The effect of tax incentives on investment among Export Processing Firms (EPZs) in Kenya

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Tax incentives may have the potential of encouraging investment in a sector where they are offered. The purpose of this study was to establish the effect of tax incentives in Export Processing Zones firms (EPZs) on business investment in Kenya. The study sought to achieve two specific objectives: to establish the various types of tax incentives offered to EPZ firms on their business investment in Kenya and to determine the effect of tax incentives on investment. The study adopted a descriptive design. The population for the study included all 104 Export Processing Zones firms in Kenya. Purposeful sampling was adopted in arriving at a sample of 65 firms situated in the Nairobi Metropolitan (Nairobi and Kajiado Districts). Primary data was collected through value added questionnaires and secondary data was obtained from published company records. A pilot study was conducted by the researcher and the results were analyzed for validity and reliability of the research instruments. The Pearson's Product Moment Correlation Co-efficient was used where it was found to be 0.87 and indication that the instruments were consistent. Descriptive statistical techniques multivariate regressions were utilized in data analysis while inferential analysis was used to reach conclusions. The findings from the study reveal that investments in EPZ firms increase with increase in sales, profit as well as tax incentives. However, given the significance level of 0.39, the influence of tax incentives on investments in EPZ is insignificant. The study recommends that that the Government of Kenya should consider other incentives apart from the tax particularly on those that will enhance more sales since this is the most significant factor attracting investment in EPZ especially foreign direct investment.

Key words: Tax incentives, investment, Export processing zones (EPZs).

INTRODUCTION

The contemporary world is characterized with intergovernmental competition for the sole purpose of attracting multinational companies and this has made fiscal incentives to become a global phenomenon. Poor African countries rely on tax holidays and import duty exemptions, while industrial western European countries allow investment allowances or accelerated depreciation. This trend seems to have grown considerably since the early 1990s as evidenced by the number of high profile foreign investments, such as Toyota in Northern France or Mercedes-Benz A. G in the U.S state of Alabama. These have generated considerable debate about whether governments have offered unreasonably large incentives to entice those firms to invest in their area. The debate about the effectiveness of tax incentives is hardly new and has accumulated a long history (Harris, 1993). Export Processing Zones (EPZs) were amongst the first initiatives pioneered in developing countries with the aim of promoting export growth and diversification. The first generation EPZs initiated mainly by what were to become the Newly industrialised countries (NICs) of East Asia, took the form of providing investors with remissions on import duties for inputs and raw materials, with enhanced or improved infrastructure (usually within a geographically restricted physical area) and with speeded-up customs clearance procedures. These schemes generated some substantial initial impacts, leading to their adoption by a large majority of developing
countries today (Din, 1994).

The Kenyan government pursued an export – led growth strategy (Republic of Kenya, 2003). This was a major shift from its previously favoured import-substitution policies. In order to stimulate exports, the government implemented export promotion incentives such as the EPZ and manufacturing-under-bond (MUB) schemes. The introduction of these forms of exports compensation, especially with the advent of liberalization and globalization, was intended to move the Kenyan economy towards a more open regime, with increased market access for her products and services in the global market (Republic of Kenya, 2003).

Several studies have been conducted on Export Processing Zones in Kenya. Mutunga (2006) studied the response of trade unions to challenges posed by conditions of work at the EPZs in Kenya. Hapisu (2003) addressed the relationship between strategic planning and competitive advantage in the EPZs in Kenya. Chabari (2000) studied the role of EPZs in Kenya. Therefore this clearly indicates that no study has been conducted on the impact of tax incentives on business investment of EPZs in Kenya.

One of the findings of the literature is that the impact of tax rates on investment decisions is generally higher on export – oriented companies such as EPZs, than those seeking the domestic market or location-specific advantages. In these EPZs firms, managers have responded more favourably to tax incentives. This finding is not really surprising because export-oriented firms such as garments manufacturers are operating in highly competitive markets with very slim margins. Moreover, these EPZs firms are often highly mobile, and more likely to compare taxes across alternative locations. Hence taxes can be an important part of their cost structure, and the firms can easily move to take advantage of more favourable tax regimes.

According to Chabari (2000), many countries especially in the industrial world allows fast write –offs for investment expenditures, either all investments, or those they especially want to induce through tax allowances or credit. He identifies that investment tax allowances have distinctive advantages. The incentive is correctly targeted at the desired activity since an EPZ company receives the benefit of lower corporate taxes only if it makes capital investments. What is the effect of tax incentives in export processing zones firms on business investments in Kenya?

**Literature Review**

**Theoretical review**

The use of tax incentives is widespread even though the available empirical evidence on the cost-effectiveness of such incentives in stimulating investment is highly inconclusive. An important contribution factor to this development is undoubtedly the heightened need perceived by many countries, especially in a regional context, to compete for investment in a world of broadening trade liberalization and high capital mobility. To these countries, tax incentives are often a visible and flexible handle for attracting investment (Surrey, 1970).

Equally important in fuelling the spread of tax incentives could have been the impressive economic successes of a number of Asian countries that also happened to make heavy use of such incentives, although the extent of the contribution of the incentives to the growth performance of these countries is unclear (Tanzi and Shome, 1992).

**A q – Theory approach**

The approach inspired by Tobin’s q-theory of investment (Tobin, 1969). In all endogenous growth models, output growth is driven by the ceaseless accumulation of physical, human or knowledge capital. The rate of real investment determines the rate of capital accumulation and this is where the q-theory comes in. Tobin’s approach focuses on the ratio of a firm’s stock market value to the replacement cost of its capital.

The stock market value of a unit of capital is the present value of its income stream; its replacement cost is the marginal cost of new capital in exogenous growth models, q determines the steady-state capital-labour ratio. In endogenous growth models, it determines the level of real investment. Now because endogenous growth models all make assumptions implying that a constant level of real investment yields constant growth, changes in (or more precisely 1–1) predict growth rate changes (Baldwin and Forslid, 1996).

The effects of tax policy on capital accumulation and valuation based on James Tobin’s q theory of investment. Tobin (1969) argued, increases in the return to capital will raise the market value of existing capital signalling the profitability of additional investment. Additional investment will drive down the marginal product of capital, reducing the asset price of capital goods until equilibrium is restored. While models linking the stock market to investment have been estimated, they have not been used to examine the impact of economic policies on investment.

This approach has several advantages when compared to previsions empirical approaches to modelling investment. Almost all previous evaluations of tax policy’s impact on investment have relied on single equation models linking investment to its proximate determinants, usually output and the cost of capital. For the most part, individual taxes have been ignored and the process of adjustment has been handled in an ad hoc fashion. Most critically, existing approaches to modelling investment decisions are subject to the “Lucas criticism”. The estimated parameters are not likely to be invariant to the choice of policy rules. The equations thus do not provide a basis for estimating the true effects of changes in policy rules (Summer, 1981).

Several authors including Von Furstenberg (1977),
Ciccolo (1977) and Engle and Foley (1975) have estimated variants on equations with exception of Ciccolo (1977), no account was taken of tax effects. Ciccolo’s tax adjustments differ from those used here because he takes no account of individual taxes, and implicitly makes different assumptions about the tax treatment of adjustment costs. These studies have all related components of business fixed investment to q, which may not be appropriate for non-corporate investment.

**The Common – Agency approach**

This approach involves limiting the government’s power to tax in interesting ways and then investigating the resulting implications for tax competition. One such aspect is incompleteness in a government’s information about the firms that it is attempting to tax. For example, firms may differ in the degree to which they are inter-regionally mobile, but such differences may be difficult for the government to observe. In this case, the government cannot tax a firm in a way that directly depends on its unobserved aspects of firm behaviour that may serve as signals of these characteristics, such as the firm’s business investment decisions (Wilson, 1999).

The common – agency approach seems especially useful for analyzing the taxation of multinational, such as EPZs. Many countries attempt to tax the income of foreign subsidiaries, suggesting a common agency problem in which the home and host countries are the principals. Bond and Gresik (1996) present an interesting model in which the home and host countries independently confront the multinational with subsidies and trade taxes. Relative to setting these policy instruments cooperatively, tax competition is shown to lower the countries aggregate welfare and leave the multinational worse off. In other words, the inefficiencies associated with tax competition turn out to be detrimental to all parties.

**Types of tax incentives**

Tax incentives usually take the form of direct or indirect taxes. Indirect tax incentives are usually either partial or full exemptions from import tariffs excises, and/or sales tax on (in the case of VAT, the zero-rating of) inputs purchased by qualified enterprises. Direct tax incentives are usually categorized into two categories; those that tax corporate profits at a lower nominal rate than the regular Corporate Income Tax (CIT) rate; and those that provide more attractive terms for recovering investment costs than under the regular CIT provisions (Easson, 2001).

**Indirect tax incentives**

Granting indirect tax incentives to export-oriented industries is a prevalent practice worldwide. Conceptually, relieving inputs used in the direct production of exports from the burden of indirect taxes is clearly justifiable on the principle of destination-based taxation, and should, in general, be supported. The question that remains is largely one of execution rather than policy: what would be the preferred mechanism to grant such incentives to minimize the leakage risks; since exercises are seldom imposed on inputs, the issue mainly concerns tariff and Value Added Tax (VAT) exemptions (Zee et al, 2002).

Tariff exemptions are in two common mechanism, which effect tariff exemptions on imported inputs used in the production of exports; the first one is duty drawback schemes. Here tariffs are first payable upon importation of all inputs, but are then refunded on that portion of imported inputs embedded in goods that are actually exported; refunds are typically provided on the basis of some input-output relationships of the exported goods in question; and the second one is suspensive regimes, where the payment of tariff on imported inputs is suspended upon importation by qualified exporters (the typical qualifying criterion is a threshold level of exports to total sales); those inputs used in the production of goods sold domestically would become taxable at a later stage (Chia and Whalley, 1995).

VAT exemptions is a form of export-oriented incentive, granting indirect tax incentive. Since exports are zero-rated under a destination-based VAT and, therefore do not bear any VAT burden, the zero-rating of inputs used in the direct production of exports is strictly unnecessary (Mclure, 1999). But, major exporters are perpetually in an excess VAT credit position when their inputs are taxed and will therefore bear a possibly significant cash-flow burden even if such credits are refunded in a timely fashion (Mchure, 1999).

**Direct tax incentives**

Direct tax incentives under the Corporate Income Tax (CIT) can be broadly classified into two categories; those that tax corporate profits at a lower nominal rate than the regular CIT rate; and those that provide more attractive terms for recovering investment costs than under the regular CIT provisions. While the intended goal of any incentive in both categories is the same; to reduce and effective CIT burden on business investment, for analytical purposes it is important to distinguish the two, as they could entail very different policy and administrative implications (Easson, 2001). Incentives in the form of reductions in the CIT rate could range anywhere from complete exemption (CIT holidays) to a rate that is below the regular CIT rate for qualified investment projects. Of all the different forms of tax incentives, CIT holidays are the most popular among developing countries, but are now rarely found in developed countries. The most frequently cited advantages of CIT holidays are that; they relieve the tax authorities of the burden of administering them; they allow qualified investors the added benefit of being able to side-steps often complex tax laws, onerous tax regulations, and corrupt tax administrations; and they are
neutral in their impact on the relative factor (capital and labour) intensities of qualified projects (Zee et al., 2002).

Investment allowances are incentives that typically stipulate that certain percentages of the initial costs of plant and equipment investments can be written off immediately as expenses in the current period, in addition to the normal allowable depreciation on the full costs of such investments. Compared with CIT holidays, these incentives have a number of advantages. They are, for example, a much better targeting instrument than CIT holidays for promoting particular types of investments, as noted earlier, and their revenue costs are much more transparent and easier to control (a property shared with CIT rate reductions). Investment allowance is a type of tax incentive that is most amenable to both effective targeting and transparent administration (Chia and Whalley, 1995).

Investment tax credits is another form of direct tax incentive. In contrast to investment allowances, investment tax credit provides stipulated percentages of investment costs that could be deducted from CIT liabilities. If the CIT rate is uniform, investment and investment tax credits are clearly equivalent forms of tax incentives in all substantive aspects, and hence share the same advantages and shortcomings as the former are directly expressible in terms of the latter irrespective of the scale of the investment (Easson, 2001).

**Effects of tax incentives**

Tax incentives have been used by countries to achieve a variety of different objectives, not all of which are equally compelling on conceptual grounds. Stimulating investment in general, and in most developing countries attracting Foreign Direct Investment (FDI) in particular, is usually the primary motivation for granting tax incentives. Other commonly cited objectives include reducing unemployment, promoting specific economic sectors or types of activities as a matter of either economic or social policy, and addressing regional development needs. Quite often countries pursue multiple objectives with overlapping tax incentives (Zee et al., 2002). Tax incentives also distort resource allocation, as some activities, as some activities are encouraged over others not because they are necessarily more economically productive, but because they have been given a tax advantage. Granting of tax incentives creates opportunity for corruption and socially unproductive rent-seeking activities (Chirinko, 1993). In view of the potentially harmful effects from the spread of tax incentives, many economists have argued that to attract investment, countries should instead implement appropriate financial policies to ensure macroeconomic stability, and should pursue tax and other structural reforms to enhance competitiveness and better enable the market to efficiently allocate resources (Zee et al., 2002).

The realistic approach that recognizes that, regardless of their limitations, tax incentives are unlikely to be abandoned by most especially developing countries as policy instruments for furthering a variety of national objectives, notably for attracting/competing for FDI and/or stimulating the general level of investment. For this reason, it focuses not on the complete elimination of tax incentives, but on ways to minimize their harmful effects (Easson, 2001).

A crucial consideration that bears on the decision to grant tax incentives should be their cost effectiveness. This implies that the mere identification of the existence of positive externalities associated with certain types of investment projects is not sufficient in and of itself for justifying the use of incentives in all instances. Rather, their use should be predicated on the belief that the benefits to the economy that can be expected from an increase (if any) in the incentive-favoured activities would actually outweigh the total costs of the tax incentives granted (Fiflio and Blonigen, 2000).

Cost-effectiveness is a positive effect of tax incentive on business investment globally. Granting tax incentives entails four types of costs; distortions between investments granted incentives and those without incentives; forgone revenue (on the assumption that the government operates under a revenue constraint, so that the cost revenue would have to be compensated from alternative distortive taxes); administrative resources required to administer them; and the social costs of corruption and/or rent-seeking activities connected with abuse of tax incentive provisions. While these costs could be substantial, the benefits to the economy that could be attributed solely to tax incentives are less clear and not easily quantifiable. Hence, the cost-effectiveness of tax incentives is often questionable (Zee et al., 2002).

The distortion costs of tax incentives could arise even if such incentives are used to correct for externalities, since the amount of incentives granted may not conform exactly to the extent of the externalities involved, due to the inherent difficulties in measuring the latter. By extension, such costs would also arise wherever tax incentives are erroneously granted to investment projects with no positive externalities, as could happen (for example) through abuse and leakage on the system (Hall and VanReenan, 2000).

The revenue costs of tax incentives have two different dimensions. First, investment projects could have been if there has been no tax incentive. For these projects, which typically comprise those of the highest profitability and, therefore, having the greatest economic merits, the availability of tax incentives would simply represent a free gift from the government to either the investors or, if they are of foreign origin, the treasury of their home countries. The latter outcome would come about if any income that is spared from investors' home countries as it would be the case when these countries have tax systems that are based on the residence principle (Chirinko, 1993).

**METHODOLOGY**

This study adopted a descriptive design because the study aims at giving accurate description on the situation
of the tax incentives and the probable effect on export processing zone. In order to maintain these occurrences, descriptive survey is preferred because it makes enough provision for the protection against bias and maximizes reliability of the evidence collected (Kothari, 2004). Descriptive research studies are designed to obtain pertinent and precise information concerning the current status of a phenomenon and whenever possible, to draw a valid general conclusion from the facts discovered (Kombo and Tromp, 2006). The target population for this research comprised of all the Export Processing Zones Firms in Kenya which according to EPZ Authority (2012), there are 104 in number categorized as active, dormant, closed or setting up as presented in Appendix II. A sample size of 65 EPZ firms situated in the Nairobi Metropolitan (that is Nairobi, Athi River and Kajiado Districts) was obtained through purposive sampling. This was adequate since it represents 62.5 percent, far much above the 20 percent, which is recommended by Norman and Fraenkel (2001) as the minimum adequate sample size for any study. Both primary and secondary data was collected. Primary data was collected through value added questionnaires from finance managers whereas secondary data was collected from organizational journal and statements of account.

The validity of the data collection instrument was tested through content validity. A pilot study was conducted by the researcher and the results were analyzed for validity and reliability of the research instruments. During the pretest, respondents were requested to leave unanswered items they find ambiguous. Completed questionnaire were later analyzed and improved depending on the need to do so. The research instruments were piloted in two EPZs which were not be involved in the main study. The Pearson’s Product Moment Correlation Co-efficient was used where it was found to be 0.87 and indication that the instruments were consistent hence reliable. An analytical model was developed to analyze the relationship between performance of EPZ firms and tax incentives, the following model was used:

\[ I = \alpha + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \beta_4X_4 + \epsilon \]

Where:

'\( I \)' - Dependent variable and it represents investments of EPZ firms.

'\( \alpha \)' - Was the autonomous component, which was level of performance of EPZ firms that was not affected by the factors in question. It also gives the intercept of the curve.

'\( \beta_1 \)' - This was the coefficient of proportionality which tells the amount by which performance of EPZ firms changes due to a unit change in tax incentives.

'\( X_1 \)' - This was one of explanatory variable, tax incentives.

'\( \beta_2 \)' - It was a coefficient of proportionality which was showing by how much our dependent variable change with one unit change in profit/value added.

'\( X_2 \)' - This presents second independent variable profit/value added.

'\( \beta_3 \)' - This was the coefficient of proportionality which tells the amount by which performance of EPZ firms changes due to a unit change in sales.

'\( X_3 \)' - This was one of explanatory variables, sales.

'\( \beta_4 \)' - This was the coefficient of proportionality which tells the amount by which performance of EPZ firms changes due to a unit change in total expenditure.

'\( \epsilon \)' - Was a random error term and takes care of other factors that influence performance of EPZ which are not defined in the model.

RESULTS

Types of Tax Incentives offered to EPZ Firms

The study sought to establish the various types of tax incentives offered to EPZ Firms in Kenya. A 5-point Likert scale rating was used where 1 represents the least extent while 5 represent the greatest extent. Mean and standard deviation were then used to interpret the results were the higher the mean the larger the extent and vice versa. As per the standard deviation, a higher value indicated a larger deviation from the mean and vice versa. The most prevalent factor would therefore be considered as the one with higher mean (close to 5) and a lower standard deviation (close to 0). The results are presented in table 1.

Most respondents expressed that their business investments have benefited on the grants or loan guarantees (4.7), corporate income tax incentives (4.4), tax holidays or reduced tax rates (4.1), investment allowances (4.0), exemption from import tariffs (4.0), exemption from sales, wage income or property taxes (3.9) and subsidized financing (3.6). On the other hand, only a few respondents had the feeling that, their businesses have benefited from provision of infraprofit/value added, training (2.0), protection from import competition (2.3), preferential access to government contracts (2.4), reduction of social security contributions (2.7), subsidized delivery of goods and services (2.8) and accelerated depreciation (2.8).

Effect of Tax Incentives on Investment

Positive effects

The study sought to determine the effect of tax incentives on investment. Both positive and negative effects were considered. The findings on positive effects are presented in table 2.

Positive impact of tax incentives on performance of EPZs as indicated by the respondents include increased foreign exchange earnings for the state (4.7), tax breaks (3.9), increased gross exports that are used to boost business investments in the country (3.7), high quality manpower (3.6), good source of labor training and learning by doing including assisting countries in developing an industrial labor force (3.6) and procedural incentives (3.6) as well as travel connections and quality
Table 1: Level of business benefit from different taxes

<table>
<thead>
<tr>
<th>Tax incentive</th>
<th>Mean</th>
<th>Standard Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate income tax incentives</td>
<td>4.4</td>
<td>0.7</td>
</tr>
<tr>
<td>Tax holidays or reduced tax rates</td>
<td>4.1</td>
<td>0.8</td>
</tr>
<tr>
<td>Tax credits</td>
<td>3.4</td>
<td>1.2</td>
</tr>
<tr>
<td>Investment allowances</td>
<td>4.0</td>
<td>1.5</td>
</tr>
<tr>
<td>Accelerated depreciation</td>
<td>2.8</td>
<td>1.5</td>
</tr>
<tr>
<td>Reinvestment or expansion allowances</td>
<td>3.3</td>
<td>0.8</td>
</tr>
<tr>
<td>Exemption from or reduction of withholding taxes</td>
<td>3.4</td>
<td>1.3</td>
</tr>
<tr>
<td>Exemption from import tariffs</td>
<td>4.0</td>
<td>1.5</td>
</tr>
<tr>
<td>Exemption from export duties</td>
<td>3.1</td>
<td>1.8</td>
</tr>
<tr>
<td>Exemption from sales, wage income or property taxes</td>
<td>3.9</td>
<td>1.4</td>
</tr>
<tr>
<td>Reduction of social security contributions</td>
<td>2.7</td>
<td>1.1</td>
</tr>
<tr>
<td>Subsidized financing</td>
<td>3.6</td>
<td>1.1</td>
</tr>
<tr>
<td>Grants or loan guarantees</td>
<td>4.7</td>
<td>0.5</td>
</tr>
<tr>
<td>Provision of infraprofit/value added, training</td>
<td>2.0</td>
<td>1.1</td>
</tr>
<tr>
<td>Preferential access to government contracts</td>
<td>2.4</td>
<td>1.5</td>
</tr>
<tr>
<td>Protection from import competition</td>
<td>2.3</td>
<td>1.2</td>
</tr>
<tr>
<td>Subsidized delivery of goods and services</td>
<td>2.8</td>
<td>1.4</td>
</tr>
</tbody>
</table>

Table 2: Positive effects of tax incentives

<table>
<thead>
<tr>
<th>Positive impact</th>
<th>Mean</th>
<th>Standard Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax breaks</td>
<td>3.9</td>
<td>1.0</td>
</tr>
<tr>
<td>Procedural incentives</td>
<td>3.6</td>
<td>1.3</td>
</tr>
<tr>
<td>Better infraprofit/value added</td>
<td>2.1</td>
<td>1.3</td>
</tr>
<tr>
<td>Travel connections and quality of life</td>
<td>3.5</td>
<td>1.5</td>
</tr>
<tr>
<td>Low cost location</td>
<td>2.6</td>
<td>1.3</td>
</tr>
<tr>
<td>High quality manpower</td>
<td>3.6</td>
<td>1.1</td>
</tr>
<tr>
<td>Increased foreign exchange earnings for the state</td>
<td>4.7</td>
<td>0.5</td>
</tr>
<tr>
<td>Increased gross exports that boost investments in the country</td>
<td>3.7</td>
<td>1.1</td>
</tr>
<tr>
<td>Job creation / income creation for the nationals</td>
<td>3.3</td>
<td>0.9</td>
</tr>
<tr>
<td>Average wage in EPZ higher than average wage outside the firm</td>
<td>2.3</td>
<td>1.2</td>
</tr>
<tr>
<td>Good labor training assists in developing an industrial labor force</td>
<td>3.6</td>
<td>1.2</td>
</tr>
<tr>
<td>Management and supervisory training</td>
<td>3.1</td>
<td>1.7</td>
</tr>
</tbody>
</table>

Table 3: Negative effects of tax incentives

<table>
<thead>
<tr>
<th>Negative impact</th>
<th>Mean</th>
<th>Standard Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>The administration is legally complicated and conflictive</td>
<td>4.3</td>
<td>1.1</td>
</tr>
<tr>
<td>The government revenue loss through taxation is not worth it</td>
<td>2.3</td>
<td>1.2</td>
</tr>
<tr>
<td>Represents unfair international competition and accelerate downfall</td>
<td>2.8</td>
<td>1.4</td>
</tr>
<tr>
<td>The workers are denied their basic rights</td>
<td>2.0</td>
<td>1.1</td>
</tr>
<tr>
<td>Cause unhealthy competitions in the sector</td>
<td>3.7</td>
<td>1.0</td>
</tr>
<tr>
<td>Hide social production costs hence an environmental “time-bomb”</td>
<td>3.0</td>
<td>1.1</td>
</tr>
</tbody>
</table>

of life (3.5). Better infraprofit/value added and average wage in EPZ being higher than average wage outside the firm were however stated as the least positive impacts derived from tax incentives to EPZ.

**Negative effects**

The findings on negative effects of tax incentives on investment are presented in table 3. Regarding the extent to which respondents agree with some allegations regarding the negative impact of the tax incentives to the free firms, the administration is legally complicated and conflictive was found to be the most prevalent factor with mean of 4.3 while the observation that, there are unhealthy competitions in the manufacturing sector caused by the tax incentives to the EPZ had mean of (3.7). Respondents also moderately argued that, free firm companies do not pay the social costs of production and may be creating a health and environment "time-bomb" in developing countries with mean of 3.0. Tax incentives, however, are not connected with the argument that, the workers are denied their basic rights as supported by mean of only 2.0.
Relationship between tax incentives and investment
A multivariate regression analysis was conducted to determine the relationship between tax incentives and investments. The findings are presented in Table 4.

The researcher considered five variables to be significantly influencing performance of EPZ which included the organization profit/value added, tax incentives, total expenditure and sales. The study revealed that the most prevalent factor among the five mentioned was sales with beta value of 0.64 while tax incentives, profit/value added and total expenditure had beta value of 0.10, 0.85, 0.53 and 0.33 respectively. At 95% confidence level, all explanatory variables apart from sales were not significant since had an alpha of more than 0.05 (that is, 0.44 for profit/value added, 0.39 for tax incentives and 0.95 for total expenditure. Sales were considered significant for this study because the significant level was stated at 0.05 which was less than 0.05. Based on objectives of this study, even if tax incentives contribute to direct investments in EPZ, the influence is insignificant.

From the model, the constant value of 0.64 implies that the level of investment of EPZ will have an index of 0.64 when coefficients for all variable factors are zero. This is an indication that the five independent variables under investigation were positively related to the dependent variable (investment of EPZ firms).

<table>
<thead>
<tr>
<th>Model</th>
<th>Un-standardized coefficients</th>
<th>Standardized coefficients</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
</tr>
<tr>
<td>(Constant)</td>
<td>0.64</td>
<td>0.01</td>
</tr>
<tr>
<td>Profit/value added</td>
<td>0.53</td>
<td>0.33</td>
</tr>
<tr>
<td>Tax incentives</td>
<td>0.85</td>
<td>0.05</td>
</tr>
<tr>
<td>Total expenditure</td>
<td>0.33</td>
<td>0.25</td>
</tr>
<tr>
<td>Sales</td>
<td>0.56</td>
<td>0.10</td>
</tr>
</tbody>
</table>

DISCUSSION
The study in consistence with the statistical data shows that, investments in EPZ firms increase with increase in sales, profit as well as tax incentives. The Export Processing Zones (EPZ) programme recorded a downward trend in the performance of key indicators in 2009, as a result of adverse effects of global economic recession, especially in the US Market which is a prime destination of EPZ exports. The situation was further aggravated by unfavourable business environment characterized by high costs of production and stiff competition from Asian countries. The EPZ programme is undergoing transformation to Special Economic Zones (SEZ) with a wider scope of activities envisaged to meet the objectives of the Vision 2030.

According to Ministry of Planning (2011), the number of enterprises operating under the EPZ rose to 83 in 2009 from 74 in 2008. Local ownership of investment within the EPZ increased from 14.3 per cent in 2008 to 19.3 per cent in 2009. Joint ventures went up by 24.1 per cent compared to 24.7 per cent in 2008 while foreign investments constituted 56.6 per cent in 2009 compared to 60 per cent reported in 2008. The authority has started implementing an incubator project in order to attract and nurture local business. As argued by Fiflio and Blonigen, (2000), a crucial consideration that bears on the decision to grant tax incentives should be their cost effectiveness. This implies that the mere identification of the existence of positive externalities associated with certain types of investment projects is not sufficient in and of itself for justifying the use of incentives in all instances. Rather, their use should be predicated on the belief that the benefits to the economy that can be expected from an increase in the incentive-favored activities would actually outweigh the total costs of the tax incentives granted. At the same time, foreign exchange earnings are an important benefit of FDI. Improvement of the hard currency earnings of the host economy is frequently cited as a major objective behind an EPZ which is a foreign direct investment. This can occur principally from increased (net) exports but may also come from the initial FDI injection where this goes to domestic actors (e.g., construction, purchase of equipment). This in turn is expected to boost the balance of payments position of the host economy, thereby relaxing possible macroeconomic constraints.

CONCLUSIONS
The study reveals that, the level to which EPZs have benefited on the following tax incentives include grants or loan guarantees; corporate income tax incentives; tax holidays or reduced tax rates, investment allowances; exemption from import tariffs; exemption from sales, wage income or property taxes and subsidized financing. The Firms however do not largely benefit from subsidized delivery of goods and services; accelerated depreciation; reduction of social security contributions; preferential access to government contracts; protection from import competition as well as provision of infraprofit/value added, training. Notable was the fact that, tax incentives, even though they related directly to investments, they have very little influence as given by a high significance level of 0.39.

Positive impact of various attractive incentives
extended to the export processing zones include increased foreign exchange earnings for the state, tax breaks, increased gross exports that are used to boast business investments in the country, high quality manpower, good source of labor training and learning by doing and assisting countries in developing an industrial labor force as well as procedural incentives. Negative impacts, on the other hand include the administration is legally complicated and conflictive; unhealthy competitions in the manufacturing sector caused by the tax incentives to the EPZ and free firm companies not paying the social costs of production and may be creating a health and environment "time-bomb" in developing countries. It is also worth noting that, performance of EPZs is highly influenced by the amount of profit made in a particular fiscal period, cost of production (expenditure), annual sales realized and tax incentives awarded by the government.

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