

Foreign Direct Investment and Sustainable Growth: A Case Study on Bangladesh

by

Razeen Kabir

Adviser Elena Pesavento

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In Loving Memory of My Father

Mahbub Kabir

Whose Moral Values & Lifetime of Dedication to Bangladesh's Public Policy  
Will Forever Be Cherished

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## **Abstract**

There are several benefits of Foreign Direct Investment (FDI) on a macroeconomic level, particularly for a Third World Nation such as Bangladesh, where inflows of foreign investment can expand economic production and growth. FDI provides capital from sources abroad which the country is unable to supply domestically. The inflows facilitate the growth of a number of economic sectors, including industry, manufacturing, infrastructure, and energy. The expansion leads to a rise in the availability of jobs and a fall in the unemployment rate. Consequently, GDP and per capita income increase which, in a developing country, fosters poverty alleviation. In addition, FDI strengthens ties with developed countries that may yield cost advantages in the form of advanced technology transfers and resulting positive externalities. Increased financial associations also lead to stronger capitalistic markets and ideals of corporate governance and social responsibility. On the basis of this intricate link between FDI and growth, the trade regime of Bangladesh has been intensely liberalized to maintain the streams of investments and finances from abroad. These reasons also increase the effort of the Government of Bangladesh in trying to make the country an attractive destination for FDI which in itself has several advantages. The result has validated a reinforced incentive to educate and train the population to make Bangladesh's labor force more competitive through higher national education expenditure. The objective of this study is to conduct a historical and statistical analysis of the relationship between foreign investment inflows and sustainable economic growth.

## Introduction

The objective of this paper is to analyze the effects of foreign direct investment (FDI) and its role in driving economic development in Bangladesh. The study will provide a deeper understanding of the relationship between FDI and development by examining the different factors that have affected both economic factors.

The definition of FDI will be followed in accordance with the United Nations Conference on Trade and Development (UNCTAD) and its World Investment Report 2006<sup>1</sup>, which states that “FDI is 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)”. The Bangladesh Board of Investment (2004) maintains the same definition. FDI consists of three core parts: Equity Capital, Reinvested Earnings, and Intra-company Loans. Equity Capital, as the name suggests, refers to ownership and a foreign investor’s purchase of shares of an enterprise that is in a country other than his own. Reinvested earnings refer to the investor’s share of earnings that are not distributed back to him, i.e. profits that are not given out as dividends but are kept within the firm (or any of its affiliates) as retained earnings. On the other hand, intra-company loans involve debt transactions in the form of short and long-term lending by the foreign parent company to its affiliates (UNCTAD 2006)<sup>2</sup>.

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<sup>1</sup> “Methodical Notes: Definitions and Sources” section

<sup>2</sup> “Methodical Notes: Definitions and Sources” section

FDI inflows to Bangladesh have increased dramatically in recent years and have had some positive influence on development. However, the extent to which FDI has helped this developing nation has been limited. This paper intends to provide plausible explanations of why this has been the case. The structure of this study will constitute a discussion of the history of FDI followed by a discussion of the history of Bangladesh's development. After evaluating the two components separately, the paper will examine the relationship between the two. The evaluation will consist of a theoretical module, based on previous studies, and an empirical module, based on data collected on Bangladesh by the World Bank (2006). Economic concepts will be used to discuss details of how FDI inflows enhance the production capacity of the economy and raise employment levels. This leads to an increase in exports that allows the country to earn foreign currency with which to pay for external debt, import volumes, and further inflows of FDI. The process continues to help sustain economic growth. A series of regressions using the Ordinary Least Squares model will follow to justify the notion that foreign investment significantly contributes to sustainable growth in Bangladesh. The core part of the empirical analyses will consist of time-series data to identify trends of FDI and World Development Indicators (World Bank 2006) since the 1980s, when inflows of foreign capital first emerged in Bangladesh. A number of indicators will be used as metrics of development, including GDP per capita, GDP, telecom distribution, and export volumes. The analyses will examine correlations that may exist between FDI and these development indicators to support the theory.

In focusing on the history of FDI in Bangladesh, the paper will provide an overview of the different policy measures the Government of Bangladesh has

implemented since the country's independence in late 1971. Until 1985, GNP per capita did not manage to grow nearly as fast as other low income countries (Mondal 2003). In trying to overcome this stifled growth, external pressure from foreign donors induced the government to privatize major industries and adopt economic reforms of its investment policies as a means to attract more FDI and boost economic growth (Mondal 2003). Factors that have influenced FDI will also be emphasized, i.e. policy changes, over-valued exchange rates, financial risks, political stability, and tax liabilities.

There are several other reasons why FDI has not produced the expected result with regards to economic development. With a population nearing 150 million in an area of 144,000 square kilometers (CIA 2007), Bangladesh has become one of the most densely populated countries in the world. As a result, development is made even more arduous as any benefits of FDI are quickly absorbed. At the same time, according to the 2006 Corruption Perceptions Index<sup>3</sup> (CPI), Bangladesh is the third most corrupt country in the world. Corruption includes bribes given to government officials by foreign donors, producing a less than pareto-efficient outcome that deters the performance of the economy. Such hurdles impact economic growth, as the issue of FDI misallocation is discussed. Another viable explanation for the slow progress in development includes the capital flight caused by incoming FDI and foreign aid (Quazi 2004). The argument suggests that the investment of foreign savings has replaced the use of domestic savings, as a result of which the latter have moved abroad. On the other hand, exports and foreign investment abroad (FDI outflows) have also produced a number of positive effects on development. Many other issues will be touched upon including the privatization of the

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<sup>3</sup> by Transparency International

Bangladesh economy, the different economic sectors which have attracted FDI, and possible solutions to make FDI more efficient in driving development.

Overall, the purpose of this study is to conduct a historical analysis on FDI and its effect on development in Bangladesh. In doing so, the paper will reveal why the mass inflows of foreign capital have not led to the development that was expected and why Bangladesh continues to lag behind its peers in the nearby South Asian region.

## **Chapter I: The History of FDI and the Bangladesh Government's Investment Policies**

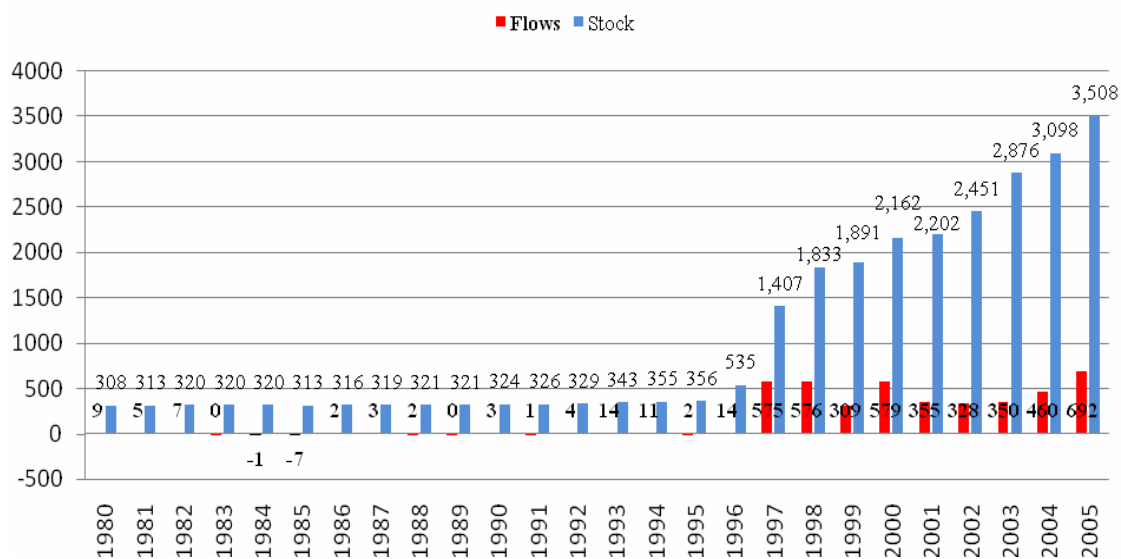
Until the early 1980s, many of the Least Developed Countries, including Bangladesh, were skeptical of the intentions of FDI and perceived it as a tool for promoting foreign interests. Consequently, a wide array of restrictions were imposed to control FDI inflows through regulations on profit and dividend repatriations, limits on foreign equity and capital, and required royalty payments (Sattar 1995). In an increasingly globalized world economy, countries have now lifted such barriers to open their economies and take advantage of the benefits of foreign investment.

FDI inflows in Bangladesh have grown from a trickle during the 1980s (Sattar 1999) to above \$300 million towards the end of 1990s; in 2005, it stood at about \$692 million (UNCTAD 2007). Figure 1<sup>4</sup> illustrates the rising trend of FDI inflows in Bangladesh:

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<sup>4</sup> Based on the database UNCTAD (2007), which also states “FDI inflows comprise capital provided (either directly or through other related enterprises) by a foreign direct investor to a FDI enterprise” and “FDI stock is the value of the share of their capital and reserves (including retained profits) attributable to the parent enterprise, plus the net indebtedness of affiliates to the parent enterprises.”

**Figure 1**  
**UNCTAD: FDI Inward**  
**(in millions, current US \$)**



Many factors have led to this dramatic rise and in order to better understand them, it is necessary to discuss the history of the economic policy implemented by the Government of Bangladesh since the country's independence from Pakistan in 1971.

Immediately after the birth of the sovereign nation, the new government attempted to establish a socialist state and adopted the Nationalization Order of 1972 to foster economic growth. 86% of the industrial sector was brought under government control (Alam 1999), including key industries such as sugar, jute, and cotton textiles (Mondal 2003). The First Five Year Plan was undertaken from 1973 through 1978 and focused on a state directed economy. The nationalized industries, however, were inefficient and the economy experienced low growth. The losses incurred by the public sector and its State Owned Enterprises created a build-up of political pressure and the government initiated more laissez-faire measures to encourage a larger role of the

private sector. Consequently, Bangladesh has undergone a series of policy reforms to induce a more capitalistic economy by progressively increasing funding allocations to the private sector; these reforms include the 1978-1980 Two Year Plan, the 1980-1985 Second Five Year Plan, the 1985-1990 Third Five Year Plan, and the 1990-1995 Fourth Five Year Plan.

Owing to the lack of financial ability, knowledge, and management within the nascent economy of a new nation, the government could not solely rely on the domestic financial market for economic growth. While other low income countries experienced a 3.8% growth of GNP per capita, Bangladesh struggled at 0.4% per year till 1985 (Mondal 2003). To accelerate the development of the economy, foreign investment became a priority and in 1980, the Bangladesh Parliament approved the Foreign Private Investment Act (Alam 1999). FDI, however, rose very little owing to the upheld trade restrictions and the Investment Act of 1989 soon followed to establish the Board of Investment (UNCTAD 2000), the primary objective of which is aimed at attracting and facilitating investment from abroad (Mondal 2003).

Figure 1 demonstrates that the Bangladeshi economy reflected the efforts of the Board of Investment with increases in FDI inflows, particularly throughout the 1990s. It is important to emphasize the years between 1995 and 1998 which saw the sharpest and most sudden rise in FDI flows. This period can be attributed to a variety of factors. During the mid-1990s, numerous foreign enterprises led exploratory research campaigns into the nation's natural gas reserves, which have an estimated capacity greater than 10 trillion cubic feet according to the U.S. Geographical Survey (UNCTAD 2000). Given the world's scarce resources, external pressure finally urged the Bangladeshi government

into liberalizing the energy sector, a move which almost immediately attracted increasing levels of FDI<sup>5</sup>. Concurrently, the government also eased capital controls and reduced its bureaucratic red tape to allow private firms to borrow foreign loans without governmental permission (Alam 1999), thus encouraging more joint ventures with international companies. In 1995, the Bangladesh government opened up the mobile telecommunication industry for private investment, an area which has fostered technology transfers as well as hundreds of millions of dollars in FDI ([www.supro.org](http://www.supro.org)). All these reforms and policies combined to shape Bangladesh into the nation that it is today.

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<sup>5</sup> Based on Mondal (2003)

## **Chapter II: The Current Situation of FDI inflows in Bangladesh**

From a policy perspective, the Bangladesh Board of Investment has taken measures to transform the country into the most liberalized investment regime in the South Asian region (UNCTAD 2000). This is largely reflective of the increasingly capitalistic model of the economy where growth is fueled primarily by the private sector. Thus, foreign enterprises are allowed to reduce associated business risks by undertaking joint ventures with domestic private firms.

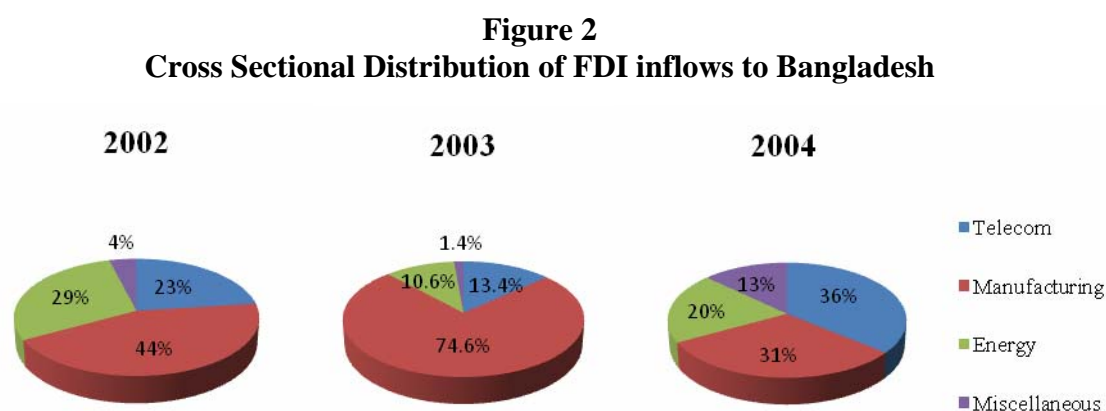
A number of other advantages make Bangladesh a prime destination for FDI. With a 150 million population, the most abundant factor of production is low-cost labor. This attribute makes the country ideal for labor-intensive industries. The densely populated city centers also provide for an untapped, sizeable market (UNCTAD 2000). The only limit to such a market is that the products offered will either only appeal to the upper socioeconomic strata or will have to incorporate low-cost items to appeal to the general population. There is also an abundance of natural resources, such as methane gas, water, coal, and oil ([www.supro.org](http://www.supro.org))<sup>6</sup>. Furthermore, many areas of the Bangladeshi infrastructure remain underdeveloped and this provides a wide array of markets for incoming foreign investment with little or no domestic competition. It is also important to realize that the government has neither the capital nor the resources to expand many areas of its infrastructure and consequently has attempted to open its economy towards foreign capital, particularly in areas such as power plants, construction, transportation, etc. (UNCTAD 2000.) Hence, the country has adopted a sequence of liberalized industrial policy reforms ([www.supro.org](http://www.supro.org)). The government has also established two

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<sup>6</sup> see bibliography for the full website address

export-processing zones (i.e. areas with minimized trade restrictions) in the country's two largest cities, Dhaka and Chittagong (UNCTAD 2000), which account for most of the inward flows of FDI. It is important to note that so far roughly 90% of FDI inflows in Bangladesh have come in the form of equity and reinvestment (Bangladesh Board of Investment 2004) since there is currently no limitation on equity participation for foreign private investment (www.supro.org). About 10% has come in the form of intra-company borrowings. In addition to the Board of Investment, two more bureaucratic bodies keep track of FDI registrations and they include the Bangladesh Export Processing Zones Authority and the Bangladesh Bank.

Figure 2<sup>7</sup> shows the cross-sectional distribution of FDI inflows from 2002 to 2004:



It is important to observe that FDI inflows have increased each of these years and the above only represents the share of FDI each sector has received relative to the other (and not in absolute value). The pie charts express how the dimensions of FDI inflows have changed in recent years. The reduction in FDI shares of manufacturing demonstrates that it is no longer a stronghold for foreign investment and other sectors, such as telecom and

<sup>7</sup> Based on percentages gathered from the Bangladesh Board of Investment 2002, 2003, 2004 respectively.

energy, are gaining prominence as well. The agro-based industry is particularly important since Bangladesh is a sub-tropical delta with very fertile land and is ideal for dairy, poultry, fruits, vegetables, shrimp and fish farms ([www.supro.org](http://www.supro.org)). The smallest, miscellaneous proportions include services in finance, engineering, and computer software.

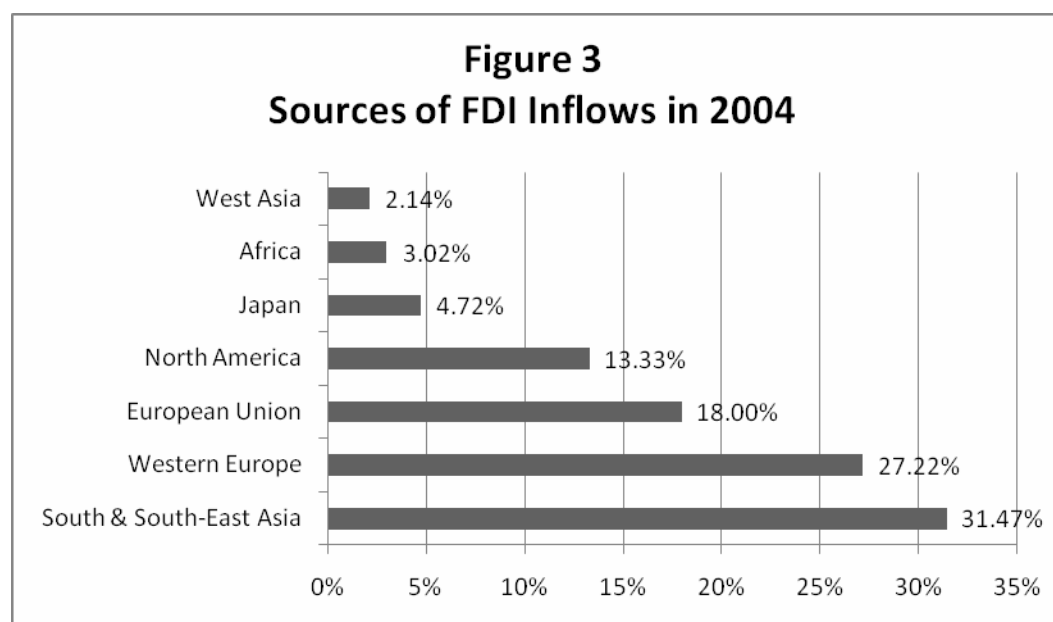
As recently as 2003, the manufacturing sector received the majority of foreign investment inflows. A vital part of this was owing to the success in textiles through the ready-made garments (RMG) industry. The manufacturing sector involves products which fall under sub-categories such as textile, chemicals, agriculture, food, glass, ceramics, leather, rubbery, printing and publication (Bangladesh Board of Investment 2004).

In 2004, however, manufacturing was overtaken by the telecommunications sector as the leading recipient of FDI. Owing to increased privatization efforts by the government, telecom has emerged as one of the fastest growing sectors in the Bangladesh economy. Much of this can be explained by the increased competition between large private corporations that have magnified efforts to attract FDI and attain better technology to optimize profits. At the same time, Grameen Phone's efforts to loan out mobile phones to female operators in remote villages have also increased the demand for foreign investment in telecom and satellite communication technologies.

In addition, the energy sector draws in significant levels of FDI albeit in comparatively lower quantities. The country's natural gas reserves partially explain this. Another factor is the country's difficulty in generating electricity. The lack of production capacity causes the government to frequently 'load shed' power, by imposing blackouts

in areas of low power usage to meet the needs of areas of higher power usage. Hence, the energy sector offers much scope for foreign investment as the government lacks the capital and liquidity of building power-grids and expanding the country's electric capacity. Other imports in the energy sector include solar and hydro-electric generators but these have been installed only in limited quantities.

Further evidence of the growing credibility of Bangladesh's investment regime can be seen from the numerous countries which have decided to invest in the country, as shown in Figure 3<sup>8</sup>:



More than a third of FDI originates from developed parts of the world such as North America, Europe, and Japan. Another approximate third are investments from Bangladesh's South Asian neighbors, mostly from the rapidly growing Indian economy. Furthermore, the Bangladesh Board of Investment (2002) reports that though

<sup>8</sup>Based on percentages provided by the Bangladesh Board of Investment (2004)

approximately 60% of all FDI inflows are transferred through joint ventures to hedge risk, 40% come straight from the parent company without any medium domestic firms (via the establishment of affiliate firms in the host country).

In summary, there are many prospects for FDI in Bangladesh. The nation has many resources and scope to yield many advantages and opportunities for foreign investors. The government and economy have also been made very conducive to investment through a series of reforms allowing the nation to become the most liberalized trade regime of the South Asian region (UNCTAD 2000). Despite the pros, it is also important to recognize that Bangladesh lags behind its neighboring counterparts such as India and Sri Lanka. In many aspects, it is still viewed as an FDI underperformer (UNCTAD 2006) and the country is far from achieving its full potential. It will take time before Bangladesh achieves better results in attracting FDI but as long as the inflows continue to increase, the possibilities for the country's future remain hopeful.

### Chapter III: The History of Development in Bangladesh

**Figure 4**

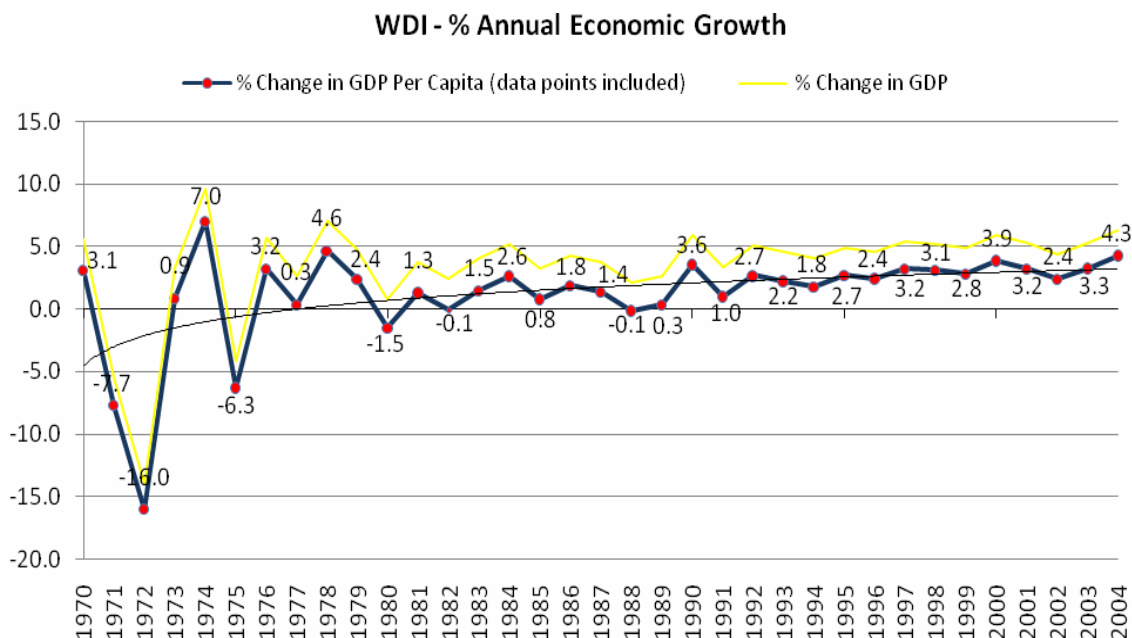


Figure 4<sup>9</sup> uses the annual percentage growth in GDP per capita as a proxy to indicate the history of development in Bangladesh, which has been a turbulent one consisting of many ups and downs. For demonstrational purposes, the annual percentage change in GDP has also been illustrated. The logarithmic trend line runs through the middle of the chart and has an upward slope emphasizing that, despite all the volatility, the country has managed to experience modest levels of economic growth throughout its 35 years of its sovereignty. For practical purposes, the discussion of development in Bangladesh will be divided into the following four sections: (i) Post Liberation Period: 1971-1979, (ii) Period of Sluggish Growth and Instability: 1980-1989, (iii) Period of

<sup>9</sup> Based on data from the World Bank (2006), World Development Indicators (WDI).

Stable Economic Growth and Significant Development: 1990-1999, and (iv) Summary of Bangladesh's Overall Transition in Development.

(i) Post-Liberation Period: 1971-1979

After nine months of war and the approximate loss of 3 million lives, in the years following independence Bangladesh encountered a plethora of difficulties to worsen its already dire economic situation, including high population density, scarcity of resources, frequent occurrence of natural disasters and famine, inefficient government policy, political nepotism, and corrupt governance (Mujeri and Sen 2002). These factors combined to induce a very negative image of the country during its beginning years as the international community remained pessimistic of the Bangladeshi economy's ability to emerge from its seemingly permanent "below poverty level equilibrium trap" (United Nations Development Program 2000) and sustain itself in the long-run without massive flows of foreign assistance. Bangladesh's future appeared bleak compared with its neighboring High-Performing Asian Economies and, with a Human Development Index rising from a mere 0.20 in 1970, it could do little to avoid being labeled a "test case of development" (Munjeri and Sen 2002) or as Henry Kissinger's State Department so famously put it "an international basket case" (Sachs 2005). Regardless of the skepticism, the decade after liberation constituted the phase of economic recovery.

During the first half of the decade, it was in trying to pursue reconstruction and economic growth that the Government of Bangladesh established a Socialist economic system to boost development. This, however, ended up being a contradiction in that the inefficient State Owned Enterprises were only able to produce meager levels of GDP to barely facilitate economic growth. To further hinder development, the agricultural sector

was barraged with both droughts and floods while the 1973 oil crisis dramatically raised the cost of production. Combined with inflation, these factors also propounded Bangladesh's balance of payments deficit. In addition to having one of the lowest levels of income per capita during this period, Bangladesh's struggle with poverty exacerbated as its dense population grew at a rate of nearly 3% (Mujeri and Sen 2002).

During the second half of the 1970s, the government recognized the shortcomings of their Socialist economy and took steps to ease state control and encourage a greater role for the private sector. The 1974/1975 reforms of the industrial investment policy were introduced to allow access to private investment (of up to a higher revised cap of Taka 30 million) for all sectors except eighteen that remained under the directive of the public sector. Foreign investors were also permitted to collaborate with domestic private investors. It is important to note that such reforms were promoted by the International Monetary Fund and the World Bank owing to their influence on the country through loan assistance. This entailed restructuring the economy on a number of different fronts and included rationalization of the tax system, subsidy reduction for the food sector, trade liberalization, increased regulation on credit expansion, improved domestic resource allocation, and privatization of small scaled enterprises. The objective of these policy changes was to remove barriers that adversely affected the productivity and efficiency of major industries. After the military coup d'état in 1975, previously state-run industries were also allowed to take part in joint collaborations with the private sector (Mujeri and Sen 2002).

Moreover, the government set up development financial institutions (DFIs) which financed credit and provided industrial capital to complement the equity of private

enterprises (Mujeri and Sen 2002). Though DFIs boosted Bangladesh's economic performance during its beginning years, they also created the persistent long-term problem of loan defaulting.

The makeover of Bangladesh's economy from a Socialist state to a somewhat capitalistic mixed economy involved a wide array of policy changes. During the 1970s, however, the nation continued to be bombarded with macroeconomic shocks and the implemented reforms did not immediately improve the country's economic situation. Compared to the other Least Developed Countries of that time, Bangladesh underwent a relatively longer time lag but the significance of the reforms slowly started to materialize as the nation emerged out of its post-war reconstruction phase and entered into the 1980s.

#### (ii) Period of Sluggish Growth and Instability 1981-1989

Figure 4 reflects how the 1980s exhibited some degree of stability relative to the turbulence of the previous decade. The effects of the reforms of the 1970s began to show towards the beginning of this period as important development indicators were restored to pre-independence levels (such as GNP per capita, gross national savings as a % of GDP, gross national investment as a % of GDP). On the other hand, inherent structural problems continued to limit the nation's potential for growth and rapid development.

Economic growth was sluggish for many reasons during this period. With very little improvement in productivity, state industries and public enterprises continued to underperform owing to a lack of infrastructure and inadequate policy measures taken by the government. The inefficiency of the economy in producing goods and services increased import demand (and severely limited the country's export capacity) as the

population continued to grow; the trade imbalance was only somewhat contained by artificially controlling for import demand using tariffs, quotas, and a tight exchange rate. Weak governance and the dismal condition of law and order allowed corruption and crony capitalism to become deeply rooted within the economic and political systems, particularly within the bureaucratic and regulatory framework; this widened the socioeconomic gap as the already privileged businessmen and government officials became even wealthier than the majority of the low-income population. Furthermore, with a largely poor population the inability to collect tax revenues weakened fiscal conditions as government expenditure increased. Over-expansionary monetary policy invoked inflationary pressures as the central bank pumped more money into the economy. The strategy of greater access to credit within the private sector backfired as debt defaults plagued the banking system. To make matters worse, the consecutive floods of 1978 and 1988 severely damaged the agricultural sector and inflicted a famine on some parts of country.

Despite its economic travails, the country was able to produce a number of social developments under the management of both government agencies and non-government organizations (NGOs). Mujeri and Sen (2002) observe that development indicators such as child mortality, total fertility, and primary school enrollment rates began to improve during this era. With regards to NGOs, the Grameen Bank and the Bangladesh Rural Advancement Committee (BRAC) served as renowned microcredit providers for the rural poor and aided village businesses and organizations through targeted development assistance (Davis 2006). Other areas of social progress include rural advancement in infrastructure, food provision, water purification, healthcare, and crisis management. It is

important to note that the focus of such programs was mainly on the rural population where “extreme poverty,” income of less than a \$1 a day, was the most prominent. At the same time, it is important to specifically identify the Food for Works and Vulnerable Group Feeding programs of the 1970s which shaped the future success in delivering rural infrastructure and food to the poor.

During this period, Bangladesh employed another series of reforms to better acclimate the economy towards driving growth and development. Like those of the 1970s, the changes were guided by the International Monetary Fund and the World Bank. The measures (e.g. the Bank-Fund’s Enhanced Structural Adjustment Facility) intended to reduce the structural problems that were generating the aforementioned internal and external instabilities. This involved further deregulation to untangle the red tape associated with excessive state presence and greater liberalization to create a more open laissez-faire economy by expanding the span of the private sector. As firms maximized profits and competed with each other, the reforms aimed to increase the incentive to efficiently allocate resources, raise productivity, enhance the nation’s production base, and improve the levels of domestic investment, savings, and overall GDP. As indicative by the unbalanced growth during this period, the extent of such progress was limited owing to the “uneven incidence of the adjustment burden on various socioeconomics groups” (Mujeri and Sen 2002). Regardless of the struggles, the 1980s experienced vital social developments and economic reforms that paved the way for better economic progress for the next period.

(iii) Period of Stable Economic Growth and Significant Development: 1990-1999

The beginning of the 1990s witnessed the success of a democratic parliamentary system through free and fair elections. In addition, the economic reforms of the previous decades finally began to show effect as the nation gained momentum in achieving stable growth and concomitant development.

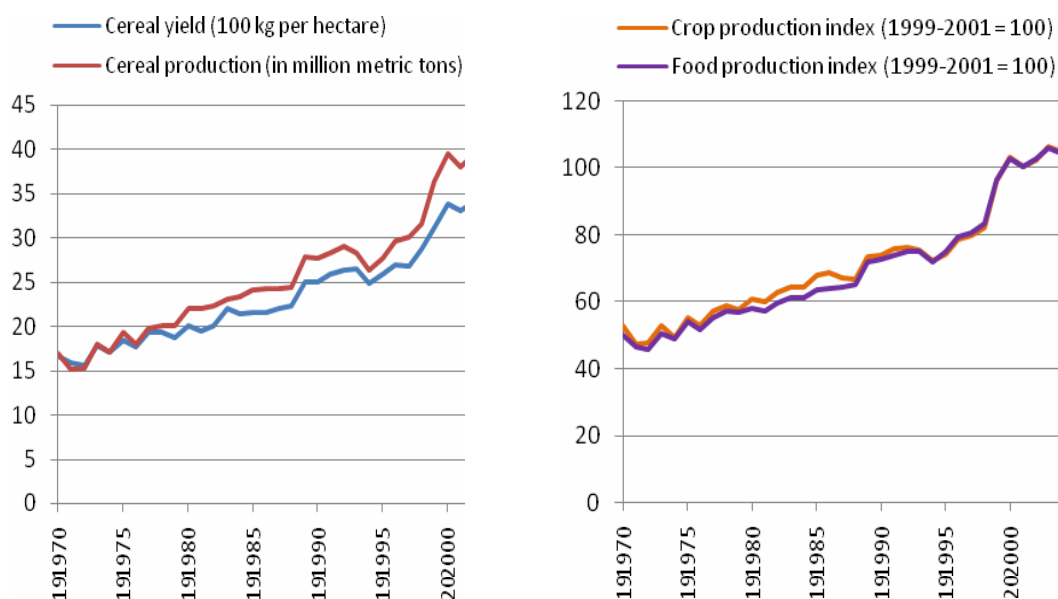
The reforms of the previous decade allowed for greater trade liberalization in the 1990s and gave domestic firms freer access to import much needed raw materials and capital goods. This particularly helped with domestic production to not only meet the demand for goods and services within the country's borders but also develop export-oriented industries to earn much needed foreign currency. The ready-made garments (RMGs) industry fared exceptionally well in its ability to export its textile products and also helped reduce the gender wage gap by employing mostly women.

Though problems such as lackluster infrastructure, wasteful state enterprises, and non-performing loans continue to persist, the trade policies of the 1990s were able to produce an outward-oriented liberalized economy. The changes consisted of a reduction of trade tariffs, quotas, and duties, all of which were impeding the trade. Such measures were emphasized mainly as a means to strengthen and broaden the country's export base to make it more competitive, e.g. by establishing specific export-processing zones. Other adjustments were made to the exchange rate by implementing a price basket system and allowing some flexibility through slow devaluation. The advantages of trade will be elaborated further in subsequent chapters.

The agricultural sector, in particular, performed extremely well. The use of high yield variety crops meant that there was a dramatic rise in the amount of food grains available. Other areas such as poultry, livestock, and fish farms also contributed to the

country's development. The rapid progress can be demonstrated in the management of the floods of 1998, the worst in Bangladesh's history thus far. Not only did the nation avoid a famine but it also did not require any additional food imports, evidence of the economy's increased capacity for food production (and consequently its ability to cope with natural disasters and economic shocks). Figure 5 illustrates the progress of the agricultural sector:

**Figure 5**



The 1990s witnessed a much more stable macroeconomic period with comparatively higher economic growth and fewer shocks. Inflation remained low in the single digits (at roughly 6%) while various social and human development indicators showed promising signs, particularly in terms of total fertility, child mortality, and school enrollment rates which steadily continued to improve since the 1980s (Mujeri and Sen 2002). Other developments were in infrastructure, clean water access, and healthcare. The success of the Grameen Bank in terms of microcredit also contributed to

this as it not only helped expand village businesses but also facilitated the spread of technology and female empowerment through its phone program, which rented cell phones to village women enabling them to become operators in remote areas which lacked communication links. Given the Bangladesh's relatively low level of GDP per capita at \$340 in 1999 (World Bank 2006), the success of the 1990s was quite remarkable and led into the current state of development in Bangladesh.

(iv) Summary: The Transition of Bangladesh's Development to its Present State

**Box Chart 1**

	1970/71	1980/81	1990/91	2000/01	2004/05
<b>GDP (billions, constant 2000 US\$)</b>	18.24	19.77	28.49	45.52	55.97
<b>GDP per capita (constant 2000 US\$)</b>	280.96	240.51	273.80	353.13	402.07
<b>Gross capital formation (% of GDP)</b>	11.34	14.44	17.05	23.86	24.02
<b>Gross domestic savings (% of GDP)</b>	7.15	8.39	9.65	18.42	18.67
<b>Agriculture, value added (billions, constant 2000 US\$)</b>	6.81	6.63	8.48	11.62	12.85
<b>Industry, value added (billions, constant 2000 US\$)</b>	3.16	3.36	5.89	11.51	15.21
<b>Manufacturing, value added (billions, constant 2000 US\$)</b>	1.82	2.20	3.57	6.93	8.92
<b>Age dependency ratio (dependents to working-age population)</b>	0.91	0.87	0.79	0.69	0.65
<b>Birth rate, crude (per 1,000 people)</b>	44.42	40.44	34.99	28.49	26.66
<b>Fertility rate, total (births per woman)</b>	6.33	5.39	4.32	3.22	2.99
<b>Life expectancy at birth, total (years)</b>	44.55	48.81	55.05	61.53	63.46
<b>Mortality rate, infant (per 1,000 live births)</b>	145.00	129.00	100.00	66.00	56.40
<b>Mortality rate, under-5 (per 1,000)</b>	239.00	205.00	149.00	92.00	77.00
<b>Population growth (annual %)</b>	2.42	2.37	2.27	1.97	1.88
<b>Physicians (per 1,000 people)</b>	0.12	0.12	0.18	--	0.26
<b>Telephone Lines (per 1,000 people)</b>	--	1.16	2.10	3.81	5.94

Note: -- represents missing data

Source: World Bank 2006

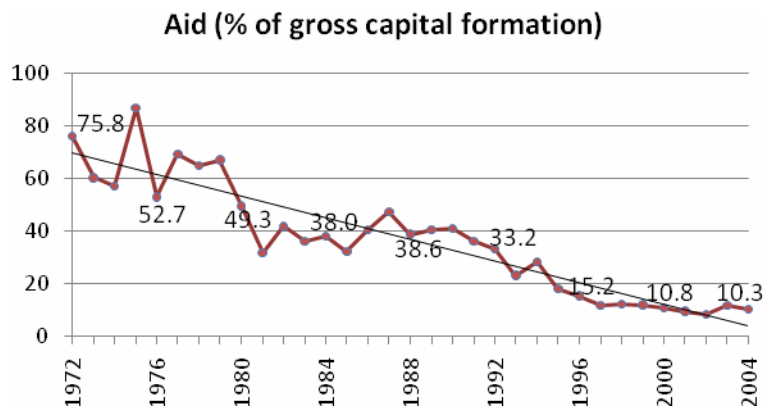
Over the span of the last 35 years, Bangladesh has gained strides in its quest for development. The indicators in Box Chart I above demonstrate the nation's progress in

improving the standard of living of its citizens. Though the percentage change has varied, the country has maintained a positive rate of growth on a number of different fronts while experiencing a substantial total factor productivity growth (Mujeri and Sen 2002). As a result of foreign investment, both the industrial and manufacturing sectors have taken greater roles in the economy, while the low-income agricultural sector has dwindled in leading the country's production of goods and services. As indicative by the growth of telephone lines, telecom is emerging as another sector promising to fuel continued growth. The number of physicians have also increased progressively, though the 2004/05 figures infer a mere 260 physicians for every million of the population. Other notable achievements are worth mentioning to summarize the nation's progress amidst the complex challenges.

In 2006, Bangladesh pushed economic growth passed the 5% mark. Despite a population of over 150 million, the country has now significantly contained its annual population growth to below 2%, owing much to the massive family planning drive of the 1970s; total fertility rate dropped from 6.33% in 1970 to below 3% in 2005. This reduction is especially noteworthy as it marks an emergence from the poverty trap in which families bear many children in fear of a high infant mortality rate. Primary school enrollment levels have also increased from 77% in 1990 to 96% in 2002/03, mainly owing to increased female participation; in 2001, the percent ratio of girls to boys stood at 51:49 (Ahmed 2006). Part of this has been due to the distribution of microcredit and the empowerment of women in possessing greater social capital within their families. The country's declining need for foreign aid, illustrated in Figure 6, is further evidence

of the many obstacles the country has successfully overcome to achieve an impressive level of development, given the low level of income per capita.

**Figure 6**

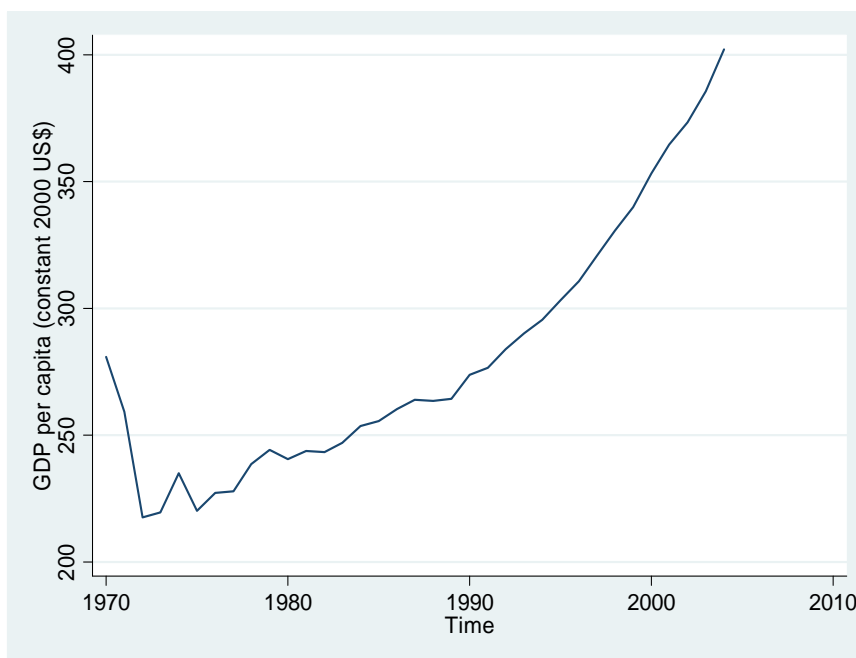


The country's reduced dependency on foreign aid is attributed to several factors. Firstly, gross capital formation and domestic savings have both doubled since the 1970s, allowing the country to sustain itself better. The government has also been able to better manage its resources and enhance tax collection policies such that local tax revenues now finance 72% of all public expenditure (Ahmed 2006). A dramatic rise in inflows of worker remittances from Bangladeshi expatriates, \$4.3 billion in 2005, has also helped lower the reliance on donor governments (World Bank 2007). Furthermore, the Food for Works and Vulnerable Group Feeding programs from the 1970s have continued to make sure that extreme poverty no longer persists even in remote villages. As will be discussed in the next chapter, the advantages of FDI inflows have also helped lower the need for external assistance.

Overall, it is lucid that Bangladesh's progress has been a very gradual one involving a series of imperative reforms from the past few decades that have led into its current development platform. The country has been able to shed its negative image of

the 1970s and is now considered a lead performer among the Least Developed Countries, to the extent that many in the international community question whether it should continue to be grouped among the most poverty-stricken Third World nations. Figure 7<sup>10</sup> illustrates the rise in GDP per capita since 1970 in constant 2000 U.S. dollars to account for inflation.

**Figure 7**



After a sharp decrease following the Liberation War, GDP per capita has gradually increased, albeit somewhat linearly; this partly illustrates the autocorrelation issue discussed in the following chapter. GDP per capita managed to rise just above \$400 in 2004. As one of the most densely populated countries in the world with low levels of income per capita, Bangladesh's achievements are noteworthy.

<sup>10</sup> Based on data from the World Bank (2006)

Despite the development, it is important to remember that Bangladesh continues to be a relatively poor nation and many challenges lie ahead. Extreme poverty may no longer have a stronghold but moderate poverty remains a major concern as per capita earnings remain considerably low in light of the slow rate of income-poverty reduction. Relative to the neighboring High-Performing Asian Economies, Bangladesh has struggled to even compare. In 2004, the country's Human Development Index of 0.53 ranked 137<sup>th</sup> out of 177 countries while its Human Poverty Index of 44.2 ranked 85<sup>th</sup> among 102 developing nations (United Nations Development Program 2006). There is further reason to be wary over the level of external debt accumulating as it currently stands well above \$20 billion (World Bank 2006). This raises questions over long-term development and here lies the importance of foreign direct investment as a means to sustain long-term growth. The following chapter takes a closer look at this relationship.

## **Chapter IV: The Relationship between FDI and Economic Growth in Bangladesh**

### *(i) Theoretical Concepts*

There are several benefits of FDI on a macroeconomic level, particularly for a Third World Nation such as Bangladesh, where inflows of foreign investment can help broaden economic production and growth. FDI provides capital from sources abroad which the country is unable to supply domestically. Foreign investment helps to fill the saving-investment gap caused by the lack of domestic savings converting into investment (Ahmad 1990). Bangladesh specifically faces many obstacles in expanding its cities with overpopulation and low GDP per capita (Sattar 1999). The inflows facilitate capital formation and the growth of a number of economic sectors, including industry, manufacturing, infrastructure, and energy. The expansion leads to a rise in the availability of jobs and a fall in the unemployment rate<sup>11</sup>. Consequently, GDP and per capita income increase which, in a developing country, fosters poverty alleviation. In addition, FDI strengthens ties with developed countries that yield cost advantages in the form of advanced technology transfers and resulting positive externalities. Increased financial associations also lead to stronger capitalistic markets and ideals of corporate governance and social responsibility ([www.supro.org](http://www.supro.org)). On the basis of this intricate link between FDI and growth/development, the trade regime of Bangladesh has been intensely liberalized to maintain the streams of investments and finances from abroad. These reasons also increase the effort of the government to try and make the country an

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<sup>11</sup> In [www.supro.org](http://www.supro.org) (see bibliography for the full website address), it is noted that the lack of data on employment figures has made it difficult to calculate the impact of FDI in this regard. Nonetheless, their estimates suggest foreign firms have produced 2.7 million jobs within the manufacturing sector.

attractive destination for FDI, which in itself has several benefits. The result has validated a reinforced incentive to educate and train the population to make Bangladesh's labor force more competitive through higher national education expenditure. The effectiveness of domestic institutions such as the Grameen Bank, however, appears to be more effective in fostering investment in human capital (via female empowerment) than FDI.

Fry (1999) finds that foreign capital in non-Asian countries has induced decreasing rates of national saving, domestic investment, and economic growth. His study suggests that in most regions FDI tends to substitute and crowd out domestic investments. In the case of South and East Asia, however, foreign investment has been beneficial in increasing capital formation and has produced positive effects similar to home investment (Fry 1999). Since there is little domestic investment to crowd out in Bangladesh, foreign investment can effectively assist with economic growth to increase the country's GDP.

In a country like Bangladesh, where the economy is driven by high volume imports, a huge capital account deficit accumulates as foreign exchange flows out. Sattar (1999) notes that FDI is a fundamental and necessary component for long-term sustainable growth in Bangladesh. In this context, FDI enables various economic sectors to become efficient and increase the production of the economy. Sattar (1999) discusses the advantages of exports and FDI outflows in this context. Outflows enable a nation to earn foreign exchange and improve its capital account; it can increase an already existing surplus or, as in the case of Bangladesh, reduce its budget deficit and possibly help bring about a surplus in the distant future. FDI inflows tend to deter the capital account as Fry

(1999) identifies a strong association with higher imports. However, when such inflows help raise the production capacity, the economy can become more export-oriented (Fry 1999) and gain foreign exchange currency (Sattar 1999). This earned currency can finance increased imports or inflows of foreign capital and, in turn, sustain further growth and development (Sattar 1999). Thus, Bangladesh has adopted a capitalistic, export-oriented growth strategy ([www.supro.org](http://www.supro.org)). Specifically, the relatively recent success of the RMG industry exemplifies this cycle. Sattar (1999) highlights the logic that has underscored Bangladesh's trade policy regime.

Though FDI entails many positives, there remains a concern over capital flight. This notion involves outflows of domestic capital that hurts the country's current account and foreign exchange reserves. Quazi (2004) suggests that international aid and foreign investment tends to accelerate such outflows and stunt economic growth. The study suggests that the foreign currency generated by FDI helps finance the flow of domestic capital abroad as incoming foreign capital substitutes for it within the home country's borders. Conversely, Mondal (2003) identifies reduced capital flight as a benefit of FDI. This infers that the benefits of FDI reduce the risk of home investments by stabilizing economic output and reducing the incentive to invest abroad.

The number of studies examining the precise relationship between FDI and economic growth has been somewhat limited. This can be attributed to a number of reasons. In terms of the macro economy, there are a number of wide-ranging factors that can influence growth and development outside of foreign investment; not including all such factors raises concerns over omitted variable bias in the empirical estimation. This occurs when a significant variable is excluded and the statistical model is underspecified,

that is, it has not accounted for all relevant factors. In order for their to be bias, the excluded independent variables must affect both the dependent variable as well as other independent variables of the equation. An upward bias occurs when independent variables are neglected such that the effects of the independent variables are included in the regression are overemphasized. In contrast, a downward bias is the effects of the independent variables are underestimated. Moreover, independent variables are often times correlated with each other and create issues of multicollinearity as well, which can severely misconstrue the analysis. Ahmad (1990) notes the presence of such interdependence among variables.

*(ii) Empirical Evidence & Analysis*

This section includes a series of regressions<sup>12</sup> to underscore the many advantages and growth prospects that FDI inflows have brought to the Bangladesh economy. The objective is to not only gain insight into the country's economic progress in recent years but to also provide a better understanding of its limitations. The methodology of the empirics constitutes a series of regressions using the Ordinary Least Squares (OLS) model to prove a significant correlation between FDI and economic growth. In trying to analyze such effects of a Third World Nation such as Bangladesh, it is important to recognize that data on key development indicators are often times missing or inaccurate. For this reason, the data used in the analysis will begin from 1980 when FDI had just begun to flow into the nation after the era of reconstruction and war recovery. The tables express the coefficients and t-statistics of each independent x-variable to demonstrate its

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<sup>12</sup> For Tables 1-4 in this section, estimations involving corruption and government stability were based on 1984-2004 data gathered from the Political Risk Services (PRS) Group's International Country Risk Guide. Estimations involving all other variables were based on data gathered by the World Bank (2006).

level of significance. The R-squared or coefficient of determination is included to represent how much variation in the dependent y-variable is captured by the regression. Moreover, the dependent variables were lagged in Table 1 to control for serial correlation. Also known as autocorrelation, this occurs when successive error terms are correlated with each other over time and the reliability of the least squares estimates are overstated (Hill 2001). The lags account for heteroskedasticity or the non-randomness of variables, in that the error term is increasing with each observation over time.

**Table 1A**  
Effect of FDI Inflows (monetary value) and Socioeconomic Variables on  
GDP Per Capita

GDP per capita (US\$)	(1)	(2)	(3)
FDI, net inflows (US\$ millions)	0.334 (6.54)***	0.014 (2.40)**	0.013 (2.73)**
Adjusted savings: net national savings (% of GNI)		0.289 (1.34)	
Manufacturing, value added (annual % growth)		0.668 (3.62)***	0.649 (3.75)***
Population growth (annual %)		-8.773 (0.74)	15.189 (1.21)
Time Trend (1980-2004)		-0.006 (0.02)	0.238 (0.83)
Adjusted savings: education expenditure (% of GNI)			-14.141 (3.13)***
Govt. Stability: rating out of 12, higher the better (PRS Group)			0.492 (1.69)
GDP per capita lagged by 1 year (US\$)		0.978 (19.14)***	0.574 (3.44)***
GDP per capita lagged by 2 years (US\$)			0.593 (2.97)**
Constant	274.664 (40.10)***	-35.593 (0.06)	-535.102 (0.92)
Observations	25	24	21
R-squared	0.65	0.99	0.99

Absolute value of t statistics in parentheses

\* significant at 10%; \*\* significant at 5%; \*\*\* significant at 1%

Table 1A utilizes GDP per capita as a proxy for growth and development. Regression (1) is merely GDP per capita against FDI and serves as a benchmark to demonstrate the positive relationship between the two. It shows that a \$1 million increase in FDI inflows raises GDP per capita by \$0.334. Regression (2) of Table 1A significantly reduces the omitted variable bias as more independent variables are introduced into the equation. As a result, the coefficient of FDI also decreases to \$0.014. In the second column, FDI is found to be significant at the 10% level and is positively correlated to GDP per capita, such that a \$1 million increase in FDI inflows raises GDP per capita by \$0.014. Though this does not appear to be an economically significant increase in GDP per capita, it is important to note that in a Third World country such as Bangladesh, money has more value in that \$1 (currently equivalent to about 70 Taka) has relatively higher purchasing power in Bangladesh than in the United States. GDP per capita is also limited by Bangladesh's population, which is quickly approaching 150 million. Furthermore, the annual growth of the manufacturing sector is significant at the 1% level. A unit increase in the percent growth of manufacturing leads to a \$0.668 increase in GDP per capita. As mentioned in the previous sections, manufacturing growth in textiles has assisted with domestic production and has helped the country gain momentum in development, especially through the RMG industry. However, there is some doubt as to whether this will continue in the face of increased competition once the quotas from the Multi Fiber Agreement (MFA) are dropped ([www.supro.org](http://www.supro.org)). Industry was not included since it is almost perfectly correlated with manufacturing such that one can substitute the other. Though insignificant, it is worth mentioning that net national savings are adjusted by the World Bank to account for factors such as education

expenditure, consumption of fixed capital, environmental damage by particulate emissions and carbon dioxide, as well as the depletion of energy, mineral, and forest resources (2006).

Regression (3) of Table 1A adds government stability as a new variable and replaces net national savings with saving adjusted only for education expenditure. Once again, FDI and growth in manufacturing are significant, with their correlations with GDP per capita slightly reduced in comparison to Regression (2). This may be because the effect of savings (adjusted for education expenditure) proves significant at the 1% level but is negatively correlated with GDP per capita. The inverse relationship may be because the size of the labor force shrinks as more people enroll to pursue education. From a historical point of view, the increased enrollment in schools would correspond with a higher number of female students and a reduction of child labor, possibly accounting for the fall in GDP per capita. Government stability has also been included to capture political unrest, which is common particularly in the form of ‘hartals’ or general political strikes aimed to stem business activity; however, it is not significant in the context of GDP per capita. A plausible explanation for this is that the Bangladeshi people have become quite resilient in managing to run offices among such strife, although commercial businesses do suffer. The ranking system used in the PRS Group’s International Country Risk Guide model could have also attributed to the insignificance of the variable.

**Table 1B**  
Effect of FDI Inflows (as % of GDP) and Socioeconomic Variables on  
GDP Per Capita Growth

GDP per capita growth (annual %)	(1)	(2)	(3)
FDI, net inflows (% of GDP)	3.804 (3.77)***	2.535 (2.58)**	2.239 (2.43)**
Gross domestic savings (% of GDP)		-0.002 (0.02)	
Manufacturing, value added (annual % growth)		0.239 (3.80)***	0.259 (3.89)***
Population growth (annual %)		0.650 (0.17)	1.023 (0.26)
Time Trend (1980-2004)		0.097 (0.84)	0.153 (1.39)
Adjusted savings: education expenditure (% of GNI)			-2.655 (2.35)**
Govt. Stability: rating out of 12, higher the better (PRS Group)			0.180 (1.57)
GDP per capita growth (annual %) lagged by 1 year		-0.262 (1.84)*	-0.427 (2.44)**
Constant	1.467 (5.44)***	-194.353 (0.82)	-303.010 (1.35)
Observations	25	24	21
R-squared	0.38	0.81	0.85

Absolute value of t statistics in parentheses

\* significant at 10%; \*\* significant at 5%; \*\*\* significant at 1%

Table 1B examines the relationship between FDI inflows (as a percent of GDP) and the annual growth in GDP per capita, which is arguably a better indicator for economic growth since it deals with the percentage change rather than the absolute value. Regression (1) has been included as a benchmark to demonstrate the positive correlation between GDP per capita growth and FDI inflows. It suggests that a unit increase in FDI inflows (percentage of GDP) induces a 3.804 increase in GDP per capita growth. In Regression (2), the correlation between FDI and GDP growth is reduced as

we add more independent variables. Nonetheless, FDI inflows and the annual growth in manufacturing are significant at the 5% and 1% level respectively. A unit increase in FDI results in a 2.535 increase in the annual percent growth of GDP per capita; similarly, a unit increase in manufacturing growth results in a 0.239 increase in GDP growth. Manufacturing has a stronger influence on GDP per capita than FDI since in recent years, the concomitant textiles industry has increased employment levels particularly among women, which has contributed to the reduction of gender inequality. For Regression (3), in addition to FDI inflows and the growth of manufacturing, savings adjusted for education expenditure is also significant and is negatively correlated with GDP per capita growth at the 5% level. Overall, the significant results of Table 1B are quite similar to those of Table 1A.

**Table 1C**  
Effect of FDI inflows (as % of GDP) and Socioeconomic Variables on GDP Growth

GDP growth (annual %)	(1)	(2)	(3)
FDI, net inflows (% of GDP)	3.219 (3.23)***	2.659 (3.12)***	2.568 (2.07)*
Manufacturing, value added (annual % growth)		0.257 (4.41)***	0.243 (2.78)**
Adjusted savings: education expenditure (% of GNI)		-2.001 (1.93)*	
Population growth (annual %)		2.588 (0.74)	0.140 (0.02)
Time Trend (1980-2004)		0.197 (1.86)*	0.073 (0.41)
Gross domestic savings (% of GDP)			-0.127 (0.61)
Corruption: rating out of 12, higher the better (PRS Group)			0.101 (0.31)
Govt. Stability: rating out of 12, higher the better (PRS Group)			0.050 (0.36)
GDP growth (annual %) lagged by 1 year		-0.281 (2.20)**	
Constant	3.823 (14.37)***	-391.672 (1.81)*	-142.299 (0.39)
Observations	25	24	21
R-squared	0.31	0.81	0.70

Absolute value of t statistics in parentheses

\* significant at 10%; \*\* significant at 5%; \*\*\* significant at 1%

Table 1C examines the influence of FDI inflows (as a percentage of GDP) on the annual percentage growth of GDP. As before, Regression (1) acts as a bench mark to illustrate the positive relationship between the two; it suggests that a unit increase in FDI results in a 3.22 increase in GDP growth. Regression (2) finds that FDI net inflows, annual growth of the manufacturing sector, savings adjusted for education expenditure, and the time trend are all significant variables. Regression (3) includes additional variables such as government stability and corruption; savings adjusted for education expenditure is replaced by gross domestic savings to focus purely on savings. The results

show that only FDI inflows and manufacturing growth are significant. Though Bangladesh has been rated as one of the most corrupt countries in the world, corruption does not appear to be significant in its effect on GDP growth as it has had very little variation since the country's independence; government stability has also behaved similarly. This may suggest that corruption and government stability are captured by the regression as fixed effects. The International Country Risk Guide model could have also influenced the statistical regression to render both corruption and government stability insignificant. Gross domestic savings is insignificant and this can be attributed to Bangladesh's very low level of income per capita, where many citizens do not earn enough to save and invest. It is interesting to note its negative coefficient or inverse relationship with GDP growth, since it leads to a decrease in aggregate demand, lower firm production, and a fall in the full-employment level.

**Table 2**  
Effect of FDI inflows (monetary value) and Socioeconomic Variables on  
Telecom Distribution

	Fixed line and mobile phone subscribers (per 1,000 people)
FDI, net inflows (BoP, US\$ millions)	0.019 (1.85)*
Gross capital formation (% of GDP)	-0.607 (0.79)
Gross domestic savings (% of GDP)	-0.069 (0.12)
Aid (% of GNI)	0.669 (0.84)
General government final consumption expenditure (US\$ millions)	0.019 (5.73)**
Time Trend (1980-2004)	-0.611 (1.63)
Constant	1,196.379 (1.161)
Observations	25
R-squared	0.90

Absolute value of t statistics in parentheses

\* significant at 10%; \*\* significant at 5%; \*\*\* significant at 1%

Table 2 depicts how FDI accelerates the expansion of the consumer base within the telecom sector and emphasizes another dimension within development and growth. Foreign investment allows for technology transfers from developed countries to assist Bangladesh in developing its telephone network and satellite bases. As seen in Chapter 2, telecommunications is a major recipient of FDI shares and has played an integral role in building the nation's communications infrastructure. FDI has facilitated the recent expansion of the telecom sector, which is a large contributor to Bangladesh's GDP and has the potential to provide more jobs to foster economic growth. Though not expressed in the regression, the spread of phone subscriptions is also indicative of growing use of the internet. Government expenditure is also significant since it helps finance the

distribution of land and mobile phones and exerts a stronger effect in increasing phone subscribers.

**Table 3**  
Effect of FDI inflows (monetary value) and Socioeconomic Variables on  
Commodity Exports

	Exports of goods and services (US\$)
FDI, net inflows (BoP, US\$)	2.784 (2.15)**
General government final consumption expenditure (US\$)	0.081 (0.10)
Household final consumption expenditure (US\$)	0.340 (2.23)**
Aid per capita (US\$)	-1.421e+08 (4.90)***
Time Trend (1980-2004)	-6.556e+07 (0.73)
Constant	1.254e+11 (0.72)
Observations	25
R-squared	0.98

Absolute value of t statistics in parentheses

\* significant at 10%; \*\* significant at 5%; \*\*\* significant at 1%

Table 3 reveals that foreign direct investment is positively correlated with exports at the 5% level. It suggests that a \$1 increase in FDI leads to a \$2.784 increase in exports. The regression demonstrates the key relationship between incoming foreign investment and exports. As FDI increases, the economy's production capacity also increases enabling the country to export more goods and services. This allows Bangladesh to earn foreign currency with which to further inflows of FDI and increase the economy's production capacity even more. The analytics provide an understanding of how FDI can help sustain economic growth. GDP is not included in the equation because exports are already a part of GDP and this would account for it twice. Furthermore, household consumption and aid per capita are both significant. Consumption is

positively correlated with exports since it can boost aggregate demand to encourage economic output which, in turn, enables firms to expand not only for the domestic market but for exports as well. Aid per capita is negatively correlated at the 1% level and this may be because it moves opposite to exports in the latter's representation of economic independence and self-sustainability. In addition, household consumption is correlated with exports at the 5% level.

**Table 4**  
Effect of Exports and Imports (monetary value) on Bangladesh's Current Account

	Current account balance (BoP, US\$)
Exports of goods and services (US\$)	0.616 (4.25)***
Imports of goods and services (US\$)	-0.545 (-3.94)***
Constant	5.78e+08 (1.92)*
Observations	25
R-squared	0.47

Absolute value of t statistics in parentheses

\* significant at 10%; \*\* significant at 5%; \*\*\* significant at 1%

Table 4 simply serves as a bench mark to illustrate the effects of exports and imports on the current account. It suggests that the positive impact of exports currently outweighs the negative impact of imports on the current account. This reinforces the aforementioned importance of FDI as a way to increase the economy's production capacity and help adopt an export-oriented trade regime to raise foreign exchange reserves. Amongst the backdrop of the current situation of high import volumes, such a gain in momentum can help improve the dynamic of the current account of Bangladesh to sustain economic growth for the long-run.

Lastly, it is important to note that a deeper analysis could have been provided if more data was available but it is necessary to consider that Bangladesh is a relatively

new nation only 35 years of age. There are not as numerous data collection agencies working domestically to convey such information while government corruption often times leads to misconstrued information. Nonetheless, multinational organizations such as the UN and World Bank are now more involved within the Bangladeshi economy and have been able to remedy many such issues.

### **Concluding Remarks**

This study has undertaken a scientific approach to examining the relationship between FDI and economic growth. The histories of each respective component were separated to examine them as independent economic factors before evaluating their connection with each other. The history of Bangladesh exemplifies the plethora of factors that have shaped the country, particularly through reforms in economic policy and public management. The investment regime has undergone a complete transformation via privatization and trade liberalization. These factors have allowed the country to adapt in an increasingly interdependent, global economy, and Bangladesh has successfully reaped many benefits of foreign investment.

Though the country is performing much better than the dire straits of extreme poverty during the 1970s and 1980s, it remains poor and populous with very low income per capita. Such inadequacies have stifled growth and development. Therefore, FDI is pivotal in providing Bangladesh the necessary finance and capital to achieve sustainable growth as well as poverty alleviation. Statistical analyses were used to exemplify the essential function of foreign investment in maintaining economic growth. FDI inflows have been able to increase GDP by raising the economy's output capacity and full-employment level. At the same time, it has also delivered development by improving per capita income levels. These enhancements are allowing the country to become more export-oriented and continue on its quest for development. Overall, FDI can provide the necessary tools for Bangladesh to progress further and realize higher growth levels by utilizing all its resources to their fullest potential.

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