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# Renewed Effort to Develop Special Economic Zones in Northeast Asia

## Comparing Shanghai Pilot Free Trade Zone, Incheon Free Economic Zone and Tokyo Strategic Special Zone

### Topic and Research Question

With the slowdown of traditional trade and the general trend of trade and investment liberalization, new trends in global economy has called into question the efficacy of SEZs (particularly EPZs), not to mention the social and environmental problems that have been increasingly associated with SEZs. In response, Asian countries started to revamp or upgrade their zone approaches, objectives, policy packages and institutional arrangements, with the expectation to further tap the potential of SEZs and upkeep their relevance in the current context. South Korea started early by introducing Free Economic Zones (FEZ) to break away from traditional manufacturing; China introduced Pilot Free Trade Zone program (FTZ) in 2013 after a more ambitious leadership took office; even Japan, a country that had so far been unlucky with SEZs, launched the National Strategic Special Zone program (NSSZ) in 2013 to overhaul vested interests that have hindered development in the past.

Three specific zones are chosen for detailed analysis: China's Shanghai Pilot FTZ, South Korea's Incheon FEZ and Japan's Tokyo NSSZ. All three zones are the first of its kind in the country. This paper compares the three specific zones so as to find out:

- What differences and similarities can be identified among the three SEZs?
- Which zone has the best practices?
- Can a Northeast Asian type of SEZs be identified in the three countries' latest SEZ pursuit?

### State of the Art

The huge body of academic literature on SEZs can be categorized into theoretical studies, empirical analysis, and descriptive case studies. These studies concern themselves with two major topics – zone practices and zone impacts, and each topic can be analyzed through the lens of economy, political science, sociology, public policy, business studies and urban planning.

The theoretical foundations for SEZs can be found in orthodox neoclassical theory and heterodox approach that draws on developmental state theory, new institutional theory or new endogenous growth theory (Aggarwal, 2010; Farole, 2011; Asian Development Bank, 2015). In terms of zone impacts, the fundamental debate in academia revolves around the question

whether SEZs can bring about dynamic outcomes. Some scholars cast doubt on the effectiveness of SEZs in achieving more dynamic and long-term outcome (Warr, 1989; Madani, 1999; Jayanthakumaran, 2003), while some studies, generate more upbeat findings regarding SEZs' spillover effect in the wider economy (Aggarwal, 2010; Wang, 2013). In terms of zone performance determinants, quantitative analysis finds national investment climate to be positively correlated with direct outcomes (Aggarwal, 2005; Farole, 2011); particularly, private sector involvement is found to be an important factor (Engman, 2011), but government's role is crucial in some cases (Baissac, 2011).

The SEZ literature is heavily concentrated on the old generation of zones, but newly established zones are of equal research value as they continue to stay relevant in Asia. By looking at China, South Korea and Japan's renewed SEZ effort, the paper aims to help fill up the gap in SEZ literature.

### Methodology and Approach

The research questions will be addressed through qualitative exploratory cases studies. A framework-based approach will be taken to structure the analytical process. By drawing a list of variables from SEZ theories and empirical literature, an analytical framework for zone practices and impacts (see *Table 1*) is developed, which will explain why the variables are chosen and more importantly how to operationalize them when comparing specific cases. Based on the framework, comparative cases studies on three representative zones will be conducted to analyze in-depth their similarities and differences and to see if a shared pattern can be identified. The analysis of cases relies on secondary data, including laws, regulations, government policy directives and other legal documents, reports and surveys from international organizations, statistics released by government bodies and companies, news release, and research articles.

Table 3. A Framework of Zone Performance Determinants

National/Regional Factors	National investment climate
	Human capital
	SEZ approach
	SEZ legislation
	Location in the country
Zone-Specific Factors	The quality of infrastructure
	Fiscal and financial incentives
	Deregulation
	Administrative system
	Institutional arrangements

### Main Facts

**Investment climate** – Japan imposes less restrictions on foreign investors than China and Korea in terms of restrictions, while China remains relatively closed to foreign investment.

**Human capital** – China is lagging far behind its two neighbors from a nationwide perspective, but when the scope is narrowed down to Shanghai, its performance in education is on par with Tokyo and Seoul.

**SEZ approach** – the three countries all have adopted a GVC and cluster approach to their latest major SEZ program, aiming to strengthen their international competitiveness in activities that are at the higher value-added end of GVC.

**SEZ legislation** – South Korea and Japan started with the enactment of an overarching SEZ act; China held back from an overarching statutory FTZ law and chose to gradually formulate its legal framework by relying on local legislation.

**Location** – they all enjoy one of the best geographical positions within the country and are very much on par with each other when compared at the international level.

**Infrastructure** – they all have built up robust transport infrastructure; they are all focused on developing infrastructure for businesses that will be the next growth drivers; they all value social infrastructure.

**Incentives** – the Incheon zone offers most competitive package of tax breaks of the three zones, while tax concessions in the Shanghai zone can be quite a disappointment to investors.

**Deregulation** – they have all made deregulation a top agenda; deregulation has been most forceful in the Shanghai FTZ; Incheon and Tokyo zone both focus on deregulation in the labor market.

**Administration** – the one-stop system of the Shanghai zone is focused on procedural facilitation, while that of the Incheon and Tokyo zone provides more value-added services; South Korea and Japan are two pioneers in the use of the single window customs system.

**Institutional arrangements** – they all have taken a state-led institutional approach towards their zone programs; China is different in that its zone authority is not anchored to a committee or board at the central level.

### Results

Despite differences in legislation, administration and infrastructure, the three countries share important similarities in their latest SEZ effort: all of the zones under study boast great locational advantages and can benefit from the country's most vibrant regional economy; the state has played a critical role in all three zone programs by integrating zone programs with national development strategy and controlling zone authorities; they all have adopted a global value chain and cluster approach, emphasizing new technologies, value-added services and cluster formation. Particularly, the three countries' shared feature of state-led institutional system and emphasis on value-added activities can differentiate their zones from those in Africa, Latin America, South and Southeast Asia. However, they have more in common with free trade regimes like Singapore and Hong Kong, as they aspire to emulate the good practices of the latter. Continued observation of future developments is needed to tell if a Northeast Asia type of special economic zones can be identified.

As to best practices, the Incheon zone stands out for its competitive incentive package, relatively relaxed market access, high administrative efficiency and solid legal and institutional system. However, the Shanghai zone could win investors over without much effort, given the fact that it is a major gateway to China's huge domestic market and sophisticated supply chains.

### References

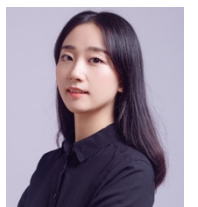
All references can be found in the full version of the MA thesis available at <http://othes.univie.ac.at>

### About the Author

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