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Foreign Direct Investment in Bangladesh: Prospects and Challenges

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Abstract
Foreign Direct Investment (FDI) plays a vital role in developing country all over the world. It is an part of the industrial development, economic transition, business liberalization and macro economic growth story in Bangladesh over the last decade.FDI plays a dominant role in the economy of Bangladesh through accelerating Gross Domestic Product (GDP), export and domestic investment. So it is vital for a developing country like Bangladesh to carry out effective measures in protecting the prospective foreign investors so that they can get a congenial atmosphere to invest their capital.The present scenario of FDI in Bangladesh is not still satisfactory enough, because of some recognizing barriers but Bangladesh has some competitive advantages also i.e., that are abundant natural resources, human recourses, cheap labor forces, sectors for prospective investment are textile, frozen foods, leather, agro-based industries and information technology, a stable political atmosphere, monetary and fiscal policy, improvement of infrastructure and long term strategic planning to stimulate FDI might be able to make the condition favorable to attract foreign investment in Bangladesh. This paper recommends some guidelines that can be used to foreign investment in Bangladesh. This paper also investigates the state of the business environment in Bangladesh, identifies determinants affecting the FDI and the benefit that the country may derive from it.
Keywords: FDI, GDP, prospects, and problem of FDI.

Introduction

Foreign direct investment (FDI) is one of the vital ingredients and a potent weapon for overall development process of a developing country like Bangladesh. Industrial development is an important pre-requisite for economic growth of a developing country. FDI inflows help to increase the surplus of capital account, improving balance of payment and macroeconomic stability of the economy. The poor countries usually have low rates of capital accumulation and thus, FDI is regarded as a vital supplementary source of capital to support domestic investment, to achieve economic growth.FDI provides the poor countries better access to modern technology, easier technology transfer, improving managerial and labor skills, etc the phenomenon, usually referred to as spillover effect of FDI , which contribute to the increase labor productivity of domestic enterprises and ultimately to economic growth.

In Bangladesh, FDI plays a significant role in GDP acceleration and economic growth (Mottaleb 2007). So, Government of Bangladesh is trying to create a favorable investment environment through introducing economic policies, incentives for investors, and so on. Various positive attributes of Bangladesh is now drawing the attention of the investors from both developed and developing countries. In Bangladesh, it is available to get skilled labor and relatively stable macroeconomic environment. These two important factors can make Bangladesh an alluring destination for foreign investors. Lowest wage among the Asian countries, tolerable inflation rate, investment friendly, customs regulations and attractive incentive packages make Bangladesh is a favorable investment destination.

According to A.R.Chowdhury (2012), Foreign Direct Investment (FDI) has been an important part of the economic transition, business liberalization and macro-economic growth story in Bangladesh over the decade. According to the 2012 World Investment Report (WIR) of the UNCTAD, the garment sector attracted the highest amount of FDI following by the banking, energy and telecommunication sectors, respectively. So for this reason, FDI is very much helpful for Bangladesh economy.

Objectives of the study:

The Objectives of this paper are:
1. To evaluate the FDI status in Bangladesh.
2. To find out the prospects and problems of FDI in Bangladesh.

3. Suggests a few necessary steps to make the FDI more useful for Bangladesh.

The Methodology of the Study

This paper is prepared on secondary information. The relevant secondary data are collected from Board of Investment, Bangladesh, Statistics Department and Research Department of Bangladesh Bank (Central Bank of Bangladesh), Bangladesh Bank Bulletin, Economic Trend, Bangladesh Economic Review, World Investment Report 2010 published by UNCTAD, various articles, Publications of the World Bank, several books, and web sites, journal report etc. are also considered.

Literature Review

There is a global race for attracting FDI, but how much it can contribute to host country's economic development is a matter of assessment. If the investing country s wealthier than the host country then capital will flow to the host country (Zhao, 2003).

Rothgeb (1984) found an immediate troublesome effect of FDI flows on developing countries. This effect would overcome after a short period of time, with positive impacts on growth. Rothgeb (1984) used his model to explore the impact of foreign investment on the growth of Bangladesh and found that FDI has a positive impact on growth. He also found a strong positive effect of the change in the level of domestic investment on growth.

Balasubramanyan,V. N et al (1996) did an examination about the impact of FDI on economic growth in developing economies using ordinary least squares. Applying the export promotion strategy, they found positive and significant impact of FDI on economic growth in developing countries. Simultaneously, it also showed that such relations do not exist in developing countries applying the import substitution strategy.

Borenszteina et al (1998) examined the data on FDI inflows of sixty nine developing countries by regression framework and found the importance of FDI as a means of transferring technology that contributes more to growth than domestic investment.

Mottaleb (2007) studied the determinants of FDI and its effect on economic growth in developing countries. He studied panel data of FDI flows of sixty low-income and lower-middle income countries and found that FDI has an important effect on economic growth of third world countries by creating bridge between the gap of domestic savings and investment and familiarizing the up to date technology and management skill from developed countries.

Foreign Direct Investment (FDI):

In the context of the new theory of economic growth, FDI is considered as an engine of growth of mainstream economics and accounts for more than half of the private capital flows between countries in the world (Thilakaweera, 2011). FDI definition will be followed in accordance by the International Monetary Fund (IMF-) ,"Investment that is made to acquire lasting interest in an enterprise operating in an economy other than that of the investor , the investor's purpose being to have an effective source in the management of the enterprise

History of FDI in Bangladesh:

FDI played a minor role in the economy of Bangladesh until 1980, a crucial year of policy change. The Government of Bangladesh (GOB) enacted the "Foreign Investment Promotion Act, 1980' in an attempt to attract FDI. Expect five industries, which were reserved for the public sector: defense equipment and machinery, nuclear energy, forestry in the reserved forest area, security printing and railways, FDI was allowed in every sector of the economy.

The trend of inflow in Bangladesh has increased over the 1980s as compared to earlier periods ,and this same momentum continues in 1990s as well. The total inflow of FDI has been increasing over the years. During the periods of 1997-2010, total inflows of FDI were USD 8927.9 million, among which the inflows of FDI during 2006-2010 was USD 4158.63 million. In 1977, this inflow was USD 7 million, and in 2008, annual FDI reached to USD 1086.31 million.

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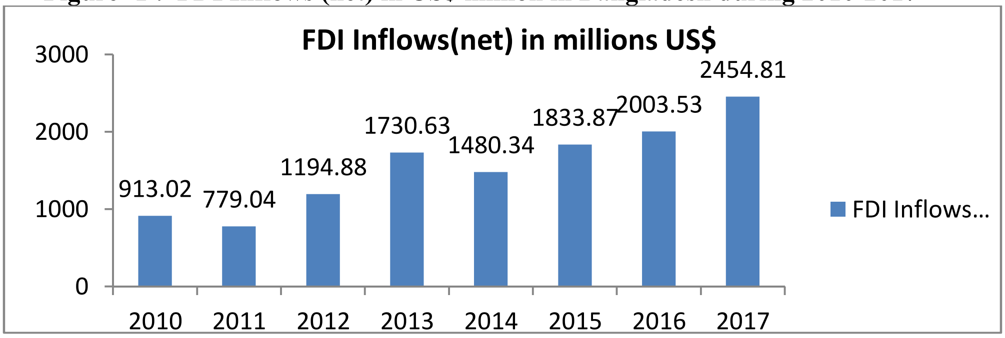
i) Present scenario of FDI in Bangladesh:

Figure- 1 : FDI Inflows (net) in US$ million in Bangladesh during 2010-2017



Source: Survey Report, Statistics Department, Bangladesh Bank (January-June, 2017)

Figure: 1 shows an inconsistent proceeding of FDI inflows during the period.FDI inflows were US$ 913.02 million in 2010. But in 2011 it was a decline in the FDI to US$ 779.04 million. The FDI inflow was on the steady rise from 2012 to 2017.

Total inflows (net) accomplished to US$ 2454.81 million in 2017 which was increased by US$ 451.28 million or 22.52% compared to FDI inflows during 2016 (US$ 2003.53) while in 2016 FDI inflows was increased by US$ 169.66 million or 9.25 % compared to 2015 and an increase of US$ 353.53 million or 23.88% during 2015 compared to 2014.

FDI Inflows (net) by components:

Table - 1: FDI Inflows (net) by components (Figures in million US$)

Year	Equity capital	Reinvested earnings	Intra –company loans	Total inflows
2010	515.14	33.10	66.78	913.02
2011	249.95	445.19	83.90	779.04
2012	454.10	542.35	198.43	1194.88
2013	761.03	645.64	323.96	1730.63
2014	233.84	795.78	450.72	1480.34
2015	528.03	1141.34	164.50	1833.87
2016	505.55	1154.45	343.53	2003.53
2017	1006.74	1253.00	195.07	2454.81

Source: Survey Report, Statistics Department, Bangladesh Bank (January-June, 2017)

In Bangladesh FDI consists of three components: Equity capital, Reinvested earnings and Intra-company loans. In the year of 2010, the equity capital was 515.14 US$ million, Reinvested 331.10 US$ million and Intra –company loans 66.78 US$ million and in the year of 2017, the equity capital was 1006.74 US$ million, Reinvested earnings 1253.00 US$ million and Intra company-loans 195.07 US$ million.

The shifting of component-wise FDI inflow in Bangladesh is clearly shown in figure 3 and figure 4. In present years 2017, the major share of FDI in Bangladesh come from Reinvested earnings .In 2010, the share of Reinvested earnings in total FDI was 36% which increases to 51 % in 2017.On the other hand, share equity capital in total FDI was 56 % in 2010, and in 2017 it was decreased by 41% . On the other, a share of Intra company loans in total FDI was
7.9% in 2017 and 7.31 % in 2010.

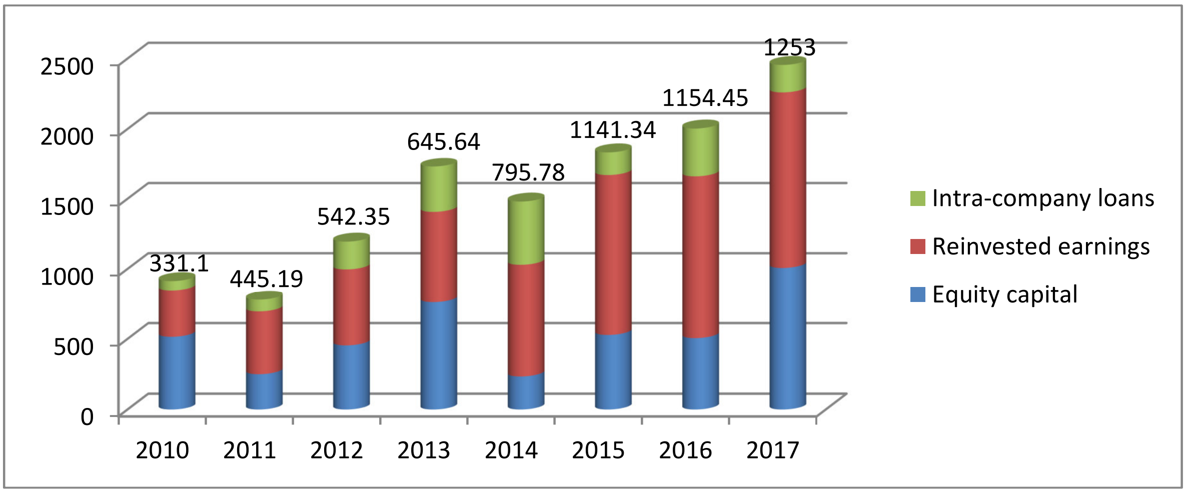


Figure-2: FDI inflows (net) by components during 2010-2017.
Source: Survey Report, Statistics Department, Bangladesh Bank (January-June, 2017)

Figure-3: FDI inflows by components in 2010

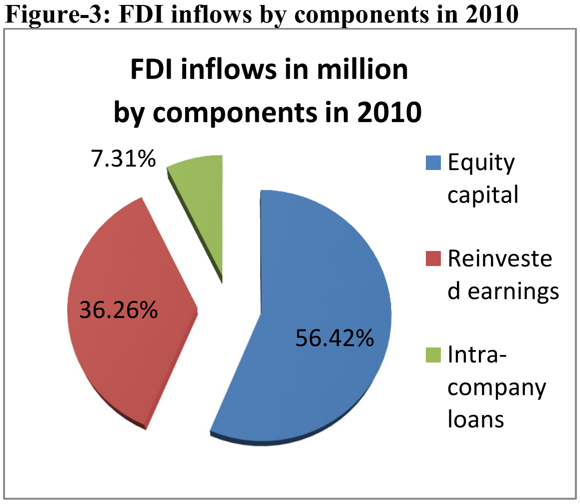
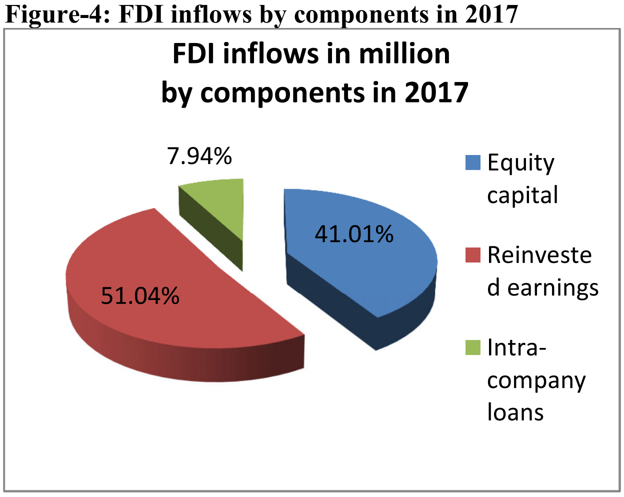


Figure-4: FDI inflows by components in 2017



Source: Survey Report, Statistics Department, Bangladesh Bank (January-June, 2017)

FDI Inflows (net) by Areas (EPZ and non- EPZ) :

Figure 5: shows in the EPZ areas, the FDI inflows were always in steady directions. It also reveals that FDI inflows in Non-EPZ areas was increasing trend during 2010-2017.The FDI inflows in Non- EPZ areas in 2010 recorded to US$ 761.91 , and it continues to increase US$ 2071.35 million in 2017.

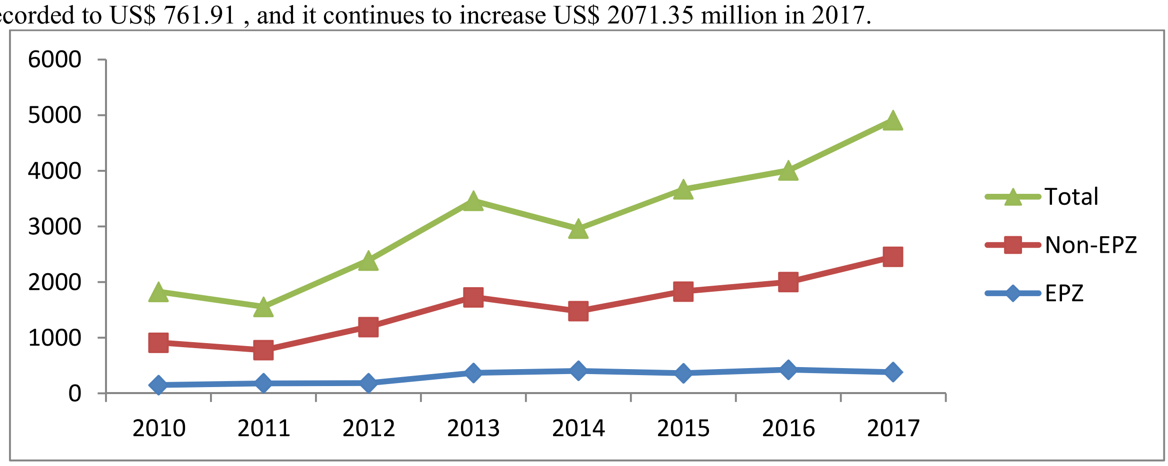


Figure-5: FDI inflows in a million US$ by area (EPZ and Non- EPZ) in Bangladesh during 2010-17
Source: Survey Report, Statistics Department, Bangladesh Bank (January-June, 2017)

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FDI Inflows (Net) by major Sectors (2010-2017):

Table-2: FDI Inflows (Net) by major Sectors (2010-2017) (Figures in million US$)

Sectors	2010	2011	2012	2013	2014	2015	2016	2017
Agriculture & Fishing	10.95	11.53	49.50	29.72	28.99	29.22	36.57	43.26
Power	36.79	52.59	64.20	71.32	47.72	80.44	207.84	334.26
Gas & Petroleum	36.87	74.60	180.77	22.35	2.71	199.54	222.32	133.67
Textiles & Wearing	157.94	225.17	241.39	412.43	445.82	351.62	396.05	360.35
Chemicals & Pharmaceuticals	8.05	8.98	14.09	30.39	47.92	25.71	37.02	35.97
Metal & Machinery products	1.84	4.90	11.73	14.42	14.81	11.43	2.80	.05
Leather & Leather products	8.75	12.92	8.29	28.01	36.23	36.79	16.35	23.38
Banking	111.56	208.78	253.44	268.53	225.53	389.58	245.20	155.58
Insurance	11.27	15.81	4.27	7.09	.00	-16.01	28.39	42.58
Telecommunication	445.82	52.41	178.90	525.29	267.09	197.22	267.12	593.89
Computer Software & IT	3.40	4.43	8.44	20.34	29.69	4.44	14.13	29.60

Source: Survey Report, Statistics Department, Bangladesh Bank (January-June, 2017)

Table 2 shows the trend of FDI inflows toward power, telecommunication, textile, agriculture, leather products, banking, and insurance. The sectors that attracted maximum FDI (Net inflows) for the year 2017 include Telecommunications (US$ 593.89 million), Textile and Wearing (US$ 360.35 million), power (US$ 334.26 million), Banking (US$ 155.58 million) and Gas and petroleum (US$ 133.67 million) which were 33.88 %, 20.54 %, 19.07 %, 8.88 %, and 7.63 % respectively towards the contribution of total FDI inflows by among major 11 sectors discussed in table 2 .

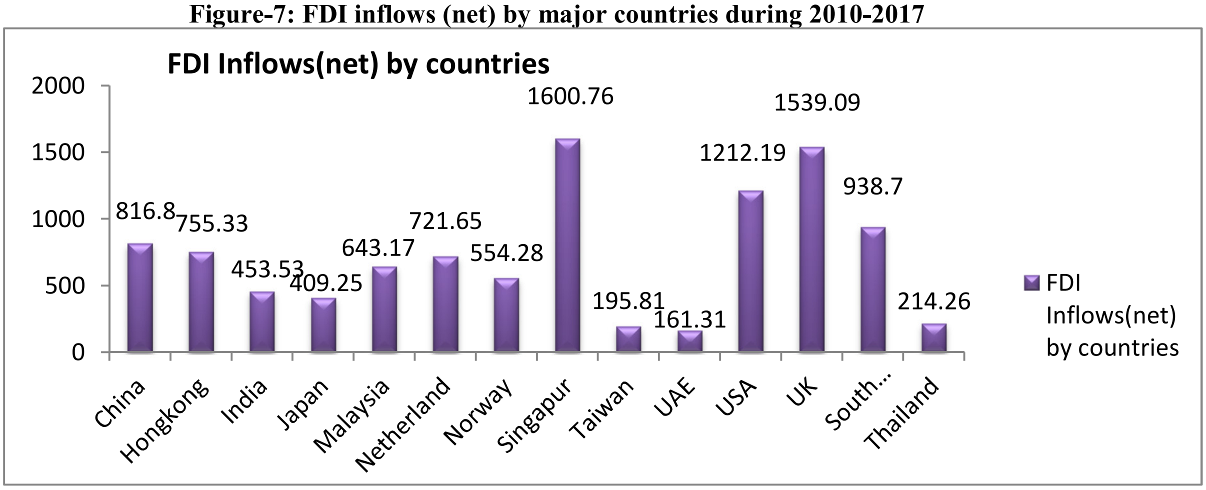
- FDI inflows in agriculture and Fishing sectors reached to US$ 43.26 million in 2017 which increased by US$ 32.31 million compared to 2010.
- FDI inflows (net) into Telecommunication sector arrived at US$ 393.89 million in 2017.
- FDI inflows into Textile and wearing achieved in US$ 360.35 million, which was increased by US$ 202.41 million to 2010. The success in textile through the ready-made garments (RMG) industry was a vital part of this investment.
- FDI inflows into power sector arrived at US$ 334.26 million which was increased by US$ 297.47 million compared to 2010.
- FDI inflows in banking sectors reached to US$ 155.58 million which was increased by US$ 44.02 million compared to 2010.
- FDI inflows (net) in Gas and Petroleum achieved into US$ 133.67 million which was increased by US$ 96.8 million in 2010.

FDI Inflows (net) by major countries during (2010-2017):

FDI inflows (net) from major countries for the year 2017 are arranged in the following order of magnitude were : Singapore (US$701.40 million), United kingdom (US$ 313.87 million), United States of America (US$ 208.71 million), Norway (US$ 187.41 million), South Korea (US$ 178.50 million), India (US$ 95.41 million), China (US$ 608.58 million), Netherlands (90.4 million), and Thailand (US$ 58.69).

China, for the first time, was the world's second – largest investor as FDI inflows by US$ 608.58 million in 2017, which is a new high.

Figure-7: FDI inflows (net) by major countries during 2010-2017



Source: Survey Report, Statistics Department, Bangladesh Bank(January-June, 2017)

Prospects of FDI:
Bangladesh has been promoting FDI for decades with the most liberal investment policy and incentive regime in South Asia. The Foreign Private Investment (promotion and protection) Act. , 1980, ensures equal treatment for local and foreign investors. This act also provides legal protection to foreign investment in Bangladesh against nationalized and expropriation. It also gives the guarantee of repatriation of capital and dividend.

Bangladesh is ranked 119th position globally and 4th in the SAARC region in the EASE of Doing Business Ranking by World Bank and IFC report entitled "Doing Business in 2010."

Some Roles of FDI played in Bangladesh:
1. Proper Utilization of Domestic Resources (Raw Materials and Labor)
2. Investment in Unconventional and Profitable Sectors
3. Development of Skilled Personnel
4. Bangladesh- a promising Market Segment
5. Bangladesh-An attractive Investment Center
6.FDI Reduces Imports, Saves Currency and Provides Lower Price of Product.
7. Introduction of Advanced Technology

Facilities and Incentives for foreign Investors:
1. Tax exemption on royalties, technical knowhow and technical assistance fees and facilities for their repatriation
2. Tax exemption on interests on foreign loans
3. Tax exemptions on capital gains from transfer of shares by the investing company
4. Remittances of up to 50% of salaries of the foreigners employed in Bangladesh and facilities for repatriation of their savings and retirement benefits at the time of their return
5. No restrictions on issuance of work permit to project related foreign nationals and employees
6. Facilities for repatriation of invested capital, profits, and dividends
7. Provision of transfer of shares held by foreign shareholders to local investors
8. Reinvestment of remittable dividends would be treated as a new investment
9. Level playing field: foreign- owned companies duly registered in Bangladesh will be on the same footing as locally owned ones.

Financial incentives for export- oriented industries
1. Cash incentives and export subsidies ranging from 5% to 20% grant on the FOB value of the selected products
2. 90% loans against letters of credit (by banks)
3. Permission for domestic market sales of up to 20% of export oriented companies outside EPZ (relevant duties apply)

Problems of FDI
The problems that have restricted FDI potentials in the country are as follows:
1. Bureaucratic interference
2. Irregularities in processing papers
3. Overlapping administrative procedures
4. The Absence of a transparent system of formalities
5. Continuity and prevent timely implementation of strategic, procedural, and even routine duties
6. Frequent power failures
7. Poor infrastructure support
8. Labor unrest
9. Political unrest
10. Lack of professional personnel
11. lack of commitment on the part of local investors
12. Unexpected delays in selecting projects in studying the feasibility
13. Frequent changes in policies on import duties for raw materials, machinery and equipment etc.

Conclusions and Policy Suggestions:
The global experience suggests that, depending on the country context, the benefits of FDI are highly uneven and can become ambiguous. However, given its present characteristics, Bangladesh is likely to benefit through more FDI inflows. It is therefore, for Bangladesh to ensure an investment climate that can attract more FDI flows to the country. For the purpose, several policy areas are important that include:
Quality of Bureaucracy and Governance: Appropriate reforms should need in the country's administrative

system. The bureaucracy needs reorganization to bring about a perceptible improvement in its efficiency and productivity. Bureaucratic control and interference in business and investment activities should minimize on a priority basis.

Improvement of Law and Order Situation: Law and order situation needs to be improved through appropriate reforms in law enforcement and introducing other measures. A social consensus is to establish the rule of law, avoid political confrontation, and reduce corruption.

Development of Infrastructure and Human Resource: Both the government and private sector need to come forward to invest in infrastructure development including under Public Private Partnership(PPP) arrangements. Appropriate mechanisms like BOO, BOT, BOOT, etc.may be devised to encourage foreign investors to invest infrastructure services both public and private universities should come forward in introducing courses/programs that produce graduates with technical and management skills required in modem industrial and other activities.

Improvement of Port Services: Despite recent improvements, the efficiency of the port services can be further improved through appropriate measures. Similarly, the custom clearance procedures can be further simplified along with improvement in physical facilities and reforms in the labor management system.

Privatization and further Reforms: The privatization program of the state- owned enterprises needs to equipp that would stimulate domestic and foreign investments. Several financial institutions and some of the public utilities should privatize to ensure better and more efficient services. The policies should encourage private sector participation in several key sectors like agricultural processing, manufacturing, infrastructure including transportation, telecommunication, power, port, and in the production of high value- added products.

Setting up Industrial Parks: The development of new industrial parks can help in creating a favorable environment for foreign investment. The availability of ready infrastructure along with secure and enabling investment climate can act as a powerful catalyst in attracting foreign investors for investment in profitable ventures.

Setting up new EPZs: The government may come up with a phased program of setting up new EPZs to extend facilities to - oriented investors. The private sector may also be encouraged to set up new EPZs.

Improving the Country's Image in Abroad: Positive developments regarding the country's economy, society, and prospects, including the hospitable investment climate, and the facilities available to foreign investors, should be projected abroad, especially among the potential investors. Such „image building‟ efforts would be crucial to dispel the negative images that have persisted for long and discouraged the investors from coming forward.

Policies Regarding Macroeconomic Stability: The government should implement appropriate policies to ensure macroeconomic stability, foster growth promoting and growth accommodating policies, and undertake further actions to reduce poverty at a faster rate. Bangladesh has already achieved notable success in this regard and achievements in both economic and social development should be actively publicized abroad to promote a positive image of the country among the prospective foreign investors.

Economic and Commercial Diplomacy: Strengthening economic and commercial diplomacy is a factor in attracting FDI in the present world characterized by rapid globalization and increasing competition. In this respect, improved bilateral relations with potential investor countries can act as a catalyst to increasing FDI inflows to Bangladesh. Moreover, it is not only to improve relations with countries that have already invested in Bangladesh. It also to identify potential investors in other countries and undertake appropriate measures to attract them to invest in the country.

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