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A Tale of Two Free Zones

Learning from Africa's Success

Greg Mills

Strengthening Africa's economic performance

THE BRENTHURST FOUNDATION

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Dr Greg Mills heads the Johannesburg-based Brenthurst Foundation, established in 2005 by the Oppenheimer family to strengthen African economic performance. He holds degrees from the Universities of Cape Town and Lancaster, and was the National Director of the SA Institute of International Affairs from 1996 to 2005. He has directed numerous reform projects in more than a dozen African governments (including in 2017 for example with the governments of Ghana, Lagos State, the five states of SE Nigeria, Lesotho and Mozambique), sat on the Danish Africa Commission and on the African Development Bank's high-level panel on fragile states, and has served four deployments to Afghanistan with NATO. A member of the advisory board of the Royal United Services Institute, he is the author, *inter alia*, of the best-selling books *Why Africa is Poor*, *Africa's Third Liberation* (with Dr Jeffrey Herbst), *Making Africa Work* (with President Olusegun Obasanjo, Dr Herbst and Major-General Dickie Davis), and most recently *Democracy Works* (with President Obasanjo, Dr Herbst and Tendai Biti).

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Executive Summary

Africa's population is projected to double over the next generation to more than two billion people. Free trade zones offer some possibilities for the continent's governments to create the jobs necessary to meet the aspirations of their youthful populations. Success is not only dependent on cheap labour, though this helps. To ensure these zones are more than just sweatshops, Ethiopia and Morocco show that the full package of policy aspects has to be addressed, including: political stability, free trade deals, logistics to and through ports, integrated value chains, and tax and other incentives. Crucially, if countries are to quickly move up the industrial ladder enabling higher incomes, then improving skills is a crucial component.

As Africa's population doubles over the next generation to more than two billion people, might industrial parks – free trade zones by another name – offer some answer to the jobs necessary? Ethiopia and Morocco, where Greg Mills has been researching the subject, offer some pointers.

Ethiopia's Industrial Parks: Hard Yards, But What's the Alternative?

Hawassa. Some 270 kilometres south of Addis Ababa, the picturesque Rift Valley city has relied on agriculture as source of income and employment, the regional Sidama coffee one of Ethiopia's best-known brands, and the name of the local football side.

Above and below: Without the park, Hawassa's income depends on coffee and some tourism.

That was until the establishment of the Hawassa Industrial Park (HIP), inaugurated by then Prime Minister Hailemariam Desalegn in June 2017. Flanked by Lake Hawassa, HIP is the largest government industrial park, built at a cost of US$250 million in just nine months by the contractor, the Chinese Civil Engineering Construction Corporation (CCECC). The first phase covers 140 hectares with 52 factory sheds, housing 20 textile and apparel firms from 11 countries.

By the start of 2019 Hawassa's factories employed 23 000 local workers and 700 expats. Though it was not the first, other government industrial parks are today modelled on Hawassa, which itself incorporated lessons from the first park at Bole Lemi in Addis. Five of 11 government parks are to date in operation (with six due to be inaugurated in the next six months) and two of four privately-owned examples. Together the five operational government industrial parks host 36 companies, providing 45 000 jobs that did not, ten years before, exist. A town of 350 000, Hawassa's GDP has alone increased four-fold in just two years.

The parks have been Ethiopia's response to the challenge of unemployment and the need for economic diversification. 'I assigned a team led by Dr Arkebe [Oqubay]' – now the chairman of the Ethiopian Industrial Parks Corporation (EIPC), recalls Hailemariam. 'We made a study of the successes and failures of industrial parks around

The Industrial Park has driven Hawassa's GDP up four times in just two years.

the world, looking at Nigeria, Mauritius, Taiwan, Vietnam, Singapore, South Korea, and of course to China. Nigeria, we concluded, failed because of a lack of leadership, and that it was unsupported by the state beyond giving the developers land. Mauritius, which was a success, emphasised the value of location, logistics, clear policy and organisational structure. We also wanted to avoid the situation that Vietnam found itself in, with 30 per cent of its sheds unoccupied.'

'People,' observes the former PM, 'think that an industrial park is just building sheds and providing infrastructure, but rather it's all about the regulatory and policy environment, the provision of one-stop facilities, clarity and efficiency on customs, labour law and visas, relations with local government.'

'It's all about setting up a system,' he says, 'not just a shed.'

Hawassa was selected as a site, given the large local labour reservoir of some 5–6 million. But while it is the prototype government park, it was not the first.

The first: The Eastern Industry Zone, south of Addis Ababa.

Thirty kilometres south of Addis is the Eastern Industry Zone, built by a Chinese investor out of the profits of his original cement plant established 15 years earlier on the site. Today it hosts 98 (mostly Chinese) enterprises, employing 14 500 Ethiopians and 1 100 Chinese. Originally focused on industries aiming at import substitution, today 80 per cent of production is destined for the export market. The most famous of these is the Huajian shoe-factory.

Started by a retired soldier, Zhang Huarong, from a home workshop in China with three sewing machines and ten workers in 1984, within two decades the business had expanded to 23 000 employees in giant factories in Dongguan and Ganzhou.

In a 'third stage' of expansion, his factory in EIP, near Bishiftu, opened in 2012. Employing 2 000 locals, it produces an average of 4 000 shoes daily, including a line for Ivanka Trump. All are destined for export.

The reason for firms setting up in Ethiopia are clear: A package of incentives (including duty free imports of capital equipment, and tax exemptions of up to seven years) combined with cheap electricity at US0.04c kw/h, cheap rentals, duty-free access to the US market through the African Growth and Opportunity Act (especially important for the apparel sector), one-stop services in each facility, including customs and permits, and plentiful labour at cheap rates. Of the 36 operational factories in the government parks, seven are in textiles, two in shoes and gloves, and the remainder in apparel manufacture.

Ethiopia offers, additionally, some value chain advantages to manufacturers. Huajian for example uses only Ethiopian leather on its shoe uppers. The Horn of Africa country is Africa's largest livestock producer. And as much as 2.6 million hectares is suitable for cotton production.[1]

Salaries are the key arbitrage, at least until infrastructure improves. Huajian's show factory in the Eastern Industry Zone.

But it's labour that is the notable advantage. The average salary at Huajian is 900Bir, or US$30; while workers start at just 750Bir in Hawassa. The top end is 3 000Bir. 'Our strategic advantage,' reflects Hailemariam, 'is low labour cost. That requires free movement of labour and continued education to remain competitive' he notes.

Sue Dong Linpei has been a manager of the Eastern Industry Zone for three years. 'We are here because of the size of the local market originally when we were focused on import substitution, and we stay because of comparative political stability, stable electricity and water, security, and the cost of labour. We learnt in China of the importance of industriousness and efficiency, and less positively of the need for environmental management.' She sees the same qualities in Ethiopians. Even though changing labour's attitude from an agrarian to an industrial workforce is a constant challenge, 'I reckon that labour efficiency is about 80% of what we have now in China' she notes. She is disdainful of unions. 'Unions are only here to push at problems,' she claims, 'not to solve them'.

The government's incentive packages and one-stop facilities are handled by the Ethiopian Investment Commission (EIC). Its outgoing director, Ato Fitsum, was formerly the Chief of Staff in Prime Minister Abiy's office. 'Our role is to provide the incentive packages and one-stop facility, which integrates 28 different services under one roof in each park.' He judges their success in part by the conversion rate between company registration and those that ultimately became operational. It has quickly improved from 60 per cent to nearly 100 per cent, with just one company failing to convert in the last few years. A further metric is in the time for imports, which has reduced from four years to four months for capital equipment. 'Our role,' he summarises, 'is to regulate, facilitate, trouble-shoot, and hand-hold.'

Addis' tortuous traffic hints at one of the major problems faced by the parks – logistics. The export route from Hawassa to the port of Djibouti can take five days. The building of new roads will help, as will integration with the Chinese-constructed Standard Gauge Railway (SGR). Also, additional port options through Berbera in Somaliland (which is being refurbished by Dubai) and, with the recent improvement in relations with Eritrea, Massawa on the Red Sea, should also help to bring down costs.

Early challenges include the difficulty, says Lelise Neme Sori, the CEO of the IPDC, of integrating government services such as water and electricity. 'When we were moving at a much greater pace, there were,' she notes, 'some 55 government stakeholders alone to be aligned.' Today's challenges centre on the provision of local accommodation for the sudden influx of workers, the deleterious effects of regional (ethnic) job reservation and its impacts on competitiveness, local policing inefficiency and occasional strikes over what business sees as 'minor issues'.

The contrast of toll roads and horsepower. Ethiopia ranks 91st out of 160 countries in the World Bank's rankings on logistics.[2]

There are other challenges, unrelated to operational conditions, but rather the fiscal burden on government of establishing the parks. Hawassa and others were financed through a US$780 million Sheba bond; the two most recent parks (the Bole Lemi expansion and that at Kilinto) by US$250 million in World Bank concessional funding. The 756km, US$3,4 billion SGR was funded 70:30 by a Chinese Exim Bank loan and the Ethiopian government respectively, which is hoping to extend the term of repayment from 15 to 25 years and to soften the commercial terms.

As Ato Fitsum remarks, 'We have come to terms with the fact that government cannot create jobs, and that the private sector must. The government can only create the enabling environment.' Hailemariam says that it was always the intention that government offered a catalyst for others to follow, and that the Eastern Industry Zone is the model to follow in the future now that the export manufacturing sector is established. 'Government had to be the pioneer,' he observes, 'as the private sector wanted to de-risk their investment. We could not afford failures or ghost parks'.

China's FDI stock in Ethiopia totals at least US$200 million this century.[3]

Such costs have complicated Ethiopia's fiscal challenges, which are underscored by a low tax to GDP ratio of just 13 per cent[4], about half of where it should be, and have led to a periodic shortage of forex, not least hampering the inputs for some export businesses. Floating the exchange rate will help, as will offloading some State-Owned Corporations, including the industrial parks themselves.

My 17-year old daughter was horrified at the low cost of labour when I explained the route that Ethiopia has embarked on to meet the annual inflow of 500 000 new job seekers including 100 000 university graduates into the market. 'How can they live on that?'

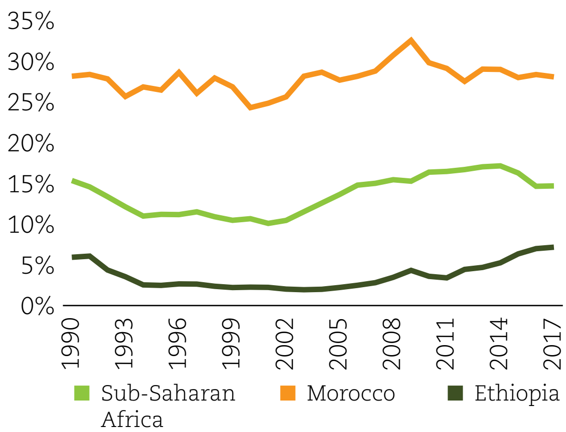
'We don't really have an option' says Hailemariam. 'There is no one silver bullet. Tourism offers some possibilities.' There is plenty of upside in this sector: Ethiopia only receives one million visitors annually. 'But one bullet and, like Kenya has learned, and they are gone' he warns. 'Together with agriculture, and agro-industry, manufacturing will provide the bedrock of what we are trying to build.'

Or as Ato Fitsum has noted. 'We are criticised for taking the route of apparel and textiles, given the threat of modernisation. But we still believe that labour intensive industries are a special route and option for Ethiopia given that our labour rates are much lower, unlike those African countries where, for instance, commodities drive up wages. We also need to leverage our demography, while there are huge outsourcing possibilities created too as a result, such as in IT.'

Overall the strategy is delivering growth, even though the breakneck pace of infrastructure investment is causing debt, balance of payments and exchange rate issues. With growth and rising incomes, the political challenge of inequality will also perhaps inevitably arise. Combined with the country's ethnic and political mix, this could be an explosive combination, fears about which have contributed to Prime Minister Abiy Ahmed's far-reaching reforms since he came into power in April 2018. The short-term imperative, however, apart from dealing with the fiscal and monetary aspects, is to ensure competitiveness and growth, not just through low labour costs, but to lower logistical costs and quickly move up the value chain into export sectors other than apparel.

	Ethiopia	Morocco
Population (million)	105	37.7
GDP per capita (real US$, 2017)	549.85	3 292.45
GDP growth % 2009–2017	10	3.7
Literacy % (adults, 15+)	39	69.4
Life expectancy	65.5	75.8

GDP per capita as % of world GDP per capita



The impressive bit about Ethiopia is the extent to which, whatever the concerns of privilege, the economic policy options have been thought through and acted on. Political stability cannot, the government acknowledges, be sustained without economic delivery. Such is the virtuous cycle of investment, democracy, people, jobs and growth.

Tangier: Marching to a Different Beat

Casablanca is just a four-hour flight from Lagos. But it's a world away.

Instead of paralysing traffic, we move quickly on a multi-lane highway towards Rabat, not a pothole in sight. Instead of sprawling tin and wooden slums the expressway is dotted with cranes atop new multi-story housing settlements stretching out toward the horizon. Instead of clusters of yellow Lagosian *danfo* taxis clustered at informal stops hindering the flow, Morocco's roadside amenities and its *péage* would not be out of place in Europe; neither Casablanca's surly immigration officers.

As you leave the city, instead of bush and mounds of garbage, there are ploughed fields, acres of which are under a different sort of plastic, greenhouses producing for Europe's tables just 14kms away across the Gibraltar Strait from Tangier. For a while the 350km road from Casablanca to Tangier hugs the TGV rail-line opened in November 2018 after ten years of planning and construction, cutting the journey to a fuss-free two hours.

Morocco's US$2 billion TGV – Al Boraq – was financed by loans of a billion dollars from France, and another half-billion from the Gulf states.

Traditions remain. Women in *jellaba* and men in Obi-Wan Kenobi-style pointy-hatted *amama* tend sheep on the verges of the motorway. And neither is it perfect. Poverty levels remain high in the rural areas. Four million of Morocco's 36 million today live near or in poverty, three-quarters of them in the rural areas.

Tangier is at the epicentre of this merging of European modernity and Berber tradition, which has so far worked to Morocco's advantage, the economy touching 5 per cent growth for nearly 15 years, driven by foreign investors and they, in turn, by a carefully-sweated combination of policy, stability and infrastructure.

Tangier's modernisation has hinged around the development of a new port, known as Tangier Med, three 'free zones' (the original Tangier Free Zone opened in 2000, Renault Tangier Med, and Tangier Automotive City), and two industrial parks at Tetouan. With US$8 billion in investment to date, together these employ 80 000 with US$7 billion in turnover, making this the largest free zone in Africa.

To these developments has been added a 45 000-seat sports stadium in the centre of the city, an expanded new business district, and renovated tourist infrastructure.

Tangier Med is connected to the city by a brand new expressway.

Once famed for its tangerine production, today Tangier is better known for its sweet Renaults. In 2018 the Kingdom produced 430 000 passenger vehicles, second only on the continent to South Africa, which produced 600 000. Nearly all are exported to Europe from Tangier Med. The 300-hectare Tangier plant employed 6 700 workers and produced 318 600 cars in 2018, making it the third-largest Renault plant worldwide. With a significant onsite government training centre, great pride is taken in the upskilling of the workforce.

Peugeot too will soon open a factory in the free zone in Kenitra, with a capacity of 300 000 units per annum and 200 000 drive-trains. But the value also comes from the associated automotive component manufacturers, including the likes of Magnetti Marelli, Federal Mogul, Hands and Valeo. None are household names, but nine of the largest 15 auto parts firms worldwide are represented in Tangier.

Morocco is leveraging its main comparative advantages: location, stability and wages. The minimum wage is US$300 per month, compared to US$338 in Tunisia, US$430 in Turkey, and nearly ten times more in nearby Spain, though companies have come to Morocco not just because of cheap labour, but also the availability of skilled labour. Incentives play their part, too, with government subsidies of as much as US$6 000 a year per person for training in higher-tech areas. Up to 15 per cent of the total investment amount can be met through subsidies through the Hassan II Fund. There are also tax exemptions, including zero per cent corporate tax during the first five years and then a reduced rate of 8.75 per cent for the next 25 years; and VAT and customs exemption along with the tax-free repatriation of foreign earnings.

Construction on Tangier Med, 40kms north-east of the city, began in 2003, opening four years later. Today it handles 3.5 million (20-foot equivalent unit, or TEU) containers, the export or transhipment of 500 000 new cars, three million passengers (mostly to Spain and France), and the movement of 300 000 trucks, ranking it the 45th largest container port worldwide, and the busiest in Africa. Port Said is next in the African rankings in the 52nd position, with 3 million containers, Durban 65th (down from 51st in 2017) with 2.7 million and Mombasa 114th (previously 112th) with 1.2 million. With the second phase of the port opening later this year, it aims to be at 10 million TEUs within eight to 10 years.

It's a slick, high-tech operation, handling an average of 38 ships per day, connecting to 188 ports in 80 countries. And it's a showcase for Public Private Partnerships, much talked about in Africa, but much less carried out.

Tangier Med is the result of US$4 billion of public investment concentrated on the port, purchase of the land, and the construction of 50kms of expressway. The private sector added 'everything on top' says Rachid Houari, director of the port, including cranes, factories, and warehousing. There are three private container port operators with 25-year concessions, and one each for hydrocarbon and car operations.

The first stage of Tangier Med has seen the flow of TEUs at 3.5 million in 2018, which will increase potentially three-fold by the second phase expansion, below.

Although much of the traffic today is transhipment, the concept of Tangier Med was unlike any other major port. 'We had ambitions to be the most modern port in Africa but also to make best use of our excellent geographic position,' he says, with the Rock of Gibraltar clearly visible over his shoulder on a clear day, 'to attract big factories. The Dubai model is mostly about logistics, not manufacturing. I suppose we would like,' he smiles, 'to look like Rotterdam in terms of container handling, Dubai in terms of logistics, and Singapore in terms of industry'.

Vision is important, but political stability and predictability plays a key part. Because of this 'We were able to leverage,' notes Houari, who received his post-graduate education at Southampton University, famed for its naval engineering excellence, 'Morocco's reputation as a safe, stable country where you can do business in a predictable way.'

And there is one additional, related and crucial advantage. Morocco has free trade agreements in place with the European Union, the United States, and Gulf countries among others, representing 1.6 billion people and 60 per cent of global GDP.

In an era where globalisation seems to be on the retreat, Morocco has made access to richer markets a core foreign policy ambition.

But openness is nothing new to the city. In some respects, it's a case of back to the future.

As an international protectorate from 1923 until Morocco's independence in 1956, Tangier was always open, both to trade, the free use of currencies and as a counter-cultural icon. It became a nub for hedonistic experimentation, in writing as in drugs and openly gay lives, the setting for William Burroughs' *Naked Lunch* and long-time resident Paul Bowles' *The Sheltering Sky*. As Burroughs put it, 'Tangier is one of the few places left in the world where, so long as you don't proceed to robbery, violence, or some form of crude, antisocial behaviour, you can do exactly what you want.' He certainly did so in delving into heroin, morphine, majoun and various opioids.

Naked Lunches, Sheltering Cafes and the odd Interzone: Ghosts of Bowles and Burroughs are chased by tourists in search of the 'old' Tangier.

Opposite the French mission, the corrugated façade of the Café de Paris, supposedly the haunt of Burroughs, Bowles, Jack Kerouac, Alan Ginsberg and disciples of the Beat generation, offers a clear 180 degree vantage of the passing traffic through its floor-length windows. Sad faced, inevitably moustachioed red jacketed waiters mill their way through the heavy brown leather chairs serving coffee and the occasional croissant, just as they might have done 60 years ago. Nearby, the Grand Café in the old medina's Petit Socco with its *fin-de-siècle* facades, offers similar people-watching opportunities, with shop vendors hassling tourists in hustling all manner of tat from fezzes to fridge magnets.

From the ubiquitous felines to the fetid smells, one can imagine the effects on Burroughs in the spaced-out writing of his disturbing, if seminal *Naked Lunch* as he traversed his dreamlike Interzone.

Bowles described Tangier as 'rich in prototypal dream scenes: covered streets like corridors with doors opening into rooms on each side, hidden terraces high above the sea, streets consisting only of steps, dark impasses, small squares built on sloping terrain so that they looked like ballet sets designed in false perspective, with alleys leading off in several directions; as well as the classical dream equipment of tunnels, ramparts, ruins, dungeons and cliffs.'

That's the Tangier portrayed more recently in *The Bourne Ultimatum*, and the gripping fight-to-the-death between the eponymous star and itinerant hitman Desh. It's a cameo of high-speed chases through narrow, cobbled medina lanes, up stairwells, along narrow streets and ramparts, over flat-topped roofs dodging satellite dishes, jumping over streets, through windows and, finally, into a small bathroom where the grim fight is concluded with one winner. There are no Desh sequels.

Four other free zones are run by the government agency MEDZ. The aerospace hub at Midparc in Casablanca, with 16 companies employing 2 400, the abovementioned automotive zone at Kenitra on the Atlantic, and those at Oujda and in Salé alongside the capital Rabat. Each of these is fed, like Tangier, by an ecosystem of incubators developing implementable ides, local financing, and connections with business. There are more than 70 000 workers at MEDZ-run free zones and industrial parks countrywide.

The seven free zones countrywide are interspersed with industrial parks and feeder incubators.

The aerospace sector is expected to receive a boost with the relationship between Royal Air Maroc and Boeing, and that in turn by an expansion in the national carrier's routes, flying to 13 European countries (including 11 cities in France), 24 in Africa, three in the Americas and two in the Middle East.

Call centres have also recently grown rapidly due, in particular, to Moroccan costs and proficiency in French. Now more than 20 000 work in this sector.

Royal Air Maroc, which is fully owned by the government of Morocco, carried 7.3 million passengers in 2017.[5]

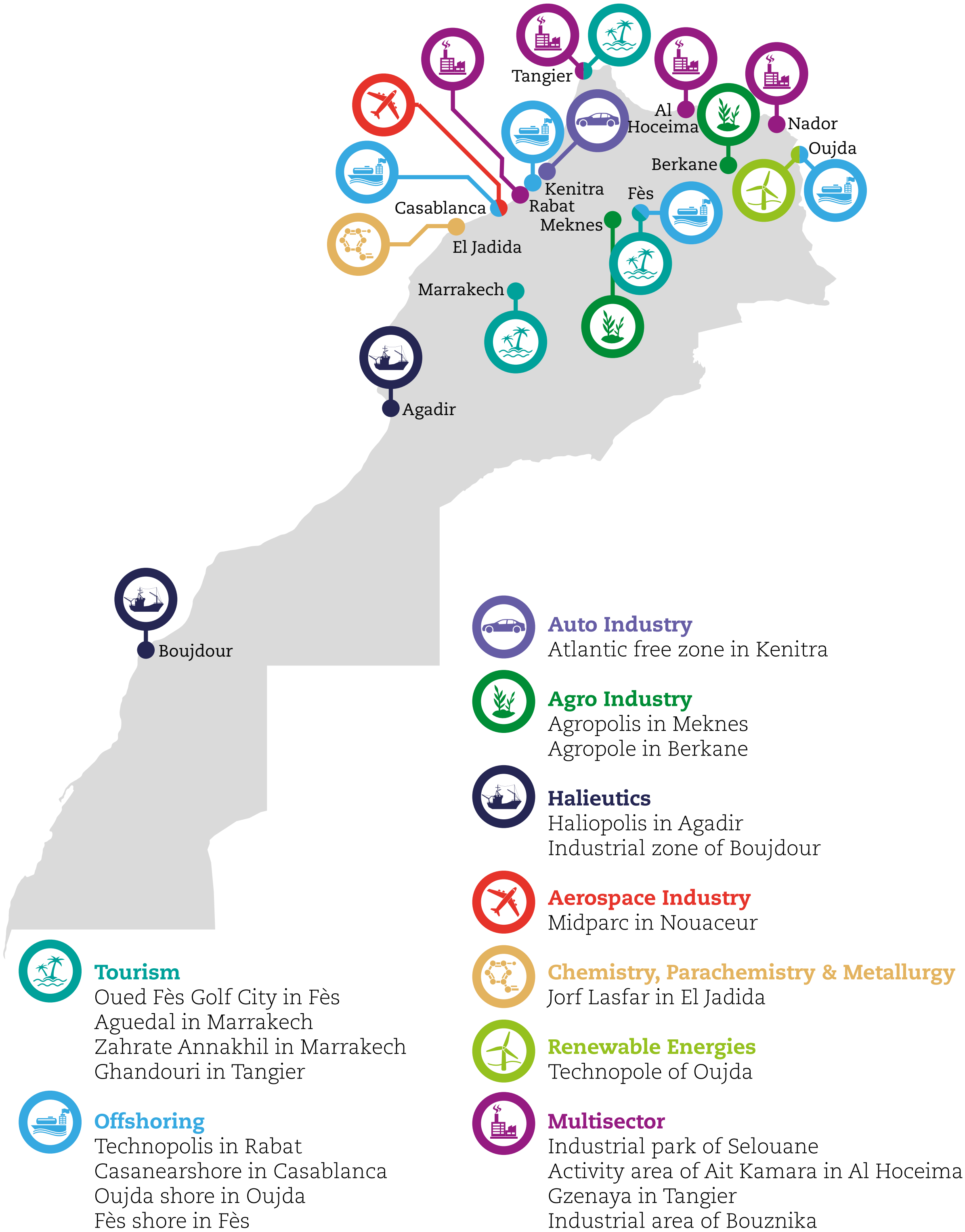
There is some academic debate, notes MEDZ's Mustapha Abir, about whether 'the expenditure of tax revenue in subsidies is equal to the value of the jobs created and technology transferred'. But this argument presumes there is a better scheme available to create jobs. It also, as he notes, does not factor in the value of knowledge and skills transfer to Moroccans, without which they would exist on the periphery of the global economy.

The Midparc Free Zone at Casablanca's airport should double in size with the arrival of Boeing in 2020.

Morocco is not without its challenges. At independence the population was 10.5 million. Sixty years later it has more than tripled. But this trend is flattening, population growth falling from a high of 3.3 per cent per annum in the late 1950s to 1.4 per cent in 2016. Urbanisation has been rapid. At independence 29 per cent of the population lived in cities, now it's more than double that. Tangier's population has swelled six-fold to over 1.5 million in the last 35 years. With a need to create jobs for 200 000 graduates every year, the pressure is on not just to plan, but to do.

There is little alternative but to forge ahead on job creation, lessons that the rest of Africa

MEDZ-run Industrial Parks and Free Zones



would be wise to heed, as it faces a doubling of its population over the next generation. 'Africa needs to average 7% economic growth each year until 2050,' observes Mouhcine Jazouli, the Kingdom's Minister for Africa, 'if it is to keep pace with population growth and achieve income growth'.

A source of subsidies and services: Tangier Med's one-stop-shop.

Another lesson from Morocco is that credibility with investors does not come from speeches or good intentions. 'It comes from doing things on time, from sticking to our commitments,' reflects Rachid Houari, 'from doing what we say.' He sees himself as a 'facilitator' for business, acting to 'undo any bureaucratic obstacles so that things move smoother and faster for the client.' Similarly, the *Agence Spéciale Tanger Mediterranée* was set up as a one-stop-shop for industrial investors, where 'every authorisation necessary can be signed' notes Sara Maatouk, one of its directors, like Houari also European educated.

Tangier is less hedonism today, than hard yards and hard work.

During the week that I visited Tangier Med, President Cyril Ramaphosa appeared on television at Davos berating the continued imposition of sanctions on Zimbabwe. Colonialism and conspiracy ruled. Similarly South Africa's relations with Morocco have been handicapped by Pretoria's preference to view them through the prism of Western Sahara. The ANC also remains doubtful about free trade, dubious about PPPs, and ambiguous about the value of the private sector.

Morocco, on the other hand, is living in the present and building for the future.

Endnotes

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