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The Transformation of Special Economic Zones in the Philippines

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Economic zones come in different names and forms such as industrial agglomeration, industrial parks, technology parks, and export processing zones (EPZ). These economic zones are often instituted to attain various development goals such as industrial development, regional development, infrastructure development, knowledge-transfer and spillovers. In the Philippines, the number of special economic zones (SEZ) have increased rapidly over the past years. As of 2017, there are 379 zones which are operational, and more than hundred zones are currently being developed. In the light of the unprecedented growth of economic zones this study seeks to analyze the transformation of economic zone development in the Philippines. This study also presents key facts and figures about economic zones in the Philippines. This research also explores the impact of the transformation of economic zones on investments, exports, and employment.

Economic zones in the Philippines are defined as selected areas with highly developed or have the potential to be developed into agro-industrial, industrial tourist/recreation, commercial, banking, investment, and financial centers. IT Parks/Centers constitute the largest number of operating and planned economic zones. The development and management of economic zones are dominated by private sector. The geographical distribution of economic zones demonstrates distinct patterns. IT Parks/Centers and Manufacturing SEZ tend to concentrate in few and relatively developed areas of the country. Meanwhile, Agro-industrial SEZ and Tourism SEZ are relatively scattered across the country. Firms who choose to locate within economic zones are entitled to both tax-related and non-tax related incentives. In addition to these incentives, the Philippines also offers the following advantages: fast-growing economy, favorable investment credit rating, large labor pool, liberalized and foreign investor-friendly policies, strategic location, low-cost of doing business, and high-class amenities for expatriates.

There are three main phases of economic zone development in the Philippines: government-led EPZ (1970-1994); private sector-driven SEZ (1995-1999); and Information Technology (IT) industry-centered SEZ(2000-present). The first phase of economic zone development (1970-1994) began in late 1960s. RA 5490 or Export Processing Act in 1969 legislated the creation of the Mariveles, Bataan as the first free port zone. The same act also established the Foreign Trade Zone Authority which is mandated to develop and manage the zones. Three more public EPZ were inaugurated in the following years: Baguio City Export Processing Zone(BCEPZ) and Cavite Export Processing Zone(CEPZ) in 1980, and Mactan Export Processing Zone(MEPZ) in 1986. The establishment of these EPZs have paved the way for the integration of the Philippines into the global production networks.

The second phase (1995-1999) of economic zone development started with the enactment of RA 7916 or the Special Economic Zone Act of 1995. The act enabled the private sector to participate in development and management of economic zones. The act also expanded incentives to firms which are engaged in non-export activities such as commercial/trade services, utilities and facilities, and real estates. The same act also established Philippine Economic Zone Authority (PEZA), a government agency tasked to promote investments, provide assistance, and facilitate incentives to investors or locators within the special economic zones. PEZA took charge in management of the existing public EPZs.

The third phase(2000-present) of economic zone development commenced in 2000 when amendments were made to Special Economic Zones act to encourage and support the investments in IT industry through the establishment of IT Parks/Buildings and provision of incentives to IT enterprises. During this time, the IT and business processes outsourcing (IT-BPO) have just started to gain traction and government have started to take notice of its potential and provided appropriate incentives.

The shift from government-controlled and export-oriented EPZ to private-led zones with wide spectrum of activities has several significant consequences. First, number of economic zones has expanded significantly. Second, as result of larger number of zones, the number of firms has also surged. Third, the industrial composition of activities has changed from manufacturing dominated activities to services-based activities. The number of economic zones has increased from 2 in 1970s to 379 in 2017. There is a remarkable increase in number of economic zones from 1996 after private sector was allowed and incentives were given to IT industry. Majority of the established economic zones from 2000s are IT Parks/Buildings. Subsequently, the increasing number of economic zones has attracted more firms. There is an exceptional surge in number of firms from 2000s. The main industrial composition of activities within economic zones have also changed from traditional manufacturing of export-oriented intermediate processed goods or semi-finished products to IT services and real estate. The changes in the industrial composition of activities within economic zones reflect of the overall structural transformation that have occurred in the Philippines. In 1970s, the contribution of manufacturing and services to GDP were at the same level at 35%. Starting from 1990s, almost half of the total country's GDP were sourced from services with 47% and the percentage of the agriculture sector have fallen to 20%. In 2000s, the services sector remained as the top contributor of economic output with 53% share.

The transformation in economic zone development is manifested in economic indicators of investments, exports, and employments. In the early phase of economic zone development, the contribution of FDI from economic zones to total FDI is negligible at 0.3%. In the second phase of economic zone development, the flow of FDI from economic zones has expanded to 19% share. In the third phase of economic zone development (2000-2015), economic zones accounts for 58% share of the total FDI. In the first phase of economic zone development, export from economic zones constitutes only 7% of the total exports. In the second phase of economic zone development, the share of exports from economic zones has significantly expanded to 38%. In the third phase of economic zone development, economic zones have become the most dominant source of exports in the country with 75% share. In the first phase of economic zone development, the employment in economic zones constitutes a mere 0.2% of the total employment. In the second phase of economic zone development, economic zones accounts for 2% share of the total employment. In the third phase of SEZ development, economic zones contribute 3% share of the total employment. In contrast to investments and exports, the impact of economic zones on employment generation is relatively weak. The plausible explanation behind the marginal effect of economic zones on employment is because the only available data is direct employment.