

## **THE ROLE OF FREE ECONOMIC ZONES (FEZS) IN ATTRACTING FOREIGN DIRECT INVESTMENT (FDI): THE CASE OF SOUTH KOREA**

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### **ABSTRACT**

*This paper explores the role of Free Economic Zones (FEZs) in attracting Foreign Direct Investment (FDI) in South Korea. FEZs are designated areas that offer preferential policies and incentives to foreign investors, such as tax preferences, regulatory support, and advanced infrastructure. This study investigates the effectiveness of these zones in enhancing FDI inflows and their impact on the South Korean economy. Through an analysis of policy frameworks, economic data, and specific case studies, FEZs have contributed to increased foreign investments, job creation, export growth, and regional development were studied in this paper. Despite these successes, the study also highlights challenges such as competition from other countries, and sustainability concerns. The findings suggest that while FEZs have been instrumental in driving economic growth, further policy enhancements are necessary to sustain their attractiveness and effectiveness in a competitive global environment.*

**Key words:** *Free Economic zones (FEZ), Foreign Direct Investment (FDI), export, economic growth*

## **ERKIN IQTISODIY HUDUDLARNING TO‘G‘RIDAN-TO‘G‘RI XORIJIY INVESTITSIYALARNI JALB QILISHDAGI ROLI: JANUBIY KOREYA MISOLIDA**

### **ANNOTATSIYA**

*Ushbu maqola Janubiy Koreyada to‘g‘ridan-to‘g‘ri xorijiy investitsiyalarni (TTXI) jalb qilishda erkin iqtisodiy zonalarning (EIZ) rolini o‘rganadi. Erkin iqtisodiy hududlar xorijiy investorlarga soliq imtiyozlari, ma‘muriy qo‘llab-*

*quvvatlash va ilg'or infratuzilma kabi imtiyozlarni taklif qiluvchi belgilangan maxsus tartib amal qiluvchi hududlardir. Ushbu tadqiqot ushbu zonalarining to'g'ridan-to'g'ri xorijiy investitsiyalar oqimini oshirishdagi samaradorligini va ularning Janubiy Koreya iqtisodiyotiga ta'sirini o'rganadi. Ushbu maqolada erkin iqtisodiy hududlarning ma'muriy-huquqiy asoslari, iqtisodiy ma'lumotlar va aniq misollarni tahlil qilish orqali xorijiy investitsiyalar, yangi ish o'rinlari yaratish, eksport o'sishi va mintaqaviy rivojlanishga hissasi o'rganiladi. Ushbu maqolada erishilgan natijalar bilan birgalikda, boshqa mamlakatlarning raqobati va barqarorlik muammolari kabi muammolarga ham e'tibor qaratiladi. Natijalar shuni ko'rsatadiki, EIZlar iqtisodiy o'sishni rag'batlantirishda muhim rol o'ynagan bo'lsa-da, raqobatbardosh global muhitda ularning jozibadorligi va samaradorligini saqlab qolish uchun iqtisodiy siyosatni yanada takomillashtirish zarur.*

**Kalit so'zlar:** *Erkin iqtisodiy zonalar (EIZ), to'g'ridan-to'g'ri xorijiy investitsiyalar (TTXI), eksport, iqtisodiy o'sish*

## **РОЛЬ СВОБОДНЫХ ЭКОНОМИЧЕСКИХ ЗОН (СЭЗ) В ПРИВЛЕЧЕНИИ ПРЯМЫХ ИНОСТРАННЫХ ИНВЕСТИЦИЙ (ПИИ): НА ПРИМЕРЕ ЮЖНОЙ КОРЕИ**

### **АННОТАЦИЯ**

*В данной статье исследуется роль свободных экономических зон (СЭЗ) в привлечении прямых иностранных инвестиций (ПИИ) в Южную Корею. СЭЗ — это обозначенные территории, которые предлагают преференциальную политику и стимулы для иностранных инвесторов, такие как налоговые преференции, нормативная поддержка и развитая инфраструктура. В этом исследовании изучается эффективность этих зон в увеличении притока прямых иностранных инвестиций и их влияние на экономику Южной Кореи. Посредством анализа политических рамок, экономических данных и конкретных тематических исследований в этой статье были изучены СЭЗ, которые способствовали увеличению иностранных инвестиций, созданию рабочих мест, росту экспорта и региональному развитию. Несмотря на эти успехи, исследование также выдвигает на первый план такие проблемы, как конкуренция со стороны других стран и проблемы устойчивого развития. Результаты показывают, что, хотя СЭЗ сыграли важную роль в стимулировании экономического роста, необходимы дальнейшие улучшения политики для поддержания их привлекательности и эффективности в конкурентной глобальной среде.*

*Ключевые слова: свободные экономические зоны (СЭЗ), прямые иностранные инвестиции (ПИИ), экспорт, экономический рост.*

## **INTRODUCTION**

Foreign Direct Investment (FDI) is a vital driver of economic growth, providing capital, technology transfer, and managerial expertise that can significantly enhance the productive capacities of a host country. Recognizing the importance of FDI, many nations have implemented various strategies to attract foreign investors, with Free Economic Zones (FEZs) being one of the most prominent tools. FEZs are specially designated areas within a country where businesses benefit from preferential policies, including tax incentives, streamlined regulations, and superior infrastructure, aimed at creating a conducive environment for foreign investment.

South Korea, an exemplar of rapid industrialization and economic advancement, has effectively utilized FEZs as part of its broader economic strategy. The country's transition from a war-torn economy in the mid-20th century to a global industrial powerhouse by the early 21st century is largely attributed to its open economic policies and strategic investment initiatives. As of today, South Korea hosts several FEZs, each with its unique focus and advantages, such as the Incheon Free Economic Zone (IFEZ), the Busan-Jinhae Free Economic Zone (BJFEZ), and the Gwangyang Bay Area Free Economic Zone (GFEZ).

The purpose of this paper is to delve into the role of FEZs in attracting FDI to South Korea, examining how these zones contribute to the nation's economic objectives. The analysis will cover the policy frameworks that underpin the establishment and operation of FEZs, the economic impacts they generate, and the specific advantages they offer to foreign investors. Additionally, this study will identify the challenges FEZs face and propose recommendations to enhance their effectiveness.

By investigating the South Korean model, this paper aims to provide valuable insights into the efficacy of FEZs as a mechanism for attracting FDI and fostering economic development. The findings could serve as a useful reference for other countries looking to implement or improve their own FEZ strategies to better compete in the global market. Through a detailed exploration of South Korea's FEZs, this paper will highlight both the successes and the areas requiring further improvement to ensure sustained economic growth and competitiveness.

## **LITERATURE REVIEW**

The concept of FEZs is rooted in economic theories related to spatial economics, agglomeration economies, and trade liberalization. FEZs aim to create a favorable

investment climate by reducing barriers to trade, offering fiscal incentives, and providing superior infrastructure. According to Ghazalian (2023) the creation of such zones can foster competitive advantages by concentrating resources and economic activities in specific regions, thus benefiting from agglomeration economies. These zones serve as testing grounds for broader economic reforms and can enhance a country's overall investment climate. Johansson and Nilsson (1997) argue that FEZs can reduce operational costs and risks for foreign investors, thereby increasing their attractiveness compared to non-FEZ regions.

**South Korean Experience with FEZs.** South Korea's experience with FEZs offers valuable insights into their effectiveness as a tool for attracting FDI. The country has established several FEZs since the early 2000s, including the Incheon Free Economic Zone (IFEZ), Busan-Jinhae Free Economic Zone (BJFEZ), and Gwangyang Bay Area Free Economic Zone (GFEZ). These zones have been instrumental in transforming South Korea into a regional economic hub. Lee (2022) provide an in-depth analysis of the IFEZ, highlighting its success in attracting high-tech industries and multinational corporations. They attribute this success to the zone's strategic location near Incheon International Airport, comprehensive infrastructure, and targeted incentives for specific industries.

Comparative studies offer a broader perspective on the effectiveness of FEZs. Farole and Akinci (2011) analyze FEZs in various countries, including China, the United Arab Emirates, and India, highlighting the factors that contribute to their success. They argue that while tax incentives are important, factors such as political stability, market access, and the quality of infrastructure are equally crucial.

Jong-Wha Lee (2016) provide critical evaluations of FEZs in South Korea and China, noting that while these zones can attract significant FDI, their impact on broader economic development is mixed. Issues such as labor exploitation, environmental degradation, and economic enclaves can limit the positive spillover effects of FEZs.

## **METHODS**

The basis of the research methods is the work carried out in our country to increase GDP. In the analysis process, comparison, systematic analysis methods were used. Based on the statistics, the indicators of GDP growth are considered.

## **RESULTS AND DISCUSSION**

1. FDI Inflows into FEZs. The analysis of FDI data from 2003 to 2023 reveals a significant increase in foreign investment within South Korea's Free Economic Zones

(FEZs). The Incheon Free Economic Zone (IFEZ) attracted the highest volume of FDI, followed by the Busan-Jinhae Free Economic Zone (BJFEZ) and the Gwangyang Bay Area Free Economic Zone (GFEZ). Key findings include:

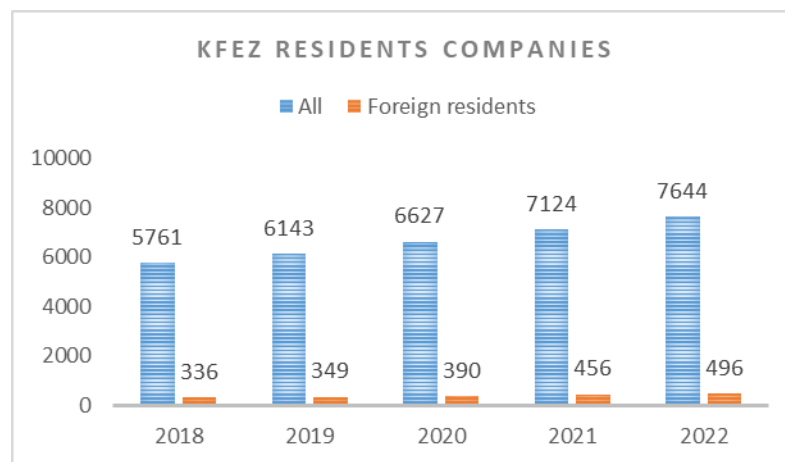
- Incheon Free Economic Zone (IFEZ): IFEZ experienced a steady growth in FDI, with major investments in logistics, biohealth, and information technology sectors. Notable investors include multinational corporations like Samsung Biologics and GE Healthcare.

- Busan-Jinhae Free Economic Zone (BJFEZ): BJFEZ attracted significant investments in maritime industries, shipbuilding, and logistics. Companies like Hyundai Heavy Industries and CMA CGM have established substantial operations in this zone.

- Gwangyang Bay Area Free Economic Zone (GFEZ): GFEZ saw considerable investments in steel production, petrochemicals, and logistics. POSCO and LG Chem are among the prominent investors.

Figure 1.

**KFEZ Residents companies<sup>1</sup>**



2. Economic Impact of FEZs. The economic performance indicators show that FEZs have positively impacted South Korea's economy. Key impacts include:

- Job Creation: FEZs have generated substantial employment opportunities.

- Export Growth: The zones have significantly boosted export volumes. The GFEZ, with its strong industrial base, contributed notably to South Korea's steel and petrochemical exports.

<sup>1</sup> [Korean Free Economic zones Major statistics \(fez.go.kr\)](https://www.fez.go.kr/fezstat/eng) https://www.fez.go.kr/fezstat/eng

- Regional Development: FEZs have promoted balanced regional development, reducing economic disparities between the capital region and other parts of the country.

Figure 2.

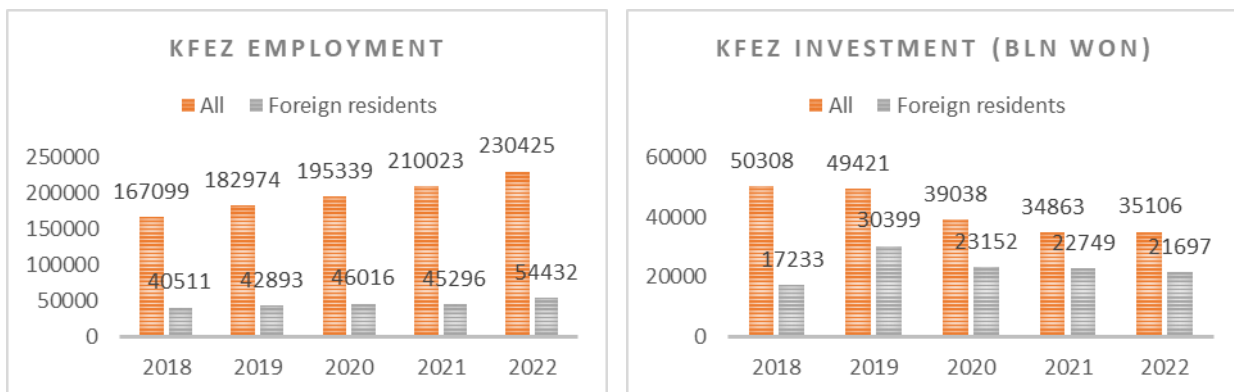
**Korean FEZ Economic statistics<sup>2</sup>**

3. Sectoral Contributions. Different FEZs have specialized in various sectors, contributing to the diversification of South Korea's industrial base:

- IFEZ: Focus on high-tech industries, including biotechnology and information technology.
- BJFEZ: Emphasis on maritime industries, shipbuilding, and international trade.
- GFEZ: Strong presence in heavy industries, particularly steel and petrochemicals.

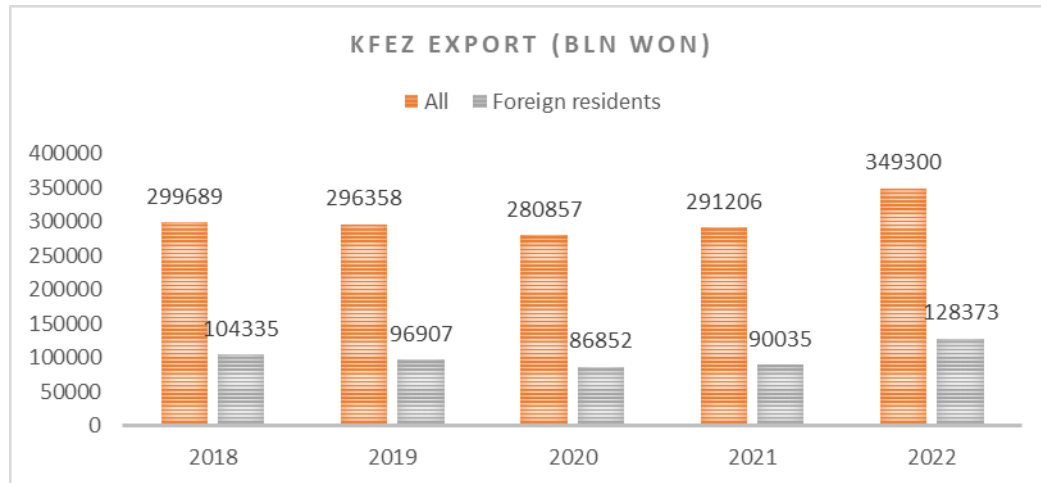
Figure 3.

**KFEZ Export statistics (2018-2022)<sup>3</sup>**



<sup>2</sup> [Korean Free Economic zones Major statistics \(fez.go.kr\)](https://www.fez.go.kr/fezstat/eng) https://www.fez.go.kr/fezstat/eng

<sup>3</sup> [Korean Free Economic zones Major statistics \(fez.go.kr\)](https://www.fez.go.kr/fezstat/eng) https://www.fez.go.kr/fezstat/eng



**SWOT analysis**

<b>Strengths</b>	<b>Opportunities</b>
<ul style="list-style-type: none"> <li>○ Strategic Location;</li> <li>○ Robust Infrastructure;</li> <li>○ Advanced Facilities;</li> <li>○ Comprehensive Support Services;</li> <li>○ Policy Incentives;</li> <li>○ Tax Benefits;</li> <li>○ Regulatory Flexibility;</li> <li>○ Educational Excellence;</li> </ul>	<ul style="list-style-type: none"> <li>○ Emerging Industries;</li> <li>○ High-Tech and Green Technologies;</li> <li>○ Regional Integration;</li> <li>○ Economic Partnerships;</li> <li>○ Innovation and R&amp;D;</li> <li>○ Collaborative Ventures;</li> <li>○ Policy Enhancements;</li> <li>○ Further Reforms;</li> </ul>
<b>Weaknesses</b>	<b>Threats</b>
<ul style="list-style-type: none"> <li>○ High Costs;</li> <li>○ Living and Operating Expenses;</li> <li>○ Limited Scale;</li> <li>○ Zone Size and Capacity;</li> </ul>	<ul style="list-style-type: none"> <li>○ Global Competition;</li> <li>○ Rival FEZs;</li> <li>○ Economic Volatility;</li> <li>○ Global Economic Fluctuations;</li> <li>○ Geopolitical Tensions;</li> <li>○ Regional Instability;</li> <li>○ Environmental and Sustainability Concerns;</li> <li>○ Sustainability Issues;</li> </ul>

The SWOT analysis highlights that South Korean FEZs possess significant strengths in terms of strategic location, robust infrastructure, and favourable policies, making them attractive destinations for FDI. However, addressing weaknesses such as bureaucratic challenges and high costs is essential. By seizing opportunities in

emerging industries and innovation, and mitigating threats from global competition and economic volatility, South Korean FEZs can enhance their role in attracting FDI and contributing to the country's economic growth.

#### Discussions

1. Effectiveness of Policy Frameworks and Incentives. The success of South Korea's FEZs can be largely attributed to well-designed policy frameworks and attractive incentives. Tax breaks, streamlined regulations, and advanced infrastructure have created a favorable business environment. However, the effectiveness varies across different zones:

- IFEZ: Its strategic location and focus on high-tech industries have made it highly successful in attracting top-tier multinational corporations.

- BJFEZ and GFEZ: These zones have leveraged their industrial strengths and geographic advantages to attract substantial FDI, although they face competition from similar zones in neighboring countries.

2. Challenges and Areas for Improvement. Despite their success, FEZs in South Korea face several challenges:

- Competition from Other Countries: Increasing competition from FEZs in China, Vietnam, and other countries poses a threat to South Korea's attractiveness as an investment destination.

- Sustainability Concerns: Managing environmental sustainability and urban development within FEZs is a growing challenge. Ensuring that industrial activities do not compromise environmental standards is critical for the long-term viability of these zones.

3. Recommendations for Enhancing FEZs. To further enhance the effectiveness of FEZs in attracting FDI, several recommendations are proposed:

- Infrastructure Investment: Continue investing in cutting-edge infrastructure to maintain a competitive edge, particularly in high-tech and green technology sectors.

- Sustainable Development: Implement robust environmental regulations and sustainable practices to ensure that economic growth within FEZs does not come at the expense of environmental health.

- Promotion of Innovation: Foster innovation through incentives for research and development (R&D) and by encouraging partnerships between foreign and domestic firms.

#### **CONCLUSION**

The study concludes that Free Economic Zones have played a crucial role in attracting Foreign Direct Investment to South Korea, contributing significantly to the nation's economic growth, job creation, export expansion, and regional development.



While the FEZs have been largely successful, addressing the existing challenges and implementing the recommended improvements can further enhance their effectiveness. This will ensure that South Korea remains a competitive and attractive destination for foreign investors in the increasingly globalized economy.

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