# ISAS Brief

**No. 203 – 17 June 2011**



469A Bukit Timah Road
#07-01, Tower Block, Singapore 259770
Tel: 6516 6179 / 6516 4239
Fax: 6776 7505 / 6314 5447
Email: isassec@nus.edu.sg
Website: www.isas.nus.edu.sg


## NMIZs in India: Haunted by SEZs?


**Amitendu Palit**[1]



### Abstract

*India's draft national manufacturing policy proposes National Manufacturing and Investment Zones (NMIZs) as instruments for revitalising manufacturing. The policy addresses major challenges for Indian manufacturing such as inflexible labour laws, multiple procedures and environment-friendly production. However, NMIZs pose several questions with respect to their relationship with Special Economic Zones (SEZs). Unless states are consulted actively, the paper argues, NMIZs might be as controversial as SEZs.*


### Introduction

The High Level Committee on manufacturing, chaired by Prime Minister Dr Manmohan Singh, recently gave its in-principle approval to the draft national manufacturing policy.[2] Prepared by the Department of Industrial Policy and Promotion (DIPP), the policy aims to raise the share of manufacturing in India's gross domestic product to 25 per cent by the year 2025, from what is 16 per cent at present. Ministerial consultations on the policy are expected to be completed within a month, following which it will be reviewed by the Cabinet and announced formally.

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1 Dr Amitendu Palit is Head (Development & Programmes) and Visiting Senior Research Fellow at the Institute of South Asian Studies (ISAS), an autonomous research institute at the National University of Singapore. He can be reached at isasap@nus.edu.sg. The views reflected in the paper are those of the author and not of the institute.

2 'PM Chairs High Level Committee on Manufacturing', *India's Prime Minister's Office* (9 June 2011), http://pmindia.nic.in/pressrel.htm. Accessed on 11 June 2011.

The change and dwells at length on how production in NMIZs will be encouraged to be 'green'. Considerable attention has also been devoted to inflexible provisions in India's different labour laws and the options available to manufacturers in NMIZs for overcoming these inflexibilities. The policy also highlight of the policy is its emphasis on NMIZs as principle instruments for enhancing manufacturing output and exports. The policy takes note of India's imperatives in tackling climate addresses two critical constraints of Indian manufacturing – shortage of skilled labour and complying with multiple procedures – and offers various suggestions for overcoming the constraints.

**What are NMIZs?**

A discussion paper prepared by the DIPP, which is the basis of the new manufacturing policy, explains NMIZs.[3] These are proposed to be dedicated areas devoted to manufacturing and will not only include industries producing manufactured items but also public utilities, logistics, residential complexes, environmental safeguards and other administrative services. Like SEZs, NMIZs will have distinct 'processing' and 'non-processing' segments; the former will house core production facilities backed by logistics and production-related infrastructure, while the latter will comprise of the institutional infrastructure such as residential, commercial and social facilities.

The policy expects the Central Government and state governments to meaningfully coordinate the development of NMIZs. The main responsibility of the Central Government, other than approving establishment of the zones, would be to connect them with external physical infrastructure facilities such as rail, road, seaports, airports and telecommunications. This will be done through appropriate public-private-partnerships (PPPs), wherever necessary. State governments, on the other hand, will be responsible for identifying and acquiring land, and ensuring supply of electricity, water, sewerage, state road connectivity, health facilities and safety measures. The governing authorities for NMIZs will be in the form of special purpose vehicles (SPVs)[4] with participations from developers, industry associations and the major manufacturers in zones. The SPVs will be responsible for preparing master plans for the zones, specification of land use, demarcation of processing and non-processing segments, identifying industries that can emerge in the zones, approving establishment of units within zones, planning and developing internal infrastructure and determining user charges for various facilities. The SPVs will also be responsible for

3 'National Manufacturing Policy: A Discussion Paper', *Department of Industrial Policy & Promotion (DIPP), Ministry of Commerce and Industry, Government of India*, www.dipp.nic.in/NMP_DiscussionPaper /NMP_DiscussionPaper_2010.pdf. Accessed on 11 June 2011.

4 SPVs are business associations of individuals or other legal entities formed with well-defined and specific objectives. Technically, these are companies as they have to abide with all regulations under the Companies Act, though within their specified focus. Promoting companies, while setting up SPVs, hive off chunks of their assets into SPVs de-linking these assets from the parent company. Thus prospects of the latter do not affect those of the former thereby making it simpler for SPVs to raise funds from investors.

choosing the developers for the zones and those developers can be either government, private agencies or PPPs.

## 'Green' Production, Labour Laws, Skills and Procedures

'Green' production is heavily emphasised in NMIZs with such production encouraged by specific fiscal incentives. Those fiscal incentives include cheap loans for investing in projects with green technologies, creating earmarked funds for supporting research on green manufacturing and investment subsidies for independent power plants in NMIZs using green technology. In addition to incentivising green manufacturing, the policy also contains suggestions for making labour absorption and retention in NMIZs a more flexible process. Several exemptions for NMIZ industries have been proposed under the Industrial Employment (Standing Orders) Act of 1946, the Industrial Disputes Act of 1947, the Employees State Insurance Act of 1948, the Factories Act of 1948 and the Payment of Gratuity Act of 1972. NMIZ enterprises have been proposed permanent 'public utility' status so that they are unaffected by production disruptions from unexpected strikes and lockouts. Subject to specific conditions, the Trade Union Act of 1956 and other laws relating to trade unions will be inapplicable to NMIZs.

The policy has tried to address the Indian manufacturers' demand for uninterrupted supply of skilled labour, by recommending establishment of training centres in NMIZs through PPPs with training curricula addressing specific needs of industries located in the zones. Training will focus on building three skill pools; an abundant pool of minimally trained workers, a sizeable body of well-trained personnel and a select group of highly specialised employees. In an attempt to reduce the significant transactions cost involved in obtaining multiple clearances and complying with various procedures, producers in NMIZs are proposed to benefit from 'single-window' clearance systems for both the Central Government and state government clearances.

## Unresolved Questions

The new manufacturing policy attempts to address some major challenges confronting industrial production in India. Over the years, these challenges – inflexible labour laws, multiple procedures, shortage of skilled labour and energy-inefficient carbon-intensive production – have assumed chronic proportions, casting serious doubts over manufacturing's ability to increase output in a cost-efficient and sustainable fashion. The proposed NMIZs are expected to do exactly this by providing manufacturers enabling environments comprising quality infrastructure, effective logistics and incentivising green production.

While objectives behind proposing NMIZs are laudable, they raise a few questions. First and foremost, with NMIZs coming up, what happens to SEZs? Five years ago, SEZs were launched with almost identical objectives. Now, 133 SEZs are functioning in India, including several manufacturing zones. [5] Many of these are focused on manufacturing. The question is will introduction of NMIZs lead to lesser roles of SEZs in India's industrial strategy?

The DIPP paper suggests NMIZs can include one or more SEZs. This 'inclusive' nature of NMIZs can create complications. For example, given a choice, where would industries prefer to be located – SEZs or NMIZs? Incentives are likely to influence the choice. By locating in SEZs, industries not only enjoy duty-free imports but are also exempt from paying income tax, central sales tax, service tax and other state taxes. 'Single-window' clearance facilities are also available to SEZs. In contrast, general incentives for NMIZ industries, such as tax exemption on expenditure incurred in obtaining international certification like the International Organization for Standards' ISO 9000, or subsiding expenditure on filing of patents, while useful, might fall well short of the fiscal largesse available to SEZ enterprises. This might create difficulties in incentivising industries to move to NMIZs, unless they are in SEZs within NMIZs.

A particular incentive proposed for NMIZ producers, distinct from SEZ industries, is the assurance of purchase preference in government procurements. While this could be encouraging for producers and draw industries to the zones, it might, in the long run, be incompatible with procurement rules of the World Trade Organization (WTO). WTO rules do not encourage discriminatory treatment for specific enterprises in government procurement.

Availability of land and issues surrounding its acquisition will remain in full public glare as NMIZs take shape. If NMIZs include SEZs – along with additional logistics, support services, and processing and non-processing segments – they can hardly be small in size. As in case of the bigger SEZs, land can be a critical factor in curbing expansion of NMIZs. Other than a handful states and private developers with large land banks, obtaining land for large NMIZs will be a daunting task for both government and private agencies. More so, given that the policy expects states to bear the initial funding of land through either low-cost loans from international agencies or by raising resources from the market through long-term tax free bonds with land as the security. Poor maintenance of land records for establishing title rights to property and India's relatively underdeveloped bond market make land a rather risky asset for issuing bonds against.

The SEZ experience underscores the importance of consulting states before implementing an industrial policy that depends heavily on active participation of states. India's SEZs could

[5] 'List of Operational SEZs of India', *Department of Commerce, Ministry of Commerce and Industry, Government of India*, www.sezindia.nic.in/writereaddata/pdf/ListofoperationalSEZs.pdf. Accessed on 15 June 2011.

have avoided much of the controversies they generated had the consultations between the Centre and states been deeper and wider. Success of NMIZs will depend upon how far the states have been consulted on the policy and to what extent they are keen on pursuing it. Hopefully the ongoing consultations on the policy will involve states as well. Otherwise, NMIZs might become as despised as SEZs and can be assumed by most as ‘land grab’ efforts by greedy real estate developers, as opposed to being virtuous vehicles for industrial growth.

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