

McKinsey
& Company

Ensuring Customs involvement for FZs' competitiveness, safety and sustainability

WCO FREE ZONE CONFERENCE

14 DECEMBER 2020

CONFIDENTIAL AND PROPRIETARY

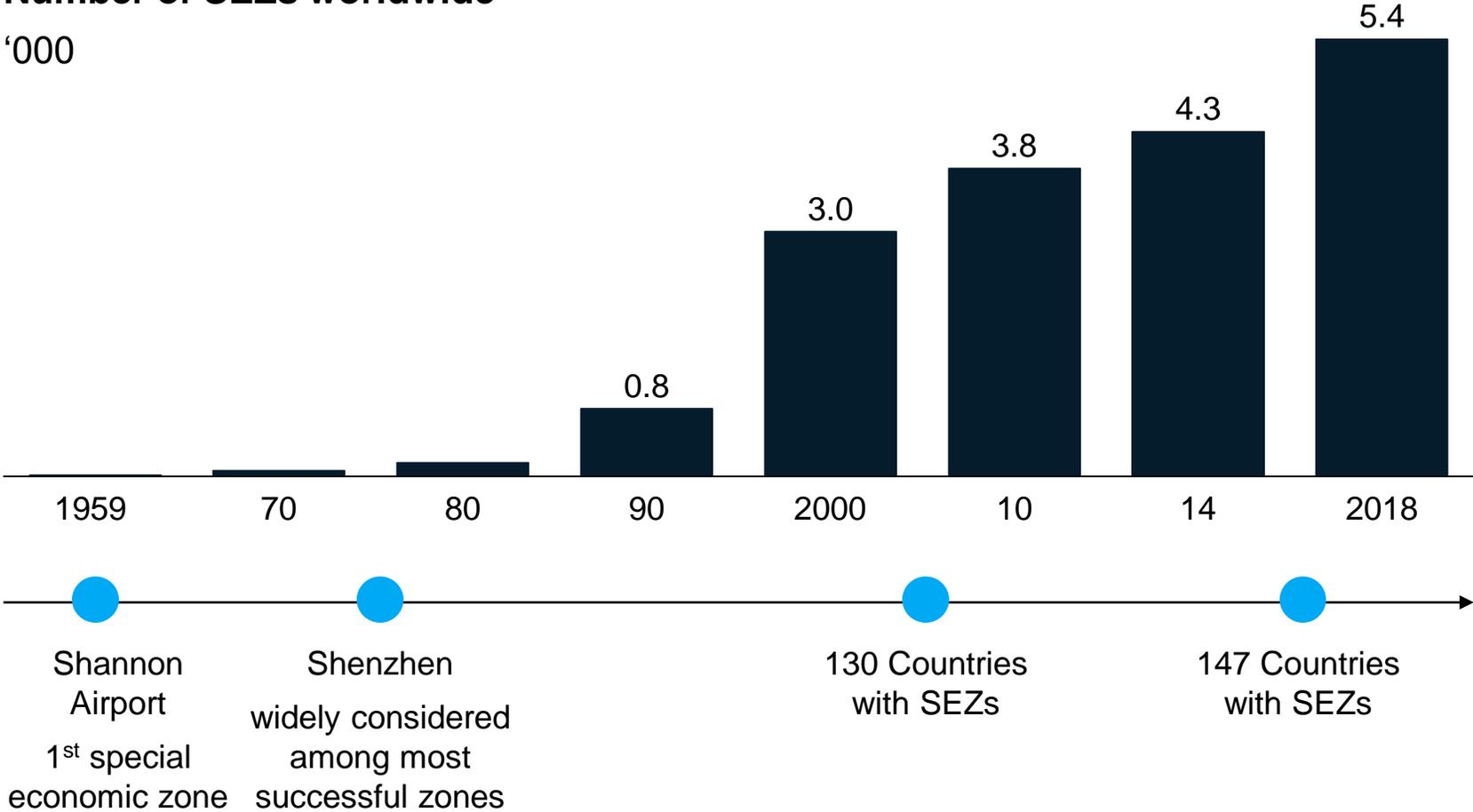
Any use of this material without specific permission of McKinsey & Company
is strictly prohibited



Since the 1950s, over 5,000 Special Economic Zones (SEZs) have been set-up in 147 countries, with a significant acceleration since the 1990s

Number of SEZs worldwide

'000



Economic benefits of SEZs include:

- Job creation – 70million+ jobs
- FDI attraction
- Acceleration of industrialization goals
- Reputation building for country

Source: The Economist 2015. "Special Economic Zones, Political priority, economic gamble", UNCTAD

Success is by no means guaranteed as there are several common pitfalls that cause zones to underperform

NON-EXHAUSTIVE

SEZ failure is common

Research of 30 benchmarked zones shows **~50%** have underperformed their national base economy

SEZs which have the **same starting conditions can have widely different outcomes.**

In one country, one of the first 4 SEZs accounts for **~80%** of SEZ exports

Examples of pitfalls

Ease of doing business



Lack of follow-through on cutting bureaucracy and red tape



Regulatory rigidities that conflict with specific investor needs



Opaque dispute settlement mechanisms, as well as unclear and inconsistent lines of decision-making authority within the government

Start-up challenges



Lack of adequate primary infrastructure for large scale industry



Lack of access to financing and capital deployment during the early stages



Challenges in attracting and/or developing necessary talent at sufficient scale

Five foundations for success of SEZs that improve chances of success and contribution to economic growth

Foundational elements to set-up a special economic zone could include the following:

NON-EXHAUSTIVE



Develop a cohesive SEZ strategy

Establish clear objectives for the zone, a compelling value proposition, and identify specific sectors where the zone can realistically compete to win



Reduce the friction of doing business

Create a “one-stop shop” to minimise administrative regulatory burden, and provide targeted relief from duties and/or taxes



Attract anchor investors

Target specific anchor investors in sectors where the zone can be competitive vis-à-vis regional peers and catalyse necessary infrastructure and other incentives



Build on anchor investors to attract adjacent industries

Pursue broader ecosystem of investors surrounding anchors (e.g., OEMs in auto, specialty logistics players)



Develop surrounding infrastructure and foster a thriving community

Grow the residential attractiveness of the zone and deepen linkages to the domestic economy to sustain growth over time

Creating a successful SEZ is a complex undertaking

NON-EXHAUSTIVE

Successful investor attraction requires choices of which levers matter most...

Set-up and ecosystem readiness

- Quality of talent
- Labour productivity¹
- Social services and lifestyle availability²
- Primary infrastructure development³
- Market connectivity through transport system⁴
- Network ecosystem⁵

Regulatory framework

- Foreign ownership
- Land ownership
- Labour flexibility
- Safety & Security
- Dispute resolution system
- Capital repatriation

Financial incentives

- Corporate tax
- Personal tax
- Corporate loan rate
- Financial subsidies⁶
- Customs regime

Service level provided

- Registration
- Licensing
- Trading across borders
- Global enabling trade
- Ease of doing business
- Global competitiveness

Cost positioning

- Labour cost
- Construction cost
- Land lease cost
- Utilities cost
- Telecom cost

- Local labour
- Hospitals, schools, ITC
- Power, water, commercial and industrial infrastructure
- Port, land, rail, air transport
- Number of Multi-National Companies (MNC) and facilities present in a zone
- Including set-up and training aid, land and utilities subsidies



... coupled with high performance

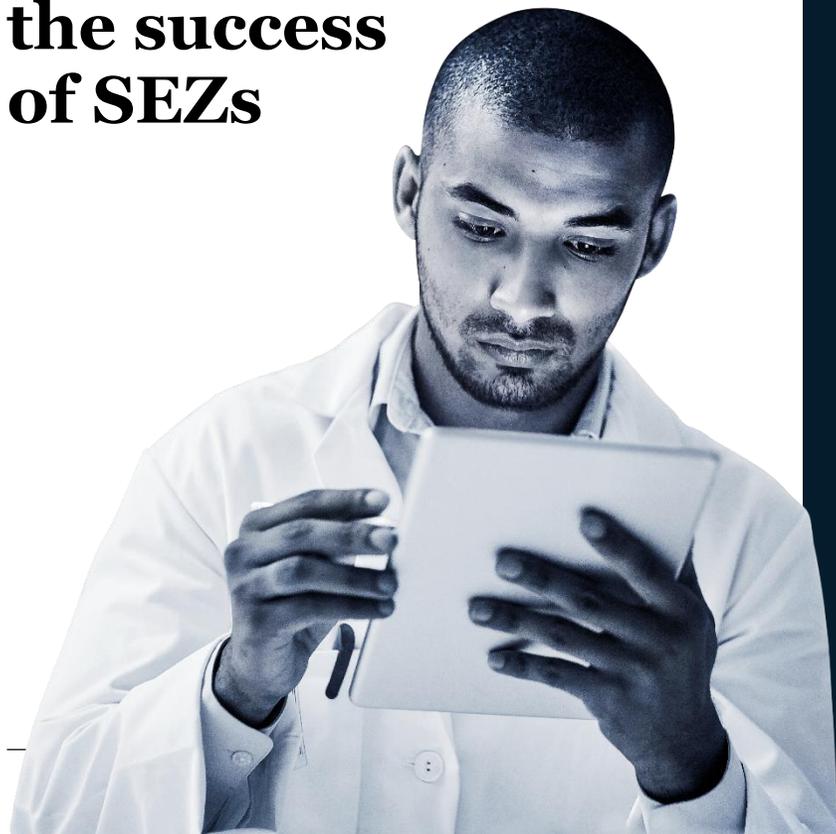
Successful SEZs strive for **Delivery against performance commitments** across key operational processes (e.g. regulatory approvals, customs procedures, etc.)

Effective collaboration with the private sector through formal and informal channels

Streamlined governance among zone operators, customs, and relevant partner government agencies

Clarity of overall vision and objectives among government leaders regardless of their portfolio (e.g., economic development, customs and trade, security)

Customs agencies have a crucial role to play in enhancing the success of SEZs



Deliver on promises made to investors about trade facilitation (trade promotion and incentives) to increase investor confidence

Use information to inform strategy – To be effective in achieving revenue and security objectives despite fast-changing digital landscape in logistics, customs agencies could consider investing in maximizing information resources and keeping up by building data sets and using cutting edge analytics

Secure a seat at the table, early – Agencies could consider embracing a collaboration mindset and be at the table from the initial proposal to establish a SEZ through the daily operations and management of an established SEZ

Safeguard good governance – Take the lead in designing and upholding proper governance frameworks to ensure that zones are managed according to local, regional, and global regulatory requirements

Become global ambassadors – Leading customs agencies could facilitate global peer-level discussions to share best practices, success stories and lessons learned through bilateral discussions, partnerships, and regional bodies like the World Customs Organization