India's policy on Special Economic Zones under fire

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27 October 2006

Only eight months ago, when the Indian government's Special Economic Zones (SEZ) legislation commenced, it was touted as a lever to modernise India's infrastructure and economy for the coming decades. Today, business and political commentators are already branding the SEZ law a failure.

The SEZs were promoted by Commerce Minister Kamal Nath as creating a large flow of foreign and domestic investment that would bridge the gap between China and India in infrastructure and exports, and create massive employment opportunities.

The Congress party-led government sought to attract companies to the zones by exempting them from licenses and duties on imported goods and allowing the free repatriation of profits. The commerce ministry's web site described the SEZs as "designated duty free enclaves to be treated as foreign territory for trade operations and duties and tariffs".

In addition, the government offered companies operating in SEZs a tax holiday for the first five years and a 50 percent tax reduction for the next five years. SEZ developers receive ten years tax-free.

Although the commerce ministry continues to tout the zones, the International Monetary Fund, India's finance ministry and the Reserve Bank of India have criticised the policy in recent weeks. All have pointed to hundreds of proposed or approved SEZs that are far too small to improve India's performance in the long term. These SEZs have proved to be little more than tax loopholes for real estate speculators and developers.

The commerce ministry's Board of Approvals has authorised 181 SEZs and endorsed another 128 "in principle". A developer can set up an SEZ on as little as 10 hectares. The average size of the approved SEZs in Indian is only 420 hectares, compared to zones of 40,000 hectares or more in China.

On September 14, the IMF research director Raghuram Rajan described India's SEZ policy as a tax "give-away" that was likely to shift Indian production to SEZs rather than create new economic activity. He said the zones would be viable only if they focused on providing superior infrastructure, business-friendly regulations and exemptions from labour laws "rather than offering often misdirected subsidies, guarantees, and tax sops that a stretched budget can ill-afford".

Business leaders are pushing for more pro-corporate labour laws, regulations, land zoning and taxation across the country, not just in the SEZs.

In many cases, the SEZs are little more than real estate ventures rather than production zones. The rules require only that 35 percent of a SEZ be devoted to productive activity. A developer can use the rest of the land to build apartments, hotels and commercial offices.

Significantly, the SEZ Act facilitates the forceful acquisition of land for conversion to other uses, providing a massive windfall to the developers. This measure has already provoked opposition from farmers.

The finance ministry complained that existing or planned investment would simply be diverted into the SEZs. According to its calculations, the resulting loss in direct taxes, customs and excise duties would be 900 billion rupees ($US19.5 billion) by 2009-10.

On September 21, Congress party president Sonia Gandhi also expressed opposition. She said, "prime agricultural land should not normally be diverted to non-agricultural uses" and called for satisfactory compensation to be paid when land was taken over. Her comments were followed by a string of similarly empty comments by other Congress leaders designed to quell growing discontent among farmers.

The government sought to dispel the media speculation about the SEZ policy by presenting a united face at an October 7 meeting. Finance Minister P Chidambaram said he and the commerce minister had agreed on the SEZ policy. Prime Minister Manmohan Singh declared that the policy would not change.

Despite the government's determination to proceed, the flaws and criticisms of the SEZs are a significant blow to the Indian corporate elite. New Delhi designed the SEZ policy to give an impetus to the private sector to overcome India's massive infrastructure problems, which are widely acknowledged an impediment to investors.

A recent *Financial Times* article described the situation. "While manufacturers are attracted to India's low-cost environment and burgeoning domestic market, they are worried about moving their goods—be it cars, mobile phones or textiles—through the country's poor network of roads, overburdened airports and clogged ports. Power cuts can force business to a grinding halt."

Indian economic planners have long envied China which has devoted large swathes of land to SEZs and provided government-financed infrastructure to developers. Commerce Minister Nath tried to put a positive spin on his policy, declaring: "India will have a very India specific model as we do not have large lands available." Unlike India, China's nationalised land and police state laws have facilitated the forcible acquisition of areas for SEZs.

Indian farmers are protesting against the forced acquisition of their lands. In the Raigad district of Maharashtra, the state government has served acquisition notices on 20 villages with 1,200 farmers to make way for the Mumbai Special Economic Zone (MSEZ), to be developed by the giant Reliance Group. The villagers have stopped Reliance officials setting foot on the land.

This land is particularly valuable to the farmers because of the promised, but not delivered, irrigation water from the 1980 Hetwane Dam project. Now the state government is forcibly buying the land for a pittance even though its market value is expected to jump by over 15 times when rezoned.

Thousands of farmers have attended protests addressed by the Communist Party of India (Marxist). The CPI(M) and other Left Front parties claim to oppose the SEZ Act, but in reality are proposing minor modifications to the policy. The CPI(M) calls for the allocation of 50 percent, rather than 35 percent, of land in an SEZ to productive activity and an end to the forcible acquisition of prime agricultural land.

The CPI(M)'s opposition is particularly hollow given its crucial support in passing the SEZ legislation in May 2005. The party voted for the package in both the Lok Sabha (lower house) and Rajya Sabha (upper house). The CPI(M)'s role on the SEZ law is similar to other social issues—to act as a political safety valve for protests and popular opposition, while providing the Congress-led government with crucial parliamentary support.

The Left Front government in West Bengal, headed by CPI(M) chief minister Buddhadev Bhattacharjee is at the forefront of forcefully acquiring land for SEZs. In the past year, it has acquired land for industrial zones for Tata, Reliance and Indonesia's Salim group. Much of the land acquired in Singur for the Tata car manufacturing complex was agricultural land, provoking determined protests by hundreds of farmers.