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# Free Zones World Economic Barometer

## F-WEB NOTE 2018-Q4

**The World Free Zones Organization, in cooperation with the Kiel Institute for the World Economy, has launched the Free Zones World Economic Barometer (F-WEB) a quarterly, survey-based sentiment indicator designed to gauge current momentum and future trends of economic activity in free zones around the globe. The results of the 2018Q4 round, conducted in the second half of November, suggest that economic conditions in free zones worldwide have improved compared with the previous quarter. Half of the free zones regard their current economic situation as good, up from 32 percent in 2018Q3, and followed by 44 percent that consider the current activity normal. Only 6 percent experience poor conditions. This translates into an F-WEB Economic Conditions Index of 44. While this is a considerable improvement compared to the situation last quarter where the indicator value was 25, it is still below the level in the first half of the year. Despite the improvement in current economic conditions, the outlook for the next three months has deteriorated. The F-WEB indicator dropped from a stable 64 over the past six months to 44 in 2018Q4.**

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.

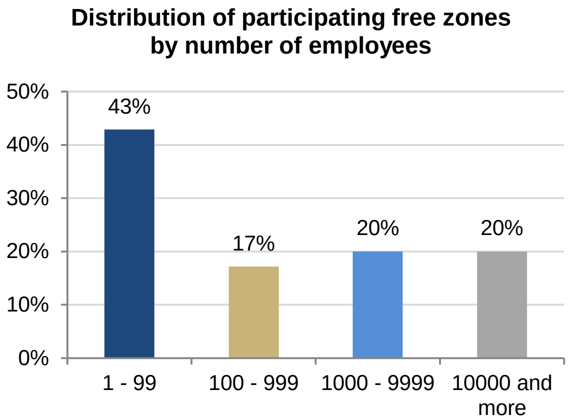
The aim of the F-WEB is to condense the available information into easily interpretable indicators. To this end, positive answers get the value of 100 and negative answers the value of -100. Neutral answers get the value of 0. Our indicator value is then calculated as the aggregate value of received 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.

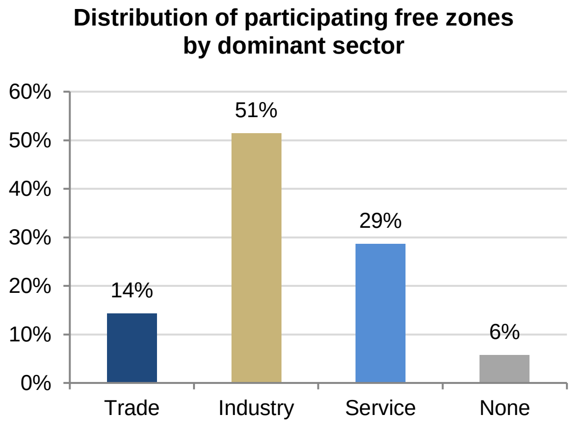
In this note, we present a summary of the results from 2018Q4, the fourth round of F-WEB. An extensive description of the questionnaire can be found in the first World Free Zones Economic Outlook produced by the World Free Zones Organization in cooperation with the Kiel Institute for the World Economy.

# F-WEB 2018-Q4 RESULTS

## GENERAL INFORMATION

The 2018Q4 survey is the fourth round of the newly established F-WEB. It was conducted between November 19 and December 5, 2018. Representatives of 40 free zones in 22 countries worldwide participated in the survey. While in the 2018Q3 round of F-WEB, the number of respondents was relatively evenly spread over free zones with less than 100 employees, zones with 100 to 999 employees and zones with over 1000 employees, in 2018Q4 the majority (43 percent) of responses came from small free zones with less than 100 employees.



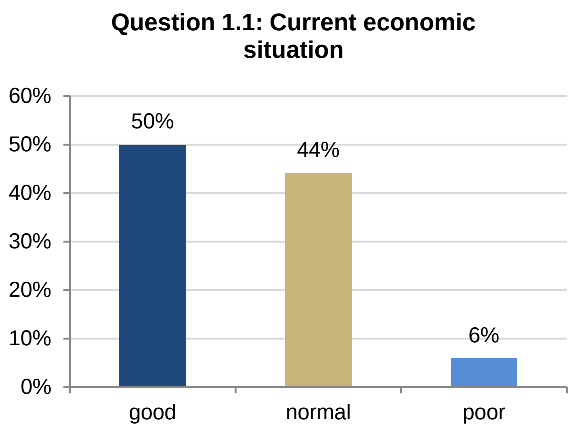



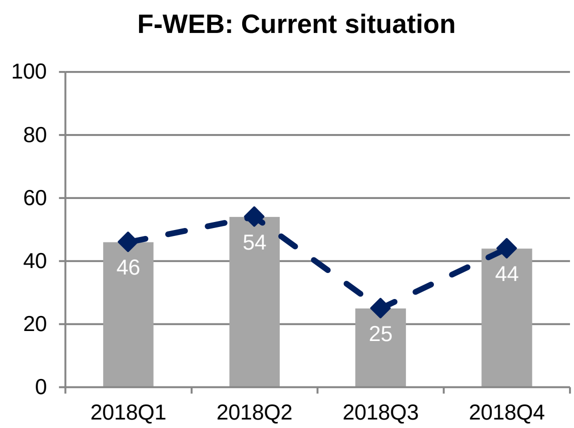

More than 50 percent of free zones that participated focus on industrial activities. 14 percent of the responding free zones report trade as their dominating sector; 29 percent focus on services. Compared to the previous rounds of F-WEB, this reflects a shift towards service-oriented free zones that almost doubled their relative share. Only a very small number of free zones has no clear focus on a specific sector.

## 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?"**

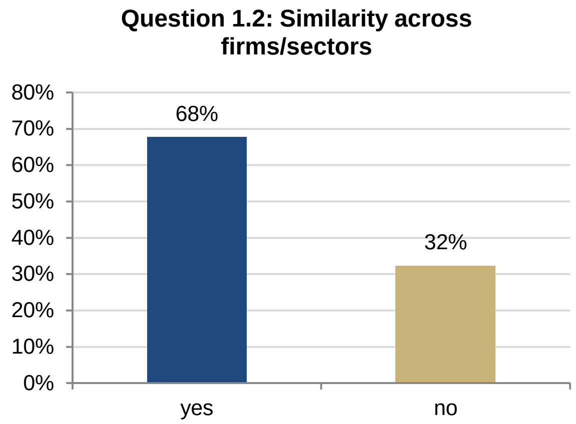


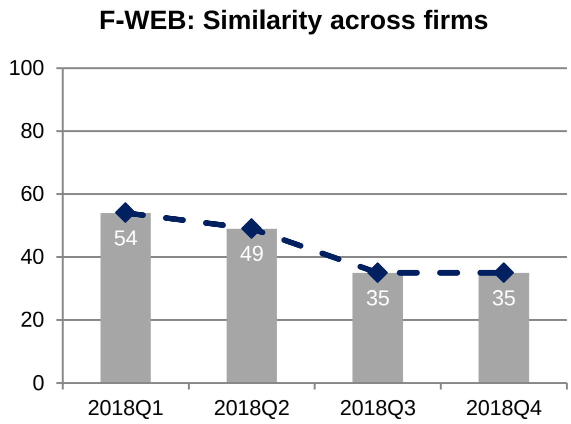



Half of the representatives of free zones that answered the F-WEB survey regard the current economic situation as good, followed by 44 percent that consider the situation normal. Only 6 percent experience poor conditions. The corresponding F-WEB indicator value is 44. This is a considerable improvement compared to the situation last quarter but still below the values in the first half of the year. In the 2018Q3 round, the share of free zones reporting a better than normal economic situation was at 32 percent; the majority of 61 percent evaluated the situation as normal, while a similar share reported a poor business situation.

## 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)?"**




A majority of free zones report that all firms or sectors, respectively, in their free zone experience similar economic situations (68 percent). One in three free zones, on the other hand, describes the situation of sectors/firms in the free zone as substantially diverse. The responses are thus almost the same as in 2018Q3. The F-WEB indicator for similarity of economic conditions across firms/sectors is unchanged at 35.

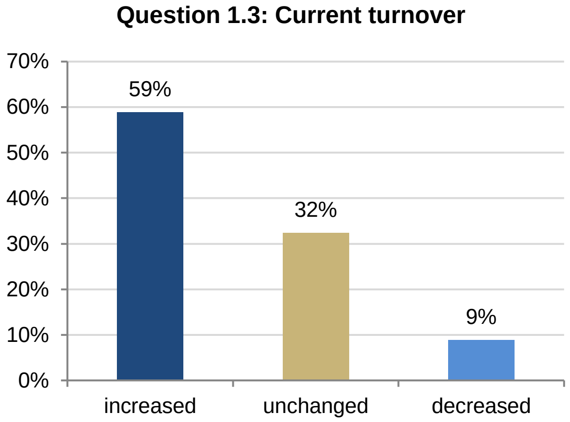
## Detailed dimensions

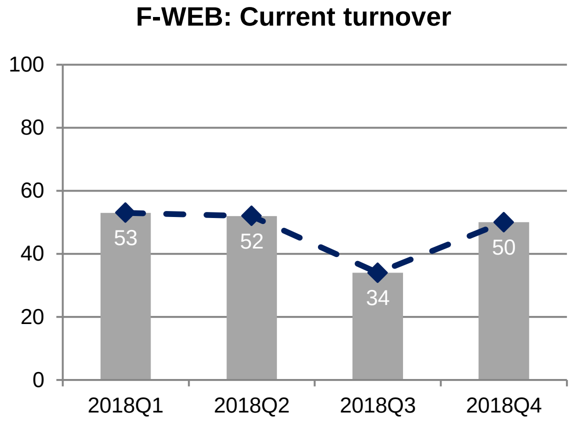
**Questions 1.3-1.6 relate to recent developments in more detailed economic dimensions: "Compared to the previous three months and taking into account the usual seasonal pattern…" how has turnover/employment/investment/profitability developed?**

In general, more than half of the free zones report positive economic developments regarding turnover, employment, investment, and profitability over the last three months. At the same time, the share of free zones reporting worse economic performance compared to the previous three months is low at between 3 and 9 percent.

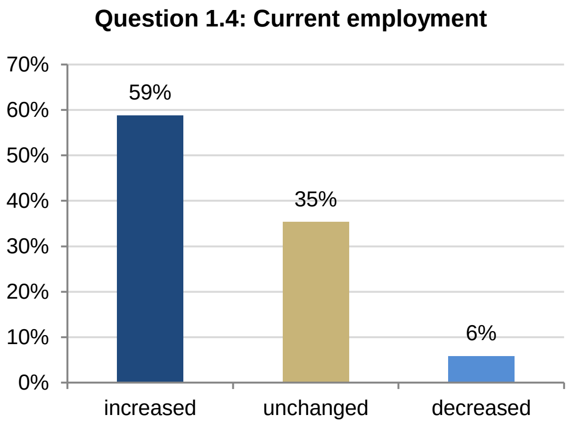
The responses translate into – for most economic dimensions substantially – higher values of the corresponding F-WEB indicators in 2018Q4 compared with 2018Q3 when respondents reported especially poor performance in profitability and turnover. The F-WEB indicators for turnover (50), employment (53) and investment (59) are (almost) back at their level 2018Q2. The profitability indicator also increased considerable from 34 in 2018Q3 to 47. However, it failed to reach the 2018Q2 high of 63.

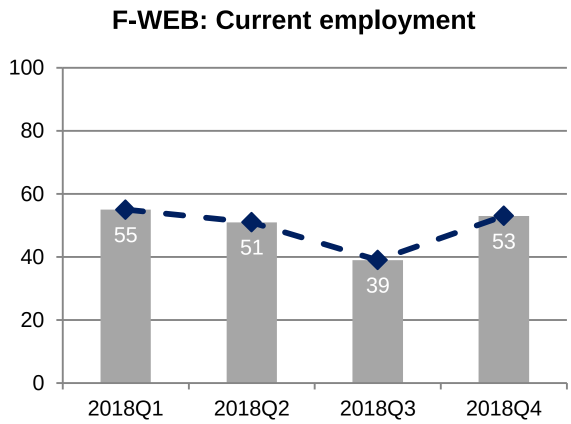
In the case of **turnover**, 59 percent of respondents saw an increase with respect to the previous three months, 32 percent experienced hardly any change, and 9 percent report decreasing business activity. The corresponding F-WEB indicator value for current turnover in 2018Q3 is 50, substantially above last quarter's value of 34. Thus, the turnover indicator is almost back to its level in the first half of 2018.



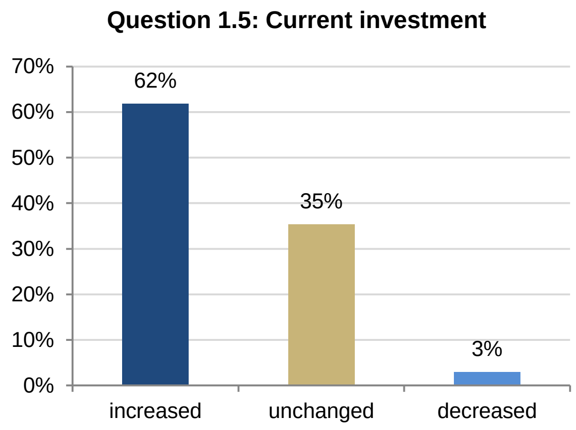



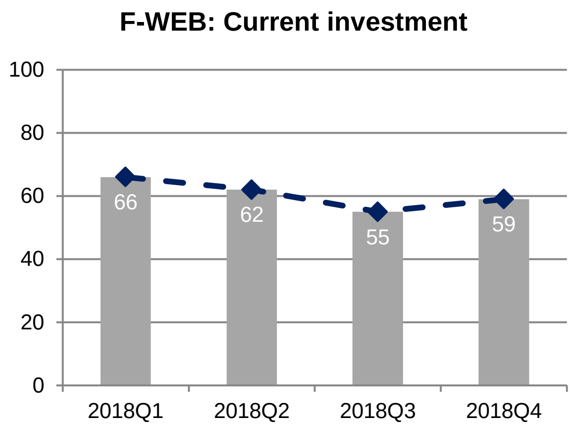

**Employment** has increased compared to the previous three months in 59 percent of the free zones, slightly more than in Q3, and similar to recent turnover development. The share of free zones reporting negative developments in terms of employment is slightly lower compared to the result for turnover, at 6 percent. As a result, the F-WEB indicator for current employment at 53 is somewhat higher than the F-WEB for turnover. Thus, the overall development is similar: the employment indicator also bounced back from the plunge in 2018Q3 to the level reached in the first half of 2018.



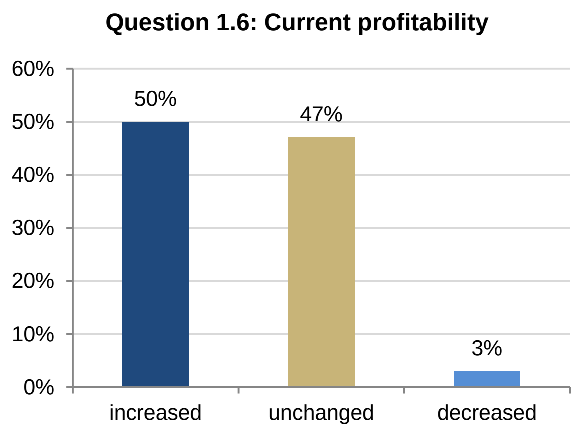



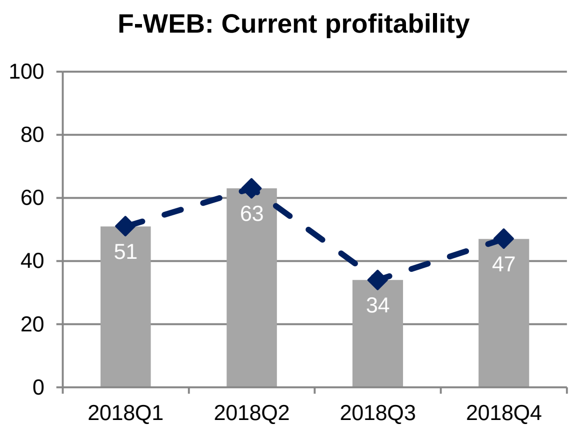
The assessment of the recent evolution of **investment** remains more positively compared to the other dimensions of economic performance, with 62 percent of free zones reporting increasing investment (similar to Q2 and Q3 with 62 and 61 percent, respectively). Only 3 percent of respondents experienced deteriorating investment, down from 7 percent last quarter. Therefore, the F-WEB indicator for current investment has increased to 59 from 55 2018Q3.



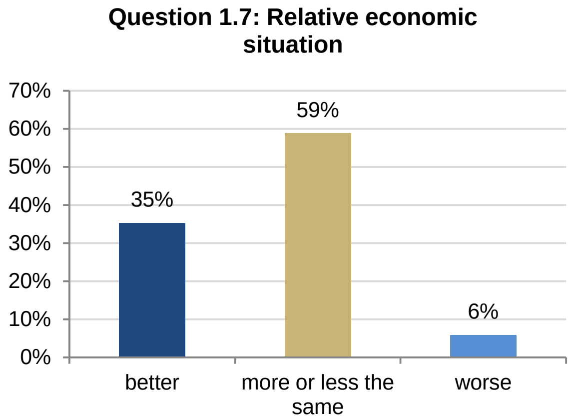

**Profitability** has increased over the past three months in half of the free zones, a similar outcome as in the previous round of F-WEB. The share of negative answers came down substantially from 14 percent in 2018Q3 to 3 percent now. As a result, the F-WEB indicator for current profitability has bounced back to 47, up from 34. However, it is still below the performance in the first half of 2018 where the F-WEB was at 51 and 63 in Q1 and Q2, respectively.

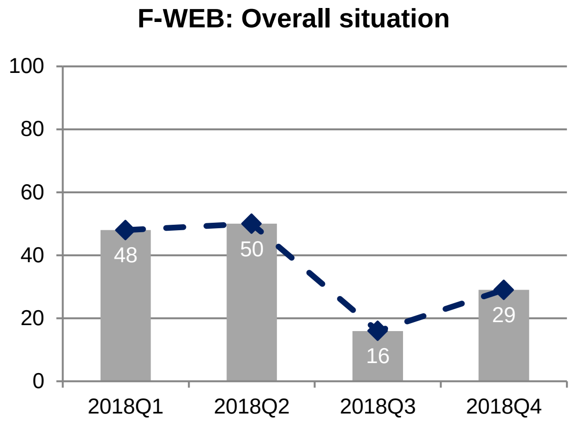


## Relative assessment

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



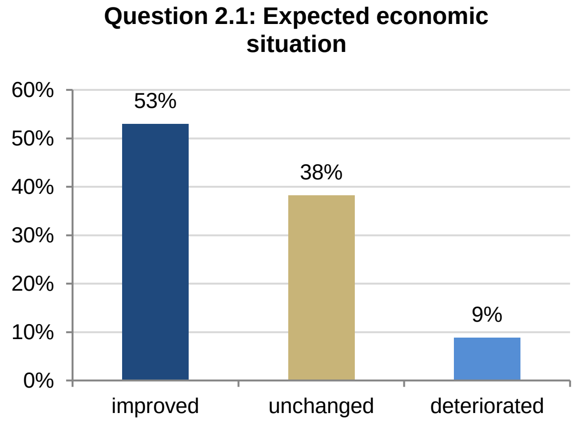



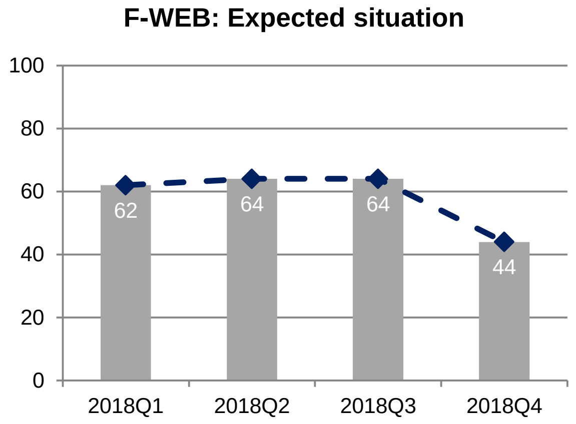

Most participating free zones (59 percent) have faced a similar economic situation in the past three months as their host countries in general. While 35 percent outperformed with respect to the rest of the country, 6 percent of free zones report a more negative economic situation. The resulting F-WEB indicator for relative performance of free zones is at 29 and thus – similar to the indicators of economic performance – higher than in the previous quarter but still below the values of the first half of 2018.

## 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?”**



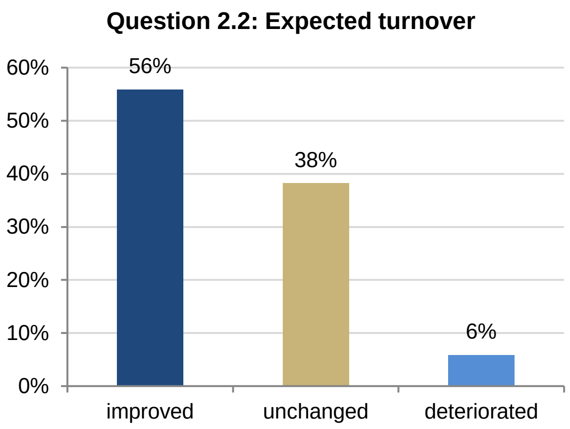

Despite the current economic performance being more positive than in the previous quarter, expectations on future business conditions and performance have worsened. While a majority of 53 percent of free zones still has a positive outlook and the share of free zones expecting negative developments continues to be below 10 percent, the answers reflect a deterioration compared with the 2018Q3 round of F-WEB where 68 percent had positive and only 5 percent had negative expectations. Accordingly, the F-WEB indicator dropped from a stable 64 over the past six months to 44 in 2018Q4.

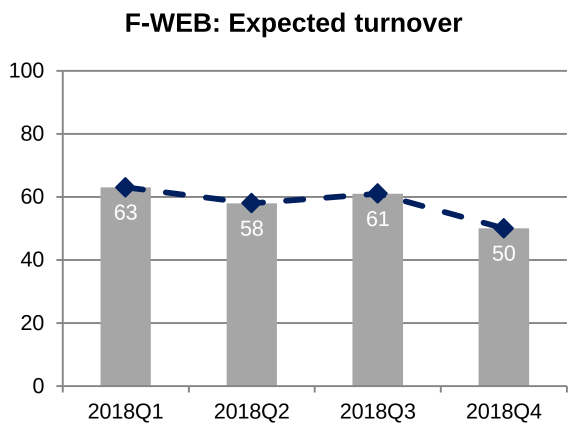
### Detailed dimensions

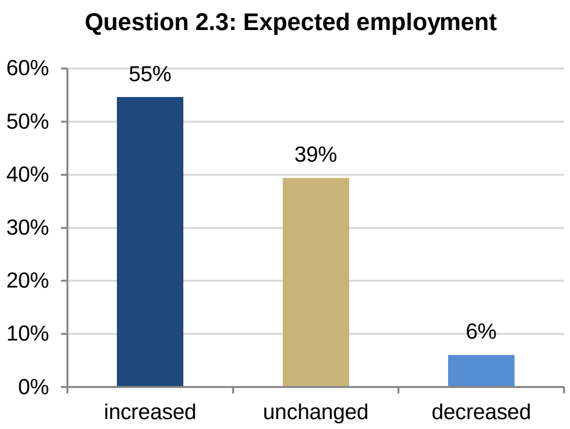
**Questions 2.2–2.5 relate to the expectations for developments in specific economic dimensions in the near future: “Overall, compared to the current situation, how do you expect developments in your Free Zone over the next 3 months” … regarding turnover, employment, investment and profitability, respectively?**

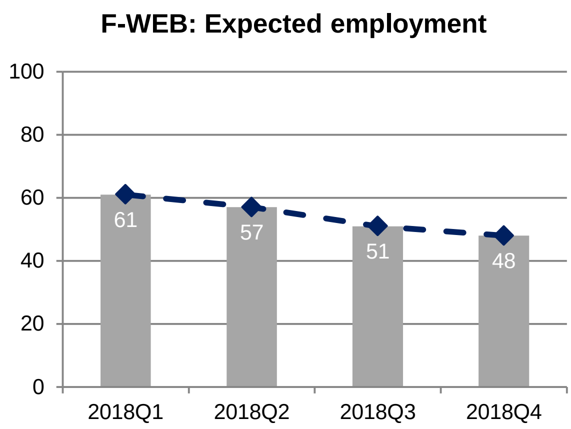
The outlook of respondents with respect to turnover, employment, investment and profitability over the next three months has become less optimistic, on average. Regarding expected turnover, employment and investment, more than half of the free zones still have a positive outlook for the next three months. Less than half of the respondents (44 percent) expect profitability to increase over the next quarter. The share of negative answers has increased somewhat for all dimensions but employment, and is most pronounced for expected investment and profitability where 9 percent of the survey participants anticipate deteriorating future performance (up from 0 and 2 percent, respectively).

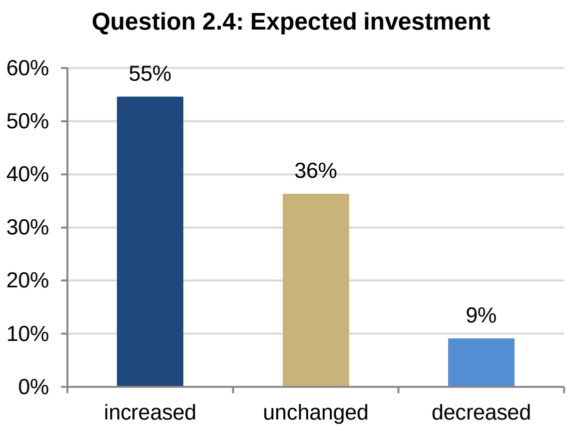
This development is reflected in the corresponding F-WEB values. The indicator for expected investment recorded the most pronounced fall in absolute terms from 69 in 2018Q3 to 45 in the current quarter. The drop was similarly strong regarding the profitability outlook which is down to 35 from 56 in the previous quarter. The F-WEB indicator for expected turnover decreased from 61 in 2018Q3 to 50, while the indicator for expected employment experienced the most gradual decline from 51 to 48, thus continuing its downward trend since the beginning of the year.

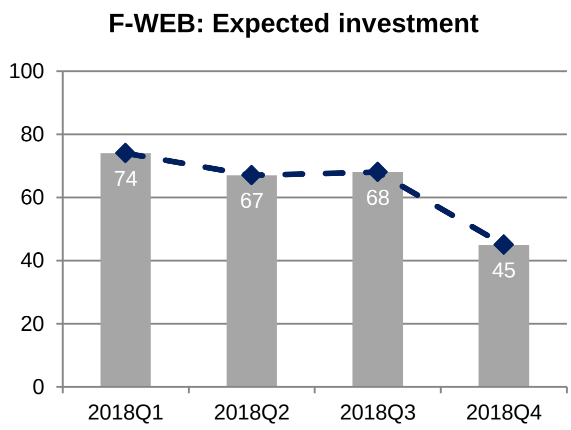

Question 2.2: Expected turnover
60%
50%
40%
30%
20%
10%
0%
56%
38%
6%
improved
unchanged
deteriorated

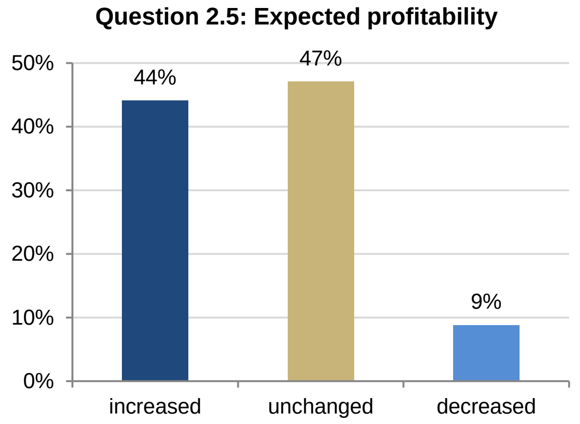

F-WEB: Expected turnover
100
80
60
40
20
0
63
58
61
50
2018Q1
2018Q2
2018Q3
2018Q4

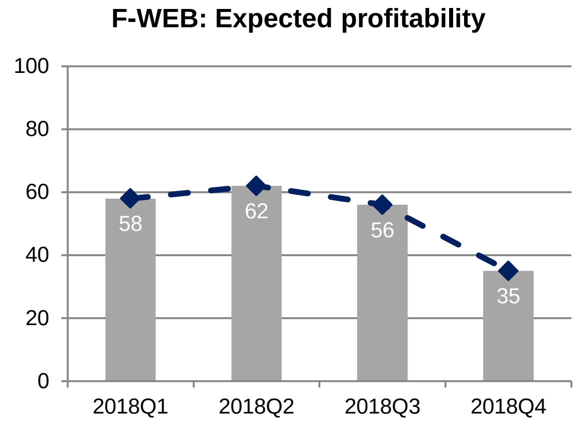

Question 2.3: Expected employment
60%
50%
40%
30%
20%
10%
0%
55%
39%
6%
increased
unchanged
decreased


F-WEB: Expected employment
100
80
60
40
20
0
61
57
51
48
2018Q1
2018Q2
2018Q3
2018Q4


Question 2.4: Expected investment
60%
50%
40%
30%
20%
10%
0%
55%
36%
9%
increased
unchanged
decreased


F-WEB: Expected investment
100
80
60
40
20
0
74
67
68
45
2018Q1
2018Q2
2018Q3
2018Q4




## SPECIAL FOCUS QUESTIONS

In this section of the questionnaire we ask questions regularly, but at a lower than quarterly frequency, or spontaneously in response to specific economic or political developments that may have an impact on free zones. In the 2018Q4 F-WEB survey, two special questions were asked.

**Special Question 1: How was business activity in your free zone in the last year affected by the rising number of free zones worldwide?**

The free zone approach continues to gain importance and thus, the number of free zones worldwide has increased substantially over the past decades. According to a rigorous study by the World Free Zones Organization, there were 2198 free zones active in 2017. Based on varying definitions of free zones, also called (special) economic zones, estimations by some international organizations come to even higher numbers. Free zones policies are increasingly promoted in developing countries by several multilateral agencies such as the World Bank and the United Nations Organization for Industrial Development.

Against this background, the question arises to what extent existing free zones are affected by the rising number of free zones worldwide. On the one hand, the increasing quantity of free zones reflects the growth in popularity – existing zones can thus benefit from increased attention towards the free zone approach and a growing network of peers. At the same time, this development also implies more competition among free zones when trying to attract investors. Therefore, a priori both positive and negative answers to Special Question 1 are possible.

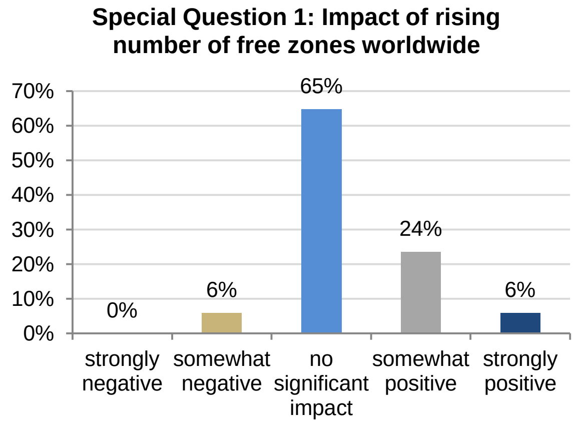
According to the results of Special Question 1, the overall impact of the rising quantity of free zones is positive, on average. While 65 percent of respondents have not experienced any effect over the past year, a total of 30 percent of free zones have benefitted from the free zones boom: 24 percent report some positive effects and 6 percent have even experienced substantial gains. Only 6 percent of participants report somewhat negative impacts. All in all, these results suggest that positive effects resulting from the prominence of the free zones approach and potential network effects outweigh the negative effects that can arise from increased competition among free zones worldwide.

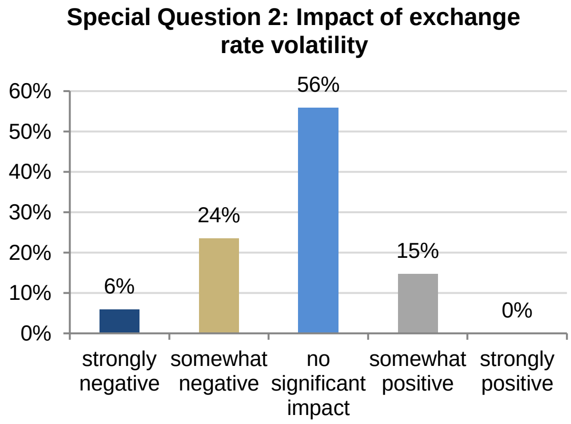
**Special Question 2: Have fluctuations in the exchange rate of your host country's currency vis-à-vis the US-dollar affected business activity in your free zone over the past three months?**

Recently, emerging and developing economies have been facing challenges as financial conditions have tightened. Since interest rates in the US have increased faster than expected due to favorable US economic conditions and additional fiscal stimulus, emerging and developing economies' currencies have come under pressure as investors have withdrawn funds. So far, Argentina and Turkey have been hit the most, with significant implications for the real economy. However, other countries – including some of the survey participants' locations such as India, Uruguay or Liberia – have also experienced significant depreciations vis-à-vis the US-dollar throughout 2018.

The exchange rate effects for free zones are ambiguous. On the one hand, a depreciation of the host countries' currency vis-à-vis the US-dollar has the potential to boost exports since domestic goods become more competitive on the world market. However, there are caveats to this impact channel. Most importantly, free zones often import a large share of intermediate goods which become more expensive as a result of the exchange rate depreciation. This, in turn, harms global competitiveness. On the other hand, the exchange rate fluctuations experienced recently by many developing and emerging economies have been accompanied by high economic uncertainty. The reason is that the risk of contagion through the global financial system is generally high among emerging economies as differentiation of investors between assets from different emerging markets tends to be limited. While this risk has not materialized, investors may have been more cautious in the presence of uncertainty.

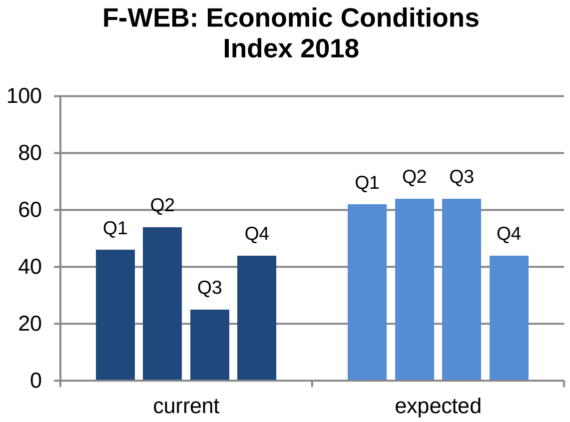
The responses to Special Question 2 show that more than half of the free zones (56 percent) have not been significantly affected by exchange rate volatility over the past six months. Among these responses are, not surprisingly, free zones from countries that were not subject to unusual degrees of exchange rate volatility. But also some free zones from countries with substantial devaluations of their currencies report little impact from movements in their host countries' exchange rate (examples are free zones in Uruguay and Colombia). The average effect is nevertheless negative, on average. A total of 30 percent of respondents report somewhat (24 percent) or strongly negative (6 percent) impacts of exchange rate volatility. Only 15 percent of free zones have benefitted somewhat from exchange rate effects, but no substantial gains in competitiveness have emerged. Interestingly, the responses are not equal among free zones in the same country. For example, some Turkish free zones report somewhat positive exchange rate effects, others report somewhat negative consequences.

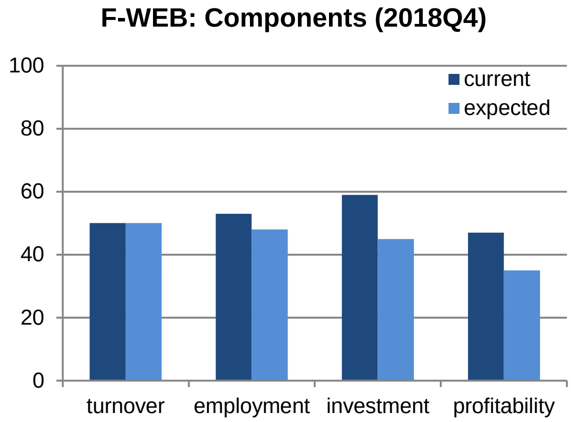


## SUMMARY

In 2018Q4, the F-WEB survey indicates that economic conditions in free zones worldwide have improved compared to the previous quarter. Half of free zones regard the current economic situation as good, up from 32 percent in 2018Q3, followed by 44 percent that consider the current activity normal. Only 6 percent experience poor conditions. This translates into an F-WEB Economic Conditions Index of 44. While this is a considerable improvement compared to the situation last quarter where the indicator value was 25, it is still below the values in the first half of the year. Despite the improvement in current economic conditions, the outlook for the next three months has deteriorated. Accordingly, the F-WEB indicator dropped from a stable 64 over the past six months to 44 in 2018Q4.




A closer look at the various elements of business activity – i.e. turnover, employment, investment, and profitability – reveals that economic performance has improved across all dimensions, most notably regarding turnover, profitability, and employment. However, the outlook for the next three months has deteriorated significantly – particularly for investment and profitability – after having been stable at a high level since the beginning of 2018. Nevertheless, free zones reporting a positive outlook still outnumber by a large margin those reporting negative expectations.