



# INDUSTRIAL POLICY IN PAKISTAN

## Decades of Stagnation: Reimagining Export Processing Zones of Pakistan

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Export-led growth remains a distant dream in Pakistan and the country's exports have not seen any remarkable increase. Effective policymaking and institutional competency remain the biggest bottlenecks. The establishment of Export Processing Zones (EPZs) in Pakistan began in the 1980s and after four decades of operation, the exports from the EPZs have hovered around \$1 billion. Investors face bureaucratic hurdles, manual procedures, and dual controls, contributing to the high cost of doing business and stagnation.

Pakistan began establishing EPZs with the objective of promoting and facilitating exports. The rationale for establishing bonded areas was to ensure the efficient provision of services and to avoid the bureaucratic hurdles that are prevalent throughout the country (Akhtar, 2003<sup>23</sup>). The unique feature of EPZs is a special regulatory environment with additional fiscal and non-fiscal incentives (Aggarwal, 2005<sup>24</sup>). One-window facility eases investors' access to the requisite approvals and infrastructure to facilitate manufacturing activities.

It is pertinent to highlight that EPZs were designed for micro and small-scale industries, which have limited capital to purchase land and build infrastructure, and require government support and facilities to enable them to compete globally. Moreover, a cluster-based approach is usually adopted, in which the cohabitation of suppliers, manufacturers, and service providers optimizes supply chains, transfers knowledge and skills, and leads to joint ventures, business development, and economies of scale.

This article is based on the research carried out for the Export Processing Zones Authority (EPZA<sup>25</sup>), which evaluates the performance of EPZs, highlights the challenges faced by investors and presents a way forward to improve the performance of the zones.

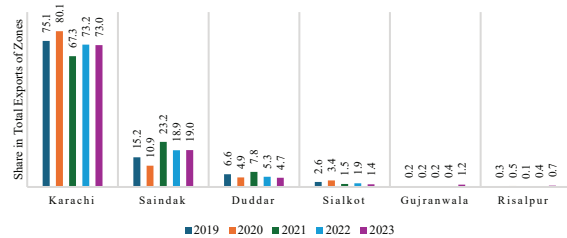
## BACKGROUND AND PERFORMANCE ASSESSMENT

Pakistan initiated work on EPZs with the promulgation of the EPZA Ordinance, the formation of the Export Processing Zones Authority in 1980, and the issuance of guiding principles in the form of the EPZA Rules in 1981.

There are six operational export processing zones in Pakistan: Karachi, Sialkot, Gujranwala, Risalpur, Daddur and Saindak, with cumulative exports of \$910 million<sup>26</sup> in 2023. Karachi Export Processing Zone (KEPZ) has two operational phases, covering 211 acres and 94 acres, with the third phase under planning. Risalpur Export Processing Zone (REPZ) has an area of 92 acres and operations started in 2002. Saindak Export Processing Zone is a single industrial unit zone operational since 2003, covering 1,284 acres. Sialkot Export Processing Zone (SEPZ) has an area of 238 acres and became operational in 2005. Gujranwala Export Processing Zone (GEPZ) has an area of 113 acres and became operational in 2013. Dadduar Export Processing Zone is also a single industrial unit that started operations in 2009.

Exports from zones have not shown substantial improvement over the last couple of years. The share of zone exports in the country's total exports increased from 2.85 percent in 2019 to 3.28 percent in 2023, amounting to \$218 million. The comparative analysis of zone exports indicates that KEPZ has the highest share. The export of KEPZ stood at \$665 million while its share declined from 75.1 percent in 2019 to 73.1 percent in 2023 (Figure 1). Export of Saindak stood at \$173 million and its share increased from 15.2 percent in 2019 to 19 percent in 2023. Export of Daddur cloaked at \$43 million and its share in total exports of zones declined from 6.6 percent in 2019 to 4.7 percent in 2023. The shares of Sialkot, Gujranwala, and Risalpur have been less than 2 percent, with exports of \$11.8 million, \$10.3 million, and \$6.3 million, respectively.

Figure 1: Export Performance of EPZs



Source: Author's Compilation

The analysis of trade composition is important, as EPZs were developed to use local raw materials and export at least 80 percent of production. In the case of KEPZ, around 86 percent of the raw materials used are imported from abroad, while 14 percent is imported from the tariff area (Figure 2). Moreover, KEPZ is exporting 82 percent abroad, while 18 percent is to the tariff area. In the case of GEPZ, the industrial units are consuming 100 percent of imported raw materials, which contradicts one of the objectives of using local raw materials. Moreover, GEPZ exports 97 percent abroad and 3 percent to the tariff area.

In the case of SEPZ, around 81 percent of the raw materials used are imported from abroad, while 19 percent is imported from the tariff area. Moreover, SEPZ is exporting 75 percent abroad while 25 percent to the tariff area, which is in contradiction to the EPZA rules. In the case of REPZ, around 92 percent of the raw materials used are imported from abroad, while 8 percent are imported from the tariff area. Moreover, REPZ is exporting 98 percent abroad, while 2 percent to the tariff area.

23. Akhtar, M. H. (2003). An evaluation of Karachi export processing zone: a preliminary investigation. *The Pakistan Development Review*, 927-940.

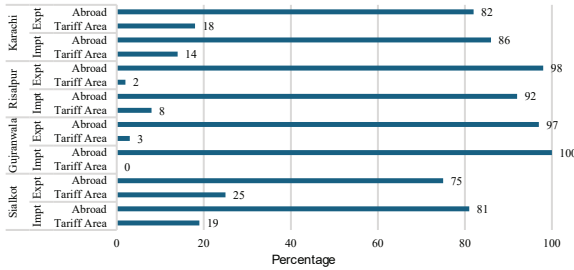
24. Aggarwal, A. (2005). Performance of Export Processing Zones: A comparative analysis of India, Sri Lanka and Bangladesh (No. 155). Working paper.

25. The data is taken from the report "Export Processing Zones in Pakistan: Improvement Plan and New Sites" commissioned by the Export Processing Zones Authority.

26. Export Processing Zones in Pakistan: Improvement Plan and New Sites, Export Processing Zones Authority.

The analysis indicates that all zones use imported raw materials rather than local inputs.

Figure 2: Composition of Trade

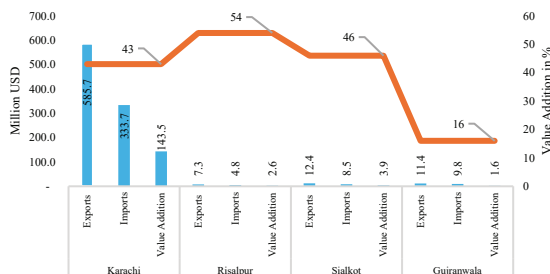


Source: Author's compilation

The zones have shown some improvement in exports. However, it is critical to evaluate the growth in real terms, which could be indicated by value addition. The value addition implies a difference between imports and exports in dollar terms. Value addition is higher in zones with higher levels of manufacturing and processing activity. The highest value addition is observed for REPZ cloaking at 54 percent or \$2.6 million. In the case of SEPZ, exports stood at \$12.4 million, imports at \$8.5 million, and value addition are \$3.9 million, or 46 percent (Figure 3). In the case of KEPZ, exports stood at \$85.7 million, imports at \$333.7 million, and value addition are \$143.5 million, or 43 percent.

In comparison, the exports of GEPZ are \$11.4 million, imports are \$9.8 million and value addition are \$1.6 million or 16 percent. The lower value addition of GEPZ results from its narrow focus on recycling and processing, importing scrap and exporting raw metal billets without graduating to manufacturing sophisticated or consumer goods.

Figure 3: Value Addition by Zones in 2023



Source: Author's Compilation

## UNDERLYING CAUSES OF SUBOPTIMAL PERFORMANCE OF ZONES

### One window facility and manual processes

EPZs are supposed to provide ease of doing business by removing bureaucratic hurdles and manual processes. However, manual processes and approvals continue to prevail. The absence of workshops and service centers in the zones prompts investors to send materials outside the zones for engineering services at various stages of production, requiring EPZA approval. The approval is obtained in the form of a gate pass, for which a specific form is submitted to the EPZA. This highlights two problems emanating from manual processing. First, the time required to visit EPZA to submit the form and obtain approval causes delays. Second is the difficulty in managing records. The expeditious provision of services becomes impossible if processes are manual. Moreover, tracking the movement of goods becomes difficult, which may lead to malpractices or misreporting.

### Investor admission criteria

Since its inception, EPZA has not developed a comprehensive set of investor admission criteria to clarify the objectives of EPZs. At present, there are no guidelines available to evaluate business proposals. Moreover, the zone-specific investor admission criteria have not been developed. As a result, non-manufacturing activities such as trading, warehousing, and the recycling of used textile clothing have increased. Another objective of facilitating micro and small investors remains unfulfilled due to the sale of plots in GEPZ and SEPZ, and the leasing of plots in KEPZ at high prices to investors who have transitioned from small to medium enterprises.

Until now, investors have been granted approvals randomly, without any due diligence or detailed evaluation of business proposals. This can be illustrated by the fact that diverse activities are carried out inside sections of the zone. A planned strategy would have been to allot plots to investors in the same vicinity who intend to carry out the same type of activity. For instance, all traders

should have been located in the same vicinity within the zone, while manufacturers should have been located together. This would have promoted synergy among the industries operating in the same domain.

## DUALITY OF CONTROL

The ownership and utilization of land hold significant importance in attracting investors to the zone. The land at KEPZ is owned by EPZA; therefore, it is easier to upgrade infrastructure and provide utilities to investors. However, the land of GEPZ, SEPZ and REPZ is owned by provincial governments; therefore, development of infrastructure is the responsibility of the provincial governments. Moreover, investors must deal with the provincial government, EPZA and customs while operating in the zones. In multiple instances involving GEPZ and SEPZ, the provincial government sold plots to investors without prior approval of the business plans from EPZA, making it difficult to promote manufacturing activities. The biggest problem arising from the duality of control is the real estate business, where investors purchase land, hold it for years, and then sell it at higher prices, as a lack of coordination between EPZA and provincial governments led to the evasion of penalties for delays in starting industrial activity. This also nullifies the cardinal objective of the EPZs, which is to provide all necessary amenities for industries without bureaucratic hurdles or unnecessary delays.

## INFRASTRUCTURE

The operations in the EPZs are compromised due to infrastructure gaps and service deficiencies. To begin with, the poor state of roads effectively discourages potential investors. Since these roads fall under provincial jurisdiction, the EPZA's ability to act depends largely on collaboration with the local government. Within the zones themselves, the road networks are in poor condition and give a poor impression to prospective businesses. Security is another challenge. Broken boundary walls across multiple zones have led to repeated theft incidents, making investors feel vulnerable. There is no common facility center to support smaller investors, no proper display or exhibition area to showcase locally manufactured goods, and no dedicated library or research space for guidance. The zones lack on-site restaurants and lodging facilities,

forcing investors to arrange meals and accommodation outside the zones and making them unsuitable for hosting foreign clients or attracting skilled professionals from other cities.

Banking services are also limited. The existing facility handles only foreign currency, so converting funds or paying wages to labor often involves risky cash transfers or trips outside the zone. There are no fuel stations, logistics companies, or trucking stations within the zones. As a result, transportation is outsourced at a higher cost, and trucks are frequently seen parked on the roads. Utilities are also unreliable. Power outages are common in several zones, and because there is no dedicated grid, investors bear the heavy expense of running generators. The waste disposal system is outdated and treated as a revenue source rather than a step toward sustainability.

These challenges create an environment where operational costs are high, profitability is uncertain, and convenience is lacking, which runs counter to the objectives of EPZs.

## WAY FORWARD

Keeping in view the problems prevalent in the zones and bottlenecks faced by the investors, the following recommendations are in order:

Investor admission criteria should be developed using a cluster approach to ensure the desired industrial activity is carried out within the zones. An investment promotion strategy needs to be developed for the promotion of exports.

Priority attention is required for the development and maintenance of physical infrastructure. Business and common facility centers need to be developed in the zones.

A plug-and-play facility should be introduced in the zones to conserve scarce capital and reduce the burden on investors.

Adoption of the Enterprise Resource Planning System is crucial to digitize processes and ensure the timely availability of data for decision-making.

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