

A Study On The Performance Of Special Economic Zones In Terms Of Net Foreign Exchange Earnings With Reference To Karnataka State.

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Abstract

The present research article is going to analyse the performance of Karnataka Special Economic Zones (SEZs) in terms of Net Foreign Exchange earnings. Earning the net foreign exchange from international trade is one of the prime motives behind the enactment of SEZ Act with such a pro-business nature in India. As a result, SEZs have been contributing significantly to the export sector. In this contribution from the SEZs to the export sector, Karnataka state stands in front with a remarkable portion of India's total SEZs export. However, the question is how far they have succeeded in earning net foreign exchange from their international trade since the import from these zones is sizeable. At the same time, these zones are free to trade within the country in the name of export and import, and such a kind of sale will be called as Domestic Tariff Area (DTA) sale to differentiate from the actual export and import. This kind of sale from the SEZs will not bring foreign exchange to our country. In this background, the present research work is going to know how far the Karnataka SEZs have been successful in earning net foreign exchange from their business operation. The present research work is descriptive in nature and used secondary data to analyse the research problem with the simple statistical tools.

Keywords: SEZ, Export, Import, Foreign Exchange, DTA sale.

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I. Introduction

International trade allows countries to expand their markets and access goods and services that otherwise may not have been available domestically. As a result of international trade and the market is more competitive. This ultimately results in more competitive pricing and brings a cheaper product home to the consumer comparatively. Due to inadequate allocation of resources, no country in the world is able to produce the things it needs on its own. Therefore, it is necessary for every country to have international trade relations with the rest of the world for its needs. Moreover, such intensive globalization that developed in the latter half of the 20th century made this imperative even stronger. Globalization has grown to such an extent that the world is said to be a village i.e., a "Global Village". At this point, countries need to prevent any external factors from undermining their economies. At the same time, it is also essential to have adequate foreign exchange reserves for their daily international business. Fluctuations in foreign exchange reserves weaken the economy not only externally but also internally. Therefore, earning foreign exchange reserves is as important as managing them. That is why all the countries today are more interested in export promotion measures in their economic policies as well as in industrial policies. In this regard, the Special Economic Zones Act, of 2005 is a milestone in the development of international trade in India.

The Special Economic Zone Act was framed with various objectives such as employment generation, investment promotion, creation of infrastructure facilities, export promotion, and creation of additional economic activities in the country. But export promotion is the most important of these. As per Rule 18 (2) (i) in Chapter III of the SEZ Rule, 2006¹, it is mandatory to earn net foreign exchange, according to Rule 53 of the SEZ Rules, 2006, to get the privileges offered by the SEZ Act, 2005. In this context, the most important reason for the establishment of Special Economic Zones is to earn net foreign exchange through export promotions in the country.

Karnataka has been playing a crucial role in the progress the of growth and development of SEZs in India since the enactment of SEZ Act in the country. Karnataka stands second in place with Telangana state in terms of

¹ SEZ rules - 2006

operational SEZs in India. Especially, in IT sector export, Karnataka stands first with a share of 40 percent in the country. SEZs have been contributing remarkably to this achievement in the state. In this background, made an attempt to know at what extent the Karnataka Special Economic Zones have been contributing to India's net foreign exchange earnings.

II. Review of Literature

Introducing SEZs leads to a greater impact on exports spread across SEZ firms (Ronald B. Davies and Arman Mazhikeyev, 2019). The SEZs are believed to create an adequate environment for foreign direct investment, export promotion, infrastructure creation, transfer of technology, and additional employment generation in the country. India's total export is showing an increasing trend with the fluctuating situation (Aravindaraj. K, A.Muthusamy, 2019). SEZs have been significantly contributing to India's total export value every year progressively. The share of SEZs to GDP is remarkable with 5.07 percent of contribution in the study period (Ayisha and Thowseaf, 2016). In respect of contribution to national trade, SEZ's are lagging way behind the expectations. The SEZ policy does not seem to be successful in diversifying the exports basket, which in turn has affected the direction of exports by the SEZ's (Malini L. Tantri, 2012).

These studies show that the SEZs have been positively impacting on international trade by exporting a significant amount of goods and services in India. Meanwhile, it is more important to know that, from this export, how far it is contributing to the addition of net foreign exchange reserves. In this background the present research work is going to know that the performance of Karnataka SEZs in terms of net foreign exchange earnings.

III. Objectives

The main objective of this paper is to know the performance of Karnataka SEZs in terms of earning net foreign exchange reserves. Apart from that, there are two other objectives

1. To know the impact of Karnataka SEZs imports on India's Forex reserve, and
2. To know the status of the DTA sale of Karnataka SEZs.

IV. Hypothesis

Hypothesis 1:

H₀: The import intensity of Karnataka SEZs is the same among different types of SEZs.

H₁: The import intensity of Karnataka SEZs is not the same among different types of SEZs.

Hypothesis 2:

H₀: There is no statistically significant difference in terms of DTA sales among different types of SEZs in Karnataka.

H₁: There is a statistically significant difference in terms of DTA sales among different types of SEZs in Karnataka.

Hypothesis 3:

H₀: There is no statistically significant difference in terms of net foreign exchange earnings among different types of SEZs in Karnataka.

H₁: There is a statistically significant difference in terms of net foreign exchange earnings among different types of SEZs in Karnataka.

V. Methodology

The present paper "A Study on the Performance of Special Economic Zones in Terms of Net Foreign Exchange Earnings with Reference to Karnataka State" is descriptive in nature. To analyse the research objectives, secondary data has been collected from the official sources related to 30 operational SEZs of Karnataka state till 31-10-2020. Simple statistical tools were used to process and analyse the collected data. Single-factor ANOVA has been used to test the proposed hypothesis.

VI. SEZ's in Karnataka

The establishment of SEZs in Karnataka has been started in 2006 and onwards when the government of India enacted the SEZ Act in 2005. Prior to that, though the SEZs were established in various states under different policies, Karnataka had not made any attempt to establish SEZs in the state. After 2006, the State Government has taken the initiative to promote the SEZs which the government has considered the engine of growth of the state economy. Attractive incentives and concessions given in SEZ Act magnetized investors around the world. Karnataka has not lagged behind to utilize this opportunity for the development of the state's economy. To implement the policy more effectively, Karnataka passed an amendment regarding the establishment of SEZs in

2009 to strengthen the policy in the state. Since the SEZ act was enacted, there are 63 formal approval SEZs in Karnataka. In that 52 SEZs are notified and 32 SEZs started their production in the state.

VII. Discussion

Special economic zones have been facilitated by the government through various incentives and fiscal measures. Exemption from income tax for a period of five years for developers and manufacturers of SEZs and thereafter, 50% income tax exemption is given for the next five years. Besides, the government is spending hundreds of crores from its coffers to build infrastructure for them. While the government has provided these facilities, it is necessary to contribute significantly to the development of the economy through foreign trade.

India naturally has some disadvantages in terms of many resources. Because of that, some goods and services are not able to produce on our own. Some of those commodities are very essential for the smooth running of economic activities. For example, petroleum products. Yet some goods are related to people's emotions such as gold and luxurious goods. Further, capital goods appear to have emerged due to research and development in developed countries. Those goods and services are not allowed to produce as they are copyrighted by the owned countries. But, as mentioned earlier, such kind of advanced capital goods, necessary goods and services are inevitable for any economy. Due to all these reasons, unable to control imports effectively in the current scenario. In this circumstance, the nation should earn enough foreign exchange to import enough amount of goods and services required. In this regard, Special Economic Zones should help India to earn enough foreign exchange by promoting exports. When that happens, the government's efforts to build them will be fruitful and the facilities given to them will indirectly help in strengthening the economy. As observed the Karnataka's contribution to the national export it is very clear that the Karnataka SEZs have been contributing a significant portion. However, the question is how far that helps in earning net foreign exchange. Merely exporting by SEZs does not mean that they have been earning enough foreign exchange rather it has depended on their import intensity. In this regard, it is important to know that how effectively Karnataka SEZs are earning net foreign exchange.

Loss of Forex Reserves due to DTA Sale

Government of India to enable the smooth functioning of SEZs, under Section 53(1) of SEZ Act 2005, SEZs are considered as deemed to be foreign territory for the purposes of authorized operations. It implies that any kind of goods and services sent out from an SEZ is considered as export. It could be to another SEZ or to sell elsewhere domestically. Therefore, for any SEZ to call its production an export, it does not need to be sold to foreign countries. Instead, it was sold domestically, we call it an export. As such, it is difficult to know how much foreign exchange is earned by a particular SEZ. However, to solve this problem, goods and services sold in the domestic area will be considered as DTA sales. From this type of sale, SEZs are not able to earn any foreign exchange currency. Otherwise, even from such sales, we would have a chance to earn foreign exchange. Because of this reason, India has been losing the opportunity to earn foreign exchange. Thus, as SEZs sell more of their products domestically, the foreign exchange available from SEZs foreign trade will get decreases.

**Table 1 - Sector wise DTA sale of Karnataka SEZs from their total production
(In Percentage)**

Year	Type of SEZ						
	IT	BT	Engineering	Textile	Pharmaceutical	Multi-Product	Aerospace
2006-07	0.00	0.00	*	0	*	*	*
2007-08	3.65	11.24	0	1.12	0	*	*
2008-09	1.55	18.48	0.13	1.34	0	*	*
2009-10	2.54	19.10	13.50	1.75	0	0	0
2010-11	2.37	30.11	20.33	6.53	0	0	0
2011-12	1.64	25.37	52.00	3.21	0	0	0
2012-13	2.34	24.53	17.98	6.19	0.00	0	0
2013-14	1.21	22.80	15.08	2.11	0.17	1.38	0
2014-15	2.55	21.39	17.49	4.28	0.73	13.64	0
2015-16	2.89	15.93	47.43	4.78	4.78	15.46	2.83
2016-17	1.97	13.68	42.46	5.21	0.78	27.43	13.66
2017-18	3.61	48.08	22.14	8.87	12.60	17.95	1.77
2018-19	1.20	35.71	18.37	7.51	4.80	23.17	14.47
2019-20	0.37	10.72	7.22	2.87	NA	34.88	9.77
Average	1.99	21.22	21.09	3.98	1.99	12.17	3.86

Source: Compiled data from www.csez.com

* Production not yet started in the particular year, NA- Data not available

The DTA sales is not the same among different sectors in Karnataka SEZs rather it varies from sector to sector. Some sectors sold more than 40 percent of their production in DTA in a particular financial year. At the same time, some of the SEZ sold below one percent of their product in DTA. Hence, it remains to be seen how much net foreign exchange is being earned in the Special Economic Zones in Karnataka. Sector wise DTA sale of Karnataka SEZs has been explained in table 1. As mentioned in table 1, the DTA sale of Karnataka SEZs has not been showing uniformity among various sectors over a period of time. Sector to sector it is showing remarkable difference in DTA sale. As it is observed by sector wise, the IT sector has sold 1.99 percent of its total production in DTA till 2019-2020 and it accounts total rupees 11968.2 crore. In the beginning year, 2007-08, it has sold 3.65 percent of its production in DTA. Within the IT sector DTA sale has been fluctuating close to three percent from year to year. As compared to any other SEZs, BT sector has the highest DTA sale after engineering sector from its total production with 21.22 percent till 2019-2020 and it accounts rupees 5221.25 crores. As mentioned in the table 1, in 2017-18, it has sold 48.08 percent of its production in DTA itself. So far, most of the year, the BT sector SEZ selling its product in DTA has been crossing on an average 20 percent every year. In Karnataka 2 SEZs are there in Engineering sector. It is the second largest sector in selling its product in DTA after BT SEZ. From 2007-08 engineering sector SEZs started their production. Till 2019-20, on an average 21.09 percent of its production have been selling every year. Rupees 2006.42 Crore worth of product has been sold so far in DTA from the engineering sector. In 2011-12, 2015-16 and 2016-17 sold the highest amount of their production in DTA with 52, 47.43 and 42.46 percent respectively.

Looking at the textile SEZ, 3.98 percent of the production is being sold domestically and it accounts rupees 193.37 crore in the total production. Pharmaceutical SEZ has sold 1.99 percent of its production in DTA Since 2007-08. In 2015-16, 2017-18 and 2018-19 pharmaceutical sector has sold the highest amount of its production in DTA with 4.78, 12.60 and 4.80 respectively. Except these years not sold much in DTA. Multi-product sector is the third largest sector in Karnataka in terms of DTA sale. It has sold on a 12.17 percent of its production in DTA every year. In the beginning years, 2009-10 to 2012-13, it has not sold any of its production in the DTA. Only after 2013-14, it has started to sale its products in the DTA. In 2019-2020, it sold the highest production in DTA with 34.88 percent. The multi-product sector SEZ, till 2019-2020 sold 13727.95 crore rupee worth of goods in the DTA. The Aerospace sector SEZ sold 3.86 percent of its production in the DTA.

Loss of Forex Reserves due to Imports

As discussed in the beginning part of this article, export promotion is the prime agenda of the establishment of SEZs in India. As we sacrifice lot of resources to make easier and smooth functioning of the SEZs in the country, importing more than what they export, may cause to lose our forex reserves. However, it is impossible to restrict import completely. Because of that reason importing larger amount of goods and services will badly affect the economy.

**Table:2 Sector wise Imports of Karnataka SEZs
Numbers in Crores)**

Year	IT	BT	Engin eering	Textile	Pharmac eutical	Multi-Product	Aero space	Total
2006-07	38.5	19.56	*	0	*	*	*	58.06
2007-08	1640.89	204.6	3307.17	6.15	41.49	*	*	5200.3
2008-09	1678.1	207.31	11779.89	26.41	52.62	*	*	13744.33
2009-10	3206.25	264.1	458.66	191.86	37.04	0.41	160.61	4318.93
2010-11	2201.7	339.05	468.05	160.71	38.5	63.41	74.09	3345.51
2011-12	2942.69	389.35	378.31	166.19	64.41	19.45	77.51	4037.91
2012-13	3791.58	414.69	429.06	238.6	71.97	29.9	156.16	5131.96
2013-14	3293.89	436.37	489.11	249.42	1.41	29.93	7.64	4507.77
2014-15	5279.72	719.72	311.03	281.8	7.29	1784.63	14.47	8398.66
2015-16	4732.37	644.46	553.99	34.92	5.74	131.61	68.23	6171.32
2016-17	5652.25	920.95	582.5	44.32	12.19	3160.15	115.72	10488.08
2017-18	2516.07	645.03	554.12	49.04	30.23	3978.59	95.88	7868.96
2018-19	8966.73	1625	491.75	42.66	23.61	4710.95	203	16063.7
2019-20	3526.37	1398.31	416.05	6.46	0.00	244.03	297.69	5888.91
Total	49467.11	8228.50	20219.69	1498.54	386.50	14153.06	1271.00	95224.40
%	51.95	8.64	21.23	1.57	0.41	14.86	1.33	100.00
CAGR	38.08	35.66	-14.74	0.38	-4.24	78.75	5.77	39.09

Source: Compiled data from www.csez.com

* Production not yet started in the particular year

In Karnataka, not all the SEZs import the same amount of goods and services. Their import density varies from sector to sector. Sector-wise import of Karnataka SEZs has shown in table 2. From 2006-07 to 2019-2020, Karnataka SEZs have imported rupees 95224.4 crore worthy products. The imports of Karnataka SEZs have been increasing at 39.09 CAGR. In that, IT sector alone contributes 51.95 percent of imports with rupees 49467.11 crore. IT sector imports have been increasing at 38.08 CAGR. BT sector accounts 8.64 percent of in the imports of Karnataka SEZs since 2006-07. Till 2019-20, it has imported rupees 8228.50 crore worthy products. The engineering sector contributes 21.23 percent to the total import of Karnataka SEZs. it is the second largest sector in terms of imports of SEZs after IT sector in Karnataka. till 2019-20, it has imported rupees 20219.69 crore worthy products. Multi-product sector is the third largest sector in importing the goods and services for their operational requirements. It accounts 14.86 percent in the total imports of Karnataka SEZs. Till 2019-20, it has imported total rupees 14153.06 crore. Apart from these sectors, Textile, Pharmaceutical and Aerospace SEZs have very less percentage of share as compared to any other sector with 1.57, 0.41 and 1.33 percent respectively. Year wise growth of imports of Karnataka SEZs has shown in the figure 2.

At the end of 2019-20, India lost rupees 95224.40 crore foreign exchange due to imports of Karnataka SEZs. This is not to argue that we should not do imports because of this. But Indian government have made several compromises and sacrifices for the smooth functioning of the Special Economic Zones. The main reason for all this is to make India a strong country in foreign trade by strengthening the export sector. But if these types of industries are increasing imports instead of increasing exports, the prime purpose of this policy will be undermined. Imports are inevitable because we cannot produce some goods as we mentioned earlier. But if they continue to increase so much then the sacrifices, we are making for them will be meaningless. We treat SEZs differently from all other industries. It may be in the procedure itself, it may be in the facilities provided by the government, basic infrastructure facilities providing by the government, labour laws and etc. that is why expecting the increase of exports than imports from SEZs. As observed the table 3, Karnataka SEZs imports are equal to 14 percent of their total exports till 2019-20.

Total Loss of Forex Reserves

As mentioned in the above discussion, India has been losing its forex reserve in both the way that is directly and indirectly. While importing the goods and services losing forex reserves directly and in the case of DTA sale missing the opportunity to earn the forex reserves indirectly. Table 4 shown the forex reserve forgone from these two reasons.

**Table:5 Sector wise Net-Foreign Exchange Earning of Karnataka SEZs
(Numbers in Crores)**

Year	IT	BT	Engineering	Textile	Pharma ceutical	Aerospace	Total
2006-07	134.86	17.1					151.96
2007-08	-472.16	112.7	-3307.17	68.14	-41.49		-3639.98
2008-09	6206.55	213.79	-9962.65	236.29	-52.62		-3358.64
2009-10	7893.55	405.38	353.85	157.11	-37.04	-160.61	8612.24
2010-11	15152.3	273.3	86.29	175.39	-38.5	-74.09	15574.71
2011-12	21439.8	366.74	-399.58	342.61	-64.41	-77.51	21607.65
2012-13	32532.4	622.87	156.93	330.8	-69.72	-156.16	33417.13
2013-14	72892.3	868.25	184.17	629.54	10.62	25992.65	100577.57
2014-15	45250.4	832.51	80.48	542.81	11.68	-10.99	46706.92
2015-16	59597.1	1276.86	-520.86	66	10.52	-51.2	60378.45
2016-17	66751.8	799.71	-467.62	73.53	34.59	-82.93	67109.08
2017-18	56658.8	1193.09	-158.71	76.91	28.79	17.04	57815.95
2018-19	97426.4	-549.73	-7.95	90.35	58.16	-75.37	96941.81
2019-20	99377.3	1319.5	120.83	134.32	0	-20.15	100931.79
Total	580842 (96.35%)	7752.07 (1.29%)	-13841.99 (-2.30%)	2923.8 (0.49%)	-149.42 (-0.02%)	25300.68 (4.20%)	602826.6 (100%)
Average	41488.68	553.72	-1064.77	224.91	-11.49	2300.06	43059.05

Source: Compiled data from www.csez.com

As observed in the table, since 2006-07, Karnataka SEZs exports have been increasing at 58.18 CAGR. At the same time imports and DTA sale have been increasing at 39.09 and 38.05 CAGR respectively. Till 2019-2020, Karnataka SEZs have lost total 18.38 percent of forex reserves out of their export's earnings. In that 14.20 percent of forex reserves forgone due to import payment whereas 4.17 percent of forex reserves lose indirectly that is due to DTA sale. From 2006-07 to 2019-2020, Karnataka SEZs have earned total net foreign exchange of rupees 547052.4 crore.

In terms of foreign exchange earnings, Karnataka SEZs have not been performing equally among different sectors. It is varying from sector to sector significantly. In table 5 showing the sector wise performance of Karnataka SEZs in terms of net foreign exchange earnings. Out of total net foreign exchange earnings of Karnataka SEZs, 96.35 percent has earned from IT sector itself. IT sector has contributed the major part in the earning of forex reserves from the Karnataka SEZs. The second largest share has given from aerospace SEZ. It has earned rupees 25300 crore from their export income which accounts 4.20 percent in the total net foreign exchange earnings from the Karnataka SEZs. Apart from that, BT sector SEZ has earned net foreign exchange of rupees 7752.07 crore, which stands in the third place with 1.29 percent in the total earnings. Textile sector has contributed 0.49 percent to the total net foreign exchange earning with rupees 2923.8 crore. Remaining two sectors, Engineering and Pharmaceutical sectors have shown the negative net foreign exchange earnings from their business activities. Engineering sector has caused to lose rupees 13841.99 crore whereas Pharmaceutical sector SEZ has lost rupees 149.42 crore.

VIII. Testing of Hypothesis

Hypothesis 1:

- H₀: The import intensity of Karnataka SEZs is the same among different types of SEZs.
- H₁: The import intensity of Karnataka SEZs is not the same among different types of SEZs.

Table 6: ANOVA Tested Values of Hypothesis 1

Source of Variation	SS	df	MS	F	P-value	F crit
Between Groups	130891059.67	6	21815177	8.860692	0.00	2.20
Within Groups	224043572.80	91	2462017			
Total	354934632.47	97				

**Source: Calculated values based on Table-2
Significance level: At 0.05**

The calculated p-value is 0.00. Since the p-value of 0.00 is less than the significance value of 0.05, the study has enough evidence to reject the null hypothesis. For all tests, the alternative hypothesis specifies that the import intensity of Karnataka SEZs is not the same among different types of SEZs in Karnataka. Hence, it is concluded that the import intensity is different from product to product in Karnataka SEZs.

Hypothesis 2:

- H₀: There is no statistically significant difference in terms of DTA sale among different types of SEZs in Karnataka.
- H₁: There is a statistically significant difference in terms of DTA sale among different types of SEZs in Karnataka.

Table 6: ANOVA Tested Values of Hypothesis 2

Source of Variation	SS	df	MS	F	P-value	F crit
Between Groups	5593.244	6	932.2073665	9.889543	0.00	2.211303
Within Groups	7729.478	82	94.26192295			
Total	13322.72	88				

**Source: Calculated values based on Table-1
Significance level: At 0.05**

The calculated p value is 0.00. Since the p value 0.00 is less than the significance value of 0.05, the study has enough evidence to reject the null hypothesis. For all tests, the alternative hypothesis specifies that there is no significant difference in terms of DTA sale among different types of SEZs in Karnataka. Hence, it is concluded that, the SEZs located in the Karnataka State have been selling their product in the DTA more or less equally with their respective percentage of total production.

Hypothesis 3:

- H₀: There is no statistically significant difference in terms of net foreign exchange earnings among different types of SEZs in Karnataka.
- H₁: There is a statistically significant difference in terms of net foreign exchange earning among different types of SEZs in Karnataka.

Table 6: ANOVA Tested Values of Hypothesis 3

Source of Variation	SS	d.f	MS	F	P-value	F crit
Between Groups	19517255891	5	3903451178	17.12164098	0.00	2.341828
Within Groups	16414810077	72	227983473.3			
Total	35932065968	77				

Source: Calculated values based on Table-3

Significance level: At 0.05

The calculated p value is 0.00. Since the p value 0.00 is less than the significance value of 0.05, the study has enough evidence to reject the null hypothesis. For all tests, the alternative hypothesis specifies that There is no significant difference in terms of net foreign exchange earning among different types of SEZs in Karnataka. Hence, it is concluded that, the net foreign exchange earning is not varying from SEZ to SEZ based on the type of product it is producing in Karnataka.

IX. Conclusion

As observed in the discussion, Karnataka SEZs have not been causing much to damage the India's forex reserves whereas they only importing 14.20 percent from all the SEZ located in the state. As compared to any other industries, it is a significant contribution to the stock of India's net forex reserves by the Karnataka SEZs with rupees 547052.4 Crore from 2006 to 2020. Though the Karnataka SEZs have lost the chance of earning foreign exchange due to DTA sale, this accounts only 4.17 percent in the total production of all SEZs. Moreover, it is directly helping our economy to faster the production function in many ways. But the problem here is the sector-wise performance of earning net foreign exchange. Engineering and Pharmaceutical sectors have been showing negative net foreign exchange earnings from their operational activities. Both the sector SEZs have been losing on an average rupees 1064.77 and 11.49 crore respectively in each year from 2007-08 to 2019-2020. However, the IT sector plays a crucial role in earning net foreign exchange and contributing significantly to the India's forex reserves.

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