

## **Foreign Direct Investment in Bangladesh : An Analysis**

**Khondoker Abdul Mottaleb**

### **Introduction**

Most countries of the world are economically associated with each other in three different ways. These are through international trade; or through Overseas Development Assistance (ODA); or by the way of international capital flow.

International trade does pay a vital role in the growth and development of a country. The basis of international trade is comparative advantage, which implies that flow of goods will take place from efficient low cost producers to inefficient high cost producers. But the poor basis of the industrial sector in the domestic economy and weak comparative advantage emanating from the inefficient operation of the industries had been constraining, many developing countries in realizing the benefit of trade.

After the cold war era, the availability of foreign aid is showing a steadily decreasing trend. For example, in Bangladesh the actual amount of inflow of foreign aid (grants+loans) in the FY 1990/91 was US\$1732 million<sup>1</sup> and in the FY1997/98, the aid made of fresh aid pledges US\$ 190 million.<sup>2</sup>

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\* Research Officer, BPATC.

1 Government of Bangladesh, *Bangladesh ArthanaitikSmiksha*, 1998 (Dhaka:Ministry of Finance, Finance Division, June, 1997), P.133.

2 *The Bangladesh Observer* (November 14, 1997).

Now a day's Foreign Direct Investment (FDI) is the most important issue in most of the country's foreign economic policy. FDI is now acting as super alternative of ODA. In the "Dictionary of Modern Economics" FDI is defined as "any investment in another country which is carried out by private companies or individuals as opposed government aid."<sup>3</sup> Foreign private Investment (Promotion and Protection) Act-1980, defines foreign private investment as "Investment of foreign capital by person who is not a citizen of Bangladesh or by a company incorporated outside Bangladesh, but does not include investment by a foreign government or an agency of foreign government."<sup>4</sup>

The positive role of FDI in accelerating pace of development in developing countries as is evidenced in Hong Kong, Singapore, Korea and Taiwan (these countries are known as Newly Industrialized Economies), attracting FDI has become a priority agenda for the developing countries foreign economic policy. At present there is hardly any country in around the globe big or small, financial base or newly emerging which is not in the race of capturing foreign investment."<sup>5</sup>

### **Importance of FDI in Bangladesh**

Generally, investment in an economy raises out put and improves standard of living of the people. But there are arguments for and against foreign investment in under-

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3 David W. Pearce. *Macmillan Dictionary of Modern Economics* (London : The Macmillan Press Ltd, 1986)P-159.

4. GOB, *Guide to Investment Bangladesh*, (Dhaka : Board of Investment, Prime Ministers Office, March, 1998) P. 104.

5 A. H. M. Nurul Islam and Sujit R. Shaha, "Foreign Direct Investment in Bangladesh : Expectations and Realities" *Bank Parikrama*, Vol. 18, No's 3 & 4 (September & December, 1993), PP. 71-72.

developed countries. Those against, say that it constitutes economic colonialism and is an attempt to retain control of ex-colonies. The arguments supporting foreign investment are that, this type of investment achieved beneficial results in the East Asian countries, and therefore will succeed elsewhere. There can be no general solution to this debate since each individual case has to be judged on its own merits. In Bangladesh, a healthy flow of FDI is increasingly getting priority in the government economic agenda. A news item published in "The Financial Express" said that, "along with the government, private sector investment need to be increased immediately to bridge the yawning gap in infrastructure sector."<sup>6</sup> The same report said that, Bangladesh requires a minimum of 1.75 billion dollars each year for infrastructure development. In a report the World Bank states that, most developing countries need massive investment in sanitation and in water supply infrastructure. In developing countries, one of the most pressing problems is the overwhelming need to invest heavily in sanitation facilities and the provision of clear water. The World Bank has estimated, over the next decade, between \$600,000 millions and \$800,000 million will be required to meet the total demand for fresh water, including for sanitation, irrigation and power generation.<sup>7</sup> Since the supply of capital from the local source in Bangladesh is not adequate to meet the growing need for investment due to low rate of domestic savings, the importance of FDI is increasing day by day.

In the previous period, the country's savings investment gap were bridged by foreign aid or loans. But given the current aid scenario, Bangladesh have to look for other sources of foreign

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6 *The Financial Express*. (February 1, 1999).

7 United states Information Services, *News Feature*



exchange to support its current account balance as well as rising investment level. The most promising source of foreign exchange for the developing countries in recent years has been foreign direct investment (FDI). Therefore, there is now widespread support for the need of FDI in Bangladesh.

### **FDI and the policy of Bangladesh government**

Over the recent past, most nations in the world including the former socialist bloc, are adopting increasingly more open policy towards FDI. For example, "during 1991, 35 countries made 82 changes in foreign direct investment policy. Nearly 80 of these changes were in the direction of greater liberalization of FDI".<sup>8</sup> Bangladesh is not behind in terms of policy formulation towards FDI. In the initial years of after liberation, the aim of the country was to build up an exploitation free society, for this reason, private and foreign investment were both discouraged at that time. But in the face of increasing globalization, the country has realized the importance of strong private sector. In order to strengthen private sector, the government of Bangladesh adopted the policy of privatization and this procedure is still continuing. Moreover to attract both foreign and domestic investment the government announced "New Industrial Policy" (NIP) in June-1982<sup>9</sup> and as well as "Private Foreign Investment Act-1980"<sup>10</sup>. The main provisions of "Private Foreign Investment Act-1982 are as follows:

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8 Roy. J Ruffian, "The Role of Foreign Direct Investment in Economic Growth of the Asia and Pacific Region" *Asian Development Review* Vol. II No. I (1993) P. 13

9 For Details See Government of Bangladesh. *Industrial Policy-1982*(Dhaka : Ministry of Industries, 1982).

10 For Details See *Report of the Task Forces on Bangladesh Development Strategies for the 1990s, Managing the Developing Process*, Vol. 2, S. A. L. Reza (Conveynor). (Dhaka : University Press Limited, 1991), pp. 75-77.

- ◆ Ensuring equal treatment for foreign and local investment in all respects;
- ◆ Protection of foreign investment from nationalization, reinsuring repatriation of proceeds from sale of shares and profits;
- ◆ Protection of intellectual property rights.

The government of Bangladesh has also formulated new industrial policy In 1986 and in 1991 (revised in 1992), to accelerate the private investment. In the industrial policy 1991 (revised in 1992), all sectors of the economy are allowed to private investor except the following five<sup>11</sup>

- ◆ Arms ammunition and other defense equipment and machinery;
- ◆ Production of atomic energy;
- ◆ Forest plantation and mechanized extraction within the bounds of reserved forest;
- ◆ Security printing (currency notes) and minting; and
- ◆ Railways and air transportation (except air cargo and domestic air transportation).

All Sectors excepting the aforementioned reserved industries, are open for private sector investment. Investment in the form of joint venture and 100% foreign ownership by foreigners in the following five listed areas are specially encouraged by the government:

- ◆ Export oriented industries;
- ◆ Industries located in the Export Processing Zones;

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11 GOB, *Guide to Investment in Bangladesh*. Op. Cit. PP.10-11.

- ◆ The industries that are based on the high technology, that are either efficiently import substituted or export oriented;
- ◆ The industries beside on intensive use of the local resources;
- ◆ Such types of industry, where there is scope for improving quality, production and marketing.

In the present policy packages of the government, there are a good number of incentives offered towards the foreign investors, which are as follows:

- ◆ Depending on the nature and location of industry, 2.5% to 15% concession of the payable rate of duty on the imported machinery;
- ◆ Tax holiday for 5 to 12 years;
- ◆ Instead of tax holiday, allowances of accelerated depreciation;
- ◆ For the tax assessment, liberal investment allowances;
- ◆ Tax exemption on, royalties interest on foreign loans, capital gains from the transfer of shares and technical assistance fees;
- ◆ Repatriation of invested capital, and dividends;
- ◆ No restrictions for the foreign nationals in issuing work permit in Bangladesh;
- ◆ On the basis of bilateral agreement avoidance of double taxation;
- ◆ Income tax exemption up to three years for the foreign technicians employed under the approved industries;



- ◆ Investment in share's and securities through Dhaka Stock Exchange without prior approval of Bangladesh Bank;
- ◆ Treatment of reinvested reportable dividends as new investment.

Nevertheless duty free import of capital machinery for the export oriented industries are also included in the incentive packages offered by Board of Investment.<sup>12</sup>

The government enacted "The Bangladesh Private Export processing Zones Act 1996, allowing setting up of export processing zones in the private sector with a view to attracting more investment especially foreign investment in the country. Recently the government has been taken the following measures for maximizing foreign investment. These are:

- ✱ Law Reform Commission Act;
- ✱ Investment Visa for the Investors;
- ✱ Permission to set up clinic by foreign doctors by joint venture.

Actually the scope and incentives currently provided by Bangladesh in comparison with SAARC countries and other East Asian countries are broadly similar, or some where more liberal than the policy of the other countries in this region. A news item published in 1999 that, now the policy of Bangladesh in terms of FDI is the most liberal policy in the whole Asia<sup>13</sup>.

12 For Details See *Report of the Task Forces on Bangladesh Development Strategies for the 1990s, managing the Developing Process*, Op. Cit. PP.58-59.

13 The Daily Ittefaq (April 12, 1999).

### The trends of FDI inflow in Bangladesh

Recently in Bangladesh FDI inflow in each year is showing a positive rising trend. In 1980s the average annual inflow of FDI (excluding reinvested earnings) were around US\$ 2 million per annum for Bangladesh.<sup>14</sup> In the 1990s it increases to US\$ 26.33 per annum.<sup>15</sup>

Table -1: The year wise Position Joint venture/100% Foreign Investment Projects registered with the BOI from 1991 to June 1998.

Year	No. Of Units	Proposed Investment (In million Taka)
1991-92	24	1017.500
1992-93	28	2108.667
1993-94	100	32164.645
1994-95	145	29195.939
1995-96	127	62607.847
1996-97	138	45153.865
1997to June 1998	140	153079.238
Total	702	325327.69

Source : Compiled from, GOB, Board of Investment (BOI), 1998 (Unpublished)

From Table-1, in 1991-92 the total sanctioned units were 24, with an amount of registered investment with BOI were 1017.500 million taka. But in the fiscal year 1997-98 total number of sanctioned units are 140 and the amount of proposed registered investment with BOI are 153079.238 million taka. From Table-1, since 1991-92 to 1997-98, the total FDI registered with BOI is 325327.69 million taka. The

14 Sanjaya Lall, "Foreign Direct Investment in South Asia", *Asian Development Review* Vol. II, No. 1(1993).

15 Compiled from Asian Development Bank, *Asian Development outlook 1997 and 1998*. P.239.



amount is not negligible at all. Therefore one can say that Bangladesh is going to treat as a profitable destination for investment to the foreign investors.

### **Sector wise Distribution of FDI :**

The table-2 of the next page is showing a detail picture about the inflow of FDI in each sector from 1991-92 to 1997-98. From table 2: it is clear that in 1991-92 Food and Allied industries and Textile Industries were the two largest FDI exploitor sector respectively. The inflow of FDI in these two sector was 443 and 293 million taka respectively, which were 43.6% and 28.83% of total FDI. In 1992-93 Food and Allied industries were the largest FDI consuming sector. In that period total FDI inflowed to that sector was 1120 million taka which was 52.13% of the total FDI. In 1993-94 Textile Industries and the Chemical Industries were the two largest FDI recipient sector. The percentage of FDI flowed in these two sector were 44.80% and 46.27% out of total FDI respectively. In 1994-95 Textile Industries and Engineering Industries were the two larger recipient sector. These two sector had received 23.17% and 24.38% of total FDI respectively. In the fiscal year 1995-96, the Chemical Industries were the largest FDI recipient sector. It received 37.02% of total FDI in that fiscal year. But in the fiscal year 1996-97, service sector was the individual largest sector in terms of receiving FDI. it received 50.34% of total FDI in that period and still this sector is the dominant sector in receiving FDI. In the fiscal year 1997-98 the service sector was the largest recipient sector in terms of receiving FDI, it exploited 72.22% of total FDI flowed in the country the amount of which was 110546.511 million taka. Data provided by BOI showed that, the largest recipient sector in terms of FDI is the Service sector, Textile industries and Chemical Industries.

**Table-2 :** The group wise particulars of FDI projects registered with the BOI form 1991 to 1998 (June) (in million taka). The value in the Parenthesis shows the Percentage

Name of the Group	No. of Units	Sector wise flow of FDI and the percentage of total FDI from 1991-92 to 1997-98 (in million taka)							Total Proposed Investment	% of total FDI
		1991/92	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98		
Agro-Based Industries	44	26 (2.56)	0	670 (2.08)	1638 (5.61)	1910 (3.05)	662 (1.46)	385.456 (0.25)	5291.456	1.64
Food & Allied Industries	76	443 (43.6)	1120 (53.13)	137 (0.43)	534 (1.83)	1357 (2.17)	2312 (5.12)	16804.054 (10.98)	22707.054	6.98
Textile Industries	181	293 (28.83)	223 (10.58)	14411 (44.80)	6766 (23.17)	3979 (6.35)	6798 (15.05)	4498.816 (2.94)	36968.816	11.36
Printing and Publishing	16	2 (0.19)	118 (5.60)	44 (0.13)	214 (0.73)	41 (0.06)	117 (0.26)	0	536	0.17
Tannery and Lather Industries	33	125 (12.3)	0	194 (0.60)	901 (3.80)	669 (1.06)	169 (0.37)	1023.088 (0.67)	3081.088	0.95
Chemical Industries	81	5 (0.49)	37 (1.75)	14882 (46.27)	5069 (17.36)	23182 (37.02)	3451 (7.64)	2611.916 (1.71)	49237.916	15.13

Source : GOB, Board of Investment 1998 (unpublished)

**Table-2 (2) :** The group wise particulars of FDI projects registered with the BOI form 1991 to 1998 (June) (in million taka). The value in the Parenthesis shows the Percentage

Name of the Group	No. of Units	Sector wise flow of FDI and the percentage of total FDI from 1991-92 to 1997-98 (in million taka)							Total Proposed Investment	% of titak FDI
		1991/92	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98		
Glass Ceramics and Other non metallic Mineral Products	26	0	0	316 (0.98)	4805 (16.45)	1942 (3.10)	4731 (10.48)	4820.369 (3.14)	16614.369	5.11
Engineering Industries	117	47 (4.63)	290 (13.76)	964 (2.99)	7120 (24.36)	6695 (10.69)	3830 (8.48)	515.048 (0.34)	19461.048	5.98
Service Industries	88	0	301 (14.28)	363 (1.12)	1986 (6.80)	2586 (4.13)	22730 (50.34)	110546.511 (72.22)	138512.51	42.57
Misc./NEC	40	75 (7.38)	19 (0.90)	184 (0.57)	163 (0.55)	20247 (32.33)	354 (0.78)	11873.980 (7.76)	32915.98	10.11
Total	702	1016	2108	32165	29196	62608	45154	153079.238	325326.24	100

Source : Compiled from GOB Board of Investment, (BOI) 1998 (Unpublished).





**Table-3 (1) : The Major Investor Countries and Proposed Investment Registered with BOI from 1991/92 to 1997/98 (In million Taka)**

Country	1991/92	1992/93	1993/94	1994/95	1995/96	1996/97	Sub-total	1997/98	Total
USA		59.260 (2.82)	95.006 (0.295)	508.93 (1.74)	2982.796 (4.76)	324.250 (0.72)	3970.242	66859.262 (43.68)	70829.504 (21.77)
Malaysia			10802.191 (33.58)	5583.3 (19.12)	22137.634 (35.36)	1870.465 (4.14)	40393.59	13969 (9.13)	54362.59 (16.71)
Lebanon								3910.00 (11.99)	39010.00 (11.99)
Japan	37.692 (3.71)	83.708 (3.96)	1985.03 (6.17)	3362.75 (11.52)	25897.79 (41.37)	456.538 (1.01)	31823.508	2840.206 (1.86)	34663.714 (10.65)
Hongkong	96.121 (9.44)	18.962 (0.9)	36.944 (0.12)	4413.987 (15.12)	625.335 (1.0)	20823.386 (46.12)	26014.735	7592.287 (4.96)	33607.022 (10.33)

Source : Compiled from GOB Board of Investment, (BOI) 1998 (Unpublished).

**Table-3: (2)**

Country	1991/92	1992/93	1993/94	1994/95	1995/96	1996/97	Sub-total	1997/98	Total
KSA	—	—	11388.4 (25.41)	72.0 (0.24)	—	—	11460.4	26.0 (0.01)	11486.4 (3.53)
UK	115.109 (11.32)	72.366 (3.43)	2892.732 (9.0)	2057.834 (7.05)	2968.087 (4.74)	3398.07 (7.53)	11504.187	1557.59 (1.02)	13061.777 (4.01)
S. Korea	14.993 (1.48)	257.833 (12.23)	789.034 (2.45)	1432.764 (4.91)	1257.233 (2.01)	3695.217 (8.18)	7447.074	4354.257 (2.84)	11801.331 (3.62)
Singapore	90.040 (8.84)	814.67 (38.64)	38.0 (0.11)	2137.18 (7.32)	27.300 (0.04)	5677.911 (12.57)	8785.101	1603.27 (1.05)	10388.371 (3.19)
Others	663.545 (65.21)	801.868 (38.02)	4137.308 (12.86)	9627.194 (32.98)	6711.683 (10.72)	8908.028 (19.73)	30929.174	15267.358 (9.97)	46196.532 (14.2)
Total	1017.5 (100)	2108.667 (100)	32164.645 (100)	29195.939 (100)	62607.847 (100)	45153.865 (100)		153079.238 (100)	325327.69 (100)

Source : Compiled from, Board of Investment (BOI), 1998 (Unpublished).



### **Problems in relation to FDI in Bangladesh**

Though a positive rising trend is showing in terms of FDI (form table-I), Bangladesh lags far behind as compared to most other Asian countries in attracting FDI. The data published by Asian Development Bank Show that, Sri Lanka received 7% of total FDI (The amount of which is US\$ 195 million) in the SAARC region. In spite of LTTE insurgency in the North West, Sri Lanka is still an attractive country for foreign investment. While in Bangladesh, the amount of FDI inflowed in 1995 was only 5% (US\$125 million) of total FDI in the SAARC region. It is depicted that, India is the largest recipient of FDI among the SAARC countries. In 1995 India received 65% of total FDI inflowed in this region the amount of which was 1750 million US\$. Pakistan is the second largest FDI recipient country. In 1995 actual inflow of FDI in Pakistan was 23% of total FDI in the SAARC region (the amount of which is 639 million US\$).<sup>15</sup>

Actually in terms of registration with BOI, it shows that the inflow of FDI is increasing day by day. But this satisfaction is based only on the information in terms of project investments in the registration/approved only. BOI undertook a survey during July-Nov. 1994, with a view to estimate the realization rate, under the proposed enterprises, who registered between 1992 and 1994. The survey reports that, between 62 to 65 percent of foreign private enterprises are being implemented, out of which 35 to 40 percent have gone into production.<sup>16</sup> A recent survey of the Board of investment says, during July 1996 to June-1998, the BOI registered a

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15 Asian Development Bank, *Asian Development Outlook 1997 and 1998* (Manila : ADB, 1998) P. 239

16 GOB, *Fifth Five year plan* (Draft) 12997-2002pvi-10)

total 278 foreign projects worth 4.4 billion dollar. The BOI survey mentioned that, 120 foreign projects involving an amount of 2.9 billion dollar have not yet made any physical progress<sup>17</sup>. Sadrel Reza, in his book mentioned that, before liberation (up to 1971), total sanctioned units with FDI were 23, all of those had gone into production. From 1982/83 to 1990/91 total sanctioned units were 101. Out of those, only 40 units had gone into production. In the fiscal year, 1991/92 total registered units were-24, out of those 18 units had gone into production<sup>18</sup>.

Another problem with FDI is that, all foreign investments does not represent net transfer of resources from abroad to Bangladesh, maximum investments are just reinvested earnings. Compared to freshly imported capital, reinvested earnings originate as savings from investments previously made. In Bangladesh the share of reinvested earnings in FDI "had risen above 90 percent in 1988 and 1990, it never went below one third of the total during the entire period under consideration."<sup>19</sup>

Therefore it is now a common feature with Bangladesh that, many of the approved investment proposals involving FDI are not actually implemented. There will be some natural 'drop out's which can be considered as normal for a certain number of proposals. But the fact is that, there has only been about 62-65% realization rate and new investment sanctioned is not descent at all. This rate is much below the experience of other Asian Countries. For instance, about

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17 *The Bangladesh Observer* (October 28, 1988)

18 Sadrel Reza, *Transnational Corporations in Bangladesh. Still at bay?* (Dhaka : University Press Limited, 1995). PP.21-22.

19 *Ibid*, p.27.

80% of the projects approved in the period from 1971 to 1983 in Malaysia, started production or were in the advanced stages of implementation. So in Bangladesh the experience is not sweet. Therefore one could observe a significant discrepancy on the annual amount of FDI among the BOI data table-1 and the data recently published in the Asian Development Outlook 1997 and 1998.

Another problem relating to FDI is that, FDI is not coming enormously to the thrust sector of the economy. For example, Agro-Processing and Computer software sector are the two thrust sector of the country. In view of large international trade volume in the area of software development, data entry and data processing, foreign private investment encouraged and accorded priority. This industry has an enormous potential for generating foreign exchange and employment. But the fact is that, this sector has received only US\$ 4 million of FDI<sup>20</sup>. But to facilitate rapid expansion of this sector, FDI have to encourage this sector. The main thrust of private investment in agriculture is attainment of food self sufficiency, crop diversification and acceleration of investment in the livestock, fisheries and forestry sub-sectors. One of the major efforts in this area is the construction of the "Ganges Barrage". So a healthy inflow of FDI is expected in this sector. But this sector received only 7 million dollars of FDI. So the thrust sectors fails to draw FDIs properly.

There are various things working as barrier in the way of FDI. The major impediments in the way of the sufficient inflow of FDI is, the negative image of the country. Moreover political instability, particularly repeated heartless, redtapism, bureaucratic hurdles and lengthy administrative procedure,

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20 *The Bangladesh Observer* (October 28, 1998).



inadequate infrastructure, particularly energy and telecommunication facilities, rigid and conservative banking system and absence of service-oriented banks, lack of accurate information for taking correct business decision etc. are now workings barrier in the way of sufficient inflow of FDI. Even due to non-fulfillment of commitment by financial institution many foreign investors have to suspend implementation of their projects<sup>21</sup>. The bureaucratic road block, poor reaction by authorities towards quick solution of problems and absence of economic solution hamper the enormous inflow of FDI in the country. A survey reported that, "problems in getting land and service facilities for a project, bureaucracy and port hazards have stalled progress of the proposed foreign investment nearly 3 billion dollar during the last two fiscal year (i. e. 1996/97 and 1997/98).<sup>22</sup>

### Conclusion

In order to face the challenges of the 21st century, the government have to take necessary measures to remove those constraints, e. g., shortage of power, inadequate infrastructures, low level of human resources etc. and have to promote the image of the of the country as a safe and profitable destination of FDI. So far the latest Industrial policy of Bangladesh is considered to be one of the most liberalized policy in South Asia. Despite that, we are not yet able to draw the much-needed foreign direct investment in large volume. In this connection, it is mentionable that, the investment climate of both India and Pakistan are not that congenial than that of our country. Recently the two coun-

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21 Dewan Zakir Hossain, "Investment Climate and trend of Foreign Investment in Bangladesh : A Study of Japanese investors" (Seminar Paper BPATC, 1997).

22 *The Bangladesh observer* (October 28, 1998)

tries have got them engaged in nuclear arms race. As a result, the investment climate of these two countries are largely affected. Foreign investors may look for alternative countries for investment. At this critical juncture, we must avail our self of this opportunity by drawing US and Japanese investment as much as we can. In this regard, parliamentary democracy and political stability of the country are the important elements, which need to be rallied and provided by both party in power and parties in opposition.

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