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Can non-fiscal incentives like reverse job work revive the SEZs? The case study of gems and jewellery sector in India

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CAN NON-FISCAL INCENTIVES LIKE REVERSE JOB WORK REVIVE THE SEZ?

THE CASE STUDY OF GEMS
AND JEWELLERY SECTOR
IN INDIA

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ESHANA MUKHERJEE

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List of Abbreviations

ASCM	Agreement on Subsidies and Countervailing Measures
ASI	Annual Survey of Industries
CAGR	Compound Annual Growth Rate
CBIC	Central Board of Indirect Taxes and Customs
CGST	Central Goods and Services Tax
CY	Calendar Year
DESH	Development of Enterprise and Services Hub
DTA	Domestic Tariff Area
EPZ	Export Processing Zone
EU	European Union
FDI	Foreign Direct Investment
FTZ	Foreign Trade Zone
FY	Financial Year
GJEPC	Gems and Jewellery Export Promotion Council
GST	Goods and Services Tax
GVC	Global Value Chain
HUID	Hallmark Unique Identification
ITC	International Trade Centre
KII	Key Informant Interview
LDC	Least Developed Country
MOOWR	Manufacturing and Other Operation in Warehouse Regulation
MSME	Micro, Small and Medium Enterprises
NCAER	National Council of Applied Economic Research
NFE	Net Foreign Exchange
NSDC	National Skill Development Council
PEZA	Philippines Economic Zone Authority
PLI	Production Linked Incentives
R&D	Research and Development
RoDTEP	Remission of Duties and Taxes on Exported Products
ROO	Rules of Origin
SEEPZ	Santacruz Electronics Export Processing Zone
SEZ	Special Economic Zone
UAE	United Arab Emirates
UK	United Kingdom
UN Comtrade	United Nations International Trade Statistics
UNCTAD	United Nations Conference on Trade and Development
USA	United States of America
WTO	World Trade Organization

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Abstract

Globally, special economic zones (SEZs) are created to boost exports and promote investment by providing units located inside the zones with certain fiscal and non-fiscal incentives that are not available to and/or are different from those given to units in the domestic tariff area (DTA). In India, the SEZ Act (2005) and the SEZ Rules (2006) aimed to create a regulatory framework to meet certain objectives, which include attracting private investment, creating employment, and promoting exports. Among the fiscal incentives given to units in Indian SEZs, the income tax benefits are conditional upon the units being net foreign exchange earners (NFE) in five years, which is an export-linked prohibited subsidy under the World Trade Organization's (WTO) Agreement on Subsidies and Countervailing Measures (ASCM). In March 2018, the United States of America (USA) challenged this export-linked subsidy in the WTO and India lost the case in October 2019, requiring the country to withdraw such subsidies.

Globally, many countries have designed WTO compliant fiscal incentives and are offering non-fiscal incentives like reverse job work in their SEZs. This has prompted India to design WTO compatible zones and the country is in the process of initiating the Development (Enterprise and Services) Hubs (DESH) Bill, 2022. This Bill has removed the NFE requirement for giving incentives and proposed certain non-fiscal incentives such as reverse job work.

This paper explores the costs and benefits of allowing non-fiscal incentives like the reverse job work in Indian SEZs in the gems and jewellery sector, and its likely impact on units both in SEZs and in the DTA. The paper found that India is among the world's top gems and jewellery exporters and this is a key export item from Indian SEZs. Based on secondary data analysis, stakeholder consultations, and a pilot survey, it presents the issues faced by gems and jewellery units in SEZs and makes policy recommendations on how to enhance exports of gems and jewellery from Indian SEZs. As the DESH Bill (2022) evolves, this paper aims to enhance the debate and discussion on incentives in SEZs, based on the requirements of the units and global best practices.

Keywords: World Trade Organisation (WTO), special economic zones (SEZs), international trade, gems and jewellery, subsidies, reverse job work

JEL classification: L5, F13, L61

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Can Non-Fiscal Incentives Like Reverse Job Work Revive the SEZs?

The Case Study of Gems and Jewellery Sector in India

Arpita Mukherjee, Nida Rahman and Eshana Mukherjee

1. Introduction

Special economic zones (SEZs) are created to boost exports and promote investment by providing units located inside the zones certain fiscal and non-fiscal incentives that are not available and/or are different from those given to units in the domestic tariff area¹ (DTA). When able to increase linkages with the DTA, the SEZs can increase exports, generate employment and increase investment (United Nations Conference on Trade and Development (UNCTAD), 2019). In the current world of a highly intertwined network of global value chains (GVCs), SEZs are increasingly seen as an important vehicle in facilitating GVCs participation by bringing down transaction costs (World Bank, 2020). In some countries like China, the SEZs serve as testing grounds for new policies and innovations prior to their adoption as national policies. For example, in China, the negative list of the foreign direct investment (FDI) plan was first tested in the free trade zone in Shanghai in 2013 (Yao and Whalley, 2015).

Free zones are a part of the territory of a contracting party where any goods introduced are generally regarded, in so far as import duties and taxes are concerned, as being outside the customs territory (The Revised Kyoto Convention, World Customs Organization, 2008).

While SEZs started in both developed and developing countries, they have spread rapidly in developing and least developed countries (LDCs) after developed countries moved away from the format of fiscal subsidy-based zones after the formation of the World Trade Organization (WTO). From 500 SEZs in 1995,

they have increased more than ten-fold to reach 5400 SEZs in 2018, spreading across 147 economies (UNCTAD, 2019). Developing economies account for around 83 per cent of total SEZs in the world.

India was a pioneer in Asia – it set up the first Export Processing Zone (EPZ) in Kandla, Gujarat, in 1965. As of June 30, 2022, the number of formally approved² SEZs in India was 425, of which 268 SEZs were operational.³ Among the operational SEZs, 57 per cent are concentrated in the IT/ITeS, electronic hardware and telecommunication sectors (as of January 28, 2022).⁴ As of November, 2021, there were around 5604 units in Indian SEZs, contributing around 35 per cent to India's total exports and generating employment for 25,60,286 persons.⁵

1.1 Gems and Jewellery Units in Indian SEZs

The gems and jewellery sector is among the key sectors in Indian SEZs. Prior to 2019, there were around 500 gems and jewellery units in the Indian SEZs. During 2021-22, there were close to 360 gems and jewellery units in the Indian SEZs. These gems and jewellery units are located in both single-product and multi-product SEZs. As of 30 September, 2022, there are four single-product gems and jewellery SEZs, while another 25 multi-product operational SEZs have gems and jewellery units. Among these 25 multi-product SEZs, the Santacruz Electronics Export Processing Zone (SEEPZ), Mumbai, Maharashtra, has several gems and jewellery units. The single-product gems and jewellery SEZs include Manikanchan in Kolkata, West Bengal, Hyderabad Gems SEZ limited in Hyderabad, Telangana, Sitapur I Special Economic Zone, and Sitapur II Special Economic Zone, Jaipur, Rajasthan.⁶

1 Domestic Tariff Area (DTA) refers to the whole of India (including territorial waters and the continental shelf) but does not include the areas of the special economic zones.

2 Formal approval is given when the land is in the possession of the developer. <https://link.springer.com/book/10.1007/978-81-322-2806-6> (last accessed November 21, 2022)

3 Source: www.sezindia.nic.in (last accessed July 22, 2022)

4 Source: <http://sezindia.nic.in/cms/operational-sezs-in-india.php> (last accessed July 22, 2022)

5 Source: India's Special Economic Zones: A Primer <https://www.india-briefing.com/news/guide-indias-special-economic-zones-9162.html/#:~:text=As%20per%20data%20from%20the%20Ministry%20of%20Commerce,shown%20below.%20Location%20of%20the%20above%20seven%20SEZs%3A> (last accessed September 07, 2022)

6 A company can have more than one unit located in the SEZs.

1.1.1 India's Gems and Jewellery Exporters in SEZs are Facing an Uncertain Situation

During 2020-21, gems and jewellery units in the Indian SEZs contributed around 20 per cent of total gems and jewellery exports from India, a sharp decline from the near 30 per cent share in total gems and jewellery exports it accounted for during 2019-20. The units in Indian SEZs face an uncertain operational environment as export-linked subsidies offered under Indian SEZ regulations have come under the scanner for non-compliance with the WTO's Agreement on Subsidies and Countervailing Measures (ASCM). Fiscal incentives offered in the Indian SEZs are contingent on the requirement of net foreign exchange (NFE) earnings for five years. According to Article 3.1 (a) of the WTO ASCM, "*subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance shall be prohibited*".⁷ As a member of the WTO, India has to abide by the ASCM. The United States of America (USA) challenged a number of Indian export promotion incentives including the SEZ policy in the WTO and won the case in 2019. Subsequently, India has been in the process of revising its SEZ policy to make it WTO compliant. During the 2022-23 Union Budget speech, Finance Minister Smt. Nirmala Sitharaman announced the replacement of the SEZ Act, 2005, with a new legislation, the Development of Enterprise and Service Hubs (DESH) Bill, 2022, that the government plans to table in the winter session of Parliament (November to December 2022).⁸ Some of the core features of the Bill includes the removal of export-linked subsidies and the offer of non-fiscal incentives similar to that given by other countries, including allowing SEZ units to sell in the domestic market with duties to be paid only on imported raw materials and inputs instead of final products.

1.2 Objective

The objective of this paper is to study how the gems and jewellery units operating in the Indian SEZs can be revived through non-fiscal incentives such as reverse job work (sales to retailers in the DTA and allowing workers in SEZs to provide maintenance and repair services for the DTA). The paper examines the impact of reverse job work on units located in SEZs, its impact, if any, on DTA units and whether

it will enhance sourcing from within Indian SEZs vis-à-vis imports. It presents the issues faced by gems and jewellery units in SEZs and makes policy recommendations to the government on how to enhance exports of gems and jewellery from Indian SEZs without any negative consequences on the DTA exporters. The broader objective of this paper is to make recommendations on how to make Indian SEZs a global manufacturing hub for gems and jewellery.

1.3 Revamping the SEZ Policy and DESH Bill (2022)

As mentioned earlier, the government is in the process of introducing the DESH Bill, 2022, to revamp the SEZ Act to ensure that it is WTO compliant. This bill proposes to do away with the NFE criteria around which fiscal incentives were provided in the SEZ Act. The DESH Bill (2022) is yet to develop fiscal incentives in line with the WTO ASCM. It proposes several non-fiscal incentives such as reverse job work and ease of entry and exit norms for investors, going beyond what is offered under the SEZ Act 2005 and SEZ Rules 2006.

1.3.1 Definition of Job Work and Reverse Job Work Under the SEZ Regulation and DESH Bill 2022

One key non-fiscal incentive in SEZs is allowing job work to workers in the DTA. While the SEZ Act, 2005, does not specifically define job work, it refers to links between SEZs and DTAs. Section 7 of the SEZ Act, 2005, states that, '*Any goods or services exported out of, or imported into, or procured from the Domestic Tariff Area by, (i) a Unit in a Special Economic Zone; or (ii) Developer, shall, subject to such terms, conditions and limitations, as may be prescribed, be exempt from the payment of taxes, duties or cess under all enactments specified in the First Schedule.*' Section 2 (68) of the Central Goods and Service Act (CGST), 2017, defined job work as '*any treatment or process undertaken by a person on goods belonging to another registered person*'. The one who does the said job would be termed as '*job worker*'. The ownership of the goods does not transfer to the job worker and continues to rest with the principal.

⁷ https://www.wto.org/english/docs_e/legal_e/24-scm.pdf (last accessed September 09, 2022)

⁸ Source: https://www.business-standard.com/article/economy-policy/finmin-s-proposed-tax-incentives-under-revamped-sez-law-hit-logjam-122080700649_1.html (last accessed August 11, 2022)

There is no official definition of reverse job work. Broadly, reverse job work allows the SEZ units to do job work for DTA retailers and manufacturers when export demand is low. This helps units mitigate risk related to seasonality in export demand and these units can replace the demand for imported goods in the DTA. Given that the primary role of the units in SEZ is to export, countries like Turkey allow reverse job work subject to certain terms and conditions, like payment of appropriate taxes and duties. When SEZ units undertake job work for the DTA, it can include after sales repair and maintenance services. According to the United Nation's Statistical Division Central Product Classification (UNSD-CPC) Version 2.1 Code 886,⁹ basic metal manufacturing services includes the outsourced portion of a manufacturing process or a completely outsourced manufacturing process. Since it covers manufacturing services only, the output is not owned by the unit providing this service. The value of the service is based on the service fee paid, not the value of the goods manufactured. Such services can be given fiscal subsidy in the current WTO framework as there is no discipline on subsidies in services.

While job work is permitted, there is no policy on reverse job work in the existing SEZ regulation in India. However, the DESH Bill, 2022, is expected to allow reverse job work, i.e., permitting SEZ units in a development hub to render manufacturing services to or receive manufacturing services from a unit in the DTA, subject to conditions as may be prescribed by the central government. However, there is a need to clearly define the manufacturing services and align such definition with international definitions like the UNSD-CPC version 2.1 so that fiscal subsidies, if any

given, can be aligned with WTO requirements.

1.4 Methodology

This study is based on secondary research and data analysis, and a pilot survey that included key informant interviews (KIIs) and four stakeholder consultations. The secondary data is on the current market structure, international trade and overall manpower availability. The pilot survey tries to understand the issues faced by the SEZ units, the type of incentives required by them, the impact of such incentives with particular reference to reverse job work and expectations from the new SEZ policy, i.e., the DESH Bill (2022).

1.4.1 Secondary Data Analysis

To analyse trade data, three data sources have been used, namely United Nations International Trade Statistics (UNComtrade), International Trade Centre (ITC) Export Potential Map and Department of Commerce, Ministry of Commerce and Industry (MOCI). UNComtrade provides trade data based on the calendar year (CY), and month-wise data, for three levels of HS Codes (2/4/6-digit HS code). For our study, we have used UNComtrade as the data source, which provides data at the HS code 6-digit level. To understand seasonality in the trade of gems and jewellery, a quarter-wise analysis has been done; the quarters are based on the financial year (FY); i.e., Q1 (April to June), Q2 (July to September), Q3 (October to December) and Q4 (January to March).

The HS codes used for the analysis of the selected sub-sectors in the study are given in Table 1.1.

Table 1.1: Select Products and their HS Codes

HS Code	Product
711319	Gold Jewellery
711311	Silver Jewellery
710239	Cut & Polished diamonds
7103	Coloured Gemstones
710490; 710420	Lab-grown diamonds

Source: UNComtrade

⁹ For details, refer <https://unstats.un.org/unsd/classifications/Econ/Structure/Detail/en/1074/88> (last accessed October 17, 2022)

1.4.2 Pilot Survey Methodology

The pilot survey framework is given in Table 1.2, which includes three broad categories of respondents – SEZ units, DTA retailers and DTA manufacturers. Apart from them, policy makers and sector experts have been interviewed. Each stakeholder consultation had around 8-10 participants from the industry.

While the SEZ units were selected through stratified random sampling (stratified by product categories and location), DTA retailer units were selected on the basis of the purposive sampling technique. For the survey, semi-structured questionnaires were

prepared. The questionnaire has incorporated some open-ended questions to elicit the views of the survey participants. The objective of the survey was to analyse the type of units in SEZs, benefits received by the SEZs, pattern of exports and imports, etc. It also covered the concerns of units located in the SEZs and DTA, demand patterns in India, imports vis-à-vis sourcing from Indian SEZs, issues faced by the SEZ units and view on different types of incentives, including reverse job work, and expectations from the government as it designs the new SEZ policy. The core objective of the survey is to understand how to make India a global manufacturing hub for gems and jewellery.

Table 1.2: Pilot Survey Framework

Description	No. of Respondents
SEZs units	14 Respondents and 2 stakeholder consultations
DTA retailers	19 Respondents
DTA manufacturers	5 Respondents and 2 stakeholder consultations
Total	38 Online Respondents; and 4 stakeholder consultations

1.5 Layout

The next section, Section 2, presents an overview of the Indian SEZ policy and the gems and jewellery sector in India and the types of fiscal and non-fiscal incentives that are currently available. Given that India needs to phase out fiscal incentives and focus more on non-fiscal incentives, it then looks at the incentives given by other countries to their gems and jewellery sector in SEZs vis-à-vis those received by the gems and jewellery units in Indian SEZs.

Section 3 looks at the market size of the gems and jewellery sector, international trade in the product, the sector's export potential, and SEZ exports of gems and jewellery. The section, based on secondary data and information analysis, also covers India's position in the global value chain of gems and jewellery. Section 4 presents the key findings of the pilot survey. Section 5 discusses the barriers faced by the sector and Section 6 presents recommendations on how to make units in SEZs globally competitive, enhance exports and domestic value addition, create jobs and enhance investment.

2. Overview of SEZ Policy in India – Fiscal and Non-Fiscal Incentives

SEZs in India were created to achieve economic growth by emulating China's success with SEZs. The SEZ Act, 2005, set out to achieve five objectives; (a) generating additional economic activity (b) promoting the export of goods and services (c) attracting domestic and foreign investment (d) generating employment and (e) developing infrastructure.¹⁰ To meet these objectives, certain fiscal and non-fiscal incentives were given to these zones vis-à-vis the rest of the economy/DTA. The units in SEZs were offered certain income tax exemptions that were conditional upon the units being NFE earners in five years. As mentioned earlier, fiscal subsidy conditional on exports is a prohibited subsidy under the WTO ASCM and, therefore, needed to be withdrawn. Subsequently, income tax holidays available to the Indian SEZs were withdrawn with effect from 31st March, 2020. Some examples of the incentives that are applicable to SEZ developers and units are presented in Figure 2.1.

10 Source: Ministry of Commerce and Industry, Department of Commerce, www.sezindia.nic.in/upload/uploadfiles/files/SEZAct2005.pdf (last accessed July 25, 2022)

Figure 2.1: Examples of Incentives to SEZs

SEZ Developers	SEZ Units
<ul style="list-style-type: none"> • Fiscal Incentives • Exemptions from customs/excise duties for development of SEZs for authorised operations • Zero-rate supplies under the Integrated Goods and Services Tax Act, 2017 • Exemption from state government levies • Income tax exemption • Exemption from central sales tax (CST) and service tax • External commercial borrowings (ECB) after receiving government approval for providing infrastructure facilities within SEZs 	<ul style="list-style-type: none"> • Fiscal Incentives • Customs duty • Zero-rate supplies under the Integrated Goods and Services Tax Act, 2017 • Certain exemptions from state taxes, levies and duties; but these vary across states • Income tax exemption (sunset clause) • Duty-free import/domestic procurement of goods for development, operation and maintenance of SEZ units • Non-Fiscal Incentives • Freedom to sub-contract • Single window clearance system • No licence to import

Source: Compiled from Ministry of Commerce and Industry, Department of Commerce. Available at <http://sezindia.nic.in/cms/facilities-and-incentives.php> (last accessed July 25, 2022)

Fiscal incentives to Indian SEZ units in the past have repeatedly come under scrutiny by other WTO member countries for being WTO non-compliant.¹¹ In fact, with the formation of the WTO, many of its member countries have changed their fiscal incentives to make them WTO compliant and/or have come up with innovative non-fiscal incentives to improve the ease of doing business and reduce costs. Such non-fiscal incentives range from single window clearances to easier work permits and visas for foreign nationals to fast-track patents and/or allowing reverse job work. It is also important to note that the WTO is yet to develop a discipline on subsidies in services and many countries subsidise manufacturing by subsidising services, like cost of worker training and/or subsidising logistics or the cost of information technology, that are used in manufacturing. With increasing servicification of manufacturing, WTO smart subsidies can be designed focusing on the services sector and its linkages with manufacturing.

2.1 Non-Fiscal Incentives and Reverse Job Work – Some Global Examples

To comply with the WTO ASCM, many WTO member countries have either re-oriented subsidies/tax incentives or provided non-fiscal incentives that

help improve the ease of doing business. These non-fiscal incentives range from single window fast-track clearances for investment to fast-track work permits and patents to helping SEZ units optimise the use of their labour, equipment and other resources. Reverse job work, which allows SEZs units and their labour to cater to DTA demand, is one such non-fiscal incentive. It helps optimise the use of sophisticated technologies bought by the units in the SEZs and other resources during periods of lean export demand, and helps SEZ units lower costs and improve their competitiveness.

Countries such as the Philippines, China, Turkey, the USA and Canada have allowed reverse job work in their SEZs (see Box 2.1). These are allowed to help the SEZs firm mitigate risk due to seasonality in demand for exports and cater to domestic demand for certain types of products. The Free Trade Zones (FTZs) in the Middle East in countries like the United Arab Emirates (UAE) and Qatar have autonomous legal framework and high degree of customer orientation that enables them to attract units (World Free Zones Organisation, 2022). In sectors like gems and jewellery, the demand from key markets such as the USA or the European Union (EU) is seasonal. The demand in India is also seasonal but the demand

11 In 2018, the USA challenged India in the WTO for various export-linked subsidies including subsidies given in the SEZs on the premise that India has graduated from the USD1000 GNI mark, ending the transition period of three years. The WTO ruling went in favour of the USA, declaring India's subsidies prohibited and called for a phase out within 90-180 days.

cycles in a country like India and its export markets are different. Therefore, during the lean export period, domestic demand can be catered to from SEZs. Taking this into account, many other countries have allowed reverse job work, which enhances value addition in the country. Since SEZs have the benefits

of duty-free imports, countries ensure that units in SEZs should pay appropriate duties and should not have any undue advantages over units located in the DTA. The countries have also taken care that the core objective of SEZs of promoting exports is retained.

Box 2.1: Learning From the Experience of Other Countries in Reverse Job Work

- The Philippines: The Philippines Economic Zone Authority (PEZA), the government agency set up to enhance investments and incentivise SEZs, allows finished registered export products of free trade enterprises (not included in the negative list) to be sold domestically in the customs territory or retail stores/shopping malls within the commercial/tourist or other authorised areas of the ECOZONES (SEZs), subject to payment of customs duties and internal revenue taxes (as per the provisions of the Retail Trade Nationalization Law, Philippines).
- Guangdong Province of China*: Shantou, Shenzhen and Zhuhai cities of Guangdong province have been designated as SEZs and in these cities, products are allowed to be sold in the interior of China/DTA subject to the approval of the Guangdong Provincial Committee for the Administration of SEZs; these products have to go through the procedures for paying customs duties.
- Turkey: In January 2021, Turkey allowed sales from all its free zones to the domestic market with the exception of consumer and risky products.
- USA: The foreign trade zones (FTZs) in the USA are allowed to sell products in the domestic market, subject to applicable duty rates for the goods entering the domestic market for consumption.
- Canada: In Canada, goods from FTZs can be sold in the domestic market subject to taxes and duty deferment until the time of entry. Duties and taxes need to be paid once the goods enter the Canadian marketplace.

Source: Compiled by authors from <http://www.peza.gov.ph/index.php/about-peza/implementing-rules-and-regulations>; https://www.wto.org/english/thewto_e/acc_e/chn_e/wtaccchn46_leg_8.pdf; <https://www.trade.gov.tr/free-zones/advantages-of-the-turkish-free-zones>; <https://fas.org/sgp/crs/misc/R42686.pdf>; <https://www.canada.ca/en/departement-finance/programs/international-trade-finance-policy/foreign-trade-zone.html> (last accessed July 2, 2021)

Note: *In China, as of 2014, there were 6 SEZs, 14 open coastal cities, 4 pilot free trade areas and five financial reform pilot areas (last accessed July 6, 2021)

2.2. Job Work and Reverse Job Work in Indian SEZs – Past Regulation

Given the linkage between SEZs and DTA provided in the SEZ Act, 2005, and the subsequent amendments made to the SEZ Act, 2005, the consolidated SEZ rules containing amendments allowed job work in the gems and jewellery industry, subject to certain conditions. The job work policy has changed from time to time subsequent to the amendments in the SEZ Act, 2005. Amendment notification number 483 to Part 2 of Section (3), sub-section (1), titled, ‘Special

Economic Zones (Amendment) Rules, 2017, dated June 13, 2017, of the Department of Commerce, Ministry of Industry and Commerce, however, stated that *‘In the principal rules, in rule 50, in sub-rule (1), in clause (c), the word ‘job work’ shall be omitted.’*¹² Some restrictions were also imposed on the gems and jewellery sector “job work”. These were later relaxed by amendment notification number 80 to Part 2 Section 3 Sub Section 1, titled *‘Special Economic Zones (Amendment) Rules, 2019’*, dated February 6, 2019, which allowed “job-work” subjected to certain conditions.¹³ Though the 2019 amendments

¹² Source: <http://sezindia.nic.in/upload/uploadfiles/files/amendmentrule2006.pdf> (last accessed June 26, 2021)

¹³ Source: <http://sezindia.nic.in/upload/uploadfiles/files/Rules%20amendment.pdf> (last accessed June 26, 2021)

to the SEZ Act provide a well-defined policy on job work, a policy on reverse job work in India does not exist. However, the warehousing scheme known as Manufacture and Other Operations in Warehouse Regulations, 2019 (MOOWR Scheme) of the Central Board of Indirect Taxes and Customs (CBIC) allows reverse job work and the government is contemplating allowing reverse job work in export-oriented units (EOUs).¹⁴

The justification for allowing reverse job work is that exports of gems and jewellery from SEZs have their lean and peak periods. Given the significance of the gems and jewellery sector in India's exports and the important role of SEZs in export promotion, reverse job work can be used for addressing the demand seasonality related issues in the sector as has been adopted and successfully demonstrated by countries like China, Turkey, the Philippines and Canada (see Box 2.1). Although the current SEZ policy does not allow reverse job work, the DESH Bill, 2022, has provisions for reverse job work. While gems and jewellery units located in Indian SEZs have been asking that reverse job work be allowed, there is hardly any study on the impact of allowing reverse job work on units in the DTA. There may be concerns that DTA units will face competition and loss of productivity and employment.

2.3 The DESH Bill 2022 and Reverse Job Work

The DESH Bill (2022) proposes to create two kinds of development hubs, the enterprise hub and the services hub. The core objective of the Bill is to provide “for the establishment, development and management of Development Hubs, including Special Economic Zones, as enclaves for the purposes of the promotion of economic activity, employment generation, integration with global supply and value chains and maintenance of manufacturing and export competitiveness, development of infrastructure facilities, promotion of investments, and investment in research and development and for matters connected therewith or incidental thereto”. It aims to allow units to produce for both the domestic and export markets. The bill is expected to allow SEZ units to provide or receive manufacturing services to

and from the DTA. Hence, reverse job work may be allowed. The wider objective of the bill is to promote domestic manufacturing and job creation through the creation of ‘development hubs’, where Indian states can be a partner to development. It takes away the net foreign exchange requirement for incentives and may focus on other performance linked criteria (for example, growth, investment, employment generation or innovation) to give incentives. However, the criteria for giving incentives is not clearly specified in the Bill. There is also lack of clarity on a few areas as given below:

- Will schemes like Remission of Duties and Taxes on Exported Products (RoDTEP) be applicable to SEZ units?¹⁵
- How many units and what kinds of units are eligible for such schemes in development hubs?
- Will the same criteria, for example, R&D and innovation, apply irrespective of the product type (say gems and jewellery versus electronics)? Certain sectors like gems and jewellery are more labour incentive than others.
- How will exports from SEZs to the DTA compare with imports from a country where duty is zero under a trade agreement and which is also a supplier of raw materials? More importantly, will units in SEZs be able to comply with the requirement of 40 per cent domestic value addition under the rules of origin (ROO) after importing the raw material? Or in other words, can labour and other value addition in the SEZ be 40 per cent of the total cost to meet the ROO condition for gems and jewellery?

Regarding non-fiscal incentives, while the Bill seems to have allowed reverse job work, there is yet no clarity on what percentage of the product produced in an SEZ can be sold to the DTA, given that the SEZ should primarily focus on exports. Overall, unless the types of benefits and criteria for giving them are known, it is difficult for gems and jewellery units to understand the impact of the DESH Bill (2022). This is discussed later.

14 Export-oriented units (EOUs) are units that undertake to export their entire production of goods. EOUs can engage in manufacturing, services, development of software, repair, remaking, reconditioning, and re-engineering, including the making of gold/silver/platinum jewellery and articles.

15 The objective of Remission of Duties and Taxes on Exported Products (RoDTEP) is to refund taxes and levies that are not currently refunded:

(i) Duties/taxes/levies at the central, state and local level borne on the exported product, including prior stage cumulative indirect taxes on goods and services used in the production of the exported product and

(ii) Such indirect duties/taxes/levies in respect of the distribution of the exported product

Refer <https://commerce.gov.in/wp-content/uploads/2021/08/Notification-No.-19-English.pdf>

3. Overview of the Gems and Jewellery Sector in India

This section presents an overview of the gems and jewellery sector in India, focusing on market size, growth projections, employment, position in the value chain, international trade, key export destinations and competitors, and the export potential of select gems and jewellery products. It also examines gems and jewellery exports from Indian SEZs and seasonality, if any.

3.1 Market Size and Growth Projections

There is no official data on market size available for India's gems and jewellery industry, making it difficult to have a robust estimate of the market size and future growth. According to India Brand Equity Foundation, the sector has continued on an upward trajectory with its market size reaching USD78.50 billion in FY 21.¹⁶ The same study pointed out that the aim is to have USD70 billion in jewellery export in the next five years (until 2025), up from USD35 billion in 2020. Another study estimates that the gems and jewellery sector contributes around 7 per cent to India's gross domestic product (GDP) and employs over 5 million people. The sector was estimated at INR5.63 trillion in 2020 and is expected to reach

INR6.64 trillion by 2023, with demand growing at a CAGR of 5.60 per cent until 2023.¹⁷ According to India Investment Grid, the industry is projected to touch USD110 billion by FY22.¹⁸ According to Statista (2022), the market size of jewellery and watches in organised retail in India will increase to USD 38 billion by 2025.¹⁹ While estimates vary, they project growth, which is attributed to a rise in disposable income, growing urban population, variety of designs and rise in millennial demand. Some of the estimates and growth projections are presented in Table 3.1.

The sector has gradually corporatized and large retailers and brands are driving growth. The products reach consumers through a variety of retail formats, including online retailing/e-commerce. Indians are one of the largest consumers of gold globally, with the majority consuming 22-carat "pure" gold, unlike consumers in the western market, such as in the UK or the USA, where 9-carat gold or 10-carat gold respectively is preferred.²⁰ However, in recent years, there has been a shift in consumer preference for studded, fusion and light-weight jewellery, according to the participants in the stakeholder consultations. Online buyers also prefer light-weight daily wear jewellery in 18-carat gold.²¹ Manufacturers adopt a mix of machine and hand-made jewellery to cater to this demand.

Table 3.1: Examples of Market Size (Current and Forecast) of India's Gems and Jewellery Sector & Growth Projections

Name of Study	Study Time Frame	Coverage	Market Size in USD Billion (Year)	CAGR* (per cent)	Estimated Market Size in USD billion (Year)
Confederation of Indian Industry	2018-2023	Gold, diamonds, coloured gemstones	75 (2018)	5.6	103.06 (2023)
Statista	2015-2025	Jewellery and watches	10 (2015)	14.28	38 (2025)
India Investment Grid	2017-2022	Gold, diamonds, diamonds in gold, gemstones, silver and others**	55 (2017)	7.8	110 (2022)

Source: Compiled by authors from various sources. Available at <https://www.eoilisbon.gov.in/docs/1613021865Economy%20Matters%20December%202020%20-%20Gems%20&%20Jewellery.pdf>; <https://www.statista.com/topics/5031/jewelry-market-in-india/> ; <https://indiainvestmentgrid.gov.in/sectors/gems-and-jewellery> (last accessed September 14, 2021)

Note: *Compound Annual Growth Rate

**Product category not defined

¹⁶ Source: <https://www.ibef.org/industry/gems-jewellery-india> (last accessed July 25, 2022)

¹⁷ Source: Gems and Jewellery Industry in India | IKON Marketing Consultants (last accessed July 25, 2022)

¹⁸ Source: <https://indiainvestmentgrid.gov.in/sectors/gems-and-jewellery> (last accessed July 25, 2022)

¹⁹ Source: <https://www.statista.com/topics/5031/jewelry-market-in-india/> (last accessed October 26, 2022)

²⁰ Source: Why Indians are increasingly buying low carat gold jewellery for non-investment purposes - The Economic Times (indiatimes.com) (last accessed October 26, 2022)

²¹ Source: Jewellery market structure: India gold market series | World Gold Council (last accessed October 26, 2022)

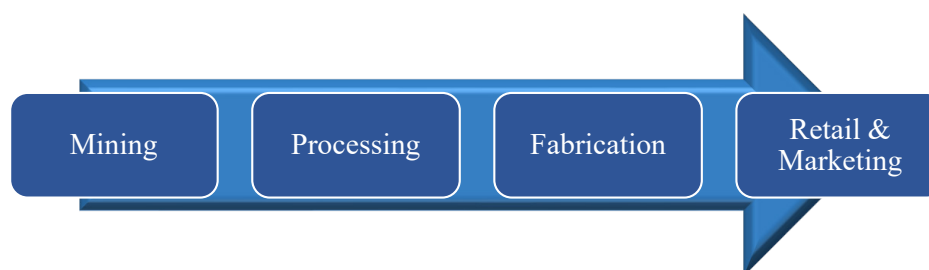
The gems and jewellery sector in India is fragmented and unorganised, resulting in lack of data on clusters, investment, and number of employees. Even units in the organised sector have contractual and seasonal employment. According to the Annual Survey of Industries (ASI) NIC code 321, there were 1,64,666 workers in the jewellery, bijouterie and related articles sector during 2018-19, a 7 per cent decline from 2017-18.²² A study by the National Council of Applied Economic Research (NCAER, 2020) estimated 341 gems and jewellery district clusters, employing 42.89 lakh workers. A substantial proportion of employees in gems and jewellery manufacturing are present in the sub-categories hand-made jewellery (31.6 per cent) and diamond jewellery (19.1 per cent). The use of machines and technology in the sector is rising, according to the same study.

3.2 Indian Companies in Gems and Jewellery Global Value Chain

The gems and jewellery industry functions in a four-stage production chain (1) mining/extraction (2) processing through cutting and polishing (3) fabrication and (4) retail to consumers (see Figure 3.1).

India is a net importer of raw materials. India's major role begins in the processing stage, followed by manufacturing and then retailing. Cutting and polishing diamonds and other precious stones are some of the major tasks performed in India.²³ In manufacturing, India has well-established capabilities in making cast, diamond set jewellery, hand-made gold, and gem set jewellery. In the area of diamonds, Indian jewellers have been focusing on moving up the value chain, from polishing rough diamonds to manufacturing jewellery.²⁴

Figure 3.1: Value Chain of Gems and Jewellery



Source: Based on report titled “Human Resource and Skill Requirements in the Gems and Jewellery Sector-2022” National Skill Development Council (NSDC). Available at http://www.investment-hr.com/next_opper_doc/INDIA-Gems-Jewellery%20-.pdf (last accessed June 26, 2021)

3.3 India's Trade in Gems and Jewellery

The following sub-sections cover India's total gems and jewellery trade, product-wise trade, its key competitors globally, export potential of the sector, and export pattern over the decade 2011-12 to 2021-22. The final sub-section looks at gems and jewellery exports from SEZs and their share in total gems and jewellery exports. Although India is positioned in the processing stage of the value chain of the gems and jewellery sector, it is difficult to identify the extent of value addition by SEZs in the sector due to unavailability of longitudinal data on product wise exports and any data on imports of the gems and jewellery SEZs.

3.3.1 India's Total Trade of Gems and Jewellery

India's exports of gems and jewellery increased from USD32.46 billion in 2010 to USD38.15 billion in 2021 (see Figure 3.2). However, during 2010-2021, exports have shown a variable trend, growing to a value of USD50 billion in 2011 and registering the lowest export value of USD24.45 billion in 2020. A similar trend is seen in the imports of gems and jewellery during this period. India's imports of gems and jewellery increased from USD68.3 billion in 2010 to USD88.3 billion in 2021. Both imports and exports declined substantially and reached the lowest in 2020, owing to the COVID-19 pandemic-induced restrictions. In 2021, exports recorded a year-on-year growth of 56 per cent whereas imports increased by

²² Source: <http://www.csoisw.gov.in/CMS/cms/Feedback.aspx> (last assessed on August 13, 2021)

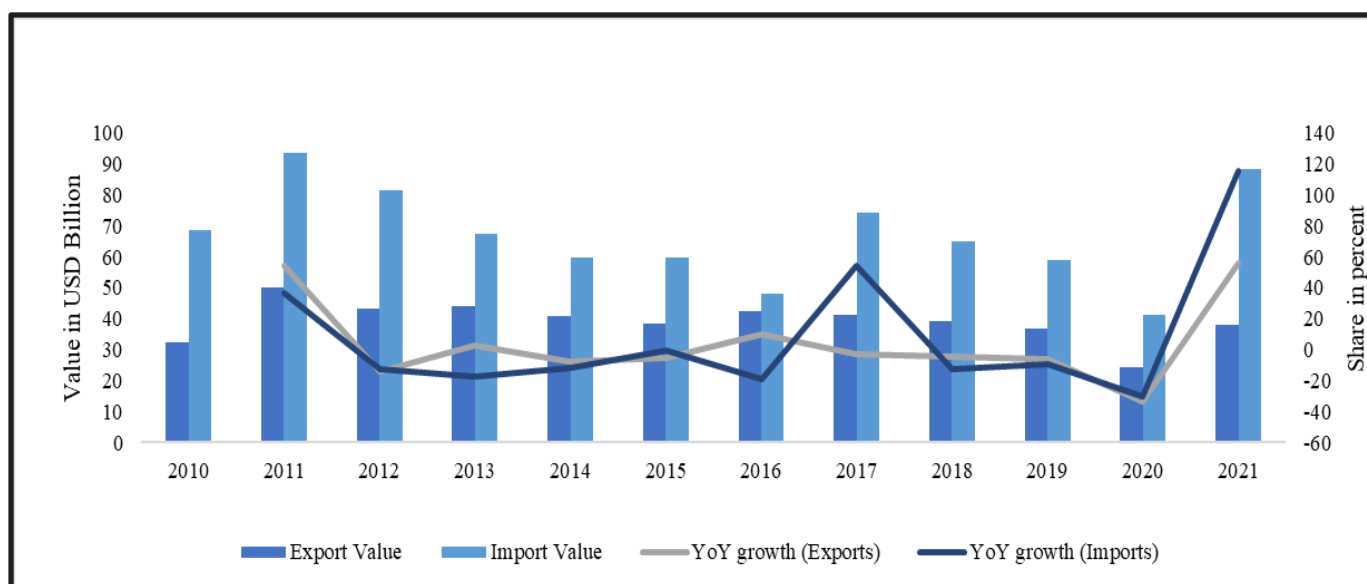
²³ Source: <https://www.rough-polished.com/en/analytics/119913.html> (last accessed June 28, 2021)

²⁴ Source: <https://www.diamondworld.net/contentview.aspx?item=2226> (last accessed June 28, 2021)

115 per cent. In 2021, India ranked 6th globally in gems and jewellery exports with a share of 4.7 per

cent.²⁵ India is a net importer of raw materials and there is strong import dependency.

Figure 3.2: India's Trade in Gems and Jewellery, Calendar Year (2010-2021)



Source: Author's own, based on data from UNComtrade. Available at <https://comtrade.un.org/data/>

3.3.2 India's Product-wise Trade of Gems and Jewellery

The exports of all product categories of gems and jewellery sector showed a positive growth rate between 2010 and 2021. The highest growth is observed in the exports of lab grown diamonds and silver jewellery. Between 2010 and 2021, silver jewellery exports have grown more than its imports (see Table 3.2) while coloured gemstones imports have grown more than

its exports. Export of gold jewellery has increased only by 1 per cent. Global demand for gold in 2021 was 948 tons, 8 per cent lower than the demand in 2020.²⁶ While imports of finished gold jewellery has grown at a compound annual growth rate (CAGR) of 7 per cent, the import of raw material, i.e., gold bars, declined over the period 2010-11 to 2021-22. Although cutting and polishing diamonds is prominently done in India, its exports have only grown by 0.7 per cent during the period 2010-21.

Table 3.2: India's Trade in Gems and Jewellery, Product-wise

Amount in USD billion, CAGR in Per cent

Product Category	Export		CAGR*	Import		CAGR*
	2010	2021	2010-2021	2010	2021	2010-21
Gold Jewellery (711319)	7.47	8.43	1.01	0.69	0.50	(-)2.65
Silver Jewellery (711311)	0.36	2.12	15.93	0.04	0.06	7.06
Cut & Polished Diamonds (710239)	21.71	23.80	0.77	19.97	8.50	(-)6.36
Coloured Gemstones (7103)	0.31	0.76	7.69	0.35	1.69	17.22
Lab-grown diamonds (710490, 710420)	0.01	1.25	47.58	0.02	2.84	48.87

Source: Extracted and compiled from UNComtrade Database, available at <https://comtrade.un.org/data/> (last accessed July 26, 2022)

Note: *Compound Annual Growth Rate

²⁵ Source: <https://www.gjepec.org/statistics.php> (last accessed July 25, 2022)

²⁶ Source: https://www.business-standard.com/article/markets/gold-jewellery-demand-in-india-likely-to-dip-in-h2-world-gold-council-122072800149_1.html (last accessed August 03, 2022)

3.3.3 India's Key Export Destinations and Key Competitors

In 2021, the USA, Hong Kong, the United Arab Emirates (UAE), Belgium and Israel were the top five destinations for Indian gems and jewellery exports (see Figure 3.3). In these markets, India faces competition from China, the USA, Switzerland and Italy. While China remains a key competitor in gold and silver jewellery, the USA is closely catching up with India in cut and polished diamonds. Overall, key competitors vary by product categories.

According to participants in the stakeholder consultations, Indian exporters face tough competition in the export of products like light weight gold jewellery from countries like Turkey. India's gold jewellery exports have grown only marginally, and imports have declined between 2010 and 2021, due to tough competition, primarily from Turkey. Turkey ranks among the top three global gold jewellery producing countries,²⁷ and its exports and imports of gold jewellery are growing at a CAGR

of 15 per cent and 9.5 per cent respectively. Turkey's import of raw materials for gold jewellery has also increased, signalling an increase in its manufacturing. According to the respondents of KIIs and stakeholder consultations, Turkish units have spent more on research and development (R&D) and innovation and are now able to offer tough competition. Turkey allows reverse job work and permits its free trade zones to cater to demand in the domestic market, and both, exports to third countries as well as the domestic market, have increased between 2016 and 2021.²⁸ Turkey is strongly positioning itself in markets where India has been the leading exporter of gold jewellery such as the UAE, the United Kingdom (UK), and Hong Kong. According to the survey respondents, minimising the weight of gold and use of better technology has become a priority for Indian gold jewellery manufacturers to cater to the growing demand for light weight jewellery.²⁹ At the same time, Indian exporters are striving hard to be price competitive with exports from countries like China, Turkey and Thailand.

Figure 3.3: Key Export Destinations and Competitors of India's Gems and Jewellery, 2021



Source: Extracted and Compiled from UNComtrade. Available at <https://comtrade.un.org/data> (last accessed August 03, 2022)

3.3.4 Export Potential of Select Categories of Gems and Jewellery

This section uses the International Trade Centre (ITC) export potential map tool to assess the export potential of select categories of India's gems and jewellery sector. The Export Potential Indicator, is a combination of 3 factors: (i) supply, (ii) demand, and

(iii) easiness to trade and is calculated as follows:

$$EP_{ijk} = Supply_{ik} \times Easiness_{ij} \times Demand_{ijk}$$

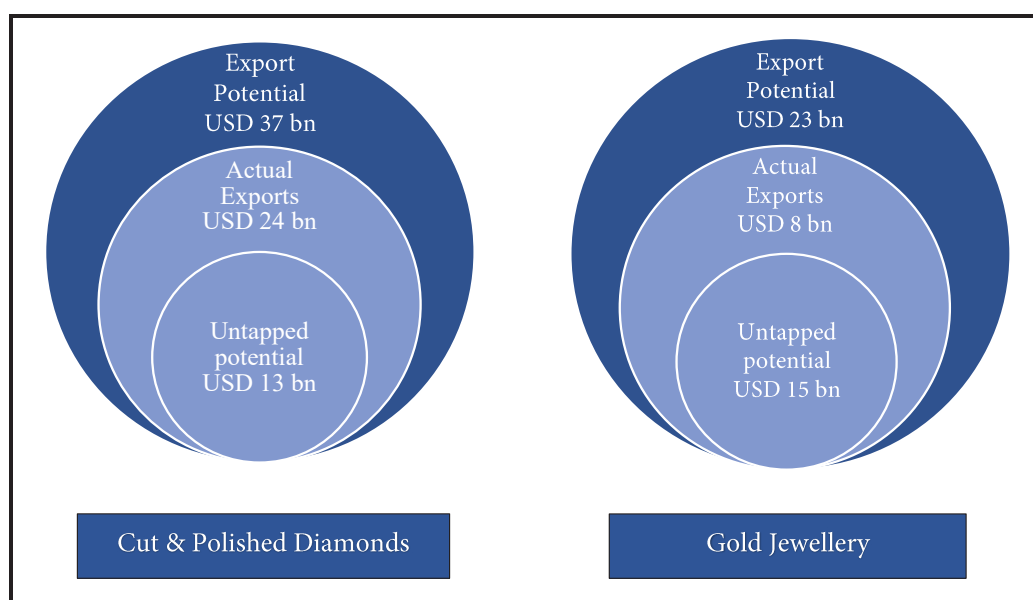
where i stands for exporting country, j for the destination country and k for the product (Decreux & Spies, 2016).

²⁷ Source: <https://www.trade.gov.tr/data/5b8fd5bf13b8761f041fee9b/Gold%20Jewellery.pdf> (last accessed August 03, 2022)

²⁸ Source: https://www.trade.gov.tr/data/61efdeb313b876476cc9faa0/statistics_of_the_turkish_free_zones_Jan2022.pdf (last accessed August 3, 2022)

²⁹ Source: <https://www.msn.com/en-in/money/topstories/gem-26-jewellery-exporters-bank-on-india-international-jewellery-show-2022-to-sustain-post-covid-growth-ar-AA-10ipuj?fromMaestro=true> (last accessed August 03, 2022)

Figure 3.4: India's Export Potential in Gems and Jewellery across Selected Categories, 2021



Source: Author's own, based on ITC Export Potential Map calculations

Figure 3.4 shows that there still remains huge untapped export potential in the cut and polished diamonds category of USD13 billion and in the gold jewellery category of USD15 billion. In cut and polished diamonds, India's actual export is around USD24 billion, less than the export potential of USD37 billion. Similarly, in gold jewellery, the actual exports of around USD8 billion lags behind the export potential of USD23 billion. The untapped export potential in selected gems and jewellery products signals ample room for the growth of the sector in the future.

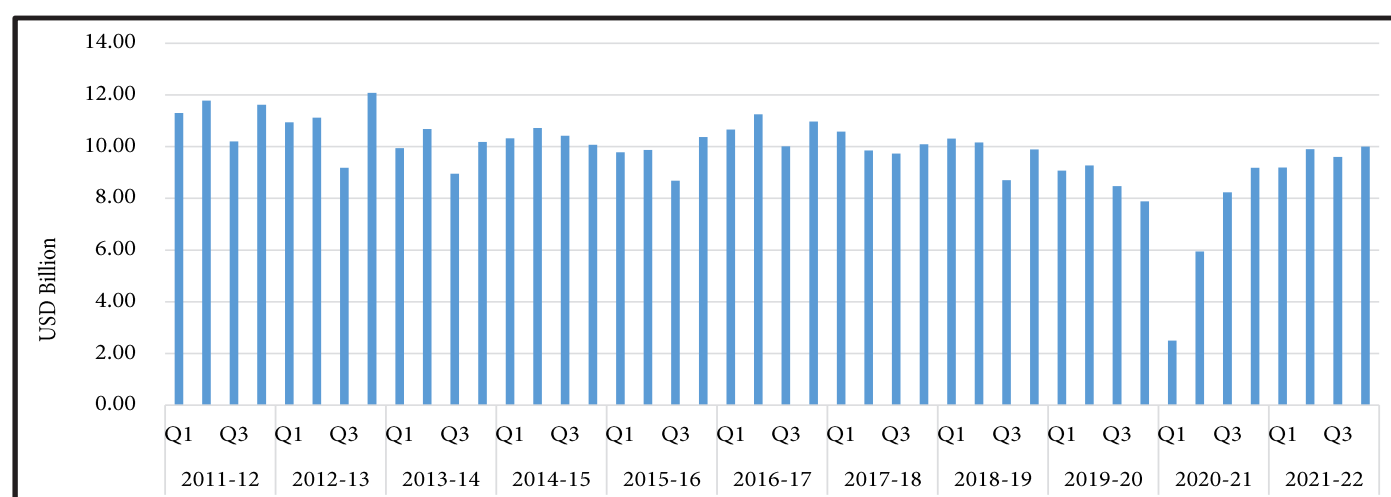
3.3.5 Seasonal Variation in India's Gems and Jewellery Exports

During the stakeholder consultations, gems and

jewellery exporters said that exports have a seasonal pattern with exports concentrated in certain quarters of the year. To understand trends, we have tried to map exports by the four quarters of the financial year, namely Q1 (April to June), Q2 (July to September), Q3 (October to December) and Q4 (January to March) between 2011-12 and 2021-22.

Gems and jewellery exports peaked during the second and last quarter over the last 10 years, followed by Q1 (see Figure 3.5). However, exports during Q1 2021-22 were the lowest, which may be due to COVID-19 induced supply chain disruptions. Over the last 10 years, exports have been the lowest during Q3 except in FY 2021-22. So, there seems to be some kind of seasonality.

Figure 3.5: Seasonal Variation in India's Exports of Gems and Jewellery, 2011-12 to 2021-22



Source: Extracted and Compiled from UNComtrade, Available at <https://comtrade.un.org/data/> (last accessed August 03, 2022)

Note: Financial Year Quarters have been considered.

3.3.6 Gems and Jewellery Trade in Indian SEZs

The data on exports and imports of gems and jewellery from SEZ is available only for two years and therefore cannot be used for robust analysis of seasonality and extent of value addition.

The available data shows that SEZs exports of gems and jewellery were USD10.66 billion during FY 2019-2020, accounting for a share of around 30 per cent in total gems and jewellery exports. During FY 2020-

21, SEZs exports of gems and jewellery halved to USD5.22 billion, primarily due to pandemic related demand and supply chain disruptions and thus their share in total gems and jewellery exports also declined to around 20 per cent. However, gems and jewellery SEZs share in total imports rose from 22.5 per cent in 2019-20 to around 33 per cent in 2020-21. Between 2019-20 and 2020-21, the deficit in gems and jewellery SEZs balance of trade also increased from USD1.58 billion during 2019-20 to USD12.77 billion during 2020-21 (see Table 3.3).

Table 3.3: Gems and Jewellery Trade in Indian SEZs and Their Share in Total Gems and Jewellery Trade and Balance of Trade (BoT)

Financial Year (FY)	Total G&J Exports from SEZ (USD Billion)	Share in Total Exports (in Per cent)	Total Imports in G&J SEZ (USD Billion)	Share in Total Imports (in Per cent)	Balance of Trade in G&J SEZ (USD Billion)
2019-2020	10.66	29.59	12.24	22.54	-1.58
2020-2021	5.22	20.10	17.99	32.88	-12.77

Source: Calculated from data provided by the Department of Commerce, Ministry of Commerce and Industry

Note: Data provided were in INR crores and is now converted to USD billion using RBI's Financial Year (FY) Annual Average conversion rate <https://rbi.org.in/scripts/PublicationsView.aspx?id=21234>

3.3.7 SEZ Supply from the DTA and SEZ-DTA Sale

Table 3.4 shows the link between gems and jewellery units in the SEZs and DTA. During 2019-20 and 2020-21, more than 95 per cent of DTA supplies to the gems and jewellery SEZs are of diamonds, while other commodities account for only a minuscule share. The survey found that this may be because

the SEZ units are giving job work like diamond polishing to the DTA. SEZs sales to the DTA in heavy handcrafted gold jewellery has drastically increased from INR17735 crore during 2019-20 to INR96246 crore during 2020-21. This sharp increase indicates that although international demand for heavy gold jewellery manufactured in Indian SEZs is reducing, the domestic demand for the same is rising.

Table 3.4 Gems and Jewellery SEZs Supplies from the DTA and SEZ-DTA Sale

Product Code	Description	SEZ Supplies from DTA (INR crore)		SEZ-DTA Sale (INR crore)	
		2019-20	2020-21	2019-20	2020-21
7102	Diamonds, whether or not worked, but not mounted or set	4135	4325	-	-
7103	Precious stones (other than diamonds) and semiprecious stones	220	182	-	-
7104	Synthetic or reconstructed precious or semiprecious stones, whether or not worked or graded but not strung, mounted or set	126	127	-	-
7108	Gold (including gold plated with platinum) unwrought or in semi-manufactured forms, or in powder form	-	-	17735	96246

Source: Department of Commerce, Ministry of Commerce and Industry

Some highlights, emerging from the analysis of the trade in gems and jewellery, are presented in Box 3.1.

Box 3.1: Key Highlights of Gems and Jewellery Trade

- **Lower Growth of Exports:** In gold jewellery, and cut and polished diamonds, exports have grown marginally during 2010-2021.
- **Increasing Trade Deficit:** Trade deficit of SEZs in the gems and jewellery sector has increased significantly between 2019-20 and 2020-21. The growing negative trade balance is a cause for concern.
- **SEZ-DTA Link:** There has been an increase in the sale of gold jewellery from SEZs to DTA between 2019-20 and 2020-21. During this period, SEZ supplies from the DTA were predominantly in diamonds, reflecting SEZs units may be engaged in job work.
- **Falling Share of SEZs Exports:** The share of SEZs in total gems and jewellery exports from India has fallen from around 30 per cent during 2019-20 to around 20 per cent during 2020-21. The decline has been attributed to pandemic related demand and supply chain disruptions, SEZ policy uncertainty, etc., by the survey respondents.
- **Seasonality in Exports:** Over the past decade, between 2011-12 and 2021-22, gems and jewellery exports have been seasonal with Q2 (July-September) and Q4 (January-March) as the peak period and Q3 (October-December) as the lean period. Seasonality in exports in SEZs could not be calculated due to the unavailability of longitudinal export data by quarters.

Source: Based on secondary trade data analysis

4. Key Findings of the Survey and Stakeholders' Consultations

This section presents the key findings of the pilot survey, which covered 14 units located in the SEZs, 19 retailers located in the DTA, five DTA manufacturers (total 38 online survey respondents) and 4 stakeholder consultations.³⁰ The survey aimed to get the perspectives of the SEZ units, DTA retailers and DTA manufacturers on export performance, investment, issues and fiscal and non-fiscal incentives, including reverse job work. While the following subsections cover the key findings of the survey, the barriers are presented in Section 5.

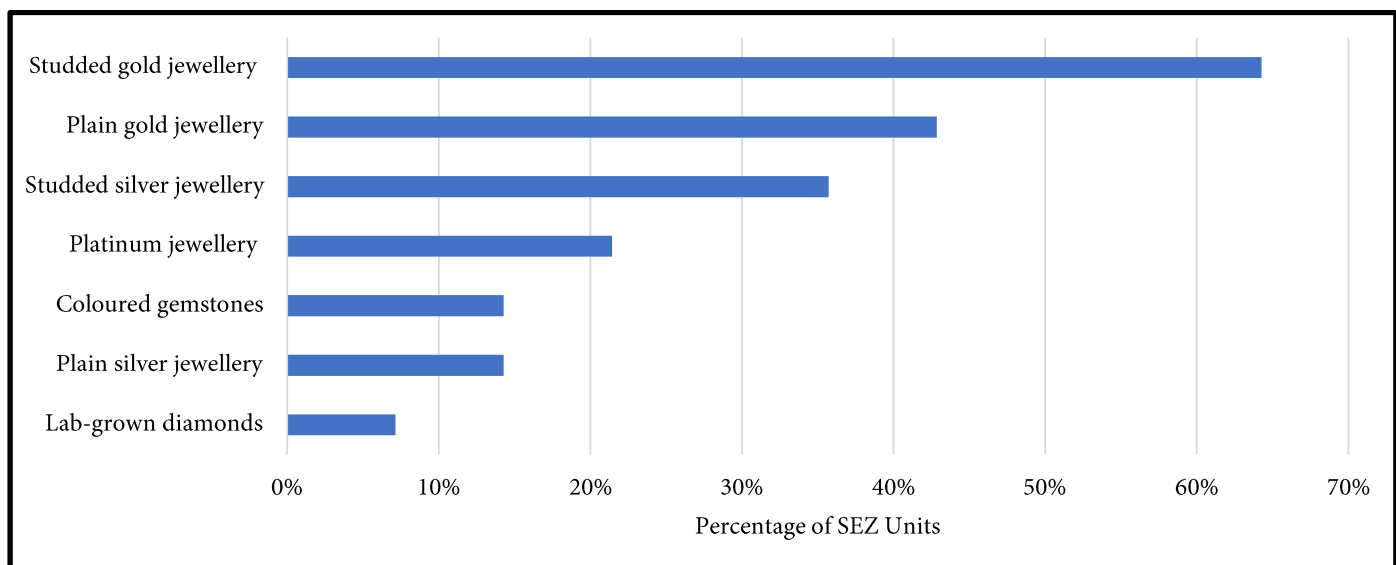
4.1 Perception of Units in SEZ

Filled in questionnaires were received from 14 units located in four SEZs, namely, Surat SEZ, SEEPZ, Sitapura SEZ, and Manikanchan SEZ across the states of Gujarat, Maharashtra, Rajasthan and West Bengal respectively. Around 20 members and sector experts were also consulted for their qualitative responses.

All the 14 units are involved in the production of gold jewellery, either studded or plain, with varying share in the total output of the unit. Studded gold jewellery is the most common product across all the units (64 per cent), followed by plain gold jewellery (43 per cent), and studded silver jewellery (36 per cent) (see Figure 4.1). Platinum jewellery, and coloured gemstone jewellery are only produced by the sample units located in SEEPZ, Maharashtra, and Sitapura SEZ, Rajasthan, while lab-grown diamond jewellery is only produced by the units in SEEPZ, Maharashtra.

³⁰ The survey does not cover artificial jewellery

Figure 4.1: Product-wise Distribution of Units in SEZ



Source: Pilot Survey of SEZ Units

Note: One SEZ unit can be involved in more than one type of jewellery.

4.1.1 Investment across SEZ Units

Investment is mostly concentrated in ‘plant and machinery’ and ‘building’. Only four units out of the sample of 14 reported having invested in R&D, technological advancement, and skilling of the workforce. This is an area of concern as units from competing countries like Turkey are investing in these areas. It is important to note that all the units reported domestic investment as the source of capital. Only two units, one each in SEEPZ, Maharashtra, and in Manikanchan, West Bengal, reported foreign direct investment (FDI) along with domestic investment. Overall, FDI inflows in this sector is low, even for units in SEZs.

4.1.2 Exports from SEZ Units

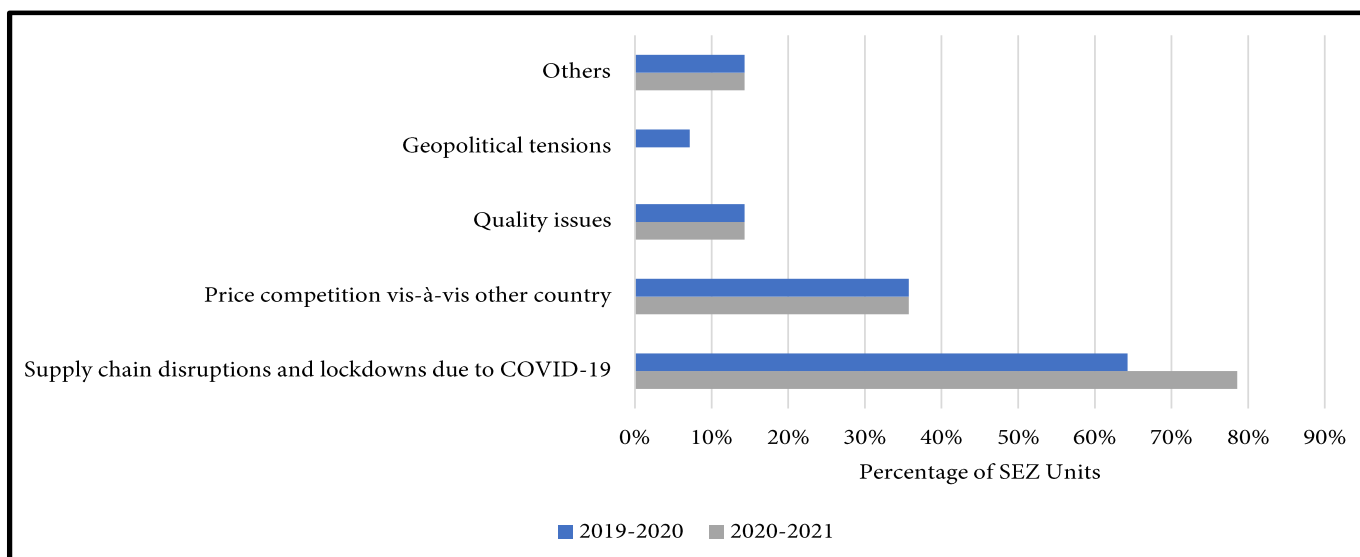
The survey revealed that the top five export markets of the SEZ units are the USA, the UK, the UAE, Australia, and Singapore. The secondary analysis also identified the USA and the UAE as the key export destinations for Indian gems and jewellery exports (see Section 3.3.3). Most of the units in the survey said that export demand has a seasonal trend and, in the lean season, their labour and equipment remain idle while in the peak season, they engage in job work with the DTA.

4.1.2.1 Factors Adversely Affecting Exports

Overall, exports are declining and units in SEZs face an uncertain export situation due to various factors. For a majority of the units (64 per cent), supply chain disruptions and lockdowns due to the COVID-19 pandemic have disrupted exports in the last two years, 2019-20 and 2020-21. The other top reasons listed by the SEZ units were price competition vis-à-vis other countries, quality issues, and geopolitical tensions (see Figure 4.2). These are further discussed in Section 5.

According to the surveyed Indian SEZ units, SEZ units in countries like China and Turkey are able to offer competitive prices due to policies like reverse job work, which allows more efficient utilisation of labour and equipment during periods of low export demand. They explained that workers in SEZs need to be trained. If a unit employs a permanent trained workforce, this workforce has to be efficiently employed throughout the year and not just during the period of peak export demand. The workforce and equipment in Indian SEZs remain underutilised during the lean period/if there is low demand in export markets. Such under-utilisation adds to the cost of production.

Figure 4.2: Factors that Adversely Impacted Exports of SEZ Units in 2019-20 vs. 2020-21



Source: Pilot Survey of SEZ Units

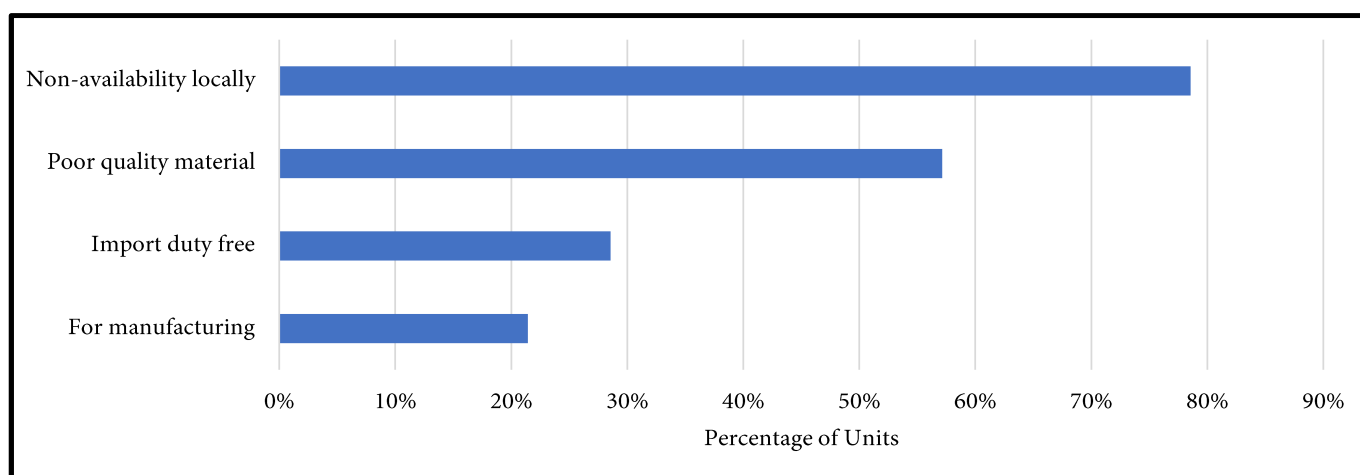
Note: Other reasons include lack of access to domestic skilled workers and restrictions on sourcing locally made products for exports

4.1.3 Import of Raw Materials/ Intermediate Goods

The survey and consultations confirmed that the sector is import dependent for raw materials due to a variety of reasons listed in Figure 4.3. The most commonly imported material by the surveyed units is raw/pure gold from the UAE (36 per cent), due to lack of availability in India, and duty-free imports.

Units locate in SEZs to get the benefit of duty-free imports. However, if duty free imports come into the DTA through India's trade agreements, and/or if DTA units get some form of subsidies, which are not applicable to the SEZs, then units located in the SEZs are at a disadvantage as they are not allowed to cater to the DTA under the same terms and conditions as a unit located in an FTA partner country or DTA units in India.

Figure 4.3: Top Reasons Cited for Importing Raw Material/Intermediate Products



Source: Pilot Survey of SEZ Units

Note: Multiple Choice Question

4.1.4 Benefits Received in an SEZ

There are several benefits of being located in an SEZ. The most common benefits, across the units surveyed,

covered both fiscal and non-fiscal incentives as shown in Figure 4.4. Since raw materials are imported, duty free import is among the top fiscal incentives received in an SEZ. Zero-rated goods and services tax (GST)

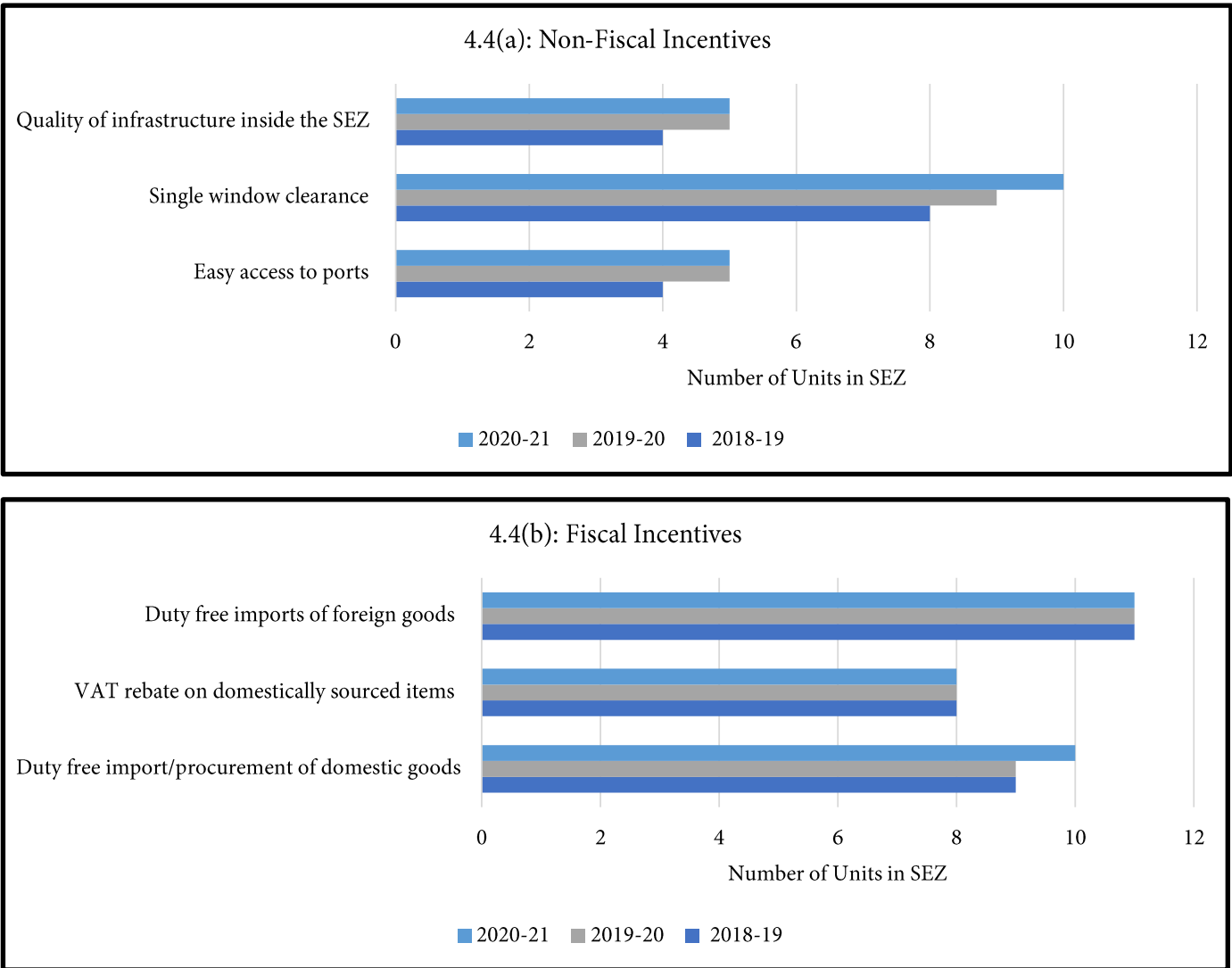
was another fiscal incentive mentioned by the units in SEEPZ, Maharashtra, and Manikanchan, West Bengal.³¹

Among non-fiscal incentives, the ease of doing business in terms of fast-track clearances and better infrastructure has in the past attracted units to the SEZs. However, there is scope to further improve infrastructure by creating R&D hubs, high quality common user facilities and/or innovation centres in the zones.

During the survey, units were uncertain about the future benefits in SEZs as the policy has been pending for long. They said that while they have benefited from the job work policy during the peak

season, many of their employees are permanent and they want to create a permanent skilled workforce and upgrade equipment. Therefore, they would like to have a clear and transparent reverse job work policy for optimum labour and equipment utilisation. They would also need a reverse job work policy to cover after sales services to DTA clients. They said that units in SEZs can cater to the demand for imported jewellery and policy should facilitate it. With increasing servicification of manufacturing, SEZ units said that the future SEZ policy may look at subsidising services used in manufacturing, which will be WTO compliant. Units also expressed their concern about the performance indicators future benefits are likely to be linked to.

Figure 4.4: Top Three Benefits of Being Located in SEZ over the Last Three Years



Source: Pilot Survey of SEZ Units

31 Previously, units in the SEZ were exempt from central sales tax, service tax and state sales tax, which were subsumed under IGST Act, 2017, and services/goods to SEZs are taxed at zero (0) per cent. For more details see <http://sezindia.nic.in/cms/facilities-and-incentives.php> (last accessed September 21, 2022)

4.1.4.1 Importance of Non-Fiscal Incentives

The units in SEZs received certain benefits in terms of tax exemptions; these have now been withdrawn due to their non-compliance with the WTO ASCM. According to 64 per cent of the surveyed units, fast-track clearances and allowing job work, subject to certain conditions, were the most important non-fiscal incentives. Fifty-seven per cent of the units opined reverse job work was also an important non-fiscal incentive.

4.1.4.2 Importance of Fiscal Incentives

In India, logistics and other input costs like electricity are high and, according to the surveyed units, fiscal incentives help reduce costs and improve price competitiveness. Units in the SEZ claimed they would face issues, such as reduced price competitiveness in the international market, if fiscal benefits are withdrawn since it would raise input and production costs.

All units felt that fiscal benefits should be given priority and smartly designed to make it WTO compliant. If the government gives a package of non-fiscal incentives, like allowing for DTA sale and reverse job work, it may improve productivity and efficiency and enhance the ease of doing business.

4.1.5 SEZs' Engagement with the DTA

A manufacturing unit within the SEZ can be engaged with DTA in two ways: by (i) providing job work to workers in DTA during the peak season and/or (ii) catering to the DTA retailers' demand for gems and jewellery. The key findings of the survey, regarding SEZ units engaging with DTA, are discussed in the following subsections.

4.1.5.1 Job-Work to Workers in DTA

To cater to the increased demand during the peak quarters, SEZ units give job work to DTA labourers on a temporary basis. Of the 57 per cent SEZ units who engage in job work, 75 per cent said that they give job work to DTA workers.

4.1.5.2 Opportunity to Cater to the DTA

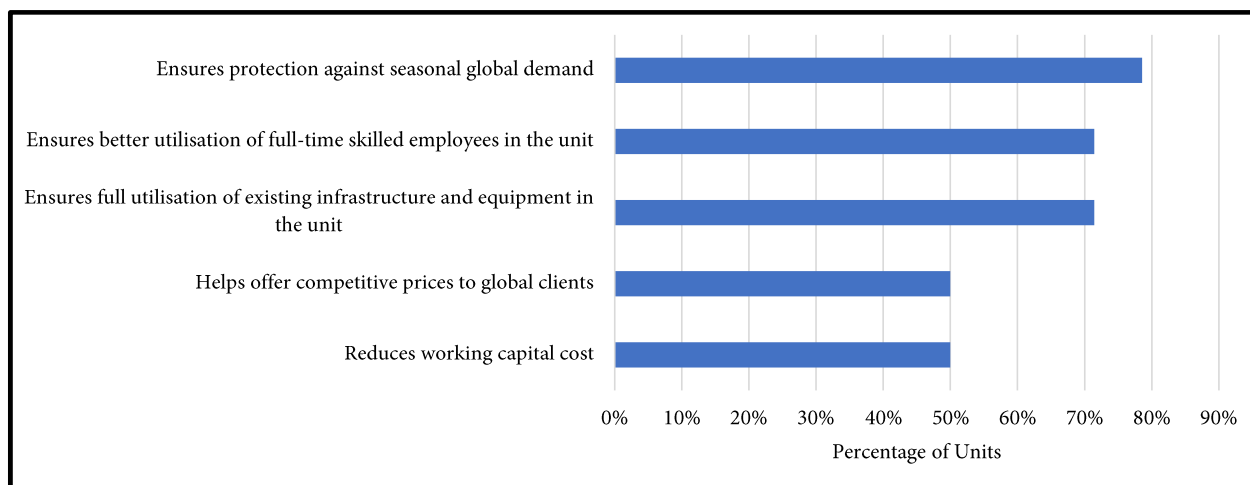
According to 64 per cent of the SEZ units, domestic demand for jewellery is growing. They can support this increase in domestic demand if they are allowed to sell to DTA manufactures and/or retailers. Eighty-six per cent of the units said they will benefit from

ease of sale in the DTA, but 79 per cent said that they are interested in selling in the DTA. Some said that selling in the DTA also implies that they may need to offer after sales service. Some units said that since their location in SEZs are primarily for exports and benefits are linked to exports, there may be a limit on how much they can sell in the DTA. Besides, the terms and conditions under which they can sell in the DTA are important. For example, if the raw material is imported, they may not be able to meet the 40 per cent value addition condition on rules-of-origin for exports to the DTA.

Seventy-one per cent of surveyed SEZ units said that they would benefit from a transparent reverse job work policy. Reverse job work, according to them, helps address the issue of seasonality of demand and, therefore, workers can be gainfully employed throughout the year. This also leads to more efficient utilisation of equipment, which remains idle during the lean period. Further, though imports might not decline immediately, if SEZ units are allowed to export to the DTA, in the long run it may, and the policy will allow world class products to enter local Indian markets. For example, many Indian retailers currently import jewellery or products from Italy or Europe due to better finishing. SEZs can help fulfil this demand as units in the SEZ have the needed experience and capability to manufacture products of international quality. Thus, importers/retailers can source world class jewellery from domestic SEZ units rather than the international market – in line with the 'Aatmanirbhar Bharat' campaign.

Many SEZs units also have manufacturing units in the DTA. They can combine all units in one place instead of running two duplicate operations, which would also ensure better and more efficient utilisation of resources. This may lead to economies of scale. The units are happy to pay the applicable duty while catering to the DTA. If allowed to cater to the domestic market, the SEZ units opined that production costs, which increased after the withdrawal of fiscal benefits (for example tax holidays) making it very expensive to maintain SEZ units only for exports, would decrease. Reverse job work also allows the creation and retention of permanent employment throughout the year. There will be more value addition and job creation in the country, and it will allow SEZ units to serve customers better by maintaining international standards in manufacturing, as more skilled workers and tools and technology are available with the SEZs. It will increase the profitability of SEZ units (see Figure 4.5).

Figure 4.5: Benefits of Allowing Reverse Job Work



Source: Pilot Survey of SEZ Units

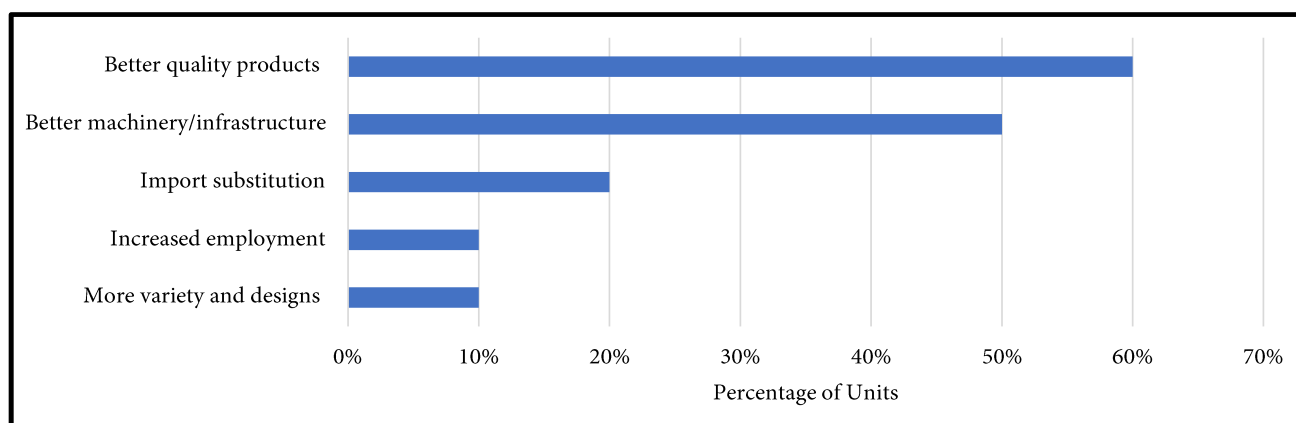
Currently, Indian companies in SEZs produce for overseas brands and retailers. The knowledge, technical knowhow and proprietary information that has been gained by working with global units can be used to benefit the local Indian industry and market. The product quality will be better, which in turn, will improve sales and make the units cost effective.

There are long-term benefits. India has the potential to become a leading hub for gems and jewellery processing and this will require modernisation of the sector. As technology and knowhow penetrates the domestic market, the industry will over time modernise and the workforce will become skilled. The surveyed units said that currently SEZ units in India are competing with units in China, Turkey and Thailand, where most units are allowed to both export and cater to the domestic market (DTA sales). In India, SEZ units have been proactive in developing world-class manufacturing facilities and products. The export markets function in a typical business cycle, with a few months of high and then low activity. Hence, allowing DTA access to SEZ

units will enable them to manage their costs better, employ workers round the year and avoid losses in case one of the export markets performs weakly. Thus, reverse job work will allow SEZ units to make use of the investment made on space, manpower and machinery more efficiently compared to the current scenario where SEZ units are completely dependent on global sales cycles that are becoming increasingly unpredictable.

The SEZ units pointed out that reverse job work can provide better quality products and new trendy designs to Indian consumers, which are not available in the market, like platinum and palladium jewellery. It also allows for better quality products at a cheaper price with faster delivery compared to imports from other countries (see Figure 4.6). Reverse job work allows DTA units access to a skilled workforce, who can deliver better quality products, and, with cost optimisation, units can invest in technology and R&D, and in better designs and variety to increase profit (see Figure 4.6).

Figure 4.6: Benefits to DTA Retailers on Sourcing from SEZ Units



Source: Pilot Survey of SEZ Units

According to the surveyed DTA retailers, products from SEZ units have better finishing and more western designs, and it, therefore, would be beneficial to source from SEZ units, subject to payment of duty (see section 4.2.3).

4.1.5.3 Likely Impact of Reverse Job Work on DTA Manufacturers

Allowing SEZ units to cater to the domestic market may adversely impact DTA manufacturers; therefore, the survey covered DTA manufacturers located near SEZ manufacturers to understand the impact of reverse job work on DTA units, especially in terms of access to labour, if allowed. There is concern among some DTA units on the implication of allowing reverse job work to SEZ units and whether this would lead to business loss and labour shortages. Consultations with jewellery units revealed that a majority believed that the purpose of locating a manufacturing unit in the DTA and in the SEZ are different and is dependent on the objective of the firm. While a unit in the SEZ is primarily export focussed, a unit in the DTA caters to both exports and the domestic market with primary focus on the domestic market. While the SEZ provides certain incentives, a manufacturer can also locate in the DTA and avail duty-free imports if India has an FTA with the trading partner or if such benefits are given unilaterally through policies like the foreign trade policy. In other words, incentives are being availed by units in both SEZs and the DTA, but the type of incentives may vary. Units review the incentives and market they want to cater to and accordingly locate in an SEZ or the DTA.

As the gems and jewellery industry moves towards specialisation in terms of products, companies leverage each other's strengths and specialisations to cater to changing consumer preferences and demand; therefore, DTA manufacturing units are keen to take advantage of manufacturing inside SEZ units for better processes, techniques and designs to enhance their exports. DTA manufacturing units felt that SEZs should be allowed to cater to the domestic market, subject to payment of duties, to add value to the Indian gems and jewellery market, generate employment in the sector, and for import substitution in line with the central government's 'Aatmanirbhar Bharat' and 'Make in India' initiatives. Two of the surveyed units said that the domestic consumer will get price benefits, as the prices of SEZ products will be lower than that of imported goods, in addition to easy availability, procurement and after sales services. At the same time, DTA manufacturers felt that they may be hard hit and it may defeat the purpose of locating in an SEZ if the unit in the SEZ does not export at

least 60 per cent of its production. In other words, there should be a limit on sales in the DTA, which can be 40 per cent or less of total production.

According to DTA manufacturers, the domestic market will expand at more than six per cent in the next five years, resulting in an increase in the demand for labour by the gems and jewellery sector. An increase in labour demand in SEZs through reverse job work can lead to shortages of skilled workforce in the DTA and, therefore, there is need for training and skill upgradation, which the government should support through the right policy initiatives. There are shortages of skilled and specialised workforce in some clusters and a need for manpower training on the latest equipment and technology. There is need for high quality training centres. Companies should also be incentivised to set up R&D and innovation centres in SEZs. There should be scope for collaborations and foreign partnerships. Support from the government in brand development and marketing India as a gems and jewellery hub will be beneficial.

4.1.6 Labour and Employment in SEZs

Since one of the concerns related to allowing reverse job work was the shortage of skilled workforce in this sector, the survey covered questions on manpower availability and employment, skill and training. Over 50 per cent of the full-time employees in the surveyed SEZ units were permanent, the remaining full-time production workers being non-production workers (e.g., managers, administration, salesperson, etc.). The majority of employees were skilled production workers in 2020-21. In terms of permanent female workers employed full-time, the number was higher in non-production than in production, in 2020-21.

4.1.6.1 Seasonal/Temporary Workers

The survey revealed that from 2019-20 to 2020-21, the number of seasonal/temporary workers increased in the SEZ units, with their employment period varying between two and six months. Most of the surveyed units hired seasonal workers during Q2 (42 per cent), and Q3 (37 per cent). This matches with seasonality in demand, and the quarters when SEZs engage in job work (see section 4.1.6). Out of the units which did hire seasonal/temporary workers, 60 per cent hired from outside the SEZ but within the same state. The remaining 40 per cent hired from other units in the SEZ.

4.1.6.2 Education and Experience of Workers

While most (58 per cent) of the units said workers

do not need any form of formal education, 50 per cent preferred workers with some school education, and 33 per cent preferred class 10th pass workers, and another 33 per cent said they hire people with industry experience. Given that there is a preference for industry experience and basic education, training and skill development is needed.

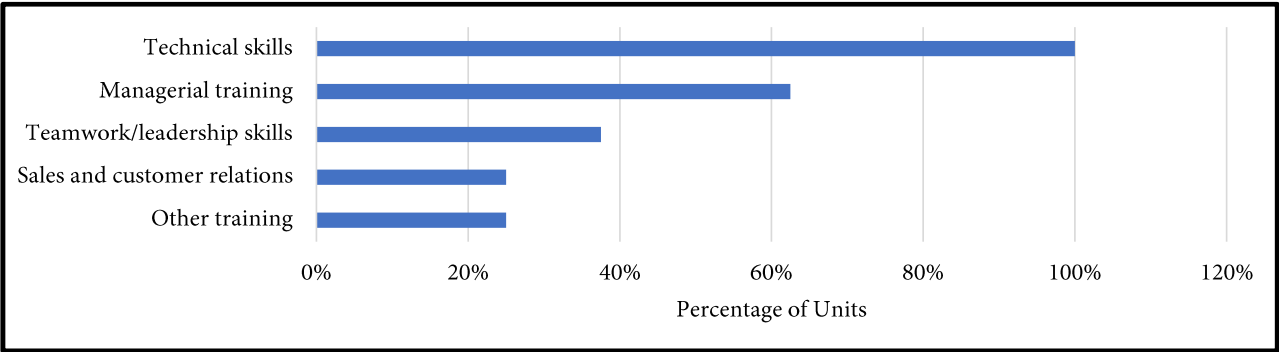
4.1.6.3 Training Programmes

Over the last two years, 2019-20 to 2020-21, only 57 per cent of the SEZ units surveyed conducted formal training programmes for their permanent, full-time

employees. These units belonged to either SEEPZ, Maharashtra, or Manikanchan SEZ, West Bengal. The areas of focus of the training programmes are shown in Figure 4.7. Overall, there is need for more technical training for skill development and for mitigating labour shortages.

All training programmes were conducted by the company themselves with in-house training sessions. Only 25 per cent were conducted by a private provider and 13 per cent by a government agency, showing limited government involvement in skill development.

Figure 4.7: Focus of Training Programmes



Source: Pilot Survey

Note: Other Training includes programmes such as awareness programs on human rights, HIV-AIDS, etc.

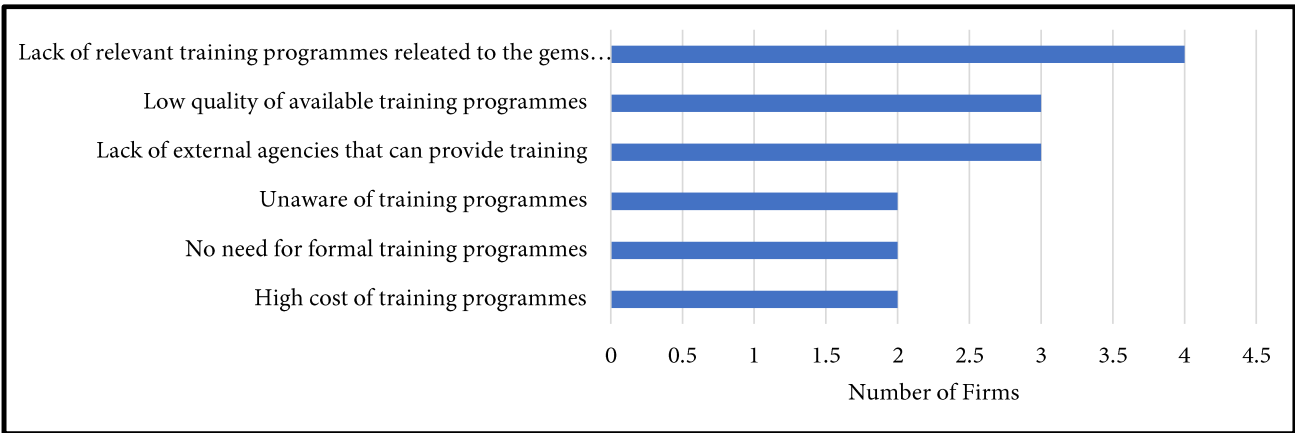
4.1.6.4 Reasons for Lack of Training Programmes

The most common reason cited for the lack of a trained workforce is the lack of a relevant training programme. Other top reasons are mentioned in

Figure 4.8.

Having discussed the perspective of SEZ units, subsection 4.2 analyses the perspective of DTA retailers.

Figure 4.8: Reasons for Lack of Training Programmes



Source: Pilot Survey

4.2 Perception of the Retailers in DTA

The pilot survey covered 19 retailer units in the DTA, covering the states of West Bengal and Uttar Pradesh.

The most common jewellery type sold by DTA retail units is gold jewellery (both plain and studded), at 95 per cent, followed by silver (plain silver) at 63 per cent and, coloured gemstone and diamond jewellery

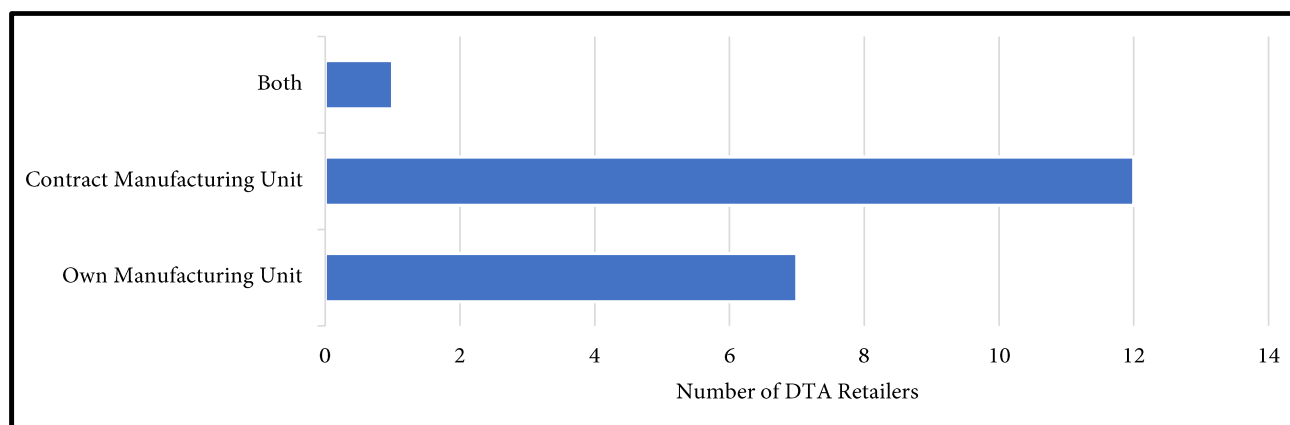
at 32 per cent and 26 per cent respectively.

All surveyed units were engaged in manufacturing and retailing. Only 16 per cent of the units were engaged in wholesaling and exporting, with just 11 per cent importing jewellery.

4.2.1 Business Operations

Sixty-three per cent of the retail units outsource their manufacturing to a contract manufacturer (see Figure 4.9). Of the 37 per cent retailers who own a manufacturing unit, only 14 per cent are located in a DTA.

Figure 4.9: Type of Manufacturing Unit



Source: Pilot Survey of DTA Retailers

4.2.2 Importing Jewellery

Eighty-nine per cent of the surveyed DTA retailers said that they had not imported any jewellery in the last five years. The remaining 11 per cent said that they imported was less than 1 per cent of the total products in their outlet. These included finished products of plain or studded gold jewellery from Dubai (UAE) or Bangkok (Thailand) respectively. Better designs in these countries were the reason for import.

4.2.2.1 Domestic Demand for Imported Jewellery

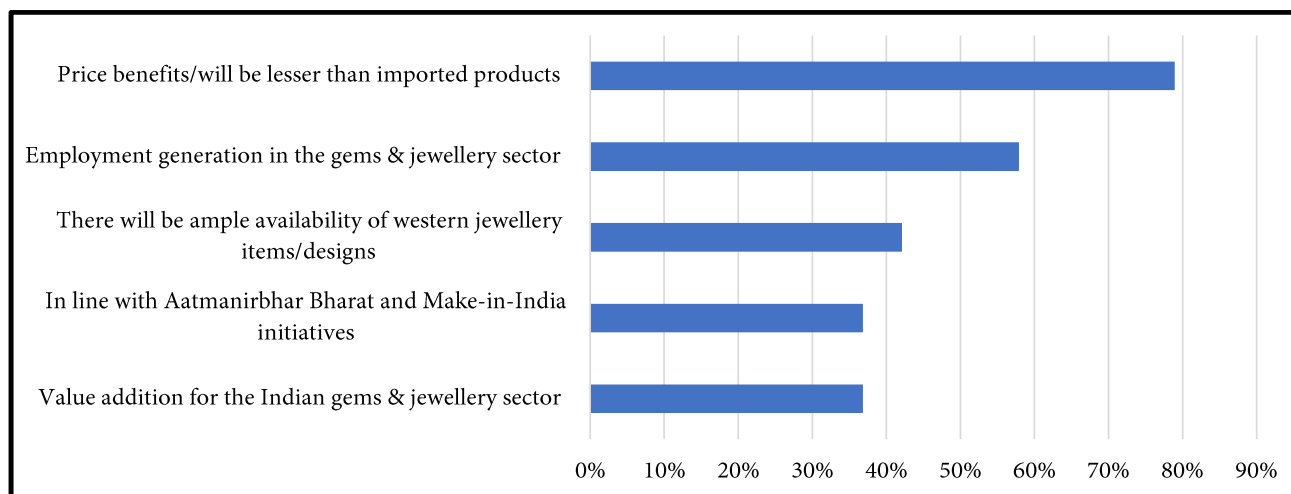
Eight out of the 19 surveyed retailers (42 per cent) said that there is no and/or limited domestic demand for imported jewellery in India compared to six (32 per cent) retailers who said there is demand and that the demand for imported jewellery is increasing. They further said that the demand for imported

products from countries like Hong Kong and China like 14 carat light weight gold jewellery, etc., can be replaced by similar products manufactured in Indian SEZs. There is a growing demand for gold jewellery, in particular of the type produced in Indian SEZs, in the DTA and this is also reflected by the data on DTA sales from SEZs.

4.2.3 Sourcing from Indian SEZs

Retailers said there is a demand in the market for jewellery produced in the SEZs. The products from SEZs, according to 58 per cent retailers, have better finishing and more western designs. Eighty-nine per cent of retailers agreed/strongly agreed that Indian SEZs should be allowed to sell their products to domestic retailers, subject to payment of duty. The top five reasons cited by the retailers are given in Figure 4.10.

Figure 4.10: Top Five Reasons for Retailers to Source from SEZ Manufactures



Source: Pilot Survey

Note: This was a multiple-choice question.

Around 11 per cent of the retailers who were not keen on reverse job work or sourcing from Indian SEZs mentioned reasons such as the adverse impact/loss of business for units in DTA, time taken to source products from SEZ, and low customer demand for the type of jewellery produced in SEZs. Overall, a large majority of domestic retailers felt that sourcing from the SEZs will be beneficial.

4.2.4 Indian Market for Gems and Jewellery

To understand the Indian market and future growth trends, it is important to know the consumer profile, consumer preferences and their purchase pattern. The key findings from the pilot survey, in this context, are discussed below.

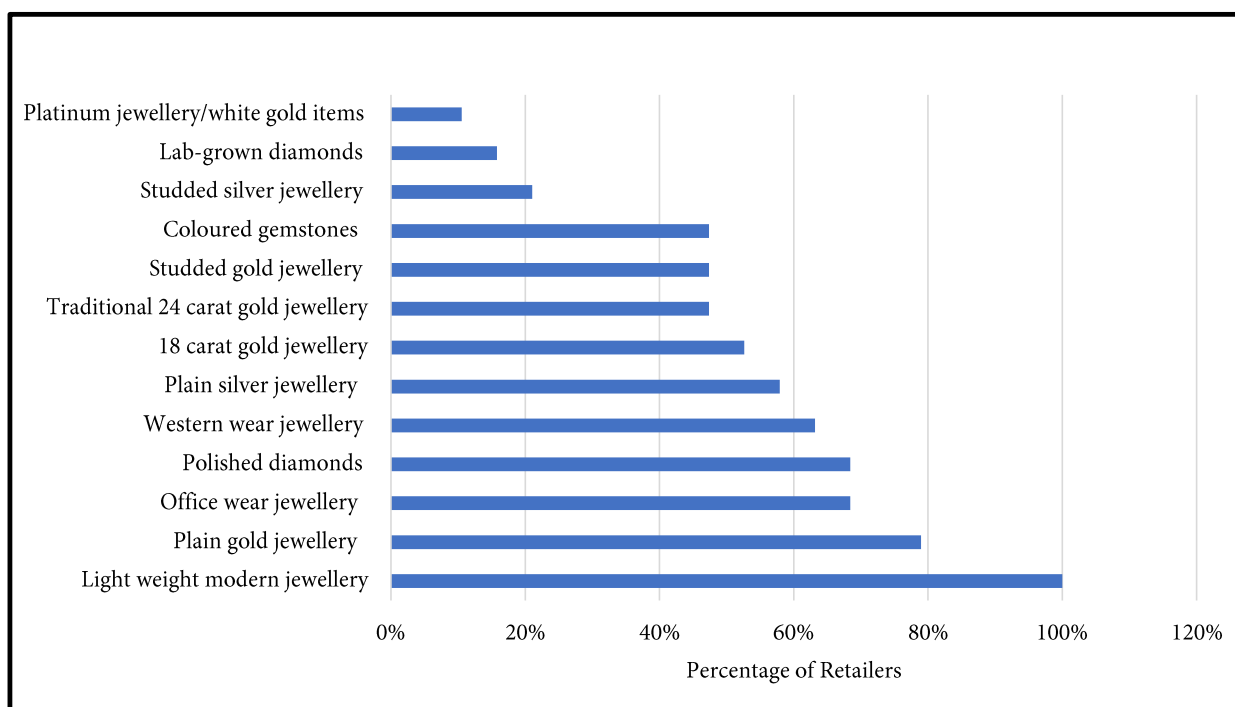
4.2.4.1 Consumer Profile

Most of the domestic consumers were from the upper-middle class (59 per cent) and lower-middle class (33 per cent). Age-wise, 79 per cent of the retailers said that their consumers are between 40 and 50 years of age, followed by 32 per cent that catered to the age group of 30-40 years, and 26 per cent catering to consumers above 50 years.

4.2.4.2 Consumer Product Preferences

A majority of the retailers surveyed said that the demand for jewellery in the domestic market has increased in the last five years. All surveyed retailers agreed that domestic demand for light-weight modern jewellery has increased. Seventy-nine per cent said the demand for plain gold jewellery increased, and 68 per cent said demand for office-wear and polished diamond jewellery increased.

Figure 4.11: Increase in Consumer Demand in Domestic Market from 2016 to 2020



Source: Pilot Survey of Retailer Units

Note: This was a multiple-choice question.

In terms of decrease in demand, 53 per cent respondent retailers said that demand for lab-grown diamonds decreased while 47 per cent said that demand for studded silver jewellery decreased. The domestic demand for platinum jewellery has remained constant according to 47 per cent retailers. It is important to note here that gold jewellery was the most common jewellery type sold by the surveyed retailers.

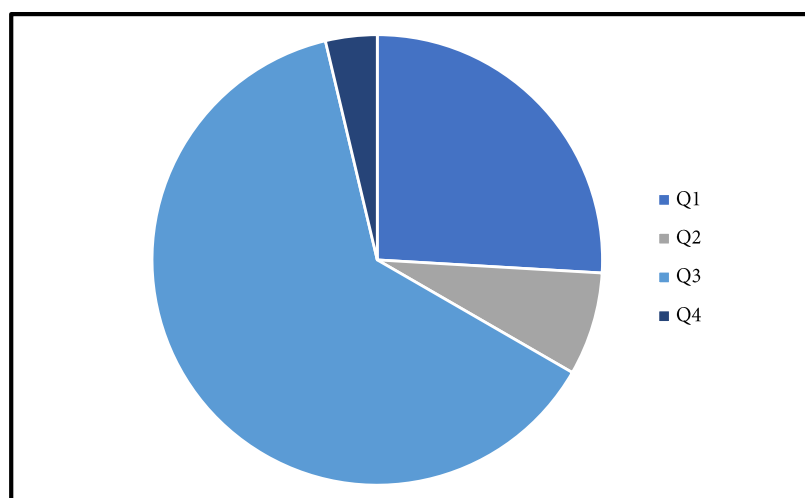
In terms of imported jewellery, 37 per cent of the retailers said that domestic demand has remained constant from 2016 to 2020, while 26 per cent said

that the demand has declined.

4.2.4.3 Purchase Pattern – Seasonality

According to 89 per cent of the DTA retailers, the peak demand season in the domestic market is during Q3 (October to December), (see Figure 4.12). The other months of major purchases are in Q1 (April to June), according to 37 per cent retailers. The period of the peak demand season in the domestic market, thus coincides with key festivals in India, followed by the wedding season.

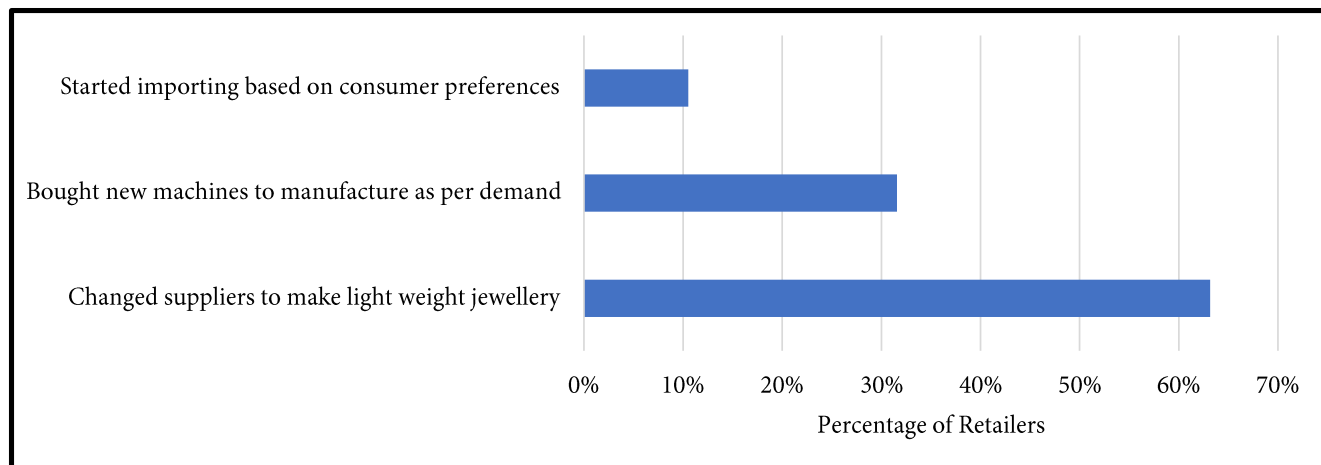
Figure 4.12: Demand Seasonality in Domestic Market



Source: Pilot Survey

Note: This was a multiple-choice question. FY Quarters are followed.

Figure 4.13: Measures to Cater to Changes in Consumer Demand



Source: Pilot Survey

Note: This was a multiple-choice question.

4.2.4.4 What Retailers are doing to Cater to Changing Demand

As consumer demand and preferences change, the DTA retailers have also taken certain measures to address the changes; these are summarised in Figure 4.13 below. As the demand for light weight modern jewellery increases, the most common measure among the surveyed retailers has been to change their suppliers.

4.2.4.5 Labour and Employment in DTA

Some DTA manufacturers are also retailers. According to 53 per cent of the retailers, the slow growth in the domestic market during the COVID-19 pandemic related lockdown was accompanied by a decrease in the demand for labour. Thirty-seven per cent said that the demand will increase while 11 per cent said the demand for labour in the next five years will remain the same. However, if domestic demand for jewellery increases, 53 per cent retailers said there would be a shortage of labour in manufacturing, leading to an increase in salary/wages. Thus, there are some concerns related to labour shortages in this sector. According to all the surveyed retailers, labour shortage can be mitigated through training and skill development.

4.3 Future Growth and Performance of Industry and Domestic Market

Units in both the SEZ and DTA expect positive growth in the gems and jewellery industry. According to the SEZ and DTA units, both the domestic and export market will experience growth over the next five years. Among the SEZ units, 67 per cent said they

expect cumulative growth of more than 10 per cent in the domestic and export markets in the next five years. Fifty-eight per cent of DTA retailers foresee a 1 to 5 per cent cumulative growth in the domestic market for gems and jewellery in the next 5 years. Twenty-one per cent think growth in the domestic market will be less than 1 per cent, while 16 per cent believe the growth will be between 6 and 10 per cent.

5. Barriers to Gems and Jewellery Exports from SEZs

This section discusses the barriers faced by SEZ units in India's gems and jewellery sector. Barriers can be linked to external issues such as global market related uncertainties (for example, Russia-Ukraine war, rising inflation, slowdown in importing countries), tough competition, supply chain disruption, and seasonality in export demand. It can also be linked to domestic market issues like withdrawal of fiscal support, limited non-fiscal benefits, uncertainty about the future of the SEZ policy and some concerns related to the DESH Bill (2022). The core barriers identified by the gems and jewellery units are listed below.

5.1 Policy Uncertainty and Gaps in the DESH Bill (2022)

Units located in both SEZs and DTA said that there is a lot of ambiguity and uncertainty around the evolving new SEZ policy, i.e., the DESH Bill (2022). The DESH Bill (2022) was expected to be tabled in the monsoon session of Parliament. It has been postponed and is now likely to be discussed in the winter session. There is speculation about the kind of fiscal incentives given under this bill and how it compares

with the incentives applicable in the DTA. There is lack of clarity on the criterion for giving incentives and in the performance monitoring mechanism. More precisely, the ambiguity surrounding the new SEZ policy/DESH Bill (2022) and the type of fiscal incentives it will provide to the units, the conditions that are required to be met to get the incentives, and the terms and conditions applicable to sell to the DTA are some of the areas where both the SEZ and DTA units need more clarity. At the same time, the SEZ units have welcomed the broad intention of the government to delink export conditions for giving incentives and allowing reverse job work. DTA units pointed out that the sole objective of a firm in deciding to locate in an SEZ or a DTA is the market they want to focus on – the international or the domestic market. There is a fear that units may locate in the development hubs to get duty free imports to cater to the domestic market. While this can lead to domestic value addition, it can take away business from DTA units. Some units raised concerns that there can be relocation of units from DTA to development hubs just to avail the fiscal and non-fiscal benefits.

5.2 Seasonality of Exports

Due to the seasonality in demand in the export market, labour and equipment capacity in SEZs are not optimally utilised. Since exports from SEZs is completely dependent on cyclical global demand, this seasonality hampers SEZs prospects, particularly during times of uncertainty emerging from global shocks such as the COVID-19 pandemic, the Russia-Ukraine war, etc.

5.3 Strong Competition from Other Countries

SEZ units in India are facing increasing competition from gems and jewellery units in other countries like China and Turkey, in terms of price, quality and designs. Turkey is gradually taking over in the light weight gold jewellery segment. The competition is due to a mix of technology and innovation, better utilisation of existing resources and the ability to offer competitive prices, lower cost of production, and policies such as allowing reverse job work that allow efficient utilisation of labour and equipment. Reverse job work in such countries also led to scale expansion.

5.4 Limited Non-Fiscal Incentives

In general, Indian SEZs have fewer non-fiscal incentives compared to their counterparts in many developing countries. As SEZs are not allowed to

sell in the domestic market, their skilled permanent workforce and state-of-art-equipment and facilities remain underutilised during periods of low export demand. This increases the cost of operation and makes Indian units less competitive compared to units from countries like China and Turkey, which have allowed their SEZs to cater to the foreign as well as domestic markets, thus mitigating the issues related to seasonality in demand, if any. Besides, many global SEZs are provided incentives like fast-track patenting, common user facilities, single-window fast track clearances, etc., which Indian SEZ units do not get. Logistics cost is much higher in India with many restrictions on carrying gems and jewellery through the express cargo mode. More recently, in the Union Budget 2022-23, the government announced that measures will be taken to ease the restriction on exports gems and jewellery through the express delivery mode.

5.5 Withdrawal of Fiscal Incentives from SEZ Units

The withdrawal of fiscal incentives granted to SEZs and uncertainty about the future SEZ policy led to the shutdown of many gems and jewellery units in the SEZs. Both the financial as well as production costs rose when financial benefits were withdrawn from the SEZs. The SEZs are given the benefit of zero duty imports but with the signing of trade agreements, imports from FTA partner countries can also be at zero duty. At the same time, units in Indian SEZs face high input costs linked to high logistics costs and cost of inputs like electricity. Fiscal incentives helped to cushion against the high input costs. At present, units in SEZs are at a disadvantage from units in countries with whom India has zero import duties and from whom India sources raw materials and final products for the domestic market. The SEZ units do not know what kind of incentives will be applicable to units in the DTA through the foreign trade policy and fear that DTA units may get fiscal incentives that they would not.

5.6 Limited Investment in Research and Development and Low FDI Inflows

Only a few units in the gems and jewellery SEZs invest in R&D, innovation, technological advancement, and training and skilling of the workforce. This is an area of concern as units from competing countries like Turkey are investing in these areas.

FDI inflows also remains low or nil for a majority of the units in SEZs. One of the reasons for low FDI

in Indian SEZs is the lack of investor protection agreements, unlike countries like Vietnam that have laws such as Vietnam's 2005 Investment Law which make provisions for protection against expropriation and the mechanisms for cooperation.

5.7 Limited Government-led Skill Development and Labour Training Programmes

The survey participants pointed towards skill shortages. The government's role in upskilling of the technical workforce is limited and there is limited partnership with the private sector in this area.

5.8 Low Ease of Doing Business

The SEZs suffer from certain problems that undermine the ease of doing business. Government SEZs can only lease the land for a period of 15 to 30 years making it difficult for units in such SEZs to avail bank loans against their factories.³² However, private SEZs and state SEZs can have the lease for a period of 99 years, thus enabling them to avail bank loans/limits against their factories. The existence of redundant procedures and duplication of paperwork, i.e., requiring both online and physical filing, emerges as a strong barrier to SEZ units. The SEZ online system is not integrated with ICEGATE, leading to inefficiencies.³³ Entry and exit norms are rigid under the present SEZ policy. Some SEZ units pointed out that the exit process in SEZs is cumbersome as it involves approvals from multiple authorities, both at the central and state levels. The exit clause requires exiting units to pay a penalty in case they were not making net foreign exchange earnings. The procedure of entry and exit in the current SEZ policy is lengthy as compared to the process in other countries such as the Philippines and Indonesia. According to Rule 74 of the SEZ Act, exiting units not following the proper exit order will be deemed to be an SEZ unit till the date of final exit.³⁴ This prevents the developer from allotting the space to new units.

5.9 Impact of COVID-19 Pandemic

The gems and jewellery sector was no exception to the disruptions caused in the wake of the COVID-19 pandemic. The pandemic related lockdown and fall in consumer demand was observed as a major barrier

to SEZ exports. As the gems and jewellery industry operates in the processing stage of the value chain, the dependence on imported raw material, disruptions in raw material availability, and the disruption in the logistics and transport sectors hindered exports of gems and jewellery. Export demand showed a sudden increase once the pandemic related lockdown eased. Around 79 per cent of the retailers observed a decline in domestic demand for jewellery during the pandemic. However, two DTA retailers observed an increase in domestic demand. Plain gold jewellery comprises more than 80 per cent of their jewellery portfolio. A larger survey is needed to understand the impact of the pandemic on domestic demand.

5.10 Other Issues

High GST rates, low demand and the increasing price of gold were a few of the key issues prior to the pandemic. These issues were again highlighted in the post-pandemic period. Some respondents also said that they faced labour shortage and a cumbersome process of tax filing and receiving a Hallmark Unique Identification (HUID) number.

6. Policy Recommendations and Way Forward

India is among the world's leading processing hubs and exporters of gems and jewellery. Several gems and jewellery units, in the past, had located in Indian SEZs for three key reasons: (a) zero import duty in a sector that is import dependent (b) better infrastructure and ease of doing business in SEZs and (b) the fiscal and non-fiscal benefits provided to units in SEZs. Exports from SEZs was around 30 per cent of the sector's total exports in 2019-2020. However, after India lost the case to the USA on export-linked subsidies, fiscal subsidies had to be withdrawn and many gems and jewellery units pulled out of the SEZs. Exports from SEZs also declined to 17.7 per cent of total export in 2021-22. At the same time, Indian exporters in this sector face tough competition from countries like Turkey in products like light weight gold jewellery in export markets like the USA and the EU. A combination of factors, ranging from a need to upgrade technology, skills and processes to high logistics costs and lack of incentives vis-à-vis those offered by competing countries such as Turkey, has

32 Source: https://www.epces.in/issues_of_eou_sez.php (last accessed August 11, 2022)

33 Source: EPCES Newsletter April-June 2022 <https://www.epces.in/uploads/EPCES-Newsletter-April-June-2022-edition.pdf> (last accessed August 08, 2022)

34 Source: https://www.epces.in/issues_of_eou_sez.php (last accessed August 11, 2022)

resulted in tough competition for Indian units in export markets. They face the risk of losing market share, which is evident from the current export trends in this sector. Given that India has the potential of developing as a gems and jewellery processing hub, promoting exports from this sector has been a priority for the government. The government is in the process of re-drafting its SEZ policy and has come up with the DESH Bill (2022).

Given the issues facing the sector, ranging from policy uncertainty to seasonality of exports and supply chain disruption to limited non-financial incentives, limited FDI inflows, and limited investment in R&D, innovation and training, this section presents some policy suggestions based on the survey, stakeholders' consultations and secondary analysis. These are mostly related to aligning the SEZ policy with the broad objective of export promotion and developing India as an export hub.

6.1 Need for More Data-Driven Policy Making

The lack of longitudinal data on product wise exports and imports in SEZs makes it difficult to identify the extent of value addition from the gems and jewellery sector. Without an estimate of the value addition in the gems and jewellery SEZs, it is very difficult to design a policy on job work and reverse job work. Given the dearth of data, it is also difficult to make an impact assessment of the benefits to SEZs in India. Thus, there is a strong need for data collection on domestic sales, export sales, imports, etc., from the gems and jewellery SEZs in India.

6.2 Need for Robust Policy and Export Strategy

There is a need for a robust trade policy and export strategy for this sector, with a focus on SEZ policy and enhancing exports from SEZs. The survey found that units in SEZs need both fiscal and non-fiscal incentives that will help reduce costs and improve their productivity, efficiency and global competitiveness; they also strongly advocated fiscal incentives and designing WTO smart incentives. At the same time, units in Indian SEZs do not get many non-fiscal incentives given to units in competing countries. These non-fiscal incentives include allowing reverse job work or having high quality common user facilities or innovation centre in the zones. These may be given to the SEZ units. Some experts talked about incentivising manufacturing services and allowing SEZs to offer such services

to units in the DTA. There is need for a detailed study on non-fiscal incentives given by competing countries, which can help the Indian government design a comprehensive non-fiscal incentive package to facilitate exports and develop India as a gems and jewellery processing hub. The study may also cover whether other countries allow manufacturing services from their SEZs to DTA and how countries like Turkey, Italy, Vietnam and Thailand have been building brands, marketing their products, and exploring new markets.

While the DESH Bill (2022) is likely to introduce non-fiscal incentives such as reverse job work for SEZ units and enhance the ease of entry and exit for investors, the policy needs to have clarity on the kind of WTO compliant fiscal incentives that can be provided to units in development hubs. While gems and jewellery units participating in the survey have welcomed the DESH Bill (2022), they pointed out that to give incentives, there is need for more clarity on issues such as the following:

- Performance criteria and their measurement against which the fiscal incentives may be given to the units: Several performance indicators mentioned in the draft DESH Bill (2022) such as integration with the global supply and value chains are difficult to measure. Thus, there is need for a robust SEZ policy that clearly mentions quantifiable performance indicators and eliminates vague and difficult to measure performance indicators.
- Rules-of-origin: Some units felt that 40 per cent rules-of-origin or value addition in an SEZ (where the raw materials are imported) for sale to the DTA may be difficult to comply with as labour, equipment and other costs may not be 40 per cent of the final price of the jewellery.
- Clarity in the incentives that will be provided to SEZ units to decide on location of units: Firms will find it difficult to decide whether to locate in an SEZ or in the DTA unless they know which incentives are given to development hubs and compare it with incentives given to units located outside the hub. They would also like to know how incentives in SEZs compare to incentives under the foreign trade policy, what the total incentive package is likely to be and how many units will be eligible.

In any country, SEZ policy is a part of the overall trade policy. In India, too, the DESH Bill (2022),

has to fit into the overall trade policy and there is need for alignment across different ministries and departments of the government – for example, between the Department of Commerce, the Ministry of Commerce and Industry and the Ministry of Finance. State governments also have to give their buy-in for the DESH Bill (2022) to ensure policy certainty. The SEZ policy in the past had faced severe backlash from certain state governments. Export zones are globally created to push exports. Hence, most of the output of units in such zones should be exported. What proportion can be sold in the DTA needs to be clearly specified.

6.3 Need for Definitional Clarity

The term ‘job work’ is referred to in the SEZ Rules, including amendments up to July 2010.³⁵ However, there is no specific definition of job work. Similarly, there is no official definition of reverse job work. The DESH Bill, 2022, is expected to allow reverse job work, i.e., permitting SEZ units in a development hub to render or receive manufacturing services to or from a unit in the DTA, subject to conditions as may be prescribed by the central government. However, it is necessary to clearly define the manufacturing services and align the definition with international definition like the UNSD-CPC version 2.1 so that fiscal subsidies, if any given, can be aligned with WTO requirements. The UNSD-CPC version 2.1 Code 886 for basic metal manufacturing services includes outsourcing portion of a manufacturing process or completely outsourced manufacturing process. At present, the DESH Bill, 2022, is not clear on what kind of manufacturing services may be included if reverse job work is permitted. Thus, it is important that the DESH Bill lays out a glossary of terms on job work, reverse job work, manufacturing services, etc., which is currently missing.

6.4 A Careful and Research-Based Approach to Designing Incentives

The SEZ units want the government to offer fiscal incentives to make them more competitive and reduce operating costs. They felt that the Remission of Duties and Taxes on Exported Products (RoDTEP) scheme should be extended to SEZs to boost exports from the sector, as has been done in the case of EOUs. Currently, the SEZ policy is unclear on the applicability of RoDTEP and the production linked

incentives (PLI) schemes to SEZ units. However, there are two views on applicability of the RoDTEP to units in SEZs – one, that SEZs do not need the RoDTEP since imports are duty free and the other that SEZs units do import from the DTA, which can attract high import duties, and, therefore, they need the RoDTEP. However, there is need for a detailed study on the costs and benefits of extending the RoDTEP scheme to units in SEZs and the remission rates. To ensure level playing field, SEZs supplies to the DTA may be allowed on duty foregone principle, and there is a need to study the amount of RoDTEP applicable on SEZ units in gems and jewellery sector. Refund of duties on inputs for the supplies made to DTA may follow the case of EOUs and Manufacturing and Other operation in Warehouse Regulation (MOOWR) scheme to promote manufacturing and value addition in SEZs (EPCES, 2021).

The survey participants mentioned that the DESH Bill (2022) and subsequent rules need to clearly mention what kind of WTO compliant fiscal incentives it will provide to SEZ units. Further, there is need to understand the budgetary allocations needed to provide such incentives for units located in development hubs and what the terms and conditions for claiming the incentives will be. In this context, there is hardly any study on what kind of fiscal incentives are claimed by gems and jewellery units located in the SEZs vis-à-vis those located in the DTA. The incentives may vary by states. There is also a need to examine what kind of fiscal incentives are offered by competing countries. Similarly, it is important to understand the need for and the kind of non-fiscal incentives offered by competing countries. More importantly, it is necessary to estimate the growth in exports as a result of the incentives.

Focusing on WTO compliant/smart subsidies, the removal of the NFE criteria may not make SEZ exports WTO compatible. With the removal of the NFE criteria, the subsidies given to SEZs will be taken as actionable rather than prohibited under the WTO ASCM. In that case, the importing country needs to establish injury to their domestic industry before applying trade remedial measures like countervailing duties (CVDs). Therefore, any subsidy given to our SEZs will continue to be closely monitored by our trading partners. However, if subsidies can be linked to services, they are less likely to face trade remedial measures. With increasing servicification of

35 Refer http://sezindia.nic.in/upload/uploadfiles/files/14_SEZ_Rules_July_2010.pdf (last accessed November 07, 2022)

manufacturing, subsidies can be given to the services used in manufacturing (like worker training, or in logistics services). Since there is no discipline on subsidies in services, these can be WTO complaint. Also, incentives can be linked to R&D and be given for software implementation. There is need to support trade mark and design protection in this sector and subsidies can be linked to such activities. There is also need to examine the scope for giving incentives to micro, small and medium enterprises (MSME), marketing and brand building. A number of countries carefully design their incentives to support R&D and innovation, while others focus on skilling and some focus on improving the competitiveness of MSMEs. These global best practices may be examined. It is important to examine both fiscal and non-fiscal incentives. Non-fiscal incentives may also include flexibility regarding labour laws, environmental laws, easier trade facilitation, fast track approvals, easier documentation, etc. However, they can have both positive and negative impacts if they are not carefully designed. For example, labour law flexibility can lead to lower wages and lower protection of workers' rights and environment regulation flexibility can lead to the growth of polluting industries. The incentives should be designed in a way that supports sustainable business practices. Therefore, the DESH Bill needs to carefully design non-fiscal incentives, prioritise them based on the needs of SEZ units and use them to guide SEZ units to upgrade and export. For example, sustainable business practices can be incentivised. In this context, there is need for a detailed study on the type of incentives given by other countries and how India can adopt global best practices in designing fiscal and non-fiscal incentives. While designing incentives, it is also important to look at supporting units located in the DTA that export. Incentives should not lead to relocation of units between SEZs and DTA or vice versa.

6.5 Remove Restrictions on Imports of Raw Materials/Intermediate Products

The restrictions on advance payments for import of gold and silver and its articles must be removed. This will be beneficial for units to run with low working capital. The government must adopt easier custom processes for SEZs that allow imports through courier/express mode with similar terms and conditions as in the case of general cargo. For sales to the DTA using imported raw materials, domestic value addition has to be calculated for each product category and this information has to be provided to the Department of Commerce for designing policy on rules-of-origin for sales to the DTA.

6.6 Need for Government Support in Training and Research & Development

Of late, countries such as Turkey have emerged as top exporters of light weight gold jewellery through skill and technology upgradation, innovation and faster delivery. The survey found that both SEZs units and DTA manufacturing units in the gems and jewellery sector require skilled manpower to meet the demands of the global consumer. Skilling will help address labour shortages if job work and reverse job work are allowed. To match the skills of the Indian workforce with emerging competitors in various segments, the government must raise upskilling efforts by sponsoring and supporting various capacity building and training programmes, customised to the needs of this sector. In this regard, training institutes should work closely with industry to identify skill requirements and design training modules. The SEZs or development hubs should have common facilities for training, common user R&D and innovation centres, and other common user facilities as is needed by the industry.

6.7 Improving Ease of Doing Business

Some SEZ units in the survey highlighted the prevalence of cumbersome exit rules that undermine the overall ease of doing business in the SEZs. Current SEZ rules also makes it difficult for units to access finance from banks and other financial institutions. As access to finance is crucial for the gems and jewellery sector to thrive, the focus should be on making the process smooth and easy, enabling SEZs to avail loans at favourable terms; the norms should be on par with that for other sectors such as roads, railways, airports, etc. The SEZ units surveyed also recognised the need for government support in areas such as lowering GST rates to help lower overall production costs, easing the HUID paperwork, lowering input costs and fixing the charges for making hallmarked ornaments. Also, there is need for time bound clearances/approvals. In this context, India can learn from the experiences of the foreign trade zones in the middle-eastern countries like the UAE and Qatar, which have autonomous legal frameworks and a high level of customer orientation, that enables them to attract units. In India too, there is need for the SEZs to have an autonomous legal framework and customer orientation to attract units along with improvement in overall ease of doing business. There is a need for fast-tracking the dispute resolution mechanism in Indian SEZs.

Conclusion

India is aiming to increase its share in world trade to 10 per cent by 2047, with a vision to brand India as a supplier of high-value and high-growth products. One of the goals for promotion of international trade is to support the setting up of SEZs as an extension of 'Atmanirbhar Bharat' or linking India to the global value chain and improving the logistics infrastructure. Globally, SEZs have been leveraged to promote exports, induce investment and generate employment. India can also leverage SEZs to achieve the target of USD1 trillion exports of goods and services each by 2030.

The gems and jewellery sector is one of the core exporting sectors, located in Indian SEZs. This report found that India has the potential to develop as a global gems and jewellery processing hub, with SEZs playing a key role in facilitating and enhancing exports. It is expected that the recommendation presented in this report will help design a robust SEZ policy, which will help improve the export competitiveness of the gems and jewellery sector. At the same time, the industry needs to modernise, invest in R&D and innovation, and upgrade skills. There is scope for collaboration between the business and government in areas such as capability building and training and brand building. In this area,

India can learn from countries such as Vietnam and UAE to provide an investor friendly regime, market strengths of its SEZs, and to address the misperceptions and prejudices and some concerns (like promoting unequal development) related to the SEZs. Non-fiscal incentives like reverse job work can help address some of the issues faced by units in SEZs including seasonality of demand, but such incentives need to take into account three factors: (a) they should not lead to relocation of firms from the DTA simply to claim the incentives (b) there should not be an adverse impact on revenue and employment in the DTA and (c) it should be aligned with the overall objective of creating export zones, which is to promote exports. As many developed countries are entering into a possible recessionary phase that can adversely impact our exports, the Indian government must keep open the possibilities of SEZs catering to the domestic market. It is, however, important to see that such policies do not put the DTA manufacturers at a disadvantage; they should also not be a drain on government finances and should benefit the country. This requires the Department of Commerce, Ministry of Commerce and Industry, Government of India, to do a thorough study on the costs and benefits of an SEZ or the future Development Enterprises and Services Hub. The cost and benefits of SEZs can be shown through a data-driven impact analysis of SEZs.

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