

An Analysis of Single-Factory Special Economic Zones in Zanzibar and Tanzania



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KEY TAKEAWAYS

Zanzibar and Tanzania allow single factories to be declared as Special Economic Zones (SEZs).

In this policy brief, we look at four advantages claimed for traditional SEZs and consider their implications for single-factory SEZs in Zanzibar and Tanzania: (1) larger SEZs perform better, (2) SEZs can showcase economic reforms, (3) SEZs allow for concentrated infrastructure investment, and (4) SEZs can reduce rent-seeking and corruption.

We find that small single-factory SEZs in Zanzibar and Tanzania work poorly, prevent the use of SEZs as showcases or test-beds of economic reform, leave those factories exposed to poor quality infrastructure, and increase the opportunities for damaging rent-seeking and corruption.

Governments in Zanzibar and Tanzania should stop promoting, and look to phase out, the single-factory SEZ model.

Executive Summary

Zanzibar and Tanzania allow single factories to be declared as SEZs.

This policy brief discusses the single-factory SEZ model in Tanzania and Zanzibar and assesses whether it can fulfill the beneficial claims made for it on the Export Processing Zones Authority (EPZA) website and elsewhere.

Lacking data on single-factory SEZs, we have to be sensitive when using evidence to analyze the functioning and outcome of single factory SEZs in Zanzibar and Tanzania. In this policy brief, we look at four benefits that have been claimed for traditional SEZs and explore the implications for these discussions on the likely impact of single-factory SEZs in Zanzibar and Tanzania.

Single Factory SEZs in Zanzibar and Tanzania:

- ✧ Single-factory SEZs comprise the majority of SEZ firms in Tanzania but we have no available data about their prevalence in Zanzibar. There is an urgent need to provide better data (via surveys) or access (via improved government information sharing) about the role, functioning, and outcome of single-factory SEZs in Zanzibar and Tanzania.
- ✧ Despite little research on single-factory SEZs, much of the more general research shows large SEZs work better. As size is correlated with SEZ success, then a reasonable conclusion is that single-factory SEZs are likely to be the worst of the SEZ models.
- ✧ SEZs allow governments in Zanzibar and Tanzania to target the provision of good-quality infrastructure to a concentrated geographical area. This has been identified by firms as their main reason to locate in African SEZs. Single-factory SEZs in Zanzibar and Tanzania, dispersed as they are around the national-economy, by contrast, will be constrained by existing poor-quality national-level infrastructure.
- ✧ The single-factory SEZ scheme in Zanzibar and Tanzania is poorly designed and it is likely to increase opportunities for private sector rent-seeking that diverts energies away from productive entrepreneurial activity to corruption. The government of Tanzania does not have the capacity to manage the added demands on governance created by the single-factory SEZ scheme.

Main policy recommendation from this policy brief:

- ✧ Governments in Zanzibar and Tanzania should stop promoting, and commit to phasing out, the single-factory SEZ model.

Introduction: What is a Single-Factory Special Economic Zone?

A Special Economic Zone (SEZ) has been defined by the World Bank as a: “spatially delimited area within an economy that functions with administrative, regulatory, and often fiscal regimes that are different (typically more liberal) than those of the domestic economy. Operating through a variety of different forms – such as export processing zones, economic processing zones, free zones, and foreign trade zones – SEZs aim to overcome barriers that hinder investment in the wider economy, including restrictive policies, poor governance, inadequate infrastructure and problematic access to land”¹.

There are no clear criteria in this definition to explain how big that ‘delimited area’ has to be. In Zanzibar and Tanzania, a SEZ can comprise a single factory. The Export Processing Zone Authority (EPZA) that manages the SEZ scheme in Tanzania, describes what they call a ‘Standalone EPZ’ on their website: “The EPZ Act of 2002, also amended in 2006, allows individuals to own an EPZ in the sense of having a factory that produces products for export. Through this program, more and more companies continue to make production for export in various parts of mainland Tanzania” (<https://www.epza.go.tz/pages/epz-standalone>).

In Zanzibar, the relevant SEZ legislation and the Zanzibar Investment Promotion Authority (ZIPA) website is less clear. The Zanzibar Investment Promotion and Protection Authority Act, 2018 says: “the President may, by order published in the Official Gazette, declare any other area of Unguja² or Pemba to be a Free Economic Zone for the purposes of this Act and may define the demarcations thereof” (p.23). The Zanzibar Investment Act of 2023 states: “The President may, by a notice published in the Gazette, designate any area of Zanzibar to be a Special Economic Zone and define their demarcations, incentives, and regulators whether public or private” (p.16). While not explicitly mentioning single-factory SEZs, this legislation does not prohibit them.

In private communication with a Zanzibar government lawyer, SEZs were referred to as a “status” rather than as a “geographical” location. Elsewhere, the 2018 and 2023 Investment Acts both discuss tax incentives that are available for investors outside the SEZ scheme and legislate for the special category of ‘Strategic Investor’, through which a single firm can qualify for tax and other incentives.

This policy brief explores the single-factory SEZ model in Tanzania and Zanzibar and specifically assesses whether it can achieve the beneficial claims made for it on the EPZA website and elsewhere.

Single-Factory SEZs in Tanzania, Zanzibar, Sub-Saharan Africa, and Beyond

Single-factory SEZ models have been utilized in Zimbabwe, Malawi, Kenya, Ghana, Namibia, Senegal, Togo, Tanzania, and Mauritius in Africa. Data from 2008 indicates that the single-factory scheme was prevalent in Kenya (155 single units), Senegal (300 units), and especially Ghana (2,806 single units)³. In India, a conventional geographical-SEZ scheme was launched in 1965. However, the government run scheme was marred by inefficient bureaucracy and poor infrastructure; it failed to achieve its aims with respect to exports and withered throughout the 1970s. In 1981, in response to this failure, and as tentative measures were being taken to liberalize the Indian economy more generally, the government established the Export Oriented Unit (EOU) scheme. An EOU was effectively a single-factory SEZ that received various tax and other concessions. By 2009, there were 2,500 EOUs operating in India⁴. The single factory SEZ model is also utilized in Malaysia, Fiji, Mexico, the US, Honduras, and the Dominican Republic. The SEZ scheme in the US is not tied to any location and consists of access to selective tariff reductions for individual firms. In 2014, single-firm SEZs in the US accounted for nearly 18% of manufacturing value added, imported \$288 billion of goods eligible for incentives, and constituted over 28% of all taxable imports⁵.

It is difficult to access detailed and reliable data on the operation of the zones, and in particular the activities of firms located within them. There is no reliable publicly shared data on how many firms operate in the various economic zones in Tanzania. One recent report estimated that 173 companies have been licensed as SEZ or EPZ firms, of these about 120 are operational, and the majority of those (80%) are single-factory units⁶. This number is significantly different from other recent estimates. An impressive effort by academic researchers from the UK to undertake original fieldwork collected data on all companies operating under the SEZ scheme from its inception until 2022⁷. This survey found that from 2008 until 2019 the EPZA licensed 148 firms that started operations and reported production for export in at least one year. By 2019, there was evidence that 100 companies were registered and operating under the SEZ/EPZ scheme. The survey also found that over the period 2008–2018, a total of 48 firms exited the scheme, with the number of exiting firms increasing after 2017. By March 2022, a year after President Samia Suluhu Hassan took office, the EPZA was reporting that 23 new firms had entered the scheme⁸.

By 2019, over 70% of the SEZ companies were operating as single-factory SEZs, and were outside any public or privately constructed SEZ. Most of these firms were located in the industrial hub between Dar es Salaam and Bagamoyo⁹.

There is no mention of single-factory SEZs anywhere on the equivalent ZIPA website in Zanzibar, no accessible data on the number or functioning of single-factory SEZs, and no equivalent survey efforts to collect data.

There are a few scattered claims about the economic benefits that can be offered by single-factory SEZs, though there is very little research to support them. The SEZ scheme, including the single-factory component, was successful in Mauritius, though the geography of the island meant that there was little distinction between single-factory and general SEZs, with most SEZ firms ending up concentrated in a few industrial areas¹⁰. By 2009, the EOU scheme in India was responsible for 9% of all-India's exports, compared to only 4% of Indian exports

from the conventional SEZ scheme. This was summarized by one scholar: *“Indian EOUs [...] seem to have been an unwitting, success story, both in terms of policy-driven export generation as well as developmental influence.”*¹¹

In Tanzania, the EPZA website declares: *“The advantage of this program is that one can build his own factory anywhere in mainland Tanzania, in the area he likes and fits his investment project and get all the attractions as investors who are in the SEZ areas”* (<https://www.epza.go.tz/pages/epz-standalone>).

One scholar¹² offers some support for this view, noting that government officials may be under political pressure to designate certain areas that are often backward or politically influential as SEZs. The single-factory SEZ model avoids this problem and allows the government to grant incentives to single firms without compelling them to re-locate into zones chosen for political rather than economic and commercial reasons. Another scholar¹³ notes that single-factory SEZ models may work, but only when the country has achieved a sufficient level of development so that, *“high-quality infrastructure is widely available and services can be delivered effectively, for example through the use of ICT infrastructure”*¹⁴. As we demonstrate later, this is not the case for Tanzania and Zanzibar.

Lacking data on single-factory SEZs, we have to be sensitive when using evidence to analyze the functioning and outcome of single factory SEZs in Zanzibar and Tanzania. In this policy brief, in looking at four benefits that have been claimed for traditional SEZs, we can assess the implications for these discussions on the likely impact of single-factory SEZs both countries. These benefits are large. SEZs work better, can be a showcase or test bed for economic reform, can enable the targeting of concentrated infrastructure provision, and can help minimize, or even eliminate, rent-seeking and corruption.

Policy recommendation: while single-factory SEZs comprise the majority of SEZ firms in Tanzania, we have no information about their prevalence in Zanzibar. There is an urgent need to create (via surveys) or access (through improved government websites) better data about the role, functioning, and outcome of single-factory SEZs in Zanzibar and Tanzania.

Benefits of SEZs No 1: Large SEZs Work Better

There is little specific research on single-factory SEZs but more general research indicates that large SEZs work better. If size is correlated with SEZ success, then a reasonable conclusion is that single-factory SEZs are the worst of these models.

By 2010, SEZs in China accounted for more than 30 million jobs, 22% of national GDP, 46% of FDI and 60% of exports¹⁵. The success of the Chinese SEZ program in the 1980s and afterwards has been attributed to the fact that the first four zones, in Shenzhen, Zhuhai, Shantou and Xiamen, and later zones in Hainan, Pudong and Tianjin Binhai, all included entire urban areas within the scope of the SEZ special regulatory regime¹⁶. Large SEZ size facilitated the integration of urban and economic planning by providing, for example, housing and transport for workers to ensure that the labor market would function effectively.

A wider study of 346 zones in 22 countries across the developing world and South Korea uses nightlight data from the US Defense Meteorological Satellite Program for 1992-2012 to measure economic activity within zones. Nightlight data is a good proxy or rough indicator of both employment and the number of firms within SEZs. The results show that the size of the SEZ is positively and significantly correlated with economic performance. Size matters and large zones have more growth potential¹⁷.

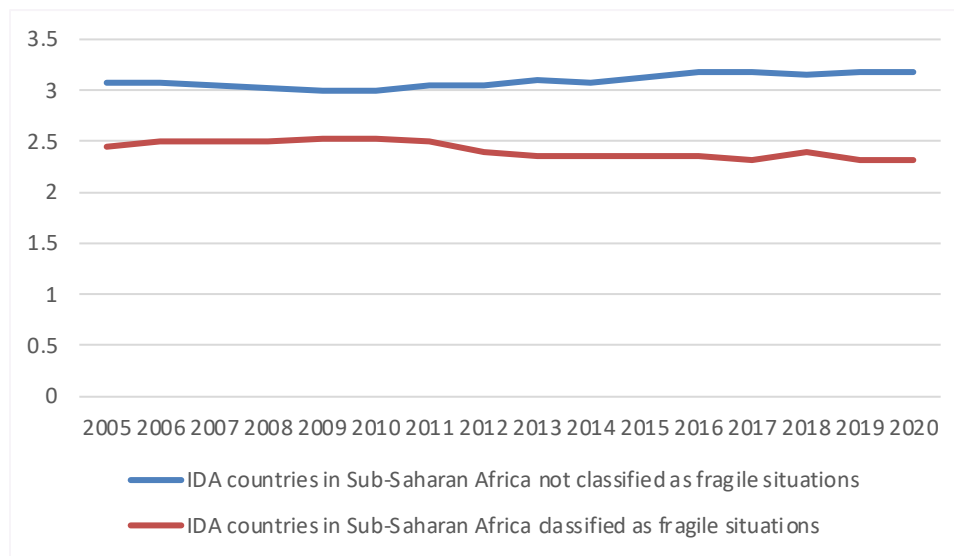
Contrary to this evidence that size matters, African zones generally have fewer firms than those in the rest of the world. A survey from 2009 found a striking contrast between SEZs in the Dominican Republic (550+ firms), Honduras (almost 350 firms), and Vietnam (3,500 firms), and those within African zones (35 firms on average)¹⁸. A more recent survey found that while there are some successful, large zones in Africa, such as the Tangier Free Zone in Morocco (750 firms) or the Egypt Alexandria Free Zone (405 firms), African zones on average had only 60 firms or fewer and 94% of zones surveyed had less than 200 firms¹⁹. The small size of African zones has been blamed as a contributory factor in the relative failure of zones in Africa compared to those in Asia.

Policy recommendation: increase the size of SEZs in Zanzibar and Tanzania to encompass entire urban areas. Governments in Zanzibar and Tanzania should also stop promoting, and phase out, the single-factory SEZ model. Consolidating small zones into fewer large zones could make sense, but is likely to be difficult if those small zones are spread across a wide geographical area.

Benefits of SEZs No 2: SEZs as a Test-Bed or Showcase of Economic Reform

There is widespread agreement that the first-best policy to boost domestic and foreign investment is to create national-level good governance and well-protected property rights. Figure One shows how hard this reform is to achieve in practice. Despite all the local and international efforts to help strengthen rule-based governance and protection of property rights across Africa, measures of both have shown little or no improvement over the last two decades.

Figure One: Property Rights and Rule-based Governance Rating in Sub-Saharan Africa, 2005-2020 (1=low to 6=high)²⁰



In Tanzania, according to the Atlantic Council Freedom and Prosperity Index, 'Property Rights²¹' were marginally lower in 2022 (51) than they were in 2015 (51.7). 'Investment Freedom²²' in 2022 (57.9) was lower than in 2010 (68.4). In 2020, according to the World Bank Doing Business Indicators, Tanzania ranked 162nd out of 190 countries for starting a business, 149th in dealing with construction permits, 165th in paying taxes, and 146th in registering property²³.

National-level reform of governance and property rights in Sub-Saharan Africa has been undermined by the interests of elites, characterized by a lack of property rights that makes it easier to acquire the property of the politically disenfranchised at low-cost, overlapping property rights (where some property is private and some held through customary or tribal laws), a lack of government capacity, and stalled progress towards full democracy, all of which making it easier for elites to protect themselves.

A widely discussed advantage of SEZs is that they allow reform, and lead to better governance and protection of property rights through a focus on a single SEZ. The demonstrable success of that SEZ can lead to its growth, replication (more SEZs), and positive influence on national-level policy making.

Traditional SEZs can serve as policy test-beds. Experiments in new policies such as foreign ownership or regulatory reform can be launched in a small-area, which is both easier than undertaking projects on a national scale, are less damaging if they do not work, and less politically threatening to elites who benefit from the maintenance of the status quo²⁴. SEZs can also be used as showcases, with a focus reform in a SEZ demonstrating the success of that reform. Once opponents or the wider public see rising exports, employment, and investment, they may be persuaded to support the rolling out of SEZ-style reform to a national level²⁵. China set up four SEZs in 1980 that were widely regarded as successful experiments. Those Chinese SEZs experienced rapid growth, they inspired the creation of more SEZs in China, and they prompted national-level economic reform that led China away from state-socialism into market-globalism.

Single-factory SEZs are invisible, lost amidst hundreds of other firms, while a physical and highly visible SEZ provides opportunities for observation. It is difficult, as in Zanzibar and Tanzania, to collect and process data on hundreds or even thousands of single factory SEZs, making any assessment of their economic success or otherwise problematic. Single-factory SEZs cannot serve as test-beds or showcases of economic reform.

Policy recommendation: single-factory SEZs cannot be used as test-beds or showcases of economic reform.

Benefits of SEZs No 3: SEZs and Targeted-Concentrated Infrastructure Provision

Tanzania has poor quality infrastructure that undermines the ability of firms to produce, transport, and export goods and services efficiently and competitively. According to the 2019 Global Competitiveness Report published by the World Economic Forum, out of 141 countries Tanzania ranked 110th in transport infrastructure, 121st in utilities (electricity and water supply), and 133rd in ICT adoption²⁶. Given government budgetary, organizational, and capacity constraints in Zanzibar and Tanzania, it is difficult to improve infrastructure for investors and exporters nation-wide. An SEZ will allow infrastructure construction and provision to be targeted to, and concentrated in, one-location. An alternative argument is that single-factory SEZs with the freedom to locate anywhere will choose optimal locations where they can best access a labor force, customers, and suppliers. One study of states in India finds that EOUs (single-factory SEZs) are most successful when they are integrated into an existing industrial structure and physically linked to that wider economy²⁷. There is little evidence for Africa, but that evidence is quite clear. Firms choose to join SEZ programs because of the better infrastructure they offer.

A 2009 survey by the World Bank of more than 600 firms located in SEZs across 10 countries, including in Africa, Ghana, Kenya, Lesotho, Nigeria, Senegal, and Tanzania, as well as Bangladesh, Vietnam, the Dominican Republic and Honduras, found that the two most important reasons for joining a SEZ in Africa were 'cost and quality of utilities' and 'access to transport infrastructure'. Other factors such as 'access to highly skilled labor', 'access to suppliers', and 'access to low-cost labor' rated 6th, 7th, and 8th²⁸.

Policy recommendation: SEZs allow governments in Zanzibar and Tanzania to target the provision of good-quality infrastructure to a concentrated geographical area. This has been identified by firms as their main reason to locate in African SEZs. By contrast, single-factory SEZs in Zanzibar and Tanzania, dispersed around the national-economy, will be constrained by existing poor-quality national-level infrastructure. Governments in Zanzibar and Tanzania should stop promoting, and phase out, the single-factory SEZ model.

Benefits of SEZs No 4: SEZs, Rent-seeking, and Corruption

As noted earlier, SEZs may allow a reform-minded faction in central and local government to implement reform, thereby providing good governance and protecting property rights in a single geographical location that acts as a test-bed or showcase for wider economic reform. A related question is how SEZs impact on the incentives of elites to engage in rent-seeking and corruption. A well-designed and well-functioning SEZ will offer elites a higher payoff from economic reform rather than maintaining or expanding the rent-seeking and corruption opportunities offered by the status quo²⁹.

A well-designed SEZ scheme will offer central and local elites benefits in terms of local employment creation, provision of more local infrastructure (roads, energy and water), more local tax revenues, as well as increased inflows of foreign investment. Fiscal decentralization will allow locally connected leaders to keep a substantial amount of the tax revenues that they generate³⁰. So, a well-designed SEZ will incentivize central, and especially local, elites to pursue further economic reform. A poorly designed SEZ model may work in the opposite direction, encouraging more rent-seeking and corruption. The SEZ scheme in Poland has been criticized as being driven by rent-seeking, whereby companies spend their time and entrepreneurial energy lobbying for more tax and other concessions in the SEZ rather than competing in the market³¹. In India, SEZs failed to generate positive developmental outcomes and, instead, politicians sought SEZ status so they could participate in lucrative land speculation, buying farming land cheaply and selling it for factory and housing construction in SEZs at vastly inflated prices³².

There is excellent data on the operation of the US single-factory scheme. The application process imposes a significant bureaucratic hurdle on firms. To produce as a single-factory SEZ, a firm must obtain permission. This process involves an application that becomes easily accessible to anyone and can be contested by any other party. Granting permission can take a year. If the firm then wishes to source new foreign imports, expand capacity, or add a new output, it must apply for new permission and repeat the same process. The application process is driven by lobbying and politics. Once a firm has applied for permission to become a single-factory SEZ, industry groups, individual producers, local and state governments, unions, congressmen, senators, and individual SEZ governing bodies all lobby to influence the final decision. Controversial decisions may feature dozens of statements from different groups. One study shows that industries with significant political influence are more likely to be granted SEZ status. The process is about politics rather than commercial or economic realities³³.

There is no equivalent data summarizing the application process for single-factory SEZ status in Zanzibar or Tanzania. There are suggestions that the single-factory scheme cannot be implemented efficiently based on any economic and commercial criteria and that the scheme has exposed the governments of Zanzibar and Tanzania to more opportunities for rent-seeking and corruption.

This policy brief has already noted that recent surveys have estimated very different numbers of single-factory SEZs in Tanzania. The official data held by the EPZA on “EPZ firms

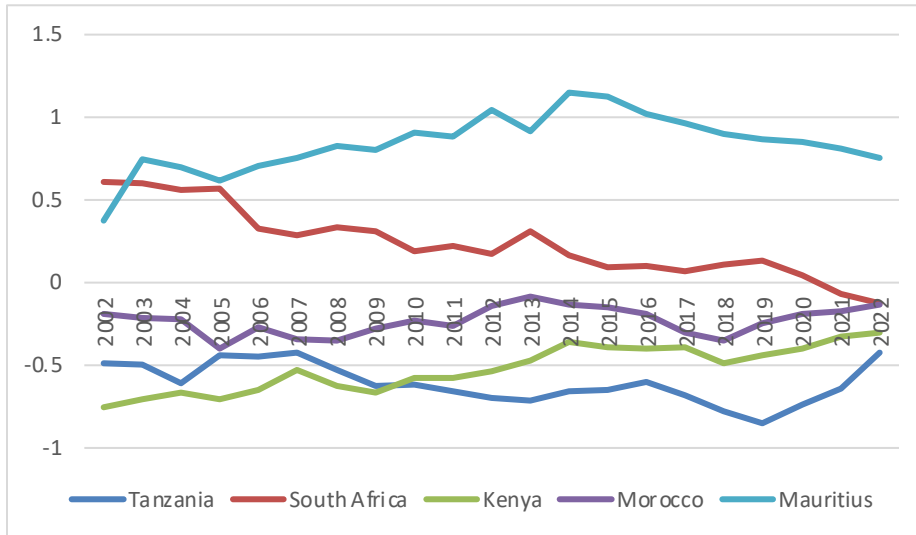
*(operational status, employment, exports, etc.) are contradictory, patchy and unreliable.*³⁴ Different ministries in Tanzania hold contradictory data, for example the Ministry of Finance shows that 31 companies received SEZ status during April to June 2015, while only 17 of these companies were on the list managed by EPZA³⁵. Consistent enforcement of EPZA or ZIPA rules is impossible given the inadequate data on the number and functioning of single-factory SEZs. The lack of visibility and understanding of the single-factory scheme creates an opportunity for firms to bribe government officials to obtain the tax and other incentives associated with single-factory SEZ status³⁶.

The single-factory SEZ scheme in Zanzibar and Tanzania creates a second means by which incentives can be distorted. As per the rules, firms in Zanzibar and Tanzania can only enjoy the tax and other benefits of SEZ status if they export 80% of their output. Firms will have an incentive to avoid this onerous obligation and divert domestic production to the domestic market. It is relatively easy to monitor firms inside SEZs through customs and other officials being posted to an SEZ to visit firms and monitor compliance. Scattered single factory SEZs are much harder to monitor, especially if the government has poor data on their number and location³⁷. There is evidence that the government of Tanzania has faced problems in monitoring trade flows and firms are prone to mis-invoice imports and exports³⁸.

There is anecdotal evidence that firms are engaged in extensive lobbying of the government of Tanzania to obtain the benefits associated with SEZ status, or even to modify existing rules further to their own benefit. One study gives an example from 2006 of a textile firm, NIDA, that obtained the benefits associated with SEZ status, negotiated a further set of incentives with the Ministry of Finance to import raw materials more easily, and then negotiated a further reduction, to 50% of output, of its export obligations. The lobbying by NIDA was countered by local industrialists and suppliers. Contrasting with the transparency of the US example, there is no information on how these decisions were reached beyond speculative journalism³⁹.

Figure Two shows the World Bank measure for 'government effectiveness⁴⁰' in four African countries (South Africa, Kenya, Morocco, and Mauritius) that have been widely acknowledged as running successful SEZ programs, as compared to Tanzania, the subject of this policy brief. Figure Two shows that government effectiveness is low, and generally declining in Tanzania, indicating that the government is unlikely to have the capacity to manage the added complexities related to data requirements or cope with the extra incentives to engage in rent-seeking and corruption created by the single-factor SEZ program.

Figure Two: Government Effectiveness⁴¹



Policy recommendation: the single-factory SEZ schemes in Zanzibar and Tanzania are poorly designed and likely to increase opportunities for private sector rent-seeking that divert energies away from entrepreneurial activity to corruption. The government of Tanzania does not have the capacity to manage the added demands on governance created by the single-factory SEZ scheme. Governments in Zanzibar and Tanzania should stop promoting, and phase out, the single-factory SEZ model.

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Endnotes

- 1 Farole (2011a:17).
- 2 Unguja is another name for the main island of Zanzibar.
- 3 Farole (2010:12).
- 4 Cheesman (2012:7).
- 5 Grant (2020:1545).
- 6 UNECA (2022:49).
- 7 Andreoni et al. (2022).
- 8 Andreoni et al. (2022:19).
- 9 Andreoni et al. (2022:19).
- 10 Farole (2011b:73).
- 11 Cheesman (2012:7).
- 12 Moberg (2017).
- 13 Farole (2011c).
- 14 Farole (2011c).
- 15 Alexianu et al. (2019:4).
- 16 Dercon et al. (2019).
- 17 Frick et al. (2019:49).
- 18 Farole (2010:12).
- 19 Rodriguez-Pose et al. (2022:461).
- 20 World Bank (2024).
- 21 *"This indicator assesses the extent to which a country's legal framework allows individuals to acquire, hold, and utilize private property, secured by clear laws that the government enforces. Its component parts are protection of property rights and risk of expropriation, which are taken from the Fraser Institute's "Economic Freedom of the World Annual Report" and the Credendo Group's "Expropriation Risk Country Rankings," respectively (Atlantic Council Methodology, p.2) <https://www.atlanticcouncil.org/wp-content/uploads/2022/06/Methodology-for-researchers.pdf>*
- 22 *"This indicator measures the ability of individuals and firms to move capital within and across a country's border without restrictions. It comes from the Heritage Foundation's "Index of Economic Freedom" (Atlantic Council Methodology, p.4) <https://www.atlanticcouncil.org/wp-content/uploads/2022/06/Methodology-for-researchers.pdf>*
- 23 World Bank (2024).
- 24 Moberg (2017:72).
- 25 Moberg (2017:73).
- 26 WEF (2019).
- 27 Cheesman (2012:37).
- 28 Farole (2011d).
- 29 Moberg (2017).

- 30 Moberg (2017:80).
31 Moberg (2017).
32 Alkon (2018).
33 Grant (2020:1546).
34 Andreoni et al. (2022:27).
35 Andreoni et al. (2022:27).
36 Andreoni et al. (2022:29).
37 Andreoni et al. (2022:21).
38 Andreoni et al. (2022:31).
39 Gray (2013:196).
40 *"Government Effectiveness captures perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies. Estimate gives the country's score on the aggregate indicator, in units of a standard normal distribution, i.e. ranging from approximately -2.5 to 2.5"* (World Bank, 2024).
41 World Bank (2024).

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