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## **INTEGRATION OF THE SPECIAL ECONOMIC ZONES IN THE LOCAL ECONOMY: THE CASE OF SPECIAL ECONOMIC ZONES IN CAVITE PROVINCE**

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### **Abstract**

*The main objective of this study was to examine and analyze the status of integration of the Cavite Special Economic Zones in the local economy. In order to determine the status of integration of the Cavite Special Economic Zones, it is important to note if these SEZs were able to generate employment opportunities to the locals. Moreover, the different types of local businesses that emerged in the area after the establishment of the special economic zones in the different municipalities in Cavite where these SEZs are located were also considered. Likewise an in-depth analysis of the role of the local government in local economic development was also considered since the local government unit plays an important role in achieving the goal of this export-led strategy, establishing SEZs in the area. Lastly, the factors considered by the Locators when they decided to establish their businesses inside the SEZs in the province of Cavite were also included in the analysis. The researcher used the descriptive method and a multi-stage sampling. The researcher had to select a sample which can represent the pulse of the entire*

*population of the SEZ Locators. The researcher used the survey questionnaire. Aside from the survey questionnaire, the researcher also used the interview method wherein a combination of formal and informal styles or the semi-standardized formats were used. Lastly, the researcher also used the focus group discussion and actual observation of the area as tools in gathering data. Thirty-five (35) locators or (6.61%) of the total number of locators out of the five hundred thirty (530) locators declined to give information/details about their businesses due to confidential reasons. Therefore, there were four hundred ninety-five (495) or (93.39%) locators subjected to interviews and survey. Results showed that the Special Economic Zones in the province of Cavite are highly integrated with the local economy.*

**Keywords**

Export-Oriented Industrialization Strategy, Export Processing Zones, Locators' Integration, Technology Transfer, Foreign Investment

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**1. Introduction**

The paradigm shift from import substitution strategies towards export-oriented industrialization had pushed countries the need to create special economic zones or SEZs. The special economic zones take on many different names and functions. Free trade zones may offer facilities for storage, trans-shipment and redistribution. Export processing zones (EPZs) are mainly for manufacturing and for other exporting industries. The single enterprises can constitute so called “single factory zones”, while the free ports in contrast are often large and diversified (FIAS, 2008; Costachie, 2008; Farole and Akinci, 2011).

The concept of special economic zones (SEZs) has been around at least since the 16th century. Special economic zones were in place already in Gibraltar and Singapore as early as 1704 and 1819 respectively. However, the first modern SEZ was founded in Ireland in 1959 (Gangway, 2003). In 1975, there were still only seventy-nine (79) SEZs in the world (ILO, 2007).

As early as the 1960s, many developing countries have adopted the export-oriented industrialization strategy through the establishment of special economic zones (SEZs) in order to promote industrialization in the area. The Philippines followed the same strategy.

The Philippine State heeded this call of industrialization. The idea of establishing EPZs in

the Philippines dates back to 1923 (Castro, 1982) when the Chamber of Commerce of the Philippines agreed on the setting up of a free port to serve as a free trade zone. In 1937, President Quezon received a favorable recommendations from the committee appointed to study the plan. After the 1946 Declaration of Independence, implementation of the plan was delayed for several years.

There was a shift from an inward-looking import substitution policy of the 1950s and 1960s to a more outward-looking, market-oriented policy in the 1970s. That move was to hasten the development of the country. Only during the 1970s when government sponsored export processing zones (EPZs) were developed here in the Philippines. Those zones were intended to compensate for infrastructure deficiencies throughout the country, thereby facilitating investment in manufacturing. By developing sites with readily available transportation, power and communication facilities, the four EPZs located in Bataan, Mactan, Baguio and Cavite are said to be attractive destinations for foreign direct investment (FDI, 2004).

The EPZ policy continued and was supported by the 1987 Philippine Constitution. It is the declared policy of the Philippine State to attract, promote and welcome productive investments from foreign individuals, partnerships, corporations, and governments, including their political subdivisions, in activities which significantly contribute to national industrialization and socio-economic development to the extent that foreign investment is allowed in such activity by the Constitution and relevant laws.

On the 19<sup>th</sup> of October 1990, the late President Corazon C. Aquino launched the CALABARZON (Cavite-Laguna-Beatings-Rizal-Quezon) Program. This was a regional development program that aimed to promote an export-oriented industrialization (EOI) strategy to the specified areas (PEZA, 1997).

The EOI strategy continued until the declaration of the Republic Act No. 7916 or The Special Economic Zone Act of 1995. The said law provided for the creation of the Philippine Economic Zone Authority (PEZA) attached to the Department of Trade and Industry (DTI). Under the new law, the responsibility of the PEZA has included the administration of industrial estates (IEs), free trade zones (FTZs), and tourist/recreational centers referred to as special economic zones (SEZs) or eco-zones (Congress of the Philippines, 1995). The said law was amended by Republic Act No. 8748.

To date, the existing law which supports the EOI strategy is RA No. 8748 or An Act Amending RA No. 7916, otherwise known as the Special Economic Zone Act of 1995. Republic Act 7916, otherwise known as the Special Economic Zone Act of 1995, authorized the establishment of economic zones in strategic locations and introduced mechanisms that would attract foreign investments into these areas. The areas shall be developed through any of the following schemes: (1.) Private initiative; (2.) Local government initiative with the assistance of the national government and (3.) National government initiative (RA No. 7916, Sec.5).

Under this legislation, firms or the so-called locators were no longer required to be either wholly export-oriented or engaged only in industries being promoted. That is, firms or locators can choose to locate in these economic zones regardless of market orientation, while a distinct group of EPZs will continue to be predominantly oriented towards export production. All locators should be virtually located outside customs territory.

The province of Cavite had decided to establish a number of economic zones in the province as a response to the CALABARZON project, a development project of the late President Corazon Aquino to promote export-oriented industrialization in the area. The province's decision of adopting the Export-Oriented Industrialization strategy or policy through the establishment of a number of economic zones has provided impetus to the development of Cavite. At present, there are a total of eight (8) special economic zones in the province (PEZA, 1997 retrieved at <http://www.peza.gov.ph>, last December 6, 2014).

The Cavite Economic Zone is a special economic zone which was established through local government initiative with the assistance of the national government. The other seven (7) special economic zones were established through private initiative schemes. These include the Cavite Economic Zone II; Daiichi Industrial Park; EMI Special Economic Zone; First Cavite Industrial Estate (FCIE); Gateway Business Park (GBP); Golden Mile Business Park and People's Technology Complex (PTC).

These special economic zones are expected to perform the innate goals as stipulated in the "Special Economic Zone Act of 1995" or Republic Act No. 7916 as amended by Republic Act No. 8748. These innate goals are the following: attracting foreign investment, earning foreign exchange, export growth, employment generation, technology transfer, domestic linkages and regional development. These innate goals also serve as indicators that determine if these economic zones are highly integrated with the local economy.

Studies revealed that as long as the economic zones, through their locators are highly integrated with the local economy, the host community could maximize the benefits or opportunities that these economic zones provide. In line with this, the prime objective of this study was to examine and analyze the status of integration of these special economic zones with the local economy. By looking at this area, there could be an extensive evaluation if the province was able to maximize the benefits or opportunities that these economic zones provide to the province of Cavite.

Likewise by looking at this perspective, the study would contribute to public management through a careful analysis of the existing law on special economic zones which is the Republic Act No. 7916 (Special Economic Zone Act of 1995) as amended by RA No. 8748 (An Act Amending Republic Act No. 7916). Therefore a thorough evaluation needs to be conducted whether these special economic zones in the province of Cavite are highly integrated with the local economy and thus, would determine if the existing law is still effective or some of its provisions need to be amended.

This research applied the Systems and Neo-Liberalism Perspectives. Based on the social systems model, an institution is a system of social interaction; it is an organized whole comprising of interacting personalities bound together in an organic relationship (Waller, 1932). In this sense, the local government unit such as the Cavite Province is an institution wherein when it started adopting the export-oriented industrialization and had several special economic zones (SEZs) established in the different areas of the province, these SEZs would have interacted with other personalities or entities in the province such as the local entrepreneurs, residents of the province, the LGU itself and the national government as well. There must be a healthy interaction among these actors or stakeholders in order to determine whether the program or project and a shift in the economic policy from import-oriented to an export-oriented industrialization can be considered successful.

In applying the social systems model, establishing SEZs was a neo-liberalist perspective. When the Philippines decided to adopt the export-oriented industrialization strategy through establishing several export-processing zones, it opened the State to the global as well as to the international arena. By adopting this EOI strategy, the Philippine government did follow and apply the neo-liberal perspective. The Philippines adopted the EOI strategy, the province of Cavite followed suit.

In a neo-liberalism perspective, export-led growth and foreign direct investments serve as factors of growth to every state. The main objective why these countries set up an EPZ is always to attract investment (ILO, 2007, retrieved at <http://www-ilomirror.cornell.edu/public>, last February 6, 2015). Countries look to such investments to: create jobs; transfer new skills to local human resources; boost the export sector; earn foreign exchange; create links to increase the output and raise the standards of local enterprises that supply goods and services to zone investors; introduce new technology; and even to kick-start the economy as well.

Neo-liberal perspective views EPZs as having important dynamic functions. EPZs play a crucial initiating role in the development of national industrial capacity by offering a platform for internationally mobile productive units; creating an environment conducive to concentrated exchanges between domestic and foreign private sectors; initiating a shift in the orientation of the domestic private sector toward export activities. And just like what happened to Cavite Province, with the presence of Special Economic Zones (SEZs), this served as a venue for foreign firms to expand their market and for the local firms to learn from the foreign firms in terms of: (a) familiarization with the global markets and market standards; (b) these local firms were able to improve their products and increase their productivity; (c) gain confidence to enter the global market since their products are now competitive in the international trade; and (d) was able to acquire that technology transfer and linkage with the foreign zone firms.

Neo-liberals also believed that an entrepreneur is a person whose profession is, to respond to market forces (Treanor, 2008). An entrepreneur changes activities in accordance with the market. Without the entrepreneur, there is no free market therefore; market liberals demand a privileged status for the entrepreneur. Neo-liberals tend to believe that humans exist for the market, and that is good to participate in the market and that those who do not participate have failed in some way. Every human being is an entrepreneur managing their own life, and should act as such.

When SEZs in Cavite province were established at the different areas in Cavite, the people there grabbed the opportunity to put up their own business from offering commercial and residential units for rent to opening a small eatery or mini-store. These only showed that being an entrepreneur is innate to the people of Cavite province. Likewise, these local entrepreneurs also tried to penetrate the zone by accepting sub-contracts from the foreign zone firms. Through this activity, there would be technological transfer from the foreign zone firms to the local

entrepreneurs of the province. Such technological transfer would foster industrial development in non-traditional goods and efficiency gains in production processes of the traditional ones. Such a transfer would also foster a backward linkage to the local firms which would allow them to step in as suppliers to the foreign firms located inside the Cavite SEZs.

In the SEZs, interaction and linkage among economic actor/s such as the foreign firms and domestic firms is expected. Formal equality and access is not enough, they must be used to create links to other members of the society. This attitude has been accurately labelled 'connectionist' (Treanor, 2008). Multi-National Companies (MNCs) should adjust their production and marketing operations to meet the local needs and tastes, and to become heavily involved in joint ventures and strategic alliances to take advantage of foreign markets. As well as creation of sub-markets typically within an enterprise is being practiced by the foreign firms inside the economic zones. Sub-contracting is itself an old market practice, but was usually outside the firm. It is now a standard practice for large companies to create competition among their constituent units.

Over time, the EPZ has fostered the development of a competent core of domestic firms that have progressively increased their capability to serve foreign markets under a number of production arrangements. This has been made possible by extensive cooperation between foreign and domestic firms. Under a number of arrangements, including sub-contracting, joint ventures and observation, domestic firms progressively learned production techniques, internalized elements of production, distribution and marketing processes that they use to upgrade their competitive position (FDI magazine, 2004).

One of the prospects of establishing EPZ is to provide possible backward and forward linkages between foreign zone firms and the local firms. It is believed that EPZ can stimulate the inflow of local raw materials, equipment, components and packaging material from the domestic sector, and can also provide impetus to subcontracting, thus encouraging the growth of supporting industries and ancillary services (FDI magazine, 2004). It is without doubt that, with the gradual shift towards more technologically-oriented productions in the SEZs of Cavite province, the amount of domestic linkage will increase. This will normally be achieved by subcontracting the production of parts and components to local firms, leaving the integration of the more advanced production lines to the foreign zone firms or locators.

For linkage to occur, the foreign firms inside the Cavite SEZs should use basic production processes, where domestic raw materials and intermediate inputs could be used. Likewise it is helpful to know and identify the profile of the zone enterprises or locators as well as the profile of the local entrepreneurs to determine if there has really been a linkage between the two actors: Cavite SEZs locators and the local entrepreneurs.

Neo-liberals tend to see the world in terms of market metaphors (Treanor, 2008). Referring to nations, cities and regions as companies is common nowadays. In neo-liberal regional policy, cities are selling themselves in a national and global marketplace of cities. They are considered equivalent to an entrepreneur selling a product, but the product is the decision of a city or a region as a location for entrepreneurs. Just like what happened in Cavite province, the province adopted the export-oriented industrialization strategy by establishing several SEZs that attracted foreign locators. The province became an entrepreneur selling the province to be a location for foreign investors.

Neo-liberals believe that greater economic and political interdependence will lead to progress and a reduction of international conflict. Greater international economic transactions create greater opportunities for cooperation among nations, governments and corporations and can eventually lead to a more peaceful world. Liberalism assumes that international economic interactions can be mutually beneficial or a positive-sum game (Watson, 2005). In a positive-sum game, all actors can gain together. There is mutual gain from exchange, in which everyone benefits. In the case of a successful EPZ foreign direct investment would be accompanied by technological transfer, knowledge spill-over and demonstration effects that would act as catalysts for domestic entrepreneurs to engage in production of non-traditional products. Cavite SEZs provided the physical location and infrastructure and acts as a matchmaker in bringing together the foreign firms and the local firms.

As for the foreign zone firms or locators, the net impact will be positive. These zone firms or locators will provide additional resources and capabilities to the local firms. Likewise, these zone firms or locators will also bring new management styles and a more active and dynamic and competitive practices by injecting entrepreneurship and work cultures to the locality.



Aside from these, the local firms and entrepreneurs will become more familiar with the global markets and market standards, to improve their products and productivity, and to become more competitive in the international trade.

In implementing this EOI strategy, there were five (5) actors involved in this study namely: the Local Government Unit; the Cavite SEZs; the SEZs Locators and the local firms. Liberalism assumes that international economic interactions can be mutually beneficial or a positive-sum game (Watson, 2005). In a positive- sum game, all actors can gain together.

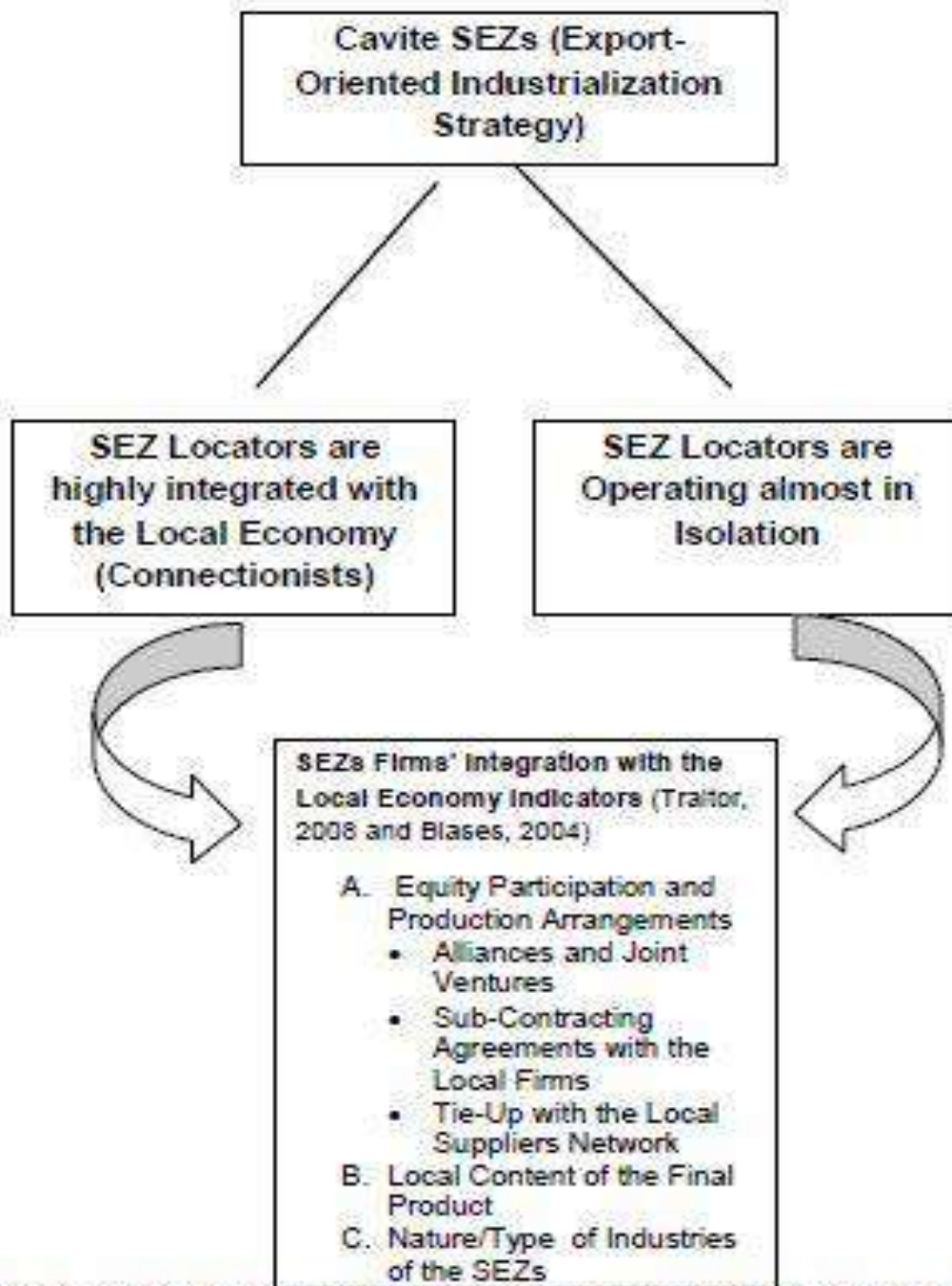


Figure 1: Theoretical Framework. Prepared by the author through literature review (adapted from Treason, 2008)

Figure 1 shows the theoretical framework of the study. As what the figure depicts, the presence of SEZs in Cavite reflected that the province has adopted the EOI strategy. Being an EOI strategy, these SEZs could increase the foreign investments to the province, thus contributing to the growth of the local economy. How can we say that these SEZs are contributing to the growth of the economy? If these SEZs are highly integrated with the local economy or these SEZs are operating almost in isolation. The SEZ firms or locators are highly integrated with the local economy if these SEZ firms are “*connectionists*” (Traitor, 2008).

To determine whether a certain SEZ is a connectionist, there are indicators to be considered: [a] the equity of participation and production arrangements (like alliances and joint ventures; sub-contract agreements with the local firms; tie-ups with the local suppliers’ network) between the SEZ firms and the local entrepreneur; [b] local content of the final product; [c] and the nature of the industries inside the SEZs (Treason, 2008; Baissac, 2004). The more integrated these EPZ firms with the local economy, the more EPZs opportunities are maximized.

It is important to know the profile of Cavite SEZs locators in order to know what type of foreign investments these Cavite SEZs locators have and to determine the internationalization motives of these locators. In that sense, the researcher was able to determine whether these Cavite SEZs locators made use of the services of the local if these SEZs are highly integrated with the local economy or these SEZs are operating almost in isolation. The SEZ firms or locators are highly integrated with the local economy entrepreneurs as their sub-contracts for the products that they produce or had any tie-ups with the local suppliers’ networks for the supply of raw materials needed in their manufacturing processes. Likewise, it is also worthwhile to know if these locators had alliances and joint ventures with the local entrepreneurs.

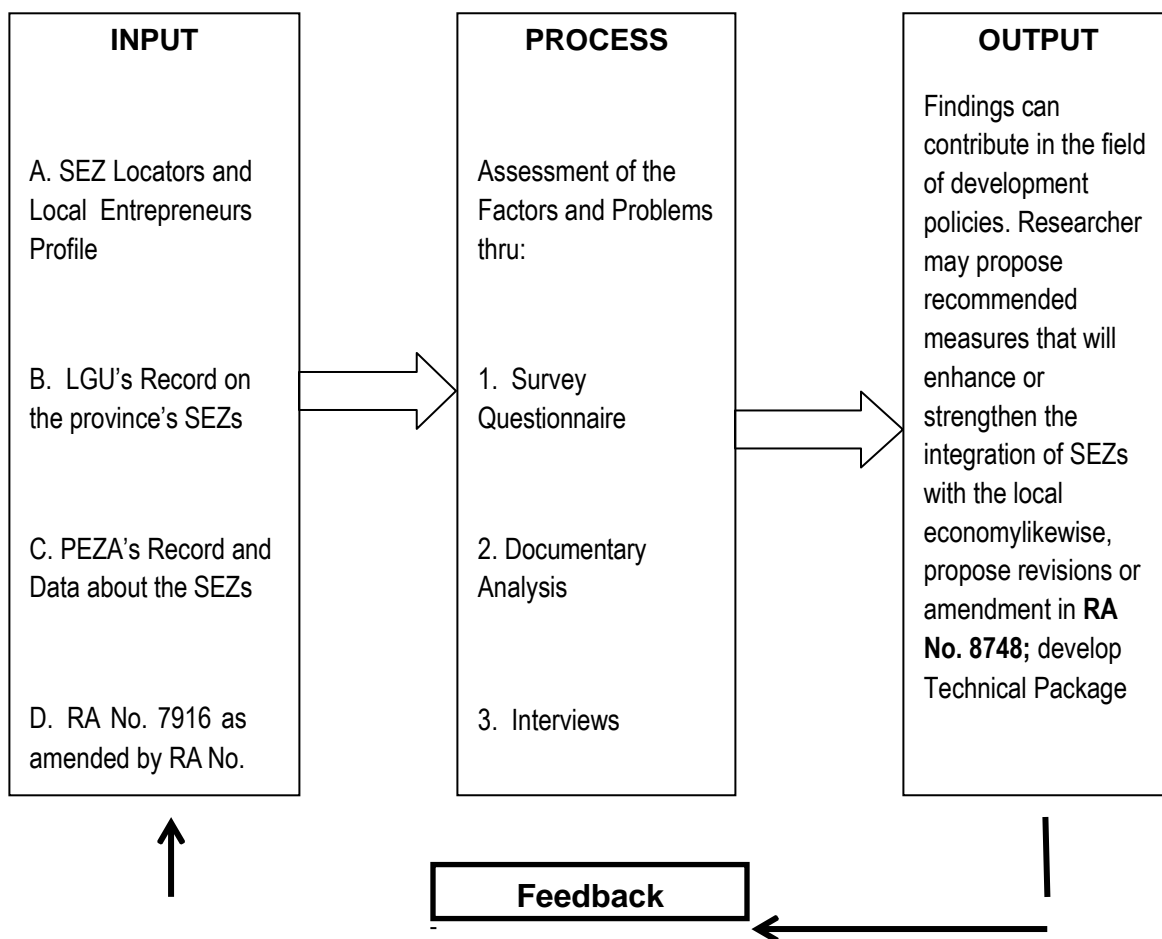
What happened to Cavite province when it decided to establish SEZs in the area was really a positive-sum game? In a positive-sum game, all actors can gain together (Watson, 2005). There is mutual gain from exchange, in which everyone benefits. The Cavite SEZs, the locators, the people in the area, the local entrepreneurs, as well as the whole country, all benefited from this EOI strategy.

Again, the researcher emphasized that the more integrated these SEZ firms with the local

economy, the more SEZ opportunities are maximized by the host community. In the case of the Cavite SEZs, it is worthwhile to know if the SEZ locators were highly integrated with the local economy or these SEZs is operating almost in isolation.

## 2. Conceptual Framework

Below is the conceptual framework or the blue print of the study.



**Figure 2: Conceptual Framework of the Study**

## 3. Results and Discussion

### 3.1 The Status of Integration of the Special Economic Zones with the Local Economy

With regard to the SEZs in the Province of Cavite, they are highly integrated with the local economy since all of the indicators or factors as stipulated in Tenors' work (2008) and

adapted by the researcher in her theoretical framework were satisfied except for one factor which is the use of raw materials in their manufacturing needs. It is obvious though that most locators inside the SEZs are PEZA registered. These PEZA registered locators were not that fully integrated with the local economy since most of their needed raw materials are not available in the locality. These PEZA registered locators still have to search for suppliers coming from other special economic zones outside Cavite province.

Although the factor or indicator, use of raw materials was not satisfied, other factors or indicators were fully utilized. SEZ locators avail of the services of the local entrepreneurs by having or offering contracting services. The following are the contracting services offered by the local entrepreneurs to the SEZ locators: a) shuttle bus or services; [b] delivery and service vans; [c] freight forwarder; [d] customs broker [e] trucks; [f] security guards; [g] janitorial and maintenance services; [h] concessionaires; [i] suppliers; [j] warehouse location and [k] contractors. These contracting services usually lasts from three (3) to twelve (12) months period, and may be renewed if the SEZ locator still wants the services of these contracting companies.

### **3.2 SEZs in Cavite to Generate Employment Opportunities to the Locals**

Having these SEZs around definitely created a positive effect on employment generation in the Province of Cavite.

### **3.3 The Proliferation of Local Businesses in the Host Communities as a Response to the Existence of SEZs in the Area**

The local entrepreneurs of the host communities were not able to optimize the benefits or opportunities that SEZs provide since they did not form joint ventures, subcontracting or tie-ups with the SEZ locators. The reasons for such were lack of knowledge and technological know-how, capabilities and capital.

Although findings showed that there was no substantive linkage or integration between SEZ locators and the local entrepreneurs of the host communities in terms of production arrangements and use of local raw materials, there is still a line linking the SEZ locators and the local entrepreneurs.

These local entrepreneurs offers contracting services to the SEZ locators like having these local entrepreneurs to provide shuttle bus or services; delivery and service vans to the SEZ

locators; serve as a freight forwarders and customs brokers for SEZ locators and accepting these local entrepreneurs as firms that provide security guards; janitorial; maintenance services and concessionaires; and building contractors. These local entrepreneurs even put-up small stores that cater to the basic needs of the employees of the SEZs. They had barbershop, computer shop, laundry shop, billiard and others to name a few.

### **3.4 The Role of the Local Government Unit in the Implementation of the Export-oriented Industrialization or the EOI Strategy by Establishing SEZs**

It is evident that the Province of Cavite is true to her objective which is to encourage local and foreign investors in the province. And the province was successful in doing this because the LGU has a very attractive incentive package and programs for the investors. According to the LGU, Cavite is for the investors.

### **3.5 Factors considered by the Locators before they establish Businesses inside the SEZs and the Problems encountered by the locators when they established their business inside the SEZ**

Locators considered the physical infrastructure, accessibility and incentives as very important for them in choosing the area where they will invest and have a business venture. Since most of them are PEZA registered locators, availability of raw materials are not that important to them.

Most of the locators inside the SEZs in Cavite are PEZA registered locators; the only problem they encountered was the availability of raw materials in the locality.

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