FOREIGN DIRECT INVESTMENT IN BANGLADESH: TREND AND PERFORMANCE

DOCTOR OF PHILOSOPHY

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For my

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FOREIGN DIRECT INVESTMENT IN BANGLADESH: TREND AND PERFORMANCE

Thesis submitted to the University of Dhaka for the Degree of Doctor of Philosophy In Marketing

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FOREIGN DIRECT INVESTMENT IN BANGLADESH: TREND AND PERFORMANCE

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DECLARATION

The work presented in this thesis is original and has not been submitted by me to any University or Institution for the award of any degree or diploma. The thesis entitled 'FOREIGN DIRECT INVESTMENT IN BANGLADESH: TREND AND PERFORMANCE' submitted by me for the award of the Degree of Doctor of Philosophy at the University of Dhaka is based upon my own work carried under the supervision of Professor Haripada Bhattacharjee, Department of Marketing, University of Dhaka, and that neither of this thesis nor any part of it has been submitted for the award of any degree or diploma anywhere.

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Md. Mizanur Rahman

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ACRONYMS

AIP:	Amended Industrial Policy
BEPZA:	Bangladesh Export Processing Zone Authority
BMPP:	Burge Mounted Power Plants
BMRE:	Balancing, Modernization, Replacement and Expansion
BOI:	Board of Investment
BOO:	Build, Operate and Own
BSCIC:	Bangladesh Small and Cottage Industries Corporation
CDA:	Chittagong Development Authority
CEPZ:	Chittagong Export Processing Zone
DEPZ:	Dhaka Export Processing Zone
DESA:	Dhaka Electric Supply Authority
DESCO:	Dhaka Electric Supply Company
DFI:	Development Financial Institution
EO:	Export Oriented
EOSP:	Employee Owned State Program
EPB:	Export Promotion Bureau
EPZ:	Export Processing Zone
ESAF:	Enhanced Structural Adjustment Facility
EXPB:	Export Performance Benefit
FERA:	Foreign Exchange Regulation Act
FFYP:	First Five Year Plan
FY:	Fiscal Year
GATT:	General Agreement on Trade and Tariffs
GDP:	Gross Domestic Product
GIR:	General Index Register
GNP:	Gross National Product
GSP:	Generalized System of Preference
HSC:	Harmonized System Code
HYV:	High Yielding Varieties
IFC:	International Finance Corporation
IIP:	Industrial Investment Policy
IJO:	International Jute Organization
IMF:	International Monetary Fund
IP:	Industrial Policy
IPI:	Industrial Production Index
IPO:	Initial Public Offering
IRC:	Import Registration Certificate
IS:	Import Substitution
JV:	Joint Venture
KDA:	Khulna Development Authority
L/C:	Letter of Credit
LDC:	Least Developed Country
MFA:	Multi Fiber Agreement
MIS:	Management Information System

MVA:	Manufacturing Value Added
NBR:	National Board of Revenue
NFCD:	Non-resident Foreign Currency Deposit
NIC:	Newly Industrialized Country
NIE:	Newly Industrialized Economy
NIIP:	New Industrial Investment Policy
NIP:	New Industrial Policy
NPC:	National Productivity Council
NPR:	Nominal Protection Rate
OECD:	Organization for Economic Cooperation and Development
PAYE:	Pay As You Earn
PDB:	Power Development Board
PGCB:	Power Grid Company of Bangladesh
PHED:	Public Health and Engineering Department
PSI:	Pre Shipment Inspection
R& D:	Research and Development
RDA:	Rajshahi Development Authority
REB:	Rural Electrification Board
RIP:	Revised Industrial Policy
RMG:	Ready- Made Garments
SAF:	Structural Adjustment Facility
SAP:	Structural Adjustment Program
SAR:	Structural Adjustment Reform
SCI:	Small and Cottage Industries
SEC:	Securities and Exchange Commission
T&T:	Telegraph and Telephone
TCC:	Tripartite Consultative Council
TFYP:	Third Five Year Plan
TNC:	Transnational Corporation
TRC:	Telecommunication Regulatory Authority
UNCTAD:	United Nations Conference on Trade and Development
UNDP:	United Nations Development Program
USTDA:	United Nations Trade and Development Agency
VAT:	Value Added Tax
WASA:	Water and Sewerage Authority
WTO:	World Trade Organization

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CHAPTER- I

BACKGROUND AND RATIONALE OF THE STUDY

Economic development involves a process by which a backward stagnant economy gets transformed into a self-sustained one. This process is generally characterized by a rise in levels of investment and saving, an increase in human skills, progressive modernization of technology, a substantial change in the composition of output and employment, changes in social modes and outlook, development of institutions, and the like. Although the process of development requires that all or most of these grow proportionately and simultaneously, in the ultimate analysis, investment or capital accumulation happens to be the ***dramatis personae***.

Capital accumulation can take place only if an economy has the necessary capacity to save. A typical developing country with low levels of consumption and huge unemployment has hardly any capacity to save and is caught up with what Ragner Nurkse calls a vicious circle of poverty (Nurkse, 1962). The low level of income is a reflection of low productivity, which, in turn, is due to lack of capital, resulting from an inability to save.

Applying certain exogenous forces this vicious circle can be broken down. One way is to import capital from outside, which may make the transition from economic stagnation to self- sustaining economic growth possible. The experience of the Western European countries during the post-war period is an illuminating example of how foreign assistance facilitated high rates of investment and saving caused by redistribution of income in favor of the business sector. Although, due to their historical technical base and the established patterns of production and trade, the situation of Western European countries is rather incomparable with those prevailing in most less developed countries, the lesson is not less significant (Rahman, 1984).

In the history of the economic development of nations it is almost impossible to find a single instance where a country did not depend upon external resources at some stage

of its development, irrespective of the forms in which the inflow of such resources took place. The forms of such inflow had been as diverse as plunder, political and economic extortion, capital carried by immigrants, private investment, public borrowing and grants, etc. Now-a-days, the inflow of external resources, variously called external finance, foreign aid, external assistance, foreign capital etc. come in the forms of government loans, grants, project assistance and FDI mainly from the established market economies.

APPEARANCE OF FOREIGN CAPITAL IN GROWTH LITERATURE

Foreign capital plays a dual role in countries that suffer from the two well-known stylized gaps: the saving gap and the trade gap. The former relates to the inadequacy of domestic saving in relation to the required volume of investment for achieving a desired rate of growth. The latter relates to the inadequacy of the required complementary inputs, such as, machinery and capital output, industrial raw materials, technical know-how etc. which is caused by a deficit in the current account balance of payments.

Harrod (1948) and Domar (1957) initially introduced the concept of foreign capital in generating capital stock of the resource poor developing countries in the modern growth economic theory. Harrod-Domar assigned a crucial double role to capital accumulation in the process of economic growth. In the Harrod-Domar model, it is the saving which, in turn, becomes the investment and is the key to economic growth. The critical rate of growth depends upon two factors: the relationship between income and spending on the one hand, and the additional output generated (capital-output ratio) by the initial investment, on the other. Therefore, with the help of foreign capital, an economy can grow at a faster rate than that is permitted by its domestic savings ratio. The Harrod-Domar model has subsequently been refined by a number of developmental economists, but its basic characteristic-that capital is the only factor of production, which explicitly determines economic growth - remains at the fulcrum.

After more than four decades of experience in fostering growth (with the help of external assistance) in developing countries, the view regarding the relationship between capital accumulation and economic development has not changed though it is

now reckoned that there are other complementing factors such as market facilitating public policies, stable macroeconomic and political environment and a versatile human resource base.

The international flow of capital involving borrowing and lending across political borders dates back to the ancient history. Helen Hughes (1979) has provided a historical perspective of such capital flow. She records that the bulk of flows during 1870-1913 were in the form of private investment channeled only from developed countries. Up until the early 1940's, there had hardly been any official capital flows to developing countries. The official flow of capital from developed to developing countries became important in the mid-forties. These official capital flows gradually came to be dominated by aid and loan. The underlying idea was that aid and economic growth are directly related, that is, aid promotes development in the receiving countries. The United Nations itself endorsed this view and actively participated in channeling assistance from resourceful developed nations to resource poor backward nations for the long run self- sustained growth (Bhattacharjee, 1998).

EFFECTS OF FOREIGN CAPITAL ON ECONOMIC GROWTH

The development literatures that investigate the overall effects of foreign capital on the savings and economic growth of developing economies is quite rich. The effects are frequently measured in terms of the impact of inflows of foreign capital on domestic savings and growth rates. The results are however, inconclusive. Neither the theoretical underpinnings nor the empirical evidence is clear-cut on the role of foreign capital in augmenting the domestic savings and growth rates of receiving countries.

In the early 1960s, a group of economists had argued that foreign capital inflows increase national savings and investment and, therefore, such inflows increase the Gross National Products (GNP) of the aid receiving countries (Adelman and Chenery, 1966; Chenery and Strout, 1966; Over, 1971). The findings of this group were, at first, challenged by Haavelmo (1965) who observed that foreign capital inflows have an adverse effect on domestic savings and argued that because of negative effect, foreign capital inflows are likely to have retarding effect on economic growth. Subsequently, on the basis of theoretical arguments and empirical studies, Rahman

(1968), Griffin (1970), and Hazari (1976) have shown that foreign capital has a negative effect on domestic saving. Their arguments center on the psychological hypothesis. According to this hypothesis, an increase in foreign capital inflow causes a relaxation of the government saving efforts and thus causes a reduction of the average saving rate.

Psychological hypothesis is bitterly criticized by Kennedy and Thirlwall (1971), Stewart (1971), and Papanek (1972). They have argued that domestic saving is in part a function of investment opportunities; foreign capital inflow increases investment opportunities irrespective of whatever constraint to growth is dominant and thus causes an increase in domestic saving. In addition, they are also of the opinion that an increase in investment due to foreign capital inflow is expected to increase income that leads to increase of domestic saving. Consequently, expecting a positive relationship between domestic saving and foreign capital inflow is more justified.

Landau (1969) empirically tests the psychological hypothesis in the context of ten Latin American countries. Landau's regression results were mixed. Five countries showed a negative coefficient, although none of them were significantly different from zero; the other five countries showed positive coefficients, two of them being significant. Landau's results thus cast doubt on the validity of a negative impact of foreign capital inflow on domestic saving rates.

Griffin (1970) examines the relationship between foreign capital and domestic growth. With some empirical evidence to support his assertion, Griffin argues that foreign money tends to substitute domestic savings in the developing countries, reduce their saving efforts and thus retard their growth and development.

Heller (1975) investigates the effects of foreign capital on government revenues, consumption and investment of eleven African countries of both British and French colonial heritage. Heller concludes that the source and forms of money are the two important determinants of the effect of foreign money on the public sector of the national economy. His result, however, does not indicate that foreign capital is harmful for economic growth.

Choi and Wasow (1980) have studied the effect of foreign capital on domestic saving behavior in Korea during 1954-1978. They find that ' A dollar of capital inflow ***ceteris paribus*** reduces domestic saving by approximately a quarter '.

FOREIGN CAPITAL AND BANGLADESH ECONOMY

For its marked dependence on foreign money, Bangladesh provides a test case for conducting both theoretical as well as empirical investigation into the behavior of external assistance. External assistance seems to have stabilized roughly at a level of 7-8 percent of the gross domestic product of Bangladesh and finances over 75 percent of the entire public sector investment, including a substantial part of its local currency costs (GOB, 1998). Although conceptually foreign money is granted to finance development programs in developing countries, in Bangladesh the revenue budget can not escape the stigma of dependence. During 1975-1988, for example, 33 percent of the total revenue earnings was collected from customs duties alone (Sobhan et.al 1990).

Most of the empirical studies on the role of foreign capital on domestic saving in Bangladesh economy are inconclusive. Islam (1972), in his descriptive survey for the then East Pakistan infers an inverse relationship between the capital inflows and the rate of domestic savings for the 1950's, but positive results between these two variables for the 1960's.

Alamgir (1974) has found a statistically significant positive relationship between foreign capital inflow and domestic savings for the eleven-year period ranging from 1959-60 to 1969-70. Rahman (1979) using the unified Pakistan's data tests the psychological hypothesis, based on argument that an increase in foreign capital inflow leads to relaxation of the government savings efforts and thus causes a reduction in average domestic savings rate. He reports that foreign capital inflow has an adverse effect on domestic saving.

Rahman (1984) reports that in an import dependent economy like Bangladesh, foreign aid expands the tax base and increases the flexibility of tax structure. Rahman notes

that inflow of foreign capital has facilitated the growth of GNP at a higher real rate through which it contributed to the growth rate of savings.

Employing a two-stage least squares method, which according to him is better since it can also consider the indirect effect, Ahmed (1990) suggests that the government did not relax its saving efforts during 1960-61 to 1979-80 and domestic savings were not substituted by foreign capital inflow. Ahmed (1990) in his dual gap analysis shows that scarcity of foreign exchange was one of the constraints on the economic growth of Bangladesh. Ahmed (1990) examines the effect of foreign capital inflow on growth of output, imports and production structure for the Bangladesh economy. His findings suggest that foreign capital inflow was conducive to economic growth of Bangladesh. It has increased the productive capacity of the economy and facilitated the expansion of the tertiary sector. The increased service from the tertiary sector along with increased imports of raw materials and intermediary goods increased output in the primary and manufacturing sectors. Ahmed concludes that " foreign capital inflow favorably changed the production structure of the Bangladesh economy with resulting changes in the composition of GDP, exports and imports".

Hill (1988) develops twenty-two linear equations, two-stage least squares macroeconomic model of the Bangladesh economy. Her simulation experiment estimates that with a fifty percent reduction in net foreign capital inflows, the real level of national output would drop by approximately 9 percent during 1960-1979 period.

Choudhury (1990) investigates the fiscal impact of foreign capital on the public sector. He explores how foreign capital impacts on taxes, non-tax revenues, government consumption and investment. The study finds positive and statistically significant relationship between foreign money and government's consumption (expenditure on civil administration), its socioeconomic consumption (expenditure on education and health). His model estimates highly significant positive relationship between foreign capital and government revenue, investment, taxes, and public savings.

Contrary to these findings, in a series of studies, Sobhan and his associates (1990) have shown the distortive consequences that foreign money had on the country's development process. Their analyses range from the political economy of external dependence, political leverage exercised by Western donors led by the World Bank, politics of food and famine in Bangladesh, the beneficiaries of foreign aid, sectoral and structural dimensions of the external dependence on annual development programs.

Sobhan and Bhattacharya (1986) have argued that external dependence has served to reinforce a system that has been hostile to the mobilization of domestic resource and the efficient use of productive capabilities. He claims that the process has led to establishing a social class of intermediary bourgeois, who without being productive which they could have been, engage themselves to eternalize the system at the expense of their country's harmonious and independent development.

Sobhan (1990) tests the validity of the proposition that foreign capital inhibits domestic resource mobilization and thus perpetuates external dependence of the country. Their short-run aggregate analysis, using multiple regression method, reveals that foreign money has an overall negative effect on internal resource mobilization.

From this short review of the literature regarding the contribution of foreign capital on the growth of developing countries, three conflicting claims stand out (i) foreign capital inflow positively affects the GDPs of the recipient countries, (ii) foreign capital inflows have adverse effects on national saving, and (iii) the effects of foreign capital inflows on national saving, investment and income are either negligible or indeterminate.

FOREIGN DIRECT INVESTMENT IN DEVELOPMENT DISCOURSE

Inflow of foreign capital generally comprises three forms: (i) official development assistance in the form of grants or loans, (ii) non-concessional credit in the form of food aid, commodity aid, and project assistance, and (iii) all types of private flows especially foreign direct investment (International Finance Corporation, 1997). Available literature indicates that among the three forms of foreign capital, Foreign

Direct Investment (FDI) stimulates significant favorable impact on economic growth of the developing countries compared to the other two forms of capital (Rana, 1990; UNDP, 1998). It has a larger impact on domestic investment. It is also found that far from crowding domestic investment, FDI seems to supplement it (IFC, 1997).

FDI in developing countries has soared over the last ten years, overtaking official finance as a source of external funding for economic development. FDI to developing countries has grown rapidly, especially since the mid 1980s. In 1970-96, these flows grew by 10 percent a year in real term. Real FDI in 1980-89 was 50 percent more than in the previous 10 years, and two-fifth of that in the next 7 years. FDI now averages 1.7 percent of developing countries' GDP. In 1998, developing countries received nearly 40 percent of global FDI (UNCTAD, 1999). The lion's share of the inflows to the developing countries have come to the Asian developing countries, accounting for as much as 70 percent of total such inflows in 1998 (UNCTAD, 1999). Within the developing Asian and Pacific Region, the ASEAN sub-region accounted for over 90 percent of the intra-regional FDI (UNDP, 1998).

FOREIGN DIRECT INVESTMENT: BRIEF HISTORICAL ROUTE

The story of development almost everywhere includes FDI, from the Persian Gulf's oil fields to India's tea plantations and Malaysia's rubber plantations. Early in the twentieth century, a large part of the world's infrastructure was developed through foreign investment, including electric power in Brazil and telecommunications in Spain. British firms invested in consumer goods manufacturing abroad from an early date. German chemical companies were expanding outside German before World War I as were U.S auto manufacturers. Swedish, Swiss, French, and Japanese firms had established foreign subsidiaries before 1914 (IFC, 1997). These investments were based on new technologies and management and organizational practices. By 1914, the world stock of FDI was estimated at $15 billion, about one third of all investment at that time. The United Kingdom was then the largest source of investment, followed by the United States and Germany (UNCTAD, 1996).

The stock of world FDI had risen to $66 billion by 1938, with U.K. firms still the largest investors. More than half of this investment had been made in developing

countries, mainly in Latin America and Asia. Much of it was in agriculture and mining, but a significant part was also in infrastructure. These patterns shifted after World War II as U.S. firms became the main source of FDI, and manufacturing investment became most prevalent. However, because of inward-oriented development strategy pursued by most of the developing countries during the 1950s and 1960s, the flow of FDI across the globe had been deterred. Production for the domestic markets was encouraged over export, and imports were discouraged or restricted. Governments played an active role in regulating and directing private business. Critics of FDI at that time were concerned about possible adverse consequences such as creation of economic dependency, political interference, and weakening of domestic companies.

The creation of domestic markets protected from imports gave foreign producers an incentive to shift production into the country, instead of trying to export to it. Thus, FDI was concentrated in import-substitution industries through a process known as tariff jumping (Borenzstein et. al. 1995). This incentive was strongest in countries with large internal markets such as Brazil and Mexico, which attracted large volumes of FDI to industries protected from imports. FDI also continued unabated to countries that were rich in natural resources and locations that gave products preferential access to export markets. Because of the inward-oriented development strategy, FDI to developing countries stagnated in the 1970s (IFC, 1997).

This stagnation continued into the first half of the 1980s, as developing countries struggled to restore economic stability in the face of falling commodity prices, recession in industrial countries, and high global interest rates that together triggered a debt crisis. Furthermore, the consequences of inward-looking, state-oriented economic policies became apparent in low investment productivity and public enterprises' mounting losses. Insulation from the global economy led to a collapse in exports and massive balance of payment deficits in many countries.

In response to deep-seated balance of payments and fiscal deficits, many developing countries embarked on SAP designed to reorient their economies toward private sector production, international trade, and competitiveness. In response to this change,

FDI flows to developing countries began to increase in the second half of the 1980s. These flows were more focused than in the past on export oriented industries, attracted by low operating costs and market links.

Liberalization of FDI policies by developing countries continues into the 1990s. Indeed, it would be difficult to find a developing country that has not enacted more liberal investment laws in the 1990s. FDI flows signify a long-term commitment on the part of the investors and are thus far more stable than other flows. Moreover, once established on the ground, they can generate the interest of other foreign investors, such as suppliers of components or of supporting services, to join the pioneers and start virtuous circle of foreign investor interest (United Nations, 1997). Remarkable change in the FDI share of China in the late 1980s is a glaring example. China received some $167 billion which was, on average, 4.8 percent of China's GDP. The huge influx of FDI has significantly contributed to the spectacular GDP growth rate (11%) in China (IFC, 1997).

Taking FDI flows as a ratio of GDP, Singapore and Malaysia stand out, with FDI amounting to 10 and 8 percent of these countries' GDP respectively. Similarly, the ratio of FDI to gross fixed capital formation is the highest in Singapore and Malaysia (well over one quarter) while the average for East and South-East Asia is around 5 to 6 percent (United Nations, 1997)

Overall, during 1983-1990, FDI is estimated to have grown by an unprecedented nominal rate of nearly 38 percent per annum which was three times the corresponding growth rates of exports and four times that of world output (UNCTAD, 1999). This change has been brought about by a combination of a sustained increase in world output, a spectacular growth in the service sector, a sharp rise in technological networking or "technoglobalism" . So dramatic has been this change that according to a World Bank study, " a new FDI era has arrived – an era marked by a greater recognition of the benefits of FDI"(Brewer, 1991).

The new FDI era represents the final stage of the three interrelated but analytically separable phases of growing inter-national linkages among countries since the end of

the Second World War (Ostry, 1992). The first phase, characterized as the golden age of the 1950s and 1960s, was driven by trade, resulting from the dismantling of protectionist barriers in successive GATT rounds. The second phase, characterized as financial integration, was initiated by three massive commodity and oil shocks in the world over the 1970s. The present third phase beginning in the early 1980s is called globalization and is led by FDI waves. Liberalization and privatization are the two most important policy trends of the 1990s as part of broad-based attempts to attract foreign investors (Reza, 1995).

JUSTIFICATION OF THE STUDY

As noted earlier, there has been a dramatic shift in the attitudes of developing countries, especially in the Asian nations towards FDI in the last two decades. Although the major share of total FDI flows to developing countries has come to Asia, the South Asian countries have been only marginal recipients of such flows. Six countries of South Asia (India, Pakistan, Srilanka, Bangladesh, Nepal, and Maldives) together received only $538 million in FDI flows in 1986 compared to $5575 received by Singapore alone and $3487 million by China alone (UNCTAD, 1998). The meager inflows of FDI in the 1970s and 1980s to South Asia were the result of long entrenched inward looking development strategies and overcautiousness towards FDI.

The South Asian countries have recently changed their attitudes towards FDI. They are now welcoming and seeking higher inflows of FDI as part of their newly launched economic reforms based on market driven, private sector led and globally more open national economies. It is by now widely recognized by the policy planners of the South Asian countries including Bangladesh that FDI benefits both investing (home) countries and recipient (host) countries.

Bangladesh emerged as an independent and sovereign state on 16 December, 1971. The economy was in a ravaged condition at that time following the nine-month long liberation war against Pakistan. To ensure recovery and reconstruction and also to achieve the relatively longer term development goals, the country started on the course of planned development almost right from the beginning.

In Bangladesh, resource endowment in the conventional sense is meager. Unfortunately, the nation has experienced unprecedented economic and political exploitations by the British and the Pakistanis for more than two hundred years. Since its freedom from sub-colonial states to sovereign nation in 1971, economy failed as part of past legacies to generate sufficient domestic savings. For instance, the domestic saving rate has remained a negative value (-1.9% to GDP) over the country's First Five Year Plan (1972-76) (Reza et. al., 1987) and on an average of about 6 percent during 1977-1997 (GOB, 1998). The turn-around from the initial commitment for socialist transformation of the economy came with a clearly defined policy for encouraging the private sector in 1976, which culminated with the announcement of the New Industrial Policy in June 1982, later revised in 1986, and made further market-friendly in 1991.

The policy changes provided, included among others, liberalized investment and trade procedures, attractive incentive package for local and foreign investment, financial sector reforms, and large-scale privatization of industries. As a result of these endeavors, the economy has been successfully stabilized showing some remarkable improvement in the macroeconomics indicators between 1985 and 1998. For example, fiscal deficit has been lowered from over 8 percent of GDP in the early 1980s to 5 percent, the inflation has been squashed, according to the Central Bank, the current account deficit has virtually disappeared and the foreign exchange reserves have increased to a comfortable levels at $3 billion in 1998 which is equivalent to about 7 months' import bills (GOB, 1999).

In spite of some changes in the economy of Bangladesh over years, the development challenges remain formidable. The economic development of Bangladesh has been constrained, from the very inception of the country, by the so-called two- gap vintage relating both to shortages of domestic savings and foreign exchange resources. With extremely low level of savings, a country like ours cannot industrially be developed without the inflow of FDI. Available information witnessed that Bangladesh started attracting FDI immediately after the change in state power and policy in 1975. The volume of FDI inflow has started to accelerate since the mid-1980s. Foreign investors have been attracted to the manufacturing sector by its low wages and, in particular, its

unused quota for exporting textiles and apparel to the markets of the European Union and the United States. FDI into that industry accounted for nearly one fifth of approved investment inflows in 1998, excluding export- processing zones. As a result, ready-made garments account for over 76 percent of the country's export earning in 2000. FDI in Bangladesh has also been important in the food- processing, electric machinery, chemical and natural resource extraction sector.

Despite growing importance of FDI inflows to Bangladesh, it is ironically one of the less researched areas in the economic literature on the Bangladesh economy. Although, a few scholars have dealt with the issue of FDI ***en passant*** in various research papers and mimeographs, but these are more concerned with a general analysis of the role of FDI and Transnational Corporations in the economy of Bangladesh. Studies, which have given undivided and exhaustive attention to the topic of FDI, have relatively been few. The main objective of this study is to fill this gap by generating and evaluating extensive data in an integrated form relating to FDI in Bangladesh.

OBJECTIVES OF THE STUDY

The literature on FDI is replete with heated and often subjective debates regarding the impact, and hence, desirability of foreign capital inflow into developing countries. While regarded as an engine of growth by some one, others have dubbed FDI as a suction pump for exploiting the peripheral, poor countries by the rich, industrialized center.

The oft-cited reasons for welcoming FDI are such expected gains as capital augmentation, transfer of technology, export promotion, greater enterprise, improved management and marketing capabilities and so on. Entry by foreign firms can also increase competition in domestic markets, reduce monopoly profits, and stimulate quality upgradation of products and services by all firms in the sector.

This study has concentrated on investigating the nature and characteristics of FDI in Bangladesh. The specific objectives of the study are:

(1) to assess the trend of FDI in Bangladesh;

(2) to evaluate the performance of FDI in Bangladesh ;and

(3) to assess the determinants of FDI with respect to conventional macro-economic indicators.

METHODOLOGY OF THE STUDY

(a) DEFINITIONS, DESCRIPTIONS AND DISCREPANCIES IN THE DATA

The two main definitions of FDI are contained in the Balance of Payment Manual (International Monetary Fund, Washington, D.C., 1977) and the Definition of Foreign Direct Investment (Organization for Economic Co-operation and Development, Paris, 1983), both of which are currently under revision.

According to the Balance of Payments Manual, foreign direct investment refers to investment made to acquire lasting interest in enterprises operating outside of the economy of the investor. Further, in cases of FDI, the investor's purpose is to gain an effective voice in the management of the enterprise. The foreign entity or group of associated entities that makes the investment is termed the "direct investor". The unincorporated or incorporated enterprise - a branch or subsidiary, respectively, in which direct investment is made - is referred to as a "direct investment enterprise". Some degree of equity ownership is almost always considered to be associated with an effective voice in the management of an enterprise; however, IMF does not specify an exact percentage of equity ownership that qualifies an investor as a foreign direct investor.

The benchmark definition of the Organization for Economic Co-operation and Development (OECD) is more explicit than the definition of IMF in that it specifies a percentage of ownership as a threshold for FDI. It defines a direct investment enterprise as an incorporated or unincorporated enterprise in which a single foreign investor either owns 10 per cent or more of the ordinary shares or voting power of an enterprise (unless it can be proved that the 10 per cent ownership does not allow the investor an effective voice in the management) or owns less than 10 per cent of the

ordinary shares or voting power of an enterprise, yet still maintains an effective voice in management. An effective voice in the management only implies that direct investors are able to influence the management of an enterprise and does not imply that they have absolute control. The most important characteristic of FDI, which distinguishes it from portfolio investment, is that it is undertaken with the intention of exercising control over the enterprise.

There is a notorious lack of comparability of the FDI data of different countries. This lack of comparability usually results in discrepancies between total outflows and total inflows or between outward stocks and inward stocks. There are three main causes for the lack of comparability and discrepancies. First, countries differ in their definitions of FDI, since most depart in one way or another from the conventions recommended by IMF or OECD. Second, countries differ in their methods of data collection; a principal problem is the difficulty of identifying the ultimate beneficiary as opposed to the immediate beneficiary of FDI. Third, corporate accounting practices and valuation methods differ between countries. Each of those groups of issues is discussed in turn below.

(b)COMPONENTS OF FOREIGN DIRECT INVESTMENT

(i) The threshold equity ownership

As stated above the components of FDI are equity capital, reinvested earnings and inter-company loans. As countries do not always collect data for each of these components, reported data on FDI are not comparable across countries. In particular, data on reinvested earnings, the collection of which depends on company surveys, are often unreported by developing countries.

(ii) The threshold equity ownership

Countries differ in the threshold value for foreign equity ownership, which they take as evidence of a direct investment relationship. This is the level of participation at or above which the direct investor is normally regarded as having an effective say in the management of the enterprise involved. The threshold value usually chosen ranges between 10 and 50 per cent and in

recent years it has tended to move towards the lower end of this range, owing to the fact that even a small shareholding may allow an effective voice in management. Some countries do not specify a threshold point, but rely entirely on other evidence, including companies own assessments as to whether the investing company has an effective voice in the foreign firm in which it has an equity stake, owing to the large proportion of FDI which is directed to majority-owned subsidiaries and branches.

(iii) Defining a controlling interest and treatment of non-equity forms of investment

Other than having an equity stake in an enterprise, there are many other ways in which foreign investors may acquire an effective voice. These include subcontracting, management contracts, turnkey arrangements, franchising, leasing, licensing and production sharing. A franchisee (a firm to which business is subcontracted) or a company, which sells most of its production to a foreign TNC, may be just as effectively controlled as an affiliate. Although data on control by a foreign firm through means other than an equity stake are not usually collected, some countries have begun to contemplate doing so. For example, OECD treats financial leases between direct investors and their branches, subsidiaries or associates as if they were conventional loans; such relationships will therefore be included in its revised definition of FDI.

(c) DEFINITION AND SOURCES OF DATA

The Bangladesh Bank and the Board Investment report data on FDI in Bangladesh. In the case of the Bangladesh Bank data, the distinction between foreign direct and portfolio investment is that 25 per cent or more of the voting stock must be held by foreign nationals in order for an enterprise to be considered a recipient of FDI. FDI inflows consist of cash capital, capital equipment and reinvested earnings. Cash capital is often supplemented physically by capital equipment imported into the country instead of. Or in partial payment into Bangladesh on investment licenses, for which no payment has been made from the country's foreign exchange reserves or from workers' remittances. Reinvested earnings reflect (i) the value of imports on investment licenses marked "valid for remittance" out of retained profits for firms

incorporated or registered abroad, but functioning in Bangladesh, (ii) bonus shares issued in favour of foreigners by enterprises incorporated and operating in Bangladesh with foreign equity participation.

There are two types of FDI enterprises/projects accounted for in the data: (i) those incorporated or registered abroad, but having operations in Bangladesh: and (ii) those incorporated in Bangladesh having foreign equity participation and functioning in Bangladesh. Partnerships operating in Bangladesh are excluded.

FDI inward stock data reflect the net debtor or creditor position of foreign companies in Bangladesh and of Bangladeshi joint stock companies having FDI participation. The net debtor or creditor position is defined as the difference between liabilities and assets.

The Statistics Department of the Bangladesh Bank conducts surveys on FDI inflows and inward stock, in order to supplement the balance-of-payment estimates of private foreign investment. Balance-of-payments data are based on information available from the records of the Exchange Control Department of the Bangladesh Bank and are neither systematically collected nor adequate in their coverage. Data collected through the Exchange Control Department refer only to cash capital inflows because of the availability of such data in the banking system, and do not cover capital equipment brought in without any payment from the country's own foreign exchange reserves or reinvested earnings. The aim of the annual surveys undertaken by the Statistic Department of the Bangladesh Bank is to bridge that gap. As an indication of the coverage of those surveys, out of 108 FDI enterprises identified in 1986, 97 submitted their financial returns and were included in the survey.

The Board of Investment, which has functioned since 1 January 1989, is responsible for making decisions on all matters related to the implementation of foreign investment projects and acts as a "one-stop" service to foreign investors. The Board of Investment collects data on proposed foreign equity in joint ventures and on the total amount of investment in approved projects, by country of origin and by industry of destination.

Since 1983, the International Monetary Fund has reported data on FDI inflows, defined as net changes in direct investment, in Bangladesh. Until 1982, FDI inflows were reported under the category "other long-term liabilities of sectors", in the capital account, along with portfolio investments. This study utilizes all the above sources of data after making necessary scrutiny.

(d) Statistical Tools Used

The study is prepared based mainly on published and unpublished data. In evaluating the trends and performance of FDI in Bangladesh, various descriptive statistical tools have been applied. In determining the determinants of FDI in Bangladesh, multiple regression analysis was carried out to test the hypotheses. The trend of FDI has been estimated by using a semi-log regression model. Details of the statistical techniques that have been used are outlined chapter wise. The study covers twenty-two years FDI data spanning from 1977 to 1999.

Organization of the Study

The study is consisted of nine chapters. Following from the introductory Chapter, Chapter two gives a brief account of Bangladesh economy between 1972 and 1999. Chapter three provides theoretical and empirical foundation of the study. Chapter three is divided into two sections. Section one examines the theoretical underpinnings of FDI and section two identifies the empirical determinants of FDI in some selected countries. Chapter four evaluates the government policies toward FDI. Chapter five assesses the trend, structure and performance of FDI in Bangladesh over a period of 22 years spanning from 1977 to 1999. Chapter six assesses the performance of Export Processing Zones in attracting FDI in Bangladesh. Determinants of FDI on the economy of Bangladesh have been investigated in Chapter seven. Chapter eight discusses and compares FDI policies of some selected Asian countries including Bangladesh. Chapter nine concludes the study.

CHAPTER-II

CHANGES IN THE ECONOMY OF BANGLADESH, 1972-1999

The literature suggests that the FDI of a country is linked with the economic environment of the host country. The development strategies and macro-organizational policies of the host-country government influence this economic environment in turn (Dunning, 1993). This chapter, therefore, examines the macroeconomic changes in Bangladesh economy between the period 1972 -1999.

Bangladesh started its journey towards development immediately after independence when the country's first Annual Development Plan was formulated in 1972 with the objectives of relief and reconstruction. A Second Annual Plan was drafted in 1973 which, continued the tasks of recovery efforts but set the self - sufficiency in food as the principal development target.

In late 1973, country's First Five-Year Plan (FFYP) for 1973-78 was announced. In the formulation of FFYP, several causes of slow growth in agriculture were identified. These are lack of suitable development strategy, absence of appropriate technology, inadequate credit facilities and absence of proper institutional facilities. The Plan which incorporated twelve objectives emphasized the broad goals of national self-reliance, increased production, employment creation, income distribution, food self - sufficiency and an industrial policy of import substitution and export promotion. The first plan was based on an input-output model formulated by Planning Commission economists (Stepanek, 1979).

The FFYP undertook rural and agricultural development, poverty alleviation as one of the major objectives of the plan. For this purpose, it envisaged redesigning and restructuring existing institutions, more participation and utilization of resources through local plan. Therefore, the plan identify the weaknesses of existing institutional system as "one imposed from the top, non-representative in character,

and a channel for distribution and utilization resources from outside without adequate emphasis on mobilization of resources within" (GOB, 1973, 88). During this time cooperatives had been taken as the major vehicle for organizing rural development at the grassroots and ultimately for poverty alleviation.

To achieve the target of increasing agricultural production, the plan aimed at replacing the traditional agriculture by a modern one based on increased cultivation of High Yielding Varieties (HYV) through exploiting all available opportunities and by gradual structural transformation (Hossain, 1991). During this time, poverty alleviation remained the major thrust of government development efforts. The FFYP was followed by a Two-Year Development Plan (1978-80) which mostly carried out the incomplete tasks of FFYP, and also filling the shortfall of resource availability during the implementation of the previous plan. The Second Five-Year Plan (SFYP 1980-85) took a more realistic approach and deviated from the previous rhetoric of socialism and emphasized the growth of income and employed in the poverty alleviation programs. During the SFYP, local institutions such as cooperatives, ***Union Parishads*** were further strengthened to accelerate poverty alleviation. The main objective of agriculture was the attainment of food self-sufficiency through a rapid expansion of water-seed-fertilizer technology, land reform and institutional reform at the grassroots level.

During the preparation of Third Five-Year Plan (TFYP 1985-90), fresh attempts were made to integrate the productive sectors of the economy with its infrastructure development as well as the rural development programs. An applied general equilibrium model was formulated in this regard for better resource allocation and greater efficiency. Poverty alleviation, increase in agricultural productivity, attaining self-sufficiency in food production, expansion of employment opportunities remained the major objectives of TFYP. Unlike the previous plans, the attainment of these objectives was tied to modern HYV technology, which was expected to absorb 40% of additional labor force. The withdrawal of agricultural subsidies and credit restrictions have led to lower purchasing power of farmers (Hossain, 1991), which has significant impact on the growth of the economy.

However, one noticeable development during the TFYP plan phase was that interventionist role of government and the role of public sector came under increasing attack from donor and international organizations. They emphasized less government control, denationalization and also advocated for greater role of market forces. This ultimately came to be known as Structural Adjustment Reform (SAR) which was expected to open the economy to more internal and external competition. The Fourth Five-Year Plan (1990-95) and the Fifth Five-Year Plan (1995-2000) were formulated in the line of the so-called Structural Adjustment Program (SAP).

In spite of these modest achievement in certain areas, Bangladesh still ranks as one of the poorest countries in the world. A large number of people, both in the urban and rural areas, still live in abject poverty and "progress in poverty reduction is one of the slowest in the world" (Rahman, 1994 pp3-11). We may identify several constraints that act as hindrance to socio-economic development of Bangladesh (Box-1).

Box 1

Major Problems of Development in Bangladesh

A. Structural

- → General poverty.
- → High level of illiteracy.
- → High growth of population.
- → Limited availability of land.
- → System of land tenure.
- → Unequal distribution of wealth.
- → Lack of employment opportunities.
- → Bureaucratic and urban bias in development.

B. Socio-cultural and Economic

- → Family and kinship pattern.
- → Religious beliefs and values.
- → Traditional values, norms and worldviews.
- → Low level of achievement orientation.
- → Higher propensity to consume.
- → Lack of awareness about health.
- → Ethnic problems.

C. Economic and Environmental

- → Lack of capital.
- → Low capital formation.
- → High capital - output ratio.
- → High rate of population growth.
- → Low land - man ratio.
- → Rural - urban migration.
- → Declining ecological reserves.
- → Deforestation.
- → Over-exploitation of common property resources.
- → High frequency of natural disasters.
- → Vulnerability and insecurity.

INDUSTRIALIZATION IN BANGLADESH: POLICIES AND PERFORMANCE

There is, perhaps, very little disagreement on the notion that rapid industrialization is the key to sustained economic growth and development. Going with the premise, of course, does not imply a rejection of the role that agricultural sector has to play to tune economic development. In fact, historical records show that industrial development almost always took place in tandem with agricultural development. Industrial growth can hardly bulge keeping agricultural growth at bay (Lewis, 1954).

From the very inception of Bangladesh till day, the premises mentioned above were given due cognizance in plan documents and policy papers. Successive political regimes of Bangladesh orchestrated a plethora of programs towards a simultaneous development of the two sectors. However, in the realm of industrial development, disagreements always seem to have hovered around two issues. First, should the private or the public sector constitute the arbor of industrialization process in Bangladesh? Second, whether the Import Substitution (IS) or Export Oriented (EO) strategy should spearhead in the whole industrial development process? Divergent views on these scores by successive regimes developed and the consequent policy shifts seemingly injected a number of convulsions in the nascent industrial sector of Bangladesh. The convulsions, again, had impacts on the subsequent nature and degree of industrial development. It is, therefore, important that a brief resume of the various policies and programs by successive regimes is in order for a proper evaluation of the performance of the industrial sector in Bangladesh.

EVALUATION OF INDUSTRIAL POLICIES

For a better understanding of the policies pursued by different regimes and the political economy thereof, an attempt was made to present the policies in phases keeping in mind, of course, that policies have continuities and spill-over effects across regimes. Again, attempts were also made to highlight few of the major episodes that are believed to have affected the fabrics of industrial growth and structure.

NATIONALIZATION PHASE (1971-75)

Nationalization of industries to install a public sector - led industrial development became the guiding principle of industrial policy stances in the immediate post-independence era. The policy of nationalization (vide the Presidential Order No. 27 of 1972) in the post-independence period appeared sensational and sensitive but perhaps not surprising. It simply sounded a stage rehearsal of the commitments made in the election manifesto of ***Awami League*** in 1970. Radical pressures within the party in power to lean to the left, the world wide geo-political predicaments, existence of a number of abandoned industrial units left behind by non-Bengali owners are reported to have fuelled the nationalization spree (Bayes et. al, 1998).

Following nationalization, all abandoned medium and large size industrial properties were brought under strict state controls. Again, Bengali owned units with fixed assets exceeding Tk. 15 million were also placed under public sector. Small and cottage industries as well as foreign enterprises, however, were allowed to remain outside the purview of government management. According to available documents, a total of 725 industrial units with 92 percent of the total industrial fixed assets in the modern manufacturing sector were placed under 10 public corporations, thus, letting 8 percent of fixed assets to stay in the private sector, compared to 53 units and 34 percent of fixed assets held by the state sector in 1969-70. On the other hand, the first industrial policy of Bangladesh (declared in January, 1973) limited the permissible private investment to Tk. 2.5 million, with an allowance for further reinvestment through profits (Bhattacharya ,1992; Zohir ,1995).

The industrial policy pronouncements of the immediate post independence period, arguably, inserted a major convulsion as far as industrialization in this part of the world was concerned. The steps taken than, in terms of ownership of industrial assets as well as private investment limits, seemingly marked as 'U-turn' when compared with the immediate past policies of a vastly privatized industrial sector. However, there seemed to be no fundamental department in terms or policies determining the degree of openness of the economy. The same inward looking IS strategy was followed. The then industrial incentive packages were geared to favor IS over EO industries through an avalanche of discriminatory devices, viz., an over-valued

exchange rate (anchored to a fixed exchange rate systems), higher levels of tariff and non-tariff barriers, import licensing system, foreign exchange rationing, etc. Needless to mention, perhaps, that all these policy instruments, allegedly, went to shelter IS industries and debilitates the export industries (Bayes et. al, 1998).

The maintenance of ***status quo*** with respect to IS strategy could be adduced to the following three principal factors: (i) it was embraced by a host of other countries of the world during the time Bangladesh emerged as an independent state, (ii) there was pervasive presence of IS industries in the economy that needed to be highly protected -- a legacy of the pre-independence era and (iii) the spectre of "export pessimism" shook many of the then LDCs including Bangladesh.

Literatures on the nationalization of industrial sector in Bangladesh are available. The performance of the nationalized industrial sector in the immediate post-independence period came under heavy scrutiny. Of course, as some had argued, such an evaluation may not sound meritorious in the wake of a very short span of time that nationalization pervaded the industrial sector. However, a few studies observed that there was sustained growth in the output of nationalized sector on aggregate basis during 1972-75. Even the index of production during that time is reported to have surpassed the 1969-70 production figures. The same studies, of course, acknowledged the significant deficiencies of the nationalized sector and adduced them to non-adherence to many of the recommendations but forwarded at that time by the Planning Commission (Sobhan, 1990).

Close at heel, critics of nationalization were abounding. They flayed the philosophy of socialism and nationalization that swept early Bangladesh. Suffice it to air, perhaps, the general notion that the nationalized industrial sector miserably failed to become the vanguard of a rapid industrial development in Bangladesh. The apparent failures are said to have sprang, ***inter alia***, from the following principal impediments: (i) lack of a political commitment on the part of the then rulers to pursue with a socialistic framework of industrialization in right earnest, (ii) absence of autonomy for the nationalized sectors, (iii) managerial deficiencies arising from the vacuum created by the department of the non-Bengali owners (and also by the overthrow of Bengali

owners), and (iv) politicization of management structure of the nationalized units without much credence having been given to their proper management on a commercial footing, etc (Bayes et. al ,1998).

Private investments at the same time (from home and abroad) tended to flinch. The factors that, allegedly, cramped private investments were as follows:(a) private investment ceiling at Tk. 2.5 million appeared insignificant, especially, in the wake of turgescent inflationary trends, (b) there was absence of an incentive structure to promote private investment, (c) unfriendly law and order situation, fuelled by an outdated legal system, apparently detracted interests in new ventures, (d) underdeveloped infra-structure hindered smooth flow of inputs and outputs, and (e) fear of further nationalization continued to haunt potential investors (Sobhan,1990).

Such a bleak lurking on the industrial horizon confounded the then politicians, planners and policy makers. To minimize the rots, a number of steps were taken up by the then government, mostly, to lure private investors: (a) enhancement of the investment ceiling from Tk. 2.5 million to Tk. 30 million (and later to Tk. 100 million), (b) provisions for additional fiscal and monetary incentives to allow more corridors to the private sector, (c) enhancement of a moratorium for nationalization for up to 15 years, (d) provisions for tax holidays for less-developed areas, (e) devaluation of currency by a substantial margin etc. It was expected that proper implementation of these policy change would help invigorate the somnolent private sector (Bayes et. al, 1998).

The immediate post-independence industrial policies, by and large, aimed at (i) a public sector-led industrial development, (ii) a gradual opening of spaces for the private sector so that private investments could duly flock in and (iii) promotion of IS industries.

DENATIONALIZATION PHASE (1975-82)

The violent overthrow of the ***Awami League*** government- the government that nourished and nurtured nationalization through thick and thin - culminated the end of a very short - lived nationalization episode. The subsequent industrial policy shifts to

the "right", right or wrong, marked a radical departure from the immediate past and, possibly, reflected the emerging global scenario of that period. The policy changes apparently evoked a second convulsion in the industrial sector within a short span of four years only.

Major changes of that time were as follows: (a) elimination of ceiling on private investment, (b) relaxation of investment sanctioning procedures, (c) amendment of the constitution to allow denationalization, (d) reviving the stock market, (e) shifting from the fixed rate system of the 1970s to a 'managed' system of floating exchange rate, (e) introduction of a number of export promotion measures, etc. The then thrust of policies lay in the development of a private sector-led growth. The period witnessed large-scale denationalization of industrial enterprises, and private sector investment began to pick up with liberal credit policies and generous lending by commercial banks and Development Financial Institutions (DFIs), ***ipso facto***. A few steps were also taken to boost up the export sector (Bayes, 1990).

It is, however, alleged that the reforms ushered since the late 1970 were constrained by limited scope and slow pace. Further, it is also alleged that privatization at that time took place with much fervor and in great haste. In the name of denationalization and privatization, not only enterprises were sold at knockdown prices, but they were also sold to those with very little entrepreneurial background. The newly established private interest groups, allegedly, enjoyed debt relief and new loans with the help of unproductive and rent-seeking mandarins and clientalist power brokers. In some cases, such transfers of industrial units were driven more by political interests rather than being drawn by economic rationale (Bayes, 1990; Rahman, 1990). Liberal credit policies were, allegedly, mis-utilized and, on occasions, misappropriated. It is, of course, true that some of the disinvested units had to swallow a few disadvantageous legacies, such as large and inefficient labor force and wage policy, inappropriate working environment, while having been denied of the advantages that those units reaped at the time of their public ownership.

By and large, the industrial scenario was gripped by ***adhocism***, ambivalence and devoid of any vision for industrial development. Despite all the changes towards

deregulation and denationalization, the industrial regime remained mostly inward looking, breast-fed by an arsenal of protective devices of earlier periods. The levels of effective assistance as enjoyed by IS and EO industries at the period tend to bear out the fact that Bangladesh had proceeded very little to expose her industries to the outside world.

STRUCTURAL ADJUSTMENT PHASE (1982-90)

The period witnessed the advent of SAPs in Bangladesh. The purpose of SAP was to revamp the economy by removing various price and non-price distortions, thus, allowing resource shifts from non-tradable to tradable sectors. However, the "watershed" in the history of Bangladesh's industrial policy making was marked by the New Industrial Policy 1982 (NIP, 1982). The NIP had to carry over a number of the objectives from the earlier ones. The principal objectives of the NIP, as documented, were to: (i) emphasize export oriented growth which necessitated substantial changes in the regime of trade and industrial incentive structure with prominence placed on export diversification and import liberalization, (ii) assign the private sector the pivotal role to play in rapid industrialization of the country, (iii) down-size the role of the public sector to a substantial extent by specifying its areas of existence to a limited number of restricted areas, (iv) rationalize the tariff structure and pursue appropriate fiscal measures (GOB, 1986).

To facilitate the fulfillment of the above objectives, large-scale denationalization continued to take place. According to a World Bank Report, Bangladesh carried out one of the largest denationalization in the world by transferring as many as 57 enterprises belonging to the jute and textile sectors within one year (World Bank, 1989; Zohir, 1995). To arrest declining share of exports to GDP, the government instituted new incentive scheme such as Duty Drawback system, system of Export Performance Benefit (XPB), etc. As far as import liberalization was concerned, major thrusts were assigned on simplification and rationalization of tariff structure (Bayes et.al, 1995).

The Revised Industrial Policy of 1986 (RIP, 1986) just followed the earlier moves towards deregulation and privatization with more teeth on the on-going SAP. More

export incentive instruments were made available to the exporters, more deregulation proceeded and the number of items on the "negative" list was progressively reduced to pave ways for further import deregulation.

TRADE LIBERALIZATION PHASE (1991-95)

The industrial policy 1991 could be marked as another "watershed" in the history of Bangladesh's industrial processes. In items of philosophical underpinning, it appeared to be of little difference with its forerunners, but in terms of depth and width some discernible differences could be noticed. The whole industrial policy was premised on the philosophy of a market-based competitive economy. A number of relatively more positive and biting policy initiatives were undertaken to lure foreign and domestic investors, e.g. elimination of concessionary interest rates and special credit facilities, deletion of any requirement of permission to set up industries, removal of restrictive provisions for equity participation by foreigners, etc. (Farid, 1992).

The most perceptible changes that the policy seems to have injected are in the arena of foreign exchange and trade regimes. The changes were, apparently, consistent with a free market, neo-classical paradigm and within its fold, with an outward looking, export-led growth strategy. Besides, having been hooked on to a more flexible exchange rate system, in October 1993, Taka was made convertible on current account. There was expeditious move towards liberalizing the foreign trade sector through rationalization of the tariff structure and reduction of tariff and non-tariff barriers. The early 1990s experienced the most pro-active phase of trade liberalization. For example, by 1994 the share of free import items rose to 94% of all Harmonized System Code line items, only 0.4% remained banned.

A PROFILE OF THE INDUSTRIAL SECTOR

The manufacturing sector of Bangladesh is small. This sector is reported to generate less than one-tenth of total employment in the economy, 11-12 percent of GDP and about one-tenth of aggregate investment. However, few of the structural

characteristics of the manufacturing sector, given below, should give a purview of the impact of policy shifts that spanned over a period of two decades or so.

Dualistic Structure

Even after 30 years of its existence, the dualistic structure of the manufacturing sector of Bangladesh is sharply in evidence. A little over half of the Manufacturing Value Added (MVA) seems to originate from the modern large industries (with employment level 10+). This compares with only 17 percent MVA contributed by the traditional cottage industries. In terms of employment, however, the situation is just the reverse. The former accounts for only 13 percent of manufacturing employment as compared to about two-third by the latter. The difference in terms of generation of MVA and employment, as between the modern large and the traditional small, is reported to have sharpened over the last two decades or so. The trend perhaps implies that the dualistic feature of the manufacturing sector intensified, instead of easing, during the last two decades or so (Bakht, 1993; Bhattacharya, 1992).

Narrow Base of Manufacturing Sector

The base of the manufacturing sector seems to be no scope for a comfortable feeling either. Half of the employment and MVA of large industries are contributed by only 7 percent of enterprises in that group implying a narrow base and a skewed size distribution. These "lucky" 4-digit industries are, for example, textiles (jute and cotton), fertilizer, petroleum refinery, allopathic medicine, etc. Narrow base also grips the small industry sub-sector with only textile, food processing and metal products sharing bulk of employment and MVA. However, the size distribution is less skewed in this category. The cottage industry is relatively more diversified (Bakht, 1993).

Share in Employment

According to the 1973-74 Labor Force Survey, only 5 percent of total labor force were employed in the industrial sector. The share almost doubled (10 percent) in the mid- 1990s. However, the incremental employment in the industrial sector should be interpreted with a little bit of caution. It is because: (i) successive LFS embodied extended coverage, (ii) a large slice of the incremental labor force originated from the

informal, unorganized sector and (iii) rise in employment in the face of a stagnant share to country's GDP, arguably, signals the fall in labor productivity (Bhattacharya, 1992).

The export-led growth that has been espoused and fanned by various supportive steps, does not seem to have made any substantial dent in terms of the share of the export sector to GDP, employment generation or MVA. The top five EO industries account for only 12 percent of organized labor force in the industrial sector and only 17 percent of MVA. However, the surge in the growth of the Ready-Made Garments (RMG) units contributed in eking out a substantial amount of foreign exchange earnings. In fact, from as small as 1 percent of total export earnings of the early 1970s, the share of RMG shot up to about 76 percent of total export earnings in 2000. The sector is, however, constrained by the lack of any development on its backward integration in the economy.

Share in GDP

The share it contributes usually measures the size of an industrial sector in the economy to GDP. Looking from this angle, the share of the industrial sector to GDP averaged 16.5 percent during 1973-80 period with manufacturing holding a share of 12 percent. Preliminary estimates made by available reports place the share of the recent past at 18.1 percent and 10.4 percent, respectively. The most disconcerting episode is that while the industry sector's share to GDP went up marginally over the period of three decades or so, the share of the manufacturing to GDP, in fact, had fallen during the same period.

Growth Rate

Between FY 1973-80, the growth rate of the industry sector as a whole averaged 7.9 percent which dipped to an average growth rate of 5 percent during the 1980s and picked up a little over 7 percent in the early 1990s. The manufacturing sector, on the other hand, grew at an average rate of 7.8 percent during FY 73 - 80 which nose dived to average only 3.2 percent during FY 81-99. However, the sector convalesces in early 1990s and grew at an average rate of 8 percent. The share of GDP and the

growth rate for large, medium and small industries in Bangladesh in three different periods are shown in the following Table (Table-: 1).

Table-1: Share to GDP and Growth Rate of Industrial (Manufacturing) Sector
(At 1984-85 constant price in %)

Industry	1973-74		1983-84		1998-99	
	Share	Growth rate	Share	Growth rate	Share	Growth rate
Large	11.7	42.6	10.3	7.5	12.0	7.8
Medium	5.9	137.3	5.6	13.3	6.9	10.2
Small	5.6	1.0	4.7	1.3	4.0	4.0

Source: Bangladesh Economic Survey, 2000

Product Classification

The long history of the industrialization of countries now recognized as industrialized market economy bears evidence of a transition of industrial structure significantly through three stages dominated successively, by consumer goods, intermediate goods and capital goods industries. The inherent dynamism of any industrial base is said to be reflected by the share of the production of capital goods. For example, in 1977-78, the share of consumer goods industries to total value addition stood at about 76 percent followed by intermediate goods (about 18 percent) and capital goods (6 percent). In 1981-99, there was a fall in the consumer goods share (48%) and rise in the intermediate goods share (about 38 percent). However, capital goods share in value addition fell to 4.1 percent. Available evidence tends to show the consumer goods still account for more than two-third of MVA, intermediate goods for one-third and capital goods for the rest. It appears that in the production of intermediate and capital goods and thus in the search for a self-propelled industrialization process, Bangladesh made only a marginal progress over the last two decades or so. The economy is still heavily import dependent for the supply of its basic industrial ingredients (Bhattacharya, 1992; Bayes, 1990).

Twenty-five years of Bangladesh's industrial experiences, thus, represent an era where its industrial sector weathered deregulation, privatization and trade liberalization. Bangladesh's manufacturing sector has traveled a long distance in terms of openness of the economy, deregulation and privatization, especially, when comparison is made with the 1970s and the early 1980s. At present, 40 percent of the industrial fixed assets are reported to be owned by the public sector and the effective assistance levels continue to remain high for some of the IS industries. The economy that started its journey with export pessimism in the early 1970s seems to have developed export optimism in 1990s. On the other hand, in contrast to a socialist framework of industrialization in the 1970s, the economy had landed in a world consistent with free market and free trade based industrialization.

But despite a volley of structural adjustment and reform programs undertaken so far, Bangladesh's industrial sector progressed very little towards expected structural change, growth rate and employment generation. It is alleged that investment rate in the economy has not picked up sufficiently over the years. "Historically, there was only one short-lived episode of investment boom, from the late 1970s to the beginning of the 1980s, with investment in both public and private sector growing at nearly 15 percent annually" (Mahmud, 1995). As has been said earlier, this period coincided with a time when Bangladesh received substantial amount of aid pursued 'lavish' credit policies and provided hefty incentives to lure private investments. However, the honeymoon years of industrial investment soon dissipated leaving a large number of industrial units falling sick.

THE EXTERNAL TRADE SECTOR OF BANGLADESH

The Bangladesh economy progressed at a painfully slow rate in the 1970s. The growth of exports was disappointingly sluggish. The volume of exports of its major traditional items was actually lower in most of the seventies than that attained in Fiscal Year (FY) 1970. Both the balance of trade deficit and the current account deficit as a proportion of GDP almost doubled between FY 1973 and FY 1980. At the same time industrial growth was disconcerting despite various attempts by the government to galvanize the industrial sector. The share of manufacturing output in GDP at constant prices instead of rising actually fell slightly from 11.7 percent in FY 1974 to 14.2 percent in FY 2000.

In the seventies several influential studies (Kravis, 1970; Krueger, 1978) challenged the conventional wisdom regarding the IS. The success of the Newly Industrialized Countries (NICs) which followed an outward oriented and less interventionist policy brought out clearly the relative merit of outward oriented vis-a-vis an inward oriented policy. At the same time profound changes was taking place in the economic thinking in the developed countries. Thus, at the beginning of the 1980s the stage was set for a dramatic turn in the trade policy. Economic liberalization involving "getting prices right", reduction of government intervention in the economy, privatization of public enterprises, contraction of money supply, etc., was accepted as the cornerstone of government economic policy.

The liberalization attempts in Bangladesh can be divided into three phases in terms of the coverage and the degree of implementation of the program: phase I (FY 1982 - FY 1986), phase II (FY 1992 onwards). The first modest attempt at trade liberalization was made during FY 1982-1986. This came on the heels of the New Industrial Policy of June 1982, which envisaged denationalization of public enterprises, simplification of investment sanctioning procedures, etc. The policies undertaken during this phase led to some reductions in the level of quantitative restrictions and in the rates and dispersion in the rates of tariffs, and removal of import licensing in 1983-1984. Some

new measures were introduced and a few of the old measures were reformed to promote exports.

A more heightened attempt at trade liberalization was made during the second phase when Bangladesh initiated a three-year long SAP (FY 1987-89) in terms of an arrangement with the IMF under its Structural Adjustment Facility (SAF). Thus reform program also came on the heels of the revised industrial policy of 1986 which expanded the scope of the New Industrial Policy pertaining to private sector development. The reform package was directed at (a) removing quantitative restrictions on imports, (b) decreasing tariff levels, (c) rationalizing the tariff structure and (d) simplifying trade procedures. Some progress was made in achieving the stated objectives though the achievement was less than targeted. "Distortions, especially those emanating from high rates and exemptions, still remain in the trade regime. Both the average and maximum tariff rates are still far too high and need to be substantially reduced, as they provide excessive levels of protection for many items distorting resource allocation and perpetuating inefficiencies. Prevailing tariff levels also entail a strong bias against exports which must be corrected to promote export growth and develop a competitive and efficient industrial structure" (Bhuyan et.al, 1993).

The third phase (FY 1992 onwards) marks significant intensification of the trade liberalization program. Bangladesh contracted a three-year loan under the Enhanced Structural Adjustment Facility (ESAF) of the IMF covering the period FY 1991-93. The adjustment program included policies to make the economy more export oriented and more market friendly. Under the Industrial Policy'1991, greater incentives for private investment were provided through various provisions like greater tariff rationalization, tax holidays, accelerated depreciation allowances, etc. The Industrial Policy also provided generous incentives for foreign investment in specified industries.

The trade liberalization program carried out in the 1990 has progressively moved to lower the protectionist nature of the trade regime. One study shows that the number of goods whose imports were banned or restricted was reduced from 478 in FY 1985 to 109 in FY 1994. The highest customs duty rate was brought down from 400 percent in

FY 1989 to 60 percent in FY 1995. The number of operative customs duty rates has also been progressively reduced from 18 in FY 1991 to only 7 in FY 1995. As a result of tariff restructuring both unweighted and trade-weighted Nominal Protection Rate (NPR) have declined. The unweighted rate of nominal protection for the whole economy stood at 94 percent in FY 1989; it fell to 30 percent in FY 1995 to 28 percent in FY 1994. These declines in the NPR have, however, not been accompanied by corresponding declines in the dispersion in the protection rates. The coefficient of variation in the nominal protection rate actually increased from 59 in FY 1991 to 74 in FY 1995 resulting in greater variation in effective protection rate.

Import clearance procedures have been gradually simplified. The complete removal of import license requirements in 1993, the modification of voluntary Pre-shipment Inspection (PSI) scheme in 1994, introduction of a computerized valuation for calculation of duties have to some extent simplified the import clearance procedures.

FOREIGN TRADE AND BALANCE OF PAYMENTS

The development in the external sector of Bangladesh in the period from FY 1973 to FY 1999 is presented in the Table-2 (given below). Several broad pictures emerge from the Table-2 (i) with the exception of FY 1974 and FY 1975 the export / GDP ratio varied between 5 to 6 percent until FY 1986. The export / GDP ratio has been continuously rising since FY 1987 reaching its historically highest level in FY 1993. Thus FY 1987 marks a watershed in so far as exports are concerned. (ii) The import dependence of the economy has varied widely from about 10 percent to about 20 percent. The import / GDP ratio seems to have stabilized between 14 - 16 percent in FY 1987 but jumped to 22.48 percent in FY 1995. (iii) There are substantial year to year fluctuations in both trade balance / GDP ratio and current account / GDP ratio. Both attained their highest levels in FY 1982 indicating a severe balance of payments crisis. It is not surprising that the government launched a liberalization program in FY 1982 and allowed Taka to undergo a sharp nominal devaluation of 23 percent. The balance of payments situation is much more manageable in the nineties with sustained growth of exports as well as unilateral transfers especially workers' remittances relative to imports. Bangladesh has managed its balance of payments with relatively

Table-2: Development in the External Sector, 1972-73 to 1998-99
(as proportion of GDP)

Year	Exports	Imports	Trade Balance	Balance on Current Account	Foreign Exchange Reserves*
1972-73	5.53	12.17	-6.64	-5.79	2.7
1973-74	3.89	9.73	-5.84	-5.76	1.5
1974-75	2.46	10.02	-7.56	-7.16	2.3
1975-76	5.01	17.16	-12.15	-11.87	2.0
1976-77	5.40	11.67	-6.27	-5.86	4.0
1977-78	5.10	14.05	-8.95	-8.10	2.4
1978-79	5.53	13.61	-8.28	-7.27	3.0
1979-80	5.70	18.73	-13.03	-11.35	1.4
1980-81	5.02	17.90	-12.88	-10.09	1.2
1981-82	4.84	19.90	-15.06	-12.32	0.5
1982-83	5.54	18.65	-13.11	-8.24	1.8
1983-84	5.75	16.68	-10.93	-6.72	2.8
1984-85	6.42	18.19	-11.77	-9.03	1.8
1985-86	5.25	15.16	-9.91	-6.84	2.5
1986-87	6.10	14.89	-8.79	-5.49	3.4
1987-88	6.44	15.63	-8.19	-5.81	3.6
1988-89	6.35	16.66	-10.31	-6.85	3.4
1989-90	6.80	16.78	-9.98	-7.02	1.9
1990-91	7.34	14.83	-7.49	-4.16	3.3
1991-92	8.39	14.57	-6.18	-2.43	5.8
1992-93	9.84	16.46	-6.62	-2.55	6.6
1993-94	9.84	16.27	-6.43	-1.63	8.1
1994-95	14.19	22.48	-8.27	-3.54	6.7
1995-96	16.04	23.45	-7.41	-3.83	7.3
1996-97	16.36	22.12	-5.76	-2.81	6.2
1997-98	18.01	22.43	-4.42	-3.05	5.8
!998-99	18.56	22.89	-4.33	-2.79	4.3

Source: BBS, Statistical Year Books of Bangladesh, Various Years. (Own Calculation).

- Months of imports equivalent.

low level of foreign exchange reserves. Reserves less than 3 months equivalent of imports have been a recurrent phenomenon in the 1970s and 1980s. In the nineties there has been significant reserve growth, the level of reserves reaching 8.1 months equivalent of imports in FY 1994. The rapid and continuing build up of reserves represents a 'structural' surplus in the balance of payments as well as in the aggregate supply-demand balance in the economy (Mahmud, 1995).

On the whole, Bangladesh's export performance is distinctly better since FY 1987 than in the preceding period. Her trade balance and current account balance seems to be more manageable in the nineties than in the previous decades.

MOVEMENTS IN TERMS OF TRADE

Increase in exports (or imports) is attributable to a change either in price or in quantity of the exports (or imports) or both. An increase in the price of exports leads to higher exports but it may lead to worsening balance of trade if import prices rise at a faster rate. The commodity terms of trade index measures the behavior of export prices relative to import prices. It is now recognized that the income terms of trade multiplied by volume of export provide a better measure of export performance of developing countries. The income terms of trade in effect measures the purchasing power of exports or the capacity to import based on export revenue.

Movements in the export price index are quite erratic with occasional spurts and dips though it shows slight upward trend in recent years. Import price index doubled in FY 1974 from its low level in FY 1973. The index fell in FY 1975 and FY 1976 and then continuously rose till FY 1982. From FY 1983 to FY 1988 the index slided down and then rose continuously with a sudden decline in FY 1992; it reached its historically highest level in FY 1995 (GOB, 2000).

Wide swings and a slight downward trend characterize the terms of trade. It is known that an improvement in the terms of trade represents a favorable external shock and deterioration represents an adverse shock to the economy. Thus the economy has been subjected to frequent adverse external shock during the period under study and the

cost of the terms of trade change has been as high as 3.8 percent of a year's output. Bangladesh now imports fewer units for each unit of exports than it did in the seventies. The income terms of trade has a significant upward trend interspersed by declines. The capacity to import as measured by the terms of trade has a decidedly upward turn since FY 1987. A comparison of the commodity and terms of trade makes it clear that the recent improved export performance is largely a volume phenomenon i.e. exports rose because of rise in quantity with relatively stable prices.

COMPOSITION OF EXPORTS AND IMPORTS

In the early seventies jute and jute manufactures contributed more than 80 percent of export earnings. Their share in exports has consistently declined and fell below 50 percent in FY 1987. It reached a meager 14.4 percent in FY 2000. Traditional exports comprising of jute, jute manufactures, tea, leather and leather products dominated exports in the seventies and a part of the eighties. Their contribution to export earnings fell below 50 percent in FY 1988. In FY 1999 their combined contribution stood at 18 percent (GOB, 2000).

Non-traditional exports comprising mainly of frozen shrimps, frog legs and fish, naphtha and furnace oil, urea and readymade garments have a rising share in exports. The share of frozen shrimps, frog legs and fish rose from 1.3 percent in FY 1973 to 8.7 percent in FY 1999. Readymade garments exports, which was non-existent in the seventies grew at a phenomenal rate and by FY 1999 their share in exports reached a staggering 77 percent. The rapid growth of exports in the nineties as adduced earlier is thus attributable mainly to the accelerated growth of Ready-Made Garment (RMG) exports.

The issues relating to the existing export structure are extensively discussed in Bayes, Hossain and Rahman (1995). Few caveats should be in order. First, the export / GDP ratio in Bangladesh is only two-third of the ratio of LDCs. Second, the country could hardly achieve export diversification over the years; commodity concentration continued to haunt the export sectors. In the 1980s only one commodity, e.g., RMG

appeared as hero of the export sector by accounting for over two-third of the total export earnings. Third, of particular concerns are the missing opportunities to capture higher value addition through backward linkages and the possible impact of phasing out of the Multi Fiber Agreement (MFA) by 2005. While significant opportunities for backward linkages in the RMG sector exist, one should also take note of the fact the materials for these inputs will also have to be imported rather than sourced domestically (Love, 1995). The phasing out of the MFA which has allocated market shares to different countries will put Bangladesh on an equal footing with more established producers like Korea, Hongkong, etc., as well as recent entrants like Cambodia, China, Vietnam, etc. Fourth, there is evidence of an unhealthy geographic concentration of exports. For example, more than three fourths of the total exports of Bangladesh are boarded on for OECD countries. Trade with LDCs is very low and the growth rate is very feeble.

Most categories of imports exhibit substantial fluctuations in their share in total imports. However, some clear trends can be easily identified. Food-grains were a major import in the 1970s when devastation caused by the liberation war, frequent natural calamities and population growth outstripping production growth led to demand-supply imbalance and necessitated large scale importation of food-grains. The growth of production due to the expansion of HYV technology has reduced the demand for food-grains imports. However, if the recent deceleration in food-grains growth (Abdullah et. al, 1995) continues for long, the demand for imports may soon have an upward turn. Further, sudden production shortfalls caused by floods, draught etc., may also necessitate temporary larger food imports. It may be noted, in passing, the continued growth of food-grains production will require increasing imports of fertilizers and irrigation equipment unless import substitution takes place in these sectors. Successive liberalization attempts, especially, the accelerated liberalization regime of the 1990s have not led to a significant increase in the import / GDP ratio. This raises serious questions about the effect of liberalized import policy on the flow of imports. It may be that even with restrictions the importers were able to import what the market could bear. Restrictions were evaded through use of directly unproductive activity so that a surge in imports is not observed after liberalization.

Further, there may be smuggling along the borders and official import data give a gross underestimation of imports.

Debt service payment as a proportion of export earnings and as a proportion of total foreign exchange earnings shows erratic movements with no distinct long-run trend. Debt-service payment was 4.7 percent of export earnings and 4.2 percent of foreign exchange earnings in FY 1973. They soared to 18.5 percent and 14.4 percent, respectively in the following year. The average levels of these ratios were at higher level from FY 1986 to FY 1998 when debt service payment exceeded twenty percent of export earnings. The debt service liability has improved in the 1990's.

CONCLUSION

Bangladesh, with nearly half of its population still groaning under the poverty line, is said to be at cross roads in search of economic and social development. For the last 25 years, GDP growth rates averaged below 5 percent per annum as opposed to a required rate, without any pause for a long while, of 7 - 8 percent for making any dent to the poverty scenario. On the assumption that the current capital-output ratio is 3 : 1, this much of growth rate would demand an investment level of 21 - 24 percent per annum as compared to the present level of investment of around 13 percent only. Given the macro-economic balance that the economy witnessed in the early 1990s, according to available findings, the investment / GDP ratio could be raised to 18 - 20 percent within a five year period without having any pressures on the economy's resource balance. Although the rate could still trail far behind the average for low-income countries (30 percent), certain spurt in the overall growth rate of the economy could be made (Mahmud, 1995). To move towards that "illusory" point, economic policy tinking should be made judiciously. But the most important objective of the government at the moment should be in tackling the non-economic factors that bedevil the attainments of fruits from economic policy changes.

In the wake of dwindling foreign aid availability and growing globalization, the politicians, policy makers and the people at large need to revisit the costs following from past mistakes and thus relieve the nation of the pains by providing an acceptable

future. Attracting more FDI investors may provide some relief to the nation from this pain.

In economic history, the last decade of the twentieth century will best be remembered as the Age of the Investors (Estrin, 1997). Instead of restricting FDI flows, most countries are competing to attract FDI inflows as FDI, which is now seen to have positive attributes of enhancing private sources of investment and providing employment and foreign exchange. In the next chapter (Chapter three), theoretical underpinnings and empirical evidences of FDI have taken up for discussion.

CHAPTER- III

FOREIGN DIRECT INVESTMENT: THEORETICAL UNDERPINNINGS AND EMPIRICAL EVIDENCES

International trade and Foreign Direct Investment (FDI) have much in common (Riedel, 1991). Both are market responses to opportunities (Frank, 1980) provided by differences among countries in production capabilities. Since both serve the same purpose, a central question that arises in regard to direct investment is why it takes place at all. The essence of FDI is that it is a package of capital, technology and managerial skill. This immediately suggests that an understanding of the economics of FDI requires a different orientation than that of the framework of traditional trade theory.

Traditional trade theory is based on the assumptions that factors of production are internationally immobile and that technology is identical between trading partners (Balasubramanyam, 1990). Traditional trade theory does not explain the process of knowledge transfer, nor does it explain the factors motivating the generation of new knowledge (Corden, 1987). FDI, therefore, posses two further questions to the theorists: (i) why do firms prefer to export the package rather than exporting the products? and (ii) why do firms prefer to create production facilities abroad rather than export the capital or the knowledge, or both separately?

The answers to these questions given by the theorists are briefly highlighted in this chapter. The chapter is divided into two sections. Section-I examines the theoretical development of FDI. Section-II provides some country-wise empirical evidences on the determinants of FDI. Relevant data and information of section-II have been derived from various UN reports.

SECTION-I

THEORETICAL UNDERPINNINGS OF FDI

The several avenues of the theoretical development are classified as: the compensating advantage theory of Hymer and Kindleberger (1969); the currency area phenomenon of Aliber (1970, 1971); the product life cycle model of Vernon (1966, 1971); the internalization theory of Buckley and Casson (1976, 1987); and the eclectic theory of Dunning (1977, 1979, 1980, 1981). The strands of the theory, however, go back to much further, to Coase (1937). However, in this study we have only reviewed the oft-cited FDI theories.

The Hymer-Kindleberger Model

The initial core of modern theory of the FDI was a deceptively simple proposition, that in order to compete with indigenous firms, which possess innate strengths such as knowledge of the local environment, market and business conditions, foreign entrants must have some compensating advantage. At a stroke, this proposition took FDI away from the theory of capital movements into the theory of industrial organization. For in a perfect market, foreign direct investment could not exist because local firms would always be able to out-compete foreign entrants (Buckley and Casson, 1987). The initial phase of the Hymer-Kindleberger approach was ,therefore, the search for the compensating advantage which foreign investors possessed.

Kindleberger's exposition (1969) examined four main areas of internationally transferable advantages. First, departures from perfect competition in good markets, including product differentiation, marketing skills and administered pricing. Second, departures from perfect competition in factor markets, including access to patented knowledge, discrimination in access to capital and skill differences embodied in the firm. Third, internal and external economies of scale, including those arising from vertical integration; and finally, government intervention, particularly those forms restricting output or entry. Such advantages enable the foreign entrant to overcome its

lack of knowledge of local conditions innate in the local firms, which the foreign firm can only acquire at a cost.

The focus of investigation was thus placed in the field of industrial organization and was more specifically related to the analysis of imperfect competition. Hymer had relied greatly on Bain's (1956) pioneering work on barriers to entry to an industry. This thread of analysis has been deepened and broadened by Caves (1982). Caves suggested that the critical Hymer-Kindleberger advantage was the ability to differentiate a product, thus enabling the firm to serve simultaneously several international markets.

Currency Area Phenomenon

A variant of the Hymer-Kindleberger approach, particularly associated with Aliber (1971) deals with an advantage, which is not specific to particular firms, but to all firms based in a particular currency area. According to Aliber it is the international financial market in which TNCs have an advantage over host country firms. Consequently, Aliber argues that FDI can take place even if the market for advantage is perfect (Buckley and Casson, 1985).

The analysis centers on the currency premium. The holder of debt dominated in a particular currency bears the risk that his returns will be reduced if that currency depreciates in value relative to other currencies. If there is no aversion to risk then, the rate of interest on the debt dominated in a particular currency will exactly reflect the expected rate of depreciation of that currency. But investors are averse to risk and demand for a premium for bearing the uncertainty of exchange risk. However, Aliber argues that the market is subject to a bias in the application of the currency premium. Investors are myopic- they treat all the assets of a TNC as if they were in the same currency area as the parent firm. Consequently, a UK factory is a sterling asset, but when that factory is owned by a US company it is regarded by the market as if it were a dollar asset (Buckley and Casson, 1985).

The effect of these propositions is that source-country firms are ones which are able to borrow at lower interest rates and are more highly valued by the market because their

earnings are all capitalized at the rate relevant to the source-country currency (Buckley and Casson, 1985).

Several criticisms of Aliber's theory are in order (Buckley and Casson, 1976; Dunning, 1977). First it seems unlikely that as a long-term explanation investors' myopia can bear the weight placed on it. Second, the theory fails to explain the industrial distribution of FDI and the phenomenon of simultaneous cross-investment within one industry between currency areas. In broad terms, the approach explains well the direction of TNC investment in the post-war world; US expansion followed by extensive German and Japanese outward investment and the invasion of the US by European multinationals during the 1970s and early 1980s (Hymer, 1976).

Product Cycle Model

The product cycle hypothesis chiefly associated with Raymond Vernon (1966, 1971) has yielded a large number of insights into the development of the FDI. The model rests on four basic assumptions. (i) products undergo predictable changes in production and marketing, (ii) restricted information is available on technology, (ii) production processes change over time and economies of scale are prevalent, and (iv) tastes differ according to income and thus products can be standardized at various income levels (Wells, 1972).

The model consists of four stages. The first stage of the model begins when an "innovation" is introduced. It is argued that new products would appear first in the most advanced country (the USA). Reasons are many, of which two are prominent. First, rich countries have the financial, organizational and intellectual resources to undertake the requisite research (the 'supply' exists). Second, these countries have large number of consumers with high incomes and "adventurous tastes" (Lall and Streeten, 1980) to test new products on, and the greatest pressures of competition, high wage costs or scarce materials to spur innovation (the "demand" for innovations is high).

The second stage of the model begins when the product is successful in the rich markets. It is argued that if the product is successful in the rich markets, the

production of new product will be expanded, new markets will be cultivated and export development will be started. In this stage the innovators still have the technological lead, but competitors are attracted by its success to work on imitations or to develop similar products.

The third stage starts when sufficient competition has developed, and the technology has become standardized enough, for cost and local-marketing considerations to become important. At this stage, the innovating firm seeks to maintain its profits by making more intense marketing efforts and by investing abroad in cheaper locations and nearer to foreign market (Lall and Streeten, 1980).

The fourth and final stage of the model begins when the production shifts in location down the income scale. At this stage, in the life of the product, cost considerations are of great significance and, therefore, production facilities are moved to least developing countries (LDCs) to take advantage of lower labor costs.

However, Vernon's model has the virtues of simplicity and directness. It explains US investment in other advanced countries and the phenomenon of 'offshore production' in cheap labor countries (Moxon, 1974). The model has been outdated by events. Firstly, the US is no longer totally dominant in foreign investment. Second, TNCs are now capable of developing, maturing and standardizing products almost simultaneously, differentiating the product to suit a variety of needs without significant time lags. However, in spite of its oversimplified explanation, the model has several merits: (i) it provides an explanation of why innovations occur mostly in developed countries, (ii) it provides an explanation for both trade flows and investment flows, and (iii) it provides an explanation for the rapid growth in exports of manufactured goods from LDCs in recent years.

Internalization Theory

Attempts at integration of the various strands of the theory of the multinational firm have centered on the concept of internalization. The central argument of this approach is that TNCs exist because of market imperfections. If all markets operated perfectly there would be no incentive for firms to go to the trouble of controlling subsidiaries in

different countries and to internalize markets between them, rather than engaging in arm's length transactions with independent firms. Internalization then is a way of bypassing imperfections in external markets.

The growth of TNCs follows from the view that they are essentially an efficient means of overcoming market failure. They, therefore, act to increase efficiency in the world economy. As with the product cycle theory, technology or information plays a central role in internalization theory. It is argued that the activity of TNCs makes both goods and financial markets more efficient than they would otherwise be (Rugman, 1981). It has been suggested that market imperfections are more pervasive in the developing countries than in the advanced capitalist countries; developing countries are in a position to gain even more through TNC operations which circumvent such imperfections (Agmon and Hirsch, 1975).

Pater Buckley and Mark Casson (1976) enunciated the theory. The theory holds that the internal organization of the multinational firm is an approximation to a perfect market whereby the firm's internal processes are designed to transmit shadow prices to the key decision-makers, which optimize the firm's price signals to other decision-makers in cost or profit centers (Buckley, 1992). The multinational enterprise is thus a device for reducing transaction costs by buying or creating complementary assets in different nations and integrating their operations within a single unit of control. This is the internal market for intermediate goods and services. In this way, individual managers within the firm have decentralized decision-making powers. The aim has been to control over the intermediate product actually changes hands as the product moves between plants, although ownership of the product does not (Casson, 1981).

It gains the benefits of international transfer pricing in order to reduce the firm's overall tax bill, to obtain improved quality control and to gain vertical integration benefits (Buckley, 1992). The internationalization of markets national boundaries results in FDI.

In a nutshell, the explanation of FDI according to the internationalization approach is that the transnational firm is seen as an internalized bundle of resources which can be

allocated (i) between product groups (changes in which are identified as conglomerate diversification and (ii) between national markets. The growth of the firm 'relative to markets' is determined by its internationalization decisions. The firm grows by replacing or creating neighboring markets according to the positive balance between the benefits of internationalization versus the costs of each distance. The growth of the firm is determined by the net benefits of internal control relative to the extra cost of using imperfect external markets in intermediate products and services.

The internationalization theory was however empirically tested by Buckley (1988), Williamson (1985), Teece (1983) and Nicholas (1986). The results produce a mixed reaction. The major problems of the theory arise in the definition and measurement of transaction costs: the magnitude of transaction costs in relation to transport costs, production costs, marketing and distribution costs.

Eclectic or OLI Theory

The theory was propounded by Dunning (1977). The theory pulls together the different strands in various explanation of FDI. Dunning asserts that three conditions are necessary under which a firm will engage in FDI. The first necessary condition of FDI is that, a firm must have an ownership advantage, such as proprietary rights to a product or a production process, which gives an advantage over foreign companies. The second condition is that, the foreign country must have a locational advantage for production, such as tariff or transport cost barriers to imports or low factor prices, that leads the multinational to produce in that market rather than export. The third condition is that, there must be an internalization advantage for production that leads a multinational to buy or create a foreign subsidiary rather than license production and/ or distribution of a product to a foreign firm.

Of these ownership—locational—internalization (OLI) advantages, the literature on locational advantages of host countries is the most relevant. This literature has focused on the real cost and availability of the basic factors of production and on the size structure of local markets. Locational factors also influence the relative costs facing a multinational enterprise with a choice of locations. The major locational

factors include: availability and cost of human and other resources, size of markets, infrastructure, government policies (e.g. tariffs, quotas, and taxes), and assistance to foreign investors.

Under this framework with the exception of market size, none of the determinants tends to change very much over short periods of time and many variables do not change much even in the medium term (say 1 to 5 years). The framework generally does not concern itself with business cycles, and thus its treatment of the role of market size is incomplete in a time - series approach (Caves, 1982).

Previous empirical work on FDI determinants have one overriding common theme; that is, market size or related variables are almost always crucial determinants of the variation in FDI, whether that variation be measured across time or other dimensions. The important role of this variable stems from the fact that transnational usually sell the majority of their output in host-economy markets (Agarwal, 1980). Other studies have found that per capita GNP and GDP growth to be significant variables (Dunning, 1993).

Among the OLI variables, cross-section studies have tended to highlight the importance of ownership - specific variables such as Research and Development (R & D) intensity, skilled - labor intensity, and advertising intensity as well as internalization - related and location variables such as import restrictions, tax rates, and market size (United Nations, 1992). Most cross-section studies have found that wages are not a significant determinant of FDI inflows, though a few have found that productivity may be more important (United Nations, 1992).

Surveys have generally found that while the reduction of labor costs was important, it became less so in all countries examined. For investments in Singapore and Hong Kong, building international networks and collection of information was also important. Other surveys have highlighted the role of trade policies. After trade barriers were reduced, firms in the less-protected apparel industry and the electrical / electronic industry were geared primarily for the export market (United Nations, 1995).

One of the few studies which examine FDI flows in particular countries over time for Indonesia, Republic of Korea, Malaysia, the Philippines, Singapore, Taiwan Province of China, and Thailand is the study by Lucas (1993). This study found that investment was related in most cases to wages. The deterrent effect of higher wages is estimated to outweigh substitution towards greater capital intensity. In most cases, however, the cost of capital had only a small impact on FDI, and the capital stock of a country had only a weak association with FDI.

It is obvious that host countries have very little scope to influence the ownership and internalization advantages of a TNC. These are acquired by a TNC over its lifetime through its own decisions. In certain aspects, of course, home country policies may be helpful. For example, subsidized access to finance capital in a country may confer an ownership advantage on the enterprises of that country

Recent Theories of Foreign Direct Investment

Several theories of the FDI and its principal agent-the multinational firms-have been identified in the previous discussions. These theories have been tested empirically by many. For example, the ideas of Coase (1973) have been extensively applied to the MNCs by Buckley and Casson (1976, 1985), and Rugman (1981), in what has become known as the internationalization approach. In addition, Dunning's eclectic theory (1977, 1981) of FDI has been empirically tested all over the world. In fact, a number of attempts had been made to explain and to integrate the standard Heckscher-Ohlin theory of trade with international investment, particularly in the context of less developed countries until 1980s. But none of these proved in providing a general answer to the question of the causes of FDI.

However, a recent article by Horstmann and Markusen (1989) attempts to encompass the welfare effects of direct foreign investment in a simple general equilibrium model. The model assumes that the market structure is characterized by perfect competition and that each factor is paid its marginal product. Given these assumptions, it demonstrated that inflows of foreign capital increase total output and augment labor's share of the output, and that the host government gains by way of increased tax revenues. This is why the developing countries continue to attract FDI to their shores.

Brent McClintock (1988) analyses the nature of FDI from the viewpoint of institutional approach, which includes: (i) the infusion of more radical elements such as forbearance, trust, reciprocity, commitment in an overarching concept of corporation, particularly in the context of joint venture, (ii) the inclusion of corporate culture more specifically within the analysis, and (iii) more explicit attention to the welfare implication of multinational investment.

Porter (1986) explained the FDI using competitive advantage strategy approach. Competitive advantage is defined as the advantage of one firm "relative to another firm". Thus a firm can have a relative cost advantage deriving, for example, from economies of scale, and absolute cost advantage deriving from control of key inputs, superior product technology or cheaper physical distribution, and product differentiation advantages arising from superior products or more effective marketing. The model as used by Porter is directly analogous to Dunning's firm -specific advantage.

Teece (1983) has extended Williamson's (1985) markets and hierarchies' approach in explaining the nature of FDI. This approach attaches fundamental importance to the role of transaction costs in the development of multinational firms. The approach is the ramifications of internationalization approach advanced by Buckley and Casson (1976).

Recently, US business schools developed internationalization / globalization model of the development of multinational firms, which suggests an incremental approach to development: 'deepening involvement' with foreign markets is suggested, a process of 'creeping incrementalism' as the firm grows in international stature. The applicability and relevance of this model are limited in scope (Young, 1987, Porter, 1986).

The insights provided by several recent explanations of FDI (analyzed above) clearly demonstrate that the theoretical arguments are highly controversial, complicated and inconclusive in nature. It is, therefore, essential that the grafting of new concepts should occur in explaining the FDI on a solid core.

SECTION-II

DETERMINANTS OF FDI: EMPIRICAL EVIDENCES

This section examines the determinants of FDI inflows in six countries: Hong Kong, Indonesia, Malaysia, Singapore, Thailand, and India. These countries are selected because of their tremendous success in attracting FDI inflows. Data for this section have been obtained from published and unpublished documents of the Economic and Social Commission for Asia and the Pacific of the United Nations and the world investment reports of various years.

Hong Kong

FDI has always played a key role in the economic development of Hong Kong. Hong Kong was founded as a British trading post in the 19th century. In the 1950s, the influx of capitalists and industrialists from China helped transform the Hong Kong economy from an ***entrepot*** to a manufacturing base. More recently, with the opening up of China, Hong Kong has become the gateway to the mainland and foreign investors are investing heavily in Hong Kong to enter the China market. Thus, notwithstanding its known change of status from 1997, FDI has continued to flow into Hong Kong and has helped to sustain its economic vibrancy.

Hong Kong imposes no restrictions on foreign ownership and FDI is extensive in all major economic sectors. Because of rising land and labor costs, labor-intensive processes are being phased out, and new investments are concentrated in more capital and technology - intensive processes. In line with the growing service orientation of the Hong Kong economy, FDI is increasingly concentrated in services.

Hong Kong is unique among East Asian countries in its policy of non-intervention with regard to FDI and its policy of nondiscrimination between foreign and local enterprises. Hong Kong's laws and policies do not distinguish between foreign and domestic enterprises. Foreign and local businesses are registered under the same laws,

are subjected to the same set of business regulations, and are taxed at the same rate. Legal requirements are few and restrictions are minimal.

A survey of the determinants of FDI in Hong Kong found that firms from developed countries were attracted to Hong Kong by its labor cost and availability, infrastructure, and geographic location. In fact, the availability of skilled and technical personnel at competitive wage levels was more important than general labor availability. Access to the Hong Kong domestic market and raw materials were not major factors. For firms from developing countries, Hong Kong's geographic location in relation to China and the rest of Asia was the most important pull factor; for some multinational firms, ethnic ties were also an important motivation, while some also considered Hong Kong's relatively superior technology an inducement to invest (Chen, 1994). Chen's study also found that ownership-specific advantages such as superior technology, management, and marketing were of lesser importance for investing in Hong Kong.

In 1993, Hong Kong Industry Department conducted a survey on the foreign firms' assessment of the Hong Kong investment. Firms were asked to respond to 12 factors on the investment environment, including government policy, industrial infrastructure, factor costs, geographical location, and political climate. Respondents considered the three most important factors to be labor cost, infrastructure cost, and banking and financial facilities, followed by labor productivity, the political climate, government economic policy, and cost of office/factory space. Regional location, local market potential, and support of linkage industries were considered to be lesser important (United Nations, 1995).

On a closer examination, the role of the government has also been critical to Hong Kong's economic success. Successful macroeconomic management has kept Hong Kong financially sound and the inflation rate low and maintained external confidence in the Hong Kong economy and its currency. The adequate provision of physical infrastructure and education and training has contributed to the favorable investment climate and the competitiveness and efficiency of the private sector. Administrative efficiency and fiscal prudence have kept budgetary expenditures low and, together with large revenues from land sales, have enabled the private sector to enjoy one of

the lowest tax rates in the world. Finally, an open-door policy towards trade and capital flows have enabled and pressured the Hong Kong private sector to remain internationally competitive (United Nations, 1995).

Singapore

Foreign Direct Investment has played a crucial role in Singapore's economic success. Inflow of FDI has been actively promoted since the early 1960s, and until overtaken by China in 1991, this city-state nation was the largest recipient of FDI among developing countries (United Nations, 1995). The degree of foreign penetration is exceptionally high, with foreign equity accounting for more than one-third of total equity investments in Singapore in the 1980s, and with the bulk of foreign investments undertaken by wholly foreign - owned and majority foreign - owned firms.

FDI is welcomed in almost all areas of economic activity in Singapore, the notable exceptions being the mass media and defense industries where restrictions are imposed for national security reasons. Foreign equity investments in Singapore are concentrated in manufacturing and services (commerce, transport and storage, financial and business services, and social and personal services), with the primary sector and construction accounting for only negligible shares. Up to 1980, the manufacturing sector accounted for the largest share of FDI. More recently, with growing labor and land constraints following decades of sustained high economic growth, the promotion of inward FDI has become increasingly focused on high-tech and high value added industries and services.

Four features characterize the foreign investment policy of Singapore. These are: a general absence of ownership restrictions and performance requirements, de-emphasis on protection of the domestic market and emphasis on ensuring availability of factor supplies and services to contain business costs, liberal use of fiscal incentives, and consistency and predictability of policy over time.

Surveys have found that like in other countries more than one-half of all Japanese firms that have invested in Singapore, aim their products at the domestic market and nearly a third invest to export to a third country. The most recent data indicate,

however, that investment for sales to the local market is becoming more important. Singapore is a small, but growing market for Japanese subsidiaries. One study of the determinants of FDI in Singapore over the period 1961-1987 (Lucas, 1993) found that the elasticity of the cost of labor and capital was negative and significant. The study also found that the interaction between domestic and foreign investment was statistically positive indicating that domestic capital complements FDI.

Various international business surveys have consistently ranked Singapore as one of the most attractive investment locations in the world. The major factors that contribute to Singapore's attractive investment climate include its geographical location and physical infrastructure, its manpower, and its institutional infrastructure and environment.

Singapore is strategically located at the crossroads of international air and sea routes. It is a regional distribution and transshipment hub and is an advantageous location for time sensitive shipments. Singapore enjoys a time zone advantage as a financial center, as its working day straddles the working days of other major financial centers. This locational advantage has enhanced growth and the ensuing demand for financial services has outstripped those of other geographic regions.

The Singapore work force has consistently been rated as one of the best worldwide for work attitude, productivity, and skills. Singapore possesses a skilled, English-speaking, disciplined, and hardworking work force. Favorable labor environment in Singapore is the product of three decades of inculcating social discipline in the population and heavy investments in education and training. Government agencies teamed up with leading foreign firms in Singapore and with foreign governments to run training centers to produce specialists manpower in machinery industries, electronics, and information technology.

The pursuit of an export-oriented industrial strategy is another factor behind Singapore's success. Singapore embarked on this strategy in the mid-1960s against the conventional wisdom of import substitution. Export-orientation not only prevented a foreign exchange bottleneck, but also forced the MNCs to adopt appropriate technology and be competitive internationally, resulting in efficient industrialization.

The pursuit of a stable macroeconomic environment is another factor that enabled foreign investors to take a long-term view of their investments in Singapore and not be pressured into short-term expedience. Macroeconomic policies have contributed to a low inflation environment, the high economic growth rate, excellent government finance and external reserves, and low sovereign risks (United Nations, 1998).

Indonesia

Indonesia has been extremely successful in attracting FDI in the late 1980s and 1990s.Total FDI inflows into Indonesia have increased by more than 20 percent annually in the 1990s, making it the fifth-largest recipient among developing Asian countries. An important factor for this success has been its large population size, its abundance of natural resources and liberalized foreign investment laws.

One analysis of determinants of FDI in Indonesia found that over the period 1975 - 1987, the real wage had a significantly positive relationship with FDI inflows (Locus, 1993). Allen (1979) found that the motive for 51 percent FDI in Indonesia was to secure, maintain, or develop an overseas market, while 46 percent were to secure and develop raw material supplies. Only 3 percent of investments were motivated by the low wages of Indonesia.

In another survey (United Nations, 1995) shows that the most important motive of foreign investors in Indonesia was to secure local markets. Low wages were not a factor in the 1970s but have become more important in the 1980s and 1990s. Thus, reducing labor costs became increasingly important while government incentives became less important over time. Using a flexible accelerator approach in Indonesia, the UN study also found that wage and real interest rates were significant determinants of FDI inflows in a few industries such as textiles and garments.

Malaysia

Malaysia has enjoyed rapid economic growth averaging over 8 percent for the periods 1971-1995 (United Nations, 1998). While mainly domestic resources financed growth

in the 1970s, the influx of FDI since 1986 has significantly contributed to the spectacular growth thereafter.

The marked surge of FDI in Malaysia in the late 1980s and early 1990s is quite conspicuous, with much of this investment concentrated in the manufacturing industry. In particular, the most striking characteristic observed is the large and growing role of investment in electric machinery. This increase is even more impressive if viewed in the context of the rapid increase in manufacturing investments by foreign firms, as both fixed asset stocks and paid-up capital stocks more than doubled in this short five-year period.

Although Malaysia initially embarked on an import-substitution strategy in the 1960s, the country has moved more quickly than some of its neighbors moved to a relatively open trade and investment regime. Presently, there are generally no restrictions on foreign participation in the manufacturing sector, though levels of foreign equity ownership are subject to various restrictions. In particular, the percentage of foreign ownership allowed is often dependent on export-to-total sales ratios or if high - technology or priority goods for the domestic market are being produced. Malaysia also provides fiscal incentives for FDI for export sectors, research and development, and other preferred investments.

Previous studies of determinants of FDI in Malaysia stressed demand-side variables such as the role of Malaysian policy. And the supply side emphasized the effects of changing comparative advantage in major investors and exchange rate realignments in recent years. Malaysia's relatively good infrastructure and low labor costs, which generated a comparative advantage in labor-intensive manufactures, were pointed to as locational advantages (United Nations, 1997).

Surveys reinforce the fact that expanding sales in the Malaysian market is an important determinant of virtually all FDI flows. The desire to utilize Malaysian labor was another motive of similar importance. Surprisingly, firms also sought to take advantage of Malaysian policies and protectionism. Despite the relative openness of

the Malaysian economy, it is clear that continued protection in some industries has drawn import-substituting investments (United Nations, 1998).

The UN study (1995), using the flexible accelerator approach, found some interesting results on the determinants of FDI in Malaysia. First, the net sales variable is the most consistently significant determinant of both equity and fixed investment. However, this variable was not a significant determinant in agriculture and construction, and for equity investment in mining. This is likely due to the fact that FDI in agriculture and construction has been very small and much of the FDI in mining is export oriented. Second, lagged capital stock portion of the flexible accelerator was a significant determinant of equity and fixed investment in manufacturing and construction, while it was a significant determinant of equity investment only in mining, and fixed investment only in banking and finance. Third, the real interest rate variable was not significant. Fourth, the wage variable's coefficient is negative and weakly significant in the fixed investment equation for manufacturing sector.

Thailand

Thailand embraced an import-substitution policy approach to its international commercial policies until the 1980s when prices of its major export commodities plummeted in the 1980s. Liberalization of trade and FDI regulations was seen as a way to expand exports and capital inflows. There are no special registration requirements to set up a branch office. However, a foreign corporation's branch office must comply with existing laws and regulations. For many foreign firms, these restrictions are often not significant. The Board of Investments (BOI) also provides incentives of export and other preferred industries though foreign investors can invest in Thailand without any involvement with the BOI.

Previous surveys examining motives for FDI found that FDI across industries was attracted to Thailand primarily because of the availability of cheap, productive labor and raw materials, Thai government incentives, and adequate local demand. Less important but nevertheless considerable were contributions of equity and management know-how (United Nations, 1997). One survey found that exporting firms, which also

happened to be the larger firms studied, expressed exclusive concern with labor inputs, production for external markets, exchange rates, and tax incentives, with some secondary concerns about other financial variables observed (United Nations, 1998). Major disincentives identified in another survey were excessive import duties, high company and income taxes, arbitrary or cumbersome customs and taxation procedures, lack of patent protection, and restrictions on firm growth (United Nations, 1999).

The flexible accelerator model, used by the UN study in 1995,did relatively well in explaining FDI flows at the sectoral level. The industrial GDP level is by far the most consistently significant determinant of FDI flows. Agriculture was the only sector in which this variable was not a significant determinant. The coefficient on the lagged capital stock portion of the flexible accelerator was consistently significant in only one industry, manufacturing. The coefficient on the rate interest rate variable was not consistently significant. The wage variable's coefficient is negative and significant in agriculture and manufacturing, and positive and weakly significant in mining. In other industries, the variable is negative but not consistently significant. A similar result is obtained in the exchange rate case, with this variable being a significant determinant in agriculture and manufacturing (Foo, 1993).

India

The case of India is an extremely interesting one because throughout the 1980s, FDI inflows were minimal despite the fact that it has many of the attributes of a country likely to attract FDI inflows. Indeed, after policy changes in 1985 and again in 1991, FDI inflows increased sharply and maintained the higher levels. This illustrates the importance of policies in attracting FDI flows; it is not a sufficient condition, but clearly it is a necessary one.

India has been known for its policies promoting self-sufficiency that deliberately insulated its economy from external competition and exerted comprehensive controls on private enterprises. In its seventh five-year plan, however, the government introduced reforms to decontrol industry, liberalize imports, reform prices, and

encourage private enterprises. These reforms, while halting at best, went further than earlier attempts at liberalization. Further liberalization of FDI regulations began in July 1991, which provided automatic approval of FDI project proposals in priority industries. At the same time, local content regulations were withdrawn. Full ownership was allowed for foreign firms on a case-by-case basis, and foreign investors were given the freedom of repatriation of earnings. An array of tax holidays and capital gains concessions was implemented to attract FDI. At the same time, import duties were lowered and a system protecting intellectual property rights was instituted.

Surveys found that the large Indian market largely motivated the FDI inflows. Policies governing investment and business regulations have had the largest impact on FDI inflows. GDP growth rates have fluctuated over the period generally between the 4 to 5 percent range with a few outlying years. India has maintained a relatively stable macroeconomics environment with inflation rates confined to single digits since 1981. Exchange rates have been relatively stable with a 20 percent depreciation in 1984, and several successive devaluations in the late 1980s (United Nations, 1998).

Conclusion

This chapter has briefly examined the theoretical explanation of FDI and discussed the patterns and determinants of FDI flows in several Asian countries. Individual country analyses show both similarities and differences in these determinants. The most interesting findings are:

First, both empirical and theoretical findings indicate that changes in host country variables can explain the vast majority of the variation in FDI inflows. This indicates that policymakers have the ability to influence FDI flows by influencing economic fluctuations in the host economies. In other words, policies that contribute to economic growth are the most important elements attracting FDI. Empirical studies emphasize that market size or related variables are almost always the most crucial determinants of FDI. The importance of this variable is due to the fact that

transnational corporations usually sell the majority of their output in host-economy markets.

Second, when wages and interest rates are correlated with FDI flows, that correlation is generally negative. The cost of capital in the host country, however, has been insignificant in most cases. This result may be due to the difficulty of measuring capital costs or in some cases the presence of capital controls. Low wages, on the other hand, have been a major motivation for some FDI in the countries examined in the study, especially in the manufactured goods sector and in particular, in textiles, garments, and other labor - intensive industries. Nonetheless, the importance of labor costs has declined over time for most countries and sectors in the 1980s. In some countries and industries, in fact, there was positive correlation between labor costs and FDI inflows. The likely explanation is a spurious correlation due to rising wages in a period of rising economic growth and increasing FDI inflows. Studies also show that differences in relative costs in neighboring countries have little impact on FDI inflows, thus making competition to lower costs through fiscal incentives are misconceived.

Third, liberalizing rules governing investment and other restrictive business regulations is a necessity but it may not be a sufficient condition for attracting FDI. The case of India shows that liberalization of such policies can have a significant impact on the level of inflows. Liberalization of policies such as those governing ownership, repatriation of profits, and the ability to conduct business can move FDI inflows to a higher level. Yet despite the increase in inflows into India after deregulation began in 1991, FDI into India still remains low in comparison to that of the East and Southeast Asian countries examined.

Fourth, incentives to foreign investors have little impact over the long run. Thus, competition by developing countries to provide incentives to investors tends to be an unnecessary transfer of funds from the host country to the firm. Incentives have been cited as being important only on the margin.

Fifth, liberal trade regimes tend to attract more FDI. This conclusion is certainly true in the case of export-oriented investments that need to import machinery and equipment at reasonable prices. But interestingly, large inflows of FDI have occurred in countries with low rates of protection even when sales were aimed at the domestic market.

Finally, as the OLI framework points out, source country factors are also an important determinant of the level of FDI flows. Thus large outflow in a certain period may reflect economic factors or adjustments in the source country. The large FDI outflows from the Newly Industrialized Economies (NIEs) in the 1980s and 1990s indeed stem largely from rising wages and appreciating currencies. Past studies have found that rising income in home countries has a positive impact of FDI.

The development strategies and macro-organizational policies of the host-country government influence this economic environment. Host country policies and policy pronouncements affect the perception of "political risk" by transnational corporations and thereby the amount of investment of these companies. In addition, host country policies can be instrumental in channeling investment flows toward sectors considered to be of particular importance to the country's development. Industrial and trade policy regulations of a country are frequently considered in the literature as a proxy for the distribution of FDI (Aggarwal, 1997). The next chapter (Chapter four) therefore provides a brief overview of the Bangladesh State policy towards FDI.

CHAPTER- IV

FDI POLICY IN BANGLADESH: A BRIEF REVIEW

Bangladesh is basically an agricultural economy. Its industrial capacity is negligible for processing locally produced agricultural raw material. This made it imperative for succeeding governments to improve the country's manufacturing capacity. In order to achieve this objective, however, changing types of industrial policies have been implemented in different times with a changing focus on either the private sector or the public sector.

Bangladesh State policy towards FDI has been elaborated in the industrial policies announced and revised from time to time. There has been several such policy packages announced since 1973. The first Industrial Investment Policy (IIP) announced in1973, allowed foreign collaboration in public enterprises only with minority equity participation of 49 percent. The policy had given a dominant role to the public sector in industrial ownership and entrepreneurship, allowing only a minor role to the private sector.

The response of foreign investors to this policy was not encouraging, as could be expected. The sudden shift toward nationalization of private sector industrial units shattered private investors' confidence. A new investment policy (NIP) in 1974 permitted foreign investors to collaborate with both government and local private entrepreneurs, except in some basic industries. The policy was revised in 1975 and the revised investment policy (RIP) allowed foreign investors to collaborate with private sector subject still however to various restrictions.

After the dismal performance of the industrial sector following the 1972 nationalization, a change occurred in 1977 in the government's approach toward the role of the public and private sectors. The role of the public sector was restricted to consolidating existing enterprises, and further investment in this sector was strictly

restricted. A New Industrial Investment Policy (NIIP) in 1978 was formulated. The new policy statement reiterated that the government would continue to pursue a pattern of a mixed economy, with the private and public sector reinforcing each other.

Bangladesh began to implement a more liberal foreign investment policy as part of its overall economic reform program toward the end of the 1980s. Accordingly, a new industrial policy package was introduced in 1986 based on the recognition of the primacy of the private sector. A number of policy and regulatory measures were taken to improve the business environment in general and attract FDI in particular. The Board of Investment (BOI) was set up to help generate opportunities for FDI and provide investment services. A "one-window facility" was established to overcome difficulties in setting up new industries.

The 1991 Industrial Policy (IP), which allowed up to 100 percent foreign private investment along with joint venture, brought the FDI policies to its most liberal phase, with a 1992 amendment incorporating additional facilities and incentives. The Guide to Investment in Bangladesh (July 1995) published by the Board of Investment (BOI) contained the latest status of investment laws and rules. This latest status of FDI policy will be here called the Amended Industrial Policy (AIP) 1992.

Several factors influence the foreigners to invest in host countries. The major factors are fiscal and financial incentives, incentives to export, low cost of labor and availability of skilled and unskilled labor, growth prospect of the host country's market, and infrastructural facilities. While FDI policies can package financial, fiscal and export incentives to foreign investors, most of the other factors are part of the overall economic environment of the country.

In the latest industrial policy (AIP, 1992), the government of Bangladesh took several positive steps for attracting FDI, including further reducing the reserve list and liberalizing incentives. FDI was allowed in all sectors of the economy with the exception of the five sectors of arms, ammunition and other defense equipment and machinery; production of nuclear energy; forest plantation and mechanized extraction within the bounds of reserved forests; security printing (currency notes) and minting;

and air and railway transportation. This brought the reserve list of industries down to the minimum ever. In the NIP 1974, 18 sectors were kept reserved, eight in RIP 1975, seven in NIIP 1978, six in the NIP 1982, and seven in RIP 1986.

The government however, has also announced a "discouraged list" of industries from time to time. The RIP 1986 designated a list of 12 such industries on grounds of non-viability and over-subscription. The list was subsequently enhanced to 28. The AIP 1992 had not stated anything specifically about this list but envisaged to frame rules from time to time for certain industries to protect the environment, public health and national interests.

The Government of Bangladesh welcomes foreign investment under joint venture or 100 percent ownership by foreign enterprises in:

- Export-oriented industries.
- Industries in the export processing zones (EPZs).
- High technology products that will be either import substitute or export-oriented.
- Undertaking in which more diversified use of indigenous natural resources is possible.
- Basic industries based mainly on local raw materials.
- Investment towards improvement of quality and marketing of goods manufactured.
- Labor intensive / technology intensive / capital intensive industries.

The AIP 1992 ensures equal treatment for local investment, joint venture and 100 percent foreign investment. Following this policy, it has been declared that no government permission would be necessary to set up industries and for Balancing, Modernization, Replacement and Expansion (BMRE) of existing industries with the entrepreneurs' own funds, or finance from private financing institutions.

The following are some of the major privileges provided to foreign investors under AIP 1992.

- No limitation pertaining to equity participation i.e., up to 100 percent equity ownership is allowed.

- Treatment of re-invested repatriable dividends as new investments.
- Working capital loan / term loan facility to foreign investors from local commercial banks.
- Investment in shares and securities through Dhaka Stock Exchange without prior approval of the Bangladesh Bank.
- Remittance of 50 percent of the salary of the foreigners employed in Bangladesh.
- Repatriation of invested capital, profits and dividends; and
- Convertibility of Taka, the currency of Bangladesh for international payments on current account.

The above package of privileges granted under the 1991 and 1992 policy reforms made Bangladesh's FDI policies one of the most liberal anywhere. However, confusion still remained in the matters of exact scope and definition of industries requiring clearance on the grounds of environment and over-saturation. The 1991 industrial policy categorically demanded clearance of industries on environmental grounds. Nothing however was said with respect to the exact type of industries requiring clearance or the criteria on the basis of which to grant approval. Again, which industries needed to be discouraged on the ground of over-saturation or national interest was not clear either.

The Board of Investment (BOI) reportedly advised the financing institutions not to finance such industries as edible oil refining, electric fans, corrugated iron sheets, and the like, apparently on grounds of saturation, although the investors tended to believe that a better or a cheaper products could be produced with further investment (United Nations, 1998). These created scope for not only confusion but also opportunities for corruption for those responsible for registration and environmental clearance.

Re-investment of repatriable dividends is treated as new foreign investment in AIP 1992. This implies that not all recorded FDI represents a net transfer of resources from abroad into Bangladesh. Similarly, repatriation of profits by foreign investors is also allowed under AIP 1992. Studies comparing new FDI with remittances for the period 1976-77 to 1982-83 (Sobhan and Bhattacharya, 1986) showed that profits and dividends from FDI far exceeded the total inflow of foreign capital into Bangladesh.

That indicated that unless there was a quantum escalation in new inflows of FDI, further liberalization of provisions for remittance of profits by foreign investors, will in the years ahead, increase the net drainage of resources out of Bangladesh.

The AIP 1992 provided the following noteworthy fiscal incentives to foreign investors:

- Tax holiday for five years in developed areas and seven years in other areas.
- Duty-free import of capital for hundred percent export-oriented industries.
- Hundred percent accelerated depreciation allowance.
- Tax exemption on royalties, technical know-how and technical assistance fees, interest on foreign loans and capital gains from transfer of shares.
- Avoidance of double taxation on the basis of bilateral agreements; and
- Income tax exemption up to three years for the foreign technicians employed under the approved industries.

Presently tax holiday for five year is allowed for industries located in developed areas (Dhaka and Chittagong) and seven years for industries in other areas. For the same purpose, various areas of the country were divided into developed areas, less developed areas, least developed areas and special economic zones (i.e., export processing zone). Tax holiday for these areas was 5, 7, 9 and 12 years, respectively. Under RIP 1986, the tax holiday was given for 5, 7 and 9 years for industries to be set up in developed areas, less developed areas and least developed areas.

Accelerated depreciation allowance in lieu of tax holiday is also allowed under AIP 1992. The rate is 80 percent of actual cost of machinery in the commencing year and 20 percent for the following year if the industry is located in a developed area and 100 percent for the less developed area. This provision of accelerated depreciation did not exist in RIP 1986.

Another important change was made with respect to the duty on imported capital machinery. Import duty payable on capital machinery and spares imported for initial installation or for BMRE of the existing industries was reduced to 7.5 percent ad-valorem under AIP 1992 from 10 percent in 1991. Third, import duty for other export

-oriented industries (exporting minimum 70 percent of output) is 5 percent for developed areas and 2.5 percent for other areas under AIP 1992.

At present, if any industry exports 70 percent of its products, that industry is termed as export-oriented industry, reducing it from 80 percent earlier.

Incentives for industries in EPZs include: Tax holiday for 10 years; exemption of income tax on interest on borrowed capital; duty - free import of machinery, raw materials, and materials for construction of factory buildings; duty - free export of goods produced in the zones; and exemptions from national import policy restrictions. **However, details of the Industrial Policy of 1999 and the Foreign Investment Policy and Incentives are given in Appendix-II.**

With all these financial, fiscal and export incentives, Bangladesh now offers opportunities like never before for both local and foreign investment in the industrial sector. However, before we go on to discuss the impact of the above stated policy packages on FDI inflows in Bangladesh the institutional set up for administration and implementation of the policy and their efficacy may be critically examined.

INSTITUTIONS AND INFRASTRUCTURE

Institutional and Infrastructural Facilities

A prospective investor in Bangladesh, local or foreign, has to usually approach a large number of institutions and agencies for opening a business. The process is very long and cumbersome and naturally creates disappointment and frustration for the entrepreneurs, particularly the new comers. To ease the situation, the Government of Bangladesh has been shifting its role from regulatory to promotional. The sanctioning and other procedures for obtaining facilities and services are being simplified. For promoting private investment, a high-powered institution named the Board of Investment (BOI) was set up in 1988. This Board is responsible to take decisions for speedy implementation of new industrial projects and provide operational support services to the existing ones.

The following are the various key government agencies a foreign investor has to deal with from the point of filing an application for investment till opening the business and during its operation, for various purposes as indicated.

(a) Registration:

At the outset, a foreign investor is advised to meet the Member (Communication) of the BOI for initial discussion and subsequent meeting with counselors on the investment proposal that he has. An application is to be made giving such information as the type of industry proposed to be set up, annual capacity, total investment, and mode of financing and list of machinery. The BOI is responsible for giving registration to all industrial projects outside the authorities of the Bangladesh Small and Cottage Industries Corporation (BSCIC), that deals with, as the name implies, the small and cottage industries having capital investment not exceeding Tk. 30 million and requiring no borrowing, and the Bangladesh Export Processing Zones Authority (BEPZA), which takes the overall responsibility of the industrial undertakings located within the two EPZs in Bangladesh. These three agencies also act as the sponsoring agencies responsible for promoting, assisting, supervising and administering as well as offering pre-registration services to the industries falling within their jurisdictions.

(b) Infrastructure facilities:

No approval or permission is required for establishing an industry in the free sectors open to FDI with own source of financing. However, for availing of such infrastructure facilities as industrial plots, gas, water, electricity, and telecommunications, a foreign investor may either apply directly to the concerned authority or approach the BOI for assistance in which case, the investor is required to submit the application along with a copy of the registration letter. The investors Facilities and Service Wing of the BOI, on processing the application, recommends the case to the authorities concerned, follow it up and informs the investor of the action taken. The relevant authorities responsible for infrastructure facilities are as described below.

Industrial plot: Planned and developed of plots of land are available for projects in BEPZA and BSCIC estates. Outside of these areas, there are four industrial estates

owned / controlled by city development authorities at Dhaka (RAJUK), Chittagong, Chittagong Development Authority (CDA), Khulna, Khulna Development Authority (KDA) and Rajshahi, Rajshahi Development Authority (RDA). Electricity, gas, water and telecommunication facilities are easily available in these estates. If required, BOI also recommends cases to the concerned authorities for acquisition of land for setting up industries. In these cases, the investors need to submit relevant papers and information in connection with the land to be acquired to the concerned Deputy Commissioners.

Gas supply: Applications may be made to Titas Gas Transmission and Distribution Company Private Ltd., or Bakhrabad Gas System Ltd. or Jalalabad Gas Transmission and Distribution Private Ltd. All these three companies are subsidiaries of the Bangladesh Oil, Gas and Mineral Corporation, a semi-government body.

Water supply: Within Dhaka Metropolitan city and Narayanganj Municipality, the authority is the Dhaka WASA (Water and Sewerage Authority), for Chittagong Metropolitan city, the authority is Chittagong WASA and for all other municipal areas, the authority is the Public Health and Engineering Department (PHED).

Electricity connections: There are three authorities namely, the Power Development Board (PDB), the Dhaka Electric Supply Authority (DESA for greater Dhaka only) and the Rural Electrification Board (REB, for rural areas not covered by PDB), to which approach should be made for the supply of electricity to the industrial site.

Telecommunicaiton service: The main authority is the Telegraph and Telephone Board (T & T Board), a government agency. A telecommunication company i.e., Bangladesh Rural Telecommunication Authority has commenced operation in the private sector. Cellular telephone service is easily available now.

(c) Other requirements and facilities:

In other to avail of the institutional support facilities, a foreign investor can apply to BOI for necessary assistance. Simple but prescribed forms are available for this. The main requirements and institutional support provided by the various departments / agencies are discussed below.

Registration as Joint Stock Company: In Bangladesh, a locally incorporated company may carry on a business and a foreign company incorporated outside but registered in Bangladesh. Prior to registration as an industrial undertaking, the sponsors of a project may apply to the Securities and Exchange Commission(SEC) along with a copy of the draft memorandum and articles of association for clearance of incorporation of the company. On clearance, the Registrar of Joint Stock Companies and Firms will register the company under the Companies Act, 1994.

Foreign credit: No approval is required for obtaining foreign credit in the form of foreign loans, suppliers' credit or PAYE (pay-as-you-earn) scheme in which the effective rate of interest is within LIBOR + 4 percent, down payment is less than 10 percent and repayment period exceeds 7 years. A copy of the foreign loan agreement signed by both parties is however required by the BOI for information and automatic registration of the same. For all other cases, the investor needs to apply to the BOI for approval. The BOI normally disposes of the fully documented cases within 7 days.

Import or raw materials and machinery: No import license is necessary for items on the free list such as raw and packing materials and machinery registration is however required for items on controlled list. Upon receiving applications, the BOI issues pass books (through the chief controller of imports and exports) within 30 days. Similarly, Import Registration Certificate (IRC) is issued by the concerned authority in favor of the investors within 30 days of receiving the application. For restricted items on the controlled list, BOI, BSCIC and BEPZA are responsible for assistance in importing these items.

The detailed procedures are as follows. The applications should accompany such documents as (a) GIR certificate; (b) Trade License (c) Membership certificate of relevant trade association /chamber; (d) Certificate from the nominated bank regarding opening of account; (d) Incorporation certificate (in case of limited companies); and (f) Letter of registration with BOI. After necessary field inspection, the BOI advises the client to deposit IRC and Pass book fees and submit the proof of the same for onward transmission to the office of the chief controller of imports and exports which then issues ***adhoc*** IRC and pass book. The former is handed over to the

applicant and the latter to the nominated bank. The investor then approaches his nominated bank for opening L/C for import. After going into commercial production, the investor may apply to BOI for regularization of the ad hoc entitlement.

It may be added that for import of raw materials and other inputs required for the pharmaceutical industry, the Drug Administration Department prepares block lists on a half-yearly basis.

Remittances: No approval / permission of the BOI is required for entering into agreements for remitting fees for the purpose of royalty, technical know-how and technical assistance if the total fees and other expenses do not exceed an aggregate limit of 6 percent of the cost of imported machinery and that of the previous year's sales of the firms as declared in the tax return. For information and automatic registration, the necessary documents to this effect are required by the BOI. For all other cases, prior approval of the BOI is needed. With necessary documents and copy of the relevant draft agreement, the investor will have to file an application to the BOI.

Work permit: For employing expatriate personnel, the investor will have to seek permission from the BOI in a prescribed form. Given certain conditions, initial employment for foreign nationals is considered for a term of two years extendable for further periods depending upon the merit of the case.

Safety measures: For anti-pollution safety measures and safety of working conditions in the factory, the investors are required to take clearance from the Department of Environment and register with the chief inspector of factories and establishment.

Monitoring and supervision: Monitoring and supervision, particularly after the industrial units go into operation, are essential for the productive operation of the project. In Bangladesh, the investors are needed to furnish quarterly report incorporating the basic data about the progress of the industry to the BOI / sponsoring agencies. The sponsoring agency then monitors the activities of the project and provides the necessary guidelines for future action.

(d) Setting up the plant:

Upon meeting the above formalities / criteria, the foreign investor can set up an industrial undertaking in Bangladesh.

Effectiveness of key institutions:

Although a large number of agencies are involved in FDI, the roles of BOI, BEPZA and EPB (Export Promotion Bureau) are crucial. It was the hope of the Government of Bangladesh (GOB) that these agencies would emulate the East Asian Investment Promotion Agencies which had served to underpin those countries' success in attracting foreign investment and technology transfer. In the following paragraphs an attempt is made to assess their role in investment promotion.

(a) The Board of Investment:

The BOI was established in 1988 primarily to act as a 'one stop shop' to help minimize transaction costs and reduce some of the risks and extra expenses associated with the regulatory system in Bangladesh.

The 'one stop shop' service idea has not worked. The relevant wing is named simply as "Service Wing". Although it was hoped that the demand for different infrastructural facilities land, gas, water, electricity and telecommunication could be met within the service wing of the BOI, in practice the service center cannot do anything but recommend the case to the departments / agencies concerned. In other words, the BOI still has to depend upon the usual bureaucratic channel for obtaining those critical facilities. The procedure has remained lengthy and cumbersome.

Reports suggest that transaction costs have remained as high as before (United Nations, 1998). Most of the BOI staff (700 plus) do not appear to be well-geared for the jobs they are doing. Since they are seconded to the Board from other departments, they continue functioning in a bureaucratic mode. The 1991 industrial policy categorically stated that the GOB would shift its policy from regulatory to promotional. To this end, it was declared even that registration would be voluntary, rather than compulsory. This however, seems to have little effect. Registration with

the BOI is compulsory if one wants to avail of the infrastructure facilities. Even if the firm in question does not require any such services through the BOI, it has to be registered for other services like reviewing proposals for foreign borrowings, certifying the eligibility to import restricted items, and issuing special passbooks for remittances relating to royalties, etc.

The role of BOI is limited even in cases in which it has been clearly empowered to take action. For instance, it is empowered to grant work permit to foreign nationals but has no say in the issuance of multiple visas. The fiscal incentives are administered by the National Board of Revenue (NBR) while the incentives relating to (say) remittance and export facilities are administered by the Bangladesh Bank.

The BOI is responsible for monitoring and supervision before and after the industrial units go into production. There are reasons to believe that BOI has not effectively discharged this responsibility. The main reason behind this failure is the non-cooperation of the investors to supply necessary up-to-date information to the BOI. BOI also does not insist apparently for fear of generating the ire of foreign investors, but the more reasonable explanation appears to be the lack of proper motivation and technical skills of the BOI staff.

(b) The Bangladesh Export Processing Zones Authority:

The Bangladesh Export Processing Zones Authority (BEPZA) was established through an act of parliament in 1980 for the purpose of implementing the "Open Door Policy" for attracting foreign investment into Bangladesh. This authority is the official organ of the government to promote and facilitate foreign investment in the EPZ areas only. Presently there are two EPZ areas in Bangladesh, one located at Chittagong (CEPZ) and the other at Dhaka (DEPZ).

The CEPZ, established in 1983, has so far 126 industries with an actual investment of $ 189.4 million. The DEPZ, created in 1993, has so far 68 industries with an investment of $ 63 million. The employment figures, as on 30 June 1998, stood at 39,574 and 17120 in CEPZ and DEPZ, respectively. The economic impact of two

operational EPZs in terms of investment drawing, employment generation, export earning, and other aspects are discussed in Chapter six.

Given the overall poor state of infrastructure and bureaucratic regulations, the EPZs have become very attractive to the foreign investors because of their superior infrastructure and their liberal import and exchange control regimes. The BEPZA can be regarded as the most successful agency engaged in attracting foreign investment in Bangladesh.

There is, however, another side of this picture. The BEPZA's relative success is said to be more a reflection of its special privileged status rather than its cost effectiveness, compared to similar zones operated in other Asian countries. Already doubts are being cast against the net benefits of FDI flows. It is stated that attraction of FDI through extensive financial, fiscal and other incentives and subsidized infrastructure facilities may not be worth the benefit. Benefits from the EPZ, industrial park etc. have been criticized by many. They argue that these incur huge amount of cost. although these attempts create some employment of unskilled workers.

(c) The Export Promotion Bureau (EPB):

The EPB is another important institution that has direct relationship with the promotion of foreign investment into Bangladesh. It is responsible for organizing Bangladesh's participation in international trade fairs. Observers believe that this promotional activity has been largely successful although there are some complaints regarding the selection of participants for the fairs abroad. A large number of staff of this agency are also criticized as being unskilled and having bureaucratic attitudes. Virtually, this is an extension of the Ministry of Commerce to which it is attached. It is suggested that aspects of EPB's promotional role be delegated to Chamber / trade bodies (World Bank, 1996).

In order to meet the challenges posed by the integration of global markets and the heightened competition for trade and investment from countries with similar labor-cost advantages, significant improvements will have to be made in the GOB's private

sector promotion agencies. The following recommendations made in a recent World Bank study (1996) deserve serious consideration.

a) A Prime Minister's private sector advisory council be established with membership of key economic ministers / secretaries and leading businessmen representing different sectors and regions. This council should meet at last once in a month to review the progress of foreign investment. For effective interface between the Government and the private sector business councils have been set up in many Asian countries including Malaysia, the Republic of Korea and Singapore.

b) The accountability of the promoting agencies (i.e. and the BOI, EPB and BEPZA) to clients should be enhanced. For this it is suggested that membership of their Boards / Oversight bodies should include their clients, i.e. private sector executives and exporters. These bodies should have the authority to hire and fire the agency heads.

c) The promotional agencies (particularly BOI) should be made more efficient and cost-effective. Pending reorganization, hiring professional staff and phasing out redundant staff (almost two - thirds) of the BOI should be urgent priorities. Greater flexibility in recruitment will be necessary, and pay scales must be separated from those of the civil service to enable them to draw on private sector talent.

d) Unnecessary regulation and control functions of these agencies (such as the EPB's issuing of export licenses) should be removed.

(e) Given the similarity of functions, it is recommended that the BEPZA is merged with BOI. This would help reduce not only the overhead costs but also help improve the overall management.

(d) Administration of the regime of financial incentives:

The incentives offered are administered by a large number of agencies and departments having very little coordination among them. Efficiency of these institutions in terms of speed, fairness etc. leaves much to be desired.

First, the most tangible incentive offered to the foreign investors related to export-oriented industries (defined as those directly) exporting 70 percent or more of the total

value of their products). These industries are given access to tax - free imports of intermediate inputs (except a few) and access to all imported inputs including banned or restricted items. The NBR outside the EPZs provides bonded warehouse (BW) facilities similar to those available at the EPZs. This provides for clearance of imported materials free of taxes. This facility is not however automatic. The investors need to apply to the concerned Collector of customs for a license to won and operate the BW. License is given provided the collector has at his disposal adequate number of trained staff for supervision for which the physical location of BW is also a consideration. The BW operator is also accountable for waste materials and foreign exchange earnings to the satisfaction of another agency, i.e., the Bangladesh Bank. The procedure is therefore considered somewhat lengthy and complex.

The foreign investors of 100 percent export-oriented industries can also avail of the facility of Duty Drawback (DD) in place of BW facility. The procedure of calculating this DD has remained cumbersome. This involves, among others, determination of input-output coefficients, scrutiny, inspection and survey. The concerned agency (NBR) has however taken enough steps in speeding up the process of Duty Drawback. The extent and spread of international production activity are gauged from the number of enterprises that are involved in it and their various dimensions in host countries.

In Bangladesh, FDI started to gear up since 1976. The trend and performance of FDI in Bangladesh are, therefore, evaluated in next chapter five within the policy presentation as contained in the New Industrial Policy'1999.

CHAPTER- V

TREND AND PERFORMANCE OF FDI IN BANGLADESH

Foreign Direct Investment (FDI) generally comprises all transfers of finance and intangible assets (Brewer, 1991). Traditionally, such investments were in the form of whole or majority ownership. In recent times, however, there has occurred a proliferation of new forms of minority ownership including a variety of non-equity contractual arrangements (Reza, 1995). In this section our analysis confines both to majority or minority equity participation and non-equity forms of foreign enterprises. We however, start our discussion by analyzing the majority or minority equity forms of MNCs in Bangladesh, followed by non-equity forms of participation.

The success of FDI policies can be judged by the size of the inflow of capital. Bangladesh has been making efforts to attract FDI and such efforts have been intensified with the advent of deregulation, privatization, and liberalization policies initiated at the beginning of the 1980s. The table-1 (in the appendix-I) documents the trend of FDI flows in Bangladesh during 1977-78/1998-99. The amount of sanctioned investments, excluding the investments in Export Processing Zones, totaled about Taka 7373 million (in current price) for a total of 318 sanctioned units during the period under investigation.

One noticeable feature (table-1) is that the difference between the number of units sanctioned and that actually gone into production has gradually been diminishing, particularly, since the fiscal year 1985-86. About 50 percent of the recently sanctioned FDI units are reported to be in production (GOB, 1999). As a result, the real magnitude of FDI inflow into Bangladesh has been declining.

Significant periodical and annual variations have also marked the inflow of FDI. The peak inflow was registered in 1997-98, after major policy reforms were introduced in the economy in the early nineties. Another notable feature emerging from the table-1

is that overall quantum of FDI flowing into Bangladesh coincides with changes in the governments and policies. With changes in state power in 1981, 1990, and 1995 a discernible pattern in the bulk of FDI inflows can be traced. The figure-1(a) clearly demonstrates the trends of FDI flow in Bangladesh between the time period 1977-78 and 1998-99 in terms of total sanctioned units as well as the number of units in production and the figure-1(b) shows the trend of the amount of investment in the sanctioned units between the same time period.

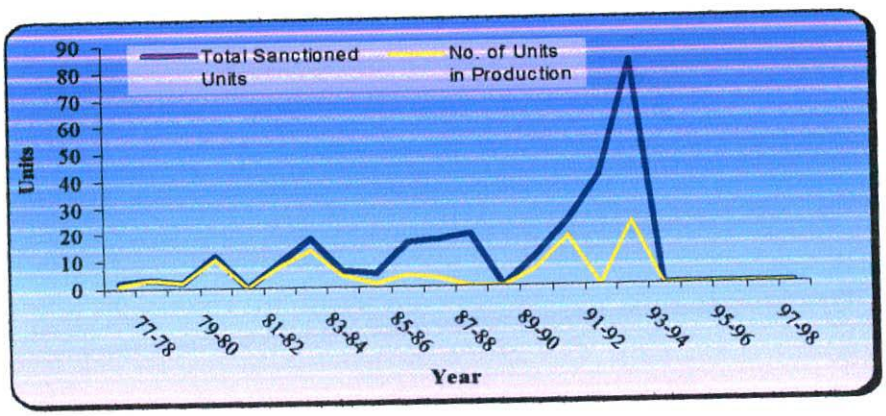


Figure-1(a)

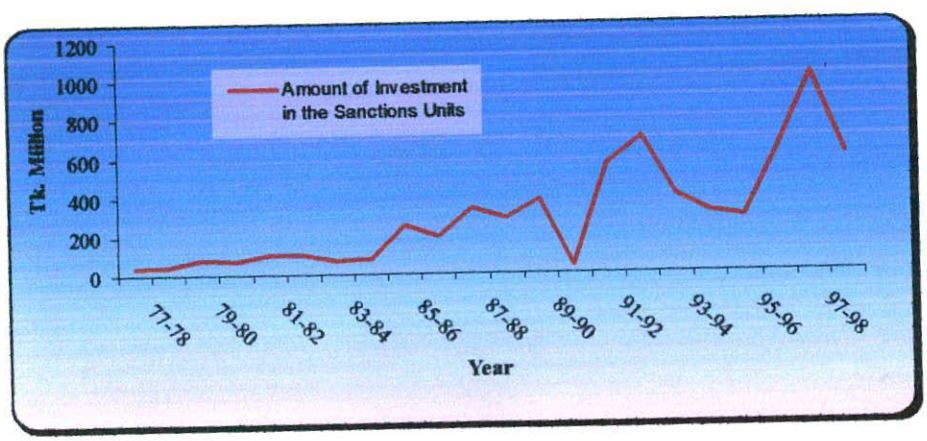


Figure-1(b)

The negligibly low inflow of FDI in Bangladesh can at least partly be explained by historical factors. The general characteristic of foreign investment in the fifties and the early sixties was that FDI was attracted to export-oriented extractive industries and production of agricultural cash crops. Bangladesh had little to offer in this direction. Except for jute, which had a significant export market and tea to a lesser extent, Bangladesh had precious little in the nature of extractable resources or agricultural cash crops, which had an export potential so as to generate interest amongst the foreign investors (Reza, 1987). In addition to the disadvantage of having

a poor natural resource base, there was a second factor that militated against the inflow of foreign capital into pre-liberation Bangladesh.

The economy of Bangladesh (the then East Pakistan) was considered by West Pakistani business house to be a "captive" market which was to be controlled and thereby exploited (Sobhan, 1981). The political and administrative machinery of Pakistan, controlled by West Pakistanis, ensured this by enacting laws that favored investors from the West wing of the country and discriminated against the foreign investor. The result was that, in Bangladesh, foreign investment was pre-empted by West Pakistani investment and the economy was dominated by West Pakistani capital. This pattern of a negligibly low level of foreign investment continued in independent Bangladesh up till 1975 (Reza, 1995).

The Government of Bangladesh, in the immediate post-liberation period, was committed to a Socialist pattern of development and, hence, had nationalized a large part of the industrial sector. The pattern of development pursued was such that not to speak of foreign capital, even domestic private capital had little role to play in it. It is, therefore, not surprising that foreign investment shied away from Bangladesh. As a result, the inflow of FDI into Bangladesh in the immediate post-liberation years remained negligible.

With change in state power in August 1975, the environment became significantly conducive to inflows of foreign investment. The successive governments made efforts towards attracting liberal measures aimed at ensuring increasingly greater flow of foreign investment (stated above). This resulted in a rise although marked by significant annual variations in foreign capital inflow in Bangladesh. The increasing trend in the FDI flow continued unabated except for the year 1981/82. The rate of increase has been particularly pronounced since 1982. This may be attributed as a result of favorable change in the policy environment encouraging both domestic and foreign investment.

The increasing trend was again disrupted by political turmoil in 1990. Again with change in state power in 1991, the government had been pursuing significant market-

oriented reforms for increased private sector investments, which had yielded some favorable results. Evaluating the foreign investment climate, the joint Euro-money Publication of UK and the Bangladesh Board of Investment conference in January 1995 at Dhaka has referred to the Bangladesh economy as the emerging tiger (Reza, 1995)

The impact which foreign investment can make on the economic development of the host country depends upon its volume and its share in gross national product, as well as upon the sectors and conditions of its investment. Both as a ratio of total investment and of imports, the contribution of FDI are extremely negligible in Bangladesh. The shares of FDI to total investment and imports (Table- 2) have been minimal-less than 0.3 percent of the country's total investment (between 1977-78 and 1999-00), despite alluring package of benefits offered by the government of Bangladesh to attract FDI.

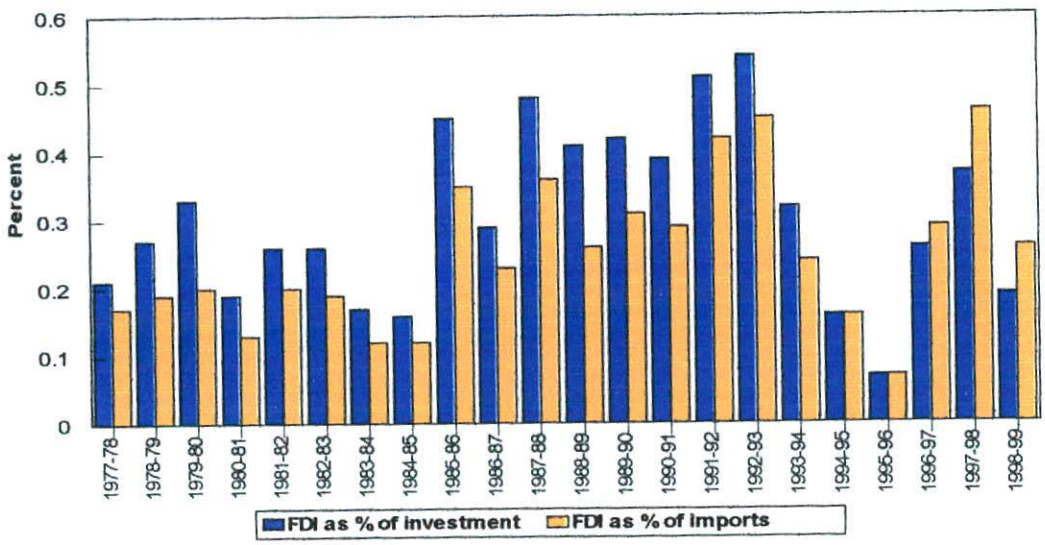


Figure-2

The Bar Diagram (figure-2) exhibits FDI in Bangladesh as percentage of total investment and import from 1977-78 to 1999-2000. The Bar Diagram also discerns marked fluctuations in the percentage of FDI. The figure-2(a) represents the indexes of total investment, FDI and import from the time period 1977-78 to 1999-2000.Among the three indexes, the magnitude of fluctuation is the highest in the FDI flow.

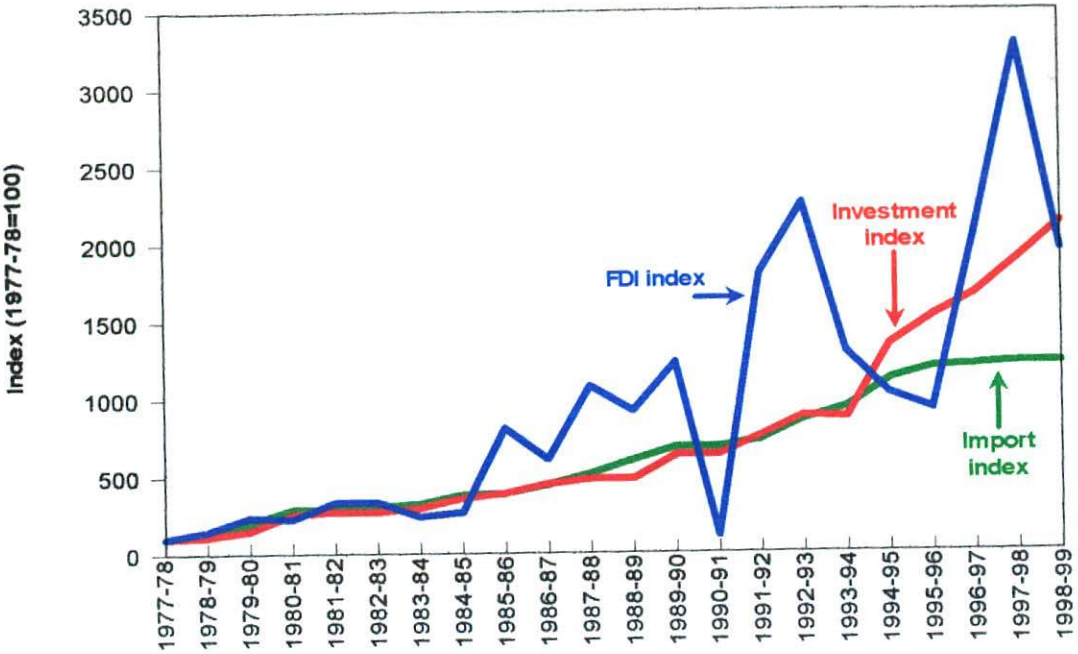


Figure-2(a)

Bangladesh remains far below in attracting FDI in the global context. Measuring FDI as percentage of GNP, Brazil, China, Mexico, Malaysia, Indonesia, Thailand, Argentina and Chile have been among the top 12 recipients in the three successive 10-year periods from 1970 to 1999. These countries received FDI flows greater than 2 percent of their GNP (Table-3). The ranks of top twelve recipients of FDI among the developing countries in three different time periods are exhibited in the Scattered Diagram (figure-3).

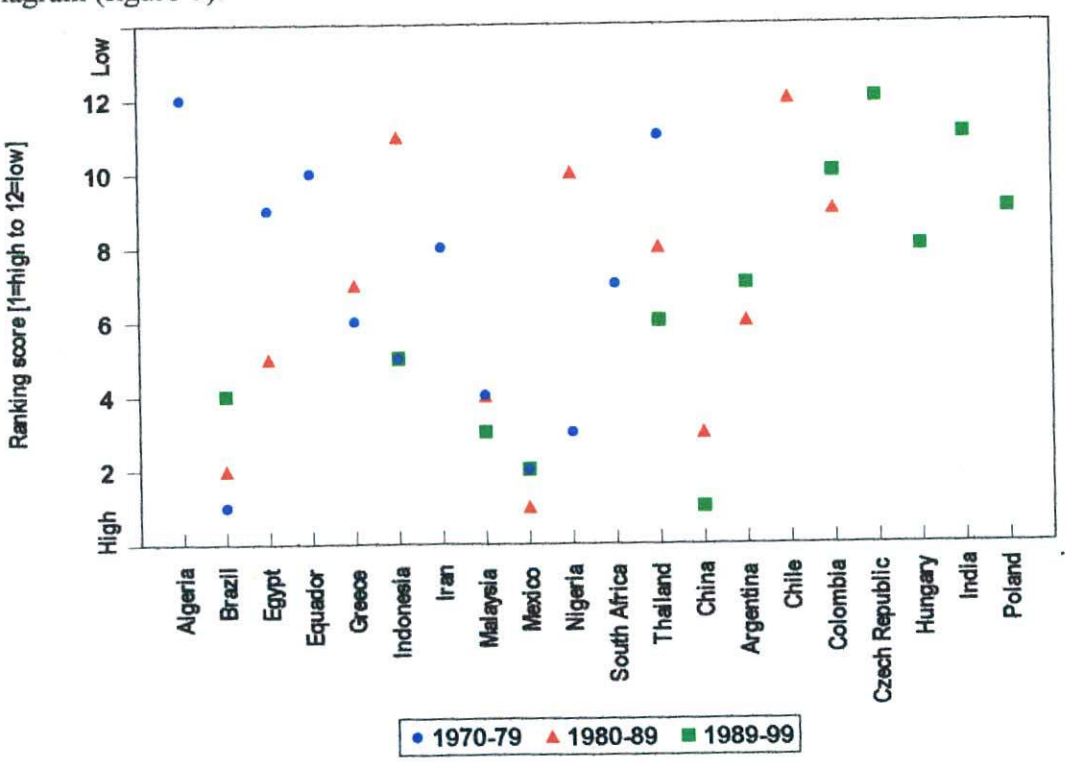


Figure-3

Compared to low-income Asian countries, Bangladesh remains way down the list, with FDI of 0.001 percent of GNP, against India's 0.8 percent (UNCTAD, 1999). The FDI flowing into Bangladesh has been the lowest in all times among the selected Asian countries (table-4). Although some positive improvements have been observed in the recent past, FDI is seen to have played a very minor role in Bangladesh both as a ratio of total resource inflows and of gross domestic capital formation up till now. This reflects that Bangladesh lags far behind in restructuring growth and orienting its policies to encourage FDI.

STRUCTURAL COMPOSITION OF FDI

In Bangladesh, FDI consists primarily of three elements: (a) capital brought in, (b) capital equipment brought in, and (c) re-invested earnings. This information is given in the table-5. The table shows that the structure of sources of financing has undergone a noticeable change during the period 1977-99. The majority of the FDI came in through direct remittances from abroad in the form of cash (52 %) in 1977, but the share of such remittances had gone down to only 11 percent in 1999. This exogenous financial flow of capital is supplemented by capital equipment imported into the country in lieu of, or in part payment of, a foreign investors' equity share. This component i.e. capital equipment brought in has, however, never risen above 48 percent in one year (1998), with lowest limit in 1980, 1986,1987, and 1988.

The share of the re-invested earnings in total FDI, in contrast, increased from 45 percent to 97 percent during the same period. Despite some variations in this pattern, particularly in the early nineties, this tendency for foreign investors emerged as the principal source of capital (derived from their operating surpluses). The largest share of re-invested earnings in total FDI may imply that all such investments do not represent net transfer of resources from abroad into Bangladesh. Because, compared to freshly imported capital, re-invested earnings originate as savings from investment previously made. It may also be mentioned that the resort to internal sources of financing was not limited to re-investment of earnings. A number of foreign investors resort to term financing either from the Development Financial Institutions (DFIs) or the commercial banks in Bangladesh. Such earnings could, under law, be transferred out of the country after payment of taxes. To that extent even FDI originating from reinvested earnings has an opportunity cost to the foreign investors.

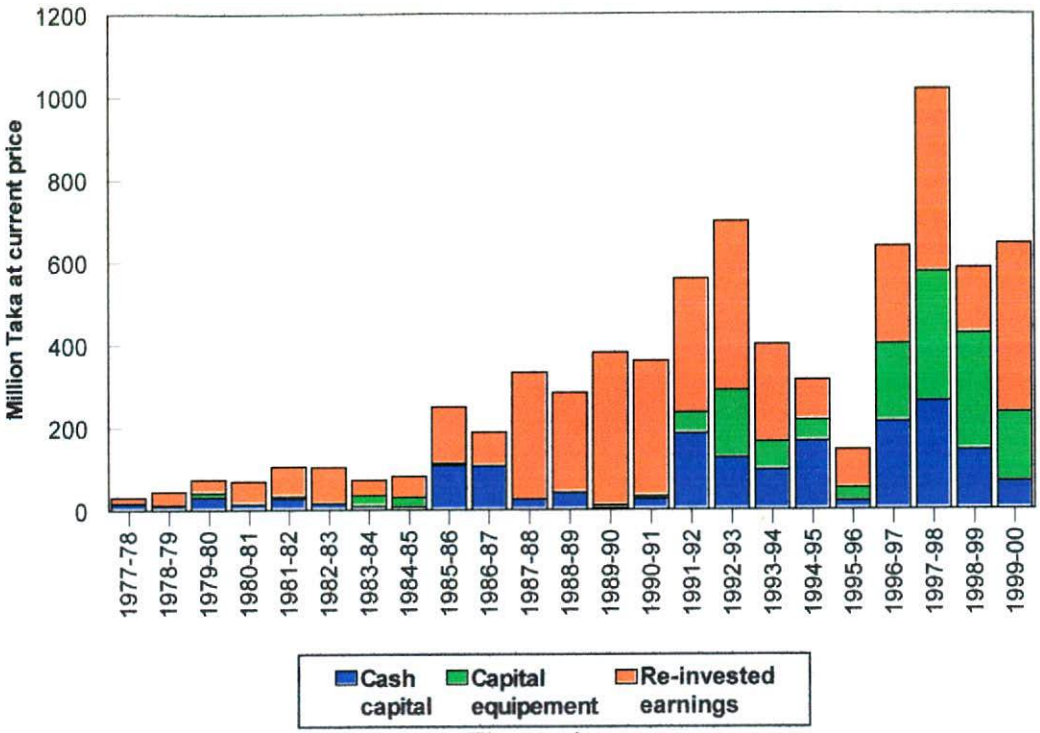


Figure-4

The amount of cash capital brought in, capital equipment and re-invested earning at current price from 1977-78 to 1999-2000 is shown in the Bar Diagram figure-4. The percentage share of these three components at current price is given in the figure-4(a).

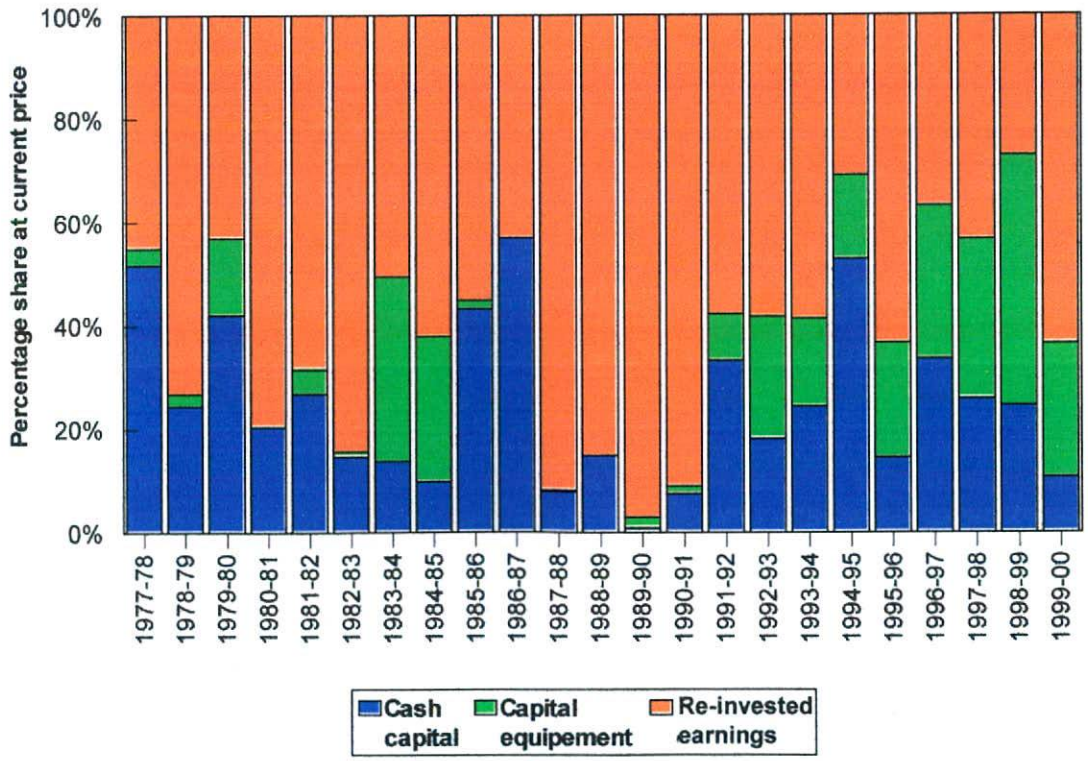


Figure-4(a)

By analyzing the structural elements of FDI in Bangladesh, three conclusions can be drawn. Firstly, re-invested earnings became the dominant forms of FDI in Bangladesh during the entire period under consideration. Secondly, the item labeled capital equipment brought in has never constituted a significant element in the structure of FDI except for three or four years, suggesting limited technology transfer by MNCs in Bangladesh. Thirdly, the share of major element of FDI, which includes cash capital inflow, has never risen above 40 percent of the total investment except in 1977, 1986, and 1994. Country-wise structural composition of FDI, that is, (a) capital brought in, (b) capital equipment brought in, and (c) re-invested earnings are shown in details in the Tables- 6, 7 and 8 respectively.

Figures-5(a)and 5(b) show the percentages of cash and capital equipment brought in by six developed countries respectively and the figure 5(c) shows re-invested earnings invested by eight developed countries.

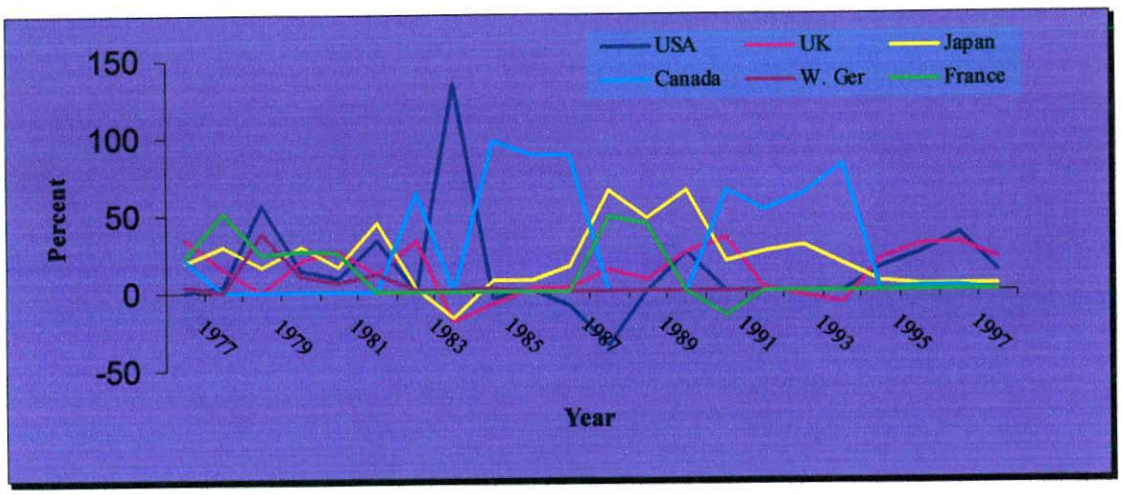


Figure-5(a).

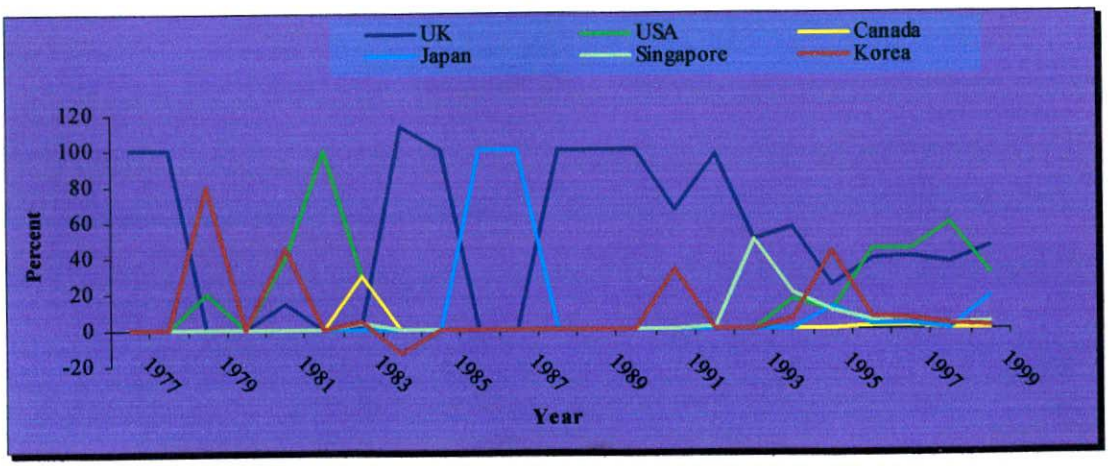


Figure-5(b).

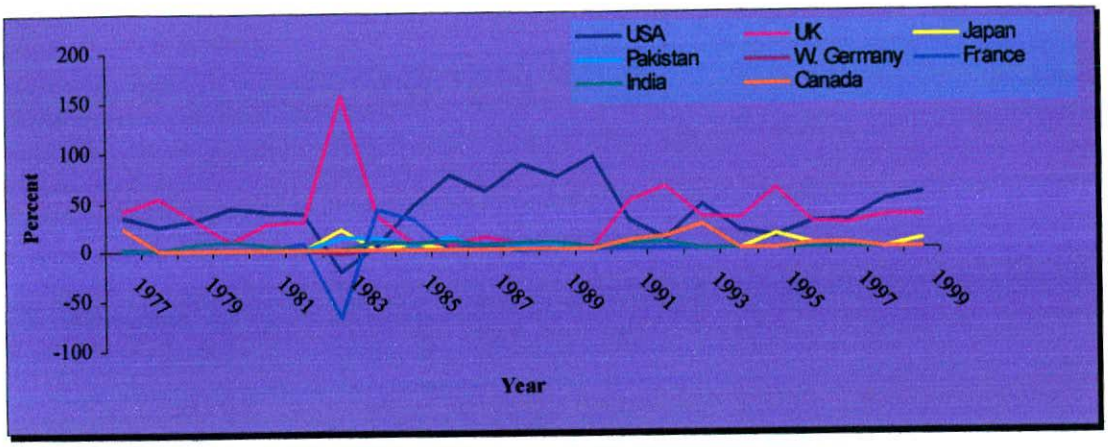


Figure-5(c).

SECTORAL COMPOSITION OF FDI IN BANGLADESH

The analysis of sectoral distribution of FDI manifests two things: (i) the preferential treatment of the host country government given to certain sectors while encouraging FDI, and (ii) foreign investors' own preference to certain sectors (Reza, 1995).

The flow of FDI in Bangladesh has undergone a structural change when analyzed by economic sectors at the national level. Sectoral composition of FDI flows into Bangladesh also exhibits considerable year-to-year fluctuation. Data presented in the table-9 show that manufacturing industries and commerce are the sectors, which have traditionally dominated the preferences of the foreign investors up to 1990.

The sectoral share of manufacturing industries has witnessed sharp decline from 45 percent in 1977 to 25 percent in 1982, revived in 1983, may be as the aftermath of the introduction of the New Industrial Policy when it reached an all time high share of 82 percent, and significantly declined since then.

The share of commerce, on the contrary, is seen to have increased continuously between 1977 and 1990, tapered off temporarily in 1983 and started increasing again since 1984, rising to over 92 percent in 1989 and 1990.This increasing trend is however, continued to decline almost steadily from 55 percent in 1991 to 18 percent

in 1999. The increase in the sectoral share of commerce seems to have taken place at the cost of the decrease in the shares of manufacturing and miscellaneous industries sectors. The turning point of this structural change is marked by the year 1990 when the share of manufacturing industries fell to its lowest of 2 percent and that of commerce reached its highest level of 92 percent. The share of FDI in three major economic sectors (e.g.manufacturing, commerce and the rest) compared to total FDI inflow from 1977 to 1999 is shown in the Bar Diagram (figure-6).

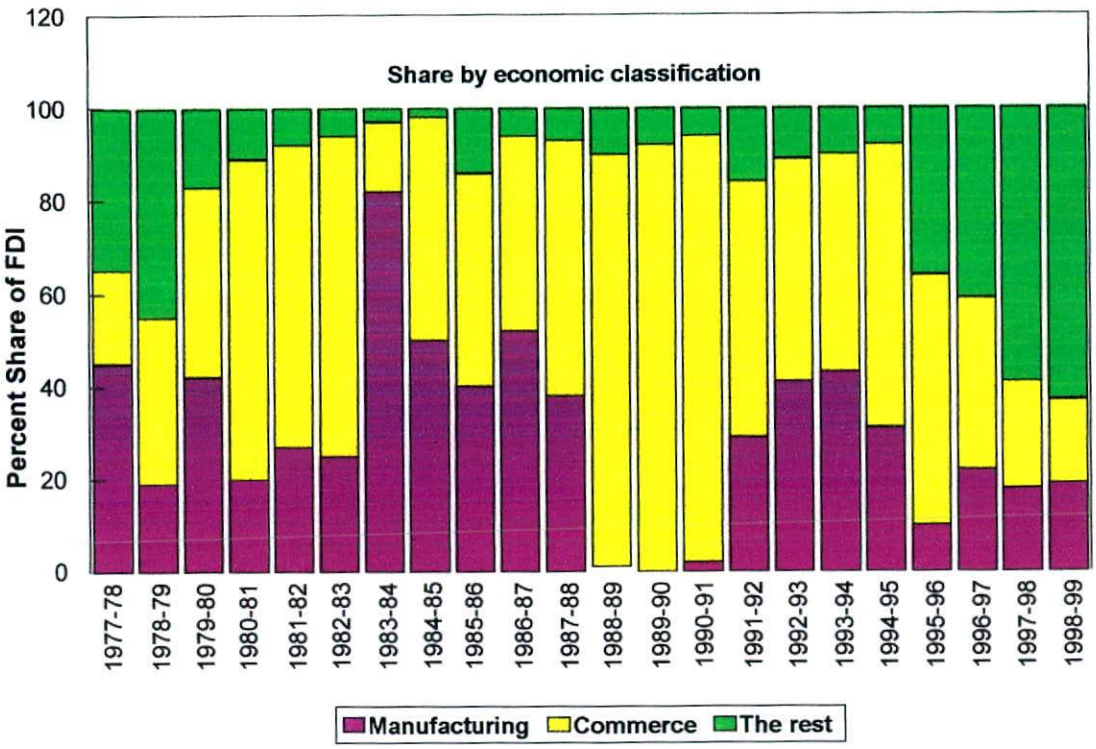


Figure – 6

* The rest include agriculture, mining and quarrying, construction, transportation and communication and miscellaneous sectors.

Movement of FDI from manufacturing to trade and commerce is a feature not confined to Bangladesh alone but has been observed in many developing countries as a whole during the decade 1980 to 1990 (IFC, 1997). Like in Bangladesh, trade and commerce have the dominant recipient of FDI in other developing countries, such as, Argentina, Malaysia, Brazil and Pakistan, "because of higher profits and lower risks" - the two propelling forces motivate the foreign investors while taking any decision to invest in abroad (World Bank, 1994). The increasing interests in commerce have also

probably been accompanied by increasing liberalized trade and industrial policies introduced in Bangladesh particularly since the beginning of the eighties.

In the remaining economic sectors - agriculture, transport and communications, and construction-flow of FDI has been insignificant and erratic because of the limited opportunities open for foreign exploitation in these areas. Another important feature of the structure is that in recent years the two sectors-mining and quarrying-have been attracting significant amount of FDI. According to the Bangladesh Economic Review (1999) these two sectors have attracted more than 40 percent of total flows of FDI in Bangladesh, as reflected in the table-10.

Figures-7(a) and 7-(b) both represent the distribution of FDI percentage in Bangladesh in three broad economic sectors such as manufacturing, commerce and the rest from 1977 to 1999. Both the Bar Diagrams obviously show that commerce all the time holds the top position, followed by manufacturing and the rest sectors.

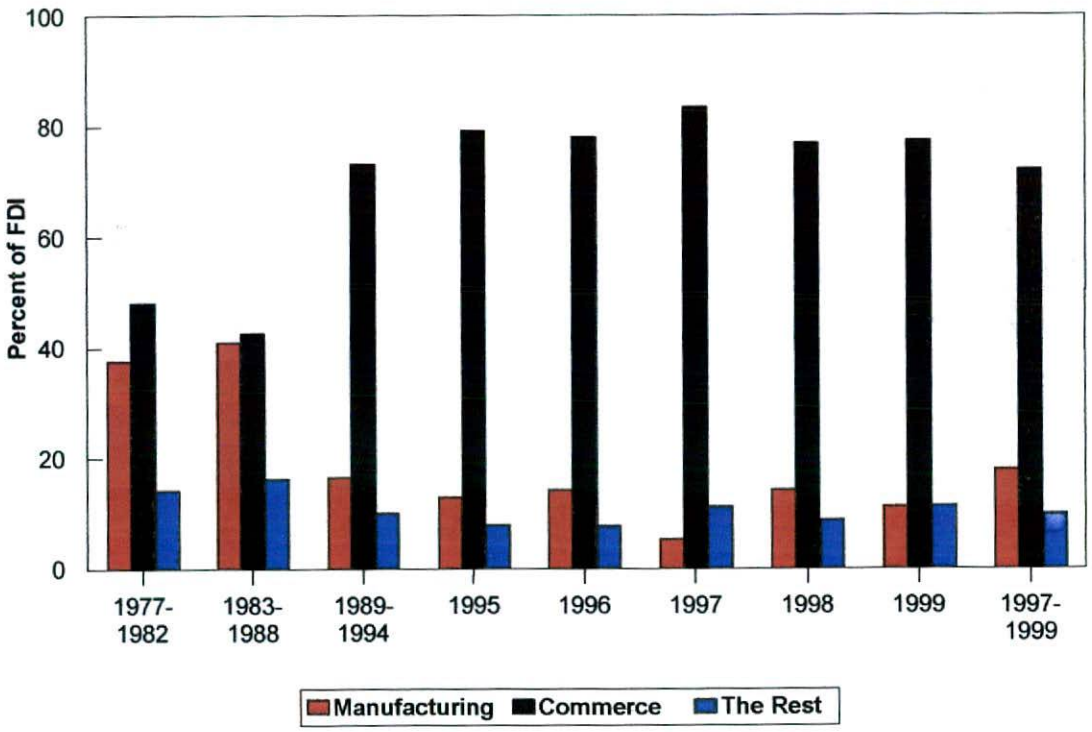


Figure –7(a)

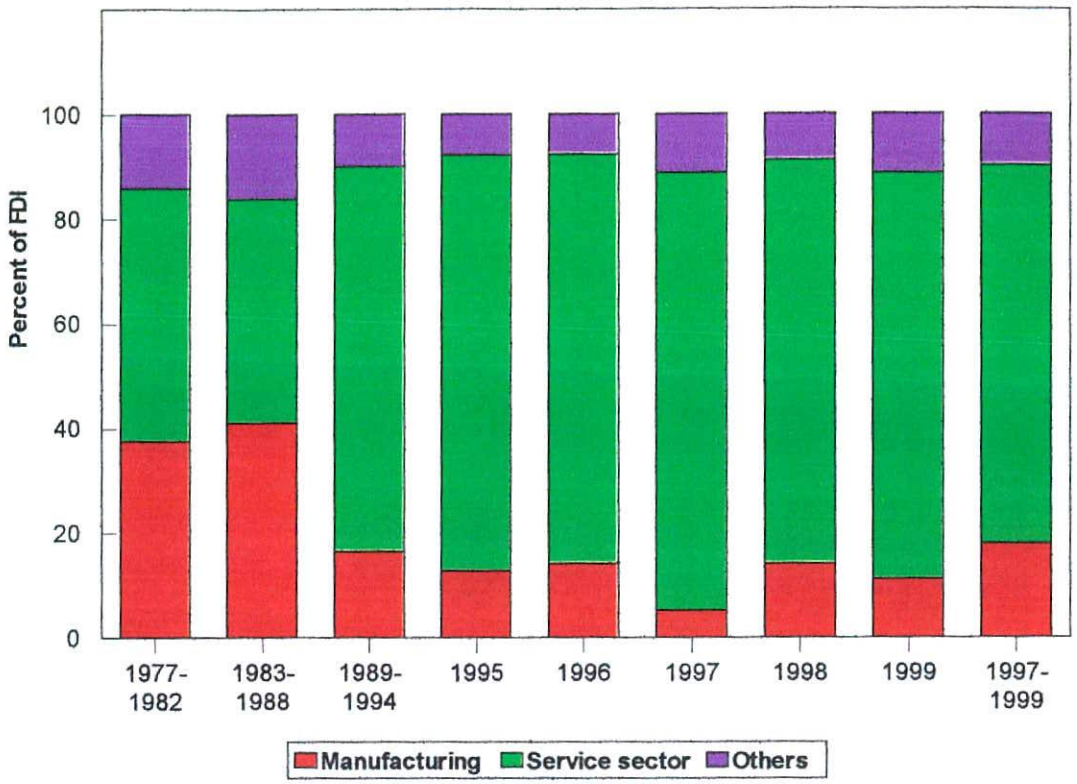


Figure –7(b)

* Others include agriculture, transportation construction and miscellaneous sectors.

As noted earlier, Bangladesh has few agricultural cash crops with export potentials which could attract foreign investors. In tea, prospects of any additional foreign investments are limited. Foreign participation in such other areas as gas and petroleum, are often generated controversies within the country.

INDUSTRIAL DISTRIBUTION OF FDI IN BANGLADESH

The industrial distribution of foreign investments in Bangladesh during the period 1977-99 is presented in the table-11. Table depicts some visible changes in its composition over time. Prior to independence, pharmaceutical and chemical industries were seen to have dominated in attracting the bulk of FDI (Siddiqi, 1983). A total of 37 joint-venture firms are reported to have been in operation before the independence of Bangladesh, of which 28 were operating in these industries. Concentration of foreign investment in these industries is attributed to the import substituting industrialization strategy pursued by Pakistan prior to 1971 (Reza, 1987).

Medicine and fuel were two essentially needed commodities, which had to be imported at significant foreign exchange cost. Therefore, the government decided on manufacturing these locally, behind high protective walls, but since local initiative was lacking in terms of both the amount of capital required and the technology to be used, foreign investment was allowed to enter these two industries. However, the relative importance of the pharmaceutical and petroleum industries has diminished in post- independence Bangladesh.

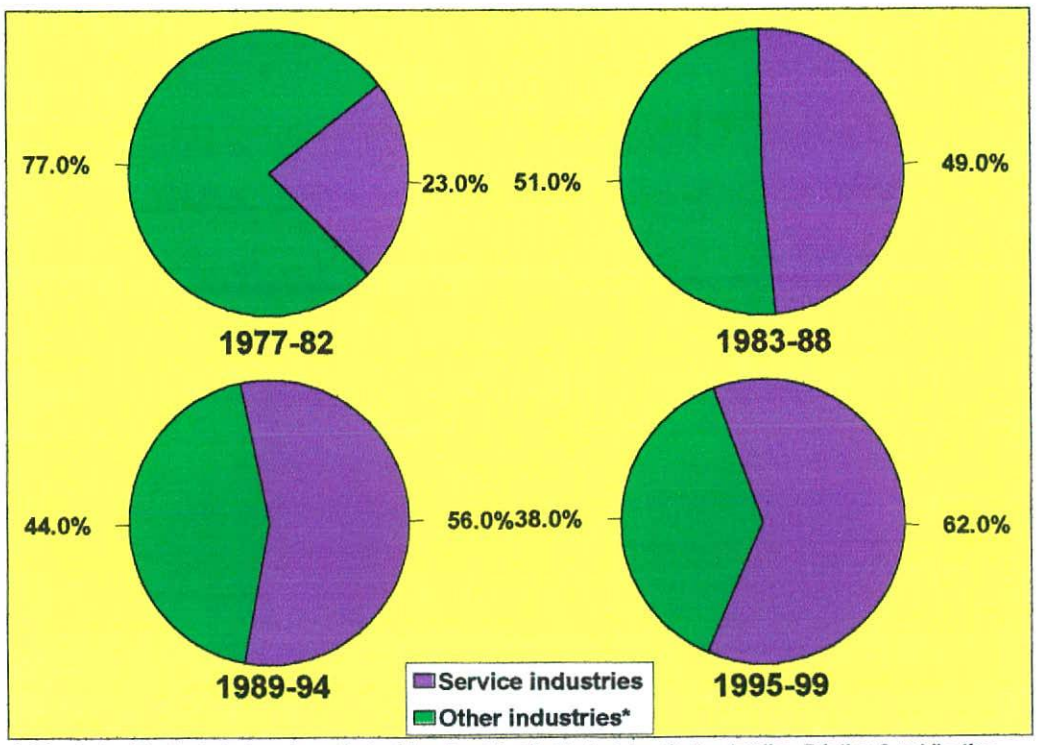
The Drug Policy introduced by the government of Bangladesh in 1982, which prohibits production of several medicines mainly manufactured by TNCs has doubtlessly discouraged and even forced withdrawal of some foreign investment from the pharmaceutical sector.

Mainly service industries followed by textiles (primarily ready-made garments, textile spinning mills and hosiery units), and chemical industries have subsequently dominated the inflow of FDI. During the period 1977-99, these three industries together accounted for over 70 percent of the total private foreign investment. The other industries attracting FDI include metals (4.58%), electrical goods (4.77%), and food and allied industries. The recent change of sectoral-mix is an indication of increasing diversity in the industrial composition of FDI flows in Bangladesh.

Compared to the earlier trend, the foreign investors now seen to be interested in making investment in a number of export-oriented products. The most significant stride with regard to export-oriented products, has been the ready-made garments industry, whose share in export earning was 12.4 percent in 1984 but now (1999) accounts for more than 76 percent (GOB, 1999). This change of sectoral emphasis of FDI may in part be explained by the overall shift of the development policy of Bangladesh towards a more export - oriented growth strategy designed to attract foreign capital into sectors with export prospects.

In addition to the increased export promotion incentives, a factor which might have motivated the foreign investors from many Asian countries to move into garments sector is the rising labour costs at home and the relatively low labour costs in

Bangladesh (Reza, 1995). The quota free export market status of Bangladesh in the earlier period also acted as a strong incentive in this regard. The other notable trends about FDI in Bangladesh are: (i) the operations of the foreign firms in the electrical goods and electronics industries have remained primarily import-substituting in nature; (ii) almost in every year between 1977-78 to 1998-99, one or two investment proposals accounted for the bulk of total FDI flows; (iii) new investors appear declined to stake their equity in areas where there is already a sizeable transnational presence.



* Other industries include Agro-based industries, Food & allied industries, Cotton textiles, Printing & publication, Leather production, Chemical industries, Metal industries , Engineering industries, and Miscellaneous.

Figure- 8

Four Pie charts for four different periods are presented in the figure-8. Pie charts clearly show that as an individual sector the contribution of service sector to FDI in Bangladesh was remarkably significant and ranked first position all the time. Sector-wise FDI percentage in Bangladesh in four different time periods is also exhibited in the figure-8(a). The figure-8(a) also shows that the FDI in Bangladesh in service industries compared to all other sectors was most of the time highest.

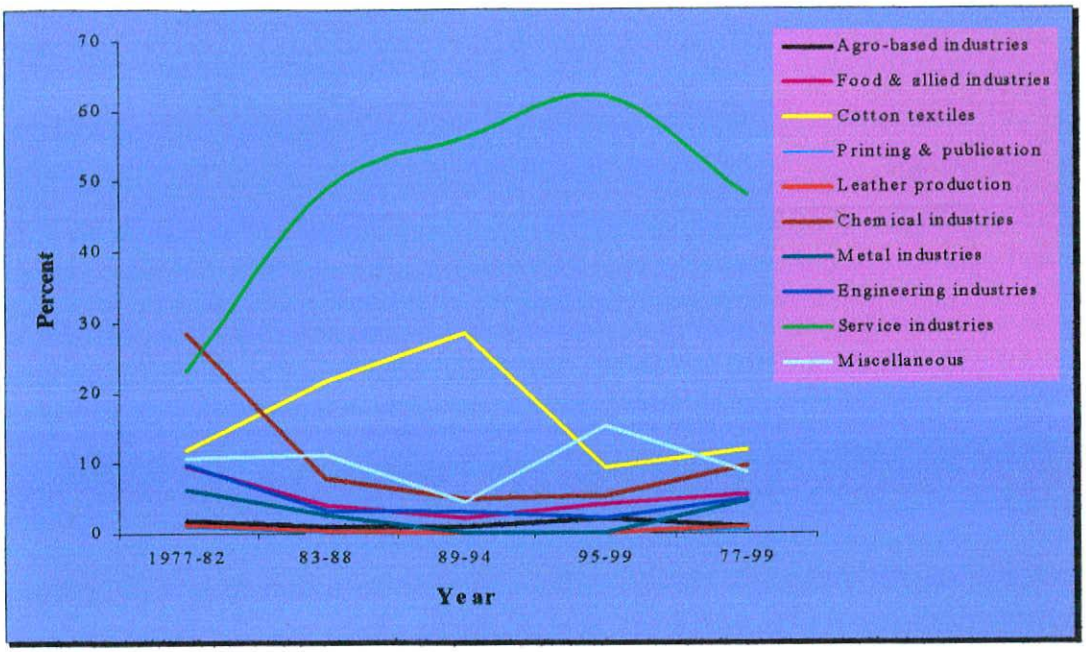


Figure- 8(a)

In the post liberation period, for example, the traditional sectors preferred by foreign investors, such as petroleum drilling, refining, inland water transport, and tea companies attracted few new investors at all up till 1994. While the "miscellaneous" sector commanded, on average, 8.5 percent of FDI, the other important sectors such as machinery and equipment, electronics, and electrical goods combined did not account for even 5 percent of the FDI in between 1977 and 1999, suggesting the very limited contribution of FDI to technology transfer in Bangladesh.

FLOW AND MODE OF FDI ACCORDING TO COUNTRY SOURCES

Through long 25 years partnership with Pakistan during 1947-71, Bangladesh (the then east Pakistan) was able to attract only 27 MNCs, of which 21 companies were from Europe and 14 of them were from United Kingdom alone (Siddiqqi, 1983). There were only 4 companies from America. Only two countries, namely Japan and Malaysia were involved in joint-venture project in Bangladesh from Asian countries (Jamal Uddin, 1986). This pattern however, has substantially changed after independence, with Asian countries emerging as equally important as the developed market economies in terms of the volume of investment.

As can be seen from the table-12 that during the seventies, the high income countries", originated mainly from Western Industrialized economies had dominated foreign investment in Bangladesh. British and German MNCs, which were operating in Bangladesh since the Pakistan days, continued to infuse new capital into their ventures. The seventies also witnessed the entry of the Asian investors into Bangladesh. Participation by Asian Investors / firms, particularly from the newly industrialized economies such as Hong Hong, Singapore, and Thailand increased rapidly during the decade of the eighties; though the foreign investors from high - income countries also stepped up their operations in Bangladesh during the decade (Jamal Uddin, 1986). The figure-9 shows country-wise percentage of FDI flow in Bangladesh from 1991 to 1998. The figure-9 demonstrates that UK, USA, Canada and Singapore are the major countries from which substantial amount of FDI inflow comes.

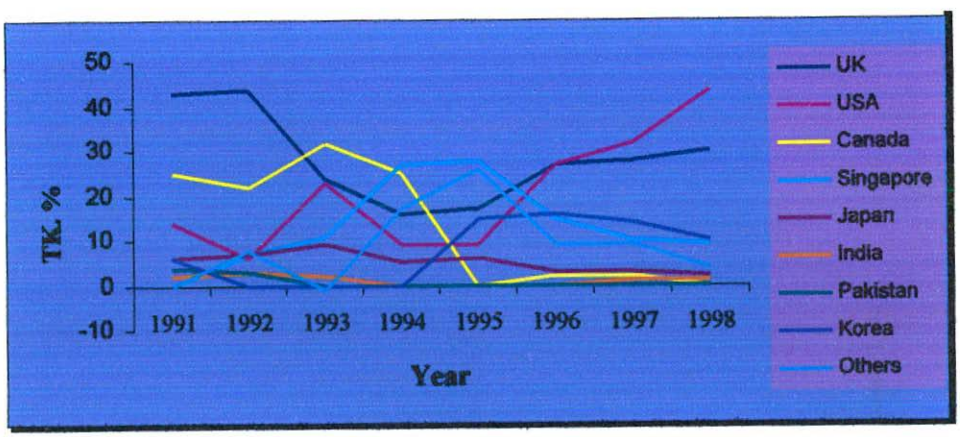


Figure-9

Country-wise distribution of FDI also reveals that investment from India, China and South Korea dominated the scene in 1987-88, 1990 and onwards. The other two notable features are: (i) in aggregate terms, the amount of foreign investment from the developed market economics exceeded that from the Asian countries up to the end of the eighties. The situation has turned dramatically by 1994, when the middle-income countries' share in FDI flows to Bangladesh become more than two - third of the total investment; and (ii) the post - liberation FDI is that it has been mostly of the joint - venture type. Based on the analysis of investment composition of 99 firms from development market economies and 76 firms from Asian countries up to 1993, Reza (1995) found that FDI through equity participation has been the dominant mode of investment in Bangladesh.

NON -EQUITY FORMS OF MNCS PARTICIPATION

Though FDI through equity participation remains the dominant form in Bangladesh, investment by foreigners have also taken various "non-equity" forms. They refer to international business operations, which lie in a gray area between traditional FDI and traditional export operations. Examples would include less-than-majority-owned joint ventures and various contractual forms such as technical licensing, franchising, counter trade, co-production agreements, technical assistance, management agreements, marketing assistance, turnkey operations, and international subcontracting (Oman, 1984)

Forms of non-equity participation by foreign firms are presented in the table-13. Lack of any systematic record keeping by the concerned agencies, we could not determine in any meaningful way trends in non-equity forms of MNC participation in Bangladesh. However, Reza (1995) identified a total of 106 of such non-equity agreements in the private sector since 1976.The table-14 shows that technical collaboration has been the dominant form of non-equity participation by MNCs between the period 1976 and 1993, followed by licensing and technical know-how, royalty, and technical assistance.

The table-15 presents data on non-equity participation by MNCs according to the broad industrial groups. The important industries in which a large number of non-equity agreements have been made are machineries, chemicals, electronics and pharmaceuticals. This is in contrast to high equity participation in such other industries as textiles and food processing in which new non-equity forms of investment appear to be of insignificant magnitude. This pattern may be explained primarily by technological factors.

Though these industries are apparently more technology-intensive, the level of technology involved in the operations in Bangladesh is not high enough to warrant the desire of MNCs to exercise control over the technological assets through ownership. In the more traditional industries, with a larger domestic market, greater equity

involvement is possibly also dictated by other considerations, including the availability of cheap labor and fiscal incentives.

Another interesting characteristic of non-equity agreement in Bangladesh is that, except for United Kingdom - the country with which Bangladesh has had economic relationships from colonial times, a relatively large number of agreements have been made with enterprises originating from developing countries. A recent study found that out of 80 non-equity agreements made so far with 10 countries, the number of such agreements with firms originating from India is 19 (24%), followed by South Korea (8%) and China (4%). At the policy level, this warrants more intensified efforts to explore possibilities of greater non-equity collaboration with firms from those countries who may be agreeable to better terms and conditions, including the ones in the spares of technology transfer, than the established MNCs from the developed countries. More diversified geographical source may help improve the bargaining position of a country like Bangladesh vis-a-vis the MNCs from the industrialized countries.

GEOGRAPHICAL DISTRIBUTION OF FDI WITHIN BANGLADESH

The pattern of regional distribution of FDI flows into Bangladesh has been overwhelmingly skewed in favor of the largest urban centre of the country, namely Dhaka. Administratively, Bangladesh is divided into six divisions, namely Dhaka, Chittagong, Khulna, Rajshahi, Barisal and Sylhet. Data on regional distribution pattern of FDI flow into Bangladesh is scanty as well as of doubtful validity. On the basis of addresses of the foreign firms sanctioned by the Board of Investment, it was found that, in terms of amount of investment and number of firms, the overall locational pattern (of FDI) is highly concentrated in the major urban centers of the country in Dhaka division. Data presented in the table-16 show that among the six divisions of Bangladesh, Dhaka division attracted the highest number of foreign investors (78%) during 1977-99.

The geographical distribution of FDI by major industry sectors also exhibits similar locational concentration. Except for food processing industry where the regional

distribution of FDI is somewhat less concentrated in Dhaka, with Chittagong receiving over 44% share, Dhaka division has been the most dominant center of attraction for all other industries. Remaining four divisions, including Khulna with seaport, have failed to attract foreign company, despite availability of various types of concessional financial and fiscal facilities.

Reasons for higher locational concentration in Dhaka are not difficult to explain. Dhaka, being the capital city of the country, offers the entrepreneurs the easiest access to the administrative, financial and infrastructural facilities, including all other utilities and services.

Chittagong coming next in these respects and also offering the developed port facilities as well as the facilities offered at the Chittagong Export Processing Zone. It may be noted here that, foreign investors who have set-up plants in Export Processing Zone are not generally happy with the idea of BEPZ having its head - office at Chittagong since all major government offices have headquarters at the capital city of Dhaka and other facilities are also easily available here (Reza, 1987). This attitude of the foreign investors is clearly reflective of further deepening of industrial concentration in the major urban centers of the country in Dhaka division. In this context, development of effective industrial estate facilities at various district headquarters may be thought of as complementing arrangements to go with the overall improvements in the infrastructural and administrative facilities within the regions where the foreign investors feel insecure to invest.

TRENDS IN OUTFLOWS OF PROFITS AND DIVIDENDS BY FOREIGN COMPANIES

Remittance of profits and dividends by foreign companies out of Bangladesh remain an important of the costs of private foreign investment to the Bangladesh economy and its rewards to current and aspirant investors. In Bangladesh, detailed figures are not available on profits and dividends and other fees remitted out of the country by foreign firms. Bangladesh Bank - the central bank of the country, which is supposed to maintain a systematic record keeping in this regard, has been found to be extremely

unscientific. Intensive efforts to obtain the relevant information from scattered official files have at best generated only a partial picture in this regard.

However, Sobhan and Bhattacharya (1986) have found that during the period 1977-1984 Taka 5491 million was remitted abroad as profits, dividends, royalties and other fees by foreign investors operating in Bangladesh. Of the total amount remitted, the highest proportion of the outflow took place in 1984-85 (Tk. 6 million) and the lowest in 1981-82 (Tk. 54.3 million). In other years the figure varied from Tk. 72.1 million to Tk. 1247.4 million. Analyzing the annual breakdown of the outflow of profits and dividends earned by the foreign companies, it would appear that the rate of remittance went up after the government announced the new industrial policy in1982. This policy offered the maximum incentives to foreign investors by relaxing the provision for repatriation of profits. Since, over the same period, the amount of equity investments increased substantially, a large part of the increase in total remittances can also be explained such equity inflows.

Another important aspect of the remittance figures is that the list of the beneficiaries is overwhelming dominated by a single country, the United Kingdom. It was found in a study that foreign companies of UK origin took away 77% of the total amount (remitted abroad) during the period 1976-77 to 1983-94, followed by the USA (15.6%) and Switzerland (Sobhan and Bhattacharya, 1986). This pattern would appear to reflect the high volume of remittances made by British - owned tea companies and by Bangladesh Tobacco, which is one of the most profitable of the transnational corporations operating in Bangladesh.

It should be kept in mind that FDI figures are the sanctioned amounts and not the actual inflows. This tends to inflate estimates somewhat since not all sanctioned projects are actually implemented. Moreover, the FDI figures include re-invested earnings. If one takes into account only new capital flowing into the country from abroad and adds "transfer pricing" amounts, then it is not unlikely the total outflow of remittances from FDI would exceed the total inflow of foreign private capital into Bangladesh. Commenting on the rising trends in such outflows, Sohban and Bhattacharjee (1986) noted that:

..... FDI in Bangladesh has been a drain on national resources. As between 1977 and 1986, at a time when the Government of Bangladesh was laying down the red carpet for foreign investors, Bangladesh, one of the poorest countries in the world, was exporting capital abroad to the extent of Taka 5491 million on account of private foreign investment in the country. It follows that unless there is quantum escalation in new inflows of FDI the further liberalization of provisions for remittances of profits by foreign investors will in the years ahead the net drainage of resources out of Bangladesh.

In these circumstances, realism would appear to demand to just a scaling-down of the extravagant expectations entertained by policy - makers about the role of private foreign investment but a serious review of the prevailing policy package which has made Bangladesh into an exporter of capital.

As an adjunct to export-led industrialization strategy, Bangladesh has also turned to setting up Export Processing Zones (EPZs). Various fiscal and other incentives have been offered to attract investment by foreign investors in these zones. In recent years, data show that much of the FDI is channeled to the country's two EPZs, namely, Chittagong and Dhaka EPZs. The contribution of the two EPZs on the process of economic development of Bangladesh deserves special attention for scrutiny. Therefore, the impacts of EPZs in creating employment and earning foreign money have been taken up for discussion in the next chapter (Chapter six). Problems of FDI in Bangladesh have also been discussed in Chapter six.

CHAPTER-VI

FDI IN EXPORT PROCESSING ZONES OF BANGLADESH

The creation of an Export Processing Zone (EPZ) is viewed as a special drive to attract foreign investment, particularly as an adjunct to the export-led industrialization process. There has been a rapid proliferation of EPZs in different parts of the developing world over the last three decades, particularly in the 1970s (Germidis, 1984). In 1966, for example, there were only two EPZs, one at Kandla in India and other at Mayaguez in Puerto Rico (Reza et.al, 1987). By 1970 their number had increased to eight. The rate of EPZs creation accelerated during the 1970s. 23 zones were set up in 11 countries between 1971 and 1975, most of which were situated in Asian countries. The period 1976-1996 saw the creation of 66 new zones across the globe (WTO, 1999). Prospects of increased manufactured exports, foreign exchange earnings and employment have formed the ***raison d etre*** of setting up EPZs. This chapter examines the two operational EPZs of Bangladesh in terms of investment drawing, employment generation, and export earning. The analysis is followed by an assessment of the problems of FDI in Bangladesh.

Bangladesh conceived the idea of establishing export-processing zones (EPZs) as an adjunct to the adoption of open economic policy in the late 1970s. The aim behind the idea of setting up of EPZs was to offer favorable conditions to attract foreign and local private investment. To translate the idea into a reality Bangladesh enacted "The Bangladesh Export Processing Zones Authority Act, 1980". The first EPZ of the country, Chittagong Export Processing Zone (CEPZ) started functioning in 1983. Subsequently, the Dhaka Export Processing Zone (DEPZ) was set-up, which came into operation in 1992. The Bangladesh Export Processing Zones Authority or BEPZA has been empowered to supervise the overall affairs of EPZs in Bangladesh.

Availability of the inexpensive and productive labor force in Bangladesh has aided to dub the EPZs in Bangladesh as the "optimum profit making bases" in the world (Mansur, 1994). Also it is perceived that of over 800 zones in more than 100 countries

listed in the WEPZA International Directory of Export Processing Zones and Free Trade Zones (The Flagstaff Institute, 1997), the EPZs in Bangladesh will offer a very competitive environment for foreign investment among the developing countries.

An industry or a set of industries has to be 100 percent export oriented industries to qualify to be established in the EPZs. The procedure for getting permission to set up an industry is easy, for which an application in a prescribed form has to be made to the BEPZA which upon being satisfied that the applicant fulfils the requirements, grants permission to do so. The BEPZA then allots or leases out on rental basis or otherwise land and building space in a zone to him who has been granted permission to set up an industry in that zone. Industries, which may be set up in the EPZs in Bangladesh, are classified as:

TYPE A INDUSTRIES:

100 percent foreign ownership includes investment by Bangladesh nationals ordinarily resident abroad. The total investment cost of the industrial project including cost of construction shall have to be financed by the investor's own foreign exchange resources. In this type of industries the cost of raw material and the entire working capital requirement have to be financed out of remittances received in convertible foreign currencies or export proceeds of the enterprise. The entire output of the enterprise has to be exported outside Bangladesh.

TYPE B INDUSTRIES:

This is joint venture type project between foreign and Bangladeshi investors resident in Bangladesh. In the collaboration, the cost of capital machinery and spare parts imported from abroad and the cost of entire raw materials used for manufacturing or processing, either imported or locally procured, shall have to be provided by the foreign partners by funds of foreign origin. The joint venture under this arrangement has to be registered in Bangladesh as a Bangladeshi company under the Companies Act.

TYPE C INDUSTRIES:

These are the 100 percent Bangladeshi investor-owned enterprise. The cost of machinery, spare parts, raw materials and other imported capital goods have to be financed under non-repatriable foreign exchange, suppliers credit, **pay-as-you-earn** (PAYE) or other approved arrangements. Local currency could be used to finance costs of approved areas like construction, working capital, etc. These enterprises have to surrender their entire export proceeds to Bangladesh Bank, and they come under the foreign exchange regulations of the country.

A favorable investment climate does not depend only on inexpensive labor costs and other financial incentives and physical facilities offered to the investors, but also on non-applicability of various domestic laws which can create a plethora of obstacles and restrictions in the functioning of the industries. The BEPZA Act of 1980 has ensured that many of the domestic laws and decrees have no or partial applicability in the zones. This makes the EPZs "privileged enclaves for the investors within a country".

An exclusive package of incentives and facilities is offered in the EPZs in Bangladesh. This package is specially designed either to increase the rate of return of a particular industry or to reduce or redistribute its costs or risk. The incentive measures certainly affect the locational decision of foreign enterprise, but they cannot ensure flows of foreign investment.

FISCAL INCENTIVES

Like most of the free zones, the EPZs in Bangladesh offers a variety of fiscal incentives to the investors. The overall objective of these incentives is to reduce the tax burden of the producers who set up their plants inside the EPZs. The main types of fiscal incentives are:

1. **Tax Based**
   - → Tax holidays for 10 years.
   - → Exemption of income tax on borrowed capital.
   - → Relief from double taxation subject to bilateral agreement.

- Complete exemption from dividend tax for tax holiday period of foreign nationals.
- Exemption of income tax on salaries of foreign technicians for 3 years subject to certain conditions.

2. Import-Export Based

- Duty free import of machinery, equipment and raw materials.
- Duty free import of three motor vehicles for use of the enterprises in EPZs under certain conditions.
- Duty free import of materials for construction of factory buildings in the zones.
- Duty free export of goods produced in the zones.

3. Financial Incentives

The internal resource constraints do not permit the Government of Bangladesh to offer financial incentives such as the provision of funds to firms by means of grants, credits, government equity participation and insurance at preferential rates and so on. Bangladesh instead has been trying to woo foreign investors by offering a host of policy incentives that indirectly help them financially, or their investment inducement remains upbeat. These measures are:

. Law secures all foreign investments and no ceiling is imposed on the extent of foreign investment.

. Full repatriation of profit and capital is permissible after tax and dividend obligations, if there are any, are met.

. Other approved earnings by foreign investors / employees are re-patriable.

OTHER INCENTIVES

There may not be easy classifications for these sorts of incentives **(for details, see Appendix-II).** The common denominator of these incentives is being that they are designed to increase the operational efficiency and profitability of an investor inside

the EPZs. Bangladesh has a long list of offerings to attract the foreign and local investors in the EPZ areas. Some of these are mentioned below:
The zones provide Land, factory buildings (on rental basis), electricity, water, gas and telecommunications.

Import and export permits are issued by EPZ within 24 hours.
Work permits are issued by BEPZA.

Relocation of existing industries from abroad or of industries from one zone to another within the country is allowed.
Intra-zone and inter-zone export is permitted.

All customs formalities are done at the gate site of the respective factory building within the zones.

Repair and maintenance of machinery and capital equipment from domestic tariff area are allowed.

For an undisturbed work environment in the EPZs, formation of labor unions and strikes within the zones have been prohibited.

INVESTMENT, EMPLOYMENT AND EXPORT ISSUES OF THE EPZS

The EPZs in Bangladesh are assumed to provide an opportunity to "export labor" or to promote commodity export to create employment for the otherwise unemployed domestic labor, and to earn foreign exchange in the process. The extent of these achievements, particularly the nature of various aspects of investment, employment and export impacts of the two functioning zones, viz., CEPZ and DEPZ in Bangladesh are discussed below.

Investment Aspect

The issue of investment in the EPZs needs a thorough and careful analysis to see the benefits of setting up of EPZs in Bangladesh. As noted earlier, Bangladesh is vigorously trying to be on the investors mind and map as their investment destination. But irony is that, with all the potentials, Bangladesh is yet to emerge as a favored place for FDI. The very tiny annual figures of investment inflows in Bangladesh substantiate its stature as an investment drawer. However, the investment aspects in the EPZs in Bangladesh have been discussed from three different angles: (i) investment as per the ownership of enterprises, (ii) product-wise investment, and (iii) investment as per country of origin.

Ownership-wise Investment Distribution

Ownership type-wise classifications of enterprises, which are in operation or under implementation in the two functioning EPZs in Bangladesh, have already been discussed above. Information on investment endowment of each of these categories in the two zones is discussed below.

In the CEPZ, a total of 126 business enterprises were either in operation or under implementation phase. Please see the table-: A.1 in the appendix-1. Out of the total enterprises, 67 entities were in the A-Type category, 29 in the B-Type category and 30 were in the C-Type category. In category A, 46 enterprises were fully operational with a total investment of $ 130.2 million (against the proposed of investment of $ 85 million, one-tenth of which had been actually brought in. Under the Joint-Venture Type, 15 enterprises became functional and 14 were in the waiting to become fully operational. Against the proposed investment of $ 41 million, only $ 17 million had so far been invested in this category. Type - C enterprises are fully owned by the Bangladeshis. Out of the 30 C-Type enterprise, 15 became fully operational with an investment of $ 31.3 million during the period of our consideration.

In the DEPZ, a total of 68 enterprises had been working in the three categories. The break-up of enterprises which are operational and under-implementation were: Type A - 21 and 17, Type B - 3 and 10, and Type C - 2 and 15 respectively. Again Type-A

enterprises were the highest investors with $ 56.3 million actual inflows against a proposed figure of $ 385.0 million. The proposed figure indicates that the enterprises are showing greater desire to bring more investment in the future. The local entrepreneurs are also involving themselves more and more in the investment drive in the DEPZ. A ratio analysis of actual investment against the proposed amount is presented in the table-1. This table clearly indicates that the ratio between actual and proposed investment has an overall better show in the CEPZ than in the DEPZ. This is quite understandable because of the difference in duration of their operation.

Table-: 1 Ratios of actual and proposed investment CEPZ and DEPZ (in dollar terms)

Types Of Enterprises	CEPZ		DEPZ	
	Operational	Under Implementation	Operational	Under Implementation
A Type	1 : 1.21	1 : 9.96	1 : 3.50	1 : 13.97
B Type	1 : 1.34	1 : 5.77	1 : 1.31	1 : 22.87
C Type	1 : 1.04	1 : 11.35	1 : 1.68	1 : 23.08

Source: Computed from BEPZA statistics, upto September 1998.

Product-wise Investment

Product-wise cumulative investment figures in CEPZ and DEPZ makes out one important point, that is, investment in both the zones are heavily loaded in textile and garments related products. The Bangladesh Export Processing Zones Authority or BEPZA brings out statistics of product-wise investment in the two zones under a total of 19 product-heads. The major heads are - fishing reel and golf, textile, terry towel, metal products, electronic and electrical goods, garments, footwear and leather goods, plastic goods, knitting and other textile products, garments accessories, caps, etc. By September 1997, the cumulative amount of investment in CEPZ was $ 189.4 million (against the proposed $ 338.6 million), while for DEPZ the figure stood at $ 63.0 million (against the proposed $ 466.9 million). The table-A.2 (see appendix-1) gives the product-wise distribution of investment in the two EPZs.

Investments in both CEPZ and DEPZ have been marked by a lop-sided development, i.e. investment inflow in textile and garments related products are much higher than in

other products. Foe example, out of the total of 126 enterprises in the CEPZ, 56 enterprises were related to textile and garments products and they constituted about 55 per cent of the actual investment (or 49 percent of the total proposed investment). Investment in garments constituted the single largest component. Figure-wise, 21 firms were involved in the production of garments constituting 25 percent of the actual (or 19 percent of the total proposed) investment in CEPZ.

In DEPZ, the similar trend had been observed. Five "product heads" viz., textile, garments, knitting and other textile products, garment accessories and caps had 41 enterprises out of the 68 firms that so far invested in the zone during the period. Together they accounted for 87 percent of the actual (or 80 percent of the total proposed) flow of investment in DEPZ. Textile product received the highest attention in case of investment proposal made to DEPZ, constituting 59 percent of the total. But garments products had experienced a higher inflow when considered against the gap between proposed and actual flows.

Two important features can be identified from the previous discussion. Firstly, within a short span of functioning, DEPZ had received investment offers totaling $ 466.9 million and in that process surpassed the figure of $ 338.6 million at CEPZ. But the gap between proposed and actual investment was much wider in regard to DEPZ. Secondly, investors are probably skipping the areas of high-tech investment in EPZs or for that matter in Bangladesh as well. Therefore, any expectation of technology transfer for industrialization in the high-tech industries might remain unfulfilled by the EPZ initiative in the near future.

Country-wise Investment

In the country-wise analysis of investment, discussion is only made on the Type-A, 100 percent foreign-owned industries. The table-2 gives cumulative figures of investment for CEPZ and DEPZ since their respective inception.

Table-2: Cumulative investment in the A-Type enterprise (figures in US $ million).

	CEPZ			DEPZ		
	No.of Enter-prise	Proposed	Actual	No.of Enter-prise	Proposed	Actual
Total Investment (TI)	126	338.6	189.4	68	466.9	63.0
Investment by A-Type Enterprises (i) Total % of TI	67	242.5 (71.6)	138.8 (73.2)	38	385.0 (82.5)	56.3 (89.4)
(ii) In Operation % of TI	46	157.5 (46.5)	130.2 (68.7)	21	134.0 (28.7)	38.3 (60.9)
(ii) Under Implementation % of TI	21	85.0 (25.1)	8.5 (4.5)	17	251.0 (53.8)	18.0 (28.5)

Source: Calculated from BEPZA statistics, upto September 1998.

The contribution of A-Type industries in the total amount of investment in the two EPZs is shown in the table-3 given below. In the two EPZs, Bangladesh received FDI mainly from 9 countries. In particular, CEPZ actually hosted investment from all these countries making a total actual investment of $ 138.8 million in 67 enterprises, 46 of which were fully operational and the rest were under the process of implementation. Country-wise break-up clearly reveals that the S. Koreans were by far the largest group of investors in both the EPZs in Bangladesh. For instance, out of 67 A -Type enterprises in CEPZ, the Koreans were involved in 23 firms, investing a total of $ 56.4 million in actual terms (against a proposed figure of $ 112.8 million) or 41 percent of the total. Japan followed South Korea. Please see the table- A.3 in the Appendix-1.

The Japanese had a smaller margin of difference between actual and proposed investment (proposed investment $ 50.4 million, actual $ 49.0 million in 17 enterprises). Hong Kong (9 enterprises with actual investment $ 16.2 million against $ 23.6 million proposed), USA (5 enterprises with $ 7.7 million and $ 12.4 million respectively), UK (6: $ 2.6 million: $ 25.1 million), Malaysia (2 enterprises) and Singapore (2 enterprises) were the other major investors in the CEPZ.

In DEPZ, a total of 38 foreign enterprises were set up by August 1997. Of these 18 were owned by the Koreans (with an actual investment of $ 31.7 million against proposed $ 139.4 million), 6 by investors of Hong Kong (actual $ 20.7 million; proposed $ 46.6 million), 5 by investors from the United Kingdom (actual $ 1.5 million; proposed $ 12.3 million), 3 by the Japanese, 2 by investors of Malaysia, and 3 by others. In recent years, however, DEPZ is attracting more investment proposals and likely to surpass the figure of investment in CEPZ in terms of actual inflow of foreign investment very shortly.

It is worthwhile to mention here that many enterprises of Korea and Hong Kong origin are investing more than their proposed figure, and their investment are mainly in the textile, garments and apparel enterprises. The reason behind this bias in investment could be explained by the fact that though these products might be looking like products of "sun-rise" industries to Bangladesh, they are actually passing a "sun-setting phase" in those countries (Barai, 1998).

The two EPZs probably now host most of the foreign investment coming to Bangladesh. This remains a statement from perception, because, the statistical figures maintained by different selected organizations like the Board of Investment (BOI), BEPZA, Bangladesh Bank etc. are not clear about the issue of share of FDI of the two EPZs. Moreover, the currency denomination of FDI also makes a problem for conversion into Taka or dollar figures.

Table-3: Annual investment in CEPZ and DEPZ and FDI inflows in Bangladesh from 1990-91 to 1998-99(figures in million US $).

	CEPZ	DEPZ	Total of EPZs	Country Total FDI
1990-91	22.054		22.54	3.2
1991-92	23.659		23.659	1.4
1992-93	22.048		22.048	3.7
1993-94	29.181	8.224	37.405	14.0
1994-95	27.669	8.265	35.934	11.0
1995-96	16.128	14.455	30.583	1.9
1996-97	22.887	31.012	53.899	1.8
1997-98	42.675	26.834	69.509	1.2
1998-99	36.167	35.543	71.710	4.6

Source: World Trade Organization (2000) Trade Policy Review: Bangladesh.

The table-3: shows the annual investment in CEPZ and DEPZ and FDI inflows in Bangladesh from 1990-91 to 1998-99(figures in million US $).

EMPLOYMENT CREATION

Providing employment opportunities to its vast pool of manpower has become a prime concern for the Government of Bangladesh. Economically active labour force in Bangladesh is estimated at present to be around 55 million (LFS, 1999). The positive employment effect of the EPZ has also encouraged the government to go for setting up zones to entice local and foreign investors.

It is evident from the above analysis is that investment in both the EPZs are concentrated to few products which have coincidentally labor-intensive manufacturing base. The concentration of investment in labor-intensive components has actually helped many male and female workers to get employment in the enterprises at the EPZs. Had the investment been in the high-tech capital-intensive products, the employment opportunity would have been very limited.

The employment aspect of EPZs in Bangladesh has been analyzed from two angles: (i) product-wise employment generation in the zones (please table-A.4) and (ii) actual employment of Bangladesh employees in the A-Type (100 percent foreign-owned) enterprises operating in the EPZs (please table-A.5). In the two EPZs of Bangladesh, CEPZ and DEPZ had a total local employment of 56694 people in September 1997. Individually CEPZ had 39574 local employees in 19 product heads that were being manufactured in the zone, while DEPZ had 17120 persons employed in 18 product heads at that time.

In CEPZ, product head "garments" was having the highest number of employment, i.e., 19430 employees in 21 enterprises; each enterprise had an average of 925 workers. Footwear and leather products had the second-highest level of employment numbering 3689 persons in 13 enterprises, giving a labor intensity of 284 worker per enterprise. Product 'caps' had some importance in the context of employment generation in CEPZ as 8 enterprises had an employment of 3337 personnel at their

compounds. Textile was the fourth largest product-head with 2732 workers. There was only one enterprise producing fishing reel and gold equipment absorbed about 2150 people. In DEPZ, garments again stood to be the largest employment generating product-head with a local employment figure of 11,367 in 16 enterprises. The employment intensity of investment per million Dollar in the EPZs is shown in

Table-4: Employment impact of investment in the EPZs (employment per million US $)

PRODUCTS	CEPZ			DEPZ		
	Employment (Actual)[2]	Investment $ million[3]	Impact	Employment (Actual)	Investment $ million	Impact
Fishing Reel and Golf Equipment	2150	33.15	64.9	-	-	-
Textile	2732	34.44	79.3	559	24.29	23.0
Terry Towel	1866	6.35	293.9	-	-	-
Metal Product	799	9.27	86.2	0	0	0
Footwear and Leather Goods	3689	17.24	214.0	91	0.63	144.4
Electronics and Electrical Goods Garments	1253	9.42	133.0	0	0	0
Garments	19430	47.20	411.7	11369	20.78	547.1
Plastic Goods	690	5.68	121.5	252	2.87	87.8
Knitting and Other Textile Products	1933	7.02	275.4	1431	1.67	858.9
Garments	29	1.97	17.7	33	0.48	68.8
Garment Accessories	29	1.97	17.7	33	0.48	68.8
Caps	3337	7.04	474.0	2961	7.58	390.6
Other Products	1666	10.61	157.0	424	4.66	91.0
Total	**39574**	**189.42**	**208.9**	**17120**	**62.96**	**271.9**
G. Total Employment = 56694			G. Total Investment = $ 252.36			
Employment impact per million US $ = 224.66 persons						

Source: Calculated from Trade Policy Review of Bangladesh (WTO, 2000).

.It becomes amply clear from Table-: 4 that on an average a million dollar investment in DEPZ helped to generate employment for more work force than that in CEPZ- 272 and 209 respectively. In CEPZ, 'caps' is the most labor-intensive product-head followed by garments, terry towel, knitting and other textile products, footwear and leather goods and so on. While in DEPZ, knitting and other textile product-head is the most labor-intensive head. An average investment of $ 1 million could employ about 859 workers in this category.

A one million-dollar investment in garments in DEPZ could also employ more labor than that of CEPZ. Thus, if the workers of CEPZ and DEPZ are equally productive, then DEPZ seems too more attractive (less costly) for the investors at least in terms of production cost of the products. On the same ground, production of caps and footwear and leather goods had a comparative advantage in CEPZ over DEPZ. The table-:5 shows the figures of employment in the Type A industries in CEPZ and DEPZ.

In commensurate with their investment level, the Koreans are also the largest employers of Bangladeshi workers in their enterprises in the EPZs. 18,687 workers were working with 18 Korean firms in CEPZ and 10,035 in 12 firms in DEPZ. Investors from Hong Kong had employed 5493 local workers in CEPZ, and in DEPZ the figure was 2380. Investors from Japan, USA and UK were the other major employers. In all, a total of 47,718 local employees (32819 in CEPZ and 14899 in DEPZ) were employed in the - Type industries in the EPZs. This means, on averages a $ 1 million FDI in CEPZ supported 236 jobs for Bangladeshis, while in DEPZ the figure was 265 for the same.

One may conclude that growth of investment in the two EPZs has been matched by the growth of employment. To substantiate, CEPZ started with a tiny investment figure of $ 0.874 million and an employment figure of 624 in 1983-84. In 1996-97 the figures stood at $ 189.4 million and 39574 respectively. For DEPZ, in four years of functioning, it was housing an investment of $ 62 million with an employment of 17120 workers. Gender-wise distribution of employment reveals that 68 percent of the workforce in CEPZ are females while in DEPZ, they constituted 42 percent of the total workforce. This again seems to be an extension of the fact that garments industry is truly dominated by female workers both in national units as well as units inside the EPZs.

EXPORT IMPACT

Export impact of EPZs has been assessed from three points of view: (i) national growth of export versus growth of export from EPZs, (ii) contribution of exports from EPZs to national export and (iii) value-added contribution of EPZs in the export amount. These observations are depicted in the table-5.

Table-5: Growth and contribution of exports from EPZs to national export for 1990-91 to 1996-97 (U.S. million $)

Year	Total Export	Growth %	Export from EPZs	Growth %	% of EPZs Contribution to Total Export
1990-91	1980	12.0	48	40	2.69
1991-92	1994	12.02	77	60	3.86
1992-93	2383	19.51	127	65	5.32
1993-94	2534	6.34	147	15	5.80
1994-95	3473	37.06	228	57	6.56
1995-96	3800	9.12	337	48	8.87
1996-97	4417	16.26	463	37	10.48

Source: Calculated from BEPZA statistics, upto September 1998

The growth of national export met a fluctuating fortune ranging from 6 percent to 37 per cent during the period under study. Interestingly the lowest and highest growth in export happened in 1994-94 and 1994-95 respectively. The highest percentage of export growth could be explained by two factors. Firstly, in that year garments saw a very high demand in the international market and secondly, in the previous year 1993-94 export was relatively low. So it made a low base for comparison for exports of 1994-95. Figure-10 exhibits two indexes of export from EPZs and total export. In both the indexes figures in 1990-91 is assumed as base year. A sharp rising trend in the index of export from EPZs is discernible.

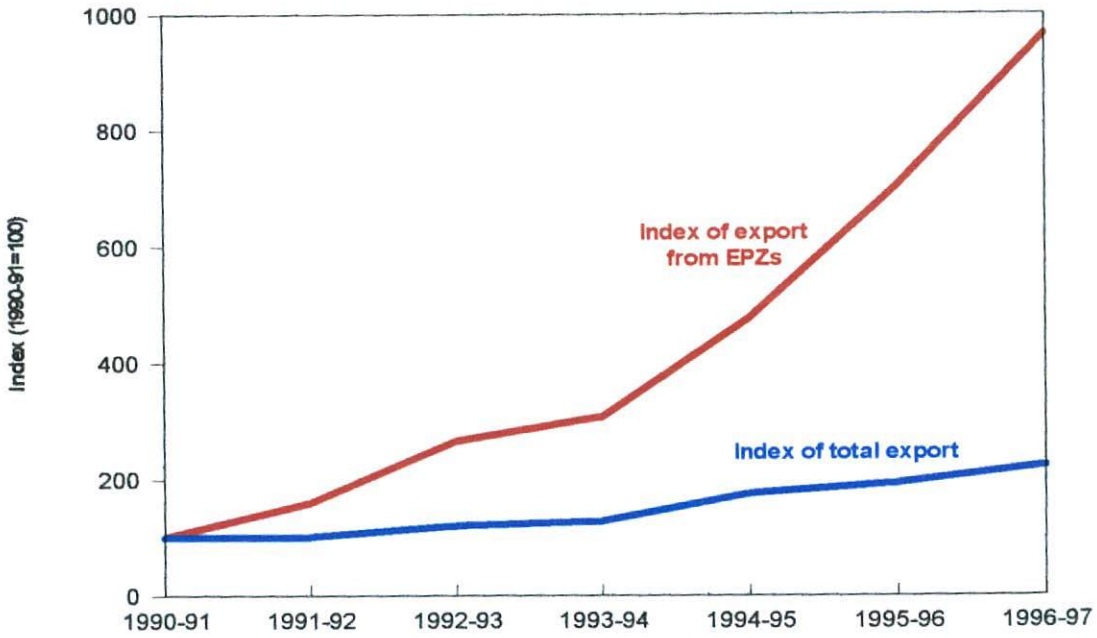


Figure-10

It is, however, to be followed that in 1994-95 export from EPZ also enjoyed a very high growth, 57 percent to mention the percentage-wise growth. Equally important is to note that export from EPZs experienced a slow growth in 1993-94. However, in rest of the fiscal years, exports from EPZs grew rapidly, and growth of 65 percent was the highest in 1992-93. Exports from DEPZ started in 1993-94 with a tiny amount of $ 5.249 million. But by 1996-97 the figure went up to $ 119.45 million (see table-:5).

The share of exports from EPZs to the national export figure is increasing every year. Percentage-wise share of exports from EPZs vis-a-vis the national exports were 2.69 percent, 3.86 percent, 5.32 percent, 5.80 percent, 6.56 percent, 8.87 percent and 10.48 percent respectively from1990-91 to 1996-97. Though the share of exports from EPZs is a growing phenomenon, the contribution is yet to play a significant part.

The export performance of EPZs in Bangladesh can also be judged in terms of their value-added contribution. Conceptually, the export of an enterprise in the EPZ would be equal to its output. On the assumption that imported raw material would be equal to raw material (including packaging and auxiliary material) consumption, the difference between value of export and value of raw material import over a period of time would roughly indicate the value added contribution made by the EPZs in Bangladesh. On the above basis, the value added by the EPZs in Bangladesh needs to be put under scrutiny. Table- A6 and Table- A7 show the import-export statistics of CEPZ and DEPZ respectively for the year 1996-97.

The CEPZ exported $ 343.3 million and imported $ 285.5 million in the year 1996-97. This makes a value added contribution of $ 57.8 million or 16.84 percent of the total export. If we assume that import from Domestic Tariff Area (DTA) makes a part of the value-added, and if we add back the amount with the differential then the figure rises to $ 61.3 million or 17.86 percent of export. This is not a significant contribution. Statistics of DEPZ for the year 1996-97 belie all expectations of value added. During the period, enterprises in DEPZ imported ($ 131.6 million) more than they exported ($ 119.5 million). In that sense, DEPZ has still remained a net importing zone.

If the outflow of foreign contribution in the form of dividend, royalty and other current payment of direct and indirect nature arising from the collaboration (JVs in the EPZs) with foreign firms are taken into account, then the net domestic value added of the EPZs in Bangladesh could lead to some uncomfortable questions.

SUMMARY

In Bangladesh, EPZs, have emerged as the main centers of attraction for FDI inflows. Most of the investment in the two EPZs has come from East and South East Asian countries viz., South Korea, Japan, Hong Kong, Malaysia and Singapore. Textile and apparels and related products have absorbed the maximum amount of investment in the EPZs, and are proving to be the more employment generating and export earning products because of their labor-intensive production nature. Female workers are getting more importance in terms of employment in the EPZs, and the number of female workers is more than that of the male workers in CEPZ. On an average a $ 1 million investment in EPZ supports 225 jobs for the Bangladeshis. Garments, knitting and other garment related products are the most labor-intensive products produced in the EPZs. The share of export earnings of EPZs in the total national export is increasing and now hovering around 11 percent. In terms of value added contribution of the EPZs, the present level seems to be very insignificant in general, and for DEPZ it was negative in 1996-97 in particular.

PROBLEMS OF FOREIGN DIRECT INVESTMENT IN BANGLADESH

This section mainly deals with the constraints and hindrances of FDI inflow in Bangladesh. Most FDI problems in Bangladesh are primarily related to social, political, economic and cultural spectrum. Since 1976, governments of Bangladesh have immensely realized that the pace of economic development largely depends on FDI inflow and the subsequent governments after 1976 have taken quite a series of liberal policies to attract FDI. Over the last twenty-five years, governments of Bangladesh have offered quite a number of incentive packages and brought about series of changes in the FDI policies and administrative set-ups with a view to attracting more FDI. The cheap and abundant labor coupled with liberal policies and

incentive packages was expected to help swell up the FDI inflow. However, available data on FDI influx register that the amount of FDI yet has remained far below the desired level.

Political unrest, bureaucratic tangles and corruption, poor and fragile infrastructure, regular donation to political and non-political bodies, contribution to local hoodlums under duress on regular basis etc. are the most obvious factors most people blame for augmenting the total amount of cost of the foreign investors which result in least amount of FDI attraction. But there are quite a large number of sunk and invisible hindrances that are far away from our range of vision. All these contribute to raising the cost of foreign investment and keeping the FDI far below the desired level. These overt and covert obstacles straightly diminish the labor cost advantages as well as privileges provided by the governments through liberal policies and alluring incentive packages.

Labor cost in Bangladesh is comparatively cheaper than any other countries. Most labors in Bangladesh are unskilled and their incidental costs sometimes become too much and too numerous. The low productivity of unskilled labor sometimes fades away the cost advantage of labor. Labor unrest and political instability lead to frequent interruptions of working days (Reza and Rashid,1997). Thus, the cost of labor increases because of the lost of paid hours.

But there are too many hidden costs that most people are unaware of these. To install a new telephone/fax line, foreign investors have to pay a fixed amount of money to telephone/fax authority and failing to pay this amount must result in longer period of delay. Payment of this amount does not ensure the better telephone/fax service. They have to make monthly contributions to avoid fake telephone/fax bill and to keep the telephone/fax in working conditions.

Likewise, to install new gas lines and to keep them in working order, foreign investors have to continue the same type of subscription. Failing to make this donation must result in unnecessary delay and regular disruption in gas supply. The episode with the Gas line in EPZ-Chittagong where one designated engineer from *Titas Gas* did not

show up in spite of repeated requests was probably due to the lack of understanding of the foreign investor to make personal donations (Amin, 1996). Moreover, frequent power failure, fluctuating voltage of power, delay in installing power point, unnoticed long time power failure, fictitious electric bill etc. directly contribute to augmenting the cost of foreign investors.

To avoid the chaos and turmoil, and to ensure the peaceful atmosphere in factory premises, foreign investors have to make regular donations to keep local hooligans happy. Rampant *hartals,* strikes, labor unrest hamper and sometimes stop the flow of production, transportation, marketing and other regular activities of the company. Consequently, company usually fails to reach its production goal or marketing goal or sales goal. Sometimes, export oriented companies may loose foreign customers due to failure of delivery of goods on time. This fact is truer in case of garment industry in Bangladesh. Apart from these costs, foreign investors have to regularly pay tolls to the law enforcing agencies and local administrations to have a minimum guarantee of safety and security. Sometimes, theft, robbery and some other types of mishaps also increase the total amount of costs. All these types hidden incidental costs straightly outweigh the apparent cost advantage of labor in Bangladesh. Therefore, investment in Bangladesh is perceived less lucrative to the foreign investors.

The size and growth of the domestic economy is another important determinant of foreign investment inflows (UNCTC, 1999). The economic factors and parameters Bangladesh inherits are not conducive to FDI attraction. The population of around 125 millions may apparently be large enough to make an impressive market for consumer products. But the negligible amount of per capita income (below $280) does not create any effective demand for most consumer goods. The amount of domestic investment sometimes serves as a parameter to attract FDI. Since the amount of domestic investment is far below the expected level, foreigners feel the least interest in direct investment in Bangladesh.

The predicament of most roads and highways is miserable. The country astoundingly lacks sufficient number roads and highways and they are not properly maintained and repaired. Moreover, most roads are not too wide to freely move different vehicles. All

these factors spawn horrendous traffic jam, delay in transportation and sometimes deterioration of the quality of some products. Moreover, to ensure the smooth flow of raw materials and finished goods, most investors have to pay tolls at different points of the roads. These factors eventually lead to increment the overall costs of foreign investors.

Since independence, Bangladesh has not yet achieved desirable stability in its political arena. But political stability is a crucial factor determining the amount of amount of FDI. At present, the political environment is sharply partitioned into two sections- ***ProAwamileague*** and ***Anti-Awamileague***. Frequent *hartals* and blockage, rise of Islamic fundamentalism, politically biased civil and government administration, brittle law and order situation etc all have shattered the confidence of the foreign investors. Moreover, government policy drastically changes with the changes of government. This discontinuity of government policy coupled with the political instability induces the foreign investors to shy away from investing in Bangladesh. . Present days, foreign investors are very much afraid of the prevalent hostile political atmosphere.

Existing cultural environment is not suitable for foreigners. Language barrier, religion conservatism, and the lack of western style or oriental style recreation facilities, relatively poor accommodation and broadcasting facilities all over the country in general and the major cities in particular make it quite difficult for foreign investors to stay in Bangladesh for a prolonged period of time (Amin, 1996). Singapore, Malaysia, Indonesia and Thailand have been successful to resolve some cultural problems maintaining the traditional religious values as well as providing some facilities like sufficient number of bars and liquor shops, other recreational facilities at night etc. that closely match their style. In this respect we are far behind than these countries and also lag behind FDI attraction.

Apart from physical infrastructure, the development level of social infrastructure is not at all up to the mark. A foreigner can hardly manage and recruit expert technicians or expert mid-level / top-level management personnel or expert /qualified workers from Bangladeshi people. Mostly they have to hire these people from foreign

countries at higher salaries. These higher salaries eventually neutralize the cost advantages of labor.

However, the problems of FDI in Bangladesh are myriad and multifarious-some are visible and some are invisible. But the ultimate cost of invisible factors is no less than that of visible factors. The steps hitherto taken by the government have not been expectedly successful in attracting FDI because most of them are primarily intended to remove visible problem factors only. The area of hidden cost factors is so vast that researchers can further investigate these aspects of FDI. However, it is worth placing equal emphasis on identifying and solving visible as well as invisible problem factors to attract more FDI. But it may be difficult to identify all the hidden factors.

All these lead observers to make comments such as the following. An officer in a large donor agency said, " The longer I am here the less confidence I have in any government program". The head of a bilaterally funded project said, "we have tried every way, but there are no measurable results. I will just stay until the end of my contact". A UN consultant opined, "Bangladesh is the most difficult country in the world in which to get any development work done" (Maloney, 1988).

CHAPTER-VII

DETERMINANTS OF FDI IN BANGLADESH

Most developing countries including Bangladesh today consider FDI an important resource for development. However, the economic effects of FDI are almost impossible to measure with precision. TNCs represent a complex package of attributes that vary from one host country to another. These are difficult to separate and quantify. Measurement is even more difficult where their entry has large (non-marginal) effects. There is no precise method of specifying a counter-factual - what would have happened if a TNC had not made a particular investment. Thus, the assessment of the development effects of FDI resorts to one of two general approaches. The first is econometric analysis of the relationships between inward FDI and various measures of economic performance. The second is a qualitative analysis of particular aspects of TNC contribution, without any attempt at calculating a net rate of return (UNCTAD, 1999).

The conclusions of the econometric analysis of FDI and economic growth remain unclear, especially as regards the causality within the relationship. Some analyses show a positive impact of FDI on growth, others a negative impact; yet others have found growth to be a determinant of FDI. Since growth depends on many factors whose effects are difficult to disentangle, and since FDI itself affects several of these factors, an indeterminate conclusion is probably the most sensible. But there is little doubt that fast growth and large FDI inflows go hand in hand in many instances. In this study an attempt was made to measure the effects of FDI on the economy of Bangladesh from both the angles.

QUALITATIVE EFFECTS OF FDI: REVIEW OF LITERATURE

The qualitative analysis of FDI, taking its different components separately, is more appealing. World Investment Report' 99 has adopted this approach. The purpose has

not been to analyze the impact of FDI in an abstract sense, but to start from the premise that it offers a mixture of positive and negative effects. The task facing host countries is then to disentangle these effects, and take measures that maximize one and minimize the other.

FDI comprises a bundle of assets, some proprietary to the investor and others not. The proprietary assets are what the literature terms the "ownership advantages" of TNCs. These give TNCs an edge over other firms (local and foreign) and allow them to overcome the transaction costs of operating across national boundaries. Non-proprietary assets - finance, capital goods, intermediate inputs and the like - can be obtained from the market, at least in part. Proprietary assets can only be obtained from the firms that create them. They can be copied or reproduced by others, but the cost can be vary high (particularly in developing countries and where advanced technologies are involved). TNCs are naturally reluctant to sell their most valuable assets to unrelated firms that can become competitors or could leak them to others that have not paid for it.

Of proprietary assets, the most prized is probably technology. But there are others: brand names, skills, and the ability to organize and integrate production across countries or to establish marketing networks. They also include privileged access to the market for non-proprietary assets: TNCs may be able to raise funds, or purchase equipment, on better terms than smaller firms, or firms in developing countries. Taken together, these advantages mean that TNCs can contribute significantly to host developing countries - if the host country can induce them to transfer their advantages in appropriate forms and has the capacity to make good use of them.
The assets the FDI bundle comprises are:

Capital: FDI brings in investible financial resources to host countries. The inflows are more stable and easier to service, than commercial debt or portfolio investment. In distinction to other sources of capital, TNCs invest in long-term projects, taking risks and repatriating profits only when the projects yield returns.

Technology: developing countries tend to lag in the use of technology. Many of the technologies deployed (even in mature industries) may be outdated. More importantly, the efficiency with which they use given technologies may often be relatively low. Even if part of their productivity gap is compensated for by lower wages, technical inefficiency and obsolescence can severely handicap the quality of their products and their ability to cope with new market demands. TNCs can bring modern technologies, some not available without FDI, and they can raise the efficiency with which existing technologies are used. They can adapt technologies to local conditions, drawing upon their experience in other developing countries. They may, in some cases, set up local R&D facilities. They can upgrade technologies as innovations emerge and consumption patterns change. Moreover, they can stimulate technical efficiency in local firms, supplies, clients and competitors, by providing assistance, acting as role models and intensifying competition.

Market access: TNCs can provide access to export markets, both for existing activities (that switch from domestic to international markets) and for new activities that exploit the host economy's comparative advantages. The growth of exports itself offers benefits in terms of technological learning, realization of scale economics, competitive stimulus and market intelligence.

Employment, skill and management techniques: TNCs possess advanced skills and can transfer these by bringing in experts and by setting up state-of-the-art training facilities. (The need for training is often not recognized by local firms.) New management techniques can offer great competitive benefits. Where affiliates are integrated into TNC networks, they can develop capabilities to service the regional or global system in specific tasks across the entire spectrum of corporate functions.

Environment: TNCs often possess clean technologies and modern environmental management systems, and can use them in all countries in which they operate. Some TNCs are in the forefront of adopting high environmental standards at home and abroad (UNCTAD, 1999 pp 315-317).

QUANTITATIVE STUDIES: EMPIRICAL DETERMINANTS

The few long-period cross-section growth studies that included FDI as a variable tended to find some positive relationship. For example, one study reported a significant relationship between inflows of FDI as a percentage of GDP and the growth of per capita GDP across all developed countries for the period 1960-1985 (Blomström, 1994). It suggested that although the gap in technology and productivity between foreign-owned firms and locally-owned ones is larger in poorer countries than in richer ones, that does not necessarily mean that the poorer countries gain the most from inward FDI. It argued that "the least developed countries may learn little from the multinationals, because local firms are too far behind in their technological levels to be either imitators or suppliers to the multinationals" (Blomström, 1994, pp. 250-251). And it found, in confirmation of this supposition, that inflows of FDI were significant as determinants of growth for the upper half of the distribution of developing countries, by per capita income, but not in the lower half.

A similar conclusion was reached in a study for 69 developing countries of growth in per capita GDP from 1970 to 1989 (Borensztein, 1995). FDI itself was a marginally significant positive influence on growth, but FDI interacting with a measure of average educational attainment was a stronger and more consistent influence. The higher the level of education of the labor forces, the greater the gain in growth from a given inflow of FDI. An interaction between FDI and education was also found in a paper on FDI in China that concluded, "Education becomes even more effective when it is associated with foreign knowledge that accompanies the investment". However, "the coefficient on foreign investment becomes negative when the interaction term is introduced, implying that much of the power of foreign knowledge many come through the local base of human capital" (Mody and Wang, 1997, p. 309).

Another mechanism through which the influence of FDI can take effect is through the impact of inward FDI on domestic capital formation. Another study found that FDI increases investment in one-to-one ratio or encourages capital formation by domestic firms, so that "a one-dollar increase in the net inflow of FDI is associated with an

increase in total investment in the host economy of more than one dollar" (Borensztein, 1995, p.3). This does not, of course, mean that cases of FDI crowding out local capital formation can be ruled out.

Very few long-period cross-section studies have included a measure of FDI as a potential source of growth (Blomström, 1994; and Borensztein, 1995). Reflecting this, a comprehensive review of variables used in such studies did not include FDI. However, some of the variables identified in these did not include factors of growth are typically under the influence of FDI. For example, relatively "robust" relations were found between investment ratios (investment/GDP) and growth and between investment ratios and trade ratios. But, both investment ratios and trade ratios could be affected by FDI flows, and thus, indirectly form a channel for an effect of FDI on growth. Another example refers to the effects on growth of knowledge spillovers (Eaton and Kortum, 1994). FDI is also a plausible vehicle for these knowledge spillovers, by itself (through R&D, for example) and through its relation to the intensity of trade.

The relation of FDI to trade is more generally a possible connection that may obscure the relationship of FDI to growth in quantitative studies including both variables. There is a great deal of evidence that foreign-owned firms in most countries trade more with their parents. "MNEs or their affiliates generally enjoy a larger share of home or host country exports and imports than they do of output ...this is partly explained by their being concentrated in trade-intensive sectors, and partly because their trading propensity in any given sector tends to be greater than that of uninational or indigenous firms" (Dunning 1993, p. 386). It is likely, therefore, that high foreign ownership, or a large inflow of FDI, will increase the importance of trade for a host country, thus affecting growth indirectly.

Time series studies focused initially on the impact of FDI on domestic investors. In an early example, relating to Canada, some regression coefficients, taken at face value, implied that "$1.00 of direct investment 'led to' $3.00 of capital formation" (Lubitz 1966, pp. 97-98). A later study of FDI into Canada, with somewhat different methods, a slightly longer time span, and annual rather than quarterly data, found a positive

direct effect on capital formation greater than the amount of the FDI (Van Loo, 1977). That is, there was some complementary effect on fixed investment by domestic firms. However, when indirect effects through impacts on other variables, such as exports (negative), imports (positive), and consumption (negative), operating through the accelerator, were added, the addition to total capital formation was much smaller, a little over half the inflow. The offsetting negative effects on domestic investment are quite model-specific, and involve accepting plausible, but statistically insignificant, coefficients.

RECENT EMPIRICAL FINDINGS

Recent empirical studies of the determinants of inward FDI are based on three approaches: micro-oriented econometric studies, survey data analyses and aggregate econometric analyses (Jun and Singh, 1996). Because each approach has its limitations and advantages, methodological pluralism is not necessarily undesirable. Indeed, one way of checking the robustness of the results is to expose the same model of the determinants of FDI to different methodologies.

Although many aggregate econometric studies have been conducted, a consensus on some of the determinants of FDI has often been elusive. This can be attributed partly to the lack of reliable and accurate data on FDI and these determinants, particularly at the sectoral level, and to the fact that most empirical work has analyzed FDI determinants by pooling data for a group of countries that may be diverse structurally. Structural differences refer to substantial discrepancies in the basic macroeconomic variables that characterize an economy. The analysis here suggests that the empirical results may differ significantly for country groups that are structurally different. Apart from the traditional economic variables- GDP per capita, GDP growth, and wage cost-factors that may influence FDI flows include socio-political variables, business operating conditions and export orientation.

Socio-political variables

Political risk is frequently thought to influence the decisions to invest in another country. Empirical results do not always support this assertion. Aharoni (1966) revealed that executives rank political instability as the most important variable, apart from market potential. Levis (1979), employing two proxies for political stability, obtained mixed results. He found the absence of aggressive domestic behaviour within the political system against groups or officeholders to be a significant determinant of FDI for the current period, but not if a lag time is introduced. Another variable, the legitimacy of the regime, was found to be significant for a lagged period, but not for the current period.

Discriminant analysis of 58 developing countries by Root and Ahmed (1979) found that the number of regular (constitutional) changes in government leadership between 1956 and 1967 was significant. However, other political variables, such as the number of internal armed attacks, the degree of nationalism and colonial affiliation, were not significant.

Schneider and Frey (1985) found a negative relationship between the number of political strikes and riots in host countries and FDI inflows. Nigh (1985), using the COBDAB database - which constructs aggregate measures of intra-country and inter-country conflict and cooperation - found that, for developed countries, inter-country political events were more significant determinants of FDI than intracountry events. For developing countries, intra-country political events had a more robust relationship with FDI.

More recently, Wheeler and Mody (1992) found a broad principal component measure of administrative efficiency and political risk to be statistically insignificant. Lucas (1993) does not directly incorporate proxies for socio-political risk in his model of FDI determinants. Rather, he found episodic dummies for "good events". President Aquino's accession in the Philippines, to be positively related to inward FDI. Conversely, "negative events", such as Sukarno's rule in Indonesia. Park's assassination in the Republic of Korea, and Ferdinand Marcos' martial law in the Philippines have had a negative effect on inward FDI.

The empirical evidence on the impact of political risk is not unequivocal, partly because it is difficult to obtain reliable quantitative estimates of this qualitative phenomenon for an extended period of time, particularly of those aspects of political risk that are viewed as a direct constraint by foreign investors. Most proxies that are available capture only some aspects of this determinant.

Business operating conditions

As Helleiner (1988) and UNCTAD (1996) have pointed out, investment incentives created by governments appear to play a limited role in FDI decisions. Most of the empirical literature supported the notion that specific incentives do not have a major impact, particularly when these incentives are thought to compensate for other comparative disadvantages. It is also believed that removing restrictions and providing good business operating conditions will affect positively FDI flows.

Within this context, there is a wide array of government policies that influence FDI flows. It is difficult to quantify these policies in a single comprehensive explanatory variable. An alternative approach adopted is to use a qualitative index of government policies representing the judgements of experts in the field.

Tariff barriers have received considerable attention as a factor influencing FDI. Protective tariff barriers, by stimulating import-substituting FDI, encourage "tariff hopping". Most of the available evidence supports this hypothesis, exemplified by United States FDI in the European Community.

Export orientation

In addition to the size of the domestic market in a host country, export orientation may be important for encouraging FDI flows. Recently, Hein (1992) and Dollar (1992) found that outward oriented developing economics (i.e., those that rely on new export markets) have been successful in attracting FDI flows. Robert Lucas's (1993) investigation of South-East Asian countries shows that FDI is more elastic with respect to the demand for exports than with respect to the aggregate domestic demand. If outward-oriented economics are successful in attracting FDI, the size of the

domestic market need not be a handicap. Even small host countries could influence global corporate decisions by adopting export-oriented polices.

One caveat in the empirical literature is that it is not clear whether FDI flows are attracted by economies that are already export-oriented (i.e., exports precede FDI flows) or whether FDI leads to export increases (i.e., FDI precedes exports).

RESULTS AND DISCUSSIONS

QUALITATIVE EFFECTS OF FDI IN BANGLADESH

Capital Inflows: From a trickle in the 1980s, inflow of FDI in Bangladesh have risen to nearly $400 million in fiscal 1998-99 and are expected to average about $800 million a year for the next five years. Though trailing behind India-- South Asia's largest recipient of private capital flows, it now matches India's per capita FDI inflow of $3.2 (World Bank, 1999).

Stable FDI Inflow: Bangladesh has experienced a more stable (less vulnerable) form of capital inflow, with FDI making up about 85-90 per cent of total inflows so far. This indicates trade and exchange liberalization, current account convertibility, and liberalization of the investment regime have all helped to bring this about. More importantly, it is the opening up of infrastructure and services to the private sector that has provided the biggest impetus to FDI in Bangladesh.

Diversified Product Composition: One major feature of the flow of FDI to the developing countries as a whole has been a shift in emphasis over time from extractive industries and agriculture to manufacturing and other modern industries. This pattern has been found to hold well in the case of Bangladesh as well. One study estimated that in the pre-liberation period tea, petroleum and pharmaceuticals accounted for about two-third of the TNC sales. And in independent Bangladesh, these three sectors constituted less than 10 per cent of the total TNC sales. The TNCs

are now engaged in producing a wide variety of products including food- processing, ready-made garments, electrical goods, leather products etc.

Value Added: Since most of the TNCs are involved in assembly type of production and usually are found to refrain from basic manufacturing, they are not expected to generate substantial value addition. However, a study by the World Bank (1999) estimated around 25-30 per cent value addition by the TNCs in the ready-made garment sectors only. In the electronics, pharmaceuticals and leather sectors value addition, although is not significantly high enough, but some experts put at around 10-15 per cent.

Technological Effect: Foreign collaboration is an important channel of international transfer of technology. Although technology does not necessarily have to be embodied in capital, the fact that a very small (around 25 or less) per cent of FDI in Bangladesh has come in the form of capital equipment in the recent past, indicating that capital transfer has been minimal.

Employment Effect: The total industrial employment in Bangladesh is estimated at around 4.5 million (GOB, 2000). It is not possible at the current state of knowledge to determine the number of employment generated by FDI-related industries. On the whole, with a few exception, TNCs are found to be relatively more-intensive compared to their local counterparts. This means TNCs in Bangladesh have generated less employment per unit of investment. Equally true is that TNCs generally preferred to employ relatively better-trained and skilled personnel. This is also alternatively confirmed that the contribution of TNCs in generating employment is very minimal excepting the ready-made garment sectors and the three export-processing zones of Bangladesh.

Competition: There is evidence to suggest that foreign firms have increased competition among the local entrepreneurs in industries, which do not require high technology. Examples are the marine food processing, ready-made garments, leather goods industries. Even in the pharmaceutical sector, particularly after the introduction of the Drug Policy by the Bangladesh government in 1982, many local enterprises have been set up; the stiff competition and changed milieu have forced some TNCs to

withdrawal from the country. Similarly, tobacco, shoe and also electrical industries have also experienced an increase in the market share of local firms (WTO, 2000).

Socio-Cultural Effect: Socio cultural impact of foreign firms is generally judged in terms of their social welfare projects, donations to charitable organizations, sponsorship in games and sports, and promoting other cultural activities in the host country. In Bangladesh, a number of TNC units appear to be making some contributions in this regard although any attempt to quantify the same in terms of financial expenditure has not been made until recently.

FDI IN BANGLADESH: DETERMINANTS

HYPOTHESES AND MODEL

Hypotheses

The steady growth of FDI in Bangladesh is well documented in the macroeconomic literature despite however some controversies. It is now thus critical for both the public and private sectors to have as complete an understanding of the macroeconomic determinants of this phenomenon as possible. Studies on the determinants of FDI in Bangladesh from macroeconomic perspective are very scant. This study seeks to explain, based on the incorporation of factors found in previous studies in developing countries, the behavior of FDI inflows in Bangladesh. The study covers the period 1978-1999. The full set of contributing factors and the logic for their inclusion in a model of FDI in Bangladesh lays out latter. The hypotheses are:

H_1: The larger the home country market, the greater the FDI in flows.

H_2: The higher the per capita income in the home country, the greater the FDI inflows.

H_3: The higher the export in the home country, the greater the FDI inflows.

H_4: The higher the debt-equity swaps, the greater the FDI flows.

H_5: The greater the amount of existing trades between the Bangladesh and a particular country of origin, the greater the FDI into the Bangladesh.

H_6: The lower the wage cost in the home country, the higher the FDI into the Bangladesh.

H_7: The greater the revaluation of the home-country currency against the &US, the greater the FDI into the Bangladesh.

MODELS

In this study, two models have been tested to capture specific forces that influence on FDI inflows into the Bangladesh. The first one is widely used by the United Nations (1993) to analyze the determinants of FDI flows to the major regions of the world economy. The model takes the form:

$$FDI_t = \alpha_0 + \alpha_1 GDP_{t-1} + \alpha_2 \Delta GDP_t + \alpha_3 (I/GDP)_{t-1} + \alpha_4 XR_t + \alpha_5 V(XR)_t$$

Where,

FDI_t = inflow of FDI to Bangladesh in year t.

GDP_{t-1} = the level of GDP in year t-1 of Bangladesh (which signifies the size of the market).

ΔGDP_t = the change in GDP between years t-1 and t.

$(I/GDP)_{t-1}$ = the ratio of domestic investment to GDP in year t-1 of Bangladesh.

XR_t = the exchange rate, defined as a ratio of the domestic currency to the US $ at year t.

$V(XR)_t$ = the squared deviation of the exchange rate from its mean over the period 1977-1999.

The model is estimated using regression analysis with annual data for the period 1977-1999.

RESULTS OF THE (UN) MODEL

The result shows that there is a moderate relationship between inflows of FDI into the Bangladesh and the size of the market, depicted by GDP_{t-1}, but no relationship was found between changes in GDP and the level of FDI. This is partly because the change in GDP has varied slightly as measured by the coefficient of variation; Bangladesh economy has been growing at a fairly stable and therefore, the increase in the level of GDP_{t-1} captures both the expansion of the economy and its fluctuation. The share of domestic investment in GDP did not play a statistically significant role because there was vary little variation in that ratio for Bangladesh during the period under consideration when is measured in constant price. The level of neither the exchange rate nor its variation also had no significant effect on the inflows of FDI to Bangladesh.

Of course, this does not mean that those variables may not have been important in determining FDI inflows in actuality. Their potential effect might have been obscured by other variables. In this case, it is the level of indebtedness and the trade variable (the latter measuring the degree of openness - calculated as the ratio of export plus import to GDP), that might have precluded the effects of the level of exchange rate or its variation on FDI inflows entering the equation in a statistically significant manner.

During 1978-1999, there was a substantial increase in indebtedness in Bangladesh that led to the depreciation of the currency in several times. Thus, while a high ratio of trade to GDP would be expected to induce inflows of FDI, the external indebtedness played a significant role in discouraging inflows of FDI to Bangladesh economy.

Estimation of the Model for Bangladesh : 1978-1999

(t-ratios in parentheses)

Constant	GDP_{t-1}	ΔGDP	$(I/GDP)_{t-1}$	XR_t	$V(XR)_t$
-1.02	.018	.023	.063	.021	-1.06
(-.73)	(3.11)	(.86)	(.97)	(.52)	(1.28)
					$R^2 = .83$
					D.W = 1.39

Model Two

There are several time series econometric models that have attempted to quantify the effects in determining the behavior of FDI inflows (UNCTC, 1999). In this study, in formulating a model of FDI inflows in Bangladesh, some of the factors suggested in the literature have been quantified. The fullest version of the reduced form of the model used in this study is:

$$FDI = \beta_1(GDPCAP) + \beta_2(GDPGROW) + \beta_3(IPI) - \beta_4(EARN) - \beta_5(XRATE) + \beta_6(EXPORT) + \beta_7(DSWAP)$$

Where,

GDPCAP	=	GDP per capita
GDPGROW	=	GDP growth rate
IPI	=	Industrial Production Index
EARN	=	Wage Cost
XRATE	=	Real Exchange Rate
EXPORT	=	Export orientation
DSWAP	=	Debt-equity Swap

Let us explain the rational for choosing the independent variables in equation.

Size of the market: The size of the market, typically proxied by the level of GDP appears to be an important determinant of FDI flows. Root and Ahmed (1979), Torrist (1985), Schneider and Frey (1985), Petrochilas (1989), Wheeler and Mody (1992), Jun and Singh (1996) found market size to be a significant determinant of inward FDI. Hence, both per capita GDP (GDPCAP) and the growth rate of GDP (GDP%) are included to control actual market size.

Export: There is widespread perception that open economics receive more FDI (Chen, 1994; Rana, 1990). The export variable is included in the equation for at least four reasons. First, exports enable countries to specialize in the production of commodities in which they have a comparative advantage; resources, which are saved

in this way, can then be used for investment. Second, trade provides a vent for surplus commodities, which bring other wise unemployed resources into use. Third, trade can expand production possibilities through its effect on such factors as competition, access to new knowledge, technology and ideas; these are so-called dynamic gains from trade. Fourth, trade enables countries to purchase goods from abroad. If there are no domestic substitutes, the ability to import can relieve bottlenecks in production and thus increase savings and investment, and imports may simply be more productive than domestic resource. Hence, export in relation to GDP is included as a control variable (EXPORT).

Debt-equity Swaps: Since the late 1980s, several developing countries with large debt burdens have implemented debt-conversion programs. Countries with sizable programs include Argentina, Bolivia, Brazil, Chile, Mexico, Philippines and Venezuela (Jun and Singh, 1996). Those components of debt-equity swaps are found to be correlated with FDI flows. Debt-equity swaps as ratio of the total long-term debt is employed here as a control variable (DSWAP).

Industrial Production: Culem (1988) and Jun and Singh (1996) analysed the bilateral flows of FDI for 66 countries. They found that the characteristics of the investing firm's home country (such as growth rates and labor costs) did improve the performance of the model. In order to control home country characteristics, the average industrial production index of Bangladesh is included here as a control variable (IPI).

Exchange Rate: Some literature exists on the relationship between FDI and exchange rate movements (Lucas, 1993). The response of FDI to exchange rate movements may take numerous forms. Firms may expand or contract existing production operations, enter or exit foreign markets, change the location of their facilities, reinvest or repatriate earnings or consolidate market power through mergers and acquisition. In order to control for this possibility, the real exchange rate (XRATE) is included in the equation.

Wage Cost: Recent results for developing countries indicate that wage costs are a significant determinant of FDI flows. Schneider and Frey (1985), Locas (1993),

Wheeler and Mody (1992) and Jun and Singh (1996) all found wage cost variable to be significant. In this study, a real earnings index as a control variable for real wages (EARN) is included.

RESULTS

Model -1: Initially, FDI is regressed with GDP growth rate (GDPGROW) and a time dummy (to capture other time-related effects). GDP growth rate is significant at the 5 per cent level (with a t-value of 1.86). The time dummy and GDP per capita are significant but only at the 10 per cent level.

Model -2: In this specification, real earning (EARN) and debt-equity swaps (DSWAP) are included as control variables. As expected, the earning coefficient is negative and both variables are statistically insignificant.

Model -3: This specification includes the exchange rate (XRATE) and the average industrial production (IPI). The exchange rate has the expected negative sign. Both variables are statistically insignificant.

Model -4: This specification includes export orientation (EXPORT) as control variable. The EXPORT is significant at the 10 per cent level with t-value 1.38. Given that EXPORT has the strongest correlation with FDI, this result is not surprising. The correlation between EXPORT and FDI is 0.62.

Regression results are summarized in the table given below. Overall, regression results suggest that there is a moderate relationship between inflows of FDI in Bangladesh and the size of the market depicted by GDP growth rate. The time dummy and GDP per capita are also found significant but only at the 10 per cent level. To some extent, export variable also influences in attracting FDI in Bangladesh. Results of the regression model-2 do corroborate the findings of the UN model mentioned above. From the regression results of model-2, we can conclude that home country market, per capita GDP and export-orientation are the major determinants of FDI in Bangladesh. That is, hypotheses 1, 2 and 3 as outlined earlier can be accepted to analyze the behavior of FDI in Bangladesh.

Regression Results				
	Model-1	Model-2	Model-3	Model-4
Dependent variable	FDI	FDI	FDI	FDI
Constant	-1.81	-1.02		
	(-4.62)	(-2.49)		
Time	. 018	. 06		
	(3.13)	(2.89)		
GDPGROW	.023	. 021	. 022	. 019
	(1.86)	(1.94)	(2.71)	(1.23)
GDPCAP	. 006	. 003	. 004	.001
	(1.38)	(1.12)	(.19)	(.52)
DSWAP		. 013	. 016	. 02
		(.12)	(.15)	(.18)
EARN		-. 001	-. 001	-. 004
		(-. 16)	(-. 16)	(-. 31)
IPI			. 021	. 016
			(.12)	(.07)
XRATE			-. 001	-. 001
			(-. 014)	(-. 10)
EXPORT				. 018
				(1.38)
F-value	19.07	23.20	17.15	22.71
D.W.	1.86	1.72	1.36	1.68
R^2	.64	.48	.45	.38

CHAPTER VIII

FDI POLICIES OF SOME SELECTED ASIAN COUNTRIES: COMPARISON WITH BANGLADESH

In recent years, Asia and the Far East have seen the emergence of some of the fastest growing economies in the world. In very large measures, these economies have been highly externalized and the main force has been export led growth. Some of the larger continental economies like India and China have followed a different logic and path to economic development and this has been intrinsically linked to their socio-economic philosophies. This chapter attempts a comparative assessment of the growth paths followed by various countries in this region and the role of and environment for FDI in promoting economic development. All the data and information used in this chapter have been derived from the World Investment Reports of various years.

Governments of different developed and developing countries have variant and district attitudes toward FDI. Some countries are found to have highly positive attitude toward FDI as reflected through their liberal and lucrative FDI policies; whereas some are found to have moderately positive attitude as because FDI policies they adopted entail some sort of regulatory frameworks that help determine the magnitude of FDI inflow into different sectors, the proportion of equity participation, the pattern of management control of TNCs (Transnational Corporations), the forms of incentives, mode of profit and capital repatriation etc.

A few number of countries – specially some East European Countries are still noticed to have a bit negative attitude, overtime the attitude is gradually changing to positive direction, toward FDI as manifested through their FDI policies. Sharp perusals of their policies distinctly expound that they are more restrictive rather than liberal in view of FDI inflow attraction.

"Foreign Direct Investment (FDI) and TNC operations can impact on social, political and economic conditions in a host country. Hence, government policies towards

investment and technology transfer by TNCs can best be viewed within the context of a country's overall social, economic and political development system and its goals" (United Nations, 1992 p.4). Whatever lucrative and liberal FDI policy formed and offered, it will not work well, if the government of a country fails to ensure sufficiently well educated and skilled labor force, adequate transport system, fair legal system, strong antimonopoly policy, sound macroeconomic policy, and wealth creating culture.

Evidence of recent years in most developing countries discerns that they adopt a more flexible and liberal FDI policy with a view to modernization, technological upgrading and improving the productivity and global competitiveness of different sectors in their economies.

FDI policy adopted by a host government should be constituted and operationalized in such a way that optimizes the net benefits of the nation arising from FDI inflow, technology transfer and other operations by multinational companies. In fact, FDI policy system is highly interactive, complex and ever changing. "For example, if the country's goal is to expand exports by attracting export-oriented FDI, its exchange rate must be maintained at a level to foster exports; its import tariffs and non-tariff barriers to trade in capital goods and intermediate inputs must be such that firms can access these necessary products at competitive costs; and its system to regulate international capital flows must allow inflows of required capital and inflows of profits and other payments for factors of production and inputs sources from abroad" (United Nations, 1992, p.4).

In forming FDI policy, a country must consider a wide range of factors such as economic development level of the country, resources availability, labor and employment condition, level of technology, sufficiency of capital, political and economic system and philosophy, trade structure, etc. Countries interested in attracting FDI inflow should frame FDI policy that must ensure equal treatment for local investment, joint venture and 100% foreign investment, simplify the formalities and procedures relating to the inception of FDI, and guarantee different incentives system and facilities commensurate with the economy. Inappropriate FDI policy and

incentives system may bring perverse and unexpected results/costs rather than envisioned net benefits on the economy of the host country. In general, the responsibility of instituting FDI policy is entrusted to the government of a country.

Government normally sets some development goals in light of its country's pace of economic development, level of technology, growth of export and import, job creation, the balance of payments and competitive strength and growth of domestically owned firms. Once the FDI policy is instituted, it must be operationalized through a set of regulatory and promotional frameworks and implemented through administrative structures and processes of the government.

FDI policy is not constant but subject to constant reforms and modifications as new phenomena – constraints and opportunities – appear in conditions both internal and external to the country. No FDI policy or incentives system is appropriate in attracting FDI for all countries under all circumstances. "The evaluation of the performance of TNCs under any incentives will vary from country to country, depending on foreign investment policies. A system that is appropriate for one country may be highly inappropriate for another country. The reasoning, 'the incentives system in country X has been successful, therefore country Y should use this system' is incorrect, except in the unlikely situation in which the goals, policies, evaluation criteria, economic conditions, and the institutional structures, values and abilities of government administrators to implement the system are the same in both countries" (United Nations, 1992, p.4). A policy system that is appropriate at one time may be deemed inappropriate at some other time.

In general, FDI policy has two components: regulatory aspect and promotional aspect. Regulations are designed to absorb maximum benefits per unit of investment and to ensure that TNC activities are consistent with achieving the country's goals and objectives. Promotions are designed to encourage TNCs to invest more with a view to maximizing the total amount of FDI inflow. Promotions entail different forms of incentives package such as tax holiday, ownership facility, accelerated depreciation, facilities for repatriation of invested capital, profit and dividend, reduction of import tariffs on inputs and capital equipment, trade protection, labor subsides and so on.

In framing the pragmatic and suitable FDI policy for a country, a balance between regulation and promotion is indispensable and failure to make a proper balance must result in adverse performance of FDI. The amount of regulation or promotion in FDI policy largely depends on the pervasiveness of regulations in country's overall economy. The more regulated the economy of a country, the more restrictive and regulatory FDI policy tends to be – resulting less promotional features exposition in FDI policy. Conversely, the less the regulation in the economy of a country, the less the restrictive FDI policy – resulting more promotional features exposition in FDI policy. If a country's FDI policy is more restrictive, its incentives system for FDI attraction will be more complex and extensive. For example, in Indonesia, where there has been pervasive regulation of the economy, the incentives system for FDI attraction is highly complex and promotional feature in FDI policy is restrictive. But in neighboring countries Malaysia and Singapore, where there are low level of government regulation of their overall macroeconomics and their incentives system is relatively simple that emphasizes promotional features over regulation.

Over the last two decades, it is discernible that the environments in most developing countries have acted to extricate their economies from regulations and moved towards more liberal FDI policies and continued to modify their incentives system to make lucrative and simplistic to the foreign investors. Incentives system in many developing countries is found to have placed more emphasis on the promotional features instead of regulations.

The underlying objective of placing emphasis on promotional aspect (that is incentives system) is to achieve country's development goals. However, 'increasing investment should not be the goal of an incentives system" (United Nations, 1992). The chapter discusses the policy and incentives systems of some selected Asian Countries that have attracted maximum amount of FDI in the last two decades. A comparison of the policy and incentives system between the successful FDI attracting countries and Bangladesh has also been made.

CHINA

FDI influx into China took place following the Deng Xiaoping's 'open door policy' in 1978 with the expectation of hastening the country's modernization in technology and management, promoting exports and also encouraging outward FDI from China. 'open door policy' under socialist conditions of China registers a two-tier economy in which private marketing networks based on market mechanisms coexist with government planning and distribution system. China invites FDI, leaving no concession on national economic and political sovereignty, to become a capital exporter eventually. China liberalized its external trade, technology transfer, investment and so on under 'open door policy. At the beginning of 'open door policy', it was replete with the gamut of restrictions, although incessant flexibility and liberalization were brought in over subsequent years. As a result from the mid-1990s FDI influx had gone up by leaps and bounds and reached a paramount height in the late1990s.

'The Chinese-Foreign Joint Ventures 1979' is the basic law for the first time that allowed FDI inflow into China. Later three major policy announcements were made: the implementing regulation of 1983, the State Council Provisions of 1986, and the 1990 amendments to the basic law (Chandra N.K.,1999). Under the basic law only a joint venture (JV) with a Chinese firm was allowed with the sole approval of the central government and the contract between the two parties would determine the respective shares on each side, the composition of the board of directors, the allocation of financial responsibilities between both parties, the time limit of the contract (beyond which assets of JV be owned by Chinese partner) and so on.

Over years, some initial stipulations on JV were relaxed gradually. This situation has increased the flexibility of China's incentives system, but at the cost of considerable delays in the approval process and a dysfunction increase in the uncertainty of both foreign firms and Chinese administrators, enterprises and organizations when entering into the negotiation process over the operations of foreign firms in China (United Nations, 1992). The incentives measures below offered by the government of China in different years are a clear evidence of liberal attitude about FDI: approval of FDI

contracts by the provincial and local governments, absolute control of foreigners on the management of the company, extenuation of the tenure of JV (as mentioned in the initial contract), remittance of all profit, right to use land by paying fees, favorable tax bracket and so on.

INDIA

Immediately after the independence, India remained highly reticent and protectionist about foreign capital influx and followed a restrictive policy toward FDI inflow. A crux of rules, regulations and procedures were incorporated to its policy to build-up self-reliant economy circumscribing the role of FDI influx. India's FDI policy was first enunciated by then prime minister Jawaharalal Nehru in 1947, allowing some sort of FDI influx subject to a lot many stringent restrictions. A policy of 'Selectivity' was adopted to minimize the country's dependence on foreign investment through better utilization and promotion of domestic human and material resources (Mathur A, 1992). In 1949, Jawaharalal Nehru relaxed restrictions on FDI inflow a bit following on the statement on the enunciation "the necessity of FDI" at parliamentary meeting. In the late 1950s government further liberalized FDI policy 'in the form of tax holidays, subsidies and long-term credit' (kidron M. 1965) when faced with two severe crises – a foreign exchange flight and a crisis in financial resource mobilization. Government also ensured to some extent equal treatment for both the firms – domestic and foreign.

In the 1960s, policy on FDI became restrictive and 'this shift in policy occurred in part due to revival of concern about certain effects of FDI, including the drain of foreign exchange and foreign economic domination (Mathur A.,1992). As an evidence of restrictive attitude government set-up the 'Foreign Investment Board' (FIB) in 1968 to deal with the foreign firms having equity participation not more than 40% or Rs 20 million. This attempt narrowed down the role of FDI not only in terms of the sectors it is allowed to enter but also the percentage of equity shareholding foreign firms are permitted. The scope and opportunities for FDI were significantly tightened by the "Foreign Exchange Regulation Act" (FERA) in 1973.

In the decade of 1980s, Indian government evidently realized that FDI influx had a positive role to play in country's growth and development. Within the overall policy framework, India's policy toward FDI attraction and transfer of technology became more open and liberal. This shift in official policy occurred in the wake of the second oil crisis and India's failure to boost significantly her manufactured exports (Kumar N. 1990). In recent years, to encourage TNCs to undertake export-oriented manufacturing, different incentive measures and liberalizing steps were taken by the Indian government. The "amendment to the restrictions on large and foreign-controlled enterprises under MRTP (Monopolies and Restrictive Trade Practices Act) and FERA (Foreign Exchange Regulation Act) signal this more liberal environment (Mathur A.,1992). The continuation in the liberalization of FDI policy was reflected in the industrial policy of 1990. In very recent years, FDI in India is expected to create more employment, accumulate financial resources and modernize technology and accelerate the country's efforts to increase manufactured exports and government is determined to continue more favorable treatment to foreign investors to keep on pace of economic development.

REPUBLIC OF KOREA

Republic of Korean industrialization was somewhat akin to Japanese industrialization process. Textiles, clothing and foodstuffs were the leading industries until 1962 and since then government has been endeavoring to attain faster industrialization through economic planning and fiscal measures. Unlike other countries, Korea emphasized foreign debt rather than FDI in the beginning stage of its industrialization. The high-debt ratio of Korean companies is a direct result of heavy borrowing for investment purposes (The confederation of Engineering Industry, 1992).

In the first half of 1960s labor-intensive consumer goods and in the latter half, the petroleum products and cement and in the 1970s heavy and chemical product industries grew rapidly. No other countries in Asia had been able maintain spectacular economic growth rate in the 1970s, 1980s and early 1990s without sufficient amount of FDI influx. In recent years, FDI is very much welcome to Republic of Korea and is allowed in most industries.

The basic laws governing and regulating FDI in Republic of Korea are 'Foreign Capital Promotion Act 1966' and 'Foreign Capital Inducement Act 1983'. Modifications of laws and offering diverse incentives system are common phenomena in Korea. However, the overall policy taken by the government of Korea does not impute any major restrictions on the foreign investment equity ratio (which is determined according to the agreement between a foreign investor and Korean partner), management of the company, employment of labor, remittance of profit, etc.

The amount of FDI influx attracted by Korea compared to its size of economy and level of economic development is relatively meager when compared with that of some other Asian countries, despite offering different incentives system. In the late 1990s, Korea bitterly experienced that sufficient amount of FDI influx is inevitable. However, to keep on pace of economic development, it further liberalized its policy by offering some other additional incentives to the foreign investors.

PHILIPPINES

Philippines economic policy welcomes FDI for achieving its economic development goals. FDI influx into Philippines was virtually commenced in 1967 with the enactment of Investment Incentives Act, although it was not initially successful enough to attract sufficient amount of FDI as the 'policy was somewhat ambivalent then' (Esiritu A.C. 1977). During the 1970s. 5 percent growth rate in industrial sector was observed. The contribution of the industrial sector to GDP increased by 34 percent in 1984 compared to the 28 percent growth in 1960. Indeed, since martial rule (1972), there has been a climate of increasing economic stability – at least in terms of legal framework, not necessarily in terms of employment and price levels – and an expansion of fiscal incentives inspire of the combined effects of the worldwide recession and inflation and the quadrupling of oil prices (Esiritu A.C., 1977).

In the early 1970s, some imprudent and ambitions development programs placed emphasis on high cost industrial undertakings that were largely financed by foreign investors in cooperation with some affluent families. The government of Philippines subsequently assumed the ownership of these undertakings due to the inefficiencies

and the severe oil crisis. "During the social and political upheavals between 1983-86, foreign investment tended not to shy away, but disinvest from country. However, the gains in 1987 and 1988 have put the economy back on track with a targeted rate of growth of 6.5 percent unit 1992 (The confederation of Engineering Industry,1992, p.52).

Recently, the economic policy Philippines adopted and incentives system it offered to foreign investors are more encouraging, where lots of options and opportunities are available. Recently adopted incentives system allow 100 percent foreign ownership if the company is involved in pioneer activity or located in an area of 'Export Processing Zone' (EPZ). Moreover, participation in management of company, tax holiday facility, exemption of custom duties on import machinery, equipment and spare parts, and so on are allowed under new incentives system.

THE REPUBLIC OF SINGAPORE

Singapore, a relatively small and fine country with highly skilled labor, has been able to maintain a fairly upturn growth rate since its independence. It places heavy emphasis on efficiency and growth in its overall policies. The government attitude toward FDI inflow has been highly liberal and open. To maintain the pace of economic growth rate, Singapore continuously emphasizes FDI inflow and outflow and technology transfer to restructure and develop its economy, until recent years. The role of FDI has, however, tended to increase, though domestic technology has continued to be of vital significance for service sector in Singapore.

'The Economic Expansion Incentive Act-1967' (amended 1970 and 1975) is the basic law concerning FDI. Initially this law entailed some restrictive measures regarding FDI although some were dropped significantly in two successive amendments. Recently, Singapore welcomes all types and sizes of industries for further economic development and promoting Singapore as an international center for business. Singapore is such a country that continuously reviews its policy and incentives system on regular basis. Presently, the policy it adopts is comparatively more promotional and open for FDI inflow compared to that of some other neighboring countries. To encourage FDI inflow, policy waives restrictions on remittance, duration of JV, export

obligations, ownership of industrial or commercial land; and offers different facilities like tax holidays, reduction of income tax etc.

THAILAND

Thailand is one of the rapidly growing countries in the Asia and its pattern of economic development is somewhat akin to Malaysia, Indonesia, Singapore Philippines etc. The continual economic growth basically rests on flourishing agricultural and manufacturing sectors. The fast growing industrial sector of Thailand keeps on the pace of global standard. "The economy reached take-off stage in 1988, with on 8.5 percent growth rate, much of it from manufacturing. The main priorities for industrial development have been export oriented industries, agro base industries, electronics and engineering" (The confederation of Engineering Industry, 1992).

'The Alien Business Law 1972', 'Investment Promotion Legislation 1954' and 'Investment Promotion Act. 1977' are the basic laws guiding and controlling FDI influx. In the late 1950s and 1960s, the attitude of Thai government was not so open as these recent years. Keen interest in Thai government has been found since long to flourish high technology industry base (like electronics) by attracting multinational companies. To materialize its objective, the package of incentives and facilities offered to foreign investors has been made very attractive and consequently there has been a great deal of interest shown by investors especially from Japan, Hong Kong, the Republic of Korea and Taiwan Province of China (The Confederation of Engineering Industry, 1992).

The Thai government has been very successful to attract substantial amount of FDI in 1990s due to cheap and skilled labor force, control of inflation, and some favorable environment within the country. The Thai government at present views the private sector as a powerful vehicle of economic development and emphasizes FDI inflow to strengthen private sector. However, the FDI inflow into Thailand is still observed to have upturn trend due to different incentives package continuously offered by Thai government.

MALAYSIA

Before 1980s, Malaysia's government attitude toward foreign investment was reticent and the government emphasized policies to enhance the role of ownership in the economy by ethnic Malays under its 'Bumiputera Policy'. The government of Malaysia brought about drastic change in its policy about multinational companies in the first half of 1980s when it confronted with the problem of falling energy and commodity prices-which narrowed down the prospect for economic growth under policies adopted then. The resultant effect of the problem was sharp decline of FDI. However, the government of Malaysia adopted a policy for multinational company, far away from regulation, toward promotion of FDI influx and technological transfer.

In fact, the government of Malaysia undertook major revolutionary industrialization programs in 1982 and continued to function consistently to achieve its development goals. The government of Malaysia also changed its foreign investment incentives system. The purpose of this change was to accelerate economic growth, even if this change entailed a shortfall in its goal of increasing the level of Bumiputera ownership (United Nations, 1992). Although quite a satisfactory growth rate of 7.5 percent per annum was noticed in Malaysia during the 1970s and early 1980s, the country faced a slow down in its growth rate in 1986-1988 due to falling commodity prices. However, the crisis prompted the policy makers to restore the economy from slow down condition by attracting and employing foreign government investment into manufacturing sector. In view of this the Malaysian government has taken several measures to remove restrictions and attract foreign investments and in 1988, 4.5 percent of private sector investment which went into manufacturing came from foreign sources (The confederation of Engineering Industry, 1992).

Over last three years, a change has been discernible in the policy of Malaysian government due to slow down of economic growth and continuous economic recession arising out of unfavorable ties with US government. However, the government of Malaysia is at present emphasizing more on domestic investment rather than foreign investment – as a step of being self-reliant with less dependence on foreign capital.

INDONESIA

Indonesia is still in the early stage of industrialization. Although its economy is predominantly agricultural, the substantial amount of FDI inflow was absorbed in petroleum, gas, coal, rubber and some other extractive industries. In fact, Indonesia was not so open and free about FDI inflow since its emergence. During the 1970s, Indonesia had been successful in maintaining quite an impressive growth rate (about 8 percent) – where mining was the main factor behind this growth rate. In the mid-1980s, Indonesia faced a severe problem of price fall of oil and to restore the economy from slow down condition, the government announced a new package of incentives to attract more FDI inflow and to enhance export through gas and non-oil commodities. The incentives enunciated by the government had been very much successful in gearing up the FDI inflow. Agriculture, industry, mining, energy, pharmaceutical, food products, diary and agro products and plantations, etc. were virtually open for foreign investors. The new set of incentives allowed the foreign investors to hold upto 80 percent equity in a company subject to availability of potential for export.

The government of Indonesia also started a process of denationalization in the mid 1980s. As a result of the deregulation measures and incentives for foreign investment announced in 1987, the total value of foreign investment projects signed in 1988 was double the 800-900 million registered in the previous two years (The Confederation of Engineering Industry, 1992). Recent years witness that Indonesia is getting more liberal attitude toward FDI inflow and to keep on pace of economic growth it is more emphasizing on FDI inflow. The series of new incentive measures announced in different years by the government and upturn trend of FDI influx over years corroborate the government's open and free policy in favor of FDI inflow. However, comparison of the incentive measures in selected Asian countries with that of Bangladesh is given below:

COMPARISON OF THE INCENTIVE MEASURES IN SELECTED ASIAN COUNTRIES

Particulars	China	Thailand	Republic of Korea	India
(Foreign Investment) basic policy	Encourages foreign businessmen, overseas Chinese and Chinese compatriots from Hong Kong. Maco and Taiwan to enter into JVs or other forms of cooperation with PRC institutions. They are also allowed to establish firms under their exclusive ownership.	The Alien Business Law-1972 places business activities into 3 categories A, B and C. A. Closed to aliens B. Closed to aliens unless Promoted by the BOI C. Open Aliens are granted permits only if the authorities are convinced that such an activity cannot be carried out completely by a majority Thai owned company	Foreign investment is welcome and allowed in all industries excepts for those specified in the negative list.	Foreign investment is welcomed specially when accompanied with the transfer of sophisticated technology. Foreign investors are seldom allowed portfolio investment.
(Regulations for foreign investors) Limitation on foreign equity	The law on Chinese-foreign JVs sets a minimum of 25 percent of investment by foreign party, but no maximum. The Government encourages a majority foreign share because it increases the likelihood of new technologies being brought in and also increased exports.	If production is mainly for domestic distribution Thai nationals are required to hold shares not less than 51 percent of the registered capital. For a project in a agriculture, mineral exploration or service sector, Thai nationals must hold not less than 60% of the registered capital. Where at least 50% of the output is for export, foreign investors may hold majority shares. In case all production is for export 100 percent can be owned.	No restrictions on the foreign investment equity ratio which is determined according to the agreement between a foreign investors and his Korean partner. Any foreign ownership composition up to 100 percent is permitted.	Under FERA, foreign equity cannot exceed 74 percent except in case of 100 percent EOUs. For any new issue of equity capital, 40 percent must be placed within India if foreign equity holding is between 60-74 percent and 25 percent if between 40-51 percent. In the pharmaceutical industry certain specific types of drugs have been identified to which FERA companies are restricted.

Particulars	China	Thailand	Republic of Korea	India
Remittance	Allowed joint ventures can remit abroad all net profits as well as funds received upon the scheduled expiration or early termination of the venture.	All remittances of funds into and out of Thailand require exchange control approval, which is granted depending on a company's tax liability. Foreign exchange controls are seldom exercised in Thailand but BOI promotion provides extra protection against possible constraints on the remittance of interest and profits or the repatriation of the capital.	Overseas remittance of the following items is guaranteed in accordance with the contents of approval based on the Foreign Capital Inducement Act: a. Dividends received by holding the stock or shares; b. Sales proceeds of the stock or shares; c. Principal, interest and fees to be paid under a loan contract or a public loan agreement; d. Royalties to be paid.	Under India's existing regulations, remittances of technical fees, interest, dividends etc. are freely permitted subject to the payment of Indian taxes. Repatriation of capital along with appreciation in stock, if any, is freely permitted subject to Indian taxes.
Acquisition of real estate	Foreign investment in land is not permitted. However a foreign investor may obtain the right to use of land paying a fee for its use. Investment in housing, both within and outside special economic zones, is prevalent in the case of tourist hotels, apartments and residential housing.	Ownership of land is limited to Thai nationals except when BOI grants special permission in connection with a promoted project. Under current regulations, land ownership by foreign companies listed on the securities exchange and promoted by the BOI is limited to five rai for industrial purposes, 10 rai for commercial use, 25 rai for industrial use and 50 rai for agriculture.	Property rights of a foreign investor and a foreign invested enterprise are guaranteed in accordance with the provisions of the laws. The Alien Land Law requires that firms with more than 50 percent foreign ownership obtain approval from the Home Affairs Ministry to buy land. No firm, foreign or local, may own property that is not directly connected with its business operations	Not allowed except to set up manufacturing activities governed by the location rules.

Particulars	China	Thailand	Republic of Korea	India
Employment	According to provision for labour management in Chinese-foreign JVs, JV has the right to decide on the employment of its staff and workers. When a JV recruits its employees, it has to apply to the local labour department for a quote for the recruitment stating the number of people and their qualifications.	No restrictions.	No restrictions-free to employ anyone.	No restrictions.
Transfer of shares Liquidation of company	In case it is prior to the date of expiration the intention of dissolution should be announced clearly and the joint venture should register with the Department in charge of Industry and Commerce. Otherwise liquidation to be under-taken by a liquidation committee. The Board of Directors to work out procedures and principles.	No special regulations apply but restrictions on foreign ownership effectively prevent foreign interests from acquiring majority control of locally owned companies in most cases.	Free to transfer shares if publicly quoted. Foreign firms cannot acquire existing stock in local companies. No restriction on liquidation except that employee has to be notified three months in advance.	Indian laws and regulations permit transfer of shares by overseas investors. The investors can also retain their shares as long as they like. Any transfer of shares of a company registered in India by a non-resident to another person/company to be valid should be confirmed by RBI.
Incentives	Preferential treatment is available for investment in government preferred sectors. These are: 1) More favorable terms of cooperation. 2) Faster government approval. 3) Priority arrangement for designing and	A promoted investment project is granted exemption from corporate income tax for a period of 3 to 5 years depending on the size of investment or number of full time employees. Guarantees: Against competition from new state	Regulations on capital goods imports by foreign investors significantly eliminated. Procedures for foreign firms wishing to do business in other areas simplified. Those joint ventures whose ownership is less than 50 percent, whose investment	Complete tax holiday. A 100 percent export oriented undertaking or a new industrial undertaking set in the export processing zones permitted a completed tax holiday for a period of 5 years during the fast 8 years of operations. This 5-

Particulars	China	Thailand	Republic of Korea	India
Incentives continued	construction by Chinese engineers and for supply of building materials and equipment 4) Faster granting of import licenses for materials and equipment. 5) Tax concessions (obtained through application). a) Exemption from import duties. b) Preferential income tax rate of 15 per cent for firms investing in the special economic zones. c) Exemption from income tax in the first two years and 50 per cent reduction in the next 3 years for firms investing in above areas with an operation period of 10 years or more. Priority for getting raw and processed materials, fuels and other sources of energy needed for production. 6) Export licenses and exemption from export duty on unrestricted exports. 7) An increased	enterprises. Against state monopolization of the sale of products similar to those produced by promoted projects. Against price controls. Permission to export. Against imports by government agencies for state enterprises with taxes exempted. Protection measures (subject to justifications and needs). Imposition of surcharge on foreign products at a rate not exceeding 50 percent of the CIF value for a period not more than 1 year at a time. Import ban on competitive products. Authority by the Chairman to order any assisting actions or tax relief measure for the benefit of promoted projects. Permissions: To bring in foreign technicians and experts to work in promoted projects. To own land for carrying out promoted activities.	amount is less that $1 million and who did not apply for tax exemptions for their operation in Korea, need only report their intentions to the Government when they want to produce a new product in the same industrial category. Joint venture firms, more than 50 percent of which are owned by foreign partners, no longer need the approval of the trade committee when they want to engage in foreign trade. Various tax exemptions and reduction given to all foreign invested enterprises in the past were abolished through the adjustment of the tax exemption and reduction system. However, for any foreign invested project which is deemed to contribute critically in the development of the economy, the period of tax exemption is 5 years.	year holiday is available to all tax payers including foreign companies. Such units are also allowed to sell upto 25 percent of their production in domestic target area subject to payment of appropriate customs duties. Partial tax holiday. New industrial undertakings producing commodities other than the ones specified in the 11th Schedule of IT Act, 1961 ships or hotels or business repairs to occan-going vessels or other powered crafts are allowed deduction of 25 percent from their profits (20 percent in the case of non-corporate taxpayers) for a period of 8 years. Incentives for exports. The whole income derived from export of goods qualifies for exemption. Interest payable by an industrial undertaking in India on money borrowed or debts incurred in a foreign country for purchase of plant and machinery or raw materials is exempt from income tax up to a stipulated rate.

Particulars	China	Thailand	Republic of Korea	India
Incentives continued	proportion of domestic sales for products urgently needed in China and those, which are still being imported even to the extent of becoming the main proportion.	To take or remit abroad foreign currency. Tax incentives: Exemption or 50 percent reduction of import duties and business taxes on imported machinery. Reduction of import duties and business taxes of up to 90 percent on imported raw materials and components. Exemption from corporate income taxes for 3 to 8 years with permission to carry forward losses and deduct them as expenses for up to 5 years. Exemption of up to 5 years on withholding tax on goodwill, royalties or fees remitted abroad. Exclusion from taxable income of dividends derived from promoted enterprises during the income tax holiday. Additional incentives: (i) For enterprises in investment promotion zones Maximum reduction up to 90 percent of business tax on the sales of products for a period up to 5		Units exporting part of their production get incentives like duty drawback, cash compensatory support and confessional export credits

Particulars	China	Thailand	Republic of Korea	India
Incentives continued		years. Reduction up to 50 percent of corporate income tax for 5 years after the termination of a normal income tax holiday. Allowance to deduct from the taxable corporate income up to 25 percent of the costs of installing infrastructural facilities for 10 years from the date of income earning. (ii) For export enterprises: Exemption of import duties and business taxes Allowance to deduct from the taxable corporate income the amount equivalent to 5 percent of an increase in income derived from export over the previous years, excluding costs of insurance and corporate income tax for 5 years after the termination of a normal income tax holiday or from the date of income earning.		
Taxation	Industrial and commercial consolidated tax levied on agricultural and industrial products and on turnover of commercial and service trades. There are 104	Business tax is levied on gross receipts and is usually calculated monthly. The rate depends on the nature of business. A municipal tax at 10 percent of the business tax is		General level of tax on royalties, dividends and know-how fees is as follows: Dividends 25 percent, know-how fees 30 percent, royalty 30

Particulars	China	Thailand	Republic of Korea	India
Taxation continued	categories and a total of 42 tax rates. Income tax is on the net profit of JVs at 30 percent and local tax of 10 percent of the assessed income tax making a total of 33 percent. JVs in SEZs, in economic development zones and on Hainan Island pay income tax at 15 percent. Investment projects in energy, communications or harbors building, projects introducing new technology and projects with an investment of $30 million or more and slow capital returns at 15 percent. Other investment project in above areas at 20 percent. A new joint venture with foreign investment may be exempted from income tax in the first 2 profit making years and allowed a 50 percent reduction in the third to fifth year. Real estate tax: Tax on buildings (on the owner) at 1.2 percent of its value or 18 percent annum. Tax on land (on	paid at the same time. Corporate income tax is payable on profits and is assessable twice a year. Profits remitted or retained abroad from a business operated in Thailand are subject to a 20 percent withholding tax in addition to corporate tax. Withholding rate on dividends is 20 percent. Corporate tax --- standard rate is 35 percent on net taxable profits. For companies registered on the Securities Exchange of Thailand tax is at 30 percent.		percent corporate tax 50 percent. A host of tax incentives such as accelerated depreciation. Investment allowance, partial tax holiday, full tax holiday (in case of units in FTZs and 100 percent EOUs, tax exemption on profits from exports, etc. Income tax rates are given in the Finance Bill each year. For 1989-90 they are: Foreign company- dividend at 25 percent. Interest received from Government or Indian concern or money borrowed or debt incurred by Government or Indian concern in foreign currency, at 25 percent. Royalties or fees for technical services at 30 percent. Other income at 65 percent. Domestic company: Widely held-total income at 50 percent. Closely held – trading and investment companies at 60 percent. Other than above at 50 percent. For foreign technology costs a lump sum payment can be made but this is subject to a

Particulars	China	Thailand	Republic of Korea	India
Taxation continued	the occupant) at 1.8 percent of the value based on location. Income tax on foreign enterprise is levied at a progressive rate: 20 percent annum for income <250,000Yuan 25 percent p.a. for 258,001 500,000 Yuan 30 percent p.a. for 500,001- 750,000 Yuan 35 percent p.a. for 750,001 - 1,000,000 Yuan 40 percent p.a. for>1,00,000 Yuan.			tax at 30 percent. While this can be borne by the Indian venture, the tax must necessarily be added to the overall project cost. Normally, royalty should not exceed 5 percent of net sales. The tax of 38 percent also applies to such payments, the net amount payable is in fact 3.5 percent.

Particulars	Singapore	Malaysia	Indonesia	Philippines	Bangladesh
(Foreign Investment) basic policy	Welcomes all types and sizes of industries for further economic growth and promoting Singapore as an international business centre.	Welcomes foreign investment, particularly in the manufacturing sector and priority industries, with technology transfer to Malaysia.	Welcomes foreign investment to increase the export of non-oil commodities and to save foreign exchange. Closed business areas may be opened for foreign investment if the production is intended for export(at least 85 percent).	Welcomes foreign investment for the development of the country. 100 percent foreign ownership is allowed if it is engaged in pioneer activity or located in an export-processing zone.	Foreign investment is welcomed in all areas of the economy except five industrial sectors reserved for public sector investment only. These are (i) arms, ammunition and other defence equipment, (ii) production of nuclear energy (iii) extraction from reserved forests (iv) security printing (currency notes) and minting (v) air transportation (excepting domestic airlines and international cargo transportation) and railway.

Particulars	Singapore	Malaysia	Indonesia	Philippines	Bangladesh
(Regulations for foreign investors) Limitations on foreign equity	No restriction on foreign participation in equity except banking, newspapers and companies owning residential properties.	100 percent foreign equity is allowed for export oriented projects or companies which employ 350 full time Malaysian workers (Effective until December 1990)	Initial foreign investment up to 80 percent (95 percent foreign investment allowed to export oriented units). Foreign shareholding shall be reduced to 49% within 15 years	Generally up to 40 percent. 100 percent foreign equity is allowed if the enterprise is engaged in pioneer activity or it exports at least 70 percent of total production.	No restrictions on the foreign investment equity ratio. 100% foreign ownership and joint venture with local partners of the private or public sector are freely allowed.
Remittance	No restrictions.	Allowed (but approval required for remittances over M$10,000).	Allowed	Approval required of Central Bank. Subject to emergency restrictions for exchange operations.	Under existing regulations remittances of profits, dividends sales proceeds including capital gains of portfolio investments of non-residents, technical fees and royalties etc are freely allowed subject to the agreements in conformity with BOI guide lines. In this regard, prior approval of the Bangladesh Bank is no longer required.
Acquisition of real estate	No restriction on the ownership of industrial or commercial land.	Ownership of land is allowed to foreigners.	Ownership of land is restricted to Indonesian nationals. The right of the expropriation is held by the Indonesian partner for the duration of JV for 30 years. Ownership of land is restricted to Philippine		Foreigners are allowed to use land and factory buildings on rental basis. They can also enjoy special privilege in Export Processing Zone with regard to the use of land, building and other facilities

Particulars	Singapore	Malaysia	Indonesia	Philippines	Bangladesh
Acquisition of real estate continued			nationals and to corporation whose foreign investment is 40% or less.		
Employment	Employment of foreign professionals, skilled workers is allowed.	Employment of foreign technical and skilled personnel is allowed.	Key expatriate positions for which qualified nationals are not yet available are permitted	Key positions are filled with foreigners under approval of BOI.	(a) Liberal employment of foreign technicians/ experts allowed. (b) Foreigners employed in the Zones enjoy equal rights similar to those of Bangladesh nationals (c) Law forbids formation of any labor union in the Zones. Strike within the zones are also prohibited.
Transfer of shares/ liquidation of company	No restriction. Liquidation (voluntary) permission of creditors is necessary.	No restriction until 1990 Liquidation to be done in accordance with Companies Act here.	The initial minimum share holding for Indonesian participants is 20 percent. Indonesian shareholders shall acquire majority shareholding within 15 years. For certain types of investment the initial shareholding of the Indonesian partner may be 5 percent, which has to be increased to 20 percent within 5 years and to 51 percent within 15	An enterprise of 100 percent foreign ownership must reduce its shareholding up to 40 percent within 30 years. Liquidation: no restriction	No restriction on the liquidation of the company. Minimum restriction on the transfer of shares.

Particulars	Singapore	Malaysia	Indonesia	Philippines	Bangladesh
Transfer of shares/ liquidation of company continued			years. Shareholders meeting decide liquidation of company, than the board of directors asks legalization from Department of Justice.		
Incentives	1. Tax holiday (1) Pioneer enterprise: 5-10 years. (2) Expanding enterprise maximum 5 years. (The size of the relief according to the increase of income) (3) Export enterprise: Non pioneer –5 years, Pioneer export 3 years after tax holiday. (4) Qualified manufacturers: Tax exemption of 90 percent of the excess of the export profit. (5) International trading company, warehousing company and consultancy company: 5 years on half of their qualifying income. II.	1. Tax holiday (1)Pioneer enterprise: 5-10 years. (2)Exemption from tax on imported capital goods. Exemption from customs duties on plants and machinery not manufactured locally. (3)Taxes on imported raw materials reduced to 2 percent for manufacturing industry. Deduction from taxable corporate income. (4) Deduction from taxable corporate income. (a) Qualifying capital expenditure and losses during tax relief period may be carried forward to the post-pioneer period. (b) Abatement of adjusted	1. Exemption from tax on imported capital goods. (1) Import duties on machinery, equipment and spare parts approved by Investment Coordinating Board. (2) 10 per cent value added tax on machinery and equipment can be deferred. (3) Import duties on raw materials for manufacturing industry are reduced to 2 per cent. 4. Exemption from import duties for producers of export commodities in bounded zones/export-processing zones. 5. The	1. Tax holiday. (1)Registered firms: pioncer-6 years, non-pioneer-4 years (extension is possible). (2)Exemption of 100 percent of the customs duties on import machinery, equipment and spare parts. (Under certain conditions set by Board of Investment.) (3)Zone-registered enterprises and enterprises located in industrial estates are exempted form taxes on imported raw materials. (4)Additional deduction from taxable income of 50	Prominent among the incentives and facilities provided to foreign investors are (1)Tax holiday for a period from 5 to 10 years depending on location of the project, and for 15 years for power generation. (2)80%-100% accelerated depreciation of actual cost of machinery and plant, in lieu of tax holiday. (3)Avoidance of double taxation on the basis of bilateral agreements. (4)Import duty at

Particulars	Singapore	Malaysia	Indonesia	Philippines	Bangladesh
Incentives continued	Reduction in income tax rate: (1) Qualified post-pioneer company. Not less than 10 percent for 5 years. (2) OHQ-10 percent (dividends from overseas are exempt).	income for export-oriented manufacturer – 5 percent value of indigenous Malaysian materials. (c) Double deduction for any expense incurred in promoting the export of Malaysian goods. (d) Investment tax allowance for capital expenditure incurred within five years (maximum 100 percent). (e) Reinvestment allowance for expanding manufacturers –25 percent of the expenditure (until December 1988).	interest rate for report credits is set at conventional rate of 9 percent a year.	percent of the wages corresponding to the increase in the number of workers (for registered enterprises) (5)The regional headquarters of multinational complainer: Exemption from income tax contractor's tax and local tax	the rate of 7.5% advalorem is payable on capital machinery and spares imported for initial installation or for BMR/BMRE of the existing industry. (5)No duty on imported capital machinery and raw materials by 100% export oriented industries. (6)Tax exemption on the interest on foreign loans and on capital gains from the transfer of shares (7)Tax exemption of royalties, technical know-how and technical assistance fees. (8)Exemption on income tax upto three years for foreign technicians employed under

Particulars	Singapore	Malaysia	Indonesia	Philippines	Bangladesh
Incentives continued					registered industries. (9)Easy availability of work permits to foreign nationals. (10)Six months multiple visa for the investors. (11)33% of IPO reserved for foreign investors. (12)Facilities for repatriation of invested capital, profit and dividend. (13)No discrimination on duties and taxes for similar industries in public and private sectors and also within private sector between local and foreign investments. (14)Term loan and working capital from local banks for foreign investors. (15)Bangladesh currency 'Taka'

Particulars	Singapore	Malaysia	Indonesia	Philippines	Bangladesh
Incentives continued					convertible for current account transactions and so forth. (16)Any person from a country recognized by Bangladesh may get permanent residentship by investing a minimum of US$ 75,000 or/and equivalent amount (nonrepatriable) and citizenship by investing a minimum of US$ 0.5 million or transferring US$ 1 million to any recognized financing institution. (17)Non-resident Bangladeshi investors will enjoy facilities similar to those of foreign investors. Moreover, they can buy newly issued shares/ debentures of Bangladeshi companies. A

Particulars	Singapore	Malaysia	Indonesia	Philippines	Bangladesh
Incentives continued					quota of 10% has been fixed for non-resident Bangladeshis in primary public shares. Furthermore, they can maintain foreign currency deposits in the Non-resident Foreign Currency Deposit (NFCD) Account.

Sources:

(i) Board of Investment, (January 1998), "Guide to Investment in Bangladesh".
(ii) The Dhaka Chamber of Commerce and Industry (August, 1997), " A Guide to Investment and Business in Bangladesh".
(iii) GOB, Ministry of Industries (Dhaka), (1999) Industrial policy.
(iv) The Confederation of Engineering Industry (1992), Foreign Direct investment & Technology Transfer in India.

CHAPTER-IX

SUMMARY AND CONCLUSION

A typical developing country like Bangladesh with low levels of consumption and huge unemployment has hardly any capacity to save and is caught up with what Ragner Nurkse calls **a vicious circle of poverty**. The low level of income is a reflection of low productivity, which, in turn, is due to lack of capital, resulting from an inability to save.

Applying certain exogenous forces this vicious circle can be broken down. One way is to import capital from outside, which may make the transition from economic stagnation to self- sustaining economic growth possible. The experience of the Western European countries during the post-war period is an illuminating example of how foreign assistance facilitated high rates of investment and saving caused by redistribution of income in favor of the business sector.

For its marked dependence on foreign money, Bangladesh provides a test case for conducting both theoretical as well as empirical investigation into the behavior of external assistance. External assistance seems to have stabilized roughly at a level of 7-8 percent of the gross domestic product of Bangladesh and finances over 60 percent of the entire public sector investment, including a substantial part of its local currency costs. Although conceptually foreign money is granted to finance development programs in developing countries, in Bangladesh the revenue budget can not escape the stigma of dependence. During 1975-1998, for example, 27 percent of the total revenue earnings was collected from customs duties alone.

Inflow of foreign capital generally comprises three forms: (i) official development assistance in the form of grants or loans, (ii) non-concessional credit in the form of food aid, commodity aid, and project assistance, and (iii) all types of private flows especially FDI. Available literature indicates that among the three forms of foreign capital, FDI stimulates significant favorable impact on economic growth of the

developing countries compared to two other forms of capital. It has a larger impact on domestic investment. It is also found that far from crowding domestic investment, FDI seems to supplement it.

Available information witnessed that Bangladesh started attracting FDI immediately after the change in state power and policy in 1975. The volume of FDI inflow is started to accelerate since the mid-1980s. Foreign investors have been attracted to the manufacturing sector by its low wages and, in particular, its unused quota for exporting textiles and apparel to the markets of the European Union and the United States. FDI into that industry accounted for nearly one fifth of approved investment inflows in 1998, excluding export-processing zones. As a result, RMGs account for over 76 percent of the country's export earning.

Despite growing importance of FDI inflows to Bangladesh, it is ironically one of the least researched areas in the economic literature on the economy of Bangladesh. Although, a few scholars have dealt with the issue of FDI ***en passant*** in various research papers and mimeographs, but these are more concerned with a general analysis of the role of FDI and Transnational Corporations in the economy of Bangladesh. Studies, which have given undivided and exhaustive attention to the topic of FDI, have relatively been few. The main objective of this study is to fill this gap by generating and evaluating extensive data in an integrated form relating to FDI in Bangladesh.

This study has concentrated on investigating the nature and characteristics of FDI in Bangladesh. The specific objectives of the study are: to assess the trend of FDI in Bangladesh; to evaluate the performance of FDI in Bangladesh and, to assess the determinants of FDI. The study mostly utilizes published data from different sources. Analysis was carried out by applying various statistical tools and covers time period from 1977 to 1998.

The study is consisted of nine chapters. Following from the introductory chapter, chapter two gives a brief description of Bangladesh economy. Chapter three provides theoretical and empirical foundation of the study. Chapter four analyses the FDI

polices in Bangladesh. Chapter five assesses the trend, structure and performance of FDI in Bangladesh over a period of 22 years spanning from 1977 to 1999.Chapter six assesses the performance of Export Processing Zones in attracting FDI in Bangladesh. Determinants of FDI on the economy of Bangladesh have been investigated in chapter seven. Chapter eight compares and contrasts FDI policy of Bangladesh in comparison with some selected Asian countries. Chapter nine concludes the study.

Since economic and political factors largely explain the growth of FDI, a brief description of the economy of Bangladesh is outlined in chapter two. Bangladesh started its journey towards development immediately after independence (1972) when the country's first Annual Development Plan was formulated with the objectives of relief and reconstruction. A Second Annual Plan was drafted in 1973 which, continued the tasks of recovery efforts but set the self - sufficiency in food as the principal development target.

In late 1973, country's First Five-Year Plan (FFYP) for 1973-78 was announced. The plan which incorporated twelve objectives emphasized the broad goals of national self-reliance, increased production, employment creation, income distribution, food self - sufficiency and an industrial policy of import substitution and export promotion. The first plan was based on an input-output model formulated by Planning Commission economists

The FFYP was followed by a Two-Year Development Plan (1978-80) which mostly carried out the incomplete tasks of FFYP, and also filling the shortfall of resource availability during the implementation of the previous plan. The Second Five-Year Plan (SFYP, 1980-85) took a more realistic approach and deviated from the previous rhetoric of socialism and emphasized the growth of income and employed in the poverty alleviation programs.

During the preparation of Third Year Plan (TFYP 1985-90), fresh attempts were made to integrate the productive sectors of the economy with its infrastructure development as well as the rural development programs. This was done with the help of an applied general equilibrium model so that resource allocation could be based on better balance and greater efficiency.

The Plan emphasized less government control, denationalization and also advocated for greater role of market forces. This is ultimately came to be known as SAR which was expected to open the economy to more internal and external competition. The Fourth Five-Year Plan (1990-95) and the Fifth Five-Year Plan (1995-2000) were formulated in the line of the so-called SAP.

Bangladesh, with nearly half of its population still groaning under the poverty line, is said to be at cross roads in search of economic and social development. For the last 30 years, GDP growth rates averaged below 5 percent per annum as opposed to a required rate, without any pause for a long while, of 7 - 8 percent for making any dent to the poverty scenario. On the assumption that the current capital-output ratio is 3: 1, this much of growth rate would demand an investment level of 21 - 24 percent per annum as compared to the present level of investment of around 13 percent only. Given the macro-economic balance that the economy witnessed in the early 1990s, according to available findings, the investment / GDP ratio could be raised to 18 - 20 percent within a five year period without having any pressures on the economy's resource balance.

The theoretical and empirical determinants of FDI have been revised in chapter three. Summary findings are succinctly described below:

Several avenues of the theoretical development are classified as: the compensating advantage theory of Hymer and Kindleberger, the currency area; phenomenon of Aliber; the product life cycle model of Vernon; the internalization theory of Buckley and Casson ; and the eclectic theory of Dunning . The strands of the theory, however, go back to much further, to Coase, Kaldor and Robinson.

Among the various theories of FDI, the eclectic theory of Dunning has yielded a large number of insights into the development of FDI. The model rests on four basic assumptions. (i) products undergo predictable changes in production and marketing, (ii) restricted information is available on technology, (iii) production processes

change over time and economies of scale are prevalent, and (iv) tastes differ according to income and ,thus, products can be standardized at various income levels .

The theory consists of four stages. The first stage of the theory begins when an "innovation" is introduced. It is argued that new products would appear first in the most advanced country (the USA). Reasons are many, of which two are prominent. First, rich countries have the financial, organizational and intellectual resources to undertake the requisite research (the 'supply' exists). Second, these countries have large number of consumers with high incomes and "adventurous tastes" to test new products on, and the greatest pressures of competition, high wage costs or scarce materials to spur innovation (the "demand" for innovations is high).

The second stage of the theory begins when the product is successful in the rich markets. It is argued that if the product is successful in the rich markets, the production of new product will be expanded, new markets will be cultivated and export development will be started. In this stage the innovators still have the technological lead, but competitors are attracted by its success to work on imitations or to develop similar products.

The third stage starts when sufficient competition has developed, and the technology has become standardized enough, for cost and local-marketing considerations to become important. At this stage, the innovating firm seeks to maintain its profits by making more intense marketing efforts and by investing abroad in cheaper locations and nearer the foreign market.

The fourth and final stage of the theory begins when the production shifts in location down the income scale. At this stage, in the life of the product, cost considerations are of great significance and, therefore, production facilities are moved to least developing countries (LDCs) to take advantage of lower labor costs.

The insights provided by several recent explanations of FDI clearly demonstrate that the theoretical arguments are highly controversial, complicated and inconclusive in

nature. It is, therefore, essential that the grafting of new concepts should occur in explaining the FDI on a solid core.

The study has also examined the determinants of FDI inflows in six countries: Hong Kong, Indonesia, Malaysia, Singapore, Thailand, and India. Because of tremendous success in attracting FDI inflows, these countries are selected.

Hong Kong

A survey of the determinants of FDI in Hong Kong found that firms from developed countries were attracted to Hong Kong by its labor cost and availability, infrastructure, and geographic location; for some, availability of skilled and technical personnel at competitive wage levels was more important than general labor availability. Access to the Hong Kong domestic market and raw materials were not major factors. For firms from developing countries, Hong Kong's geographic location in relation to China and the rest of Asia was the most important pull factor; for some multinational firms, ethnic ties was also an important motivation, while some also considered Hong Kong's relatively superior technology an inducement to invest.

Singapore

Surveys have found that like in other countries more than one-half of all Japanese firms that have invested in Singapore, aim their products at the domestic market and nearly a third invest to export to a third country. The most recent data indicate, however, that investment for sales to the local market is becoming more important. Singapore is a small, but growing market for Japanese subsidiaries. One study of the determinants of FDI in Singapore found that the elasticity of the cost of labor and capital was negative and significant. The study also found that the interaction between domestic and foreign investment was statistically positive indicating that domestic capital complements FDI. Various international business surveys have consistently ranked Singapore as one of the most attractive investment locations in the world. The major factors that contribute to Singapore's attractive investment climate include its geographical location and physical infrastructure, its skilled manpower, and its institutional infrastructure and environment.

Indonesia

A UN survey in 1995 shows that the most important motive of foreign investors in Indonesia was to secure local markets. Low wages were not a factor in the 1970s but have become more important in the 1980s and 1990s. Thus, reducing labor costs became increasingly important while government incentives became less important over time. Using a flexible accelerator approach in Indonesia, the UN study also found that wage and real interest rates were significant determinants of FDI inflows in a few industries such as textiles and garments.

Malaysia

Studies of determinants of FDI in Malaysia stressed demand-side variables such as the role of Malaysian policy. And for the supply side emphasized the effects of changing comparative advantage in major investors and exchange rate realignments in recent years. Malaysia's relatively good infrastructure and low labor costs, which generated a comparative advantage in labor-intensive manufactures, were pointed to as locational advantages.

The UN study (1995), using the flexible accelerator approach, found some interesting results on the determinants of FDI in Malaysia. First, the net sales variable is the most consistently significant determinant of both equity and fixed investment. However, this variable was not a significant determinant in agriculture and construction, and for equity investment in mining. Second, lagged capital stock portion of the flexible accelerator was a significant determinant of equity and fixed investment in manufacturing and construction, while it was a significant determinant of equity investment only in mining, and fixed investment only in banking and finance. Third, the real interest rate variable was not significant. Fourth, the wage variable's coefficient is negative and weakly significant in the fixed investment equation for manufacturing sector.

Thailand

Surveys examining motives for FDI found that FDI across industries was attracted to Thailand primarily because of the availability of cheap, productive labor and raw materials, Thai government incentives, and adequate local demand. Less important

but nevertheless considerable were contributions of equity and management know-how. One survey found that exporting firms, which also happened to be the larger firms studied, expressed exclusive concern with labor inputs, production for external markets, exchange rates, and tax incentives, with some secondary concerns about other financial variables observed.

India

Surveys found that the large Indian market largely motivated the FDI inflows in India. Policies governing investment and business regulations have had the largest impact on FDI inflows. GDP growth rates have fluctuated over the period generally between the 4 to 5 percent ranges with a few outlying years. India has maintained a relatively stable macroeconomics environment with inflation rates confined to single digits since 1981. Exchange rates have been relatively stable with 20 percent depreciation in 1984, and several successive devaluation in the late 1980s.

The literature suggests that the distribution of FDI be linked with the economic environment of the host country. The development strategies and macro-organizational policies of the host-country government influence this economic environment, in turn. Host country policies and policy pronouncements affect the perception of "political risk" by transnational corporations and thereby the amount of investment of these companies. In addition, host country policies can be instrumental in channeling investment flows toward sectors considered to be of particular importance to the country's development. Industrial and trade policy regulations of a country are frequently considered in the literature as a proxy for the distribution of FDI. In chapter four, a brief overview of the Bangladesh State policy towards FDI is ,thus, examined

The state policy of Bangladesh towards FDI has been elaborated in the industrial policies announced and revised from time to time. There has been several such policy packages announced since 1973. The first Industrial Investment Policy (IIP) announced in1973, allowed foreign collaboration in public enterprises only with minority equity participation of 49 percent. The policy had given a dominant role to

the public sector in industrial ownership and entrepreneurship, allowing only a minor role to the private sector.

The response of foreign investors to this policy was not encouraging, as could be expected. The sudden shift toward nationalization of private sector industrial units shattered private investors' confidence. A New Investment Policy (NIP) in 1974 permitted foreign investors to collaborate with both government and local private entrepreneurs, except in some basic industries. The policy was revised in 1975 and the Revised Investment Policy (RIP) allowed foreign investors to collaborate with private sector subject still however to various restrictions.

After the dismal performance of the industrial sector following the 1972 nationalization, a change occurred in 1977 in the government's approach toward the role of the public and private sectors. The role of the public sector was restricted to consolidating existing enterprises, and further investment in this sector was strictly restricted. A New Industrial investment policy (NIIP) in 1978 was formulated. The new policy statement reiterated that the government would continue to pursue a pattern of a mixed economy, with the private and public sector reinforcing each other.

Bangladesh began to implement a more liberal foreign investment policy as part of its overall economic reform program toward the end of the 1980s. Accordingly, a new industrial policy package was introduced in 1986 based on the recognition of the primacy of the private sector. A number of policy and regulatory measures were taken to improve the business environment in general and attract FDI in particular. The Board of Investment (BOI), was set up to help generate opportunities for FDI and provide investment services. A "one-window facility" was established to overcome difficulties in setting up new industries.

The 1991 Industrial Policy (IP), which allowed up to 100 percent foreign private investment along with joint venture, brought the FDI policies to its most liberal phase, with a 1992 amendment incorporating additional facilities and incentives.

In the latest industrial policy the government of Bangladesh took several positive steps for attracting FDI, including further reducing the reserve list and liberalizing incentives. FDI was allowed in all sectors of the economy with the exception of the five sectors of arms, ammunition and other defense equipment and machinery; production of nuclear energy; forest plantation and mechanized extraction within the bounds of reserved forests; security printing (currency notes) and minting; and air and railway transportation. The latest Industrial Policy (AIP 1992) is annexed.

Chapter five examines the trend and performance of FDI in Bangladesh during the period 1977-1999. Various dimensions of FDI, such as inflow of capital, structure of FDI, industrial and geographical distribution of FDI, country-wise analysis of FDI inflow, profit and remittance of MNCs etc. in Bangladesh have been evaluated in this chapter. Overall analysis does suggest an insignificant contribution of FDI the economy of Bangladesh despite alluring package of benefits offered to the foreign investors by the government of Bangladesh. The trend and performance of FDI in Bangladesh are briefly summarized below:

Significant periodical as well as annual variations have also marked the inflow of FDI. The peak inflow was registered in 1997-98, after major policy reforms were introduced in the economy in the early nineties. One notable feature is that overall quantum of FDI flowing into Bangladesh coincides with changes in the governments and policies. With changes in state power in 1981, 1990, and 1995 a discernable pattern in the bulk of FDI inflows can be traced.

With change in state power in August 1975, the environment became significantly conducive to inflows of foreign investment. The successive governments made efforts towards attracting liberal measures aimed at ensuring increasingly greater flow of foreign investment. This resulted in a rise-although marked by significant annual variations in foreign capital inflow in Bangladesh. Expect for the year 1981/82, the increasing trend in the FDI flow continued unabated. The rate of increase has been particularly pronounced since 1982. This may be attributed as a result of favorable change in the policy environment encouraging both domestic and foreign investment.

Evaluating the foreign investment climate, the joint Euromoney Publication of UK and the Bangladesh Board of Investment conference in January 1995 at Dhaka has referred to the Bangladesh economy as the emerging tiger.

The impact which foreign investment can make on the economic development of the host country depends upon its volume and its share in gross national product, as well as upon the sectors and conditions of its investment. Both as a ratio of total investment and of imports, the contribution of FDI are extremely negligible in Bangladesh. The share of FDI to total investment and imports have been minimal-less than 0.3 percent of the country's total investment (between 1977 and 1999), despite alluring package of benefits offered by the government of Bangladesh to attract FDI.

Bangladesh remains far below in attracting FDI in the global context. The FDI flowing into Bangladesh has been the lowest at all times among the selected Asian countries. Although some positive improvements have been observed in the recent past, FDI is seen to have played a very minor role in Bangladesh both as a ratio of total resource inflows and of gross domestic capital formation up till now. This reflects that Bangladesh lags far behind in restructuring growth and orienting its policies to encourage FDI.

By analyzing the structural elements of FDI in Bangladesh three conclusions can be drawn. Firstly, re-invested earnings became the dominant forms of FDI in Bangladesh during the entire period under consideration. Secondly, the item labeled capital equipment brought in has never constituted a significant element in the structure of FDI except for three or four years, suggesting limited technology transfer by MNCs in Bangladesh. Thirdly, the share of major element of FDI, which includes cash capital inflow, has never risen above 40 percent of the total investment except in 1977, 1986, and 1994.

Sectoral composition of FDI flows into Bangladesh also exhibits considerable year-to-year fluctuation. The sectoral share of manufacturing industries has witnessed sharp decline from 45 percent in 1977 to 25 percent in 1982, revived in 1983, may be as the

aftermath of the introduction of the New Industrial Policy when it reached an all time high share of 82 percent, and significantly declined since then.

The share of commerce, on the contrary, is seen to have increased continuously between 1977 and 1990, tapered off temporarily in 1983 and started increasing again since 1984, rising to over 92 percent in 1989 and 1990.This increasing trend is ,however, continued to decline almost steadily from 55 percent in 1991 to 18 percent in 1999. The increase in the sectoral share of commerce seems to have taken place at the cost of the decrease in the shares of manufacturing and miscellaneous industries sectors. The turning point of this structural change is marked by the year 1990 when the share of manufacturing industries fell to its lowest of 2 percent and that of commerce reached its highest level of 92 percent.

In the remaining economic sectors - agriculture, transport and communications, and construction - flow of FDI has been insignificant and erratic because of the limited opportunities open for foreign exploitation in these areas. Another important feature of the structure is that in recent years the two sectors - mining and quarrying - have been attracting significant amount of FDI. According to the Bangladesh Economic Review (1999) these two sectors have attracted more than 40 percent of total flows of FDI in Bangladesh.

Compared to the earlier trend, the foreign investors now seen to be interested in making investment in a number of export-oriented products. The most significant stride with regard to export-oriented products, has been the RMGs industry, whose share in export earning was 12.4 percent in 1984 but now (1999) accounts for more than 76 percent. This change of sectoral emphasis of FDI may in part be explained by the overall shift of the development policy of Bangladesh towards a more export - oriented growth strategy designed to attract foreign capital into sectors with export prospects.

Country wise distribution of FDI also reveals that investment from India, China and South Korea dominated the scene in 1987-88, 1990 and onwards. The other two notable features are: (i) in aggregate terms, the amount of foreign investment from the

developed market economics exceeded that from the Asian countries up to the end of the eighties. The situation has turned dramatically by 1994, when the middle-income countries' share in FDI flows to Bangladesh become more than two - third of the total investment; and (ii) the post - liberation FDI is that it has been mostly of the joint - venture type.

Through long 25 years partnership with Pakistan during 1947-71, Bangladesh (the then east Pakistan) was able to attract only 27 MNCs, of which 21 companies were from Europe and 14 of them, were from United Kingdom alone. There were only 4 companies from America. Only two countries, namely Japan and Malaysia were involved in joint-venture project in Bangladesh from Asian countries. This pattern, however, has substantially changed after independence, with Asian countries emerging as equally important as the developed market economies in terms of the volume of investment.

When FDI is evaluated in terms of non-equity agreement in Bangladesh, data show that expect for United Kingdom- the country with which Bangladesh has had economic relationships from colonial time, a relatively large number of agreements have been made with enterprises originating from developing countries. A recent study found that out of 80 non-equity agreements made so far with 10 countries, the number of such agreements with firms originating from India is 19 (24%), followed by South Korea (8%) and China (4%). At the policy level, this warrants more intensified efforts to explore possibilities of greater non-equity collaboration with firms from those countries who may be agreeable to better terms and conditions, including the ones in the spares of technology transfer, than the established MNCs from the developed countries. More diversified geographical source may help improve the bargaining position of a country like Bangladesh vis-a-vis the MNCs from the industrialized countries.

Administratively, Bangladesh is divided into six Divisions, namely Dhaka, Chittagong, Khulna, Rajshahi, Barisal and Sylhet. Data on regional distribution pattern of FDI flow into Bangladesh is scanty as well as of doubtful validity. On the basis of addresses of the foreign firms sanctioned by the Board of Investment, it was

found that, in terms of amount of investment and number of firms, the overall location pattern (of FDI) is highly concentrated in the major urban centers of the country in Dhaka Division. Data show that among the six divisions of Bangladesh, Dhaka division attracted the highest number of foreign investors (78%) during 1977-99 followed by Chittagong and Khulna division.

Remittance of profits and dividends taken by foreign companies from host country is one of the important factors that usually induce (private foreign investment) the aspirant investors. In Bangladesh, detailed figures are not available on profits and dividends and other fees remitted out of Bangladesh by foreign firms. Bangladesh Bank - the central bank of the country, which is supposed to maintain a systematic record keeping in this regard, has been found to be extremely unscientific.

One study records that in the period between 1977 and 1989, Taka 5491 million was remitted abroad as profits, dividends, royalties and other fees by foreign investors operating in Bangladesh. Of the total amount remitted, the highest proportion of the outflow took place in 1984-85 (Tk. 6 million) and the lowest in 1981-82 (Tk. 54.3 million). In other years the figure varied from Tk. 72.1 million to Tk. 1247.4 million. Analyzing the annual breakdown of the outflow of profits and dividends earned by the foreign companies, it would appear that the rate of remittance went up after the government announced the new industrial policy in 1982. This policy offered the maximum incentives to foreign investors by relaxing the provision for repatriation of profits.

Another important aspect of the remittance figures is that the list of the beneficiaries is overwhelming dominated by a single country, the United Kingdom. It was found in a study that foreign companies of UK origin took away 77% of the total amount (remitted abroad) during the period 1976-77 to 1983-84, followed by the USA (15.6%) and Switzerland. This pattern would appear to reflect the high volume of remittances made by British - owned tea companies and by Bangladesh Tobacco, which is one of the most profitable of the transnational corporations operating in Bangladesh.

One study notes:

..... FDI in Bangladesh has been a drain on national resources. As between 1977 and 1986, at a time when the Government of Bangladesh was laying down the red carpet for foreign investors, Bangladesh, one of the poorest countries in the world, was exporting capital abroad to the extent of Taka 5491 million on account of private foreign investment in the country. It follows that unless there is quantum escalation in new inflows of FDI the further liberalization of provisions for remittances of profits by foreign investors will in the years ahead the net drainage of resources out of Bangladesh.

In these circumstances, realism would appear to demand to just a scaling-down of the extravagant expectations entertained by policy - makers about the role of private foreign investment but a serious review of the prevailing policy package which has made Bangladesh into an exporter of capital.

In recent years, the major source of FDI in Bangladesh is the two export processing zones, the CEPZ and the DEPZ, which were established in 1983 and 1993 respectively under the Bangladesh Export Processing Zones Authority Act, 1980. The economic impact of two EPZs in terms of investment drawing, employment generation and export earning is evaluated.

Bangladesh conceived the idea of establishing export-processing zones (EPZs) as an adjunct to the adoption of open economic policy in the late 1970s. The aim behind the idea of setting up of EPZs was to offer favorable conditions to attract foreign and local private investment. To translate the idea into a reality Bangladesh enacted "The Bangladesh Export Processing Zones Authority Act, 1980". The first EPZ of the country, CEPZ started its functioning in 1983. Subsequently, the DEPZ was set-up, which came into operation in 1992. The Bangladesh Export Processing Zones Authority or BEPZA has been empowered to supervise the overall affairs of EPZs in Bangladesh.

Availability of the inexpensive and productive labor force in Bangladesh has aided to dub the EPZs in Bangladesh as the "optimum profit making bases" in the world. Also it is perceived that of over 800 zones in more than 100 countries listed in the WEPZA

International Directory of Export Processing Zones and Free Trade Zones, the EPZs in Bangladesh will offer a very competitive environment for foreign investment among the developing countries.

In Bangladesh, EPZs, have emerged as the main centers of attraction for FDI inflows. Most of the investments in the two EPZs have come from East and South East Asian countries viz., South Korea, Japan, Hong Kong, Malaysia and Singapore. Textile and apparels and related products have absorbed the maximum amount of investment in the EPZs, and are proving to be the more employment generating and export earning products because of their labor-intensive production nature. Female workers are getting more importance in terms of employment in the EPZs, and the number of female workers is more than that of the male workers in CEPZ. On an average a $ 1 million investment in EPZ supports 225 jobs for the Bangladeshis. Garments, knitting and other garment related products are the most labor-intensive products produced in the EPZs. The share of export earnings of EPZs in the total national export is increasing and now hovering around 11 percent. In terms of value added contribution of the EPZs, the present level seems to be very insignificant in general, and for DEPZ it was negative in 1997-98 in particular.

Most developing countries including Bangladesh today consider FDI an important resource for development. But the economic effects of FDI are almost impossible to measure with precision, because TNCs represent a complex package of attributes that vary from one host country to another. The conclusions of the past econometric studies of FDI and economic growth are unclear. The World Investment Report'1999 has, however, taken a different approach to measuring the impact of FDI. The new approach is known as 'Qualitative Approach'.

Under this new approach, different components of FDI, such as ownership advantage, market access, employment, skillful management techniques, environmental impact of FDI etc. have been measured separately. In this study, an analysis was made to assess both the qualitative and quantitative effects of FDI in Bangladesh. The results are described in chapter seven. The study also seeks to explain the major contributing factors of FDI in Bangladesh. Two econometric models have been tested for this

purpose. The first model is a proto-type model used by the United Nations to analyze the determinants of FDI flows to the major regions of the world economy.

The second model was formulated by incorporating variables that were found significant in the past econometric studies. Multiple regression equations were fitted for these two models to accept or reject the proposed hypotheses. Regression results in both the models suggest that market size as depicted by GDP growth, GDP per capita and export orientation are three major factors that influence the FDI flows into Bangladesh. The coefficient of GDP growth rate is significant at the 5 per cent level. The GDP per capita and export variable are significant at the 10 per cent level. Of course, this does not mean that other variables may not have important role in determining FDI inflows in Bangladesh. Their potential effects might have been obscured by other variables. Further research may be carried out in this direction to test their validity empirically.

Finally, a comparative assessment of the policy and incentive systems of some selected Asian countries that have attracted maximum amount of FDI in the last two decades has been made in chapter eight. Results show that:

FDI policy and incentives system of any country is not constant but changeable as and when required. As new phenomena in an economy appear, FDI policy and incentives system calls for reforms and modifications to cope with the pace of economic development. FDI policy and incentives system adopted by every country is different and distinct. What policy system to be adopted by a country largely depends on the level of economic development, levels of technology, labor conditions, political conditions, and so on. The same mode of incentives does not evenly and efficiently works in all the countries. One incentive effective in one country may be deemed highly ineffective in other countries.

Recent years witness that liberal and promotional FDI policy and incentives system positively contributes to the overall development of the economy. However, most countries are viewed to adopt liberal policy and continue to liberalize their FDI policy and incentives system. No FDI policy is absolutely free from all sorts of restrictions,

rather a tendency of FDI policy of being liberal or restrictive is observed. Every country welcomes FDI through liberal policy but it is scared about economic and political sovereignty. Most of the incentives systems are designed to flourish some priority sectors in an economy. The government of a country usually determines the priority sectors.

APPENDIX-I

[All Tables]

Table-1: Flow of FDI in Bangladesh

Year	Total Sanctioned Units	No. of Units in Production	Amount of Investment in the Sanctioned Units (Tk. Million)
77-78	2	1	31
78-79	3	3	45
79-80	2	2	74
80-81	12	11	69
81-82	NA	NA	103
82-83	9	8	103
83-84	18	14	73
84-85	6	4	82
85-86	5	1	250
86-87	16	4	188
87-88	17	3	333
88-89	19	NA	283
89-90	NA	NA	381
90-91	11	6	34
91-92	24	18	559
92-93	41	NA	698
93-94	83	23	400
94-95	NA	NA	315
95-96	NA	NA	283
96-97	NA	NA	636
97-98	NA	NA	1017
98-99	NA	NA	604

Source: *Statistics Department*, Bangladesh Bank.

Table-2: Share of FDI in total investment in Bangladesh. (Tk. million in current price)

Year	Total Investment	Imports	FDI	FDI as % of Total Investment.	FDI as % of Imports
1977-78	14618	18270	31	0.212	0.170
1978-79	16543	23340	45	0.272	0.193
1979-80	22290	36760	74	0.332	0.201
1980-81	37232	52160	69	0.185	0.132
1981-82	39837	52360	105	0.264	0.201
1982-83	39212	54890	103	0.263	0.188
1983-84	43081	58690	73	0.169	0.124
1984-85	52012	68740	82	0.158	0.119
1985-86	56220	70650	250	0.445	0.354
1986-87	64900	80260	188	0.290	0.234
1987-88	69440	93290	333	0.480	0.357
1988-89	69560	108480	283	0.407	0.261
1989-90	91830	123750	381	0.415	0.308
1990-91	91820	123780	360	0.392	0.291
1991-92	109590	132110	559	0.510	0.423
1992-93	128370	156010	698	0.544	0.447
1993-94	126173	170000	400	0.317	0.235
1994-95	194651	202170	315	0.162	0.156
1995-96	221200	216000	145	0.066	0.067
1996-97	242420	218200	636	0.262	0.291
1997-98	275860	221390	1017	0.369	0.459
1998-99	310982	221500	584	0.188	0.264
1999-00	-	-	642	-	-

Source: *Statistics Department*, Bangladesh Bank.

Table- 3: Top 12 Developing-country recipients of FDI (by value in US $)

Rank	1970-79	1980-89	1989-99
1	Brazil	Mexico	China
2	Mexico	Brazil	Mexico
3	Nigeria	China	Malaysia
4	Malaysia	Malaysia	Brazil
5	Indonesia	Egypt	Indonesia
6	Greece	Argentina	Thailand
7	South Africa	Greece	Argentina
8	Iran	Thailand	Hungary
9	Egypt	Colombia	Poland
10	Equador	Nigeria	Colombia
11	Thailand	Indonesia	India
12	Algeria	Chile	Czech Republic

Source: Calculated from the World Investment Reports.

Table- 4: Comparative levels of FDI in South Asia (million $US)

Country	1981	1991	1992	1993	1994	1995	1996	1997	1998	1999*
Bangladesh	o.6	1.0	4.0	14.0	11.0	2.0	15.0	11.0	16.0	21.0
India	235	74	277	550	974	2144	2587	2073	2117	2679
Pakistan	40	257	335	346	419	719	690	239	244	263
Srilanka	30	48	123	195	166	56	119	78	128	148
Nepal	-	2.0	5.0	9.0	13.0	8.0	19.0	17.0	23.0	21

Sources:1. Upto 1997, World Bank (1990)
2.Since 1998, UNCTAD(1999) World Investment Report; 1999.
*Estimated

Table- 5: Structural composition of FDI. (million Tk. in current price)

Year	Total FDI	Cash brought in	Capital equipment	Re-invested earnings	Percentage Share		
		1	2	3	1	2	3
77	31	16	1	14	52	3	45
78	45	11	1	33	25	2	73
79	74	31	11	32	42	15	43
80	69	14	-	55	20	-	80
81	105	28	5	72	27	5	68
82	103	15	1	87	15	1	84
83	73	10	26	37	14	35	51
84	82	8	23	51	10	28	62
85	250	108	4	138	43	2	55
86	188	107	-	81	57	-	43
87	333	26	1	306	8	-	92
88	283	42	-	241	15	-	85
89	381	3	8	370	1	2	97
90	360	27	5	328	8	1	91
91	559	185	50	324	33	9	58
92	698	126	164	408	18	24	58
93	400	97	68	235	24	17	59
94	315	166	51	98	53	16	31
95	145	21	32	92	15	22	63
96	636	213	188	235	33	30	37
97	1017	262	313	442	26	31	43
98	584	143	282	159	25	48	27
99	642	68	166	408	11	26	63
Total	**7373**	**1727**	**1400**	**4246**	**23**	**19**	**58**

Source: *Statistics Department*, Bangladesh Bank.

Table- 6: Cash brought in by countries (in percent)

Year	Country							Total
	USA	UK	Japan	Canada	W. Ger	France	Other	
1977	-	34	19	20	4	23	-	16
1978	4	15	29	-	-	51	-	11
1979	56	-	17	-	39	24	-35	31
1980	14	20	29	-	10	27	-	14
1981	9	27	17	-	6	26	14	28
1982	33	11	45	-	11	-	-	15
1983	-	33	2	64	1	-	-	10
1984	135	-19	-17	-	1	-	-	8
1985	-4	-8	8	97	2	-	5	98
1986	1	2	8	88	-	-	2	108
1987	-9	3	17	88	-	-	-	107
1988	-34	14	65	-	-	49	6	26
1989	-	8	48	-	-	43	-	42
1990	26	26	66	-	-	-	-17	3
1991	-	34	19	65	-	-16	-2	185
1992	-	2	26	53	-	-	19	126
1993	-	-2	30	63	-	-	9	97
1994	-	-8	18	82	-	-	8	166
1995	15	20	7	-	-	-	58	21
1996	25	29	4	2	-	-	40	213
1997	37	31	4	2	-	-	27	262
1998	13	21	4	-	-	-	61	143
1999								68

Source: *Statistics Department*, Bangladesh Bank.

Table -7: Capital equipment brought in by countries (in percent)

Year	Country						Total (million Tk.)
	UK	USA	Canada	Japan	Singapore	Korea	
1977	100	-	-	-	-	-	1
1978	100	-	-	-	-	-	1
1979	-	20	-	-	-	80	11
1980	-	-	-	-	-	-	-
1981	14	40	-	-	-	46	5
1982	-	100	-	-	-	-	1
1983	2	30	30	-	3	4	26
1984	113	-	-	-	-	-13	23
1985	100	-	-	-	-	-	4
1986	-	-	-	100	-	-	1
1987	-	-	-	100	-	-	1
1988	100	-	-	-	-	-	1
1989	100	-	-	-	-	-	8
1990	100	-	-	-	-	-	5
1991	67	-	-	-	-	33	50
1992	98	-	-	-	1	-	164
1993	50	-	-	-	50	-	68
1994	57	17	-	-	20	6	51
1995	25	10	-	12	10	43	32
1996	39	44	1	2.7	5	7	188
1997	40	44	1	1.8	6	6	313
1998	37	59	-	-	2	2	282
1999	46	31		18	3	1	166

Source: *Statistics Department*, Bangladesh Bank.

Table -8: Re-invested earnings invested by countries (in percent)

Year	Country									Total (million Tk.)
	USA	UK	Japan	Pakistan	W. Germany	France	India	Canada	Other	
1977	34	41	0.3	-	-	-	2	23	-	14
1978	25	53	-	-	0.02	-	-	-	22	33
1979	30	30	-	-	-	-	6	-	34	32
1980	42	8	-	-	-	-	9	-	40	55
1981	39	26	-	-	1	1	5	-	28	72
1982	37	28	-	-	-	6	1	-	28	87
1983	-22	156	21	12	-4	-68	-	-	5.6	37
1984	4	34	-	12	-	40	9	-	-	51
1985	44	6	7	5	-	31	6	-	-	138
1986	76	4	-	12	1	-	8	-	-	81
1987	59	13	-	1	2	5	4	-	16	306
1988	85	4	-	4	1	-1	7	-	-	241
1989	74	-	-	5	-	-	6	-	14	370
1990	94	2	-	-	-	-	3	-	1	328
1991	29	50	-	8	-	-	4	8	-	324
1992	11	64	-	6	-	-	6	12	-	408
1993	45	32	-	-	-	-	-	24	-	235
1994	19	30	-	-	-	-	-	-	51	98
1995	13	61	15	-	-	-	-	-	11	92
1996	26	26	5	-	-	-	-	4	39	235
1997	28	25	5	-	-	-	-	4	38	442
1998	50	32	-	-	-	-	-	-	18	159
1999	56	32	8	-	-	-	-	-	4	408

Source: *Statistics Department*, Bangladesh Bank.

Table-9: Total flow of foreign investment in Bangladesh by economic classification (in percent)

Year	Sector							Total (Million Tk.)
	Agriculture	Mining & Quarrying	Manufacturing	Construction	Commerce	Transport storage & Communi-cation	Misc. Services	
1977	-	-	45	1	20	-	34	31
1978	2	-	19	1	36	-	42	45
1979	-	-	42	-	41	-	17	74
1980	-	-	20	-	69	-	11	69
1981	1	-	27	-	65	-	7	105
1982	-	-	25	-	69	-	6	103
1983	1	-	82	-	15	-	2	73
1984	-	-	50	-	48	-	2	82
1985	12	-	40	-	46	-	2	250
1986	-	-	52	-	42	1	5	187
1987	-	-	38	-	55	1	6	333
1988	1	-	1	-	89	1	8	283
1989	2	-	-	-	92	-	6	381
1990	1	-	2	-	92	1	4	360
1991	11	-	29	-	55	-	5	559
1992	7	-	41	-	48	-	5	698
1993	2	-	43	-	47	-	8	400
1994	4	-	31	-	61	-	4	315
1995	9	-	10	-	54	-	27	145
1996	2	34	22	-	37	-	5	636
1997	3	53	18	-	23	-	3	1017
1998	4	57	19	-	18	-	2	584
1999								642

Source: *Statistics Department, Bangladesh Bank*

Table-10: Distribution of FDI in Bangladesh by broad economic sector (percentage share)

Year	Sectors						Total
	Agricul-ture	Manufac-turing	Comme rce	Trans-port	Constr-uction	Miscella-neous	
1977-1982	1.28	37.63	48.16	0.45	0.38	12.10	100
1983-1988	1.44	41.05	42.66	1.19	-	13.66	100
1989-1994	0.22	16.56	73.36	1.08	-	8.78	100
1995	0.18	12.90	79.28	0.10	0.40	7.14	100
1996	0.21	14.18	78.10	0.23	0.11	7.17	100
1997	0.26	5.33	83.46	0.16	-	10.79	100
1998	0.14	14.17	77.05	-	0.50	8.14	100
1999	0.11	11.24	77.44	1.38	0.40	9.43	100
1997-1999	0.48	17.93	72.22	0.20	0.08	9.09	100

Source: *Statistics Department*, Bangladesh Bank

Table -11: Industrial classification of FDI in Bangladesh (in percent)

Year / Sector	1977-1982	1983-1988	1989-1994	1995-1999	1977-1999
Agro-based industries	1.70	0.99	1.01	2.11	1.01
Food & allied industries	9.50	3.87	2.06	4.00	5.51
Cotton textiles	11.80	21.57	28.37	9.33	11.81
Printing & publication	1.01	-	0.10	-	0.50
Leather production	1.21	0.20	0.10	-	0.80
Chemical industries	28.33	7.71	4.84	5.16	9.50
Metal industries	6.08	2.40	-	-	4.58
Engineering industries	9.67	3.23	2.89	2.03	4.77
Service industries	23.00	49.00	56.28	62.08	47.97
Miscellaneous	10.70	11.03	4.35	15.29	8.50
Total	**100**	**100**	**100**	**100**	**100**

Source: *Statistics Department*, Bangladesh Bank

Table-12: Flow of FDI in Bangladesh by major countries

Year	Country									Total (million Tk.)
	UK	USA	Canada	Singapore	Japan	India	Pakistan	Korea	Others	
1991	43	14	25	-	6	2	4	6	-	628
1992	44	6	22	7	7	3	3	-	8	653
1993	24	23	32	11	9	2	-	-	-1	400
1994	16	9	25	27	5	-	-	-	17	315
1995	17	9	-	28	6	-	-	15	26	283
1996	27	27	2	15	3	-	-	16	9	630
1997	28	32	2	10	3	1	-	14	9	1013
1998	30	44	-	9	2	1	-	10	4	603

Source: *Statistics Department*, Bangladesh Bank.

Table-13: Home country of non-equity TNC participants in Bangladesh

Sectors	Number of Participants									
	UK	Japan	West Germany	South Korea	Italy	Switzerland	China	India	Pakistan	Others
Food processing	-	3	-	-	-	-	-	2	-	3
Tobacco	4	-	-	-	-	-	-	-	-	-
Textiles	-	1	-	-	-	-	-	1	-	1
Pharmaceuticals	4	-	3	1	-	-	-	3	-	1
Other chemicals	9	-	1	-	-	-	-	5	1	3
Electronics	3	3	-	3	-	1	-	-	-	-
Machinery, spares & equipment	1	3	1	-	1	2	-	5	-	6
Miscellaneous	6	-	2	2	1	1	3	3	1	8
Total	**27**	**10**	**7**	**7**	**2**	**3**	**3**	**19**	**2**	**26**

Source: BOI, *Unpublished Documents.*

Table-14: Nature of non-equity agreements by major sectors/activities

Sectors	Nature of Agreements
Food processing	Technical Collaboration and Technical Services
Tobacco	Licensing, Technical Know-how and Technical Assistance
Textile	Technical Know-how and technical Assistance, Machinery Design, Layout Agreements and Technology Transfer
Pharmaceuticals	Licensing and Technical Know-how, Technical Assistance, Project Preparation, Quality Control and Production Method, and Technology Transfer
Other chemicals	Licensing, Technical Collaboration, Technical Assistance, Technical Know-how and Formulation
Electronic goods	Licensing, Technical Know-how, Technical Collaboration and Technical Assistance
Engineering	Licensing and Technical Collaboration, Technical Assistance, Licensing patent and Technical Know-how
Miscellaneous	Licensing and Technical Collaboration, Technical Know-how, Technical Assistance, Project Preparation Services, Technology Transfer, Management Contract, Machinery Installation Services, Marketing Assistance, and Leasing Technique

Source : BOI, *Unpublished Document*

Table -15: Non-equity participation by industrial groups

Year	Name of the major industrial sectors							
	Food Processing	Tobacco	Textiles	Pharmaceuticals	Other Chemicals	Electronics Equipment	Machinery, spares &	Miscellaneous
1976	-	-	-	-	1	-	-	1
1977	-	-	-	-	-	-	-	-
1978	-	-	1	2	1	-	-	1
1979	1	-	-	1	1	-	2	-
1980	-	-	-	-	-	-	-	-
1981	-	-	-	-	-	1	-	1
1982	-	1	-	-	3	-	-	1
1983	-	-	-	1	-	2	1	2
1984	-	-	-	1	2	1	4	1
1985	-	-	-	-	-	3	-	1
1986	-	-	-	-	1	-	-	1
1987	-	-	-	-	1	4	4	1
1988	-	-	1	4	4	-	-	3
1989	1	1	-	-	-	-	-	2
1990	-	-	2	2	4	2	5	7
1991	5	1	-	-	-	-	3	1
1992	-	-	-	-	1	-	-	2
1993	1	1	1	1	-	-	-	2
Total	8	4	5	12	19	13	19	27

Source: BOI, *Unpublished Documents*

Table-16: Geographical distribution of FDI in Bangladesh by major industrial sector, 1978-1997(in million Tk. current prices)

Industry Sectors	Divisions			
	Dhaka	Chittagong	Khulna	Total FDI
Food processing	981.90	764.00	-	1745.90
Tobacco	416.19	-	-	416.19
Textiles	2090.23	431.19	-	2521.42
Pharmaceuticals	460.41	-	-	461.41
Other Chemicals	1023.38	74.80	11.00	1109.18
Metal Industry	880.60	-	-	880.60
Electronics	365.41	-	-	365.41
Electrical	921.85	-	-	921.85
Machineries	216.45	7.86	-	224.31
Leather and Products	518.21	-	-	518.21
Plastic Products	459.10	13.40	21.16	493.66
Paper & Paper Products	1038.44	-	-	1038.44
Miscellaneous	2610.00	216.17	-	2531.66

Source: Board of Investment, Ministry of Industries, Government of Bangladesh Unpublished document

Table-A.1:Type-wise list of industries and investment (accumulated figure in '000' US $)

Major Products	No. of Enterprise	CEPZ		No. of Enterprise	DEPZ	
A Type (100% foreign)						
a) In operation	46	157539	130214	21	133959	38311
b) Under Implementation	21	85046	8537	17	251035	17967
Sub-Total	**67**	**242585**	**138751**	**38**	**384884**	**56278**
B Type (Joint-Venture)						
a) In operation	15	17882	13338	3	3660	2798
b) Under Implementation	14	23188	4021	10	36665	1602
Sub-Total	**29**	**41070**	**17359**	**13**	**40325**	**4400**
C Type (100% Bangladesh)	15	32766	31360	2	860	513
a) In operation	15	22170	1954	15	40752	1766
b) Under Implementation						
Sub-Total	**30**	**54936**	**33314**	**17**	**41612**	**2279**
Total	**126**	**338591**	**189424**	**68**	**466922**	**6257**

Source: Computed from BEPZA statistics, upto September 1998

Table- A.2:Product-wise investment (cumulative figure in '000' US $)

Products	CEPZ			DEPZ		
	No. of Enterprises	Proposed	Actual	No. of Enterprises	Proposed	Actual
Fishing Reel and Golf Equipment	1	28099	33150	-	-	-
Textile	15	52217	34435	14	274459	24286
Terry Towel	9	8491	6345	-	-	-
Metal Products	13	15385	9271	1	650	-
Electronics and Electrical Goods	12	14688	9421	2	6134	-
Garments	21	63524	47202	16	40267	20784
Footwear and Leather Goods	13	59149	18280	7	15364	629
Plastic Goods	4	9246	5683	2	7040	2866
Knitting and Other Textile Products	7	21374	7019	5	17407	1674
Garment Accessories	4	5224	1969	4	4240	478
Caps	8	14590	7042	2	39250	7582
Others[2]	19	46604	10607	15	22111	4658
Total	**126**	**338591**	**189424**	**68**	**466922**	**62957**

Source: Calculated from BEPZA statistics.

Notes :

1. Information update upto September, 1997.
2. Others include Furniture, Paper Products, Tent, Toyes, Ropes, Surgical Towels and Sponges, and Miscellaneous product-heads

Table-A.3: Ownership Type-wise distribution of investment Type - A: 100% foreign-owned industries
(investment figure in "000" US $)

Countries	CEPZ						DEPZ					
	Enter-prises	In Operation		Enter-prises	Under Implementation		Enter-prises	Operation		Enter-prises	Under Implementation	
		Proposed	Actual		Proposed	Actual		Proposed	Actual		Proposed	Actual
S. Korea	18	75375	56369	5	37390	308	12	102161	30978	6	37200	756
Japan	11	42252	47062	6	8151	1929	2	2278	1059	1	650	0
H.K.	6	11224	14318	3	12399	1911	4	24187	4913	2	22437	15785
U.S.A.	5	12387	7655	-	-	-	-	-	-	1	10216	0
U.K.	2	5650	2258	4	19400	389	2	4103	462	3	8214	10144
Malaysia	2	6250	2224	-	-	-	-	-	-	2	168018	0
Singapore	-	-	-	2	4706	400	-	-	-	-	-	-
Others	2	4400	324	1	2500	0	1	1230	890	2	4300	372
Total	**46**	**157539**	**130214**	**21**	**84546**	**8537**	**21**	**133959**	**38311**	**17**	**251035**	**17967**

Source : Compiled from BEPZA Statistics.
Note : Information update upto September, 1997.

Table –A.4: Product -wise distribution of employment in the EPZs

Product-Heads	CEPZ					DEPZ				
	No. of Enter.	Proposed		Actual		No. of Enter.	Proposed		Actual	
		Local	For.	Local	For.		Local	For.	Local	For.
Fishing Reel and Golf Equipment	1	1008	16	2150	6	-	-	-	-	-
Textile	15	5312	80	2732	54	14	9279	226	559	61
Terry Towel	9	1878	4	1866	7	-	-	-	-	-
Metal Products	13	1509	53	799	12	1	181	5	0	0
Footwear & Leather goods	13	12294	115	3689	4	7	1992	29	91	1
Electronics and Electrical Goods	12	2355	45	1253	11	2	315	3	0	0
Garments	21	2276	194	19430	95	16	17231	208	11369	83
Plastic Goods	4	2134	27	690	8	2	243	2	252	1
Knitting and other textile products	7	4885	87	1933	59	5	2865	57	1431	10
Garment Accessories	4	597	4	29	0	4	348	3	33	0
Caps	8	4747	76	3337	46	2	4993	59	2961	24
Others	29	8599	48	1666	15	15	3918	66	424	11
Total	**126**	**68068**	**749**	**39574**	**317**	**68**	**41365**	**660**	**17120**	**191**

Source : Compiled from BEPZA Statistics.

Notes : Information is update upto September, 1997.
Others include Furniture, Paper Products, Tent, Toys, Ropes Surgical Towels and Songes and Micellaneous product-heads.

Table-A.5: Country-wise distribution of local employment in A-Type industries

Countries	CEPZ						DEPZ					
	No. of Industry	In Operation		No. of Industry	UNDER Implementation		No. of Industry	In Operation		No.of Ind.	Under Implementation	
		PROPOSED	Actual		Proposed	Actual		Proposed	Actual		Proposed	Actual
S. Korea	18	20235	18687	5	10846	0	12	14453	10035	6	3981	0
Japan	11	2684	3972	6	1153	9	2	160	140	1	-	383
H.K.	6	4138	5493	3	2838	114	4	2434	1997	2	843	0
U.S.A.	5	2181	3585	-	-	-	-	-	-	1	921	0
U.K.	2	1547	538	4	3174	0	2	403	274	3	402	0
Malaysia	2	337	227	-	-	-	-	-	-	2	3122	-
Others	2	847	294	1	691	0	1	164	640	2	754	200
Total	**46**	**32069**	**32696**	**21**	**19132**	**123**	**21**	**194189**	**14316**	**17**	**10204**	**583**

Source : Calculated from BEPZA Statistics.
Note : Information update upto August, 1997.

Table-A.6:Import-export statistics of CEPZ for 1996-1997(figures in '000' US $)

Country-wise Enterprises	Number	Import					Export				
		Raw, Packaging and Auxiliary Material									
		DTA	Foreign	Intra zone	Inter zone	Total	EOI	Intra zone	Inter zone	Foreign	Total
Bangladesh	12	580	23411	102	0	24093	3346	1584	1230	28902	33955
U.S.A.	7	340	17035	42	0	17418	0	0	0	27375	2775
Hong Kong	7	270	30608	198	8	31083	0	0	0	48582	48582
Japan	12	430	32825	924	77	34256	71	0	0	44822	44894
S. Korea	19	1160	162329	1404	1408	16630	3175	544	591	125477	169788
U.A.E.	1	23	0	0	0	23	0	0	0	0	98
Pakistan	3	102	3772	0	0	3875	0	0	0	6208	6208
Malaysia	2	167	3919	19	0	4104	0	0	0	5650	5650
Thailand	1	0	336	121	0	348	0	0	0	451	451
France	1	0	0	0	0	0	0	0	0	78	78
U.K.	4	0	2604	0	0	2604	0	0	-	04847	4847
Germany	1	375	556	0	0	931	0	0	0	809	809
Denmark	1	40	337	22	0	380	0	0	0	527	527
Total	**72**	**3488**	**277811**	**2704**	**1492**	**285496**	**6593**	**2127**	**714**	**293876**	**343311**

Source: Computed from BEPZA statistics, upto 1996-97

Notes : DTA - Domestic Tariff Area.
EOI - Export Oriented Industries.

Table-A.7: Import-export statistics of DEPZ for 1996-97

(figures in '000' US $)

Country-wise Enterprises	Number	Import					Export				
		Raw, Packaging and Auxiliary Material					EOI	Intra zone	Inter zone	Foreign	Total
		DTA	Foreign	Intra zone	Inter zone	Total					
Bangladesh	2	0	166	0	0	166	2	232	0	0	234
Panama	1	73	42	0	0	155	0	0	0	0	0
China	1	0	658	0	0	658	165	0	0	1	166
Hong Kong	7	635	18463	22	90	19211	0	0	0	15025	15025
Japan	3	132	2726	0	0	43226	0	0	0	358	385
Germany	1	162	4068	0	0	4230	0	0	0	5372	5372
U.K.	2	0	695	0	0	695	12	0	0	620	632
S. Korea	13	1082	97615	1162	3765	103623	9971	1156	1559	54954	97640
Total	**30**	**2084**	**124502**	**1184**	**3856**	**131625**	**10150**	**1388**	**1559**	**76358**	**119455**

Source: Computed from BEPZA statistics, upto 1996-97

Notes : DTA - Domestic Tariff Area.

EOI - Export Oriented Industries.

APPENDIX-II

[Industrial policy'1999]

APPENDIX-II

GOVERNMENT OF THE PEOPLE'S REPUBLIC OF BANGLADESH INDUSTRIAL POLICY, 1999

Introduction

In order to achieve the objective of accelerating industrial growth and to gain a greater share of industry in the gross domestic product (GDP) as well as to make the industrial policy responsive to the changes occurring in the global economy, it is imperative that the industrial policy is updated. Such modifications are made to bring about the necessary structural changes within the sector. The Government is mindful of the fact that a continuous process of reform is necessary to propel the industrial sector of Bangladesh to the take-off stage. Therefore, the policy initiatives undertaken to trigger broad - based industrial investments seek to do the following:

a. The objectives outlined in the policy statement project a clear sense of direction.

b. The strategies and the policy framework are coherent and consistent.

c. The policy pronouncements are backed by adequate legislative endorsements and effective modalities of implementation involving close interaction between the Government and the private sector.

d. There is a monitoring system in place to assess the performance of the sector on a regular basis to bring about necessary modifications in the policy framework as needed.

It is fortunate that Bangladesh enjoys political consensus across all political parties that a competitive and market-oriented economic policy is pursued in order to accelerate the economic growth process.

THE VISIONS OF INDUSTRIAL DEVELOPMENT

Bangladesh will have within a decade a sizable industrial sector where manufacturing will account for at least 25 percent of the GDP, and at least 20 percent of the

employed workforce. This will mean a considerable rise from the figure of 10 percent around which the sector's share in GDP and employed population have hovered for most of the past two decades.

A vibrant and dynamic private sector will be the principal actor in Bangladesh's industrial arena. The industrial sector of Bangladesh will be competitive in the liberalized internal market as well as in the external market. The industrial sector of Bangladesh shall have a dominant export orientation.

The goal of external competitiveness implies the pursuit of industrialization in accordance with the dynamic comparative advantage of the economy. Given Bangladesh's resource endowment, the principle of dynamic comparative advantage means production of labour intensive manufactures with skill up-gradation and productivity growth as its cutting edge. This, however, does not preclude the possibility of Bangladesh having a niche high-tech industrial sub-sector that may be externally competitive.

Dispersal of small and medium industries will constitute an important element in the industrial policy approach. Industrial development will be sustainable from the point of view of environmental concerns and resource availability.

Industrial Policy 1999 aims at addressing these concerns building on earlier efforts and gains towards industrialization of Bangladesh economy.

Objectives

The following are the prime objectives of the Industrial Policy 1999:

2.1 To expand the production base of the economy by accelerating the level of industrial investment.

2.2 To promote the private sector to lead the growth of industrial production and investment.

2.3 To focus the role of the government as a facilitator in creating an enabling environment for expanding private investment.

2.4 To permit public undertaking only in those industrial activities where public sector involvement is essential to facilitate the growth of the private sector and / or where there are overriding social concerns to be accommodated.

2.5 To attract FDI in both export and domestic market-oriented industries to make up for the deficient domestic investment resources, and to acquire evolving technology and gain access to export markets.

2.6 To ensure rapid growth of industrial employment by encouraging investment in labor intensive manufacturing industries including investment in efficient small and cottage industries.

2.7 To generate female employment in higher skill categories through special emphasis on skill development.

2.8 To raise industrial productivity and to move progressively to higher value added products through skill and technology up gradation.

2.9 To enhance operational efficiency in all remaining public manufacturing enterprises through appropriate management restructuring and pursuit of market oriented policies.

2.10 To diversify and rapidly increase export of manufactures.

2.11 To encourage the competitive strength of import substituting industries for catering to a growing domestic market.

2.12 To ensure a process of industrialization which is environmentally sound and consistent with the resource endowment of the economy.

2.13 To encourage balanced industrial development throughout the country by introducing suitable measures and incentives.

2.14 To effectively utilize the existing production capacity.

2.15 To coordinate with trade and fiscal policies.

2.16 To develop indigenous technology and to expand production based on domestic raw materials.

2.17 To rehabilitate deserving sick industries.

Broad Strategies

3.1 All regulatory barriers will be removed within the quickest possible time to facilitate easy and rapid flow of domestic private and FDI. Appropriate legal framework will be put in place to protect both investor and consumer rights to

ensure proper market operation and, consequently, for lowering cost of doing business.

3.2 There will be no discrimination between domestic and foreign investment. Due emphasis will be given to promotion of regional and sub-regional cooperation.

3.3 Existing public sector enterprises will be progressively privatized and public industrial investment will be limited to only those cases where there is special need to complement private investment or where there is an overriding social and national objective to be achieved.

3.4 The capital market will be developed and strengthened to mobilized domestic savings and to attract foreign investment.

3.5 Development of the infrastructure including port facilities, energy, transport and communication and human resource development will receive high priority. Private investment including "Build, Operate and Own" (BOO) and "Build", Operate and Transfer" (BOT) methods will be particularly encouraged in these sectors.

3.6 Intensive industrial zones development will be undertaken together with a balanced geographical dispersal of the zones in areas with growing potential for the utilization of local resources as more infrastructure and other facilities are put in place.

3.7 Consistent with the charter of World Trade Organization (WTO), protection to domestic industries from external competition will be rationalized.

3.8 To retain the competitive edge of domestic products, wage increases will be linked to productivity trends, and appropriate labor laws will be put in place to ensure congenial industrial relations.

3.9 The industrial investment will be encouraged through tariff rationalization and appropriate fiscal measures. The import and export policies will also be made supportive of and consistent with the industrial policy.

3.10 In order to develop small and cottage industries, special incentives and infrastructure facilitates will be provided.

3.11 Infrastructure, financial and technical facilities will be provided to encourage establishment and expansion of agro-based and agro-supportive industries.

3.12 Measures will be taken to encourage research and development (R&D) and promote development, acquisition and transfer of appropriate technology. At the same time, market responsive institutional framework for overall technology development will be created.

3.13 The growth of value adding linkage industries including subcontracting industries will be encouraged.

3.14 To ensure productivity growth, emphasis will be given on human resource development through providing better access to education, skill specific training and market information. Progressive infusion of new technology leading to increasingly efficient corporate structure will be encouraged.

3.15 Measures will be taken so that industrial development in the country may take advantage of the emerging regional cooperation.

3.16 FDI will be targeted, as an important vehicle of technology transfer, skill development and promotion of management and marketing know - how.

3.17 Special incentives and support will be proved for the development of export-oriented industries.

3.18 An integrated and comprehensive Management Information System (MIS) will be put in place in the Ministry of Industries, which will be made accessible at Divisional and District levels.

3.19 These strategies and measures emanating from the industrial policy 1998 will be implemented through and interactive process between the government, industry and others.

3.20 To build industrial production capacity, long- term credit will be made available and to assist commercial production of innovative industrial products, venture capital fund will be created.

3.21 Together with expansion of regional and sub-regional cooperation, joint venture with the neighboring countries / region will be encouraged.

3.22 Acquisition and dissemination of technology will be pursued through technology dissemination cell of the ministry of science and technology, trade and industries associations and Bangladesh missions abroad.

3.23 For rapid, firm and economic resolution of trade disputes, administrative judicial system will provide positive support.

3.24 Prime Minister's Council of Private Enterprise will be established for providing prompt advice in matters relating to trade and industry.

Definition and Classification of Industry

4.1 "Industry" is broadly defined to include both manufacturing industry and service industry.

4.2 "Manufacturing Industry" includes all production, processing and assembling activities as well as repairing and reconditioning of processed goods.

4.3 "Service Industry" includes those service-oriented activities, which involve significant use of equipment or fixed assets.

4.4 "Large Industry" is defined to include all industrial enterprises employing 100 or more workers and / or having a capital of over Taka 300 million.

4.5 "Medium Industry" will cover enterprises employing between 50 and 99 workers and / or with a fixed capital investment between Taka 100 million and Taka 300 million.

4.6 "Small Industry" will mean enterprises employing fewer than 50 workers excluding the cottage units and / or with a fixed capital investment of less than Taka 100 million.

4.7 "Cottage Industry" covers household-based units operated mainly with family labor.

4.8 "Reserved Industries" are those which are earmarked exclusively for public investment through executive order.

4.9 "Thrust Sectors" are those industrial activities, which are identified or so declared by the Government for the purpose of targeting special incentives and supportive measures.

4.10 The definition of "Industry" may be modified consistent with contemporaneous need.

Facilitative Role of the Public Institutions

5.1 Private sector will be the prime mover of future industrial development of Bangladesh. Industrial Policy 1999 is committed to attain this goal. In fulfilling its facilitating and promotional role, the Government will establish

effective coordination amongst the concerned agencies through structural and operational reforms.

5.2 The following is the investment framework for the development of the private sector:

a. No prior permission will be necessary to start a new industry outside those in the list "Reserved Industries" and to undertake its subsequent Balancing, Modernization, Replacement and Expansion (BMRE). However, prior clearance will be obtained in respect of public safety and environmental concerns under the existing laws and regulations. Clearance is to be taken for setting up of Ready-Made Garments (RMG) units, banks, insurance companies and other financial institutions.

b. All foreign investments shall be registered in the prescribed manner with the concerned promotional body before setting up an industry.

c. Bangladesh Small and Cottage Industries Corporation (BSCIC) will allot industrial plots to respective industrial units in its own industrial estates and estates developed by it under special orders. Similarly, Bangladesh Export Processing Zones Authority (BEPZA) will allot land in its own estates. Board of Investment (BOI) will recommend and pursue allotment of public land wherever available.

d. Concerned facilitating agencies will, after discussion with the relevant authorities, determine the time limit for receipt of power, gas, water, drainage and telecommunication connection as well as provide clearance relating to environment pollution. These facilities will be provided by the "One Stop Service" cell of the facilitating agencies.

e. BOI, BEPZA and BSCIC will approve, wherever necessary, the payment of any royalties, technical know-how or technical assistance fees and approve appointment and payment of remuneration of foreign personnel.

f. Private sector is allowed to set up export processing zones and develop industrial parks. Government will extend support to these zones and parks. Industries located in the private zones EPZs will enjoy the same facilities as those enjoyed by the units located in the public EPZs.

Privatization and State-owned Enterprises Reform

6.1 The present policy of privatization of public manufacturing enterprises will be vigorously pursued.

6.2 Investment by public sector will be limited to the "Reserved Industries". Future public investment in the industrial sector will be residual in nature. Public enterprises will be encouraged to supplement and compete with the private sector.

6.3 Existing public will be given autonomy to be run on sound commercial principles. The Government will try to improve the management of public enterprises through corrective measures and may invite foreign collaborator / investors to enter into technical collaboration or management contracts to make these industries competitive.

6.4 State-owned enterprises may be disinvested to enterprise workers in special cases under Employee Owned Stock Programme (EOSP).

Fiscal and Financial Incentives

7.1 There will be no discrimination in case of duties and taxes for the same type of industries set up in the public and private sectors.

7.2

(a) Tax holiday facilities will be available for five or seven years depending on location of the industrial enterprise. Tax holiday facilities will be provided in accordance with the existing laws. The period of such tax holiday will be calculated from the month of commencement of commercial production. Tax holiday certificate will be issued by NBR for the total tax holiday period within ninety days of submission of application.

(b) Industrial undertakings not enjoying tax holiday will enjoy accelerated depreciation allowance. Such allowance is available at the rate of hundred percent of the cost of the machinery or plant if the industrial undertaking is set up in the area falling within the cities of Dhaka, Narayanganj, Chittagong and Khulna and areas within a radius of ten miles from the municipal limits of those cities. If the industrial undertaking is set up elsewhere in the country, accelerated depreciation is allowed at the rate of eighty percent in the first year and twenty percent in the second year.

7.3 The present structure of concessional duties on imported capital machineries, based on area demarcation, viz. "Developed" and "Underdeveloped", will remain in force. Value Added Tax (VAT) is not payable for import of capital machineries and spares. In addition to other measures, creation of an Equity Development Fund will be considered for providing assistance to the industrial entrepreneurs in underdeveloped areas.

7.4 There will be a differential duty structure for imported raw materials, intermediate inputs and finished products in ascending order. Tariff anomalies, if any, will be reviewed in accordance with the existing rules and regulations.

7.5 In order to eliminate any unfair competition, tariff rationalization will be undertaken keeping in view the interests of the entrepreneurs as well as consumers. Bangladesh Tariff Commission will regularly review such cases and recommend necessary measures.

7.6 Industrial enterprises in the private sector outside the Export Processing Zones (EPZs), and joint venture (Type - B) and Local (Type - C) industries units in the EPZs may, with prior BOI approval, enter into supplier's credit and other foreign currency loan contracts with lenders abroad. 100% foreign owned (Type - A) industrial units located within the EPZs may freely borrow abroad without any prior approval. Remittance abroad towards repayments of principal and interest on these borrowings may be sent through banks without prior Bangladesh Bank approval.

7.7 Special incentives will be provided to encourage non-resident Bangladeshi (NRBs) for investment. In case of their investment in Bangladesh, they will enjoy facilities similar to those given to the foreign investors. In case of initial public offering (IPO) of shares, ten percent of the shares will be reserved by the Securities and Exchange Commission (SEC) for the NRBs. Furthermore, this can maintain foreign currency deposits in the Non-resident Foreign Currency Deposit (NFCD) account.

7.8 Special fiscal incentives may be provided to industries identified as the "Thrust Sectors" as well as to small and cottage industries. Special financial arrangement may, from time to time, be designed by the Government in support of these sectors.

7.9 An Entrepreneur will not be required to pay transfer fee and / or capital gain tax in case (s) he wants to use his / her own land to establish a new enterprise (duly registered with the BOI) under his / her ownership or wants to convert his / her existing enterprise into a "limited company" without changing the ownership structure.

7.10 Measures will be taken to create industrial fund in the Bangladesh Bank, strengthen specialized Banks, establish country fund, expand capital market, create venture capital and rationalize tax holiday system.

7.11 The rate of stamp duty will be rationalized for the purpose of mortgaging of immovable property in the banking system.

Industrial Relations

8.1 Industrial Policy 1999 seeks to promote a sound labor-management relationship geared to productivity industrial development. The legal framework of the industrial relations in Bangladesh will be provided under the concerned provisions of existing statutes, recommendations of the labor law commission and commitments to international labor organization (ILO).

8.2 The industrial relation system will be guided by a tripartite consultative process involving the workers, employees and the Government.

8.3 As a rule, collective bargaining over wage fixation, organization of work, job work and access to skills and training will take place at enterprise level.

8.4 National level tripartite bodies such as Tripartite Consultative Council (TCC), National Productivity Council (NPC) will deal with policies concerning employment promotion, productivity growth, training and skill development etc. Measures will be undertaken to evolve sectoral partnership in these areas.

8.5 To encourage female industrial employment statutory provisions relating to working conditions of female workers will be enforced at enterprise level.

Small and Cottage Industries

9.1 Bangladesh Small and Cottage Industries Corporation (BSCIC) as the relevant promotional body will remain responsible for overseeing and extending

support to the Small and Cottage Industries (SCIs). The BSCIC will do the following:

a) Arrange special credit line.

b) Allocate plots in the BSCIC Estates.

c) Organize entrepreneurship development programs with emphasis on women, unemployed youth, skilled artisans, returnee migrant workers and landless people.

d) Oversee extension of infrastructural facilities to SCIs.

e) Support market development programs for SCIs products.

f) Register the units and monitor the performance of the sub-sector.

9.2 The BSCIC will continue its efforts in creating infrastructural facilities in the growth centers similar to those available in the BSCIC Estates. In the regions, where there are no industrial estates, the relevant authorities will, on the recommendation of BSCIC, provide infrastructural facilities to the small and cottage industries on a priority basis.

9.3 Efforts will be undertaken to develop linkages of the SCIs units with the corporate sector, particularly by encouraging sub-contracting arrangements. To promote subcontracting, banks and financial institutions will make provisions for special funds. The sub-contracting industries shall enjoy incentives and facilities similar to those provided to the SCIs sector irrespective of their location.

9.4 The small industry credit guarantee scheme will be made more extensive and effective through joint collaboration of Bangladesh small and cottage industries corporation, Bangladesh Bank and public / private insurance companies.

9.5 Incentives and facilities as mentioned in article 7.8 will be available for the SCI units.

9.6 BSCIC industrial estates will accord priority to foreign investors in setting up units in their estates.

Export-Oriented and Export-Linkage Industries

10.1 Export-oriented industrialization is one of the major objectives of the industrial policy 1999. Export-oriented industries will be given priority and public policy support will be ensured in this respect.

10.2 An industry exporting at least 80 percent of its manufactured goods or an industry contributing at least 90 percent of its products as an input to finished exportable, and similarly, a business entity exporting at least 80 percent of services including information technology related products will be considered as an export-oriented industry.

10.3 To make investment in 100 percent export-oriented industries attractive, the following incentives and facilities will be provided:

a) The existing policy of duty free import of capital machinery and spare parts up to ten percent of the value of such capital machinery will continue.

b) Existing facilities for Bonded Warehouse and back-to-back letter of credit will continue.

c) The system for duty drawback will be further simplified and to this end, duty drawback will be fixed at a flat rate on exportable and potentially exportable goods. Exporters will receive duty drawback at a flat rate directly from the relevant commercial banks.

d) The arrangement for providing loans up to 90 percent of the value against irrevocable and confirmed letter of credit / sales agreement will continue.

e) To ensure backward linkage, incentives will be extended to the "deemed exporters" supplying indigenous raw materials to export-oriented industries. Export-oriented industries, including export-oriented RMG industries, using indigenous raw materials will be given facilities and benefits at prescribed rates.

f) The export-oriented industries, further to the provisions of Bangladesh Bank foreign exchange regulations, will be entitled to receive additional foreign exchange, on case to case basis, for publicity campaign, opening overseas offices and participating in international trade fairs.

g) The entire export earning from handicrafts and cottage industries will be exempted from income tax. For all other industries, income tax rebate on export earnings will be given at 50 percent.

h) The facility for importing raw materials, which are included in the banned / restricted list of imports, but required in the manufacture of exportable commodities, will continue.

i) The import of specified quantities of duty-free samples for manufacturing exportable products will be allowed consistent with prevailing relevant government policy.

j) The local products supplied to local industries or projects against foreign exchange payment or foreign exchange L/C will be treated as indirect exports and are entitled to all export facilities.

k) The export credit guarantee scheme will be further expanded and strengthened.

10.4 Ten- percent products of the enterprises, located in both public and private EPZs units will be allowed to be exported to domestic tariff area against foreign currency L/C on payment of applicable duty and taxes.

10.5 One hundred percent export-oriented industry outside the EPZs will be allowed to sell twenty percent of their products in the domestic market on payment of applicable duties and taxes.

10.6 The export-oriented industries, which are identified by the Government as "Thrust Sectors" will be provided special facilities and venture capital support.

10.7 Existing facilities for assessment and payment of duties and taxes on imported goods before its arrival will continue. Procedure and for formalities for release of goods from port will be streamlined. Pre-Shipment Inspection (PSI) system will be improved.

10.8 Greater care will be taken to ensure that production losses are avoided in industries linked to export.

Foreign Investment

11.1 The policy framework for foreign investment in Bangladesh is based on foreign investment (promotion and protection) act, 1980, which provides for:

- Non-discriminatory treatment between foreign and local investment.
- Protection of foreign investment from expropriation by the state; and
- Ensured repatriation of proceeds from sale of shares and profit.

11.2 Foreign investment, with particular preference to FDI will be encouraged in all industrial activities in Bangladesh including service industries and toll manufacturing, excluding those in the list of "Reserved Industries" and RMG, banks, insurance companies and other financial institutions. Such investments may be undertaken either independently or through joint ventures, either with the local private or public sector. The capital market will also remain open for portfolio investment.

11.3 For foreign investments in Bangladesh, there will be no limitation pertaining to equity participation, i.e. 100 percent foreign equity will be allowed. Fully foreign owned firms or joint ventures would in no way be obliged to sell their shares through public issues, irrespective of the amount of their paid-up capital. However, foreign investors or companies with foreign investments will be eligible to buy shares through the stock exchange and their participation will be guided by framing appropriate rules. Foreign investors or companies may obtain full working capital loans from local banks. The terms of such loans will be determined on the basis of bank-client relationship.

11.4 Foreign entrepreneurs will enjoy the same facilities as the domestic entrepreneurs in respect of tax holiday, payment of royalty, technical know-how fees etc. A foreign technician employed in foreign companies will not be subjected to personal income tax up to three years, and beyond that period his / her personal income tax payment will be government by the existence or non-existence of agreement on avoidance of double taxation with country of citizenship.

11.5 Full repatriation of capital invested from foreign sources will be allowed. Similarly, profits and dividend accruing to foreign investments may be transferred in full. If foreign investors reinvest their reportable dividends and / or retained earnings, those will be treated as new investment. Foreigners employed in Bangladesh are entitled to remit up to 50 percent of their salary and will enjoy facilities for full repatriation of their savings and retirement benefits.

11.6 The process of issuing work permit to foreign experts on the recommendation of investing foreign companies or joint ventures will operate without any hindrance or restriction. "Multiple entry visa" will be issued to prospective

foreign investors for three years. In case of experts, "Multiple entry visa" will be issued for the whole tenure of their assignments.

11.7 Foreign investment in "Thrust Sectors", particularly in small industrial units, will be given priority in allocation of plots in BSCIC Industrial Estates.

11.8 Investment of non-resident Bangladeshis will be treated at par with FDI.

11.9 Measures will be taken to protect the intellectual property rights of new products and processes.

11.10 Investment guarantee and dispute settlement will be guided by international arrangements and provisions.

Board of Investment

12.1 As per the BOI Act of 1989, the Board is mandated to promote, assist and provide necessary facilities to private sector investment in Bangladesh. The Board, headed by the Prime Minister of the Republic and represented by Ministers and Secretaries of the concerned Ministries, is vested with necessary powers to take decisions for speedy implementation of new industrial projects and provide operational support services to the existing ones.

12.2 The major functions of Board of Investment (BOI) include the following:

a) Undertaking investment promotion activities at home and abroad.

b) Providing all types of facilities for promotion of capital investment and rapid industrialization.

c) Registration of industrial projects including infrastructure, manufacturing and service-oriented industries as well as foreign loan, royalty, technical know-how and technical assistance agreement wherever required.

d) Approval of payment of royalty, technical know-how and technical assistance fees to foreign nationals / organizations beyond the prescribed limits.

e) Issuing work permit to expatriate personnel working in private sector industrial enterprises.

f) Providing import facilities to industrial units in the private sector.

g) Approval of the terms and conditions of foreign private loan and suppliers' credit beyond the prescribed limit.

h) Allotment of land in the industrial areas / estates for industrial purpose.

i) Conciliation of disputes relating to foreign investors; and

j) Providing assistance to avail infrastructure facilities for industries.

12.3 BOI will extend "One Stop Service" to the investors, particularly in the following areas:

a) Electricity and gas connection.

b) Water and sewerage connection.

c) Telecommunication facilities.

d) Custom clearance of imported machinery, spare-parts and raw materials.

e) Clearance from the environmental agencies; and

f) All other facilities and services that may be required for speedy setting up and operation of an industry.

To this end, functionaries of all concerned government agencies with adequate decision making authority are attached to the BOI "One Stop Service Center".

Export Processing Zones

13.1 To assist establishment of export-oriented industries, Export Processing Zones have been created in Bangladesh under Bangladesh Export Processing Zones Act, 1980, where necessary infrastructural facilities including communication and utility connection have been provided. The Bangladesh Private Export Processing Zones Act, 1996 allows establishment of private EPZs entirely through foreign investment or through joint ventures or local initiative.

13.2 The following three types of investment are allowed in the EPZs:

Type (A): Fully foreign owned units having one hundred percent foreign investment including investment by non-resident Bangladeshis. Under this type of investment, the total investment cost including the construction, raw material cost and requirement for the whole of working capital have to be met through the foreign investors' own source of foreign currency.

Type (B): Joint venture projects by foreign investors and Bangladeshi investors living within the country. Under this type of investment, project costs will be shared in accordance with arrangement executed between local and foreign partners, provided that cost of all imported machineries is financed by the foreign partners.

Type (C): Fully locally owned where one hundred percent investment made by Bangladeshi investors residing in Bangladesh. Under this type of investment all project costs including imports of machineries will be financed from local investors' own source., suppliers' credit, non-repatriable foreign currency, Pay-as-You-Earn Scheme or any other acceptable arrangement.

13.3 The following facilities are provided to units located in the EPZs :

a) Income tax exemption for ten years and 500 percent income tax rebate on export earning after that period.

b) Duty free import of raw materials machinery, construction materials and other materials used in manufacturing process.

e) Tax exemption on royalties, technical know-how and technical assistance fees.

f) Tax exemption on profits on account of transfer of shares by foreign companies listed with the Stock Exchange.

g) Relocation of running manufacturing units from abroad to EPZs.

h) Units in the EPZs will be permitted to supply linkage material for manufacture of exportable to industries operating in domestic tariff area through bonded warehouse and / or back to back L/C;

i) Off-shore banking facilities; and

j) Establishment of backward linkage industries will be encouraged for supplying inputs in Export Processing Zones.

Industrial Technology

14.1 Industrial Policy 1999 aims at facilitating change and advancement of technology to gain and retain competitive strength, to reduce consumer cost through use of cost effective technology and to promote an environment-friendly industrial production system. A combination of improved management and production technology can lead to enhanced profit for entrepreneurs and provide them the flexibility to operate efficiently within a changing global and local market condition. To this end, relevant public policies will be reviewed periodically.

14.2 Support schemes based on highly selective or targeted measures geared to promote new technology to accelerate import replacement and / or export

expansion will be put in place for potential activities within the "Thrust Sectors".

14.3 Procedure for licensing of imported, adapted and domestic technologies shall be simplified.

14.4 A corporate culture conductive to a planned human resource development and creation of a work force capable of adapting to technological changes will be encouraged.

14.5 Approved Research and Development (R&D) expenditure will receive tax breaks. Effective links will be established between universities, research institutions and industries for disseminating research results.

Source: Investing in Bangladesh (Board of Investment, Dhaka, October 1999, Pages: 140-159).

APPENDIX-III

[Potential sectors for investment in Bangladesh]

APPENDIX-III

POTENTIAL SECTORS FOR INVESTMENT IN BANGLADESH

Bangladesh, traditionally known for jute and tea exports, has recently attracted world-wide attention for readymade garments and leather exports. Bangladesh foresees an expansion of her agricultural sector, as well as increased diversity in non-traditional industries and business. Below is a short account of a few potential investment areas.

Textile

From a modest beginning in 1978 as an insignificant non-traditional item of export, fetching only US $ 6.4 million in 1981, garment sector of Bangladesh has now become a 3.8 billion foreign exchange earner, enjoying the status of 5th largest exporter and largest shirt and T - shirt exporter to the EU and 6th largest apparel exporter to USA. Apart from contributing 73.28% of total foreign exchange earning of the country, this sector has become the largest source of employment generation. This sector employs over 1.5 million people of whom 90% are women. Directly and indirectly, about 15 million people are dependent on this sector. Today over 2800 small and medium scale privately owned garment factories registered with BGMEA, spread in cluster over the EPZs and urban areas of Dhaka, Chittagong and Khulna are manufacturing ready-garments of varied specifications as per size and designs stipulated by the overseas buyers.

The apparel sector has created an export oriented captive market for over 3 billion yards of fabrics per year, which is increasing by not less than 20% each year. The textile sector, rather capital intensive one requires foreign capital to flourish to successfully match the fabric requirement of the export oriented RMG sector of the country. Presently around 85% of the total requirement of woven fabric and around 35% of the total requirement of knit fabric are imported by the export oriented RMG industry.

a) Yarn gap: During the year 1996-97 country's yarn production was about 160 million kg out of which 56 million kg of yarn has been supplied to RMG and knitwear industry. The yarn demand for 1998 is 545 million kg. Out of which 186 million kg will be required for domestic fabric. The yarn demand for domestic requirement will increase from 186 million kg to 207 million kg in 1999-2000 and to 263 million kg in 2004 - 5. For export - oriented RMG industry, the yarn requirements will increase from 398 million kg to 434 million kg in 1999-2000 and to 554 million kg in 2004-5.

b) Fabric gap: The fabric demand for 1998 is 4095 million metre, out of which 2422 million metre will be required for RMG industries and 1673 million for local consumption. In 1997 country's fabric production was about 1150 million metre which met approximately 35% of the country's total fabric requirement. At present only 15% of the woven fabric requirement of the export oriented RMG industries is met with local supplies.

c) Government projection: The government envisages establishment of 242 spinning mills, 476 weaving mills and 475 dyeing-printing-finishing mills by the year 2005, to meet the demand gap of yarn and finished fabric.

Jute goods (diversified jute products)

Jute is the second most important natural fibre, after cotton. Of the global production of about 3 million tons of jute and allied fibres, the five major jute producing countries, namely, Bangladesh, China, India, Nepal and Thailand account for about 97 percent. Bangladesh is the second largest producer of jute. A substantial amount of foreign exchange (Tk. 1500 - 1700) crore per year) is earned by Bangladesh through export of jute and jute products.

Jute is usually known for its use as packaging material, and remains as an important packing material in national and international trade. The traditional jute products are *sacking, hessian* and carpet backing cloth.

The International Jute Organization (IJO), in cooperation with national and international research institutions, have developed a number of technologies,

processes and products for diversified use of jute. These are now ready for commercial exploitation. Prospective investors may avail themselves of the opportunity to invest in these projects for which guidance and assistance will be forthcoming from IJO. Feasibility viability reports of few such projects, the outlines of which are mentioned below can be collected from the IJO.

Home textile has been identified to be an area where jute blended with other fibres can produce a range of products suitable for consumption as home textile materials. The process has also been developed for blending jute with cotton and other fibres to spin relatively finer quality of yarns for use as textile grade materials. Fabrics as well as home textiles like curtain, bed covers, bed sheets, pillow covers, sofa set covers, mattress covers, wall mats, prayer mats etc. and other products like soft luggage bags, fancy packaging, covering blankets, shoe uppers, denims, jackets, wrappers, mufflers, caps etc. could be made out of these jute blended yarn. A number of composite materials have been developed with jute and resins. Such materials can replace wood for various applications. The products are not only cheaper in cost, but also have excellent properties like fire resistance and insects proof. Door panels, window frame, tables, furniture, paneling materials and engineering structural material can be produced with such resin treated jute.

Jute can also be reinforced with plastic to produce molded products by using any molding techniques. Up to the extent of 40% of jute, the flow property of the plastic remains unchanged, whereas the products improve in their physical properties. Jute can also replace environmentally hazardous synthetic products as well as glass fibre materials in many applications.

Non-woven products made of jute and jute blended with other fibres can replace shoe in soles in a big way. The non-woven technology can also produce jute mats that can be used by the intermediate suppliers of automotive component for various applications. This natural jute fibre can replace glass fibre in such application. This bio-degradability and re-cycleability of jute will come handy in such uses. Moreover, the jute products will be cheaper and lighter than the glass fibre materials making the vehicles cost competitive and fuel efficient.

Using whole jute or jute fibre as an input for making paper pulp is now an established phenomenon. In this process forest resources are substituted by jute, which is an annual crop and thereby help preventing deforestation.

Flexible jute bags laminated with aluminum foils and plastics can be used for packaging tea. Paper based flexible bags are replacing tea chests for carrying tea in order to keep aroma and flavor of tea which can easily be replaced by flexible jute bags.

Jute textile is an existing product used for soil erosion control and agro-plant mulching. This natural fiber based geotextile can easily replace the synthetic geotextile in many applications. Jute as an annual crop, available at cheap price is the basic raw material for all of these diversified products. International awareness of eco-friendliness, bio-degradability and re-cycleability of jute adds advantage to this natural fiber for substituting others. As a new sector for investment, all these diversified products have potential for earning attractive returns.

Leather goods

There is already a substantial domestic leather industry, mostly export-oriented. The leather includes some ready-made garments, although that aspect is confined mainly to a small export-trade in "Italian-made" garments for the US market. Footwear is more important in terms of value added, accounting for just over US$ 4 million export in FY 1992-93. The figure raised at US $ 22.77 million in FY 1996-97. This is the fast growing sector for leather products. Presently, Bangladesh produces between 2 and 3 percent of the world's leather market. Most of the live-stock base for this production is domestic which is estimated as comprising 1.8 percent of the world's cattle stock and 3.7 percent of the goat stock. The hides and skins (average annual output is 150 million sq. ft.) have a good international reputation. FDI in this sector along with the production of tanning chemicals appears to be highly rewarding.

Having the basic raw materials for leather goods as well as for the production of leather shoe, a large pool of low cost but trainable labor force together with tariff concession facility to major importing countries under GSP coverage, Bangladesh can

be a potential off shore location for leather and leather products manufacturing with low cost but high quality.

Frozen Food

The frozen fish export is the second largest export sector of the country with annual turnover of US $ 321 million (17.05 M. lbs) in 1996-97. The average annual growth rate is 28%. This 100% export oriented industry includes the following sub-sectors, which need proper attention for augmentation of production and export earnings.

- Hatcheries.
- Sustainable aqua-culture technology.
- Feed meals plants.
- Processing unit for value-added products.

Foreign investment with technology in this potential sector has been recognized as the most viable areas in Bangladesh.

Natural resources

Bangladesh is now on the threshold of an investment break through in the oil and gas section. The enemy sector as a whole enjoyed an annual accelerated growth rate of 15.31 percent during the Fourth Five-Year Plan period against a target of 9.28 percent. During Fifth Year Plan this rate is expected to be 25 percent. This sector also mobilizes a significant amount of financial resources for public sector investment. In 1996-97 an amount of Taka three thousand crore was generated on account of CD VAT and other payment which is about 25% of the annual development budget.

The government has taken up some short term and long term programs to solve the present energy crisis in the country. With these, country's energy situation is expected to improve within a short time. 58 km Ashuganj-Bakhrabad gas transmission pipe line has been commissioned and Chittagong has been connected with the national grid. This would lead to an additional gas supply of 82 MMCFD. Meghna-Bakhrabad gas transmission line (35 km) has been commissioned this year. Meghna (17 MMCFD) and Salda (15 MMCFD) gas fields have begun production and gas supply to national grid has increased by 32 million cft. daily. The Belabo gas field was also brought to production by completion of Belabo-Narshingdi gas pipe line (13 km). The Kailastila

well no. 4 (28 MMCFD) also has started production. Habiganj (No. 9) has been completed and started production this year (20 MMCFD). An urgent programme is in hand to complete gas transmission line across Bangabandhu Bridge, which is expected to be commissioned soon.

Contracts for Oil and Gas exploration under production sharing contracts have so for been signed for 8 blocks. Gairn Energy plc. and Occidental Ltd. have geared up their exploration efforts in the country. In order to further intensify and expand gas production, the remaining 15 blocks were put up for bidding. It was found that most of the global players in oil and gas participated for 12 blocks. Award of blocks will be finalized soon. An LPG plant has been established at Kailashtila with an annual production capacity of 5000 M. ton. LPG is being marketed since August 1998. Attempts have been made to encourage foreign investments in this field. Three MOUs have been signed.

An NGL, plant at Ashuganj will be set up by RPGCL with World Bank funding. A Pilot CNG Project has been implemented to popularize the use of environment friendly fuel and already about 800 vehicles have been converted to CNG. Steps have been taken to expand the use of CNG in the country. Private sector participation in CNG activities is being encouraged.

Barapukuria Coal Mine Development Project is under implementation and production is expected to be started from 2000. About 10 million tons of coal will be produced per year of which 85% will be used for a 300 MW power plant. Maddhapara Hard Rock Plant is under implementation and is expected to be commissioned by 2001.

Reform measures have been taken to strengthen operational capability of the sector. To this end, initiatives are afoot to establish a Gas Regulatory Authority (GRA) and Hydro-Carbon Unit. A study is being conducted by the Asian Development Bank to formulate a "Gas Act". The study is being carried out by NERA, a British consulting firm. Simultaneously, the United States Trade and Development Agency (USTDA) is conducting another Gas Sector Strategic Study to determine the future uses of gas in Bangladesh.

Power sector (electricity)

An adequate supply of electricity at a reasonable reliability and cost is a pre-requisite for the socio-economic development. 17% of the Bangladesh population have access to electricity and per capita generation is 106 kw. The potential for growth of this sector is very high. The Government of Bangladesh has attached top priority for the development of the power sector.

a) **Power generation**: Since the creation of Bangladesh the installed generation capacity has increased to 3603 MW (including 302 MW IPP) from 550 MW in 1971-72. The maximum demand of 183 MW in 1871-72 also increased to 2449 MW at present. However, the present available generation capacity is about 2400 MW. Many of the existing power plants are gradually reaching at a stage where balancing, modernization, rehabilitation has become necessary. It is possible to involve the private sector in this aspect in the near future.

A Power System Master Plan study was conducted in 1995. The study has identified the least cost power development plan for the next 20 years. It is estimated that the peak demand in FY 2000 will be about 3150 MW and this will increase to about 4600 MW in FY 2005.

The Siddirganj 210 MW power plant is under construction and the installation of Shahjibazar 60 MW, Haripur 109 MW and Baghabari 100 MW power plants are under process.

b) **Private sector generation:** The government is committed to provide adequate electricity supply to its population at a reasonable price. In view of the large capital requirement in the power sector and limitations of government fund, private sector investment would be necessary for desired development of the power sector. Accordingly, Bangladesh has amended its industrial policy and the power sector has been opened up to the private sector.

The government approved the "Private Sector Generation Policy of Bangladesh" in 1996 to attract private investment in power generation. Under the policy, the private power companies shall be exempted from corporate income tax for a period of 15 years and the companies will be allowed to import plant and equipment without payment of custom duties and VAT.

Contracts have already been awarded for installation of 4 Barge Mounted Power Plants (BMPP) with a capacity of 100 MW each, Haripur 360 MW and Meghnaghat 450 combined cycle power plant in the private sector. Out of these, the Barge Mounted Power Plants at Khulna, Haripur,and Baghabari have been commissioned. The process of signing contracts for Baghabari 115 MW gas Turbine Power Plant and Noapara 100 MW Barge Mounted Power Plant in the private sector is underway. The Rural Power Company is setting up 60 MW gas turbine power plant in Mymensingh. Further steps have been taken to set up small power plants having capacity up to 10 MW in rural areas for ensuring uninterrupted power supply and overall economic development of the country.

c) **Transmission:** The transmission voltages are 230 kv and 132 kg. The route length of transmission lines has increased from 994 km. in 1971-72 to 3500 km. at present. The distribution voltages are 33 kg, 11 kv and 0.4 kv. The distribution network has also expanded and increased from 9010 km. in 1971-72 to 136,000 km. With the increased supply of electricity, the number of consumers has increased from 254,000 in 1971-72 to 3,700,000 now.

With the increase in the supply of gas resources in future, the spread of the electrical system through rural area electrification will be given priority.

The government has recently completed the construction of Comilla - Bara Aulia 132 kv and undertaken the construction of Comilla - Hat hazari 230 transmission line to increase the reliability of the power transmission system and to evacuate the surplus power generated in the Chittagong area.

The Power Grid Company of Bangladesh (PGCB) constituted under company's Act has undertaken the construction of Comilla-Meghnaghat-Haripur 230 kv line for evacuation of power to be generated at Meghnaghat Power Plant and construction of Tongi-Kallyanpur-Hasnabad 230 kv line for increasing the reliability and stability of power supply in Dhaka area.

d) **Distribution**: In September, 1998, the power distribution system of the Mirpur area of Dhaka has been handed over to the Dhaka Electric Supply Company (DESCO), established under company's act. Necessary work for building the

infrastructure for distribution of additional 400 MW to meet the growing demand of greater Dhaka area has already been taken up.

Necessary rules and regulations are being formulated in order to establish a National Energy Regulatory Commission to ensure safety, security of electrical system to promote competition and efficient market conduct, to protect the interest of the consumers, investors and other stockholder's, to provide uninterrupted and reliable power supply at a reasonable price etc.

Telecommunication

The Government of Bangladesh has adopted National Telecommunication Policy, 1998. The strategic vision of the government is to facilitate universal telephone service throughout the country and where there is a demand all those value added services such as cellular mobile telephone, paging, data services, access to internet (including electronic mail), voice mail and video conferencing all at an affordable cost without compromising performance. To achieve the vision, government's role as a service provider will diminish as the private sector's role increases. The government's objective will be to create a new policy environment to support the new scenario. Its ability to create policy, regulate and facilitate will be strengthened through a new Telecommunication Act which reflects the government's new policies, objectives and strategies and establishment of new institutions including a Telecommunication Regulatory Commission (TRC) which will become the guardian of the Act and fulfill its regulatory functions.

By opening the telecommunication sector to competition and consolidating an independent regulatory board, private sector investment both domestic and foreign is encouraged. Private participation will improve access to and quality of both basic and value-added services, which historically have remained monopolistic. Investment is encouraged through BLT / BOT / BOO / BTO and other joint venture schemes which, by greatly increasing the capacity, quality and type of services, will create improved efficiencies in other sectors such as transportation energy, and the textile industry.

The present teledensity of Bangladesh is about 0.4 telephone per 100 persons. In order to substantially eliminate the unserviced demand and increase the teledensity from 0.4

telephone to 1 telephone for every 100 persons, target for expansion of telephone penetration is fixed at 1,300,000 line units including associated inland and overseas transmission links and facilities by the year 2000. The aim is to lay emphasis on the efforts to upgrade the semi-urban and rural telecommunication facilities and make the telecommunication services with the latest technology available in phases to all the upazilas, unions, growth centers and ultimately to the villages by the year 2005.

To meet the telecommunication requirements of the country, the government has been developing and expanding the systems and services of BTTB. Private sector operations in the rural telecommunication, paging, cellular telephones and riverine radio trunking have already been allowed. At present 7 private operators are providing their services to about 100,000 customers. Government has allowed expanding 300,000 digital telephone in Dhaka City by private sector participation through open tendering.

In accordance with overall national policy, liberalization of the telecommunications sector will continue. However, the government retains the sole authority to determine the number of competitions that are economically viable for certain services. The strategy is to provide equal and rational opportunities to all competitors.

Air transportation

In air transport, the government has given provisional domestic air transport operating license to 6 private companies for STOL services. Seven airports have been refurbished to cater their needs. International air and cargo transport in the private sector is now allowed for operation in Bangladesh.

Electronics

Bangladesh's experience in basic electronics spans over two decades. In recent years, European and Asian electronic firms have established technical collaboration with their Bangladeshi counterparts to produce some electronic goods at competitive prices. This has tremendous potentiality for expansion.

Light engineering industries

Light industries in Bangladesh produce a multitude of labor intensive goods including toys, consumer items, small tools and paper products for the domestic market. Further development of these industries offers various investment opportunities. Export-oriented production in light industries has gained momentum in the past few years. Entrepreneurs from Hong Kong, Japan and Korea have taken advantage of Bangladesh's cheap and easily trainable labor and its infrastructure facilities to manufacture products for the export market.

Tourism

With growing international interest in travelling through Asia, tourism is taking roots in Bangladesh. Bangladesh offers a variety of historically significant and culturally unique sites for tourists. Sylhet's tea gardens, Cox's Bazar sea-beach, the Royal Bengal Tiger, deer and the Sundarbans, the largest mangrove forest in the world with unique bio-diversity offer tourist attractions. Ancient mosques, Buddhist monasteries, Hindu temples, monuments and other landmarks dot the countryside.

Additional hotel and resort facilities could be created for attracting tourists from home and abroad. Dhaka and Chittagong also have an unmet demand for additional hotel rooms, restaurants, entertainment and recreational facilities.

Agriculture

Raw jute, tea, tobacco, vegetables, spices and tropical fruits are the key potential products. Agriculture is the biggest private sector operation contributing 35% of GDP. The government has gradually removed the constraints imposed by state intervention, deregulated and liberalized the markets to allow further private participation, particularly in the supply of inputs and distribution of outputs. The government has drastically reduced duties and taxes on a range of agriculture inputs. Fertilizer is exempted from customs duties and VAT. Bangladesh continues to grow about 2 percent of the world's tea in some 150 plantations in the north-east region of Sylhet. Tropical fruits and vegetables are grown seasonally and have recently begun to be exported in various forms. Tobacco farming is also well established.

Agro-based industries

Bangladesh has the basic attributes for successful agro-based industries, namely, rich alluvial soil, a year-round frost free environment, and adequate water supply and an abundance of cheap labor. Increased cultivation of vegetables, spices and tropical fruits now grown in Bangladesh could supply raw materials to local agro-processing industries for both domestic and export markets.

Progressive agricultural practices improved marketing techniques and modern processing facilities would enable the agro-processing industry to improve its quality and expand production levels significantly.

Computer software development, data entry and data processing

Availability of substantial number of qualified and experienced young people in various branches of engineering, science and technologies have opened up the scope of profitable investment in these sectors. Comparatively short training period and low investment have made such ventures highly profitable.

Source: Investing in Bangladesh (Board of Investment, Dhaka, Page, 43-53)

APPENDIX-IV

[Thrust sector and service sector industries in Bangladesh]

APPENDIX –IV

THRUST SECTOR AND SERVICE SECTOR INDUSTRIES IN BANGLADESH

Thrust Sector Industries

1. Agro-based industries.
2. Artificial flower-making.
3. Computer software and information technology.
4. Electronics.
5. Frozen Food.
6. Floriculture.
7. Gift items.
8. Infrastructure.
9. Jute goods.
10. Jewllery and diamond cutting and polishing.
11. Leather.
12. Oil and gas.
13. Sericulture and silk industry.
14. Staffed toys.
15. Textiles.
16. Tourism.

Service Industries

1. Entertainment (i.e. cinema, amusement parks etc.)
2. Hospitals and clinics.
3. Information technology-based activities (i.e. computer software, data entry and management, electronic communication etc.).
4. Construction.
5. Hotels and guest house.

Source: Investing in Bangladesh (Board of Investment, Dhaka 1999, Page, 98).

APPENDIX-V

[Indicative list of private sector investment opportunities in Bangladesh]

INDICATIVE LIST OF PRIVATE SECTOR INVESTMENT OPPORTUNITIES IN BANGLADESH

Private investment is welcomed in all areas of the economy except four reserve sectors. An indicative list of private sector investment opportunities is given below:

Food and allied products

- Dairy farming and dairy products.
- Poultry farming and poultry products.
- Shrimp, crab and other fish culture, processing and preservation of fish and other seafood.
- Fish meal production.
- Fruits and vegetables processing and canning.
- Seed production and processing.
- Other agro-based industries.

Textile Industry

- Composite textile mills.
- Specialized textile mills.
- Sericulture, reeling and filature.

Leather and rubber products

- Leather finishing.
- Footwear including shoe upper, sole etc.
- Tyres and tubes.
- Leather goods, such as gloves, bags, jackets etc.

Chemical and allied industries

- Soda ash.
- Paper and pulp (based on jute wastes and cuttings).
- Paper converting including artificial flowers and toys.
- Jute goods.
- Dyes, pigments and colour (basic manufacture).
- Pharmaceutical chemicals (basic manufacture).
- Plastic products including acrylic pipes and toys.
- Special chemicals, such as extraction of amino, organic and other acids from agricultural wastes.
- Chemicals for tanneries.
- Manufacture of basic pesticides.

Glass and ceramic

- Cement including portland and white cement.
- Sheet and plate glass.
- Fluorescent tubes and electronic ballasts.
- Parts and components of power hydrants, water supply and sewerage equipment.

Engineering industries

- Ship building, machinery and equipment.
- Sponge iron.
- Railway engine and ancillary equipment.
- Agricultural machinery and equipment.
- Gas distribution machinery, meters and fittings.
- Air conditioners, air coolers and refrigerators including compressors.
- Electrical appliances and accessories.
- Electric motors including fan motor, DC motors and their parts.
- Mechanically propelled vehicles and components.
- Electronic goods.
- Television, radio and audio and video gadgets and their components.
- Scientific and precision instruments including laboratory equipment.

- Optical lenses, prisms, microscopes etc.
- Disposable needles and syringes.
- Office equipment such as typewriter, photocopier, calculator, fax and telex machine.
- Component of fishing reel and equipment.
- Telecommunication equipment and their parts.
- Electronic watch and clock.
- Construction machinery and equipment.

Others

- Computer software and software application.
- Gems cutting and polishing.
- Sports goods.
- Tourism, hotel and resort facilities.
- Photographic and video camera, lens.
- Oil, gas, mineral explorations.
- Power and electric generator.
- Export-oriented flower and orchid farming as well as artificial flower.
- Mechanical toys.
- Imitation jewellery.
- Exportable gift items.
- Computer data entry, data processing.
- Other high tech and export oriented industries.

Source: *Investing in Bangladesh* (Board of Investment, Dhaka 1999, Pages:98-101)

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