

The Stalled ZONES

The global economic slowdown, political resistance to land acquisition and lack of clarity on tax policy drive developers to pull out of special economic zones

By Nivedita Mukherjee

It's the favourite mantra of policy-makers, politicians and India Inc and they never tire of prescribing it as a driver of growth and employment generation. Tragically though, for all the chants, once a top item on the infrastructure agenda of the Essars, DLFs and Parsvnaths, special economic zones (SEZs) are now off the priority list of corporate investments. There is a veritable queue of companies asking for extensions, resizing and denotification of proposed projects. At least 10 big developers have got denotifications, allowing them to withdraw from the projects, and of the 236 SEZs that are yet to become operationalised, about 20 are waiting to be denotified.

The big why is usually answered by an allusion to the meltdown. The global climate is indeed not conducive to investments in export-oriented manufacturing facilities, what with global growth shrinking to 1 per cent in 2009 from 2.5 per cent

in 2008. The slowdown of SEZs is an older story that dates back to 2008 when there was widespread political resistance to land acquisitions. Add new policy blocks and the new direct tax code that threaten to take away exemptions that make the SEZs attractive to investors. In short, all the things that these large and sprawling complexes house—factories, information technology parks, office space, warehouses targeting export markets—were meant to be free of encumbrances but it didn't happen.

In December 2009, the Union Ministry of Commerce revealed what was widely speculated—that some of the most talked-about SEZs were on the pending denotification list. Among those looking to pull out are DLF, Essar and Parsvnath.

The original idea of the SEZs, explains D.K. Mittal, additional secretary, Ministry of Commerce, was to create an attractive fiscal package with minimum possible regulations to draw investments. "This would trigger a large flow of foreign and do-

mestic investment in infrastructure and productive capacity, leading to generation of additional economic activity and creation of employment opportunities," says Mittal.

When the story was first narrated to corporates and global investors, the Government was not disappointed. In the rush hour that followed the consolidation of disparate pieces of executive orders, press notes, and regulations governing the SEZ framework in February 2006, there was a scramble to get aboard the SEZ bandwagon. These laws, which had been in existence since April 2000 and now being given effect as a cogent piece of legislation called the SEZ Act 2005, threw up visions of world class infrastructure facilities as in Dubai, Malaysia or China.

Companies across sectors, size and segments trooped in with applications before the Board of Approval, committing mega bucks and plans from Ambala to Mangalore. If Reliance Industries talked of pumping in Rs 30,000 crore into two SEZs,

The SEZ Story So Far

574 SEZs were given formal approvals.

346 were notified.

236 SEZs are not yet operational.

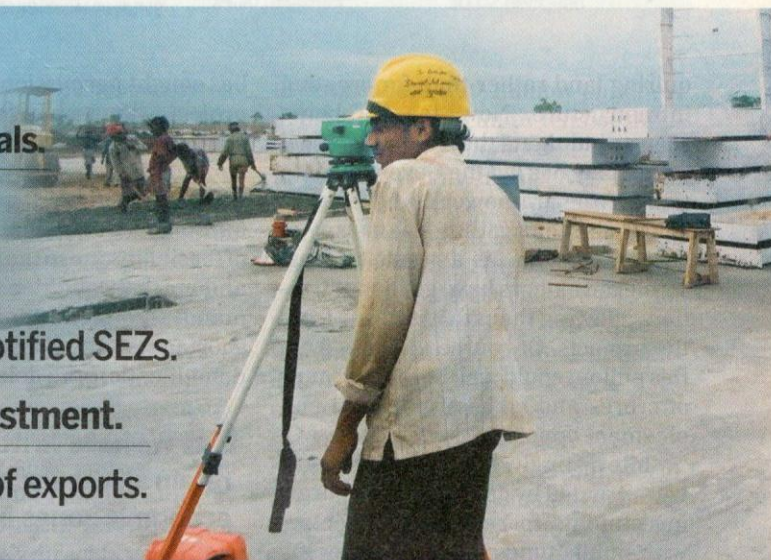
39,120 hectares is the area for notified SEZs.

Rs 98,498 crore is the total investment.

Rs 99,688.87 crore is the worth of exports.

Developers of **29 SEZs** have sought denotification and 16 have sought extension.

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DLF sought to make an investment of Rs 31,000 crore in four units in Punjab and Haryana and others such as Bharat Forge, Videocon, Suzlon, etc were ready with over Rs 1,000 crore each for SEZs in places like Pune and Mangalore. Even the lack of clarity in norms and government flip-flop till a year back did not dampen the enthusiasm of players. The result: a mind-boggling 110 operational SEZs handling businesses from biotech to IT/ITES and other services, 574 approvals, 346 notifications, and investments worth Rs 98,498 crore across 39,120 hectares of land.

It is this mad rush for SEZ approvals that also brought many non-serious players into the fray for whom SEZ applications became a tool for ac-

SEZs were initially capitalised with government money. India though is unique. The idea here was to bring in private resources and management to create an ecosystem for growth. The Rs 1,10,000 crore from 2006-09 poured into SEZs has all come from private sector. The rush though has now turned into a logjam. "Investments have also slowed down substantially," confirms Mittal.

This was, according to Mittal, bound to happen with the global slowdown affecting the SEZ plans of major players. The main attraction of the industrial houses clamouring for SEZ projects a few years ago was the export potential. Essar SEZ Hazira Ltd, which invested close to Rs 8,000 crore in four manufacturing units in Hazira,

Commerce Ministry official says that the entire real estate sector has been hit by a credit crunch. According to industry sources, firms like DLF and Parsvnath have been unable to raise funds for their projects. This is especially seen in the IT/ITES SEZs, a sector which has seen a drastic fall in exports and earnings. The country's largest real estate player, DLF, has approached the Government to surrender five of its nine IT/ITES SEZs, confirms Rajeev Talwar, director, DLF. "We are the biggest provider of IT space. All of us were caught up in the 10 per cent growth story, a potential driver of which was exports. The downturn which has hit exports badly is the main reason for companies pulling out of SEZs. It has hit IT exports badly,

LAND ACQUISITION Political friction, lack of rehabilitation policy and clearance delays have hurt timelines.

GLOBAL SLOWDOWN Shrinking global growth has hit demand, affecting exports and investments.

DIRECT TAX CODE Fearing withdrawal of tax sops, developers have gone into cancel mode.

RED TAPE Lack of clarity in policy and bureaucratic resistance to regulatory changes has hit new projects.

POLICY HURDLES No flexibility to switch from exports to domestic markets has made SEZs unviable.

quiring land rather than for creating infrastructure. Now, fear of being seen as indulging the companies' real estate play has led the Government to tighten the framework and change rules, shattering the dream run of corporate India. As a result, at least 10 big developers have got denotification, allowing them to withdraw from the projects. Of course, the loss from this pullout could well be in thousands of crores and lakhs of potential employment opportunities.

Interestingly, the world over SEZs were created by governments to draw investments to regions and sectors with public funds. China's successful

has sought permission to pull out of a project, citing change in the global perspective which will make it difficult to achieve its exports target. Royal Palms India Pvt Ltd too has requested for denotification stating lack of feasibility due to the global scenario and market conditions. Besides a demand slump, developers cite fund shortage as the reasons for seeking denotification and delay in projects. A

leading to a huge resource crunch, and prompting the move to denotify the SEZs."

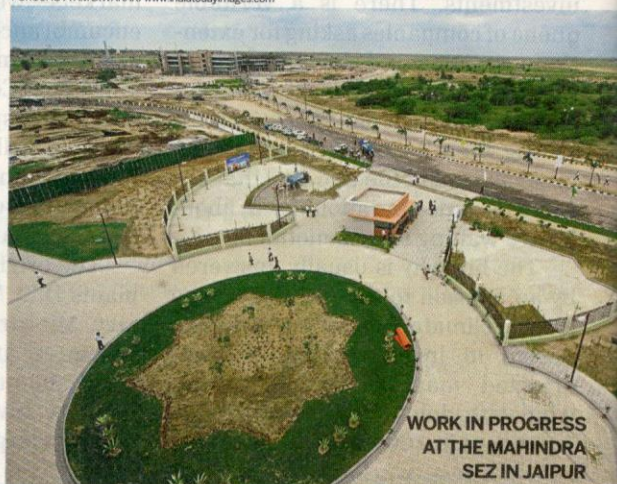
The demand slump has also led to idle excess capacity which, thanks to stringent norms, cannot be used, points out Pradeep Jain, chairman, Parsvnath Developers. "At a time of funds crunch, we are constrained by the absence of any provision for selling part of the land notified for the SEZ

“We have written to the Finance Ministry to retain all the fiscal incentives for the special economic zones in the new direct tax code.”

ANAND SHARMA, Commerce Minister



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WORK IN PROGRESS
AT THE MAHINDRA
SEZ IN JAIPUR

or selling of built-up spaces or giving it on long-term lease to any strategic investor. The non-processing areas should be looked at as an instrument to raise funds for the processing areas," says Jain.

B.K. Subaiah, chief operating officer of Mahindra and Mahindra, which is executing mega projects like the \$1-billion Mahindra World City in Chennai and the \$2-billion Mahindra World City at Jaipur, feels that a large number of applications in smaller SEZs would have resulted in a supply glut had all of them fructified. However, he agrees there do exist certain factors like land that considerably slow down the pace of development. "Land acquisition is among the most challenging issues that puts a strain on the



“All got hit in the recession. We were no exception. We have put on hold 11 SEZ projects and decided to focus on ongoing projects.”

PRADEEP JAIN, Chairman, Parsvnath Developers

Government is talking about a new rehabilitation package for land acquisition related to large projects. It is being debated since 2008. Meanwhile, land costs are soaring and social and political oppositions have been wrecking project plans. Other procedural issues like how much land can be exploited commercially and what can be reserved for what purpose dog those trying to complete projects.

The other big reason for a pullout

which a draft paper has been circulated in the public domain. Those tax concessions specifically meant for SEZs should continue," says Sharma.

Though India's SEZ policy was inspired by global examples of government-industry efforts to cut costs and multiply forex earnings, in practice the compromises made to adapt the model to Indian situations have undermined its viability. The size of an SEZ is capped at 50 sq km, whereas the additional demand for urban space to

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(LEFT) THE RELIANCE SEZ OFFICE IN GURGAON; FARMERS PROTEST LAND ACQUISITION IN PUNE

Denotified SEZs

Essar SEZ, Engineering
Hazira (Gujarat)
267 hectares

Royal Palms India
IT/ITES
Goregaon (Mumbai)
26 acres

Lahari Infra, Services
Kondakal
(Andhra Pradesh)
220 acres

Maytas SEZ, Biotech
Pochampalli
(Andhra Pradesh)
14.16 hectares

DLF, IT/ITES
Gandhinagar
10.12 hectares

DLF, IT/ITES
Sonepat (Haryana)
10.12 hectares

DLF, IT/ITES
Kolkata
10.48 hectares

DLF, IT/ITES
Bhubaneswar
10.23 hectares

Shivaji Marg SEZ, IT/ITES
Shivaji Marg (Delhi)
10.02 hectares

developer, affecting timelines, causing massive delays and jeopardising all project plans," says Subaiah. He is not exaggerating. The problems in acquiring land are making developers re-think their SEZ plans. Reliance Industries, for instance, planned to create two SEZs in Haryana and Maharashtra totalling 6,000 hectares. In both states, the company has faced huge political resistance, led by NGOs in Maharashtra and political parties in Haryana. Indeed, West Bengal, which looked at SEZs as a way to industrialise the state, is the worst hit. Nandigram has now become synonymous with failed SEZs and politics. The

from the SEZs is the proposed direct tax code. Says Hitendra Mehta, who spearheads Assocham's Committee on SEZ: "The draft direct tax code that will lead to an overhaul of the Income Tax Act has created uncertainty among developers. It could take away exemptions and sops like income tax holiday for SEZs, deny them fair play and hurt export competitiveness." Concerned over withdrawal from SEZs, Commerce and Industry Minister Anand Sharma promises to ensure that the sops continue. "We have written to the Finance Ministry to retain all the fiscal incentives for the SEZs in the new direct tax code, for

accommodate 200 million-plus new urbanites would run to tens of thousands of square kilometres. Although developers want themselves out of such projects, director-general of the Export Promotion Council for EoUs and SEZs, L.B. Singhal feels the concept of tax-free enclaves is not passe yet. "People have been expressing doubt... but the number of applications for denotification is minuscule," Singhal says.

There is no doubt that the SEZs have a lot of advantages, but world class infrastructure will reap benefits only when the Government gets its act right anytime soon.