

FDI and Bangladesh: A Study of South Asian Territories

^{1*} Syed Moudud-Ul-Huq, ² Md. Abdul Mannan Khan, ³ Md. Habibur Rahman

¹ School of Management, Huazhong University of Science and Technology, Wuhan, Hubei, P. R. China

² Department of Accounting and Information Systems, Bangabandhu Sheikh Mujibur, Rahman Science and Technology University, Gopalganj, Bangladesh

³ Department of Management, Govt. M. M. Ali College, Kagmari, Bangladesh

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ABSTRACT:

Foreign Direct Investment plays a crucial role in the economy of developing countries like Bangladesh through accelerating Gross Domestic Product (GDP), export and domestic investment followed by overall economic growth. The present scenario of FDI in Bangladesh is not still satisfactory enough but given the availability of abundant resources, skilled and cheap labor forces, a stable political atmosphere, effective monetary and fiscal policy, improvement of infrastructure and long term strategic planning to stimulate FDI might be able to make the condition favorable to attract foreign investment in Bangladesh. South Asian countries need to improve their domestic investment, exports and infrastructure facilities, along with more foreign investment, to achieve higher growth. This report analysis of FDI flows to south Asian countries reveals that there has been an increasing trend of FDI into South Asian countries. Findings analysis suggest that FDI has a positive impact on export growth through its positive spillovers for South Asian countries FDI in South Asia is mostly concentrated in manufacturing and services. Despite some policies reforms, Bangladesh could not attract handsome flow of FDI as yet. Furthermore, the lion's share of FDI is being repatriated. The main focus of this paper is to reveal how attractive the position of Bangladesh in south Asian countries. We find from the report that Bangladesh hold the second position in FDI but not in attractive position. The paper also analyses the problems and prospects of FDI in Bangladesh. The study also provides some remedies to solve the problems.

Keywords: Foreign Direct Investment (FDI), South Asian countries, Economic development, Prospects, Problems

INTRODUCTION

As a developing country, Bangladesh needs FDI for its ongoing development Process. Foreign Direct Investment (FDI) is considered as one of the vital ingredients for overall development process of a developing country like Bangladesh. Industrial development is an important pre-requisite for economic growth of a developing country. Bangladesh is basically a

country of agrarian economy. For her economic development, industrial economy is imperative. So Bangladesh is gradually moving from agrarian economy to industrial economy. In the age of globalization, it has become a burning issue to exchange views, ideas, capital and human resources. Government of Bangladesh is trying to create a favorable investment

*Corresponding Author, Email: moudud_cu7@yahoo.com

environment through introducing economic policies, incentives for investors, promoting privatization and so on. Therefore, the contribution of FDI is necessary in the enhancement of a country's economic growth. It is a potent weapon for developing the economy and achieving the country's socio-economic objectives. The current issue of the Bangladesh Economic Update focuses on the magnitude, dynamics, sectorial distribution, and country-wise sources of FDI inflow in the country. The flow of foreign direct investment is of utmost importance in the current backdrop of overall slump in investment in the economy in recent days. If FDI falls, it will reduce investment, which in turn will shrink employment generation. These may lead to decline in consumption level and savings will face a downward trend. There would be, as a result, a contagious pressure on the GDP growth of Bangladesh. The climate for investment is determined by the interplay of a whole set of factors: economic, social, political, technological and environmental that has a bearing on the operation of businesses. Foreign direct investment (FDI) has the potential to generate employment, raise productivity, transfer skills and technology, enhance exports, and contribute to the long-term economic development of the world's developing countries. More than ever, countries at all levels of development seek to obtain FDI for enhancing growth and creating jobs. Foreign affiliates of some 64,000 corporations now generate 53 million jobs (The World Bank Research Observer, 2002). FDI is the largest source of external finance for developing countries. The total inflows of FDI have been increasing over the years. In 1972, annual FDI inflow in Bangladesh was 0.090 million USD, and after 33 years, in 2005 annual FDI rose to 845.30 million USD and to 989 million USD in 2006.

FDI played a minor role in the economy of Bangladesh until 1980, a crucial year of policy change. The Government of Bangladesh (GOB) enacted the „Foreign Investment Promotion and Protection Act, 1980“ in an attempt to attract FDI.

Except five industries, which were reserved for the public sector: defense equipment and machinery, nuclear energy, forestry in the reserved forest area, security printing and

railways, FDI was allowed in every sector of the economy. Foreign Direct Investment (FDI) is considered as one of the crucial ingredients for fostering economic development of a developing country. Countries that are lagging behind to attract FDI are formulating and implementing new policies for attracting more investment. Even compared to other South Asian countries, FDI inflow to Bangladesh has traditionally been lower. The future outlook of FDI is grim. Based on the recent years' performance, it is predictable that the share of FDI as percentage of GDP may decline by widening gaps between the projected medium term targets by the government and the actual receipts of the inflow. The FDI inflows as percentage of total investment may decline further. During 1980s, FDI to Bangladesh was very little and mostly focused in banking and a few other sectors. Bangladesh started attracting FDI since 1996 in energy and power sector because of favorable and supportive policies for foreign investment, economic reform as well as unexplored gas and oil resources. In 1972, annual FDI inflow was 0.09 million USD and in 1996, it became 231.61 million USD which rose significantly in 2008 to 1086 million USD which declined to 913.32 million USD in 2010 (source: Bangladesh Board of Investment).

FDI and Its Concepts

The term FDI refers to investment that is made to acquire a lasting interest in an enterprise operating abroad, the investor's purpose being to have an effective voice in the management of the enterprise. In other words, FDI is an international financial flow with the intention of controlling or participating in the management of an enterprise in a foreign country. It is observed that there is serious conceptual ambiguity in understanding FDI. The following definitional aspects of FDI have been cited from World Investment Directory to facilitate a better understanding of the phenomenon.

The two main definitions of FDI are contained in the Balance of Payment Manual (Washington, D.C., IMF, 1997 and 1993) and the second edition of the detailed benchmark definitions of FDI (Paris, Organization for Economic Co-operation and Development (OECD) 1992 and 1996). According to Balance of Payment Manual, FDI 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 management of the enterprise. The foreign entity or group of associated entities that make the investment is termed as 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. In the revised edition of the manual, IMF suggests a threshold of 10% of equity ownership to qualify an investor as a foreign direct investor. According to the benchmark definition of the OECD, a direct investment enterprise is an incorporated or unincorporated enterprise in which a single foreign investor either owns 10% or more of the ordinary shares or voting power of an enterprise or owns less than 10% of the ordinary shares or voting power of an enterprise, yet still maintains an effective voice in management. An effective voice in 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 an enterprise. The World Investment Report 2002 (UNCTAD: 2002:291) has detailed FDI as following: FDI is defined as an investment involving a long-term relationship and reflecting a lasting interest and control by a resident entity in one economy (foreign direct investor or parent enterprise) in an enterprise resident in an economy other than that of the foreign direct investor (FDI enterprise or affiliate enterprise or foreign affiliate). FDI implies that the investor exerts a significant degree of Influence on the management of the enterprise resident in the other economy. Such investment involves both the initial transaction between the two entities and all subsequent transactions between them and among foreign affiliates, both incorporated or unincorporated. FDI may be undertaken by individuals as well as business entities.

Ahmed S. finds that FDI plays an important

role in the process of industrialization and economic growth in the developing countries. Most of the countries in the world have recognized that FDI by Transitional Corporations (TNCs) contributes in many ways to the process of economic growth of the host countries. Since 1980s, there has been a dramatic shift in the attitude of developing countries towards FDI. Kumer, N. (2002) says that Foreign Direct Investment (FDI) has emerged as the most important source of external resources flows to developing countries over the 1990s and has become a significant part of capital formation in the country despite their share in global distribution of FDI continues to remain small or even declining. Ikiara, M.M (2003) proposed that compared to foreign bank loans and portfolio investment, the capital flow into productive capacity, and is largely motivated by prospects of long –term profitability.

Mallampally and Sauvart (1999) states that FDI is widely thought to bring with it, into the host country, a bundle of productive assets, including long-term foreign capital, entrepreneurship, technology, skills, innovative capacity and managerial, organizational and export marketing know-how. Mian, E.U. and Alam, Q. (2006), conducted an important study entitled "Foreign direct investment and development: The Bangladesh Scenario". They mentioned that Foreign Direct Investment is a determinant of the economic growth and development of Bangladesh. Both government ineffectiveness in controlling corruption, improving political stability and

Establishing rule of law and its failure to create physical and policy infrastructure are the most influential determinants for attracting FDI in Bangladesh.

Nature of FDI

- ✓ In all such transactions there is a basic intention to participate in the management of the target company.
- ✓ In most cases it involves a long term commitment, that is, there is no intention to seek quick capital gains.
- ✓ By convention an investment is considered as FDI when it involves acquisition of a minimum of 10% of the paid up equity of the target company.

- ✓ Generally all such investments are accompanied by technology transfers and access to newer markets therefore the partnership involves access to raw materials for the foreign entity and access to technology for the target company.
- ✓ Such investments involve creation of physical assets which generally increase the productive capacity of the target company. This generates employment and consequently economic growth in the host country.
- ✓ Investment by the foreign entity may involve fresh issue of capital or sale of shares held by promoters in the target company. Therefore such transactions are essentially primary market operations.

- ✓ National income
- ✓ Government restriction
- ✓ Exchange rates

Importance of FDI in Bangladesh

In Bangladesh the country's savings-investment gap had been mainly bridged by external economic assistance. However, after the cold war era, the availability of foreign aid is decreasing gradually. As a result, there is now widespread support for the need for FDI in Bangladesh. If the economy is to grow faster, as is being envisaged, there is the need for larger inflow of FDI in Bangladesh with a view to creating jobs for vast labor force, increasing foreign exchange earnings, acquiring new and modern technology and management skills, accelerating overall growth and development of the economy. FDI is thought of contributing to economic development (and therefore poverty reduction) through initial macroeconomic stimulus and by raising total factor productivity and efficiency of resource use in the recipient economy by:

Factors Affecting Foreign Direct Investment

Because Foreign Direct Investment can significantly affect a country's economy, it is important to identify and monitor the factors that influence it. The most influential factors are:

- ✓ Inflation

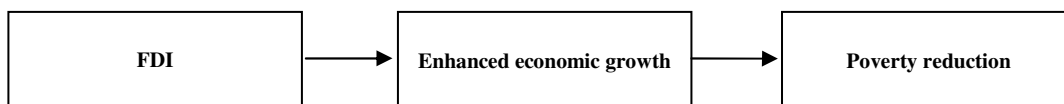
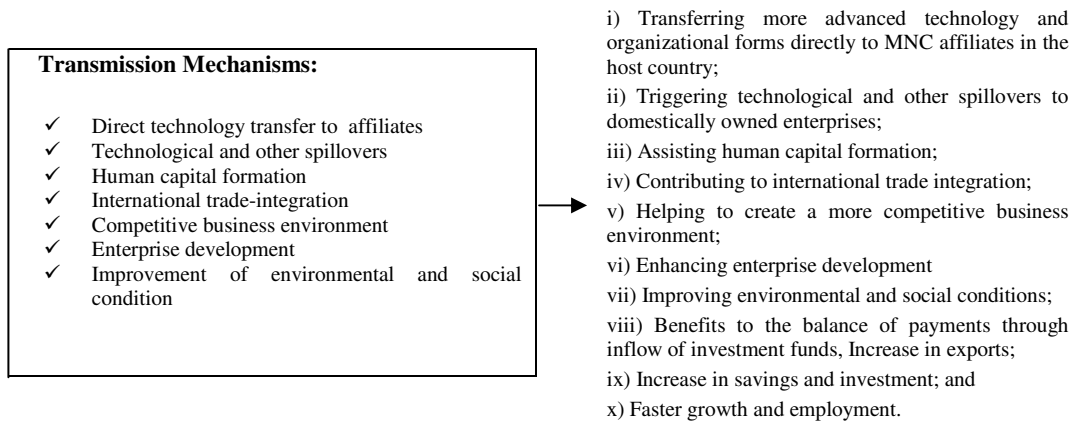


Figure 1: Transmission mechanisms between FDI and poverty reduction

Figure 1 shows transmission mechanisms. They all lead to higher economic growth, which is the most potent tool for poverty reduction in the developing countries.

Literature Review

Numerous studies have been carried out world-wide over the recent past decades to investigate the factors influencing FDI, status, nature or benefits and strategies of FDI. Here, some of them are given priority and make this paper more significant.

Rayhan (2009) analyzed that for attracting FDI, Bangladesh has to reinforce its infrastructure facilities, and improve the quality of services. Furthermore, this study concluded that FDI follows domestic investment, and if the level of domestic investment is low, it will not help FDI to rise at the desired level. Hossain showed that FDI contributes positively to raising imports and exports and can either improve or deteriorate the country's trade balance depending on the relative factors and this study also provides that FDI brings net benefit to Bangladesh. These benefits appear to be important for integrating the domestic economy with the global economy and in the area of technology and skill transfer.

Lall and Narula (2004) suggested that MNEs and FDI may well lead to an increase in productivity and exports, but they do not necessarily result in increased competitiveness of the domestic sector or increased industrial capacity, which ultimately determines economic growth in the long run. FDI does not provide growth opportunities unless a domestic industrial sector exists which has the necessary technological capacity to profit from the externalities from MNE activity.

FDI is now regarded as one of the key indicators of economic health. Thus, there is a global race to attract foreign funds through this route. India too is not behind in this race. Investors are showing their growing confidence in the immediate and medium term prospects of the Indian economy. This section of the paper aims to conduct an in-depth analysis of pattern and direction of flow of FDI in India.

Ibrahim and A. Muthusamy (2014) said that FDI inflow has a positive relationship with exports, inflow and GDP (Gross Domestic Product) made by the country. They also found

that The FDI inflow of the country increases which in turn; the amount of foreign exchange reserve is also increased. Afsana Rahman (2012) realized that FDI is a key success factor for achieving expected economic growth and development. At the same time, FDI has also made a contribution in improving the income level of Bangladesh. There is an increasing trend in foreign investment due to positive effect of the incentives provided and changes in our economic policies.

Sahoo (2006) concluded that there has been a positive change in policies with regard to FDI in all the South Asian Countries. These low-income economies have realized that FDI is not only good debt, but also has a major role in enhancing economic development. Stepping up the economic reform process and making their economies politically stable and free from internal conflict would go a long way toward making South Asia an attractive destination for FDI. However, the image of South Asian countries as corrupt nations, with overprotective labor laws and internal law and order problems, will have to be mitigated to facilitate the entrance of much needed foreign investment. Saha (2012) analyzed and discussed that, the FDI has been playing its role to the economy of Bangladesh since long, but whether the role is fruitful or productive can be a questionable phenomenon because of the fluctuating trend of the same.

Alam (2010) found that In SAARC FDI from outside is more important than in intra-regional investment in most countries (the only exception is Nepal, where Indian investments dominate. The concept of some regions can be applicable to increase intra-regional FDI, there are some regions (ANDEAN, ASEAN, MERCOSUR) have cooperation Schemes which aim to establish regional enterprises by promoting joint ventures. Sultana and Akhter (2013) claimed that though the country has the huge potentiality to attract the FDI but one key factor is making everything in vain, is bad political culture. Zero tolerance of two leading political parties over their decisions, less commitment for the countries development although some changes are occurring and FDI inflow trend is increasing. If the political culture is stabilized i.e. less political chaos then it can create a good business environment and more FDI can be flown to the

country. To investigate how the political culture or situation hampers the FDI inflow of a country needs further research.

Rahman (2011) found the long-run relationship and causality between FDI and trade (export and import) in Bangladesh taking data between 1972 and 2007. For Bangladesh foreign investment has not caused export enhancement and the necessary trade and investment policies are needed to take advantage of such foreign investment for economic growth in general and growth in trade particularly, through accumulation of positive effects of such investments by Taking more macroeconomic variables into consideration and also industry-level data and by applying more rigorous techniques .

Agrawal , Gupta and Mishra (2012) shows in their study that Trade Openness, GDP and Direct Investment have a positive impact on FDI whereas Labor had a negative influence. These results can be justified by studying the political and economic developments over the past 20 years. The negative influence that labor has on FDI can be explained by the fact that many developed countries have become very insecure about outsourcing off. Rajan, Rongala and Ghosh (2008) analyzed in the study that it needs massive investments to sustain high-quality economic growth, particularly in the energy and infrastructure sectors (both physical and social). Policymakers are looking at FDI as the primary source of funds in such cases.

Adhikari shows that despite the growing salience of FDI, not only for traditional business- related activities but also for financing development, LDCs in general have not been able to tap this opportunity. South Asia as a whole has been receiving reasonably good amount of FDI, although the total FDI received by the region represents a meager 2.6 percent of the global FDI inflow. This is based on the —employment intensity index of FDI. Ansari and Ranga (2010) observed that FDI is now regarded as one of the key indicators of economic health. Thus, there is a global race to attract foreign funds through this route. Investors are showing their growing confidence in the immediate and medium term prospects of the Indian economy.

Athreya and Kapur (2001) emphasized that since the contribution of FDI to domestic capital

is quite small, growth-led FDI is more likely than FDI-led growth. Dua and Rasheed (1998) indicted that the Industrial production in India had a unidirectional positive Granger-Casual impact on inward FDI flows. They also concluded that economic activity is an important determinant of FDI inflows in India and not vice-versa. Singer, 1950; Griffin, 1970, FDI and growth postulated a negative association for developing countries. The logic of these studies was that FDI was concentrated on low-priced primary exports to developed countries, and had a negative impact on overall growth.

However, studies by Rodan (1961) and Chenery and Strout (1966) showed that FDI had a favorable impact on productivity and growth in developing countries. Furthermore, Barro and Sala-i-Martin, (1999) and Helpman and Grossman (1991) argue that FDI has long term positive impact by generating increasing returns through technology and knowledge transfers.

Investment policy reviews by UNCTAD provide evidence of benefits of FDI in terms of employment generation, wages, and linkages with local firms, increases in technology intensive exports, range of new products and services, etc. Overall, UNCTAD investment reviews suggest that FDI has a positive impact on growth but that it varies from country to country (UNCTAD, 2003). By and large, previous literature suggests that FDI contributes to growth through capital formation and technology transfer.

Blomstrom *et al.* 1996 and Borensztein *et al.* (1995) along with accumulation of knowledge due to labor training and skill acquisition (Mello, 1999). Therefore, the most frequently cited common benefits of FDI are productivity spillovers for the host economy, resulting in higher growth. The logic is that FDI provides a stock of knowledge capital to less developed or developing economies and make factors of production, namely labor and capital, more productive. Blomstrom *et al.* (1994) find that FDI has a positive impact on growth in rich countries. Further, Borensztein *et al.* (1998) argue that FDI inflows are positively related to per capita GDP growth provided the host country has a highly educated workforce. Alfaro *et al.* (2000) find that FDI positively affects growth in sufficiently developed markets.

Balsubramanyam *et al.* (1996) emphasize trade reforms to create a positive impact of FDI on growth. Based on a disaggregate analysis, Wang (2002) finds that FDI in manufacturing has a significant positive impact on growth. Bende-Nebende and Ford (1998) find that the output of less developed countries responds more positively to FDI. Borensztein *et al.* (1995) explain that because of the transfer of technology, FDI contributes more to growth than domestic investment. Bashir (1999) demonstrates that FDI improves growth in MENA countries, though the effect varies from country to country.

Chowdhury and Mavrotas (2003) find unidirectional causality running from growth to FDI in the case of Chile but find bidirectional causality for Thailand and Malaysia.

Further, FDI boosts the demand for intermediate goods from domestic firms leading to more entry of new firms, an increase in competition, industrial growth and an increase in national welfare (Markusen and Venables, 1999; Haaland and Wooton, 1999). However, in theory, externalities associated with FDI may raise or reduce national welfare. This depends on whether the positive spillover created by FDI is more than the negative externalities (such as the crowding out domestic investment by reducing their profit margins). If the impact of multinationals on the profitability of domestic firms is sufficiently negative, FDI may lower host country welfare. In some conditions, where the multinational demand for labor is weaker than that of existing domestic firms, it may also lower the national welfare. Moreover, the repatriation of profit may drain capital from the host country. Thus, the impact of FDI on national welfare and economic growth can be negative. Carkovic and Levine (2002) find that FDI inflows do not have an independent influence on economic growth. Similarly Ericsson and Irandoust (2001) fail to find any relationship between FDI and growth for Denmark and Finland but find causality from FDI to GDP growth for Norway. Germidis (1977), Haddad and Aitken (1993) and Mansfield and Romeo (1980) find that FDI does not accelerate growth. Further micro level studies by Aitken, Hanson and Harrison (1997), Mello (1997), and Harrison (1996) also fail to lend support for the hypothesis that FDI

accelerates overall economic growth. The potential benefits of FDI are realized only if the local firms have the ability to absorb the foreign technologies and skills (Blomstrom and Kokko, 2003). In fact, it has been 28 empirically proven that FDI is an important tool for development in host countries which have well-developed infrastructure and stable economic conditions (Balsubramanyam, 1998; Blomstrom *et al.*, 1994). On the other hand, big multinational enterprises may drive out local firms because of their financial power and their technological and management superiority.

Empirical evidence on the nature and extent of spillovers from FDI to domestic firms is mixed. The spillover effect depends on the technology gap between foreign and domestic firms. In the Indian context, earlier studies show that FDI has no such positive impact on growth (Dua and Rashid (1998); Chakrabarthy and Basu, 2003). Mello (1997) and Kokko (1996) find a negative relationship between FDI and total factor productivity. However, Sahoo and Maathai (2003) find a positive association between FDI and growth. There are studies finding a positive relationship between productivity growth, liberalization and foreign firms (Basant and Fikkert, 1996; Srivastava, 1991; Kathuria, 1998; 2000). The gap of the report is that little work is one on FDI area and there is no such report done about this topic of research.

Objectives of the Study

As the developing countries are in the process of graduating from being the aid-dependent economy into a trading economy, therefore, the main objective of this paper is to reveal current status of FDI and also analyzes the trends of FDI inflow and repatriation as well as what Bangladesh is doing presently to attract healthy flow of FDI in south Asian countries. The specific objectives of the study are as follows:

- ✓ To measure the status of FDI inflows in Bangladesh as compared to South Asian countries;
- ✓ To study the importance of FDI in Bangladesh;
- ✓ To reveal the relative features of FDI.

- ✓ To outline the major policies attracting FDI in Bangladesh;
- ✓ To compare the inflows and outflows of FDI;
- ✓ To identify the major prospects and problems of FDI in Bangladesh; and
- ✓ To provide some modest suggestions regarding FDI in Bangladesh

RESEARCH METHOD

Scope of the Study

The present study is limited to a total number 5 South Asian country on the basis of FDI. The name of the countries are Bangladesh, India, srilanka, Pakistan, Nepal out of 8 Asian country have been selected for the study.

Data Collection Methods

The study is the outcome of secondary data. The secondary data is collected from different websites, journals, books and newspapers. By using these data, the study at first has figured out the present condition of FDI of Bangladesh. Thereafter, these data were analyzed to assess the impact of foreign direct investment in the economic development of Bangladesh. Lastly, some policies are suggested for the efficient and useful utilization of FDI by removing existing obstacles to

Achieve the desired level of economic development for the country.

Data Analysis and Interpretation

The collected data were analyzed and interpreted critically by the authors in order to make the study more effective, valuable & useful to the readers. On the basis of the analysis and the interpretation, the authors have developed the present report.

FINDINGS AND ANALYSIS

Current position of FDI in Bangladesh

Bangladesh is in the process of transition from a predominantly agricultural economy to a modern economy there has been a considerable change in global flows of trade and finance including a surge in FDI. It is argued that more open trade policies are associated with the presence of foreign firms and economy wide technological and productivity gains in developing countries like Bangladesh. The trend of Inflow of FDI in Bangladesh has increased

over the 1980s as compared to earlier periods and this same momentum continues in 1990s as well. During the period of 1977-2010, total inflows of FDI were USD 8927.9 million, among which the total inflows of FDI during 2006-2010 was USD 4158.63 million. In 1977, this inflow was USD 7 million and in 2008, annual FDI reached to USD 1086.31 million. Unfortunately, there was a declination in inflows of FDI in 2010 which was USD 913.32 million (Source: Survey Report, Statistics Department, Bangladesh Bank). Bangladesh has attracted USD 913 million foreign direct investments (FDI) in 2010 calendar year, a leap by 30 per cent. This upgrades the country's position to 114 from 119 out of 141 nations in the World Investment Report (WIR). During this period the telecom sector received USD 360 million FDI, the manufacturing sector received USD 238 million in investment from abroad, USD 145 million in the textile and clothing sector, while leather and leather products got USD 46 million. (The financial Express, 27 July, 2011). It is to be noted here that FDI inflow to Bangladesh has traditionally been lower, even compared with other South Asian countries. Considering FY 1996-97 as the base year, the statistics reveals that FY 2011-12 might be a net FDI receipt of USD 806.52 million. If the current trend of FDI inflow persists, the country might receive USD 888.96 million of FDI in FY 2014-15 and growth rate of FDI might be only 3.19 percent. There was a significant jump from FY 2003-04 to FY 2004-05 but after that, the incremental growth rate is neither significant nor adequate. The actual FDI recorded US\$ 768.7 million in FY 2007-08. During FY 2008-09; the actual FDI recorded US\$ 960.6 million, which was higher than the previous fiscal year. The key feature of this increasing flow of investment during FY 2008-09 was a favorable investment environment and political stability. In FY 2009-10 (up to December 10) the actual FDI recorded US\$ 342.2 which is lower than the previous fiscal year because of world economic recession (figure 2). The figure also shows an inconsistent proceeding of FDI inflows during the period. In 1999 there was a sudden decline in the FDI and the falling trend continued for many reasons again in 2001, 2002 and 2003. Serious political unrest during the period discouraged foreign investment and it took quite some time to regain

the confidence of foreign investors. There were also some other factors that force this declination. The FDI inflow was on the steady rise from 2003 to 2005. It rose to US\$ 1086.3 million in 2008 but slumped to US\$ 700.16 in 2009 and again increased to \$913.32.

Current status of FDI in India

Foreign investment plays a significant role in development of Indian economy. Foreign direct investment (FDI) is a major source of non-debt financial resource for the economic development of India. Foreign companies invest in India to take advantage of cheaper wages, special investment privileges like tax exemptions, etc. For a country where foreign investments are being made, it also means achieving technical know-how and generation of employment. The continuous inflow of FDI in India, which is now allowed across several industries, clearly shows the faith that overseas investors have in the country's economy. The Indian government's policy regime and a robust business environment have ensured that foreign capital keep flowing into the country. According to a recent report by global credit rating agency Moody's, FDI inflows have increased significantly in India in the current fiscal. This, according to Moody's, is due to India's current pro-growth policies. Net FDI inflows totaled US\$ 14.1 billion in the first five months of 2014-15, representing a 33.5 per cent increase from the same period in 2013-14. Total FDI inflows into India in the period April 2000–November 2014 touched US\$ 350,963 million. Total FDI inflows into India during the

period April–November FY15 was US\$ 18,884 million. Mauritius is again emerging as the largest source of FDI in India, accounting for an inflow of US\$ 83,730 million in the April 2000–November 2014 period. This is attributed to contribution from service sector, computer software, telecommunication, real estate etc. India's Foreign Direct Investment (FDI) policy has been gradually liberalized to make the market more investor friendly. The results have been encouraging. These days, the country is consistently ranked among the top three global investment destinations by all international bodies, including the World Bank, according to a United Nations (UN) report. For Indian economy which has tremendous potential, FDI has had a positive impact.

FDI inflow supplements domestic capital, as well as technology and skills of existing companies. It also helps to establish new companies. The flows of FDI in India shows a positive trend from the year 2005 to 2008 but it was little bit stagnant during 2008 to 2009 (figure 3). After recovering of stagnant situation now it is again increasing.

Current Status of FDI in Nepal

Nepal succeeded in attracting foreign direct investment inflow worth \$95.49 million in 2011, which is \$8.75 million more than the \$86.74 million it was able to attract a year ago, according global report. With more foreign direct investment inflow, the country has also improved its ranking in UNCTAD's World Investment Report 2012.

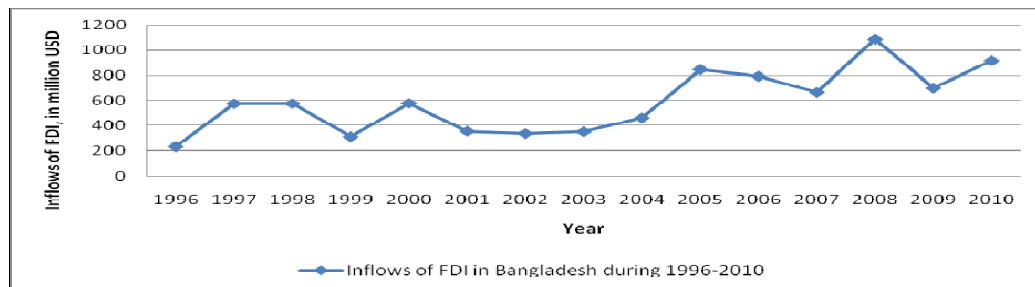


Figure 2: The trend of FDI inflows in Bangladesh during 1996-2010

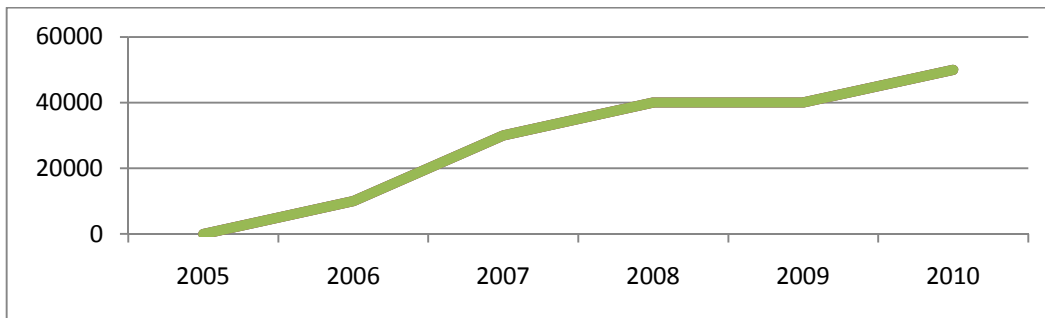


Figure 3: Trend of FDI inflows in India

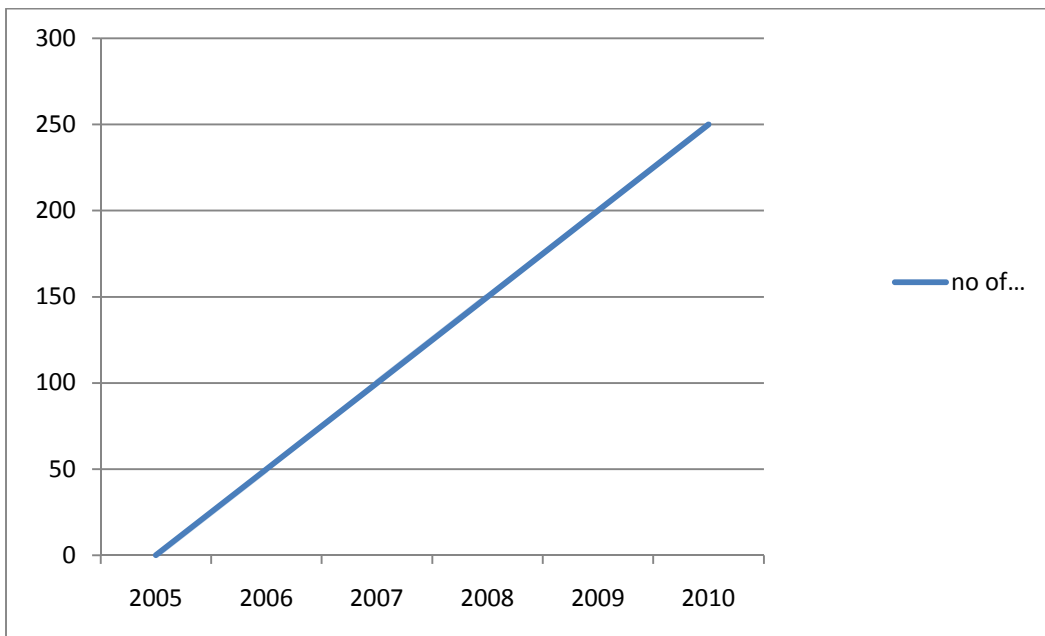


Figure 4: Flows of FDI in Nepal

According to World Investment Report 2012, FDI suffered a setback in the recent past due to global financial crisis, followed by the ongoing debt crisis. Although global FDI flows exceeded the pre-crisis average in 2011, reaching US\$1.5 trillion, they still remained some 23 percent below their 2007 peak (figure 4). Buoyed by the growth in FDI inflow into the largest economy of the region (India), South Asia witnessed a robust growth of 23 percent in 2011 compared to the previous year. However, Nepal remains one

of the worst performers in the region despite robust growth of 125 percent attained in 2011 according to the UNCTAD data. 5 In terms of the FDI potential index, Nepal ranks the lowest in the region, i.e., 175 out of 182 countries ranked globally. On the contrary, if we look at the country-level data for FDI approval as provided in Figure 1, the picture does not look that bleak, in particular from 2006/07 onwards, which coincided with the end of the armed conflict.

Current FDI Status of Pakistan

The decline in FDI in Pakistan after 2008 (figure 5) was mainly due to deteriorated law and order situation, political instability, energy crisis, weak economic activity along with global recession. A detailed analysis of FDI reveals that major decline was recorded in telecommunication and oil and gas exploration sectors. The decline in telecom is obvious as this sector has already reached a saturation point in the country. In case of the oil & gas exploration, a growing circular debt and the deteriorating law & order situation seem to be the major hurdles in attracting fresh FDI. However, increasing volume of FDI also increases the size of imports and profit repatriation. There is a large body of empirical literature showing positive effects of FDI on receiving country's economy including transfer of technology, employment creation, growth enhancement and tax collection. However, relatively less focused area is related to problems resulting due to FDI inflows in small open economies like Pakistan. FDI inflows in developing countries may cause exchange rate appreciation (Dutch disease), trade and income account balance worsening thus having serious implications for overall balance of payments and foreign exchange reserves.

Current Position of FDI in Sri Lanka

Sri Lanka is focusing on long-term strategic and structural development challenges as it strives to transition to an upper middle-income country. Key challenges include boosting investment, including in human capital, realigning public spending and policy with the needs of a middle-income country, enhancing the role of the private sector, including the provision of an appropriate environment for increasing productivity and exports, and ensuring that growth is inclusive. Sri Lanka seeks to achieve \$4,000 in GDP per capita by 2016, from \$3,280 in 2013, but faces three particular macroeconomic challenges. Sri Lanka will also need to demonstrate sustained commitment to ensuring an attractive investment environment with clear rules of the game applied equally. Sri Lanka's economy depends on FDI to

bring in innovation. The import of FDI is further underscored by the country's limited domestic savings rate, brought about largely by its demographic trends. Contrary to most economies in South Asia, Sri Lanka does not have a demographic dividend: by 2036, more than 22 percent of the population will be over 60, and there will be 61 dependents per 100 adults. Increases in the labor force, employment rates and productivity will be central to growth. Against the background of an aging society, efficient and well-targeted social assistance will also become more important. Sri Lanka's growth and competitiveness are constrained by a skills gap that has emerged with the changing labor market conditions. Sri Lanka's economy is no longer dominated by the agriculture sector but rather by services, followed by industry and manufacturing. Employment patterns have followed, shifting significantly from agriculture to industry and services. Labor productivity levels need to rise. There is also a mismatch between graduates and private sector needs particularly with regard to "soft skills". Improving the quality of human capital through effective education and skills development is central to Sri Lanka's economic growth and competitiveness and to the government's aspiration of becoming knowledge based economy. However, during the year of 2006 to 2010 the trend of FDI flows increasing (figure 6).

Comparison of FDI Inflows among the South Asia Countries

Economies are listed according to the magnitude of their FDI flows. After comparing of FDI inflows among the south Asian countries we can find that the position of FDI lies in the most top position where the inflow is Range \$10 billion (table 1). Also the second position is captured by Bangladesh (table 1) and Pakistan and they are between \$1 to 9.9 billion. Sri Lanka, Maldives are between the range of \$ 0.10 to 0.9 billion. Again Nepal, Afghanistan and Bhutan are from Range: \$below to Range: \$ 0.01.

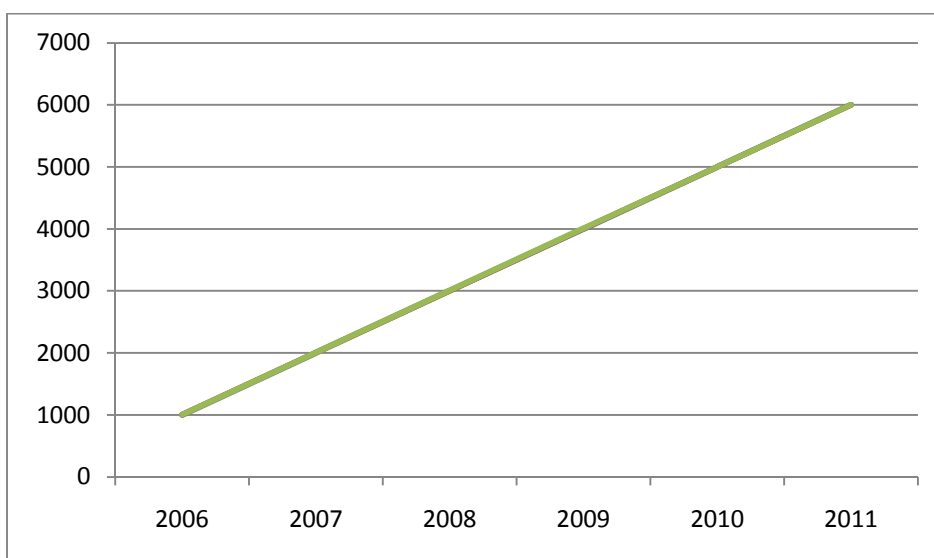


Figure 5: FDI inflows in Pakistan

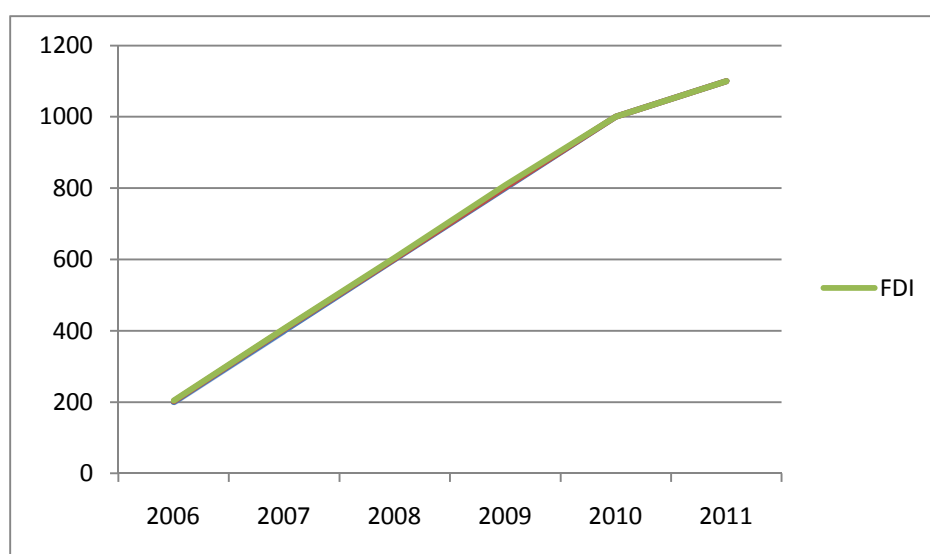


Figure 6: FDI inflows in Sri Lanka

Table 1: Comparison of FDI flows among economies, by range, 2011(South Asian Countries)

Range: \$10 billion	Inflow	Out flow
\$ 10 billion	India	India
\$1 to 9.9 billion	Pakistan, Bangladesh	
\$ 0.10 to 0.9 billion	Sri Lanka, Maldives	
Range: \$Below \$ 0.01	Nepal, Afghanistan, Bhutan	Pakistan, Sri Lanka, Bangladesh

Relationship between Exports and FDI of Bangladesh (figure 7)

Relationship between Exports and FDI of India (figure 8)

Relationship between Exports and FDI of Pakistan (figure 9)

Relationship between Exports and FDI of Sri Lanka (figure 10)

Relationship between Exports and FDI of Nepal

(figure 11)

There is positive relation between FDI and exports. It is shown from the above figure that in most of the country if percentages of FDI in GDP increases then Exports also increases but all country have not positive relation with FDI and exports. This relationship also describes that Bangladesh has better position in FDI after India but not in attractive position.

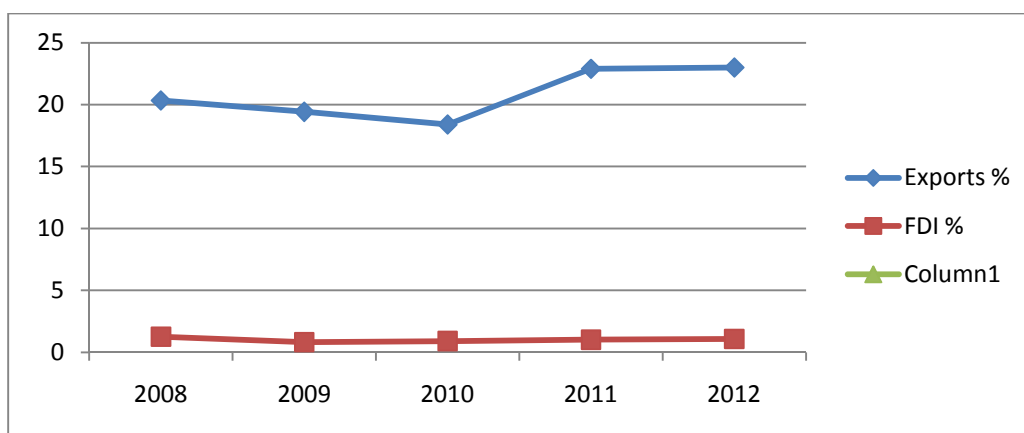


Figure 7: Relationship between exports and FDI of Bangladesh

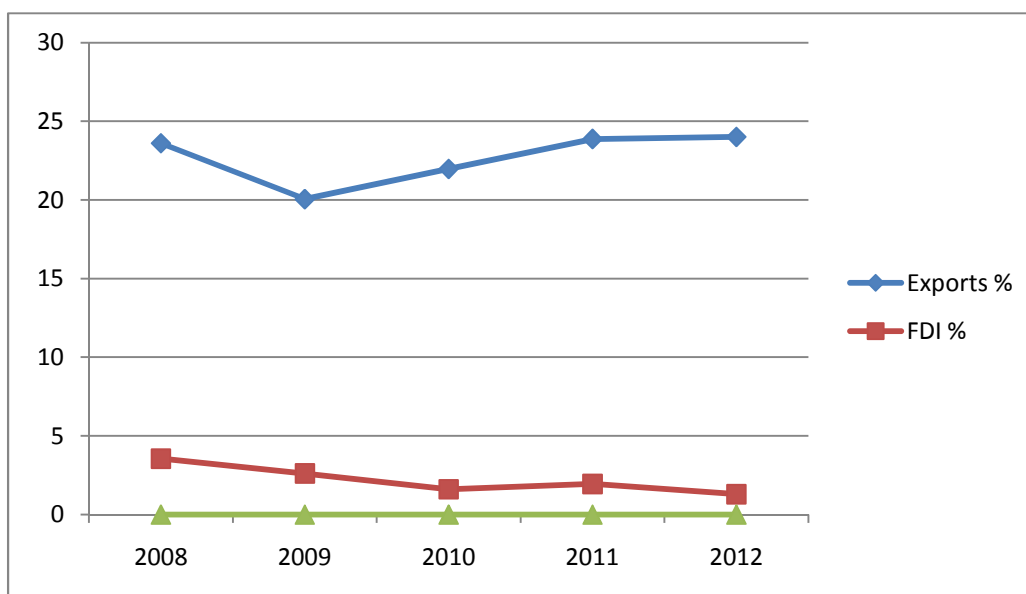


Figure 8: Relationship between exports and FDI of India

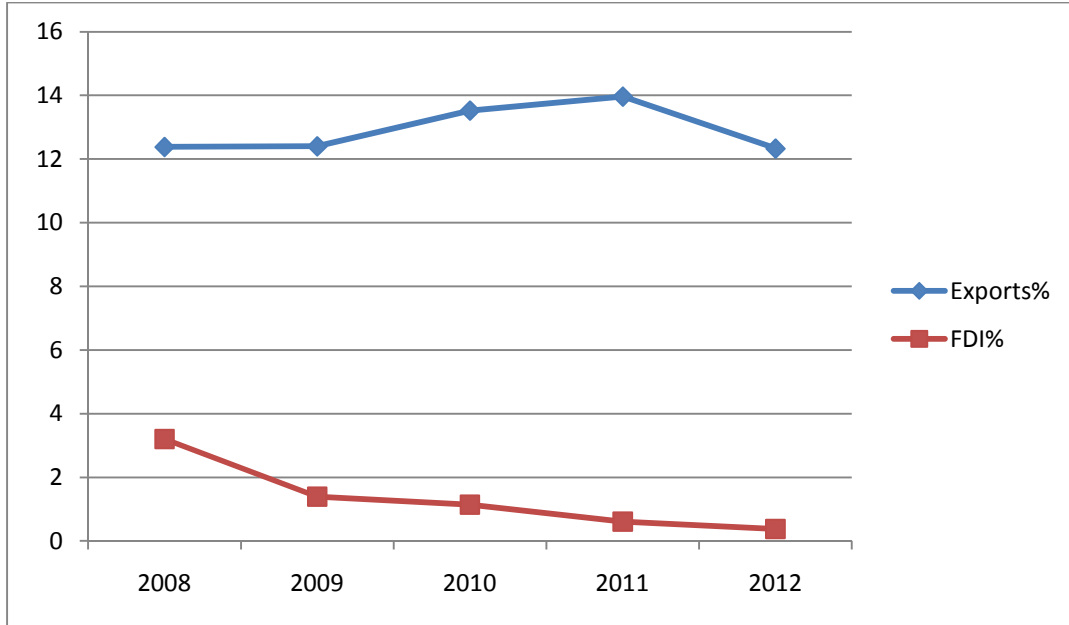


Figure 9: Relationship between exports and FDI of Pakistan

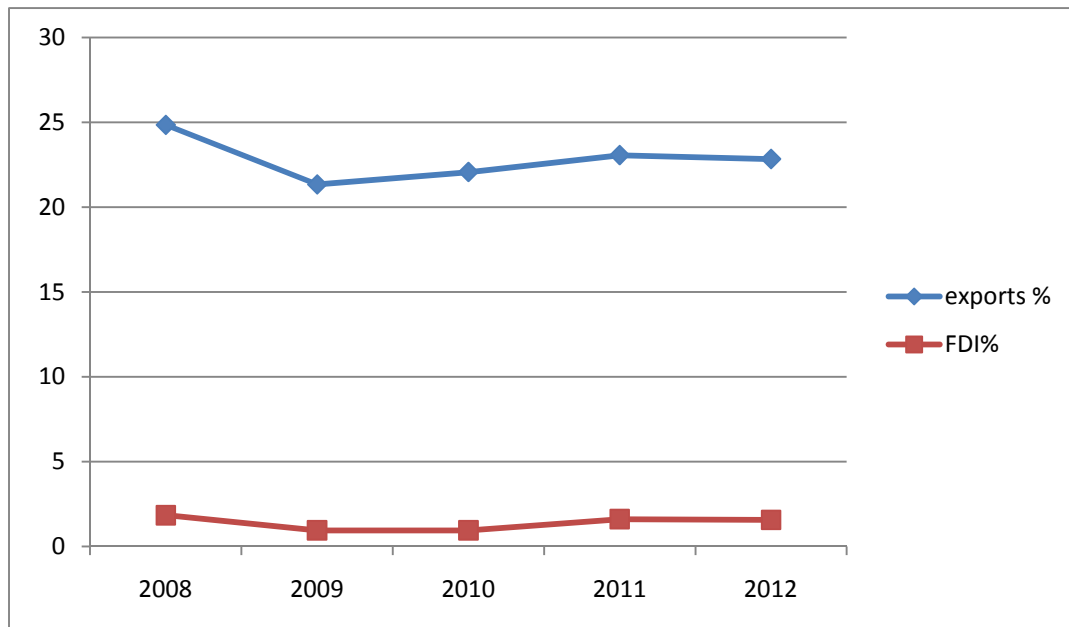


Figure 10: Relationship between exports and FDI of Sri Lanka

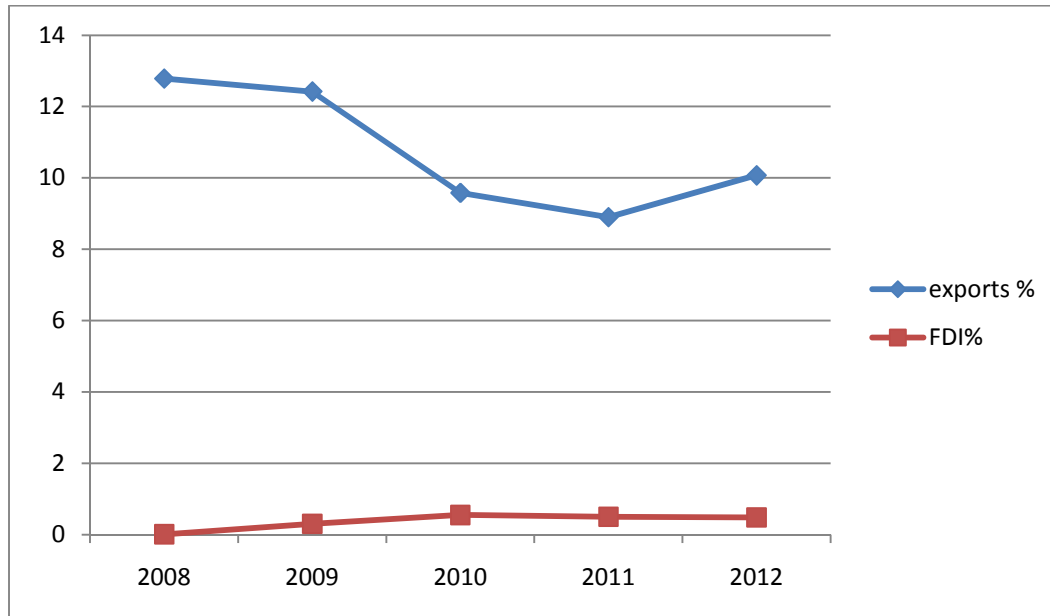


Figure 11: Relationship between exports and FDI of Nepal

Prospects of FDI

In early part of 1990's Bangladesh introduced various reforms for liberalizing its trade and investment policies with necessary protection and alternative incentive package. As a result, potential investors from local and foreign countries have grown substantially in Bangladesh. A number of multinational companies are operating in various sectors in Bangladesh for decades. Among these sectors manufacturing, telecommunication, energy and gas sectors attract the foreign investment most in addition to this, the following sectors or sub sectors are very promising for potential private investment.

Composite Textiles and Linkage Industries

In the last two decades, the RMG (Ready Made Garments) of Bangladesh have grown substantially and now constitute 70% of total exports of Bangladesh. Currently, 2500 RMG units spend approximately 60% of their export earning on import of fabrics. To meet the import requirements of the RMG industries additional investment in spinning, weaving, dyeing,

printing and finishing is required on a top priority basis.

Telecommunication

In Bangladesh, the systems and services of telecommunication have been expanded. Government has already allowed private operation in this sector and has plans to increase the number of fixed telephone lines by 1.6 million. As a result, it has emerged as one of the largest sectors having huge growth potential in the reform environment of telecom sector.

Information and Telecommunication Technology (ICT)

Bangladesh has the scope of profitable investment of ICT. Bangladesh IT firms are interested to join in with foreign investors. In accordance with greater interest with the Government it would be given the highest level of support from the government.

The energy sector of Bangladesh has remained the chief recipient of FDI inflow up to the period 1988-1990. In the 1988-1990 fiscal more than half of the dollar 380 million of the FDI came to the gas sector alone. But, after that

a share of energy and gas sector has sharply declined. This sector was able to attract 10.6% of FDI during January-June 2003. However, given the present utility infrastructure situation of the country and projection faster growth of industries in recent years, energy and gas could be attractive sector for investment in future.

Infrastructure

Bangladesh needs to develop its infrastructure facilities and a service in various sectors and in this context has encouraged private participant with a number of policy initiatives. The potential areas are:

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

Bangladesh has achieved a consistent GDP growth of over 5% in the last decade and never experienced a negative growth. Even Bangladesh sustained growth of over 5% during the recent global economic crisis. In 2009 Bangladesh achieved a 5.9% GDP growth. Various necessary steps like generation of huge number of SMEs, success in microcredit and NGO activities, rapid spread of telecommunications services, record level of foreign remittances, acceleration of export earnings are taking the economy at a higher level of growth. Its investment friendly climate offers generous and attractive packages of incentives for foreign investors like 100% ownership, tax and duty exemptions and others. Actually, Bangladesh has gained a higher ranking than many developing countries in terms of incentive package. A lot of additional fiscal incentives are offered to export oriented industries. The government has created Export processing zones (EPZs) to attract private investment. The government targets foreign investors to invest in EPZ.

The vision is that the unique opportunities in energy and power, infrastructures, manufacturing and knowledge-based sectors will attract substantial investment. Bangladesh has

become a least cost producer in the world with various positive factors like industrious low-cost workforce, strategic location, regional connectivity and worldwide access, strong local market and growth, low cost of energy, proven export competitiveness, competitive incentives, export and economic zones, positive investment climate.

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

Major Obstacles to FDI in Bangladesh

Though Bangladesh has most attractive FDI policies in SAARC region and though there is an evidence of boom of FDI flow in energy sector, the overall scenario of FDI inflow to Bangladesh is not at all satisfactory. The following factors can be identified as major obstacles to FDI in Bangladesh:

- a) Poorly developed socio-economic and physical infrastructure
- b) Lack of skilled people at various levels
- c) Unreliable energy supply
- d) Corruption
- e) Administrative complexity and non-transparency
- f) Poor implementation of existing policies
- g) Low labor productivity
- h) Frequent change in govt. policies
- i) Unhealthy trade union practices
- j) Underdeveloped money and capital markets and regulations on these markets
- k) Less improved seaport facilities & malpractices at the port
- l) Deteriorating law and order situation
- m) Political instability and disturbances
- n) High cost of doing business
- o) Red-tapism and corruption in getting infrastructural facilities
- p) Unfriendly legal system
- q) Complicated bureaucracy

Incentives for Foreign Direct Investment

- ✓ Protection of foreign investment from nationalization and expropriation.
- ✓ Abolition of ceiling on investment and equity share-holding by foreigners.
- ✓ Tax holiday of 5-10 years depending on location of industries and 15 years' tax

- holiday for Private power-generation companies.
- ✓ Accelerated depreciation in lieu of tax holiday is allowed at the rate of 80% per plant for the Year in which production starts and 20% for the following years. Rate of depreciation is 100% for areas specified by NBR.
 - ✓ Concessionary duty at the rate of 5% ad valorem on imported capital machinery and spares for initial installation and for BMR/BMRE of existing industries.
 - ✓ Value Added Tax (VAT) is not payable for imported capital machinery and spares.
 - ✓ Rationalization of import duties and taxes and higher tax and duties for import of goods that are produced locally.
 - ✓ Six months' multiple-entry visa for prospective new investors.
 - ✓ Citizenship by investing a minimum US \$ 500,000 or by transferring US \$ 1,000,000 to any recognized financial institution (non-repatriable).
 - ✓ Permanent resident ship by investing US \$ 75,000 (non-repatriable).
 - ✓ Tax exemption on capital gains from the transfer of shares of public limited companies listed with the stock exchange.
 - ✓ Bonded warehouses and back-to-back letters of credit for export-oriented industries.
 - ✓ Non-resident Bangladeshis will enjoy facilities similar to those of foreign investors and a quota of 10% will be fixed for them in primary public shares.
 - ✓ Avoidance of double taxation with different countries on the basis of bilateral agreements.
 - ✓ Tax exemption and duty-free importation of capital equipment and spares for 100 per cent export-oriented industries.
 - ✓ Facilities for easy repatriation of invested capital, profit, dividend, royalty, technical fee, by foreign investors.
 - ✓ Tax exemption on royalty, technical know-how and technical assistance fees and salaries of foreign personnel working in Bangladesh.
 - ✓ Exemption of income tax up to 3 years for the foreign technicians employed in industries specified in the relevant schedule of the income tax ordinance.
 - ✓ Provision of banking facilities and other utility services on equal footing with local investors.
 - ✓ Protection of intellectual property rights, such as patents, designs and trade-marks and copyright on the basis of bilateral agreements.
 - ✓ Keeping the taka freely convertible for international payments in the current account.
 - ✓ Treatment of re-investment of reportable dividends as new investment entitled to all these incentives.
 - ✓ Protection of foreign investment from nationalization and expropriation.
 - ✓ Abolition of ceiling on investment and equity share-holding by foreigners.
 - ✓ Tax holiday of 5-10 years depending on location of industries and 15 years' tax holiday for private power-generation companies.
 - ✓ Accelerated depreciation in lieu of tax holiday is allowed at the rate of 80% per plant for the year in which production starts and 20% for the following years. Rate of depreciation is 100% for areas specified by NBR.
 - ✓ Concessionary duty at the rate of 5% ad valorem on imported capital machinery and spares for initial installation and for BMR/BMRE of existing industries.

CONCLUSION

Foreign direct investment plays an important role in the economic development of the country. This paper shows that Bangladesh holds good position but the proper attractive position is not happened. It helps in transforming of financial resources, technology and innovative and improved management techniques along with raising productivity. FDI off course might be one of the important sources of financing the economic development. The FDI can bring huge change in any country's economic growth. Especially developing countries like Bangladesh, it is not mere a strategic option but is a significant key factor for the development of a country' In Bangladesh FDI plays a very important role in achieving expected economic growth. FDI flows have been successful in increasing GDP. At the same time, FDI has also made a contribution in improving the income

level of Bangladesh. FDI can ensure Bangladesh to realize higher growth by having the capabilities of using all the resources to the fullest potential. There is an increasing trend in foreign investment due to positive effect of the incentives provided and changes in our economic policies. FDI has positive correlation with GDP, export and private investment.

Limitation of the Study

The present study suffers from the following limitations:

- ✓ The sample size was relatively small as compared to total countries.
- ✓ The study was limited to only one aspect that is FDI of Bangladesh current position in South Asian countries
- ✓ The information that is collected from secondary sources were also little.
- ✓ Some of the sources were not approachable and we lacked from data of that sources.
- ✓ Factors are mostly in qualitative factors in nature and therefore cannot be measured in numerical way.

In analyzing the report we have presented some factors that determine the shape of the flow of FDI. But these are not surely the only factors and many important factors may be omitted from the analysis. And another thing is that the underlying the consequences are that we failed to provide absolute guideline about restructuring policy and some other decisions. The finding of the report is based on some assumed scenario and changes on those scenarios may reshape the future flow of FDI. That is the analysis is situation and time based. The biggest problem we faced in the reporting period is the paradoxical data set.

RECOMMENDATIONS

In order to sustain the economic growth and continue the present status of FDI inflow, Bangladesh needs to maintain some effective steps.

- ✓ The administrative system of the country should be reformed through appropriate and effective measures. The bureaucracy needs to be reorganized. The control of bureaucracy should be minimized.

- ✓ Government should look into the law and order situation to ensure business friendly environment.
- ✓ A social consciousness is much more needed to ensure the rule of law and reduce the various effects of corruption.
- ✓ Both the government and private sector should be taken much more priority in this sector.
- ✓ They need to come ahead in investing in developing the infrastructure.
- ✓ Appropriate policy measures are needed to be developed so that private sector can run smoothly. If both public and the private sector work together in the same view of implementing economic reforms, Bangladesh will surely upgrade her position.
- ✓ Similarly, the further simplified custom clearance procedures can be very helpful in improving the present situation. In order to stimulate domestic and foreign investments, the privatization program can be initiated at large scale.
- ✓ It is important for a developing country like Bangladesh to modernize the laws relating to business and investment. It should be done focusing on international practices.
- ✓ The development of new industrial parks can play a very important role in attracting foreign investment in Bangladesh.
- ✓ The government may consider setting up new EPZs to encourage export oriented investors.
- ✓ Necessary steps should be taken to improve the image of the country abroad.
- ✓ An investment promotion agency needs to provide functions such as investment generation and policy advocacy.
- ✓ Bangladesh needs to strengthen economic and commercial diplomacy in attracting FDI in by rapid globalization and increasing competition.
- ✓ Bilateral relations with potential investor countries should be improved.
- ✓ Bangladesh should take effective steps in accelerating reform measures for banks, other financial institutions and capital market.
- ✓ A good governance and political stability should be ensured.
- ✓ Corporate governance will play a key role in enhancing the investment climate of

Bangladesh. So we should implement corporate governance strongly in financial sector. The rate of corporate taxes is 40% for non-listed companies. It is one of the highest in Asia. This rate should be favorable for investors. Different ministries and organization needs to work in an integrated manner to successfully address issues regarding sectors.

In future, the prospect of the Bangladesh economy would be affirmative if initiatives can be taken to consolidate the proposed reforms. Recently Bangladesh has taken steps to simplify

Various processes to encourage increased FDI. The government, total financial sector and foreign investors must work together to achieve the goal of making Bangladesh a progressive economy by the end of this decade.

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