (2011), P. 8

⁵⁷ Howard Stein, *Industrial Policy and Export Processing Zones, Lessons from Asia*, University of Michigan, Paper Presented in Addis Ababa for Africa Task Force Meeting, Unpublished, (2008), P. 4

⁵⁸ Guangzhe Chen, Michael Geiger, Minghui Fu, *Manufacturing FDI in Sub Saharan Africa; Trends, Determinants and Impacts*, World Bank group, (2015), P. 1

⁵⁹ *Ibid.*

⁶⁰ *Ibid.*

⁶¹ *Ibid.*

⁶² *Ibid.*

been uniformly replicated in the developing world's less prosperous environs, particularly in countries with small markets.⁶³

3. Models of Evaluating the Success or Failure of Export Processing Zones

Some people argue that EPZs have a propensity to attract FDI and larger domestic investors mainly in the short term; they are not a direct cause of development of local small and medium enterprises. While certain zones have demonstrated more positive long-run economic impacts, many neoclassical and neoliberal thinkers and institutions criticized EPZs for hampering nation-wide economic liberalization.⁶⁴ The argument by neoclassical theorists holds that EPZs cannot encourage domestic investment since they provide lower return than the protected segment of the economy.⁶⁵ They also contend that EPZs create distortions and are welfare-reducing since the inflow of capital into the zones will attract labor from labor-intensive sectors of production to comparatively more capital-intensive sectors in the zones.⁶⁶ Investments in zone infrastructure have in many cases resulted in 'white elephants,' which cost more to maintain than the benefits that they bring, or zones where investors take advantage of tax breaks without delivering substantial employment or export earnings.⁶⁷ Many of the traditional EPZs seem at the outset successful in attracting investment and generating employment opportunity in the short term, but fail to sustain competitiveness in the face of rising wages or erode trade preferences.⁶⁸ Nevertheless, Johansson strongly criticizes the neoclassical theory of failing to consider the spillovers from foreign direct investments within EPZs, and advocates new growth theory. According to him the enclave nature of EPZs and the low-skilled production process do not

⁶³ Ibid.

⁶⁴ Farole, Thomas; Moberg, Lotta, It Worked in China, So Why Not In Africa? The political Economy Challenge of Special Economic Zones, *supra* note at 41, p. 13

⁶⁵ Hamada, K., "An Economic Analysis of the Duty Free Zone," *Journal of International Economics*, (1974), 4 (3), P. 231

⁶⁶ Ibid.

⁶⁷ Farole Thomas and Lotta Moberg, It worked in China, So Why Not in Africa? The political Economy Challenge of Special Economic Zones, *supra* note at 64, P. 8

⁶⁸ Ibid.

promote technology transfers and associated externalities to the outside society.⁶⁹

Among the various models used to evaluate the success or failure of EPZs, two of them are famous, i.e. cost-benefit approach (which tries to compare the situation with the zone to the hypothetical situation without it, but under an alternative set of industrial policies) and teleological analysis of comparing the actual results of EPZs with the goals or objectives set.⁷⁰ Warr (1989) and Jayanthakumaran (2003) are well-known for their cost-benefit analysis of EPZs based on several case studies in South East Asia. Their research has shown that industrial park development programs bring net positive contribution to economic welfare of the country.⁷¹ However, their models are criticized for generalizing from few selected EPZ. According to critiques, the conclusions of Warr are made only based on a case study made on few successful EPZs of South East Asia, which cannot represent EPZs of other countries.⁷² The second model of evaluating the success of EPZs is by cross-checking the aspired goals against the actual achievements. This approach forms a way of developing well-written targets and their respective performance indicators that show a clear picture of the results expected from the EPZ programme activities.⁷³

4. The Status of Export Processing Zones in sub-Saharan Africa

When compared to South East Asian countries, most African nations are latecomers to the concept of export processing zone. The earliest countries which embarked on establishing EPZs development programmes with the sole purpose of exporting commodities were Liberia in 1970, Mauritius in 1971 and Senegal in 1974 in an attempt to replicate the success of the Asian

⁶⁹ Johansson, H. 'The Economics of Export Processing Zones Revisited', *Journal of Development Policy Review*, Vol. 12(4), (1994), P. 395

⁷⁰ Jose Daniel Amado, *Free Industrial Zones: Law and Industrial Development In The New International Division of Labour*, *University of Pennsylvania Journal of International Law*, (1989), Vol.11(1), P. 136

⁷¹ Jayanthakumaran, K, *Benefit-Cost Appraisals of Export Processing Zones: A Survey of The Literature*. *Development Policy Review*, (2003), Vol.21(1), P. 58: See also Warr, P. G., *Export Processing Zones: The Economics of Enclave Manufacturing*. *The World Bank Research Observer*, 4(1), (1989), P. 72.

⁷² Farole Thomas, *Special Economic Zones in Africa: Comparing Performance and Learning from Global Experience*, *supra* note at 40, p.12

⁷³ Charles Dominican, *An Evaluation of Tanzania's EPZ Program—Challenges and Prospects*, conference paper, (2009), p. 32

countries of the 1960s and 1970s.⁷⁴ Most of the EPZ development programmes began only in the late 1990s or early 2000s, in response to the US Africa Growth and Opportunities Act (AGOA) and the Multi-Fiber Arrangement (MFA). Most comprehensive studies conducted on the effect of EPZ in sub-Saharan Africa revealed that these programmes have largely failed in view of small static benefits such as employment, investment, and export figures and dynamic impacts like structural transformation and economic development. By 2008, the number of zones built in Africa reached 114.⁷⁵ In fact, those zones were largely different from the modern large scale multiuse zones that are currently being proposed.⁷⁶ So far, Africa's EPZs have played a negligible role in both the static and dynamic contribution to growth and development. When assessed using a number of success indicators, EPZs in Africa have been largely unsatisfactory as compared to the experiences of many South East Asian countries.⁷⁷ Many observers agreed that except for few countries, EPZs have brought insignificant impact on economic growth of host states, have created little jobs, are footloose companies with poor quality of jobs, have attracted little foreign direct investment, lacked backward linkages with domestic industries, and brought limited foreign exchange earnings.⁷⁸ Senegal and Kenya are the best examples whose zones were left empty after being constructed at the cost of more than a billion dollars.⁷⁹

A lot of factors are responsible for the underperformance of African EPZs, including problematic legal, regulatory and institutional frameworks, poor business environment and high cost of doing business, lack of strategic planning and a failure to adopt a demand-driven approach, lack of policy consistency, and a failure of host governments to maintain commitments to

⁷⁴ African Development Bank Group, Special Economic Zones in Fragile Situations, A Useful Policy Tool?, AFDB Publisher, (2015), P.13, available at: file:///C:/Users/user/Desktop/SEZ_anglais_SEZ_anglais.pdf

⁷⁵ Farole Thomas, Special Economic Zones in Africa: Comparing Performance and Learning from Global Experience, *supra* note 40, P. 11

⁷⁶ *Ibid.*

⁷⁷ Howard Stein, Industrial Policy and Export Processing Zones, Lessons from Asia, *supra* note at 57, P. 14

⁷⁸ *Ibid.*, See also Farole, Special Economic Zones Performance, Comparing Performance and Learning from Global Experience, *supra* note 26, P. 8

⁷⁹ *Ibid.*

zones, lack of infrastructure, weak planning and management and lack of administrative commitment.⁸⁰

5. Export Processing Zones of Ethiopia

Ethiopia, though very late and newcomer to EPZs, is rushing towards revolutionarizing her EPZs development. The government has been taking economic policy reforms since 1991. The first reform measure was the structural adjustment program which was followed by the formulation of a full-fledged industrial strategy of the 2003 known as Agricultural Development Led Industrialization programme. Since then the government of Ethiopia has been adopting and implementing four five-year successive national plans, namely the Sustainable Development and Poverty Reduction Program (2002-2005), the Plan for Accelerated and Sustained Development to End Poverty (2005-2010), the GTP I (2010-2015) and GTP II (2015-2020). The objective of GTP I and II is to transform Ethiopia into a middle-income country by 2025 and one of the key pillars to reach the target is the development of light manufacturing industries.⁸¹ The main strategy devised by the GTP I and II is to make Ethiopia African hub of light manufacturing industries with the help of EPZs and clusters in the different parts of the country.⁸²

In the last five years alone, Ethiopia has got ten government built zones and three major foreigner private owned zones. Moreover, the construction of at least ten EPZs is underway throughout the country. While some of them are nearing completion, some are at their initial stages. The government of Ethiopia has been spending billions of dollars earned from foreign loan for the construction of these zones and infrastructure. Zones which are completed so far include Hawassa Industrial Zone, Kombolcha Industrial Zone, Mekelle Industrial Zone, Jimma Industrial Zone, Adama Industrial Zone, Bole Lemmi Industrial Zone, Kilinto Industrial Zone, Eastern Industrial Zone, Dire Dawa Industrial Zone, Bahir Dar Industrial Zone,

⁸⁰ UNDP, Comparative Study on Special Economic Zones in Africa and China, *If Africa Build the Nests Will the Birds Come?* Working Group Series, (2015), p.12: see also Zeng, Douglas Zhihua, *Special Economic Zones in Africa: Putting the Cart in Front of Horse?* Washington, DC: World Bank, (2012), P.16

⁸¹ Federal Democratic Republic of Ethiopia, National Planning Commission, *Growth and Transformation Plan II*,(2016), P. 143

⁸² *Ibid.*

Debre Berhan Industrial Zone and Arerty Industrial Zone.⁸³ In addition, other four EPZs are under construction whereas four agro-processing zones are already built with the plan to build thirteen more zones.⁸⁴ The government has established Ethiopian Industrial Zones Corporation with a mandate to own, regulate and control the day to day activities of EPZs. Moreover, the Industrial Parks Corporation, Ethiopian Investment Commission and Ministry of Trade and Industry are organs responsible for the management and governance of the zones.

5.1 Why Ethiopia Began Building Export Processing Zones?

The decision of the government to build EPZs emanates from the need to repeat the Asian Tiger development model so as to achieve fast economic development through industrialization.⁸⁵ Both the Growth and Transformation Plan I and II put it that EPZs are indispensable to bring economic structural transformation through industrialization through export diversification, foreign currency earnings, employment creation, technology transfer, and revenue generation.⁸⁶ While GTP I envisaged the establishment of five big industrial parks, GTP II increased the number of industrial parks to be built around thirty. The GTP II plan puts the objectives of industrial policy as follows:

The manufacturing industry plays a leading role in terms of production and productivity, contribution to export earnings, technology transfer, skills development and job creation. By fostering manufacturing value addition and the productive capacity of the sector, the aim is to substantially increase manufacturing products in kind, quality and quantity. This will in turn render the manufacturing industry a major source of foreign exchange earnings. It can also reduce pressure on foreign exchange by substituting imports of strategic products by local products and enable the manufacturing industry to play an important role in the overall economy. The GTP Plan aspired to earn 3. 6 billion USD at the end of 2020 from export revenue from the manufacturing industry and to increase the

⁸³ *Supra* note at 16

⁸⁴ *Supra* note at 17

⁸⁵ UNIDO, Industrial Parks Development in Ethiopia Case Study, (2018), P. 16

⁸⁶ FDRE, National Planning Commission, Growth and Transformation Plan II, p. 136

*share of manufacturing export in total merchandise export to 25% by 2020.*⁸⁷

While the EPZs of the south East Asia are praised for being successful in accelerating the economies of these countries, their counterparts in sub-Saharan Africa are used as examples of failures.⁸⁸ Despite those ambitious efforts and huge spending for the development of industrial parks, the impact those parks brought remains meager. The economic contribution of the EPZs programme remains insignificant and far below the targets in terms of size of investments, jobs created and value and volume of exports.⁸⁹ Even if the aspiration of the government in building the zones is to make Ethiopia a manufacturing hub of Africa by bringing light manufacturing industries, the fact on the ground is far from reality. Some of the intended benefits expected by the government in establishing parks include job creation, export diversification, foreign currency generation, technology spillover, balanced foreign trade, capital flow and economic structural transformation. However, there are indications that Ethiopia might not be in the right direction to achieve the aspired benefits from EPZs. One of the biggest concerns is in relation to employment including the poor quality of the jobs, inadequate wages, job benefits, health and safety standards, job security, and lack of adequate training,⁹⁰ The other concern focuses on fewer-than-expected spillovers, such as low levels of technology transfer, labor migration to city-based zones which burdens already weak urban infrastructure, and over-dependence on zone investors who may move to other countries when labor costs rise.⁹¹ Sometimes no foreign investor may come in to EPZ and the zones may remain vacant for a long period of time.

Despite expending billions of dollars in constructing the zones, employment opportunities remain very low and if there any, they pay inadequate wages and have low labor standards. The exchange rate gains from exports remain

⁸⁷ Ibid.

⁸⁸ Zeng, Global Experiences with Special Economic Zones with a Focus on China and Africa, World Bank, *supra* note at 13 .p. 9

⁸⁹ According to GTP II, Ethiopia plans to earn 3.6 billion USD from exports. But in 2018/2019 budget year only 108 Million USD is the total amount earned from export of the manufacturing sector despite the completion of ten EPZs.

⁹⁰ Petter Gibbon,et,at, An Assessment of the Impact of Export Processing Zones and an Identification of Appropriate Measures to Support their Development, *Supra* note 5, p.14

⁹¹ Ibid.

one of the least gains much lower than the planned gain.⁹² According to Growth and Transformation Plan II the government planned to earn 3.6 billion USD from exports.⁹³ The government of Ethiopia had a plan to earn 1 billion foreign currencies from Hawassa Industrial Park only.⁹⁴ However, in the Ethiopian 2018/ 2019 fiscal year the total revenue from the export of the manufacturing sector was only 103 million USD.⁹⁵ The figure shows that Ethiopia is very far away from realizing its goals. The other bad news about Ethiopia's EPZs is the failure in raising the employment rate. The plan of the government while developing industrial parks was to hire more than two million individuals by 2025. Nevertheless, so far only less than 70,000 people have got employed although half of the planned industrial parks are already completed.⁹⁶ Moreover, the quality of the jobs is very low standard. Evidence has proven that people who work in Ethiopian industrial parks are the lowest paid in the world.⁹⁷ Furthermore, there have been frequent complaints by the workers of poor labor conditions and human rights violations. One of the private EPZs marred by labor abuse is the eastern industrial zone located in Dukem, which is found 30 kilometers away from Addis Ababa. Hawasa Industrial Zone is the other zone, at which employee dissatisfaction is high. People who have been working there complain of insufficient wage payment, inability to make trade unions, being forced to work in unprotected conditions, absence of government response for their complaints.⁹⁸ Thousands of workers in Hawassa EPZ have left their work due to lack of response to their problems of low salary, unsafe working environment and being exposed to sexual abuses and abduction.⁹⁹

Some of the EPZs which were completed more than a year ago remain still vacant. Some of these parks which remain unoccupied or partially occupied include Kombolcha, Jimma, Mekelle, Adama, and Debre Berhan EPZs

⁹² Ethiopian Embassy to Brussels, Available at, (March, 2019): <https://ethiopianembassy.be/2019/05/02/ethiopian-industrial-parks-generate-103-million-export-income/> Last Accessed on February 26/2020

⁹³ FDRE, Federal Plan Commission Growth and Transformation Plan II, p. 136

⁹⁴ CNBC News, (May 2019), available at: <https://www.ien.com/supply-chain/news/21067585/report-ethiopian-garment-workers-are-worlds-lowest-paid> last accessed on 19/07/2019

⁹⁵ *Supra* note; at 92

⁹⁶ *Ibid.*

⁹⁷ See *supra* note at; 94

⁹⁸ *Ibid.*

⁹⁹ Addis Insight, (March 2019), Available at: <https://www.addisinsight.net/2019/03/07/abduction-rape-and-low-salary-at-hawassa-industrial-park-resulted-in-workers-strike/>

though the government has incurred cost of approximately three billion USD to build the sheds and infrastructure. Some of the EPZs are not fully operational even though they are occupied by companies. Evidence has shown that one of the potential benefits of EPZs, i.e. forward and backward linkage, has not yet materialized.¹⁰⁰ Some people also criticize the government for locating EPZs in wrong sites due to political pressure despite some other regions having better potential to be selected as locations for EPZs.¹⁰¹

5.2. Challenges of Export Processing Zone Development in Ethiopia

5.2.1. Insufficiency of the Existing Legal and Regulatory Framework

Ethiopia enacted industrial parks/EPZs proclamation in 2015 with the aim of regulating export processing zones. On the surface it shows that a lot of effort has been exerted to establish a regulatory framework. Nevertheless, Ethiopia's current legal and regulatory framework for EPZs and the various laws that are applicable in relation to EPZs are marred by numerous irregularities and complexities.

One of the areas of law with a proven gap is the land law particularly the law on compensation during expropriation. The compensation principle in Ethiopia is not clear. However, it is known that Ethiopian compensation principle is not in line with indemnity principle which gives an equal or equivalent amount of compensation to the loss sustained by the owner of the expropriated property.¹⁰² The vagueness of the law of compensation has been the source of discontent for smallholder farmers, who have been victims of inadequate compensation. The government seizes large tracts of land from peasants with little compensation which is not adequate for peasants to support their livelihood.¹⁰³ The biggest problem arises from the FDRE Constitution itself when it failed to consider land as a compensable interest.¹⁰⁴ This is always followed by social crisis of hundreds of thousands of households. Dispossessed farmers angered by the government's move

¹⁰⁰ Bayisa Tesfaye, Prospects and Challenges of Industrial Zones Development, *supra* note 12

¹⁰¹ *Ibid.*

¹⁰² Daniel Weldegebriel, Land Rights and Expropriation in Ethiopia, PHD Dissertation, Unpublished, P. 230

¹⁰³ *Ibid.*

¹⁰⁴ See FDRE Constitution, Proclamation Number 1, year 1, p. 1, Article 40(8)

stage demonstrations and violence which leads to the closure of factories.¹⁰⁵ This is because the state denies the people the right to get compensation for the land, as if it is the sole owner of all the land.¹⁰⁶

The other gap relating to EPZs is the gap seen on Ethiopian labor law. So far there is no minimum wage limit both outside the parks and in the parks.¹⁰⁷ The labor proclamation of Ethiopia provided that the wage issue is to be decided by the agreement of the parties only.¹⁰⁸ In fact, the wage amount paid to Ethiopian daily laborers is registered as the lowest in the world. The labor laws of many other countries provide minimum wage limits for laborers.¹⁰⁹ This has led the firms investing inside EPZs to pay the lowest wage in the world.¹¹⁰ One may argue that absence of minimum wage cannot be the reason for the failure of EPZs since they will benefit from the low wage. However, it should not be forgotten that the success of EPZs depends upon how much quality employment opportunity they have created. If they fail to create the required job opportunity which can support their livelihoods, then they are failures.

Lack of adequate regulatory law and implementation on environment is the other regulatory defect which poses a great problem on the wellbeing of the society and animals. The Ethiopian legal system lacks detailed standards on various environmental issues such as impact assessment and the amount of pollutant liquid allowed for release. The proclamation establishing the Environment Protection Authority, the Environmental Protection Organs Establishment Proclamation, and the Environmental Pollution Control Proclamation, has given the mandate at different times to the Environment Protection Authority (EPA) to set standards for water, air, soil, noise, and waste management. Nevertheless, EPA has failed to issue those standards until 2008 except for few “guidelines” for air, surface water, and

¹⁰⁵ Esther De Haan and Martje Theuws, Quick Scan of the Linkages Between the Ethiopian Garment Industry and the Dutch Market, p. 5 available; <https://www.somo.nl/quick-scan-linkages-ethiopian-garment-industry-dutch-market/>

¹⁰⁶ Daniel W. Ambaye, Land rights and Expropriation, Unpublished, Phd dissertation, *supra* note at 102, at p. 287

¹⁰⁷ Yirgalem Germu, The Law and Practice of Minimum Wage at Industrial Parks in Ethiopia, LL.B thesis, Unpublished, p. 38

¹⁰⁸ Labor Proclamation, Proclamation. Proclamation number 377/2003, Article 53(1), Fed. Neg.gaz. Year 10, no. 12

¹⁰⁹ Yirgalem Germu, The Law and Practice of Minimum Wage at Industrial Parks in Ethiopia, p. 20

¹¹⁰ *Ibid.*

groundwater.¹¹¹ Even then the guidelines were limited to effluent air and water discharges.¹¹² Moreover, there is also poor governmental supervision of environmental standards in the zones.¹¹³ Although the majority of Ethiopia's policies and laws on paper are well-written and excellent, their implementation is not as such effective.¹¹⁴ This difficulty is the possible cause of a significant gap between the official commitments and objectives and practices on the ground.¹¹⁵

The other inhibiting law on foreign investment by putting exclusionary provisions against foreign investment is the investment proclamation. The Ethiopian investment law is criticized for being exclusionary and illiberal.¹¹⁶ As a result, many sectors remained closed only to the government or to domestic investors. This has an effect on other sectors. Building EPZs before establishing effective regulatory frameworks is like putting the cart before the horse.¹¹⁷ Hence, the government must think carefully before rushing to spend billions of dollars.

The financial laws and policies used as an incentive to encourage foreign direct investment are also defective for they can damage the Ethiopian economy. One of the incentive policies severely criticized is the loan policy that the government follows to attract investment. The government of Ethiopia provides monetary loan of up to seventy per cent (70%) for investors who come up with 30% of the required capital through

¹¹¹ Environmental Protection Authority Establishment, Proc. No. 9/1995, art. 6(3). Fed. Neg. gaz. Year 1, no. 9; See also Environmental pollution control proclamation, proclamation number 300/2002, art. 4. Fed. Neg. gaz. year 9, no. 12; See also, Environmental Protection Organs Establishment Proc. No. 295/2002., art. 15, year 9, number 16

¹¹² James Kruger, Aman Gebru and Inku Asnake, Environmental Permitting in Ethiopia, No Restraint on Unstoppable Growth, *Haromaya Law Review*, vol.1, no. 1, pp. 73-102

¹¹³ Mulugeta Getu, the Ethiopian Environmental Legal Regime, Versus International Standards, Policy, Legal and Institutional Frameworks, *Haromaya Law Review*, Vol.1, No. 1, pp. 43-72

¹¹⁴ *Ibid.*

¹¹⁵ Emelie Dahlberg, *Anders Ekbom, Menale Kassie, & Mahmud Yesuf, Ethiopian Environment & Climate analysis*, School of Economics and Commercial Law, Goteborg. Goteborg, Sweden. (2008), p. 13

¹¹⁶ Investment Proclamation, Proclamation no.769/2012, art.3-8 Fed. .Neg. Gaz. Year 25, no. 4 and Investment Incentives and Areas Reserved for Domestic Investors Regulation no. 270/2012, art, 3-14, fed. Neg. gaz. Year 19, no. 4

¹¹⁷ Douglas Zhihua Zeng, Global Experience with Special Economic Zones With a Focus on China and Africa, The World Bank Trade and Competitiveness Global Practice, A paper Presented at Investing in Africa Forum, Addis Ababa, (2015), P.9

development Bank of Ethiopia.¹¹⁸ However, using financial incentive such as loan by one of the least developed countries like Ethiopia has a detrimental effect on its economy since it drains the budget of the government.¹¹⁹ As a result, many developing countries are not advised and do not prefer to use financial incentives.¹²⁰ The credit policy followed by the development Bank of Ethiopia is also risky due to the failure of recollection after granting the loan requested by the potential investors.¹²¹ The fact that banks provide credits of huge sum of government money for domestic as well as foreign ‘investors’ without sufficient collateral only with the conditions of the financial viability of the project itself and first-degree collateral security has paved the way for fraudulent entities to embezzle the taxpayers money and to disappear even before starting any investment project.¹²²

Last but not least, there are challenges related to the tax laws. The tax incentives provided by Ethiopia are principally tax holidays and exemption from import duties.¹²³ These types of incentives are known in the literature as profit-based incentives.¹²⁴ Profit-based incentives, as opposed to cost-based incentives, though relatively simple to administer, are not less costly means of encouraging investment. Instead, the best incentive mechanisms are the cost-based incentive approaches.¹²⁵ Cost-based incentives consist of investment allowances, tax credits and accelerated depreciation, which decrease the cost of capital. The would-be extra investment gained per unit of revenue spent is higher for cost-based incentives, since the benefits to investors only accrued if capital investments are made.¹²⁶ Moreover, the

¹¹⁸ Development Bank of Ethiopia, A Short Guide to Access the DBE’s Loans, available at: <https://www.dbe.com.et/BusinessPromotion/Policy/DBENewPolicyEng.pdf> last accessed on 09/01/2020

¹¹⁹ UNCTAD, Tax Incentives and Foreign Direct Investment, Aglobal survey, United Nations Publications,(2000), p.3

¹²⁰ Ibid.

¹²¹ Fasika Tadesse, What Went Wrong With Ethiopia’s Policy Bank? June1, (2019), *Addis Fortune*, available at: <https://addisfortune.com/what-went-wrong-with-ethiopias-policy-bank-dbe/> last accessed on 09/01/2020

¹²² Addis Ababa Chamber of Commerce and Sectoral Associations, Business Finance Guide,(2016), p. 6.

¹²³ Investment Incentives and Areas Reserved for Domestic Investors Regulation, *supra* note at 117.

¹²⁴ Economic and Social Research Council, Review of Corporate Tax Incentives For Investment in Low- and Middle-Income Countries, the Institute for Fiscal Studies, march (2018), p. 13

¹²⁵ Ibid.

¹²⁶ IMF, Options for Low Income Countries’ Effective and Efficient Use of Tax Incentives for Investment, a Report to the G-20 Development Working Group by the IMF, OECD, UN &WB, (2015), p. 20. Cost-based tax incentives involve specific allowances linked to investment expenses, such as accelerated depreciation schemes and special tax deductions and credits. Profit-based tax

principal benefit that the investors are said to benefit from EZS is a better tax incentive relative to other investors who invest outside the zones. Nevertheless, this principle is not applied in relation to Ethiopian EPZs since no separate incentive is provided to the EPZ investors. The sustainability of the investment policy of Ethiopia is seriously questionable given the fact that Ethiopia is in the process of accession to the WTO. The various incentive mechanisms and preferential treatment of EPZs will definitely be inconsistent with the international WTO rules since WTO doesn't allow export subsidy and preferential treatment of selective EPZS.¹²⁷

5.2.2 Poor Business Environment

The costs of doing business are high in Ethiopia due to the bureaucracy during registration, licensing, taxation, trade logistics, customs clearance, foreign exchange, and service delivery. The one-stop-shop service introduced by the government could not bring the expected result. The investment and business environment in Ethiopia is very poor at the national level, and the cost of doing business is very expensive. An enabling business atmosphere is crucial not only to mobilize domestic resources but also to effectively attract foreign investment in the industrial parks.¹²⁸ The World Bank Annual Report (2018) shows a considerable correlation between the Doing Business (DB) indicators and flows of FDI into the industrial parks.¹²⁹ Based on the world ranking of cost of doing business, Ethiopia stands 168th among the 190 countries surveyed.

5.2.3 Civil Strife and Political Instability

Some of the most important causes responsible for Ethiopia's underdevelopment are prolonged civil wars, internal turmoil and civil strife that have been ravaging the country for many decades.¹³⁰ Ethiopia has been a

incentives generally reduce the tax rate applicable to taxable income. Examples include tax holidays, preferential tax rates or income exemptions.

¹²⁷ Dennis Arnold, *Export Processing Zones*, John Wiley & Sons, Ltd.(2017), p. 4

¹²⁸ Abbas Karami, et al, *Ranking the Factors to Attract Foreign Direct Investment in Special Economic Zones*, *European Journal of Scientific Research*, Vol. 101(4), (2013), P.489

¹²⁹ World Bank Group, *Doing Business 2018, Reforming to Create Jobs, Comparing Business Regulation for Domestic Firms in 190 Economies*, World Bank Flagship Report, The World Bank Group, 1818 H Street NW, Washington, DC, P. 2 also available at: <https://www.doingbusiness.org/content/dam/doingBusiness/media/Annual-Reports/English/DB2018-Full-Report.pdf> last accessed on 23/08/2019

¹³⁰ Alemayehu Geda, *Does Conflict Explain Ethiopia's Backwardness? Yes and Significantly* Paper presented at Making Peace Work Conference at WIDER, Helsinki, Finland), (2004), P. 15,

country of ethnic polarization and conflicts for many centuries. Armed rebellions and border wars have been intense in many parts of the country.¹³¹ Although the country has been relatively stable for over a decade, the civil strife and popular uprising resumed in 2016 due to frequent protests. This has brought a lot of challenges to the booming economy of the country.¹³² The flow of foreign direct investment has decreased significantly following the unrest in major cities of the country.¹³³ Due to the unrest, EPZs such as Bahir Dar EPZ, Kombolcha EPZ, Debre Berhan EPZ, Dire Dawa EPZ, Mekelle EPZ and Bole Lemi II EPZ are still unoccupied or partially unoccupied even though over a year has passed since their completion.¹³⁴ Multinational companies will not dare to reside in the EPZs built by the government unless they are sure that their investments will be safe.

5.2.4 Lack of Adequate Infrastructure

This is an overall constraint for all the zones but at different levels. In general, power, gas, roads, ports, and telecom are the key constraints and many governments and developers try to resort to the PPP approach to solve the constraints. For instance, all the four EPZs which are built in Amhara region are not fully operational due to electric power shortage. Except for Dire Dawa, Adama and Bole Lemi EPZs, the rest of the zones are not connected to the harbour through railway line.

5.2.5 Expropriation and Compensation Challenges

The laws relating to compensation are so vague, unfair, and discriminatory and old that they are creating discontent everywhere.¹³⁵

¹³¹ Ibid.

¹³² International Crisis Group, Ethiopia Ethnic Federalism and Its Discontents, Sept. (2009), P.23; Available at; <https://www.refworld.org/pdfid/4aa4c0c82.pdf>, Last accessed on 01/01/2020

¹³³ Washington Post, Available at: https://www.washingtonpost.com/world/africa/investors-shy-away-from-ethiopia-in-the-wake-of-violent-protests/2016/11/01/2d998788-9cae-11e6-b552-b1f85e484086_story.html; Last accessed on 01/01/2020

¹³⁴ Ethiopian Industrial Parks development Corporation, available at: <http://www.ipdc.gov.et/index.php/en/industrial-parks>, Last accessed on 01/01/2020

¹³⁵ Brightman G/Michael, The power of Land Expropriation in the Federation of Ethiopia: The approach, Manner, Source and Implications, *BDU Journal of Law*, Vol.7(1), (2019), P.8: See also Daniel Wolde Gebreil, Land Rights and Expropriation in Ethiopia, *supra* note at p. 289

5.3 Legal and Policy Recommendations for a Better Achievement from EPZs

The success or failure of EPZs depends on the measures taken by each country and the socioeconomic and political situations of a given country. Each successful EPZ is the result of a number of internal and external factors. What has worked for one country may not work for the other country. Ethiopia must adopt policies and strategies which are appropriate for the conditions of the country. In fact, there is no one-size-fits-all rule for all EPZs. Ethiopia should customize the development of the zones to fit the domestic conditions and the needs of the time. For instance, South Korea's EPZs model was one of the most successful since the zones were developed for promotion of export-driven light industries with global competitiveness in 1960s, and laid the foundation for industrial growth in 1970s. Nevertheless, the model of Korea, which was adopted decades ago, cannot be the best solution for the condition that exists in Ethiopia now unless it is modified to fit the Ethiopian situation since international economic situations have greatly changed, and the development levels and circumstances of Ethiopia differ from the Korea of the 1960s.¹³⁶ That is why many African countries failed in their EPZ project.¹³⁷ The textile and garment factories of Ethiopia are unable to compete with other countries such as Bangladesh despite a lot of effort from the government.¹³⁸ Hence, the writer of this article suggests that the government could ameliorate the failure and profit from EPZs if it takes the following legal and policy measures.

5.3.1 Take Broad National Economic Reforms

Many scholars and institutions including the World Bank prove that EPZs should only be taken as a second best policy choice¹³⁹. Effective and stable monetary and fiscal policies such as proper budget management, reduced inflation, and independent fiscal policy, legally protected private ownership of property and land and investment laws provide a general favorable environment for the success of EPZs. The government of Ethiopia is advised

¹³⁶ Hyeyoung Cho, Industrial Park Development Strategy and Management Practices, *supra* note at 11, p. 107

¹³⁷ Farole Thomas, Special Economic Zones in Africa: Comparing Performance and Learning from Global Experience, *Supra* note at 72, P

¹³⁸ *Supra* note, at 105

¹³⁹ Dorsati Madani ,A Review of the Role and Impact of Export Processing Zones, World Bank, (1999), P.7

to take a broader economic reform regardless of whether targeted or general policies are deemed suitable. The prominent issue is that EPZs cannot be taken as isolated entities. It has been reported that the investment law has been amended more than eight times since 1991. Nevertheless, the fact that the government still controls some sectors such as the financial sector and excludes some sectors of the economy invites a lot of criticism against the economic policy the government follows. Some might argue that the government has registered a double digit economy with a restrictive policy and there is no need of liberalization. However, it should not be forgotten that the current economic growth is due to a huge loan from abroad and is temporary in nature since it is the result of service sector led growth. For dynamic gains to be possible EPZs must be part of a broader policy environment.¹⁴⁰ In this regard, Farole states:

One of the main differences between EPZ programs that have been successful and sustainable and those that have either failed to take off or have become stagnant enclaves is the extent to which they have been integrated in the broader economic policy framework of the country. Successful EPZ programs do not simply view zones as a static instrument of trade and investment policy. EPZs have not had a catalytic impact in most countries, in part because they have been disconnected from wider economic strategies. Often, EPZ programs are put in place and then left to operate on their own, with little effort to support domestic investment into the park or to promote links, training, and upgrading. Unlocking the potential of a park requires clear strategic integration of the program, and governments must play a leading role in potentiating the impact of the zone.¹⁴¹

5.3.2 Improve the Supply of Utilities

The term utility includes electricity, water, land, etc. which are used by firms to carry out their production activities. When high-quality, consistent utilities are available, companies can install up to date production techniques and

¹⁴⁰ Peter Gibbon, et, al, An assessment of the Impact of Export Processing Zones and an Indication of Appropriate Measures to Support Their Development. *Supra* note at 40, P. 56

¹⁴¹ Farole, Thomas, Special Economic Zones in Africa , Comparing Performance and Learning from Global Experience, *supra* note at 57, p 9

ensure the efficient use of resources; but if they are absent, costs rise, productivity suffers, and output is inconsistent.¹⁴² Ethiopia is far from being satisfactory as regards utility supplies. Even though the cost of electricity and water, and investment land is considered one of the lowest in the world, the consistency of the supply remained highly unsatisfactory. Hence, if the government of Ethiopia wants to obtain positive impact from EPZs, it should work on improving utilities.

5.3.3 Establish Improved Business Regulation Mechanism

The reality in Ethiopia shows that there are very complex, rigid laws, regulations, procedures and bureaucracy which weaken competitiveness of firms by raising the costs and risks of doing business, consuming substantial management time, and distorting the incentives that are the basis of competition. It is needless to say that the procedure followed to start a business such as obtaining a business license, an investment permit, land access procedures, preparing facilities, and access to utilities and other services are more often than not time-consuming, costly, and prone to corruption by government officials.¹⁴³ Hence, it is better for the government to revisit its procedural hurdles.

5.3.4. Revise the Tax Incentive Legal Regime

The current Ethiopian investment law provides various fiscal incentives such as customs duty exemption for investors of importing of raw material and inputs including machineries, tax holiday on income taxes ranging from zero to nine years depending upon the type of the industry, and various other exemptions.¹⁴⁴ Nevertheless, those who reside in the export processing zones are not entitled to additional fiscal exemptions from investors residing outside export EPZs. Empirical research done on the area has shown that tax incentives are not the priority considerations for investors to invest in a given country.¹⁴⁵ Moreover, the various fiscal incentives provided by the government do not apply to all EPZs operating in the country since the investment incentives regulation excluded those EPZs operating in and

¹⁴² Ibid.

¹⁴³ Ibid.

¹⁴⁴ Investment Incentives and Investment Areas reserved for Domestic Investors Council of Ministers Regulation Number 270,/2012, Art.3-13, Reg, Fed. Neg. Gaz. Year 19, no. 4

¹⁴⁵ Jose Daniel Amado, Free Industrial Zones: Law and Industrial Development In the New International Division of Labour, (1989), Vol.11(1), P. 136

surrounding Addis Ababa from the income tax holiday. Based on this law, EPZs such as Bole Lemmi I and II, Kilinto, Eastern Industrial Zone, etc. are not entitled to tax exemption.¹⁴⁶ The other gap in the tax and investment law of Ethiopia is it doesn't deal with tax issues if an enterprise re-registers in another name after its tax holiday is over. This is due to the fact that multinational companies change their names simply to use it as a tax avoidance scheme when the tax holiday comes to an end. The Ethiopia tax incentive scheme should also be changed from benefit-based incentive to cost-based incentive system. Hence, the tax regime must be amended to address these issues.

5.3.5 Improve the Labor Law and Labor Conditions

The Ethiopian labor law suffers from numerous defects and gaps relating to labor rights and conditions. For instance, it doesn't provide for minimum wage limits. Rather the employment proclamation leaves the issue of wage to the agreement of the parties.¹⁴⁷ Even though Ethiopia unlike some other developing countries did not adopt special lax labor regulations that apply only within the zones, the general labor proclamation couldn't address some of the basic rights and interests of the workers. This attitude has led to abuses by zone employers. In several EPZs, work environments are substandard, safety measures are almost nonexistent, strikes are banned, industrial injury compensation is lacking, and workers are employed on a temporary basis.¹⁴⁸ The biggest gaps in the Ethiopian labor law are the absence of minimum wage limit and the absence of minimum monthly overtime work. The government is urged to revise the labor proclamation in a way which entitles workers to rights such as a minimum required wage, bonuses, profit sharing, housing, education, and to bring administrative reform towards improving the labor conditions of the employees.

5.3.6 Encourage Domestic Content Requirement

No legislation or measure in Ethiopia put local content requirement on investors investing inside EPZs. Due to the right of complete exemption from import duties provided to investors by the investment regulation, investors in the EPZs prefer to satisfy their input needs from imported

¹⁴⁶ *Supra* note at 144, p. 9

¹⁴⁷ Labor Proclamation, Proclamation Number 377/2003, Art. 58, Fed. Neg. Gaz. Year 10, No. 12

¹⁴⁸ *Supra* note; at 78, p. 68

commodities.¹⁴⁹ In the absence of an explicit law obliging investors to cover a portion of their inputs from the domestic market and in the existence of tax free importing rights, investors are inclined to import their input needs from abroad. For example, the textile industries residing in Ethiopia are trying to satisfy their cotton needs by importing from abroad on the ground of scarcity of the cotton product produced domestically and/or the low quality of domestic cotton is as compared to the imported cotton raw material. This makes the textile industries less competitive vis-a-vis other foreign industries.¹⁵⁰ Due to this reason the net foreign exchange that the companies in EPZs bring is negligible although the gross foreign exchange looks huge. Thus, to maximize the net foreign exchange gain and improve the country's hard currency reserves, Ethiopia must specify in its laws the share of the local inputs that each operator in the EPZs must utilize.

5.3.6. Modify the Land Expropriation Law in a way which Improves EPZ Effectiveness

Ethiopia's current land expropriation law and policy suffers from numerous unfairness issues and weaknesses as it causes a rise in land prices and limits rights of ordinary citizens to own land. The approach in which the Ethiopian government has regulated land deals has been contested, and there are various known cases of land grabs.¹⁵¹ Large-scale land deals are often led by government-led villagisation projects, in which local populations are forcibly removed from their land without proper compensation.¹⁵² The existing land policy prohibits land from being sold, or exchanged and in whatever way transferred.¹⁵³ It also limits the ownership of land to the state and the nation's nationalities and peoples of Ethiopia.¹⁵⁴ The policy makes a different tenure system between rural and urban land. As long as the urban land is concerned, the urban land lease proclamation states that anyone can possess urban land only through lease system which is done only through

¹⁴⁹ Amado, Free Industrial Zones, Law and Industrial Development in the New International Division of Labor, *Supra* note at 55, P. 136

¹⁵⁰ *Supra* note, at 105

¹⁵¹ The Oakland Institute, 'We Say The Land Is Not Yours: Breaking the Silence Against Forced Displacement in Ethiopia', (2015), p. 8

¹⁵² *Ibid.*

¹⁵³ FDRE, Constitution, (1995), Art. 40(3), Proclamation No. 1/1995. Fed. Neg. Gaz. Year 1, No. 1

¹⁵⁴ *Ibid.*

auction.¹⁵⁵ As a result, getting access to residential and service sector urban land has become highly expensive whereas land for manufacturing is obtained for little price.¹⁵⁶ This has caused the increase in land prices which encouraged the rich to speculate urban land price.¹⁵⁷ Due to this reason the rich began accumulating urban land with a view that the price will increase in the future. Moreover, the law fails to take land as a compensable interest.¹⁵⁸ To fully exploit the urban lands and to reduce the disappointment of land holders in the land expropriation procedure, the government of Ethiopia must amend the land expropriation and land access law in a way which avoids land speculation and encourages genuine developers.

5.3.7 Improving Infrastructure and Service Provision

EPZs are more than simple physical infrastructure. The provision of devoted services, infrastructure and utilities are what is expected from sector specific parks. The so-called ‘soft services’ of EPZs related to the management support of a hosted company are of utmost importance. An effective EPZ must offer all of them; constant supply, high and consistent quality, and low cost of infrastructure are essential for all services. Grand infrastructures such as railways, airports, harbors, highways, national power grids, water supplies and power substations are essential. A lot is yet to be done if Ethiopia wants to be effective in EPZ. Factories need a range of inputs such as telephone, electricity, water, internet, sewage treatment, transportation, and residence. A service-driven approach means that EPZs will provide a variety of building accommodation to host investors and start-up companies.¹⁵⁹

5.3.8 Improve the Business Environment and the Cost of Doing Business

One of the most important measures that should be taken by the government of Ethiopia to make EPZs successful is to improve the business environment and reduce the cost of doing business. An enabling business atmosphere is crucial not only to mobilize domestic resources but also to effectively attract

¹⁵⁵ Urban Lands Lease Holding Proclamation, (2011), Art. 3, Proc.no.721/2011, Fed. neg. Gaz. Year 18, no.4

¹⁵⁶ Ibid.

¹⁵⁷ Bayisa Tesfaye, Prospects and Challenges of Industrial Zones Development, *supra* note at 12, p. 12

¹⁵⁸ Daniel Weldegebriel Ambaye, Land Rights and Expropriation in Ethiopia, *supra* note at 106, p. 289

¹⁵⁹ UNIDO, Europe and Central Asia Regional Conference On Industrial Parks, As a Tool to Foster Industrial Development, Azerbaijan, (2012), P.15

FDI in the EPZs.¹⁶⁰ The World Bank Annual Report (2018) shows a considerable correlation between the Doing Business (DB) indicators and flows of FDI into the EPZs.¹⁶¹ Based on the world ranking of cost of doing business, Ethiopia stands 168th among the 190 countries surveyed.¹⁶² The 2018 aggregate ranking on the ease of DB was based on 10 indexes: starting a business, dealing with construction permits, getting electricity, registering property, getting credit, protecting investors, paying taxes, trading across borders, enforcing contracts and resolving insolvency.¹⁶³ Even though the government has tried to introduce reforms like BPR, Kaizen and Deliverology, the world ranking on the ease of doing business report of the World Bank tells us that Ethiopia has a lot to do to improve its business environment.

5.3.9. Stabilize the Political Situation of the Country

Recent studies have shown that political stability ranks among the most important factors that multinational companies consider when deciding to invest in a third world country.¹⁶⁴ The political situation of Ethiopia for the past three years is not helpful to realize the expectations from EPZs. Hence, if the government wants to maximize the benefits, it must improve the volatile political landscape and must reduce the ethnic tensions that jeopardize the stability of the country.¹⁶⁵

5.3.10 Situate EPZs in Appropriate Locations

The government of Ethiopia has been constructing some of the EPZs such as Jimma EPZ, Bahir Dar EPZ, Mekelle EPZ, Hawassa EPZ, and Debre Berhan EPZ in remote locations where there is no adequate infrastructure such as railway line connecting the zones with seaports. The lack of seaports is

¹⁶⁰ Abbas Karami, et al, Ranking the Factors to Attract Foreign Direct Investment in Special Economic Zones, *European Journal of Scientific Research*, *supra* note at 128, P. 492

¹⁶¹ World Bank Group, *Doing Business*, *Reforming to Create Jobs, Comparing Business Regulation for Domestic Firms in 190 Economies*, *Supra* note at: 129

¹⁶² *Ibid.*

¹⁶³ *Ibid.*

¹⁶⁴ For example, a linkage has been found between the political instability in Panama since late 1987 and a decrease in the interest of potential investors in visiting the Colon EPZs. See, Bettwy, *Mexico's Development: Foreign Trade Zones and Direct Foreign Investment*, *Comp. Jud. Review*. Vol.22(49),(1985), p.11

¹⁶⁵ Alemayehu Geda, *Does Conflict Explain Ethiopia's Backwardness? Yes and Significantly*, *supra* note at 130, p. 14

exacerbated by lack of modern large scale infrastructure. But EPZs have to be easily reachable and closer to seaport or an airport. Moreover, EPZs must be located in places where there is abundant supply of human resources. Building EPZs in remote and less accessible areas for the sole reason of balanced regional development will not make the zones efficient and effective if they are not located in places where there is natural resource, access to seaport, railway lines and utilities.

Concluding Remarks

In a nutshell, as it is observed from the various strategic documents of the country, the goals of designating and developing EPZs were to create a middle income country by 2025. They were set to provide dynamic and static benefits including the creation of two million jobs, 3.6 billion USD foreign currency earning, backward and forward linkage with the domestic investors, technology transfers and a catalyst effect on the economy. However, ten years after the launch of the EPZ programme and after ten EPZs have built throughout the country with the expenditure of more than three billion USD, the result appears that it is a disappointment for the country. When the results achieved so far are contrasted with the objectives set by the strategic plans of the government based on the teleological approach, the envisioned goals of employment generation, export diversification and foreign currency and technology spillover are not happening as expected. Absence of appropriate legal, regulatory framework on labor law, tax law and policy, environment law and policy, financial law and policy, expropriation law and policy, poor business environment, civil strife and political instability and lack of adequate infrastructure are identified by this paper as the main factors for the underperformance and lesser impact on the economy of the country. Well-designed reform in the laws and policies, improving the business environment to reduce the cost of doing business, restoring permanent peace and security are the suggestions that this paper makes for the authorities.