Palestine Economic Policy Research Institute (MAS)

Background Paper

Roundtable (5)

Palestinian Industrial Estates and Free Zones: Investment Attraction

Author
Nasr Etyani

2018

Background and Rational

An *Industrial Estate* is a tract of land developed and sub-divided into industrial plots according to a comprehensive plan, with provision for infrastructure (public utilities of water, electricity, sanitation services, roads and transport, and telecommunications) with or without ready built-up factories for the use of a community of industrialists (UNIDO, 1997). An *industrial free zone* is "a geographically defined area… assigned to service one or more beneficiaries for export related activities having special customs and tax provisions guaranteed by this law" (Law on PIEFZA of 1998).

Industrial estates and free zones (IEFZs) are an essential determinant of economic development worldwide, considering their significant contribution to GDP, employment, exports, and other macroeconomic indicators. In Turkey for example, like many other countries, IEFZs have been a real lever for economic growth. Their number rose from 12 in 1980 to 120 in 2009 with an operating capacity of more than 880,000 workers. In Thailand, there were 27 large industrial estates and zones with investment worth of USD 21 billion, while in Vietnam there were 71, employing 22% of the workforce (MAS, 2013).

There are three main drivers for establishing IEFZs.[1] First, the developmental driver aims to develop and improve manufacturing industries in a specific area. Second, the promotional driver aims to encourage the creation of new industries, and the development of existing ones, and enhancing synergies between industrial enterprises by strengthening backward linkages of existing industries with new industries. Third, the organizational driver aims to gather dispersed industries through the provision of industrial sites for businesses facing expansion difficulties, or through the organization of industrial projects, especially small and medium industrial enterprises, and guiding IEFZs to settle in lands with suitable topographic and geographical assets. This is important, because separating industrial clusters from residential areas will reduce their ecological impact and maximize utilization of land use. Therefore, industrial enterprises are encouraged to move from cities and residential areas to industrial estates and zones supported with industrial-level facilities and services, which also helps to avoid traffic jams (MAS, 2013). An example of a haphazard and dispersed industrial zone in Palestine is the Ramallah and Al-Bireh Industrial Zone.

There is an assortment of incentives and privileges granted by the law to projects involved in IEFZs, depending on the nature, type, purpose, and geographical location of the IEFZs. According to UNIDO Handbook (UNIDO, 1997) incentives that IEFZs projects could benefit from include:

- Relatively low rental fees for built-up industrial establishments and for using the lands;
- Subsidies for infrastructure services (water, electricity, telecommunications, and other facilities and services);
- Establishment of a one-stop shop to facilitate licensing procedures and other paper work;
- Tax exemptions on imports and exports as well as other taxes, such as income tax, or provision of governmental aid (this applies to Industrial boarder and free zones) (World Bank, 2009).

Since its establishment in 1994, the Palestinian National Authority (PNA) has been keen on planning for and establishing industrial estates and free zones. In 1996, the PNA designated a specialized department within the (then) Ministry of Industry, to follow up on the industrial estates and zones program. Later in 1998, the department was transformed into the Palestinian Industrial Estates & Free Zones Authority (PIEFZA), an independent governmental organization responsible for fostering IEFZs through attracting foreign and domestic investments. During the same year, the PNA issued Law No. 15 of 1998 on Free Industrial Estates and Free Zones, in addition to a package of economic legislation, most importantly, the Investment Encouragement Law, the Securities Law and the Tax Law, aspiring

[1] Industrial zones should be differentiated from industrial estates. The former are usually unplanned industrial clusters coming without a comprehensive development plan. They are merely a tract of land earmarked by the local authority for clustering industrial projects in one site, which means prohibiting establishing industrial projects outside that site. What distinguishes industrial estates is that they are established according to a comprehensive plan set in advance, which encompasses economic, social and environmental and urban roles and aspects of the industrial estates. For example, this definition does not apply on Ramallah and Al Bireh industrial zone (MAS, 2013).

to boost investment in Palestine in general, and in IEFZs in particular (Makhoul and Etyani, 2004). These efforts culminated in the establishment of several industrial estates with the support of donor countries and international organizations. These include: Gaza Industrial Estate, Jericho Agro Industrial Park, Jenin Industrial Free Zone, Bethlehem Industrial Estate, in addition to Tarqumiya Industrial Zone, which is still under construction.

This background paper was prepared as a discussion note for the fifth roundtable session within MAS's Annual Roundtable Program, which aims to discuss topical issues relevant to economic and socioeconomic policy-making. In this context, the paper discusses if IEFZs have been successful or not in attracting investment, in addition to touching upon investment incentives and public policies pertinent to IEFZs.

A Preview of Existing IEFZs

This section presents statistical data on IEFZs, based on information the author of the paper had access to during the time he served as Director of Industrial Estates. These statistics include figures on existing enterprises only, and exclude enterprises that are not in operation yet. Therefore, it is worth noting that the discrepancy between figures cited in the paper and PIEFZA's figures is ascribed to the fact that the latter takes into account existing enterprises and those that have completed/are about to complete legal registration procedures.[2]

1. Gaza Industrial Estate (GIE)

GIE is the first industrial estate established in Palestine. It was built in 1997, and started operating in 1999. The estate enjoys a strategic location being close to airports, ports, and crossing points. It is located 3 km north of Gaza city. Facilities and utilities in the area include: banking services, customs clearance, freight and shipping, and infrastructure services, as well as a central electricity station in addition to the national grid. GIE's total area covers 50 hectares (500 dunums), 66% of which are designated for industrial uses, 30% for roads and green spaces, while the remaining 4% constitute water tanks and wastewater pumps. GIE targeted most of Palestinian industries, including food, plastic, metal, clothing, textiles and other industries. By the end of 2017, the number of operating factories was around 26. Some 700 workers are employed by the GIE, however, its full labor capacity is expected to reach 1500. According to PIEFZA's data, its total investments, after aid and grants, reached about USD 168 million.

Regarding the types of leasing offered in GIE, they are either:

1- Industrial buildings ready for rent (hangars), for USD 26 per square meter per annum; or,
2- Open lots with the provision of infrastructure services (public utilities, water supply, electricity, sanitation services, roads and transportation, and telecommunications, etc.), rented for USD 8 per square meter per annum.

2. Jenin Industrial Free Zone (JIFZ)

JIFZ is located north of the city center, about 1.6 km west of road 60, on the boarders between the West Bank and Israel.

The total area of JIFZ is 95 hectares (950 dunums), 68.6 hectares of which are used by industrial and commercial enterprises, while the remaining lands are allocated for roads, parking lots, storehouses, in addition to green spaces.

The project was launched in 1996 to create new jobs, absorb increasing numbers of the workforce in the northern West Bank governorates, reduce Palestinian dependence on Israeli labor market and attract domestic and foreign investments. JIFZ targeted all industrial activities and sectors, including agriculture, food and hi-tech.

[2] Refer to Table (1) in the paper appendix, summarizing main indicators of IEFZs

The German government was highly interested in JIFZ, and has taken upon itself the provision of the external infrastructure in the area. In addition, the Turkish government supported the project by allocating USD 12 million for the acquisition and preparation of land for leasing. The concession of running and developing the internal infrastructure of JIFZ was granted to a Turkish company (TOBB-BIS). Investments in the industrial zone, including internal and external infrastructure, is expected to reach USD 74 million. There are also two types of leasing in the zone: industrial buildings ready for rent (hangars) and open lots providing infrastructure services. Although it has been two decades now since the start of work, JIFZ is expected to start operation by 2020.

3. Jericho Argo- Industrial Park (JAIP)

JAIP was part of the Japanese government's initiative in 2006 "the Corridor for Peace and Prosperity", which responds to the Palestinian development vision envisaged for Jericho and the Jordan valley. In 2012, the PNA, represented by PIEFZA, signed a concession contract with Jericho Agro-Industrial Park Company, to launch work on the industrial park's internal infrastructure. JAIP company implemented this step, in collaboration with PIEFZA and Japan International Cooperation Agency (JICA), which culminated in putting the Park into operation by 2014.

JAIP is located north-east of Jericho, 4km from the city center, 900m from road 90 connecting northern Palestine to the south. The Park has an area of 61.5 hectares (615 dunums). In the first phase of the implementation (at that point covering 14 hectares/140 dunums), the Park targeted agro industries and related activities. However, in phase II (covering 48.5 hectares/ 485 dunums) the Park was open to all industrial activities and types of investments. JAIP offers the same leasing options as in JIFZ and GIE.

Since start of Phase II, 10 hectares (100 dunums) were paved and prepared. Currently, PIEFZA is handing the Park over to the developer company. By the end of the second quarter 2018, the number of operating factories and companies in the Park reached 15, yet, about 50 more factories are expected to become operational by the end of 2018. In addition, the Japanese government has donated USD 4 million to fund the establishment of an industrial training center in JAIP. In addition, it has collaborated with the developer to build a solar energy system on the roofs of the industrial buildings and hangars at an estimated cost of about USD 5 million.

4. Bethlehem Industrial Estate –BIE

BIE is located in Hindaza- Bred'a village, 10 km from Bethlehem's city center.

The French government supported establishing BIE following the signing of the French-Palestinian protocol in 2008 between the State of Palestine and the French Republic. BIE was established on an area of 19.5 hectares (195 dunums) and targeted small and medium industries. PIEFZA has contracted a Palestinian-French developer to develop the infrastructure of the estate. The project will be built in three phases, the first phase covers rehabilitating around 53 dunums, the second covers 40 dunums, and in the third phase, an industrial training center will be built on 16 dunums.

The estate is designed to accommodate 23 operating factories by the end of Phase I, which are expected to employ 350-400 workers, yet the number of operating factories currently is only 10. When finished, the estate is expected to create 1500 direct job opportunities, while the number of operational factories will reach around 60.

BIE offers one type of leasing, which is open lots with infrastructure services for USD 8 per square meter per annum. Total investment in BIE is estimated at USD 50 million, including aid and grants from the French government and funds allocated for the rehabilitation of external and internal infrastructure, in addition to factories and investments inside the estate's lands.

The Government's Policies

There are several factors that impact IEFZs achieving their objectives, most importantly: an attractive investment environment, a legal and legislative framework regulating the business and various economic activities, especially industrial activities, in addition to services and incentives offered to investors, whether local or foreign (Makhol, 1998 and Al-Siraj, 2003). In this context, the Palestinian government has established a number of policies and incentives as follows:

Public Policies pertinent to Industrial Estates (Investment Incentives)
The Law No. 10 of 1998 on Industrial Estates and Industrial Free Zones, identified incentives granted to industrial establishments in IEFZs, as follows:

Article (38): custom duties exemption: All goods, materials, machinery and vehicles imported from abroad into the industrial free zone with the purpose of using them inside its boundaries or in any of its industrial projects, shall be exempted from customs duties, other custom-related duties and import licenses.

Article (39): exemption of supplied goods: Local goods and products supplied to the industrial free zone from any Palestinian city shall be exempted from applicable taxes or duties.

Article (40): **exemption of IEFZs exported goods:** All goods and products manufactured in the industrial free zones exported abroad shall not be subject to terms and legal procedures applied on Palestinian exports, or to export taxes and any other applicable taxes.

Article (47): Income Tax: Licensed projects, manufacturing projects, or developers' works shall be subject to income tax as specified in this law or any other law, whichever serves the best interest of these projects.

Council of Ministers' Decision No. (8) of 2017 on the regulation of incentive package contract to encourage investments within Industrial Estates and Free Zones, as follows:

Article (4) Project Incentives: Projects registered at the Palestinian Investment Promotion Agency (PIPA) shall be granted privileges of the additional Incentive Package Contract stipulated in this law as follows:

1. The tax reduction incentive granted by the Law for five years is extended up to an additional three years; for new projects or for expansion or development of an existing project that has not benefited from the grants program prior to registration, and within approved areas.

2. For projects benefiting from the Law incentives, which are moving to an area within the approved areas and have not benefited from the grants programs prior to moving, the tax reduction incentive granted by the Law is extended for an additional three years for the same tax bracket within which projects are listed in at the time of operation after moving.;
3. The tax reduction incentive granted by the Law for five years is extended up to an additional three years for new projects or for developing an existing project that has benefited from the grant programs prior to registration, and which are implemented within the approved areas.

Article (5) Financial Institutions' Incentives: Soft loans, granted by financial institutions and banks to finance projects within the approved areas, shall be subject to same regulations applied on loans granted to Small and Medium-Sized Enterprises (SMEs) as stipulated in Income Tax Law and its regulations.

According to Article (2) in the Decision of the Council of Ministers, eligibility requirements to benefit from the incentives are that they should:

1. Be licensed by the competent authorities;
2. Comply with all terms stipulated in the Law, as well as regulations and instructions issued in relation to the law; and

3. Maintain the minimum number of employees during the benefit period. The Board of Directors shall issue the instructions in regards to the number of employees and their fields of specialty.

In addition, it is important to take into consideration the specificity of the Palestine, being under occupation, which, unlike neighboring countries, lacks sovereignty over its territory, added to which the political and economic instability and the high degree of dependence on the Israeli economy. Such a challenging environment requires devising special incentives that can aid in confronting these impediments. However, investment incentives granted to Palestinian industrial zones by the law, fall behind those applied in other countries. For example, investment incentives in Turkey include:

- Establishments that consume less than 1,000 kW are exempted from electricity connection fees and costs of installing meters.
- 100% VAT exemption until 2015.
- 100% telecommunications tax exemption until 2015.
- 15% discount on prices of real estate for industrial uses.
- 50% contribution to R&D expenditures.
- 50% contribution to pollution treatment costs.
- 30% contribution to costs of human resource development and training.

In Thailand investment incentives include:

- Discount on import taxes on raw materials and machinery.
- Discount on commercial trademark and patents for five years.
- Up to 90% discount on sales tax for tenant establishments in industrial estates for a maximum of five years.
- 10% discount on electricity fees for five years since the start of operation.

In conclusion

Clearly, the PNA has undertaken intensive efforts to establish IEFZs, which have culminated in drafting and enacting of laws, investment incentives and public policies. Work is still ongoing, which is evident by the lately-established Tarqumiya industrial zone in Hebron. As mentioned, the basic objectives for establishing IEFZs (namely developmental, promotional, and eliminating dispersed industrial clusters within residential areas), aspire to achieving national development goals through a set of policies, facilities and investment incentives.

The paper has shown how the legal incentives provided for in the Palestinian laws for estates and free zones are behind those applied in other countries that have exhibited a successful model of economic growth. However, the current operational and projected capacity of these estates and zones indicate that IEFZs have not been successful in attracting industrial sectors away from residential areas and clustering those industries in industrial estates and zones, which have negatively impacted the realization of economic and development goals.

Based on the above, the following set of questions and pillars are pertinent:

- Have industrial estates and free zones succeeded in achieving their development objectives of boosting industrial activity and promoting exports tangibly?
- Have adequate investment incentives and facilities been employed? Can we consider the current performance of industrial estates and zones, in terms of attracting investments, satisfactory?
- While new and recently established industrial estates and zones are being developed, the infrastructure and the regulation of old industrial zones (like those in Hebron) are being neglected, which gives rise to the question: What about the future of these areas? Are there any plans to move these areas? Or, what is the position of decision-makers?
- Have the first and second implementation phases of industrial estates and zones been completed successfully as planned? What obstacles and impediments have they faced?
- Does the private sector consider investing in industrial estates and free zones feasible or not? Why?

References:

- فلاح، بلال، وأبو هنطش: دراسة استكشافية لنقل الصناعات في محافظة رام الله والبيرة من المناطق الحالية الى مناطق صناعية جديدة. معهد أبحاث السياسات الاقتصادية الفلسطيني- ماس- رام الله، فلسطين.2013
- السراج، يحيى. منطقة غزه الصناعية: تقييم مرحلي. سلسلة تقارير الأبحاث رقم 14. مركز تطوير القطاع الخاص. نابلس، فلسطين. 2003.
- صالح، حس. مدخل الى جغرافية الصناعة. الطبعة الاولى. دار الشروق للنشر والتوزيع. عمان، الأردن. 1985.
- عبد الرحمن، عبد الله. التنمية الصناعية في العالم الثالث: دراسة ميدانية على منطقة الرسيل الصناعية سلطنة عمان. مجلة العلوم الاجتماعية- العدد الثالث. 1994.
- مكحول، باسم. المناطق الصناعية الفلسطينية ودورها المتوقع في التشغيل. ورقة مقدمة الى المؤتمر الدولي للتشغيل في فلسطين- أوراق العمل الكاملة، المجلد الثاني. وزارة العمل. رام الله، فلسطين. 1998.
- مكحول، باسم، وعطياني، نصر. هيكل التكاليف واقتصاديات الحجم في الصناعات الفلسطينية وأثرهما على القدرة التنافسية. معهد أبحاث السياسات الاقتصادية الفلسطيني- ماس. رام الله، فلسطين. 2004.
- وزارة التخطيط الفلسطينية. خطة التنمية متوسطة المدى 2005- 2007. رام الله، فلسطين. 2005.
- الهيئة العامة للمدن الصناعية والمناطق الصناعية الحرَّة. رام الله- فلسطين. بيانات غير منشورة. 2018.
- United Nations Industrial Development Organization- UNIDO. Industrial Estates: Principles & Practice. Vienna.1997.

Appendix (1): IEFZs Main Indicators

Estate/Free Zone	Investments USD Million	Purpose / type	Size	Labor size (currently)	Leased Areas	Rent Fees per square meter annually	Start of Operation
JAIP	80	Agro-industrial	615	600	140	Open lots: 9 Hangars: 17	2014
GIE	186	industrial	500	700	85	Open lots: 8 Hangars: 26	1999
BIE	50	Hi-tech agro food industries	195	350-400	53	Open lots: 6	2013
JIFZ	40	Multiple industries	902	---	---	---	2020

Source: PIEFZ and developer companies, 2018.