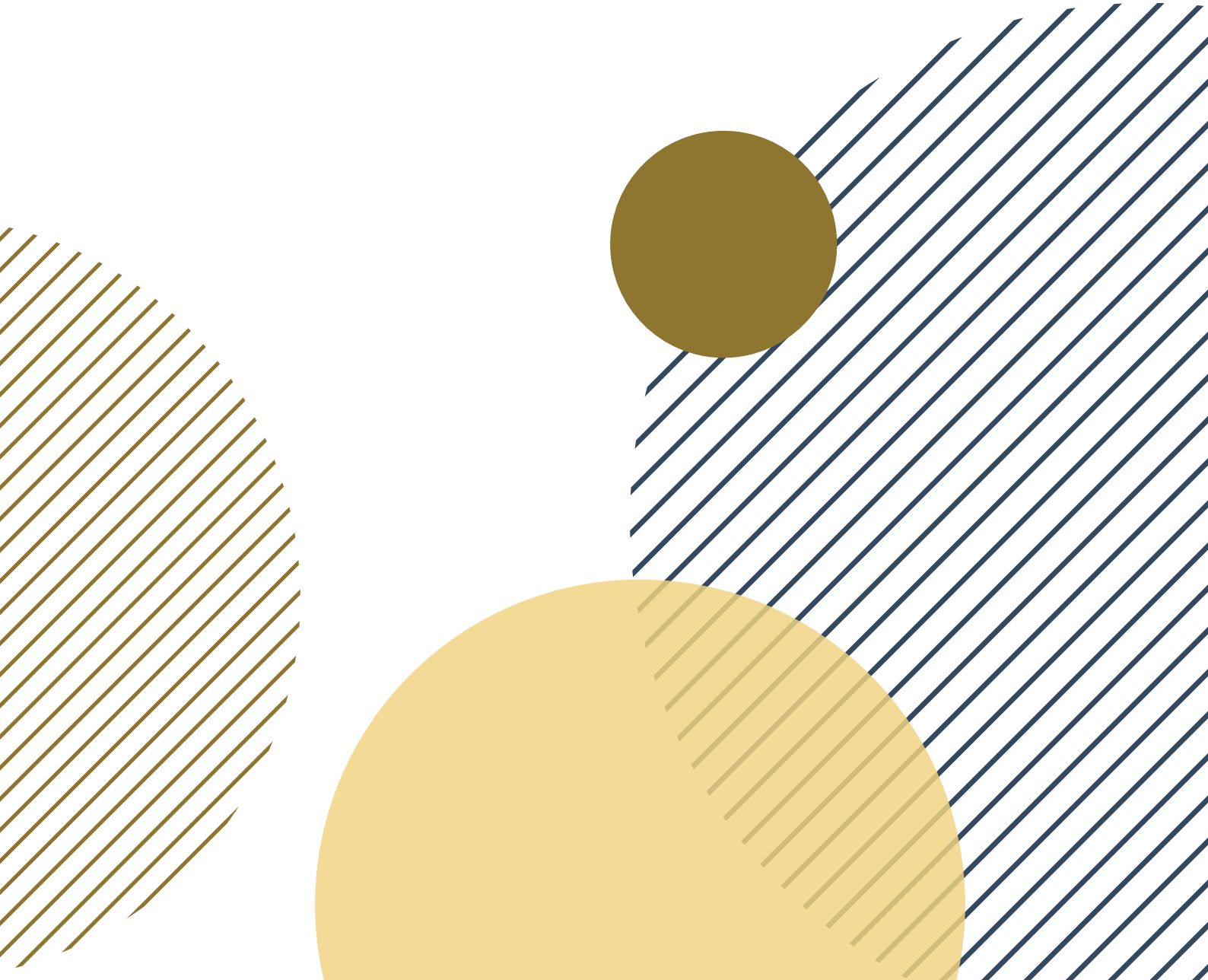
FOREWORD BY DR. MOHAMMED ALZAROONI

WORLD FZO OUTLOOK REPORT 2020

THE WAY FORWARD



WORLD FREE ZONES ORGANIZATION

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OUTLOOK 2020

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ifw KIEL INSTITUTE FOR THE WORLD ECONOMY

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WORLD FREE ZONES ORGANIZATION

World Free Zones Organization Outlook 2020

FOREWARD

2020 began on a note of cautious optimism, with international institutions predicting an uptick in growth. The reality was starkly different. The Covid-19 virus spread across the world and brought in its wake uncertainty, fear and disruption on a scale not seen for generations. In recent weeks, this global pandemic has affected our entire lives, and more specifically, our livelihoods.

Forced to react, governments have taken drastic measures to quell the spread of this disease. Lockdowns, air travel embargos, and emergency stimulus packages have impacted every economy on the Global Value Chain. Central banks are adapting their monetary policies and expanding liquidity, possibly at the cost of severe inflation in the near future. The World Trade Organization predicts that the slowdown will be on a scale reminiscent of the Great Depression of the 1930s. Consumption is dropping fast, a natural consequence of national lockdowns and confinement policies. Fiscal revenues are likely to fall, putting pressure on tax incentives of any sort. These are unprecedented times.

Free zones have not escaped this global disruption. However, their special status and distinct structures can help them weather this pandemic storm in unique ways. By putting clear strategies in place to manage their risk palette, from production to market and trade threats, free zones can emerge stronger and leaner from this crisis.

To offer guidance and support in these difficult times, the World Free Zones Organization, as the apex global representative body of free zones everywhere, has put together this Outlook 2020 report in collaboration with the Kiel Institute for the World Economy.

I am pleased to present in this report a snapshot analysis of the global economic environment, as well as the first results of our Business Excellence and Economic Contribution Survey launched in 2019. This is built on our database of free zone activity worldwide, tracking free zone performance and contributions to their host economies. The Outlook 2020 report also contains summaries of economic prospects and trends in free zones using its proprietary Free Zones World Economic Barometer (F-WEB), a quarterly, survey-based sentiment indicator. In fact, a special F-WEB survey was carried out at the end of March 2020, specifically focused on the channels through which the pandemic affects free zone economic performance.

Together, these insights form a bank of unique free zone knowledge and recommendations that can point the way forward in these troubled times.

Our strategy has always been to look ahead. This is why we have developed a range of certification programs and a palette of exclusive tools for free zones to thrive in any environment. From our Safe Zone certification to our Izdihar Index, together with our Free Zone of the Future initiative (Free Zone 4.0), these programs will form a new set of global standards for free zones to emulate and embrace, for the benefit of all their stakeholders around the world.

We will emerge stronger from this crisis. Free zones will build resilience. They will strengthen their frameworks. Together, we will help all free zones to rise to the occasion and grow more able to do business in challenging environments. This is the beginning of a new phase, with a whole new outlook on the world.

Let us come together to overcome this adversity and defeat this global threat.

Dr Mohammed Al Zarooni

Chairman

World Free Zones Organization

WORLD FREE ZONES ORGANIZATION

Content

1 Global Economic Environment

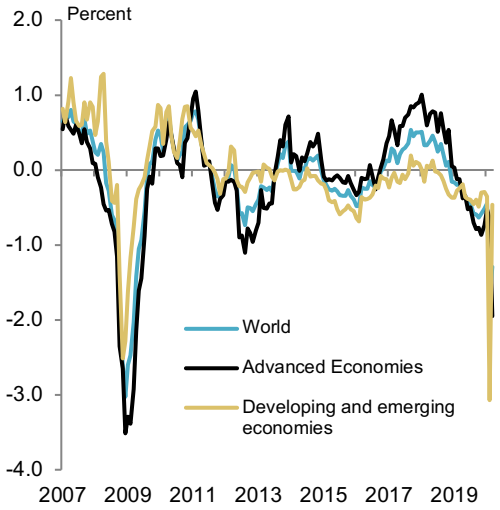
1.1 Overview

In spring 2020 the world economy is severely affected by the consequences of a novel coronavirus and the measures implemented to arrest its spreading. Tentative signs of a strengthening of global growth at the turn of the year have turned around in February with the implementation of wide-ranging measures in China to contain the COVID-19 disease associated with the virus. Initial hopes that it would be possible to stop the wave of infections in China and that the economic consequences would be largely confined to Asia proved illusionary as the virus started spreading globally. In order to slow the process of contagion, measures are taken almost everywhere and they strongly reduce economic activity. Uncertainty over the economic outlook is extremely high, additionally weighing on demand. As a result, the world economy is poised for a recession in 2020 which is only comparable to the economic downturn in the wake of the Global Financial Crisis.

Economic sentiment has dropped dramatically. Sentiment, as measured by the ***Kiel Institute-Indicator for World Economic Activity*** calculated by the Kiel Institute for the World Economy, had been on a declining trend since early 2018 led by weakening sentiment in advanced economies (Figure 1). A tentative improvement around the turn of the year, that seemed to herald a gradual acceleration of global growth in early 2020, ended abruptly when sentiment in China collapsed in February reflecting harsh measures taken to contain the spread of COVID-19. While sentiment indicators outside Asia remained strong in February – as did stock markets which rose to new records in Europe and the US despite the disturbing news from China –, the situation turned around in March. At that time, it became clear that the coronavirus had spread globally and more and more countries reacted with increasingly restrictive measures to contain the pandemic. Sentiment plummeted at a record pace in advanced economies to levels seen only in the Great Recession 2009. A glimmer of hope is the strong rebound in Chinese sentiment already in March, which drives the development of the indicator for emerging economies. It should be noted, however, that it reflects an upturn in production from extremely depressed levels. Moreover, it

seems unlikely that confidence in other countries will recover at a similar speed given that COVID-19 is still not under control in most of the rest of the world. On a quarterly basis, the Kiel Institute Indicator for World Economic Activity signals strongly declining global growth momentum for 2020Q1 (Figure 2). ***However, most of the negative impact of COVID-19 will probably become visible only in the second quarter as the economic consequences of the pandemic outside China were only starting to be recognized towards the end of the first quarter.***

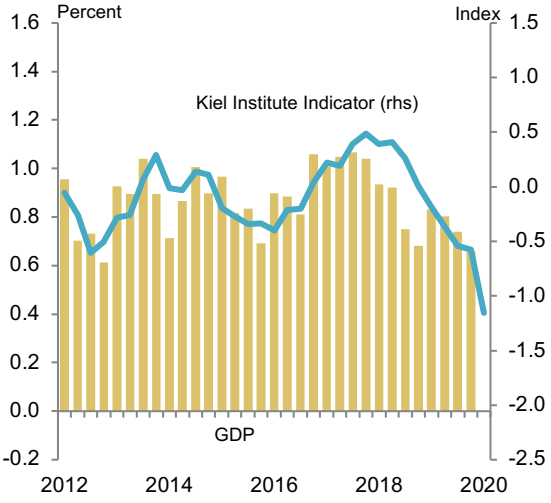
Figure 1: Business expectations by groups of countries, 2007-2020



Notes: Monthly data, seasonally adjusted. Indicators are based on buisness expectations in 42 countries (34 advanced economies and 8 emerging economies).

Source: OECD, *Main Economic Indicators*; national sources; Kiel Institute calculations.

Figure 2: World Economic Activity, 2012–2020



Notes: Quarterly data, seasonally adjusted. Indicator is based on business expectations in 42 economies. GDP: price adjusted, change over previous quarter, 46 countries, weighted by purchasing power parities.

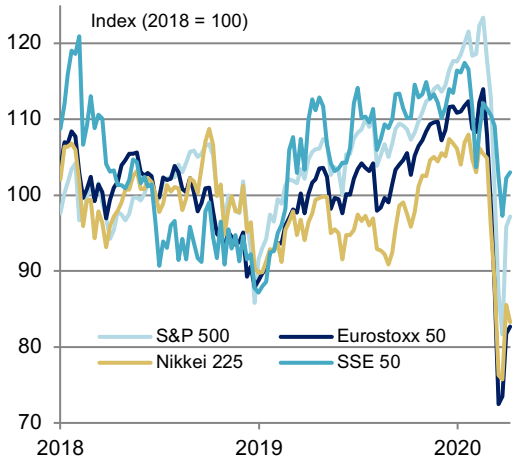
Source: OECD, *Main Economic Indicators*; national sources; Kiel Institute calculations.

The COVID-19 pandemic hits the global economy in a situation when growth was already subdued. World output had progressively lost momentum throughout 2019. In the fourth quarter, growth was weak particularly in advanced economies, with stagnating economies in the euro area and the UK, and a significant contraction in Japan due to negative effects of a typhoon and an increase of the value-added tax. While the US economy continued to expand on the back of robust private consumption, growth was moderate and investment showed signs of weakening. By contrast, emerging economies, which experienced a period of sluggish growth in 2018 and much of 2019, appeared to have picked up towards the end of the year. GDP growth in Asian emerging economies in general, and in China in particular, accelerated on a sequential basis. In addition, countries emerging from recessionary episodes such as Brazil and Turkey registered a notable pickup in activity.

Financial markets have turned bearish. After an initial period of apparent neglect, stock markets in the US and Europe declined steeply, by up to 40 percent from the historically high levels reached in mid-February (Figure 3). Most emerging economies also saw stock prices decline markedly, and their currencies came under devaluation pressure (Figure 4). Emerging markets recorded substantial capital outflows during February and March as a result of a flight to safety by international investors. According to the IMF, by the end of March investors had withdrawn 83 billion US dollars from emerging markets since the beginning of the coronavirus crisis, which is the largest capital outflow on record.[1] Conversely, yields of safe haven government bonds such as US-treasuries or German Bunds revalued markedly, although some reversal took place in recent weeks.

[1] See IMF Managing Director Kristalina Georgieva's Statement Following a G20 Ministerial Call on the Coronavirus Emergency (23 March 2020).

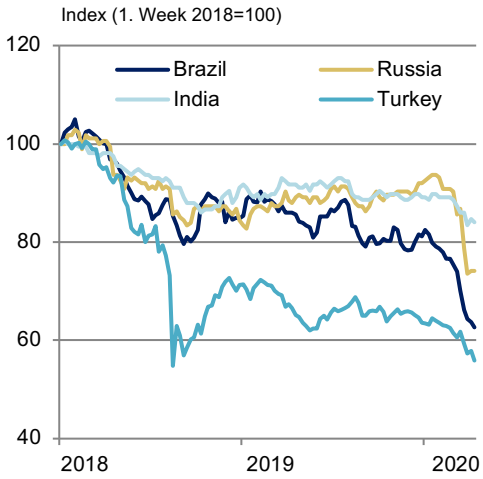
Figure 3: Stock prices in selected markets, 2018-2020



Notes: Weekly data, last observation 6.4.2020.

Source: Thomson Reuters, Datastream

Figure 4: Selected emerging economy US-$ exchange rates, 2018–2020

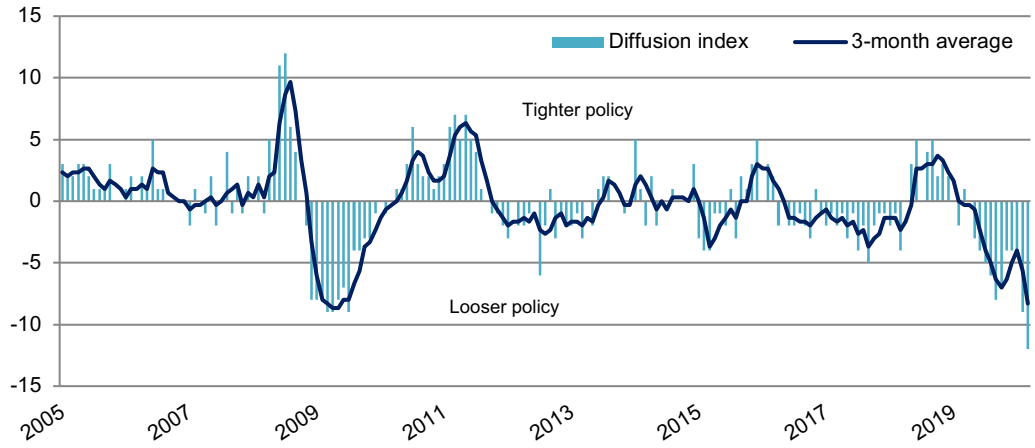


Notes: Weekly data. Last observation: 6.4.2020.

Source: Thomson Reuters, Datastream.

Monetary policy has been eased. Traditional tools of macroeconomic demand management cannot prevent that COVID-19 and the measures to contain the pandemic lead to a substantial reduction of economic activity. However, appropriate policy responses can help that – what is expected to be – a temporary decline in business activity does not lead to persistent scars in the real economy due to a wave of bankruptcies and unnecessary large job losses. Monetary policy can secure ample liquidity in the financial sector in order to facilitate credit to the non-financial sector and reduce financing costs to help ease liquidity constraints. To that end, the US central bank has reduced the target range for the Federal Funds Rate from 1.5-1.75 percent to 0-0.25 percent and provided massive amounts of additional liquidity to the financial sector. Interest rates have also been cut in Australia, Canada and the United Kingdom to close to zero. In Japan and in the euro area, where interest rates are already at or below zero, measures were concentrating on further increasing market liquidity and containing the rise in risk premia by targeted asset purchases. In emerging economies, the trend towards lower policy rates continued (Figure 5). The potential for further interest rate reductions may, however, be limited by the increased risk aversion of investors in the international capital markets, especially in countries that depend on sizable capital inflows to finance current account deficits.

Figure 5: Monetary policy in emerging economies



Notes: Monthly data. The diffusion index is the number of central banks raising policy rates less the number of central banks decreasing policy rates in a given month. Emerging markets included are: Argentina, Brazil, Chile, China, Colombia, Indonesia, India, Mexico, Malaysia, Peru, Philippines, Russia, Thailand, Turkey, South Africa.

Source: Bank of International Settlements (BIS); Kiel Institute calculations.

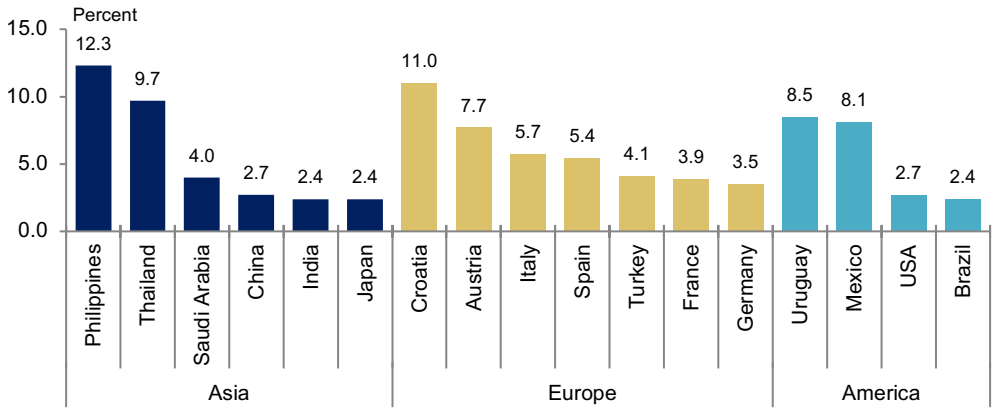
Governments are putting together fiscal packages to support the economy, often of unprecedented dimensions. Fiscal measures designed to cushion the blow to the economy include direct support of businesses, credit guarantees and income support to workers and self-employed. Governments around the world are revising their budgets and implementing fiscal packages which often are unprecedented in size. For example, the US authorities introduced a 2 trillion US dollar stimulus bill in response to the COVID-19 crisis, and comparable initiatives in Europe amount to a similar size. As a result, fiscal policy in the advanced economies will be strongly expansive in 2020. Fiscal policy in emerging and developing countries are often more constrained, but international organization have pledged substantial funds to support these countries in their efforts to deal with the pandemic.

Length and depth of the global economic downturn depend on the further evolution of the pandemic and the measures that will be necessary for its containment. The tougher the measures for containment, the bigger the chances that the current wave of the pandemic will run out soon, but the larger will likely be the negative short-term impact on the economy. Initially, draconic measures of the Chinese government to contain the disease led to a sharp decrease in production in China with a substantial negative impact on the global economy in general, and Asian

economies in particular, through a reduction in goods trade and tourism. As COVID-19 spread globally, more and more countries experience substantial limitations to economic activity due to anti-pandemic measures of their own.

In contrast to normal recessions, economic activity is particularly affected in a number of service industries. Cyclical fluctuations of economic activity on the macroeconomic level are typically driven by fluctuations in capacity utilization of the industrial sector. In the case of the COIVD-19 crisis, however, also large parts of the service sector are directly hit, including transport, accommodation and restaurants, recreational facilities and parts of retail trade. All these services involve social interaction to some extent, which is reduced in the current situation as a result of administrative instructions or voluntary changes in behavior in order to reduce the risk of infection. Tourism is already hit strongly, and it can be expected that activity in this sector will remain depressed for a relatively long period of time even in the case of a V-shaped recovery. Hence countries with a high share of economic activity directly attributable to tourism can be expected to experience a relatively slow rebound. Such countries include the Philippines or Thailand in Asia; Croatia, Greece, Italy or Spain in Europe; Uruguay and Mexico in the Americas, but also (and especially) many smaller countries (Figure 6).

Figure 6: Contribution of tourism to GDP in selected countries, 2019

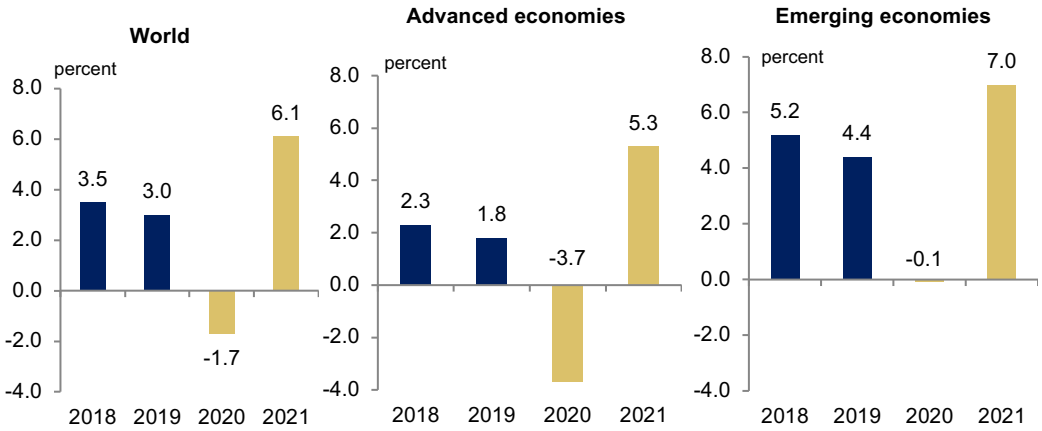


Note: Direct contribution to GDP calculated as contribution to gross value added in sectors leisure and hospitality, transport, and retail sales.

Source: World Travel and Tourism Council.

A global recession is almost inevitable, but a V-shaped recovery is likely, provided that the COVID-19 pandemic is contained in the coming months. International organizations have withdrawn their most recent forecasts for GDP growth in the world economy and indicated that they would revise downwards drastically as the negative short-term impact of the measures to contain the pandemic is found to be massive. Under the assumption that it will be possible to get COVID-19 under control within a couple of months, the global economy should normalize from mid-year onwards resulting in a swift rebound of activity. Monetary policy has already been eased and fiscal measures are being put in place to support the economy. Even in this scenario, however, global growth in 2020 as a whole would be negative despite strong rates of growth in the second half of the year on a sequential basis, according to the latest assessment of the Kiel Institute. In 2021, assuming a progressive recovery of economic activity over time, global output could rise by around 6 percent (Figure 7).

Figure 7: World economic output growth by country group 2018-2021



Note: Real GDP, based on PPP-weights. 2020-2021: forecast.
Source: IMF, Kiel Institute for the World Economy.

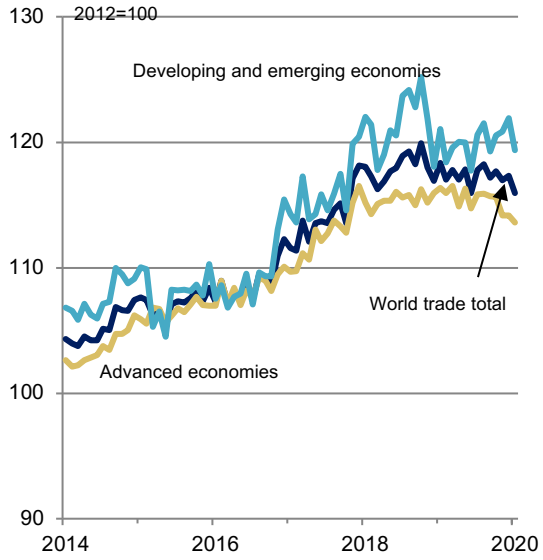
There are substantial downward risks to growth related to the uncertainty regarding the success of stemming contagion. Less benign assumptions about the development of the pandemic lead to more negative outcomes for the world economy with different profiles of economic activity. In case that restrictions on economic activity would need to be more persistent, the economy would take longer to recover, resulting in a U-shaped path for GDP. W-shape developments in the business cycle could materialize in case that repeated waves of infections occur.

Other downward risks pertain to a potential increase of financial stress. The economic downturn could be reinforced by financial feedback loops, leading to liquidity problems in the corporate sector, progressively rising risk premia in certain sovereign debt markets, or rising savings rates in response to lower asset valuations. Continuation of capital outflows could lead to a severe tightening of financial conditions in (some) emerging economies. Similarly, commodity producers, which are currently under additional strain due to the stark drop in raw material prices, could face more adjustment pressures, especially if oil prices remain on their current extremely low levels.

1.2 World Trade

World trade remained weak throughout 2019. According to the figures compiled by the Netherlands Bureau for Economic Policy Analysis (CPB), trade of goods in volume terms declined by 0.4 percent in 2019 compared to 2018 (Figure 8). World trade was sluggish against the backdrop of the trade conflict between the US and China, which led to a strong decline of trade between the world's two largest economies (Figure 9) and impacted negatively on activity elsewhere, partly through increased policy uncertainty. January figures for world trade show a significant drop as COVID-19 started to impact on the Chinese economy and US exports dipped.

Figure 8: World trade volume, 2014-2020



Notes: Monthly data.

Source: CPB, *World Trade Monitor*; Kiel Institute calculations.

Figure 9: US-China bilateral exports, 2014–2020

Notes: Monthly data; year-on-year changes.

Source: US Census Bureau, China Customs.

The Phase-1 trade deal between the US and China has reduced the risk of further escalation in the trade conflict, but is not expected to improve the environment for global trade significantly. 2019 was characterized by a ratcheting up of the US trade conflict with tit-for-tat tariff increases finally poised to cover virtually all of Chinese exports to the US and the major part of US exports to China. The final stage of the tariff increases scheduled for December was, however, put off as negotiations on a trade deal proceeded. The US-China Economic and Trade Agreement (ETA), also known as Phase-1 trade deal, was enacted on 14th February 2020, marking a new phase in the US-Chinese trade relations. The ETA includes specific targets for increased Chinese imports of US goods and services amounting to 200 billion US dollar over 2020 and 2021 compared to the 2017 level. The targets for the increase of Chinese imports from the US are ambitious, especially in light of the economic slowdown due to COVID-19, and most of the newly imposed tariffs remain in place until it is clear that they will be reached. Thus, uncertainty remains substantial at least until agreement on a more comprehensive Phase-2 trade deal is reached, which is far from certain as a number of contentious issues are on the agenda.

The purchase commitments made in the US-China trade deal can generate substantial trade diversion effects and lead to significant market share shifts for China's top trading partners. Additional imports on top of the 2017 baseline envisaged by ETA amount to 32 billion US dollar in agricultural products, 77.7 billion US dollar in manufacturing and 52.4 billion US dollar in energy. Much of these incremental imports from the US will not be additionally imported by China. Instead, they will come at the cost of traditional suppliers of these kinds of goods (trade diversion not trade creation).[2] In manufacturing, Germany, Japan and Korea stand to lose most as the hitherto most important suppliers of vehicles, aircraft and industrial machinery. In energy products, Russia and Australia are likely to be most affected as important suppliers of crude oil and coal to China. In the agricultural sector, Brazil will be particularly hit amongst China's top trading partners mainly due to lost exports in soybeans. A recent World Bank study finds the impact of the trade deal to be potentially negative for most countries except the US, with losses relative to national income particularly large in the East Asian region and Latin American countries

[2] For details see Chowdry and Felbermayr (2020).

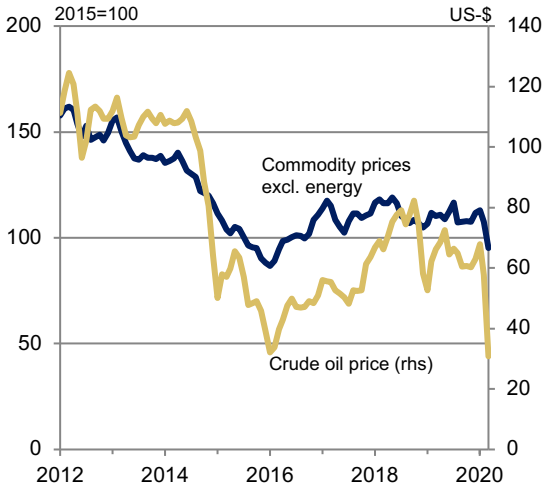
(Freund et al. 2020). The welfare effects, however, depend on how the trade deal is implemented by China. If China were to achieve the targeted increase in imports from the US by a multilateral approach, i.e. a significant reduction of tariffs across the board, this would make everybody but the US better off, including China.

Meanwhile trade tensions between Europe and the US have intensified. In autumn 2019 a pending trade conflict between the US and the European Union heated up as the US raised tariffs in response to illegitimate Airbus subsidies by the European Union following a WTO ruling in October. Further protectionist measures were proposed as a reaction to a planned digital tax by the French government. While the Trump administration so far has not followed through on its threat to impose tariffs on automotives and auto parts from Europe, uncertainty around this issue remains as well, with potential consequences for production processes that are organized along global value chains.

1.3 Commodity markets

The COVID-19 crisis has depressed commodity prices. Commodity prices declined significantly almost across the board in response to the strong reduction of economic activity in China due to measures to contain the coronavirus (Figure 10). China is the most important consumer of commodities worldwide; in the case of a number of non-ferrous metals the share of China in global demand is in excess of 50 percent. In March, the escalation of the COVID-19 crisis in advanced economies put commodity prices under renewed pressure. Quotations for copper – a key indicator for market sentiment in the markets for industrial commodities – declined by more than 20 percent since January.

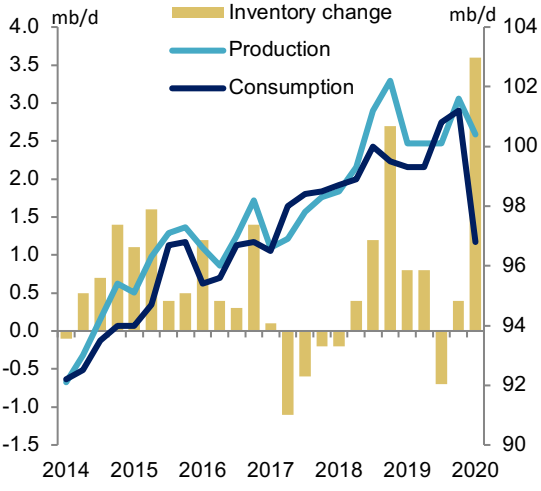
Figure 10: Commodity prices, 2012-2020



Notes: Monthly data; commodities prices without energy: HWWI-index based on US dollar; oil price: Spotpreis Brent.

Source: International Petroleum Exchange via Thomson Reuters Datastream; HWWI, Commodity Price Index.

Figure 11: Oil market balance, 2014–2020



Notes: Quarterly data, million barrel per day. Inventory change calculated as difference of production and consumption. First quarter: forecast.

Source: International Energy Agency, Monthly Oil Market Report, Kiel Institute calculations.

Oil prices dropped to multi-year lows amid lack of consent among major producers to reduce production. The price for crude oil initially fell from close to 70 US dollar to around 50 dollar per barrel (Brent) in response to declining demand from China and the resulting huge inventory built-up expected for the first quarter (Figure 11). In early March, the OPEC failed to find agreement with Russia to reduce production quotas further. In response, Saudi Arabia announced to increase production to its capacity limits which led to a collapse of the oil price to close to 20 dollar for Brent (and even below 10 dollar for some other varieties). In early April, signals were building that OPEC-plus would finally be able to agree on a concerted reduction of output, and oil prices regained some ground. However, with economies in widespread lockdown in many countries, including in the US and Europe, fuel demand is declining steeply and could fall below the previous year's level by as much as 25 million barrel per day, which is an order of magnitude that cannot possibly compensated by OPEC-plus output cuts, according to the assessment of the International Energy Agency (IEA).[3] The further development of the oil price will depend on the timing and strength of the economic recovery and the decisions on and credibility of production quota for the foreseeable future.

[3] See IEA: OPEC Can't Save The Oil Market, published on 03.04.2020.

1.4 Outlook for Individual Countries and Regions

The record-breaking spell of economic expansion in the United States is being stopped abruptly. Throughout 2019, the US economy continued to grow, and in July the upturn became the longest on record with 121 months of uninterrupted growth. In the course of the year, growth decelerated as the impact of the strong fiscal stimulus of the previous year faded and external demand was sluggish. Overall, real GDP rose by 2.3 percent following 2.9 percent in 2018. Signs of weakness emerged in investment, whereas private consumption appeared to be robust amid steady employment growth and unemployment at 50 year-lows. The situation turned dramatically to the worse, however, as the coronavirus spread progressively in March and more and more measures had to be taken to prevent the number of infections from spiraling out of control. Unemployment is rising at a record pace with 10 million new applications for unemployment insurance in the last week of March and the first week of April alone. Although monetary policy has been eased and a fiscal package of historic dimensions was launched to support income of workers and the solvency of firms, the economy is poised to contract substantially in the first half of 2020. Even with a progressive recovery in the second half of this year, GDP will fall considerably for the year as a whole. Under the assumption that COVID-19 can be contained in the next couple of months and new waves of the disease can be prevented, the normalization of economic activity should result in a strong rate of growth next year. Although the industrial sector is not at the heart of the economic contraction as social distancing measures primarily affect service industries, manufacturing output is expected to also decline substantially as demand for many products falls and disruptions of production through interrupted value chains may occur.

Output in China fell sharply due to the COVID-19 crisis, but has already started to recover. In the first quarter of 2020, economic activity in China was massively affected by measures to contain the coronavirus. Up to 77 million people were temporarily in quarantine (5.5 percent of the population) and around 500 million people were severely restricted in their mobility. In January/February sentiment indicators dived, industrial production fell by 13.5 percent year-on-year, exports declined by 17.2 percent and retail sales dropped by 20.5 percent. In March, however, the pace of new infections with COVID-19 slowed dramatically according to official numbers and

restrictions on production and mobility were gradually eased. As a result, production has started to pick up according to a number of high frequency activity indicators such as traffic, transport volume or energy consumption, and measures of sentiment have rebounded. However, economic activity is still far from normal with many social services still restrained and an almost complete ban on international travel remaining in place. The recovery of manufacturing will also be inhibited by a lack of demand from abroad where the crisis is still unfolding. As a result, GDP growth in 2020 will drop to the lowest level since the transformation began in the late 1970s even under the assumption of a rapidly normalizing economy in the second half of the year.

Deep recession in Europe will take time to be overcome. A number of European countries are among the countries hit hardest by the COVID-19 pandemic, with strong pressure on medical systems and harsh containment measures implemented in response. In Italy and Spain, production has been stopped altogether except vitally important sectors. As the European economies are strongly integrated, this will also affect output in other countries via production chains. Thus, the immediate decline of GDP during the crisis is expected to be relatively large in Europe by international comparison. Moreover, tourism accounts for a relatively large share of the economy, especially in the Mediterranean countries but also in Austria, France and the United Kingdom. Tourism-related activities will be slow to restart and are expected to take relatively long to recover to their pre-recession levels. While the increase of unemployment will be contained by extensive use of short-time work schemes (government-subsidized in-job unemployment), this will come at a substantial fiscal cost and risks compromising fiscal sustainability in some countries with already high public debt. A debate on how to deal with the fiscal burden imposed by the crisis in the European Union has just begun.

The Indian economy faces the next serious challenge. In India**,** the government imposed a nationwide lockdown for three weeks in response to rising numbers of infections with the novel coronavirus. Even if this measure proves successful, it will lead to a strong decrease in production in the spring quarter of this year. The corona-crisis will obstruct what has looked like a tentative recovery from a period of sluggish growth due to a crisis in the shadow banking sector, which led to a dramatic decline of credit from this source. In 2019, Indian GDP is estimated to have increased by just 5 percent, the lowest rate of growth since 2008. However, in February, just before COVID-19 hit the country, the composite Purchasing Manager Index compiled by HIS

Markit had risen to its highest level in eight years suggesting that a recovery of private sector activity had finally picked up speed. When production will recover and at what speed will depend on the evolution of the pandemic and the measures necessary to contain it. Economic confidence will probably take time to rebuild. Additional risks are associated with the need to attract foreign capital to finance the chronic current account deficit which might prove difficult in the current environment of increased uncertainty.

The Latin American economy is in the doldrums for a number of years already. In Latin America the coronavirus is currently spreading progressively although from a relatively low base. Measures to contain the disease are increasingly affecting activity. Substantial damage of the COVID-19 pandemic is also inflicted on the Latin American economies by the strong decline in demand for commodities, the main export goods of this group of countries, and the associated fall in commodity prices. A number of countries, including Mexico, are also strongly hit by collapsing tourism revenues. Capital outflows have put additional downward pressure on Latin American currencies which have declined in value against the US dollar by 25 percent in the case of the Mexican peso and 20 percent in the case of the Brazilian real. Argentina is in a particularly difficult position with respect to external debt sustainability, according to an assessment published by the IMF in February that a debt restructuring would be unavoidable. All in all, a recession in 2020 seems likely in the region even if COVID-19 would be quickly contained.

The outlook for the MENA region (Middle East and North Africa) is clouded by COVID-19, low oil prices and insufficient progress in structural reforms. The coronavirus pandemic hits the MENA region through different channels. Impediments to domestic production stemming from measures to contain the disease combine with a strong reduction in international travel and tourism which affects a number of countries substantially, including Egypt, Tunisia, Morocco, Jordan and the United Arab Emirates. Also in Saudi Arabia the direct contribution of tourism to GDP is significant (4.0 percent in 2019) mainly due to the large number of pilgrims visiting Mecca and Medina. There is a strong possibility that Hajj will be cancelled this year over fears that the coronavirus would spread. Reduced demand for oil and extremely low oil prices are an additional burden for oil producers which generally need much higher oil revenues to finance government expenditures and balance the current account. The COVID-19 crisis hits the region in a period of already subdued growth. GDP in 2019

grew by only 0.6 percent, according to World Bank estimates, much less than needed to create enough jobs for the rapidly growing work force. Part of the weakness was due to the carbon sector as oil production was curtailed to support the oil price (and due to US sanctions in the case of Iran). Growth outside the oil sector was generally more robust and non-oil exporters registered relatively strong increases of GDP (around 5.5 percent in the case of Egypt). The situation is particularly challenging in Iran, where oil exports have collapsed after the re-introduction of US sanctions. Thus, oil production is down by 30 percent and GDP contracting by an estimated 8 percent. Structural rigidities and elevated government debt limiting the fiscal space to raise social and infrastructure expenditures remain major obstacles to improve the growth potential of the economies in the region in the longer term.

A fragile recovery of the Turkish economy will end for the time being. The Turkish economy strengthened markedly in the second half of 2019, with GDP in the fourth quarter growing at the quickest pace in nearly two years. Growth was mainly driven by surging domestic demand amid increasing private consumption in response to lower interest rates and increased access to credit. Accelerating growth was, however, accompanied by strong import growth while exports increased only modestly, which pushed the current account deficit back into the red. Early indications for the first quarter of 2020 were pointing to another strong outturn – before the COVID-19 pandemic. In recent weeks, after a period of initial neglect, the government intensified measures to contain the disease which will weigh on activity in the coming weeks. In addition, the tourism sector, a major pillar of the Turkish economy, will suffer a decline, which will most likely be more persistent than the limitations on production in the rest of the economy. Downward pressure on the Turkish lira is also indicating renewed loss of confidence in the economy.

Growth in ASEAN countries will take a hit from reduced demand for manufacturing goods and slumping tourism. Against the backdrop of weakness in China and sluggish world trade, economic growth in the region slowed in 2019 from 5.3 percent in 2018 to below 4.5 percent (ASEAN-5). The slowdown was particularly pronounced in Thailand with GDP growth down to only 2.4 percent for the year, as agricultural output decreased amid drought conditions and tourism faltering as the number of Chinese visitors fell. The COVID-19 pandemic is affecting ASEAN countries as well, although so far to a lesser degree than elsewhere as far as the number of confirmed infections and corona-related deaths are concerned. The expected severe

global manufacturing recession as well as lower commodity prices will nevertheless reduce growth dramatically. Another important negative is the drastic decrease of international travelers to which a number of ASEAN countries is particularly exposed, including Thailand, the Philippines and Cambodia.

Risks for growth in sub-Saharan Africa increase amid COVID-19. In 2019, GDP growth in sub-Saharan Africa was steady at 3.2 percent, according to IMF estimates, although with a wide range of outcomes across countries. Oil exporters were generally underperforming, with declining GDP in Angola and Equatorial Guinea and sluggish growth in Nigeria, as OPEC quotas were reduced and the economies are still in the process of adapting to lower oil prices after the boom years up to 2014. South Africa also continued to grow only slowly and even fell into recession towards the end of the year amid infrastructure bottlenecks and escalating problems with power outages which hampered manufacturing production and mining output. At the other end of the spectrum, a number of countries in West Africa (such as Cote d'Ivoire, Ghana and Guinea) and East Africa (especially Ethiopia, but also Kenya and Tanzania) registered substantial economic growth of up to 10 percent. The COVID-19 pandemic is a particularly difficult challenge as the medical system in many countries is weak and social distancing is not a feasible option for a large part of the population. Growth will be hit by lower external demand for locally produced goods and a decrease in tourism. Lower commodity prices and increased risk aversion of international investors may lead to financial stress in some countries. While countries' ability to mitigate the shock by implementing fiscal support measures are limited in many cases, international organizations have pledged substantial funds to support disease-related policies, including an IMF 50 billion US dollar rapid-disbursing emergency facility, which includes 10 billion dollar on highly concessional terms for low income countries.

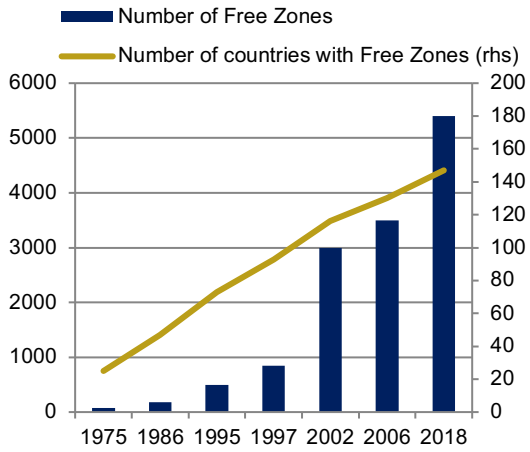
2 The Business Excellence and Economic Contribution Survey

2.1 Introduction

Around the globe, Free Zones have become an increasingly popular instrument of industrial policy. The number of Free Zones has risen considerably over the past decades. According to the most recent estimations provided by UNCTAD (2019), there are currently more than 5,000 Free Zones in over 140 countries, up from less than 200 in the 1980s (Figure 12). Most of them are concentrated in China, but more and more Free Zones are established in all regions of the world (Figure 13) . There is a wide range of different types of Free Zones and an even wider range of terminology used to describe them – “Free Zone”, “Special Economic Zone”, “Economic Zone”, “Free Trade Zone” and many more. The World FZO uses the term “Free Zone” and defines it as an area designated by one or more government(s) where economic activities – whether production or trade, physical or virtual with respect to goods, services or both – are permitted and relieved (totally or partially) from customs duties, taxes, fees or regulatory requirements that would otherwise apply.

More research is needed to identify success factors of Free Zones and evaluate their economic contribution. Despite the veritable Free Zone “boom”, surprisingly little is still known about economic activities carried out in Free Zones, their performance, and their contribution to and impact on the wider economy of the host country. Attempts to evaluate the success of Free Zones often rely on case studies while systematic cross-country analysis has been hampered by insufficient availability of cross-country data to measure Free Zone outcomes. However, this information is critical for the design and implementation of Free Zones, for example to identify success factors for investment attraction.

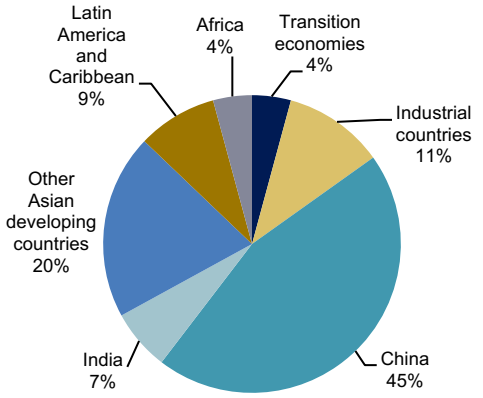
Figure 12: **Global development of Free Zones**



Note: Single Factory Free Zones, i.e. single firms that have SEZ status, are not included.

Source: Boyenge (2007), estimates by UNCTAD (2019) for 2018.

Figure 13: Geography of Free Zones



Note: Industrial countries: Europe, North America, Australia, Isreal, Japan, New Zealand. Transition economies: Countries in Eastern Europe, Central Asia as well as Russia.

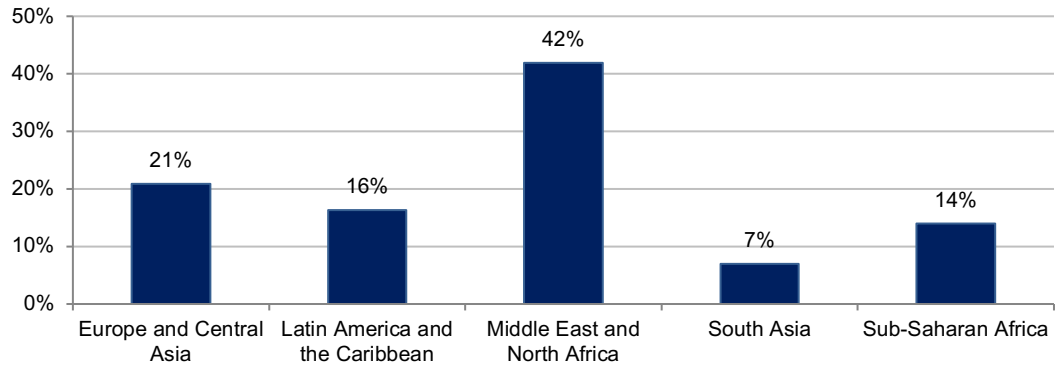
Source: UNCTAD (2019).

To address the existing data gap, the World FZO launched the Business Excellence and Economic Contribution – in short: BEEC – survey. The BEEC survey collects information on the main characteristics and incentives of Free Zones around the globe and gathers data on economic indicators such as investment and employment. The resulting set of Free Zone data will enable the analysis of the structure and developments of economic activity in Free Zones around the globe along various dimensions. It is also possible to compare developments in Free Zones with those in the general economy. The data is designed to deliver information relevant to evaluate policy decisions or inform policy initiatives. Needless to say, the BEEC survey can only reach its full potential if a large enough subset of Free Zones participates in the survey on an annual basis. In this chapter, we provide descriptive results of the first BEEC survey conducted in 2019. Deeper analyses, for example on the success factors of investment attraction, will become possible over time with regular participation of an increasing number of Free Zones.

2.2 Characteristics of BEEC Free Zones

Free Zones from over 20 countries representing 600,000+ employees and 45,000+ firms participated in the BEEC Survey 2019. The largest number of participating Free Zones is located in the Middle East and North Africa (MENA), with a share of 42 percent of all participants, followed by Europe and Central Asia with 21 percent (Figure 14). The number of Free Zones from Latin America and the Caribbean and Sub-Saharan Africa represented in the survey is similar; their shares are 16 and 14 percent, respectively. Only few Free Zones from South Asia participated. In comparison to the regional distribution of all Free Zones worldwide, Free Zones from Asia therefore are underrepresented, while the other regions – especially the MENA region – are overrepresented in the BEEC survey.

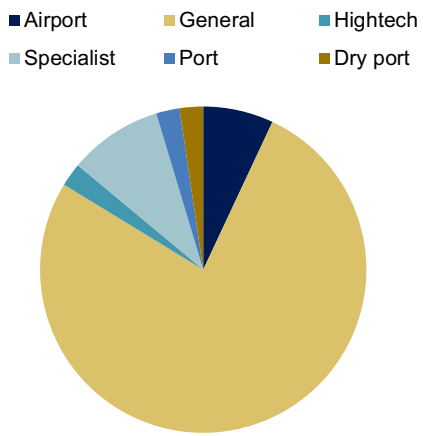
Figure 14: Geography of BEEC participants



Source: BEEC Survey 2019.

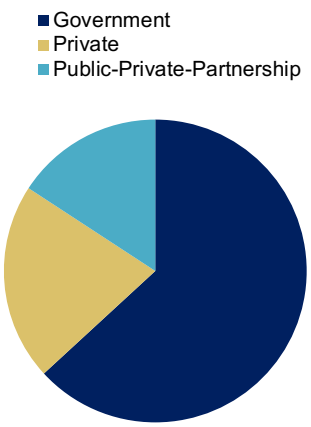
Most BEEC Free Zones are general-purpose zones and government-owned. 77 percent of Free Zones are general-purpose zones, while 12 percent are specialist, among others with a focus on financial services, healthcare services, information and communications technology or high-tech sectors (Figure 15). The other participants are airport, port or dry port Free Zones. Almost two-thirds of participating Free Zones are owned by the government (Figure 16). 21 percent are privately-owned while 16 percent are structured as public-private partnerships.

Figure 15: BEEC participants by type



Source: BEEC Survey 2019.

Figure 16: BEEC participants by ownership

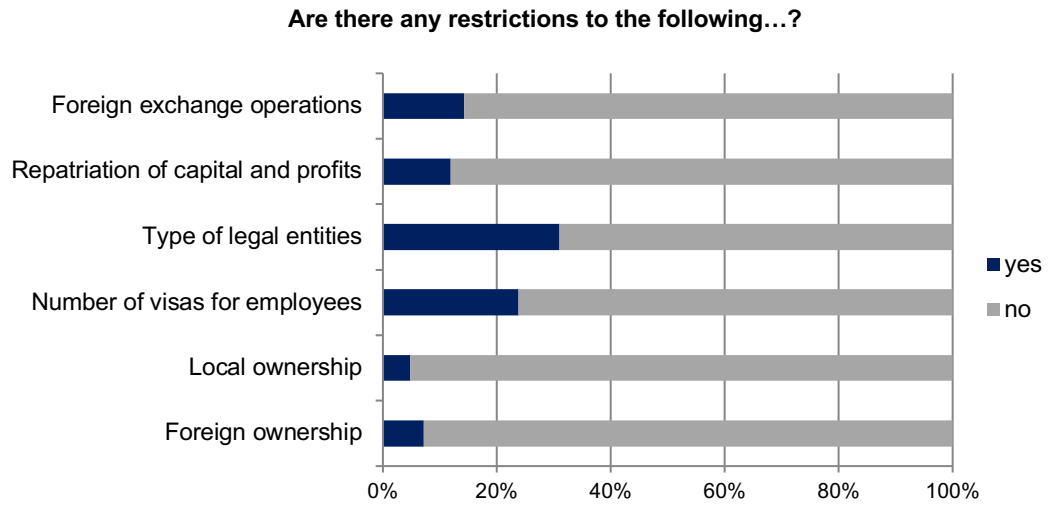


Source: BEEC Survey 2019.

2.3 Ease of Doing Business and Incentives

Business activities in Free Zones are restricted by regulations across several dimensions to a varying degree. Figure 17 provides an overview of the ease of doing business in Free Zones participating in the BEEC based on the presence of restrictive regulations. Roughly one third of responding Free Zones pose restrictions on the type of legal entities that can be established. Around one fourth restrict the number of visas firms can apply for in order to hire employees. Foreign exchange operations and the repatriation of capital and profits are restricted in 14 and 12 percent of Free Zones, respectively. In relatively few Free Zones, the ownership structure of firms active in the zone is restricted. While 5 percent of the participants report restrictions on local ownership, 7 percent report restrictions on foreign ownership. Moreover, more than half of all responding Free Zones report to have a minimum requirement for capital investment.

Figure 17: Ease of doing business in Free Zones based on restrictions to business activity

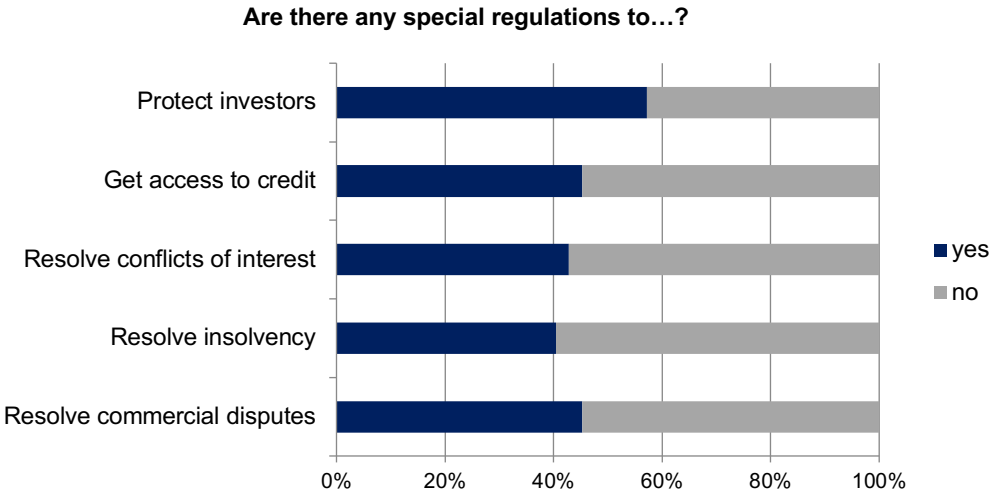


Source: BEEC Survey 2019.

Many Free Zones provide special regulatory arrangements to support investors. Across all dimensions of investment facilitation surveyed, more than 40 percent of

BEEC participants report to have some special mechanism in place (Figure 18). 57 percent of participants have special tools to protect investors, and 45 percent have Free Zone-specific mechanisms to facilitate access to credit and to resolve commercial disputes. In addition, many Free Zones offer specific mechanisms to resolve conflicts of interest and cases of insolvency.

Figure 18: Ease of doing business in Free Zones based on special regulations



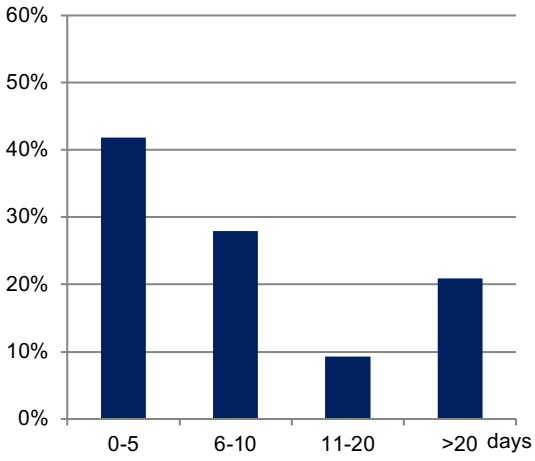
Source: BEEC Survey 2019.

The time required to set up business operations in Free Zones varies widely. In over 40 percent of Free Zones that participated in the BEEC a business can be registered in less than five days (Figure 19). In over 50 percent of Free Zones a permanent electricity connection can be obtained within the same time frame (Figure 20). At the same time, around one in five Free Zones report that more than 20 days are required to register a business and obtain a permanent electricity connection, respectively.

Most Free Zones provide on-site customs clearance within one day. Five out of six Free Zones report to provide customs clearance on-site (Figure 21). In 75 percent of the responding Free Zones customs clearance for exports is done within one day, while just below 70 percent of Free Zones report the same efficiency for imports

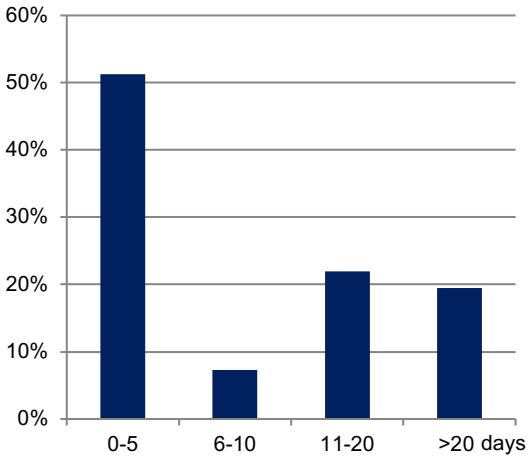
(Figure 22). At the same time, 11 percent of participants state that more than 5 days are required for customs clearance, both regarding exports and imports.

Figure 19: Time required to register a Free Zone business (in days)



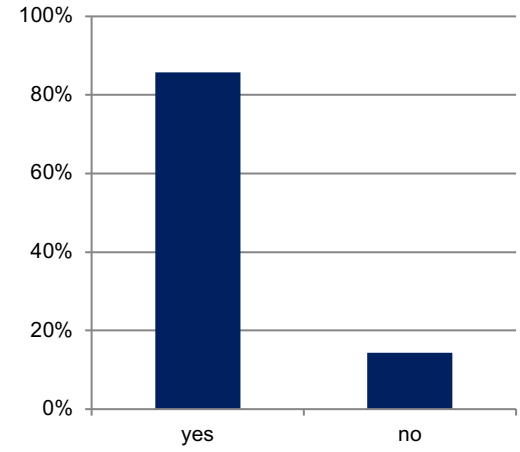
Source: BEEC Survey.

Figure 20: Time required to obtain a permanent electricity connection (in days)



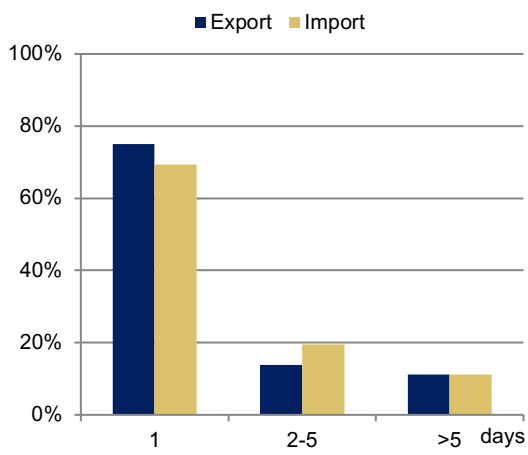
Source: BEEC Survey.

Figure 21: Customs clearance on-site



Source: BEEC Survey.

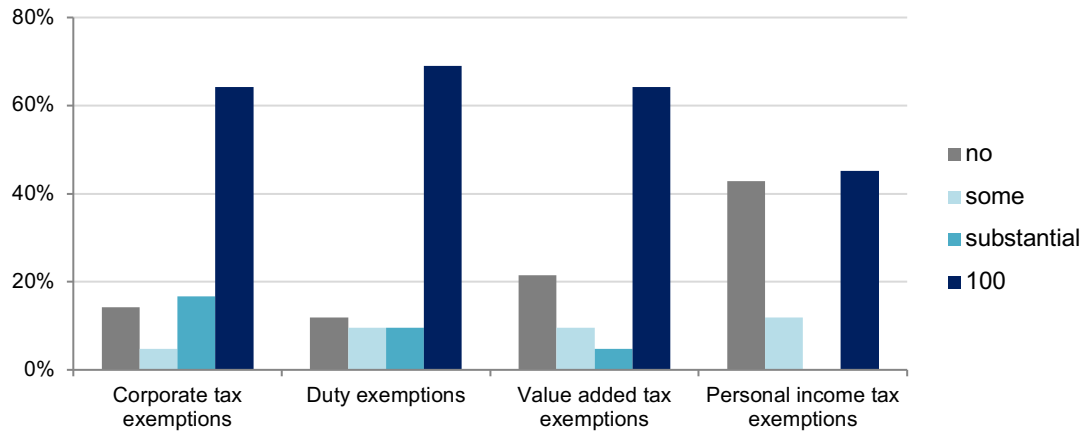
Figure 22: Time required for customs clearance



Source: BEEC Survey.

The large majority of Free Zones provide sizable fiscal incentives. Over two-thirds of Free Zones have in place a 100 percent exemption for corporate taxes, value-added taxes and duties (Figure 23). The share of Free Zones providing full personal income tax exemptions is somewhat lower at 45 percent. At the same time, 14 and 21 percent of participating Free Zones do not offer corporate tax and value-added tax exemptions, respectively. The share of Free Zones without duty exemptions is slightly lower, while over 40 percent do not offer personal income tax exemption. It is important to note that the effect and sustainability of fiscal incentives are controversially discussed in the literature (UNCTAD 2019; Hachmeier and Mösle 2019).

Figure 23: Tax incentives offered in Free Zones

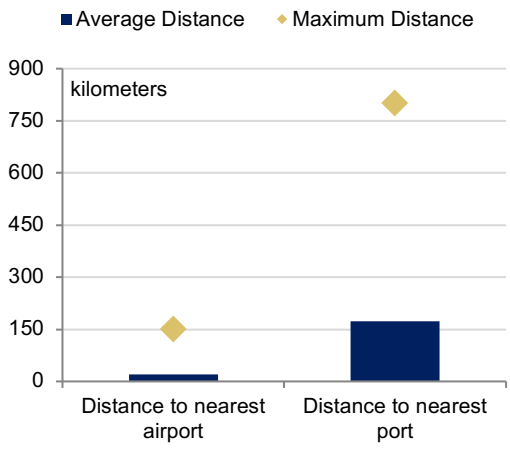


Source: BEEC Survey.

2.4 Infrastructure and Facilities

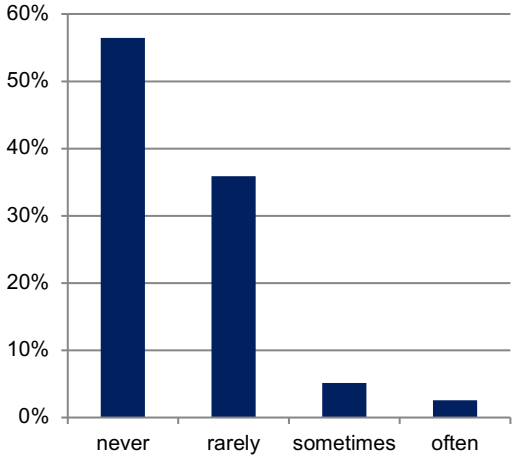
Free Zones strive to provide high-quality infrastructure and services to investors. Insufficient infrastructure and suboptimal location with poor access to markets can hamper the success of Free Zones (Farole 2011; Farole and Moberg 2017; Mösle 2019). According to the BEEC survey, participating Free Zones have better access to airports than to ports, on average (Figure 24). The average distance to the nearest airport is roughly 20 kilometers; with a maximum distance of 150 kilometers. The average distance to the nearest port is substantially higher at 170 kilometers; with a maximum distance of 800 kilometers. Over 50 percent of Free Zones have direct access to railway transportation (Figure 26). Regarding electricity supply, the large majority of Free Zones report power outages occur never (56 percent) or rarely (36 percent) (Figure 25). However, 8 percent indicate a higher frequency of power outages. Five out of 6 Free Zones have on-site generators to prevent power failures. The same share of Free Zones provides investors with access to broadband internet.

Figure 24: Proximity to transport infrastructure



Source: BEEC survey.

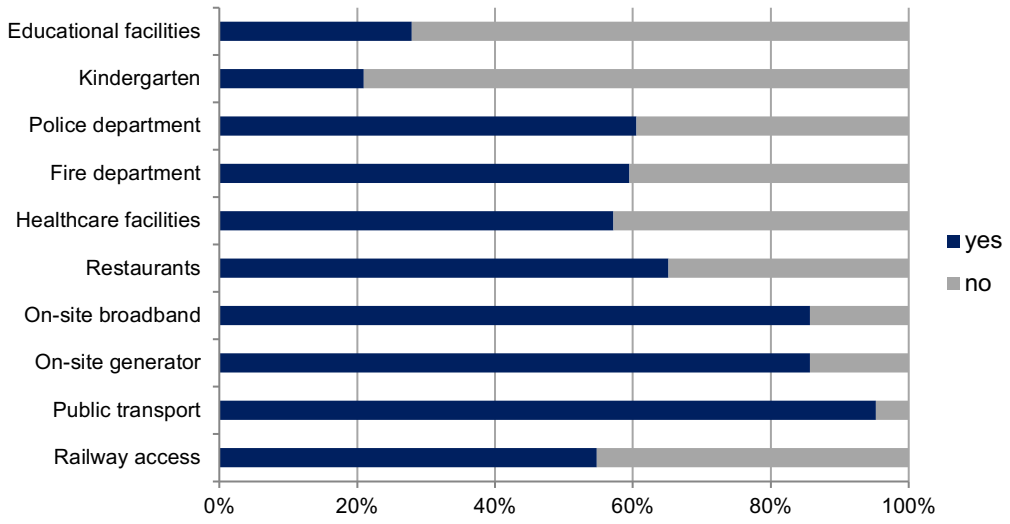
Figure 25: Frequency of power outages



Source: BEEC survey.

Some Free Zones offer facilities for the safety and well-being of their employees. 60 percent of the BEEC participants report to have a police and fire department on-site, respectively (Figure 26). Almost the same share of Free Zones provides healthcare facilities. Two out of three Free Zones have restaurants on their premises. Almost all participating Free Zones (95 percent) can be reached via public transportation. However, the share of Free Zones offering educational facilities is substantially lower at 28 percent and only 21 percent offer childcare facilities.

Figure 26: Facilities and access to transportation

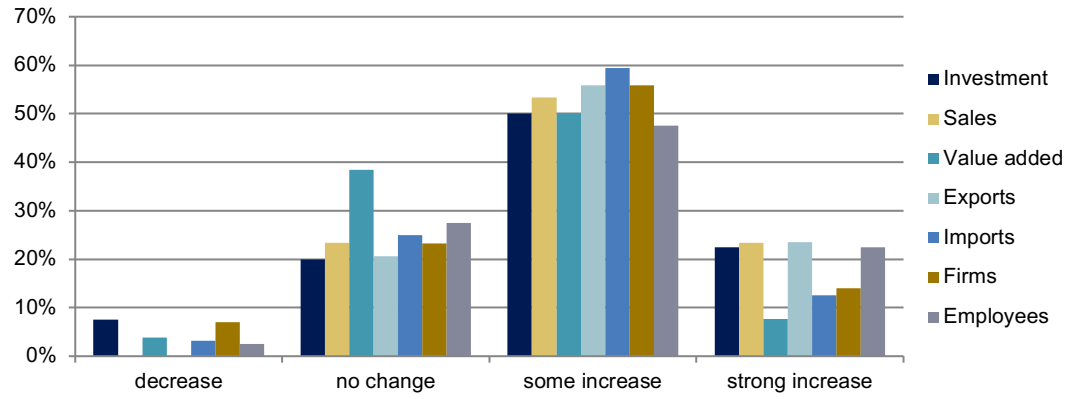


Source: BEEC Survey.

2.5 Economic Performance and Contribution

On average, 2018 was a good business year for Free Zones according to the BEEC survey.[4] More than 600,000 employees worked in over 45,000 companies located in the Free Zones participating in the BEEC. The large majority of them saw an increase in economic activity across various dimensions. At least 70 percent of Free Zones reported a rise in investment, sales, exports, imports, employment and the number of firms (Figure 27). The performance was somewhat less positive regarding the value-added generated in Free Zones, i.e. their contribution to national GDP. While almost 40 percent of Free Zones saw no change in value-added compared with the previous year, in 50 percent of Free Zones it increased to some extent. Only 8 percent report a strong increase, the lowest percentage compared with the other economic dimensions. The number of Free Zones reporting a decrease for any measure of economic activity was low. Still, investment and the number of employees fell in 8 and 7 percent of Free Zones, respectively.

Figure 27: Development of key economic indicators in 2018

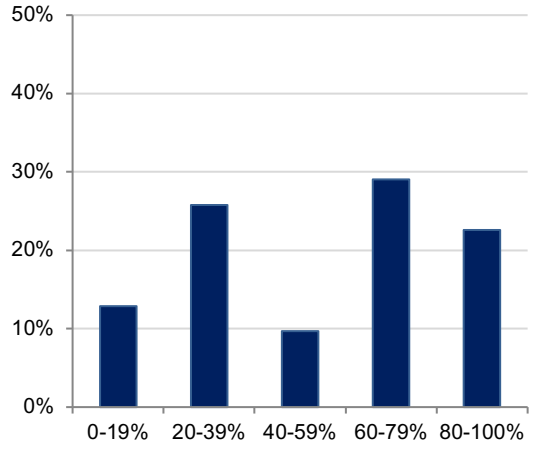


Source: BEEC Survey.

[4] This chapter presents the results of the BEEC survey conducted in 2019 which surveyed economic outcomes of 2018. For more recent developments of economic activity in Free Zones, please refer to Chapter 3 analyzing the Free Zones World Economic Barometer (F-WEB).

Investment in Free Zones is not only generated by large, foreign companies. Only slightly over 50 percent of participants report that more than 60 percent of the investment flowing into their Free Zone can be attributed to large enterprises (Figure 28). This implies that the investment generated by small and medium-sized enterprises is substantial and that both large companies and SMEs contribute significantly to economic activity in Free Zones. Regarding the ownership structure of Free Zone firms, the contribution of foreign-owned firms is larger than the contribution of local firms. Over 80 percent of participants report that more than 60 percent of investment in their Free Zone is generated by foreign-owned companies (Figure 29).

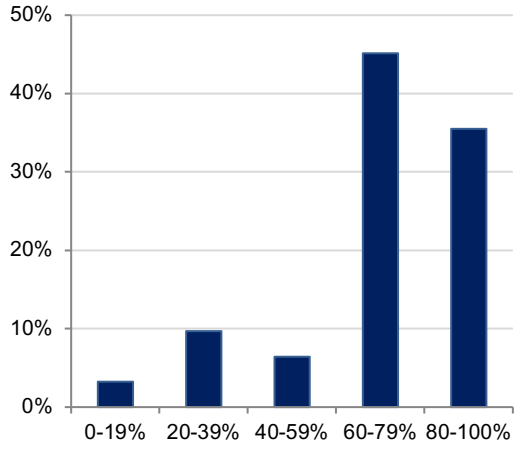
Figure 28: Share of investment generated by large companies



Note: Horizontal axis: Percentage of investment generated by large companies (vs. SMEs); vertical axis: share of BEEC responses.

Source: BEEC Survey.

Figure 29: Share of investment generated by foreign companies

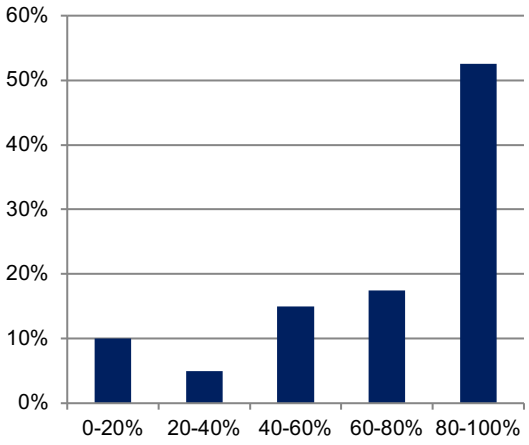


Note: Horizontal axis: Percentage of investment generated by foreign companies (vs. local companies); vertical axis: share of BEEC responses.

Source: BEEC Survey.

Many Free Zones still have the capacity to grow. Over the past three years, almost 35 percent of the BEEC Free Zones expanded their land area and even more – around 40 percent – plan to expand over the next three years (Figure 31). At the moment, slightly more than half of all BEEC participants report an occupancy rate of 80 to 100 percent (Figure 30). Almost one fifth of respondents have an occupancy rate of 60 to 80 percent, while in 15 percent of the participating Free Zones more or less half of the zone is in use. However, 10 percent – mostly newer zones founded after 2010 – state that at least 80 percent of their space is still vacant.

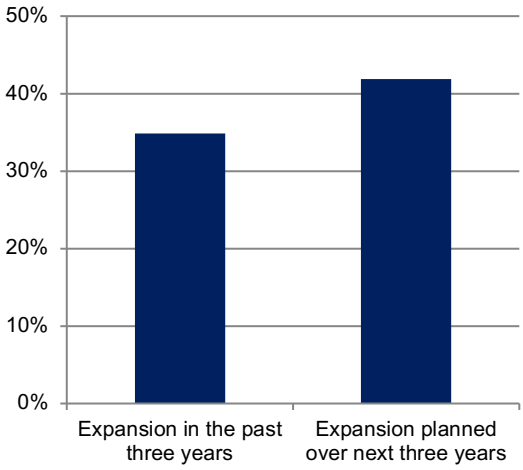
Figure 30: Occupancy rate



Note: Horizontal axis: occupancy rate; vertical axis: share of BEEC responses.

Source: BEEC Survey.

Figure 31: Capacity development

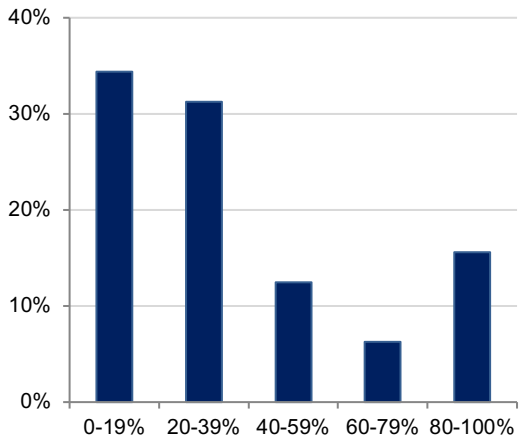


Source: BEEC Survey.

Most Free Zones export most of their output. Free Zones are a tool of industrial policy often used to attract and facilitate foreign direct investment, to create employment opportunities and to increase and diversify exports. Indeed, most Free Zones export the majority of their output (Figure 32). More specifically, 65 percent of BEEC participants report that they sell less than 40 percent of their output domestically. Only 16 percent of Free Zones sell almost all of their output in the local market.

While Free Zones heavily rely on imported input goods in the production process, they also purchase from local suppliers. In addition to investment and export promotion, policy makers often hope for broader, economy-wide benefits from Free Zones such as the integration of local firms outside the Free Zone into global value chains, promoting technology and knowledge transfer from foreign investments. While it is difficult to evaluate these effects empirically, the percentage of inputs used in the production process sourced domestically can give at least some indication regarding the extent of economic linkages between Free Zone firms and domestic firms. According to the BEEC survey, less than 20 percent of Free Zones source less than 20 percent of inputs from the host economy (Figure 33). Slightly more than 40 percent purchase 20 to 39 percent of inputs domestically, and 30 percent of Free Zones buy between 40 and 60 percent of goods in the local economy. Around 10 percent of the BEEC Free Zones source more than 60 percent locally.

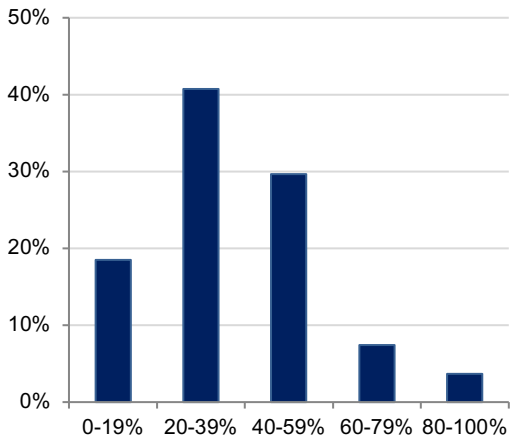
Figure 32: Domestic sales



Note: Horizontal axis: percentage of produced output sold in host country; vertical axis: share of BEEC responses.

Source: BEEC Survey.

Figure 33: Domestic sourcing



Note: Horizontal axis: percentage of input goods sourced in host country; vertical axis: share of BEEC responses.

Source: BEEC Survey.

2.6 Concluding Remarks

The BEEC Survey aims at establishing a database on Free Zones worldwide that helps analyze their performance and their contribution to the broader economy and improve knowledge about the factors that make Free Zones thrive. In 2019, Free Zones from over 20 countries representing 600,000+ employees and 45,000+ firms responded to the survey. They provided data on the main characteristics of their Free Zone, on the incentives and infrastructure they offer as well as on economic indicators such as investment and employment. This chapter provided a descriptive overview of the results of the 2019 survey at an aggregate level.

The more Free Zones participate, the more valuable the BEEC Survey can become for the community. Ideally, the number of Free Zones participating in the survey will increase in the coming rounds and participants of the 2019 survey will update their information every year. Deeper analyses, for example on the success factors of investment attraction, will become possible over time with regular participation of an increasing number of Free Zones. Additionally, if a sufficiently large number of Free Zones within one region or country participate, analysis at the regional or country level will become possible. For example, country reports could provide a comparison of developments in Free Zones with those in the general economy. In addition, the contribution to the host economy could be analyzed. Overall, the BEEC survey can contribute to delivering information relevant to evaluate policy decisions and to informing policy initiatives.

3 The Free Zones World Economic Barometer (F-WEB)

3.1 Introduction

The F-WEB is a quarterly, survey-based sentiment indicator designed to gauge current momentum and future trends of economic activity in Free Zones around the globe. It was launched by the World Free Zones Organization in cooperation with the Kiel Institute for the World Economy in 2018. This chapter summarizes economic trends and prospects in Free Zones around the globe as measured by the F-WEB focusing on 2019 and the first quarter of 2020 in particular. It should be noted that the most recent dramatic change in the global economic environment due to the COVID-19 pandemic has not yet been picked up in the latest regular F-WEB round conducted in early February 2020. To get insights on the impact of COVID-19 on Free Zones activity, in late March and early April a special survey has been conducted. The results are presented in the Chapter 4.

For Free Zones around the globe, the F-WEB is a unique tool to evaluate their relative performance. The quarterly F-WEB notes provide detailed reports of the survey results and can help Free Zone representatives put recent developments in their Free Zone as well as their expectations into a broader perspective. Thus, the F-WEB offers the opportunity to benchmark the current and expected performance of an individual Free Zone against an international peer group.

The F-WEB captures Free Zones' sentiment regarding current and future economic performance. The F-WEB survey consists of a set of questions related to the economic performance in Free Zones that are asked every quarter in order to establish a history of results that can be used to extract information. In addition, a small number of special questions is included in every round that will be asked at a lower frequency or irregularly as a reaction to specific developments. The questions are qualitative in nature and can be answered by choosing positive answers (increasing,

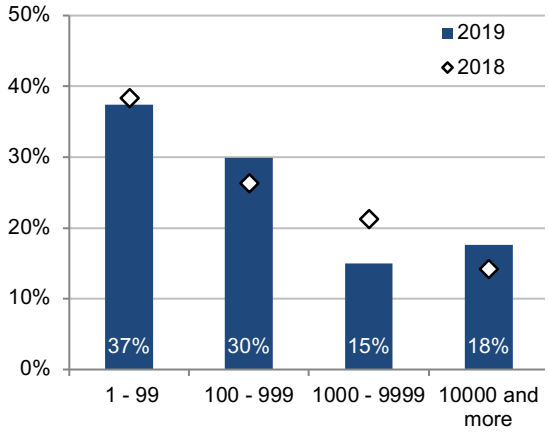
improving, good), negative answers (decreasing, deteriorating, poor) or neutral answers (unchanged, more or less the same, normal) from dropdown menus.

The aim of the F-WEB is to provide easily interpretable indicators. To this end, the available information is condensed. Thus, positive answers get the value of 100 and negative answers the value of -100. Neutral answers get the value of 0. Our indicator value is then calculated as the aggregate value of received answers divided by the number of respondents to each answer. The index value is 100 when all participants give positive answers and -100 when there are uniformly negative answers. An index value of 0 results in the case of 100 percent neutral answers or in the case that the same number of positive and negative answers is given. A detailed description of the design of the survey and the F-WEB methodology, as well as all quarterly F-WEB reports, can be found in www.worldfzo.org ..

3.2 General Information

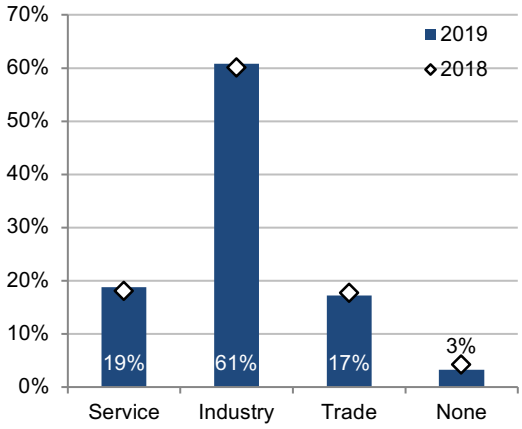
The F-WEB survey is conducted on a quarterly basis. More specifically, the surveys are usually conducted in February, May, August and November each year. On average, more than 50 Free Zones took part in each survey; a number we hope can still be raised in coming rounds of the F-WEB.

Figure 34: Distribution of participating Free Zones by number of employees



Source: F-WEB Survey.

Figure 35: Distribution of participating Free Zones by dominant sector



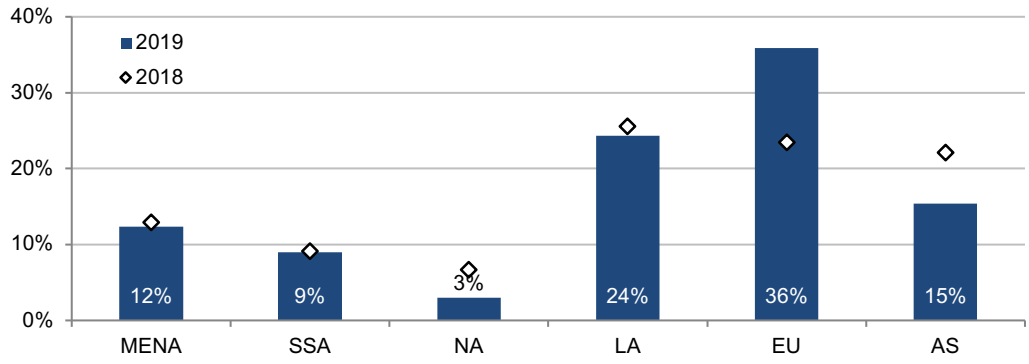
Source: F-WEB Survey.

Free Zones of all sizes participate in the F-WEB. Around two-thirds of Free Zones participating in 2019 had less than 1,000 employees (Figure 34). 37 percent of participants represent small Free Zones with 1 to 99 employees, followed by 30 percent of Free Zones with 100 to 999 employees. 15 percent of answers came from Free Zones with 1,000 to 9,999 employees, while 18 percent had more than 10,000 employees. In comparison with the results from 2018, the share of Free Zones with less than 1,000 employees increased slightly. At the same time, the share of participating Free Zones with 1,000-9,999 employees decreased from 21 percent in 2018 to 15 percent in 2019, while the share of Free Zones with more than 10,000 employees increased from 14 percent to 18 percent.

Most participating Free Zones focus on industry. Overall, 61 percent focus on this type of activity (Figure 35). With 19 percent and 17 percent, respectively, Free Zones specializing in services and trade were almost equally represented in the F-WEB indicators in 2019. Only a very small number of Free Zones have no clear focus on a specific sector. Compared with the results from 2018, the distribution by dominant sectors remained almost identical which is a good sign regarding comparability of the F-WEB over time.

Free Zones from all around the globe share their assessment with the community. In 2019, the largest number of participants came from Free Zones in Europe (EU) and Latin America and the Caribbean (LA) which account for 36 and 24 percent of all responses, respectively (Figure 36). Asia was the third most important region represented in the F-WEB in 2019, with 15 percent of answers coming from Free Zones there, followed by the Middle East and North Africa (MENA) which accounted for 12 percent in all answers. Fewer participants came from Sub-Saharan Africa (SSA, 9 percent) and North America (NA, 3 percent). In total, Free Zones from 68 countries around the globe participated in the F-WEB in 2019. In comparison with the results from 2018, the share of Free Zones from Europe increased noticeably from 24 to 36 percent. The F-WEB also saw an increase in participation from the American continent, albeit much less pronounced than in the case of Europe. At the same time, the share of participants from Asia decreased from 22 to 15 percent, while participation from Africa and the Middle East remained more or less the same.

Figure 36: Distribution of participating Free Zones by region

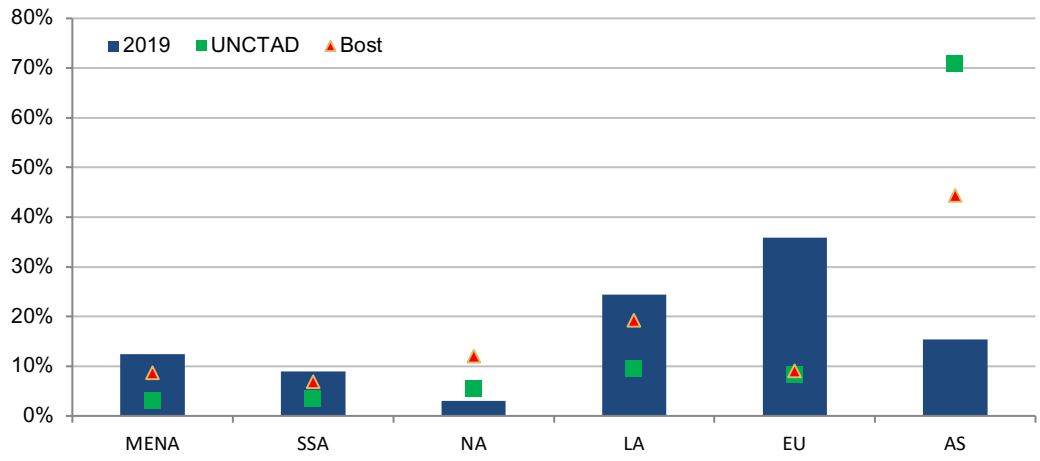


Note: Region acronyms: MENA (Middle East and North Africa), SSA (Sub-Saharan Africa), NA (North America), LA (Latin America and the Caribbean), EU (Europe), AS (Asia).

Source: F-WEB survey.

Asian Free Zones are underrepresented in the F-WEB so far. Depending on the definition of Free Zones, counting their number in a specific world region yields different results. We use two different data sources, the World Free Zones Organization (2018) and UNCTAD (2019) to compare the regional distribution of F-WEB participants to the regional distribution of the universe of Free Zones. The comparison illustrates that the survey data does not fully reflect the actual regional distribution of the universe of Free Zones (Figure 37). Especially Asia is underrepresented in the F-WEB data.[5] On the other hand, the share of participants from Europe is considerably larger than the corresponding share at the global level.

Figure 37: Regional distribution of F-WEB participants in comparison to regional distribution of all Free Zones



Note: Region acronyms: MENA (Middle East and North Africa), SSA (Sub-Saharan Africa), NA (North America), LA (Latin America and the Caribbean), EU (Europe), AS (Asia).

Source: F-WEB survey, World FZO (2018), UNCTAD (2019).

[5] According to the numbers provided by UNCTAD (2019) more than half of all Free Zones worldwide are located in China. Since the F-WEB aims to capture developments in Free Zones around the globe and not just in a specific country, some underrepresentation of Asia in the F-WEB survey is acceptable.

3.3 Past and Recent Developments

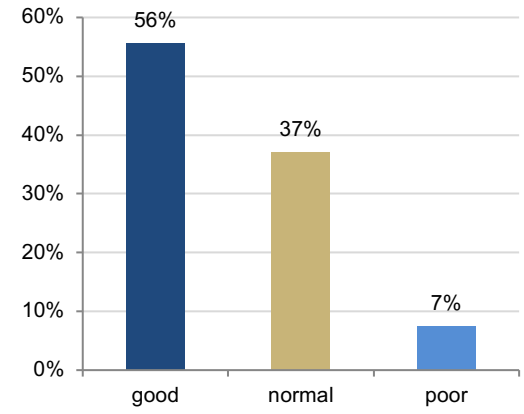
In the following, past and current developments of the F-WEB are briefly described. While general trends will be addressed, the emphasis is on the most recent round of the F-WEB, 2020Q1, which was conducted between February 3 and February 17. Representatives of 34 Free Zones in 24 countries participated in the survey.

3.3.1 Current Economic Situation

General situation

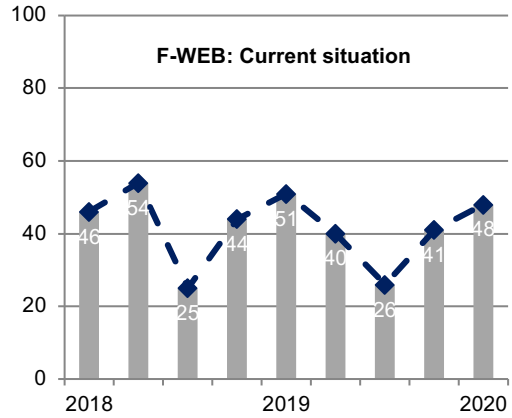
Question 1.1: "Overall, how do you assess the current economic situation in your Free Zone, taking into account the usual seasonal pattern?"

Figure 38: Current economic situation



Source: F-WEB Survey.

Figure 39: F-WEB indicator for current economic situation



Source: F-WEB Survey.

Free Zones started the year 2020 on a relatively positive note. The F-WEB indicator for current economic situation was 48 in the first quarter. Thus, economic conditions in Free Zones continued to recover from the pronounced deterioration seen

in the third quarter of 2019 which may have been reflecting trade disputes between China and the United States, the social unrest in many South American countries, as well as uncertainties and progress surrounding Brexit.

The positive start into the new year had been anticipated by the Free Zones community. In the last quarter of 2019, two out of three Free Zones expected that economic conditions in the following three months would improve. In 2020Q1, the share of Free Zones reporting a good current economic situation increased to 56 percent, up from 46 percent in the previous quarter (Figure 38). At the same time, the share of Free Zones indicating normal conditions decreased from 49 to 37 percent. The number of Free Zones facing a poor situation remains low; their share increased slightly to 7 percent (2019Q4: 5 percent).

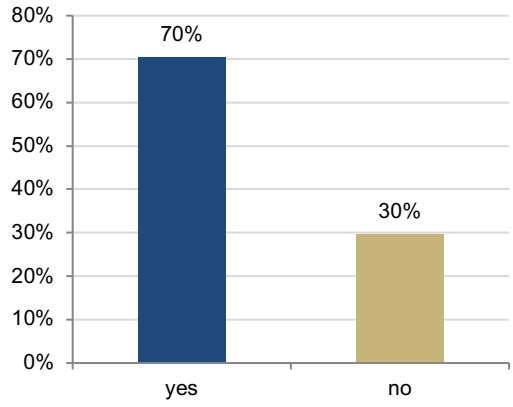
On a more technical note: While global and regional factors may have contributed to the cyclical pattern observed in 2019, the similar developments observed in 2018 and 2019 could also be a sign of seasonality ((Figure 39). Although participants are asked to provide their assessment taking into account the usual seasonal pattern, it cannot be ruled out that seasonal factors still influence the F-WEB. Once the F-WEB is available over a longer time horizon, a rigorous analysis of this issue will be possible.

Structural Pattern

Question 1.2: "Is the current economic situation similar in all sectors/most companies hosted by your Free Zone (answer yes) or are there pronounced differences across sectors/companies (answer no)?"

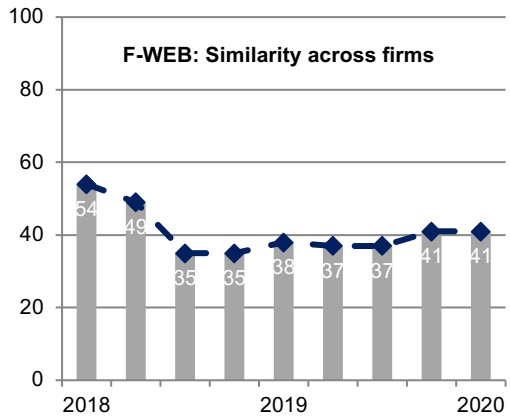
The majority of Free Zones report that all firms or sectors, respectively, encounter similar economic circumstances. In fact, the dispersion of economic activity within the Free Zones has not changed much since the second half of 2018 (Figure 41). Most recently, more than two out of three Free Zones report that all firms or sectors, respectively, in their Free Zone face a similar economic situation (Figure 40). At the same time, 30 percent describe the situation of sectors/firms in the Free Zone as substantially diverse. Thus, in 2020Q1 the F-WEB indicator for similarity across firms results in a value of 41, unchanged from the previous quarter and only somewhat higher than the readings seen in the quarters before.

Figure 40: Similarity across firms/sectors



Source: F-WEB Survey.

Figure 41: F-WEB indicator for similarity across firms



Source: F-WEB Survey.

Detailed dimensions

Questions 1.3-1.6 relate to recent developments in more detailed economic dimensions: "Compared to the previous three months and taking into account the usual seasonal pattern…" how has turnover/employment/investment/profitability developed?

The F-WEB indicators for current turnover, employment and profitability all experienced a downward trend in 2019 and reached their lowest levels towards the end of the year. The deterioration was most pronounced for employment, where the F-WEB indicator dropped from an all-time high of 59 at the start of the year 2019 to 24 in 2019Q4 (Figure 44 & 45), followed by turnover (2019Q1: 58, 2019Q4: 31; Figure 42 &43) and profitability (2019Q1: 46, 2019Q4: 23; Figure 48 & 49). Investment – which overall shows the lowest volatility across economic dimensions – was less affected by the general downturn of 2019 but there was still some deterioration recorded in the second half of 2019 (2019Q1: 54, 2019Q4: 46; Figure 46 & 47).

Figure 42: Current turnover

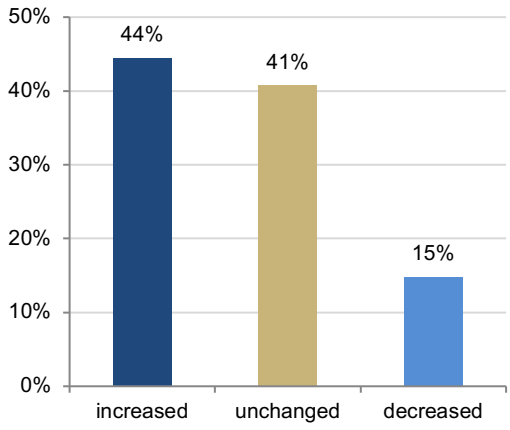


Figure 43: F-WEB indicator for current turnover

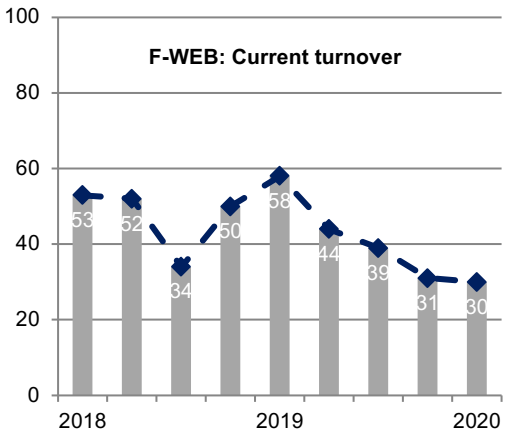


Figure 44: Current employment

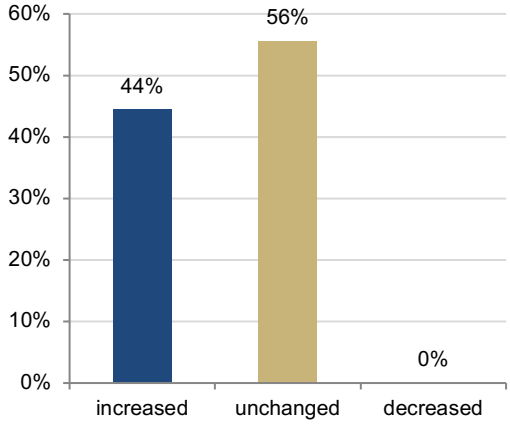
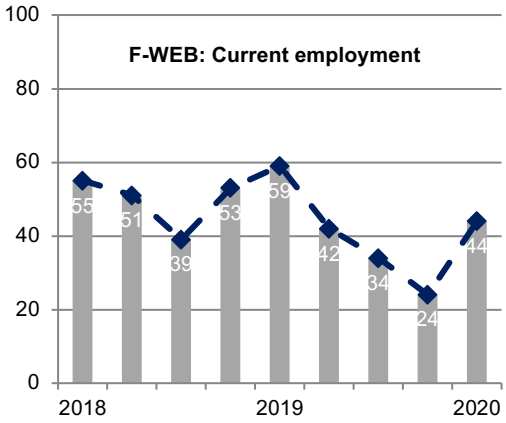


Figure 45: F-WEB indicator for current employment



Source: F-WEB Survey.

Figure 46: Current investment

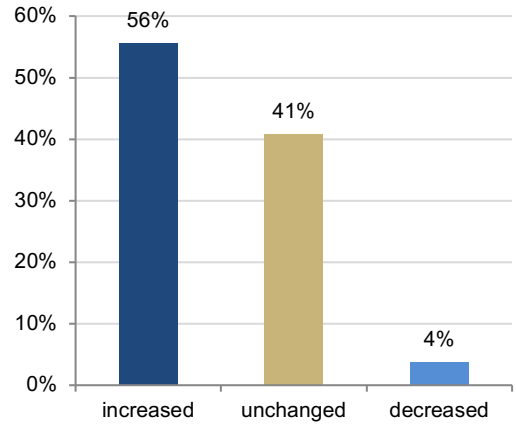


Figure 47: F-WEB indicator for current investment

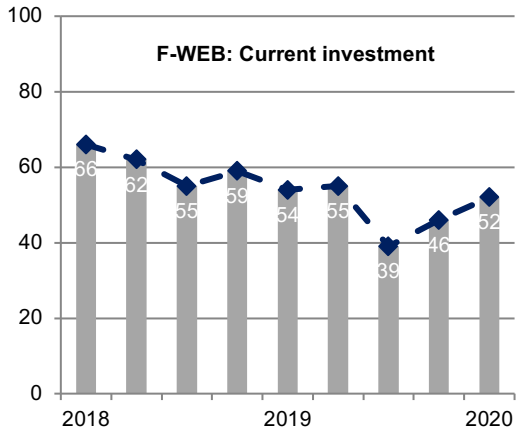
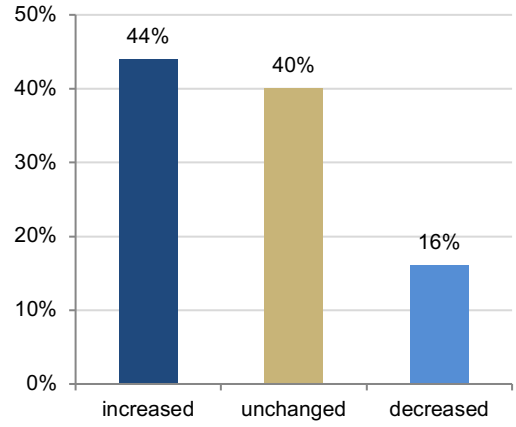
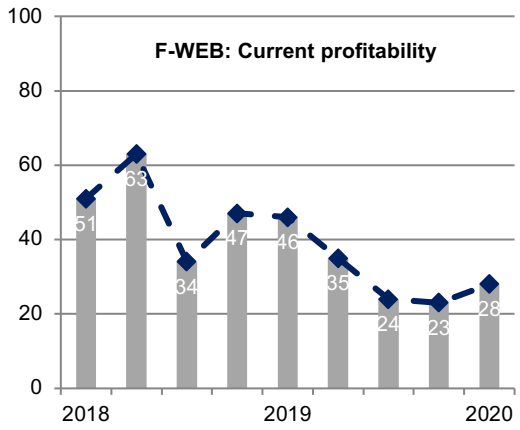


Figure 48: Current profitability



Source: F-WEB survey.

Figure 49: F-WEB indicator for current profitability

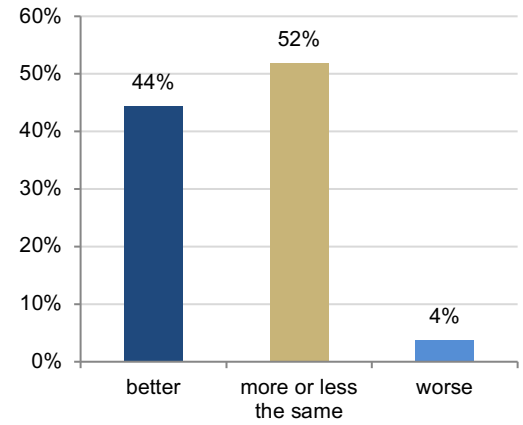


Most recently, economic sentiment recovered – at least partly – from its decline seen in 2019. The F-WEB indicators for current employment, investment and profitability all increased compared to the last quarter of 2019. The uptake was most pronounced for current employment, where the F-WEB indicator jumped from a value of 24 in 2019Q4 to 44 in 2020Q1. Only the indicator for current turnover did not pick up. Still, across dimensions, at least 44 percent of F-WEB participants report an increase in activity compared with the previous quarter. The share of Free Zones reporting a decrease is very low for employment (0 percent) and investment (4 percent); for current turnover and profitability it is somewhat higher at 15 and 16 percent, respectively.

Relative assessment

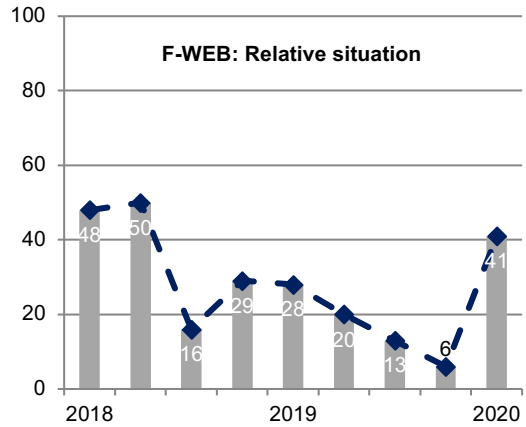
Questions 1.7: "Compared to the economic situation in your host country how do you assess the overall economic situation?"

Figure 50: Relative economic situation



Source: F-WEB survey.

Figure 51: F-WEB indicator for relative situation



Source: F-WEB survey.

More Free Zones experienced a better economic situation than their respective host countries at the start of 2020. In 2019, the F-WEB indicator capturing the economic situation in Free Zones compared to the host country displayed a steady

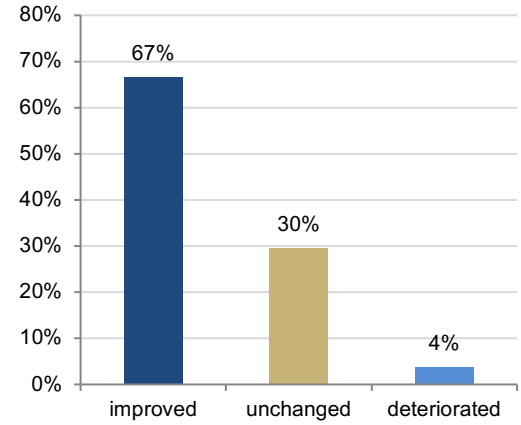
downward trend from a value of 29 in 2018Q4 to a value of six in 2019Q4. The year 2020 started with a significantly higher number of 41, reaching a level close to the all-time high 50 seen in the second quarter of 2018 (Figure 51). Nearly every second Free Zone reports to experience a better economic situation than their respective host country (Figure 50). The other half of participants reports a similar situation and only a very small number of Free Zones state a significantly worse situation. That implicates a better overall situation than in 2019 for most Free Zones.

3.3.2 Expectations

General situation

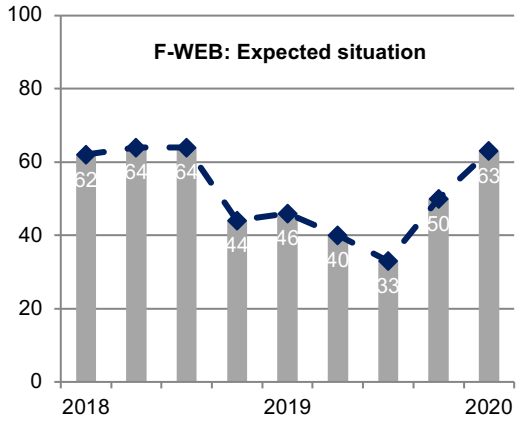
Question 2.1: "Overall, compared to the current situation, how do you expect economic conditions to develop in your Free Zone over the next 3 months?"

Figure 52: Expected economic situation



Source: F-WEB Survey.

Figure 53: F-WEB indicator for expected situation



Source: F-WEB Survey.

Short-term expectations of economic conditions were deteriorating through most of 2019 but improved markedly towards the end of the year and in early 2020. With a value of 63 in 2020Q1, the F-WEB indicator for expected economic situation reached a level last seen in 2018 (Figure 53). Nearly two-thirds of the

participating Free Zones expected an improved economic situation in the near future, while 30 percent predicted no change in economic activity in their Free Zone (Figure 52). The share of Free Zones expecting deteriorating conditions was at only 4 percent, well below the 10 percent recorded in the previous quarter.

Detailed dimensions

Questions 2.2–2.5 relate to the expectations for developments in specific economic dimensions in the near future: "Overall, compared to the current situation, how do you expect developments in your Free Zone over the next 3 months" … regarding turnover, employment, investment and profitability, respectively?

Across all economic dimensions, Free Zones had a more pessimistic outlook in 2019 than in the previous year. This is true for expectations regarding turnover (Figure 55), employment (Figure 57), investment (Figure 59) and profitability (Figure 61). It is also in line with the overall F-WEB indicator for expected economic situation.

At the start of the year 2020, however, the outlook of Free Zones became more optimistic again. Thus, expectations of participating Free Zones for turnover, employment, investment and profitability became more optimistic in 2020Q1, on average. The share of Free Zones with a positive outlook increased substantially across all dimensions to between 58 (employment) and 67 percent (turnover), respectively. For employment, investment and profitability it was the second consecutive improvement regarding the outlook, while the expectations for turnover improved only now. The share of negative answers remained low in the single digits for all dimensions, as in the previous quarters.

The F-WEB indicator values for expectations across all dimensions increased at the start of the year. The increase was most pronounced for expected turnover, which had remained stable in the previous quarter despite improvements across all other dimensions of economic activity. In 2020Q1 it increased markedly to a value of 63, up from 50 recorded in the second half of 2019 (Figure 54). The indicator for expected employment continued to recover from its sharp drop in 2019Q3 and – with a value of 54 – reached a level similar to the one seen before its decline (2019Q3: 31; 2019Q4: 44; Figure 56). Similarly, the F-WEB indicators for expected investment and

profitability increased for the second consecutive quarter. The indicator for expected investment is now 54 (2019Q3: 42; 2019Q4: 50) and thus, comparable to the level seen in the first half of 2019 (Figure 58). The F-WEB indicator for expected profitability increased to 52 (2019Q3: 36; 2019Q4: 44) – a level last seen in 2018 (Figure 60).

Figure 54: Expected turnover

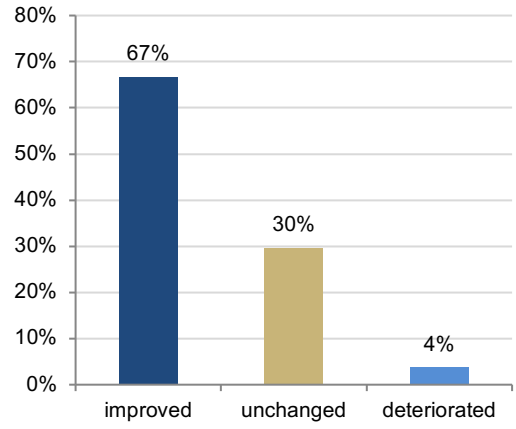


Figure 55: F-WEB indicator for expected turnover

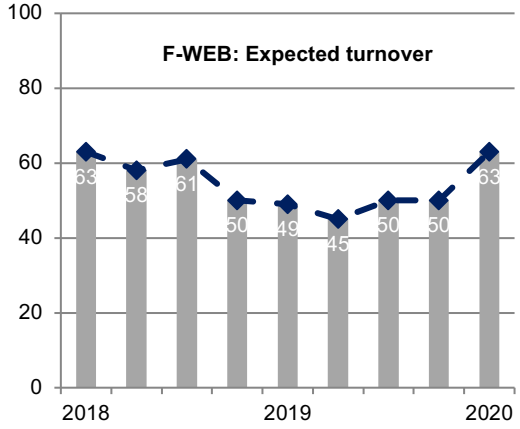


Figure 56: Expected employment

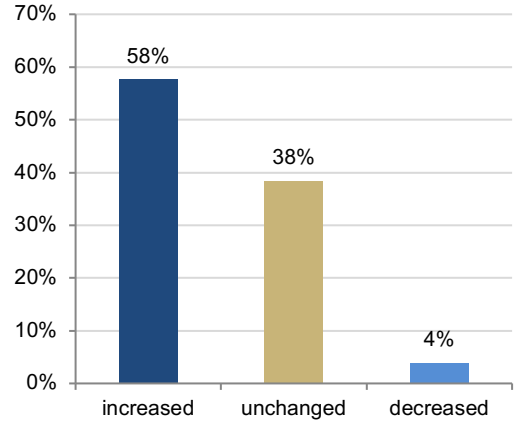
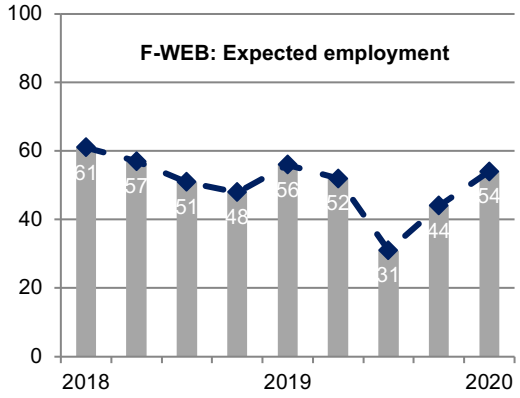


Figure 57: F-WEB indicator for expected employment



Source: F-Web survey.

Figure 58: Expected investment

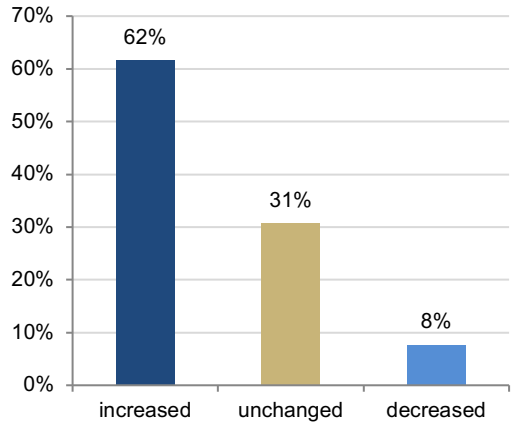


Figure 59: F-WEB indicator for expected investment

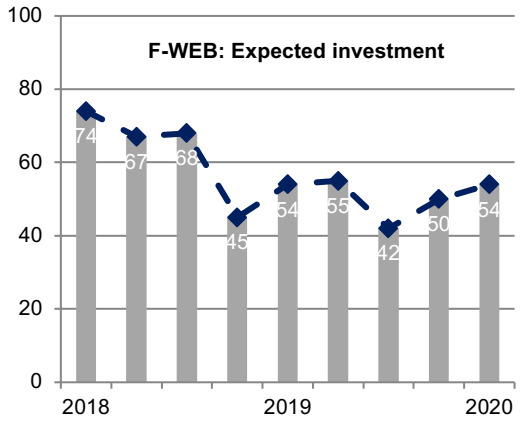
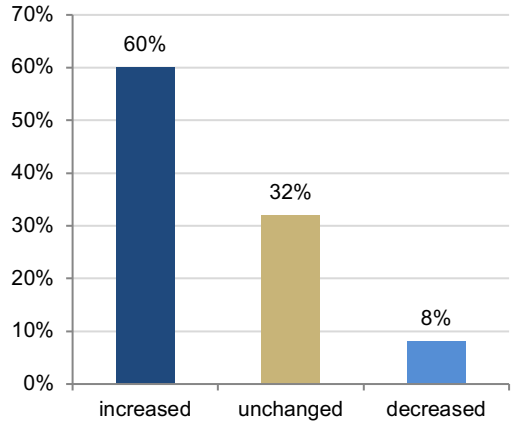
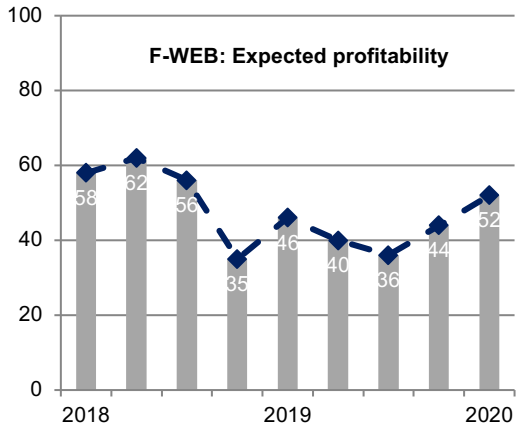


Figure 60: Expected profitability



Source: F-WEB survey.

Figure 61: F-WEB indicator for expected profitability



3.4 Summary

Similar to the two previous years, 2020 started out on a positive note. This is reflected by an indicator value for current economic situation of 48 (2019Q1: 51, 2018Q1: 46), up from a value of 41 in the last quarter of 2019. The share of Free Zones assessing their situation as good increased to 56 percent, up from 46 percent in 2019Q4. A smaller share of Free Zones (37 percent) now report normal conditions, down from 49 percent, while the share of Free Zones experiencing poor conditions remains low at 7 percent (2019Q4: 5 percent). Thus, after the deterioration in economic sentiment seen during the second and third quarter of 2019, signs of improvement becoming visible in the fourth quarter were confirmed in 2020Q1 – at least as of early February 2020 when the survey was conducted.

Figure 62: F-WEB economic conditions index

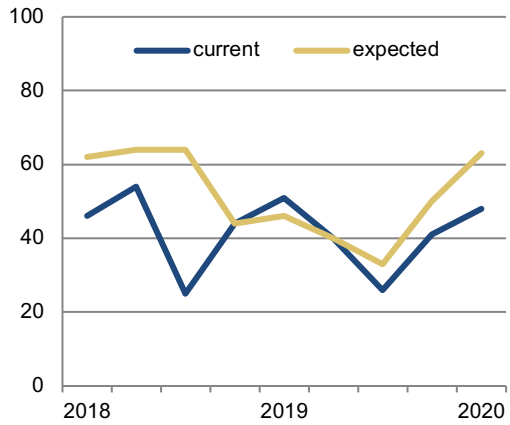
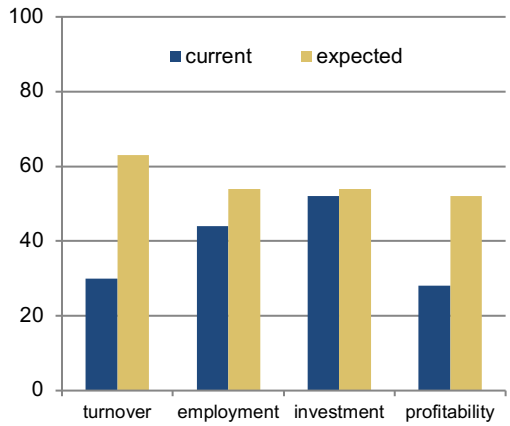


Figure 63: F-WEB components 2020Q1



Source: F-WEB survey.

The outlook for the next three months also became more positive at the start of the year. After having jumped from 33 to 50 in the previous quarter, the F-WEB Expected Economic Conditions Index improved further to a value of 63 – a similar level was last recorded in 2018. In detail, Free Zone representatives have become more optimistic across all economic dimensions, i.e. turnover, employment, investment and profitability (Figure 62).

A closer look at the various elements of current business activity reveals that economic performance improved on a broad basis at the start of 2020. An exception is turnover for which the current situation is largely unchanged compared with the previous round of the F-WEB and remained modest. The F-WEB indicators for employment, investment and profitability all increased (Figure 63). The outlook of respondents with respect to turnover, employment, investment and profitability also became more optimistic, on average. The indicator values for all dimensions increased compared with the 2019Q4 round of the F-WEB.

The F-WEB will only reach its full potential over time and with increasing and regular participation of the Free Zones community. The full amount of information contained in the F-WEB indicator values can, of course, only be assessed once there is a sufficiently long time series available. It is generally the fluctuations of sentiment indicators that can inform about current and future developments more than the absolute value. Moreover, the survey results can be evaluated with respect to several dimensions of Free Zones, such as size, dominant sector or geographical location. However, exploiting the full potential of analysis will require an increased number of participants. The F-WEB will only reach its full potential over time and highly depends on the regular participation of a large number of Free Zones. We therefore hope that the number of participants will further increase, enhancing the benefits for the whole Free Zones community, and thank all regular respondents.

3.5 Special Questions

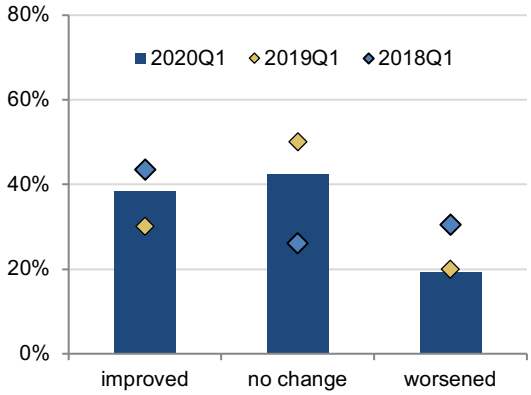
Each F-WEB survey closes with two special questions. Some of them are asked on an annual basis, others irregularly as a reaction to specific developments. This section gives an overview of the results. For additional background information and interpretation, please refer to the respective quarterly F-WEB notes available on the website of the Kiel Institute for the World Economy.

Annual Special Questions

Q1 – "In your view, over the last few months the global trade environment has improved, stayed the same, or worsened?"

In 2020, more F-WEB participants evaluate the trade environment as improved compared with the situation one year ago. However, it is still regarded as less positive than in 2018 (Figure 64). This is likely to be the result of the developments in international trade policy, in particular of the US government, and the uncertainty evolving around the future trade system.

Figure 64: Global trade environment from a Free Zone perspective

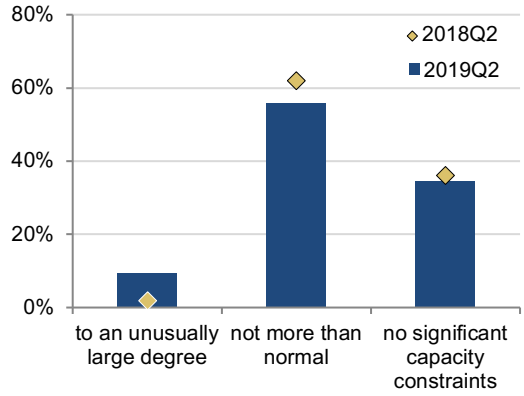


Source: F-WEB survey.

Q2 – "To what extent is current production in your Free Zone limited by capacity constraints?"

Even though the world economy had lost momentum in the second half of 2018, unemployment continued to be at multi-year lows in many countries and survey results indicated that capacity utilization in many economies was still high. In Free Zones, production capacity was still no particular constraint in 2019Q2, although a few more Free Zones reported unusually high capacity utilization than in the year before (Figure 65).

Figure 65: Capacity constraints

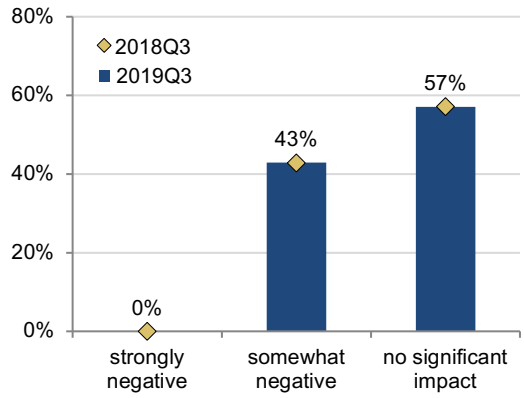


Source: F-WEB survey.

Q3 – "How do you expect trade tensions between several countries and the United States to affect business in your Free Zone?"

In light of the more protectionist stance of the US administration, this special question asked explicitly about potential consequences of these policies for Free Zones. While a majority of Free Zones did not expect a significant impact on their business activities, a substantial share of 40 percent did expect some negative effect (Figure 66).

Figure 66: Impact of trade tensions

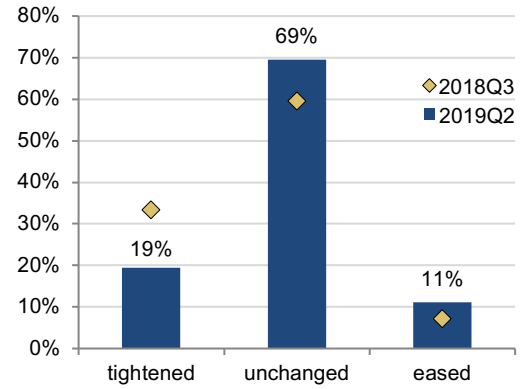


Source: F-WEB survey.

Q3 – "How have financing conditions for businesses in your Free Zone developed over the past six months?"

After a period of rising interest rates in 2018, the US central bank started to lower interest rates again in mid-2019 potentially increasing the room to maneuver also for central banks in emerging economies. This seems to have transmitted – at least to some extent – to Free Zones. Compared to the situation in 2018, the share of Free Zones facing tighter financing conditions dropped and the share facing easier money increased somewhat (Figure 67).

Figure 67: Financing conditions

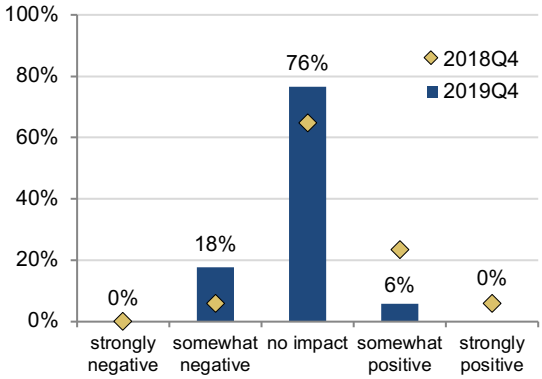


Source: F-WEB survey.

Q4 – "How was business activity in your Free Zone in the last year affected by the rising number of Free Zones worldwide?"

The number of Free Zones worldwide has increased substantially over the past decades. On the one hand, the increasing quantity of Free Zones reflects the growth in popularity – existing zones may benefit from increased attention and a growing network of peers. At the same time, it also implies more competition. In 2019, the overall impact of the rising quantity of Free Zones was, on average, negative according to F-WEB participants which reflects a reversal compared to one year ago (Figure 68).

Figure 68: Impact of rising number of Free Zones worldwide



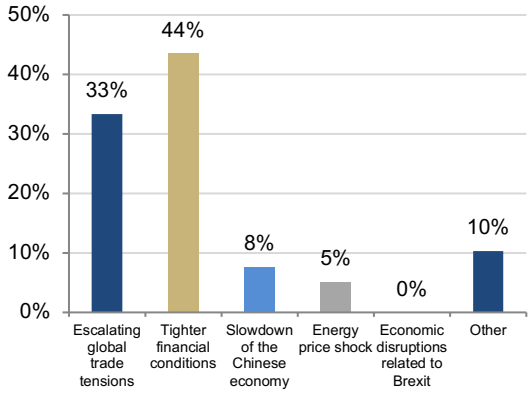
Source: F-WEB survey.

Additional Special Questions

2019Q1 – "In your opinion, which of these risks to the global economy pose the highest risk to the economic activity in your Free Zone?"

This question was asked to find out which of the risks to the global economy ranking high in the public debate at that time was most relevant for Free Zones (Figure 69). The results show that the majority of participants considered tighter financial conditions the most pressing global risk to the economic activity in their Free Zone, followed by escalating global trade tensions.

Figure 69: Global risks for Free Zones

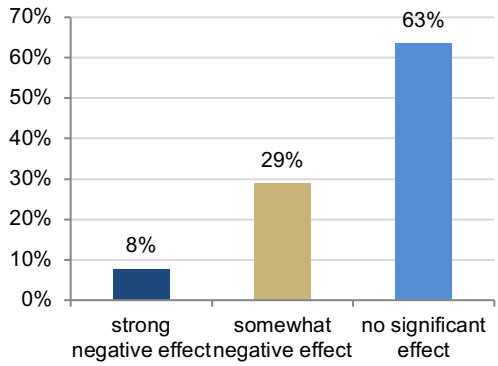


Source: F-WEB survey.

2019Q2 – "Over the past 6 months, has your Free Zone been affected by the elevated levels of economic policy uncertainty observed globally?"

Economic policy uncertainty had been elevated since mid-2018 mainly due to the trade conflict between the US and China as well as geopolitical tensions in the Middle East. More than one in three participating Free Zones was affected by these uncertainties (Figure 70).

Figure 70: Impact of global economic uncertainty

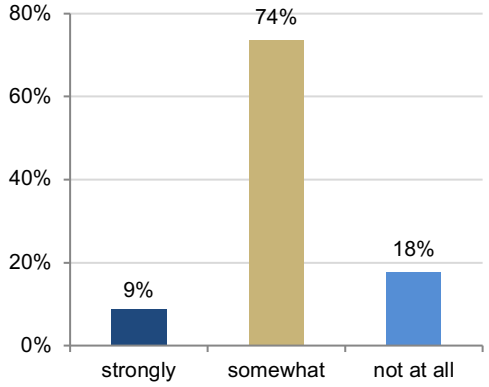


Source: F-WEB survey.

2019Q4 – "How has the slowdown in global economic activity over the past year been reflected in your Free Zone?"

After strong growth in 2017 and early 2018, the world economy slowed down significantly in the course of 2018, and growth remained subdued in 2019. The combination of several negatives, including higher interest rates in the US, increased policy uncertainty, as well as slower growth in China weighed on global economic activity and also affected most Free Zones to some degree (Figure 71).

Figure 71: Impact of global economic slowdown

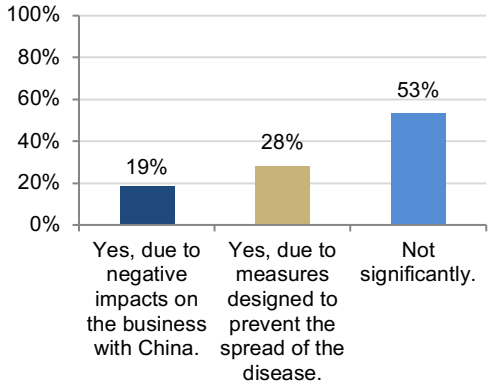


Source: F-WEB survey.

2020Q1 – "Do you expect business in your Free Zone to be affected by the outbreak of the Coronavirus in China?"

Against the backdrop of an escalating situation with respect to COVID-19 in China and increasing signs that it would spread rapidly globally, we asked about the impact on business in Free Zones. At that stage – in early February – still more than 50 percent of Free Zones felt largely unaffected (Figure 72). In those reporting negative effects on business, it was mostly due to preventative measures.

Figure 72: Impact of the coronavirus pandemic



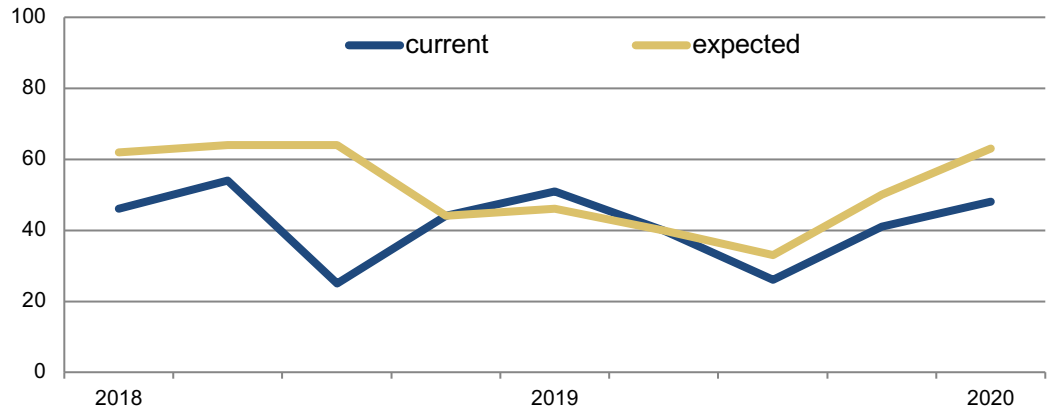
Source: F-WEB survey.

4 F-WEB Special Survey on the Coronavirus Pandemic

4.1 Introduction

In spring 2020, the world is severely affected by the COVID-19 pandemic. As the novel coronavirus has spread to more and more countries, measures designed to contain the disease are weighing on economic activity and are adding to the significant negative impact on growth from the steep decline of production in China, where the virus was first discovered. Initially, the virus progressed most in Asia and Europe where the probability of disruptions of production through interrupted value chains is particularly high. By now, developed and developing countries around the globe are affected by the pandemic and governments worldwide have taken wide-ranging measures as a response. Measures range from social distancing regulation and quarantine of (potentially) infected individuals to shutdown of significant parts of the economy and curfews for the whole population.

Figure 73: F-WEB Economic Conditions Index before impact of COVID-19 pandemic



Source: F-WEB survey.

The COVID-19 pandemic hits Free Zones at a time when economic sentiment had been improving. After the deterioration in economic sentiment seen during the second and third quarter of 2019, signs of improvement becoming visible in the fourth quarter were confirmed in the first quarter of 2020 (Figure 73) – at least as of early February 2020 when the most recent regular F-WEB survey was conducted. The outlook for the next three months had also become more positive at the start of the year. However, the most recent dramatic change in the global economic environment due to the COVID-19 pandemic had not yet been picked up in the survey conducted in early February 2020.

Free Zones are affected by the pandemic through various channels. First, economic activity in many countries has come to a halt due to measures taken by governments to contain the spread of the virus. These measures also affect Free Zones, especially since they are often engaged in sectors and activities where working from home is not an option. Second, health measures and high levels of uncertainty regarding the future development of the pandemic drag on consumption and investment. Recent estimates of UNCTAD (2020) based on earnings revisions of the largest multinational enterprises suggest that FDI could drop by as much as 30 to 40 percent on a global basis during 2020-2021. Third, production in Free Zones could be affected by supply chain disruption. For many goods, China lies at the heart of global value chains (GVCs) and is a major producer of intermediate inputs required for production in other countries. Due to the severe drop in industrial production and exports seen in January and February, raw materials and input goods are now missing for other stages of production. Even though there are some signs of recovery in China by now, the supply chain disruptions likely have amplified with the further spread of the pandemic. And fourth, the economic downturn could be reinforced by financial feedback loops, leading to liquidity problems in the corporate sector. In an apparent flight to safety international investors have already withdrawn a record amount of 83 billion US dollars from emerging markets since the beginning of the coronavirus crisis, according to the IMF.[6]

[6] See IMF Managing Director Kristalina Georgieva's Statement Following a G20 Ministerial Call on the Coronavirus Emergency. (23 March 2020).

An F-WEB Special Survey was conducted on the impact of the coronavirus pandemic on economic activity in Free Zones. The following three questions were asked between March 23, 2020, and April 3, 2020.

1. **Is activity in your Free Zone currently affected by the economic impact of coronavirus pandemic?**

    a. Not really
    b. To some extent
    c. Substantially

2. **Do you expect activity in your Free Zone to be affected by the coronavirus pandemic in the coming months?**

    a. Not really
    b. To some extent
    c. Substantially

3. **By which channels is or will activity in your Free Zone likely be affected?** ***(Select all that apply.)***

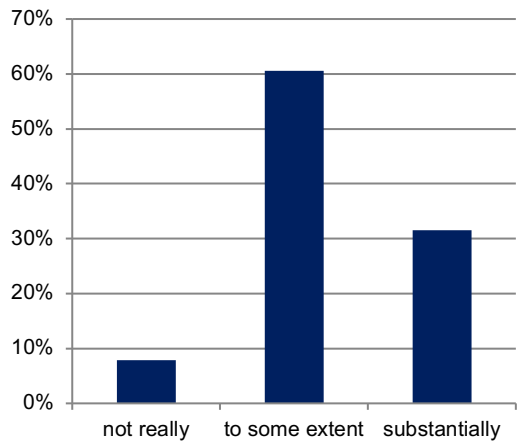
    a. Limitations to activity due to measures to contain the virus
    b. Loss of business due to drop in demand
    c. Production problems due to supply chains
    d. Deterioration in the financial environment

Representatives from 81 Free Zones in 41 countries responded. This chapter presents the results of the F-WEB Special Survey on the Coronavirus Pandemic. In addition to a global analysis, regionally disaggregated results are also presented in order to gain a better understanding of the consequences for Free Zones in different parts of the world.

4.2 Results at the Global Level

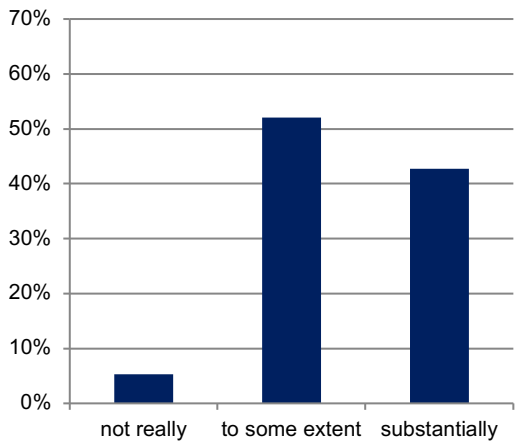
Most Free Zones worldwide are currently affected by the pandemic and expect limitations to activity to become worse in the coming months. Over 90 percent of Free Zones state that economic activity in their Free Zones is currently hampered by the spread of COVID-19 (Figure 74). While 60 percent of Free Zones report some limitations, over 30 percent report the impact of the pandemic to be severe. Only 8 percent of respondents indicate that their Free Zone is currently not really affected. Over the next few months, the impact is expected to intensify. Almost 95 percent of the participants expect to be affected by the pandemic in the future (Figure 75). Compared with the current situation, fewer Free Zones (52 percent) expect moderate consequences, while more than 40 percent see substantial negative impacts in the coming months.

Figure 74: Current degree of limitations to activity due to COVID-19 pandemic



Source: F-WEB survey.

Figure 75: Expected degree of limitations to activity due to COVID-19 pandemic

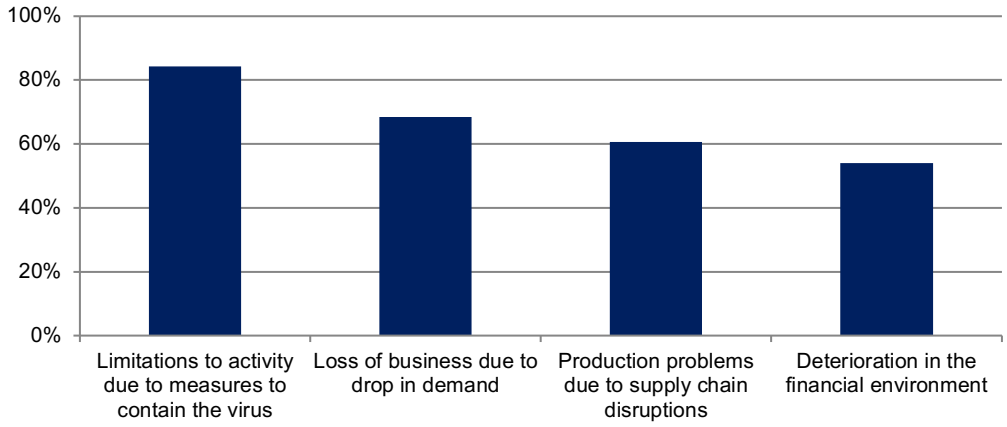


Source: F-WEB survey.

Free Zones are affected by the pandemic through various channels at the same time. Almost 85 percent of participating Free Zones report that activity in their Free Zone is or will be affected by measures to contain the spread of the disease (Figure 76). 68 percent report a loss of business due to the global drop in demand while 60

percent report production problems due to disruptions of supply chains. Also a deterioration of the financial environment due to the COVID-19 crisis is affecting (or is expected to affect) a substantial share of Free Zones – 54 percent. In sum, all transmission channels of economic effects seem to be relevant for Free Zones, although to a varying degree.

Figure 76: Transmission channels for the negative effects of the COVID-19 pandemic

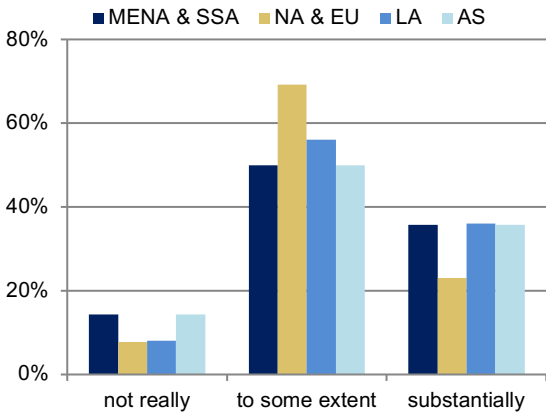


Source: F-WEB Survey.

4.3 Regional Analysis

Free Zones in all world regions are affected by the pandemic. Currently, Free Zones in all world regions report to be affected to a similar extent (Figure 77). Only in North America and Europe, Free Zones are somewhat less affected compared with other world regions, according to the F-WEB special survey. Regional heterogeneity is somewhat larger when it comes to expectations over the coming months. While almost all Free Zones independent of their location expect negative impacts of the pandemic over the coming months, the degree of expected limitations to activity varies somewhat across regions (Figure 78). In Africa and the Middle East, roughly two out of three Free Zones expect to be affected to some extent, the rest expect substantial negative consequences. In comparison, in North America and Europe as well as in Latin America a smaller share of Free Zones expects to be affected to some extent (56 and 50 percent, respectively) and a larger share (40 and 46 percent, respectively) expects substantial consequences. However, in those regions and as in Africa and the Middle East, Free Zones expecting some effects still outnumber those expecting a severe impact. This is not the case in Asia where half of all responding Free Zones expect substantial consequences.

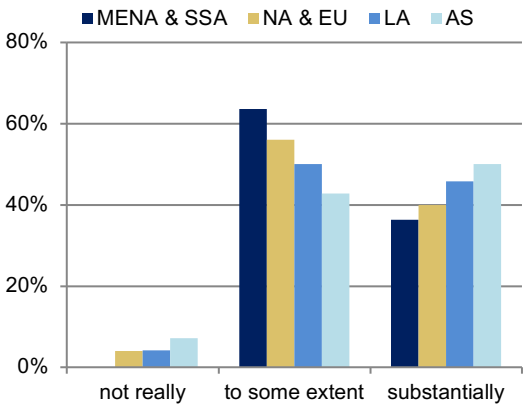
Figure 77: Current degree of limitations to activity due to COVID-19 pandemic by region



Note: Region acronyms: MENA (Middle East and North America), SSA (Sub-Saharan Africa), NA (North America), LA (Latin America and the Caribbean), EU (Europe), AS (Asia).

Source: F-WEB survey.

Figure 78: Expected degree of limitations to activity due to COVID-19 pandemic by region



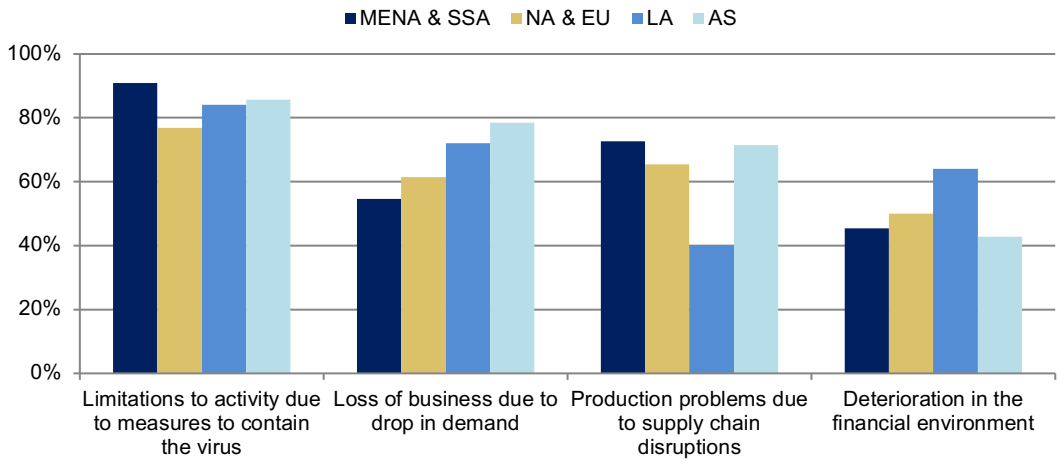
Note: Region acronyms: MENA (Middle East and North Africa), SSA (Sub-Saharan Africa), NA (North America), LA (Latin America and the Caribbean), EU (Europe), AS (Asia).

Source: F-WEB survey.

Free Zones in all regions worldwide are similarly affected by measures to contain the virus. Across world regions, between 77 and 91 percent of Free Zones report production limitations due to measures to contain the virus. The share of Free Zones affected via this channel is highest in the Middle East and Africa and lowest in North America and Europe.

Depending on their region of location, Free Zones are affected by the pandemic to a different extent via the demand, supply and financial channels. Across regions, a majority of Free Zones reports to be affected via the demand channel (Figure 79). The share of Free Zones reporting a loss of business due to a drop in global demand is highest in Asia (79 percent), followed by Latin America (72 percent), North America and Europe (62 percent), and Africa and the Middle East (55 percent). In all regions but Latin America, Free Zones are affected to a similar extent via the supply and the financial channel. Thus, between 65 and 73 percent of Free Zones report to face production problems due to supply chain disruptions and between 43 and 50 percent report consequences due to the deterioration in the financial environment. Latin America, however, is the only region where the deterioration in the financial environment is regarded as a transmission mechanism by more Free Zones (64 percent) than supply chain disruptions (40 percent).

Figure 79: Transmission channels for the negative effects of the COVID-19 pandemic



Note: Region acronyms: MENA (Middle East and North Africa), SSA (Sub-Saharan Africa), NA (North America), LA (Latin America and the Caribbean), EU (Europe), AS (Asia).

Source: F-WEB Survey.

4.4 Concluding Remarks

The F-WEB Special Survey provides first evidence how Free Zones around the globe are affected by the coronavirus pandemic via different channels. While most Free Zones around the globe already experience negative effects, expectations are that limitations to activity become even worse in the coming months. Measures to contain the spread of the disease are currently the main transmission channel of negative economic effects. However, a majority of Free Zones is also hit by the drop in demand, supply chain disruptions as well as the deterioration in the financial environment attributable to the COVID-19 crisis.

The next regular F-WEB survey scheduled for May will provide further insights into the impacts on the Free Zones community. The regular F-WEB questions on current and expected economic situation, as well as the questions on detailed dimensions of economic activity including turnover, investment, employment and profitability, are well suited to capture the effects of the pandemic on Free Zones. In addition, special questions on the COVID-19 pandemic will again be asked. By May, the economic consequences for individual Free Zones will also be clearer. Those who are on our F-WEB email list will receive an invitation for participation in May. Those who are not yet registered but would like to share their assessment with the community are invited to send an email to FWEB.worldfzo@ifw-kiel.de. A detailed description of the design of the survey and the F-WEB methodology, as well as all quarterly F-WEB reports, can be found in www.worldfzo.org .

5 The Way Forward – Road to Recovery

BY DR MOHAN GURUSWAMY AND DR SAMIR HAMROUNI

5.1 Introduction

Global economic outlook has deteriorated in recent weeks in the wake of Covid-19 pandemic. The impact has been severe, not only on human life and well-being, but also on the economic health of nations. Even advanced economies with strong healthcare infrastructure have been deeply affected.

Manufacturing and services sectors have suffered. Businesses are either locked down or operating at sub-optimal levels. Workers are being laid off. Capacity utilization has suffered. International trade has slowed. Global value chains are disrupted. Investments have dried up. Consumption demand has slowed markedly. Commodity prices (energy, industrial metals) have collapsed.

The pandemic has inflicted colossal economic cost. According to the International Monetary Fund (IMF), the cumulative loss of 2020-21 could reach $9 trillion, or the size of Germany's and Japan's economies, combined. By conservative estimates, this may result in, the world losing US$ 100 Billion every day of forced inactivity. The fall in stock markets and emerging market currencies bears witness to a tremendous loss of confidence as evidenced by the behavior of the stock market and debasement of emerging market currencies. We are set for the year 2020 going down in history as a challenging turning point of the 21st century.

In coordinated action, central bankers have dropped interest rates sharply and expanded liquidity. Governments have also announced fiscal stimuli to contain the negative impact of economic slowdown.

As at mid-April, it is unclear how soon the pandemic will come under reasonable control. At least three scenarios are possible. (a) Short-term: Pandemic contained in 1-2 months; (b) Medium-term: Pandemic contained in 3-4 months; and (c) Pandemic continues well beyond four months.

Even assuming the virus comes under control in 1-2 months, it may take 2-3 additional months for the real economy – production, consumption, marketing, world trade and so on - to gradually normalize or revert to its pre-Covid level. In that event, it is possible financial markets will rebound and commodity prices (energy, industrial metals) will start to rise from current low levels, in the second half of the year, driven by excess liquidity.

The Medium-term scenario means a worsening of already weak sentiment. In this case, financial stress will worsen. Companies may be forced to downsize. Lay-offs of workers, shortage of raw material, pile up of finished goods and cash crunch are likely to occur. Commodity markets will continue to languish because of demand erosion.

If, for any reason, the pandemic outbreak extends beyond 4-6 months (e.g. due to inadequate healthcare or recurrence), the risk of economic recession will become very real. This will inflict a demoralizing effect on businesses. Many will be forced to explore exit options which will increase the negative impact on finances and employment. The ripple effects might be disastrous. In the event of scenarios (b) and (c), all the markets will take a hit and it may take several quarters of staggered growth to return to a semblance of normalcy.

So, the world is currently facing an uncertain outlook characterized by VUCA (Volatility, Uncertainty, Complexity, Ambiguity) conditions.

As economic entities and key links of the Global Value Chain, Free Zones (FZs) cannot remain insulated from these uncertainties. However, hazards fueled by the ongoing VUCA conditions can be mitigated with smart risk management policies focused on resilience.

It is possible, we may not return to ‘business-as-usual’. If cataclysmic change in business sentiment were to occur, economic activity may remain flat (little growth) for an extended period of time. Addressing such an eventuality will require a radically different mindset.

5.2 Recommendations

The World FZO recommendations are presented below for the consideration of our constituent members. We are conscious there may be unique country-specific or region-specific challenges that will also affect FZs. **These recommendations are indicative and by no means exhaustive.**

1. **Recognize the possibility of three different scenarios**: Short-term; Medium term; and Beyond. In such uncertain times, FZs should conduct an in-depth internal analysis to assess their Resilience. Based on internal financial and non-financial strengths and weaknesses, work out action plans for each of the scenarios. It is safer to assume worst case scenario and start working to maximize economic benefits in that scenario. Plan for the worse, hope for the best.

2. **Go digital in all transactions**. This is a great opportunity to introduce Tech-ready systems. As part of Free Zone of the Future Program (**Free Zone 4.0**), one of the certifications being developed by World FZO is Smart-Zone certification. This would further enable free zones to transform themselves into a 'lean and mean' organization.

3. **Review all business processes for scale, efficiency and effectiveness** including management of inventory, manpower, finance, trade and technology. Use the opportunity to optimize the scale of operations (maximize benefits, minimize costs). This is also a good opportunity to focus on Capability development through retraining, re-skilling or up-skilling employees /workers.

4. **Review long-term strategic plans and Business Performance management systems**. Tools to measure, monitor and improve performance must be examined to adopt productivity enhancement measures. Now is the time to explore new vendors, new customers, new markets and develop strategies to capture them.

5. **Explore new methods of financing.** Interest rates are currently low and considerable liquidity has entered the banking system. It is advisable to make full use of ultra-loose monetary policy and stimulus packages initiated by many governments. FZs can make a case, either as independent entities or through local and regional free zone associations, to policymakers for additional incentives or benefits.

6. **Introduce an Enterprise Risk Management (ERM) Framework.** Formulating and implementing a Risk management strategy and policy in all areas of free zone is critical – production risk, process risk, quality risk, market risk, currency risk. In case of exposure to a commodity, hedge price risk through derivatives exchange. Imperative for successful decision making and for driving value in free zones, such a framework needs top management commitment and the engagement of all stakeholders.

World FZO's 'Free Zone of the Future' (FZF), **Free Zone 4.0**, is a unique initiative designed to make free zones 'future ready'. Its flagship Izdihar Index ('Prosperity' in Arabic) introduces appropriate metrics for all key elements of the FZF program. The Index is built on 4 Pillars and a tracking methodology. The base pillar is Business Excellence and Economic contribution (BEEC), supporting 3 core pillars of Best in Class, Innovation and Sustainability.

Each of the core pillars include three elements each: Best in Class (Knowledge based, Safe Zone, Tech-Ready Zone), Innovation (Entrepreneurial, SME Development, Innovative Zone), and Sustainability (Environment Friendly, Good place to Work and Socially Responsible).

Implementing the Free Zone 4.0 Program is recommended for FZs to achieve faster recovery from the crisis situation as well as develop capabilities to be more dynamic and resilient, and become future-ready.

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