

Trend of FDI and Economic Growth: A Study on Bangladesh

Md. Edrich Molla

Abstract:

This study is expected to mainly show the trend of foreign direct investment and economic growth influencing overall economic development of Bangladesh. FDI employed in EPZ and Non-EPZ areas by foreign investors while analyzing and interpreting relevant data in some of designated areas linked to contributing to the sustainable economic development of the country. Taking the utmost significance of this FDI and economic growth throughout worldwide economic performance into consideration it is believed to be a useful study which is expected to explore present situation in Bangladesh. This study focuses on foreign investors' preferred areas which contribute to a large scale of economic growth of Bangladesh. The factors considering measures taken by the government have helped boost the amount of foreign investment in the recent years. Last but not the least, this paper shows how FDI helps to build a strong economic basement of Bangladesh.



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1. Introduction

Foreign direct investment is the international investment that reflects the objective of a resident entity in one economy obtaining a lasting interest in an enterprise resident in another economy (The resident entity is the direct investor. On the other hand, the enterprise is the direct investment enterprise). A foreign direct investor may be an individual, an incorporated or un-incorporated and/or un-incorporated enterprise that has a direct investment enterprise i.e. a subsidiary, associate or branch operating in a country other than the country or countries residence of the foreign direct investor(s). The lasting interest implies the existence of a long-term relationship between the direct investor and enterprise and a significant degree of influence by the investor on the management of the enterprise. Furthermore, Direct investment comprises not only the initial transaction establishing the relationship between the investor and the enterprise but also all subsequent transactions between them and among affiliated enterprises, both incorporated and un-incorporated. It is mentionable that a direct investment enterprise owns 10 percent or more of the ordinary shares or voting right for an incorporated enterprise or the equivalent for an un-incorporated enterprise (IMF, Balance of Payment Manual, 5th addition, 1993, page-86). The components of FDI are: a) Equity capital b) Reinvested earnings and c) Intra-company loans.

In order to conduct the current FDI survey for the period January-March, 2017 and April-June, 2017, the updated lists of FDI enterprises have been collected from the Authorized Dealer Banks, Bangladesh Investment Development Authority (BIDA) and Bangladesh Export Processing Zones Authority (BEPZA). During the period January-March, 2017 FDI survey forms were sent to 2038 enterprises, among them, 277 enterprises are located in EPZ areas and the rest 1761 are in Non-EPZ areas. For January-March, 2017 a total number of 1572 (77.13%) enterprises submitted FDI returns, of which 243 from EPZs and 1329 from Non-EPZ areas. During the period April-June, 2017 FDI survey forms were sent to 2104 enterprises, among them, 281 enterprises are located in EPZ areas and the rest 1823 are in Non-EPZ areas. In April-June, 2017 a total number of 1628 (77.38%) enterprises submitted FDI returns, of which 248 from EPZs and 1380 from Non-EPZ areas. FDI data in connection with the rest of 466 (22.87%) enterprises were not included in the survey report because of non-response during the 1st quarter of 2017. Among these 466 non-respondents 432 are located in Non-EPZ areas and 34 are in EPZ areas. On the other hand, during the 2nd quarter of 2017 the rest of 476 (22.62%) enterprises were not included in the survey report because of non-response. Though 466 enterprises in January-March, 2017 and 476 enterprises in April-June, 2017 did not submit FDI returns, the survey captured the maximum enterprises having large amount of FDI

2. Problem Statement

Researcher required getting sufficient authentic data on FDI and economic growth to study, analyze and present data to conduct this study but sometimes it was experienced that different sources show different result in a certain period of time such as one source shows that the FDI inflow is US\$ 3037.92 million but other source claims that it is US\$ 4012.10 million. On the other hand, some sources of data show that growth rate is 7.1% but another source indicates 7.5%. Therefore, a number of secondary sources were studied to get authentic data to interpret and present properly for this study. Besides, it was difficult to access all the related departments to get relevant data. On the other hand, government sources have been found insufficient data to collect during the time of this study.

3. Research Gap

This study investigates the trend of FDI and economic growth of Bangladesh. Researcher found while conducting this study that there is insufficient researches have been conducted in this current field though it is a vital area to study for the researchers. Foreign investors and government require more study and more information on this field. Investors seek authentic relevant information on trend of FDI to make investment decisions. On the other hand, government requires understanding the trend of FDI and economic growth to attract foreign investors. Therefore, this study will help to understand both foreign investors and government on FDI and economic growth of Bangladesh.

4. Review of Literature

Researcher reviewed a number of previous studies on this field as it is an inseparable task to conduct a research for the study. Researchers have tried to find out the relationships between FDI and economic growth of a country. Besides, they have focused on current scenario regarding the study through comparative data analysis, interpretation and data presentation. As researchers follow a standard guide lines to review of literature, a number of relevant studies on FDI and economic growth is reviewed for conducting this research. According to **Nair-Reichert, U. et al. (2001)**, the remarkable increase in FDI flows to developing countries over the last decade has focused attention on whether this source of financing enhances overall economic growth. They also used a mixed fixed and random (MFR) panel data estimation method to allow for cross country heterogeneity in the causal relationship between FDI and growth and contrast our findings with those from traditional approaches. Besides, they found that the relationship between foreign investment and economic growth in developing countries is highly heterogeneous and that estimation methods which assume homogeneity across countries can yield

The fact is that FDI mostly flows towards the developed countries and only a small portion of FDI flows to a limited number of developing countries. Thus, most of the developing nations almost fail to attract a handsome amount of FDI. **Mottaleb, K. A. (2007)** claimed that using panel data from 60 low-income and lower-middle income countries that firstly the influential factors that determine FDI inflow in the developing countries and secondly empirically demonstrates the relationship between economic growth and FDI. It was also found that countries with larger GDP and high GDP growth rate and maintain business friendly environment with abundant modern infrastructural facilities, such as internet could successfully attract FDI and FDI on the other hand, significantly affect economic growth of a country. FDI affects on economic growth of a country tremendously for the socio-economic development. **Wang, M. (2009)** showed by following a standard guidelines, government can attract foreign investors leading to economic development and high growth of GDP in the economy. Researcher also describes that introduction to the analytical framework as to how FDI can impact economic growth, followed by each other; it also indicated that inward FDI in different sectors have differential impacts on host country.

Providing suitable area or industrial parks and creating a favorable environment for foreign investors to make investment decision can help to grow GDP. **Hossain, M. A. (2008)** prescribed that Foreign Portfolio Investment (FPI) and Foreign Direct Investment (FDI): characteristics, similarities and differences, policy implications and development impact that might lead to increase rapidly economic growth of an economy. Furthermore, researcher finds a positive increase of FDI, contribute to be positive growth. **Alfaro, L., et al. (2004)**

indicated that FDI alone plays an ambiguous role in contributing to economic growth. However, countries with well-developed financial markets gain significantly from FDI. The results are robust to different measures of financial market development, the inclusion of other determinants of economic growth, and consideration of endogeneity. **Agrawal, P. (2000)** recommended that the past decade was marked by the increasing role of foreign direct investment (FDI) in total capital flows that exist and employ in growth progression to associate the impact of the interaction with FDI on economic growth. **Sahoo, P. (2006)** found that the effect of FDI on domestic investment needs to estimate an investment function and then analyze the impact of FDI. Researcher also considered how FDI can contribute to high level of economic growth. Another study it was evidenced by **Gillis, M., et al. (1992)** that the determinants and effects of foreign direct investment in a country, with a strong focus on attraction, promotion towards the foreign investors to invest suitable industries. There were two main sources from which information is drawn: survey studies and econometric studies.

FDI is an important source of development financing, and productivity gains by providing new investment, better technology, management expertise and export markets. **Adhikary, B. K. (2010)** gave a clear indication that source constraints and lack of investment in developing countries, there has been increasing reliance on the market forces and private sector as the engine of economic wealth. Therefore, all countries, particularly developing country like Bangladesh seeks to attract foreign direct investment for the package of benefits it brings along with it into the country's economy. Governments often promote inward foreign investment to encourage technology 'spillovers' from foreign to domestic firms. **Bhattacharya, D. (1998)**. Using panel data on Venezuelan plants, the authors find that foreign equity participation is positively correlated with plant productivity (the 'own-plant' effect), but this relationship is only robust for small enterprises. They then test for spillovers from joint ventures to plants with no foreign investment. Foreign investment negatively affects the productivity of domestically owned plants. The net impact of foreign investment, taking into account these two offsetting effects, is quite small. The gains from foreign investment appear to be entirely captured by joint ventures. Foreign direct investment (FDI) inflow has been a key concern for Bangladesh to obtain additional support for the economic development. The Government of Bangladesh continuously competing with other South Asian countries and putting more effort to increase the number of FDI inflows in the country. **Jadhav, P. (2012)** discussed that from the country's perspective, the constant increasing rate of economic growth shows a positive outcome of FDI inflow. However, the Bangladesh is still not performing up to the mark to pull enough FDI inflows to its potential. **Athukorala, P. P. A. W. (2003)** discussed about the major determinants and factors affecting FDI inflows in Bangladesh. Among those determinants and factors, infrastructural facility is considered as the most important to affect FDI inflows and economic growth. FDI inflow is fundamentally depending upon infrastructural facilities to achieve its desire success. Foreign investors take this issue very seriously because based on this they can measure their ease of doing business in the host country. **Hossain, A., et al. (2012)** described that despite of providing a large market size, due to having weak and lack of infrastructural facilities, Bangladesh is facing trouble in drawing attention of the foreign investors. In order to make the infrastructural facilities happen, it is highly required to organize each of the systems under of it. **Temiz, D., et al. (2014)**, discussed about the weak infrastructures in Bangladesh such as transport and communication, power and energy, education system, and governance services. Improvement in one of these systems cannot provide valuable positive changes on FDI inflows. It requires

improvement in all the weak systems to grasp multinational companies and attract foreign investors.

5. Objective of the Study

The main objective of this paper is to show the trend of FDI and economic growth that is current scenario of FDI leading to economic growth of Bangladesh. The specific objectives (Malhotra, 2007) are: (a) To identify current trend of FDI and economic growth of Bangladesh, (b) To present data relating to FDI and economic growth, (c) To examine relationship associated with FDI and economic growth, (d) To figure out major challenges of the government on attracting foreign direct investment and keeping consistent economic growth (e) To provide some suggestions for increasing FDI at the same time sustainable economic growth in Bangladesh in the future.

6. Methodology

This study is mainly based on secondary data. It was to analyze and relate to FDI and economic growth of Bangladesh. This is why EPZ and Non-EPZ wise FDI trend and potential sectors were analyzed based on past data during the years 2008 to 2018. Basically, secondary data were collected from different authentic sources like websites (Bangladesh Investment Development Authority, Bangladesh Bureau of Statistics, Bangladesh Bank, Asian Development Bank, International Monetary Fund, World Bank etc.), research articles, newspapers etc. On the other hand, primary data were collected from focused group discussion to identify the challenges toward FDI inflows and economic growth of Bangladesh. Besides, few key information interviews were taken for collecting primary data to enrich this study with specialized views of experts in this field.

7. Data Presentation & Discussion on the Findings

7.1 FDI Statistics

Foreign Direct Investment in Bangladesh increased by 1706 USD Million in 2017. Foreign Direct Investment in Bangladesh averaged 1195.10 USD Million from 2008 until 2017, reaching an all time high of 1726 USD Million in 2013 and a record low of 748 USD Million in 2008.

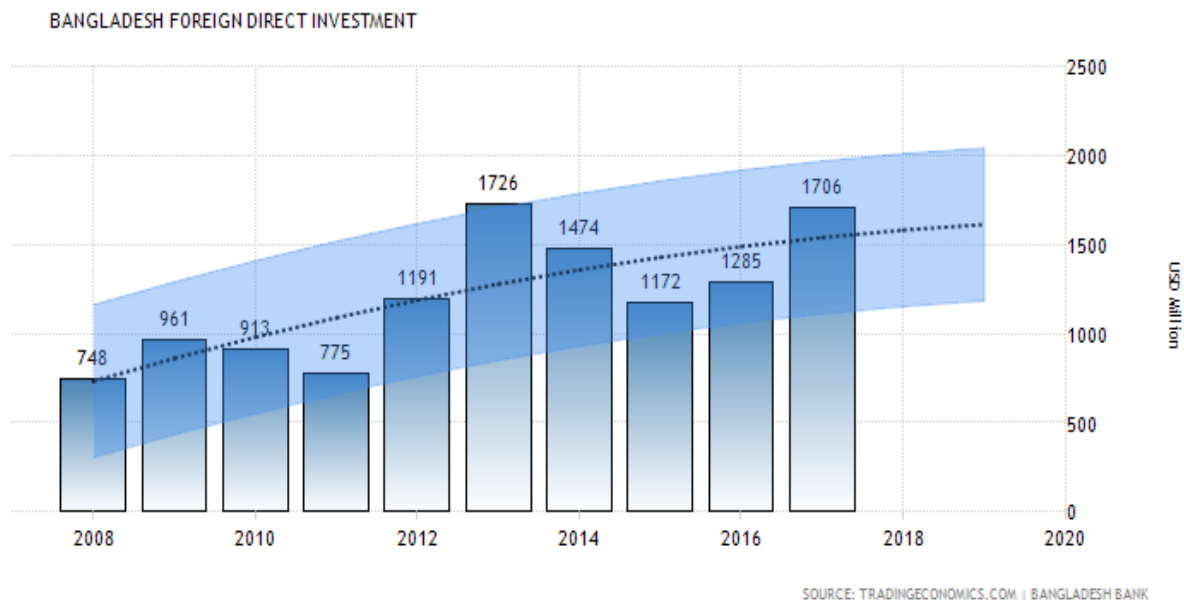
Figure-1 (Bar-chart 1): Trend of Foreign Direct Investment in Bangladesh



Source: Tradingeconomics.com: Bangladesh Bank

Foreign Direct Investment in Bangladesh is expected to be 1575.50 USD Million by the end of this quarter, according to Trading Economics global macro models and analysts expectations. In the long-term, the Bangladesh Foreign Direct Investment is projected to trend around 1900.00 USD Million in 2020, according to our econometric models.

Figure- 2 (Bar-chart 2): Forecast on Foreign Direct Investment of Bangladesh in 2020



Source: Tradingeconomics.com: Bangladesh Bank

Figure- 3 (Table 1): Status of FDI Enterprises by EPZ and Non-EPZ areas during FY 2017¹

| Area | No. of Enterprises | | | | No. of Respondent enterprises | | | | No. of Non Respondent enterprises | | | |
|--------------|--|--|--|--|---|---|---|---|--|--|--|--|
| | Jul-Sep 2016 | Oct-Dec 2016 | Jan-Mar 2017 | Apr-Jun 2017 | Jul-Sep 2016 | Oct-Dec 2016 | Jan-Mar 2017 | Apr-Jun 2017 | Jul-Sep 2016 | Oct-Dec 2016 | Jan-Mar 2017 | Apr-Jun 2017 |
| EPZ | 262 (100.00 %) | 276 (100.00 %) | 277 (100.00 %) | 281 (100.00 %) | 234 (89.31 %) | 249 (90.22 %) | 243 (87.73 %) | 248 (88.26 %) | 28 (10.69 %) | 27 (9.78 %) | 34 (12.27 %) | 33 (11.74 %) |
| Non-EPZ | 1564 (100.00 %) | 1680 (100.00 %) | 1761 (100.00 %) | 1823 (100.00 %) | 1257 (80.37 %) | 1297 (77.20 %) | 1329 (75.47 %) | 1380 (75.70 %) | 307 (19.63 %) | 383 (22.80 %) | 432 (24.53 %) | 443 (24.30 %) |
| Total | 1826 (100.00 %) | 1956 (100.00 %) | 2038 (100.00 %) | 2104 (100.00 %) | 1491 (81.65 %) | 1546 (79.04 %) | 1572 (77.13 %) | 1427 (77.38 %) | 335 (18.35 %) | 410 (20.96 %) | 466 (22.87 %) | 476 (22.62 %) |

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

The country's overall FDI inflow (net) decreased by US\$ 480.63 million or 32.75% during January-June, 2017 over the previous period, July-December, 2016 due to mainly significant decrease of equity capital (net) by US\$ 482.66 million or 64.81%. FDI inflows (net) in Equity capital arrived to US\$ 262.04 million during January-June, 2017 which was decreased by US\$ 482.66 million or 64.81% compared to July-December, 2016 (US\$ 744.70 million). Whereas in July-December, 2016 Equity capital (net) was increased by US\$ 578.02 million or 346.78% compared to January-June, 2016 and a decrease of US\$ 172.19 million or 50.81% during January-June, 2016 compared to July-December, 2015 (Table-2).

Figure- 4 (Table 2): FDI Inflows (Net) by Components (FY 2016 to FY 2017)².

| Component | FY 2016 | | | | | | FY 2017 | | | | | |
|---------------------|-----------------------------|-----------------------------|------------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|------------------------------|-----------------------------|-----------------------------|-----------------------------|
| | Jul-Dec | | | Jan-Jun | | | Jul-Dec | | | Jan-Jun | | |
| | Jul-Sep | Oct-Dec | Total | Jan-Mar | Apr-Jun | Total | Jul-Sep | Oct-Dec | Total | Jan-Mar | Apr-Jun | Total |
| Equity Capital | 224.91 (37.61) | 113.96 (21.09) | 338.87 (29.76) | 90.29 (21.99) | 76.39 (15.94) | 166.68 (19.27) | 258.52 (37.61) | 486.18 (21.09) | 744.70 (29.76) | 140.35 (28.30) | 121.69 (24.77) | 262.04 (26.55) |
| Reinvested earnings | 244.38 (40.86) | 304.71 (56.38) | 549.09 (48.23) | 299.86 (73.02) | 305.50 (67.24) | 605.36 (69.98) | 294.55 (40.86) | 315.48 (56.38) | 610.03 (48.23) | 319.30 (64.40) | 323.67 (65.89) | 642.97 (65.14) |
| Intra-company Loans | 128.79 (21.53) | 121.78 (22.53) | 250.57 (22.01) | 20.53 (4.99%) | 72.43 (16.82) | 92.96 (10.75) | 60.92 (21.53) | 52.07 (22.53) | 112.99 (22.01) | 36.19 (7.30%) | 45.89 (9.34%) | 82.08 (8.31%) |
| FDI inflows (net) | 598.08 (100%) | 540.45 (100%) | 1138.53 (100%) | 410.68 (100%) | 454.32 (100%) | 865.00 (100%) | 613.99 (100%) | 853.73 (100%) | 1467.72 (100%) | 495.84 (100%) | 491.25 (100%) | 987.09 (100%) |

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

FDI inflows (net) in Reinvested earnings reached to US\$ 642.97 million during January-June, 2017 which was increased by US\$ 32.94 million or 5.40% compared to July-December, 2016 (US\$ 610.03 million). While in July-December, 2016 reinvested earnings (net) was increased by US\$ 4.67 million or 0.77% compared to January-June, 2016 and an increase of US\$ 56.27 million or 10.25% during January-June, 2016 compared to July-December, 2015 (Table-2). FDI inflows (net) in Intra-company loans arrived to US\$ 82.08 million during January-June, 2017 which was decreased by US\$ 30.91 million or 27.36% compared to July-December, 2016 (US\$ 112.99 million). Whereas in July-December, 2016 intra-company loans (net) was increased by US\$ 20.03 million or 21.55% compared to January-June, 2016 and a decrease of US\$ 157.61 million or 62.90% during the period January-June, 2016 compared to July-December, 2015 (Table-2).

7.2 Growth Rate Statistics

The Gross Domestic Product (GDP) in Bangladesh expanded 7.11 percent in 2016 from the previous year. This indicator has been discontinued and replaced by Bangladesh GDP Annual Growth Rate. GDP Growth Rate in Bangladesh averaged 5.69 percent from 1994 until 2016, reaching an all time high of 7.11 percent in 2016 and a record low of 4.08 percent in 1994.

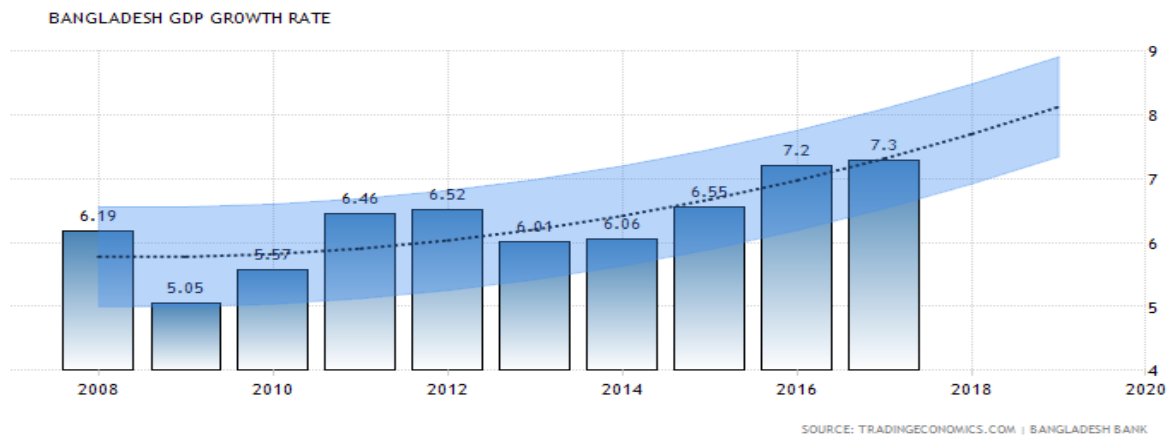
Figure- 5 (Bar-chart 3): GDP Trend 2008 to 2018



Source: Tradingeconomics.com: Bangladesh Bank

Bangladesh is considered as a developing economy. Yet, almost one-third of Bangladesh's 150m people live in extreme poverty. In the last decade, the country has recorded GDP growth rates above 5 percent due to development of microcredit and garment industry. Although three fifths of Bangladeshis are employed in the agriculture sector, three quarters of exports revenues come from producing ready-made garments. The biggest obstacles to sustainable development in Bangladesh are overpopulation, poor infrastructure, corruption, political instability and a slow implementation of economic reforms. This page provides - Bangladesh GDP Growth Rate - actual values, historical data, forecast, chart, statistics, economic calendar and news. Bangladesh GDP Growth Rate - actual data, historical chart and calendar of releases - was last updated on September of 2018.

Figure- 6 (Bar-chart 4): GDP Forecast in 2020



Source: Tradingeconomics.com: Bangladesh Bank

GDP Growth Rate in Bangladesh is expected to be 7.20 percent by the end of this quarter, according to Trading Economics global macro models and analysts expectations. In the long-term, the Bangladesh GDP Growth Rate is projected to trend around 6.80 percent in 2020, according to our econometric models.

8. Conclusion and Recommendations

In Bangladesh it is observed that attracting FDI into backward and forward linkage industries including testing laboratories, common facility centers, industrial park development and international value chain linkage industries through preparing complete project profile (PP) and approaching relevant multinational companies (MNCs), establishing an investment promotion agency other than the Board of Investment (Regulator). Declaring a long range of fiscal, nonmonetary incentive or having competitive advantage in factors of production is insufficient to get FDI into a country. Increasing government's investment (could be under PPP modality) is to achieve trust of foreign investors, functional one stop investment service center to reduce investment relevant harassments. It is also seen that attracting investment in infrastructure development, it is trying to emphasizing on the job training to facilitate technology transfer and employment generation. To some extent, basically Bangladesh requires to increasing power generation and other utilities (like gas, water) supplies to the manufacturing entity to attracting cluster based investment to upgrade existing SME clusters as well as Emphasizing on labor intensive, import substitute, and export oriented industries. The study concludes that Bangladesh having experienced that a certain percentage of growth is contributing by FDI due to lack of proper steps taking by the government to foreign investors. But at this moment, it can be said that there is apposite trend to increase FDI and

economic growth in the economy of Bangladesh. Therefore, different steps should be taken by the government immediately to increase both FDI and economic growth of Bangladesh. Government has to be proactive for creating and maintaining an FDI friendly business environment in Bangladesh. To get satisfactory amount of FDI, Bangladesh has to complete its home work like identifying potential sectors, preparing specific project proposal, approaching potential FD investor companies etc. Dedicated agency is needed to promote investment instead of regulator of investment. Ensuring hassle free power and utilities supply, smooth registration and certification mechanism has a direct linkage to get foreign or inspire local investment. Maintaining peaceful political and reliable legal environment is equally important to get foreign investment in a country. Bangladesh has to increase the amount of FDI attraction at any cost. Otherwise, it would be tough to achieve and maintain a double digit GDP growth. Without achieving double digit growth rate we cannot meet vision 2021 in time. Currently the figure of FDI investment is manipulated with reinvestment of locally earned profit. If we drop the locally earned profit amount as FDI then the figure during last few years is very dissatisfactory. So this is the pick time to concentrate upon it and start new drives for increasing FDI inflow and economic growth of Bangladesh.

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