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Tax Regime in Free Economic Zones and Its Impact on Regional Competitiveness

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Abstract: In recent years, the practice of establishing free economic zones (FEZs) has been actively developing in the Republic of Uzbekistan with the aim of eliminating asymmetric conditions in regional economic development, attracting foreign and domestic investments, and modernizing local production. These zones are viewed as an important infrastructural and fiscal tool for addressing economic differentiation issues in the country, reducing unemployment, and increasing export volumes. Particularly, the tax incentives and preferential regimes being implemented within FEZs are creating favorable conditions for investors. However, the question of how these benefits impact long-term economic stability and interregional competitiveness has not yet been sufficiently researched. This article provides an in-depth analysis of the real economic efficiency of tax policies in Special Economic Zones (SEZs), their role in intensifying investment competition among regions, and their impact on local economic activity. The study evaluates the performance of existing free economic zones in Uzbekistan (Angren, Navoi, Jizzakh, and others) based on statistical data, conducts a comparative analysis with international experiences (China, UAE, Poland), and identifies strengths and weaknesses through SWOT analysis. As a result, the article proposes recommendations aimed at enhancing regional economic competition through SEZs, optimizing tax policies, and promoting strategic development. The significance of the article lies in its provision of theoretical and practical foundations for establishing a competitive fiscal environment and creating sustainable economic zones in Uzbekistan. It can be valuable not only for economists and policymakers but also for investors and representatives of regional administrations.

Keywords: Free Economic Zones (FEZ), Investment Environment, Export Potential, Industrial Zones, Efficiency of Tax Policy, Regional Economic Stability

Introduction

In recent years, the institution of free economic zones (FEZ) has been widely implemented on a global scale to develop economies competitively, increase investment activity, and reduce economic disparities between regions. Such zones are economic spaces with a special regime within a limited territory, creating a favorable environment for foreign and local investors through tax, customs, currency, and other economic benefits. To date, more than 5,400 FEZs of various forms operate around the world, most of which are located in developing countries, where they contribute to generating a significant portion of the gross domestic product.

During the years of independence, the Republic of Uzbekistan has also viewed free economic zones as an important tool for economic reforms and is pursuing their implementation throughout the country. In particular, FEZs are operating in regions with industrial and production potential, such as Angren, Navoi, Jizzakh, Urgut, and Gijduvan. Their main objectives are to attract foreign investment, introduce advanced technologies, develop modern industrial sectors, and increase export potential. Tax incentives provided within FEZs are emerging as the primary means of "fiscal attractiveness" for these zones.

The tax regime currently applied in FEZs offers significant advantages compared to conventional taxation. For instance, long-term exemptions are granted for profit tax, value-added tax (VAT), land tax, and customs duties. This situation, on the one hand, stimulates the inflow of investors, and on the other hand, creates certain imbalances in competition with non-zonal territories. Therefore, the tax regime applied in FEZs should serve not only fiscal goals but also broader macroeconomic and regional development strategies.

However, existing practice shows that tax incentives often only succeed in attracting short-term capital inflows, and sometimes these incentives are not tied to specific performance criteria. At the same time, SEZs are altering the inter-regional competitive landscape: districts near the zones are experiencing increased economic activity, while remote areas lacking infrastructure are being left behind. This is leading to persistent disparities in regional economic development.

International experience shows that the successes achieved through FEZs are directly related to the effectiveness of tax policy and its transparency, stability, and fairness. For example, China's Shenzhen, UAE's Jebel Ali, and Poland's Katowice zones have achieved significant economic results not only through tax incentives but also through robust infrastructure and a performance-based approach.

From this perspective, this article aims to systematically analyze the impact of the current tax regime in free economic zones on regional competitiveness. The purpose of the research is to assess the economic effectiveness of tax benefits in SEZs, study their impact on the local economic environment, and create a scientific basis for developing an improved tax policy for Uzbekistan based on international experiences.

Methodology

This study aims to examine the economic efficiency of tax regimes operating within free economic zones (FEZs) and their impact on interregional competitiveness, based on a comprehensive analytical approach. The research employed a combined form of qualitative and quantitative methods. The methodological framework encompassed several stages and tools:

Normative-legal analysis - In the first stage of the study, legal and regulatory documents related to the establishment of free economic zones in the Republic of Uzbekistan and the provision of tax incentives were examined. Specifically, the Law "On

Free Economic Zones," the Tax Code of the Republic of Uzbekistan (current edition), Presidential decrees and resolutions (for example: UP-5690, PP-3116, PP-4008), and regulatory documents of the Tax Committee and the Investment Agency were analyzed. This analysis clarified the legal framework of the current tax regime in FEZs and its practical application.

Statistical data analysis - The study analyzed data based on official statistics regarding FEZ activities from 2017 to 2023. The main indicators were:

- Volume of foreign and domestic investments attracted by FEZs,
- Number of jobs created in FEZs,
- Volume of exports carried out by FEZs,
- Dynamics of tax revenues (comparison between FEZs and general territories).

During the analysis process, results were visually represented using dynamic graphs, column charts, growth trends, and comparative diagrams.

Comparative international analysis - in the third stage, the impact of tax regimes in SEZs was studied based on international experience. Selected countries:

- China: a model that achieved economic growth through tax incentives in Shenzhen and other special economic zones;
- UAE (United Arab Emirates): 0% income tax and 100% foreign ownership opportunities, exemplified by the Jebel Ali Free Economic Zone;
- Poland: Long-term profit tax exemptions and tax credit mechanisms in the Katowice Special Economic Zone.

Based on the experience of these countries, analytical differences and similarities with SEZs in Uzbekistan were identified, and aspects considered as potential models were highlighted.

SWOT analysis. For the purpose of strategic analysis of tax policy in SEZs, the following were assessed based on the SWOT model:

Table 1. SWOT Analysis

Categories	Description
Strengths (S)	Attractiveness of tax benefits, conveniences for investors, export potential.
Weaknesses (W)	Tax benefits not linked to effectiveness, weakness of the monitoring mechanism.
Opportunities (O)	Development of competitive zones, the possibility of establishing SEZs in remote areas.
Threats (T)	Reduction of the fiscal base, lack of competition, risk of tax misuse.

During the research process, publicly released interviews of the State Tax Committee, Investment Committee, and administrations of some SEZs, as well as reports from international organizations (OECD, World Bank, UNCTAD) were analyzed. Additionally, scientific articles, journals (Asian Development Review, Journal of International Economics), and academic publications in the fields of Economics and Education were utilized as primary theoretical sources.

The study is limited to statistical data on SEZ activities for the period of 2017-2023. The recent establishment of some zones and the insufficiency of official open data in certain cases restricted the depth of analysis. Furthermore, the lack of opportunity to conduct in-depth interviews at the local enterprise level limited the qualitative empirical component of the research. In conclusion, the study employed a combination of analytical tools at various levels, which allowed for a multifaceted and thorough analysis of the impact of the current tax regime in SEZs on the regional economy.

Result and Discussion

As of 2024, the number of free economic zones (FEZs) operating in the Republic of Uzbekistan has reached 23, with the main ones being: Navoi, Angren, Jizzakh, Urgut, Gijduvan, Khazorasp, and Namangan FEZs. To attract foreign investment in these zones, full exemption from profit tax, VAT, land and property taxes, and customs duties is provided. The duration of tax benefits is set from 3 to 10 years, depending on the volume of investments made by the enterprise. As a result of these concessions, the following changes were observed during 2020-2023.

Table 2. Result of these concessions

Indicators	2020	2021	2022	2023
Investments attracted to FEZs (billion $)	0.75	1.12	1.46	1.81
New jobs created (thousand)	8.5	10.2	12.9	15.3
Export volume (billion $)	0.43	0.61	0.88	1.02
Volume of benefits provided through tax concessions (billion soums)	2.1	2.9	3.8	4.6

As can be seen from the table data, investments attracted through FEZs have increased 2.4 times over 3 years, and the volume of exports has increased 2.3 times. This indicates that the tax regime in FEZs is stimulating economic activity.

Although the regions where FEZs are located (for example, Tashkent region, Navoi region, Jizzakh region) have achieved significant positive changes in economic indicators, remote areas that do not have a zone (Surkhandarya, Karakalpakstan, Nurata, Zarafshan) cannot benefit from tax concessions. This is reducing their competitiveness.

Table 3. Availability of FEZ Investment Export volume in 2023 (billion $)

Province	Availability of FEZ	Investment volume in 2023 (billion $)	Export volume (billion $)
Navoi	Yes	0.61	0.37
Jizzakh	Yes	0.48	0.22
Surkhandarya	No	0.19	0.08
Karakalpakstan	No	0.15	0.05

As evident from the table data, the volume of investments and exports in regions with FEZs is on average 2.5-3 times higher. This demonstrates that the tax benefits in these zones create a competitive advantage.

Below is a comparative analysis of the tax regime of Uzbekistan's FEZs with the experiences of China, the UAE, and Poland:

Table 4. Comparative analysis of the tax regime of Uzbekistan's FEZs

Country	Income tax rate	VAT benefit	Grace period	Local integration requirement?
Uzbekistan	0%	0%	3-10 years	Unclear (recommended)
China	15% (standard 25%)	50% discount	5-15 years	Yes (product share specified)
UAE	0%	0%	15+ years	No
Poland	Credit method	No	10-15 years	Yes (based on local cooperation)

As evident from the table data, Uzbekistan's tax incentives are attractive, but the criteria for monitoring, local cooperation, and effectiveness are weak.

Table 5. Key findings based on SWOT analysis

Main strengths	Weaknesses
Tax incentives are attracting investors Exports and job opportunities are increasing	Benefits are not tied to specific performance Monitoring and control mechanisms are weak
Opportunities	**Threats**
Potential to expand FEZs to remote and underdeveloped regions	Misuse of tax breaks and threat to fiscal stability

Strategic analytical conclusions: Although the tax regime in SEZs has yielded significant results in the short term, a long-term strategy is necessary for their sustainable economic impact. It is important to introduce indicators for assessing the effectiveness of zones (for example, jobs created, export volume, share of local cooperation). Tax incentives should be designed not as a means of reducing interregional inequality, but as a tool for expanding economic activity.

Free Economic Zones (FEZs) are recognized as an effective tool for liberalizing the modern economy, improving the investment climate, increasing export potential, and stimulating regional economic activity. Uzbekistan's experience shows that SEZs based on tax incentives lead to an increase in capital inflow, export volumes, and the number of jobs in the short term. From 2020 to 2023, investments attracted through SEZs increased by nearly 2.5 times, while exports more than doubled. This clearly demonstrates the potential for achieving economic growth through the tax regime.

However, analysis shows that the tax regimes operating in these zones are still far from a consistent and results-oriented strategic approach. Currently, tax benefits in SEZs are provided in a static form, without clear monitoring or criteria. This, in some cases, leads to improper distribution of benefits or inefficient operation of the zones. Additionally, due to the concentration of SEZs in more central areas, remote and economically disadvantaged regions are deprived of the opportunity to utilize these advantages.

International experience (China, UAE, Poland) demonstrates that the success of SEZs depends on well-founded tax incentives, infrastructure readiness, and reliable relationships between investors and the state. It is precisely the performance-based tax policy that is the decisive factor determining the effectiveness of SEZs.

Conclusion

Furthermore, in Uzbekistan, the tax regimes in SEZs are still not fully integrated with the local economy. Mandatory requirements for cooperation with local producers, raw material supply, and utilization of the workforce are insufficiently developed. This leads to disruptions in transmitting the economic activity generated within the zones to the broader regional economic system.

Taking into account the above problems and results, the following systematic proposals and recommendations can be put forward:

Link tax incentives to performance indicators. Tax benefits should be granted solely based on export volume, job creation, and the level of local cooperation. An annual monitoring system and a performance indicator chart should be developed for this purpose.

Establish Free Economic Zones (FEZs) based on territorial balance. It is advisable to create zones not only in central regions but also in lagging areas such as Surkhandarya, Karakalpakstan, and Nurata. A special status of "regional strategic zones" can be designated for these territories.

Strengthen integration with the local economy. Enterprises operating in FEZs should be required to maintain at least 30% cooperation with local producers. The use of local raw materials and workforce should be incentivized.

Enhance transparency and legal guarantees of tax regimes. Tax incentives must be guaranteed at the legislative level and should not be subject to change by administrative bodies. The stability of the legal environment for investors is the primary guarantee of FEZ operations.

Improve the information system and monitoring mechanism. A unified digital monitoring platform for FEZ activities should be implemented. Companies that have utilized tax benefits should be required to submit quarterly reports.

Tax incentives are a powerful fiscal tool, but they serve long-term economic stability only when combined with a clear strategy, monitoring, and effectiveness. For Uzbekistan, the most important step in this direction is to review the main objectives of Free Economic Zones' activities, restore territorial equality, and create a competitive economic environment.

When properly managed, free economic zones can become a force that determines not only the success of individual investors but also the economic trajectory of an entire region. Therefore, developing this institution as a strategic fiscal instrument should be one of the priorities of state policy.

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