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2022/23 KSP Policy Consultation Report

Peru

Roadmap for the Implementation of FDI Attraction Strategies for SEZs in Peru

Ministry of Economy and Finance

KDI Korea Development Institute

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Ministry of Economy and Finance
KDI Korea Development Institute
SIV
MERI

2022/23 KSP Policy Consultation Report

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In Cooperation with	The Ministry of Foreign Trade and Tourism

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2022/23 KSP Policy Consultation Report

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Preface

Knowledge is a crucial enabler of innovation and growth and a significant instrument for implementing Sustainable Development Goals. The international community is therefore emphasizing knowledge sharing for mutual prosperity and inclusive growth.

Korea has achieved remarkable economic development in recent decades. Through trial and error and innovation, Korea has laid the foundations for sustainable economic growth. Korea's development experience and know-how is an important asset to the international community.

The Ministry of Economy and Finance (MOEF) and Korea Development Institute (KDI) launched the Knowledge Sharing Program (KSP) in 2004 to meet the international demand for policy implications of Korea’s development model and sustainable prosperity. As an important platform for economic cooperation, KSP aims to share knowledge with partners and build a solid foundation for expanding economic and political cooperation.

Peru has one of the fastest-growing economies in Latin America. The Peruvian economy is known for its strong mining sector, which contributes significantly to the country's Gross Domestic Product (GDP) and export earnings. The Peruvian government recognizes that Foreign Direct Investment (FDI) is essential to the country's development, and has made significant efforts in this area. As a factor in attracting foreign investment, this KSP project was commenced to share Korea’s economic development experience regarding Special Economic Zones (SEZ).

Therefore, Korean and Peruvian experts in the Special Economic Zones (SEZ) shared their experiences of operating the SEZs. Throughout the process, I also learned how collaborative efforts can lead to overcoming difficulties and how the importance of knowledge sharing has diminished as more countries understand how others have dealt with challenges.

On behalf of the KSP research and consultancy team, I would like to express my deepest appreciation to the government of Peru and MINCETUR for their cooperation in this project. In particular, I would also like to express my deep gratitude to Ms. Claudia Parra Silva, Director General of Trade Facilitation, and Mr. Yungjoon Jo and Mr. Jong Wook Choi, Ambassador of the Embassy of the Republic of Korea in Peru, for their generous support. The completion of this project would not have been possible without their dedication. I am also very grateful to Senior Advisor Dr. Heenam Choi and the professors of Chungnam National University and the KSP

consultancy team - Principal Investigator Professor Hee Cheol Moon, Professor Keunyeob Oh, Professor Taejoong Kim, Professor Jongheuk Kim, Professor Chulhyung Park, Professor Taek Ho Kwon, CEO (AJ Consulting) Youngjin Kim, Researcher Mr. Hyeongeun Song and Project Officer Ms. Dongsoon Kang for preparing this report.

This project has benefited greatly from the work of many MINCETUR officials, including Ms. Carol Flores Bernal, Mr. Brayan Miguel Palomino Espino, Ms. Valeria Lezcano Bartra, and especially Ms. Ana Palacios De La Peña, and local Peruvian consultants, Mr. Javier Hernando Illescas Mucha, Mr. Cristian Leonardo Calderón Rodríguez , Ms. Patricia Rocío Leonardo Marín , who provided valuable inputs for the preparation of this report.

Furthermore, many stakeholders within and outside the Peruvian government have benefited from this project. To all those who made valuable contributions and showed dedication to the successful completion of this project, I would like to express my sincere and special thanks. I am also grateful to the Reviewers and Consultants for their fruitful advice in preparing this report and would like to thank everyone who contributed to and remained committed to the successful completion of the project.

I also thank the Center for International Development of KDI, especially Project Manager, Hokyung Bang, Project Officer Ms. Keunyoung Yoon and Team Leader Bora Nam for their hard work and dedication to the project.

I am confident that this KSP will serve as a stepping stone to enhance mutual learning and cooperation between Peru and Korea. I hope it will contribute to government innovation and public reform.

CEO

Young Koo Brad Kim

QIV

Contents

2022/23 KSP with Peru ····· 015
Executive Summary ····· 023

Chapter 1
Analysis on Constraining Factors on FDI Attraction for SEZs in Peru and Its Implications

Summary ····· 029
1. Introduction ····· 031
2. Economic Status of Peru and Its Policies ····· 032
  2.1. Current Economic Status of SEZ and FDI in Peru ····· 032
  2.2. National Level Economic Policies and Strategies ····· 038
3. Constraining Factors on FDI Attraction in SEZ of Peru ····· 043
  3.1. PEST and SWOT Analysis on FDI Attraction in SEZ of Peru ····· 043
  3.2. Analysis of Core Elements for Infrastructure Development in Peru ····· 050
4. Case Study of FDI Attractions in Important Countries and Policy Implications ····· 052
  4.1. Challenges and Prospects of Special Economic Zones in South Korea ····· 052
  4.2. Current Status of Neighboring Countries in Latin America: Mexico, Brazil, and Panama ····· 056
  4.3. Comparison with Peru SEZs' Case and Policy Implications for FDI Attractions ····· 058
5. Economic Analysis on the Selection of Industries for FDI Attraction in SEZ ····· 060
  5.1. Analysis Methodology ····· 060
  5.2. Results: Peru as a Whole Country ····· 062
  5.3. Analysis for SEZs in Peru ····· 065
6. Conclusion and Policy Recommendations ····· 068
References ····· 070
Appendix ····· 072

Chapter 2
Analysis of FDI Attraction Strategies for SEZs in Peru, Including Incentives and Other Tools

Summary ····· 079
1. General Status of Peru's SEZ Incentives ····· 081
  1.1. General Incentives ····· 081
  1.2. Incentives for Each SEZ ····· 082

1.3. Interview with Tenant companies ····· 086
1.4. Survey ····· 087
1.5. Implications ····· 089
2. Analysis of Korea's SEZ Incentives ····· 090
2.1. Scope of Analysis ····· 090
2.2. Korea's SEZ Incentives ····· 091
2.3. Free Economic Zone ····· 092
2.4. Foreign Investment Zone ····· 095
2.5. Free Trade Zone ····· 097
2.6. Implications ····· 100
3. Analysis of Korea's SEZ Development ····· 100
3.1. Overview ····· 100
3.2. Analysis of Korea's SEZ FDI ····· 101
3.3. Masan Free Export Zone ····· 102
3.4. Saemangeum Special Zone ····· 108
3.5. Implications ····· 115
4. Policy Proposal and FDI Attraction Strategies for Peru's SEZ ····· 116
4.1. Review of OECD Recommendation Criteria ····· 116
4.2. Incentive Programs for Tenant Companies and Public-side Developers ····· 117
4.3. Strategies for Attracting Anchor Companies ····· 118
5. Implications and Policy Recommendations ····· 118
5.1. Major Implications ····· 118
5.2. Policy Recommendations ····· 118
References ····· 121

Chapter 3
Selection Criteria for Peruvian SEZs and Improvement of the Governance System

Summary ····· 123
1. Introduction ····· 125
2. Status of SEZs in Peru ····· 125
2.1. Operations of the SEZs in Peru ····· 125
2.2. Performance Analysis of the SEZs in Peru ····· 127
2.3. Problems of the SEZs in Peru ····· 128

Contents

3. Selection Criteria for Existing SEZs in Peru 129
3.1. Main Considerations for the Development and Designation of SEZs 129
3.2. Legislative Foundations of SEZ Selection Criteria 130
4. Governance System of the SEZs in Peru 131
4.1. Governance Structure of the Peruvian SEZs 131
4.2. Legislations and Policies Related to SEZs 133
5. Lessons from Korean Experience 138
5.1. Categories of Korean SEZs 138
5.2. Development of SEZs in Korea 145
5.3. Success Factors of the Korean SEZs and Policy Implications 146
5.4. Benchmarking the Governance System of Selected Countries 149
6. Development of New Selection Criteria and Governance System 153
6.1. AHP/IPA Analysis of SEZ Selection Criteria 153
6.2. Developing a New SEZ Model: Focusing on Transition from Public to Private 165
7. Conclusion and Policy Recommendations 167
7.1. Conclusion 167
7.2. Policy Recommendations 168
References 170
Appendix 173

Contents | List of Tables

Chapter 1

<Table 1-1> Special Economic Zones in Peru ····· 036
<Table 1-2> SWOT Analysis Based on PEST Results ····· 049
<Table 1-3> InfraCompass 2020 Ranking of Peru: Among 76 Countries ····· 052
<Table 1-4> Current Designation Status of Main Special Economic Zones ····· 055
<Table 1-5> Results of Industry Selection for Peru ····· 063
<Table 1-6> Analysis Results for ZED Paita ····· 066

Chapter 2

<Table 2-1> Tax Exemptions ····· 082
<Table 2-2> Summary of SEZs Included ····· 085
<Table 2-3> Satisfaction with the Five Tax Reduction Benefits ····· 087
<Table 2-4> Satisfaction with the Tariff Benefits ····· 088
<Table 2-5> Additional Incentives Needed ····· 089
<Table 2-6> Incentives for Domestic Companies ····· 091
<Table 2-7> Incentives for Foreign Companies ····· 092
<Table 2-8> Incentives Comparison between Peru and Korea ····· 092
<Table 2-9> Korean Government's FDI Policy ····· 102

Chapter 3

<Table 3-1> SEZs in Peru ····· 126
<Table 3-2> SEZ Investment, Exports, and Imports (2022) ····· 127
<Table 3-3> Main Markets of Operational SEZs in Peru ····· 128
<Table 3-4> Specific Roles of the Government Agencies Related to the SEZs ····· 132
<Table 3-5> Problems and Tasks for Sustainable SEZs in Peru ····· 137
<Table 3-6> Governance System of Korean SEZs ····· 139
<Table 3-7> Comparison of Major SEZs in Korea ····· 144
<Table 3-8> Laws Related to Major SEZs in Korea ····· 145
<Table 3-9> Development of SEZs by Generation ····· 145
<Table 3-10> Major Success Factors and Problems in Korean SEZ ····· 149
<Table 3-11> Major Characteristics of Governance System in Selected Countries ····· 152
<Table 3-12> Scale of Importance for Pairwise Comparison ····· 155

Contents | List of Tables

<Table 3-13> Components of SEZ Selection/Evaluation Criteria ····· 157
<Table 3-14> Results of AHP Analysis ····· 159
<Table 3-15> SEZ Selection Criteria Explained ····· 162
<Table 3-16> Summary of IPA Results ····· 163
<Table 3-17> AHP/IPA Survey Statistics ····· 164

Contents | List of Figures

Chapter 1

[Figure 1-1] GDP and Terms of Trade ····· 033
[Figure 1-2] GDP Growth by Type of Expenditure ····· 033
[Figure 1-3] Export and Import Trends ····· 034
[Figure 1-4] Export Destinations: 1990 vs 2021 ····· 035
[Figure 1-5] FDI Inflows and Export Prices, 2000~2022 ····· 038
[Figure 1-6] Analysis Model for Industry Selection ····· 062
[Figure 1-7] Industry Position on the Present-Future Framework for Peru as a Whole ····· 064
[Figure 1-8] Results of Present-Future Analysis for ZED Paita ····· 066
[Figure 1-9] Results of Present-Future Analysis for ZED Matarani ····· 067
[Figure 1-10] Results of Present-Future Analysis for ZED Ilo ····· 067
[Figure 1-11] Results of Present-Future Analysis for ZOFRATACNA ····· 068

Chapter 2

[Figure 2-1] Korea Free Economic Zones ····· 094
[Figure 2-2] Korea Foreign Investment Zones ····· 097
[Figure 2-3] Korea Free Trade Zones ····· 099
[Figure 2-4] Masan Free Export Zone ····· 103
[Figure 2-5] President Park's Visit to the Construction Site of the Masan Free Export Zone ·· 103
[Figure 2-6] Construction of Masan Free Export Zone (1970) ····· 104

Chapter 3

[Figure 3-1] Special Economic Zones in Peru ····· 127
[Figure 3-2] Governance Structure of Peruvian SEZs ····· 131
[Figure 3-3] Free Trade Zone Management System ····· 140
[Figure 3-4] Extended One-stop-service System ····· 141
[Figure 3-5] Free Economic Zone Committee Organization Chart ····· 142
[Figure 3-6] Free Economic Zone Planning Team Organization Chart ····· 142
[Figure 3-7] AHP Flow Chart ····· 154
[Figure 3-8] Evaluation Framework for SEZ Selection Criteria by AHP Method ····· 155
[Figure 3-9] IPA Method ····· 158
[Figure 3-10] IPA Result (Government Officials) ····· 160
[Figure 3-11] IPA Result (SEZ Experts) ····· 160

Contents | List of Figures

[Figure 3-12] IPA Result (Tenants) ····· 161
[Figure 3-13] IPA Result (All Respondents)····· 161
[Figure 3-14] Results of AHP/IPA Survey ····· 165
[Figure 3-15] Proposed New Model for Sustainable SEZs of Peru ····· 167

2022/23 KSP with Peru

Dongsoon Kang (QIV)

2022/23 KSP with Peru

Dongsoon Kang (QIV)

1. Background of the Project

Peru is making efforts to increase exports and strengthen the functions of Special Economic Zones (SEZs) by actively attracting Foreign Direct Investment (FDI). Currently, exports through SEZs account for less than 1% of Peru's total exports, which is significantly lower than values for other Latin American countries such as the Dominican Republic, Nicaragua and Costa Rica, which account for around 40%. At the same time, there are various constraints to attracting FDI, so it is time for Peru to consider new approaches and strategies to attract FDI.

Peru has the second highest stable investment credit rating in Central and South America after Chile, but the economic impact of SEZs in terms of attracting FDI, creating jobs and increasing exports is weak. In addition, Peru's SEZs face difficulties in attracting foreign investment due to the lack of relevant systems and infrastructure, as well as the absence of a proper policy strategy from relevant ministries such as the Ministry of Finance and Economy (MEF) and the Ministry of Foreign Trade and Tourism (Ministerio de Comercio Exterior y Turismo - MINCETUR). The lack of incentives for tax benefits for companies located in SEZs, the sporadic operation of laws and systems related to SEZs, and the limited acceptance of foreign investment in the region present constraints to the optimal operation of SEZs. There is, therefore, a need for consultative cooperation. Korea's experience with the development of Special Economic Zones could be a source of inspiration.

2. Project Planning

2.1. Purpose of the Project

The project aims to support economic development and attract Foreign Direct Investment

in Peru by sharing Korea's successful economic development model, specifically focusing on Special Economic Zones (SEZs) such as Free Trade Zones (FTI). The project's objectives include facilitating a sustainable operating strategy for partner organizations, enhancing the capabilities of operating personnel, strengthening the functions of Peruvian SEZs, and expanding FDI attraction. By sharing Korea's SEZ experience and related policies, the project seeks to provide policy implications for Peru and explore opportunities for long-term cooperation, fostering stronger international cooperation between Korea and Peru and creating investment opportunities for Korean companies in the Peruvian market.

2.2. Scope of the Project

Since 2010, the KSP with Peru has undertaken 18 projects in various fields, including vocational training, health insurance, ICT, flood prevention, and smart cities. The theme for the 2022/23 KSP with Peru is "Establishment of a Roadmap for Attracting Foreign Direct Investment in Peru," in collaboration with MINCETUR. The Peruvian government aims to increase export share through SEZs and enhance their functions by attracting more FDI. The selected topics include 'Analyzing Factors Hindering FDI Attraction', 'Developing FDI Attraction Strategies for SEZs', and 'Improving the Governance System'. Local consultants recommended by MINCETUR will contribute to joint research activities and policy proposals. The project also includes plans for knowledge sharing and capacity building through expert lectures and ongoing policy development.

2.3. Implementation of the Project

It was planned that the main activities of this project, such as the Kick-off Meeting and the In-depth Study, would take place in Peru. However, due to the political issues caused by the impeachment of the Peruvian President during the planned date of the KSP Policy Seminar and In-depth Study, the aforementioned activities were held via online video-conferencing and e-mails. In particular, the In-depth Study was carried out via online video conferences and e-mail communication with local consultants who were specially hired for this project to help Korean researchers who cannot directly conduct on-site interviews or in-depth fact-finding on the ground.

Moreover, the governance of FDI and SEZs in Peru was also analyzed through interviews with relevant stakeholders and online demand surveys. To ensure the quality of the interim and final reports, the project plan and interim report were evaluated through consultative evaluation meetings to improve the quality of the final report.

Policy Consultation Research		
Sub-topics	**Researchers**	**Local Consultants**
1. Analysis on Constraining Factors on FDI Attraction for SEZs in Peru and Its Implications	Keunyeob Oh (Professor / Chungnam National University) Jongheuk Kim (Professor / Chungnam National University)	Javier Hernando Illescas Mucha (Economist)
2. Analysis of FDI Attraction Strategy for SEZs in Peru, Including Incentives and Other Tools	Taejoong Kim (Professor / Chungnam National University) Chulhyung Park (Professor / Chungnam National University) Youngjin Kim (CEO/ AJ Consulting)	Cristian Leonardo Calderón Rodríguez (Lawyer)
3. Selection Criteria for Peruvian SEZs and Improvement of the Governance System	Hee Cheol Moon (Professor / Chungnam National University) Taek Ho Kwon (Professor / Chungnam National University)	Patricia Rocío Leonardo Marín (Lawyer)
• Senior Advisor: Dr. Heenam Choi / Former Chairman& CEO, Korea Investment Corporation (KIC), Former Deputy Minister of Ministry of Economy and Finance • Project Director: Hokyung Bang / Specialist, Center for International Development (CID), KDI • Project Manager: - Youngkoo Brad Kim / Project Manager / CEO, QIV - Hee Cheol Moon / Principal Investigator / Professor, Chungnam National University - Keunyoung Yoon / Project Officer / Research Associate, KDI, Center for International Development (CID), KDI - Dongsoon Kang / Project Officer / Manager, QIV - Hyeongeun Song / Research Assistant / Chungnam National University		

3. Main Activities

3.1. Kick-off Meeting with KDI (3 November, 2022, Korea)

After selecting QIV Consortium as the implementing agency (QIV Inc. and Chungnam National University), a Kick-off Meeting was held with KDI to review the project plan and preparations for the 2022/23 KSP with Peru. Prior to the full implementation of the project, KDI was briefed on the requirements and provided with guidelines regarding mandatory requirements for successful project implementation.

The researchers analyzed opinions on the local demand for advice based on preliminary data research. The future research direction and research plan were shared through the Project Plan, along with pointers on what to discuss when visiting local agencies. Guidance was also provided on the overall timeline of the KSP project and the document preparation schedule.

3.2. Launching Seminar and Initial In-depth Study (November 20~27, 2022)

The 2022/23 KSP with Peru was launched through a Kick-off Seminar conducted by QIV Consortium. The seminar participants discussed research topics, gathered requirements, and received feedback from high-ranking officials and ministries in Peru. Meetings with MINCETUR provided insights into SEZ policies and operations, while interviews with trade offices and companies involved in projects in Peru offered valuable perspectives. Visits to the Tacna SEZ and interviews with resident companies provided insights into their experiences. Local experts were selected and assigned with tasks, and future cooperation plans were discussed.

The importance of monitoring project performance and aligning the project with partner ministries' capabilities and the policy environment was emphasized during an interview with the Embassy of Korea in Peru.

Date	November 21, 2022
Time	14:30~17:30
Venue	Conference Room of MINCETUR, Lima, Peru

3.3. KSP Policy Seminar and In-depth Study (March 13~17, 2023, Korea)

The Policy Seminar and In-depth Study served as a platform for Korean and Peruvian researchers to share their research findings with policy practitioners and researchers. Korean researchers examined Korea's experiences with SEZs as a means to revitalize Peru's SEZs and highlighted the roles of central and local governments.

During the policy seminar, the research findings, which emphasized the need for concrete policy proposals to develop practical strategies in the interim and final stages, were discussed with the Peruvian counterparts. Consequently, there were collaborative discussions aimed at internalizing the policy recommendations by integrating the SWOT analysis conducted at the sub-theme level and incorporating Peruvian opinions into the policy research.

Date	March 13~17, 2023
Time	09:00~11:00 (Peru) 23:00~01:00 (Korea)
Format	Video conferencing (Zoom)

The in-depth study was conducted through focus group interviews with Korean researchers, Peruvian government stakeholders, SEZ operating institutions, SEZ-based companies and private companies in Peru based on pre-distributed questionnaires.

3.4. Meeting for Evaluation of Interim Report (April 6, 2023, Korea)

KDI established an evaluation committee and conducted a review meeting to assess the interim reports and provide recommendations for enhancing their quality and gathering research directions.

The evaluation committee, comprised of SEZ specialists, evaluated each topic covered in the interim reports and offered suggestions and guidance to the QIV inspectors for adjustments, improvements, and further data collection. The inspectors and researchers incorporated these evaluation results into the final report.

Sub-topics	Evaluation Advisory Committee
1	Dr. Bokhyun Cho (Topic 1) Professor, Hanbat University
2	Dr. Yul Kwon (Topic 2) Senior Research Fellow, Korea Institute for International Economic Policy (KIEP)
3	Dr. Yune Lee (Topic 3) Professor, Incheon University
4	Dr. Namkwon Moon (Overall) Professor, Hankuk University of Foreign Studies

3.5. Interim Reporting and Policy Practitioners' Workshop (April 24~28, 2023, Korea)

The QIV consortium organized an interim reporting workshop and a policy practitioners' workshop, where Korean and Peruvian researchers discussed their interim findings and preliminary policy suggestions.

The workshop involved senior advisors, Korean researchers, KDI project managers, and Peruvian policy practitioners. The interim report provided an overview of the research background, including the identified problems and their severity, research directions, and the current situation in Peru and Korea related to each subtopic. It also examined Korea's challenges, experiences, and policies in the relevant areas. Provisional policy alternatives were presented, and the feasibility and potential adoption of these proposals by Peruvian organizations were discussed.

Date	April 24~28, 2023
Time	10:00 ~ 13:00
Venue	Ruby Room, The Plaza hotel, Seoul, Korea

Policy Practitioners' Workshop was organized as a program to share success and failure cases of SEZ policy establishment and operation in Korea. Participants visited SEZ-related institutions located in Incheon, Daegu, Masan, and Changwon, over a period of five days to understand the cases, and experts were invited to give presentations.

3.6. Final Report Workshop and Senior Policy Dialogue (July 10~15, 2023, Peru)

A Final Reporting Workshop and a Senior Policy Dialogue were held in Peru to review the final research findings and share them with various participants and opinion leaders representing the Peruvian government, the private sector, academia and the media for more productive results and valuable advice.

At the Senior Policy Dialogue, policymakers from Peru and senior officials from Korea discussed the final policy recommendations and implications based on the final research findings and explored further steps for deriving mutual benefit. The results of the policy proposal were presented in Spanish. More detailed policy recommendations were also presented, as identified in the in-depth study.

Date	July 10~15, 2023
Time	14:00~17:50
Venue	Conference Room of MINCETUR, Lima, Peru

Executive Summary

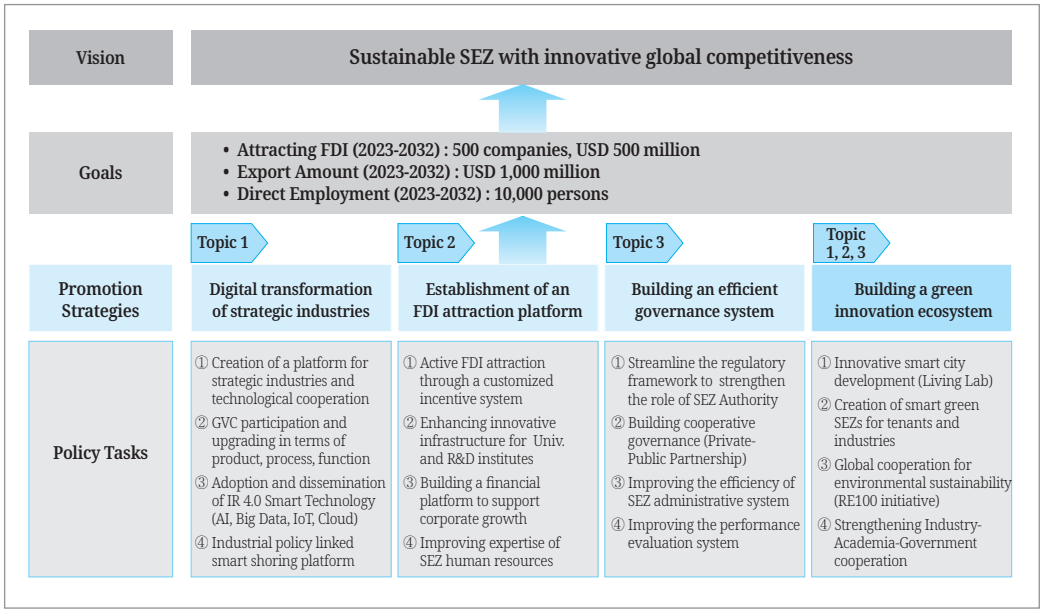
Hee Cheol Moon (Chungnam National University)

Executive Summary

Hee Cheol Moon (Chungnam National University)

The Knowledge Sharing Program (KSP) 2022/23 with Peru explores ways to attract FDI to the Peruvian SEZs. To this end, the KSP team proposes a roadmap for attracting FDI by identifying the constraints, establishing strategies for FDI attraction including incentives, and analyzing new criteria for the selection of SEZs and governance system.

[Figure] Proposed New Model for Sustainable SEZs of Peru



Source: Adapted from MOTIE (2022).

1. Lessons Learned from Successful Foreign Cases and Industry Selection for FDI Attraction

In Chapter 1, the KSP team explores the barriers and challenges faced by Peruvian SEZs in attracting FDI and strives to find reliable solutions at broader levels.

Based on the results of a PEST (Political, Economic, Socio-cultural, Technological environments) analysis, the KSP team identifies strengths, opportunities, weaknesses, and threats that policymakers or regulatory agencies of SEZs may consider. Peru has its own merits in terms of stable macroeconomic policies, a largely open market structure for global trade, and relatively lower price levels. Moreover, Peru also presents opportunities, largely based on its natural resources and related industries. However, the result of PEST analysis shows several limitations or weaknesses in attracting FDI to the SEZs. In addition, there are a few threatening factors in attracting FDI, such as vulnerability to natural and external economic shocks.

The KSP team derives important policy implications for Peruvian SEZs from the case studies on Korea and some other countries. First, it was found that a specialization in a specific industry or strategy is the most important factor for successful FDI attraction. For example, IFEZ in Korea specializes in the fields of pharmaceutical and biotechnology industries and Panama has achieved success with a strategy of forming clusters of high-value-added industries such as aviation and electronics. Secondly, governance structure within a single SEZ or at a collective level is an important factor for successful management of the zones. Thirdly, conformity with development or industrial policies at the national level is a crucial part for a successful SEZ policy, as demonstrated by the early success of Masan FTZ in Korea, which can be attributed to Korea's export-led growth policy.

The KSP team conducted an analysis based on the "Present-Future Model" to determine which industries should be the focus of intensive FDI attraction activities in Peruvian SEZs. The analysis revealed that for the overall Peruvian economy, industries such as Vegetables, Food Products, Textiles and Clothing, and Minerals possess current competitiveness and are also deemed desirable industries for the future, making them the target industries for FDI attraction. Industries such as Machinery, Electrical, Transportation, and Chemicals, while not highly competitive currently, were identified as industries that should be strengthened through FDI for the future of Peru. In addition, the target industries for each SEZ are suggested.

2. Strategy for FDI Attraction Including Incentives and Other Tools

In Chapter 2., the KSP team explores FDI attraction strategies for SEZs in Peru, focusing on incentives and tools to attract overseas investments. The key challenges faced by Peruvian SEZs include low import tariff rates, lack of unique incentives, and a shortage of skilled labor. To overcome these challenges, it is recommended that Peru create more attractive investment conditions and active incentives, such as rent reduction, employment incentives, and improved infrastructure, drawing lessons from Korea's SEZs experience.

The report emphasizes the significance of domestic companies moving into SEZs to enhance competitiveness, leverage technology transfer, and expand opportunities for export. Incentive programs for tenant companies and public-side developers play a crucial role in addressing competitiveness gaps. These incentives include provision of one-stop services such as approval of tenant companies and the active resolution of complaints using the Ombudsman System as done in Korea. The attraction of anchor companies and integration into regional value chains are highlighted as vital strategies.

Drawing insights from Korea's successful SEZs, such as Masan Free Export Zone and Changwon National Industrial Complex, the report suggests key policy recommendations, including government commitment, selection of optimal locations, active attraction of investments, and technology transfer. Moreover, it delves into Korea's strategy for SEZ development, discussing incentives provided in Free Economic Zones, Foreign Investment Zones, and Free Trade Zones, offering valuable insights for Peru's SEZ development.

The KSP team proposes provision of tailored incentive systems, support for domestic enterprises, and the creation of a renewable energy pilot zone as policy imperatives from the perspective of incentives. By implementing these measures, Peru can attract FDI, enhance competitiveness, and foster sustainable economic growth. These recommendations aim to position Peru as an attractive destination for foreign investments and drive overall economic development.

3. Selection Criteria for Peru's SEZs and Improvement of the Governance System

In Chapter 3, the KSP team investigates "Criteria for Selection of Peruvian SEZs and Improvement of the Governance System" to provide the Peruvian government with useful policy suggestions and hands-on recommendations they can utilize when designating new

SEZs or making existing SEZs more sustainable by evaluating SEZ selection criteria in Peru using the AHP/IPA method and examining ways to improve Peru's SEZ governance system in light of the experiences of Korea and other countries worth benchmarking.

According to the results of AHP/IPA from the Peruvian government officials, the SEZ experts, and the CEOs of tenant companies, the Peruvian government officials and the SEZ experts recognized policy feasibility, especially policy imperatives, as the most important criteria for selecting SEZs, but most of the SEZs in Peru do not meet these criteria. Therefore, rather than designating SEZs in a hurry to achieve policy goals such as balanced regional development, policymakers in charge of SEZs need to select and designate special zones in consideration of technological feasibility factors such as operational efficiency and location/infrastructure, economic feasibility factors such as performance and enforceability of special zones, and the needs of (prospective) tenant companies.

Thus, in conclusion, the following policy recommendations are presented from a governance perspective.

① Streamline the legal framework for SEZs: Instead of designating SEZs based on individual laws, it is recommended that Peru enact the "Special Law on the Designation and Operation of Special Economic Zones of Peru" (tentative title). This law would consolidate relevant laws and regulations, streamline administrative procedures, and minimize bureaucratic obstacles.

② Establish transparent criteria for selection, performance evaluation, and cancellation or exit: The selection criteria for SEZs should consider political feasibility (policy compliance and governance), technological feasibility (operational efficiency, location/infrastructure), and economic feasibility (performance, project implementation), and need to be incorporated explicitly into laws and regulations. Additionally, a framework for monitoring and evaluating performance should be established to assess the impact of SEZs on investment, exports, employment, economic growth, and regional development. Furthermore, criteria or procedures should be developed for the cancellation of SEZ designation or the exit of tenants.

③ Enhance coordination and institutional capacity: Improve coordination among government agencies responsible for SEZ administration to ensure consistent implementation of policies and regulations. Strengthen the institutional capacity of these agencies to effectively manage SEZs, including sufficient resources, expertise, and efficient decision-making processes.

④ Compliance with global standards and enhancement of environmental sustainability: Considering global standards, it is essential to incorporate environmental considerations into the governance system of SEZs. This includes implementing stringent environmental regulations, conducting environmental impact assessments, and attracting environmentally friendly companies to strengthen ESG (Environmental, Social, and Governance) management.

⑤ Beyond the knowledge sharing programs: This year as Korea and Peru celebrate the 60th anniversary of diplomatic relations, both countries recognize that it is crucial to pursue mutual collaboration and identify bilateral and multilateral international development cooperation projects. Furthermore, beyond the KSP, proactive measures should be taken to promote mutually beneficial economic cooperation, including joint efforts to attract Korean companies to Peru's SEZs and facilitate their expansion in overseas markets.

Implementing these policy recommendations could improve governance systems in Peru's SEZs, leading to increased investment, economic development, job creation and sustainable growth.

01

CHAPTER

Analysis on Constraining Factors on FDI Attraction for SEZs in Peru and Its Implications

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1. Introduction
2. Economic Status of Peru and Its Policies
3. Constraining Factors on FDI Attraction in SEZ of Peru
4. Case Study of FDI Attractions in Important Countries and Policy Implications
5. Economic Analysis on the Selection of Industries for FDI Attraction in SEZ
6. Conclusion and Policy Recommendations

Keywords
Special Economic Zone, Foreign Direct Investment, National Industrial Development Policy, PEST Analysis, SWOT Analysis

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Summary

This chapter explores the barriers and challenges faced by Peruvian Special Economic Zones (SEZs) in attracting FDI and aims to suggest reliable solutions at broader levels.

After achieving an annual GDP growth rate of 6.2% between 2002 and 2010, the Peruvian economy entered a phase of slow growth. However, Peru has comparative advantages in terms of relatively abundant natural resources such as minerals, hydrocarbons, forests, and others. Furthermore, Peru has implemented its macroeconomic policies, including monetary and fiscal policies, in a disciplined manner.

The KSP team assessed major national economic development plans and their relevance to the strategy to attract FDI for SEZs in Peru. From the analysis, the KSP team derived two significant policy implications. First, there is insufficient support for SEZs and FDI attraction strategies from the central government and constitutional bodies. Each national plan considers the SEZs only at a minimal level and offers no explicit support. Second, there is no clear central authority capable of overseeing the overall operations of SEZs, as many functions are divided among several related institutions.

Utilizing the PEST (Political, Economic, Socio-cultural, and Technological environments)[1] analysis framework, the KSP team categorized the influencing factors into four distinct groups. There is a lack of clear and consistent criteria for determining the location of SEZs. Additionally, there is the issue of overlapping and duplicated local and national regulations governing SEZs, and regulatory approvals and cancellations are not simplified adequately, not only at the level of a single SEZ, but also for individual enterprises.

1 PEST analysis is a management method whereby an organization can assess major external factors that influence its operation in order to strengthen its competitiveness in the market. As described by the acronym, those four areas are central to this model.

In terms of economy, there are three main obstacles to the attraction of FDI to SEZs. Firstly, most SEZs are concentrated in low-level industries, which generate only a modicum of value-added in exports. Secondly, regarding the enhancement of services offered to investors in the SEZs, customs and infrastructure are not sufficiently developed to facilitate trade. Thirdly, in improving the economic incentive framework for the SEZs, absence of simplified labor provisions and incorrectly calibrated tax incentives present hurdles.

Based on the results of our PEST analysis, the KSP team has identified strengths, opportunities, weaknesses, and threats that policymakers or regulators of SEZs should consider. The previous PEST analysis shows several limitations or weaknesses in attracting FDI to the SEZs. In addition, there are a few threatening factors in FDI attraction, such as vulnerability to external economic and natural shocks.

Next, the KSP team examined cases of FDI attraction in SEZs of South Korea and three major Latin American countries. From the intensive case studies, several important policy implications for Peruvian SEZs were derived. Firstly, a specialization in a specific industry or strategy is the most important factor for successful FDI attraction. Secondly, sound governance structure within a single special economic zone or at a collective level is essential for successful management of the zones. Thirdly, conformity with development or industrial policies at the national level is a crucial part for a successful SEZ policy.

In the last part of the chapter, the KSP team conducted analyses to determine which industries should be the focus areas for intensive FDI attraction activities in Peruvian SEZs. To do so, an analytical framework that considers two aspects was established: industries that currently possess competitiveness and industries that are desirable for the future Peruvian economy. The KSP team named this framework as the “Present-Future Model.”

To identify industries with current competitiveness, the KSP team conducted extensive analysis of Peruvian export data. The KSP team utilized UN COMTRADE data for the overall Peruvian economy, and the data provided by MINCETUR (Ministerio de Comercio Exterior y Turismo; Ministry of Commerce, Export and Tourism) for each SEZ. Then, the share of each industry’s export in the total export value of all industries was calculated and ranked accordingly. This ranking was used as the current competitiveness index. To identify promising industries for the future, surveys among government officials and SEZ experts regarding the importance of each industry were conducted. The average scores for each industry were ranked in descending order. This ranking served as an index to identify desirable industries for the future.

The results show that for the overall Peruvian economy, industries such as Vegetables, Food Products, Textiles and Clothing, and Minerals possess current competitiveness and are deemed desirable industries for the future, making them the target industries for FDI attraction. Industries such as Machinery, Electrical, Transportation, and Chemicals, while not highly competitive currently, should be strengthened for the future of Peru.

1. Introduction

Peru has been one of the most open economies in Latin America, and its economic performance depends heavily on international trade. Owing to its unique business-friendly environment for foreign investors, such as advanced and systematic macroeconomic policies and relatively cheaper costs for business inauguration, Peru has become one of the most favorable destinations for Foreign Direct Investment (FDI, hereafter) in recent years.

To strengthen FDI attraction, stimulate trade volumes, and support regionally balanced economic growth, the Peruvian government introduced Special Economic Zones (SEZs, hereafter) in various areas. The government aimed to enhance the country's economic prosperity through the SEZs by achieving objectives such as reducing logistical barriers and regional imbalances and stimulating the positive effects of infrastructure and technology.

However, the recent performances of the SEZs have been modest. Only four of all SEZs are in operation, and the economic contribution of these four SEZs is below expectations. Despite the government's efforts to attract FDI to the SEZs, not only has the overall volume of FDI decreased in the Zones, but also the volatility of FDI inflows has worsened.

This report examines the barriers and challenges faced by Peruvian SEZs in attracting FDI and aims to suggest reliable solutions at broader levels. In the second section, this report briefly overviews the macroeconomic conditions of the Peruvian economy and summarizes the important long-term economic plan related to the SEZs. Next, the report analyzes the constraining factors that hamper possible FDI inflows into the country's SEZs using various research methodologies. In the fourth section, the Knowledge Sharing Program (KSP) team lists several countries that have been successful in attracting FDI into their SEZs in recent times and derives policy implications from the study. In the fifth section, the KSP team suggests the optimal industries to be operated in the SEZs for FDI attraction. The last section concludes by presenting some policy implications.

2. Economic Status of Peru and Its Policies

2.1. Current Economic Status of SEZ and FDI in Peru

Peru is a small open economy that relies heavily on primary industries such as mining, agriculture, a few manufacturing sectors, and tourism, which form the basis of its exports. Mining and hydrocarbons account for approximately 14.4% of the Gross Domestic Product (GDP) and are the primary sources of tax revenue that support government expenses.

2.1.1. General Information and the Current Economic Status of Peru

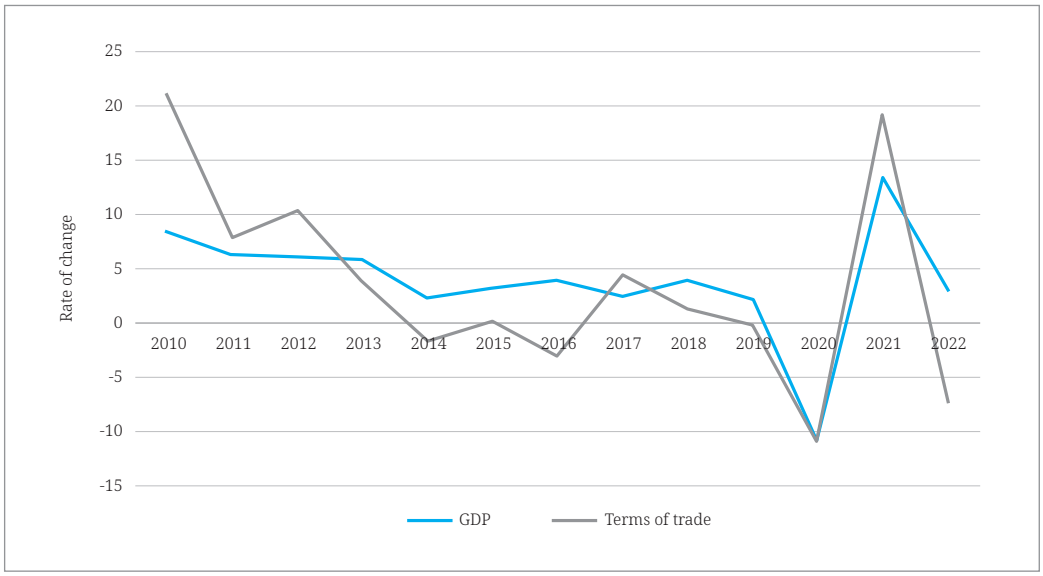
2.1.1.1. GDP

After achieving an annual GDP growth rate of 6.2% between 2002 and 2010 on account of the significant economic reforms of the 1990s and the general boom of the world economy, the Peruvian economy entered a phase of slow growth. The current trend of slow economic growth raises concerns about a potential slowdown in the growth rate. This necessitates the identification of new drivers to fuel further growth. Peru being a small open economy highly dependent on international trade of raw materials, drops in the terms of trade due to the slowdown of the world economy, including China and the European Union, which are Peru's main trading partners, presented impediments to the country's economic performance (See Figure 1-1). While the annual growth rate of the Terms of Trade (TOT) between 2002 and 2010 averaged 8.0%, the rate dropped to 2.0% since then (2011-2022).

As of 2022, the largest portions of GDP were mining and hydrocarbons (14.4%), manufacturing (16.5%), agriculture (6.0%), construction (5.1%), and commerce (10.2%). Looking at types of expenditure, between 2010 and 2021, GDP growth was sustained based on private consumption (64%) and private investment (20%). Meanwhile, since public investment accounts for only 5% of GDP, a fourth of private investment, the capacity of countercyclical macroeconomic policy to offset the biggest economic downturns (2008 Global Financial Crisis and 2020 COVID-19 pandemic) was limited.

[Figure 1-1] GDP and Terms of Trade

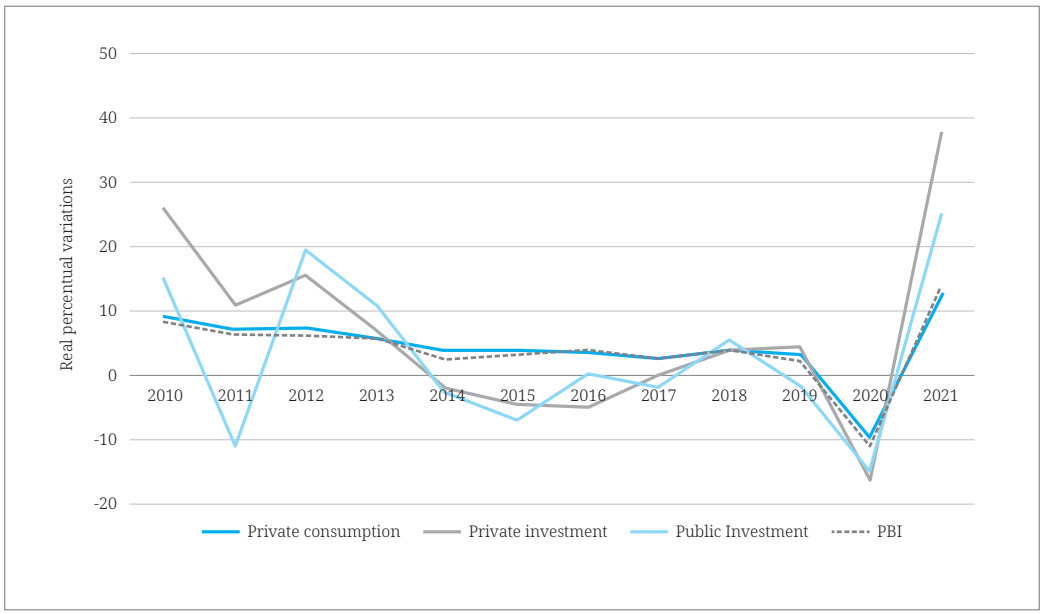
(Unit: %)



Source: Adapted from Central Reserve Bank of Peru Statistics (https://www.bcrp.gob.pe/en/statistics.html, accessed on May 18, 2023).

[Figure 1-2] GDP Growth by Type of Expenditure

(Unit: %)



Source: Adapted from Central Reserve Bank of Peru Statistics (https://www.bcrp.gob.pe/en/statistics.html, accessed on May 18, 2023).

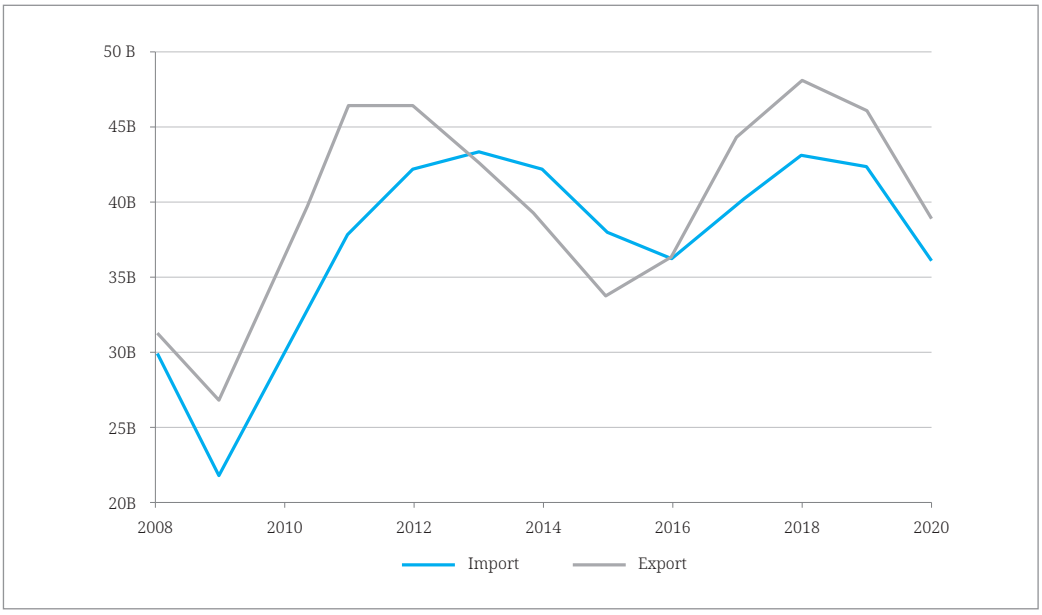
2.1.1.2. International Trade

In the first decade of the 2000s, there was a trend of high growth in the Peruvian economy, with exports of goods growing more than eight times, from 7,714 million USD in 2002 to 63,151 million USD in 2021, with an average annual growth of 11.7%. However, this trend became more volatile since 2010, largely due to a combination of negative external and internal factors (See Figure 1-3).

The Peruvian economy has a comparative advantage in terms of relatively abundant natural resources such as minerals, hydrocarbons, forests, and others. In the Peruvian statistical system, exports related to these types of resources are called 'traditional exports' (representing 74% of total exports in recent years). 'Non-traditional exports' (26% of total exports) have become more dynamic in recent years. Some sectors are based on natural resources, while others are industries either related to mining resources, such as metal-mechanical products, steel, and jewelry, or related to the cultivation and traditional processing of cotton, as is the case of the textile sector.

[Figure 1-3] Export and Import Trends

(Unit: USD)

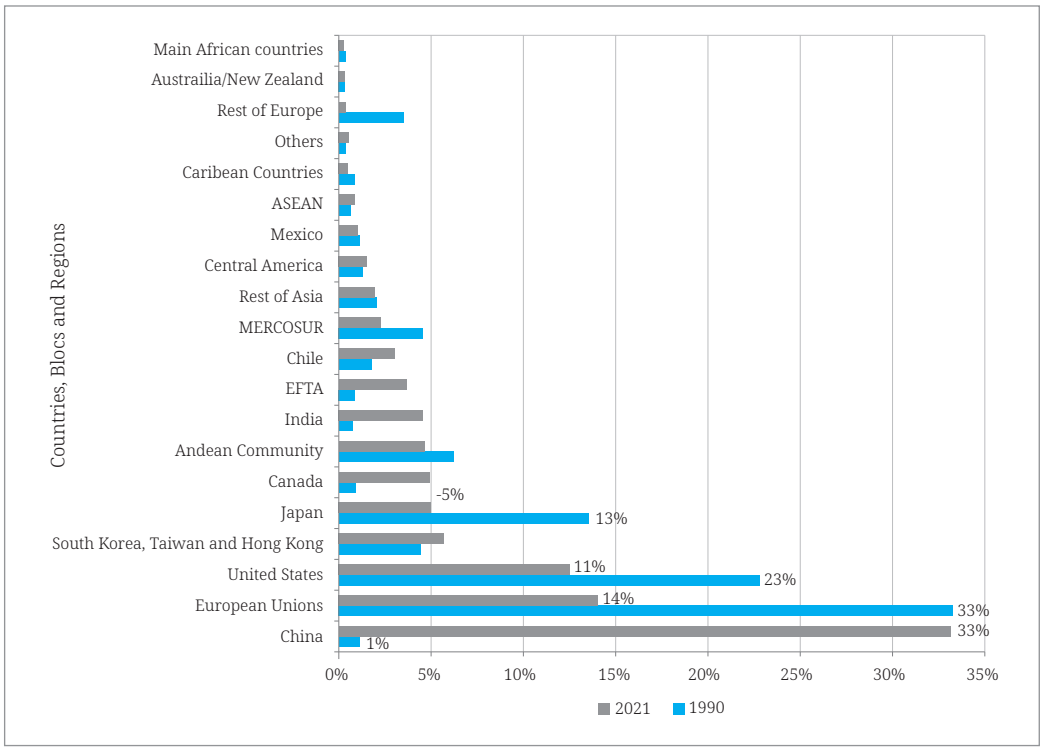


Source: Adapted from World Integrated Trade Solution (https://wits.worldbank.org/, accessed on May 19, 2023).

Regarding the destinations of Peru's exports, in 1990, about 70% of exports were directed to the most westernized countries, such as the United States (22.8%), the European Union (33.3%), and Japan (13.5%), while China accounted for only 1.1%. Three decades later, the concentration of destinations changed significantly, and China became Peru's primary trading partner, with a 33.1% share in 2021, while the export share of the European Union dropped by 19 percentage points, accounting for only 14%. The shares of the US and Japan also reduced to 12.5% and 5.0%, respectively (See Figure 1-4).

[Figure 1-4] Export Destinations: 1990 vs 2021

(Unit: %)



Source: Adapted from Ministry of Economy and Finance Statistics (https://rb.gy/6k49p, accessed on May 20, 2023).

2.1.1.3. Macroeconomic Policy

Peru has implemented its macroeconomic policies, such as monetary and fiscal policies, in a disciplined manner since the 1990s when an economic stabilization plan was implemented to address hyperinflation. The Central Reserve Bank of Peru is an autonomous monetary policy maker with the goal of stabilizing the economy. In 2002, the bank introduced a rule to contain inflation with a target annual inflation rate of 2%. To anchor inflation expectations from the private sector, the bank has been operating a variety of policy tools such as reserve interest rates (open market operations) and public

announcements (forward guidance). In the last 20 years, The Peruvian Central Bank has been quite successful in curbing its inflation rate under 4% for most years, except during a few extraordinary crisis periods such as the 2008 Global Financial Crisis and the COVID-19 Pandemic in 2020-22.

On the fiscal policy side, since 1999, the Non-Financial Public Sector has been required to comply with a set of macro-fiscal rules to maintain fiscal stability. These rules set ceilings for total gross public debt, public deficit, total non-financial expenditure, and current expenditure of the general government. While the fiscal rule promotes long-term fiscal sustainability in developing countries, it can impede the policy flexibility and resilience of fiscal authorities. This is particularly notable when newly developed industries or areas necessitate the formation of supporting functions, -such as attracting FDI in SEZs. Overall, while Peru's macroeconomic stabilization policies are fundamentally sound, they have a rather limited capacity to support a strategy for attracting FDI to SEZs.

2.1.2. Current Economic Status of Special Economic Zones in Peru

Currently, there are four operational Special Economic Zones (SEZs) in Peru: three Special Development Zones (SDZs) established in 1996, located in Ilo, Paita, and Matarani, along with the Tacna Free Trade Zone (FTZ), established in 1990. Additionally, there are four special zones, two SDZs in Tumbes and Loreto, one SEZ in Puno, and one FTZ in Cajamarca that were created but are currently not operational.

<Table 1-1> Special Economic Zones in Peru

Location	Name	Year Created	Status	Decree of Law
Tacna	FTZ	1990/2002	In Operation	Law 27688
Paita	SDZ	1996	In Operation	DL No. 864
Ilo	SDZ	1996	In Operation	DL No. 842
Matarani	SDZ	1996	In Operation	DL No. 842
Puno	SEZ	2006	No Operations	Law 28864
Tumbes	SDZ	2011	No Operations	Law 29704
Loreto	SDZ	2013	No Operations	Law 26953
Cajamarca	FTZ	2021	No Operations	Law 31343

Source: IMF (2022).

Both SDZs and FTZs in Peru are open to various types of businesses, since the country does not follow a policy of establishing specific types of industries selectively within the SEZs. This encompasses a wide range of manufacturing activities, including assembly, logistics,

and trade. However, certain businesses are strictly prohibited, such as specific industries enumerated on a so-called 'negative list,' including oil and flour manufacturing. Importantly, there is no minimum requirement to join a SEZ in Peru, in contrast to neighboring countries such as Colombia and Costa Rica that have stricter membership prerequisites.

Companies that establish themselves in Peru's Special Economic Zones (SEZs) benefit from extensive tax exemptions, except for social security contributions. These tax benefits primarily include exemptions from the General Sales Tax (Impuesto General a las Ventas: IGV), Selective Consumption Tax (Impuesto de Promoción Municipal: IPM), and Excise Tax (Impuesto Selectivo al Consumo: ISC) on goods produced for export, as well as waivers on tariffs and customs duties for imported items. Furthermore, companies operating within SEZs are granted a full income tax exemption, along with an exemption from withholding tax on dividends distributed to their shareholders.

The economic outcome of the SEZs has been modest since the start of operations. As of 2019, the total export share from SEZs in Peru was under 1%[2], which stood in stark contrast to countries like the Dominican Republic, Nicaragua, and Costa Rica, where SEZs currently contribute around 40% to the total export share. According to UN (2019), the four SEZs in Peru rank among the lowest in terms of the share of Foreign Value Added (FVA) in exports among Latin American and Caribbean countries, registering only 10%. This is in sharp contrast to countries like Mexico, which recorded a 30% share in FVA, and Chile, which recorded 23%.

2.1.3. Recent Volatility of Foreign Direct Investment Inflows

The economic stabilization at the beginning of the 1990s entailed drastic changes in economic policy, including constitutional reforms, which provided greater certainty to investors in general. These changes included the establishment of an advanced system for the central bank, equal opportunities for foreign investors, a well-established market economy, the State being relegated to a subsidiary role, the freedom to submit investor-state disputes to international institutions, and the freedom to possess foreign currency, among others.

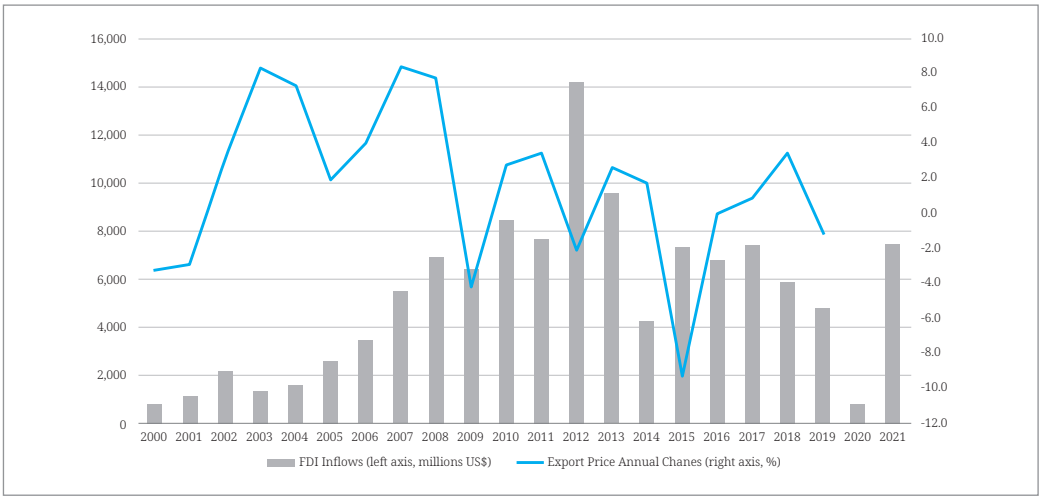
Over the last two decades, FDI inflows into Peru have generally been procyclical with fluctuations in export prices, given the country's heavy reliance on international market prices for natural resources and other major export goods (See Figure 1-5). FDI

2 According to IMF (2022), in 2018, the four active SEZs generated US$47 million in exports and created over 1,400 direct jobs. This is a very small fraction of Peru's economic activity.

inflows reached a peak of just over US$ 14 billion in 2012 due to capital contributions to companies, reinvestment of profits, and a higher balance of medium and long-term private debt. However, FDI inflows declined subsequently, amid falling prices for primary export goods, which were further exacerbated by the corruption scandals and political instability associated with the Lava Jato case that began in 2016, followed by the pandemic that began in 2020.

FDI inflows recovered between 2021 and 2022, largely due to the reinvestment of profits, which were closely linked to the high commodity prices of 2021, representing the largest increase in the last ten years, and investment in debt instruments.

[Figure 1-5] FDI Inflows and Export Prices, 2000~2022



Source: Adapted from the World Bank and Penn World Table 10.0 (https://www.rug.nl/ggdc/productivity/pwt/?lang=en, accessed on June 2, 2023).

2.2. National Level Economic Policies and Strategies

The KSP team assessed major national economic development plans and their relevance to the FDI attraction strategy in SEZs. Notable logistics plans, such as Transport Logistics Services Development Plan, or macro-level, long-term national plans, such as the Bicentennial Plan, were studied meticulously. From the analysis, the KSP team derived two significant policy implications. First, there is insufficient support for SEZs and FDI attraction strategies from the central government and constitutional bodies. Each national plan considers the SEZs only minimally and offers no explicit support. Second, there is no clear central authority capable of overseeing the overall operations of SEZs, since many functions are divided among several related institutions.

2.2.1. Plan for the Development of Transport Logistics Services

In 2019, the Ministry of Transport and Communications published the "Transport Logistics Services Development Plan (TLSDP)" as a tool for analyzing, evaluating, planning, and promoting solutions to the main challenges in transport, logistics, and industry in Peru, with the aim of improving the country's competitiveness. The Plan defines various future scenarios for the economy, giving great importance to aspects related to the national logistics system.

The Plan is designed in three phases:

① Creating a strategic development framework for a sustainable and effective logistics scheme: This scheme aims to integrate Peru's unique potentialities and promote the global competitiveness of national products in the international trade market.

② Identifying the development needs or potential evolution of various types of logistics centers and platforms and integrating existing elements from different modes of transport: The goal is to propose, plan and establish a network of infrastructure and integrated logistics services throughout Peru, in line with international best practices and the guidelines set by the national government.

③ Supporting the development and consolidation of an integrated, intermodal logistics infrastructure that includes road, rail, port, and airport facilities: These infrastructures, operating at advanced levels in different strategic nodes of Peru, will serve as centers with potential for value-added services and logistics activities.

The Plan reviews several prior studies and plans at the national level that provided relevant background information for analyzing the development of the logistics and transport sector. In relation to SEZs, the plan briefly examines the MINCETUR investigation study on SEZs and Logistics Activity Zones[3]. However, it derives minimal policy implications or supportive plans related to the FDI implementation strategy within the SEZs.

2.2.2. Bicentennial Plan: Peru towards 2021

"The Bicentennial Plan: Peru towards 2021" is a long-term economic development plan prepared in 2011 by the National Center for Strategic Planning. This Plan proposes national development policies up until 2021. Representatives of central government entities, regional

3 This study was prepared within the framework of the Support Project to Improve the Productive Offer and Improve Competitiveness.

governments, constitutionally autonomous bodies, and private entities participated in formulating the Plan. The Plan does not set annual quantitative goals as its primary purpose is to provide general guidance for economic development strategies.

The Plan identifies national objectives in six areas: fundamental rights and dignity of the people; opportunities and access to services; State and governance; economy, competitiveness, and employment; regional development and infrastructure; and natural resources and environment.

The Regional Development and Infrastructure Plan (the fifth element on the list), which shares a common purpose with the implementation of SEZs, underscores the importance of supporting economic corridors. However, it does not explicitly mention SEZs in any of its provisions. In its policy guidelines, the Plan emphasizes the vital role of regional governments in promoting investment in transport and energy infrastructure, development of human capital, and technological and productive innovation. The aim is to increase regional labor productivity in agriculture, agro-industry, and manufacturing industries. However, the Plan does not assign any role to SEZs in these recommendations.

2.2.3. National Export Strategic Plan (Plan Estratégico Nacional Exportador: PENX)

The PENX is a national plan designed for the expansion and diversification of the export sector, prepared and supervised by the Ministry of Foreign Trade and Tourism (Ministerio de Comercio Exterior y Turismo: MINCETUR). The latest version of PENX, drafted in 2015, is "PENX 2025". This version integrates the institutional roles of other essential sectors beyond the purview of MINCETUR. Participating institutions include Fund for Innovation, Science and Technology, the Research and Development Fund for Competitiveness, and the MSME Fund.

"PENX 2025" outlines the following strategic objectives: deepening the internationalization of domestic companies; ensuring sustainability and diversification in the exports sector with value-added goods and services; and improving the competitiveness of the exports sector.

In terms of facilitating international trade and improving the efficiency of global supply chains, the Plan addresses the importance of promoting interoceanic corridors and overcoming impediments caused by insufficient and expensive logistics infrastructure. However, it neither mentions SEZs specifically nor provides significant policy recommendations related to FDI attraction strategies.

2.2.4. National Competitiveness and Productivity Plan

"The National Competitiveness and Productivity Plan (Política Nacional de Competitividad y Productividad: PNCP)" was prepared by the National Competitiveness and Formalization Council (Consejo Nacional de Competitividad y Formalización: CNCF), with its latest version released in 2019. The CNCF is comprised of the Board of Directors and the Technical Secretariat, with the former serving as the highest deliberative and decision-making body. The Board of Directors is headed by the Minister of Economy and Finance and also includes representatives from other public entities and private associations.

The goal of the PNCP is to connect the country's vision, as defined by the plan, with the implementation of necessary policy measures to guide the nation towards that vision. However, realizing this goal necessitates the involvement of public and private agents who lead economic and social activities. To prepare the plan, the CNCF coordinated with the Public-Private Technical Committees (Comites Tecnicos Publico Privado: CTPP), holding workshops and meetings with members of various public and private institutions, unions, academia, and civil society.

The PNCP outlines objectives in nine priority areas, from which transversal measures are deduced. These priority areas are: infrastructure, human capital, innovation, financing, labor market, business environment, foreign trade, institutions, and environmental sustainability.

The Plan makes a notable mention of SEZs, particularly in the section outlining the objectives for international trade. The Plan proposes measures designed to attract foreign investment and stimulate regional economic growth. Further, it also introduces a national-level management system, termed the National System of Special Economic Zones. This system aims to bolster both public and private administrative and operational management of private operators through improvements in the regulatory framework. The passage of the Framework Law for Special Economic Zones in December 2019 marked a significant milestone for the Plan. The National SEZ System was expected to be implemented by July 2021, with its management significantly strengthened. However, the law is yet to be enacted, and thus far, there has been no tangible improvement in the management efficiency of SEZs.

2.2.5. National Industrial Development Policy (PNDI)

"The National Productive Development Plan (Política Nacional de Desarrollo Industrial: PNDI)," which was supported by the Inter-American Development Bank (IDB) and

was announced in November 2022 by the Ministry of Production, aims to promote the development of the manufacturing industry in Peru. Its goal is to reinforce technological capabilities, complexity, and diversity in the country's industry to achieve economic growth, by addressing existing market failures and improving competitiveness.

To improve manufacturing competitiveness, the PNDI proposes four priority objectives:

- **Increase the productivity of companies in the manufacturing sector.** The PNDI suggests coordinating job training and education programs to develop the necessary human capital for the industry. It also recommends providing entrepreneurs with financial and tax incentives to encourage business formalization and the acquisition of infrastructure to create and promote promising manufacturing centers.

- **Increase the complexity of products in the manufacturing sector.** The PNDI proposes identifying industrial branches and/or products with comparative advantages based on factors such as availability raw material, unused installed capacity, geopolitical location, agricultural diversity, and clean and safe energy sources.

- **Increase production infrastructure and specialized services adequately for manufacturing companies.** The PNDI recommends increasing the availability of suitable physical spaces for manufacturing processes, especially for sectors that have not seen significant increases in productivity by substitution between labor and capital.

- **Improve the quality of the institutional and regulatory environment for the development of manufacturing activities.** The PNDI recognizes the importance of consistent institutional support over time to facilitate industry development, and cites successful examples of institutional support in the salmon industry in Chile and agribusiness in Peru.

The PNDI identifies the scarcity of production infrastructure and specialized services as a significant obstacle to industrial development in Peru. To address this, the plan recommends that the Ministry of Production coordinate with the Ministry of Foreign Trade and Tourism to attract infrastructure investments to the SEZs[4]. However, the PNDI does not provide further guidance on this recommendation, and does not offer any institutional or regulatory support plan for strengthening infrastructures in SEZs.

4 See pages 82, 85, 89, 112 and 352 of the PNDI.

3. Constraining Factors on FDI Attraction in SEZ of Peru

3.1. PEST and SWOT Analysis on FDI Attraction in SEZ of Peru

The KSP team employed mainstream research methodologies to identify obstacles to Foreign Direct Investment (FDI) within Peru's Special Economic Zones (SEZs). Utilizing the PEST analysis framework, the KSP team categorized the influencing factors into four distinct groups: Political, Economic, Socio-cultural, and Technological aspects. After conducting rigorous literature reviews and data collection and detailed analysis, the KSP team created comprehensive on-site survey questionnaires. These questionnaires were distributed among Peruvian government officials, tenants, and SEZ experts, from whom the KSP team received insightful feedback. Additionally, the KSP team conducted in-depth interviews with government officials at MINCETUR. The KSP team utilized this qualitative and quantitative data to uncover significant implications in our PEST analysis. Based on the result of PEST analysis, the KSP team drew a simple SWOT analysis, which categorized strengths, weaknesses, opportunities, and threats of Peru's SEZs.[5]

3.1.1. Analysis of PEST Factors

3.1.1.1. Political and Institutional Environment

Since Peru's return to democracy in 1980, especially after the transitional government under Valentin Paniagua and Alejandro Toledo in early 2000's, the country has been steadily gaining positive reputation with regard to the stability and soundness of its macroeconomic stabilization policies. Monetary policy has been designed for controlling inflation, and the fiscal authorities have been cautious about possible overly expenditures and have successfully controlled the overall budget during economic fluctuations. This fundamental policy support is crucial to the success of industrial level strategies such as SEZs. Another positive aspect of Peru's institutional environment is its efficient legal framework governing business registration. A detailed evaluation is provided in the next subsection.

Although there have been improvements to the legal and regulatory framework in the last several decades, the KSP team identifies the following potential obstacles in the political and institutional dimensions based on policy research and interviews with related parties, such as tenant firms, SEZ management corporation, and central government officials.

5 The KSP team would like to clarify that the research methods used in this study (PEST, SWOT, GI-Hub, BCG/PF) were proposed by the research team and subsequently finalized and used in consultation with the evaluation committee and Peruvian officials at the planning document evaluation stage and the intermediate report evaluation stage.

Firstly, there is a lack of clear and consistent criteria for determining the location of SEZs. As indicated in various official documents released at the time of establishing the SEZs, the zones were selected with the intention of promoting balanced regional economic growth. This is in contrast with an alternative approach of maximizing the economic efficiency of exporting Peru's most competitively advantageous goods or services. As will be discussed in depth in the next section, many countries comparable to Peru in terms of economic development, size, or structure, such as Panama and Brazil, have adopted criteria leaning towards increasing efficiency for their SEZs, such as strategic clustering or industrial specialization. However, in the case of Peru, questions have been consistently raised about why the eight regions were selected and which industries should have been strategically fostered.

Secondly, there is the issue of overlapping and duplicated local and national regulations within the SEZs. This will be thoroughly examined in Chapter 3, where the KSP team proposes an institutional reform plan aimed at improving the efficiency of FDI attraction for the SEZs. In the current landscape, the laws and orders governing Peru's SEZs are notably vague, leaving room for excessively discretionary decisions. Furthermore, regulatory oversight is overlapped and divided among various institutions, leading to a fragmentation of supervisory power. These issues of redundancy and confusion in the regulatory structure inhibit the effective management and growth of the SEZs, indicating a clear need for streamlined institutional reforms.

Thirdly, regulatory approvals and cancellations are not sufficiently simplified, not only at the level of an SEZ, but also for individual enterprises. Our research found no clear criteria in any government document or related law for the cancellation of a SEZ or an enterprise already established within a SEZ. The lack of institutional support for these administrative decisions could impede the promotion of economic flexibility and efficiency of firms in the SEZs, consequently hampering the attraction of potential FDI.

Lastly, there is an ongoing global concern about the political instability in Peru, which could pose additional geographical risk for potential foreign investors. Recent volatile changes in government raise questions about the consistency of administrative functions, including institutional support from the central government for regional ones. If government bodies are heavily influenced by bipartisan political parties with reform plans that veer toward extremes, the continuation of the national development plan, including the promotion of SEZs, may also be affected negatively.

3.1.1.2. Economic Environment

One of the main strengths in terms of the economic environment of Peru, related to the SEZs, is its wide openness to the world economy, and Peru has had comparative advantages in terms of natural resources and cheaper labor costs as well as efficient allocation of resources. Abundance in many natural resources has given Peru a massive opportunity to strengthen its economy faster than expected, and cheaper price level compared to its competitor countries has reinforced Peru's comparative advantage. Rental prices in business and labor costs in unskilled and skilled labor markets are also relatively cheaper, which make Peru's SEZs more attractive.

As discussed above, the official, main objective of SEZs is to stimulate regional development, but different institutions pursue different economic goals, which causes fragmentation of supervisory power and, moreover, economic inefficiency in the areas. The KSP team derives the following potential economic obstacles to FDI attraction in SEZs.

Firstly, most SEZs are concentrated in low-level industries, which generate only a modicum of value-added in exports. For example, according to a 2016 evaluation by the World Bank, the Tacna area, identified as the most successful SEZ in Peru, attracted 51 investors from Peru, Colombia, and China, with logistics being the main activity (32 companies). Further, 70% of the manufactured products were sold tax-free in the local market through the Tacna Commercial Zone, while 30% were exported. However, 60% of these companies ceased operations within the first three years. In 2021, Tacna's FTZ (ZOFRATACNA) exported a total of US$ 4.1 million worth of goods, of which 83% were chemical products. Despite this success, the manufacturing sector in the Tacna region only accounts for 3.5% of the gross value added, to 47.4% for mining, according to the National Institute of Statistics and Informatics (Instituto Nacional de Estadística e Informática: INEI).

Another case is Zed Paita, which attracted 19 investors specializing in food processing (only one is a foreign company), creating 1,200 direct jobs. The main activity in this SEZ is the storage of goods with suspended tariffs. As of 2021, exports amounted to US$75.3 million, with 38.8% being chemical products, 38.5% agro-industrial products, and 21.2% fishing products. This is somewhat consistent with the fact that in the Piura region, the total percentage of the gross value-added generated by agriculture, fishing-aquaculture, and manufacturing is 24.4%.

In the case of Zed Matarani, as of 2016, there were only 17 firms (mainly logistics service companies; warehouses; companies engaged in repair of mining equipment; and companies

oriented towards agro-industrial exports, residuals processing, and light industry). The region's exports in 2021 were US$4.6 million, with 39.7% being agro-industrial products, 36.6% fishing products, and 23.6% chemical products.

Secondly, regarding the services offered to investors in the SEZs, there are deficiencies in trade facilitation at customs and in infrastructure provision. Many tenant firms have consistently complained about the lack of infrastructure and insufficient supporting facilities in their SEZs, even including supply of water and electricity. Lack of fundamental and basic infrastructure is a significant discouraging factor, putting Peru at considerable disadvantage compared to neighboring countries in attracting FDI.

Thirdly, in improving the economic incentive framework of the SEZs, incorrectly calibrated tax incentives and the absence of simplified labor provisions are found. The most significant economic incentive for enterprises is tax exemption. According to the IMF (2022), the legal framework of SEZs includes a broad exemption for all "taxes created and to be created." However, this generous tax exemption program alone has not boosted economic performance to the anticipated high level, as pointed out in the previous section.

The recently published report by the Center for Economic Research and Global Business (Centro de Investigación de Economía y Negocios Globales) concludes that the tax privileges granted to SEZs are not sufficiently attractive for investment, since the zones lack additional factors essential to business success. According to the report, the tax benefits alone are insufficient to compensate for these deficiencies and cannot generate successful investment dynamics independently. The report also argues that the geographic location of the SEZs is a significant negative factor, as these zones lack social development and infrastructure, skilled labor, and networks of suppliers, which are crucial conditions for the development of business activity and foreign investment.

3.1.1.3. Socio-Cultural Environment

The main obstacles to FDI attraction in social and cultural dimensions are twofold: the lack of specialized labor supply directed towards the SEZs, and relatively high levels of poverty in the regions.

In terms of education, there are differences in educational quality between regions. Considering the average years of study achieved by the population aged 15 and over, by 2021, the regions of Moquegua, Arequipa, and Tacna have one of the highest averages (between 10.8 and 11.1 years), even compared to the Lima region. However, in our

interviews and surveys, many tenants complained that it is extremely difficult to find qualified workers or foreign investment experts in the regions, due to the lack of high-level educational institutions related to these fields and the considerable distance from the most populated cities in the country.

Demographically, according to the 2017 INEI census figures, the entire population of the regions where the four operating SEZs are located represents only 12.7% of the country's total population. Piura and Arequipa have the largest shares in the total, with 6.3% and 4.7% respectively. Even though the Tacna SEZ accounts for only 1.1% of the country's population and lacks a port, it is more dynamic than the other SEZs mainly because it is closely linked with the Tacna Commercial Zone, which sells many of the products that are imported into the free zone.

Considering poverty levels where the SEZs are located and using the poverty range of Metropolitan Lima (23.9%-28.6%) as a reference (INEI 2020), the Tacna region has a poverty level in the same range as Lima, while the Piura region has a higher poverty rate (31.3%-34.6%) and those of Arequipa and Moquegua have lower poverty rates (both between 15.1% and 19.5%). The generally high poverty level in entire Peru is a potential drawback for the development of foreign investment, especially in SEZs.

3.1.1.4. Technological Environment

The biggest obstacle in terms of the technological environment is access to high-speed internet. According to INEI data from 2021, the regions of Arequipa, Tacna, and Moquegua had similar levels of internet penetration to Lima (66.3%, 60.6%, and 58.6%, respectively), while the Piura region lagged behind at 38.7%. However, in interviews with tenants and SEZ experts, they pointed to a lack of high-speed internet access, which has been identified as a major factor in delaying business activity for active users and discouraging entry into the SEZs for potential enterprises.

In broader scope, Crespi and Castillo (2020) identified several problems with the science and technology policy, including a lack of coordination, overlapping functions, and duplication of actors and systems. The basic institutional framework consists of the National System of Science, Technology, and Technological Innovation (Sistema Nacional de Ciencia, Tecnología e Innovación Tecnológica: SINACYT) and the National Council of Science, Technology, and Technological Innovation (Consejo Nacional de Ciencia y Tecnología: CONCYTEC), which are attached to the Presidency of the Council of Ministers (PCM). The PCM is the entity responsible for designing and coordinating the National Plan for Science

and Technology, and directing, coordinating, and evaluating the activities of the entire public sector in these matters. However, there is no strategic actor that proposes guidelines or national priorities for science and technology in the medium and long term.

3.1.2. SWOT Analysis Based on PEST Results

Based on the results of our PEST analysis, the KSP team has identified Strengths, Opportunities, Weaknesses, and Threats that policymakers or regulators of SEZs should consider (See Table 1-2). Overall, Peru has several merits such as stable macroeconomic policies, such as a successful monetary policy regime, a largely open market structure for global trade, and relatively lower price levels, including rent prices, which provide a positive incentive in terms of the cost of starting a business. These traits can be described as strengths in attracting FDI.

Additionally, Peru also presents opportunities, largely based on its natural resources and related industries. Abundant natural resources and low labor costs are the main comparative advantages that Peru has in international trade competition, and there is room for the development of related industries based on these strengths. Attracting foreign investment to higher value-added manufacturing industries that build upon these first-generation industries may be a reasonable strategy.

On the other hand, the previous PEST analysis reveals several limitations or weaknesses in attracting FDI to the SEZs. In the legal and institutional dimension, a lack of clear and consistent criteria for determining the location of SEZs can be highlighted as the first issue. Overlapping and duplicated local and national regulations, as well as insufficient simplification of regulatory approvals and cancellations, pose additional limitations. From an economic perspective, the main weakness is the heavy concentration of low-level industries that generate minimal value-added in exports in most regions. Deficiencies in trade facilitation, infrastructure provision, and the absence of well-calibrated tax incentives are also problematic. In a social context, the main weaknesses are the lack of FDI experts in the regions and an overall high poverty level. The limited access to high-speed internet has been widely mentioned as a technological limitation in the SEZs.

There are a few factors posing threats to FDI attraction. Firstly, due to its small open economy structure, Peru is vulnerable to external economic shocks. The recent high volatility in FDI inflows serves as a good example. Peru is highly dependent on exports of natural resources, which are sensitive to price fluctuations in international markets. Foreign investors may be reluctant to enter the Peruvian SEZs given the volatility of these prices.

Secondly, Peru is also vulnerable to natural disasters such as the El Niño phenomenon, which can lead to excessive rainfall and floods that damage crops and public and private infrastructure, resulting in a negative impact on output and employment. Thirdly, there is growing concern over the rise in social and political unrest in the country, particularly in the southern region where three of the SEZs are located. This instability potentially reduces the attractiveness of investment.

Another issue to address is climate change across the country. In the year 2023, Peru experienced an extraordinarily warm winter season in July, primarily influenced by El Niño. These dramatic climate changes could potentially attract a few new industries, such as healthcare services or heavy equipment for restoration. However, considering that Peru's most reliant industries have been agriculture and related low value-added sectors, unexpected climate changes pose additional risks for foreign investors.

<Table 1-2> SWOT Analysis Based on PEST Results

Strengths	Weaknesses
1. Strong fundamentals in the economy, and stable macroeconomic policies 2. Well integrated market regulations and openness toward trade with the global economy and efficient resource allocation 3. A basic legal framework for promoting and developing SEZs 4. Fast legal process of registration 5. Cheaper rent prices than the competitor countries.	**Legal Weaknesses:** 1. Lack of clear and consistent criteria for determining the location of SEZs 2. Overlapping and duplicated local and national regulations within the SEZs 3. Insufficient simplification of regulatory approvals and cancellations **Economic Weaknesses:** 1. Concentration in low-level industries, which generate only a modicum of value-added in exports 2. Deficiencies in trade facilitation at customs and in infrastructure provision 3. Absence of simplified labor provisions and incorrectly calibrated tax incentives **Social Weaknesses:** 1. Lack of specialized labor supply directed towards the SEZs 2. Relatively high levels of poverty in the SEZs **Technological Weaknesses:** 1. Inadequate accessibility to high-speed internet 2. Lack of guidelines for R&D at national level
Opportunities	**Threats**
1. Relatively abundant natural resources in mining, fishing, forestry, and land for agriculture, which can attract more FDI to the SEZs 2. Room for greater value-added manufacturing from further processing of natural resources within the SEZs	1. Vulnerability to external economic shocks 2. Vulnerability to natural disasters such as the effects of the El Niño phenomenon 3. The rise in social and political unrest

3.2. Analysis of Core Elements for Infrastructure Development in Peru

3.2.1. GI-Hub Analysis on Infrastructure in Peru

The Global Infrastructure Hub (GI Hub) is a not-for-profit organization established by the G20 with the aim of promoting sustainable, resilient, and inclusive infrastructure in developing countries. Formed in 2014, it serves as a knowledge-sharing hub that connects public sectors, private sectors, development banks, and other international organizations in implementing the G20's infrastructure agenda. The GI Hub has proposed frameworks for sustainable infrastructure investment, including increased participation by the private sector. One such framework is InfraCompass 2020, which assesses countries' ability to deliver better infrastructure outcomes and provides guidance for effective management of infrastructure at the government level. In this subsection, the KSP team applies this framework to analyze the current infrastructure environment in Peru's SEZs and propose more sustainable options for foreign investment participation in SEZ projects in Peru (See Appendix 2).

3.2.2. Overall Performance of Peru's Infrastructure in 2020

In terms of the overall economy, Peru has prioritized infrastructure development and implemented national-level plans to attract foreign investment for funding infrastructure projects and promoting business activities. However, the COVID-19 pandemic and low rate of GDP growth together have had a negative impact on the country's FDI inflows, and the lack of liquidity in the capital market has further exacerbated the outflow trend. In 2019, Peru invested approximately 4.8% of its GDP in infrastructure projects, and over the past five years, the country's private infrastructure investment has averaged $1,643 million. According to InfraCompass metrics, Peru's overall infrastructure quality was rated at 62.3 in 2019 on a scale of 0 to 100 (with 100 being the best).

Here are top three performing metrics for Peru's infrastructure:

- Registering property (91.5/100): According to the World Bank, it takes only 9.5 days to register a property in Peru, which is faster than the Upper Middle Income Countries' average of 21.7 days. This helps reduce cost and risk and is therefore beneficial for infrastructure projects that require property rights.

- Financial stability (90.1/100): Peru has become more financially stable and ranks

slightly above the Upper Middle Income Countries' average of 88.6. The stability is driven by strong capital buffers and the profitability of the banking sector, although COVID-19 may have impacted this to some extent.

- Cost to start a business (81.1/100): According to the World Bank, it costs 9.4% of income per capita to start a business in Peru, which is slightly lower than the Upper Middle-Income Countries' average of 11%. This makes it easier for new firms to enter the market.

Further, the following are three areas for improvement:

- Post-completion reviews (Negative): Currently, Peru does not conduct post-completion reviews for infrastructure projects. Implementing these reviews could help to determine if projects have achieved their objectives and identify areas for improvement.

- Stocks traded (0.9/100): Peru's value of stocks traded is only 1% of GDP, which is far below the Upper Middle Income Countries' average of 26%. This indicator measures the liquidity of equities, which is important for infrastructure investors as they need to be able to exit investments at appropriate points.

- Long-term GDP growth trend (41.6/100): Peru's long-term GDP growth rate is 4.4%, which is higher than the Upper Middle Income Countries' average of 3.1%. However, this growth may have been impacted by COVID-19 and it is important to monitor this area as it may correlate with greater infrastructure spending.

In additional to the above three main categories that Peru must improve, our on-site questionnaires and GI-Hub commonly point out the lack of physical infrastructures, such as supplies of water, electricity, internet, and the lack of efficient institutional support such as tax-exempt services to the tenant firms, which is being successfully provided in Brazil as discussed in the next chapter, or on-site export supporting agencies.[6]

6 More specific problems and solutions will be discussed in Chapters 2 and 3, as part of the structure of this study.

<Table 1-3> InfraCompass 2020 Ranking of Peru: Among 76 Countries

Category	Rank (Overall)	Rank (among Latin American countries)	Score (/100)
Governance	69	7	34
Regulatory frameworks	36	2	61
Permits	45	4	68
Planning	11	2	97
Procurement	52	8	65
Activity	17	4	48
Funding capacity	32	2	41
Financial markets	50	4	28

Source: Deloitte. InfraCompass 2020 (2020).

3. Case Study of FDI Attractions in Important Countries and Policy Implications

In this section, the KSP team examines notable cases of FDI in SEZs across Asian and Latin American countries. It is crucial for Peruvian policymakers to learn from the successes and failures of other nations in order to design effective policy and governance strategies that attract foreign investors to SEZs. Through this analysis, this KSP team aims to identify valuable policy implications for Peruvian decision-makers.

4.1. Challenges and Prospects of Special Economic Zones in South Korea

South Korea presents a unique case in the realm of Special Economic Zones due to the diversity of zones and their extensive coverage of the national territory. The origin of these zones was the Free Trade Zone in Masan, a city in southern Korea, in the 1970s. With national strategic support for the manufacturing industry to attract foreign investments and promote exports, Masan and other industrial cities drew considerable benefits from tax incentives and the easing of regulations. However, as globalization and competitiveness in the manufacturing industry intensified, the Korean economy faced many challenges, and economic growth slowed down. As a new way to overcome these difficulties, Korean policymakers decided to extend their special economic zones aggressively to attract foreign investments and stimulate industries such as finance, logistics, trade, and information technology.

As of 2023, there are 48 idiosyncratic laws and regulations, with 12 different overseeing government departments responsible for governing 50 distinct types of Special Economic Zones. The total number of districts or areas designated as Special Economic Zones amounts to 748, covering an area 1.2 times the size of the nation's territory.

The most notable types of Special Economic Zones in South Korea are the Free Economic Zones (FEZs), Foreign Investment Zones (FIZs), and Free Trade Zones (FTZs). These zones are established to attract foreign investment, promote international trade, facilitate international logistics, and stimulate regional development under separate special acts. The following provides a brief history and background information on these three main categories of special economic zones.

- **Free Economic Zones (FEZs)** in South Korea were first established under the 『Special Act on Designation and Management of Free Economic Zones』 (Act No. 17487) in 2003. Initially, three areas were designated: Gwangyang, Busan, and Incheon-Songdo. In 2008, the second generation of FEZs, including Gyeonggi, Daegu-Kyeongbuk, and Saemangeum, was introduced. The third (the East Sea Area and Chungbuk) and fourth (Ulsan and Gwangju) generations of FEZs were announced in 2013 and more recently in 2020, respectively. FEZs are the largest among all Special Economic Zones in South Korea, with the largest allocation of total budget. The Ministry of Trade, Industry, and Energy (MOTIE) serves as the main body of the Free Economic Zone Committee, which performs deliberations and makes resolutions on matters concerning FEZ. Regulatory and operational bodies for FEZs are twofold. The Free Economic Zone Planning Group under MOTIE is responsible for developing plans and strategies for all FEZs, while local (regional) governments have their own Free Economic Zone Authority to promote the attraction of foreign investment and development.

- **Foreign Investment Zones (FIZs)** were established under the 『Foreign Investment Promotion Act』 (Act No. 10232) in 1998. The Act aims to accelerate foreign investment attraction, promote trade, facilitate international logistics, and foster regional development. It outlines specific conditions for designation of FIZs, offering tax incentives on corporate, acquisition, income, and registration taxes. Regional governments are the main entities responsible for designating FIZs within their territories, while the Ministry of Trade, Industry, and Energy (MOTIE) reviews the validity of the designation. Regional governments also designate the management institutions. As of 2023, there are 114 operational FIZs, which consist of three types of districts: complex-type (27 places), individual-type (84 places), and service-type (3 places). Complex-type FIZs are designated within industrial complexes exclusively

for foreign-invested firms, and currently, 224 companies reside in this type of FIZ. Individual-type FIZs are set aside for companies that invest more than a threshold value in manufacturing, logistics, tourism, or R&D. Service-type FIZs are designated for foreign investors operating high value-added industries such as finance, insurance, or knowledge-based industries.

- **Free Trade Zones (FTZs)** were established under the 『Act on Designation and Management of Free Trade Zones』 (Act No. 6142) in 2000. A 'Free Trade Zone' is defined by Article 4 of the Act as a zone designated for free activities of manufacturing, logistics, distribution, and trade, with exemptions provided by relevant Acts, including the Customs Act and the Foreign Trade Act, along with other assistance. FTZs offer incentives such as tariff exemptions, rent reductions, and subsidies for R&D and human resource development to domestic as well as foreign firms. As of 2023, there are 13 FTZs in operation, including 7 industry complex-type zones (e.g., Masan, Gunsan), 5 port-type zones (e.g., Busan, Gwangyang), and 1 airport-type zone (Incheon).

Since the initial designation of these special economic zones, they have achieved certain outcomes in terms of attracting foreign investment. From 2004 to 2014, FEZs attracted a total of $9.95 billion, accounting for 6.9% of South Korea's total FDI during the same period. Currently, more than 2,000 domestic firms and over 200 foreign firms operate in the 8 FEZs, with the Incheon-Songdo area hosting the most firms (881) among the FEZs. It is challenging to compile comprehensive data on foreign investment or employment for FIZs and FTZs because, unlike FEZs which are directly controlled by MOTIE, these two zones lack a national-level control tower, leading to scattered FDI data. However, FIZs and FTZs have also experienced gradual growth in foreign investment attraction since their inception.

There have been rigorous evaluations of the performance of these special economic zones, with several problems and challenges identified.

① **Some areas are overlapping, or too many areas have been designated.** There are more than 50 types of Special Economic Zones, encompassing 1,550 districts, with the total area of all zones amounting to 1.2 times the size of the nation's territory. The definitions, purposes, or functions of many Special Economic Zones overlap. For example, among the most representative Special Economic Zones in South Korea, FEZs have 3 out of 8 zones that are also designated as other special economic zones, such as FTZs, FIZs, Research Development Special Zones (RDSZs), Industrial Complexes (ICs), or High-Tech Medical Complexes (HTMCs). Regional governments are economically incentivized to request excessive designation of Special Economic Zones for reasons

such as additional tax revenue or promotion of local employment. However, there is no clear legal mechanism for the central government to reject such applications. Consequently, this duplication of administrative costs may lead to a decrease in the overall efficiency of the zones' performance.

<Table 1-4> Current Designation Status of Main Special Economic Zones

FEZ	Incheon	Busan	Gwangyang	Saemangeum	Daegu	Gyeonggi	East Sea	Chungbuk
FTZ	○	○	○					
FIZ		○		○				
RDSZ		○			○			
IC	○	○		○	○		○	○
HTMC					○			○

Source: Jeong and Zeng (2016).

② **The majority of Special Economic Zones lack specialization.** Most Special Economic Zones share similar purposes and functions. FEZs, FIZs, and FTZs all aim to attract foreign investment, promote international trade and logistics, and foster regional development in common. Moreover, due to these shared policy goals, government support programs also lack differentiation. For instance, foreign investors receive complete exemption of tariffs for five years, and local taxes are reduced for 15 years across all three types of Special Economic Zones. In addition, there have been ongoing complaints from domestic firms within the zones regarding potential reverse discrimination. Although domestic firms are eligible to enter most Special Economic Zones, the special acts governing these zones provide certain benefits exclusively for foreign firms, including exemptions from employment duties or reductions in the price of allotments. Incheon-Songdo FEZ (IFEZ) is one of a few exceptional cases, in which the FEZ successfully specialized in biotechnology and R&D industries, drawing benefits from its unique locational strength.

③ **There is a lack of a control tower in the governance system.** Given the common policy goals of Special Economic Zones, centered on attracting foreign investment, it is essential for public sectors to establish a main control tower to efficiently manage functions across various special economic zones. However, each Special Economic Zone is controlled by different central or regional government bodies, resulting in a lack of unified command or control tower within the overall system of Special Economic Zones. The governance of individual FTZs varies according to their type. In the case of FEZs, the control tower is divided between the FEZ Committee, which

is directly controlled by MOTIE and the FEZ Authorities, governed by each regional government.

④ **Purposes and functions of many SEZs tend to overlap.** The aforementioned systemic inefficiency is strongly related to the overlapping purposes and functions of many Special Economic Zones, as mentioned earlier. Without a single control tower, it is challenging to design a national-level plan for foreign investment attraction. Furthermore, the undesirable competition between different Special Economic Zones could exacerbate performance inefficiency.

There are potential solutions to the aforementioned problems, and these suggestions may also provide policy implications for the development of Peruvian SEZs. Firstly, a comprehensive national plan for attracting FDI should be devised, and a strong control tower must guide all Special Economic Zones towards their common objectives. The main issue with FDI attraction in South Korea is that the focus has been on cost reduction rather than improving the quality of FDI projects. To achieve more efficient allocation of resources and enhance FDI quality, the central government should establish a comprehensive plan for FDI attraction.

Secondly, it is necessary to develop a more efficient structure for Special Economic Zones. In the long term, canceling the designation of underperforming areas within a zone could be a solution. In the short term, promoting competition between areas within zones could increase efficiency.

Thirdly, developing new strategies for the future is crucial. Establishing a comprehensive management plan for the numerous overlapping Special Economic Zones will strengthen their connections with national industrial and enterprise policies. Additionally, forming knowledge-based industry clusters within some zones can secure new growth engines at the national level.

4.2. Current Status of Neighboring Countries in Latin America: Mexico, Brazil, and Panama

In this subsection, the KSP team reviews a few examples from neighboring countries of Peru. In the context of global supply chains, some Latin American countries are more directly related to the economy of Peru, especially to its export industries. They serve as important providers or buyers in intermediate or final goods markets for Peru, while these countries could also be potential competitors for Peru in limited markets. The KSP

team selected three countries as examples: Mexico, Brazil, and Panama, due to their recent developments in Special Economic Zones and FDI attraction, as well as their economic relevance to Peru in terms of potential competition in global supply chains and international trade.

- **Mexico** currently operates seven Special Economic Zones (Puerto Chiapas, Coatzacoalcos, Lázaro Cárdenas, Progreso, Salina Cruz, Dos Bocas, and Champotón). The SEZs were originally introduced to address regional economic imbalances. There are several tax benefits for foreign investors: exemption of income tax for the first 10 years; 50% reduction of income tax for the next five years; 0% VAT on goods acquired for use in the SEZs; 0% VAT on services rendered to foreign investors; and exemption from treatment as exports for goods imported to Mexico for exclusive use in the SEZs. Political instability is one of the main factors that hamper potential foreign investment. To alleviate these concerns and to ensure certainty and transparency in the management of SEZs, the new government in 2018 established a licenses and permissions committee. Furthermore, to secure potential long-term investment, the government has arranged for the development plan of SEZs to be directly covered by federal law and national authorities.

- Free Trade Zones, one of the best-known SEZs in **Brazil**, were initiated in 2018 with the purpose of promoting economic and social integration in Western Amazonia and addressing economic inequalities across regions. The Free Trade Zones in Brazil offer several incentives to foreign investors. First, offices of customs authorities are located inside the zones, speeding up the administrative process. Second, foreign exchange treatment is supported by law. Third, federal and state (regional) taxes on purchased or imported goods are suspended. Furthermore, the country is currently working to simplify the various special schemes offered to exporters to improve efficiencies in logistics and trade.

- **Panama** recently initiated five new Special Economic Zones in Panama City, Chiriqui Province, and Herrera Province, supported by the Panamanian government which is trying to consolidate Panama as a logistic hub of the Americas. These Special Economic Zones, clustered in the Metropolitan corridor along the Panama Canal, offer domestic and foreign firms incentives to reduce costs in strategic locations in Latin America. Colon Free Trade Zone, located on the Atlantic side of Panama, is the largest Special Economic Zone and one of the most effective distribution channels for accessing Latin American and Caribbean markets. Approximately 2,500 companies are in operation in this zone, focusing on B2B activities related to the import and re-exports of products

without adding value. Another important area is the Pacifico Special Economic Area, located on the Pacific side of Panama, where 160 companies are in operation. This zone focuses on attracting distribution centers, high-tech manufacturing factories related to industries such as aircraft maintenance, and back-office and call center services.

4.3. Comparison with Peru SEZs' Case and Policy Implications for FDI Attractions

In this section, the KSP team derives important policy implications for Peruvian SEZs based on the case studies on the countries analyzed above and compares them with Peruvian cases.

4.3.1. Specialization

One of the most important factors for success in some Special Economic Zones has been specialization in a competitive industry. In other words, some zones that failed to gain interest from foreign investors lacked sufficient specialization. For a country faced with intense competition in exports, it is necessary to decide on a direction of specialization to consolidate the capacities of its special economic zones toward greater competitiveness, based on an analysis of comparative advantages.

For instance, Free Economic Zones in South Korea have suffered from a lack of specialization and overlapped economic interests, except for the Incheon-Songdo area. The Incheon-Songdo FEZ aimed to maximize its unique location advantage of proximity to Incheon airport and port as well as to Seoul, and strived to promote FDI attraction by specializing in biotechnology and research industries, in contrast to other FEZs that focused on traditional manufacturing industries. As a result, Songdo hosts world-leading multinational companies in the related fields, such as Samsung Biologics, Celltrion, and SK Bioscience, and these knowledge-based industries have created a new market and contributed to the rapid economic growth of the Songdo area.

If Peru could find a meaningful comparative advantage for its SEZs based on their competitiveness merit and build a good economic environment for FDI attraction in those areas, it will be easier to make the SEZs successful cases in the long term. The KSP team presents an example of the related analysis in the next section, in which the simple methodology shows optimal industries not only for Peru as a whole but also for individual SEZs in Peru.

4.3.2. Governance Structure and Incentive System

Governance structure within a single Special Economic Zone or at a collective level is an important factor for successful management of the zones. A few countries in our case study, including South Korea, have suffered from a lack of efficient governance structure and consequently lost efficiency in management. Furthermore, with this lack of efficiency in the governance structure, it is harder for each SEZ to offer attractive economic incentives for foreign firms.

One of the potential risks of poor governance is the possibility of reverse discrimination against domestic firms within a SEZ. Foreign investors are usually motivated by realistic profitability and marketability in a specific region or country, which is largely affected by existing domestic sellers. If a flawed incentive system creates a disincentive for domestic investors, it could crowd out foreign investors as well, by forcing them to create a new market by themselves, which is a cost-pushing factor.

The current overlapping or scattered regulatory and supervisory system should be reconstructed. An appropriate incentive system must be carefully designed to increase economic interest equally for foreign and domestic investors. Market profitability and long-term prospects should be fully considered before proceeding with a legal designation process.

Cases of Mexico and South Korea can be good examples. Mexico has a branch of Custom Service Office, where the process is boosted by the efficient administration, and the Saemangeum FEZ in South Korea overcame the potential reverse discrimination problem by introducing equal treatment policy.

4.3.3. Conformity with the National Plan

Conformity with development or industrial policies at the national level is a crucial factor for a successful SEZ policy. From our case studies, including Peru and South Korea, there has been a lack of national support from the central government in the process of SEZ development. Exclusion from the national development or industrial plan or a lower level of support from the central government could result in serious problems in some important categories: procurement, funding, development of related market, and planning.

In many countries, strong support from the central government has been one of the main factors for success. Some successful FEZs in South Korea had a relatively healthy financing

structure with strong participation from the central government. In Mexico, the designation process of initial SEZs was totally controlled by the central government, and currently, the regulation is completely protected by federal law. Unifying the different economic perspectives adopted by various regional governments into a national-level development plan led by the central government minimizes unnecessary social costs and improves the overall efficiency of SEZs. Masan SEZ, the first Special Economic Zone constructed in South Korea, is a good example of conformity with the national economic plan. A detailed discussion on the Masan case will be carried out in the Chapter 2.

4. Economic Analysis on the Selection of Industries for FDI Attraction in SEZ

5.1. Analysis Methodology

5.1.1. Criteria for the Selection of Industries

In this section, actual data were analyzed to determine which industries to focus on for the purpose of attracting FDI to the Special Economic Zone (SEZ). The research was conducted in two directions: desirable industries at the national level and desirable industries in each region. For the country as a whole, industries that are more competitive than others can be identified using export performance. However, each SEZ has its own economic characteristics and must be approached accordingly. In addition, when considering both Peru as a whole and each region in which a SEZ is located, it is important to not only look at current competitiveness but also consider the government's policy stance. This will be determined through a survey of government officials and experts.

As a result, the KSP team established the following two criteria for both Peru as a whole and for each region:

- Competitive industries in the current situation;
- Promising industries for Peru and for each region.

5.1.2. Methodology

The two criteria mentioned earlier can be utilized to identify industries that require concentrated efforts to attract investments in the SEZ. Firstly, we must determine which industries are the most competitive currently. Secondly, research needs to identify which industries are desirable for Peru in the future. Therefore, it is necessary to find a

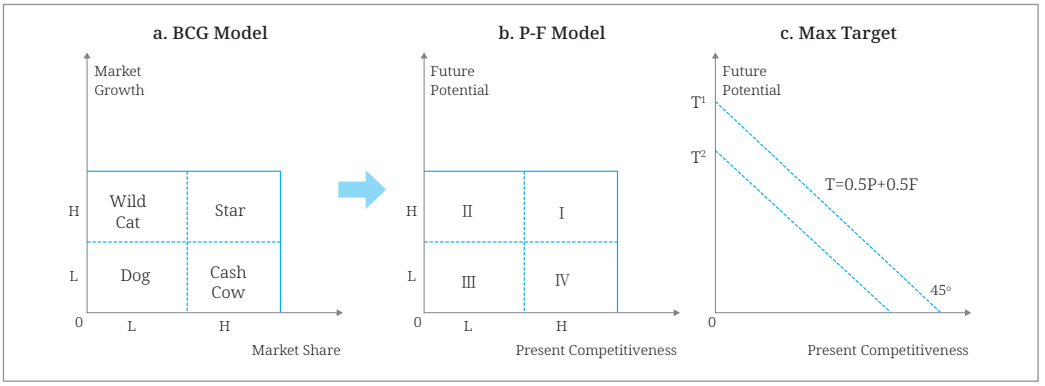
methodology that considers both directions for analysis.

The KSP team initially considered applying the Market Share - Market Growth Matrix. This method, developed by the Boston Consulting Group in the early 1970s, is widely used as a fundamental analysis tool for establishing a company's market strategy. By classifying the company's product portfolio into high/low market share and high/low market growth, it divides the portfolio into four categories, as shown in [Figure 1-6a]. However, since this study focuses on industry analysis rather than firm analysis, it is necessary to adopt a method that is slightly different from the BCG model. Furthermore, it is important to consider not only the current competitiveness but also industries that are desirable for the future of the Peruvian economy. Taking these factors into account, the following research was conducted.

To evaluate the current competitiveness, the KSP team first calculated the proportion of exports for each industry in relation to the total exports of all industries. However, in the case of Peru, the current market share of certain industries, such as the mining industry, is overwhelmingly large. Using the market share directly could lead to distorted results. Therefore, the KSP team calculated the market share for each industry and then scored them based on their ranking. The numbers obtained from this procedure are shown on the horizontal axis of [Figure 1-6.b]. A higher number indicates a higher current competitiveness for that industry.

For promising industries for the future, the KSP team conducted a questionnaire survey for the government officials and SEZ experts. (See the appendix for the details of the survey). In the survey, respondents were asked to rate the importance of each industry for the future of Peru on a scale from 1 to 5. In this analysis, the average score for each industry was calculated, and the industries were ranked according to the magnitude of their average scores. Finally, an index was created using these rankings, where a higher value indicates greater importance. The index is plotted on the vertical axis in the graph (b) of [Figure 1-6].

[Figure 1-6] Analysis Model for Industry Selection



Now, by combining future potential with the previously plotted current competitiveness index on the horizontal axis, the KSP team obtained the graph (b) of [Figure 1-6], a modified form of the BCG model, which is named as the Present-Future model (PF model).

In the graph (c) of [Figure 1-6], the KSP team presents a method where equal weights are assigned to present competitiveness and future potential, allowing us to calculate a single index representing both aspects. Desirable industries are selected based on the value T from the following equation:

T = 0.5P + 0.5F (Target Industry = 0.5* Present Competitiveness + 0.5*Future Potential)

By calculating the value of T using this equation, the industry ranks are obtained starting from the largest value. As shown in the graph (c) of [Figure 1-6], this method shows the selection in the order of being in the upper right position by drawing the 45-degree line T. The graph (c) of [Figure 1-6] shows two lines as examples, where T^1 is preferred to T^2. The results obtained from this method can be called Target Industries for FDI attraction.

5.2. Results: Peru as a Whole Country

This study aims to identify industries with a comparative advantage over other industries, utilizing UN COMTRADE data from 2017-2021 and MINCETUR data from 2012-2021. The export share from each industry in relation to total export was analyzed in the context of the overall Peruvian economy and each SEZ, which provided two models as follows:

- Model (1) Countrywide Targets for FDI attraction;
- Model (2) Targets for FDI attraction to each SEZ.

However, it should be noted that the industrial classification may not match precisely between country-wide data for entire Peru and data for each region, due to the limitation in data acquisition.

The following <Table 1-5> presents the scoring of the current and future competitiveness of the Peruvian economy as a whole. As mentioned earlier, when calculating the current competitiveness, using the market share directly could lead to distortion in the case of Peru due to the overwhelming market share of the mining sector. Therefore, the KSP team analyzed the market share based on its ranking rather than the actual share itself. The "Point" column in <Table 1-5> represents the scoring derived from these rankings. A higher point indicates a higher level of competitiveness. The KSP team also applied this concept to the future potential by assigning rankings to the scores obtained from surveys conducted with Peruvian government officials and experts. The table provides the actual average scores obtained and the corresponding rankings, which were used to calculate the Point column once again. Ultimately, the KSP team calculated the Total Points by combining the current points and future points assigning the same weight, and the Final Rank is presented based on these scores.

<Table 1-5> Results of Industry Selection for Peru

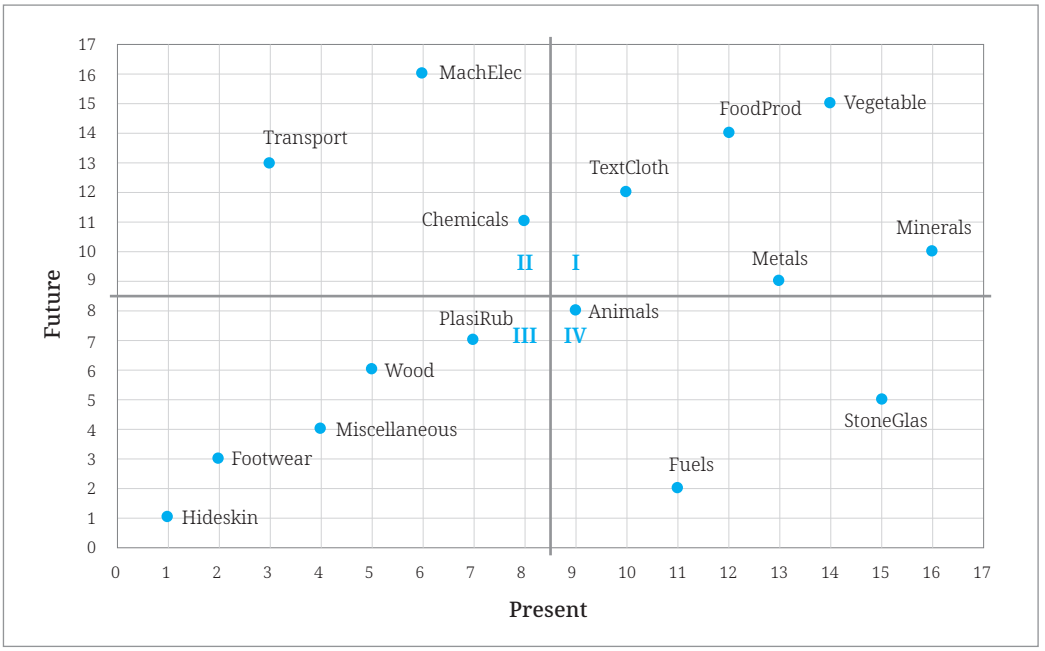
Product Code*	Industry	Abb.	Present		Future		Targeting	
			Share	Points	Score	Points	Total Points	Final Rank
01-05	Animals. Fish, Dairy	Animals	2.5%	9	3.80	8	17	9
06-15	Vegetables	Vegetable	12.8%	14	4.23	15	29	1
16-24	Food Products, Tobacco	FoodProd	7.3%	12	4.17	14	26	2
25-26	Minerals (Salt, Stones, Ores)	Minerals	37.5%	16	3.93	10	26	2
27-27	Fuels	Fuels	6.9%	11	3.37	2	13	12
28-38	Chemicals	Chemicals	1.9%	8	4.00	11	19	8
39-40	Plastic or Rubber	PlasiRub	1.4%	7	3.73	7	14	11
41-43	Hides and Skins	Hideskin	0.1%	1	3.33	1	2	16
44-49	Wood, Paper	Wood	0.5%	5	3.63	6	11	13
50-63	Textiles and Clothing	TextCloth	2.9%	10	4.00	12	22	4
64-67	Footwear	Footwear	0.1%	2	3.40	3	5	15
68-71	Stone and Glass	StoneGlas	16.4%	15	3.40	5	20	7
72-83	Metals	Metals	8.6%	13	3.90	9	22	4
84-85	Machinery, Electrical	MachElec	0.8%	6	4.40	16	22	4
86-89	Transportation	Transport	0.2%	3	4.10	13	16	10
90-99	Miscellaneous	Miscellan	0.3%	4	3.40	4	8	14

Note: Product Codes are imported from UN COMTRADE (https://unstats.un.org/wiki/display/comtrade/UN+Comtrade+Reference+Tables, accessed on August 8, 2023).

For example, as observed, the Machinery and Electrical industries have a current competitiveness score of 6, but they demonstrate the highest potential with a score of 16 for the future. As a result, they are assigned Total Points of 22, ranking them fourth among all industries that require efforts for investment attraction.

[Figure 1-7] shows the results of analyzing Peru's economy based on the export amount by industry using UN COMTRADE data and questionnaire survey.

[Figure 1-7] Industry Position on the Present-Future Framework for Peru as a Whole



Industries such as Vegetables, Food Products, Textiles and Clothing, and Minerals, located in Quadrant I of the [Figure 1-7], not only possess current competitiveness but also demonstrate potential for the future. Industries in Quadrant II, namely Machinery, Electrical, Transportation, and Chemical, may not currently exhibit significant competitiveness but are identified as industries that require development for the future. Industries appearing in Quadrant III do not require significant attention for attracting Foreign Direct Investment (FDI). Industries in Quadrant IV are currently competitive but do not necessarily require focus in efforts to attract FDI. Rather, industries in Quadrants I or II would be more desirable for Peru's future.

When looking for a simple ranking, the results obtained through the formula explained above are presented in the last column of <Table 1-5>. The result is equivalent to drawing a

downward-sloping 45-degree line as described in [Figure 1-6.c] for the selection of industries. The industries that should be of greatest interest are Vegetables, Food Products and Tobacco, Minerals (Salt, Stones, Ores), Textiles and Clothing, Metals, and Machinery, Electrical, just as depicted in the figure and the <Table 1-5>.

5.3. Analysis for SEZs in Peru

5.3.1. Analysis Using Export Share for Each Region

Using the Present-Future model, the KSP team calculated the current competitiveness and future potential of each SEZ and deduced the present target industries accordingly. The KSP team utilized export data provided by MINCETUR from 2012 to 2021. However, analyzing the current competitiveness using the export performance of each SEZ itself proves challenging due to the frequent occurrence of significantly low export values. Consequently, it was problematic to utilize such data for analysis purposes.

Therefore, the KSP team conducted the analysis using export data from the regions to which each SEZ belongs, following the same methodology as the analysis for the entire country of Peru. First, the KSP team obtained the export value by industry for each region from MINCETUR data. Then, KSP team calculated the proportion of export value by industry in the total export value. The KSP team ranked them in descending order based on the proportion, which is defined as “Present Competitiveness.”

Additionally, similar to the analysis for Peru as a whole, the KSP team utilized the survey questionnaires administered to government officials and SEZ experts to incorporate their insights into the analysis of future potential. However, unlike the industry classification of Peru’s total exports obtained from UN COMTRADE, the export data from each region distinguishes between traditional and non-traditional industries. With this distinction in mind, the KSP team explains the analysis results for attracting FDI to each SEZ based on the P-F model. Here, the prefix “T” denotes traditional industries. The following discussion focuses on non-traditional industries.

5.3.2. Analysis Results for Each Region

First, for ZED Paita, the KSP team presents the analysis results in the form of a table to facilitate understanding. To save space, only the corresponding figures are provided for other SEZs.

5.3.2.1. ZED Paita (Piura)

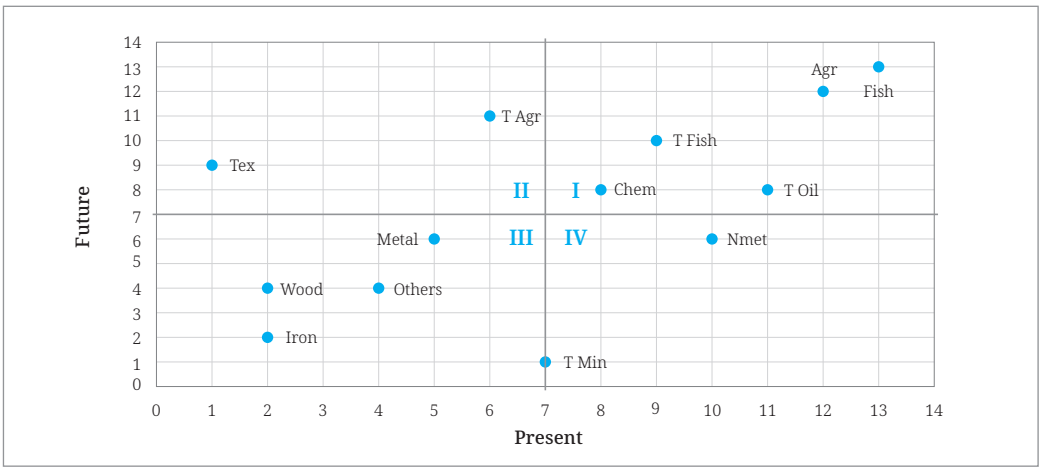
<Table 1-6> Analysis Results for ZED Paita

Industry	Abb.	Present		Future		Targeting	
		Share	Points	Score	Points	Total Points	Final Rank
Agriculture & Livestock	Agr	33.3%	13	4.27	13	26	1
Chemicals	Chem	3.6%	8	3.70	8	16	6
Fishing	Fish	31.2%	12	4.17	12	24	2
Iron-Metallurgical, Jewelry	Iron	0.0%	2	3.53	2	4	13
Metal-Mechanics	Metal	0.4%	5	3.67	6	11	8
Non-metallic minerals	Nmet	8.7%	10	3.67	6	16	6
Others Non-traditional	Others	0.0%	4	3.60	4	8	10
Textiles	Tex	0.0%	1	3.73	9	10	9
Wood and Paper	Wood	0.0%	2	3.60	4	6	12
Traditional Agriculture	T Agr	0.7%	6	4.07	11	17	5
Traditional Fishing	T Fish	5.8%	9	4.03	10	19	3
Traditional Mining	T Min	2.4%	7	3.20	1	8	10
Traditional Oil & Natural Gas	T Oil	13.8%	11	3.70	8	19	3

In terms of industry rankings, Agriculture & Livestock and Fishing are considered the most promising industries. This result is well reflected in the quadrant I of [Figure 1-8], as shown below.

It is important to take interest in Agriculture & Livestock, Fishing, and Chemicals, located in the quadrant I, as well as Textiles, located in the quadrant II.

[Figure 1-8] Results of Present-Future Analysis for ZED Paita

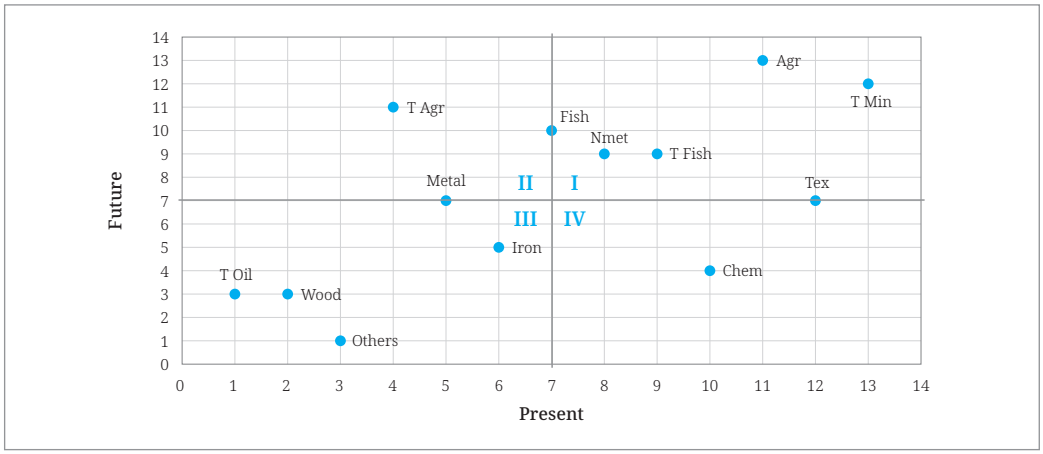


To save space, detailed tables will not be provided below. Instead, the analysis results using the P-F model are presented in the form of figures only. For detailed numbers, see Appendix 3 and Appendix 4.

5.3.2.2. ZED Matarani (Arequipa)

It is necessary to focus on attracting activities in the Agriculture & Livestock, Fishing, and Textile industries in Quadrant I, as well as the Metal-mechanics industry in Quadrant II.

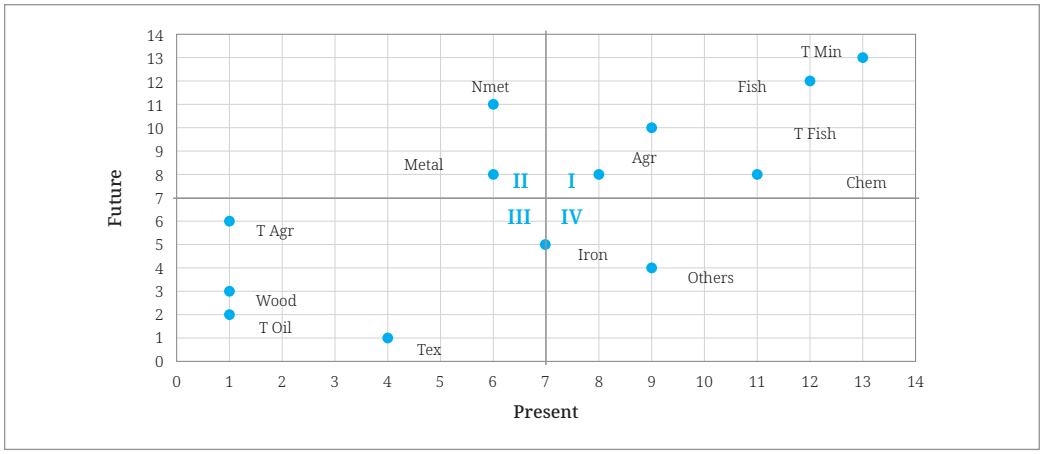
[Figure 1-9] Results of Present-Future Analysis for ZED Matarani



5.3.2.3. ZED Ilo (Moquegua)

The Fishing, Chemicals, and Agriculture & Livestock industries in Quadrant I, as well as the Metal-mechanics industry in Quadrant II, are promising target industries.

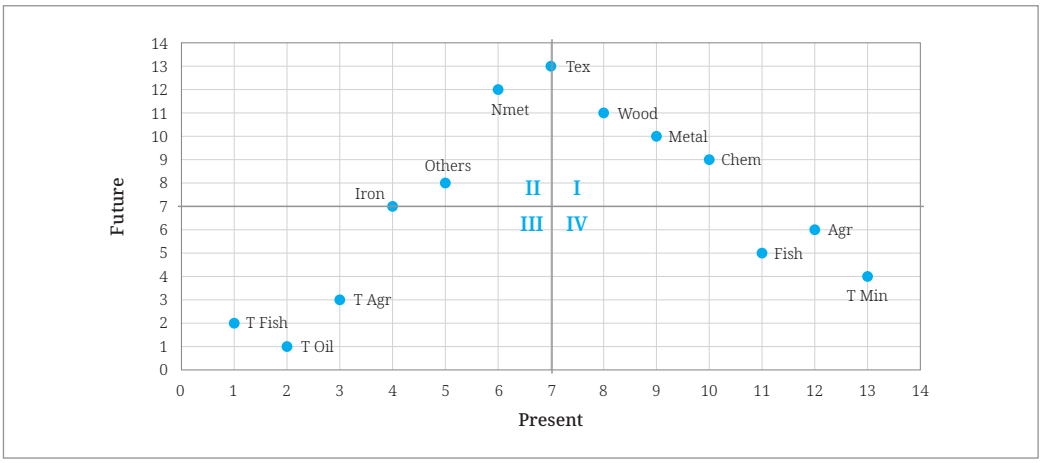
[Figure 1-10] Results of Present-Future Analysis for ZED Ilo



5.3.2.4. ZOFRATACNA (Tacna)

To attract FDI, it is crucial to focus on the Textiles, Metal-mechanics, Wood and Paper, and Non-metallic Minerals industries in Quadrant I, as well as the Iron-metallurgical and Jewelry industries in Quadrant II.

[Figure 1-11] Results of Present-Future Analysis for ZOFRATACNA



Based on the above results, the following recommendations can be made. (i) Efforts should be made to attract investments in industries that possess current competitiveness while considering industries that are desirable for the future of the Peruvian economy. (ii) When attracting investments in sectors such as mining, agriculture, and fisheries, it is important to consider avenues for increasing value-added through processing and other means. (iii) SEZs like Tacna should specialize in high-value-added industries.

5. Conclusion and Policy Recommendations

In this chapter, the KSP team explored four dimensions of challenges to the Peruvian economy, particularly in the context of SEZ development, to find an optimal solution for attracting FDI to Peruvian SEZs. The current macroeconomic conditions of the Peruvian economy were analyzed, and the factors impeding FDI inflows were investigated through PEST and GI-Hub methodologies. Third, the KSP team listed several notable cases of SEZs development and FDI attractions in foreign countries. Lastly, the KSP team suggested some important industries for FDI attraction using a Present Competitiveness - Future Potential model.

The key findings are threefold. Firstly, the Peruvian economy has sound and advanced macroeconomic policy systems, but it has limited ability to adjust volatility of business cycles. Combined with political instability in recent years and high regional imbalances that have become permanent, ups and downs of FDI inflows have been exacerbated, but policy remedies have not been very effective. Secondly, there are institutional barriers and inefficiencies that have hampered potential FDI inflows into SEZs. Overlapping regulations and laws have produced unnecessary confusion for foreign investors, and the non-existence of post-completion reviews on infrastructure projects has added to inefficiency. Thirdly, however, there are opportunities for a significant improvement of FDI inflows to SEZs, based on well-performing government functions and an investor-friendly business environment. Property is strongly protected by regulation, and the financial market is stable albeit in need of further development. Moreover, the cost to start a business is the biggest factor of competitiveness for the country in enticing foreign investors. These strengths should form the foundation for policy design to attract FDI inflows to SEZs.

The KSP team suggests focusing on the comparative advantages that Peru has achieved in recent times in order to attract FDI for the development of SEZs. It is also necessary to enhance the GVC participation level by upgrading industries based on the comparative advantages the country has. Firstly, our research results show that exports of natural resources and foods are optimal industries for SEZs, but creating more value-added should be prioritized to improve both qualitative and quantitative output of SEZs. It is important to design a better infrastructure environment, not only to attract foreign capital in natural resources or food industries where Peru already has a comparative advantage, but also to extend the country's capacities to manufacturing or other second-level industries. Secondly, luring anchor companies, of multinational firm level, with advanced technology is a key to success in each region. Advantages that are mentioned above - high-quality regulation system, cheaper cost for starting business, stability of the financial market - could provide a good starting point to promote new FDI consideration. Better economic incentives should be added for the bigger foreign investors. Thirdly, inefficient governance structures and regulation complexity should be addressed immediately. The research results show that regulatory and institutional inefficiency has been the main obstacle for further FDI inflows to SEZs. More specific policy proposals are presented in Chapter 2 and Chapter 3.

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Appendix

<Appendix Table 1-1> Main Incentive Laws and Their Benefits for the SEZs

Special Regime	Profits	
	Tributaries	Customs Officers
Tacna Free Zone - ZOFRATACNA	Exemption from Income Tax on profits (29.5% outside ZOFRATACNA)	The goods entered from abroad or from the national territory to the Free Zone are not subject to any customs regime due to the customs extraterritoriality condition.
	Exemption from the General Sales Tax (16%)	Benefit of drawback and return of the IGV for the final entry of national or nationalized merchandise from other parts of the national territory to the ZOFRATACNA.
	Exemption from the Municipal Promotion Tax (2%)	The entry of goods from other parts of the territory facilitates the regularization of operations under the temporary admission regime.
	Exemption from the Selective Consumption Tax (ISC)	The indefinite permanence of merchandise within the Free Warehouses is allowed.
	Exemption from all taxes imposed by the central, regional and municipal governments created to be created, except EsSalud contributions and rates.	Suspension of the payment of import duties and taxes for equipment, machinery, tools, spare parts and construction materials from abroad, which are necessary for the development of its activities.
	N/A	The output of products manufactured in ZOFRATACNA to the national territory requires the lowest tariff rate (ad valorem of 0%), according to current international agreements and conventions.
	N/A	The output of goods can qualify for temporary importation for outward processing or re-exportation in the same state.
	N/A	Exports of products made in ZOFRATACNA will benefit from the trade agreements signed by Peru, the origin requirements established in each of the agreements and the agreements that do not exclude products from free zones

<Appendix Table 1-1> Continued

Special Regime	Profits	
	Tributaries	Customs Officers
Paita Special Development Zone - ZED Paita	Exemption from: Income Tax (in general regime IT amounts to 29.5% on profits), General Sales Tax (16%), Municipal Promotion Tax (2%) and Selective Consumption Tax (between 2% and 30% depending on the type of product). Ad valorem of 0% for merchandise of foreign origin (raw material, supplies, machinery, equipment); in general regime the rates are 0%, 6% and 11%.	Suspension of the payment of tariffs and import taxes on machinery and equipment that user companies need for their production processes. These can enter the national territory paying taxes for their depreciated value.
	Exemption from all taxes imposed by the central, regional and municipal governments to be created.	Entry and exit of merchandise through any customs office in Peru.
	N/A	The goods resulting from the maquila activity that return to the national territory only pay taxes for the incorporated value.
	N/A	Suspension of taxes for the permanence of merchandise until the year 2042.
	N/A	The Drawback benefit for export is applicable (4% of the exported FOB value).
	N/A	The export of processed products draws commercial benefits based on the scope of the Free Trade Agreements (FTA).
Matarani Special Development Zone - ZED Matarani	Exemption from all taxes –created or to be created– for export activities.	For the entry of merchandise, machinery, equipment, raw materials and inputs from abroad, the customs destination is suspended as long as said goods are within the ZED Matarani. The term of permanence is valid until the year 2042 (Law 30446).
	The production for national territory is free from income tax up to 28%.	It is possible to carry out the forwarding and re-shipment of goods abroad.
	All goods and services that enter the ZED Matarani from national territory are considered as exports and are not subject to VAT.	The entry of national or nationalized merchandise and other services for the companies that use the ZED Matarani will be considered as exports.
	Free Trade Agreements, Integration Treaties and Trade Agreements apply.	The entry of merchandise is allowed through any customs office in the Republic.
	The Drawback benefit for exports is applicable (Recovery of a percentage of the FOB value).	When having a Transfer Request, the point of arrival benefit is applied for the direct unloading of merchandise to the ZED Matarani without requiring the intervention of the customs agent.

<Appendix Table 1-1> Continued

Special Regime	Profits	
	Tributaries	Customs Officers
	N/A	To transfer merchandise to the ZED Matarani from border posts (Tacna, Puno or Madre de Dios) it is only necessary to process the international transit of merchandise (covered by a MIC/DTA). It does not require the intervention of the customs agent.
Ilo Special Development Zone – ZED Ilo	Exemption from Income Tax, General Sales Tax (IGV), Selective Consumption Tax (ISC) and Municipal Promotion Tax; as well as all other taxes (Central Government, regional governments and municipalities) created or to be created, including those that require an express exemption rule.	The entry of machinery, equipment, raw materials and inputs from abroad enjoy the suspension of the payment of import duties and taxes; their time of permanence is equal to that of the company in the ZED Ilo (according to the terms established in their contract).
	The transfer of goods and the provision of services between installed users are exempt from Income Tax, IGV, ISC and any other tax – created or to be created – including even those that require express exemption.	When having the Transfer Request, the point of arrival benefit is applied for the direct unloading of merchandise to the ZED Ilo without requiring the intervention of the customs agent.
	Electricity services demanded within the ZED Ilo are exempt from the General Sales Tax (IGV).	To transfer merchandise to the ZED Ilo from border posts (Tacna, Puno or Madre de Dios) it is only necessary to process the international transit of merchandise (covered by a Manifiesto Internacional de Carga/Declaración de Tránsito Aduanero MIC/DTA). It does not require the intervention of the customs agent.
	All merchandise that enters the national territory towards the ZED Ilo is considered an export and is not subject to the General Sales Tax (IGV).	The entry of merchandise is allowed through any customs office in the Republic.

<Appendix Table 1-2> InfraCompass 2020 Framework

Variables	Definition	What Good Looks Like	Metrics
Governance	Governance, institutions (including rule of law and prevention of corruption), and legal environment required to support infrastructure investment	Robust governance, leadership and capable institutions supporting the rule of law, and effective and independent decision-making structures for infrastructure investment	Rule of law Recovery rate Political stability and absence of violence score Shareholder governance Infrastructure or PPP agencies Post-completion reviews
Regulatory frameworks	The extent to which regulation, openness to investment, and competition frameworks support infrastructure delivery	Stable, consistent, predictable and tranparent regulatory agencies and decision-making processes, and low barriers to investment enhance competition, drive down costs and increase quality of infrastructure	Regulatory quality Prevalence of foreign ownership Product market regulatory score, network sectors Strength of the insolvency framework Effect of taxation on incentives to invest Investment promotion agencies
Permits	The efficiency of planning and licencing procedures for the issuance of permits and acquisition of land required for development	Permits, approvals and land acquisition processes that are timely, predictable and navigable, and which minimize red tape to appropriate and justifiable levels	Quality of land administration Cost to start a business Registering property Time required to start a business Dealing with construction permits
Planning	The government's ability to plan, coordinate, and select infrastructure projects	Planning, not just of projects, but transparent setting of strategic social-economic-environment goals and integrated sectoral and system plans, enabling projects to be measured against clear objectives	Preparation of PPPs Published infrastructure plans Published projects pipeline Economic analysis assessment Market sounding and/or assessment Analysis of environmental impact
Procurement	The extent to which procurement processes and bid management frameworks are standardized, transparent, and non-onerous to bidders	Procurement practices that are transparent, enable efficient risk allocation and innovation, deliver value-for-money, enhance	Transparency in public procurement Average procurement duration Procurement of PPPs Published infrastructure procurement guidelines PPP contract management
Activity	The extent and nature of recent infrastructure investment activities and the extent of private sector involvement over the last five years, relative to the size of the economy	High levels of recent infrastructure activity and high value of recent infrastructure deals that involve private and foreign investment	Infrastructure investment Value of closed PPP infrastructure deals Private infrastructure investment Value of closed infrastructure deals with foreign equity sponsorship
Funding capacity	Stability and sustainability of the government's fiscal management	Fiscal sustainability that allows for the allocation of infrastructure expenditure by governments	Summary credit rating GDP per capita Long term GDP growth trend Gross government debt
Financial markets	Strength and capability of local financial markets	Ability to provide a variety of capital market instruments to encourage investors to finance infrastructure	Financial depth Financing through local equity market Domestic credit to private sector Stocks traded Financial stability

[Appendix Table 1-3] Results of Questionnaire Survey for each SEZ

Industry	ZED Paita (Piura)			ZOFRATACNA (Tacna)			ZED Ilo (Moquegua)			ZED Matarani (Arequipa)		
	Gov.*	SEZ**	Total	Gov.	SEZ	Total	Gov.	SEZ	Total	Gov.	SEZ	Total
Fishing (T)	3.42	4.44	4.01	3.17	3.22	3.17	3.42	4.11	3.81	3.83	4.06	3.96
Agriculture (T)	3.75	4.28	4.06	3.58	3.22	3.35	3.42	3.89	3.68	4.17	4.06	4.11
Mining (T)	3.25	3.17	3.18	3.25	3.56	3.41	3.50	4.39	4.02	4.17	4.11	4.11
Oil and Natural Gas (T)	3.75	3.67	3.73	3.00	3.06	3.00	3.08	3.44	3.27	3.75	3.61	3.66
Agricultural & Livestock (NT)	3.67	4.67	4.26	3.42	3.50	3.48	3.33	4.06	3.78	4.17	4.17	4.17
Fishing (NT)	3.58	4.56	4.15	3.25	3.61	3.48	3.50	4.11	3.85	4.08	4.00	4.00
Textile (NT)	3.75	3.72	3.73	3.33	3.94	3.71	3.17	3.28	3.24	3.83	4.00	3.96
Wood and Paper (NT) and their Products	3.50	3.67	3.58	3.25	3.94	3.64	3.17	3.44	3.31	3.58	3.72	3.69
Chemicals (NT)	3.75	3.67	3.73	3.17	3.89	3.64	3.17	4.11	3.74	3.42	3.89	3.71
Non-Metallic Minerals (NT)	3.33	3.89	3.71	3.33	3.94	3.68	3.50	4.11	3.85	3.83	4.06	3.99
Iron-metallurgical & Jewelry (NT)	3.33	3.67	3.54	3.17	3.72	3.47	3.25	3.89	3.64	3.75	3.89	3.89
Metal-Mechanics (NT)	3.75	3.61	3.66	3.17	3.94	3.64	3.33	4.00	3.74	3.92	3.94	3.96
Metals (NT)	3.25	3.56	3.44	3.17	3.94	3.64	3.33	4.11	3.81	4.00	4.11	4.07
Others Non-Traditional (NT)	3.17	3.89	3.64	3.00	3.94	3.57	3.08	3.72	3.47	3.42	.78	3.65

Note: T: traditional; NT: Non traditional.

* Gov.: 18 government officials.

** SEZ: 12 SEZ experts.

[Appendix Table 1-4] Results of Industry Selection for SEZs - ZED Matarani (Arequipa)

Industry	Abb.	Present		Future		Targeting	
		Share	Point	Score	Point	Total Point	Final Rank
Agriculture and Livestock	Agr	2.70%	11	4.17	13	24	2
Chemicals	Chem	1.40%	10	3.7	4	14	8
Fishing	Fish	0.40%	7	4.03	10	17	5
Iron-metallurgical, Jewelry	Iron	0.30%	6	3.83	5	11	10
Metal-Mechanics	Metal	0.20%	5	3.93	7	12	9
Non-metallic Minerals	Nmet	0.40%	8	3.97	9	17	5
Others-Non-traditional	Others	0.10%	3	3.63	1	4	12
Textiles	Tex	3.90%	12	3.93	7	19	3
Wood and Paper	Wood	0.00%	2	3.67	3	5	11
Traditional Agriculture	T Agr	0.10%	4	4.1	11	15	7
Traditional Fishing	T Fish	0.40%	9	3.97	9	18	4
Traditional Miners	T Min	90.20%	13	4.13	12	25	1
Traditional Oil & Natural Gas	T Oil	0.00%	1	3.67	3	4	12

<Appendix Table 1-5> Results of Industry Selection for SEZs - ZED Ilo (Moquegua)

Industry	Abb.	Present		Future		Targeting	
		Share	Point	Score	Point	Total Point	Final Rank
Agriculture & Livestock	Agr	0.1%	8	3.77	9	17	5
Chemicals	Chem	2.2%	12	3.73	8	20	4
Fishing	Fish	0.7%	10	3.87	12	22	2
Iron-metallurgical, Jewelry	Iron	0.1%	7	3.63	5	12	9
Metal-Mechanics	Metal	0.0%	6	3.73	8	14	7
Non-metallic Minerals	Nmet	0.0%	5	3.87	12	17	5
Others Non-traditional	Others	0.1%	9	3.47	4	13	8
Textiles	Tex	0.0%	4	3.23	1	5	11
Wood and Paper	Wood	0.0%	1	3.33	3	4	12
Traditional Agriculture	T Agr	0.0%	1	3.70	6	7	10
Traditional Fishing	T Fish	0.9%	11	3.83	10	21	3
Traditional Mining	T Min	95.9%	13	4.03	13	26	1
Traditional Oil & Natural Gas	T Oil	0.0%	1	3.30	2	3	13

<Appendix Table 1-6> Results of Industry Selection for SEZs - ZOFRATACNA (Tacna)

Industry	Abb.	Present		Future		Targeting	
		Share	Point	Score	Point	Total Point	Final Rank
Agriculture & Livestock	Agr	19.7%	12	3.47	6	18	5
Chemicals	Chem	2.8%	10	3.60	9	19	2
Fishing	Fish	14.1%	11	3.47	5	16	7
Iron-metallurgical, Jewelry	Iron	0.0%	4	3.50	7	11	10
Metal-Mechanics	Metal	2.3%	9	3.63	10	19	2
Non-metallic Minerals	Nmet	0.5%	6	3.70	12	18	5
Others Non-traditional	Others	0.3%	5	3.57	8	13	9
Textile	Tex	1.0%	7	3.70	13	20	1
Wood and Paper	Wood	1.6%	8	3.67	11	19	2
Traditional Agriculture	T Agr	0.0%	3	3.37	3	6	11
Traditional Fishing	T Fish	0.0%	1	3.20	2	3	12
Traditional Mining	T Min	57.5%	13	3.43	4	17	7
Traditional Oil & Natural Gas	T Oil	0.0%	2	3.03	1	3	12

02

CHAPTER

Analysis of FDI Attraction Strategies for SEZs in Peru, Including Incentives and Other Tools

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1. General Status of Peru's SEZ Incentives
2. Analysis of Korea's SEZ Incentives
3. Analysis of Korea's SEZ Development
4. Policy Proposal and FDI Attraction Strategies for Peru's SEZ
5. Implications and Policy Recommendations

Keywords
Special Economic Zone, Masan Free Export Zone, Incentives, Foreign Direct Investment, Anchor Company

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Summary

The Second Chapter focuses on the analysis of strategies to attract Foreign Direct Investment (FDI) for Special Economic Zones (SEZs) in Peru, including incentives and other tools. In the first section, this report overviews the general status of SEZ incentives in Peru, highlighting the tax exemptions and customs incentives offered to tenant companies in SEZs. The specific incentives for each SEZ, namely Tacna, Ilo, Matarani, and Paita, are discussed in detail.

At a glance, this report identifies three main problems faced by the Peruvian SEZs: low import tariff rates, lack of unique incentives, and a shortage of skilled labor. The report emphasizes the need for more attractive investment conditions and active incentives, such as rent reduction, employment incentives, and improved infrastructure, based on Korean SEZ's experience. Additionally, it highlights the importance of securing high-quality labor to meet industry demands.

Interviews with tenant companies and surveys with SEZ experts reveal that geographical location plays a crucial role in their decision to invest in SEZs. The availability of export items, proximity to neighboring countries, and accessibility to transportation networks are key factors influencing their choice. Respondents expressed satisfaction with the existing tax reduction benefits. However, there is room for improvement with regard to customs benefits, infrastructure development, and administrative services for tenant companies.

Next, this report analyzes Korea's SEZs and the incentives provided for attracting FDI. The history of SEZ development in Korea is outlined, highlighting the various types of zones established to promote balanced national development and industry-specific growth. The incentives provided in Korea's SEZs are examined, including simplified licensing procedures,

infrastructure development, project support, and tax reductions. The report differentiates between incentives for domestic and foreign companies in terms of infrastructure support, settlement conditions, tax reductions, and regulatory special provisions. The Free Economic Zone (FEZ) is highlighted as a significant category of SEZ in Korea, and details are provided on its development and associated incentives. The incentives include exemptions from charges, tax reductions, tariff reductions, and regulatory exemptions to foster investment. Foreign Investment Zones (FIZ), including complex-type and development-type zones, are also explored, emphasizing their role in attracting foreign investment and promoting regional development. Common incentives provided in these zones are discussed, such as exemption from regulations and the ability to change business types. Lastly, the report examines the Free Trade Zone (FTZ), which facilitates free trade activities, logistics, and distribution. The development and qualifications for occupancy in Free Trade Zones are outlined, highlighting the benefits for exporting companies, foreign-invested firms, wholesalers, and logistics businesses. Overall, Korea's SEZs offer a range of incentives to attract FDI, promote industrial growth, and enhance regional development.

In the third section, this report examines the development of Korea's SEZs, focusing on the Masan Free Export Zone and the Changwon National Industrial Complex. The Masan Zone successfully attracted foreign investment and anchor companies but faced challenges such as rising labor costs and the withdrawal of key businesses. The Changwon Complex specializes in machinery, transportation, and electronics industries. Lessons from the success and limitations of these zones offer valuable insights for the development of SEZs in Peru. Key policy suggestions include government commitment, selection of optimal location, demand surveys, active measures for investment attraction, incentives, attraction of anchor companies, and technology transfer.

The Saemangeum SEZ in Korea aimed to attract investment and promote economic co-operation. It involved significant costs, with the government providing incentives and subsidies to developers, local companies, foreign companies, and foreigners. In the initial project phases, limited investment presented challenges such as delays and rising costs. However, there has been a notable surge in overseas investment in recent times. The establishment of a Korea-China Economic Cooperation Complex and the development of a RE100 Industrial Complex were among the initiatives within the zone. The Vietnam Hung-Yen Province Industrial Complex served as an example for the involvement of Korean public agencies in establishing foreign industrial parks. The creation of a RE100 National Industrial Complex aimed to support companies' transition to renewable energy.

In the fourth section, this report outlines policy proposals and strategies for attracting FDI to Peru's SEZs. Key points include the importance of domestic companies moving into SEZs to enhance competitiveness, leverage technology transfer, and expand export opportunities. Incentive programs for tenant companies and public-side developers are crucial to address gaps in competitiveness. The attraction of anchor companies and the integration into regional value chains are emphasized. The recommendations include establishing an incentive system based on economic conditions, providing equal support to domestic companies, and creating a renewable energy-focused industrial complex. Implementing these measures will help attract FDI, strengthen the economy, and promote sustainable development.

At the end, this report's recommendations include establishing tailored incentive systems, supporting domestic enterprises, and creating a renewable energy pilot zone. By implementing these measures, Peru can attract FDI, enhance competitiveness, and foster sustainable economic growth.

1. General Status of Peru's SEZ Incentives

1.1. General Incentives

Special Economic Zones (SEZs) were created to promote investment and economic development in specific geographic areas. By providing incentives to companies that operate within the zones, SEZs aim to attract new businesses, encourage growth, and create jobs.

SEZ tenant companies in Peru receive two primary types of incentives. The first type is exemptions from income tax, general sales tax, selective consumption tax, and municipal promotion tax. The second type is a suspension of payment for import duties and taxes for goods imported from abroad. The permitted industries in Peru include the following: agribusiness, maquila and assembly, logistics, repair or refurbishment, telecommunications, information technology, research, scientific and technological development, human health research services, and infrastructure development.

<Table 2-1> Tax Exemptions

Tax	SEZ	Outside SEZ
Income Tax	0	29.5%
General Sales Tax	0	16%
Municipal Promotion Tax	0	2%
Selective Consumption Tax	0	2~30%
Ad Valorem when goods enter from abroad	0	0%, 6%, 11%
All taxes of the Central, Regional and Municipal Governments to be created, except contributions to EsSalud and fees	0	N/A

1.2. Incentives for Each SEZ

1.2.1. Tacna

Tax exemptions are as follows:

- Income Tax on profits (29.5% outside ZOFRATACNA);
- General Sales Tax (16%);
- Municipal Promotion Tax (2%);
- Selective Consumption Tax (ISC);
- Any tax from the Central, regional and municipal governments created or to be created, except EsSalud contributions and rates.

Customs incentives are as follows:

- The customs extraterritoriality condition exempts goods entering the Free Zone, whether from abroad or from the national territory, from any customs regime.
- ZOFRATACNA allows for the benefit of drawback and the return of the IGV for the final entry of national or nationalized merchandise from other parts of the national territory.
- The entry of goods from other parts of the territory facilitates the regularization of operations under the temporary admission regime.
- Free Warehouses allow for the indefinite storage of merchandise within them.
- The suspension of duties and import taxes is allowed for equipment, machinery, tools, spare parts, and construction materials from abroad that are necessary for the

development of activities.

- Products manufactured in ZOFRATACNA that are exported to the national territory are subject to the lowest tariff rate (Ad Valorem of 0%), in accordance with the current international agreements and conventions.
- The issuance of goods may qualify for temporary importation for outward processing or re-exportation in the same state.
- Exports of products made in ZOFRATACNA are eligible for the trade agreements signed by Peru, and they will meet the origin requirements established in each agreement, as well as any agreements that do not exclude products from free zones.

1.2.2. Ilo

Tax exemptions are as follows:

- Tenant enterprises of SEZs enjoy exemption from Income Tax, General Sales Tax, Selective Consumption Tax, and Municipal Promotion Tax.
- They are also exempted from any tax, including those created or to be created, that require an express exemption rule, whether imposed by the Central Government, regional governments, or municipalities.
- The transfer of goods and services between installed users is also exempt from Income Tax, General Sales Tax, Selective Consumption Tax, and any other tax created or to be created, including even those that require an express exemption.
- The electricity services demanded within the ZED Ilo are exempt from the General Sales Tax.
- All merchandise entering the national territory towards the ZED Ilo is considered an export and is not subject to the General Sales Tax.

Customs Incentives are as follows:

- The entry of machinery, equipment, raw materials, and inputs from abroad is exempt from import duties and taxes, and their time of permanence is the same as that of the company in the ZED Ilo, as established in the contract.
- Merchandise can be directly unloaded to the ZED Ilo with a Transfer Request, without the intervention of a customs agent at the point of arrival.
- To transfer merchandise to the ZED Ilo from border posts (Tacna, Puno, or Madre de Dios), it is only necessary to process the international transit of merchandise, covered

by a MIC/DTA, and it does not require the intervention of a customs agent.

- Merchandise can enter through any customs office in the Republic.

1.2.3. Matarani

Tax exemptions are as follows:

- Exemption from all taxes – created or to be created – for export activities;
- All goods and services entering the ZED Matarani from the national territory are considered as exports and are not subject to the General Sales Tax.

Customs Incentives are as follows:

- For the entry of goods, machinery, equipment, raw materials and inputs from abroad, the customs destination is suspended as long as said goods are within the ZED Matarani. The term of permanence is valid until 2042 (Law 30446).
- Re-dispatch and reshipment of goods abroad can be carried out.
- The entry of national or nationalized goods and other services for companies using the ZED Matarani will be considered as export.
- Entry of goods is allowed by any customs office of the Republic.
- Based on the Transfer Request, the benefit of arrival point is applied for the direct unloading of goods to the ZED Matarani without requiring the intervention of a customs agent.
- To transfer goods to the ZED Matarani from border posts (Tacna, Puno or Madre de Dios) it is only necessary to process the international transit of goods (covered by a MIC/DTA). It does not require the intervention of a customs agent.

1.2.4. Paita

Tax exemptions are as follows:

- Exemption from Income Tax, General Sales Tax, Selective Consumption Tax, and Municipal Promotion Tax is granted to all companies operating within the Special Economic Zone (SEZ).
- Goods of foreign origin, such as raw materials, inputs, machinery, and equipment, are subject to an Ad Valorem rate of 0% within the SEZ.
- Exemption from any tax created or to be created by the Central Government, regional

governments, and municipalities, including those requiring an express exemption rule, is provided to companies operating within the SEZ.

Customs Incentives are as follows:

- Suspension of the payment of tariffs and import taxes on machinery and equipment that user companies need for their production processes: These can enter the national territory by paying taxes for their depreciated value.
- Entry and exit of goods through any customs office in Peru.
- The goods resulting from maquila activity that return to the national territory only pay taxes for the incorporated value.
- Suspension of taxes for permanence of goods until 2042.
- Drawback export benefit (4% of the exported FOB value) is applicable.
- The export of processed products has commercial benefits according to the scope of the Free Trade Agreements (FTA).

<Table 2-2> Summary of SEZs Included

SEZ	Income Tax	General Tax	Selective Consumption Tax	Municipal Promotion Tax	Duty and Tax on Imported Products
Tacna	○	○	○	○	○
Ilo	○	○	○	○	○
Matarani					○
Paita	○	○	○	○	○
Outside SEZ	29.5%	16%	2~30%	2%	Ad Valorem when goods enter from abroad (0%, 6%, 11%)

1.2.5. Problems

The problems of the Peruvian SEZ can be summarized under three main categories. First, Peru's import tariff rate is the lowest in the world, with a real tariff of only 0.9. Therefore, tariff reduction benefits for moving into special economic zones are less effective. Second, apart from tax cuts and tariff benefits, Peru's SEZs lack unique incentives. Tax cuts and tariff benefits are passive support measures, and it would be good to provide active incentives such as rent reduction, low rent, or employment incentives, and to improve settlement

conditions through the construction of schools, hospitals, and apartments. Third, since there is a lack of skilled labor at present, efforts are needed from the Peruvian government to secure and provide high-quality labor.

1.3. Interview with Tenant companies[1]

It was found that the tenant companies were satisfied with the basic incentives provided, and in particular, considered the geographical location a great advantage when making the move-in decision. They first look at the ease of securing export items, accessibility to neighboring countries such as Chile, and distance from highways and ports before deciding whether to move in. Since the items exported from Peru are primary products of industries such as agriculture and mining, smooth physical movement is a very important factor in attracting tenant companies.

Through interviews with tenant companies, the research team discovered three problems: lack of infrastructure, incentives, and administrative services. First, availability of infrastructure such as electricity, water, and telecommunications is not adequate in the Peru SEZs. In the case of Ilo, the electricity supply is not sufficient to meet the businesses' demand, and accessibility by road is poor. The Matarani SEZ is also suffering from a lack of power supply. SEZs located in the south of Peru generally do not have sufficient electricity supply. In addition, companies are suffering from the lack of high-speed Internet communication. Additionally, the insufficient number of ships and containers in the port was also raised as a problem.

Second, tenant companies are demanding additional incentives apart from the current tax benefits. For example, they demanded services that allow indefinite storage of imported raw materials and special measures for personnel recruitment and management. Some wanted to find people with expertise, so they also requested the provision of a relevant talent pool. However, the corresponding information could not be provided.

Third, administrative services for tenant companies are not sufficient. In the case of Ilo, a one-stop service was provided a few years ago, but it is not available currently. It is scheduled to start again in 2023 due to the demand of companies. In the case of Matarani and Paita, it takes too long to get approval from the government due to slow administrative procedures. The number of customs officers is also not enough, so the waiting time is long.

1 Date: March 17, 2023 (Fri) 23:00~23:50, Target: Representatives of four tenant companies in Peruvian SEZs.

In particular, Peru needs to actively utilize the ombudsman system to improve the issue of insufficient administrative services raised at the end. Korea is making the most of the ombudsman system to actively attract foreign direct investment.

1.4. Survey[2]

The research team conducted a local survey to analyze satisfaction with SEZ incentives in Peru and future improvements. The survey was conducted over a period of two weeks from March 13 to March 24, 2023, and a total of 43 people responded.

① Are the following tax exemptions or exoneration necessary to attract more FDI to SEZ in Peru?

Satisfaction with the five tax reduction benefits currently provided was investigated. More than 70% responded that they were satisfied with all items, and the item with the highest satisfaction was Exemption from the Ad Valorem Tariff (86.3%). On the other hand, satisfaction with Exoneration of the Municipal Promotion Tax was the lowest at 70.4%.

<Table 2-3> Satisfaction with the Five Tax Reduction Benefits

(Unit: %)

Item	① Strongly necessary	② Necessary	③ Neutral	④ Not necessary	⑤ Not necessary at all	⑥ Not available
Income Tax exemption (IT outside the SEZs is 29.5%).	43.2	38.6	13.6	2.3	2.3	0.0
Exemption from General Sales Tax (IT outside the SEZs is 16%).	40.9	40.9	11.4	4.5	2.3	0.0
Exoneration of the Municipal Promotion Tax (The same tax outside the SEZs is 2%).	29.5	40.9	20.5	6.8	2.3	0.0
Exemption from the Selective Consumption Tax (Outside the SEZs, it varies between 2% and 30% depending on the product).	36.4	38.6	11.4	11.4	2.3	0.0
Exemption from the Ad Valorem Tariff when goods enter from abroad (Outside the SEZs, the rates are 0%, 6% and 11%).	47.7	38.6	9.1	2.3	2.3	0.0
Exoneration of all taxes of the central, regional and municipal governments to be created, except contributions to EsSalud and fees.	31.8	38.6	18.2	4.5	6.8	0.0

2 Duration: From March 13, 2023 (Monday) to March 24, 2023 with the participation of 43 respondents.

② Is the following customs benefit applied to your company? And to what extent are you satisfied with the following customs benefits?

Next, participants were asked about their satisfaction with the tariff benefits. Satisfaction with tariff benefits was found to be lower overall compared to satisfaction with tax reduction. Excluding 'not applicable', satisfaction with import of products according to international agreements and conventions was the highest at 71.1%, and satisfaction with direct export without going through the customs system was the lowest at 51.5%.

<Table 2-4> Satisfaction with the Tariff Benefits

(Unit: %)

Item	① Very Satisfied	② Satisfied	③ Neutral	④ Dissatisfied	⑤ Very Dissatisfied	⑥ Not Available
Deferment of customs duties and taxes when importing raw materials and equipment from overseas	25.0	27.3	31.8	0.0	2.3	13.6
Indefinite permanence of goods within the SEZs	31.8	25.0	27.3	2.3	0.0	13.6
Direct export without going through the customs system	20.5	18.2	34.1	2.3	0.0	25.0
Import of products according to international agreements and conventions	34.1	27.3	22.7	2.3	0.0	13.6
No need for prior storage when bringing in goods	40.9	18.2	25.0	2.3	0.0	13.6

③ What kind of additional incentives are needed to develop SEZs in Peru and attract more companies?

Finally, participants were asked about additionally necessary incentives, with 16 items mentioned with the question. The most urgent task was found to be the expansion of infrastructure. 'Construction of highways and railways' showed the highest rate with 97.7%, followed by 'Renewable energy supply' with 86%. Next to infrastructure, incentives for land use were high. Demand for 'Permission to use land and buildings' was 81.4%, and 'Support for office construction costs' was 61.4%.

Other than that, requests for direct cost support and improvement in foreign settlement conditions were found to be high. As for direct cost support, 'Support for education and training expenses' accounted for 60.5% and 'Support for equipment purchase costs' accounted for 52.3%. As for the improvement of foreign settlement conditions, 'Establishment

and operation of foreign educational institutions' accounted for 54.8% and 'Provision of foreign language services' accounted for 54.5%.

<Table 2-5> Additional Incentives Needed

(Unit: %)

Item	① Strongly Necessary	② Necessary	③ Neutral	④ Not Necessary	⑤ Strongly Not Necessary	⑥ Not Available
Permission to use land, buildings, etc.	29.5	50.0	13.6	4.5	0.0	2.3
Rent reduction	11.4	31.8	34.1	18.2	2.3	2.3
Support for office construction costs	13.6	47.7	34.1	4.5	0.0	0.0
Support for equipment purchase costs	11.4	40.9	40.9	6.8	0.0	0.0
No interest on equipment purchase	4.5	29.5	56.8	2.3	2.3	4.5
Provision of housing	6.8	25.0	43.2	22.7	0.0	2.3
Provision of foreign language services	18.2	36.4	40.9	4.5	0.0	0.0
Establishment and operation of foreign educational institutions	9.1	43.2	36.4	6.8	0.0	4.5
Establishment of a day care center exclusively for foreign children	2.3	20.5	56.8	13.6	2.3	4.5
Establishment of a foreign medical institution or pharmacy exclusively for foreigners	0.0	29.5	54.5	6.8	4.5	4.5
Permit for casino business only for foreigners	0.0	6.8	50.0	22.7	11.4	9.1
Broadcasting in foreign languages	0.0	20.5	59.1	6.8	4.5	9.1
Support with employment subsidy	4.5	34.1	29.5	22.7	2.3	6.8
Support for education and training expenses	20.5	38.6	34.1	4.5	0.0	2.3
Renewable energy supply	43.2	40.9	11.4	2.3	0.0	2.3
Construction of highways, railways, etc.	61.4	34.1	2.3	0.0	0.0	2.3

1.5. Implications

As a result of analyzing the current status of incentives in the Peruvian Special Economic Zone and conducting interviews with resident companies, it is judged that investment in basic infrastructure, active provision of incentives, building clusters for related industries and recruitment of tenant companies through linkage with the regional value chain are necessary to activate FDI.

First, even if there is a geographical advantage, it is difficult for companies to move into Special Economic Zones if basic infrastructure for business activities is not in place. Sufficient supply of electricity and water, establishment of high-speed Internet communication network, and smooth connection with highways and ports are the requirements that must be fulfilled preemptively in revitalizing the Peruvian Special Economic Zones and expanding foreign direct investment in the future.

Secondly, the incentives offered in Peruvian Special Economic Zones are currently limited to tax cuts and tariff benefits, without any active support measures in place, such as subsidies, improved settlement conditions, or the provision of auxiliary facilities. As a result, there is a lack of sufficient incentives for domestic companies to enter the zone, which has led to insufficient economic activity within the Special Economic Zones. Without additional supporting incentives, it may be difficult to attract companies to the Special Economic Zones and fully realize the potential benefits of this policy.

Thirdly, in order to vitalize Peruvian Special Economic Zones and FDI, it is necessary to build clusters in Peru where related industries can develop. Since tenant companies are currently running businesses mainly in agriculture and mining, it is possible to consider building clusters to create synergies by gathering related businesses.

Lastly, in order to develop new industries, it is important to link with Regional Value Chains (RVCs), although there are no existing industries in Peru. In producing agricultural and mining products based on the primary industry, it is necessary to establish an export strategy by selecting items that allow Peru to have a competitive edge compared to neighboring countries such as Chile and Bolivia. Currently, Peru is producing mainly primary industrial products, but in order to develop into a high value-added industry in the future, it is necessary to accumulate technology by linking with RVC.

2. Analysis of Korea's SEZ Incentives

2.1. Scope of Analysis

Korea has designated and developed various types of Special Economic Zones to promote balanced national development and revitalize local economies, including regionally specialized development special zones, special tourism zones, enterprise cities, and innovation cities. In addition, special zones and base support systems such as R&D special zones and high-tech medical complexes have been introduced to develop specific industries

and fields. Chapter 2 provides an overview of the incentives provided to Free Economic Zones (FEZ), Foreign Investment Zones (FIZ), and Free Trade Zones (FTZ) among various types of Special Economic Zones in Korea so that the Peruvian government may consider the incentives appropriate for Special Economic Zones in the country. Please refer to Chapter 3 for the general characteristics of Korea's Special Economic Zones.

2.2. Korea's SEZ Incentives

Special Economic Zones are established based on policies aimed at creating industrial clusters and regional development through intensive attraction of foreign-invested companies, and are areas that attract foreign investment to collectively develop specific areas through intensive investment, development, and incentives.

Special Economic Zones vary from system to system, but in general, special regulatory measures such as deregulation and simplification of licensing procedures, creation of infrastructure and settlement conditions, development project support, and tax reduction are provided as incentives.

Korea operates various Special Economic Zones, and each special zone is eligible for a differentiated incentive system. Korea's incentive system can be divided into support for developers and support for tenant companies, and support for domestic companies and support for foreign companies. Support for developers includes support for infrastructure construction and improvement of living conditions, and support for tenant companies includes tax cuts and rent cuts.

<Table 2-6> Incentives for Domestic Companies

Type	Supporting Developers		Supporting Tenant Companies				
	State Support for Infrastructure	Settlement Conditions (Complex Development)	Tax reduction or exemption			Location Support (Low-cost Rental)	Regulatory Special Provisions (Management, Labor)
			Corporate Tax, Income Tax	Customs Duties	Local Taxes		
Free Economic Zone	○	○	X	X	X	X	X
Foreign Investment Zone	○	X	X	X	X	X	X
Free Trade Zone	X	X	X	X	X	X	○

Source: Adapted from KIEP (2015).

<Table 2-7> Incentives for Foreign Companies

Type	Supporting Developers		Supporting Tenant Companies				
	State Support for Infrastructure	Settlement Conditions (complex development)	Tax reduction or Exemption			Location Support (low-cost rental)	Regulatory Special Provisions (management, labor)
			Corporate Tax, Income Tax	Customs Duties	Local Taxes		
Free Economic Zone	○	○	○	○	○	○	○
Foreign Investment Zone	○	X	○	○	○	○	△
Free Trade Zone	X	X	○	○	○	○	△

Source: Adapted from KIEP (2015).

There is a big difference between Korea and Peru in terms of incentive systems. It must be noted once again that Peru is implementing passive policies focused on tax reduction, while Korea is implementing active incentive policies such as infrastructure construction, settlement improvement, low rental rates, and management support.

<Table 2-8> Incentives Comparison between Peru and Korea

Country	Supporting Tenant Companies					Supporting Developers	
	Tax Reduction or Exemption			State Support for Infrastructure	State Support for Infrastructure	State Support for Infrastructure	Settlement Conditions (complex development)
	Corporate Tax, Income Tax	Customs Duties	Local Taxes				
Peru	○	○	X	X	X	X	X
Korea	○	○	○	○	○	○	○

2.3. Free Economic Zone

2.3.1. Development Status

Korea's efforts to promote the establishment of Special Economic Zones were formalized in the 「Special Act on the Designation and Management of Free Economic Zones」, enacted to foster business hubs in Northeast Asia and attract foreign investment. Following amendments to the relevant laws in December 2002, three Free Economic Zones were designated in Incheon, Busan/Jinhae, and Gwangyang Bay in 2003, followed by Daegu/Gyeongbuk, Yellow Sea, and Saemangeum in 2008. The total area of the Free Economic Zones now stands at 293km², with the project being of high national importance. As part of government support, about 2.25 trillion won has been invested in infrastructure

construction. Over 6,600 domestic companies and 450 foreign investment companies were located within the zones at the end of 2021.

2.3.2. Incentives

Incentives provided to a foreign investment company for Free Economic Zones are as follows:

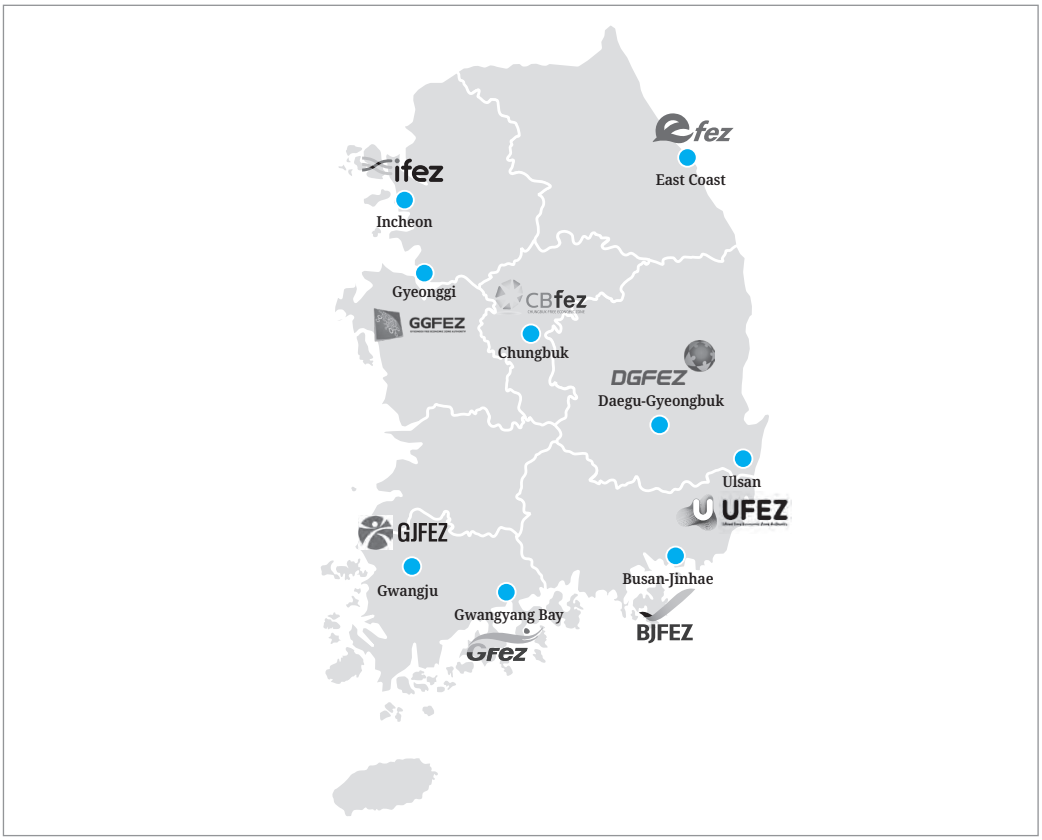
- During the development phase, both domestic and foreign developers are facilitated with special procedures and regulatory exceptions. This includes exemptions from seven different charges, such as development charges, traffic congestion charges, and farmland preservation charges. In addition, 50% of the national budget is allocated to support the construction of access and arterial roads, which can help reduce construction costs.
- Foreign investment companies may be eligible for a 100% exemption from corporate tax and income tax for five years, followed by a 50% exemption for an additional two years. To qualify, the company must make a minimum investment of $30 million for manufacturing, $20 million for tourism, $10 million for logistics, $2 million for R&D, or $30 million for development.
- Foreign investment companies in Free Trade Zones can enjoy 100% tariff reduction for 5 years. This incentive is provided for manufacturing companies investing more than $30 million, tourism companies investing more than $20 million, logistics companies investing more than $10 million, R&D companies investing more than $2 million, and development companies investing more than $30 million.
- Regarding foreign investment company, local taxes, such as acquisition tax and property tax, can be reduced or exempted for up to 15 years by means of ordinances enacted by local governments.
- Foreign investment companies can receive various deregulation and special treatments related to labor and management. For example, they may be excluded from the obligation to hire persons with disabilities and men of merit, and also from restrictions on duration, work, and unpaid leave for dispatched workers. Additionally, the application of regulations may be excluded so that new factories can be built in the metropolitan area.
- A special exception is granted to create a foreigner-friendly settlement environment. Foreign educational institutions and medical institutions are allowed to be established, and foreign educational institutions that move in are provided support with construction and initial operating expenses.

- National and public land can be leased for 50 years, and the rent is 1% of the land value. The rent can be reduced by 50-100% according to local government ordinances.
- Fund support up to 30% of the investment amount (R&D 40%) is provided when investing in new technology, large-scale job creation, R&D center, etc.

There are other incentives provided to companies occupying Free Economic Zones.

- 100% exemption from customs duties for 5 years, and 100% exemption from acquisition tax and property tax for up to 15 years.
- In the case of building infrastructure such as roads, railways, airports, ports, and sewers, 50% of government subsidy is provided, and 100% support can also be availed according to the decision of the Free Economic Zone Committee.
- In addition, various regulatory special cases are applied, such as exempting various approvals and permits required for development, excluding the upper limit on the sale price of apartment houses, and easing the building-to-land ratio and floor area ratio.

[Figure 2-1] Korea Free Economic Zones



Source: Korea Free Economic Zone Office.

2.4. Foreign Investment Zone

2.4.1. Development Status

Foreign Investment Zones are designated to attract large-scale foreign investment, promote the advancement of the Korean economy's industrial structure, facilitate technology transfer, and create opportunities for employment. The government offers various incentives including tax cuts and rent reductions, as well as the streamlining of administrative regulations, to encourage investment in these regions. There are two types of investment zones: complex-type Foreign Investment Zones and development-type Foreign Investment Zones.

- Complex-type Foreign Investment Zone: Introduced in 1994 as a way to promote domestic investment by foreign companies as well as the development of advanced, cutting-edge technologies.
- Development-type Foreign Investment Zone: Introduced for the purpose of facilitating the balanced development of national regions and attracting foreign investment to regions with low investment levels and high potential for development.

Despite their differing origins and legislative frameworks, both complex-type and development-type foreign investment zones were merged into a unified entity under the 2004 Foreign Investment Promotion Act, considering their common goal of promoting foreign investment. Presently, more than 250 companies are housed in the 21 complex-type and 71 development-type Foreign Investment Zones that have been designated.

2.4.2. Incentives

Incentives for Foreign investment Zones are as follows:

2.4.2.1. In Common

When a foreign-invested company chooses to relocate or establish a factory with an area of at least 500 square meters in a Foreign Investment Zone, they are not subject to other regulations or laws. Additionally, they are permitted to change their type of business during this process.

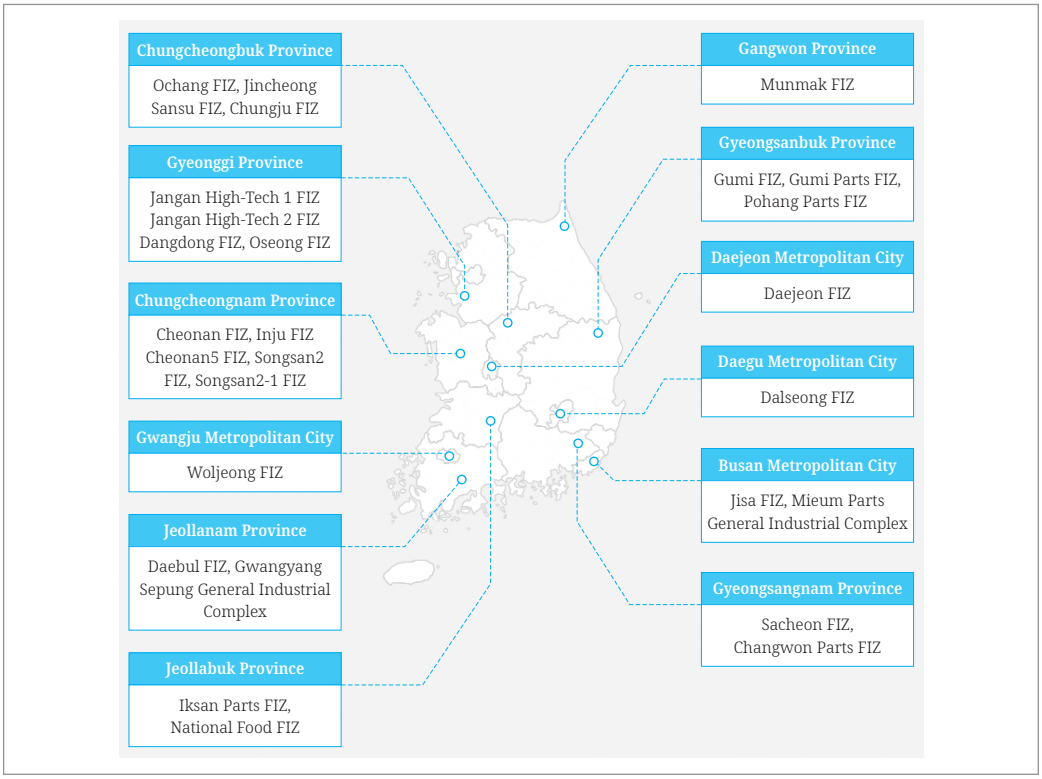
2.4.2.2. Complex-Type

- Support for land purchase costs is provided, with a rate of 40% in metropolitan areas and 60% in other regions.
- For the first three years from the commencement of business, foreign-invested companies are exempted from acquisition tax and property tax. For the following two years, they can avail a reduced rate of 50%.
- Tariff exemption of 100% is granted on imported capital goods for a period of 5 years.
- A reduction of 100% in local taxes is offered for up to 15 years.
- Rent reduction is provided in proportion to the amount of investment by foreign investors, and the number of full-time workers is calculated based on the month before the notice of rent payment. The rent for national and public properties is at least 5% of the acquisition price, but if a company establishes its facility in a Foreign Investment Zone, the rent is set at a minimum 1% of the acquisition price.

2.4.2.3. Individual Type

- Support for land purchase costs is available at a rate of 40% in metropolitan areas and 60% in other areas.
- Acquisition tax and property can be waived in full for 5 years from the date of business commencement, with a 50% reduction for the following 2 years.
- Reduction in local tax is available for up to 15 years.
- Reduction of rent is subject to the decision of the Foreign Investment Committee, which may approve up to 100% reduction based on the impact on the national economy.

[Figure 2-2] Korea Foreign Investment Zones



Source: Korea Trade Investment Promotion Agency.

2.5. Free Trade Zone

2.5.1. Development Status

Free Trade Zones (FTZ), managed under the 「Act on Designation and Management of Free Trade Zones」, provide a guarantee for free trade activities such as manufacturing, logistics, and distribution. These zones serve as a system to promote trade and regional development through free trade, and to attract foreign investment and introduce advanced technologies. The establishment of Free Trade Zones began with the Free Export Zone Establishment Act in 1970, which aimed to increase employment by creating new export engines.

In 2000, the 「Act on the Designation and Management of Free Tariff Zones for Fostering International Logistics Bases」 was enacted, and in 2002, the Customs Free Zone was established to facilitate logistics between countries. This was intended to foster the region as an international logistics center and contributed to the sound development of the national economy. Tariffs were suspended for international logistics companies and exporters, and customs procedures were simplified to facilitate free logistics activities at airports, ports,

and hinterlands.

In 2004, the「Act on Designation and Management of Free Trade Zones」was amended, and the Customs Free Zone was integrated into the Free Trade Zone. The existing free export zones and free customs zones were combined and operated as Free Trade Zones. Currently, there are two types of Free Trade Zones: industrial complex type and airport/port type. A total of 13 Free Trade Zones are designated and in operation, including 7 industrial complex types and 6 airport/port types, with over 300 companies located in these zones, including over 200 foreign-invested companies.

2.5.2. Qualifications for Move-in

Qualifications for occupancy in Free Trade Zones can be largely divided into four categories: manufacturing mainly for the purpose of export, foreign-invested companies, wholesalers mainly engaged in import and export transactions, and complex logistics-related businesses.

- Exporting companies must have an export ratio of 30% or more[3]. For foreign-invested companies, the amount of foreign investment has to be 100 million won or more and the share ratio has to be 10% or more.
- Priority is given to businesses that attract foreign investment in connection with high-tech industries, high-tech accompanying businesses, and regional strategic businesses.

2.5.3. Incentives

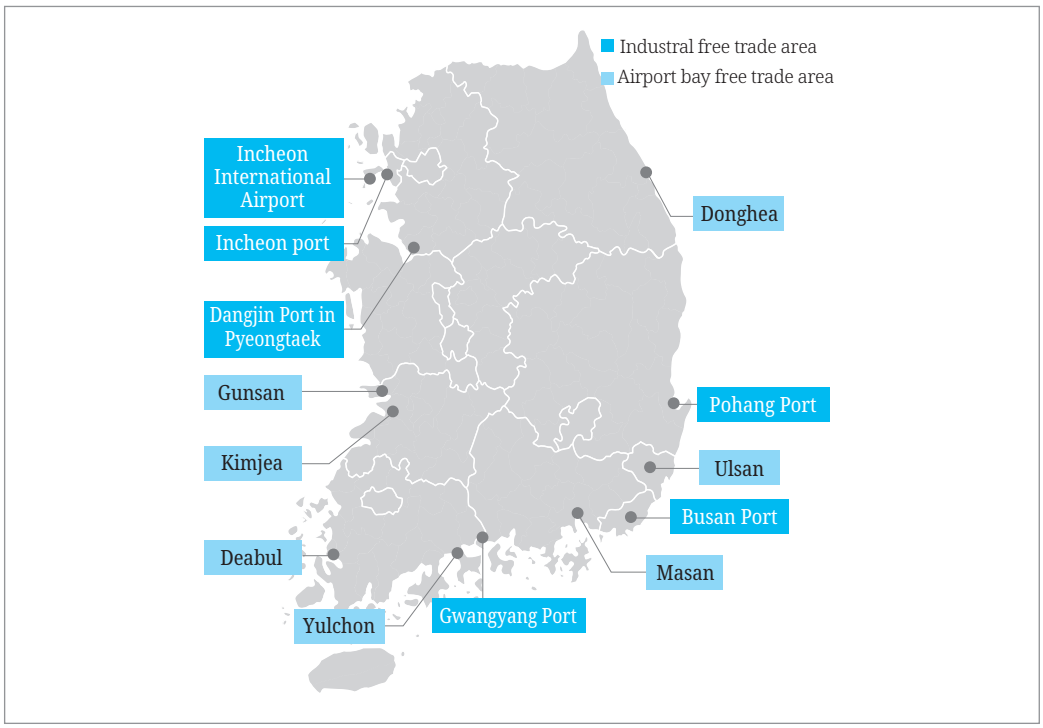
Incentives for Free Trade Zones are as follows:

- Customs duties are deferred when importing goods necessary to achieve business purposes, such as facility materials, raw materials, and construction materials from abroad.
- For corporate tax and income tax, companies in the Masan Free Export Zone receive exemptions of 100% for 5 years and 50% for an additional 2 years, and in other regions, the exemptions are 100% for 3 years and 50% for an additional 2 years.
- Acquisition tax, registration tax, property tax, and collective land tax are exempted up to 100% for 15 years and the reduction rate is determined by local government ordinances.

3 Small and Medium-sized Enterprises account for 30%, and medium-sized enterprises and large enterprises have different export obligations.

- Foreign goods and services supplied or provided between resident enterprises within the Free Trade Zone are exempted from value-added tax.
- Raw materials imported for export are exempt from value-added tax.
- If the foreign investment ratio is 30% or more, the rent is waived.
- For a foreign-invested company in which a foreigner is the largest shareholder, the rental fee is exempted if the investment amount is over $1 million.
- Part of the manufacturing process can be completed in the domestic customs area, and the processed product can be exported locally.
- Foreign goods, such as facilities and equipment necessary for processing, can be taken out of the domestic customs area in an assembled state.
- Products such as idle equipment and production parts can be taken out of the country.
- Resident companies are exempted from traffic congestion charges.
- Foreign-invested companies are not subject to employment protection regulations.
- Local governments provide various subsidies such as recruitment subsidies and training subsidies.

[Figure 2-3] Korea Free Trade Zones



Source: Korea Free Trade Zone Office.

2.6. Implications

The analysis of Korea's current Special Economic Zones and incentives yielded three implications. Firstly, Korea's special economic zones offer common incentives like tax cuts and tariff benefits to foreign-invested companies, regardless of the type of Special Economic Zone. However, unlike Peru, Korea's Special Economic Zones share the common feature of reduced rent. Secondly, incentives are not only provided to resident companies but also to development projects that create an environment conducive to attracting companies. For instance, Free Economic Zones and Foreign Investment Zones invest in building infrastructure and creating special economic zones. Free Economic Zones are particularly proactive in attracting foreign investors by setting up hospitals and schools for foreigners and supporting construction and initial operational costs. Thirdly, the Korean government provides both passive incentives like tax cuts and tariff benefits, as well as active incentives like subsidies and regulatory exceptions. In the case of Free Trade Zones, local governments provide subsidies for personnel recruitment and training, while in Free Economic Zones, labor laws are relaxed, allowing foreign companies to draw benefits from separate regulations.

3. Analysis of Korea's SEZ Development

3.1. Overview

Korea's Special Economic Zones have continued to develop over the past 50 years. The Masan Free Export Zone, which was first established in Korea in 1970, has played a major role in economic development as an export development base in Korea. The Changwon National Industrial Complex that began operations in 1975, played a role in the Masan Free Export Zone's continued growth. In 1978, large companies based on heavy and chemical industries such as Geumseongsa, Daewoo Heavy Industries, Kia Engineering & Construction, Korea Special Steel, Busan Steel, Samsung Heavy Industries, and Hyosung Heavy Industries entered the market. At the same time, the Masan Free Export Zone strengthened exports by serving as a production base for the Changwon National Industrial Complex.

Since the 2000s, the Korean government has promoted the development of the Saemangeum Special Economic Zone to strengthen it as the economic center of Northeast Asia. Accordingly, in 2011, under the supervision of the Prime Minister's Office, the Saemangeum Comprehensive Development Plan was established and efforts were made to develop it as the most attractive investment target in Northeast Asia. In addition, several

types of incentives were prepared so that various subjects could benefit from development, and joint development with the private sector was facilitated to resolve financing and increase the possibility of success.

Since the 2020s, carbon reduction issues have emerged around the world, and Korea's Special Economic Zones are also actively trying to respond to the climate change issue. In the case of the Saemangeum Special Economic Zone mentioned above, a large-scale solar power generation complex is being created to produce new and renewable energy. In particular, Dangjin is developing Korea's first RE100 industrial complex and is promoting it to be designated as a Special Economic Zone eligible for deregulation.

3.2. Analysis of Korea's SEZ FDI

Korea's first Foreign Direct Investment was allowed in 1962, when Chemtex of the United States invested $580,000 in the Filament Nylon project in Korea. In introducing foreign capital, the Korean government promoted a strategy to attract loan-based foreign investment rather than direct investment, limiting Foreign Direct Investment until the early 1980s. However, in the 1980s, policy changes were made in the direction of actively utilizing FDI, and the foundation for attracting Foreign Direct Investment began to be established. In the 1990s, liberalization policies focused on attracting foreign investment in the high-tech sector were promoted to advance the industrial structure.

Korea's foreign investment policy has changed considerably since the financial crisis of 1997. The government has shifted its foreign investment policy stance from existing overseas lending and investment regulations to attract and support investment that stably makes up for the insufficient foreign currency. Furthermore, it was intended to promote the restructuring of the domestic industry and introduce advanced technologies and management techniques. During this period, foreign exchange transactions were liberalized by abolishing regulations on overseas remittances and overseas investment by Koreans to promote foreign investment, and opening the securities market to foreigners to induce the advancement of the capital market.

In 1998, the Foreign Investment Promotion Act was newly enacted to reorganize laws and systems to attract foreign investment. This law can be seen as the basis of Korea's foreign investment support system in that it stipulates the requirements, procedures, and support for foreign investment, and it is also the basis for foreign investment areas, one of the special economic zones.

<Table 2-9> Korean Government's FDI Policy

Division of Years	Korean Government's Policy	Main Contents
1960s	The introduction of a foreign investment system	Initiating aid and introduction of foreign capital from overseas allies (Deputy loans, etc.)
1970s	Allowing limited foreign investment	- Protecting domestic industries and restricting investment - Designation of Free Export Zone
1980s	Foreign Direct Investment regulations and loan focus	Attracting foreign investment with a focus on loans
Since 1997	Relax investment restrictions and expand investment	Liberalize investment, open investment, improve the living environment, etc.

3.3. Masan Free Export Zone[4]

3.3.1. Background and Purpose

In 1962, the Korean government initiated its first Five-year Economic Development Plan with the aim of modernizing the country's industrial structure. Despite recognizing the importance of Foreign Direct Investment (FDI), the country struggled to achieve significant results. Though exports increased, Korea remained heavily dependent on foreign resources to promote economic development. This imbalance led to an unstable balance of payments since raw materials were imported, processed, and then re-exported. To address this situation, the government shifted its economic structure from import substitution to an export-led structure and identified the need to establish special export zones in coastal areas.

The concept of a free export zone emerged from visits by officials from the Federation of Korean Industries to Japan and Taiwan in 1964. At a meeting in January 1969, the Federation suggested the establishment of a special free zone in the coastal areas to increase exports, a proposal that was ultimately adopted by the Korean government. The Masan Free Export Zone was established as an optimal solution to utilize FDI more actively in the process of economic growth. The goal was to create a large-scale coastal industrial complex to attract foreign investment, increase exports, expand employment, and absorb advanced technologies to secure technological capabilities. The Office of the President played an active role in all stages of development, from site selection to complex development, and in July 1969, the government officially announced the establishment of a Free Export Zone.

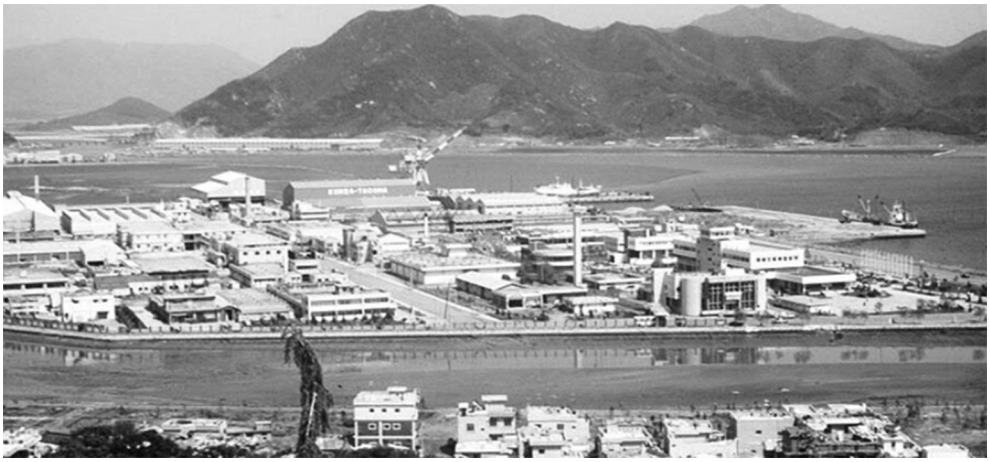
4 The Masan Free Export Zone was renamed to Free Export Zone after 2000.

[Figure 2-4] Masan Free Export Zone

[Figure 2-5] President Park's Visit to the Construction Site of the Masan Free Export Zone

Source: Masan Free Trade Zone Office.

[Figure 2-6] Construction of Masan Free Export Zone (1970)



Source: Masan Free Trade Zone Office.

3.3.2. Progress and Achievements

In March 1970, the Ministry of Construction established a construction office in the Masan Free Export Zone to begin the construction project in earnest, which lasted from April to December of 1971. The government invested a total of 9.216 billion won in constructing complexes and standard factories until 1977. Public facilities, welfare facilities, and infrastructure such as roads, sewage, electricity, telegraph, industrial water, and port facilities were also constructed to support the launch of the Masan Free Export Zone as an export base.

The Masan Free Export Zone provided resident companies with one-stop services for all administrative tasks such as notification of foreign investment opportunities and related requirements and processes, factory building permits, and import and export approval. To attract investment and promote exports, various benefits such as tax cuts, low rent, and support facilities were granted to foreign investors. Import and export activities were more convenient due to its status as a non-tariff zone. However, the government enforced strict qualifications for initial occupancy, selecting industries with high labor intensity, long processing duration, backward manufacturing and processing technologies in Korea, and industries that do not hinder domestic export industries.

The Masan Free Export Zone has led Korea's export industry since 1971. The factory Saemaeul Movement was also actively carried out to attract foreign-invested companies. The zone saw rapid growth from 4 companies in 1970 to 115 companies in 1973, with exports

exceeding $300 million in 1976 and investment exceeding $100 million in the same year. As of the end of 2021, the Masan Free Export Zone's exports reached $947 million, accounting for 50.4% of the total Free Trade Zone exports of $1,838.4 million, and the number of employees was 5,314, accounting for 50.4% of the 10,543 employees at Free Trade Zones nationwide.

When Masan Free Export Zone was established, 74% of the 98 companies were Japanese sole-investment companies and 21% were Japanese and Korean joint ventures, and the remaining 5% were companies that received investments from countries other than Japan. Since Masan is located geographically close to Japan, Japanese companies have been very active in investing. Their average investment was $81.3 million per company. Most of the tenant companies were small and medium-sized labor-intensive Japanese companies, followed by businesses in electronics (27%), machinery (23%), chemistry (14%), and metal (11%). The Korean government hoped to attract heavy and chemical industries such as steelmaking, steel, machinery, and shipbuilding to the Masan Free Export Zone, but in reality, most of the companies that moved in belonged to light industries.

It was in the 1980s that the technology of Masan Free Export Zone reached advanced levels. In the 1980s, emphasis shifted from simple labor-intensive industries to technology-intensive industries due to wage increases as well as technology transfer and management know-how transfer from advanced companies. In the 1970s, sewing, shoes, miscellaneous goods, and assembly of simple electronic components were the main focus areas, while after the 1980s, precision equipment, processing, and high-end electronic component assembly were mainly developed. As a result, exports exceeded USD 1 billion in 1986, and the number of employees in 1987 was 36,411, which was the highest ever.

3.3.3. Attracting Anchor Enterprises

The attraction of anchor companies has played a major role in the success of the Masan Free Export Zone. Conversely, exports also decreased significantly as anchor companies reduced their business size or withdrew from the Zone. The representative anchor companies in Masan Free Export Zone are Sony Electronics Korea and Nokia TMC.

Sony Electronics Korea first moved into the Masan Free Export Zone in 1972. Based on Sony's technology, Masan produced high-value-added products such as ultra-precision electronic components, high-performance broadcasting equipment, and mobile projectors, and succeeded in exporting $1 billion and hiring 5,000 workers in the early 2000s. However, due to rising labor costs in Korea, production lines were shifted to China, Malaysia, and

Thailand in 2003, and the size of the project decreased to $100 million in exports and 400 employees as of 2012.

Another example of an anchor company is Nokia TMC. Nokia TMC moved into Masan Free Export Zone in 1984 for the purpose of manufacturing mobile phones. As Nokia's global market share increased, Nokia TMC's production and export volume also increased. Exports of $50 million in 1998 and $2 billion in November 2001 were achieved, and the company provided employment to more than 2,000 workers annually until the mid-2000s, accounting for 80% of the exports from the Masan Free Export Zone. However, since the 2010s, Nokia's global mobile phone sales have declined, reducing its workforce to less than 200. Eventually, Nokia's headquarters moved some of its production lines to its Chennai plant in India, where labor costs were low, and the company withdrew from Masan Free Export Zone in April 2014.

3.3.4. Implications

Masan Free Export Zone began in the 1970s with the growth of the Korean economy and has been successful enough to account for a large proportion of Korea's exports. Direct achievements include attracting foreign investment, increasing exports, acquiring foreign currency, and increasing employment in economic terms. Indirect achievements include transfer of advanced technology, transfer of advanced management know-how, and revitalization of the local economy in terms of social benefits.

With the success of the Masan Free Export Zone, it was able to contribute to economic development at both the national and global levels. At the national level, it was possible to promote the creation of new Free Trade Zones such as Gunsan and Daebul by acquiring know-how on the creation and operation of Free Trade Zones. In addition, based on Masan's success, it was able to play a positive role in encouraging foreign-invested companies to enter Korea. In terms of global performance, as Korean companies participated in the Global Value Chain, they were able to expand trade opportunities and contribute to increasing the size of trade.

However, the limitations of the Masan Free Export Zone include loss of competitiveness due to wage increases, lack of differentiation compared to new Special Economic Zones, and decline due to the reduction and withdrawal of anchor companies. After the 1988 Seoul Olympics, the democratization and increased autonomy of the Republic of Korea led to changes in the labor-management environment. Workers' strikes and labor disputes also occurred in Masan's Free Export Zone, and exports fell by 5.8% in 1989 and 15.7% in

1990 for the first time. Next, as the first Free Export Zone in Korea, its attractiveness has also decreased due to aging. As the overall production facilities and infrastructure are underdeveloped, the attractiveness has decreased compared to new Special Economic Zones. Finally, since the 2000s, Masan's Free Export Zone has begun to decline as business size of anchor companies decreased, such as Sony Electronics Korea's reduction in business size and Nokia TMC's withdrawal of business operations.

Since the 2010s, the Masan Free Export Zone has been promoting a new type of development. The local government promoted the modernization of facilities in the Masan Free Export Zone through structural advancement projects for aging facilities. As of the end of 2022, the number of companies in the Masan Free Export Zone is 127, of which only 65 companies, or half, are foreign-invested companies. Over time, the share of foreign investment decreased significantly, while the share of domestic companies moving in increased.

3.3.5. Policy Suggestions

The Masan Free Export Zone, a policy model, is Korea's first Free Export Zone and a successful model globally, and offers a great lesson for Peru's Special Economic Zones. Accordingly, the KSP team would like to present seven policy proposals.

① The Peruvian government should pursue the development of Special Economic Zones from preparation to completion with deep interest and strong will.

② It is necessary to select the optimal location where ports, airports, and large cities are close by.

③ A demand survey for potential tenant companies must be conducted based on the regional supply chain.

④ It is necessary to pursue active measures to attract investment by dispatching investment attraction groups to neighboring countries.

⑤ Strong incentives such as tax exemptions, tariff exemptions, and low rents should be provided.

⑥ In order to revitalize exports, it is necessary to attract anchor companies.

⑦ It is necessary to upgrade the industry by transferring technology and management know-how from advanced companies.

<Box 2-1> Changwon National Industrial Complex

Construction of the Changwon National Industrial Complex began in February 1974 for the purpose of creating a comprehensive machinery industrial complex under the policy of fostering the heavy and chemical industry, and development was completed in December 2006. As of 2005, the Changwon National Industrial Complex specialized in specific industries, with the machinery industry accounting for 62.1% of the tenant companies. In addition to the machinery industry, the shares of transportation industry and electronics industry are 15.2% and 13.5% respectively, and other industries account for 9.2%, which is mainly composed of the machinery industry.

The Changwon National Industrial Complex and the Masan Free Export Zone are adjacent to each other and have mutually positive influences. In particular, the government strategically established a machinery industrial complex near the Masan Free Export Zone, which was operated mainly for simple assembly production, so that the Masan Free Export Zone could be used as a hinterland city of the Changwon National Industrial Complex. Furthermore, as a planned city, Changwon was built with self-sufficiency in mind.

3.4. Saemangeum Special Zone

3.4.1. Background and Purpose

As the Masan Free Export Zone went through a period of decline, the Korean government became more interested in the continued development and growth of SEZs in Korea. Accordingly, when developing the Saemangeum Special District, great attention was paid to improving the settlement conditions for foreigners. Incentives include schools, hospitals, apartments, and casinos that foreigners can use exclusively.

The Saemangeum development project was a huge undertaking worth more than 22 trillion won. Therefore, there was a limit to covering all costs with government finances, so a development model in which the private sector participated was established. The central government paid 49.1%, the local government 4.3%, and private companies invested the remaining 46.6% to complete the project.

3.4.2. Development Status

The total cost of the Saemangeum reclamation project was 22.2 trillion won, with the central government contributing 10.9 trillion won, the local government 0.95 trillion won, and private companies investing 10.33 trillion won. The project attracted over 8 companies and achieved an investment of 13 trillion won, including foreign companies such as Toray, Solvay, and OCISE, as well as the Chinese CNPV, which installed a solar power generation plant in 2016.

3.4.3. Incentives

Incentives for Saemangeum Special Zone is as follows:

3.4.3.1. Incentives for the Developers

- The state and local governments may reduce or waive the following charges if necessary to support the Saemangeum project: development charges, farmland preservation charges, alternative forest resource creation costs, infrastructure installation costs, shared water surface occupancy and usage fees, rivers occupation fee and usage fee, alternative grassland development fee, traffic generation fee, ecosystem preservation cooperation fee, environment improvement fee, and metropolitan transportation facility fee.
- Grant of subsidies.
- For the smooth implementation of the Saemangeum project, the government may issue subsidies or provide long-term loans to project operators within budgetary limits after review of the application/proposal by the Project Deliberation Committee.
- In order to attract partner companies, the state and local governments may purchase land or construct buildings for use by partner companies.
- The state and local governments can grant private developer's permission to use public facilities, purchase land or facilities necessary for business instead or grant business rights for the development of surrounding areas.
- The head of the Korea Forest Service can revoke the designation of the Saemangeum Business Area as a conservation area if necessary for the efficient development of the Saemangeum Business Area.

3.4.3.2. Incentives for Domestic Companies

- Tenant companies can use state-owned land or buildings in the Saemangeum Business Area for 50 years, and the period can be extended within the range of another 50 years.

3.4.3.3. Incentives for Foreign Companies

- Tenant companies can use state-owned land or buildings in the Saemangeum Business Area for 50 years, and the period can be extended within the range of another 50 years.
- The national and local governments can exempt national taxes, customs duties, and

local taxes for foreign-invested companies moving into the Saemangeum Business Area.

- The state and local governments can support the following expenses for partner companies of foreign-invested companies moving into the Saemangeum Business Area: Land or building purchase costs, rent, construction costs, equipment purchase costs, recruitment subsidy, training subsidy and facility installation costs for electricity, communication, medical care, education, housing.
- In the case of leasing state-owned property, the usage fee or rental fee of the relevant state-owned property can be reduced or exempted.
- The state and local governments may license, lend, or sell public property owned by the state and local governments to companies moving into the Saemangeum Business Area through a private contract.
- The local government can provide employment subsidies within budgetary limits when foreign-invested companies hire people.

3.4.3.4. Incentives for Foreigners

- Special housing supply can be provided to non-homeowner foreigners within the range of 10/100 of the construction volume.
- The state and local governments must provide foreign language services such as publication, receipt, and processing of public documents.
- A foreign educational institution can be established in the Saemangeum Business Area.
- The state and local governments may provide funds or donate land for foreign educational institutions established in the Saemangeum Business Area for purchase of land, construction of facilities, or operation of schools.
- In the case of an international high school located in the Saemangeum Business Area, foreigners can be appointed as teachers.
- The head of an international high school may admit foreigners who are recognized as having an academic background higher than a middle school diploma.
- A foreigner or a corporation established by a foreigner for the purpose of medical business may open a foreign medical institution in the Saemangeum Business Area with permission from the Minister of Health and Welfare.
- Foreigners can open a foreigner-only pharmacy in the Saemangeum Business Area if they register with the Minister of Health and Welfare.

- Foreign doctors, dentists, pharmacists, nurses, and medical technicians can work at foreign medical institutions or foreigners-only pharmacies established in the Saemangeum Business Area if they meet the standards set by the Ministry of Health and Welfare.
- Pharmacists working at foreigner-only pharmacies cannot prepare or sell medicines to Koreans.
- The Minister of Culture, Sports and Tourism may grant permission for a foreigner-only casino business in the Saemangeum Business Area if the person seeking a permit for a casino business intends to make foreign investment.
- A cable broadcasting company that uses the Saemangeum Business Area as its broadcasting area can configure and operate the required number of channels and areas for retransmission of foreign broadcasting.
- The state, local governments, or social welfare corporations can establish and operate a daycare center exclusively for foreign children in the Saemangeum Business Area and the national and local governments can support social welfare corporations.
- Foreign universities can establish and operate foreign university curricula.

3.4.4. Joint Development with Private Companies

The total project cost to build the Saemangeum Special Economic Zone was 22.2 trillion won. Out of this, 10.9 trillion won (49.1%) was invested in state funds, and 10.33 trillion won (46.6%) was invested in the private sector to build a Special Economic Zone. Local governments raised the remaining 0.95 trillion won (4.3%). The project cost was 10.9 trillion won for land creation, 6.6 trillion won for construction of infrastructure, 2.9 trillion won for improvement of water quality, and 1.8 trillion won for others.

The government provided active incentives such as reduction of levies, subsidies, and permission to install sports facilities so that private companies could participate in the development of the Saemangeum Special Economic Zone. However, as the period was extended in the process of reclaiming Saemangeum, the cost exceeded the initial budget. In addition, the project cost increased significantly as additional costs for treating soft ground were incurred. Due to the delay in the construction period and the increase in the sale price due to the rise in project costs, only some of the companies that initially hoped to invest made actual investment. In the development stage of the Saemangeum Special Economic Zone, 81 companies signed MOUs for investment, but less than 10 of them made actual investments. Afterwards, with the completion of the development of the Saemangeum

Special Economic Zone and the active efforts of the Saemangeum Development Office, the SEZ was able to attract investment from 21 companies in 2022.

3.4.5. Establishment of Korea-China Economic Cooperation Complex

The Saemangeum Special Economic Zone was promoted to create a win-win economic environment by combining capital and technology from Korea and China. Korea and China jointly promoted complex creation, corporate attraction, and R&D at the national level within the Saemangeum Special Economic Zone. The level of collaboration between the two countries included cooperation in various fields such as sharing and transferring various technologies, joint marketing, human and material exchanges, and attracting companies.

After sharing the need for joint development of economic cooperation complexes at the Korea-China Economic Ministers' Meeting in December 2013, a plan to promote joint research through the Saemangeum Economic Cooperation Complex was formed at the Korea-China Summit in July 2014. Immediately after the Korea-China summit in October 2015, the Saemangeum Special Economic Zone was confirmed as a Korea-China Industrial Cooperation Complex based on the Korea-China FTA through an MOU.

<Box 2-2> Vietnam Hung-Yen Province Industrial Complex

Korea Housing Corporation is currently preparing to establish an industrial complex in Vietnam that can only accommodate Korean companies. LH, a Korean company, has formed a joint venture with local partners in Vietnam to build a clean industrial complex exclusively for Korean companies in Hung Yen Province, with the aim of supporting domestic companies entering Vietnam. The project has received support from the governments of both countries, and LH will supply land of various sizes to companies that apply. The first 12 lots of industrial land were supplied in March, and an additional 19 lots of 240,000 square meters are on offer at a supply price between $102 and $113 per square meter with a lease period until July 5, 2071.

Vietnam is an example of a case where a Korean public agency such as LH took on the role of a developer and collaborated with foreign governments to establish industrial parks. The reason why this was possible in Vietnam was due to the presence of anchor companies such as Samsung Electronics. Many small and medium-sized enterprises in Korea also sought to expand into Vietnam, and public agencies provided active support for them in the process.

3.4.6. Development of RE100 Industrial Complex

By introducing a floating solar power generation project in Saemangeum, Korea is promoting the creation of an industrial complex that uses 100% of the large-scale renewable energy produced thereby. In April 2021, the Saemangeum Administration signed a "Business Agreement to Attract Renewable Energy, and Saemangeum Investment" with SK E&S, and agreed to develop a 200MW water solar business, establish a start-up cluster and data center, and promote the Saemangeum Green Industrial Complex based on RE100 and

green hydrogen. SK E&S proposed a specific blueprint to attract about 2.1 trillion won in investment to build start-up clusters and data centers and foster Saemangeum as a representative carbon-neutral innovative city in Korea. Since it is not efficient to install only renewable energy sources such as solar power, construction of a transmission line to link the power grid is also underway and is scheduled to be completed by the end of 2024.

In July 2022, the Ministry of Land, Infrastructure and Transport and the Saemangeum Development Office announced that the Saemangeum National Industrial Complex' had been designated as the country's first 'Smart Green National Pilot Industrial Complex'. 'Smart Green Industrial Complex' is a project to create a new future-oriented industrial complex, with focus on minimizing energy use, expanding the supply of renewable energy, establishing infrastructure to support corporate production, and providing pleasant living conditions. To this end, the Industrial Complex promotes digitalization of tenant companies and facilities, focuses on energy self-sufficiency and eco-friendliness, and requires a reduction of 25% or more of greenhouse gas emissions. Ultimately, the RE100 industrial complex will be realized by 2040, and 100% of the energy used in the industrial complex will be supplied and consumed as renewable energy. To achieve the goal, a total of 180MW solar power generation facilities including parking lots and building rooftops will be created in the short term by 2029, and the realization of RE100 by utilizing floating solar power and fuel cell power generation will be supported in the long term by 2040.

<Box 2-3> Korea's First RE100 National Industrial Complex

RE100 is a private voluntary campaign to convert 100% of the power used by companies into renewable energy by 2050. Companies wishing to join should publicly declare their commitment to use 100% renewable energy electricity, and establish plans and clear strategies for procuring more than 60% of renewable energy by 2030, more than 90% by 2040, and finally 100% of renewable energy by 2050.

Samsung Electronics is pursuing a "New Environmental Management Strategy" that includes the development of ultra-low power semiconductors and products, and the recycling of semiconductor water to achieve carbon neutrality by 2050. In the case of overseas businesses, Vietnam and Southwest Asia aim to adopt renewable energy within five years starting 2022; Latin America by 2025; and Southeast Asia, Independent State Association (CIS), and Africa by 2027. Hyundai Motor Group is also pushing to achieve its carbon neutral goals by establishing an eco-friendly smart factory for efficient production, including the use of 100% renewable energy, pursuing electrification of vehicles, and inducing and supporting carbon neutrality in the parts supply chain.

As major Korean conglomerates declared their commitment and continue to push for RE100, small and medium-sized companies that supply parts to them have also emerged as a challenge facing RE100. Since SMEs cannot produce renewable energy on their own, they have no choice but to purchase it through carbon emission trading. In response, Dangjin City is pushing to build the RE100 National Industrial Complex for the first time in Korea.

Dangjin City has established a plan to create an industrial complex with a total area of about 500,000 square meters, with industrial facilities occupying 39.3 million square meters (78%), support facilities 0.54 square meters (1%) and public facilities 10.4 square meters (21%). The total cost for the project is about 130 billion won, which is being promoted to attract companies that can lead the sustainable future development of Dangjin City by minimizing the sale price.

<Box 2-3> Continued

The tenant industries include electric/gas/steam and air conditioning supply, manufacturing of electric equipment, and automobile/trailer parts manufacturing. The industrial complex will be in charge of producing renewable energy, and will create the first RE100 industrial complex in Korea. After the announcement, the Industrial Complex move-in proposal was sent to the top 100 domestic conglomerates and the infrastructure construction work was discussed with GS Engineering & Construction and LG Chem.

Dangjin City signed a mutual cooperation MOU between GS Engineering & Construction in September 2020 to establish power supply infrastructure for the RE100 Industrial Complex, submitted a feasibility study to the Ministry of Public Administration and Security in January 2022, and carried out a central investment review and a feasibility review of SPC corporation's investment.

The creation of the RE100 Industrial Complex will help achieve 1.5419 trillion won in production, 771.1 billion won in value-added, and 2,874 new jobs. Companies in the RE100 Industrial Complex will be able to use renewable energy such as green premiums, new energy supply certificates (RECs), and third-party PPA.

3.4.7. Implications and Policy Suggestions

The Saemangeum Special Economic Zone presents various implications for the Peruvian Special Economic Zone. First, Saemangeum provides various types of incentives to various subjects. It also includes active measures such as support from local governments. Separate incentives are provided not only to foreign companies moving into the Saemangeum Special Economic Zone but also to project implementers for the development of the Special Economic Zone. In addition, special benefits are provided to foreigners living in the Special Economic Zone, such as housing supply, establishment of foreign educational institutions, establishment of foreign medical institutions, transmission of foreign broadcasts, and establishment of foreigner-only casinos. In the Peruvian Special Economic Zone, various types of similar incentives are required for various entities.

Second, Saemangeum was jointly developed by the public and the private sector, but due to the delay in the schedule, tenant companies were not able to attract investments smoothly. Private companies were unable to promote investment smoothly due to the delay in the development schedule of the Saemangeum Special Economic Zone and the increase in development costs. In Peru, when developing Special Economic Zones, public-led construction can be considered as a way to reduce risks rather than joint development with the private sector.

Third, Korea wanted to create a model for economic cooperation with neighboring China in the Saemangeum Special Economic Zone. In addition to attracting tenant companies, various areas of economic cooperation were promoted, such as joint development and marketing of special economic zones, joint R&D, and human and material exchanges for tenant companies. Peru's Special Economic Zones can also consider joint investment and

development of Special Economic Zones through cooperation with neighboring countries.

Fourth, the Saemangeum Special Economic Zone has recently been promoting the creation of a RE100 complex through solar power generation. Carbon footprints are becoming a very important change factor worldwide, which has an inevitable impact on Special Economic Zones. Peru will also need to come up with alternatives such as the creation of RE100 industrial elements in order to take the lead in responding to future global economic changes.

3.5. Implications

The Masan Free Export Zone was designated based on its favorable accessibility to Japan, and its subsequent success in creating an export-driven industrial complex was made possible through the utilization of Japan's regional value chain. Similarly, as economic zones are established along the coastal areas of Peru, it is imperative to identify products that can be exported by leveraging the regional value chain of neighboring countries, much like in the case of Masan.

Masan Free Export Zone gained great popularity from the beginning due to the export strategy that utilized Masan's geographical advantages and the government's strong support. There were so many applications from companies that wanted to move in that the government had to strictly control the number of companies moving in. In the first year of its launch, 4 companies moved in, followed by 70 companies after 2 years and 115 companies after 3 years. In other words, for the vitalization of SEZs, the initial move-in of domestic companies is very important and acts as a decisive factor determining the success of SEZs.

The Saemangeum Special Economic Zone invested a total of 22.2 trillion won in development costs to create land, build infrastructure, and improve water quality. Of the total project cost, 10.9 trillion won (49.1%) was procured from the central government, and 10.3 trillion won (46.4%) from the private sector and 0.95 trillion won (0.5%) from the local government. The Saemangeum Special Economic Zone was a case in which the central government and the private sector jointly built a Special Economic Zone, but as a result of joint public-private participation, the construction of infrastructure such as ports was delayed, resulting in increased costs and cancellation of move-in by companies, which caused considerable difficulties. Through the Saemangeum Special Economic Zone, the Korean government tried to create a model for developing a Special Economic Zone with the participation of the public and private sectors, but in the end, it did not achieve good

results. Therefore, it is not desirable to rely on private capital for the development of Special Economic Zones, which entails large-scale investment and may delay the construction period.

In conclusion, the case study suggests three implications from the development of Korea's Special Economic Zones: 1) the need for a corporate attraction strategy at the level of central and local governments to strengthen existing industries; 2) the use of attractive incentives, considering the neighboring countries' regional value chain, to attract businesses; and 3) the need for a national-level strategy to attract anchor companies to create a strategic industry or future growth industry. These three implications serve as the preliminary basis for presenting the strategic plan.

4. Policy Proposal and FDI Attraction Strategies for Peru's SEZ

4.1. Review of OECD Recommendation Criteria

The OECD adopted the Recommendation on Foreign Direct Investment (FDI) Quality for Sustainable Development at its Council of Ministers in June 2022. The OECD recommendation consists of five items, including governance, with focus on major policy principles/directions. The five items are: governance; domestic policies and legal frameworks; financial and technical assistance; information and facilitation services; and development cooperation.

Since the early 2000s, the OECD has defined tax systems of each country that can lead to undesirable tax competition in the world economy as harmful tax systems. The Peruvian Special Economic Zones should also be developed within the scope where the tax reduction policy for attracting regional headquarters of multinational companies or Foreign Direct Investment does not fall under harmful tax competition as defined by the OECD. After the midterm report, it is planned to closely analyze the OECD recommendations and standards to establish an FDI attraction strategy that includes support for business activities and tax support for companies residing in existing Special Economic Zones.

In order to enhance the competitiveness of the Peruvian economy and promote industrial development, it is imperative to attract foreign-invested companies to Special Economic Zones. To ensure the expansion of positive results, it is advisable for domestic companies with high relevance to foreign-invested companies to move in.

The move-in of domestic companies can lead to a dissemination of advanced technologies and management techniques through exchanges with foreign-invested companies. Even without a direct transactional relationship, the transfer of transparent corporate management culture and cooperative labor practices can be highly advantageous.

Furthermore, domestic companies can leverage the overseas sales networks of foreign-invested companies located in Special Economic Zones to develop new overseas markets or increase exports. Additionally, the creation of forward and backward related effects, such as the purchase of domestic raw materials and the processing of subsidiary materials and parts in neighboring regions, can amplify the positive impact.

Therefore, incentivizing domestic companies to move into Special Economic Zones is crucial. Encouraging foreign-invested companies to share business opportunities with domestic companies and enter into mutually beneficial business relationships can contribute significantly to strengthening the technological and management competitiveness of domestic companies.

4.2. Incentive Programs for Tenant Companies and Public-side Developers

If an industry lacks competitiveness or if domestic companies have low production efficiency, actively accepting foreign investment is essential to compensate for these weaknesses. The case of Masan in Korea illustrates that the potential for increasing productivity and competitiveness in the domestic industry increases when foreign investment is introduced along with leveraging low labor costs and active production and export support from the country and capitalizing on the value chains of neighboring countries such as Japan.

Peru recognizes the importance of regional value chains and has made efforts to integrate into them. The country has developed a national export plan that identifies key sectors and products for export and aims to increase the competitiveness of these sectors in regional and global markets. Peru has also established trade agreements with its neighboring countries, and participates in regional integration initiatives such as the Pacific Alliance. These efforts have helped to promote greater economic cooperation and integration in the region, which has led to increased trade and investment flows between Peru and other countries in Latin America. Overall, Peru sees regional value chains as a key driver of economic growth, and is committed to further integrating into them to enhance national competitiveness and expand its opportunities for trade and investment in the region.

4.3. Strategies for Attracting Anchor Companies

The anchor function refers to the role played by core companies, such as large companies in a specific field, that act as an anchor for other businesses in the early stages of development. When foreign-invested companies decide to move into a Special Economic Zone, they consider the possibility of business success and investment risks, and the presence of domestic conglomerates can encourage them to move in. Furthermore, foreign-invested companies try to create business opportunities and secure markets through exchanges with related companies and formation of production networks, which can also attract more foreign investment.

Foreign-invested companies in Special Economic Zones tend to seek out transactions, exchanges, and networks with related companies to reduce various risks and improve investment performance. The move-in of an anchor company into the Special Economic Zone in its early stages can help reduce risks, promote foreign investment, and serve as an anchor that contributes to the early settlement of foreign-invested companies.

5. Implications and Policy Recommendations

5.1. Major Implications

In order to attract foreign investment for economic zones, it is imperative that domestic enterprises first establish a solid presence within said zones. Subsequently, a strategic decision-making process must be employed to identify the industries and products that Peru can leverage for export by analyzing the value chains of neighboring countries. Finally, the attraction of anchor companies is essential. The successful attraction of anchor companies necessitates the fulfillment of all conditions that are required by the companies, which in turn requires the implementation of public-led development. Since private companies may make short-term decisions that prioritize profit, it is crucial to pursue development initiatives that can support businesses in the long-term, even if it means accepting immediate losses through public-led development.

5.2. Policy Recommendations

5.2.1. Establishment of an Incentive System According to Economic Conditions

Ideally, the incentive system for Foreign Direct Investment should be structured

differently based on economic conditions such as the stage of development. During the early stage of development, where investment resources and industrial bases are relatively weak, the goal is to vitalize investment and promote employment by attracting foreign capital. In this case, an incentive system is established to support omnidirectional tax reduction for foreign-invested companies across industries. Conversely, during the late stage of development, the focus is on cash grants and financial support incentives to attract investment in specific strategic industries such as high-tech sectors.

5.2.2. Contribute to the Vitalization of Special Economic Zones

To promote investment in special economic zones and strengthen the Peruvian economy, equal support should be provided to domestic companies, alongside foreign-invested companies, in order to prevent foreign investment from overshadowing domestic investment. Providing discriminatory tax support solely to foreign-invested companies could result in domestic investment being substituted, leading to outflows of domestic and overseas relocation of domestic businesses.

Moreover, encouraging domestic companies to undertake high-tech projects through incentives will contribute to improving their technological capabilities. Given the large size of Special Economic Zones, relying solely on foreign-invested companies to activate economic performance is impractical. Therefore, it would be beneficial for the country to revise its foreign investment-oriented policy goal and promote the attraction of domestic companies to Special Economic Zones. This is because relying solely on foreign-invested companies may lead to some locations being deemed undesirable by foreign investors, making it imperative to encourage domestic companies to move in as well.

5.2.3. Establishment of an Export Expansion Strategy through the Creation of RE100 Industrial Complex

Issues at the global level, such as climate change and global food security, which are difficult to address at the individual national level, are emerging as tasks. It is necessary to designate and operate a pilot zone for renewable energy generation in Peru's Special Economic Zones for industries such as mining, which have uniquely Peruvian advantages in global value chains. Financial resources for the creation of renewable energy generation in the pilot zone may be prepared in connection with international development cooperation funds. Development finance is a concept that encompasses various methods of financial support in the public sector related to development in developing countries. In terms of financing, it can expand the financial base by utilizing not only government finances

but also self-financing resources from external partners such as market lending entities. Through this, Peru can increase its chances to export to advanced North American markets (companies participating in RE100) such as the United States.

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03

CHAPTER

Selection Criteria for Peruvian SEZs and Improvement of the Governance System

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1. Introduction
2. Status of SEZs in Peru
3. Selection Criteria for Existing SEZs in Peru
4. Governance System of the SEZs in Peru
5. Lessons from Korean Experience
6. Development of New Selection Criteria and Governance System
7. Conclusion and Policy Recommendations

Keywords
Special Economic Zone, Governance, Ombudsman, Analytical Hierarchy Process, Importance Performance Analysis

Selection Criteria for Peruvian SEZs and Improvement of the Governance System

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Summary

In Chapter 3, the KSP team investigates "Selection Criteria for Peruvian SEZs and Improvement of the Governance System" to provide the Peruvian government with useful policy suggestions and hands-on recommendations they can utilize when designating new SEZs or considering measures to make existing SEZs more sustainable. In order to come up with viable suggestions, the KSP team evaluated SEZ selection criteria in Peru using the AHP/IPA method and examined ways to improve Peru's SEZ governance system in light of the experiences of Korea and other countries worth benchmarking.

According to the results of AHP/IPA survey from the Peruvian government officials, SEZ experts, and the CEOs of tenant companies, the Peruvian government officials and the SEZ experts recognized policy feasibility, especially policy imperatives, as the most important criteria for selecting SEZs, but most of the SEZs in Peru do not meet these criteria. Therefore, rather than designating SEZs in a hurry to achieve policy goals such as balanced regional development, policymakers in charge of SEZs need to select and designate special zones in consideration of technological feasibility factors such as operational efficiency and location/infrastructure, economic feasibility factors such as performance and enforceability of special zones, and the needs of (prospective) tenant companies.

Thus, in conclusion, the following policy recommendations are suggested from a governance perspective.

① **Streamline the legal framework for SEZs:** Instead of designating SEZs based on individual laws, the Peruvian government may consider enacting the "Special Law on the Designation and Operation of Special Economic Zones of Peru" (tentative title). This law would consolidate relevant laws and regulations, streamline administrative

procedures, and minimize bureaucratic obstacles.

② **Establish transparent criteria for selection, performance evaluation, and cancellation or exit:** The selection criteria for SEZs should consider political feasibility (policy compliance and governance), technological feasibility (operational efficiency, location/infrastructure), and economic feasibility (performance, capacity for project implementation), and need to be explicitly incorporated into laws and regulations. Additionally, a framework for monitoring and evaluating performance should be established to assess the impact of SEZs on investment, exports, employment, economic growth, and regional development. Furthermore, clear criteria and procedures should be developed for the cancellation of SEZ designation or the exit of tenants.

③ **Enhance Coordination and Institutional Capacity:** Improve coordination among government agencies responsible for SEZ administration to ensure consistent implementation of policies and regulations. Strengthen the institutional capacity of these agencies to effectively manage SEZs, including sufficient resources, expertise, and efficient decision-making processes.

④ **Compliance with global standards and enhancement of environmental sustainability:** Considering global standards, it is essential to incorporate environmental considerations into the governance system of SEZs. This includes implementing stringent environmental regulations, conducting environmental impact assessments, and attracting environmentally friendly companies to the SEZs to promote ESG (Environmental, Social, and Governance) management.

⑤ **Beyond the Knowledge Sharing Programs:** As Korea and Peru celebrate the 60th anniversary of diplomatic relations in 2023, it is crucial for both counties to identify opportunities for bilateral and multilateral international development cooperation projects. Furthermore, beyond the KSP, proactive measures should be taken to promote mutually beneficial economic cooperation, including joint efforts to attract Korean companies to Peru's SEZs and facilitate their expansion in overseas markets.

It is expected that implementing these policy recommendations will improve governance systems in Peru's SEZs, leading to increased investment, economic development, job creation and sustainable growth.

1. Introduction

The Special Economic Zones (SEZs) in Peru are designated areas established to attract private investment and promote productive activities and services, with an emphasis on foreign trade businesses and connection to global value chains. By providing special and flexible tax and customs regulations, the Peruvian government aims to improve the region's economic prosperity, reduce logistical barriers, stimulate the economy, bring down unemployment, and promote the expansion of infrastructure and new technologies. Currently, there are eight SEZs in Peru, but only four are operational: ZOFRA (Zona Franca) Tacna, ZED (Zonas Especiale de Desarrollo) Paita, ZED Ilo, and ZED Matarani. However, analysts in Peru generally agree that the SEZs have not been successful.

In this chapter, the KSP team evaluates the existing criteria for selection of SEZs in Peru using the AHP/IPA method, which is widely used in complex multi-attribute decision-making. They explore potential problems with Peruvian SEZs and provide recommendations based on the experiences of Korea and other selective countries to improve the governance of SEZs in Peru, modify laws and regulations to encourage Foreign Direct Investment (FDI) and increased exports, and promote economic cooperation between Korea and Peru. This final report concludes by offering policy implications and suggestions for promoting more successful and sustainable operation of SEZs and fostering economic cooperation between Korea and Peru.

2. Status of SEZs in Peru

2.1. Operations of the SEZs in Peru

Currently, there are four operational Special Economic Zones (SEZs) in Peru, three of which have been formally designated as Special Development Zones (SDZs) since 2016. These SDZs are located in Ilo, Paita, and Matarani, while the fourth SEZ is the Tacna Free Trade Zone (FTZ). Additionally, four SEZs are not currently in operation: the SDZs Loreto, Tumbes; SEZ in Puno; and the FTZ in Cajamarca, as shown in <Table 3-1>. Enterprises that establish themselves in SEZs benefit from a special customs and tax regime for a specific period, which is until 2042 for SDZs and until 2032 or 2049 for the Tacna FTZ, depending on how the law is interpreted.

<Table 3-1> SEZs in Peru

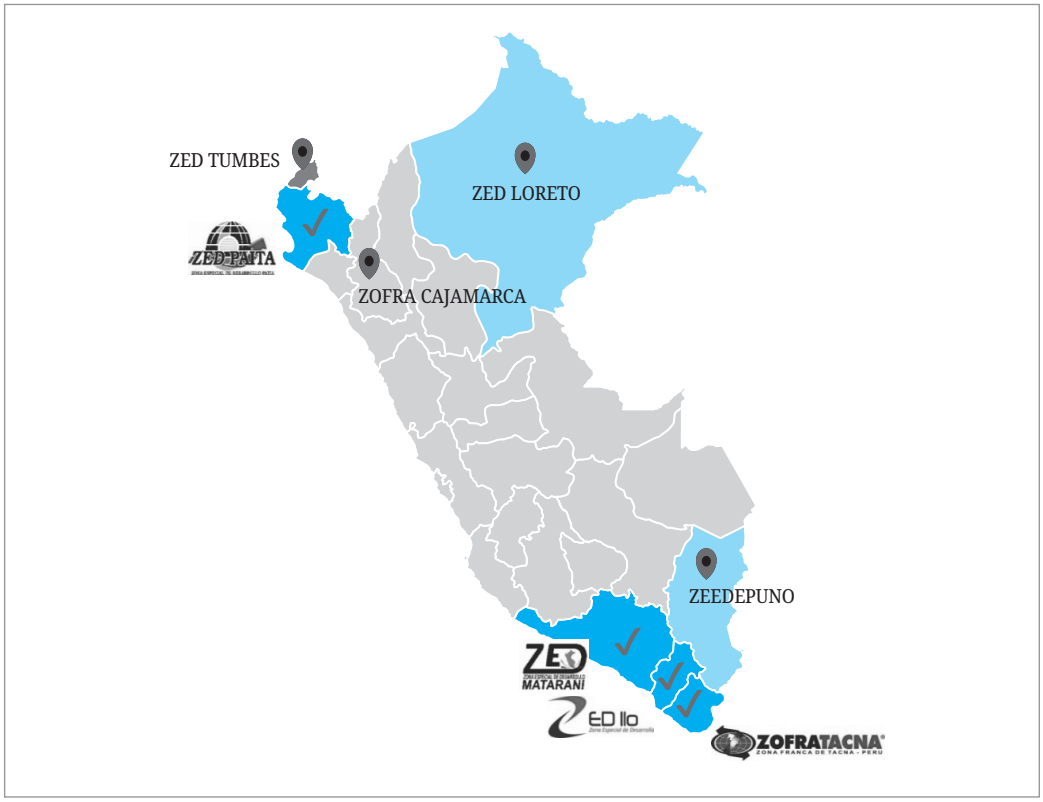
Location	Function	Year Created	Status	Decree or Law
Tacna	FTZ	1990/2002	In operation	Law 27688
Paita	SDZ	1996	In operation	DL No. 864
Ilo	SDZ	1996	In operation	DL No. 842
Matarani	SDZ	1996	In operation	DL No. 842
Puno	SEZ	2006	No operation	Law 28864
Tumbes	SDZ	2011	No operation	Law 29704
Loreto	SDZ	2013	No operation	Law 26953
Cajamarca	FTZ	2021	No operation	Law 31343

Source: MINCETUR (2022).

SEZs have been present in Peru since 1989 and have undergone several regulatory changes since then. The primary objective of these zones is to promote regional development, generate employment opportunities in disadvantaged areas, and contribute to the modernization of the ports near which they are situated. The procedures and requirements for accessing SEZs are similar across all regimes, whether in a SDZ or a FTZ. National or foreign individuals or entities that enter into an onerous use assignment contract for the land in SEZs or exercise the purchase option for such land are eligible to avail the regime. A public bid process is required for user qualification in both cases. The SEZs are managed by a committee or management board that is attached to the regional government. Recently, private administration of SEZs has also been allowed.

SDZs and FTZs can host any kind of business, and there is no selective industrial policy intent in the designation of SEZ. Any manufacturing activities can be undertaken, including maquila and assembly, services, logistics, and trade, except prohibited activities such as the sale of weapons and narcotics and activities on a short negative list connected with the manufacturing of oil and flour. There is no minimum investment requirement in Peru to become a SEZ tenant. Unlike some other countries, Peru does not require a minimum investment to access SEZ benefits. Additionally, there is no minimum requirement for hiring staff, such as in Colombia's and Costa Rica's FTZs. However, the MEF is considering a plan to introduce a minimum investment amount, which would be a positive development.

[Figure 3-1] Special Economic Zones in Peru



Source: MINCETUR (2022).

2.2. Performance Analysis of the SEZs in Peru

<Table 3-2> SEZ Investment, Exports, and Imports (2022)

SEZ	Number of Companies Installed	Companies Operating	Investment Committed[1)]	Exports	Imports to the RNT[2)]	Direct Employment
			Millions of USD			
Tacna	90	41.	31.1	4.0	71.4	1,057
Paita	41	26	136.8	80.6	66.2	1.034
Matarani	20	16	17.4	9.3	19.5	180
Ilo	16	10	0.8	0.0	57.7.	71
Total	167	93	186.1	93.9	214.9	2,342

Note: 1) Represents the amount of accumulated investment commitment at the end of 2022.
2) Includes the operations from the SEZ to the Rest of the National Territory by the nationalization of goods.

Source: MINCETUR (2022).

According to the data provided by Peru's Ministry of Foreign Trade and Tourism (Ministerio de Comercio Exterior y Turismo: MINCETUR), the major economic performances of four Peruvian SEZs have fallen far short of expectations. As of 2022, only 93 companies are actually operating in these four SEZs, and the investment amount is 186.1 million USD, with exports of 93.9 million USD and imports of 214.9 million USD. Direct employment also remains at the 2,300 level. This is a very small fraction of Peru's total economic activity.

Even in the case of major export markets, except for Paita and Matarani, they are concentrated mainly in the nearby Central and South American markets. Hence, it is necessary to diversify more to include countries or regions that have signed FTAs with Peru.

In the case of Peruvian SEZs, even in the special zones currently in operation, there is a slump in indicators such as foreign investment attraction, import and export, and employment because the SEZs do not have a long-term master plan, clear performance goals for each indicator, or performance evaluation system.

<Table 3-3> Main Markets of Operational SEZs in Peru

SEZ	Major Markets
ZED Paita	Ecuador, Colombia, Japan, United States, Netherlands, Canada, Spain, Bolivia, and South Korea
ZED Matarani	China, Bolivia, United States, Germany, Ecuador, and New Zealand
ZED Ilo	Rest of the National Territory
ZOFRATACNA	Chile, Colombia, Bolivia, Puerto Rico, and Dominican Republic

Source: MINCETUR (2022).

2.3. Problems of the SEZs in Peru

Apparently, the SEZs in Peru have been largely unsuccessful in expanding economic activity and creating jobs, and there is a lack of consensus among analysts regarding the causes of these disappointing results. However, there are two central governance problems identified in the management of the SEZs: a vague legal framework and mismanagement from regional governments.

The first issue arises because different government agencies are responsible for different aspects of the SEZs, which can lead to confusion and inefficiencies. The Ministry of Foreign Trade and Tourism (MINCETUR) sets the public policy for SEZs, the Ministry of Finance regulates the customs tax benefits, and the Ministry of Production authorizes new permitted activities. This fragmented system can make it difficult for businesses to understand and comply with the requirements.

The second issue is related to the management of the SEZs by regional governments, which have been criticized for appointing ineffective managers who are not able to attract investment or create jobs. There are legal obstacles to delegating the management of SEZs to private operators, and the MINCETUR has been reluctant to take away the administration of the SEZs from regional governments, which has further contributed to mismanagement.

Overall, the SEZs in Peru seem to be facing significant governance challenges that need to be addressed to make them more attractive to investors and more effective in promoting economic development in disadvantaged areas.

3. Selection Criteria for Existing SEZs in Peru

The Constitution of Peru only requires approval from two-thirds of Congress to create a Special Economic Zone (SEZ), without imposing any additional requirements or criteria. However, in practice, the establishment of SEZs usually involves other legal, regulatory, and administrative procedures, such as the approval of specific laws, regulations, and decrees, as well as the identification of suitable locations, preparation of infrastructure and services, and the selection of eligible users.

3.1. Main Considerations for the Development and Designation of SEZs

There are no clear economic criteria for the creation of SEZs in Peru; it has always been a political decision. The rationale is to create a development hub in the geographical area where the SEZ is located. The first SEZ to be established was ZOFRATACNA, which was intended to reduce smuggling along the southern border. Subsequently, the ZED Ilo, Matarani, and Paita were created to foster industrial hubs near the port. The ZEE (Zona Economicas Especiales) Puno was established in response to social demands from that region. The ZED Tumbes was created because the rulers at the time were originally from those regions.

The MINCETUR has developed a report outlining the minimum requirements or objectives that should be met to approve a SEZ, but political leaders often disregard it.

3.2. Legislative Foundations of SEZ Selection Criteria

The fundamentals of the rules always mention that tax exemption is the most attractive factor for companies to settle. The rules for creation of each zone express the decision to generate economic development in the zone of influence of the SEZ as follows:

- The development of the southern zone of the country was declared a priority interest and centers of export, transformation, industry, commercialization, and services are being created (ZED Ilo, Matarani, Paita).

- Generate a development pole along the northern border (ZED Tumbes).

- The development of the Tacna Free Trade Zone – ZOFRATACNA – was declared as a project of national significance for carrying out industrial, agro-industrial, maquila, and service activities in the Tacna Commercial Zone, to promote the sustainable socioeconomic development of the Department of Tacna, through investment and technological development (ZOFRATACNA).

- The Special Economic Zone of Puno – ZEEDEPUNO was declared as a project of national interest to carry out industrial, agro-industrial, maquila, and service activities and thereby contribute to the sustainable socioeconomic development of the Department of Puno, through the promotion of investment and technological development (ZEEDEPUNO).

- Contribute to the sustainable socioeconomic development of the Peruvian Northeast region, through the promotion of investment and technological development (ZOFRA Cajamarca).

<Box 3-1> ZOFRA CAJAMARCA

The regional government of Cajamarca and the company Huawei signed a cooperation agreement to promote the digital transformation of the region in industrial sectors such as agriculture and improve access to basic services such as health and education.

It is estimated that the agreement will benefit more than 100,000 citizens of the region, and aims to provide technical assistance for digital transformation through technologies such as AI, IoT, Cloud, and 5G. Further, the agreement has plans to promote acquisition of digital talent through international training courses and certification systems; and support the development of the Center for Productive Innovation and Technology Transfer - CITE Digital Cajamarca.

Currently, this cooperation project does not aim to influence the implementation of the Cajamarca Free Trade Zone.

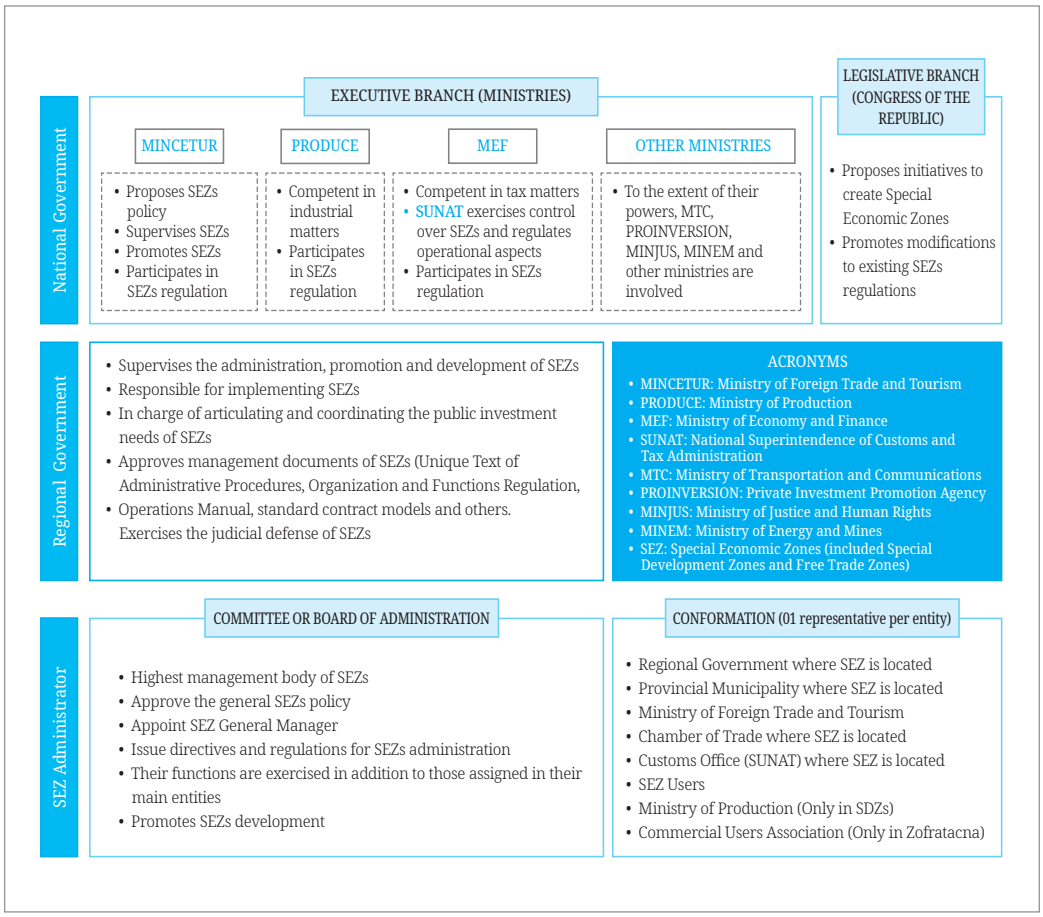
Source: Official websites of the Regional Government of Cajamarca and Huawei (https://www.huawei.com/mx/news/mx/2021/ gobierno-regional-de-cajamarca-y-huawei-firman-acuerdo-de%20cooperacion-por-la-transformacion-digital, accessed on July 5 2023).

4. Governance System of the SEZs in Peru

4.1. Governance Structure of the Peruvian SEZs

4.1.1. Governance Scheme of Peruvian SEZs

[Figure 3-2] Governance Structure of Peruvian SEZs



Source: MINCETUR (2022).

Similar to Korea and other countries that operate special economic zones, the designation and management of Peru's special economic zones involves many government agencies including MINCETUR (Ministerio de Comercio Exterior y Turismo - Ministry of Foreign Trade and Tourism), PRODUCE (Ministerio de la Produccion- Ministry of Production), and MEF (Ministerio de Economia y Finanzas - Ministry of Economy and Finance) at the central government level, as shown in [Figure 3-2]. Local governments also carry out many tasks related to the management, promotion, and supervision of the development of special zones,

as well as the actual operation of special zones. In addition, the SEZ committee or board of administration, which is composed of central and local government officials, serves as the de facto highest management body of SEZs.

Specific roles of the government agencies related to the SEZs are summarized in <Table 3-4>.

<Table 3-4> Specific Roles of the Government Agencies Related to the SEZs

Name	Specific roles
MINCETUR (Ministry of Foreign Trade and Tourism)	• Governing entity of the SEZs in Peru • Plans, formulates, directs, coordinates, executes, supervises, and evaluates national and sectoral policies for the development of activities in the SEZs. Proposes, coordinates, approves, and evaluates the regulations related to SEZs
MEF (Ministry of Economy and Finance)	• Formulates, proposes, executes, and evaluates the guidelines and measures regarding the tariff and tax policy • Carries out customs controls on the entry and exit of goods from the SEZ
PRODUCE (Ministry of Production)	• Competent authority in matters of industry, domestic trade, promotion, and development of micro, small and medium-sized enterprises • Proposes a list of allowed activities
PROINVERSIÓN (Agencia de Promoción de la Inversión Privada - Investment Promotion Agency)	• Promotes foreign direct investment in SEZs • In charge of the selection process of the private operator of ZOFRATACNA
SUNAT (Superintendencia Nacional de Aduanas y de Administración Tributaria - National Superintendency of Customs and Tax Administration)	• Responsible for enforcing customs regulations and collecting taxes • Monitoring and verifying compliance with customs and tax benefits granted to companies in SEZs
GORE (Gobierno Regional - Local governments)	• Plans and promotes the development of the SEZs. • Approves, evaluates and supervises the execution of the Strategic Promotion Plan, as well as the programs and projects that promote the development of the SEZs • Appoints the Administration Committee • Supervises the management of the SEZs

Source: MINCETUR and the KSP team.

4.1.2. Management Committee of each SEZ

The administration of each SEZ is carried out by a Committee or Board of Administration, which is attached to the regional government and has administrative, economic, and financial autonomy. This Board is composed of representatives from various public and private entities, including GORE (Regional Government), MINCETUR, SUNAT, the municipality, users, and the relevant port.

They are special decentralized entities that have the following characteristics:

- They enjoy autonomy in their creation of the applicable special regulations.
- They have an organizational identity.
- Their organization is formalized in an Operations Manual that is approved by the entity under whose scope it is located.
- Their organizational design is governed by the principles and criteria concerning organizational matters.
- They are subject to the supervision of the entity under whose scope they are located, without this supervision affecting their autonomy.

4.2. Legislations and Policies Related to SEZs

4.2.1. SEZ-Related Laws and Regulations

The legal framework for SEZs in Peru is aimed at promoting private investment and economic development in specific regions and sectors, to generate jobs, increase exports, and promote technological innovation. In general, Peru's Special Economic Zones have a legal system related to special zones in the form of Laws approved by Congress, Supreme Decrees promulgated by the President, and General Procedures of related government agencies. For the specific legal framework regarding the designation and operation of special zones, see Appendix 1.

4.2.2. Functions of the Central and Regional Governments in the Private Sector Participation Process

The MINCETUR, among its objectives related to foreign trade (Numeral 5, Article 4, Law No. 27790), stipulated the promotion of activities in Free Trade Zones, Special Commercial Treatment, and Special Development Zones to increase exports. This is consistent with the supervisory functions that the MINCETUR must carry out on the private operator of the Tacna Free Trade Zone and the commercialization zones assigned by articles 32 and 34 of Law No. 27668.

For the ZED (and also for the ZOFRATACNA), it's the second article of Law No. 29014 that assigns the central government the supervision and regulation of said zones, specifying in Article 5 of Law No. 30777 that the private operators of the ZED will be authorized and supervised by the MINCETUR.

As can be seen, the rules applicable to the ZED establish not only the supervision but also the authorization of the private operator, unlike the rules applicable to the Tacna free Zone. It is worth mentioning that the aforementioned regulations do not have any stipulations regarding the supervision or authorization of operators for the extension zones (which have a customs and tax regime for the SDZ area).

Law No. 29014, in the second article, makes it clear that the "regional governments will be in charge, in accordance with the regulations applicable to their management, of supervising the administration, promotion, and development of the organizations referred to in the first paragraph, in their respective territorial areas. The first paragraph of the aforementioned article of Law No. 29014 does not mention any boards or administration committees, but rather the Special Economic Zones themselves. In other words, the regional government does not supervise the board or committee, but rather the Special Economic Zone directly, regardless of whether the administrator is a public or private operator. Therefore, it could be understood that each regional government shares the functions of supervision, promotion, and development of economic zones in their jurisdiction with the MINCETUR.

Regarding the process of the project to promote investments in the special economic zones, Law No. 30976, in its final dispositions, indicates that the call on granting concessions on the design, financing, execution, and operation of the industrial infrastructure and services of the free zone and the commercial zone of Tacna is to be taken by the private investment promotion agency - PROINVERSIÓN (Fourth Complementary Disp. Final).

While the promotion of investment in ZOFRATACNA is carried out by PRODUCE, MINCETUR, PROMPERÚ, and PROINVERSIÓN (Fifth Final Complementary Disp.), this is a singular norm that is not repeated for the other economic zones, and the participation of PROINVERSIÓN is applicable only in a single private investment model (Boot Concession).

Article 6 of Legislative Decree No. 1362 authorizes regional governments to be owners of investment projects through the modality of public-private associations, but this does not mean that the corresponding regional government can initiate a process of private investment in their respective Special Economic Zone because they do not have ownership or control of the assets that would be the object of the concession.

If the geographical areas are registered in favor of each regional government, and there is a mandate to deliver the zone to the private sector, the economic and technical conditions must be established for said delivery, so that users, the government, and the investor obtain

favorable results. This evaluation should include whether the promotion process would be carried out independently or jointly with other regional governments, as permitted by Legislative Decree No. 1362. It is to be noted that regional governments do not have the mandate to lead or operate the zones, and the committees or boards only carry out this task as long as there is no private operator. Therefore, in legal terms, it is understood that there is an implicit mandate to grant a concession, and its conditions must be determined.

4.2.3. Public Policy Instruments Related to SEZs

The National Export Plan of Peru is a multisectoral instrument to promote exports from Peru. The current plan has been in force since 2013. It has four pillars, Pillar 3 being the trade facilitation pillar. This is where the public policies for SEZs have their origin.

PILLAR 3: Facilitation of Foreign Trade and Efficiency of the International Logistics Chain

Line of Action 3.1 Logistics and International Transport

- Improvement and promotion of regimes that facilitate foreign trade
- Strengthening of the regime of Special Economic Zones through the unification of the relevant regulatory framework and promotion of private investment
- Promotion of the development of the existing Special Economic Zones as centers of logistics, distribution, and production of goods and services with high added value

For its part, the National Competitiveness and Infrastructure Plan also addresses the issue of SEZs.

National Competitiveness and Productivity Plan (PNCP) 2019-2030

Priority Objective - OP No. 7: "Facilitate conditions for foreign trade of goods and services."

Policy Measure 7.5 Special Economic Zones

The SEZs are based on mechanisms to promote private investment in Peru, particularly in technology that increases the degree of sophistication in goods and services and contributes to regional economic growth.

It is necessary to consider the coordination and interrelation of the entities involved in foreign trade activities, to make the processes related to foreign trade more efficient and

competitive compared to other parts of the world. In order to achieve these objectives, it is essential to improve the regulatory framework, strengthen the management of the SEZs and the administrative and operational management by private operators.

Trade Agreements Signed by Peru

Within the framework of the Trade Promotion Agreements signed, goods produced in the SEZs are considered in the negotiations so that they enjoy Tariff Preferences.

The SEZ legislation has been adapted to international regulations to benefit from the agreements signed by the country (requirements to use national inputs, elimination of performance requirements, and export percentages for goods produced in SEZs).

Finally, through review of reports, the MINCETUR has determined the following criteria:

- Evaluation of the social and economic impact of the SEZ in the region, through a Master Development Plan supported by technical, economic, and financial feasibility studies.
- Evaluation of the project's impact on the generation of direct and indirect employment in the region.
- Consider aspects of location, logistical connectivity, provision of basic services (water, energy, internet, etc.), and other essential elements that facilitate the development of the SEZ and ensure the viability of the activities carried out by the user companies.
- Evaluate the size of the SEZ and its reasonableness.
- Consider the option of Private Administration that pursues a business model focused on attracting large investments, through an Investment Promotion Plan subject to meeting goals.
- Determine the activities to be promoted in the SEZ and assess their impact considering the national and regional industry.
- Establish flexible internal procedures and processes that allow traceability for the control and supervision of merchandise based on a computer system that allows users of the regime to interact with the current customs and tax and foreign trade systems, as well as have the necessary infrastructure and equipment that allows its use meeting international standards.
- A computer system that allows the User Architecture to be interoperable with the customs and tax systems of VUCE 2.0 and SUNAT, as well as provides the necessary

infrastructure and equipment in accordance with international standards based on the National Exporter Strategic Plan - El Plan Estratégico Nacional Exportador 2025 (PENX 2025).

4.2.4. Policy Implications for Improving the Governance System of Peruvian SEZs

The problems of the Peruvian Special Economic Zone analyzed so far and the government's major policy tasks to solve them could be summarized as <Table 3-5>. Based on these issues, the KSP team would like to present several policy implications for the sustainable development of the Peruvian Special Economic Zones from the governance perspective.

<Table 3-5> Problems and Tasks for Sustainable SEZs in Peru

Problems of Peruvian SEZs	Major Tasks of Government Agencies
• Need for improving governance due to the involvement of multiple ministries or governmental agencies • Insufficient provision of social infrastructure and services • Mismatch with OECD Recommendations and WTO Agreement in SEZ operation • No basic plan and promotion strategies for sustainable SEZs • Insufficient legal provisions in the designation and operation of SEZs from the economic perspective	• Unify the current legal framework • Enable the creation of new SEZs based on space requirements, connectivity, Master Development Plan, infrastructure investment, fenced areas, and private operation. • Improve competitiveness, attract investment, generate jobs, and increase Peru's exports through SEZs. • Implement a National System of Special Economic Zones - NSSEZ (SEZ, operators, companies, and other services). • Attract tenant companies with a new exportable offer. • Create a supportive and flexible customs regime, ensuring the flow of goods. • Establish a tax regime with benefits for users and the operators subject to investment requirements. • Attract investment: Attraction of operators or developers of SEZ and companies engaged in research, scientific development, and innovation activities.

Source: MINCETUR (2022) and the KSP team.

① Regulatory complexity: The regulatory framework for SEZs in Peru tend to be complex and cumbersome, leading to difficulties for investors and operators in understanding and complying with the requirements. The overlapping jurisdiction of multiple government agencies involved in SEZ administration and the need to navigate through various regulations and permits can create delays and administrative burdens.

② Inconsistent implementation: There have been instances of inconsistent implementation and interpretation of SEZ regulations by different government entities. This lack of uniformity can create uncertainty and unpredictability for investors and businesses operating within SEZs.

③ Infrastructure and connectivity: Inadequate infrastructure, including transportation, logistics, and utilities, can pose challenges for SEZs. Insufficient connectivity to transportation networks, ports, and airports potentially hinder the efficient movement of goods and services, impacting the competitiveness of SEZs.

④ Limited institutional capacity: The management and oversight of SEZs require robust institutional capacity. However, there have been concerns about the capacity of government agencies responsible for SEZ administration in terms of resources, expertise, and coordination. Insufficient capacity often lead to delays in processing permits, inadequate supervision, and challenges in providing necessary support to SEZ operators.

⑤ Lack of stakeholder engagement: Effective stakeholder engagement is crucial for the successful governance of SEZs. However, there have been instances where local communities, environmental groups, and other stakeholders have had limited involvement in decision-making processes and impact assessments. This can lead to social and environmental concerns and conflicts.

Addressing these challenges requires a comprehensive approach that includes streamlining regulations, improving coordination among government agencies, investing in infrastructure development, enhancing institutional capacity, promoting stakeholder engagement, and implementing measures to enhance transparency and combat corruption. Efforts to address these issues can contribute to creating a more efficient and investor-friendly environment for SEZs in Peru.

5. Lessons from Korean Experience

Korea has been actively using the Special Economic Zone (SEZ) system to attract foreign capital and secure advanced technology in the process of industrialization, and it is evaluated that there have been significant achievements. Masan Free Export Zone, the first SEZ, was designated in 1970, and various SEZs have been established since then according to economic and industrial development.

5.1. Categories of Korean SEZs

Korea's Special Economic Zones can be divided into eight categories: Free Trade Zones (FTZ), Free Economic Zones (FEZ), Foreign Investment Zones (FIZ), Saemangeum

special zones, corporate cities, regional special development zones, R&D special zones, and international science business belts (KIEP, 2015, pp. 2-3). Each Special Economic Zone provides special incentives to develop the economy, but there are differences in the purpose of designation and specific implementation methods. To help understand the characteristics of these SEZs, the governance system for each Special Economic Zone is shown in <Table 3-6>.

<Table 3-6> Governance System of Korean SEZs

Types	Appointment	Administration	Administrative Agency	Decision Making Unit (Chairperson)
Free Economic Zone	MOTIE	MOTIE	FEZ Authority and Local Government	FEZ Committee (Minister of MOTIE
Free Trade Zone	MOTIE	MOTIE, MOLIT	FTZ Office and Port Authority	
Foreign Investment Zone	MOTIE	MOTIE	Local Government	FIZ Committee
Saemangeum Special Zone	MOLIT	MOLIT	Saemangeum Development Agency	SDI Committee (Prime Minister)
Enterprise City	MOLIT	MOLIT	Local Government	City Development Committee (Minister of MOLIT)
R&D Special Zone	MSIT	MSIT	Korea Innovation Foundation	Innopolis Committee (Minister of MSIT)
International Science Business Belt	MSIT	MSIT	Korea Innovation Foundation	Innopolis Committee (Minister of MSIT
SEZ for Regional Development	MSS	MSS	Local Government	RSEZ Committee (Minister of MSS)

Note: MOTIE : Ministry of Trade, Industry, and Energy.
MOLIT : Ministry of Land, Infrastructure, and Transport.
MSIT : Ministry of Science and ICT.
MSS : Ministry of SMEs and Startups.
Source: Adapted from KIEP (2016).

Among the eight types of SEZs mentioned above, this chapter focuses on Free Economic Zones (FEZs), Free Trade Zones (FTZs), and Foreign Investment Zones (FIZs) that have similar characteristics to Peru's SEZs, and examines the main contents of the underlying laws and regulations for their establishment.

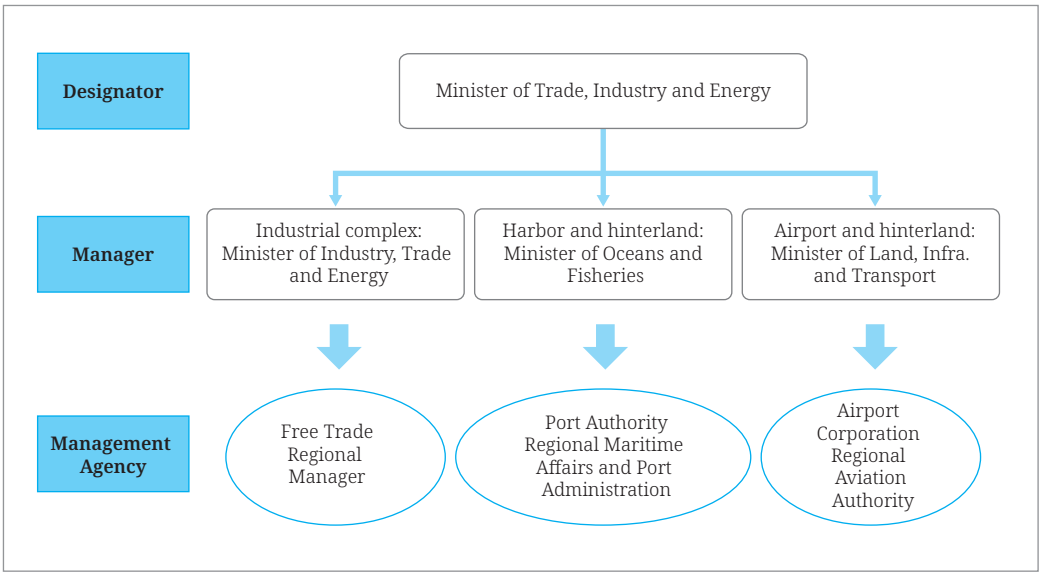
5.1.1. Free Trade Zone

The Masan Free Export Zone, designated in 1970 and later renamed the Masan Free Trade Zone, was the first SEZ established in Korea. Masan is a port city located in the southern part of the Korean Peninsula, close to Japan.

Free Trade Zones in Korea can be classified into two types: industrial complex type and airport/port type. The former refers to a Free Export Zone (FEZ), and the latter is a Free Customs Zone (FCZ). Seven industrial complex-type Free Trade Zones (Masan, Gunsan, Daebul, Donghae, Yulchon, Ulsan, and Gimje) have been designated. There are a total of six port/airport-type Free Trade Zones (Busan Port, Gwangyang Port, Incheon Port, Pohang Port, Pyeongtaek/Dangjin Port, and Incheon International Airport).

The Masan Free Trade Zone is managed by the Minister of Trade, Industry, and Energy. The management of airports and hinterland complexes falls under the authority of the Minister of Land, Infrastructure, and Transport, while ports and hinterland complexes are managed by the Minister of Oceans and Fisheries. The management system for free trade zones is as shown in [Figure 3-3].

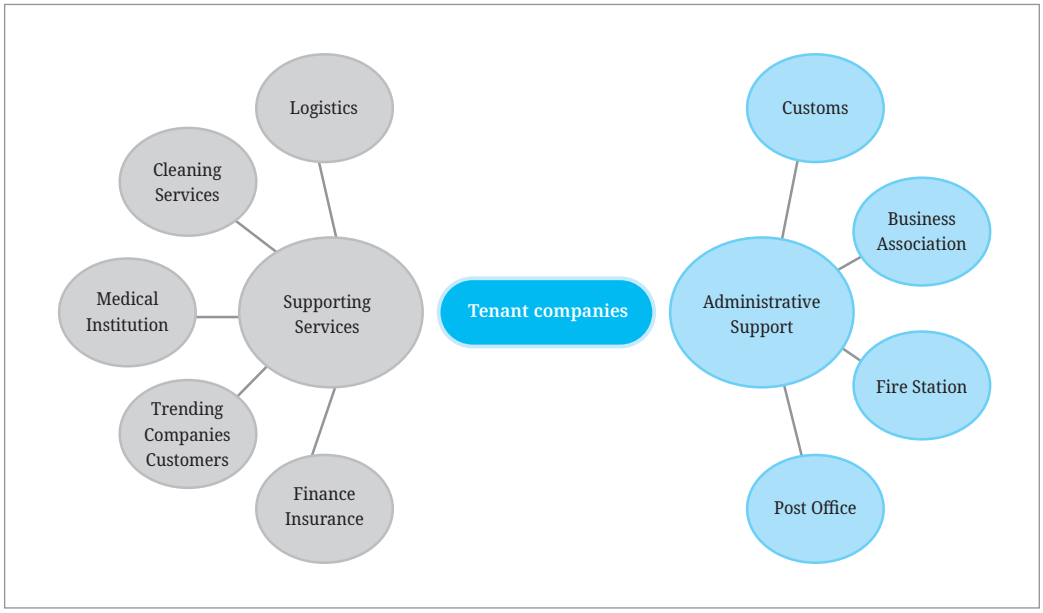
[Figure 3-3] Free Trade Zone Management System



Source: KIEP (2016).

Although there are slight differences by region, Free Trade Zones provide incentives such as tax (national and local taxes) deduction, exemption from special tariffs, exemption from value-added tax, and low rent. The Masan Free Trade Zone operates the following one-stop-service system to support foreign-invested companies.

[Figure 3-4] Extended One-stop-service System



Source: Masan Free Trade Zone (http://www.motie.go.kr/ftz/masan/, accessed on December 28, 2022).

Since its designation, the Masan Free Trade Zone has achieved results such as acquisition of foreign exchange, increased exports, employment growth, technology acquisition and transfer of management know-how. In addition, local enterprises have contributed to the national economy by establishing forward and backward linkages and participating in the global value chain. However, with the expansion of Free Trade Agreements (FTAs), the uniqueness of the Free Trade Zone as a tariff-free zone has declined.

5.1.2. Free Economic Zone

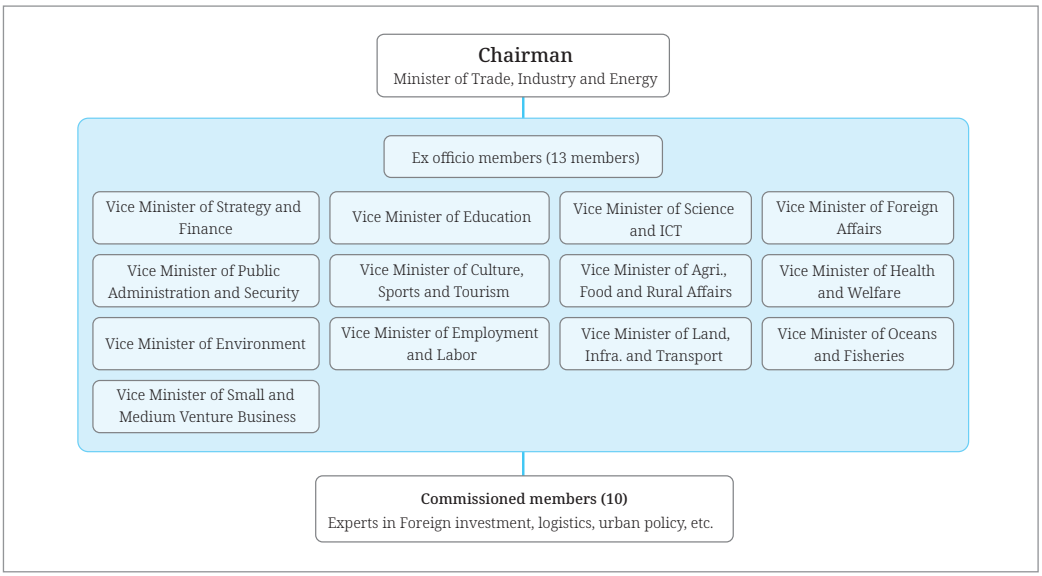
The Korean government began operating the Free Economic Zone system in 2003 to foster business hubs in Northeast Asia and expand foreign investment attraction. As of December 2022, nine Free Economic Zones, distributed across the country (Incheon, Busan-Jinhae, Gwangyang Bay Area, Gyeonggi, Daegu-Gyeongbuk, East Coast, Chungbuk, Gwangju, and Ulsan), have been designated and are being operated.

Free Economic Zones are managed by the Free Economic Zone Committee and the Free Economic Zone Planning Team. The organization chart of the Free Economic Zone Committee is shown in [Figure 3-5]. The Free Economic Zone Committee is composed of ex officio members, composed of vice ministers from 13 related departments and 10 external commissioned members composed of external experts (foreign investment, logistics, and urban policy experts). The committee performs deliberations and prepares the major

policies and plans for the Free Economic Zones, as well as overall matters related to the operation.

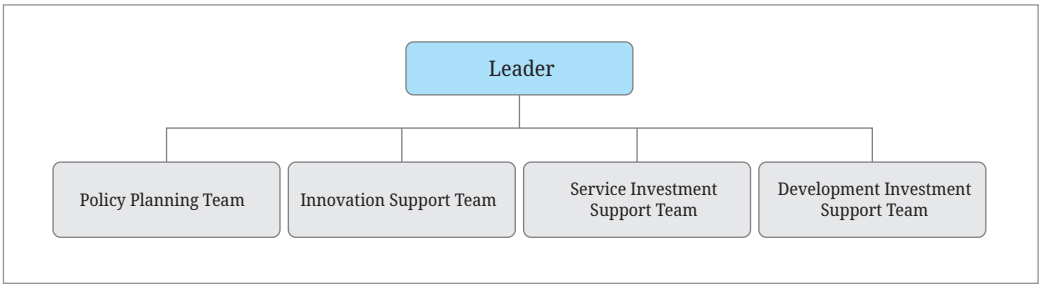
The Free Economic Zone Planning Team is in charge of drafting related policies and systems. The management of the Free Economic Zones and discussions on the development plan are also carried out by the Free Economic Zone Planning Team. The organization chart of the Free Economic Zone Planning Team is shown in [Figure 3-6].

[Figure 3-5] Free Economic Zone Committee Organization Chart



Source: Korea free Economic Zone (https://www.fez.go.kr/, accessed on December 28, 2022).

[Figure 3-6] Free Economic Zone Planning Team Organization Chart



Source: Korea free Economic Zone (https://www.fez.go.kr/, accessed on December 28, 2022).

Business support includes various forms of financial and site support, such as cash grants, infrastructure assistance, and rent subsidies. These incentives are provided based on 「the Special Act on Designation and Management of FEZs」, 「the Foreign Investment Promotion Act」, and local ordinances.

Under the One-stop Service Program, each FEZ designates individual project managers who support all investment procedures from preliminary review of investment to follow-up management. The project managers provide not only business consulting for new investment opportunities and prospective investment partners but also administrative support for legal affairs, accounting, and tax management. This will help investors make swift business decisions.

Since the designation of the Free Economic Zone, the attraction of Foreign Direct Investment (FDI) has steadily increased, but it has not reached the level expected at the time of designating the Free Economic Zone. This inadequacy is related to the lack of a comprehensive strategy for attracting foreign investment to the Free Economic Zones. Issues such as the lack of development strategies specific to each Free Economic Zone, the lack of discriminatory target industries for attracting investment to the Free Economic Zone and the resultant competition between FEZs, the lack of anchor companies, and inadequate living conditions for foreigners have been identified as problems that need to be addressed.

5.1.3. Foreign Investment Zone

A Foreign Investment Zone (FIZ) is a special area that provides incentives such as tax cuts, rent cuts, and administrative deregulation to foreign companies that wish to invest, in order to achieve advancement of industrial structure, technology transfer, and employment increase through large-scale attraction of foreign investment.

Foreign Investment Zones are divided into complex-type and individual type. The complex type was introduced in 1994 to promote domestic investment by foreign companies with advanced technologies, while the individual type was introduced after the 1997 foreign exchange crisis to allow investors to designate an investment area. Although based on different laws, the Korean government enacted the Foreign Investment Promotion Act in 2004 to integrate and manage these two types jointly.

The Korean government is making efforts to expand social overhead capital and improve the business environment and attract Research and Development (R&D) and high-value-added service industries. To this end, various incentives such as tax reductions and exemptions, location support, cash grants, and R&D centers are provided.

In the early stages of Foreign Investment Zone designation, there was a high growth rate of foreign investment. However, the growth rate slowed down later. In the case of industrial park-type Foreign Investment Zones, which operate by designating a specific

area in advance, if the Foreign Investment Zone is designated as a national industrial park, it is managed by the Industrial Complex Authority. However, in other cases, the local government or the local public enterprise are responsible for management according to their jurisdiction. To improve this situation and establish an efficient management system, it is necessary to improve the governance structure.

5.1.4. Comparison of Major SEZs in Korea and Their Legal Basis

Korea's SEZs have their own establishment laws, as shown in <Table 3-7>. In other words, FEZs are established and operated on the basis of the 「Special Law on the Designation and Operation of Free Economic Zones」, FIZs under the 「Foreign Investment Promotion Act」, and FTZs under the 「Act on Designation and Management of Free Trade Zones」. In addition, each law stipulates in the general provisions: 1) the purpose of the establishment of the SEZ (in the General Regulations) and the administrative and financial support obligations of the central and local governments to achieve it; 2) the establishment, designation, and operation of the basic plan; 3) the implementation of development projects; 4) support to be provided for the management activities of foreign-invested enterprises; 5) the improvement of living conditions for foreigners; 6) the regulations applicable to the SEZ Committee, etc.; 7) the evaluation and preparation of statistics on business performance (in supplementary provisions); and 8) penalty provisions to secure the efficient designation and operation of special zones. The main contents are summarized in <Table 3-8>.

<Table 3-7> Comparison of Major SEZs in Korea

Classification	Free Economic Zones	Foreign Investment Zones		Free Trade Zones
		Complex	Individual	
Legal basis	「Special Law on the Designation and Operation of Free Economic Zones」	「Foreign Investment Promotion Act」		「Act on Designation and Management of Free Trade Zones」
Purpose	Attracting foreign capital, strengthening national competitiveness, promoting balanced regional development	Foreign capital attraction, advanced technology transfer, job creation		Foreign investment, trade promotion, and regional development
Location	Around international airports, harbors, etc.	In Industrial Complexes	Unrestricted	Ports, airports, industrial complexes, cargo terminals, etc.
Entry requirements	- Foreign-invested companies - Manufacturing, logistics, healthcare, education, foreign broadcasting, financial institutions	- More than 30% share through foreign investment - Over 100 million KRW in foreign investment	- More than 10% share through foreign investment - Over 100 million KRW in foreign investment	- Domestic and foreign companies for export purposes - Foreign-invested companies - Main purpose of import and export transactions by wholesale business - Complex logistics related business

Source: Adapted from Jang (2023).

<Table 3-8> Laws Related to Major SEZs in Korea

Name	Main Contents
「Foreign Investment Promotion Act」	- The law underlying the Foreign Investment Zone system • Specify supportive policies to encourage foreign investment • Foreign investment requirements and procedures • Investment support system (Tax reduction, location support, cash support, etc.)
「Special Act on Designation and Management of Free Economic Zones (FEZ)」	- The laws underlying the Free Economic Zone system • Designation and development of Free Economic Zones • Support for business activities of foreign-invested enterprises (Tax reduction, land lease reduction, infrastructure support, etc.) • Improve living conditions for foreigners (Authorization of foreign educational institutions, foreign medical institutions, foreign casino businesses, etc.)
「Act on Designation and Management of Free Trade Zones (FTZ)」	- The law underlying the Free Trade Zone system • Designation, management, and occupancy of free trade zones • Incentives for foreign-invested enterprises (Deemed to be a company in a foreign-invested zone)
「Act on Restriction of Special Taxation」	- General law on tax specialties, specifying tax breaks for foreign-invested companies

Source: Adapted from Jang (2023).

5.2. Development of SEZs in Korea

Special Economic Zones (SEZs) have gone through several generations of development since the concept was first introduced in the 1960s. These generations are characterized by different models of development and different policy frameworks. Here is a brief overview of the different generations of SEZ development.

<Table 3-9> Development of SEZs by Generation

Generation	Characteristics
1st Generation SEZ (1960s-1980s)	• Mainly located in Asian countries, such as Taiwan, South Korea, and China, these zones were designed to attract foreign investment and promote export-oriented manufacturing. • The policy framework for first-generation SEZs included tax incentives, streamlined bureaucratic procedures, and infrastructure development.
2nd Generation SEZ (1990s-2000s)	• Characterized by a more diversified set of activities, such as high-tech manufacturing, research and development, and services, these zones were located in a broader range of countries, including those in Africa and Latin America. • The policy framework for second-generation SEZs focused on creating business-friendly environments and promoting technology transfer
3rd Generation SEZ (2000s-2010s)	• Characterized by a more strategic approach to development, with a focus on sustainable economic growth and development, these zones were located in countries such as China, India, and Indonesia. • The policy framework for third-generation SEZs included a broader set of policy instruments, such as public-private partnerships, cluster development, and social and environmental responsibility.
4th Generation SEZ (2010s-Present)	• Still evolving and characterized by a focus on innovation, knowledge-based industries, and digital technologies, these zones are being developed in countries such as Singapore, South Korea, and China. • The policy framework for fourth-generation SEZs includes incentives for innovation, the development of smart cities, and the promotion of entrepreneurship.

Source: Adapted from KIEP (2016).

Overall, the evolution of SEZs has been driven by changes in the global economy, as well as shifts in policy priorities and technological advancements. The different generations of SEZs reflect the changing needs and aspirations of countries as they sought to attract foreign investment, promote economic growth, and create new opportunities for their citizens.

Korea's special zone system has developed into various types reflecting the policy vision and goals of the times. Overall, the special zone system is evaluated as having positive economic results, but there are also some problems.

5.3. Success Factors of the Korean SEZs and Policy Implications

Korea's SEZ operation experience provides some useful implications that Peru may consider in its efforts to attract foreign direct investment through the SEZ system.

5.3.1. Continuous Revision of the Master Plan for SEZ Development

So far, the Korean government has established and implemented the 10-Year Basic Plan for Free Economic Zones every 5 years, on three occasions in line with changes in internal and external environments. The key elements of the basic plan are the establishment of a new vision, and the designation and development of policy directions to promote investment attraction, strengthen the innovation ecosystem, and enhance the efficiency of special zones. The vision of the first basic plan (2013-2022) was "Business Hub with Global Competitiveness"; in the case of the second basic plan (2018-2027), it was "Global New Industrial Hub Leading Innovative Growth," and the vision of the third basic plan of FEZs (2023-2032) is "Completion of Global FEZ through Construction of Innovative Platform," In the plan, 16 policy tasks are selected with the goals of "establishing an innovative platform for fostering core strategic industries," as well as "establishing a future-oriented smart green platform, an investment attraction platform, and a cooperative governance platform." Guidance provided in this plan would be of great help in designing a master plan for SEZs in Peru.

5.3.2. Effective Governance

One useful lesson from Korea's experience is the need to simplify the governance system for SEZs. When various government agencies are involved in the operation of SEZs, it is necessary to find a way to simplify the governance structure as much as possible. In the case of Korea's Free Economic Zones, the Free Economic Zone Committee is responsible for the deliberation/decision-making on major policies, systems, and overall management, while the

Free Economic Zone Planning Team is responsible for policy planning and implementation. This configuration may be an effective option for efficient SEZ operation in situations where multiple government agencies are involved.

In relation to SEZ operation, coordination among various government agencies can be achieved if the FEZ Committee is given charge of deliberations and decision-making on matters related to their interests. Operational efficiency can be improved if the FEZ Planning Group is empowered to work actively in the process of coordination and operation.

5.3.3. Establishment of Infrastructure

To attract investment to SEZs, it is important to establish infrastructure related to corporate management, such as transportation, logistics, communication, and the internet, around the SEZs. The infrastructure status should be considered during the initial designation stage, but it can also be expanded as part of the government's support policy after SEZ designation, as seen in the case of Korea's Masan Free Trade Zone.

5.3.4. Government Involvement and Support

To ensure the success of SEZs, it is important to concentrate on the nation's capabilities. For this purpose, the central and local governments should cooperate and show active involvement from the stage of establishing the SEZ strategy and provide the necessary support. Especially, Korea's SEZs are utilizing a one-stop service system. From the point of view of foreign companies investing in Peru, the system and culture of Peru may not be familiar. The operation of a one-stop service system that can solve the licensing and permitting process required for investment at once can have a positive effect on attracting investment.

Another important support system in Korea is Foreign Investment Ombudsman (FIO). FIO and the associated grievance resolution body collect and analyze information concerning the problems foreign firms experience, request cooperation from relevant administrative agencies and recommend implementation plans, propose new policies to improve the foreign investment promotion system, and carry out other necessary tasks to assist foreign-invested companies in resolving their grievances.

<Box 3-2> Foreign Investment Ombudsman in Korea

The Foreign Investment Ombudsman system was first introduced on October 26, 1999, under the Foreign Investment Promotion Act, with a view to resolving grievances of foreign-invested companies operating in Korea. Its role comprises the resolution of almost all grievances in the areas of taxation, law, construction, finance, foreign exchange, visa, etc. The Foreign Investment Ombudsman is commissioned by the President on the recommendation of the Minister of Trade, Industry and Energy following deliberation by the Foreign Investment Committee. The Foreign Investment Ombudsman also heads the grievance settlement body, which supports the duties of Ombudsman.

Source: Invest Korea (https://ombudsman.kotra.or.kr/ob-en/cntnts/i-2643/web.do).

5.3.5. Other Success Factors

In addition, there are many factors that contributed to the success of Korean SEZs, including: 1) designation of a special zone at an appropriate location and time, as in the case of Masan FTZ; 2) establishing a productive relationship between SEZ and the outside world; and 3) providing manpower necessary for corporate management.

5.3.6. Problems Faced by Korean SEZs

While Special Economic Zones (SEZs) in Korea have been successful in attracting investments and promoting economic growth, they also face certain challenges in their governance system. Some of the problems are:

① Regulatory Complexity: The governance framework for SEZs in Korea tends to be complex and involves multiple government agencies and regulations. The overlapping jurisdictions and complex procedures may create administrative burdens and delays for investors and businesses operating in SEZs.

② Lack of Coordination: The governance structure of SEZs involves multiple government entities responsible for various aspects such as infrastructure, investment promotion, customs, and labor regulations. In some cases, insufficient coordination and communication among these entities lead to inconsistencies in policy implementation and decision-making.

③ Limited Autonomy: While SEZs aim to provide greater flexibility and incentives for businesses, the extent of autonomy granted to SEZs in Korea is relatively limited compared to some other countries. This restricts the ability of SEZs to make independent decisions, adapt regulations to specific needs, and respond promptly to changing market conditions.

④ Stakeholder Engagement: Effective stakeholder engagement, including local communities, labor unions, and environmental groups, is crucial to implement

sustainable development and address social concerns. Ensuring meaningful participation and involvement of stakeholders in decision-making processes and addressing their concerns can be a challenging aspect in the governance of SEZs.

⑤ Environmental Impact: SEZs, due to their industrial and economic activities, may have environmental implications. Ensuring environmental sustainability and mitigating negative impacts, such as pollution and resource depletion, require robust environmental regulations, monitoring, and enforcement mechanisms.

5.3.7. Policy Implications of Korean Experience

By comparing the success factors and problems of the Korean Special Economic Zones, it is possible to draw policy implications that can help the sustainable development of the Peruvian Special Economic Zone (See Table 3-10).

Addressing the aforementioned governance challenges in Peruvian SEZs requires a holistic approach. This includes improving coordination among government agencies, simplifying regulations, enhancing autonomy and decision-making powers of SEZs, investing in infrastructure development, promoting skill development programs, fostering stakeholder engagement, and implementing effective environmental management practices. By addressing these issues, the governance system of Peruvian SEZs can be strengthened, leading to sustainable and inclusive economic development.

<Table 3-10> Major Success Factors and Problems in Korean SEZ

Success Factors	Problems
• Establishment of a basic plan based on laws • Effective governance • Establishment of infrastructure • Strong government support • Others	• Regulatory complexity • Issues of fragmented governance • Limited autonomy • Insufficient stakeholder engagement • Late response to environmental changes

Source: Adapted from KIEP (2016).

5.4. Benchmarking the Governance System of Selected Countries

Looking at the background of the Special Economic Zone, from the early stages of international trade (Hong Kong, the Netherlands) to the production-oriented (Korea's 'Free Trade Area', Ireland, Mexico) and production/trade models (Singapore, China), Korea has also established a variety of new knowledge-creation-type Special Economic Zones.

It is very difficult to organize Special Economic Zones or Free Economic Zones, which

have been established over a long period of time with somewhat similar names in various regions and numerous forms worldwide, into a handful of categories. However, it can be understood that the basic purpose is to create and distribute maximum economic value by designating a specific space. In either case, the biggest short- and long-term purpose is understood to be attracting businesses and foreign investment, and this applies to Peru as well.

5.4.1. Singapore

Singapore is known around the world as a trade-focused country with pro-business free trade regulations that form the core of its international trade policy. Singapore's free-trade agreements, investment guarantee agreements, and more than 80 Double Tax Treaties, or Double Taxation Avoidance Agreements (DTAAs), including the India-Singapore DTAA and the Malaysia-Singapore DTAA, facilitate smooth trade with nearly every country in the world.

Another advantage that Singapore offers to international trade firms is its Free-Trade Zones (FTZs). FTZs in Singapore were first established in 1969 to support the country's drive to establish itself as a center for entrepot trading and transshipment activities. Their objectives have expanded since then. FTZs in Singapore are designated areas where the payment of duties and taxes is suspended when goods arrive, are stored, or are sold within the FTZ. Singapore's main legislation on the country's FTZs is embodied in the Singapore Free Trade Zones Act, which came into effect in 1966 and was last amended in 2014.

The Singapore Free Trade Zones Act outlines:

- The authorities in charge of verifying the activities of companies operating in the Free-Trade Zones in Singapore, namely the Free Zone Advisory Committee, the Director of the Singapore Customs, and the Ministry for Trade and Industry;
- Activities that may be undertaken by Free Trade Zone companies in Singapore;
- Types of licenses and permits required to manufacture and sell goods in the free zones;
- Penalties for not abiding by regulations imposed by the free zone authorities.

5.4.2. China

SEZ development was a key feature of China's reforms and opening from 1978, allowing China's previously internationally isolated economy to gradually engage with the world economy and pursue global trade and foreign investment. Almost by default, discussions

in the literature cover China's early-reform era SEZs, especially the first four, established in advantageous coastal locations – Shenzhen, Zhuhai, Shantou, and Xiamen. Over time, the zones grew in number and spread along the coast and later into interior regions through a gradual process (Zeng, 2015). With the establishment of SEZs, the central government aimed to attract foreign capital, encourage joint ventures and partnerships between local and foreign firms, and promote exports. It introduced special legal frameworks to protect property rights in the zones, provide tax incentives, and allocate land use rights. At the same time, significant authority over SEZ management was decentralized and granted to local governments (Wang, 2013).

5.4.2.1. FDI Attraction Agency at Central Government Level

In China, various organizations are involved in attracting and managing foreign investment at the Chinese central government level. The following institutions are involved, such as the State Council, the highest administrative agency, the Ministry of Finance and Economy, the Ministry of Foreign Affairs and Trade, the Ministry of Finance and the National Tax Service, the National Price Bureau, the National Trade and Industry Administration, and the Ministry of Foreign Exchange.

5.4.2.2. Administrative Committee of China Development Zones

This organization is an administrative agency established by local governments for the management of development zones, and conducts economic and social management of development zones on behalf of local governments. For example, the Shanghai Free Trade Area Administration Committee has unified control over administrative affairs in the Free Trade Zone and manages financial income and expenditure as an independent accounting unit. Regarding other functions, first, it is responsible for the enforcement of laws and regulations on free trade and the establishment and publication of rules for the management of Free Trade Zones. Second, development plans and industrial policies for Free Trade Zones are prepared and implemented with the approval of the municipal government. Third, the Committee is responsible for the exercise of authority delegated by the City regarding inspection, approval, and permission related to planning, state-owned property, overseas economic trade, public finance, local taxes, statistics, industrial and commercial administration, public security, labor and manpower supply, external affairs, transportation, infrastructure, land and real estate, environmental conservation, and public facilities. Fourth, it is in charge of cooperation with state agencies related to customs, national taxes, finance, and inspection.

5.4.3. India

Like China, India combined central government policy direction on SEZs with devolved day-to-day management by local governments (Tantri, 2013). Specifically, India's SEZ Act 2005 granted state governments much latitude over the development and management of SEZs, and significant authority was delegated to the local level administration, often to the state development commissioner. The Act's comprehensive and dedicated legislation replaced the range of policies and ministries that governed India's EPZs before 2005. It allowed India's SEZs to operate under different regulatory frameworks from the undesignated parts of the country, with company "self-certification" being introduced to reduce the need for inspections and official attestation (Kennedy, 2014; Singh, 2009). Similar to China, India's new SEZs were also envisaged as encompassing all the social facilities that make up a small city, which distinguished them from the EPZs' more modest industrial parks (Knoerrich, Mouan and Goodburn, 2021).

5.4.4. Dominican Republic

The Dominican Republic is often considered an example of the successful implementation of Special Economic Zones in Latin America. Surgical equipment, chemicals and plastics, and footwear have recently emerged as the new drivers of export dynamism in the Dominican Republic's special zones (World Bank, 2016). The developmental impact of SEZs in the Dominican Republic can be found in the i) regulatory reforms aimed at complying with WTO disciplines regarding the elimination of incentives conditioned on export performance for SEZs firms, ii) the extent to which SEZs participate in Global Value Chains, and iii) their close linkages with domestic suppliers.

<Table 3-11> Major Characteristics of Governance System in Selected Countries

Country	Characteristics	Implications
Singapore	The most open country to trade Singapore FTZ Act amended in 2014	Close cooperation among related agencies Effective on-line administrative support
China	FDI attraction agency at central govt. level Active role of the Administrative Committee	Decentralized SEZ management by local govt. Close cooperation with central govt.
India	Comprehensive legislation (SEZ Act 2005) Deregulation using self-certification	Delegation of authority to local level City-level social infrastructure
Dominican Republic	Specialization in prospective industries Complying with WTO disciplines	Need for regulatory reforms Close linkages with domestic suppliers

6. Development of New Selection Criteria and Governance System

6.1. AHP/IPA Analysis of SEZ Selection Criteria

6.1.1. Analytical Hierarchy Process (AHP)

Analytic Hierarchy Process (AHP) is a multiple-criteria decision-making tool, first developed in the management science field over 40 years ago (Saaty, 1980). It was developed to help managers make decisions that are more effective by structuring and evaluating the relative attractiveness or the priority ratings of multiple competing attributes. In short, this is an Eigenvalue approach to pairwise comparisons. It also provides a methodology to calibrate the numeric scale for the measurement of quantitative as well as qualitative performances. The scale ranges from 1/9 for 'least valued than', to 1 for 'equal', and 9 for 'absolutely more important than', covering the entire spectrum of comparison (Vaidya and Kumar, 2006).

Some key and basic steps involved in this methodology are shown in [Figure 3-7].

① State or identify the problem.

② Broaden the objectives of the problem or consider all actors, objectives, and their outcomes.

③ Identify the criteria that influence the behavior or the decision.

④ Structure the problem in a hierarchy of different levels constituting goals, criteria, sub-criteria, and alternatives.

⑤ Compare each element in the corresponding level and calibrate them on the numerical scale. This requires n(n - 1)/2 comparisons, where n is the number of elements with the consideration that diagonal elements are equal or 1, and the other elements will simply be the reciprocals of the earlier comparisons.

⑥ Perform calculations to find the maximum Eigen value, CI (Consistency Index), CR (Consistency Ratio), and normalized values for each criterion/alternative.

⑦ If the maximum Eigenvalue, CI, and CR are satisfactory then the decision is taken based on the normalized values; otherwise, the procedure is repeated till obtaining values in a desired range.

The Analytic Hierarchy Process (AHP) is a decision-making method that facilitates group consensus by incorporating multiple opinions and perspectives. It typically involves using a

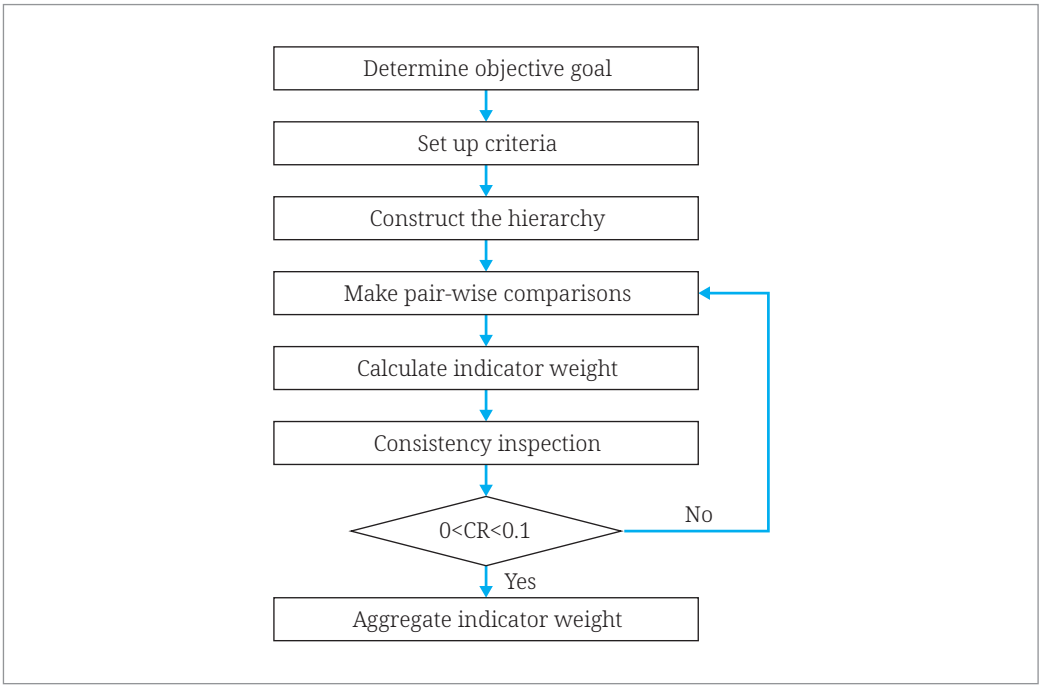
questionnaire to compare each element and calculate geometric means to determine a final solution. The hierarchical structure employed in AHP offers several advantages.

In the context of assessing the Special Economic Zone (SEZ) selection criteria, the KSP team utilizes AHP to determine the priority or relative importance of these criteria. This evaluation framework aligns with the widely employed feasibility or validity evaluation framework used in assessing the performance of various national projects, including SEZs in Korea (referencing KIEP, 2015).

By applying AHP, the KSP team can effectively assess the significance of each SEZ selection criterion, taking into account multiple perspectives and ensuring a more comprehensive decision-making process. This approach enhances the objectivity and transparency of the evaluation, allowing for informed decision-making with regard to the selection of SEZs based on their feasibility and validity.

- Derive core elements that are crucial to translating Peru's SEZ into a sustainable and inclusive economic infrastructure.
- The derived criteria weights were applied to the performance scores to evaluate each SEZ's relative overall sustainability performance.

[Figure 3-7] AHP Flow Chart



Source: Adapted from Satty (1980).

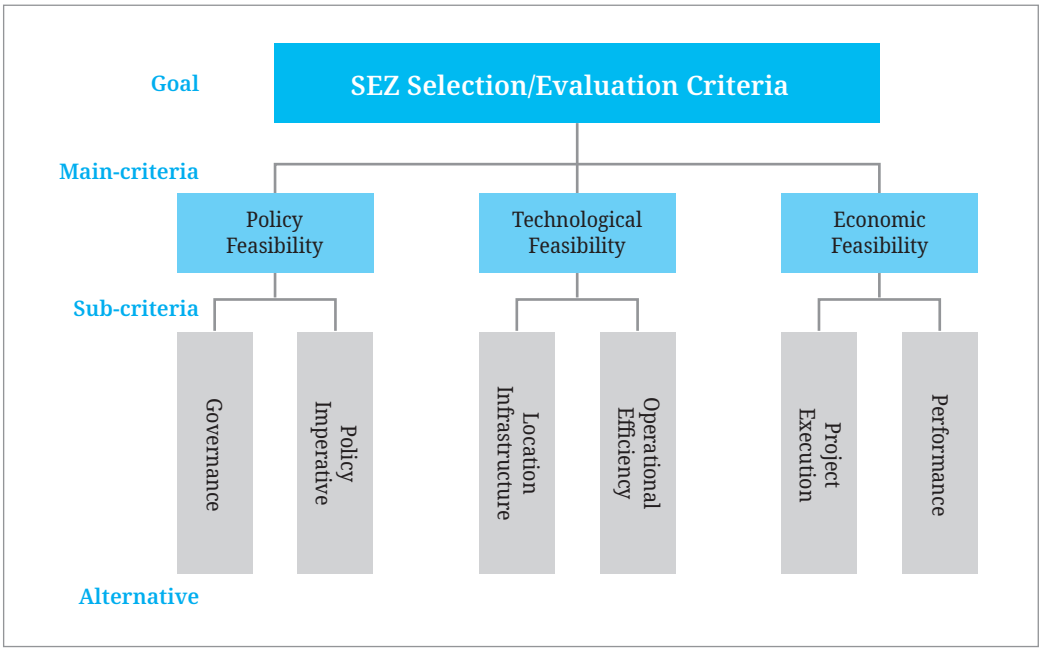
In the Analytic Hierarchy Process (AHP), the scale of importance for pairwise comparison is used to assess the relative importance or priority of one criterion or factor over another. The scale typically ranges from 1 to 9, with the following scale of importance as shown in <Table 3-12>.

<Table 3-12> Scale of Importance for Pairwise Comparison

Scale	Definition	Linguistic expression
1	Equally important	Two components are equally important in terms of the criteria for the next-highest objective
3	Somewhat important	One component is a little more important than the other
5	Important	One component is more important or valuable than the other
7	Considerably important	One component is considerably important or valuable than the other
9	Absolutely important	Incomparably important compared to the other
2, 4, 6, 8	The middle or close number	Use if necessary

Source: KIEP (2015).

[Figure 3-8] Evaluation Framework for SEZ Selection Criteria by AHP Method



Source: Adapted from KIEP (2015).

The evaluation on the feasibility of a SEZ can be conducted based on three perspectives: policy feasibility, technological feasibility, and economic feasibility as shown in [Figure 3-8].

① Policy Feasibility

Policy feasibility assesses whether the special relief plan is appropriate for the time and region, considering the needs of the times, regional characteristics, stage of economic development, and the purpose of implementation. This evaluation can be conducted based on the following criteria.

Adequacy of the purpose of designation: Examining whether the goals and objectives of the special relief plan align with the specific needs and challenges applicable to the region or situation it aims to address.

Necessity of the role of the state: Assessing the level of government intervention and support required for the successful implementation of the plan, taking into account the experiences and lessons learned from similar cases of Special Economic Zones (SEZ) in Korea and other countries.

② Technological Feasibility

Technological feasibility focuses on the operational measures and strategies associated with the special relief plan. It examines the soundness and appropriateness of the location and incentives provided to promote the success of the special zone. Key considerations include.

Appropriateness of the location: Evaluating whether the location selected for the special zone is strategically advantageous, considering factors such as infrastructure availability, access to markets, transportation networks, and proximity to resources or target industries.

Operational efficiency: Assessing the effectiveness and efficiency of the operational measures implemented within the special zone, including administrative processes, regulatory frameworks, and business facilitation services.

③ Economic Feasibility

Economic feasibility evaluates the financial viability and sustainability of the SEZ. This assessment can be conducted by examining the following factors.

Degree of execution of the project: Evaluating the progress made in implementing the SEZ, including the establishment of necessary infrastructure, attraction of investments, and development of targeted industries.

Achievement of performance goals: Assessing the extent to which the SEZ has achieved its intended economic outcomes, such as job creation, revenue generation, export promotion, technological advancements, and overall economic growth.

In this context, the KSP adopted the framework that was used in KIEP (2015) to conduct AHP on SEZ selection criteria as shown in <Table 3-13>. By evaluating the SEZ from these three perspectives, policymakers can gain a comprehensive understanding of its feasibility and make informed decisions regarding its designation/operation, modification, or cancellation.

<Table 3-13> Components of SEZ Selection/Evaluation Criteria

Main Criteria	Sub-Criteria	[Explanations] and <Evaluation Index>
Policy Feasibility	Policy Imperative	[Is it a SEZ reflecting the national development strategy and global trends?] <Type of SEZ, Development method>
	Governance	[Is it a SEZ that the government should manage instead of market?] <Ownership: Public, PPP, Private>
Technological Feasibility	Operational Efficiency	[Are the supporting means including incentives appropriate to achieve the purpose of the SEZ?] <Incentives, tax exemption, mitigation of regulations, administrative services>
	Logistics/ Infrastructure	[Is the location selected for the SEZ suitable for designation or demand?] <Electricity, transportation, logistics costs, settlement conditions, GRDP, ICT infrastructure>
Economic Feasibility	Performance	[Is it a SEZ that can achieve direct and indirect economic effects?] <Employment, production, export, FDI attraction>
	Project Execution	[Is the SEZ project being faithfully implemented or is it possible to be executed?] <Execution rate, rate of sold land>

Source: Adapted from KIEP (2015).

6.1.2. Importance Performance Analysis

Martilla and James (1977) first used a market strategy developed and organized based on Importance Performance Analysis (IPA), which came to be widely used for various purposes over the years. IPA is a tool used in business and marketing to evaluate the performance of a product or service by comparing its importance to consumers against its actual performance. The goal of IPA is to identify areas needing improvements and to prioritize those improvements based on their importance to customers.

IPA involves surveying customers to determine their perceptions regarding a product or service, including how important various features are to them and how well the product or service performs on those features. The results of the survey are then plotted on a graph, with importance on one axis and performance on the other.

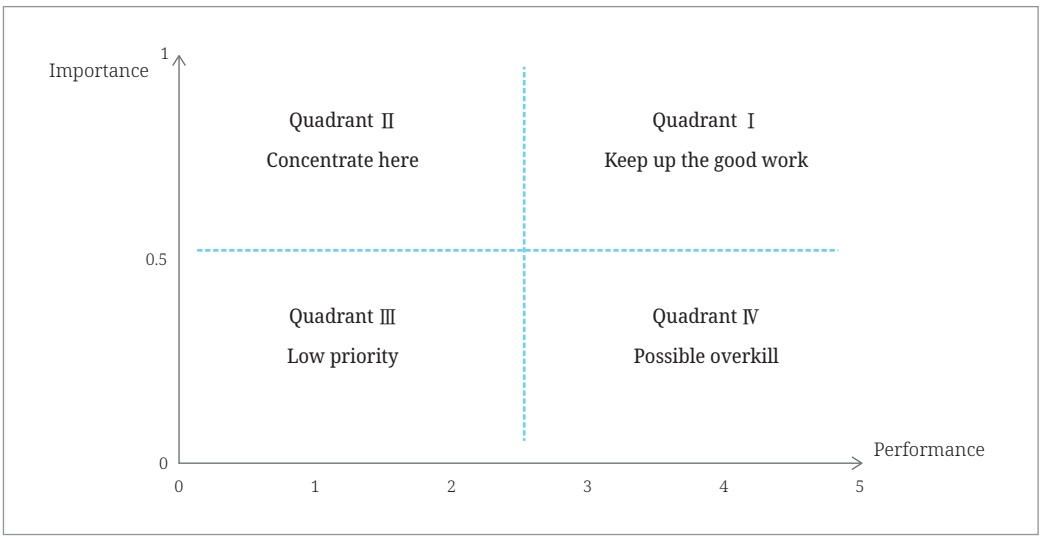
The graph is divided into four quadrants, with the first upper-right quadrant indicating high importance and high performance, the second upper-left quadrant indicating high

importance but low performance, the third lower-left quadrant indicating low importance and low performance, and the fourth lower-left quadrant indicating low importance but high performance as shown in [Figure 3-9].

The areas in the upper-left quadrant are the most critical to address, as these are the features for which performance is not adequate even though they are important to customers. The areas in the upper-right quadrant are areas of excellence, while the areas in the lower-left quadrant may not need much attention, as they are of low importance to customers.

IPA is a useful tool also for policy making like the designation of SEZs, as it provides a way to focus resources on the areas that will have the most impact on economic performance or stakeholder satisfaction. By prioritizing improvements based on perceived importance, businesses and policy makers can improve their decisions in a way that is most likely to drive economic benefits and development.

[Figure 3-9] IPA Method



Source: Martilla and James (1977).

6.1.3. Results of AHP Survey

The AHP/IPA in-depth survey was conducted using the Google Survey from March 13 to March 31, 2023, due to political instability in Peru. The research targets were selected among participants of the "Policy Practitioners' Workshop," who were recommended by MINCETUR considering the SEZ related job description. They were grouped as government officials, SEZ experts, and tenants according to the purpose of the survey. A total of 46

questionnaires were distributed. After examining consistency ratio and consistency indices, the questionnaire responses from 14 government officials, 7 SEZ experts, and 16 tenants were used for final analysis.

<Table 3-14> Results of AHP Analysis

Main-Criteria	Sub-Criteria	Weight of Importance		Rank	
SEZ Selection/ Evaluation Criteria	Policy Feasibility	0.4045		1	
	Technological Feasibility	0.3484		2	
	Economic Feasibility	0.2471		3	
Policy Feasibility	Policy Imperative	0.6588	0.2665	1	1
	Governance	0.3412	0.1380	2	5
Technological Feasibility	Operational Efficiency	0.6022	0.2098	1	2
	Location / Infra.	0.3978	0.1386	2	4
Economic Feasibility	Performance	0.6742	0.1666	1	3
	Project Execution	0.3258	0.0805	2	6

First of all, according to the AHP analysis of the policy, technological, and economic feasibility of the Peruvian SEZs, government officials and SEZ experts consider policy feasibility to be the most important factor at 40.5%, followed by technological feasibility at 34.8% and economic feasibility at 24.7%. This is somewhat different from the results of the KIEP (2015) report, which showed that technological feasibility was the most important factor at 49.8% in the AHP analysis of Korean SEZs. In order to revitalize the Peruvian Special Economic Zones and enhance their sustainability, it is expected that the Special Economic Zone should be selected and operated with priority given to performance such as export and employment growth, and rate of project execution.

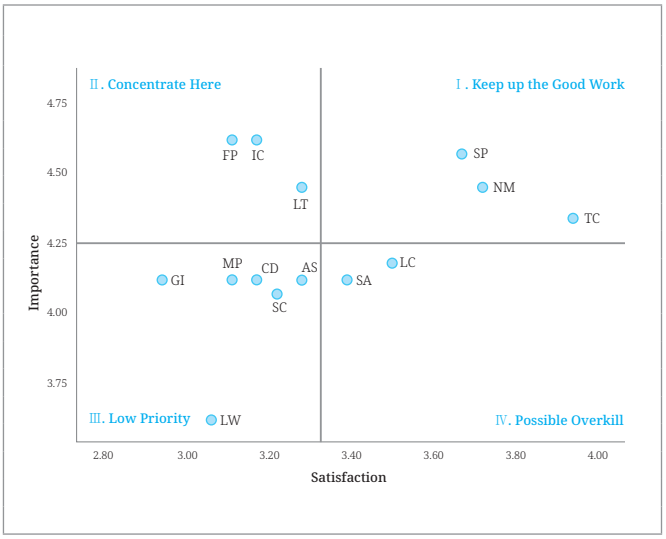
In terms of the overall ranking, policy imperative, which means whether the SEZ is in line with the national development strategy or global trends, was the most important factor at 26.7%, followed by operational efficiency (21.0 percent) in second place, performance (16.7%) in third place, logistics/infrastructure (13.9%) in fourth place, governance (13.8%) in fifth place, and business execution (8.1%) in sixth place.

According to the Korea's Third Master Plan for Free Economic Zones, while strengthening its status as a strategic partner considering the changes in the international environment such as new protectionism, GVC reconfiguration after COVID-19, and the expansion of multilateral FTAs, Korea is focusing on the completion of the global FEZ through the establishment of an innovation platform using the technologies of the 4th Industrial

Revolution. Nevertheless, in light of the importance of performance related to operational efficiency, logistics/infrastructure, and economic feasibility among the technological feasibility factors pertaining to the special zone, it is very important to choose a location with a designated purpose and assess the extent of performance that can be achieved. Therefore, the criteria for selecting a desirable SEZ should be determined by systematically reflecting these factors of policy feasibility, technological feasibility, and economic feasibility.

6.1.4. Results of IPA Survey

[Figure 3-10] IPA Result (Government Officials)

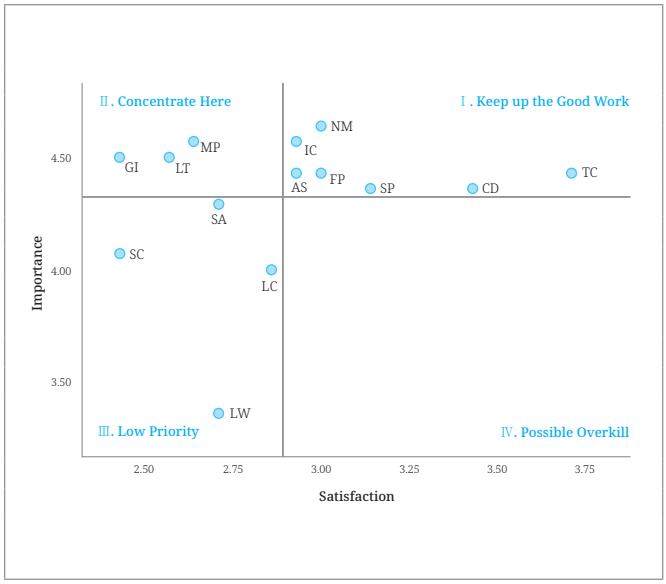


Contents	Importance		Performance	
	Mean	Rank	Mean	Rank
GI	4.11	8	2.94	14
CD	4.11	8	3.17	9
IC	4.61	1	3.17	9
FP	4.61	1	3.11	11
TC	4.33	6	3.94	1
AS	4.11	8	3.28	6
LT	4.44	4	3.28	6
SC	4.06	13	3.22	8
SP	4.56	3	3.67	3
LW	3.61	14	3.06	13
MP	4.11	8	3.11	11
NM	4.44	4	3.72	2
SA	4.11	8	3.39	5
LC	4.17	7	3.50	4
Aver.	4.24	-	3.33	-
Max.	4.61	-	3.94	-
Min.	3.61	-	2.94	-

[Figure 3-11] IPA Result (SEZ Experts)

Contents	Importance		Performance	
	Mean	Rank	Mean	Rank
GI	4.75	1	2.67	14
CD	4.42	2	3.33	8
IC	4.42	2	2.92	12
FP	3.92	12	2.83	13
TC	4.08	9	3.92	1
AS	4.33	4	3.67	5
LT	4.33	4	3.08	11
SC	3.92	12	3.33	8
SP	4.25	6	3.50	7
LW	3.58	14	3.75	3
MP	4.17	8	3.33	8
NM	4.25	6	3.58	6
SA	4.08	9	3.92	1
LC	4.08	9	3.75	3
Aver.	4.18	-	3.40	-
Max.	4.75	-	3.92	-
Min.	3.58	-	2.67	-

[Figure 3-12] IPA Result (Tenants)



Contents	Importance		Satisfaction	
	Mean	Rank	Mean	Rank
GI	4.50	4	2.43	13
CD	4.36	9	3.43	2
IC	4.57	2	2.93	6
FP	4.43	6	3.00	4
TC	4.43	6	3.71	1
AS	4.43	6	2.93	6
LT	4.50	4	2.57	12
SC	4.07	12	2.43	13
SP	4.36	9	3.14	3
LW	3.36	14	2.71	9
MP	4.57	2	2.64	11
NM	4.64	1	3.00	4
SA	4.29	11	2.71	9
LC	4.00	13	2.86	8
Aver.	4.32	-	2.89	-
Max.	4.64	-	3.71	-
Min.	3.36	-	2.43	-

[Figure 3-13] IPA Result (All Respondents)

Contents	Importance		Performance	
	Mean	Rank	Mean	Rank
GI	4.41	4	2.70	14
CD	4.27	8	3.30	6
IC	4.55	1	3.02	9
FP	4.36	6	3.00	11
TC	4.30	7	3.86	1
AS	4.27	8	3.27	7
LT	4.43	3	3.00	11
SC	4.02	13	3.00	11
SP	4.41	4	3.45	2
LW	3.52	14	3.14	8
MP	4.27	8	3.02	9
NM	4.45	2	3.45	2
SA	4.16	11	3.32	5
LC	4.09	12	3.36	4
Aver.	4.25	-	3.21	-
Max.	4.55	-	3.86	-
Min.	3.52	-	2.70	-

<Table 3-15> SEZ Selection Criteria Explained

Contents	Description	Contents	Description
GI	Continued Investment by the Government	SC	Settlement Conditions
CD	Conformity with the Purpose of SEZ Designation	SP	Sales/Export Potential
IC	Development of an Industrial Cluster	LW	Low Wages
FP	Ease of Financing from the Private Sector	MP	Ease of Supply of Skilled Manpower
TC	Tax/Customs Incentives	NM	Ease of Access to Neighboring Markets
AS	Administrative Support	SA	Ease of Site Acquisition
LT	Logistics Costs/Transportation	LC	Low Land Cost

According to the results of the IPA, government officials evaluated that 1) Development of Industrial Cluster, 2) Ease of Financing from Private Sector, and 3) Sales/Export Potential are the relatively more important factors when selecting a region as SEZ, while Peru's SEZs showed relatively higher performance in terms of 1) Tax/Customs Incentives, 2) Ease of Access to Neighboring Markets, and 3) Sales/Export Potential. In comparison, SEZ experts rated the importance of 1) Continued Investment by the Government, 2) Conformity with the Purpose of SEZ Designation, and 3) Development of Industrial Cluster relatively higher, while Peru's SEZ showed relatively higher performance in terms of 1) Tax/Customs Incentives, 2) Ease of Site Acquisition, and 3) Low Land Cost.

However, tenants in Peruvian SEZs rated 1) Ease of Access to Neighboring Markets, 2) Ease of Supply of Skilled Manpower, and 3) Development of Industrial Clusters as important factors in that order, while 1) Government's Continued Investment, 2) Settlement Conditions, and 3) Logistics Cost/Transportation showed low satisfaction. Thus, cumulative IPA results for all respondents showed that the importance of 1) Development of Industrial Cluster, 2) Ease of Access to Neighboring Markets, 3) Logistics Cost/Transportation, and 4) Sales/Export Potential was relatively higher, while 1) Continued Investment by the Government, 2) Ease of Financing from Private Sector, 3) Logistics cost/Transportation, and 4) Settlement Condition are the most unsatisfactory factors in the management of SEZs.

As mentioned above, the most important aspect in the development of policy tasks through IPA is the second quadrant, where relative importance is high but relative performance or satisfaction is low. In other words, all respondents felt that the efficient operation of the Peruvian SEZs requires continuous investment by the government, the development of industrial clusters, enhancement of the ease of financing from private sector, reduction of logistics and transportation costs, and the smooth supply of skilled manpower, among others. The factors reflected in the questionnaire were considered

relatively important criteria for selection of SEZs in numerous previous studies. Therefore, the government officials in charge of the Peruvian SEZs should prepare the appropriate criteria in selecting SEZ in full consideration of those factors, and they should make every effort to actively attract FDI to the SEZs.

<Table 3-16> Summary of IPA Results

Group	Government Officials		SEZ Experts		Tenants		All Respondents	
I	TC	Tax/Customs Incentives	AS	Administrative Support	CD	Conformity with the Purpose of SEZ Designation	CD	Conformity with the Purpose of SEZ Designation
	SP	Sales/Export Potential	SP	Sales/Export Potential	IC	Development of Industrial Clusters	TC	Tax/Customs Incentives
	NM	Ease of Access to Neighboring Markets	NM	Ease of Access to Neighboring Markets	FP	Ease of Financing from Private Sector	AS	Administrative Support
	-	-	-	-	TC	Tax/Customs Incentive	SP	Sales/Export Potential
	-	-	-	-	AS	Administrative Support	NM	Ease of Access to Neighboring Markets
	-	-	-	-	SP	Sales/Export Potential	-	-
	-	-	-	-	NM	Ease of Access to Neighboring Markets	-	-
II	IC	Development of Industrial Clusters	GI	Continued Investment by the Government	GI	Continued Investment by the Government	GI	Continued Investment by the Government
	FP	Ease of Financing from Private Sector	CD	Conformity with the Purpose of SEZ Designation	LT	Logistics Costs/ Transportation	IC	Development of Industrial Clusters
	LT	Logistics Costs/ Transportation	IC	Development of Industrial Clusters	MP	Ease of Supply of Skilled Manpower	FP	Ease of Financing from Private Sector
	-	-	LT	Logistics Cost/ Transportation	-	-	LT	Logistics Cost/ Transportation
	-	-	MP	Ease of supply of skilled manpower	-	-	MP	Ease of Supply of Skilled Manpower
III	GI	Continued Investment by the Government	FP	Ease of Financing from Private Sector	SC	Settlement Conditions	SC	Settlement Conditions
	CD	Conformity with the Purpose of SEZ	SC	Settlement Conditions	LW	Low Wages	LW	Low Wages
	AS	Administrative Support	-	-	SA	Ease of Site Acquisition	-	-
	SC	Settlement Conditions	-	-	LC	Low Land Cost	-	-
	LW	Low Wages	-	-	-	-	-	-
	MP	Ease of Supply of Skilled Manpower	-	-	-	-	-	-
IV	SA	Ease of Site Acquisition	TC	Tax/Customs Incentives	-	-	SA	Ease of Site Acquisition
	LC	Low Land Cost	LW	Low Wages	-	-	LC	Low Land Cost
	-	-	SA	Ease of Site Acquisition	-	-	-	-
	-	-	LC	Low Land Cost	-	-	-	-

6.1.5. Combined Results of AHP/IPA Survey

In consideration of the limitations of the AHP method, which is limited to the analysis of relative importance or priority, the KSP team attempted to combine the AHP method and IPA method. For this purpose, the cloud-based software 'Social Science Research Automation (SSRA)' was used for AHP analysis, and 'SPSS Statistics 28' was used for IPA method. In order to compare the importance of values according to AHP stratification analysis with the same scale as the importance/satisfaction of IPA, the min-max method was used to switch the 9-point scale to a 5-point scale as shown in <Table 3-17>.

<Table 3-17> AHP/IPA Survey Statistics

Main Criteria	AHP Weight (a)	Sub-Criteria	AHP Weight (b)	AHP Weight (a*b)	Criteria	Importance Rating		Satisfaction Rating	
						Mean	Rank	Mean	Rank
Policy Feasibility	0.405	Policy Imperative	0.6588	0.2665	PI	5.00	1	3.00	6
		Governance	0.3412	0.1380	GO	1.55	5	3.01	5
Technological Feasibility	0.348	Operational Efficiency	0.6022	0.2098	OE	3.48	2	3.57	1
		Location / Infrastructure	0.3978	0.1386	IN	1.56	4	3.04	4
Economic Feasibility	0.247	Performance	0.6742	0.1666	PF	2.31	3	3.45	2
		Project Execution	0.3258	0.0805	PR	0.00	6	3.34	3
					Aver	2.32	-	3.50	-
					Max	5.00	-	3.57	-
					Min	0.00	-	3.00	-

As shown in <Table 3-17> and [Figure 3-15], the relative importance of policy imperative was the highest, while performance or satisfaction was the lowest. This means that Peruvian government officials and SEZ experts recognized policy feasibility, especially policy imperative, as the most important criteria for selecting SEZs, but most of the SEZs in Peru do not meet these criteria. Therefore, rather than designating special zones in a hurry to achieve policy goals such as balanced regional development, policymakers in charge of SEZs need to select and designate special zones in consideration of technological feasibility factors such as operational efficiency and location/infrastructure, economic feasibility factors such as performance and enforceability of special zones, and the needs of (prospective) tenant companies.

[Figure 3-14] Results of AHP/IPA Survey

6.2. Developing a New SEZ Model: Focusing on Transition from Public to Private

In light of Korea's and other benchmarked countries' experiences, most of countries are establishing special zones primarily in metropolitan areas to enhance international competitiveness. Furthermore, nationwide special zones are being established to promote balanced regional development and nurture local specialized industries. Additionally, incentives are being provided to eliminate discrimination between domestic and foreign companies.

Previously, the special zone system in Korea exhibited discriminatory practices against domestic companies in favor of attracting foreign companies or introducing cutting-edge technologies. However, as Korea's technological powers has advanced, and the promotion of exports and job creation have become common objectives for special zones worldwide, incentives and deregulation are now being applied equitably to both domestic and foreign companies.

Nevertheless, in Korea, while expanding the autonomous operation of SEZs and their tenant companies, the government has introduced a performance evaluation system. This system involves conducting evaluations by external experts to ensure objectivity and comprehensiveness.

6.2.1. Major Considerations for Developing a Sustainable SEZ Model

The development of a sustainable special zone model requires careful consideration of various factors from a long-term perspective. On the one hand, the special zone for attracting investment, increasing exports, and creating jobs is evolving from a traditional model to a new model. For example, the traditional SEZ model in developing countries such as Bangladesh is based on low wages or comparative advantages in infrastructure and is in a suitable location for logistics exchanges, and furthermore the government-led system provides limited incentives to foreign companies. On the other hand, the new special zone model, such as the Suzhou Industrial Park, a joint venture between China and Singapore, promotes large-scale development and operation of private roads under the proper control of the government, facilitates bilateral trade or free trade, and strengthens ties with domestic enterprises (World Bank Group 2011).

The roles of special zones in major countries, which are attracting attention as recent success stories, are changing from static purposes such as job creation, export promotion, increase of national fiscal revenue, and foreign currency acquisition to dynamic objectives such as technology transfer, improvement of workers' skills, innovation of domestic enterprises, diversification of products, and increase of productivity. In particular, as the new special zone is aligned with global megatrends, its status is changing as a test bed for low-carbon green growth, a platform for urban regeneration, an IT-based smart city, and a knowledge business service hub (KIEP 2015).

6.2.2. Core Components of the New SEZ Model

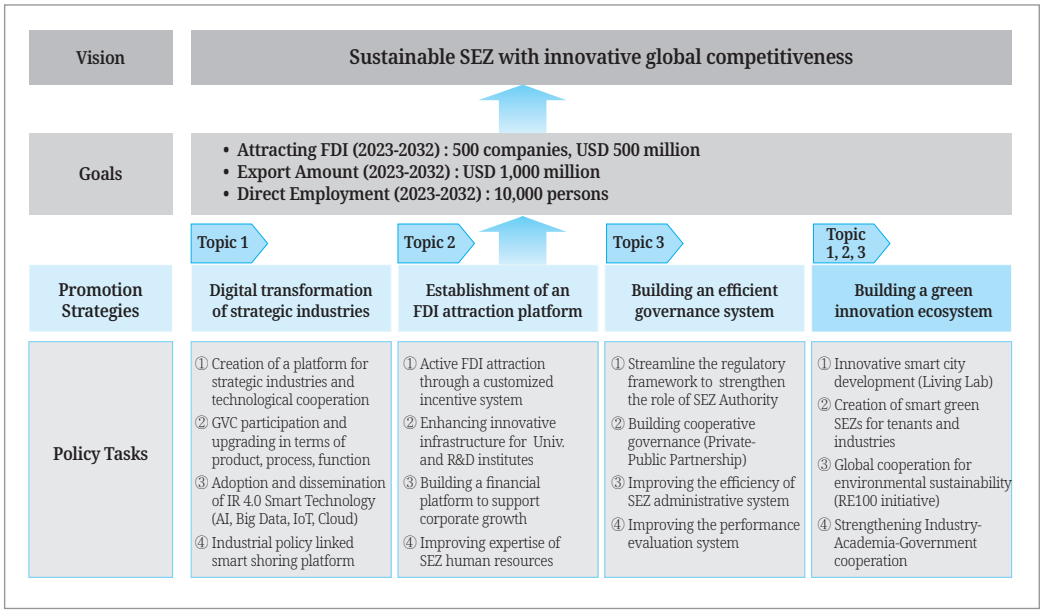
The core components of the new SEZ model are: 1) presenting a new vision, 2) setting clear performance goals, 3) designating and developing SEZ, 4) attracting foreign and domestic investment, 5) building an innovation ecosystem, 6) strengthening the competitiveness of the SEZ, and 7) improving the governance system. Concrete strategies and policy tasks for those components should be specified in the basic master plan for SEZs.

6.2.3. Proposing a New SEZ Model for the Sustainable Development of Peru

Rather than explaining the new SEZ model at length, the KSP team would like to briefly propose a new model that should be reflected in the Basic Plan for the Sustainable Development of the Peruvian SEZs based on the ideas adapted from the draft of Korea's 3rd Master Plan for Free Economic Zones.

Of course, the proposed Master Plan shown in [Figure 3-16] is prepared as an example based on the results of the analysis of the detailed topics. It is hoped that the basic plan will be finalized as soon as possible and used for the sustainable development of the Peruvian Special Economic Zone with the participation of various stakeholders of the Special Economic Zone, including the members of the Peruvian Free Economic Zone Committee, as well as managers of Special Economic Zones, developers, managers of tenant companies, environmental NGOs, and labor unions, etc.

[Figure 3-15] Proposed New Model for Sustainable SEZs of Peru



Source: Adapted from MOTIE (2022).

7. Conclusion and Policy Recommendations

7.1. Conclusion

SEZs have multiple purposes, encompassing economic development as well as facilitating policy innovation and coordination between national and local governments. The development of SEZs and local decentralization can be seen as interconnected concepts. SEZs provide a governance framework where the central government holds legislative authority, but the administrative function is shared with local governments. The distinction between a centrally controlled system and local autonomy, as implied in the discussion about SEZs and legislative competence, could potentially revolve around how the legislative and administrative functions are distributed between the central government and local

government.

In conclusion, this chapter aimed to present more desirable selection criteria and governance system to establish and operate SEZs in Peru more effectively. According to the lessons from the experiences of Korea and other notable cases in advanced countries, and AHP/IPA results, the implications for the successful and sustainable development of SEZs can be summarized as follows:

- Consistent and transparent legal framework and strong support of the central government;
- Creating an attractive investment environment: Making SEZs truly "Special";
- Delicate planning, visualization, and execution;
- Sustainable supplementation of workers' education and high-quality manpower;
- Strategic positioning and strong connectivity;
- Formation of industry clusters including increased connectivity to domestic companies;
- R&D institutes, and universities;
- Harmonious economic and social development by upgrading GVC;
- Performance monitoring, evaluation, and exit system.

7.2. Policy Recommendations

The policy recommendations presented in this final report are primarily divided into five categories. The first is streamlining the legal framework for SEZs. The second is establishing transparent criteria for selection, performance evaluation, and cancellation or exit. The third is enhancing coordination among SEZ-related agencies and their institutional capacity. The fourth is following global standards and pursuing environmental sustainability. The fifth is promoting more active and fruitful economic cooperation between Korea and Peru beyond the Knowledge Sharing Programs.

① **Streamline the legal framework for SEZs:** Instead of designating SEZs based on individual laws, the enactment of the "Special Law on the Designation and Operation of Special Economic Zones of Peru" (tentative title) is recommended. This law would consolidate relevant laws and regulations, streamline administrative procedures, and minimize bureaucratic obstacles.

② **Establish transparent criteria for selection, performance evaluation, and cancellation or exit.** The selection criteria for SEZs should consider political feasibility (policy compliance and governance), technological feasibility (operational efficiency, location/infrastructure), and economic feasibility (performance, project implementation), and need to be explicitly incorporated into laws and regulations. Additionally, a framework for monitoring and evaluating performance should be established to assess the impact of SEZs on investment, exports, employment, economic growth, and regional development. Furthermore, criteria for the cancellation of SEZ designation or the exit of tenants should be developed.

③ **Enhance coordination and institutional capacity:** The designation and operations of SEZs in Peru involve many central government agencies including MINCETUR, MEF, Produce, PROINVERSIÓN, SUNAT and GORE (local governments). Improve coordination among those agencies responsible for SEZ administration to ensure consistent implementation of policies and regulations. Strengthen the institutional capacity of these agencies to effectively manage SEZs, including sufficient resources, expertise, and efficient decision-making processes.

④ **Compliance with global standards and enhancement of environmental sustainability:** Considering global standards, it is essential to incorporate environmental considerations into the governance system of SEZs. This includes implementing stringent environmental regulations, conducting environmental impact assessments, and attracting environmentally friendly businesses to promote ESG (Environmental, Social, and Governance) management.

⑤ **Beyond the Knowledge Sharing Programs:** As Korea and Peru celebrate the 60th anniversary of mutual diplomatic relations this year, both countries recognize that it is crucial to pursue mutual collaboration and identify bilateral and multilateral international development cooperation projects. Furthermore, proactive measures should be taken to promote mutually beneficial economic cooperation, including joint efforts to attract Korean companies to Peru's SEZs and facilitate their expansion in overseas markets.

It is expected that implementing these policy recommendations would improve governance systems in Peru's SEZs, leading to increased investment, economic development, job creation and sustainable growth.

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Appendix

SEZ-Related Laws and Regulations

The legal framework for SEZs in Peru is aimed at promoting private investment and economic development in specific regions and sectors, to generate jobs, increase exports, and promote technological innovation.

Law No. 27688

Free Trade Zone and Commercial Zone Law of Tacna.

Law No. 30446

The law that establishes the complementary legal framework for the Special Development Zones, the Free Zone, and the Commercial Zone of Tacna.

Law No. 30777

The law that modifies provisions on Special Development Zones to facilitate their investments.

Law No. 30976

The law that modifies Law No. 27688, viz. the Law of Free Zone and Commercial Zone of Tacna.

Supreme Decree No. 011-2002- MINCETUR

Regulation of Law No. 27688, Law of Free Zone and Commercial Zone of Tacna.

Supreme Decree No. 002-2006- MINCETUR

Supreme Decree that approves the Single Ordered Text of the Regulation of Law No. 27688, Law of Free Zone and Commercial Zone of Tacna.

General Customs Law and its Regulation

Rules applicable to the operations related to entry, permanence, transfer, and exit of merchandise to and from the customs territory.

Supreme Decree No. 019-2009-PCM

Regulation of Law No. 29014, Law that assigns the CETICOS of Ilo, Matarani, and Paita

to the Regional Governments of Moquegua, Arequipa, and Piura; the ZOFRA Tacna to the Regional Government of Tacna and the ZEEDE Puno to the Regional Government of Puno.

Supreme Decree No. 022-2015- PRODUCES

Supreme Decree that approves the list of merchandise included in the national subheadings corresponding to extractive and/or manufacturing activities concerning which industrial and agro-industrial companies may not establish facilities in the Free Trade Zone and Commercial Zone of Tacna.

Supreme Decree No. 018-2017- MINCETUR

Regulation of Violations and Sanctions of the Law of Free Zone and Commercial Zone of Tacna, Law No. 27688.

Supreme Decree No. 005-2019- MINCETUR

Regulation of the Special Development Zones-ZED.

Supreme Decree No. 015-2019- PRODUCES

Supreme Decree that approves the negative list of merchandise included in the national subheadings, concerning which users may not carry out manufacturing or production activities within the Special Development Zones.

Supreme Decree No. 004-2021- MINCETUR

Supreme Decree that modifies the Regulations of the Law of Free Zone and Commercial Zone of Tacna.

General Procedure DESPA PG.22 (Version 2)

Procedure for the dispatch, transfer, entry, permanence, and exit of merchandise destined for the Special Development Zones.

General Procedure DESPA PG.23 (Version 3)

Procedure for the transfer, entry, and exit of goods to and from ZOFRA Tacna and the Tacna Commercial Zone.

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Sejong Government Complex, 477, Galmae-ro, Sejong-si 30109, Republic of Korea
Tel. 82-44-215-7747
www.moef.go.kr

Korea Development Institute (KDI)
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Tel. 82-44-550-4114
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QIV Corp.
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Tel. 82-70-4221-4409
www.QIV.co.kr

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Tel. 82-42-821-5518
https://meri.re.kr

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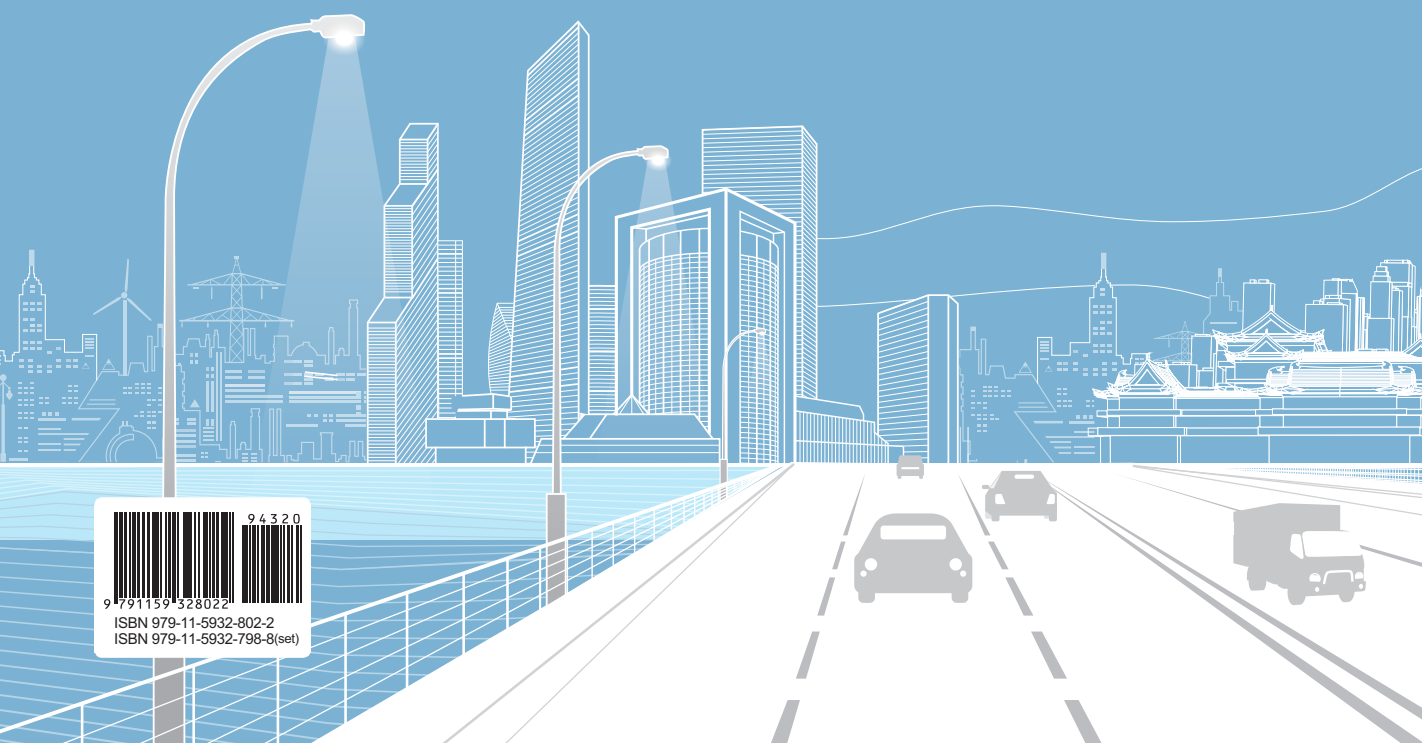

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